



CITIZENS RESEARCH COUNCIL OF MICHIGAN

Michigan's Economic, Revenue and Budget Outlook

C.S. Mott Foundation Trustee Meeting

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Citizens Research Council

- Founded in 1916
- Statewide
- Non-partisan
- Private not-for-profit
- 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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What is Happening in Michigan?

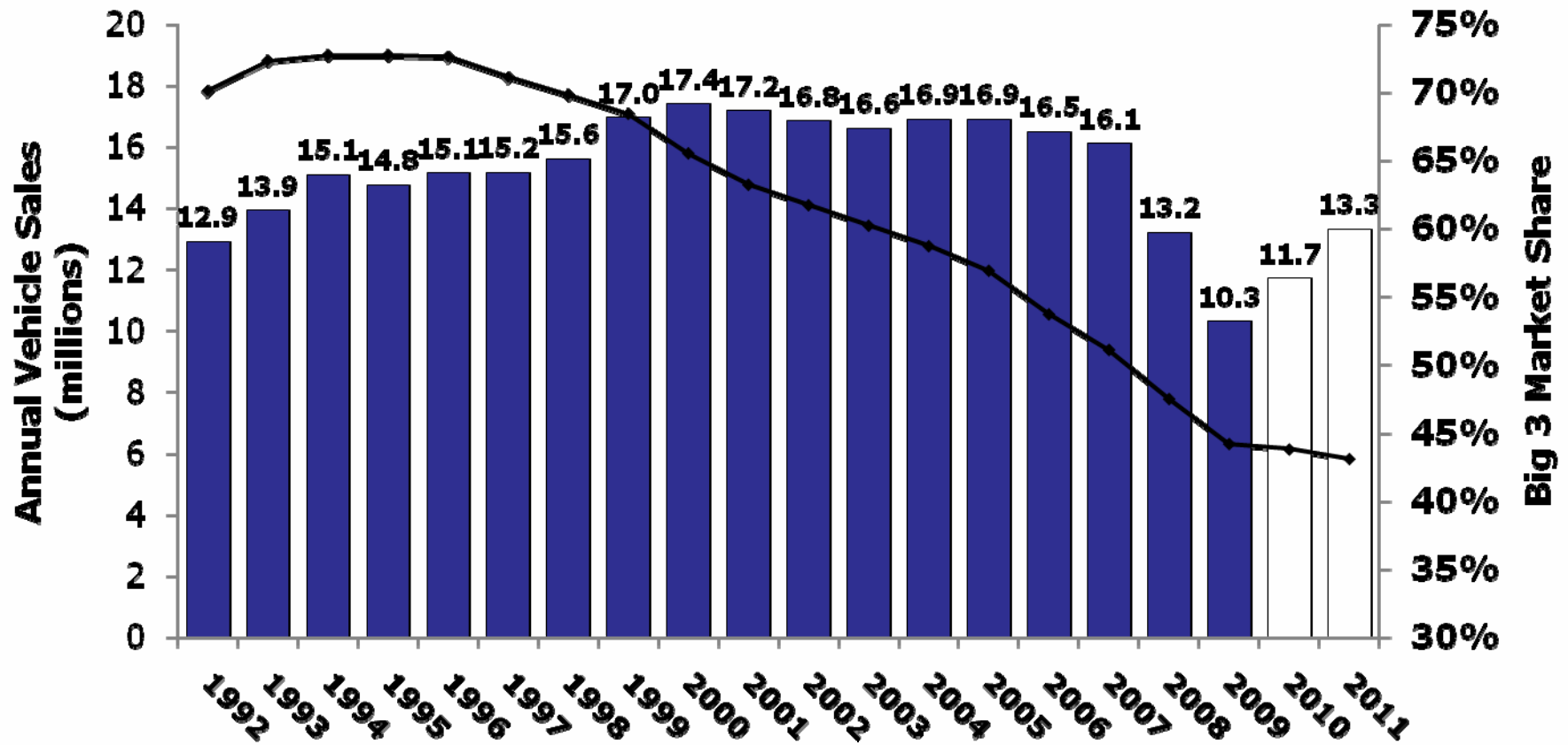


The Last Decade Has Been an Economic Disaster for Michigan

| | Growth 2000 to 2009 | | Michigan |
|------------------------|---------------------|-----------------|-------------|
| | <u>U.S.</u> | <u>Michigan</u> | <u>Rank</u> |
| Population | 8.8% | 0.1% | 51 |
| Real Per Capita GDP* | 9.7% | -3.8% | 51 |
| Employment | -0.7% | -17.1% | 51 |
| Real Per Capita Income | 3.6% | -7.1% | 51 |



Big 3 Market Share Plummet

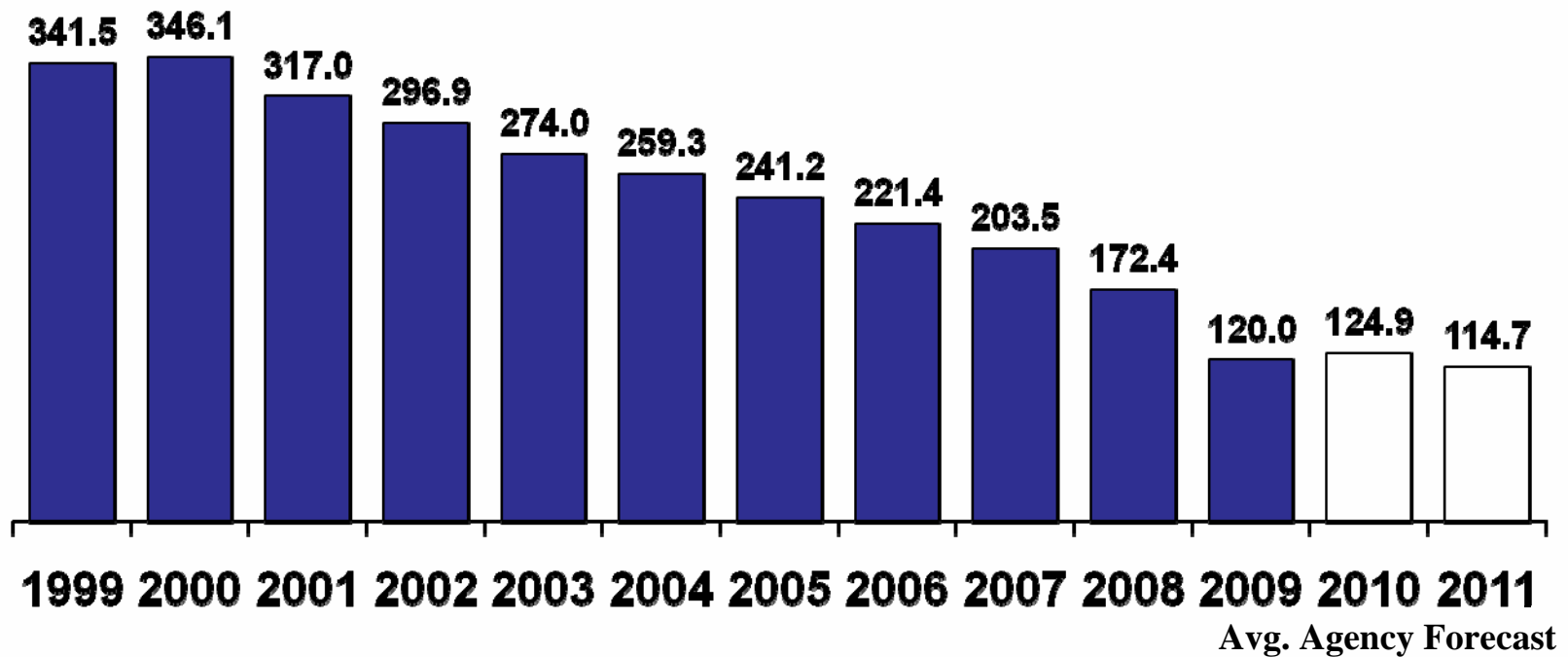


Source: 2009-2011 sales are the May 2010 Cons. Estimates; 2009-2011 share RSQE.



3 in 4 Auto Jobs Lost by 2011

Michigan Transportation Equipment Employment
(In Thousands)





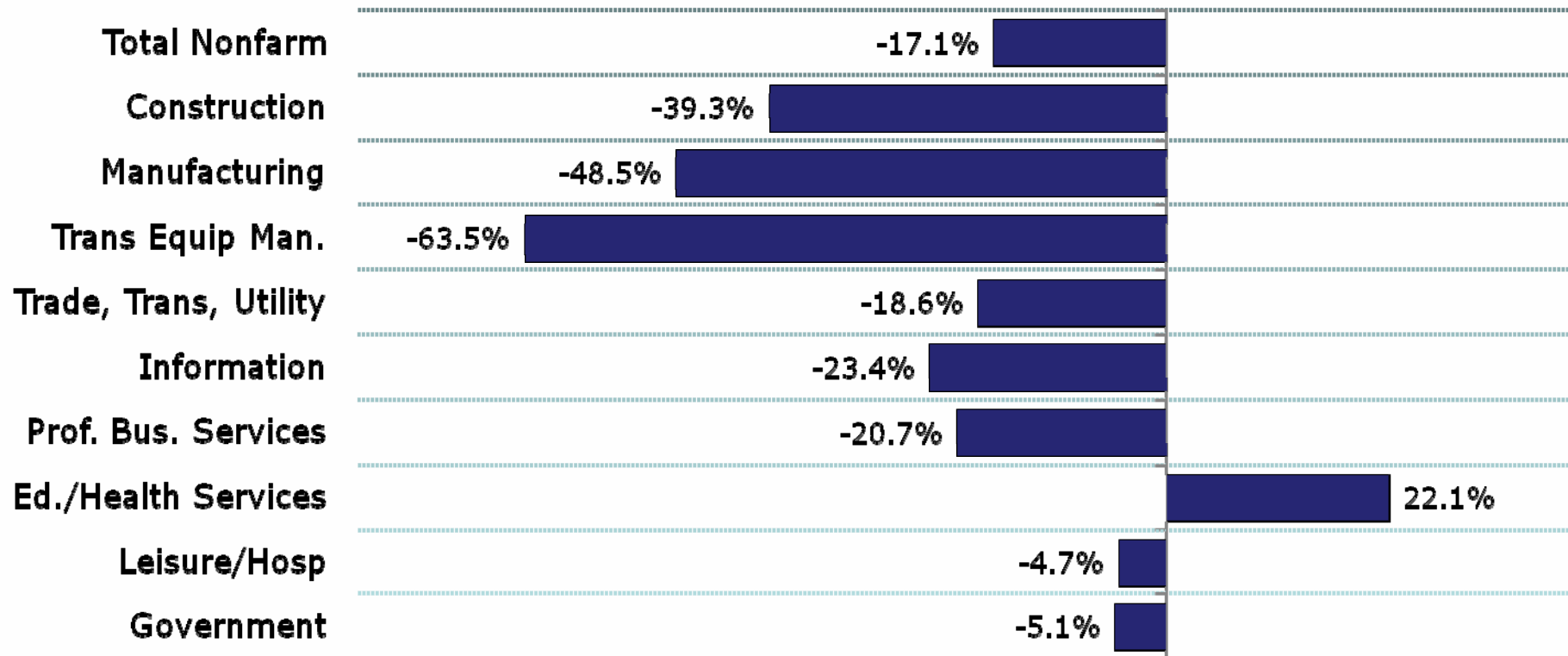
Michigan's Manufacturing's Footprint Now Significantly Smaller

| | <u>2001 Q3</u> | <u>2009 Q3</u> | <u>% Change</u> |
|----------------------------------|----------------|----------------|-----------------|
| Number of Establishments | 17,924 | 14,135 | -21.1% |
| Number of Employees | 810,594 | 455,667 | -43.8% |
| Total Wages Paid (000 \$) | \$9,528,420 | \$6,431,979 | -32.5% |



Almost Every Sector in Michigan Has Lost Jobs

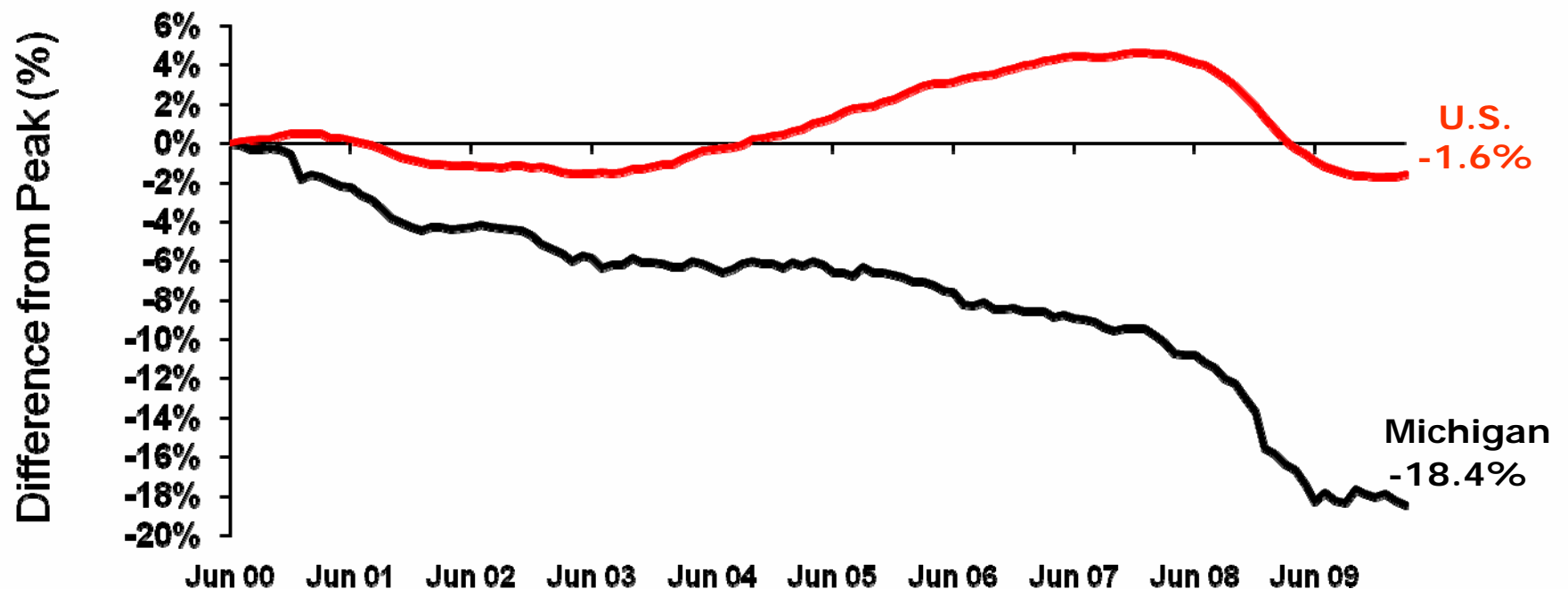
2000 to 2009





A Lost Decade of Michigan Employment

1 in 6 Jobs Lost Since June of 2000



- 9 Note: Peak is calculated from Michigan's June 2000 Peak. Data are through March 2010.
Source: Bureau of Labor Statistics and CRC calculations.



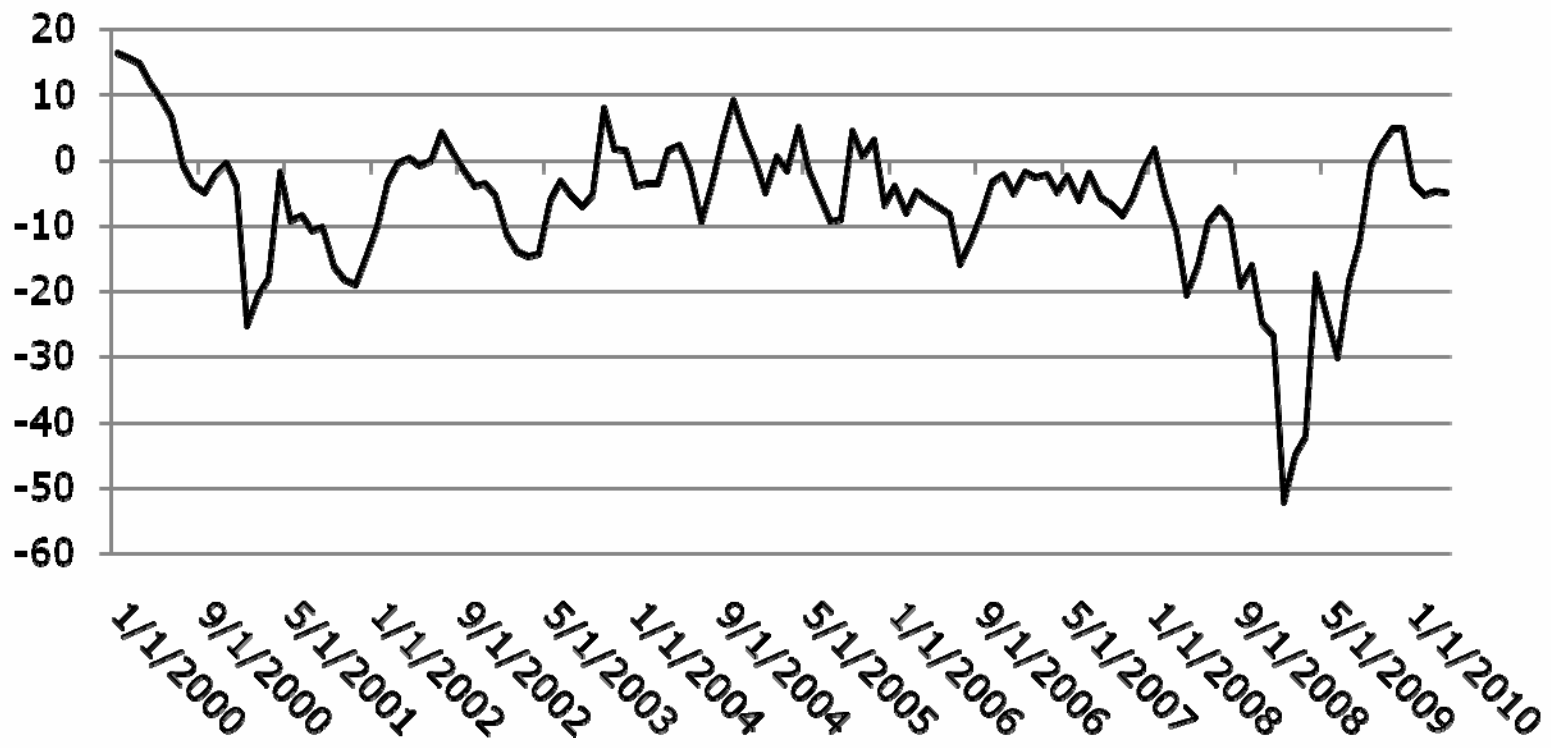
Unemployment is Widespread in Michigan

| | Mar/Apr 2010 Unemployment Rate |
|-----------------------------|---|
| Statewide (Apr) | 14.0% |
| Detroit MSA (Apr) | 15.0% |
| City of Detroit (Mar) | 25.3% |
| Grand Rapids MSA (Mar) | 12.8% |
| City of Flint (Mar) | 27.0% |
| Grand Traverse County (Mar) | 15.3% |
| Marquette County (Mar) | 12.1% |



Michigan Job Losses are Starting to Abate

Monthly Change in Michigan Employment (3 month avg. thousands)

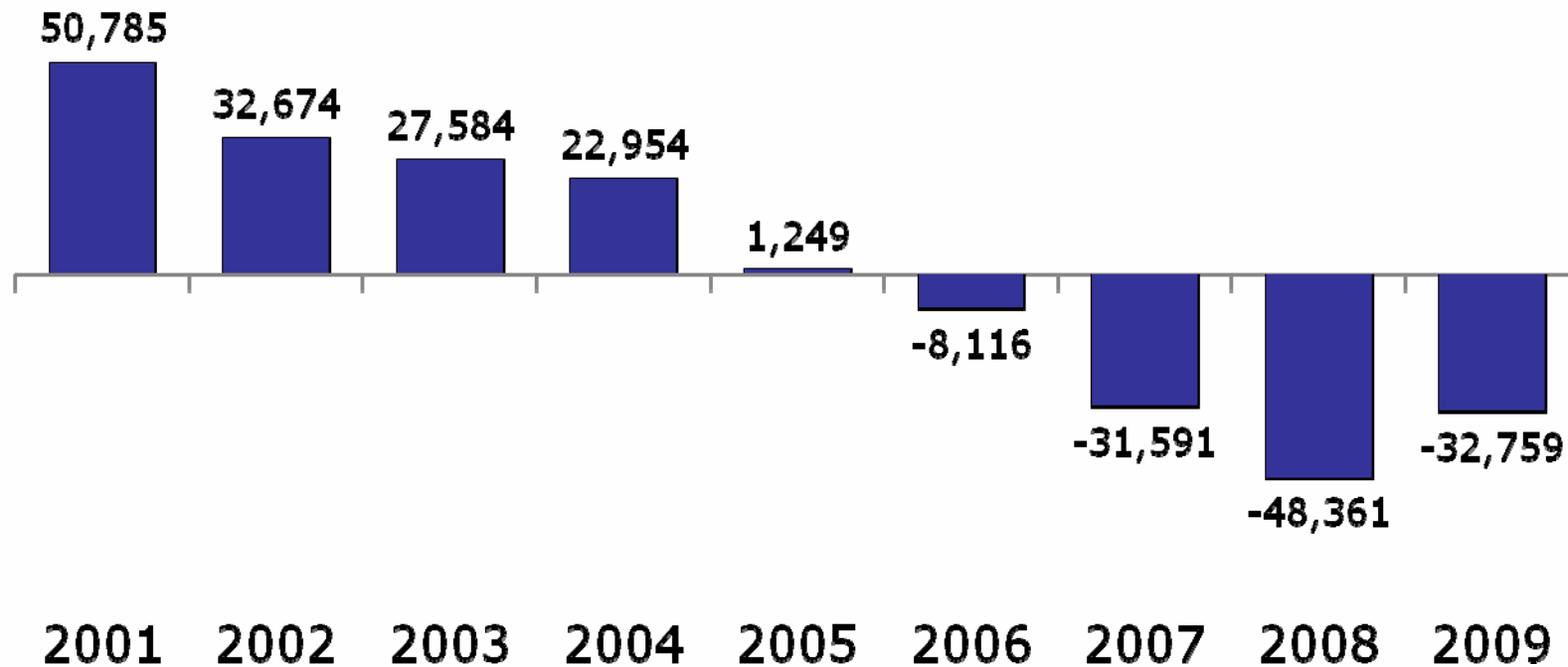




Michigan's Population is Declining

Population Has Declined by 120,000 Since 2005 (Population of Flint is 112,900)

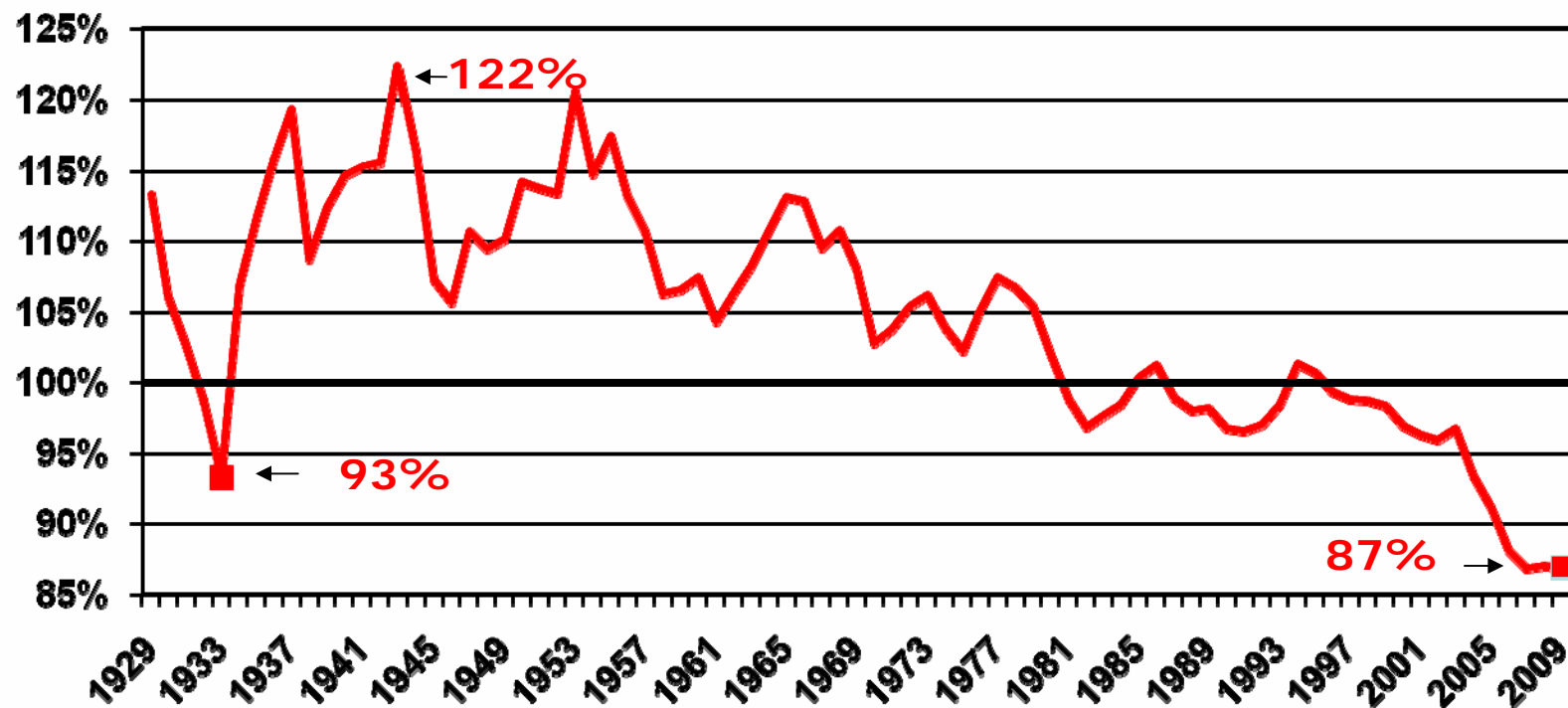
Annual State Population Change





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 20th in 2001 to 37th in 2009





What Does This Mean for the Budget?



FY 2000 to FY 2010 Budget Changes

- Inflation up approx. 23%
- Total state spending up 22.5% but increases in federal aid drove increase; state spending from state sources up 2.3%
- Spending changes from state sources:
 - K-12 +8.2%
 - Community Colleges +0.7%
 - Universities/financial aid -13.7%
 - Revenue sharing -34%
 - Corrections +27.2%
 - Medicaid +49.9%



Revenues Crash in 2009

Annual Growth Rates

| | <u>FY 2009</u> | <u>Projected FY 2010</u> | <u>Projected FY 2011</u> |
|--------------------------|----------------|------------------------------|------------------------------|
| Sales Tax | -10.1% | 1.3% | 1.5% |
| Income Tax | -19.0% | -8.1% | 2.9% |
| Use Tax | -19.0% | 3.6% | 1.5% |
| State Education Tax | -1.9% | -7.2% | -3.2% |
| Real Estate Transfer Tax | -26.2% | 1.4% | 10.2% |
| GF-GP | -21.3% | -9.6% | 6.6% |
| School Aid | -5.1% | -1.6% | 0.8% |



FY2010 GF Cuts Were Severe

- Medicaid provider rates (cut 8% from original FY2009 level)
- Non-Medicaid CMH funding (\$40M cut)
- Elimination of \$238M from DHS budget
- Revenue Sharing to CVTs down 9.7%
- State employee concessions/layoffs (varied)
- Average of -8.4% cut (GF-GP) across all state departments
 - Some larger than others
 - Some areas protected from cuts per ARRA
- Scholarships to university students cut by two thirds (incl. elimination of Promise Grants)



FY 2010 Had Significant School Aid Cuts

- Ongoing FY 2010 SAF revenues projected to be \$1.0 billion below FY 2008
- Enacted FY 10 Cuts:
 - \$165 per pupil (\$263M)
 - ISD reduction (\$16M)
 - 20j veto (\$52M)
 - Other Cuts (\$35M)
- Proposed proration \$127 per pupil (\$212M) was rescinded



Stimulus Spending Has Been Supporting State Budgets (millions of \$)

| | <u>FY 2009</u> | <u>FY 2010</u> | <u>FY 2011 CSB</u> |
|----------------------|----------------|----------------|--------------------|
| Total GF-GP Spending | \$9,753.7 | \$9,151.8 | \$9,176.7 |
| ARRA | \$1,298.1 | \$1,071.3 | \$209.6 |
| ARRA % of Budget | 13% | 12% | 2% |
| | | | |
| Total SAF Spending | \$13,139.6 | \$12,715.5 | \$12,773.9 |
| ARRA | \$597.5 | \$450.0 | \$185.5 |
| ARRA % of Budget | 5% | 4% | 1% |



Governor's Proposal for FY 2011

Mix of Short- and Long-Term Fixes for GF

- Spending cuts (\$433M)
 - Corrections reforms (\$129M)
 - Retirement system changes (\$98M)
 - Private college scholarships (\$32M)
 - Rescind non-union pay bump (\$18M)
 - Community Health (\$39M)
 - Human Services (\$39M)
- Non-recurring resources
 - Continuation of Medicaid match rate - \$500M – **requires yet to be enacted federal legislation**
- 20 • Medicaid provider tax on physicians - \$100M



Gov's FY 2011 SAF Solution

- Original Estimates put shortfall at \$422 million for FY 11
- Tax Restructuring – two parts
 - Expand sales tax base to group of services @ 5.5%
 - Reduce existing rate of sales and use taxes to 5.5%
 - Net effect: \$729M
- Begin two-year elimination of Michigan Business Tax Surcharge
 - Net effect: (\$174M)
- Overall: \$554M to avert \$250 per-pupil reduction
- By 2014 there is no net new revenue from proposal
- **Revenue estimating adjustments made on May 21st eliminated the shortfall for FY 11**
- **Retirement changes save \$680M in FY 11 and \$3.2B over next ten years**



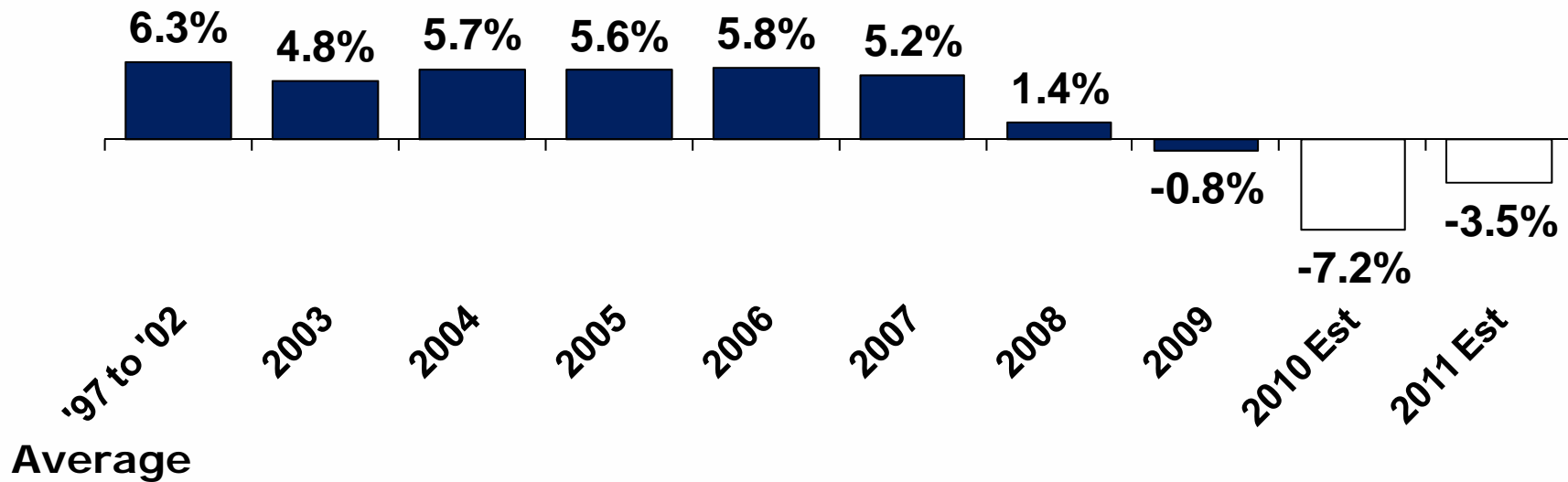
Local Tax Revenues Have Held Up Relatively Well Until Now

- To date, local property tax has helped to provide stability to local government revenue picture ~ 5% growth/yr ('00 – '07) and flat in 08 and 09
 - Going forward, this picture changes dramatically
 - Taxable value falls in 2010 and 2011
 - State revenues will not be positioned to help
- Coming out of the downturn, tax value growth capped (Prop. A) – restrains revenue growth
- Local cuts are coming and will be much more visible than many state cuts



TV Growth Provided Stability But Taxable Value Now Falling

% Change in Total Taxable Value





Significant Policy Issues Facing Michigan



Local Government Fiscal Issues

- How can we increase collaboration among local governments (or otherwise increase the efficiency of government service provision)?
- What (if anything) should be done to address employee legacy costs?
- Many local governments are in dire fiscal straits. Should state government be doing more to help struggling cities?
- Is PA 72 adequate to address local governments in a fiscal emergency?
- How should the state respond if a local government with an emergency financial manager runs out of cash or contemplates bankruptcy?



State Tax Structure

- Should the state's tax structure be reformed?
- Potential areas for reform:
 - Base significantly smaller due to economic contraction and does not support current spending – should taxes be increased or should government expenditures be reduced?
 - Major taxes (sales, income, property) not expected to grow as fast as personal income – will put continuing pressure on state and local budgets – should this be addressed?
 - Should the structure be modified to improve the potential for economic development?



Public Employee Costs

- Cost of public employees has been rising due to rising healthcare costs for current and retired employees while revenues have been declining (avg cost per state employee up 59% this decade)
- Public schools, state government, and many local governments have significant unfunded retiree healthcare liabilities
- Should an attempt be made to pre-fund these liabilities at a time when spending on other priorities is being reduced?
- Should pay and/or benefits for active and retired public workers be reduced?



Economic Development

- Michigan's 18% employment decline makes economic development of critical importance
- Is there a role for government in economic development?
- If government does take an active role is it better to have lower taxes and less regulation, or to invest in key areas such as education or quality of place measures (i.e. art, parks, public transportation)?
- Are targeted tax credits more effective at increasing investment than broader tax policy changes?
- Should government be targeting particular industries (e.g. film industry, battery manufacturing)?



How Do We Start to Think Longer Term?

- Economy starting to grow, **but there is no quick recovery from an 18% employment decline**
- Spending, primarily due to healthcare costs, poised to grow faster than revenues over long-term
 - Gap is 1.7% per year on average in SAF
 - Gap is 5.4% per year in GF-GP, exacerbated by scheduled tax cuts, esp. IIT rate cut
- Huge budget gap will reappear in FY 2012 due to loss of stimulus funds and IIT rate cut
- Michigan's problems are long-term and structural we need to start thinking and planning longer-term



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