

# Inflation: An Alaska Perspective

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## Agenda

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1. Inflation Background
2. Alaska Economy Overview
3. State Revenue Impacts
4. Budget Impacts
5. REMI Modeling of Higher Inflation
6. Takeaways



# Inflation Background

## Inflation Background: Different Measures

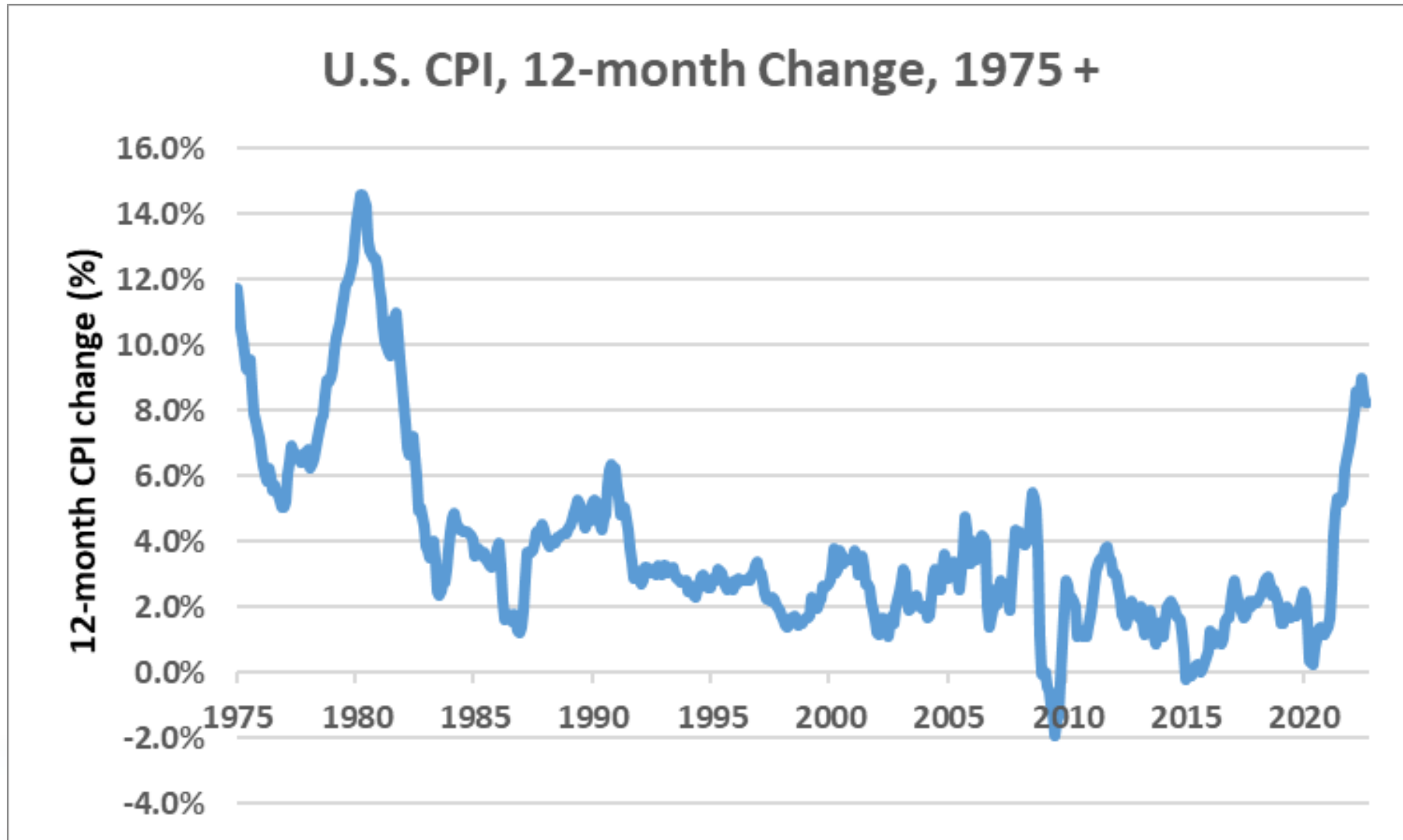
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- **Consumer Price Index (CPI)**
  - Published by Bureau of Labor Statistics
  - Price of a basket of goods over time
  - Most common / well-known index
  - “Headline” (all items) or “core” (excluding food and energy)
- **Personal Consumption Expenditures (PCE)**
  - Published by Bureau of Economic Analysis
  - Attempts to track what is actually purchased - broader, allows for substitution
  - Federal Reserve preferred measure; less volatile
  - “Headline” (all items) or “core” (excluding food and energy)

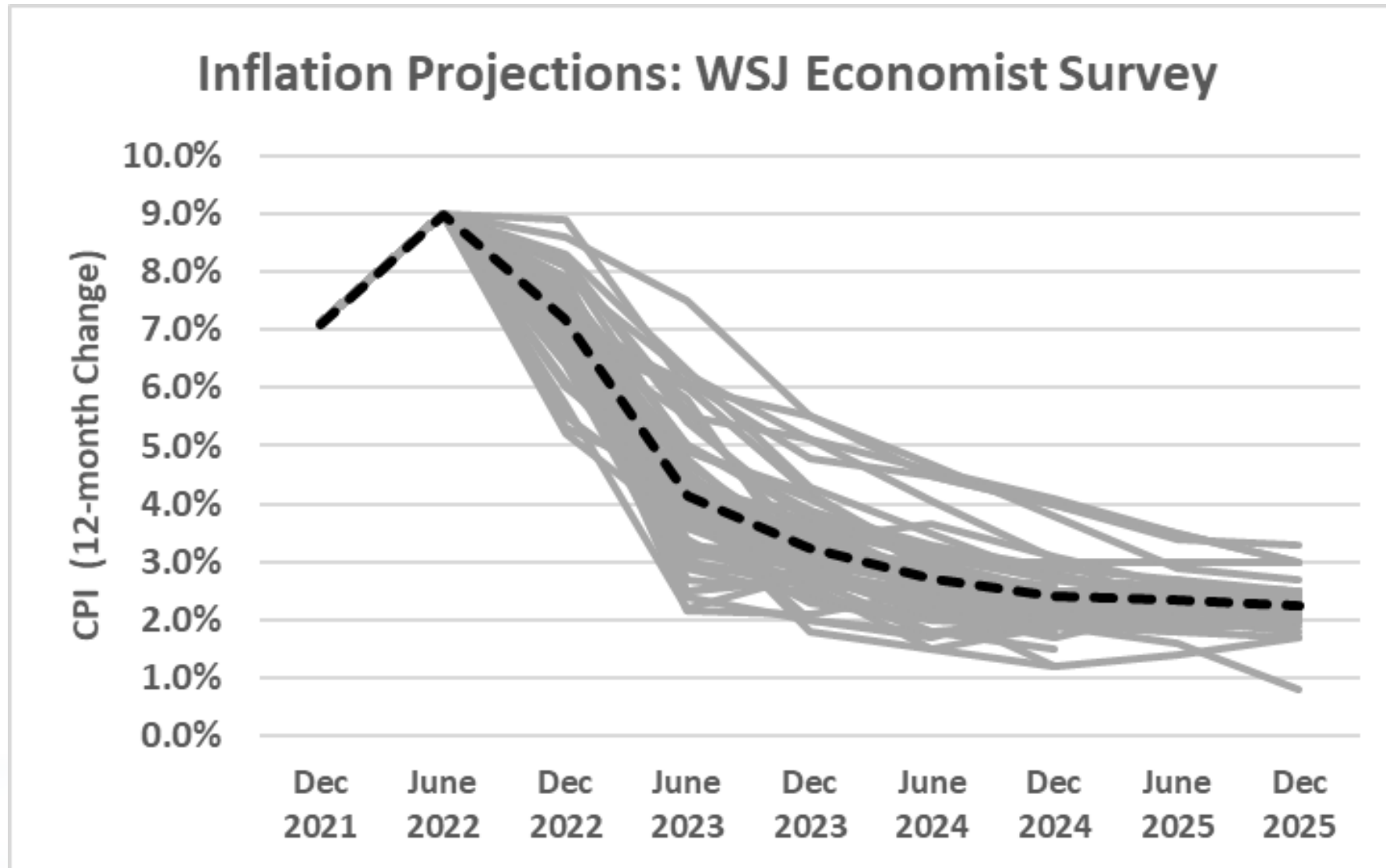




## Inflation History: Exceeded 4% since April 2021



## Inflation Outlook: Wall Street Journal Economist Survey



## Inflation Outlook: Different Sources

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- Private Forecasters – Expect inflation to reach 2.4% by end of 2024, 2.25% by end of 2025
- State Forecast (Callan) – 2.25% over 10 years
- Market Implied Inflation Outlook – 2.35% over 10 years
- Fed Target – 2.0% long term (expect to reach in 2025)
  - Target is based on PCE; CPI tends to be slightly higher
- Conclusion: There's a consensus that inflation will return to the 2.0-2.5% range
  - *But we're being asked: what if it doesn't?*



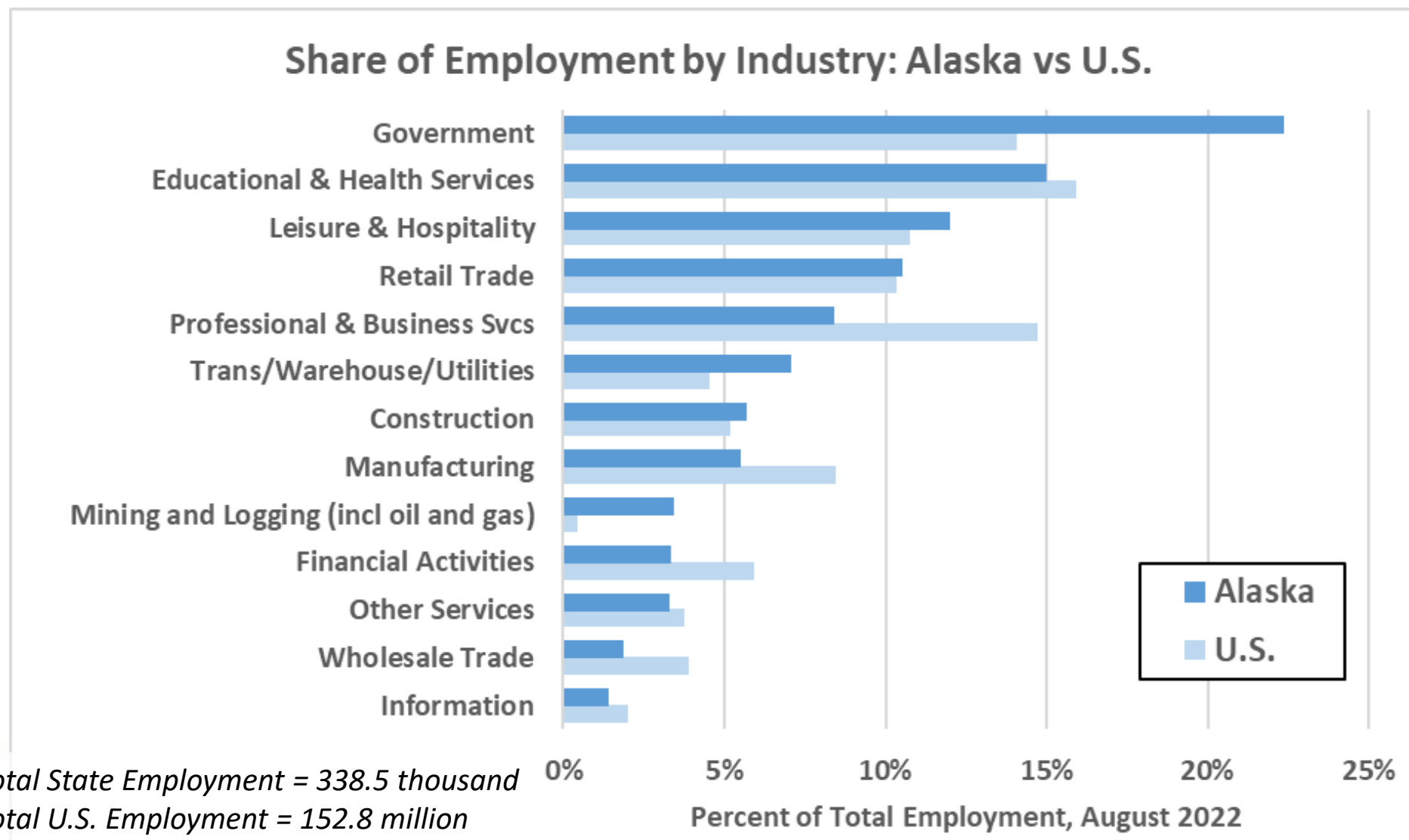
# The Alaska Economy



## Contributions to State GDP: 2022



## Contributions to State Employment: August 2022



## Relative Contributions to Total State Revenue: FY 2023

**Total State Revenue: \$16.4 Billion**

**Petroleum  
31.4%**

**Federal  
Revenue  
31.2%**

**Investment  
Earnings  
30.0%**

*Alaska does not have a state sales tax or  
personal income tax.*

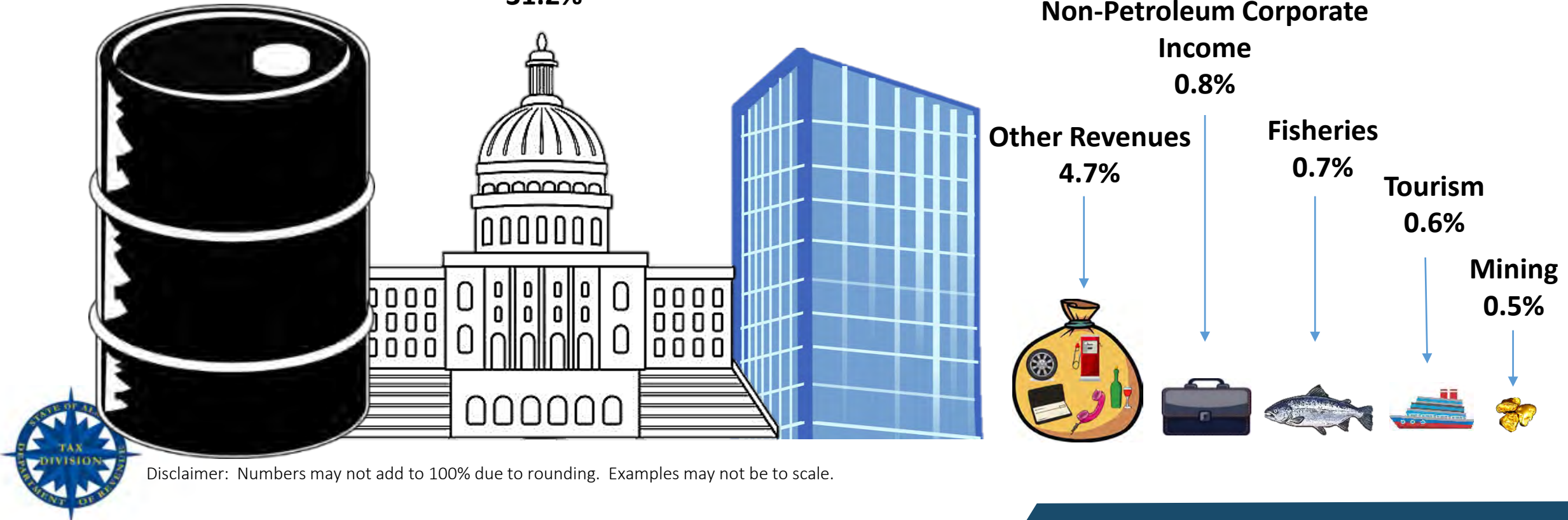
**Non-Petroleum Corporate  
Income  
0.8%**

**Other Revenues  
4.7%**

**Fisheries  
0.7%**

**Tourism  
0.6%**

**Mining  
0.5%**



## The Permanent Fund

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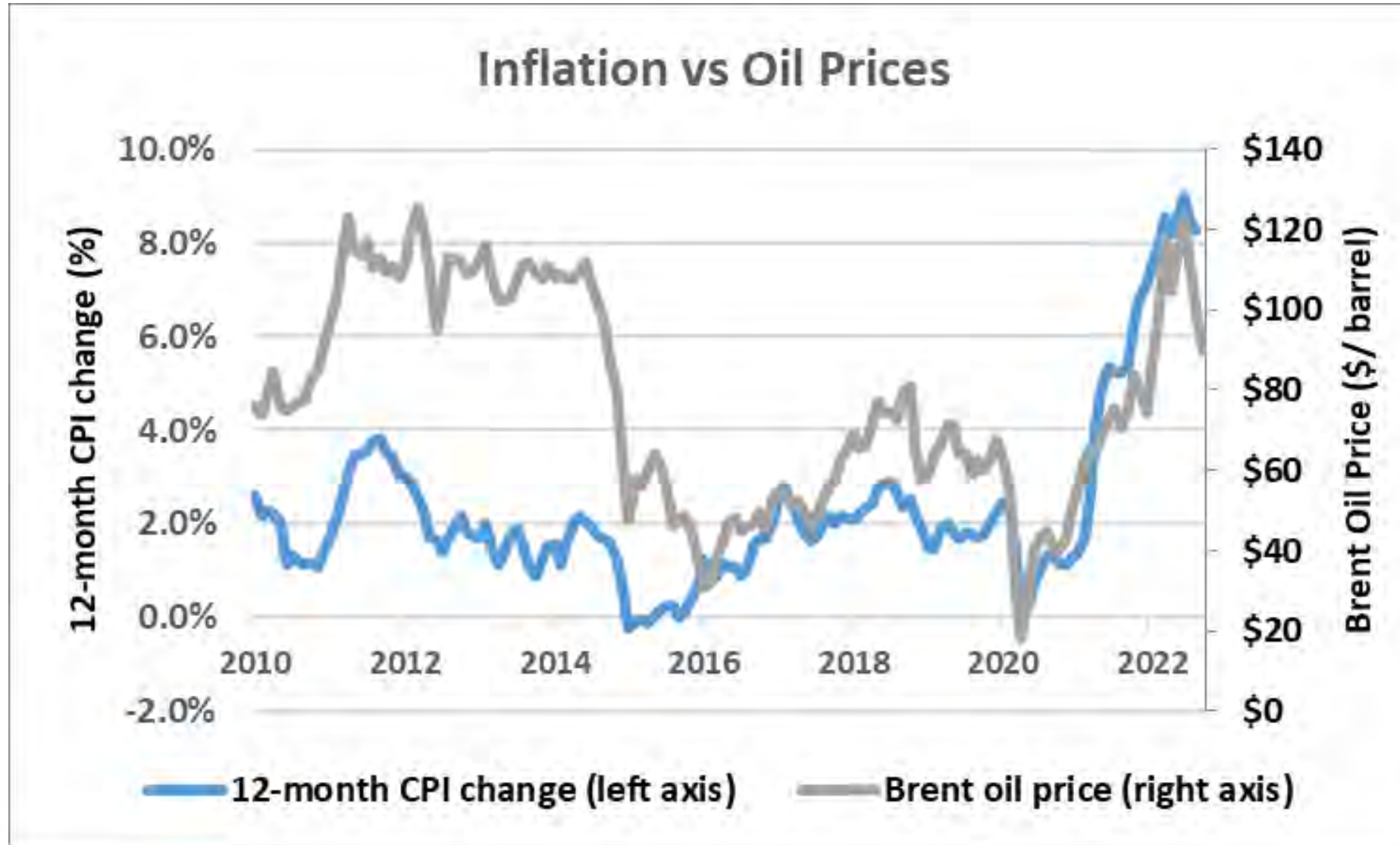
- Unique asset for Alaska
- Funded based on 25-50% of minerals royalties
- Invested in a broad mix of stock, bonds, etc.
- Payout of 5% of trailing five-year average fund value
  - Growth should match or exceed inflation over time, even after payout
- \$74 billion fund value as of August 31, 2022
  - That's about \$100,000 for every resident
- Contributed \$3.4 billion to state budget in FY 2023
  - \$2.1 billion used to send \$3,284 Permanent Fund Dividends (PFDs) to every eligible resident in September/October 2022
  - Remaining \$1.3 billion to fund government operations





# Inflation and State Revenues

## State Revenue Impacts: Oil and Gas



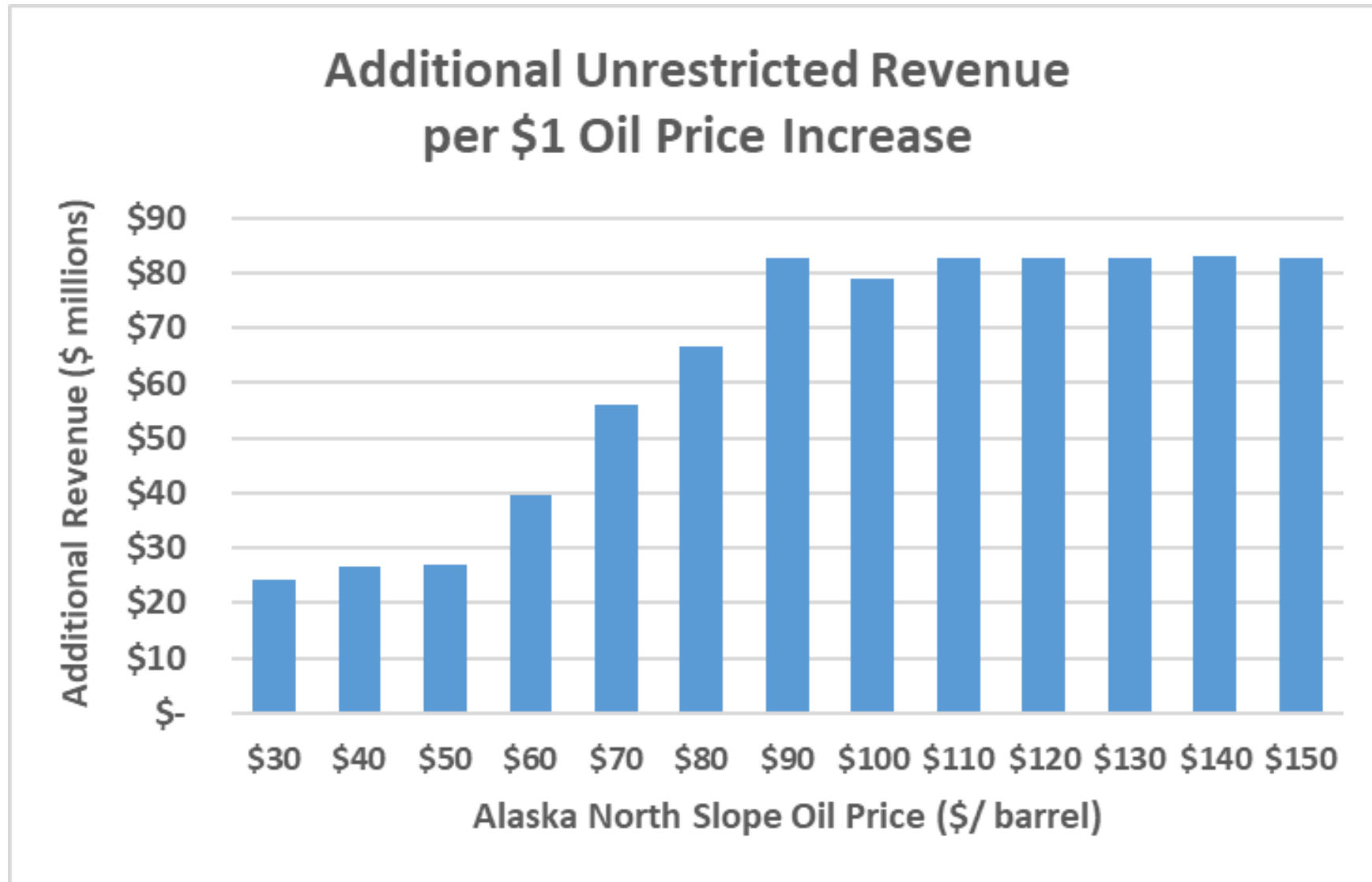
## State Revenue Impacts: Oil and Gas

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- Four sources of oil and gas revenue:
  1. Property tax – based on fixed percent of value.
  2. Royalties – based on fixed percent of value.
  3. Corporate income tax – based on progressive percent of profit.
  4. Production tax – based on progressive percent of profit.
    - 4% Gross tax floor
    - 35% Net profits tax less per-taxable-barrel credits
    - Tax credits reduce from \$8 to zero at wellhead values from \$80-150 (~ oil prices from \$90-160)
    - State's effective tax rate increases as prices increase

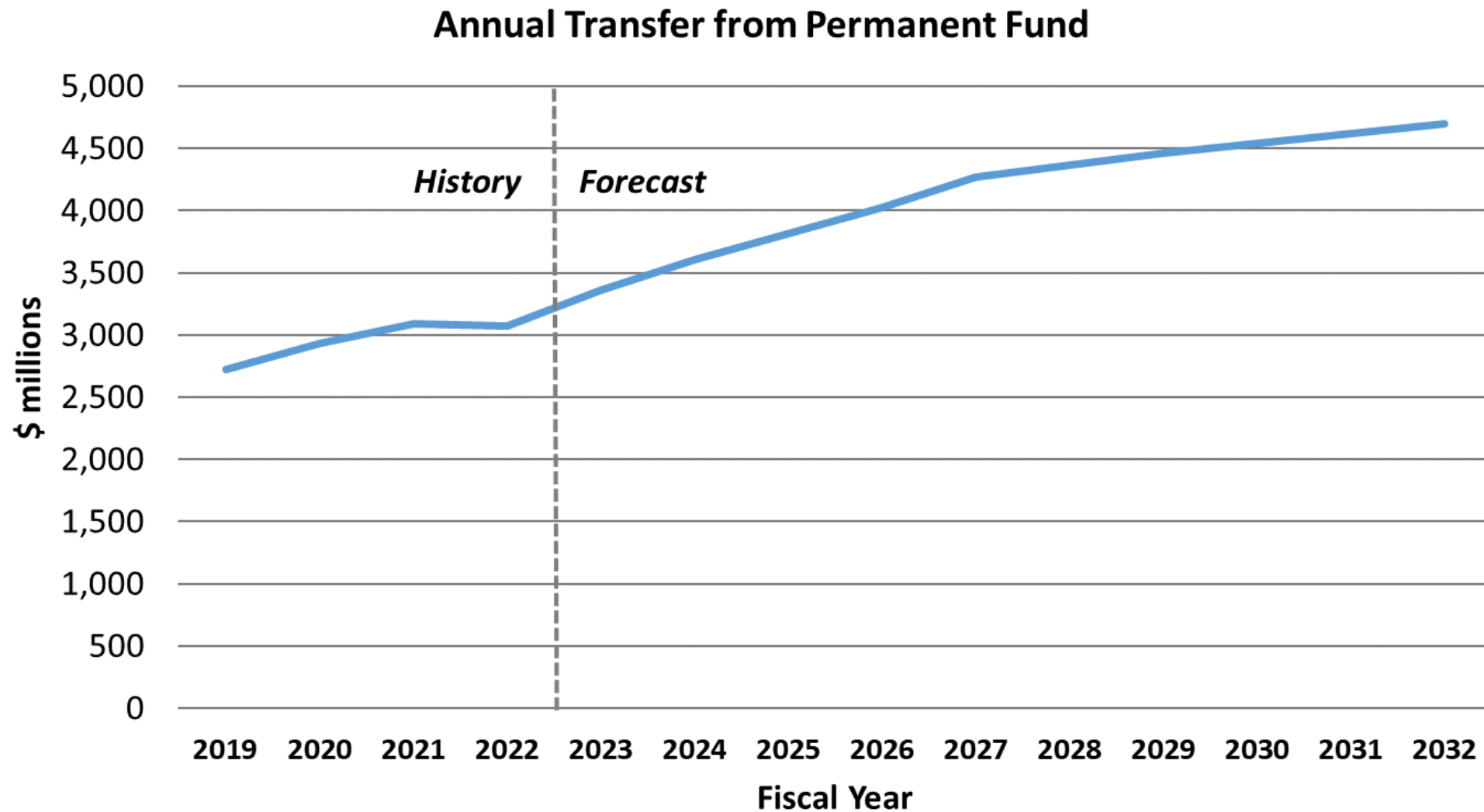


## State Revenue Impacts: Oil and Gas





## State Revenue Impacts: Investments: Permanent Fund transfer increases over time



## State Revenue Impacts: Federal and Other Sources

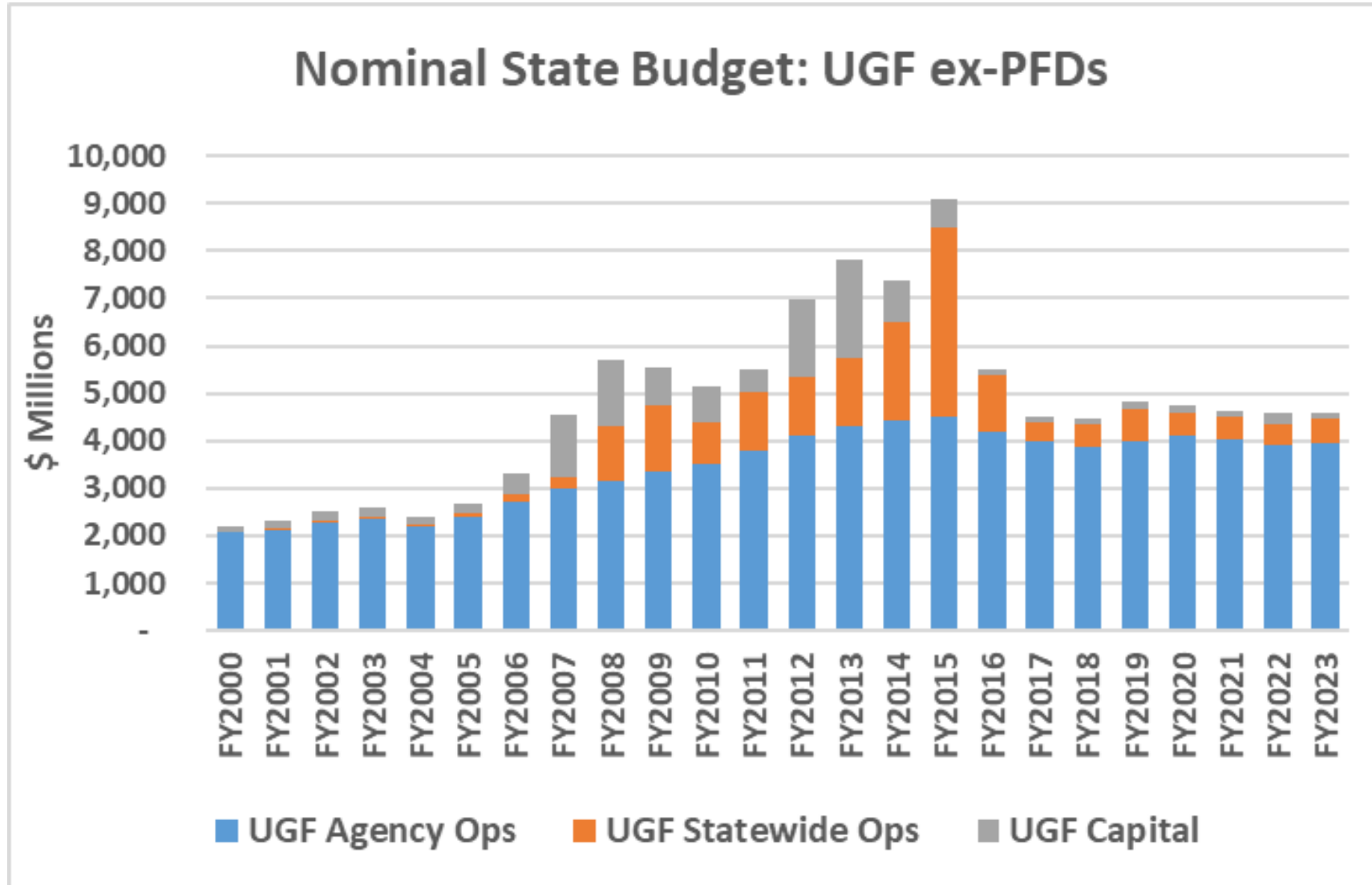
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1. Federal Revenues will depend on federal policy
  - Strong federal revenues in coming years with IIJA
  - Eventually, federal government will have to restrain spending... right?
2. Other Revenues
  - Revenues based on share of value or profit will be resilient to inflation
    - Corporate income tax, mining tax, some excise taxes (tobacco products, vehicle rental)
  - Revenues based on a per-unit assessment will decline in real value
    - Most excise taxes (motor fuel, alcohol, cigarette, etc.) and some charges for state services



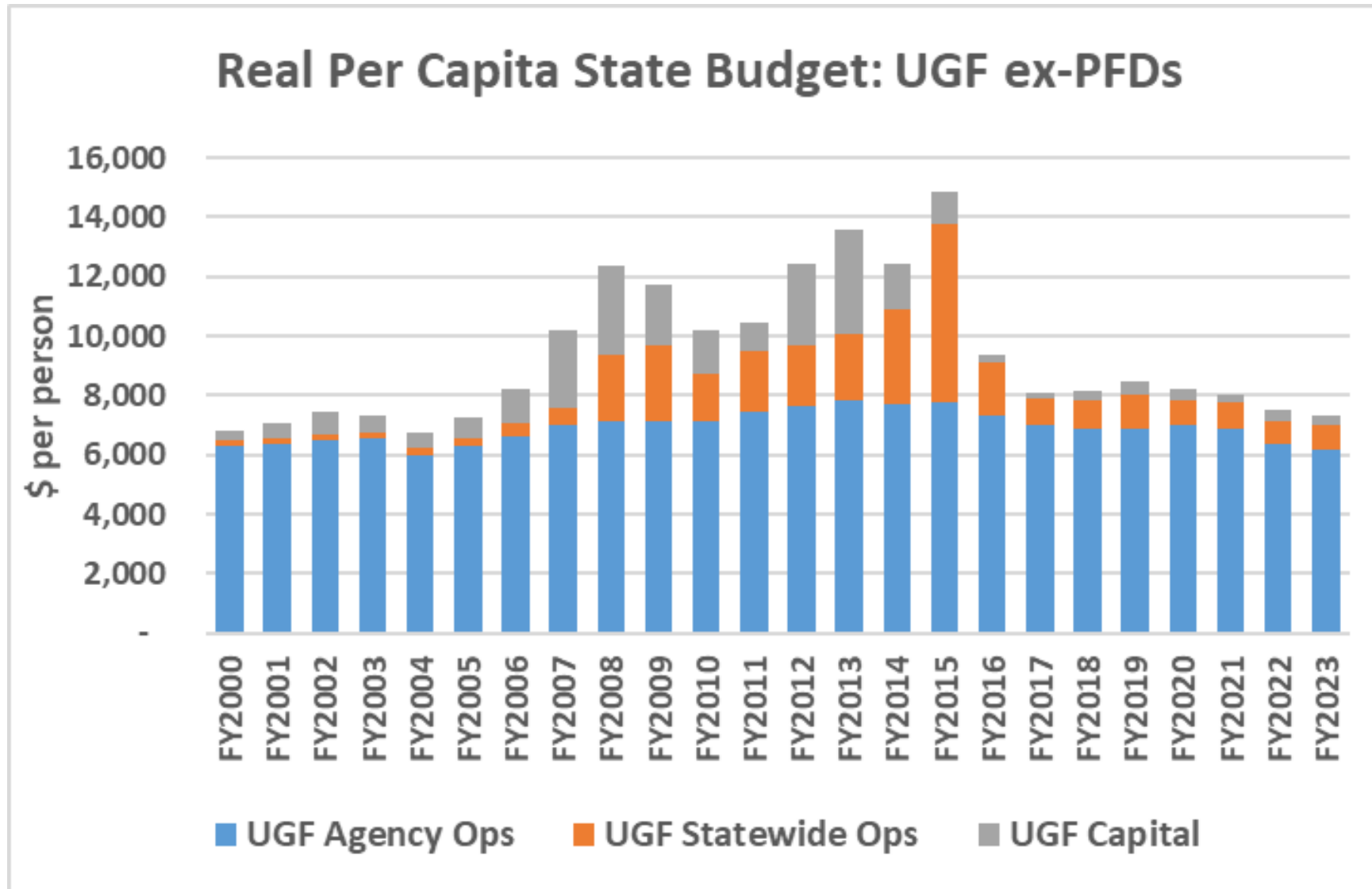
# Inflation and State Budgets

## Budget: Historical UGF Budgets (Not Including PFDs)





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## Budget Impacts: Forward Looking

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1. FY 2023 10-Year plan assumes inflation can be contained:
  - Capital budget flat funding
  - Agency operating budgets flat funding in FY 2024
    - 1.0% Medicaid growth FY 2025+
    - 1.5% FY 2025+ growth for education, all other agency operations
2. Inflationary pressures in multiple areas of the budget:
  - Local government support
  - Education formula
  - Employee wages & benefits
  - Etc.
3. Inflation adds pressure for continued higher PFDs



# REMI Modeling

## REMI Modeling of Inflation Impacts

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- Scenarios looking at U.S. inflation 1-3% over baseline over a decade.
- Higher inflation has an overall negative impact on state economy
  - Higher oil prices do benefit the state and industry, but...
  - More than offset by reductions to overall economic growth and economic activity
- Construction, Manufacturing, Recreation, and “Private Households” are the most impacted sectors
- Government, pipeline transportation, and fishing are least impacted sectors





# Conclusions



## Takeaways

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### How does a higher inflation environment impact Alaska?

1. State government will be okay
  - State spending will face upward pressure, but...
  - Most revenue sources will automatically grow with inflation
  - For specific taxes, impact depends on whether tax is per-unit or percent of value
2. Resource extraction industries should be okay
  - Resource prices (oil, minerals, fish, etc.) tend to move with inflation
  - Partially offset by higher taxes in real terms for oil industry
3. The rest of the economy faces bigger questions
  - Restrained state spending shifts burden to local governments, which may find it harder to absorb inflation
  - Biggest impacts on households, consumer, and tourism-related industries



# THANK YOU

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