



BRIEFLY

The March forecast reduces the funds available for the 2001-2003 biennium and shows an increased risk of recession. The legislature should be cautious in writing a budget for the upcoming biennium.

March Revenue Forecast Released

Last Friday, March 16th, state economist Chang Mook Sohn presented the revised forecast of the state General Fund revenues for the current (1999-2001) and upcoming (2001-2003) biennia. Traditionally, the presentation of the March revenue forecast marks the beginning of the period of serious budget deliberations by the legislature.

On the surface Dr. Sohn's forecast took the form of the archetypical economist's pronouncement: on the one hand forecast revenue for the current biennium is up by \$143.5 million; on the other hand the forecast is down by \$111.6 million for the 2001-2003 biennium. The net result is apparently a \$31.8 million increase in revenues for the two biennia taken together.

However, when account is taken of the manner in which state law earmarks reserves, the forecasts actually reduce the funds available for general fund spending in the 2001-2003 biennium by \$88.4 million. Moreover, the forecast shows a slowing economy and a significantly increased risk of recession. In writing a budget for the upcoming biennium, the legislature should be cautious.

Much of the revenue bump for the current biennium is earmarked for education

Table 1 shows balance sheets for the current biennium. The left column reflects the situation as of the November 2000 forecast, while the right column incorporates the March 2001 revisions.

TABLE 1
1999-2001 Balance Sheet
(Millions of dollars)

	November 2000	March 2001
Resources		
Beginning Fund Balance	462.0	462.0
November Revenue Forecast	21,168.9	21,168.9
March 2001 Changes		143.5
Current Revenue Totals		21,312.4
Adjustments		(1.0)
Total Resources	21,631.0	21,773.4
Expenditures		
1999-01 Appropriations	20,851.1	20,851.1
Preliminary I-601 Expenditure Limit	20,934.7	20,934.7
General Fund Balance		
Total Ending Balance	779.9	922.2
Transfer to Emergency Reserve	(234.3)	(377.7)
Unreserved General Fund Balance Before I 728 Spillover	545.6	544.6
I 728 Spillover	4.8	21.8
Unreserved General Fund Balance	550.4	566.4
Emergency Reserve Fund		
Beginning Balance	535.7	535.7
Transfer to Transportation	(35.0)	(35.0)
Transfer from General Fund	234.3	377.7
Interest Earnings	63.8	63.3
Transfer to Education Construction Account	(242.8)	(310.5)
Transfer to Student Achievement Account	(14.4)	(65.5)
Transfer to General Fund	(4.8)	(21.8)
Emergency Reserve	536.8	544.0

Note: Due to rounding, detail may not sum to totals
Source: Senate and House Fiscal Committees and Office of Financial Management

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The March forecast has boosted available resources (the beginning fund balance plus forecast revenues) for the current biennium by \$142.5 million, to \$21.77 billion. Of this boost, an increase of \$133.9 million is due to changes in the economic forecast tied to higher than anticipated revenue collections in the four months since the November forecast, and an increase of \$9.5 million is due to Initiative 722. A technical adjustment reduces available revenue by \$1.0 million.



Appropriations for the biennium stand at \$20.85 billion so far, while the preliminary I-601 expenditure limit is \$20.93 billion. The legislature will most likely boost appropriations via a supplemental budget. The legislature may also take actions that would boost the I-601 limit. (See *I-601 Not Dead Until Legislature Declares It So*, ePB01-3, February 21, 2001.)

Changes in recent years have created a complicated set of rules governing general fund reserves. Reserves are now held both in the General Fund itself and in the Emergency Reserve Fund, created by Initiative 601. Money spills into the Emergency Reserve Fund from the General Fund when revenues exceed the I-601 spending limit. When the balance in the Emergency Reserve exceeds 5 percent of annual revenues, the excess is spilled out to other accounts. Prior to enactment of I-728, the Education Construction Account received this excess. Under the provisions of I-728, beginning January 1, 2001, 75 percent of the excess goes to the Student Achievement Account and 25 percent back into the General Fund.

As a result of these provisions and the current value of the I-601 limit, the greater part of the increased resources identified by the new forecast go into the education accounts. The Education Construction Account receives \$67.7 million while the Student Achievement Account gets \$51.1 million. Only \$16.0 million is added to the General Fund’s ending balance, and only \$7.2 million to the Emergency Reserve ending balance.

A slowing economy reduces forecast revenue for the 2001-2003 biennium.

As a result of the forecast, less money is available to legislators writing the budget for the 2001-2003 biennium, as shown in Table 2.

The beginning General Fund balance is up by \$16.0 million.

Forecast revenue for the 2001-2003 biennium is down by \$111.6 million. The state’s economist has reduced the estimate of the rate of growth of the state’s economy for the years 2001 and 2002, and therefore dropped forecast revenues by \$123.9 million. This is offset in part by a \$12.3 million adjustment associated with Initiatives 722 and 728.

Thus General Fund resources are down by \$95.6 million. With the additional \$7.2 in the Emergency Reserve Fund, available funds are down \$88.4 million.

Discussion

A tough situation just got tougher. We noted in December (*Lawmakers Face Toughest Budget Challenge since*

TABLE 2

2001-2003 General Fund Resources (Dollars in millions)

	November 2000	March 2001
Beginning Balance	550.4	550.4
March 2001 Forecast Change		16.0
Adjusted beginning Balance		566.4
November 2000 Forecast	22,327.1	22,327.1
March 2001 Forecast Changes		(123.9)
Non Economic Changes		12.3
Adjusted Revenues	22,327.1	22,215.5
Total Resources	22,877.5	22,781.9
Emergency Reserve Fund		
Beginning Balance November 2000 Forecast	536.8	536.8
March 2001 Changes		7.2
Adjusted Beginning Balance	536.8	544.0

Source: Office of the Forecast Council



1993, ePB 00-36, Dec. 14, 2000) that simply to meet the continuing costs of current programs and services would take \$300 million more in spending than allowed by the I-601 expenditure limit. Since then, the Caseload Forecast Council upped its forecasts K-12 education and General Assistance, and the Nisqually earthquake shook the state.

Besides the reduction in forecast revenues for the 2001-2003 biennium, the March 16 revenue meeting brought the news that the Dr. Sohn sees an increased probability that the state will actually slip into recession. The probability of this “pessimistic scenario” is now put at 45 percent rate. Under this scenario, 2001-2003 revenues are forecast to be \$934 million lower than the baseline forecast.

There is an extraordinary degree of uncertainty in the outlook of the state

The warning signs of a possible recession are all around. Dot coms are dying off at a faster rate than salmon. The stock market has fallen significantly, evaporating the options values that have been driving the growth in our state’s personal income. California’s pseudo deregulation has roiled western electricity market as drought threatens the supplies of Northwest hydro power and the meager incomes of Washington’s farmers.

Nevertheless, state revenues have remained remarkably strong in recent months.

The state seems poised to end the biennium with healthy balances in both the General Fund and the Emergency Reserve Fund.

With the current levels of reserves, the state does have the flexibility to address the costs of earthquake recovery through a supplemental budget for the current biennium.

With all of the uncertainty, however, the legislature should preserve its options, writing a budget for the 2001-2003 biennium that avoids new long-term commitments and maintains these healthy reserves. If we are lucky, if the state avoids a recession and revenue inflows to the state remain strong, the 2002 legislature will have the opportunity to revisit the spending plan through a supplemental budget.



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