

Washington State Economic & Revenue Outlook

Presented to
Financial Management Advisory Council

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February 25, 2010
Olympia, Washington



WASHINGTON STATE
ECONOMIC AND REVENUE FORECAST COUNCIL



Summary

- We are coming out of the "Great Recession"
 - The economy will gain traction by mid-year
 - The recovery in revenues is underway, but progress will be slow
- The economic recovery faces headwinds
 - Real estate, especially commercial
 - Banking, particularly local and regional banks
- The revenue recovery too faces headwinds
 - Slow job growth
 - Tentative consumer confidence
- Upside
 - Exports
 - Stable aerospace and software publishing

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Dead Cat Bounce

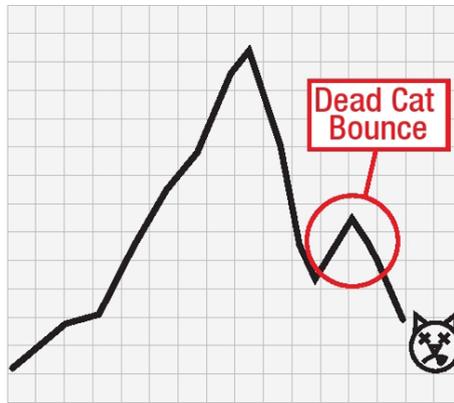


Diagram 1

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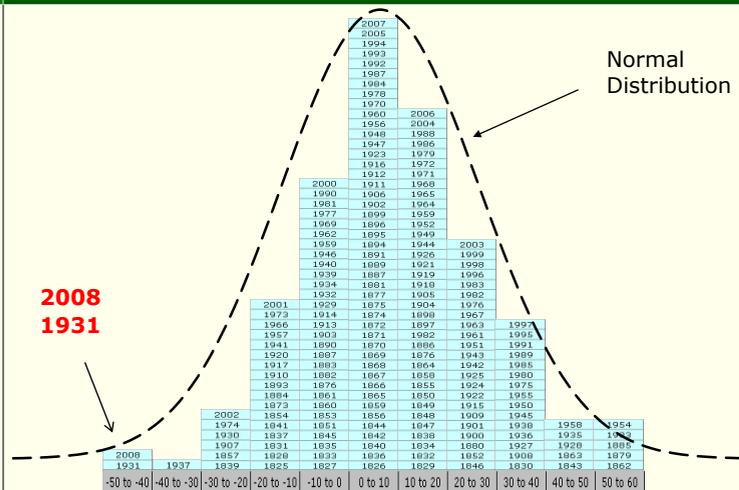
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Equity returns in 2008 were a tail event

U.S. Stock Market Total Returns 1825 - 2008



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Source: AXA

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At this stage in 1982-83, employment had started to recover

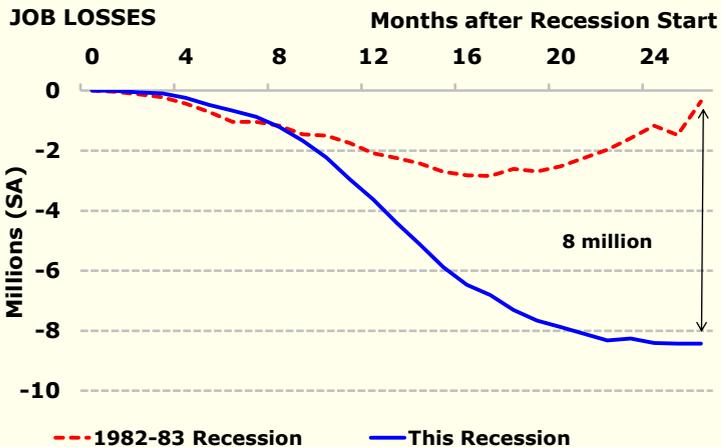
Cumulative job losses at 26 months

1982-83:
1.4% of labor force

This time:
4.7% of labor force

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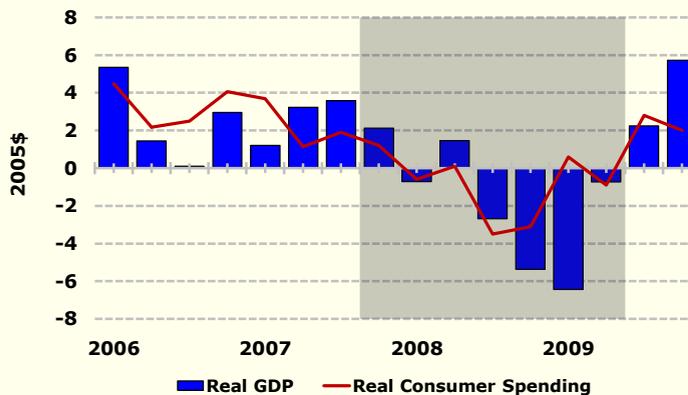
Source: BLS, ERFC; data through January 2009

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GDP returned to growth in Q3

Percent growth, SAAR



Source: BEA, data through 2009 Q4

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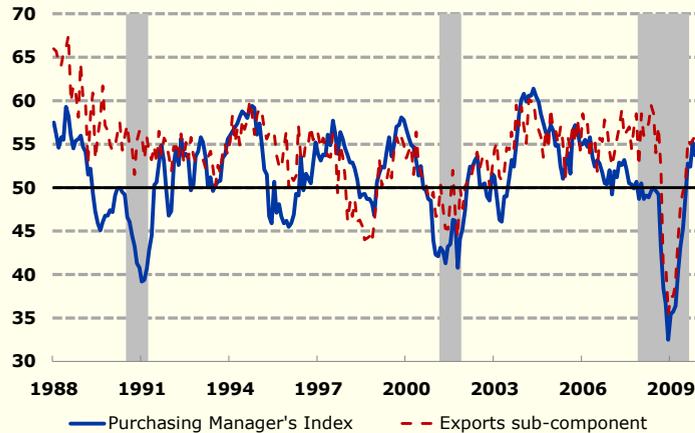


Manufacturing is growing again thanks to exports

An index greater than 50, implies growth

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Source: Institute of Supply Management; data through January 2010

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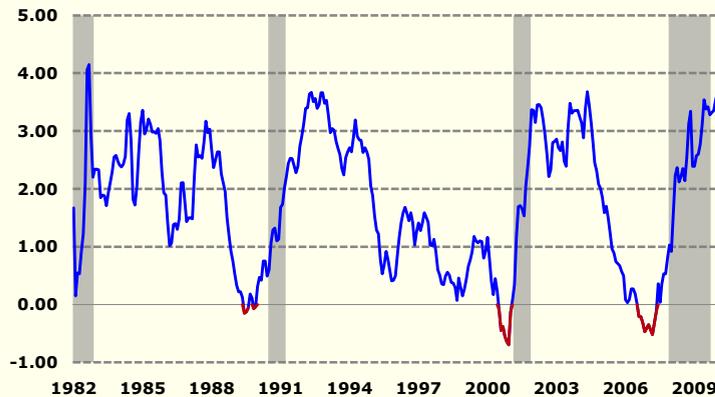
Increasing yield curve spread points to growth

An inverted yield curve typically precedes a recession while a steepening yield curve signifies a recovery

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Yield Curve Spread 10-Year minus 3-Month U.S. Treasuries



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Unemployment is still high

It is normal for this rate to continue to rise even after the economy is in recovery

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Unemployment Rate, Percent, SA



Source: WA ESD, BLS; data through January 2010

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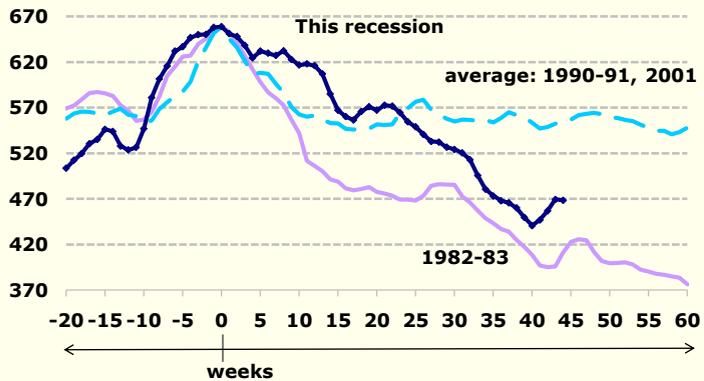
The recovery in employment has been slow, but is poised to improve

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U.S. Initial Unemployment Claims

Thousands, 4-week MA



Source: U.S. Department of Labor, ERFC; data through Jan 30, 2010

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Consumer confidence is improving, but tentatively

Index
Mich: 1966Q1 = 100, SA
Conf Board: 1985 = 100, SA



Source: University of Michigan; Conference Board, data through January 2010, preliminary

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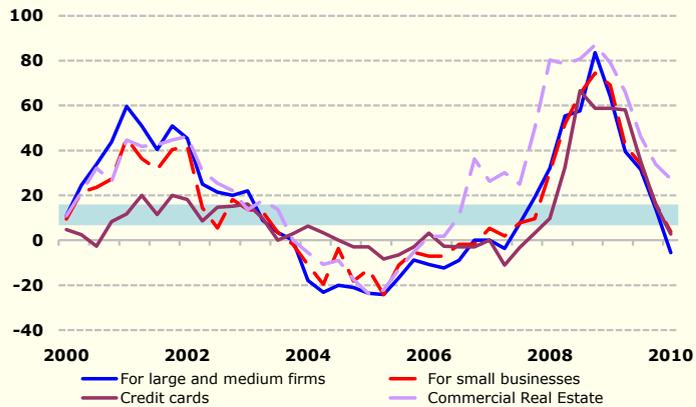
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Bank lending appears to be easing, but not for commercial real estate

Net Tightening minus Easing
Percent



Source: Federal Reserve Board, Senior Loan Officers Quarterly Survey; data through January 2010 survey

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Survey includes 60 large domestic banks and 24 U.S. branches of foreign banks

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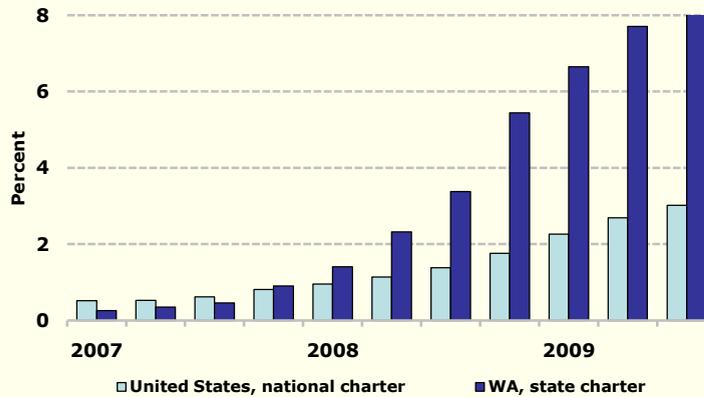
Asset quality of regional banks is deteriorating because of over exposure to commercial real estate

This is generally true for state chartered banks in other states as well

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Ratio of Non-Performing to Total Assets



Source: FDIC, data through 2009 Q3

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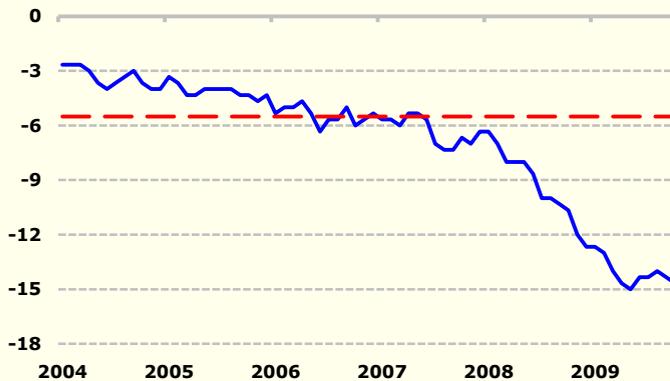


Credit conditions remain tight for small business...

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Availability of Loans Net Percent ("Easier" minus "Harder"), 3mma



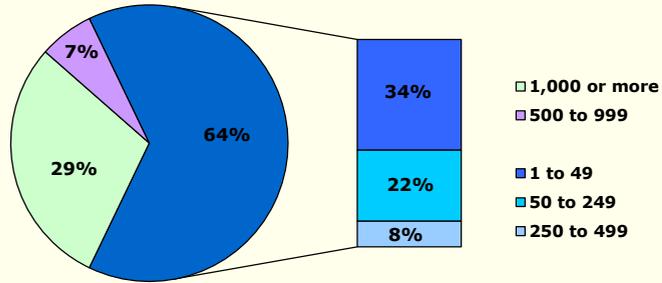
Source: National Federation of Independent Business; data through December 2009

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... who create most of the jobs

Since 1992, 64% of the net change in employment has occurred in small businesses



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Source: BLS, data from 1992 Q3 to 2009 Q1

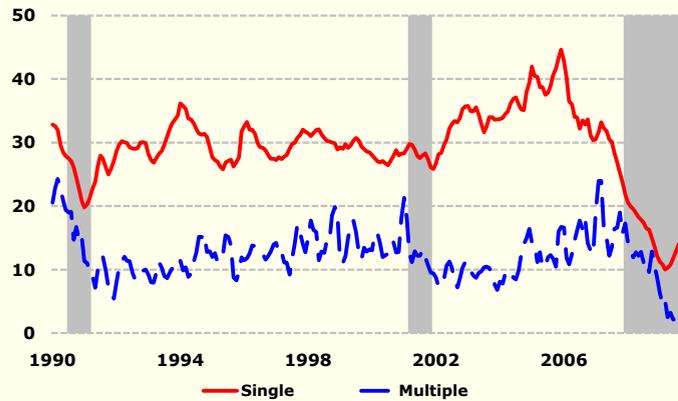
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WA single family building permits are doing better than multi-family

Thousands, SA, 3MMA



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Source: U.S. Census Bureau; data through December 2009

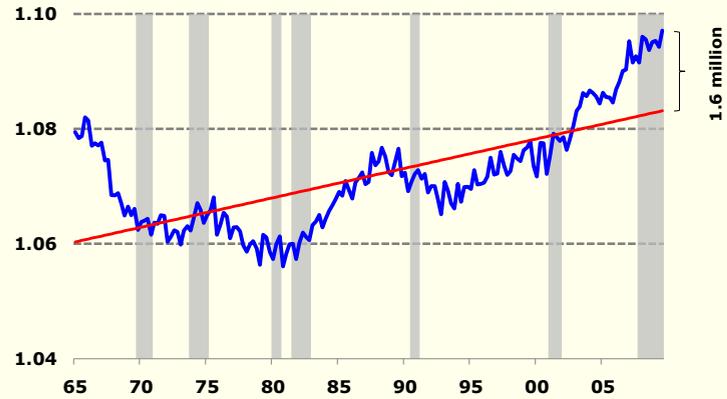
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National housing inventory remains well above trend

Housing Units per Household



Source: U.S. Census Bureau, ERFC; data through 2009 Q3

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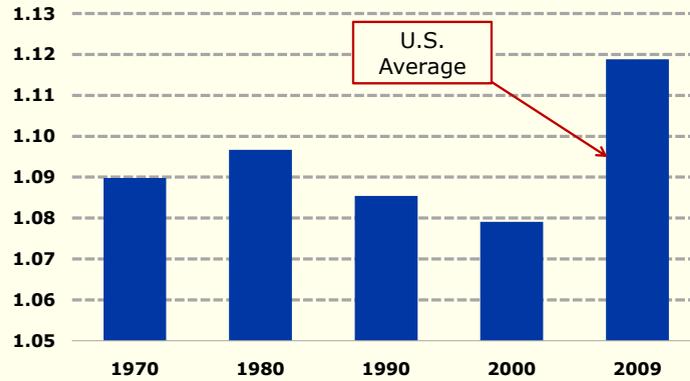
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WA housing units per household is higher than the nation

Washington State Housing Units Per Household



Source: U.S. Census Bureau, OFM; data through December, 2009

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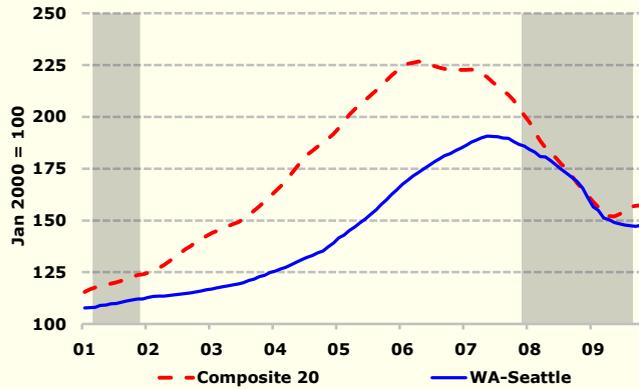
Home prices in Seattle appear to be leveling off, but lag the nation in the turnaround

Seattle Home Prices

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Case Shiller Seattle House Price Index, SA



Source: S&P/Case-Shiller; data through November 2009

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REET collections fell after first round tax credits expired

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Seasonally adjusted taxable real estate excise activity

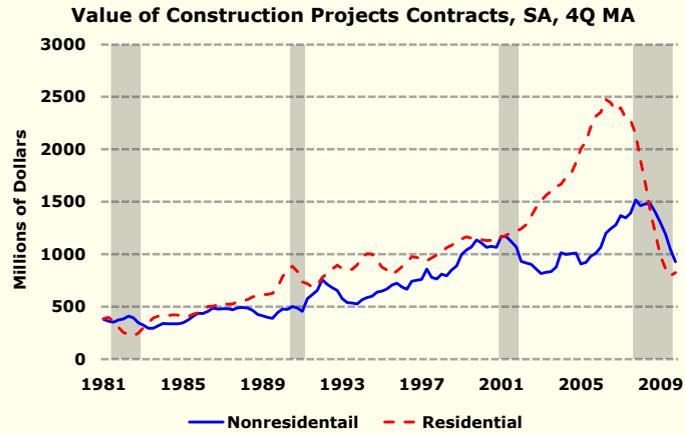


Source: ERFC; Monthly data through January 2010

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Non-residential construction lagged residential on the way down, and has yet to find bottom



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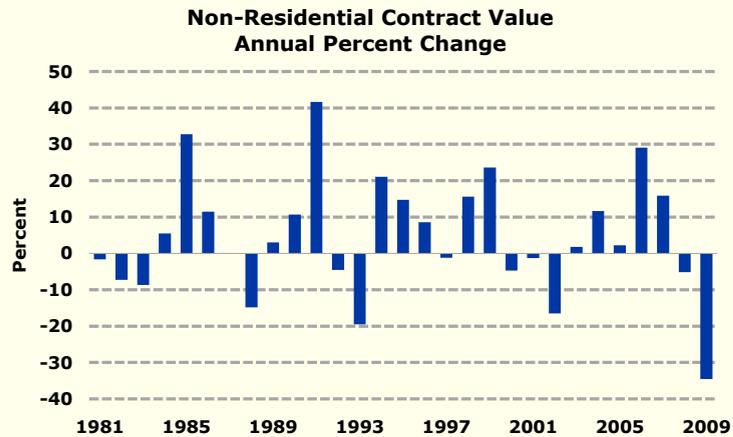
Source: McGraw-Hill Construction, ERFC; data through 2009 Q4

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This is the worst downturn in non-residential construction in 30 years



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Source: McGraw-Hill Construction, data through December, 2009

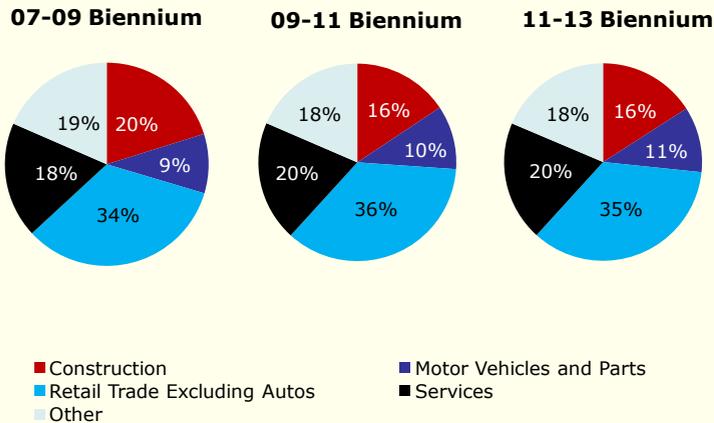
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The share of construction in the Retail Sales tax base has shrunk

USD Millions



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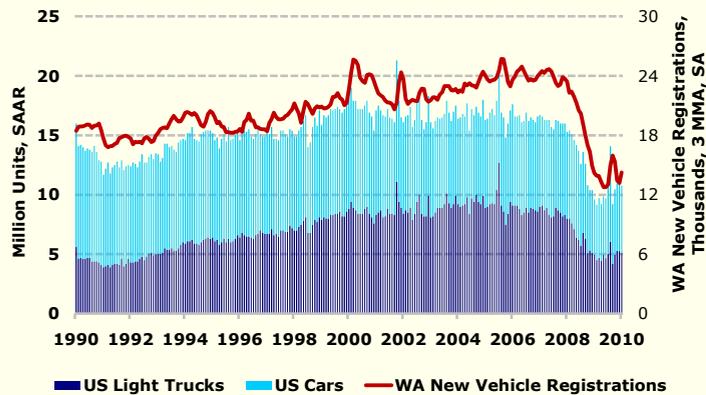
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Automotive sales have stabilized nationally and in the state

National car sales were 1.2 million units (ann.) higher in January 2010 than in January 2009



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Source: Autodata Corporation, WA DOL; data through January 2010

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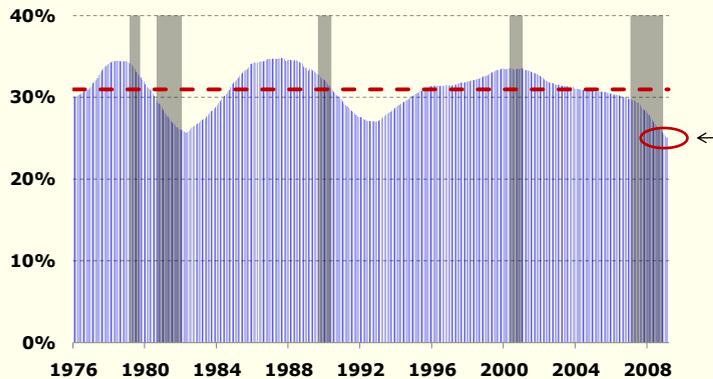
Relative age of the car fleet indicates imminent turnaround in car sales

The percent of "old" cars on the road is at a historic high

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U.S. LMV Sales: Ratio of 36/120 Months



Source: Autodata Corporation, ERFC; data through January 2010

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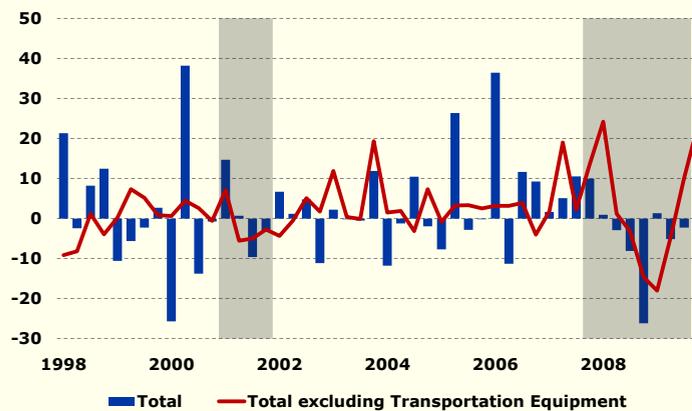
Exports will help the state recover faster than the nation

Exports excluding transport equipment were up 23% in Q4

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Exports, SA Percent Change, quarter ago



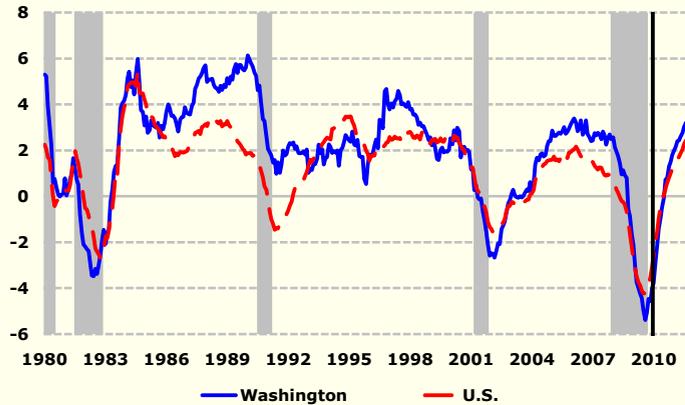
Source: Wisier Trade Data; through 2009 Q4

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WA employment lagged the nation in the downturn and will recover a little stronger than the nation

Percent change, year ago



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Source: ERFC November 2009 forecast; actual through December 2009

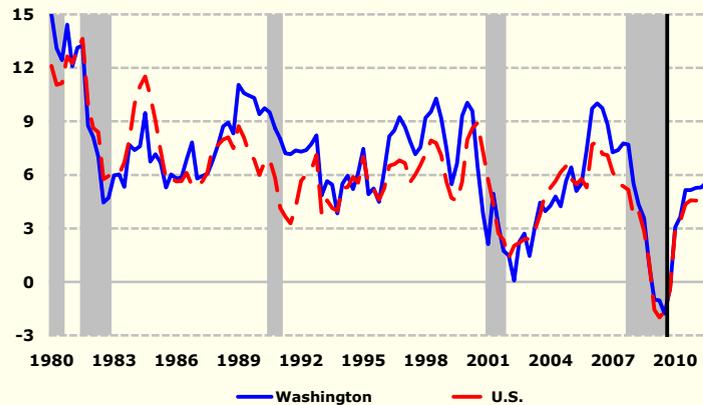
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The recovery in WA personal income growth is expected to be better than the nation's

Percent change, year ago



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Source: ERFC February 2010 forecast; actual data through 2009Q3

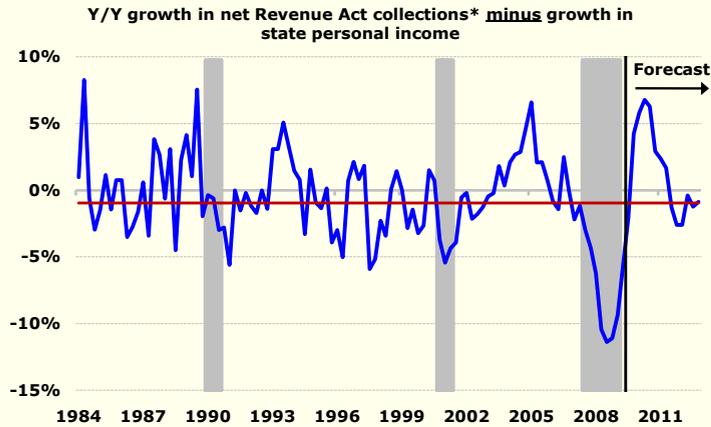
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Revenue growth relative to income is starting to turn around

The difference between the growth rate of Revenue Act collections and state personal income began to shrink in the second quarter of 2009.



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* Adjusted for new legislation, current definition of Revenue Act
Source: DOR and ERFC; data through 2009Q4 estimated

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Forecast changes: General Fund State, 2009-2011 Biennium

November Forecast:

\$28,843 million

USD millions	February '10 Forecast				Total Change*
	Collection Experience	Non-economic Change	Forecast Change	Forecast	
Dept. of Revenue	\$61	(\$150)	(\$52)	\$27,245	(\$141)
All other agencies	\$1	\$0	\$22	\$1,479	\$23
Total GF-S	\$61	(\$150)	(\$30)	\$28,725	(\$118)

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* Detail may not add to total due to rounding

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Initial Forecast: General Fund State, 2011-2013 Biennium

USD millions

USD millions

	Forecast
Dept. of Revenue	\$30,658
All other agencies	\$1,566
Total GF-S	\$32,224

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* Detail may not add to total due to rounding

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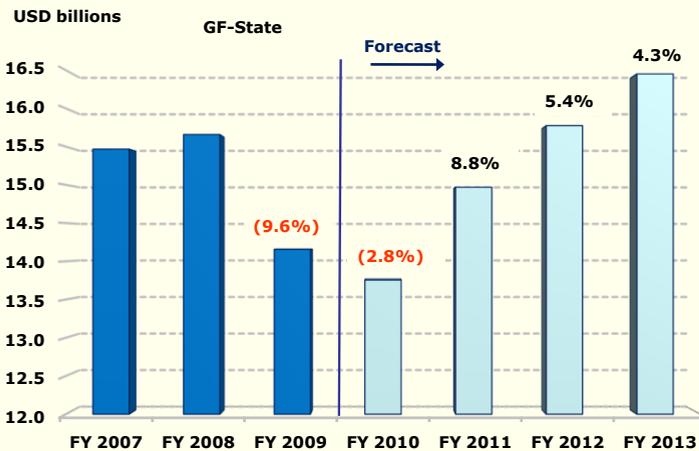


General Fund* forecast by fiscal year

* General Fund & Related Funds for FY 07, 08, and 09

General Fund - new definition, for FY 10-13

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Conclusion

Pluses

- Recovery in progress
- Employment likely to improve soon
- Car sales have stabilized
- Large banks able to extend credit

Minuses

- Problems at community banks
- Weak consumer confidence
- Slow recovery in construction

- Revenues have come in close to our November forecast, and are bumping along the bottom
- We expect 12.2% revenue growth in the 11-13 biennium compared to the current one

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Questions



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