

Economic Review Meeting

November 2, 2016



Washington State
Economic and Revenue Forecast Council

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WASHINGTON STATE
ECONOMIC AND REVENUE FORECAST COUNCIL

AGENDA

ECONOMIC REVIEW MEETING

November 2, 2016
2:30 p.m.

- Approval of meeting minutes:
 - ✓ September 21, 2016
 - ✓ September 7, 2016
 - ✓ June 15, 2016
- Preparation of the November 2016 Budget Outlook
- Presentation of economic outlook and revenue collection experience

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STATE OF WASHINGTON

ECONOMIC AND REVENUE FORECAST COUNCIL

Capitol Plaza Building, PO Box 40912 □ Olympia, Washington 98504-0912 □ (360) 534-1560

Meeting Minutes Revenue Review

September 21, 2016

John L. O'Brien, Hearing Room D

Economic and Revenue Forecast Council

Members Present

Andy Hill, Senate, Chair (via phone)
Terry Nealey, House of Representatives (via phone)
Timm Ormsby, House of Representatives
James McIntire, Treasurer
David Schumacher, Office of Financial Management

Staff

Steve Lerch, Executive Director, ERFC
Andy Toulon, House
Pam Davidson, OFM
Michael Bezanson, Senate

Call to Order

The meeting was called to order by Director Schumacher at 10:03 a.m.

Budget Outlook Presentation

Members of the Budget Outlook Work Group presented options on growth factors as requested by the Council. Questions were posed regarding long-term trends and the debt model. The Outlook Work Group members indicated that the Legislative Evaluation & Accountability Program committee (LEAP) has rebuilt the K-12 fiscal model so that it can now produce a four-year expenditure estimate as required by the budget outlook. Director Schumacher, Treasurer McIntire, and Representative Ormsby agreed that the Outlook should utilize the most robust numbers and be consistent with growth rates used by the Governor and legislative fiscal committees for budget purposes.

Motion

Director Schumacher moved to follow the staff recommendation regarding growth factors, including the use of the K-12 fiscal model, in the Budget Outlook process. The motion was seconded by Treasurer McIntire. The motion passed at 10:14 a.m.

Forecast Presentation

Dr. Lerch presented information on the final economic and revenue forecast. Dr. Lerch summarized the forecast changes. Discussion ensued regarding the long-term relationship between personal income and state revenues and the pessimistic forecast.

Motion

Representative Ormsby moved, seconded by Treasurer McIntire, that the baseline revenue forecast be adopted. Council unanimously approved the motion at 10:30 a.m.

Adjournment

Meeting adjourned at 10:31 a.m.

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Capitol Plaza Building, PO Box 40912 □ Olympia, Washington 98504-0912 □ (360) 534-1560

**Meeting Minutes
Economic Review**

September 7, 2016

John L. O'Brien, Hearing Room D

Economic and Revenue Forecast Council

Members Present

Jim Hargrove, Senate

Timm Ormsby, House of Representatives (via phone)

Terry Nealey, House of Representatives (via phone)

David Schumacher, Office of Financial Management

Staff

Steve Lerch, Executive Director, ERFC

Call to Order

The meeting was called to order by Director Schumacher at 10:06 a.m.

Presentation on the Economic Forecast

Dr. Lerch presented information on the economic forecast. Dr. Lerch summarized the forecast changes and provided background information on both the U.S. and Washington economies. Discussion ensued regarding labor productivity, housing outside of the Seattle metro area, and sales tax on electronic sales.

Adjournment

Meeting adjourned at 10:22 a.m.

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STATE OF WASHINGTON

ECONOMIC AND REVENUE FORECAST COUNCIL

Capitol Plaza Building, PO Box 40912 □ Olympia, Washington 98504-0912 □ (360) 534-1560

**Meeting Minutes
Revenue Review**

June 15, 2016

John L. O'Brien, Hearing Room D

Economic and Revenue Forecast Council

Members Present

Andy Hill, Senator, Chair (via phone)
Jim Hargrove, Senator
Terry Nealey, House of Representatives (via phone)
Timm Ormsby, House of Representatives (via phone)
James McIntire, Treasurer (via phone)
David Schumacher, Office of Financial Management

Staff

Steve Lerch, Executive Director,
ERFC

Call to Order

The meeting was called to order by Director Schumacher at 10:02 a.m.

Motion

Representative Ormsby made a motion to approve the meeting minutes from June 1, 2016, seconded by Director Schumacher. Council approved the motion at 10:02 a.m.

Forecast Presentation

Dr. Lerch presented information on the final economic and revenue forecast. Dr. Lerch summarized the forecast changes. Discussion ensued regarding housing permits, growth rates, and revenue forecast drivers including real estate excise taxes and retail sales tax.

Motion

Representative Ormsby moved, seconded by Director Schumacher, that the baseline revenue forecast be adopted. Council unanimously approved the motion at 10:23 a.m.

Adjournment

Meeting adjourned at 10:37 a.m.

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To: Economic and Revenue Forecast Council

From: State Budget Outlook Work Group

Subject: Preparation of the November 2016 Outlook

In this document, the State Budget Outlook Work Group (work group): (1) notes several analytical approaches it is taking for the November 2016 Outlook for concurrence by the Economic and Revenue Forecast Council (ERFC); and (2) raises several questions for the ERFC to provide guidance on in the preparation of the November 2016 Outlook.

(1) Methodology Notes

Resource Updates

- The November 2016 Outlook will be updated for the November 2016 revenue forecast. However, the Budget Stabilization Account (BSA) transfer and the extraordinary revenue growth (ERG) calculation based on the November 2016 forecast will not be available. The work group will use the BSA transfer and ERG calculation from the September 2016 forecast.
- Reversions for fiscal year 2016 will reflect actuals. Future year reversion assumptions will not be changed.

Maintenance Level Updates

The November 2016 Outlook will begin with a preliminary estimate by the Office of Financial Management of the 2017-19 projected maintenance level costs (with some possible adjustments by the workgroup if necessary). These estimates reflect projected expenditures based on the estimated cost of providing ongoing services currently authorized in the 2015-17 budget and any mandatory items that start in 2017-19. The 2017-19 maintenance level projection will be the basis for the 2019-21 projection using the outlook growth factors and adding any mandatory items that start in 2019-21. This estimate of the Governor's projected maintenance level is not final.

Outlook Growth Factors

At its September 21, 2016 meeting, the ERFC adopted updated growth factors for the Outlook. These updated growth factors will remain constant for Outlooks prepared during the 2017-19 biennium, from November 2016 through the Outlook on the enacted 2018 supplemental budget, unless otherwise modified by the ERFC.

(2) Questions posed by the Workgroup for guidance on how to proceed with preparing the draft November 2016 Outlook

2017 Supplemental Budget

A 2017 supplemental budget will affect the beginning balance in FY 2018 for the 2017-19 biennium. For the November 2016 Outlook: (1) should the Work Group include a proxy for 2017 supplemental appropriations such as agency requested FY 2017 supplemental budget items that appear at maintenance level; or (2) ignore the 2017 supplemental?

Ballot Initiatives

There are six initiatives on the statewide ballot. The fiscal impacts for these initiatives indicate that three would have a quantifiable impact on NGF-P resources and/or expenditures; one would have an indeterminate impact, and two would have no impact. The election results will not be officially certified until November 29th, after the November Outlook is presented to the ERFC on November 16th. The Outlook Work Group needs guidance from the ERFC on whether the November Outlook should reflect the initiative costs based on initial election results.

If the ERFC would like to include initiatives which appear to be passing based on initial election results and have a quantifiable fiscal impact, the Work Group proposes the November Outlook would reflect the fiscal impact statement as prepared by the Office of Financial Management. It should be noted that there is discretion regarding the phase in of costs and other funding levels; actual funding levels would be determined through the Legislative process.

Following is a breakout of the six initiatives on the November 2016 statewide ballot:

Initiatives with quantified fiscal impacts based on the fiscal impact statements:

- Initiative Measure No. 732 concerning taxes (\$834 million net loss)
- Initiative Measure No. 1433 concerning labor standards (\$21 million net gain)
- Initiative Measure No. 1464 concerning campaign finance laws and lobbyists (\$1.8 million net gain)

Initiative with indeterminate fiscal impact based on the fiscal impact statements:

- Initiative Measure No. 1491 concerning court-issued extreme risk protection orders temporarily preventing access to firearms

Initiatives with no fiscal impacts based on the fiscal impact statements:

- Initiative Measure No. 1501 concerning seniors and vulnerable individuals
- Initiative Measure No. 735 concerning a proposed amendment to the federal constitution

Other Items

The Outlook on the Enacted 2016 Supplemental budget included items affecting the ensuing biennia, both 2017-19 and 2019-21, that are not fully reflected in either carry-

forward or maintenance level for 2017-19. In addition, there are potential new items that have not been previously included.

Should the November 2016 Outlook separately reflect these items:

- Early Childhood Education and Assistance Program (ECEAP) entitlement and phase-in. ECEAP costs are part of the November Outlook because it includes costs at the current funded level through FY 2021. There are currently 11,691 funded ECEAP slots. Under current law, ECEAP becomes an entitlement in FY 2021. Current caseload projections estimate the demand for ECEAP slots in FY 2021 at over 19,000 slots. The annual cost of each 1,000 ECEAP slots is approximately \$7.6 million.

RCW 43.215.456 requires a phase in of ECEAP funding but does not specify how to phase in the program. Should the November 2016 outlook reflect funding growth for the entitlement only in FY 2021 or assume some phase-in and if so what level of phase in?

- Hepatitis C Medications. Prior to recent court rulings, authorization for new medications which provide treatment for Hepatitis C required some documentation that the virus was having a clinical impact on the patient such as evidence of liver scarring. Preliminary injunctions enjoining this practice were ordered by judges in cases involving both the Medicaid program (May 2016) and the Public Employee Benefits Program (August 2016.) Assuming these injunctions are not overturned on appeal, the costs associated with the Medicaid program would typically be considered maintenance level and therefore included in the November 2016 outlook. The costs associated for PEBB would typically be considered policy level and not included in the November 2016 outlook. Should the November 2016 outlook reflect the costs associated with eliminating restrictions to Hepatitis C treatment based on liver scarring for the Medicaid program and/or the PEBB program?
- Elimination of school district dependency on local levies for implementation of the state's program of basic education (compensation element of *McCleary*). During the 2016 session, language in the enacted operating budget as well as language incorporated in E2SSB 6195 provided general legislative commitments for legislative acts in 2017 to eliminate school district dependency on local levies to fund the program of basic education. To be implemented, these changes would require additional specific policy action during the 2017 legislative session.

This summer the *McCleary* court requested that the state provide it with information on the full cost of implementing basic education in the 2017-19 biennium. The state explained that due to the need for additional research and legislative policy decisions to determine appropriate compensation allocations, the state could not provide the court with an amount certain. The court's October 6 order did not require the state to fund any specific expenditures. Instead, it

required the state to fully fund the program beginning with school year 2018-19, with appropriations and revenue sources in place by the adjournment of the 2017 legislative session.

For that reason, questions arise about how to treat this upcoming compensation obligation in the outlook. Beginning with the 17-19 outlook, the *McCleary* exception in RCW 43.88.055 does not apply to the ensuing biennium. RCW 82.33.060, which governs what costs must be included and excluded from the outlook, requires that estimates for ensuing biennium expenditures exclude the costs of policy items for legislation that has not yet been enacted by the legislature:

*The estimate of ensuing biennium expenditures must include maintenance items including, but not limited to, continuation of current programs, forecasted growth of current entitlement programs, and **actions required by law**, including legislation with a future implementation date. **Estimates of ensuing biennium expenditures must exclude policy items including, but not limited to, legislation not yet enacted by the legislature**, collective bargaining agreements not yet approved by the legislature, and changes to levels of funding for employee salaries and benefits unless those changes are required by statute. RCW 82.33.060(2)(a) (emphasis added)*

Actions required by a court could potentially be included under “actions required by law,” but the court at this stage has not required any specific actions or expenditure levels, and the state did not provide the court with any estimates. Because future *McCleary* compensation costs will be determined by upcoming legislative policy decisions, these costs would typically be considered policy level and not included in the November 2016 outlook.

As a policy level item, staff have no way to estimate new *McCleary* costs for the 17-19 and 19-21 biennia. (*McCleary* costs attributable to the remaining K-3 step are included, as they are both known and required by statute.) If the ERFC wants to include the *McCleary* compensation costs in the November 2016 Outlook, the ERFC would need to provide staff with a clearly stated set of compensation allocation assumptions that could be used to cost out an estimate as part of the official outlook.

**Economic & Revenue Forecast Council
State of Washington**



Economic Review: November 2, 2016

Executive Summary

- This preliminary forecast was based on a modified version of Global Insight's October 2016 Control forecast for the U.S. economy. As usual, we have adjusted real gross domestic product (GDP) to match the Blue Chip "Consensus" GDP forecast. The October Blue Chip forecast for real GDP growth in 2016 and 2017 was unchanged from September at 1.5% and 2.2%. The Blue Chip long term forecast, however, was revised down slightly to 2.1%, 2.1%, 2.1%, and 2.0% in 2018 through 2021 from 2.2%, 2.1%, 2.2%, and 2.1%.
- The first estimate of real GDP growth for the third quarter, 2.9%, was released after completion of our preliminary economic forecast. We will incorporate this information into our final economic forecast.
- Our oil price forecast reflects the futures markets, primarily the Brent (North Sea) oil price but also the West Texas Intermediate (WTI) benchmark. This forecast was based on the Wednesday, October 26, 2016 closing prices for Brent and WTI futures. The latest futures prices are slightly higher than the prices used in the September forecast. The refiner acquisition price of crude oil in the fourth quarter of 2016 is now expected to average \$47 per barrel compared to \$45 in the June forecast. As in September, oil prices are expected to rise gradually during the remainder of the forecast. By the end of 2021, the refiner acquisition price is expected to increase to \$57 per barrel.
- Global Insight revised their outlook for housing construction in their October forecast. The near-term forecast for housing starts is lower, the recovery is slower, and starts to plateau at a lower level than expected in September. The reasons cited for the lower projections are slower household formation as well as labor shortages, tighter lending standards, a shortage of developed lots, and unfavorable regulatory treatment of loans for land development. Our forecast for U.S. housing starts is virtually identical to Global Insight's. In our preliminary November forecast, starts average 1.161 million units (SAAR) in the fourth quarter of this year compared to 1.212 million units in the September forecast. Starts are now expected to plateau at 1.503 million units in 2021 compared to 1.656 million units in the September forecast.
- Through September 2016, the U.S. labor market expanded by a monthly average of 178,000 net new jobs, down from the 221,000 average monthly gain in 2015. Data for October employment will be incorporated into our final economic forecast.
- Two key measures of consumer confidence both indicated less optimism in October. The University of Michigan (UM) index of consumer sentiment decreased by 4.0 points to 87.2. After two consecutive gains, the Conference Board index of consumer confidence decreased 4.9 points to 98.6 in October. The Conference Board survey noted more pessimistic consumer assessments regarding the labor market and business conditions, while the decrease in the

UM index was attributed to less positive views on prospects for the economy despite optimism regarding personal finances.

- Initial claims for unemployment insurance decreased by 3,000 to 258,000 (SA) in the week ending August 27th. The four-week moving average of initial claims increased by 1,000 to 253,000.
- Industrial production increased by 0.1% (SA) in September. Despite increasing in three of the last four months, industrial production is 1.0% below its September 2015 level. New orders for core capital goods (i.e., durables excluding aircraft and military), which is a proxy for business investment, decreased by 1.2% (SA) in September according to preliminary Census data.
- U.S. housing data were generally stronger this month. Housing units authorized by building permits in September were 6.3% (SA) above their August level and 8.5% above their September 2015 level. September housing starts decreased for a second consecutive month, falling 9.0% (SA) compared to August and by 11.9% compared to their year-ago level. Existing home sales in September were 3.2% (SA) above their August level after two consecutive monthly declines. Existing home sales are now 0.6% above September 2015 sales. New single family home sales increased from a revised 575,000 (SAAR) in August to 593,000 in September, an increase of 3.1%. New single family home sales are now 29.8% above their year-ago level. The seasonally adjusted Case-Shiller national home price index for August was 0.6% above its July level and 5.3% above its year-ago level.
- Major threats to the U.S. and Washington economies remain, including a slowing U.S. and global economy, weaker export growth, and slow growth in labor productivity.

Washington

- We have just one month of new Washington employment data since the September forecast was released. Total nonfarm payroll employment rose 6,000 (seasonally adjusted) in September, which was 2,900 more than the 3,000 expected in the September forecast. The manufacturing sector accounted for much of the variance in job growth with no net change in jobs in September; the September forecast had expected a reduction of 1,200 manufacturing jobs. The aerospace sector was expected to shed 1,500 jobs but instead added 200. Construction employment increased 1,000 and government payrolls expanded by 800 jobs. As is usually the case, the bulk of the job growth was in private, service-providing sectors which added 4,000 jobs in September.
- Though aerospace employment rose slightly in September, we have retained the overall decline in aerospace employment implied by the Boeing announcement earlier this year. In 2017 through 2019 we expect a more gradual decline in aerospace employment similar to the assumption made in September. We project no change in aerospace employment in the final two years of the forecast.
- We have also incorporated another quarter of benchmark employment data from the Quarterly Census of Employment and Wages (QCEW). The new

- QCEW data and other revisions raised the estimated level of total employment in August 2016 by 3,600 jobs (0.1%). As a result of the upward revision to history and stronger-than-expected growth, the total effect is 6,500 (0.2%) more jobs in September 2016 than expected in the September forecast.
- In September, the Bureau of Economic Analysis released estimates for state personal income through the second quarter of 2016. This release also reflected the results of the annual revision to the national income and product accounts (NIPA). We have incorporated the new BEA estimates as well as additional Washington Quarterly Census of Employment and Wages (QCEW) and other wage data also through the second quarter. Our current estimate of Washington personal income in the second quarter of 2016 is \$388.3 billion which is \$5.1 billion (1.3%) higher than assumed in the September forecast. Wages and salaries were \$1.6 billion higher than believed in September and other sources of personal income were \$3.5 billion higher. The large increase in the estimate of nonwage income was due to the annual NIPA revision.
 - Washington housing construction was weaker than expected in the third quarter. Washington housing units authorized by building permits averaged 38,400 units (SAAR) in the third quarter of 2016, down from 45,300 in the second quarter. The September forecast expected an average rate of 40,500 units in the third quarter. Multi-family permits averaged 17,900 units in the third quarter which was exactly the amount expected in the September forecast. Single-family permits, however, averaged 20,500 units in third quarter which was 2,100 fewer than expected.
 - Seattle home prices continue to rise rapidly. According to the S&P/Case-Shiller Home Price Indices, seasonally adjusted Seattle area home prices rose 0.8% in August following four monthly increases that averaged just 0.4%. As we have been saying, we believe the slowdown in April through July was due to problems with the seasonal adjustment process. A more reliable measure is the over-the-year growth which shows an 11.4% increase in prices since the previous August and which is more the double the 5.2% increase in the Composite-20 index. Seattle home prices are up 51.8% since the November 2011 trough and prices now exceed the May 2007 peak by 5.5%.
 - Seattle area consumer price inflation is well above the national average. Over the last year, from August 2015 to August 2016, consumer prices in the Seattle area rose 2.1% compared to 1.1% for the U.S. city average. Lower energy costs this year are helping to keep the headline rate down both nationally and in the Seattle area. Core prices, which exclude food and energy, were up 3.3% in Seattle compared to 2.3% for the nation. The higher Seattle inflation is due to more rapid growth in shelter costs. During the year, shelter costs in Seattle rose 6.1% compared to 3.4% for the nation. With shelter excluded, Seattle inflation was the same as the U.S. city average at 0.0% over the year.
 - The Institute of Supply Management - Western Washington Index (ISM-WW) edged back into positive territory in September after negative growth in August. The index, which measures conditions in the manufacturing sector, increased from 47.7 in August to 51.4 in September (index values above 50 indicate positive growth while values below 50 indicate contraction). The production, orders, employment, and deliveries components all increased in

September while the inventory component declined. Manufacturing has fluctuated around the 50 mark since mid-2015.

- Washington car and truck sales rebounded in September but remain below the post-recession peak. Seasonally adjusted new vehicle registrations rose 3.9% in September following declines of 0.9% in July and 0.3% in August. Car and truck sales are down 7.6% since the post-recession peak in January but are up 3.5% over the year.
- Washington employment is expected to grow 2.9% this year, up slightly from 2.8% in the September forecast. As in September, we expect growth to gradually decelerate as the recovery matures. We expect employment growth to average 1.4% per year in 2017 through 2021 which is slightly higher than the 1.3% rate assumed in September. As in September, our preliminary forecast for nominal personal income growth this year is 4.8%. Our new forecast for nominal personal income growth in 2017 through 2021 averages 5.0% per year, also up slightly from the 4.9% rate in the September forecast.

Washington State Economic Outlook & Revenue Collection Experience

Presented to
The Economic & Revenue Forecast Council

Steve Lerch
Executive Director

November 2, 2016
Olympia, Washington



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ECONOMIC AND REVENUE FORECAST COUNCIL**

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Summary

- The U.S. preliminary economic forecast is similar to September; the WA preliminary forecast is slightly stronger
- The housing forecast is lower than September
- The forecast assumes the Federal Reserve will increase interest rates in December; two 0.25% rate increases are assumed during 2017
- Downside risks to the baseline also remain similar to those discussed in September: slow global and U.S. economic growth, the impact of a stronger dollar on exports, weak labor productivity growth
- Revenue collections since the September forecast are \$30 million (2.3%) above expectations

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Slide 1

WASHINGTON STATE ECONOMIC AND REVENUE FORECAST COUNCIL



Economic news continues to suggest risks to forecast

Upside:

- Stronger than expected Washington job growth
- Rising wage growth

Downside:

- Slowing U.S. and global economy
- Weaker economy leads to slower consumer spending
- Negative impact of stronger dollar on exports
- Slow growth in labor productivity

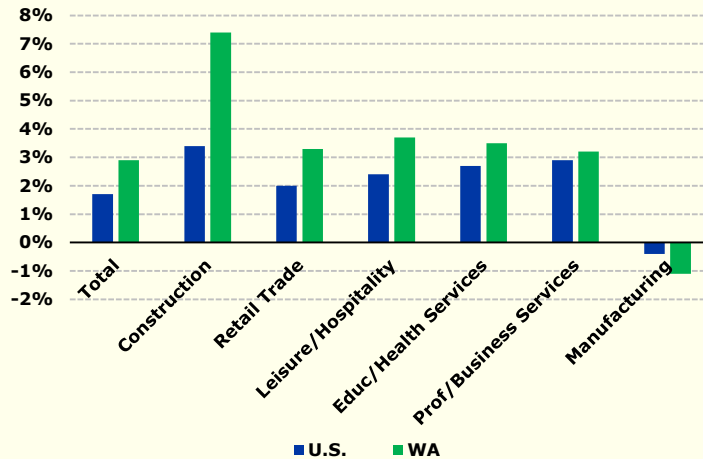
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Slide 2

WASHINGTON STATE ECONOMIC AND REVENUE FORECAST COUNCIL



Washington vs U.S. employment growth: Sept. 2015 to Sept. 2016



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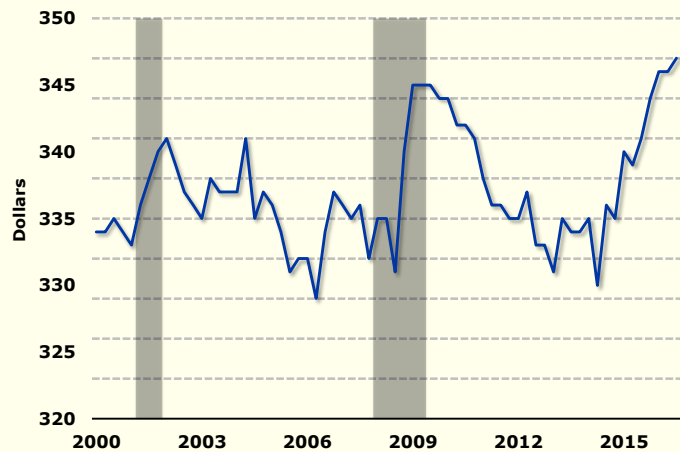
Slide 3

Source: Employment Security Dept., ERFC; data through Sept. 2016

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U.S. real median weekly wages, full time workers (1982-84 dollars)



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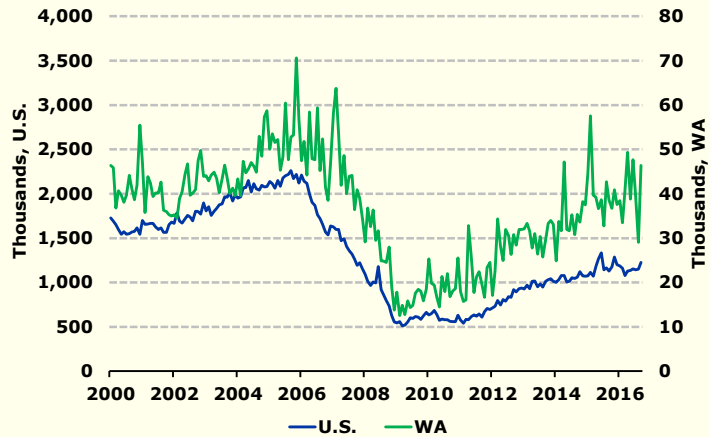
Slide 4

Source: U.S. Bureau of Labor Statistics, data through 2016 Q3

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U.S., WA housing permits trending up; U.S. remains below historical averages



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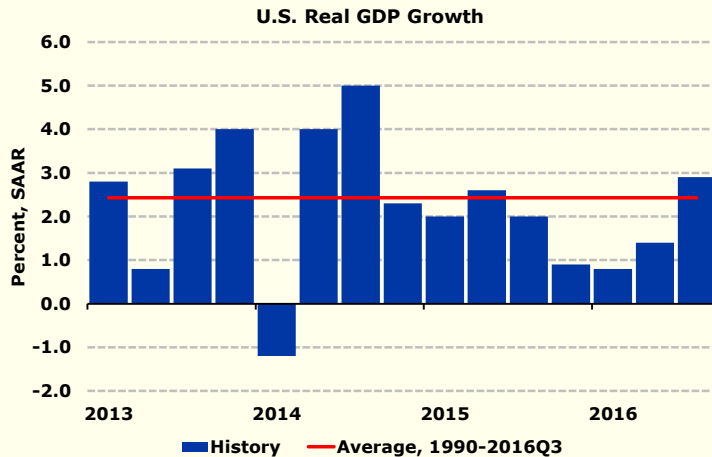
Slide 5

Source: U.S. Census Bureau, data through September 2016

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Third quarter GDP growth was highest in two years



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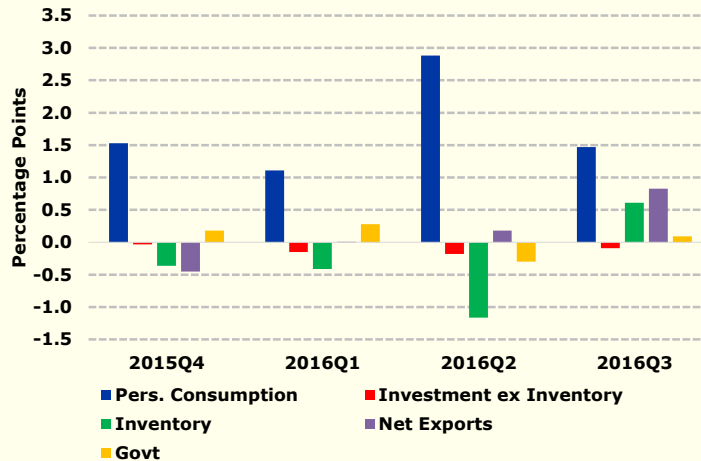
Source: U.S. Dept. of Commerce, BEA, data through 2016 Q3

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Contributions to percent change in real U.S. GDP

Net exports in Q3 were driven by record soybean exports due to a poor crop in South America



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Source: U.S. Bureau of Economic Analysis, data through 2016 Q3

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Household debt payments as a fraction of income have declined

Debt service includes mortgage, auto and other consumer debt payments



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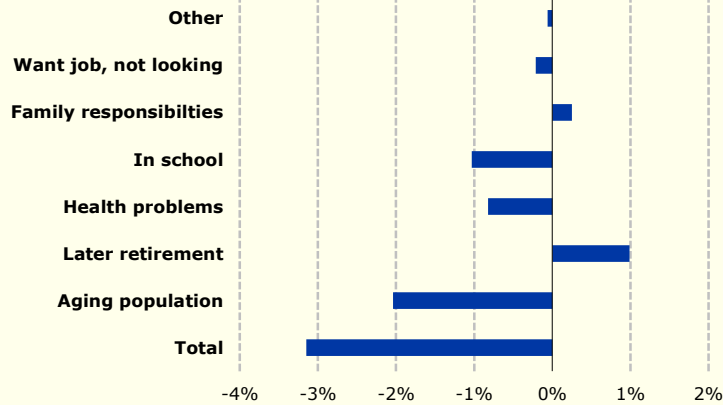
Source: Federal Reserve Board, data through 2016 Q2

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Components of change in labor force participation rate, 2007Q2 to 2016Q2



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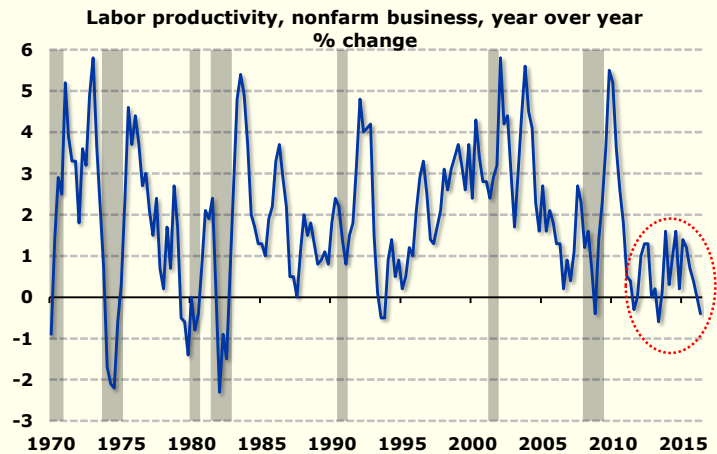
Slide 9

Source: U.S. Bureau of Labor Statistics, Atlanta Federal Reserve

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Labor productivity growth has remained low since 2011



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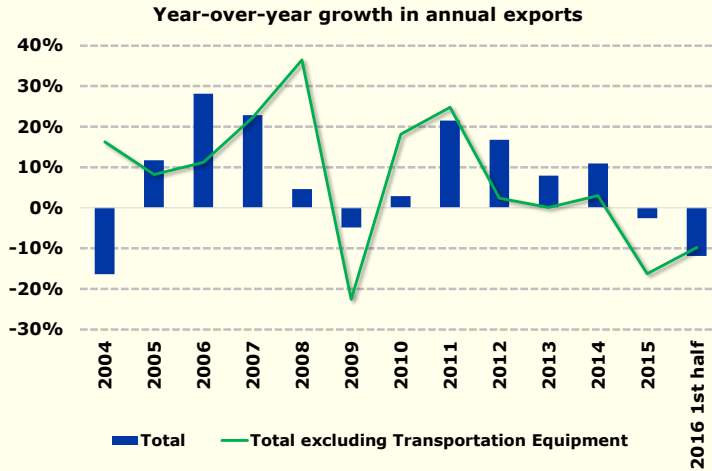
Slide 10

Source: U.S. Bureau of Labor Statistics, data through 2016 Q2

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Washington exports have weakened



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Source: WiserTrade; data through June 2016

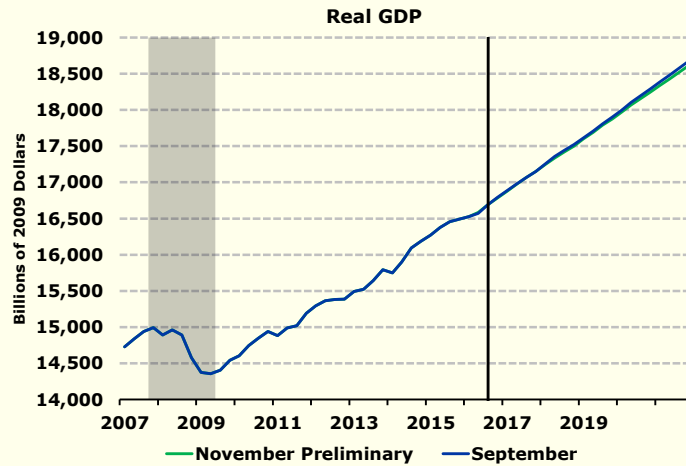
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Real GDP is similar to the September forecast

The long term forecast was revised down slightly.

The level at the end of 2021 is 0.3% lower than in the September forecast.



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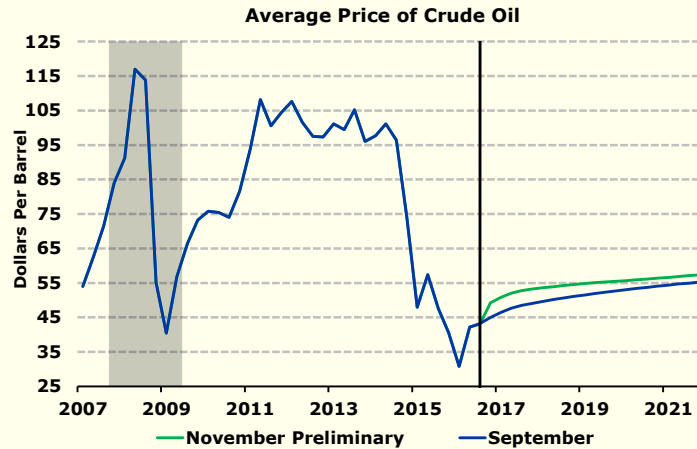
Slide 12

Source: ERFC November 2016 Preliminary forecast; data through Q2 2016

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Oil prices are slightly higher compared to the September forecast



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Slide 13

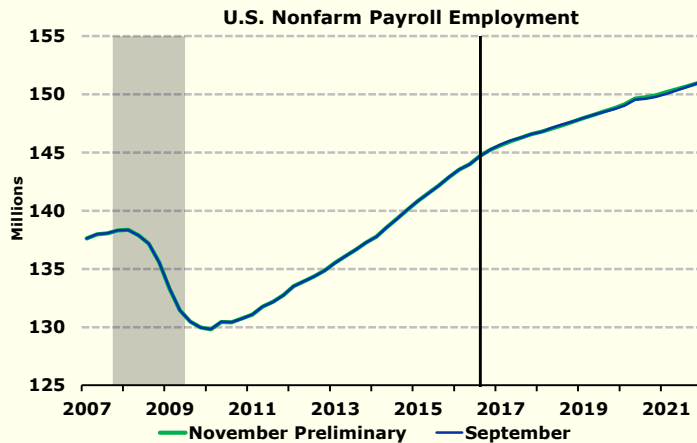
Source: DOE, ERFC November 2016 Preliminary forecast; historical data through 2016Q2

WASHINGTON STATE ECONOMIC AND REVENUE FORECAST COUNCIL



The U.S. nonfarm payroll employment forecast is nearly identical to September

Monthly employment growth averaged 146,000 in the second quarter and 192,000 in the third quarter.



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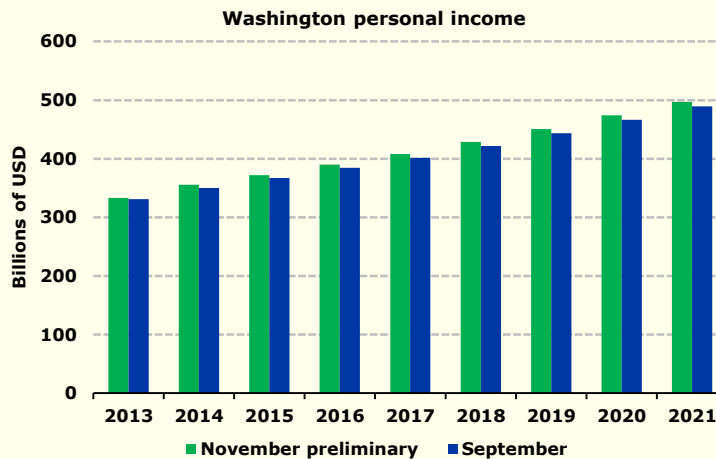
Slide 14

Source: ERFC November 2016 Preliminary forecast; data through Q3 2016

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Washington personal income is slightly higher than in September



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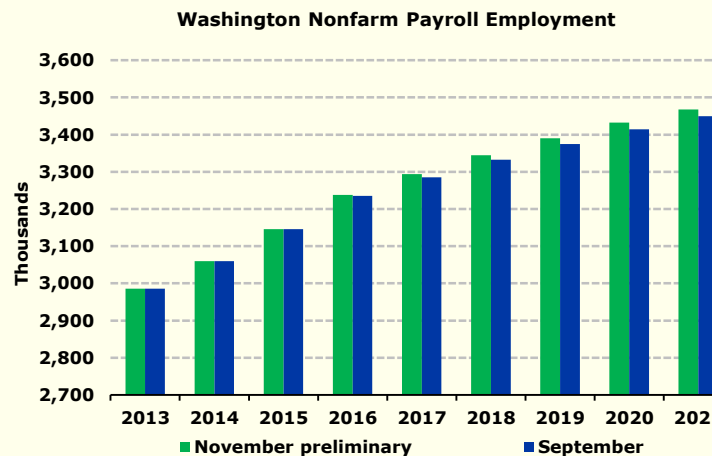
Slide 15

Source: ERFC November 2016 Preliminary forecast; historical data through 2015

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Washington employment forecast is slightly higher than in September



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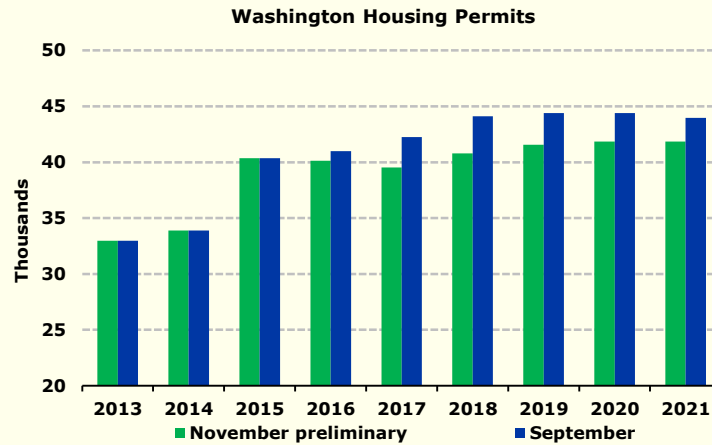
Slide 16

Source: ERFC November 2016 Preliminary forecast; historical data through 2015

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Washington housing permits forecast is lower compared to September



Economic Review
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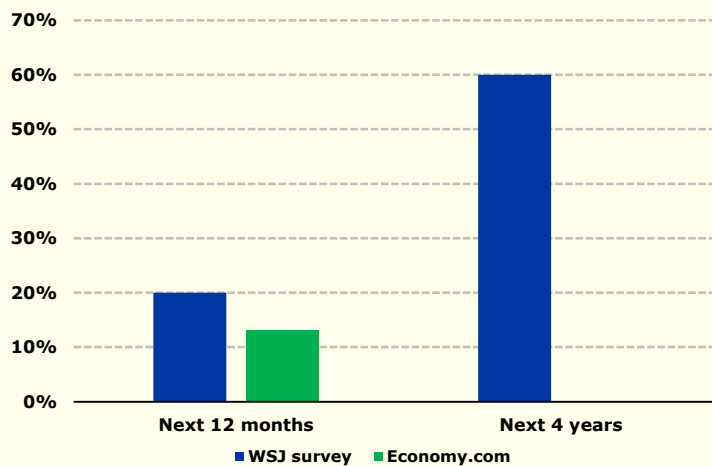
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Source: ERFC November 2016 Preliminary forecast; historical data through 2015

WASHINGTON STATE ECONOMIC AND REVENUE FORECAST COUNCIL



WSJ survey of economists finds low probability of recession in next year but much higher in next four years



Economic Review
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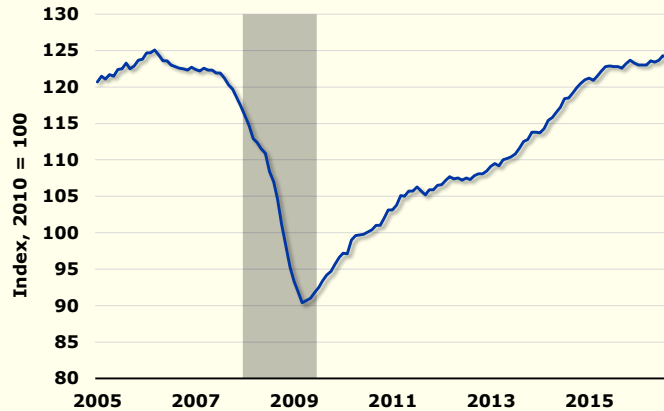
Source: Wall Street Journal, Moody's Economy.com; Oct. 2016

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U.S. Leading Economic Index trending up but at slower rate

The LEI is an index of economic indicators that tend to indicate the direction of economic growth



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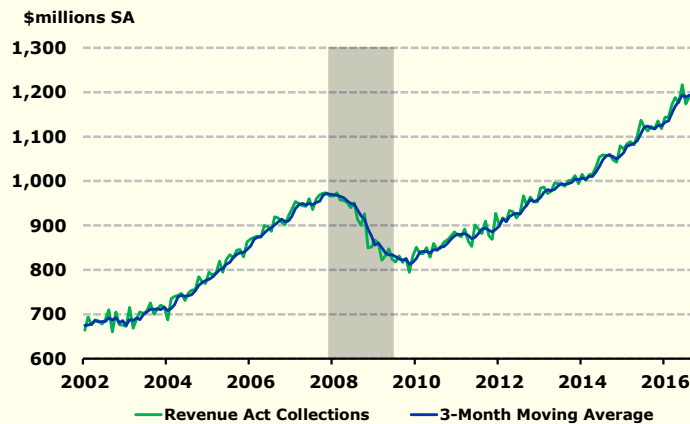
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Source: Conference Board, data through September 2016

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Revenue Act collections growth has slowed after August spike



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

Source: DOR and ERFC; monthly data through estimated August 2016 activity

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Large commercial property sales show continued strength as other activity grows

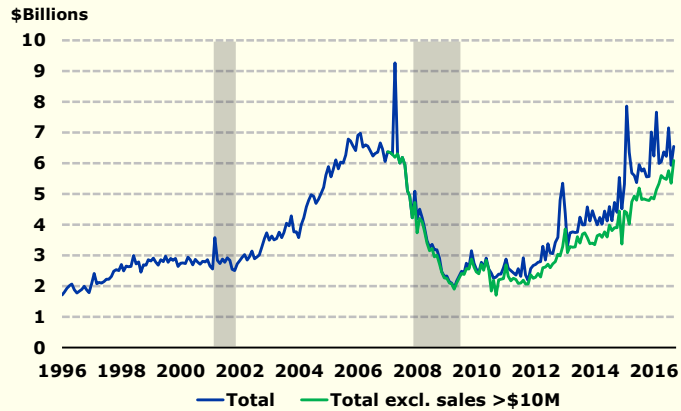
Large commercial sales (>\$10 million) were \$743 million in August and \$506 million in September.

Residential prices are still growing faster than sales volume.

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Seasonally Adjusted Taxable Real Estate Excise Activity



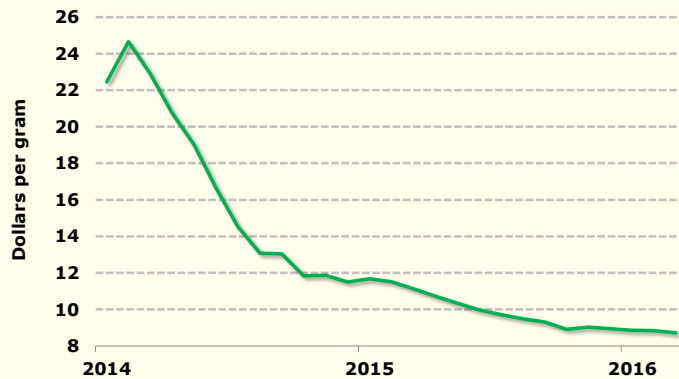
Source: ERFC; Monthly data through September 2016 preliminary

WASHINGTON STATE ECONOMIC AND REVENUE FORECAST COUNCIL



We are nearing a floor in the price of cannabis

Price of Recreational Cannabis Sold at Retail Stores



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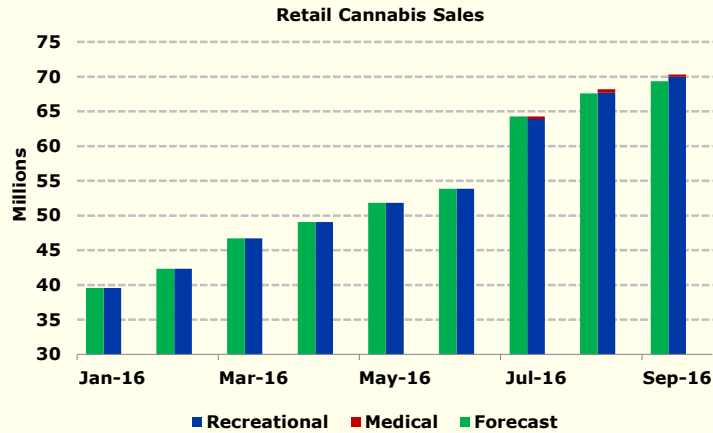
Source: LCB, ERFC; data through September 2016

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Cannabis revenue continues to increase

Retail medical sales became subject to the 37% excise tax on July 1, 2016



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Source: LCB, ERFC; data through September 2016

WASHINGTON STATE ECONOMIC AND REVENUE FORECAST COUNCIL



Revenue collections to date

**Collections Variance Since September Forecast
(September 11, 2016 – October 10, 2016)
dollars in thousands**

	<u>Estimate</u>	<u>Actual</u>	<u>Difference</u>	<u>Pct.</u>
Dept. of Revenue	\$1,338,619	\$1,369,228	\$30,609	2.3%
All other agencies	\$7,036	\$6,866	(170)	(2.4%)
Total GF-S	\$1,345,655	\$1,376,093	\$30,438	2.3%

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Conclusion

- The Washington economic forecast is slightly stronger than in September; we continue to expect moderate growth
- As has been the case for some time, Washington is continuing to outperform the nation by a small margin
- Threats to economic expansion include slower domestic and international economic growth, the impact of a stronger dollar on exports, and a slowdown in labor productivity
- The next monthly revenue collection report will be available on November 11th and the revenue forecast will be presented on November 16th

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Questions



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November 2, 2016

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Economic & Revenue Forecast Council
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Olympia WA 98504-0912

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U.S. Economic Forecast Comparison
October 2016

	2016Q3	2016Q4	2017Q1	2017Q2	2016	2017	2018	2019	2020	2021
Real GDP, Percent Change, Annual Rate										
ERFC (Preliminary November)	2.6	2.3	2.3	2.3	1.5	2.2	2.1	2.1	2.1	2.0
Global Insight	1.9	2.1	2.4	2.3	1.4	2.2	2.2	2.2	2.1	2.2
Economy.com	3.0	2.9	3.2	2.9	1.6	2.9	2.7			
Blue Chip Average*	2.7	2.3	2.2	2.3	1.5	2.2	2.1	2.1	2.1	2.0
Blue Chip Top 10*	3.2	2.8	2.7	2.7	1.6	2.5	2.5	2.5	2.5	2.4
Blue Chip Bottom 10*	2.3	1.8	1.7	1.8	1.4	1.9	1.5	1.6	1.6	1.6
Real Consumption, Percent Change, Annual Rate										
ERFC (Preliminary November)	2.7	2.4	2.4	2.4	2.6	2.5	2.2	2.2	2.1	2.1
Global Insight	2.9	2.6	2.1	2.3	2.7	2.5	2.3	2.5	2.3	2.3
Economy.com	3.0	2.8	3.5	3.2	2.7	3.2	3.1			
Blue Chip Average*	2.7	2.4	2.3	2.4	2.6	2.5	2.2	2.2	2.1	2.1
Blue Chip Top 10*	3.1	2.9	2.8	2.8	2.7	2.8	2.6	2.6	2.5	2.5
Blue Chip Bottom 10*	2.2	2.0	1.8	1.9	2.6	2.2	1.7	1.7	1.6	1.7
Federal Funds Rate										
ERFC (Preliminary November)	0.4	0.5	0.7	0.7	0.4	0.8	1.5	2.4	2.8	2.8
Global Insight	0.4	0.5	0.7	0.7	0.4	0.8	1.5	2.4	2.8	2.8
Economy.com	0.4	0.4	0.7	0.8	0.4	0.9	2.2			
Three Month T-Bill Rate										
ERFC (Preliminary November)	0.3	0.4	0.6	0.6	0.3	0.7	1.4	2.2	2.6	2.6
Global Insight	0.3	0.4	0.6	0.6	0.3	0.7	1.4	2.2	2.6	2.6
Blue Chip Average*	0.3	0.4	0.6	0.7	0.3	0.8	1.7	2.2	2.5	2.7
Blue Chip Top 10*		0.6	0.8	1.0	0.4	1.1	2.6	3.2	3.4	3.5
Blue Chip Bottom 10*		0.3	0.3	0.5	0.3	0.5	1.0	1.2	1.6	1.8
10-Yr. T-Note Yield										
ERFC (Preliminary November)	1.6	1.7	2.0	2.0	1.7	2.1	2.7	3.3	3.5	3.5
Global Insight	1.6	1.7	1.9	2.0	1.7	2.1	2.7	3.4	3.6	3.6
Economy.com	1.6	1.9	2.2	2.6	1.8	2.8	3.8			
Blue Chip Average*	1.6	1.7	1.8	2.0	1.7	2.1	2.8	3.1	3.4	3.6
Blue Chip Top 10*		1.9	2.1	2.4	1.8	2.6	3.7	4.0	4.4	4.3
Blue Chip Bottom 10*		1.5	1.5	1.6	1.6	1.7	2.0	2.2	2.5	2.7
Consumer Price Index, Percent Change, Annual Rate										
ERFC (Preliminary November)	2.1	3.6	2.0	2.8	1.4	2.6	2.3	2.2	2.3	2.3
Global Insight	1.7	3.2	1.9	3.2	1.3	2.5	2.4	2.6	2.5	2.4
Economy.com	1.4	2.3	2.4	2.9	1.2	2.4	2.7			
Blue Chip Average*	1.6	2.4	2.2	2.3	1.2	2.3	2.3	2.3	2.3	2.3
Blue Chip Top 10*	1.8	3.3	2.7	3.1	1.3	2.7	2.6	2.7	2.7	2.6
Blue Chip Bottom 10*	1.2	1.7	1.7	1.7	1.2	1.9	1.9	2.0	1.9	1.8
Payroll Employment, Millions										
ERFC (Preliminary November)	144.7	145.2	145.6	146.0	144.4	146.1	147.2	148.4	149.6	150.5
Percent Change, Annual Rate	2.0	1.4	1.1	1.0	1.8	1.2	0.8	0.8	0.8	0.6
Global Insight	144.6	145.1	145.5	145.8	144.3	146.0	147.2	148.7	150.0	151.2
Percent Change, Annual Rate	1.7	1.3	1.1	1.0	1.7	1.2	0.9	1.0	0.9	0.8
Economy.com	144.6	145.1	145.6	146.2	144.3	146.4	148.4			
Percent Change, Annual Rate	1.7	1.5	1.4	1.5	1.7	1.5	1.4			
Unemployment Rate, Percent										
ERFC (Preliminary November)	4.9	4.8	4.8	4.7	4.9	4.7	4.6	4.6	4.7	4.8
Global Insight	4.9	4.9	4.9	4.8	4.9	4.8	4.6	4.6	4.7	4.8
Economy.com	4.9	5.0	4.9	4.9	4.9	4.8	4.7			
Blue Chip Average*	4.9	4.8	4.7	4.6	4.9	4.6	4.7	4.7	4.7	4.8
Blue Chip Top 10*		4.9	4.9	4.8	4.9	4.8	5.1	5.4	5.2	5.3
Blue Chip Bottom 10*		4.7	4.6	4.4	4.8	4.4	4.3	4.2	4.3	4.3
Real Disposable Personal Income, Percent Change, Annual Rate										
ERFC (Preliminary November)	2.1	1.6	2.3	1.6	2.5	1.9	2.5	2.6	2.3	2.3
Global Insight	2.7	2.3	2.8	1.8	2.6	2.4	2.8	2.7	2.5	2.5
Blue Chip Average*	2.6	2.2	2.4	2.3	2.6	2.3	2.3	2.3	2.2	2.2
Blue Chip Top 10*	3.4	3.1	3.0	2.9	2.8	2.7	2.8	2.7	2.7	2.8
Blue Chip Bottom 10*	1.8	1.1	1.8	1.9	2.3	1.9	1.7	1.7	1.7	1.6
West Texas Intermediate										
ERFC (Preliminary November)	44.9	49.4	50.4	51.9	43.2	52.0	54.1	55.3	56.1	56.9
Global Insight	44.9	47.3	46.9	50.6	42.7	50.2	54.4	67.6	74.9	81.1
Economy.com	44.9	50.0	51.6	55.0	43.5	56.0	61.1			

* Forecasts beyond 2017 are from the October 2016 Blue Chip Economic Indicators

U.S. Forecast Comparison	Fiscal Years					
	2016	2017	2018	2019	2020	2021
Real GDP						
Billions of 2009 dollars						
November Preliminary Forecast	16,513	16,832	17,199	17,552	17,928	18,293
<i>Growth</i>	1.7%	1.9%	2.2%	2.1%	2.1%	2.0%
September Forecast	16,510	16,837	17,207	17,572	17,954	18,340
<i>Growth</i>	1.7%	2.0%	2.2%	2.1%	2.2%	2.2%
Difference in level	3	-5	-8	-19	-27	-48
<i>Difference in growth forecast</i>	0.0%	-0.1%	0.0%	-0.1%	0.0%	-0.1%
Real Consumption						
Billions of 2009 dollars						
November Preliminary Forecast	11,356	11,664	11,929	12,192	12,453	12,714
<i>Growth</i>	2.7%	2.7%	2.3%	2.2%	2.1%	2.1%
September Forecast	11,357	11,674	11,945	12,215	12,481	12,757
<i>Growth</i>	2.7%	2.8%	2.3%	2.3%	2.2%	2.2%
Difference in level	-1	-10	-16	-23	-28	-43
<i>Difference in growth forecast</i>	0.0%	-0.1%	-0.1%	-0.1%	0.0%	-0.1%
Implicit Price Deflator						
Index 2009 = 100						
November Preliminary Forecast	110.0	111.8	113.8	115.9	118.1	120.4
<i>Growth</i>	0.7%	1.6%	1.8%	1.8%	1.9%	2.0%
September Forecast	110.0	111.7	113.6	115.6	117.7	120.0
<i>Growth</i>	0.7%	1.6%	1.6%	1.7%	1.9%	2.0%
Difference in level	0.0	0.0	0.2	0.3	0.4	0.4
<i>Difference in growth forecast</i>	0.0%	0.0%	0.2%	0.1%	0.1%	0.0%
Unemployment Rate						
Percent of Labor Force						
November Preliminary Forecast	5.0%	4.8%	4.7%	4.6%	4.7%	4.7%
September Forecast	5.0%	4.7%	4.6%	4.6%	4.7%	4.7%
<i>Difference in forecast</i>	0.0%	0.1%	0.0%	0.0%	0.0%	0.0%
30 Year Fixed Mortgage Rate						
Annual Average						
November Preliminary Forecast	3.8%	3.6%	4.3%	5.0%	5.5%	5.6%
September Forecast	3.8%	3.7%	4.5%	5.2%	5.8%	5.8%
<i>Difference in forecast</i>	0.0%	-0.1%	-0.2%	-0.2%	-0.2%	-0.2%
3 Month T-Bill Rate						
Annual Average						
November Preliminary Forecast	0.2%	0.5%	1.0%	1.8%	2.5%	2.6%
September Forecast	0.2%	0.5%	1.2%	2.0%	2.8%	2.8%
<i>Difference in forecast</i>	0.0%	-0.1%	-0.2%	-0.3%	-0.2%	-0.2%

Washington Forecast Comparison
Fiscal Years

	2016	2017	2018	2019	2020	2021
Real Personal Income						
Billions of 2009 dollars						
November Preliminary Forecast	346.1	357.2	367.5	379.5	391.5	403.0
<i>Growth</i>	3.7%	3.2%	2.9%	3.3%	3.2%	2.9%
September Forecast	342.0	351.7	362.5	374.4	386.4	398.0
<i>Growth</i>	4.1%	2.8%	3.1%	3.3%	3.2%	3.0%
Difference in level	4.1	5.5	5.0	5.1	5.1	4.9
<i>Difference in growth forecast</i>	-0.4%	0.4%	-0.2%	0.0%	0.0%	-0.1%
Nominal Personal Income						
Billions of dollars						
November Preliminary Forecast	380.8	399.3	418.1	439.7	462.3	485.4
<i>Growth</i>	4.3%	4.8%	4.7%	5.2%	5.1%	5.0%
September Forecast	376.3	393.0	411.7	432.7	454.8	477.7
<i>Growth</i>	4.8%	4.4%	4.7%	5.1%	5.1%	5.0%
Difference in level	4.5	6.2	6.4	7.0	7.5	7.7
<i>Difference in growth forecast</i>	-0.4%	0.4%	0.0%	0.1%	0.0%	0.0%
Nonfarm Payroll Employment						
Thousands						
November Preliminary Forecast	3,193.3	3,268.0	3,319.8	3,368.6	3,412.1	3,450.1
<i>Growth</i>	2.9%	2.3%	1.6%	1.5%	1.3%	1.1%
September Forecast	3,194.1	3,261.8	3,309.3	3,354.6	3,395.0	3,431.2
<i>Growth</i>	2.9%	2.1%	1.5%	1.4%	1.2%	1.1%
Difference in level	-0.7	6.1	10.5	14.0	17.2	18.9
<i>Difference in growth forecast</i>	0.0%	0.2%	0.1%	0.1%	0.1%	0.0%
Housing Permits						
Units Authorized, Thousands						
November Preliminary Forecast	39.8	39.0	40.2	41.2	41.7	41.9
<i>Growth</i>	3.0%	-2.0%	3.1%	2.6%	1.2%	0.4%
September Forecast	39.8	41.1	43.4	44.2	44.4	44.2
<i>Growth</i>	3.0%	3.3%	5.7%	1.8%	0.5%	-0.6%
Difference in level	0.0	-2.1	-3.2	-3.0	-2.7	-2.3
<i>Difference in growth forecast</i>	0.0%	-5.3%	-2.6%	0.7%	0.7%	1.0%

**Year-Over-Year Employment Growth by Industry
(September 2015 to September 2016)
Washington vs. U.S.**

	Washington		U.S.
	(000)	% Chg.	% Chg.
Total	91.7	2.9%	1.7%
Electronic Shopping and Mail-Order Houses	8.4	27.6%	NA
Construction	12.8	7.4%	3.4%
Software Publishers	3.3	5.8%	NA
Mining and Logging	0.3	5.3%	-13.8%
Information Excluding Software	3.0	5.1%	0.0%
Transportation, Warehousing and Utilities	4.2	4.1%	0.8%
Leisure and Hospitality	11.4	3.7%	2.4%
Education and Health Services	15.7	3.5%	2.7%
Professional and Business Services	12.5	3.2%	2.9%
State and Local Gov Non-Education	6.6	3.1%	0.7%
Other Services	3.5	3.0%	1.6%
Financial Activities	3.7	2.5%	2.0%
State and Local Gov Education	3.6	1.4%	0.4%
Wholesale Trade	1.5	1.1%	1.0%
Manufacturing Excluding Aerospace	0.0	0.0%	NA
Aerospace Product and Parts Manufacturing	-3.3	-3.5%	NA
Information	6.3	5.4%	0.3%
Retail Trade	11.8	3.3%	2.0%
Manufacturing	-3.3	-1.1%	-0.4%

Source: WA State ERFC Kalman filtered data, U.S. Bureau of Labor Statistics