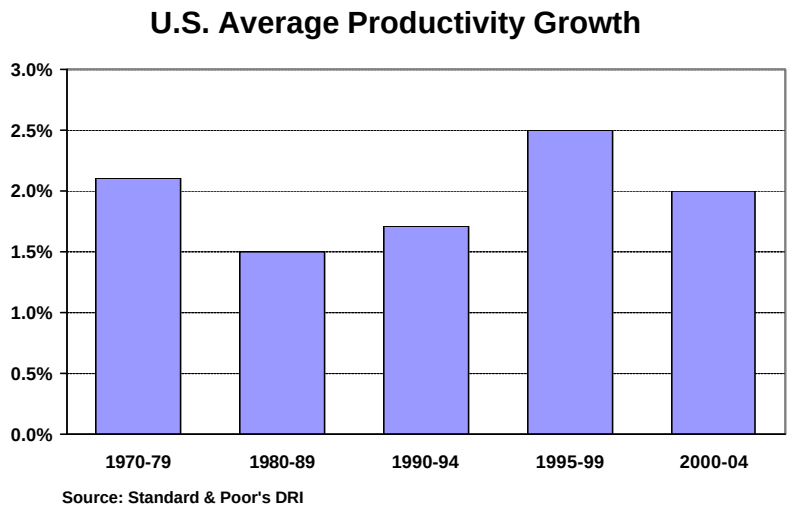
IDAHO OUTLOOK

NEWS OF IDAHO'S ECONOMY AND BUDGET

STATE OF IDAHO | DIVISION OF FINANCIAL MANAGEMENT | MARCH 2000 VOLUME XX NO. 9

Raising the GDP Speed Limit. Last June, DFM reported that the U.S. economy could grow between 2.0% and 2.5%, while enjoying both full employment and low inflation. DFM was not alone in its thinking; most economists felt this was feasible given reasonable expectations for labor force and productivity growth. However, a year later it seems that this estimate may have been too conservative. Again, DFM is in good company. For example, the Congressional Budget Office (CBO) has raised its measure of potential output over time. In 1996, it estimated it was 2.2%. It was raised to 2.8% in 1999 and to 3.2% in 2000.



There are several reasons to bump up the potential GDP growth rate. The first has to do with changes made to the definition of GDP. It was recently changed to include business purchases of software. Before this, these software purchases were considered intermediate goods and were not included in GDP. The U.S. Department of Commerce estimates that this alone added $95 billion to GDP in 1996. The addition of software purchases, as well as other changes, raised the average annual growth of real GDP by about 0.4 of a percentage point in both of the last two decades. The inclusion of one of the fastest growing parts of the economy has raised the potential GDP growth rate.

The second factor that will propel potential GDP is increased productivity. Throughout the 1970s and 1980s, economists were perplexed by the alarming slowdown in productivity. However, this slide was reversed in the 1990s, with productivity booming during the closing years of that decade. It rose by more than 2% in 1996 and 1997. In 1998 and 1999 it advanced more than 3%. One reason for this productivity explosion has been the strong investment in capital. This surge in spending has been fueled by the dwindling supply of labor, intense competition, and attractive interest rates. It now appears that productivity will grow by 2% to 2.5% over the next few years, compared to the 1.5% predicted last year. Combined with the labor force growth of about 1.0%, this implies the U.S. economy can advance comfortably by 3% to 3.5% annually.

Interestingly, it appears that no one has informed the economy of its speed limit. Real GDP has been growing faster than its potential since 1996, and it is expected to do so again this year. While it is not unusual for the economy to run hot for short periods of time, eventually imbalances should occur that pull it back towards its potential. So far, these imbalances have been absent. Inflation, the bane of the central bank, remains tame. However, it appears Chairman Greenspan is growing weary of waiting for the economy to slow itself down, and push for several more interest rate hikes this year. The impacts of these increases will be felt in the second half of this year. Thus, after 2000, real GDP growth should be more in line with its potential.

On a Personal Note. Earlier this month, our extraordinary Administrative Assistant, Shauna Wallace, left DFM to make her mark in the private sector. For six years she provided invaluable assistance to the publication of the *Outlook* and numerous other publications. Thank you, Shauna, for all your help and best of luck in your new job!

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General Fund Update

As of February 29, 2000

Revenue Source	$ Millions FY00 Executive Estimate[3]	DFM Predicted to Date	Actual Accrued to Date
Individual Income Tax	892.2	560.8	564.1
Corporate Income Tax	99.3	57.2	60.4
Sales Tax	617.6	420.7	424.1
Product Taxes[1]	15.8	10.6	10.7
Miscellaneous	83.4	41.6	49.5
TOTAL GENERAL FUND[2]	**1,708.4**	**1,090.9**	**1,108.8**

1 Product Taxes include beer, wine, liquor, and cigarette taxes
2 May not total due to rounding
3 Revised Estimate as of January 2000

General Fund revenues in February were $3.3 million below the month's target, bringing year-to-date revenue to a level $17.9 million above predictions. February's revenue weakness was only the second month of fiscal year 2000 that has come in below the target; revenues fell $1.5 million short of the predicted amount in July 1999. The current month's revenue shortfall is due almost entirely to under-performance in the Individual Income Tax.

Individual Income Tax collections appeared to be weak in February at $7.5 million below the target. However, this apparent weakness is due entirely to unusually high refund payments. February refunds were actually $23.4 million, compared to projected level of $14.7 million predicted. A major increase in the use of electronic filing has accelerated refunds dramatically. As of March 10, 2000 the number of refund returns processed were up 40% from 1999 to 2000, from 72,699 to 102,115. The dollar value of refunds increased even more, from $24.2 million in 1999 to $35.3 million in 2000, a 45% increase. The good news in all this is while the new electronic filing age has complicated the revenue monitoring process, it also is very likely that the surge in early refunds will be offset by fewer refunds later in the fiscal year. Also, withholding collections and filing collections were both ahead of their respective predicted values for February.

Corporate Income Tax collections were slightly below the target for February. Higher-than-expected refunds and lower-than-expected filing collections were the sources of February's weakness. Corporate Income Tax receipts remain a healthy $3.2 million ahead of the year-to-date target.

Sales Tax collections rebounded in February; they were $4 million ahead of the predicted amount. This follows January's shortfall of $1.7 million. January's weakness was unusual in view of the strong December sales reports from retailers, and February's surge is most likely a timing shift. Year-to-date sales tax collections are now $3.4 million ahead of the prediction.

Product Taxes and Miscellaneous Revenues were both slightly higher than expected in February, with nothing unusual to report in either category.