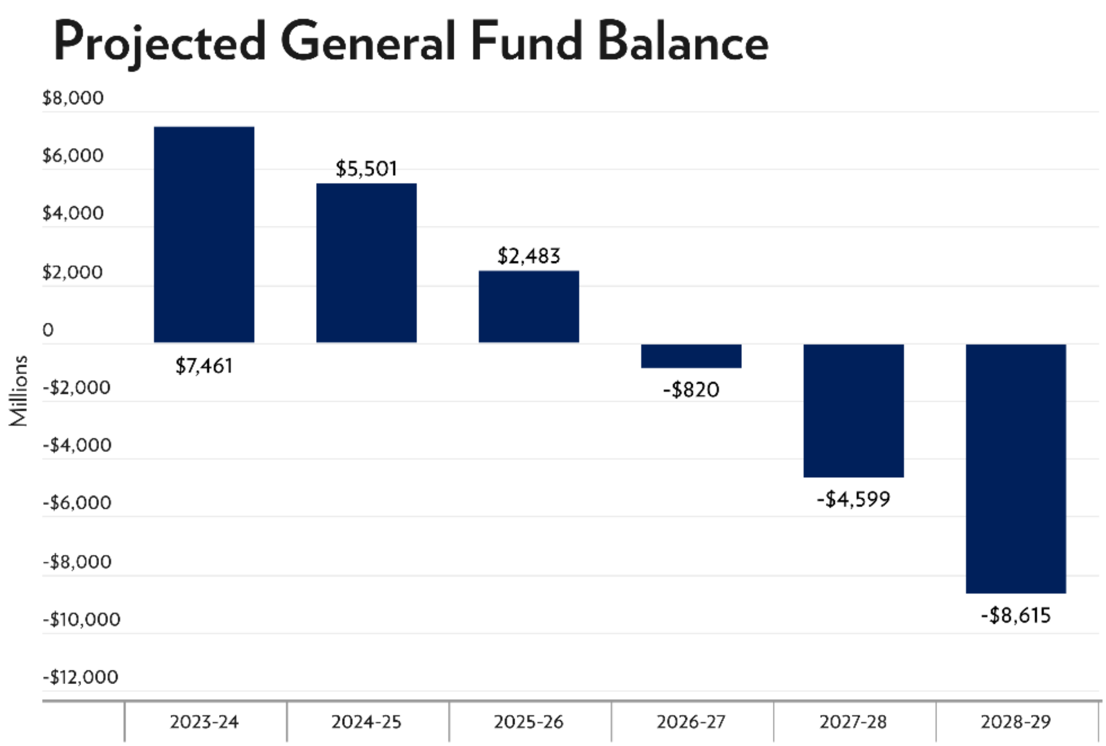
Pennsylvania's Structural Deficit

SUMMARY

- Pennsylvania's state budget is out of balance, currently operating at a $1.1 billion budget deficit.
- The state's Independent Fiscal Office (IFO) projects that Pennsylvania's annual budget deficit will rapidly expand in the next two years, reaching $3 billion in fiscal year (FY) 2025–26. At the present pace, Pennsylvania will exhaust the entirety of the General Fund balance during FY 2025–26.
- Pennsylvania's population is aging and out-migrating, which will only exacerbate the existing budgetary challenges.

FISCAL CHALLENGES

- In the current fiscal year, FY 2023–24, Pennsylvania is operating at a $1.1 billion budget deficit. The IFO projects the state's annual budget deficit will balloon to $3 billion over the next two years.
  - According to the same IFO projections, the expanding budget deficit will deplete the current General Fund balance ($7.4 billion) during FY 2025–26, at which point lawmakers will have to ***increase taxes or decrease expenditures***.



Source: Pennsylvania Independent Fiscal Office, "Five Year Economic and Budget Outlook," November 2023, http://www.ifo.state.pa.us/download.cfm?file=Resources/Documents/Five_Year_Outlook_2023.pdf

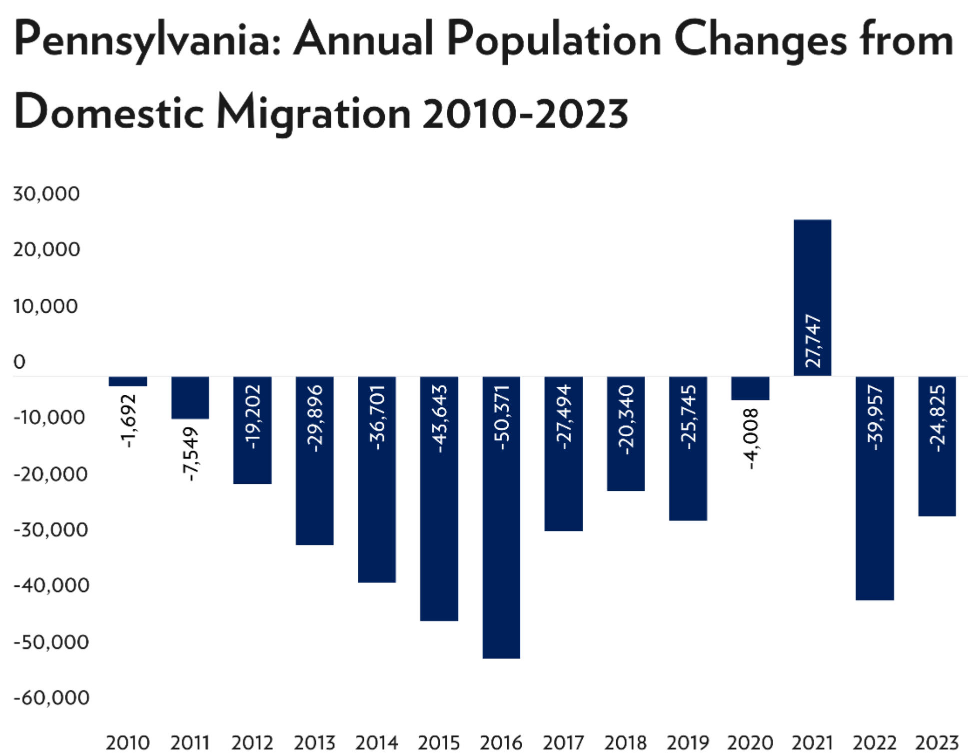
- Recent credit upgrades from Moody's and Fitch were a result of the state holding stable budgetary reserves. Pennsylvania's Treasury transferred $898 million to the commonwealth's Rainy Day Fund in November. With the transfer, Pennsylvania has enough reserves—in the case of recession, disaster, or emergency—to fund state government for 48 days. Maintaining these reserves is essential to Pennsylvania's fiscal health.
- However, using the Rainy Day Fund for ongoing overspending is illegal. State law dictates Rainy Day Fund reserves "shall not be used to begin new programs but to provide for the continuation of vital public programs in danger of being eliminated or severely reduced due to financial problems resulting from the economy."

- Rapid expenditure growth is driving the increasing budget deficit.
  - The IFO projects General Fund expenditures to grow by 3.4 percent per year while revenue grows by 2.1 percent.
  - Line items for long-term living (33.5 percent), intellectual disabilities (23 percent), state personnel (20.9 percent), medical assistance (19.6 percent), and pre-K to 12 education (13.8 percent) are the driving factors behind rapid expenditure growth.
    - Long-term living expenditures continue to increase, with the program accounting for an ever-larger portion of the state budget. During FY 2018–19, the program was 8.3 percent of total expenditures. The IFO projects long-term living will account for 14.3 percent of total expenditures in FY 2028–29.

SHIFTING DEMOGRAPHICS

- Pennsylvania's aging population is a driving factor behind rapid expenditure growth. As the population ages, the demand for social services programs such as long-term living and medical assistance increases accordingly.
  - The advanced age cohort, defined as residents over the age of 80, is forecast to expand by 20.8 percent from 2025 to 2030.
  - The dependency ratio, which measures the number of working adults per senior, is rapidly decreasing. The IFO projects that the dependency ratio will decrease to 2.5 working adults per senior in 2030, down from 3.5 in 2015.
  - The labor force participation rate remains below where it was before the COVID-19 pandemic. Older individuals are less likely to participate in the labor force, and a segment of the working-age population that left the labor force during the pandemic has not yet returned.
- An aging population also has significant impacts on slower revenue collection. Pennsylvania does not tax retirement income and offers property tax breaks for seniors. As the senior and retiree population expands, the state will collect less tax revenue.
- Adding to the aging demographic shift, Pennsylvania's working-age residents are leaving for other states.
  - Pennsylvania has lost population to other states from domestic outmigration in 12 of the last 13 years, including a combined 64,782 residents over the past two years.

- A recent survey from the Commonwealth Foundation found that 52 percent of polled Pennsylvanians under 30 years old have thought about leaving the state, know someone considering a move, or they know someone who's already left.
    - Desires for a lower cost of living, lower taxes, and better jobs and opportunities were the three reasons most cited for leaving Pennsylvania.
- The IFO sees the state's working-age population shrinking by 2.6 percent between 2020 and 2025, then dropping an additional 1.7 percent between 2025 and 2030.
- Experts project that Pennsylvania's population loss will lead to the state losing a U.S. House of Representatives seat and an electoral vote in 2030.



United States Census Bureau, "Annual Population Estimates, Estimated Components of Resident Population Change, and Rates of the Components of Resident Population Change for the United States, States, the District of Columbia, and Puerto Rico: April 1, 2010 to July 1, 2020" https://www.census.gov/programs-surveys/popest/technical-documentation/research/evaluation-estimates/2020-evaluation-estimates/2010s-state-total.html
2020-23 Data: United States Census Bureau, "Annual and Cumulative Estimates of the Components of Resident Population Change for the United States, Regions, States, District of Columbia, and Puerto Rico: April 1, 2020 to July 1, 2023," https://www.census.gov/data/tables/time-series/demo/popest/2020s-state-total.html#v2023