# EXECUTIVE SUMMARY

**December 2021**

The economic recovery from the pandemic continues to be robust. Booming wage gains are now offsetting the fading federal aid. Household incomes and consumer spending remain strong, supporting an overall bright outlook. The economy is set to reach full employment a year from now, or three times faster than in the aftermath of the Great Recession.

The fundamental economic challenge remains the supply side of the economy trying to keep pace with demand. Labor runs through everything, from production to logistics to sales. Firms are looking to hire as quickly as possible, while labor supply has been slower to recover. Labor shortages are likely to ease some in the coming months as more workers search for a job in earnest. Even so, the labor market will remain tight for structural reasons like more retirements and less immigration.

In a supply-constrained economy real economic growth is challenging. Firms invest in new technologies to raise productivity, but this takes time. Persistent inflation is a risk. The Federal Reserve, and many private forecasters, expect inflation to cool some as the impacts of reopening the economy fade and supply chain struggles ease. While not the baseline outlook, the ultimate risk is that the economy runs too hot and the Fed raises rates sharply, creating a boom/bust dynamic in the years ahead instead of engineering the expected soft landing.

Recent forecasts have called for tax collections to return to earth. Federal aid has expired, and economic activity is beginning to return to normal with workers reentering the labor force, returning to offices and spending more on services. Instead of normalizing, however, revenue growth has accelerated further. In recent weeks, daily collection records have been set for both personal income tax withholdings and corporate tax collections. In addition, Lottery sales continue to set records for this time of year.

The revenue boom is being supported by a wide range of income sources. Most importantly, healthy gains in labor income are generating personal income tax payments. Despite Oregon having 70,000 fewer jobs relative to pre-pandemic levels, taxable wages and salaries are far above pre-pandemic trends. A persistently tight labor market is putting upward pressure on wages, leading to significant payroll growth despite the job losses.

The return of inflation after a 30-year hiatus is also generating additional revenue across a range of tax instruments. With demand so strong across the economy, businesses currently have a considerable amount of pricing power, and have been able to pass most of their cost increases along to consumers. As a result, profits and other taxable business incomes are booming. In addition to the direct boost to tax collections, healthy business earnings are supporting equity markets and other forms of investment income.

Inflation is also generating additional Corporate Activity Tax collections. Business sales are taxed by value, not by the quantity sold. As a result, tax liability has risen along with prices, and is expected to remain higher throughout the forecast horizon.

The recent revenue boom, together with an improving outlook for labor earnings, have led to a significant upward revision to the outlook for personal and corporate income tax collections. The current forecast now projects both a $558 million personal income tax kicker, and a $250 million corporate kicker as the forecasts have been raised more than 2 percent since the Close of Session. However, considerable uncertainty remains. Although the baseline outlook calls for continued growth, overheating remains a real possibility. Inflationary booms of the sort we are experiencing today traditionally do not end well, putting recent revenue gains at risk going forward.