

ECONOMIC REPORT

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Winter 2010

787's in the air, tax the tanners, but not the botoxers, Newport, Bellingham, or Seattle? The Year of the Tiger, BSU Broncos triumph, Skaters to Spokane, Light rail to Sea-Tac, FTC goes after Oregon's largest private employer, Runways cleared of record snow as leaders return from Copenhagen. A New Decade gets underway.

THE NATION:

The end of 2009 was a more upbeat experience than the end of 2008, when fear stalked the land amidst collapsing financial markets, plummeting employment, and policy makers in overdrive and uncharted territory. As 2009 ended, output was once again rising with a 2.2 percent annual growth rate in the third quarter, and there were signs of an approaching end to the decline in employment. Net worth has been rising for two consecutive quarters, albeit well below previous peaks and financial markets are looking a bit more normal. The full array of fiscal and monetary tools (even some we did not know about) has been used to mitigate the downturn. Now the question is whether the economy will transition to growth based on things other than cash for clunkers, homebuyer credits, and stimulus plans. The coming year will be better than 2009 with growth returning to near three percent, inflation near 2

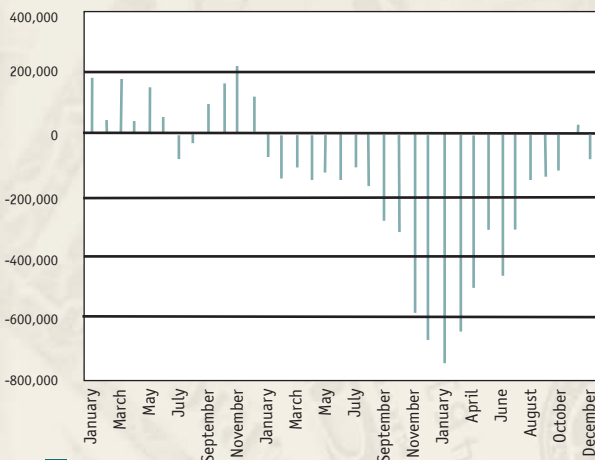
percent and a slow increase in short term rates as the monetary authority unwinds its accommodation. You cannot keep zero interest rate targets without serious long term consequences. There are lots of assumptions - that business investment will increase, that the global economic rebound will continue and that the housing drag will keep diminishing, amongst others. Huge issues confront us: How will a new medical system work? Can we unwind the monetary stimulus before inflation rises? Can we shrink trillion dollar deficits financed by uneasy savers and central banks around the world fast enough? The decade and the recession might be over, but the excitement is not.

THE REGION:

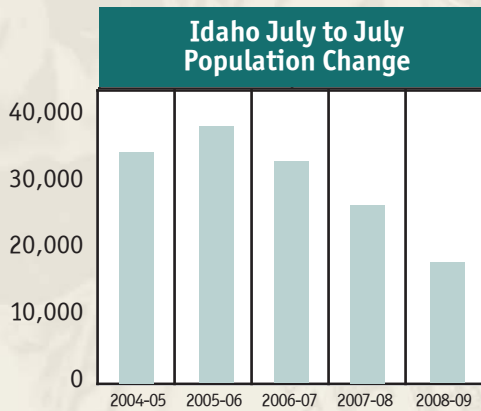
Personal income rose .3 percent between the second and third quarters of 2009 according to the Bureau of Economic Analysis. Within the region, personal income increased by .6 percent in Washington, .5 percent in Oregon and .2 percent in Idaho. Montana income was unchanged. All the states had increases in net earnings, but Washington and Idaho has no change in dividends, interest and rents. Washington, Oregon and Idaho had increases in transfer payments while Montana had a decline in transfer payments as well as dividends, interest and rents. Alaska, New Jersey, New York and Washington had the highest income growth rates.

The Census Bureau released its population estimates for July 1, 2009 showing a .9 percent or 2.63 million increase in the US population to 307,006,550. Washington lead the region with a 1.5 percent or 98,122 person increase, followed by Idaho at 1.2 percent or 18,295 residents and Oregon at 1.1 percent or 42,666 people. The estimated Montana increase was .7 percent or 6,954 people. Oregon, Idaho and Montana saw slower population growth than the previous year while Washington defied the regional pattern. The problems in the housing and labor market throttled back migration and interrupted some of the long lasting flows to the south and west. Previous magnets like Nevada and Florida lost population to the rest of the nation. Hiccup or pattern change?

Monthly Change Payroll Employment January 2007 to December 2009 (-7.2 Million Since December 2007)



Looking ahead, all four states will be in the process of transitioning from decline to recovery and then expansion in 2011-2013 as the recession job losses are made up. The employment and income news will improve, diminishing some of the fiscal issues and ending the torrent of negative news. Trade and investment are increasing and the housing decline has seemingly ended. The dramatic declines, particularly in Oregon and Idaho, will take years to make up.



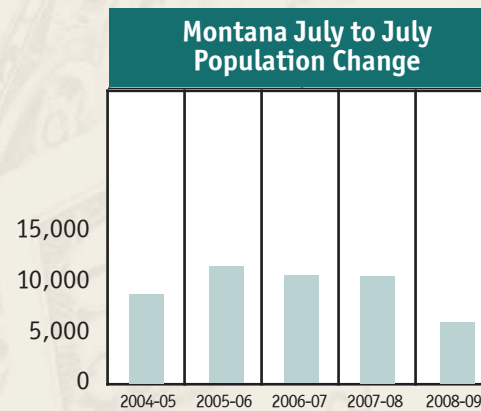
Source: Census Bureau

IDAHO:

Idaho wage and salary employment fell by 5.2 percent or 33,200 jobs over the year to November. The seasonally adjusted unemployment rate was 9.1 percent up slightly from 9 percent in October. This is the highest rate that the state has seen since the early 1980s when the rate reached 9.4 percent, according to the Department of Labor. As in the nation, the rate of decline is easing and the October to November job decline was less than that seen over the last five years. Hopefully these glimmers will turn to job growth in 2010. The wage and salary employment data displayed the common pattern of increases in education and health services and annual declines elsewhere.

Southwestern Idaho has had a long run of relatively strong performance since the mid-1970s with the exception of the serious recession in the early 1980s. Thus it was notable, that the Metropolitan Policy Program at the Brookings Institution in their Mountain Monitor declared Phoenix, Boise and Las Vegas to be three of the most troubled metropolitan areas in the nation in the third quarter of 2009. The performance assessment was based on changes in employment, the unemployment rate, estimates of Gross Metropolitan Product and real house prices. Residential real estate markets are correcting with minimal new construction and increased affordability. The continuation of the national recovery with a resumption of business investment and population movement will be vital to restoration of strength in the metro area.

Idaho fall potato production was 13.1 billion pounds up 12.5 percent from 2008 production. The gain came from an increase in acreage harvested from 304,000 to 319,000 and record yields of 411



Source: Census Bureau

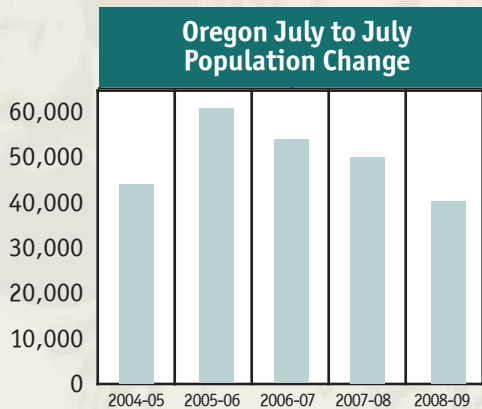
hundredweight per acre. Idaho accounted for one third of the nation's fall potato production. The November price report for the Department of Agriculture indicated that Idaho average prices were down 10.7 percent over the year. Washington was the second largest producer at 8.8 billion pounds followed by Colorado then Oregon.

MONTANA:

Montana unemployment rate continues to be the lowest in the region at 6.4 percent in November. Wage and salary employment was down 1.7 percent or 7,600 jobs over the year, continuing a pattern that has been in place since October of 2008. Annual increases were few with 300 jobs in government and 100 in education and health services. The declines were concentrated in construction down by 3,100 jobs, retail trade down by 2,100 jobs and food services where employment fell by 3,100 jobs. The Department of Labor and Industries reported that seasonally adjusted employment fell by 2,500 jobs between October and November taking the total to 436,500.

Montana has, according to the Energy Information Agency, about 5.2 percent of US coal reserves: a portion of which are under school trust lands. Coal has become a controversial energy source amidst the climate change issue and the state's renewable energy mandate. On December 21, 2009 the State Land Board voted 4-1 to lease lands containing about 572 million tons of coal in the Otter Creek Valley southeast of Billings. State revenues from royalties and the upfront bonus bids go towards schools with the potential to increase total funding. This Montana issue is a microcosm of the choices that will have to be made but are non-issues for states that lack significant fossil fuel energy resources.

The forest products industry in the region has been severely impacted by the construction collapse, but related sectors such as the production of paper products and packaging have also been impacted. Smurfit-Stone Container, operating in bankruptcy, announced that its mill in Frenchtown, Montana, near Missoula, would be closed at the end of 2009. The mill had over 400 employees with an average wage level of \$70,000. Another high profile packaging mill in the region in Millersburg, Oregon operated by International Paper and employing 270 closed in mid-December. Hopefully the rebound in activity will end the litany of closures in the forest products related sectors.



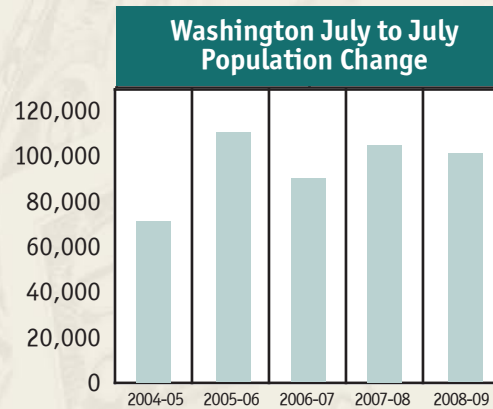
Source: Census Bureau

OREGON:

Oregon continued to shed employment in November with an adjusted decline of 4,600 jobs, according to the Employment Department. The unemployment rate was 11.1 percent, down slightly from the 11.2 percent in October. The year over year job decline was 5.1 percent or 88,200 jobs. As has been the case in recent months the only major sector with annual increases was education and health services that includes private education and health services employment. A large decline in federal government employment was related to initial work for the 2010 Census being completed. Local government employment was down over the year, while state employment rose.

The Shepherds Flat Wind Farm, which for a while will be the world's largest, is under construction on over 30 square miles of eastern Oregon, near Arlington. In December, it was announced that General Electric would be the supplier of 338 turbines to the project. The \$2 billion project is owned by Caithness Energy and will supply power to Southern California Energy. Southern Idaho is also experiencing increased interest in wind projects with construction underway near Hagerman. Windland is planning a 100 turbine project near Burley with construction possible in 2010.

According to the Census Bureau, residential permits in Oregon through November totaled 7,019 which is 40 percent below the corresponding figure for 2008 and 75.3 percent below the 2005 peak of 29,571 units. Single family permits fell by 31.4 percent or 2,386 over the year while residential units in buildings with 5 or more units dropped by 56.5 percent or 2,113 units. Minimal construction, falling prices, low rates, and tax incentives have increased Oregon's sales activity for three consecutive quarters according to the National Association of Realtors. Months of available inventory are trending down in many of the markets covered by the RMLS data.



Source: Census Bureau

WASHINGTON:

In November, Washington seasonally adjusted employment fell by 4,800 for the second consecutive month. In the first 11 months of 2009 only July showed an increase in employment. The November unemployment rate edged down from 9.3 to 9.2 percent and the year over year job decline was 4.3 percent or 128,600 jobs. Only one of the major sectors to increase was education and health services with a gain of 10,100 jobs. Construction, manufacturing and trade employment fell by 38,000 jobs, 27,700 jobs and 20,800 jobs respectively. Seattle employment was down 5.9 percent or by 87,000 jobs over the year while the Tri-Cities employment, benefiting from activities at the Hanford Reservation, rose 3.8 percent.

Forty seven states reported annual declines in revenue during the third quarter, according to the Census Bureau with revenues down 11 percent. The only states with increases were Nevada, New Hampshire and Rhode Island. Governors and legislatures are confronting ongoing fiscal shortfalls from previous plans. Washington is facing a \$2.6 billion difference between planned spending and revenues for the remainder of the biennium. The upcoming legislative session will sort out the conflicting priorities and policy mix of budget reductions and possible tax increases. Compatriots in Boise, Salem and Helena will be doing the same. Last year there were no general tax increases in Washington in filling a \$9 billion shortfall.

The Washington Center for Real Estate Research reported that the third quarter saw home resales up 2.6 percent from the same quarter of 2008 and 15.6 percent from the second quarter of 2009 at an adjusted annual rate. Median resale prices were down 7.7 percent over the year. A Center survey indicated that about half the sales were to buyers using the first time homebuyer credit. The Census Bureau reported that Washington permits through November were 15,395, down from 27,300 to November of 2008. The weakness was concentrated in multifamily with a 69.6 percent or 6,020 unit drop in projects with 5 or more residences (Think condo bust and rental market weakness) and single family which fell by 4,777 units. The correction is ongoing.