# Washington State Economic & Revenue Outlook

## *"When will the real estate market recover in Washington?"*

Presented to
Washington Realtors

Arun Raha
Chief Economist

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Olympia, Washington

WASHINGTON STATE
**ECONOMIC AND REVENUE FORECAST COUNCIL**

# Summary

- 2010 will be a year of transition
  - The economy will gain traction by mid-year
  - The recovery in revenues is underway, but progress will be slow
- The economic recovery faces headwinds
  - Real estate, especially commercial
  - Banking, particularly local and regional banks
- On the upside, a synchronized global recovery now unfolding, means exports will kick in earlier in the cycle
- Self sustaining housing recovery not until early 2011; non-residential not until later that year

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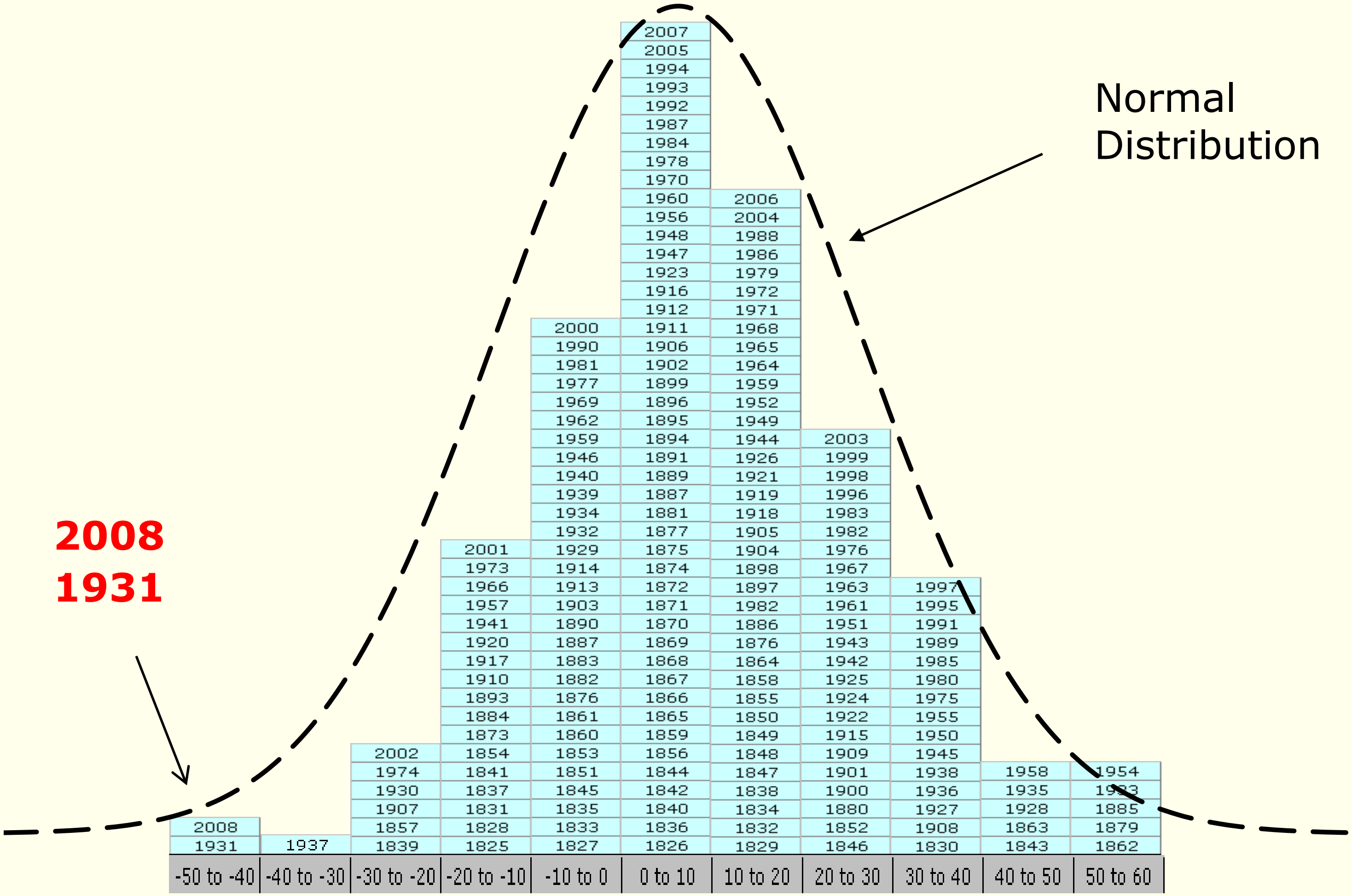
# Equity returns in 2008 were a tail event

**U.S. Stock Market Total Returns**

**1825 - 2008**




Source: AXA

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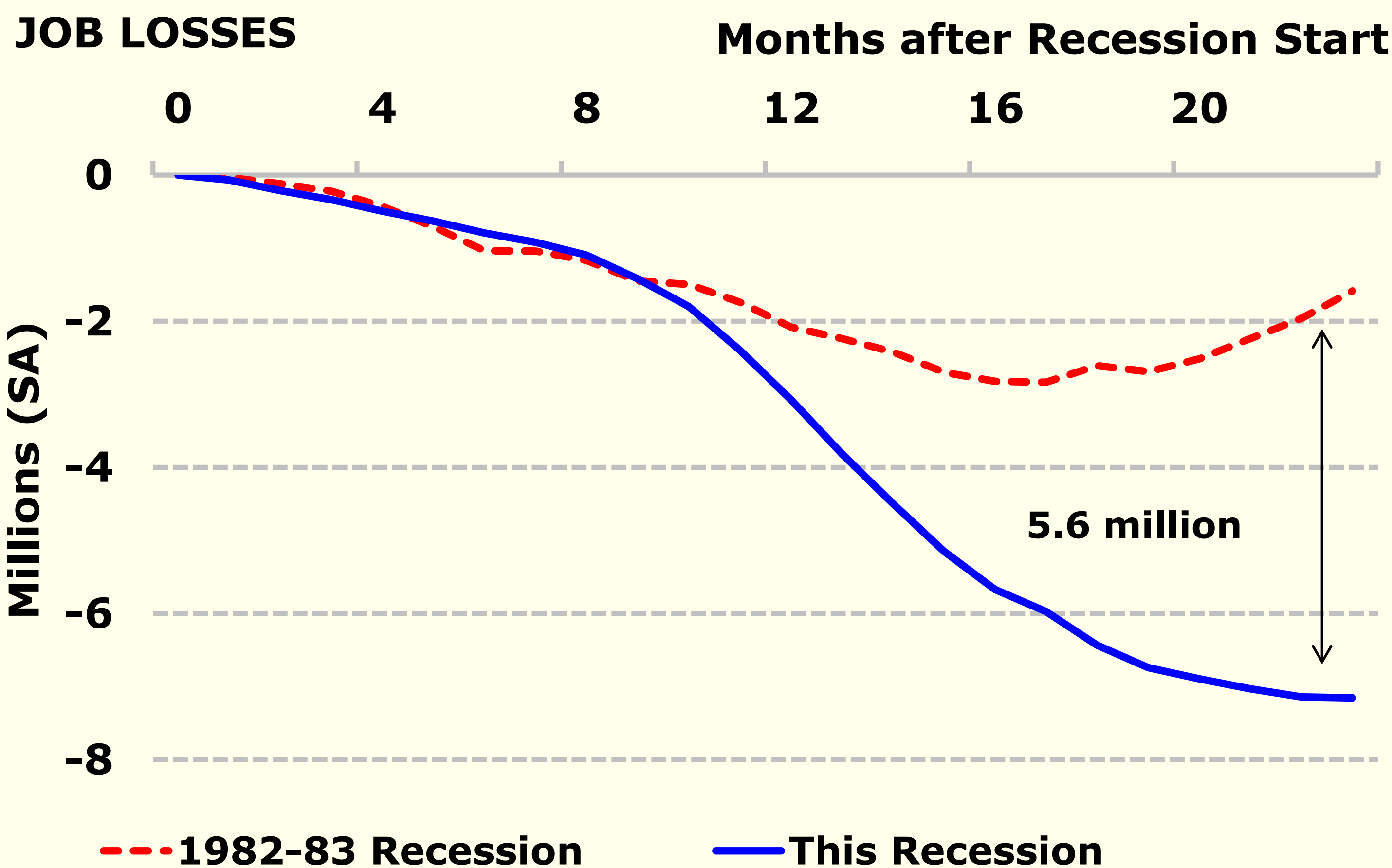
# At this stage in 1982-83, employment had started to recover




Source: BLS, ERFC; data through November 2009

Cumulative job losses at 23 months

**1982-83:**

1.4% of labor force

**This time:**

4.7% of labor force

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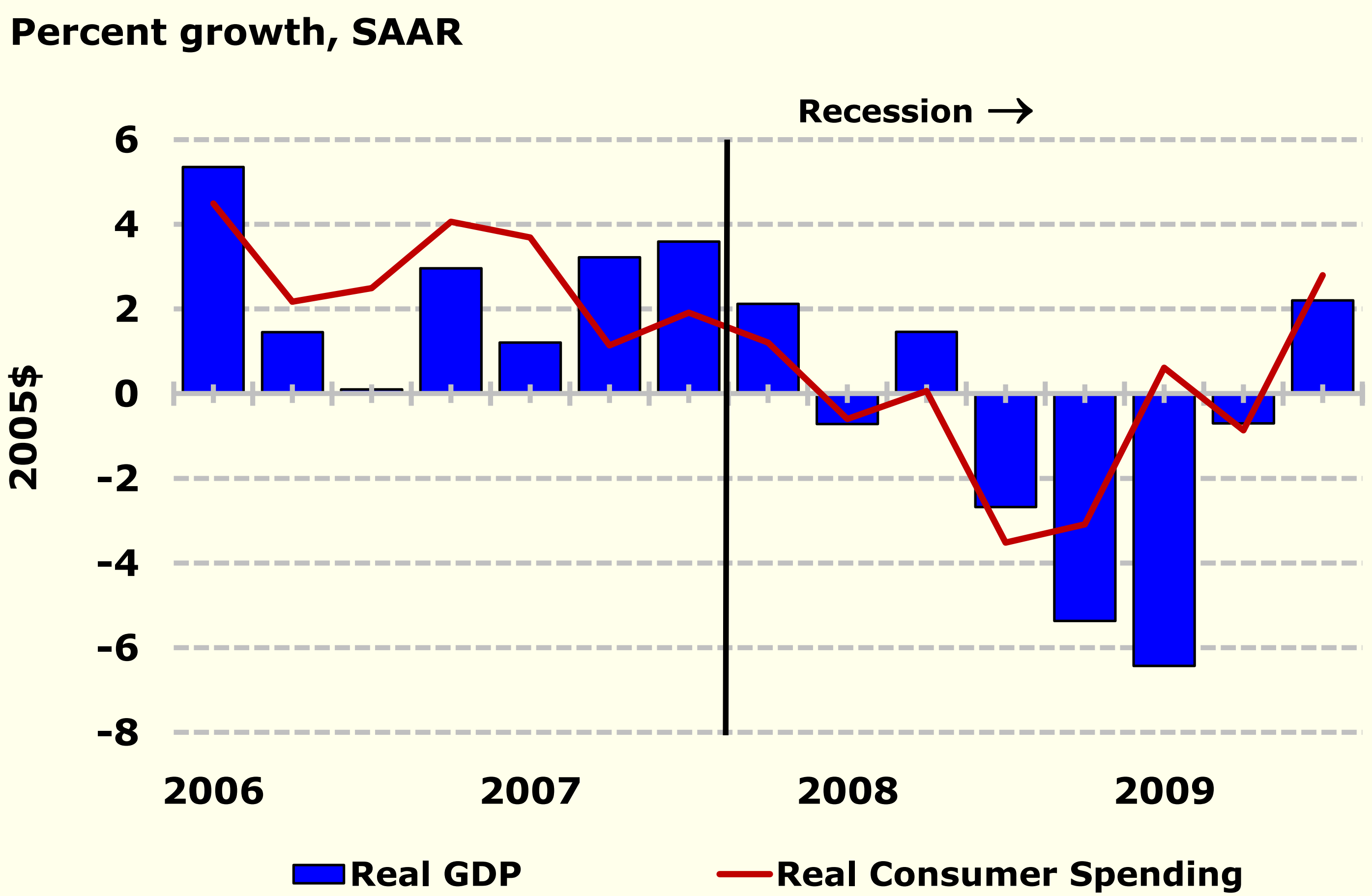
# GDP returned to growth in Q3




Source: BEA, data through 2009 Q3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# Increasing yield curve spread points to growth

An inverted yield curve typically precedes a recession while a steepening yield curve signifies a recovery

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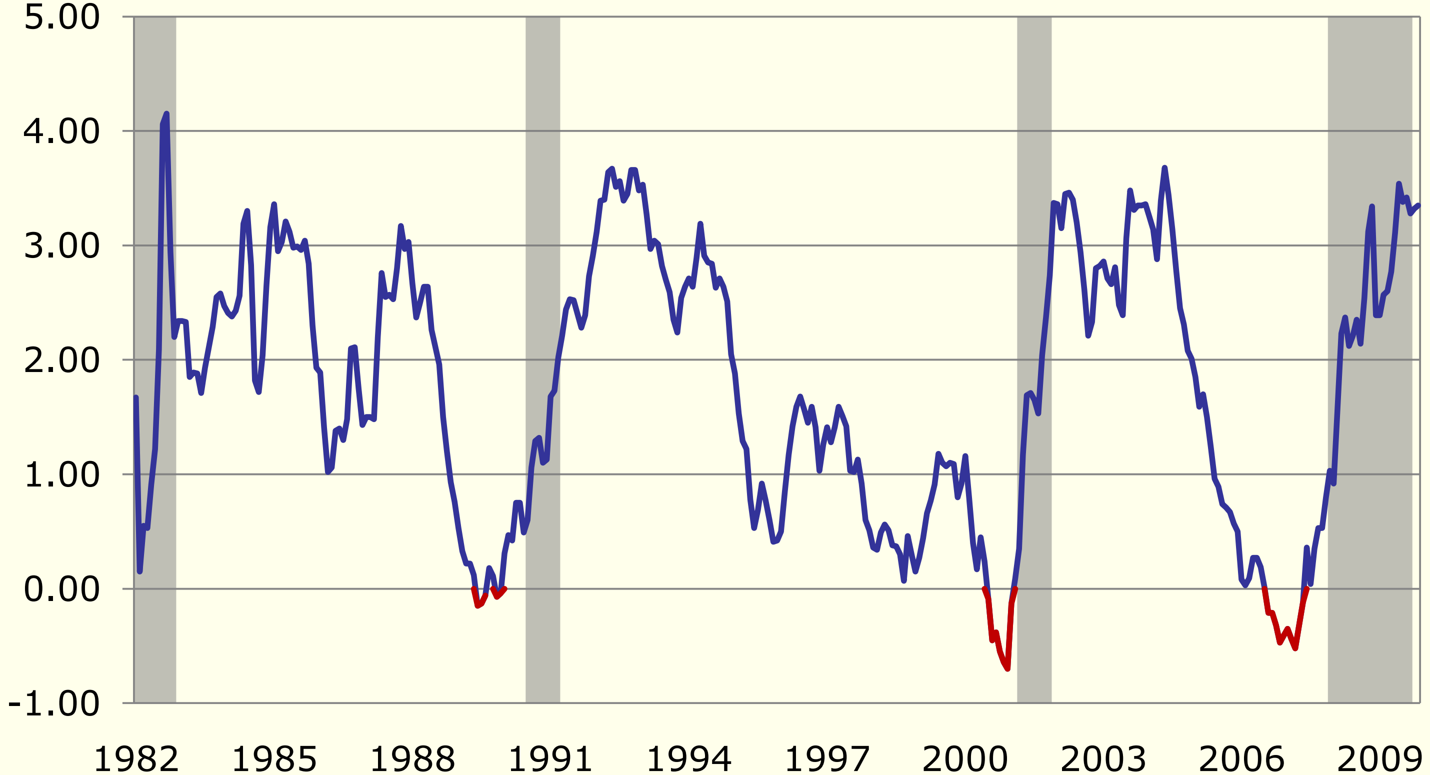
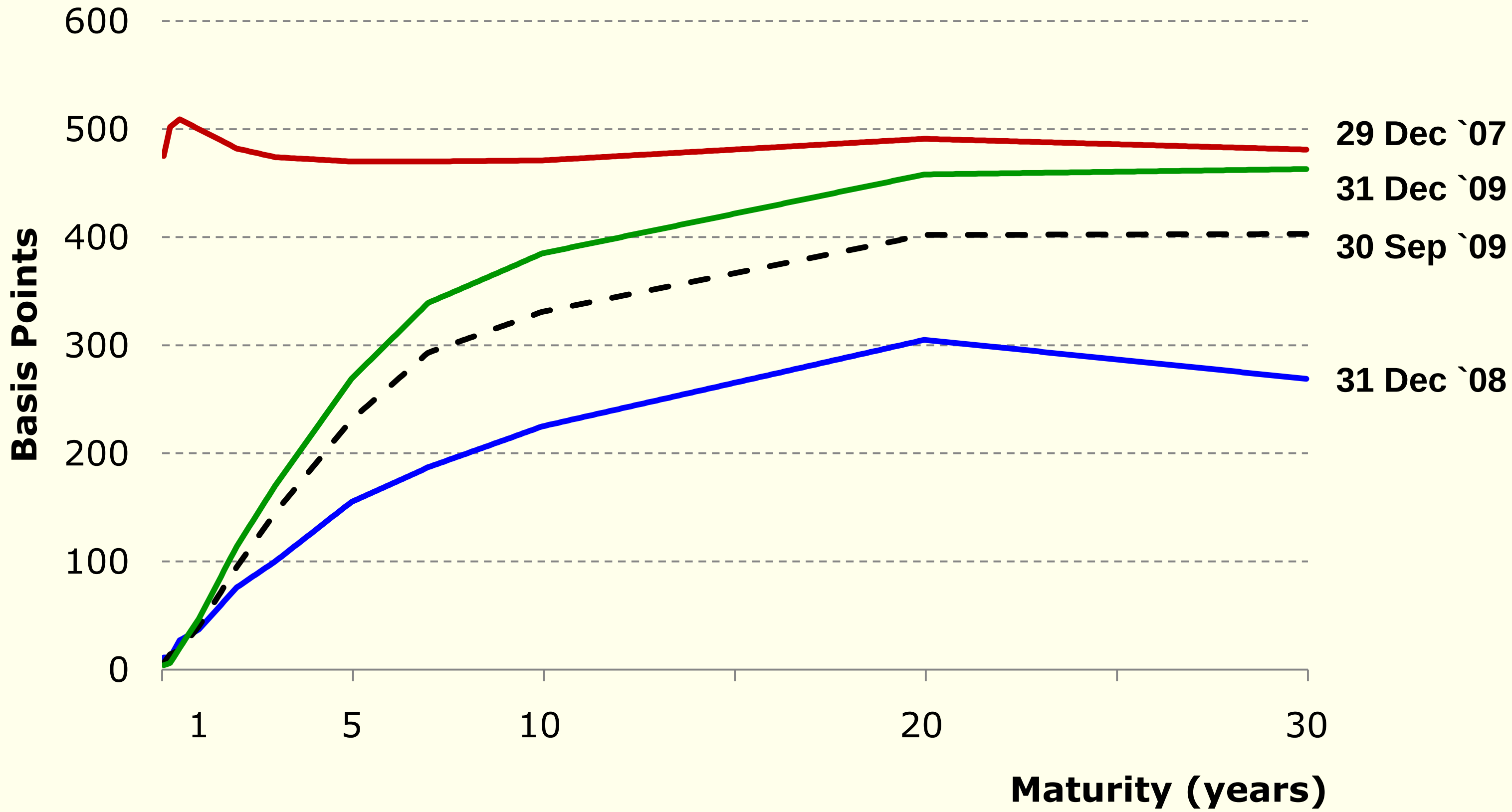
**Yield Curve Spread**
**10-Year minus 3-Month U.S. Treasuries**




Source: Federal Reserve Board, ERFC; data through November 2009

# Steepening yield curve reflects expectations the economy will grow

**Yield Curve**
**U.S. Treasuries, constant maturities**




Source: Federal Reserve Board, ERFC

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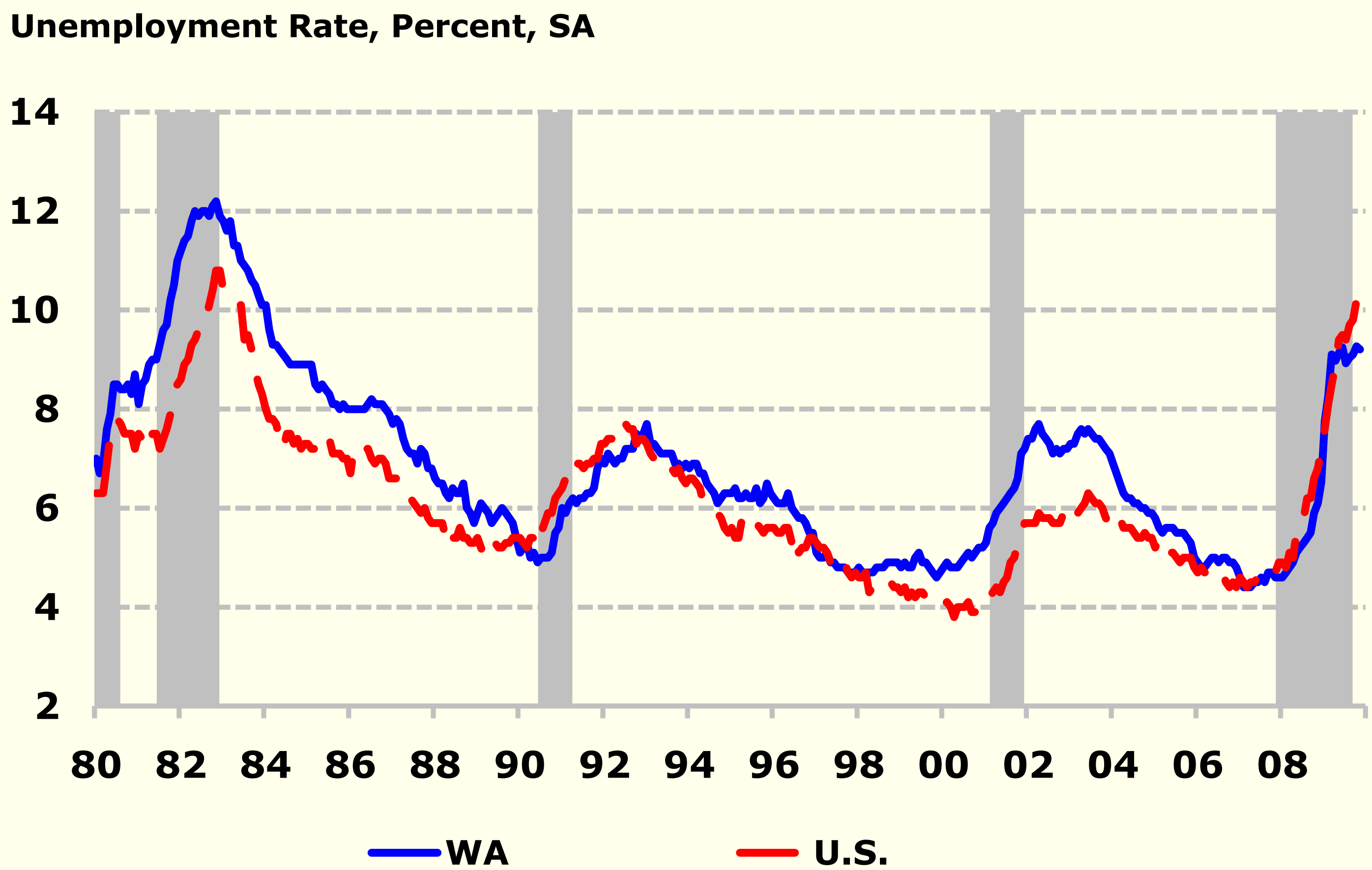
# Unemployment is still high

It is normal for this rate to continue to rise even after the economy is in recovery




Source: WA ESD, BLS; data through December 2009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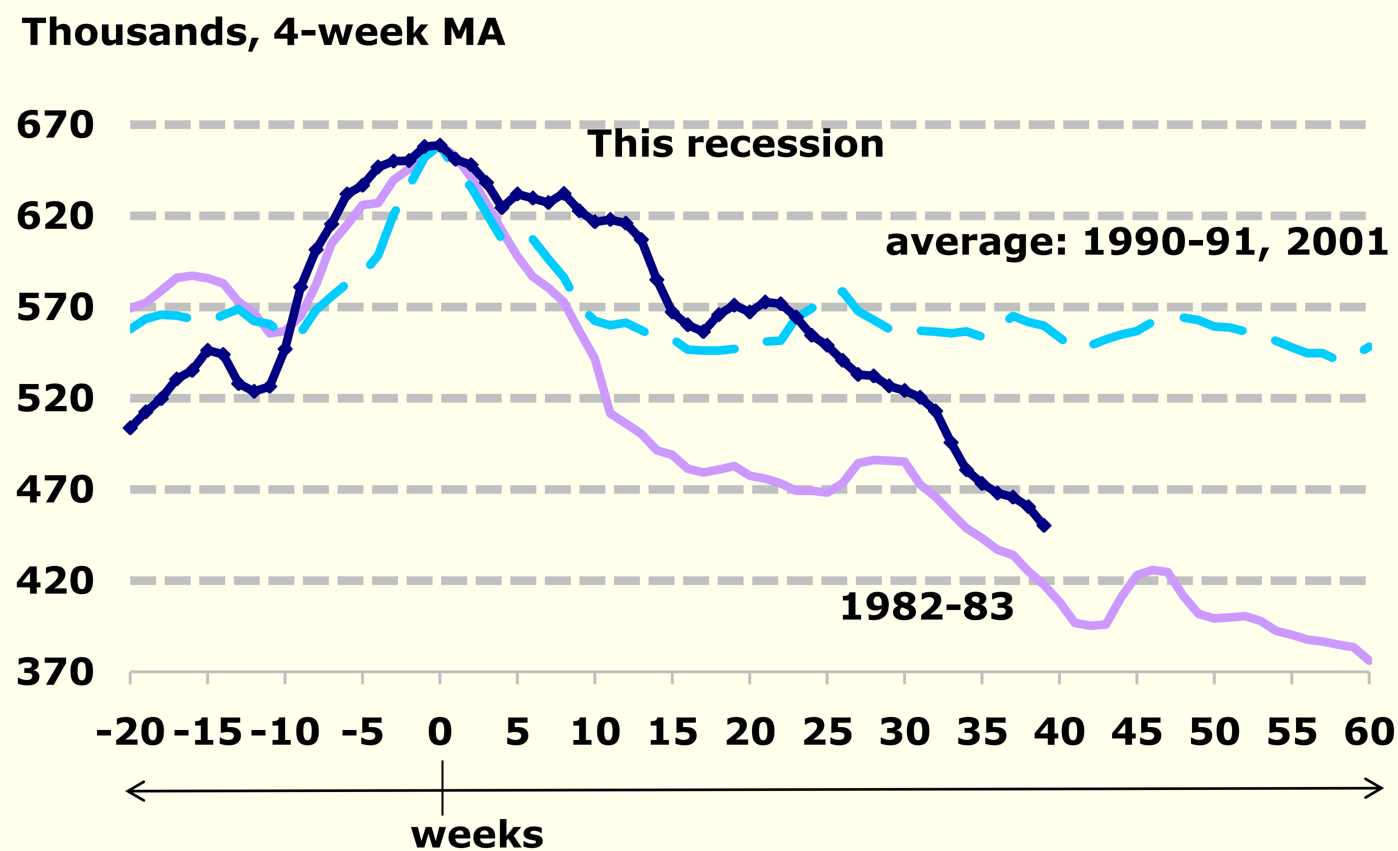
# The recovery in employment has been slow, but is poised to improve

It is normal for the unemployment rate to continue to rise, even after job losses end

## U.S. Initial Unemployment Claims




Source: U.S. Department of Labor, ERFC; data through Jan 2, 2010

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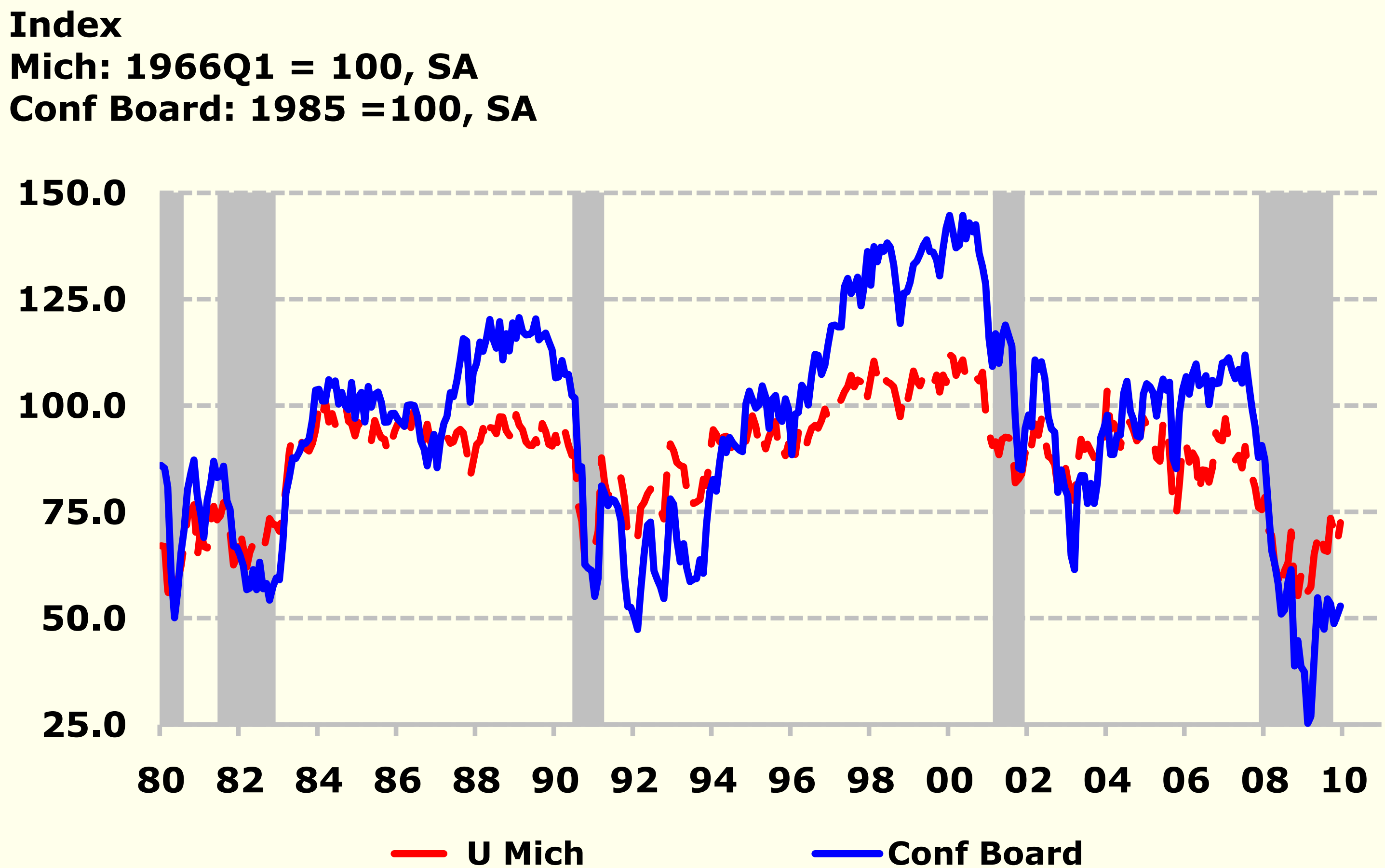
# Consumer confidence is looking for direction




Source: Conference Board, University of Michigan; data through January 2010, preliminary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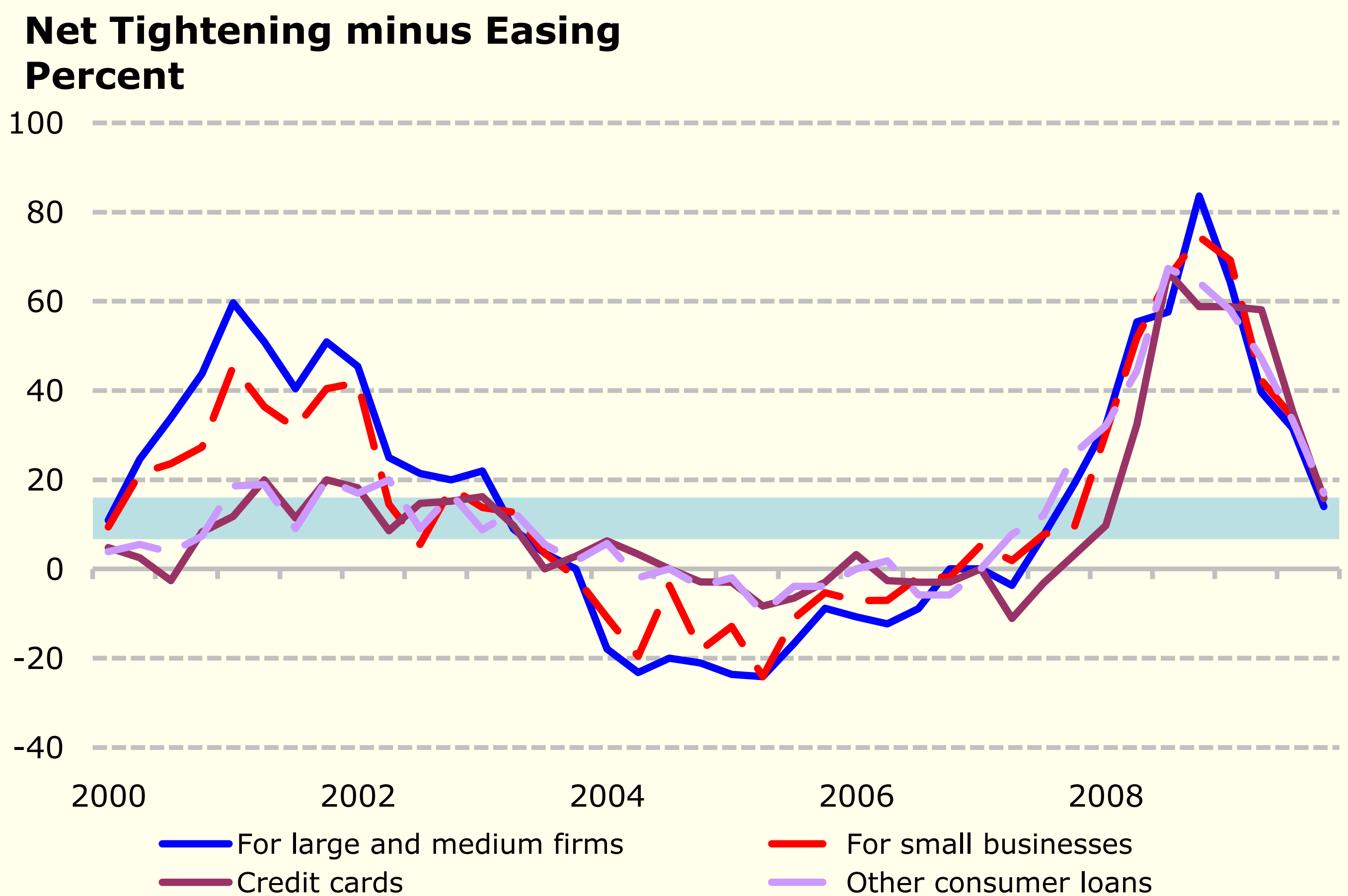
# Bank lending to businesses and consumers appears to be easing, but...

Survey includes 60 large domestic banks and 24 U.S. branches of foreign banks




Source: Federal Reserve Board, Senior Loan Officers Quarterly Survey; data through October 2009 survey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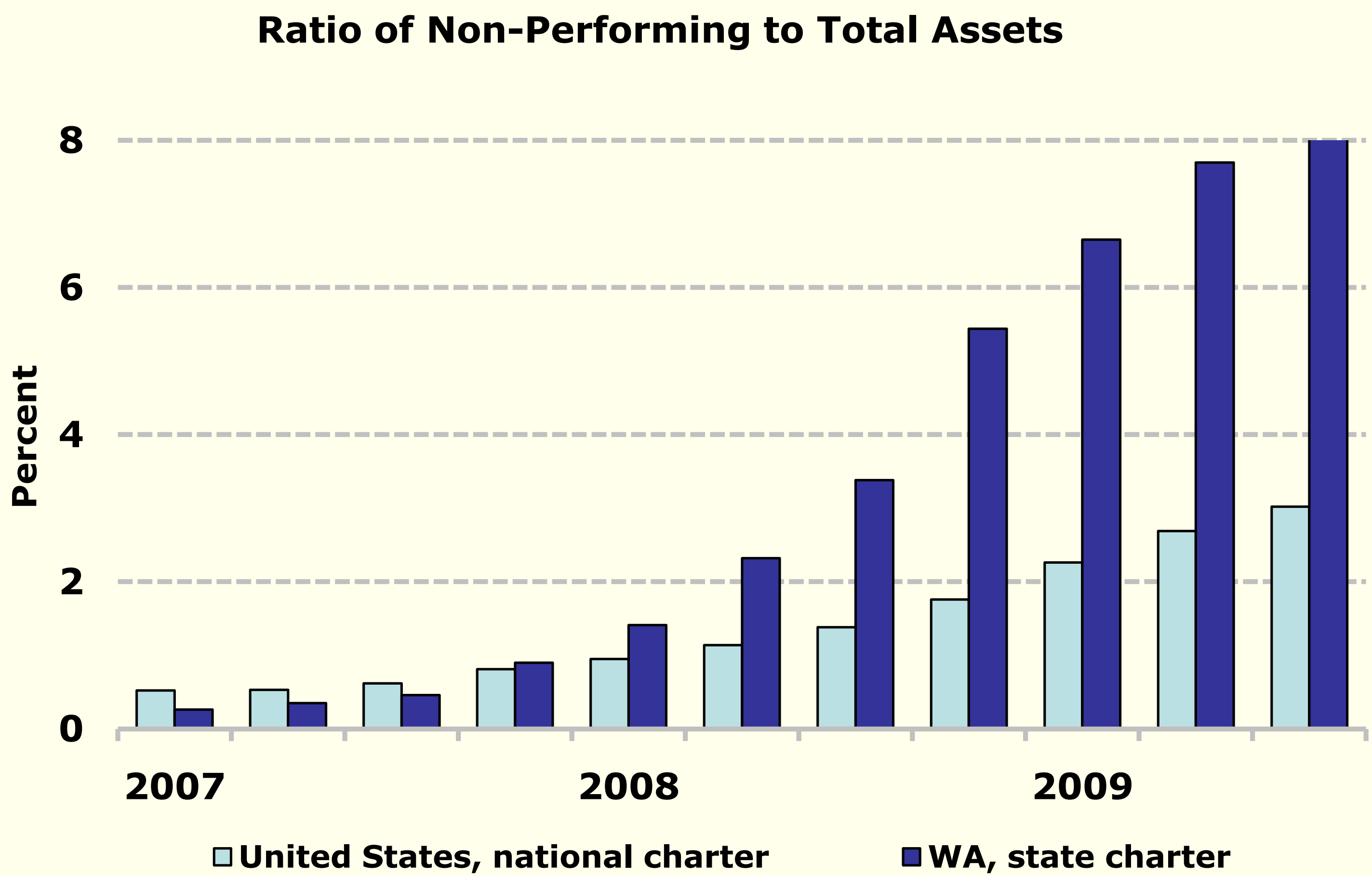
# … asset quality of regional banks is deteriorating because of over exposure to commercial real estate…

This is generally true for state chartered banks in other states as well



Source: FDIC, data through 2009 Q3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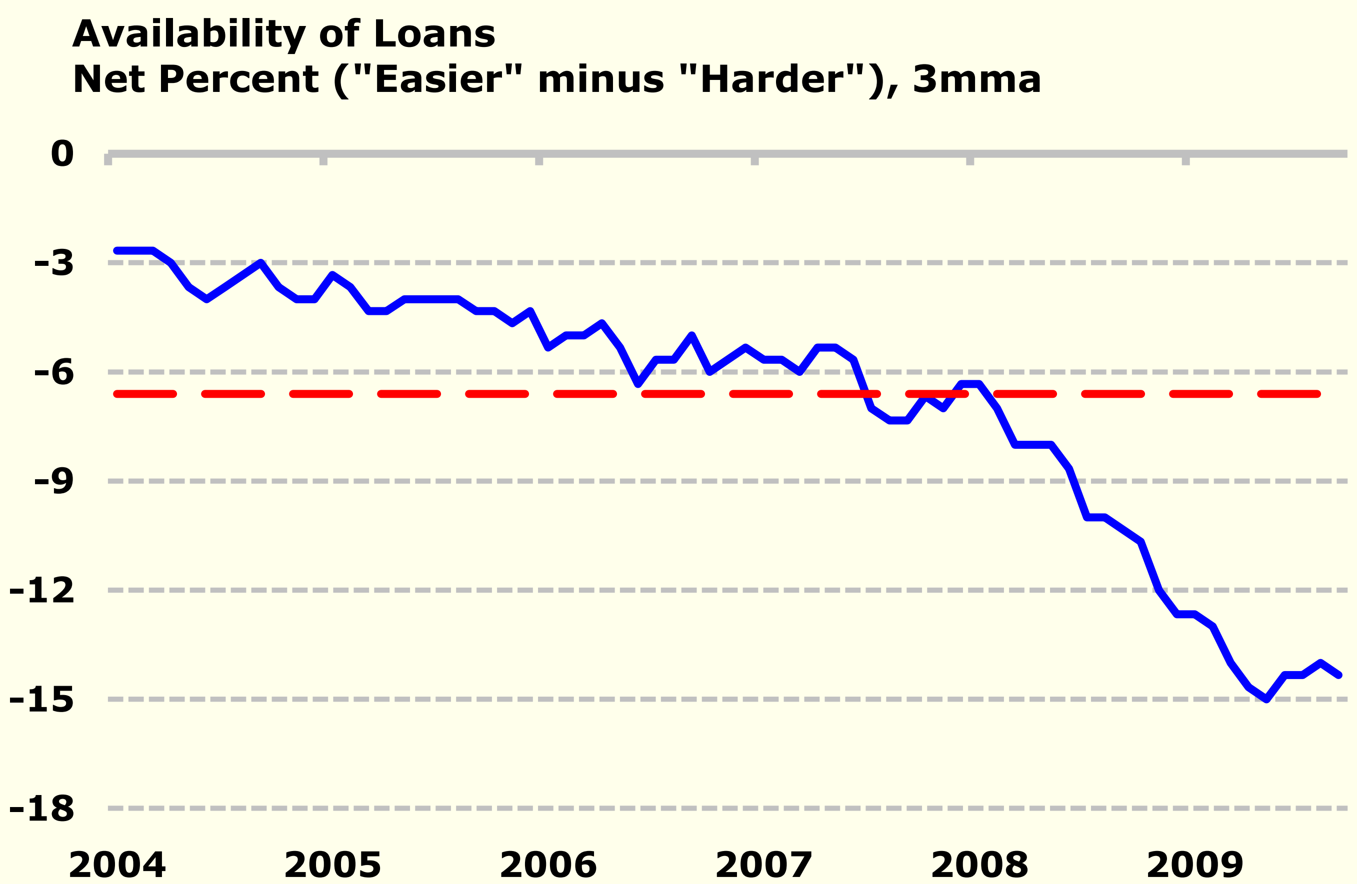
# ... and credit conditions remain tight for small business...




Source: National Federation of Independent Business; data through November 2009

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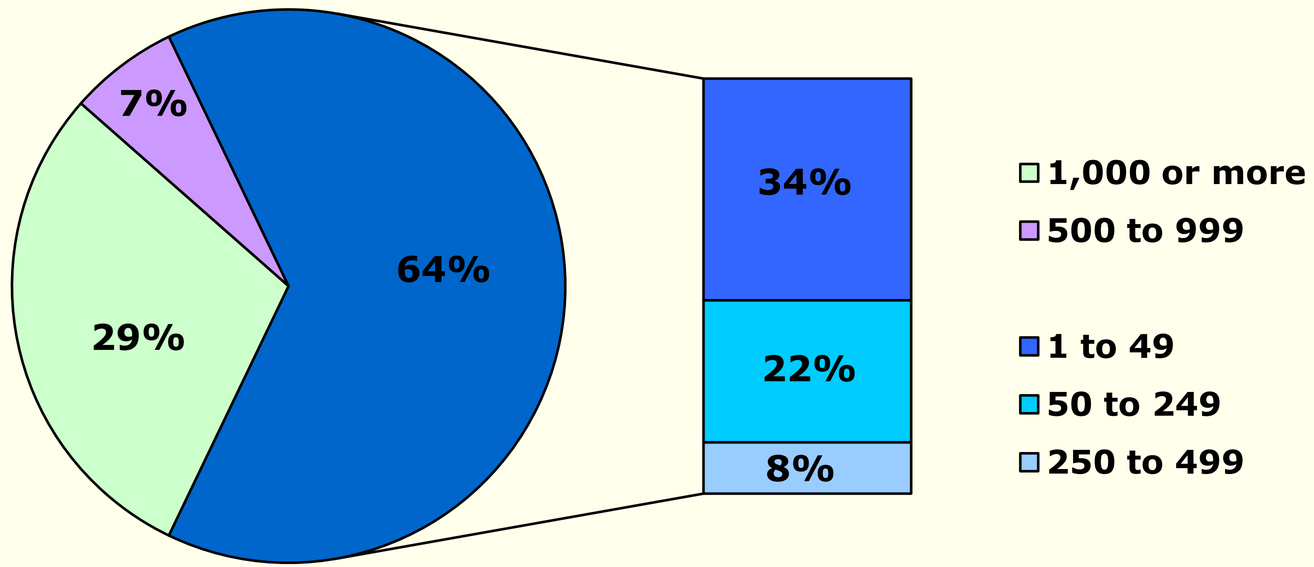
# ... who create most of the jobs

**Since 1992, 64% of the net change in employment has occurred in small businesses**




Source: BLS, data from 1992 Q3 to 2009 Q1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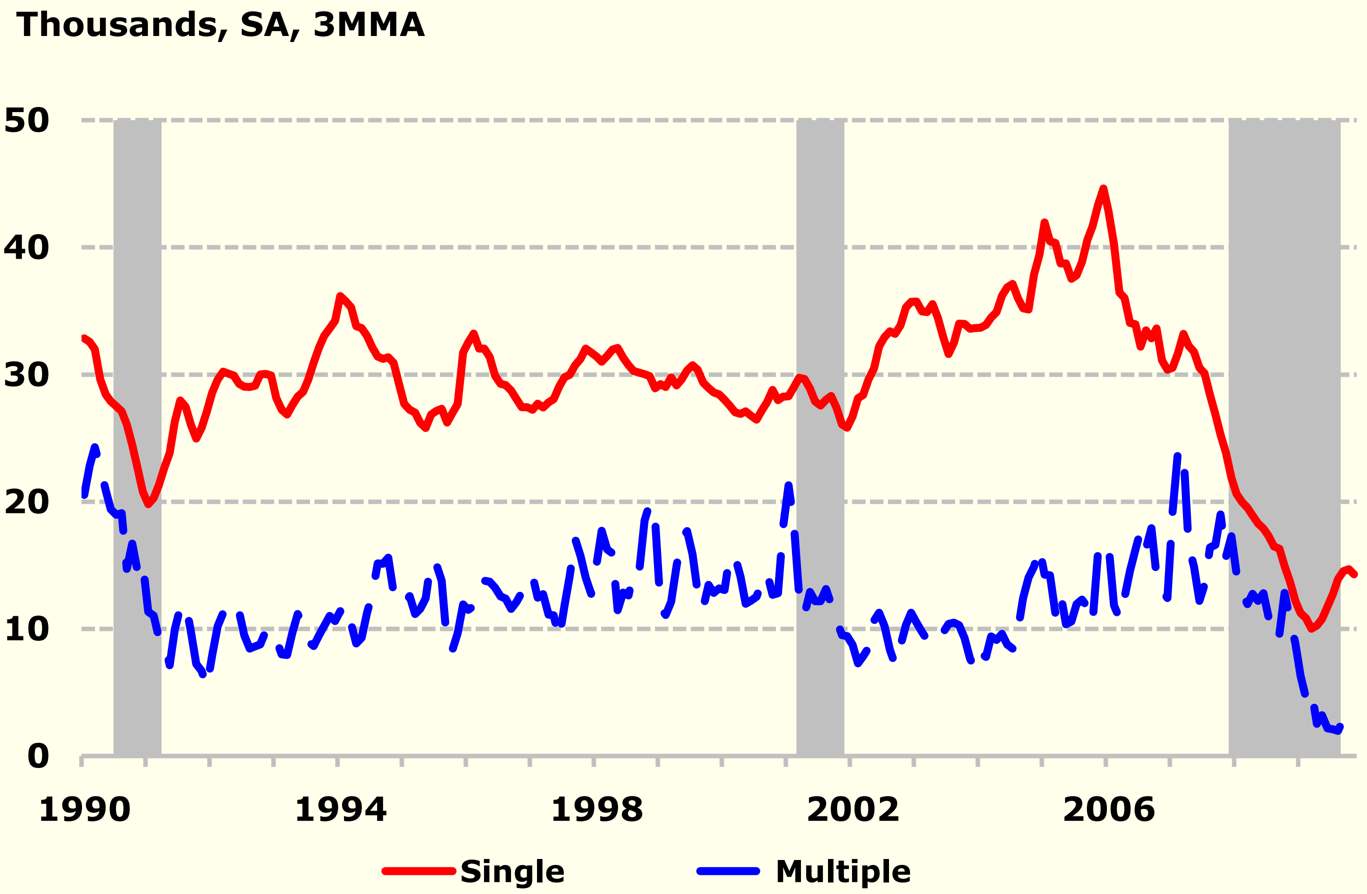
# WA single family building permits are doing better than multi-family




Source: U.S. Census Bureau; data through November 2009

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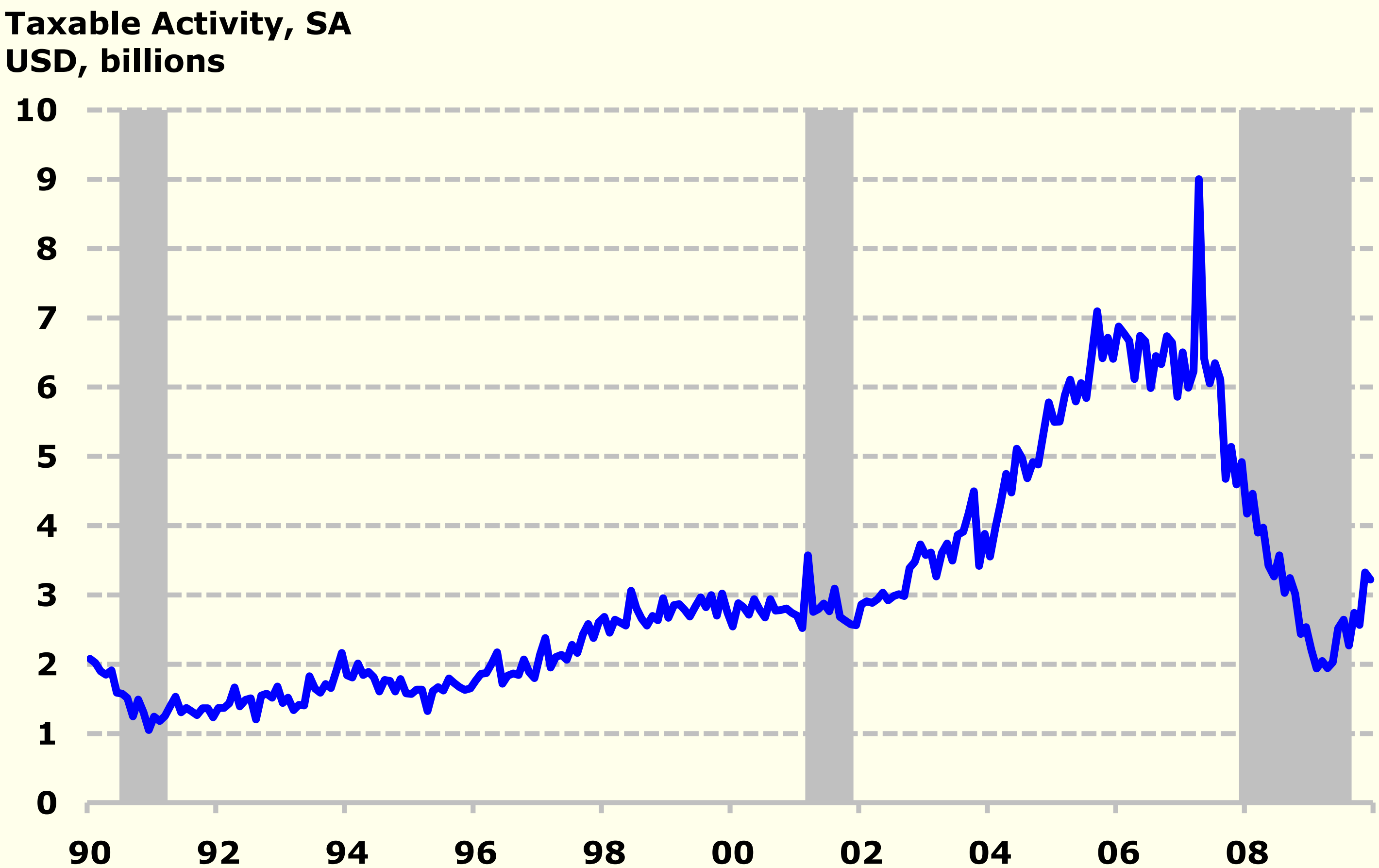
# Taxable real estate excise tax activity is on the rise

December activity was roughly on par with November due to extension of federal tax credit




Source: DOR and ERFC; data through October 2009 preliminary

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# REET transactions soared in November while value per transaction showed first growth in two years

*Taxable activity divided by the total number of transactions.

Activity based on real estate excise tax paid at closing.

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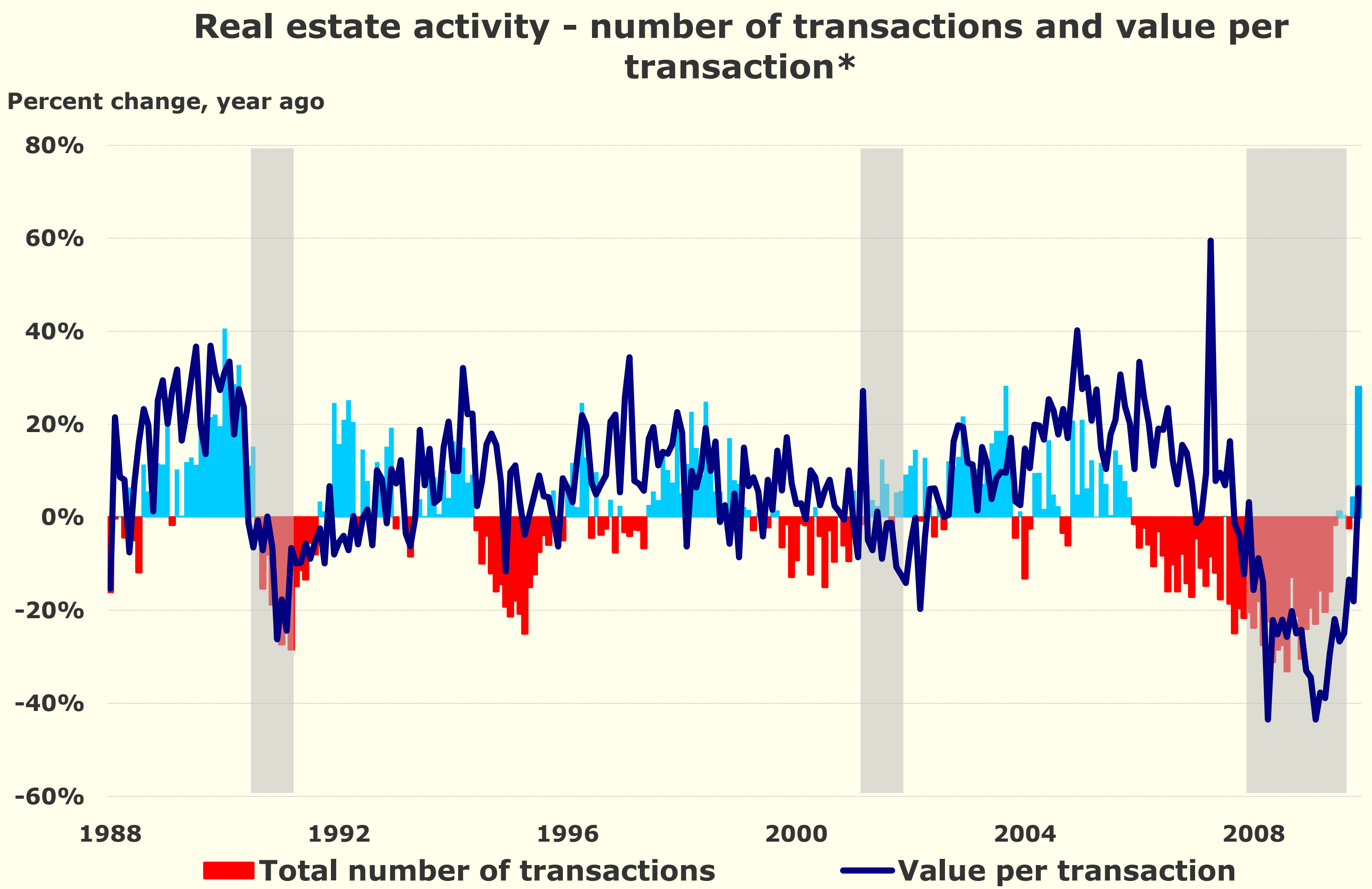
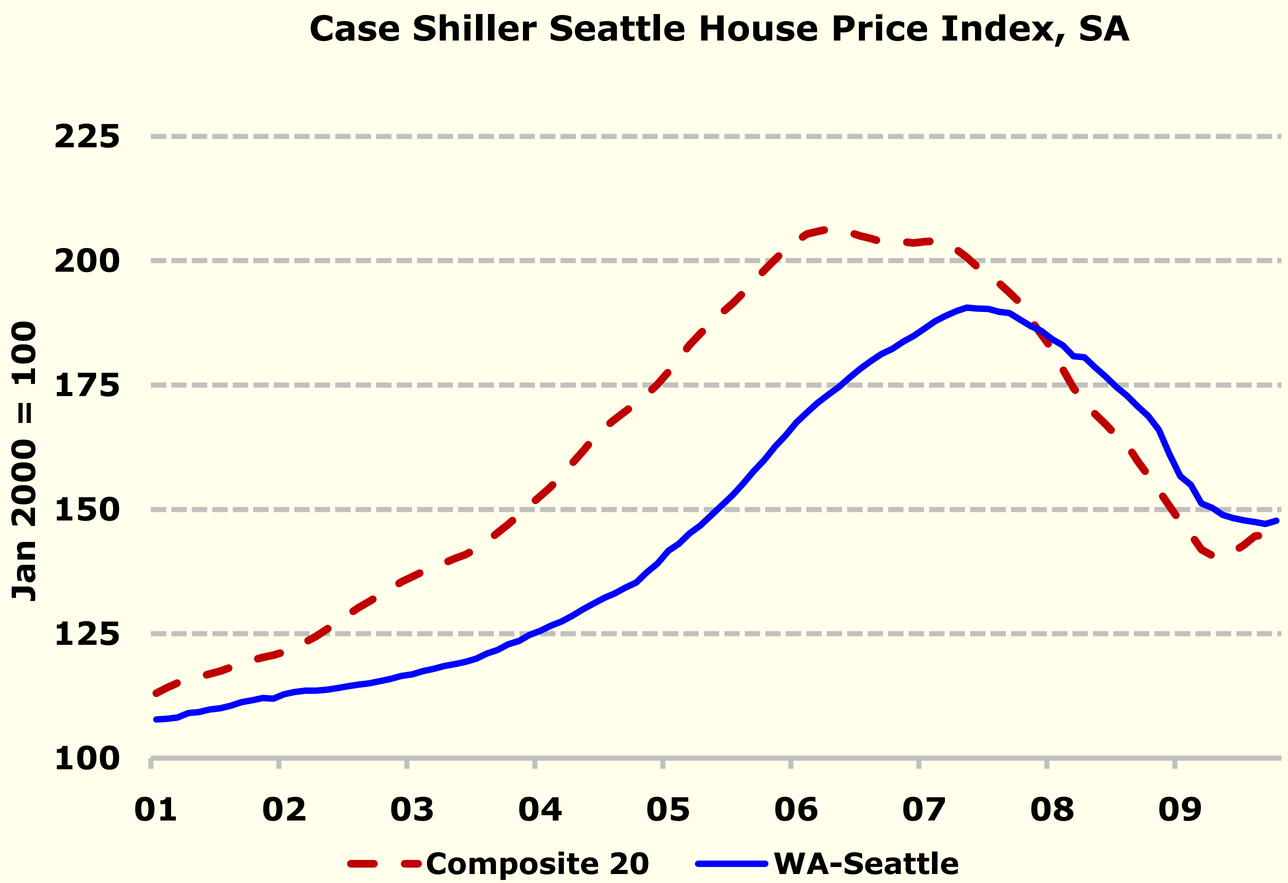



Source: DOR and ERFC; data through November 2009 activity

# Home prices in Seattle appear to be leveling off, but lag the nation in the turnaround

**Seattle Home Prices**




Source: S&P/Case-Shiller; data through October 2009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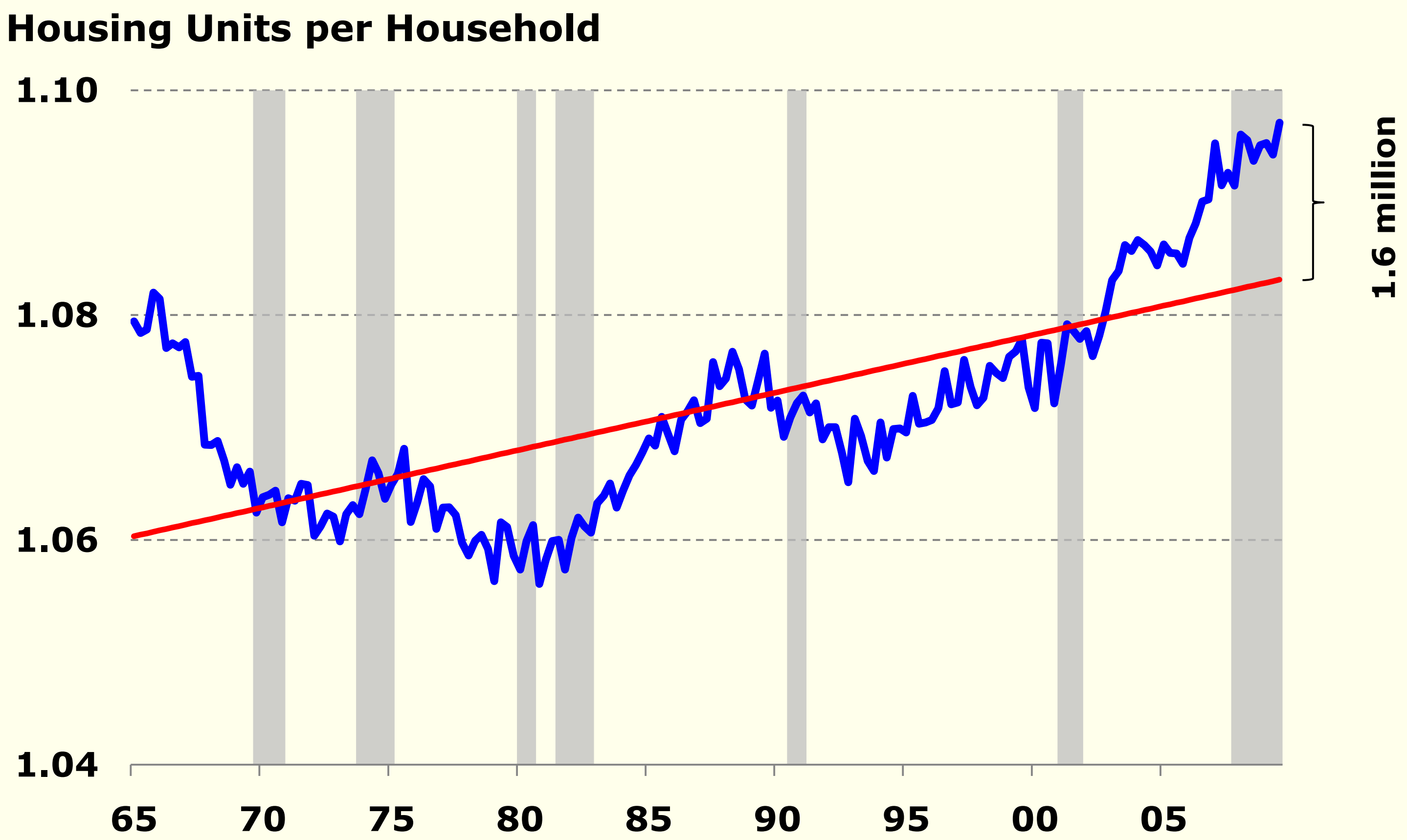
# Housing inventory remains well above trend




Source: U.S. Census Bureau, ERFC; data through 2009 Q3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# Foreclosures are adding to the supply of homes and putting downward pressure on prices

Mortgage Banker's Association

Nov 11, 2009

- The mortgage loans delinquency rate on residential properties rose to 9.6% of all loans outstanding at the end of 2009 Q3
- This is the highest rate of delinquency, since 1972, when the Mortgage Banker's Association started keeping records.
- Prime fixed-rate loans are the largest share of foreclosures started – 33% of 3Q foreclosures started were on prime fixed-rate loans
- Prime fixed-rate loans are 54 % of the increase in loans 90+ days delinquent

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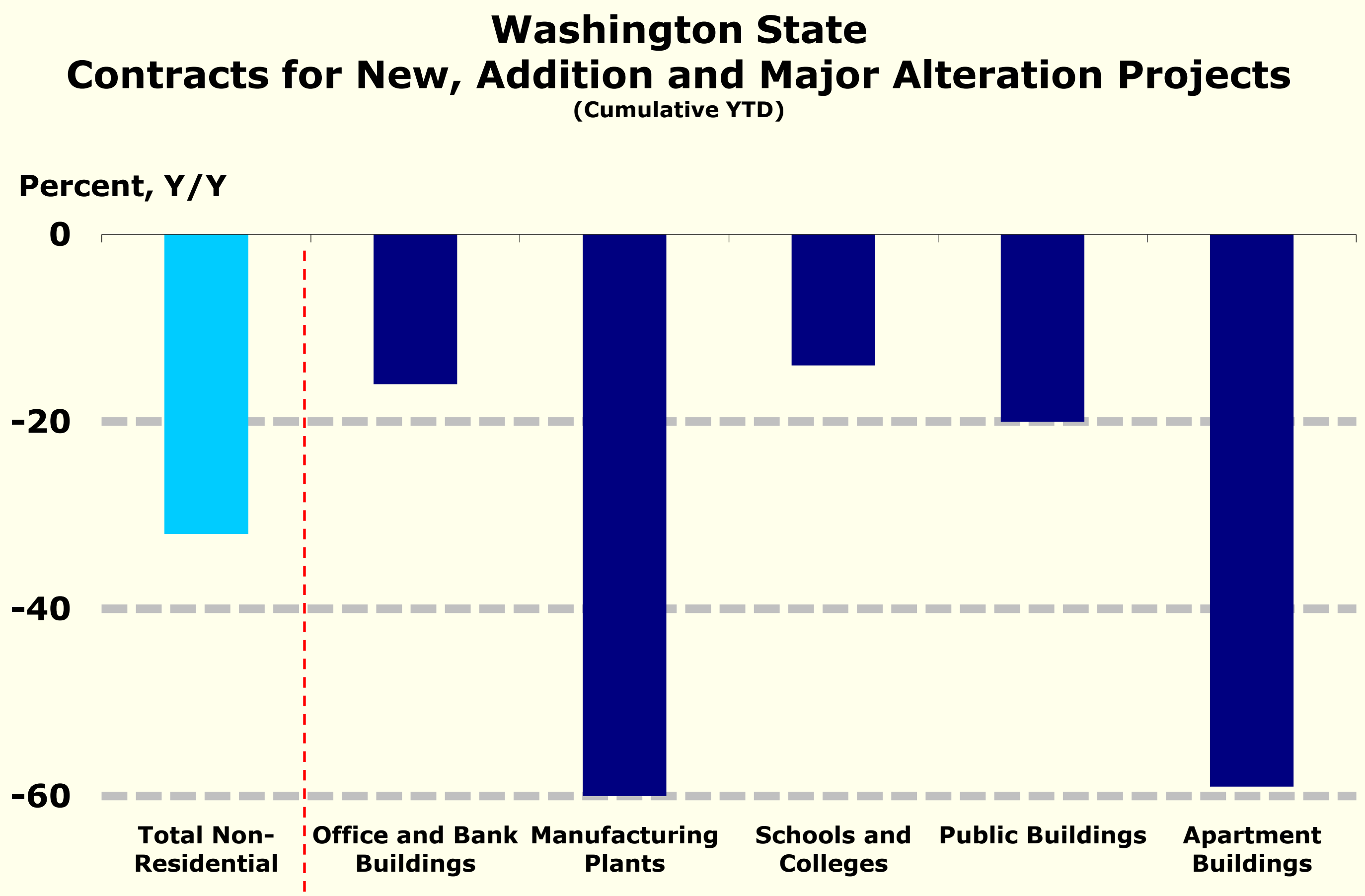
# Contract data indicate WA non-res construction will remain weak




Source: McGraw-Hill Construction, data through November, 2009

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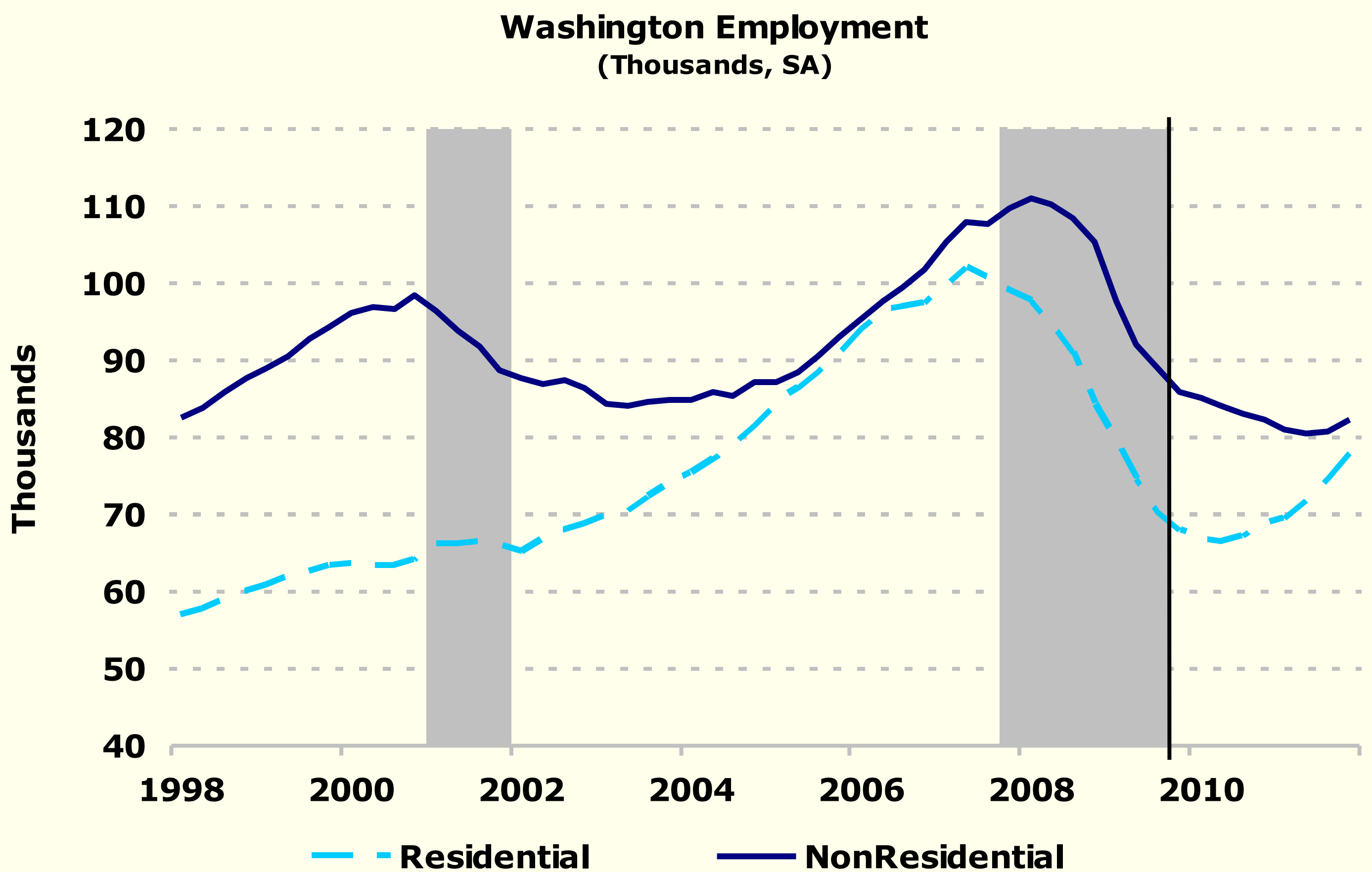
# Non-residential construction will lag residential construction




Source: WA State ESD; actual data through 2009 Q3, ERFC Forecast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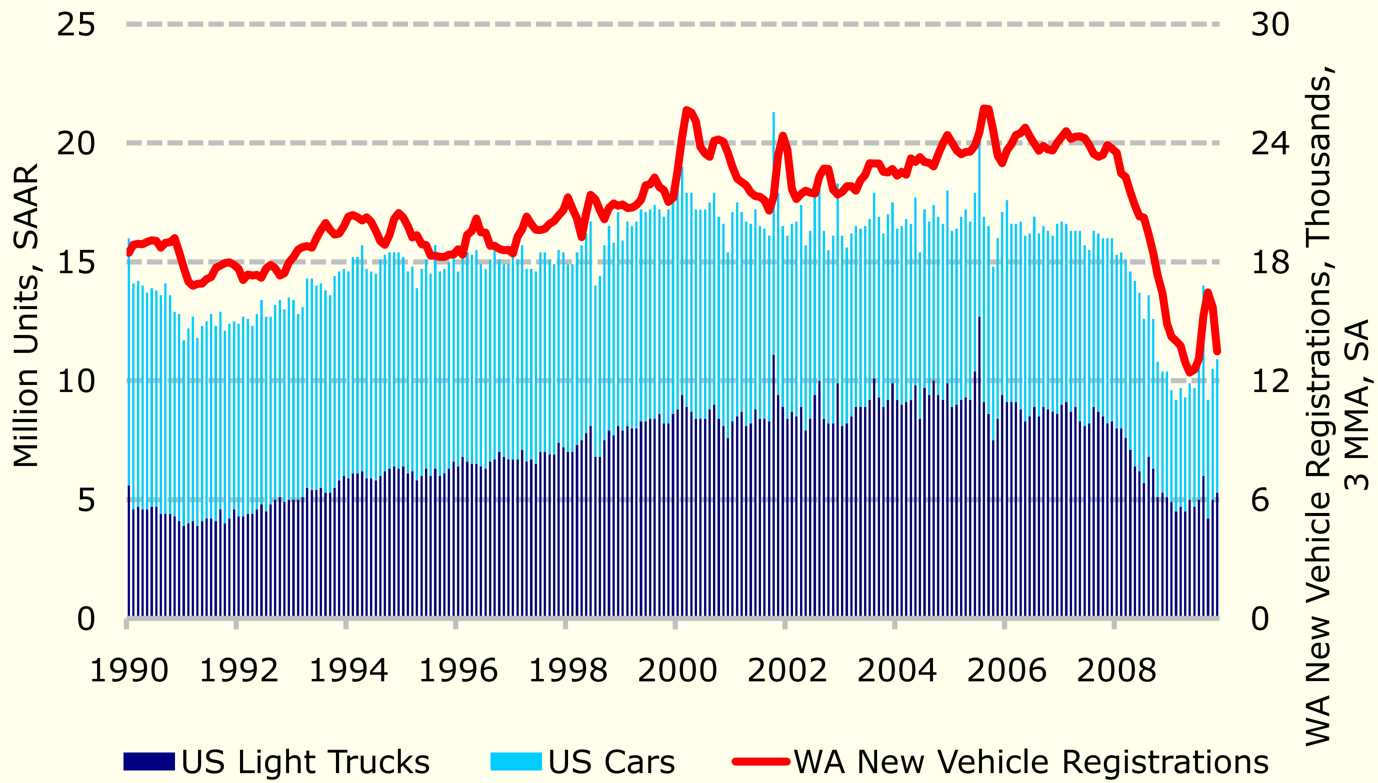
# Automotive sales have stabilized nationally and in the state

National car sales were 2 million units higher in December than in January




Source: Autodata Corporation, WA DOL; data through Dec 2009

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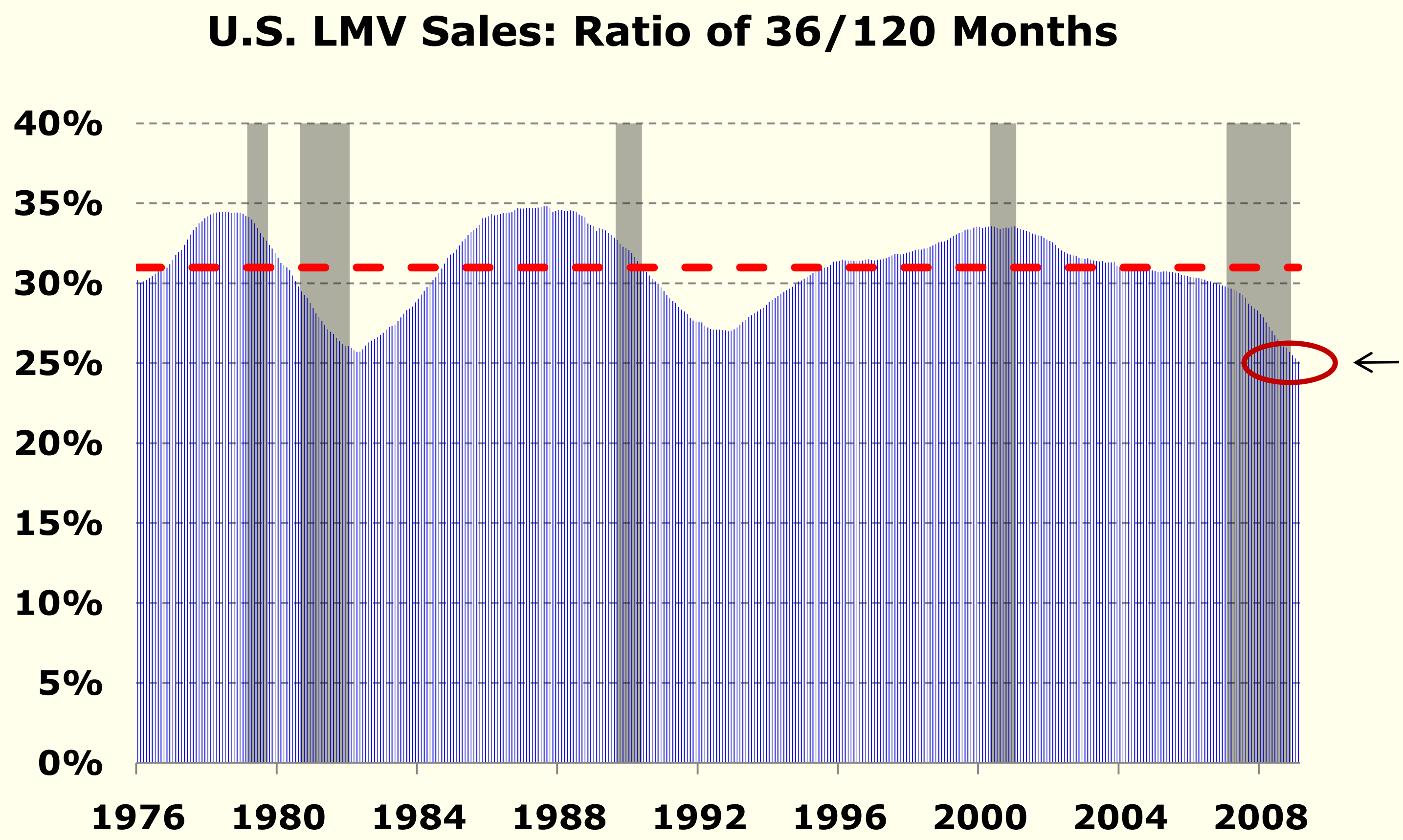
# Relative age of the car fleet indicates imminent turnaround in car sales

The percent of "old" cars on the road is at a historic high




Source: Autodata Corporation, ERFC; data through December 2009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# We are witnessing an unprecedented global recovery

These economies represent 32% of global GDP.

The US is 25% of global GDP

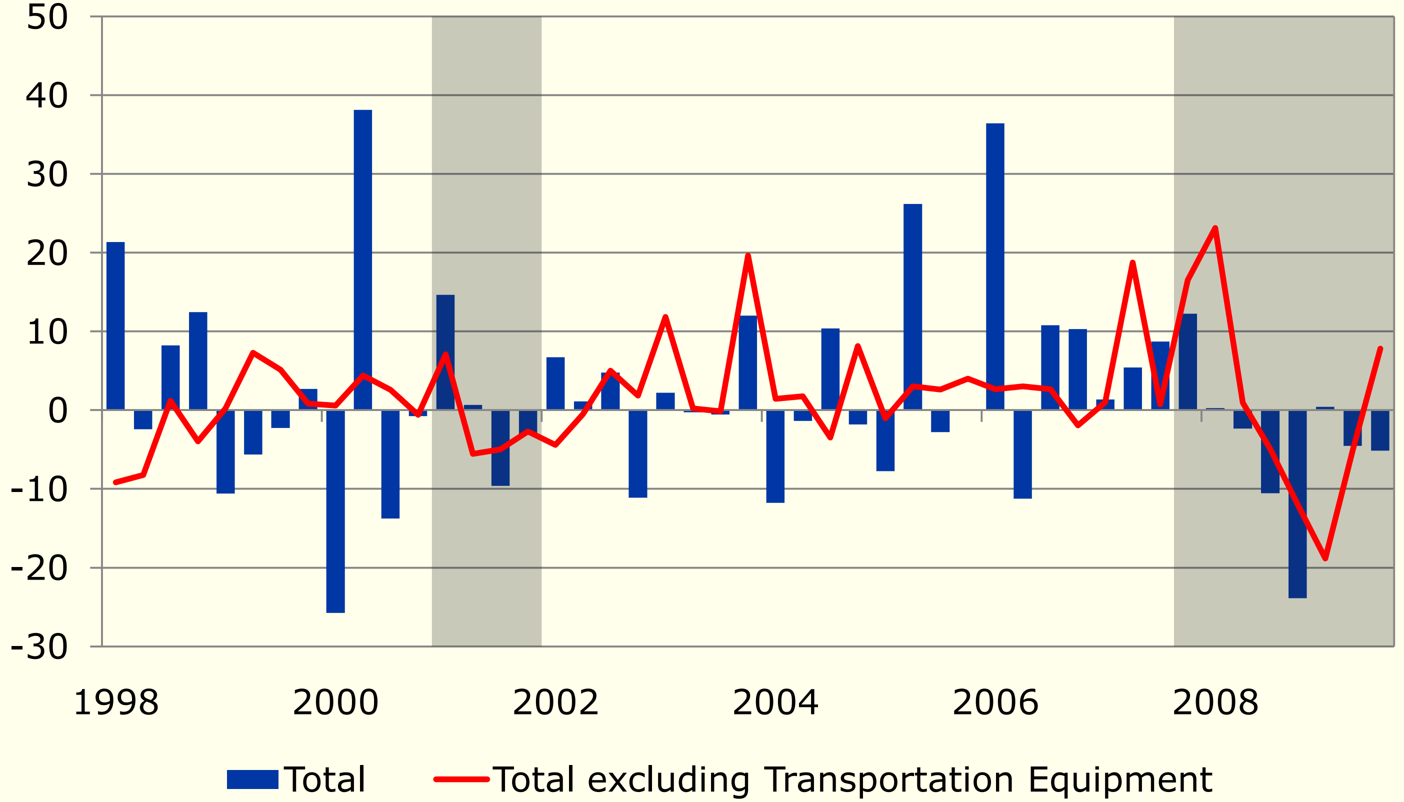
| | | Q/Q, SAAR % | | |
|---|---|---|---|---|
| | GDP share | 2009 Q1 | 2009 Q2 | 2009 Q3 |
| Japan | 8.0% | -14.2 | 2.7 | 4.8 |
| China | 6.2% | 5.6 | 16.0 | 11.5 |
| Germany | 6.0% | -13.4 | 1.8 | 2.9 |
| France | 4.7% | -5.7 | 1.0 | 1.3 |
| India | 2.0% | 7.0 | 6.5 | 13.9 |
| Korea | 1.9% | 0.5 | 9.7 | 12.3 |
| Indonesia | 0.8% | 1.7 | 4.8 | 7.5 |
| Taiwan | 0.7% | -11.3 | 18.8 | 8.3 |
| Thailand | 0.4% | -5.9 | 9.1 | 5.3 |
| Hong Kong SAR | 0.4% | -16.1 | 14.8 | 1.6 |
| Malaysia | 0.3% | -17.7 | 12.3 | 8.7 |
| Singapore | 0.3% | -12.2 | 20.7 | 14.9 |
| Philippines | 0.3% | -8.3 | 7.0 | 4.1 |

Source: Goldman Sachs, ERFC

# Exports will help the state recover faster than the nation

Exports excluding transport equipment was up 8% in Q3

**Exports, SAAR**
**Percent Change, quarter ago**




Source: Wiser Trade Data; through 2009 Q3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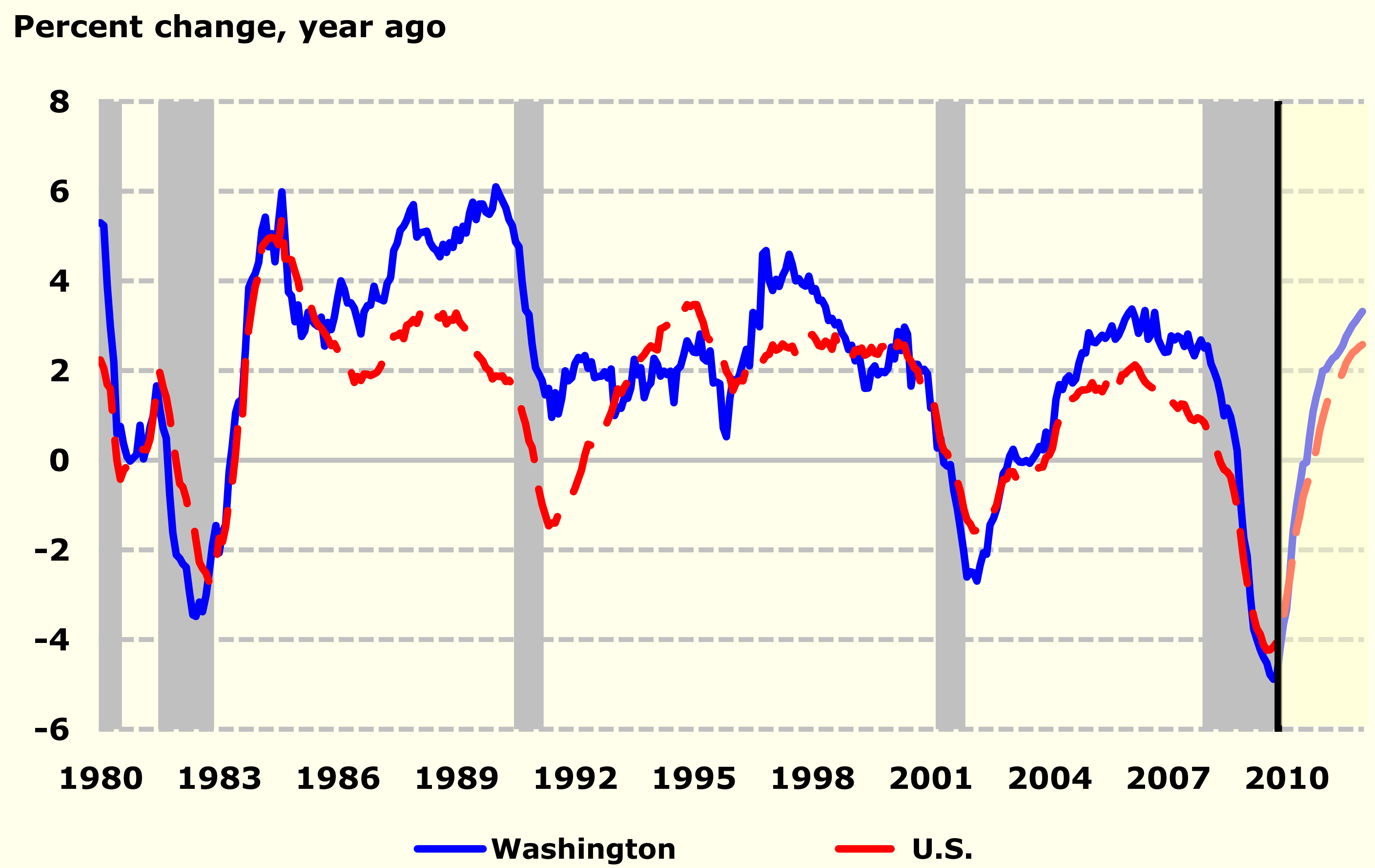
# WA employment lagged the nation in the downturn and will recover a little stronger than the nation




Source: ERFC November 2009 forecast; actual through October 2009

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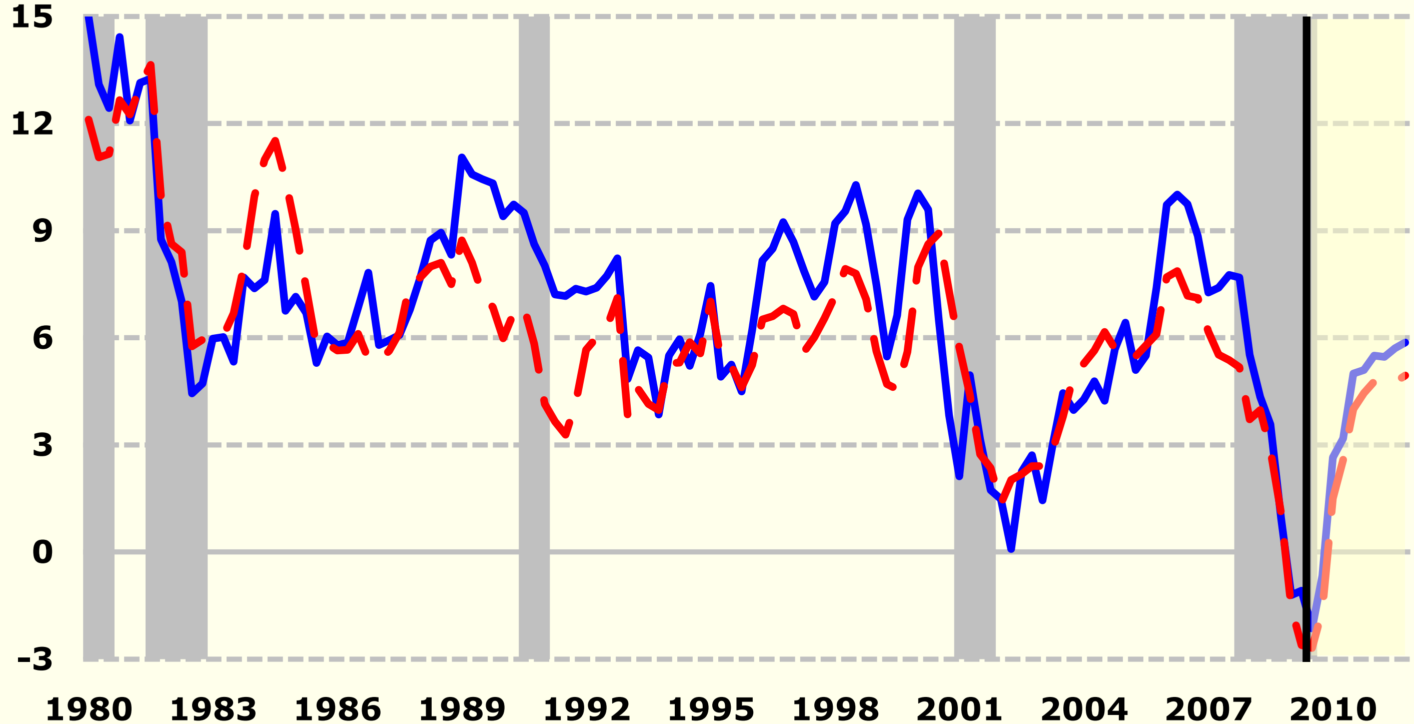
# The recovery in WA personal income growth is expected to be better than the nation's

Percent change, year ago




Source: ERFC November 2009 forecast; actual data through 2009Q2

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# General Fund* forecast by fiscal year

* General Fund & Related Funds for FY 07, 08, and 09

General Fund – new definition, for FY 10, and 11

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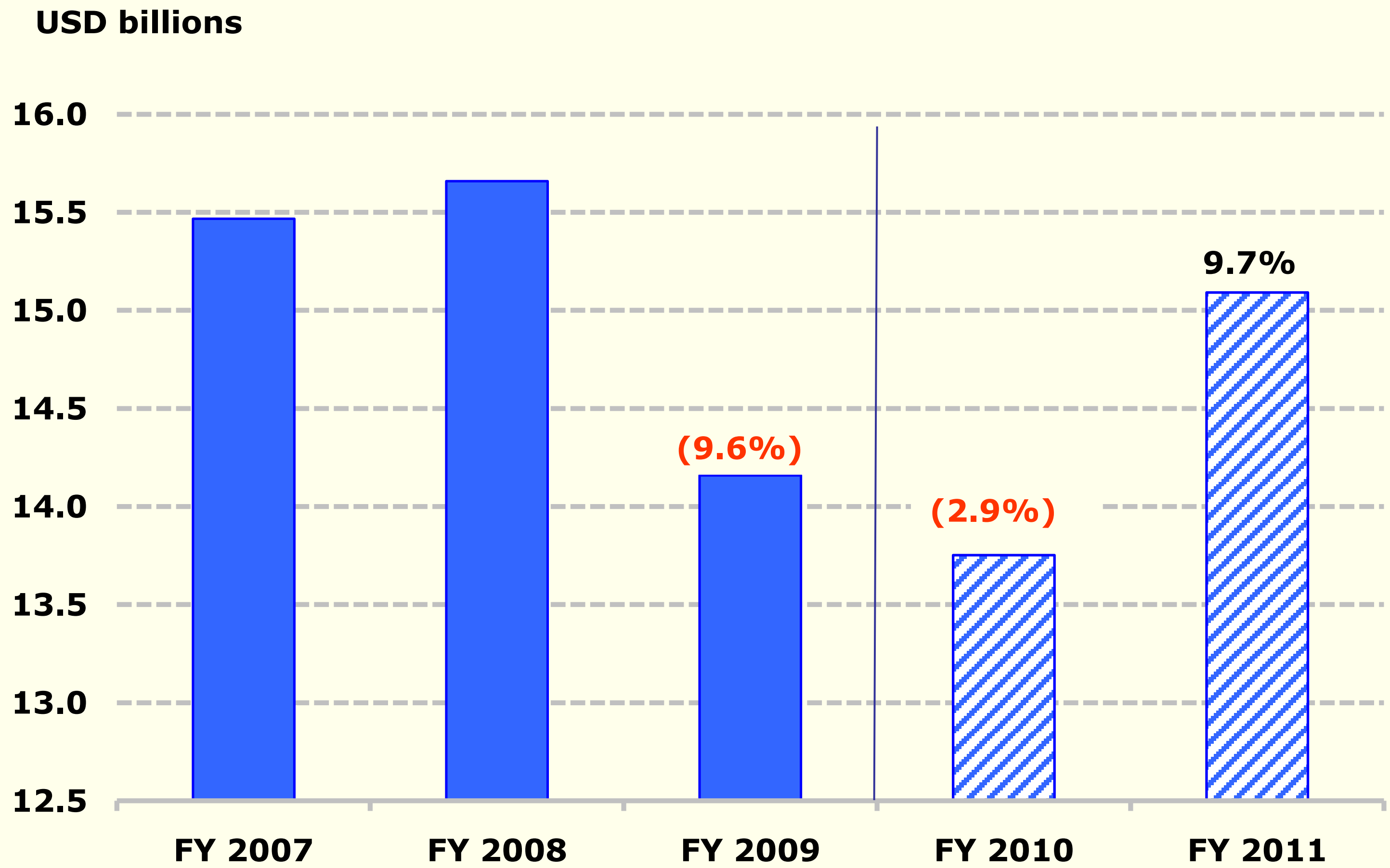


Source: ERFC forecast, November 2009

# Conclusion

Pluses

- Recovery in progress
- Employment likely to improve soon
- Car sales have stabilized
- Large banks able to extend credit

Minuses

- Problems at community banks
- Weak consumer confidence
- Slow recovery in construction

- Consumer spending has to recover for this to become a self-sustaining recovery and for revenues to grow again
- Housing is expected to recover early in 2011; non-residential later that year

# Questions

**Economic & Revenue Forecast Council**
**1025 E. Union Avenue, Suite 544**
**Olympia WA 98504-0912**

**www.erfc.wa.gov**
**360-570-6100**