



Economic Monitor

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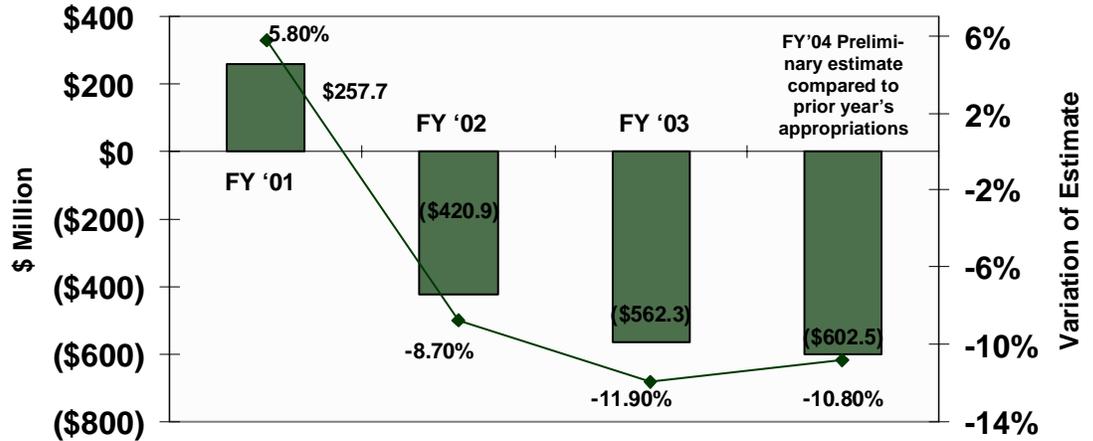
Oklahoma Legislators Set to Face another Bleak Budget Year

For the third fiscal year in a row, Oklahoma legislators must begin this legislative session with the daunting task of appropriating scarce dollars due to the current budget shortfall. The FY'04 budget estimate which was certi-

fied on December 20, 2002 is over \$600 million less than was appropriated in FY'03, that represents a 10.8% decline. In the two preceding budget years (FY'02 and FY'03) collections came in at 8.7% and 11.9% below the estimates respectively.

The 5.8% budget surplus in FY'01 is now a distant memory. When looking a little closer into what has caused the downturn in Oklahoma's tax collections, gross production taxes stand out as the primary cause. In FY'01
(Continued on page 4)

Revenue Estimates Miss Target



OU POLL Reveals How Oklahomans Feel State is Perceived by Outsiders

Oklahomans were asked what they believed to be the most attractive aspect of Oklahoma, and were then asked what they think keeps more people outside the state from traveling to Oklahoma. These open-ended responses were categorized and are presented below.

Both state and city respondents

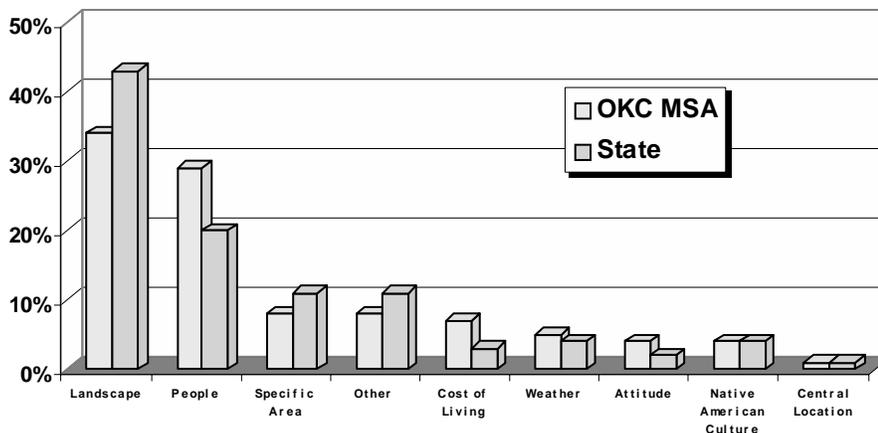
cited the lakes and landscape of Oklahoma as its most attractive aspect, followed closely by the

quality and friendliness of the people. Those from the state sample found the landscape to

be Oklahoma's biggest attraction at 43 percent, compared to 34 percent of OKC MSA residents,

but OKC MSA respondents were more supportive of the attractiveness of the people (29%) than those in the overall state (20%). Eleven percent of the state and 8 percent of OKC MSA respondents cited a specific area of the state being the most attractive, with answers ranging from Little Sahara to the Talihina Drive to
(Continued on page 6)

Landscape and people are the most attractive aspects of Oklahoma



Oklahoma is not Alone: Most States Facing Fiscal Challenges

According to recent reports conducted by NCSL and the National Governors Association and the National Association of State Budget Officers, states are facing their most dire fiscal crisis since World War II. While the majority of states have been dealing with tight budget conditions for the past two years, some of the most difficult policy decisions loom ahead as many of these states have exhausted budget cuts and drawn down most if not all rainy day funds.

Two-thirds of the states reported declining revenues and over half of the states face expenditures that exceeded levels projected

in the fiscal year 2003 budgets. Sixteen states in the nation experienced negative growth in FY'02. NCSL's survey found that states will have a collective \$17.5 billion budget gap to fill before FY'03 ends. The initial gap for FY'03 was expected to be \$49.1 billion but most of that was resolved by the time states began the new fiscal year.

NGA Executive Director Raymond C. Scheppach attributes the dismal state of fiscal affairs to four major factors. He states that "the combination of long-run deterioration in state tax systems coupled with an explosion of health care costs are

creating an imbalance between revenue and spending. To make matters worse, we've had a collapse of capital gains tax revenues added to the overall loss of revenue attributable to slow economic growth".

Below is a table from the NCSL State Budget Update which shows which states have experienced spending overruns and whose revenues are lower, on target or higher than expected. Oklahoma is one of 19 states that experienced both spending overruns and lower than expected revenues.

States Meeting Spending and Revenue Targets

Spending overruns and lower than expected revenues (19 states)		Spending on target and lower than expected revenues (14 states)	
California	Missouri	Alabama	Michigan
Georgia	Montana	Arizona	Oregon
Hawaii	Nebraska	Colorado	Pennsylvania
Illinois	Nevada	Delaware	South Dakota
Iowa	New Hampshire	Idaho	Tennessee
Kansas	New Mexico	Indiana	Utah
Kentucky	Oklahoma	Louisiana	Wisconsin
Massachusetts	South Carolina		
Mississippi	Vermont		
	Virginia		
Spending overruns and revenues on target (5 states)		Spending and revenues on target (3 states)	
Connecticut	Washington	Minnesota	
New York	West Virginia	New Jersey	
	Wyoming	North Carolina	
Spending overruns and higher than expected revenues (4 states)		Spending on target and lower than expected revenues (4 states)	
Alaska	Maryland	Arkansas	Ohio
Florida	North Dakota	Maine	Rhode Island

Note: Texas did not provide information on revenue performance but reported spending overruns. Expenditures for Medicaid and CHIP are over budget.

Source: NCSL State Budget Update: November 2002

Oil and Gas Sector Salaries Continue to Lead Market

A recent U.S. Department of Labor Bureau of Labor Statistics employment and wage survey revealed a large gap in average annual pay for employees of the various industrial categories. The BLS data revealed an average annual pay in Oklahoma of \$27,615 for the 1.17 million Oklahoma workers.

The goods-producing categories led by Natural Resource and Mining outpaced the service-providing categories by nearly \$10,000 per year in average pay. By far the highest average annual pay category at almost \$47,000, Natural Resource and Mining employees which comprise about 3.1% of Oklahoma's total employment. The average is buoyed by the Oil and Gas extraction sector which averages \$66,000 in annual pay.

The Information sector, comprised of media, Internet, and telecommunications industries, was the second highest average

paying sector at just over \$37,000. The Information sector made up about 3.2% of the total employment in Oklahoma in 2001.

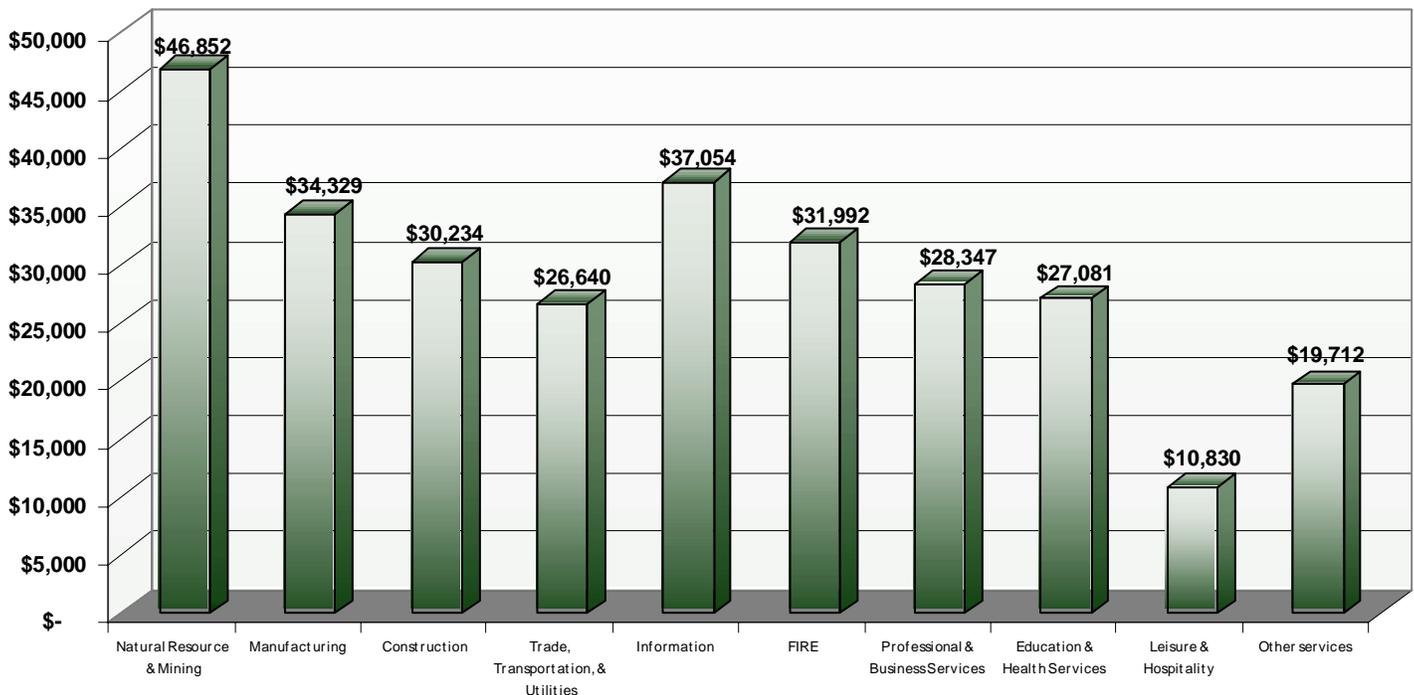
Trade, Transportation, and Utilities (TTU) was the largest sector of Oklahoma's employ-

ment encompassing nearly one-quarter of Oklahoma's private sector employment, followed by Manufacturing at 14.5%, Professional & Business Services at 14.2%, and Education and Health Service at 13.8 per-

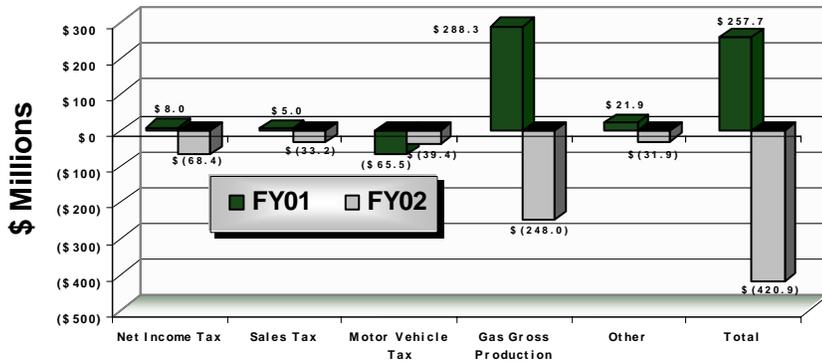
cent. Leisure & Hospitality, consisting primarily of hotel and food-service employees, was the lowest-earning category in the survey at just under \$11,000 annually.

	Employees	Average Annual Pay	Total Wages (\$Billions)	Percent of total employment	Percent of total wages
Natural Resource & Mining	35,853	\$ 46,852	\$ 1.68	3.1%	5.2%
Manufacturing	170,085	\$ 34,329	\$ 5.84	14.5%	18.1%
Construction	65,805	\$ 30,234	\$ 1.99	5.6%	6.2%
Total Goods-Producing	271,742	\$ 34,990	\$ 9.51	23.2%	29.4%
Trade, Transportation, & Utilities	288,539	\$ 26,640	\$ 7.69	24.6%	23.8%
Information	37,066	\$ 37,054	\$ 1.37	3.2%	4.2%
FIRE	77,311	\$ 31,992	\$ 2.47	6.6%	7.6%
Professional & Business Services	166,641	\$ 28,347	\$ 4.72	14.2%	14.6%
Education & Health Services	161,353	\$ 27,081	\$ 4.37	13.8%	13.5%
Leisure & Hospitality	126,855	\$ 10,830	\$ 1.37	10.8%	4.2%
Other services	40,738	\$ 19,712	\$ 0.80	3.5%	2.5%
Total Service-Providing	899,620	\$ 25,388	\$ 22.84	76.8%	70.6%
Total	1,171,362	\$ 27,615	\$ 32.35	100%	100%

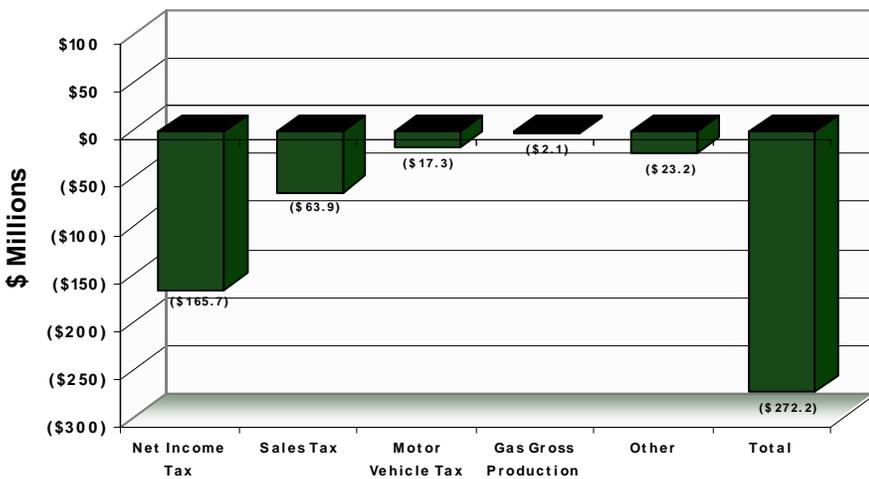
2001 Oklahoma Private Sector Employment - Average Annual Pay



**FY01 and 02 GR Collections
(Estimate v. Actual)**



**FY 03 GR Collections
(Estimate v. Actual To Date)**



(Continued from page 1)

with gas prices and production at high levels, gross production taxes were primarily responsible for the increased revenue that year. However, that quickly turned around in FY'02 when gross production taxes came in at \$248 million (or 52.3%) below estimate. This decline in gross production taxes explained over half of the total shortfall in FY'02.

The blame for the revenue shortfall in FY'03 can be more equally distributed. As the graph on the left shows, Oklahoma has felt the downturn in the economy in all its major tax sources in FY'03, with income taxes (both personal and corporate) taking the biggest hit. The numbers included in this graph are through November 2002, when annualized that number is expected to be approximately -\$562.3 million.

The economic recovery has not begun yet in Oklahoma, according to the FY'04 revenue estimates. The FY'04 estimate projects individual income tax to decline by 7.9%, Sales taxes down by 6.2%, motor vehicle taxes decline 8.3% and gross production taxes down by 10.5%. In addition to the 10.8% decline in funds available for appropriation, Legislators will not have the luxury of pulling as much money out of reserves as they have in past years, as only \$72.4 million remains in the Rainy Day Fund. Last year legislators accessed \$286.6 million to lessen the blow of the 11.6%

Oklahoma's Appropriations Checks and Balances

Unlike the U.S. government, Oklahoma has a constitutional requirement to balance the budget. The state cannot deficit spend in order to maintain existing service levels when times are tight. Many people are unaware that Oklahoma has a rather conservative method of determining the amount of money which can be appropriated by the legislature each year. There are two statutory measures which were implemented to control state government spending and which serve as a built in safety net. First, appropriations are limited to 12% growth from one year to the next. Secondly, each year appropriations are limited to 95% of projected revenues for any given year. The graph at right shows an example of the FY'01 general revenue. In this year, revenue came in at 105.7% of the estimate. This 5.7% above the estimate was deposited into the Rainy Day fund.

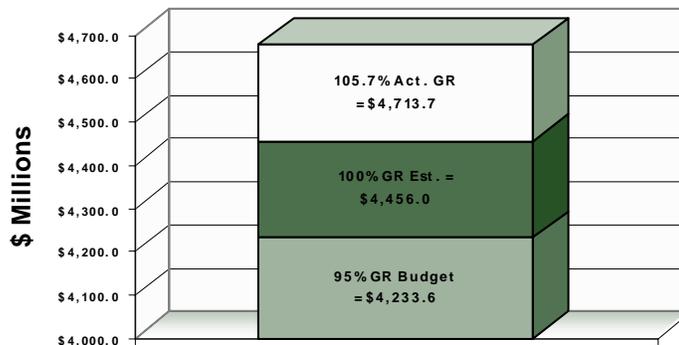
The excess revenue, the amount over 100% of projections is deposited into the Constitutional Reserve Fund (Rainy Day Fund), where other safeguards on spending have been employed. The Rainy Day Fund can be used if:

1. General revenue estimates decline from one year to the next
2. Emergency declaration by the Governor

nor and a 2/3 vote in both the Senate and the House of Representatives
3. 3/4 vote by both the Senate and the House of Representatives.

Revenue estimates and projections are submitted to the Board of Equalization by the Office of State Finance and are based on information prepared by the Oklahoma Tax Commission and other state revenue collecting and estimating agencies. Projected revenues are certified by the Board of Equalization. The Governor, Lt. Governor, State Superintendent of Instruction, and the President of State Board of Agriculture comprise the Board of Equalization.

The governor has line item veto authority over all appropriation bills. Vetoes can be overridden by a super-majority vote by Senate and House.



Revenues Decline, Natural Gas Lone Bright Spot

Oklahoma's revenue collections remain sluggish for the first half of fiscal year 2003. Actual collections of just over \$2 billion were 12 percent below the year-to-date estimate.

Natural Gas Gross Production tax collections are on target with estimates and, as prices continue to rise, should exceed estimated collections.

Over sixty percent of the \$271 million shortfall can be attributed to lower-than-expected income tax collections, both individual and corporate. Legislation passed in 2002 directed the first \$41 million of corporate income tax collections be deposited into the HB 1017 education

fund. Thus far \$36.9 million has been deposited into the fund. \$3.6 million has been paid out to corporations who filed 2001 return extensions and are receiving refunds. OSF's \$26.5 million YTD estimate accounted for the \$41 million HB 1017 deposit and the anticipated refunds. Actual collections, therefore, are over \$30 million below estimates.

Corporate layoffs may be to blame for a significant portion of the lower individual income tax collections. Tulsa-based Williams Companies along with other large employers such as WorldCom combined to layoff thousands of employees in 2002.

The majority of the remainder of the shortfall

can be found in the sales tax collections. Collections of \$64 million below estimates represent 10 percent less sales tax revenue than expected.

The Oklahoma legislature makes its appropriations based on the estimated collections for the next fiscal year. Oklahoma statute limits appropriations to 95 percent of the estimated revenue. While this safeguard normally insulates the budgeting process from a slight variation in revenues, a drop below the 95 percent collection rate, such as this year, necessitates mid-year budget modifications to account for the revenue shortage.

General Revenue Fund					
Comparison with OSF Estimate and Prior Year Collections (\$ Millions)					
(\$ MILLIONS) Revenue Source	Column 1	Column 2	Col 2 / Col 1	Column 3	Col 2 / Col 3
	Actual Collections			Estimated Collections	
	FY-2002 YTD	FY-2003 YTD	FY-03 as % of FY-02	FY-2003 YTD	FY-2003 as % of Estimate
TAXES:					
Income					
Individual	\$955.3	\$927.4	97%	\$1,062.6	87%
Corporate	\$47.5	(\$3.6)	-8%	\$26.5	-14%
Gross Production, Gas	\$119.8	\$128.3	107%	\$130.4	98%
Sales	\$632.1	\$602.0	95%	\$665.8	90%
Use	\$38.9	\$27.0	69%	\$38.6	70%
Motor Vehicle	\$113.0	\$104.7	93%	\$122.0	86%
Insurance Premium	\$16.0	\$16.5	103%	\$14.8	111%
Franchise	\$29.0	\$27.7	96%	\$28.1	99%
Inheritance/Estate	\$46.6	\$39.9	86%	\$45.9	87%
Cigarette	\$13.0	\$13.0	100%	\$17.8	73%
Beverage	\$12.7	\$12.5	98%	\$12.9	97%
Alcoholic Beverage	\$8.2	\$8.6	105%	\$8.0	108%
Mixed Beverage	\$8.3	\$9.1	110%	\$9.6	95%
Pari-Mutuel	\$1.5	\$1.4	93%	\$1.3	108%
Other	\$39.6	\$41.1	104%	\$37.6	109%
Subtotal: Taxes	\$2,081.5	\$1,955.6	94%	\$2,221.9	88%
Licenses, Permits, & Fees	\$15.6	\$15.9	102%	\$15.3	104%
Income From Money/Property	\$52.0	\$24.6	47%	\$30.0	82%
Other Income	\$11.1	\$10.7	96%	\$11.2	96%
Continuing Collections	\$2,160.2	\$2,006.8	93%	\$2,278.4	88%
Transfers & Lapses	\$1.2	\$0.7	58%	\$0.8	88%
Total Revenues	\$2,161.4	\$2,007.5	93%	\$2,279.2	88%

Data includes December 2002 collections.

Outsider Opinion

Continued from page 1)

the Bombing Memorial or downtown Oklahoma City or Tulsa. OKC MSA residents are more attracted to Oklahoma's lower cost of living (7%) than those in the state overall (3%).

The most common reason cited for keeping people from traveling to Oklahoma in both the state and MSA samples was a belief that those outside the state think there is nothing to do in Oklahoma (35% OKC MSA, 24% state). Oklahomans also believe outsiders hold strong misconceptions about the sophistication of the state and its residents, that people from outside Oklahoma hesitate to travel or vacation here because of our "dust bowl" and "cowboy and Indian" image. The third most commonly stated reason against travel was that Oklahomans believe outsiders don't have enough advertising information about what the state has to offer.

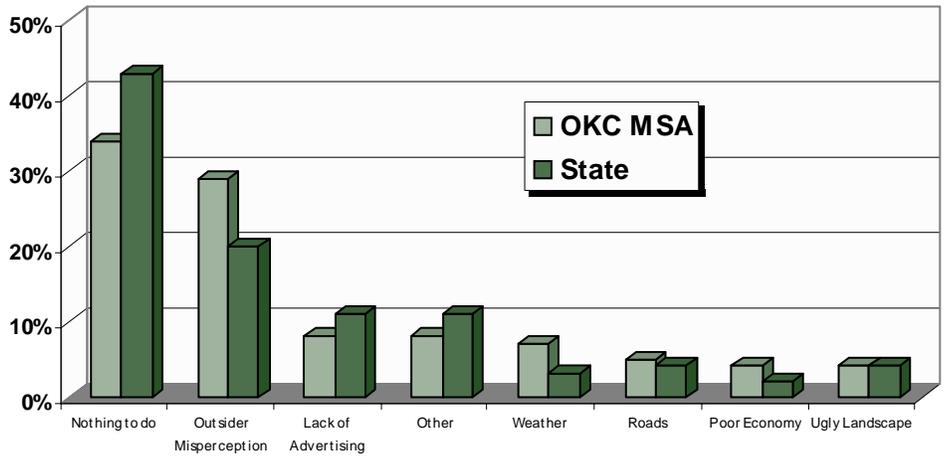
The condition of Oklahoma's roads and the number of toll roads were of

great concern. Five percent of OKC MSA residents and a full 17 percent of the state respondents listed either the poor condition of the roads, the high cost of the tolls, or the amount of construction as roadblocks to visitation. Five percent each of state and MSA respondents cited the poor economy as a deterrent to visitation, with 3 percent in each sample reporting they believe that outsiders think Oklahoma's landscape is

ugly, and that keeps them from visiting. Weather was of relatively minimal concern to each group, with 6 percent of MSA and 5 percent of state residents saying outsiders are either scared of Oklahoma's tornadoes, or wouldn't like the heat.

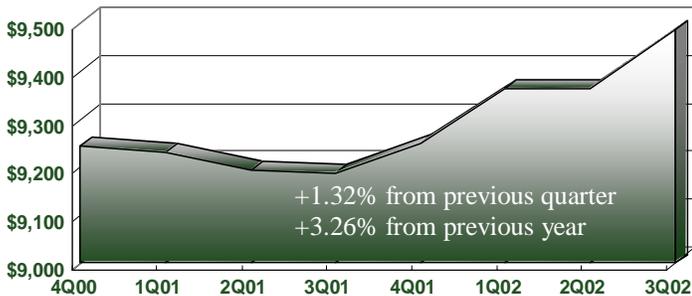
Source: Oklahoma Opinion Quarterly, OU POLL

What keeps people from traveling to Oklahoma?

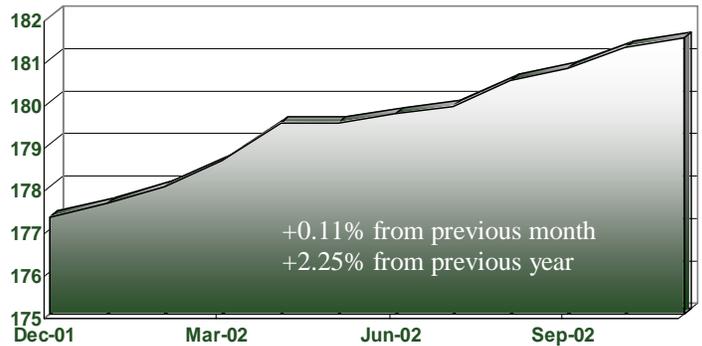


Oklahoma Economic Indicators

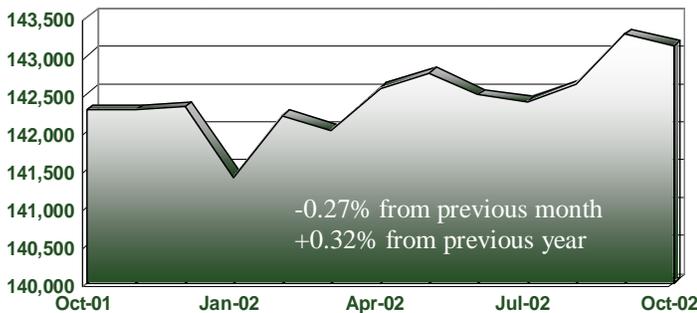
US Gross Domestic Product (Billions of Chained 1996 \$s)



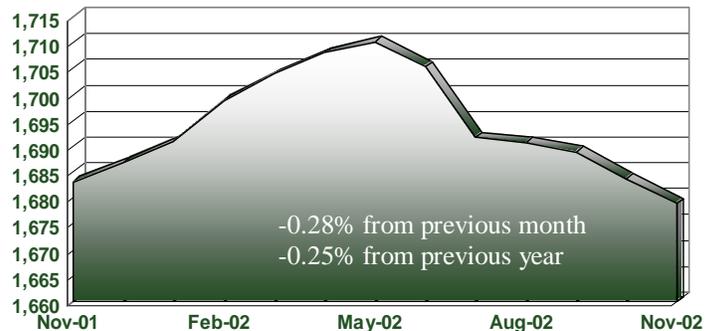
U.S. CPI (All Urban Consumers)



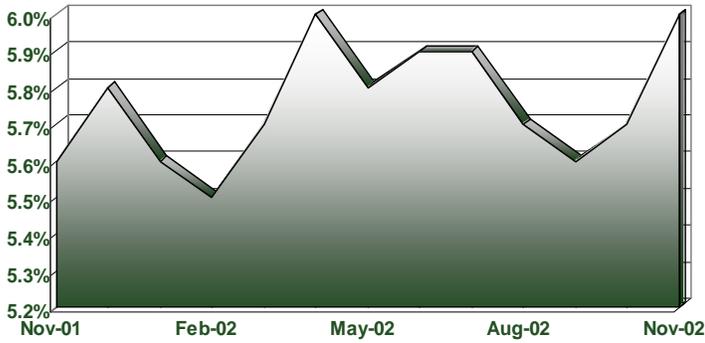
U.S. Total Employment (Civilian Labor Force, 000s)



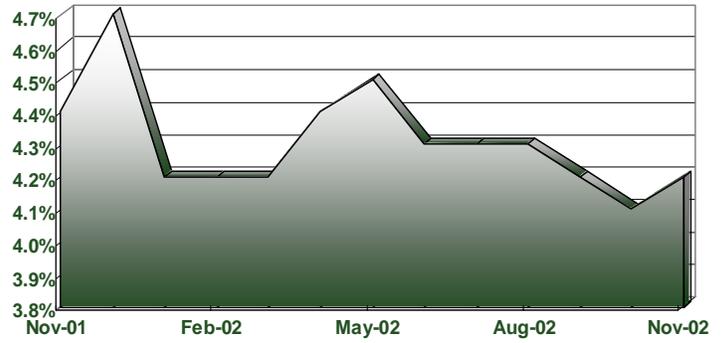
OK Labor Force (thousands)



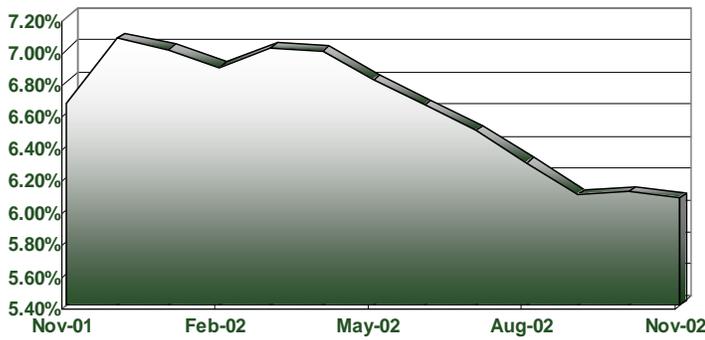
US Unemployment Rate



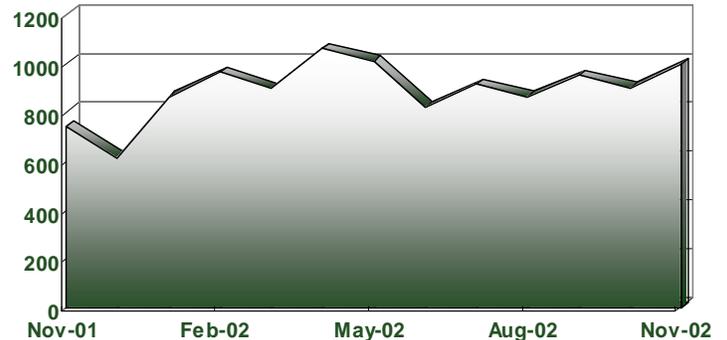
OK Unemployment Rate



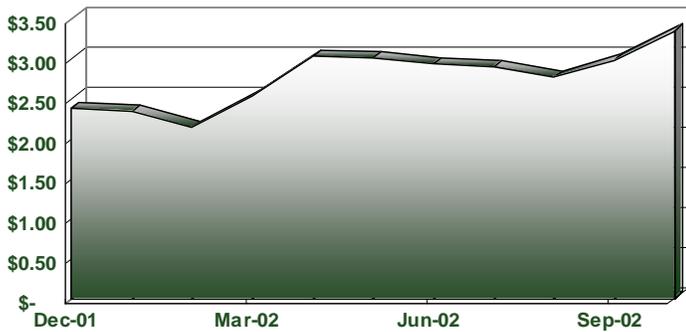
30-Year Mortgage Interest Rates



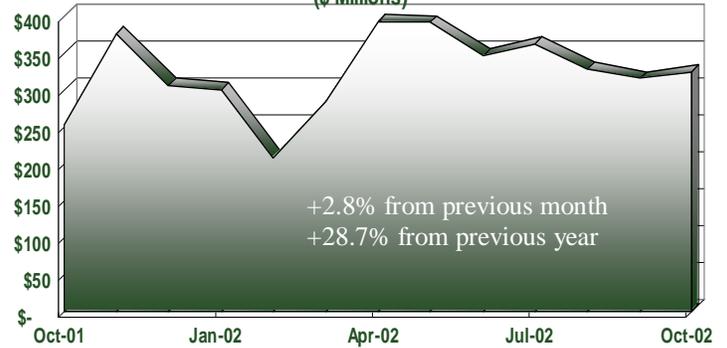
OK Single Family Building Permits Authorized



Natural Gas Wellhead Price



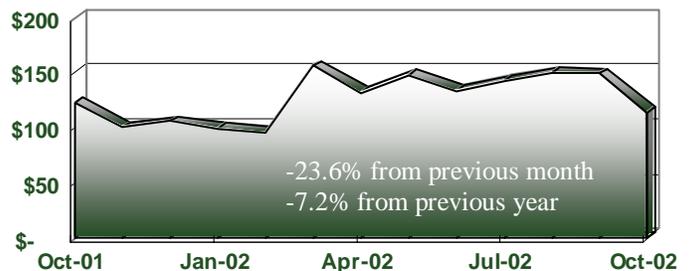
Value of Oklahoma Natural Gas (\$ Millions)



Crude Oil Prices



Value of Oklahoma Oil Production (\$ Millions)



State Could Lose Significant Revenue Under Proposed Federal Stimulus Plan

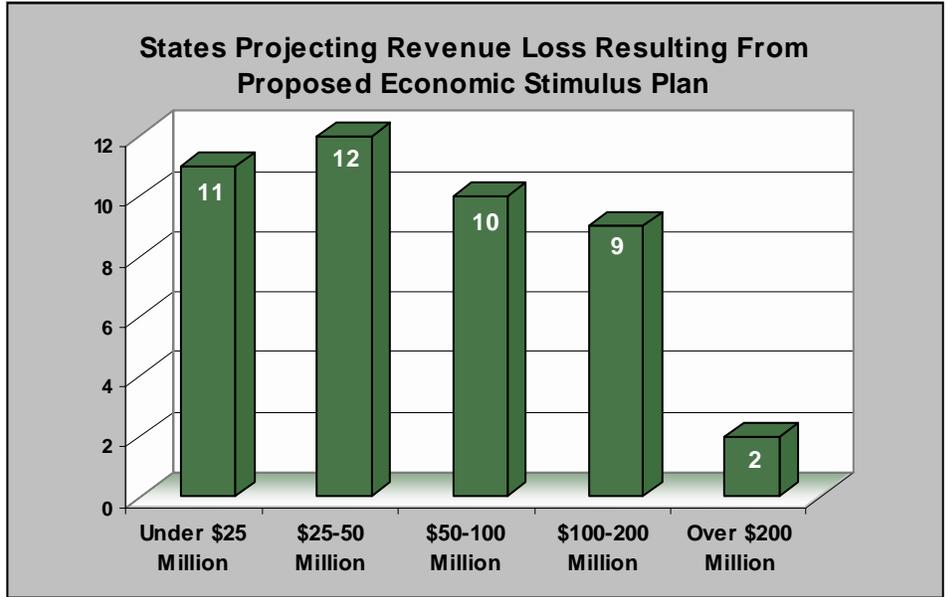
A proposed federal economic stimulus plan may cause Oklahoma's state revenues to dip and credit ratings to further erode according to Standard and Poor's rating services.

Revenue loss to Oklahoma could reach \$36 million

S&P's Research Services in a January 9, 2003 release states: "State legislatures now convening to develop fiscal 2004 budget will have to consider significant budget and tax policy issues arising from the federal stimulus package, however it develops. To preserve the state revenues coming from dividends, state would be required to decouple current state income tax structures from the federal system ...if the proposal moves forward in its current form, fiscal pressure will be even more acute for state governments already facing estimated fiscal 2004 budget deficits totaling more than \$60 billion. As a result, further credit deterioration over the next year is likely."

37 states (Oklahoma included) use federal income definitions in their own tax systems. In most cases revenues from dividend taxes based on the federal definition of taxable income would be lost in any plan that excluded dividend income from taxation. Some states, such as Alabama, Arkansas, Mississippi, New Jersey, Pennsylvania and Tennessee require

taxpayers to report dividend income separately from dividend income derived from federal returns. If other states wanted to avoid the revenue loss they would have to enact this type of income reporting also. It has been estimated using the Internal Revenue Service, *Statistics of Income Bulletin, 2001* that Oklahoma's loss would be approximately \$36 million.



Economic Monitor

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Senate Website News

Visit the Senate website at www.lsb.state.ok.us for contact information for senators, bill tracking, current and past issues of the Economic Monitor and more. The Oklahoma State Senate website will soon have a special kids section with information about how an idea becomes a law, trivia and other activities.