

FIFTH ANNUAL ECONOMIC FORECAST SUMMIT

Budget & Economic Update

INDEPENDENT FISCAL OFFICE
FEBRUARY 28, 2017

Independent Fiscal Office

- ▶ **Similar to the Congressional Budget Office.**
 - Supply non-partisan analysis.
 - No governing board. Separate from legislature.
- ▶ **Our primary duties:**
 - General Fund Revenue Estimate: May 1 & June 15.
 - Five-Year Economic & Budget Outlook: Nov. 15.
 - Actuarial analysis of pension legislation.
 - Special studies at request of General Assembly.
- ▶ **Office makes NO policy recommendations.**

Projected Budget Deficit

	2015-16	2016-17	2017-18	Growth
Begin Balance	\$275	\$2	-\$936	
Revenue Available	29,855	30,994	31,309	1.0%
Expenditures	30,127	31,931	33,410	4.6%
Ending Balance	\$2	-\$936	-\$3,037	

Note: millions of dollars.
 Source: FY 2017-18 Executive Budget presentation, Feb. 7, 2017. Excludes all policy initiatives.

Proposed Deficit Reduction

	2-Year Impact
Revenue Package	\$1,006
Revenue Enhancements	304
Loans or Leasebacks	335
Gaming Expansion	250
Reduce Tax Credits	100
Consolidation/Closures/Complement	351
2016-17 DHS Savings	165
Pupil Transport Savings & U. Penn Approp.	82
Miscellaneous Efficiency Savings	<u>451</u>
Total Change to Balance Sheet	\$3,043

Note: millions of dollars.
Source: FY 2017-18 Executive Budget and Feb. 7, 2017 budget presentation.

The Revenue Package

2017-18

Broaden Tax Base

Sales – Custom Programming	\$330
Sales – Storage and Aircraft	160
Insurance Premiums Tax	142

Tax Reform

Corporate – Combined Reporting	0
Corporate – Rate Reduction	0
Corporate – NOL Threshold	81

New Severance Tax – 6.5% 294

TOTAL **\$1,006**

Note: millions of dollars. The combined reporting and lower corporate tax rate (6.49%) proposals are effective or phased-in beginning 1/1/19. Source: FY 2017-18 Executive Budget.

PA Economics and Demographics

	Annual Growth Rate					
	2011	2012	2013	2014	2015	2016
Real GDP	1.3%	1.6%	1.9%	1.8%	2.8%	0.7%
Net Job Gains (000s)	64.7	39.9	14.7	47.6	48.6	43.5
Wages and Salaries	3.9%	3.7%	1.8%	3.9%	4.0%	2.5%

Source: Data from the U.S. Bureau of Economic Analysis, U.S. Bureau of Labor Statistics and U.S. Census Bureau.

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Philadelphia CPI-U	2.7%	1.8%	1.2%	1.3%	-0.1%	0.6%
Social Security COLA	0.0%	3.6%	1.7%	1.5%	1.7%	0.0%

Source: Data from the U.S. Bureau of Economic Analysis, U.S. Bureau of Labor Statistics and U.S. Census Bureau.

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Age 0-19	-0.9%	-1.0%	-1.0%	-0.8%	-0.6%	-0.6%
Age 20-64	0.6%	-0.1%	-0.1%	-0.1%	-0.3%	-0.6%
Age 65+	0.8%	3.3%	2.3%	2.1%	2.2%	2.2%
Total Population	0.3%	0.2%	0.1%	0.1%	0.1%	-0.1%

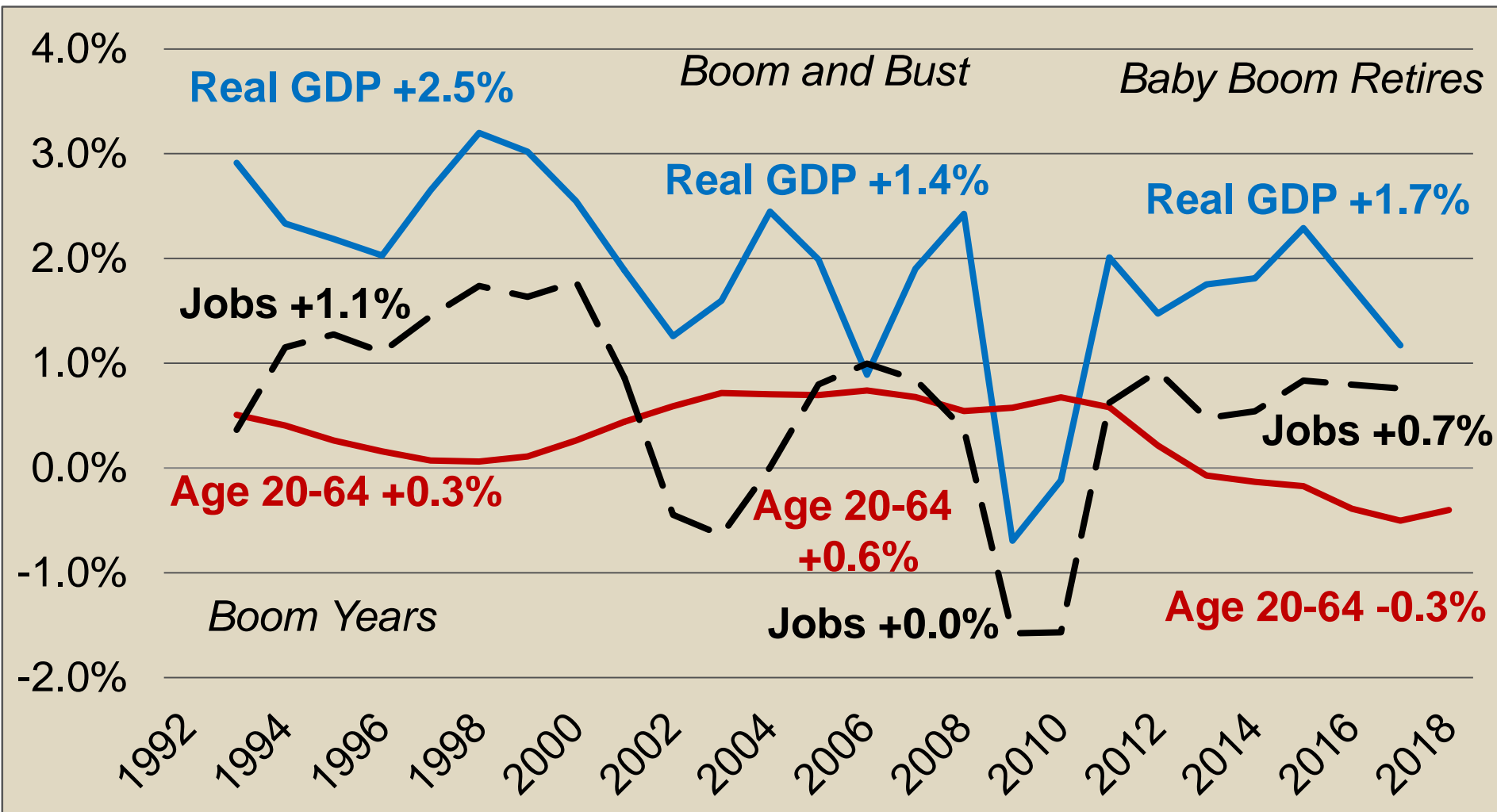
Source: Data from the U.S. Bureau of Economic Analysis, U.S. Bureau of Labor Statistics and U.S. Census Bureau.

Service Sector Adds Jobs (000s)

	2008	2016	Change	Percent
Manufacturing	644	566	-78	-12.1%
Local Government	493	448	-45	-9.1%
Construction	254	234	-20	-7.9%
Wholesale-Retail	883	864	-19	-2.1%
All Other Sectors	1,286	1,274	-11	-0.9%
Professional Services	317	345	28	8.8%
Food Service-Accomm.	417	460	44	10.5%
Healthcare	875	978	102	11.7%
Transportation-Storage	240	270	29	12.2%
Admin-Management	<u>392</u>	<u>442</u>	<u>50</u>	<u>12.7%</u>
Total Employment	5,800	5,880	80	1.4%

Source: U.S. Bureau of Labor Statistics. Data for 2016 are preliminary.

PA Economy Downshifts



Source: U.S. Bureau of Economic Analysis, U.S. Bureau of Labor Statistics and U.S. Census Bureau. Growth rates are two-year averages.

Revenues Weak Through February

	Actual Amounts			Base Amounts	
	2016-17	Change	Growth	Change	Growth
Total General Fund	\$17,973	\$218	1.2%	-\$9	-0.1%
Corporate Net Income	1,281	-136	-9.6%	-94	-6.6%
Capital Stock	35	-71	-67.0%	0	n.a.
Sales - Non-Motor	5,712	86	1.5%	60	1.1%
Sales - Motor Vehicle	884	12	1.3%	12	1.3%
Pers. Inc. - Withholding	6,253	98	1.6%	201	3.3%
Pers. Inc. - Other	1,269	-62	-4.7%	-68	-5.1%
Tobacco Taxes	859	264	44.5%	-36	-6.0%
Inheritance	598	-6	-1.1%	-6	-1.1%
Realty Transfer Tax	310	-15	-4.7%	-3	-0.8%
All Other	770	49	6.9%	-75	-10.5%

Note: millions of dollars. Slide has been updated to reflect February's actual collections. Base amounts control for tax law changes (e.g., cigarette tax) and timing issues.

Gaming Trends Also Weak

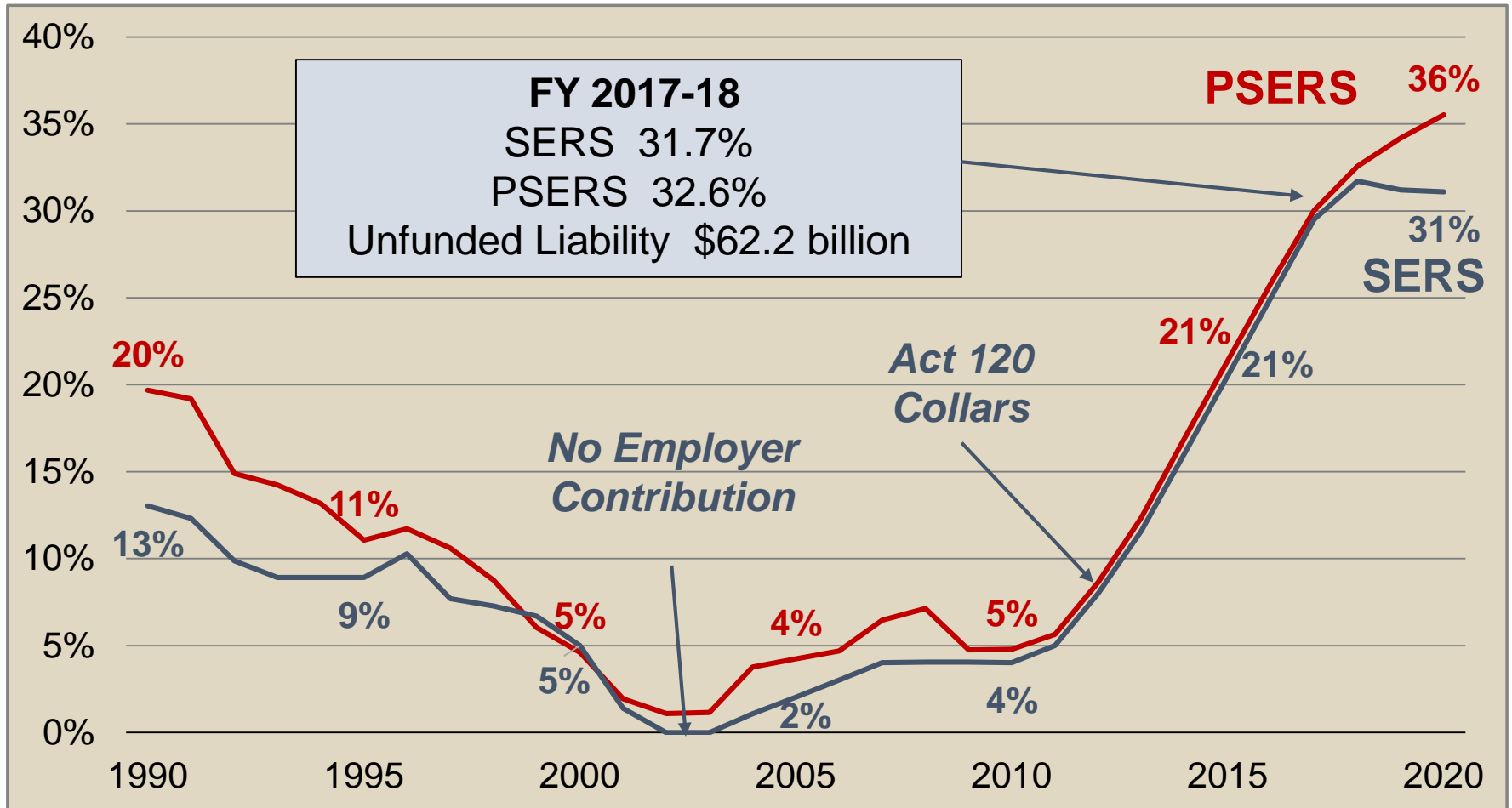
	Dollar Amounts			
	2013-14	2014-15	2015-16	2016-17
Slots Tax Revenues	\$1,289	\$1,296	\$1,325	\$1,293
Table Games Revenues	105	112	120	122
Lottery Sales	3,800	3,820	4,135	4,050
Instant Tickets	2,445	2,592	2,793	2,809
Numbers and Lotto	1,355	1,228	1,342	1,241
Annual Growth Rate				
Slots Tax Revenues	-4.8%	0.6%	2.2%	-2.4%
Table Games Revenues	2.3%	6.5%	6.7%	1.6%
Lottery Sales	2.7%	0.5%	8.3%	-2.1%
Instant Tickets	6.1%	6.0%	7.8%	0.6%
Numbers and Lotto	-2.9%	-9.4%	9.3%	-7.6%
Note: millions of dollars.				
Source: IFO forecast from Gaming Trends Research Brief, February 2017. Slots and table games revenues have not been reduced for \$45.3 million in CY 2016 refunds. Table games excludes impact of temporary rate increase for FY 2016-17.				

Budget Cost Drivers

	Dollar Amounts		Growth	
	2015-16	2016-17	2015-16	2016-17
Human Services	\$11,390	\$12,068	1.2%	6.0%
Education	10,382	10,733	-0.2%	3.4%
Corrections	1,963	2,059	2.6%	4.9%
Debt	1,128	1,111	2.8%	-1.4%
PSERS	1,719	2,064	48.5%	20.1%
SERS	665	787	24.8%	18.4%
All Other	<u>2,882</u>	<u>2,943</u>	<u>3.3%</u>	<u>2.1%</u>
General Fund	\$30,127	\$31,766	3.3%	5.4%

Note: millions of dollars.
 PSERS is Public School Employees' Retirement System and SERS is State Employees' Retirement System.
 Source: IFO Five-Year Outlook Reports and Executive Budgets.

Pensions – Employer Rates



Note: Employer contribution rates after FYE 2018 for PSERS and FYE 2017 for SERS are based on system projections. Unfunded liabilities are based on the valuation years used to determine the employer rates for FY 2017-18.

Fiscal and Economic Outlook

- ▶ **Short and long-term challenges.**
 - Current year shortfall approaches \$1.0 billion.
 - Long-run growth rate of expenditures > revenues.
- ▶ **Economic growth to remain subdued.**
 - Demographics dominate. Workforce may contract.
- ▶ **Budget requires close scrutiny.**
 - Certain programs grow automatically (healthcare and retirement).
 - Forward looking investments may comprise a smaller share: education, infrastructure and capital formation.
 - Also consider regular review of tax credits and tax expenditures.

Thank you.

Presentation available at www.ifo.state.pa.us