Gerald Faverman, Ph.D. • *Chairman of the Board*
Robert J. Kleine and Frances Spring • *Editors*
Vol. 1, No. 9 • November 1991

Public Sector Reports

Michigan ECONOMIC BULLETIN

The Good News

➤ Led by gains in the manufacturing sector, U.S. **labor productivity**—output per hour of work—rose by 2.4 percent in the third quarter, the first gain posted since the third quarter of 1990. This follows a second-quarter revised drop of 0.3 percent.

➤ **Interest rates** continue their descent: On November 5, the Federal Reserve lowered the discount rate (the rate it charges on loans to member banks) from 5 to 4.5 percent (the lowest since 1968), and induced a drop (from 5 to 4.75 percent) in the federal funds rate (the rate member banks charge one another on short-term interbank loans) for the second time in less than a month. Large banks have responded by lowering their prime rate (from 8 to 7.5 percent), which could result in credit expansion and a spurt in spending.

The Bad News

➤ Despite discounts and the lure of the new model year, **October motor vehicle sales** remained weak, falling 10 percent from the year-ago level. During the same period, domestic auto sales were down 12.7 percent, while truck sales declined 7.7 percent. Among the Big Three, only Chrysler showed an improvement over last year's mark, with total vehicle sales up 3.3 percent from October 1990. GM sales were down 11.5 percent; Ford sales declined 15.8 percent. In response, the Big Three intend to cut **fourth-quarter production** a combined 130,000 units from previously planned levels.

➤ **Michigan wage and salary employment** continued weak in the second quarter of 1991, declining 2.4 percent from the year-ago level to 3,864,000. September employment improved slightly, falling only 1.8 percent below the level posted in September 1990.

➤ The national index of **leading economic indicators**, designed to foretell the state of the economy in the next three to six months, declined by 0.1 percent in September, the first dip since January.

➤ Following August's revised 4.1 percent decline, **orders for durable goods** fell again in September, by 3.9 percent. Excluding the volatile transportation equipment category, orders rose a minimal 0.9 percent for the month.

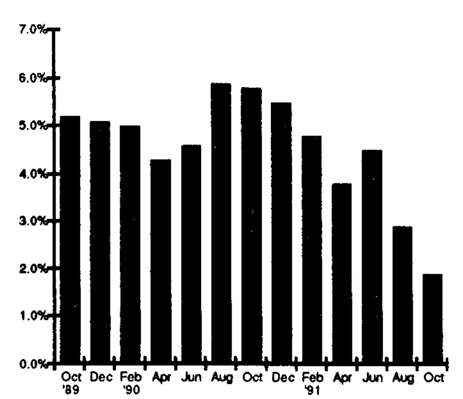
➤ After no change in August, **industrial output** rose a scant 0.1 percent (seasonally adjusted) in September. The manufacturing-only component (durable and nondurable goods production), rose 0.5 percent, in part due to an 8 percent gain in **motor vehicle production**.

➤ Despite the 2.4 percent annual increase in third-quarter **GNP**, negative factors outweighed the positive. Most of the gains occurred in July and August, and in the export sector the deficit increased from \$12.6 billion to \$32.8 billion. Exports rose a meager 0.1 percent.

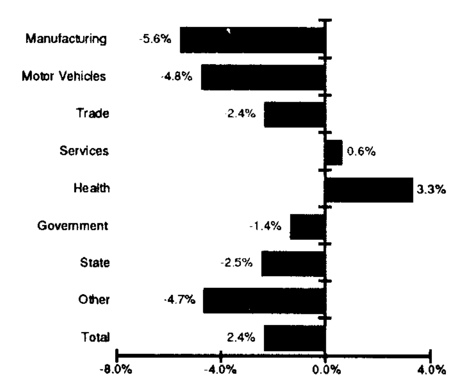
IN THIS ISSUE

MICHIGAN ECONOMIC INDICATORS

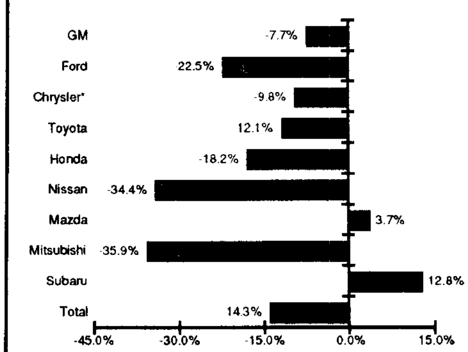
Detroit-Ann Arbor CPI-U (percent change from previous year)



Michigan Wage and Salary Employment (percentage change from year-ago quarter)



Early November Sales of Domestically Produced Cars (percent change from year-ago period)



* Total vehicle sales

SOURCES: Bureau of Labor Statistics.

Public Sector Consultants, Inc.
Knapp's Centre • 300 S. Washington Sq • Suite 401
Lansing, MI 48933-2134 • (517) 484-4954

Another Year Older and Deeper in Deficit/Debt

The FY 1991 federal government deficit reached a record high of $268.7 billion, breaking the 1986 red-ink record of $221.3 billion. The most recent deficit figure was lower than the levels projected earlier by both the White House and the Congressional Budget Office (CBO) due to the delayed sale of assets held by the deposit insurance funds in charge of handling the savings and loan (S&L) and bank bailouts. These assets are still on the FY 1991 books; once the sales are made, however, losses on the sale of those assets will swell the deficit in the year in which the transactions are recorded, many in the next fiscal year. Indeed, the White House has projected that the FY 1992 deficit will total $348.3 billion, a one-year increase of nearly $80 billion.

The lower than expected FY 1991 figure also helped to mask the extent of the deficit problem in terms of the total economy, namely its share of total production, or gross national product (GNP). The deficit as a percentage of GNP is important, as it measures the degree to which the nation's productive capacity is encumbered by debt. In FY 1991, the deficit accounted for 4.8 percent of the nation's GNP, a rise of 17 percent from last year's figure but below the 6.3 percent record set following the end of the last recession in 1983. (Refer to Exhibit 1.)

The deficit also has added to cumulative government debt: The nation's debt is now near $3.5 trillion. (Refer to Exhibit 2.) To pay off such an amount would require every person in the United States to remit $14,000 to the federal government. The government share (federal, state, and local governments) of total debt (including government, business, and individual obligations) has been rising at a rapidly increasing pace. For example, private debt increased by $345 billion *more* than government debt in 1989 and by $119 billion more in 1990. Through the third quarter of FY 1991, however, government debt expanded by $79 billion more than debt in the private sector. Government debt now accounts for 36 percent of all debt; it was only 30 percent in 1980.

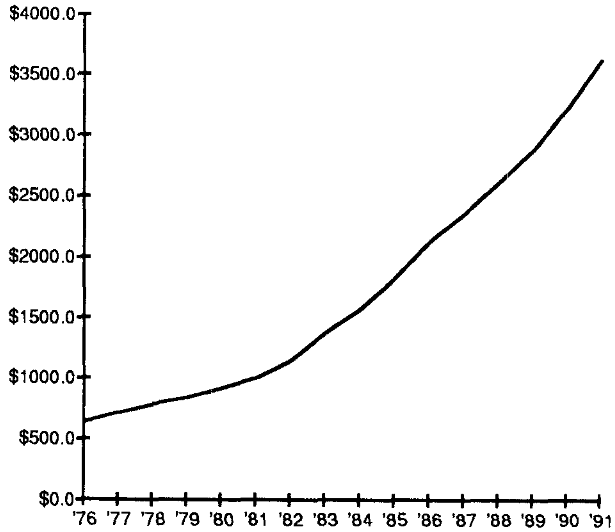
Rising national debt is not necessarily a problem during recessionary periods. Business and personal loan demand generally decline heading into and during a downturn, while government borrowings rise. During this recession, however, the recent run-up in debt, for the most part, has not been the type that would stimulate economic activity and growth. Instead, debt has grown as the government transfers the obligations of failed financial institutions off private sector books and onto the government's ledgers. While the government takeover of failed banks and S&Ls does prevent further questionable loans from being extended, it does not add to national output or stimulate economic growth, which is the theory behind expansionary fiscal policy. Moreover, the massive additions to the national debt over the last decade make it increasingly difficult for the economy to recover from recession. During an upturn, business and personal loan demand rise, yet government borrowing shows no signs of abating; this could exacerbate the existing credit crunch.

EXHIBIT 1

Federal Deficit as a Percentage of GNP, FY 1976–FY 1991

EXHIBIT 2

Total Federal Debt, FY 1976–FY 1991 (dollars in billions)



Stadium Financing, State Pensions, and Supplementals

While the dust has far from settled regarding the FY 1992 budget (see discussion below), the signing of the first round of budget bills has allowed the legislature to turn its attention to other matters. Below are synopses of several bills currently pending in the legislature, as well as an update on budget-related activity.

Stadium Financing Act

House Bill (HB) 5300 would allow Wayne County voters to approve additional taxes to finance the construction of a new baseball stadium in Detroit. The new levies—which would take the form of an excise tax of one percent on hotels and restaurants and 2 percent on rental cars—would be used to retire the county's portion of bond debt incurred to finance the $200 million structure. The tax would raise an estimated $15–18 million per year. There is some question, however, about the constitutionality of the tax; the courts could rule that it is essentially a sales tax on food and beverages, which the legislature is proscribed from authorizing. The bill currently is awaiting action by the full House.

Taxing Government Employee Pensions

A package of bills being discussed in the Senate Finance Committee would tax as income pension benefits received by state workers, including legislative and school employees. Senate Bills (SBs) 131 and 577–579 would impose a 4.6 percent levy on state pension benefits exceeding $7,500 for single filers and $10,000 on joint returns. The revenues from the proposed tax—estimated at $20 million per year—would be used to allow the exemption from taxation of the first $4,500 in interest and dividend income of state residents with no pension benefits.

Senator Nick Smith, Finance Committee chair and sponsor of the legislation, has argued that it is inequitable for state workers to be exempt from such taxes while 70 percent of Michigan residents do not receive pension income and workers receiving private sector pension income remit taxes on those benefits.

Representatives of state government workers' organizations have argued that changing the taxation rules now would be unfair, as contracts were negotiated on the premise that benefits would not be subject to state taxation; others assert that state pension benefits are lower than private sector benefits for just that reason. The bills are being held over in committee to review and resolve questions.

State Budget

Although the preliminary budget bills were signed by the governor in early October, the FY 1992 budget is far from settled (for details of the enacted budget, see our *Public Policy Advisor* "Analysis of Michigan Budget Appropriations," November 4, 1991). Currently pending are three competing supplemental appropriations bills for the Department of Social Services, two of which—SBs 213 and 219—could be decided on as early as the week of November 18. SB 213 is pending in the House Appropriations Committee, SB 219 in a House/Senate conference committee. The third bill, HB 4605, is pending in the Senate Appropriations Committee and is unlikely to be acted on soon, if ever. Additional activity is likely regarding the budget, as it is doubtful that current revenue estimates will match spending targets; our estimate is a budget shortfall of $500–550 million, with a revenue shortfall of about $300 million.

PUBLICATIONS OF INTEREST

Advisory Commission on Intergovernmental Relations, ***Significant Features of Fiscal Federalism, Volume 2: Revenues and Expenditures***, #M-176-II (Washington, D.C.: ACIR, October 1991).

Everything you might possibly want to know about state, federal, and international government expenditures and revenues. Includes (1) current and historical data on spending and revenues, by government level (federal, state, and local), and by revenue and expenditure type on both national income/product account and census bases; (2) tax capacity and tax effort, by state and by tax and revenue type; (3) general statistics (such as population and income data) at the federal and state levels; (4) a new section on government employment and state employee retirement systems, by state; and (5) a special section that includes Medicaid and school finance data. Available for $17.50 from the ACIR, 1111 20th St., N.W., Washington, DC 20575; or call (202) 653-5640.

"State Economic Performance," ***State Policy Reports***, vol. 9, issue 18 (Alexandria, Virginia: State Policy Research, Inc., September 1991), pp. 2–6.

This article provides an index number for each state based on economic momentum and an analysis of the corresponding results. Growth over the past 12 months is based on changes in population, employment, and personal income relative to the national average. Michigan ranked 40th among the states with an index of -0.76. (An index number of zero would reflect a growth rate equal to the national average.)

Michigan Revenue Report

Although the books will not be closed for several weeks, final revenues for FY 1990–91 were collected in October, and one of the worst years ever for the state budget finally has ended. General fund/general purpose (GF/GP) and school aid fund (SAF) revenue declined an estimated one percent from the previous year (adjusted for one-time revenues in FY 1989–90), the first decline since FY 1980–81.

October collections (September activity) offered no sign that revenue growth would improve in the near future (see table below). Personal income tax withholding collections increased 11.9 percent, but this was inflated by an estimated $37 million in accelerated withholding and other adjustments. Excluding this one-time revenue, the increase was only one percent.

Sales and use tax collections also increased one percent, little changed from recent months. Motor vehicle collections rose 0.7 percent, the first increase in a number of months. This "boom" is likely to be short-lived, however, as motor vehicle sales continue to stall. Single business tax collections fell a sharp 13.4 percent in October, but whether this was due to a change in the collection pattern or a weakening economy will not be known until November collections are in.

Lottery collections for FY 1990–91 are complete and show a 5 percent decline from FY 1989–90. The profit to the school aid fund fell 6.7 percent to $456.4 million. October lottery sales continued weak, down 11 percent from October 1990; the past three months' collections are down from last year as well, falling 11.3 percent from the August–October 1990 period.

In last month's *Economic Bulletin* we estimated that GF/GP and SAF revenues for FY 1990–91 would fall $50 million short of the current Department of Treasury estimate of $9,248 million. It now appears that revenue will fall about $100 million below the Treasury estimate.

MONTHLY TAX COLLECTIONS (dollars in thousands)

Type of Revenue	Preliminary October 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	$379,127	1.0%	$1,183,490	1.4%[a]	$4,350,505	1.5%[a]
Quarterly and Annual Payments	12,280	-5.1	123,933	-10.5	752,648	-16.5
Gross Personal Income Tax	391,407	0.9[a]	1,307,423	0.6[a]	5,103,153	0.0[a]
Less: Refunds	-18,305	109.9	-74,081	67.5	-1,153,128	10.6
Net Personal Income Tax	373,102	-2.0[a]	1,233,342	-2.0[a]	3,950,025	-2.8[a]
Sales and Use Taxes	274,547	1.0	806,395	-0.7	3,135,619	-0.5
Motor Vehicles	44,346	0.7	130,415	-6.1	447,262	-10.2
Single Business Tax	134,808	-13.4	420,407	4.8	1,647,074	-9.3
Cigarette Tax	20,379	-2.1	67,473	2.8	256,720	-0.4
Public Utility Taxes	59	0.0	55,314	-11.8	144,956	1.9
Oil and Gas Severance	2,950	-36.1	10,645	-14.4	48,509	5.8
Lottery[b]	88,193	-11.0	111,897	-11.3	456,435	-11.0
Penalties and Interest	1,074	8.8	15,448	103.0	86,737	40.9
SUW—Annuals and Undistributed[c]	3,944	174.3	-1,405	-114.5	22,301	-12.9
Other Taxes[d]	52,213	52.0	84,559	24.2	460,821	27.6
TOTAL TAXES (GF & SAF)[e]	$951,269	-0.8%[a]	$2,890,759	-1.0%[a]	$10,206,088	-1.9%[a]
Motor Fuel Tax[f]	$55,378	0.2%	$179,030	0.3%	$690,053	-0.6%

SOURCE: Data supplied by Michigan Department of Treasury.
NM = Not meaningful
[a]Adjusted to reflect $37 million in accelerated withholding payments.
[b]The state share of lottery collections is estimated to be 41.1 percent (FY 1991). The previous year's figures are adjusted to the current year's profit margin; the percentage change reflects the increase in ticket sales. Lottery collections accrue to the fiscal year in which they are collected; year-to-date collections are therefore equivalent to October revenues.
[c]These revenues are distributed to the sales, use, and withholding (SUW) accounts when final numbers for the month are reconciled.
[d]Includes intangibles, inheritance, foreign insurance premium, corporate organization, and industrial and commercial facilities taxes.
[e]Excluded are beer and wine, liquor, and horse racing taxes, which are not collected by the Department of Treasury.
[f]The motor fuel tax is restricted to the Transportation Fund.

Printed on recycled paper.