Treasury Windfalls Boost Revenues

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The Pennsylvania Treasurer generally invests all Commonwealth funds not required to meet current operational needs. For purposes of the General Fund, this excess balance is invested in fixed income securities, primarily of a short duration, with a goal of generating a competitive return while preserving capital (e.g., money market funds). (See the Pennsylvania Treasury website for more information.) Treasury earnings are posted monthly as General Fund revenue and those amounts have increased dramatically over the past 15 months. This research brief examines the cause of the historically high collections and explains why the windfall is not expected to continue over the long-term.

Treasury collections totaled $452 million in fiscal year (FY) 2022-23, up dramatically from the $23 million collected in FY 2021-22. The table below displays the General Fund average daily balance, the Federal Funds Target Rate, Treasury collections and the effective interest rate (actual collections divided by the average daily balance) for FY 2014-15 through FY 2023-24. The data illustrate that the higher earnings are due to the combination of two factors: (1) unprecedented General Fund balances and (2) historically high interest rates.

High Interest Rates Drive Treasury Collections

Fiscal Year	GF Avg. Daily Bal.	Fed Funds Target Rate	Treasury Collect.	Effective Rate
2014-15	$1,908	0.0%	$8	0.4%
2015-16	2,970	0.1	14	0.5
2016-17	1,552	0.5	20	1.3
2017-18	1,367	1.2	31	2.3
2018-19	1,606	2.1	72	4.5
2019-20	1,394	1.2	30	2.1
2020-21	3,343	0.0	9	0.3
2021-22	11,175	0.2	23	0.2
2022-23	13,372	3.7	452	3.4
2023-24	*12,500*	*5.2*	*650*	*5.2*

Note: Dollars in millions. Daily General Fund balance from Pennsylvania Treasury website. Average computed by the IFO. Lower limit for the Federal Funds Target Rate is shown. Effective Rate is equal to actual collections divided by the General Fund Average Daily Balance. FY 2023-24 is estimated.

Prior to FY 2020-21, the typical General Fund average daily balance was roughly $1.8 billion. For FY 2020-21, that balance more than doubled to $3.3 billion and then surged to $11.2 billion in FY 2021-22 due to federal COVID relief funds and extraordinarily strong revenue growth. Even with the much higher balance, Treasury collections were muted due to the very low interest rates in effect. By early 2022, the Federal Reserve Board began to rapidly increase the Federal Funds Target Rate, causing the effective rate earned on General Fund deposits to rise from 0.2% (FY 2021-22) to 5.2% (FY 2023-24 projected).

The combination of high balances and interest rates should continue this fiscal year, but not over the longer term. Based on the latest published General Fund balance sheet for FY 2023-24, the ending balance is expected to decline $1.4 billion by June 2024, and most economic forecasts project that interest rates will begin to fall gradually in mid-to-late 2024. If both projections hold, then Treasury collections for this fiscal year could reach $650 million. Through September 2023 (first three months of fiscal year), Treasury collections total $201 million (preliminary). Going forward, each $1 billion decline in the fund balance (at current rates) results in a $50 million revenue reduction while each 1% drop in interest rates (at current balances) results in a $150 million reduction.