ANALYSIS OF THE NEW JERSEY

FISCAL YEAR 2003 - 2004 BUDGET

TAX AND REVENUE OUTLOOK

PREPARED BY

OFFICE OF LEGISLATIVE SERVICES

NEW JERSEY LEGISLATURE

APRIL 2003

NEW JERSEY STATE LEGISLATURE

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THE FY 2003 AND FY 2004 TAX AND REVENUE OUTLOOK

Introduction

This report has been prepared by the Office of Legislative Services (OLS) to assist the Senate Budget and Appropriations Committee and the Assembly Budget Committee as they develop the FY 2004 appropriations act. The OLS revenue estimates reflect a careful review of current State revenue collections, historical revenue collection patterns, and a variety of economic data and forecasts.

While the *OLS Tax and Revenue Outlook* focuses on FY 2003 and FY 2004 revenues, the factors that caused the revenue crisis in FY 2002 have cast a long shadow over the current, proposed, and future budgets. The State has become particularly dependent on substantial temporary revenues, most prominently the securitization of the future proceeds of the Tobacco Settlement Fund. Within this context, our report reflects the following:

? For FY 2003, the OLS's revenue estimates are $81 million above the Executive budget estimates (page 4).

? For FY 2004, the OLS's revenue estimates are $321 million below the Executive budget estimates (page 5).

? Over both fiscal years, the OLS's revenue estimates are a total of $240 million lower than the Executive budget estimates.

? Each fiscal year is supported by at least $2 billion in temporary revenues, including Tobacco Settlement amounts of over $1.7 billion in FY 2003 and over $1.4 billion in FY 2004.

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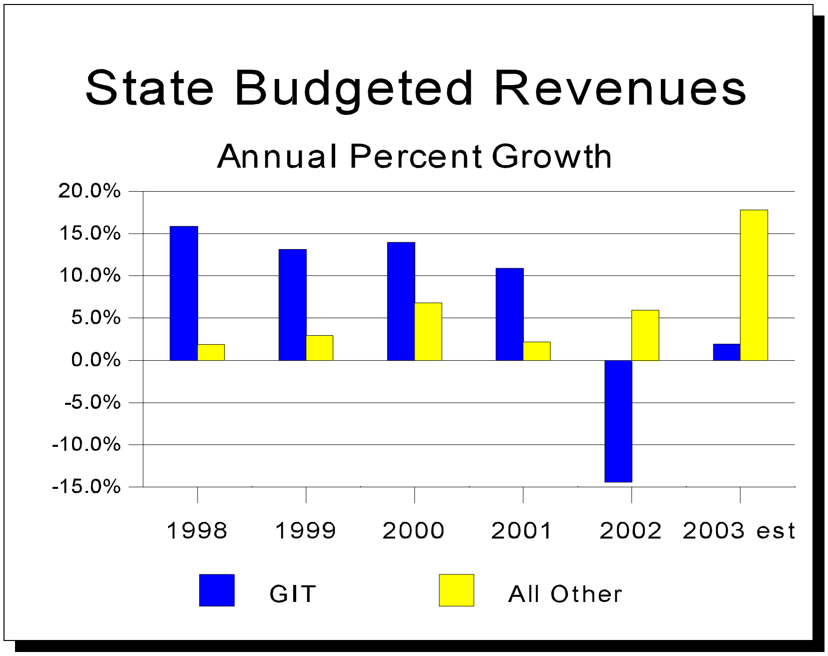
Recap: FY 2003 Collections to Date

Figure 1



Revenue collection patterns have undergone a significant shift in the last two fiscal years. During much of the 1990's, the gross income tax accounted for about two-thirds of annual revenue growth. The dramatic decline in gross income tax (GIT) revenues since the peak in FY 2001 has forced the State to seek growth from other forms of revenue.

Figure 1 displays recent annual State tax revenue growth rates for the gross income tax compared with all other State budgeted revenues. In FY 2002 and under the Executive's FY 2003 estimates, the prior revenue growth pattern has been inverted:

? Annual GIT growth averaged over 13.0% from FY 1998 to FY 2001, but plummeted by an unprecedented 14.4% in FY 2002. The Executive is now estimating a modest 1.9% increase in FY 2003.

? Growth in all other revenues has generally been more moderate and steady, ranging between 1% and 7% from FY 1998 to FY 2002. However, the Executive is anticipating 18% growth in all other revenues in FY 2003. Most of this growth is attributable to two actions (corporation tax increases and the receipt of funds from the sale of tobacco bonds) undertaken to bolster State resources.

Figure 2 contains a more detailed display of current FY 2003 revenue collections through the end of February. Key points include:

? GIT collections are declining by 1.3% compared to last year, rather than the slight growth of 1.9% anticipated by the Treasury as a year-end target.

? Sales tax collections are running only a fraction ahead of last year's levels.

? Corporation business taxes are running about 90% ahead of last year's levels, a rate higher than that anticipated for the full year by the Treasury.

Recap: FY 2003 Collections to Date

Figure 2
FY 2003 Year-To-Date
Selected Revenue Comparison
Through the End of February 2003 vs. February 2002

($ millions)

Revenue Source	FY 2002 Actual Year-To-Date	FY 2003 Actual Year-To-Date	FY 2003 Actual Year-To-Date % Change	FY 2003 Year-End Treasury % Change Target
Gross Income Tax	$4,072.7	$4,019.3	(1.3)%	1.9%
Sales Tax *	3,451.9	3,480.7	0.8%	0.1%
Corporation Business Tax	496.7	937.7	88.8%	68.6%
Lottery	457.5	480.1	4.9%	3.8%
Motor Fuels *	307.3	305.0	(0.7)%	1.2%
Motor Vehicle Fees	242.9	277.1	14.1%	9.0%
Casino	229.5	227.3	(1.0)%	2.0%
Inheritance Taxes	349.4	290.4	(16.9)%	(17.7)%
Insurance Premiums	113.1	115.0	1.7%	0.6%
Cigarette (Budgeted)	97.1	254.1	161.7%	88.8%
*Cigarette (Total)***	*252.1*	*409.1*	62.3%	*53.6%*
Petroleum Products *	129.7	127.2	(1.9)%	(2.1)%
Alcohol Excise *	45.3	44.6	(1.5)%	0.9%
CBT -- Banks & Financials	27.9	53.8	92.8%	89.7%
Realty Transfer *	51.3	68.5	33.5%	22.2%

Sources: Year-To-Date revenues are from Treasury's monthly cash reports. The year-end Treasury percentage change target is based on the February revised revenue estimates for FY 2003 contained in the proposed FY 2004 budget.
** Revenues represent seven months of cash collections. All others represent eight months of cash collections.*
*** Cigarette (Total) includes $155 million deposited directly into the off-budget Health Care Subsidy Fund in both FY 2002 and FY 2003.*

Fiscal Year 2003 Revenue Estimates

Figure 3 presents the FY 2003 revenue certification from the Appropriations Act (July 2002), the Executive's February revisions, and the OLS's forecast as contained in this report.

Figure 3
Fiscal Year 2003 Revenue Estimates
($ millions)

	Approp. Act (7/1/02)	Revised Executive (Feb.)	Executive Changes	Office of Legislative Services (March)	Difference OLS vs. Revised Executive
Gross Income Tax	$7,298	$6,966	($332)	$6,840	($126)
Sales Tax	6,172	6,000	(172)	6,000	0
Corporation Business Tax	1,830	1,987	158	2,137	150
Tobacco Settlement Fund	1,352	1,769	417	1,769	0
Other Revenues*	6,763	6,456	(307)	6,513	57
Grand Total, All Funds	$23,414	$23,178	($236)	$23,258	$81

See Appendix for additional detail. Numbers may not add due to rounding.
** The reduction in other revenues includes a $143 million transfer of certain motor vehicle fee revenues to an off-budget account.*

FY 2003 Executive:

? In February the Executive revised estimates for all revenues downward by a net $236 million from the level certified in the FY 2003 Appropriations Act.

? The estimates include $811 million in downward adjustments for various revenues including the gross income tax (down $332 million), the sales tax (down $172 million), and other revenues (down $307 million).

? The estimates include a $158 million upward adjustment to the corporation business tax.

? The estimates also include $417 million that draws down the remainder of the funds from the 2002 sale of tobacco securitization bonds.

FY 2003 Office of Legislative Services:

? The OLS's revenue estimates are $81 million above the Executive's total.

? The OLS's estimates are $126 million lower for the gross income tax, but $57 million higher for "Other Revenues", primarily the cigarette tax.

? The OLS's estimate for the corporation business tax is $150 million greater than the Executive's estimate.

? The OLS notes the use of additional tobacco funds will require legislation.

Fiscal Year 2004 Revenue Estimates

Figure 4 presents the Executive's FY 2004 revenue estimates and the OLS's forecast as contained in this report.

Figure 4
Fiscal Year 2004 Revenue Estimates
($ millions)

	Executive	% Change 03 to 04	Office of Legislative Services	% Change 03 to 04	Difference OLS vs. Exec.
Gross Income Tax	$7,494	7.6%	$7,280	6.4%	($214)
Sales Tax	6,334	5.6%	6,255	4.3%	(79)
Corporation Business Tax	1,823	(8.3)%	1,770	(17.2)%	(53)
Tobacco Settlement Fund	1,448	(18.1)%	1,383	(21.8)%	(65)
Other Revenues	6,755	4.6%	6,844	5.1%	90
Grand Total, All Funds	$23,853	2.9%	$23,532	1.2%	($321)

See Appendix for additional detail. Numbers may not add due to rounding.

FY 2004 Executive:

? The Executive expects total revenues to grow by $676 million, or 2.9% over FY 2003.

? Tobacco Settlement Fund revenue estimate assumes the securitization of the remaining portion of the State's projected future revenues.

? The Executive's total revenues include a number of proposed tax increases totaling an estimated $446 million (see discussion on page 13).

FY 2004 Office of Legislative Services:

? **The OLS's revenue estimates are $321 million below the Executive's total.**

? The OLS's estimate reflects recent information that the tobacco securitization sale netted $65 million less than anticipated.

? The OLS assumes the realization of the Executive's proposals for comparability purposes. The legislation for these proposals has not yet been made public.

Budgetary Impact of the OLS Revenue Estimates

The OLS estimates FY 2003 revenues will be $81 million *above* the Executive estimates, while FY 2004 revenues will be $321 million *below* the Executive estimates. Combined over the two year period, the OLS estimates a net $240 million less than the Executive.

As part of its analysis, the OLS typically recalculates the State's year-end budgeted balance based solely on the revenue forecast difference between the Executive and the OLS. Figure 5 assumes that the spending plan and tax law changes in the FY 2004 Executive budget will be followed. However, any calculation of the actual balance must take into account numerous spending decisions as well as anticipated revenue. Decisions on these and other matters will be made by the Executive, both budget committees and the full Legislature over the next two months.

Figure 5
OLS Adjusted FY 2004
Year-End Balance

Executive Estimate	$253,000,000
OLS Revenue Adjustment	($240,000,000)
OLS Estimate	$13,000,000

As is shown in Figure 5, the Executive estimates an FY 2004 year-end balance of $253 million. All other things being equal, the lower OLS revenue estimates would produce a year-end balance of $13 million, $240 million less than the Executive.

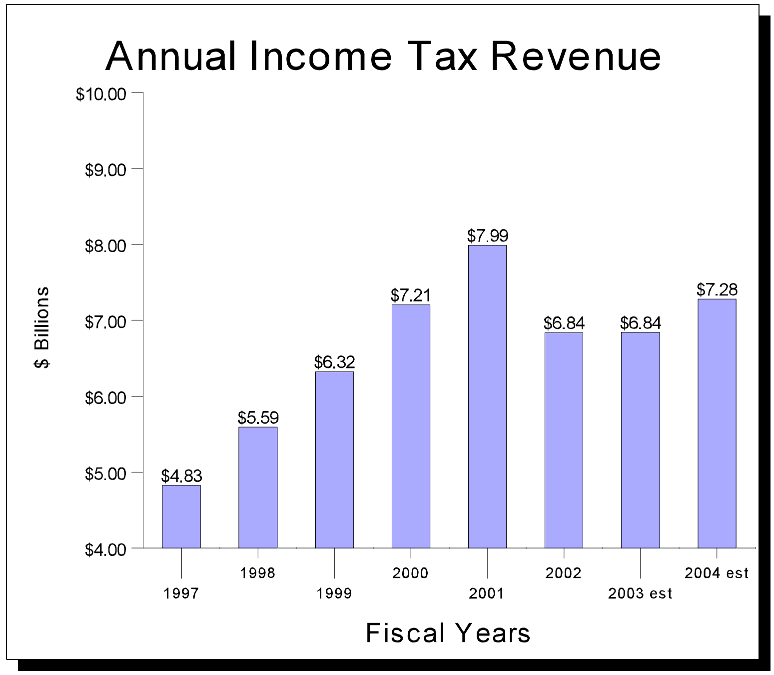
Because this analysis does not address possible changes to appropriations, Executive spending patterns, the Executive's proposed revenues changes, or other non-tax revenues, it is premature to draw conclusions about actual year-end balances from this analysis of State revenues.

Projections of the State's year-end balance are a static image of a moving target. Because of the large number of changes that occur in both spending and revenues throughout any fiscal year, the surplus changes significantly between the enactment of the annual appropriations act and the end of the fiscal year and a review by State auditors. Historically, spending is adjusted and new revenue measures are instituted during the fiscal year when such actions are necessary to maintain a balance.

Gross Income Tax

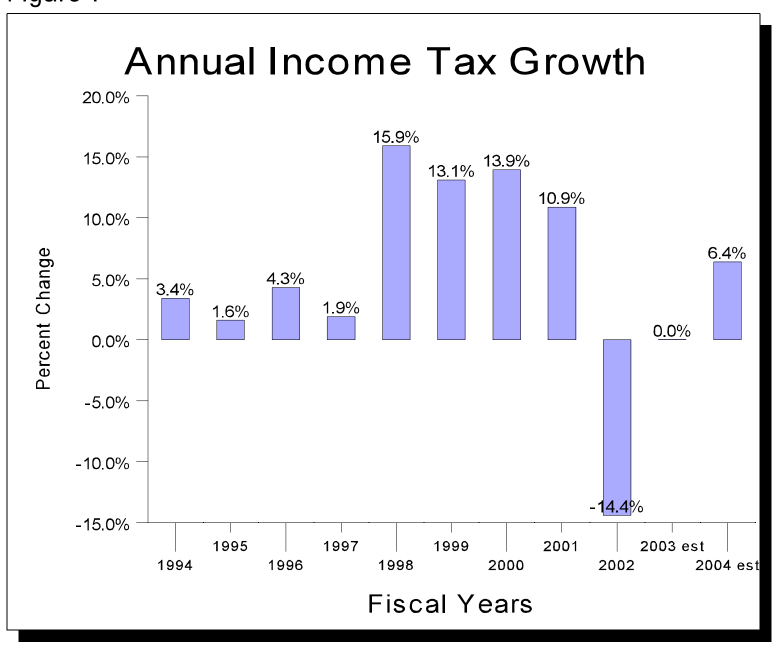
Although gross income tax (GIT) revenues tumbled precipitously in FY 2002, this tax remains the State's most important tax revenue source, accounting for over 30% of budgeted revenues. When the GIT does well, as it did between FY 1998 and FY 2001 when it accounted for over two-thirds of total revenue growth, budgeted revenues do well. But when the GIT bubble bursts, as it did in unprecedented fashion in FY 2002 (see Figures 6 and 7), the entire budget is deflated.

Figure 6



The causes of last year's sudden 14% drop in GIT revenues have been discussed in great detail in prior editions of the *Tax and Revenue Outlook* and other reports. The story has become familiar:

Figure 7



? The GIT is particularly dependent on high-income earners, as those taxpayers with income over $100,000 contribute close to 80% of GIT liabilities.

? High-income taxpayers receive significant income from volatile non-wage sources such as capital gains, stock options, and partnership/business income.

? All major stock market indices have been tumbling for three years. The NASDAQ, since its peak on March 10, 2000, has fallen 75%.

? Massive capital gains that had accumulated during the stock market run-up, have now been either realized or eliminated by the markets' fall.

The same forces that fueled the income tax's robust growth in the late 1990's have now had a similarly powerful impact in reverse. Recovery for the GIT, and the State budget, may be years away.

Gross Income Tax (Continued)

GIT Components

In analyzing the GIT, it is helpful to break up the revenue stream into four basic components:

1. Withholding collections are paid throughout the year by employees through their employers as a deduction from each paycheck, bonuses and some stock options;
2. Estimated payments generally are paid in the months of September, January, April, and June by taxpayers with significant non-wage income;
3. Final year-end payments are the familiar payments made by April 15th each tax filing season. As with estimated payments, taxpayers who must make large final tax payments generally have significant sources of non-wage income;
4. Refund payments are paid by the State, largely in the spring and summer, to taxpayers whose April 15 tax filings show payments exceeding their tax liability.

FY 2003

Neither the Executive nor the OLS anticipate that FY 2002's sharp GIT decline will continue in FY 2003. The Executive estimates $6.966 billion, or 1.9% growth over FY 2002. The OLS estimates essentially flat revenues of $6.840 billion.

The $126 million difference between the OLS and the Executive is relatively small and does not reflect a different view of the economy. The OLS estimate is based primarily on current trends for the major components of the GIT -- withholding, estimated payments, final year-end payments, and refund payments.

Withholding Collections: The largest component of income tax collections is from *employer withholding*. Withholding receipts are up 2.6% so far in FY 2003. The OLS believes this growth will continue and improve slightly to 3% growth for the rest of FY 2003.

Estimated Payments: Estimated tax payments fell 25% in FY 2002. That sharp decline has moderated somewhat in FY 2003, but estimated payments are still down 8% from last year's levels. This suggests declining non-wage income and signals likely weakness in final year-end payments due in April. The OLS believes estimated payments will decline by about 5% for the rest of the fiscal year.

Final Year-End Payments: Paralleling the fall in estimated payments, final year-end payments tumbled 23% in FY 2002. The bulk of these payments come in during April and May. The OLS believes final payments will decline about 5% from last year's levels. In June the State should also see payment declines from the enhanced levels seen during last year's tax amnesty program.

Refund Payments: On the heels of the sharp declines in income tax payments in FY 2002, refund payments jumped by 22%. The OLS believes that last year's historically high refund amounts should level off. The OLS is estimating flat refund payments with last year.

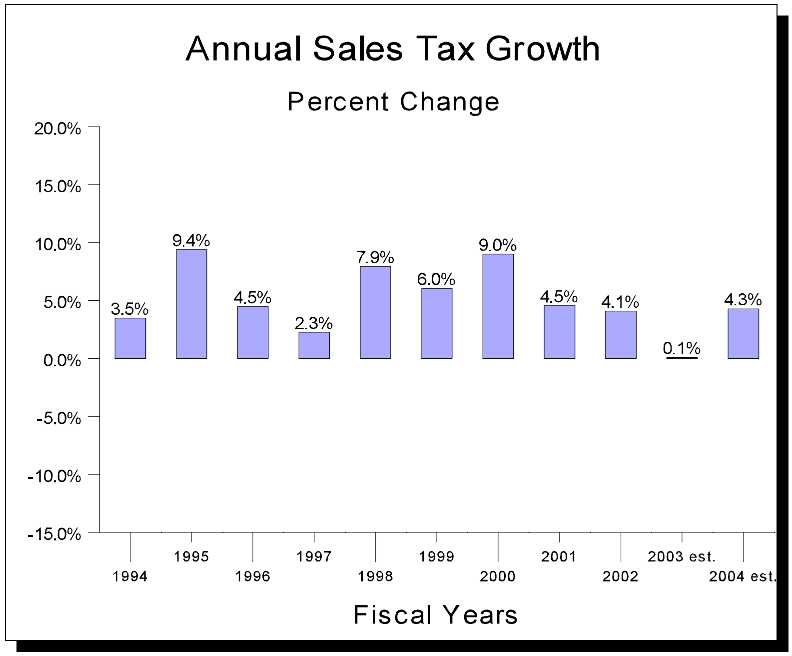
FY 2004

The Executive is estimating $7.494 billion in GIT revenue for FY 2004, an increase of 7.6% over FY 2003. The OLS is estimating $7.280 billion, or 6.4% growth over a lower FY 2003 base amount. The OLS's amount is $214 million less than the Executive's amount.

The OLS anticipates modest growth for the major components of withholding, estimated payments and final year-end payments, generally in the 4% to 5% range. In addition, the OLS estimates further reductions in refund payments of about 5%, which helps push net revenue growth up to 6.4%.

Sales Tax

Figure 8



The Sales tax is the second largest source of revenues supporting the State budget, accounting for over one quarter of total revenue. Through much of the last decade the sales tax has produced fairly reliable growth each year, ranging between 2.3% and 9.4% and averaging about 5.7% per year.

Due to the mild recession that began in the Spring of 2001, sales tax revenue growth moderated to 4.1% in FY 2002. Indeed, after adjusting for $81 million in net tax amnesty receipts, sales tax collections grew by only 2.7% last year. Collections in FY 2003 have slowed further and both the Executive and the OLS expect sales tax growth in FY 2003 to remain essentially flat with the prior year, while resuming modest growth in FY 2004.

FY 2003

Sales tax collections through the end of February are running only 0.8% ahead of the same period one year ago. Although home sales and auto sales remain high by historical standards, auto sales are down from last year's high levels. Consumer confidence measures have been sliding for months, reaching levels not seen since the Fall of 1993. It is widely believed that geopolitical concerns have dampened spending behavior. The Executive and the OLS agree that prospects for the remainder of FY 2003 are weak. Current trends and technical adjustments for last June's tax amnesty collections suggest that collections this year will finish flat with last year at $6.0 billion.

FY 2004

The Executive and the OLS both anticipate sales tax growth in FY 2004, as retail sales resume growth. The Executive anticipates collections of just over $6.334 billion, or 5.6% growth. This growth consists of 4.8% underlying growth plus an estimated $45.0 million in new revenues from the imposition of the sales tax on casino complimentary rooms and meals.

The OLS is somewhat more cautious in its outlook for FY 2004. The Council of Economic Advisors anticipates an average of about 3% growth in retail sales during FY 2004 and does not expect the recovery in auto sales until the latter half of the fiscal year. Accordingly, the OLS estimates $6.255 billion, or 4.3% growth in collections. This amount assumes 3.5% growth in underlying sales tax revenue and accepts for comparability purposes the $45.0 million from the Executive's proposed sales tax on complimentary rooms and meals.

Corporation Business Tax

The corporation business tax (CBT) underwent a significant revision with the passage of the Business Tax Reform Act last year (P.L. 2002, c.40). The act included a number of both permanent and temporary provisions which were anticipated to increase total CBT revenues in FY 2003 by at least $1.0 billion, effectively doubling the size of this revenue source. The preliminary receipts under the reform act have exceeded the original expectations, and the Executive and the OLS have revised their estimates for the current fiscal year upward.

FY 2003

Through the end of February, CBT collections were running 89% ahead of the same period in FY 2002. The first increase in payments under the reform act were expected in December of 2002, at which time corporations were to pay 25% of their annual tax liability. The substantially increased final payments are due in April for most taxpayers, with estimated payments for the next tax year due in April and June. The strength of collections so far suggests that the tax law changes are generating more revenue than was originally anticipated. Accordingly, the Executive has increased its revenue estimate for FY 2003 by $158 million, to a total of $1.987 billion.

While uncertainty surrounding this revenue is high -- and we will not know what revenues were produced by which provisions in the law until well into the next fiscal year -- the strength of year-to-date collections indicate that the actual collections are likely to exceed the Executive's revised estimate. Despite the uncertainty about this revenue source, the OLS estimates total year-end collections of $2.137 billion, $150 million greater than the Executive's estimate.

FY 2004

CBT revenues will decline in FY 2004. Several factors are responsible for inflating the first fiscal year revenues from the tax changes. Most significantly for the alternative minimum assessment and loophole closing provisions, the timing of the enactment of the law results in FY 2003 receiving all of the increase for tax year 2002 and a portion of the increase for tax year 2003. Timing also concentrates in FY 2003 most of the impact of the two year suspension of the use of net operating losses. Additionally, the provision shifting certain third quarter payments into the second quarter is effectively a one-shot revenue in excess of $100 million in FY 2003. Accordingly, both the Executive and the OLS estimate reduced revenues from the CBT in FY 2004.

Figure 9
OLS Corporation Business Tax Revenue Estimates
$ Millions

	FY 2003	FY 2004	
Category	Amount	Amount	% Change
CBT Base	$1,000	$1,050	5.0%
Energy	$12	$0	-100.0%
Tax Changes	$1,125	$720	-36.0%
Total	$2,137	$1,770	-17.2%

Tax changes include provisions of the Business Tax Reform Act, P.L. 2002, c.40.

Corporation Business Tax (Continued)

The Executive estimates an 8.3% decline, yielding a total of $1.823 billion. The OLS estimates a sharper 17.2% decline from a higher FY 2003 base. The net result is an OLS estimate of $1.770 billion that is $53 million less than the Executive's total.

When OLS produced a fiscal estimate for the Business Tax Reform Act, the impact of each component of the law was estimated for a three year period. As noted, for many of the components the revenue levels are anticipated to drop from the first year to the second. In the aggregate the fiscal estimate projected a 36% decline from FY 2003 to FY 2004 in the CBT revenues generated by the tax change. While it now appears likely that the overall revenue gain from the changes will exceed the aggregate estimate, we do not have any indication of which components are responsible for the windfall. In the absence of such information, we have applied the 36% decline to the total estimate of tax law change gains for FY 2003. In the OLS forecast, this decline is partially offset by an optimistic assumption that taxable corporate profits will grow during the year.

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The Cigarette Tax

The cigarette tax was increased by 70 cents per pack at the beginning of FY 2003. The Executive is now proposing an additional 40 cent per pack increase effective at the beginning of FY 2004. Figure 10, on the following page, displays the estimated impact of those tax changes in FY 2003 and FY 2004.

FY 2003

The FY 2003 Appropriations Act assumed total on-budget and off-budget revenues of $642 million, an increase of 62% over the prior year. The 70 cent tax increase, up 88%, was not expected to increase revenues by a full 88%, because price increases discourage consumption and cigarettes can be purchased out-of-state with some ease. Since the appropriations act revenue certification, the Executive reduced its estimate of FY 2003 revenues by $41 million. In FY 2003, total cigarette tax revenue is estimated by the Executive to grow by 54% to $601 million.

The OLS does not believe the Executive's $41 million downward revision in FY 2003 is warranted. Through the end of February, total cigarette tax revenues are up 62% (see Figure 2 on page 3). Accordingly, the OLS estimates $635 million in total revenues in FY 2003 ($480 million on-budget), or $34 million more than the Executive.

The Cigarette Tax (Continued)

Figure 10
Cigarette Tax Revenue Estimates
$ Millions

	FY 2002	FY 2003		FY 2004	
	Actual	Exec.	OLS	Exec.	OLS
Baseline	$381	$373	$373	$366	$366
One-Time Effect	$10	--	--	--	--
70 Cent Tax Increase	--	$228	$262	$210	$256
40 Cent Tax Increase	--	--	--	$78	$133
Grand Total	$391	$601	$635	$654	$755
Percent Growth		*54%*	*62%*	*9%*	*19%*
HCSF Dedication	$155	$155	$155	$155	$155
On-Budget Total	$236	$446	$480	$499	$600

Baseline revenue assumes an annual 2% decline in consumption.
The FY 2002 one time effect is due to advanced purchases prior to the July, 2002, tax rate increase.
HCSF = Health Care Subsidy Fund, an "off-budget" account.

FY 2004

The Executive estimates total cigarette tax revenues will grow to $654 million in FY 2004, or an increase of about 9% from their FY 2003 estimate. This increase includes the impact of the proposed 40 cent per pack tax rate increase (see Figure 10). On-budget cigarette tax revenues are estimated at $499 million.

The OLS believes growth will be significantly better than 9% and will grow from a higher FY 2003 base. The proposed 40 cent tax rate increase, up 27%, should result in additional sales losses, but not to the extent assumed by the Executive. Based on a conservative use of accepted economic assumptions,[1] the tax increase could cause a 6% sales decline. Further, assuming the continuation of longer-term declines in cigarette consumption of 2%, the OLS estimates the proposed 27% tax increase will yield a 19% revenue increase (27% - 6% - 2% = 19%). Total revenues should grow from $635 million in FY 2003 to $755 million in FY 2004. After subtracting $155 million for the Health Care Subsidy Fund, the OLS estimates on-budget cigarette tax revenue of $600 million in FY 2004, $101 million more than the Executive.

[1] Cigarette price elasticity is commonly estimated at about -0.4, which means that a 10% price increase would result in a 4% sales decline. The proposed 40 cent tax increase in New Jersey amounts to a price increase of approximately 10%, which would trigger a sales decline of 4%. The OLS assumes an additional 2% sales decline due to the relative ease with which New Jersey residents may purchase cigarettes out-of-state.

Remaining Revenue Differences

Three remaining revenues in which there are more than minor differences between the Executive and the OLS are inheritance taxes, insurance premiums taxes, and the Casino Revenue Fund.

Inheritance taxes: The OLS is estimating $10 million more in FY 2003 and $22 million more in FY 2004 than the Executive. As is shown in Figure 2 on page 3, current collections trends are slightly better than the Executive's year-end assumptions require. The OLS is also slightly more optimistic that the recent declines in inheritance tax revenues, though continuing, will slow in FY 2004.

Insurance premiums taxes: The OLS is estimating $17 million more in FY 2003 and $24 million more in FY 2004. Current collection trends indicate stronger growth in this revenue than the Executive anticipates.

Casino taxes: The OLS is estimating less than the Executive -- $10 million less in FY 2003 and $45 million less in FY 2004. Current collection trends suggest a lower amount is likely in FY 2003. FY 2004 is complicated by the assumption of $90 million in new revenues from a proposed increase in this tax. As with most Executive proposals, the OLS accepts the $90 million estimated amount from the tax increase for comparability purposes. However, the OLS believes the Executive's FY 2004 growth assumptions are too high, even after excluding the tax increase, and adjusting for the anticipated opening of a new casino.

Most of the remaining divergence between the OLS and the Executive revenue estimates involve small differences based on current revenue growth patterns. The first two tables in the appendix display the revenue differences in detail.

Proposed New Revenues

Lastly, the OLS notes that the Executive's budget proposal includes revenues from a number of new sources, including many that will require legislation. While legislation to achieve these goals has not yet been introduced, it is the practice in OLS revenue analyses to assume that all gubernatorial revenue proposals will be realized. Some of the following proposals have been discussed previously in this report; others are included in the “all other” totals in the tables:

? New 7% Hotel/Motel Occupancy Tax: $140 million.

? Increase Realty Transfer Fee rate on sales above $150,000: $93 million.

? Increase Casino Revenue Tax from 8% to 10%: $90 million.

? Increase Cigarette Tax by 40 cents per pack: $78 million (*OLS estimates $133 million*).

? Extend Sales Tax to complimentary rooms and meals: $45 million.

? Increase Fees and Fines: $82 million.

? Increase Universal Service Fund utility surcharges: $72 million.

? Impose a new Wireless Service Assessment: $46 million.

? Enhance Debt Collection from certain motor vehicle and hospital debts: $62 million.

? Institute transfers from various Trust Funds: $220 million.

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Appendix Contents:

Detailed Fiscal Year 2003 Revenue Estimates
$ Millions

Revenue Source	Approp. Act	Executive Revised	OLS	Diff: OLS - Executive
Major Taxes:				
Sales Tax, Total	$6,172.0	$6,000.0	$6,000.0	$0.0
Corporation Business Tax, Total	1,829.5	1,987.1	2,137.1	150.0
Corporation Business Tax, Base	*1,823.0*	*1,975.0*	*2,125.0*	*150.0*
Corporation Business Tax, Energy Contribution	*6.5*	*12.1*	*12.1*	*0.0*
Motor Fuels	536.0	530.0	525.0	(5.0)
Motor Vehicle Fees*	424.9	281.5	281.5	0.0
Inheritance Taxes	530.0	420.0	430.0	10.0
Insurance Premiums	345.0	348.0	365.0	17.0
Cigarette	487.0	446.0	480.0	34.0
Petroleum Products Gross Receipts	225.0	215.0	220.0	5.0
Corporation Business - Banks and Financial	52.0	79.0	85.0	6.0
Alcoholic Beverage Excise	79.0	82.0	82.0	0.0
Realty Transfer	96.0	110.0	110.0	0.0
Savings Institutions	5.0	19.0	19.0	0.0
Tobacco Products Wholesale	13.0	10.0	10.0	0.0
Public Utilities Excise	8.7	8.7	8.7	0.0
Subtotal, Major Taxes	$10,803.1	$10,536.3	$10,753.3	$217.0
Misc. Taxes, Fees and Revenues				
Public Utility Taxes (State retention)	$69.0	$69.0	$69.0	$0.0
Transitional Energy Facility Assessments	226.2	219.5	219.5	0.0
Medicaid Uncomp. Care Reimbursement	414.2	465.7	465.7	0.0
Other	1,445.5	1,361.1	1,361.1	0.0
Subtotal, Misc. Revenues	$2,154.9	$2,115.3	$2,115.3	$0.0
Interfund Transfers				
State Lottery Fund	$797.0	$783.0	$783.0	$0.0
Tobacco Settlement Fund	1,351.7	1,768.6	1,768.6	0.0
Unclaimed Personal Property Trust Fund	255.0	270.6	270.6	0.0
Other	325.5	315.9	315.9	0.0
Subtotal, Interfund Transfers	$2,729.2	$3,138.1	$3,138.1	$0.0
TOTAL GENERAL FUND	$15,687.1	$15,789.7	$16,006.7	$217.0
Property Tax Relief Fund (Income Tax), Total	$7,297.5	$6,966.0	$6,840.0	(126.0)
Casino Revenue Fund	364.8	357.9	347.9	(10.0)
Casino Control Fund	62.7	62.7	62.7	0.0
Gubernatorial Elections Fund	1.5	1.5	1.0	(0.5)
GRAND TOTAL, ALL FUNDS	$23,413.6	$23,177.8	$23,258.3	$80.5

* The $281.5 million amount for motor vehicle fees assumes that $143 million will be transferred to an off-budget account. This assumption was not part of the original appropriations act certification.

Detailed Fiscal Year 2004 Revenue Estimates
$ Millions

Revenue Source	Executive	% Change	OLS	% Change	Diff: OLS - Executive
Major Taxes:					
Sales Tax, Total	$6,333.8	5.6%	$6,255.0	4.3%	($78.8)
Sales Tax, Base	*6,288.8*	*4.8%*	*6,210.0*	*3.5%*	*(78.8)*
Sales Tax, Casino Comp.'s	*45.0*		*45.0*		*0.0*
Corporation Business Tax, Total	1,823.0	(8.3)%	1,770.0	(17.2)%	(53.0)
Corporation Business Tax, Base	*1,823.0*	*(8.3)%*	*1,770.0*	*(17.2)%*	*(53.0)*
Corporation Business Tax, Energy Contribution	*0.0*		*0.0*		*0.0*
Motor Fuels	544.0	2.6%	535.0	1.9%	(9.0)
Motor Vehicle Fees	234.0	(16.9)%	234.0	(16.9)%	0.0
Inheritance Taxes	378.0	(10.0)%	400.0	(7.0)%	22.0
Insurance Premiums	356.0	2.3%	380.0	4.1%	24.0
Cigarette	499.0	11.9%	600.0	25.0%	101.0
Petroleum Products Gross Receipts	221.0	2.8%	225.0	2.3%	4.0
Corporation Business - Banks and Financial	79.0	0.0%	79.0	0.0%	0.0
Alcoholic Beverage Excise	83.0	1.2%	83.0	1.2%	0.0
Realty Transfer	210.0	90.9%	200.0	81.8%	(10.0)
Savings Institutions	20.0	5.3%	20.0	5.3%	0.0
Tobacco Products Wholesale	10.0	0.0%	13.0	30.0%	3.0
Public Utilities Excise	8.7	0.0%	8.7	0.0%	0.0
Subtotal, Major Taxes	$10,799.5	2.5%	$10,802.7	0.5%	$3.2
Misc. Taxes, Fees and Revenues					
Public Utility Taxes (State retention)	$69.0	0.0%	$69.0	0.0%	$0.0
Transitional Energy Facilities Assessment	175.1	(20.2)%	175.1	(20.2)%	0.0
Medicaid Uncomp. Care Reimbursement	455.1	(2.3)%	455.1	(2.3)%	0.0
Hotel Occupancy Tax	140.0		140.0		
Other	1,430.2		1,430.2		0.0
Subtotal, Misc. Revenues	$2,269.4	7.3%	$2,269.4	7.3%	$0.0
Interfund Transfers					
State Lottery Fund	$783.0	0.0%	$783.0	0.0%	$0.0
Tobacco Settlement Fund	1,447.9	(18.1)%	1,382.9	(21.8)%	(65.0)
Unclaimed Personal Property Trust Fund	172.4	(36.3)%	172.4	(36.3)%	0.0
Other	310.9	(1.6)%	310.9	(1.6)%	0.0
Subtotal, Interfund Transfers	$2,714.2	(13.5)%	$2,649.2	(15.6)%	($65.0)
TOTAL GENERAL FUND	$15,783.1	0.0%	$15,721.3	(1.8)%	($61.8)
Property Tax Relief Fund (Income Tax), Total	$7,493.8	7.6%	$7,280.0	6.4%	(213.8)
Casino Revenue Fund	512.2	43.1%	467.2	34.3%	(45.0)
Casino Control Fund	62.7	0.0%	62.7	0.0%	0.0
Gubernatorial Elections Fund	1.5	0.0%	1.0	0.0%	(0.5)
GRAND TOTAL, ALL FUNDS	$23,853.3	2.9%	$23,532.2	1.2%	($321.1)

Public Utility Tax Revenue

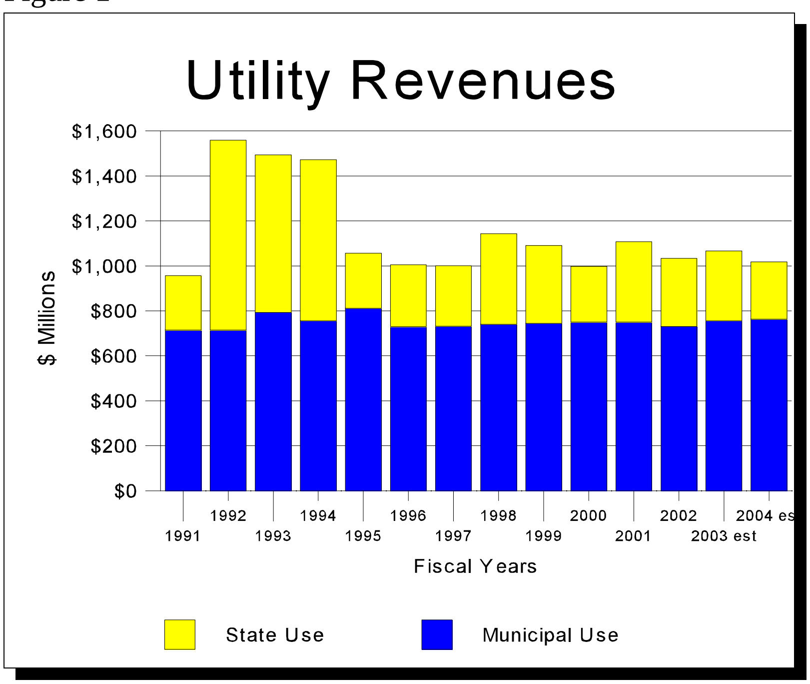
Fiscal Year 2004 will be the seventh year under the revised system of public utility, energy and telecommunications taxation. P.L.1997, c.162 repealed the 1940 State tax system of franchise and gross receipts taxes imposed on regulated gas and electric utilities and telecommunications utilities operating in New Jersey, effective on January 1, 1998. Energy utilities are now subject to the sales and use tax, the corporation business tax (CBT) and the transitional energy facility assessment tax (TEFA), a temporary tax intended to phase out over time. Telecommunications utilities became subject to the CBT under this act.

Figure 1 below displays public utility revenues between FY 1991 and FY 2004. The revenues are divided into two categories: *Municipal Use*, which is generally "off budget" and *State Use*, which is generally "on budget." Collections through FY 1997 were under the old public utility tax system. The State Use portions from FY 1992 to FY 1994 included substantial scheduled prepayments from large utilities pursuant to statutory changes at that time. Since FY 1998 taxes have been collected under the current law. Figures 2 through 4 display the actual and anticipated revenues from the replacement taxes between FY 2002 and FY 2004 in greater detail.

P.L 1997, c.167 replaced the complex aid distribution formulae that were contained in the franchise and gross receipts statutes and provided a new system for the distribution of State aid to municipalities. In FY 1998, $740 million from the taxes were credited to the Energy Tax Receipts Property Tax Relief Fund and distributed to municipalities according to the new formula. The amount credited to this fund grew to $755 million in FY 2003. For FY 2004, the Executive is estimating a $7.7 million increase to $762.7 million.

From a budgeting perspective, the tax revenues credited to the Energy Tax Receipts Property Tax Relief Fund are considered "off budget" and therefore not included in either the anticipated revenues or the amount of State aid appropriated in the annual appropriations act.

Figure 1



The TEFA was originally scheduled to end in FY 2002. However, P.L. 2001, c.433, extended the assessment through FY 2006. For FY 2002 through FY 2004, the 2001 assessment rates will be used. The TEFA then phases down in FY 2005 and FY 2006, and under current law will not exist in FY 2007.

Figure 2

Actual Public Utility Tax Revenue Fiscal Year 2002

($ Millions)

Revenue Source	On-Budget (State Use)	Off-Budget (Municipal Aid)	Total
Sales and Use Tax		$565.6	$565.6
Corporation Business Tax		$163.2	$163.2
Transitional Energy Facilities Assessment (TEFA)	$221.2	$0.2	$221.4
Customer Specific Tax	$2.0		$2.0
Franchise and Gross Receipts Tax Water and Sewer Utilities	$72.7		$72.7
Public Utility Excise Tax Water and Sewer Utilities	$9.9		$9.9
Total	$305.8	$729.0	$1,034.8

Source: Department of Treasury, March 2003.

Figure 3

Anticipated Public Utility Tax Revenue Fiscal Year 2003

($ Millions)

Revenue Source	On-Budget (State Use)	Off-Budget (Municipal Aid)	Total
Sales and Use Tax		$588.5	$588.5
Corporation Business Tax	$12.1	$166.5	$178.6
Transitional Energy Facilities Assessment (TEFA)	$219.5		$219.5
Customer Specific Tax	$2.0		$2.0
Franchise and Gross Receipts Tax Water and Sewer Utilities	$69.0		$69.0
Public Utility Excise Tax Water and Sewer Utilities	$8.7		$8.7
Total	$311.3	$755.0	$1,066.3

Source: Department of Treasury, March 2003.

Figure 4
Anticipated Public Utility Tax Revenue Fiscal Year 2004
($ Millions)

Revenue Source	On-Budget (State Use)	Off-Budget (Municipal Aid)	Total
Sales and Use Tax		$609.3	$609.3
Corporation Business Tax		$109.0	$109.0
Transitional Energy Facilities Assessment (TEFA)	$175.1	$44.4	$219.5
Customer Specific Tax	$2.0		$2.0
Franchise and Gross Receipts Tax Water and Sewer Utilities	$69.0		$69.0
Public Utility Excise Tax Water and Sewer Utilities	$8.7		$8.7
Total	$254.8	$762.7	$1,017.5

Source: Department of Treasury, March 2003.

The New Jersey Budget Faces Ongoing Strains

State budgets are likely to face several years of structural shortfalls. The four years from FY 1998 to FY 2001 saw annual revenues grow by 6.7% and annual State expenditures grow by 6.9%, on average. The sudden drop in revenues in FY 2002 precipitated a budget crisis, and initiated an ongoing need to find substantial temporary sources of revenue over the next several years.

The FY 2003 and the proposed FY 2004 budgets are each supported by at least $2.0 billion in temporary revenues. Recurring revenues from current taxes are unlikely to replace these temporary revenues in the next few years, even under the most optimistic economic growth expectations. Indeed, the longer an economic recovery is delayed, the deeper the structural problems will become.

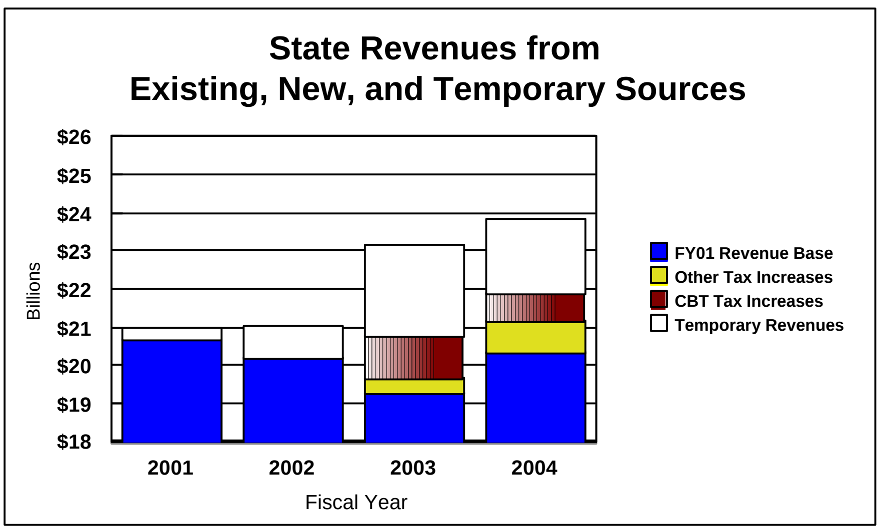


Figure A displays existing, new, and temporary revenues for Fiscal Years 2001 through 2004. FY 2001 represented a peak year with nearly $20.7 billion in recurring, statutory revenues. Temporary revenues such as the Transitional Energy Facilities Assessment (TEFA) and various fund transfers accounted for less than $300 million of additional revenues. The fiscal crisis of FY 2002 saw State revenues decline for the first time in decades, largely due to an unprecedented 14% decline in income tax revenues. Temporary revenues grew to over $800 million. To help weather the crisis, the State implemented spending constraints[1] and drew down the surplus by about $1.0 billion.

FY 2003 revenues have been supported by a major tax increase and a substantial jump in the use of temporary revenues. The corporation business tax (CBT) was significantly reformed under P.L. 2002, c.40, and may be contributing more than $1.1 billion in new State revenue. Temporary revenues are approaching $2.4 billion, including more than $1.7 billion from the Tobacco Settlement Fund, the extension of the TEFA, and numerous transfers from a variety of State funds. Other tax and fee increases raised about $360 million. Recurring revenues from the FY 2001 base have declined to less than $19.3 billion.

The proposed FY 2004 budget revenues anticipate that recurring revenues will grow to $20.3 billion. However, due to temporary features of the CBT reforms, corporation revenues are anticipated to decline by hundreds of millions of dollars. Temporary revenues total about $2.0 billion, including over $1.4 billion from the Tobacco Settlement Fund. The FY 2004 budget also assumes the State will enact a number of new revenue sources worth over $400 million. Chief among those new revenues is the proposed $140 million hotel/motel tax, a $93 million increase in the realty transfer tax, a $90 million increase in casino taxes, and $133 million (OLS estimate) from a 40 cent increase in the cigarette tax.

[1] The spending constraints are outside the scope of this revenue analysis.

The difficulty facing the State in FY 2005 and beyond is that the temporary revenues cannot be replaced by growth in recurring revenues. While some of the smaller fund transfers may be replaceable with different future fund transfers, the most important temporary revenue, the Tobacco Settlement Fund, is not easily replaceable. In FY 2005 little or no tobacco money will remain for budget use, creating a $1.4 billion revenue hole. In addition, the TEFA will begin phasing down until it disappears in FY 2007, and certain provisions of the CBT reform act, such as the net operating loss disallowance, will also end.[2]

Recurring revenues cannot replace the loss of these substantial temporary revenue sources. During the remarkable boom years from FY 1998 to FY 2001, when growth in non-wage income pushed the income tax to double digit rates of growth each year, the State saw annual tax revenues grow by between $1.0 billion and $1.4 billion. A repeat of that kind of State revenue boom would first require several years of a surging stock market to eliminate recent asset losses and begin to create asset gains. Even if such a market boom were about to begin, any potential revenue surge would still be years away.

Declining Surplus

In addition to the prospect of on-going structural shortfalls in the coming years, the State also faces a slim margin for error. Each enacted budget lists anticipated resources in excess of appropriations, leaving a projected surplus to meet contingencies. Figure B displays the actual State budget surpluses since FY 1983. The estimated $102 million surplus for FY 2003 is the lowest level since the $139 million amount 20 years ago and the $162 million amount 13 years ago.

Figure B
State Budget Surpluses
$ Millions

FY	Actual Amount
1983	$139.3
1984	$645.8
1985	$891.2
1986	$640.9
1987	$882.6
1988	$1,203.0
1989	$595.8
1990	$162.1
1991	$370.6
1992	$836.2
1993	$1,149.6
1994	$1,264.6
1995	$950.3
1996	$882.2
1997	$1,106.4
1998	$1,256.7
1999	$1,268.0
2000	$1,284.6
2001	$1,287.6
2002	$292.3
2003	*est $101.5*
2004	*est $253.0*

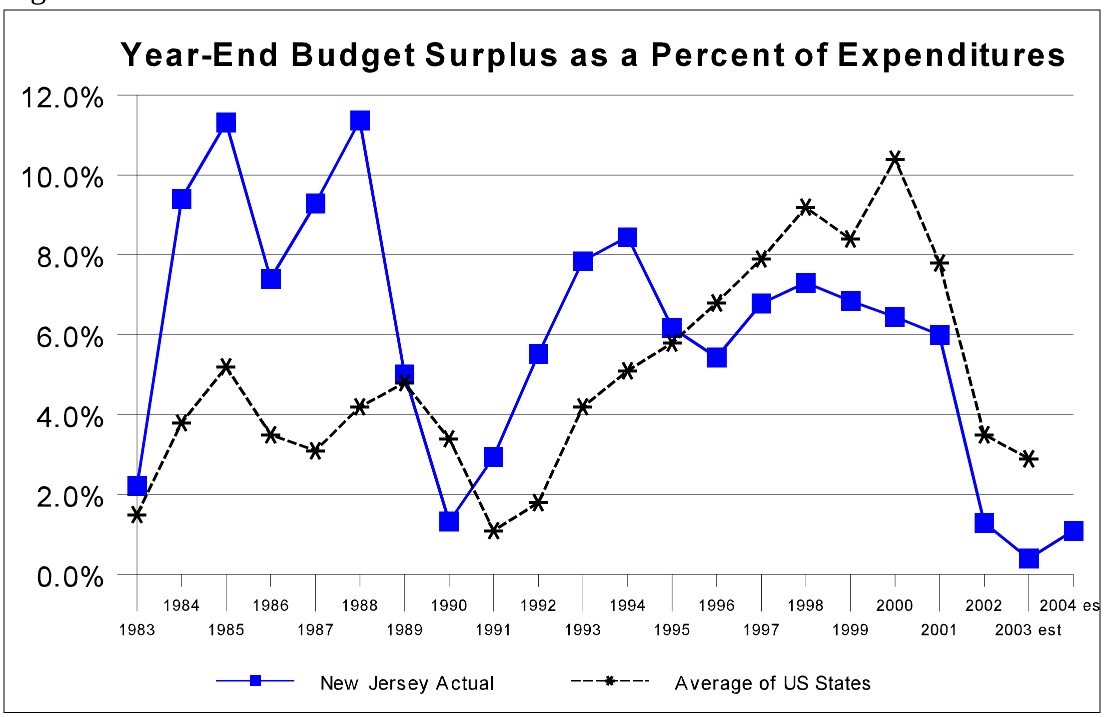
Surplus includes amounts from the General Fund, Property Tax Relief Fund, Casino Revenue Fund, Casino Control Fund, Gubernatorial Elections Fund and the Surplus Revenue Fund (ie., the "Rainy Day" Fund).

[2] In addition to these revenue concerns are a number of significant "off-budget" spending items supported by revenues that are not included in the annual budget, such as some $600 million in federal monies in dispute and over $300 million in Charity Care payments supported by payroll taxes.

In fact, the FY 2003 surplus is proportionately much lower than in the past, leaving the State with little room to maneuver in a $24 billion budget. Figure C displays the year-end budget surplus as a percent of expenditures over the last 20 years. New Jersey's budget surpluses peaked in the 1980's at over 11% of annual expenditures, fell below 2% in FY 1990, rose above 6% during much of the 1990's, and then dropped again to only 0.4% in FY 2003. The Governor's FY 2004 proposed surplus would equal 1.1% of appropriations. In recent years New Jersey has consistently lagged behind national averages compiled by the National Association of State Budget Officers.

In summary, the State faces the prospect of several more daunting budget years. The availability of substantial temporary revenues will end with the FY 2004 budget, particularly the Tobacco Settlement Fund. The likelihood of a surge in recurring revenues such as during the boom years of the late 1990's is uncertain and distant. Delayed economic recovery following international political events would magnify current structural revenue problems. Meanwhile, low budget surpluses leave the State walking a fiscal tightrope. The old rally cry, "wait 'til next year," may have an ironic twist for the State.

Figure C



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New Jersey Review and Economic Outlook for 2003-2004

State of New Jersey
Council of Economic Advisors
February 2003

The Office of Legislative Services thanks the Council for permitting the reproduction of its annual economic report in the following appendix pages of the FY 2003-2004 Revenue Analysis.

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NJ Review & Economic Outlook for 2003-2004

Forecast Summary: "New Jersey's economy is seeking direction in the cross-current of expansionary monetary and fiscal policies versus the restraints of uncertainty about war and hesitant consumer and business spending."

Joseph J. Seneca, Chairman

NJ Forecast 2003-04

The economy of New Jersey is expected to parallel national patterns of growth for the next two years.

Summary:

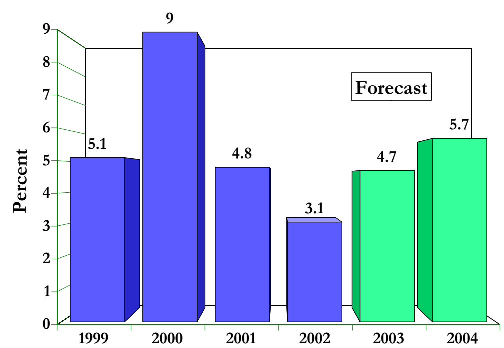
	2003	2004
Gross State Product (Current $)	4.7%	5.7%
Personal Income (Current $)	4.0%	4.7%
Retail Sales (Current $)	2.7%	3.2%
Consumer Price Index (All Urban)	2.7%	2.9%
Non-ag Employment	0.9%	1.3%

For 2003, NJ's growth prospects hinge to a large degree on federal policy and spending initiatives.

Federal fiscal policy offers a double-barreled prospect for New Jersey. Spending on defense and homeland security will increase sharply in FY03 and 04. Although NJ ranks 31st in per capita federal procurement, spending increases for technology products, surveillance, communications, and related goods, create opportunities for the State's hi-tech sector. Also, the tax cut proposal by President Bush, $103 billion in 2003, will benefit NJ households. These changes, if approved, will have a multi-billion dollar impact on the disposable income of NJ taxpayers. A large share of this additional income will be spent in our state, with positive, if modest, effects on employment, sales and state tax revenues. The implications of the federal tax proposal are detailed later in this report. Missing, unfortunately, from the proposal is any direct fiscal relief to NJ and the other states.

A continuation of the Federal Reserve's low interest rate policies will support NJ's growing cluster of financial industries, extend the home buying and home building market with low cost financing, boost consumer incomes for homeowners who refinance their existing mortgages, and help maintain the rate of retail spending.

NJ Gross State Product, Current $, % Change



The forecast is for NJ Gross State Product to advance 4.7% in 2003 and 5.7% in 2004. Non-farm employment should add almost 40,000 jobs this year (on an average annual basis), accelerating to a gain of 50,000 in 2004. Job gains help boost personal income by 4.0% in 2003, and 4.7% in 2004. The unemployment rate slowly falls to 5.2% this year and 4.9% next year. The level of home building should remain level near 28,000 new units this year, but non-residential building is constrained by high vacancy rates and the slow growth of new service jobs. Inflation advances to almost 3% due to higher home prices, medical and energy costs.

Other positive signs for the New Jersey economy are new developments in Atlantic City, and improved business capital spending which will support the technology sector. The absence of excesses, aside from high office vacancy rates, positions the State well as business and consumer demand increase.

The US Economy ……………………

The US economy finished 2002 with Gross Domestic Product (GDP) advancing 2.4%, up from a .3% gain in 2001. Final sales improved by (only) 1.7% last year as inventory rebuilding absorbed a larger share of current production. Total payroll employment fell last year by .9% and the average unemployment rate rose a full percentage point to 5.8%. Although GDP had risen for five straight quarters, remarkable gains in labor productivity, estimated in the 4-5% range, limited additions to employment, but kept inflation to well under 2% for the year.

Sectors contributing the most to US growth in 2002 were consumer spending which increased 3%, and (federal) government spending with a 4% gain. Defense spending led the government sector with a 9% increase in outlays. Restraining the economy last year were business capital investment, down another 5.5% following a 5% decline in 2001, and a rising trade deficit aggravated by continued weak overseas markets.

Despite a weak 4th quarter, GDP growth is expected to improve in 2003 with moderating growth in consumer spending offset by another surge in federal government purchases and a return to a positive rate of growth for business capital outlays. State & local government spending remains weak as budget deficits widen.

The US outlook, however, hinges on uncertainty of war in the Middle East, threats to the US oil supply, a stable monetary policy, and the specifics of a federal fiscal stimulus tax-cut program.

Across The States …………………..

For 2002 economic recovery remained elusive for most states. Jobless rates were higher or stable in 31 states and lower in only 19 states. Although unemployment in the Mid-Atlantic region (5.8%) remained below the national average, the region still felt the effects of the bursting of the high tech bubble, the demise of over-leveraged startups, stock market shocks and weakness in financial services.

Over the year, jobs actually decreased in 31 states. The largest declines were in Illinois (-67,100), Missouri (-47,400), and Georgia (-44,600). The biggest over-the-year gains in employment occurred in Florida (+43,700), Nevada (+29,200), and Wisconsin (+23,900).

Manufacturing was the weakest industry group, with 47 states posting over-the-year employment decreases. The downturn in demand for industrial equipment and consumer durable goods were felt the most in the Midwest and Southeast regions. Employment losses also were widespread in transportation and public utilities with over-the-year declines in 45 states. Contributing to employment were job gains in government for 46 states. Modest employment improvements in services occurred in 41 states.

Economic issues facing most states include budget deficits, increased costs for homeland security, a rise in healthcare costs and mandates to improve primary and secondary education. Magnifying the state's problems is that most have exhausted readily available financial options, using rainy day funds, tobacco settlement monies and increased borrowing to close budget gaps from the previous year.

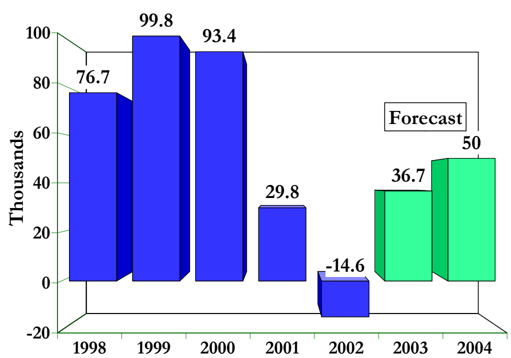
Competitive economic development advantages and disadvantages among states stand to widen in the next two years as states seek to impose tax and fee increases along with spending cuts that will effect education, infrastructure, services and capital improvements that support long term growth.

NJ Employment…………………..……

For 2002 the NJ labor market symbolized the jobless recovery. Despite modest economic growth in 2002 total non-ag employment averaged 4,009.7 thousand, a decline from 2001 of 14,600 jobs. However, the average annual job loss was .4%, versus a .9% loss nationally. If measured on a December to December calendar year basis, NJ employment fell by 13,900.

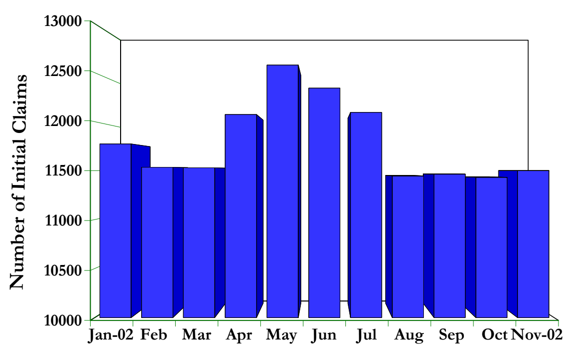
For 2002, the NJ unemployment rate averaged 5.4%, up from 4.2% in 2001, and 3.8% in 2000. With relatively better employment prospects in construction, retail/wholesale trade, the State's jobless rate remained lower than the US average of 5.8%.

NJ Non-ag Employment, Annual Change



A closer look at labor market trends by month provides clear evidence of the early stages of a recovery. Initial claims for unemployment insurance, a leading job indicator, have stabilized.

Initial Claims for NJ Unemployment Insurance Three Month Moving Average

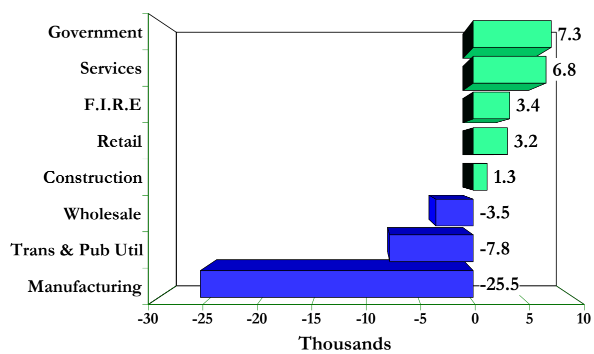


The three-month moving average for new UI claims has not increased since the 2nd quarter of 2002.

Employment by Industry ....

By sector, government posted the best average annual performance adding 7.3 thousand jobs, a gain of 1.2%. This sector was bolstered by gains related to homeland security hiring and additions to local government. Services expanded by 6.8 thousand jobs, or .5%. This sector added jobs in engineering & management services, health services and social services. The finance sector (FIRE) added 1.2%, or 3.4 thousand jobs due, in part, to interstate business relocations to NJ. Retailing and construction added a modest 3.2 thousand and 1.3 thousand jobs, respectively.

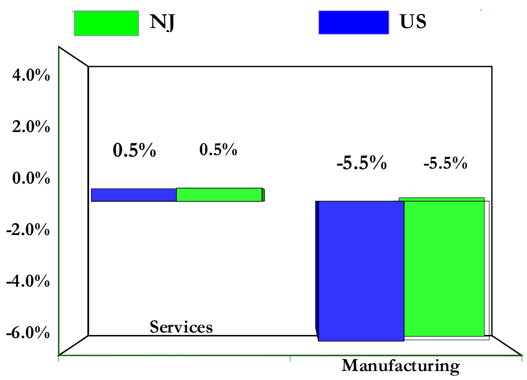
NJ Employment Growth by Industry, 2001-02



The manufacturing sector lost 25.5 thousand jobs on an average annual basis, a decline of 5.5% from 2001. The end of the technology cycle, a national recession led by sharp declines in business capital spending, and weak international markets contributed to employment losses in virtually all components of manufacturing. The transportation/public utilities sector lost 7.8 thousand jobs (-2.9%) from downsizing at telecommunication companies and weakness in the travel (especially air transportation) sectors.

NJ's labor market performance for 2002 matched US trends in two important sectors. Both services and manufacturing employment patterns in NJ equaled their US counterparts; services gained .5% and factory jobs declined by 5.5%.

Employment % Change, 2001-02
Selected Sectors, NJ & US



NJ Growth Clusters ……………………

NJ's growth clusters (logistics, finance, research & technology services, casino/entertainment, information technologies, and pharmaceutical/bio-tech) account for about 30% of private sector employment, and more than 40% of job growth during the 1990's. These clusters, however, experienced net job losses during 2002. For the first time in over ten years the six growth clusters lost 21,600 jobs, a decline of 1.9%. The combination of the technology downturn, over-investment in telecommunications, travel disruptions, and financial turmoil affected each cluster. Since clusters tend to lead NJ economic growth, their near-term outlook is critical to the State's overall forecast.

Employment in NJ Growth Clusters, Change 2001 - 02

	Number (000)	Percent
Casino/Entertainment	1.1	0.9%
Pharm/Bio Tech	-0.3	-0.5%
Finance	-2.5	-1.7%
Research & Tech.Services	-3.2	-1.8%
Logistics	-6.4	-1.6%
Information Tech.	-10.3	-4.8%
Cluster Total	-21.6	-1.9%
Total Non-Cluster	3.6	0.1%

The Outlook by cluster -

Finance – On the positive side a monetary policy geared to low interest rates is favorable to the finance sector(s) that are concentrated in the Northeast and the West coast. For NJ, this sector contributed to job gains in 2002, with part of the gain attributed to the relocation of finance firms from NYC. However, recent monthly data suggest some financial company movement back to NYC. The cluster should experience a cyclical recovery in 2003-04, but it remains unclear on which side of the Hudson River.

Research & technology services – a cyclical recovery in corporate R&D, engineering and consulting often lags the general recovery and will hinge largely on a recovery in business capital spending. The cluster, which includes engineering, accounting, business consulting, and testing laboratories, may benefit from increased defense and homeland security spending on new technology.

Pharmaceuticals – and biotechnology weathered the 2002 recession with a stable employment and output base. Long term demographic trends plus research and development needs remain favorable to the cluster.

Casino & entertainment – Atlantic City's current $1.75 billion casino and retail development is creating demand for labor -- an expected 12,000 new workers in 2003. The Borgata, a $1 billion casino entertainment resort that seeks 5,000 workers, is set to open in the summer of 2003, while several other casinos are expanding and adding another 2,000 rooms. In mid-2002, ground was broken for a $60 million retail district, expected to generate 4,000 to 5,000 jobs.

Logistics – a modest recovery is in the pipeline, but a prolonged recovery will depend on a continuation of consumer spending growth, recovery in air travel, and gains in international trade.

Information technology – Industry analysts claim the worst is over for the telecommunications sector, however employment continues to erode. The cluster will gain from homeland security spending initiatives.

GUNS AND BUTTER - AGAIN!

The very large tax cut proposal, $103 billion in 2003, by President Bush is a variant of the era of President Lyndon Johnson who sought to fight a war while increasing domestic government spending. President Bush seeks to raise military spending and to cut taxes (and simultaneously change the structure of the federal tax code). How would all this affect New Jersey?

First, the easy answers –

1. The acceleration of the child tax credit and reduction of the marriage tax will benefit all eligible NJ families. These changes will tend to assist low and middle income taxpayers disproportionately since the reduction in tax liabilities will represent a larger percentage tax liability reduction in these income categories compared to higher income taxpayers.

2. The acceleration of the threshold income level subject to the lowest marginal income tax rate (10%) will also benefit low-income NJ families. These changes will increase the disposable income of NJ taxpayers. A large share of this additional income will be spent, and spent in our state, with positive, if modest, effects on employment, sales, and state tax revenues.

3. The faster write-off of investments will be a positive incentive for NJ's small business community and will boost capital spending and possibly profits.

4. The proposed spending accounts for unemployed workers to assist job searches, job training, and other expenses incurred to find work can reduce the time between jobs and cushion the negative effects of being without work. However, the administration of this program will create challenges for the states to implement and for individuals to access.

After these relatively straightforward components, the task of assessing the other components of the proposal is more complex – the centerpieces of the proposal are; 1. the exemption of dividends from federal taxation, and 2. the acceleration of the future income tax cuts already enacted into the current calendar year.

NJ, as a high income, high wealth state, will benefit disproportionately more than most other states, with a resulting increase in disposable income and spending. Any increase in equity values as a result of the dividend exemption will also benefit NJ taxpayers relatively more since ownership of stock in our State exceeds the national average. Finally, since legislation is required for all of these changes, any benefits are not likely to show up in individual's incomes until the second half of 2003, or later.

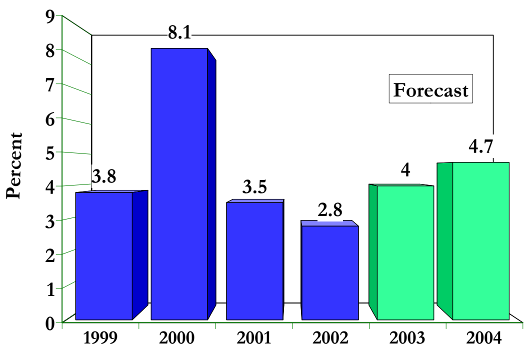
However, the dividend proposal is not actually a short-term stimulus to the national economy. It is a structural change in the tax code designed to encourage more investment, reduce the dependence of corporations on debt financing, and stimulate the issuance of stock. Its benefits are likely to be long-term, and result from the effects of increasing the growth rate of the national economy.

The major disappointment for NJ, and for all states in general, is the absence of any immediate, significant relief in the President's proposals to the deep fiscal problems caused by the sharp drop in tax revenues from the recession and the bear equity markets of the past three years. Any stimulus effect to the national economy from the tax cuts will be offset, to an extent, by the painful and inevitable retrenchment in spending and the increase in taxes by states as they respond to budget problems. Hopefully, the case for budget relief for the states will influence the federal legislative process and result in large, flexible grants, to provide critically needed help for NJ and others.

Personal Income & Retail Spending…

The latest data available suggest a 2.8% increase in NJ personal income for 2002. The modest gain closely trailed the 3% national rate of growth. For the year personal income was limited by overall employment losses in the state, a stagnating New York City economy, sharp reductions in non-wage income (investment earnings), and proprietor incomes.

NJ Personal Income, Current $, % Change



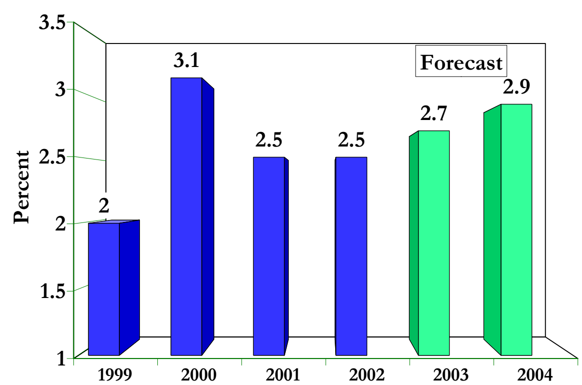
Job losses in NJ's growth clusters, which include most of the State's highest paying sectors, cut into income gains. Job losses in the finance cluster along with sharp reductions in year-end bonuses limited income gains. On a per capita, after tax basis, disposable incomes rose 3.5% in 2001 and an estimated 3.7% in 2002.

NJ retail markets were battered by several factors that left 2002 retail sales flat versus a year ago. Job losses and slower income growth throughout the Region affected consumer confidence and spending plans. Less travel meant fewer outside visitors to the State's tourist destinations. The Port Authority of NY and NJ reported that passenger traffic through Newark/Liberty airport fell 13% in 2002. On the positive side, retailing was supported by little, or no, inflation for many consumer goods, lower interest rates (and financing costs), sales promotions, and incentives for many goods (especially autos). A relatively strong year for new home construction and home buying, in general, created demand for furnishings and fixtures, and appliances. Lastly, mortgage refinancing contributed to household cash flow and retail spending.

Consumer Prices……………………

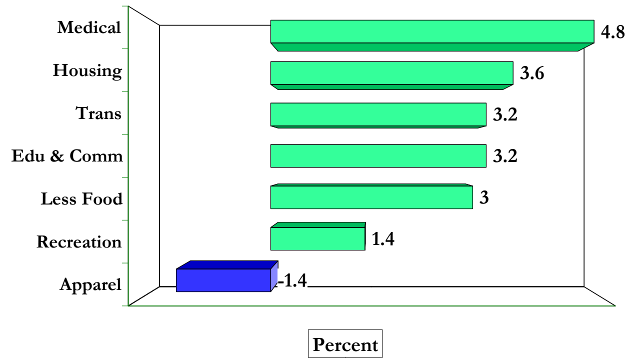
Regional consumer prices (New York City, Northern NJ metropolitan region) posted an average annual increase of 2.5% in 2002, following a similar 2.5% increase in 2001. For the US, consumer prices rose only 1.6% partly due to weaker job markets and housing markets in other states.

Consumer Price Index, % Change (NY/NJ PMSA)



A local factor boosting overall NY/NJ consumer prices in 2002 was a 3.6% increase in the housing component (which includes the cost of new and existing homes, rentals, and costs related to home ownership and operations). Transportation prices rose 3.2%, education 3.2% and recreation rose only 1.4%. Apparel prices fell 1.4% over the year, partly reflecting heavy price discounting and sales promotions during the Christmas retail season.

NY/NJ Consumer Price Index,
By Expenditure Category
% Change 2001-02

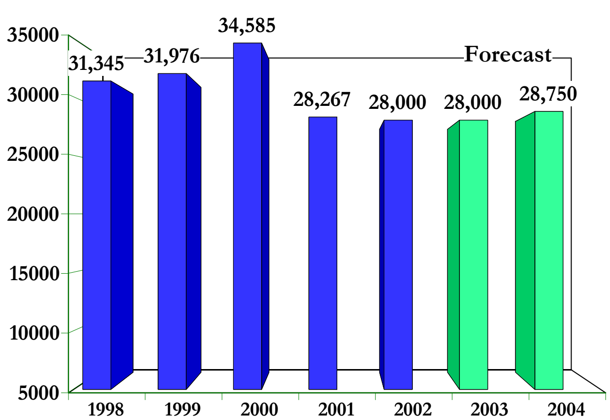


Local prices rose slightly more than expected for several factors created outside the region; including higher energy/fuel prices related to war threats in the Middle East, and a recurrence of health care inflation (+4.8%).

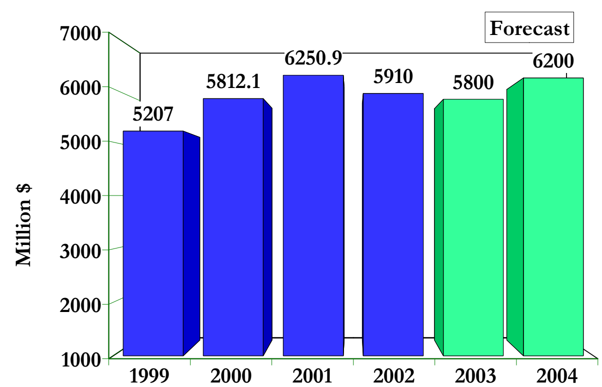
Investing in New Jersey ....

NJ home building defied the brunt of last year's recession with an estimated 28,000 new residential permits filed. Home building benefited from mortgage rates at 37 year lows and added demand from household in-migration. Increased residential demand also pushed prices upward. By years' end the average value of a new residential building permit exceeded $200,000, an increase of approximately 40% in the past five years. The rise in new home construction also carried over to the existing home market where the median priced NJ home rose 17% in 2002 to $261,600. Nationally, the median priced home increased by 7%, to $161,800 . Thus the median NJ home value exceeded the national average by over $99,000, or by 62%.

NJ Residential Building Permits, No.



NJ Non-residential Building Permits, Billions $



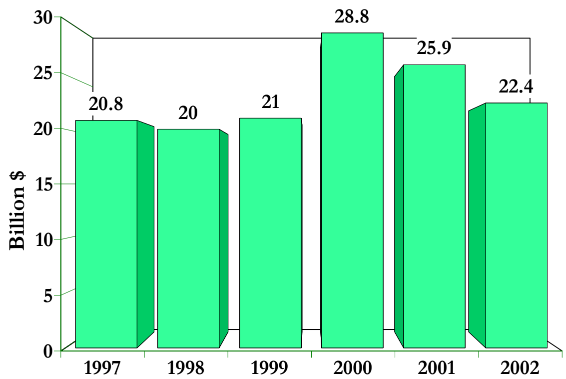
The non-residential construction market (office, commercial, industrial) endured the cyclical downturn relatively well with an estimated 5% year-over-year decline in the construction contracts. The office market suffered from corporate layoffs, restructuring and technology company failures during the year. Meanwhile, pre-leased office space was returned to the market as a number of companies revised their long-term office needs downward. As a result, office vacancy rates rose to approximately 15% in northern NJ. For 2003-04, recovery in office building will depend on expected gains in service employment.

International Trade....................

Exporting was the weakest NJ sector in 2002. From a year earlier, shipments from NJ manufacturers dropped 15% compared to a 10% decline in other Northeast states, and a 7% national decline. For 2002 exporting accounted for (only)

5.8% of Gross State Product down from a 7% share five years ago.

NJ Exports, in Billions $



NJ exporting was clearly affected by the bursting technology bubble and declines in business capital spending. Through the 3rd quarter, technology exports (computer, electronics and electrical machinery) fell 57%, machinery exports fell 19%, metals fell 33%, and transportation equipment exports dropped 9%. Processed food exports, typically a stable export product, dropped by 21%. Exports of chemicals, NJ's largest export good accounting for 33% of the total, was flat at $5.5 billion, while printing & publishing grew 7% and paper exports added 14%.

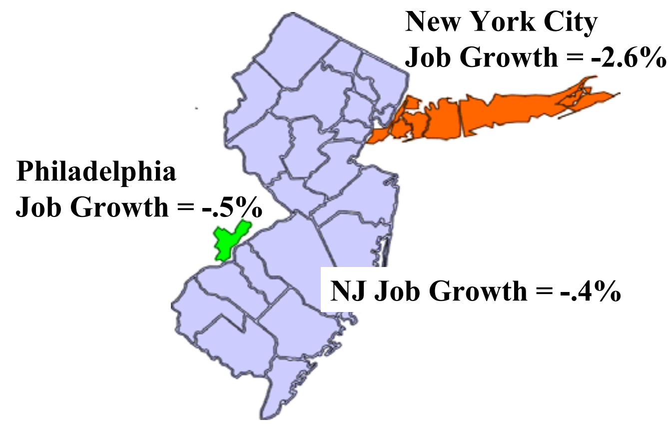
Fragile export markets overall provided few new opportunities for NJ manufacturers who also faced very weak domestic markets last year. The economies of the State's largest trading partners, the European Union (EU) and the Pac Rim, improved only marginally, while the threat of war in the Mid East and political and financial turmoil in Latin America reduced export prospects.

The Region ……………………………

By the end of 2002 employment losses in NYC dominated the regional economy. Total non-ag employment dropped .4% in NJ, .5% in Philadelphia, and 2.6% in New York City. This translates into a loss of almost 100,000 NYC jobs. The NYC unemployment rate rose to 7.6%, compared to 5.4% in NJ and 7.5% in the smaller Philadelphia job market.

Key industries affected the most included financial services that may have lost 30,000 jobs (although a portion of these jobs, temporarily or permanently relocated to NJ), restaurants, hotels, and air transportation. Lesser impacts were felt in business services, manufacturing and the printing & publishing industries. Each of these sectors has economic spillover effects on NJ's service and support industries.

Payroll Employment, % Change 2001-02



In spite of a weak 2002, a recent Report by the Federal Reserve Bank of New York concluded that the mid and long term outlook for NYC was positive based on a favorable industry mix, production efficiencies and quality of life. However, the NYC short-term outlook hinges on rebuilding a destroyed infrastructure, maintaining quality municipal services, safety and public transit in the face of a widening budget gap.

The Philadelphia metro region retains a higher percentage of manufacturing jobs than other Mid-East markets that were impacted by the national slowdown last year. Even though Philadelphia manufacturers report modest improvements, weakness in retail sales, commercial real estate markets and home sales provide little stimulus to the larger NJ economy.

For 2003-04 expect New Jersey to lead the region in economic and employment growth.

NJ Labor Markets ....

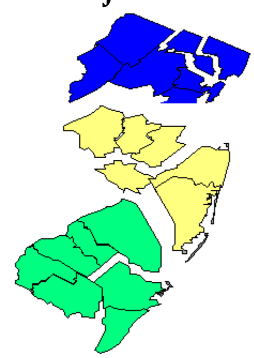
New Jersey's economy is built upon diverse, but inter-dependent labor markets. Each labor area offers a varying mix of industries and cost conditions that impact the overall NJ outlook. The northern labor areas (Bergen, Newark, Hudson and Passaic) that account for almost one-half (48%) of the State's jobs posted a cumulative loss of over 19,000 jobs, or –1%, in 2002.

Northern NJ labor markets were impacted by weakness in manufacturing which makes up a larger share of these markets than in the central and southern areas of the State. Downsizing in telecommunications contributed to weakness in northern labor markets. And, a wide range of northern NJ 'service' and 'transportation' sectors experienced job losses related to a weak New York City economy and softness in New York metropolitan area travel and trade.

Central NJ (Middlesex-Somerset-Hunterdon, Monmouth-Ocean, and Trenton) finished 2002 with a secure job base, a gain of 300 jobs, or .02%. The three labor areas, which account for 32% of Central NJ non-ag employment, have a stable base of pharmaceuticals and research and technology services, were aided by gains in home building.

Southern NJ (Atlantic-Cape May, Camden, and Vineland labor areas) gained a modest 1,100 jobs, or +.14%. The region benefited from a steady flow of visitors to Atlantic City, new casino and related construction activity, and an established base of service industries.

Payroll Employment, % Change 2001-02



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NJ Review & Economic Outlook: 2003 - 2004

(Current $ or Nos.)	1999	2000	2001	2002	**2003** (CEA Forecast)	**2004** (CEA Forecast)
Gross State Product (bill)	$332.96	$363.09	$380.56	$ 392.4	**$ 411.0**	**$ 434.3**
Personal Income (bill)	$ 289.4	$ 312.9	$323.7	$ 332.8	**$ 346.1**	**$ 362.4**
Retail Sales (bill)	$93.6	$101.9	$105.0	$ 105.0	**$ 107.9**	**$ 111.4**
New Vehicle Registrations (000's)	582.5	663.5	655.5	650.0	**618.0**	**645.0**
Non-Res. Construction Contracts (mill $)	$5,207.0	$5,812.1	$6,250.9	$5,910.0	**$ 5,800.0**	**$6,200.0**
Residential Building Permits (No.)	32,004	28,284	28,622	28,000	**28,000**	**28,750**
Consumer Price Index (1982-84=100)	177	182.5	187.1	190.8	**196.0**	**201.7**
(Real 1982$)						
Gross State Product (bill)	$188.1	$199.0	$203.4	$205.6	**$209.7**	**$215.4**
Personal Income (bill)	$163.5	$171.4	$173.0	$174.4	**$176.6**	**$179.7**
Retail Sales (bill)	$52.9	$55.8	$56.1	$55.0	**$55.0**	**$55.2**
Non-Res. Construction Contracts (mill $)	$2,941.8	$3,184.7	$3,340.9	$3,096.8	**$2,959.2**	**$3,074.6**
Employment:						
Total Non-Farm (000)	3,901.1	3,994.5	4,024.3	4,009.7	**4,046.4**	**4,097.0**
Manufacturing (000)	466.5	464.0	450.1	424.6	**414.6**	**408.0**
Service Producing Industries (000)	2,709.4	2,785.4	2,810.9	2,812.8	**2,852.9**	**2,896.0**
Government	577.6	588.9	600.7	608.0	**612.7**	**620.0**
Unemployment Rate (%)	4.6%	3.8%	4.2%	5.4%	**5.2%**	**4.9%**

Percent Change from previous year:	**1999**	**2000**	**2001**	**2002**	**2003**	**2004**
Gross State Product (Current $, bill)	5.1%	9.0%	4.8%	3.1%	**4.7%**	**5.7%**
Personal Income (Current $, bill)	3.8%	8.1%	3.5%	2.8%	**4.0%**	**4.7%**
Retail Sales (Current $, bill)	9.3%	8.9%	3.0%	0.0%	**2.7%**	**3.2%**
New Vehicle Registrations	5.8%	13.9%	-1.2%	-0.8%	**-4.9%**	**4.4%**
Non-Res. Construction Contracts	23.1%	11.6%	7.5%	-5.5%	**-1.9%**	**6.9%**
Residential Building Permits (No.)	2.1%	-11.6%	1.2%	-2.2%	**0.0%**	**2.7%**
Consumer Price Index (All Urban)	2.0%	3.1%	2.5%	2.0%	**2.7%**	**2.9%**
Gross State Product (82$, bill)	3.1%	5.8%	2.2%	1.1%	**2.0%**	**2.7%**
Personal Income (82$, bill)	1.8%	4.8%	0.9%	0.8%	**1.3%**	**1.8%**
Retail Sales (82$, bill)	7.2%	5.6%	0.5%	-2.0%	**0.0%**	**0.4%**
Non-Res. Construction Contracts (82$)	20.7%	8.3%	4.9%	-7.3%	**-4.4%**	**3.9%**
Employment:						
Total Non-Farm (000)	2.6%	2.39%	0.75%	-0.4%	**0.9%**	**1.3%**
Manufacturing (000)	-2.4%	-0.5%	-3.0%	-5.7%	**-2.4%**	**-1.6%**
Service Producing Industries (000)	3.6%	2.8%	0.9%	0.1%	**1.4%**	**1.5%**
Government	1.0%	2.0%	2.0%	1.2%	**0.8%**	**1.2%**

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The Office of Legislative Services provides nonpartisan assistance to the State Legislature in the areas of legal, fiscal, research, bill drafting, committee staffing and administrative services. It operates under the jurisdiction of the Legislative Services Commission, a bipartisan body consisting of eight members of each House. The Executive Director supervises and directs the Office of Legislative Services.

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The Office of Legislative Services Central Staff provides a variety of legal, fiscal, research and administrative services to individual legislators, legislative officers, legislative committees and commissions, and partisan staff. The central staff is organized under the Central Staff Management Unit into ten subject area sections. Each section, under a section chief, includes legal, fiscal, and research staff for the standing reference committees of the Legislature and, upon request, to special commissions created by the Legislature. The central staff assists the Legislative Budget and Finance Officer in providing services to the Appropriations Committees during the budget review process.

Individuals wishing information and committee schedules on the FY 2004 budget are encouraged to contact:

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