Washington State Economic Update

Presented to
Roundtable of Thurston County

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Executive Director

April 11, 2019
Olympia, WA
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
ERFC Forecast Process

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

- U.S., WA forecasts similar to the November forecast
- Baseline forecast has slowing growth but no recession
- Wage growth and inflation remain moderate
- Downside risks to the baseline include uncertainty regarding trade and fiscal policy, geopolitical concerns and a maturing economic expansion
- 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
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

- China – U.S. trade deal no longer seems imminent
Consumer confidence dipped in late 2018 but has partially recovered, remains strong.

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

Sources: University of Michigan, Conference Board; data through March 2019
Small business optimism has weakened recently but remains strong

Source: National Federation of Independent Business; data through Feb. 2019
Job openings continue to grow at a strong pace

An average of 5.7 million jobs were open in 2018.

WA, U.S. unemployment rates are below pre-recession levels

U.S. job growth slowed in February but picked up in March

Nominal wage growth has averaged 3.3% in last 12 months regardless of educational level

Source: Federal Reserve Bank of Atlanta, data through Feb. 2019
Exports to China are declining

After four quarters of year over year growth, WA exports declined in 2018 Q4.

Source: WISERTrade; data through 2018 Q4
After four consecutive quarters of growth, WA exports declined in the fourth quarter of 2018

<table>
<thead>
<tr>
<th>Year</th>
<th>Growth</th>
</tr>
</thead>
<tbody>
<tr>
<td>2017Q4</td>
<td>0.6%</td>
</tr>
<tr>
<td>2018Q1</td>
<td>3.9%</td>
</tr>
<tr>
<td>2018Q2</td>
<td>3.7%</td>
</tr>
<tr>
<td>2018Q3</td>
<td>2.6%</td>
</tr>
<tr>
<td>2018Q4</td>
<td>-2.7%</td>
</tr>
</tbody>
</table>

Source: WISERTrade; data through 2018 Q4
The Case-Shiller index for Seattle rose by 0.3% in January after decreasing for six consecutive months.

Source: Case-Shiller, data through January 2019
Relative to population, WA residential construction activity is stronger than the U.S.

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

WA personal income growth has outpaced the U.S. in 26 of last 36 quarters

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

Source: U.S. Bureau of Economic Analysis, data through 2018 Q4
U.S. retail sales growth has slowed recently

Year over year growth, %

Source: U.S. Census Bureau data through January 2019
Business investment trended down in last five months of 2018

Source: U.S. Census Bureau; data through Feb. 2019
By 2029, federal debt is expected to reach 93% of GDP

Source: Congressional Budget Office: Budget and Economic Outlook, Jan. 2019
Leading economic indexes for WA, U.S. dipped recently but do not suggest a recession in near term.

Source: Federal Reserve Bank of Philadelphia, data through Dec. 2018
OECD leading index suggests slowing growth in next 6 – 9 months

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

Source: Organization for Economic Cooperation and Development, data through Jan. 2019
An inverted yield curve (short-term interest rates > long-term rates) is a consistent recession predictor.

Although not apparent with the monthly averages shown here, the yield curve inverted from Mar. 22\textsuperscript{nd} until Mar. 28\textsuperscript{th}.

Timing of next recession: National Assoc. of Business Economists survey

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

GCEA members:
Average probability of recession in next 12 months = 36%

Recession probabilities in next 12 months based on economic and financial markets data

The probabilities are derived from models developed by Moody’s Analytics.

Source: Moody’s Analytics, October 2018 – February 2019
Due to the partial Federal government shutdown, 2018 Q4 data, which was released Feb. 28th, was not available for the ERFC March forecast.

Source: U.S. Bureau of Economic Analysis. Data through Q4 2018
Many forecasters expect U.S. economic growth to slow further.
GDP is slightly lower than in November

Source: ERFC March 2019 forecast; historical data through 2018
Oil prices are slightly lower than in the November forecast

Source: Energy Information Administration, IHS Markit, ERFC; data through Q4 2018
Note: Vertical black line indicates last actual
The Federal Reserve is not expected to raise interest rates as high as anticipated in November.

Source: ERFC March 2019 forecast; historical data through Q4 2018
U.S. nonfarm payroll employment growth is very similar to the November forecast.

Source: IHS Markit, ERFC; data through Q4 2018
Note: Vertical black line indicates last actual
Washington personal income is slightly lower than in November

Source: ERFC March 2019 forecast; historical data through 2017
Washington employment forecast is slightly lower than in November.

Washington Nonfarm Payroll Employment

Source: ERFC March 2019 forecast; historical data through Q4 2018
Online retail employment forecast consistent with press comments about future hiring plans

Source: ERFC March 2019 forecast; historical data through Q4 2018
Permits forecast for 2019 – 2023: average unchanged, timing slightly different compared to November.

Source: ERFC March 2019 forecast; historical data through 2018
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%
2018Q3: 7.6%
2018Q4: 7.4%

* 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
Adjusted Rev Act growth YOY:

18Q1: 8.2%
18Q2: 8.8%
18Q3: 7.6%
18Q4: 7.5%

November personal income YOY growth estimates:

18Q1: 7.3%
18Q2: 7.0%
18Q3: 6.9%
18Q4: 6.2%

Source: ERFC; Quarterly revenue data through Q4 2018, March 2019 income estimates

*Adjusted for large one-time payments and refunds and payments under the amnesty program

WASHINGTOLON 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.

Source: ERFC; Monthly data through February 2019 preliminary
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

Source: ERFC March 2019 forecast; historical data through 2018
Cannabis revenue growth is expected to moderate

Source: ERFC March 2019 forecast; historical data through February 2019
Cannabis excise tax and license fee estimates

<table>
<thead>
<tr>
<th></th>
<th>2017-19</th>
<th>2019-21</th>
<th>2021-23</th>
</tr>
</thead>
<tbody>
<tr>
<td>GF-S share of excise</td>
<td>$247</td>
<td>$272</td>
<td>$291</td>
</tr>
<tr>
<td>tax and license fees</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Non-GF</td>
<td>$501</td>
<td>$527</td>
<td>$545</td>
</tr>
<tr>
<td>Total</td>
<td>$749</td>
<td>$799</td>
<td>$836</td>
</tr>
</tbody>
</table>

Total change since November forecast:
- 2017-19: +$0.02M
- 2019-21: +$1.67M
- 2021-23: -$2.85M

* Detail may not add to total due to rounding
Forecast changes: Near General Fund-State, 2017-2019 biennium

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

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

As of March 11, General Fund-State collections were $245.0 million higher than the November forecast.
### Forecast changes: Near General Fund-State, 2019-2021 biennium

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<th>$Millions</th>
<th>November 2018 Forecast*</th>
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<th>March 2019 Forecast</th>
<th>Total Change#</th>
</tr>
</thead>
<tbody>
<tr>
<td>General Fund-State</td>
<td>$49,064</td>
<td>$115</td>
<td>$430</td>
<td>$49,609</td>
<td>$545</td>
</tr>
<tr>
<td>Education Legacy Trust Account</td>
<td>$672</td>
<td>$0</td>
<td>$1</td>
<td>$673</td>
<td>$1</td>
</tr>
<tr>
<td>WA Opportunity Pathways Account</td>
<td>$266</td>
<td>$0</td>
<td>$8</td>
<td>$274</td>
<td>$8</td>
</tr>
<tr>
<td><strong>Total Near GF-S</strong></td>
<td><strong>$50,002</strong></td>
<td><strong>$115</strong></td>
<td><strong>$439</strong></td>
<td><strong>$50,555</strong></td>
<td><strong>$553</strong></td>
</tr>
</tbody>
</table>

* Forecast for the 2019-21 biennium adopted November 20, 2018
# Detail may not add to total due to rounding
Near GF-S forecast changes by source

Source: ERFC March 2019 forecast
## 2017-19 Biennium alternative General Fund-State forecasts

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

*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, March 2019
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.

- Threats to economic expansion include concerns about international trade and fiscal policy, geopolitical risks and a maturing expansion.

- 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.