

Executive Summary

This report provides a review and evaluation of Kentucky General Fund and Road Fund for the third quarter of Fiscal Year 2004 (FY04). General Fund receipts totaled \$1,627.2 million during the third quarter, an increase of 4.5 percent from the same period of FY03. This represents \$69.4 million more than reported receipts for the third quarter of FY03.

Road Fund receipts in the third quarter of FY04 were \$276.6 million, an increase of 2.3 percent from the third quarter of FY03. This is \$6.2 million more than reported in the same period of FY03.

The third quarter of FY04 saw the economy solidifying as the recovery began to gather momentum. Real gross domestic product (GDP) expanded at an annual 4.8 percent rate in the third quarter. Personal income, a measure of spending power, was up by 3.5 percent annualized. Nonagricultural employment growth, which had been the missing ingredient in the recovery, began to appear in the third quarter, although at a low rate of 0.1 percent over one year earlier.

Kentucky's personal income was estimated at \$111.0 million in the third quarter of FY04, representing an increase of 3.4 percent from one year ago. Employment in the Commonwealth managed a meager 0.2 percent growth, with a gain of 4,200 jobs. Manufacturing, mining, information services, "other" services and government reported job losses, while construction, the combined trade,

transportation and utilities sector, and several service sectors all had healthy growth.

General Fund receipts in the third quarter grew strongly despite significant one-time gains that boosted third-quarter FY03 revenues. Unusually high individual income tax declaration payments a year ago lifted

the General Fund balance. Nevertheless, total General Fund receipts in the current quarter were even higher. Performance by major tax type is detailed in Table 3 on page 9. Among the major accounts, the sales and use tax grew by 8.9 percent, the individual income tax fell 7.5 percent, and

corporate income and license tax receipts were \$32.8 million compared to a minus \$4.1 million a year ago. The coal severance tax ended its slide by rising 5.6 percent, property taxes were up by 18.1 percent due to timing differences, and the lottery was unchanged from a year earlier. All other taxes in the General Fund combined for a growth of 3.4 percent.

The Road Fund posted a small increase in the third quarter of FY04, increasing 2.3 percent with total revenues of \$276.6 million. Summary data on third-quarter Road Fund receipts appears in Table 4 on page 11. During the third quarter, motor fuels taxes rose 4.2 percent, and the motor vehicle usage tax was



up 1.4 percent. The weight distance tax was up 6.2 percent. The remaining accounts in the Road Fund fell by 1.5 percent, due principally to a decline in toll and investment revenues.

The national economic outlook for the next fiscal quarter is for GDP growth to be 5.4 percent. In the first half of FY05, GDP should grow by 4.2 percent. During the upcoming quarter, Kentucky personal income should grow by 3.6 percent compared to 4.2 percent nationally. In the first two quarters of FY05, personal income in Kentucky is expected to rise by 3.7 percent. Employment growth in the state is expected to be muted, with a 0.6 percent rate of increase in the final quarter of FY04, rising to 1.1 percent in the first half of FY05.

The General Fund and Road Fund outlook for the next three fiscal quarters is for General Fund revenue to grow by 3.2 percent during the final quarter of FY04. For the entire fiscal year, growth should be 2.0 percent. This will result in General Fund revenues that are \$86.4 million more than forecasted in January 2004 by the Consensus Forecasting Group. Sales tax revenues should continue their growth, rising 4.5 percent during the period. Individual income taxes will rise by 3.3 percent, compared to one-time growth in the final quarter of FY03.

Other revenue sources should exhibit positive growth with the exception of the corporation income and license taxes and the Lottery. Due to a moratorium on enforcing the ITW decision, the corporation license tax should decline, making the loss 2.0 percent for the combined income and license accounts. The Lottery is forecasted to be unchanged, reflecting the impact of the new Tennessee lottery.

The first half of FY05 should see General Fund revenues up by 3.2 percent. Most major accounts will see increases except for the Lottery, which will continue to experience a drop in demand as a fallout of the Tennessee lottery. The "other" accounts will fall based on lower inheritance taxes and abandoned property receipts.

The interim forecast for the Road Fund is for a decline of 0.4 percent during the final quarter of FY04. Revenues should exceed the January 2004 consensus estimate by \$3.1 million. Motor fuels taxes are expected to grow by 0.2 percent, and motor vehicle usage tax receipts are forecasted to rise by 3.3 percent. These should be countered by declines in toll income and investment income, which are forecasted to drop by 68.6 percent and 57.3 percent respectively. For the first two quarters of FY05, the Road Fund is forecasted to expand by 2.7 percent.

The Economy

NATIONAL ECONOMY

Third Quarter, FY04

Though the recession of 2001 has been over for two years, the lack of job growth and consumer confidence has made this a lackluster recovery at best. During the third quarter, however, job growth has strengthened, even as productivity has continued to increase. The upturn in the employment market, in spite of the scare from outsourcing and the conflict in Iraq, has caused consumer confidence to rise.

Real gross domestic product (GDP) is an inflation-adjusted measure of the total output of goods and services produced in the United States. Real GDP is estimated to have increased by a robust 4.8 percent in the third quarter. This is a continuation of the strong economic growth that was established a year ago with GDP growth of 3.3 percent in the third quarter of FY03. Growth rates within the 3.5 percent to 5.0 percent range are thought to be optimum for increasing employment. The current recovery seems to be the result of several factors. Chief among them are the aggressive monetary policy of the Federal Reserve and the fiscal impact of tax cuts earlier this fiscal year. Both of these policies have had an impact on consumers.

The strength of the domestic economy is derived from the American consumer. Consumption expenditures account for about two-thirds of real GDP. Real consumption

was up 3.4 percent during the third quarter following an increase of 2.7 percent in the previous quarter. However, the consumption of durable goods was down 3.2 percent, because of an anticipated decline in automobile purchases (down 8.2 percent) after more than a year of feverish growth. Consumption of nondurable goods was up 5.7 percent. Nondurables are normally quite stable and not prone to swings from interest rates and incentives. The strong growth was from the rise in fuel prices and the associated increase in food expenditures resulting from increased transportation costs. Services constitute a little over one-half of all consumption and about 35 percent of total GDP. The consumption of services increased by 3.6 percent in the third quarter. Much of the increase came from the area of personal and business services.

Investment spending continues to improve and indicates that the economic recovery is here to stay. Total investment comprises close to a fifth of real GDP and is usually sensitive to both interest rates and future expansion opportunities. The investment component of GDP increased by 10.9 percent during the third quarter after having posted robust growth of 15.8 percent in the previous quarter. One of the areas with the biggest gains was investment in equipment and software, up 14.5 percent.

Government spending constitutes 17 percent of GDP and was up 3.9 percent. Defense spending, as would be expected, was up 13.6 percent during the third quarter. State and local government spending declined by 0.2

percent primarily as a result of revenue constraints. For the third quarter in a row the weak dollar has caused exports to increase faster than imports. During the third quarter U.S. exports grew by 10.6 percent, but imports were up by just 7.1 percent.

GOEA monitors industrial production because it is a measure of the output of heavy industries like mining and manufacturing. These industries continue to play a vital role in Kentucky's economy. Industrial production is a raw measure of output, comprised of only the final products. Total industrial production was up 5.0 percent during the third quarter compared to 0.9 percent a year ago. The rise in domestic industrial production is caused to some extent by the weakness of the dollar with respect to the yen and the euro. All major areas of production were up except textile mills and apparel. Much of this reflects consumer confidence shoring up as a result of positive business news, and from the feeling that the long-drawn recession is finally over. The University of Michigan Consumer Sentiment Index for the third quarter was at 96.9 compared to 80.0 a year ago. Factory capacity utilization is still very low (74.9 percent) as production costs in Asian countries, particularly China, make it cost-effective to locate manufacturing plants abroad.

Personal income, which is a measure of spending power, was \$9,409.7 billion in the third quarter, for an annualized increase of 3.5 percent over the previous quarter. Real disposable income was up 4.2 percent while real expenditure was up 3.4 percent. The lower spending has kept the savings rate at 1.8 percent.

During the first half of FY04 nonfarm employment declined by 0.2 percent, even as

the economy grew in terms of output. In the third quarter, however, employment registered a slight up tick with a job growth of 0.1 percent. The unemployment rate also dropped to 5.6 percent from 5.8 percent a year ago.

The increase in crude oil prices during the third quarter has caused inflation to rise to 3.4 percent compared to 0.7 percent in the previous quarter.

STATE ECONOMY

The long recession that dragged down Kentucky's employment seems to be over. Employment has not returned to March 2000 levels, but there has been positive movement in the economy in response to the federal fiscal and monetary stimulus. During the third quarter key measures like employment and income firmed up, indicating that Kentucky is on a steady path to recovery.

Kentucky's personal income is estimated to be \$111.0 billion in the third quarter of FY04, an increase of 3.4 percent from a year ago. U.S. personal income grew by 4.0 percent during the same period. Wages and salaries constitute a little over half of personal income. Income derived from wages and salaries is estimated to have grown by just 1.6 percent in FY04:3, compared to 2.9 percent nationally. Kentucky's lower growth in wage and salary income is because of the continued erosion of the traditionally high-wage manufacturing sector. Other areas of personal income, namely dividends, interest, and rent as well as proprietors' income, grew more slowly in Kentucky than in the national economy.

Employment data is commonly used to gauge the strength of the state's economy, primarily because of its timely availability and its

impact on consumer spending and confidence. Kentucky gained approximately 4,200 jobs during the third quarter compared to a year ago. Though the employment gains are slight at just 0.2 percent, it is an important turnaround from the decline in employment over the last three quarters.

Manufacturing jobs in Kentucky have been the hardest hit by the recession. During the third quarter manufacturing employment continued to slide, resulting in a loss of 3,900 jobs. Among the large industries hardest hit in Kentucky were electronic and electrical equipment and fabricated metal productions. Both of these sectors have suffered nationally, too, as jobs have moved overseas. The automotive sector posted a strong gain in response to brisk sales. The Ford F-series

truck was the best selling vehicle in 2002 and the Toyota Camry was the best selling car. Both are manufactured in Kentucky.

A little over one-third of Kentucky's nonagricultural jobs are in the services sector. The service-related industries are part of four categories or super sectors. These are business services, educational and health services, leisure and hospitality services, and other services. Overall employment in services was up 0.6 percent with the strongest gains in business services, up 2.1 percent. The business service category is dominated by temporary employment services, and it is possible that the strong growth in this sector is from the reluctance of businesses to hire permanent employees until the economic recovery has strengthened.



Table 1
National Economic Indicators
Third Quarter, FY04

	FY03:3	FY04:2	FY04:3	SAAR** FY04:2 to FY04:33	FY03:3 to FY04:3 Percent Change
Real GDP (billion 2000 \$)	10,210.4	10,599.2	10,724.1	4.8	5.0
Personal Income (billion \$)	9,048.7	9,329.3	9,409.7	3.5	4.0
Real Disposable Income (billion 2000 \$)	7,662.0	7,872.0	7,953.7	4.2	3.8
Consumer Price Index (annual percent change)	3.9	0.7	3.4	-	-
Industrial Production (annual percent change)	0.9	5.4	5.0	-	-
Civilian Labor Force (millions)	145.9	147.0	147.3	0.8	1.0
Total Nonagricultural Employment (millions)	130.0	130.0	130.2	0.5	0.1
Manufacturing Employment (millions)	14.8	14.3	14.3	-1.0	-3.2
Unemployment Rate (percent)	5.8	5.9	5.6	-	-

Sources: Global Insight, Inc., and U.S. Dept. of Commerce, Bureau of Economic Analysis.

* Data for FY04:3 are March 2004 estimates and cover the period January to March 2004.

** Seasonally adjusted annual percent growth rate.

Table 2
Selected Kentucky Economic Indicators
Seasonally Adjusted Data

	FY03:3	FY04:3	Percent* Change
Total Personal Income (\$ millions)	107,330	110,980	3.4%
Wage & Salary Income (\$ millions)	57,940	58,881	1.6%
Total Nonagricultural Employment	1,783.2	1,787.4	0.2%
Contract Construction	82.5	86.2	4.5%
Mining	19.3	19.1	-1.4%
Manufacturing	268.7	264.8	-1.4%
Trade, Transportation & Utilities	370.2	373.8	1.0%
Information	30.6	29.9	-2.2%
Finance	85.6	86.1	0.6%
Business Services	154.0	157.2	2.1%
Educational and Health Services	227.0	228.0	0.4%
Leisure and Hospitality Services	154.6	157.2	1.7%
Other Services	76.2	73.9	-3.1%
Government	314.4	311.0	-1.1%

* Seasonally adjusted rate from a year ago.

Source: Governor's Office for Economic Analysis, Macromodel of Kentucky, March 2004.

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Revenue Receipts

THIRD QUARTER, FY2004

General Fund

The third quarter of FY04 posted a 4.5 percent increase over the third quarter of FY03, following weaker performance for the previous two quarters of FY04. Receipts in the third quarter totaled \$1,627.2 million compared to \$1,557.8 million received in the third quarter of FY03. Sales tax collections were higher in this quarter than in several consecutive past quarters, as was the withholding component of individual income tax.

Collections in the major revenue categories are shown in summary form in Table 3. Detailed information on these and other accounts appears in the Appendix.

As usual, variations in the quarterly receipts are affected by differences in the timing of payments into revenue accounts. This was true for both individual and corporate income taxes, where differences resulted from the processing of refund claims.

Total sales and use tax receipts for the quarter were \$598.6 million, compared to \$549.6 million in the third quarter of FY03. This increase of 8.9 percent is an improvement over recent quarters.

The individual income tax posted receipts of \$566.5 million, compared to last

year's third-quarter receipts of \$612.6 million. This decline of 7.5 percent was solely the result of unusual individual declaration payments in January of FY03 that were significantly higher than this year.

Corporation income tax receipts posted positive revenues of \$32.8 million, and compare to net negative year-earlier figures of \$4.1 million. Net negative receipts in the third quarter of FY03 resulted from the timing of refund payments.

Property tax receipts posted an 18.1 percent increase over the third quarter of a year ago. FY04 third-quarter receipts of \$134.7 million compare with \$114.0 million from the same period of FY03. As usual, there were some timing differences within the different property tax accounts, which account for the increase in this quarter.

Table 3
Summary General Fund Receipts
Third Quarter, FY 2004
(millions of dollars)

<u>Type Tax</u>	<u>FY04</u>	<u>FY03</u>	<u>Percent Change</u>
Sales and Use	598.6	549.6	8.9
Individual Income	566.5	612.6	-7.5
Corporation Inc./Lic.	32.8	-4.1	--
Coal Severance	34.9	33.0	5.6
Property	134.7	114.0	18.1
Lottery	50.0	50.0	0.0
All Other	<u>209.6</u>	<u>202.7</u>	<u>3.4</u>
TOTAL	\$1,627.2	\$1,557.8	4.5%

Coal severance tax reversed recent trends to post an increase of 5.6 percent. Collections of \$34.9 million compare to the FY03 third-quarter total of \$33.0 million.

Lottery receipts were \$50.0 million, matching last year's third-quarter total. Lottery receipts were significantly bolstered by large PowerBall jackpots in the third quarter of both fiscal years.

The "all other" category, which represents the remaining accounts of the General Fund, increased by 3.4 percent in the third quarter. Third-quarter receipts for FY04 were \$209.6 million and compare to \$202.7 million in FY03. The only significant variances were larger than ordinary increases in natural gas severance tax and in abandoned property receipts.

Road Fund

The Road Fund reported a small increase in the third quarter of FY04, following a small decline in the second quarter. Receipts were up 2.3 percent from the third quarter of FY03. Receipts totaled \$276.6 million and compare to \$270.4 million from the third quarter of last year. Summary

data are contained in Table 4 and detailed data are shown in the Appendix.

Motor fuels tax receipts increased at a rate of 4.2 percent during the third quarter. Receipts were \$106.3 million and compare to \$102.0 million collected during the third quarter of last year.

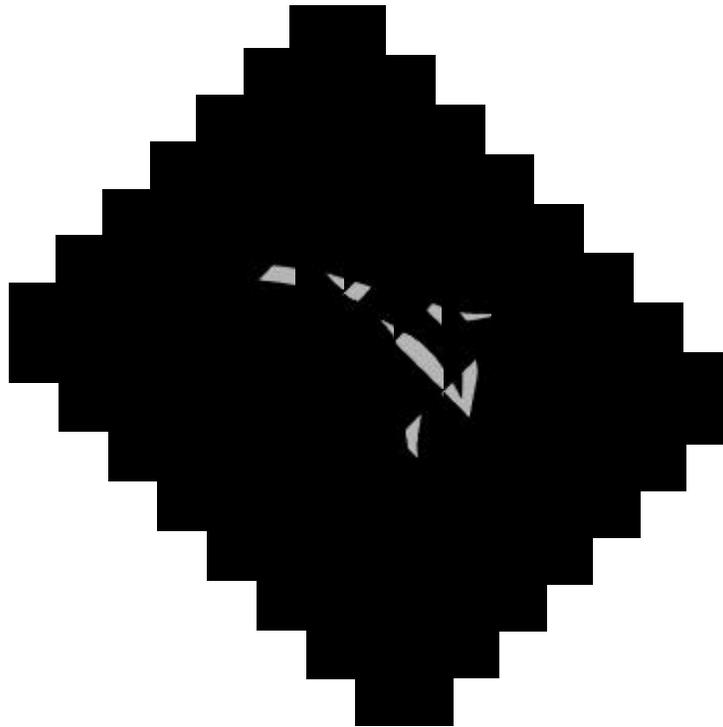
The motor vehicle usage tax also posted a small increase in the third quarter, with receipts up by 1.4 percent. Receipts during the third quarter of FY04 totaled \$103.8 million and compare to \$102.4 million collected during the same period last year.

Weight distance tax receipts of \$20.0 million represent a 6.2 percent increase over receipts of \$18.8 million during the third quarter of FY03.

The remainder of the accounts in the Road Fund combined for a decrease of 1.5 percent from a year earlier chiefly due to declines in departmental fees, highway tolls and investment income. In the "all other" category revenues of \$46.5 million were down from \$47.2 million in the third quarter of FY03.

Table 4
Summary Road Fund Receipts
Third Quarter, FY 2004
(millions of dollars)

<u>Type Tax</u>	<u>FY04</u>	<u>FY03</u>	<u>Percent Change</u>
Motor Fuels	106.3	102.0	4.2
Motor Vehicle Usage	103.8	102.4	1.4
Weight Distance	20.0	18.8	6.2
All Other	<u>46.5</u>	<u>47.2</u>	<u>-1.5</u>
TOTAL	\$276.6	\$270.4	2.3%



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Economic and Revenue Outlook

ECONOMIC OUTLOOK: Interim Forecast

The economic outlook presented here is for the three-quarter period from April to December 2004. In terms of fiscal years this period is the final quarter of FY04 (April to June 2004) and the first half of FY05. The national outlook is based on Global Insight's March 2004 forecast, and the Kentucky outlook is from GOEA's March 2004 forecast.

Broadly, Kentucky's economic outlook for the fourth quarter of FY04 is unchanged from that presented to the Consensus Forecasting Group in January. For the first two quarters of FY05, however, both employment and income estimates are lower than the earlier forecast. The continuing increase in labor productivity as well as a revision in federal data on income are the two major reasons for the downward revision in the FY05 forecast.

National Economy

The economy is expected to strengthen further during the final quarter of FY04. Almost all indicators associated with a broad recovery are strongly positive. The biggest movement is in real GDP which is forecasted to rise by 5.4 percent during the fourth quarter of FY04. Other factors like investment, productivity, and consumer confidence showed robust growth. Even employment, which had slid by 0.4 percent a year ago, should move up by 0.5 percent during the final quarter of FY04.

During the first half of FY05 real GDP is expected to grow by 4.2 percent from a year ago. Growth is expected to moderate because

the impact of last year's tax cuts has substantially lessened. Both monetary policy in the form of lower interest rates, and fiscal policy in the form of tax cuts and rebates have primed the economy enough so that it can now grow at its long-term growth rate of between 3 to 4 percent. Employment in nonagricultural industries, which has been flat or negative during the recovery so far, is forecasted to rise by 1.2 percent during the first half of FY05 compared to a decline of 0.3 percent a year ago.

The consumption component of GDP has recently been the major factor in sustaining growth. During the last quarter of FY04 real consumption expenditures are projected to increase by 4.3 percent with durable goods rising dramatically by 9.7 percent. The strong performance of durable goods is related to the purchase of furniture and a rebound in automobile sales. Consumption growth during the first half of FY05 is expected to be 3.3 percent. The slower growth is related to moderation in the durable goods market and a return to a sustainable growth rate.

Investment spending has been accelerating in recent months, and the outlook is for a continuation of that trend. During the fourth quarter of FY04 investment is expected to rise by 11.6 percent, and then by 9.0 percent in the first half of FY05. The surge in investment is from the expectation that consumer demand will increase and the economy will continue to expand.

The weak dollar is expected to cause a surge in exports, and at the same time put a damper

on imports. U.S. exports are forecasted to show gains of 13.1 percent in FY04:4, and then 12.8 percent in the first half of FY05. The corresponding import numbers are 8.0 percent and 8.6 percent.

Until recently the economic recovery had been described as either a “jobless recovery” or a “job loss recovery.” The tide has turned and employment is on the rise. The unemployment rate is expected to slide to 5.6 percent during the fourth quarter compared to 6.1 percent a year ago. It is predicted to go down to 5.5 percent in the first half of FY05 compared to 6.0 percent in the same period a year ago. Similarly, nonfarm employment is picking up. Job gains are expected to be 0.5 percent in FY04:4, and further improve to 1.2 percent during the first half of FY05 with a net gain of 1.6 million.

State Economy

Kentucky’s economy is also in the recovery phase, but the dominance of the goods-producing sector in the state economy has slowed the recovery. During the final quarter of FY04 personal income is estimated to increase by 3.6 compared to 4.2 percent nationally. The recovery is expected to be slightly stronger during the first half of FY05 with income growth of 3.7 percent, but the national average is forecasted to grow much faster at 4.5 percent. The lower growth in Kentucky is due primarily to the employment mix.

During the first three quarters of FY04 total nonagricultural employment in Kentucky declined compared to a year ago. A combination of factors are, however, expected to push employment growth to 0.6 percent in the final quarter of the year,

followed by stronger growth of 1.1 percent growth in the first half of FY05. These factors are related to a boost in consumer confidence and the subsequent increase in consumer demand.

Employment in goods-producing industries had declined dramatically in Kentucky in response to productivity gains and the shift of some manufacturing facilities abroad. However, the lower dollar and increased consumer demand are expected to result in gains in the next three quarters. During the fourth quarter of FY04 employment in the goods-producing sector is expected to be up 1.0 percent. During the first half of FY05, as manufacturing recovers, employment in the goods-producing sector is expected to be up 1.2 percent.

Service-providing industries are forecasted to do well during the fourth quarter of FY04 with an addition of 8,800 jobs. The growth rate during the first half of FY05 is expected to be 1.0 percent. The tepid growth rate of an otherwise strong sector is due to a drop in employment in the information services sector and in personal services.

General Fund

Projected General Fund revenues for the next three quarters are shown in Tables 6-A and 6-B. The interim forecast incorporates the fiscal impact of legislation enacted by the 2004 General Assembly. General Fund revenues are anticipated to total \$1,841.5 million in the final quarter of FY04, yielding a growth rate of 3.2 percent over the same period a year ago. For the entire fiscal year, total General Fund collections are expected to grow 2.0 percent, with total revenues of \$6,921.6 million. Compared to the official

consensus revenue estimate as of January 2004, General Fund revenues are now projected to be \$86.4 million higher in FY04, largely due to the strength of the sales and individual income taxes.

In the initial two quarters of FY05, General Fund revenues should grow by 3.2 percent when compared to the same period one year earlier.

Sales and use tax receipts are estimated to grow by 4.5 percent in the final quarter of FY04. Year-to-date growth in sales and use tax revenue has been low as an aftereffect of one-time monies realized in the previous fiscal year. Expectations are for this tax to grow considerably in the final quarter of FY04 as the economy strengthens. In the first two quarters of FY05, the sales and use tax will grow by 5.2 percent reflecting economic growth.

The interim forecast for the **individual income tax** calls for receipts in the remaining quarter to grow by 3.3 percent. As in the sales tax, one-time monies were realized in this account during FY03, which boosted receipts in the first three quarters of the previous fiscal year. Revenues for the fiscal year should total \$2,776.5 million, a growth rate for the entire year of 1.1 percent. In the first half of FY05, individual income tax revenue is expected to rise by 2.9 percent.

The outlook for **corporation income and license taxes** projects a decline of 2.0 percent in the final quarter of FY04. In the first three quarters, these two revenue sources fell by 7.2 percent. Revenues were down, affected by one-time revenues in FY03 resulting from tax amnesty. As a result, receipts have lagged behind so far in FY04. For the remainder of the fiscal year, revenues should continue to fall principally due a decision by

the administration to suspend enforcement of the Illinois Tool Works (ITW) decision. Corporation income and license taxes should begin to rise by 5.3 percent in the first half of FY05 as stronger growth should offset revenues lost due to suspension of ITW enforcement.

Coal severance tax revenue has fallen in the first three quarters of FY04 as the coal industry contracted in the face of declining demand. For the remaining quarter of the fiscal year, coal severance tax receipts should rise by 5.9 percent. Overall for the fiscal year, revenues should grow by 0.3 percent for a total of \$142.1 million. The growth in coal severance tax revenues should extend into the first half of FY05, when receipts are projected to rise by 6.8 percent.

Property taxes were up by 5.2 percent in the first half of FY04. Following the increase, revenues for the remainder of the fiscal year are expected to moderate to 1.2 percent growth, leading to overall revenue growth for FY04 of 4.7 percent, and revenues of \$455.1 million. Property tax receipts in the first half of FY05 should rise by 6.2 percent.

Lottery revenues for the remaining quarter of FY04 are projected to match those for the last quarter of FY03. This includes a windfall from a large Powerball jackpot that should lead to greater revenues than anticipated earlier. Total lottery revenues for the entire fiscal year should be \$173.8 million, an increase of 1.6 percent from the previous fiscal year. Due to the institution of a Tennessee lottery, receipts from this source are projected to decline by 3.1 percent in the first half of FY05.

Revenues in the **“other”** category should rise by 5.7 percent for the remainder of the fiscal year. Total revenues should therefore

equal \$532.6 million. Due to continuing expected losses in the inheritance tax as well as loss of abandoned property revenue, this category should decline by 8.6 percent in the first half of FY05.

Road Fund

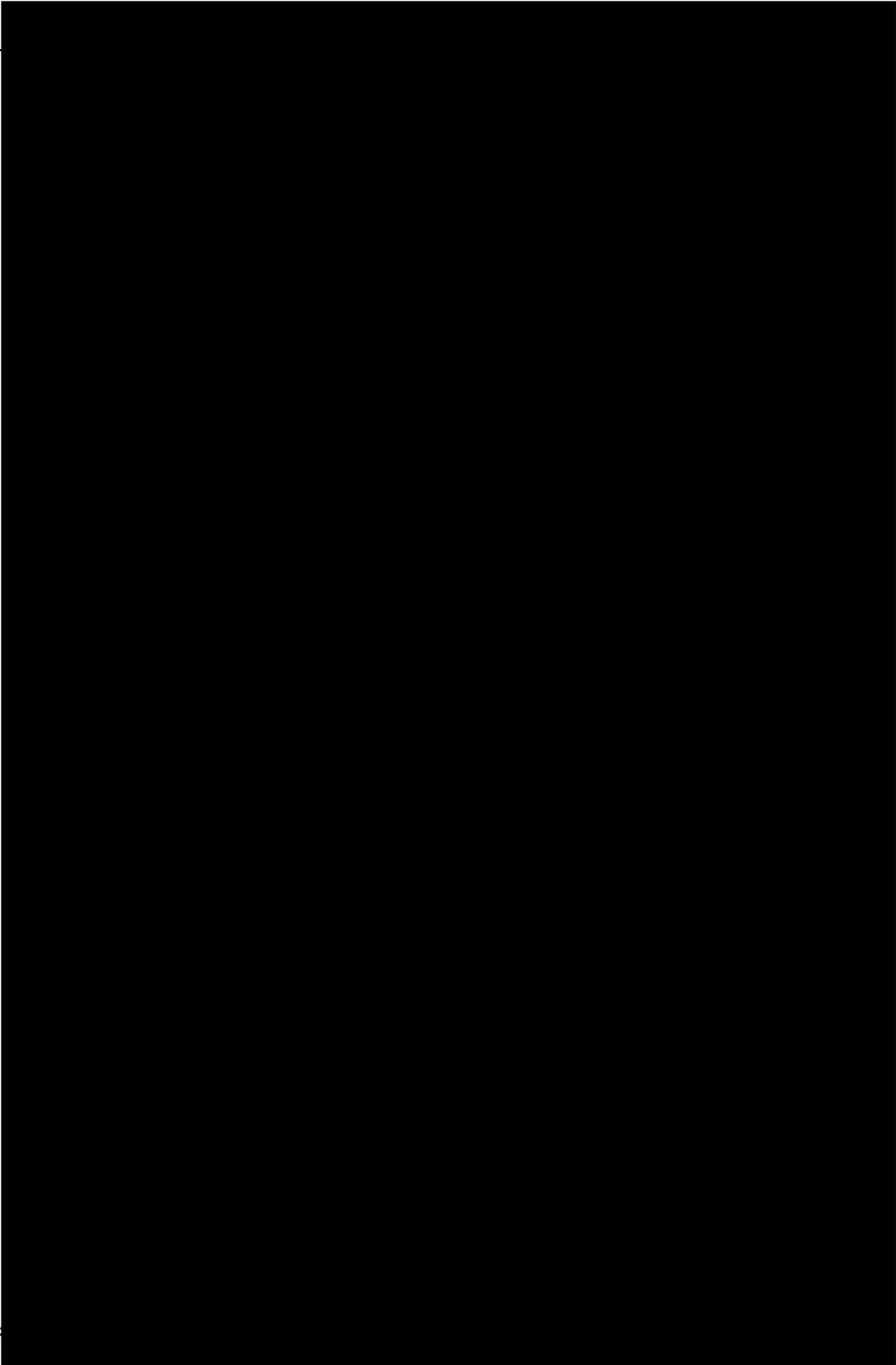
The Road Fund in the first three quarters of FY04 was slightly up by 0.4 percent, as shown in Table 7-A. The projection for the remaining fiscal quarter is for a decline of 0.4 percent. For the entire fiscal year, the Road Fund should be slightly higher than the previous year, with a total of \$1,125.7 million. Compared to the January 2004 consensus revenue estimates, General Fund revenues should be \$3.1 million higher. In the first half of FY05, revenues are expected to rise by 2.7 percent, as shown in Table 7-B.

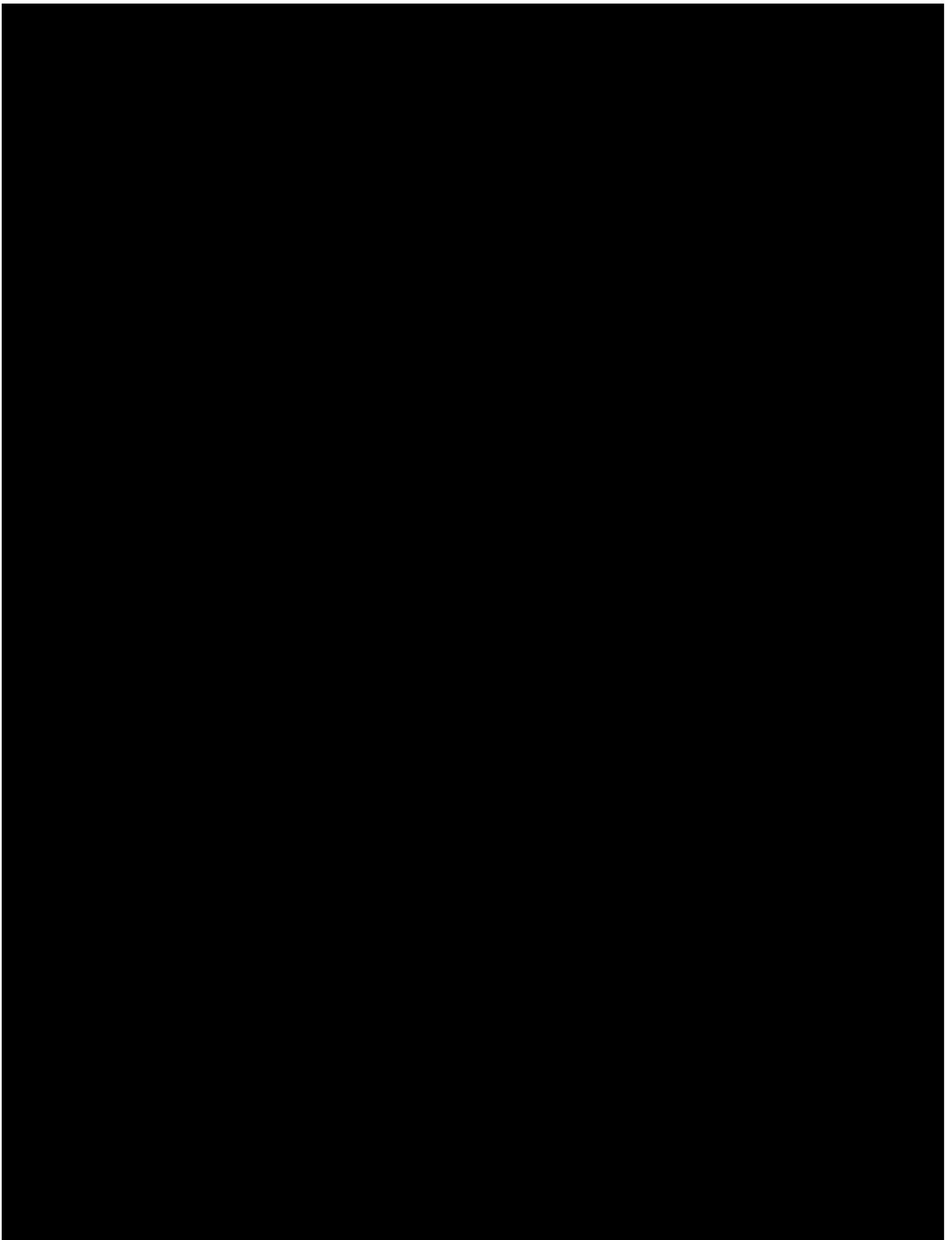
The combined total of **motor fuels normal, heavy vehicle fuel surtax, and motor fuels normal use tax** is estimated to rise by 0.2 percent in the final quarter and to rise by 1.0 percent for the entire fiscal year, with revenues of \$458.6 million. In the first half

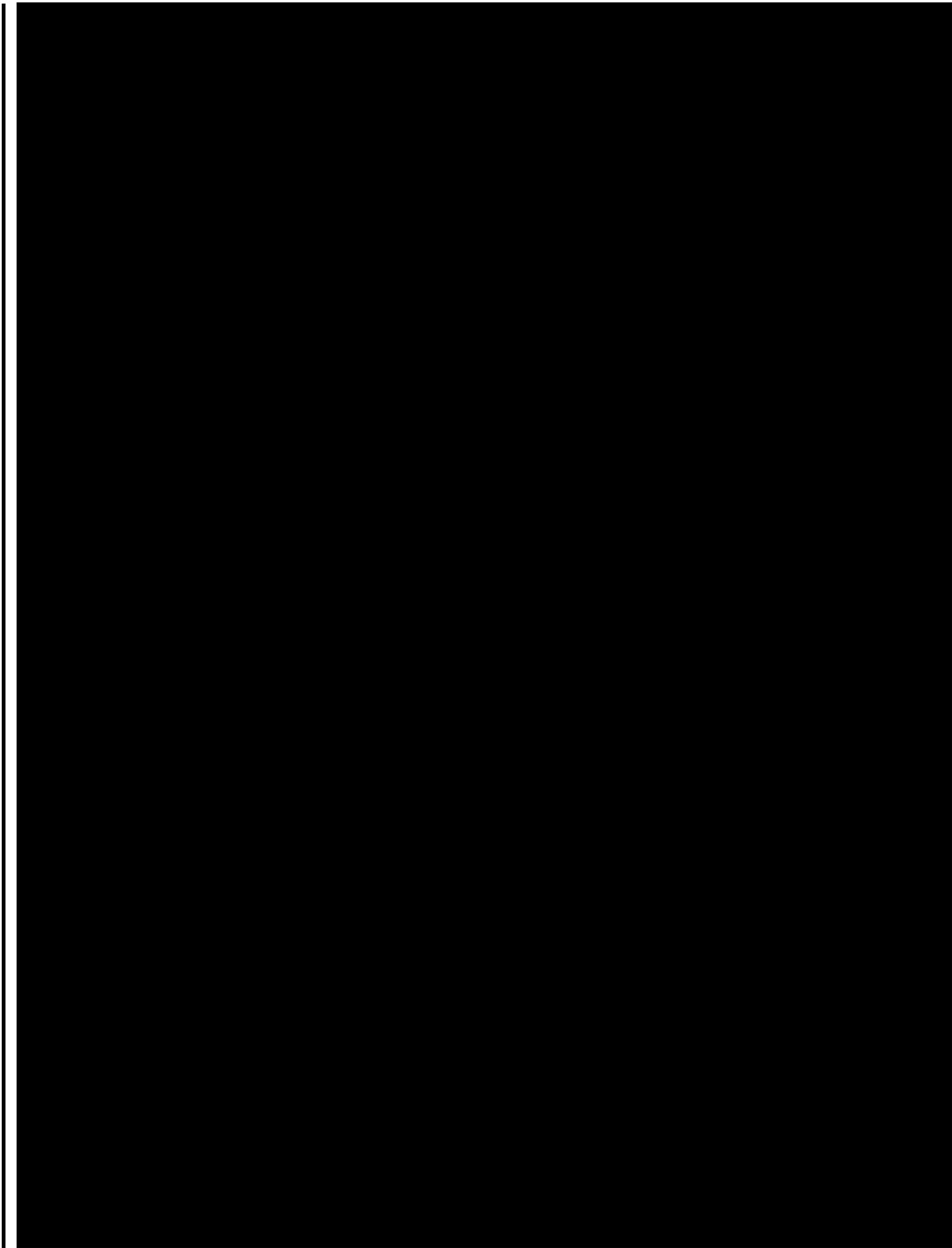
of FY05, the growth is forecasted to be 6.5 percent. The principal reason for the much higher rate of growth is the projected increase in the average wholesale price of gasoline, which should trigger an increase in the tax rate under KRS 138.220.

Motor vehicle usage taxes are expected to grow by 3.3 percent in the remainder of the fiscal year. For the entire FY04, revenues should be 1.3 percent higher than in FY03 and yield \$438.5 million. The growth is projected to continue into the first half of FY05, with gains of 2.0 percent.

To estimate growth of **all other components** of the Road Fund, Transportation Cabinet officials assessed the recent growth patterns as well as administrative factors in developing an updated estimate. License and privilege taxes (excluding the weight distance tax) are expected to rise 16.6 percent for the fiscal year, with total revenues of \$111.4 million. Toll and investment revenues are projected to decline sharply. These losses will persist into the first half of FY05.







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APPENDIX

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KENTUCKY STATE GOVERNMENT - GENERAL FUND REVENUE

	Third Quarter 2003 - 2004	Third Quarter 2002 - 2003	Percent Change	Year-to Date 2003 - 2004	Year-to Date 2002 - 2003	Percent Change
TOTAL GENERAL FUND	\$1,627,211,099	\$1,557,786,101	4.5%	\$5,080,116,858	\$4,999,694,746	1.6%
Tax Receipts	\$1,554,972,770	\$1,493,104,586	4.1%	\$4,852,017,889	\$4,812,687,049	0.8%
Sales and Gross Receipts	\$672,848,397	\$619,158,130	8.7%	\$1,982,361,927	\$1,933,661,075	2.5%
Beer Consumption	1,461,611	1,428,816	2.3	4,594,254	4,731,073	-2.9
Beer Wholesale	8,704,381	7,940,870	9.6	27,609,414	26,709,369	3.4
Cigarette	4,491,438	3,688,821	21.8	12,718,901	11,656,742	9.1
Distilled Spirits Case Sales	22,339	21,800	2.5	65,924	64,539	2.1
Distilled Spirits Consumption	2,283,449	2,215,261	3.1	6,749,125	6,525,088	3.4
Distilled Spirits Wholesale	4,356,561	4,121,543	5.7	12,681,428	12,058,064	5.2
Insurance Premium	49,705,396	47,092,198	5.5	84,467,795	79,435,667	6.3
Pari-Mutuel	771,882	702,762	9.8	1,521,991	3,117,152	-51.2
Race Track Admission	3,708	3,387	9.5	192,549	166,784	15.4
Sales and Use	598,570,894	549,581,307	8.9	1,824,767,340	1,782,624,532	2.4
Wine Consumption	523,857	512,685	2.2	1,506,171	1,440,618	4.6
Wine Wholesale	1,952,881	1,848,681	5.6	5,487,034	5,131,447	6.9
License and Privilege	\$127,077,937	\$125,633,276	1.1%	\$240,742,716	\$269,372,064	-10.6%
Alc. Bev. License Suspension	97,950	28,250	246.7	220,400	107,550	104.9
Coal Severance	34,860,757	33,001,961	5.6	104,441,772	106,162,946	-1.6
Corporation License	27,152,209	34,329,399	-20.9	50,733,906	89,018,623	-43.0
Corporation Organization	32,730	31,200	4.9	109,903	166,704	-34.1
Occupational Licenses	82,322	33,248	147.6	136,473	96,754	41.1
Oil Production	772,224	830,279	-7.0	2,343,453	2,315,939	1.2
Race Track License	3,850	3,850	0.0	287,975	285,325	0.9
Bank Franchise Tax	55,288,674	51,875,189	6.6	54,834,137	51,277,967	6.9
Driver License Fees	125,350	117,547	6.6	381,933	375,692	1.7
Minerals Severance	2,314,740	1,986,973	16.5	10,557,484	9,177,320	15.0
Natural Gas Severance	6,347,130	3,395,380	86.9	16,695,280	10,387,245	60.7
Income	\$599,267,522	\$608,440,290	-1.5%	\$2,153,150,891	\$2,128,794,860	1.1%
Corporation	32,810,242	(4,127,900)	—	183,216,077	163,022,680	12.4
Individual	566,457,280	612,568,190	-7.5	1,969,934,814	1,965,772,180	0.2
Property	\$134,691,676	\$114,021,939	18.1%	\$400,143,633	\$380,397,534	5.2%
Bank Deposits	464,372	422,944	9.8	464,093	423,204	9.7
Building & Loan Association	24,890	125,766	-80.2	61,265	158,535	-61.4
Distilled Spirits	110,967	374	—	375,637	425,348	-11.7
General - Intangible	5,697,673	3,232,839	76.2	27,175,294	22,723,818	19.6
General - Real	63,298,656	69,954,029	-9.5	186,129,841	187,424,003	-0.7
General - Tangible	41,372,148	34,176,597	21.1	118,330,322	106,352,400	11.3
Omitted & Delinquent	10,877,242	1,439,549	655.6	16,694,693	18,819,072	-11.3
Public Service	12,837,007	4,659,317	175.5	50,840,462	43,953,582	15.7
Other	8,722	10,525	-17.1	72,026	117,573	-38.7
Inheritance	\$12,390,543	\$17,382,517	-28.7%	\$48,957,103	\$78,107,706	-37.3%
Miscellaneous	\$8,696,695	\$8,468,433	2.7%	\$26,661,619	\$22,353,810	19.3%
Legal Process	6,653,789	6,524,082	2.0	20,503,275	16,599,978	23.5
T. V. A. In Lieu Payments	2,026,831	1,936,922	4.6	6,120,093	5,724,693	6.9
Other	16,076	7,429	116.4	38,251	29,139	31.3
Nontax Receipts	\$71,963,478	\$62,877,163	14.5%	\$220,937,377	\$182,005,039	21.4%
Departmental Fees	6,208,574	6,370,873	-2.5	17,349,991	16,711,574	3.8
PSC Assessment Fee	(56,566)	613	—	5,389,627	2,762,900	95.1
Fines & Forfeitures	6,843,295	6,185,385	10.6	21,337,855	22,597,492	-5.6
Interest on Investments	244,278	204,746	19.3	843,100	722,417	16.7
Lottery	50,000,000	50,000,000	0.0	132,800,000	130,000,000	2.2
Sale of NOx Credits	2,702,225	-	—	8,066,550	-	—
Miscellaneous	6,021,671	115,546	5111.5	35,150,253	9,210,656	281.6
Redeposit of State Funds	\$274,850	\$1,804,352	-84.8%	\$7,161,592	\$5,002,658	43.2%

KENTUCKY STATE GOVERNMENT - ROAD FUND REVENUE

	Third Quarter 2003 - 2004	Third Quarter 2002 - 2003	Percent Change	Year-to Date 2003 - 2004	Year-to Date 2002 - 2003	Percent Change
TOTAL ROAD FUND	\$276,583,407	\$270,372,628	2.3%	\$828,501,901	\$824,871,338	0.4%
Tax Receipts-	\$268,627,117	\$255,729,548	5.0%	\$800,623,272	\$778,222,255	2.9%
Sales and Gross Receipts	\$214,548,011	\$208,490,227	2.9%	\$661,993,786	\$655,895,053	0.9%
Motor Fuels Taxes	106,294,425	102,017,403	4.2	327,145,157	325,729,374	0.4
Motor Fuels Use & Surtax	4,357,202	4,004,653	8.8	14,255,179	11,346,709	25.6
Truck Trip Permits (fuel)	112,280	89,200	25.9	316,400	273,040	15.9
Motor Vehicle Usage	103,784,104	102,378,971	1.4	320,277,050	318,545,929	0.5
License and Privilege	\$54,079,106	\$47,239,322	14.5%	\$138,629,486	\$122,327,202	13.3%
Motor Vehicles	27,134,941	21,656,078	25.3	63,868,007	49,219,849	29.8
Motor Vehicle Operators	1,334,770	1,383,208	-3.5	4,143,938	4,247,534	-2.4
Weight Distance	19,994,286	18,821,891	6.2	59,302,464	58,164,560	2.0
Truck Decal Fees	74,246	30,607	142.6	126,757	81,631	55.3
Other Special Fees	5,540,863	5,347,538	3.6	11,188,321	10,613,628	5.4
Nontax Receipts	\$7,207,926	\$14,296,663	-49.6%	\$26,364,857	\$45,720,520	-42.3%
Departmental Fees	3,795,476	5,403,164	-29.8	11,014,194	13,612,407	-19.1
In Lieu of Traffic Fines	387,133	316,804	22.2	1,153,937	1,030,604	12.0
Highway Tolls	1,467,001	3,140,416	-53.3	6,239,211	9,750,088	-36.0
Investment Income	1,345,372	5,248,814	-74.4	7,392,463	20,885,266	-64.6
Miscellaneous	212,943	187,465	13.6	565,051	442,155	27.8
Redeposit of State Funds	\$748,364	\$346,417	116.0%	\$1,513,772	\$928,563	63.0%

1 ***Executive Summary***

3 ***The Economy***

9 ***Revenue Receipts***

13 ***Economic and Revenue Outlook***

21 ***Appendix: Third Quarter Receipts***
