



Commission on Government Forecasting and Accountability

MONTHLY BRIEFING

OCTOBER 2007

<http://www.ilga.gov/commission/cgfa2006/home.aspx>

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ECONOMY: Over a Barrel?

Edward H. Boss, Jr., Chief Economist

The price of oil jumped toward the end of October, exceeding \$90 a barrel for the first time and raising fears of a triple digit price. This added to concerns over the future strength of the economy already weakened from the continuing impact of the bursting of the housing bubble; continued fallout from the credit crisis; a renewed sharp decline in the value of the dollar, and waning consumer confidence prior to the important holiday buying season. This has led some prognosticators to feel that record high oil prices may be the final event to push the economy over a barrel, again increasing their odds of a recession developing.

Some evidence of the impact of these developments in the economy has been a slowing in employment gains both nationally and in Illinois. Even so, while new job growth has slowed, the national unemployment rate has shown little change from a year earlier and the economy had regained all of the jobs lost during the last recession by early 2005. In contrast, Illinois' unemployment rate is up almost a full percent from a year earlier and has yet to recoup all of the jobs lost during the previous recession. More important, the gain in Illinois' employment has begun to track on a slowing path. As shown in the chart on the following page, September was the fourth consecutive month that gains on a year-over-year basis weakened, from a gain of 64,000 jobs reported in May to 43,600 on the same basis by September 2007.

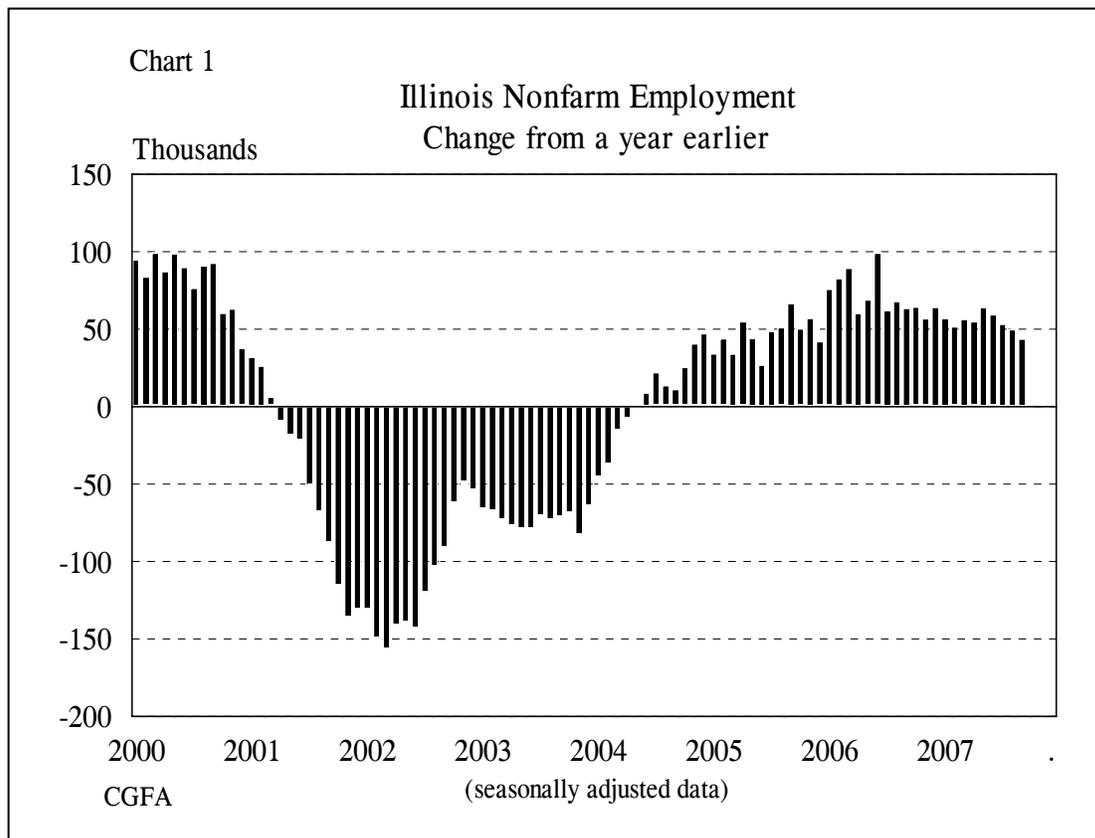
The impact of the recent surge in oil prices on the economy is still uncertain. Oil prices had already risen appreciably before the recent surge without deleterious effects on the economic expansion; however, prices had never reached these heights. Already airlines have announced ticket price

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increases due to the hike in fuel prices while a surge in heating oil, as winter approaches, will be particularly hard felt in the Northeast. Moreover, there is concern that recent energy price increases will make their way felt throughout the economy raising inflation concerns. The long-term impact of the recent surge in energy prices, however, is likely to be determined by how long prices stay at such an elevated level. At the current time, there does not appear to be a shortage of oil supplies, rather recent events in Nigeria, Venezuela, and the Middle East with possible disruption of future supplies appear to be the major factors driving up oil prices.

While the economy is dealing with a myriad of problems and odds of a recession may have increased, latest data confirm the economy was on a sound footing last quarter with prospects at this time that a

full fledged recession can be avoided. For example, while the weak dollar raises concerns about inflation, increased exports due to more competitive prices help to stimulate U.S. output. Similarly, as recently as month end, the Federal Reserve again lowered key monetary policy rates that should help in easing some of the credit concerns. Moreover, given recent gains in the equity markets, it appears that the markets feel the recent energy price spike may prove to be temporary. Finally, both nationally and in Illinois, the leading economic indicators have been trading in a narrow range rather than turning significantly downward that has happened prior to previous economic recessions. As mentioned in last month's briefing, however, a significant slowdown in economic activity in the period ahead will be reflected in reduced revenue from economically related revenue sources.



INDICATORS OF ILLINOIS ECONOMIC ACTIVITY

<u>INDICATORS</u>	<u>SEPT. 2007</u>	<u>AUG. 2007</u>	<u>SEPT. 2006</u>
Unemployment Rate (Average)	5.1%	5.4%	4.3%
Annual Rate of Inflation (Chicago)	3.7%	1.5%	3.4%
<hr style="border: 2px solid black;"/>			
	<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)	6,759	0.6%	1.4%
Employment (thousands) (September)	6,720	0.9%	0.6%
New Car & Truck Registration (September)	48,979	-29.9%	-7.8%
Single Family Housing Permits (September)	1,820	-20.1%	-38.6%
Total Exports (\$ mil) (August)	4,136	1.3%	17.3%
Chicago Purchasing Managers Index (October)	49.7	-8.3%	-6.9%

REVENUE

October Revenues Rise on Strength of Federal Sources and Transfers

Jim Muschinske, Revenue Manager

Excluding \$300 million in cash flow transfers stemming from the Hospital Assessment plan, total general funds revenues jumped \$345 million in October. Increased receipts from federal sources comprised the majority of that increase [\$175 million], but a good month for transfers as well as continued strong performance from personal income taxes contributed to the monthly gain. One additional receipting day this month also aided in the advance.

As mentioned, gross personal income tax performed very well in October with receipts up \$90 million, or \$81 million net of refunds. Public utility raised \$24 million, although it appears timing of receipts was the main

reason for the up tick. Inheritance tax earned its reputation as being one of the most volatile sources, as receipts soared \$13 million. Other sources were up \$6 million, interest income raised \$5 million, and both liquor and corporate franchise taxes each gained \$3 million.

Despite the overall monthly gain, both gross corporate income taxes and sales taxes again suffered monthly declines. Gross corporate income tax fell \$23 million, or \$19 million net of refunds, while sales tax dipped \$3 million. October marks the eighth time in the last nine months that sales tax receipts have failed to match the same prior year levels, reinforcing the concerns spelled out in last months revenue briefing.

Overall transfers did very well in October, rising \$57 million. Other transfers rose by \$32 million fueled by an \$80 transfer related to the Hospital

Assessment program. Riverboat gambling transfers increased by \$15 million and lottery transfers gained \$10 million. A jump in reimbursable spending resulted in a strong month for federal sources as receipts climbed \$175 million.

Year to Date

Through the first third of the fiscal year, overall receipts were up \$503 million. However, the vast majority of that gain stems from an increase in federal receipts. Excluding \$344 million in federal source growth, growth in all other sources was only \$159 million.

While gross personal income tax receipts continue to fare well, up \$210 million, or \$189 million on a net of refund basis, sales tax receipts continue to falter and are down \$58 million. In addition, gross corporate income taxes also are lagging, with receipts off \$40 million, or \$33 million net of refunds.

Despite a good October, overall transfers are down \$22 million for the year, as \$28 million gains in lottery and \$25 million gain in riverboat transfers were more than wiped out by a \$75 million drop in other transfers. Strong reimbursable spending has resulted in an increase of \$344 million in federal sources.

GENERAL FUNDS RECEIPTS: OCTOBER

FY 2008 vs. FY 2007

(\$ million)

<u>Revenue Sources</u>	<u>Oct.</u> <u>FY 2008</u>	<u>Oct.</u> <u>FY 2007</u>	<u>\$</u> <u>CHANGE</u>	<u>%</u> <u>CHANGE</u>
State Taxes				
Personal Income Tax	\$741	\$651	\$90	13.8%
Corporate Income Tax (regular)	56	79	(\$23)	-29.1%
Sales Taxes	615	618	(\$3)	-0.5%
Public Utility Taxes (regular)	93	69	\$24	34.8%
Cigarette Tax	29	29	\$0	0.0%
Liquor Gallonage Taxes	12	9	\$3	33.3%
Vehicle Use Tax	3	3	\$0	0.0%
Inheritance Tax (Gross)	36	23	\$13	56.5%
Insurance Taxes and Fees	2	2	\$0	0.0%
Corporate Franchise Tax & Fees	18	15	\$3	20.0%
Interest on State Funds & Investments	22	17	\$5	29.4%
Cook County IGT	0	0	\$0	N/A
Other Sources	32	26	\$6	23.1%
Subtotal	\$1,659	\$1,541	\$118	7.7%
Transfers				
Lottery	55	45	\$10	22.2%
Riverboat transfers & receipts	75	60	\$15	25.0%
Other	101	69	\$32	46.4%
Total State Sources	\$1,890	\$1,715	\$175	10.2%
Federal Sources	\$522	\$347	\$175	50.4%
Total Federal & State Sources	\$2,412	\$2,062	\$350	17.0%
Nongeneral Funds Distribution:				
Refund Fund				
Personal Income Tax	(\$72)	(\$63)	(\$9)	14.3%
Corporate Income Tax	(\$10)	(14)	\$4	-28.6%
Subtotal General Funds	\$2,330	\$1,985	\$345	17.4%
Short-Term Borrowing	\$0	\$0	\$0	N/A
Hopital Provider Fund (cash flow transfer)	\$300	\$0	\$300	N/A
Budget Stabilization Fund Transfer	\$0	\$0	\$0	N/A
Total General Funds	\$2,630	\$1,985	\$645	32.5%
CGFA SOURCE: Office of the Comptroller: Some totals may not equal, due to rounding				1-Nov-07

GENERAL FUNDS RECEIPTS: YEAR TO DATE

FY 2008 vs. FY 2007

(\$ million)

<u>Revenue Sources</u>	<u>FY 2008</u>	<u>FY 2007</u>	<u>CHANGE FROM FY 2007</u>	<u>% CHANGE</u>
State Taxes				
Personal Income Tax	\$3,037	\$2,827	\$210	7.4%
Corporate Income Tax (regular)	455	495	(\$40)	-8.1%
Sales Taxes	2,419	2,477	(\$58)	-2.3%
Public Utility Taxes (regular)	351	331	\$20	6.0%
Cigarette Tax	117	117	\$0	0.0%
Liquor Gallonage Taxes	54	50	\$4	8.0%
Vehicle Use Tax	13	13	\$0	0.0%
Inheritance Tax (Gross)	106	97	\$9	9.3%
Insurance Taxes and Fees	83	83	\$0	0.0%
Corporate Franchise Tax & Fees	85	65	\$20	30.8%
Interest on State Funds & Investments	77	68	\$9	13.2%
Cook County IGT	15	6	\$9	150.0%
Other Sources	134	122	\$12	9.8%
<i>Subtotal</i>	\$6,946	\$6,751	\$195	2.9%
Transfers				
Lottery	203	175	\$28	16.0%
Riverboat transfers & receipts	250	225	\$25	11.1%
Other	246	321	(\$75)	-23.4%
<i>Total State Sources</i>	\$7,645	\$7,472	\$173	2.3%
Federal Sources	\$1,883	\$1,539	\$344	22.4%
<i>Total Federal & State Sources</i>	\$9,528	\$9,011	\$517	5.7%
Nongeneral Funds Distribution:				
Refund Fund				
Personal Income Tax	(\$296)	(\$275)	(\$21)	7.6%
Corporate Income Tax	(\$80)	(\$87)	\$7	-8.0%
<i>Subtotal General Funds</i>	\$9,152	\$8,649	\$503	5.8%
Short-Term Borrowing	\$1,200	\$0	\$1,200	N/A
Hospital Provider Fund (cash flow transfer)	\$300	\$0	\$300	N/A
Budget Stabilization Fund Transfer	\$276	\$276	\$0	N/A
<i>Total General Funds</i>	\$10,928	\$8,925	\$2,003	22.4%
SOURCE: Office of the Comptroller, State of Illinois: Some totals may not equal, due to rounding.				
CGFA				1-Nov-07

PENSIONS

**The Financial Condition of the State
Employees' Retirement System**
Dan Hankiewicz, Pension Manager

The Board of Trustees of the State Employees' Retirement System held a meeting on October 16th to discuss the results of the June 30, 2007 actuarial valuation of the system. The principal results of the valuation are shown in Table 1 below. When compared to June 30, 2006, the assets of the system have grown by approximately \$1.2 billion in

FY 2007. The growth in assets was due in large part to excellent investment returns. By law, the System's investment function is managed by the Illinois State Board of Investment. SERS' portion of the ISBI commingled fund realized a total investment return of approximately \$1.5 billion, or 16.79%, in FY 2007. This exceedingly strong investment return served to offset the funding reduction in FY 2007 as contained in P.A. 94-0004. SERS' funding ratio at June 30, 2007 increased to 54.2%, as shown in Table 1 below.

TABLE 1		
STATE EMPLOYEES' RETIREMENT SYSTEM		
Financial Condition		
(\$ in Millions)		
	<u>June 30, 2006</u>	<u>June 30, 2007</u>
Actuarial Accrued Liability	\$20,8750.0	\$22,281.0
Actuarial Value of Assets	10,900.0	12,079.0
Unfunded Liability	9,975.0	10,202.0
Funded Ratio	52.2%	54.2%

In addition to receiving the actuary's report, the Board of Trustees certified an FY 2009 contribution of \$827.2 million, or 21.0% of payroll. There are two components to the total FY 2009 contribution: the regular contribution made in accordance with the 1994 pension funding law (P.A. 88-0593), and a contribution to pay a portion of the debt service on the 2004 pension obligation bonds for which SERS is responsible. The base contribution for FY 2009 is 19.116% of

payroll, while the debt service collected through agency payroll deduction is 1.933% of payroll. The current funding law calls for contributions to the system to be increased in equal annual increments so that by FY 2010, the contribution rate is made at a level percentage of payroll in order to achieve a 90% funding ratio by FY 2045. Table 2, on the following page, shows projected contributions through FY 2018 as prepared by the system's actuary.

TABLE 2

STATE EMPLOYEES' RETIREMENT SYSTEM
Projected Contributions Based on June 30, 2007 Valuation

Fiscal Year	Total Contribution (millions)	Assumed Payroll (billions)	Percentage of Payroll
2008	\$638.3	\$3.854	16.6%
2009	827.2	3.930	21.0%
2010	1,047.4	4.100	25.5%
2011	1,087.5	4.270	25.5%
2012	1,134.9	4.441	25.6%
2013	1,175.5	4.615	25.5%
2014	1,216.7	4.791	25.4%
2015	1,259.0	4.972	25.3%
2016	1,302.7	5.159	25.3%
2017	1,351.4	5.352	25.3%
2018	1,401.4	5.552	25.2%