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ECONOMY: Doldrums or Dip?

Edward H. Boss, Jr., Chief Economist

The economy is projected to have grown at about a 3% to 3.5% annual rate in the third quarter, up from the 1.3% rate in the second, but well below the 5% rate recorded during the first three months of 2002. However, while 40-year low mortgage interest rates, zero percent auto financing, and rising home values held up consumer spending, it was quite clear from the monthly data that conditions were deteriorating as the third quarter progressed. Thus, the question arises whether the nation's economy was experiencing the often-times repeated summer doldrums or the beginning of a dreaded "double dip" recession.

The consumer, which typically accounts for two-thirds of total spending in the economy, has been the mainstay – keeping the past recession the mildest recorded and contributing mightily to the current recovery. Even so, there is a real concern over how long this pattern can continue.

With rising unemployment, continued layoffs, and somewhat disappointing earnings, not to mention the plunge to 4-year lows in the stock market, the consumer may be petering out. As evidence of this car sales, which had surged in August, softened in September while the nation's chain store sales slipped and the nation's largest retailer, Wal-Mart, issued a sales warning, lowering its forecast for same-store sales. Further adding to the concern over consumer spending gains was the release of August figures showing income rose 0.4%, less than the 0.5% expected, while spending inched up 0.3%, much less than the 0.5% anticipated. In July, income had held unchanged although spending had surged by 1%.

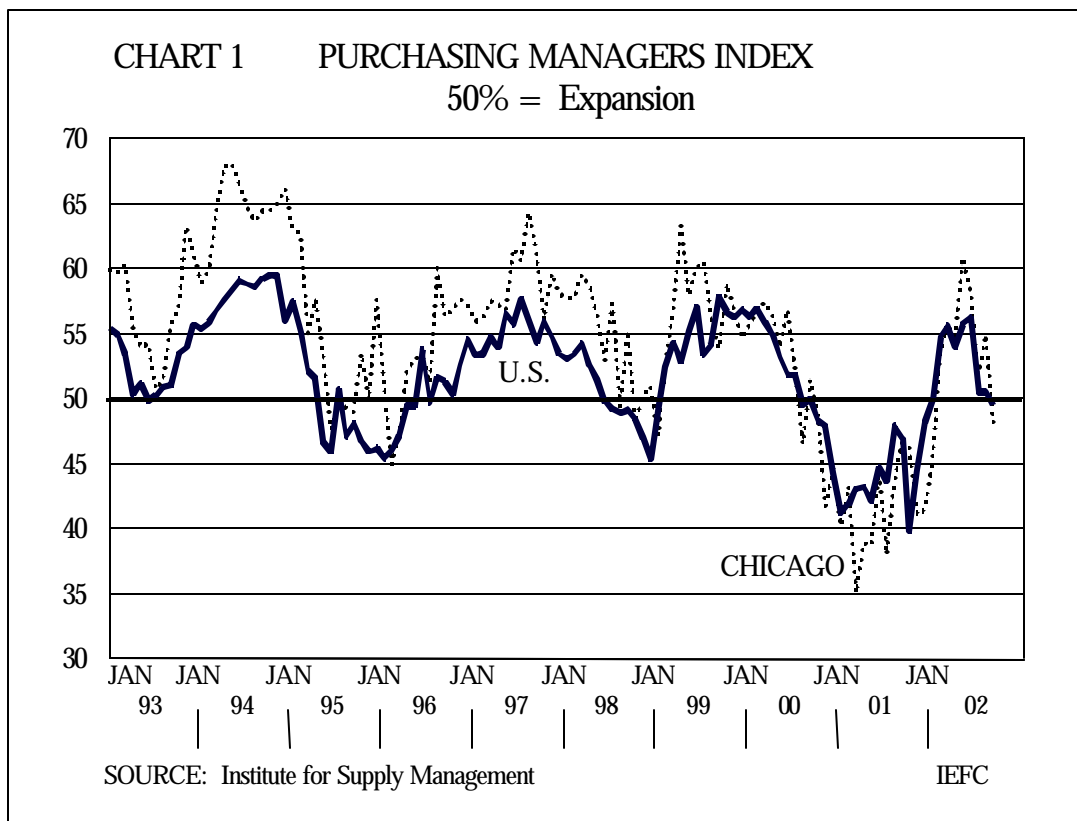
If the consumer slows its spending, the economy will have to turn to other sectors – business, government, or net exports. Government spending, spurred by the war on terrorism, is increasing at the federal level although severe budget constraints are limiting state spending. U.S. exports are rising as other nations' economies are improving in concert with the U.S. recovery, although at an even lesser rate of advance. And, the outlook for increased business spending remains cloudy.

Chart 1 shows that after seven consecutive months of expansion (a number exceeding 50%), the Institute of Supply Management reported a dip in September with the indexing down to 49.5%. This report followed one issued the day before by the Chicago Purchasing Managers whose index fell to 48.1% from 54.9% in August. This renewed contraction in the manufacturing sector, which was hardest hit during the last recession, is causing market concern over the business outlook.

Adding to this concern is the continuing work stoppage which has closed U.S. West Coast ports chocking off trade with Asia. This stoppage is estimated to cost the U.S. economy \$1 billion per day and if extended will cut into goods

available during the upcoming holidays, cutting into sales.

Despite the summer deterioration in the economy, however, odds favor continued, albeit moderate, improvement. Interest rates are at the lowest level in decades and, given the lags associated with monetary policy, are yet to be fully reflected. Moreover, the Federal Reserve is poised to move further should economic weakness persist. Fiscal policy remains stimulative and the stock market already appears to have undergone a major correction. While uncertainties persist and IEFEC's forecasting service has raised the odds on a pessimistic outcome from 25% in August to 30% in September, the odds still favor further economic growth in the months ahead.



INDICATORS OF ILLINOIS ECONOMIC ACTIVITY

<u>INDICATORS</u>	<u>August 2002</u>	<u>July 2002</u>	<u>August 2001</u>
Unemployment Rate (Average)	6.2%	6.7%	5.5%
Annual Rate of Inflation (Chicago)	2.7%	-5.9%	2.0%
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	<u>LATEST</u>	<u>% CHANGE</u>	<u>% CHANGE</u>
	<u>MONTH</u>	<u>OVER PRIOR</u>	<u>OVER A</u>
	<u>MONTH</u>	<u>MONTH</u>	<u>YEAR AGO</u>
Civilian Labor Force (thousands) (August)	6,261	-0.3%	-1.1%
Employment (thousands) (August)	5,871	0.2%	-1.8%
New Car & Truck Registration (August)	70,369	5.4%	3.6%
Single Family Housing Permits (August)	3,692	0.5%	-4.2%
Total Exports (\$ mil) (July)	2,607	-3.5%	7.4%
Chicago Purchasing Managers Index (Sept.)	48.1	-12.4%	3.2%

REVENUE

Revenues Slide in September
Jim Muschinske, Revenue Chief

Overall general funds revenues fell \$73 million in September as a poor month for federal sources dragged down what otherwise was a flat month. Revenue performance was mixed this past month as there were as many sources up as there were down. September did benefit from one extra receipting day this fiscal year.

Of those sources experiencing declines, gross personal income taxes suffered the largest drop with receipts down \$17 million. Inheritance tax revenues gave up \$13 million, while both cigarette tax and interest income each dipped \$7 million. Other sources were down \$2 million for the month and corporate franchise taxes eased \$1 million.

Offsetting much of the above declines were advancements in several areas. Sales tax managed to gain \$13 million in September, followed closely by a \$12

million increase in insurance tax receipts. Both public utility taxes and liquor taxes rose by \$4 million each. Gross corporate income taxes eked out a \$3 million increase, while vehicle use tax contributed a \$1 million gain.

Overall transfers were up \$20 million for the month. Gaming Fund transfers generated a \$10 million gain and other transfers rose \$15 million. Offsetting some of that advance was a \$5 million dip in Lottery transfers. Again, federal sources suffered the most as receipts fell \$74 million in September.

Year to Date

Despite two consecutive drops in monthly receipts, through the first quarter of FY 2003 (excluding short-term borrowing and Budget Stabilization Fund transfers), overall revenues are up \$227 million. However, most of that increase is the result of strong July federal sources and interfund transfers. Excluding federal sources and other transfers, year-to-date revenues continue to be essentially flat.

Through the first quarter, revenues from interest on State funds and investments have fared the worst, dropping \$31 million. Gross personal income tax were off \$27 million, while inheritance tax has fallen \$22 million. Other sources experienced declines totaling \$9 million.

Sales taxes have managed to post \$28 million in gains, while insurance taxes have picked up \$15 million. Other state tax sources experiencing gains totaled \$15 million.

Overall transfers are up \$201 million as a result of interfund transfers and the

changes in the riverboat tax structure. Federal sources, despite poor August and September receipts, are still up \$72 million.

Excluding short-term borrowing and Budget Stabilization Fund transfers, revenues need to grow 3.2% over the remaining nine months of the fiscal year to reach the Commission's estimate. While that needed growth rate is lower than the current year-to-date change of 4.3%, revenues are a concern and will continue to be monitored closely. The Commission has scheduled a meeting in late November at which time any required revisions will be presented.

GENERAL FUNDS RECEIPTS: SEPTEMBER

FY 2003 vs. FY 2002
(\$ million)

<u>Revenue Sources</u>	<u>SEPT.</u> <u>FY 2003</u>	<u>SEPT.</u> <u>FY 2002</u>	<u>\$</u> <u>CHANGE</u>	<u>%</u> <u>CHANGE</u>
State Taxes				
Personal Income Tax	\$696	\$713	(\$17)	-2.4%
Corporate Income Tax (regular)	165	162	\$3	1.9%
Sales Taxes	507	494	\$13	2.6%
Public Utility Taxes (regular)	72	68	\$4	5.9%
Cigarette Tax	26	33	(\$7)	-21.2%
Liquor Gallonage Taxes	10	6	\$4	66.7%
Vehicle Use Tax	4	3	\$1	33.3%
Inheritance Tax (Gross)	20	33	(\$13)	-39.4%
Insurance Taxes and Fees	54	42	\$12	28.6%
Corporate Franchise Tax & Fees	12	13	(\$1)	-7.7%
Interest on State Funds & Investments	5	12	(\$7)	-58.3%
Cook County IGT	23	23	\$0	0.0%
Other Sources	13	15	(\$2)	-13.3%
Subtotal	\$1,607	\$1,617	(\$10)	-0.6%
Transfers				
Lottery	40	45	(\$5)	-11.1%
Gaming Fund Transfer	60	50	\$10	20.0%
Other	30	15	\$15	100.0%
Total State Sources	\$1,737	\$1,727	\$10	0.6%
Federal Sources	\$265	\$339	(\$74)	-21.8%
Total Federal & State Sources	\$2,002	\$2,066	(\$64)	-3.1%
Nongeneral Funds Distribution:				
Refund Fund				
Personal Income Tax	(\$56)	(\$54)	(\$2)	3.7%
Corporate Income Tax	(44)	(37)	(\$7)	18.9%
Subtotal General Funds	\$1,902	\$1,975	(\$73)	-3.7%
Short-Term Borrowing	\$0	\$0	\$0	N/A
Budget Stabilization Fund Transfer	\$0	\$0	\$0	N/A
Total General Funds	\$1,902	\$1,975	(\$73)	-3.7%
IEFC SOURCE: Office of the Comptroller: Some totals may not equal, due to rounding				2-Oct-02

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	\$1,791	\$1,818	(\$27)	-1.5%
Corporate Income Tax (regular)	214	206	\$8	3.9%
Sales Taxes	1,561	1,533	\$28	1.8%
Public Utility Taxes (regular)	232	233	(\$1)	-0.4%
Cigarette Tax	93	100	(\$7)	-7.0%
Liquor Gallonage Taxes	31	25	\$6	24.0%
Vehicle Use Tax	9	10	(\$1)	-10.0%
Inheritance Tax (Gross)	76	98	(\$22)	-22.4%
Insurance Taxes and Fees	63	48	\$15	31.3%
Corporate Franchise Tax & Fees	33	32	\$1	3.1%
Interest on State Funds & Investments	19	50	(\$31)	-62.0%
Cook County IGT	77	77	\$0	0.0%
Other Sources	47	47	\$0	0.0%
Subtotal	\$4,246	\$4,277	(\$31)	-0.7%
Transfers				
Lottery	119	118	\$1	0.8%
Gaming Fund Transfer	160	130	\$30	23.1%
Other	226	56	\$170	303.6%
Total State Sources	\$4,751	\$4,581	\$170	3.7%
Federal Sources	\$996	\$924	\$72	7.8%
Total Federal & State Sources	\$5,747	\$5,505	\$242	4.4%
Nongeneral Funds Distribution:				
Refund Fund				
Personal Income Tax	(\$143)	(\$139)	(\$4)	2.9%
Corporate Income Tax	(58)	(47)	(\$11)	23.4%
Subtotal General Funds	\$5,546	\$5,319	\$227	4.3%
Short-Term Borrowing	\$700	\$0	\$700	N/A
Budget Stabilization Fund Transfer	\$226	\$0	\$226	N/A
Total General Funds	\$6,472	\$5,319	\$1,153	21.7%
SOURCE: Office of the Comptroller, State of Illinois: Some totals may not equal, due to rounding.				
IEFC				2-Oct-02

GENERAL FUNDS GROWTH NEEDED TO MEET ESTIMATE

FY 2003 ESTIMATE vs. FY 2002 ACTUAL

(\$ million)

Revenue Sources	July-02 ESTIMATE FY 2003	FYTD 2003	AMOUNT NEEDED FY 2003 EST.	FYTD 2002	GROWTH NEEDED	% CHANGE
State Taxes						
Personal Income Tax	\$8,405	\$1,791	\$6,614	\$1,818	\$346	5.5%
Corporate Income Tax (regular)	1,126	214	\$912	206	\$75	9.0%
Sales Taxes	6,365	1,561	\$4,804	1,533	\$286	6.3%
Public Utility Taxes (regular)	1,165	232	\$933	233	\$62	7.1%
Cigarette Tax	400	93	\$307	100	\$7	2.3%
Liquor Gallonage Taxes	125	31	\$94	25	(\$3)	-3.1%
Vehicle Use Tax	39	9	\$30	10	\$2	7.1%
Inheritance Tax (Gross)	270	76	\$194	98	(\$37)	-16.0%
Insurance Taxes and Fees	280	63	\$217	48	(\$7)	-3.1%
Corporate Franchise Tax & Fees	169	33	\$136	32	\$9	7.1%
Interest on State Funds & Investments	160	19	\$141	50	\$55	64.0%
Cook County IGT	395	77	\$318	77	\$150	89.3%
Other Sources	320	47	\$273	47	(\$192)	-41.3%
Subtotal	\$19,219	\$4,246	\$14,973	\$4,277	\$753	5.3%
Transfers						
Lottery	585	119	\$466	118	\$29	6.6%
Gaming Fund Transfer	625	160	\$465	130	\$125	36.8%
Other	650	226	\$424	56	\$27	6.8%
Total State Sources	\$21,079	\$4,751	\$16,328	\$4,581	\$934	6.1%
Federal Sources	\$4,075	\$996	\$3,079	\$924	(\$255)	-7.6%
Total Federal & State Sources	\$25,154	\$5,747	\$19,407	\$5,505	\$679	3.6%
Nongeneral Funds Distribution:						
Refund Fund						
Personal Income Tax	(\$672)	(\$143)	(\$529)	(\$139)	(\$53)	11.1%
Corporate Income Tax	(304)	(58)	(\$246)	(47)	(\$53)	27.5%
Subtotal General Funds	\$24,178	\$5,546	\$18,632	\$5,319	\$573	3.2%
Short-Term Borrowing	\$700	\$700	\$0	\$0	\$0	N/A
Budget Stabilization Fund Transfer	\$226	\$226	\$0	\$0	(\$226)	N/A
Total General Funds	\$25,104	\$6,472	\$18,632	\$5,319	\$347	1.9%
IEFC						2-Oct-02