Prevention Alliance

BUDGET MEMO: JUNE 2023 REVENUE FORECAST

On June 27th, the Economic and Revenue Council (ERFC) released the June 2023 Quarterly Economic & Revenue Forecast. The forecast showed a modest upward trend in our state revenue collections and budget projections compared to the last quarterly forecast that was released in March. The June forecast projects that when compared to the March forecast (which is what the legislature based the 2023-25 operating budget on), total net state revenue subject to the budget outlook[1] is expected to increase by $341 million in the current 2021-23 biennium, $327 million in the 2023-25 biennium, and $147 million in the 2025-27 biennium..

Overview: The Economic & Revenue Forecast Council

In Washington, the Economic & Revenue Forecast Council (ERFC) releases and adopts four official revenue forecasts each year: spring during legislative session (February in short session years; March in long session years), summer (June), fall (September), and winter before the governor releases their proposed budget (November).

These revenue forecasts look at the various revenue sources (sales tax, property tax, real estate excise tax, business & occupation tax, tobacco/cannabis/liquor tax, etc.) and the projected impact of economic factors such as unemployment, sales, airline travel (for the ripple effect on Boeing), housing construction and sales, exports, etc. Looking at all these factors, the ERFC builds a forecast for what the state's estimated revenue will be and how much larger/smaller it is than the previous forecast.

While this is a positive change to the economic and revenue forecast, the forecast is overall very similar to the March 2023 forecast and the amount of change is fairly nominal in relation to the full size of the state budget. The projected increase of $474 million total over those two biennia (2023-25 and 2025-27) is largely due to forecasted economic changes (consumer spending, unemployment rates, real estate activity, etc.). Non-economic changes (e.g., legislative changes and fund transfers made during the 2023 legislative session) had a smaller, though still positive impact. *See table 1 for more detail.*

Table 1: State Revenue Forecast March 2023 Compared to June 2023

Biennium	March 2023 Forecast (baseline)	Forecast Changes since March	Non-Economic Changes since March	June 2023 Forecast	March 2023 to June 2023 comparison
2023-25 Biennium	$65.702 bil	+$287 mil	+$39 mil	$65.999 bil	**$327 million increase**
2025-27 Biennium	$70.342 bil	+$198 mil	+$38 mil	$70.490 bil	**$147 million increase**
					Four Year Total: $474 million

[1] Funds subject to the budget outlook include the state general fund (GF-S), the Education Legacy Trust Account (ELTA), the Opportunities Pathways Account (OPA), and the Workforce Education Investment Account (WEIA). Chapter 8, Laws of 2012, requires the legislature to adopt a four-year balanced budget. Since the 2013-2015 biennium, the legislature has been required to enact a balanced operating budget that leaves a positive ending fund balance in the general fund and related funds (ELTA, OPA, and WEIA). For more background on the Four-Year Outlook, see the Prevention Alliance policy brief on Washington's Four Year Outlook.

Another budget indicator that is tracked is the amount in 'reserves'. Reserves are comprised of the projected ending balance (projected revenue and other resources minus estimated expenditures) combined with the amount in the Budget Stabilization Account, which is also known as the Rainy-Day Fund. The total reserves are estimated at $4.124 billion for the 2023-25 biennium. The total reserves amount still includes a remaining balance of $798 billion from the Washington Rescue Plan Transition Account (WRPTA), which is funding for COVID-19 response and recovery. The funding in that account includes both state funding as well as any remaining federal COVID response dollars (such as from the American Rescue Plan Act (ARPA)).

All these numbers show that overall, the June 2023 economic and revenue forecast projects improved revenue numbers. Major factors that drove the improved forecast include:

- U.S. and Washington State employment numbers have increased.
- Automobile sales in May reached their highest level in two years.
- The state capital gains tax yielded higher than expected collections and therefore the forecast for that revenue source was adjusted.
- Construction activity was slightly stronger than projected in March.
- Retail sales tax and use tax were slightly stronger than expected.

While this indicates a positive forecast showing an increase in revenue, the state economist, Dr. Steve Lerch, urged caution in that optimistic forecast. Even though revenue collections have been strong over the past couple of months, he also noted that Washington revenue collections growth has slowed, and while inflation continues to slow it remains high.

Whenever the ERFC produces the quarterly forecast, they include both potential upside and downside risks that could impact the forecast as released, for better or for worse. Some concerning indicators for economic and revenue projections include:

- Continued potential for a recession
- Technology sector layoff could be larger than expected
- The banking crisis could intensify
- Inflation could remain elevated
- The ongoing Russia – Ukraine conflict could intensify

While the current forecast may show a positive trend, the concerning factors listed above could result in a more pessimistic landscape and potential reduction in projected state revenue by the time we get to the 2024 legislative session. In fact, the pessimistic June 2023 alternative forecast produced by the ERFC projects a *reduction* of $4.52 billion for the current 2023-25 biennium (as opposed to a $327 million increase).

It is important to remember that all these numbers are simply projections, or the 'best guess', based on available data and the economic landscape. Budget writers, the Governor's office, state agencies, and advocates will be tracking actual revenue collections in the coming months to see which way the economic and revenue climate goes – more toward the optimistic or pessimistic projections.

What's Next
At this point in the year, state agencies are hard at work pulling together the funding requests (known as decision packages) that they may put forward for the Governor to consider for inclusion in his 2024 supplemental budget, which he will release in mid-December 2023. While the strength of the June revenue forecast provides a sense of stability, it does not indicate a large amount of growth and there continues to be a significant level of anticipated instability in the economic landscape. The nominal forecast changes combined with the fact that the upcoming session is a short session where the legislature crafts the supplemental budget indicates we will likely see fairly modest decision packages from state agencies. This messaging is echoed in the budget instructions for state agencies released by the Office Financial Management in June 2023. The budget instructions, which agencies follow as they prepare their decision packages, state that agencies should focus their submittals on non-discretionary changes (ex. legally mandated caseloads), technical corrections, adjustments to federal or private local funding, and other high priority needs that must be completed during the 2023-25 biennium. The only new or expanded policies that agencies should submit are directed to be consistent with Governor Inslee's highest priorities. Agency decision packages are due to the Office of Financial Management on September 13th.

The ERFC will convene again in September to release the fall quarterly revenue forecast, which will further build out the economic and revenue landscape as we prepare for the 2024 legislative session.

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