Indiana Fiscal Policy Institute

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NEWS RELEASE

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Closing the Books on Fiscal Year 2005: An Improved Outlook, but More Must be Done

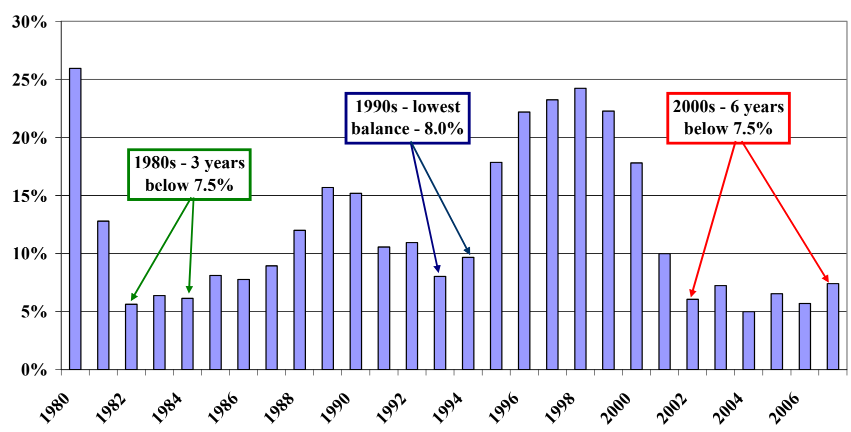
The Indiana Fiscal Policy Institute (IFPI) today released its latest Bulletin, "Closing the Books on Fiscal Year 2005: An Improved Outlook, but More Must be Done." Thanks to the tightly crafted budget and an improving revenue collection picture, the Governor announced on July 15^{th} an improving fiscal outlook and the beginning of "a new era of financial responsibility."

"If the State of Indiana is to complete its return to fiscal health, revenue forecasts must be met and remain steady, and the spending restraint of the FY 2006-2007 biennial budget must continue through FY2009," said Steve Johnson, President and CEO of the Indiana Fiscal Policy Institute. "Indiana needs a good and growing economy and our elected leadership must continue to make fiscally sound decisions."

The fiscal year (FY) 2005 year-end reserve balances were larger than last year at $749.8 million and the Office of Management and Budget now projects reserve balances of about $921.2 million, or 7.4% of revenue at the end of the current budget cycle.

However, those balances mask a still precarious perch. The report finds that should the budget projections hold true, the State will have experienced six years of reserve balances below 7.5% of operating revenue by the end of the FY 2006-2007 biennium. These are historical lows for historically long periods, as balances remained below 7.5% for only three years in the 1980s, following the severe, double-dip recessions of 1980 and 1981-1982.

Figure 1.
Combined Reserve Balances
as Percent of Operating Revenue



Source: Indiana State Budget Agency

The slow recovery and low balances mean that delayed payments to local governments, schools and higher education institutions most likely will not be reversed during this biennium. These delayed payments are a $700+ million liability incurred to help the State through the 2001 recession and remain in place four years later. More importantly, the technique, which has been used in each of the last three recessions is, until repaid, unavailable should the economy slow significantly during the next two years.

The report also finds that FY 2005 was the first year since 1999 that revenue collections exceeded their "budget-based" forecast. This followed a nine year period, beginning in 1992, during which revenue collections exceeded the budget-based forecast every year.

Since 2003, revenue growth has been strong. Annual revenue growth was 13.4% in 2003 (due in part to tax restructuring in 2002), 7.5% in 2004, and 7.7% in 2005. In contrast to the mid-1990s, when similar revenue growth led to large surpluses, reserve balances remain low. The primary reasons for that are the depth of the impact of the 2001 recession on revenue collections and the inclusion of an $800 million annual increase in property tax relief in the tax restructuring legislation.

For the first time since 1998, and after four years of very tight budget management in fiscal years 2004 through 2007, revenue will exceed expenditures in FY 2007. The 2006-2007 budget limits expenditure growth to about 4.7% in 2006 and 1.3% in 2007. Much of the budget's constraint involves the capping of the very property tax relief passed just 4 years ago in 2002. Combined over the two year biennium, expenditures for K-12 education, higher education, and property tax relief increased by only 0.9%, while the rest of the budget increased by 9.7%.

Johnson added, "Without question, the State's fiscal condition is better this year than last. The Governor and the General Assembly enacted a budget that made significant progress toward stability and fiscal health. But they should not be overly comforted, because the State's balances remain and are projected to remain at historical lows while payments delayed to local government, schools, and colleges and universities have not been reversed. While we cannot predict exactly when the next recession will come, history says we should be prepared for the unexpected. To lead us to the new era of financial responsibility, the Governor and the General Assembly have more work to do."

This report is available through the following link: http://www.indianafiscal.org/Bulletin2005-1.pdf, on-line at http://www.indianafiscal.org/pubs.html or by contacting the Indiana Fiscal Policy Institute, One North Pennsylvania Street, Suite 1000, Indianapolis, IN 46204, Telephone 317-237-2890, FAX 317-237-2893, or email us at IFPI@indianafiscal.org.

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