THE STATE OF THE ECONOMY

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Following a slow start to the year, the United States economy continued to improve as was expected. Gross domestic product has increased slightly, unemployment has continued to fall, interest rates remain low, and the price of oil has dropped significantly. Employment rose and even compensation increased slightly, while inflation continued to fall, largely attributed to the drop in energy prices. Overall, with the exception of the price of oil, the economy is behaving more or less in line with expectations.

THE WORLD ECONOMY

The International Monetary Fund's (IMF) most recent update reports that the global economy continues to grow, with moderate growth expectations of 3.5 and 3.7 percent for 2015 and 2016. While the growth should receive a boost by the drop in oil prices, other negative factors such as investment weakness in advanced and emerging economies offsets some of the advantage, with several developments influencing the outlook.

First of all, in looking at the significant decline in oil prices, a 55 percent drop since September, the IMF reports the cause being unexpected demand weakness in

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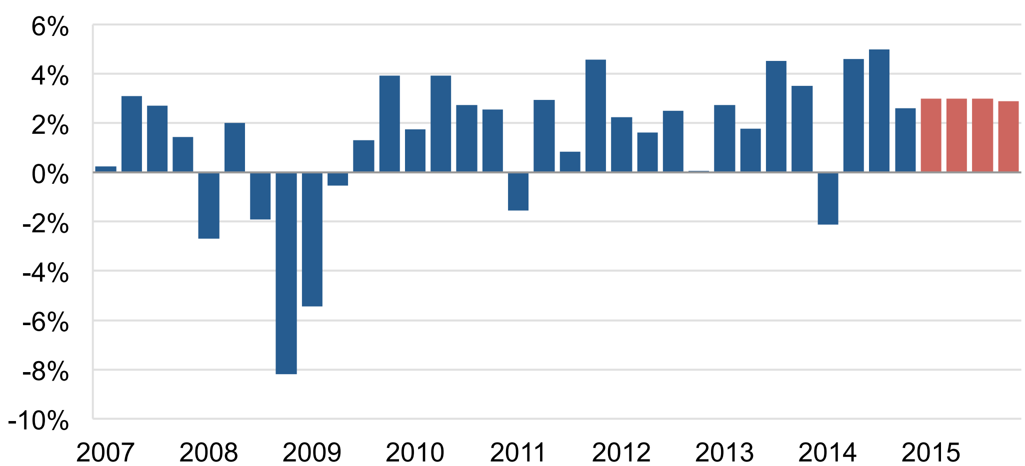
major economies, and an over-supply of production that will take time to correct. Secondly, there was a stronger recovery in the United States than expected, while all other major economies fell short in their economic performance, most likely due to diminished expectations regarding medium-term growth prospects. In looking at currencies, the U.S. dollar has strengthened 6 percent, while the euro and the yen have depreciated 2 and 8 percent respectively, showing the growth discrepancy across major economies. And lastly, interest rates and risk spreads have risen in many emerging market economies.

In general, there is increased uncertainty regarding the influence of oil prices on projected growth, and could either help or hinder growth, depending on how fast supply responds to the drop in demand. Additionally, if there are further declines in inflation, monetary policy must accommodate through other means to prevent real interest rates from rising.

THE UNITED STATES ECONOMY

The end of 2014 brought a GDP of 2.6 percent (Figure 1), lower than the previous 2 quarters, but not far outside of expectation. As noted by the IMF, the United States is the only major economy for which growth projections have been raised, and Wall Street Journal's survey of economists forecasts GDP growth of 3 percent across the four quarters of 2015.

Figure 1: Gross Domestic Product, United States, Annualized Percent Change, 2007–2015

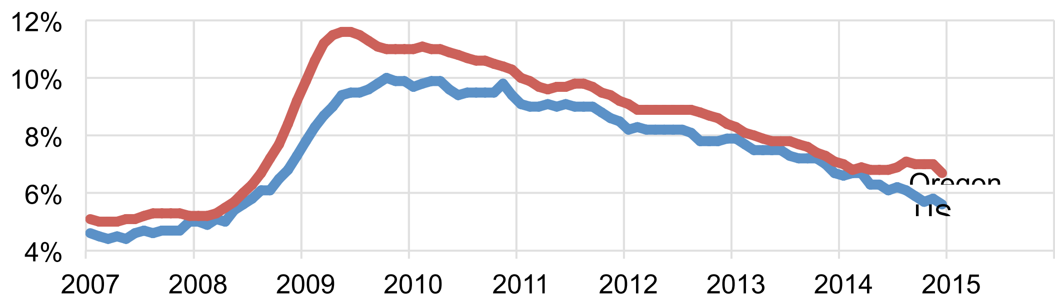


Source: Bureau of Economic Analysis and Wall Street Journal Economic Forecasting Survey

Unemployment went to a new low of 5.6 percent since the middle of 2008 (

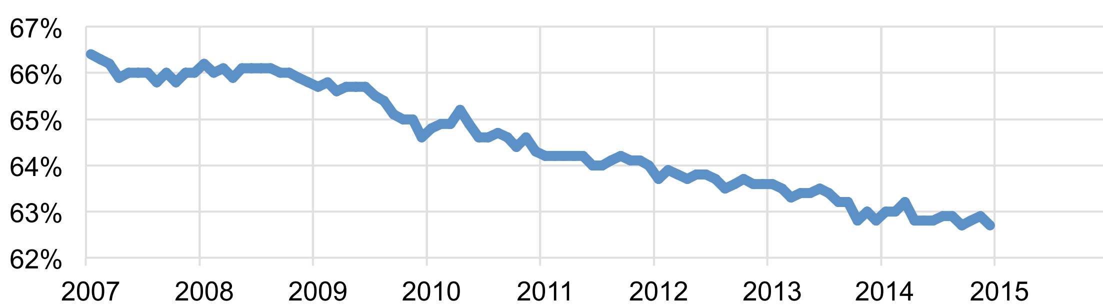
Figure **2**), and is expected to remain low provided there are no major changes in the labor force participation rate, which has continued to remain relatively low (Figure 3). According to the Bureau of Labor Statistics, nonfarm payroll employment rose by 252,000 jobs in December, with most job gains in professional and business services, construction, food services and drinking places, health care and manufacturing. Along with the increase in jobs, compensation rose 2.2 percent over the year, with benefits rising 2.6 percent.

Figure 2: Unemployment Rate, Oregon and United States, 2007-2015



Source: Bureau of Labor Statistics

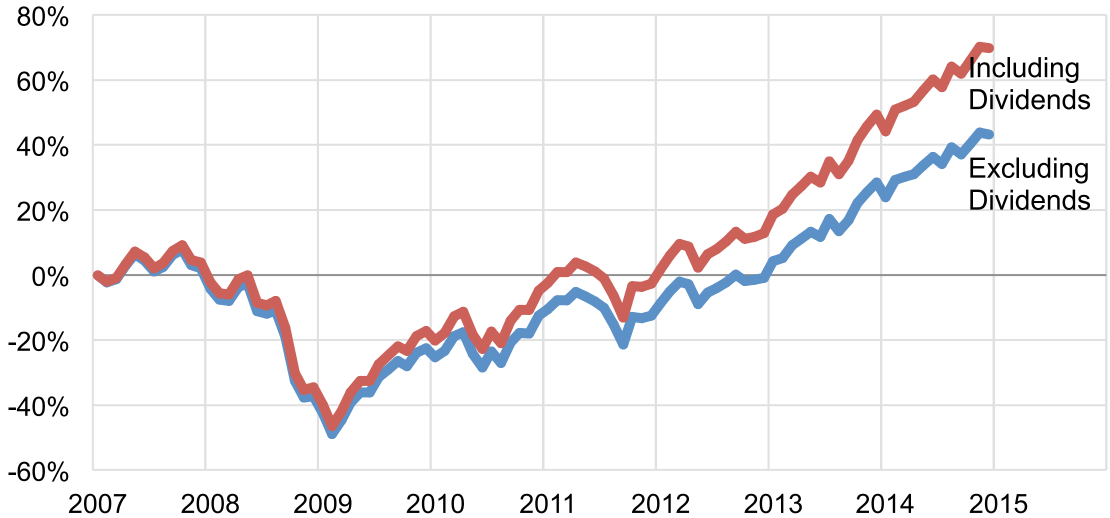
Figure 3: Labor Force Participation Rate, United States



Source: Bureau of Labor Statistics

Inflation declined 0.4 percent in December, yielding a total 12 month rate of 0.8 percent since the previous December. This is markedly lower than November's 1.3 percent change over its previous 12 months. The Bureau of Labor Statistics further notes that the energy index contributes a 10.6 percent drop over the 12 months, while the food index has increased by 3.4 percent. Kathleen Madigan writes in the Washington Street Journal that because of the cheaper oil, several economists say that inflation may turn to deflation temporarily, but this should be short-lived.

Figure 4: Standard & Poor's 500 Index, 2007–2014



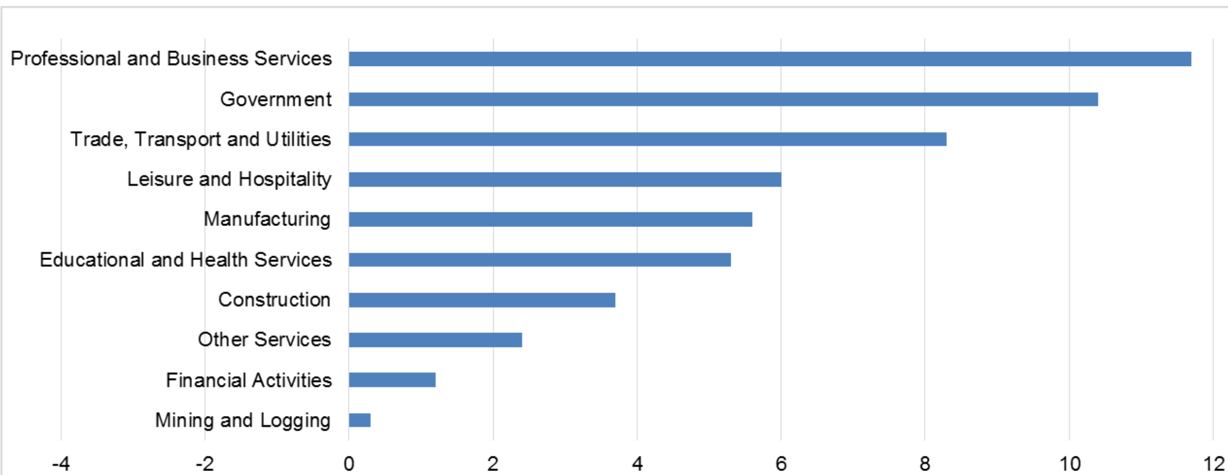
Source: S&P Dow Jones Indices, McGraw Hill Financial

The U.S. Stock Market finished strong in 2014 (Figure 4), with a gain of total annual gain of 11 percent for the S&P 500 Index. The best performing sectors were utilities, health care and technology, and with the amount of cash available to companies, there were also significant mergers and acquisitions. Thomson Reuters reports that the 2014 global M&A was up to $3.1 trillion, 52 percent higher than the previous year.

OREGON AND THE PORTLAND AREA

The state of Oregon has continued to show signs of growth, with most major economies experiencing above average growth in November. Figure 5 shows that most new jobs are in professional and business services, government, and trade, transport and utilities, with a total December increase in 8,200 jobs. The Oregon Office of Economic Analysis notes that the state's job growth advantage has returned when comparing year-over-year change to the national job growth. However, the state's economists indicate that it is the high-wage and low-wage jobs that have seen the most growth from 2010-2013, with a lack of growth in middle-wage jobs. Oregon's unemployment rate also decreased to 6.7 percent as of December, after hovering between 6.8 and 7.0 throughout 2014.

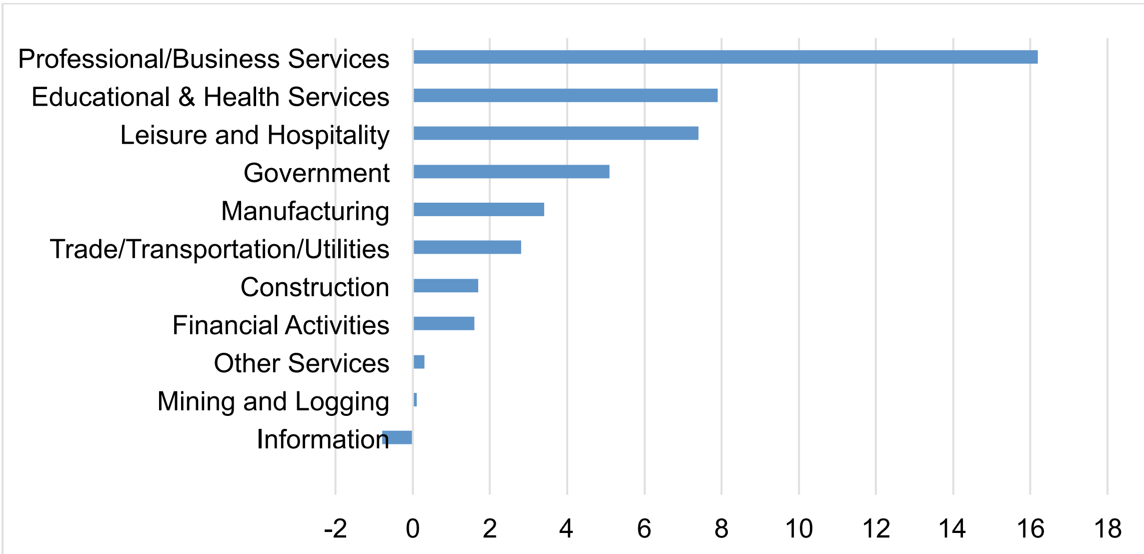
Figure 5: Oregon Job Growth over last 12 months, Nonfarm Payroll Employment, Seasonally Adjusted (1,000's)



Source: Oregon Employment Department

As of November, the Portland-Vancouver-Hillsboro MSA showed 12-month job growth of 2.7 percent, 60 basis points higher than the national growth rate. The sectors with the highest growth rate in the last 12 months (Figure 6) are Professional and Business Services (+16,200), Educational & Health Services (+7,900), and Leisure and Hospitality (+7,400), with Government and Manufacturing falling close behind (+5,100 and +3,400 jobs respectively).

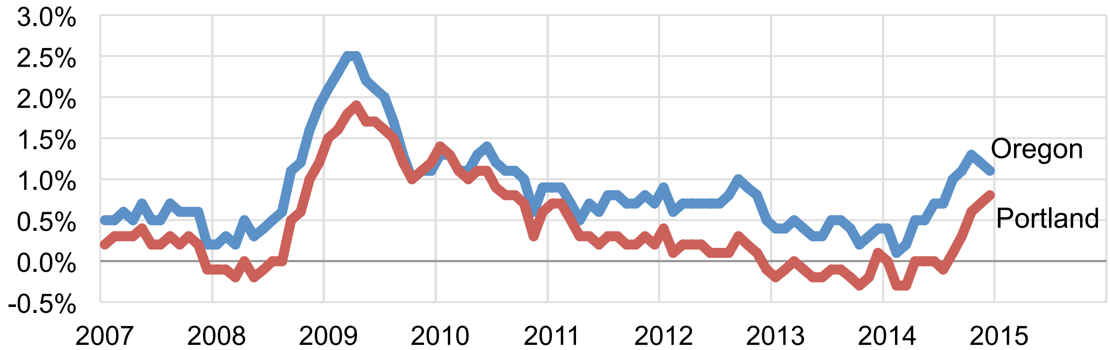
Figure 6: Portland-Vancouver-Hillsboro MSA, Nonfarm Payroll Employment Growth in Last Year, Not Seasonally Adjusted (1,000's)



Source: Oregon Employment Department

Portland's unemployment rate has continued to increase slightly over the fourth quarter, finishing 2014 at 6.4 percent, similar to the first and second quarter to 2014. As in-migration remains strong, this upward pressure is not surprising, although as Figure 7 illustrates, the unemployment rate is still below the state, but above the national average.

Figure 7: Unemployment Rate, Oregon and Portland Metropolitan Area vs. United States



Source: Bureau of Labor Statistics and Oregon Employment Department

Unemployment is lowest in Tualatin (5.0 percent) and highest in Forest Grove (6.5 percent) with a growth in labor force in Washington and Multnomah Counties of 3.3 and 3.2 percent respectively.

CONCLUSION

Overall, the national and local economy continues to grow at a steady, albeit slightly lower rate. GDP is expected to increase consistently over the coming year, interest rates should rise marginally, and there should be steady unemployment. ■