

Texas Comptroller Susan Combs
2010-11 Biennial Revenue Estimate
Jan. 12, 2009

WELCOME

- Pursuant to my Constitutional duty under **Article III, Section 49a**, I am delivering my estimate of 2010-11 available revenue to the Legislature and Governor today.
- Let me begin with a brief overview.

General Revenue-related funds available for certification of 2010-11 General Purpose Appropriations: \$77.1 billion.

- Of note here is that the comparable number for the current — **2008-09** — biennium is **\$86.2 billion**. This new biennium estimate shows a **difference of \$9.1 billion; DOWN 10.5 percent**.

This difference is primarily due to:

- A lower **beginning** General Revenue balance, or surplus, that we have on hand to start a biennium.
- The **\$7 billion** decline in beginning balances — going from almost **\$9 billion** in September 2007 to about **\$2 billion** — relates back to some monies being used to fund the **2008-09** budget and setting aside **\$3 billion** to provide for future **school property tax relief**.
- Historically, the General Revenue balance — or “surplus” — **DOES** change. It is NOT always in the billions.
- For example, at the start of the **2004-05** biennium, this surplus figure was only **\$88 MILLION**.
- The other point I would like to make is that **revenue**, expected to be collected during **2010-11**, is slightly less than the comparable number for **2008-09**. This is due to a number of factors, most notably a slowing Texas economy which, in turn, is driving reduced tax receipts.
- For example, motor vehicle sales have **plunged** both nationally and here in Texas. The motor vehicle sales tax, normally a **\$3 billion** per year tax, **is expected to drop 21.9 percent in fiscal 2009** and, while it will come back somewhat, we don't expect it to regain its former size before the end of **2010-11**.
- Another factor influencing reduced **2010-11** revenues is the stock market. The market's decline has triggered a never-before-used Texas Constitutional provision stating that the Permanent School Fund may **not make** any distributions for school funding purposes until the Fund value improves. The current biennium will see **\$1.4 billion** transferred, but for **2010-11**, we are expecting no transfers from the Permanent School Fund. Any **REPLACEMENT** funding would therefore have to come from **General Revenue** or perhaps the **Rainy Day Fund**.

So, the **2010-11** Available Revenue of **\$77.1 billion** is derived from:

- **\$2.1 billion in 2008-09 ending General Revenue balance or “surplus”** and
- **\$75 billion in revenues.**
- **The NET NUMBER of \$77.1 billion is the available revenue** for the 2010-11 biennium.
- However, state revenue collections from all sources, including **\$91 billion** in federal receipts, should total **\$167.7 billion** for the coming biennium.

WHAT ABOUT THE ECONOMY?

- When I spoke to you about the Biennial Revenue Estimate two years ago, this was an important factor. Now it has assumed even more importance.
- The U.S. economy, which was hitting on all cylinders during the early and middle years of this decade, entered into recession in December 2007. Job losses thus far nationally are approximately **2.6 million**.
- Texas might have side-stepped a slight or moderate downturn in the national economy, but the effects of what may become the worst national recession in many decades will be too large to avoid. The state is not immune to the economic forces wreaking havoc in other sections of the country.
- Employment in Texas is expected to cool rapidly from its annual pace of adding **250,000 jobs**, which we saw in 2008, to LOSING jobs. Texas employment is expected to have PEAKED in the fourth quarter of calendar year 2008, then DECLINE until the third quarter of 2009. A projected **111,000 nonfarm jobs** are expected to be lost during this time. Beginning in the fourth quarter of 2009, it is expected job growth will resume.
- Consumer confidence numbers — while down sharply from the levels seen even a year ago across the nation and in Texas — would seem to bear out the general view that Texas will trail the nation, and Texans and residents of the Southwest generally are **more optimistic** today than the rest of the country, but somewhat **gloomier** six months to the future.

I really understand that people are worrying about the future, and that is reflected in reduced spending — but we still are innately optimistic in this state.

Several quick points about employment:

- Texas job growth has been gradually DECELERATING over the past six months or so. Where we were adding an average of more than **20,000 jobs** per month, we have already slowed to below **10,000** per month.
- We also historically track the U.S. employment, and we know that — for example — during the 1981-82 and 2001 U.S. recessions, Texas saw job losses also, but they started about six months behind the U.S.
- In fiscal 2011, as we recover, we would expect to revert to a pre-slowdown growth in employment of **20,000** per month. And by the way, we led the entire nation for a very long time in job growth, and we will again.

The housing **market, oil and gas prices and growth in consumer spending** have been prime contributors to tax collections. We see that slowing dramatically.

HOUSING SECTOR

- **The vibrant housing climate in Texas has turned down. The good news is that it hasn't turned down as badly as some other states.**
- Sales of **EXISTING** homes have declined by **16.2 percent** over the last year. And as sales cool, MLS listings are up. **New home starts have declined dramatically** — more than **30 percent** in last year — similar to U.S. trends.
- Unfortunately, **prices for existing homes** in Texas are also declining by about **5.4 percent**, which is moderate compared to **20–25 percent** price drops — such as those seen in California and Florida.
- With **new home prices**, however, although starts are down, prices have remained firm.

Foreclosures:

- Looking at the time up to the start of 2007, California, Florida and Texas all had about the same number of monthly foreclosures — about **10,000**. Then California's skyrocketed up to nearly **100,000 per month**, while ours remained steady.
- Nationally, as the housing market went bust, foreclosure activity skyrocketed, especially in those areas which had seen the hottest, most rapidly rising markets.
- Putting it another way, in November 2008, **one in every 1,176 Texas households faced a new foreclosure action. Contrast this with one in every 218 California households, one in every 173 Florida households and one in every 76 Nevada households.**
- **The great news for Texas is that most people have confidence they will keep their homes, and that is hugely important to them.**

OIL AND GAS SECTOR

- Oil and gas prices have been on a steady march upward since the early 2000s and spiked in the summer of 2008. Oil prices briefly reached **\$147 per barrel** before beginning a steep descent. Natural gas prices have generally followed a similar, if not quite as exaggerated, trend.
- **Oil** is now trading — and this changes appreciably day to day — in the **\$40-per-barrel** range, which is **about where the price was four years ago**. Expect to see oil in **mid-\$30s** in the spring and summer of this year and rising back to around **\$40 per barrel** by year's end.
- **Quick note here:** Unrest around the world and unique events — such as hurricanes in the Gulf — can and do move prices abruptly. What I'm giving you here is what I see as the overall trend in prices. The next year should see prices move slowly upward as national and global economies begin to recover.
- Natural gas is expected to follow a similar pattern. **And finally ...**

MAJOR REVENUES

I'd like to talk generally about one of the **state's larger revenue sources, sales tax.**

Sales Tax:

- Total 2010-11 sales tax collections, at **\$44.4 billion**, will comprise approximately **65 percent of all TAX revenue and 58 percent of total GR funds** — up somewhat in its percentage contribution than has been the case for the past several biennia.
- The fiscal 2010 rate of growth is estimated to be **0.5 percent**, accelerating to **4.2 percent** in 2011 as the economy swings into full recovery. Both rates are down considerably,

however, from fiscal 2006's **12 percent** growth, 2007's **10.9 percent**, or even fiscal 2008's **6.6 percent**.

- As I mentioned earlier, the same factors that drove the **high** growth rates of the past two years **are the same ones expected to cool off during 2010-11** — and all three impact the sales tax.
- I mentioned oil and gas and housing.
- Within retail trade, there is a great deal of variation, and this is where we see what **average Texans are experiencing in their daily lives**.
- General merchandise, such as department and discount stores, is interesting. This sector had excellent fiscal years in 2006 and 2007. Tax collections from general merchandise have held up, compared to **specialty stores**. In fiscal 2009, year-to-date, this sector's sales tax collections are **UP 5 percent over last year**. **This may be an indication that consumers have moved — at least for now — from some specialty retailers toward these general merchandise stores.**

Franchise Tax:

- Franchise tax is another important source of funding for the state's revenues. The first complete tax cycle has been completed for the revised franchise — or margin — tax.
- Fiscal 2008 collections — the first year of collecting the margin tax — were **\$4.5 billion**. This was well short of the expected **\$5.9 billion**, and after refunds — for this first cycle — it is **\$4.3 billion**.
- We expect, going forward, that the tax will generate approximately **\$4.4 billion in both fiscal 2009 and fiscal 2010**. These two years will also be negatively impacted by economic conditions. In fiscal 2011, the tax is expected to increase to **\$4.5 billion**.
- So, over the 2010-11 biennium, the tax is expected to generate a total of **\$8.9 billion** — to be split between two state funds. General Revenue retains roughly **60 percent** of net proceeds, and the Property Tax Relief Fund gets the rest.

Oil & Natural Gas Severance Tax Revenues:

- Natural gas production tax is expected to bring in approximately **\$3.3 billion** over the 2010-11 biennium. This is much lower compared to the 2008-09 biennium, which will produce revenues of **\$4.5 billion** because of higher prices.
- **Oil production taxes are expected to generate \$1.2 billion, versus \$2.2 billion** for the current biennium.
- Together, these severance taxes will raise **\$4.5 billion**.
- Of this revenue, **an estimated \$1.7 billion will be reserved constitutionally for transfer to the Rainy Day Fund**.

Rainy Day Fund:

- The Rainy Day Fund will contain, at the end of 2008-09, **an estimated \$6.7 billion**. It is, by far, the largest balance ever contained in the fund at the end of a budget period.
- Let me take just a moment to talk about the Rainy Day Fund. It came about more than 20 years ago, following an economic downturn in the state. Its primary method of funding is a required transfer of **three-fourths of oil and gas tax revenue ABOVE what was collected in 1987, which goes to the Rainy Day Fund**.

- So, in a general sense and disregarding variations in well output, the higher oil and gas prices are, the more dollars go into the Rainy Day Fund.
- Adding to the fund, over the course of 2010-11, will be two more of these transfers of oil and natural gas revenues. All told, the Rainy Day Fund would have approximately **\$9.1 billion** in its balance at the end of 2010-11, absent any appropriations that might be made by the 81st Legislature, which for spending requires a two-thirds vote.
- By way of history, from 1990 through 2008, money has been appropriated out of the fund in excess of **\$100 million** only **six** times.
- And I want to stress that the Rainy Day Fund is not a reliable source of additional funding for the state's needs.

The outlook I am releasing today, for both state revenue and the economic picture, is decidedly cautious. Fiscal 2009, and the first part of 2010 especially, are likely to underperform what we have become used to.

We do have the large Rainy Day Fund balance available as resource for the coming biennium. But oil and gas prices are volatile, and the Rainy Day Fund hasn't always been as large as it is now and may not be in the future.

I would urge lawmakers to continue their historic practice of careful budget deliberations, with special consideration toward making sure the decisions of today will fit within our means of funding them tomorrow.

Thank you.