

IDAHO OUTLOOK

NEWS OF IDAHO'S ECONOMY AND BUDGET

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The 2.2% annualized real GDP growth during the third quarter has raised hopes that the U.S. economy is on the mend. It marks the first time in the two years since the recession's start that real GDP has expanded. Although, the economy may have turned an important corner, other pieces need to fall into place for the recovery to be sustainable. An essential component of the expansion is a healthy housing sector. During the first half of the last decade, residential construction contributed to overall output growth, but in the second half it has weighed it down. The worst years were 2007 and 2008, when the housing bust stripped about one percentage point per year from overall growth. Clearly, the economy cannot thrive if this burden persists.

National housing starts were near 2 million units annually from 2003 through 2006. By 2009, starts fell to under 600,000 units. After falling 7% in 2006, real investment on residential buildings dropped an average of 20%

annually through 2009. Home sales plunged by a third from 2005 to 2009. With demand weak and supply bloated, it is not surprising that existing housing prices also tumbled, going from an average of \$270,000 in 2006 to an estimated \$217,000 in 2009. These were the only three years on records (that go back to 1968) that housing prices have declined.

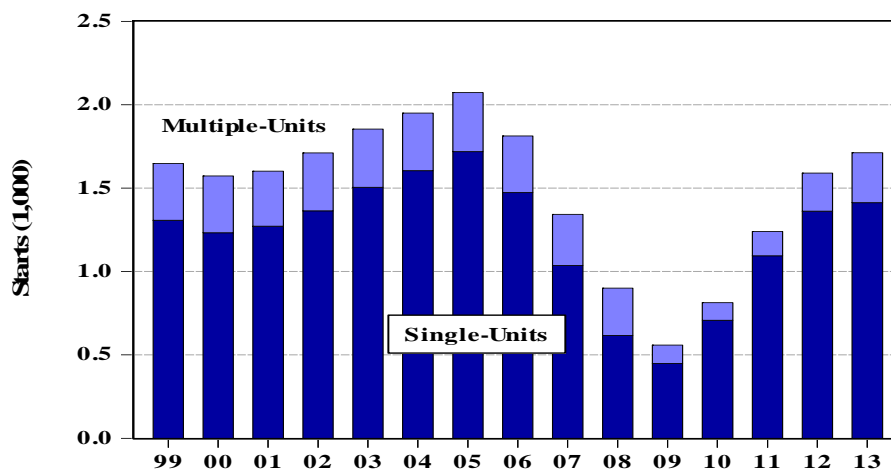
The housing sector began displaying positive signs late last year. After being stuck below 5.5 million annualized units since the recession's start, home sales jumped to 5.7 million units last summer. It is estimated sales climbed to 6.5 million units in 2009's last quarter. A key reason for this turnaround is lower housing prices made housing more affordable. Specifically, the single-family affordability index has improved from 1.1 in 2006 to 1.7 in 2009. Demand also was aided by the federal first-time homebuyer tax credit. This credit expired in November 2009, so some of the activity last year reflects

buyers trying to get in under the deadline. This strong demand has helped work down the inventory of unsold homes, which sets the stage for a revival of housing starts.

The housing recovery will be gradual. Housing starts and sales will benefit from the need to replenish inventory, a gradual pickup in household formation, and job growth. The first-time homebuyer tax credit has been extended to include sales with a binding contract occurring between January 1, 2010 and April 30, 2010. In addition, a tax credit of up to \$6,500 is available to non-first time buyers meeting certain requirements. These credits should temporarily boost sales in the first part of this year, but the annual sales should be about the same as in 2009. Housing starts should climb from their low of under 600,000 units in 2009 to 800,000 units in 2010. Unfortunately, existing housing prices are expected to drop another one-half percent in 2010.

After sliding for four consecutive years, the average sales price for an existing home is forecast to appreciate about 1% in 2011. It advances 4% in 2012 and 5% in 2013. Housing sales top 6 million units in 2011 and climb to 7.4 million units by 2013. Housing starts also improve gradually, growing to about 1.7 million units by 2013. While this is significantly lower than its peak of 2.1 million units in 2005, it is three times higher than its trough of 600,000 units in 2009. Residential fixed investment goes from being a drag on economic growth to a contributor after 2009. Thus, an essential cog in the economic recovery engine should soon be in place, but it will turn slower than it did in the middle of the last decade.

U.S. Housing Starts



Source: IHS Global Insight

Idaho General Fund Update

As of December 31, 2009

\$ Millions			
Revenue Source	FY 2010 Executive Estimate ³	DFM Predicted to Date	Actual Accrued to Date
Individual Income Tax	1,125.0	544.9	533.4
Corporate Income Tax	130.7	52.0	45.2
Sales Tax	950.1	493.0	492.9
Product Taxes ¹	40.9	21.7	21.7
Miscellaneous	102.4	44.6	50.4
TOTAL GENERAL FUND²	2,349.1	1,156.2	1,143.6

1 Product Taxes include beer, wine, liquor, tobacco and cigarette taxes
2 May not total due to rounding
3 Revised Estimate as of January 2010

General Fund revenue collections were substantially (\$12.6 million) below expectations for the month of December, but the bottom-line number masks some quite positive revenue performance in two key components of the General Fund revenue stream. Specifically, sales tax receipts were a scant \$0.1 million below the month's target. That makes December virtually dead-on and the best month for sales tax since July 2009, and without the artificial boost from the "cash for clunkers" program. Withholding collections were \$0.6 million higher than expected for December, the second straight month of better than expected withholding collections.

The \$11.5-million shortfall in individual income tax in December was by far the largest underperformance of this (or any other) revenue category this fiscal year. Over two-thirds of the gap (\$8.1 million) is due to filing collections, but this is not a reliable indicator of what is likely to occur for the entire fiscal year. Historically, there is little correlation between what happens in December's

filing collections and filing collections for the full fiscal year. Refunds contributed \$4.1 million to December's weakness, and this too is not correlated with what happens for the full fiscal year. In a nutshell, it is simply not appropriate to extrapolate filing or refund performance in December to the full fiscal year.

Corporate income tax was \$6.8 million below expectations for December. The details behind December's weakness reveal how volatile this revenue category can be. Filing collections of \$6.5 million were \$4.6 million higher than expected, and the largest dollar amount for December since FY 1996. Estimated payments of \$15.4 million were \$5.9 million lower than expected, and the smallest dollar amount for December since FY 2004. Refunds of \$8.8 million were \$5.6 million higher than expected, and the largest dollar amount since FY 2000. Another way to look at December's volatility is the share it represents of the full fiscal year. The predicted amount of corporate income tax (based on historical collection patterns) is 15.3%, but this

December is only 13.3% of the forecast amount for the fiscal year (the difference is the \$6.8 million gap). But this belies the true volatility in this revenue category. In December 2000 revenue of \$55.9 million comprised a whopping 39.4% of the total for FY 2001. December 2003 corporate income tax revenue of \$7.8 million comprised just 7.6% of the FY 2004 total.

Sales tax revenue was low by a mere \$0.1 million in December, declining at a year-over-year rate of just 3.6%. This is the best sales tax performance since July 2009, and is the first time that year-over-year gross collections have declined at less than a double-digit rate since the 9.6% decline in January 2009. The last time the sales tax declined at a slower rate was a decline of 3.4% in August 2008.

Product tax revenue was essentially on target for the month of December. Miscellaneous revenue was ahead of expectations by \$5.9 million for the month. The bulk of this gain (\$4.7 million) was due to higher-than-expected unclaimed property receipts.

