

Revenue Review

Presented to
Economic and Revenue Forecast Council

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June 19, 2018
Olympia, Washington



**WASHINGTON STATE
ECONOMIC AND REVENUE FORECAST COUNCIL**



Summary

- The economic forecast for the U.S. is slightly stronger than in February.
- The economic forecast for WA has slightly higher personal income than in February.
- Risks to the baseline include concerns about international trade, geopolitical risks and a maturing economic expansion.
- The revenue collection variance since the February forecast is \$189 million.
- Near General Fund revenue for the 2017-19 biennium has been increased by \$298 million, and revenue for the 2019-21 biennium has been increased by \$287 million.



Forecast risks

Upside

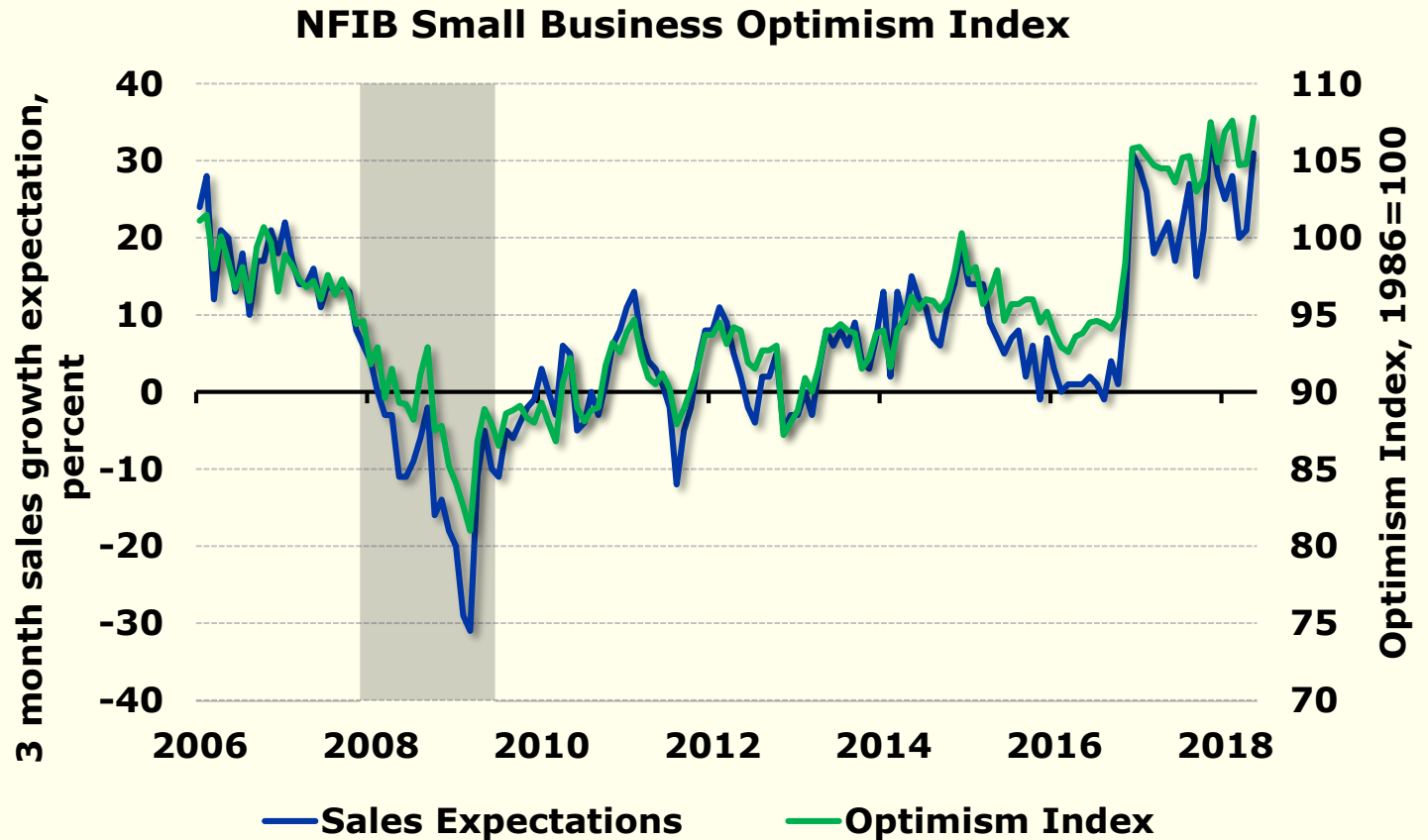
- Strong labor market
- Elevated consumer and business confidence

Downside

- International trade policy uncertainty
- Higher oil and gasoline prices
- Maturing economic expansion
- Federal Reserve raises rates too much or too quickly
- Geopolitical risks: North Korea, Russia, Middle East, Europe



Small business optimism and sales expectations are above pre-recession levels

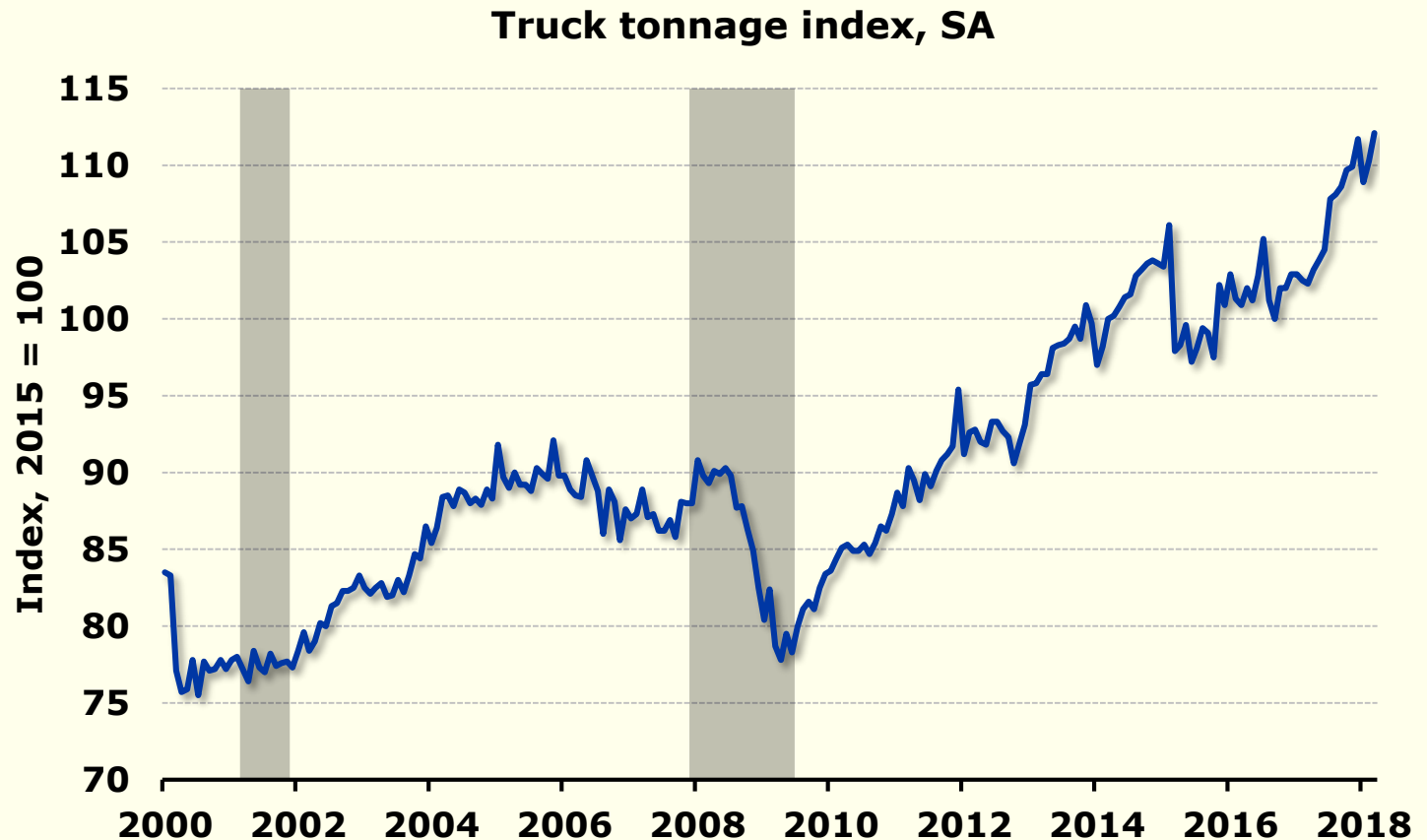


Source: National Federation of Independent Business; data through May 2018

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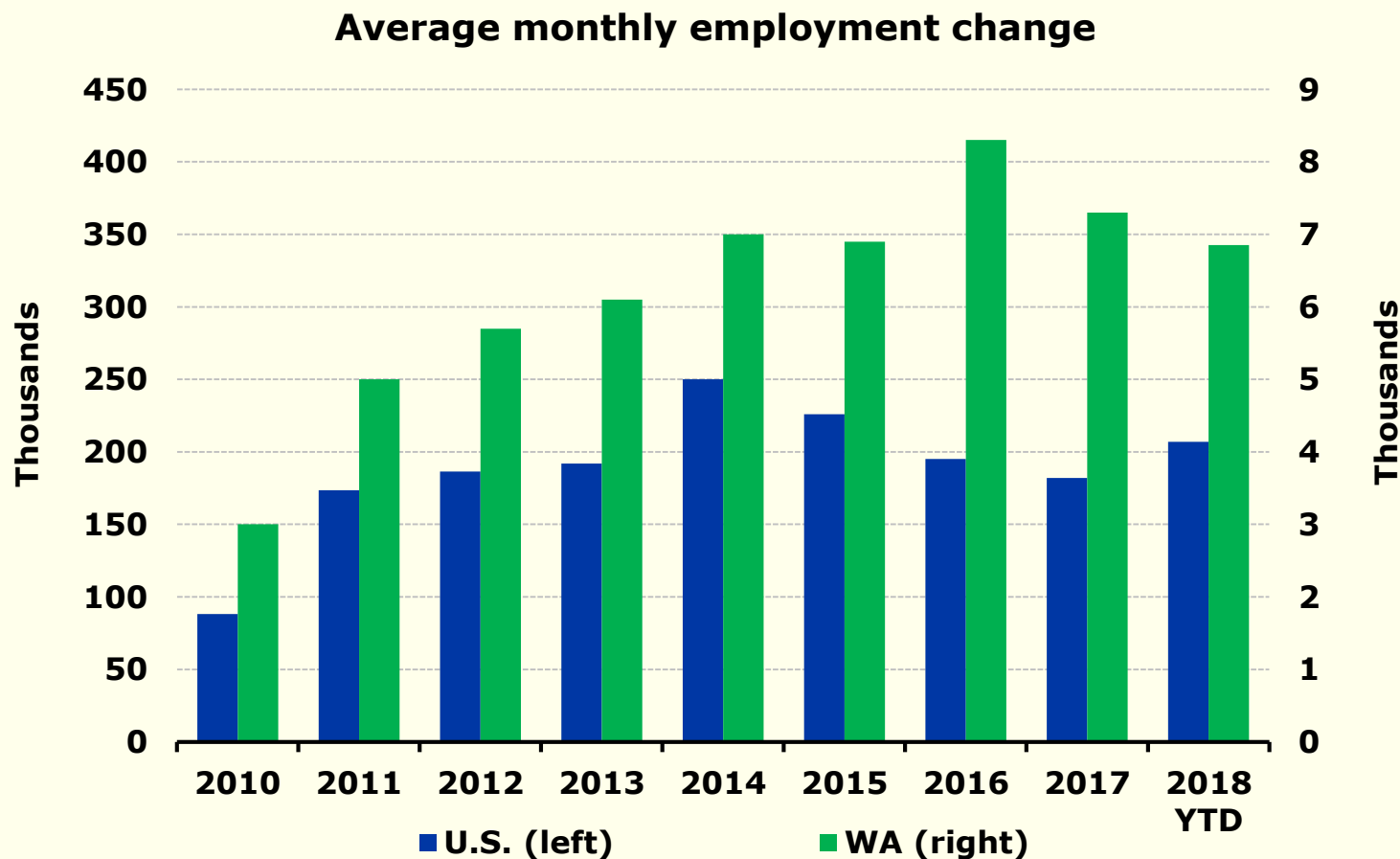


Freight carried by trucks has steadily increased since the end of the recession





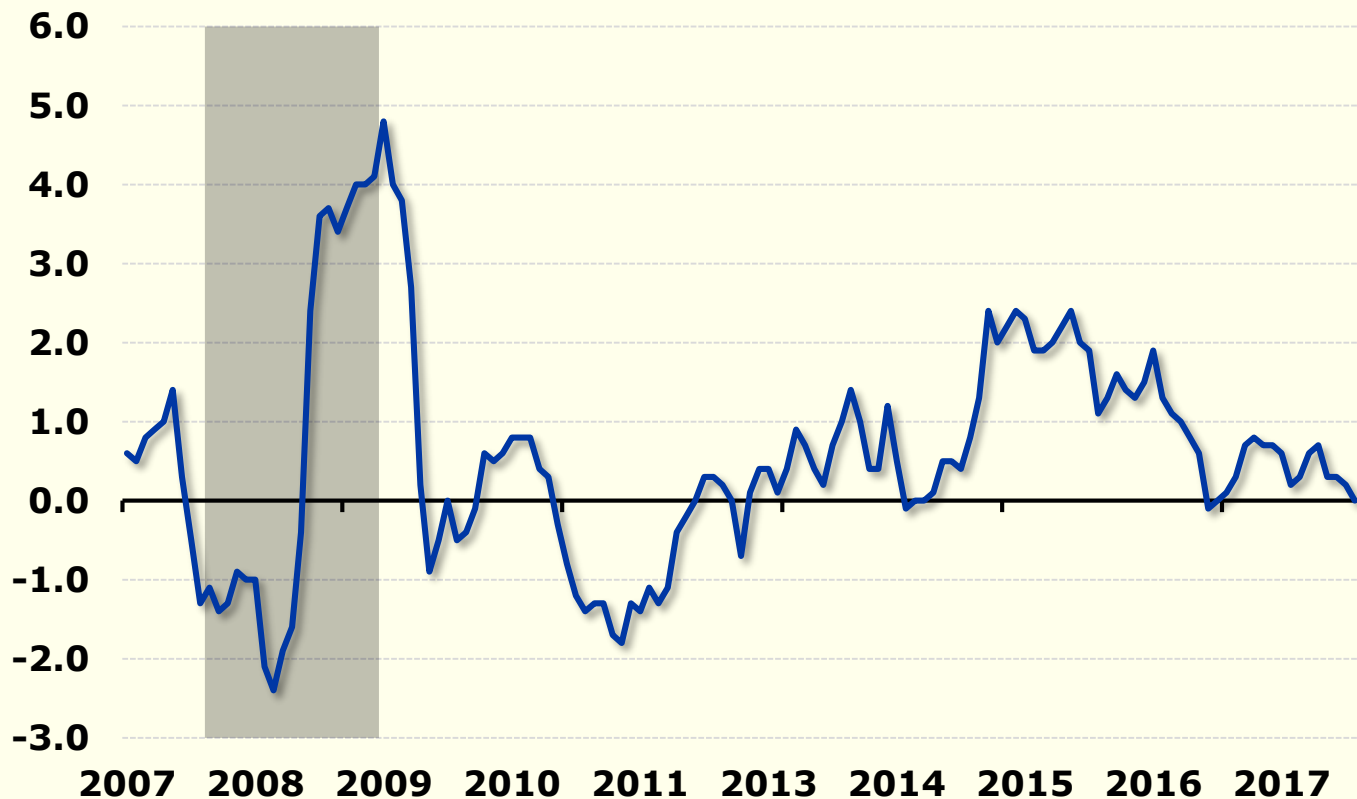
U.S., WA labor markets look strong





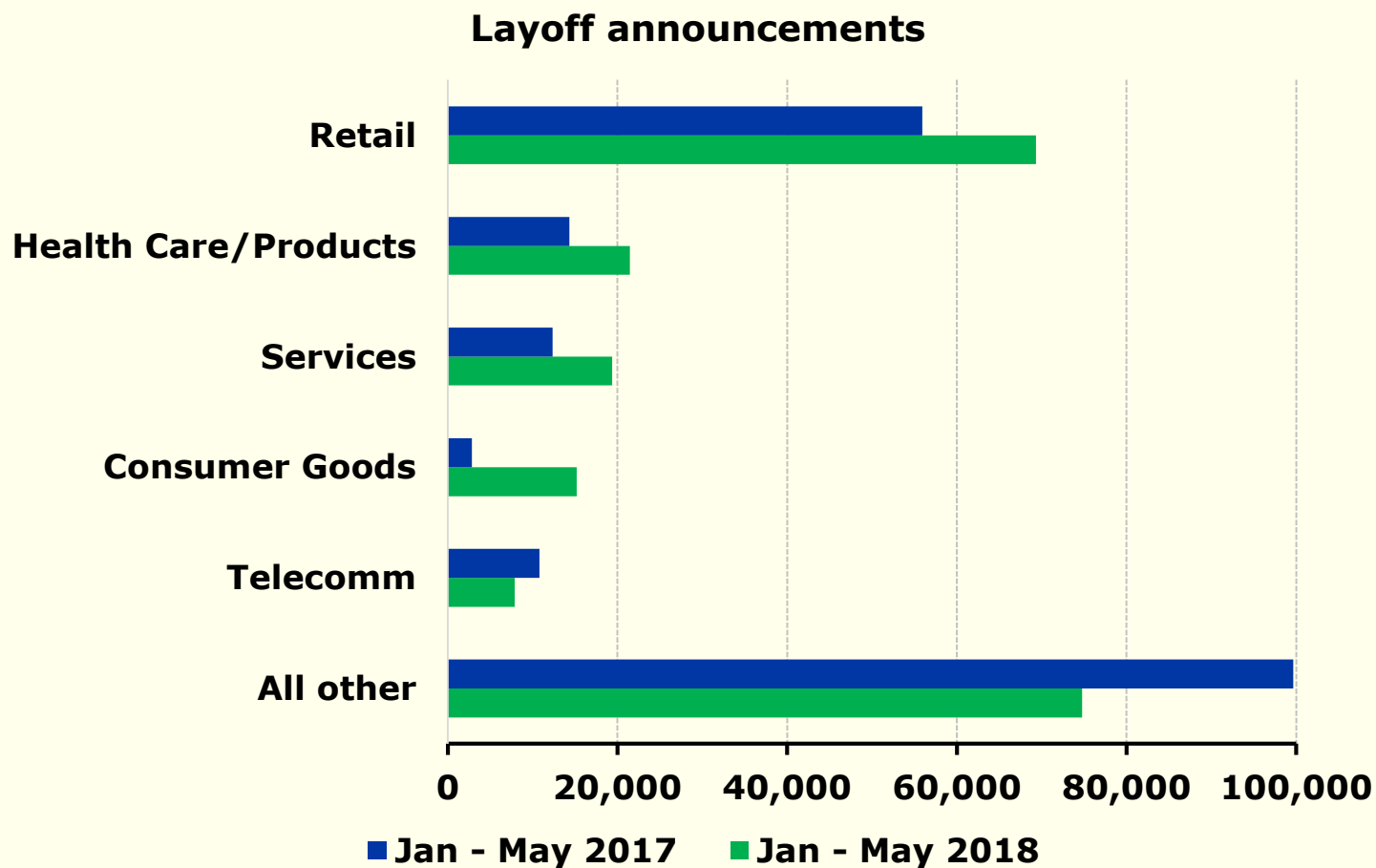
Adjusted for inflation, hourly wage growth remains muted

Year-over-year growth in U.S. real average hourly wages





Through May, layoff announcements are 6% above the same time period last year



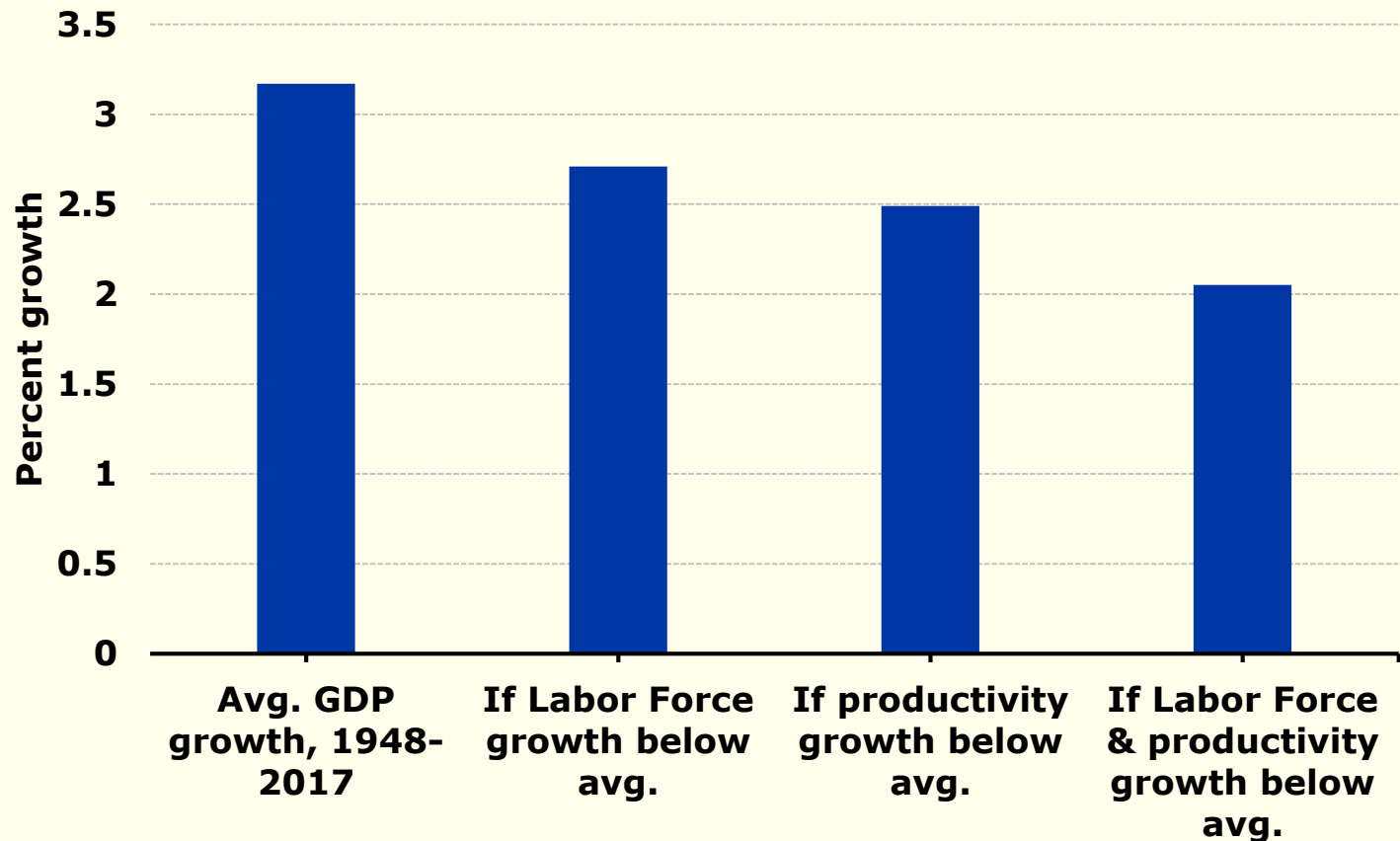
Source: Challenger, Gray & Christmas; Job Cut Report, May 2018

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Both labor force growth and labor productivity growth have been below average for last seven years

Labor force growth will remain below its 1948-2017 average in our forecast; productivity growth is very difficult to forecast



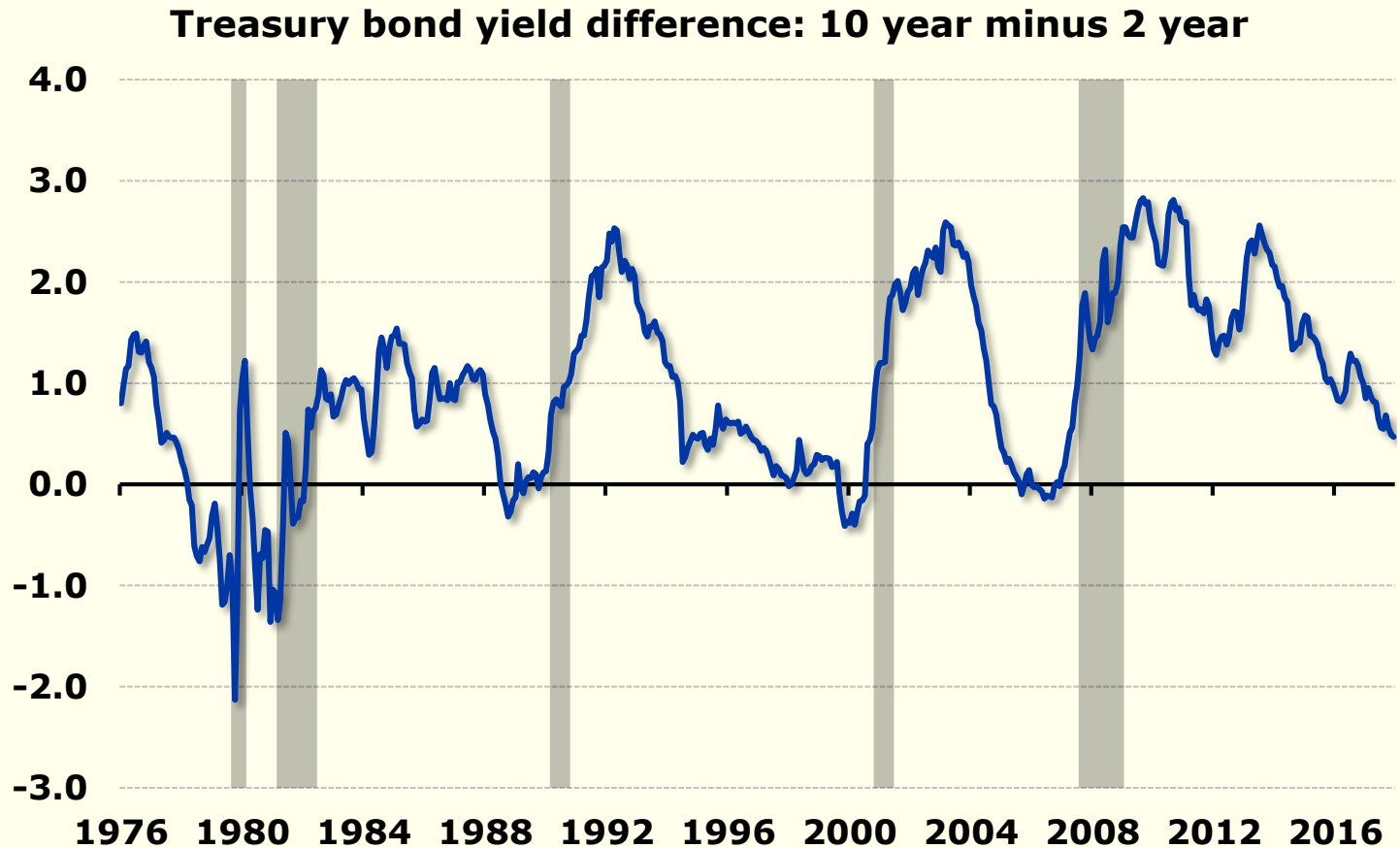
Source: U.S. Bureau of Labor Statistics, U.S. Bureau of Economic Analysis, data through 2017

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When long-term interest rates are below short-term rates, it is often a signal of coming recession

When long-term rates are below short-term rates, this is referred to as an inverted yield curve



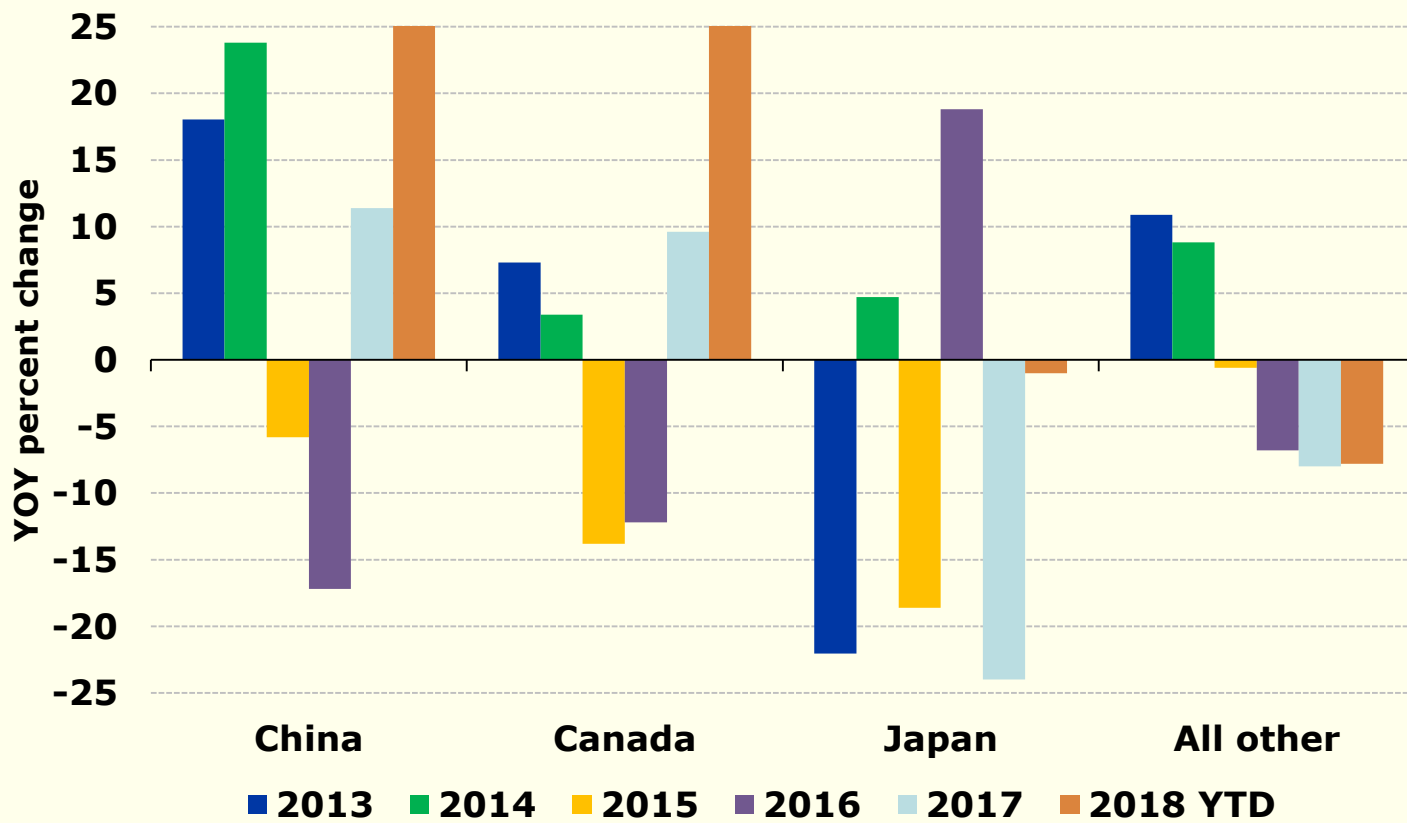
Source: Federal Reserve Bank of St. Louis, monthly data through May 2018



WA exports have slowed, but exports to China, Canada improved in 2017

Total exports declined 3.9% in 2017 but increased 0.6% in fourth quarter 2017 and 3.9% in first quarter 2018

Year-over-year growth in export value, major trading partners

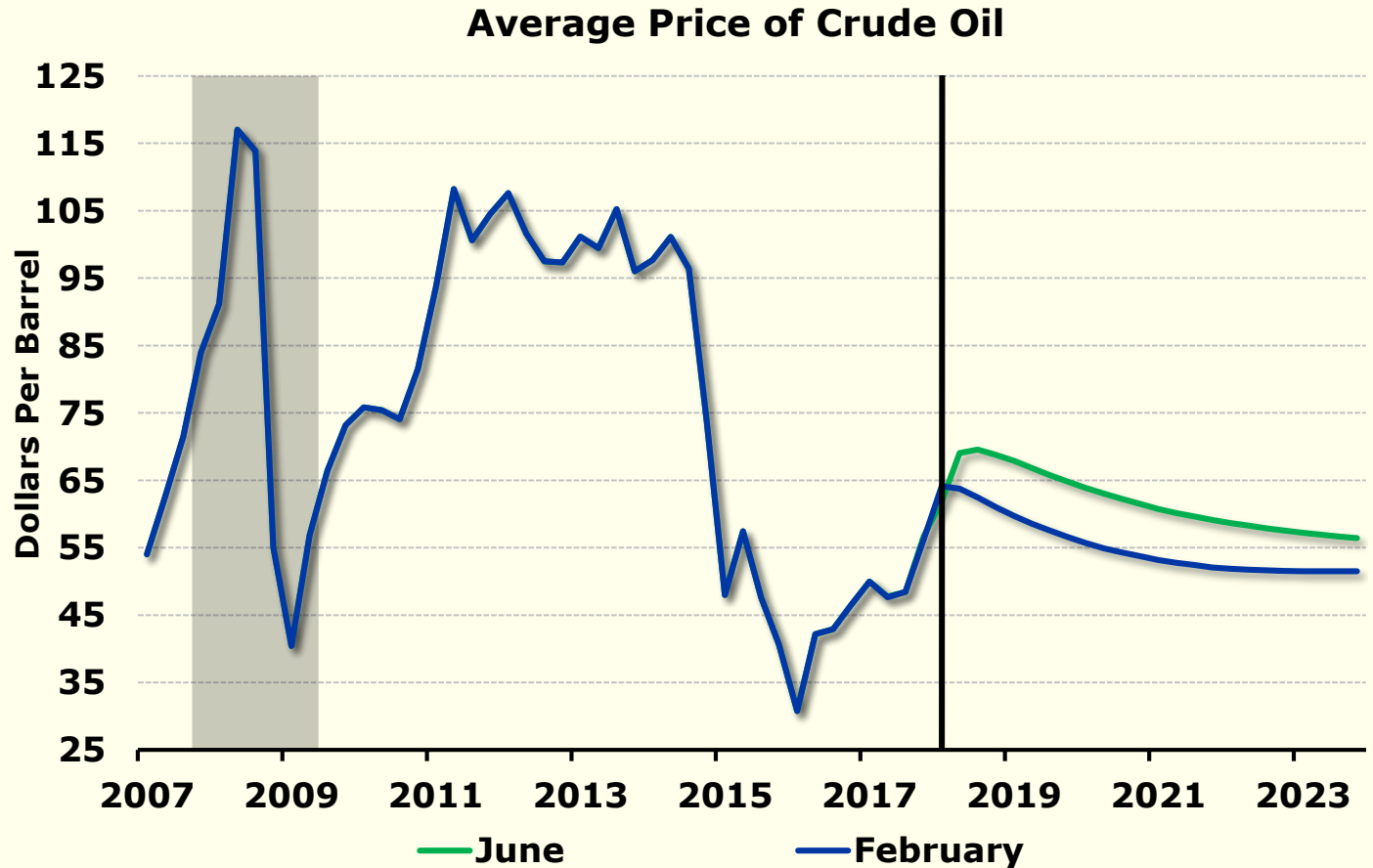


Source: WISERTrade; data through March 2018

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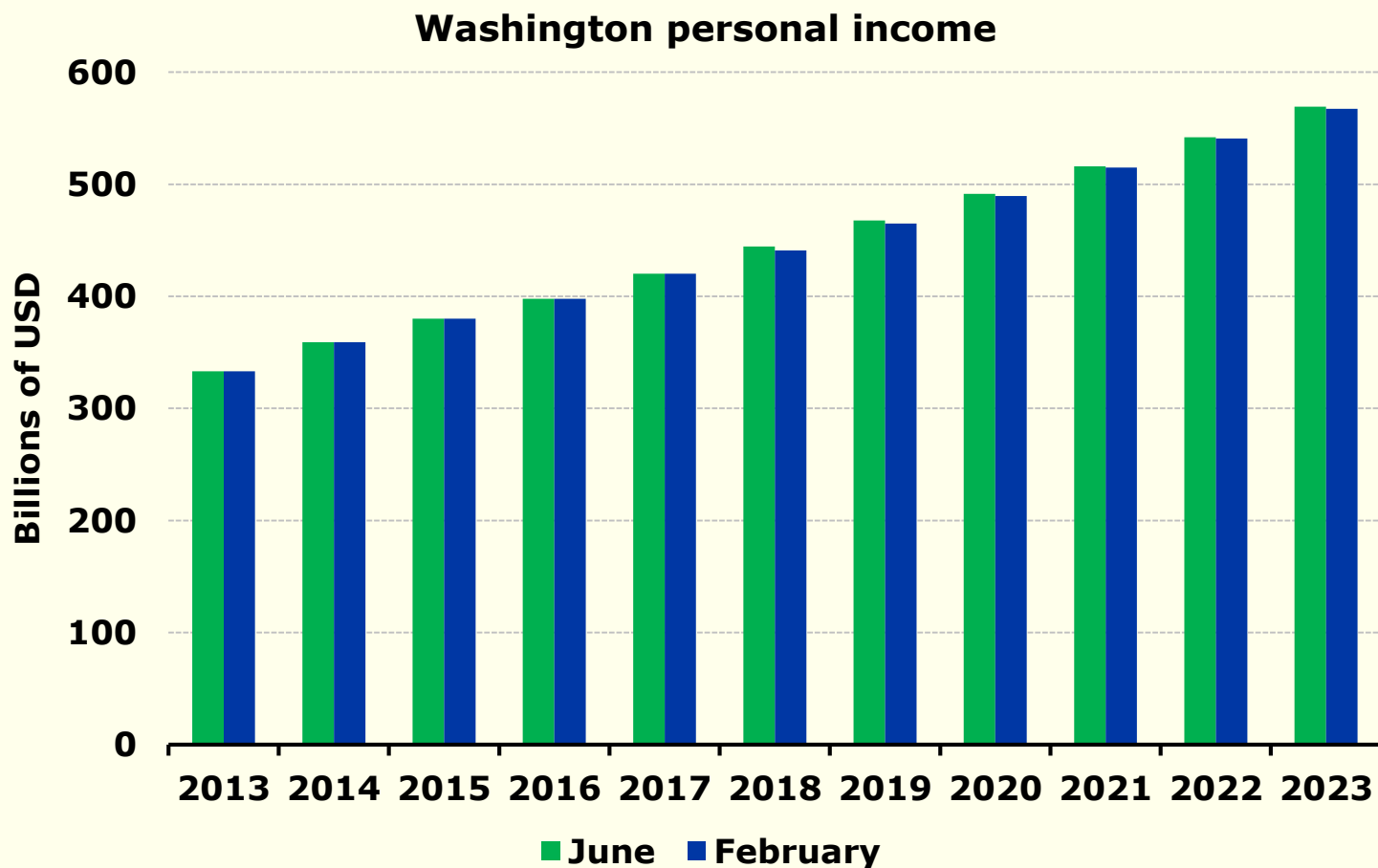


Oil prices are slightly higher compared to the February forecast





Washington personal income is slightly higher than in February



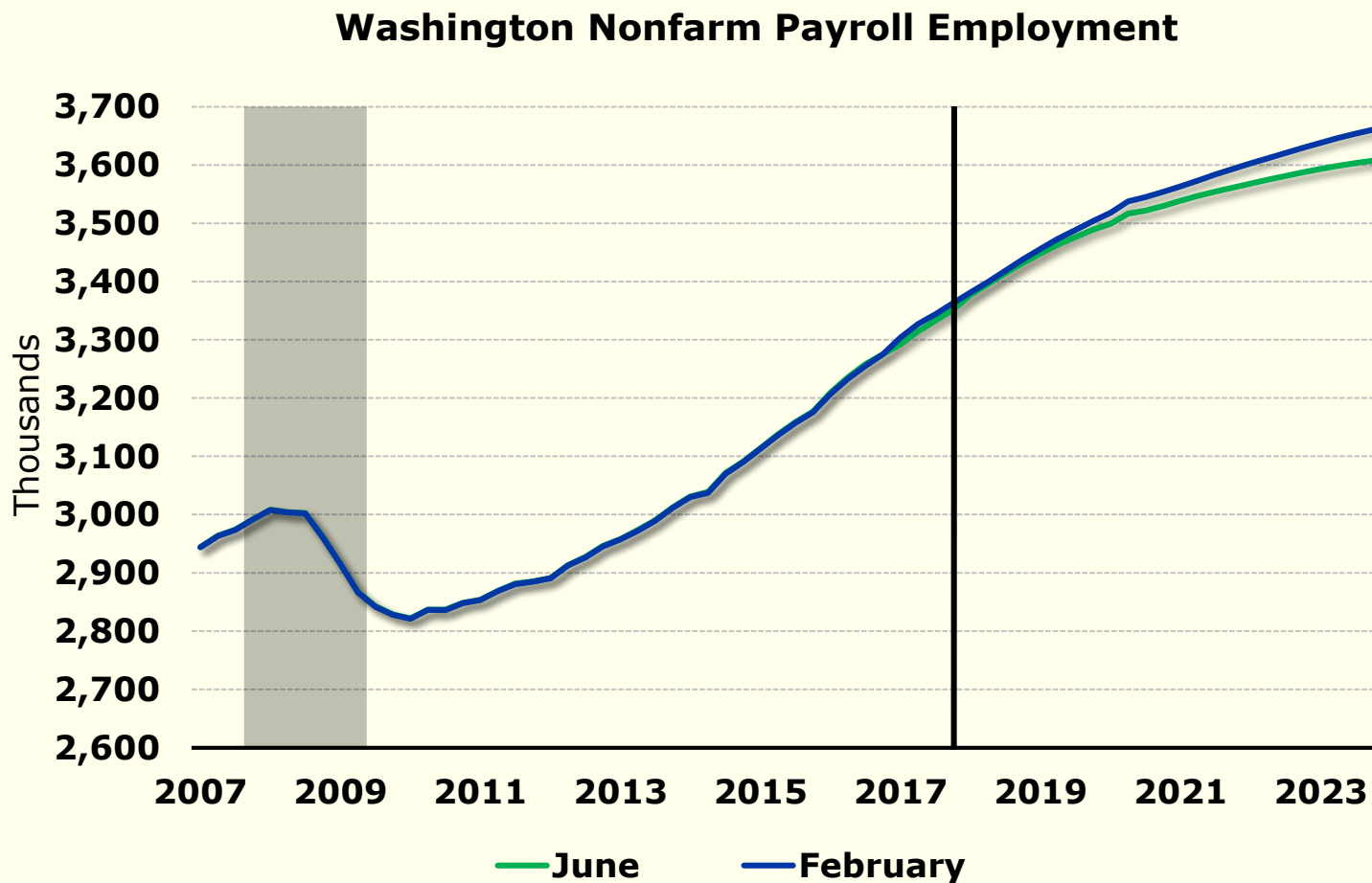
Source: ERFC June 2018 forecast; historical data through 2017

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Washington employment forecast is slightly lower compared to February

A downward revision in the population forecast has resulted in a nonfarm employment forecast 53,000 jobs lower (1.5%) by 2023 Q4 compared to February.

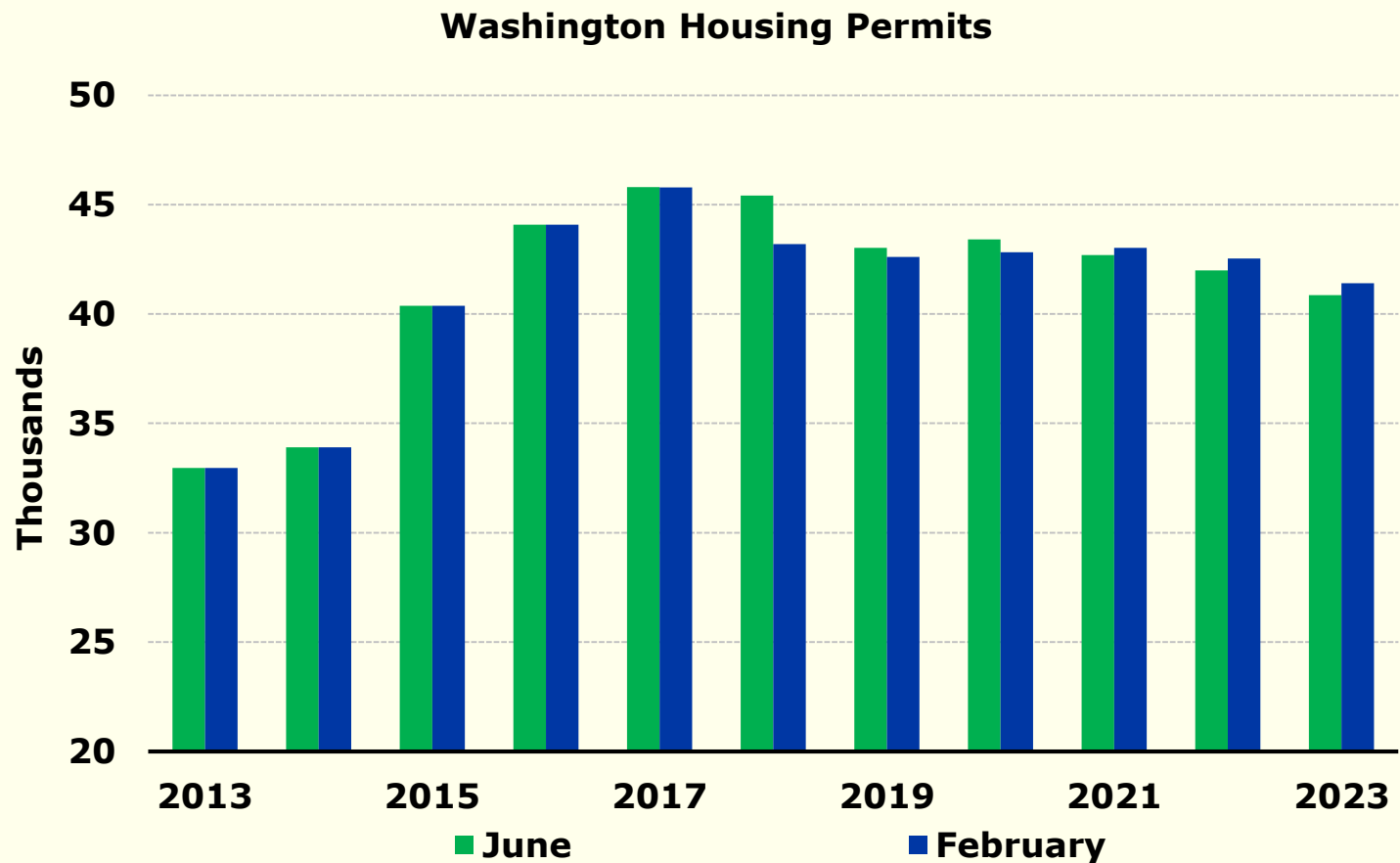


Source: ERFC June 2018 forecast; historical data through Q1 2018

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Washington housing permits forecast is higher in 2018 compared to February



Source: ERFC June 2018 forecast; historical data through 2017

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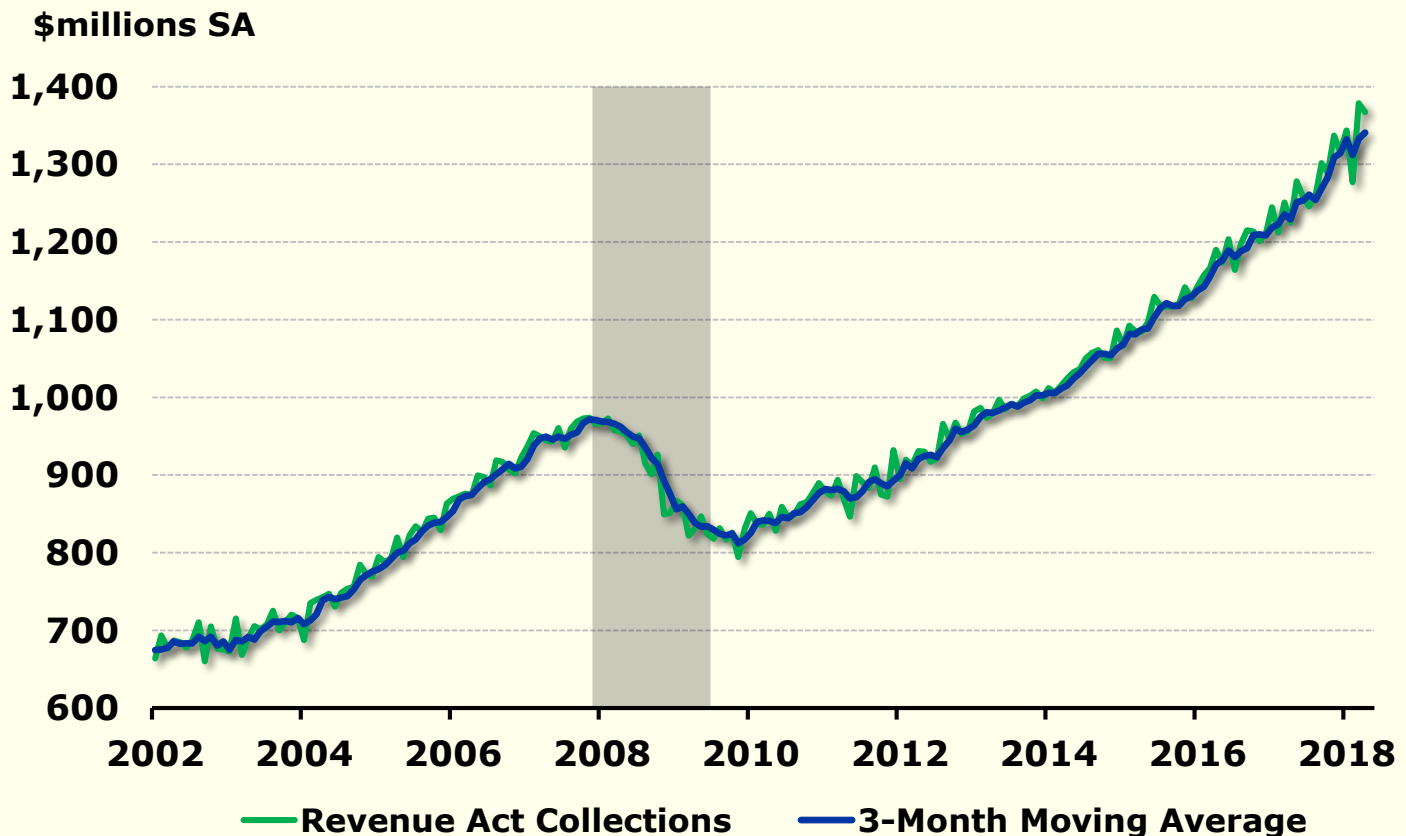


Revenue Act collections growth has been strong for two quarters

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

2017Q2: 5.6%
2017Q3: 6.4%
2017Q4: 8.3%
2018Q1: 8.2%

June 10, 2018 collections: 10.8%



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

Source: DOR and ERFC; monthly data through April 2018 activity



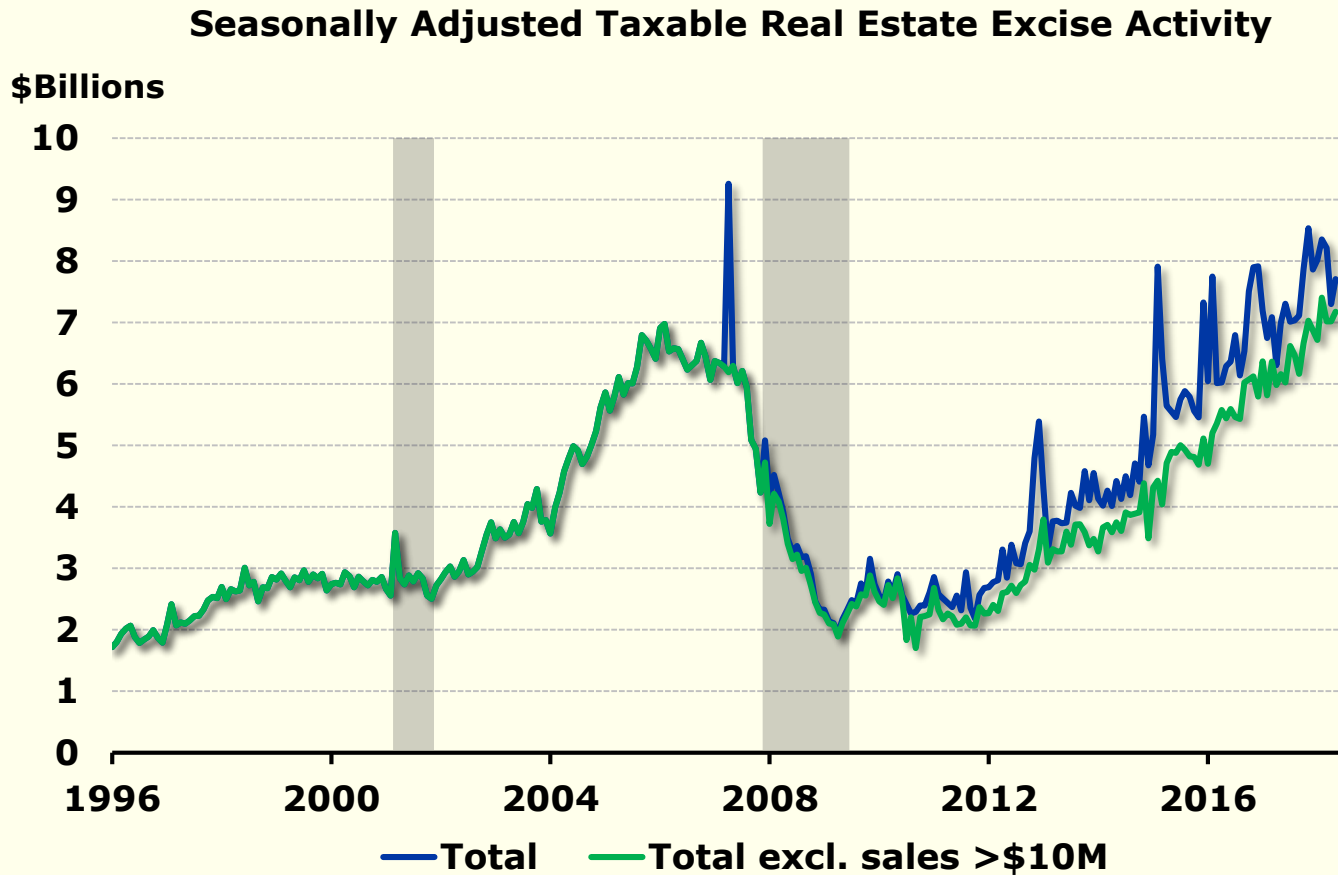
Large commercial property sales decreased but still strong in Q1 2018

Large commercial sales (>\$10 million) totaled \$2.6 billion in the 1st quarter of 2018, down from \$3.6 billion in the 4th quarter of 2017.

Residential and smaller commercial sales continue to grow.

Revenue Review
June 19, 2018

Slide 16



Source: ERFC; Monthly data through May 2018 preliminary

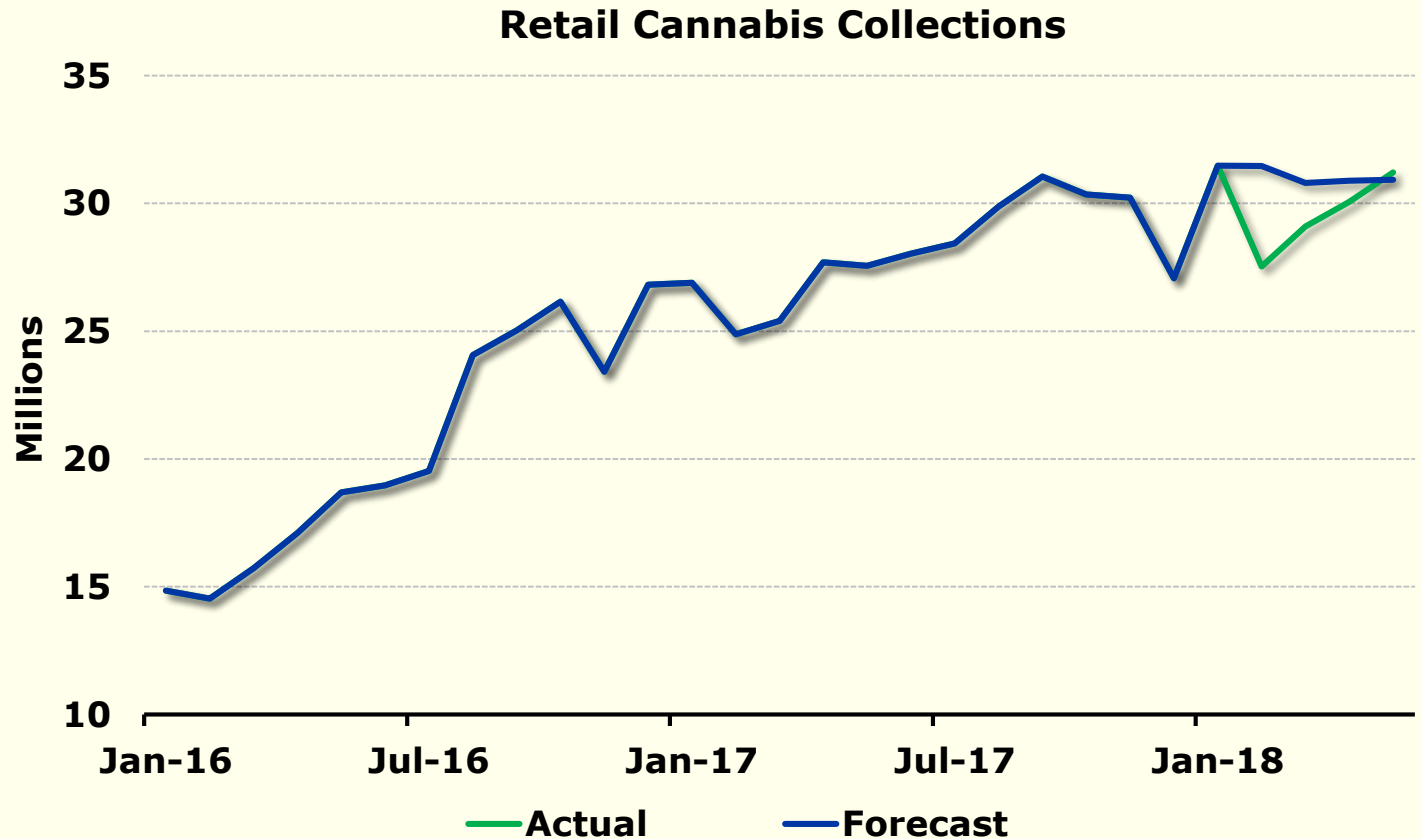
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Cannabis revenue continues to be volatile

Collections were 0.9% above forecast in May

Collections are 5.0% below forecast since February



Source: LCB, ERFC; data through May 2018

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

As of June 10, General Fund-State collections were \$189 million higher than the February forecast.

\$Millions	<u>February 2018 Forecast*</u>	<u>Non-economic Change**</u>	<u>Forecast Change</u>	<u>Forecast</u>	<u>Total Change#</u>
General Fund-State	\$44,213	(\$1,173)	\$493	\$43,532	(\$680)
Education Legacy Trust Account	\$520	\$935	\$43	\$1,498	\$978
WA Opportunity Pathways Account	\$257	\$0	\$1	\$258	\$1
Total Near GF-S	\$44,990	(\$238)	\$536	\$45,288	\$298

* Forecast for the 2017-19 biennium adopted February 20, 2018

** Sum of legislative and budget driven revenue changes from the 2018 legislative session

Detail may not add to total due to rounding

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

\$Millions	<u>February 2018 Forecast*</u>	<u>Non-economic Change**</u>	<u>Forecast Change</u>	<u>Forecast</u>	<u>Total Change#</u>
General Fund-State	\$48,253	(\$181)	\$448	\$48,520	\$267
Education Legacy Trust Account	\$565	\$0	\$17	\$582	\$17
WA Opportunity Pathways Account	\$258	\$0	\$3	\$261	\$3
Total Near GF-S	\$49,076	(\$181)	\$468	\$49,363	\$287

* Forecast for the 2019-21 biennium adopted February 20, 2018

** Sum of legislative and budget driven revenue changes from the 2018 legislative session

Detail may not add to total due to rounding



Cannabis excise tax and license fee estimates

Total change since February forecast:

- 2017-19
-\$0.2 M
- 2019-21
-\$10.8 M
- 2021-23
-\$2.6M

\$Millions

Cannabis Forecast

	<u>2017-19</u>	<u>2019-21</u>	<u>2021-23</u>
GF-S share of excise tax and license fees	\$247	\$268	\$321
Non-GF	\$501	\$530	\$530
Total	\$749	\$798	\$851

* Detail may not add to total due to rounding



2017-19 Biennium alternative General Fund-State forecasts

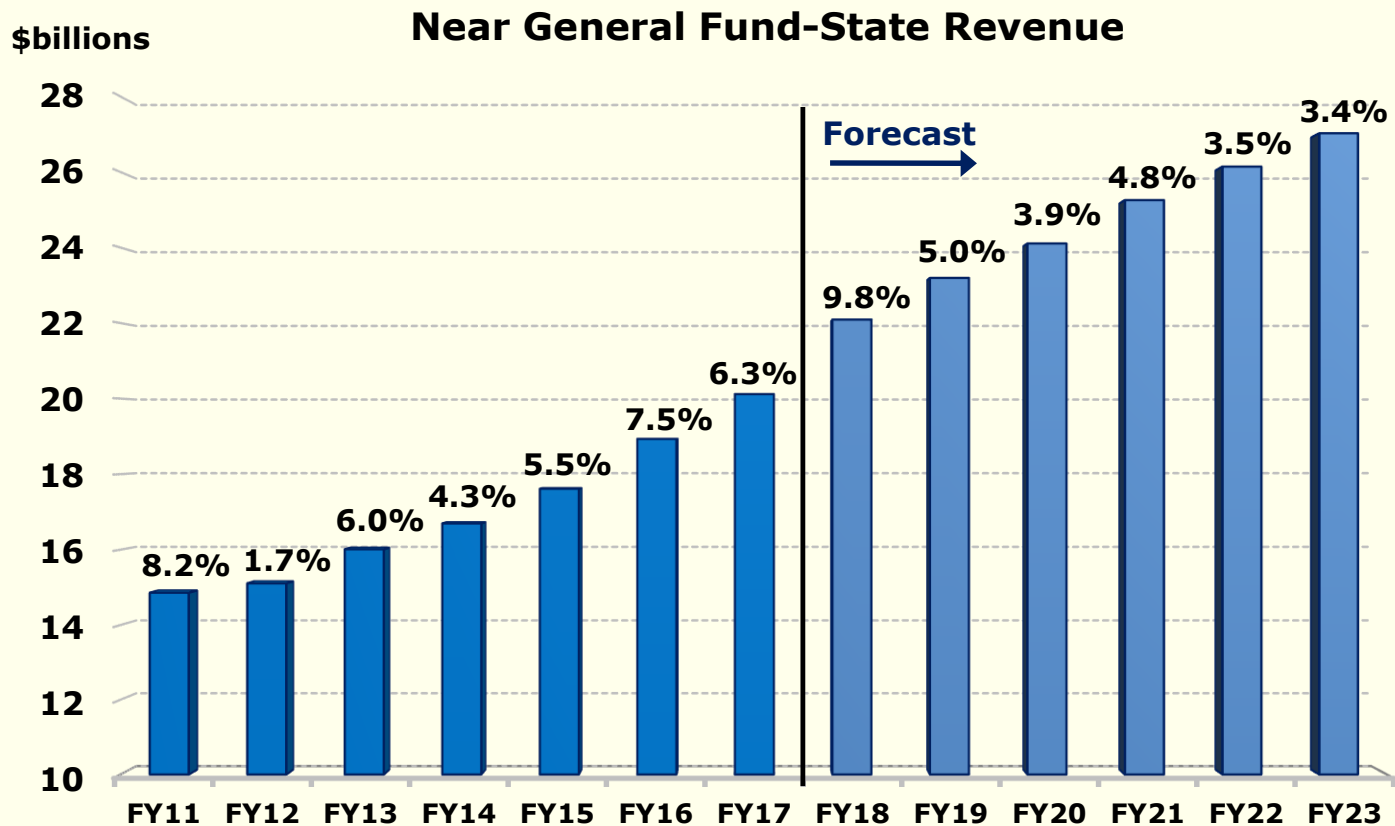
\$Millions (cash basis)	2017-19 Biennium	Difference From the baseline[#]
June 2018 Baseline (70%)	\$43,532	
<u>June 2018 Alternative Forecasts</u>		
Optimistic (15%)	\$44,383	\$851
Pessimistic (15%)	\$42,595	(\$937)
Probability Weighted Average	\$43,519	(\$13)
GCEA*	\$43,304	(\$228)

*Based on the Governor's Council of Economic Advisors' economic assumptions

#May not add to total due to rounding



Near General Fund-State* forecast by fiscal year



*Near General Fund-State equals General Fund-State plus Education Legacy Trust and Washington Opportunities Pathway Accounts
Source: ERFC forecast, June 2018



Conclusion

- WA personal income is slightly higher than in February
- As has been the case for some time, Washington's economy is continuing to outperform the nation
- Near GF-S revenues are expected to grow 16.0% between the 2015-17 and 2017-19 biennia and 9.0% 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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