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Michigan ECONOMIC BULLETIN

The Good News

- The April **U.S. consumer price index** was up at a seasonally adjusted rate of 0.2 percent, following the March decline of 0.1 percent; excluding food and energy, the index still went up 0.2 percent in April, and March's dip of 0.1 percent becomes an increase of 0.1 percent.

- The **Detroit CPI** (unadjusted for seasonal variation) rose to 131.7 in April, up 3.8 percent from last April.

- The U.S. Commerce Department announced that **retail sales** were down slightly—0.1 percent—in April but revised the March figure from a drop of 0.8 percent to a 0.4 percent increase. Sales of building materials, furniture, and automobiles all were up in April.

- **Nonfarm employment** shrank by 124,000 jobs in April, well below the 221,000 average decrease in the previous six months. There were 42,000 fewer manufacturing jobs (compared to a decline of 93,000 in March), but motor vehicle manufacturers added 13,000 jobs.

- The **merchandise trade deficit** declined to a seasonally adjusted $4 billion in March, down from the February figure of $5.5 billion. Exports rose $0.4 billion (to $34 billion) and imports dropped by $1.1 billion (to $38 billion).

The Bad News

- April **motor vehicle sales** sagged 16.3 percent below the year-ago level. Domestic passenger car sales sank 21.7 percent to an annual rate of 5.5 million units, the lowest in more than eight years. Big Three sales slumped almost 25 percent, while import sales dropped 14 percent. Japanese producers enlarged their share of the market to 31 percent from 27 percent a year ago. Truck sales dropped 19.4 percent from the April 1990 level.

- April **housing starts** stood at a seasonally adjusted annual rate of 957,000 units compared with 901,000 in March, but this was 21 percent below the April 1990 figure of 1,217,000. Authorized **housing permits** were at a seasonally adjusted annual rate of 865,000 in April, 3 percent below the revised March rate of 892,000 and 23 percent below the revised year-ago figure of 1,123,000.

- April's **producer price index** was 0.2 percent higher (seasonally adjusted) than the March figure. Energy prices declined 0.3 percent, versus a 3.9 percent average decline in the previous four months.

- **Consumer installment debt** declined in March for the fourth consecutive month; excluding the credit control period of 1980, installment debt has not fallen for four straight months since the 1958 recession.

- Real average **weekly earnings** dipped 0.1 percent in April, due both to fewer hours worked and rising inflation. Since April 1990 real weekly earnings have sagged 2.2 percent, real average **hourly earnings** were down an average 1.3 percent from year-ago levels.

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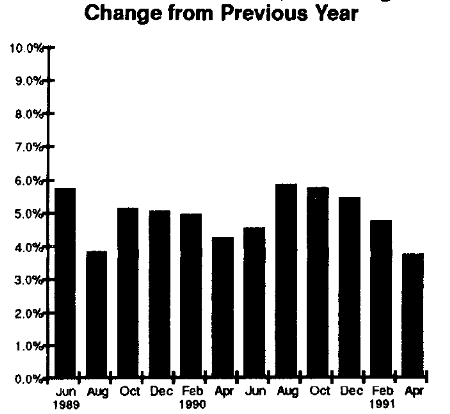
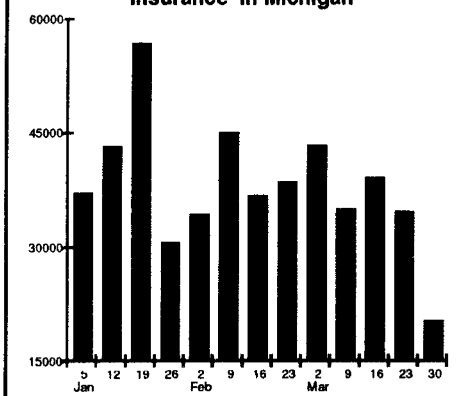
MICHIGAN ECONOMIC INDICATORS

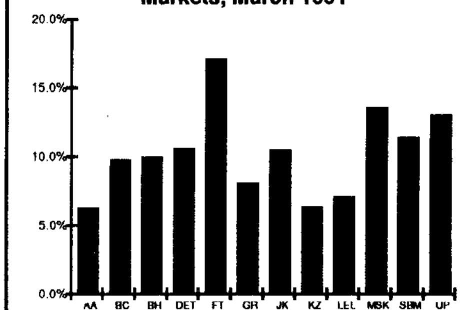
Detroit-Ann Arbor CPI-U, Percentage Change from Previous Year



Initial Weekly Claims for Unemployment Insurance in Michigan



Unemployment Rates in Michigan Labor Markets, March 1991



AA: Ann Arbor; BC: Battle Creek; BH: Benton Harbor; DET: Detroit; FT: Flint; GR: Grand Rapids; JK: Jackson; KZ: Kalamazoo; LEL: Lansing-East Lansing; MSK: Muskegon; SBM: Saginaw-Bay City-Midland; UP: Upper Peninsula.

SOURCE: U. S. Bureau of Labor Statistics and MESC, Bureau of Research and Statistics.

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Michigan Personal Income

The Bureau of Economic Analysis, U.S. Department of Commerce, recently released 1990 fourth-quarter and annual average personal income statistics for Michigan. The data show that the recession hit our state harder than the nation as a whole. In 1990 total personal income in Michigan was $170.5 billion, a 4.9 percent increase from the previous year but not as favorable as the national figure, which rose by 6.4 percent to $4.6 trillion. After adjusting for inflation, the news was even worse: Michigan real personal income was down 0.3 percent in 1990; nationally, there was a 1.1 percent gain. This was the first decline in Michigan's real earnings since the 1982 recession.

Comparing Sectors

Michigan **farming** suffered the largest percentage quarterly income declines in 1990: 24 percent in the second quarter and 19 percent in the third. (This did not contribute significantly to the overall income decline, however, because farm income accounts for only 0.6 percent of the state total.) **Manufacturing earnings**—which account for 23.2 percent of total earnings in Michigan—fell 4 percent in the final quarter, caused by decreases both in **durable** and **nondurable** goods (down 4.3 percent and 2.9 percent, respectively). Likely the result of layoffs in the automobile industry, annual manufacturing earnings were down 2.4 percent in 1990 from the previous year (see exhibit). The state **construction** industry was hit hard as well, experiencing declines of 1.5 percent in the third quarter and 4.3 percent in the fourth; this was better than the national industry, however, which experienced declines all year. State construction earnings were down 1.1 percent from 1989 levels, due to lower employment.

The news was not all bad, however. First, no sector experienced income declines every quarter, and only two—construction and durable goods manufacturing—fell below their 1989 average. Annual average earnings went up in all other sectors, ranging from jumps of 11.8 percent (**government**) to 0.8 percent (nondurable goods). Second, three sectors posted quarter-to-quarter gains in each period surveyed: finance, insurance, and real estate; services; and government. Finally, income gains in the **finance, insurance, and real estate** sector outpaced those at the national level, posting rates of increase as compared to the national sector, which recorded smaller gains in the second and third periods and a decline of 0.1 percent in the fourth quarter.

Conclusions and Implications

The deterioration of state personal income relative to the nation is not surprising, as this has been the trend for at least ten years. It reflects, in part, the shift from a manufacturing-based economy to one increasingly service oriented. In 1980 Michigan personal income accounted for 4.2 percent of the national total; by 1990 it had declined to 3.7. During the same period manufacturing jobs declined from about 26 percent of total state employment to slightly more than 21 percent, while service sector jobs rose from approximately 15.5 percent to just under 21 percent. During the current year the number of service sector jobs will likely overtake those in manufacturing for the first time. This change has slowed earnings growth because service sector jobs generally pay less than manufacturing jobs. Michigan, however, continues to rely on the manufacturing sector for earnings; as noted above, manufacturing income accounts for 23.2 percent of total state earnings but only 13.8 percent of U.S. earnings.

This switch has several implications: (1) Unless another high-earnings employment sector emerges, the state's standard of living will continue to decline relative to the national average. (2) The state's tax base will continue to erode, and unless levies are increased and/or the tax base broadened, the state will be unable to support spending at past levels.

Annual Michigan and U.S. Personal Income and Wages, Selected Years (dollars in millions)

	Total Personal Income		% Change from Previous Year, Adjusted for Inflation		Michigan Income as a % of U.S. Total
Year	Michigan	U.S.	Michigan	U.S.	
1980	$94,080	$2,254,076	–6.5%	–0.2%	4.2%
1982	101,228	2,663,432	–3.0	–0.3	3.8
1984	118,047	3,101,163	6.5	5.1	3.8
1986	135,372	3,552,203	5.0	5.2	3.8
1988	151,996	4,058,181	3.2	3.6	3.7
1990	170,534	4,647,055	–0.3	1.1	3.7

SOURCES: Calculations made by PSC based on data from Bureau of Economic Analysis, U.S. Department of Commerce, "State Personal Income: 1929–87" (Washington, D.C.: the Bureau, July 1989); and Bureau of Economic Analysis.

Legislation, the Budget, and Cash Flow

Capital Acquisition Deduction On May 16 the Senate passed legislation to amend the state single business tax (SBT) by replacing the capital acquisition deduction (CAD) with a site-specific (property) tax credit and phasing in a new SBT apportionment factor beginning in 1993. (The bill currently is in the House Taxation Committee.) In February the CAD was ruled unconstitutional by the Michigan Court of Appeals; on April 30 the court refused to reconsider its ruling, thereby eliminating language from the SBT allowing the CAD to be applied differently to in-state and out-of-state companies. With no replacement legislation, quarterly SBT collections in April plummeted because many firms began fully deducting both in-state and out-of-state capital acquisitions from their tax liability. This resulted in a substantial cash flow problem for the state.

The Senate bill—SB 69 (S-13)—would grant businesses an SBT credit on Michigan-based property beginning with the 1990 tax year. For 1990 taxpayers could use either a two- or three-factor apportioned CAD; for 1991 the proposal would allow a 2.5 percent credit on Michigan-based depreciable personal property and would raise the gross receipts threshold (for filing an SBT return) from $40,000 to $60,000; for 1992 and thereafter the tax credit would be 2.55 percent, the gross receipts threshold would be $100,000, and the SBT rate would drop to 2.3 percent. For 1993 the phase-in of a double-weighted sales apportionment factor of the SBT would begin. The total tax savings to business is estimated at $117 million by 1994, compared to the estimated $500 million annual revenue loss that would result from continuing to allow a full deduction for in-state and out-of-state capital acquisitions.

The Budget Negotiations to resolve the current year fiscal crisis again have ground to a halt. The main sticking points are between the administration and House Democrats and involve the Department of Social Services, specifically whether (1) most of the General Assistance (GA) program will be eliminated, (2) AFDC will be cut to minimum federal levels, and (3) foster care payments will be reduced. The Senate and Governor Engler have acted separately to try to settle the state's financial problems.

The Senate approved two House bills—HBs 4136 and 4137—that would provide incentives to school districts to repay their bond debt early and by direct deposit to the general fund; the savings are estimated to be $112 million the first year. Also enacted were HBs 4150 and 4104. The former allows a $222.5 million withdrawal from the Budget Stabilization Fund and provides for changes in homestead property tax credits that would result in $366 million in additional state revenue; the bill also mandates a joint annual state revenue-estimating conference. HB 4104 provides one-time revenues of $55 million by accelerating the timing under Michigan escheats law by which monies in the fund revert to the state. All except HB 4104 will not go into effect until 1992, although State Budget Director Patricia Woodworth believes that she can implement the changes for the current fiscal year. Bills (SBs 342 and 343) analogous to HBs 4136 and 4137 have been introduced in a second attempt to pass the legislation with immediate effect.

Bypassing the legislature altogether, Governor Engler obtained approval of the State Administrative Board for interdepartmental transfers of more than $200 million. One transfer would shift $60 million from GA benefits to Medicaid, which could run out of funds by late summer; the Medicaid account would receive a total of $76 million as a result of transfers. Although the governor claims that the board's action is legal, House Speaker Lewis Dodak is fighting it in court.

Cash Flow Because of the legislature's tardiness in dealing with the CAD problem, as well as the still unresolved budget situation, State Treasurer Doug Roberts said that the state cash shortage is "very critical." As a consequence, in each of the next several months K–12 school districts, higher education institutions, and local governments will receive split aid payments: Part of each disbursement will be deferred three to four weeks. This will force many school districts and local governments to borrow funds to meet their commitments.

In testimony before the Senate Finance Committee, Mr. Roberts argued in favor of legislation (SBs 236, 237, 276, and 277) to help alleviate the problem by speeding up collections of state sales, use, and income withholding taxes. Revenue collections from large businesses would be made by direct deposit and/or electronic funds transfer; penalties for late payments would be increased. The Treasury Department estimates that these changes would earn the state an additional $19 million annually. Collection fees paid (actually discounts allowed) to large companies making early sales and use tax payments could rise from their current range of .50–.75 percent of collections; the treasurer is not adverse to an increase but opposes going beyond one percent because the state could borrow necessary funds at a lower taxpayer cost.

Mr. Roberts also advocates changing the disbursement of aid to schools and higher education institutions by spreading payments over the course of the year.

Michigan Revenue Report

April revenue collections (March activity) were the weakest in memory. Total general (GF) and school aid fund (SAF) revenues fell about 10 percent from the year-ago level.

Personal income tax collections declined 8.1 percent from the April 1990 level. This almost certainly is due to a collection aberration, as economic activity points to a one to two percent increase. This weakness was offset partially by a sharp jump (9.5 percent) in quarterly and annual payments.

Sales and use tax collections declined 0.4 percent—about in line with recent experience. Motor vehicle collections fell 15 percent, as expected. Excluding these components, sales tax collections increased 2.4 percent, about the amount expected given the current level of economic activity.

The single business tax is in disarray due, in large part, to the court decision in the *Caterpillar* case, which expanded the capital acquisition deduction to out-of-state investments. As a result, multistate firms are filing on this basis and reducing their state tax payments. Legislation to resolve this problem is in process, but, meanwhile, April SBT collections were 34.7 percent below the year-ago level. This sharp decline may overstate the magnitude of the problem, however, because payments for this quarter were due April 30, and a change in the collection pattern can distort monthly comparisons. Other causes of the weakness in SBT collections are large automobile manufacturers' losses and insurers exercising their option to pay the retaliatory tax instead of the SBT; retaliatory collections doubled during the first six months of the fiscal year.

Lottery collections rebounded in recent months due to several large Lotto jackpots, and preliminary figures suggest that April sales were up 16.7 percent from a year ago. For the first time this fiscal year, year-to-date collections are slightly ahead of last year.

Public Sector Consultants has been projecting an increase of about one percent in GF/GP and SAF revenues for FY 1990–91, roughly $100 million less than the administration's current estimates. Year-to-date collections now are running 2.2 percent below the year-ago pace, and although this decline may be slightly overstated due to temporary factors, it appears unlikely that revenues will reach our current estimate. We are revising our projection of the revenue shortfall to $125 million.

MONTHLY TAX COLLECTIONS (dollars in thousands)

Type of Revenue	Preliminary April 1991	% Change from Last Year	Past 3 Months' Collections	% Change from Last Year	FY 1990–91 Year-to-Date	% Change from Last Year
Personal Income Tax						
Withholding	$346,356	–8.1%	$1,007,147	0.1%	$2,140,089	1.7%
Quarterly and Annual Payments	239,883	9.5	308,405	17.7	443,468	5.1
Gross Personal Income Tax	586,239	–1.7	1,315,552	3.8	2,613,557	3.5
Less: Refunds	–288,493	9.5	–722,178	11.1	–763,172	9.4
Net Personal Income Tax	297,746	–10.5	593,374	–4.0	1,850,385	1.2
Sales and Use Taxes	251,676	–0.4	702,561	0.2	1,536,496	0.6
Motor Vehicles	34,686	–15.0	90,031	–18.8	192,004	–9.8
Single Business Tax	128,775	–34.7	368,776	–9.3	793,396	–6.7
Cigarette Tax	19,899	–9.1	58,108	–4.2	124,258	–1.0
Public Utility Taxes	0	—	10	NM	71,666	2.6
Oil and Gas Severance	4,123	5.8	11,955	2.7	26,257	13.0
Lottery[a]	44,646	16.7	126,883	6.3	284,190	0.9
Penalties and Interest	951	NM	19,612	60.3	39,174	28.8
SUW—Annuals and Undistributed[b]	3,850	62.4	14,969	7.1	24,893	55.7
Other Taxes[c]	79,461	4.2	155,419	14.8	237,795	12.1
TOTAL TAXES (GF & SAF)[d]	$831,127	—10.2%	$2,087,745	–1.5%	$4,988,510	0.4%
Motor Fuel Tax[e]	$54,999	–0.5%	$162,568	–1.1%	$331,577	–1.6%

SOURCE: Data supplied by Michigan Department of Treasury.
NM = Not meaningful
[a]The state share of lottery collections is estimated to be 40.7 percent, based on the average profit to the state for the fiscal year 1989–90. The previous year's figures are adjusted to the current year's profit margin; the percentage change reflects the increase in ticket sales.
[b]These revenues are distributed to the sales, use, and withholding (SUW) accounts when final numbers for the month are reconciled.
[c]Includes intangibles, inheritance, foreign insurance premium, corporate organization, and industrial and commercial facilities taxes.
[d]Excluded are beer and wine, liquor, and horse racing taxes, which are not collected by the Department of Treasury.
[e]The motor fuel tax is restricted to the Transportation Fund.

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