



Commission on Government Forecasting and Accountability

MONTHLY BRIEFING

OCTOBER 2008

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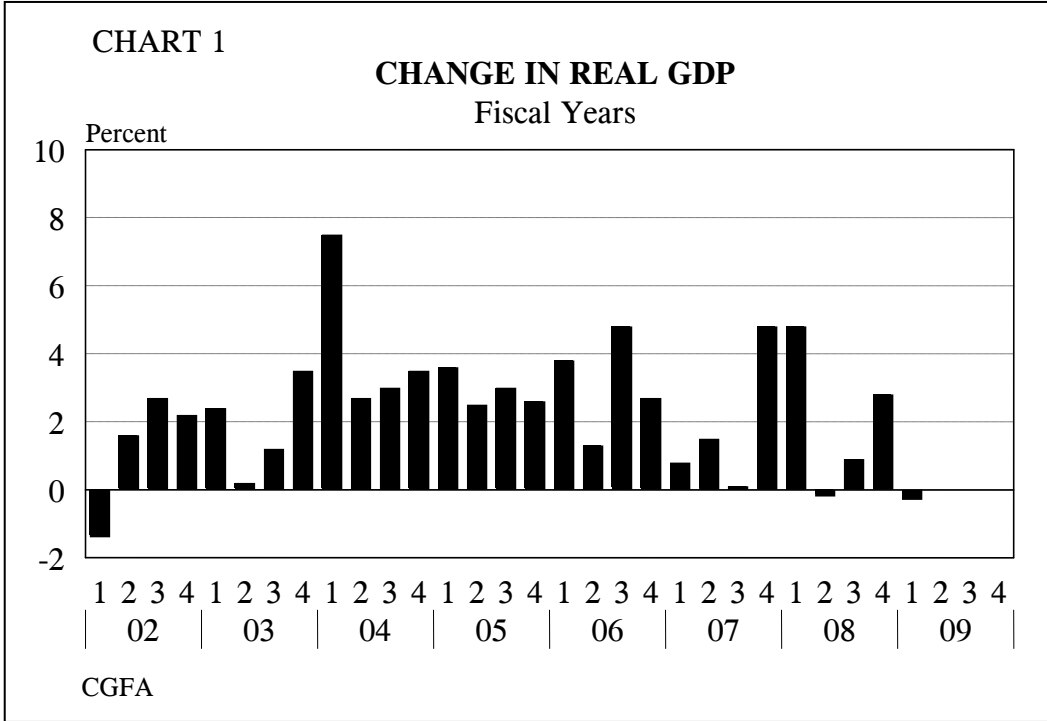
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ECONOMY: Recession

Edward H. Boss, Jr., Chief Economist

There can be little doubt that the U.S. economy is in recession. While some may argue that we have yet to see two consecutive quarters of decline in real gross domestic market (GDP), it is important to note that the National Bureau of Economic Research (NBER), the official determiners of dating recessions, does not define a recession in terms of two consecutive quarters of decline in real GDP. Indeed the so-called two consecutive declines in real GDP definition came about years ago when a Federal Reserve Chairman was asked to define a recession. He gave no definition but pointed out that in the past the economy had not gone into recession without having seen at least two consecutive quarterly declines in real economic activity. This has not been the case in recent years, however. For example, the last recession started in March 2001 and ended in November of that year, yet there was a small decline in the first quarter of 2001, an increase in the second quarter, another small drop in the third quarter followed by no further negatives until a brief a one quarter decline in the final quarter of 2007.

Rather than the incorrect rule of thumb, the official definition of *“a recession is a significant decline in economic activity spread across the economy, lasting more than a few months, normally visible in real GDP, real income, employment, industrial production, and wholesale-retail sales. A recession begins just after the economy reaches a peak of activity and ends as the economy reaches its trough.”* At month’s end, the Commerce Department issued its advanced report on GDP for the third quarter of 2008 (first quarter of fiscal 2009) it showed the economy declined



at a slim 0.3% annual rate (See Chart 1 on page 2). While there will be two more estimates of the quarter's performance as more data become available, after a dip in real GDP in the final quarter of 2007, real GDP rose at a 0.9% annual rate in the first quarter of 2008 and a 2.8% annual rate in the second quarter.

Looking at other measures, in terms of payroll employment, it has declined since the end of 2007 with the rate of decrease accelerating. Industrial production took a particularly sharp downward path in September falling 2.8%, the latest month available, although hurricanes Gustav and Ike as well as a strike at a major aircraft producer severely curtailed output that month. Even so, industrial production in September was 4 ½% below that of a

year earlier. Beginning in April, disposable personal income was buoyed by the Economic Stimulus program. As these payments ran down over the following months, however, so did their effect on income. In real terms, after a sharp rise in May, inflation-adjusted disposable personal income has declined since June. Finally, sales of retail and food sales fell 1.2% in September, with a particularly sharp decline in auto sales, and were 1% lower than in September 2007. Moreover, prospects for the important holiday shopping season appear dim and should be reflected in a particularly large decline in real GDP expected in the final quarter of 2008. Thus, it appears that there have been declines in a broad sector of the U.S. economy that have lasted for a significant enough length of time to be classified as a recession. If

we are in a recession, the question is how long will it last?

A look back at history shows us that the average length of the ten recessions in the post World War Two period was 10 months. Even so, there have been wide differences in their duration. The last two recessions in 1990 and 2001 each lasted 8 months, whereas the recessions starting in late 1973 and 1981 each lasted for 16 months, twice as long as the past two. The longest recession was at the beginning of the Great Depression that lasted 43 months while the shortest was in early 1980 with a span of 6 months.

While there is now no longer any doubt that the U.S. economy is in the midst of a recession, the official start of the decline will not be known until a recovery has been firmly established. Most economists suggest the recession began either at the end of last year or early in 2008. At the same time, it seems likely that given the severity of the financial crises, the recession will be more on the order of that seen in 1973 and 1981, which lasted 16 months, rather than the past two that were brief 8 month declines. Moreover even when a trough, or bottom, of the recession is reached, no rapid rebound is anticipated.

INDICATORS OF ILLINOIS ECONOMIC ACTIVITY

<u>INDICATORS</u>	<u>SEPT. 2008</u>	<u>AUG. 2008</u>	<u>SEPT. 2007</u>
Unemployment Rate (Average)	6.9%	7.3%	5.2%
Annual Rate of Inflation (Chicago)	-2.8%	-2.3%	4.4%
—————			
	<u>LATEST</u>	<u>% CHANGE</u>	<u>% CHANGE</u>
	<u>MONTH</u>	<u>OVER PRIOR</u>	<u>OVER A</u>
		<u>MONTH</u>	<u>YEAR AGO</u>
Civilian Labor Force (thousands) (September)	6,708	-0.2%	-0.2%
Employment (thousands) (September)	6,247	0.2%	-2.0%
New Car & Truck Registration (September)	46,473	1.2%	-5.1%
Single Family Housing Permits (September)	1,162	13.4%	-36.2%
Total Exports (\$ mil) (August)	4,738	5.9%	14.5%
Chicago Purchasing Managers Index (October)	38.7	-31.7%	-22.1%

Interview with Orim Graves
Fiduciary Investment Solutions, Inc.
Bukola Bello, Pension Analyst

In light of recent economic instability, commission analyst Bukola Bello interviewed Orim Graves, CFA, Senior Vice President of Client Services and Performance Reporting of FIS (Fiduciary Investment Solutions, Inc.) Group located in Philadelphia, Pennsylvania. FIS Group provides strategic asset allocation, manager searches and performance measurement solutions for institutional investors.

Our featured expert, Mr. Graves, has over 24 years of investment experience and is responsible for the firm's investment consulting unit, performance evaluation, reporting and risk analysis. Mr. Graves' wealth of experience includes serving as Deputy Chief Investment Officer of the City of Philadelphia Board of Pensions & Retirement, an analyst in the gaming industry and a fixed income trader for a major multinational bank. Mr. Graves serves on the board of a number of professional and charitable organizations including the National Association of Securities Professionals ("NASP"). He has also provided investment counsel to a number of institutional clients across the country.

We are truly pleased that Mr. Graves has agreed to share his expertise on the state of the current economy and its potential impact on public employee retirement systems.

CGFA STAFF: With the demise of Lehman's (bankruptcy) and Merrill Lynch now in dire constraints what can various retirement systems do to pad themselves against such downfalls? Of course there is no fool proof method, but there must be a way to ensure that annuitants are protected.

Orim Graves: Through diversification and the proliferation of asset classes, many institutional plans have limited exposure to the institutions in trouble. Most will only suffer through their exposure to the financial sector contained within their equity managers, and/or through the downdraft of the markets overall.

CGFA STAFF: Which asset classes (fixed income, private equity, hedge funds, etc.) have withstood the current market? Is diversification really enough when the market has been in a steady decline for the last 52 weeks?

Orim Graves: There really has not been a good place to hide given the breadth and severity of the deleveraging process that is now occurring. As a matter of degree within the traditional asset classes, US Government Bonds have been the best performing investment followed by the Financial Sector in equities. Hedge funds have not offered the levels of protection once advertised though they have performed significantly better than equities. Given the lack of available financing and the contraction the economy is experiencing, private equity investments are more than likely to be valued downward in the coming quarters as a result of slower economic activity.

Diversification is the main tenet of investing and while there is no doubt that a properly diversified plan would have fared marginally better during the downdraft, the severity and breadth of the market collapse left very little room and few areas for investors to hide. FIS had alerted our consulting clients of the impending “re-pricing of risk” during the past 2-3 years and recommended that they adjust their asset allocations accordingly, i.e., reduced equity exposure especially small cap.

CGFA STAFF: Can you please explain what you mean when you use the terms deleveraging and diversification?

Orim Graves: Deleveraging is the process by which leverage is taken out of the system (economy) which impacts asset prices etc. Leverage is another word for borrowing or debt. A crisis of confidence has developed in the financial sector with banks. Specifically, banks make their money lending against their capital base typically 9-10 times. In the current environment banks and other financial institutions are not lending money as freely as they did in the past couple of years thereby allowing fewer individuals and corporations to borrow money thereby reducing the amount of leverage or debt in the economy which drives asset prices down. This process has a significant impact on the economy because there is less money being spent on homes, automobiles and by small businesses which translates to fewer jobs and the overall impact can continue to spiral downward as consumers with jobs become fearful and slow their spending appreciably. This is a simplified example to give you an idea of how it starts and why it is difficult to contain once it has started.

Diversification is the strategy by which an investor utilizes multiple asset classes or investments (stocks, bonds, real estate, etc.) to spread their investible dollars across to minimize the impact of any one asset class or investment having a significant negative impact on the portfolio’s performance. An equity manager or equity mutual fund will typically have more than 20 securities in an effort to diversify the risk on their individual portfolio. Whereas a pension fund will invest their assets over a number of different asset classes trying to minimize the impact to the overall fund if any one asset class (stocks) goes through a period of poor performance relative to other classes like bonds. FIS believes that diversification is a low cost tool that should be used extensively and judiciously to maximize return and manage risk.

CGFA STAFF: Can you elaborate on how much “suffering” retirement systems (equity managers) will have to endure before the markets are stable again?

Orim Graves: Whoa, peering into my crystal ball there seems to be a number of factors that remain unsettled before the markets exhibit some level of stability. Fundamentally, we have to get through the next leg of declining home values due to increased unemployment stemming from the economic slowdown and the increase is projected to be close to the level of 8%. We then have to grapple with the consumer’s damaged psyche and figure out what will make them spend again in the face of lower home values, lower earnings prospects, the need for higher savings rate to replace their wiped out 401k portfolios and retirement savings. Deflation and deleveraging are a vicious duo that fundamentally doesn’t know

when to stop gnawing at their prey, in this case the US economy and subsequently the global economy.

The Russell 3000 is down around 40% year to date, an astounding figure to many in the industry. Valuations currently appear attractive based on the market anomalies of the past 20 years; however, the market has not valued earnings on the substantially lower economic activity we could see over the next 12 to 24 months. Pension Funds will be facing a potentially volatile landscape due to lower funding ratios brought on by lower asset values and reduced liquidity. As I stated earlier, many pension funds that have exposure to private equity will see a potential 10% to 20% write-down in valuations which will then be followed by write-downs in real estate. Plans are currently grappling with maintaining the proper levels of asset class exposure in the wake of the severe market decline. On top of that, add the difficulty that will be encountered by municipalities making their plan funding payments and a return to stability looks like it will be challenging in the near term.

CGFA STAFF: What was your reaction to the bailout bill that passed?

***Orim Graves:** On the bailout, I thought it was way too late in coming and did not address the most significant needs which were providing the banks with accounting relief for the bad loans they held, which would have allowed them to write down the losses over multiple years. The SEC had the authority to intervene on the accounting and mark to market aspects and actually did so after the cat was out of the bag, additionally it was not well publicized nor was the language forceful and clear.*

To their credit the Fed and the Treasury have done about as much as they can possibly do and think of by injecting liquidity where it is needed, to keep the global financial system afloat. The Treasury also to its credit is continually evaluating the most effective way to utilize the \$700 billion allocation with the latest proposal being a plan to buyout some troubled mortgages where the homeowner is still in the home but having difficulty paying the mortgage. The flexibility given to the Treasury on how to allocate those dollars is a major positive as it will enable them to generate creative ways to tackle the many problems that have and could continue to emerge.

CGFA STAFF: Despite what many experts say many Americans feel as though we are in a recession. Do you believe the designated \$700 billion (allocated for buying default mortgages and failing banks) was sufficient enough to stave off a prolonged recession?

***Orim Graves:** Make no mistake that we are in a recession and have probably been so for at least a quarter. The stimulus package passed in the spring prolonged the impact being felt of the financial crisis on the non-financial economy. No, it was not enough as the Treasury has continued to increase its balance sheet by lending more money and taking in more IOU's from banks, insurance companies, backstopping commercial paper markets, guaranteeing certain money market funds and providing dollars to foreign central banks. I believe the automakers are next in line followed by potentially more nationalizations of banks and insurance companies. The bottom line is that the \$700 billion is augmented by the powers of the Fed and the Treasury to provide additional liquidity into the system.*

The problem that we are facing is a not so virtuous cycle consisting of a lack of liquidity available to consumers and businesses that need it leading to reduced economic activity, leading to layoffs and lower incomes, leading to continued pressure on the banking system as businesses and consumers cannot pay their debts, then forcing the banks to experience higher charge-offs and a reduced capacity to make new loans. Everything I see indicates we are in for a long pretty nasty event (recession). There will be a host of regulatory changes reducing the ability of financial institutions to carry large contingent liabilities without reflecting them on their balance sheet. One of the offshoots of that change will be reduced leverage.

CGFA STAFF: If government intervention continues to become necessary, what implications will that have on our financial system 10 years from now?

Orim Graves: The major implications of the massive US sponsored global bailout (intervention) will be difficult to quantify due to the nature of this event being in uncharted territory. There are some risks that would appear to be readily apparent which are the ability of the US Government to bail out the world potentially as everyone starts to line up at the door for a handout, bailout, buyout, etc. Estimates of current lines and guarantees made available by the US Government are now approaching \$2.5 to \$3.5 trillion (depending on usage). Much of the credit extended may get repaid, however, the short term impact of the increased issuance has driven up long term yields. There may also be a point where the ability of the US to repay its debt may be called in to question which would be the equivalent of tossing a nuclear device into a 5 alarm fire.

When viewed over the longer term, the US government's need to issue more and more debt will begin to crowd out private sector borrowing forcing interest rates to higher levels. Additionally, some elements of the Government's largesse may never get repaid and that number could get substantial, given the haste of the programs that have been established, and the lack of a strong economy in the short term which ultimately would lead to higher burdens for the US tax payer.

CGFA STAFF: What exactly does it mean when a bank collapses?

Orim Graves: A bank collapses when it is no longer considered solvent in that its equity position becomes fully depleted as a result of charge-offs / losses. In the current climate, many banks had either made risky mortgage loans / securities or bought them in which case once the loans / securities failed to perform as expected (pay principal and/or interest). The loan then has to be categorized as a non-performing asset and under recent accounting changes marked to market or priced as a nonperforming asset. The resulting write down in value is then taken as a charge against equity on the balance sheet and if the cumulative amount of the write-down is greater than the amount of stockholder's equity, the result is an insolvent or bankrupt condition where the liabilities are higher than assets.

CGFA STAFF: What are the consequences (if any) for large public pension funds when a bank collapses?

Orim Graves: *The consequences can be significant or minimal depending on the exposure. Pension funds that maintain operating accounts at their custodial banks could be exposed in direct relation to the amount that fund has on deposit less whatever the FDIC guarantee is, which I believe was recently increased. The invested assets of the plan remain in the name of the plan and consequently are not considered assets of the custodial bank.*

The additional area of exposure could occur if an equity or bond manager is holding a shares or bonds issued by the bank, which could then be written down to zero if the bank defaults or collapses. Again, since managers are generally well diversified in their holdings, the potential exposure here would be minimal.

CGFA STAFF: **What is your position in the ongoing defined benefit vs. defined contribution plan debate?**

Orim Graves: *Ah well, what an interesting question in this climate. During the nineties, defined contribution plans were all the rage. Currently, many of those whose primary source of retirement income is based on defined contribution plans are wishing they were in a defined benefit plan. I have always believed there was a place for both and if I had only one to choose, it would be a defined benefit plan for the compelling reason that your retirement benefits are guaranteed so long as the entity holding your pension remains solvent; the subject of which could be the source of a separate discussion in and of itself.*

About ten years ago a colleague who happened to be a well known distinguished actuary postulated, in a paper on demographic trends and the defined benefit vs. defined contribution debate, what would happen to baby boomers (the majority of whom are entering retirement age now and for the next 10 -15 years) if 3-5 years prior to their retirement they encountered a prolonged bear market. The result would be detrimental to their long term prospects to retire on time and could postpone it indefinitely. He felt like Noah felt when he was building the ark as the uninformed laughed and ridiculed the need for such a ship given that the weather had been sunny and dry. The corollary was the happy days of the bull markets made ordinary investors feel like Warren Buffet. As generally happens in the investment world, cycles come and go and we are potentially in a period of a prolonged contraction which could have profound negative effects on defined contribution participants.

CGFA STAFF: **As you may already know, Illinois has the largest (and worst) unfunded liability in the nation and solvency is a huge concern. Are we building an ark that may sink one day?**

Orim Graves: *That is a great question and one that I suggested earlier could be the subject of a lengthy paper in and of itself. I don't believe the Ark will sink so much as it will take creative and determined ways to maintain the program as it was originally designed.*

CGFA STAFF: **Do you think Bush's proposal to use \$250 billion worth of US taxpayer funds to seize stakes in 9 of America's biggest banks (as part of a move to stabilize the US banking system) is a good idea?**

Orim Graves: *It was a move that not only the US, but many governments had to make to sure up their financial institutions. Many of the major banks could not secure the necessary capital they required due to the toxic mortgage securities on their books which were difficult to value and forced more and more write-downs leading to capital losses. This produced capital erosion almost as quickly as the banks were securing it from private investors until finally there were no additional investors willing to take a risk investing in banks, which ultimately left the government as the provider of last resort.*

So yes, the government's capital infusion was necessary to keep the financial system from collapsing; however, a crucial component remains unsolved: How to ease the credit crunch by providing more liquidity to consumers and small businesses at rates that make sense. This is not happening despite the massive amounts of liquidity injected into the system. According to Merrill Lynch the average investment grade spreads on corporate bonds nearly doubled increasing from 317 basis points at Sept 1, to 618 basis points as of Oct 30 the same day the Fed lowered overnight rates to 1%.

CGFA STAFF: Treasury Secretary Henry M. Paulson Jr., recently announced that the nation's banks had until Nov. 14 to apply for government financial support. He also tried to assure Americans that the bailout program might end up making money for the government. He was quoted as saying, "This is an investment — not an expenditure and there is no reason to believe that this program will cost taxpayers anything." Do you believe this?

Orim Graves: *That's a very good and difficult question to answer from this perch. Much of the focus of the bailout program has centered on the purchase of the troubled mortgages so I will start there. The primary component of whether taxpayers come out whole hinges on the simple premise of at what levels will the securities be purchased and whether the TARP asset managers will be successful in restructuring, holding and selling the more attractive parcels at levels higher than their purchase price. As of now, the Treasury is in the middle of their manager selection process.*

As far as the other components of government assistance are concerned, the Treasury should be able to sell its equity stakes in the 9 banks at some level of profit based on the fact that the banking business will be attractive with fewer competitors charging higher spreads on loans. This is beginning to take place as just this week I spoke with a long time friend who happens to be a middle market lender for a major bank in the Midwest who told me he recently made a loan to a company at a rate significantly higher than the loan they booked earlier this year. His comment also provides some evidence that the credit markets are starting to thaw ever so slightly.

Commission staff would be happy to follow up with any questions or concerns. Please email bukolab@ilga.gov with any questions or suggested topics of interest for future monthly features.

Update on the 10th Riverboat License
Eric Noggle, Senior Revenue Analyst

After years of litigation over the failed attempt to relocate the former Emerald Casino license to Rosemont, Illinois, the process of choosing a new location for the 10th riverboat license has once again begun. In July 2008, the Illinois Gaming Board announced that they hired Credit Suisse Securities LLC to handle the bidding process.

The initial step in the new selection process concluded on October 14th,

which was the deadline for the submission of all 10th license applications. At that time, applicants were instructed to represent their “best and final proposal”. On October 15th, the Gaming Board publicly announced the Corporate Entity and Partners of the applicants that submitted applications, their proposed site location, and their up-front license fee amount. The results of these bids, as provided by the Gaming Board, are shown below.

10th License Riverboat Initial Bids			
Applicant Name	Equity Stakeholders	Location	Initial Application Fee (in millions)
Trilliant Gaming Illinois LLC	Alex Yemenidjian, Armenco Holdings LLC, Onex Corporation, Onex Partners GP Inc	West of River Rd. between Balmoral and Bryn Mawr Avenues and fronting I-294 in Rosemont	\$435
Waukegan Gaming LLC	SL BDK Waukegan LLC (Richard Stein, Alan Ludwig, Charles Bidwell, Edward Duffy, Jeffrey Krol), Clairvest Group Inc, Gaming Investment Fund LLC, Michael Pizzuto	The former Lakehurst Mall site near Waukegan Rd. and Route 120 in Waukegan	\$225
SouthSide Casino LLC	David Handlon, James Griffin, Satish Gabhawala, William Krug, Jonathan Harris, John Argianis, William Tsourapas	NW corner of the interchange adjacent to intersection of I-80/294 and Halsted St in Harvey	\$175
Calumet Gaming LLC	Joe Canfora, Gary Grasso	On Torrence Ave., 1 mile north of the intersection of I-80 and I-94 in Calumet City	\$150
Hawthorne Gaming LLC	Joe Canfora, Estate of Thomas Carey	3501 S. Laramie in Stickney, on or near the existing Hawthorne Race Course	\$150
Midwest Gaming & Entertainment LLC	High Plains Gaming LLC, Neil Bluhm, Andrew Bluhm, Leslie Bluhm, Meredith Bluhm-Wolf, Gregory Carlin, 4 Bluhm family related Trusts	NW quadrant of Des Plaines River Road & Devon Ave in Des Plaines	\$100
CCH Gaming Partners LLC	Lafayette Gatling, Marguerite Gatling, Michael Reschke, Steven Craig	At Cicero Ave. and 167th St., near the convergence of I-57 and I-80	\$60
<p>Note: According to the Gaming Board, the information shown above is preliminary information "subject to further review and modification". The Board also notes that there are "many factors set forth in the Riverboat Gambling Act that will be evaluated in selecting three finalists".</p> <p>Source: Illinois Gaming Board at the following website: http://www.igb.state.il.us/whatsnew/081015Summaryofapplicants.pdf.</p>			

Now that the initial applications have been received, the Board states on their website that they will “promptly review and evaluate all Applications submitted

and select the three Finalists as soon as practical.” The Gaming Board has stated that they plan to announce the Finalists before their November 18th

meeting. Within approximately ten days of being selected as a Finalist, each Finalist will make a presentation to the Gaming Board. Shortly after the presentations, the Gaming Board will hold an open session to receive public comment regarding the presentations. Then, with the assistance of Credit Suisse, final negotiations will begin. The winning applicant will then be announced, “as soon as practical thereafter and following an in depth review of the fully negotiated proposals.”

As shown in the table, the highest bid received from the seven applicants was \$435 million from Trilliant Gaming Illinois LLC, which hopes to relocate the 10th riverboat in Rosemont. This bid was \$210 million higher than the next highest bid. However, it must be noted that the bid amount is only one of many factors set forth in the Riverboat Gambling Act that will be evaluated in selecting the winner of the new license. Therefore, the final bid amount that the State will receive from the 10th riverboat license will not be known until the bidding process has been completed.

The value of the initial applicant fees are noteworthy because of how they compare to bids from the previous application process. In 2004, the Isle of Capri Casinos Inc. was selected to

operate the 10th riverboat license with a winning bid of \$518 million, which is significantly higher than the bids just received. Furthermore, according to the FY 2009 Budget Book, “a one-time payment of \$575 million is anticipated in fiscal year 2009 in payment for the license fee from the 10th riverboat license.” Unless changes to the application fees occur during the final stages of the selection process, it appears that the winning bids will be well short of the \$575 million estimate to which the FY 2009 Budget was predicated upon.

While there are numerous variables that applicants must factor in when deciding on the amount of the bid for the 10th license, undoubtedly, the current performance of the existing riverboats weighs heavily. Through September, the nine operating Illinois riverboats’ adjusted gross receipts totals are down 22.7% so far this fiscal year. For the calendar year, receipts are down 19.3%. Regardless of whether this decline has been caused by the economy, the indoor smoking ban, or competition from other states, these recent struggles have no doubt affected the value of the 10th license.

The Commission will continue to monitor the 10th riverboat selection process and will give updates when necessary.

October Revenues Fall Due to Federal Sources and Transfers; Weakness Grows

Jim Muschinske, Revenue Manager

October revenues fell \$369 million as lower reimbursable spending caused federal sources to drop \$239 million. A lower month for transfers also contributed to the monthly retreat. October had the same number of receipting days as last year.

Of those sources experiencing declines, interest income led the falloff with earnings down \$22 million. In what is likely a quirk of receipting, less than \$1 million was deposited into the general funds related to interest earnings. It is still not certain if some of those receipts will be realized in the subsequent month, or if returns were actually that poor. Inheritance tax receipts were off by \$15 million, although the shortfall primarily reflected an extremely large month of a year ago. Sales tax dipped \$10 million, continuing it's less than impressive performance.

While overall receipts fell for the month, a few sources managed to post gains in October. Gross personal income tax grew \$12 million, or \$10 million net of refunds. Public utility taxes increased by \$9 million, while other sources advanced by \$3 million. Gross corporate income taxes eked out a \$1 million gain, as did both the liquor tax and insurance tax.

Overall transfers fell by \$109 million as other transfers dropped by \$84 million due to last year's transfer activity

related to the hospital assessment program. Riverboat transfers continue to disappoint with revenues off \$25 million. As mentioned, federal sources fell \$239 million in October.

Year to Date

Through the first third of FY 2009, overall base revenues are down \$406 million. The majority of the decline is attributed to \$296 million less from federal sources, as well as \$99 million less from transfers. Again, and to reiterate previous monthly briefings, a number of items will serve to restrict revenue growth in FY 2009 [i.e. increased refund percentage, lower miscellaneous transfers, reduced Cook County IGT, less from riverboat transfers, returns from interest income, no expected growth from federal sources]. Those items, when combined with an economy now in recession, will cause already difficult budgetary pressures to build.

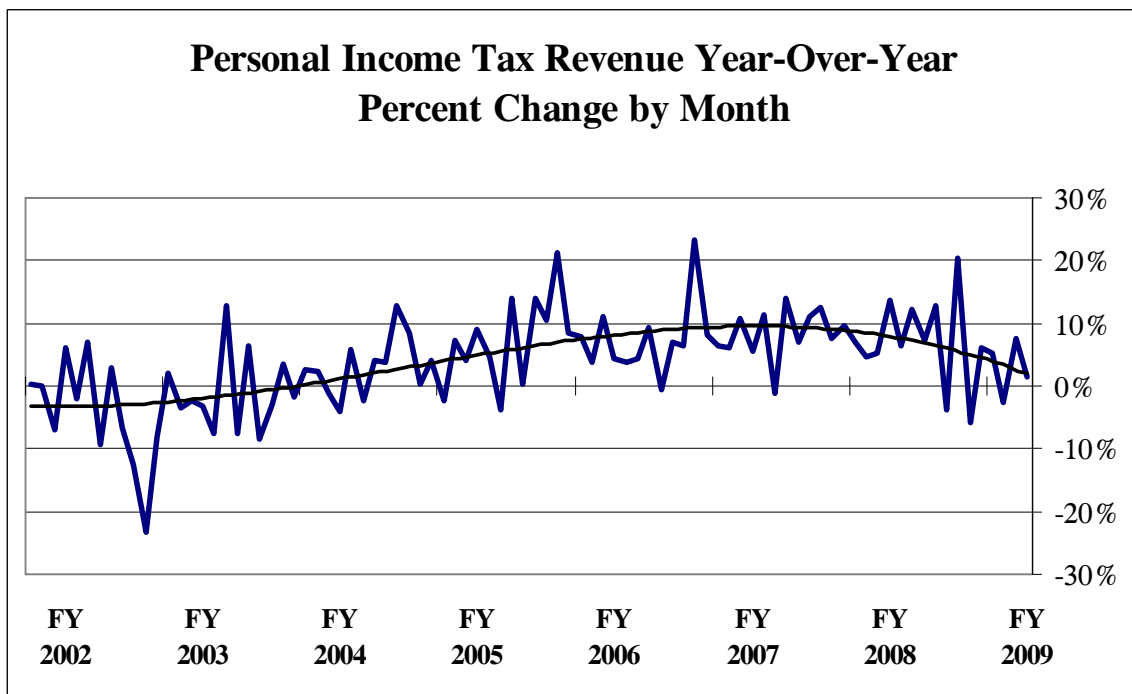
The most closely related economic sources continue their subdued performance. As shown in the following table, rates of growth are very close to those forecast at the end of the spring session. Unfortunately, worsening economic conditions suggest that even these modest rates of growth will be unable to be maintained over the remainder of the fiscal year.

Current Growth Rates vs. Forecasted

<u>Growth Rates (Base)</u>	<u>FY 2009 Thru Oct.</u>	<u>End of Session</u>	
		<u>CGFA May-08</u>	<u>GOMB May-08</u>
Personal Income Tax (Gross)	3.2%	3.2%	3.8%
Corporate Income Tax (Gross)	1.5%	0.0%	0.0%
Sales Tax	1.6%	2.0%	1.7%

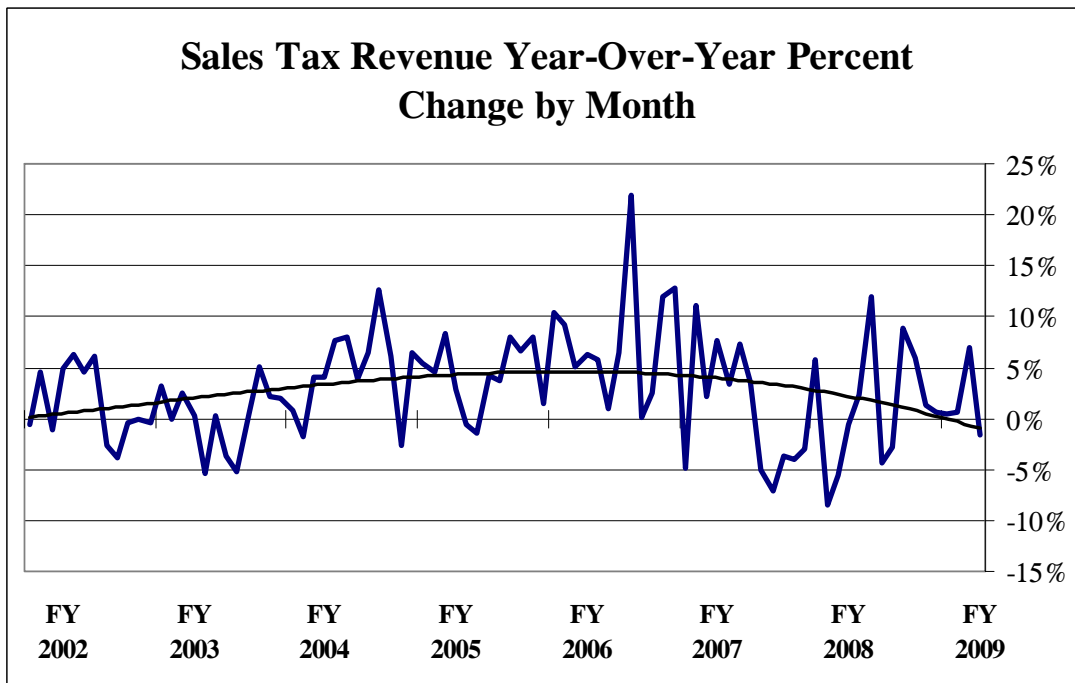
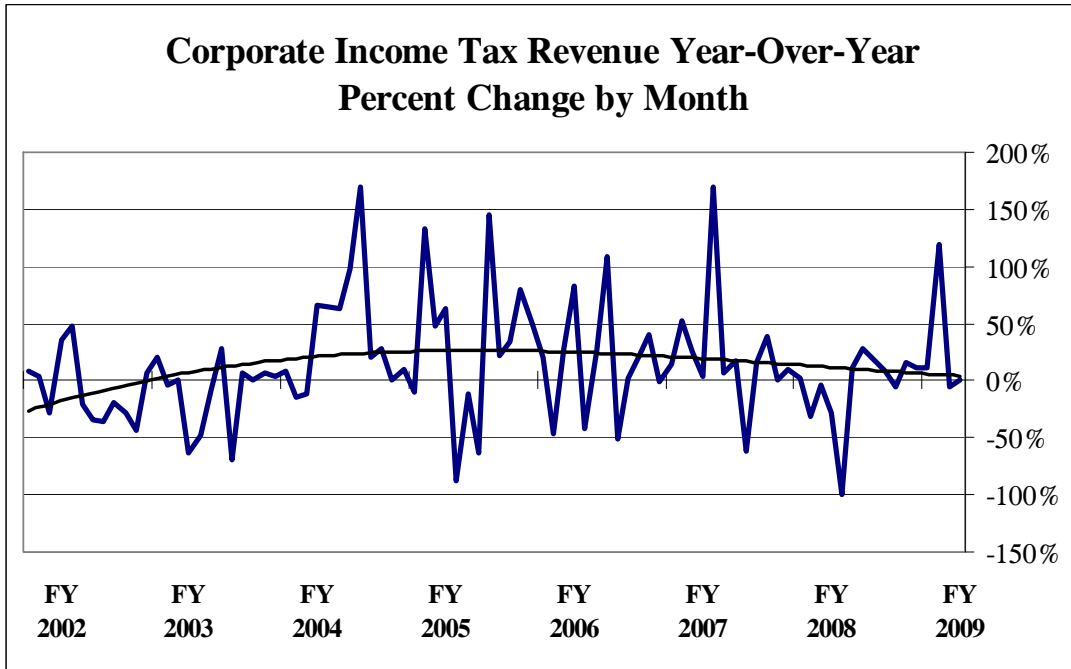
While gross personal income tax receipts are up 3.2% over the first third of the year, as shown in the following chart based on monthly year-over-year percent change, the trend is

decidedly down. If employment measures continue to fall as expected over the coming quarters, there is little reason to believe the current growth rate can be maintained.



Similarly, year-over-year percent change by month for both corporate income tax as well as sales tax point to worsening receipt patterns. Corporate profits have

been decimated over recent months, while consumer sentiments have eroded to record low levels, neither of which bode well for the remainder of the fiscal year.



The Commission anticipates holding a meeting sometime during the upcoming fall veto session. Topics of discussion will include updated economic

as well as revenue outlooks. Please check the Commission's website for information related to posted date and time.

GENERAL FUNDS RECEIPTS: OCTOBER

FY 2009 vs. FY 2008

(\$ million)

<u>Revenue Sources</u>	<u>Oct.</u> <u>FY 2009</u>	<u>Oct.</u> <u>FY 2008</u>	<u>\$</u> <u>CHANGE</u>	<u>%</u> <u>CHANGE</u>
State Taxes				
Personal Income Tax	\$753	\$741	\$12	1.6%
Corporate Income Tax (regular)	57	56	\$1	1.8%
Sales Taxes	605	615	(\$10)	-1.6%
Public Utility Taxes (regular)	102	93	\$9	9.7%
Cigarette Tax	29	29	\$0	0.0%
Liquor Gallonage Taxes	13	12	\$1	8.3%
Vehicle Use Tax	3	3	\$0	0.0%
Inheritance Tax (Gross)	21	36	(\$15)	-41.7%
Insurance Taxes and Fees	3	2	\$1	50.0%
Corporate Franchise Tax & Fees	18	18	\$0	0.0%
Interest on State Funds & Investments	1	22	(\$21)	-95.5%
Cook County IGT	0	0	\$0	N/A
Other Sources	35	32	\$3	9.4%
Subtotal	\$1,640	\$1,659	(\$19)	-1.1%
Transfers				
Lottery	55	55	\$0	0.0%
Riverboat transfers & receipts	50	75	(\$25)	-33.3%
Other	17	101	(\$84)	-83.2%
Total State Sources	\$1,762	\$1,890	(\$128)	-6.8%
Federal Sources	\$283	\$522	(\$239)	-45.8%
Total Federal & State Sources	\$2,045	\$2,412	(\$367)	-15.2%
Nongeneral Funds Distribution:				
Refund Fund				
Personal Income Tax	(\$74)	(\$72)	(\$2)	2.8%
Corporate Income Tax	(\$10)	(10)	\$0	0.0%
Subtotal General Funds	\$1,961	\$2,330	(\$369)	-15.8%
Short-Term Borrowing	\$0	\$0	\$0	N/A
Hopital Provider Fund (cash flow transfer)	\$0	\$300	(\$300)	N/A
Budget Stabilization Fund Transfer	\$0	\$0	\$0	N/A
Total General Funds	\$1,961	\$2,630	(\$669)	-25.4%
CGFA SOURCE: Office of the Comptroller: Some totals may not equal, due to rounding				
5-Nov-08				

GENERAL FUNDS RECEIPTS: YEAR TO DATE

FY 2009 vs. FY 2008

(\$ million)

<u>Revenue Sources</u>	<u>FY 2009</u>	<u>FY 2008</u>	<u>CHANGE FROM FY 2008</u>	<u>% CHANGE</u>
State Taxes				
Personal Income Tax	\$3,135	\$3,037	\$98	3.2%
Corporate Income Tax (regular)	462	455	\$7	1.5%
Sales Taxes	2,457	2,419	\$38	1.6%
Public Utility Taxes (regular)	379	351	\$28	8.0%
Cigarette Tax	117	117	\$0	0.0%
Liquor Gallonage Taxes	55	54	\$1	1.9%
Vehicle Use Tax	11	13	(\$2)	-15.4%
Inheritance Tax (Gross)	92	106	(\$14)	-13.2%
Insurance Taxes and Fees	82	83	(\$1)	-1.2%
Corporate Franchise Tax & Fees	68	85	(\$17)	-20.0%
Interest on State Funds & Investments	24	77	(\$53)	-68.8%
Cook County IGT	13	15	(\$2)	-13.3%
Other Sources	131	134	(\$3)	-2.2%
Subtotal	\$7,026	\$6,946	\$80	1.2%
Transfers				
Lottery	188	203	(\$15)	-7.4%
Riverboat transfers & receipts	185	250	(\$65)	-26.0%
Other	147	246	(\$99)	-40.2%
Total State Sources	\$7,546	\$7,645	(\$99)	-1.3%
Federal Sources				
Total Federal & State Sources	\$9,133	\$9,528	(\$395)	-4.1%
Nongeneral Funds Distribution:				
Refund Fund				
Personal Income Tax	(\$306)	(\$296)	(\$10)	3.4%
Corporate Income Tax	(\$81)	(\$80)	(\$1)	1.3%
Subtotal General Funds	\$8,746	\$9,152	(\$406)	-4.4%
Short-Term Borrowing	\$0	\$1,200	(\$1,200)	N/A
Hospital Provider Fund (cash flow transfer)	\$0	\$300	(\$300)	N/A
Budget Stabilization Fund Transfer	\$276	\$276	\$0	0.0%
Total General Funds	\$9,022	\$10,928	(\$1,906)	-17.4%
SOURCE: Office of the Comptroller, State of Illinois: Some totals may not equal, due to rounding.				
CGFA				5-Nov-08

PENSIONS
FY 2008 Monthly Net Investment Returns
 Dan Hankiewicz, Pension Manager

Table 1 below recaps the monthly investment returns for each of the five State-funded retirement systems (the assets for the State Employees' Retirement System, Judges' Retirement System, and General Assembly Retirement System are managed under the auspices of the Illinois State Board of Investment). The shaded months reflect net investment returns in

FY 2009, which, under current law, will not impact the state's contribution to the retirement systems in FY 2010.

In the November monthly revenue briefing, commission staff will publish the FY 2010 certified contribution for all five State-funded retirement systems, and a recap of the financial condition of the systems as of June 30, 2008.

Table 1					
Monthly Net Investment Returns All State Retirement Systems (Percentage Returns)					
<u>Month</u>	<u>TRS</u>	<u>SERS</u>	<u>SURS</u>	<u>JRS</u>	<u>GARS</u>
September, 2008	-8.16	-6.80	-8.10	-6.80	-6.80
August, 2008	-0.56	0.05	-0.20	0.05	0.05
July, 2008	-1.62	-1.36	-1.20	-1.36	-1.36
June, 2008	-4.75	-5.49	-5.40	-5.49	-5.49
May, 2008	1.49	1.18	1.10	1.18	1.18
April, 2008	3.31	3.11	3.40	3.11	3.11
March, 2008	-1.23	0.05	-0.70	0.05	0.05
February, 2008	-0.67	-1.27	-0.70	-1.27	-1.27
January, 2008	-4.49	-3.72	-3.90	-3.72	-3.72
December, 2007	-0.22	0.52	-0.70	0.52	0.52
November, 2007	-2.72	-2.83	-2.70	-2.83	-2.83
October, 2007	2.38	1.48	2.30	1.48	1.48
September, 2007	3.29	2.61	3.90	2.61	2.61
August, 2007	0.25	0.44	0.50	0.44	0.44
July, 2007	-1.29	-2.12	-1.30	-2.12	-2.12