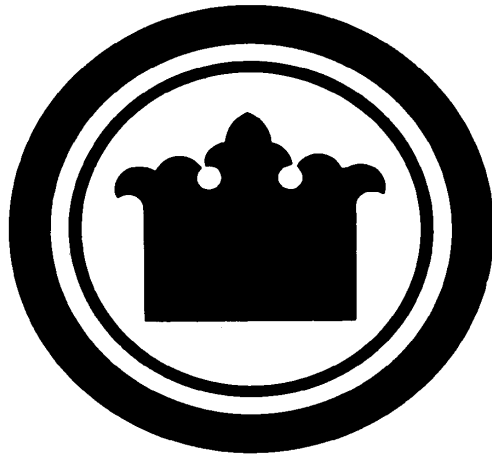


QUARTERLY ECONOMIC REPORT
2nd Quarter, 2003



KING COUNTY
OFFICE OF MANAGEMENT AND BUDGET

SUMMARY

Economic conditions, particularly local labor markets, continue to suffer the effects of the recession. After almost three years of decline, business expenditures appear to be rebounding, fueling hopes of a true recovery in the second half of the year. At the same time, a precipitous increase over the last two months in long term interest rates will undermine consumer spending, particularly in residential real estate.

The local economy is expected to improve just slightly in the coming months, with only announcement of the manufacturing location of the Boeing 7E7 jetliner likely to produce a substantial shock one way or the other. The immediate economic outlook is largely unchanged, with the prospect of only a marginal decline in unemployment in the next six months.

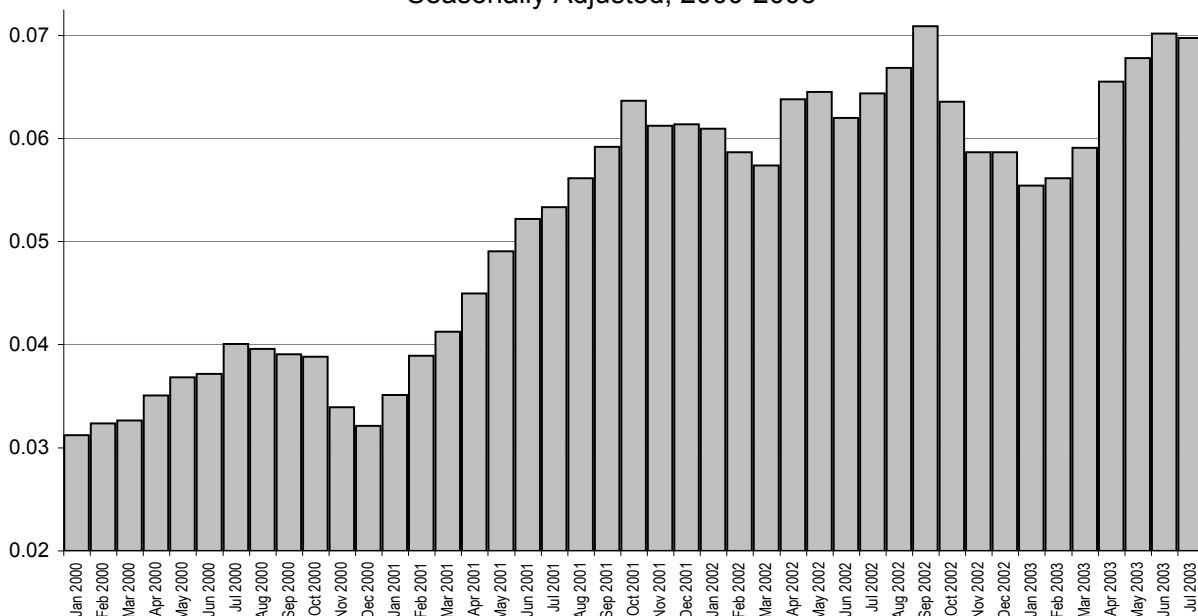
REVIEW OF ECONOMIC CONDITIONS

New national unemployment and GDP data released last week suggest some improvement, but belie other problems. The declining national unemployment rate primarily reflects fewer unemployed workers seeking new jobs: total employment has fallen for six consecutive months. Robust preliminary estimates of GDP growth for the second quarter were spurred by exceptionally high levels of defense procurement, and are probably not indicative of wider trends.

Regional economic conditions remain poor. Seasonally adjusted unemployment in King County reached a 19-year high for the month of May, at 6.78 percent. Personal bankruptcy filings in the county have grown by 12.3 percent year-to-date, while May bankruptcy petitions doubled from a year ago.

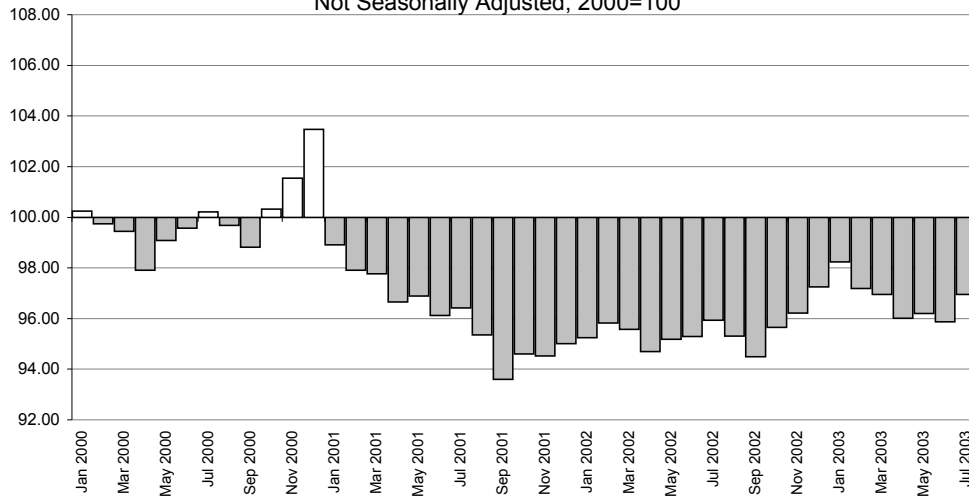
Non-energy inflation remains dormant, but concerns of deflation have eroded in the face of resurgent petroleum prices. After falling over 25 percent following the Iraq war, the price of light sweet crude oil has rebounded to above \$32 per barrel. Delays in bringing Iraqi oil production back to pre-war levels will likely keep oil 50 to 60 percent above January 2002 prices for the foreseeable future.

King County Unemployment Rate
Seasonally Adjusted, 2000-2003



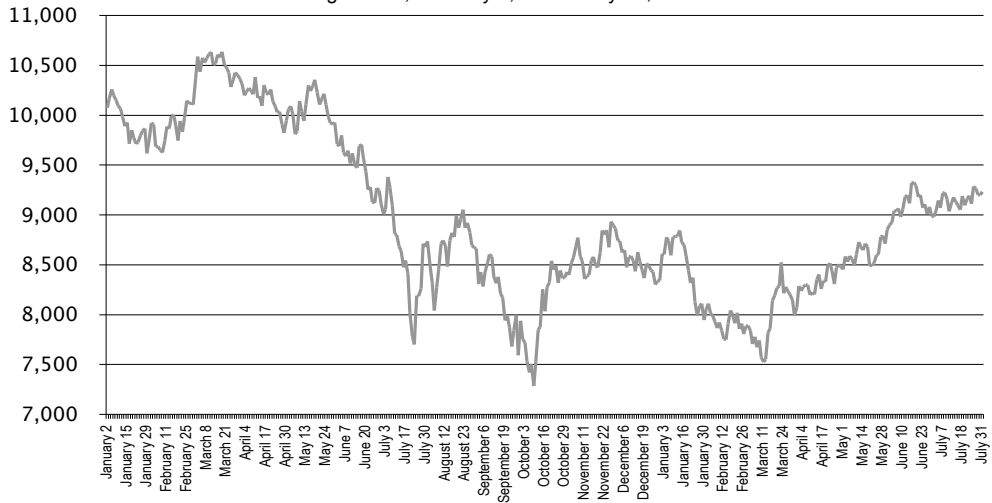
King County Total Employment

Not Seasonally Adjusted, 2000=100



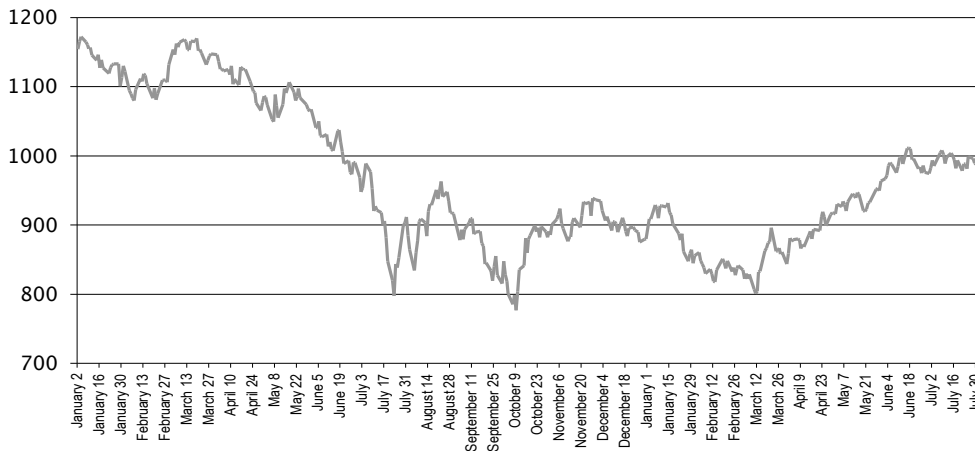
Dow Jones Industrial Average

Closing Values, January 1, 2002 - July 31, 2003



Standard and Poor's 500 Index

Closing Values, January 1, 2002 - July 31, 2003



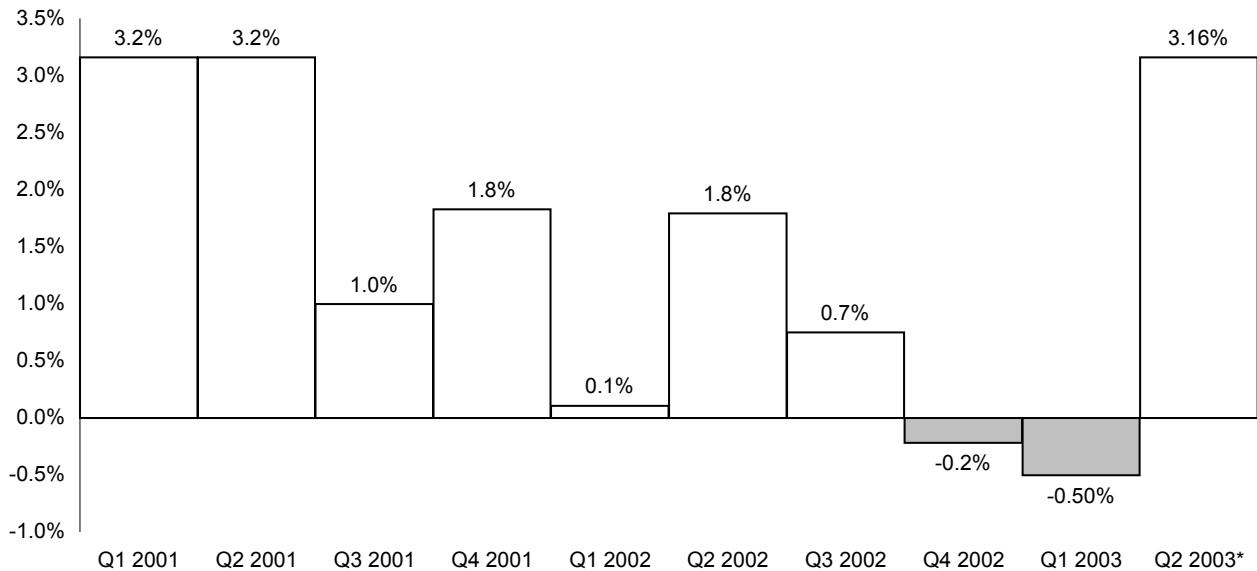
Appreciating equity markets will likely fuel higher state personal income numbers this year, but it may be fleeting. Last month's announcement by Microsoft that it will award stock rather than stock options greatly reduces the variability of this compensation even as option derived income rebounds. As a result, personal income growth will be lower when stock market valuation growth is highest – the expectation for the next couple of years as the economy recovers from recession.

Residential real estate continues to surge, although it will undoubtedly slow with higher interest rates. With demand for new homes almost certain to fall, and no appreciable increase in commercial demand, we are likely entering a period of dislocation in the construction sector.

Although local Boeing employment has fallen by 8 percent so far this year, the Air Force's announced lease of 100 in-flight refueling aircraft provides critical long term support to the faltering 767 production line. The 757 line, however, remains precarious.

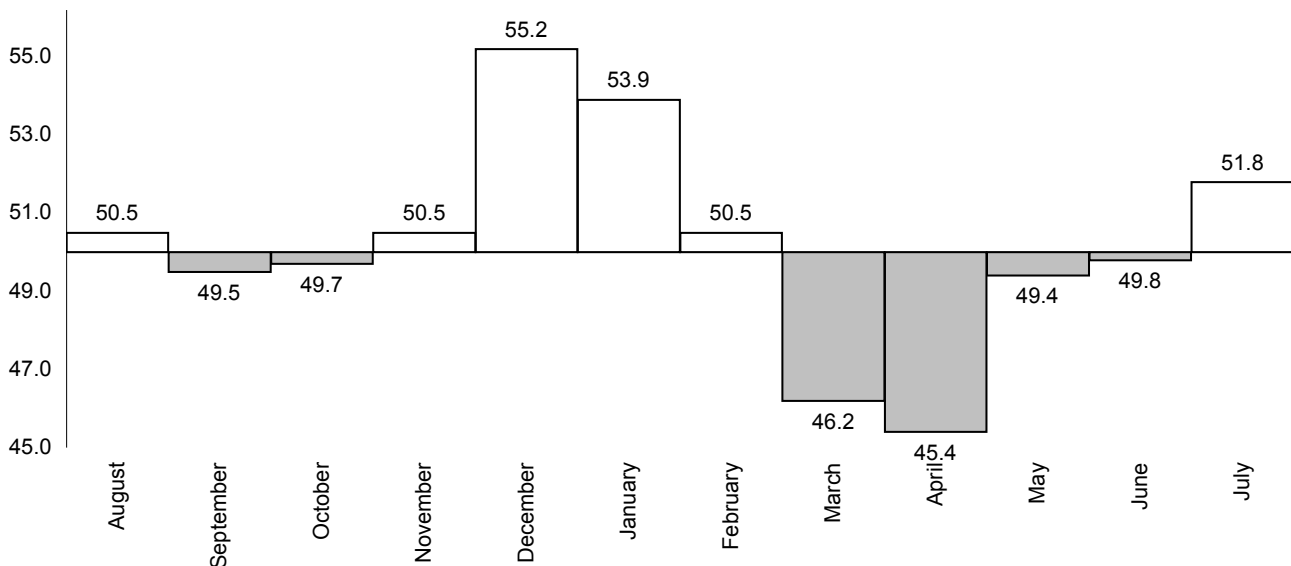
US Private Residential Construction

Quarterly Change, Completed Units



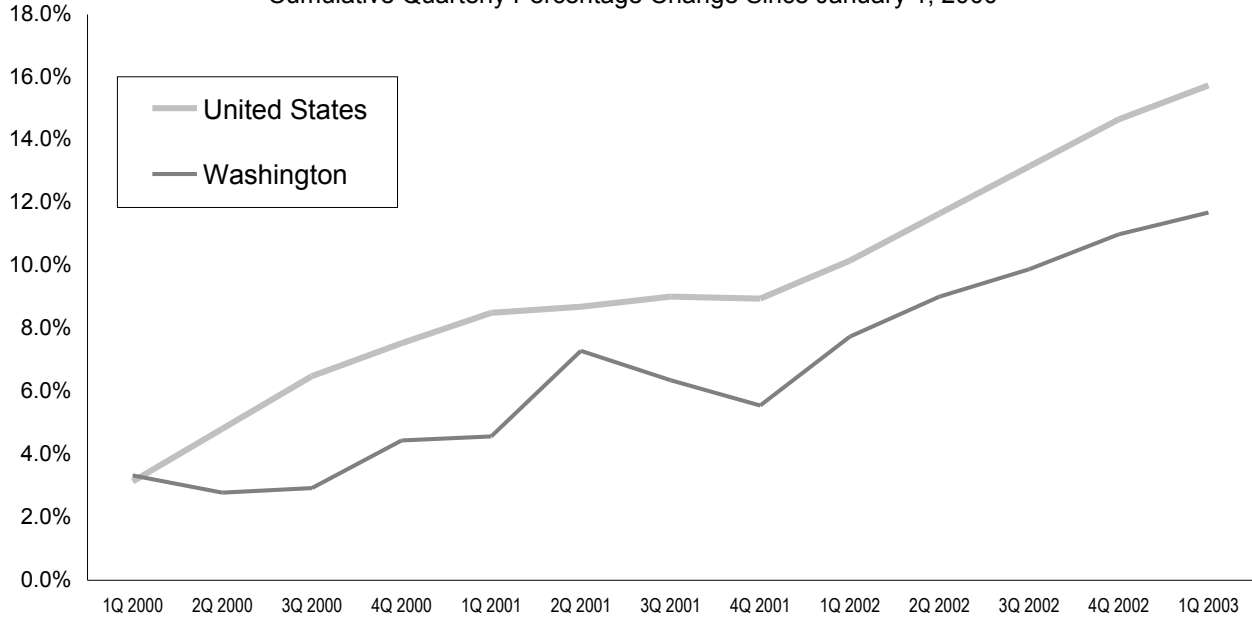
US Manufacturing Activity Index

PMI Monthly Data since August 2002; Scores Below 50 Indicate Contraction



Nominal Personal Income Growth

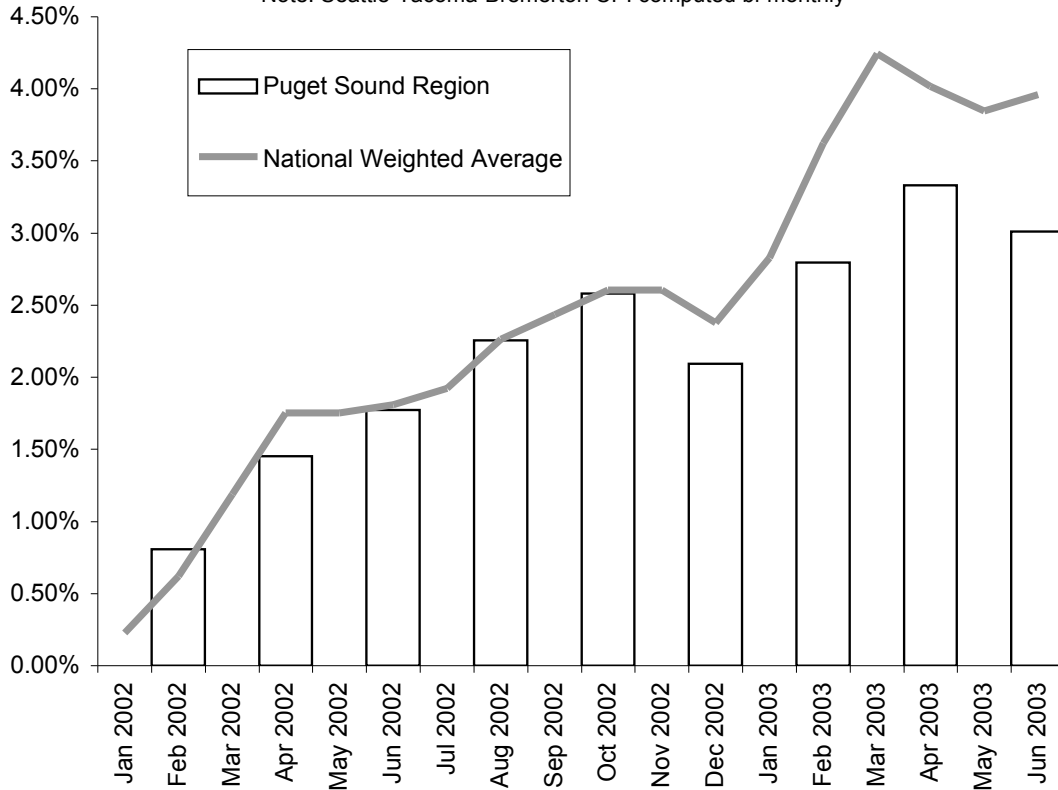
Cumulative Quarterly Percentage Change Since January 1, 2000



National and Local Inflation Comparison

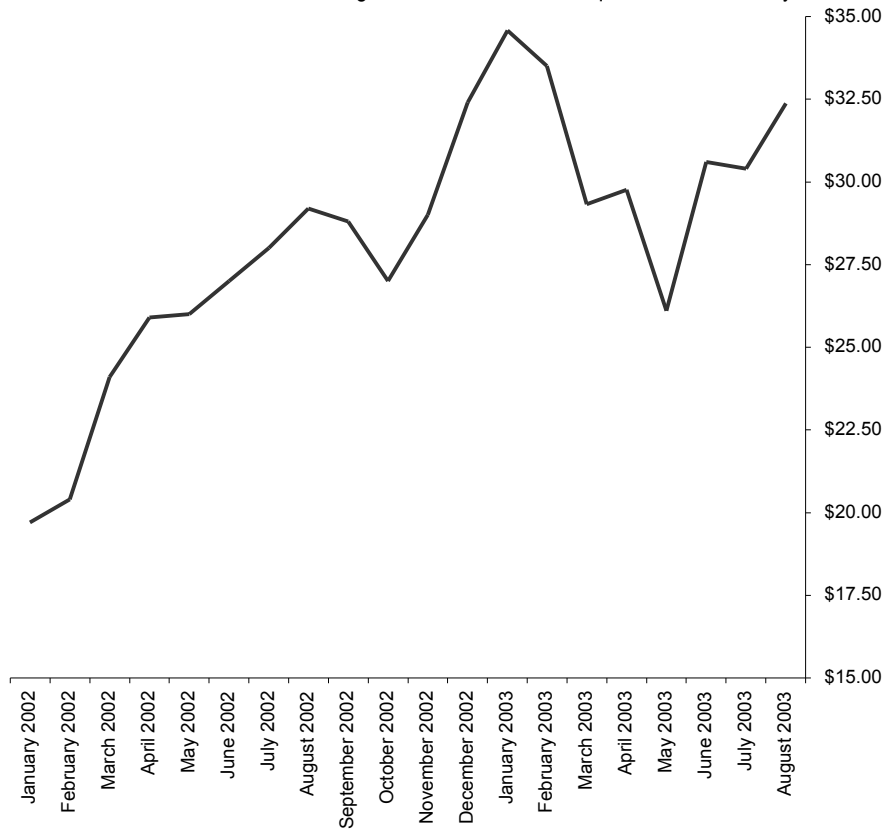
CPI-U, cumulative change since 2001

Note: Seattle-Tacoma-Bremerton CPI computed bi-monthly



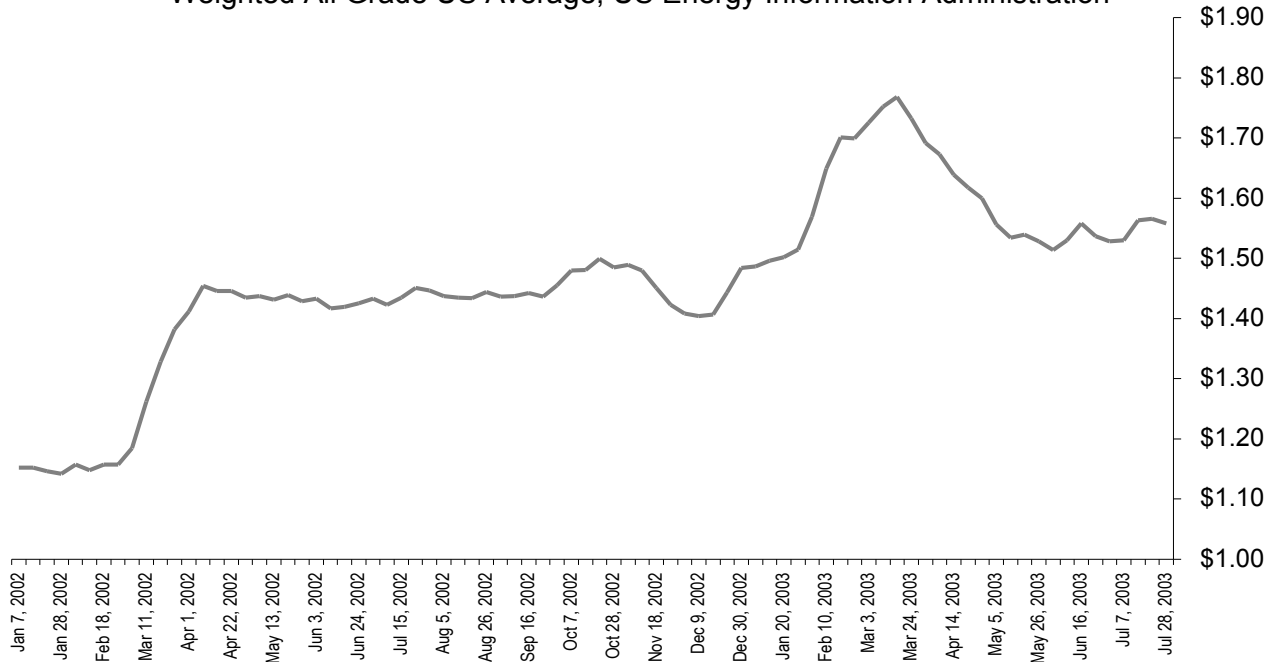
Light, Sweet, Crude Oil Price

New York Mercantile Exchange, Initial Price on Subsequent Month Delivery



Average Retail Gasoline Price per Gallon

Weighted All Grade US Average, US Energy Information Administration



A JOBLESS RECOVERY

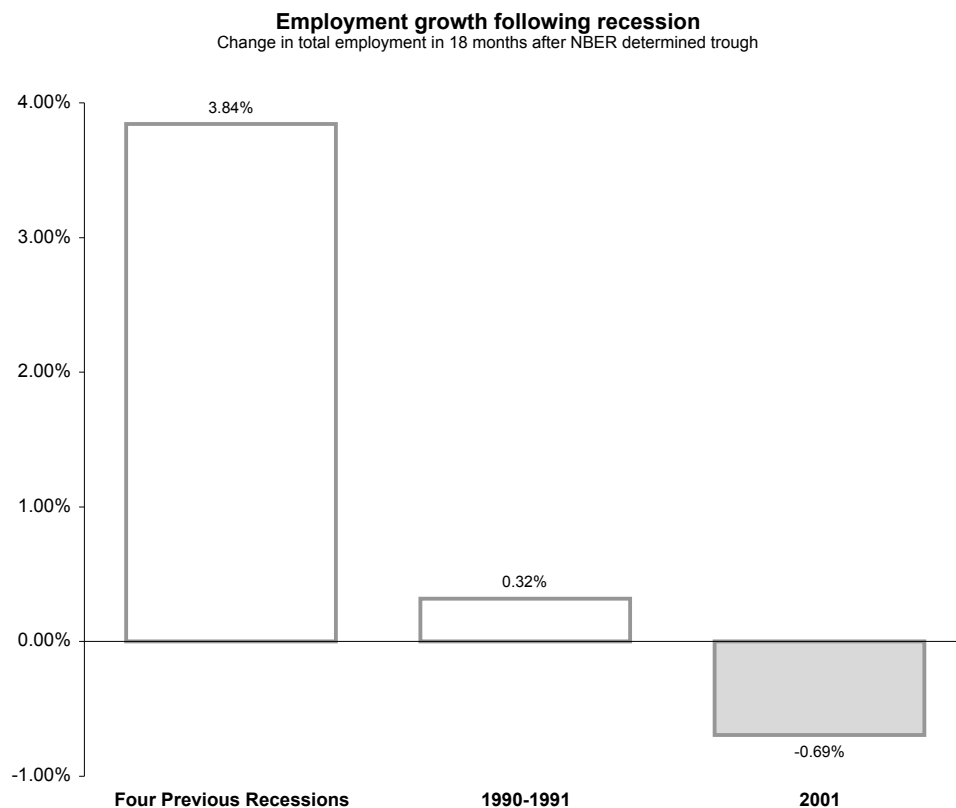
In July, the National Bureau of Economic Research determined that the national recession ended in November, 2001. The duration – eight months – is only somewhat shorter than the average of 10.4 months since the Second World War. Less typical has been the recovery. Similar to the early 1990s, the country has been mired in a jobless recovery.

A dozen years ago economic forecasters generally failed to predict the depth and duration of the employment market slowdown following the 1990-1991 recession. Although somewhat lagged, economic growth is typically strongly correlated with increased non-farm employment, especially in an economic recovery.

An analysis by the Federal Reserve Bank of Kansas City comparing previous recoveries to 1990-1991 and 2002 illustrates the difference. Instead of twelve months of steady employment growth at an annualized rate of 2.7 percent in the previous periods, the two more recent recessions have been followed by an actual decline in payrolls. This difference in percentage growth rates equates to 1.8 million fewer jobs.

Part of the disparity is explained by generally shallow economic growth. Gross Domestic Product grew by about 2.5 percent in the 12 months following the trough of the last two recessions, compared with the historic average of 6 percent. The Kansas City Fed also cited increased levels of temporary employment, up eight-fold since 1972, and part-time workers, up a more modest 40 to 60 percent over the same time period, as contributing factors. Viewed as a reflection of just-in-time production practices, low employment levels simply reflect flexible labor utilization in the face of uncertain demand.

In addition to casting doubts on prevalent forecasting methods, this line of thinking undermines a key assumption for regional growth – that national demand will drive the Puget Sound's recovery. Indeed, even as economy emerges from recession, employment growth will continue to lag.



POPULATION GROWTH SLOWS

April estimates of city and county population by the Washington State Office of Financial Management show the slowest growth rate in 20 years for both the state and King County.

King County's 2003 population is estimated at 1,779,300 – only 5,000 more people than a year ago. That's the smallest absolute increase since 1983 when the County gained 4,400 people to about 1,315,000. The primary reason for the sluggish growth is the same as 20 years ago: the economy. King County has lost roughly 5 percent of the job base since the employment peaked in mid-2000. Decreased immigration from overseas is also responsible: in the last year, only half as many immigrants have arrived as in each of the years of the late 1990s.

One consequence of this slow growth is more people moving out of King County than moving in. The natural increase (excess of births over deaths each year) is around 10,000 persons per year. Some workers and families who have lost their jobs are moving away to find opportunities. Unlike the mild recession of the early 1990s, the rest of the US is faring better than we are, so job opportunities elsewhere beckon people out of the state. It also means many of those who have stayed here are struggling: the unemployment rate is almost twice the 3.5% that it was in 1999. In addition, the slow population growth compounds the business slowdown, with fewer new firms being created while existing firms struggle to keep their customer base.

OFM does not prepare short-term forecasts, but the prevailing view among local economists is that it will be at least another year or two before the Puget Sound economy improves enough to prompt significant job growth and population growth.

The complete set of estimates is available at www.ofm.wa.gov

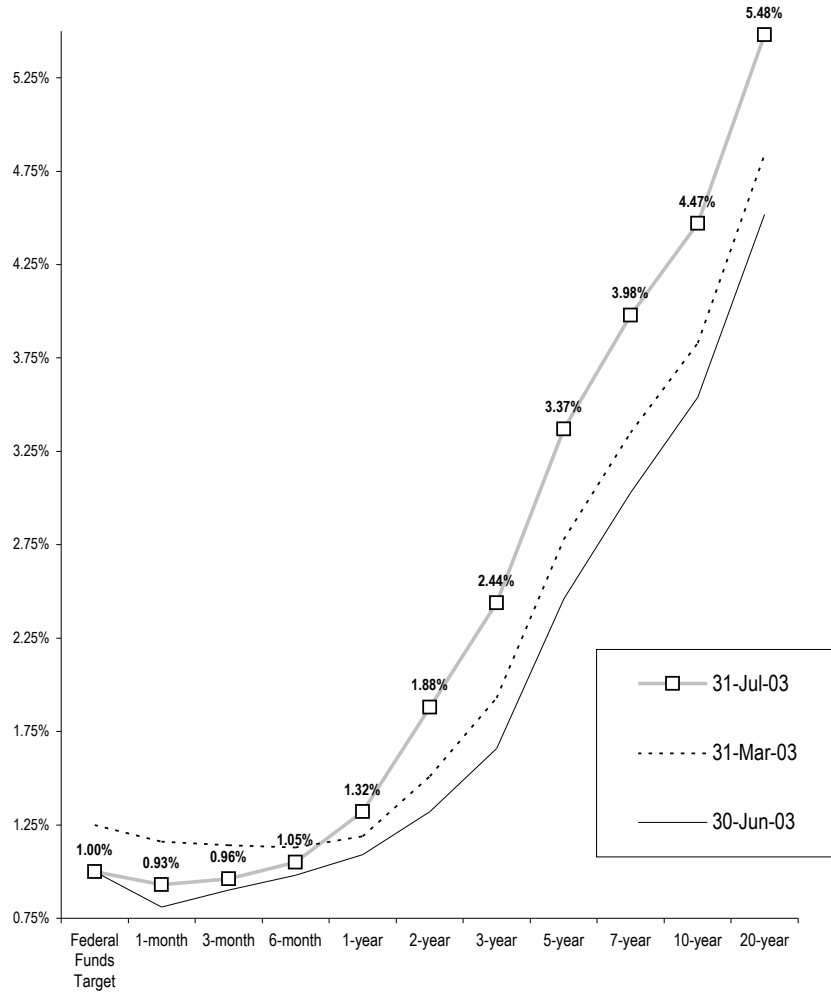
Population Trends

Official State April 1 Estimates and 2000 Census

	2000	2002	2003
King County	1,737,034	1,774,300	1,779,300
change since 2000		2.15%	2.43%
Uninc. King	349,224	351,675	351,843
change since 2000		0.70%	0.75%
Bellevue	109,827	117,000	116,400
change since 2000		6.53%	5.98%
Federal Way	83,259	83,850	83,500
change since 2000		0.71%	0.29%
Kent	79,524	84,275	84,210
change since 2000		5.97%	5.89%
Seattle	563,374	570,800	571,900
change since 2000		1.32%	1.51%
Washington	5,894,143	6,041,710	6,098,300
change since 2000		2.50%	3.46%

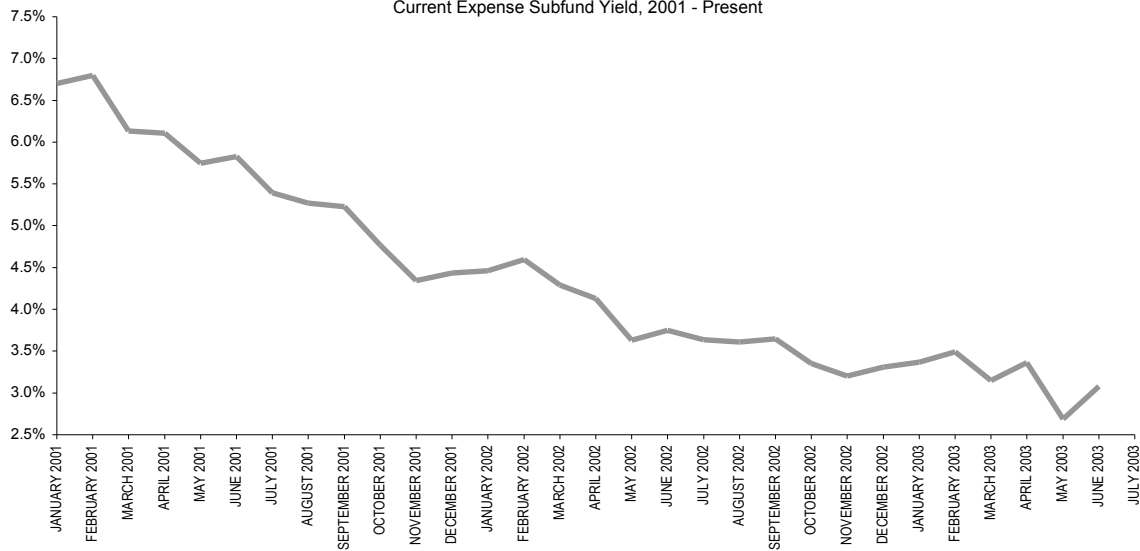
US Government Securities Yield Curve

Close of market bids, Constant Treasury Maturity Yields



Net Rate of Return on Pool Fund Balances

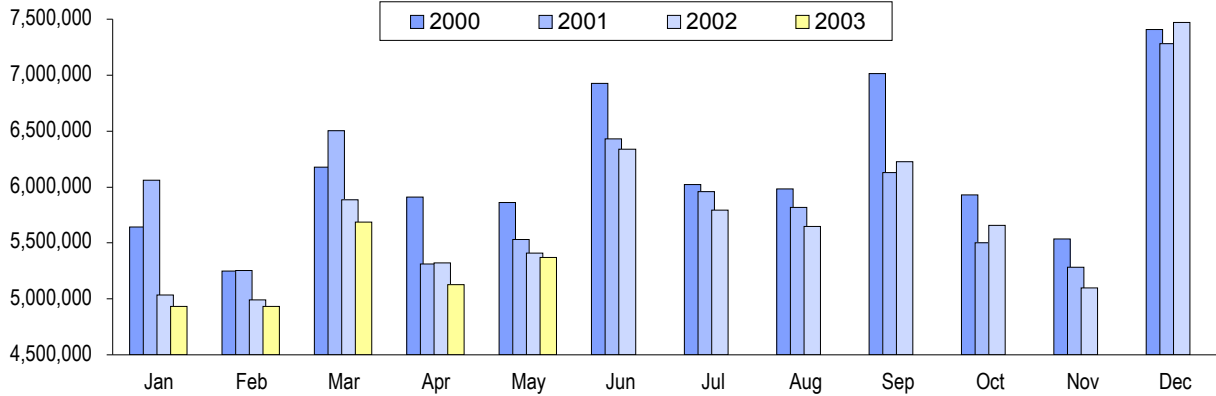
Current Expense Subfund Yield, 2001 - Present



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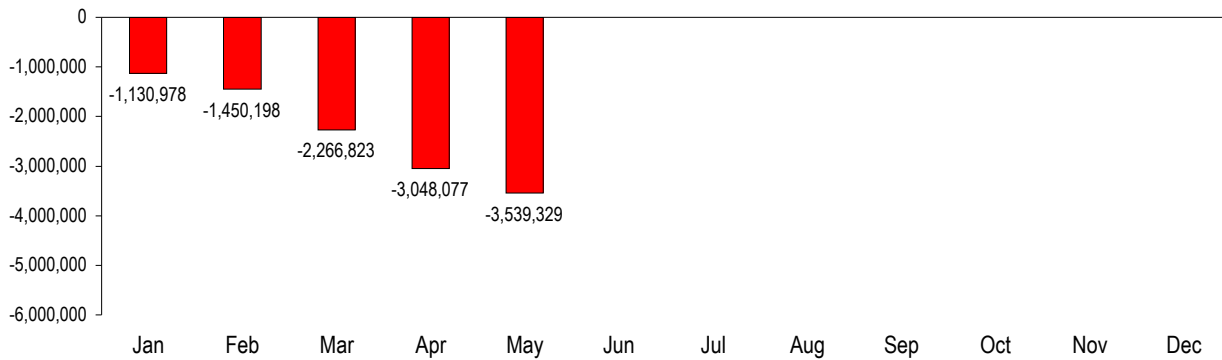
King County Monthly Sales Tax Collections



Monthly Collection Detail

	January	February	March	April	May	June	July	August	September	October	November	December
2000	5,643,746	5,247,801	6,175,848	5,908,357	5,860,285	6,924,611	6,023,919	5,982,095	7,013,757	5,929,100	5,534,585	7,407,359
2001	6,062,931	5,251,282	6,503,883	5,313,379	5,533,086	6,431,011	5,958,177	5,815,392	6,127,737	5,499,377	5,280,576	7,282,334
2002	5,036,669	4,988,719	5,884,638	5,321,370	5,407,187	6,339,046	5,792,913	5,645,463	6,228,228	5,656,303	5,096,438	7,471,553
2003	4,931,954	4,932,061	5,687,259	5,127,102	5,369,033							

Year-to-Date 2003 Variance from 2000-2001 Peak



Year-to-Date Collection Detail

	January	February	March	April	May	June	July	August	September	October	November	December
2000	5,643,746	10,891,548	17,067,396	22,975,752	28,836,037	35,760,649	41,784,567	47,766,662	54,780,419	60,709,520	66,244,105	73,651,464
2001	6,062,931	11,314,213	17,818,096	23,131,476	28,664,562	35,095,573	41,053,750	46,869,143	52,996,879	58,496,256	63,776,832	71,059,166
2002	5,036,669	10,025,388	15,910,026	21,231,396	26,638,583	32,977,629	38,770,542	44,416,005	50,644,233	56,300,536	61,396,974	68,868,527
2003	4,931,954	9,864,015	15,551,273	20,678,376	26,047,409							

* Data presented are total local option sales tax collections less Department of Revenue 1 percent administration fee. 90.4 percent of County sales tax receipts are deposited in the current expense fund. The remainder are dedicated to the Sales Tax Cont

REVIEW OF REVENUE COLLECTIONS

Recent sales tax activity has fallen 2.2 percent below 2002 levels. We are hopeful that this variance will be offset by year end collections in December, but this revenue will not be disbursed to the county until February 2004. In light of poor year-to-date collections and the speculative nature of year end revenue, forecasted sales tax revenues for the general fund were reduced by \$0.7 million in the second quarter report.

Interest earnings have remained surprisingly high. Even after another 25 basis point reduction in the Federal Reserve's target rate, the county investment pool yield is still close to 3 percent, dipping below that level only in May after property tax payments temporarily boosted the residual fund balance above \$3.75 billion. Although treasury operations has done a remarkable job of maintaining yields in the first half of the year, a return of 2.5 percent is still forecasted for the year.

ECONOMIC FORECAST

The outlook is mixed for the rest of the year. While there are signs of the abortive recovery finally taking hold in the second half of 2003, weak employment data and rising interest rates suggest that widespread improvement will wait until 2004.

Summary Economic Forecast

Percentage Change from Preceding Year

	2001	2002	2003	2004	2005
Puget Sound Region					
Employment	-0.7%	-2.7%	-0.1%	1.3%	2.6%
Nominal Personal Income	2.3%	1.8%	1.9%	4.1%	5.0%
Housing Permits	-5.3%	-3.8%	0.0%	-3.9%	1.3%
Population	1.1%	1.0%	-0.1%	0.8%	0.9%
Consumer Price Index	3.7%	1.9%	2.0%	2.0%	2.1%
Washington State					
Employment	-2.9%	1.7%	0.7%	1.4%	2.0%
Nominal Personal Income	2.6%	3.5%	3.6%	4.4%	5.0%
Housing Permits	-1.7%	11.1%	-7.2%	-1.6%	5.0%
United States					
Employment	0.2%	-0.9%	0.0%	1.4%	2.0%
Nominal Personal Income	3.3%	3.1%	3.3%	4.9%	5.3%
Housing Starts	2.0%	4.5%	-3.0%	-1.0%	-0.5%
Three-month Treasury Yield	-22.0%	-47.1%	-11.3%	4.6%	53.5%
Consumer Price Index	2.8%	1.6%	2.2%	2.1%	2.2%
GDP	0.3%	2.4%	2.1%	3.0%	3.3%