

IDAHO OUTLOOK

NEWS OF IDAHO'S ECONOMY AND BUDGET

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The economists at Global Insight have prepared a list of economic predictions for 2009. We have paraphrased this list to highlight some of the challenges and responding policies for the coming year. While all years bring challenges, next year promises to have more than its fair share of them.

Most of the world's economies are facing hard times. The current U.S. recession is already a year old, and could turn out to be the longest recession in the past six decades. Global Insight predicts U.S. output will shrink through the first half of 2009. If this forecast holds, the recession would be about 18 months long—almost twice as long as the average for post-war recessions. The anticipated decline will also test another six-decade old record. The back-to-back declines in real GDP predicted for the fourth quarter of 2008 (5.0%) and first quarter of 2009 (3.8%) are the worst since the 1982 recession. The U.S. is not alone. Japan and some European countries (Ireland, Italy, and Germany) are also in recession, and other continental economies are expected to join them soon. This downturn will be the biggest European economic contraction since the early 1990s and the first for the Eurozone. Japan, which has been no stranger to recessions since the 1990s, will suffer its nastiest set back since the Asian crises in 1998. Few large economies will escape the global slowdown. For example, even global economic wunderkind China

will see its growth slow from nearly 12% in 2007 to "just" 7% in 2009.

National central banks have already begun to respond in an effort to minimize economic woes. The Federal Reserve's Federal Open Market Committee (FOMC) lowered its federal funds rate target to the range of 0.25% to 0.0% on December 16, 2008—a move that was bolder than most Fed watchers expected. Global Insight had assumed the FOMC would not lower its target to zero until the beginning of 2009. On December 4, the European Central Bank cut its overnight rate by 75 basis points to 2.5%. On the same day, the Bank of England dropped its rate by 100 basis points to 2.0%. It is assumed these central banks will drop their respective rates further to 1.0% and 0.5%. However, cutting them to zero is also possible. On December 19, 2008 the Bank of Japan lowered its uncollateralized overnight call rate by 20 basis points to 0.1%. The People's Bank of China lowered rates 108 basis points on November 26—its largest cut in 11 years.

As U.S. interest rates head toward zero, policymakers will look to other ways to stimulate the economy. For example, the Fed may resort to quantitative easing, which is the direct purchases of long-term treasuries. However, the U.S. will hedge monetary policy with a fiscal stimulus plan. It remains to be seen what will be the size and shape of the fiscal policy. The incoming Obama administration has been looking at a stimulus package of

between \$500 billion and \$750 billion (about 3% to 5% of GDP). In its most recent forecast, Global Insight assumes it will be a \$550-billion package which consists of tax cuts, infrastructure spending, and other provisions. The only other country considering a major stimulus program is China. It has announced a \$586-billion plan (16% of GDP) that should add substantially to growth. The fiscal stimulus plans discussed by other countries are more modest. For example, plans being considered by the United Kingdom and Eurozone are only between one and one-half percent of GDP.

One consequence of the weakening global economy is concerns have moved away from inflation to deflation. The steep collapse of commodity prices over the last few months (60-80%) has been unprecedented, and they could fall even further. The most notable decline has been the price of oil, which has fallen from its summer high of nearly \$150 per barrel to well below \$40 per barrel. The 60% decline in retail gasoline prices is estimated to be the equivalent of a \$230-billion tax cut. Another result of the global slowdown is the dollar has strengthened, as its safe-haven/principal-reserve-currency status has trumped all other fears. Moreover, the markets seem to have a little more confidence that the U.S. may be able to pull out of its recession sooner and faster than other parts of the world. However, once the current crisis is over, the downward pressures on the greenback should return.

Idaho General Fund Update

As of November 30, 2008

\$ Millions			
Revenue Source	FY 2009 Executive Estimate³	DFM Predicted to Date	Actual Accrued to Date
Individual Income Tax	1,334.7	469.2	463.6
Corporate Income Tax	150.2	39.6	45.1
Sales Tax	1,134.0	497.3	477.9
Product Taxes ¹	29.7	13.4	13.4
Miscellaneous	117.7	36.8	36.3
TOTAL GENERAL FUND²	2,766.3	1,056.3	1,036.2

1 Product Taxes include beer, wine, liquor, tobacco and cigarette taxes *3 Revised Estimate as of August 2008*
2 May not total due to rounding

This is the last *Idaho Outlook* that will be based on the August 2008 General Fund revenue forecast. The next *Idaho Outlook* will be based on the January 2009 General Fund revenue forecast, scheduled to be released on January 12 during the Governor's State of the State/Budget Message delivered to the opening of the 2009 Idaho Legislative Session. This edition of the *Idaho Outlook* confirms what has been obvious for the past several months: Idaho's General Fund revenue collections are significantly underperforming the August 2008 forecast. The January 2009 forecast will contain a lower forecast of General Fund revenue for FY 2009.

Overall General Fund revenue collections fell short of expectations again in November, coming in \$9.8 million below the amount predicted for the month. This brings the year-to-date result to \$20.1 million (-1.9%) behind expectations. The majority of November's weakness was from the sales tax, but this was compounded by the first month that corporate income tax collections fell below expectations so far this fiscal year. The individual income tax took a welcome journey above expectations in November, but this was most likely a function of large severance checks that were associated with recent layoffs in the manufacturing sector.

November was the second best month this fiscal year for the individual income tax, coming in \$1.1 million higher than expected for the month. However, this leaves the fiscal year-to-date result at a level that is \$5.6 million lower than expected. November withholding collections were up 5.5% on a year-over-year basis, and this "strength" fully accounts for the month's \$1.1 million excess. However, withholding is still 0.5% lower than a year ago on a fiscal year-to-date basis, and is \$9.2 million below the predicted amount on a year-to-date basis. Strength is in quotes because it is exceedingly likely that November's individual income tax result would have fallen short of expectations were it not for withholding on large severance checks associated with recent layoffs.

The corporate income tax had its first month of lower-than-expected revenue in November, coming in \$1.7 million below the predicted amount for the month. This brings the year-to-date excess down to \$5.5 million. The corporate income tax remains the sole revenue category that is ahead of expectations for the fiscal year to date. November's corporate income tax receipts were very close to being on target (short by \$0.1 million), but refunds were \$1.5 million higher than expected for the month.

Sales tax revenue continues its search for the bottom, with November turning in the worst performance so far this fiscal year. The General Fund share of sales tax was \$9.0 million lower than expected for the month, and now stands \$19.5 million below the predicted amount for the fiscal year to date. Gross collections were down an astounding 12.4% on a year-over-year basis, and the first five months of FY 2009 are down 7.5% compared to the same period in FY 2008. Since FY 1970, there have been only three other fiscal years that have had negative gross collection growth (on a normalized, or rate-adjusted basis) for the first five months of the fiscal year—FY 1981 was down 3.7%, FY 1983 was down 0.7%, and FY 1987 was down 0.5%. The worst performance in the past decade was FY 2002, when growth was just 0.8%, which also happens to be the fifth worst year since 1970. Last year's 1.4% growth for the first five months puts its rank since 1970 at sixth from the bottom.

Product taxes and miscellaneous revenue were close to their targets for November, leaving the fiscal year-to-date result at \$-0.1 million for product taxes and \$-0.6 million for miscellaneous revenue.

