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ILLINOIS ECONOMIC AND FISCAL POLICY REPORT

The Governor's Office of Management and Budget (GOMB), pursuant to 20 ILCS 3005/7.3, annually submits an Economic and Fiscal Policy Report to the General Assembly outlining the long-term economic and fiscal policy objectives of the State, along with the economic and fiscal policy intentions for the upcoming fiscal year and for the subsequent four fiscal years. The report also includes a comparison of the current fiscal year's enacted budget with the current outlook for the fiscal year along with fiscal and policy options GOMB recommends for consideration by the General Assembly and the Governor to remedy any budgetary shortfalls in the current year or the five following fiscal years.

ECONOMIC REVIEW

NATIONAL ECONOMIC CONDITIONS

As the United States emerges from the COVID-19 Pandemic, national economic conditions have mostly recovered back to their pre-pandemic levels. While the shock caused to the economy by the pandemic was unlike anything seen in a generation, its recovery phase has proven to be much stronger and faster than expected. Since the 2020 recession ended in April 2020, U.S. Gross Domestic Product (GDP) has seen periods of both positive and negative growth. After experiencing a severe contraction in the Spring of 2020, GDP surpassed its pre-recession peak by the second quarter of 2021, one year after the trough of the recession, helped by trillions of dollars in federal stimulus and the rapid development of COVID-19 vaccines. The start of 2022 switched to a different story. U.S. GDP growth struggled with decreases of 1.6 and 0.6 percent in the first and second quarter respectively, due in large part to decreases in private inventories and fixed investments but advance third quarter data released by the Bureau of Economic Analysis (BEA) on October 27, 2022, showed a GDP increase of 2.6 percent.[1] The uneven economy still faces headwinds in the form of persistent inflation and tightening monetary policy and will be a challenge for states' economies and for those who are still struggling following the 2020 recession.

While overall U.S. economic output faces uncertainty, the U.S. labor market represents a better story. Employment normally recovers slower than output after a recession due to uncertainty in the demand for

goods and services but the post-2020 recession labor market has exceeded expectations. The September 2022 unemployment rate recovered to 3.5 percent from a record high of 14.7 percent (April 2020) in just 23 months; it took the same metric more than six years to fall to its pre-recessionary low following the Great Recession.[2] Total nonfarm employment which fell by 1.5 million jobs in March 2020 and 20.7 million jobs in April 2020 has added jobs each month (except December 2020) and by September 2022, national payroll employment had surpassed its February 2020 amount by 514,000 jobs. The labor force participation rate has made positive gains mostly for workers aged 25 to 54. Their labor force participation rate was 82.7 percent in September 2022, close to the pre-recession (February 2020) rate of 83 percent.[3]

While parts of the economy are holding on to recovery gains, others are raising serious concerns. Inflation has taken hold as a main economic concern. Prior to 2020, inflation often fell short of the Federal Reserve's 2-percent annual inflation target but pandemic-specific factors (supply-chain disruptions due to COVID-19, consumption shift from services to goods, and robust federal relief) caused an increase in prices that many thought would be temporary. Monthly inflation did subside during the summer of 2021 but quickly went back up. The inflation story continued into 2022 with the September 2022 Consumer Price Index – Urban Consumers (CPI-U) release showing prices up 8.2 percent over the last year.[4] Core inflation (which excludes volatile food and energy prices) was up 6.6 percent over the last year, its biggest 12-month gain since August 1982.[5]

Persistent price increases have necessitated an intervention by the Federal Reserve to squash inflation through interest rate adjustments. The Fed has raised its benchmark interest rates several times over the last year to a range of 3.75 to 4 percent. Federal Reserve Chairman Jerome Powell has remained committed to bringing inflation back down to 2 percent while acknowledging that some short-term pain is to be expected. According to most experts, the Fed's actions to fight against inflation make a recession the most likely scenario.[1] The consensus view among economists is that any recession that happens will be a mild one with a single period of below-trend recovery before returning to more sustainable pattern of economic growth.

Economic Framework, Inflation and Recession Risks

The year-over-year inflation rate as measured by CPI-U hit 9.1 percent in June 2022, its first time above 9 percent since November 1982. Price growth has slowed over the last few months, with September price indexes at 8.2 percent higher than they were a year ago. Earlier in the inflationary cycle, idiosyncratic shocks drove up prices in specific sectors, such as gasoline, airline tickets, and automobiles. The causes for these increases were as diverse as Russia's invasion of Ukraine, the precipitous decline in travel caused by the pandemic – and later spike in travel, and a shortage of computer chips. However, particularly over the last year, the Fed's so-called "sticky" inflation, a measure of inflation in "a subset of goods and services included in the CPI that change price relatively infrequently," has begun to rise and as of September 2022 is up 6.5 percent in the last 12 months.[6]

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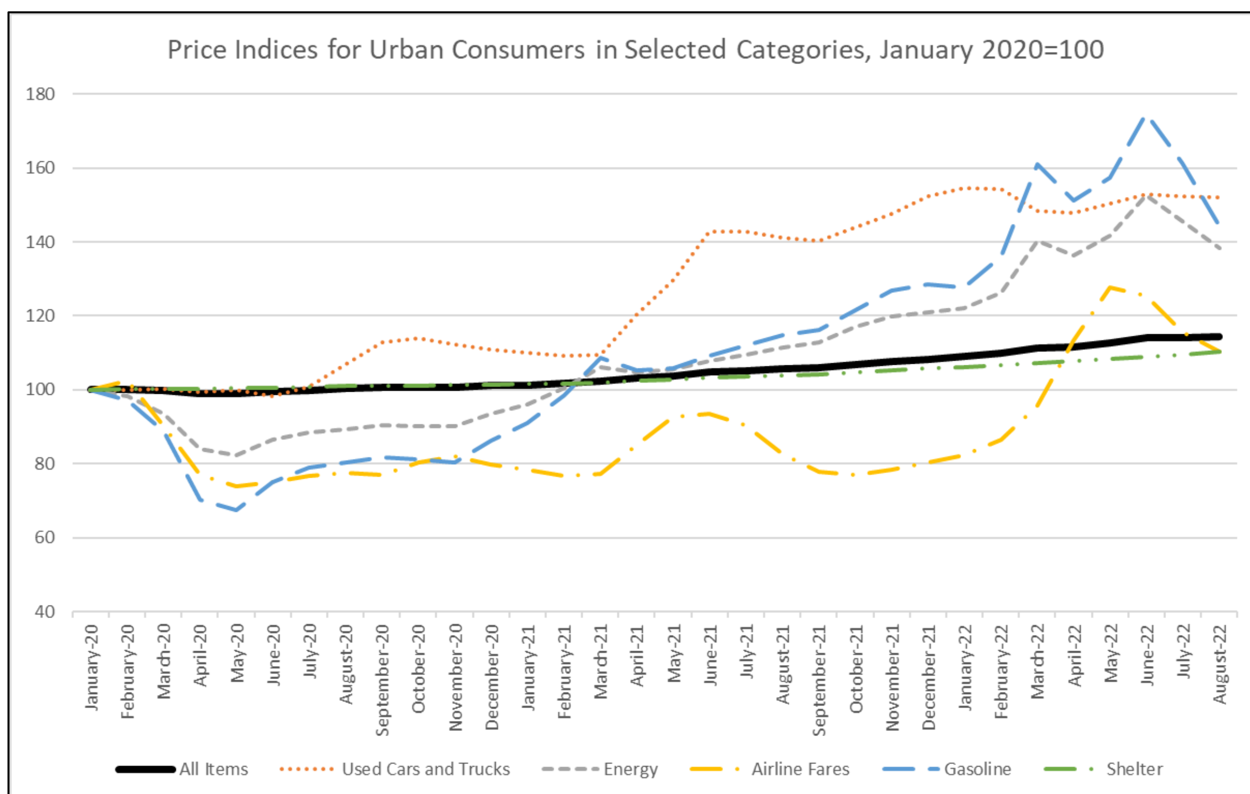
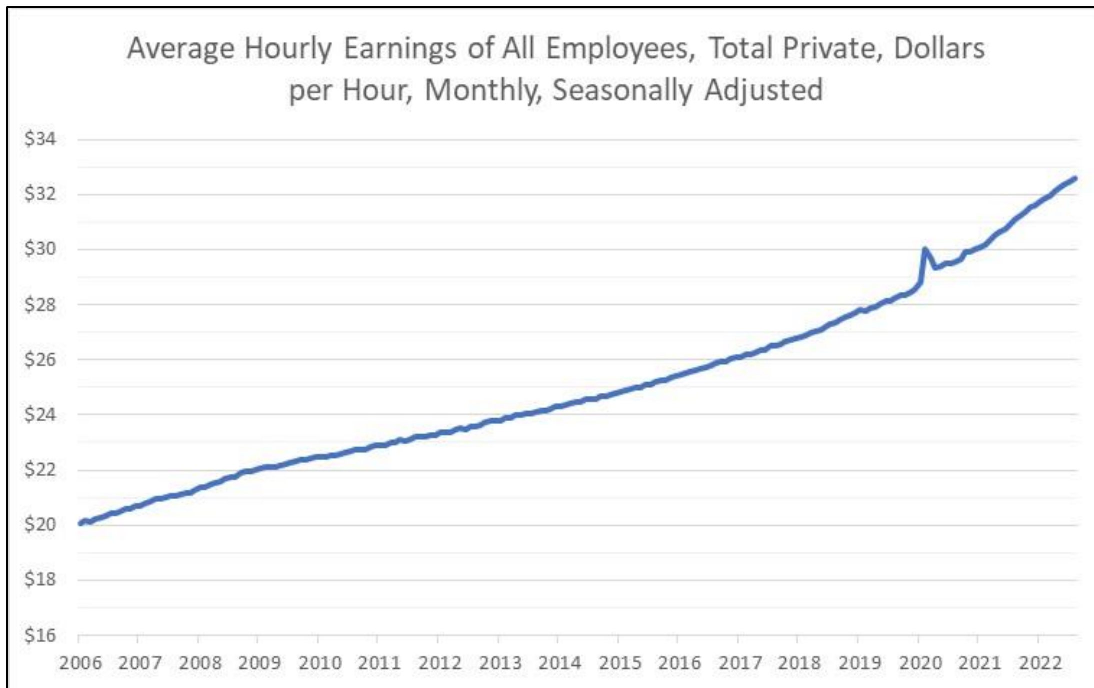
[1] According to the September CNBC Fed Survey, respondents place a 52 percent probability on a recession taking place in the next calendar year. Due to some leading recessionary indicators, some economists have placed the probability of a recession within the next calendar year at 80 to 90 percent.



Source: U.S. Bureau of Labor Statistics

As prices rose at their fastest rates since the 1980s, initial questions of whether the inflation was temporary or not, gave way to questions of how best to address rising costs. Economists and policymakers are still split over the extent to which sectoral price spikes can be attributed to short-term issues with supply chains and rapid shifts in demand, but the consensus is now that the economy needs to be slowed down. Crucially, this is the position of the Federal Reserve, which has set a goal of raising Federal Funds interest rates to about 4.4 percent by the end of 2022, a staggeringly fast rise from the near-zero rates seen as recently as March.[7]

Part of the theory behind the Federal Reserve's actions is that the labor market is still too strong, allowing workers to more easily seek out higher-paying jobs or demand pay increases, raising costs across many sectors, which runs counter to its dual mandate of maximum employment and price stability. Wages have in fact been rising; the average hourly earnings of private employees have increased by 0.4 percent per month since the economy stabilized after March of 2021; the pre-recession average from June 2009 to February 2020 was just 0.2 percent. While academic and research economists have conflicting viewpoints on the exact relationship between inflation and other measures of economic activity, there seems to be a negative correlation between unemployment and inflation, and a positive correlation between wage growth and inflation, suggesting that the faster wage growth seen in the last two years could be driving inflation.[8]



Source: U.S. Bureau of Labor Statistics

In response to rising costs, the Federal Reserve has introduced numerous interest rate increases designed to take money out of the economy by making it more expensive to borrow and more beneficial to save. By making it more expensive to borrow, the idea is to slow down spending, particularly large purchases such as homes, cars, and durable goods.[9] By reducing demand for a broad range of goods and services, inflation and then the economy, should slow down. The question then is how much the Federal Reserve will do and, crucially, whether it will go too far. If economic activity is slowed too much, it could lead to a recession. There is a possibility that, in part due to the methodology used to measure inflation, the Federal Reserve may, in fact, overshoot their goal and cause a recession.[10]

Recessions

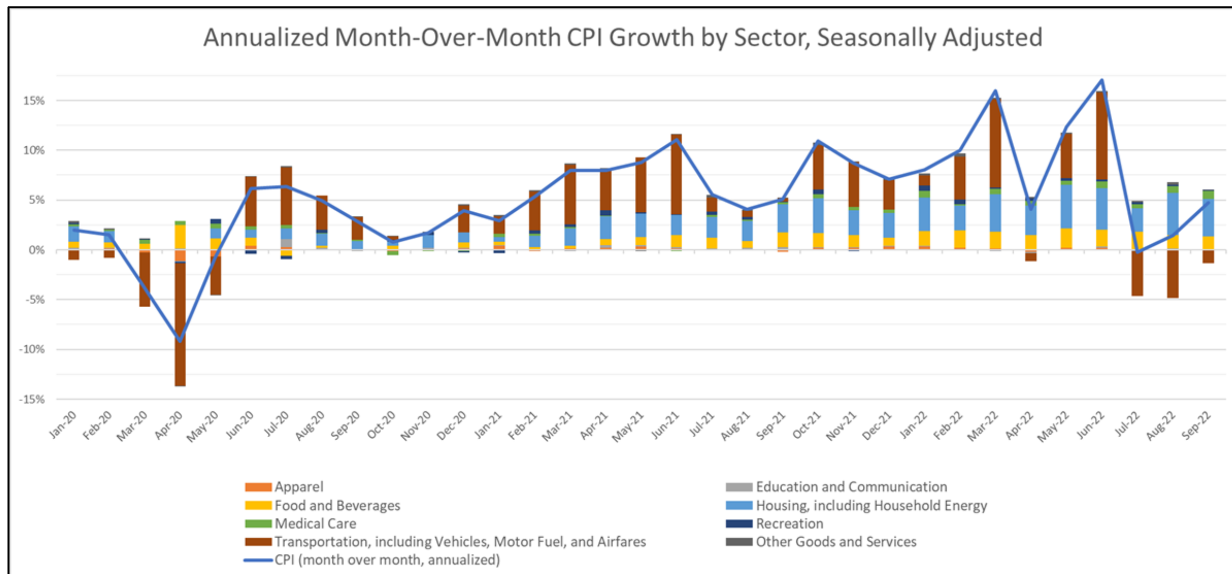
While there are conflicting definitions of a "recession," the determination is ultimately left up to the National Bureau of Economic Research (NBER) Business Cycle Dating Committee which often does not make that decision until years later. The Business Cycle Dating Committee maintains a chronology of U.S. business cycles and determines where the economy is in the business cycle. According to the NBER chronology, the most recent peak for the U.S. economy occurred in February 2020 and its most recent trough in April 2020. The NBER's definition of a recession emphasizes a significant decline in economic activity that is widespread and persistent. The committee's approach in determining dates of economic turning points is retrospective due to a lag in available data.

Economic activity is commonly measured by metrics such as real personal income less transfers, nonfarm payroll employment, employment as measured by the household survey, real personal consumption expenditures, wholesale-retail sales adjusted for price changes, and industrial production but no fixed rule applies to which measures are used.[11] In recent decades, the two most influential measures have been real personal income less transfers and nonfarm payroll employment. While a common shorthand for a recession is two consecutive quarters of decreasing real Gross Domestic Product (GDP), a measure of economic production adjusted for inflation, the NBER considers three criteria – depth, diffusion, and duration, along with the factors driving the economy.[12] While declines in GDP took place over two

consecutive quarters in calendar year 2022, the NBER Dating Committee has not determined that a recession has occurred and may not since a wider variety of economic measures remain strong.

Inflation

The different components of CPI have experienced periods of price growth and decline at different times. Even when incorporated into broad sectors, as seen in the figure below, inflation has been elevated across sectors over the last two years but has not been distributed evenly. Goods such as apparel have had relatively stable prices, but the broad-based inflation on sectors like food, energy, and durable goods have experienced multiple waves of price growth.



Source: U.S. Bureau of Labor Statistics

Real GDP and Productivity

U.S. Real GDP regained the 10.1 percent loss experienced in Spring 2020 (peak to trough) in only a year, an incredibly fast rate compared to the six quarters it took to regain the 3.9 percent contraction during the 2008-2009 Great Recession. The economy, as measured by GDP, shrank by 1.6 percent and 0.6 percent in the first two quarters of 2022, driving a belief among some economists and observers that the nation may already have entered a recession, but the NBER committee so far has not identified one. Advance third quarter GDP data, released October 27, 2022, came in at a higher-than-average annualized rate of 2.6 percent versus an estimated 2.3 percent.[13] The growth came in large part to a narrowing trade deficit, which economists expected and consider to be a one-off occurrence, increases in consumer spending, non-residential investment, and government spending. Declines in residential fixed investment and private inventories offset the gains due in large part to high interest rates.[14]

Labor Market and Income

A stalwart factor in the national economic framework has been the labor market and its continued growth amid other complicating economic factors. Recessions are often accompanied by high rates of unemployment, such as seen in the 2008 Financial Crisis.[15] In this moment, however, the unemployment rate is still extraordinarily low; unemployment has not been lower than the September 2022 mark of 3.5 percent since the 1960s. In addition, although it has not returned to its pre-pandemic levels, the labor force participation rate continued to increase in 2022.[16]

As discussed above, average wages are up significantly and increasing at a rate faster than before the 2020 recession. Real Personal Income, which includes transfer receipts, and is adjusted for inflation, has

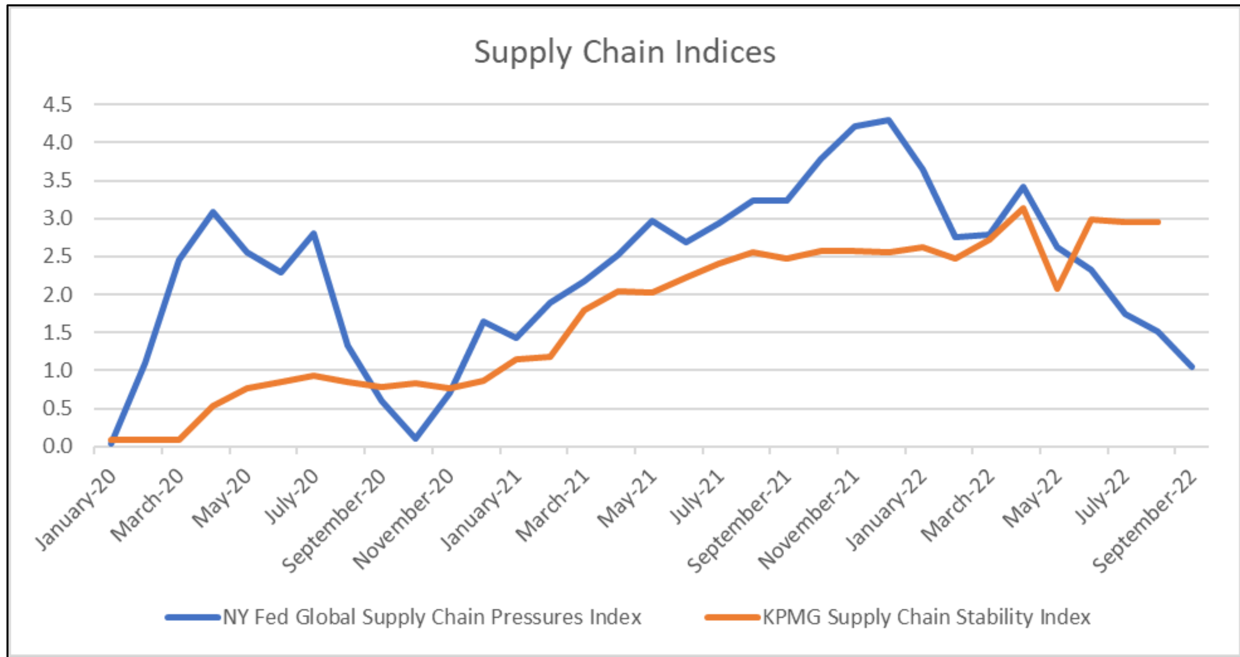
stagnated since June 2021 driven by the increase in inflation.[17] Additionally, Real Disposable Personal Income, which subtracts personal taxes, is down 5.4 percent since the second quarter of 2021. Real Disposable Personal Income is important to the national economy as it makes up a household's discretionary income. When discretionary income is increasing, households can consume or save more, which leads to a growth in consumption.

Personal Consumption and Saving

Since returning to its pre-pandemic level by January 2021, nominal Personal Consumption Expenditures have increased at 0.73 percent per month, almost double the average rate of 0.39 percent per month[18] from the end of the Great Recession to the beginning of the pandemic.[19] This trend, which appears at odds with stagnation in nominal disposable personal income, can be at least partially explained by two factors, savings and credit utilization. During the first two quarters of 2020, household savings nearly tripled from $1.59 trillion annualized in the first quarter to $4.69 trillion in the second due in large part to federal government stimulus checks and other payments.[20] The savings rate increased again following several other large federal stimulus packages. Now, Americans are dipping into rather than depositing into their savings. August's total personal saving was lower than any month since the Great Recession.[21] Another factor which has allowed consumer spending to stay high is usage of consumer loans such as credit cards; the total dollar amount of loans is greater than ever before and, since its pandemic-era low, has risen at triple the rate of the pre-2020 trend.[22]

Supply Chain

A major driver of rising costs early in the pandemic was the shutdown and later misalignment of the global supply chain. As time has gone on, supply chain issues have ebbed and flowed, often aligning with global COVID-19 outbreaks. The Federal Reserve Bank of New York's Global Supply Chain Pressure Index (GSCPI), which tracks global transportation costs and components of the Purchasing Managers Index such as delivery times, spiked in the middle of 2020, briefly returned to normal levels, and then spiked again, peaking in January 2022. The index is now declining, signifying a return to normalcy in the supply chain. The KPMG Supply Chain Stability Index (SCCI), which does not measure cost, but rather the ability of the supply chain to handle market volatility, has increased rather consistently since the beginning of the pandemic; this signified that the supply chain would be highly stressed by more market volatility.



Sources: Federal Reserve Bank of New York and KPMG/ASCM

Economic Forecasts

It is in the context of an uncertain economic outlook that this forecast is presented. Economic forecasts are evolving regularly. This report will discuss the 'baseline' economic forecast from October 2022 provided by IHS Markit (IHS), a national economic forecasting firm, but also incorporates aspects of the IHS September 2022 'pessimistic' forecast. IHS Markit gives its October baseline forecast a 55 percent probability and it reflects a mild recession from the fourth quarter of calendar year 2022 through the second quarter calendar year 2023, a shift from the September forecast that reserved the recession assumption for the 'pessimistic' scenario. The out-year revenue forecast is built as a hybrid of the October 2022 baseline outlook and aspects of the September 2022 pessimistic scenario. IHS' October 2022 projection for real GDP growth in calendar year 2023 is -0.5 percent and anticipates a U.S. GDP decline of 1.1 percent peak-to-trough and an anemic recovery in the second half of calendar year 2023. GDP is expected to grow at a below-trend of 1.3 percent in calendar year 2024, before increasing to 2.0 percent for both calendar years 2025 and 2026.[23]

This projected slowdown in economic activity is attributed to the factors described earlier, with the interest rate increases leading to decelerations in domestic consumption. In the forecast, aggregate demand has been largely impacted by the taming of inflation, resulting in increases in conventional mortgage rates, slumping stock prices, drops in national housing price indices, decreases in interest-sensitive spending, and restrictions in real personal consumption expenditures.

The baseline forecast assumes that the current tight labor market will loosen. The forecast assumes the national unemployment rate will increase 2.5 percentage points to 6.0 percent early in the recovery before settling to the full-employment rate of 4.3 percent by the end of calendar year 2023. Average payroll jobs growth is expected to slow to 55,000 jobs per month during the middle of calendar year 2023 and continue at that pace until calendar year 2025.

Personal consumption expenditures (PCE) on goods are expected to decrease in the first quarter of calendar year 2023. PCE on goods was boosted by fiscal stimulus and by substituting away from services

but have gradually declined as stimulus effects and inflation have eroded purchasing power. PCE on services during the same timeframe should see a slight acceleration. In the forecast, overall PCE growth will be constrained until economic conditions improve in calendar year 2024.

IHS's forecast has incorporated the impact of the Infrastructure Investment and Jobs Act (IIJA) and President Biden's student loan forbearance until December 2022 but has not included the President's plan to forgive approximately one-third of student debt. IIJA is expected to increase spending by $300 billion over the next five calendar years, GDP by 0.5 percent by calendar year 2025-26 and employment by 750,000 jobs before effects of the legislation wane as spending decreases.

IHS's forecast expects the Federal Reserve to maintain high interest rates until inflation subsides. The median projection of Federal Funds rate, which currently ranges between 4.5 percent and 4.75 percent, could increase by another 50 to 75 basis points in early calendar year 2023. The median projection could decline to 3.9 percent in calendar year 2024, 2.9 percent in calendar year 2025 and 2.5 percent in the long run, assuming inflation is under control.

Variables	FY23		FY24		FY25		FY26		FY27		FY28	
	(p)	(b)	(p)	(b)	(p)	(b)	(p)	(b)	(p)	(b)	(p)	(b)
U.S. Real Gross Domestic Product	-0.5%	0.3%	0.8%	0.1%	1.7%	1.7%	2.3%	2.1%	2.0%	1.8%	1.8%	1.8%
U.S. Corporate Profits	2.8%	1.9%	0.2%	0.7%	1.5%	1.1%	3.2%	2.7%	2.7%	2.7%	3.1%	3.4%
Illinois Unemployment Rate	4.9%	4.2%	6.6%	4.6%	7.3%	5.0%	6.6%	4.9%	5.9%	4.8%	5.2%	4.7%
Illinois Non-Farm Employment	1.4%	2.3%	-2.5%	-0.9%	-1.2%	-0.7%	0.4%	-0.1%	0.8%	0.1%	0.8%	0.0%
Illinois Wage and Salaries	6.4%	7.2%	1.1%	2.9%	1.5%	2.5%	3.1%	3.3%	3.7%	3.6%	3.6%	3.5%
Illinois Personal Income	3.3%	3.7%	1.7%	2.9%	3.4%	3.5%	4.0%	3.9%	3.9%	4.0%	3.6%	4.0%
Illinois Personal Consumption Expenditures	4.3%	4.7%	1.8%	1.6%	1.4%	1.9%	2.4%	2.7%	2.4%	2.8%	2.2%	2.8%

Source: IHS Markit September 2022 Forecast (p/pessimistic) and October 2022 Forecast (b/baseline) scenarios.

Illinois' Economic Conditions and Forecast

The economic conditions on the state level in Illinois are fairly like that of the country. Both economies continue to show strong signs of growth in areas such as employment and consumer spending, although measures like housing starts are down. The state has not been spared price increases for essential cost of living needs. Prices for rents, energy and food have all increased year-over-year, like the national economy. Salaries and average wages have increased but not kept pace with rising costs.

Real GSP and Productivity

As is the case for the national economy, real production, measured as Real Gross State Product (GSP) is up over the last year, but the two most recent quarters have shown decreases from one quarter to the next. As with the national economy, GSP not adjusted by inflation tells a different story; in nominal terms the state's GSP has increased by an annualized rate of 5 percent in every quarter since the beginning of 2021.[24]

Labor market

Illinois's labor market has seen similar trends to the nation; unemployment rose during Spring 2020 but has fallen to the current level of 4.5 percent. Labor force participation has regained its recessionary losses, and hourly earnings have continued to grow at a steady clip. Job postings on the website Indeed, a measure of total open positions, are up substantially in Illinois and nationally since the beginning of the pandemic.

Metrics (all seasonally adjusted)	February 2020 (pre-pandemic)	Pandemic-era max/min (mm/yy)	Sep-21	Aug-22	Sep-22
Unemployment Rate, United States	3.50%	14.7% (04/20)	4.7%	3.7%	3.5%
Unemployment Rate, Illinois	3.80%	17.4% (04/20)	5.5%	4.5%	4.5%
Labor Force Participation Rate, United States	63.50%	60.2% (04/20)	61.7%	62.4%	62.3%
Labor Force Participation Rate, Illinois	64.80%	62.3% (01/21)	63.1%	64.6%	64.20%
Average Hourly Earnings, United States	$28.81	$28.81 (02/20)	$30.88	$32.16	$32.40
Average Hourly Earnings, Illinois	$29.75	$29.75 (02/20)	$31.86	$32.54	$32.91
Job Postings on Indeed, United States (2/1/20=100)	98.6	61.0 (05/20)	143.9	150.2	149
Job Postings on Indeed, Illinois (2/1/20=100)	98.6	60.8 (05/20)	142.1	139.8	139.4

Sources: US Bureau of Labor Statistics, Indeed, and Federal Reserve Bank of St. Louis.

Note: "Pandemic-era max/min" is meant to represent the month at which the pandemic's effects were most severe and shows the month at which labor force participation, hourly earnings, and job postings were lowest, and at which unemployment was highest. Job postings data is updated daily; the figure used is from the last day of the month except for in the case of the max/min.

Economic Forecasts

State revenue growth has been particularly strong for sources tied to economic activity, particularly collections of individual and corporate income taxes. Most of this growth is attributed to temporary factors that boosted incomes in fiscal year 2021 and 2022 that are not expected to continue. Tight labor market conditions have allowed wages to grow faster than normal, while low interest rates allowed investors to take advantage of a growing stock market. Both factors have pushed taxable withholding and non-withholding income to levels not previously seen. Corporate profits have been well beyond historical highs, but their outlook remains uncertain. Higher interest rates have increased the cost of borrowing, making it more expensive for individuals and businesses to do so, while price increases have sapped the purchasing power of wages, creating a drain on consumer activity. Under both IHS forecasts, the projected slowdown for the national economy will have ripple effects for the state.

In both IHS forecasts, (baseline and pessimistic), real gross state product is anticipated to decline in fiscal year 2023 and remain at those levels until the national economy begins its recovery. The October baseline forecast presents a mild decline in the Illinois labor market, while the September pessimistic presents a deeper contraction in the state's labor market. In the September pessimistic forecast, the state unemployment rate could reach 6.6 percent by fiscal year 2024 and increase to 7.3 percent in fiscal year 2025. Wages and salaries could see a moderate decrease in fiscal year 2024 under both forecasts, before growing at a slower pace over the forecast horizon. This growth amid a national decline in hiring is mainly due to the diverse range of jobs found in Illinois. Long-term growth prospects will continue to see jobs added in the professional and business service sector, while receiving some growth in the manufacturing sector.

A Review of the Enacted Fiscal Year 2023 Budget

On April 19, 2022, the Governor signed into law the State's fiscal year 2023 budget, contained in Public Acts 102-0698 and 102-0699. The fiscal year 2023 budget plan makes substantial investments in long-term debt reduction, increases funding for education, including $350 million for the State's evidence-based funding formula, increases university and community college operational funding, and authorizes an additional $122 million for need-based aid for college students. The budget increased funding for human service and public safety agencies, and fully funds certified pension contributions. At the time of budget enactment, a general funds budget surplus of $444 million (of which $312 million would be reserved in the Budget Stabilization Fund, for a net surplus of $132 million) was projected.[25] The balanced

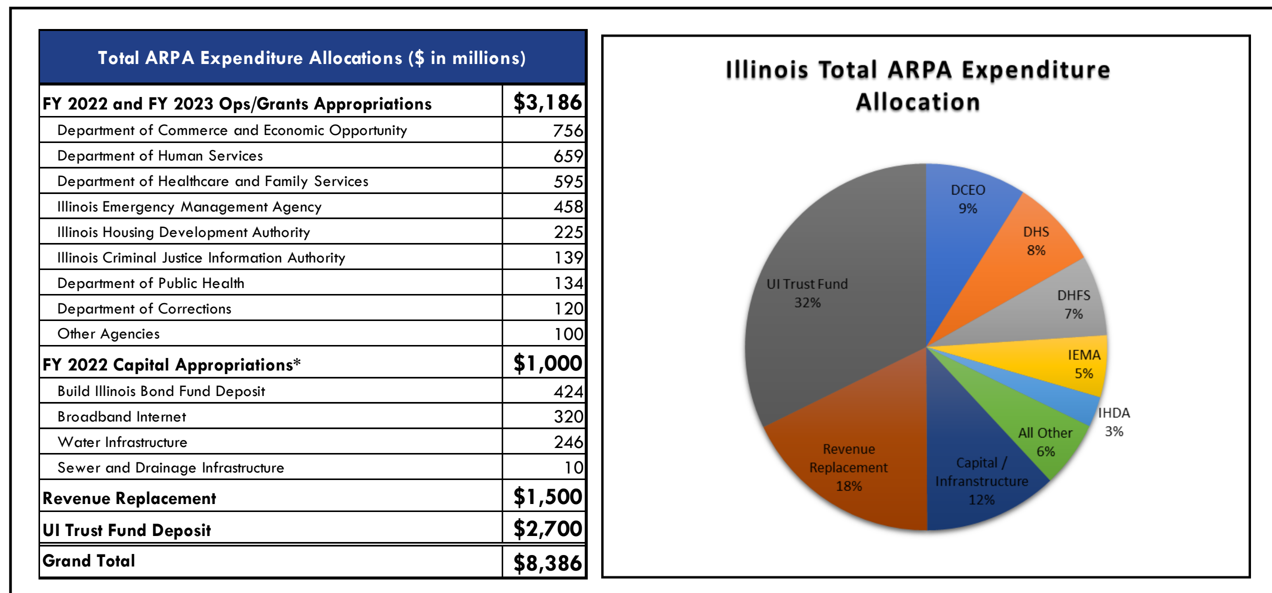
budget will allow Illinois to keep pace with the payment of the State's bills and maintain progress made on the payment delays in state bills, with vendor payment delays at the lowest levels in recent years.

The enacted fiscal year 2023 budget built upon previous fiscal responsibility investments. Following an additional $300 million contributed to the systems above certified amounts in fiscal year 2022, the budget set aside an additional $200 million for payments to the State's pension systems in excess of the statutorily required contributions for fiscal year 2023. The commitment towards long-term financial security was also continued through an additional Budget Stabilization Fund contribution of $312 million, pushing the total commitment to the Budget Stabilization Fund to over $1 billion by the end of fiscal year 2023, the largest balance the fund will have had since its creation. The enacted fiscal year 2023 budget also created permanent revenue streams for the Budget Stabilization Fund by depositing an ongoing portion of cannabis revenues (10 percent or approximately $30 million) plus monthly transfers of $3.75 million beginning July 1, 2023. As of October 31, 2022, the balance in the Budget Stabilization Fund totaled $1.045 billion.

The fiscal year 2023 budget framework provides approximately $1.83 billion in tax and fee relief to State taxpayers (of which $1.4 billion was set aside during fiscal year 2022) consisting of the following: (i) $520 million for a one-time tax rebate payment of 5 percent of property taxes paid, up to $300, (ii) $685 million for a one-time tax rebate payment of $50 per adult and $100 per dependent, (iii) $400 million for a one-year suspension of the State tax on groceries and a six-month delay in the motor fuel tax cost-of-living adjustment, (iv) $50 million for one-time back-to-school relief for families and teachers, and (v) $100 million for the ongoing expansion of the earned income credit for working families.

The fiscal year 2023 budget also allocated the majority of the remaining federal dollars received from the American Rescue Plan Act (ARPA) $8.38 billion Coronavirus State Fiscal Recovery and Coronavirus Capital Projects funds to one-time expenditures in (i) affordable housing, (ii) assistance to long-term care facilities and workers, (iii) assistance for hotels, restaurants and cultural or arts groups, (iv) assistance for tourism recovery programs and (v) funding for hospitals and ambulances.

These allocations built on initial allocations in the fiscal year 2022 budget, which allocated $2.7 billion for repayment of advances related to the State's unemployment insurance trust fund and other dollars to key areas like infrastructure, small business grants, violence prevention, healthcare, affordable housing, state agency response costs, and economic recovery. In addition to these investments, $1.5 billion was used to replace previously lost revenues to the State due to the pandemic, to fund essential government services as allowed under ARPA.



Total ARPA Expenditure Allocations ($ in millions)	
FY 2022 and FY 2023 Ops/Grants Appropriations	**$3,186**
Department of Commerce and Economic Opportunity	756
Department of Human Services	659
Department of Healthcare and Family Services	595
Illinois Emergency Management Agency	458
Illinois Housing Development Authority	225
Illinois Criminal Justice Information Authority	139
Department of Public Health	134
Department of Corrections	120
Other Agencies	100
FY 2022 Capital Appropriations*	**$1,000**
Build Illinois Bond Fund Deposit	424
Broadband Internet	320
Water Infrastructure	246
Sewer and Drainage Infrastructure	10
Revenue Replacement	**$1,500**
UI Trust Fund Deposit	**$2,700**
Grand Total	**$8,386**

Note: Allocations above are from Illinois' share of the State Fiscal Recovery Fund and the $254 million Coronavirus Capital Projects Fund.

Updated Fiscal Year 2023 Projections

Following a review of the fiscal year 2023 general funds revenue performance year-to-date, GOMB is revising the budget forecast as outlined in the following table. Even with troubling national economic factors, through the first four months of fiscal year 2023, income and sales taxes exceeded budget forecasts by significant margins,[26] reflecting the conservative nature of the initial forecast. As a result, GOMB is reporting a $1.473 billion increase in the revenue forecast from those sources. Additionally, a larger than forecasted end of fiscal year 2022 balance in the Income Tax Refund Fund (due to stronger than expected income tax performance last fiscal year) has contributed a one-time bump in the annual transfer from the fund of $1.28 billion. In total, the general funds revenue forecast is revised upward by $3.69 billion, using a review of the performance fiscal year-to-date and the economic projections under the IHS September 2022 pessimistic/October 2022 baseline forecast for fiscal year 2023. However, GOMB is continuing to monitor these forecasts closely as inflation and national/international factors may impact the economy in uncertain ways. Note that most of this fiscal year 2023 revenue forecast revision is assumed to be one-time in nature.

With the foregoing revisions, fiscal year 2023 base revenues and transfers from other State funds are estimated to total $45.256 billion, a decrease of $494 million (1.1 percent) from fiscal year 2022 base levels. The State's three largest revenue sources, individual income tax, corporate income tax, and state sales tax, are estimated to total $38.738 billion in deposits to the general funds in fiscal year 2023, a decrease of $1.7 billion (4.3 percent) when compared to fiscal year 2022 totals. The fiscal year 2023 estimate assumes deposits of $3.016 billion into the Local Government Distributive Fund, Road Fund, Public Transportation Fund, and Downstate Public Transportation Fund from income and sales tax receipts prior to the deposit of these revenue sources into the general funds.

Changes to FY 2023 Projections ($ in Millions)			
Revenues		**Expenditures**	
Individual Income Taxes	$ 638	SERS Prior Year Underpayment	
Corp Income Taxes	654	Continuing Appropriation	$ 33
Sales Taxes	181	Reduced Lapse Est (PHE HFS Spend)	500
Transfer from Refund Fund	1,281	Debt Issuance Timing	24
Federal Sources	863	Recommended Supplementals	250
All Other Changes	73	All Other Changes	25
Total Base Revenue Changes	**$ 3,690**	**Total Changes**	**$ 832**

Revision to Forecast	
Enacted Budget (Deficit)	$ 132
Increase to Base Revenue Forecast	3,690
Increase in Projected Expenditures	(832)
Proposed Add'l Rainy Day Fund Contribution	(1,300)
Revised Surplus/(Deficit)	$ 1,689

Note: Totals may not add due to rounding.

Other state source revenues are projected to total $3.224 billion, a $46 million decrease from fiscal year 2022. Transfers to the general funds are projected to total $3.294 billion, an increase of $1.202 billion (57.5 percent) from fiscal year 2022.

Federal revenues are projected to total $4.100 billion, a decrease of $484 million (10.6 percent) from fiscal year 2022 federal revenues. This year-over-year decrease reflects the expected drop of enhanced federal match three-quarters into fiscal year 2023. The federal revenue forecast increased from previous estimates due to the extension of the federal Public Health Emergency (PHE), which extends the enhanced Medicaid match rate on State expenditures, but the estimated spend by Department of Healthcare and Family Services, the State's Medicaid agency, is also increased to cover the cost of the PHE extension.

Additionally, the fiscal year 2023 revised federal revenue forecast includes $763 million in transfers from federal ARPA dollars to reimburse the State for revenues lost due to the pandemic. The timing of the transfer contributes to the revised surplus expected for fiscal year 2023. Revenue replacement transfers totaled $737 million in fiscal year 2022, bringing the total to $1.5 billion across the two fiscal years.

The fiscal year 2023 budget's revised estimated base operating expenditures are $46.568 billion. Base statutory transfers out of the general funds are projected to decrease by approximately $317 million to $405 million in fiscal year 2023 from fiscal year 2022 transfers out of $722 million. Debt service for GO Bonds is projected to total $1.604 billion from the general funds. As noted above, HFS spend is estimated to increase with the extension of the Public Health Emergency (reflected in the adjustment to the lapsed appropriations estimate).

GOMB has identified potential supplemental general funds budget pressures for fiscal year 2023 totaling approximately $250 million, including additional funds for the Department of Innovation and Technology. Additionally, the Governor proposes reserving in the Budget Stabilization Fund the additional $1.3 billion transferred from the Income Tax Refund Fund end of fiscal year 2022 balance. After accounting for these changes and the supplemental budget pressures, the revised fiscal year 2023 surplus is projected to total $1.689 billion.

FIVE YEAR BUDGETARY FORECAST

Pursuant to 20 ILCS 3005/7.3, attached to this report is a financial walk down of the budgetary outlook for fiscal year 2023 through fiscal year 2028.

The projections assume growth in revenues under existing law in fiscal year 2023 and the remainder of the forecast period following a hybrid blend of the October 2022 IHS baseline forecast and the pessimistic IHS September 2022 economic forecast. Expenditure projections are driven by statutory increases in pension payments based on end of fiscal year 2023 actuarial results, projected debt service amounts, and moderate increases in other spending. Expenditure projections are trend growth numbers that assume no significant reforms or spending controls aside from what is in current statute.

Estimated Resources

GOMB estimates that under current statutes, base general funds revenues for fiscal year 2023 will total $49.356 billion. Revenue estimates going forward are based on projections provided by Illinois Department of Revenue economists based on IHS's September pessimistic/ baseline October forecast.

The diversion rate of 9.25 percent of total individual income tax revenues in fiscal year 2023 to the Income Tax Refund Fund is assumed to continue for the remainder of the forecast. The corporate income tax forecast assumes a refund fund diversion rate of 14.5 percent in fiscal year 2023 and is maintained over the remainder of the forecast.

Fiscal year 2023 sales tax revenues are estimated to total $10.261 billion. Fiscal year 2023 and future years reflect the continued impact of the gradual shift of state sales tax on motor fuel purchases from the general funds to the Road Fund, with approximately $450 million (2 percent of the total 5 percent state share) estimated to shift in fiscal year 2023, the second year of the phase in. The shift reaches full implementation in fiscal year 2026, when the entire 5 percent state share of sales tax on motor fuel purchases will be allocated to the Road Fund.

Fiscal year 2023 estimated base general funds receipts from federal sources total $4.100 billion. This estimate is based on appropriations that are expected to generate federal match if payments are released timely and nine months of enhanced FMAP of 6.2 percent on Medicaid expenditures related to the COVID-19 federal public health emergency declaration. Generally, federal reimbursements for Medicaid spending are returned to the same fund that was used for the original expenditure. It is assumed that the Department of Healthcare and Family Services will continue to maximize use of general funds for Medicaid spending, which will produce moderate growth over the forecast horizon. However, fiscal year 2024 reimbursements will be lower than fiscal year 2023 estimates with the drop off of the enhanced FMAP after the third quarter of fiscal year 2023 and an estimated increase in the base Medicaid match rate beginning in October 2023.

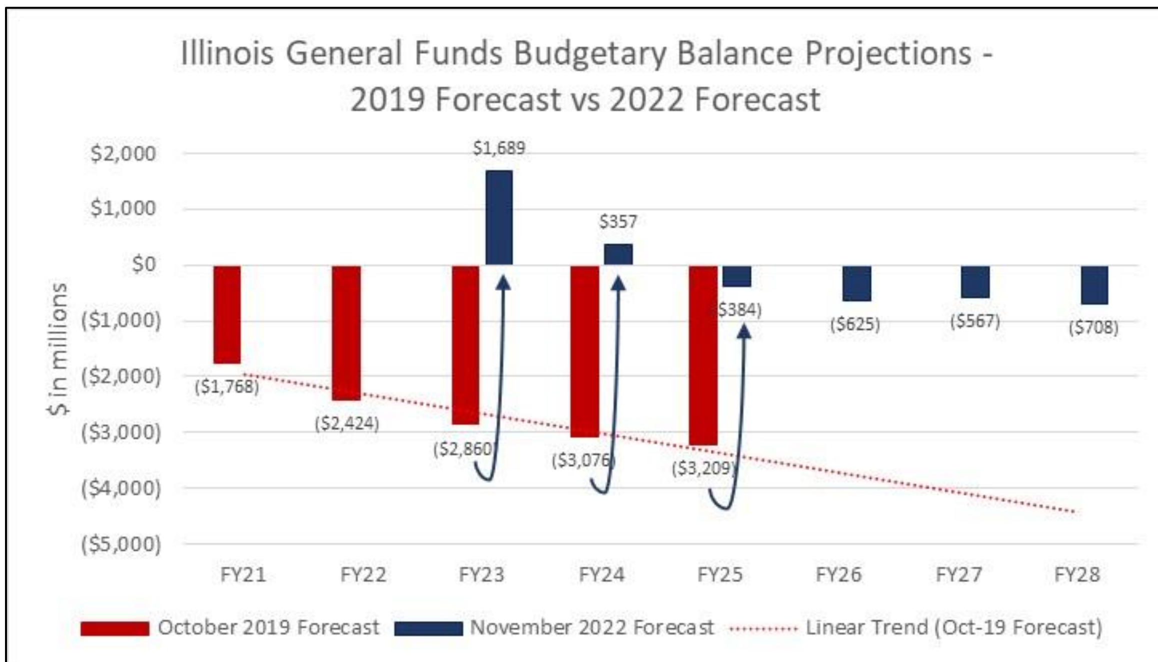
Estimated Expenditures

Fiscal year 2023 estimated general funds spending in the financial walk down totals $46.568 billion. Future-year spending estimates are based on an assumed increase in evidence-based funding for education by a minimum of $350 million per year, moderate growth rates in the various categories of state spending from fiscal year 2023 appropriations, pension spending consistent with the retirement systems' projections from fiscal year 2022 actuarial reports, and no significant changes to base programs.

Fiscal Year Results

As noted above, GOMB estimates fiscal year 2023 revenues will exceed expenditures by $1.689 billion. This is a major sign of notable progress on state finances considering that when Governor Pritzker came into office, the structural deficit was estimated to be approximately $3.2 billion a year[27]. Substantially

reducing the structural deficit reflects the commitment of the Governor and the General Assembly to achieving fiscal health for Illinois for the foreseeable future. The chart below compares the annual forecasted deficits as of October 2019 compared to the current forecast.[28] The Governor remains committed to taking steps to further improve Illinois' fiscal position.



POLICY OBJECTIVES AND INTENTIONS

Governor Pritzker remains committed to maintaining fiscal stability in Illinois' budget and spurring statewide economic growth. A key priority is investing in Illinois' people, educational system, infrastructure, and programs that assist the most vulnerable. These investments will strengthen the economy and ensure that Illinois is a strong competitor in the global marketplace.

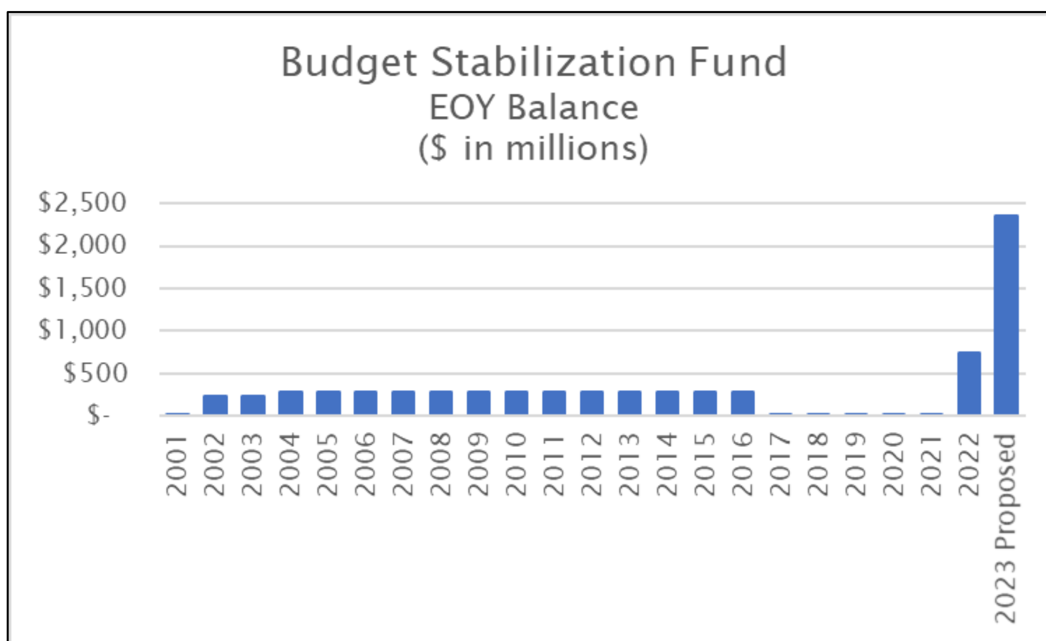
Even with a balanced budget for fiscal year 2023 and a significantly improved financial trajectory, the State must continue to build on the progress made in recent years while carefully preparing to face an uncertain fiscal outlook due to national economic conditions. Illinois is constitutionally required to pass a balanced budget for each fiscal year – thus, any challenges must be addressed as they arise.

The fiscal year 2022 budget allowed for additional steps toward fiscal stability through actions such as early repayment of COVID-19 Pandemic borrowings, directing funds to further pay down the state's existing payables and reserving additional funds for future fiscal emergencies or economic downturns. The fiscal year 2023 budget, and the Governor's proposed changes to the enacted fiscal year 2023 budget, build on the progress in the fiscal year 2022 budget. These actions, along with continued investment in economic development and responsible budget management on the spending side, will improve the budgetary outlook for future years.

Saving for the Future. The Governor is recommending the State take additional steps to prepare for the future and the potential impact of an economic recession. Keeping Illinois on a path for fiscal stability

requires further investment in the Budget Stabilization Fund. Illinois created the Budget Stabilization Fund in 2001 with the intent to use it as a "rainy day" fund for future fiscal emergencies or economic downturns. After that original funding, very little was contributed to the fund, and it was used as a tool to assist with cash flow until it was nearly drained in fiscal year 2017. During fiscal year 2017, the $275 million Budget Stabilization Fund balance was used to pay bills related to the budget impasse.

The COVID-19 Pandemic demonstrated how important a rainy day fund is to stabilizing state finances. Some states drew on their rainy day funds in 2020, while Illinois and a few others turned to short-term borrowing for cash flow assistance during the pandemic. However, strong revenue performance nationally in 2021 and 2022 enabled states to replenish and even increase their rainy day funds from fiscal year 2020 levels - the 50-state total of rainy day fund balances increased to a record level of $82.3 billion. While Illinois has its highest balance ever at $1.045 billion, Illinois is still among the smallest state rainy day funds.[29] The Governor recommends that the State make additional deposits into the Budget Stabilization Fund with the surplus balance transfer from the Income Tax Refund Fund received in fiscal year 2023. An additional contribution of $1.3 billion would bring the balance in the Budget Stabilization Fund to approximately 5 percent of state source general funds revenues.



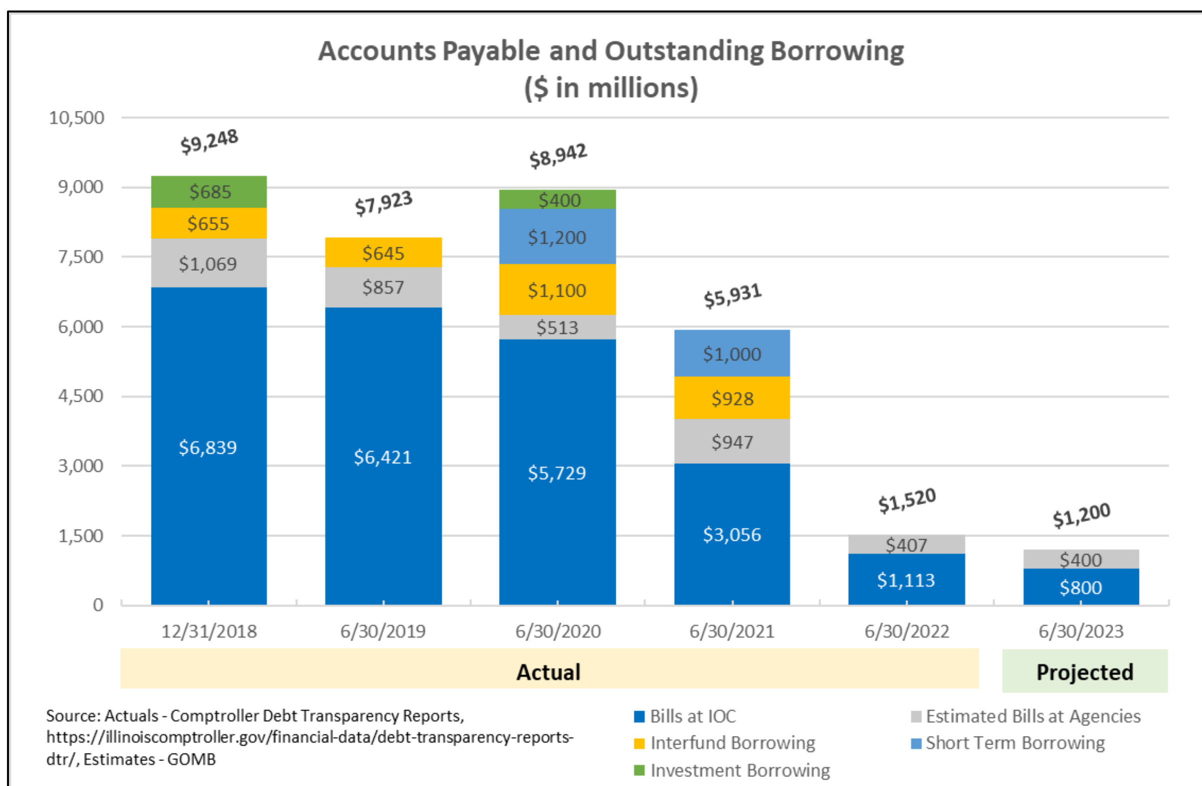
Reducing Debt Obligations and Saving on Interest Costs. In 2020, the State undertook several borrowings to address the revenue shortfalls brought on by the COVID-19 Pandemic, including $3.2 billion in borrowing from the Federal Reserve Municipal Liquidity Facility (MLF), millions in interfund borrowing, and $400 million under the State Treasurer's investment borrowing powers. As of the end of fiscal year 2022, the State had paid back these borrowings in their entirety – reducing interest costs and removing the burden of repayment from out years.

For fiscal year 2023, the Governor proposes to direct funds towards the remaining Railsplitter Tobacco Settlement Authority bonds. In December 2010, the Railsplitter Tobacco Settlement Authority issued revenue bonds in the amount of $1.5 billion to address a portion of the State's unpaid bill backlog resulting from the Great Recession. The repayment stream is the State's tobacco settlement payments under the Master Settlement Agreement between various states and various cigarette manufacturers. Of the original $1.5 billion issued in 2010, approximately $561 million – or over 1/3 of the original issue - remains

outstanding. The Governor proposes working with the legislature to provide funds towards a cash defeasance of a portion of the remaining outstanding bonds with proceeds from a recent Attorney General settlement resolving claims regarding certain payments from tobacco companies.[30] Once the bonds are paid off, the tobacco payment stream would be freed up to be used as ongoing annual state revenues to support the State's Medicaid program.

Like many states, Illinois had a healthy balance ($1.85 billion) in its Unemployment Insurance Trust fund before the pandemic. To keep unemployment benefits flowing to jobless workers once the pandemic hit, the fund was drained, and the Trust Fund was forced to borrow money from the U.S. Department of Labor. Those funds must be repaid. After several steps taken by the Governor and the General Assembly to reduce the amounts owed from last year's level of $4.5 billion, Illinois' Trust Fund currently owes a remaining $1.345 billion plus interest. The Governor proposes dedicating a portion of the fiscal year 2023 surplus to make an additional contribution towards this advance and reduce the accruing interest burden of this Trust Fund liability.

Continued Reduction in Unpaid Bills. At the end of fiscal year 2022, the Illinois Office of the Comptroller's estimate for the general funds and Health Insurance Reserve Fund bill payables totaled $1.52 billion.[31] This reflects a reduction of $7.7 billion in liabilities since December 2018. In future budget years, maintaining this lower level by enacting balanced budgets will save Illinois taxpayers millions in interest costs and move Illinois closer to a customary accounts payable cycle. Additionally, proposed supplemental appropriations to support the costs of the Technology Management Revolving Fund will further reduce the State's limited remaining interest costs.



Economic Development Investments. The State's fiscal position is dependent on the strength of the businesses that underpin Illinois economy – providing jobs and investment throughout the state. With that in mind, the Governor is proposing a contribution to a business 'closing fund' to help the Department

of Commerce and Economic Opportunity with business development and provide the State the flexibility to tailor development packages to each unique situation.

Spending controls. To manage future year budget constraints, the Governor continues to instruct agency directors to prudently manage operations with the limited available resources of state government. During this administration, the Governor has implemented spending controls in a number of areas with new efficiencies. He believes the people of Illinois expect high quality programs and services, as well as the most efficient and effective use of their tax dollars. The Governor believes that support for quality education, access to health care, and sufficient social services are all part of the essential functions of state government. Optimizing operations while identifying all possible efficiencies will help the State achieve balanced budgets in future years.

ESTIMATED INTEREST EXPENSES

The State Prompt Payment Act (30 ILCS 540/3-2) specifies the timeframe in which bills for goods and services shall be paid. If the bills are not paid within the specified time frame, an interest penalty is applied for each month, or portion thereof, until final payment is made. Similarly, the Illinois Insurance Code (215 ILCS 5/368a and 5/370a) establishes timely pay for healthcare services under the State Employees Group Health Insurance Program. If healthcare services bills are not paid within the specified time frame, the healthcare service provider is entitled to interest for each month, or a portion thereof, until final payment is made.
In order to calculate the interest due to an eligible vendor or provider, an agency must know two critical dates: the date the proper bill or invoice was received by the agency and the date the payment to the eligible vendor or provider was issued by the Illinois Office of the Comptroller (the Comptroller). Agencies use the dates to calculate the amount of days that passed beyond the established payment timeframes and the appropriate interest due to the vendor or provider. Until such time as a bill is paid, the agencies are not able to calculate interest. The Comptroller determines which bills get paid and when, making it difficult for agencies to project an interest amount.

With respect to the State Employees Group Health Insurance Program, the Department of Central Management Services (CMS) estimates the program incurred approximately $27.4 million in interest expenses in fiscal year 2022. Additional resources were provided to CMS in Spring 2022 and as a result, interest expenses in the group insurance program are expected to reduce to much lower levels. With respect to the Technology Management Revolving Fund, the Department of Innovation and Technology carried over approximately $51.2 million in interest costs from fiscal year 2021 and 2022 into fiscal year 2023. The Department expects to incur an additional $15 million in fiscal year 2023, creating an end-of-year aggregated amount of outstanding accrued and pending late payment interest totaling $66.2 million.

Due to fluctuations in the receipt of invoices and the timing of the Comptroller's payment decisions, future interest expense estimates cannot be made. However, interest expenses should continue to trend downward, and may be close to eliminated entirely, if the Governor's proposed supplemental to address unpaid delayed bills in the Technology Management Revolving Fund is implemented. This is a significant improvement from recent years when agencies submitted to the Comptroller prompt payment interest vouchers and other CMS state employee health insurance interest payments at much higher levels – in fiscal year 2018, vouchers totaled $980 million, fiscal year 2019 - $160 million, fiscal year 2020 - $137 million, and fiscal year 2021 - $112 million, fiscal year 2022 - $35 million.

STATE OF ILLINOIS GENERAL FUNDS FINANCIAL WALK DOWN Governor's Office of Management and Budget						
($ in millions)	FY 2023 Estimated	FY 2024 Projected	FY 2025 Projected	FY 2026 Projected	FY 2027 Projected	FY2028 Projected
RESOURCES						
State Sources: Revenues						
Net Individual Income Taxes	23,215	23,909	24,784	25,785	26,938	28,202
Net Corporate Income Taxes	5,262	4,939	4,855	5,157	5,379	5,577
Net Sales Taxes	10,261	10,170	10,215	10,222	10,392	10,531
Public Utility Taxes	720	701	681	667	657	663
All Other Sources	2,503	2,467	2,472	2,466	2,465	2,467
Total State Sources: Revenues	**41,962**	**42,185**	**43,007**	**44,296**	**45,831**	**47,440**
State Sources: Transfers In						
Lottery	665	678	692	706	720	734
Gaming	157	200	230	255	270	270
Adult-Use Cannabis	142	151	160	166	171	176
Other Transfers	2,330	700	707	714	721	728
Total State Sources	**45,256**	**43,914**	**44,795**	**46,137**	**47,713**	**49,349**
Federal Sources	4,100	3,690	3,782	3,877	3,974	4,073
TOTAL RESOURCES	**49,356**	**47,604**	**48,578**	**50,014**	**51,687**	**53,422**
Treasurer's Investment Borrowing [1]	-	-	-	-	-	-
ARPA Reimbursement for Essential Govt Services	763	-	-	-	-	-
TOTAL RESOURCES WITH COVID-RELATED FEDERAL RECEIPT	**50,119**	**47,604**	**48,578**	**50,014**	**51,687**	**53,422**
EXPENDITURES						
1. Education	**12,000**	**12,506**	**13,018**	**13,536**	**14,060**	**14,591**
PreK-12 Education	9,758	10,210	10,665	11,125	11,590	12,059
Higher Education	2,242	2,297	2,353	2,411	2,470	2,531
2. Economic Development	**255**	**260**	**265**	**270**	**276**	**281**
3. Public Safety	**2,228**	**2,329**	**2,434**	**2,544**	**2,659**	**2,780**
4. Human Services	**8,832**	**9,196**	**9,597**	**10,016**	**10,454**	**10,912**
5. Healthcare	**8,165**	**8,500**	**8,755**	**9,018**	**9,288**	**9,567**
6. Environment and Culture	**89**	**91**	**93**	**95**	**97**	**99**
7. Government Services	**3,677**	**3,691**	**3,793**	**3,897**	**4,003**	**4,112**
Group Health Insurance	1,831	1,862	1,927	1,995	2,064	2,137
Chicago Teachers' Pension System	309	323	327	330	333	334
Government Services	1,537	1,506	1,539	1,572	1,606	1,640
8. Unspent Appropriations	**(645)**	**(1,145)**	**(1,186)**	**(1,227)**	**(1,268)**	**(1,315)**
Total Operating Budget	**34,602**	**35,428**	**36,769**	**38,148**	**39,569**	**41,027**
EXPENDITURES: PENSIONS						
K-12 Education Pensions	5,894	6,043	6,247	6,448	6,592	6,810
State Universities' Pensions	1,904	1,914	1,963	2,012	2,052	2,153
State Employees' Pensions	1,835	1,831	1,841	1,857	1,870	1,922
Total Pension Costs	**9,632**	**9,789**	**10,051**	**10,317**	**10,514**	**10,884**
EXPENDITURES: TRANSFERS OUT OF GENERAL FUNDS						
Statutory Transfers Out	405	411	418	426	433	441
Pension Stablization Fund Contribution	200	-	-	-	-	-
Property Tax Rebate Checks to Individuals	50	-	-	-	-	-
Grocery Tax Replacement to Local Governments	75	-	-	-	-	-
Debt Service	1,604	1,620	1,723	1,747	1,738	1,778
Total Transfers Out	**2,334**	**2,031**	**2,141**	**2,173**	**2,171**	**2,219**
TOTAL EXPENDITURES	**46,568**	**47,248**	**48,961**	**50,639**	**52,254**	**54,130**
General Funds Surplus/(Deficit)	3,551	357	(384)	(625)	(567)	(708)
Budget Stabilization Fund Contribution	**(312)**	**(78)**	**(80)**	**(82)**	**(83)**	**(84)**
Supplemental Appropriations Needed[2]	**(250)**					
Proposed Additional Budget Stabilization Fund Contributio	**(1,300)**					
Adjusted General Funds Surplus/(Deficit)	1,689	279	(464)	(707)	(650)	(792)

[1] Treasurer's Investment Borrowing, authorized by PA 100-1107, allows the State Treasurer to provide funds to assist with the state's accounts payable.

[2] Recommended supplemental appropriations to address appropriation shortfalls in FY2023.

Key to Agencies by Outcome

1. Education

PreK-12 Education

- Illinois State Board of Education

Higher Education

- Illinois Board of Higher Education
- Chicago State University
- Eastern Illinois University
- Governors State University
- Northeastern Illinois University
- Western Illinois University
- Illinois State University
- Northern Illinois University
- Southern Illinois University
- University of Illinois
- Illinois Community College Board
- Illinois Student Assistance Commission
- Illinois Mathematics and Science Academy
- State Universities Civil Service System

2. Economic Development

- Department of Agriculture
- Department of Commerce and Economic Opportunity
- Department of Labor
- Department of Transportation
- Illinois Commerce Commission
- Human Rights Commission
- Southwestern Illinois Development Authority

3. Public Safety

- Department of Corrections
- Department of Financial and Professional Regulation
- Department of Insurance
- Department of Military Affairs
- Department of State Police
- Environmental Protection Agency
- Illinois Criminal Justice Information Authority
- Illinois Workers' Compensation Commission
- Law Enforcement Training and Standards Board
- Prisoner Review Board
- Property Tax Appeal Board
- Illinois Emergency Management Agency
- Illinois Labor Relations Board
- Office of the State Fire Marshal

4. Human Services

- Department on Aging
- Department of Children and Family Services
- Department of Juvenile Justice
- Department of Employment Security
- Department of Human Rights
- Department of Human Services
- Department of Public Health
- Department of Veterans' Affairs
- Illinois Deaf and Hard of Hearing Commission
- Illinois Guardianship and Advocacy Commission
- Illinois Council on Developmental Disabilities

5. Healthcare

- Department of Healthcare and Family Services

6. Environment and Culture

- Department of Natural Resources
- Illinois Arts Council
- Abraham Lincoln Presidential Library and Museum

7. Government Services (including employees health insurance)

- General Assembly and Legislative Agencies
- Office of the Auditor General
- Supreme Court and Illinois Court System
- Supreme Court Historic Preservation Commission
- Courts Commission
- Judicial Inquiry Board
- Office of the State Appellate Defender
- Office of the State's Attorneys Appellate Prosecutor
- Court of Claims
- Office of the Governor
- Office of the Lieutenant Governor
- Office of the Attorney General
- Office of the Secretary of State
- Office of the State Comptroller
- Office of the State Treasurer
- State Board of Elections
- Department of Central Management Services
- Department of Innovation and Technology
- Department of Lottery
- Department of Revenue
- Governor's Office of Management and Budget
- Office of Executive Inspector General
- Executive Ethics Commission
- Capital Development Board
- Civil Service Commission
- Commission on Equity and Inclusion
- Procurement Policy Board
- Illinois Independent Tax Tribunal
- Illinois Gaming Board
- Illinois Racing Board
- Other Government Services*
- Chicago Teachers' Pension and Retirement System

8. Pensions

- Teachers' Retirement System
- State Universities' Retirement System
- General Assembly Retirement System
- Judges' Retirement System
- State Employees' Retirement System

* Includes contributions to the Teachers' Retirement Insurance Program, College Insurance Program, operational expenses of the State Employees' Retirement System, and any additional appropriation authority needed to address the shortfall in contributions to the system in prior years (approximately $33 million in fiscal year 2023).

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