PENNSYLVANIA FISCAL OUTLOOK

FY 2026-27 TO FY 2031-32

November 2026

Independent Fiscal Office

Independent Fiscal Office
Rachel Carson State Office Building
400 Market Street
Harrisburg, PA 17105



Staff Contributors
Matthew Knittel, Director
Stacey Knavel, Deputy Director
Jesse Bushman
Robyn Toth
Rachel Flaugh
Mathieu Taylor
Frank Lill
Andrea Lin
Nolan Ciesielka

INDEPENDENT FISCAL OFFICE

November 12, 2026

The Honorable Members of the Pennsylvania General Assembly:

The Independent Fiscal Office (IFO) publishes this report to fulfill duties specified in Section 604-B of the Administrative Code of 1929. They are as follows:

- Section 604-B (a)(2): the IFO shall "provide an assessment of the state's current fiscal condition and a projection of what the fiscal condition will be during the next five years. The assessment shall take into account the state of the economy, demographics, revenues and expenditures."
- Section 604-B (b)(2): the IFO may "provide an analysis of the executive budget, including budgetary projections, economic outlook and economic impact. The budget analysis may include performance recommendations to secure greater efficiency and economy."

The Executive Budget for the upcoming fiscal year is typically released in early February, and the state Constitution requires that the document include (1) a balanced operating budget for the ensuing fiscal year setting forth in detail proposed expenditures and estimated revenues from all sources (including proposed new revenues if required to bring the budget into balance) and (2) a financial plan for the next succeeding five fiscal years.

This report provides an assessment of the state's fiscal condition for the next five years and includes recommendations for projections included in the Executive Budget to secure greater efficiency and economy. The report provides specific commentary and recommendations for the upcoming fiscal year, but more general discussion and recommendations for the succeeding four fiscal years.

Questions and feedback on this report can be submitted to contact@ifo.state.pa.us.

Sincerely,

Matthew J. Knittel
Director

Rachel Carson State Office Building, 400 Market Street, Harrisburg PA 17105
www.ifo.state.pa.us | (717) 230-8293 | contact@ifo.state.pa.us

Executive Summary

This report projects General Fund revenues and expenditures to assess the Commonwealth's fiscal condition through FY 2031-32.[1] The projections are best viewed as potential outcomes if economic growth reverts to long-term trends and current policies and demographic trends continue. This simulation approach (1) provides policymakers with a neutral baseline to assess long-term fiscal sustainability and (2) ensures consistency across publication years because economic growth rates revert to long-term trends that reflect structural factors which change slowly over time (e.g., size of the state labor force). Because it does not assume an economic downturn, these long-term projections could be viewed as an optimistic outcome under current laws and policies.

This report designates FY 2026-27 as the base year. All revenue and expenditure projections use that year as a reference year and generally assume that the policy choices embedded therein do not change through FY 2031-32. The forecast assumes that expenditures increase at a rate sufficient to maintain the level of real services provided to service populations in the base year (i.e., a current services forecast). Hence, most expenditure projections include an inflationary adjustment to compensate for rising prices and where applicable, a demographic adjustment to account for changing service populations.

For FY 2026-27, the outlook projects a current year deficit of $2.35 billion and a structural deficit of $4.70 billion if temporary measures are reversed. For FY 2027-28, the structural deficit increases to $6.65 billion due to an assumed increase of $400 million in PreK to 12 adequacy funding, the lack of a tariff refund windfall ($230 million), the annualization of Department of Human Services (DHS) rate increases effective during FY 2026-27 ($200 million) and SNAP benefit costs (nine months at $170 million). From FY 2027-28, the deficit expands moderately to $7.37 billion by FY 2031-32 as projected net revenue growth (+2.8% per annum) largely keeps pace with spending growth (+2.7% per annum). Factors that impact long-term growth include the ongoing corporate net income tax rate reduction (revenues) and an inflation extrapolator (2.2%) used for most discretionary spending.

1 A separate publication provides demographic projections used by this report. See: IFO Pennsylvania Demographic Outlook.

General Fund Financial Statement

Fiscal Year	24-25	25-26	26-27	27-28	28-29	29-30	30-31	31-32
Gross Revenues	$46.41	$48.93	$50.81	$50.89	$52.14	$53.50	$54.95	$56.84
Refunds	-2.25	-2.49	-2.50	-2.60	-2.70	-2.80	-2.90	-3.00
Net Revenues	44.16	46.43	48.31	48.29	49.44	50.70	52.05	53.84
Expenditures	-47.82	-49.03	-50.85	-55.28	-56.89	-58.34	-59.81	-61.56
Plus Prior Year Lapses	1.12	0.84	0.19	0.35	0.35	0.35	0.35	0.35
Current Year Deficit	**-2.55**	**-1.76**	**-2.35**	**-6.65**	**-7.10**	**-7.29**	**-7.41**	**-7.37**
Less DHS Cycle Roll	--	1.32	1.32	--	--	--	--	--
Less Temporary Support	0.87	1.47	1.03	--	--	--	--	--
Structural Deficit	**-3.41**	**-4.55**	**-4.70**	**-6.65**	**-7.10**	**-7.29**	**-7.41**	**-7.37**
Year End Balances								
General Fund	$4.16	$2.46	$0.11	$0.00	$0.00	$0.00	$0.00	$0.00
Rainy Day Fund	7.47	7.76	8.11	--	--	--	--	--

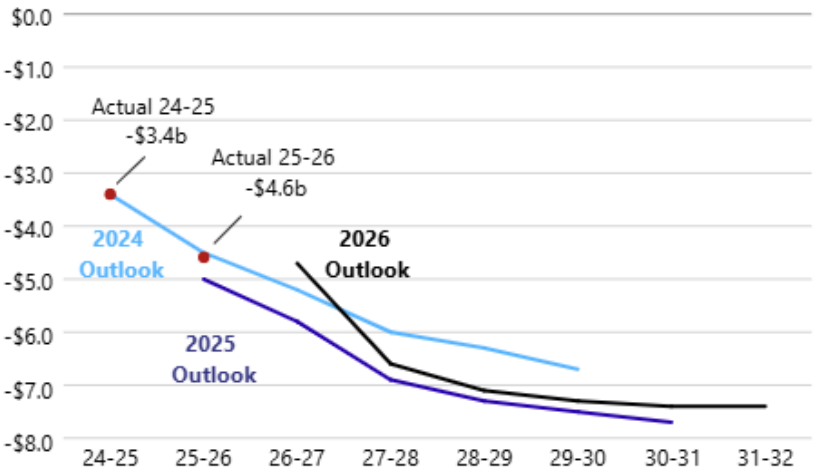
Note: Billions of dollars. FY 26-27 Prior Year Lapses are reduced for net supplemental appropriations ($218 million) anticipated in the Budget Office's Fall Update. Although the FY 26-27 spending shifts to the Motor License and Gaming Funds ($225 million) are included with temporary support for that year, the shifts are also carried forward into future years. In practice, it is unclear if those funds could support the additional spending over the long term.

Overview and Recommendations

Each November, the IFO projects the Commonwealth's fiscal outlook for the upcoming budget year and four subsequent years. Due to the lack of permanent policy changes, the current outlook has not changed materially from the November 2024 and 2025 Outlooks. A comparison shows:

- In November 2024, the IFO projected a structural deficit of $3.4 billion for FY 2024-25, growing to $6.7 billion for FY 2029-30.[2] The current outlook is similar (see graph).

Structural Deficits: Actuals and IFO Forecasts



Note: Billions of dollars.

- The November 2024 Outlook accurately projected the structural deficit for the contemporaneous (2024-25) and subsequent (2025-26) fiscal years. The November 2025 Outlook was off by $0.4 billion for FY 2025-26.
- The projected FY 2026-27 structural deficit ($4.7 billion) has improved from the November 2025 Outlook due to very strong revenue gains from a robust stock market, AI investment and consumer spending. The forecast assumes that $230 million of those revenue gains are a one-time windfall from the taxation of tariff refunds (corporate net income tax).

It is noted that all projections assume that the state and national economies operate at full potential and an economic downturn does not occur. Current data show that the state and national economies have significantly overperformed as demonstrated by these metrics for 2026 (through 2026 Q3):

- Pennsylvania unemployment rate: 4.0%, which is 0.5% to 1.0% lower than historical rates;
- U.S. domestic corporate profits: +19% compared to prior year;
- S&P 500 Index: +20% (through October); and
- U.S. Business Investment: Computers and Peripheral Equipment (includes AI): +70%.

While an economic downturn may not occur during the next five years, economic momentum must decelerate from its current pace because much is driven by substantial AI investment, which cannot be sustained. Moreover, long-term interest rates have risen appreciably during the past year, and U.S. policymakers will need to enact fiscal policies (spending cuts and/or tax increases) to address the rapidly expanding federal debt. While the forecast assumes a moderate deceleration to "normal" rates of growth, any deceleration could be stronger and occur rapidly. Current economic growth is primarily driven by a single sector, and

2 A structural deficit is the shortfall after temporary or one-time measures have been reversed, such as fund transfers and cycle rolls. For future years, it assumes that the economy operates under normal rates of growth.

some industry analysts believe that much AI investment is speculative and interdependent (e.g., use of circular financing methods). If that assessment is accurate, then the sector could be vulnerable to a rapid slowdown or outright contraction if one or two larger firms falter.

Given the magnitude of recent deficits that are projected to expand over the budget window, this outlook makes three recommendations for long-term projections included in the Executive Budget.[3] The first two recommendations reflect established best-budgeting practices used by federal and many state governments (and this outlook), while the third recommendation is prospective and facilitates discussion over viable alternatives that could be used to address long-term structural deficits.

1 Maintain the Rainy Day Fund for Unanticipated Emergencies

The Executive Budget makes revenue and spending projections for the upcoming budget year and four subsequent years (long-term). The Pew Chartitable Trusts and the National Conference of State Legislatures (NCSL) recognize long-term budgeting as a best practice to identify structural imbalances and allow policymakers sufficient time to implement effective policies to generate revenues and/or reduce spending.[4]

However, for recent budgets, Pennsylvania was the only state to propose using its entire Budget Stabilization Reserve Fund (i.e., Rainy Day Fund or RDF) to bring the long-term budget into balance (see **Table 1**).[5] Under current law, the RDF is reserved for (1) emergencies involving the health, safety or welfare of Commonwealth residents or (2) downturns in the economy that result in significant unanticipated revenue shortfalls, assuming that neither outcome can be addressed through the normal budget process.[6] The outlook recommends that, similar to other states, the Executive Budget follow best practices of fiscal sustainability and limit RDF withdrawals to partly assist in closing the shortfall for the upcoming budget year only.

A recent article by The Pew Chartitable Trusts cautions against using RDFs to address structural deficits:

> But state leaders should be cautious about relying on rainy day funds to close deficits, because many states' reported budget gaps stem from structural imbalances—when recurring revenue is insufficient to support recurring expenditures—rather than from short-term shocks. Although reserves exist to provide relief during times of fiscal stress, they are not a sustainable solution for persistent budget shortfalls.[7]

The last two enacted budgets employed significant temporary measures to bring the budget into balance. Going forward, permanent policy changes are likely required because it will not be possible to "grow out of" structural imbalances due to: (1) a state economy that is already operating above capacity (September 2026 unemployment rate of 3.9%), (2) demographic growth that will be modest or flat and (3) on-going spending pressures related to a rapidly aging population and reduced federal support.

---

3 From Section 604-B (b)(2) of the Administrative Code: the IFO may "provide an analysis of the executive budget, including budgetary projections, economic outlook and economic impact. The budget analysis may include performance recommendations to secure greater efficiency and economy."

4 For 2026, 19 states made long-term budget projections. See: The Pew Chartitable Trusts Tools for Sustainable State Budgeting and state database.

5 For FY 2026-27, some states used a portion of their RDF to bring the budget year into balance (e.g., Maryland, Nebraska, Washington).

6 See: 72. P.S. § 1703-A.

7 See: The Pew Chartitable Trusts Strength of State Rainy Day Funds Declines.

Table 1
Rainy Day Fund Usage in Prior Budgets

Budget Release	Forecast Year 24-25	25-26	26-27	27-28	28-29	29-30	30-31	Total
Feb 2024	-$0.4	$0.0	$3.0	$2.7	$2.2	--	--	$7.5
Feb 2025	-$0.3	$1.6	$2.4	$1.9	$1.2	$0.7	--	$7.4
Feb 2026	--	--	$4.6	$2.2	$1.1	$0.0	-$0.2	$7.7

Note: Billions of dollars. A negative amount indicates that the RDF received a net transfer.
Source: Executive Budget, various years.

2 Use a Current Services Approach for Mandatory Spending

The outlook recommends that the Executive Budget use a current services approach to make long-term spending forecasts for mandatory spending such as Department of Human Services (DHS) programs. The current services approach is used by many states and the U.S. Congressional Budget Office (CBO) to make baseline spending projections.[8] As noted by The Pew Charitable Trusts, under a current services approach:

> (s)tates estimate what they would need to spend to keep a program at a consistent level…A key reason to use the current services approach is that a budget that is flat in nominal terms doesn't guarantee that the state will be able to maintain a consistent level of services because costs could rise (or shrink) from factors such as inflation, population growth, or demographic changes. Current service estimates account for these factors to generate realistic spending forecasts.[9]

For FY 2026-27, DHS is the largest state agency and comprises 41% (adds back cycle roll) of total state General Fund spending. Moreover, most DHS spending is mandatory: if a resident qualifies for a program, then the state must provide services. Recent Executive Budgets have assumed long-term growth rates of 1.0% to 1.5% per annum, while actual growth rates have ranged from 5.9% to 12.8% (see **Table 2**). Given its size, the DHS spending forecast will be a primary driver of any permanent changes needed to address projected shortfalls. If policymakers must enact permanent, broad-based revenue or spending changes, they require a realistic assessment of future budget challenges to do that effectively. Therefore, forecasts should reflect recent historical rates for healthcare inflation and the demographic impact from an aging population.[10]

8 See: CBO Explains How It Develops the Budget Baseline, which notes that CBO uses inflationary adjustments and demographic forecasts for projections of mandatory and discretionary spending.

9 See: The Pew Chartitable Trusts These Fiscal Principles Can Help State Leaders Make Better Long-Term Decisions.

10 See: IFO Pennsylvania Demographic Outlook.

Table 2
DHS Projected and Actual Growth Rates

Budget Release	Fiscal Year						
	23-24	24-25	25-26	26-27	27-28	28-29	29-30
Feb 2023	16.5%	3.4%	3.1%	2.3%	2.5%	--	--
Feb 2024	13.3%	6.3%	3.8%	2.5%	2.4%	2.4%	--
Feb 2025	12.8%	6.4%	10.2%	1.7%	1.5%	1.5%	1.5%
Feb 2026	12.8%	5.9%	7.7%	6.6%	1.1%	0.9%	0.8%

Note: Budget Year is blue. Long-term projections are peach. Actual growth rates as of budget release are unshaded.

3 Provide Alternatives to Speculative Revenue Estimates Used to Close Deficits

In addition to using RDF balances, prior Executive Budgets have proposed new revenue sources to close long-term budget gaps. Recent proposals include (1) the regulation and taxation of skill games ($2.0 billion per annum once fully phased-in), (2) combined reporting for corporations ($1.1 billion) and (3) fees for legalization of recreational marijuana ($660 million).

While the Governor may propose new revenue sources as part of the Executive Budget's long-term financial plan, estimates for some proposals are subject to a high degree of variance and uncertainty. Factors that contribute to estimate uncertainty include:

- Estimates are typically based on limited or incomplete data (skill games), use outcomes from other states (recreational marijuana) or have tax bases that remain to be determined (combined reporting).
- Estimates assume that proposals can be enacted, implemented and enforced rapidly. However, many factors would likely delay implementation such as the development of regulations, the buildout of administrative and enforcement infrastructure and various legal challenges (e.g., how a unitary group is defined under combined reporting).
- The behavioral response of workers, consumers, taxpayers and firms is not known. For example, the expansion of the Local Option Small Games of Chance Act to include tavern games (Act 90 of 2013) was projected to generate $156 million per annum for the General Fund. For FY 2025-26, collections totaled $1.1 million.

Through FY 2026-27, most viable temporary measures (e.g., residual Covid funds, transfers from other funds, DHS cycle rolls) have been utilized to offset current and prior year deficits. Hence, limited options remain available to balance the budget in the short term if newly-enacted revenues fall significantly short of estimates. If the RDF is not used (or partially used) for the upcoming budget year, permanent revenues will be needed immediately to close budget gaps because the General Fund surplus has been depleted.

Therefore, the outlook recommends that the Executive Budget also include an estimate of the personal income and/or sales tax rate increase necessary to close current and future deficits if new revenue proposals fail to generate projected revenues or are not enacted. Those two revenue sources comprise 75% of total General Fund collections, and rates can be adjusted to generate required funds quickly. A proposed fall back or default option is also appropriate given the magnitude of current structural deficits. The final section of this outlook includes a simulation for a 0.5 percentage point personal income (PIT) and sales and use tax (SUT) rate increase to illustrate the (known) revenue potential from those current taxes and the tax incidence (i.e., the income group effectively paying the new tax). This outlook makes no assumptions regarding methods that will be used to close projected shortfalls. Hence, it also does not include the negative economic and revenue impact that would result from the higher taxes (or spending cuts) necessary to address shortfalls.

Revenues and Expenditures

The baseline economic forecast used for this outlook assumes that (1) the Pennsylvania economy maintains an unemployment rate that ranges from 4.0% to 5.0% (i.e., full employment), (2) the Federal Reserve largely achieves its long-term inflation target, (3) resident workers receive a moderate real pay increase that exceeds inflation and (4) a recession does not occur during the next five years.

The long-term forecast assumes a reversion to 1.8% real GDP growth, 4.0% wage growth, a regional inflation rate of 2.2% per annum and incorporates the projected change in the resident population for various age cohorts from the IFO Demographic Outlook. (See **Table 3**.) Notable economic and demographic trends and assumptions include:

- Regional inflation accelerated in 2026 largely due to energy prices (gasoline and electricity). The forecast assumes that gasoline prices fall and consumer prices increase by 2.2% per annum (similar to prior outlooks) after 2027.
- The forecast does not assume a recession, but it does include a moderate reversion largely due to (1) a slowdown (2027) and modest contraction (2028 and 2029) in investment related to AI, and (2) a flat stock market for 2027 after three consecutive years of double-digit gains.
- The working-age population continues its long-term contraction. The forecast assumes that labor force participation rates increase to facilitate payroll jobs growth of 0.6% per annum (35,000 payroll jobs).
- The age 80+ cohort surges as the oldest Baby Boomers turn 80 in 2027. The impact of that trend is reflected in the forecast for Long-Term Living expenditures.
- Although the school-age population contracts by 0.8% per annum, the forecast assumes PreK to 12 expenditures grow with inflation (plus a +$400 million adequacy funding boost in the budget year only). Therefore, real per capita spending increases by roughly 0.8% per annum.

Table 3
Pennsylvania Economic and Demographic Forecasts

	Growth Rate						
Economics	**2025**	**2026**	**2027**	**2028**	**2029**	**2030**	**2031**
Real GDP	1.8%	1.8%	1.8%	1.8%	1.8%	1.8%	1.8%
Wages and Salaries	4.2%	4.1%	4.0%	4.0%	4.0%	4.0%	4.0%
Philadelphia CPI-U	3.2%	4.2%	3.0%	2.2%	2.2%	2.2%	2.2%
Cash Income	5.5%	4.6%	3.8%	4.0%	4.0%	4.0%	3.9%

	Annual Change (000s)						
Demographics	**2025**	**2026**	**2027**	**2028**	**2029**	**2030**	**2031**
Age 0-19	-22	-22	-21	-26	-23	-22	-22
Age 20-64	-28	-31	-21	-19	-21	-18	-11
Age 65-79	51	44	5	10	10	4	-10
Age 80+	13	11	42	32	28	27	29
Total	**14**	**2**	**6**	**-4**	**-6**	**-9**	**-14**

Source: U.S. Bureau of Economic Analysis, U.S. Bureau of Labor Statistics. U.S. Census Bureau. Forecasts by IFO.

Revenue Forecast

Fiscal year-to-date General Fund tax collections (excludes non-tax revenues) through October grew by 9.4% compared to the prior year, a much stronger rate than historical averages. The strength is attributable to significant AI investment, stock market wealth gains, surging corporate profits, a one-time tariff refund windfall and robust consumer spending. From FY 2026-27 to FY 2031-32, revenues are projected to increase by 2.3% per annum. Notable factors that affect the revenue forecast include:

- Sales and use tax revenue growth decelerates from the current year due to (1) a moderation of wealth effects and (2) a contraction in taxable business investment spending. The forecast assumes the stock market will be flat in 2027, followed by average growth of 5% per annum during the forecast period.
- Following an estimated 19% increase in domestic non-financial corporate profits through the first three quarters of 2026, the forecast assumes flat profits in 2027, followed by 4% per annum growth for the remainder of the forecast. Corporate net income tax (CNIT) collections contract due to the ongoing rate reduction, which falls from 7.49% (tax year 2026) to 4.99% (2031).
- Personal income tax revenues assume wage and (base) withholding growth of 4% per annum and modest capital gains income growth (2%) for 2027. For FY 2027-28, the withholding growth rate is low (2.8%) because the prior year had an extra deposit day (+$175 million). The forecasts for small business profits, capital gains and dividends assume that recent strong gains are permanent and those forecasts all expand at long-term rates of 4% to 5% per annum.
- The gross receipts tax forecast reflects the significant increase in electricity prices for 2026 (+15%), which is assumed permanent and does not reverse in future years.
- Other miscellaneous collections (non-tax) are unusually high in FY 2026-27 due to $580 million in one-time special funds transfers authorized under Act 21-2026.

Table 4
General Fund Revenues

	Amount ($ billions)						
	25-26	26-27	27-28	28-29	29-30	30-31	31-32
Personal Income	$20.04	$21.08	$21.74	$22.59	$23.49	$24.43	$25.62
Sales and Use	15.49	16.11	16.53	16.88	17.27	17.71	18.20
Corporate Income	4.97	5.18	4.80	4.57	4.37	4.16	4.07
Inheritance	1.85	2.01	1.98	2.05	2.14	2.23	2.35
Gross Receipts	1.38	1.57	1.63	1.71	1.81	1.90	2.01
All Other	5.18	4.86	4.21	4.34	4.42	4.51	4.59
Total Revenue	**48.93**	**50.81**	**50.89**	**52.14**	**53.50**	**54.95**	**56.84**

	Growth Rate						
	25-26	26-27	27-28	28-29	29-30	30-31	31-32
Personal Income	5.7%	5.2%	3.1%	3.9%	4.0%	4.0%	4.9%
Sales and Use	5.4	4.0	2.6	2.1	2.3	2.6	2.8
Corporate Income	-3.8	4.1	-7.2	-4.8	-4.3	-4.8	-2.4
Inheritance	6.6	8.7	-1.5	3.4	4.5	4.1	5.6
Gross Receipts	4.7	13.5	3.7	5.3	5.4	5.4	5.4
All Other	14.3	-6.2	-13.4	3.1	1.8	2.0	1.8
Total Revenue	5.4	3.8	0.2	2.5	2.6	2.7	3.4

Note: Billions of dollars.

Expenditure Forecast

The expenditure outlook assumes moderate growth in General Fund spending over the forecast period. Assumptions that motivate the outlook include:

- The forecast reflects mandatory increases attributable to (1) pension, healthcare and debt service obligations and (2) various entitlement programs within DHS. At the expiration of current state employee wage contracts (June 2027), the forecast assumes wages increase 3.5% for FY 2027-28 and 3.0% per annum thereafter. Net wage gains (generally 2.0% to 2.5% per annum) incorporate agency-specific employee turnover factors (-0.5% to -1.0% per annum).
- Spending on PreK to 12 education trends with inflation. Consistent with recently enacted budgets, the outlook also includes a one-time increase of $400 million for FY 2027-28 (adequacy funds). To the extent policymakers continue to provide annual boosts to reduce funding disparities, the expenditure forecast and structural deficit will be understated.
- All other discretionary spending is grown by inflation (2.2%), except for higher education, which is held flat.

- The outlook assumes that two recent DHS cycle rolls (i.e., one-month payment delay, $1.3 billion each) used to balance the FY 2025-26 and FY 2026-27 budgets are not reversed and the FY 2026-27 cycle roll must be backfilled (i.e., a return to 12 monthly payments) in FY 2027-28.
- The forecast assumes that the state SNAP payment error rate (9.2% for 2025) initially falls within the 6% to 8% range. Under new federal requirements, this results in the payment of 5% of state benefit costs (roughly $230 million per annum) effective October 1, 2027. For later periods it is assumed that the error rate falls below 6%, and additional benefit costs are not incurred effective October 1, 2029.
- Current Motor License Fund support for the Pennsylvania State Police ($375 million for FY 2026-27) remains at that level over the forecast period.
- The outlook assumes that additional one-time measures to temporarily reduce spending are not employed (e.g., additional payment delays, one-time funding shifts).

Table 5 displays projected expenditure levels and growth rates for the largest General Fund spending categories. For FY 2026-27, expenditures increase by 3.7%, largely due to strong growth in the PreK to 12 and DHS categories. For FY 2027-28, expenditures are projected to increase 8.7% due to the lack of a DHS cycle roll and the $400 million bump for adequacy funding within the Pennsylvania Department of Education (PDE), before decelerating to a rate of 2.7% per annum for the remainder of the forecast period.

Table 5
General Fund Expenditures

	Amount ($ billions)						
	25-26	26-27	27-28	28-29	29-30	30-31	31-32
DHS	$18.07	$19.06	$22.00	$22.87	$23.57	$24.38	$25.29
PDE - PreK to 12	17.97	18.89	19.81	20.25	20.68	21.12	21.56
All State Personnel	6.07	6.05	6.46	6.61	6.72	6.83	6.98
Debt Service	1.31	1.42	1.45	1.51	1.63	1.65	1.81
All Other	5.59	5.43	5.56	5.65	5.74	5.83	5.92
Total	**49.03**	**50.85**	**55.28**	**56.89**	**58.34**	**59.81**	**61.56**

	Growth Rate						
	25-26	26-27	27-28	28-29	29-30	30-31	31-32
DHS	-1.4%	5.5%	15.4%	4.0%	3.1%	3.4%	3.7%
PDE - PreK to 12	5.1	5.1	4.9	2.2	2.1	2.1	2.1
All State Personnel	4.5	-0.4	6.8	2.3	1.7	1.6	2.1
Debt Service	19.3	8.2	1.9	4.3	8.0	1.2	9.9
All Other	2.2	-2.9	2.4	1.6	1.6	1.6	1.6
Total	**2.5**	**3.7**	**8.7**	**2.9**	**2.5**	**2.5**	**2.9**

Note: Billions of dollars. Amounts and growth rates for DHS, PDE and All Other exclude state personnel costs.

Fiscal Outlook

This section combines revenue and expenditure projections to derive the resultant structural surplus or deficit and projects the General Fund and Rainy Day Fund ending balances (see **Table 6**). Temporary measures that reduced the FY 2025-26 deficit include one-time transfers from special funds ($670 million), the first DHS cycle roll ($1.32 billion) and other temporary support ($410 million, largely the use of Pennsylvania Professional Liability Joint Underwriting Association (JUA) funds to support DHS spending). For FY 2026-27, temporary measures that reduce the current year deficit include a second DHS cycle roll ($1.32 billion), a second round of transfers from special funds ($580 million) and the shift of certain spending to non-General Fund sources ($290 million). The outlook assumes that the FY 2026-27 shifts to the Motor License Fund ($125 million) and the Gaming Fund ($100 million) continue over the forecast period.

From FY 2026-27 (base year) to FY 2031-32, average expenditure growth (+3.4% per annum, adds back DHS cycle roll in base year) outpaces average revenue growth (+2.5%, removes temporary transfers in base year). Notable factors that motivate those trends include:

- The structural deficit grows from $4.7 billion in FY 2026-27 to $6.7 billion in FY 2027-28 due to the annualization of DHS rate increases effective during FY 2026-27 ($200 million), SNAP benefit costs ($170 million, nine months), the lack of a CNIT tariff boost ($230 million) and additional adequacy funding ($400 million).
- CNIT collections contract due to the ongoing rate reduction, which falls from 7.49% for 2026 to 4.99% by 2031.
- The forecast assumes a flat stock market in 2027 and modest contraction in AI investment (i.e., computers and peripheral equipment) in 2028 and 2029. These assumptions (1) restrain taxable consumer spending and SUT collections and (2) imply modest growth in capital gains income in 2027.
- DHS expenditures grow at an average rate of 4.4% per annum from FY 2026-27 to FY 2031-32 (adds back the $1.32 billion cycle roll in FY 2026-27), driven by (1) the increase in the number of residents age 65 or older and (2) a healthcare inflation factor.

Table 6
General Fund Financial Statement

Fiscal Year	24-25	25-26	26-27	27-28	28-29	29-30	30-31	31-32
Gross Revenues	$46.41	$48.93	$50.81	$50.89	$52.14	$53.50	$54.95	$56.84
Refunds	-2.25	-2.49	-2.50	-2.60	-2.70	-2.80	-2.90	-3.00
Net Revenues	44.16	46.43	48.31	48.29	49.44	50.70	52.05	53.84
Expenditures	-47.82	-49.03	-50.85	-55.28	-56.89	-58.34	-59.81	-61.56
Plus Prior Year Lapses	1.12	0.84	0.19	0.35	0.35	0.35	0.35	0.35
Current Year Deficit	**-2.55**	**-1.76**	**-2.35**	**-6.65**	**-7.10**	**-7.29**	**-7.41**	**-7.37**
Less Temp Support	0.87	2.79	2.35	--	--	--	--	--
Structural Deficit	**-3.41**	**-4.55**	**-4.70**	**-6.65**	**-7.10**	**-7.29**	**-7.41**	**-7.37**
Year End Balances								
General Fund	$4.16	$2.46	$0.11	$0.00	$0.00	$0.00	$0.00	$0.00
Rainy Day Fund	7.47	7.76	8.11	--	--	--	--	--

Note: Billions of dollars. FY 26-27 Prior Year Lapses are reduced for net supplemental appropriations ($218 million) anticipated in the Budget Office's Fall Update. Although the FY 26-27 spending shifts to the Motor License and Gaming Funds ($225 million) are included with temporary support for that year, the shifts are also carried forward into future years. In practice, it is unclear if those funds could support the additional spending over the long term.

The forecast projects that the General Fund surplus will be largely depleted in FY 2026-27. The forecast makes no assumptions regarding future use of the Rainy Day Fund. Under current law, a distribution from the Rainy Day Fund upon the request of the Governor requires legislative approval (two-thirds majority) and can only be used for emergencies involving the health, safety or welfare of Commonwealth residents or economic downturns resulting in significant unanticipated revenue shortfalls that cannot be addressed through the normal budget process.

Table 7 compares the structural deficit projection from this outlook to the November 2025 Outlook and decomposes the change in the deficit into the revenue or spending projections. Based on this comparison:

- For FY 2025-26, the deficit is $0.4 billion lower than projected in the November 2025 Outlook due to higher net revenues.
- For FY 2026-27, the deficit falls by $1.14 billion due to higher net revenues partially offset by higher spending. Continued strong stock market gains and the AI investment boom drive the revenue overperformance, in addition to a one-time gain from the taxation of tariff refunds ($230 million).
- For FY 2027-28 and future years, positive revenue adjustments are carried forward, but they are offset by higher spending, notably the assumed lump sum adequacy increase ($400 million) for FY 2027-28 and higher DHS costs due to a rapidly aging population.

Table 7
Change in General Fund Deficit Outlook

	Actual 24-25	Actual 25-26	Budget 26-27	Forecast 27-28	28-29	29-30	30-31	31-32
November 2024 Outlook	**-$3.42**	**-$4.47**	**-$5.24**	**-$5.97**	**-$6.29**	**-$6.65**	**--**	**--**
November 2025 Outlook	**-3.41**	**-4.98**	**-5.84**	**-6.90**	**-7.27**	**-7.53**	**-$7.66**	**--**
Net Revenue Impact	--	0.48	1.40	1.16	1.08	1.01	0.97	--
Spending Impact	--	-0.05	-0.26	-0.91	-0.91	-0.78	-0.73	--
November 2026 Outlook	**-3.41**	**-4.55**	**-4.70**	**-6.65**	**-7.10**	**-7.29**	**-7.41**	**-$7.37**
Deficit Change	--	0.43	1.14	0.25	0.17	0.23	0.25	--

Note: Billions of dollars.

As noted, the General Fund surplus has been depleted and most temporary measures have been used, so that permanent revenue sources will likely be required to close the structural deficit. Therefore, **Table 8** concludes the outlook with a simulation that shows results from a 0.5 percentage point increase to the PIT and SUT rates for 2026. *The outlook does not make any recommendations regarding the methods policymakers should use to close projected structural deficits. The examples from this subsection are for illustrative purposes only, and provide context for the scope of the fiscal gap using the largest two tax sources whose revenue potential can be estimated with a relatively high degree of accuracy. It also highlights other issues that will impact residents (tax incidence, share of tax exported). Many other existing and new revenue sources are also viable options, as are discretionary spending cuts and reductions to various tax credits.*

Based on the 0.5 percentage point increase simulation:

- The higher rate generates $3.09 billion in net PIT revenues (after refunds). That estimate is static because it excludes (1) any behavioral response by workers, consumers and taxpayers, (2) direct, indirect and induced effects (i.e., multiplier effects) on all revenue sources and (3) any dynamic macroeconomic impacts.[11] The static estimate is reduced by $110 million for worker response (i.e., labor supply) and lower compliance and $90 million for multiplier effects using the IMPLAN input-output model.[12] In general, other tax revenues will decline if residents have less after-tax income to spend.
- The higher rate generates $1.45 billion in net SUT revenues (after refunds). The static estimate is reduced by $100 million for consumer response (i.e., price elasticities) and lower compliance and $50 million for multiplier effects using the IMPLAN input-output model.
- The bottom portion of the table displays the income groups that would effectively pay the higher tax. Based on the IFO tax incidence model, the PIT incidence assumes 5% is remitted by non-residents and the SUT incidence assumes 17%.[13] Despite a flat 3.07% tax rate, the state income tax is effectively

11 Multiplier effects capture impacts on firms directly impacted (e.g., retailers), firms in the supply chain (indirect) and workers/owners who will spend less due to reduced incomes from lower economic activity (induced). Dynamic impacts would reflect any expansion or contraction of the state economy due to the fiscal policy (not included).

12 The behavioral impacts would apply to all PIT revenues, not just the incremental portion from the higher tax rate.

13 See: IFO Pennsylvania Tax Incidence Model. An updated tax incidence model will be published next month. Estimates reflect taxes exported to non-residents and taxes paid indirectly (e.g., sales tax paid by businesses that is ultimately passed forward to consumers).

progressive due to tax forgiveness and the Working Pennsylvanians Tax Credit.[14] A general SUT rate increase is regressive because lower-income taxpayers remit a higher share of their pre-tax income in sales tax, and Consumer Expenditure Survey data show that (on average), their spending exceeds income. Alternatively, higher-income taxpayers remit a lower share of pre-tax income as sales tax because they remit a much larger share of pre-tax income as income tax and save a significant portion; and those amounts cannot be spent.[15]

- There is no offsetting positive impact from the new tax revenues that would be generated and spent by the state because the higher spending has already been effectively built into the forecast. The forecast assumes there is no significant reduction in state spending to bring the budget into balance, which would have a negative impact on economic growth. The forecast effectively assumes continued deficit-financed spending. However, at current levels, the full Rainy Day Fund balance could only support roughly 1.5 years of deficit spending.

Table 8
Simulation: 0.5 PPT Rate Increase (2026)

Tax Source	Static Estimate	Adjustments		Net Estimate
		Behavior	Multiplier	
Personal Income	$3,090	-$110	-$90	$2,890
Sales and Use	$1,450	-$100	-$50	$1,300

Tax Incidence		Personal Income		Sales and Use	
		Amount	Share	Amount	Share
$0	$50,000	$233	9%	$243	23%
$50,000	$100,000	$522	19%	$270	25%
$100,000	$200,000	$700	26%	$270	25%
$200,000	$500,000	$577	21%	$173	16%
$500,000	$1,000,000	$247	9%	$54	5%
$1,000,000	or more	$467	17%	$70	7%
Total		**$2,746**	**100%**	**$1,079**	**100%**

Note: Millions of dollars. Multiplier is direct, indirect and induced effects from IMPLAN. Personal income tax incidence assumes 5% remitted by non-residents; sales and use tax assumes 17%.

Although a much smaller revenue source, the phased-in CNIT rate reduction could also be delayed. The rate is scheduled to fall by 0.5 percentage points each year from 2026 (7.49%) to 2031 (4.99%). Each 0.5 percentage point reduction reduces revenues by $300 to $350 million (static estimate). Computing CNIT tax incidence is much more difficult than PIT and SUT because it is unclear how much of the tax is exported to non-resident shareholders and consumers compared to resident workers and consumers. Most research finds that the tax is mainly borne by shareholders.

14 See: IFO Personal Income Tax Progressive at Low End.

15 The effective tax rate computation in all tax incidence models uses the ratio of tax paid to pre-tax income. Therefore, although taxpayers cannot spend amounts remitted as taxes, that income will appear to reduce their effective tax rate.

Spending reductions are another policy option that could be used for deficit reduction. For example, policymakers could enact a 5% across-the-board sequester for all discretionary spending. Mandatory spending not available for sequester is assumed to include: most DHS programs, debt service, Department of Corrections, State Police and all PreK to 12 spending. For FY 2026-27:

- A 5% discretionary spending sequester yields a static spending cut of $270 (narrow definition) to $310 million (broader definition), roughly 6% of the $4.70 billion structural deficit for that year.
- A spending sequester would also have multiplier effects. Based on IMPLAN simulations using general government spending, the spending sequester would reduce General Fund tax revenues by $15 million. Overall, government spending has higher multipliers than tax changes because nearly all of the (first round) spending makes it out into the state economy, whereas a PIT rate increase would not immediately reduce spending one-for-one because some tax remittances would have been saved or are remitted by non-residents (roughly 5%).