THE PUGET SOUND
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More Good Than Bad

The U.S. Bureau of Labor Statistics reported that the nation created 295,000 jobs in February, driving the unemployment rate down to 5.5 percent, the lowest in seven years. Upon release of the employment numbers, the Dow plummeted 330 points. What gives?

Apparently, there is concern in the stock market that accelerating job growth will prompt a hike in interest rates by the Federal Reserve. That would increase the value of the dollar and reduce the profits of multinational corporations.

Even so, it is hard to understand the stock market's reaction, since it seems that the good news on the labor front far outweighs any bad news regarding the overseas performance of multinationals. Indeed, the accelerating job growth in 2014, creating more than three million new employment opportunities, holds promise of a sustained economic recovery unmatched since the 1990s.

Summary Forecast

Annual Percent Change

	2013	2014	2015	2016
Puget Sound Region				
Employment	2.8	3.0	2.6	1.9
Personal income (cur. $)	2.6	4.9	5.5	5.4
Consumer price index	1.3	1.8	0.6	2.3
Housing permits	8.9	17.1	-9.4	6.0
Population	1.4	1.4	1.3	1.2
United States*				
GDP ($09)	2.2	2.4	3.2	2.9
Employment	1.7	1.9	2.0	1.7
Personal income (cur. $)	2.0	3.9	4.3	5.1
Consumer price index	1.5	1.6	0.4	2.2
Housing starts	18.7	8.0	15.6	12.1

*Source: Blue Chip Economic Indicators

As hiring continues and the unemployment rate falls, wage rates will rise and reinforce the recovery. Anecdotes of people turning down employment offers or walking away from old jobs in search of higher pay—not to mention Wallmart's surprising offer to raise its entry level wage to $9.00 per hour—indicate that this stage of the recovery is already underway.

As much as the labor market has improved in the United States, it is even better in the Puget Sound region. Over the course of 2014, regional employment increased 2.9 percent, while the unemployment rate fell to 5.1 percent. Since the recession, average annual wages in current dollars have climbed at a 2.9 percent annual rate, 0.6 percentage points faster than national wages.

Regional Outlook

Sorting through things.

As this article is being written, the Dow has just fallen 330 points. In the past, there has been concern that the Federal Reserve's reluctance to apply the brakes to the economy during the recovery would ignite inflation. Now, the stock market fears that the Fed will raise interest rates as early as June.

All this was in reaction to the latest labor report, which showed that in February the nation added 295,000 jobs and lowered the unemployment rate to 5.5 percent. The job gains edged the economy closer to full employment and the trigger-point for Fed action.

Higher interest rates would increase borrowing costs and the value of the dollar. A stronger dollar effectively raises the price of U.S. exports and dampens the foreign sales of companies like Boeing and Microsoft. At the same time, a stronger dollar effectively lowers import prices, increasing the purchasing power of American consumers. The immediate reason for the Dow's drop was the expectation that a stronger dollar would reduce the profits of multinational corporations.

Should we be concerned about this? There are two reasons why the situation may not be as bad as it looks. First, this is still speculation, as evident by the com-

INSIDE

Regional Outlook

ment of one reporter: "U.S. stocks dropped…on increasing *views* the Federal Reserve *may* raise rates."

Second, with regard to U.S. exports—a critical consideration for our trade-dependent region—it is unclear how foreign sales would hold up against a stronger dollar. In response to a subscriber's inquiry, we checked the March 10 Blue Chip outlook. After rising 3.1 percent in 2014, U.S. exports are predicted to increase 4.2 percent in 2015 and 7.7 percent in 2016. This is not an unreasonable forecast, even with higher export prices, since the world economy is expected to grow 3 percent this year and next.

If you are having difficulty sorting through these arguments, trying to figure out what to believe, welcome to the forecasting game. Economic forecasting is more than just dropping numbers into an econometric model and turning the crank. It also requires side analyses and judgment. For example, we do not utilize a forecasting equation for Boeing employment. Instead, our judgmental predictions are based on the Boeing aircraft backlog-delivery ratio, a component of our index of leading economic indicators, and company announcements.

To handle more complicated issues, like the rising value of the dollar, we rely on the fifty Blue Chip national economists. Their highly sophisticated models do portray how the value of the dollar affects foreign exports, real Gross Domestic Product (GDP), and industrial production. Since we use their consensus predictions of real GDP and industrial production as input to the Puget Sound Economic Forecasting Model, our current regional outlook reflects, at least in part, Blue Chip's optimistic scenario for U.S. exports.

Something more important.

With all due respect, the Dow got it wrong. How terrific news about labor got twisted into bad news about potential profit losses is puzzling.

Indeed, the latest jobs report is probably the best sign yet that the national economy is now engaged in a sustained recovery. For labor it has been a long time coming.

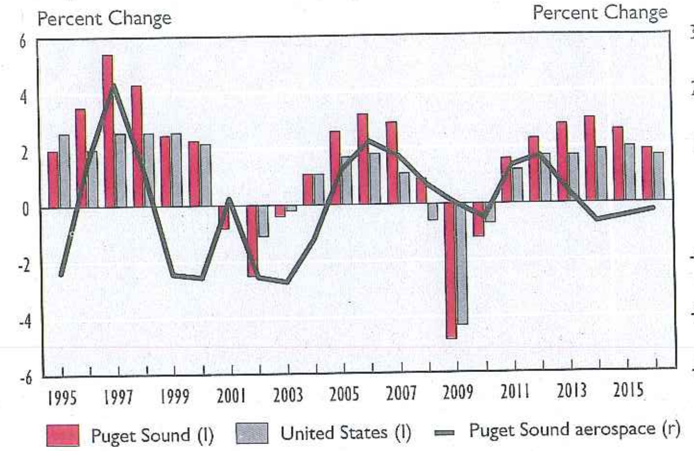
Between 2000 and 2010, the Dismal Decade culminating in the Great Recession, U.S. real GDP grew at half-speed. Because gains in labor productivity outpaced real GDP growth, nonagricultural wage and salary employment fell from 132.0 million in 2000 to 130.3 million in 2010, a loss of 1.7 million jobs. Over the prior ten years, the U.S. economy created 22.5 million jobs.

Between 2000 and 2010, the U.S. unemployment rate rose from 4.0 percent to 9.6 percent. The number of underutilized workers—unemployed people, labor force dropouts, part-time workers desiring full-time jobs—escalated from 10.1 million to a previously unimaginable 26.2 million.

Technically, the recession ended in the middle of 2009, but employment did not bottom out until early 2010. Since then the national economy has added 11.5 million jobs through February, lowering the unemployment rate to 5.5 percent and reducing the number of underutilized workers to 17.3 million. This decade the U.S. economy is on track to create as many jobs as it did in the 1990s. As another positive development, the latest labor report noted that every major industry except mining is currently expanding its workforce.

Our expectation that the national recovery has a good ways to go is based on three observations. First, job growth is accelerating. After averaging 2.5 million new jobs per year since 2011, the economy created 3.3 million jobs between February 2014 and February 2015. Second, with 17.3 million underutilized workers, there is little chance of running out of labor and cutting short the recovery. Third, the national economy is finally experiencing significant income gains, which will provide additional support for

Puget Sound and U.S. Employment



U.S. Real Gross Domestic Product
Percent Change

	2013	2014	2015	2016
Gross Domestic Product ($09)	2.2	2.4	3.2	2.9
Personal consumption	2.4	2.5	3.3	2.8
Nonresidential investment	3.0	6.1	5.3	5.2
Residential investment	11.9	1.6	6.6	10.9
State and local government	0.5	0.9	1.8	2.0
Federal government	-5.7	-1.9	-0.6	-1.4
Exports	3.0	3.1	4.2	7.7
Imports	1.1	3.9	4.9	7.6

Puget Sound Employment and Unemployment Rate

	2013	2014	2015	2016
Employment (% change)				
Puget Sound Region	2.8	3.0	2.6	1.9
King County	3.5	3.5	2.9	1.9
Kitsap County	0.1	1.7	1.9	2.2
Pierce County	2.0	3.0	2.1	1.7
Snohomish County	1.2	1.3	1.9	2.1
Unemployment rate (%)				
Puget Sound Region	6.0	5.3	4.9	4.8
King County	5.2	4.7	4.1	4.0
Kitsap County	6.8	5.8	6.2	5.9
Pierce County	8.0	6.8	7.0	6.6
Snohomish County	5.8	5.2	4.5	4.4

the expansion. After declining 0.6 percent between 2010 and 2013, nonfarm business real hourly compensation increased 0.8 percent in 2014, according to the U.S. Bureau of Labor Statistics.

Puget Sound and U.S. employment both hit bottom at the same time during the recession. Since then the region has recovered much faster than the nation. Between the first quarter of 2010 and the fourth quarter of 2014, regional and national jobs grew at annual rates of 2.4 percent and 1.6 percent, respectively. After climbing to 9.7 percent during the recession, the Puget Sound unemployment rate dropped to 5.1 percent by the end of 2014, 0.6 percentage points below the national rate at that time.

Since the trough of the recession, the region has added 205,600 jobs. This is a remarkable number considering that in the prior ten years, the region managed to boost its employment by a paltry 14,000.

In terms of job creation, the leading sectors have been other services (61,200), professional and business services (42,200), wholesale and retail trade (38,100), construction (16,800), aerospace (9,900), other durable goods manufacturing (9,100), information (8,700), and financial activities (8,400).

Despite being the largest contributor of new jobs, other services is not considered a driver of the regional economy, as it mainly caters to local businesses and households. Professional and business services is a mix of basic activities (e.g., engineering services) and nonbasic activities (e.g., temporary employment services). Much of the job gain in wholesale and retail trade is attributable to Amazon. Construction employment has bounced back from the housing collapse but it still remains well short of it previous peak. Apart from Amazon, the strength of the Puget Sound economy during the recovery is most evident in the job gains in aerospace, other durable goods manufacturing, and information, all key basic sectors. Financial activities has added back only one-half of the jobs it lost during the recession.

In addition to jobs, the Puget Sound recovery has gotten a helping hand from rising wages. Between 2009 and 2014, average annual wages measured in current dollars grew at a 2.9 percent annual rate, increasing from $57,200 to $66,100. Concurrently, national wages rose at a 2.3 percent rate, from $47,700 to $53,500.

Of late, Boeing and Microsoft have been gradually paring down their local workforce. Consequently, we are predicting a slowdown for the regional economy, though as yet we see no evidence of it. The current outlook calls for job growth to decelerate from 3.0 percent in 2014 to 2.6 percent in 2015 and 1.9 percent in 2016. Nevertheless, with ongoing support of the national recovery, we can look forward to another 90,000 jobs over the next two years and 200,000 new jobs by the end of the decade.

Never certain.

The careful reader will have noticed that the probability attached to the baseline forecast has remained at 55 percent for three years. This is not neglect on our part. Rather, it indicates that nothing has happened to cause us to radically change the odds that the regional economy is headed for either a recession or explosive growth. As the economic recovery has progressed, we have become more hopeful. Consequently, we have raised the odds of our optimistic scenario (Blue Chip High) from 25 percent to 30 percent.

Forecast Probabilities

Blue Chip High	30 percent
Baseline	55 percent
Blue Chip Low	15 percent

Alternative Scenarios

Annual Percent Change

	2014	2015	2016
Blue Chip High			
Employment	3.0	3.2	2.7
Personal income (cur. $)	4.9	6.5	6.7
Consumer price index	1.8	1.5	3.2
Housing permits	17.1	11.3	6.1
Population	1.4	1.4	1.5
Blue Chip Low			
Employment	3.0	2.3	1.4
Personal income (cur. $)	4.9	5.1	4.7
Consumer price index	1.8	-0.6	1.2
Housing permits	17.1	-18.6	-0.6
Population	1.4	1.3	1.1

Retail Sales

Cheaper driving, more eating out?

Puget Sound retail spending nearly came to a standstill in the fourth quarter of 2014. Based on U.S. retail sales published by the Census Bureau, we estimate that regional retail sales inched up at an annual rate of 0.8 percent. This follows increases averaging 6.5 percent in the first three quarters of the year.

But there is a silver lining to this tumble or at least a satisfactory explanation. Sales at gasoline stations plunged at an estimated rate of 30 percent in the fourth quarter due to the drop in gas prices. Excluding gas station sales, regional retail spending rose at a 4.0 percent rate.

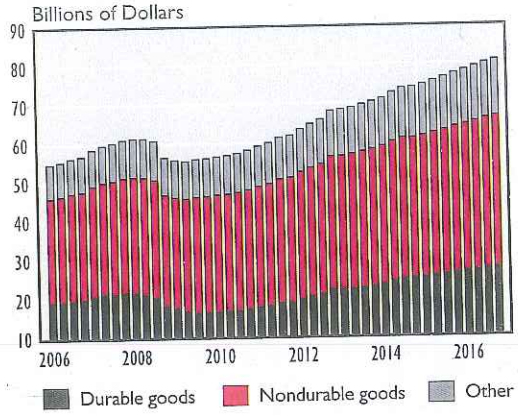
Moreover, if sustained, the drop in gas prices should be a big boon to consumers, who will use much of the savings on other purchases. According to some estimates, lower gas prices could save the average household as much as $750 annually. Where will the new-found dollars be spent? It will take time to sort it out, but within the retail trade sector restaurants and bars appear to be an early beneficiary. Monthly U.S. figures show that sales at food service and drinking places rose at an annual rate of 12.5 percent between July 2014 and January 2015.

With regard to retail sales excluding gasoline, the 4.0 percent growth rate in the fourth quarter was still disappointing. It was caused by decelerating growth in regional personal income, an uptick in the unemployment rate, and a downtick in housing permits.

While these influences are expected to linger in the first half of this year, the next two years look good. In 2015 and 2016, personal income will grow at a 5.5 percent average rate, the unemployment rate will slide to 4.8 percent, and annual housing permits will level out at 20,500 units, just shy of their long-run average.

As a result, Puget Sound retail sales are expected to grow at a 4.5 percent rate, only one-half percentage point slower than last year. Divided into three main categories durable goods (led by autos), nondurables (led by food and beverage sales), and "other" (including e-commerce and mail-order sales) the expected average growth rates are 5.4 percent, 3.4 percent, and 5.6 percent, respectively.

Puget Sound Retail Sales



PUGET SOUND RETAIL SALES

	2014		2015			Years			
	3	4	1	2	3	2013	2014	2015	2016
Retail sales (bils. $)	73.927	74.066	74.784	75.739	76.606	69.462	73.025	76.169	79.685
Building materials	5.588	5.674	5.642	5.618	5.675	4.987	5.467	5.677	5.994
Motor vehicles and parts	16.171	16.281	16.476	16.831	17.080	14.708	15.879	16.929	17.825
Furniture and electronics	3.232	3.250	3.236	3.267	3.322	2.993	3.193	3.300	3.451
General merchandise	8.714	8.794	8.903	8.988	8.991	8.211	8.630	8.980	9.183
Food and beverage	8.999	9.086	9.161	9.236	9.311	8.766	8.966	9.274	9.574
Gasoline stations	6.971	6.435	6.537	6.634	6.729	6.882	6.850	6.681	7.068
Clothing and accessories	3.702	3.741	3.780	3.827	3.874	3.521	3.667	3.850	4.024
Food services and drinking	7.650	7.740	7.818	7.914	8.008	7.268	7.600	7.960	8.323
Other retail sales	12.900	13.065	13.232	13.425	13.615	12.126	12.773	13.518	14.243
Taxable retail sales (bils. $)	78.453	79.250	79.981	81.127	82.263	72.717	77.554	81.694	86.103
Retail trade	34.650	35.044	35.308	35.729	36.194	32.702	34.408	35.974	37.794
Other taxable sales	43.803	44.207	44.673	45.398	46.068	40.015	43.146	45.721	48.309
Annual growth (% change)									
Retail sales	6.0	0.8	3.9	5.1	4.6	5.7	5.1	4.3	4.6
Taxable retail sales	6.1	4.1	3.7	5.7	5.6	7.7	6.7	5.3	5.4

Quarterly data are seasonally adjusted and expressed on an annual basis.

Construction and Real Estate

Buy-rent revisited.

In December 2009, after home prices had plummeted 20 percent, we wondered whether it was a good time to buy a house. A buy-rent analysis, taking into account mortgage and rental payments, other housing costs, investment opportunities, and tax consequences, indicated that anyone staying more than seven years in a dwelling should buy a home.

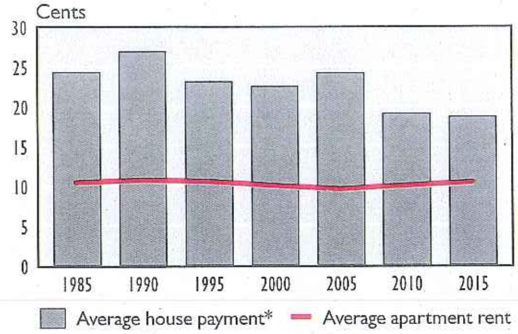
A review of that buy-rent analysis shows that we overestimated future home prices, underestimated apartment rents, and greatly underestimated the return on alternative investments, as the S&P 500 has doubled since the recession. This meant that homebuyers in 2009 would have fared better by renting an apartment and putting the down payment and savings in monthly housing costs into stocks.

We repeat the buy-rent analysis here to answer a related question: why has the residential real estate market been slow to recover? Despite recent rent hikes, the cost of living in an apartment has not changed much over the years. Today, the average monthly outlay for rent and related costs is $1,264 or 10.5 percent of average monthly personal income per household ($12,000). This share is exactly the same as it was in 1985.

Based on an average-priced home ($416,600) and a 4.0 percent mortgage rate, the current monthly outlay for new homeowners (interest and principal payments, property taxes, other costs, and tax savings) is $2,257 or 18.7 percent of household income. This is the lowest share of income in thirty years and well below the 24.3 percent share in 1985. Based on monthly outlays relative to household income, the buy-rent ratio 1.8 (=18.7/10.5) in 2015 versus 2.3 (=24.3/10.5) in 1985 clearly favors buying over renting today.

So, what is holding back the home-buying market? One answer is the 15 percent down payment—$62,500 on a $416,600 home—required to purchase a house. This amounts to 43.2 percent of today's annual household income ($144,600). Thirty years ago, the standard 10 percent down payment constituted only 20.9 percent of income. The upshot: now is an excellent time to buy a house if you have a lot of spare cash.

Puget Sound House Payment and Apartment Rent
Per Dollar of Average Household Income



*First-year payment (principal, interest, taxes, insurance, and maintenance less tax savings).

PUGET SOUND CONSTRUCTION AND REAL ESTATE

	2014		2015			Years			
	3	4	1	2	3	2013	2014	2015	2016
Housing permits (thous.)	23.6	23.0	20.3	19.4	19.8	18.8	22.0	19.9	21.1
Single-family	9.0	9.5	9.6	9.5	10.0	9.1	8.9	9.9	10.3
Multi-family	14.7	13.5	10.7	9.9	9.9	9.7	13.1	10.1	10.8
Housing permits (mils. $)	4620.6	4960.5	4528.2	4410.4	4593.6	3867.4	4398.0	4578.8	5046.7
Single-family	2758.4	2971.3	2966.9	2941.9	3112.9	2586.1	2686.1	3077.1	3342.3
Multi-family	1862.2	1989.2	1561.4	1468.5	1480.7	1281.4	1711.9	1501.6	1704.4
Average home price (thous. $)	396.8	406.5	407.8	414.2	419.8	364.3	395.0	416.6	431.6
Active home listings (thous.)	13.0	11.8	12.0	12.2	12.6	11.5	12.3	12.5	13.7
Home sales (thous.)	60.5	60.9	62.0	64.5	64.0	58.1	58.4	63.5	61.2
Apartment vacancy rate (%)	3.8	3.8	4.2	4.5	4.8	3.9	3.7	4.6	5.2
Average apartment rent ($)	1213	1223	1223	1235	1245	1108	1195	1239	1266
Annual growth (% change)									
Housing permits (mils. $)	29.5	29.4	-34.9	-10.4	16.6	12.3	13.7	4.1	10.2
Average home price	6.8	9.8	1.3	6.2	5.4	10.3	8.4	5.5	3.6
Average apartment rent	9.5	3.3	0.1	3.6	3.4	6.5	7.8	3.7	2.2

Quarterly data are seasonally adjusted and expressed on an annual basis.

Special Topic: Washington Tax Structure (3)

An argument for tax reform.

The state legislature is in a fiscal bind. Can it come up with billions of dollars for education and transportation without exacerbating Washington's notoriously regressive state and local tax system? The answer is no, not without major tax reform.

A study by this writer ("Washington State and Local Tax System: Dysfunction and Reform") compares our tax system with those of all other states and the District of Columbia. It focuses on five characteristics: fairness, adequacy, stability, transparency, and economic vitality. The findings indicate that Washington has the worst state and local tax system in the nation.

- *Fairness.* The Washington State Tax Structure Study Committee found that the state's lowest-income households paid 15.7 percent of their income on state and local taxes in 1999. The tax burden for the highest-income households was only 4.4 percent. This meant that the lowest-income households had to work 8.2 weeks out of the year to pay their tax bill, while the highest-income households had to work only 2.3 weeks. In 2013, the Institute on Taxation & Economic Policy concluded that our sales-based tax system was the most unfair in the nation.

- *Adequacy.* This is the ability of a tax system to generate sufficient revenue to meet the public needs of a growing economy. Nationally, the state and local effective tax rate (tax revenue as a percent of personal income) has averaged 10.6 percent and been quite stable for decades. In contrast, due to the heavy reliance on sales taxes, the Washington state and local effective tax rate fell from 11.4 percent (the twelfth highest in the nation) in FY 1995 to 9.4 percent (the thirty-seventh highest) in FY 2012. By taxing at a rate below the 10.6 percent national norm, Washington state and local governments have forfeited an estimated $28 billion in tax revenue since FY 2005, enough to pay—twice-over—for the new 520 bridge, the Alaska Way Viaduct replacement, and the Supreme Court's basic education mandate.

Characteristics of Tax Systems

	Washington Grade	Rank*
Fairness	F	51
Adequacy	F	50
Stability	F	47
Transparency	F	50
Economic vitality	No grade	--

*Rank among states.

- *Stability.* This refers to the stability of the effective tax rate over the course of economic cycles. Between FY 1995 and FY 2011, because of the inadequacy and volatility of the sales tax base, the Washington state and local effective tax rate was 4.6 times more unstable than the average effective tax rate for all states. Washington had the forty-seventh most stable tax system.

- *Transparency.* Every household and business should know how much it pays in taxes, a prerequisite for rational tax policy. Individual income taxes are totally transparent, since there is a record of payment. But sales taxes are only partially transparent, since few of us know our total sales tax burden at the end of the year. A transparency test encompassing five major taxes shows that without an income tax Washington has the second least transparent tax system in the nation.

- *Economic vitality.* The Tax Foundation ranks Washington as having the sixth best business tax climate in the nation. The presumption is that the lack of an income tax gives the state economy a competitive advantage. However, a statistical test shows that there is no correlation between the business tax climate of a state—namely, whether or not it has an income tax—and its ability to generate jobs. Although Washington and Oregon have fundamentally different tax systems—Washington has no income tax, while Oregon has an income tax but no sales or business and occupation tax—the two economies have performed equally well over time.

There is no good reason why Washington has to live with its dysfunctional state and local tax system. Indeed, if the state adopted a flat-rate personal income tax with a preferred rate of 10.6 percent, it could have the best—not the worst—tax system in the nation.

Consider the advantages. The single-rate tax would be fair, adequate, stable, and transparent and would have no adverse effect on economic vitality. With a 10.6 percent rate, there would be no need for a sales tax, a business and occupation tax (or corporate income tax), a property tax, or any other state and local tax.

There is a hitch, however, as the 10.6 percent rate means an increase in taxes, though not for everyone. Low-income households would pay less, middle-income households would pay about the same, and high-income households would pay more.

As for the state legislature, it could be adjourned by now.

FORECAST DETAIL 55 Percent Probability

	2014		2015			Years			
	3	4	1	2	3	2013	2014	2015	2016
Employment (thous.)	1935.8	1947.7	1960.4	1974.6	1984.4	1871.2	1927.6	1978.3	2015.9
Goods producing	291.2	295.2	296.5	298.0	298.4	284.2	291.3	297.9	299.8
Natural resources and mining	0.9	0.9	1.0	0.9	0.9	1.1	1.0	0.9	0.9
Construction	100.6	104.5	106.0	107.4	107.9	93.2	100.7	107.4	110.5
Manufacturing	189.8	189.8	189.6	189.7	189.6	190.0	189.5	189.6	188.4
Aerospace	89.8	88.5	88.1	87.8	87.6	92.9	89.9	87.7	86.5
Other durable goods	69.0	70.0	70.2	70.6	70.7	66.8	68.7	70.6	70.6
Nondurable goods	31.0	31.3	31.2	31.3	31.3	30.2	31.0	31.3	31.2
Services producing	1644.5	1652.5	1663.9	1676.5	1686.0	1587.0	1636.3	1680.4	1716.1
Wholesale and retail trade	290.9	293.4	295.2	297.0	298.0	278.1	289.1	297.3	302.1
Transportation and public utilities	64.2	63.6	63.9	64.3	64.5	62.1	63.9	64.3	64.9
Information	97.9	98.1	98.4	98.6	98.9	93.3	96.9	98.8	100.0
Financial activities	102.4	104.3	105.1	106.1	106.3	100.6	102.8	106.0	106.3
Professional and business services	266.5	267.0	271.3	276.2	280.1	254.9	263.9	277.8	291.2
Other services	527.6	530.7	533.4	536.6	539.3	508.2	526.0	537.9	549.4
Government	295.1	295.4	296.6	297.8	298.8	289.9	293.8	298.3	302.3
State and local	244.3	244.6	245.8	247.0	248.0	238.6	243.1	247.4	251.4
Federal	50.7	50.8	50.8	50.8	50.8	51.3	50.7	50.8	50.9
Unemployment rate (%)	5.0	5.1	5.1	4.9	4.9	6.0	5.3	4.9	4.8
Personal income (bils. $09)	204.4	207.5	209.2	211.5	213.4	196.4	203.4	212.3	219.3
Personal income (bils. $)	223.1	226.1	228.5	231.9	235.1	210.8	221.2	233.5	246.1
Wage and salary disbursements	128.2	129.5	131.3	133.0	134.6	120.8	127.5	133.8	140.4
Other income	94.9	96.6	97.2	98.8	100.5	90.0	93.8	99.7	105.7
Per capita personal income ($)	57292	57872	58310	58981	59620	55022	56926	59294	61767
Consumer price index (82-84=1.000)	2.472	2.465	2.452	2.465	2.479	2.416	2.459	2.472	2.530
Housing permits (thous.)	23.6	23.0	20.3	19.4	19.8	18.8	22.0	19.9	21.1
Population (thous.)	3893.2	3906.5	3918.3	3931.2	3943.8	3831.3	3886.3	3937.3	3983.5
Net migration (thous.)	28.2	28.2	22.4	26.6	25.4	29.0	28.6	24.4	18.4
Three-month treasury bill rate (%)	0.0	0.0	0.0	0.2	0.4	0.1	0.0	0.3	1.5
Conventional mortgage rate (%)	4.1	4.0	3.6	3.9	4.2	4.0	4.2	4.0	4.9
Annual growth (% change)									
Employment	3.4	2.5	2.6	2.9	2.0	2.8	3.0	2.6	1.9
Personal income (cur. $)	6.1	5.4	4.2	5.9	5.6	2.6	4.9	5.5	5.4
Consumer price index	0.1	-1.2	-2.0	2.0	2.3	1.3	1.8	0.6	2.3
Housing permits	15.7	-10.8	-47.9	-16.6	8.9	8.9	17.1	-9.4	6.0
Population	1.4	1.4	1.2	1.3	1.3	1.4	1.4	1.3	1.2

Quarterly data are seasonally adjusted and expressed on an annual basis.

Leading Index

Onward.

The Puget Sound economy has made significant strides in its recovery from the Great Recession. It is not as if the housing and financial crisis has been forgotten. Indeed, some of the effects, such as the slack in labor force participation rates, may be permanent. But in the wake of the recession, the Puget Sound economy has added 206,000 jobs (more than one and one-half times the number lost during the downturn), the unemployment rate has dropped from 9.7 percent to 5.1 percent, and personal income has rebounded 29 percent. This is a bona fide recovery.

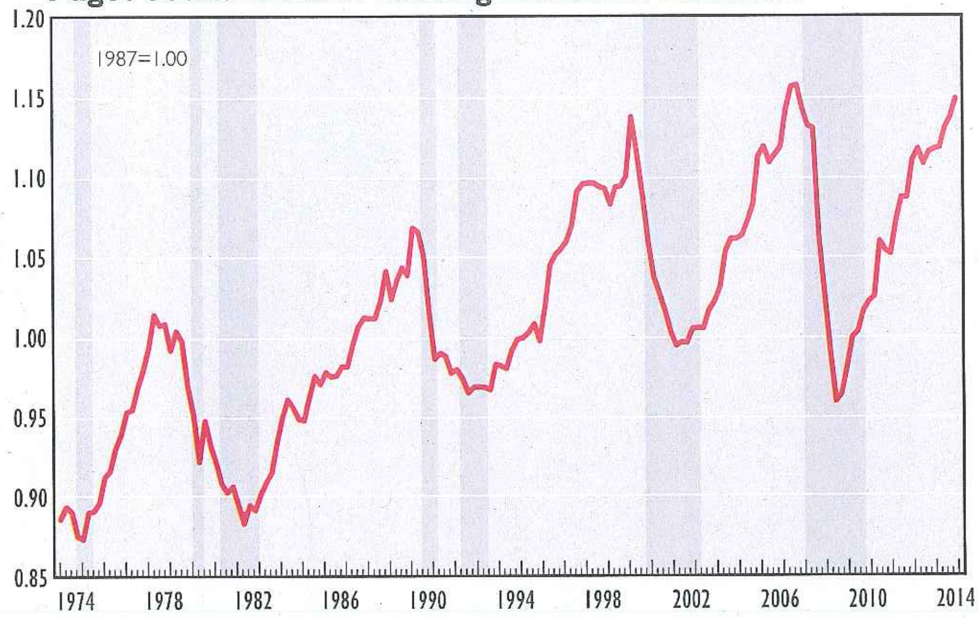
The upturn has now run 19 quarters and employment has climbed 12 percent. In terms of length and relative job growth, the current expansion exactly matches the rebound in the mid-2000s that led up to the Great Recession. Is the economy now living on borrowed time? The answer is probably no.

Forty-five years of history clearly show that the recovery phases of business cycles do not have a fixed life expectancy. While Puget Sound expansions have averaged 20 quarters, they have ranged from 11 quarters in the early 1970s to 31 quarters in the 1980s.

According to the latest reading of the Puget Sound leading index, the current upturn still has a ways to go. The leading index rose 1.0 percent in the fourth quarter of 2014. It was supported by improvement in four of seven components (manufacturing hours, help-wanted ads, new filings for unemployment compensation, and real durable goods spending). Three components (housing permits, the interest rate spread, and the Boeing backlog delivery ratio) worsened, but their impact was minimal.

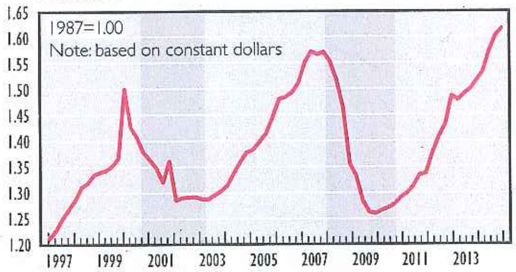
Absent a significant downward break in the leading index, there is no reason to think that the expansion will soon run out of steam. Over the next four quarters, our forecast calls for 46,000 new jobs (a 2.4 percent increase), a further decline in the unemployment rate to 4.8 percent, and 5.4 percent growth in personal income.

Puget Sound Index of Leading Economic Indicators



Shaded areas show recessions or periods of economic stagnation.

Change in Puget Sound Retail Sales of Durable Goods



Washington Manufacturing Hours

The Puget Sound Economic Forecaster (ISSN 1520-7250) is published four times a year. A one-year subscription to the newsletter is $395. A one-year subscription to the newsletter and web site is $695. For additional information, please visit **www.economicforecaster.com**. You may also contact **Dick Conway or Doug Pedersen at Conway Pedersen Economics, Inc., P. O. Box 2241, Seattle, WA 98111-2241. Telephone (206) 329-1707.**

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