Revenue Update

Presented to
Financial Management Advisory Council

Steve Lerch
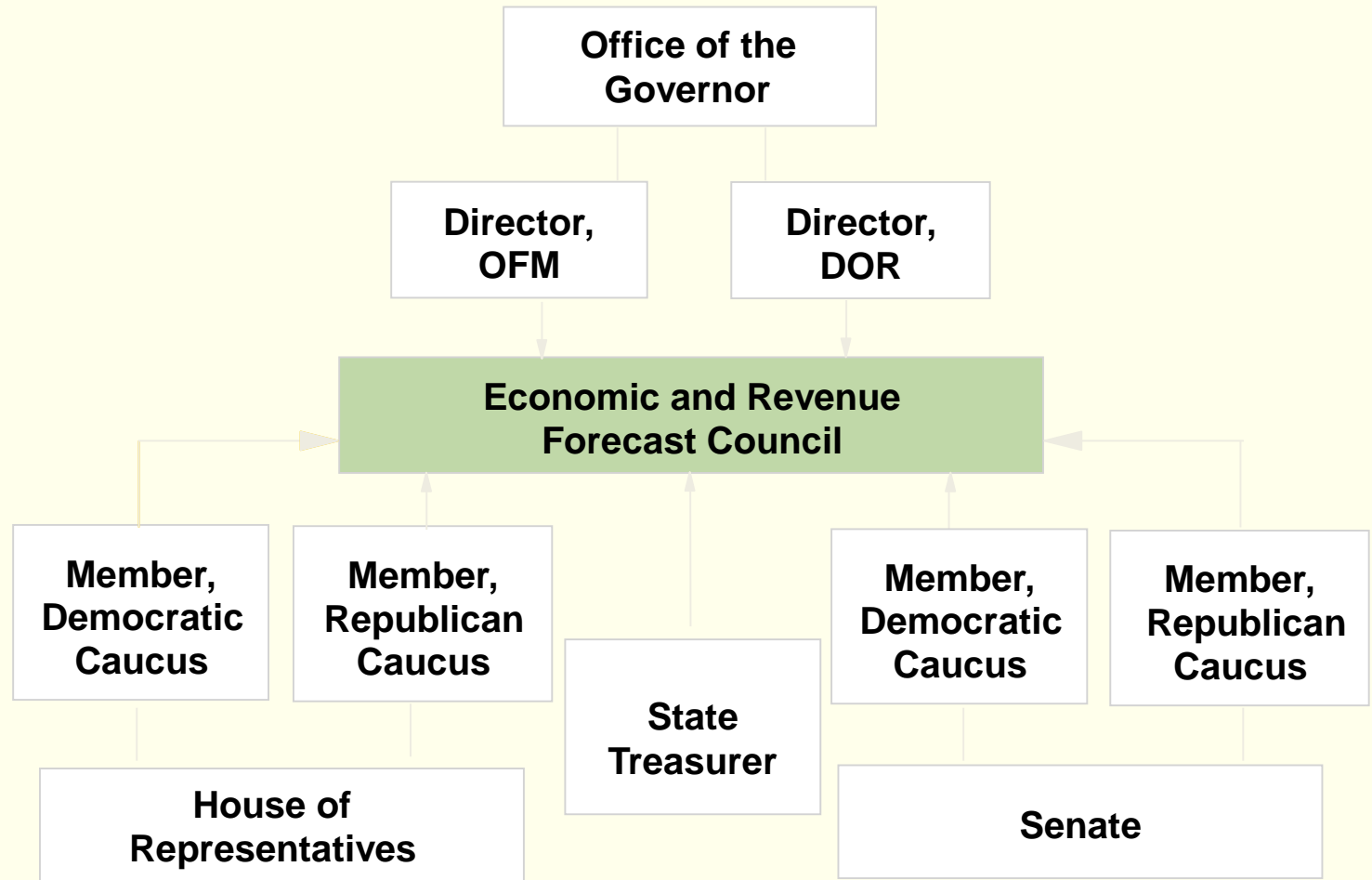Executive Director

March 28, 2019
Olympia, Washington

WASHINGTON STATE
ECONOMIC AND REVENUE FORECAST COUNCIL

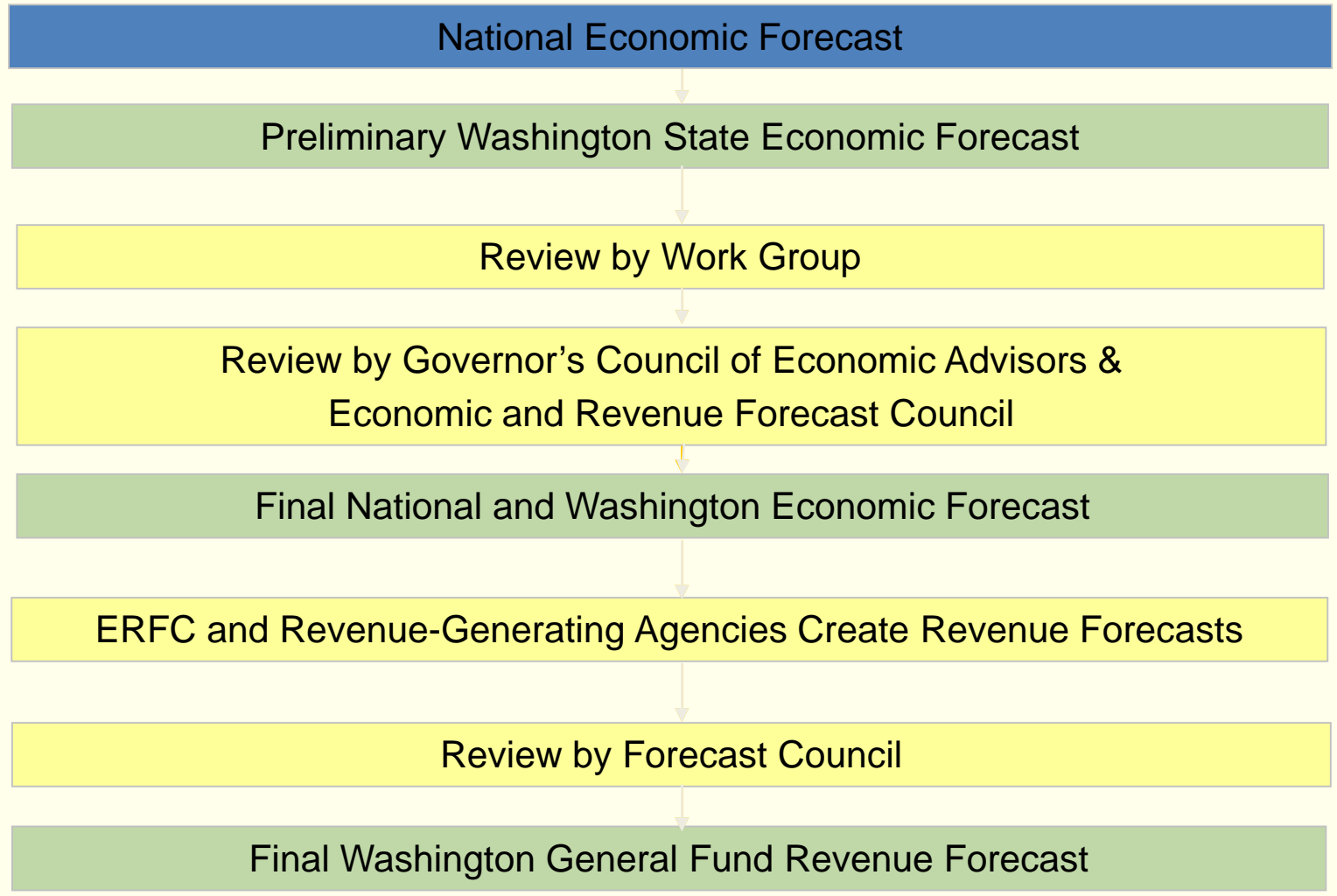# Economic and Revenue Forecast Council Organization Chart

ERFC

- Created in 1984 as part of Dept. of Revenue

- Became separate agency in 1990

Office of the Governor

Director, OFM

Director, DOR

Economic and Revenue Forecast Council

Member, Democratic Caucus

Member, Republican Caucus

State Treasurer

Member, Democratic Caucus

Member, Republican Caucus

House of Representatives

Senate

Revenue Review
September 20, 2017

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ERFC Forecast Process

The national economic forecast is based on a modified version of the IHS Markit model of the U.S. economy

National Economic Forecast

↓

Preliminary Washington State Economic Forecast

↓

Review by Work Group

↓

Review by Governor's Council of Economic Advisors & Economic and Revenue Forecast Council

↓

Final National and Washington Economic Forecast

↓

ERFC and Revenue-Generating Agencies Create Revenue Forecasts

↓

Review by Forecast Council

↓

Final Washington General Fund Revenue Forecast

WASHINGTON STATE ECONOMIC AND REVENUE FORECAST COUNCIL

Summary

- U.S., WA forecasts similar to the November forecast

- Baseline forecast has slowing growth but no recession

- Potential impact of 737 MAX grounding adds a new downside risk

- The Near General Fund-State forecast is increased by $307 million for the 2017-19 biennium and by $554 million for 2019-21 biennium

Data updates since preliminary forecast

U.S.

- February employment: +20,000 jobs

- February unemployment rate: dropped from 4.0% to 3.8%

- 2018 Q4 GDP: 0.05% higher than preliminary

- March Blue Chip GDP forecast: slightly lower than preliminary

Washington

- February employment: -4,700 jobs

Selected forecast risks

Labor markets

- Unemployment rate, initial UI claims low
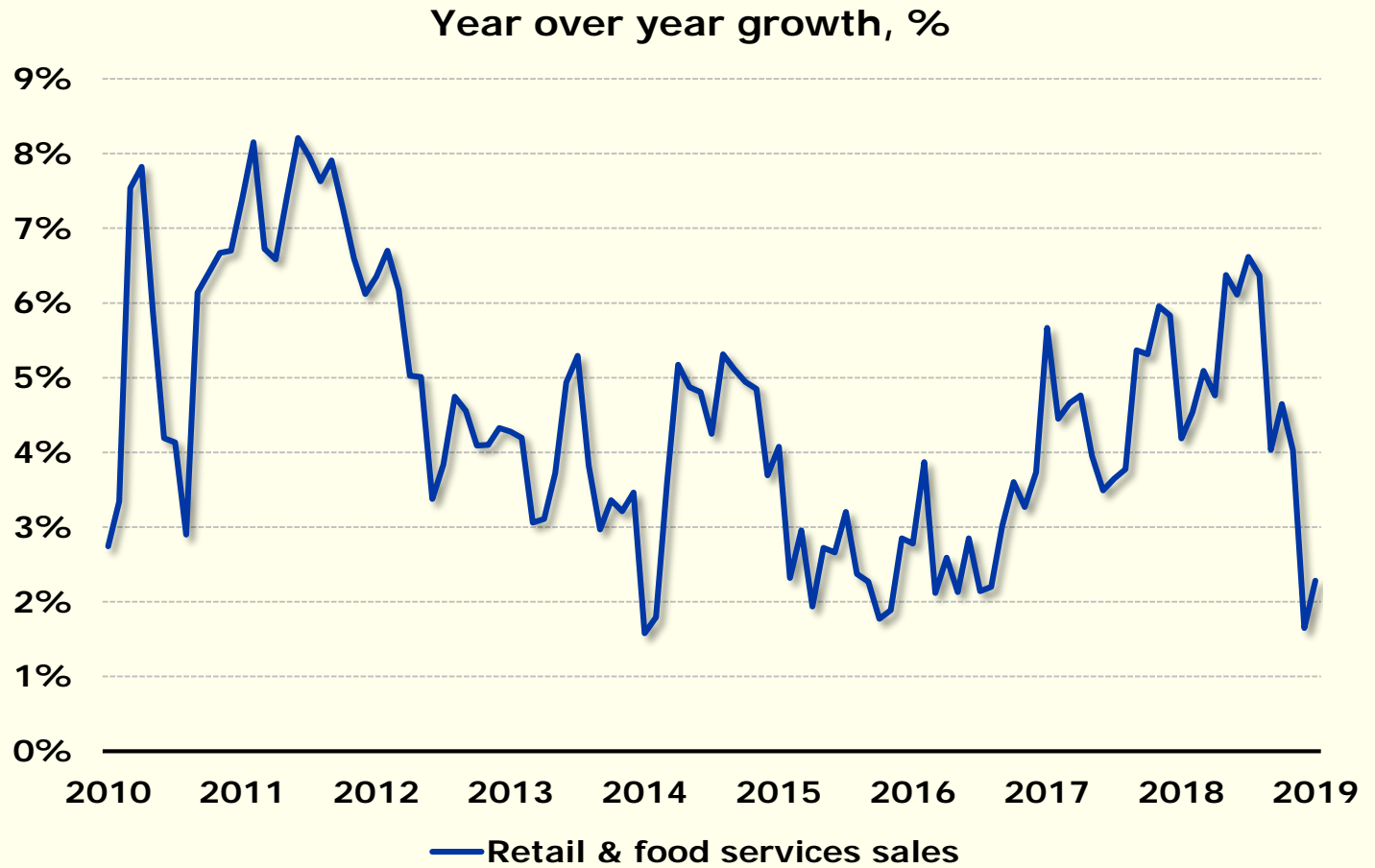
- Job growth has been strong until February

737 MAX

- Currently, impact on WA employment and personal income unclear

International trade policy

- Late March China – U.S. trade deal seems less likely

WASHINGTON STATE ECONOMIC AND REVENUE FORECAST COUNCIL

U.S. retail sales growth has slowed recently

Year over year growth, %

Retail & food services sales

Source: U.S. Census Bureau data through January 2019

WASHINGTON STATE ECONOMIC AND REVENUE FORECAST COUNCIL

OECD leading index suggests slowing growth in next 6 – 9 months

The index is designed so the long-term average is 100.

U.S. Composite Leading Indicator
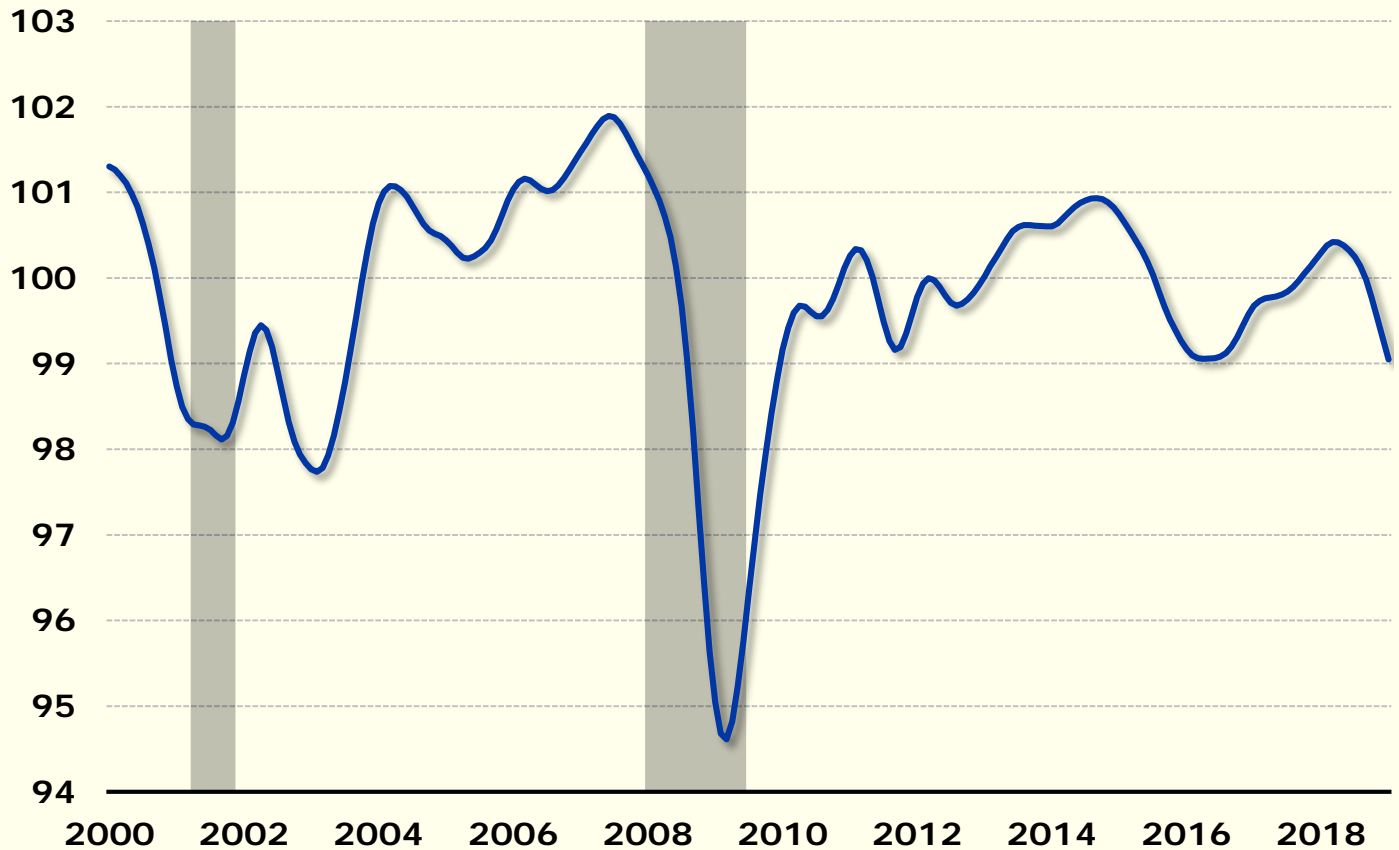
Source: Organization for Economic Cooperation and Development, data through Jan. 2019

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An inverted yield curve (short-term interest rates > long-term rates) is a consistent recession predictor

As of February 2019, 10 year Treasury bond yields were 0.24% above three month Treasury bill yields

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10 yr. Treasury rate − 3 mo. Treasury rate
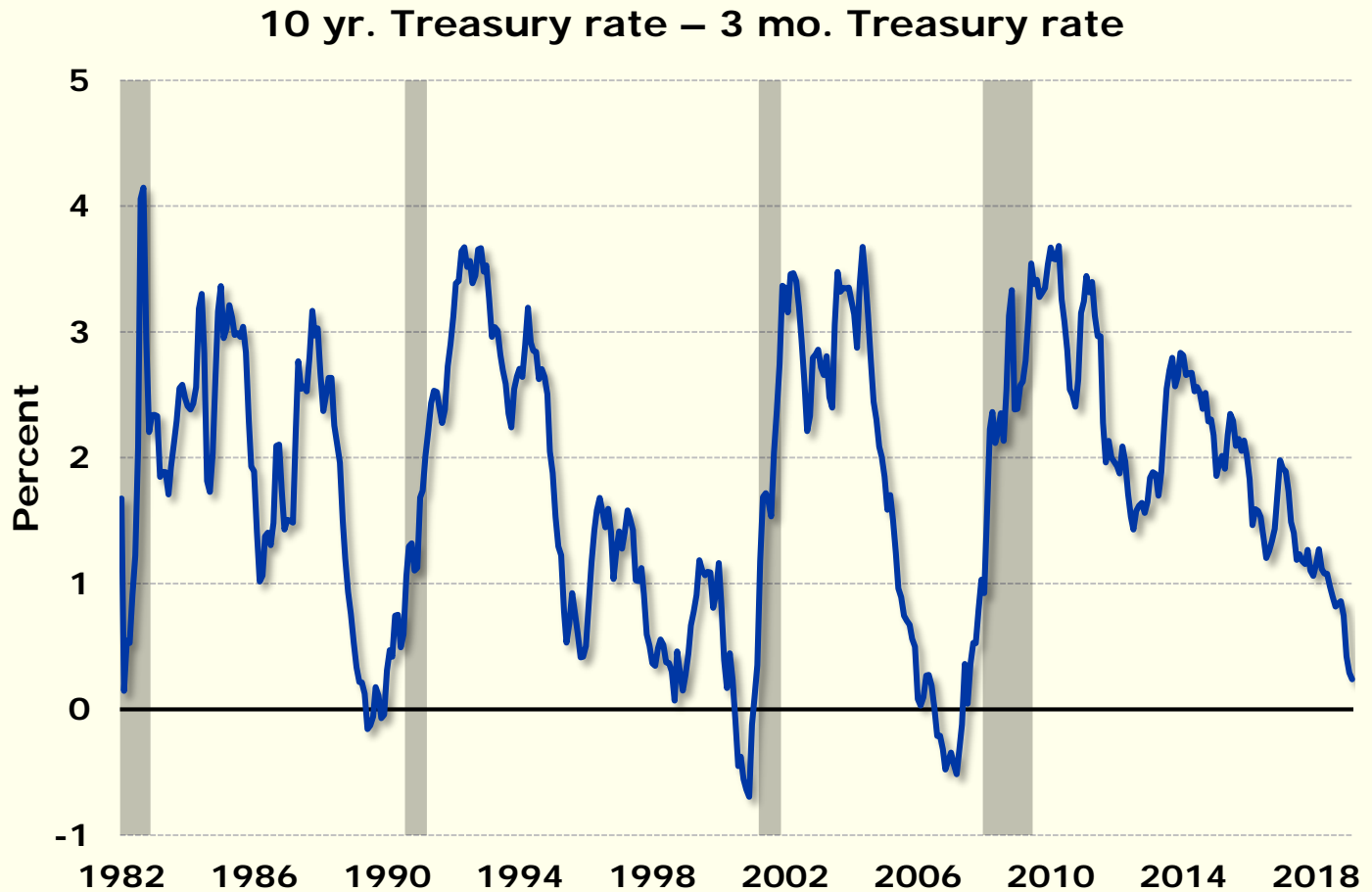
Source: Federal Reserve Bank of St. Louis, data through Feb. 2019

WASHINGTON STATE ECONOMIC AND REVENUE FORECAST COUNCIL

Wall Street Journal economists' survey shows recession probability rising but below 25%

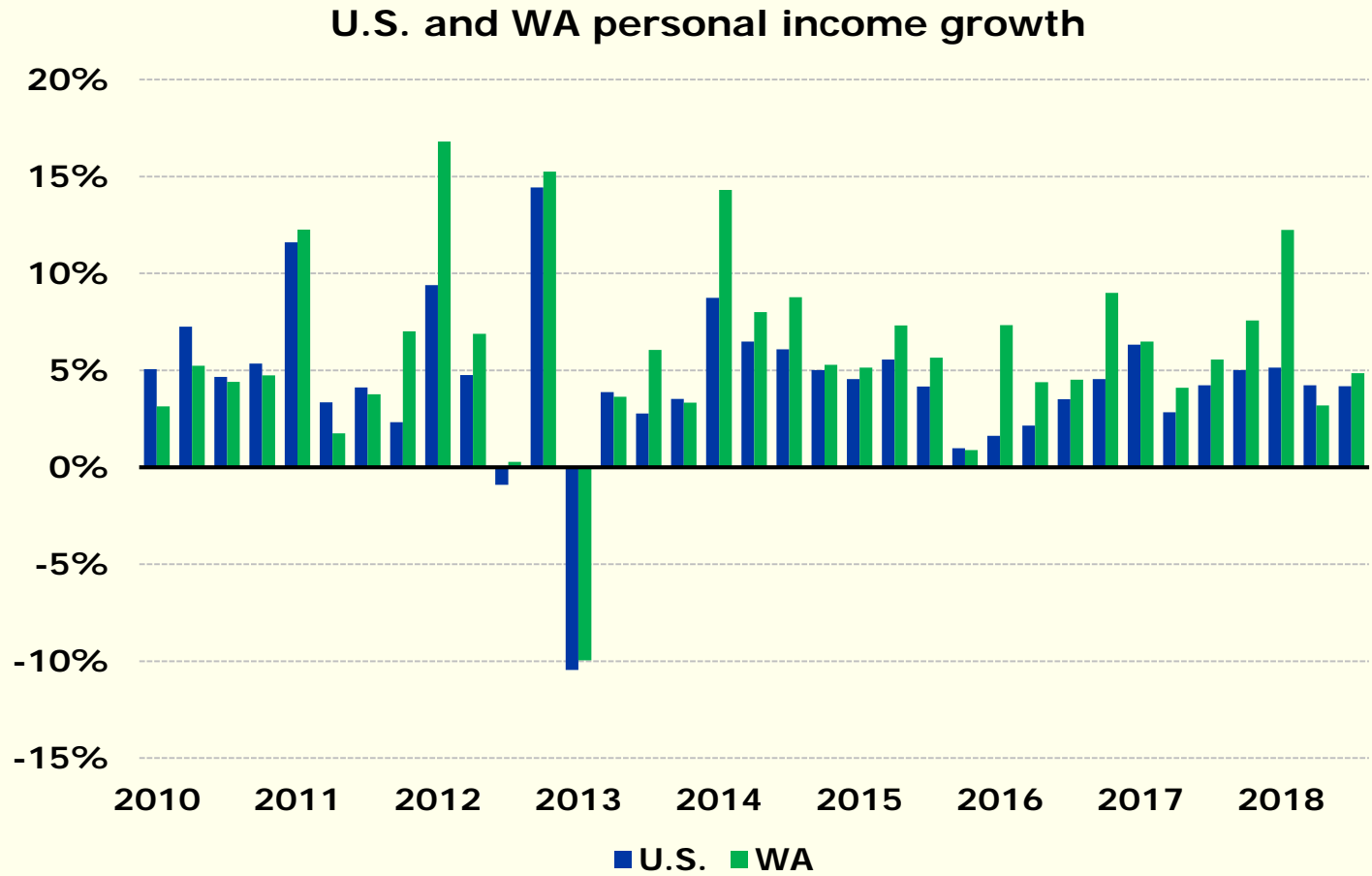## Probability of recession in next 12 months
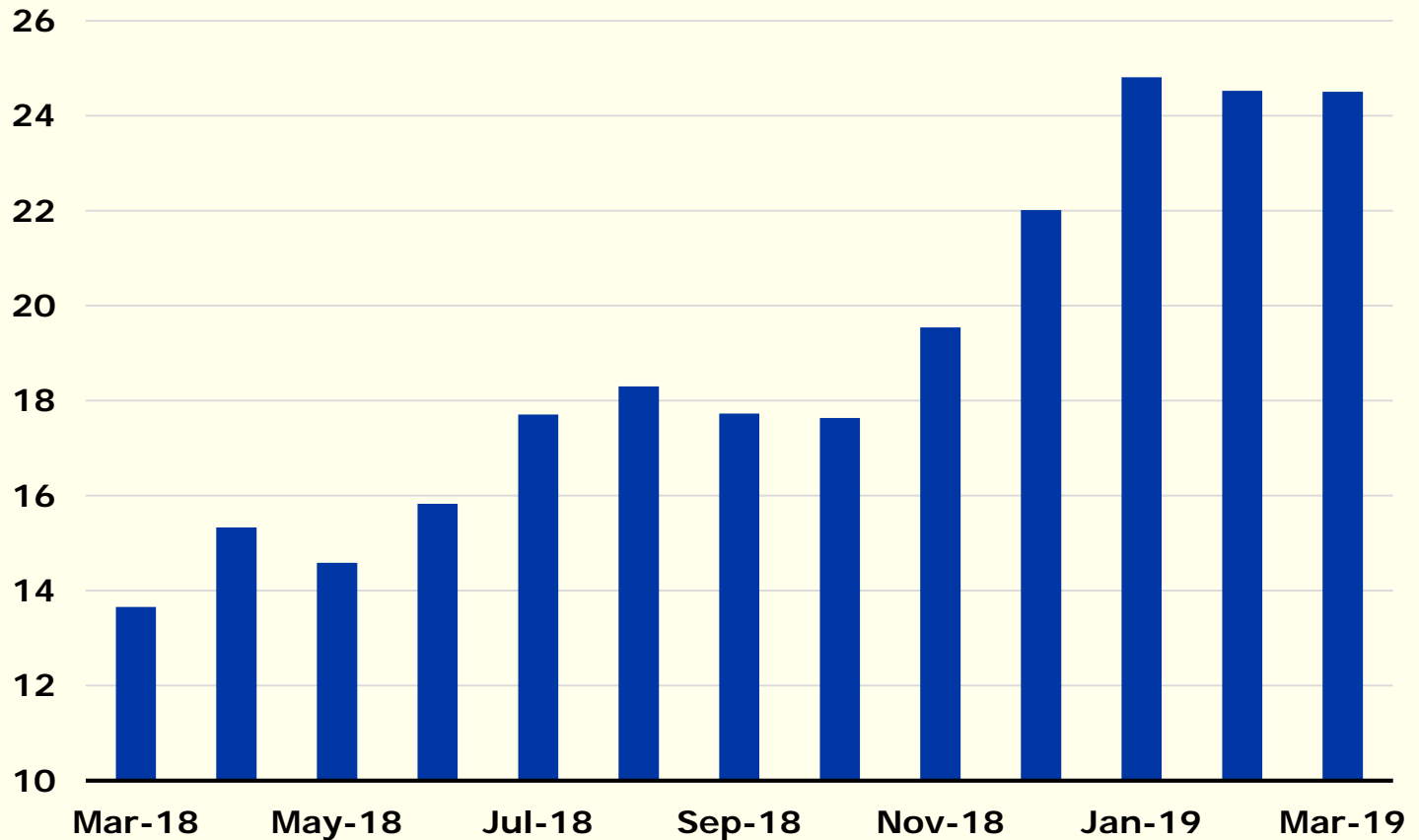
Source: Wall Street Journal economists' survey, data through Mar. 2019

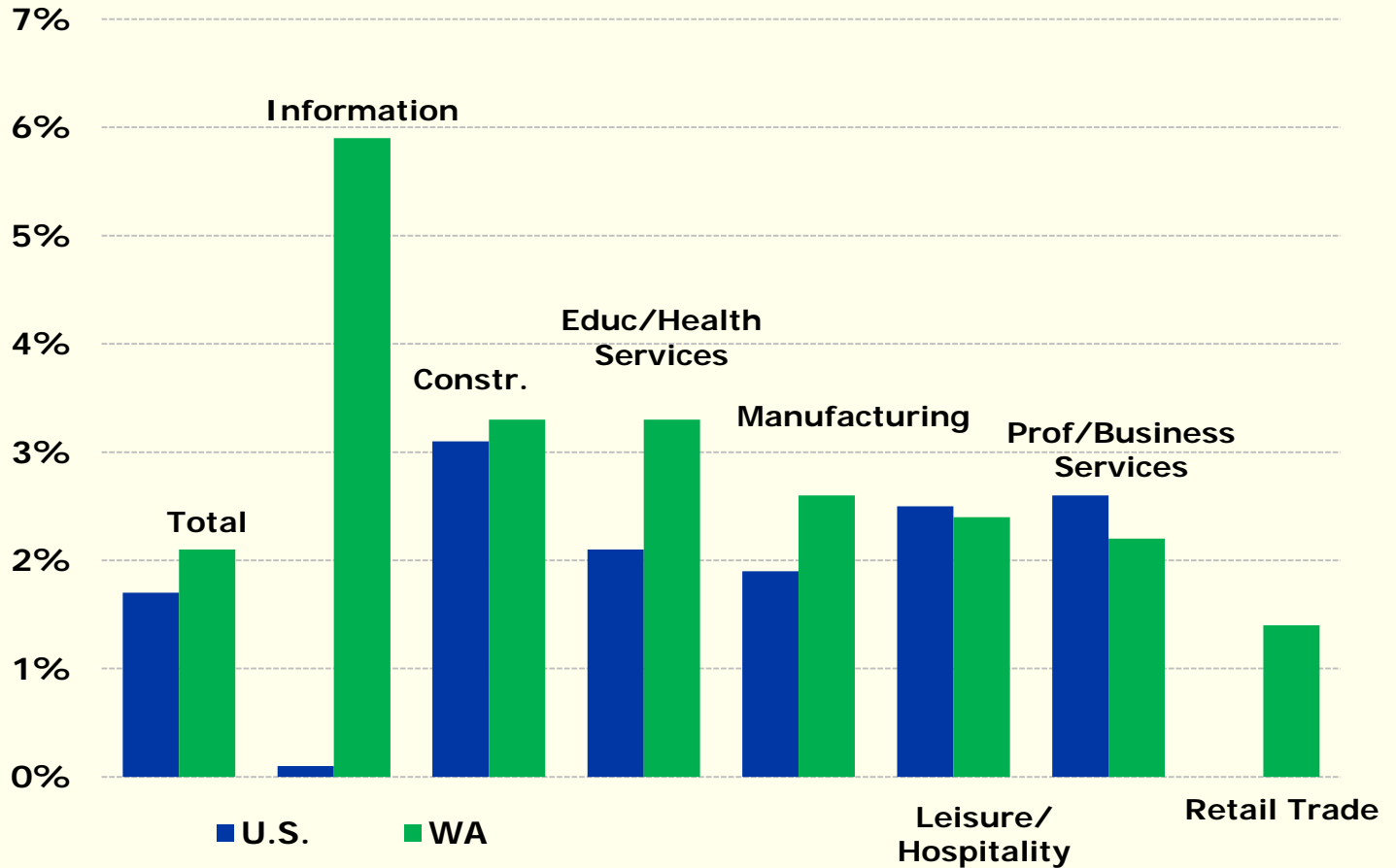# WA personal income growth has outpaced the U.S. in 26 of last 35 quarters

WA personal income growth is expected to average 4.8% per year for 2019 - 2023

U.S. and WA personal income growth

Source: U.S. Bureau of Economic Analysis, data through 2018 Q3

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Relative to population, WA residential construction activity is stronger than the U.S.

Residential building permits per 1,000 population

US — WA
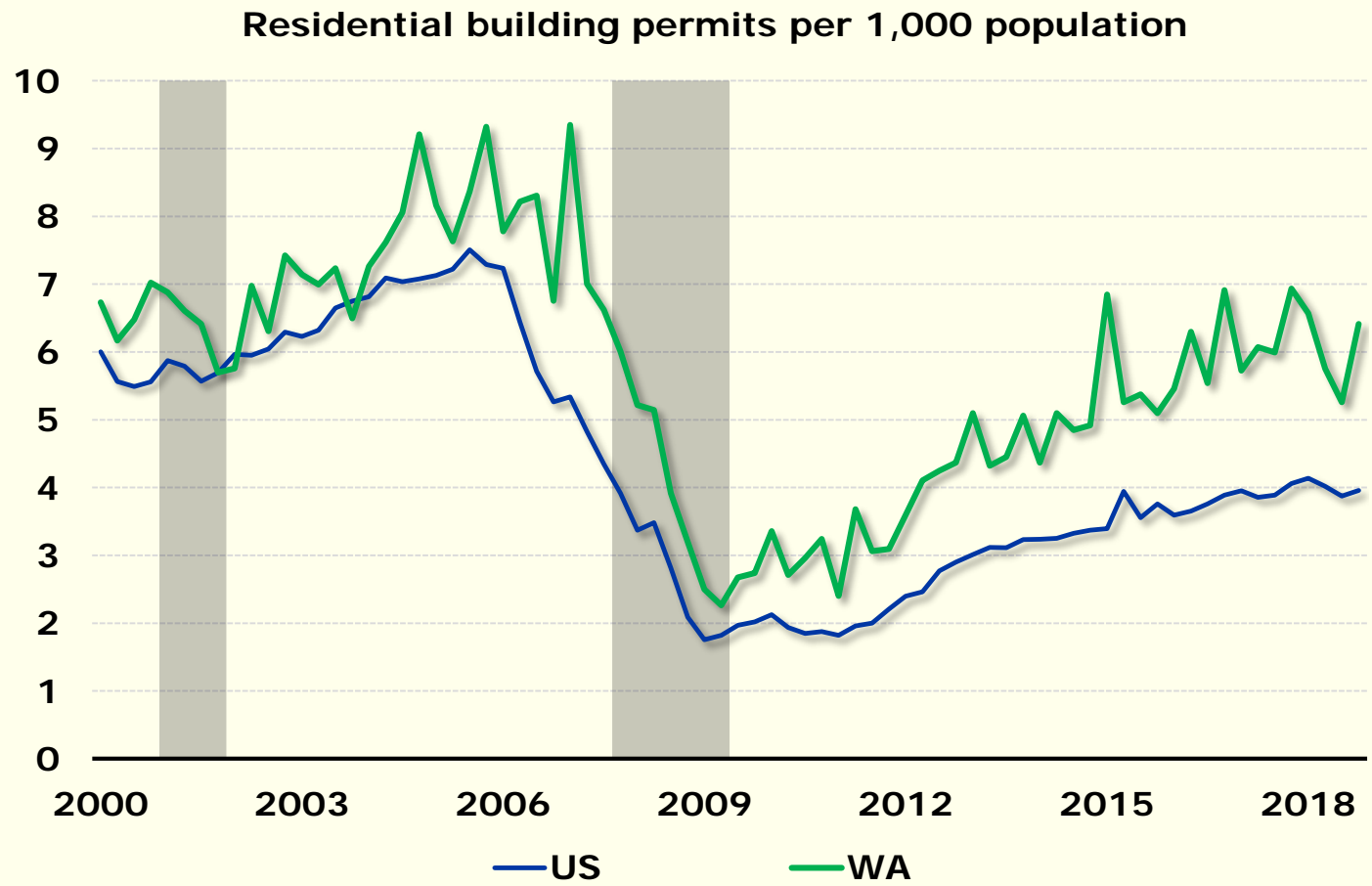
Source: U.S. Census Bureau, ERFC; data through 2018 Q4

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After four consecutive quarters of growth, WA exports declined in the fourth quarter of 2018
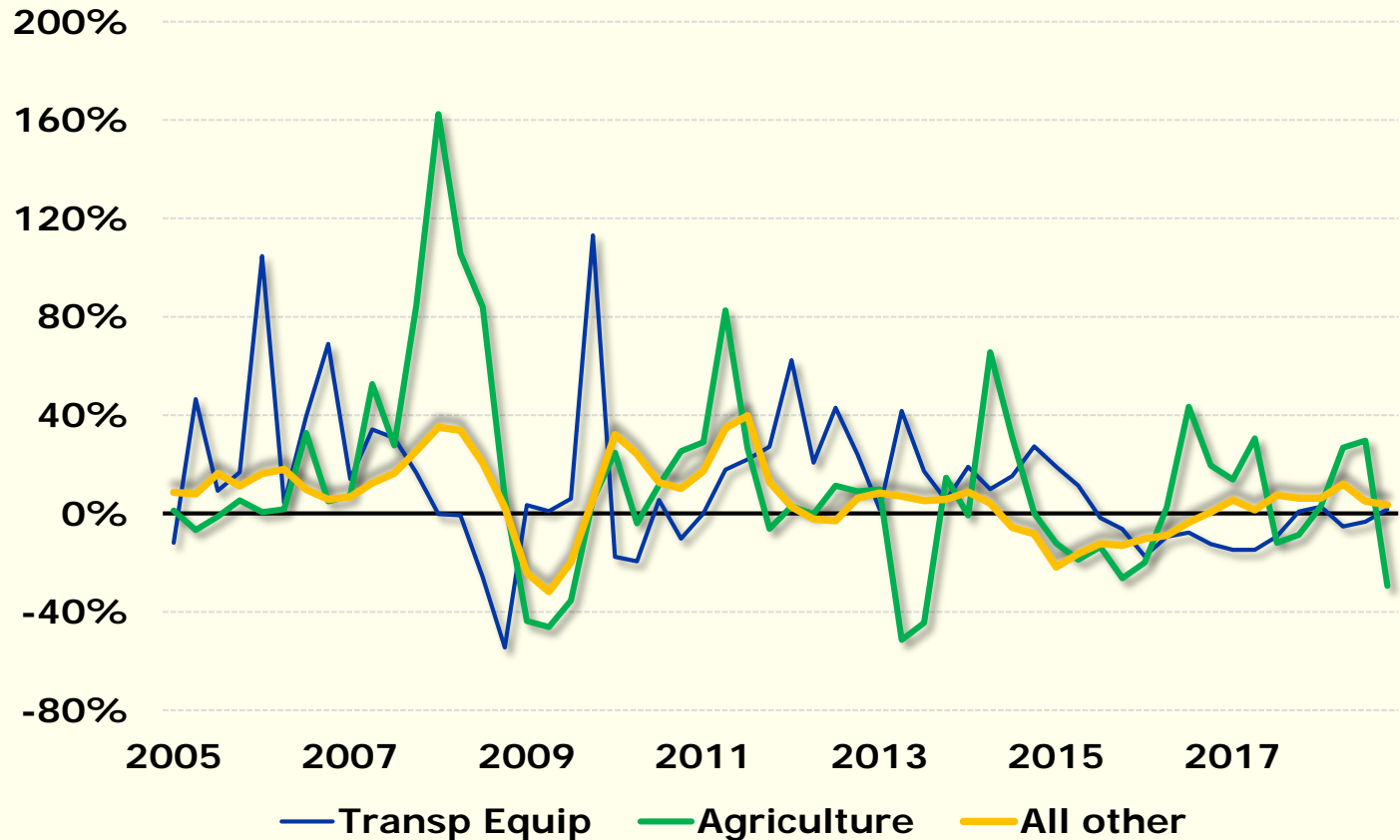
Total Export Growth

2017Q4: 0.6%
2018Q1: 3.9%
2018Q2: 3.7%
2018Q3: 2.6%

2018Q4:
-2.7%

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WA exports, year over year growth

Legend: Transp Equip — Agriculture — All other

Source: WISERTrade; data through 2018 Q4

GDP is slightly lower than in November
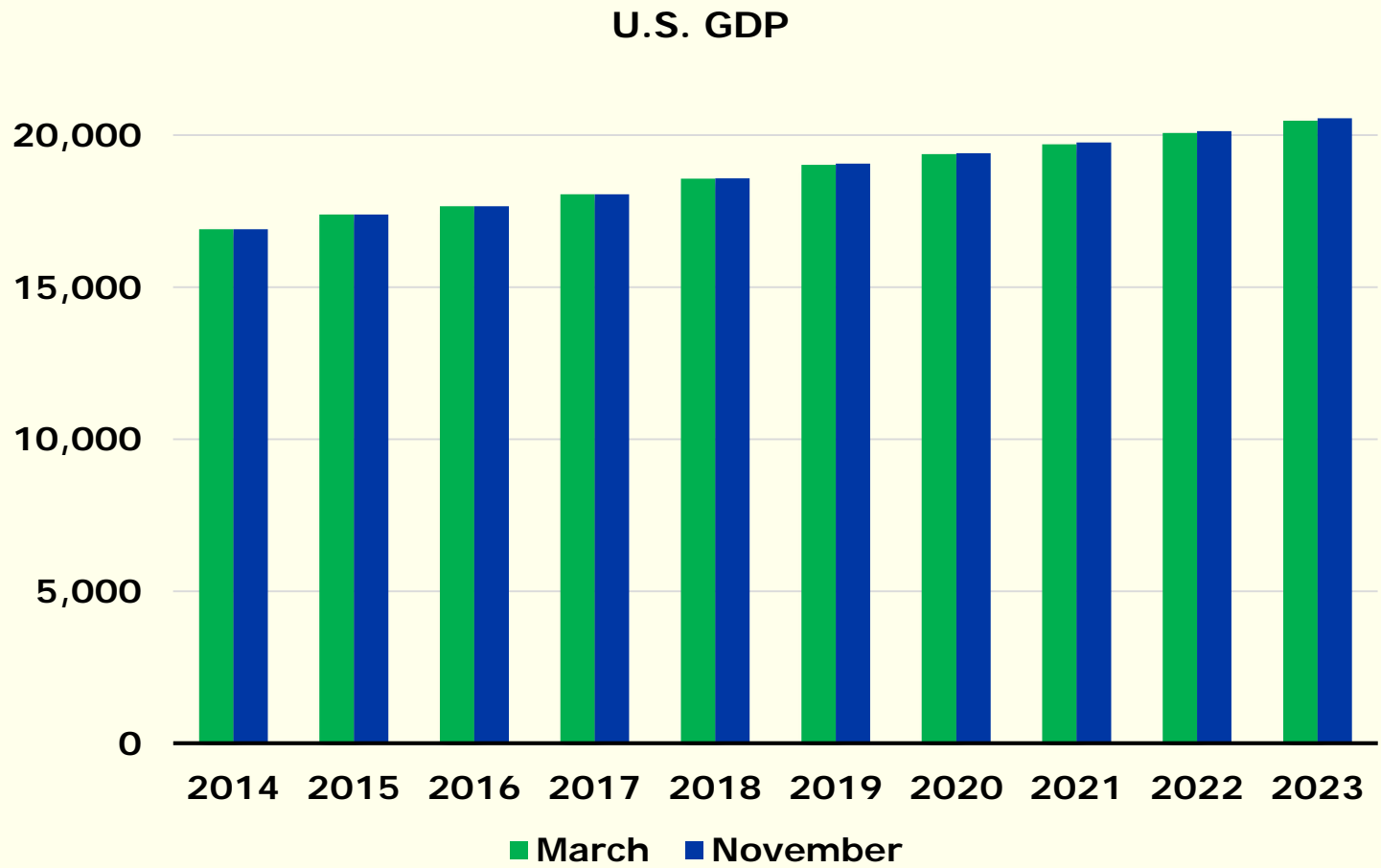
U.S. GDP

Legend: ■ March ■ November

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Washington personal income is slightly lower than in November
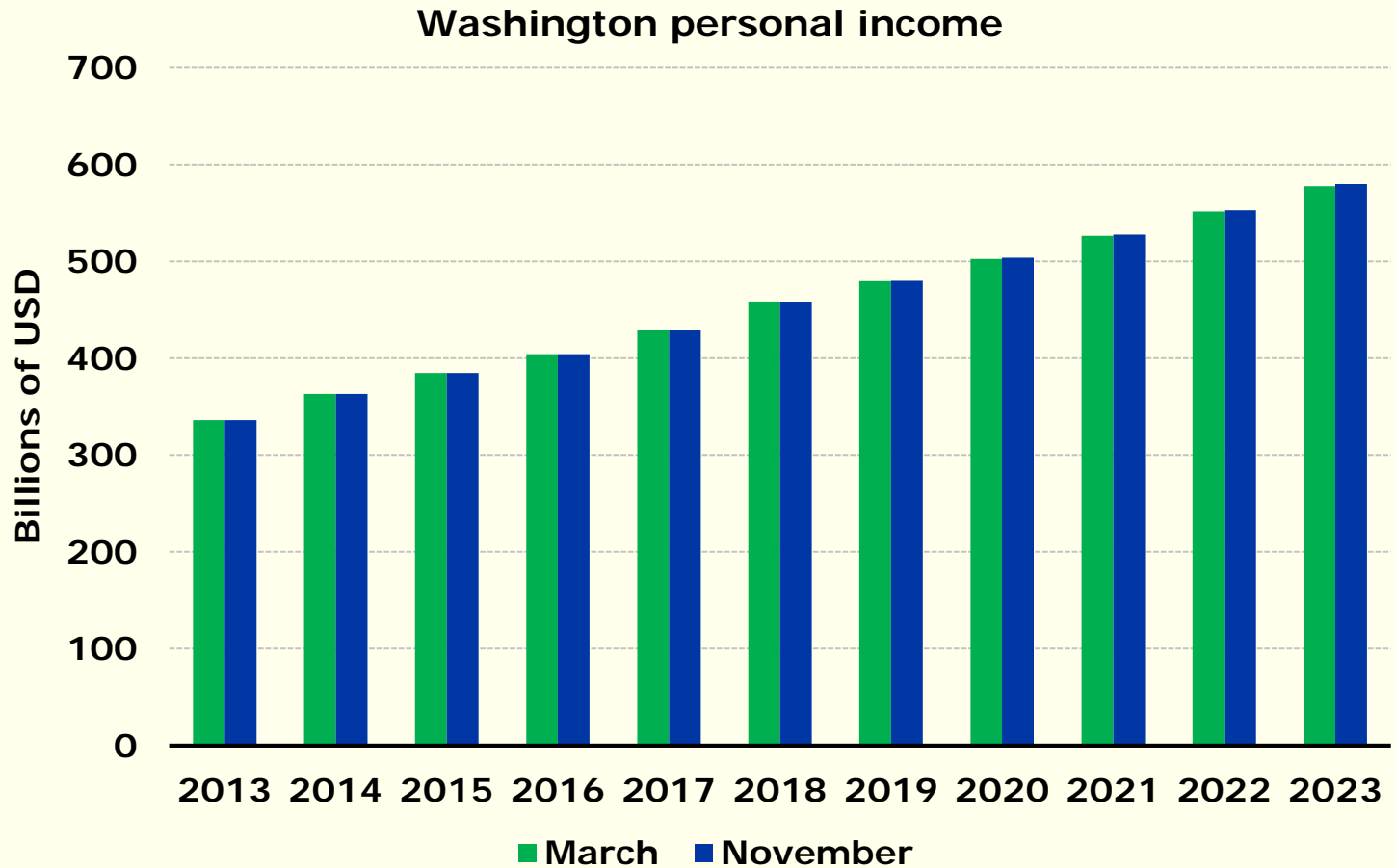
Washington personal income

Source: ERFC March 2019 forecast; historical data through 2017

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WASHINGTON STATE ECONOMIC AND REVENUE FORECAST COUNCIL

Washington employment forecast is slightly lower than in November

Washington Nonfarm Payroll Employment

Forecast →

March   November

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WASHINGTON STATE ECONOMIC AND REVENUE FORECAST COUNCIL

Permits forecast for 2019 – 2023: average unchanged, timing slightly different compared to November

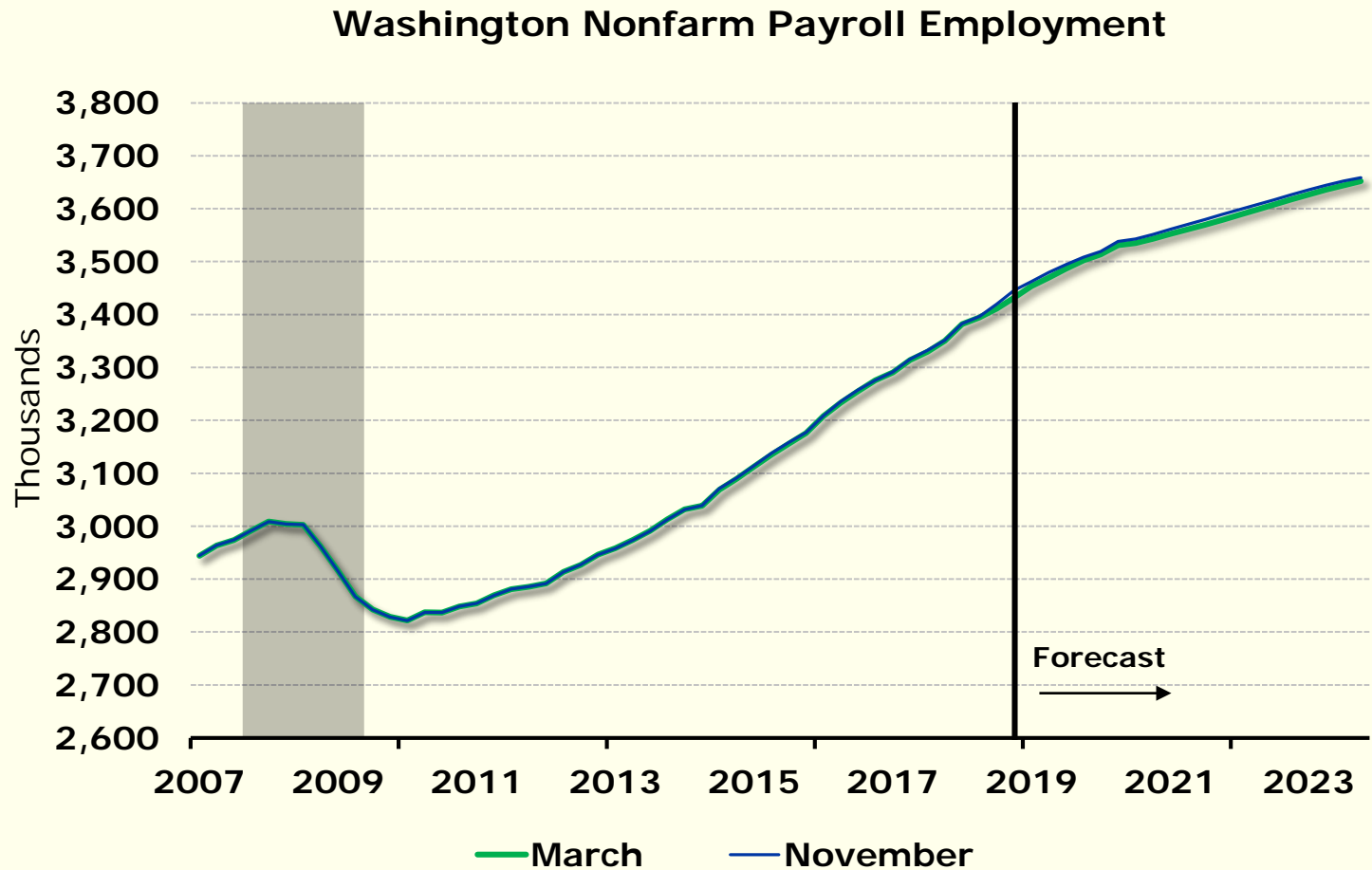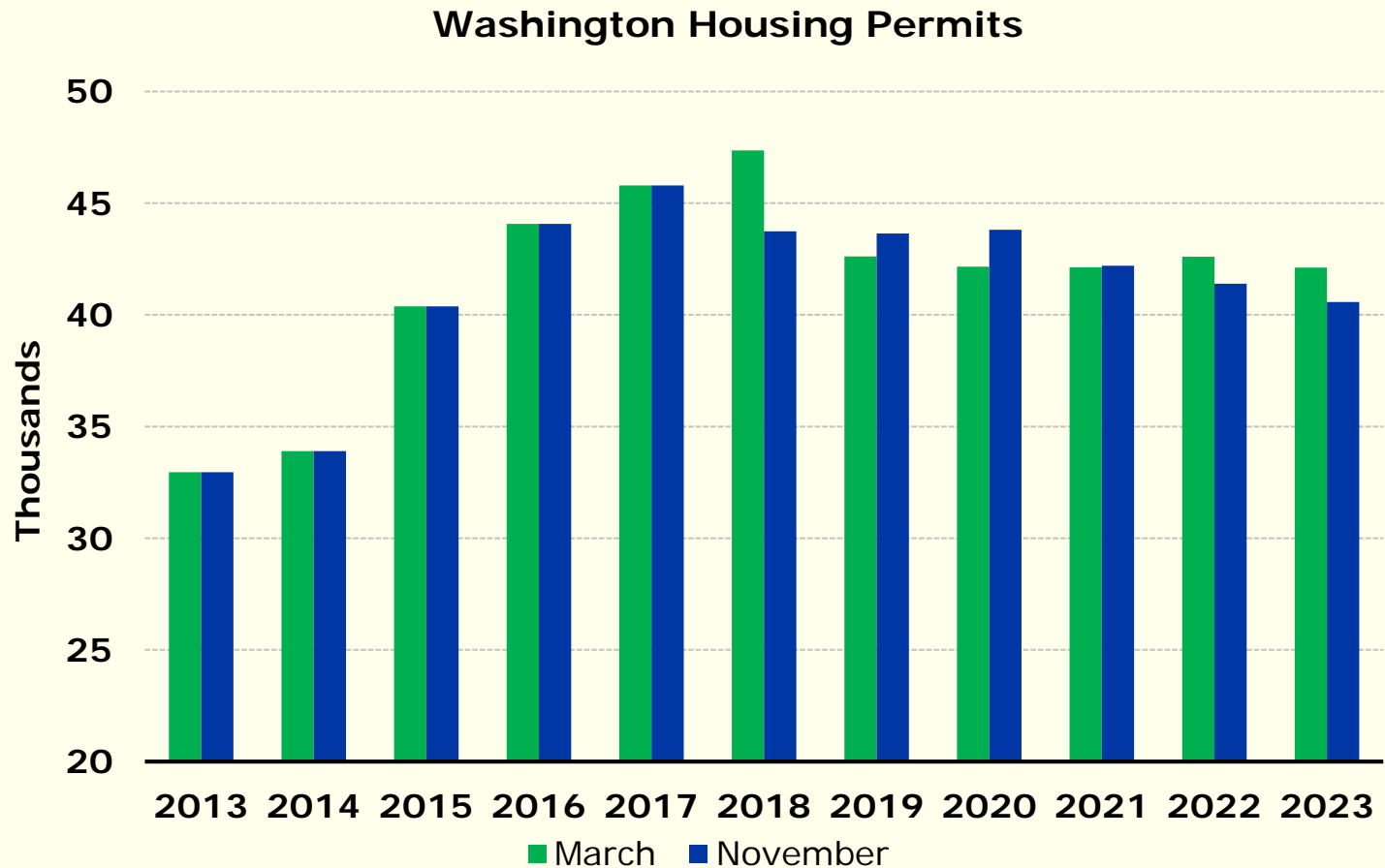
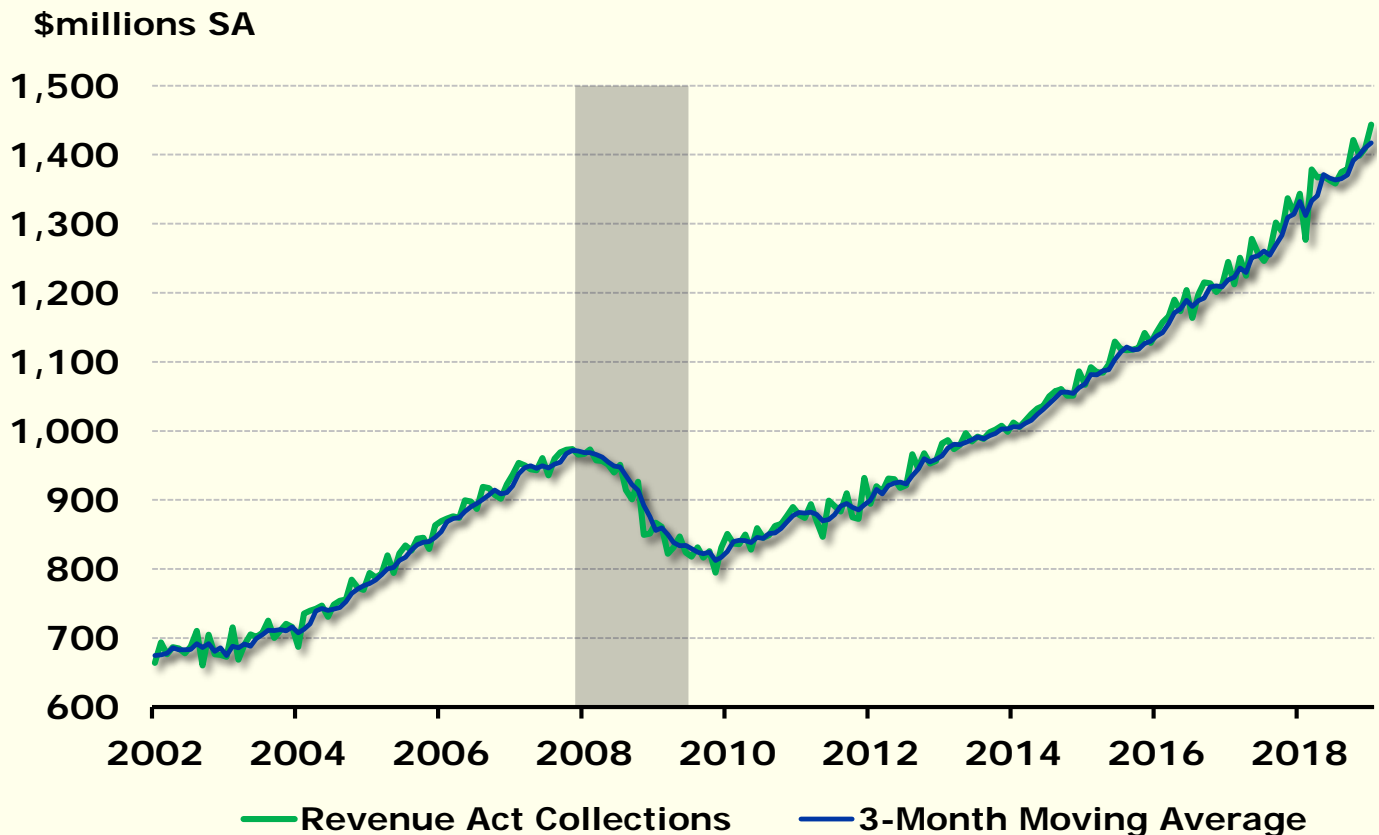Source: ERFC March 2019 forecast; historical data through 2018

WASHINGTON STATE ECONOMIC AND REVENUE FORECAST COUNCIL

Revenue Act collections growth has been strong

$millions SA

Adjusted year-over-year collections growth (by quarter of activity):

2017Q4: 8.3%
2018Q1: 8.2%
2018Q2: 8.8%
2018Q3: 7.6%
2018Q4: 7.4%

Legend: — Revenue Act Collections — 3-Month Moving Average

* Adjusted for large one-time transactions, amnesty payments and reporting frequency change, current definition of Revenue Act
Source: DOR and ERFC; monthly data through January 2019 activity

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WASHINGTON STATE ECONOMIC AND REVENUE FORECAST COUNCIL

Taxable REET activity declined in February but remained strong

There were $1.0 billion in large commercial sales (>$10 million) in February, down from $1.87 billion in January.

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Seasonally Adjusted Taxable Real Estate Excise Activity

$Billions

Legend:
— Total
— Total excl. sales >$10M
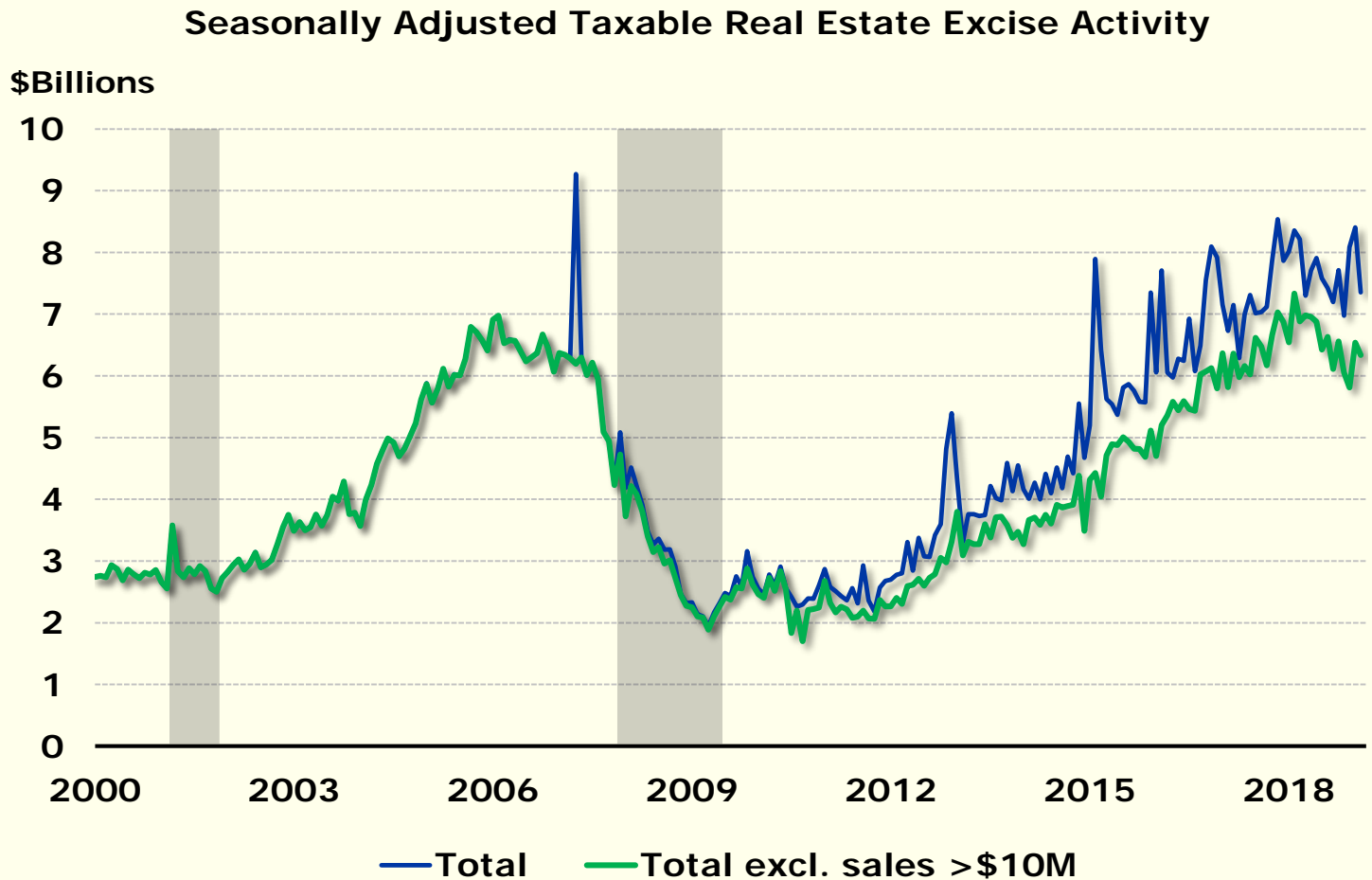
Source: ERFC; Monthly data through February 2019 preliminary

WASHINGTON STATE ECONOMIC AND REVENUE FORECAST COUNCIL

Assessed value on existing properties increased between November, March forecasts
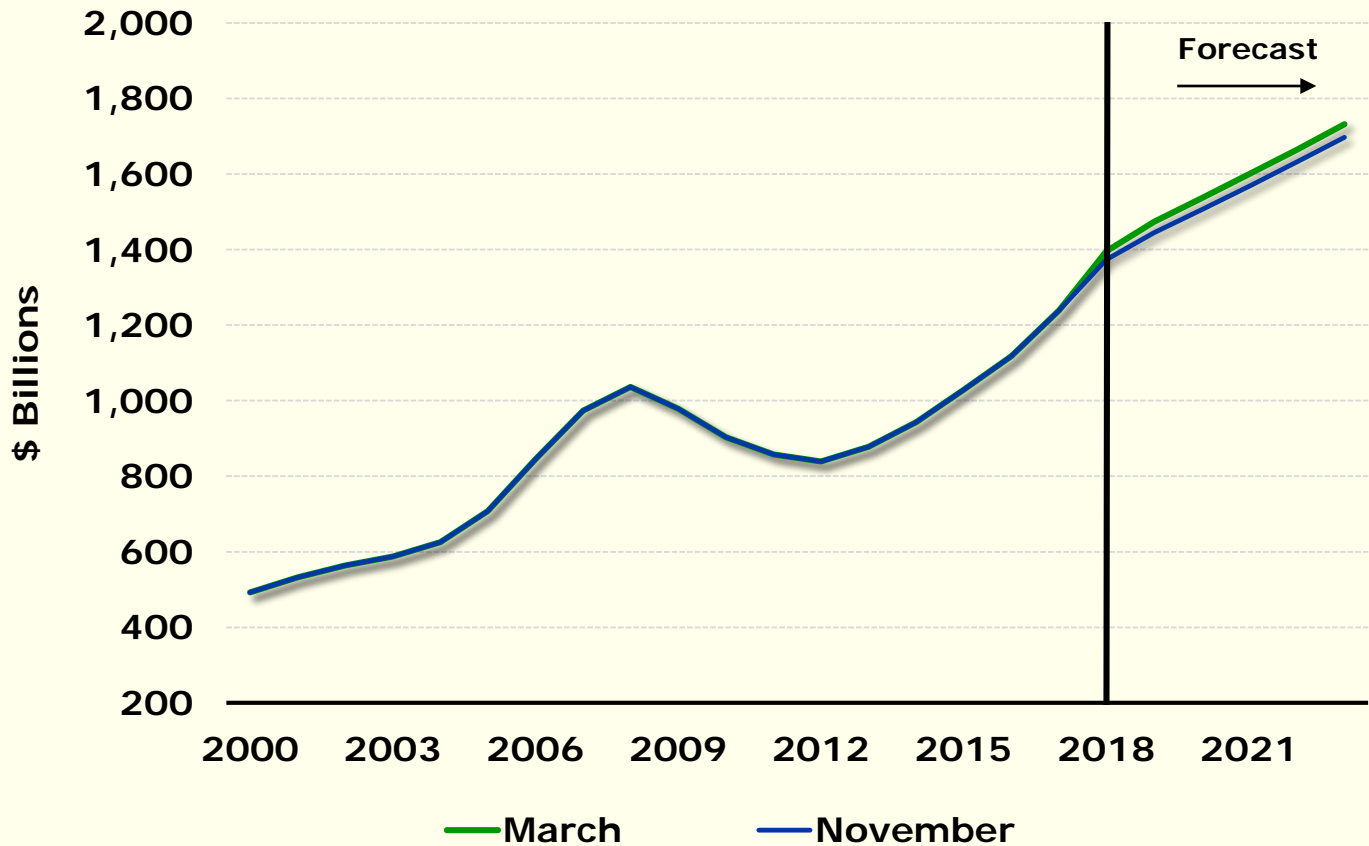
November forecast for growth in Market Value: 10.9%

Actual growth: 12.6%

Every 1.0 percentage point increase in Market Value growth adds between $30-$40 million in revenue per year

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$ Billions

Forecast →

2,000
1,800
1,600
1,400
1,200
1,000
800
600
400
200

2000 2003 2006 2009 2012 2015 2018 2021

━━ **March**   ━━ **November**

Source: ERFC March 2019 forecast; historical data through 2018

WASHINGTON STATE ECONOMIC AND REVENUE FORECAST COUNCIL

Cannabis revenue growth is expected to moderate

Retail Cannabis Collections

Millions

Forecast — Actual
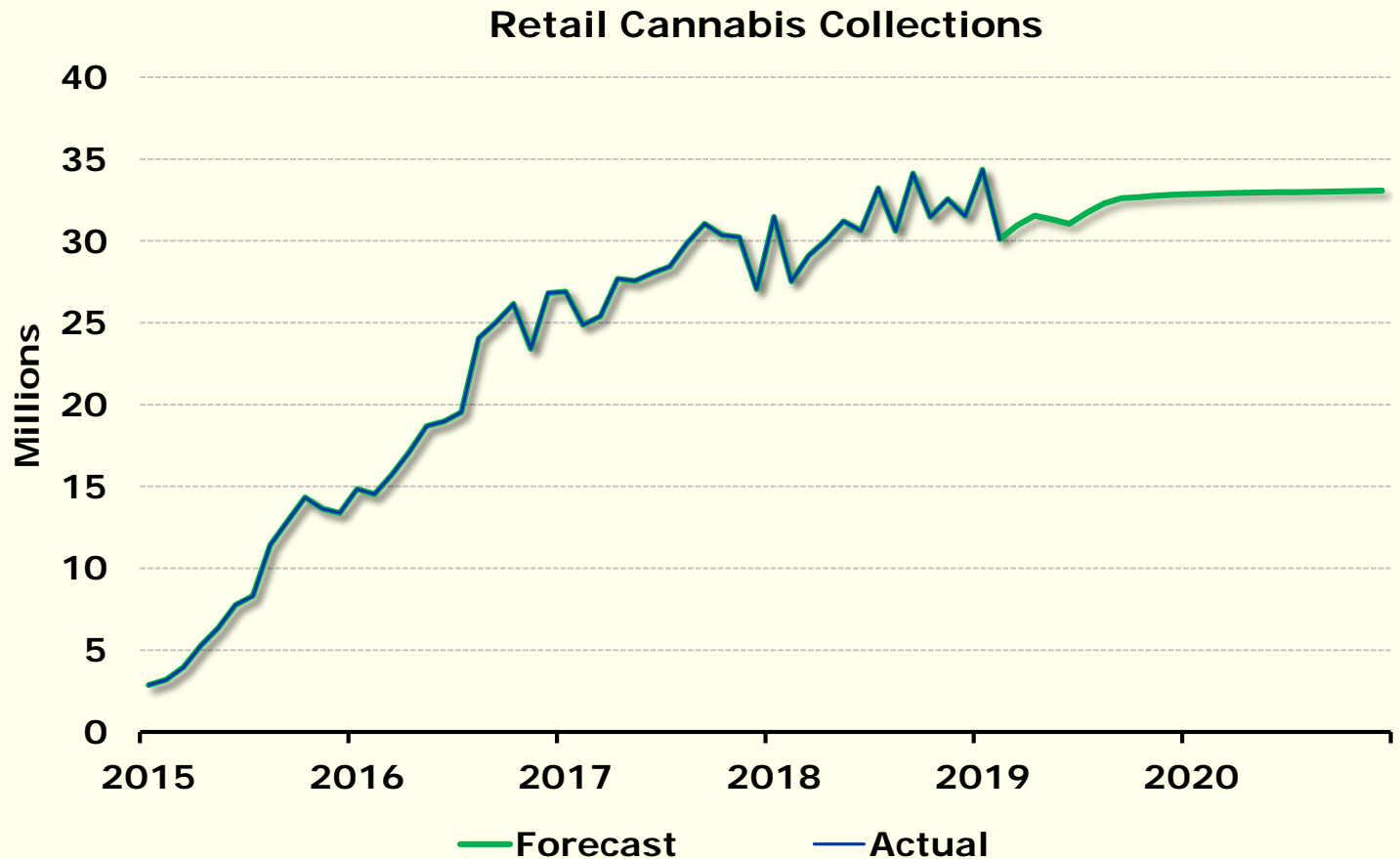
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Source: ERFC March 2019 forecast; historical data through February 2019

WASHINGTON STATE ECONOMIC AND REVENUE FORECAST COUNCIL

Cannabis excise tax and license fee estimates

Total change
since November
forecast:

• 2017-19
+$0.02M

• 2019-21
+$1.67M

• 2021-23
-$2.85M

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$Millions

	Cannabis Forecast		
	2017-19	**2019-21**	**2021-23**
GF-S share of excise tax and license fees	$247	$272	$291
Non-GF	$501	$527	$545
Total	**$749**	**$799**	**$836**

* Detail may not add to total due to rounding

WASHINGTON STATE ECONOMIC AND REVENUE FORECAST COUNCIL

Forecast changes: Near General Fund-State, 2017-2019 biennium

As of March 11, General Fund-State collections were $245.0 million higher than the November forecast.

$Millions	November 2018 Forecast*	Non-economic Change	Forecast Change	March 2019 Forecast	Total Change#
General Fund-State	$43,926	$0	$256	$44,182	$256
Education Legacy Trust Account	$1,591	$0	$51	$1,642	$51
WA Opportunity Pathways Account	$282	$0	$0.2	$282	$0.2
Total Near GF-S	**$45,799**	**$0**	**$307**	**$46,106**	**$307**

* Forecast for the 2017-19 biennium adopted November 20, 2018
# Detail may not add to total due to rounding

WASHINGTON STATE ECONOMIC AND REVENUE FORECAST COUNCIL

Forecast changes: Near General Fund-State, 2019-2021 biennium

$Millions	November 2018 Forecast*	Non-economic Change	Forecast Change	March 2019 Forecast	Total Change#
General Fund-State	$49,064	$115	$430	$49,609	$545
Education Legacy Trust Account	$672	$0	$1	$673	$1
WA Opportunity Pathways Account	$266	$0	$8	$274	$8
Total Near GF-S	**$50,002**	**$115**	**$439**	**$50,555**	**$553**

* Forecast for the 2019-21 biennium adopted November 20, 2018
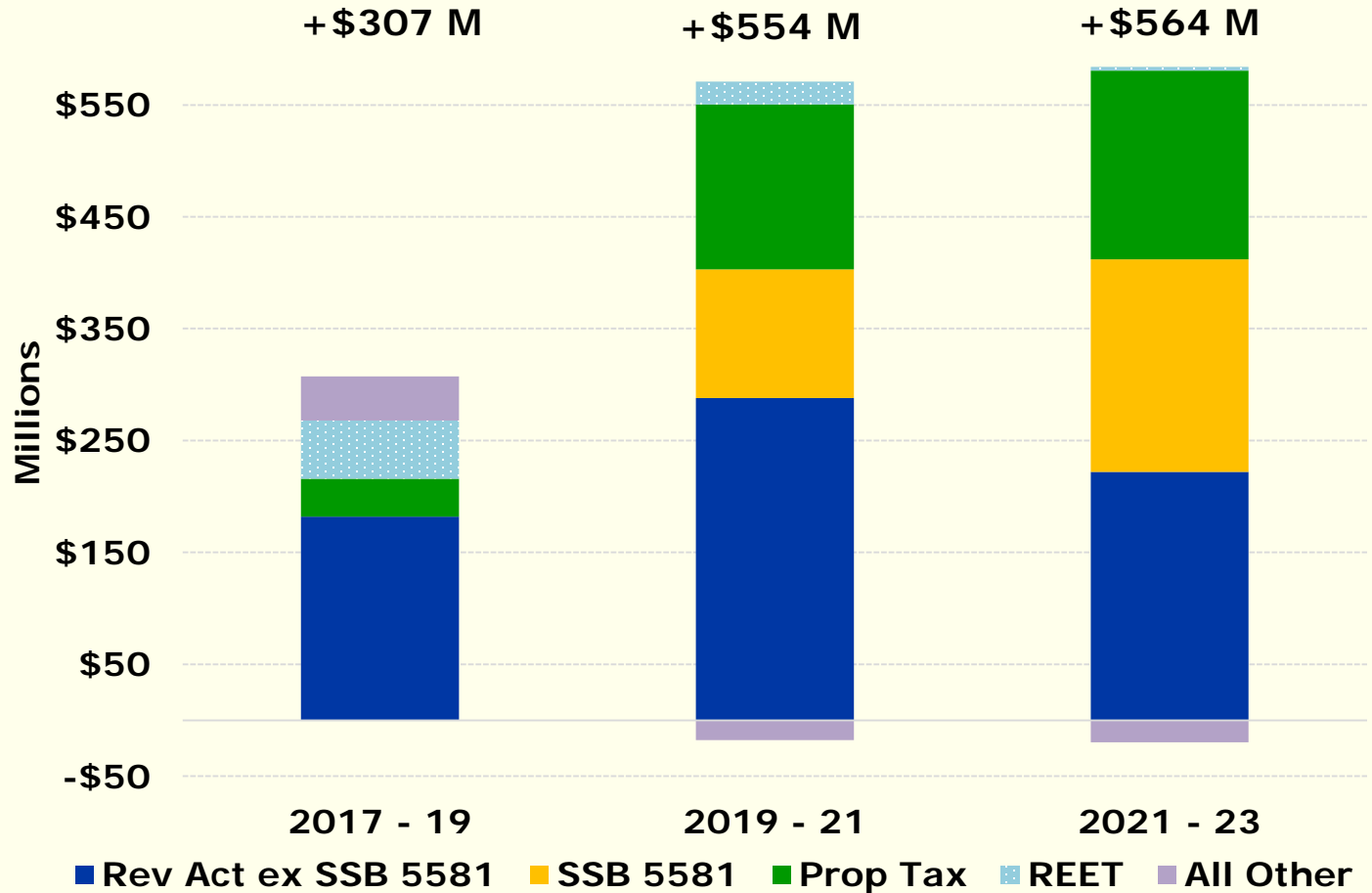\# Detail may not add to total due to rounding

WASHINGTON STATE ECONOMIC AND REVENUE FORECAST COUNCIL

Near GF-S forecast changes by source

+$307 M   +$554 M   +$564 M

Millions

$550
$450
$350
$250
$150
$50
-$50

2017 - 19   2019 - 21   2021 - 23

■ Rev Act ex SSB 5581   ■ SSB 5581   ■ Prop Tax   ■ REET   ■ All Other

Source: ERFC March 2019 forecast

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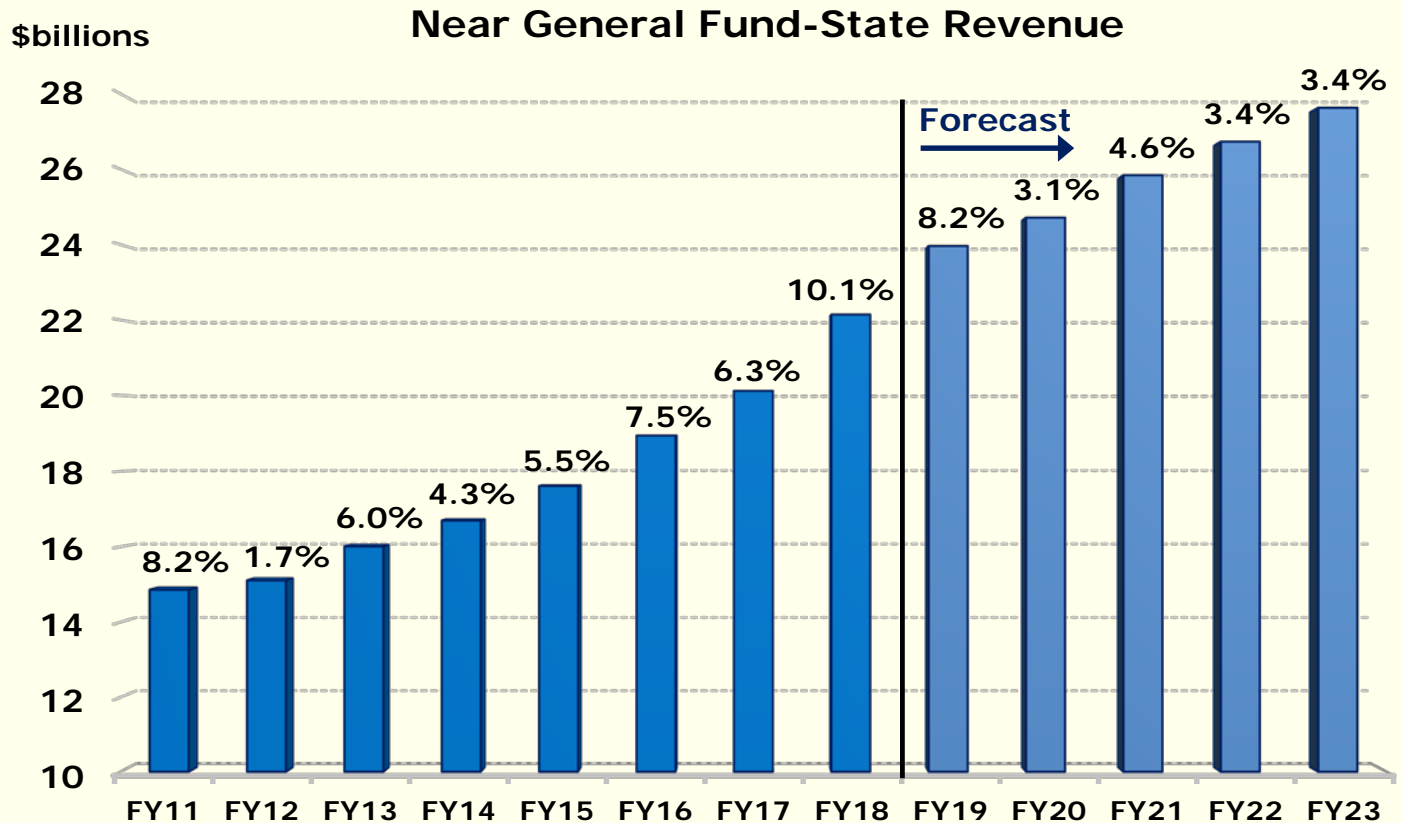
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2017-19 Biennium alternative General Fund-State forecasts

$Millions (cash basis)	2017-19 Biennium	Difference From the baseline#
March 2019 Baseline (70%)	**$44,182**	
March 2019 Alternative Forecasts		
Optimistic (15%)	**$44,413**	**$231**
Pessimistic (15%)	**$43,938**	**($243)**
Probability Weighted Average	**$44,180**	**($2)**
GCEA*	**$44,198**	**$17**

*Based on the Governor's Council of Economic Advisors' economic assumptions
#May not add to total due to rounding

WASHINGTON STATE ECONOMIC AND REVENUE FORECAST COUNCIL

Conclusion

- Economic forecasts are only slightly changed from November

- Washington's economy is continuing to outperform the nation but not as dramatically as in past

- GF-S revenues are expected to grow 15.3% between the 2015-17 and 2017-19 biennia and 12.3% between the 2017-19 and 2019-21 biennia

- The level of uncertainty in the baseline remains elevated, with downside risks outweighing upside risks

Questions

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