THE STATE OF THE ECONOMY

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The United States economy in the fourth quarter of 2013 appears to have a more robust foothold pointing to a healthier outlook for 2014. Much of the uptick is due to a pickup in personal consumption expenditures. One weak spot in the fourth quarter was related to government spending, dragged down by the Federal government shutdown that lasted nearly three weeks at the start of the quarter.

With the unemployment rate decreasing and output increasing, the Federal Reserve has begun tapering back on its multibillion-dollar-a-month asset buying spree. Some economists note that much of the change in unemployment is because of reduced labor force participation—now at a 30 year low. With the addition of relatively low inflation, it is argued that that inflation should be higher before the Fed fully implements a tapering program. On the other hand, some argue that the Fed's $4 trillion buying program has created precarious bubbles in areas such as the emerging markets and commercial real estate and thus should wind down more quickly.

The Economist reports that households continue to be the mainstay of the recovery as they are making steady progress in reducing their over-indebtedness. The ratio of household debt to disposable income fell from 126 percent in 2007 to 100.6 percent in the third quarter of 2013, according to the Fed. A ratio of around 90-95 percent was more common before the recent boom.

■ Angela Guo is a Master of Real Estate Development candidate and has been awarded the Center for Real Estate Fellowship. Any errors or omissions are the author's responsibility. Any opinions expressed are those of the author solely and do not represent the opinions of any other person or entity.

THE WORLD AND U.S. ECONOMY

The International Monetary Fund (IMF) anticipates an overall strengthening of the world economy, with output growth of 3.7 percent in 2014 and 3.9 percent in 2015. The IMF reports that China's growth will decelerate slightly from 7.5 percent in 2014 to 7.3 percent in 2015. (Figure 2)

Figure 2: IMF World Growth Projections, January 2014

			Projections		**Difference from Oct '13 WEO Projections**	
	2012	2013	2014	2015	2014	2015
World Output	3.1	3.0	3.7	3.9	0.1	0.0
Advanced Economies	1.4	1.3	2.2	2.3	0.2	-0.2
United States	2.8	1.9	2.8	3.0	0.2	-0.4
Euro Area	-0.7	-0.4	1.0	1.4	0.1	0.1
Germany	0.9	0.5	1.6	1.4	0.2	0.1
France	0.0	0.2	0.9	1.5	0.0	0.0
Italy	-2.5	-1.8	0.6	1.1	-0.1	0.1
Spain	-1.6	-1.2	0.6	0.8	0.4	0.3
Japan	1.4	1.7	1.7	1.0	0.4	-0.2
United Kingdom	0.3	1.7	2.4	2.2	0.6	0.2
Canada	1.7	1.7	2.2	2.4	0.1	-0.1
Other Advanced Economies	1.9	2.2	3.0	3.2	-0.1	-0.1
Emerging and Developing Economies	4.9	4.7	5.1	5.4	0.0	0.1
Central and Eastern Europe	1.4	2.5	2.8	3.1	0.1	-0.2
Commonwealth of Independent States	3.4	2.1	2.6	3.1	-0.8	-0.7
Russia	3.4	1.5	2.0	2.5	-1.0	-1.0
Excluding Russia	3.3	3.5	4.0	4.3	-0.1	-0.1
Developing Asia	6.4	6.5	6.7	6.8	0.2	0.2
China	7.7	7.7	7.5	7.3	0.3	0.2
India	3.2	4.4	5.4	6.4	0.2	0.1
Latin America and the Caribbean	3.0	2.6	3.0	3.3	-0.1	-0.2
Brazil	1.0	2.3	2.3	2.8	-0.2	-0.4
Mexico	3.7	1.2	3.0	3.5	0.0	0.0
Middle East, North Africa,						
Sub-Saharan Africa	4.8	5.1	6.1	5.8	0.1	0.1
South Africa	2.5	1.8	2.8	3.3	-0.1	0.0

Source: International Monetary Fund, World Economic Outlook, January 2014

While the world began to recover from the global economic crisis, emerging markets had seen their economies eclipsing recoveries in the U.S., Europe, and Japan. However, with the Fed tapering of its easy money program, the rising U.S. interest rates will likely draw investor cash from around the globe in search of higher returns. Thus, as the continued demand for investments in advanced countries increases, the IMF warns that emerging economies could struggle with the climbing U.S. interest rates, a shift that could lead capital to exit developing countries.

As the global market continues to rebalance, the IMF reports that the United States leads the recovery of the world economy. The U.S. economic recovery accelerated in the second half of 2013 as consumer spending, business investment and net exports all posted strong gains. The U.S. economy grew at an annual rate of 4.1 percent between July and September, an upward revision from the previous estimate of 3.6 percent, and the fastest pace since 2011. Most economic indicators in November and December were also strong, suggesting a relatively robust fourth quarter.

Figure 3: United States Annual Economic Growth, Actual and Forecast, 2013–2018

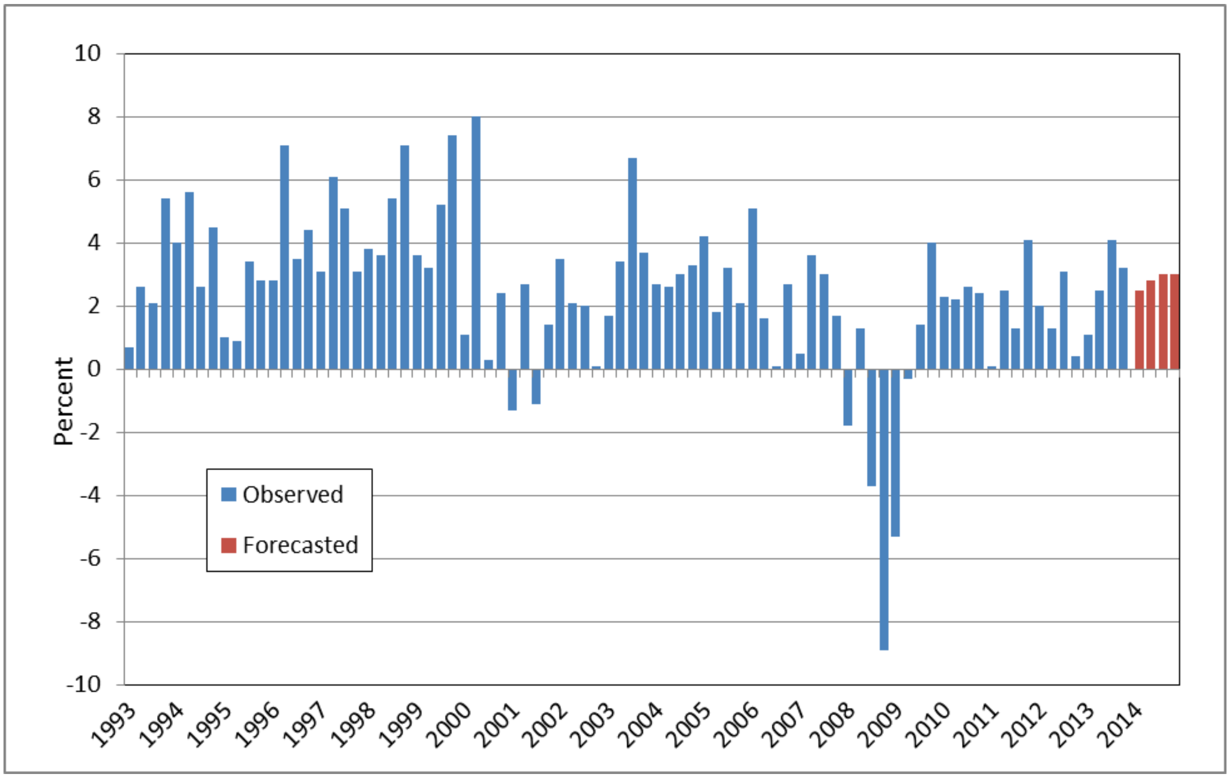
%	2013	2014	2015	2016	2017	2018
GDP	1.9	2.6	2.4	2.5	2.4	2.6
Private consumption	2.1	2.4	2.2	2.3	2.4	2.0
Government consumption	-2.0	0.1	0.2	0.2	0.2	0.4
Gross fixed investment	5.3	8.0	6.5	6.5	6.4	6.8
Exports of goods & services	2.4	3.1	3.5	3.8	3.7	4.1
Imports of goods & services	1.6	3.6	3.9	4.5	5.4	4.2
Domestic demand	1.8	2.7	2.5	2.6	2.7	2.6
Agriculture	2.1	2.0	2.5	2.9	2.9	2.9
Industry	2.5	2.8	3.0	2.5	2.4	2.4
Services	1.8	2.6	2.3	2.5	2.4	2.6

Source: Economist Intelligence Unit, January 2014

In 2013, GDP grew from 1.1 percent in the first quarter, 1.7 percent in the second quarter, 4.1 percent in the third quarter and 3.2 percent in the fourth, the U.S. Bureau of Economic Analysis (BEA) reports. The BEA reports that the increase in real GDP in the fourth quarter primarily reflected positive contributions from personal consumption expenditures (PCE), exports, nonresidential fixed investment, private inventory investment, and state and local government spending that were partly offset by negative contributions from federal government spending and residential fixed investment. Imports, which are a subtraction in the calculation of GDP, increased.

The Economist Intelligence Unit forecasts that real GDP will have a growth of 2.6 percent in 2014, before a gradual monetary tightening that will slow the rate slightly to around 2.5 percent in 2015-18.

Figure 4: Gross domestic product, Annualized Percent Change, 1993–2014

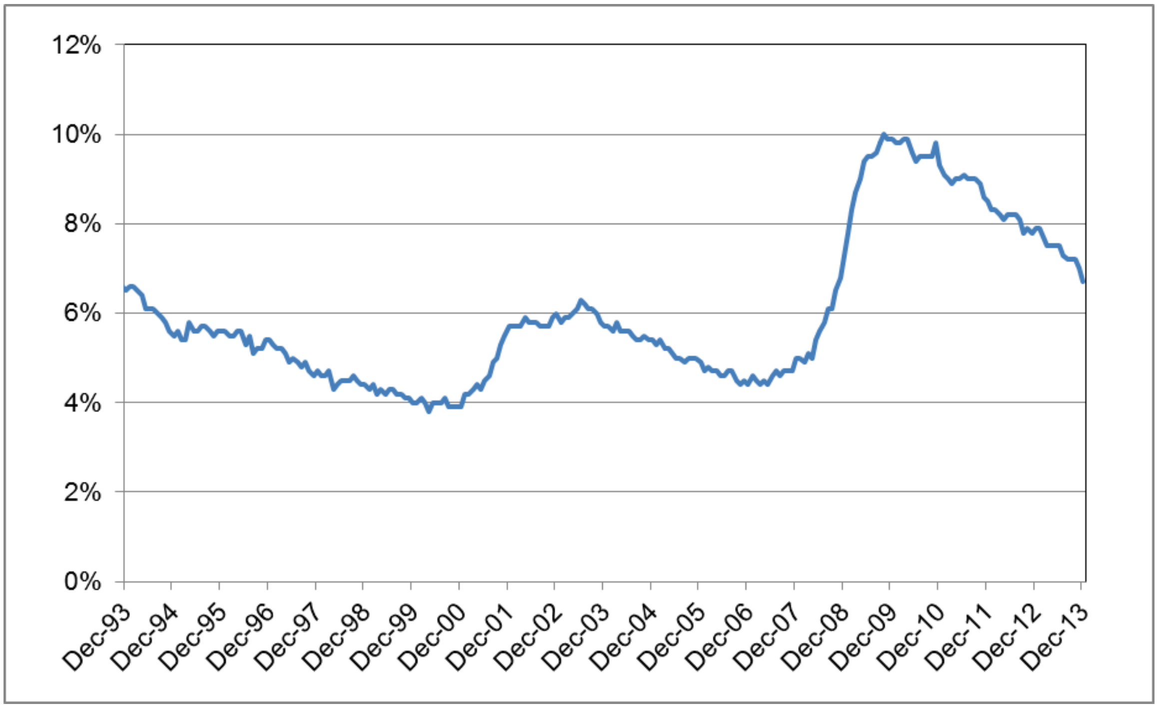


Source: Bureau of Economic Analysis and Wall Street Journal Economic Forecasting Survey

U.S. employment increased modestly in the fourth quarter. The quarter began strong with employment gains of 237,000 in October and 274,000 in November. A week report of 75,000 net new jobs in December was weaker than expected and dragged down the quarterly average. Industry sectors that reported the most growth in December were:

- Retail Trade (+55,000); retail trade added an average of 32,000 jobs per month in 2013,
- Professional and business services (+19,000); employment growth in this industry averaged 40,000 per month in 2013, and,
- Wholesale trade (+15,000); added an average of 8,000 jobs per month in 2013.

Figure 5: Unemployment Rate, United States



Source: Bureau of Labor Statistics

The U.S. created a total of around 2.3 million net new jobs during 2013. At this pace, full employment in the U.S. is remains several years away.

The U.S. unemployment figures are continuing to creep down, declining 0.5 percent since September 2013, to 6.7 percent in December 2013, according to the Bureau of Labor Statistics. The unemployment rate reached their lowest rates since late 2008. As seen in Figure 5, U.S. unemployment hovered between 4 percent and 6 percent from the mid-1990s until the recession that began in late 2008 when it spiked to 10 percent in October of 2009.

The jobs being created, however, are not the ones that were lost before the recession. While two-thirds of the jobs lost during the recession were middle-income jobs, about half of those created since have been low-wage sectors like tourism, hospitality and retail sales. Furthermore, while the decline in unemployment has been viewed as a sign of an improving economy, a portion of the decline in unemployment has been attributed to a decline in labor force participation. (Figure 6)

Some of the improvement in the unemployment rate is illusory. While employment is slowly improving, the recession has also caused millions to drop out of the labor force. While retiring Baby Boomers explain some of the drop in labor force participation rate, the recession exacerbated the decline.

Figure 6: Labor Force Participation Rate, United States

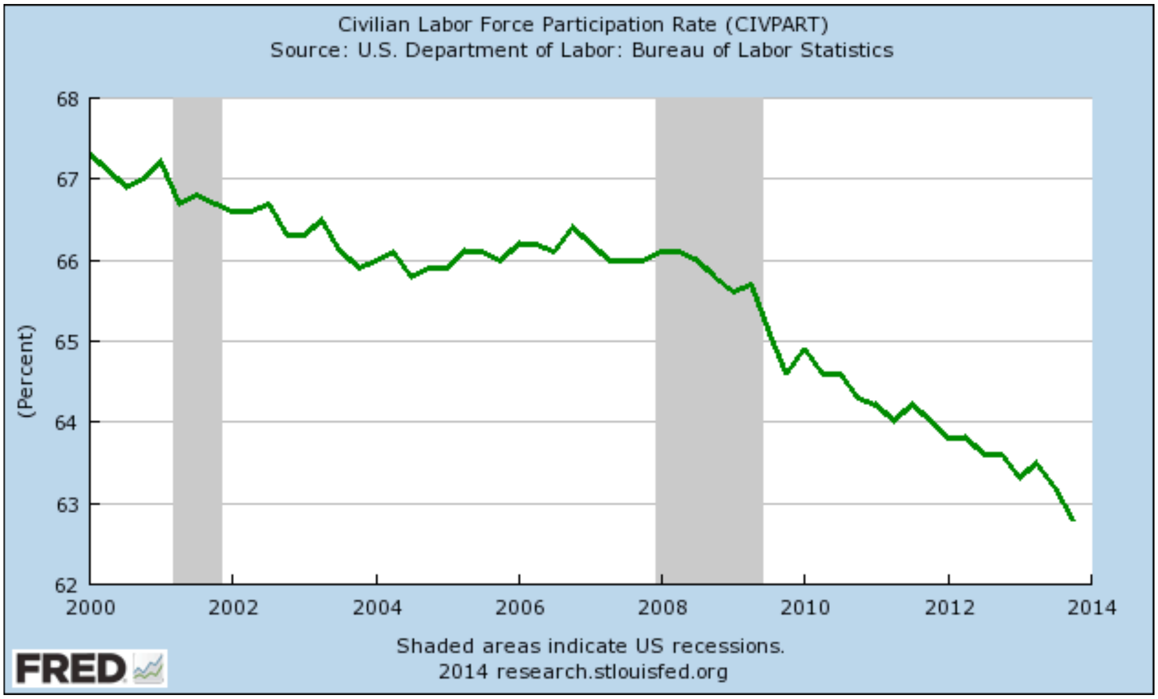
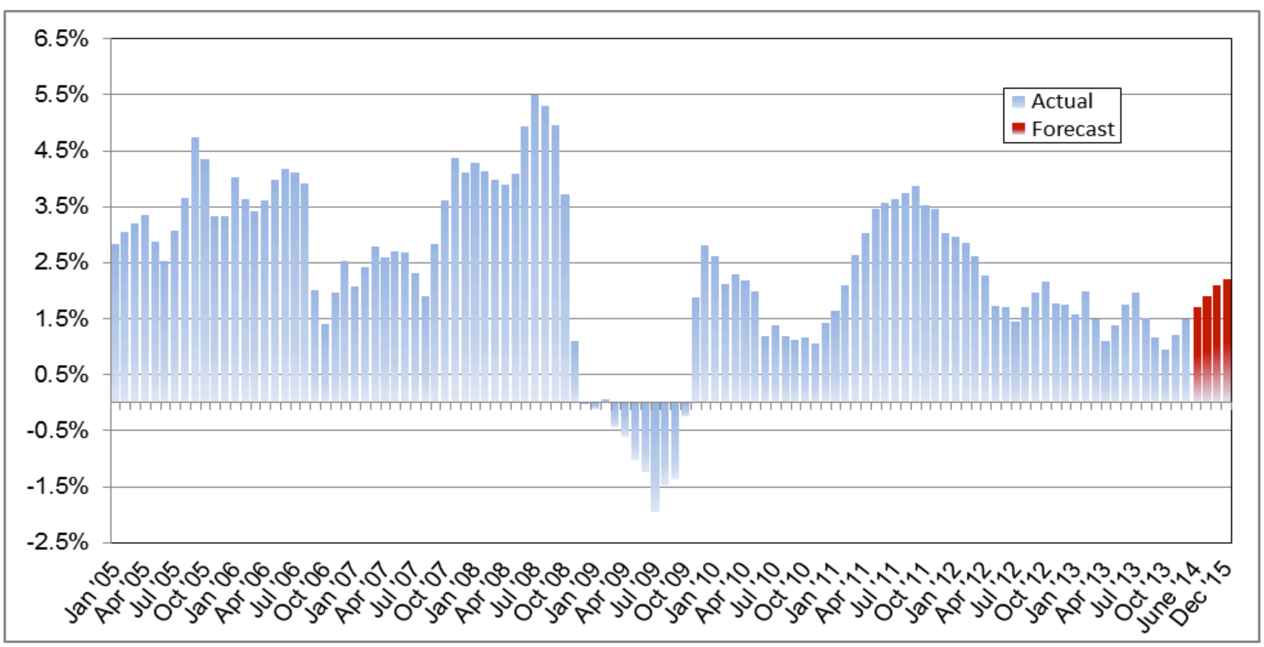


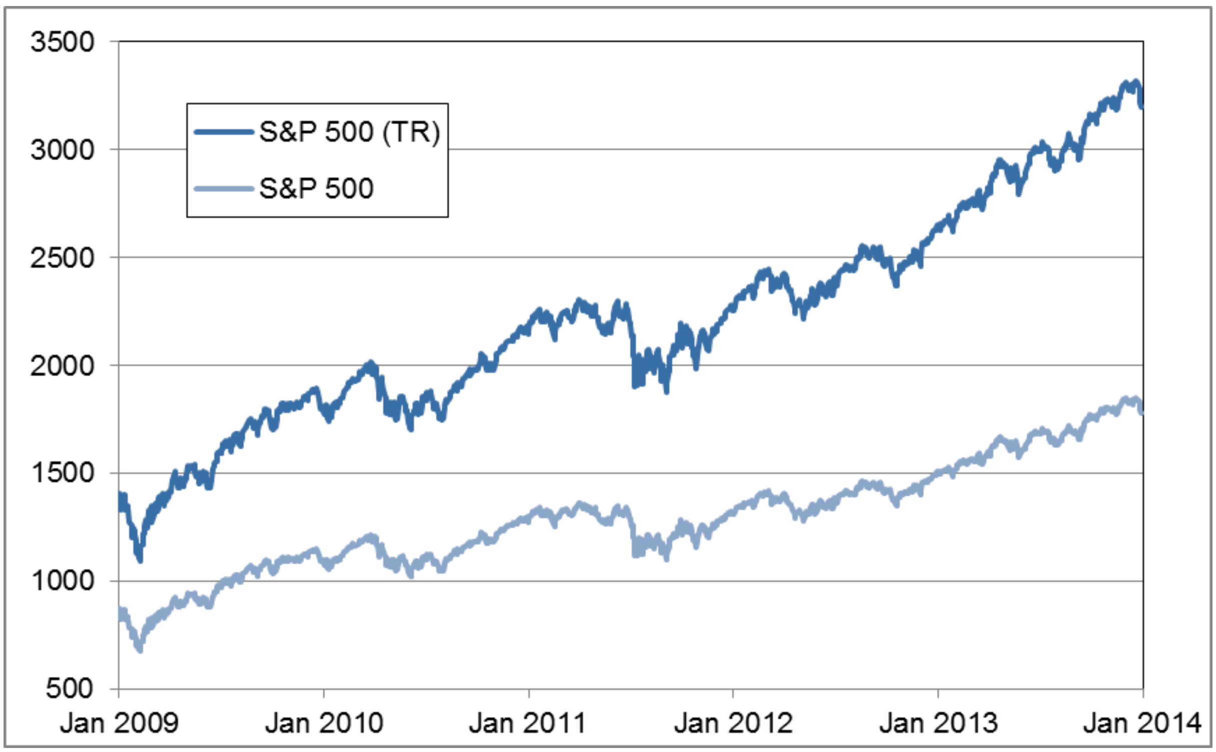
Figure 7 United States Inflation Trend, Annual Change in Consumer Price Index



Source: United States Bureau of Labor Statistics and Wall Street Journal Economic Forecasting Survey

The U.S. Bureau of Labor Statistics (BLS) reported that the Consumer Price Index for All Urban Consumers (CPI-U) increased 0.3 percent in December on a seasonally adjusted basis. Over the last 12 months, the all items index increased 1.50 percent (Figure 7). Moreover, in 2013, the BLS stated that the CPI rose 1.5 percent after a 1.7 percent increase in 2012. This is lower than the 2.4 percent average annual increase over the last ten years. This is the first time the CPI has gone up less than 2.0 percent for consecutive years since 1997-98. The Wall Street Journal forecasts that inflation rates will stay below 2.5 percent through 2015.

Figure 8: Standard & Poor's 500 stock index, 5-years



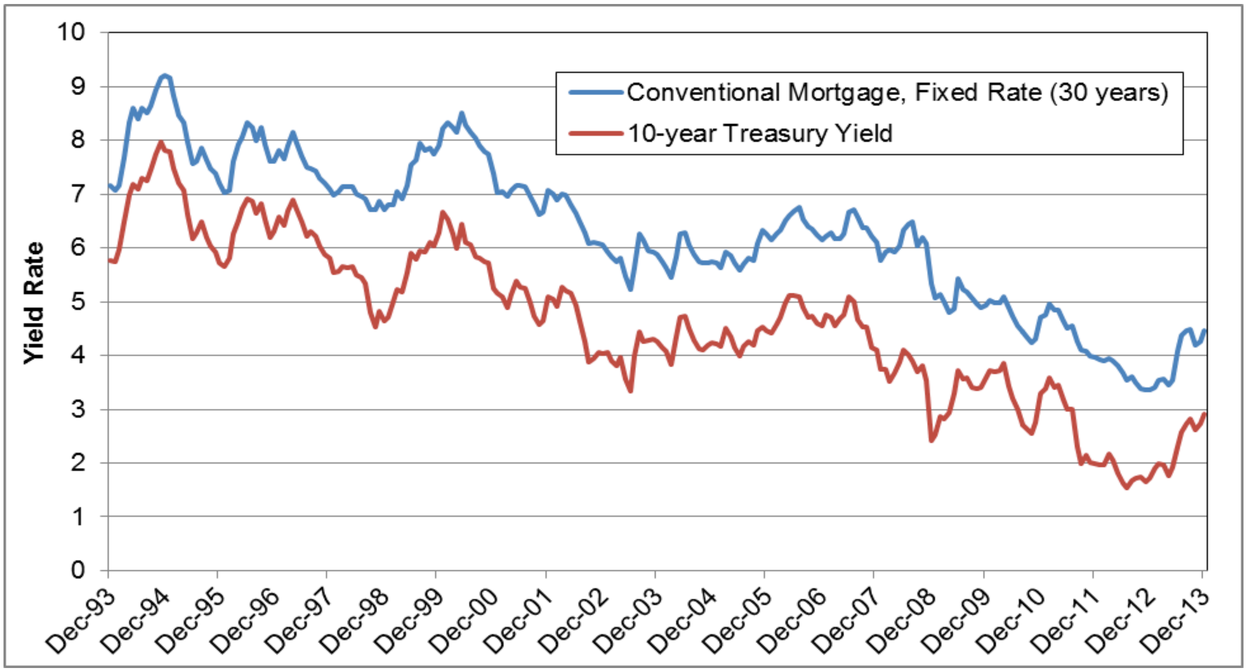
Source: S & P Dow Jones Indices, McGraw Hill Financial

Standard & Poor's long-term outlook on the U.S. credit rating to remains as "stable" and the U.S. still holds an AA+ status—which is one notch below the AAA score that the U.S. held until 2011.

Stocks finished the fourth quarter of 2013 at record highs but have been since retreated for their first monthly decline since August, in the wake of weak earnings reported by companies as well as the mounting concerns about the declining currencies in emerging markets. The S&P 400 is down nearly 4 percent for January 2014, which is the biggest decline since May 2012. (Figure 7).

Much of the reaction by the stock market is due to the decision of the Federal Reserve to buy Treasuries and mortgage bonds in an effort to drive down long-term interest rates and spur spending, hiring and investment. In December, the Fed decided to reduce the bond-buying program by $10 billion to $75 billion, but in the final meeting headed by the outgoing Bernake, the Fed announced a unanimous decision to further reduce the easy money program to $65 billion a month.

Figure 9: 10-year U.S. Treasuries vs. Conventional 30-Year Mortgage Trends, 1993–2013



Source: Federal Reserve Bank

Yields for the 10-year Treasury note increased from 2.81 in September to 2.9 in December 2013. Mortgage rates, which are closely tied to 10-year Treasury yields, began climbing in the second quarter of 2013. In April, the 30-year fixed rate was 3.45 percent. Conventional 30-year fixed rate mortgages went from 4.49 percent in September to 4.46 percent in December 2013.

Figure 10: Trade and U.S. dollar, January 2014

January, 2014	Trade balance		Current-Account Balance			Currency Units, per $		
	latest 12 months ($bn)		latest 12 months ($bn)		% of GDP	Dec 31st	year ago	% change
United States	-716.1	(Oct)	-412.9	(Q3)	-4.0	-	-	
China	+266.5	(Nov)	+14.7	(Q3)	+1.9	6.05	6.23	-2.9%
Australia	+15.8	(Oct)	-51.3	(Q3)	-2.6	1.12	0.96	16.7%
Japan	-97.4	(Oct)	+41.2	(Oct)	+1.0	105	86.5	21.4%
Canada	-8.3	(Oct)	-59.9	(Q3)	-3.1	1.06	1.00	6.0%
Sweden	+8.8	(Nov)	+34.3	(Q3)	+6.0	6.42	6.51	-1.4%
Switzerland	26.3	(Nov)	+79.9	(Q3)	+12.6	0.89	0.92	-3.3%
Britain	-170.3	(Oct)	-94.9	(Q3)	-3.5	0.6	0.62	-3.2%
Euro Area	+190.8	(Oct)	+270.7	(Oct)	+2.0	0.73	0.76	-3.9%
Germany	+256.3	(Oct)	+254.0	(Oct)	+6.9	0.73	0.76	-3.9%
Belgium	+13.1	(Oct)	-12.6	(Sept)	-1.0	0.73	0.76	-3.9%
France	-80.5	(Oct)	-45.5	(Oct)	-1.9	0.73	0.76	-3.9%
Netherlands	+58.0	(Oct)	+83.6	(Q3)	+10.6	0.73	0.76	-3.9%
Italy	+36.9	(Oct)	+16.3	(Oct)	+0.5	0.73	0.76	-3.9%
Spain	-20.0	(Oct)	+10.4	(Oct)	+0.8	0.73	0.76	-3.9%

Source: The Economist

OREGON AND THE PORTLAND AREA

Oregon ranked as the number one destination among people who moved from one state to another in 2013. According to United Van Lines' annual migration study, which tracked 129,000 moves in the United States in 2013, more than 61 percent of all interstate moves made in Oregon were for people coming to live in the state. The continued migration to the Pacific Northwest of young professionals and retirees are attributed to the availability of amenities such as public transit, green space and the local arts and entertainment scene. Inbound migration was primarily from California, Arizona, Texas, Washington and New Mexico, in descending order. Oregon's 2012-2013 population growth is estimated at 0.91 percent, significantly higher than U.S. population growth for the same time period of 0.73 percent.

The Oregon Office of Economic Analysis (OEA) states that Oregon's economy is steadily improving, much like the rest of the nation with recent job growth in Oregon's private sector being faster than the national private-sector growth. Oregon's job growth in 2013 was much stronger than in the prior two years. In 2013, 37,700 jobs were added, compared with 22,000 in 2012 and 18,400 in 2011.

The largest increase in nonfarm payroll employment (seasonally adjusted figures) since December 2012 were in the categories of Trade, Transport and Utilities (+8,500), Professional and Business Services (+7,500), Construction (+6,000), and Leisure & Hospitality (+5,800).

Figure 11: Oregon Job Growth, Nonfarm Payroll Employment, Seasonally Adjusted, Thousands

				Change From	
	Dec-13	Nov-13	Dec-12	Nov-13	Dec-12
Construction	76.0	76.4	69.2	-0.4	6.8
Manufacturing	175.8	175.5	172.5	0.3	3.3
Trade, Transport and Utilities	328.0	327.6	319.5	0.4	8.5
Financial Activities	89.1	88.9	90.0	0.2	-0.9
Professional and Business Services	206.5	204.9	199.0	1.6	7.5
Educational and Health Services	244.6	244.2	240.7	0.4	3.9
Leisure and Hospitality	178.2	178.2	172.4	0.0	5.8
Other Services	59.2	58.3	57.1	0.9	2.1
Government	289.1	287.9	289.2	1.2	-0.1
Total	1,687.5	1,683.1	1,649.8	4.4	37.7

Source: Oregon Employment Department

The OEA reports that in December, "Oregon's unemployment rate fell as more people were able to find jobs and there were fewer unemployed. There were nearly 132,000 Oregonians unemployed compared with approximately 160,000 a year earlier. This drop of more than 28,000 individuals since December 2012 was good news for many families in the state and for many sectors of Oregon's economy."

Figure 12: Portland-Vancouver-Hillsboro MSA, nonfarm payroll employment, not adjusted for seasonality

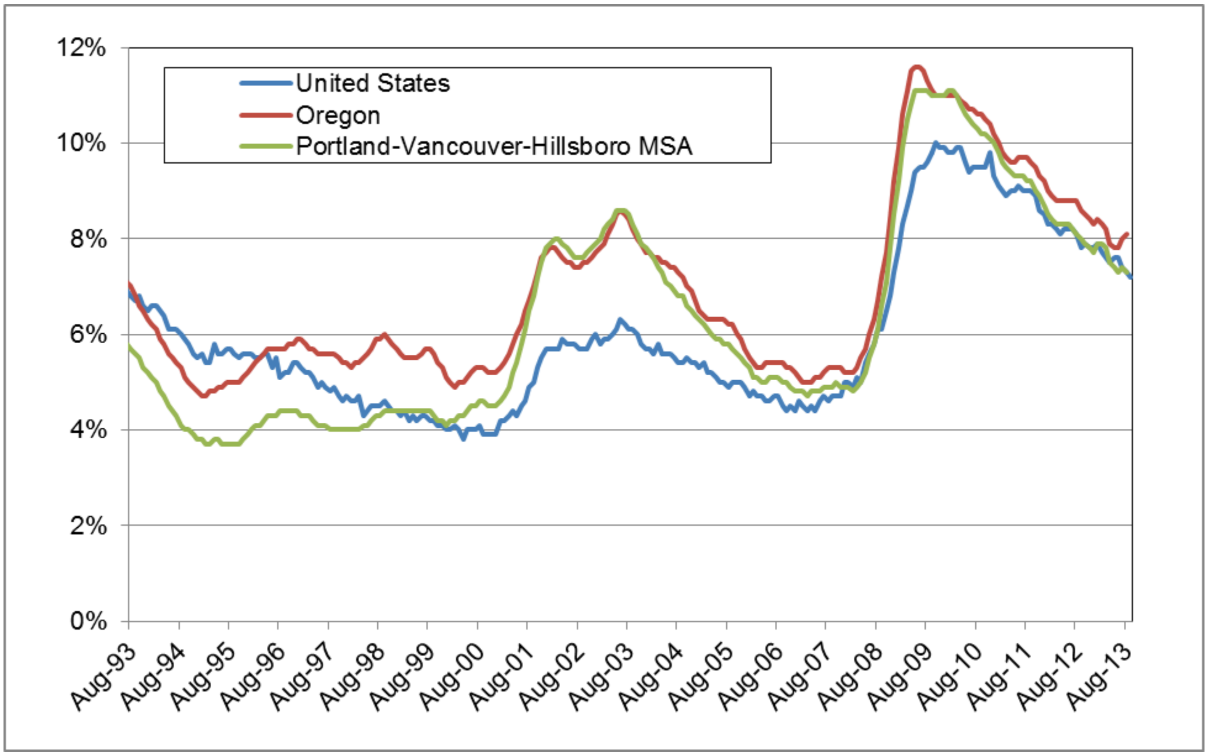
	Aug 2013		Sept 2013		Oct 2013		Nov 2013		Dec 2013	
Total Non-farm Employment	1,028,200		1,030,100		1,036,200		1,040,700		1,039,400	
Unemployment rate	7.3%		7.3%		7.0%		6.8%		6.6%	
Mining and Logging	1,000	0.0%	1,000	0.0%	900	-10.0%	900	0.0%	900	0.0%
Construction	53,700	0.8%	54,900	2.2%	54,300	-1.1%	52,700	-2.9%	51,700	-1.9%
Manufacturing	117,900	0.3%	116,700	-1.0%	116,700	0.0%	116,500	-0.2%	115,900	-0.5%
Trade, Transportation, & Utilities	198,600	-0.1%	198,200	-0.2%	198,500	0.2%	202,900	2.2%	204,500	0.8%
Information	23,100	-0.4%	23,000	-0.4%	22,900	-0.4%	23,300	1.7%	23,600	1.3%
Financial Activities	63,700	-1.4%	63,000	-1.1%	62,200	-1.3%	61,600	-1.0%	62,000	0.6%
Professional & Business Services	148,800	-0.4%	147,800	-0.7%	146,600	-0.8%	146,100	-0.3%	145,600	-0.3%
Educational & Health Services	143,700	1.3%	147,600	2.7%	150,000	1.6%	150,500	0.3%	150,100	-0.3%
Leisure and Hospitality	108,100	0.5%	105,000	-2.9%	101,600	-3.2%	101,800	0.2%	101,500	-0.3%
Other Services	37,800	1.6%	37,700	-0.3%	38,000	0.8%	37,800	-0.5%	38,200	1.1%
Government	132,500	-1.2%	135,200	2.0%	144,500	6.9%	146,600	1.5%	145,400	-0.8%

Source: Oregon Employment Department

Locally, between August to December, 2013, the industries with the majority of Portland-Vancouver-Hillsboro MSA employment growth were in Government (+12,900), Education & Health Services (+6,400), and Trade, Transportation & Utilities (+5,900), as seen below in Figure 12.

In December alone, job gains were concentrated in three of the 11 major industries: professional and business services (+1,600 jobs), government (+1,200) and other services (+900).

Figure 12: Unemployment rate, national and local



Source: Bureau of Labor Statistics and Oregon Office of Economic Analysis

Oregon's unemployment rate typically treads above the national rate and in December was 7.0 percent, slightly higher than the national rate of 6.7 percent for the same month (Figure 12). Portland-Vancouver-Hillsboro MSA has observed persistent growth in employment in recent years and, although more volatile than both the national and state unemployment rates, had unemployment remain steady at 6.6 percent in December on a seasonally adjusted basis. ■