ILLINOIS ECONOMIC
and
FISCAL COMMISSION

5-YEAR GENERAL FUNDS REVENUE OUTLOOK
FY 2001

AUGUST 2000
703 STRATTON BUILDING
SPRINGFIELD, ILLINOIS 62706

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August, 2000

TO ALL MEMBERS OF THE ILLINOIS GENERAL ASSEMBLY

I am pleased to submit the FY 2001 General Funds Revenue 5-Year Outlook. The purpose of the report is to provide several plausible economic and subsequent revenue conditions of the State over the next five years under the existing tax structure. The report includes three distinct five-year forecasts of economic factors as well as estimates of general funds revenue based on these different economic scenarios—baseline, late recession, and pessimistic. Each of these possibilities has been given a probability of occurring by DRI/McGraw Hill, the Commission's forecasting source with the Baseline a 55% probability; Late Recession a 35% probability and the Pessimistic a 10% probability.

While each of the three forecasts is unique in the factors used to determine the estimates, all three have revenue growth slowing in FY 2001 as a result of the elimination of annualizations and various one-time revenue issues related to FY 2000, and the six-month suspension of the sales tax on motor fuel. Interestingly, all three of the versions have revenues growing at approximately the same rate for the last year of the forecasted period, approximately 4.6%.

The forecasts differ significantly in both growth rates and new dollar growth for the first four years of the forecast period. The baseline estimate assumes continued growth, albeit at a more moderate rate, while the late recession forecast has near-term growth continuing before a recession impacts revenues in FY 2004. The pessimistic scenario also has a recession forecast, however, the impact is felt in FY 2002, and coincides with a natural dip in revenues due to annualization and timing issues.

I invite you to consider these scenarios when reviewing future legislative initiatives. If you have any questions, my staff and I would be glad to assist.

Sincerely,

Dan R. Long
Executive Director

DRL:dkb

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GENERAL FUNDS REVENUE GROWTH: A Look to the Future

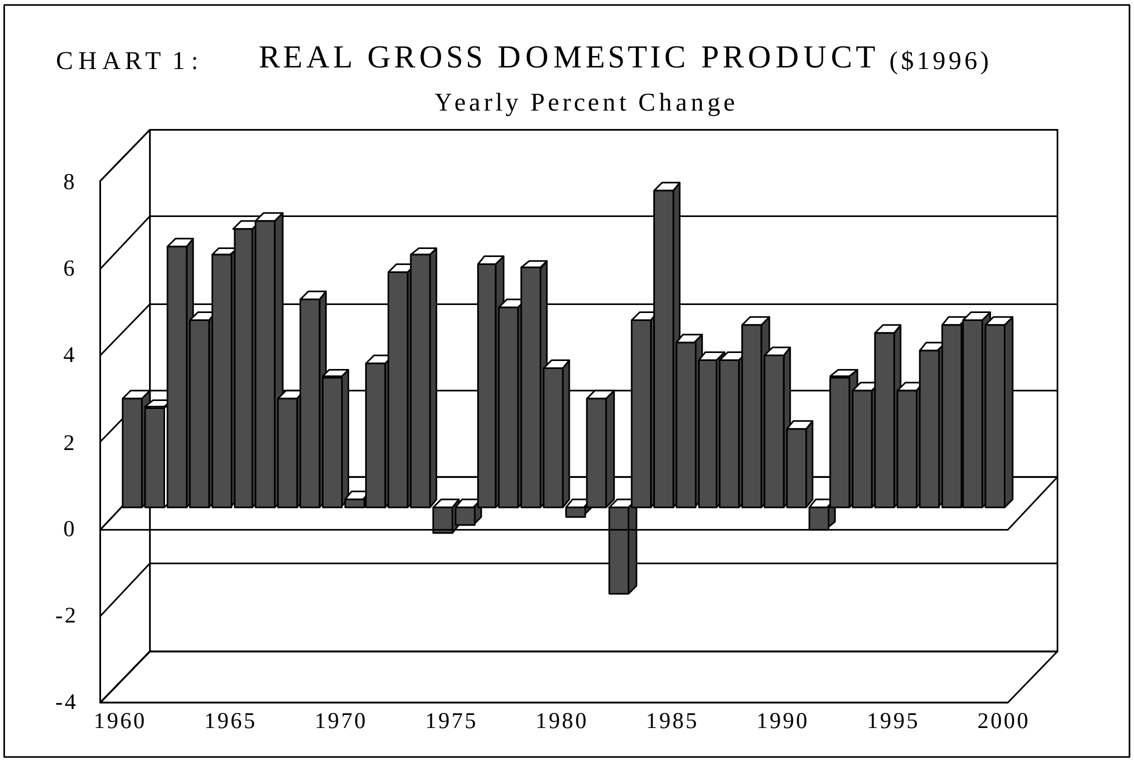
To put future revenue growth projections in proper context, a quick look back at revenue performance is in order. Table 1 below gives a history of general funds revenue dating back to FY 1980. As shown, growth in general funds revenue in Illinois has been significant over the past five years, with growth in general funds revenue, excluding short-term borrowing, averaging $1.25 billion yearly between FY 1996 and FY 2000. (For a more detailed history, see Table 2 on page 3). At the same time, the end-of-year balance has increased over the five-year period, culminating in a record $1.52 billion at the end of FY 2000. (See Table 3 on page 4).

TABLE 1: GENERAL FUNDS HISTORY
FY 1980 to FY 2000
Excludes short-term borrowing ($ in Millions)

Fiscal Year	Total General Funds	$ Change From Prior Year	% Change From Prior Year
1980	$7,442	$387	5.5%
1981	$8,100	$658	8.8%
1982	$8,265	$165	2.0%
1983	$8,287	$22	0.3%
1984*	$9,657	$1,370	16.5%
1985	$10,317	$660	6.8%
1986	$10,583	$266	2.6%
1987	$10,957	$374	3.5%
1988	$11,620	$663	6.1%
1989	$12,133	$513	4.4%
1990	$12,841	$708	5.8%
1991	$13,261	$420	3.3%
1992	$14,032	$771	5.8%
1993	$14,750	$718	5.1%
1994	$15,586	$836	5.7%
1995	$17,002	$1,416	9.1%
1996	$17,936	$934	5.5%
1997	$18,854	$918	5.1%
1998	$19,984	$1,130	6.0%
1999	$21,674	$1,690	8.5%
2000	$23,250	$1,576	7.3%

*Full fiscal year of temporary income tax increase.

However, despite significant recent increases in revenue growth, it would be dangerous to extrapolate this trend into the next five years. This is true for several reasons. First, it is unlikely that the business cycle has been eliminated. There have been 8 recessions since the end of World War II, the latest being between July 1990 and March 1991, and there is no reason to expect that this pattern will not be repeated. (See Chart 1 below). The latest expansion is now a record 111 months old, well surpassing the average of 50 months of expansion in recoveries since the end of World War II, although previous expansions have varied from 106 months, between February 1961 and December 1969, to as short as 12 months, between July 1980 and July 1981. Even so, given this record, it would not be surprising that another recession will occur sometime during the next five years.



A second reason for anticipating more moderate revenue growth over the forecast period is that select revenue sources which have been enhanced and/or restructured over recent years, after an initial growth spurt, have likely matured and are expected to level off. For example, over the last several years a number of tax rates were increased (i.e. public utility telecommunications tax, cigarette tax, and liquor taxes). In addition, some tax sources were restructured (i.e. riverboat gambling taxes, insurance taxes and fees). Finally, intergovernmental transfers have contributed to revenue growth in certain years. While these various changes have had the effect of increasing revenues in recent years, to a great extent, they have now become part of the revenue base. As a result, significant year-over-year growth for those revenue sources will be nearly impossible. In fact, in some circumstances, these revenues may actually level off or even decline in the future.

Finally, repeated analyses by the Economic and Fiscal Commission have shown that trends in Illinois follow that of the nation, although often with a significant lag. Thus, with most forecasts calling for slower growth nationally over the next five years, Illinois is likely to be affected. In assessing revenue over the next five years, we have looked at various possibilities, using the Baseline, Late Recession, and Pessimistic scenarios for the national economy provided by IEFC's forecasting service, DRI/McGraw Hill, and applied to the State revenue prospects calculated by the IEFC. Before looking at projections, it may be helpful to look at Illinois in the context of the nation as a whole.

TABLE 2: GENERAL FUNDS REVENUE
FY 1996-FY 2000
($ in Millions)

Revenue Sources	Actual Receipts FY 1996	Actual Receipts FY 1997	Actual Receipts FY 1998	Actual Receipts FY 1999	Actual Receipts FY 2000
STATE TAXES					
Personal Income Tax	$6,070	$6,552	$7,269	$7,778	$8,273
Corporate Income Tax (Reg.)	$1,209	$1,361	$1,402	$1,384	$1,527
Sales Taxes	$4,798	$4,992	$5,274	$5,609	$6,027
Other Sources	$2,026	$2,285	$2,326	$2,809	$3,050
Subtotal	**$14,103**	**$15,190**	**$16,271**	**$17,580**	**$18,877**
Transfers	**$1,126**	**$1,084**	**$1,076**	**$1,191**	**$1,359**
Total State Sources	**$15,229**	**$16,274**	**$17,347**	**$18,771**	**$20,236**
Federal Sources	**$3,339**	**$3,269**	**$3,323**	**$3,718**	**$3,891**
Total Federal & State Sources	**$18,568**	**$19,543**	**$20,670**	**$22,489**	**$24,127**
NONGENERAL FUNDS DISTRIBUTION:					
Refund Fund					
Personal Income Tax	($401)	($413)	($421)	($552)	($587)
Corporate Income Tax	($231)	($276)	($265)	($263)	($290)
Total General Funds	**$17,936**	**$18,854**	**$19,984**	**$21,674**	**$23,250**
Change from Prior Year	$934	$918	$1,130	$1,690	$1,576
Percent Change	5.5%	5.1%	6.0%	8.5%	7.3%
Short-Term Borrowing	**$200**	**$0**	**$0**	**$0**	**$0**
Total General Funds	**$18,136**	**$18,854**	**$19,984**	**$21,674**	**$23,250**
Change from Prior Year	$834	$718	$1,130	$1,690	$1,576
Percent Change	4.8%	4.0%	6.0%	8.5%	7.3%

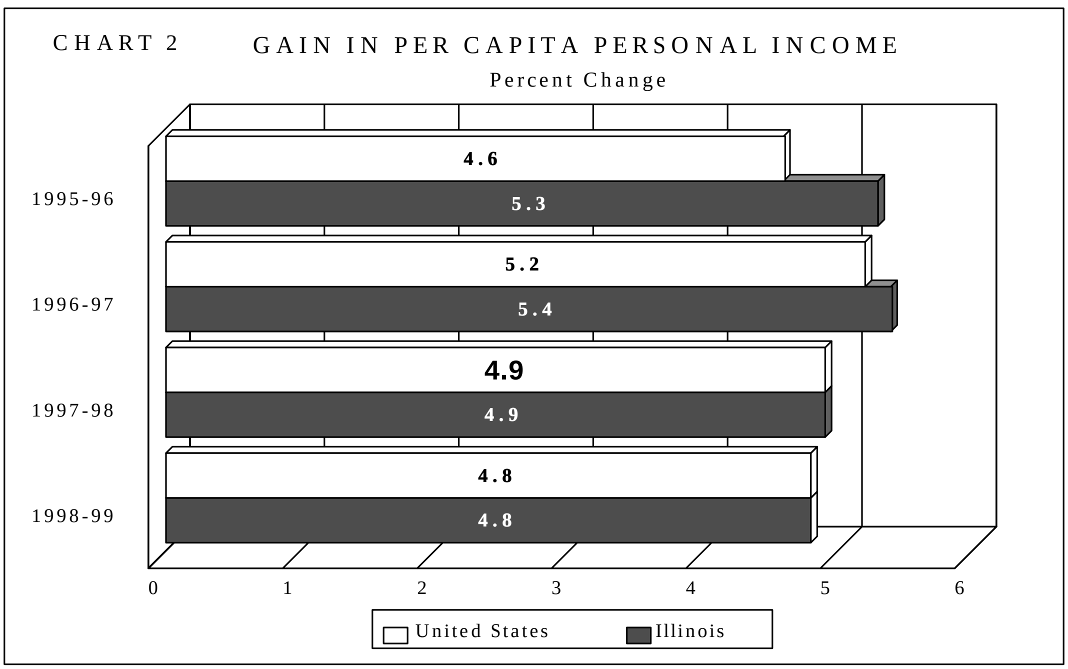
TABLE 3: GENERAL FUNDS OVERVIEW FY 1996 to FY 2000 ($ in millions)					
	FY 1996	FY 1997	FY 1998	FY 1999	FY 2000
Beginning Balance	$331	$426	$806	$1,202	$1,351
Revenue	18,136	18,854	19,984	21,674	23,750
Expenditures	18,041	18,474	19,588	21,525	23,084
Ending Balance	426	806	1,202	1,351	1,517

SOURCE: Illinois Comptroller's Office

ILLINOIS AND THE NATION

Illinois has a population of 12.1 million, ranking it fifth most populace among the 50 states. About 70% of the State's employment base is centered in the greater Chicago area, and due to the importation of workers from neighboring states, the Chicago metro area has an employment base of 4 million workers.

Illinois is a comparatively wealthy state. One of the best measures of a state's well being is personal income on a per-capita basis. In 1999, Illinois' per-capita personal income reached $31,278, highest among the Great Lakes states and holding on to its 7th place in the nation behind the eastern states of Connecticut, New Jersey, Massachusetts, New York, Maryland, respectively, and Colorado. Illinois' per-capita income was about 10% higher than the national average and grew at the average national level in the past two years after outperforming the nation during the previous two years. (See Chart 2).



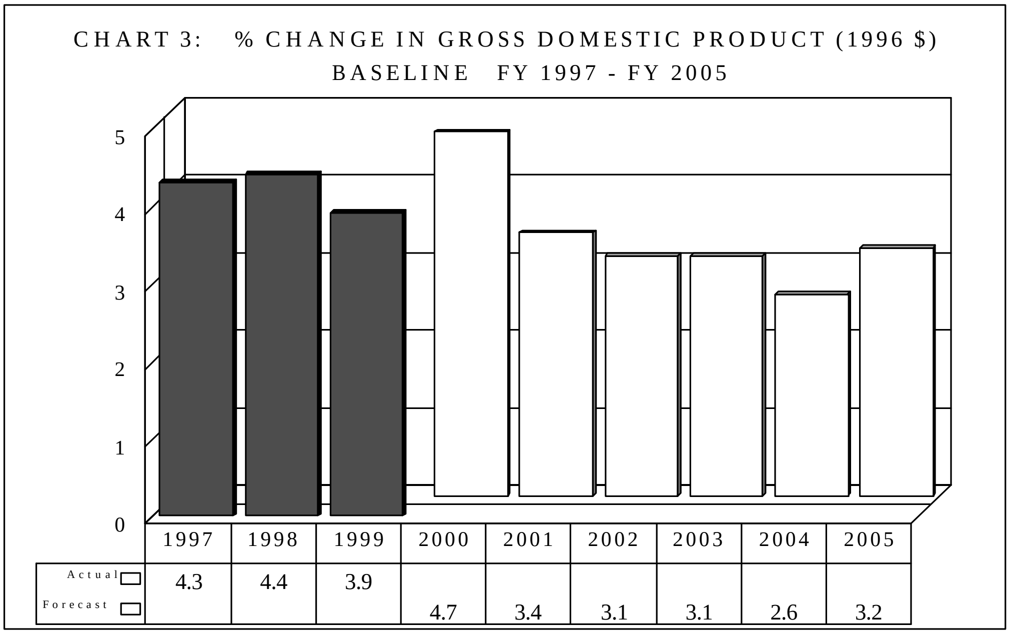
Illinois has a diversified economy with the lowest concentration of manufacturing jobs in the East North Central region, yet it is the most diverse among industries. Chicago serves as the finance and insurance hub of the Midwest and is the region's main transportation, health-care, and education center.

Outside of the Chicago metro area, the State's structure is different. Farming, food processing, government employment, and resident-driven services are the core of business activity in southern Illinois. The western part of the State is closely tied to the transportation and distribution centers served by the Mississippi River. Indeed, the Illinois portion of the St. Louis metro area forms the State's second largest commercial center located on the river's eastern bank. Finally, the Moline and Peoria metro areas have a high concentration of agriculture, construction, and heavy equipment manufacturing.

Looking ahead, Illinois' economic expansion is expected to moderate in response to slower national growth. Tight labor markets and slow population growth will continue to act as constraints. Several positives are emerging, however. Illinois' strong high-tech presence, an improvement in export growth, strong five-year investment programs stemming from Illinois FIRST, and its increased competitive footing due to the phase in of open competition for electric power auger well for continued growth. Nonetheless, weak demographics, a still ailing farm sector, consolidation of banking and insurance industries, and shrinking manufacturing employment all point to a moderation in growth that likely will lag behind that of the nation as a whole.

BASELINE PROJECTIONS: FY 2000 – FY 2005

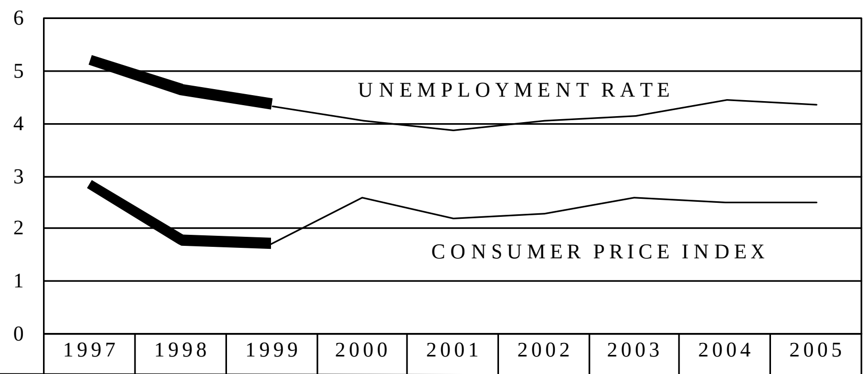
The Baseline projections are based upon DRI/McGraw Hill's latest control, or most likely, economic forecast and is given a 55% chance of occurrence. The forecast calls for continued solid growth through FY 2005 with real GDP averaging 3.4% annually, up from 3.1% during 1974-99. (See Chart 3).



The economic expansion has entered its 10th year, a record, but some signs of age are appearing. Inflation is beginning to reignite both with a pick up in the core rate, which excludes food and energy, as well as in higher employment costs. Even so, DRI believes that recent price data are less worrisome than the headlines suggest, and that the Federal Reserve will be successful in cooling the economy enough to prevent inflation from accelerating.

Consumer spending remains at the heart of the continued expansion. Despite turmoil in the stock market and high oil prices, consumer confidence has recovered nicely. Real incomes are rising, making housing very affordable. Despite the rise in short-term interest rates by the Federal Reserve, mortgage rates have actually started to decline, reflecting both the diminishing supply of new bond issues by the federal government, as budget surpluses continue, and the belief that inflation, while higher than the past two years, will not rage out of control. (See Chart 4 on the following page).

CHART 4: CHANGE IN UNEMPLOYMENT RATE & PRICES
BASELINE FY 1997-FY 2005



	1997	1998	1999	2000	2001	2002	2003	2004	2005
Actual	5.2	4.65	4.37						
Forecast				4.1	3.9	4.1	4.2	4.5	4.4
Actual	2.85	1.79	1.72						
Forecast				2.6	2.2	2.3	2.6	2.5	2.5

Actual —Forecast Actual —Forecast

Labor conditions are expected to ease slightly over the next five years, with the unemployment rate rising from 3.9% in FY 2001 to around 4.5% on average in FY 2004 as shown in Chart 4. With labor relatively scarce and expensive, businesses will continue to spend heavily on equipment and software. No major inventory correction is anticipated as accumulation dropped more sharply than expected last quarter, suggesting some rebuilding needed to restore stock levels and inventory control measures remain in tact.

The foreign exchange value of the dollar remains strong, helping contain upward price pressures, despite a widening trade gap. The strong dollar indeed lessens the competitiveness of U.S. goods abroad and, in turn, is partly responsible for the growing trade disparity. Even so, as oil prices peak and U.S. economic activity slows its pace of expansion, some improvement in the trade gap is anticipated.

On the fiscal front, spending cuts are largely over and some tax cuts are expected no matter who wins the presidency. While the budget surpluses will continue, they may prove lower than the recent enlarged projections made by the CBO. Thus, the recent restrictiveness of fiscal policy will begin to wane.

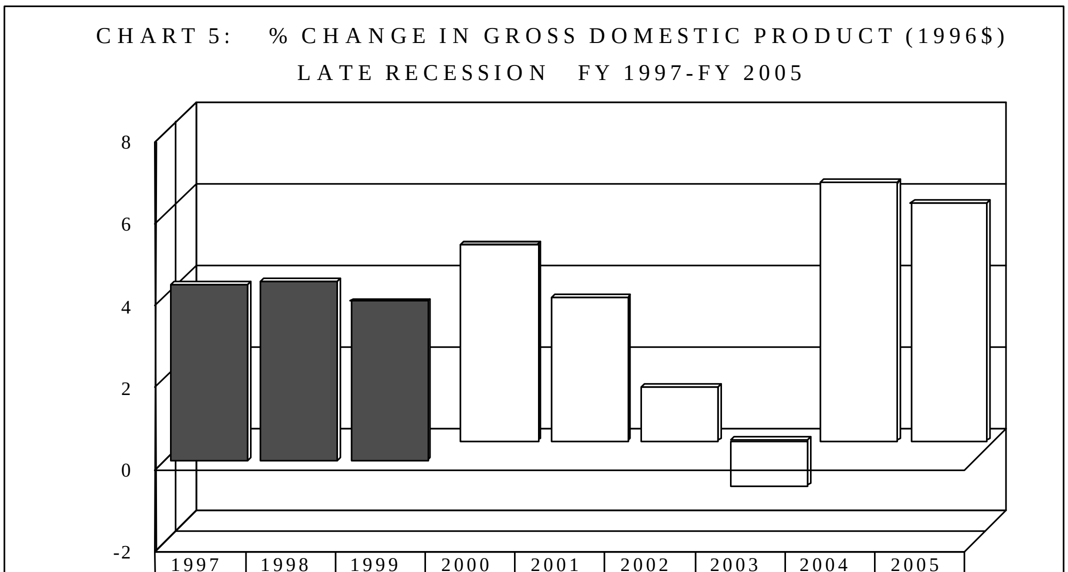
DRI's control or Baseline solution implies that the current expansion will continue through the forecast period. While some signs of age have begun to appear, the imbalances that typically signal a recession have not yet surfaced. The Federal Reserve continues to be alert to economic conditions and it is believed will be successful in achieving a soft landing of the economy.

TABLE 4: BASELINE FORECAST OF THE ECONOMY							
Real (1996 $)	FY99	FY00	FY01	FY02	FY03	FY04	FY05
Gross Domestic Product	3.9%	4.7%	3.4%	3.1%	3.1%	2.6%	3.2%
Personal Consumption	4.9%	5.1%	3.8%	3.2%	2.8%	2.8%	3.2%
Durables	11.4%	11.2%	5.6%	3.6%	3.7%	3.9%	5.8%
Nondurables	4.8%	4.9%	2.7%	2.0%	2.0%	1.9%	2.1%
Services	3.6%	4.0%	3.9%	2.8%	0.3%	3.3%	3.1%
Fixed Investment	9.9%	7.9%	6.0%	4.0%	4.8%	3.7%	5.5%
Exports	1.0%	6.7%	6.8%	8.2%	8.7%	8.2%	7.8%
Imports	10.3%	12.6%	8.4%	5.5%	6.0%	6.7%	7.7%
Government Purchases	2.5%	4.0%	1.4%	1.3%	1.1%	1.4%	1.6%
Federal	0.7%	3.2%	-1.3%	0.1%	-0.3%	0.3%	0.5%
State	3.5%	4.6%	2.8%	1.8%	1.8%	1.9%	2.1%
OTHER MEASURES							
Personal Income	4.6%	3.7%	4.0%	3.0%	2.4%	2.4%	2.9%
Disposable Income	4.0%	3.6%	4.1%	3.6%	2.4%	2.7%	3.3%
Industrial Production	3.1%	4.4%	1.8%	3.3%	1.5%	2.6%	2.8%
Consumer Prices	1.7%	2.6%	2.2%	2.3%	2.6%	2.5%	2.5%
Unemployment Rate (Avg.)	4.4%	4.1%	3.9%	4.1%	4.2%	4.5%	4.4%

LATE RECESSION PROJECTIONS: FY 2000 - FY 2005

The Late Recession Projections are based upon DRI/McGraw Hill's second most-likely economic scenario with a probability of 35%. The assumption is that the U.S. expansion is safe over the near term, but that the Federal Reserve has not responded early enough nor hard enough and inflation, a lagging indicator, already has begun to accelerate.

As pointed out by DRI, every postwar expansion has ended with rising inflation leading eventually to a Federal Reserve overreaction. The resulting higher interest rates usually aided by some external shock, such as accelerating oil prices, or fiscal policy error then causes a recession. This pattern of growth is illustrated in Chart 5.



	1997	1998	1999	2000	2001	2002	2003	2004	2005
Actual	4.3	4.4	3.9						
Forecast				4.8	3.5	1.3	-1.1	6.3	5.8

In this scenario, the CPI exceeds 4% in FY 2002 and averages over 3.5% for the year. The Federal Reserve responds, pushing the federal funds rate above 8% by early FY 2003. The stock market retreats sharply, causing a sharp decline in consumer wealth and higher borrowing costs. Consumer spending and housing both suffer, and the economy falls into a recession in early FY 2003. Unemployment surges and averages close to 7% in FY 2003. (See Chart 6).

Under this scenario, the Federal Reserve delays cutting interest rates because of higher inflation. As GNP slows and turns negative, the monetary authorities eventually loosen policy. Interest rates decline and the economy recovers quickly. Internal imbalances, however, were not severe compared to previous downturns. Because of this, the recession remains relatively mild and brief, and a renewal recovery begins in FY 2004. (See Chart 5 and Table 5).

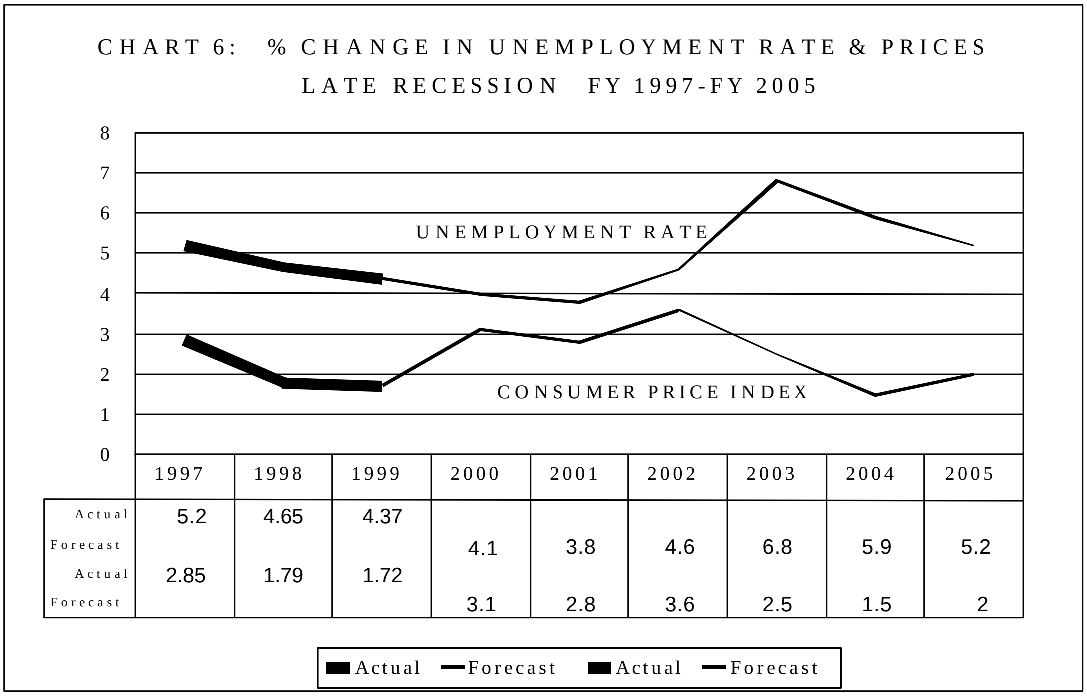
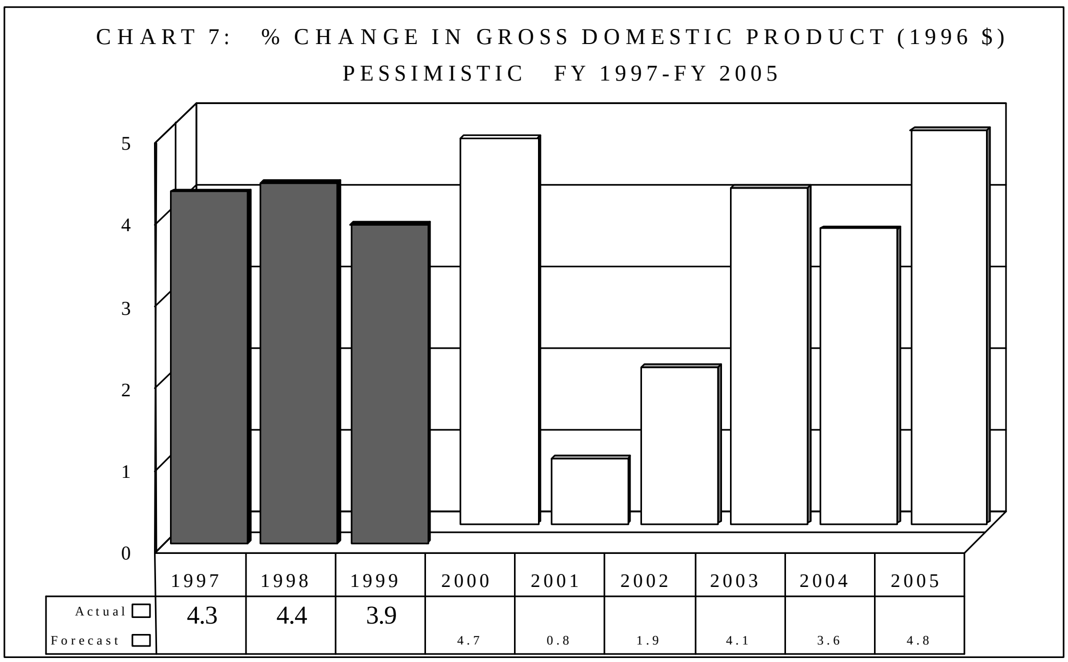


TABLE 5: LATE RECESSION FORECASTS OF THE ECONOMY							
Real (1996 $)	FY99	FY00	FY01	FY02	FY03	FY04	FY05
Gross Domestic Product	3.9%	4.8%	3.5%	1.3%	-1.1%	6.3%	5.8%
Personal Consumption	4.9%	5.1%	3.7%	1.7%	-1.0%	4.4%	5.9%
Durables	11.4%	11.3%	5.3%	-2.3%	-6.2%	13.9%	12.0%
Nondurables	4.8%	4.9%	2.6%	0.9%	-1.5%	3.3%	4.5%
Services	3.6%	4.0%	1.8%	5.9%	3.0%	2.9%	4.6%
Fixed Investment	9.9%	7.9%	6.9%	1.6%	-7.9%	9.0%	10.0%
Exports	1.0%	7.2%	9.2%	7.3%	3.0%	14.3%	11.7%
Imports	10.3%	12.7%	9.8%	4.6%	-6.1%	10.7%	14.0%
Government Purchases	2.5%	4.0%	1.4%	0.8%	0.1%	1.8%	2.4%
Federal	0.7%	3.2%	-1.3%	0.2%	-0.3%	0.4%	0.5%
State	3.5%	4.6%	2.9%	1.1%	0.4%	2.6%	3.3%
OTHER MEASURES							
Personal Income	4.6%	3.7%	3.8%	1.9%	-0.4%	3.6%	5.2%
Disposable Income	4.0%	3.6%	3.8%	2.1%	0.3%	3.5%	4.3%
Industrial Production	3.2%	4.5%	2.3%	0.3%	-1.9%	9.3%	7.9%
Consumer Prices	1.6%	3.1%	2.8%	3.6%	2.5%	1.5%	2.0%
Unemployment Rate (Avg.)	4.4%	4.1%	3.8%	4.6%	6.8%	5.9%	5.2%

PESSIMISTIC PROJECTIONS: FY 2000 - FY 2005

DRI/McGraw Hill's third most-likely economic scenario is entitled its Pessimistic projection. This scenario, which presently has only a 10% likelihood assigned to it by DRI, calls for an early recession sparked largely by a 30-40% fall in the U.S. stock market.

As higher and higher oil prices affect emerging markets, Asia and Latin American economies fall back into recession. As U.S. stock markets drop at the same time, a renewed Asian financial crisis emerges. Confidence falls and U.S. consumers, who make up two-thirds of total spending in the economy, pull back. At the same time, exports slow due to weakening foreign demand. As a result, the economy falls into recession in the months ahead. (See Chart 7).



Because inflation remains relatively low, the Federal Reserve responds quickly to ease the situation, much as it did during the last Asian financial crisis. As interest rates drop, after a mild recession the U.S. economy rebounds in late FY 2002. The lower interest rates revive investment and housing. However, heavy consumer debt burden and heightened unemployment restricts the gains in new consumer spending. (See Chart 8). Thus, the ensuing recovery picks up steam slowly. The change in GDP, its major components, and other key economic variables are illustrated in Table 6.

CHART 8: % CHANGE IN UNEMPLOYMENT RATE & PRICES
PESSIMISTIC FY 2000-FY 2005

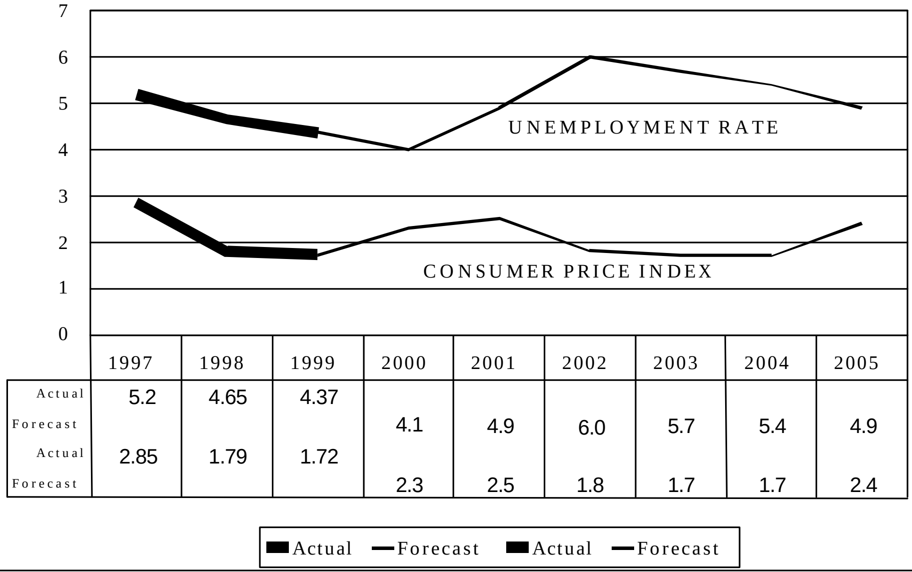


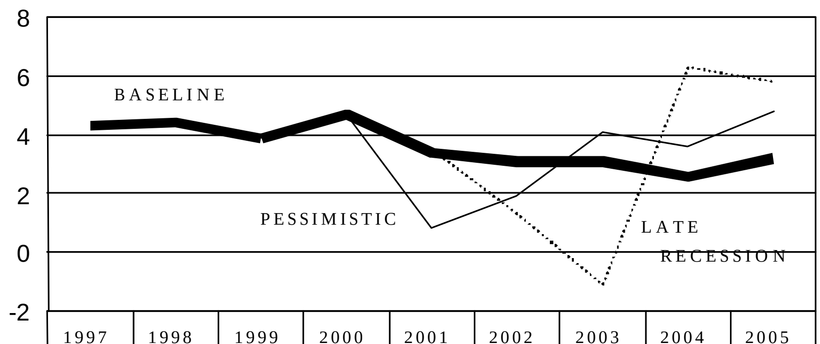
TABLE 6: PESSIMISTIC FORECASTS OF THE ECONOMY

Real (1996 $)	FY99	FY00	FY01	FY02	FY03	FY04	FY05
Gross Domestic Product	3.9%	4.7%	0.8%	1.9%	4.1%	3.6%	4.8%
Personal Consumption	4.9%	5.1%	1.2%	1.7%	3.7%	3.8%	4.7%
Durables	11.4%	11.2%	-3.0%	3.0%	7.8%	7.5%	10.0%
Nondurables	4.8%	4.9%	0.9%	0.6%	2.8%	2.8%	3.3%
Services	3.6%	4.0%	2.2%	2.0%	3.4%	3.6%	4.3%
Fixed Investment	9.9%	7.9%	1.3%	-1.0%	8.1%	7.6%	10.0%
Exports	1.0%	6.7%	5.3%	6.9%	9.4%	8.8%	8.3%
Imports	10.3%	12.6%	4.6%	0.0%	10.6%	9.2%	11.4%
Government Purchases	2.5%	4.3%	0.7%	0.9%	1.1%	1.4%	1.7%
Federal	0.7%	3.2%	-1.3%	0.2%	-0.3%	0.3%	0.5%
State	3.5%	4.6%	2.7%	1.2%	1.9%	2.0%	2.3%
OTHER MEASURES							
Personal Income	4.6%	3.7%	2.4%	1.2%	3.1%	3.2%	4.2%
Disposable Income	4.0%	3.6%	2.9%	1.6%	2.8%	3.6%	4.3%
Industrial Production	3.2%	4.4%	-1.0%	1.8%	5.6%	3.4%	4.4%
Consumer Prices	1.6%	2.3%	2.5%	1.8%	1.7%	1.7%	2.4%
Unemployment Rate (Avg.)	4.4%	4.1%	4.9%	6.0%	5.7%	5.4%	4.9%

COMPARISON OF ECONOMIC FORECASTS: FY 2000 - FY 2005

Chart 9 shows the change in real gross domestic product over the forecast period for each of the three scenarios. The Baseline projection (55% probability) shows continued growth throughout the forecast time horizon, but at a somewhat reduced rate from that experienced during each of the past three years. The Late Recession projection (35% probability) shows diminishing growth in FY 2001 and FY 2002 before developing into a full-fledged recession in FY 2003. This is followed by a bounce back in activity in the final two years of the forecast period. The Pessimistic solution (10% probability) shows an immediate weakening in economic activity followed by a prolonged modest recovery.

CHART 9: CHANGE IN REAL GROSS DOMESTIC PRODUCT
FY 1997-FY 2005

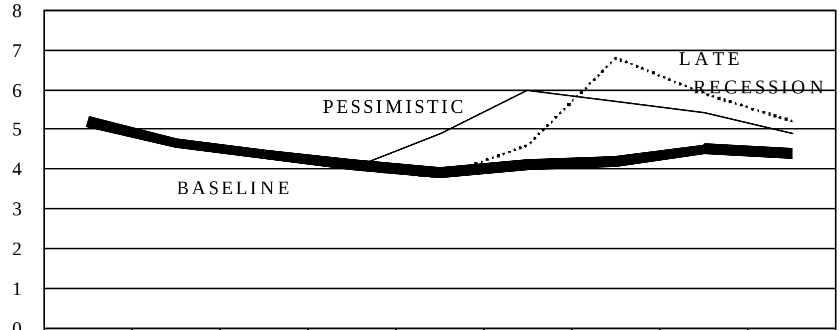


	1997	1998	1999	2000	2001	2002	2003	2004	2005
Actual	4.3	4.4	3.9						
Baseline				4.7	3.4	3.1	3.1	2.6	3.2
Late Recession			3.9	4.8	3.5	1.3	-1.1	6.3	5.8
Pessimistic				4.7	0.8	1.9	4.1	3.6	4.8

Actual Baseline Late Recession Pessimistic

The three economic scenarios give distinctly different employment and inflation forecasts (see Charts 10 and 11). The Baseline solution shows a moderate uptick in both the unemployment and inflation rates, followed by relative stability. The Late Recession solution shows a sharper near-term pick up in inflation followed by a jump in the unemployment rate before both show some improvement toward the end of the forecasted time horizon. Finally, the Pessimistic forecast shows the slowest overall growth and highest average unemployment rate, although inflation is less in this near-term recession, sluggish economic recovery solution.

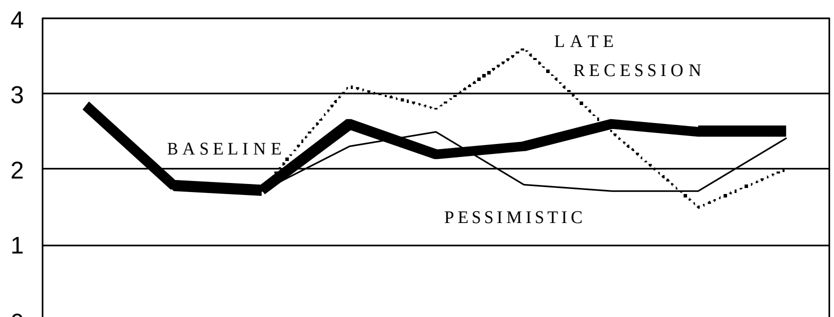
CHART 10: CHANGE IN UNEMPLOYMENT RATES
FY 1997-FY 2005



	1997	1998	1999	2000	2001	2002	2003	2004	2005
Actual	5.2	4.65	4.37						
Baseline				4.1	3.9	4.1	4.2	4.5	4.4
Late Recession			4.37	4	3.8	4.6	6.8	5.9	5.2
Pessimistic				4	4.9	6	5.7	5.4	4.9

Actual Baseline Late Recession Pessimistic

CHART 11: CHANGE IN CONSUMER PRICES
FY 1997-FY 2005



	1997	1998	1999	2000	2001	2002	2003	2004	2005
Actual	2.85	1.79	1.72						
Baseline				2.6	2.2	2.3	2.6	2.5	2.5
Late Recession			1.72	3.1	2.8	3.6	2.5	1.5	2
Pessimistic				2.3	2.5	1.8	1.7	1.7	2.4

Actual Baseline Late Recession Pessimistic

BASELINE REVENUE PROJECTION

The general funds revenue projections for FY 2001 to FY 2005, assuming the baseline economic forecast, increase annually by between 3.5% to 5.6%. Those growth rates equate into a range of new revenue (change from the prior year) of $820 million to $1.352 billion.

As shown in Table 7 on page 18, the largest increase is estimated to occur in FY 2002, when $1.352 billion in new revenue is expected. However, some of that increase can be attributed to annualizations resulting from a return to the taxing of motor fuel sales. Effective July 1, 2000 the State suspended the imposition of its 5% portion of sales tax on motor fuel. By law, the tax will resume on January 1, 2001. It is estimated that the six-month suspension of the tax will reduce sales tax receipts by approximately $175 million in FY 2001. Obviously, if the suspension were to become permanent, the annualized impact could reduce receipts by approximately $350 million.

Other assumptions unrelated to economic conditions include the continuation of the current intergovernmental transfer agreement with Cook County. It is very possible that the federal government may severely restrict or eliminate Illinois' and other states ability to take advantage of such agreements, which serve to maximize federal reimbursement. If restrictions or elimination of the agreements occur, future revenue also would be jeopardized. In addition, in FY 2001, $200 million in Build Illinois General Reserve transfers are estimated to occur and are included in the estimate of 'other sources'. It is estimated that future years include a similar transfer and, therefore, a reduction or change in the amount would impact on subsequent revenues and, resulting growth rates. Finally, in FY 2002 and each year after, the Department of Revenue will adjust the percentage of gross income taxes to be deposited into the Income Tax Refund Fund. A significant change from the current 7.1% for personal income tax and 19% for corporate income tax could result in a large change for total net receipts.

State Taxes

State taxes, which are comprised mostly of income taxes as well as sales taxes, are expected to increase between a low of 3.3% in FY 2001 to a high of 6.0% in FY 2002. Growth rates for personal income tax, after the last year of the phase-in of the doubling of the personal exemption is felt in FY 2001, are estimated to continue strong with a forecasted increase of 5.7% in FY 2002, tapering down to a 4.9% gain in FY 2005. Corporate income tax receipts are estimated to decline 9.8% in FY 2001. While base growth is expected to be essentially flat, the decline is attributed to the large ComEd deposit in the prior year that will not be repeated. Out year corporate income tax growth is forecast to be modest, in the 3.0% range.

Sales tax receipts are estimated to grow only 2.9% in FY 2001 reflecting the six-month suspension on motor fuel sales tax. According to law, the tax will be applied again beginning January 1, 2001. As a result, the estimated growth in sales tax jumps in FY 2002 to 8.5% as the annualizations of the change is felt. From then on, annual rates of growth average nearly 5.5%. While other sources to the general fund experience a significant 9.2% increase in FY 2001 as a result of the aforementioned $200 million Build Illinois General Reserve transfer, subsequent annual rates of growth fall to approximately 3.4%. Other than public utility taxes, and occasional fluctuations in interest income and inheritance tax receipts, most of the other State tax sources exhibit little growth and, in some instances, variances actually fall into negative territory. Cook County IGT levels are forecast to be static but could change significantly as a result of federal restrictions.

Transfers

In FY 2001, overall transfers are forecast to increase only 1.2%. The low growth is the result of other transfers falling 10.5%. In FY 2000, a large transfer from the Income Tax Refund Fund was made, which is not expected to recur in FY 2001. Future year estimates of other transfers are forecast to grow 5% annually. Gaming Fund transfers are expected to grow significantly in FY 2001, up over 21%. However, that growth rate is forecast to slow to an annual increase of 5%. Obviously, if a riverboat were to become operational in Cook County, the forecast would have to be adjusted. Lottery transfers are forecast to be flat over the forecasted horizon.

Federal Sources

Federal sources are estimated to grow annually by approximately 4.5%. Any significant change in reimbursable programs such as Medicaid, however, could significantly impact receipts.

Summary of Baseline Scenario

As described, the Baseline scenario estimates overall healthy growth in the near term, albeit more moderate than in recent years. Growth peaks in FY 2002 at 5.6% and then slows to levels of approximately 4.6%, or about $1.2 billion to $1.3 billion, in new revenue each fiscal year.

TABLE 7: FY 2001 to FY 2005 "Baseline"

Estimated General Funds Receipts

($ million)

Revenue Sources	Estimated FY 2001	Projected FY 2002	Projected FY 2003	Projected FY 2004	Projected FY 2005
State Taxes					
Personal Income Tax	$8,600	9,090	9,572	10,051	10,543
Corporate Income Tax (regular)	1,377	1,418	1,461	1,505	1,550
Sales Taxes	6,200	6,726	7,096	7,479	7,875
Other Sources	3,331	3,442	3,558	3,679	3,805
Subtotal	**$19,508**	**$20,676**	**$21,686**	**$22,713**	**$23,773**
Transfers	**$1,375**	**$1,418**	**$1,463**	**$1,511**	**$1,560**
Total State Sources	**$20,883**	**$22,094**	**$23,149**	**$24,223**	**$25,333**
Federal Sources	**$4,060**	**4,243**	**4,434**	**4,633**	**4,842**
Total Federal & State Sources	**$24,943**	**$26,337**	**$27,583**	**$28,856**	**$30,175**
Nongeneral Funds Distribution:					
Refund Fund					
Personal Income Tax	($611)	($645)	($680)	($714)	($749)
Corporate Income Tax	(262)	($269)	($278)	($286)	($294)
Total General Funds	**$24,070**	**$25,422**	**$26,626**	**$27,857**	**$29,132**
Change from Prior Year	**$820**	**$1,352**	**$1,204**	**$1,231**	**$1,275**
Percent Change	**3.5%**	**5.6%**	**4.7%**	**4.6%**	**4.6%**

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LATE RECESSION PROJECTION

In the Late Recession scenario, general funds continue their healthy growth for the next several years before a national recession, which begins in FY 2003, impacts Illinois in FY 2004. The somewhat delayed effect on the State reflects the normal lag time between changes in national and State activity that has occurred on a rather consistent basis in the past. As a result, revenue growth dips significantly before bouncing back in FY 2005. The Late Recession scenario results in revenue growth projections between 6.1% near term and 2.1% at the time of the recession's effect on Illinois. Year-over-year changes range from $1.469 billion to $564 million. (See Table 8 on page 20.)

<u>State Taxes</u>

The same annualization issues regarding sales tax from motor fuel as well as other risks to the forecasts [IGT, Build Illinois transfers, etc.] also exist in this scenario. State taxes are forecast to increase between 6.7% in FY 2002 to a low of 1.5% in the recession period of FY 2004. Growth rates for personal income tax receipts are estimated to be quite strong, reaching 6.2% in F 2002 before falling to 2.1% during the recession and then rebounding to approximately 5.1% in FY 2005. Corporate income tax receipts perform slightly better than the Baseline forecast through FY 2003 before suffering a 2.0% decline in FY 2004. Receipts then rebound by 4.5% to finish off the forecast period.

Sales tax receipts, after growing only 3.3% in FY 2001 due to the motor fuel tax change, rebound in FY 2002 as a result of a combination of annualizations of the tax change as well as predicted base growth of 6.2%. Growth returns to more modest levels the following year before rising only 1.3% during the recession in FY 2004. Sales tax receipts are quick to rebound and rise 5.5% during the last year of the estimate.

Other sources to the general funds grow slightly higher than the Baseline estimate in the years prior to the recession. However, since the majority of these sources are relatively stagnant, growth rates are still at a modest 3.8% before the recession pulls growth down to only 1.6% in FY 2004. Revenues return to more average rates of growth in FY 2005.

<u>Transfers</u>

Transfers grow slowly in FY 2001 due to the aforementioned lack of a Refund Fund transfer, edging up only 1.2%. Transfers rebound modestly the following year before experiencing a slowdown over the next two fiscal years, culminating in a 1% decline in FY 2004. Lottery transfers remain flat through FY 2002 before experiencing a 5% decline in each of the next two years. Gaming fund transfers rise slowly over the years two and three of the forecast before becoming flat in FY 2004. They rebound again in

FY 2005, albeit at a rather modest 3.5% rate. Other transfers also slow in the same fashion, although are able to maintain their rates of growth slightly better.

Federal Sources

Federal sources average growth of approximately 4.5% through FY 2003 before recessionary pressures on reimbursable programs cause spending to increase. As a result, federal sources actually rise 6.0% during FY 2004 before falling back to lower growth rates the last year.

Summary of Late Recession Scenario

The economy and subsequent revenue growth continues its strong growth through FY 2003 before a national recession occurs. FY 2004 finds the State in a recession and revenue growth is cut by over half before recovering in FY 2005.

TABLE 8: FY 2001 to FY 2005 "Late Recession"

Estimated General Funds Receipts

($ million)

Revenue Sources	Estimated FY 2001	Projected FY 2002	Projected FY 2003	Projected FY 2004	Projected FY 2005
State Taxes					
Personal Income Tax	$8,645	9,181	9,686	9,889	10,394
Corporate Income Tax (regular)	1,430	1,509	1,584	1,552	1,622
Sales Taxes	6,225	6,797	7,157	7,250	7,649
Other Sources	3,331	3,459	3,589	3,647	3,772
Subtotal	**$19,631**	**$20,946**	**$22,016**	**$22,339**	**$23,437**
Transfers	**$1,375**	**$1,420**	**$1,436**	**$1,421**	**$1,463**
Total State Sources	**$21,006**	**$22,366**	**$23,452**	**$23,760**	**$24,899**
Federal Sources	**$4,060**	**4,222**	**4,412**	**4,677**	**4,864**
Total Federal & State Sources	**$25,066**	**$26,588**	**$27,864**	**$28,437**	**$29,763**
Nongeneral Funds Distribution:					
Refund Fund					
Personal Income Tax	($614)	($652)	($688)	($702)	($738)
Corporate Income Tax	(272)	(287)	(301)	(295)	(308)
Total General Funds	**$24,181**	**$25,650**	**$26,876**	**$27,440**	**$28,717**
Change from Prior Year	**$931**	**$1,469**	**$1,226**	**$564**	**$1,277**
Percent Change	**4.0%**	**6.1%**	**4.8%**	**2.1%**	**4.7%**

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PESSIMISTIC REVENUE PROJECTION

The Pessimistic scenario is similar to the Late Recession in that a significant slowdown in economic activity looms on the horizon. However, under this scenario, growth begins to slow almost immediately, the recession hits approximately two years earlier and the rebound in subsequent years is not quite as marked. General funds revenues experience yearly increases of 3.1% to 4.6%, with year-over-year changes ranging from $710 million to $1.233 billion. (See Table 9 on page 22.) While FY 2001 revenues grow slightly less than the Baseline forecast, FY 2002 sees revenue growth at only 3.2%, significantly lower than the 5.6% forecast under the Baseline estimate. After the recession's impact, revenues begin to move back to more normal levels and finish the forecast period at 4.6%, the same rate of growth forecast for FY 2005 under the Baseline scenario.

State Taxes

Again, the same annualization and other risks to the forecast mentioned in earlier scenarios continue to apply under the Pessimistic version, although the impact of a recession in FY 2002 is somewhat muted by the return to a full year of sales tax on motor fuel. Obviously, if the General Assembly decides to continue the suspension of that tax, growth rates would be even lower. Overall State tax revenue growth coincides with the forecasted near-term recession as receipt growth dips to 2.7% in FY 2002 before recovering and finishing the period at a 4.8% rate of growth.

Personal income tax stumbles slightly in FY 2001 and falls further in FY 2002 as growth slows to a meager 2.0%. Recovery begins the following year and rises steadily through the next several years finishing FY 2005 up 5.2%. Similarly, corporate income tax experiences a near-term slowing and actually falls 2.0% in the recession year before slowly recovering to annual rates of growth of approximately 4.0%.

Sales tax receipts follow the same pattern, except they are buoyed in FY 2002 by the annualizations associated with the return of motor fuel sales tax. As stated earlier, if the tax suspension is made permanent, growth rates would be significantly impacted. After the FY 2002 recession, receipt growth picks up and ends FY 2005 up 5.0%.

Other sources to the general funds slow in FY 2002 to a growth rate less than 1%. However, like the rest of the other State tax sources, recovery begins immediately and ends the forecast period with growth similar to the Baseline forecast.

Transfers

Transfers start the forecast period virtually flat and it isn't until FY 2003 that very sluggish growth returns. Lottery transfers suffer losses in the first two years in the range of 2% to 3% before a leveling out of transfers occurs. Gaming Fund transfers continue strong in FY 2001, but then slow the year after, and are flat over the remainder of the forecast period. Other transfers dip in FY 2001, hold flat through the recession of the following year, and then return to annual growth of 5.0% after that.

Federal Sources

Federal sources grow by 4.3% in FY 2001 before recession impacts on reimbursable program spending resulting in FY 2002 receipts increasing by 6.0%. Growth averages approximately 5.0% over the subsequent years.

Summary of Pessimistic Scenario

A near-term recession begins nationally, and while growth in FY 2001 ends lower than the Baseline forecast, State revenues are impacted the most in the following year as growth rates dip to just over 3% before recovering slowly over the next three years. As in the Late Recession scenario, the last year of the forecast period has overall growth very similar to the Baseline forecast, approximately 4.6%.

TABLE 9: FY 2001 to FY 2005 "Pessimistic"
Estimated General Funds
($ million)

Revenue Sources	Estimated FY 2001	Projected FY 2002	Projected FY 2003	Projected FY 2004	Projected FY 2005
State Taxes					
Personal Income Tax	$8,580	8,752	9,119	9,557	10,054
Corporate Income Tax	1,350	1,323	1,349	1,403	1,460
Sales Taxes	6,190	6,556	6,838	7,146	7,503
Other Sources	3,296	3,317	3,415	3,532	3,660
Subtotal	**$19,416**	**$19,948**	**$20,721**	**$21,637**	**$22,676**
Transfers	$1,350	$1,360	$1,383	$1,406	$1,431
Total State Sources	**$20,766**	**$21,308**	**$22,104**	**$23,044**	**$24,107**
Federal Sources	**$4,060**	**4,304**	**4,540**	**4,790**	**5,006**
Total Federal & State Sources	**$24,826**	**$25,611**	**$26,644**	**$27,834**	**$29,113**
Nongeneral Funds Distribution:					
Refund Fund					
Personal Income Tax	($609)	($621)	($647)	($679)	($714)
Corporate Income	(257)	(251)	(256)	(267)	(277)
Total General Funds	**$23,960**	**$24,738**	**$25,740**	**$26,888**	**$28,122**
Change from Prior Year	**$710**	**$778**	**$1,002**	**$1,148**	**$1,233**
Percent Change	**3.1%**	**3.2%**	**4.0%**	**4.5%**	**4.6%**

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COMPARISON OF REVENUE FORECASTS: FY 2001 – FY 2005

Chart 12 illustrates how growth rates differ for each of the three scenarios over the forecast period. As shown, all versions show a dip in FY 2001 as a result of the six-month suspension of the motor fuel sales tax as well as the one-time FY 2000 windfall in corporate profits that will not be repeated in subsequent years. However, growth rates differ significantly for the scenarios during the middle years of the forecast period. While the baseline and late recession estimates forecast growth for FY 2002 between 5.6% and 6.1%, the pessimistic scenario that features a near-term recession has growth rising only 3.2%. However, as the pessimistic version has revenues slowly recovering over the following several years, the late recession scenario has the recession impacting revenues in FY 2004 before quickly recovering the year after. Interestingly, while the middle of the forecast period differs between scenarios, at the end of the fifth year, all three versions converge to approximately the same growth rate, about 4.6% to 4.7%.

CHART 12: % CHANGE IN GENERAL FUNDS REVENUE

Comparison of Projections FY 2001 – FY 2005

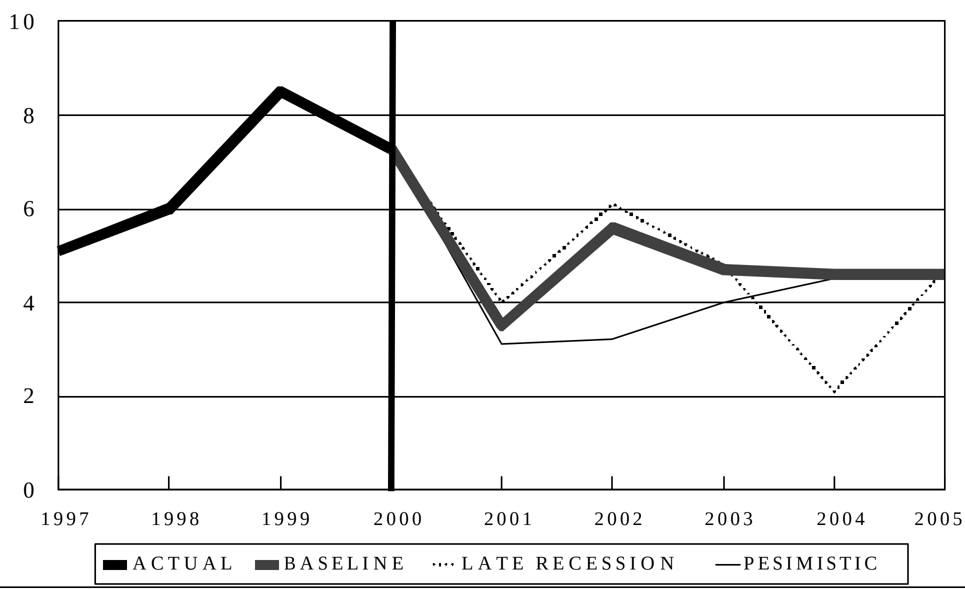

Chart 13 also depicts the differences in these scenarios, however; in this case, the dollar change is illustrated.

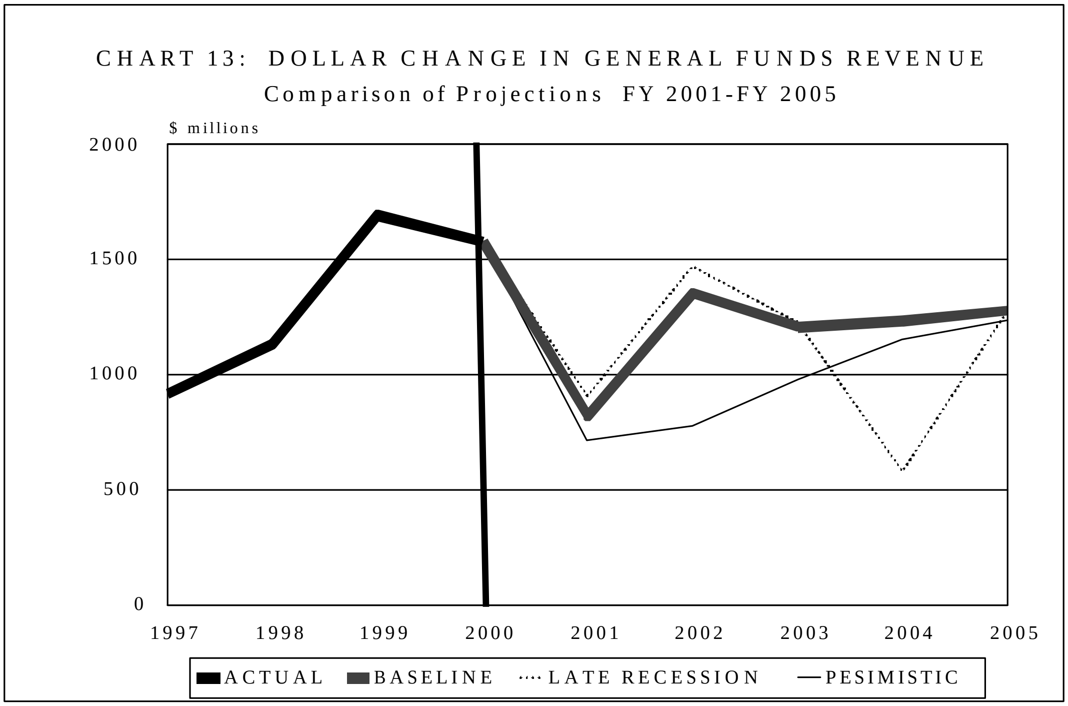

Table 10 on page 25 compares the three different scenarios and depicts total general revenue as well as the accompanying dollar and percentage growth figures as they relate to each version. In keeping with the likelihood of occurrence given each economic forecast, the Baseline revenue projection is given a 55% chance of occurrence, the Late Recession 35%, and the Pessimistic 10%.

TABLE 10: COMPARISON OF GENERAL FUNDS FORECASTS Baseline, Late Recession, and Pessimistic Scenarios ($ in Millions)				
Fiscal Year	**Forecast**	**Total General Funds**	**$ Growth**	**% Growth**
	Baseline	$24,070	$820	3.5%
2001	Late Recession	$24,181	$931	4.0%
	Pessimistic	$23,960	$710	3.1%
	Baseline	$25,422	$1,352	5.6%
2002	Late Recession	$25,650	$1,469	6.1%
	Pessimistic	$24,738	$778	3.2%
	Baseline	$26,626	$1,204	4.7%
2003	Late Recession	$26,876	$1,226	4.8%
	Pessimistic	$25,740	$1,002	4.0%
	Baseline	$27,857	$1,231	4.6%
2004	Late Recession	$27,440	$564	2.1%
	Pessimistic	$26,888	$1,148	4.5%
	Baseline	$29,132	$1,275	4.6%
2005	Late Recession	$28,717	$1,277	4.7%
	Pessimistic	$28,122	$1,233	4.6%

In interpreting the scenarios, it would be prudent to realize that actual revenue performance will likely fall within the parameters set by these versions and not strictly follow one scenario. While a recession is forecast for a particular time in a couple of the forecasts, if a recession does indeed occur, actual timing, duration, and severity may differ from those forecast. However, as alluded to earlier, these forecasts set realistic boundaries within which further discussions of revenue can begin. Obviously, any legislative changes in the various taxes, as well as other factors (i.e. Administration impacts, spending priorities, etc.) could significantly impact revenues.

RevRpt/2000 General Funds Rev 5 Yr Outlook

BACKGROUND

The Illinois Economic and Fiscal Commission, a bipartisan, joint legislative commission, provides the General Assembly with information relevant to the Illinois economy, taxes and other sources of revenue and debt obligations of the State. The Commission's specific responsibilities include:

1) Preparation of annual revenue estimates with periodic updates;

2) Analysis of the fiscal impact of revenue bills;

3) Preparation of "State Debt Impact Notes" on legislation which would appropriate bond funds or increase bond authorization;

4) Periodic assessment of capital facility plans; and

5) Annual estimates of the liabilities of the State's group health insurance program and approval of contract renewals promulgated by the Department of Central Management Services.

The Commission also has a mandate to report to the General Assembly ". . . on economic trends in relation to long-range planning and budgeting; and to study and make such recommendations as it deems appropriate on local and regional economic and fiscal policies and on federal fiscal policy as it may affect Illinois. . . ." This results in several reports on various economic issues throughout the year.

The Commission publishes two primary reports. The "Revenue Estimate and Economic Outlook" describes and projects economic conditions and their impact on State revenues. "The Illinois Bond Watcher" examines the State's debt position as well as other issues directly related to conditions in the financial markets. The Commission also periodically publishes special topic reports that have or could have an impact on the economic well being of Illinois.

These reports are available from:

Illinois Economic and Fiscal Commission
703 Stratton Office Building
Springfield, Illinois 62706
(217) 782-5320
(217) 782-3513 (FAX)

Reports can also be accessed from our Webpage:

http://www.legis.state.il.us/commission/ecfisc/ecfisc_home.html