

State Economic & Revenue Outlook

“Early Guidance” for the March 2009 Official Forecast

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Executive Director

February 19, 2009



Washington State Economic and Revenue Forecast Council



Caveats

- This is not an official forecast
- Most of the oversight components of the official forecast process were bypassed in coming up with this early guidance scenario
 - No input from the Governor's Council of Economic Advisors
 - No input from the Forecast Workgroup
 - No official vote of the Economic & Revenue Forecast Council adopting this forecast
- The official forecast process remains intact, and an official forecast will be issued March 19, 2009, as scheduled
- Given the rapidly changing economic landscape in the nation and consequently in our state, the official forecast may differ significantly from this early guidance forecast

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Outline

- Developments since our November forecast
- The current situation – we are on track for the weakest economy since the Great Depression
- “Perfect Storm” of economic uncertainty make forecasting very difficult – our computer models can only go so far
- “Early guidance” for the March official forecast

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Surprises since the November forecast

Negative

- WA economy “hit the wall” in Q4
- Layoffs at Boeing and Microsoft
- Holiday sales hurt by bad weather
- Automotive and housing sales weakened more sharply than expected
- Credit markets now unlikely to thaw until late this year

Positive

- Fiscal stimulus larger than expected in November

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Revenue collections have been even slower than predicted

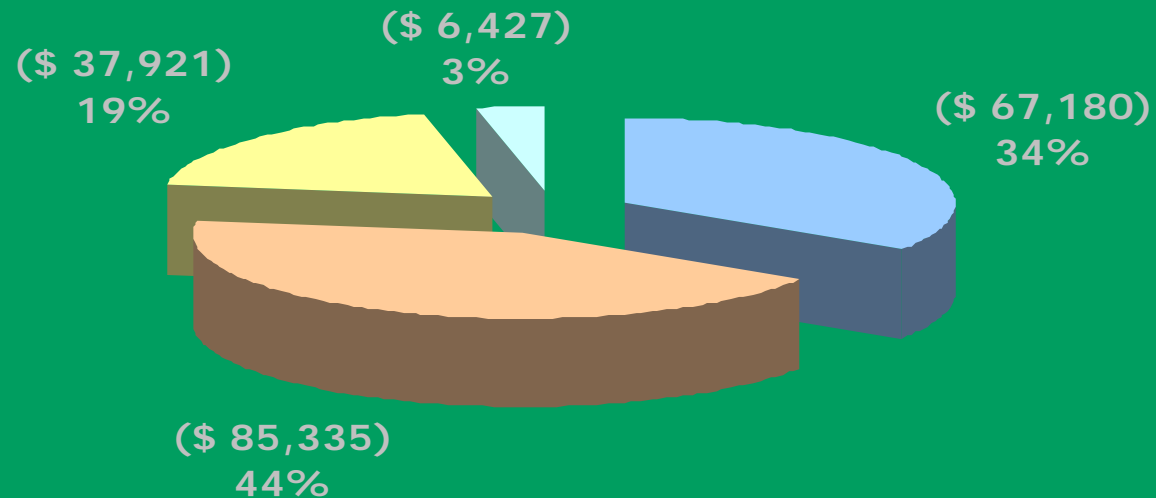
Revenue collections in the 3 months since the November forecast are USD 197 million below target

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Where were the misses?

USD Thousands



■ Retail Sales & Use ■ B&O
■ REET ■ Other

Source: ERFC estimates

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The current economic situation

- The U.S. economy has been in recession since December 2007 – this may possibly turn out to be the longest downturn since the Great Depression
- Financial sector woes are still hobbling the real economy
- Credit to consumers and business is still mostly unavailable
- Washington's economy lagged the U.S. into the downturn, but is now in recession
- State revenue collections have been affected severely, because this is a consumer led recession

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The global economy is in recession

		Share of World Economy		Q4 Growth (ann.)
1	United States	24.4%	Recession	-3.8%
2	Japan	7.7%	Recession	-12.7%
3	Germany	5.9%	Recession	-8.7%
4	China	5.8%	Slower Growth	
5	United Kingdom	4.9%	Recession	-6.0%
6	France	4.6%	Recession	-4.9%
7	Italy	3.7%	Recession	-7.0%
8	Spain	2.5%	Recession	-4.1%
9	Canada	2.5%	Recession	-2.8%
10	Brazil	2.3%	Recession	-2.5%
11	Russia	2.3%	Sharp slowdown	
12	India	1.9%	Slower Growth	
13	Mexico	1.8%	Recession	-4.0%
14	Korea	1.7%	Recession	-24.4%
15	Australia	1.6%	On the brink of recession	
TOTAL		74%		

Source: IMF, Goldman Sachs

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We are in one of the worst "bear markets" since WW II



Source: Yahoo Finance, ERFC

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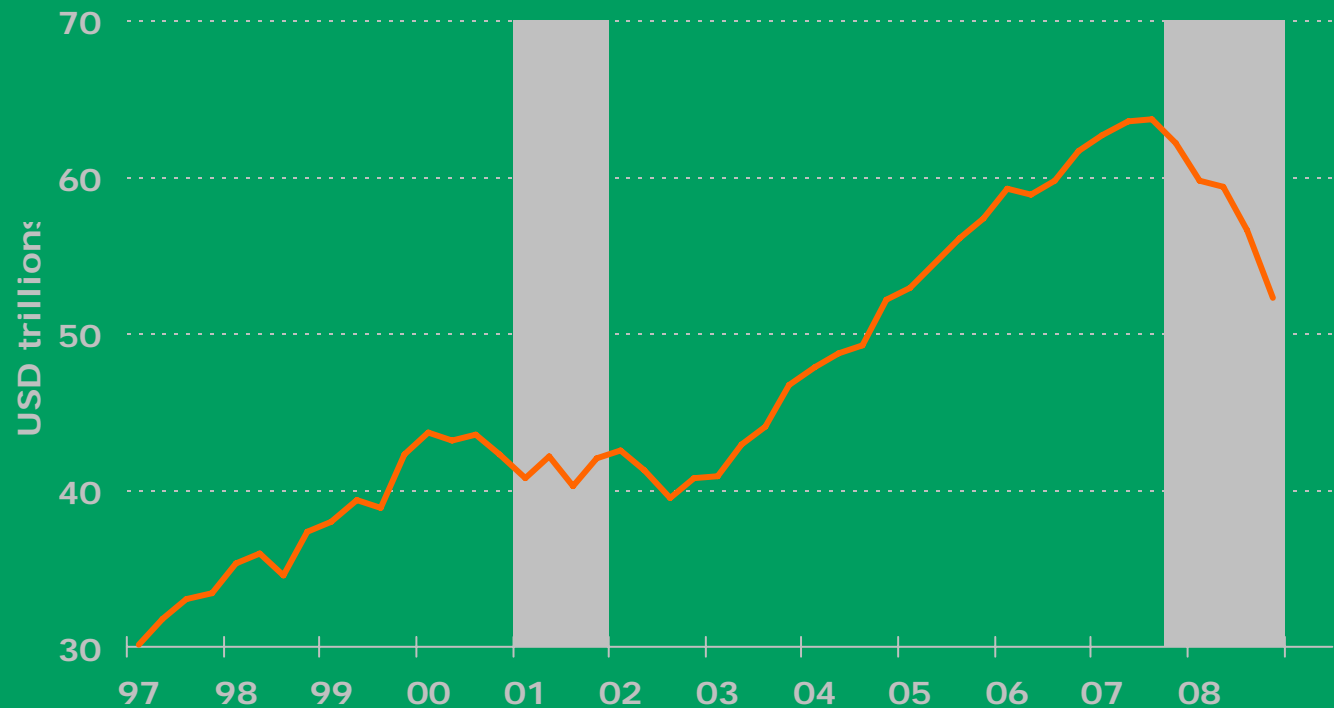
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Household net worth has declined rapidly

Household net worth at the end of 2008 was down 18% from its peak in late 2007



Source: Global Insight, data through 2008 Q4

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Although inter-bank lending has eased...

The spread indicates the premium banks have to pay to borrow from each other

USD 3m LIBOR - 3m US T-bill Spread
Basis Points



Source: British Bankers Association, US Federal Reserve Bank, ERFC; data through February 2, 2009

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... lending to businesses and consumers is still tight

There has been only modest easing in credit conditions since November – there is still a long way to go

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Net Tightening *minus* Easing
Percent



Source: Federal Reserve Board, Senior Loan Officers Quarterly Survey, data through January 2009 survey

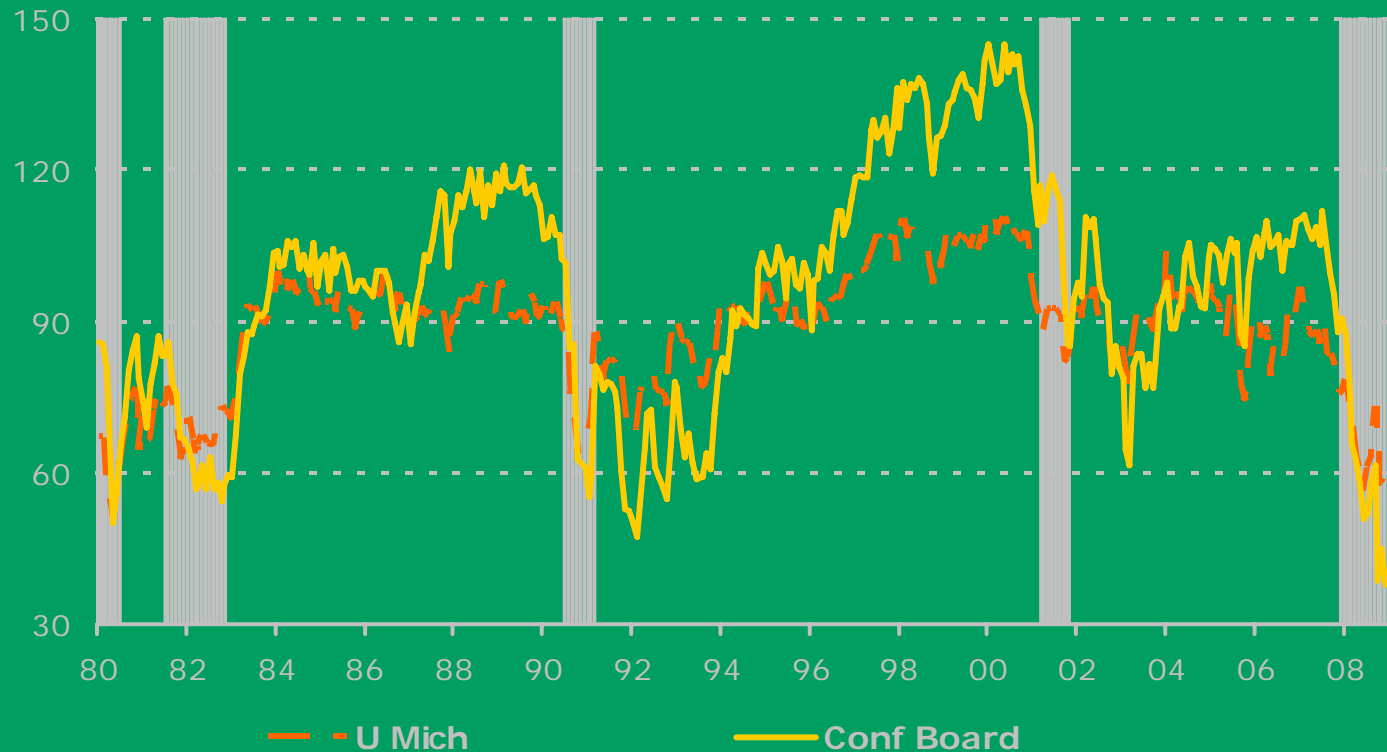
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Consumer sentiment reflects uncertainty about the economy

Conference Board measure is at a record low

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



Source: University of Michigan; Conference Board; data through January 2009.

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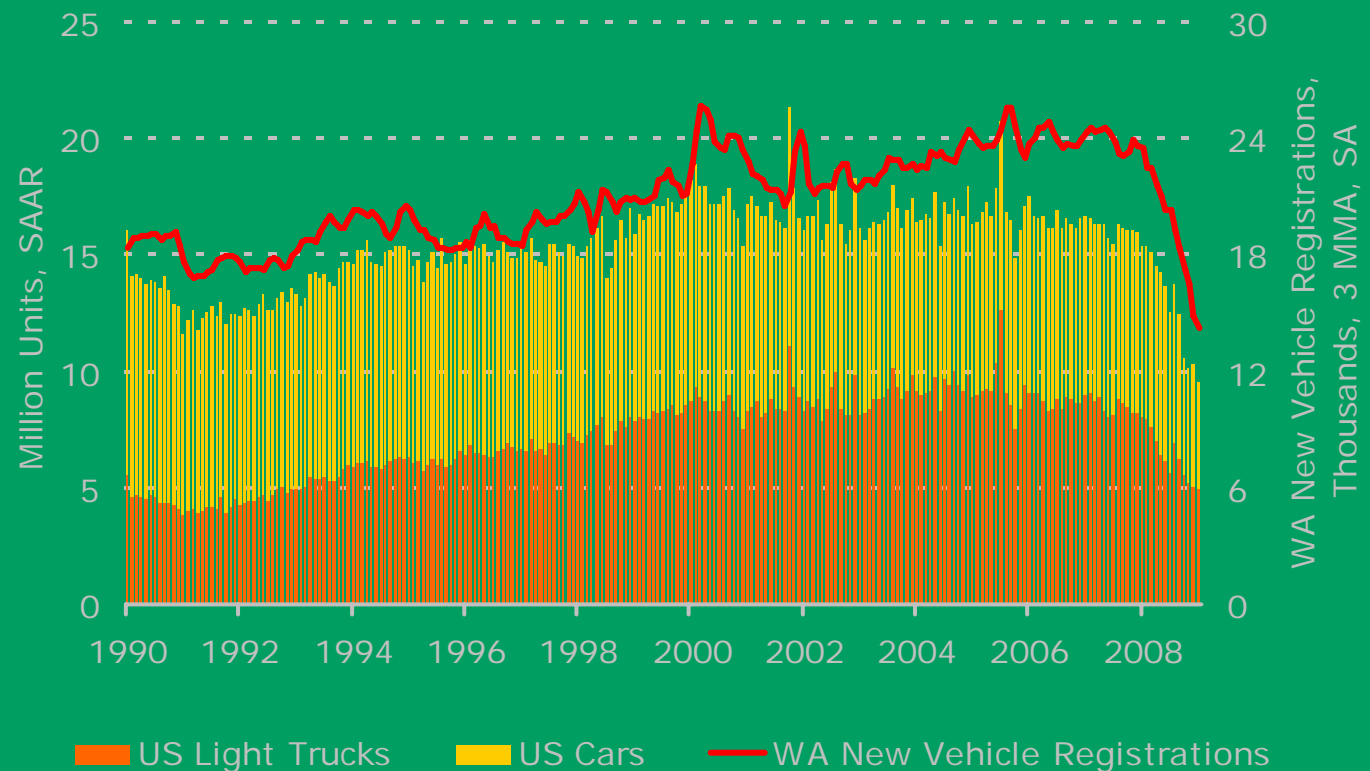
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Automotive sales have tumbled nationally, and in Washington

The rate of decline in WA auto sales has doubled since our November forecast



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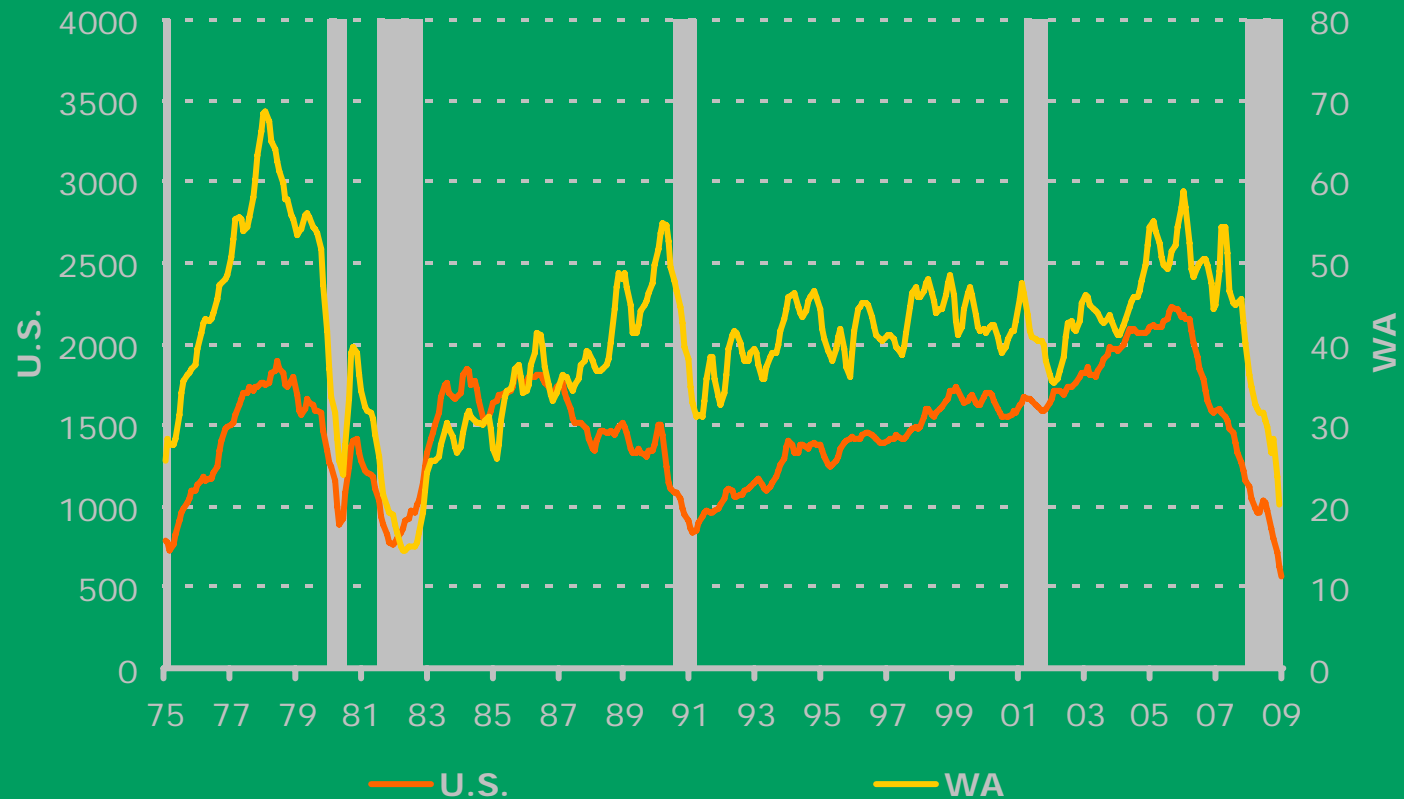
Source: Autodata Corporation, WA DOL, data through January 2009

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State housing permit activity lagged the nation, but has now slowed sharply

Thousands, annualized units, 3 MMA, SA



Source: Census Bureau, U.S. data through Jan 2009; WA data through Dec 2008

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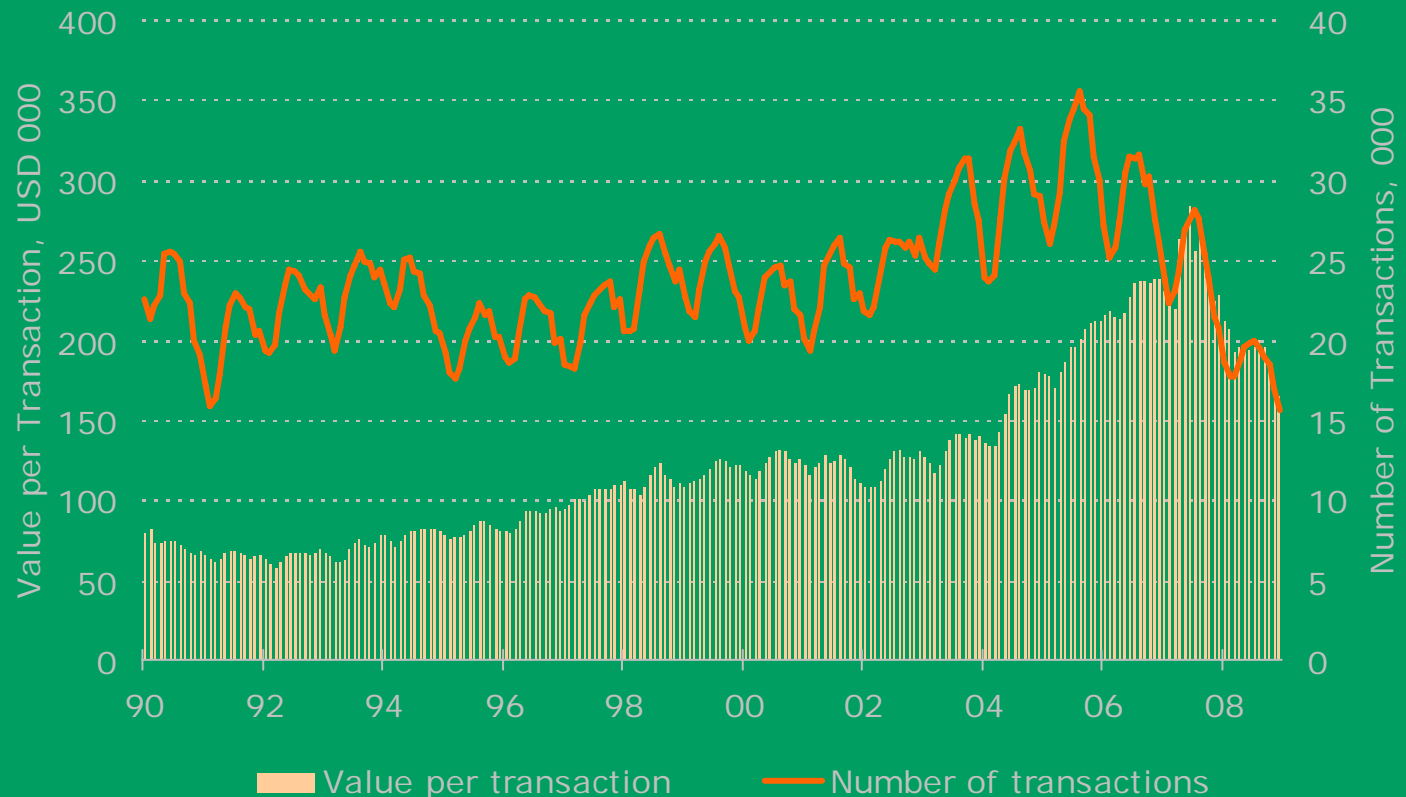
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Lower real estate activity is reflected in lower REET collections

2008 Q4 taxable value was 45% below year ago

3-month moving average



Source: ERFC, data through December 2008

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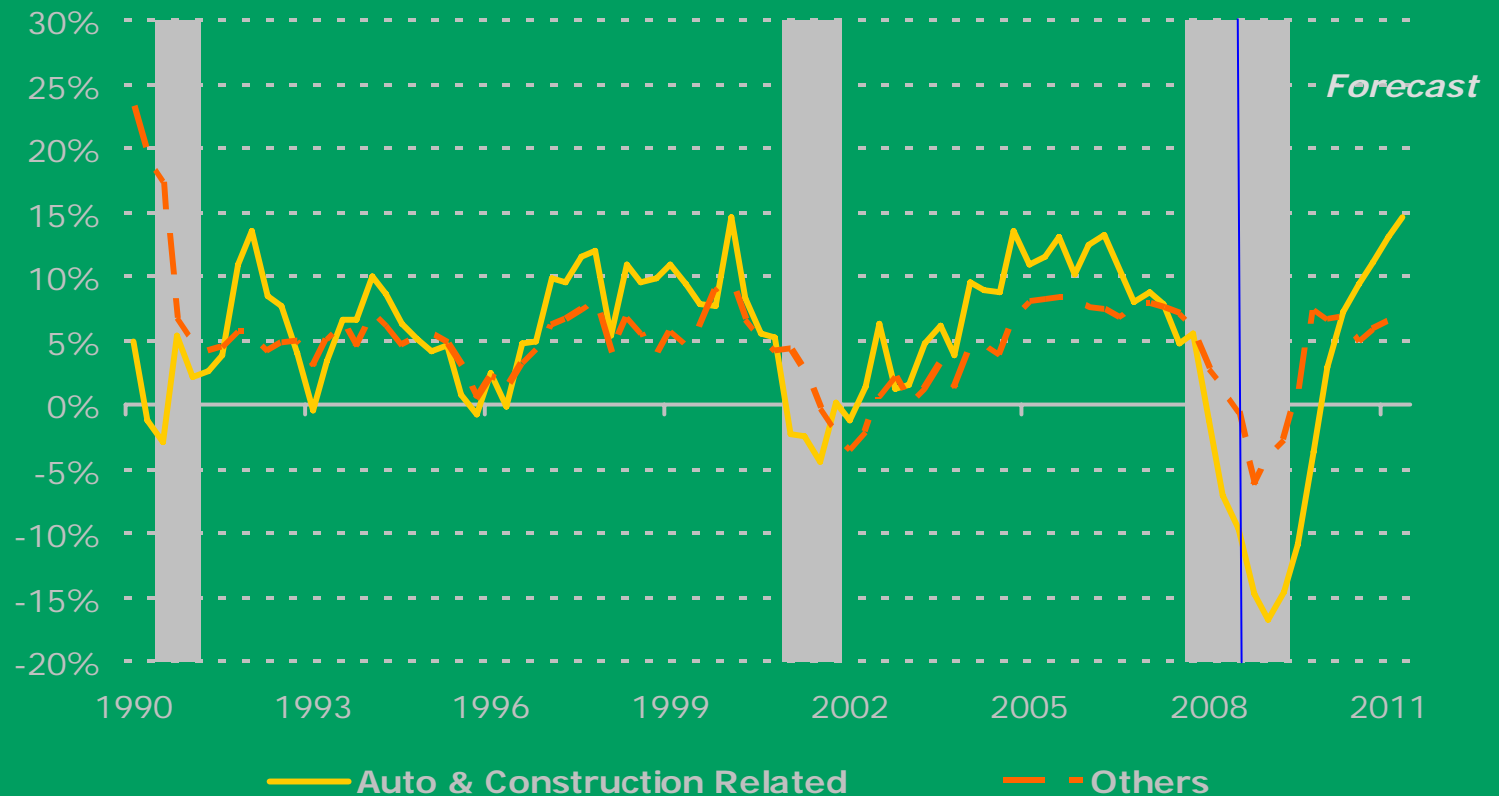
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The decline in taxable activity is mostly in the automotive and construction related sectors

Retail Sales Tax

Percent change, year ago



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Source: ERFC forecast; actual data through 2008Q3

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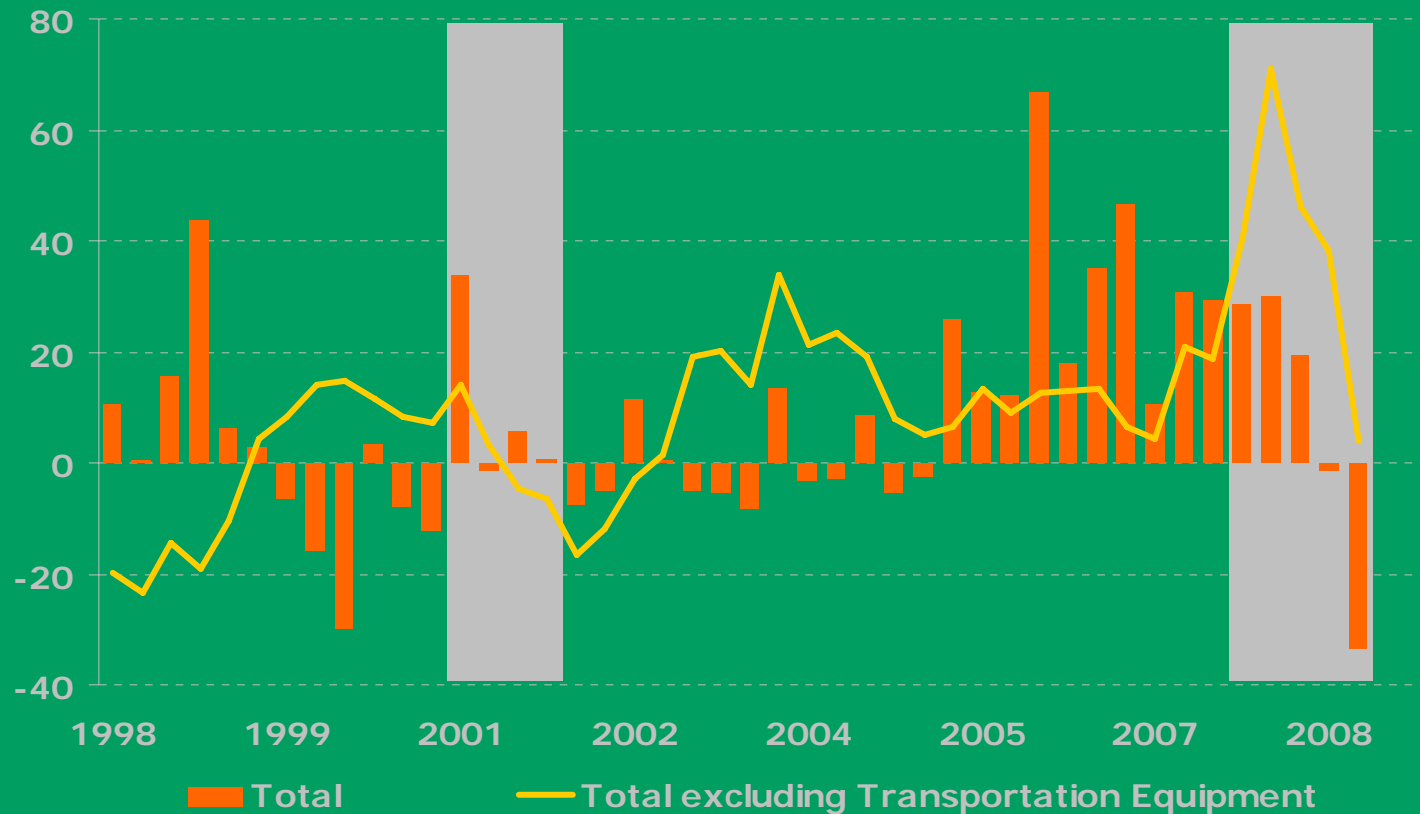
WA exports are plummeting

2008 Q4 decline in transportation equipment reflects impact of Boeing strike

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Percent Change, year ago



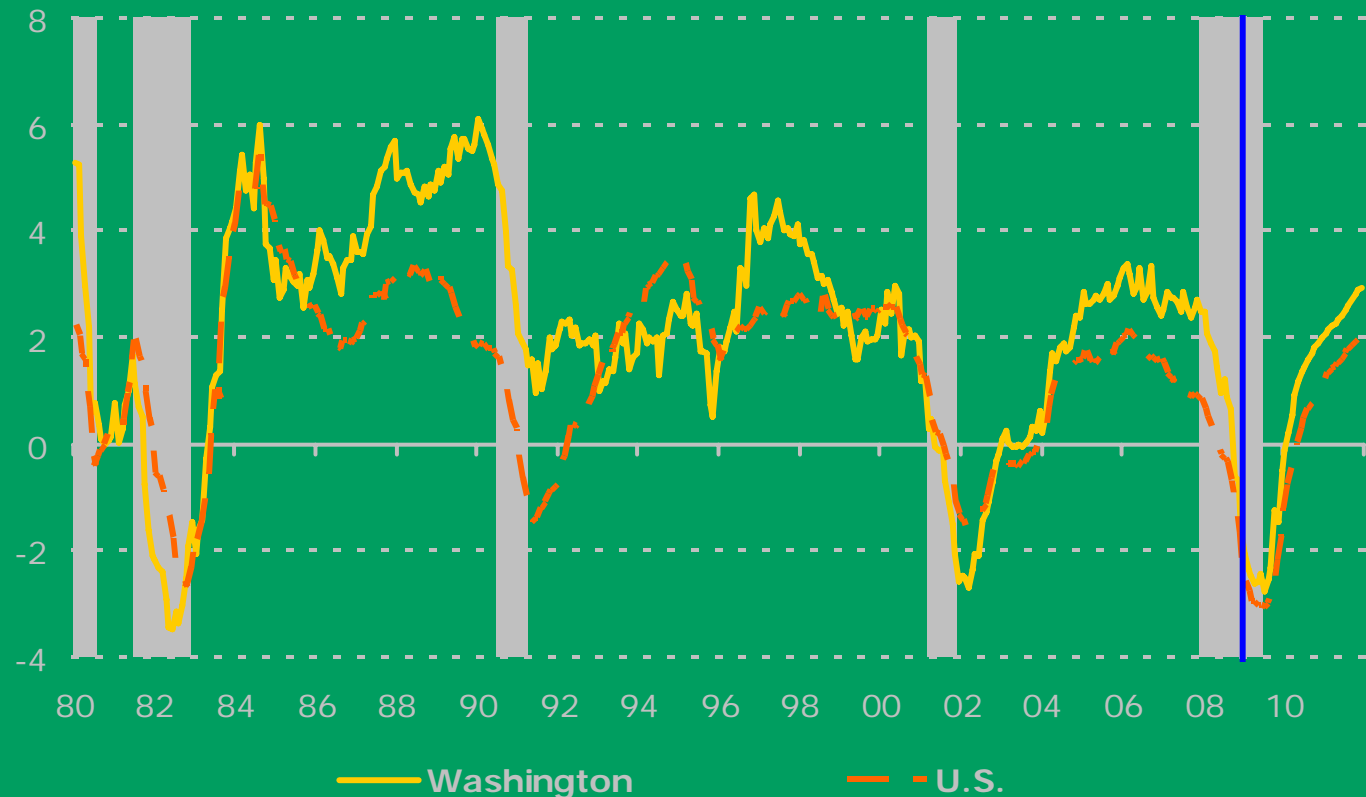
Source: Wisier Trade Data, through 2008 Q4

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WA employment is now declining at the same pace as in the rest of the nation

Percent change, year ago



Source: ERFC forecast, actual through December 2008

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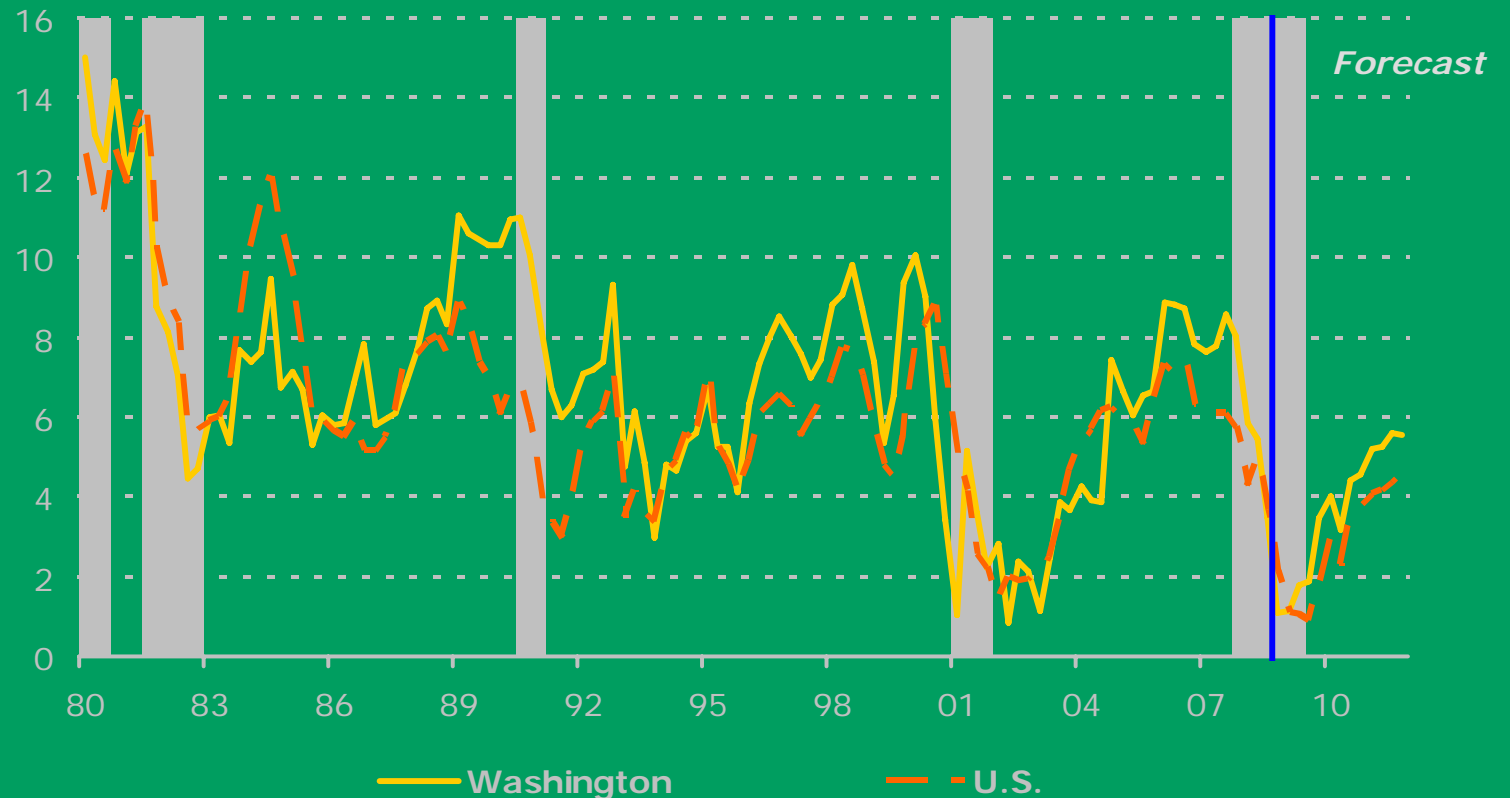
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WA personal income growth has declined sharply

Percent change, year ago



Source: ERFC forecast; actual data through 2008Q3

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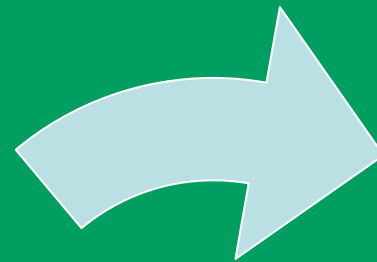
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There are many uncertainties about the recovery

- Access to credit?
- Equilibrium price?
- Foreclosures?

HOUSING



BANKING

- Toxic assets on bank balance sheets?
- Return of private investors in secondary loan markets?

**Return of Confidence
???**



JOBS

- Private spending?



- Stimulus Package?

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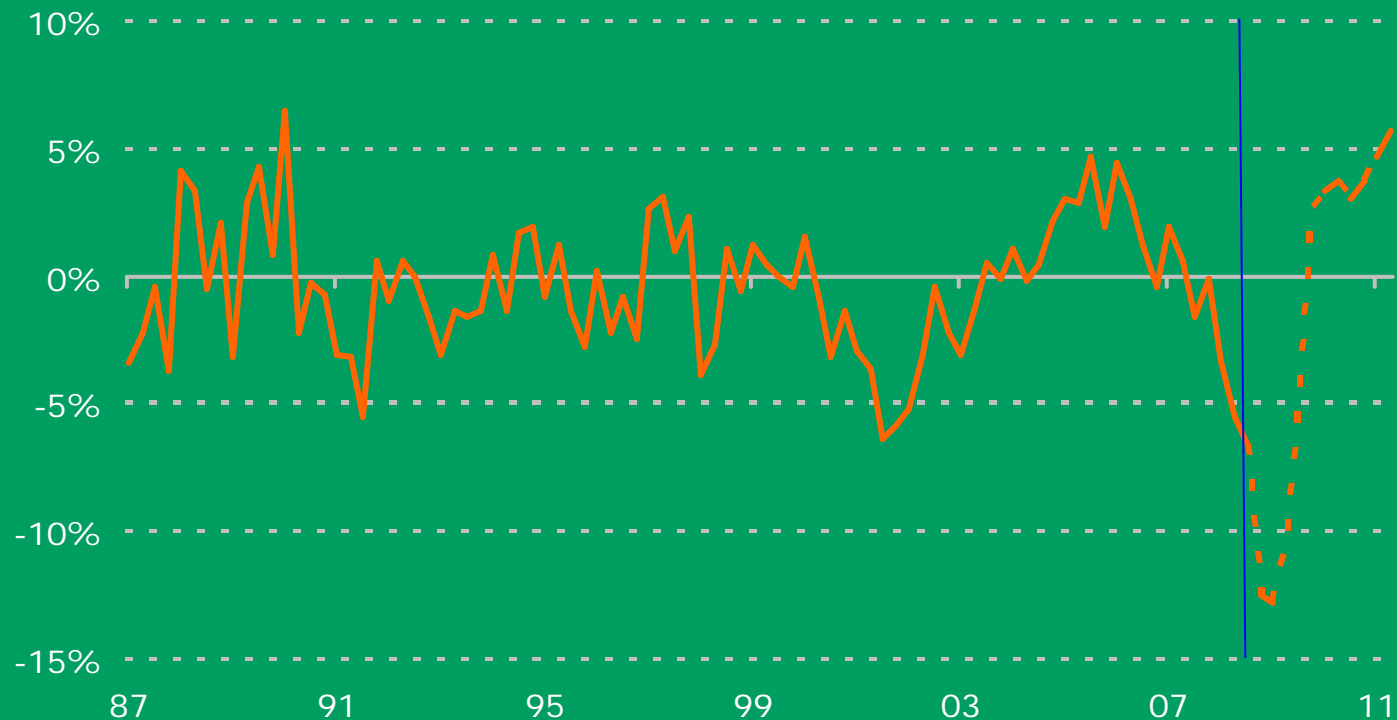
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Revenue growth relative to income continues to drop

* Adjusted for new legislation and special factors

Growth in Net Revenue Act Collections* Relative to Growth in State Personal Income



Source: ERFC; actual data through 2008Q3, estimate for Q4

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Forecast changes 2007-2009 Biennium

USD Millions

February `09 Early Guidance Forecast

	<u>Nov '08 Forecast</u>	<u>Forecast Change</u>	<u>Non- economic Change</u>	<u>Variance</u>	<u>Forecast</u>	<u>Total Change*</u>
Dept. of Revenue	\$ 27,765	(\$452)	(\$78)	(\$197)	27,038	(\$727)
All other agencies	\$ 861	(\$3)	\$9	-	\$867	\$6
Total GFS	\$28,627	(\$455)	(\$69)	(\$197)	\$27,905	(\$721)

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* Detail may not add to total due to rounding

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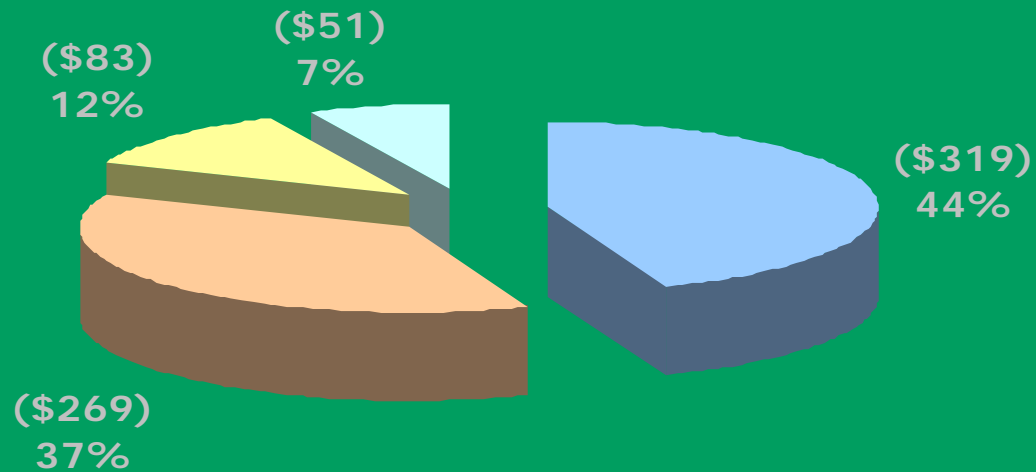


Composition of the forecast change for the 2007-09 biennium

Total change from November forecast:

(\$721,000)

USD Thousands



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■ REET ■ Other

Source: ERFC forecast, February 2009

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Forecast changes 2009-2011 Biennium

USD Millions

		February '09 Early Guidance Forecast			
	<u>Nov '08 Forecast</u>	<u>Forecast Change</u>	<u>Non- economic Change</u>	<u>Forecast</u>	<u>Total Change*</u>
Dept. of Revenue	\$29,350	(\$1,494)	(\$79)	27,778	(\$1,572)
All other agencies	\$720	(\$32)	\$17	\$705	(\$15)
Total GFS	\$30,071	(\$1,526)	(\$61)	\$28,483	(\$1,587)

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* Detail may not add to total due to rounding

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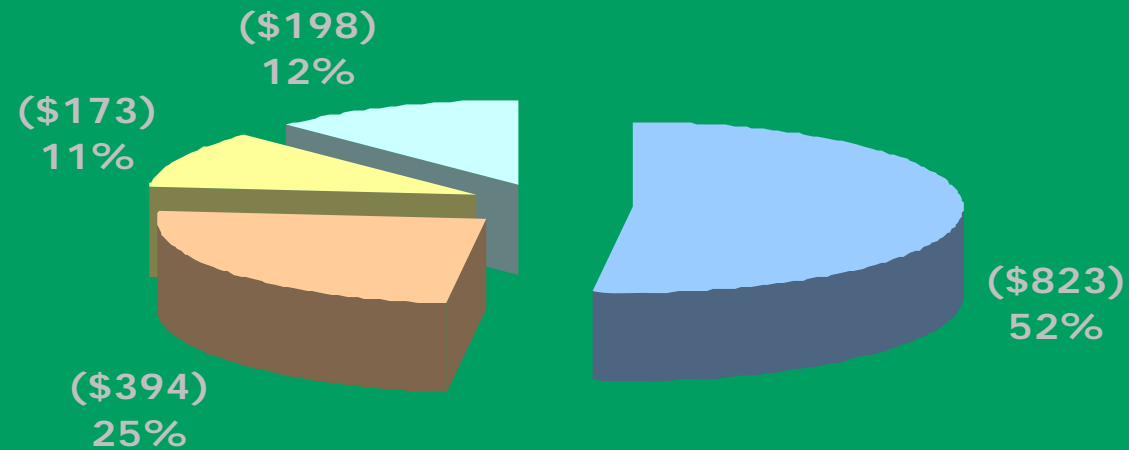


Composition of the forecast change for the 2009-11 biennium

Total change from November forecast:

(\$1.6 bill.)

USD Thousands



■ Retail Sales & Use ■ B&O
■ REET ■ Other

Source: ERFC forecast, February 2009

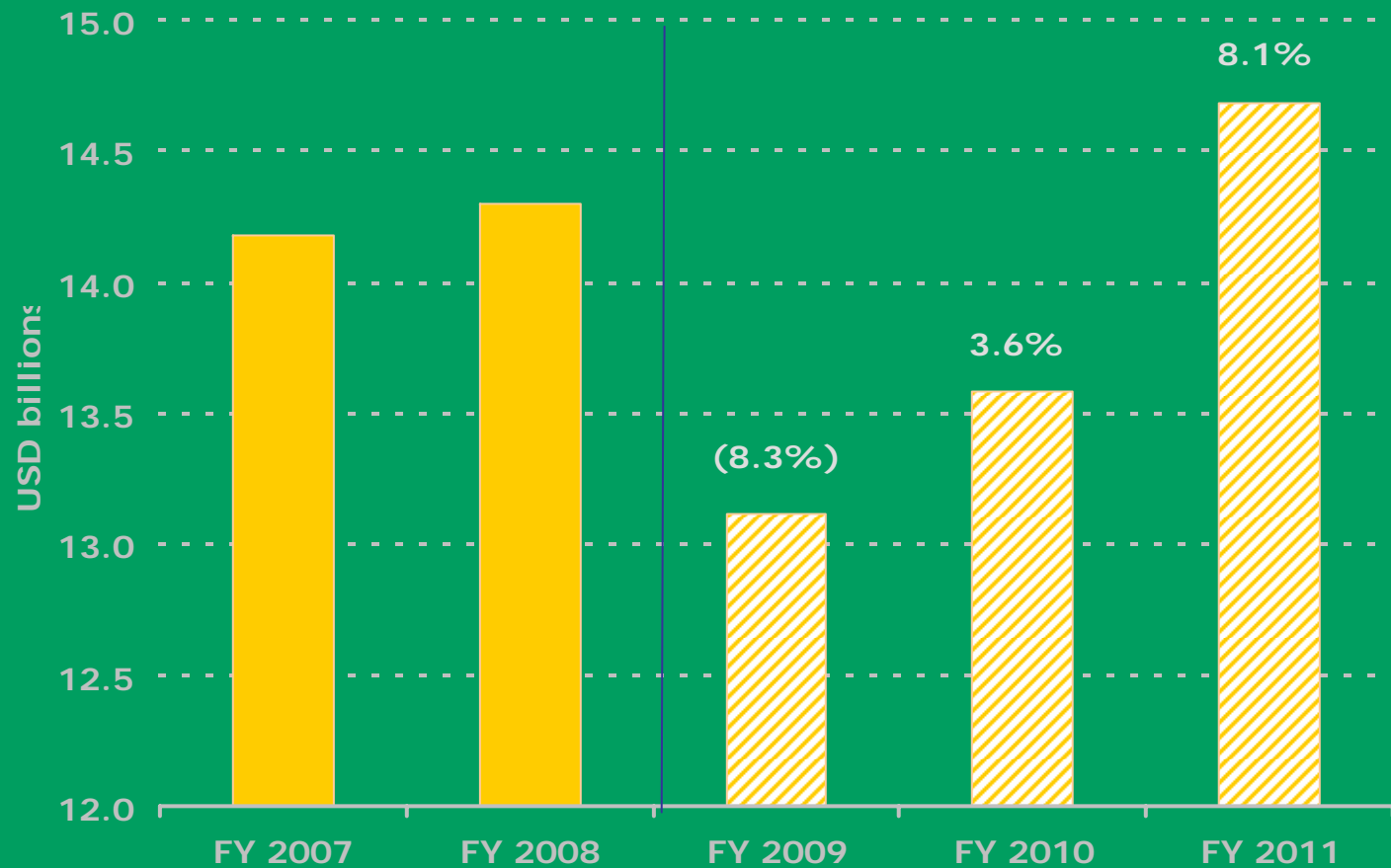
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Forecast by fiscal year



Source: ERFC forecast, February 2009

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Conclusion

- Compared to our official November 2008 revenue forecast -
- As of February 2009, an **unofficial** update reduces expected revenues as follows:

2007-09 : (USD 721 million)

2009-11 : (USD 1,587 million)

TOTAL : (USD 2,308 million)

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Questions



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