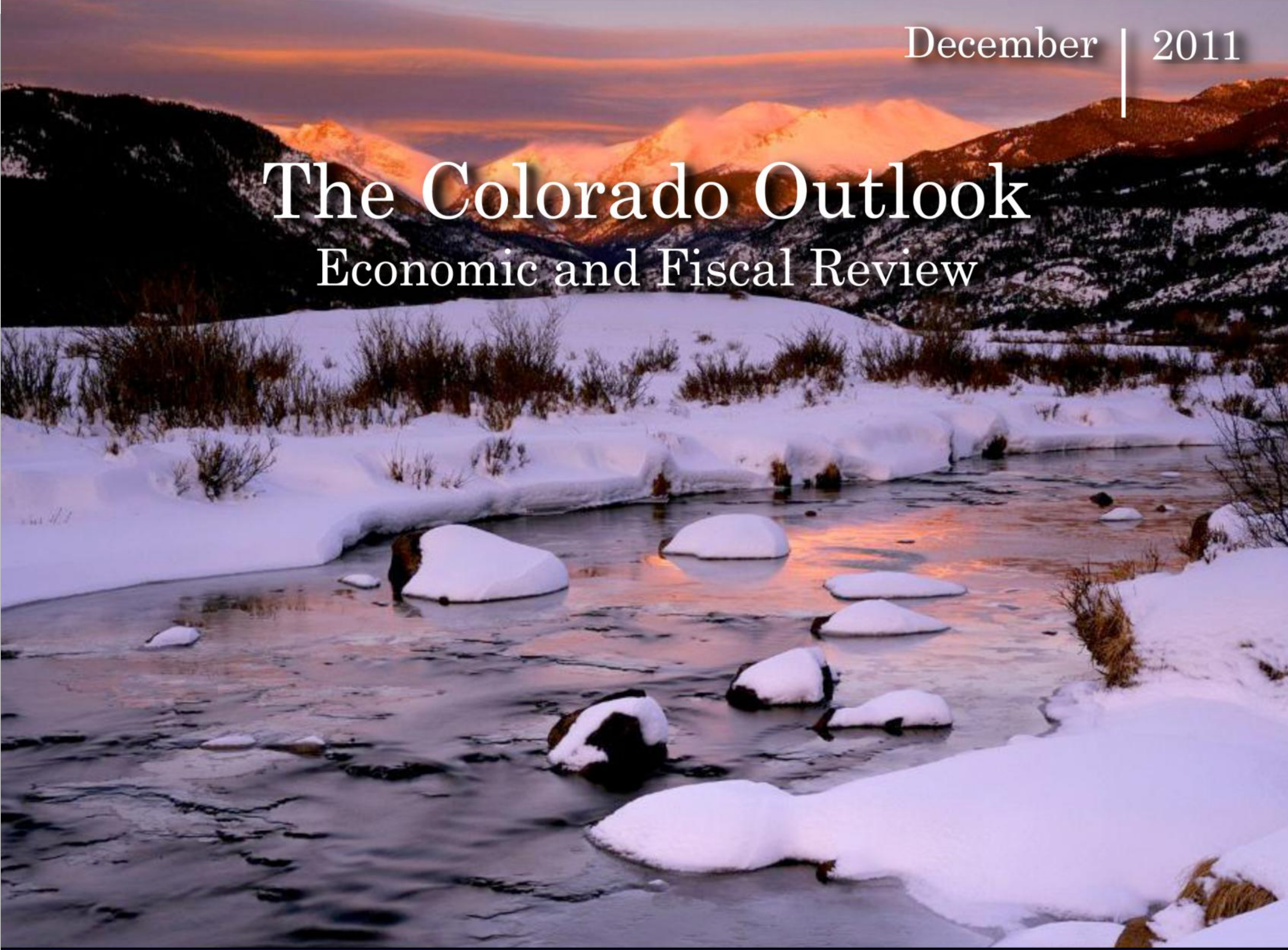
December | 2011

The Colorado Outlook

Economic and Fiscal Review



Governor's Office of State Planning and Budgeting

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Summary

- The General Fund revenue forecast for the current budget year (FY 2011-12) is $231.0 million, or 3.2 percent, higher than the September forecast. The weakening in the economy that influenced the projections in September has reversed and there is more momentum in the economy than was previously evident. Based on the higher forecast, the state will end the fiscal year with a reserve equal to 7.0 percent of appropriations, $212.2 million above the required 4.0 percent reserve level.

- OSPB projects General Fund revenue growth of 1.1 percent next fiscal year. This forecast takes a cautious approach to General Fund revenue in FY 2012-13 due to the slowing in the global economy, and especially the heightened risk of deterioration of the European financial situation. Further, the high amount of volatility in the stock market this fall caused investors to sell off assets which will reduce tax revenue from capital gains in FY 2012-13. In addition, certain tax policy changes under current law and accrual accounting changes will slow revenue growth in FY 2012-13 compared with FY 2011-12. Without these accrual and tax policy changes, FY 2012-13 revenue growth would be closer to the current fiscal year's growth rate of 4.1 percent.

- Based on this forecast, General Fund appropriations can grow 5.2 percent, or $366.5 million in FY 2012-13 under current law. This assumes that the excess reserve in FY 2011-12 is not spent and adds to the amount of money available for spending in FY 2012-13. Under the Governor's November 1, 2011 budget request for FY 2012-13, the state will end the fiscal year with an excess reserve of $331.2 million. This also assumes the excess reserve in FY 2011-12 is not spent this fiscal year. Thus, the amount available for the General Fund budget will depend on policy decisions regarding the use of this year's projected excess reserve.

- OSPB projects that cash fund revenue subject to TABOR in FY 2011-12 will total $2.4 billion, a 4.3 percent increase over FY 2010-11. In FY 2012-13, OSPB forecasts cash fund revenue growth of $52.7 million, or 2.2 percent.

- Since the publication of the September forecast, the economy has shown welcome improvement. Job growth at the state level has particularly shown signs of sustained momentum. The job market rebound has occurred across many industries and is reducing the state's unemployment rate. Claims for unemployment insurance continue to drop. The goods producing industries of manufacturing and oil and gas, which are highly beneficial to the state's economy, continue to grow. However, the overall economy is still only expanding modestly as it continues the difficult process of rebuilding from the credit and housing boom and bust. The state and national economies are highly connected to the rest of the world and dependent on credit. Thus, the European debt crisis and slowing in the global economy poses a downside risk to the forecast. Based on these factors, economic growth is expected to slow modestly in 2012. However, if European and global conditions improve, both economic and revenue growth would outperform this forecast.

General Fund Budget

GENERAL FUND OVERVIEW

Table 1 presents the General Fund Overview for the December 2011 OSPB revenue forecast under current law, while Table 1a shows the overview incorporating the Governor's November 1, 2011 FY 2012-13 budget request.

Funds available – The top portions of the tables summarize the amount of General Fund revenue available for spending. The forecast for this revenue is discussed in further detail in the *General Fund Revenue Forecast* section starting on page 8. The revenue available for spending in Table 1a incorporates the Governor's proposal to transfer $73.2 million in revenue from cash funds, mostly from severance taxes, to the General Fund (Line 4). It also shows the proposal to reduce the amount of gaming revenue credited to the General Fund by $6.1 million (Line 5) that would instead be used to fund initiatives in the Governor's Energy Office and the Office of Film, Television, and Media.

Spending subject to the appropriations limit – Line 5 in Table 1 and Line 7 in Table 1a show General Fund appropriations that are subject to the limit of five percent of Colorado personal income as specified in Section 24-75-201.1 (1) (a) (II) (A), C.R.S. These appropriations fund the State's largest programs, such as K-12 education, higher education, Medicaid, corrections, and human services. General Fund appropriations for FY 2011-12 reflect current law. In Table 1, the appropriations amount for fiscal years 2012-13 and 2013-14 reflects the level of spending that can be supported by forecasted revenue while maintaining the required General Fund reserve. The FY 2012-13 appropriations amount in Table 1a shows the Governor's November 1, 2011 budget request. The amount for FY 2013-14 in Table 1a reflects the level of spending that can be supported by forecasted revenue while maintaining the required General Fund reserve. However, the amounts in both tables will change depending on future budget decisions for the current fiscal year and FY 2012-13.

Spending not subject to the appropriations limit – Lines 8 through 16 in Table 1 summarize spending that is exempt from or is outside of the General Fund appropriations limit. These amounts are summarized in Table 1a in lines 10 to 18. The largest portion of this spending is "Rebates and Expenditures," which includes the Cigarette Rebate, Old Age Pension Fund, Property Tax, Heat, and Rent Credit, and Fire and Police Pensions Association (FPPA) contributions as outlined at the bottom of Table 2. The homestead property tax exemption expenditure amount (Line 12 in Table 1 and Line 14 in Table 1a) increases substantially under current law in FY 2012-13 to close to $100 million as the exemption for qualifying seniors returns. From FY 2009-10 through FY 2011-12, the exemption was available only to qualifying disabled veterans. As shown in Table 1a, the Governor's November 1, 2011 request suspends the senior exemption another year in FY 2012-13 which is estimated to save $96.8 million.

Reserves – The final section of the General Fund Overview tables ("Reserves") shows the amount of General Fund remaining at the end of each fiscal year. The "Year-End General Fund Balance," reflects the difference between total funds available (Line 4 in Table 1 and Line 6 in Table 1a) and total outlays (Line 17 in Table 1 and Line 19 in Table 1a). Line 20 in Table 1 and Line 22 in Table 1a shows the statutorily determined reserve requirement and the following line in each table indicates any variance from the target. For FY 2011-12, this forecast indicates that the reserve will be $212.2 million above the 4.0 percent required reserve.

State Education Fund – For informational purposes, the last line of the tables show the amount of money credited to the State Education Fund. Under the state constitutional provisions of Amendment 23, the state credits an amount equal to one-third of one percent of State taxable income to the State Education Fund. And, for FY 2011-12 only, the State Education Fund receives a portion ($221.4 million) of the General Fund revenue above required reserve from FY 2010-11 as a result of SB 11-156. In FY 2011-12, the fund will also receive money from the Tax Amnesty Program created by SB 11-184. Based on preliminary collections, this amount is roughly $6.0 million. However, additional revenue is expected to be collected through the end of December. The total amount that will be credited to the fund from the program will be known in January 2012.

BUDGET IMPLICATIONS OF THE FORECAST

FY 2011-12

Based on current law appropriations, the state will end the fiscal year with a reserve equal to 7.0 percent of appropriations, $212.2 million above the required 4.0 percent reserve level.

FY 2012-13

Under current law and based on this forecast, General Fund appropriations are able to grow 5.2 percent, or $366.5 million in FY 2012-13 while maintaining a 4.0 percent reserve. This assumes that the $212.2 million excess reserve in FY 2011-12 is not spent and adds to the amount of money available for spending in FY 2012-13.

Under the Governor's November 1, 2011 budget request for FY 2012-13, the state will end the fiscal year with a reserve equal to 8.6 percent of appropriations, $331.2 million above the required 4.0 percent reserve level. Again, this assumes that the excess reserve in FY 2011-12 is not spent and adds to the amount of money available for spending in FY 2012-13.

FY 2013-14

This forecast projects a return of stronger growth in General Fund revenue in FY 2013-14. This will help support General Fund programs, although it is not reasonable to expect many recent budget reductions to be reversed. The amount available for the General Fund budget will depend on the policies enacted for both the current year and FY 2012-13 budgets. The amount available for General Fund budget growth will be tempered in FY 2013-14 as this forecast projects required diversions to transportation, capital construction and a one-half of a percentage point increase in the General Fund Reserve. Under SB 09-228, this occurs when personal income increases by at least five percent. OSPB forecasts this to occur in 2013 as the economy picks up in momentum after a modest slowdown in 2012. OSPB projects a required transfer of $158.4 million for transportation, $40 million for capital construction, and an approximate $36 million increase in the reserve level. However, the amount of money already expected to be transferred to capital construction in FY 2013-14 exceeds the required amount under SB 09-228 as reflected in the General Fund Overview (Line 13 in Table 1 and Line 15 in Table 1a).

Risks to the Budget Outlook

Although economic conditions may prove better than what this forecast projects, the risks are weighted to the downside. The slowing in the global economy, and especially the heightened risk of deterioration of the European financial situation, creates downside risks to the future performance of the economy and thus tax collections. This is especially the case for FY 2012-13 as there is likely to be a lag between worsening financial conditions, the economy, and tax revenue. Developments in Europe and the rest of the world will therefore be monitored closely for any signs of further weakening.

Alternatively, a more comprehensive resolution to the European crisis in the near term that calms markets and loosens credit, a reversal of the slowing trends in global conditions, and increased momentum in the state's economy will cause revenue to outperform the FY 2012-13 revenue estimates. It is important to note that relatively small changes in projected revenue growth rates result in large swings in the amount of money available. For example, if growth were to increase or decrease by just three percentage points in FY 2012-13 from the projected growth rate, revenue would be approximately $220 million higher or lower.

If the economy performs better than projected in 2012, SB 09-228 could be triggered in FY 2012-13 − one year prior than expected. If the trigger were met, the transfers and the increase in the reserve would result in less money for other General Fund obligations. For FY 2012-13, the diversion for transportation could total around $155 million, while the current amount of money that is currently projected to be transferred for capital construction is above the amount that would be required under SB 09-228. The reserve would increase by around $30 million. The exact amounts would depend on the level of General Fund revenue if it were to come in higher-than-forecast due to better-than-expected economic performance.

Table 1
General Fund Overview under Current Law
(Dollar Amounts in Millions)

Line No.		Preliminary FY 2010-11	December 2011 Estimate by Fiscal Year		
			FY 2011-12	FY 2012-13	FY 2013-14
Revenue					
1	**Beginning Reserve**	**$137.4**	**$156.7**	**$491.5**	**$294.0**
2	**Gross General Fund Revenue**	**$7,085.8**	**$7,373.8**	**$7,456.3**	**$7,920.6**
3	*Net Transfers to/(from) the General Fund*	**$150.1**	**$124.8**	**($5.9)**	**($5.8)**
4	**TOTAL GENERAL FUND AVAILABLE FOR EXPENDITURE**	**$7,373.2**	**$7,655.2**	**$7,941.9**	**$8,208.8**
Expenditures					
5	**Appropriation Subject to Limit /A**	**$6,811.1**	**$6,982.3**	**$7,348.8**	**$7,401.8**
6	*Dollar Change (from prior year)*	*$179.5*	*$171.2*	*$366.5*	*$53.0*
7	*Percent Change (from prior year)*	*2.7%*	*2.5%*	*5.2%*	*0.7%*
8	**Exemptions to Limit /B**	**$8.5**	**$0.0**	**$0.0**	**$0.0**
9	**Spending Outside Limit**	**$139.0**	**$181.5**	**$299.1**	**$473.9**
10	*TABOR Refund*	*$0.0*	*$0.0*	*$0.0*	*$0.0*
11	*Rebates and Expenditures /C*	*$126.0*	*$130.5*	*$136.8*	*$155.5*
12	*Homestead Exemption*	*$1.6*	*$1.7*	*$98.5*	*$104.4*
13	*Transfers to Capital Construction /D*	*$12.0*	*$49.3*	*$63.8*	*$55.5*
14	*Transfers to Highway Users Tax Fund /D*	*N/A*	*N/A*	*$0.0*	*$158.4*
15	*Reversions and Accounting Adjustments*	*($30.9)*	*$0.0*	*$0.0*	*$0.0*
16	Enhanced Medicaid Match (reduces GF expenditures)	($0.5)	N/A	N/A	N/A
17	**TOTAL GENERAL FUND OBLIGATIONS**	**$6,927.7**	**$7,163.7**	**$7,647.9**	**$7,875.7**
Reserves					
18	**Year-End General Fund Balance**	**$445.5**	**$491.5**	**$294.0**	**$333.1**
19	*Year-End General Fund as a % of Appropriations*	*6.5%*	*7.0%*	*4.0%*	*4.5%*
20	**General Fund Statutory Reserve /E**	**$156.7**	**$279.3**	**$294.0**	**$333.1**
21	**Excess Monies Above (Below) Statutory Reserve /F**	**$288.9**	**$212.2**	**$0.0**	**$0.0**
22	*Addendum: State Education Fund /G*	*$591.9*	*$388.4*	*$389.0*	*$416.1*

Totals may not sum due to rounding.

/A Per SB 09-228, this limit equals 5.0% of Colorado personal income. The appropriations amount for Fiscal Year 2011-12 reflects current law. The amounts for FY 2012-13 and FY 2013-14 represent the level of spending that can be supported by revenue while maintaining the required reserve amounts.

/B Spending by the Medicaid program that is above the appropriated amount, called "Medicaid Overexpenditures," is usually the largest amount for this line. In FY 2010-11, Medicaid Overexpenditures amounted to $8.5 million.

/C Includes the Cigarette Rebate, Old Age Pension Fund, Property Tax, Heat, and Rent Credit, and Fire and Police Pensions Association (FPPA) contributions as outlined at the bottom of Table 2.

/D SB 09-228 requires transfers to capital construction and the Highway Users Tax Fund for FY 2013-14 since personal income is projected to increase by more than 5.0 percent in 2013.

/E Per SB 11-156, the statutory General Fund reserve required per 24-75-201.1, C.R.S. was set at 2.3% for FY 2010-11. The required reserve level increased to 4.0% in FY 2011-12. SB 09-228 requires the reserve to increase to 4.5 percent for FY 2013-14 since personal income is projected to increase by more than 5 percent in 2013.

/F Per SB 11-230, of the excess amount in FY 2010-11, $67.5 million is credited to the Public School Fund; the remainder, or $221.4 million, is transferred to the State Education Fund.

/G The State Education Fund annually receives one-third of 1% of Colorado taxable income. For FY 2011-12 only, it also receives an estimated $221.4 million of the FY 2010-11 Excess Reserve. In FY 2011-12, the fund will also receive money from the tax amnesty program created by SB 11-184. Based on preliminary collections, this amount is roughly $6.0 million. However, additional revenue is expected to be collected through the end of December. The total amount that will be credited to the fund from the program will be known in January 2012.

Table 1a

General Fund Overview with the Governor's November 1, 2011 FY 2012-13 Budget Request

(Dollar Amounts in Millions)

Line No.		Preliminary FY 2010-11	December 2011 Estimate by Fiscal Year FY 2011-12	FY 2012-13	FY 2013-14
Revenue					
1	**Beginning Reserve**	**$137.4**	**$156.7**	**$491.5**	**$618.7**
2	**Gross General Fund Revenue**	**$7,085.8**	**$7,373.8**	**$7,456.3**	**$7,920.6**
3	*Net Transfers to/(from) the General Fund*	**$150.1**	**$124.8**	**($5.9)**	**($5.8)**
4	*Net Transfers to/(from) the General Fund (Proposed)*	*N/A*	*N/A*	**$73.2**	*N/A*
5	*Proposed General Fund Revenue Changes*	*N/A*	*N/A*	**($6.1)**	**($6.1)**
6	**TOTAL GENERAL FUND AVAILABLE FOR EXPENDITURE**	**$7,373.2**	**$7,655.2**	**$8,009.0**	**$8,527.4**
Expenditures					
7	**Appropriation Subject to Limit /A**	**$6,811.1**	**$6,982.3**	**$7,189.3**	**$7,708.2**
8	*Dollar Change (from prior year)*	*$179.5*	*$171.2*	*$207.0*	*$518.9*
9	*Percent Change (from prior year)*	*2.7%*	*2.5%*	*3.0%*	*7.2%*
10	**Exemptions to Limit /B**	**$8.5**	**$0.0**	**$0.0**	**$0.0**
11	**Spending Outside Limit**	**$139.0**	**$181.5**	**$200.9**	**$472.4**
12	*TABOR Refund*	*$0.0*	*$0.0*	*$0.0*	*$0.0*
13	*Rebates and Expenditures /C*	*$126.0*	*$130.5*	*$135.3*	*$154.0*
14	*Homestead Exemption /D*	*$1.6*	*$1.7*	*$1.8*	*$104.4*
15	*Transfers to Capital Construction /E*	*$12.0*	*$49.3*	*$63.8*	*$55.5*
16	*Transfers to Highway Users Tax Fund /E*	*N/A*	*N/A*	*$0.0*	*$158.4*
17	*Reversions and Accounting Adjustments*	*($30.9)*	*$0.0*	*$0.0*	*$0.0*
18	Enhanced Medicaid Match (reduces GF expenditures)	($0.5)	N/A	N/A	N/A
19	**TOTAL GENERAL FUND OBLIGATIONS**	**$6,927.7**	**$7,163.7**	**$7,390.3**	**$8,180.6**
Reserves					
20	**Year-End General Fund Balance**	**$445.5**	**$491.5**	**$618.7**	**$346.9**
21	*Year-End General Fund as a % of Appropriations*	*6.5%*	*7.0%*	*8.6%*	*4.5%*
22	**General Fund Statutory Reserve /F**	**$156.7**	**$279.3**	**$287.6**	**$346.9**
23	**Excess Monies Above (Below) Statutory Reserve /G**	**$288.9**	**$212.2**	**$331.2**	**$0.0**
24	*Addendum: State Education Fund /H*	*$591.9*	*$388.4*	*$389.0*	*$416.1*

Totals may not sum due to rounding.

/A Per SB 09-228, this limit equals 5.0% of Colorado personal income. The appropriations amount for Fiscal Year 2011-12 reflects current law. The amount for FY 2012-13 is the Governor's November 1, 2011 budget request. The FY 2013-14 amount represents the level of spending that can be supported by revenue while maintaining the required 4.5% reserve.

/B Spending by the Medicaid program that is above the appropriated amount, called "Medicaid Overexpenditures," is usually the largest amount for this line. In FY 2010-11, Medicaid Overexpenditures amounted to $8.5 million.

/C Includes the Cigarette Rebate, Old Age Pension Fund, Property Tax, Heat, and Rent Credit, and Fire and Police Pensions Association (FPPA) contributions as outlined at the bottom of Table 2. The amounts for FY 2012-13 and FY 2013-14 incorporate the Governor's November 1, 2011 budget request to decrease funding for volunteer FPPA contributions by $1.5 million.

/D The Governor's November 1, 2011 budget request includes the suspension of the senior homestead exemption, estimated to save $96.8 million, for FY 2012-13.

/E The $63.8 million transfer to the Capital Construction Fund in FY 2012-13 is based on the assumptions contained in the Governor's November 1, 2011 budget request. This amount may be reduced by $5.9 million due to higher Federal Mineral Leasing revenue projections for FY 2012-13. SB 09-228 requires transfers to the Capital Construction Fund and the Highway Users Tax Fund for FY 2013-14 since personal income is projected to increase by more than 5.0 percent in 2013.

/F Per SB 11-156, the statutory General Fund reserve required per 24-75-201.1, C.R.S. was set at 2.3% for FY 2010-11. The required reserve level increased to 4.0% in FY 2011-12. SB 09-228 requires the reserve to increase to 4.5 percent for FY 2013-14 since personal income is projected to increase by more than 5 percent in 2013.

/G Per SB 11-230, of the excess amount in FY 2010-11, $67.5 million is credited to the Public School Fund; the remainder, or $221.4 million, is transferred to the State Education Fund.

/H The State Education Fund annually receives one-third of 1% of Colorado taxable income. For FY 2011-12 only, it also receives an estimated $221.4 million of the FY 2010-11 Excess Reserve. In FY 2011-12, the fund will also receive money from the tax amnesty program created by SB 11-184. Based on preliminary collections, this amount is roughly $6.0 million. However, additional revenue is expected to be collected through the end of December. The total amount credited to the fund from the program will be known in January 2012.

General Fund Revenue Forecast

The General Fund revenue forecast for the current budget year (FY 2011-12) is $231.0 million, or 3.2 percent, higher than the September forecast. The weakening in the economy that influenced the projections in September has reversed in certain important aspects; recent economic data point to more underlying strength and momentum in the economy than was previously evident. Revenue in FY 2011-12 is now estimated to increase 4.1 percent over FY 2010-11.

OSPB projects General Fund revenue in FY 2012-13 will grow at a slower rate of 1.1 percent. A weakening in global economic conditions and the European debt crisis are expected to slow the economy from the current pace. In addition, high stock market volatility in the fall likely caused investors to sell assets and realize capital gains that are subject to income tax. This is boosting FY 2011-12 revenue at the expense of collections in FY 2012-13, when fewer capital gains will be realized. However, with higher revenue collections this fiscal year raising the base amount from which next year's revenue will grow, this forecast projects that FY 2012-13 General Fund revenue will be $100.8 million, or 1.4 percent, higher than projected in September.

In addition to the economic reasons for the slower revenue growth rate in FY 2012-13, a few tax policy changes are affecting revenue. The sections below on income tax and sales tax revenue discuss these changes. Further, accrual accounting changes will slow revenue growth in FY 2012-13 compared with FY 2011-12. Accrual adjustments are required so revenue collected is accounted for in the fiscal year in which the economic activity that generated the revenue occurs. This fiscal year's revenue is bolstered by expected large accrual adjustments that will not occur in FY 2012-13. Without these accrual and tax policy changes, FY 2012-13 revenue growth would be closer to the current fiscal year's growth rate.

Even with the increase in revenue projected by this forecast, General Fund revenue in FY 2012-13 is expected to still be $286.6 million, or 3.7 percent, below its pre-recession level in FY 2007-08.

Projections for income, excise, and all other General Fund revenue sources can be found in Table 2.

Individual and Corporate Income Taxes

Individual income – Individual income tax revenue is expected to grow 6.6 percent in FY 2011-12. Stronger-than-expected job growth is causing income taxes withheld from workers' paychecks to come in higher than was projected in September. Income tax withholding represents about 55 percent of total General Fund revenue. Revenue growth from income tax withholding will be muted in FY 2012-13 due to an expected modest slowdown in job growth and from an accrual accounting adjustment. This adjustment is due to the timing of the payroll period at the end of the fiscal year that will bolster FY 2011-12 revenue relative to FY 2012-13.

Income tax revenue from estimated payments is the third largest General Fund tax revenue source behind income tax withholding and sales taxes. The two largest contributors to this revenue are typically capital gains and owners of small and medium sized businesses. After surging 38.2 percent in FY 2010-

11, revenue from this source is expected to post a more modest growth rate of 7.2 percent this fiscal year.

As previously noted, the recent stock market volatility is assumed to have generated increased capital gains. The anticipated federal tax increases on capital gains at the end of 2012 may also have contributed to selling to take advantage of the current lower tax rates. As investors recently sold off stocks, there is expected to be fewer capital gains in FY 2012-13 and thus less estimated income tax payments, particularly due to expectations of a relatively weak and volatile stock market from continued uncertainty regarding Europe's debt crisis.

Corporate income – An apportionment of corporations' profits based on sales in the state determines Colorado's corporate income tax revenue. Profits grew robustly for many companies beginning with the rebound in economic activity, especially as a result of their large productivity gains after cutting costs to survive the recession. However, profit growth is projected to slow for FY 2011-12 and FY 2012-13. Companies are not expected to continue to benefit from the same productivity gains that increased their margins after the recession. Further, a rise in costs, especially from increasing employee health care benefits, and a modest slowing in sales will constrain profits. These factors, along with the December 2010 federal tax policy change that increases tax deductions for business equipment purchases, will cause corporate income tax revenue to decline a projected 3.4 percent in FY 2011-12. Corporate income tax revenue will increase by a modest 3.9 percent in FY 2012-13.

Sales and Other Excise Taxes

Sales and use tax revenue represents a little over 30 percent of total General Fund revenue. Growth in these revenue sources jumped in FY 2010-11 as both consumers and business resumed their spending when the economy began to improve. Use tax revenue was bolstered by businesses replacing outdated and obsolete equipment after postponing such purchases during the recession. Thus, the surge last fiscal year was mostly a one-time event and spending for this fiscal year and FY 2012-13 will post only modest increases. Recent data, at least at the national level, has shown weakening in disposable income and household net worth due to the stock market volatility and continued weak home prices. This will weigh on consumer spending. More details on these trends can be found in the consumer spending section of the *Economic Conditions and Forecast* section on page 19 of this publication.

In addition, sales and use tax revenue to the state this fiscal year and in FY 2012-13 will show lower growth than actual spending would suggest. This is mostly as a result of certain tax policy changes. Of particular note, the partial resumption of the vendor discount this fiscal year, which allows a portion of sales taxes collections to be retained by retailers, will serve to reduce sales tax revenue collections in FY 2011-12 by about $46 million. In addition, the scheduled reinstatement of the sales tax exemption on energy used for manufacturing and industrial purposes will decrease sales tax revenue starting in FY 2012-13 by about $40 million. HB 11-1293 reinstates the exemption of certain software purchases and is estimated to decrease sales tax revenue by about $20 million in FY 2012-13.

Revenue from smaller excise tax sources, including cigarette, tobacco, and liquor taxes, will remain flat over the forecast period.

Table 2
Colorado General Fund – Revenue Estimates by Tax Category
(Accrual Basis, Dollar Amounts in Millions)

Line No.	Category	Preliminary FY 2010-11	% Chg	December 2011 Estimate by Fiscal Year FY 2011-12	% Chg	FY 2012-13	% Chg	FY 2013-14	% Chg
	Excise Taxes:								
1	Sales	$2,043.5	12.0%	$2,043.6	0.0%	$2,062.3	0.9%	$2,161.1	4.8%
2	Use	$190.1	22.0%	$194.1	2.1%	$200.3	3.2%	$210.9	5.3%
3	Cigarette	$39.3	-3.8%	$39.3	-0.1%	$36.8	-6.2%	$36.2	-1.9%
4	Tobacco Products	$13.8	-14.2%	$17.7	28.4%	$17.6	-0.5%	$18.3	3.5%
5	Liquor	$36.4	2.8%	$37.7	3.4%	$39.3	4.2%	$40.6	3.3%
6	**Total Excise**	**$2,323.1**	**12.1%**	**$2,332.4**	**0.4%**	**$2,356.4**	**1.0%**	**$2,467.0**	**4.7%**
	Income Taxes:								
7	Net Individual Income	$4,496.1	10.1%	$4,792.8	6.6%	$4,785.8	-0.1%	$5,073.9	6.0%
8	Net Corporate Income	$393.9	5.9%	$380.6	-3.4%	$395.6	3.9%	$428.7	8.4%
9	**Total Income**	**$4,890.0**	**9.7%**	**$5,173.4**	**5.8%**	**$5,181.4**	**0.2%**	**$5,502.7**	**6.2%**
10	*Less: State Education Fund Diversion*	*$370.5*	*12.6%*	*$388.4*	*4.8%*	*$389.0*	*0.1%*	*$416.1*	*7.0%*
11	**Total Income to General Fund**	**$4,519.5**	**9.5%**	**$4,785.0**	**5.9%**	**$4,792.5**	**0.2%**	**$5,086.6**	**6.1%**
	Other Revenues:								
12	Estate	($0.1)	N/A	$0.0	N/A	$45.0	N/A	$94.0	108.9%
13	Insurance	$189.7	1.5%	$206.2	8.8%	$209.7	1.7%	$214.8	2.4%
14	Interest Income	$7.9	-21.6%	$8.4	5.6%	$11.8	40.9%	$15.9	34.7%
15	Pari-Mutuel	$0.5	-0.6%	$0.6	3.4%	$0.4	-23.1%	$0.4	-6.2%
16	Court Receipts	$3.6	-80.0%	$1.3	-64.9%	$0.3	-80.0%	$0.3	0.0%
17	Gaming	$20.4	25.9%	$20.3	-0.5%	$20.3	0.0%	$20.3	0.0%
18	Other Income	$21.2	-18.8%	$19.7	-7.3%	$20.0	1.7%	$21.4	7.0%
19	**Total Other**	**$243.2**	**-5.6%**	**$256.4**	**5.4%**	**$307.5**	**19.9%**	**$367.0**	**19.4%**
20	**GROSS GENERAL FUND**	**$7,085.8**	**9.7%**	**$7,373.8**	**4.1%**	**$7,456.3**	**1.1%**	**$7,920.6**	**6.2%**
	Rebates & Expenditures:								
21	Cigarette Rebate	$11.0	-5.3%	$11.1	0.7%	$10.4	-6.2%	$10.2	-1.9%
22	Old-Age Pension Fund	$102.2	-11.4%	$100.1	-2.1%	$102.3	2.2%	$105.8	3.5%
23	Aged Property Tax & Heating Credit	$6.8	-10.0%	$7.4	9.2%	$7.4	-1.3%	$7.4	1.0%
24	Interest Payments for School Loans	$0.8	-63.7%	$1.4	74.1%	$1.6	14.3%	$1.6	0.0%
25	Fire/Police Pensions	$4.3	1.3%	$9.6	123.5%	$14.3	48.3%	$29.6	107.4%
26	Amendment 35 General Fund Expenditure	$0.9	-1.9%	$0.9	0.0%	$0.8	-3.4%	$0.8	-1.0%
27	**Total Rebates & Expenditures**	**$126.0**	**-11.2%**	**$130.5**	**3.6%**	**$136.8**	**4.8%**	**$155.5**	**13.7%**

Cash Fund Revenue Forecast

OSPB forecasts cash fund revenue subject to TABOR to grow $101.9 million and total $2.4 billion in FY 2011-12, a 4.3 percent increase over FY 2010-11. In FY 2012-13, OSPB forecasts cash fund revenue growth of $52.7 million, or 2.2 percent. Revenue growth in the hospital provider fee, severance tax, and transportation categories accounts for much of the expected increase in FY 2011-12. The relatively small growth rate in FY 2012-13 is due to a slight decline in severance tax revenue and smaller growth rates in the other main cash fund revenue sources. Notable changes since the September 2011 OSPB forecast include downward revisions to provider fee and miscellaneous revenue estimates. Provider fee estimates have been revised to reflect updated cost estimates, and the miscellaneous revenue forecast has been revised due to weak year-to-date revenue collections. The following discusses the forecasts for these major cash fund revenue sources, which are presented in Table 3.

Transportation-Related Cash Funds

Total transportation-related cash fund revenue, which includes revenue to the Highway Users Tax Fund, the State Highway Fund, and other various smaller transportation cash funds, is forecast to total $1.1 billion in FY 2011-12, an increase of 2.1 percent from FY 2010-11. OSPB forecasts FY 2012-13 collections to total 1.12 billion, an increase of 0.8 percent.

Most transportation revenue is from vehicle registrations, fuel sales, and license and permit issuances. In 2011, both car and light truck sales rebounded over the course of the year. Vehicle sales affect transportation revenue as they result in increased registrations and license and permit revenue. Fuel tax revenue, which typically comprises slightly more than half of Highway Users Tax Fund revenue, increased in FY 2010-11 and year-to-date collections suggest similar growth in FY 2011-12. Additionally, driver's license revenue is expected to increase through the forecast period because of changes to the renewal cycle. In 2005, the passage of SB 05-047 changed the driver's license renewal cycle from a ten -year cycle to a five-year cycle. The overlap of the conclusion of the ten-year cycle and the five-year cycle has increased the number of licenses issued and license revenue.

Other notable legislation to affect transportation revenue includes HB 10-1387, which will cause the transfer of approximately $22.1 million from the Highway Users Tax Fund to the Licensing Services cash fund in FY 2011-12. This transfer will not affect total transportation revenue in FY 2011-12, but it will decrease the amount in the Highway Users Tax Fund and increase the amount in other miscellaneous cash funds. The Governor's FY 2012-13 budget request proposes to make this transfer permanent.

SB 11-184 temporarily reduces the penalty for payment of overdue state taxes, and a portion of the revenue collected from the program from overdue fuel taxes will be credited to the HUTF. While the final amount will be known in January 2012, preliminary collection data suggests about $3,500 will be credited to the HUTF from the program.

Limited Gaming

FY 2011-12 gaming revenue is projected to decrease 10.4 percent and total $96.8 million. Of this amount, $6.7 million is expected to be "extended limited gaming" revenue, which is exempt from TABOR per Amendment 50. This amendment to the Colorado Constitution resulted in increased betting limits, more types of gaming, and extended gaming hours. The remaining $90.1 million is subject to TABOR and is shown in Table 4 of this forecast. The FY 2011-12 decline in gaming revenue reflects less household wealth as a result of the economic downturn and a Gaming Commission tax rate reduction of 5.0 percent. This tax change will reduce gaming tax revenue collections in FY 2011-12 by an estimated $5.2 million.

FY 2012-13 gaming revenue is forecast to grow modestly and total $99.7 million, of which $7.0 million is expected to be extended limited gaming revenue. Additionally, the Governor's FY 2012-13 budget request proposes the use of $6.1 million of the gaming revenue transfer to the General Fund for film incentives and the Governor's Energy Office. Figure 1 outlines the forecast for total gaming revenue and its allocation under current law.

Figure 1. Distribution of Limited Gaming Revenues

Distribution of Limited Gaming Revenues	Actual FY10-11	Forecast FY11-12	Forecast FY 12-13	Forecast FY 13-14
A. Total Limited Gaming Revenues	**$108.0**	**$96.8**	**$99.7**	**$104.9**
Annual Percent Change	0.3%	-10.4%	3.0%	5.2%
B. Base Limited Gaming Revenues (max 3% growth)	**$97.7**	**$87.6**	**$90.2**	**$92.9**
C. Total Amount to Base Revenue Recipients	**$86.4**	**$76.0**	**$80.5**	**$83.3**
Amount to State Historical Society	*$24.2*	*$21.3*	*$22.5*	*$23.3*
Amount to Counties	*$10.4*	*$9.1*	*$9.7*	*$10.0*
Amount to Cities	*$8.6*	*$7.6*	*$8.0*	*$8.3*
Amount to Distribute to Remaining Programs (State Share)	*$43.2*	*$38.0*	*$40.2*	*$41.7*
Amount to Local Government Impact Fund	*$3.6*	*$2.8*	*$3.2*	*$3.4*
Colorado Tourism Promotion Fund	*$12.0*	*$9.4*	*$10.5*	*$11.2*
Film Incentives Fund	*$0.2*	*$0.2*	*$0.2*	*$0.2*
Creative Industries Cash Fund	*$1.0*	*$0.8*	*$0.8*	*$0.9*
Bioscience Discovery Evaluation Fund	*$4.3*	*$3.4*	*$3.8*	*$4.0*
Innovative Higher Education Research Fund	*$1.7*	*$1.3*	*$1.5*	*$1.6*
Transfer to the General Fund	*$20.4*	*$20.3*	*$20.3*	*$20.3*
D. Total Amount to Amendment 50 Revenue Recipients	**$8.9**	**$6.7**	**$5.3**	**$8.6**
Community Colleges, Mesa and Adams State (78%)	*$7.0*	*$5.2*	*$4.2*	*$6.7*
Counties (12%)	*$1.1*	*$0.8*	*$0.6*	*$1.0*
Cities (10%)	*$0.9*	*$0.7*	*$0.5*	*$0.9*

Hospital Provider Fee

Hospital provider fee revenue comes from the payment of hospital provider fees, authorized by HB 09-1293. The program increases Medicaid reimbursements to hospitals paying the fee. Most hospitals in the state pay the fees, which are equivalent to a per-day payment for inpatient hospital services and a percentage of charges for outpatient hospital services. Revenue from the fees is expected to increase

$123.9 million in FY 2011-12 and $34.7 million in FY 2012-13, which are growth rates of 28.0 percent and 6.1 percent, respectively.

Provider fee revenue is forecast to increase as the program-eligible population is expanded and payments from providers due to this expansion increase accordingly. However, the estimates are less for each year compared with the September 2011 forecast due to reduced population cost estimates, which results in lower provider fee revenue necessary to cover such costs.

Legislation passed during the 2011 legislative session, SB 11-212, will increase revenue by increasing fees paid to the Hospital Provider Fee Cash Fund by an estimated $50 million in FY 2011-12 and $25 million in FY 2012-13. This revenue will offset state General Fund expenditures for the Medicaid program during those fiscal years.

Provider fee revenue is projected to decline in FY 2013-14 because, under the federal Affordable Care Act, certain populations will be eligible for a 100 percent federal fund match, therefore provider fee revenue will not be collected for these populations. The Office of State Planning and Budgeting would like to recognize the Department of Health Care Policy and Financing for its assistance in forecasting provider fee revenue.

Severance Tax

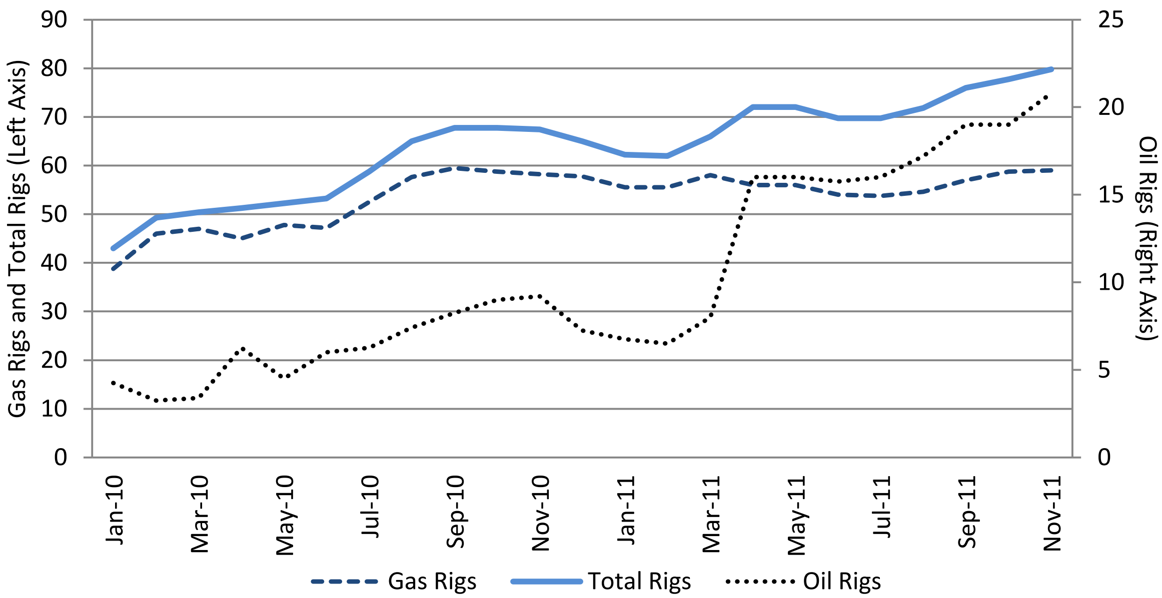
OSPB expects severance tax revenue to total $197.6 million in FY 2011-12 and $189.2 million in FY 2012-13. Natural gas production is projected to increase through the forecast period as a result of an increase in drilling rigs and other investments in the state by natural gas companies. Natural gas prices are forecast to average $4.14 per thousand cubic feet (Mcf) in 2011 and $3.95 per Mcf in 2012. High storage inventories and mild early winter temperatures have kept prices lower-than-expected in 2011. An abundance of supply is expected to keep natural gas prices below $4.50 per MMcf through 2014.

Some tax revenue which had been expected in FY 2010-11 is instead being collected in FY 2011-12 due to a lag in when oil and gas activity occurred and the severance tax liability associated with that activity. The shift in revenue to FY 2011-12 combined with lower projected natural gas prices in 2012 are the main reasons for the decrease in severance tax revenue in FY 2012-13.

While natural gas prices and production levels are the primary factors that affect severance tax revenue, recently attention has been paid to increased oil exploration and production activity in northeastern Colorado. The Niobrara formation is the site of most new oil activity in Colorado and exploratory activity continues to increase, particularly in Weld County. Figure 2 shows the change in oil and gas drilling rig counts since 2010. Although both oil and gas drilling rigs continue to increase, the figure shows a substantial uptick in oil rigs operating in the state. Most of these new oil rigs are in Weld County, and new rigs are a leading indicator for production. Thus, there is potential for strong growth in oil production in the area which would benefit the state economy.

Production activity in Weld County is forecast to increase over time as more wells come on line, but the impact of increased production on revenue collections is expected to be constrained by the ad valorem severance tax credit available to taxpayers. This credit is based on the property tax paid on the value oil and gas production. Weld County has a higher property tax rate than most other large oil and gas producing counties, which will result in higher tax credits to offset the growth in severance tax liability from the increasing oil production. Oil prices for Colorado producers are forecast to average $87 per barrel in 2011 and $95 per barrel in 2012.

Figure 2. Colorado Monthly Oil and Gas Drilling Rig Count, 2010 through November 2011



Source: Baker Hughes

Severance tax revenue from coal production is forecast to increase in FY 2011-12 after decreasing in recent years. The rebound in economic activity and the opening of a large new coal mine in southeast Colorado are contributing to the increase this year. However coal severance tax revenue is expected to gradually decline over the remainder of the forecast period due to the increasing use of other energy sources to meet the economy's energy needs. For example, the Colorado Clean Air Clean Jobs Act requires Colorado utilities to decrease nitrogen oxide emissions by retiring, retrofitting or repowering coal-fired power plants by the end of 2017 and replace them with other sources with fewer emissions. The state's plan under the Act involves using more natural gas for its energy generation.

Like with the fuel taxes to the HUTF, the state is receiving the payment of overdue severance taxes as a result of the program created by SB 11-184. Preliminary collections data show that $1.5 million has been collected. The total amount collected will be known in January 2012. This money will be credited to the State Severance Tax Cash Fund in FY 2011-12.

Federal Mineral Leasing Revenue

When federal lands are leased for mineral extraction, the federal government and the state of Colorado realize a share of the revenue from the production activity. Continued production on federal lands, particularly in northwest Colorado, is expected to increase Federal Mineral Leasing (FML) revenue through the forecast period. However, lower natural gas prices in 2012 will temper the FY 2012-13 increase. Figure 3 outlines the forecast of FML revenue. FML revenue comes from the federal government, which makes it exempt from TABOR. Thus, the amounts below are not reflected in the cash fund TABOR revenue forecast shown in Table 3.

Figure 3. Federal Mineral Leasing (FML) Payments

Fiscal Year	Bonus Payments	Non-Bonus Payments	Total FML Revenue	Percentage Change
FY 2009-10	$5.20	$117.20	$122.50	-46.1%
FY 2010-11	$2.26	$147.2	$149.48	22.0%
FY 2011-12	$5.1	$165.0	$170.10	13.8%
FY 2012-13	$6.1	$168.6	$174.70	2.7%
FY 2013-14	$9.5	$179.7	$189.13	8.3%

Dollars are in millions. FY 2009-10 and 2010-11 figures reflect actual collections, and FY 11-12 through FY 2013-14 are projections.

Other Cash Funds

Insurance-related cash fund revenue includes all insurance premiums collected for major medical insurance, subsequent injury, and worker's compensation. Insurance-related cash funds are expected to total $16.3 million in FY 2011-12 and $17.1 million in FY 2012-13. The Colorado Department of Regulatory Agencies is primarily cash funded by regulated entities, and its cash fund revenue is expected to total $63.9 million in FY 2011-12 and $65.6 million in FY 2012-13.

Year-to-date collections of other miscellaneous cash fund revenue subject to TABOR are below prior year levels, and this revenue is projected to decrease $61.6 million in FY 2011-12 compared to FY 2010-11. This category is broad and includes numerous cash fund revenue sources, mainly from licenses, fines, and fees as well as interest earnings on various cash funds.

As discussed in the transportation and severance tax revenue sections, SB 11-184 allows taxpayers to pay certain overdue state and local taxes, including one-half of any interest due, without being subject to any fine or civil or criminal penalty otherwise provided for by law. The money collected from overdue income and sales taxes is credited to a special cash fund, of which about $1 million will be used to reimburse the Department of Revenue for administering the program and to fund tax and expenditure studies, while $175,000 will be appropriated to the Family Medicine Residency Training program in the Department of Health Care Policy and Financing. The remainder in the fund will be transferred to the State Education Fund; preliminary collection data shows that this amount is roughly $6.0 million. However, additional revenue is expected to be collected through the end of December. A final total of all overdue taxes collected from the program will be available in January.

Table 3

Cash Fund Revenue Forecasts by Major Category

(Dollar amount in millions)

Category	Actual FY 2010-11	December 2011 Estimate by Fiscal Year FY 2011-12	FY 2012-13	FY 2013-14	FY 2010-11 to FY 2013-14 CAAGR*
Transportation-Related /A	$1,082.7	$1,106.0	$1,115.2	$1,127.3	
Change	2.2%	2.1%	0.8%	1.1%	1.4%
Limited Gaming Fund /B	$98.0	$87.6	$90.2	$92.9	
Change	-3.2%	-10.6%	3.0%	3.0%	-1.8%
Capital Construction - Interest	$3.0	$0.8	$0.9	$0.9	
Change	-7.8%	-73.3%	6.9%	5.0%	-33.1%
Regulatory Agencies	$69.6	$63.9	$65.6	$67.4	
Change	3.3%	-8.1%	2.7%	2.7%	-1.0%
Insurance-Related /C	$26.5	$16.3	$17.1	$17.4	
Change	-38.3%	-38.3%	4.4%	2.0%	-13.1%
Severance Tax	$149.4	$194.1	$183.3	$229.5	
Change	209.6%	29.9%	-5.5%	25.2%	15.4%
Medicaid Hospital Provider Fees	$442.6	$566.5	$601.2	$546.5	
Change	46.1%	28.0%	6.1%	-9.1%	7.3%
Other Miscellaneous Cash Funds	$472.0	$410.4	$424.7	$432.4	
Change	1.7%	-13.1%	3.5%	1.8%	-2.9%
TOTAL CASH FUND REVENUE	***$2,343.7***	***$2,445.5***	***$2,498.2***	***$2,514.3***	
Change	12.2%	4.3%	2.2%	0.6%	2.4%

* CAAGR: Compound Annual Average Growth Rate.

/A Revenue beginning in FY 2009-10 include the impact of SB 09-108 (FASTER).

/B Revenue excludes any impact from Amendment 50 as these revenues are exempt from TABOR. Exempted revenues are projected based on the formula outlined per HB 09-1272.

/C Pursuant to SB 09-037, beginning in FY 2010-11 the Workers' Compensation surcharge that is applicable for the Major Medical and Subsequent Injury cash fund will no longer be applied until the available balance in said fund falls below the unrestricted cash fund balance plus one year's worth of direct and indirect operating expenses for these programs.

The Taxpayer's Bill of Rights: Revenue Limit

The Taxpayer's Bill of Rights (TABOR) – Article X, Section 20 of the Colorado Constitution – limits the state's revenue growth to the sum of inflation plus population growth in the previous calendar year. Under the provisions of TABOR, revenue collected above the TABOR limit must be returned to taxpayers, unless voters decide the State can retain the revenue. In November 2005, voters approved Referendum C, which allows the State to retain all revenue through FY 2009-10, during a five-year TABOR "time out." Referendum C also set a new cap on revenue starting in FY 2010-11. Table 4 summarizes the forecasts of TABOR revenue, the TABOR revenue limit, and the revenue cap under Referendum C.

Beginning in FY 2010-11, the amount of revenue that the State may retain under Referendum C (line 9) is computed by multiplying the revenue limit between FY 2005-06 and FY 2009-10 associated with the highest TABOR revenue year (FY 2007-08) by the allowable TABOR growth rates (line 6) for each subsequent year. OSPB does not project that any refunds will occur during the forecast period (line 10).

TABOR requires that the population estimates used to determine the revenue limit be adjusted every decade to match the federal census. The 2010 federal census indicates that Colorado's population was overestimated during the 2000s decade. Thus, in order to account for this overestimate, the percent change in population (line 4 of Table 4) that will affect the FY 2011-12 revenue limit was lowered.

Table 4
TABOR Revenue & Referendum C Revenue Limit
(Dollar Amounts in Millions)

Line No.		Preliminary FY 2010-11	December 2011 Estimate by Fiscal Year FY 2011-12	FY 2012-13	FY 2013-14
	TABOR Revenues:				
1	General Fund /A	$7,057.7	$7,353.5	$7,436.0	$7,900.3
	Percent Change from Prior Year	*8.9%*	*4.2%*	*1.1%*	*6.2%*
2	Cash Funds	$2,366.9	$2,445.5	$2,498.2	$2,514.3
	Percent Change from Prior Year	*13.3%*	*3.3%*	*2.2%*	*0.6%*
3	**Total TABOR Revenues**	**$9,424.6**	**$9,799.1**	**$9,934.2**	**$10,414.7**
	Percent Change from Prior Year	*10.0%*	*4.0%*	*1.4%*	*4.8%*
	Revenue Limit Calculation:				
4	Previous calendar year population growth	*1.8%*	*0.1%*	*1.4%*	*1.5%*
5	Previous calendar year inflation	*-0.6%*	*1.9%*	*3.5%*	*2.3%*
6	**Allowable TABOR Growth Rate**	***1.2%***	***2.0%***	***4.9%***	***3.8%***
7	TABOR Limit	$8,654.4	$8,827.5	$9,260.0	$9,611.9
8	General Fund Exempt Revenue Under Ref. C /B	$770.3	$971.6	$674.2	$802.8
9	**Revenue Cap Under Ref. C /C**	**$10,684.9**	**$10,898.6**	**$11,432.6**	**$11,867.0**
10	*Amount Above/(Below) Limit*	*($1,260.2)*	*($1,099.5)*	*($1,498.4)*	*($1,452.4)*
11	TABOR Reserve Requirement	$282.7	$294.0	$298.0	$312.4

/A Amounts differ from the General Fund revenues reported in Table 3 (General Fund Revenues) as some double counting exists when cash funds are transferred to the General Fund (for instance, limited gaming revenues), and due to other accounting adjustments.

/B Under Referendum C, a "General Fund Exempt Account" is created in the General Fund. The account consists of money collected in excess of the TABOR limit in accordance with voter-approval of Referendum C.

/C The revenue limit is calculated by applying the "Allowable TABOR Growth Rate" to either "Total TABOR Revenues" or the "Revenue Cap Under Ref. C," whichever is smaller. Beginning in FY 2010-11, the revenue limit is based on the highest revenue total from FY 2005-06 to 2009-10 plus the "Allowable TABOR Growth Rate." FY 2007-08 was the highest revenue year during the Referendum C period.

The Economy: Current Conditions and Forecast

Since the publication of the September forecast, the economy has shown welcome improvement after worrisome signs of weakening over the spring and summer months. The jobs market has seen much of the improvement, particularly Colorado's. Continued expansion in some of the state's goods producing sectors, such as manufacturing and oil and gas, has particularly bolstered Colorado's economy. Businesses have also become more optimistic since the summer.

However, the economy is still only expanding modestly and unevenly as it continues the difficult process of rebuilding from the credit and housing boom and bust. This process will continue to take time and prevent the economy from experiencing more sustained, robust growth. The difficulty of this process is reflected in the latest data on new business activity in the state, which is an important contributor to job growth. New business creation remains modest as entrepreneurs are still struggling to accessing credit and discover ways to satisfy consumer demand as the economy restructures.

Further, just as the economy is beginning to show signs of increased momentum, global economic conditions have slowed. Most notably, the debt crisis in Europe has led to a marked downturn in economic activity there. The global slowdown, coupled with strains in the global financial system stemming from the European crisis, will slow growth in the economy in 2012. Supporting this projection, recent data on income and household wealth suggest that it will be difficult for consumers to maintain current spending levels without a stronger recovery in the job and housing markets.

Both the situation in Europe and stress in the financial system pose major downside risks to the forecast, though the outcome and effects of the crisis are impossible to predict. If the situation does not deteriorate, reduced trade, less investment from Europe, and tightened credit conditions will only moderately impact the national and state economies. Alternatively, the crisis in Europe could improve and the economy could sustain, or even accelerate, recent momentum. As a result, economic conditions would be better than this forecast projects. The history and projections for key Colorado economic indicators are shown in Table 5, on page 45, while the economic indicators for the nation are shown in Table 6, on page 46.

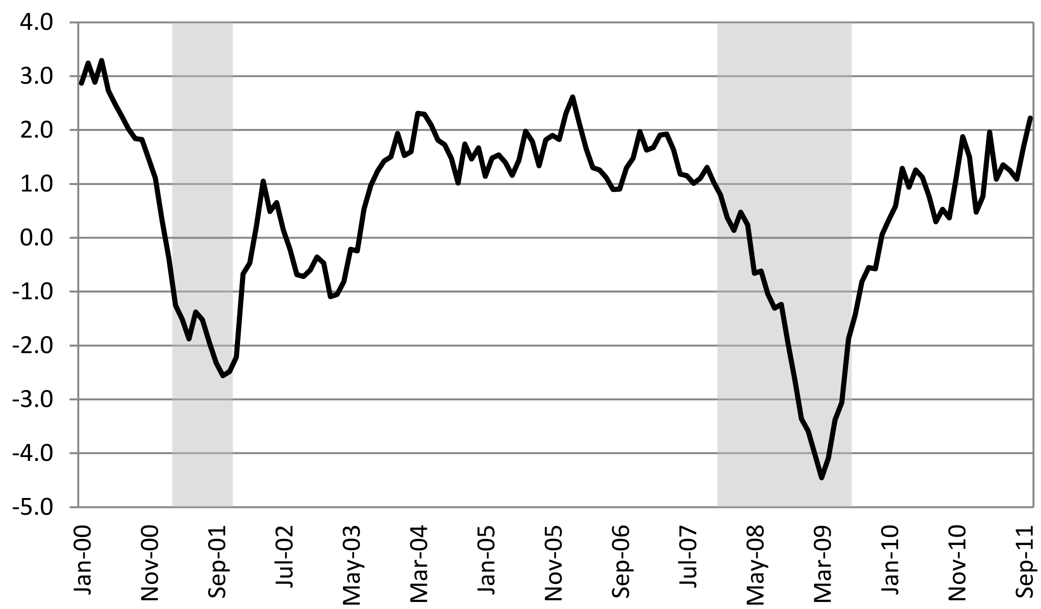
Overall Conditions

Colorado's economy has gained momentum – In certain important aspects, Colorado's economy is outperforming the nation in the rebuilding process. Surveys of businesses indicate more optimism. Indicators regarding the job market and income show stronger improvement and Colorado's unemployment rate is lower than the nation's. Colorado's business climate, industry mix − the growing oil and gas industry, for example− and educated workforce position the state well relative to many others in the national recovery. The 2011 CNBC ranking of the best states for business placed Colorado in the top five states overall.

Recent data point to continued near-term growth in the state's economy. Leading indicators are measures of specific economic activities that have been found to exhibit certain patterns before the economy slows or expands. Patterns in these activities are used to identify whether the level of economic activity is expected to decline or rise over the subsequent six to nine months.

Figure 4 shows an index of leading indicators for the state's economy constructed by the Philadelphia Federal Reserve Branch. The index shows that the state economy is likely to continue expanding in the near term. Among the activities the state leading index uses are housing permits, initial unemployment insurance claims, and delivery times from vendors to producers. This last component of the index can lead changes in economic activity because an increase or decrease in delivery time can indicate rising or slowing demand for supplies used in production.

Figure 4. Index of Leading Indicators for Colorado's Economy, 2000 through October 2011



Source: Philadelphia Federal Reserve, Gray shaded areas show national recessions as determined by the National Bureau of Economic Research

National business conditions – The Institute for Supply Management's (ISM) indices for both manufacturing and non-manufacturing businesses at the national level are hovering near 50 – an index reading above 50 indicates that the industries overall are expanding, while a reading below 50 indicates contraction. Industry performance within the manufacturing and non-manufacturing categories is mixed as sectors in each grapple with unique challenges.

Manufacturing conditions mixed **–** The ISM Purchasing Managers' Index for manufacturing businesses was 52.7 in November 2011, a slight increase from October. Most survey participants remained relatively optimistic about business conditions. For example, a representative from an electrical equipment, appliances & components company noted orders have increased after an extended "summer dip" in sales overall and expected sales to finish the year approximately 10 percent above 2010. However, reflecting the still modest hiring occurring in the economy, a representative's response from the food, beverage and tobacco products sector indicated that hiring remained suppressed, and companies are trying to achieve greater output without increasing payrolls.

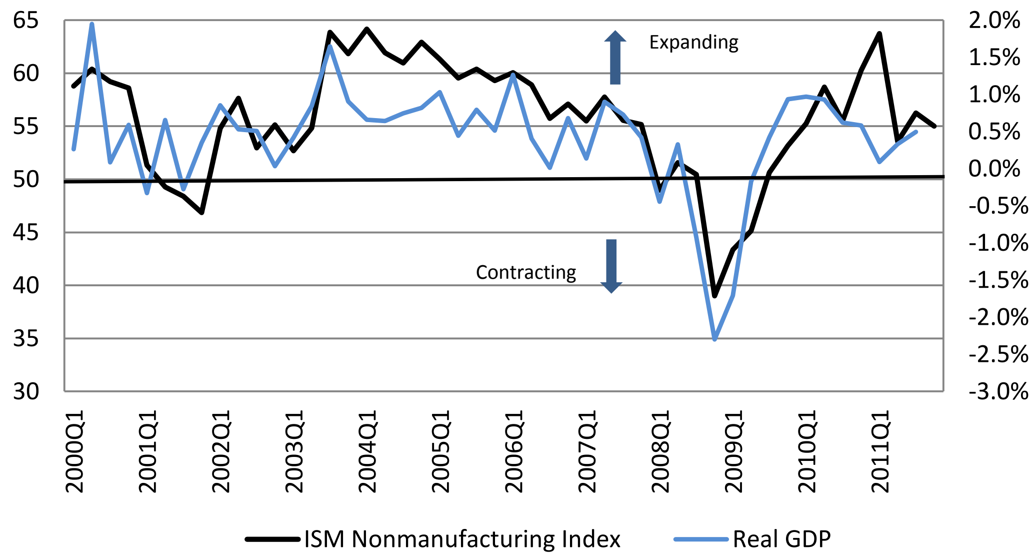
Despite the near 50 reading for manufacturing, U.S. manufacturing profits remained strong in the third quarter of 2011. Although down 4.5 percent from the second quarter, third quarter profits were still 20.4 percent greater than the same quarter in 2010. However, in more negative news for the sector, industrial production dropped slightly in November for the first time in seven months. Industrial production represents the production of all goods in the U.S., or all the output of factories, mines, and utilities.

***Non-manufacturing conditions also mixed* –** The ISM Non-manufacturing Businesses Index was 52.0 in November 2011, down slightly from October. The reading was the lowest since January 2010 when the index was 50.7. Although the latest index still suggests continued growth in the non-manufacturing sector, the slight downturn in the index is notable as the sector includes the services industry − the largest part of the U.S. economy.

Overall, survey participants had a mixed assessment of non-manufacturing business conditions. A representative from the retail trade sector noted business is slowly improving and the outlook for the next few months is good. However, a representative from the accommodation and food services sector saw no signs of a turnaround, pointing to customer nervousness about the future of their jobs and incomes which is resulting in diminished sales and less need for additional hiring. The retail trade, mining and information sectors reported the strongest growth in the November survey, while the construction, agriculture, and finance and insurance sectors reported contraction.

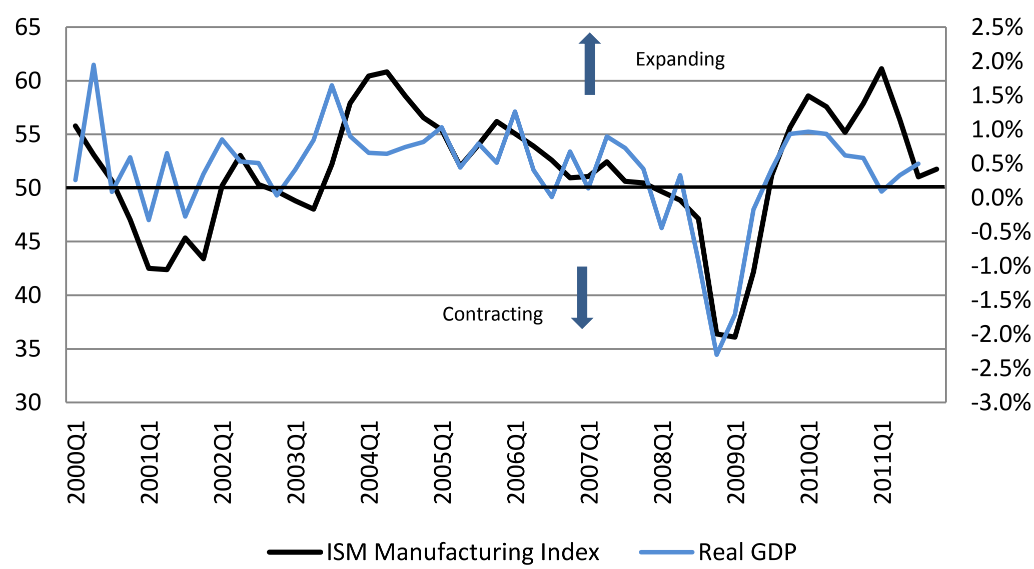
Figures 5 and 6 below show the ISM indices demonstrating the performance of the manufacturing and non-manufacturing businesses compared with growth in the economy as measured by real, or price-adjusted, national Gross Domestic Product (GDP) over time. The two indices track closely with changes in the economy over time. Based on these graphs, unless the manufacturing and non-manufacturing sectors begin to show more expansion, overall economic growth is likely to be subdued

Figure 5. Comparison of Change in ISM Non-manufacturing Business Activity Index and Inflation-adjusted Gross Domestic Product



Source: Institute for Supply Management (ISM) Report on Business, ISM Non-manufacturing Business Activity Index, seasonally adjusted quarterly average of the monthly index; U.S. Bureau of Economic Analysis

Figure 6. Comparison of Change in ISM Manufacturing Composite Index and Inflation-adjusted Gross Domestic Product



Sources: Institute for Supply Management (ISM) Report on Business, ISM Manufacturing PMI Composite Index (NAPM), seasonally adjusted quarterly average of the monthly index; U.S. Bureau of Economic Analysis

Small business conditions **–** The National Federation of Independent Businesses (NFIB) Small Business Optimism Index, which gauges sentiment among small businesses nationally, has improved from the low levels seen in the summer when economic activity was faltering. It gained 1.8 points and totaled 92.0 in November. According to the NFIB, November gains were due to improvement in labor market components, expectations for real sales gains, and the outlook for business conditions becoming less negative. Despite the November gain in optimism, business expansion activity remains low.

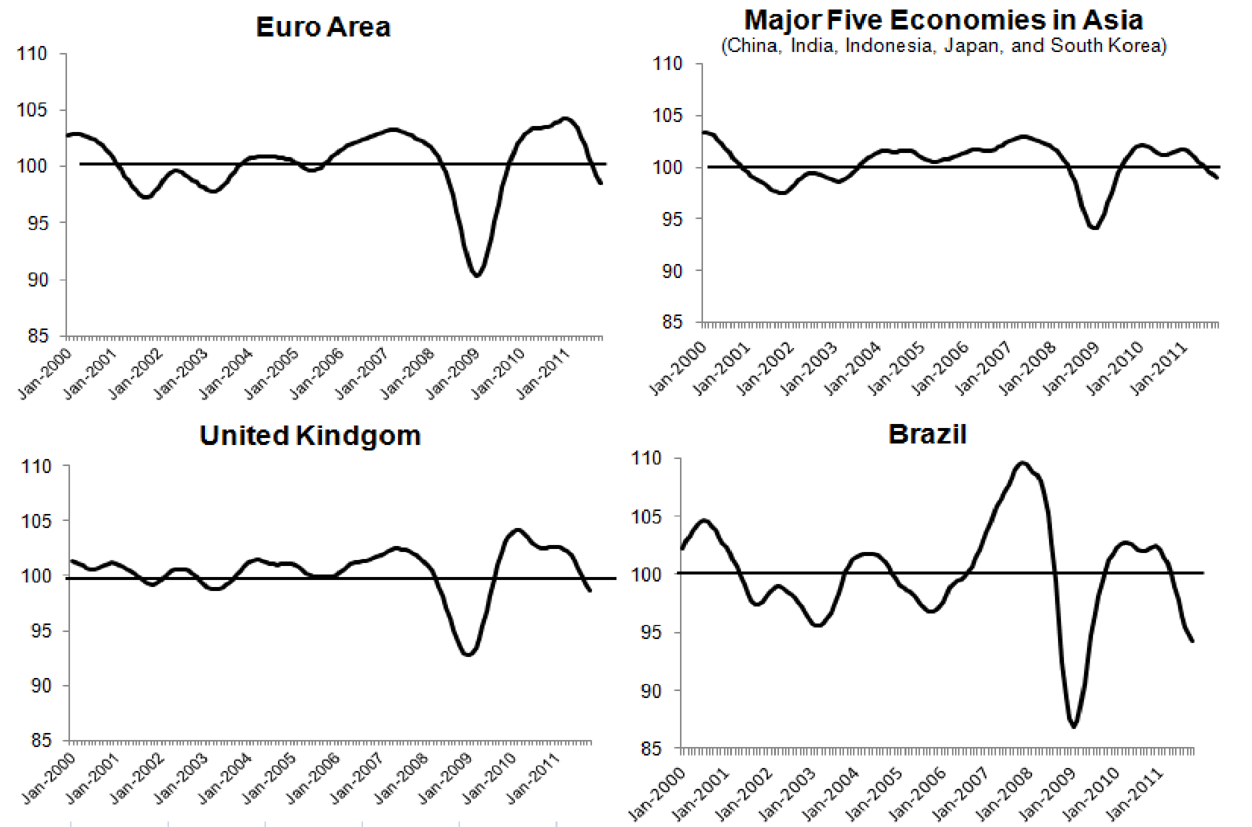
Colorado business conditions **–** The Goss Business Conditions Index, which is based on a survey of Colorado supply managers, was 56.2 in November 2011, up from 53.3 in October 2011. A value greater than 50 indicates expansion. The index uses the same methodology as the Institute for Supply Management to determine business conditions. The Goss survey index has increased for Colorado for two consecutive months. The survey notes that businesses generally continue to favor extending the average number of weekly hours worked over hiring additional workers.

A slowing global economy – Colorado and the nation are highly connected with the global economy, and conditions in other parts of world impact the state's economy. Thus, economic trends in other parts of the world are important to monitor. Unfortunately, in contrast to the more favorable economic conditions in the United States, particularly in Colorado, many of the world's largest economies have slowed.

Europe's economy is likely in recession or will soon be due to its debt crisis and the consistently underperforming economies in its southern periphery, most notably Italy, Spain, Portugal, and Greece. Asia is slowing as the European downturn impacts its economy, given that Europe is the biggest market for its goods. Further, China, the largest of the Asian economies and the second largest in the world, is affected by high inflation and a slowing real estate and construction market. A marked slowdown is occurring in the United Kingdom and Brazil, the sixth and eighth largest economies in the world, respectively.

These trends can be seen in Figure 7, which provides composite leading indicators published by the Organization for Economic Co-Operation and Development (OECD) for many of the world's economies. These indicators were created to anticipate the economic activity of an economy about six months into the future. All of indicators below show a definitive turning point and slowdown in economic activity. The slowdown in Europe will make its banking and debt problems more difficult to manage.

Figure 7. OECD Composite of Leading Indicators for Major Global Economies, 2000 through October 2011*



*An index above 100 indicates an economy is growing above its long term trend and an index below 100 indicates economic activity is below long term trend growth
Source: OECD

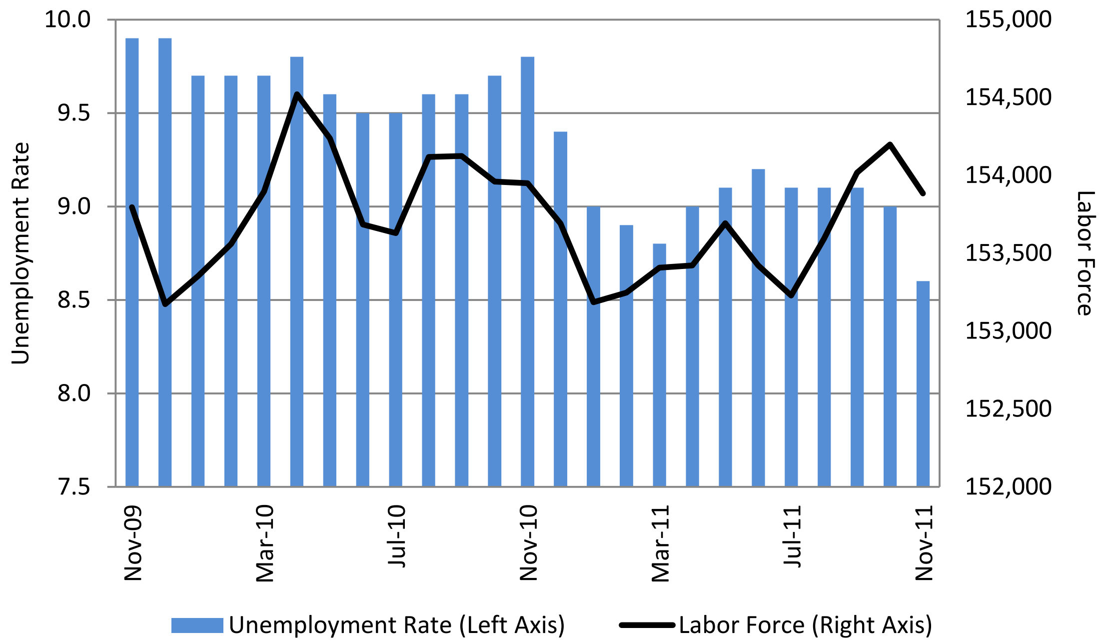
The Job Market

The employment situation has shown improvement recently, especially in Colorado. Notably, job growth has been stronger, unemployment has dropped, and initial claims for unemployment insurance (UI) continue to fall.

The nation's job market has improved but data show mixed results - The nation has added an average of 133,143 non-farm jobs per month since October 2010. And, most recently, previous month data experienced upward revisions, suggesting that there is more underlying strength in the job market than past estimates indicated. Unemployment insurance claims recently fell from their more elevated levels recently. For the week ending December 10th, the nation's claims were at the lowest level since early 2008.

In November, the national unemployment rate was 8.6 percent, a decline of 0.4 percentage points from October. However, a labor force decrease of 315,000 people accompanied the decline. Thus, a portion of the unemployment rate decline was due to unemployed workers abandoning their search for jobs. Figure 8 shows the change in the unemployment rate relative to the change in the labor force.

Figure 8. U.S. Unemployment Rate and the Level of the Labor Force, Seasonally Adjusted



Source: Bureau of Labor Statistics, Labor Force in thousands

The U.S. Bureau of Labor Statistic's most comprehensive measure of unemployment, called "U6," or more commonly, the "underemployment rate," remains very high at 15.6 percent. This measure includes: (1) the traditional unemployed counted in the unemployment rate; (2) those who have temporarily stopped looking for work due to discouraging job prospects; and (3) those working part-time rather than full-time due to economic conditions.

Colorado's job market is showing sustained momentum – In 2011, Colorado is on track to add about 27,000 jobs. Though this is a relatively modest gain compared with prior years during economic expansions, it is the largest annual gain since 2007. The jobs gain for 2011 includes OSPB's estimates of the forthcoming revisions to the currently published jobs data. Currently published jobs data from the Bureau of Labor Statistics will be revised upward based on Quarterly Census of Employment and Wage data to more accurately reflect the number of jobs in the state.

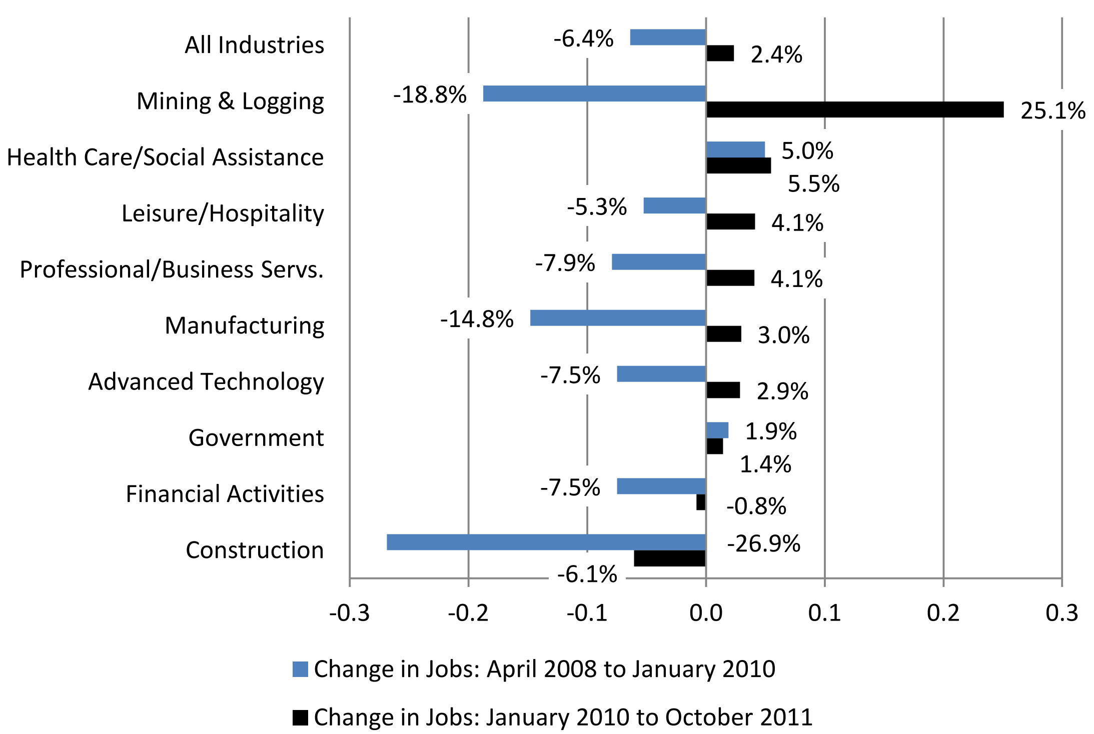
Additional evidence demonstrates momentum in Colorado's jobs market. Between October and the first week of December, the state's initial unemployment claims were 13.0 percent lower than the same period in 2010 and 24.4 percent lower from the same period in 2009.

As of October 2011, the unemployment rate in the state was a seasonally adjusted 8.1 percent. It has been falling or constant every month since February 2011. As additional proof that Colorado's job market is stronger than the nation's, the state has experienced a drop in the unemployment rate without a decline in the labor force. Since February 2011, the state's labor force has increased by about 20,000. Thus, importantly, the state is currently adding sufficient jobs to begin to absorb both the unemployed as well as a portion of individuals reentering the labor force.

The job rebound has occurred across many industries. However, most industries have still not come close to regaining their level of jobs before the recession. As of October 2011, only four major industry categories have regained all their job losses or continued to grow relative to April 2008, the peak month of employment before the state began losing jobs. These industries are: natural resources and mining; government; other services; and education and health services. Overall, the state still has about 100,000 jobs less than before the recession.

Growth in the mining industry, especially due to the oil and gas boom in northeast Colorado, has been particularly robust. It is currently the state's leading industry for job creation. Though the industry directly employs only a small portion of the state's workforce, the economic benefit from growth in this industry bolsters other industries as well, such as professional and business services, construction, lodging, food and drinking establishments, and retail.

Figure 9. Change in the Number of Colorado Jobs by Selected Industries During and After the Economic Downturn



Source: U.S. Bureau of Labor Statistics with revisions estimated by OSPB

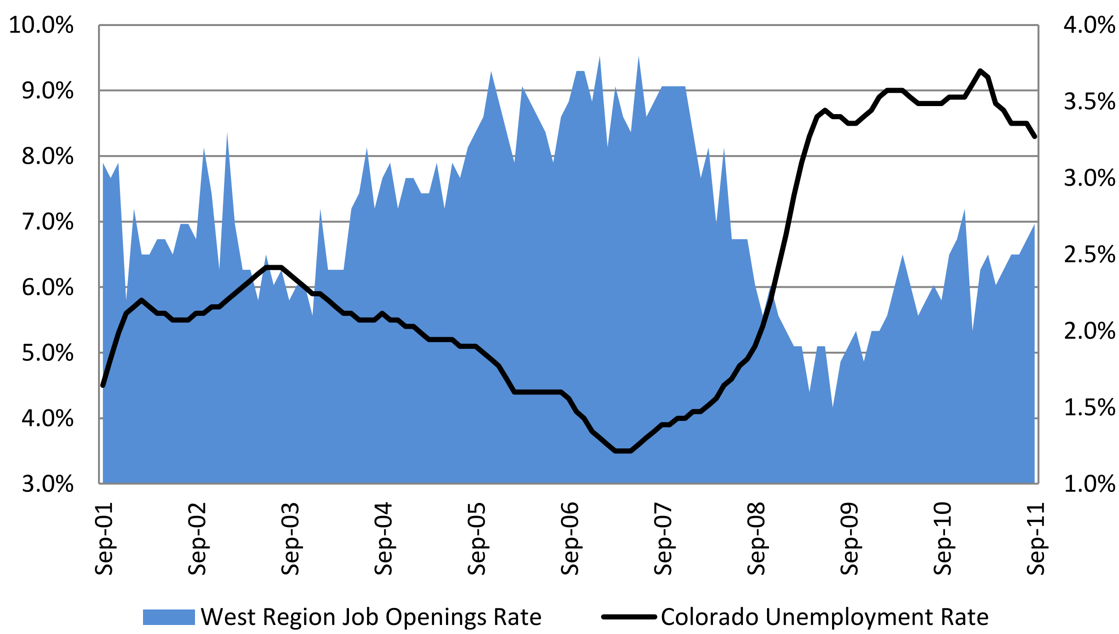
Job growth is constrained by a changing economy – Economic restructuring has held back more robust job growth as the economy transitions from one driven by real estate, finance, consumption, and excessive borrowing and debt to other sources of growth. This restructuring and rebuilding, though painful for the unemployed and underemployed, is necessary to enable more robust future growth.

Stronger and more sustainable growth will resume after businesses and workers find new ways to better employ their resources. For example, many of the unemployed workers who were in demand during the housing boom do not have the necessary skills to move into currently growing industries that require more technical, specialized skills such as health care and advanced technology. Further, many businesses and entrepreneurs are still struggling to discover ways to satisfy consumer demand in the changing economy.

The restructuring and discovery process will take time, especially due to still relatively constrained credit and less resources for investment due to the housing bust; therefore, unemployment in Colorado and the nation will remain stubbornly high. Further, there will be upward pressure on the unemployment rate as individuals who left the labor force during the recession begin to search for job opportunities. In doing so, these individuals will be counted as unemployed and part of the labor force.

As shown in Figure 10, the unemployment rate for the state compared to the rate of job openings in the region provides further evidence of the economy's structural mismatch. Even as the rate of job openings for the western states continues to return to pre-recession levels, unemployment remains very high. An indication of the severity of the downturn and associated restructuring is the gap between the unemployment rate and the rate of job openings, which remains at a near decade high.

Figure 10. Western State Rate of Job Openings and Colorado Unemployment Rate



Source: Bureau of Labor Statistics, seasonally adjusted

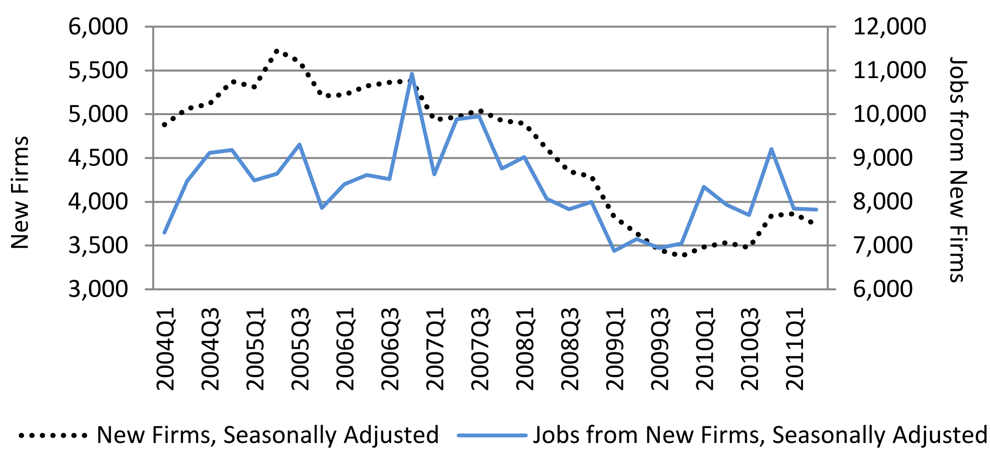
- For Colorado, OSPB forecasts total nonfarm employment growth of 1.2 percent in 2011 and 0.7 percent in 2012. Job growth will moderate in 2012 as the slowdown in the global economy negatively affects Colorado's economy, especially from a European recession and strains in the financial system. The state's unemployment rate will be 8.5 percent and 8.6 percent in 2011 and 2012, respectively. Similarly, OSPB forecasts total nonfarm employment growth of 1.0 percent for the nation in 2011 and 0.5 percent in 2012. National unemployment rate projections are 9.1 percent for 2011 and 9.4 percent for 2012.

New Businesses and Job Creation

In Colorado each year, new businesses generally create more jobs than existing firms. Thus, trends in business startup activity are important to monitor to help gauge job growth. Based on Quarterly Census of Employment and Wages data from the Colorado Department of Labor and Employment, the number of business startups fell substantially during the recession. However, business startup activity improved beginning in 2010, which has helped spur the rebound in job growth.

Figure 11 shows the number of new businesses created since the beginning of 2004 through the first half of 2011. It also shows the number of jobs created by those new businesses each quarter. The rebound in business creation has been frustratingly slow, and start-up activity remains well below its pre-recession peak. Thus, until start-up activity becomes more robust, job growth will likely be constrained. Many entrepreneurs typically use home equity loans, bank loans, credit cards, personal savings, and monetary assistance from friends and family. Weak and falling homes values, still relatively tight credit conditions for small businesses, and high household debt are likely some of the causes of the modest startup activity. Further, as the economy struggles through its restructuring and rebuilding process, entrepreneurs are likely having a more difficult time discovering what the new emerging economy values and thus how to make money.

Figure 11. New Businesses and Jobs Created from those Businesses, 2004 though the First Half of 2011

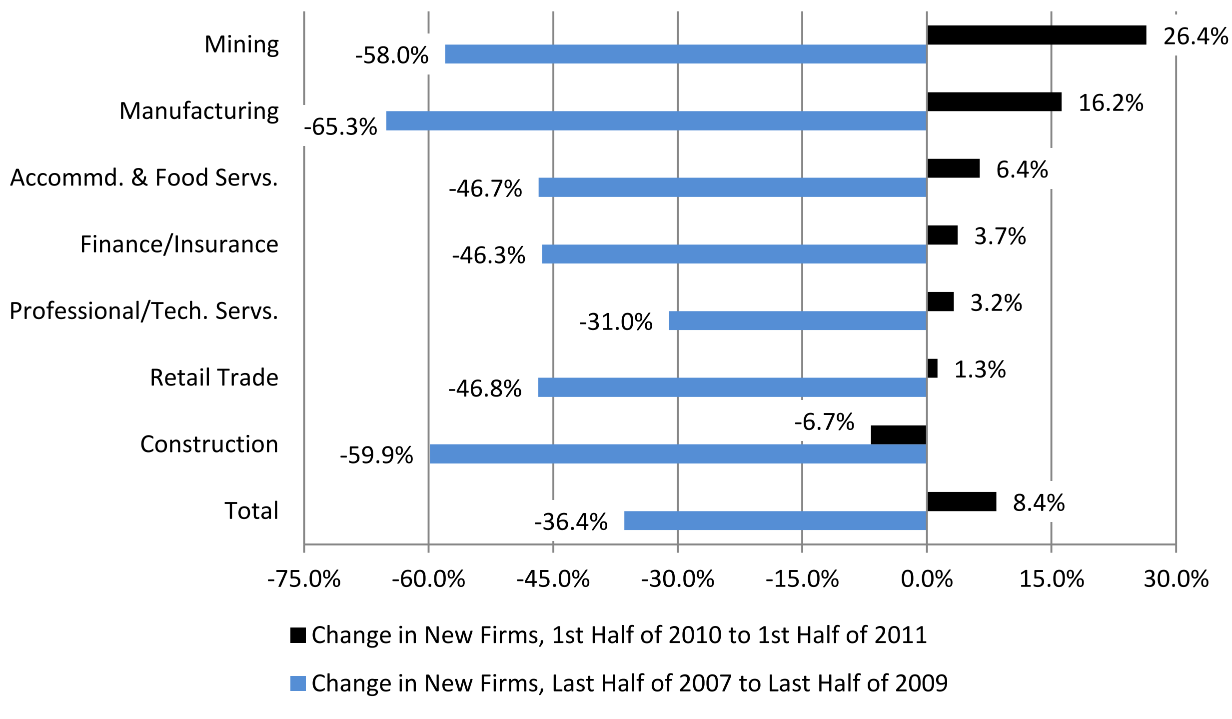


Source: Colorado Department of Labor and Employment

New business activity fell precipitously across most industries during the recession. Since 2010, new business startups have been increasing across most of the state's largest industries. Figure 12 shows the change in the number of new businesses by select industries during the recession and from the first half of 2010 to the first half of 2011. Total new startups are up 8.4 percent after falling by 36.4 percent during the recession.

Given that goods producing industries that sell their products outside the state are among the sectors that produce the most economic benefit, the growth in business startups in manufacturing and mining are positive developments for the state. Because Colorado is also a regional economic hub for the generally high wage professional and technical services sectors, such as accounting, architecture, engineering, and legal services, a rebound in new firms in this industry is another positive trend. The continuing decline in construction firms is not surprising given the continued weakness in the housing and commercial real estate markets.

Figure 12. Change in the Number of New Firms by Selected Industries During and After the Economic Downturn



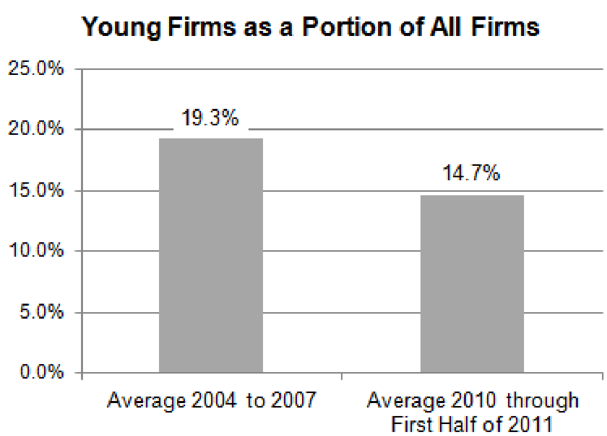
Source: Colorado Department of Labor and Employment

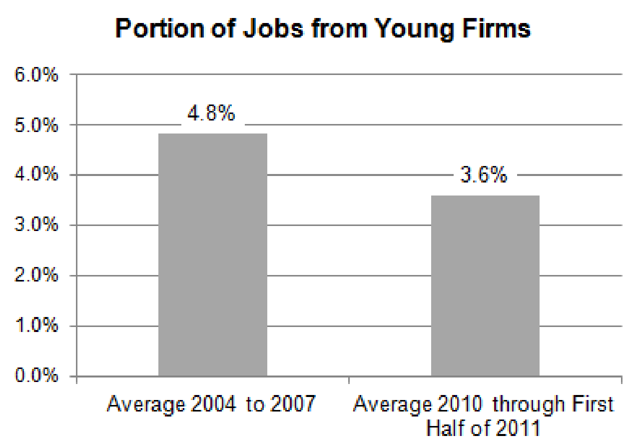
Colorado's entrepreneurial culture and job growth – Colorado has been a leader among states in entrepreneurial activity as measured by new business creation. This is a key reason why the state economy and job growth have tended to outperform the nation during periods of growth.

Employment from new and young firms correlates highly with overall employment growth, meaning that higher levels of business creation are closely associated with higher levels of employment growth. This heightened churning of jobs, where individuals move into growing young businesses, is an indicator that an economy is flexible and dynamic, and thus has a better capacity to grow. A more flexible and dynamic economy is one in which jobs and capital move to where they are the most valued as entrepreneurs and businesses respond to growth and profit opportunities.

As with new business creation, the level of entrepreneurial activity has not recovered to pre-recession levels. The average portion of new or young firms as a portion of all firms over this period was 19.3 percent, while it fell to 14.7 percent on average in 2010 through the first half of 2011. The number of workers employed at these young firms as a portion of all jobs has also fallen, from 4.8 percent to 3.6 percent. These statistics, shown in Figure 13, track with the data on the modest levels of startup-activity through the first half of 2011. This indicates that entrepreneurs have had more difficulty finding opportunities to begin and sustain new business ventures as the economy restructures from the real estate and consumption boom that began in the mid 1990s.

Figure 13. Young Firms and their Employees as a Percentage of all Firms and Jobs





Source: Colorado Department of Labor and Employment

Income and Wages

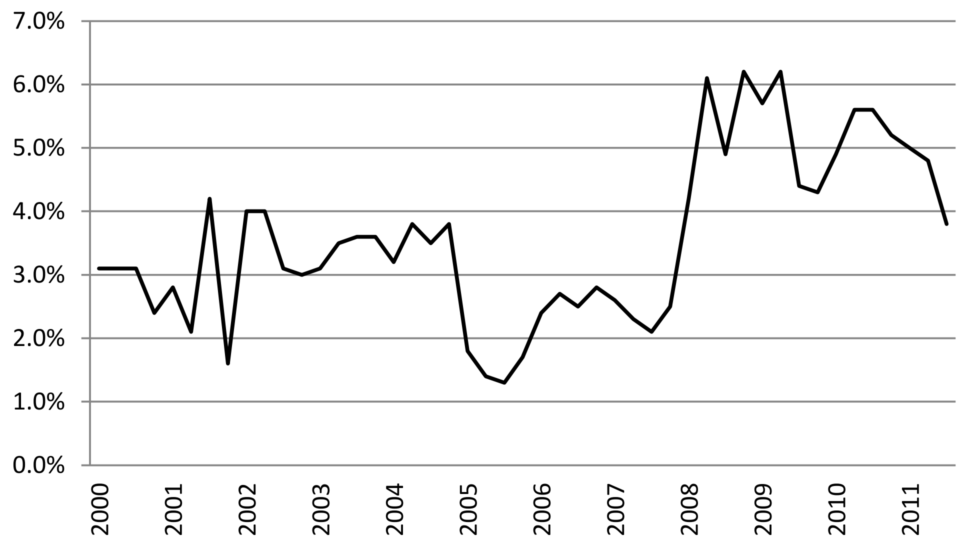
Personal income consists of wage and salary income, proprietors' (or business) income, government transfer receipts, and interest and dividend income earned on assets. Personal income growth is an important factor for economic recovery, as it improves household finances and supports consumer spending.

In October 2011, U.S. personal income increased 0.4 percent, while disposable personal income, or income after taxes, increased 0.3 percent. National and Colorado growth rates for personal income are generally similar over time, and state personal income data is available on a delayed basis from the Bureau of Economic Analysis. The most recent state personal income data available is through the second quarter of 2011. After falling during the recession through the third quarter of 2009, both national and Colorado personal income have posted gains in each quarter since. In the second quarter of 2011, personal income grew 1.1 percent for both the nation and Colorado.

Disposable personal income growth is weak **–** Real disposable income, or income adjusted for changes in price levels, increased 0.3 percent in October nationally after decreasing in five of the six previous months. Disposable personal income is the total after-tax income received by individuals, and it is the income available for spending or saving. If recent weakness in real U.S. disposable personal income persists, business sales and economic growth will suffer in 2012.

Personal savings have declined **–** The personal saving rate – the share of personal saving as a percentage of disposable income – has been generally trending downward since the early 1980s, when it was around ten percent. The personal saving rate was above 7.5 percent briefly at the end of 2009, but has trended downward since. Personal saving is important because it affects the amount of resources available for investment as well as spending patterns. Higher saving in the present often results in increased spending in later periods, as investment helps the economy grow and create jobs, and .it gives households a greater sense of financial well-being. Figure 14 shows the personal savings rate from 2000 through the third quarter of 2011.

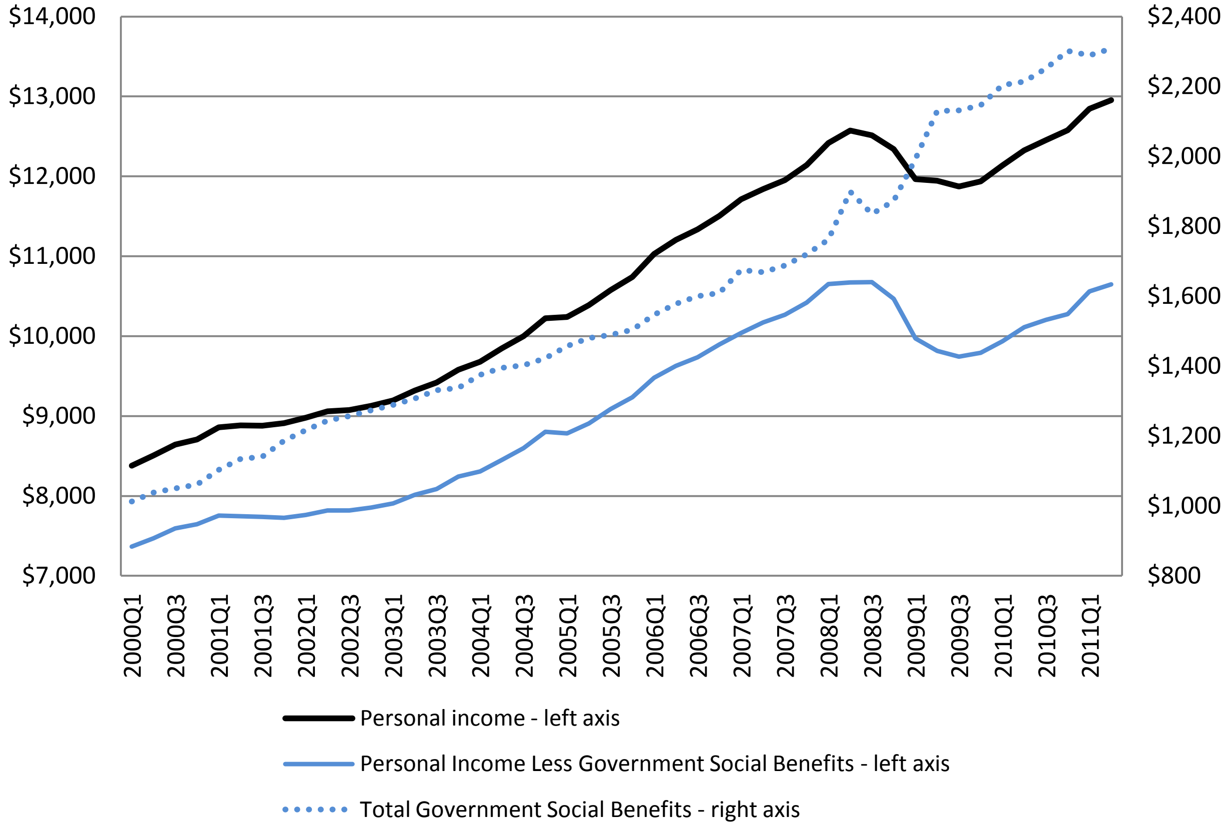
Figure 14. U.S. Personal Saving Rate through the Third Quarter of 2011



Source: Federal Reserve Bank of St. Louis, Personal Saving Rate (PSAVERT), Quarterly Average

Government assistance and social insurance is making up a large share of income **–** Real personal earnings less government transfers is a telling indicator of consumer health that provides information on actual earnings from economic activities, most notably employment. Thus, it is one of the measures considered by the National Bureau of Economic Research in determining business cycles. Figure 15 shows personal income with and without government transfers compared with the growth in such transfers. Government social insurance has increasingly comprised a greater share of personal income over the past couple of years. Persistently high unemployment has increased demand for public assistance, and the retirement of the baby boom population has begun to increase Social Security and Medicaid payments.

Figure 15. Personal Income and Personal Income Less Government Social Benefits



Source: Bureau of Economic Analysis, billions of dollars, seasonally adjusted at annual rates

Colorado wage and salary growth has continued in each quarter since the second quarter of 2009. Various sectors have been affected uniquely by the recession, and thus wage and salary changes among sectors have been mixed. Overall, however, total wages paid are growing in most industries. The construction sector is not surprisingly one of the industries seeing a decline in wages paid.

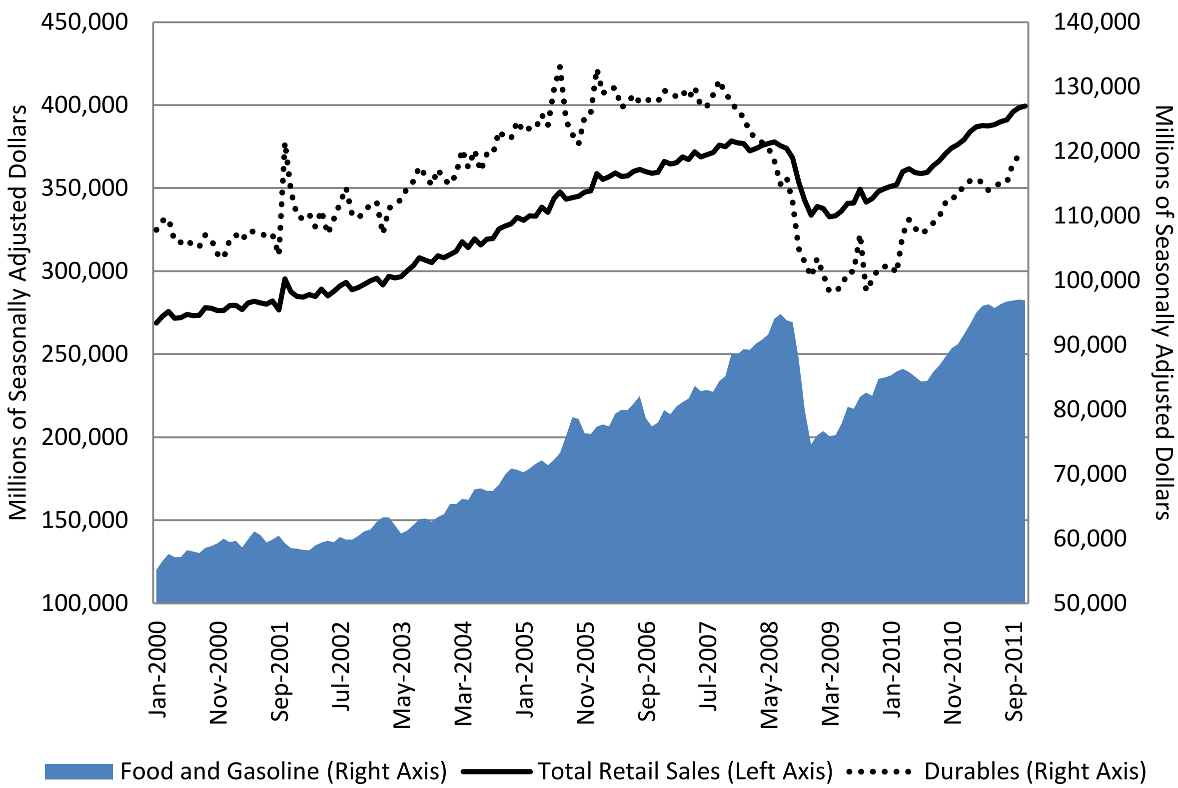
- OSPB forecasts Colorado personal income will increase 5.3 percent in 2011 and slow to 3.5 percent in 2012 as a result of the projected slower growth in jobs. OSPB projects that Colorado wage and salaries will increase 3.9 percent in 2011 and 2.8 percent in 2012. Colorado personal income and wage growth will slightly outpace the nation's.

Consumers and Households

Consumer spending has remained relatively strong despite high unemployment, weak home prices, modest income growth, and elevated gas and food prices. Nationally, retail trade sales were up 6.8 percent in November over year ago levels. Based on national data, it appears that some of the spending has been supported by borrowing and lower savings. For example, total non-revolving credit, which includes car loans, increased $7.3 billion in October to $1.7 trillion. Credit card debt also increased, though more modestly.

Figure 16 shows total retail trade sales, sales of durable goods, and food and gasoline sales at the national level through November. Unless income and job growth picks up, the aforementioned headwinds will make it difficult for consumers to sustain their current level of spending.

Figure 16. Total National Retail Trade Sales, Sales of Durable Goods, and Food and Gasoline Sales, 2000 to November 2011



Source: US Census Bureau

The graph shows that purchases of durable goods − big ticket-items such as cars, appliances, and electronics − though increasing are still below their 2008 peak. In some cases, sales of such goods require the use of credit and lower consumer confidence is likely constraining such large purchases. The graph also indicates that the surge in spending on food and gas has abated in recent months as price pressures for such items have diminished.

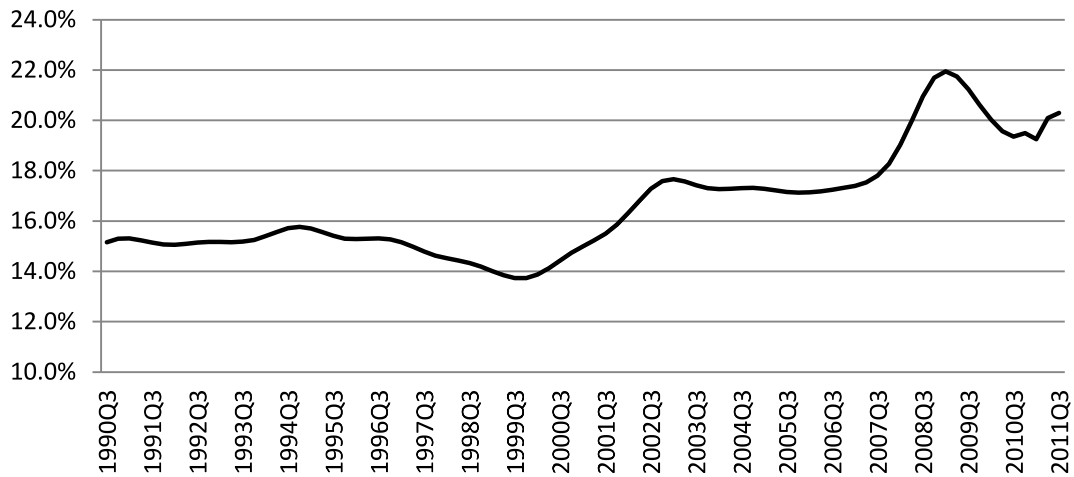
Sales tax data for Colorado, which provides the most up-to-date information on spending in the state, was up 5.0 percent in the September through November period of this year compared with a year ago. Though this data also includes spending by businesses, it shows that consumer spending in Colorado has also been increasing.

Household net worth is still weakened − The disruptions in the stock market in the fall undermined household net worth. According to the Federal Reserve, household net worth nationally declined $2.4

trillion in the third quarter of 2011 to total $57.4 trillion. In addition to the downturn and volatility in the stock market, continued falling home values are hurting the financial position of households. The third quarter drop in net worth was the largest decline since the $5.6 trillion loss in the fourth quarter of 2008 when the financial crisis hit. Households' net worth remains $9.4 trillion below its 2007 peak.

Household liabilities remain high **–** The weakness of households' net worth is reflected in their liabilities, or debts, compared with their assets. Figure 17 shows the ratio of household liabilities with their assets from 1990 through the third quarter of 2011. As shown, the debt-to-asset ratio increased markedly during the 2000s and especially when the financial crisis depleted household wealth. While households have reduced their debt since the 2008 peak of the housing bubble, liabilities as a share of total assets remains high.

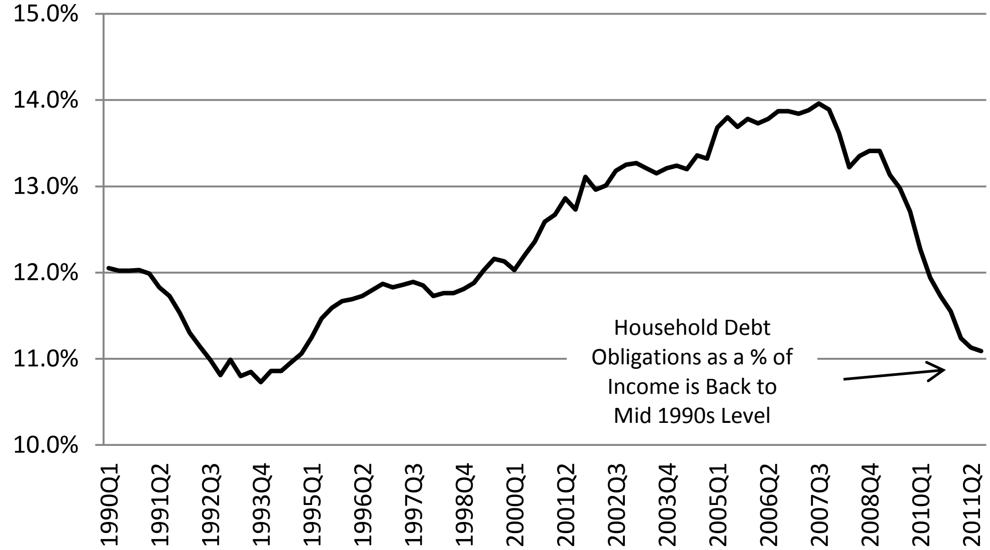
Figure 17. Total Liabilities as a Share of Total Assets, US Households and Non-Profit Organizations



Source: Federal Reserve Board Flow of Funds extracted from Moody's Economy.com

Household debt loads have improved **-** Despite the still high liabilities-to-assets ratio that reflects weakened household net worth, the debt load of households has improved markedly since hitting an all time high before the recession. Figure 18 shows the percent of disposable personal income dedicated to debt service for households as estimated by the Federal Reserve. Debt service payments as a percent of income have come down to its mid-1990s level, before households began to run up debt. In addition to paying down debt, the decline in debt service payments can also be attributed to debt defaults, bankruptcies and historically low interest rates over the past few years.

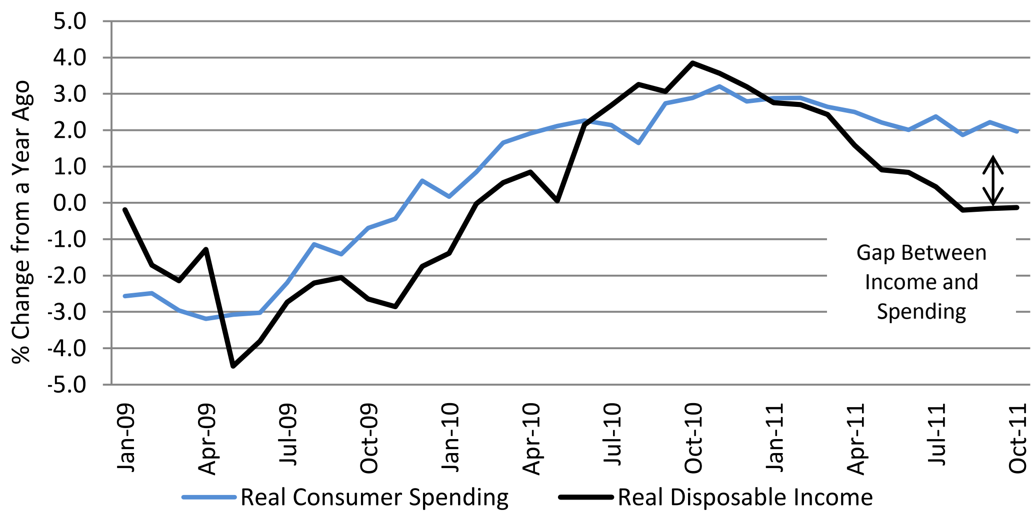
Figure 18. Debt Payments as a Percent of Disposable Household Income, 1990 through the Third Quarter of 2011



Source: Federal Reserve

Real income after taxes has been weakening since the fall of 2010, which erodes the purchasing power of households. This is illustrated in Figure 19 which shows real disposable personal income and price-adjusted consumer spending since 2009. Not surprisingly, income and spending track each other closely over time. Currently spending is above income levels, a situation that cannot be sustained.

Figure 19. Real Disposable Personal Income and Spending Nationally, Seasonally Adjusted Annual Rate



Source: U.S. Bureau of Economic Analysis

- Continued volatility in the stock market, a lack of the necessary income growth to support current levels of spending, and the expected slowdown in job growth in 2012 will cause retail trade sales at both the national and state level to slow in 2012 from 2011's surprisingly strong pace. After growing 6.3 percent in 2011, Colorado retail sales will post a more modest growth rate of 3.6 percent in 2012. Retail trade sales are expected to pick up along with the economy in 2013.

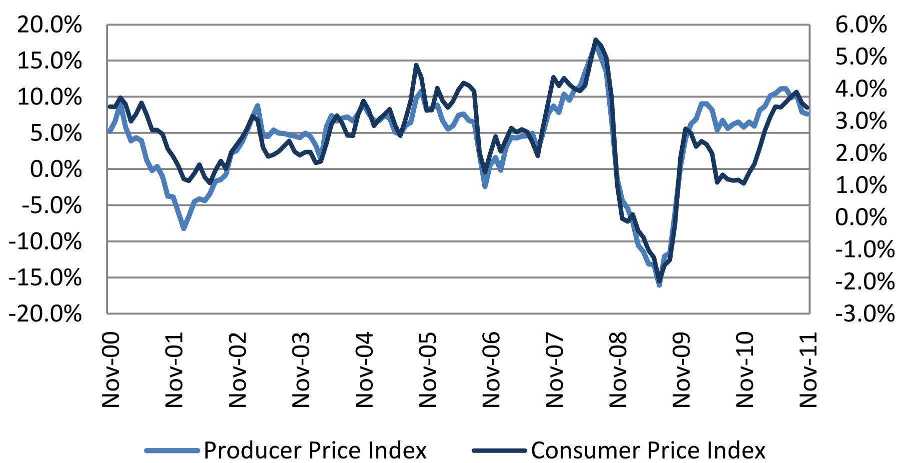
Prices

Both prices paid by businesses and consumers remain elevated, though the increase in consumer prices seen over much of the year has begun to abate.

The Producer Price Index for finished goods increased 0.3 percent in November 2011 after falling 0.3 percent in October. Recent data suggest slowing growth in Europe and Asia may minimize upward price pressure on raw materials, and high unemployment in the U.S. will make it more difficult for companies to increase their prices to consumers. The relative strength of the U.S. dollar in recent months will also help keep a lid on materials used in production and thus overall prices.

Measured year-over-year for November, the U.S. consumer price index (CPI) for all items was up 3.4 percent. However, price increases have abated in recent months. As Colorado's prices generally track national prices closely over time, the state is experiencing the same trends in prices as the nation.

Figure 20. U.S. Producer & Consumer Price Indexes, Percent Change from Prior Year



Source: Bureau of Labor Statistics, seasonally adjusted

- The Denver-Boulder-Greeley Price Index is forecast to increase 3.5 percent in 2011 and 2.3 percent in 2012. Nationally, the CPI is forecast to increase 3.2 percent in 2011 and 2.1 percent in 2012, and producer prices are forecast to increase 9.1 percent in 2011 and 2.6 percent in 2012.

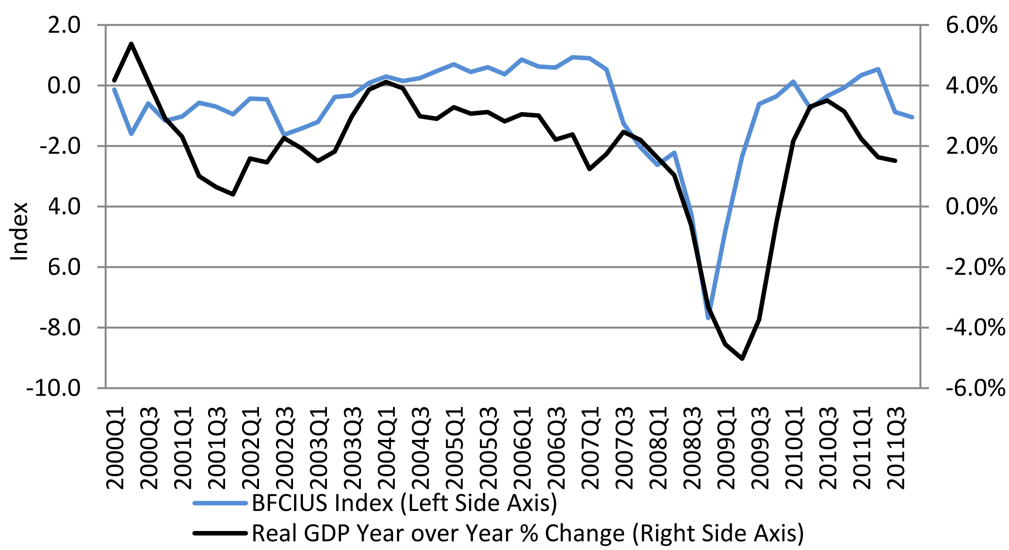
Financial Conditions

Much of commercial activity is facilitated by credit, thus the modern economy is highly influenced by financial conditions. This was evident when the financial crisis that struck the world in 2008 caused a major contraction in economic activity. Europe's sovereign debt and banking problems pose a substantial risk to both the national and Colorado economy due to the highly connected nature of the global financial system, and a significant deterioration in European financial conditions would impact the Colorado economy.

U.S. banks do not hold a large amount of European debt directly, but systemic risk is a feature of the current European crisis. Several of the United States' largest banks have substantial indirect connections to troubled European debt and banks through the credit derivatives market, and European banks provide considerable funding to both large U.S. investment banks and more traditional U.S. banks. U.S. banks borrow a substantial amount of money from western European banks to fund their activities; according to the Economist Intelligence Unit, the amount equals about 25 percent of U.S. gross domestic product.

***Financial conditions have a large effect on the economy* –** Bloomberg, the financial analysis and information firm, publishes an index to measure financial conditions in the U.S. as well as Europe. The indices assess the level of stress in the money, bond, and equity markets by measuring yield spreads, financial market volatility, and asset prices. Figure 21 shows the quarterly average of the Bloomberg Financial Conditions Index for the U.S. (BFCIUS) over time compared with the growth rate of the nation's economy. As evidence of the importance of the health of the financial system to the economy, the figure shows how closely the BFCIUS index and the economy track over time. Thus, the recent weakening in the BCFIUS as a result of the European crisis is concerning for the future trajectory of the economy.

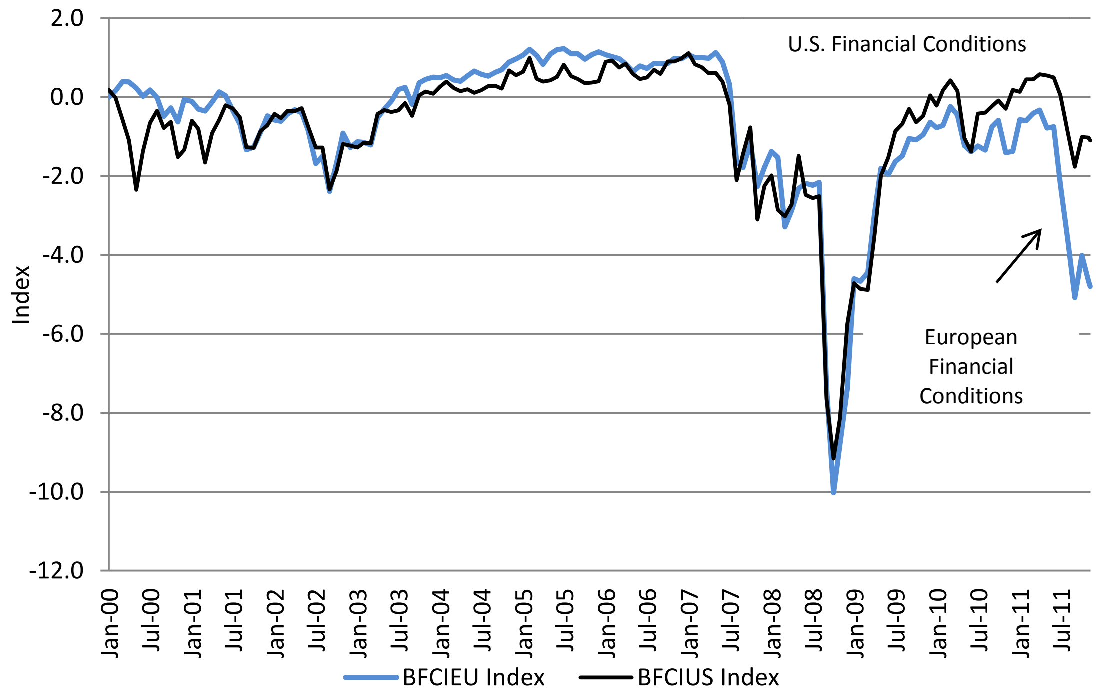
Figure 21. U.S. Financial Conditions and the Economy, 2000 through mid December 2011*



*BCFI levels below 0 represent higher funding stress, volatility in the financial system, and weaker asset prices.
Source: Bloomberg

European and U.S. financial conditions are tightly connected – Reflecting the connected nature of the global financial system, the BFCIUS and the BFCI for Europe (BFCIEU) have historically tracked each other very tightly. This is illustrated in Figure 22. European financial conditions are currently much worse than those in the U.S. The European index, though not currently at the level of extreme duress during the 2008 and 2009 financial crisis, is showing very high levels of stress. This is a worrisome trend based on how closely associated credit conditions and the health of economy are. If stress in the financial system continues or worsens, credit conditions will tighten further and will likely begin to slow economic growth in the U.S. and Colorado.

Figure 22. U.S. and European Financial Conditions, 2000 through mid December 2011*

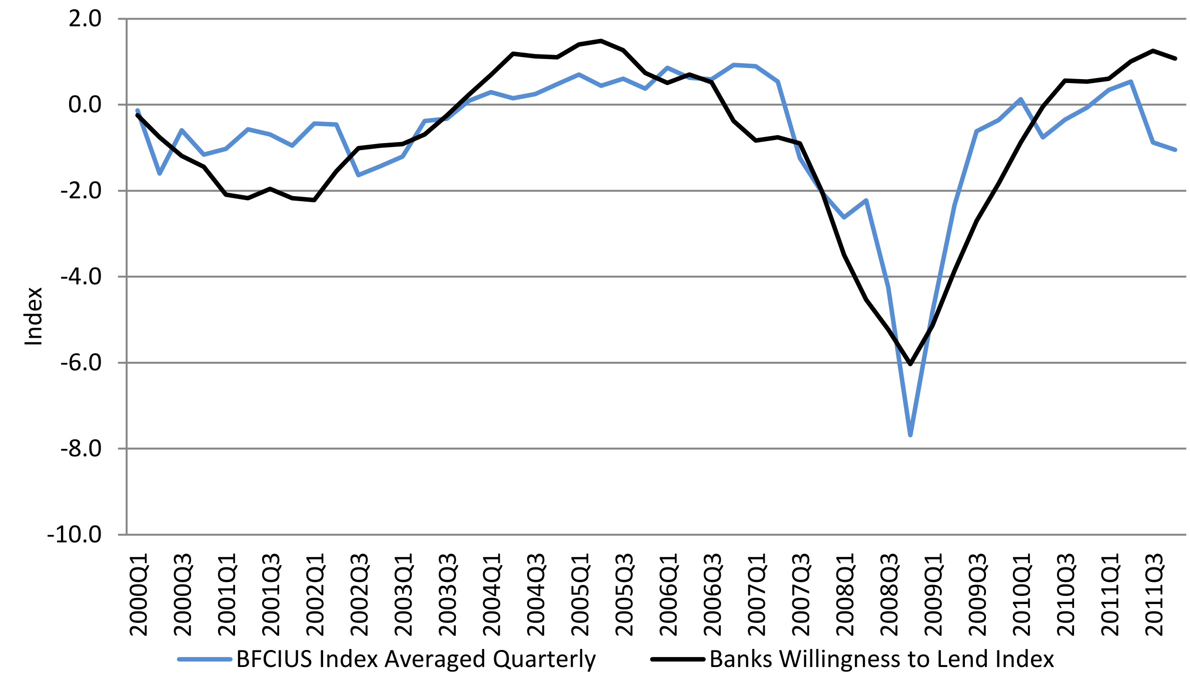


*BCFI levels below 0 represent higher funding stress, volatility in the financial system, and weaker asset prices.
Source: Bloomberg

Higher stress in the financial system will reduce lending from banks – U.S. banks have built up their capital and hold a substantial amount of reserves as a result of the Federal Reserve's monetary policies that began with the onset of the financial crisis of 2008. As noted earlier, they also hold relatively small amounts of troubled European sovereign debt directly. Because of the relative health of U.S. banks, the recent increase in stress in the financial system has not, to date, adversely affected lending conditions. Lending, especially to businesses, has loosened and banks continue to show an increased willingness to lend. This trend has likely been a major contributor to the recent uptick in economic activity.

Bloomberg also publishes an index measuring banks' willingness to lend, which is based on the Federal Reserve's quarterly Senior Loan Officer Survey. The index measures banks' lending standards for business, consumer, and residential and commercial real estate loans. As shown in Figure 23, banks' willingness to lend trends closely with the level of stress in the financial system. Although the index currently shows an upward trend in banks' willingness to lend, given recent market concerns about European financial institutions and the accompanying market volatility, a tightening in U.S. lending conditions is a future risk to the economy.

Figure 23. U.S. Financial Conditions and Banks' Willingness to Lend, 2000 through mid-December 2011



Source: Bloomberg

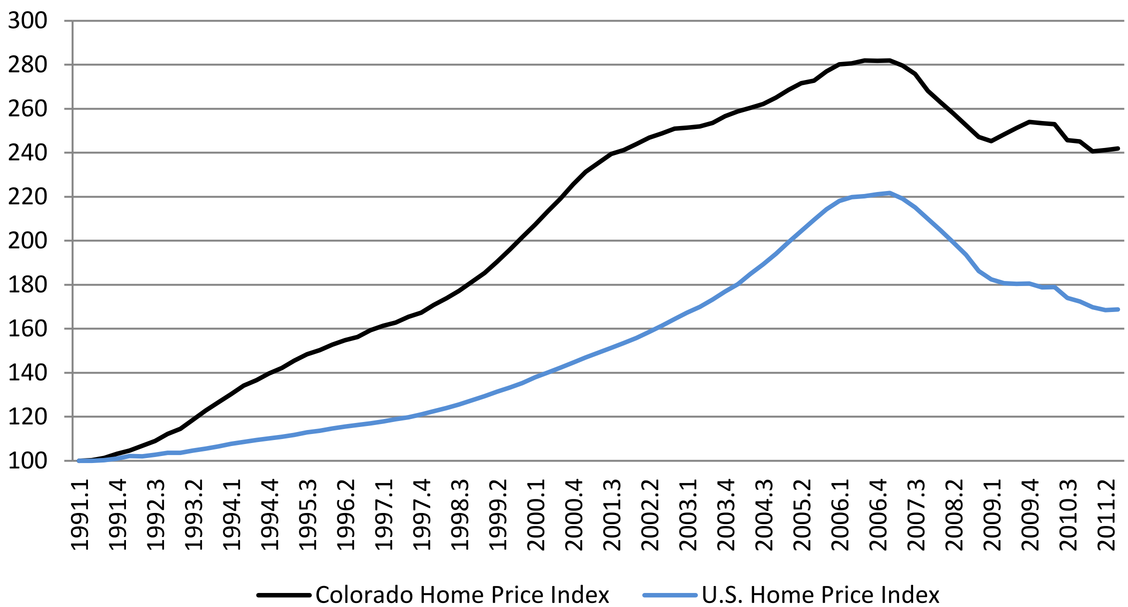
The Housing and Construction Market

Nationally, the housing sector recovery is regionally mixed. In some areas, conditions will deteriorate further before improving. Housing is the largest asset for most families and individuals, and rising prices tend to make people feel wealthier. The housing wealth effect also works in reverse, as falling prices can negatively impact consumer sentiment and put downward pressure on consumer spending and investment. Therefore, recovery in the housing sector is imperative for a more robust recovery in the broader economy. A recovery, marked by stable or rising home values coupled with increased residential construction, will spur increased economic activity in other sectors, such as retail, finance, construction.

House prices continue to remain weak or fall – Conditions in the Colorado real estate market are also mixed, but home prices continue to fare better than those of the nation. Figure 24 compares the change in home prices for Colorado and the nation, as measured by the Federal Housing and Finance

Authority's (FHFA) home price index. In the third quarter of 2011, national home prices decreased 3.7 percent while Colorado prices declined 0.2 percent compared with levels a year ago. The FHFA has a newly constructed expanded home price index which includes sales price information for homes with mortgages covered by the FHFA as well as home price information from other sources, such as county recorders. This expanded index thus reflects price trends for a broader set of homes.

Figure 24. Federal Housing and Finance Administration Housing Index for Colorado and National Home Prices, 1991 to 2011 Third Quarter

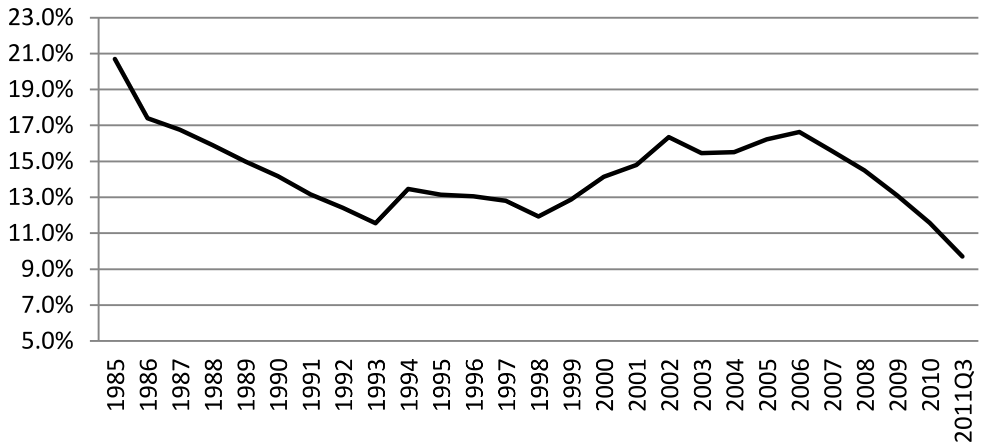


Source: Federal Housing and Finance Administration, Expanded Data Indexes by State (Expanded Indexes Incorporate Data from Enterprises, DataQuick Information Systems, and FHFA price data)

Home affordability is high – Home affordability has increased considerably in the wake of the most recent recession due to historically low interest rates and falling prices, yet consumers remain reluctant to purchase homes. Diminished demand for homes despite low prices suggests consumers may expect prices to fall further or no longer view a home as a worthwhile investment. Uncertainty related to job security and the overall strength of the economic recovery is also likely reducing demand.

Figure 25 compares average Colorado annual mortgage payments to average Colorado household income. The current level of affordability should eventually promote a housing sector recovery as consumers are able to allocate a smaller share of income toward home purchases. However, interest rates are a major factor that affects home affordability, and the possibility of increased interest rates from their extremely low levels presents a downside risk to the recovery.

Figure 25. Colorado Home Affordability, Mortgage Payment (Principal and Interest only) as a Percentage of Colorado Average Household Income, 1985 through Third Quarter2011



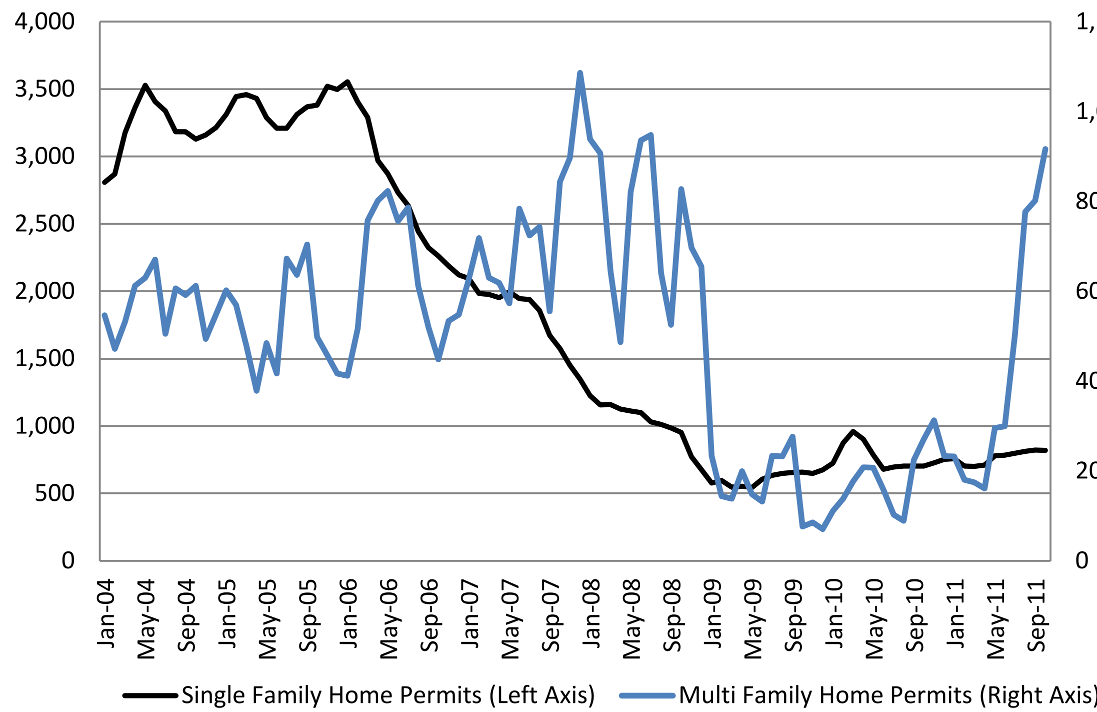
Source: OSPB calculations based on Colorado median single family home price data from the Colorado Association of Realtors, mortgage rates from Freddie Mac, estimated households from the State Demographer's Office and income data from the Bureau of Economic Analysis.

Mortgage problems persist – Mortgage market difficulties continue to weigh on the Colorado economy. A significant share of Colorado homeowners owe more for their home loans than the current value of their homes. These mortgages are often referred to as "under water" or "negative equity" mortgages. In the third quarter of 2011, the share of Colorado mortgages with negative equity was 20.4 percent according to CoreLogic, a real estate analysis firm. Out of forty three states surveyed, Colorado ranked tenth in the highest share of homes in negative equity. Nevada, with a total negative equity share of 58.3 percent, had the highest share. Nationally, of the states surveyed, the average share of negative equity mortgages was 22.1 percent in the third quarter of 2011.

The large number of negative equity mortgages is weighing down the economy in several ways. It is negatively affecting home sales as homeowners are unwilling or unable to sell their homes for less than what they owe. This is causing the workforce to be less mobile, as it makes it difficult for workers to move where there are more job opportunities. Further, it creates more distressed sales of homes which place downward pressure on home prices. It also leaves business owners and entrepreneurs with less access to financing through home equity to expand or start a business.

Multi-family construction is growing while single-family construction remains weak – Vacancy rates in Colorado, which represent the percentage of unoccupied rental units, have continued to decline. The Colorado Division of Housing reports the third quarter 2011 state vacancy rate decreased to 5.0 percent. In the third quarter of 2010, the rate was 7.4 percent. As shown in Figure 26, particularly low vacancy rates have supported the multifamily construction market in some areas of the state. The metro Denver area in particular is experiencing a multifamily building boom as more than a dozen apartment buildings are currently being built in the area and many more are planned. The decline in vacancy rates reflects lower demand for home ownership, difficulty securing financing for home purchases, and a greater number of renters in the wake of foreclosures. Figure 26 also shows the continued low level of construction of single-family homes in the state.

Figure 26. Permits for Single Family and Multi-Family Home Construction in Colorado, Seasonally Adjusted, Three Month Moving Average



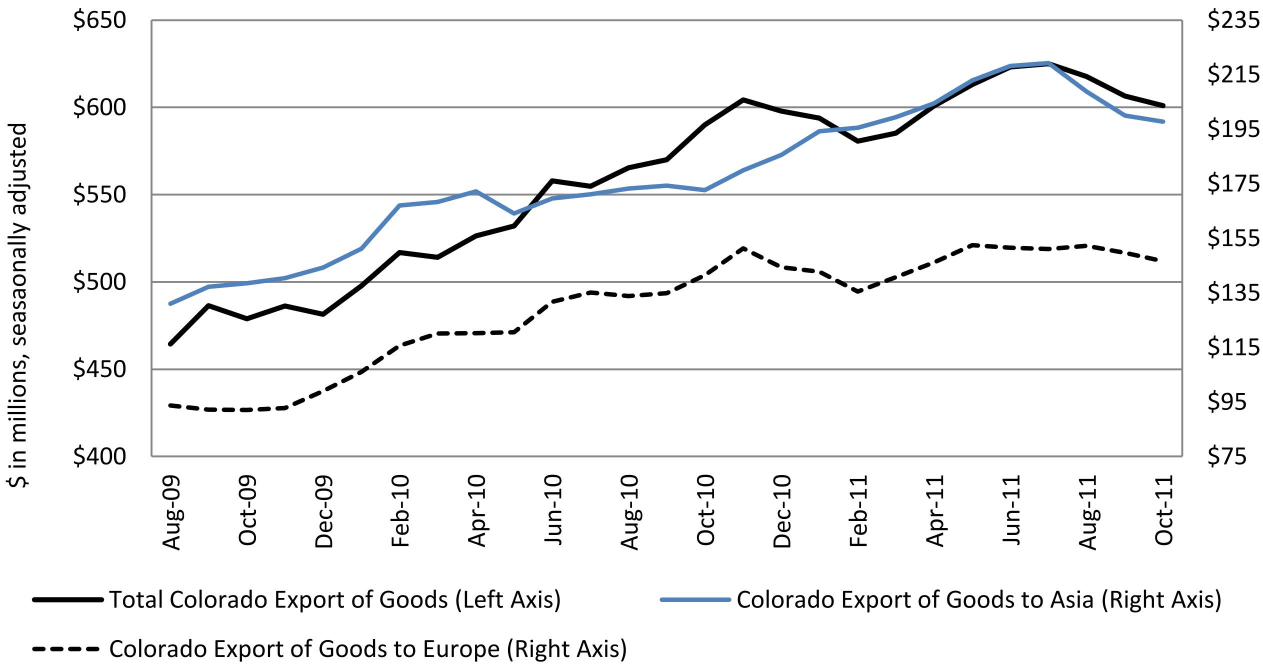
- OSPB forecasts Colorado housing permits will number 12,500 in 2011, up slightly from 2010. The continued glut of existing single family homes will weigh on construction in 2012 as well, though permits will post another modest increase and total 14,100. Construction of multifamily structures will outpace growth in the single family market.

International Trade

Exports of both U.S. and Colorado products have been one of the brightest spots in the economy. Global growth after the economic downturn, especially in developing countries, has helped businesses sell more of their products abroad. In addition, domestic producers have discovered ways to become more competitive with foreign producers. The world's increasing demand for technological goods has benefitted U.S. exports, including exports from Colorado businesses that specialize in such highly demanded products.

Signs of slowing export growth – There have been some recent signs of weakening in Colorado export growth, especially to the slowing economies in Europe and Asia, which represents about 60 percent of the total value of goods exported by Colorado. Further strains in the global financial system may negatively impact exports since international trade, like the rest of the economy, is dependent on access to credit. However, the portion of Colorado's economy represented by the export of goods is relatively small. Figure 27 below shows the value of goods exported by Colorado.

Figure 27. Colorado Exports, Mid 2009 to October 2011



Colorado's export of services – Compared with the nation, Colorado's economy is more services-intensive, particularly in regard to services that can be exported, such engineering, legal, accounting, technological, and consulting services. Unfortunately, in contrast with goods exports, there is not state level data available on the amount of services exported. A 2009 study by the University of Colorado Leeds School of Business estimates that Colorado's value of services exports may be about the same or even exceed the value of goods exports. This contrasts with the nation as a whole, in which the export of services is a much smaller proportion (about 30 percent) of total exports.

The United States' share of its total services exports[1] to Europe is much higher as a percent of its total goods exports. According to the Bureau of Economic Analysis, the United States exports close to 40 percent of all its services to Europe, while it exports a little over 20 percent of the value of its total goods exports to Europe. Because Europe buys much of the nation's services exports and Colorado is a highly services-based economy, a weak European economy may hurt Colorado's economy more than the relatively small portion of its economy represented by the selling of goods to Europe suggests. Further, a European recession and a weakened euro compared with the dollar will likely cause a hit to the state's tourism industry in 2012.

[1] Among other items, services includes education (or foreign students studying in the U.S.), travel and tourism, financial services, insurance, medical, telecommunication services, and business, professional, and technical services. For purposes of this analysis, services of military and other government services are excluded.

Summary and Risks to the Forecast

The economy, especially the state's, is improving as entrepreneurs, businesses, and workers continue their efforts to rebuild from the deep recession brought on by the housing and debt driven boom and bust. Job growth has shown signs of sustained momentum across many industries, though the number of jobs is still well below its recession peak and unemployment remains high. Businesses are still struggling to find ways to employ idle workers and use resources in the most valuable ways to serve consumers and other businesses. Further, many unemployed workers lack the skills to move into growing and emerging industries. High unemployment, relatively modest income growth, and weakened home values should constrain consumer spending over the coming year. Finally, the slowdown in economic activity worldwide and increased stress in financial markets, especially in Europe, will cause a moderate slowdown in the national and state economies in 2012.

This forecast assumes the crisis in Europe does not markedly worsen and more negatively affect the economy. However, the economy is highly connected to the rest of the world and credit markets. Therefore, there is substantial risk that a deteriorating situation in Europe will cause more negative economic conditions than this forecast projects. The outcome is highly uncertain at this time, as resolution depends on many unpredictable variables, namely investor sentiment and policy decisions. Further, even if Europe continues to muddle along on the same path, the trend in weakening global economic conditions could weigh more on growth than this forecast projects.

Alternatively, conditions could be better than projected with recent economic momentum being sustainable. If businesses and entrepreneurs find more ways to succeed in producing what the economy values, they will employ more workers and other currently underutilized resources. This will create a virtuous cycle of sustained job and income growth that will allow for increased spending and investment and more robust overall economic activity. Further, growth would outperform this forecast if a more comprehensive resolution to Europe's financial problems is achieved in the near term.

Table 5
History And Forecast For Key Colorado Economic Variables
Calendar Year 2007 - 2014

Line No.		Actual				Forecast			
		2007	2008	2009	2010	2011	2012	2013	2014
	Income								
1	Personal Income (Billions) /A	$205.2	$216.0	$205.4	$213.2	$224.5	$232.4	$244.2	$258.1
2	Change	5.6%	5.2%	-4.9%	3.8%	5.3%	3.5%	5.1%	5.7%
3	Wage and Salary Income (Billions)	$113.0	$117.0	$112.6	$114.3	$118.8	$122.1	$126.7	$133.1
4	Change	6.7%	3.6%	-3.8%	1.5%	3.9%	2.8%	3.8%	5.0%
5	Per-Capita Income ($/person)	$42,565.6	$44,059.5	$41,271.1	$42,215.3	$43,854.4	$44,722.0	$46,208.4	$47,966.6
6	Change	4.1%	3.5%	-6.3%	2.3%	3.9%	2.0%	3.3%	3.8%
	Population & Employment								
7	Population (Thousands)	4,821.8	4,901.9	4,976.9	5,050.9	5,119.8	5196.2	5285.5	5380.6
8	Change	1.6%	1.7%	1.5%	1.5%	1.4%	1.5%	1.7%	1.8%
9	Net Migration (Thousands)	35.0	40.5	36.3	38.1	33.5	36.5	49.2	54.5
10	Unemployment Rate	3.7%	4.8%	8.3%	8.9%	8.5%	8.6%	8.2%	7.3%
11	Total Nonagricultural Employment (Thousands)	2,331.3	2,350.3	2,245.6	2,222.1	2,248.7	2,265.6	2,288.8	2,332.9
12	Change	2.3%	0.8%	-4.5%	-1.0%	1.2%	0.7%	1.0%	1.9%
	Construction Variables								
13	Total Housing Permits Issued (Thousands)	30.4	19.0	9.4	11.8	12.5	14.1	20.3	25.4
14	Change	-20.7%	-37.5%	-50.8%	26.1%	5.6%	13.0%	44.0%	25.1%
15	Nonresidential Construction Value (Millions) /B	5,259.5	4,117.0	3,349.0	$3,156.5	$4,123.6	$3,153.2	$3,274.8	$3,482.3
16	Change	13.3%	-21.7%	-18.7%	-5.7%	30.6%	-23.5%	3.9%	6.3%
	Prices & Sales Variables								
17	Retail Trade (Billions) /C	$75.3	$74.8	$66.5	$70.7	$75.2	$77.9	$81.7	$86.2
18	Change	6.9%	-0.7%	-11.1%	6.3%	6.3%	3.6%	4.9%	5.5%
19	Denver-Boulder-Greeley Consumer Price Index (1982-84=100)	202.0	209.9	208.5	212.4	$219.9	$224.9	$231.8	$239.7
20	Change	2.2%	3.9%	-0.6%	1.9%	3.5%	2.3%	3.0%	3.4%

/A Personal Income as reported by the federal Bureau of Economic Analysis includes: wage and salary disbursements, supplements to wages and salaries, proporietors' income with inventory and capital consumption adjustments, rental income of persons with capital consumption adjustments, personal dividend income, personal interest income, and personal current transfer receipts, less contributions from government social insurance.

/B Nonresidential Construction Value is reported by Dodge Analytics (McGraw-Hill Construction) and includes new construction, additions, and major remodeling projects predominately at commercial and manufacturing facilities, educational institutions, medical and government buildings. Nonresidential does not include non-building projects (such as streets, highways, bridges and utilities).

/C Retail Trade includes motor vehicles and automobile parts, furniture and home furnishings, electronics and appliances, building materials, sales at food and beverage stores, health and personal care, sales at convenience stores and service stations, clothing, sporting goods / books / music, and general merchandise found at warehouse stores and internet purchases. In addition, the above dollar amounts include sales from food and drink vendors (bars and restaurants).

Table 6
History And Forecast For Key National Economic Variables
Calendar Year 2007 - 2014

Line No.						Forecast			
		2007	2008	2009	2010	2011	2012	2013	2014
	Inflation- Adjusted & Current Dollar Income Accounts								
1	Inflation-Adjusted Gross Domestic Product (Billions) /A	$13,206.4	$13,1619	$12,703.1	$13,088.0	$13,393.1	$13,607.4	$13,920.4	$14,338.0
2	Change	19%	-0.3%	-3.5%	3.0%	2.3%	16%	2.3%	3.0%
3	Personal Income (Billions) /B	$11,912.3	$12,460.2	$11,930.2	$12,373.5	$12,980.7	$13,357.1	$13,9716	$14,740.0
4	Change	5.7%	4.6%	-4.3%	3.7%	4.9%	2.9%	4.6%	5.5%
5	Per-Capita Income ($/person)	$39,524	$40,964	$38,904	$40,037	$41600	$42,395	$43,920	$45,891
6	Change	4.9%	3.6%	-5.0%	2.9%	3.9%	19%	3.7%	4.5%
	Population & Employment								
7	Population (Millions)	3014	304.2	306.7	309.1	312.0	315.1	318.1	3212
8	Change	10%	0.9%	0.8%	0.8%	10%	10%	10%	10%
9	Unemployment Rate	4.6%	5.8%	9.3%	9.6%	9.1%	9.4%	9.0%	8.3%
10	Total Nonagricultural Employment (Millions)	137.6	136.8	130.8	129.8	1311	1316	132.8	135.7
11	Change	1.1%	-0.6%	-4.4%	-0.8%	10%	0.5%	0.9%	19%
	Price Variables								
12	Consumer Price Index (1982-84=100)	207.3	215.3	214.5	218.1	$225.0	$229.8	$236.7	$244.5
13	Change	2.8%	3.8%	-0.4%	16%	3.2%	2.1%	3.0%	3.3%
14	Producer Price Index - All Commodities (1982=100)	172.6	189.6	172.9	184.7	$2016	$206.9	$217.5	$230.8
15	Change	4.8%	9.8%	-8.8%	6.8%	9.1%	2.6%	5.1%	6.1%
	Other Key Indicators								
18	Corporate Profits (Billions)	$1,510.2	$1,248.4	$1,3619	1,800.1	$1,932.5	$1,911.1	$2,015.5	$2,262.7
19	Change	-6.1%	-17.3%	9.1%	32.2%	7.4%	-1.1%	5.5%	12.3%
20	Housing Permits (Millions)	1398	0.905	0.583	0.605	0.602	0.709	0.991	1274
21	Change	-24.0%	-35.3%	-35.6%	3.7%	-0.4%	17.8%	39.6%	28.6%
22	Retail Trade (Billions)	4,4517	4,409.5	4,0917	4,355.4	$4,676.3	$4,817.9	$5,030.3	$5,242.1
23	Change	3.2%	-0.9%	-7.2%	6.4%	7.4%	3.0%	4.4%	4.2%

/A BEA revised NIPA component

/B Personal Income as reported by the federal Bureau of Economic Analysis includes: wage and salary disbursements, supplements to wages and salaries, proprietors' income with inventory and capital consumption adjustments, rental income of persons with capital consumption adjustments, personal dividend income, personal interest income, and personal current transfer receipts, less contributions from government social insurance.

Governor's Revenue Estimating Advisory Committee

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