



CITIZENS RESEARCH COUNCIL OF MICHIGAN

# Michigan Economic and Budget Update

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# State of the National Economy



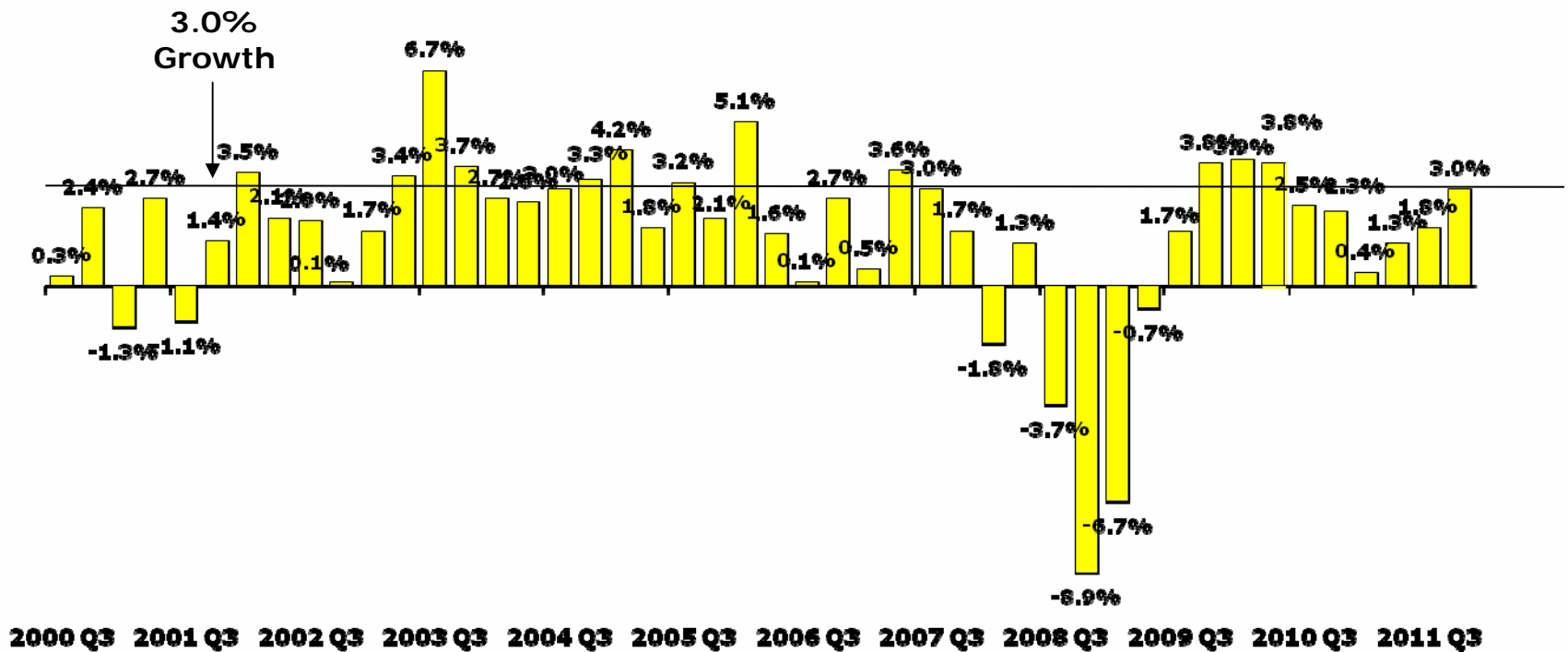
## Overview

- National recession has been over for 3 years
- Recovery has been uneven and halting; risk of double dip very high last spring
- Lately economy has been strengthening: auto sales, stock market, employment growth have all been better
- Risks to outlook include oil prices, Europe, and federal fiscal policy



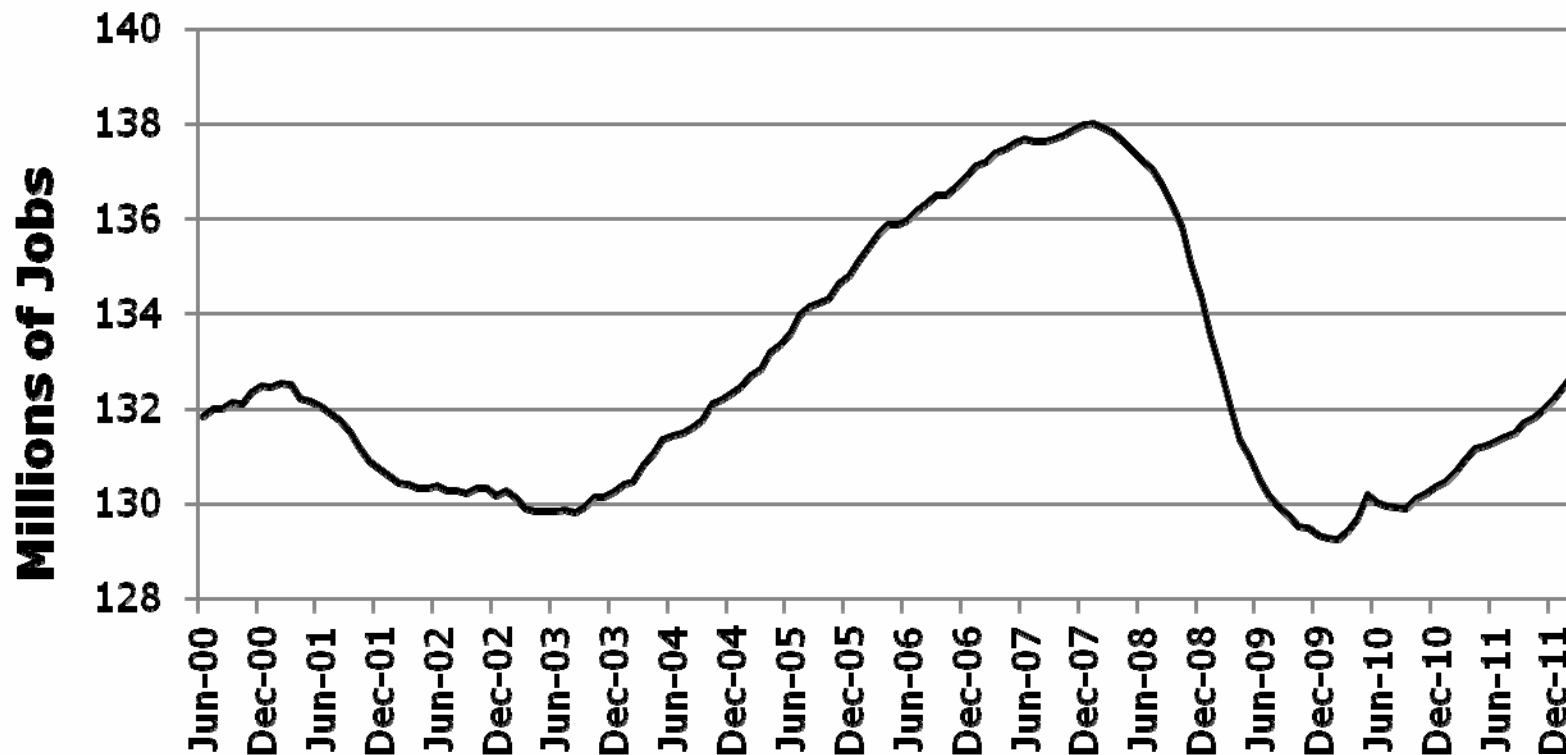
# Recession Has Been Over for Almost 3 Years

## Real GDP Growth



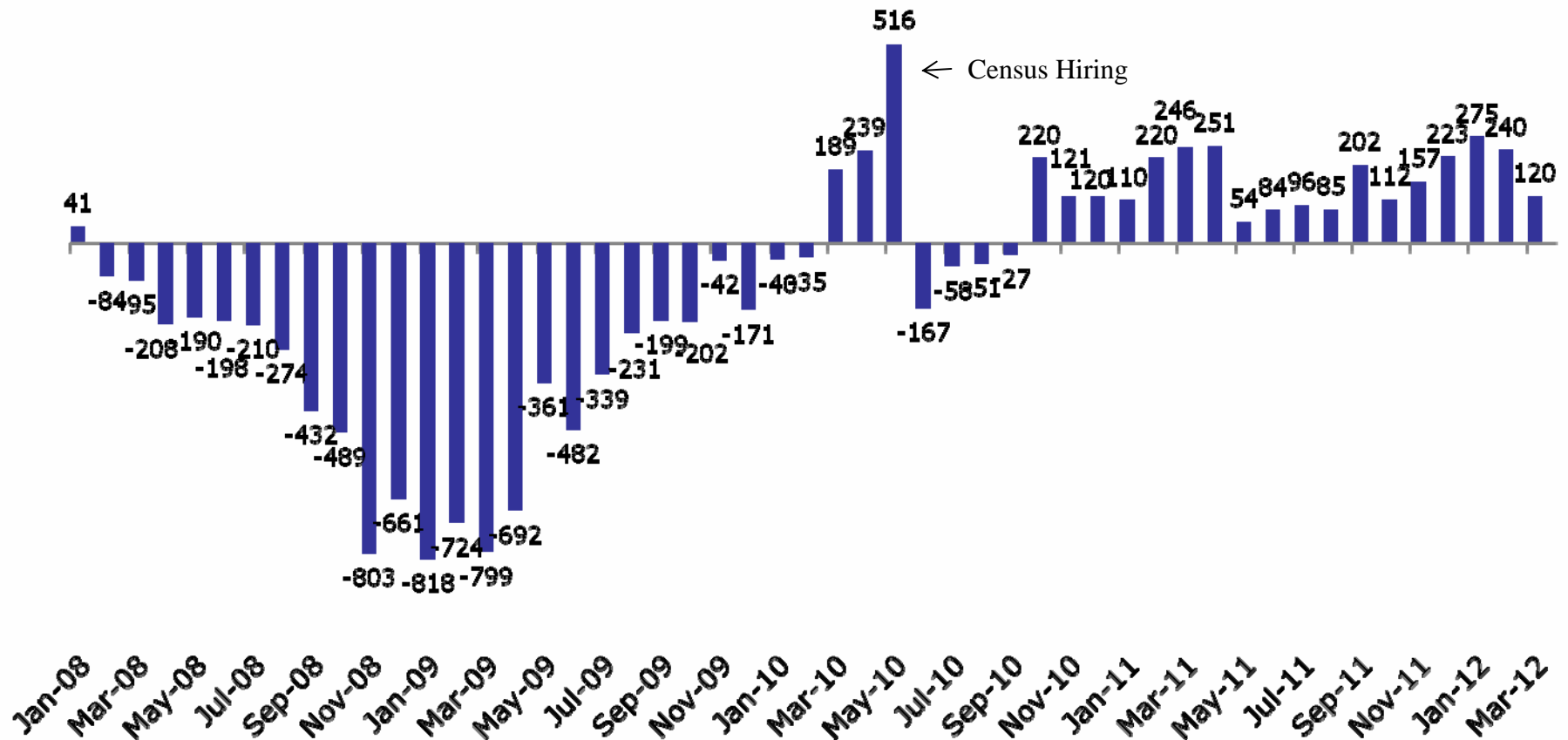


# U.S. Employment Growing But Still Down 5.3 Million Jobs from Peak





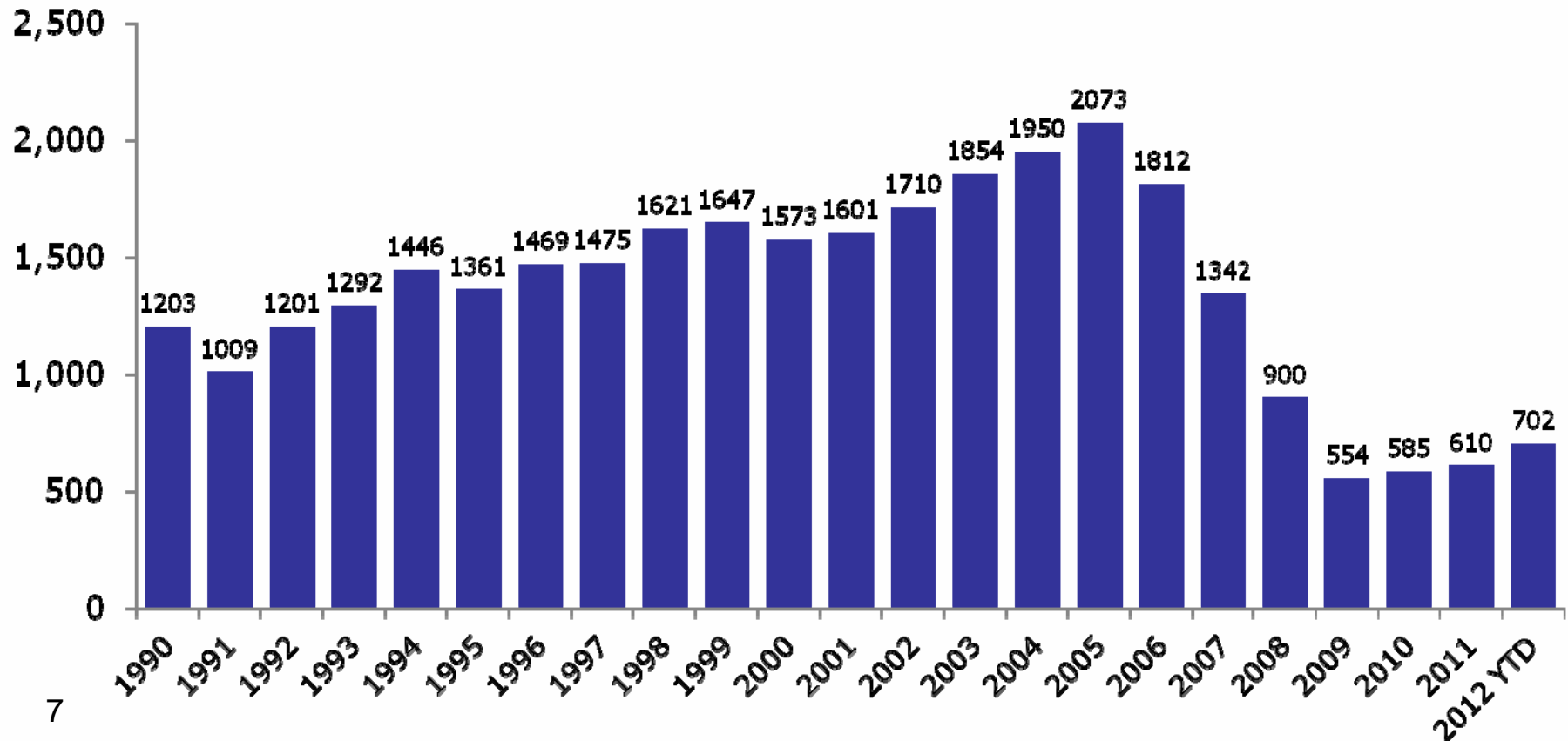
# Monthly Employment Growth Improving





# Housing Starts Improving But Remain Extremely Depressed

Between 1959 and 2007 Total Never Below 1M

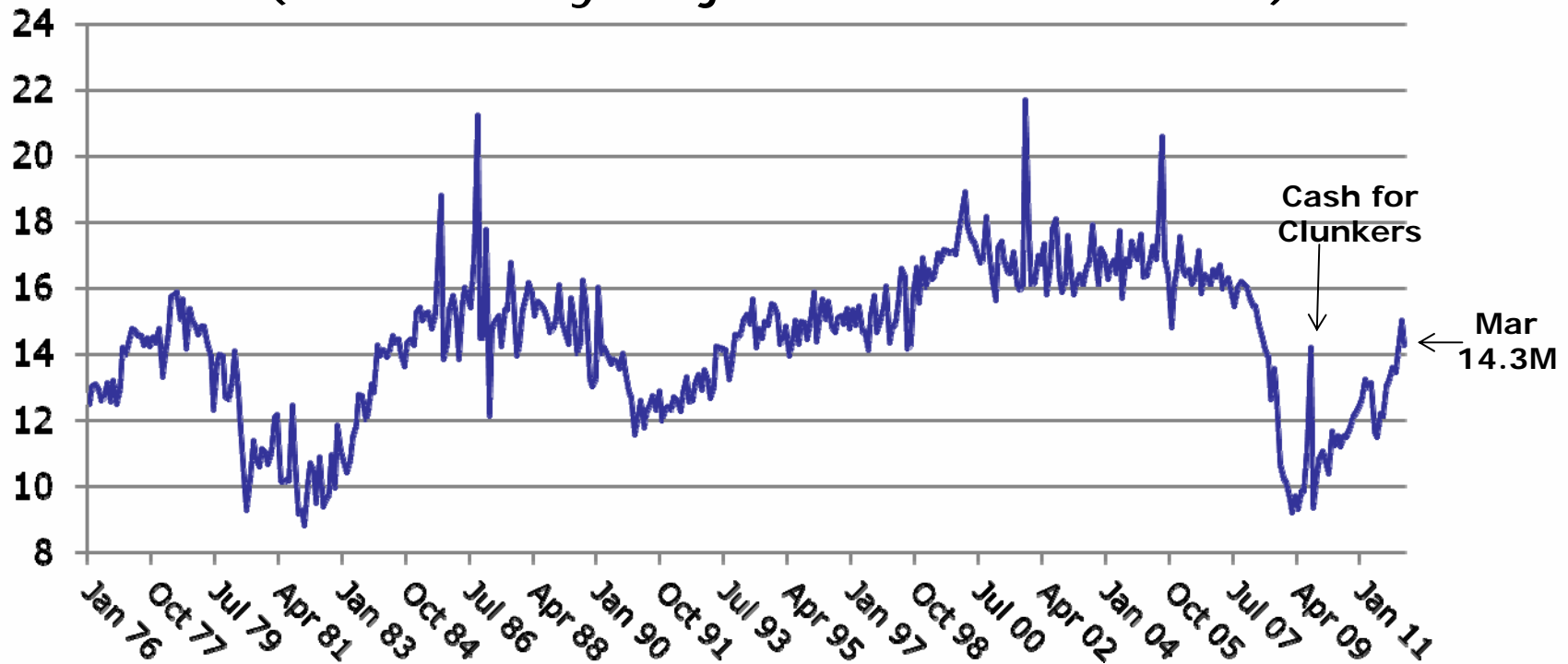


Source: Newly Privately Owned Housing Starts St. Louis Fed (FRED) 2012 annualized Jan and Feb avg..



# Vehicle Sales Are Recovering

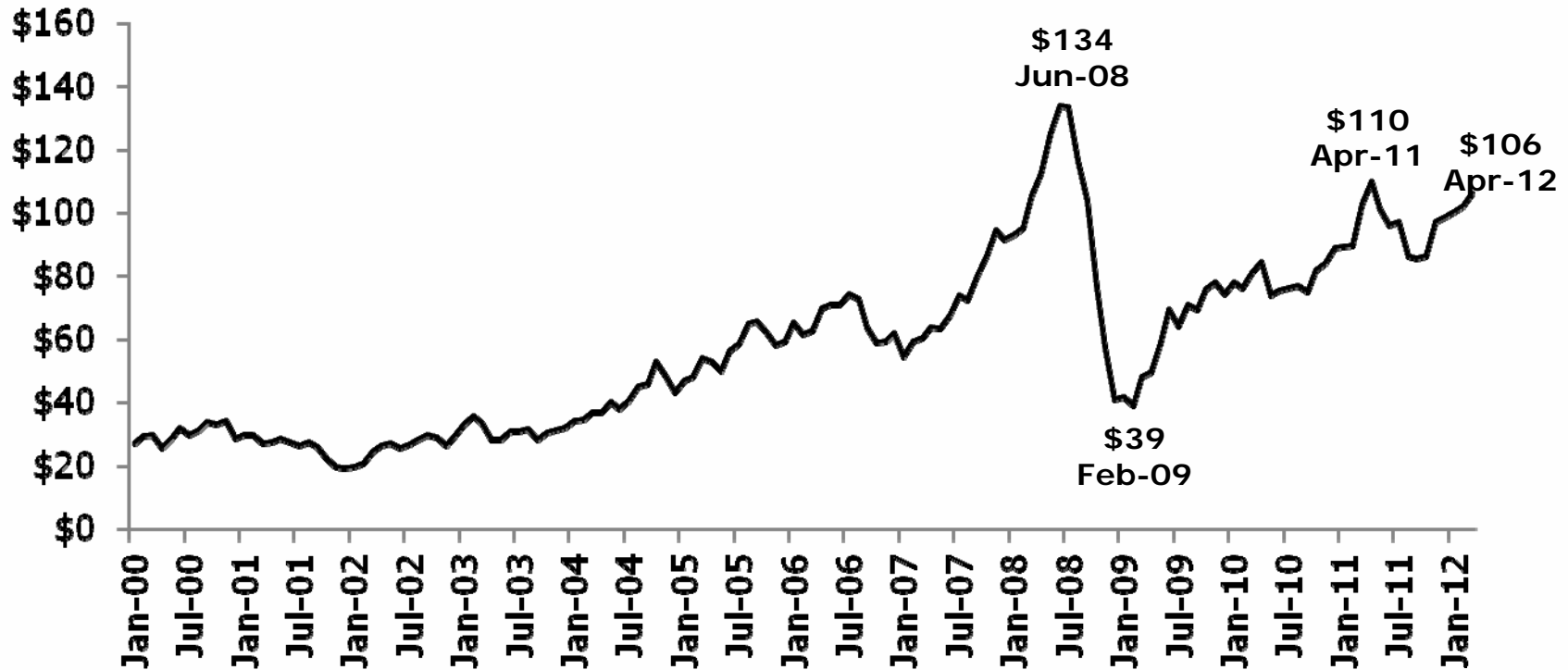
Monthly Light Vehicle Sales  
(Seasonally Adjusted Annual Rate)







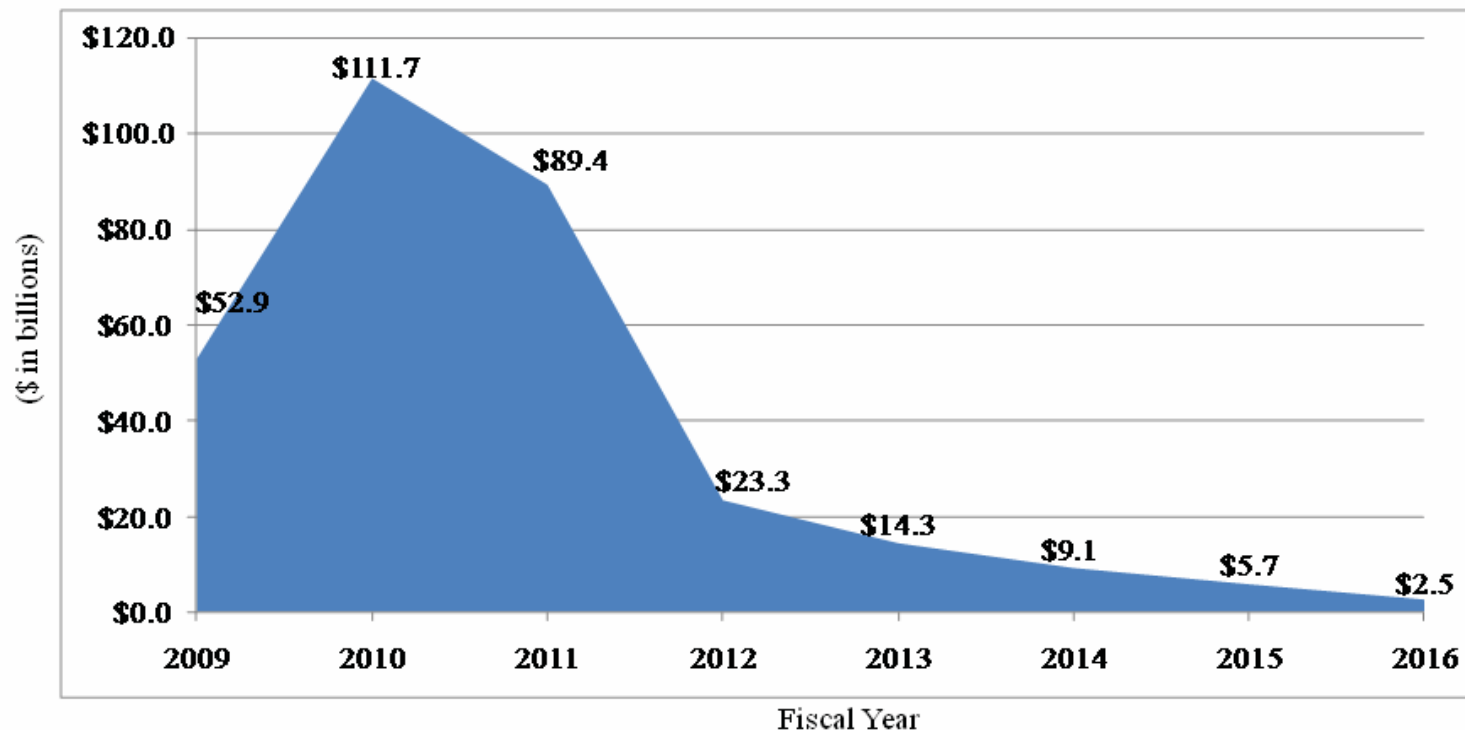
# Oil Tops \$100 Per Barrel Again





# End of ARRA and Other Stimulus Drags on Recovery

Temporary Federal Aid to States



10 Source: Government Accounting Office as presented by NASBO in *Preliminary Summary of NGA/NASBO Spring 2011 Fiscal Survey of the States*.  
<http://www.nasbo.org/LinkClick.aspx?fileticket=IW3fw0p2k0A%3D&tabid=38>



## Federal Fiscal Policy

- Federal deficit projected to be 7.6% of GDP in 2012; higher than any year from 1946 to 2008
- Under current law, many tax cuts would expire -- CBO projections have revenues going from 15.8% of GDP in 2012 to 19.8% in 2014, a 25% increase
- If Congress does not pass a bill with \$1.2 trillion in cuts by January, automatic cuts scheduled to go into effect ("sequestration"); cuts would be in defense and nonexempt programs including Medicare
- Unlikely current law will remain in place for taxes or spending, but significant deficit reduction needs to occur representing a risk for both the economic outlook and state and local programs supported by federal spending



## Summary of U.S. Outlook

- U.S. growth is improving, but still slow;
- Improving light vehicle sales are a major plus for Michigan (particularly SE Michigan)
- Rising oil prices threaten to slow growth
- Aggressively addressing the federal deficit is a significant risk to the near-term outlook; not addressing is a significant risk to the long-term outlook
- Financial markets in Europe are also a risk to outlook



# Michigan's Recent Economic Experience

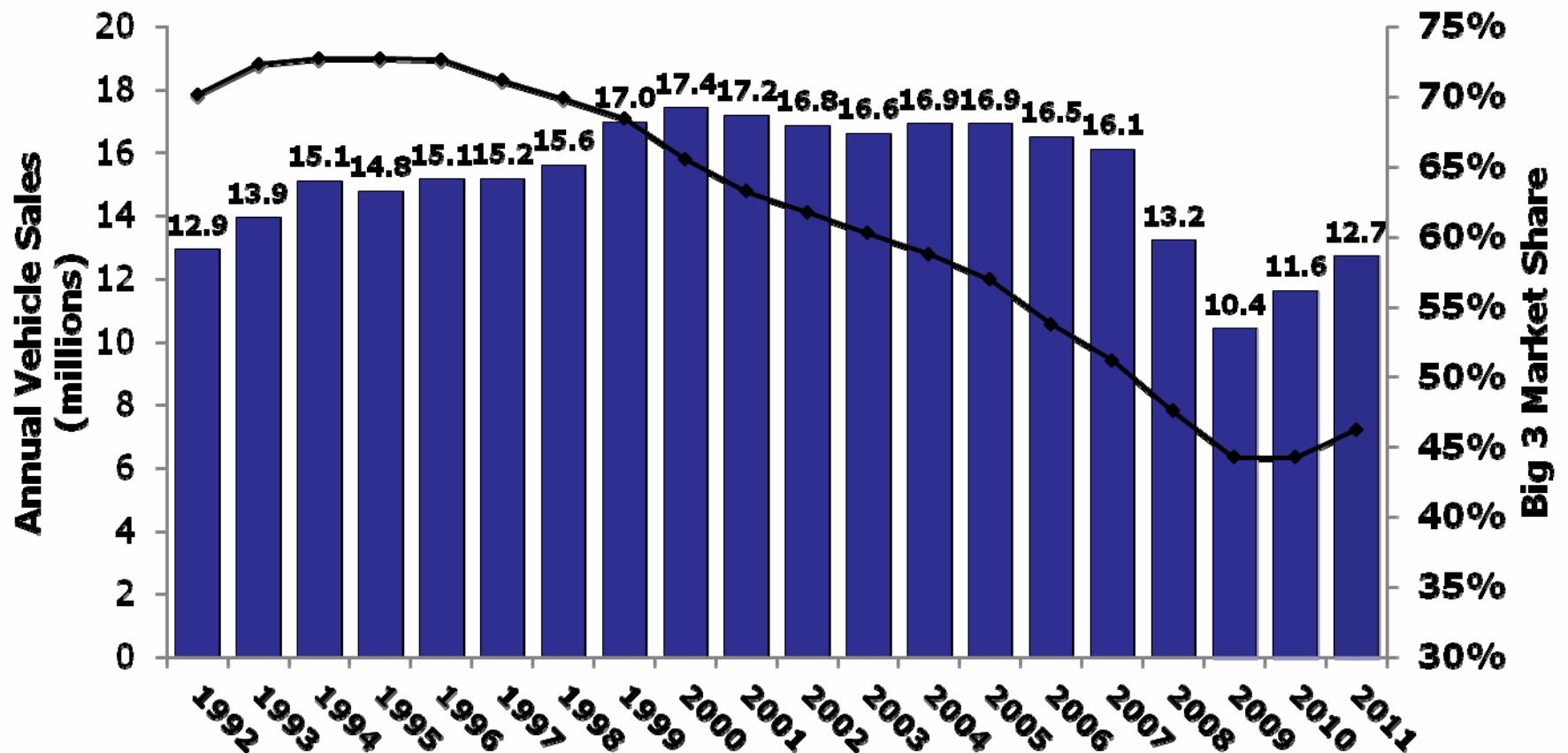


## The Last Decade Was an Economic Disaster for Michigan

	<u>Growth 2000 to 2010</u> <u>U.S.</u>	<u>Growth 2000 to 2010</u> <u>Michigan</u>	<u>Michigan</u> <u>Rank</u>
Population	9.6%	-0.8%	51
Real Per Capita GDP*	6.5%	-6.4%	50
Employment	-0.3%	-17.4%	51
Real Per Capita Income	4.0%	-6.8%	51



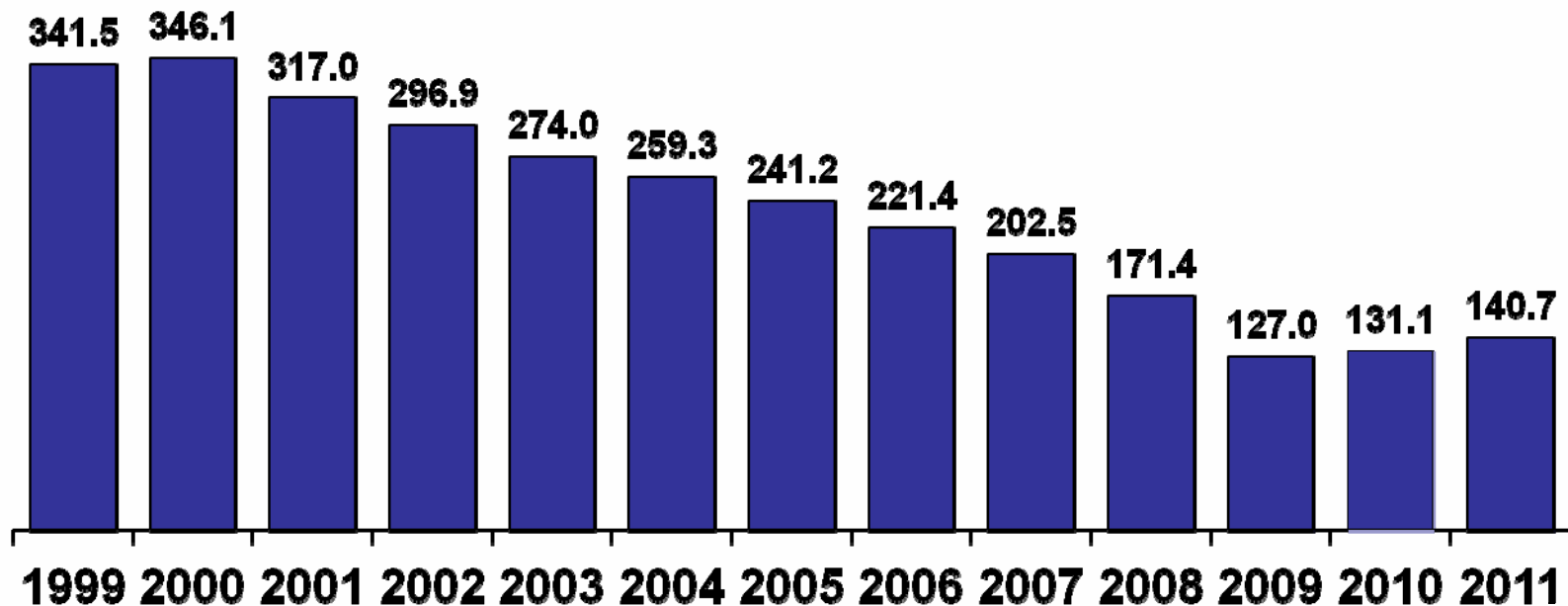
# Big 3 Market Share Plummet





# 200,000 Transportation Equipment Jobs Lost

Michigan Transportation Equipment Employment  
(In Thousands)

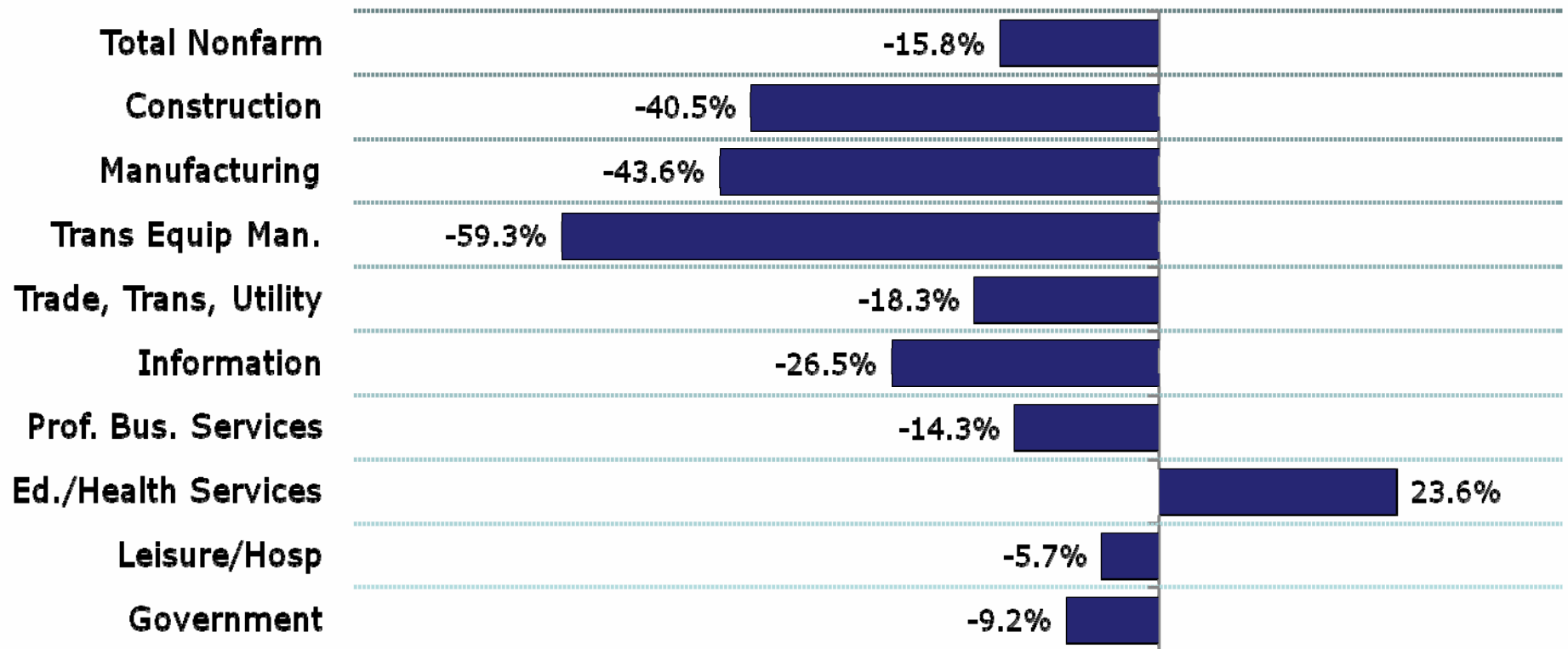






# Almost Every Sector in Michigan Has Lost Jobs

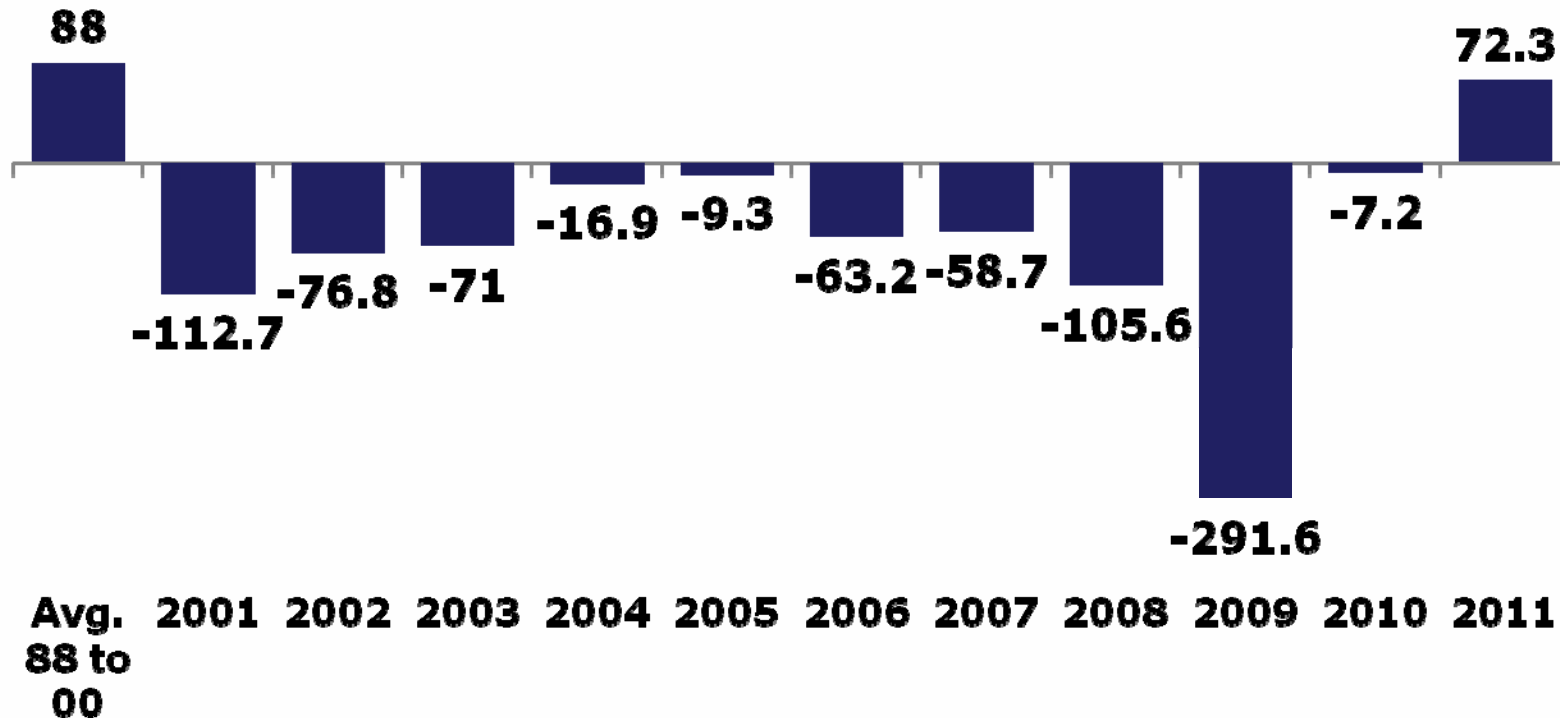
**2000 to 2011**





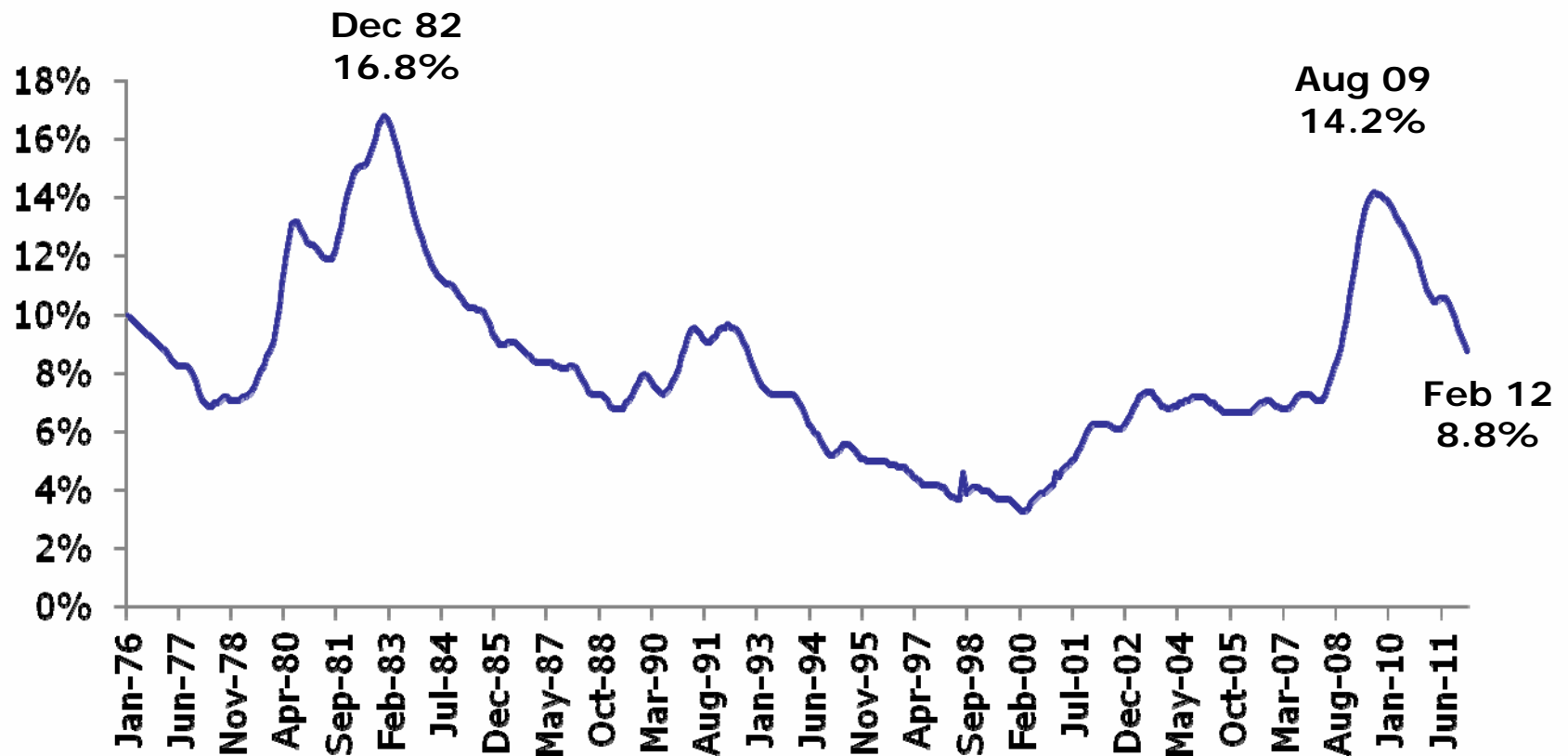
# After 10 Years of Decline Michigan Added Jobs in 2011

Annual Change in Payroll Employment (thousands)





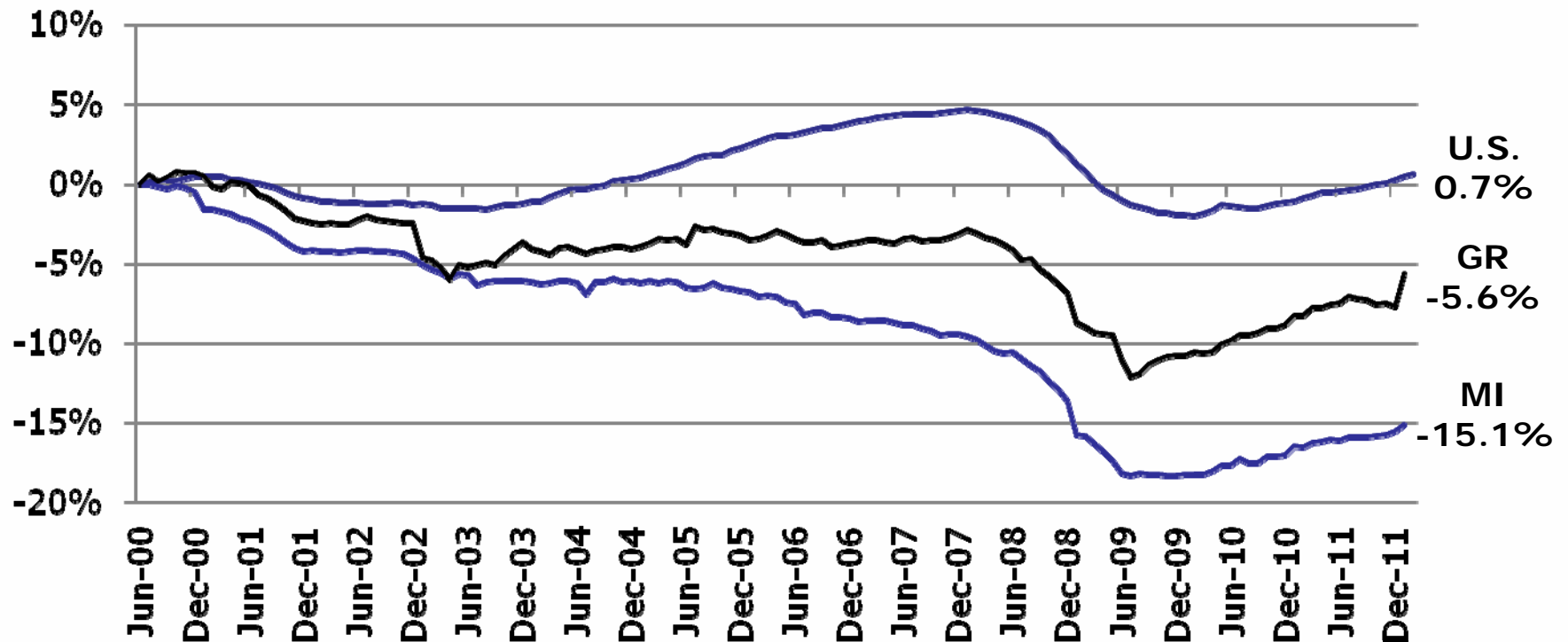
# Michigan's Y-O-Y Unemployment Rate Drop Largest in U.S.





# Grand Rapids Area Employment Lags U.S. But Out Performs Michigan

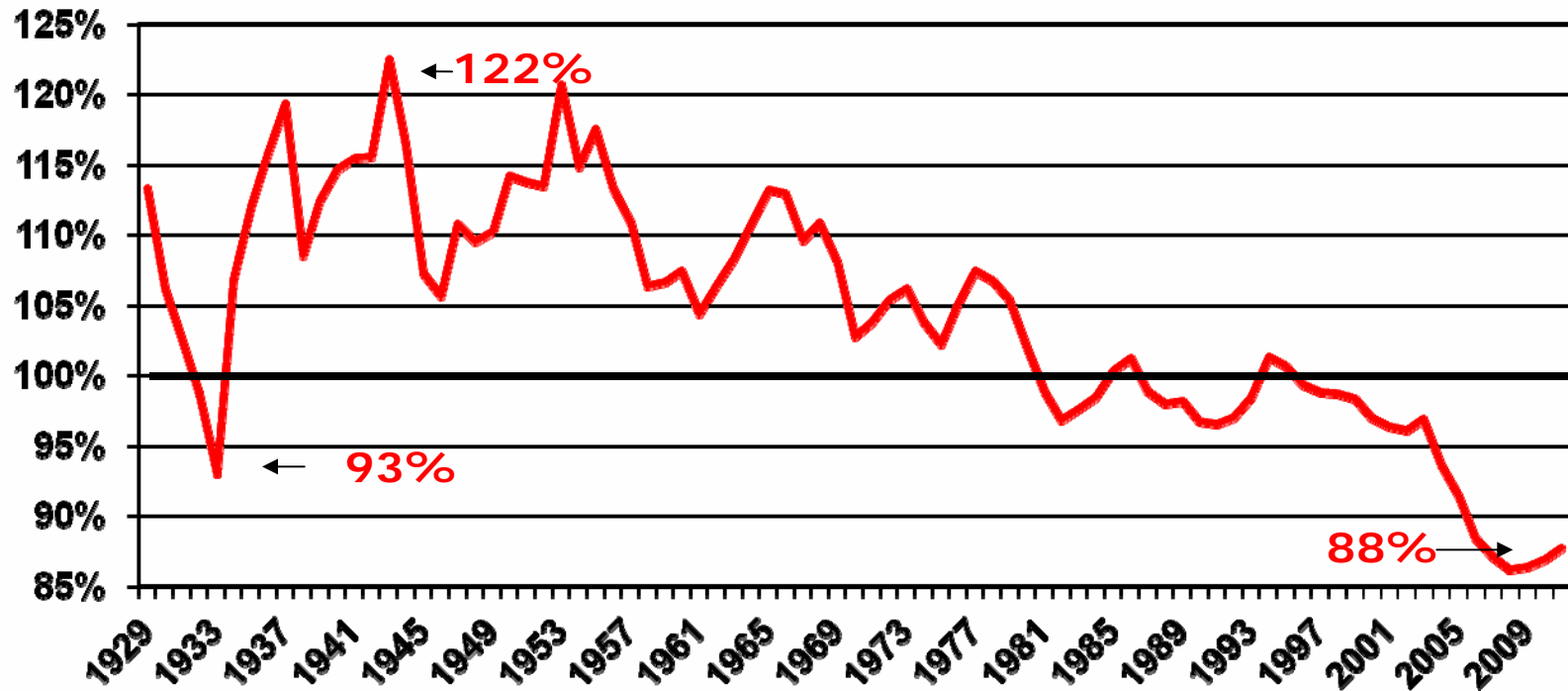
Cumulative Percent Change in Employment Since June 2000





## Michigan Has Become Poorer Relative to Other States

Michigan per Capita Income as a Percent of U.S. Per Capita Income Rank has fallen from 20<sup>th</sup> in 2001 to 37<sup>th</sup> in 2011





# State Budget – Recent History



# Michigan Taxes at Average as % of Income But Well Below Average Per Capita

## State and Local Taxes

Year	Per Capita			Per \$1,000 of Personal Income		
	U.S. (2009\$)	MI (2009\$)	MI as % of U.S.	U.S. (2009\$)	MI (2009\$)	MI as % of U.S.
1979	\$2,704	\$3,088	114.2%	\$100.13	\$108.51	108.4%
1989	\$3,287	\$3,452	105.0%	\$103.23	\$110.41	107.0%
1999	\$3,761	\$3,891	103.5%	\$103.08	\$108.46	105.2%
2009	\$4,144	\$3,627	87.5%	\$106.69	\$108.22	101.4%



## State Spending From State Resources Down in Most Categories

	FY 2002 <u>(millions\$)</u>	FY 2012 <u>(millions\$)</u>	Nominal % <u>Change</u>
Medicaid/DCH	\$3,066	\$4,901	59.8%
Corrections	\$1,653	\$1,927	16.6%
Human Services	\$1,230	\$1,155	-6.1%
K-12	\$11,221	\$10,550	-6.0%
Community College	\$320	\$284	-11.3%
Universities/Fin Aid	\$1,941	\$1,264	-34.9%
Revenue Sharing	\$1,517	\$959	-36.8%
All Other	<u>\$5,139</u>	<u>\$5,219</u>	<u>1.6%</u>
Total	\$26,087	\$26,260	0.7%
U.S. CPI - U	178.9	229.1	28.1%





## Select Budget Indicators

	<u>FY 2002</u>	<u>FY 2012</u>	<u>Percent Change</u>
Medicaid Caseload	1,211,816	1,920,000	58.4%
Prison Population	47,270	43,455	-8.1%
K-12 Pupil Count	1,647,459	1,552,300	-5.8%
Comm. Col. Students	116,802	177,277	51.8%
University Students	241,205	262,615	8.9%
Michigan Per Cap Income	30,193	35,597	17.9%
U.S. CPI-U	178.9	229.1	28.1%



## 2011 Tax Changes

- MBT repealed and replaced with CIT. Noncorporate entities are exempt.
- Business tax revenues fall From \$2,013M to \$352M a \$1.6B cut (83 percent)
- IIT increased by \$1,353M by eliminating or reducing credits and exemptions and freezing rate
- Tax changes aimed at economic development not budget balancing



## FY2012 Budget Update

### *Economic Improvement*

- FY2012 budget completed in late May 2011 (based on May 2011 revenue estimates)
- Since then, marked improvement in condition of the budget, as result of improving economic situation
- Jan. 2012 revenue estimate: add'l \$407M from May
- Estimated FY2012 year-end balances:
  - General Fund surplus: \$70M to \$628M
  - School Aid Fund surplus: \$0 to \$119
- What to do with these add'l resources?
  - Some of it one-time in nature – result of FY2011 year-end balance increase
  - Some of it ongoing – result of economic conditions which will improve base going forward
  - Important consideration: use funds appropriately to maintain structural balance in budget (ongoing revenue = ongoing spending)



## Revenue Estimates Up From May But FY2014 Below FY2011

	Change From May 2011			
	<u>FY 2011</u>	<u>FY 2012</u>	<u>FY 2013</u>	<u>FY 2014</u>
GF-GP	\$129.8	\$278.0	\$126.5	
SAF	<u>\$109.7</u>	<u>\$128.5</u>	<u>\$89.7</u>	
Total	\$239.5	\$406.5	\$216.2	

	Change From Prior Year's Revenue Total			
	<u>FY 2011</u>	<u>FY 2012</u>	<u>FY 2013</u>	<u>FY 2014</u>
GF-GP	\$1,134.5	\$217.4	\$4.1	\$201.4
SAF	\$431.2	(\$484.6)	\$291.3	\$304.7
Stimulus	<u>(\$401.0)</u>	<u>(\$1,120.0)</u>	<u>\$0.0</u>	<u>\$0.0</u>
	\$1,164.7	(\$1,387.2)	\$295.4	\$506.1



# One-Time vs Ongoing Spending

## *Key Distinction When Using Fund Balances*

- Designate items as “one-time” because ongoing revenues not sufficient to support spending
- Governments use “one-time” spending for a variety of reasons:
  - Address short-term needs
  - Pay down debt
  - Save for the future
- Substantial portions of FY2011 surpluses already designated as “one-time” spending in FY2012:
  - \$460M from the School Aid Fund
  - \$427M from the General Fund (including \$256M to the Rainy Day Fund)
- Governor’s plan exhausts fund balances in FY2013, either in “one-time” spending or deposited in the Rainy Day Fund



# **FY 2013 Budget**



## **Situation Facing Governor**

*Starting Point Different Than FY2012*

- Budget balanced (unlike FY2012 when faced with a \$1.5B shortfall in General Fund)
- Economic improvement translates to moderate revenue growth in both General and School Aid Funds
- Sizeable projected year-end FY2012 balances in both General and School Aid Fund budgets
- Pressures to restore funding, after cuts taken in FY2012
- Tax restructuring complete (although potential for personal property tax reform – affects locals mainly)
- Scheduled income tax rate cut (1/2013) costs \$133M



# Themes in Governor's Budget

*Continuation of FY2012*

- Structurally balanced in both General and School Aid Funds
- Some moderate funding increases in FY2013 – higher education, local government, public safety
- FY2014 budget - “planning budget” – basically flat
- “Best Practices” funding expanded to other areas
- “All money is green” – SAF for higher education
- Distinction between one-time and ongoing spending
- Build up reserves in Rainy Day Fund to \$388M
- Continue to pay down debt (state employee OPEB liabilities)





## K-12 School Aid Highlights

- Total spending: minimal increase (0.2%) for FY2013
  - But, \$460M in “one-time” spending in FY2012
  - Only \$150M designated as “one-time” in FY2013
  - Some “one-time” converted to ongoing spending, but remainder is removed
  - Ongoing spending: increase of \$214M or 2%
- Freezes foundation grants (min. \$6,846), continues \$470 cut
- Half-day kindergarten receives one-half foundation
- Continues “best practices” incentive funding
- Adds new student performance funding component
- Increases funding to help offset retirement costs
- Includes competitive grants to encourage consolidation



# Performance/"Best Practices" Funding

## *Adds New Programs*

- \$190M available to districts in two areas (up from \$154M in FY2012, but only \$50M is ongoing)
- New - approx. \$70M (up to \$100pp) for student achievement
  - \$30pp for math proficiency grades 3-8
  - \$30pp for reading proficiency grades 3-8
  - \$40pp for high school students across 4 years
- Approx. \$120M (est. \$78pp) for districts meeting 5 of 6 "best practices" - similar to current-year
  - Schools of choice, measure student growth 2X year, dual enrollment, online learning, health care policy holder (existing), and dashboard (existing)
- New - 5% of ISD general operation funding tied to districts meeting 4 of 5 "best practices"
  - Service consolidation plan, competitive bid non-instructional service, technology plan, dashboard, work with other ISDs



# K-12 Per-Pupil Funding

*Small Increase Offset by Retirement Rate Increase*

## Per-Pupil Funding Changes Compared to FY2012

	<u>FY2012</u>	<u>FY2013</u>	<u>FY2014</u>
Foundation (minimum)	\$ 6,846	\$ 6,846	\$ 6,846
Best Practice/Performance Funding	\$ 100	\$ 178	\$ 65
Retirement Contribution Incr. Cost Offset	\$ 100	\$ 115	\$ 115
Subtotal	\$ 7,046	\$ 7,139	\$ 7,026
% Change from FY2012		1.3%	-0.3%
Retirement Contribution Incr. (compared to '12)	\$ -	\$ (166)	\$ (215)
Net Change	\$ 7,046	\$ 6,973	\$ 6,811
% Change from FY2012		-1.0%	-3.3%

***Retirement Rate Increase: 24.5% in '12 to 27.4% in '13 of payroll***



# School Funding Down Sharply

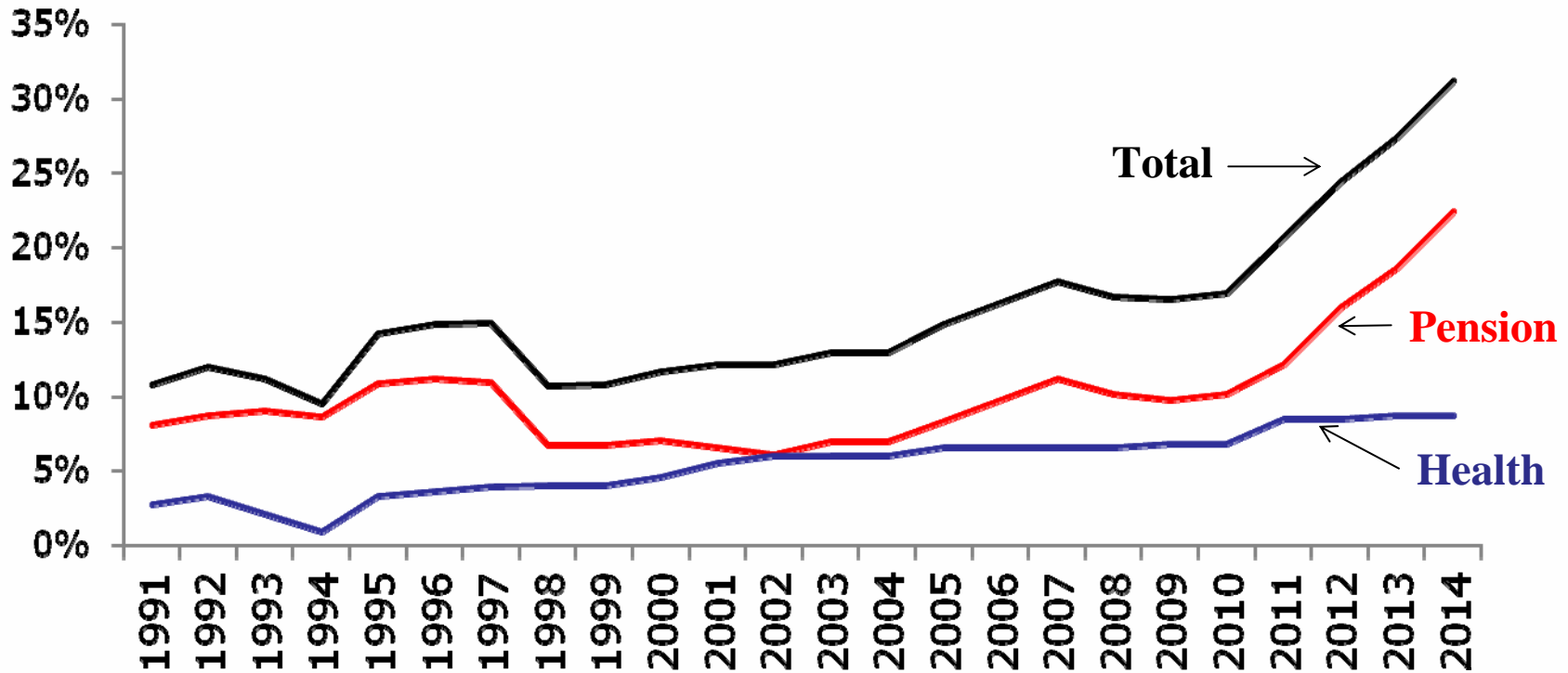
Fiscal Year	State Apppriated Funds		Pupils		Per Pupil Funding	
	Funds (2013\$)	Change From 2000	Number (millions)	Change From 2000	Amount (2013\$)	Change From 2000
2000	\$13,616.3		1.6966		\$8,026	
2001	\$14,217.7	4.4%	1.7042	0.4%	\$8,343	4.0%
2002	\$14,645.1	7.6%	1.7096	0.8%	\$8,566	6.7%
2003	\$14,454.6	6.2%	1.7149	1.1%	\$8,429	5.0%
2004	\$13,783.5	1.2%	1.7144	1.0%	\$8,040	0.2%
2005	\$13,410.3	-1.5%	1.7078	0.7%	\$7,852	-2.2%
2006	\$13,160.5	-3.3%	1.6975	0.1%	\$7,753	-3.4%
2007	\$13,187.5	-3.1%	1.6811	-0.9%	\$7,845	-2.3%
2008	\$12,435.7	-8.7%	1.6526	-2.6%	\$7,525	-6.2%
2009	\$12,122.2	-11.0%	1.6197	-4.5%	\$7,484	-6.7%
2010	\$11,467.3	-15.8%	1.5957	-5.9%	\$7,186	-10.5%
2011	\$11,305.2	-17.0%	1.5694	-7.5%	\$7,203	-10.2%
2012	\$11,217.1	-17.6%	1.5528	-8.5%	\$7,224	-10.0%
2013*	\$10,986.0	-19.3%	1.5429	-9.1%	\$7,120	-11.3%

36 \* Gov's recommendation

Source: Senate Fiscal Agency and CRC calculations.



## K-12 Retirement Costs Soar From 16.9% of Payroll in 07 to 31% in 14





## Community Colleges

### *Moderate Growth Tied to Performance*

- Total appropriation cut by 4% in FY2012 – ½ across-the-board and ½ based on performance indicators
- Overall 3% increase (\$9M) in FY2013 for new “performance funding” – designated critical skills areas (CSAs)
  - Amount varies by college based on degree completions in CSAs - range from 1.5% to 8.4%
- Small increase (\$1.7M) to help defray retirement cost increases associated with state-administered system
- Continues to use SAF (\$198M) for operational support



## Higher Education

*Moderate Growth but Short of Restoring FY2012 Cuts*

- University funding was cut 15% last year
- Overall 3% increase (\$36M) in FY2013 for new “performance funding” based on 4 factors
  - Growth in undergraduate degree completions, CSA completions, Pell Grant students, tuition restraint
  - Amounts vary by school – range from 0.9% to 7.6% (before tuition restraint allocation)
- Continues to use SAF (\$200M) for operational support



## Corrections

*Represents Over One-Fifth of General Fund Budget*

- Prison population reduced to 43,018 in 2011, down from historic peak of nearly 51,454 in 2006 (nearly 20% decline)
  - Court commitments remained stable, but moves to parole increased and fewer returns to prison
- General Fund spending declining, but not at same pace as prisoner population
- FY2013 budget increases General Fund spending by 1.6% - largely tied to employee pay/insurance
- Cost savings resulting from facility closures, position eliminations, and competitively bidding health care





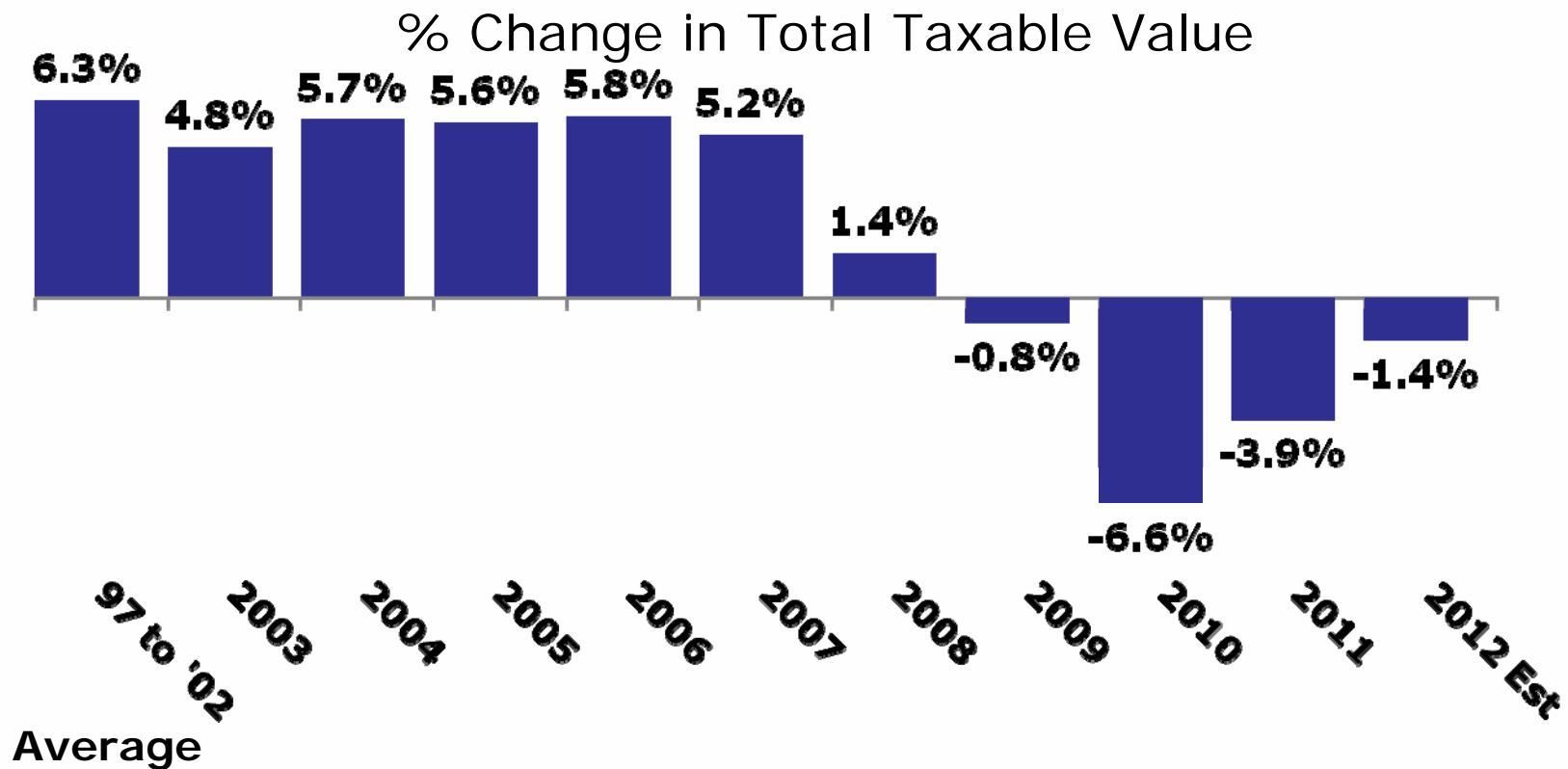
## Assistance to Local Governments

### *Small Increases*

- Constitutional payments (cities, villages, twps) to receive 2% increase based on sales tax growth
- Incentive funding (EVIP) for CVTs maintained at \$210M (cut by 1/3 in 2012)
- Counties revenue-sharing program replaced with new, incentive-based funding similar to CVTs
  - Increase of \$11M (only 75% of full amount)
- Increases funding (\$20M one-time) for competitive shared services grants to \$25M, allows counties to apply for funding



# Property Taxes Had Held Up Well But That Has Changed





## Property Tax Growth Varies Widely

	Taxable Value Growth		
	<u>2000 to 2007</u>	<u>2007 to 2011</u>	<u>2000 to 2011</u>
Pontiac	42%	-37%	-11%
Livonia	31%	-20%	5%
Grand Rapids	38%	-3%	34%
Wyoming	39%	-12%	22%
Kentwood	34%	-7%	25%
E. Grand Rapids	46%	4%	52%
Claire	38%	6%	47%
US-CPI U	20%	8%	31%



## Building Up Reserves

- FY2012 budget included \$256M deposit to Rainy Day Fund, first since FY2000
- FY2013 proposal provides additional \$133M
- Still a way off from \$1.3B surplus at end of FY2000
- Reserves serve as hedge against economic improvement stalling and federal budget cuts
- Reserves used to help manage state's cash needs throughout the year
- Sends positive message to state's creditors



## State Workforce and Employee Compensation

*Further Shrinkage*

- 3% reduction in budgeted classified FTEs (53,314)
- Recognizes the cost increases associated with recently agreed-to collective bargaining agreements
  - Net increase of \$124M in compensation increases
  - Generally, 1% base pay inc. and 1% lump sum payment
  - Non-represented employees to receive 3% base pay inc. and 2% lump sum payment
  - 80/20 health care premium sharing effective FY2013 for all state workers
- Continues to prefund OPEB liabilities for state workers (\$465M)



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- Promotes sound policy for state and local governments through factual research – accurate, independent and objective
- Relies on charitable contributions of Michigan foundations, businesses, and individuals
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## Recent Research

- Education Series – K-12 Finance; charter schools; early childhood; teaching reforms; governance; special education
- Local Government – Collaboration/consolidation (Kent County 2010); government dashboards; local income taxation
- Detroit – Fiscal situation; legacy costs; working on reform options
- State Budget – Ongoing monitoring of state fiscal situation; several budget notes published each year



**Questions?**





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