

Current Forecast

Presented to Citizens' Commission on Salaries for Elected Officials

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October 10, 2018
Olympia, Washington



**WASHINGTON STATE
ECONOMIC AND REVENUE FORECAST COUNCIL**



Summary

- The economic forecast for the U.S. is very similar to the June forecast
- The economic forecast for WA has higher personal income and employment than the June forecast
- Downside risks to the baseline include uncertainty regarding trade and fiscal policy, geopolitical concerns and higher interest rates
- The near General Fund-State forecast for the 2017-19 biennium is increased by \$348 million



Forecast risks

Upside

- Elevated consumer, business confidence could translate into stronger growth
- Strong U.S., WA labor markets

Downside

- International trade and fiscal policy uncertainty
- Geopolitical risks: North Korea, China, Russia, Iran, Venezuela
- Impact of rising interest rates
- Maturing economic expansion

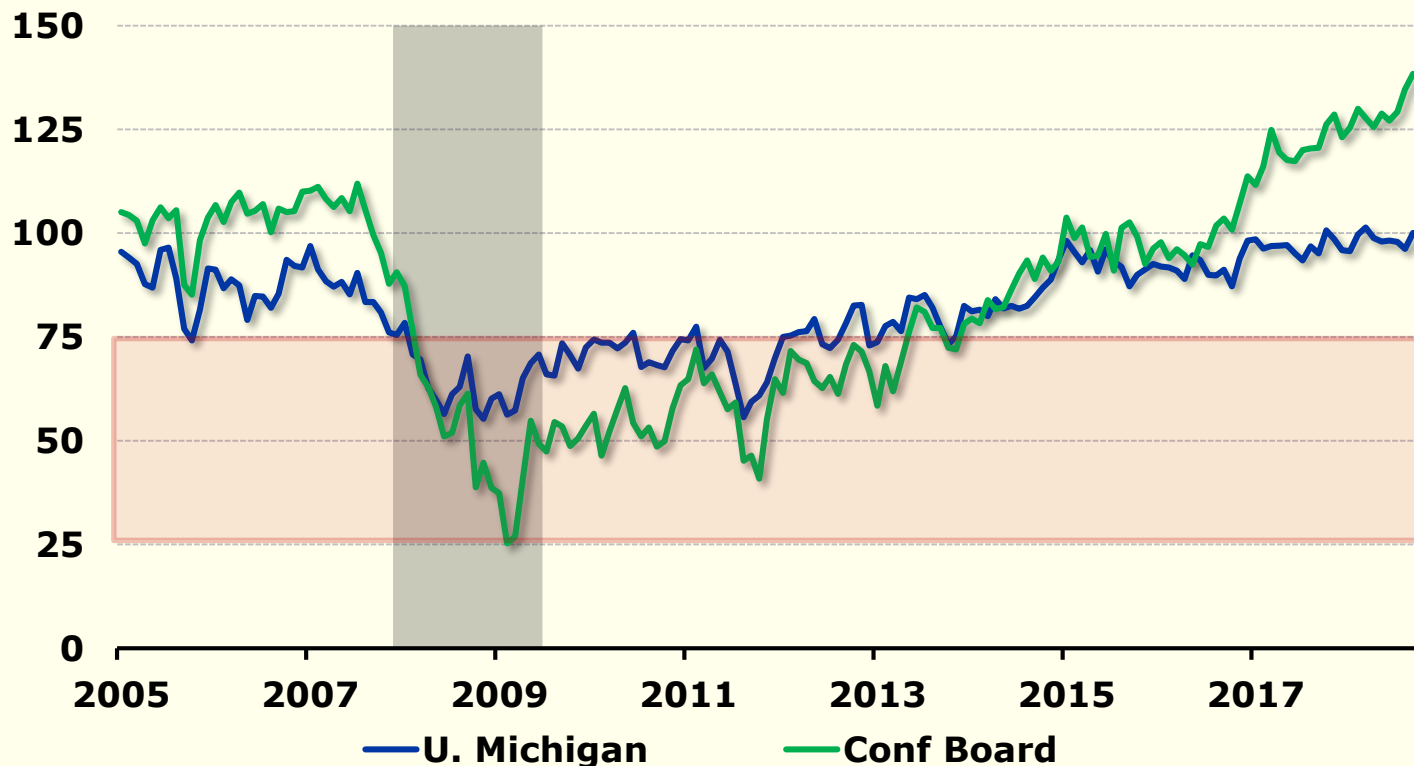


Consumer confidence remains at an elevated level

Index

Mich: 1966Q1 = 100, SA

Conf Board: 1985 = 100, SA

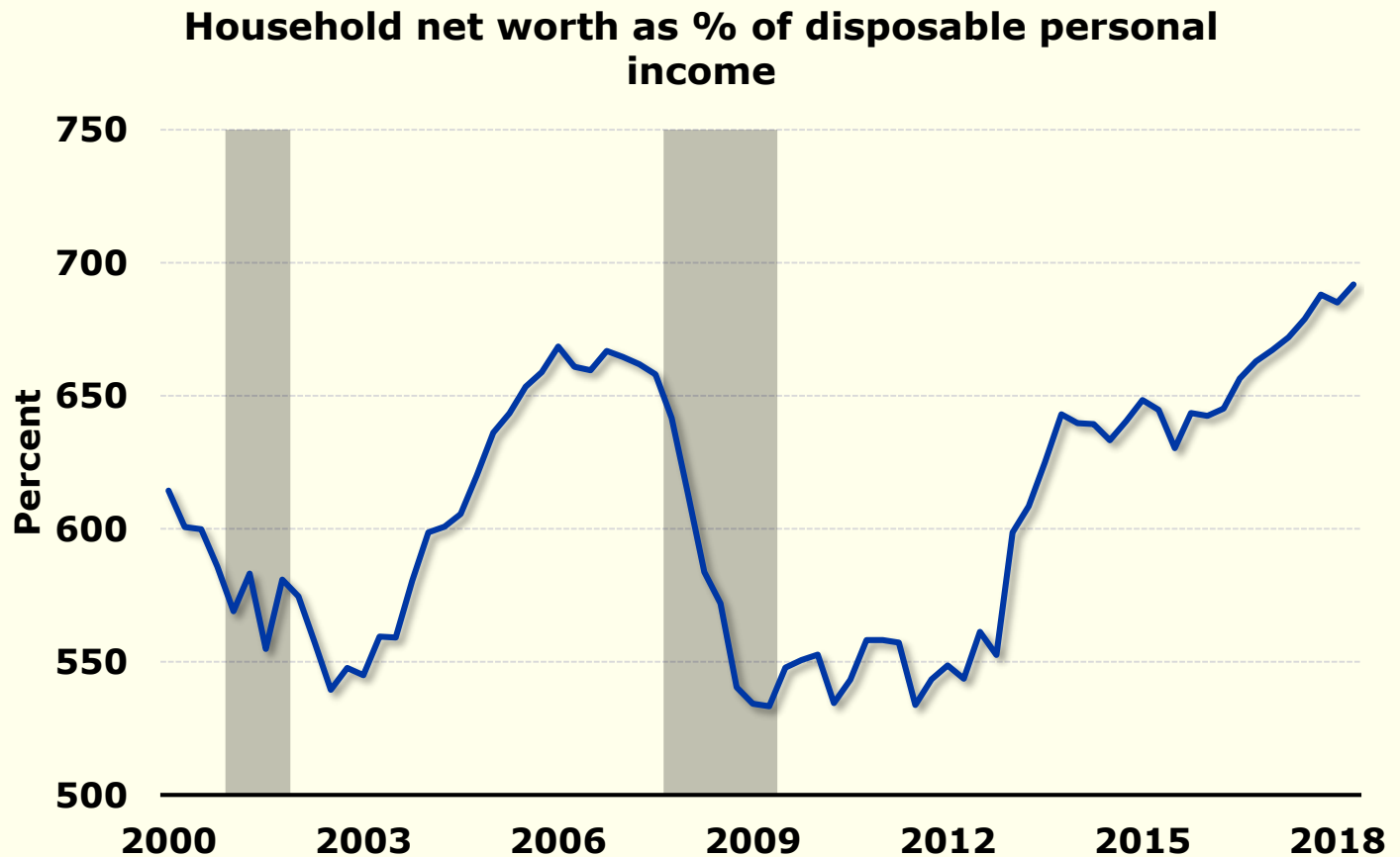


Sources: University of Michigan, Conference Board; data through September 2018

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Household net worth reached a record \$107 trillion in second quarter of 2018

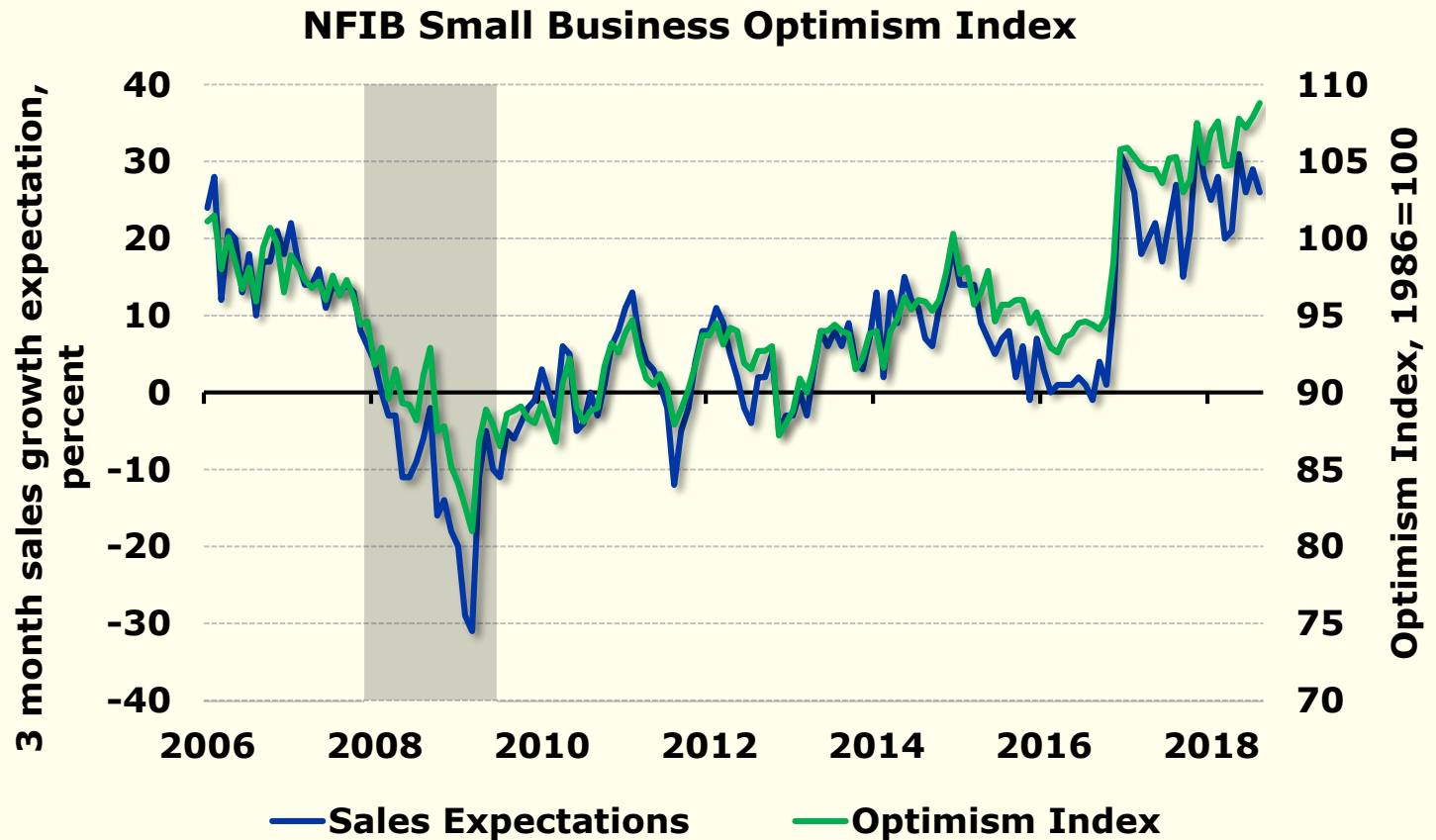


Source: Federal Reserve Bank of St. Louis, data through 2018 Q2

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

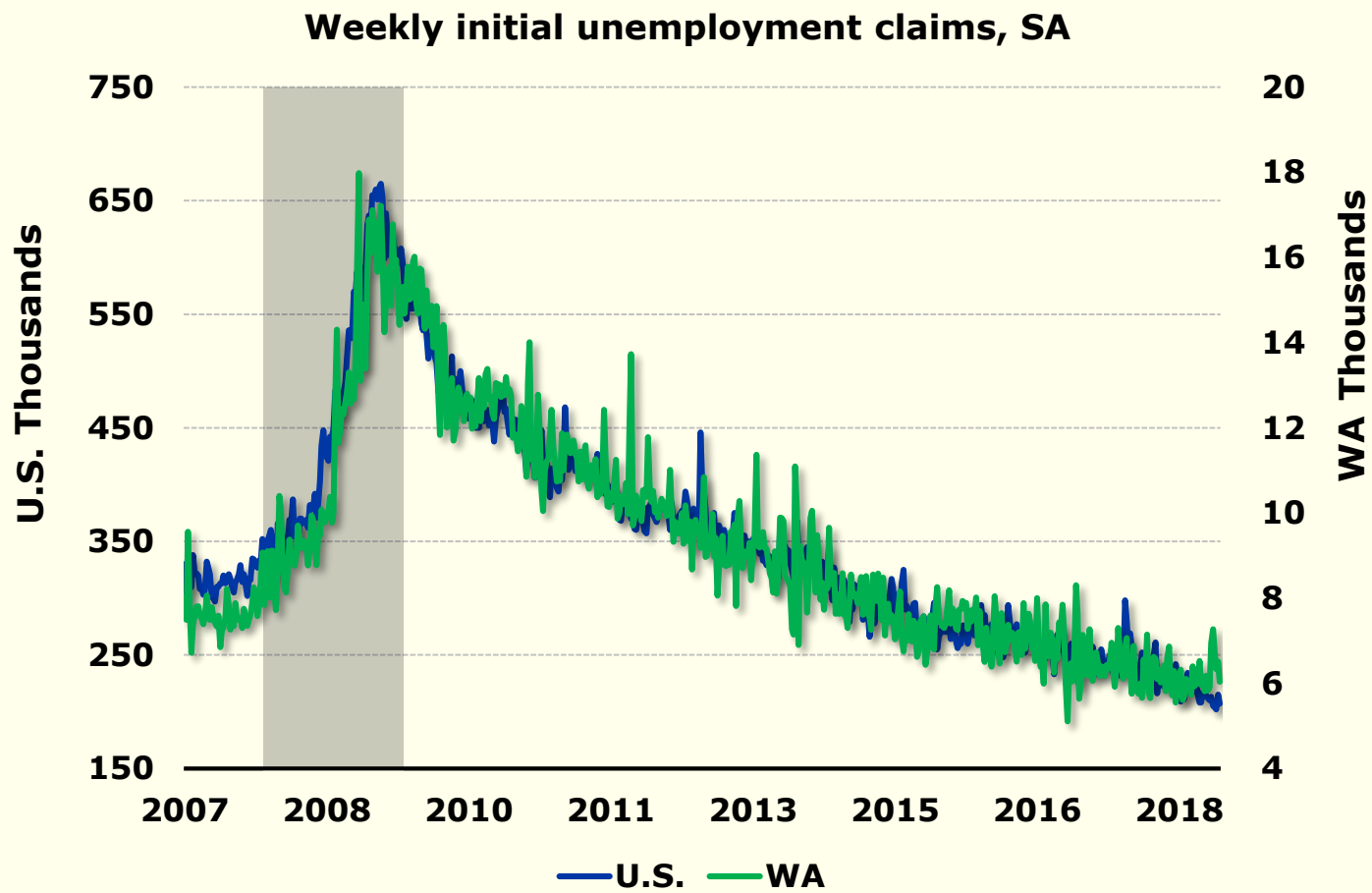


Source: National Federation of Independent Business; data through August 2018

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Both WA and U.S. initial unemployment claims remain low

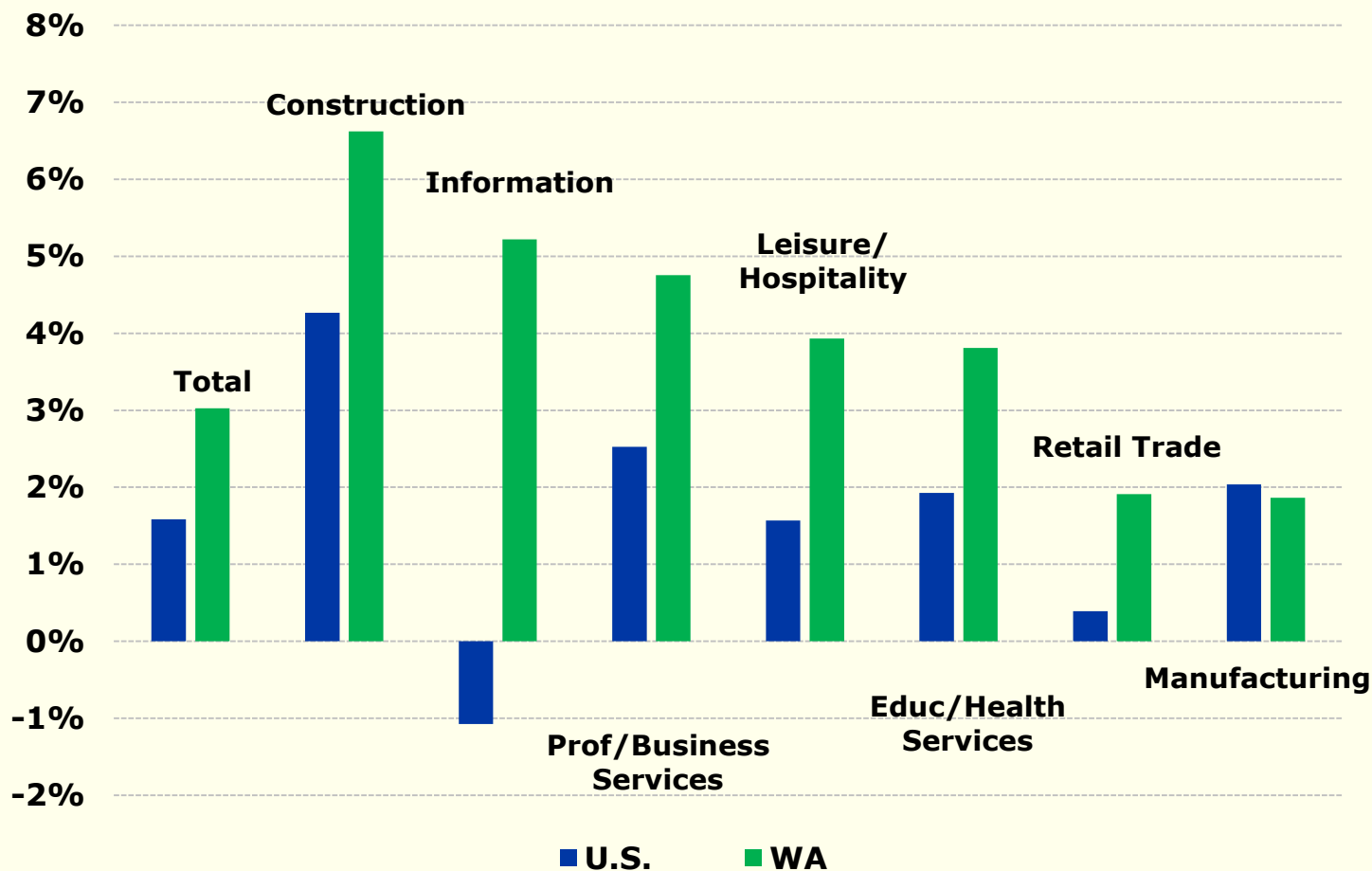


Source: U.S. Bureau of Labor Statistics, WA Employment Security Dept., data through Sept. 29, 2018

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Washington vs U.S. employment growth: August 2017 to August 2018



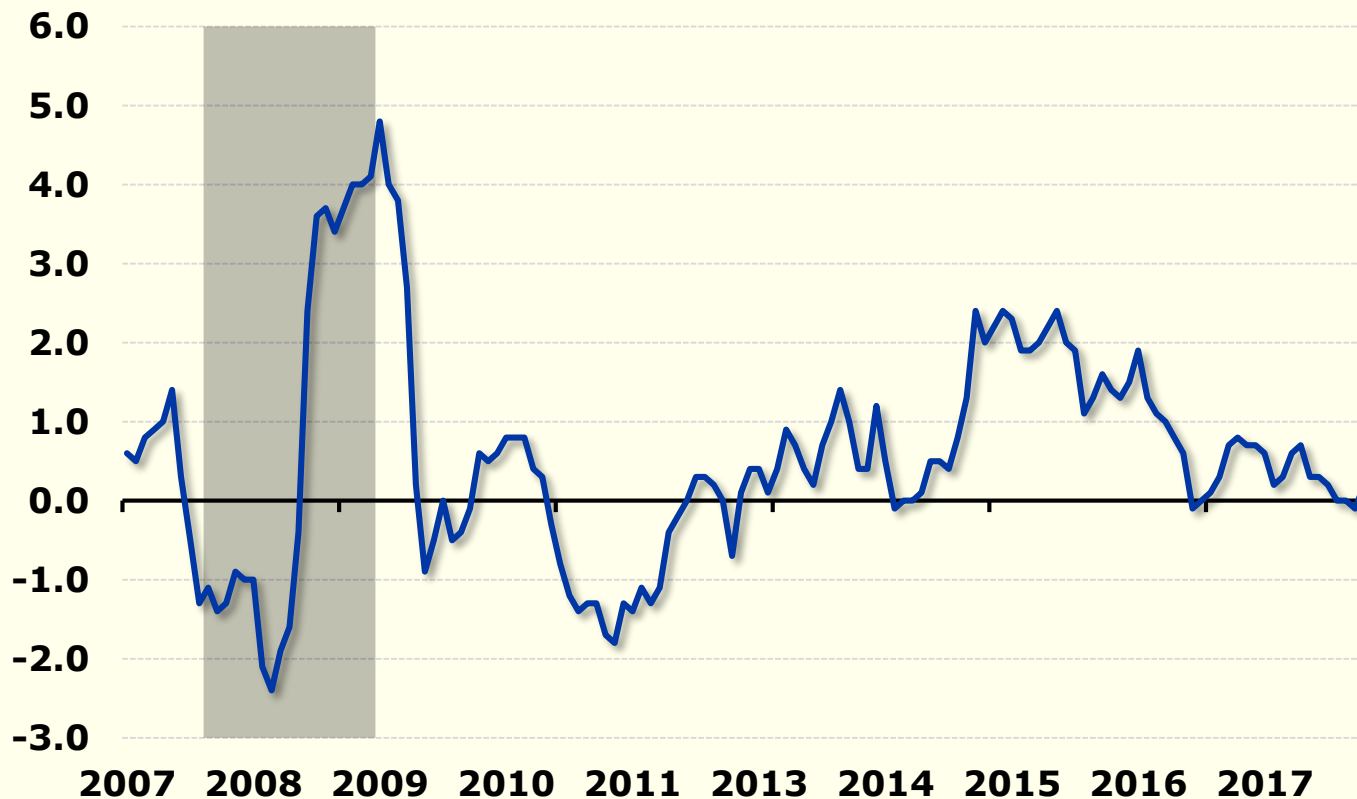
Source: U.S. Bureau of Labor Statistics, Employment Security Dept., ERFC; data through August 2018

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Adjusted for inflation, hourly wage growth remains weak

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



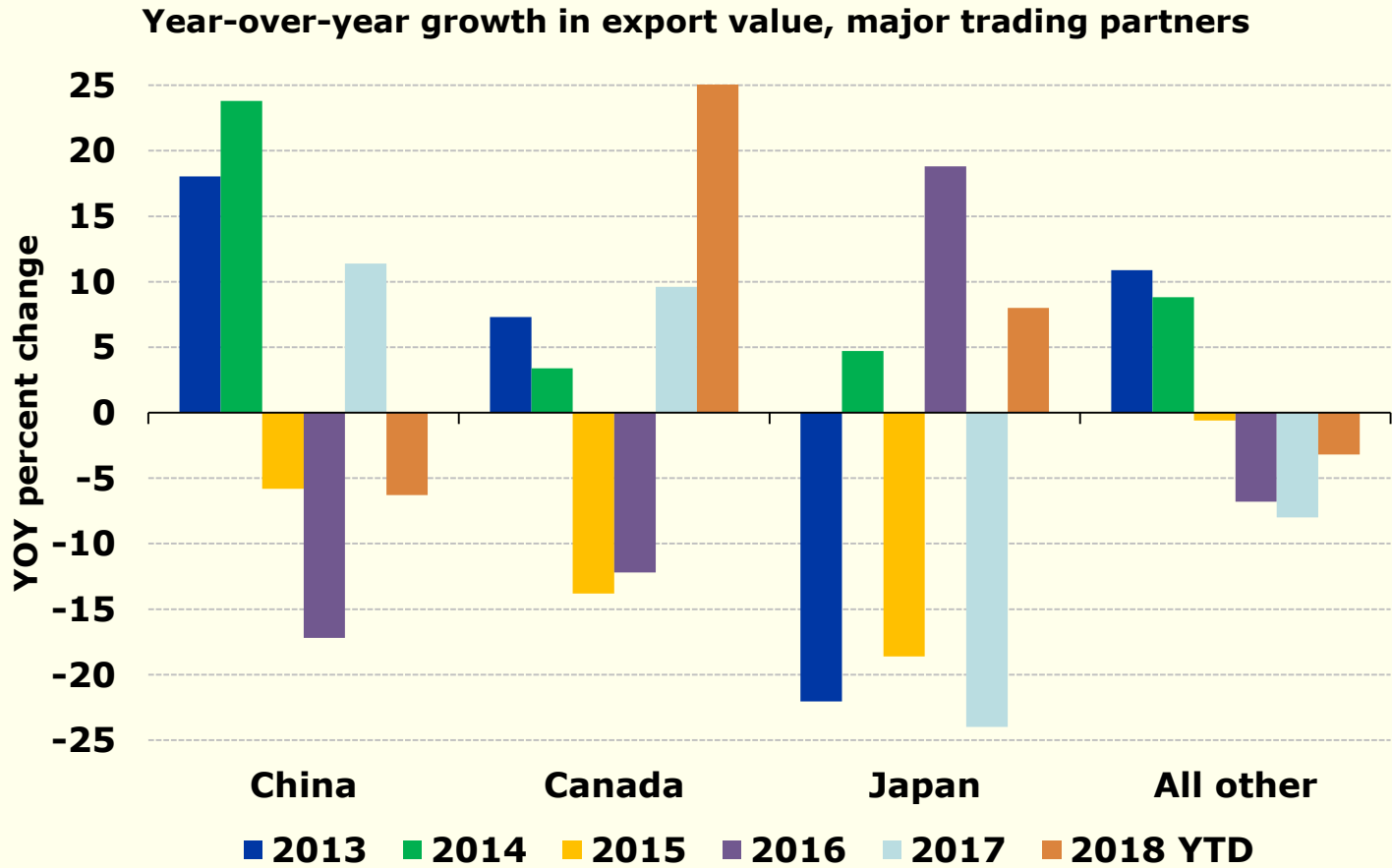
Source: U.S. Bureau of Labor Statistics, monthly data through August 2018

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So far this year, WA exports to Canada, Japan are up but exports to China are down

Total exports declined 3.9% in 2017 but increased 0.6% in fourth quarter 2017 and 3.9% in first quarter 2018 and 3.7% in second quarter 2018



Source: WISERTrade; data through July 2018

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Tariffs imposed on selected WA exports as of August 23rd

Product	Country	Tariff	WA 2017 exports (millions)
Ultrasonic Scanning Apparatus	China	25%	\$ 281.5
Wheat	China	25%	\$ 248.2
Apples, Fresh	Mexico	20%	\$ 125.6
Apples, Fresh	China	25%	\$ 17.6
Wood pulp	China	25%	\$ 119.2
Iron or Non-alloy Bars, Rods	Canada	25%	\$ 111.5
Hay, Clover, Vetches	China	25%	\$ 101.9
Cherries, Fresh	China	25%	\$ 99.7
Aluminum Plates Etc. >.2 mm	EU	25%	\$ 78.8
Aluminum Plates Etc. > .2 mm	Canada	10%	\$ 43.1
Aluminum Casks, Etc.< 300 Liters	Canada	10%	\$ 56.9
Potatoes, Frozen	China	25%	\$ 54.4
Potatoes, Frozen	Mexico	20%	\$ 36.9

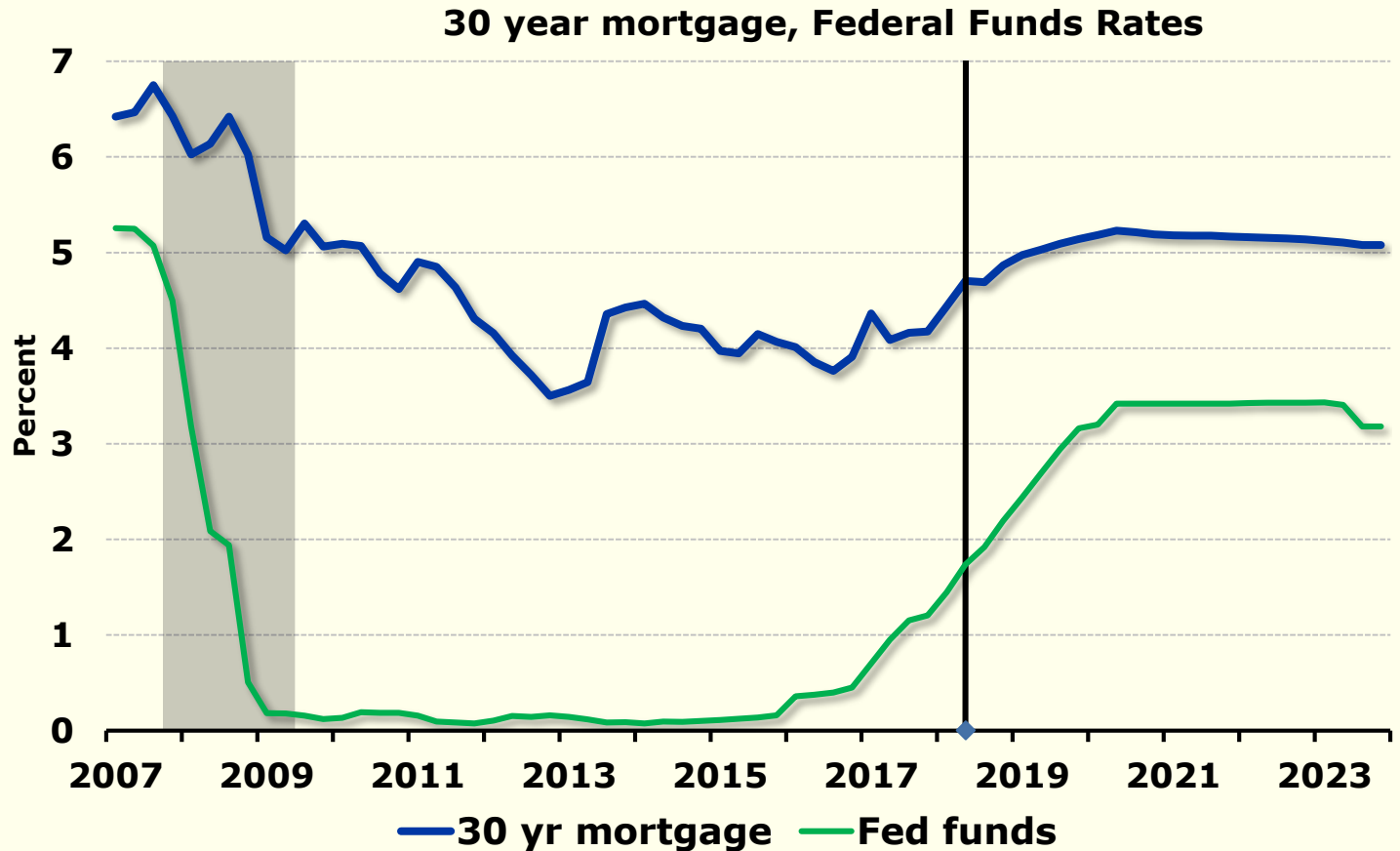
Source: WiserTrade, Economy.com

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Interest rates are expected to rise gradually over the forecast period

The forecast assumes the rate will rise gradually, with mortgage rates eventually reaching 5.2% and Fed funds 3.4% in 2020.



Source: IHS Markit, ERFC September 2018 forecast; data through Q2 2018

Note: Vertical black line indicates last actual

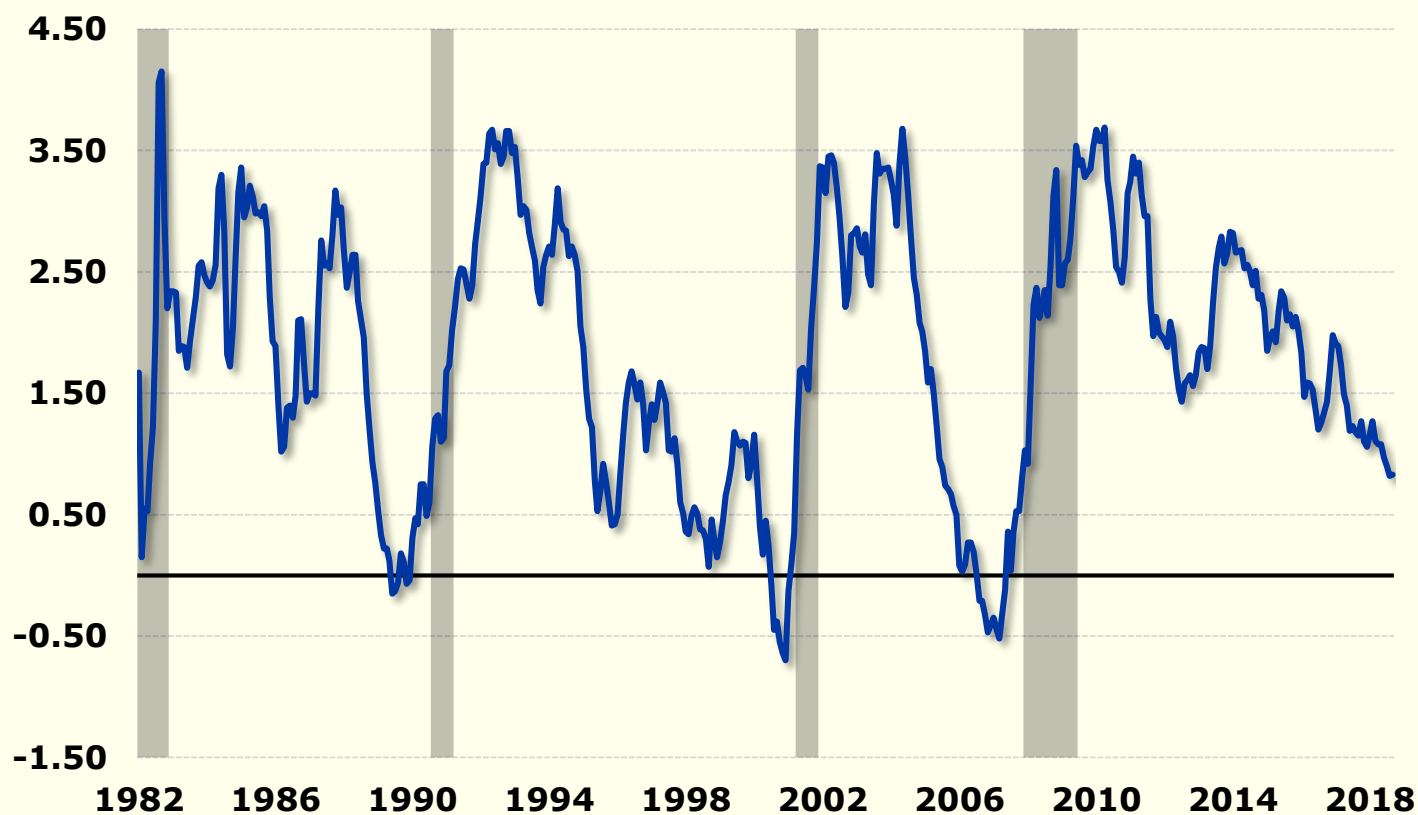
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An inverted yield curve (short-term interest rates > long-term rates) is a consistent recession predictor

As of September 2018, 10 year Treasury bond yields were 0.8% above three month Treasury bond yields

10 year – 3 month Treasury bond yields



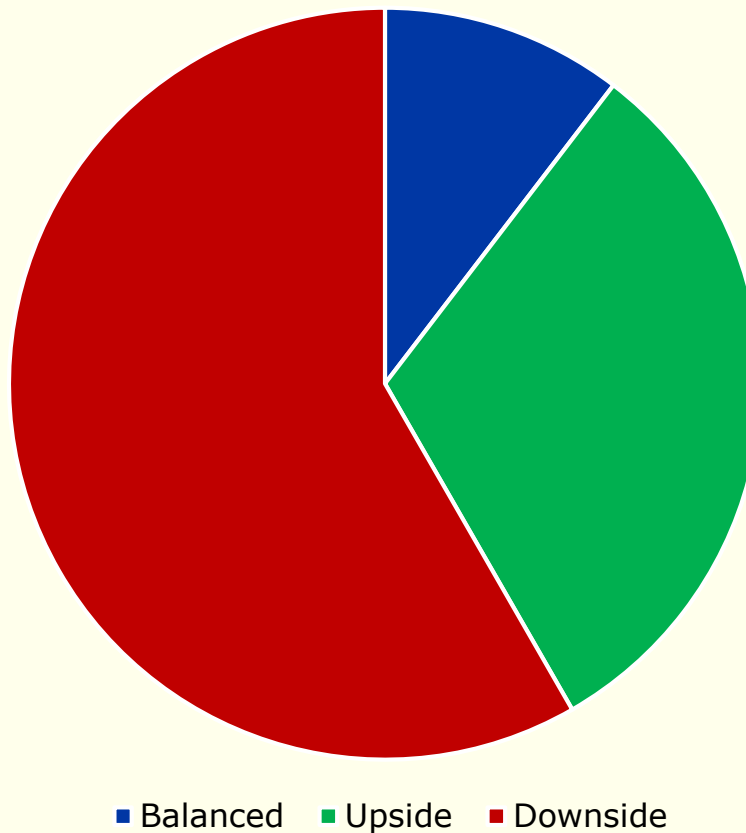
Source: Federal Reserve Bank of St. Louis, data through Sept. 2018

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In recent survey, most economists saw downside risks to their forecast over the next 12 months

Forecast Risk, Next 12 Months

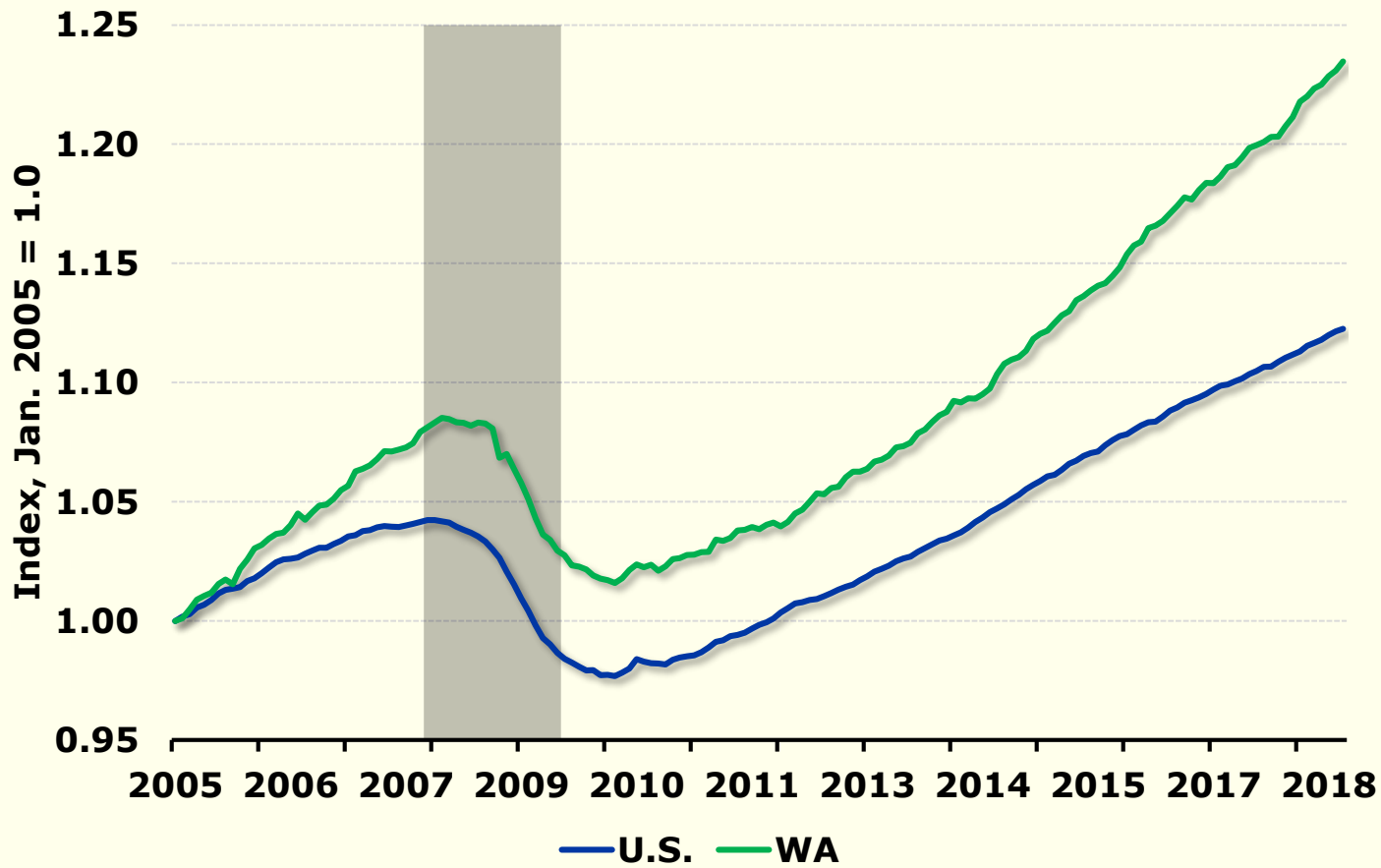


Source: Wall Street Journal monthly economist survey, August 2018

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WA employment growth continues to exceed the U.S.



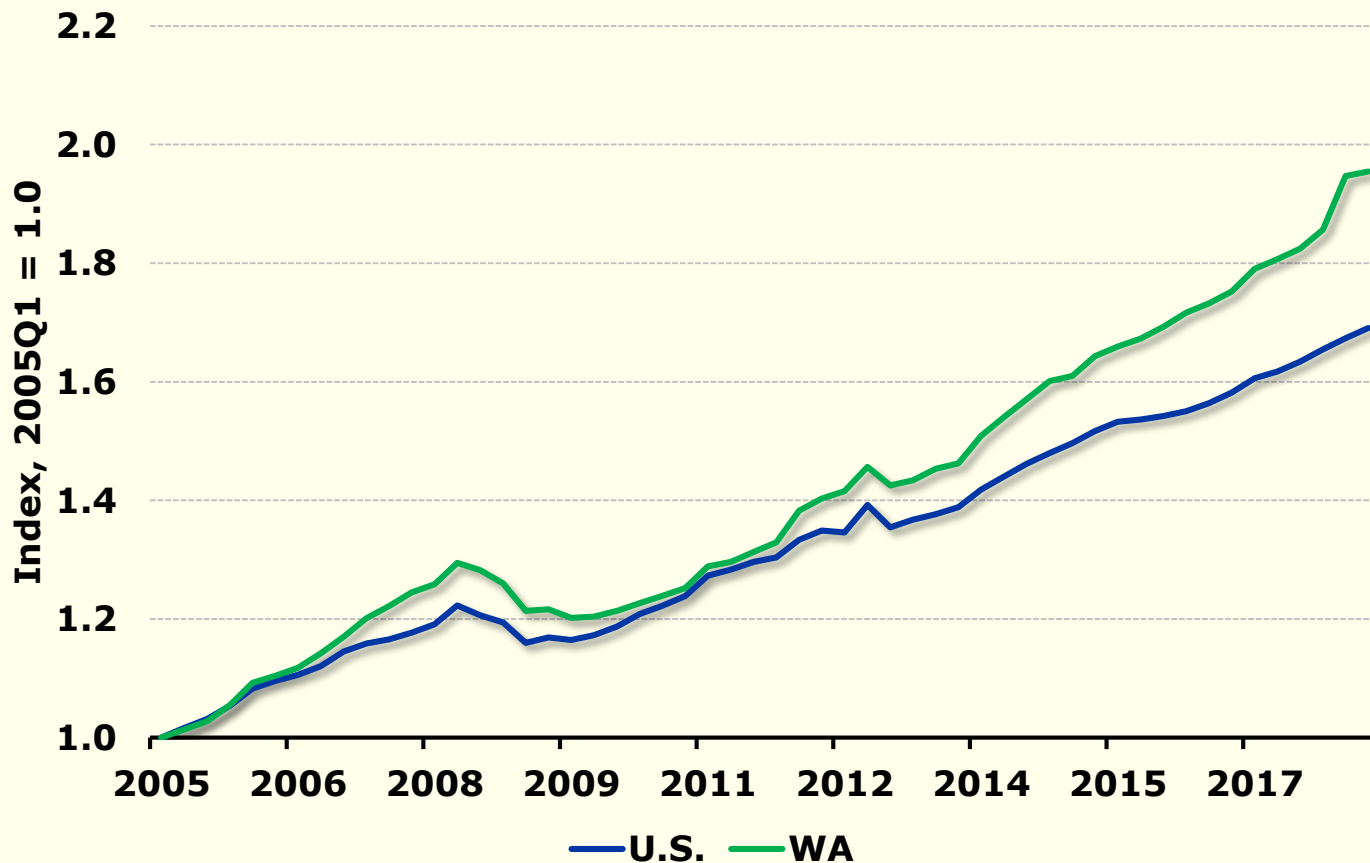
Source: U.S. Bureau of Labor Statistics, Employment Security Dept., ERFC; data through August 2018

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WA personal income growth continues to grow faster than the nation as a whole

WA personal income grew by 4.8% in 2017 compared to a 3.1% growth rate for the U.S.



Source: U.S. Bureau of Economic Analysis; data through 2018 Q2

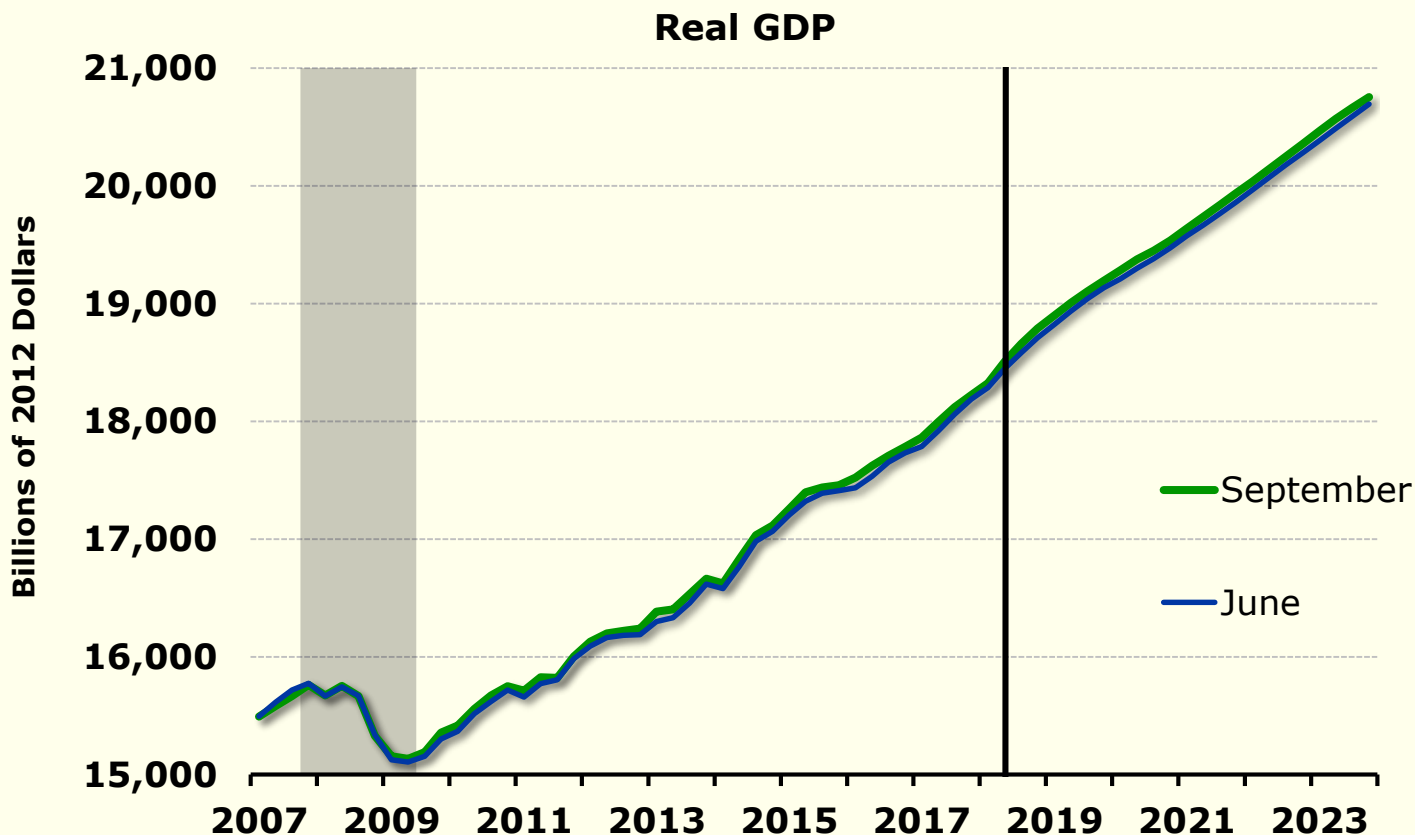
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The real GDP forecast is very similar to the June forecast

The level of real GDP is slightly higher than in June due to the comprehensive revision of the national income and product accounts.

The growth rates are virtually unchanged from the June forecast in 2018-23.



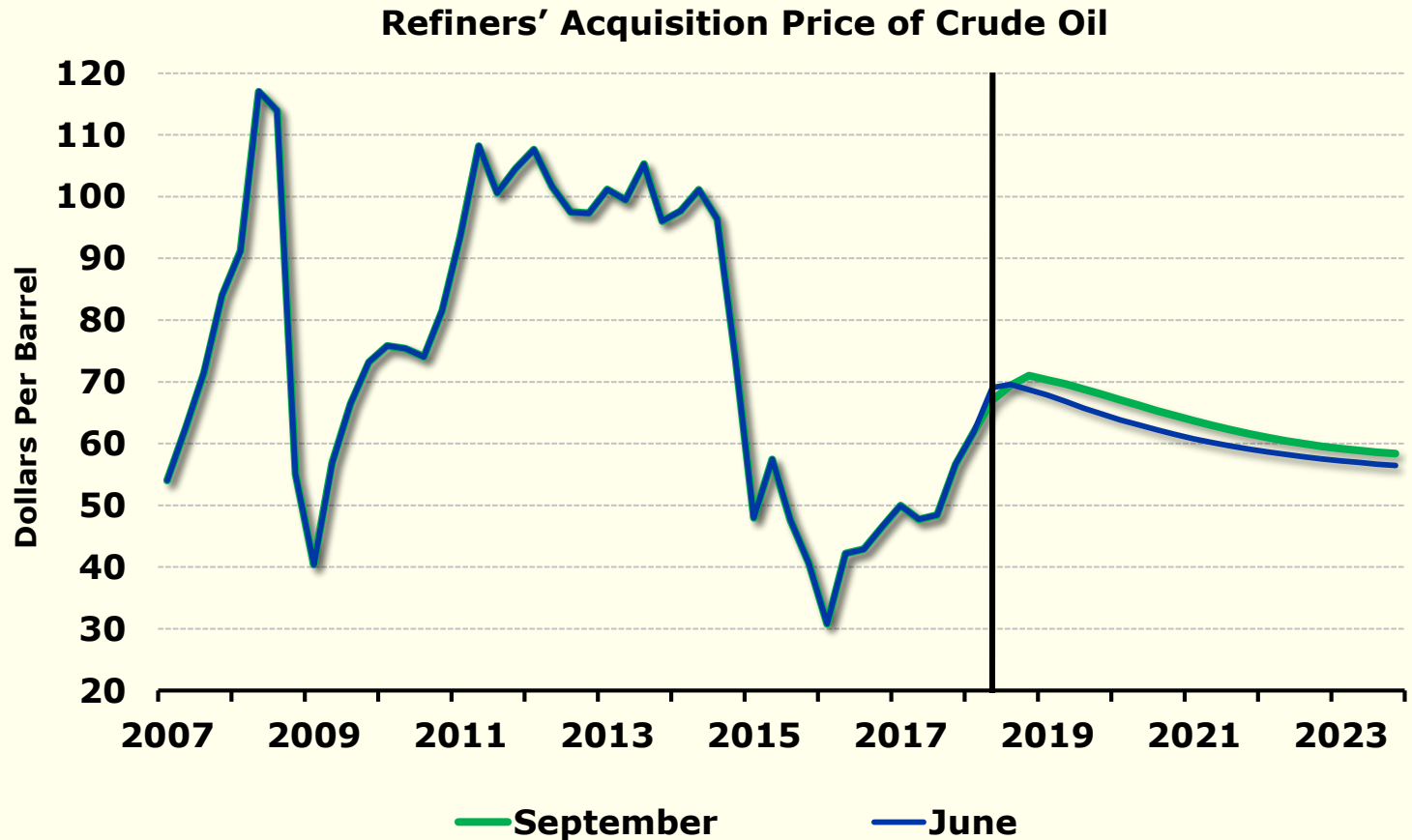
Source: IHS Markit, ERFC September 2018 forecast; data through Q2 2018

Note: Vertical black line indicates last actual

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Oil prices are very similar to the June forecast



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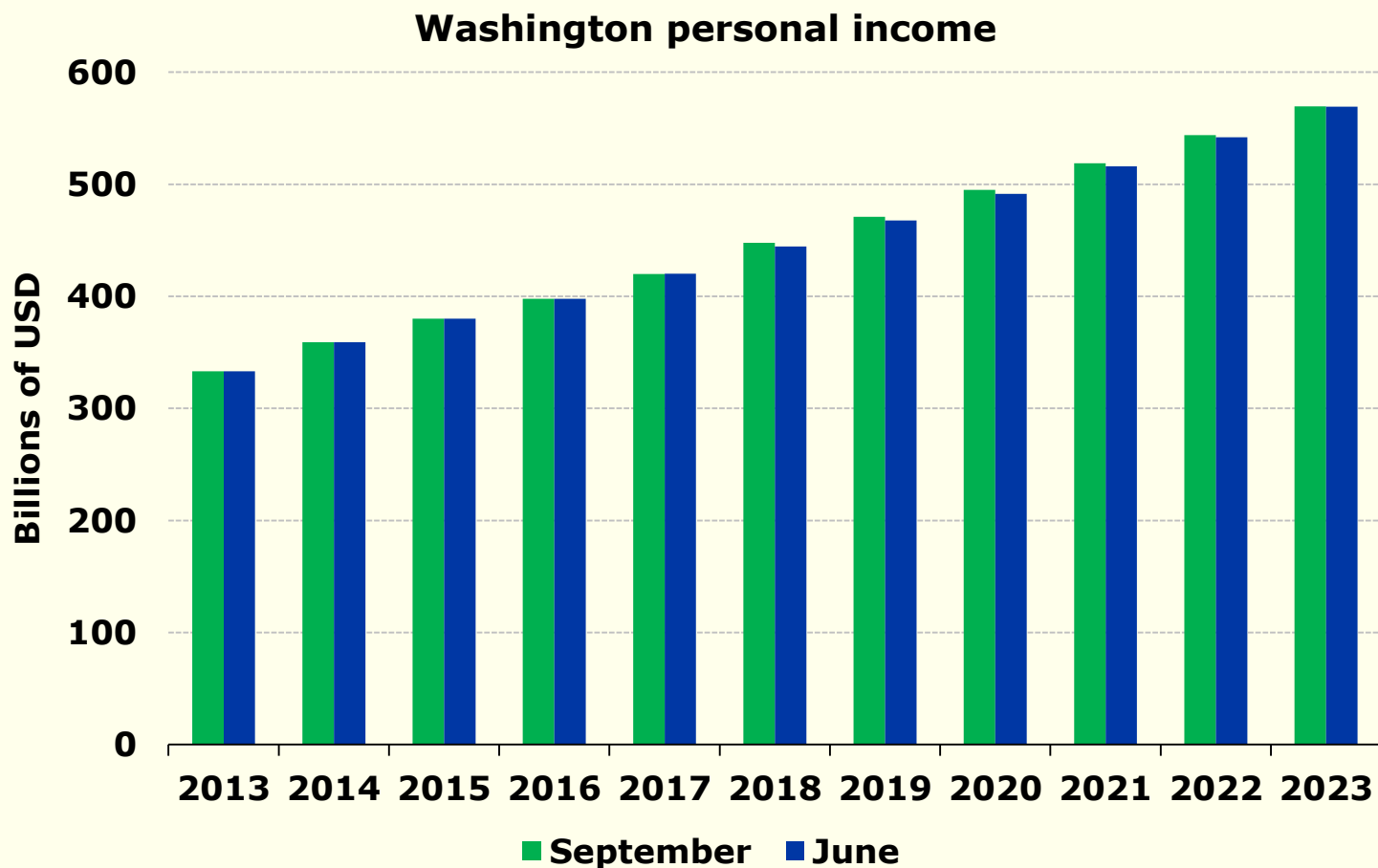
Source: Energy Information Administration, IHS Markit, ERFC September 2018 forecast; data through Q2 2018
Note: Vertical black line indicates last actual

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Washington personal income is slightly higher than in June

First quarter 2018 personal income data were revised up after the June forecast



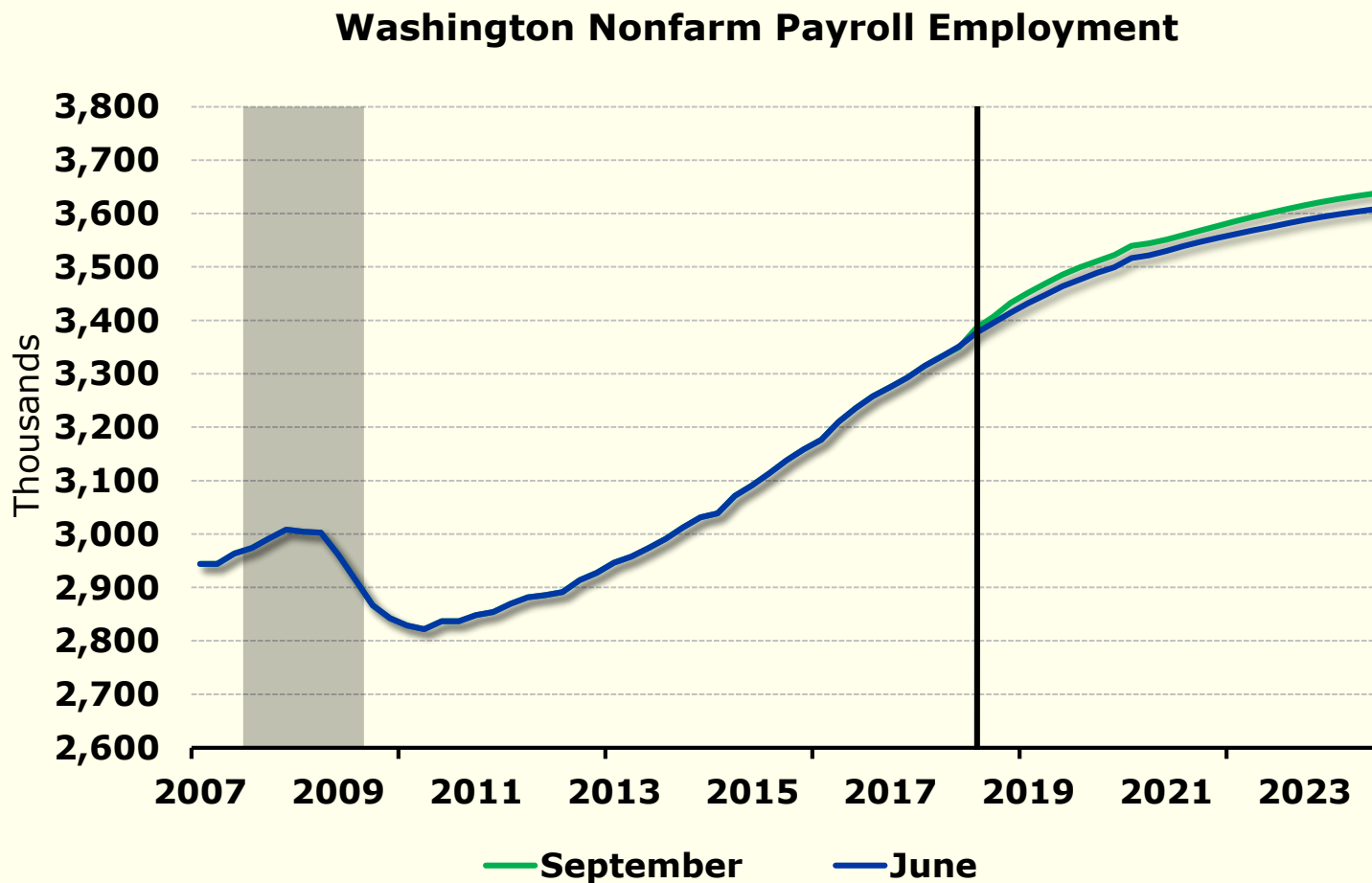
Source: ERFC September 2018 forecast; historical data through 2017

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Washington employment forecast is slightly higher than in June

The nonfarm employment forecast is 14,800 jobs higher (0.4%) this year and 29,000 jobs higher (0.8%) by 2023 compared to June.

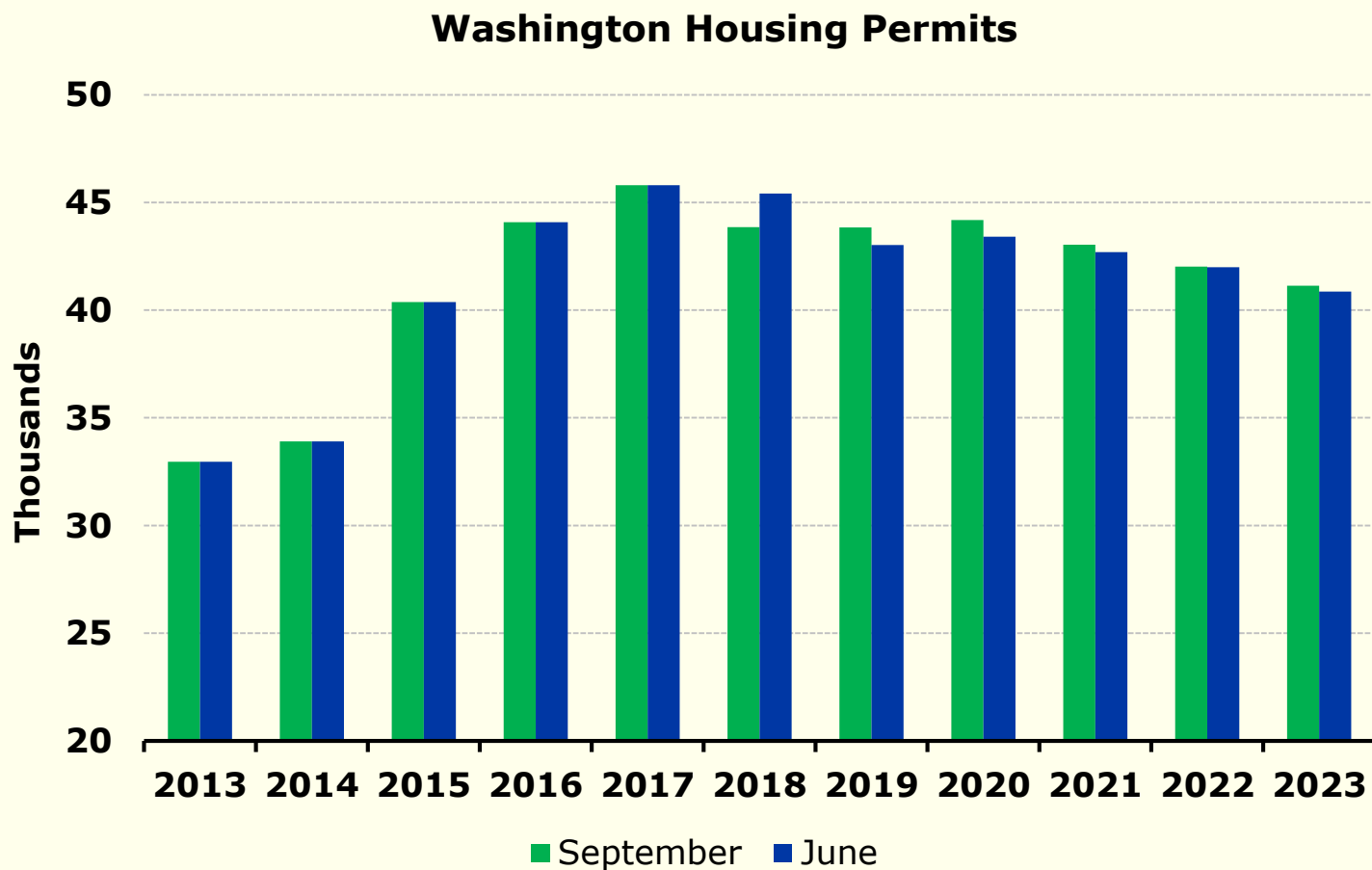


Source: ERFC September 2018 forecast; historical data through Q2 2018

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Washington housing permits forecast is lower this year, higher for 2019 – 2023 compared to June

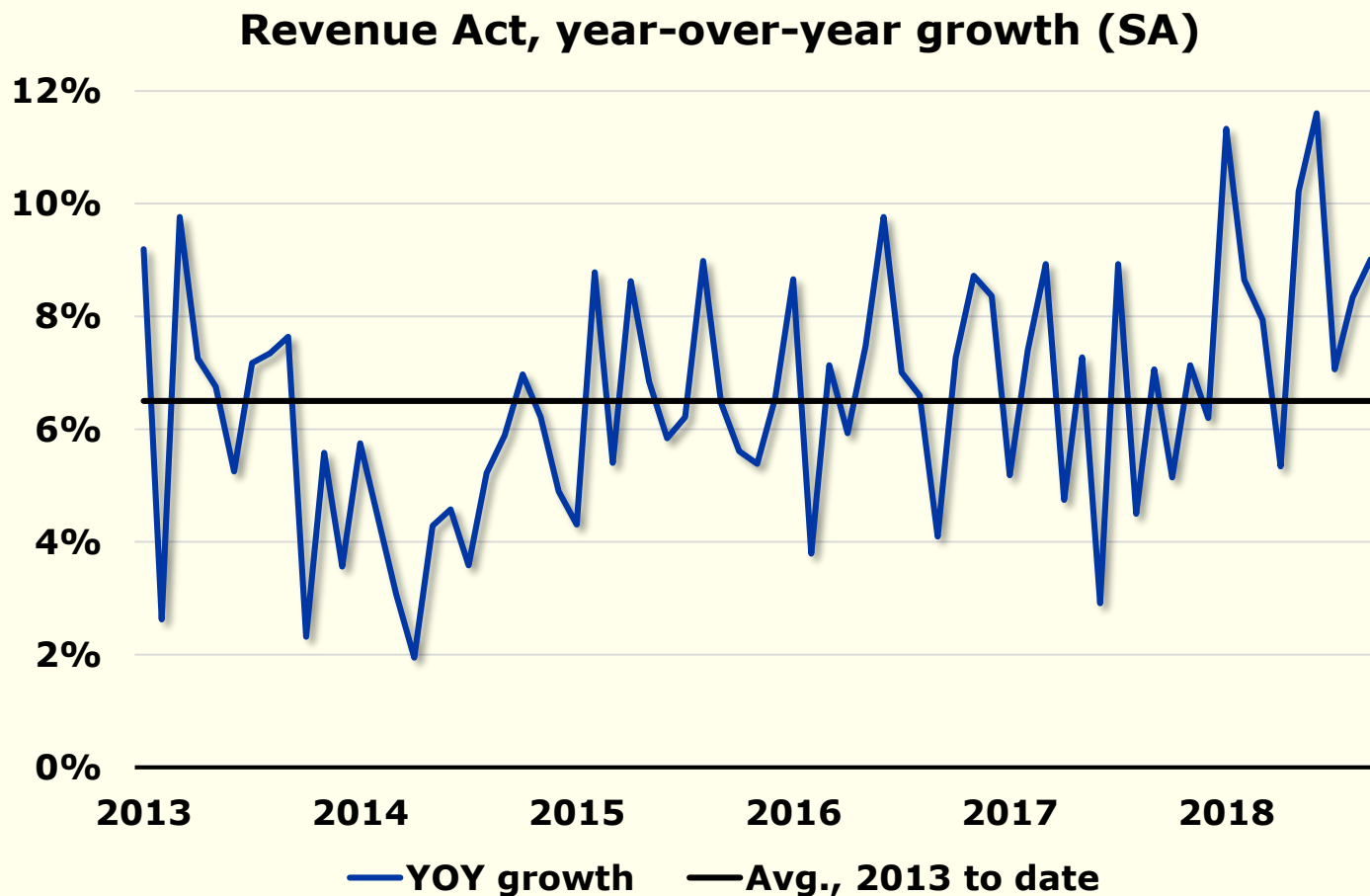


Source: ERFC September 2018 forecast; historical data through 2017

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Federal tax cuts, Marketplace Fairness Act likely contributing to strong Rev Act growth this year



* Adjusted for large one-time transactions, amnesty payments and reporting frequency change, current definition of Revenue Act; DOR and ERFC, data through Sept. 2018 activity

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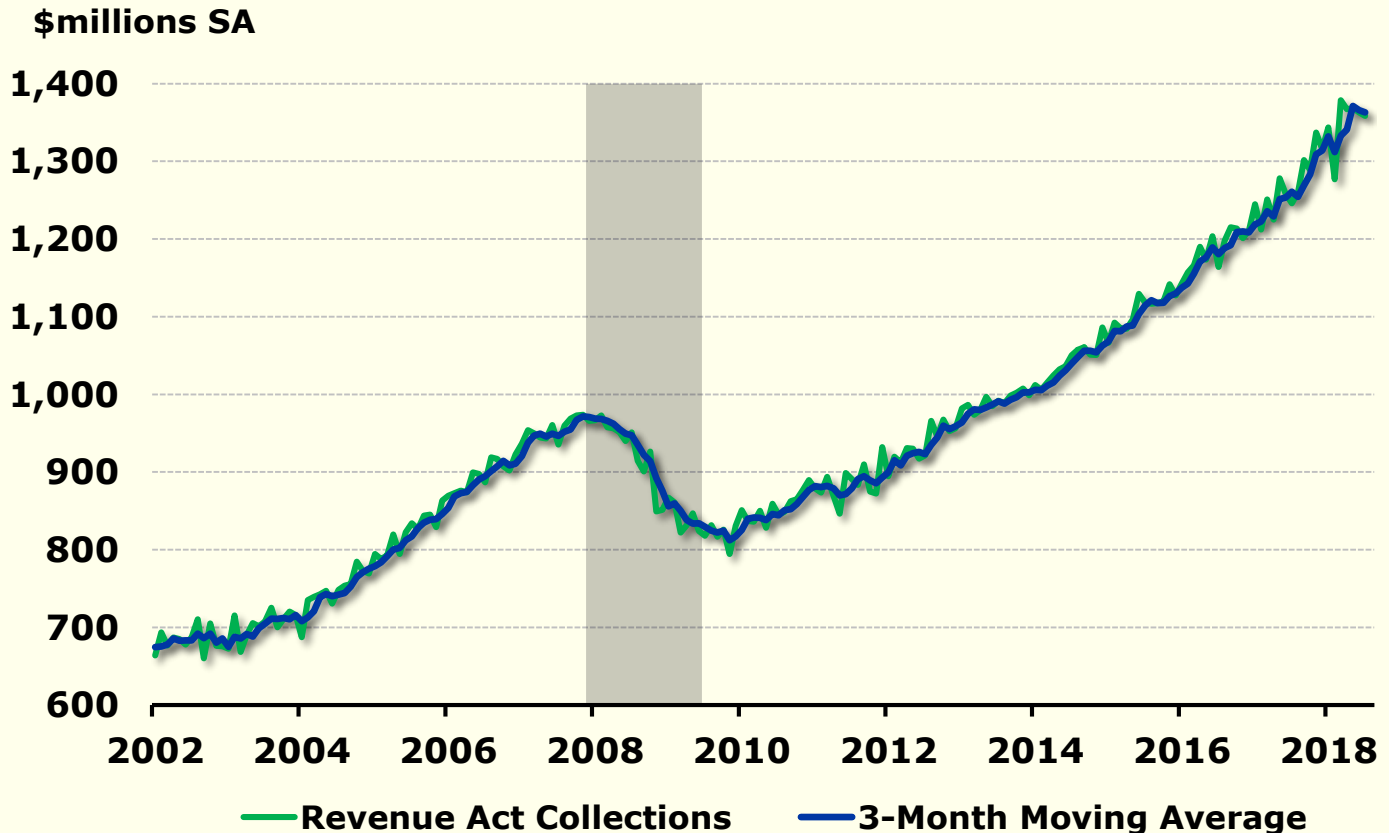


Revenue Act collections growth has been strong

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

2017Q4: 8.3%
2018Q1: 8.2%
2018Q2: 8.8%

September 10, 2018 collections: 10.0%



* Adjusted for large one-time transactions, amnesty payments and reporting frequency change, current definition of Revenue Act
Source: DOR and ERFC; monthly data through July 2018 activity

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Taxable REET activity may have peaked in Q1 2018

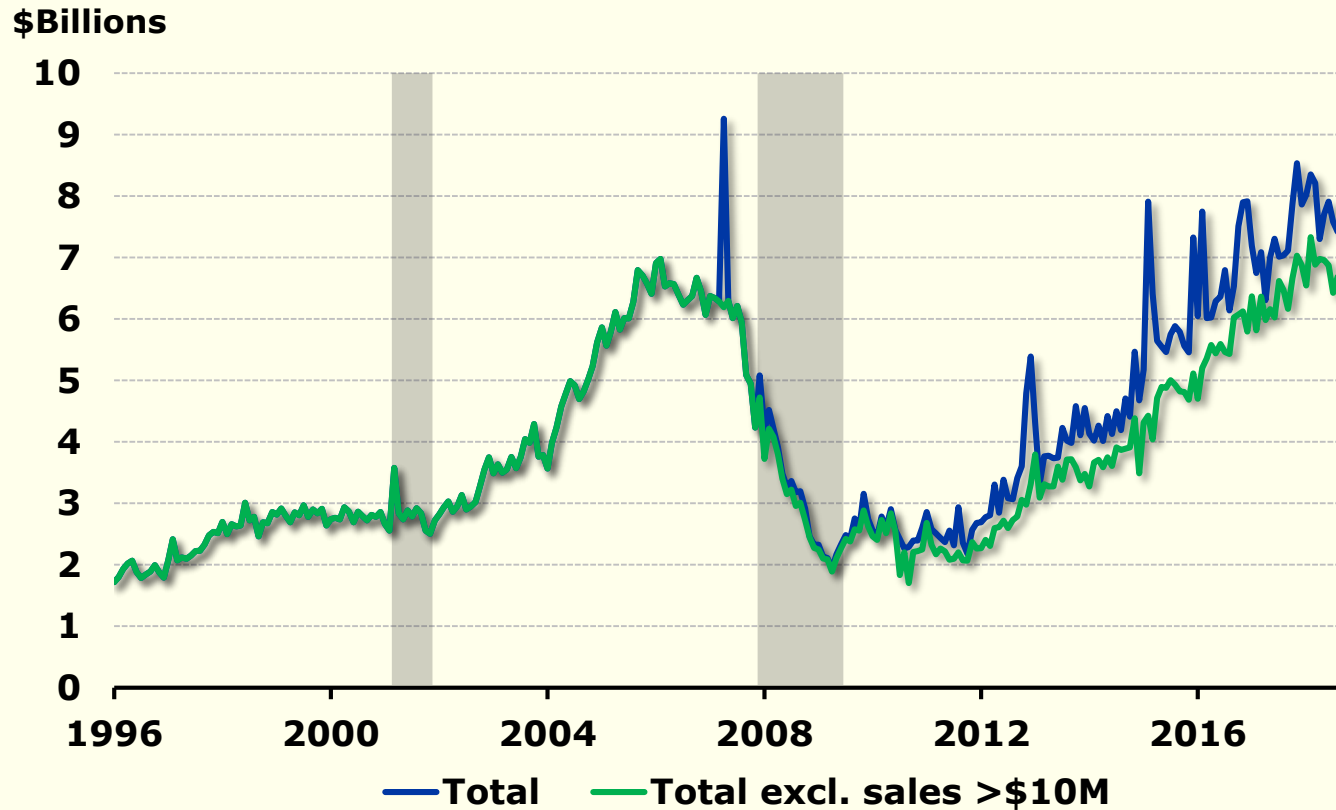
Taxable activity in residential sales has been on a downward trend since March.

Large commercial sales (>\$10 million) have slowed but have been over \$2 billion per quarter in 2018.

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Slide 23

Seasonally Adjusted Taxable Real Estate Excise Activity

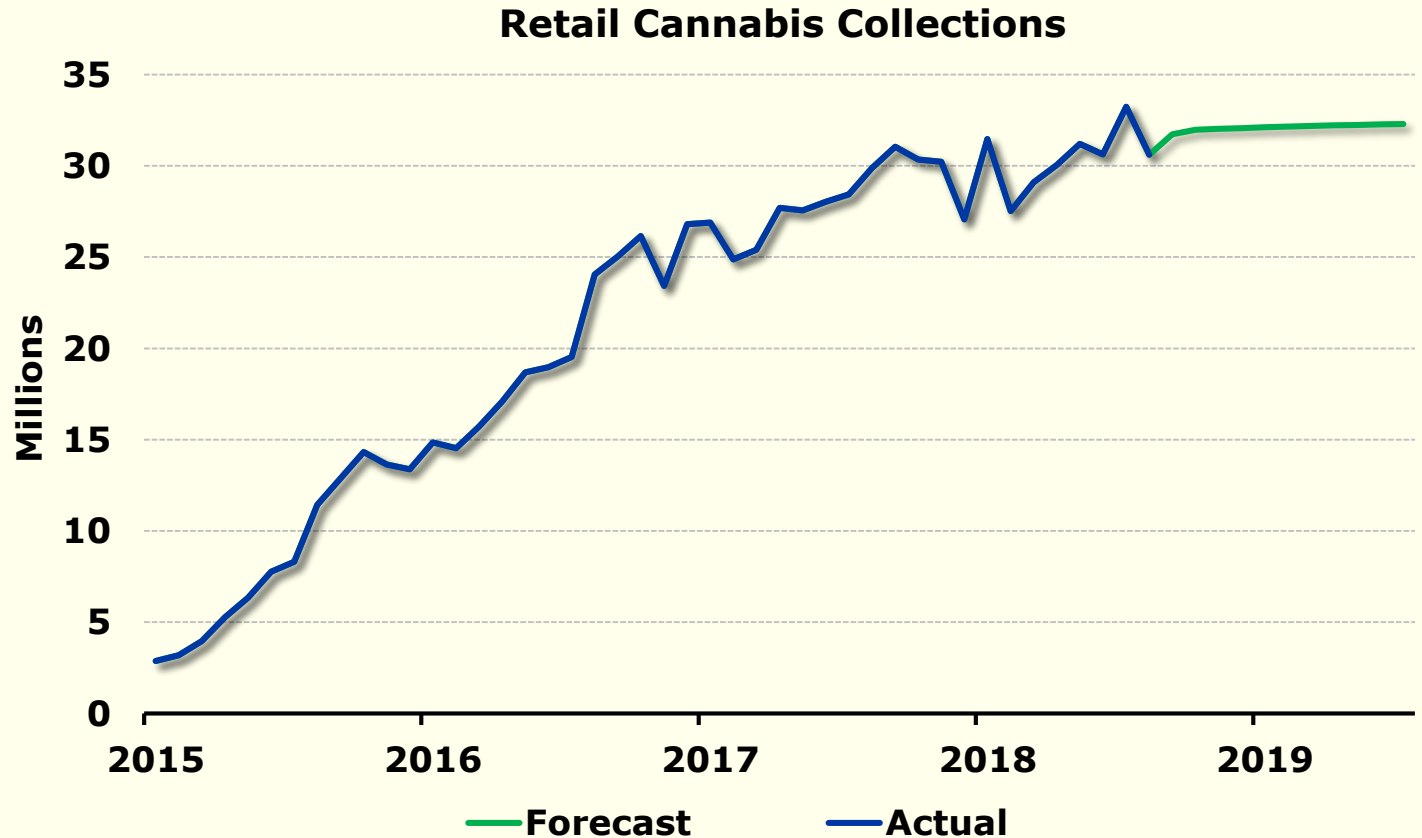


Source: ERFC; Monthly data through August 2018 preliminary

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The rapid growth in cannabis revenue is likely over



Source: ERFC September 2018 forecast; historical data through August 2018

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

As of September 10, General Fund-State collections were \$147 million higher than the June forecast.

\$Millions	<u>June 2018 Forecast*</u>	<u>Non-economic Change</u>	<u>Forecast Change</u>	<u>September 2018 Forecast</u>	<u>Total Change#</u>
General Fund-State	\$43,532	\$0	\$275	\$43,808	\$275
Education Legacy Trust Account	\$1,498	\$0	\$65	\$1,563	\$65
WA Opportunity Pathways Account	\$258	\$0	\$8	\$266	\$8
Total Near GF-S	\$45,288	\$0	\$348	\$45,636	\$348

* Forecast for the 2017-19 biennium adopted June 19, 2018

Detail may not add to total due to rounding

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October 10, 2018



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

\$Millions	<u>June 2018 Forecast*</u>	<u>Non-economic Change**</u>	<u>Forecast Change</u>	<u>September 2018 Forecast</u>	<u>Total Change#</u>
General Fund-State	\$48,520	\$38	\$317	\$48,875	\$355
Education Legacy Trust Account	\$582	\$0	\$87	\$669	\$87
WA Opportunity Pathways Account	\$261	\$0	\$1	\$262	\$1
Total Near GF-S	\$49,363	\$38	\$405	\$49,806	\$443

* Forecast for the 2019-21 biennium adopted June 19, 2018

** Estimated increase in sales tax collections due US Supreme Court ruling of June 21, 2018.

Detail may not add to total due to rounding

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Cannabis excise tax and license fee estimates

Total change since June forecast:

- 2017-19
+\$0.1 M
- 2019-21
-\$0.2 M
- 2021-23
-\$4.0M

\$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	\$317
Non-GF	\$501	\$530	\$530
Total	\$749	\$798	\$847

* 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[#]
September 2018 Baseline (70%)	\$43,808	
<u>September 2018 Alternative Forecasts</u>		
Optimistic (15%)	\$44,402	\$594
Pessimistic (15%)	\$43,138	(\$669)
Probability Weighted Average	\$43,796	(\$11)
GCEA*	\$43,619	(\$189)

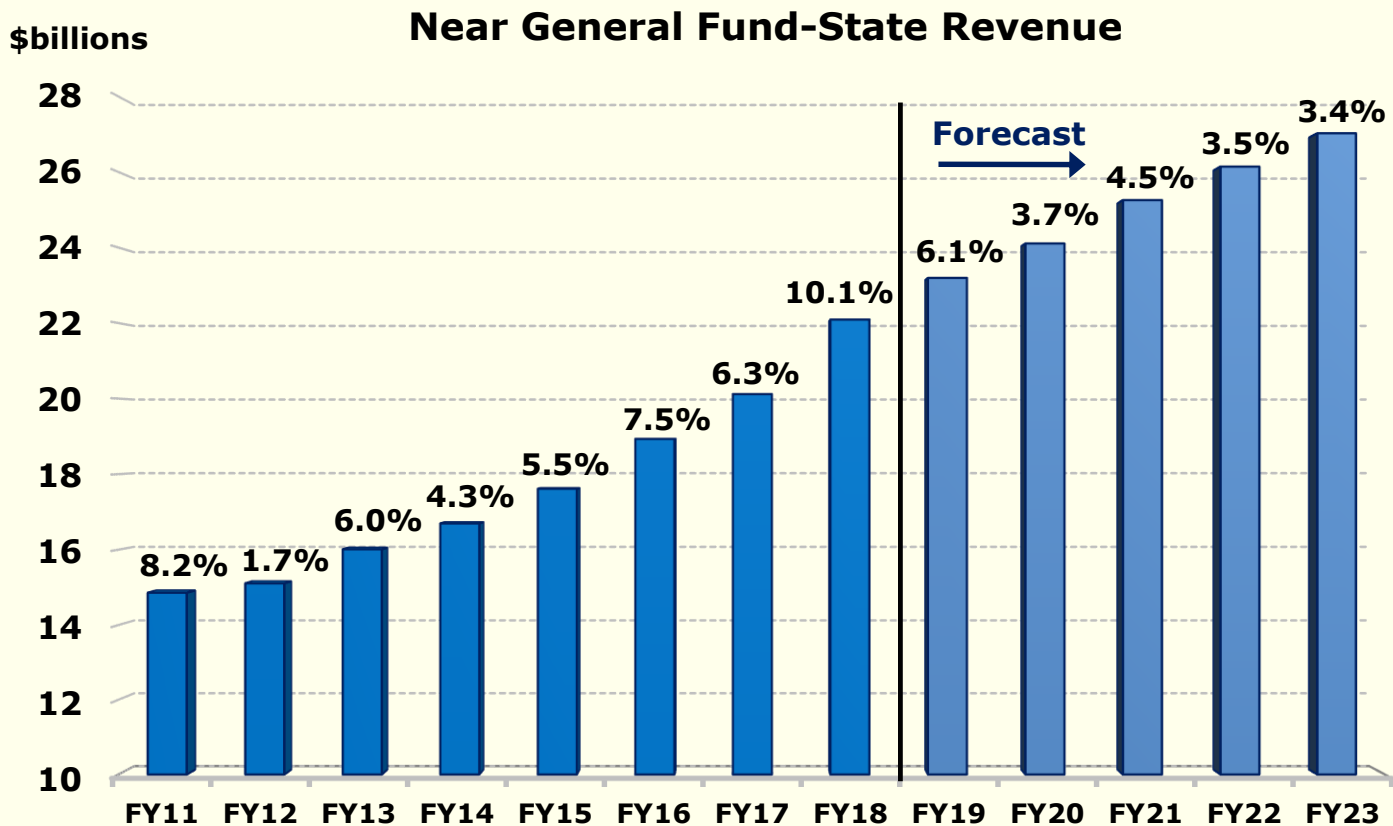
*Based on the Governor's Council of Economic Advisors' economic assumptions

#May not add to total due to rounding

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Near General Fund-State* forecast by fiscal year





Conclusion

- WA personal income and employment are higher than in June
- 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 16.9% between the 2015-17 and 2017-19 biennia and 9.1% 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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October 10, 2018

Slide 31