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ARE WE THERE YET? STATE REVENUE FORECAST REDUCED AGAIN

BRIEFLY

The September forecast reduced combined general fund revenues for the 2007–09 and 2009–11 biennia by \$238 million. For the broader near general fund, the reduction was \$230 million.

The Economic and Revenue Forecast Council met in Olympia today to formally update its forecasts of the state's economy and general fund revenue. The revisions subtracted \$6.8 million from the forecast of general fund revenues for the 2007–09 biennium and \$230.9 million from the general fund forecast for 2009–11. (Of the amount subtracted from 2009–11, \$46.1 million was the effect of a recent Supreme Court ruling with respect to B&O taxes on interest earnings.) For the broader "near general fund-state" (NGFS), which combines the general fund and other accounts, 2007–09 revenues are down \$0.3 million and 2009–11 revenues are down by \$230.0 million. (See the box on page 3 for a discussion of the distinction between the general fund and the near general fund.)

With this forecast, the state's budget is significantly out of balance. The problem, however, does not appear large enough to require the Legislature to meet in special session prior to the regularly scheduled 2010 session.

THE ECONOMIC FORECAST

The new economic forecast is little changed from that issued in June. State forecasters believe that the national economy has hit bottom, but expect the recovery to be tepid. It will be some time until main street feels like the recession has ended:

We won't know the official recession end date until some time late in 2010, or early 2011. It usually takes the National Bureau of Economic Research (NBER), the official arbiter of recessions for the United States a year or more after the recession ends to arrive at that conclusion. However, the consensus view amongst economists is that when they finally put an end point on this recession, the NBER is likely to say the recession that started in December 2007 ended in August 2009. This does not mean we are back to where we started. All it means is that the decline in activity has troughed or hit bottom. Our latest [national] forecast expects a slow U-shaped recovery, and it will be a while before we get back to the levels we fell from. To put it differently, we are crawling along at the bottom of the U. (ERFC 2009a)

Earlier this week, Federal Reserve Chairman Ben Bernanke struck a similar note following a speech at the Brookings Institution:

Even though from a technical perspective the recession is very likely over at this point, it's still going to feel like a very weak economy for some time. (Lanman and Torres 2009)

Likewise, state forecasters believe that the recovery in Washington's economy will be tepid. Nevertheless, there are signs that the state will lead the nation out of recession. The new economic forecast for the state sees fewer jobs losses this year than the old forecast, and greater job gains next year:

Typo corrected 9/23/2009

The Washington economy has performed close to what we had expected in our June forecast... The rate at which employment is declining has slowed in recent months, much more so than in the national economy. During the last four months the state has lost jobs at a 1.4% annual rate compared to 6.5% during the six months prior to that... We continue to believe that the state economy will shed jobs through the fourth quarter of 2009, with moderate job growth resuming in 2010. The Washington recovery, like the national recovery, will be slow and U-shaped.

The state's unemployment rate also appears to be leveling off in recent months after rising sharply late last year and early this year... Employment is expected to fall further while the labor force continues to grow. But we now expect the unemployment rate to peak at 9.8% which is significantly lower than the 10.5% peak we had projected in June. (ERFC 2009a)

The best economic news comes from outside the U.S., where the economies of many of the U.S.'s most important trading partners have begun to grow again. This bodes well for U.S. exports—and for Washington, which is the nation's most trade-dependent state.

While Washington's economy has closely tracked the June economic forecast, revenue collections have fallen short of the June revenue forecast. The total shortfall from June 11 to September 10 was \$86.0 million, 2.8 percent of the \$3.1 billion that had been forecast to be collected over the period. Weaker than expected consumer sales account for part of the shortfall, and state forecasters have reduced their forecast of retail sales growth in the near term. Recovery in revenue depends on an upturn in consumer spending.

BALANCE SHEET

The table on this page presents a near general fund-state balance sheet for the 2007–09 and 2009–11 biennia. We have based this balance sheet on the balance sheet published in the 2009 session edition of Legislative Budget Notes, which we have updated to reflect the June and September revenue forecasts.

The NGFS began the 2007–09 biennium with a \$2.1 billion balance. Revenues (net of the transfer to the budget stabilization account, the constitutionally established rainy day fund) were \$30.1 billion. NGFS resources were boosted by more than \$700 million transferred from other state accounts, including \$400 million from the budget stabilization account (BSA).

Coming into the 2009 session, NGFS appropriations for the 2007–09 biennium were a bit less than \$33.7 billion. The “early action” and regular supplemental budget bills shaved about \$1.1 billion from NGFS appropriations for the biennium. Much of this reduction in appropriations from the general fund was backfilled with federal stimulus funds, as indicated in the addendum at the bottom of the table, so that the overall de-

Estimated Revenues and Expenditures Near General Fund (Dollars in Millions)		
	2007-09	2009-11
RESOURCES		
Beginning Fund Balance	2,105.2	387.7
Revenue		
June Forecast	30,250.6	30,209.7
September Revision	(0.3)	(230.0)
Transfer to Budget Stabilization Account	(115.1)	(268.8)
Total Revenue	30,135.2	29,710.9
Other Resource Changes		
2007 & 2008 Fund Transfers	117.1	-
ESHB 1694 Fund Transfers	91.3	-
Use Budget Stabilization Account	400.0	45.1
Use Capital Budget Resources	77.0	700.1
Other Fund Transfers	24.5	146.7
Other Changes	18.9	1.0
Total Other Resource Changes	728.8	892.9
Total Revenues and Resources	32,969.2	30,991.5
EXPENDITURES		
Spending		
2007-09 Budget As Enacted Prior to 2009 Session	33,655.2	
2008 Actual Spending Adjustment	(15.6)	
ESHB 1694 (Early Action, 2009)	(634.7)	
2009 Supplemental	(423.4)	
Enacted 2009-11 Budget		31,388.6
Total Appropriations	32,581.5	31,388.6
RESERVES		
Ending Balance & Reserves		
Unrestricted Ending Fund Balance	387.7	(397.1)
Budget Stabilization Account Balance (Includes Interest)	21.4	245.2
Total Reserves	409.1	(151.9)
Addendum:		
Expenditures of Federal Stimulus Funds	910.7	2,528.3
NGFS Appropriations + Expenditures of Stimulus Funds	33,492.2	33,916.9

Sources: LEAP, ERFC, OFM; WRC calculations

The Near General Fund

Sound fiscal policy minimizes the amount of tax earmarking.

The Research Council has long lamented the proliferation of special accounts through which the legislature has funded general government programs (WRC 1995). In recent years, eight specific accounts (the "general fund related accounts") have functioned as adjuncts to the general fund: the health services account, the student achievement account, the education legacy trust account, the public safety and education account and its equal justice sub-account, the violence reduction and drug enforcement account, the water quality account, and the pension funding stabilization account. Monies have been freely transferred back and forth between these accounts and the general fund as needs arise. In 2006, the Washington Alliance for a Competitive Economy, of which we are a member, called for these accounts to be consolidated into the general fund (WashACE 2006).

For several years, legislative fiscal staffs have been reporting state spending in terms of a synthetic "account," the near general fund–state (NGFS), which aggregates the general fund and the eight related accounts. This has improved transparency and accountability, and we have generally chosen to use the NGFS in our discussions of the state budget (WRC 2007).

During the 2009 session, the legislature passed and the governor signed Senate Bill SB 5073, which consolidates six of the eight related accounts (all but the education legacy trust account and the pension funding stabilization account) into the general fund. We applaud this, but believe that the education legacy trust account should likewise be consolidated into the general fund. (As no taxes are dedicated to it, the pension funding stabilization account is effectively dead.)

crease in spending was around \$160 million.

Appropriations from the NGFS exceeded revenue by \$2.4 billion, and the NGFS ended the biennium with a balance of less than \$400 million.

Forecast revenues for the 2009–11 biennium (net of the required transfer to the BSA) are now \$29.9 billion. These revenues are supplemented by nearly \$900 million in transfers to the NGFS from other state funds, including \$45 million from the BSA.

Appropriations from the NGFS 2009–11 total a bit less than \$31.4 billion for 2009–11. In addition to these appropriations, the state anticipates spending \$2.5 billion in federal stimulus funds during the biennium.

The projected balance in the NGFS at the end of the biennium is negative \$397.1 million.

THE CHALLENGE

With this forecast, the state's budget is significantly out of balance. The problem, however, does not appear large enough to require the Legislature to meet in special session prior to the regularly scheduled 2010 session. Following the June forecast, Governor Gregoire directed state agencies under her control to decrease general fund employee costs by 2 percent and to maintain controls on spending for equipment pur-

chases, out-of-state travel and personal service contracts. Savings from these actions, which might total \$200 to \$300 million, are not included in the balance sheet. But on the other hand, the balance sheet does not include cost increases of comparable magnitude due to the June caseload forecast.

At the press briefing that followed the close of the Forecast Council meeting, OFM Director Victor Moore was reluctant to put a precise number on the amount by which 2009–11 spending needs to be cut, saying that it all will depend on the November revenue and caseload forecasts. When pressed by a reporter, however, Moore gave a range of \$500 million to \$1 billion.

Looking into the more distant future, the state faces a significant budget gap in the 2011–13 biennium. In the current biennium the state is using \$2.5 billion in federal stimulus funds to pay for programs that would normally be funded from the NGFS. The combined total of NGFS and federal stimulus fund spending, \$33.9 billion, exceeds NGFS revenue by \$4.2 billion. Projecting forward using normal growth rates in revenue and program costs suggests a 2011–13 budget gap in the \$2.0 billion to \$2.7 billion range.

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