

Budget Status



House Finance Committee
November 24, 2008

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Introduction

- | State is facing major budgetary problems
- | First in series of hearings
- | Focus is on overall fiscal situation for current year, budget and outyears
 - u Economy
 - u Projections

Introduction

I Further hearings

- u December 1 – Staff Presentation: FY 2008 & FY 2009 Expenditure Issues
- u December 2 – Hearing on Overruns and Failed Initiatives: Budget Management, Monitoring and Accountability
- u December 3 – Hearing on Low Cost/No Cost Options for Recession-

Introduction

I House Fiscal Staff Estimates

- u Use November revenue and caseload conference estimates for FY 2009 and FY 2010
- u Use first quarter reports from agencies, Budget Office first quarter report, and staff estimates for FY 2009
- u Staff estimates for FY 2010 and beyond

Introduction

I House Fiscal Staff Estimates

- u Current year deficit estimate is larger than data reported to date –expenditure side
- u Budget year approximately \$25 million higher than Budget Office
- u Out years are being worked on to develop consistent methodology

Introduction

- | The state is in severe economic distress
- | It faces two problems
 - u A major current year \$366.8 million deficit
 - u Continued budget year and outyear issues growing from \$486 million to \$770 million
- | The two problems have different causes and likely require different approaches to solve them

Introduction

- u The **current year** deficit is a cyclical economic problem exacerbated by unmet expenditure savings
- u The **budget and out year** gaps are a function of both cyclical economic and continued structural issues



Economic Forecast

Economic Forecast

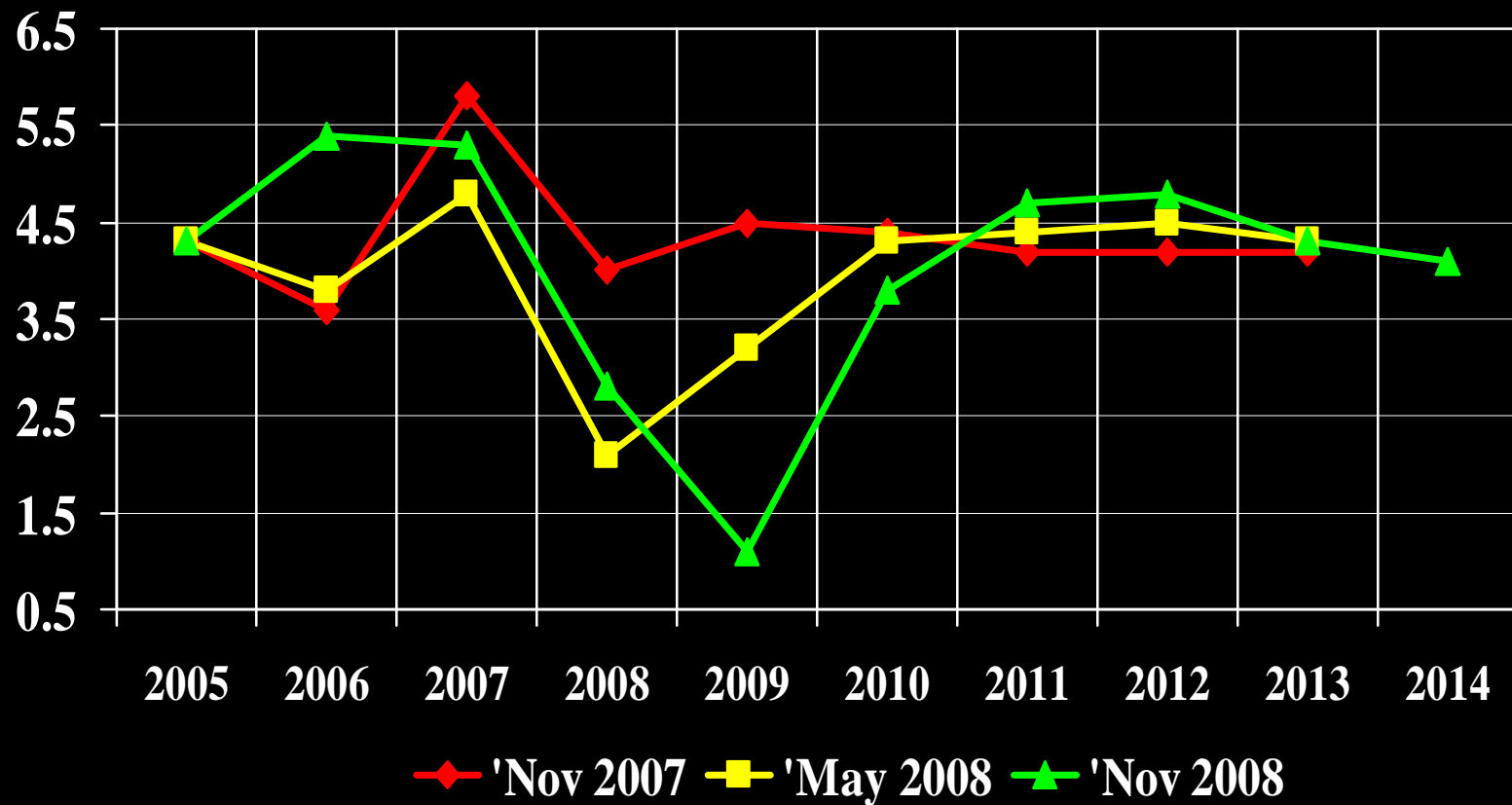
- | Revenue Estimating Conference adopts a consensus economic forecast
 - └ It takes testimony from two forecasting firms, Global Insight and Moody's Economy.com
 - └ The firms build U.S. macroeconomic models from which they derive their Rhode Island forecasts

Economic Forecast

- | The forecasts are considerably worse than last November and May
- | They even changed substantially between September and October
- | They assume \$200 billion federal economic stimulus with potential early 2009 impact

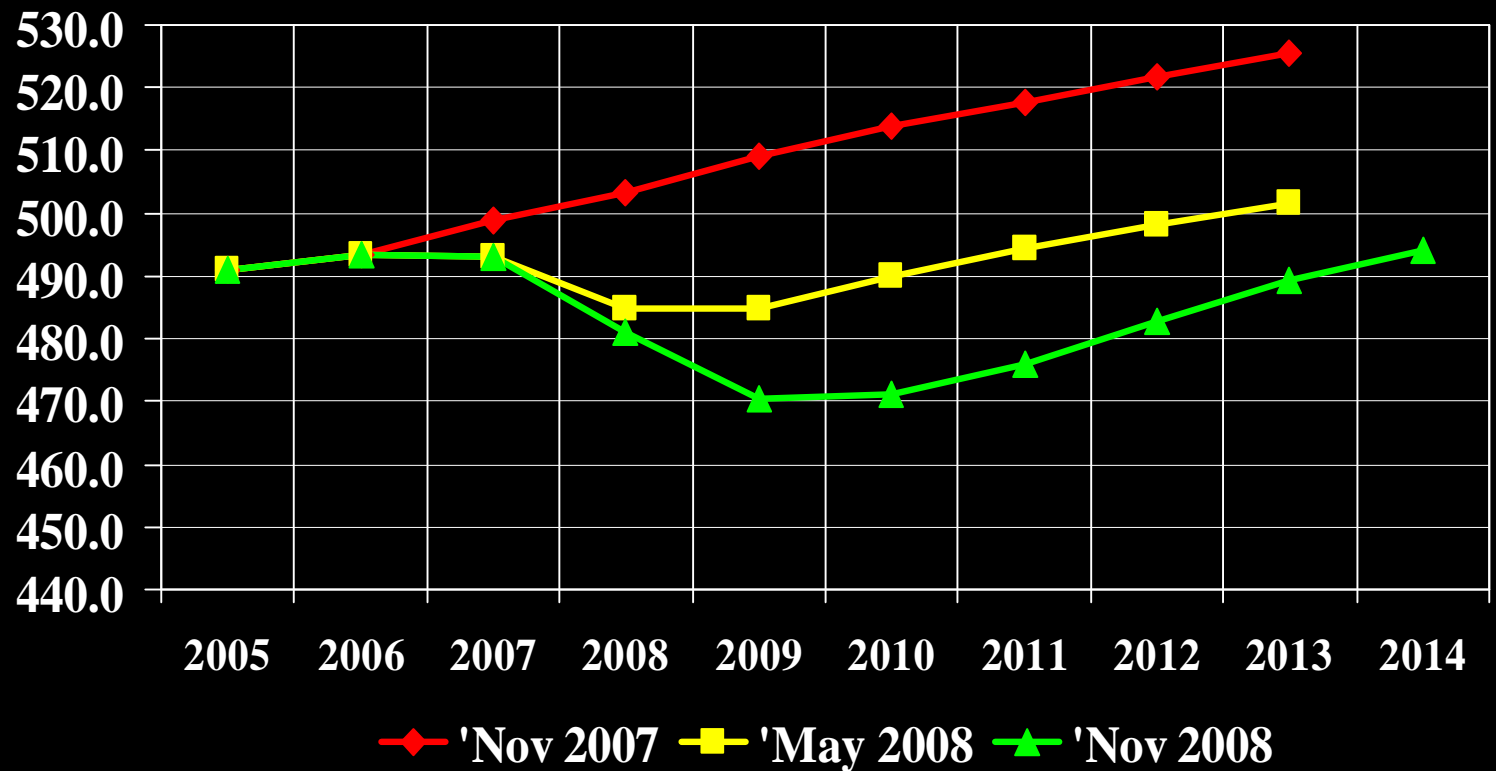
Consensus Economic Forecast

Forecast Differences - Personal Income Growth



Consensus Economic Forecast

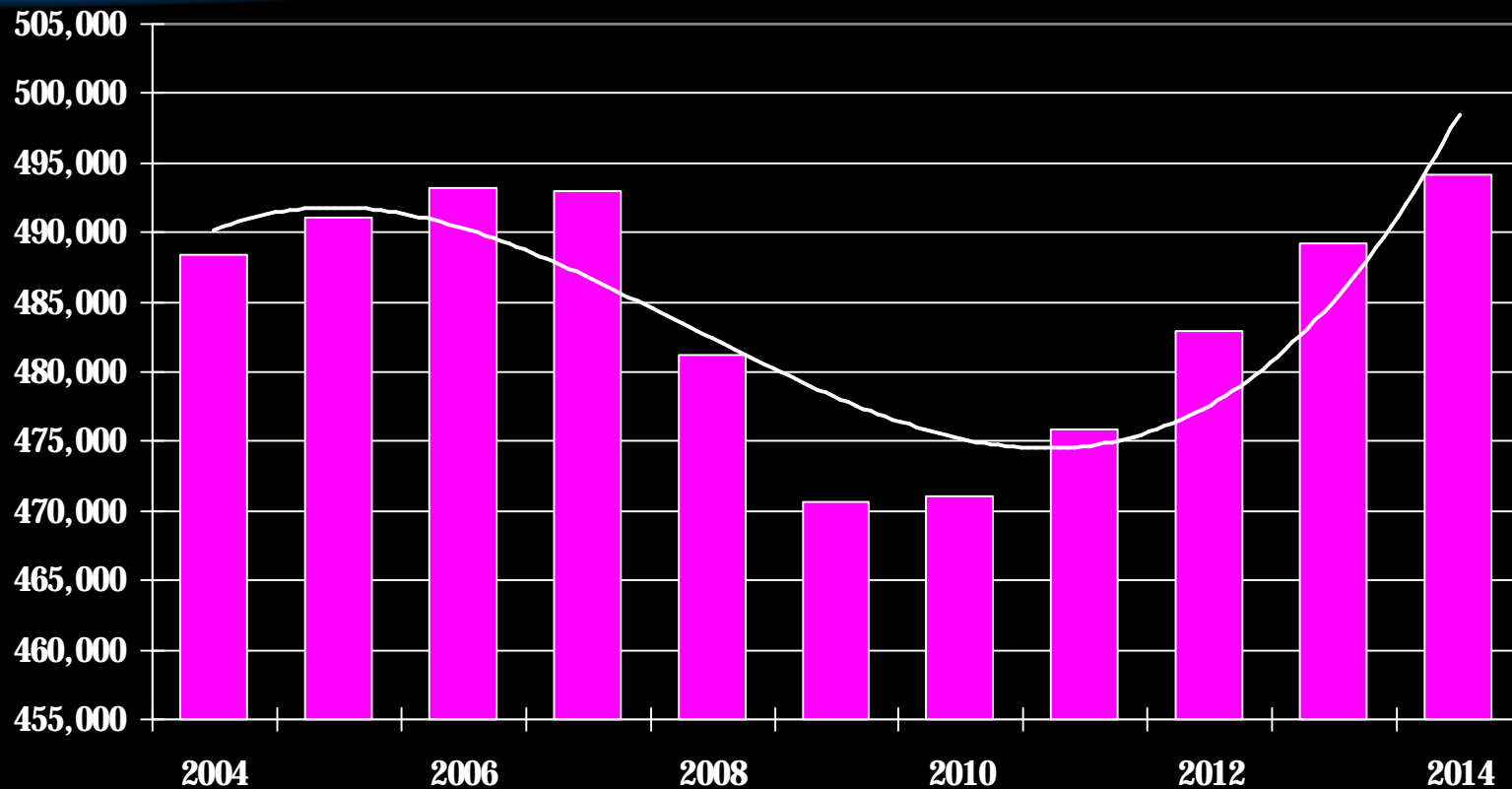
Forecast Differences - Jobs



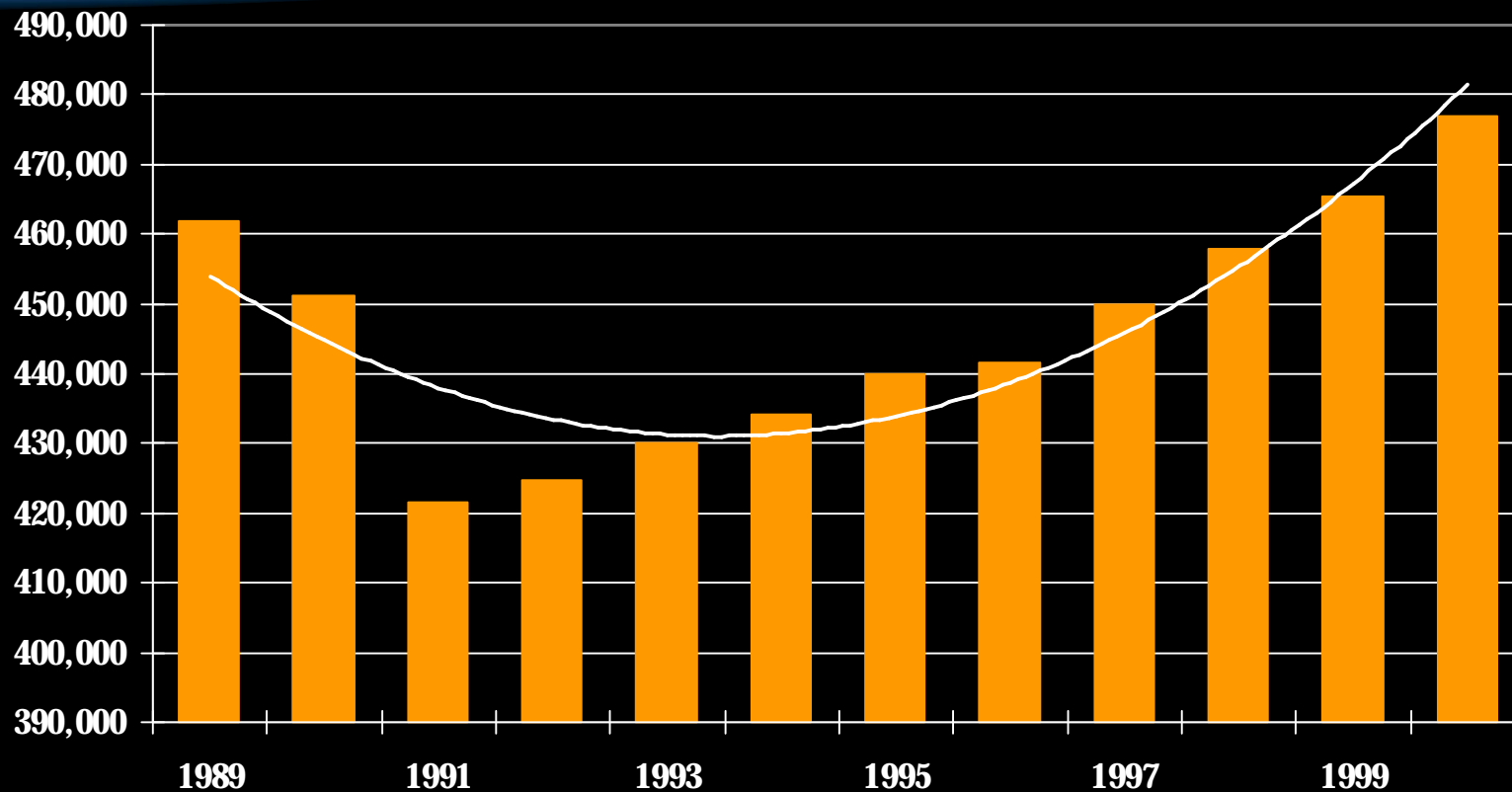
Employment – Unemployment



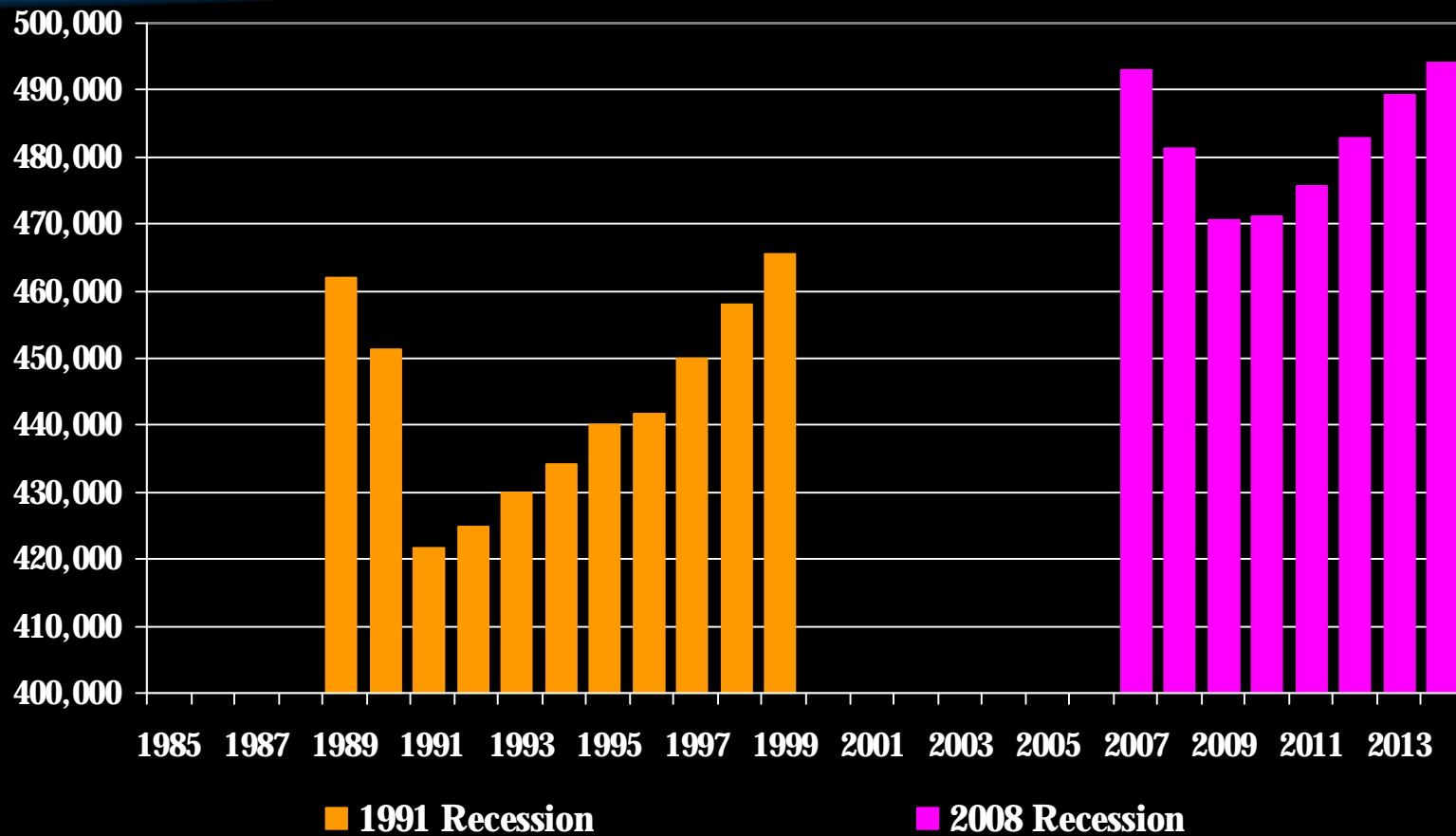
Jobs – 7 Years Peak to Peak



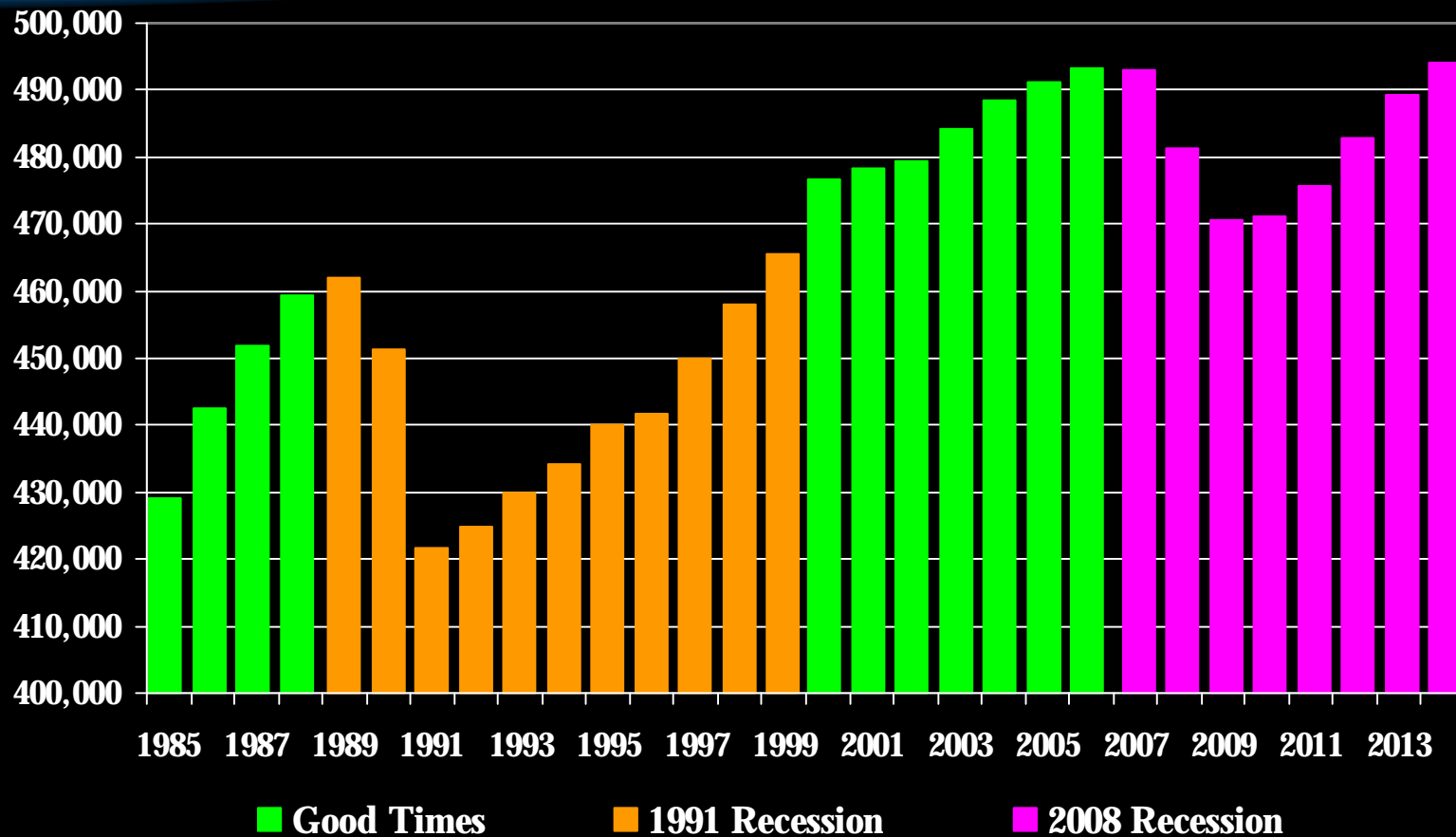
1991 – 10 Years Peak to Peak



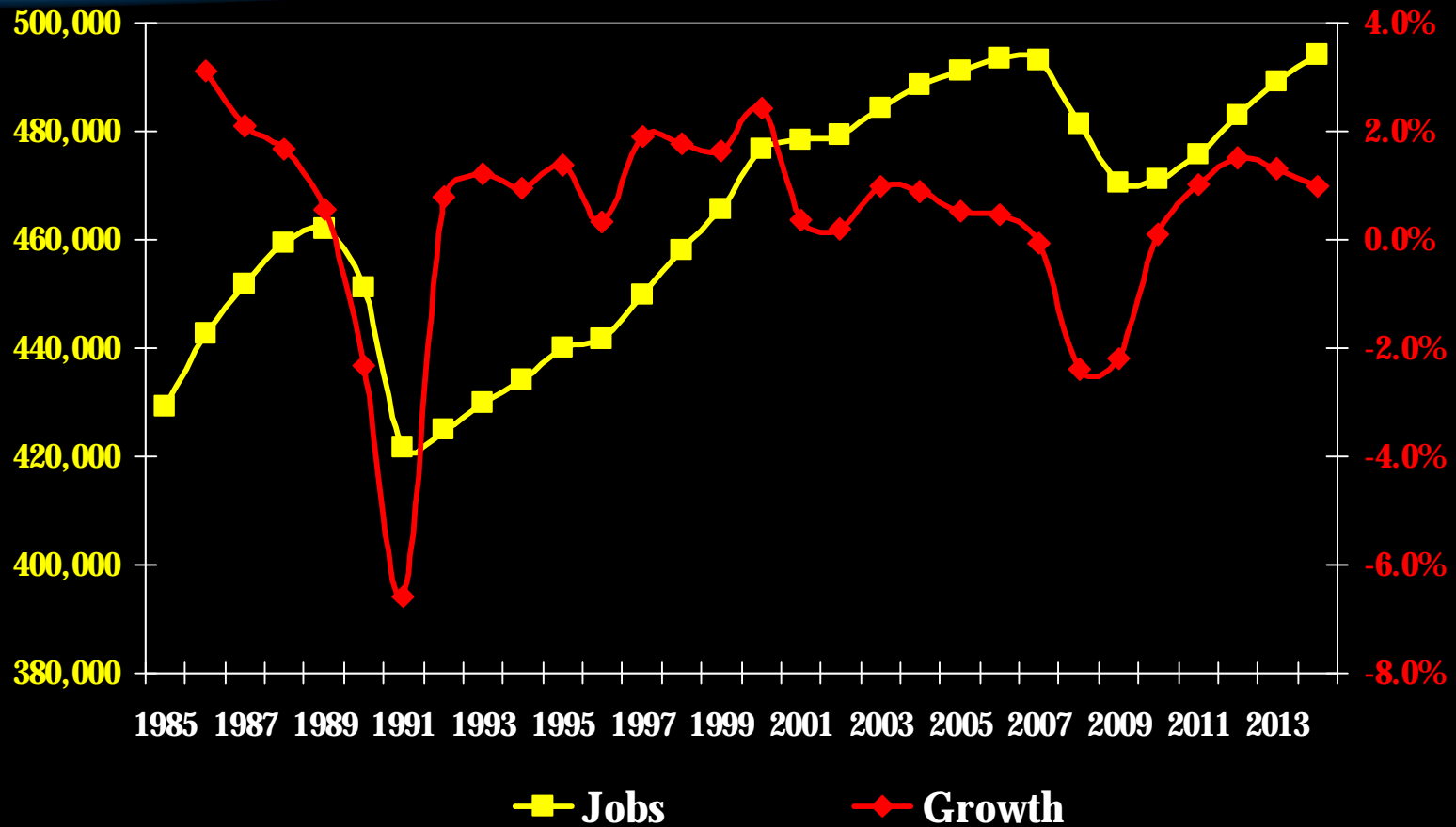
Jobs in the Recessions



Employment History

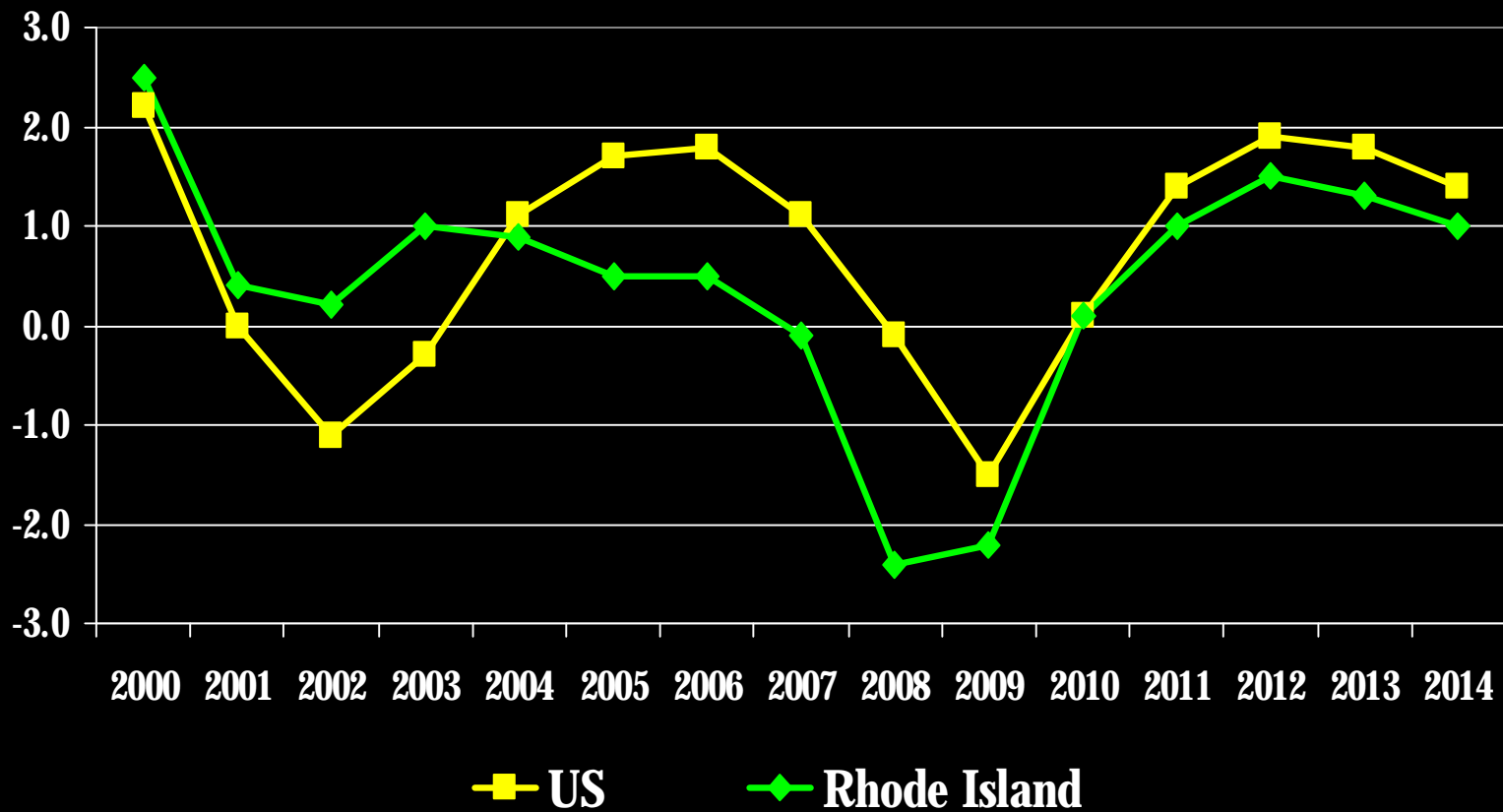


Employment Growth

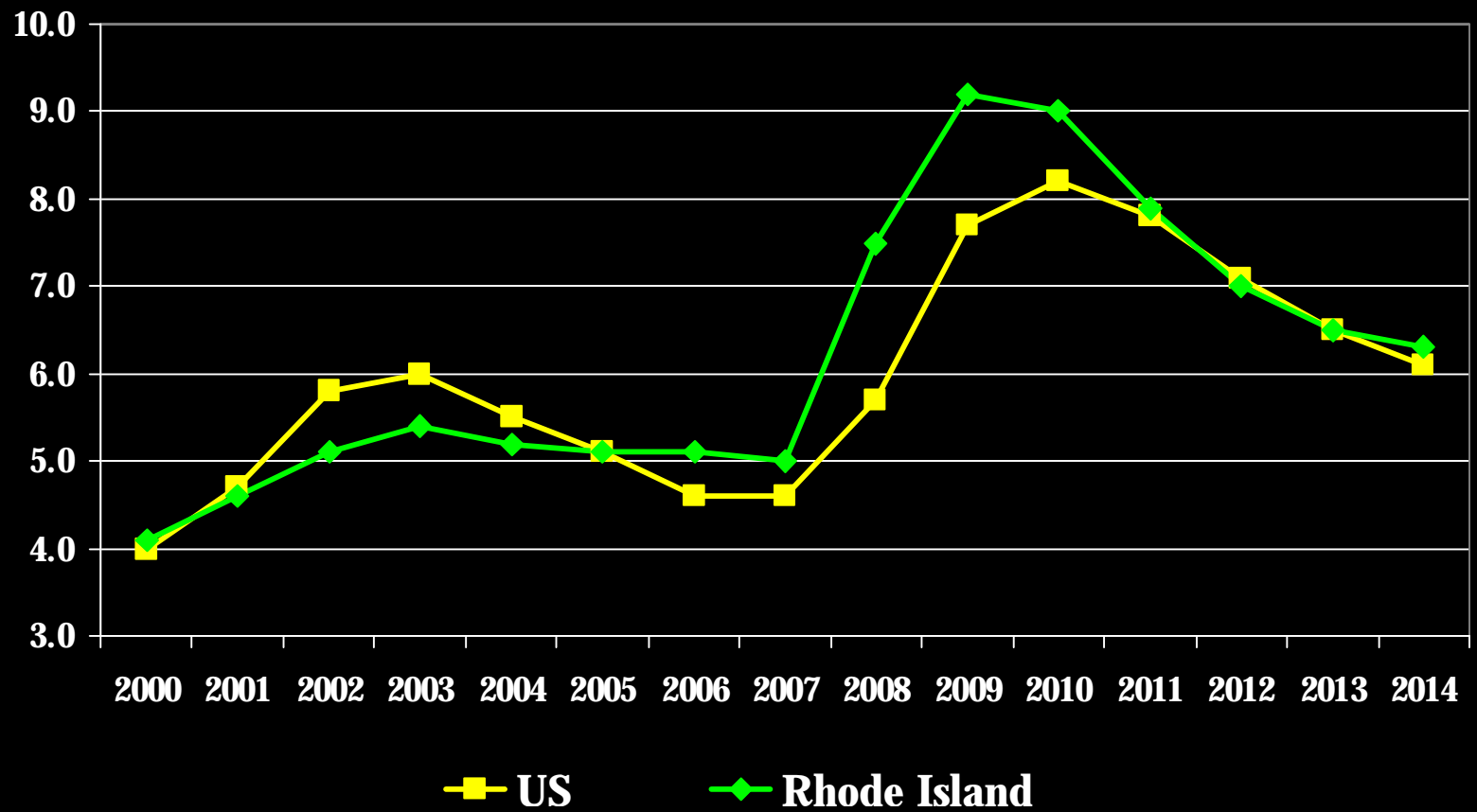


Employment Growth

Jobs Growth - RI Underperforms

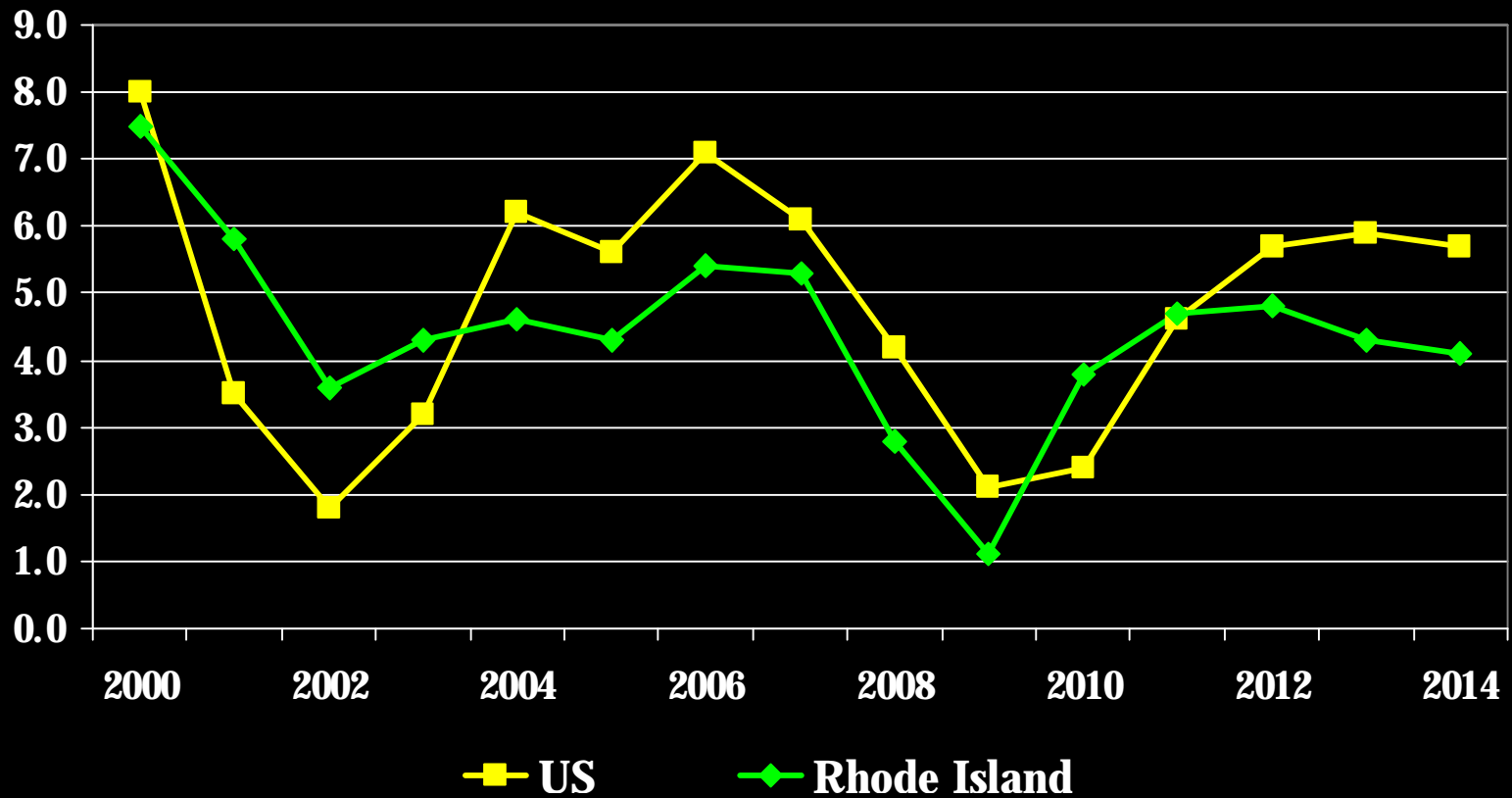


Unemployment Rates

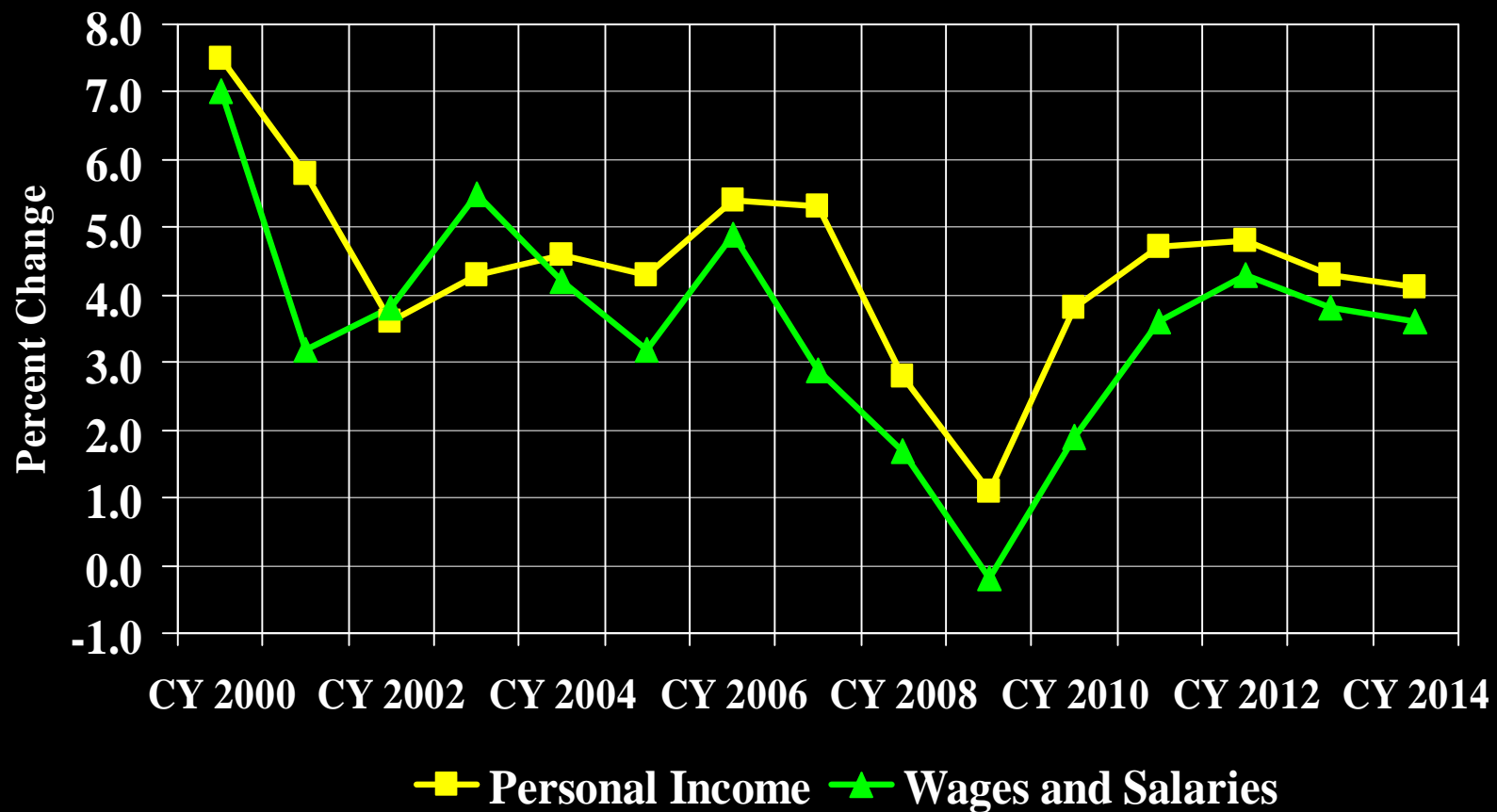


Revenues

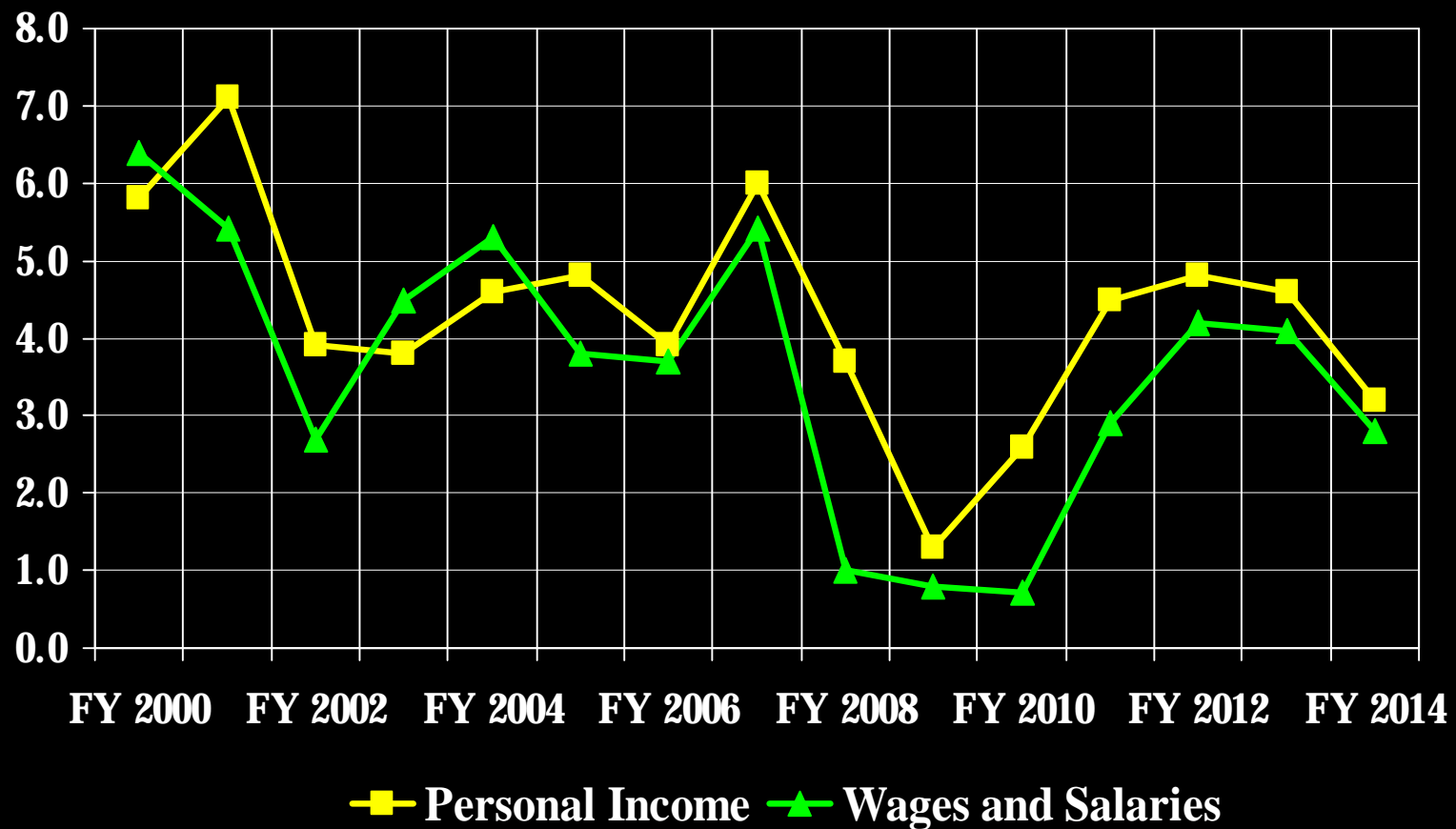
Personal Income Growth - RI Underperforms



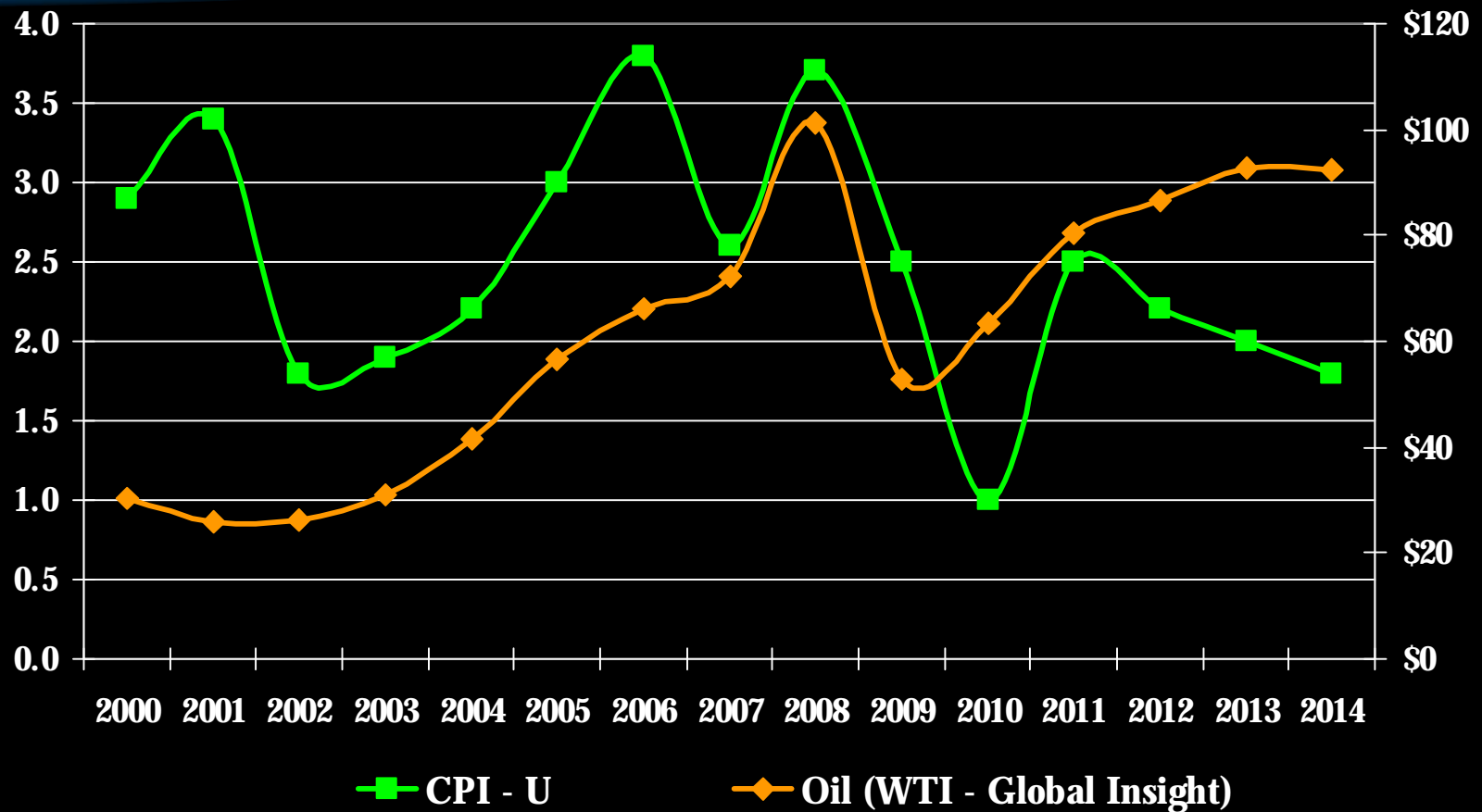
Revenue Drivers



Consensus Economic Forecast



Inflation and Oil Prices





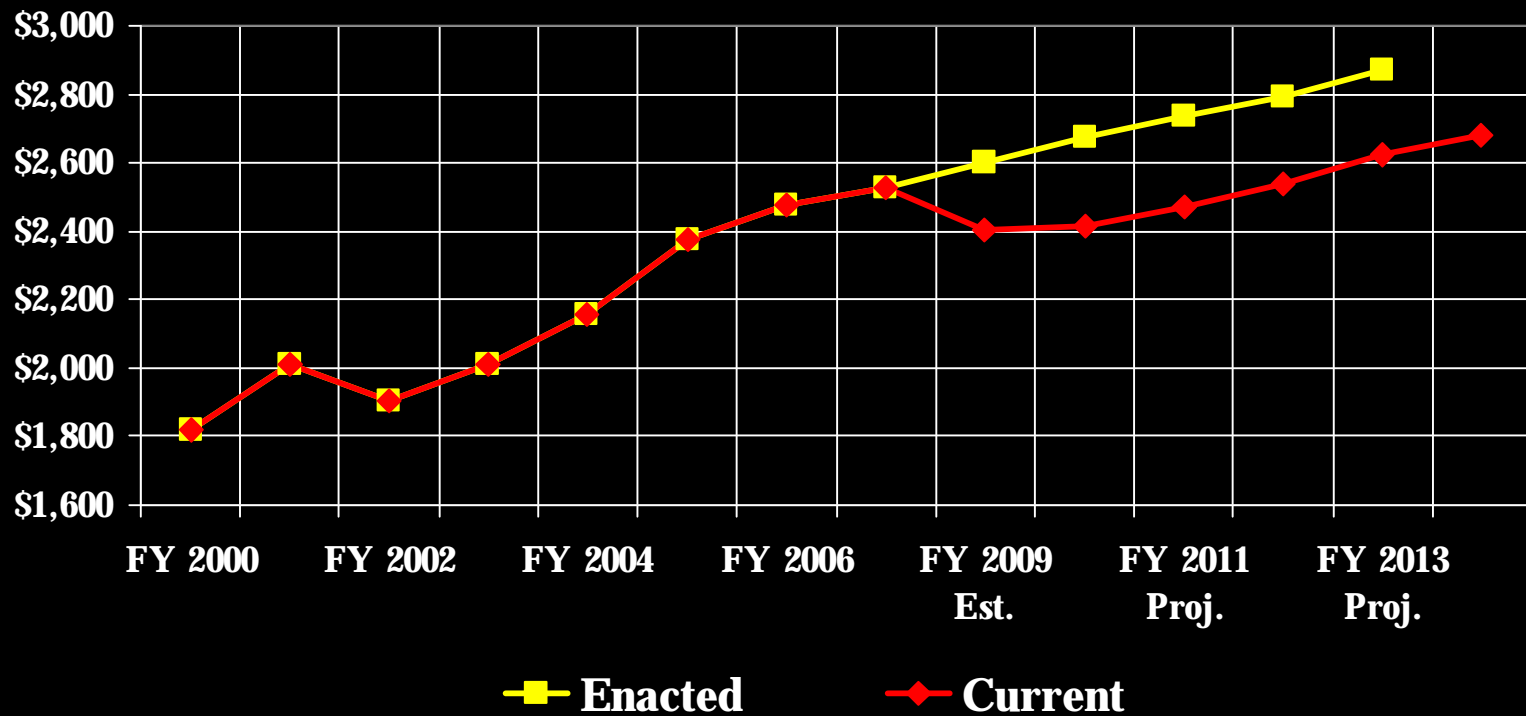
Revenues

Revenues

- | Revenue estimates are driven by trends, collections to date, and the economic forecasts
 - └ FY 2008 less than anticipated
 - └ FY 2009 collections lagging
 - └ Economic forecast significantly more pessimistic

Revenues

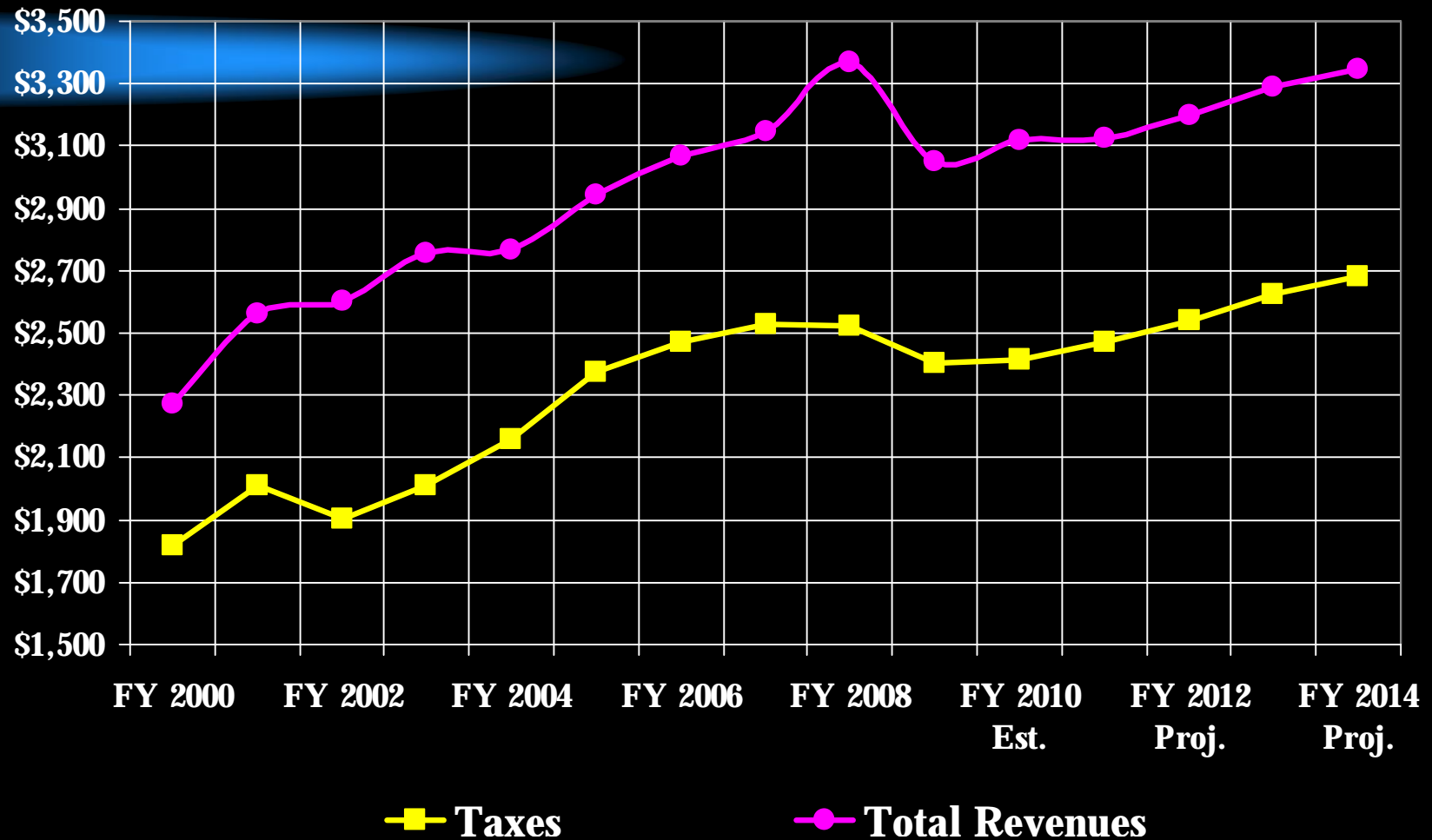
Slower Economy = Lower Tax Revenue



Revenues

- | Taxes generally make up nearly 80 percent of revenues
 - └ More susceptible to economy than other sources

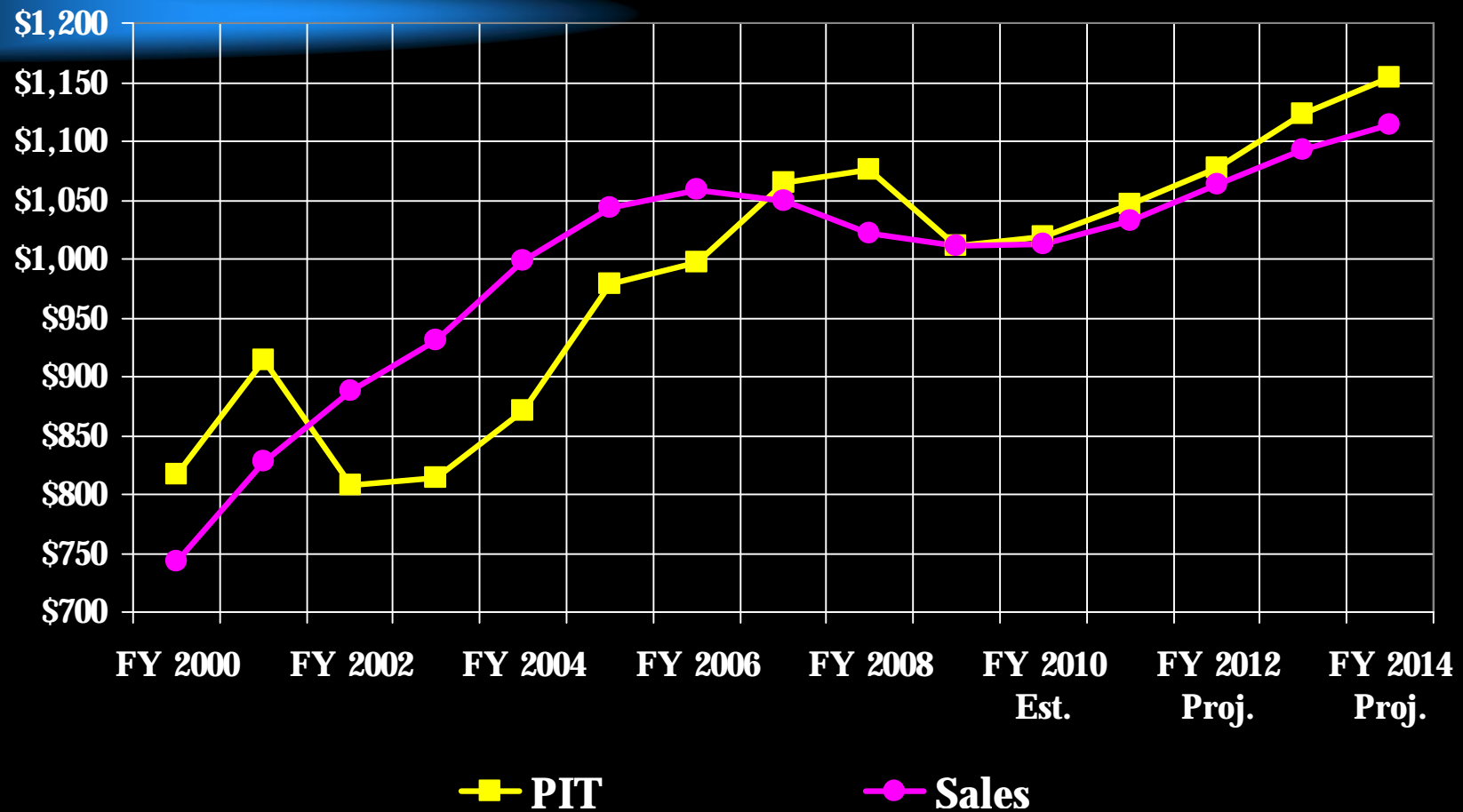
Revenues



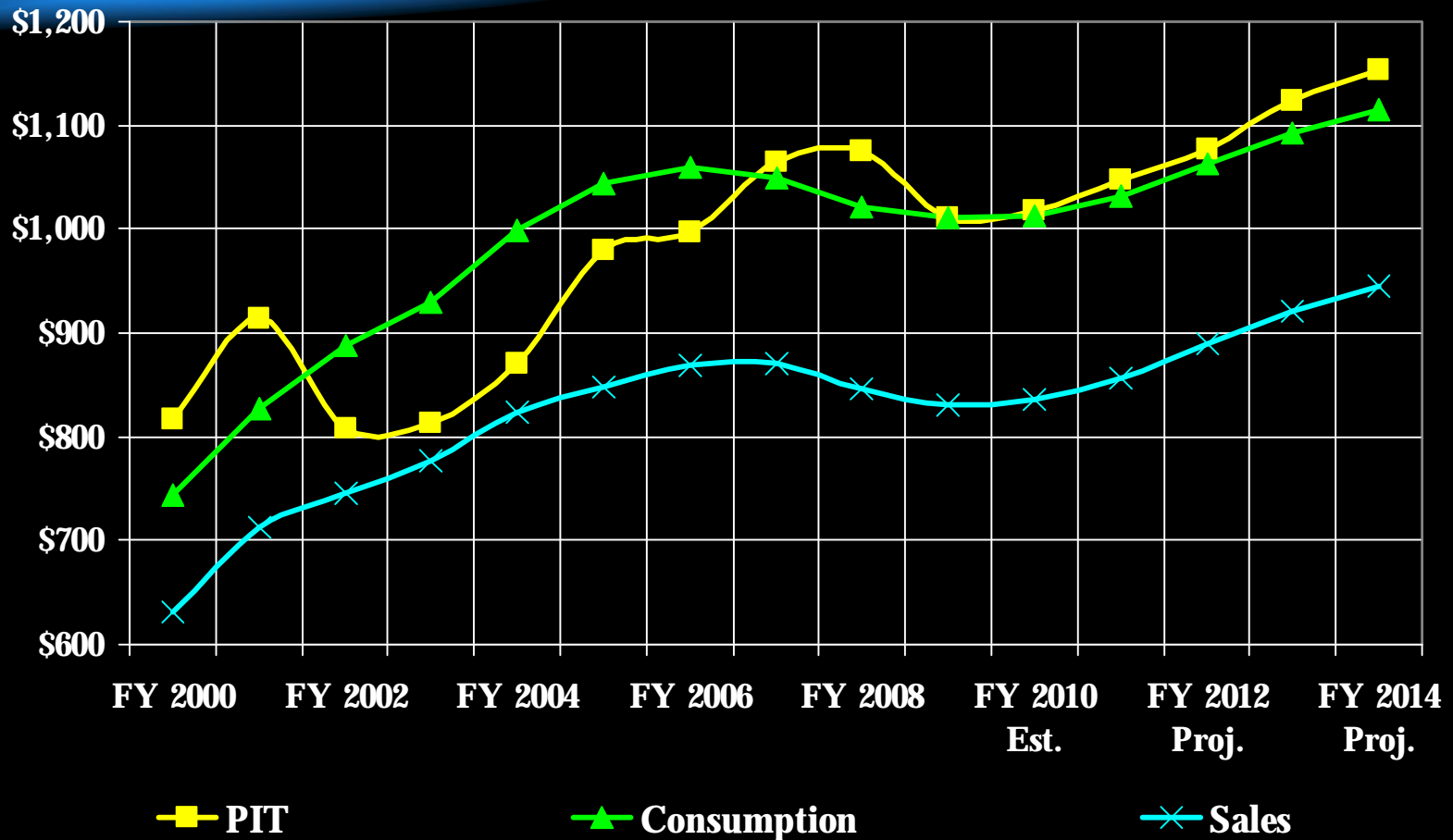
Revenues

- | Taxes generally make up nearly 80 percent of revenues
 - u More susceptible to economy than other sources
 - u In past, other miscellaneous sources have often backfilled when economy suffered (tobacco securitization, land sales)
- | Personal income and sales make up most of revenues
 - u 75% - 82% of tax revenue and 56% - 65% of total revenue

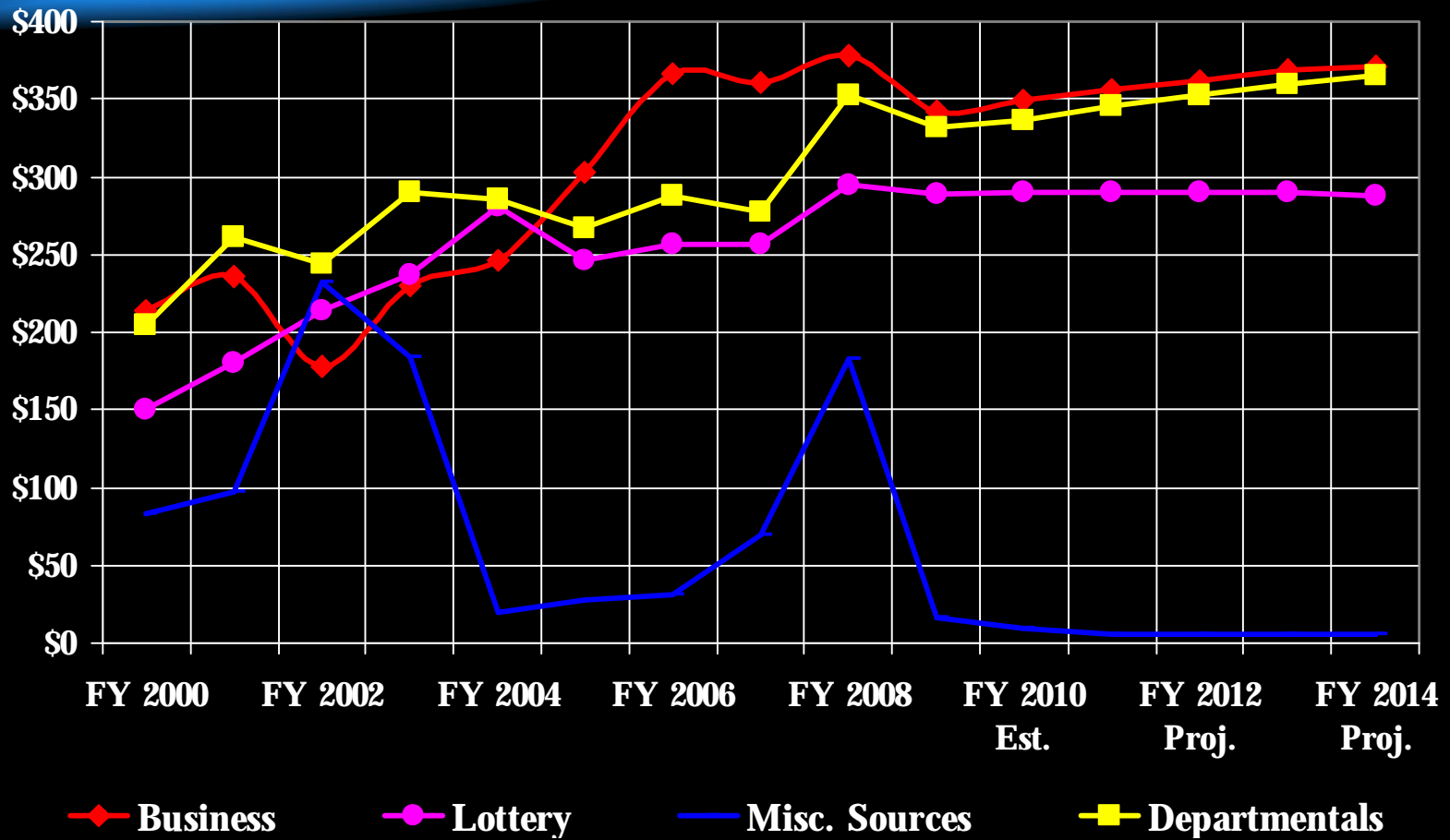
Income and Sales



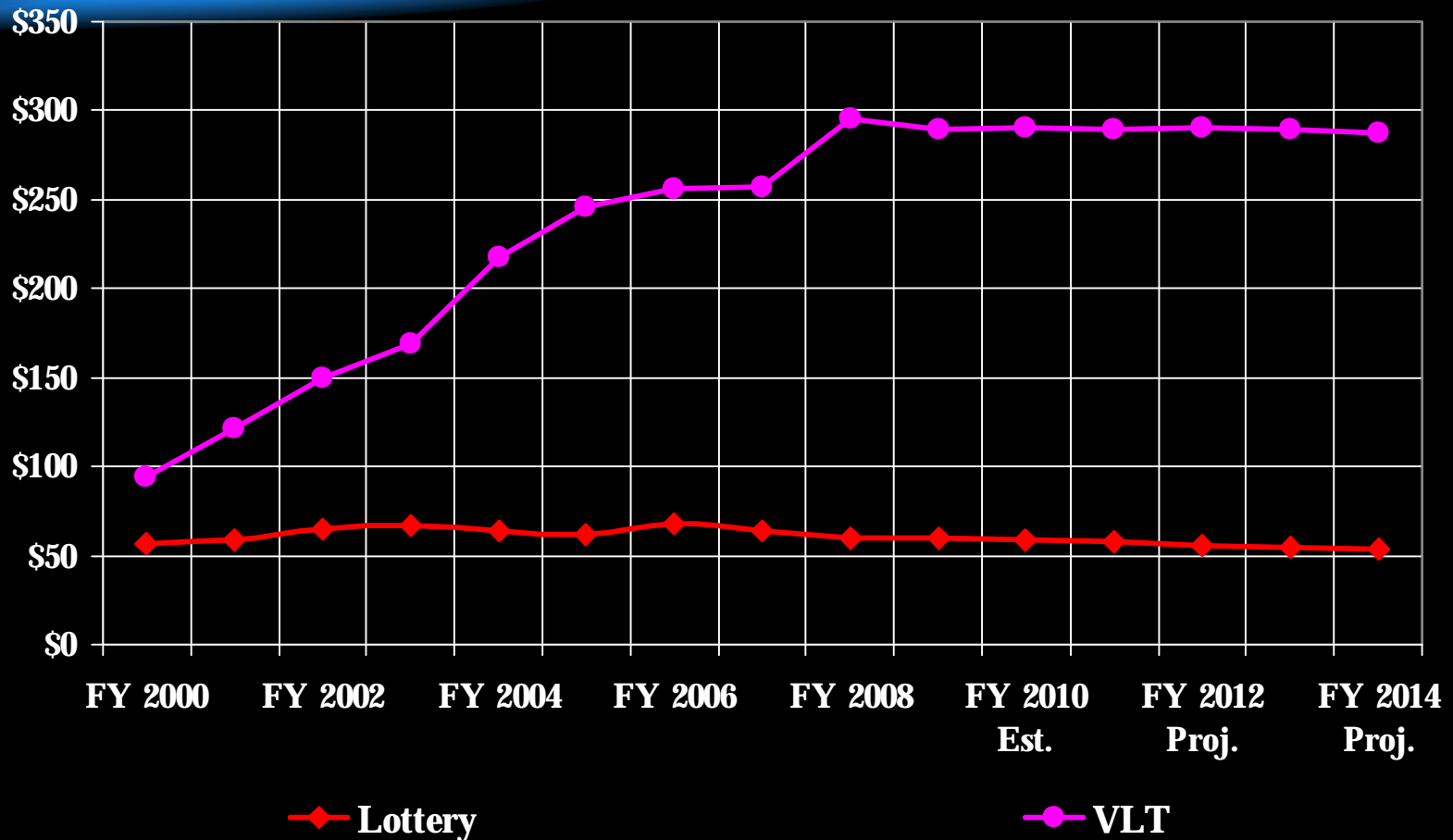
Income and Sales



Other Sources



Lottery





Budget Forecasts

Current Year Deficit

- | The *current year* is a cyclical economic problem exacerbated by unmet expenditure savings
 - u It is a mainly a *revenue side* problem caused by major national economic factors
 - u It has caused a current year deficit of \$366.8 million – 11.3 percent of all expenditures excluding debt service

FY 2009

| | Enacted | Current | Diff. |
|-----------------|-----------|-----------|-----------|
| Opening | \$ 3.2 | \$ 1.7* | \$(1.5) |
| Revenues | 3,346.7 | 3,113.1 | (233.6) |
| Rainy Day | (73.7) | (68.5) | 5.2 |
| Expenditures | (3,276.2) | (3,374.8) | (98.6) |
| FY 2009 Only | 0.1 | (328.4) | (328.3) |
| FY 2008 Deficit | | (38.4) | (38.4) |
| Total FY 2009 | 0.1 | \$(366.8) | \$(366.7) |

**Reappropriation*

FY 2008 (Unaudited)

| | Enacted | Current | Diff. |
|--------------|-----------|-----------|--------|
| Opening | \$ 3.6 | \$ 3.6 | |
| Revenues | 3,436.1 | 3,427.9 | (8.2) |
| Rainy Day | (68.7) | (68.6) | 0.1 |
| Expenditures | (3,367.8) | (3,399.6) | (31.8) |
| Reapprop. | | (1.7) | (1.7) |
| Rainy Day | | 38.4 | 38.4 |
| Free Surplus | 3.2 | 0.0 | (3.2) |

Current Year Deficit

- | Revenues are off by \$233.6 million, the major cause of the deficit
- | Expenditures less cause but still problematic
 - u \$38.4 million needed from Rainy Day for FY 2008
 - u Caseloads and medical up \$36.1 million, 5.2 percent
 - u Other appear up \$60.8 million

Current Year Deficit

- | The deficit It must be made up in 7 months
- | The state borrowed \$350 million for cash flow purposes that must be paid on June 30 which requires the deficit be closed
 - u ***Requires actual cash, not merely GAAP balancing***

Current Year Deficit

- | There are major obstacles to closing the gap
 - u Opportunity
 - u Time
 - u Limited gubernatorial authority
 - u High Tax – Low Yield Revenue Structure

Current Year Deficit Obstacles

I Opportunity

- u Low hanging fruit is long gone
- u Need to preserve options for major downward revenue revisions in May (e.g. one timers, rainy day fund)
- u Experience has shown that further deterioration more likely than the opposite

Current Year Deficit Obstacles

I Time

- u Less than 7 months
- u Actions requiring statutory changes have 5 months
- u Actions also requiring rule and regulation changes have even less time

Current Year Deficit Obstacles

- I Limited gubernatorial authority
 - u Governor cannot rescind, withdraw or transfer appropriations - changes require prior legislative action
 - u Need to make changes usually obvious by September – early action reduces severity of solution
 - u Will continue to be a problem as long as recession continues

Current Year Deficit Obstacles

- I High Tax – Low Yield Revenue Structure
 - u Nominal rates are higher than effective rates (narrow sales tax base, tax credits)
 - u Low yield relative to high tax reputation
 - u Reputation discourages location, expansion, investment

Budget Year and Outyears

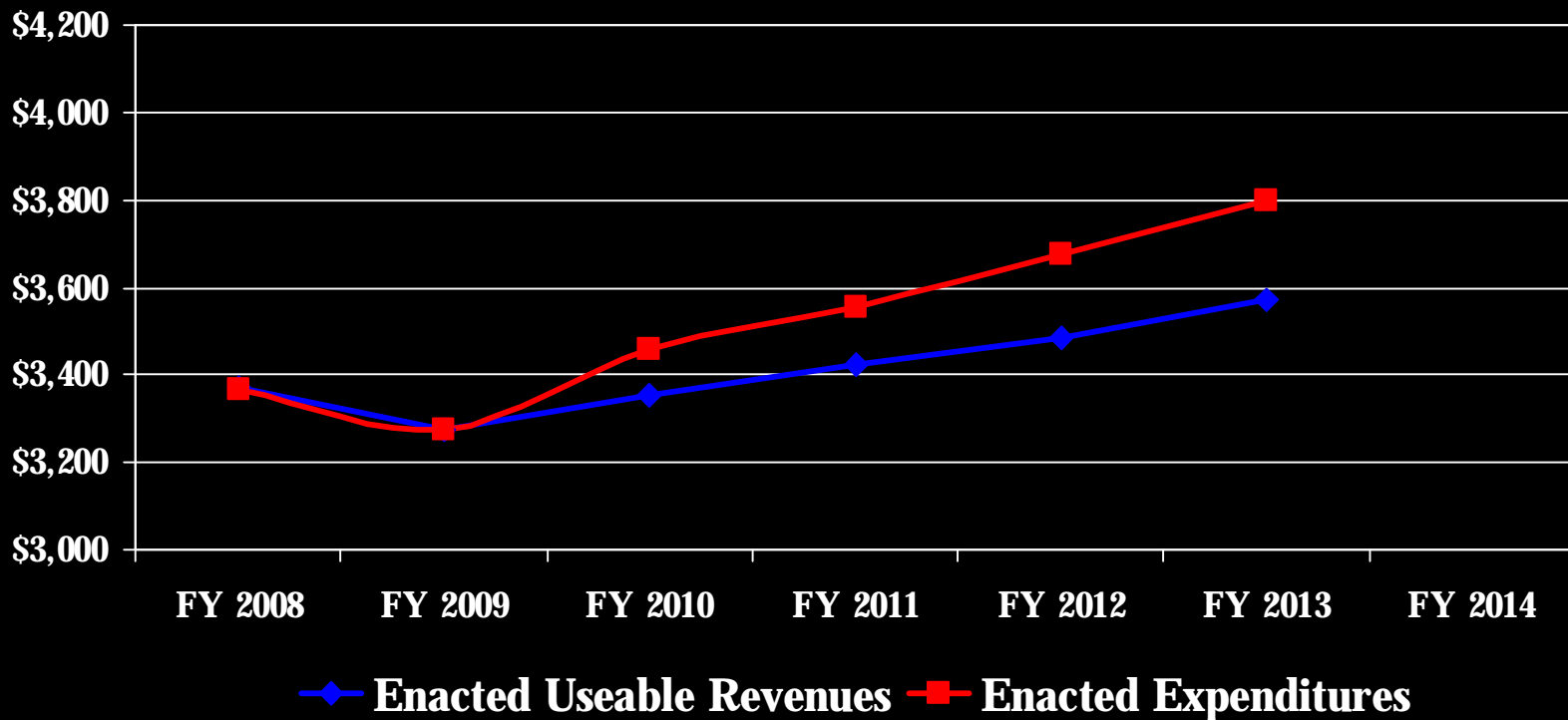
- | There are also *budget year* and *outyear problems*
 - u The budget year likely has a gap of \$486 million
 - u That gap grows in the out years to \$770 million
- | Transportation not yet factored in

Budget Year and Outyears

- | These gaps are a function of both cyclical economic and continued structural issues
 - u The 2008 Assembly attacked the structural issues on the expenditure side, resolving nearly 2/3rds

Budget and Out Years

Revenues vs. Expenditures - Enacted Budget

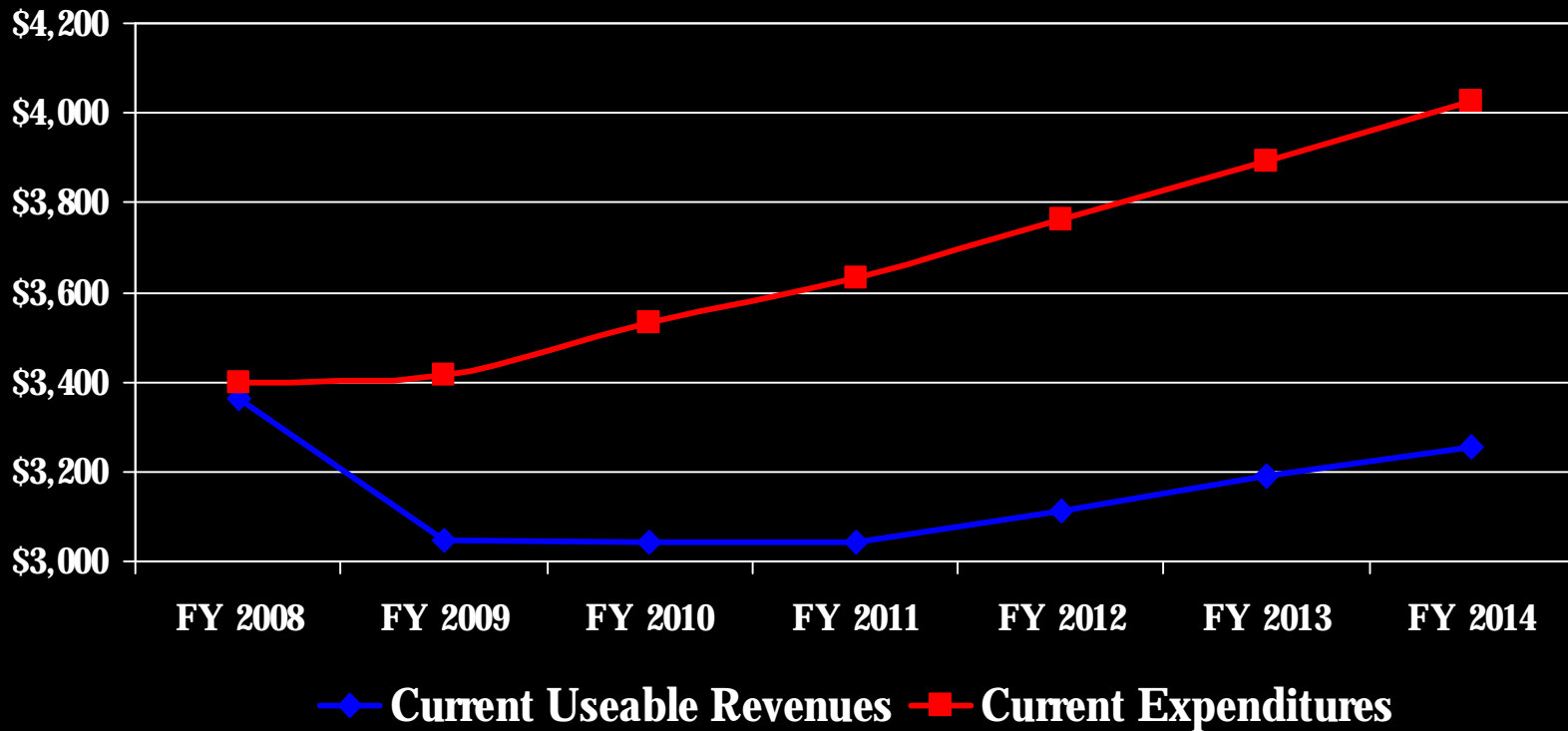


Budget Year and Outyears

- | These gaps are a function of both cyclical economic and continued structural issues
 - u The 2008 Assembly attacked the structural issues on the expenditure side, resolving nearly 2/3rds
 - u The recessionary economic cycle expands the deficits through lower revenues

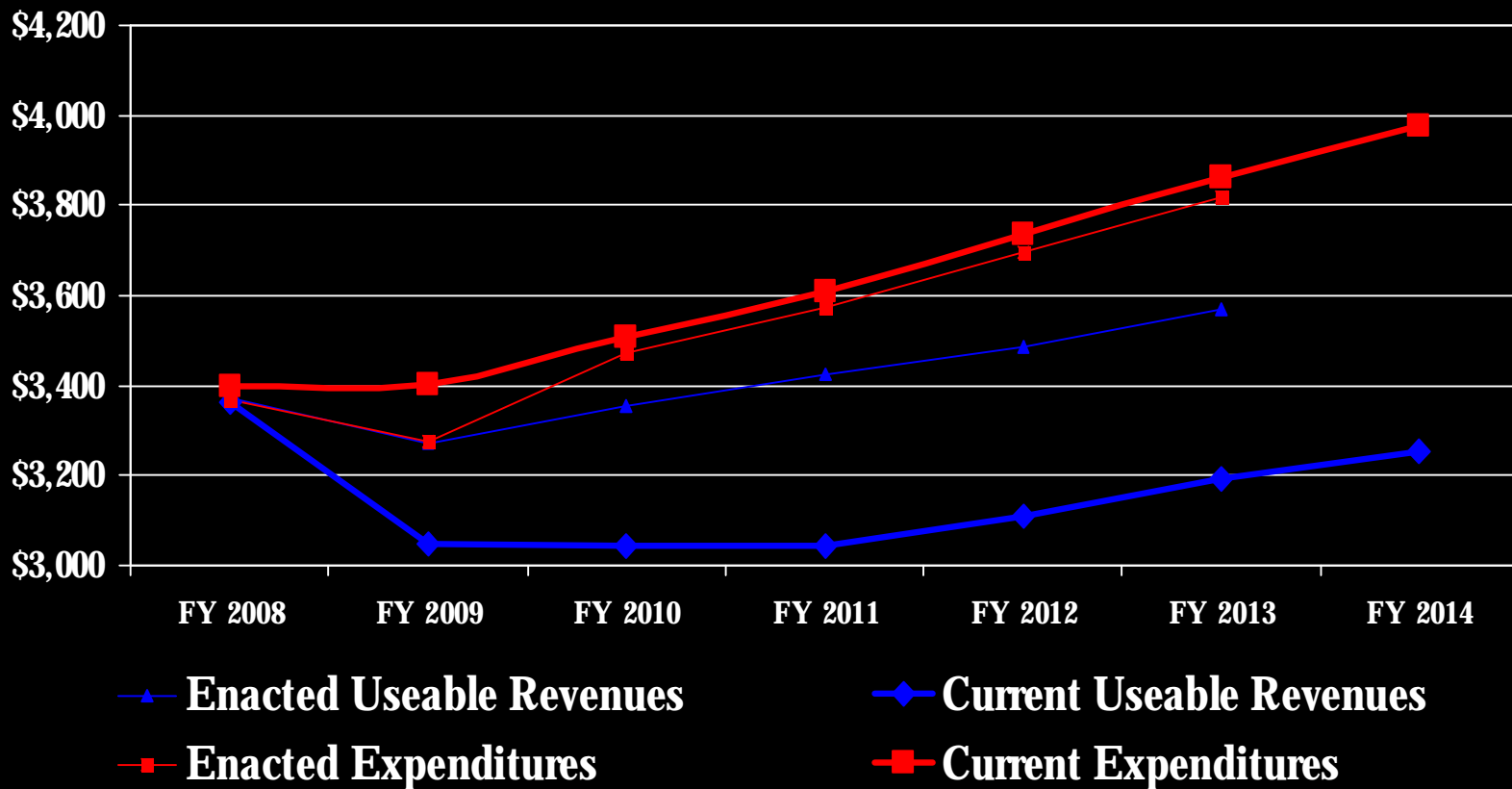
Budget and Out Years

Revenues vs. Expenditures - Current Estimates

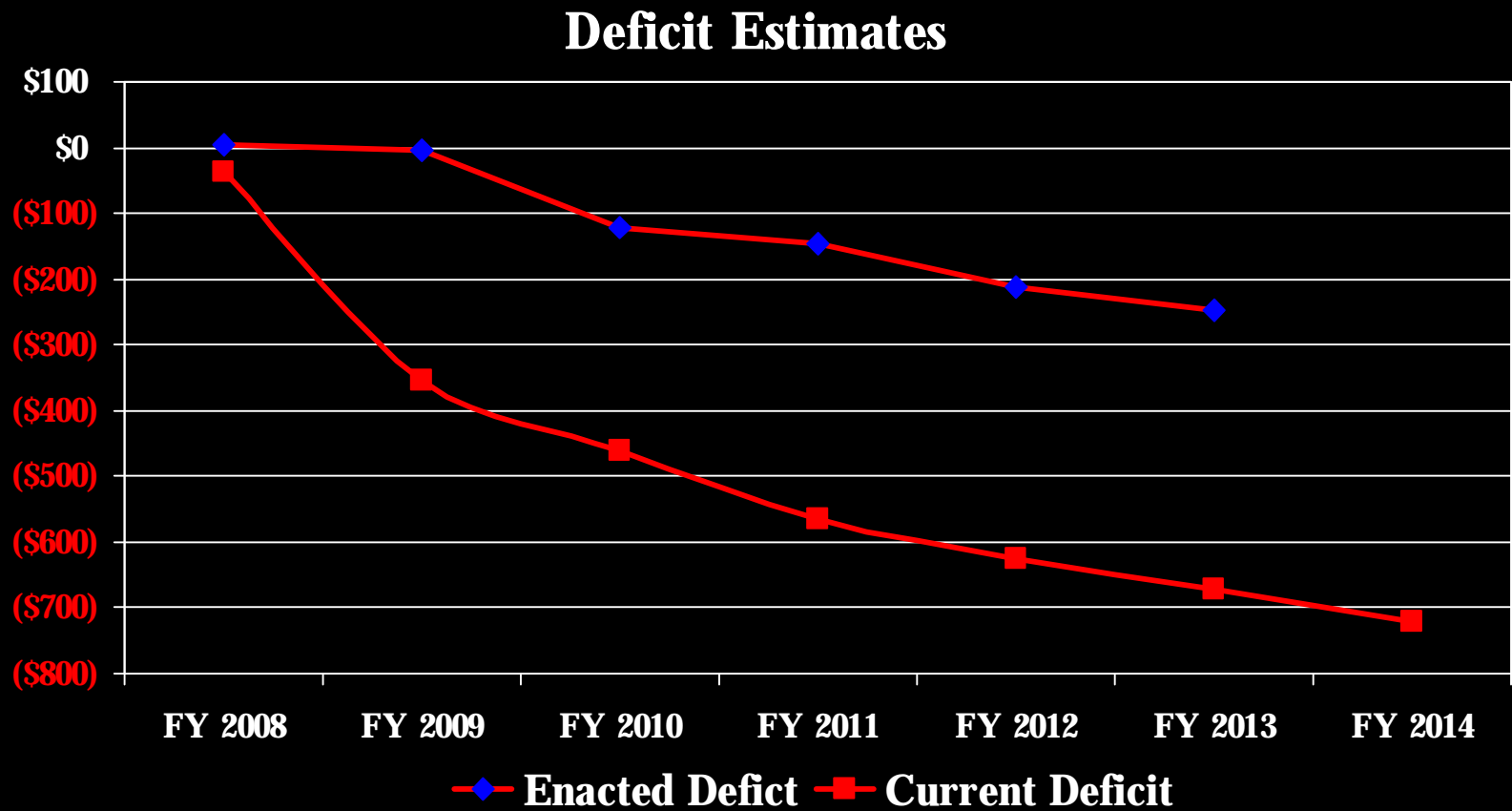


Budget and Out Years

Revenues vs. Expenditures



Budget and Out Years



Budget Year and Out Years Obstacles

- | High tax – low revenue yield structure
- | Major portions of expenditure base grow at significantly more rapid rate than economy supports

Growth Rates

| Item | Est. Annual Growth |
|--------------------------------------|--------------------|
| Jobs | 0.7% |
| State Personal Income | 3.9% |
| Taxes | 1.2% |
| Total Revenues | 1.4% |
| Total Expenditures | 3.2% |
| Salaries & Benefits – 22.8% of total | 6.0% |
| Medicaid – 21.8% of total | 7.9% |



Summary
Next Hearings

Summary

- | Major current year deficit
 - u Must be fully resolved by June 30
 - u TANS repayment due
- | Major budget and out years gaps
 - u Slow growing economy
 - u Structural tax and expenditure issues
 - u Staff continuing work on estimates

Next Hearings

- | December 1 – FY 2008 & FY 2009 Expenditure Issues
- | December 2 – Overruns and Failed Initiatives: Budget Management, Monitoring and Accountability
- | December 3 – Low Cost/No Cost Options for Recession Relief