EXECUTIVE SUMMARY

March 2021

The economy is emerging from a dark winter. The resurgent virus of a few months ago is in full retreat. The outlook brightens with every inoculation. The stage is set for stronger economic growth this year and next than the U.S. has experienced in decades, possibly generations. The combination of increased vaccinations, large and swift federal policy responses, and a more resilient underlying economy, results in a cycle unlike anything experienced before.

Most encouraging is that the amount of economic scarring to date in terms of business closures and permanent layoffs is much better than first feared. Total personal income is higher today than it was prior to the pandemic, despite Oregon having 160,000 fewer jobs. Households, particularly those in the middle and upper parts of the income distribution have built up considerable amounts of savings. As the pandemic continues to wane, pent-up demand will be unleashed, fueling growth in the months ahead. The shift in spending out of physical goods and back into labor-intensive, in-person consumer services will raise employment significantly. While the labor market remains in a deep hole today, a bit more than half of these lost jobs will be regained this year. The rest will be regained next year. Oregon’s economy will return to full employment by early 2023, or 6-9 months sooner than expected in previous forecasts.

Although many are suffering, aggregate income has risen sharply during the recession. As an income tax state, Oregon’s primary revenue instruments have followed suit. The General Fund revenue outlook has brightened accordingly. Immediately following the start of the pandemic, the revenue outlook was revised down by around $2 billion. As of the current forecast, this hole has completely been filled. The new outlook calls for a bit more revenue than was expected before the recession began.

Many factors are playing into the unexpectedly strong revenue collections, but two reasons stand out in particular. First, the unprecedented amount of federal aid has translated into around $1.5 billion in additional Oregon tax liability. Second, unlike previous recessions, asset markets have continued to gain value and corporate income has held steady.

Healthy revenue collections together with the strengthening economic outlook have put Oregon’s unique kicker law into play. Following a booming first half of the biennium, Oregon’s General Fund revenue outlook was inches away from the 2% kicker threshold when the pandemic hit. After filling all of the recessionary hole, the March 2021 forecast calls for collections to exceed the threshold by $170 million (0.9%), resulting in a kicker credit of $571 million. However, this kicker credit is far from a sure thing. With one more tax season left in the biennium, much uncertainty remains. During peak tax season, the Department of Revenue has processed more than $170 million of tax payments in a single day. Given the variance seen during our office’s 40 year forecasting record, there is currently a two-in-three chance that a kicker will be triggered when the biennium ends.

Although the additional revenue called for in the March 2021 outlook is a welcome sight, budget writers still face a challenging environment this session. Although personal income taxes have continued to grow this biennium, many other revenue sources such as Lottery sales have not. While better than past recessions, overall revenue growth remains quite modest from an historical perspective. With both federal aid and asset booms expected to expire, revenue growth will remain modest during the 2021-23 budget period. Should this baseline outlook come to pass, state resources will have remained roughly unchanged for three consecutive budgets. This growth is not sufficient to keep up with rising need for, and the cost of, providing public services.