

Economic and Revenue Outlook

Presented to
Heritage Bank Pricing Committee and
Leadership Team

Steve Lerch
Chief Economist & Executive Director

January 15, 2013
Olympia, Washington



WASHINGTON STATE
ECONOMIC AND REVENUE FORECAST COUNCIL

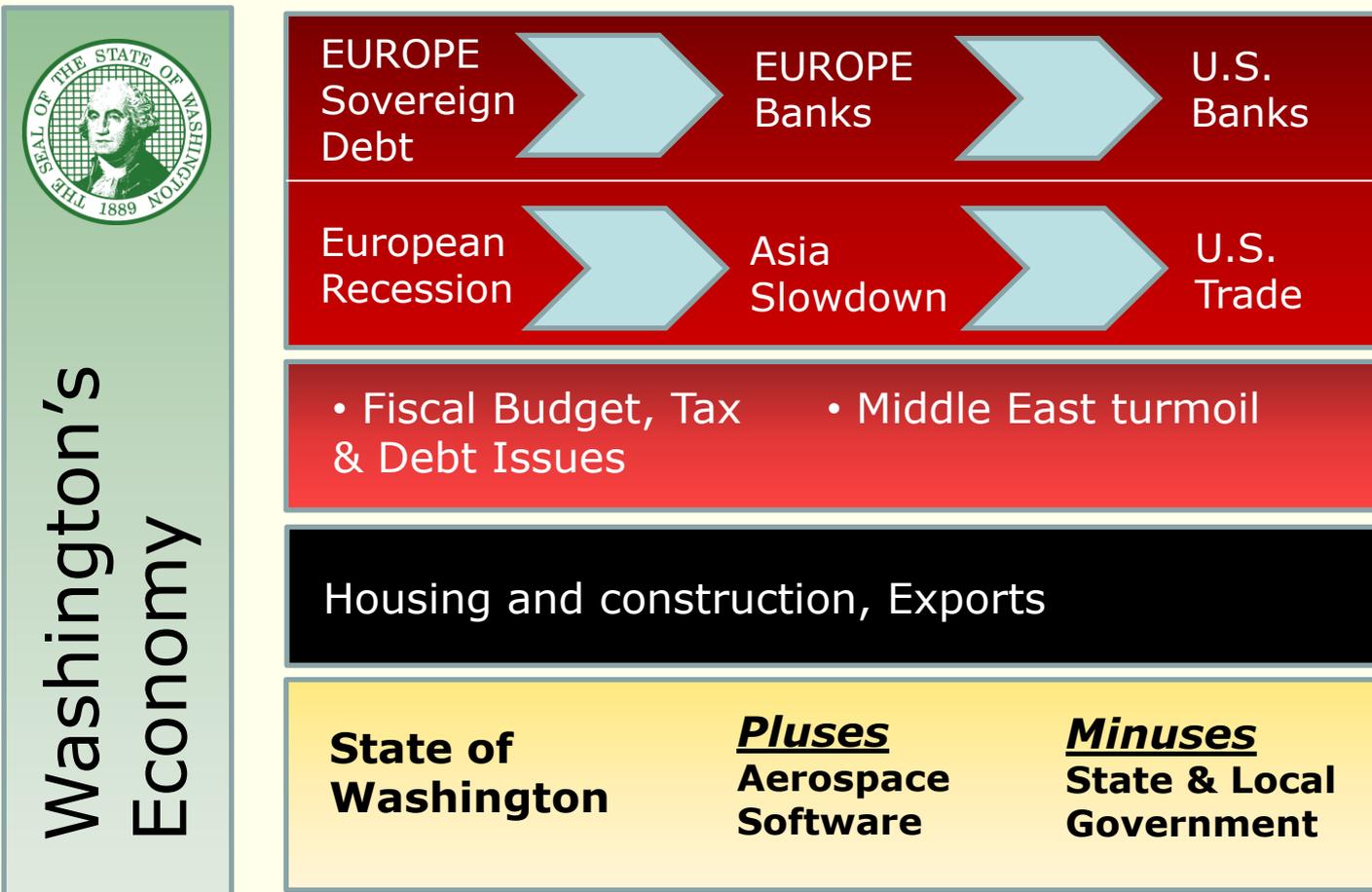


Summary

- The WA and U.S. economic forecasts have been fairly consistent since early 2012 – slow growth and relatively weak labor markets
- As a result, the WA revenue forecast has also been fairly consistent since early 2012
- Given the uncertainty around implementation, no new revenue is associated with I-502 at this time
- Uncertainty in the baseline remains very high, mostly due to on-going concerns about Europe, China, and gridlock on federal budget issues
- The housing sector appears to have stabilized and is now an upside risk to the forecast



The state's risk matrix shows most risks from outside state



Source: ERFC

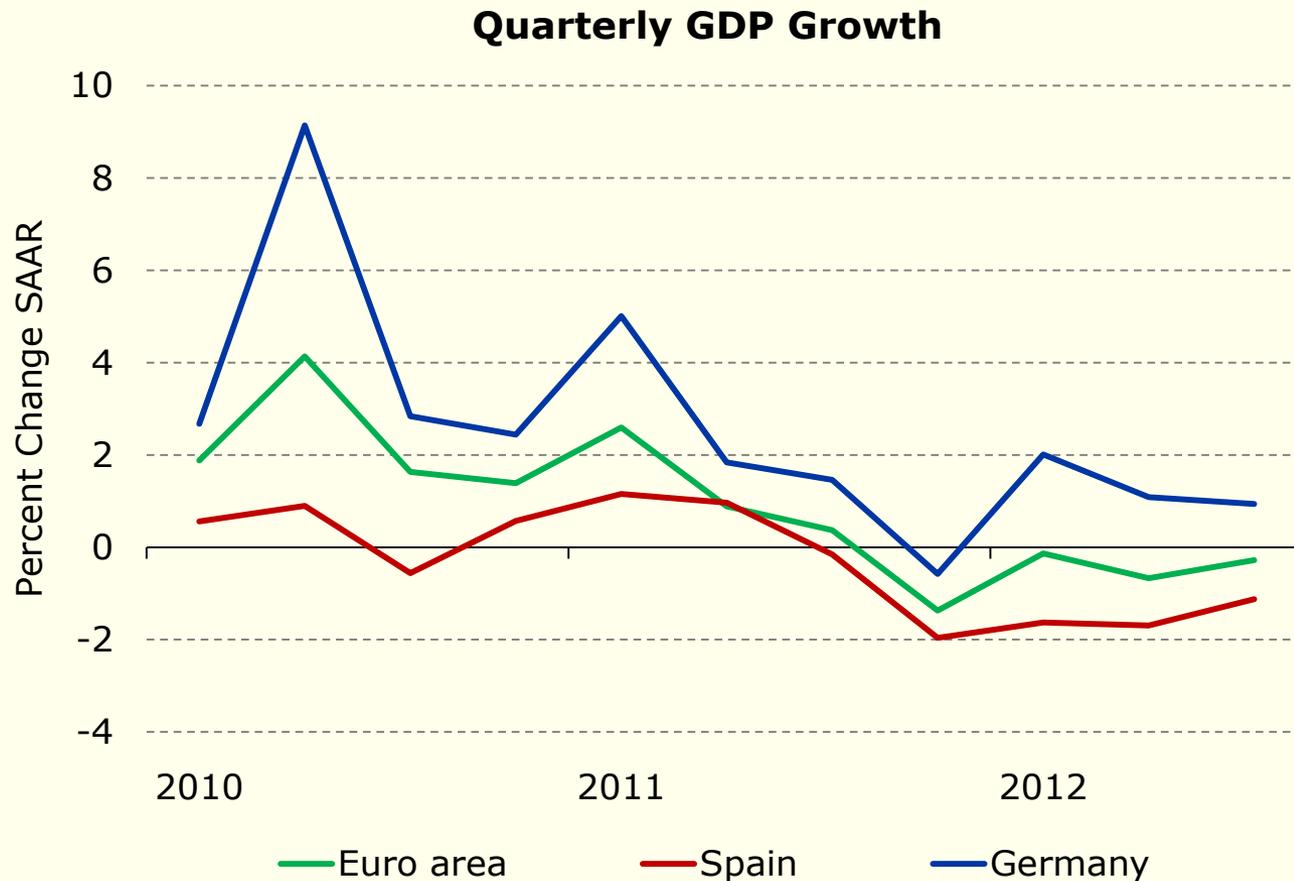


Euro area GDP growth is negative

Eurozone
Forecast:

2013: 0.0%

2014: 0.9%



Source: Eurostat; data through 2012Q3

WASHINGTON STATE ECONOMIC AND REVENUE FORECAST COUNCIL

Economic and
Revenue Outlook
January 15, 2013

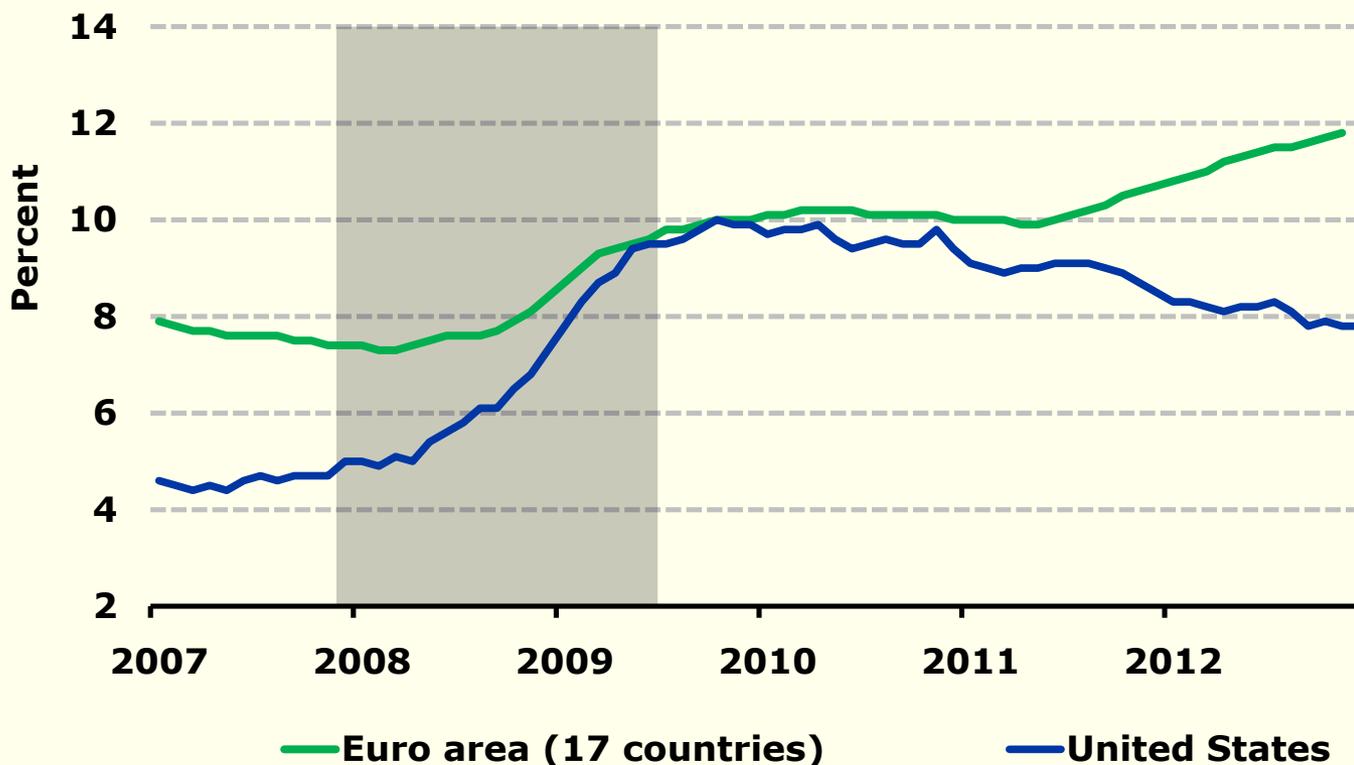


European unemployment is heading in the wrong direction

Unemployment Rate:

Spain: 26.6
Greece: 26.0
(Sept)
Germany: 5.4

Eurozone and U.S. Unemployment

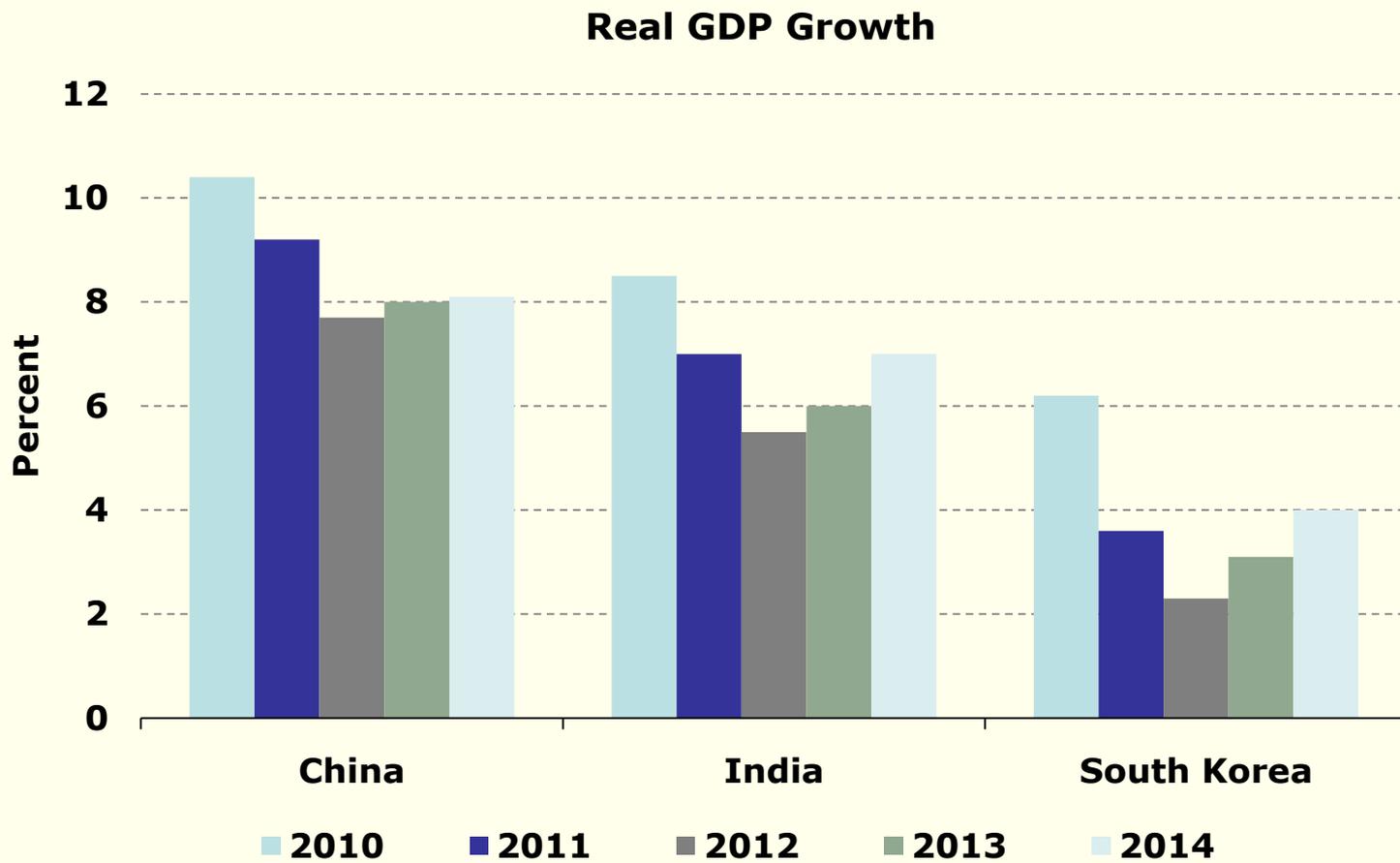


Source: Eurostat; data through December 2012

WASHINGTON STATE ECONOMIC AND REVENUE FORECAST COUNCIL



Asian economic growth has slowed but appears to be improving



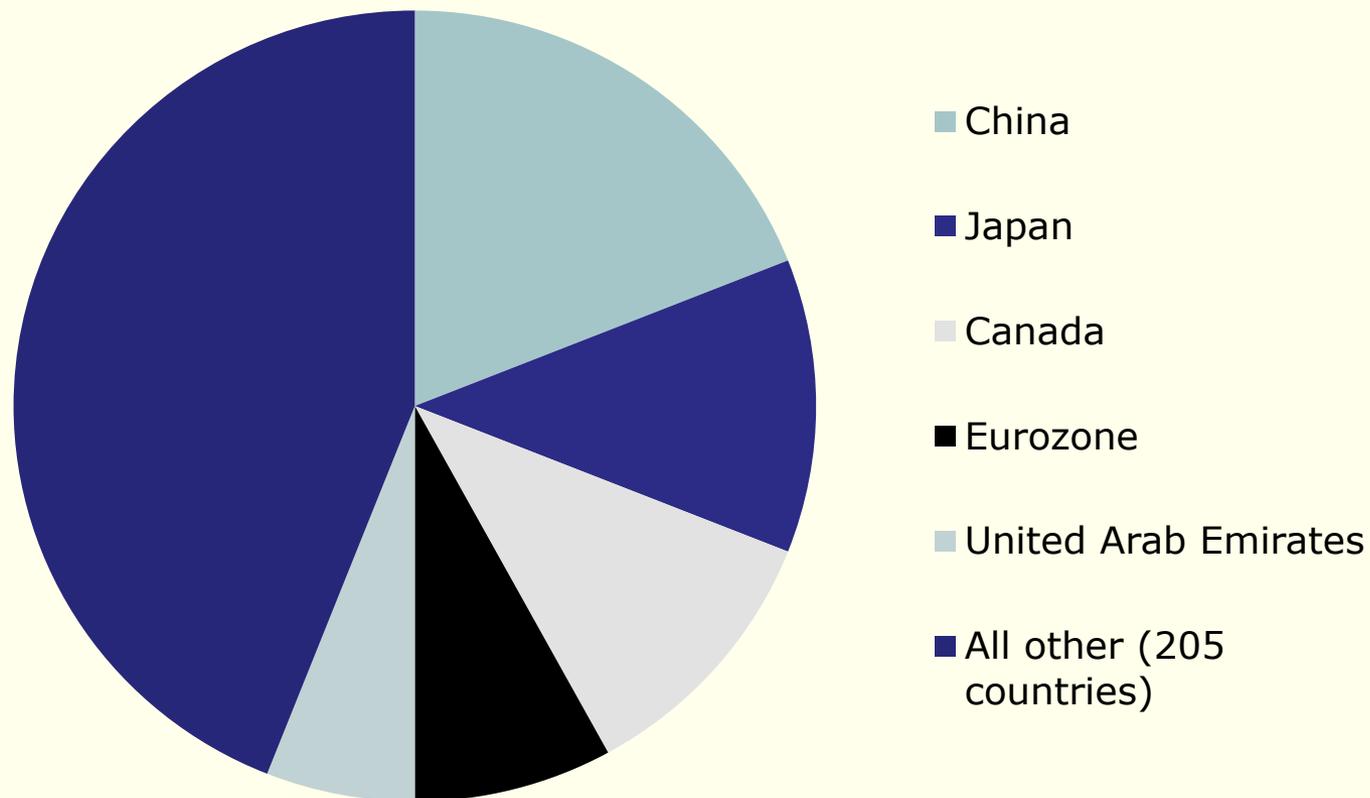
Source: Blue Chip Economic Indicators January 2013, historical data through 2011

WASHINGTON STATE ECONOMIC AND REVENUE FORECAST COUNCIL



China is Washington's Top Export Destination

Exports by destination



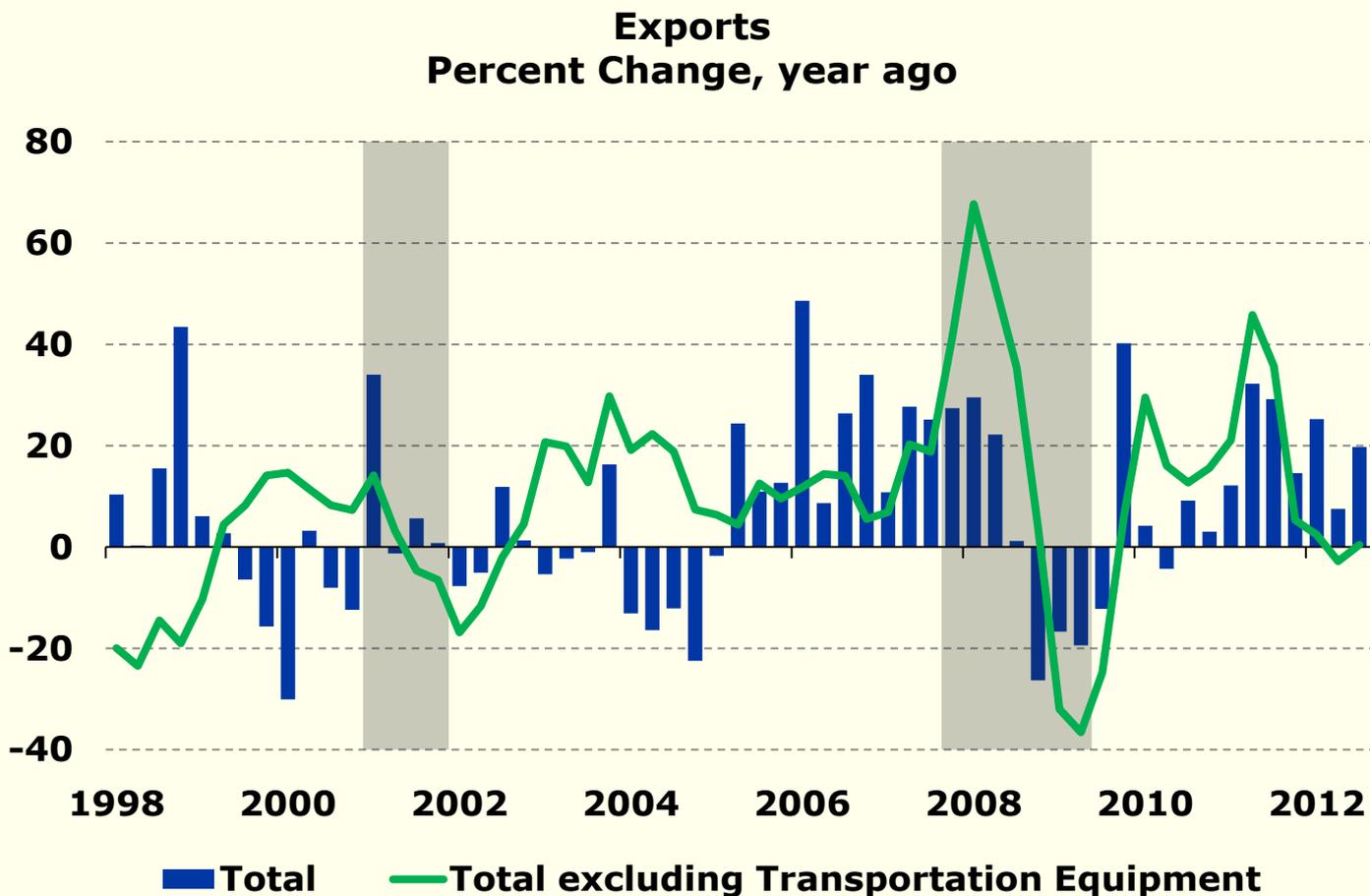
Source: WISER Trade Data; data through 2011



WA export growth has slowed

Trans. Equip. exports are up 43.4% year-over-year in Q3

All other exports are up just 0.4% year-over-year in Q3



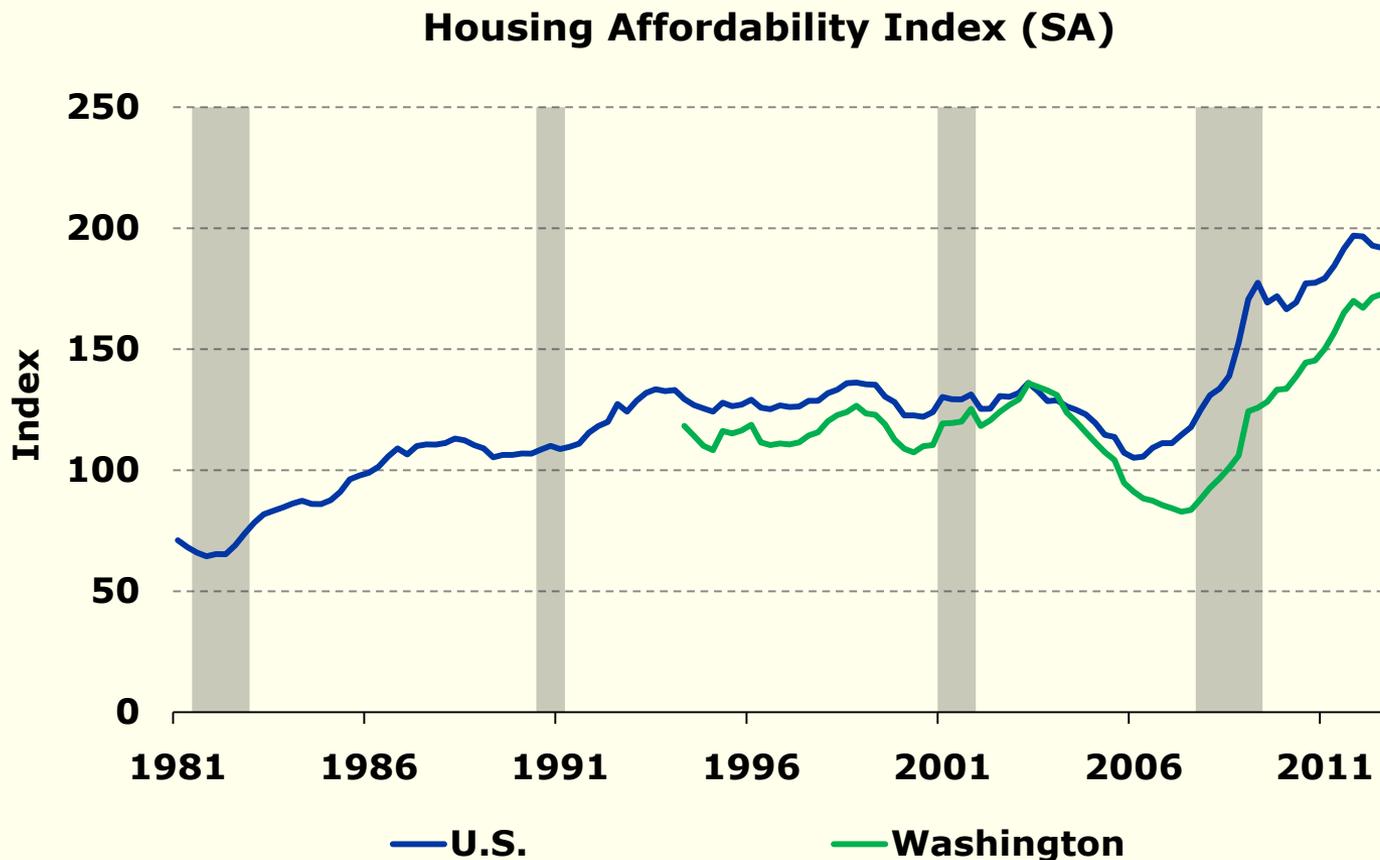
Source: WISER Trade Data; data through 2012 Q3

WASHINGTON STATE ECONOMIC AND REVENUE FORECAST COUNCIL



Home affordability remains in record territory

Affordability is 100 when the median income can just afford the median priced home. Above 100 means the median income can afford more than the median priced home



Source: National Association of Realtors, Global Insight, Washington Center for Real Estate Research; data through 2012 Q3

WASHINGTON STATE ECONOMIC AND REVENUE FORECAST COUNCIL

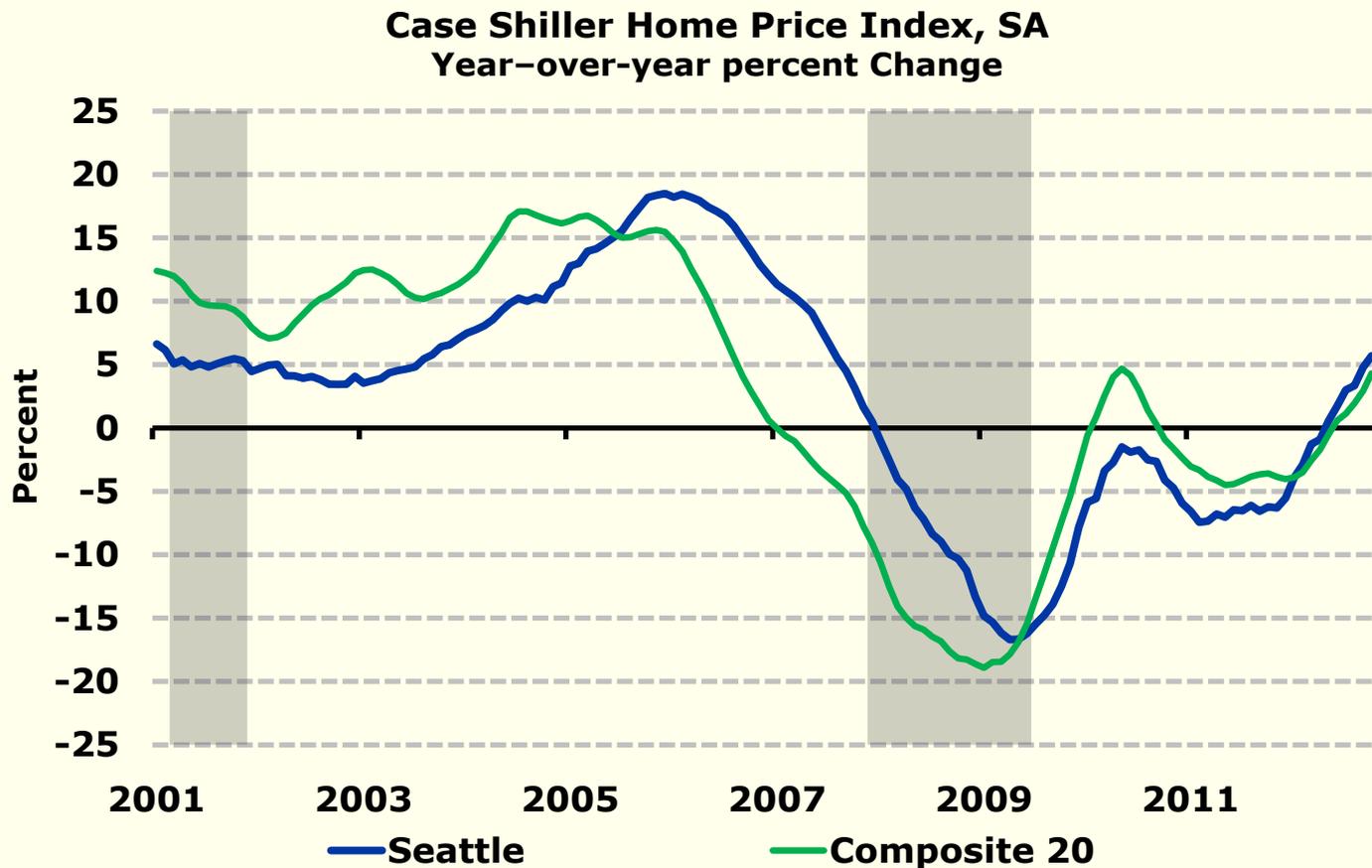


Single-family home prices are beginning to increase

Oct 2012

U.S. is up
4.3%

Seattle is
up 5.7%



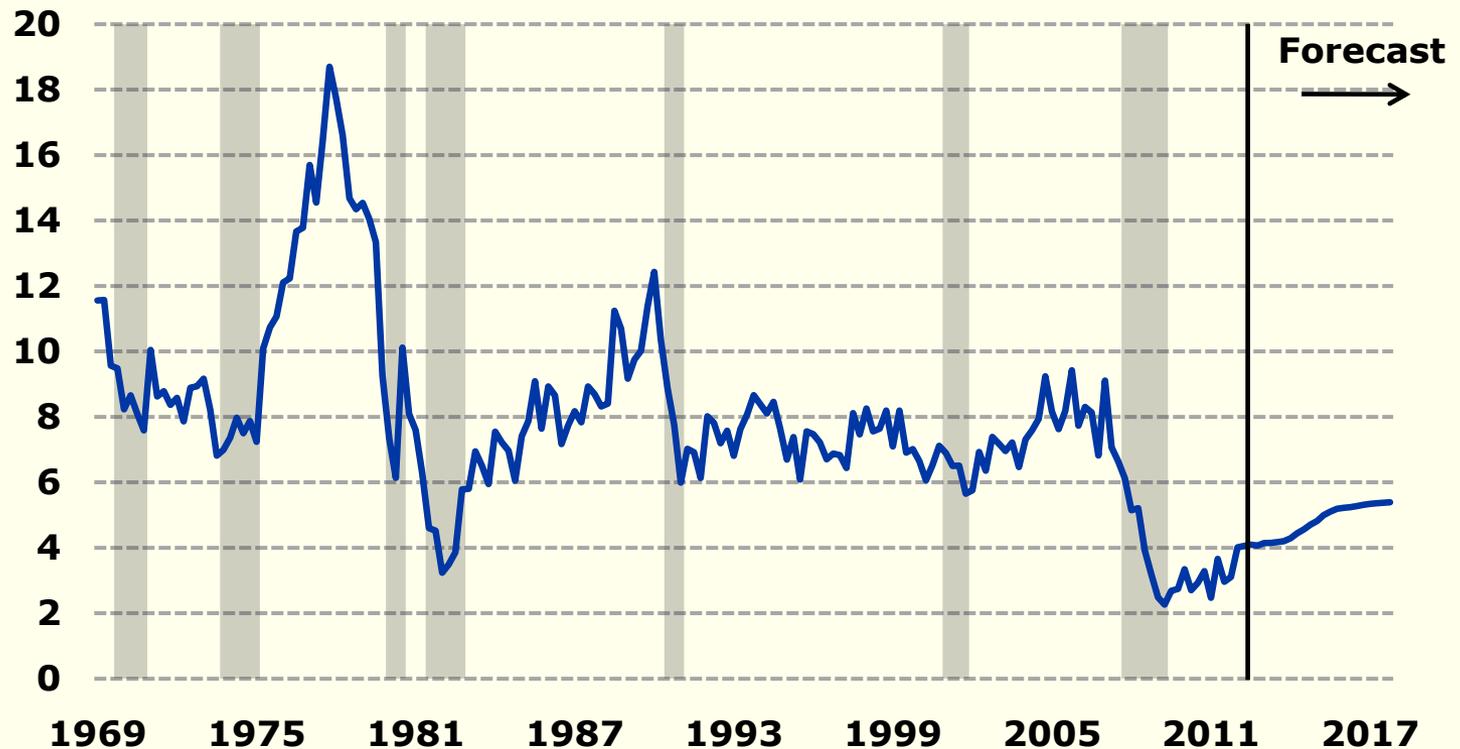
Source: S&P/Case-Shiller; data through October 2012

WASHINGTON STATE ECONOMIC AND REVENUE FORECAST COUNCIL



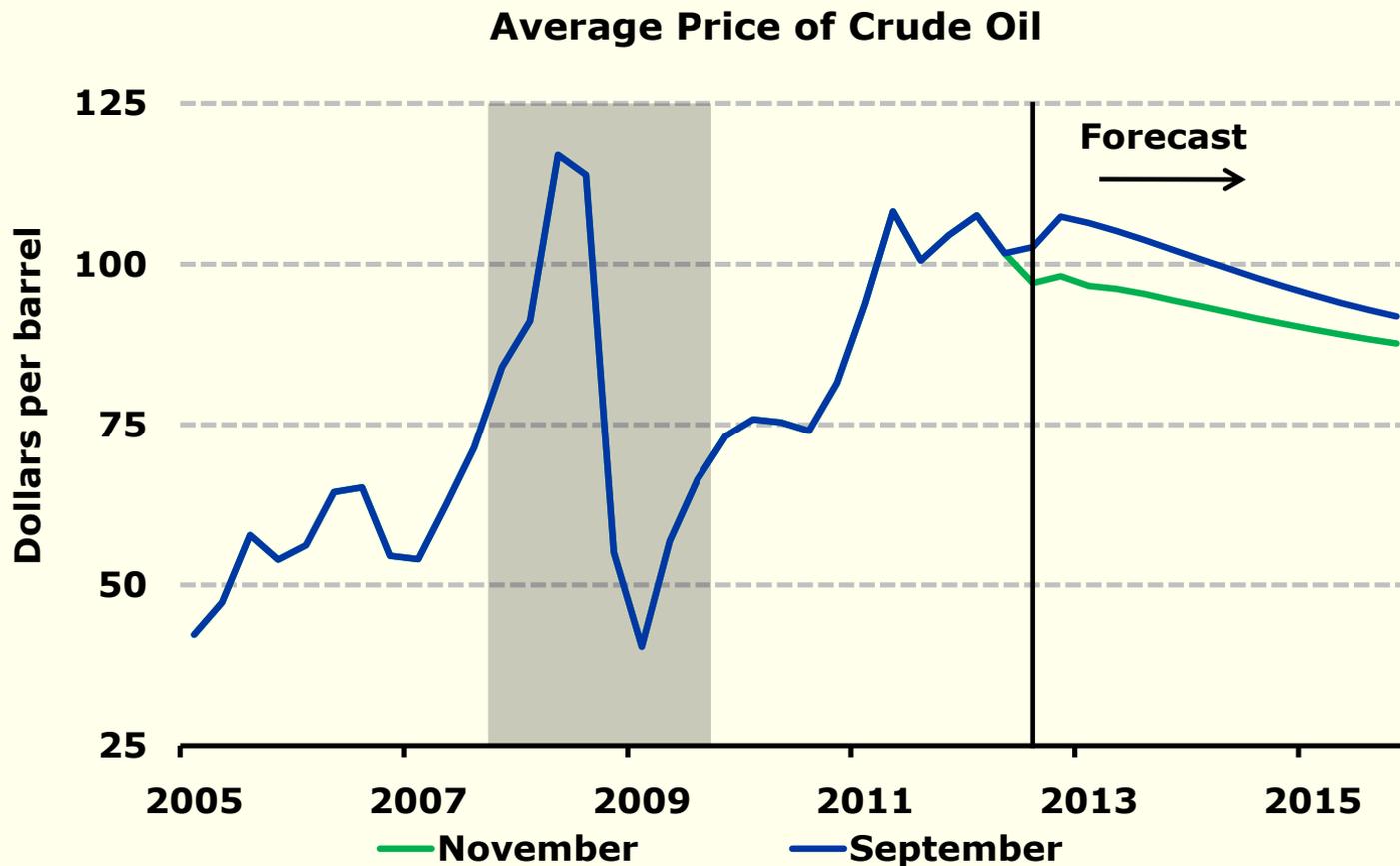
Housing permits relative to population will still be below historic levels in 2017

Washington Housing Permits per 1,000 People



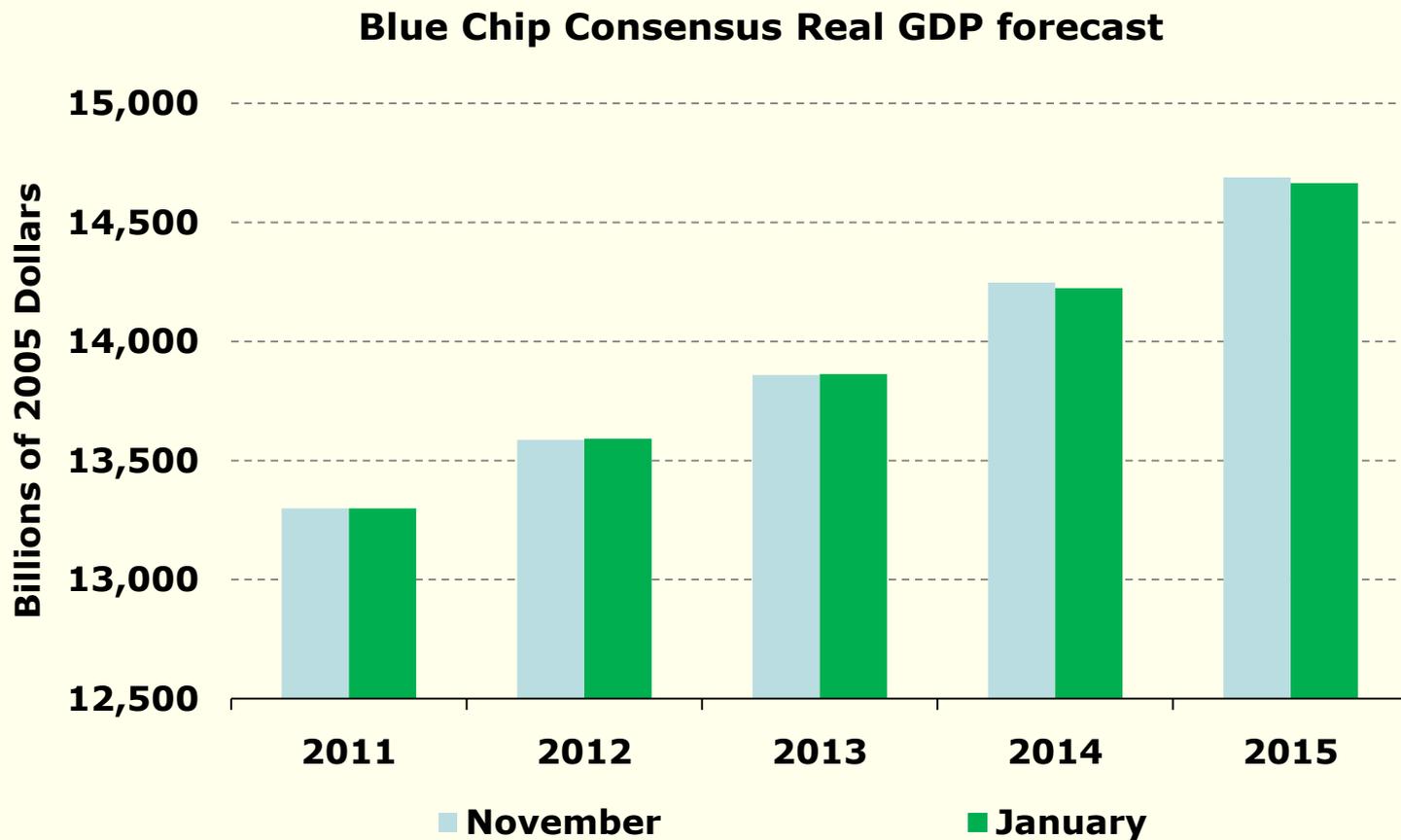


Oil prices are expected to decline





U.S. GDP Forecast Slightly Lower



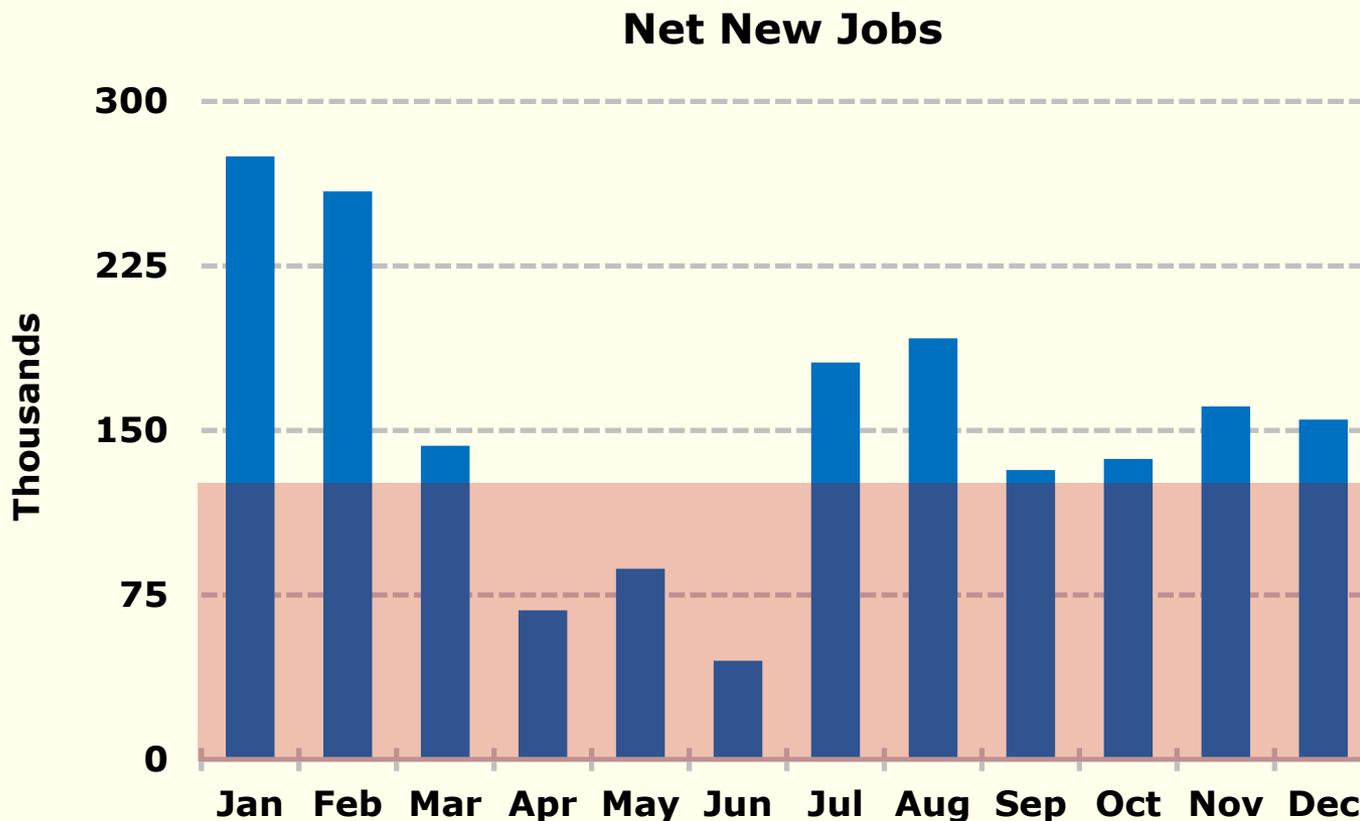
Source: BEA, Blue Chip Economic Indicators January 2013; historical data through 2011

WASHINGTON STATE ECONOMIC AND REVENUE FORECAST COUNCIL



Job growth remains weak

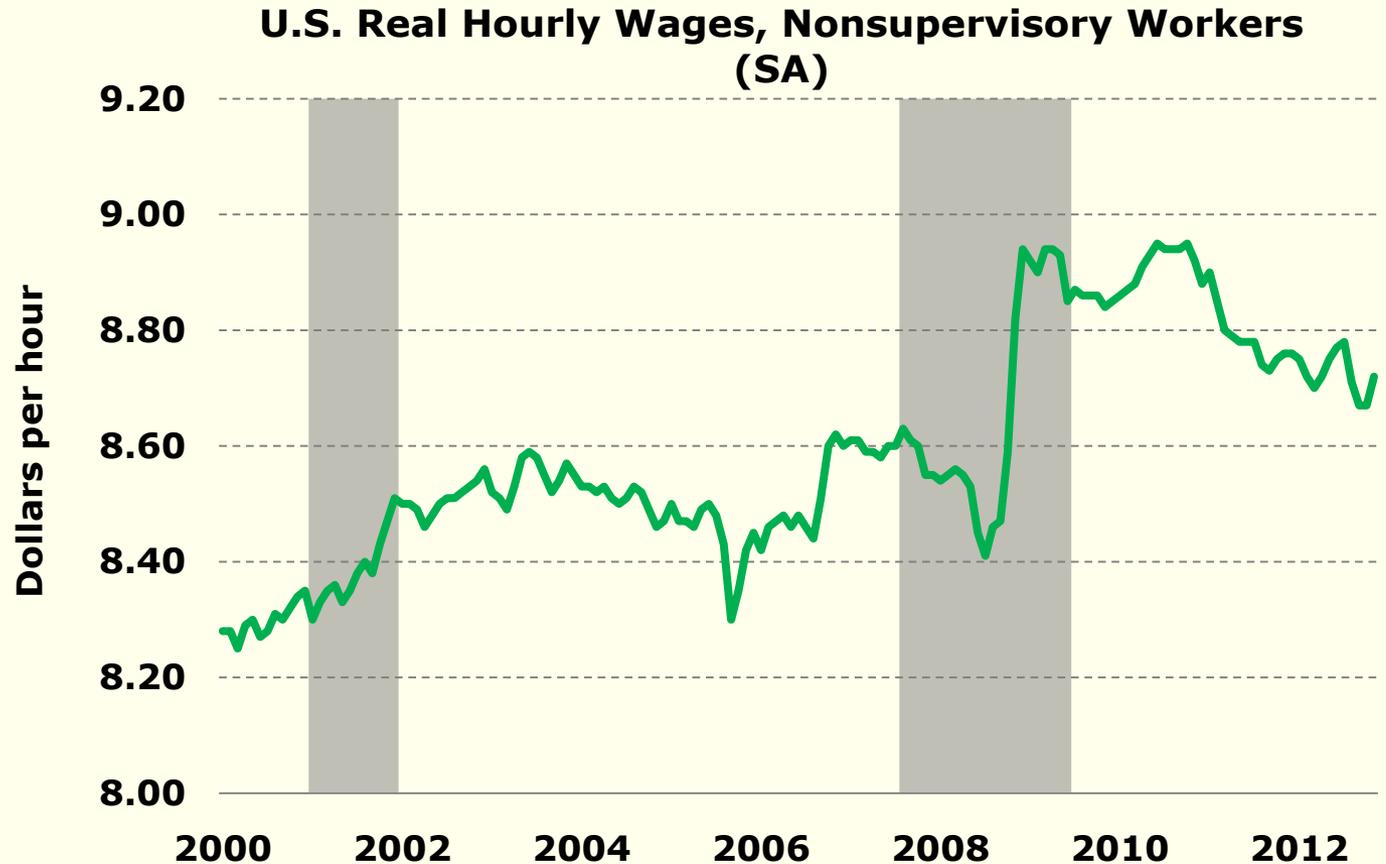
The economy needs to add roughly 125K jobs each month just to keep up with growth in the labor force



Source: Bureau of Labor Statistics, data through December 2012



Real Wages Have Trended Down Since 2011



Source: BLS; data through November 2012

WASHINGTON STATE ECONOMIC AND REVENUE FORECAST COUNCIL

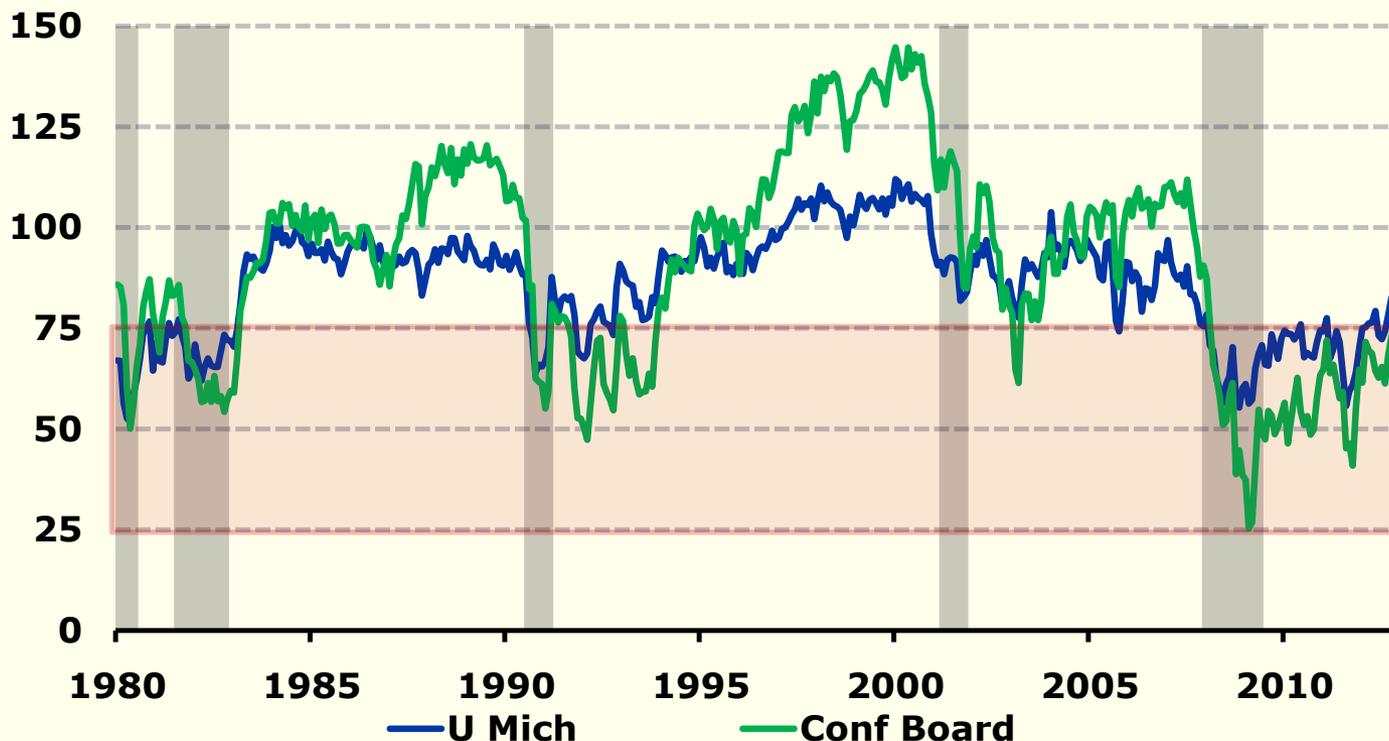


Consumer confidence dipped at the end of the year

Index

Mich: 1966Q1 = 100, SA

Conf Board: 1985 = 100, SA

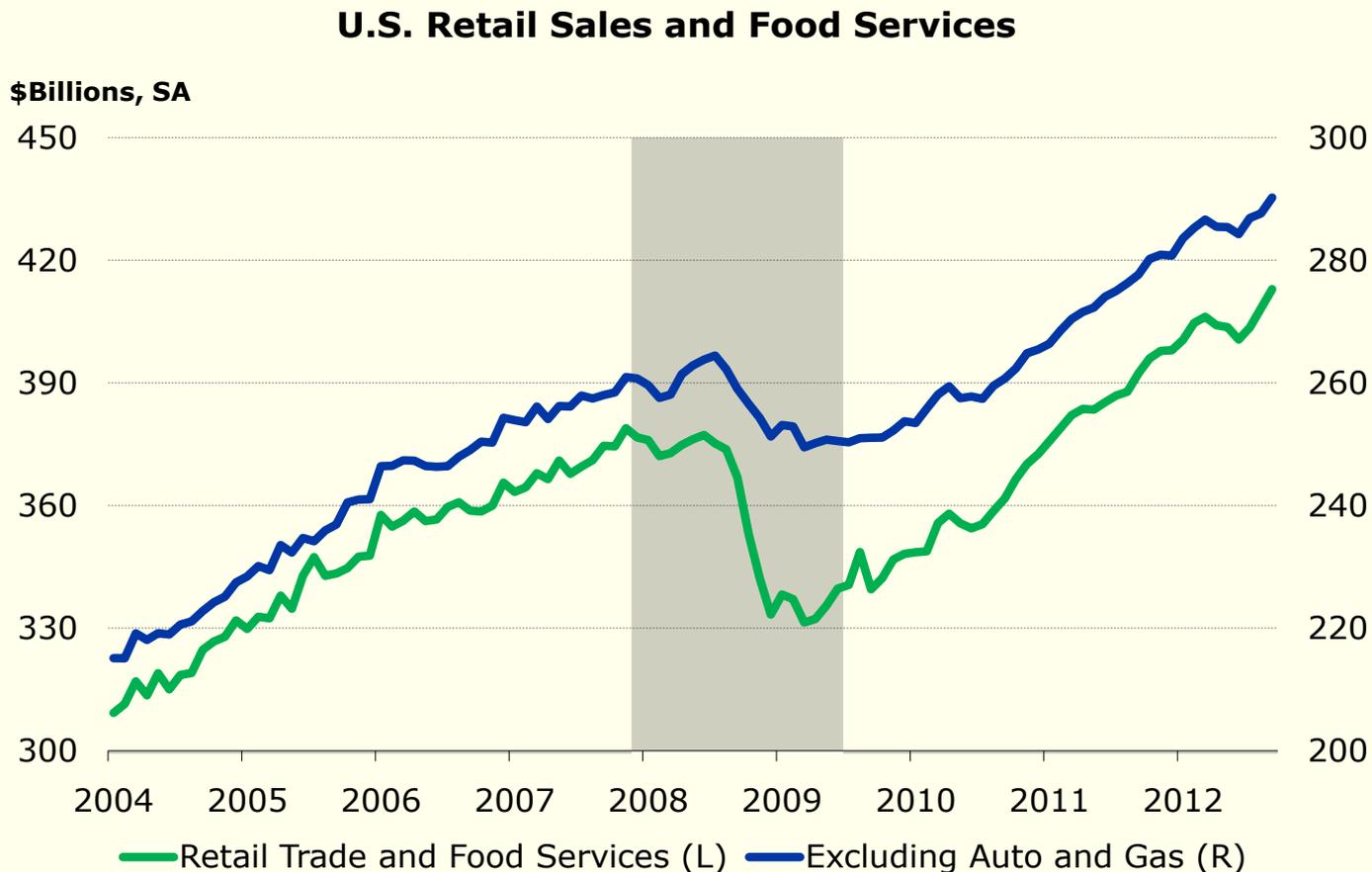




U.S. retail sales on an upswing after April-June pause

Preliminary U.S. retail trade and food services sales were up 5.3% year-over-year in August and 5.2% in September.

Excluding autos and gas, sales were up 4.1% year-over-year in August and 4.5% in September.



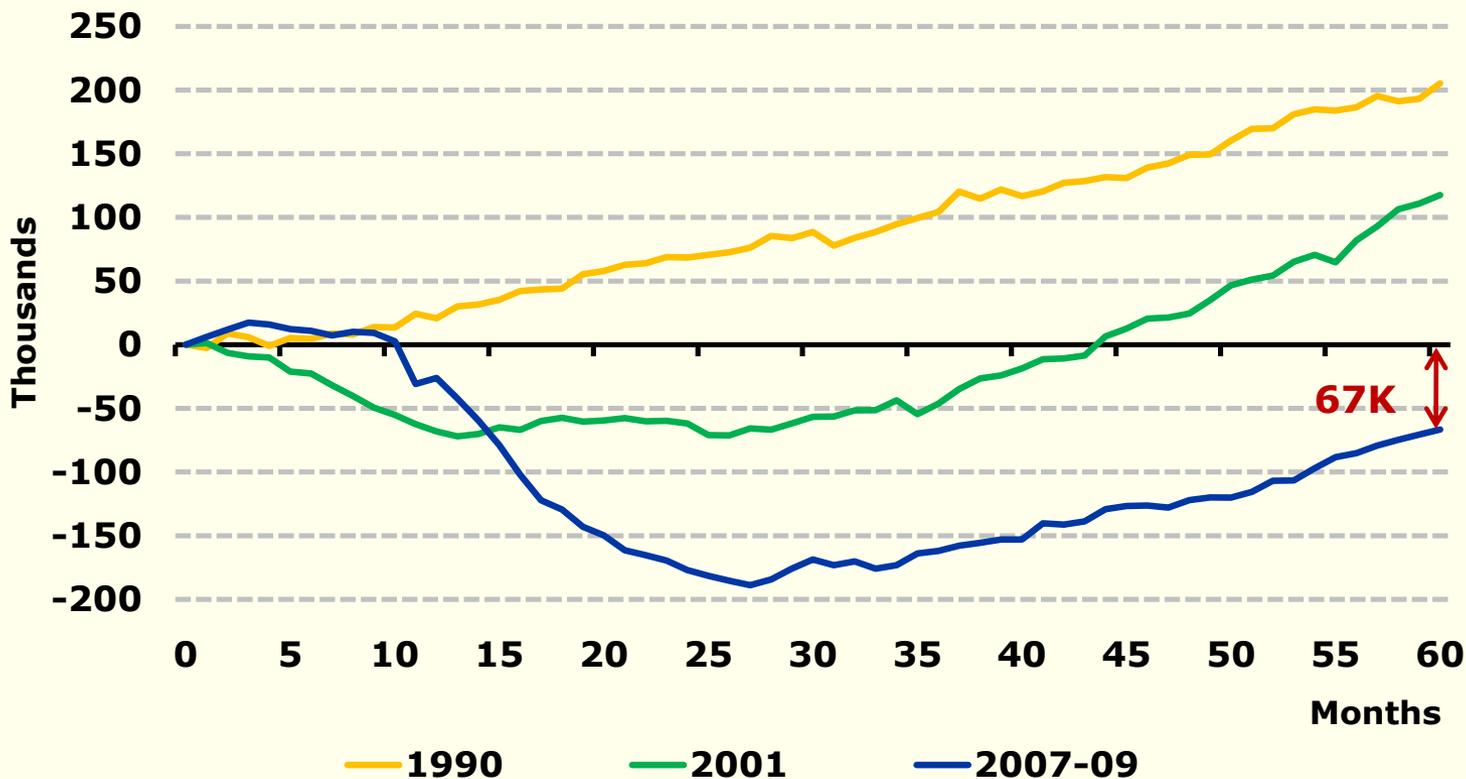
Source: U.S. Department of Commerce, Census Bureau; Data through September 2012 advance

WASHINGTON STATE ECONOMIC AND REVENUE FORECAST COUNCIL



The decline in employment has been severe

Washington Employment after Business Cycle Peak



Source: WA ESD, ERFC; data through November 2012

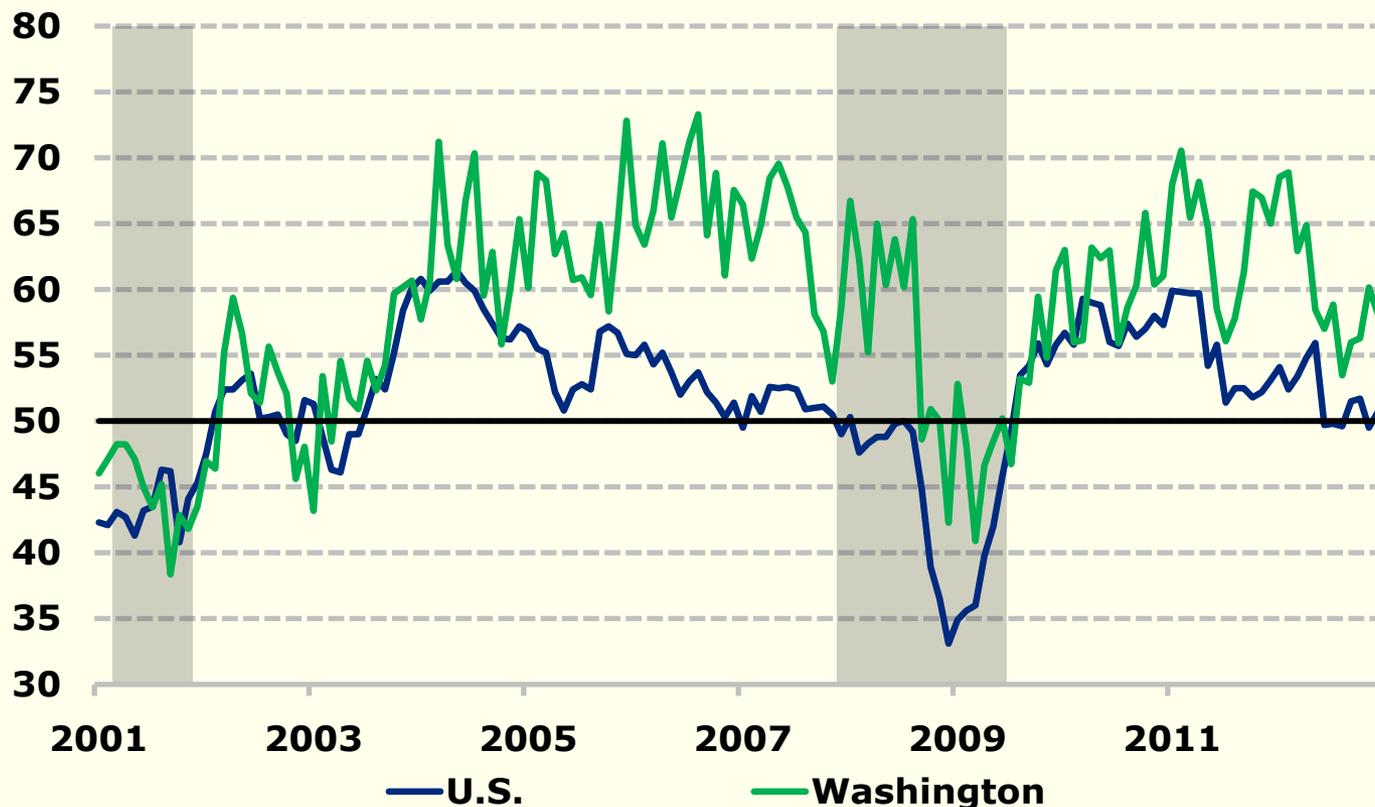
WASHINGTON STATE ECONOMIC AND REVENUE FORECAST COUNCIL



Manufacturing remains weak nationally

An index greater than 50, implies growth

Institute of Supply Management Index



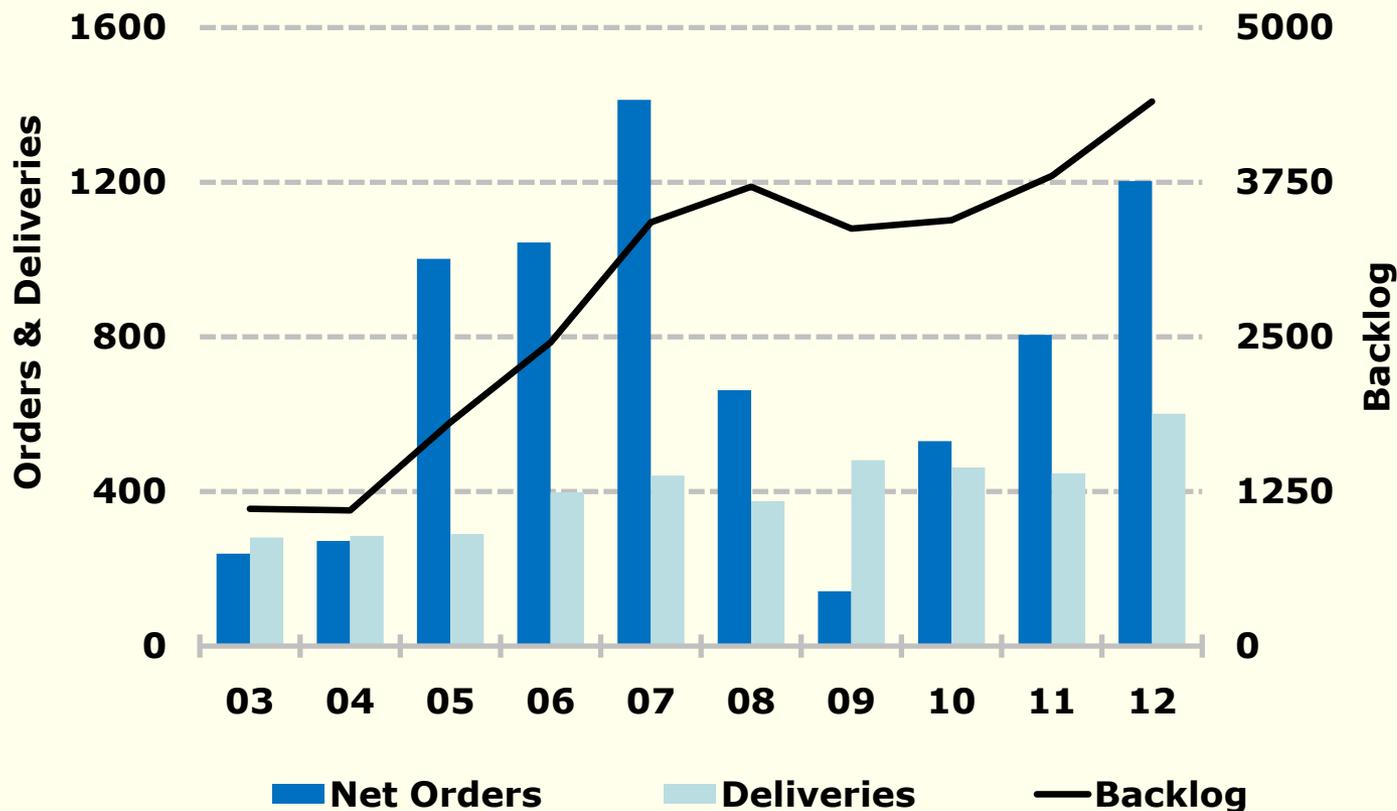
Source: Institute of Supply Management; data through December 2012

WASHINGTON STATE ECONOMIC AND REVENUE FORECAST COUNCIL



Boeing has 7 years of commercial orders on its books

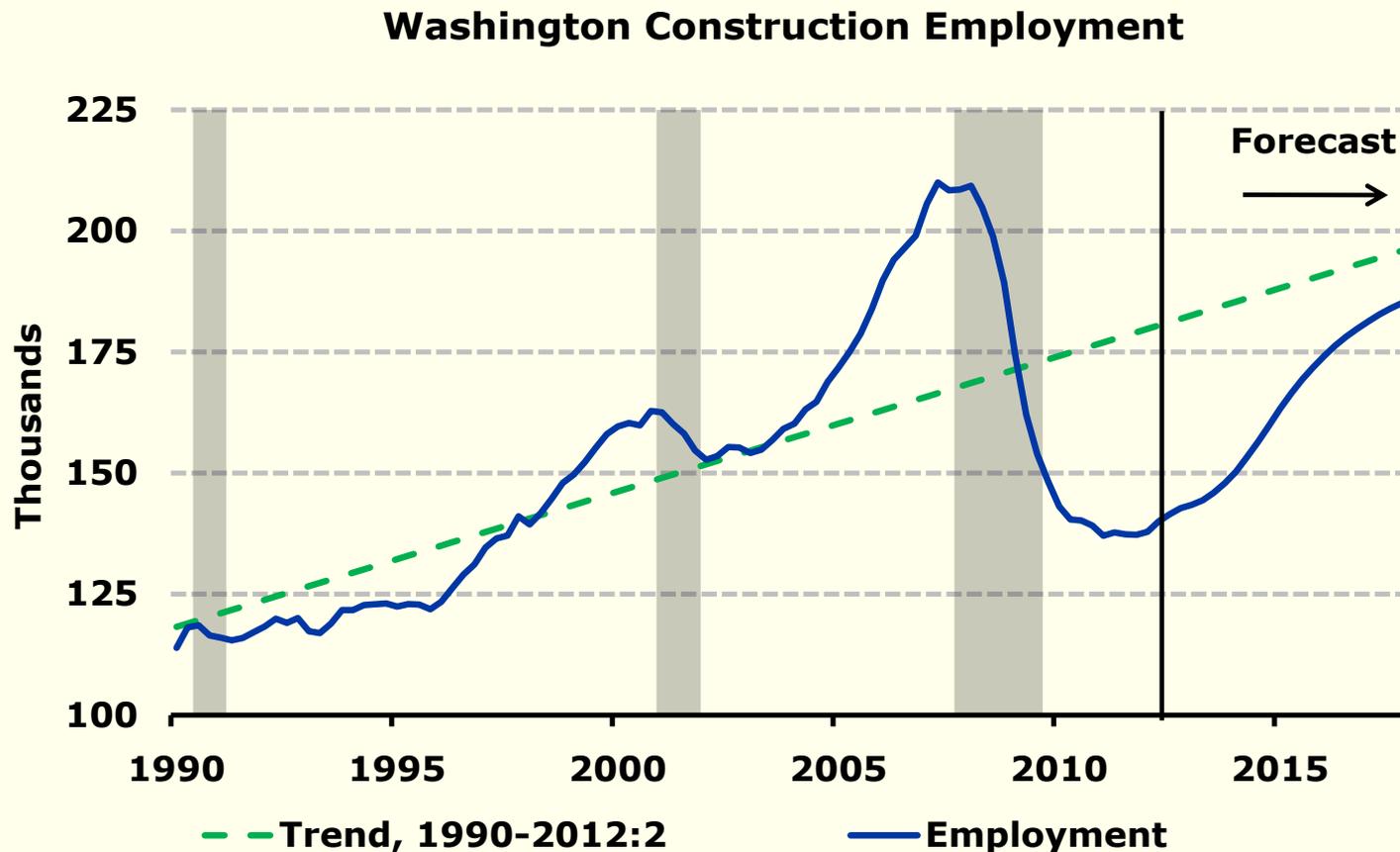
Excludes the military's new refueling tanker



Source: Boeing, data through December 2012



Washington construction employment will remain below trend throughout the forecast



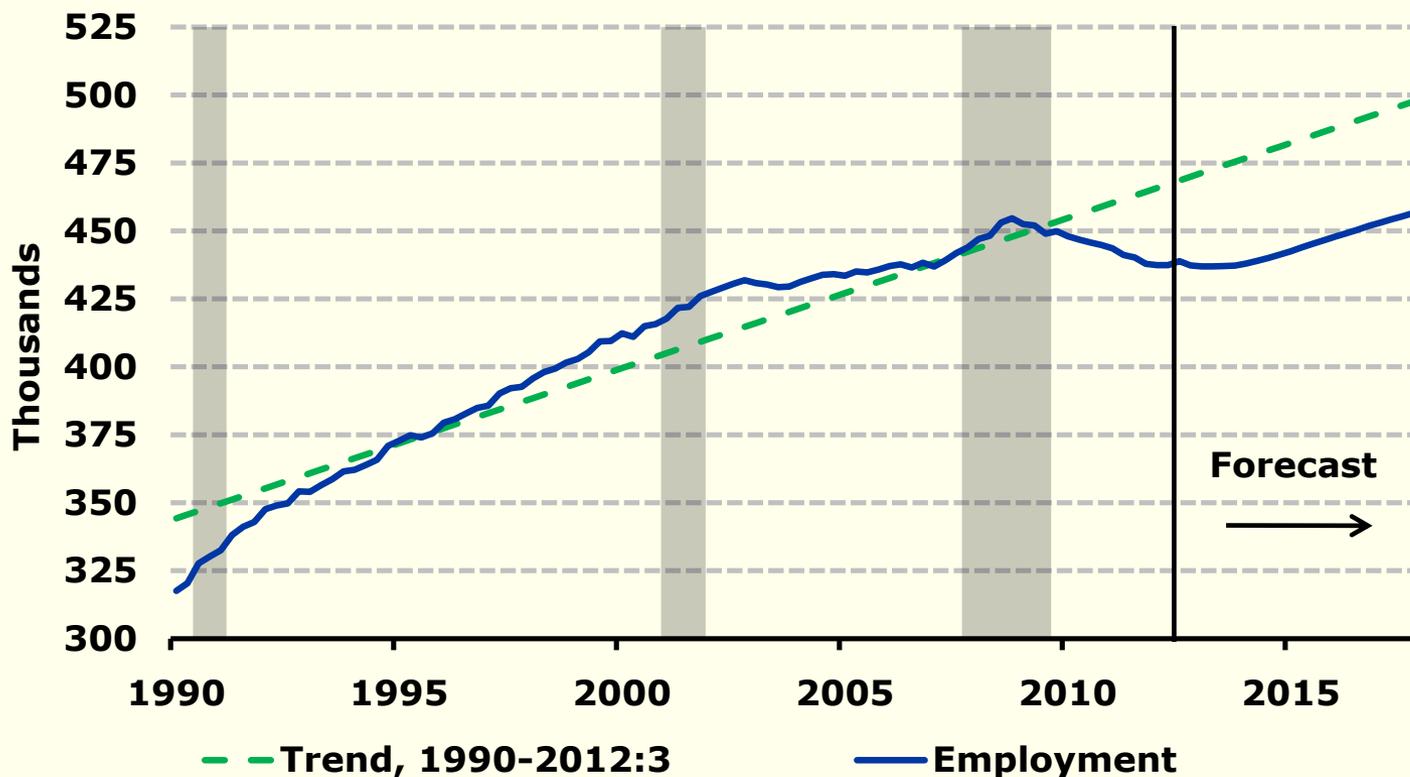
Source: ERFC November 2012 Preliminary forecast; historical data through 2012Q3

WASHINGTON STATE ECONOMIC AND REVENUE FORECAST COUNCIL



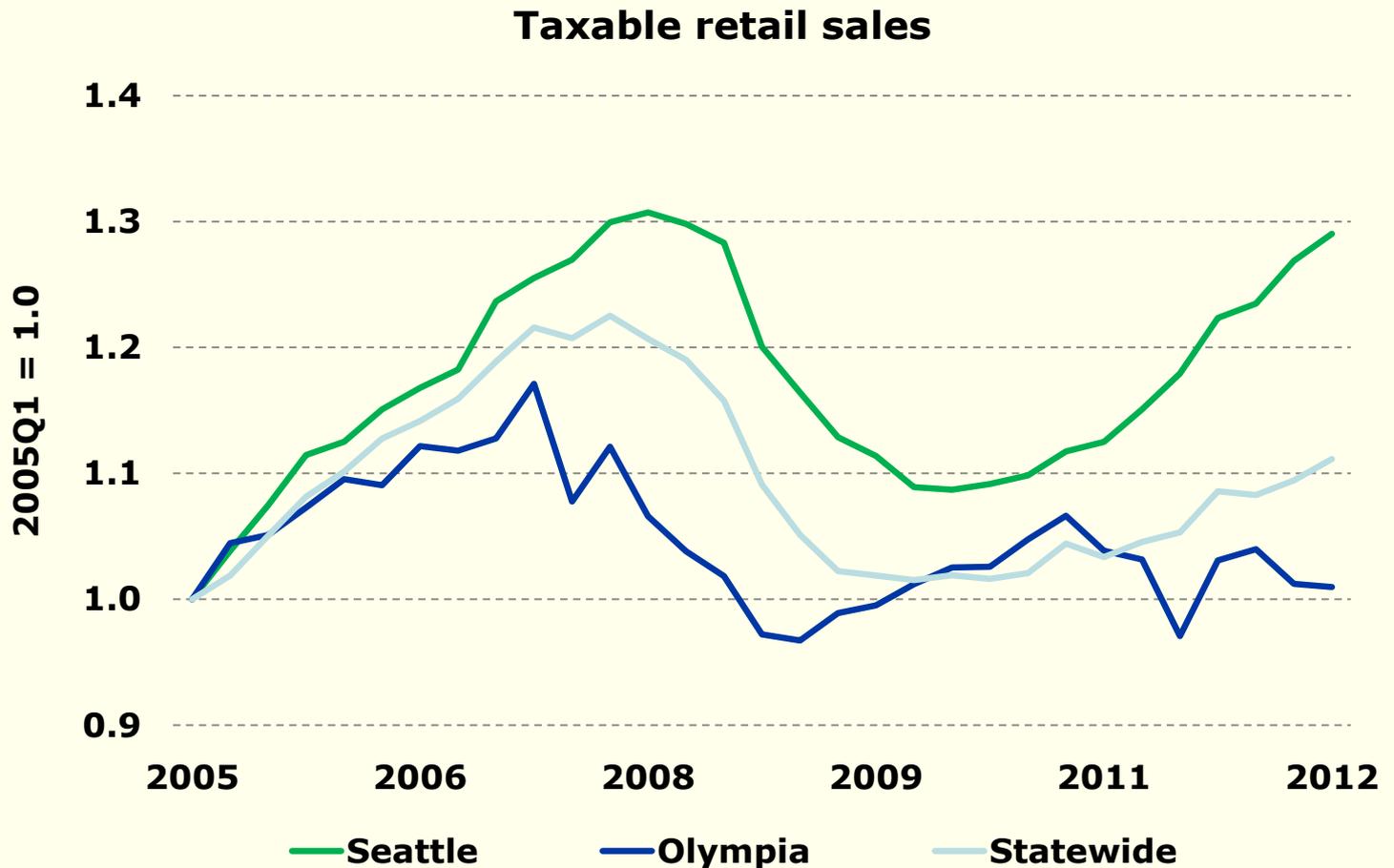
State and local government employment will remain weak

Washington State and Local Government Employment





Recovery in WA retail sales has been uneven



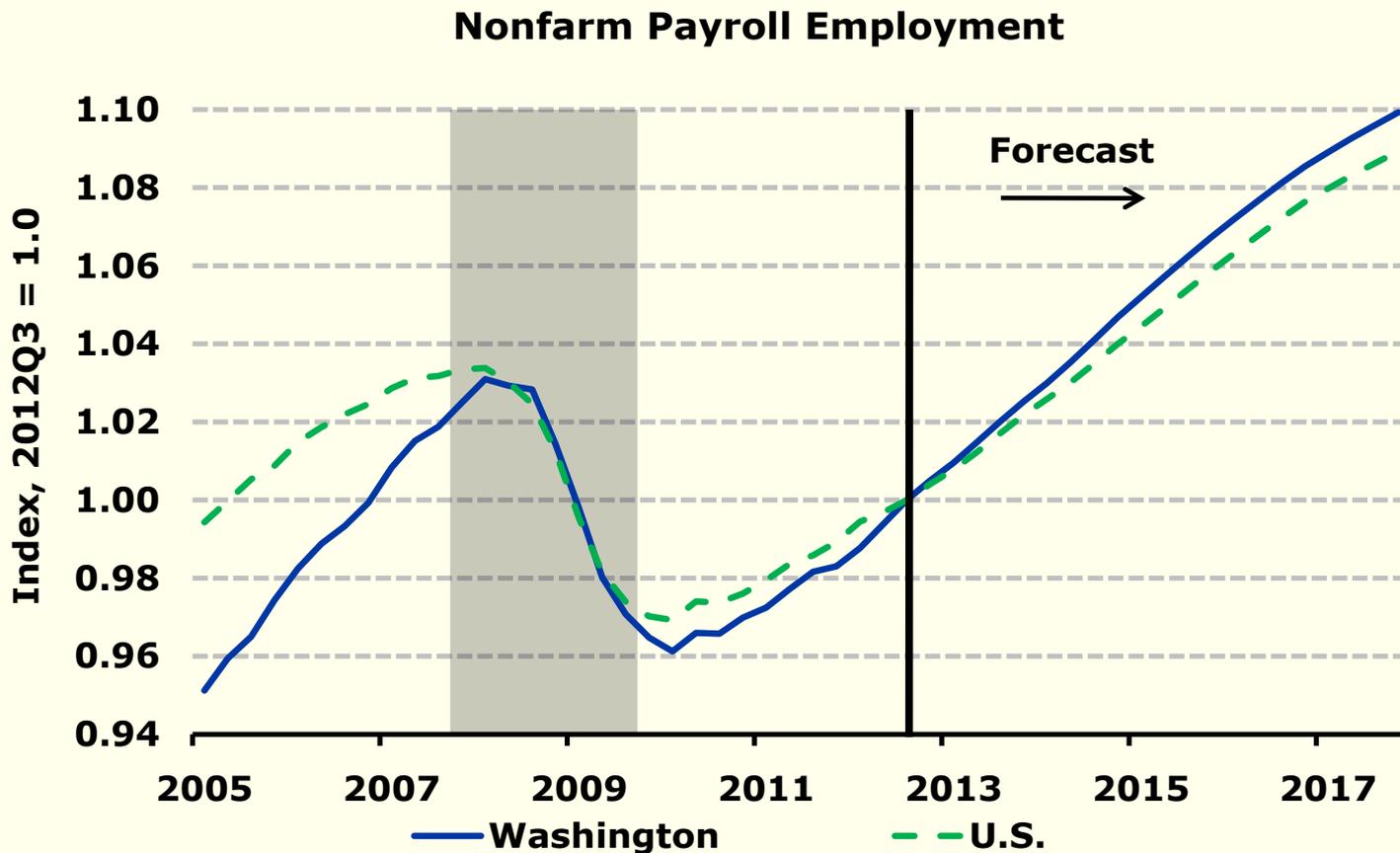


WA employment growth will continue to outpace the U.S.

Date of regaining peak:

WA:
2014Q2

U.S.:
2014Q3



Source: ERFC November 2012 forecast; historical data through 2012Q3

WASHINGTON STATE ECONOMIC AND REVENUE FORECAST COUNCIL

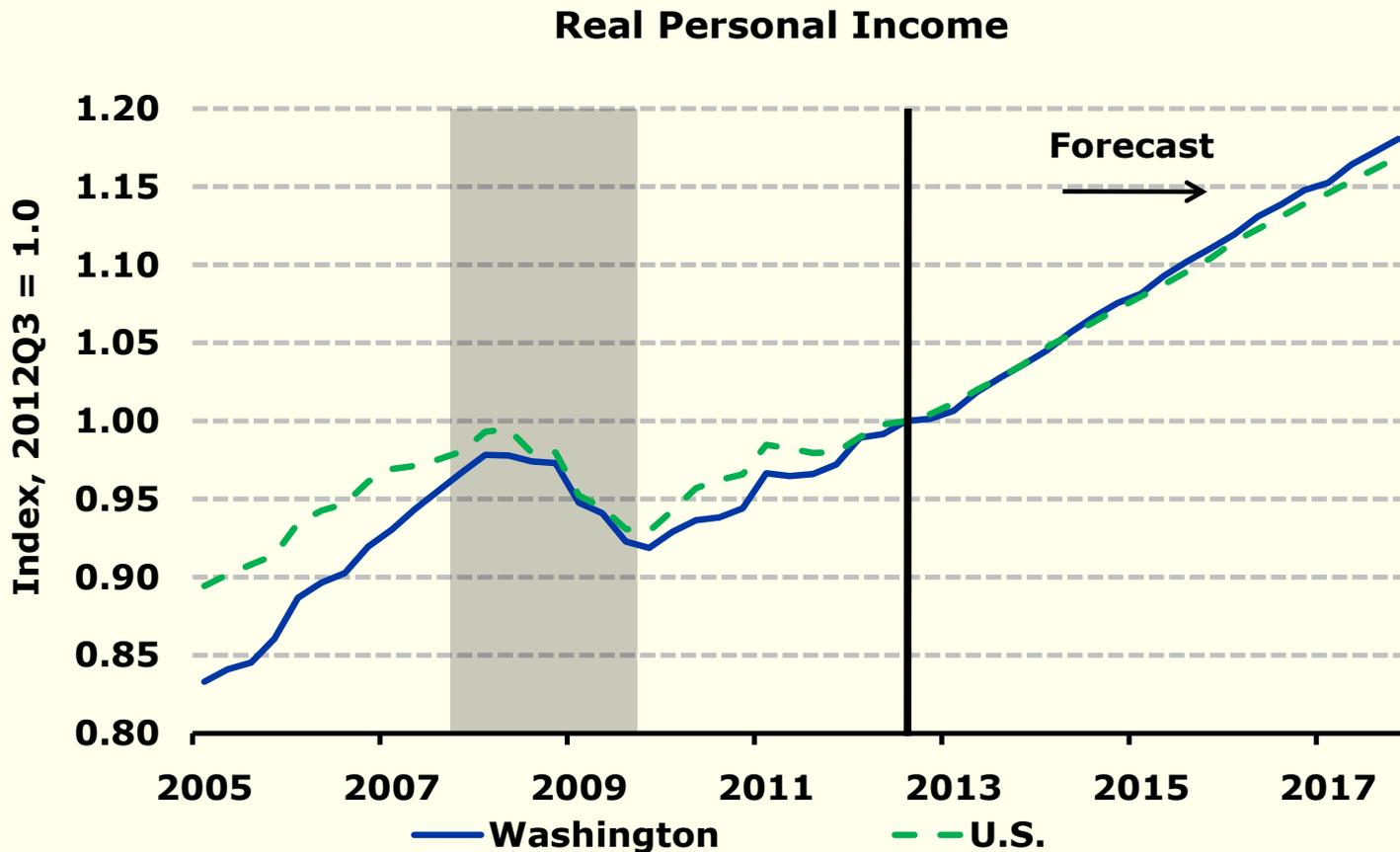


WA personal income will recover slightly faster than the U.S.

Date peak regained:

WA:
2012Q1

U.S.:
2012Q2



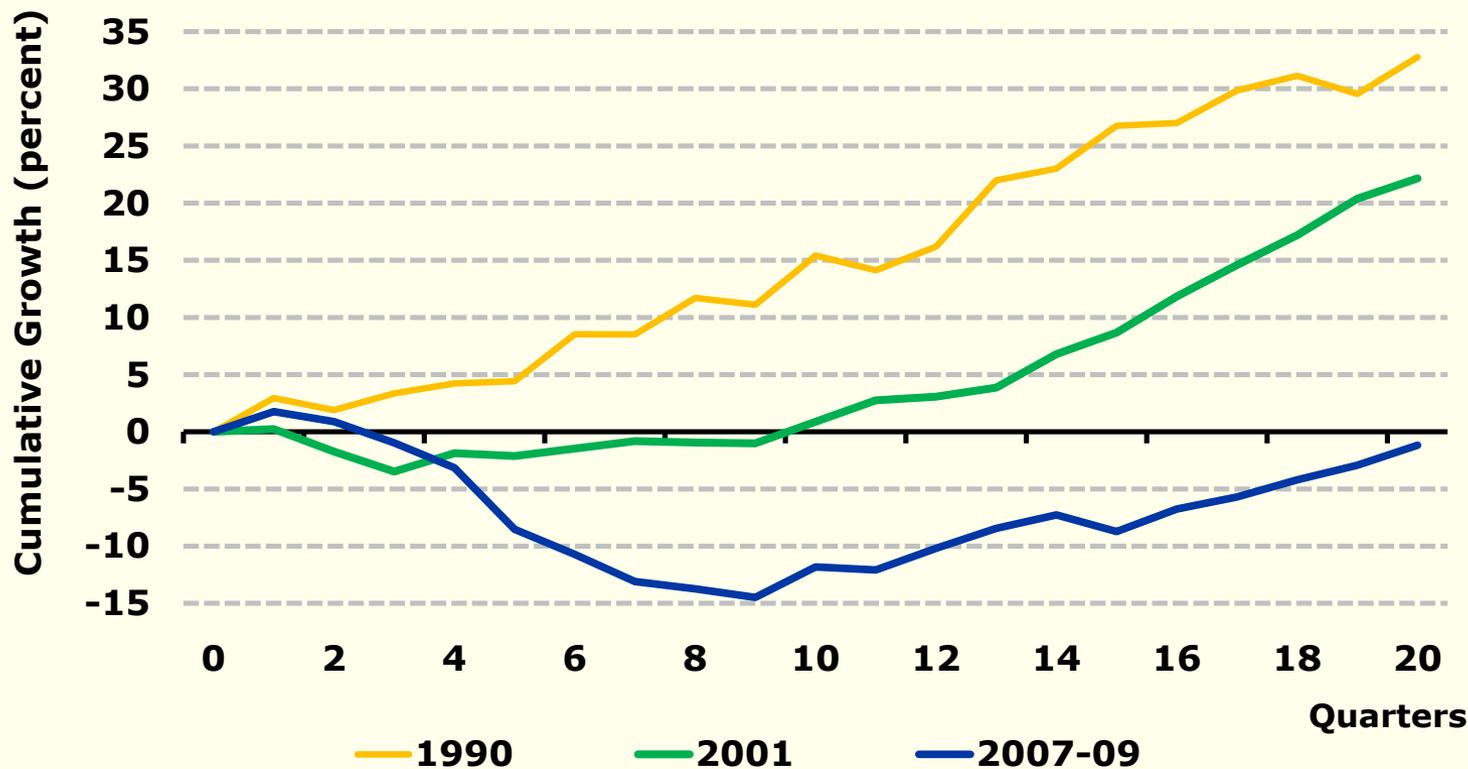
Source: ERFC November 2012 forecast; historical data through 2012Q3

WASHINGTON STATE ECONOMIC AND REVENUE FORECAST COUNCIL



Revenue collections have been weak compared to past recoveries

Revenue Act Collections after Business Cycle Peak



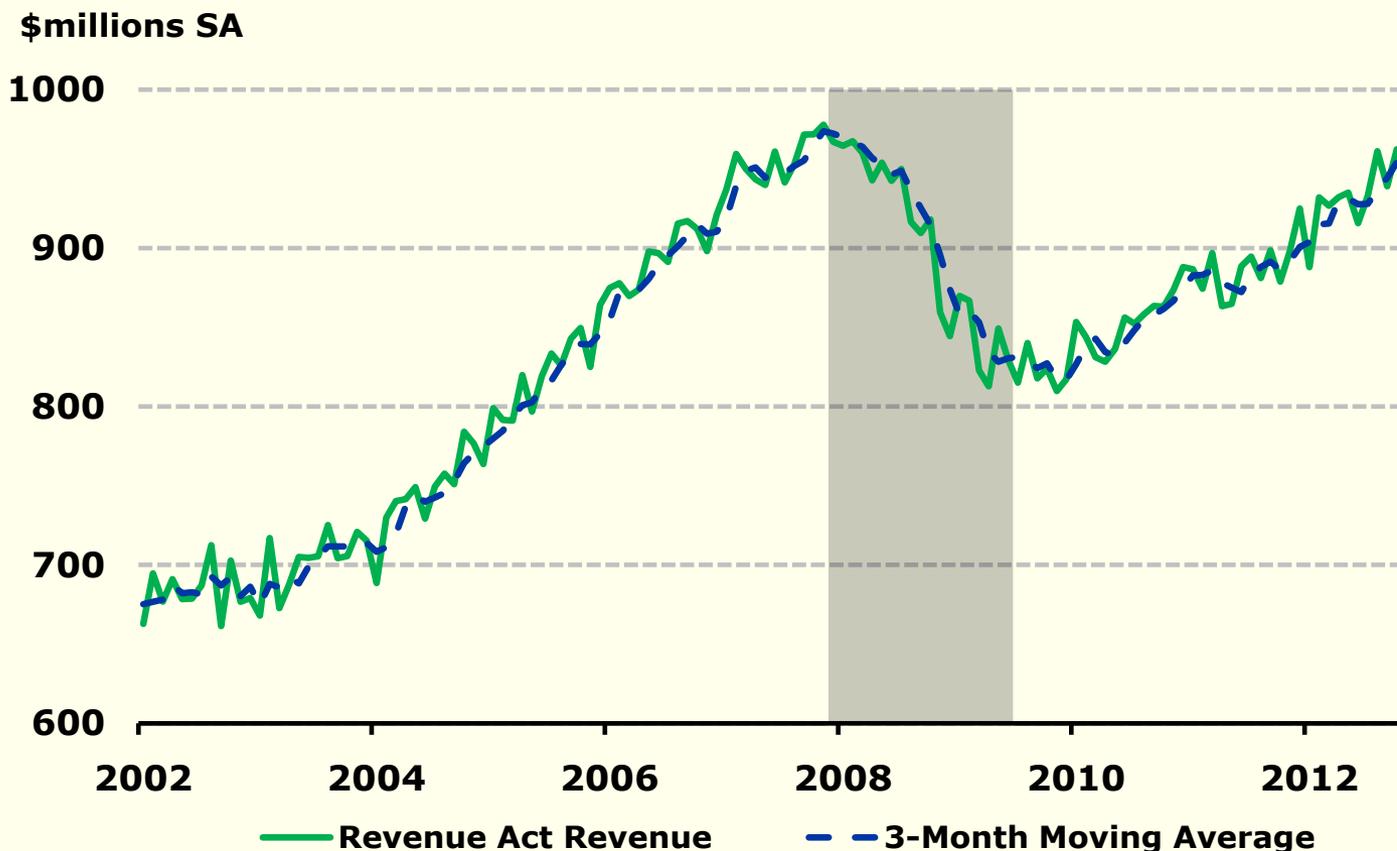
Source: ERFC; data through 2012 Q3

WASHINGTON STATE ECONOMIC AND REVENUE FORECAST COUNCIL



Revenue Act collections are still on an upward trend

Collections were up 5.4% year-over-year in the December 11, 2012 – January 10, 2013 collection period



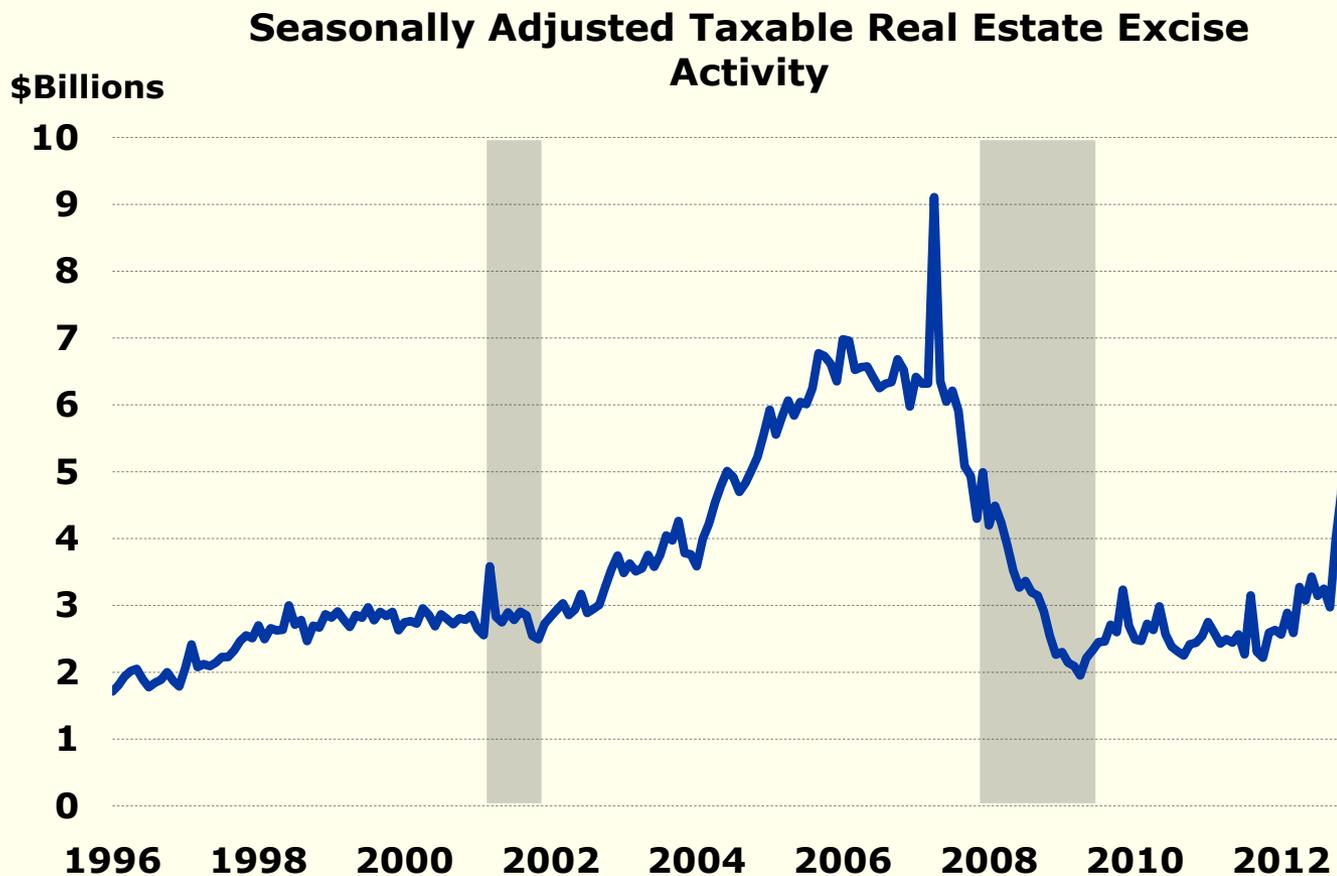
* Adjusted for large one-time transactions, amnesty payments and reporting frequency change, current definition of Revenue Act

Source: DOR and ERFC; monthly data through estimated November 2012 activity

WASHINGTON STATE ECONOMIC AND REVENUE FORECAST COUNCIL



October saw another spike in large commercial real estate sales



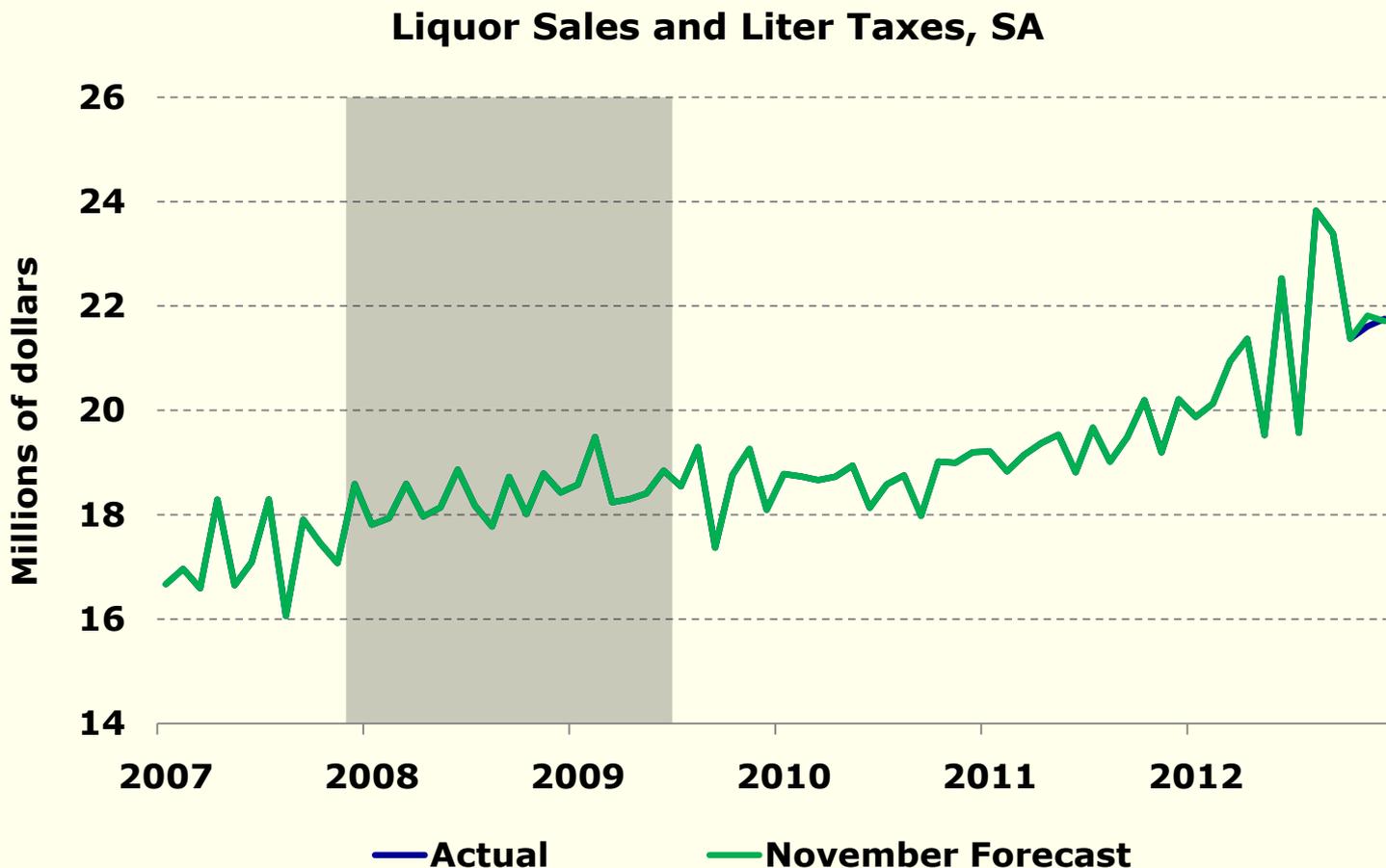
Source: ERFC; Monthly data through December 2012 preliminary

WASHINGTON STATE ECONOMIC AND REVENUE FORECAST COUNCIL



Revenue for liquor sales has been volatile recently

Revenue was \$175K (-0.4%) below the November forecast



Source: DOR, ERFC; data through December 2012

WASHINGTON STATE ECONOMIC AND REVENUE FORECAST COUNCIL



Forecast changes: General Fund State, 2011-2013 Biennium

September Forecast:

\$30,469 million

USD millions	November Forecast			
	<u>Collection Experience</u>	<u>Forecast Change</u>	<u>Forecast</u>	<u>Total Change*</u>
Dept. of Revenue	\$32	(\$3)	\$28,852	\$29
All other agencies	(\$1)	(\$20)	\$1,625	(\$21)
Total GF-S	\$31	(\$23)	\$30,477	\$8

* Detail may not add to total due to rounding



Forecast changes: General Fund State, 2013-2015 Biennium

September Forecast:

\$32,649 million

USD millions

November Forecast

	<u>Non-economic Change</u>	<u>Forecast Change</u>	<u>Forecast</u>	<u>Total Change*</u>
Dept. of Revenue	\$0	(\$113)	\$31,001	(\$113)
All other agencies	\$0	\$25	\$1,560	\$25
Total GF-S	\$0	(\$88)	\$32,561	(\$88)

* Detail may not add to total due to rounding



Forecast changes: General Fund State, 2015-2017 Biennium

September Forecast:

\$35,518 million

USD millions

November Forecast

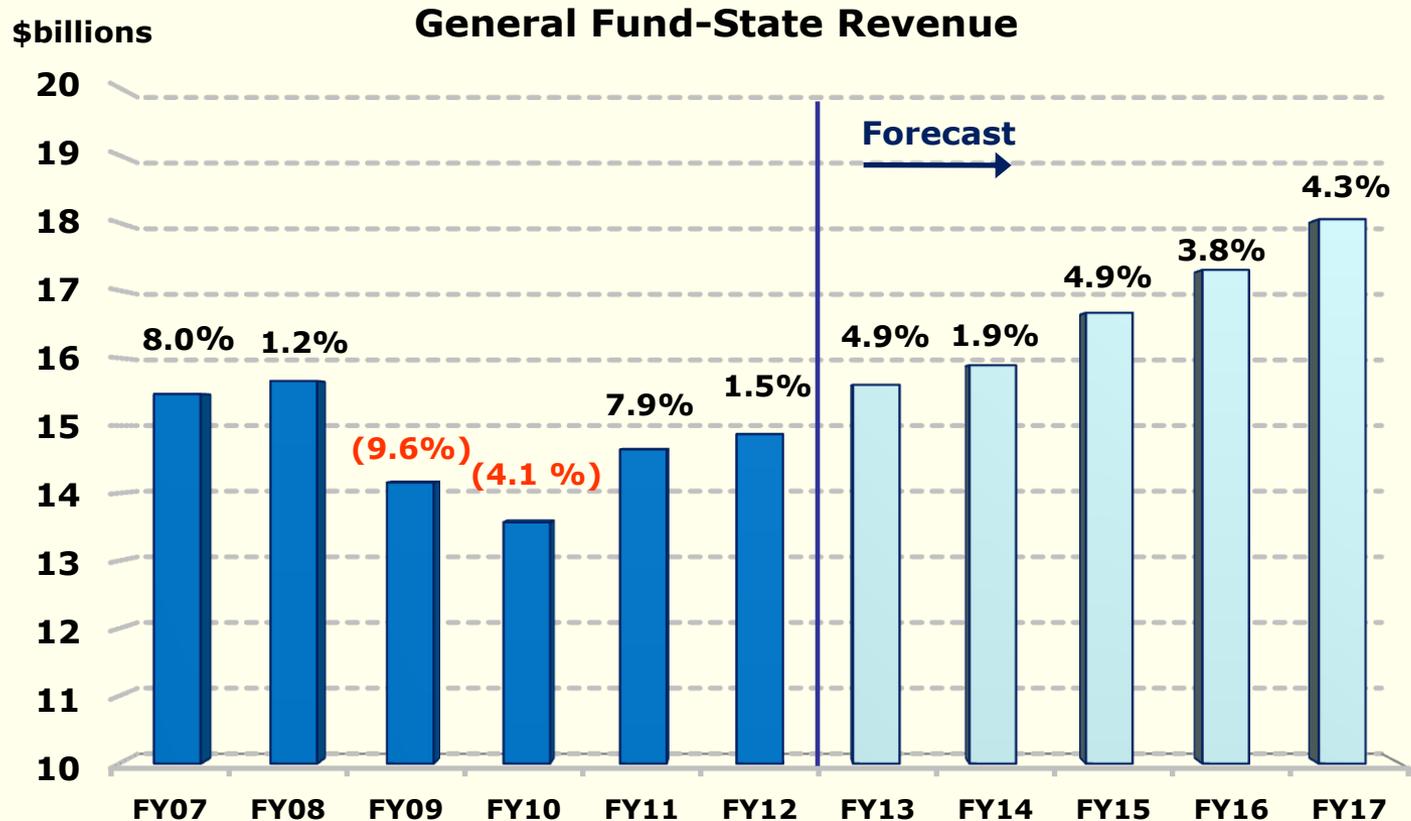
	<u>Non-economic Change</u>	<u>Forecast Change</u>	<u>Forecast</u>	<u>Total Change*</u>
Dept. of Revenue	\$0	(\$196)	\$33,906	(\$196)
All other agencies	\$0	\$33	\$1,449	\$33
Total GF-S	\$0	(\$163)	\$35,355	(\$163)

* Detail may not add to total due to rounding



General Fund* forecast by fiscal year

FY 2011 revenues were boosted by the tax amnesty program and one-time transfers of non-GF-S funds into the GF-S



Economic and Revenue Outlook
January 15, 2013

*General Fund & Related Funds for FY 07-09, General Fund – new definition for FY 10-17
Source: ERFC forecast, November 2012

WASHINGTON STATE ECONOMIC AND REVENUE FORECAST COUNCIL



Conclusion

- The forecast for the 2011-13 Biennium is \$8 million higher than in September
- The forecast for the 2013-15 Biennium is \$88 million lower than in September
- Revenues are expected to grow 8.0% between the 2009-11 and 2011-13 biennium and 6.8% between the 2011-13 and 2013-15 biennium
- As in September, we are forecasting slow economic and job growth for both the national and state economies
- The level of uncertainty in the baseline remains extremely high, and downside risks outweigh upside risks



Questions



Economic and
Revenue Outlook
January 15, 2013

Slide 34

Economic & Revenue Forecast Council
1025 E. Union Avenue, Suite 544
Olympia WA 98504-0912

www.erfc.wa.gov
360-534-1560