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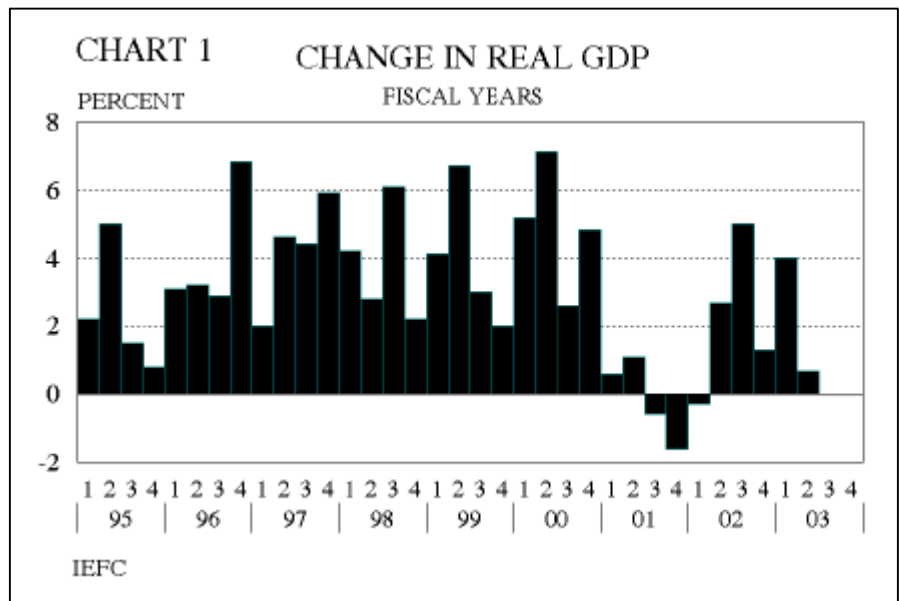
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ECONOMY: Activity Stalls As Uncertainties Mount
 Edward H. Boss, Jr., Chief Economist

The pace of economic activity came to a virtual halt in the final three months of 2002 (second quarter of FY 2003) following four quarters of continuous growth. (See Chart). It is interesting to note that, while most economists have estimated that the recession of 2001 ended sometime toward the end of that year, the official designator of business cycles, the National Bureau of Economic Research, has yet to make such a pronouncement.

As shown in the chart, the pace of real economic activity rose at only a 0.7% annual rate last quarter, well off the 4% rate of the prior quarter and below the 2.4% rate of gain for the year as a whole. The key to even the small advances seen in recent quarters has been the consumer, which normally accounts for roughly two-thirds of total spending. Still, real personal consumption expenditures rose at only a 1% annual rate last quarter as holiday sales disappointed, down from a 4.2% rate in the previous three-month period and 3.1% for the year as a whole.



This slowdown in consumer spending coincided with a weakening in consumer attitudes as measured by both the University of Michigan and Conference Board. Both measures fell further in January. Threat of an impending military conflict, concerns over possible terrorist attacks, as well as sharply declining equity markets undoubtedly were factors behind the decline. The key question is whether this deterioration in confidence will eat further into spending gains in the months ahead.

Federal government spending, largely for defense, accelerated last quarter rising at a real annual rate of more than 10% but state and local consumption slowed to a 1.7% rate from a 2.2% rate in the previous quarter. State and local spending will continue to be constrained by severe budget problems occurring in most states.

The weakest sector of the economy has been the business sector, with declines recorded in real spending for new plant, equipment, and software in 2002. There was a modest 1.5% annual rate of gain in

real business spending last quarter, following eight consecutive quarters of recorded declines. Even so, for the economy to fully recover, it will take a sustained turnaround in business spending and, most importantly, new job creation.

The January Purchasing Manager's Index for the Chicago area rose to 56 in January, its highest level since last June. However, the employment component fell to 45.6 indicating further contraction in this key sector. As shown in the following table, employment in Illinois declined again at year end. The unemployment rate improved only because those seeking jobs fell even faster than those becoming employed.

It will take real gains in employment and income before state revenues can improve. Indeed, in early January the survey of state tax receipts done by ISI, International Strategy and Investment, fell to its lowest level in five months. With both business expansion and consumer spending on hold due to uncertainties, prospects for any improvement in State revenues appear dim at best.

INDICATORS OF ILLINOIS ECONOMIC ACTIVITY			
<u>INDICATORS</u>	<u>DEC. 2002</u>	<u>NOV. 2002</u>	<u>DEC. 2001</u>
Unemployment Rate (Average)	6.4%	6.7%	6.0%
Annual Rate of Inflation (Chicago)	-5.2%	2.6%	2.5%
		<u>% CHANGE</u>	<u>% CHANGE</u>
	<u>LATEST</u>	<u>OVER PRIOR</u>	<u>OVER A</u>
	<u>MONTH</u>	<u>MONTH</u>	<u>YEAR AGO</u>
Civilian Labor Force (thousands) (December)	6,210	-0.5%	-1.8%
Employment (thousands) (December)	5,812	-0.2%	-2.2%
New Car & Truck Registration (December)	46,023	9.6%	-40.4%
Single Family Housing Permits (December)	2,748	-10.9%	28.1%
Total Exports (\$ mil) (November)	3,061	2.0%	15.4%
Chicago Purchasing Managers Index (January)	56.0	8.3%	24.2%

REVENUE

Revenues Worsen

Jim Muschinske, Revenue Manager

After a brief respite in December, monthly revenues fell once again in comparison to last year. In January, general funds revenues were down \$103 million, reflecting the bleak employment situation in this jobless recovery as well as a disappointing holiday season for retailers. Most of the more closely economically-tied sources suffered in January, highlighting a decidedly weak month for virtually all revenue areas. January had the same number of receipting days as the previous year.

Most of the larger revenue sources continued to register setbacks as the new year began. Gross personal income tax posted the largest decrease with revenues down \$68 million (\$66 net of refunds). Sales tax revenues added \$21 million to the monthly decline and public utility taxes were off \$12 million. Corporate franchise taxes fell by \$7 million, interest earnings by \$6 million, and vehicle use tax and inheritance taxes each dipped \$1 million.

Only a few revenue sources managed to post gains in January. Gross corporate income taxes rose by \$8 million (\$5 million net of refunds), while other sources increased by \$3 million. Liquor taxes were able to gain \$1 million for the month.

Overall transfers to the general funds were down \$1 million as the \$9 million increase in Gaming Fund transfers were more than offset by an \$8 million drop in lottery transfers and a \$2 million dip in other transfers. Federal sources managed to rise \$1 million in January.

Year to Date

Through the first seven months of the fiscal year, overall general revenue receipts, (excluding short-term borrowing and Budget Stabilization Fund transfers) are up \$77 million or 0.6%. However, even that very modest growth is not a true representative of this year's revenue performance as it includes approximately \$249 million in one-time interfund and tobacco settlement monies. Absent those items, revenues would actually be down approximately \$172 million, reflecting the continued weak economic activity and uncertainty.

Most of the general funds sources of revenues are below the same period of a year ago, particularly those sources most closely tied to the economy. Gross personal income tax revenues are down \$75 million (\$87 million net of refunds) reflecting the struggling employment picture. Interest on investments has declined \$52 million as a result of low balances as well as record low rates of return. Public utility taxes have declined by \$49 million primarily as a result of struggling telecommunications tax receipts. Gross corporate income tax receipts are down by \$43 million (\$49 million net of refunds) reflecting the lack of corporate profitability. Other tax sources suffering year-to-date losses contributed another \$37 million to the decline.

Very few sources have experienced yearly gains thus far in FY 2003. Other sources are up \$100 million for the year, however, approximately \$88 million of that gain is attributed to last months tobacco monies freed up from a long-term court battle. The Cook County intergovernmental transfer is up \$21 million

due to changes in the agreement. Insurance taxes and fees have continued to perform well and are up \$18 million thus far, while liquor has managed to contribute a modest \$2 million gain.

Overall transfers are up \$298 million thus far through FY 2003. Lottery transfers are down \$1 million, while the Gaming Fund transfer is up \$88 million which reflects the restructured gaming taxes and fees. Other transfers are up \$211 million, primarily the result of \$161 million in one-time interfund transfers executed so far this fiscal year. Federal sources, as expected, are down for the year, off \$43 million through January.

In order to reach the Commission's latest estimate that was calculated in November 2002, overall receipts must grow 3.3% over the remainder of the fiscal year. Clearly, the recovery phase has been extremely weak, especially when measured by job growth and business spending. Making matters worse is the looming cloud of war and uncertainties associated with its outcome and its impact on consumer activity. Absent an unexpected abrupt turnaround in receipt performance over the coming months, it will be near impossible to reach the current forecast. In fact, if revenue performance does not significantly improve, even nominal gains from last year will be difficult, raising the specter of a second consecutive year of revenue decline.

GENERAL FUNDS RECEIPTS: JANUARY

FY 2003 vs. FY 2002

(\$ million)

Revenue Sources	JAN. FY 2003	JAN. FY 2002	\$ CHANGE	% CHANGE
State Taxes				
Personal Income Tax	\$852	\$920	(\$68)	-7.4%
Corporate Income Tax (regular)	38	30	\$8	26.7%
Sales Taxes	544	565	(\$21)	-3.7%
Public Utility Taxes (regular)	106	118	(\$12)	-10.2%
Cigarette Tax	33	33	\$0	0.0%
Liquor Gallonage Taxes	14	13	\$1	7.7%
Vehicle Use Tax	2	3	(\$1)	-33.3%
Inheritance Tax (Gross)	24	25	(\$1)	-4.0%
Insurance Taxes and Fees	4	2	\$2	100.0%
Corporate Franchise Tax & Fees	14	21	(\$7)	-33.3%
Interest on State Funds & Investments	5	11	(\$6)	-54.5%
Cook County IGT	0	0	\$0	0.0%
Other Sources	28	25	\$3	12.0%
Subtotal	\$1,664	\$1,766	(\$102)	-5.8%
Transfers				
Lottery	43	51	(\$8)	-15.7%
Gaming Fund Transfer	29	20	\$9	45.0%
Other	21	23	(\$2)	-8.7%
Total State Sources	\$1,757	\$1,860	(\$103)	-5.5%
Federal Sources	\$305	\$304	\$1	0.3%
Total Federal & State Sources	\$2,062	\$2,164	(\$102)	-4.7%
Nongeneral Funds Distribution:				
Refund Fund				
Personal Income Tax	(\$68)	(\$70)	\$2	-2.9%
Corporate Income Tax	(10)	(7)	(\$3)	42.9%
Subtotal General Funds	\$1,984	\$2,087	(\$103)	-4.9%
Short-Term Borrowing	\$0	\$0	\$0	N/A
Budget Stabilization Fund Transfer	\$0	\$0	\$0	N/A
Total General Funds	\$1,984	\$2,087	(\$103)	-4.9%
IEFC SOURCE: Office of the Comptroller: Some totals may not equal, due to rounding				3-Feb-03

GENERAL FUNDS RECEIPTS: YEAR TO DATE
FY 2003 vs. FY 2002
(\$ million)

Revenue Sources	FY 2003	FY 2002	CHANGE FROM FY 2002	% CHANGE
State Taxes				
Personal Income Tax	\$4,449	\$4,524	(\$75)	-1.7%
Corporate Income Tax (regular)	431	474	(\$43)	-9.1%
Sales Taxes	3,660	3,677	(\$17)	-0.5%
Public Utility Taxes (regular)	579	628	(\$49)	-7.8%
Cigarette Tax	233	233	\$0	0.0%
Liquor Gallonage Taxes	78	76	\$2	2.6%
Vehicle Use Tax	21	23	(\$2)	-8.7%
Inheritance Tax (Gross)	160	205	(\$45)	-22.0%
Insurance Taxes and Fees	133	115	\$18	15.7%
Corporate Franchise Tax & Fees	81	99	(\$18)	-18.2%
Interest on State Funds & Investments	42	94	(\$52)	-55.3%
Cook County IGT	175	154	\$21	13.6%
Other Sources	218	118	\$100	84.7%
Subtotal	\$10,260	\$10,420	(\$160)	-1.5%
Transfers				
Lottery	287	288	(\$1)	-0.3%
Gaming Fund Transfer	378	290	\$88	30.3%
Other	391	180	\$211	117.2%
Total State Sources	\$11,316	\$11,178	\$138	1.2%
Federal Sources	\$2,267	\$2,310	(\$43)	-1.9%
Total Federal & State Sources	\$13,583	\$13,488	\$95	0.7%
Nongeneral Funds Distribution:				
Refund Fund				
Personal Income Tax	(\$356)	(\$344)	(\$12)	3.5%
Corporate Income Tax	(116)	(110)	(\$6)	5.5%
Subtotal General Funds	\$13,111	\$13,034	\$77	0.6%
Short-Term Borrowing	\$700	\$0	\$700	N/A
Budget Stabilization Fund Transfer	\$226	\$226	\$0	N/A
Total General Funds	\$14,037	\$13,260	\$777	5.9%
SOURCE: Office of the Comptroller, State of Illinois: Some totals may not equal, due to rounding.				
IEFC				3-Feb-03

GENERAL FUNDS GROWTH NEEDED TO MEET ESTIMATE
FY 2003 ESTIMATE vs. FY 2002 ACTUAL
(\$ million)

	Nov-02 ESTIMATE FY 2003	FYTD 2003	AMOUNT NEEDED FY 2003 EST.	FYTD 2002	GROWTH NEEDED	% CHANGE
Revenue Sources						
<i>State Taxes</i>						
Personal Income Tax	\$8,245	\$4,449	\$3,796	\$4,524	\$234	6.6%
Corporate Income Tax (regular)	1,075	431	\$644	474	\$75	13.2%
Sales Taxes	6,275	3,660	\$2,615	3,677	\$241	10.2%
Public Utility Taxes (regular)	1,130	579	\$551	628	\$75	15.8%
Cigarette Tax	400	233	\$167	233	\$0	0.0%
Liquor Gallonage Taxes	125	78	\$47	76	\$1	2.2%
Vehicle Use Tax	39	21	\$18	23	\$3	20.0%
Inheritance Tax (Gross)	270	160	\$110	205	(\$14)	-11.3%
Insurance Taxes and Fees	280	133	\$147	115	(\$10)	-6.4%
Corporate Franchise Tax & Fees	164	81	\$83	99	\$23	38.3%
Interest on State Funds & Investments	90	42	\$48	94	\$6	14.3%
Cook County IGT	395	175	\$220	154	\$129	141.8%
Other Sources	320	218	\$102	118	(\$292)	-74.1%
Subtotal	\$18,808	\$10,260	\$8,548	\$10,420	\$471	5.8%
<i>Transfers</i>						
Lottery	585	287	\$298	288	\$31	11.6%
Gaming Fund Transfer	625	378	\$247	290	\$67	37.2%
Other	650	391	\$259	180	(\$14)	-5.1%
Total State Sources	\$20,668	\$11,316	\$9,352	\$11,178	\$555	6.3%
Federal Sources	\$4,075	\$2,267	\$1,808	\$2,310	(\$140)	-7.2%
Total Federal & State Sources	\$24,743	\$13,583	\$11,160	\$13,488	\$415	3.9%
Nongeneral Funds Distribution:						
<i>Refund Fund</i>						
Personal Income Tax	(\$660)	(\$356)	(\$304)	(\$344)	(\$33)	12.2%
Corporate Income Tax	(290)	(116)	(\$174)	(110)	(\$44)	33.8%
Subtotal General Funds	\$23,793	\$13,111	\$10,682	\$13,034	\$338	3.3%
Short-Term Borrowing	\$700	\$700	\$0	\$0	\$0	N/A
Budget Stabilization Fund Transfer	\$226	\$226	\$0	\$226	\$0	N/A
Total General Funds	\$24,719	\$14,037	\$10,682	\$13,260	\$338	3.3%
IEFC						3-Feb-03