

# **Budget Environment**

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# Budget Environment

## Expenditure Drivers

### Inflation

The rate of inflation is expected to remain moderate through the 2005-07 biennium.

- As measured by the U.S. Consumer Price Index (CPI), inflation is projected to increase slightly from current levels. FY 2007 will see a 1.7 percent increase.
- The GDP implicit price deflator is forecast to grow moderately and stay below the 2 percent range through FY 2007.
- Medical service inflation is projected to be slightly above the 2003-05 biennium. Medical CPI will rise more than 3 percent in both FY 2006 and FY 2007.

FY	CPI	Medical Deflator	GDP Deflator
2004	1.8%	3.1%	1.4%
2005	1.3%	3.3%	1.3%
2006	1.4%	3.2%	1.5%
2007	1.7%	3.5%	1.9%

### Demographics

- Population growth is the major state government budget driver. Policies and alternative opportunities, however, often modify the direct impact of the population change on the state budget allocation. Demands for public resources as well as a state's economic health depend upon the size, composition, structure, and characteristics of its population.
- Census 2000 enumerated 3,421,399 persons in Oregon on April 1, 2000. This is an increase of 579,000, or 20.4 percent, since the 1990 Census count. Oregon's population is expected to reach 3.7 million by the year 2007, adding an average of 42,400 persons annually between 2005 and 2007.
- Although growth has slowed down in recent years, Oregon's population growth rate for the period of 1990 to 2000 was eleventh fastest in the nation. However, population growth rates in all of our neighboring states (except California) exceeded that of Oregon during this period. Therefore, high rates of population growth have been a regional characteristic.
- Nearly 73 percent of the 1990-2000 population growth was due to net migration, where the number of in-migrants exceeds the out-migrants. Oregon's growing economy during the 90's coupled with the shortage of workers, especially in hi-tech sector, attracted job seekers from other states and around the world. Net migration averaged 42,000 annually during the 90's. However, net migration during 2005-2007 is expected to average nearly 26,000 annually due to the slow but recovering economy and existing pool of unemployed workers and adults not currently in the labor force. The size and composition of Oregon's future population depends upon the nature of our economy.
- With the high volume of in-migration, the racial and ethnic composition of Oregon's population is becoming increasingly diverse. Asian and Black racial groups and the Hispanic ethnic group have grown very rapidly in recent years. The minority population (non-White, or reporting two or more

Race/Ethnicity	Number	Percent
<b>Total population</b>	<b>3,421,399</b>	<b>100.0%</b>
One race	3,316,654	96.9%
White	2,961,623	86.6%
Black or African American	55,662	1.6%
American Indian and Alaska Native	45,211	1.3%
Asian	101,350	3.0%
Native Hawaiian and Other Pacific Islander	7,976	0.2%
Some other race	144,832	4.2%
Two or more races	104,745	3.1%
Hispanic or Latino (any race)	275,314	8.0%

Source: U.S. Bureau of the Census, 2000 Census

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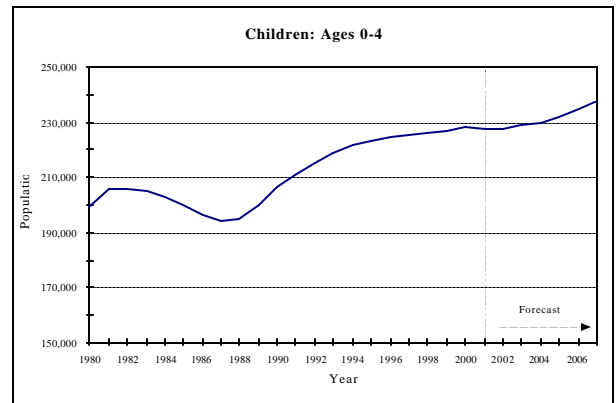
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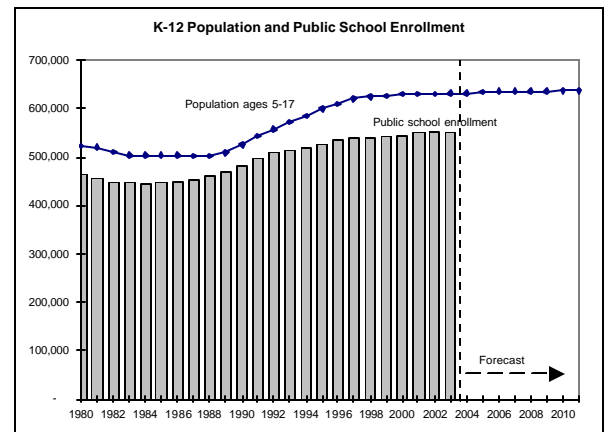
ances) in Oregon was 460,000 persons in 2000, accounting for 13.4 percent of the total population.

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- The age structure of the population has significant budgetary implications. For example, the numbers and shares of pre-school and school-age children, college-age adults, criminally “at-risk” adults, those applying for welfare, and the senior population needing public assistance pose critical budgetary choices for policy makers.
- Oregon had 223,000 children aged 0-4 in the 2000 Census. This group is expected to increase by 4,400 between the years 2005 and 2007. The slow or even negative rate of growth of 0-4 year olds is past. This group will resume an increasingly higher rate of growth and exceed Oregon’s overall growth rate starting from 2006. Between 2005 and 2007, the number of children under age 5 will increase at an annual rate of 0.9 percent. The size and growth of this population will have an impact on the demands for childcare and children’s services.



- The number of persons aged 5-17 determines the K-12 enrollment to a large extent. The population aged 5-17 constitutes 18 percent of Oregon’s total population. Total K-12 enrollments account for 98 percent of this school-age population. Nearly 91.3 percent of all K-12 students are enrolled in Oregon’s public schools. The remainder are enrolled in private schools (5.8 percent), 2.3 percent are in home schooling, and 0.4 percent in charter schools. In times of economic downturn, publicly funded schools seem to bear a greater burden as the share of students in private schools declines.

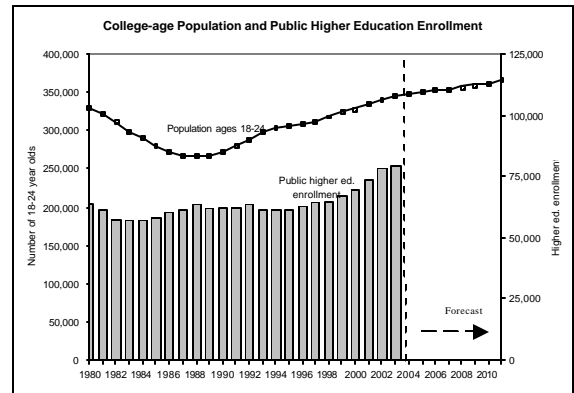


The school-age population has grown from 523,000 in the 1990 Census to 624,000 in the 2000 Census. This amounts to an average increase of over 10,000 persons per year. The first half of the 1990’s saw a very rapid growth in this population. With an average growth of nearly 15,000 persons of ages 15-17 during the first half of 1990’s, Oregon’s school system faced enormous pressure. The rate of increase has slowed down considerably since then and is expected to remain well below the overall population growth rate in the near future. Between 2005 and 2007, the annual growth of this population group will average about 700. As an effect of high migration from other countries, nearly 2.4 percent of school-age children do not speak English well or do not speak English at all. As the overall population has become more racially and culturally diverse, so has the student population. The proportion of minority students has increased from 11.2 percent in 1990 to 21.5 percent in 2002.

- Young adults aged 18-24 are generally referred to as the college-age population. Reversing a long, declining trend of the 1980s, the young adult population has grown to 328,000 in 2000. The growth rate has accelerated in the recent years. However, the rate is expected to slow down and lag behind the state’s overall growth as people age out of this cohort.

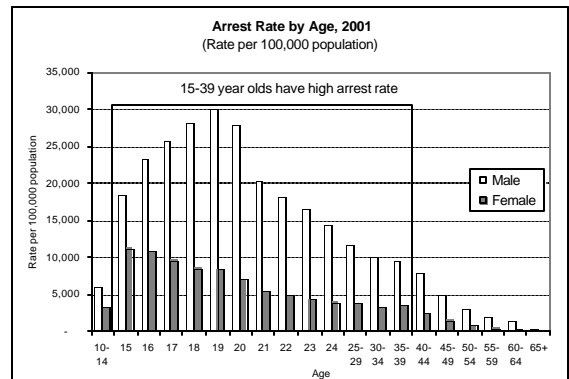
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Nearly 79 percent of all undergraduate students in Oregon's public colleges and universities are 18-24 years old. Growth in the young adult population is likely to increase demand for higher education and community colleges, work training programs, and entry-level jobs. Actual enrollment in public higher education also depends upon competing employment and educational opportunities. Consequently, despite a long period of rapid growth in the young adult population, only recently has the higher education enrollment growth rate outpaced the young adult population growth rate.

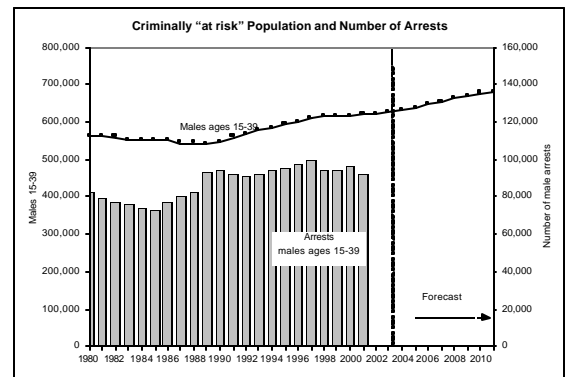


- Males aged 15-39 are considered criminally at-risk because the majority of arrests and convictions have historically been associated with this age-sex group. For example, nearly three-fourths of all arrests are of ages 15-39 and three-fourths of them are males.

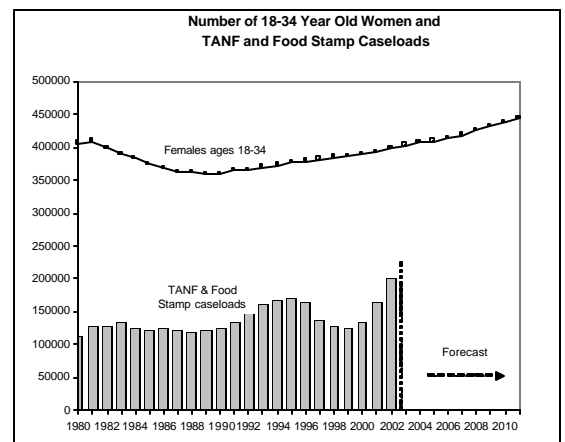
After a net decline during the early 1980's, this population has grown steadily since 1990, but at a much slower pace than overall population growth rate. However, the growth of this population group will be slightly higher than the overall population growth. This population is expected to grow by an average of 8,000 persons each year between 2005 and 2007. Growth in this at-risk population, along with tougher sentencing policies, will increase the pressure on law enforcement and the prison population.



- Income and health assistance caseloads in the Oregon Department of Human Services are affected by demographics. However, demographics provide only general trends of the population groups to be served. Actual numbers of caseloads are greatly determined by welfare-related policies.



The majority of welfare recipient households are headed by women ages 18-34. Female headed households with children tend to have one of the highest poverty rates in the state. Two major welfare programs are Temporary Assistance for Needy Families (TANF, previously AFDC) and Food Stamps. The first half of the 1990's was a period of rapid growth in these caseloads, far exceeding population growth. This period of rapid growth was followed by a rapid decline in the caseloads. In the coming years, the number of 18-34 year old women will grow nearly as fast as the overall population.



- The senior population age 65 and older accounts for nearly 13 percent of the total population. Between the 1990 and 2000 Census, the number of senior population grew

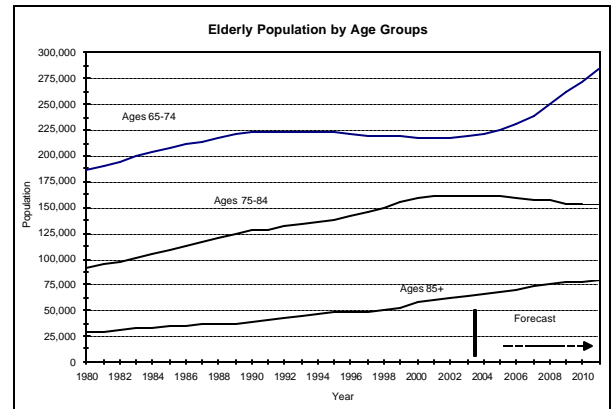
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from 391,324 to 438,177. This population has been growing at a slower pace than the overall population. However, this population group is expected to pick up steam and grow at a faster pace than the overall population.

- The number of youngest senior (aged 65-74) declined by 6,000 during the 1990's. Growth has been positive since the year 2001 and will accelerate in the future. The number of youngest senior will increase by nearly 14,000, or 6.2 percent, between the years 2005 and 2007.
- The senior population aged 75-84 has been growing much faster than the state's overall population growth rate. The number of 75-84 year olds grew from 128,071 to 161,404 between the last two censuses – an increase of 26 percent. However, despite the continued net immigration senior population, this group of seniors is expected to decline in number in the near future. Between 2005 and 2007, this group of seniors will decline by nearly 1.8 percent.
- The oldest senior population group, aged 85 and over, is small but growing very rapidly. The number of oldest senior grew from 38,815 to 57,431 between the 1990 and 2000 Censuses - an increase of 48 percent. The fast paced growth exceeding 3 percent per year will continue in the future. Between 2005 and 2007, this group of seniors will increase by 7.3 percent. Differential birth cohorts, increasing life expectancy, and continued net immigration of seniors are responsible for the accelerated growth in the oldest senior population. Many members of the senior population require health care, pension support, and special housing. They are highly dependent on state long-term care services.



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### Inmate Population

- Oregon's prison population is forecast to grow by 37 percent in the next decade. The table below shows the forecast population over the next decade with the percent change from the July 1, 2003 population. About 44 percent of this growth is directly or indirectly due to the passage of Ballot Measure 11, which mandates lengthy minimum sentences for certain violent felonies.

The prison population forecast is based on current law and interpretation of current policy. Statutory, constitutional, and criminal justice policy changes pose the most important risks to the forecast. These include changes in the law brought about by the initiative or legislative processes or cuts in criminal justice services due to budget reductions.

- In the absence of major legal or policy changes, prison intakes depend in part upon the number of arrests for serious offenses. Arrests for violent crime have been fairly stable in recent years. However, arrests for property and drug crimes have increased. These increases can put more pressure on the courts, prison, and community justice systems.

### Inmate Population Forecast

Year	July 1 Population	Cumulative Pct Change from 2003
2003	12,003	
2004	12,852	7.1%
2005	13,178	9.8%
2006	13,657	13.8%
2007	14,140	17.8%
2008	14,625	21.8%
2009	15,094	25.7%
2010	15,520	29.3%
2011	15,888	32.4%
2012	16,183	34.8%
2013	16,481	37.3%

### The Economy

#### National

- The consensus national forecast calls for the start of sustained economic growth. The job-less recovery will turn to a job-gaining recovery, building strength into 2004. Inflation and interest rates should stay relatively low which will help the recovery process. Global markets should also revive along with the U.S. economy.
- Unemployment will slowly decline through 2004.
- Business investment in equipment and software will remain strong through 2004. The housing market will see declines in 2004 from its historical highs of 2003.

#### Oregon

- The recession hit Oregon's economy harder compared to any other state. The year 2003 will close out as the third consecutive year of job losses. Oregon had the highest unemployment rate in the nation for the past two years. Recent growth of the national economy and brighter prospects for trading partners should start to add jobs in Oregon going into 2004 and 2005.
- Personal income is forecast to grow 5.7 percent in FY 2006 and 6.0 percent in FY 2007. This is slightly stronger than the projected growth of 4.5 percent in FY 2005. Employment growth is projected at 2.2 percent growth in FY 2006 and 2.0 percent growth in FY 2007. This continues the moderate growth of 2.2 percent projected in FY 2005.

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- In the near future, several forces will be at work to affect the Oregon economy. The Oregon economy will improve with the U.S. economy, but the recovery will be slow and not reach above 2.0 percent growth until mid 2004. The high technology sector will slowly recover but not reach its pre-recession peak level of employment as the 2005-2007 biennium comes to a close.

### Revenue

#### General Fund/Lottery

- Based on the March 2004 forecast, General Fund revenues are projected to grow 11.5 percent during 2005-2007, to \$11,240.4 million. Slow economic recovery in Oregon, as well as low inflation, account for the modest growth. The projected beginning balance as of the March 2004 forecast is \$20.7 million.
- Lottery resources are expected to be \$730.3 million for the 2005-2007 biennium. As of March 2004, Lottery is still evaluating means to increase sales per House Bill 3159.

#### Tobacco/Health Plan

- Cigarette and Other Tobacco taxes dedicated to the General Fund are forecast to total \$114.6 million in the 2005-2007 biennium.
- Cigarette and Other Tobacco taxes dedicated to the Oregon Health Plan are forecast to total \$374.9 million for the 2005-2007 biennium. An additional \$16.2 million in tobacco taxes will be available to fund the Tobacco Use Reduction Account.
- The greatest risk to tobacco taxes is a large increase in the wholesale price or the federal excise tax, which would decrease consumption and in turn could decrease cigarette tax revenues to the state. The Consumer Price Index for tobacco products, a proxy for the combined impact of price and tax effects, increased 97 percent between 1996 and 2002.

### Risks

#### National/International

The forecast is dependent on recovery in world markets, mainly Asian, and continued strength of domestic demand. The Oregon economy faces some of the same risks, as does the U.S. economy. If a “typical” recession occurs in 2005-2007 biennium, General Fund revenues would be reduced by about 5.6 percent, or \$664 million, from the current forecast.

- Asia, Japan in particular, is projected to recover from the world downturn with stronger growth. The declining US dollar will assist exports. Global market growth is key to the health of high technology, lumber and wood products, and agriculture.
- Consumer spending is a driving force of economic growth. Throughout the recession, the consumer continued to spend due to tax cuts and low interest rates. The recovery underway could be stalled if the consumer pulls back on spending and financial investment in businesses. Geopolitical risks have the potential to weigh on the

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confidence of consumers and thus lower their spending. Rising interest rates will slow refinancing of mortgages and lessen the use of home equity to boost consumption.

- Federal government policy. Changes in federal budget policy, either through federal programs or changes in the federal income tax base, could potentially cause significant changes in Oregon's fiscal environment.

### State Specific

Oregon faces some additional state specific risks over the next biennium.

- Recovery in the semiconductor industry: Increasing demand for computers and communications equipment, and a related increase in orders, will eliminate the excess capacity in the industry. The needs of the Internet should fuel greater demand. This will be countered by firms seeking the lowest-cost production locations and continued offshore outsourcing of production. If this sector does not rebound, the state will see very low job gains, lowered in-migration, and lowered tax revenues.
- Export growth and rising commodity prices: Global recovery of economies will increase demand for Oregon finished goods and commodities. Oregon is well positioned for trade with Asian countries. Rising commodity prices will benefit agricultural and timber producers in the state. These sectors will continue to suffer if global economies do not recover.
- Voter initiatives. Voter initiatives have had a tremendous impact on state budget policy throughout the 1990's, with likely continuance in this decade. These initiatives can take the form of expenditure mandates or reductions in the state's ability to raise revenue.