Minnesota Department of Finance

February 1999

February 1999 Economic Forecast

Highlights

Economy's Strength at Close of 1998 Boosts F.Y. 1998-99 Projected Ending Balance by $282 Million

Net general fund revenues for the 1998-99 biennium are now expected to total $22.526 billion, $285 million (1.3 percent) more than forecast in November. State expenditures for the current biennium are now projected to be $3 million more than previously anticipated. The combined revenue and expenditure changes increase the expected budgetary balance at the close of the current biennium by $282 million. A stronger than expected economy during the fourth quarter of 1998 was the source of much of the additional revenue.

Additional $450 Million Available for Next Biennium

The stronger economic outlook carries on through the end of the next biennium, raising the revenue forecast by $398 million to $25.036 billion. Revisions to expenditure projections for the next biennium cut expected spending by $52 million. The combined revenue and expenditure changes add $450 million to the projected F.Y. 2000-01 forecast balance. Although the forecast for each of the major tax sources increased, the income tax provided just over 60 percent of the additional revenue. Forecast spending for K-12 education was reduced by $63 million to reflect the sunset of a current program.

DRI Reduces Risk of Recession During 2000-01 Biennium to 30 Percent

In November DRI assigned a 45 percent probability to scenarios containing a recession during the 2000-01 biennium, and a 55 percent probability to the Control scenario in which the economic expansion continues into 2002. DRI's February outlook is more optimistic. The probability of a recession before 2002 is now at 30 percent and the Control scenario is now assigned a 60 percent probability. A scenario in which the economy outperforms the Control forecast during the next two years is given a 10 percent probability.

BUDGET SUMMARY

Balance for Current Biennium Increases by $282 Million

The forecast of general fund revenues has been raised by $285 million for the current biennium while projected spending has increased $3 million. These forecast changes increase the expected ending general fund balance to $1.235 billion.

F.Y. 1998-99 Forecast Change
($ in millions)

Higher Revenues	$285
Higher Spending	(3)
Total	***$282***

Outlook for 2000-01 Budget Improves by $450 Milllion

For the next biennium, revenues increase by $398 million and spending estimates are reduced by $52 million from November's projections, adding another $450 million to the ending balance for F.Y. 2000-01.

F.Y. 2000-01 Forecast Change
($ in millions)

Higher Revenues	$398
Lower Spending	52
Total	***$450***

Higher Balances Available for 1999 Rebate and 2000-01 Budget Proposals

With this forecast the expected available balance at the close of the current biennium is $1.235 billion. The total available forecast balance through June 30, 2001 is now $4.056 billion. Legislative action on current proposals to return all or part of the F.Y. 1999 balance as a tax rebate will reduce the amounts available for tax reductions or spending increases in F.Y. 2000-01.

Budget Summary - February Forecast
($ in millions)

	1998-99	2000-01
Beginning Balance	$1,995	$2,869
Revenues	22,526	25,036
Expenditures	21,652	22,544
Balance	2,869	5,361
Cash Flow Account	350	350
Budget Reserve	622	622
Dedicated Reserves	662	333
Available Balance	$1,235	$4,056

Forecast Gains Continue at Lower Levels in F.Y. 2002-03 Planning Estimates

For F.Y. 2002-03, higher revenues of $160 million and lower spending of $71 million combine to produce a forecast gain of $231 million over the November estimates. That gain increases Minnesota's general fund structural balance for F.Y. 2003 to $944 million, up $68 million from November's forecast. The structural balance, or the difference between current revenues and current expenditures, measures whether fiscal actions taken in one biennium will be sustainable in the next biennium. The combination of ongoing tax cuts and spending increases must remain less than $944 million per year if Minnesota's budget is to remain in structural balance through the close of the 2002-03 biennium.

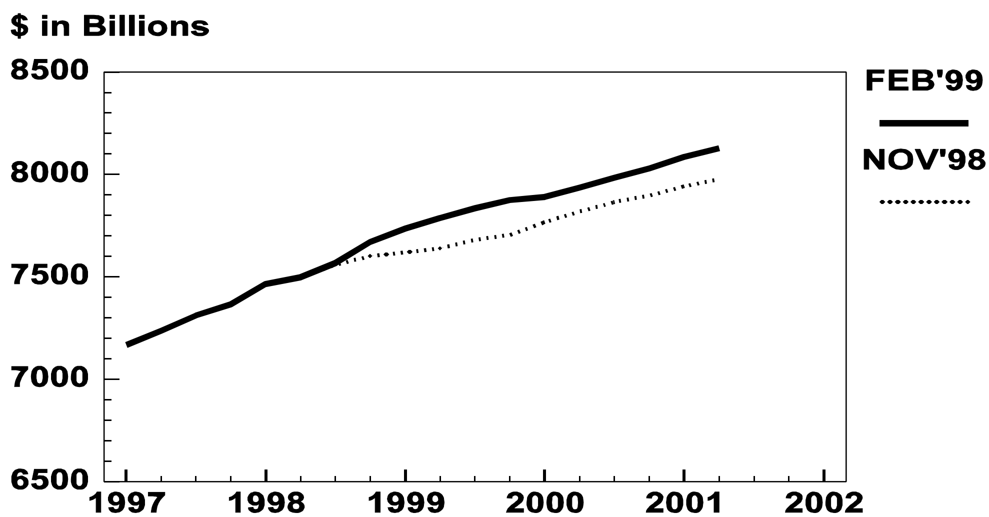
F.Y. 2002-03 Planning Estimates
($ in millions)

	November Forecast		February Forecast	
	F.Y. 2002	F.Y. 2003	F.Y. 2002	F.Y. 2003
Revenues	$13,092	$13,526	$ 13,212	$13,565
Less: One-time Tobacco	(243)	(121)	(265)	(137)
Expenditures	11,979	12,529	11,953	12,484
Structural Balance	$870	$876	$994	$944

Strong Fourth Quarter Growth Changes Economic Outlook

The U.S. economy finished 1998 much stronger than economists had expected. Auto sales and housing starts were particularly strong, and there is no evidence of an increase in inflation. Much of the rest of the world is in recession, but U.S. consumers continue to spend, and spending is increasing more than enough to offset the drag on the U.S. economy created by the loss of exports. When the U.S. Department of Commerce's fourth quarter 1998 advance estimate of real GDP growth was released showing growth proceeding at a 5.6 percent annual rate, everyone raised their forecasts significantly for 1999 and beyond.

Stronger Real GDP Growth Now Forecast

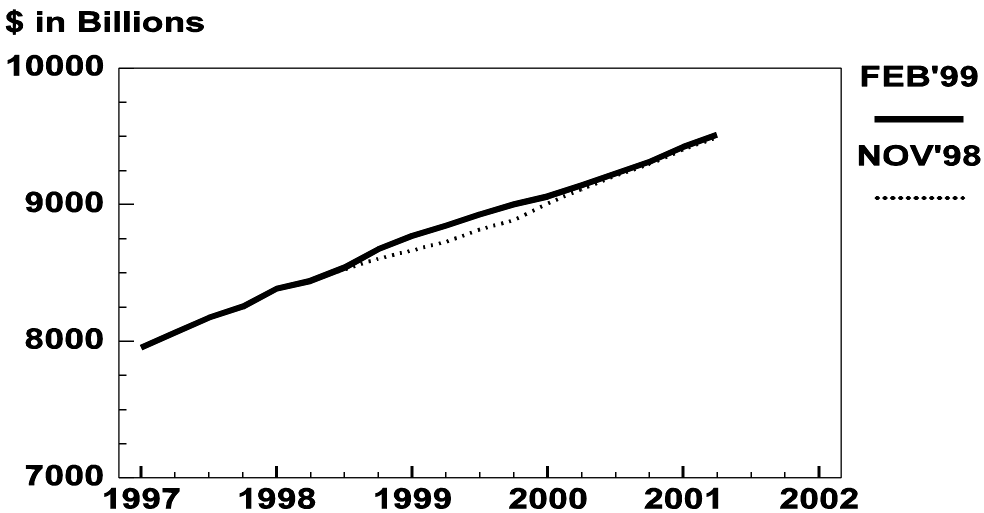


Minnesota's national economic consultant, Data Resources Inc., (DRI), was among those making very large forecast changes between November and February. November's DRI Control forecast called for real, inflation adjusted, GDP to grow at a 1.7

percent annual rate in 1999. In the February Control real growth is projected to proceed at a 3.4 percent rate, double the rate expected in November.

DRI has also changed the inflation outlook, reducing expected inflation by about 0.5 percentage points through 2003. Lower projected inflation rates limit growth in the nominal (current dollar) tax base. Lower inflation, coupled with a shift in the timing of a slight slowdown in the real economy, reduces the impact of the stronger growth projected for early 1999 on expected revenues in F.Y. 2000-01.

Little Change In The Outlook For Nominal GDP



Non-Dedicated Revenues up $285 Million in F.Y. 1998-99; $398 Million in F.Y. 2000-01

Unusually strong economic growth in late 1998 and a forecast for continued healthy growth in early 1999 have combined to raise the revenue forecast for the current and the coming biennium. The four major revenues account for about 83 percent of the growth in both the current biennium and in 2000-01.

Revenue Change from November '98 Forecast
($ in millions)

	F.Y. 1998-99	F.Y. 2000-01
Individual Income	$141	$241
Sales	1	23
Corporate	66	32
Motor Vehicle Sales	27	33
Major Taxes	235	329
Other	50	69
Total	$285	$398

An increase in expected individual income tax receipts accounted for about 60 per cent of the forecast changes in both biennia. Higher base level wages for 1998, upward revisions to forecast wage growth in 1999, and an increase in expected capital gains realizations in tax year 1998 were the primary sources of the additional revenues. Expected corporate income tax receipts increased, consistent with an increase in DRI's outlook for pre-tax corporate profits in 1998 and 1999. Net sales tax receipts in fiscal 1999 were artificially low due to an adverse judgement in a recent court case.

Expenditure Changes in Forecast Primarily Due to Technical Adjustments

State spending, including discretionary inflation is projected to be $22.544 billion, $52 million less than previously forecast. Savings from a technical correction to K-12 estimates, lower human services spending, and reduced debt service due to smaller assumed future capital budgets are partially offset by increases in tax refund interest estimates and technical corrections to base level spending information for F.Y. 2000-01 budget planning.

A complete version of the February, 1999 forecast can be found at the Department of Finance's World Wide Web site at -- www.finance.state.mn.us

ECONOMIC SUMMARY

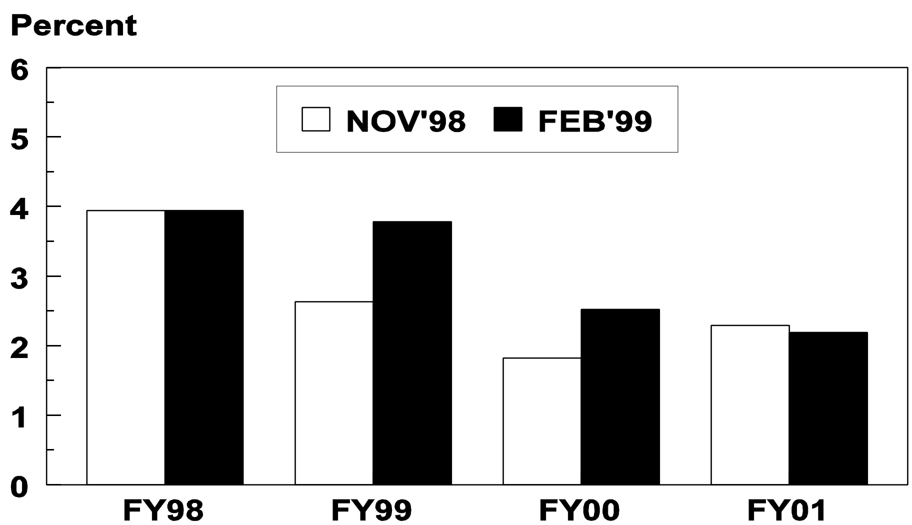
Forecasts are always works in progress, made with full knowledge that they will be revised each month as more recent evidence on the economy's progress becomes available. When the latest economic news is favorable, forecasts are increased, and when there is a preponderance of bad news, downward revisions to the outlook are likely. Usually the month's economic reports contain both good and bad news, and month-to-month changes in the overall outlook are small.

Recently that pattern has been broken. During the past three months reports on the U.S. economy have been almost uniformly favorable. An economy many thought might be burdened by last summer's stock market sell off, continued weakness in export markets, and the hint of a credit squeeze, has been performing admirably. Any final doubts were removed with the release of the fourth quarter 1998 GDP report which showed real GDP advancing at an annual rate of 5.6 percent. That strong real GDP growth, and the even stronger growth in fourth quarter final sales exceeded the expectations of even the most optimistic forecaster. U.S. consumers appear to have eliminated any lingering doubts about whether they will continue to increase their spending over the short term, and the U.S. economy seems once again to be positioned for an extended period of growth. Even with regional recessions in Asia and Latin America, and expectations for slower growth in Europe, the U.S. economy now appears capable of continuing its record of strong economic growth through the end of 1999 and beyond.

Minnesota's national economic consultant Data Resources Inc., (DRI), is among the forecasters who have made major changes to their outlook in recent months. In November, DRI forecast that real GDP would grow at an annual rate of 1.7 percent in 1999. For 2000, they projected real growth at an annual rate of 2.3 percent. Now, following the unusually strong fourth quarter growth, DRI has raised their forecast. Their February Control forecast for real GDP growth in 1999 is now 3.4 percent, double November's estimate. For 2000 expected growth has been reduced slightly to 1.9 percent. The Blue Chip Consensus Forecast has also been raised, although not as dramatically as DRI's. November's Blue Chip Consensus for 1999 was for 2.1 percent real growth. Now, the consensus forecast is for 2.9 percent growth in 1999, and 2.4 percent real growth in 2000. DRI has also reduced their inflation forecast. The CPI is now expected to increase at only a 2.0 percent rate during 1999, and a 2.3 percent rate during 2000, down 0.4 percent each year from November's forecast of 2.4 percent and 2.7 percent growth for 1999 and 2000, respectively.

Finance Department economists pointed out that a substantial portion of the changes in the projected growth rate for 1999 is already in the data. The extremely strong fourth quarter 1998 GDP results raised the base level from which future growth will occur, lifting the level for all of 1999 noticeably above previous estimates. The influence of the strong growth observed in the fourth quarter of 1998 on the forecast is highlighted when the outlook is examined on a fiscal year basis. In November the Control forecast for fiscal 1999 called for 2.6 percent growth. February's Control forecast expects growth at a 3.8 percent rate for the current fiscal year. However, even if the economy were to stagnate and there were to be no further growth during the last half of this fiscal year, the real growth rate for fiscal 1999 would be 3.2 percent, a full 0.6 percent more than was forecast in November.

DRI Raised Its Forecast For Real GDP Growth in F.Y. 1999



Consistent with the stronger economic outlook DRI has reduced the probability it assigns to a recession during the coming biennium. In November they assigned a 30 percent probability to a scenario containing a recession beginning in early 1999 and a 15 percent probability to a scenario with a recession beginning midway through 2000. DRI now notes that the "U.S. economy is showing few signs of an imbalance that would cause a recession." As a result they have changed their pessimistic scenario, moving their recession forecast back to late 1999 and early 2000. That scenario is currently assigned a probability of 30 percent. Their late recession scenario (probability 10 percent) contains a recession in 2002, but contains slightly stronger real growth during the coming biennium.

Members of the Council of Economic Advisors and Finance Department economists found no argument with DRI's assertion that the U.S. economy continues to be "the best economy in a generation." While some were more optimistic than DRI and others slightly less optimistic, everyone agreed that growth is likely to continue in the near future. Inflation is expected by all to move higher as oil prices stabilize and then begin to increase again, but no one expects a sudden, dramatic surge in prices. Foreign trade will remain a drain on the U.S. economy, but the council believes that domestic demand will be more than sufficient to offset those losses. Council members agreed that in the absence of a major financial shock or international event the current expansion should continue on and become the longest U.S. expansion in history early next year.

Council members believed that DRI's assessment of a 30 percent probability of a recession during the 2000-01 biennium was slightly pessimistic. A sudden drop in consumer spending, or an acceleration of price increases due to wage growth and higher import and commodity prices would raise concerns, but at this point there are no indications that either is likely to occur in the short term.

Minnesota's Council of Economic Advisors noted once again that it is appropriate to build the budget reserve when the economy is strong. Minnesota's budget reserve is now $622 million dollars, up significantly from earlier levels, but still only 2.7 percent of biennial spending, well below the long term goal of 5 percent of biennial spending recommended for the state.

ECONOMIC OUTLOOK

After slowing down last summer, consumers surprised most forecasters by going on a shopping binge as the holidays approached. Retailers had a good Christmas season, auto sales surged, and demand for household furnishings and appliances was strong. Many economists say the unanticipated spending reflected growing wealth and confidence.

Early indications are that much of last year's momentum will carry over, making 1999 a much better year than anyone thought possible a few months ago. Since November, DRI has doubled its forecast for 1999 real GDP growth to 3.4 percent while significantly lowering the probability of a recession. However, the improved outlook depends on continued robust household spending.

Recent spending gains reflect an apparent shift in consumer behavior. Strong auto sales suggest there is a renewed willingness to accumulate debt in order buy big ticket items. That appears to be based on consumer's belief that the current environment of rising wealth and income, low inflation, low interest rates, and readily available jobs will prevail farther into the future than expected a few months ago. DRI is like other observers in attributing the change in attitude to the stock market's quick rebound from last summer's correction. For example, *Business Week* indicates this may be the first time since the 1920s that household spending and the stock market were so closely linked.

DRI economists and others, including Federal Reserve Chairman Greenspan, think a stock market downturn could convince consumers they need to retrench. A pessimistic alternative to the February Control has a consumer led recession following loss of wealth and confidence in a market correction precipitated by declining profits in a slumping world economy. That scenario seems credible because last summer's experience showed that domestic financial markets are vulnerable to shocks from overseas. Continued deterioration in key foreign economies worries many analysts who think if bad news comes, it is quite likely to come from Latin America or Asia, or both.

Finance Department economists believe DRI and other forecasters are justified in expecting another market correction sometime this year. But, a recession does not have to follow. There is evidence that wage gains are now a strong and growing force behind consumer spending, making the economy less vulnerable to the whims of the market.

Problems in Brazil and Japan Are Unresolved

During the past several months, Brazil and Japan have accomplished almost none of the financial reforms needed to revive their faltering economies. Faced with massive losses of hard currency reserves, Brazil has been forced to let the real's value plunge while raising interest rates to more than 30 percent. But, a recent article in *The Economist* indicates these moves are not long term substitutes for reducing Brasilia's large fiscal deficit which frightens investors because of its inflationary potential. Absent meaningful reform, high interest rates needed to defend what is left of the real's value have now sent Brazil's economy into a recession which promises to be severe. As a result, imports from Brazil's neighbors will decline, slowing growth in most of Latin America.

Meanwhile, there is no good news from Japan. An overhaul of the bad-debt ridden financial system is moving very slowly. A government economic stimulus package intended to reverse the economy's consumer led free fall is generally considered to be only a temporary substitute for financial reform. And these timorous moves have been badly handled. In December, the goverment seriously miscalculated by announcing it would finance the fiscal package with bond sales. The markets responded by sharply raising long term interest rates. Frightened, the Ministry of Finance backed off, though it offered no substitute plan.

Short of expanding the money supply, a *Business Week* article indicates Japan has few viable options left. Fortunately, the Bank of Japan's recent move to drive short term interest rates to near zero may mean that it is reluctantly beginning to monetize Japan's enormous debt burden. Largely because of slow and ineffective policymaking, DRI expects Japanese real GDP to contract some 3.0 percent this year, further weakening other Asian economies as regional trade dwindles.

Without reforms, no one really knows where the bottom is for these two key economies, or how much damage their recessions will do to world trade. Japan and Brazil are, respectively, the world's second and eighth largest economies. Since both are now an increasing drag on major regional markets, U.S. exports to these areas could be significantly less than DRI expects. There is also the possibility of U.S. financial instability if international investors panic at the lack of reform and flee to the safety of Treasury bonds.

The Fed May Not Come To The Rescue Again

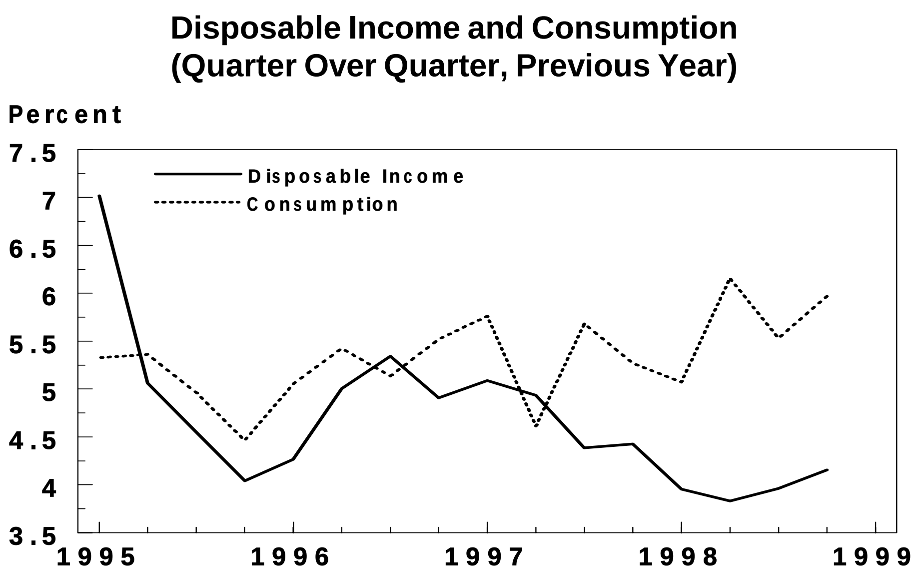
Last October and November, the Federal Reserve cut interest rates three times in a psychological move to stabilize financial markets. That worked very well and stocks rebounded to a new record only four months after the August downturn. But, once again, stocks are overvalued relative to likely growth in profits. DRI believes another correction will occur late this year.

Should stocks tumble, there may not to be another easing. Chairman Greenspan's recent remarks before Congress are widely interpreted as meaning he does not want to fuel another speculative bubble. His public statements also indicate Dr. Greenspan remains very inflation wary. Another easing could further stimulate consumer spending, raising the risk of accelerating inflation because of very tight labor markets.

Additional potentially inflationary stimulus is already in the pipeline. Beginning in the spring, there will be a delayed positive impact on spending from last fall's easing. This could save the economy from an unexpected worsening of the trade deficit, a mild stock market downturn, or some other shock. But, if drag does not materialize, the economy may become strong enough to rekindle inflation. For that reason, DRI and other forecasters expect the Fed's next move will be to tighten late this summer.

Consumption

Real consumer spending grew 4.8 percent in 1998, the best performance since 1986. Many economists believe the stock market's rapid recovery is the principal reason consumers have ignored record layoffs in 1998 as well as gloomy news from overseas. This behavior is remarkable because households are living beyond their incomes.



For several quarters, consumption has grown faster than disposable income, sending debt levels up. Economists did not anticipate such exuberant behavior, which is why their forecasts have been pessimistic.

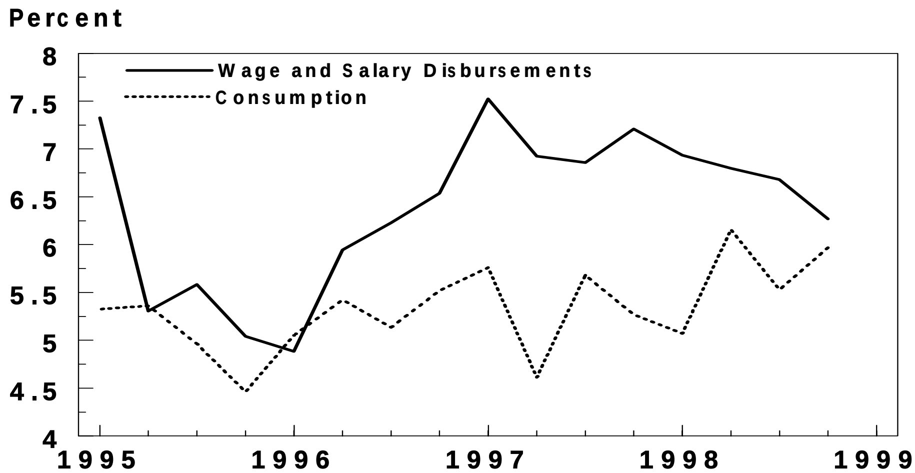
Spending has been growing faster than disposable income for several quarters. Consequently, household debt has reached a new high. As Federal Reserve Bank of St. Louis economists point out, that means households are committed to record levels of debt service in the future regardless of whether incomes meet expectations. Economists cannot fully explain such exuberant behavior, which is why their recent forecasts have been pessimistic.

Many forecasters including those at DRI now suggest consumers are responding to increases in stock market generated wealth. Finance Department economists believe rising wealth is contributing, but doubt that it alone fully explains recent household behavior. Only about 10 percent of households own some 85 percent of stocks. It is hard to believe that outlays of so few could generate all the recent observed increases in total spending which have surprised economists.

There also may be less wealth than suggested by the rebound in stock indexes. A recent *U.S. News & World Report* article indicates the S&P 500 hides significant losses. As of December 30, half of all stocks on the New York exchange had declined more than 10 percent for the year. And *Business Week* reports that just 33 stocks accounted for more than 75 percent of 1998's gains in the S&P 500 index. With gains so narrowly based, and with so few households holding significant equity positions, economists should not give stocks a leading role in explaining the current shopping splurge unless they believe consumers regard the market indexes as a bellwether for future economic conditions.

Probably more attention should be paid to wages. Finance Department economists, who regularly monitor income tax withholding, note that during the past few years inflation adjusted wages have increased significantly after remaining flat since the early 1970's. Moreover, wage gains have accelerated during the last year, and have occurred in most industries including traditionally low wage ones such as trade. So, it came as no surprise when the *Wall Street Journal* recently reported that for the first time in many years there are significant real wage increases among low wage workers, minorities, and immigrants.

Wage and Salary Disbursements and Consumption
(Quarter Over Quarter, Previous Year)



Wages have been rising faster than consumption because of steady gains in jobs and tight labor markets. For the first time in many years, there are significant wage increases among low wage workers, minorities, and immigrants.

These developments, the consequences of declining welfare rolls and tightening labor markets, must have led to significant increases in spending among low and lower middle income households who are numerous enough to generate observable changes in spending data. According to the March, 1998 Current Population Survey conducted by the Bureau of the Census, some 48 million of the country's 103 million households have annual money income less than $35,000. Rising wages and steady jobs in a near record length expansion should make these households more willing and able to borrow. In the view of Finance Department economists, that could account for recent rapid gains in consumption which were in part financed by record debt levels.

If this is true, then DRI and other forecasters should be more concerned about a sharp rise in the unemployment rate. That could easily happen if something causes employers to cut back hiring since layoffs are already occurring at a record pace as firms everywhere continue restructuring, and as manufacturers reduce their workforces in response to falling exports and rising imports.

Even if nothing has been overlooked, there is a considerable lack of precision in econometricians' measurements. DRI and other analysts do not have a reliable way of linking consumer behavior to household wealth, incomes, and other variables. For example, current econometric estimates of additional annual spending per extra dollar of wealth vary widely from 2.5 cents to twice that amount, indicating spending forecasts are subject to considerable uncertainty.

Investment

Goldman-Sachs economists say real business investment has increased at a 9.5 percent average annual rate during the past six years. But it would appear as though one of the strongest capital spending booms since the end of World War II is winding down. DRI's February Control scenario has business investment spending growth slowing from 11.9 percent in 1998 to 8.4 percent in 1999, and to 4.3 percent in 2000. In this view, the slowdown is inevitable because manufacturing capacity utilization is at a five year low and falling, profits will weaken in 1999, and Y2K costs are exceeding expectations. As a result, some capital expansion plans are being scaled back, and some money intended for new plant and equipment is being diverted to Y2K problems. It is also likely that after years of dealing with tight labor markets, many firms are running out of ways to substitute capital equipment for hard to find workers.

Mild weather in 1998 helped the housing sector set new records for sales of both existing and new homes. Year-end sales were so strong that inventories of new single family units reached all-time lows. But, the weather was only partly responsible because the underlying fundamentals were also very good. DRI's proprietary housing affordability index indicates declining mortgage rates have reduced the cost of buying a new house to its lowest point since 1972. That, plus the strong economy has led to rising home ownership and expanding demand for larger homes and second homes. DRI expects 1999 will be another good year for housing because builders say they will replace depleted inventories and because a recent University of Michigan consumer survey indicated 89 percent thought it was a good time to buy another house.

Brisk auto sales and a strong Christmas season prevented a buildup of unwanted inventories. Lack of excessive stocks should keep new orders for goods strong during early 1999. Later in the year, the February Control scenario assumes there will be some extra stocking as a hedge against supply disruptions caused by Y2K problems.

Government

When its budget moved into surplus in 1998, the federal government became a net supplier of funds to the financial markets for the first time since 1969. DRI expects the federal surplus will gradually decline from $117 billion in 1999 to about $70 billion in 2001 because of tax cuts, reduced capital gains realizations, and spending increases. The February Control assumes that much of the federal surplus will be used to pay down the national debt and that discretionary spending primarily for defense will exceed the caps established by the 1997 Balanced Budget Act. State and local governments are in surplus also, so there will be no net government borrowing, a significant factor in the outlook for continued relatively low interest rates in the Control scenario.

However, DRI warns that a recession could easily change the federal, state, and local government's fiscal outlook. Their pessisimic scenarios indicate a slump in the U.S. economy would eliminate most of the projected government surplus over the forecast horizon going out to 2003.

International

After raising interest rates to more than 30 percent and spending some $45 billion in hard currency reserves in an effort to defend its currency, Brazil first devalued and then let the real float downward in January. Brazil's actions seemed to surprise U.S. Treasury officials and renewed concerns about the international financial system and the world economy. As a result, Latin America's problems may dominate the international economic news in 1999 just as Asia's did last year. The February Control assumes that while the Brazilian government and the International Monetary Fund are unable to abate the unfolding crisis, no global financial panic results.

Brazil, Latin America's largest economy, is now in a potentially serious recession. As the recession develops, economists believe Brazil's large market will absorb fewer imports from its neighbors, weakening their economies. Argentina will be particularly hard hit. The U.S. trade deficit will worsen as a result since some 20 percent of our exports are to Latin America, though only about 2 percent are to Brazil itself.

News of the devalued real and its floating a day later briefly unsettled financial markets which had calmed as some Asian countries seemed to get a few of their immediate problems under control. DRI reports that during the last few months financial markets in Korea, Thailand, and the Philippines have been more stable and exporters are getting working capital needed to increase production.

However, major structural problems still exist in the Asian region. While Japan's difficulties are well known, China's receive relatively little media attention. China's problems are similar to Japan's though its economy is still growing. Chinese officials continue to deny they will devalue the renminbi. But DRI believes a devaluation will occur in late 1999, possibly setting off a new round of international financial instability. Some economists doubt there will be a devaluation because China needs to stimulate domestic demand, not its export sector which is generally the low cost producer in world markets. This view is supported by a recent *Business Week* article describing the Chinese government's efforts to stimulate the economy by spending on infrastructure.

Monetary

Brazil's problems quickly diverted media attention from the euro's successful introduction on January 1. It will be years before economists know the full implications of the most ambitious monetary experiment since the Bretton Woods agreement in 1945. But even though thinking about the impacts is in its infancy, some things seem clear.

The U.S. has more to gain from the euro's success than its failure. European firms will realize significant savings from eliminating currency conversion costs and exchange rate risk, making them more competitive in world markets. As a result, analysts believe some sales by U.S. firms will be lost to European rivals, but the losses are likely to be more than fully offset by increased exports to a faster growing Continental economy.

Success for the euro means that, over the next several years it will join the dollar as the world's second major reserve currency held by central banks and other financial institutions for use in international transactions. At present, Newsweek reports about one-half of world trade is denominated in dollars.

A successful euro would end European fragmentation which kept the pound, the mark, the French franc, and others from becoming significant competitors of the dollar as reserve currencies. The principal problem was that the economies of the separate countries are too small to credibly back a large number of outstanding potential claims for goods and services by foreigners. In contrast, the 11-country European Economic Union is approximately the size of the U.S. in productive capacity. That, theoretically, should make foreigners willing to hold large quantities of euros provided there are no excessive exchange rate risks.

If the euro becomes established, U.S. monetary policy will be affected. In setting U.S. interest rates, the Federal Reserve will need to coordinate with the new European Central Bank if it wants to avoid exposing international transactions to the risks of instability in the euro-dollar exchange rate. Because of the Union's importance as a U.S. export market, the euro-dollar exchange rate will be a more central consideration than were separate rates with nearly a dozen smaller countries each pursuing independent monetary policies. In effect, a certain amount of independence in setting U.S. monetary policy will be lost.

Analysts are beginning to think about the consequences of the euro's failure. What seems the most immediate risk is that the euro will be initially accepted as a reserve currency only to have something to go wrong which causes it to be abandoned for dollars. A flight to safety in dollars and dollar denominated assets could destabilize U.S. financial markets. In December, DRI included this scenario in a pessimistic alternative to its Control scenario for the first time.

The new European Central Bank's first test may not be long in coming. Growth is slowing sharply in Germany because of slumping export sales. According to the Wall Street Journal, German leaders have called for an interest rate reduction. But lowering rates would drive investors out of the euro, contrary to what analysts believe is the Bank's primary objective at this time.

Inflation

Inflation is very much subdued with consumer prices rising just 1.6 percent in 1998, the smallest annual increase since 1965. While not good for producers, weak oil and farm prices have had a major role in restraining increases in the cost of living. And by preserving the purchasing power of wage gains, low inflation is contributing significantly to strong consumer spending.

However, wage gains have accelerated as the unemployment rate has dropped, strongly suggesting that inflation is not dead. Price increases should speed up in 1999 as now very tight labor markets push wages upward even faster. If that happens, economists do not believe a still inflation conscious Federal Reserve is likely to pre-emptively lower interest rates again the way it did in 1998 should financial instability develop, or if the trade deficit grows unexpectedly.

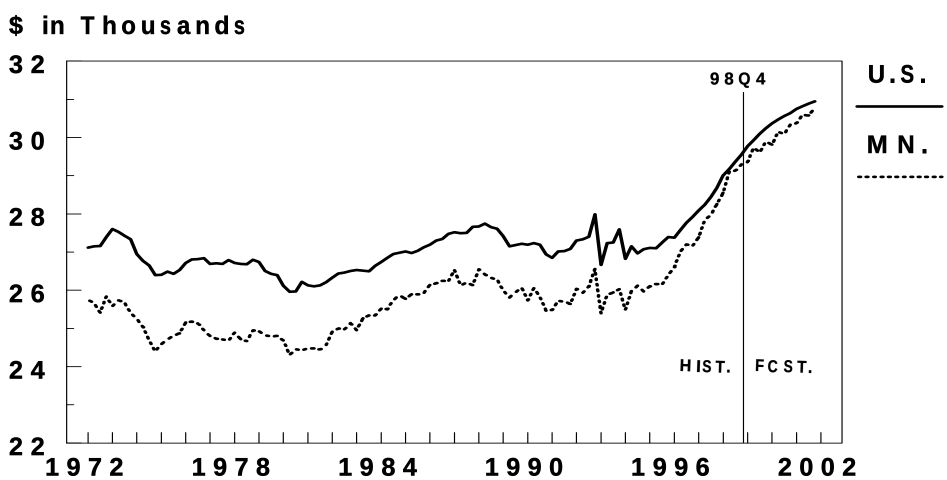
MINNESOTA OUTLOOK

The new Minnesota outlook reflects DRI's February Control scenario as well as additional historical data for 1998 which has become available since the last forecast. A full twelve months of preliminary data shows Minnesota's payroll employment increased 2.5 percent in 1998, the same as forecast in November. Using preliminary data from 1998's first two quarters, total wages are now forecast to rise 7.6 percent, up from November's 6.6 percent. For the U.S., DRI estimates 1998 employment will rise 2.5 percent, the same as in November. Total U.S. wages are expected to rise 6.7 percent, up slightly from 6.6 percent previously.

In 1999, Minnesota jobs are projected to rise 1.9 percent, compared to 1.4 percent forecast in November. February's forecast is for total wages to increase 5.5 percent, up from 5.1 percent. In comparison, DRI expects U.S. employment to increase 2.0 percent, up from 1.3 percent in November. Total wages will rise 6.0 percent, up from 5.4 percent.

If the national February Control scenario comes true and Minnesota tracks it as Finance Department economists expect, a slowdown will begin later this year and extend into 2000. Statewide employment will expand by 1.3 percent in 2000 while total wages rise 4.6 percent. However, this outlook is contingent upon employers being able to find enough workers to fill available jobs. Continuation of currently tight labor market conditions makes the outlook subject to additional uncertainty which cannot be quantified.

Real Wages Per Job, U.S. and MN



In both the U.S. and Minnesota, real wages per job are forecast to continue their unprecedented three year surge. This outlook assumes firms will be able to generate revenues needed to pay higher wages.

Minnesota Real Wages

In 1998, Minnesota real wages per job followed the U.S. in continuing an unprecedented steep climb for the third year in a row. Since the last quarter of 1995, this measure has increased 11.0 percent in Minnesota compared to 7.9 percent for the U.S. Finance Department economists believe that performance reflects the tightest labor markets since the 1960's.

The February Control forecast is for rapid increases in real wages through the end of 2001 in both the U.S. and Minnesota. This depends on continued labor market tightness and low inflation. But, perhaps more important, the outlook assumes firms will be able to generate sufficient revenues to pay higher wages.

Taconite

Last year's news of surging steel imports from Japan and Russia caused widespread concern about potential cutbacks in Minnesota taconite production. Although the Japanese have apparently reduced their shipments recently and Russia has promised to, the outlook is not clear because changes in domestic steel production trickle down to demand for Minnesota taconite only after a long lag. Inventories of ore and finished product as well as the availability and price of minimill products and foreign ore greatly complicate the relationship between the taconite industry and steel producers.

Currently, Finance Department economists think Minnesota taconite production this year is likely be 10 to 12 percent less than in 1998. That would translate into a somewhat smaller decline in the workforce through layoffs and attrition. These assumptions were built into the February forecast though they could be pessimistic if the U.S. economy turns out to be as strong as DRI expects.

Manufacturing

The U.S. manufacturing sector has been hard hit by the worldwide economic slump. As exports slipped, and overseas devaluations led to rising imports, U.S. manufacturers reduced their workforces on a seasonally adjusted basis by about 240,000 jobs or 1.3 percent since first quarter, 1998. DRI is forecasting that losses will continue at least through the end of 2001.

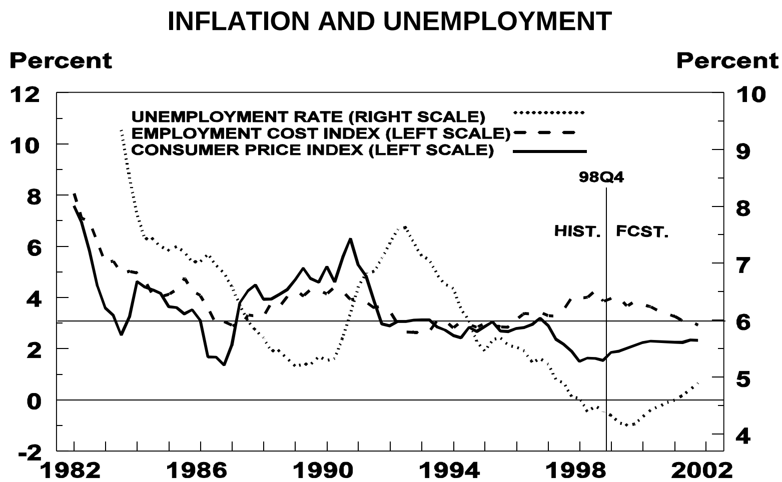
Over the same historical period, Minnesota manufacturing employment has experienced only a 0.2 percent decline, which has left the jobs numbers essentially flat. Finance Department economists expect the same for the future, with neither significant overall gains or losses through 2001.

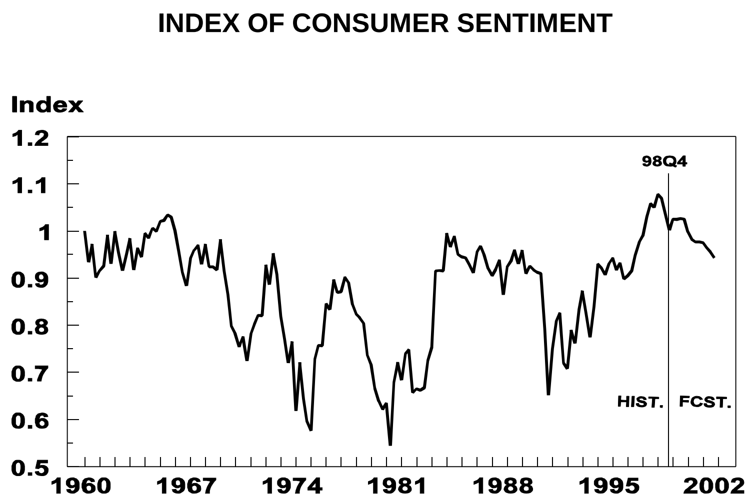
The forecast implies that Minnesota's share of total U.S. manufacturing jobs is projected to rise much as it has in the past as U.S. employment shrinks. Over the forecast horizon, this performance makes an important contribution to jobs and incomes. Clearly there is some risk in an outlook which says local manufacturing will survive better than its national counterpart in an environment of intensifying international competition which could change historic trends.

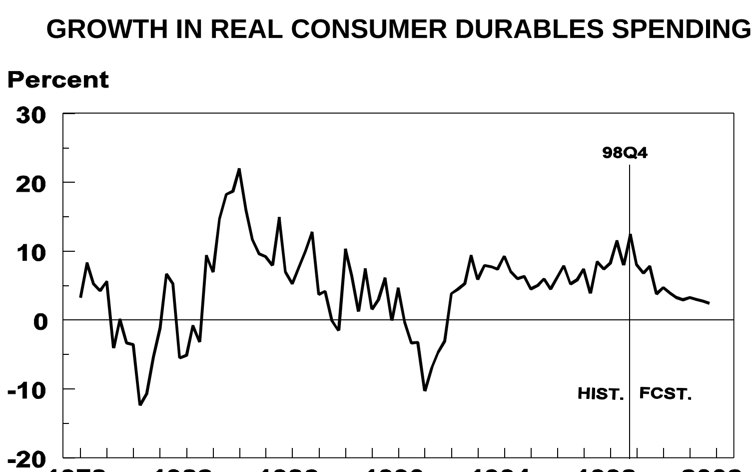
Agriculture

Minnesota farmers are expected to face a difficult year in 1999. Brazil's devaluation will allow it to take a larger share of the world soybean market, and soybean prices are likely to remain at or near 20 year lows. USDA's chief economist is now forecasting that new crop soybeans might be priced as low as $4 per bushel during next fall's harvest. USDA is also estimating that lower commodity prices brought on by reduced world demand and global competition are likely to reduce grain and soybean farmers' 1999 incomes to levels as much as 25 percent below their 5 year averages. Livestock and poultry farmers will benefit from lower grain prices, but current market prices for hogs will continue to depress incomes in that sector. The Minnesota forecast includes no federal disaster relief payments in 1999, although it does include a further acceleration of production flexibility contract payments.

Selected National Economic Indicators

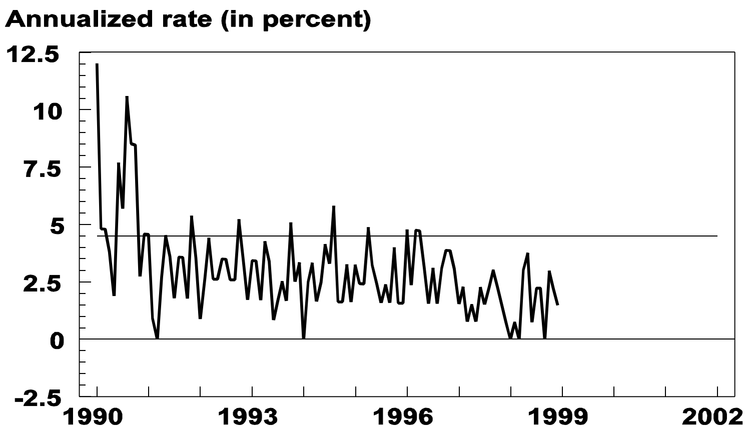




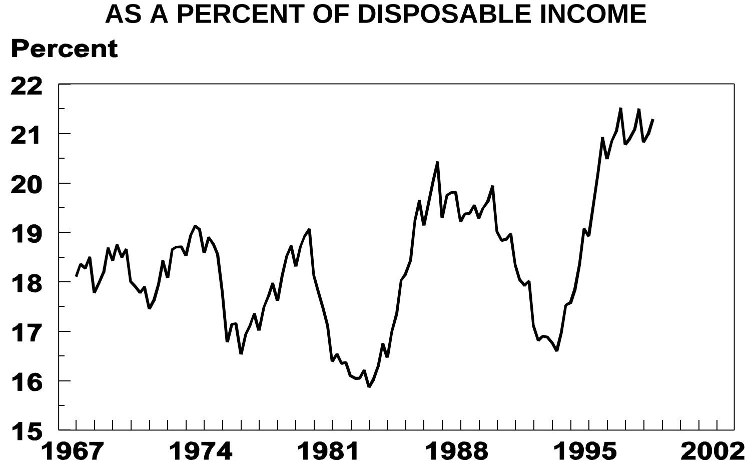


Selected National Economic Indicators

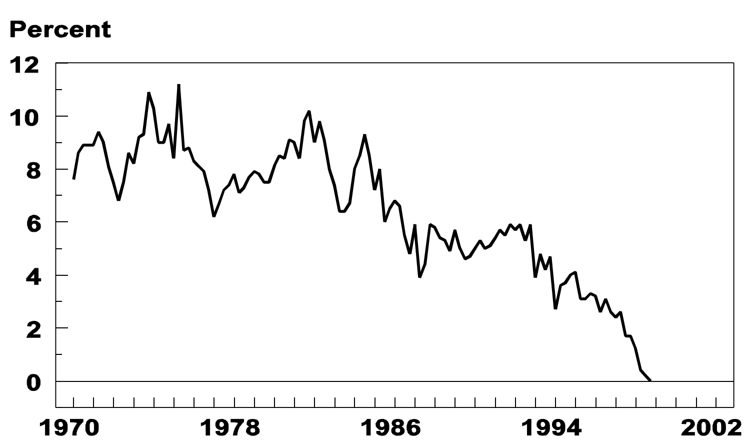
CONSUMER PRICE INDEX



INSTALLMENT CREDIT OUTSTANDING
AS A PERCENT OF DISPOSABLE INCOME

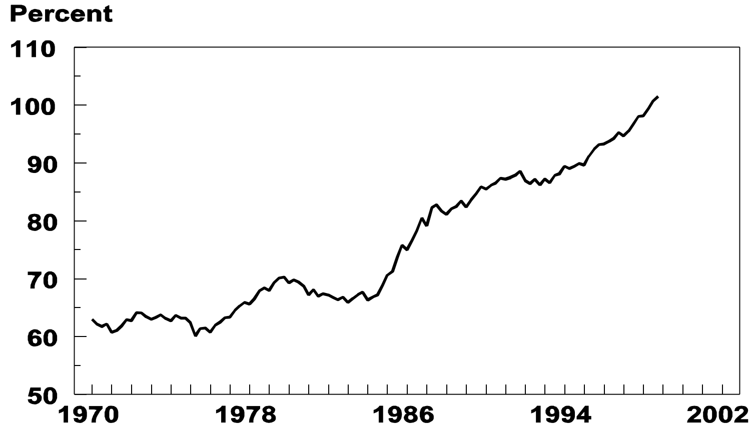


SAVING AS A FRACTION OF DISPOSABLE INCOME

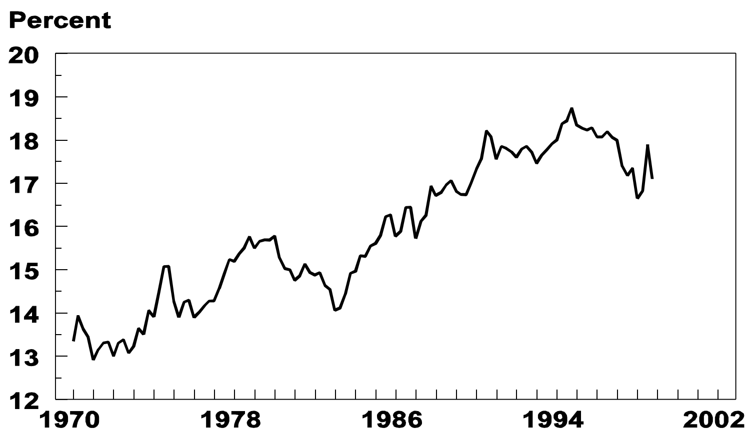


Selected National Economic Indicators

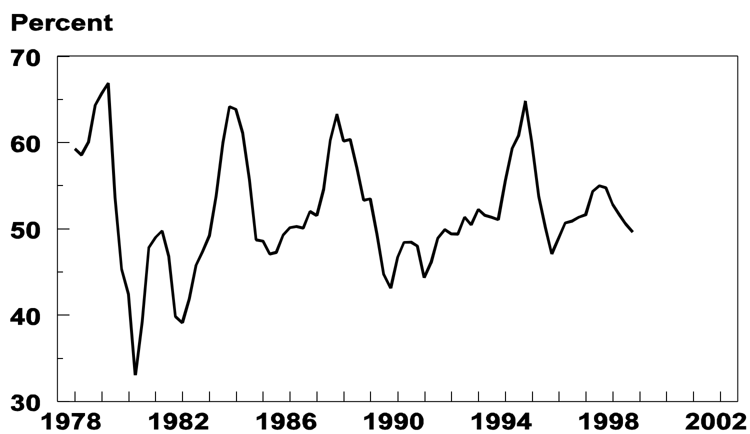
HOUSEHOLD FINANCIAL LIABILITIES
AS A SHARE OF DISPOSABLE INCOME



HOUSEHOLD FINANCIAL LIABILITIES
AS A SHARE OF NET WORTH

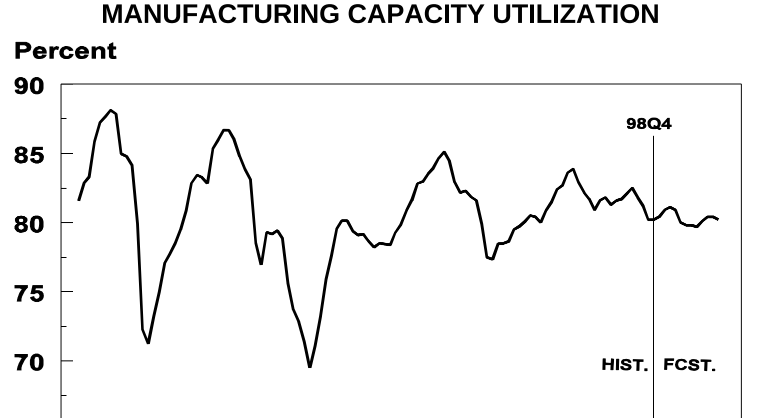


PROPORTION OF COMPANIES
RECEIVING SLOWER DELIVERIES

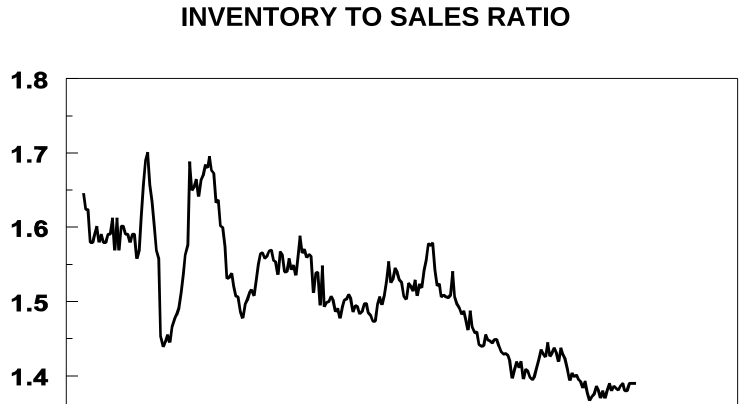


Selected National Economic Indicators

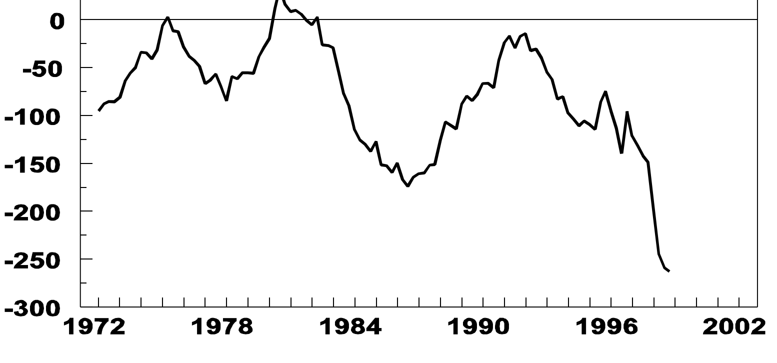
MANUFACTURING CAPACITY UTILIZATION



MANUFACTURING AND TRADE
INVENTORY TO SALES RATIO

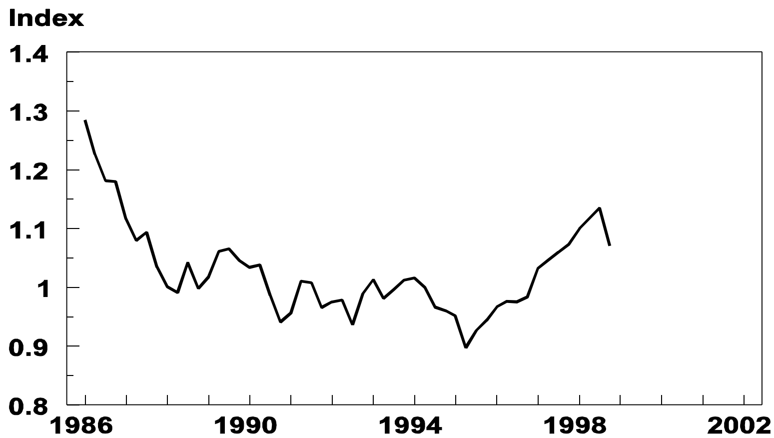


U.S. TRADE BALANCE ($1992)

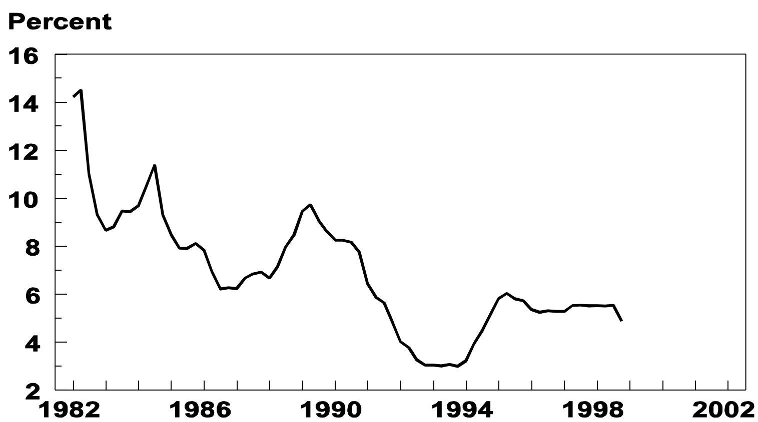


Selected National Economic Indicators

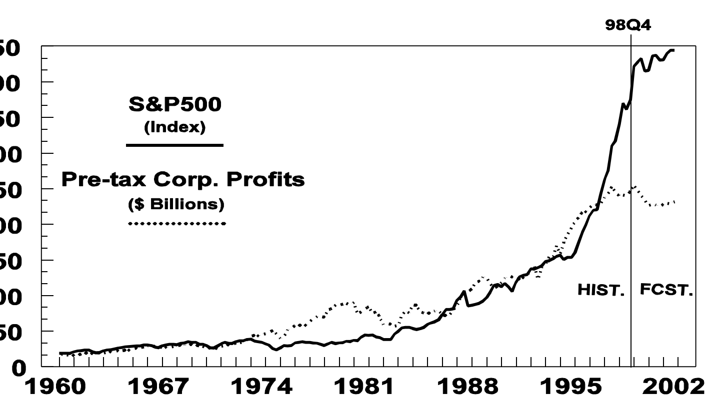
TRADE-WEIGHTED VALUE OF THE DOLLAR



FEDERAL FUNDS RATE



CORPORATE PROFITS AND THE STOCK MARKET



Forecast Update and Outlook

F.Y. 1999 Ending Balance Now Estimated At $1.235 billion

Projected F.Y. 1999 revenues and other resources have increased by $285 million for the current biennium while projected expenditures have increased by $3 million. Together, these changes increase the projected available balance for the biennium from the $953 million forecast in November to the current forecast of $1.235 billion.

F.Y. 1998-99 -- Current Biennium
Change from November 1998 Estimates
($ in millions)

	November	February	Difference
Beginning Balance	**$1,995**	**$1,995**	**$0**
Revenues	22,241	22,526	285
Expenditures	21,649	21,652	3
Cash Flow Acct	350	350	0
Budget Reserve	622	622	0
Property Tax Reserve Acct	330	330	0
Tax Reform & Reduc Acct	200	200	0
Dedicated Reserves	132	132	0
Available Balance	**$953**	**$1,235**	**$282**

An increase of $234 million in the four major taxes accounts for 82 percent of the revenue increase. Of this amount, $141 million comes from higher individual income tax collections. Estimated F.Y. 1999 spending is up $2.5 million from the November forecast.

F.Y. 2000-01 Budget Forecast

This section contains estimates of revenues and expenditures for the F.Y. 2000-01 budget that will be enacted this session. Total F.Y. 2000-01 forecast revenues are up $398 million from the November estimates. Projected individual income tax collections account for over 60 percent of this increase.

Expenditure estimates fall by $52 million in the February forecast, including $63 million in technical corrections and forecast changes in K-12 education, a $15 million decline in health care, and a $14 million decrease in debt service. These savings are partially offset by higher projected spending in state agency operations and other spending areas, including a $17 million increase in tax refund interest.

F.Y. 2000-01 Forecast
Change from November 1998 Estimates
($ in millions)

	November	February	Difference
Beginning Balance	**$2,587**	**$2,869**	**$282**
Revenues	24,638	25,036	398
Expenditures	22,596	22,544	(52)
Subtotal - Forecast Changes			*$450*
Cash Flow Account	350	350	0
Budget Reserve	622	622	0
Tax Reform & Reduc Acct	200	200	0
Dedicated Reserves	133	133	0
Ending Balance	**$3,324**	**$4,056**	**$732**

The F.Y. 2000-01 revenue forecast is based on DRI's February 1999 Control forecast. For planning purposes, revenues are projected based on current tax laws and rates; expenditure projections include discretionary inflation increases of 2.5 percent per year.

F.Y. 2002-03 Planning Estimates

The projected ending balance in F.Y. 2002-03 is up $963 million from the November forecast, of which $732 million is the balance from the prior fiscal year (that would not be available if used in F.Y. 2000-01 for tax cuts or new spending). Only $231 million of this balance reflects changes in F.Y. 2002-03 revenues and expenditures. State revenues for the period are now expected to be $160 million higher than projected in November.

Projected spending for F.Y. 2002-03 is down $71 million from the November estimates, largely reflecting similar technical corrections and forecast adjustments to those made for F.Y. 2000-01. Significant variances from this pattern occurred in health care, which increases $20 million, and debt service, which is forecast $45 million lower, largely due to the change in assumptions about the size of future capital budgets. Relatively small changes in forecast costs in other areas, including a $2 million decrease in estimated discretionary inflation, account for the remaining net difference in spending.

F.Y. 2002-03 Planning Estimates
Change from November 1998 Forecast
($ in millions)

	November	February	Difference
Beginning Balance	**$4,629**	**$5,361**	**$732**
Revenues	26,617	26,777	160
Expenditures	24,508	24,437	(71)
Subtotal - Forecast Changes			*$231*
Cash Flow Account	350	350	0
Budget Reserve	622	622	0
Tax Reform & Reduc Acct	200	200	0
Dedicated Reserves	133	133	0
Ending Balance	**$5,433**	**$6,396**	**$963**

Planning estimates of current law revenues and expenditures for F.Y. 2002-03 are presented as part of budget development to identify longer term impacts. Revenue planning estimates are based on DRI long term forecasts for calendar years 2001-2003. Expenditure estimates assume current laws and policies updated for caseload, enrollment and other forecast variables in all major program areas. Expenditure estimates also include the potential cost of discretionary inflation of 2.5 percent per year. The estimates do not reflect the Governor's budget recommendations, nor anticipate any legislative changes.

Revenue Forecast
F.Y. 1998-99

Current general fund resources for the 1998-99 biennium are now expected to total $22.526 billion, up $285 million, (1.3 percent), from November's forecast. The surprisingly strong economic growth reported for the fourth quarter of calendar 1998 and further improvements in the economic outlook for the first half of calendar 1999 explain much of the addition to the forecast. About one third of the forecast increase comes from the current positive variances in year-to date revenues.

Revenues from the four major taxes are expected to exceed November's forecast by $234 million, with the individual income tax providing $141 million or about 60 percent of the total increase. Net corporate income tax receipts are expected to be up by $66 million from November's levels, while the motor vehicle sales tax is up $26 million from previous estimates. The sales tax was almost unchanged, increasing by $1 million. Other tax and non tax revenues were $46 million more than forecast in November.

F.Y. 1998-99 Revenue Forecast
($ in millions)

	FY96-97 Biennium	FY 98	FY 99	FY98-99 Biennium
Revenues				
Individual Income Tax	8,904	4,747	5,137	9,884
Sales Tax	5,914	3,252	3,415	6,666
Corporate Income Tax	1,383	752	774	1,526
Motor Vehicle Sales Tax	783	445	461	906
Four Major Taxes	16,984	9,195	9,787	18,982
Other Revenues	1,842	1,063	1,090	2,153
Tobacco Settlement	--	--	461	461
Net Non-dedicated Revenue	18,826	10,258	11,338	21,596
Other Resources	777	486	444	930
Current Resources	19,603	10,744	11,782	22,526

Net non-dedicated revenues for the 1998-99 biennium are now projected to grow by 14.7 percent over 1996-97 biennial levels, after taking into account the property tax rebates approved in the 1997 and 1998 legislative sessions. After adjusting for revenues attributable to the tobacco settlement growth over the previous biennium is now expected to be 12.4 percent. Biennial growth rates for the income tax and the sales tax are now expected to be 11.0 percent and 12.7 percent respectively.

Individual Income Tax

Individual income tax receipts for the 1998-99 biennium are now forecast to total $9.884 billion, up $141 million (1.5 percent), from November's forecast. Much of this change will come through higher than previously projected settle-up payments accompanying tax year 1998 individual income tax filings and lower than projected tax year 1998 refunds. The year to date positive variance for the income tax is $36 million. However, it now appears estimated tax payments processed through February will exceed November's forecast by more than $70 million, $37 million more than at the end of January.

Higher wages were the source of nearly one-half of the forecast increase. Tax year 1998 wages are now believed to have grown at an annual rate of 7.6 percent, a full 1.0 percent more than forecast in November. Preliminary data on Minnesota wages during the first two quarters of 1998 provided by the U.S. Department of Commerce, and withholding tax receipts support that revision to 1998 wage growth. A further increase in the projected economic growth rate for early 1999, coupled with the higher wage base produced by the economy's strong fourth quarter growth, creates further wage and withholding tax receipt growth in early 1999 beyond that forecast in November.

Much of the remaining increase in individual income tax revenue came from a change in the forecast of capital gains realizations. Fourth quarter estimated tax payments now are known, and they exceeded November's estimates by more than $70 million. While there are a number of possible explanations for the increased payments, a larger than previously projected increase in 1998 capital gains realizations was considered to be the most likely, and the realizations forecast was raised accordingly. Capital gains are now projected to grow at a 20 percent rate in 1998, up from the 14 percent growth rate used in the November. Preliminary evidence from the 1997 sample of Minnesota tax returns indicated that 1997 capital gains realizations in this state grew at a 33 percent rate, slightly below the 40 percent rate observed nationally. In this forecast the national growth rate for 1997 was used to set the base level of realizations from which 1998 growth would proceed. This further increased expected capital gains realizations for 1998.

Even though stock market averages continued to grow in 1998, there is no guarantee that capital gains realizations kept pace. A Finance Department analysis of capital gains distributions from the nation's largest mutual funds, for example, found that distributions actually declined by 16 percent from levels observed in 1997, and last summer's dip in the stock market and the continuing volatility in individual stocks has created an environment where traders may have losses to offset some or all of their realized gains. Net capital gains realizations now appear to have nearly tripled since

1994, and it would not be surprising if the growth rate of realizations slowed dramatically or even fell in the future. Capital gains have grown to almost 10 percent of taxable income in recent years, and their volatility increases the uncertainty of the revenue forecast.

The large increase in estimated tax payments could not be fully explained by the increase in capital gains. Growth rates for pension incomes and IRA distributions were also increased by small percentages from the growth rates used in November to raise final liability to a level more in keeping with observed estimated payments. In addition, an off-model adjustment which added $18 million to partnership income was made. Farm income for 1998 and 1999 was decreased from November's levels reflecting reports of weaker farm incomes and USDA's lower forecast for farm income in 1999. No federal disaster relief package is assumed to be available in 1999. With the exception of capital gains, adjusting the composition of 1997 income to be consistent with the preliminary sample results created no major changes in the forecast.

Technical changes, including a change in the ratio of final receipts to final liability and a slight revision in the timing of estimated tax receipts added $16 million to F.Y. 1999 revenues. Property tax rebates totaled $435 million in F.Y. 1998 and are assumed to total $450 million in the current fiscal year. The total property tax rebate is assumed to be paid out over four fiscal years and is expected to total $899 million.

Sales Tax

Net sales tax receipts for the 1998-99 biennium are now expected to reach $6.666 billion, $1 million more than forecast in November. A $24 million increase in projected gross sales tax receipts is almost completely offset by a $23 million projected increase in sales tax refunds. Much of that increase in sales tax refunds was attributable to a single court decision and is non-recurring. Gross sales tax receipts for the fourth quarter of calendar 1998 were $14 million below the level forecast in November.

Projected growth rates for spending on consumer durables, business equipment, and construction, were the source of the additional sales tax revenue. DRI's February forecast shows stronger growth for all three of these components of Minnesota's sales tax base. Spending growth on the remainder of the items included in the sales tax base remained close to the rates anticipated in November. Sales tax receipts for fiscal 1999 were increased by $9 million to reflect a change in filing status for some small firms with rapidly growing sales. As taxable sales exceed certain threshholds, annual filers are required to file quarterly and quarterly filers are required to file monthly. By accelerating payments, these changes in filing status result in a one-time revenue gain to the state.

Corporate Franchise Tax

Net corporate income tax receipts for the current biennium are now estimated to total $1.526 billion, $66 million (4.6 percent) more than forecast in November. Much of that additional revenue has already been collected. Year to date corporate income tax receipts exceed levels forecast in November by $45 million.

Expected F.Y. 1999 corporate income tax refunds were reduced by $14 million, to reflect changes in the timing and composition of the payments required under the Rural American Bank case. DRI's forecast for tax year 1998 corporate profits was revised up by 2 percent to be consistent with the stronger economic growth reported in the fourth quarter.

Motor Vehicle Sales Tax

The sales tax on motor vehicles is now projected to total $906 million during the 1998-99 biennium, $26 million (3 percent) more than forecast in November. Sales of light vehicles surged during November and December accounting for 2.1 percentage points of the 5.6 percent growth in real GDP observed in the fourth quarter. Forecasters suspect that a significant portion of that growth was encouraged by GM's rebate program and borrowed from the future. But, even taking that into account the stronger income growth now forecast is expected to move auto sales for the remainder of the fiscal year above levels forecast in November.

Other Revenues

Other tax and non-tax revenues, other than the tobacco settlement payments are expected to total $2.153 billion during the current fiscal year, up $46 million (2.2 percent) from November's estimates. Tobacco settlement payments totaling $461 million have been received in this fiscal year.

Deed and mortgage tax receipts since November are now $7.6 million above forecast, reflecting both continued refinancing activity and a much higher than normal number of homes sold. The forecast for deed and mortgage tax receipts was increased by $14 million to incorporate the existing positive variance and to reflect an improved outlook for home sales during 1999.

The forecast for investment income was increased by $22 million. The increase incorporates the $14 million year to date variance in the base, and reflects both the slightly higher returns on investment currently being received and an increase in state cash balances.

Revenue Forecast
F.Y. 2000-01

Total current resources for the 2000-01 biennium are now forecast to total $25.036 billion, $398 million (1.6 percent) more than was forecast in November. Net non-dedicated revenues increase by $374 million, also a 1.6 percent increase. Revenues from the four major taxes are now forecast to be $21.584 billion, $328 million (1.5 percent) above levels projected in November. All changes in the four major taxes were within normal levels of variation. Changes in the individual income tax forecast accounted for 60 percent of the additional revenue in this forecast.

F.Y. 2000-01 Revenue Forecast
($ in millions)

	FY98-99 Biennium	FY 00	FY 01	FY00-01 Biennium
Revenues				
Individual Income Tax	9,884	5,804	6,136	11,940
Sales Tax	6,666	3,603	3,742	7,344
Corporate Income Tax	1,526	696	687	1,383
Motor Vehicle Sales Tax	906	455	461	916
Four Major Taxes	18,982	10,558	11,026	21,584
Other Revenues	2,153	1,024	980	2,004
Tobacco Settlement	461	368	393	761
Net Non-dedicated Revenue	21,596	11,950	12,399	24,349
Other Resources	930	351	336	687
Current Resources	22,526	12,301	12,735	25,036

Net non dedicated revenues in 2000-01 are currently forecast to grow by 12.7 percent over levels projected for the 1998-99 biennium. When the tobacco settlement payments are excluded, the growth rate falls to 11.6 percent. Individual income tax receipts are expected to grow by 20.8 percent, and sales tax receipts by 10.2 percent.

The unusually high growth rate in the income tax is attributable to the effects of the property tax rebate program on net income tax receipts in the 1998-99 biennium. Those rebates reduced that biennium's income tax liability by a total of $886 million. In the absence of that offset to income tax collections, 2000-01 receipts would be only 10.9 percent more than those in 1998-99.

Individual Income Tax

Receipts from the individual income tax in the 2000-01 biennium are now forecast to total $11.940 billion, $241 million (2.1 percent) more than forecast in November. The increase in tax year 1998 income caused by strong wage growth and apparently higher capital gains realizations carries forward into tax years 1999, 2000, and 2001. Wage growth rates and the growth in capital gains realizations are expected to slow during the 2000-01 biennium, but the higher base level incomes assumed at the start of the biennium create additional revenue. A drop in expected farm income in tax year 1999 reduces income tax revenues growth.

Net capital gains are assumed to grow at an average rate of only slightly more than 2 percent during the 1999, 2000, and 2001 tax years. DRI's current forecast shows only small increases in stock market averages and the value of equities held by households during the next three years. In addition, the econometric model used to forecast capital gains allows realization growth to slip below recent levels and move toward a long-term trend growth rate equal to the rate at which household financial assets are increasing. In recent years realizations have increased much more rapidly than net household financial assets.

Technical changes including a change in the ratio of final receipts to final liability and a revision in the timing of estimated tax receipts increased biennial revenues by $12 million. No federal disaster relief package was assumed available to be available for farmers in 1999.

Sales Tax

Net sales tax receipts for the 2000-01 biennium are now expected to reach $7.344 billion, $23 million, (0.3 percent) more than forecast in November. Gross sales tax receipts grew by $36 million, building on the higher base provided by the improved outlook for early 1999. Growth rates for spending on consumer durables, business equipment, and construction weaken in 2000, falling below the forecast growth rates used in November. Sales tax refunds increase by $13 million, offsetting a portion of the growth in gross sales tax receipts.

Corporate Franchise Tax

Net corporate tax receipts are estimated to total $1.383 billion in the 2000-01 biennium, up $32 million from November's forecast. The DRI forecast of 1999 pre-tax corporate profits has been increased by 8 percent, and their forecast for tax year 2000 profits has been cut by 3 percent. The result has been an increase in corporate payments in F.Y. 2000, followed by a decrease in F.Y.2001. A change in the timing and composition of expected refunds due under the Rural American Bank judgement reduced net revenues for F.Y. 2000 by $5 million. The corporate income tax remains the most volatile of all state revenue sources.

Motor Vehicle Sales Tax

Receipts from the sales tax on motor vehicles are forecast to be $916 million, $33 million (3.8 percent) more than forecast in November. Light vehicle sales will slow from the fourth quarter's unsustainable pace of 16.4 million units annually, but DRI is currently projecting annual light vehicle sales to remain at a historically high level, 15.4 million through 2001. Sales at that level would exceed the average from 1995 through 1997 by about 300,000 vehicles per year.

Other Revenues

Other tax and non tax revenues are expected to exceed levels forecast in November by $46 million. A $19 million increase in the forecast for investment income and a $33 million re-statement of expected income from the tobacco settlement to include projected inflation were the only large changes. Adjustments to forecasts for the other revenue sources were small and offsetting.

Revenue Planning Estimates F.Y. 2002-03

Current resources for the 2002-03 biennium are now projected to total $26.777 billion, 6.9 percent more than the forecast for the 2000-01 biennium. The four major taxes are expected to grow by 8 percent, while other tax and non-tax revenues are projected to decrease by 1.3 percent from projected levels for 2000-01.

This baseline planning estimate is not an explicit forecast. It is simply an extrapolation of projected trends in the economy. Because of the way it is constructed, any changes in the base level of revenues for fiscal 1998, or any subsequent year through fiscal 2001 will be reflected in the revenue planning estimates for 2002 and 2003. Other things equal, stronger than anticipated growth in either of those years will add significantly to revenues available in the 2002-03 biennium. Similarly, should the economy grow more slowly than forecast during the next three years, the revenue outlook for 2002-03 will deteriorate.

These revenue planning estimates are only a guide to the level of future revenues, not a guarantee. If the economy remains strong through 2001, if projections of capital gains realizations for tax years 1998, 1999, and 2000 are accurate, and if recent technical adjustments to the income and sales tax models are appropriate these planning estimates are likely to underestimate future revenues. But if the economy fails to perform at the level anticipated in DRI's November Control, or, if capital gains realizations fail to reach the level projected, or if the technical adjustments were unnecessary, the current planning estimates will overstate future revenues. Actual revenues could exceed or fall short of the planning estimates by as much as $2.0 billion, depending on the economy's performance during the next 4 years. There is no recession in the long term forecast, only slightly slower real and nominal growth, and while no signs of a recession are currently visible, to go through the 2002-03 biennium without a recession would mean that the U.S. economy had gone more than 12 years without a recession.

The projected growth rate for F.Y. 2002-03 revenues is less than that forecast for the 2000-01 biennium. The tobacco settlement, whose payments peak in the 2000-01 biennium, and the return to normal from the two property tax rebate programs administered through the individual income tax system produced unusually high revenue growth in 2000-01 biennium. When those one time events are netted out revenue growth in 2002-2003 is only slightly below average.

F.Y. 2002-03 Revenue Planning Estimates
($ in millions)

	FY2001-02 Biennium	FY2002	FY2003	FY2002-03 Biennium
Revenues				
Individual Income Tax	11,940	6,392	6,675	13,067
Sales Tax	7,344	3,869	4,004	7,873
Corporate Income Tax	1,383	697	725	1,422
Motor Vehicle Sales Tax	916	470	486	956
Four Major Taxes	21,584	11,428	11,889	23,317
Other Revenues	2,765	1,417	1,310	2,727
Net Non-dedicated Revenue	24,349	12,845	13,199	26,044
Other Resources	687	367	366	733
Current Resources	25,036	13,212	13,565	26,777

Estimates of 2002-03 revenues are based on DRI's Summer 1998 Cyclelong and November, 1998, Control forecasts. Nominal growth rates for variables used in projecting tax revenues were computed by multiplying the average real growth rate for each key series computed over the entire 25 year Cycle forecast horizon by the appropriate inflation estimate for that year taken from the November Control forecast.

When available, DRI's Winter Cyclelong forecast serves as the basis for February's long term revenue planning estimates. This year, however, DRI had not released their Winter long-term projections by the time the forecast went to press, so February's revenue planning estimates continue to be based on DRI's Summer 1998 long-term forecast. Since long-term real growth rates typically are very stable, use of the Summer rather than the Winter long term growth rates would normally have little impact on the revenue outlook for the 2002-03 biennium. Recently though, there have been indications that DRI may have become slightly more optimistic about the outlook for long-term growth. Should that be true, revenue planning estimates calculated using the Winter long-term forecast would show further increases in revenues beyond those given above.

Although DRI extended the forecast horizon for its Control forecast to 5 years, in October, 1996, there is still only fragmentary data on the reliability of their year four and year five forecasts. The Department of Finance has chosen to continue to use its previous methodology for preparing revenue planning estimates. Department economists will continue to evaluate the advisability of basing their long term planning estimates on the year four and year five projections from the DRI Control.

Individual income tax estimates were prepared using the House Income Tax Simulation Model. Assumed filer growth in Minnesota was consistent with average national employment growth in the Cyclelong forecast. All elements of taxable income and all individual itemized deductions were assumed to grow at the growth rate for taxable personal income forecast by DRI. Calendar year income tax liabilities were converted into fiscal year revenues using the same proportions as forecast for 1999.

Future sales tax revenues were estimated by computing percentage growth rates for each of seven broad categories of products in the sales tax base. Those growth rates for both FY 2002 and F.Y. 2003 were constructed using the estimated real growth rates from DRI's Summer, 1998 Cycle forecast and inflation from the November, 1998, Control forecast. The growth rates were then weighted by the fraction of the expected 1999 sales tax base attributable to each category of purchases. The sum of the weighted growth rates was used as a measure of expected growth in the sales tax base for 2002 and 2003.

Corporate tax receipts in Minnesota were estimated to grow at the same rate as the DRI's Control forecast of national before tax corporate profits. Minnesota's motor vehicle excise tax collections are expected to grow at the same rate as the national consumption of motor vehicles and parts. Planning estimates for other tax and non tax revenues were prepared by extrapolating existing trends.

It is impossible to anticipate the economy's performance three or four years in advance. Economic projections which look that far into the future can only be extrapolations of historical trends consistent with the current short term outlook. It is important to remember that the long term revenue planning estimate is only a guide to what revenues three and four years from now might be, not a guarantee of a specific level of revenues, and that there may be large positive or negative errors in the long term estimate.

Expenditure Forecast
F.Y. 1998-2003

Current Biennium

The February, 1999 expenditure forecast for the current biennium totals $21.652 billion, a $3 million increase from the comparable estimates in November, 1998. Minor decreases in K-12 education, health care, family support, and other major local assistance estimates, combined with slightly higher costs for property tax aids and credits and state agency spending account for the slight increase in spending in the current biennium.

F.Y. 1998-99 Expenditure Forecast
($ in millions)

	Nov. 1998	Feb. 1999	Difference
Estimated Spending by Function			
Education/Children & Families	$6,909	$6,908	($1)
Property Tax Recognition	$109	$109	
Post-Secondary Education	$2,444	$2,444	
Property Tax Aids & Credits	$2,576	$2,584	$8
Other Major Local Assistance	$1,011	$1,010	($1)
Health Care	$3,119	$3,112	($7)
Family Support	$516	$516	
State Operated Institutions	$884	$884	
Legislature, Judicial, Const. Officers	$527	$527	
State Agencies' Operations & Grants	$1,840	$1,844	$4
Debt Service	$545	$545	
Capital Projects	$900	$900	
Estimated Cancellations	($15)	($15)	
Subtotal-Major Spending Categories	$21,366	$21,369	$3
Dedicated Expenditures	$283	$283	
Total Expenditures & Transfers	**$21,649**	**$21,652**	**$3**

Expenditure Projections, F.Y. 2000 - 2003

Under current law, expenditures for F.Y. 2000-01 are forecast to total $22.544 billion, a 4.1 percent increase over the current forecast for the F.Y. 1998-99 biennium. For the following biennium, planning estimates for F.Y. 2002-03 indicate that spending is expected to rise to $24.437 billion, an 8.4 percent increase over F.Y. 2000-01.

These expenditure estimates are projections of the cost of continuing current law programs after adjusting for changes in education enrollment, human service program caseload, net tax capacity, the number of households, and other. The forecast and planning estimates provide for a 2.5 percent annual increase in the cost of goods, services and major state grant programs for each year. This discretionary inflation is not required by current law, but reflects the impact of expected price increases on the cost of government programs.

F.Y. 2000-03 Expenditure Estimates
($ in millions)

	Forecast F.Y. 2000-01	Plng. Est F.Y. 2002-03
Education/Children & Families	$7,546	$7,863
Post-Secondary Education	2,466	2,613
Property Tax Aids & Credits	3,176	3,489
Other Major Local Assistance	1,136	1,228
Health Care	3,761	4,587
Family Support	518	562
State Operated Institutions	968	1,036
Legislature, Judicial, Const. Officers	536	559
State Agencies	1,713	1,781
Debt Service and Other	521	516
Estimated Cancellations	(20)	(20)
Subtotal	$22,322	$24,215
Dedicated Expenditures	$222	$222
Total Spending	**$22,544**	**$24,437**

Total net spending for both F.Y. 2000-01 and F.Y. 2002-03 is down slightly from the November 1998 forecast.

For F.Y. 2000-01, K-12 education spending estimates are down $63 million largely because of a technical correction to base spending due to the sunset of the “learning year” program. This sunset was inadvertently omitted from the November 1998 forecast estimates and is corrected in this forecast; there is very little “real” forecast change for education finance.

Forecast health care spending is down $15 million primarily due to lower enrollments in General Assistance Medical Care (GAMC) and the Medical Assistance long term care segment. Debt Service estimates decline $14 million largely due to a change in forecast assumptions: the current forecast assumes bonding bills in even-numbered calendar years of $400 million rather than the $700 million assumed in the November 1998 forecast.

Forecast state agency operations and grant spending is up $30 million; the largest changes include a $17 million increase in tax refund interest, a $5 million technical correction to the treatment of the Gulf War veteran's bonus, and a $5 million change in indirect cost receipts. Other minor changes in forecast expenditures largely reflect minor technical changes in base spending.

For F.Y. 2002-03 projected spending is down $71 million from the November estimates. K-12 spending estimates are down $73 million, largely due to the same technical correction and forecast adjustments made for F.Y. 2000-01. Health care expenditures are up $21 million because of higher enrollments and average costs in MFIP Families and Children Basic Care and other segments, partially offset by lower Medical Assistance long term care facilities average costs. State agency operations and grants spending is forecast $22 million higher, including a $14 million increase in tax refund interest. Debt service estimates are $45 million lower, again largely due to the change in assumptions about the size of future capital budgets. Relatively small changes in forecast costs in other areas, including a $2 million decrease in estimated discretionary inflation, account for the remaining net difference in spending.

Change from November 1998 Forecast
F.Y. 2000-01 and F.Y. 2002-03 Expenditure Estimates
($ in millions)

	Forecast F.Y.2000-01	Plng. Est F.Y. 2002-03
Education/ Children & Families	($63)	($73)
Post-Secondary Education	0	0
Local Aids & Credits	3	(7)
Other Major Local Assistance	3	5
Health Care	(15)	21
Family Support	0	0
State Operated Institutions	1	2
Legislature, Judicial, Const.	3	4
State Agencies	31	22
Debt Service and Other	(14)	(45)
Estimated Cancellations		
Subtotal	**($52)**	**($71)**
Dedicated Expenditures	$0	$0
Total Spending	**($52)**	**($71)**

K-12 Education Finance Estimates Fall $63 Million Due to Technical Correction

Spending on education and children & families is now projected to total $7.546 billion in F.Y. 2000-01, a decrease of $63 million from the November 1998 forecast.

Correction of a forecast error accounts for nearly all of the change. The November forecast for K-12 education should have removed funding for a program called "learning year,"which was first enacted in 1989. The program provides school districts with additional per pupil unit revenue if they offer a longer school day, week or year. Under current projections, the program would cost $60 million in the 2000-01 biennium, and $62 million in the 2002-03 biennium. A sunset clause for the program effective for F.Y. 2000 was enacted in 1996, and was overlooked in preparing the November forecast. The funding is removed in the February forecast estimates.

Other change in projected K-12 spending is minimal. Enrollment projections have increased slightly since the November forecast, by 1,216 students for F.Y. 2000-01, to a projected total enrollment of 845,404 students in F.Y. 2001. However, this slight forecast increase does not change the overall enrollment trend, as the number of students actually declines slightly from F.Y. 2000 to F.Y. 2001. Although the pupil unit increases cost an additional $6.8 million for the 2000-01 biennium, the increase is offset by a projected $7.2 million decrease in compensatory revenue. Similar patterns are reflected in the projections for F.Y. 2002-03, with pupils adding another $3 million to K-12 costs, offset by a $7 million decrease in compensatory revenue costs.

Health Care Forecast Down by One Percent for F.Y. 2000-01

Expected Health Care spending for F.Y. 2000-01 are $15 million lower than previously forecast. Total projected spending is $3.761 billion for the biennium, including $138 million for inflation. These unusually small February forecast changes are less than 1 percent of anticipated expenditures.

Lower projected enrollment in GAMC reduces cost estimates by $14 million for the biennium. The 5 percent enrollment decline found in 1999 is carried throughout the forecast period. Another $12 million in savings is due to MA Long Term Care Facilities enrollment changes. Current resident counts are roughly 1.5 percent lower than expected, resulting in lower caseloads in F.Y. 2000-01. A $10 million increase in forecast MA Families and Children Basic Care expenditures is due largely to an adjustment in average cost. Other changes increase costs by a net $1 million.

Slight Increase in Projected Health Care Costs in F.Y. 2002-03

Health Care planning estimates are increased by $21 million for F.Y. 2002-03. Total forecast expenditures are $4.587 billion, including $383 million for discretionary inflation.

The February forecast includes a $25 million increase for estimated MA Families and Children Basic Care spending in F.Y. 2000-03. This adjustment is a combination of 1 percent increases in average cost and projected enrollment. This increase is partially offset by $12 million in savings from MA Long Term Care facilities created by lower enrollment projections. All other program changes produce the remaining net difference of $7 million.

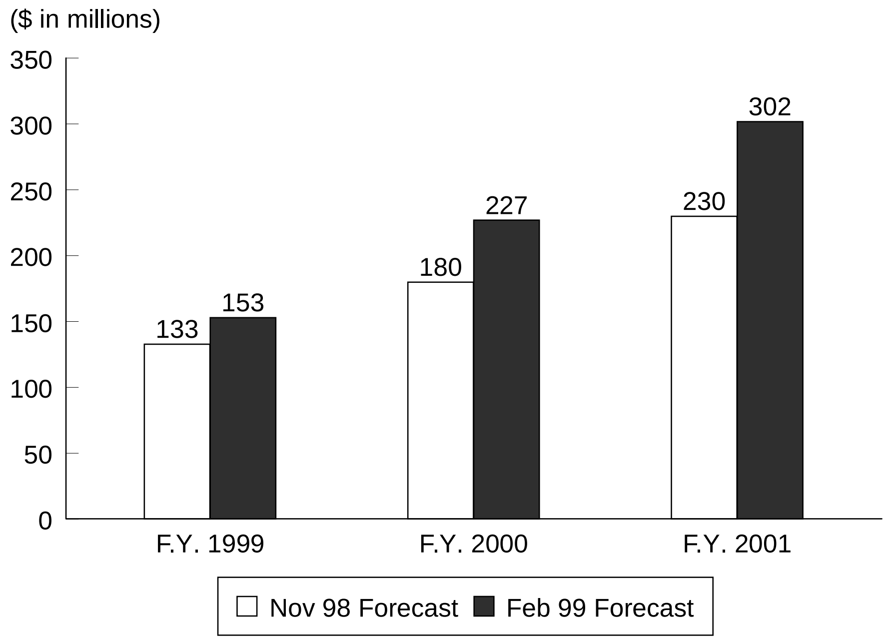
Family Support Savings Accrue to Federal TANF Reserve

The February forecast does not significantly change anticipated Family Support spending. The forecast lowers estimated F.Y. 2000-01 and F.Y. 2002-03 spending by less than a million dollars each biennium from November figures.

The small net change to the general fund reflects the balanced financing that links spending for the Minnesota Family Investment Program (MFIP) and MFIP Child Care. Lower than expected use of services reduces projected child care expenditures by almost $8 million. In turn, this spending decrease requires additional MFIP appropriations of $5 million to ensure that the state meets its federal maintenance of effort (MOE) requirements. Minor changes in other programs make up the remaining difference.

As a result, the most significant forecast changes show up in the amount of unspent federal TANF block grant (Temporary Assistance to Needy Families). Lower total spending for income assistance means that the state will use substantially lower amounts of TANF in each fiscal year of the forecast. The state's TANF Reserve, which is outside of the general fund, is the cumulation total of unused federal block grant resources. The reserve grows an additional $72 million between F.Y. 1999 and F.Y. 2001 over earlier estimates. The forecast projects that the TANF Reserve will total $302 million at the end of F.Y. 2001.

Projected TANF Reserve Balances



The federal TANF Reserve is expected to continue to grow in the F.Y. 2002-03 biennium. These figures are less reliable, however, since they assume that roughly one-fifth of Minnesota's MFIP caseload will lose eligibility for benefits due to time limits on the receipt of welfare. Under current law, with these assumptions, the TANF Reserve balance would be $486 million at the end of F.Y. 2003.

Debt Service

The forecast debt service for the 2000-01 biennium is $521 million, down $14 million from the November 1998 forecast of $535 million. Most of this change results from a change in assumptions about the size of future capital budgets. The November forecast assumed a $50 million capital budget in the 1999 legislative session and $700 million capital budgets in each future even numbered legislative session. The February forecast assumes no capital budget in the 1999 session and $400 million capital budgets in even numbered legislative sessions. The savings in the February forecast over the November forecast as a result of these changes in assumptions is $9 million. Additional savings because of revised cash flow assumptions on currently authorized bonds, higher earnings on cash balances in the debt service and bond proceeds funds, partially offset by slightly higher forecast bond interest rate costs, produce the remaining difference.

The forecast debt service for the 2002-03 biennium is $516 million, down $45 million from the November forecast of $561 million. The decline is due to the same factors producing lower debt service estimates for F.Y. 2000-01.

Other Spending Changes

Technical adjustments in state agencies' operations and grants account for most of the remaining forecast difference. The forecast for tax refund interest payments is up $7 million for F.Y. 1999, $17 million for F.Y. 2000-01, and $14 million for F.Y. 2002-03. Most of the increase is attributable to corporate tax refunds in the settlement of the Rural American litigation. A technical correction to the treatment of the Gulf War veteran's bonus removes $5 million in spending from F.Y. 1999 and increases spending an equivalent amount in F.Y. 2000-01. Lower projected indirect cost receipts increase net spending by $5 million in F.Y. 2000-01 and $3 million in F.Y. 2002-03.

Other major local assistance funding increases $3 million for F.Y. 2000-01 and $5 million for F.Y. 2002-03. Slightly lower forecast human services grant spending is offset by increases in the Ethanol Development Subsidy in the Department of Agriculture. Higher production estimates and an additional plant becoming eligible for funding combine to raise the forecast estimates by $4 million in F.Y. 2000-01 and $6 million in F.Y. 2002-03.

ALTERNATIVE FORECAST COMPARISON

Real GDP (Annual Rates)

	98III	98IV	99I	99II	99III	99IV	98A	99A	00A
DRI Control (2-99)	3.7	5.6	3.5	2.7	2.5	2.0	3.9	3.4	1.9
Blue Chip (2-99)	3.7	5.6	2.5	2.2	2.3	2.6	3.9	2.9	2.4
American Express (IDS) (2-99)	3.7	5.6	3.4	3.0	3.7	4.3	4.1*	3.4*	2.3*
Merrill-Lynch (2-99)	3.7	5.6	3.1	3.1	2.5	2.5	3.9	3.4	2.6

* 4Q/4Q

GDP Deflator (Chain-Weighted, Annual Rates)

	98III	98IV	99I	99II	99III	99IV	98A	99A	00A
DRI Control (2-99)	1.0	0.8	1.1	0.9	1.2	1.4	1.0	1.0	1.4
Blue Chip (2-99)	1.0	0.8	1.4	1.5	1.6	1.8	1.0	1.4	1.8
American Express (IDS) (2-99)	1.0	0.8	1.6	1.4	1.7	2.1	0.9*	1.7*	2.7*
Merrill-Lynch (2-99)	1.0	0.8	0.4	1.1	0.7	1.1	1.0	0.8	0.9

* 4Q/4Q

FORECAST COMPARISONS

Real Economic Growth
(Annual Percent Change in Real GDP)

	1998	1999	2000	2001	2002	2003
Feb 95 DRI Control	1.7[(1)]	1.7[(1)]	1.7[(1)]	1.7[(1)]		
Nov 95 DRI Control	1.7[(2)]	1.7[(2)]	1.7[(2)]	1.7[(2)]		
Feb 96 DRI Control	1.7[(2)]	1.7[(2)]	1.7[(2)]	1.7[(2)]		
Nov 96 DRI Control	2.4	2.0	1.6[(3)]	1.6[(3)]		
Feb 97 DRI Control	2.1	2.1	1.6[(3)]	1.6[(3)]		
Nov 97 DRI Control	2.3	2.0	2.5	1.7[(4)]		
Feb 98 DRI Control	2.7	1.4	2.4	1.7[(4)]		
Nov 98 DRI Control	3.6	1.7	2.3	2.1	1.7[(5)]	1.7[(5)]
Feb 99 DRI Control	3.0	3.4	1.9	2.3	1.7[(5)]	1.7[(5)]

Inflation
(Annual Percent Change in Implicit GDP Deflator - 1992 = 100)

	1998	1999	2000	2001	2002	2003
Feb 95 DRI Control	3.2[(3)]	3.2[(3)]	3.2[(3)]	3.2[(3)]		
Nov 95 DRI Control	2.1[(4)]	2.4[(4)]	2.1[(4)]	2.4[(4)]		
Feb 96 DRI Control	2.1[(6)]	2.4[(6)]	2.1[(6)]	2.4[(6)]		
Nov 96 DRI Control	2.3	2.4	2.6	2.8		
Feb 97 DRI Control	2.3	2.5	2.7	2.9		
Nov 97 DRI Control	2.0	2.1	2.3	2.3		
Feb 98 DRI Control	1.7	1.9	2.2	2.1		
Nov 98 DRI Control	1.0	1.6	2.0	2.1	2.3	2.5
Feb 98 DRI Control	1.0	1.01	1.4	1.7	1.9	2.0

(1) Long-term trend from DRI Cyclelong, Summer 1994 and Winter 1994/95.
(2) Long-term trend from DRI Cyclelong, Summer 1995.
(3) Long-term trend from DRI Cyclelong, Summer 1996.
(4) Long-term trend from DRI Cyclelong, Summer 1997.
(5) Long-term trend from DRI Cyclelong, Summer 1998.
(6) Summer 1994 Trendlong Forecast.

MINNESOTA - U.S. COMPARISON REPORT

Annual Percent Changes

February 1999 Control

	1994	1995	1996	1997	1998	1999	2000	2001
Wage and Salary Income								
United States	4.9	5.8	5.9	7.1	6.7	6.0	4.6	4.3
Minnesota	5.8	6.5	7.6	7.4	7.6	5.5	4.6	4.7
Implied Annual Wage								
United States	1.8	3.1	3.7	4.4	4.1	3.9	3.5	3.2
Minnesota	2.7	3.5	5.2	5.2	5.0	3.5	3.3	3.6
Non-Farm Employment								
United States	3.1	2.6	2.1	2.6	2.5	2.0	1.1	1.1
Minnesota	3.0	2.9	2.3	2.1	2.5	1.9	1.3	1.1
Personal Income								
United States	5.1	5.5	5.8	5.6	5.0	4.8	4.2	4.1
Minnesota	7.0	6.0	7.6	5.8	5.6	4.7	4.0	4.1

Comparison of Actual and Estimated Non-Restricted Revenues
Fiscal Year-To-Date, Through January, 1999
($ in thousands)

	Forecast Revenues	Actual Revenues	Variance Act-Fcst
Individual Income Tax			
Withholding	2,622,513	2,628,625	6,112
Declarations	582,600	615,698	33,098
Miscellaneous	88,005	94,094	6,089
Gross	3,293,118	3,338,418	45,300
Refunds	60,026	69,000	8,974
Net	3,233,092	3,269,418	36,325
Corporate & Bank Excise			
Declarations	380,469	411,232	30,763
Miscellaneous	48,186	51,773	3,587
Gross	428,654	463,005	34,351
Refunds	72,127	61,129	(10,997)
Net	356,528	401,876	45,348
Sales Tax			
Gross	2,064,427	2,050,837	(13,591)
Refunds	88,912	95,130	6,218
Net	1,975,515	1,955,706	(19,809)
Motor Vehicle Excise	253,783	265,020	11,237
Other Revenues			
Inherit/Gift/Estate	27,583	30,728	3,145
Liquor/Wine/Beer	31,073	32,484	1,411
Cigarette & Tobacco	98,948	98,885	(63)
Deed & Mortgage	87,155	94,800	7,645
Insurance Gross Earnings	50,294	50,778	484
Lawful Gambling	36,193	33,448	(2,745)
Health Care Surcharge	65,508	63,663	(1,845)
Other Taxes	642	610	(32)
General Fund RTC Revenues	12,433	14,169	1,736
Income Tax Reciprocity	30,968	39,367	8,399
Investment Income	85,766	100,209	14,443
Tobacco Settlement	460,800	460,800	0
Other and Unallocated	44,492	43,375	(1,117)
Other Subtotal	1,031,855	1,063,317	31,462
Other Refunds	10,142	7,715	(2,427)
Other Net	1,021,713	1,055,602	33,889
TOTAL GROSS	7,071,838	7,180,597	108,759
TOTAL REFUNDS	231,207	232,975	1,768
TOTAL NET	6,840,632	6,947,622	106,991

FACTORS AFFECTING THE INDIVIDUAL INCOME TAX

(Dollars in Billions)

	Calendar Year					
	1996	1997	1998	1999	2000	2001
Minnesota Non-Farm Tax Base						
February 1995 Control	91.190	96.611				
November 1995 Control	94.160	97.766				
February 1996 Control	94.170	97.880				
November 1996 Control	95.750	100.570	105.170	109.960		
February 1997 Control	96.410	101.500	106.270	111.140		
November 1997 Control	100.450	106.250	111.700	116.240		
February 1998 Control	100.450	107.250	113.040	116.960		
November 1998 Control	100.430	107.490	113.850	118.500	123.620	128.830
February 1999 Control	100.430	107.490	114.640	120.320	125.150	130.330
Minnesota Wage and Salary Income						
February 1995 Control	68.310	71.447				
November 1995 Control	69.518	72.278				
February 1996 Control	69.754	72.680				
November 1996 Control	71.244	74.966	78.407	82.127		
February 1997 Control	71.712	75.572	79.203	82.961		
November 1997 Control	72.146	76.118	80.099	83.793		
February 1998 Control	72.146	76.773	81.433	84.502		
November 1998 Control	72.115	77.427	82.538	86.724	91.370	95.761
February 1999 Control	72.115	77.427	83.279	87.884	91.969	96.329
Minnesota Property Income						
February 1995 Control	16.985	17.933				
November 1995 Control	17.408	17.994				
February 1996 Control	17.077	17.604				
November 1996 Control	17.084	17.987	18.925	19.740		
February 1997 Control	17.212	18.133	19.011	19.782		
November 1997 Control	21.053	22.300	23.196	23.623		
February 1998 Control	21.053	22.265	23.112	23.606		
November 1998 Control	21.053	22.380	23.117	23.348	23.438	23.891
February 1999 Control	21.053	22.380	23.129	23.787	24.317	24.821
Minnesota Proprietors' Income						
February 1995 Control	6.895	7.232				
November 1995 Control	7.238	7.490				
February 1996 Control	7.337	7.597				
November 1996 Control	7.422	7.617	7.834	8.099		
February 1997 Control	7.489	7.798	8.056	8.401		
November 1997 Control	7.251	7.833	8.400	8.821		
February 1998 Control	7.251	8.017	8.500	8.855		
November 1998 Control	7.261	7.684	8.193	8.429	8.808	9.182
February 1999 Control	7.261	7.684	8.230	8.651	8.867	9.181

FACTORS AFFECTING SALES, CORPORATE INCOME AND SALES TAX ON MOTOR VEHICLES

(Dollars in Billions)

SALES TAX

Minnesota's Proxy Share of U.S. Consumer Durable Spending

	Fiscal Year 1996	1997	1998	1999	2000	2001
February 1995 Control	7.308	7.558				
November 1995 Control	7.764	8.031				
February 1996 Control	7.729	8.151				
November 1996 Control*	7.758	8.233	8.601	8.948		
February 1997 Control	7.758	8.233	8.705	9.026		
November 1997 Control	7.802	8.334	8.911	9.430		
February 1998 Control	7.767	8.291	8.802	9.226		
November 1998 Control	7.911	8.498	9.182	9.750	10.207	10.662
February 1999 Control	7.911	8.498	9.187	9.854	10.456	10.828

Minnesota's Proxy Share of U.S. Capital Equipment Spending

	1996	1997	1998	1999	2000	2001
February 1995 Control	8.029	7.935				
November 1995 Control	8.613	8.763				
February 1996 Control	8.679	8.971				
November 1996 Control	8.069	8.757	9.316	9.900		
February 1997 Control	8.066	8.777	9.503	10.154		
November 1997 Control	7.707	8.511	9.461	10.148		
February 1998 Control	7.744	8.518	9.344	10.038		
November 1998 Control	7.824	8.555	9.475	10.338	10.743	11.224
February 1999 Control	7.824	8.555	9.485	10.417	11.103	11.461

Minnesota's Proxy Share of U.S. Construction Spending

	1996	1997	1998	1999	2000	2001
February 1995 Control	4.941	4.974				
November 1995 Control	4.830	5.024				
February 1996 Control	4.855	4.916				
November 1996 Control	4.966	5.105	5.243	5.356		
February 1997 Control	4.966	5.170	5.290	5.344		
November 1997 Control	5.015	5.436	5.752	6.018		
February 1998 Control	5.027	5.435	5.810	6.066		
November 1998 Control	5.051	5.494	5.983	6.259	6.620	6.927
February 1999 Control	5.051	5.494	5.983	6.593	6.872	7.081

* Reflects data revision.

FACTORS AFFECTING SALES, CORPORATE INCOME AND SALES TAX ON MOTOR VEHICLES

(Dollars in Billions)

	Fiscal Year					
	1996	1997	1998	1999	2000	2001
SALES TAX (Cont.)						
Minnesota Non-Farm Personal Income						
February 1995 Control	106.84	111.63				
November 1995 Control	108.91	113.59				
February 1996 Control	109.15	113.74				
November 1996 Control	110.87	115.94	121.93	127.60		
February 1997 Control	110.85	117.14	121.03	128.57		
November 1997 Control	113.98	121.14	127.68	133.13		
February 1998 Control	114.53	121.70	128.73	133.98		
November 1998 Control	114.11	121.80	129.20	135.40	141.19	147.71
February 1999 Control	114.11	121.80	129.58	136.44	142.42	148.03
SALES TAX ON MOTOR VEHICLES						
Minnesota's Proxy Share of U.S. Consumption of Motor Vehicle and Parts						
February 1995 Control	5.322	5.491				
November 1995 Control	5.479	5.560				
February 1996 Control	5.324	5.357				
November 1996 Control	5.310	5.381	5.582	5.806		
February 1997 Control	5.310	5.290	5.404	5.625		
November 1997 Control*	5.132	5.123	5.191	5.339		
February 1998 Control	5.132	5.128	5.293	5.392		
November 1998 Control	5.170	5.249	5.550	5.575	5.718	5.900
February 1999 Control	5.170	5.249	5.576	5.955	5.803	6.039
CORPORATE FRANCHISE TAX (Calendar Year)						
U.S. Corporate Profits						
February 1995 Control	460.8	467.7				
November 1995 Control	477.4	476.7				
February 1996 Control	472.5	476.6				
November 1996 Control*	624.6	618.2	642.6	671.4		
February 1997 Control	624.6	645.3	659.6	677.8		
November 1997 Control	676.6	723.9	737.4	762.6		
February 1998 Control	676.6	735.4	756.3	754.3		
November 1998 Control	680.2	734.4	711.8	678.9	697.4	710.9
February 1999 Control	680.2	734.4	725.6	732.1	678.9	688.4

* Change in definition

February 1999 Forecast
F.Y. 1999-2001
($ in Thousands)

	2-99 Fcst F.Y. 1999	2-99 Plng Est F.Y. 2000	2-99 Plng Est F.Y. 2001
Actual & Estimated Resources:			
Balance Forward From Prior Year	2,527,216	2,869,245	4,114,247
Current Resources:			
Net Non-Dedicated Revenue			
Individual Income Tax	5,137,100	5,804,100	6,136,100
Sales Tax	3,414,737	3,602,601	3,741,738
Corporate Income Tax	773,800	696,100	687,400
Motor Vehicle Sales	461,500	454,800	461,400
Tobacco Settlements	460,800	368,020	392,586
Other Non-Dedicated Revenue	1,090,177	1,024,455	979,729
Subtotal Net Non-Ded. Rev.	11,338,114	11,950,076	12,398,953
Dedicated Revenue	139,237	124,647	112,673
Transfers In	294,293	216,069	212,900
Prior Year Adjustments	10,100	10,100	10,100
Subtotal-Current Resources	11,781,744	12,300,892	12,734,626
Total Resources Available	**14,308,960**	**15,170,137**	**16,848,873**
Actual & Estimated Spending by Function:			
Education /Children & Families	3,597,138	3,729,615	31,816,728
Property Tax Recognition	90,205	0	0
Post-Secondary Education	1,281,239	1,207,571	1,258,937
Property Tax Aids & Credits	1,368,031	1,534,418	1,641,283
Other Major Local Assistance	528,791	559,160	577,094
Health Care	1,603,291	1,812,574	1,948,544
Family Support	254,552	253,815	264,486
State Operated Institutions	458,904	472,499	495,669
Legisl., Judicial, Const. Officers	277,766	266,337	269,435
State Agencies' Operations & Grants	968,419	847,971	864,874
Debt Service	299,581	266,155	255,264
Capital Projects	600,659	0	0
Estimated Cancellations	(15,643)	(5,000)	(15,000)
Subtotal-Major Spending Categories	11,312,933	10,945,115	11,377,313
Dedicated Expenditures	126,782	110,775	110,776
Total Expenditures & Transfers	**11,439,715**	**11,055,890**	**11,488,089**
Balance Before Reserves	**2,869,245**	**4,114,247**	**5,360,783**
Cash Flow Account	350,000	350,000	350,000
Budget Reserve	622,000	622,000	622,000
Property Tax Reserve Account	330,181	143,856	0
Tax Reform & Reduction Account	200,000	200,000	200,000
Dedicated Reserves	131,760	132,523	133,105
Budgetary Balance	**1,235,304**	**2,665,868**	**4,055,678**

Current Biennium Forecast Comparison
November 1998 vs February 1999
($ in Thousands)

	11-98 Fcst F.Y. 1998-99	2-99 Fcst F.Y. 1998-99	Difference
Actual & Estimated Resources:			
Balance Forward From Prior Year	1,994,720	1,994,720	0
Current Resources:			
Net Non-Dedicated Revenue			
Individual Income Tax	9,742,669	9,883,669	141,000
Sales Tax	6,665,339	6,666,422	1,083
Corporate Income Tax	1,459,461	1,525,861	66,400
Motor Vehicle Sales	879,976	906,476	26,500
Tobacco Settlements	461,097	461,097	0
Other Non-Dedicated Revenue	2,107,276	2,152,997	45,721
Subtotal Net Non-Ded. Rev.	21,315,818	21,596,522	280,704
Dedicated Revenue	345,052	345,052	0
Transfers In	544,023	548,362	4,339
Prior Year Adjustments	36,550	36,550	0
Subtotal-Current Resources	22,241,443	22,526,486	285,043
Total Resources Available	**24,236,163**	**24,521,206**	**285,043**
Actual & Estimated Spending by Function:			
Education /Children & Families	6,908,650	6,907,762	(888)
Property Tax Recognition	108,900	108,905	5
Post-Secondary Education	2,444,134	2,444,134	0
Property Tax Aids & Credits	2,575,844	2,584,281	8,437
Other Major Local Assistance	1,011,011	1,009,671	(1,340)
Health Care	3,119,167	3,112,530	(6,637)
Family Support	516,488	516,000	(488)
State Operated Institutions	884,316	884,316	0
Legisl., Judicial, Const. Officers	527,247	526,808	(439)
State Agencies' Operations & Grants	1,840,397	1,844,207	3,810
Debt Service	545,202	545,218	16
Capital Projects	900,690	900,690	0
Estimated Cancellations	(15,643)	(15,643)	0
Subtotal-Major Spending Categories	21,366,403	21,368,879	2,476
Dedicated Expenditures	283,082	283,082	0
Total Expenditures & Transfers	**21,649,485**	**21,651,961**	**2,476**
Balance Before Reserves	**2,586,678**	**2,869,245**	**282,567**
Cash Flow Account	350,000	350,000	0
Budget Reserve	622,000	622,000	0
Property Tax Reserve Account	330,181	330,181	0
Tax Reform & Reduction Account	200,000	200,000	0
Dedicated Reserves	131,760	131,760	0
Budgetary Balance	**952,737**	**1,235,304**	**282,567**

Change in F.Y. 2000-01 Outlook
February 1999 Forecast
($ in Thousands)

	11-98 Plng Est F.Y. 2000-01	2-99 Plng Est F.Y. 2000-01	Difference
Actual & Estimated Resources:			
Balance Forward From Prior Year	2,586,678	2,869,245	282,567
Current Resources:			
Net Non-Dedicated Revenue			
Individual Income Tax	11,699,400	11,940,200	240,800
Sales Tax	7,321,539	7,344,339	22,800
Corporate Income Tax	1,351,900	1,383,500	31,600
Motor Vehicle Sales	883,000	916,200	33,200
Tobacco Settlements	727,250	760,606	33,356
Other Non-Dedicated Revenue	1,991,483	2,004,184	12,701
Subtotal Net Non-Ded. Rev.	23,974,572	24,349,029	374,457
Dedicated Revenue	237,320	237,320	0
Transfers In	405,901	428,969	23,068
Prior Year Adjustments	20,200	20,200	0
Subtotal-Current Resources	24,637,993	25,035,518	397,525
Total Resources Available	**27,224,671**	**27,904,763**	**680,092**
Actual & Estimated Spending by Function:			
Education /Children & Families	7,608,952	7,546,344	(62,608)
Post-Secondary Education	2,466,476	2,466,508	31
Property Tax Aids & Credits	3,172,854	3,175,701	2,847
Other Major Local Assistance	1,133,544	1,136,254	2,710
Health Care	3,776,322	3,761,118	(15,204)
Family Support	518,697	518,301	(396)
State Operated Institutions	967,238	968,168	930
Legisl., Judicial, Const. Officers	532,328	535,772	3,444
State Agencies’ Operations & Grants	1,682,056	1,712,845	30,788
Debt Service	535,501	521,419	(14,082)
Estimated Cancellations	(20,000)	(20,000)	0
Subtotal-Major Spending Categories	22,373,969	22,322,429	(51,540)
Dedicated Expenditures	221,551	221,551	0
Total Expenditures & Transfers	**22,595,520**	**22,543,980**	**(51,540)**
Balance Before Reserves	**4,629,151**	**5,360,783**	**731,632**
Cash Flow Account	350,000	350,000	0
Budget Reserve	622,000	622,000	0
Tax Reform & Reduction	200,000	200,000	0
Dedicated Reserves	133,105	133,105	0
Budgetary Balance	**3,324,046**	**4,055,678**	**731,632**

F.Y. 2000-01 General Fund Planning Estimates
Base, Inflation, Total
($ in Thousands)

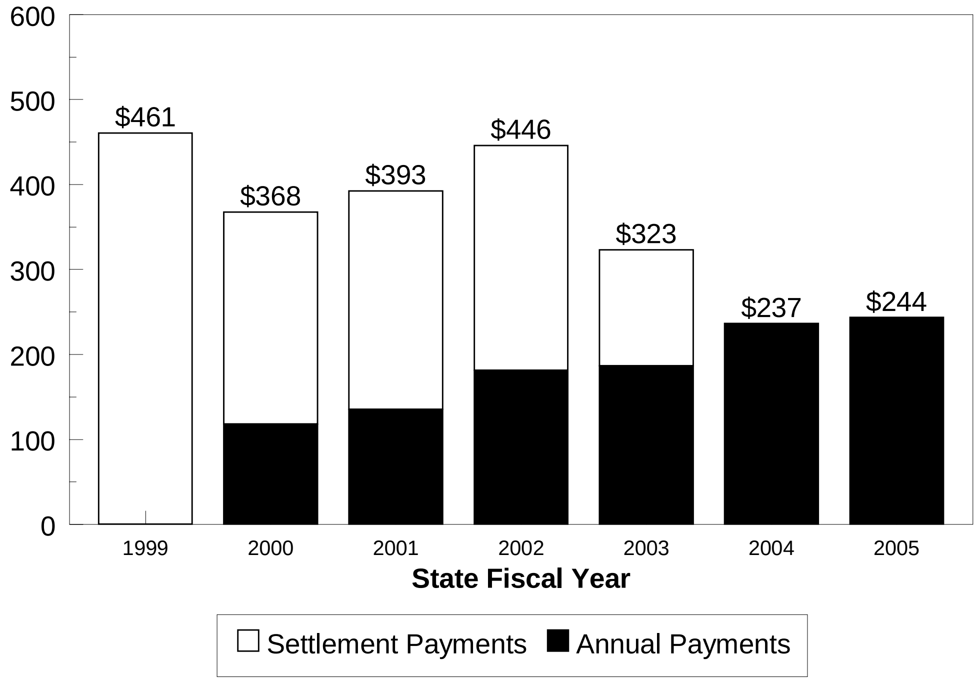
	2-99 Base F.Y. 2000-01	Inflation F.Y. 2000-01	2-99 Plng Est F.Y. 2000-01
Actual & Estimated Resources:			
Balance Forward From Prior Year	2,869,245	0	2,869,245
Current Resources:			
Net Non-Dedicated Revenue			
Individual Income Tax	11,940,200	0	11,940,200
Sales Tax	7,344,339	0	7,344,339
Corporate Income Tax	1,383,500	0	1,383,500
Motor Vehicle Sales	916,200	0	916,200
Tobacco Settlements	760,606	0	760,606
Other Non-Dedicated Revenue	2,004,184	0	2,004,184
Subtotal Net Non-Ded. Rev.	24,349,029	0	24,349,029
Dedicated Revenue	237,320	0	237,320
Transfers In	428,969	0	428,969
Prior Year Adjustments	20,200	0	20,200
Subtotal-Current Resources	25,035,518	0	25,035,518
Total Resources Available	**27,904,763**	**0**	**27,904,763**
Actual & Estimated Spending by Function:			
Education /Children & Families	7,271,466	274,878	7,546,344
Post-Secondary Education	2,376,392	90,116	2,466,508
Property Tax Aids & Credits	3,058,105	117,596	3,175,701
Other Major Local Assistance	1,094,808	41,446	1,136,254
Health Care	3,623,017	138,101	3,761,118
Family Support	499,366	18,935	518,301
State Operated Institutions	932,760	35,408	968,168
Legisl., Judicial, Const. Officers	516,293	19,479	535,772
State Agencies' Operations & Grants	1,651,573	61,272	1,712,845
Debt Service	521,419	0	521,419
Estimated Cancellations	(20,000)	0	(20,000)
Subtotal-Major Spending Categories	21,525,199	797,230	22,322,429
Dedicated Expenditures	221,551	0	221,551
Total Expenditures & Transfers	**21,746,750**	**797,230**	**22,543,980**
Balance Before Reserves	**6,158,013**	**(797,230)**	**5,360,783**
Cash Flow Account	350,000	0	350,000
Budget Reserve	622,000	0	622,000
Tax Reform & Reduction Account	200,000	0	200,000
Dedicated Reserves	133,105	0	133,105
Budgetary Balance	**4,852,908**	**(797,230)**	**4,055,678**

F.Y. 2002-03 Planning Outlook
November 1998 vs February 1999
($ in Thousands)

	11-98 Plng Est F.Y. 2002-03	2-99 Plng Est F.Y. 2002-03	Difference
Actual & Estimated Resources:			
Balance Forward From Prior Year	4 ,629,151	5,360,783	731,632
Current Resources:			
Net Non-Dedicated Revenue			
Individual Income Tax	12,881,500	13,067,000	185,500
Sales Tax	7,931,600	7,872,600	(59,000)
Corporate Income Tax	1,465,700	1,421,500	(44,200)
Motor Vehicle Sales	931,400	955,900	24,500
Tobacco Settlements	695,500	769,520	74,020
Other Non-Dedicated Revenue	1,977,368	1,957,776	(19,592)
Subtotal Net Non-Ded. Rev.	25,883,068	26,044,296	161,228
Dedicated Revenue	221,552	221,552	0
Transfers In	492,489	490,921	(1,568)
Prior Year Adjustments	20,200	20,000	0
Subtotal-Current Resources	26,617,309	26,776,969	159,660
Total Resources Available	**31,246,460**	**32,137,752**	**891,292**
Actual & Estimated Spending by Function:			
Education /Children & Families	7,935,717	7,862,888	(72,829)
Post-Secondary Education	2,613,030	2,613,470	440
Property Tax Aids & Credits	3,496,043	3,489,361	(6,682)
Other Major Local Assistance	1,223,816	1,228,360	4,544
Health Care	4,566,859	4,587,412	20,553
Family Support	561,687	561,749	62
State Operated Institutions	1,034,201	1,036,448	2,246
Legisl., Judicial, Const. Officers	555,395	559,030	3,635
State Agencies' Operations & Grants	1,759,069	1,780,683	21,615
Debt Service	561,012	515,737	(45,275)
Estimated Cancellations	(20,000)	(20,000)	0
Subtotal-Major Spending Categories	24,286,829	24,215,139	(71,690)
Dedicated Expenditures	221,552	221,552	0
Total Expenditures & Transfers	**24,508,381**	**24,436,691**	**(71,690)**
Balance Before Reserves	**6,738,079**	**7,701,061**	**962,982**
Cash Flow Account	350,000	350,000	0
Budget Reserve	622,000	622,000	0
Tax Reform & Reduction Account	200,000	200,000	0
Dedicated Reserves	133,105	133,105	0
Budgetary Balance	**5,432,974**	**6,395,956**	**962,982**

Tobacco Lawsuit Revenues*

February 1999 Forecast
($ in millions)



	FY 1999	FY 2000-01	FY 2002-03
Annual Payments	$0	$253.5	$367.7
Settlement Payments	$460.8	$507.1	$401.8
Total	**$460.8**	**$760.6**	**$769.5**

*After inflation adjustments