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BRIEFLY

At its March meeting, the Economic and Revenue Forecast Council decreased the baseline revenue forecast by \$79.8 million for 2009-11 and \$698.4 million for 2011-13.

In addition, reflecting the turmoil in the Middle East and the earthquake in Japan, the Forecast Council increased its estimate of the probability that the economy will fall back into recession to 20 percent.

MARCH FORECAST: REVENUE DOWN, UNCERTAINTY UP

Yesterday the state Economic and Revenue Forecast Council (ERFC) reduced the forecast of general fund–state revenues for the current 2009–11 biennium by \$79.8 million to \$28.047 billion and the forecast for the 2011–13 biennium by \$698.4 million to \$31.907 billion.

Following the Forecast Council meeting, Office of Financial Management Director Marty Brown estimated the gap in the 2009–11 general fund–state budget to be \$201 million and that for the 2011–13 budget to be \$5.1 billion.

With the March update to the general fund state revenue forecasts, legislators should accelerate work on writing the 2011–13 budget. Counting today, 38 days remain in the 105-day regular session.

Economic Outlook

Arun Raha, Executive Director of the Economic and Revenue Forecast Council, began his presentation with this observation concerning the high level of uncertainty in the current environment:

The economic outlook remains clouded with a great deal of uncertainty. Recent geopolitical developments have cast yet another shadow over the economic recovery. First we had the volatility in oil prices because of the political unrest in the Middle East. Now we have the tragedy in Japan, the world's third largest economy and one of the state's leading trading partners. It is a fluid and fast changing situation.

The EFRC is required by state law to prepare three forecasts each quarter: a baseline forecast, which represents the most likely path of the economy and state revenue, is bracketed by optimistic and pessimistic forecasts. Reflecting increased uncertainty due to the developments in the Middle East and Japan, the probability attached to the pessimistic forecast (under which the economy falls back into recession) increased to 20 percent from the 15 percent it carried in November. The probability of the optimistic scenario was unchanged at 10 percent, while the probability of the baseline dropped from 75 percent to 70 percent.

Since the last forecast in November, the baseline outlook for the national economy has actually improved a bit. National GDP is now forecast to grow by 3.1 percent for 2011 and 3.3 percent for 2012, compared to 2.5 percent and 3.2 percent, respectively, in the November forecast, while average unemployment rates are 8.5 percent for 2011 and 7.7 percent for 2012, compared to 9.3 percent and 8.3 percent.

Big pieces of positive news for the national economy since November included 4th quarter GDP growth (2.8 percent according to the most recent estimate), stronger than expected holiday sales, and the federal tax cuts enacted in December.

The biggest negatives are the turmoil in the Middle East (with the associated increase in the price of oil) and the earthquake in Japan.

For Washington, the new baseline forecast shows stronger personal income growth, compared to the November baseline. The new forecast for employment is slightly weaker than the old, however.

For 2011 personal income growth is now forecast to be a robust 5.4 percent, as compared to the 3.7 percent in November forecast. Some of the gain is given back in 2012, where the forecast is reduced to 4.7 percent from 5.1 percent.

The state is now expected to add 31,000 jobs in 2011 and 74,000 in 2012. The November forecast pegged job growth at 34,000 for 2011 and 76,000 for 2012. Consequently, the forecast unemployment rates, 9.0 percent for 2011 and 8.1 percent for 2012, are 0.1 percent higher under the new forecast than they had been under the November forecast.

Boeing’s victory in the competition for the contract to build tankers for the air force is another positive, although most of the impact on jobs will not be felt until after the 2011–13 biennium.

Revenue Forecast

The baseline, optimistic and pessimistic revenue forecasts for 2009–11 and 2011–13 are shown in the table below.

Over the four months since the ERFC issued its November forecast, collections totaled \$84.7 million (1.8 percent) less than expected. The shortfall would have been larger, around \$110 million, if the Department of Revenue had not shifted a number of taxpayers from quarterly to monthly payment status.

The new baseline forecast is that general fund–state revenues for the 2009–11 biennium will total \$28.047 billion, \$79.8 million less than the November baseline. In addition to the shortfall over the last four months, economic factors are expected to reduce revenue by \$105.8 million over the remainder of the biennium. Offsetting this, the tax amnesty program enacted in December, increased audit and collection efforts aimed at out-of-state taxpayers and other non-economic factors are expected to increase revenue by \$110.7 million.

The optimistic 2009–11 forecast provides \$120 million (0.4 percent) more than the baseline; the pessimistic forecast provides \$160 million (0.6 percent) less than the baseline.

The new baseline forecast for the 2011-13 biennium, \$31.907 billion, is \$698.4 million less than the November baseline. Of this reduction, \$30.1 million is revenue pulled forward to the current biennium due to the amnesty program, while the remaining \$668.3 million is due to economic factors.

The optimistic 2011–13 forecast provides \$2.325 billion (7.3 percent) more than the baseline; the pessimistic, \$2.486 billion (7.8 percent) less.

Budget Gap

The 2009–11 balance sheet distributed at the EFRC meeting shows, with the revised forecast, a deficit of \$78.8 million for the biennium. OFM director Marty Brown has stated that necessary maintenance level changes to biennial appropriations would increase the gap to \$201 million.

March Forecasts of General Fund–State Revenue for 2009–11 and 2011–13

| | Probability | 2009-11 | 2011-13 |
|-------------|-------------|------------------|------------------|
| Baseline | 70% | \$28.047 billion | \$31.907 billion |
| Optimistic | 10% | \$28.167 billion | \$34.231 billion |
| Pessimistic | 20% | \$27.887 billion | \$29.421 billion |

In December, the governor's budget staff calculated a shortfall of \$4.6 billion for the 2011-13 biennium ([WRC 2010](#)). (This calculation assumes a no beginning balance for the general fund–state and a \$900 million ending balance; accepting a lower ending balance would reduce the shortfall.) The reduced baseline forecast of 2011–13 revenues combined with the new case-load forecast (which decreases the projected expenditures for various education and human service programs by \$209 million) increase the \$4.6 billion gap to \$5.1 billion.

Discussion

In recent weeks, news sources have reported that legislators are considering a range of budget gimmicks including a twenty-fifth month (i.e. counting taxes received in July of 2013 as 2011–13 revenue) and securitization (selling bonds with the revenue from an existing source to repay the loan). The increased uncertainty in the economic environment, as signaled by the higher probability that the ERFC has given to the pessimistic forecast, makes it even more important that the 2011–13 budget gap not be closed with such gimmicks. As Gov. Chris Gregoire said in her press conference following the release of the March forecast, “We can’t rely on short-term solutions. Short-term solutions may cause less pain now, but we need a budget that is both sustainable and long-term.”

Reference

Washington Research Council (WRC). 2010. Governor Gregoire's 2011–13 Budget Proposal. PB 10-25. December 24.