

**INFORMATIONAL MEETING:**

**REVENUE FORECAST**

**TAPES 139-140, A**

## **SENATE REVENUE COMMITTEE**

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**May 14, 2001 — 9:00 A.M. - HEARING ROOM 50 - STATE CAPITOL BUILDING**

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Members Present: Senator Ted Ferrioli, Chair

Senator Lee Beyer, Vice Chair

Senator Susan Castillo

Senator Tony Corcoran

Senator Gary George

Senator John Minnis

Senator Charles Starr

Representative Lane Shetterly, Chair

Representative Janet Carlson, Vice Chair

Representative Deborah Kafoury, Vice Chair

Representative Alan Bates

Representative Chris Beck

Representative Alan Brown

Representative Mark Hass

Representative Max Williams

Representative Bill Witt

Senator Lenn Hannon, Co-Chair

Senator Kate Brown

Senator Bev Clarno

Senator Joan Dukes

Senator Verne Duncan

Senator Tom Hartung

Senator Randy Miller

Senator Cliff Trow

Senator Mae Yih

Representative Ben Westlund, Co-Chair

Representative Tom Butler

Representative Gary Hansen

Representative Cedric Hayden

Representative Jim Hill

Representative Betsy Johnson

Representative Susan Morgan

Representative Rob Patridge

Representative Kurt Schrader

Representative Jackie Winters

Staff: Paul Warner, Legislative Revenue Officer

Carol Phillips, Committee Assistant

Witnesses: Tom Potiowsky, State Economist

Cora Parker, Revenue Economist

Randall Pozdena, Ph.D. ECONorthwest

**TAPE 139, SIDE A**

005 Chair Ferrioli Meeting consisting of combined Senate Revenue, House Revenue, and Ways & Means members called to order at 9:04 a.m.

#### INFORMATIONAL TESTIMONY

016 Tom Potiowsky Introduced himself, along with Cora Parker (Revenue Economist) and Dr. Randall Pozdena (a member of the Governor's Council of Economic Advisors, sitting in for Ralph Shaw.).

026 Dr. Randall Pozdena Stated that the process of developing the revenue forecast involves a lot of private economist input to the Chief Economist's work. Experts in the fields of utilities, agriculture, forestry, high tech sector, and finance all contribute to the forecast.

035 Potiowsky Stated he would present the economic outlook and how it has changed since the March forecast was distributed. Pointed out that the economy today is faltering but, relative to the numbers available, it is still one of the best he has seen since the 1960s. However, there has been definite slowing of the overall economy, and the "R" word (recession) has been brought up recently.

046 Potiowsky Exhibit 1: Slides from PowerPoint Presentation. Discussed page 3, upper slide: Inflation Gradually Rises but is Under Control.

052 Potiowsky Page 3, lower slide: Income Rise is Slowing, Consumption is Coming Down.

056 Potiowsky Page 4, upper slide: The Fed Lowered Rates Twice in Just One Month.

062 Potiowsky Page 4, lower slide: When Will it Stop? This economic expansion is the longest in history since records started to be kept in the late

1800s. Current speculation is that there will be a hard landing when it happens.

- 069 Potiowsky Page 5, lower slide: Growth in Gross State Product: Oregon 1988-1998.
- 072 Potiowsky Page 6, upper slide: Real Gross State Product 1988-1998. Even though Oregon now has a more diversified economy, Oregon is still very much a manufacturing-based economy. The state just manufactures different products than it did 10 or 20 years ago. Because of that, the state will still be subject to volatile swings in the economy as business cycles swing one way or another. We are in a downturn now and are feeling the effects of that down economy.
- 085 Potiowsky Page 6, lower slide: Oregon Employment 88-98. Although the greatest growth has been in the value of manufacturing sector output, the bulk of employment has shifted into the service sector. This is indicative of an economy that has grown through its manufacturing sector because it provides a lot of output value per employee. There is, however, a lower value of output per employee figure when referring to services. Oregon's growth is occurring in the service sector, and that is consistent with the rest of the United States.
- 094 Potiowsky Page 7, upper slide: Oregon Slowed in the Middle of 1998. Employment growth started to fall in conjunction with the Asian financial crisis. Oregon started to pick up at the end of the 1990s, but just as that started the Federal Reserve raised interest rates in 2000. That created a national slowdown, and that is our current situation. The current slowdown was engineered by the Federal Reserve, which is now very rapidly trying to reverse that trend.
- 100 Potiowsky Page 7, lower slide: Export Volume Picked Up in 1999 but is Slowing Into 2000. Oregon's trading partners have also felt the effects of the slowing U.S. economy.

- 105 Potiowsky Page 8, upper slide: Most of Growth is in High Tech and Transportation Equipment. High tech is definitely Oregon's strongest export sector, making up over 60% of total value of exports. Since the mid-1990s, agriculture has been depressed.
- 111 Potiowsky Page 9, upper slide: Recession of 1991 Compared with Slow Growth Into 2000. Pointed out that it is possible to have a very rapid downturn with little notice.
- 122 Potiowsky Page 9, lower slide: Expected to Grow Above US Average After 2000---Slow Growth. Believes 2001 will be the most difficult year. Relative to the March forecast, the economic downturn has now shifted. All indications were that the downturn would occur mostly during the first quarter of 2001. That has been changed to around the third quarter of 2001. During the fourth quarter some strength should be seen returning to Oregon's economy. The overall economic picture is the same, but the time frame has been shifted. Overall, 2001 will be a tough year for Oregon before improvement is seen in 2002.
- 137 Potiowsky Page 10, upper slide: Lumber and Wood Stabilize into 2003. Lumber and wood products have had difficult times through the years and will continue to do so, but it will stabilize somewhat. Home starts have increased.
- 144 Potiowsky Page 10, lower slide: High Tech Will Resume Growing but at a Slower Rate. High tech is still very volatile. Projecting negative growth (job losses) for the rest of 2001.
- 152 Potiowsky Page 11, upper slide: Housing Starts and Prices. Housing starts have picked up somewhat because of the drop in mortgage rates.

- 157 Potiowsky Page 11, lower slide: Construction Will Stay at Moderate Levels. Construction has been resilient during current years, relying on commercial construction to carry the industry through 2000. Now the residential side has picked up slightly because of lower mortgage rates.
- 161 Potiowsky Page 12, upper slide: Looking Ahead.
- Consumers remain a key to continued growth, both national and state.
  - Strength in Asian markets should fuel demand for Oregon products. Still some risk remains.
  - 2001 will be a difficult year for Oregon. Growth will once again be faster than the U.S., but at a slower pace than in recent years.
- 169 Potiowsky Page 12, lower slide: Allowing Oregon to Grow Faster Than the U.S.
- 170 Potiowsky Page 13, upper slide: Per Capita Income and Wage. From 2002 on should see improvements in per capita income and average wages
- 171 Potiowsky Page 13, lower slide: Per Capita Income Growth 1990-1997. The agricultural counties will probably still have problems for some time to come, but the urban areas will benefit from the increased economy. Sherman, Gilliam, Morrow, and Wheeler (agricultural) counties will still have tough times for some time to come.
- 175 Potiowsky Page 14, upper slide: Risk Factors: Macroeconomic Policies.
- President Bush's tax cut will help the economy with \$1 billion in rebates or withholding reductions in 2001. The \$1.35 trillion tax cut package will mildly

stimulate the economy this year.

- Greenspan and Co. can move quickly, but interest rate cuts take 9 to 12 months for full impact.

189 Potiowsky Page 14, lower slide: Risk Factors: International Conditions:

- Asian countries are expected to have reasonable growth in 2001, which should assist Oregon exports.
- Japan remains a question mark. If oil prices rise dramatically, import dependent Asia could suffer.

196 Potiowsky Page 15, upper slide: Energy Prices:

- Natural gas prices are softening as spring begins.
- Wet weather in the next few months is crucial for hydro generation.
- Price spikes are still a possibility in both electric and natural gas over the next few years. Rolling blackouts, production stoppages could happen.
- California Effect — The electric reliability problems of California may cause firms to move to other states, including Oregon.

219 Potiowsky Page 15, lower slide: Stock Market:

- As of February 28, NASDAQ down to 1998 levels. The market gained 30% during April and May but still down 50% from its high over the last 12 months.
- Reverse wealth effect would slow consumer spending.
- Impact on lowering consumer confidence.

241 Potiowsky Page 16, upper slide: High Tech Industry:

- For 2001-2002, showdown in revenues

could be more than forecasted.

- Announcements of layoffs and further wage caps.
- For 2003-2005, industry could take off as in the mid-1990s.

- 255 Potiowsky Page 16, lower slide: Summary. The picture is similar to that demonstrated in March, but the timing may have changed from first quarter to third quarter 2001.
- 265 Cora Parker Page 17, lower slide: Revenue Forecast. Sections to be discussed:
- Lottery Revenue Forecast
  - General Fund Revenue Forecast
  - Kicker
  - Forecast Risks
- 277 Parker Page 18, lower slide: Lottery Resources (Millions of Dollars). Stated there was minimal change in the 1999-2001 biennium.
- 298 Parker Page 19, upper slide: Lottery Resources 2001-2003. Economists see a fairly significant increase in Lottery revenues for the biennium. Video Lottery makes up a significant portion of the increase.
- 323 Parker Page 19, lower slide: Lottery Resources Available to the State.
- 333 Parker Page 20, lower slide: General Fund Resources 1999-2001. There is a slight increase of \$27.7 million to the General Fund. The \$9.3 million increase in Corporate Income Tax is enough to enable the kicker to kick.

- 355 Parker Page 21, upper slide: General Fund Resources (Millions of Dollars) 2001-2003. No major change to March forecast figures, but showing approximately \$20 million from March.
- 393 Parker Page 21, lower slide: General Fund Resources (Millions of Dollars) 2003-05 and 2005-07.
- 414 Parker Page 22, upper slide: General Fund Revenues.
- 417 Parker Page 22, lower slide: Biennial Growth in General Fund Revenues. Compares long run average growth rate (just over 13%) with inflation.
- 434 Parker Page 23, upper slide: Biennial Growth in General Fund Revenues. Compares general fund revenue with kicker and pension adjusted revenues.
- 453 Parker Page 24, upper slide: Kicker Determination:
- Close of Session (COS) forecast established.
  - Personal Kicker...if all non-corporate revenues more than 2% above COS
  - Corporate Kicker...if corporate revenues more than 2% above COS
- 468 Parker Page 24, lower slide: Kicker Determination:
- Expenditure changes have NO IMPACT on kicker calculation
  - Kicker refunds/credits paid in following biennium (for example 1999/01 kicker(s) will be refunded in 2001-03 biennium)

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- 025 Parker Page 25, upper slide: Personal Kicker

"Timeline". September forecast takes into consideration any legislative changes made before end of 2001 session. Because of that, the forecast kicker level could change higher or lower.

- 048 Parker Page 25, lower slide: Kicker Calculation (Personal and Corporate)
- 063 Parker Page 26, upper slide: How Does the Kicker Impact the May 2001 Forecast?
- Includes estimated Personal Kicker Refund of \$355.5 million
  - To be paid in Fall 2001 on Tax Year 2000 personal income tax liability
  - Approximately 8.4% of liability
  - Average kicker refund \$190
  - Includes estimated Corporate Kicker Refund credits of \$22.5 million
- 072 Parker Page 26, lower slide: 2 Percent Surplus Kicker
- 088 Parker Page 27, upper slide: Forecast Risks:
- Economic Risks
  - Capital Gains
  - Current Law
  - Oregon Tax Law Changes
  - Federal Tax Law Changes
  - Remaining Fiscal Year 2001 Collections
- 118 Various Question and answer period.
- 476 Chair Ferrioli Adjourned meeting at 10:00 a.m.

Submitted by, Reviewed by,

Carol Phillips Kim Taylor James

Committee Assistant Revenue Office Manager

Exhibit Summary:

1. Office of Economic Analysis, Oregon's Economic and Revenue Outlook, 27 pp.
2. Department of Administrative Services, Oregon Economic and Revenue Forecast, 106 pp.
3. Department of Administrative Services, Oregon Economic and Revenue Forecast Summary, 13 pp.
4. Legislative Revenue Office, Waters, Forecast Summary, 7 pp.