ECONOMIC OUTLOOK
AND
REVENUE ESTIMATES
FOR
MICHIGAN

FY 2008-09
AND
FY 2009-10

HOUSE FISCAL AGENCY

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FOREWORD

This report presents final General Fund/General Purpose and School Aid Fund revenue estimates for fiscal year (FY) 2007-08, revised revenue estimates for FY 2008-09, and initial revenue estimates for FY 2009-10. These estimates will be presented at the Consensus Revenue Estimating Conference on January 9, 2009, and will be used to facilitate the consensus estimating process.

Included in this report are House Fiscal Agency (HFA) analyses of important factors that will affect state and national economies through the year 2010, estimates of the Countercyclical Budget Stabilization Fund, state compliance with the Constitutional State Revenue Limit, and year-end balance estimates for General Fund/General Purpose (GF/GP) and the School Aid Fund (SAF).

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EXECUTIVE SUMMARY

The national economic recession began in December 2007 as a mild downturn, but has turned into serious recession. Economic activity is retrenching in all major areas: personal consumption, businesss investment, employment, and foreign economies.

- The combination of declining housing and financial wealth, job losses, and tight credit has led to a significant decline in personal consumption. Personal consumption dropped 3.8% in the third quarter of 2008—the worst decline in 28 years; and light vehicle sales declined from an annual rate of 16.1 million units in CY 2007 to an estimated 10.2 million units in the fourth quarter of 2008—a 36.7% drop.

- Business activity has fallen sharply in both the service and the manufacturing sectors.

- In 2008, nonfarm payroll employment declined by 403,000 in September 320,000 in October, and 533,000 in November—a significant deterioration from average monthly job losses of 82,000 from January through August.

- Exports have declined as foreign countries enter into either subpar growth or recessionary territory.

Changes have been initiated by the Federal Reserve and U.S. Treasury to increase the flow of credit and stabilize the financial markets, but it will take time for the effects of these changes to be felt throughout the economy. In addition to action already taken, it is widely assumed that the next administration will use fiscal policy to stimulate the economy over the next three years; this forecast assumes a $595 billion stimulus package.

The national economy is expected to slow to 1.2% in calendar year (CY) 2008; it is forecast to decline 1.9% in CY 2009 and increase 1.9% in CY 2010. This forecast assumes the current recession will last through the second quarter of 2009, with declines in economic activity and light motor vehicle sales similar to those of the recession in the 1980s.

Michigan's economy and state revenue will be significantly affected by the national recession, the weakened level of motor vehicle sales, the tight credit conditions, and the financial condition of General Motors (GM), Chrysler, Ford, and their suppliers. Significant restructuring, in the form of employment losses and plant closings, is expected to occur in the Michigan motor vehicle sector.

Michigan's wage and salary employment has trended downward since mid-2000; it is expected to decline by 73,400 jobs (1.7%) in CY 2008, decline by 191,700 jobs (4.6%—the worst performance since CY 1982) in CY 2009, and decline by 67,000 jobs (1.7%) in CY 2010.

U. S. Forecast

Real GDP growth is forecast to decrease 1.9% in CY 2009 after increasing an estimated 1.2% in CY 2008. Real GDP is forecast to grow 1.9% in CY 2010.

Inflation, as measured by the Consumer Price Index (CPI), is forecast to decline from an estimated 4.1% in CY 2008 to 0.5% in CY 2009 and 2.5% in CY 2010.

Light vehicle sales, which totaled 16.1 million units in CY 2007, declined to an estimated 13.1 million units in CY 2008 and are forecast to drop to 10.9 million units in CY 2009 before rising to 12.2 million units in CY 2010. The import share of light vehicles is forecast to be 25.6% in CY 2009 and 25.9% in CY 2010.

The national unemployment rate is forecast to be 5.8% in CY 2008, then increase to 8.2% in CY 2009 and 8.7% in CY 2010. The unemployment rate is forecast to peak at 8.8% in the second quarter of 2010.

Interest rates on three-month T-bills are forecast to average 1.4% in CY 2008, then decrease to 0.4% in CY 2009 and 1.0% in CY 2010.

Michigan Forecast

Michigan personal income increased an estimated 2.3% in CY 2008; it is expected to fall 0.9% in CY 2009, and increase 0.9% in CY 2010.

Michigan's unemployment rate is estimated to be 8.4% in CY 2008, and is forecast to be 11.3% in CY 2009 and 11.4% in CY 2010. The unemployment rate is forecast to peak at 11.7% in the first quarter of 2010.

Inflation (as measured by the Detroit Consumer Price Index) for CY 2008 is estimated to be 2.7%; it is forecast to increase 0.2% in CY 2009 and 2.2% in CY 2010.

State Revenue

The preliminary final total baseline GF/GP and SAF revenue was $19.3 billion in FY 2007-08; it is forecast to decrease 4.9% (to $18.4 billion) in FY 2008-09 and 1.3% (to $18.1 billion) in FY 2009-10.

Baseline revenue does not include the impact of partial-year policy changes or certain policy changes that have recently occurred. Baseline estimates are comparable across fiscal years and demonstrate the changes to state revenue that are driven by changes in the economy.

The preliminary final total net GF/GP and SAF revenue was $20.9 billion in FY 2007-08; it is forecast to decrease $1,151.3 million (5.5%) in FY 2008-09. Total net GF/GP and SAF revenue for FY 2009-10 is forecast to be $19.3 billion—a decrease of $399.3 million (2.0%). Net revenue captures the effects of all policy changes and represents resources available.

Table 1 reports GF/GP and SAF revenue in terms of baseline and actual revenue. Preliminary final FY 2007-08 revenue, the recommended revisions to estimates for FY 2008-09, and the initial estimates for FY 2009-10 are reported in **Table 2 and Table 3**.

State Revenue Limit

Total state revenue is expected to be below the state revenue limit by $4.8 billion in FY 2007-08; it is estimated to be under the limit by $6.4 billion in FY 2008-09 and $7.5 billion in FY 2009-10. Final calculation of the state revenue limit is performed by the Auditor General.

Fund Balances

The year-end GF/GP balance is $458.0 million for FY 2007-08.

The year-end SAF balance is $247.0 million for FY 2007-08.

The year-end Countercyclical Budget Stabilization Fund balance is $2.2 million for FY 2007-08; it is estimated to be $2.2 million for FY 2008-09 and $2.3 million for FY 2009-10.

Table 1

HFA REVENUE ESTIMATES

(Millions of Dollars)

	Preliminary Final FY 2007-08	HFA Estimate FY 2008-09	HFA Estimate FY 2009-10
Baseline GF/GP	$8,207.1	$7,749.6	$7,639.7
Baseline SAF	$11,121.4	$10,628.3	$10,505.4
TOTAL BASELINE	**$19,328.5**	**$18,377.9**	**$18,145.1**
Actual GF/GP	$9,359.8	$8,340.4	$8,053.6
Actual SAF	$11,512.9	$11,381.0	$11,268.5
TOTAL ACTUAL	**$20,872.7**	**$19,721.4**	**$19,322.1**

NOTE: Numbers may not add due to rounding.

Table 2

FY 2007-08 HFA PRELIMINARY FINAL REVISIONS

(Millions of Dollars)

	May 2008 Consensus	January 2009 Preliminary Final	Revision
Actual GF/GP	$9,164.1	$9,359.8	$195.7
Actual SAF	$11,375.0	$11,512.9	$137.9
TOTAL ACTUAL	**$20,539.1**	**$20,872.7**	**$333.6**

NOTE: Numbers may not add due to rounding.

Table 3

FY 2008-09 HFA RECOMMENDED REVISIONS

(Millions of Dollars)

	May 2008 Consensus	January 2009 Recommendation	HFA Recommended Revision
Actual GF/GP	$8,884.6	$8,340.4	($544.2)
Actual SAF	$11,707.4	$11,381.0	($326.4)
TOTAL ACTUAL	**$20,592.0**	**$19,721.4**	**($870.6)**

NOTE: Numbers may not add due to rounding.

ECONOMIC REVIEW AND FORECAST

This section presents the economic forecast used by the House Fiscal Agency to produce its revenue forecasts for FY 2008-09 and FY 2009-10.

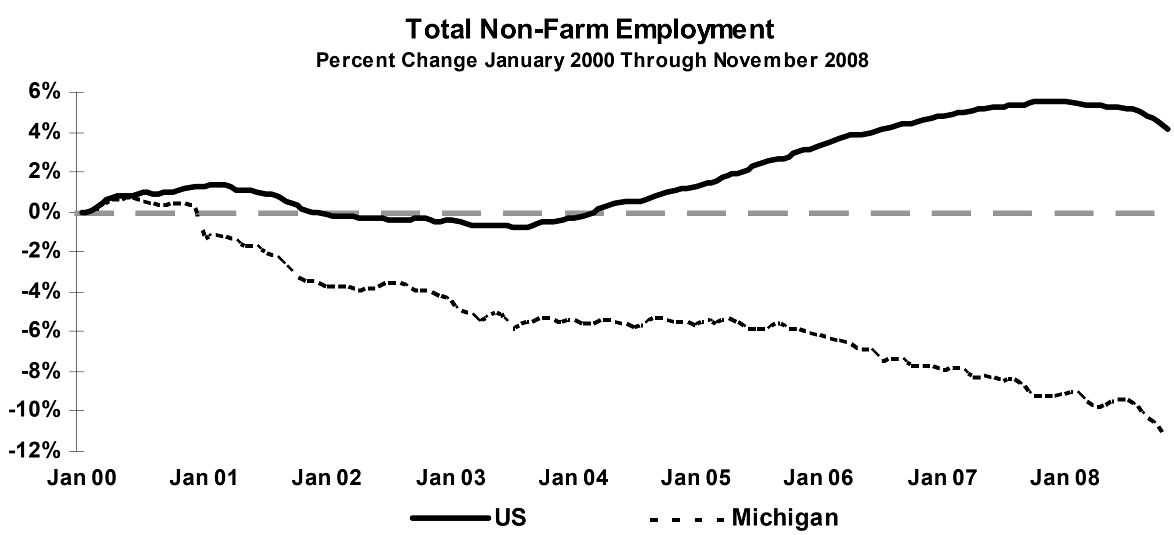
The eight-month national recession that ended in November 2001 was followed by weak economic growth throughout CY 2002 and the early part of CY 2003. As national economic growth improved, so did employment.

Job growth at the national level began to improve during the latter half of CY 2003, and continued its upward trend through December 2007—at which point the national economy officially entered a recession. Since December 2007, employment has fallen each month.

Total Non-Farm Employment

Figure 1 shows the monthly percent change in total non-farm employment for both the U.S. and Michigan from January 2000 through November 2008.

Figure 1



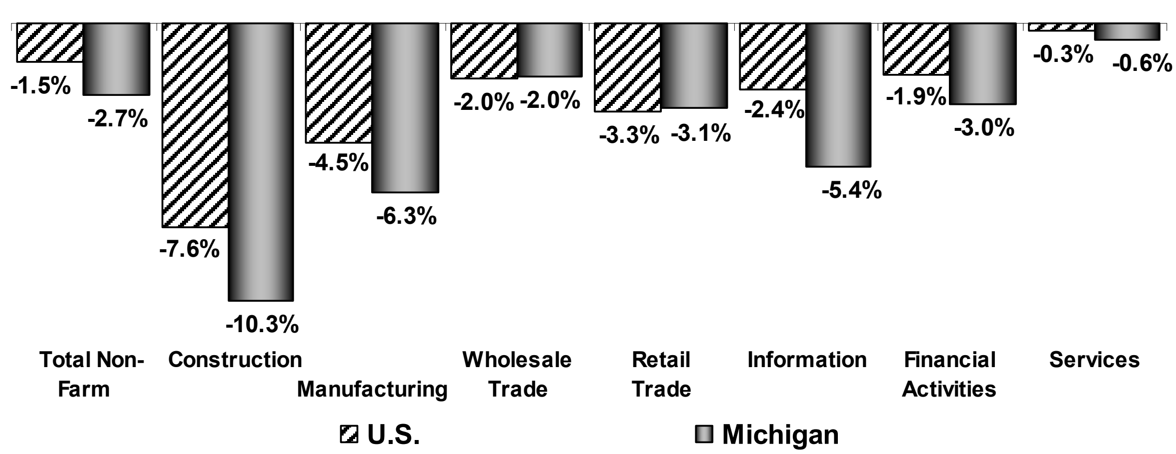
U.S. Non-Farm Employment
After U.S. employment peaked in February 2001, it began a long slide that did not end until August 2003. During this 30-month period, the national economy lost more than 2.7 million jobs—about 91,800 jobs per month on average. In the 52 months (between September 2003 and December 2007), more than 8.3 million jobs were added, but continued monthly job losses have reduced non-farm employment by more than 1.9 million thus far in 2008. The November 2008 job loss of more than 533,000 workers was the largest monthly decline since December 1974.

Michigan Non-Farm Employment
Although employment rebounded at the national level through 2007, conditions in Michigan have been far less optimistic. Employment in Michigan peaked in June 2000, a full eight months before the national level peak in February 2001. Following that June 2000 peak, employment in Michigan dropped steadily until July 2003, resulting in a loss of more than 314,000 jobs—a 6.7% decline. For the next two years, employment in Michigan fluctuated around the July 2003 level, with monthly job gains offset by subsequent monthly job losses. Since then, job losses have accelerated; during the first eleven months of 2008, more than 112,000 additional jobs have been lost.

U.S. and Michigan Employment

Figure 2 shows the percent change in employment between November 2007 and November 2008 for all private workers in several important sectors of the economy for both the U.S. and Michigan. Worsening economic conditions are evident as the U.S. lost more than 2.0 million jobs over this period while employment in Michigan fell by 114,000 jobs.

Figure 2
Percent Change in Employment
November 2007 Through November 2008



U.S. Employment
From November 2007 through November 2008, the U.S. experienced job losses in all sectors. The construction, manufacturing, and retail trade sectors were especially hard hit as they lost 576,000, 617,000 and 529,000 jobs respectively. Although the

manufacturing sector has been generally contracting for the past several years, job losses in construction are the result of the declining housing sector while losses in retail trade reflect the overall economic downturn.

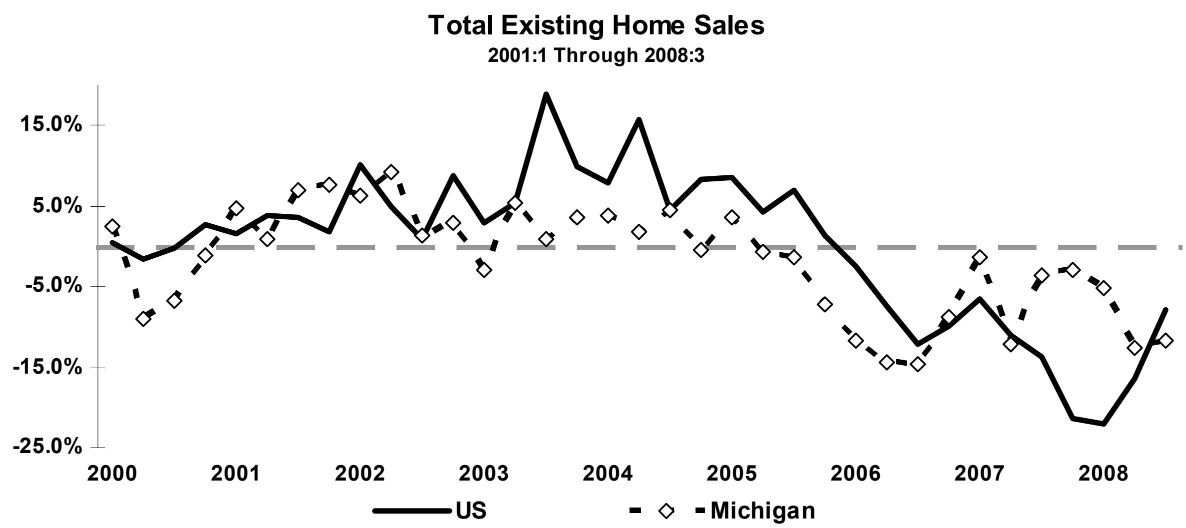
Michigan Employment

Job losses in Michigan over the past year were similarly concentrated in the construction, manufacturing, and retail trade sectors, although the service sector also experienced large declines. Michigan's manufacturing employment losses accounted for 6.2% of the total nationwide decline in manufacturing employment over the past 12 months.

U.S. and Michigan Existing Home Sales

Figure 3 shows the quarterly percentage change in sales of existing homes for the U.S. and Michigan relative to the same quarter the year before.

Figure 3



U.S. Existing Home Sales

The U.S. housing market continued to flourish during the first half of the decade, but began to turn downward in late 2005 as home sales began to falter. Sales continued to drop at an accelerating rate throughout 2007 as the full impact of the collapse of the housing market spread through the economy, and they have continued to decline through 2008, albeit at a lesser rate.

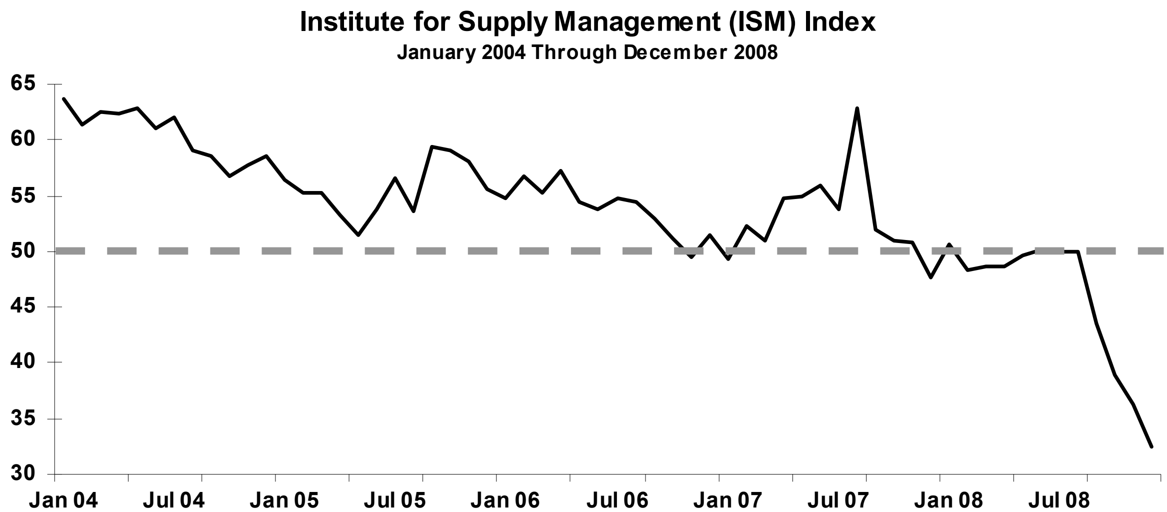
Michigan Existing Home Sales

Although there was a dip in Michigan's housing market in the early part of this decade, sales of existing homes— for the most part—followed a path similar to that of the U.S. as a whole through 2004. Starting in early 2005, existing home sales in Michigan began falling dramatically, underwent a steep decline through late 2006, and continue to fall.

Institute for Supply Management (ISM) Index

Figure 4 shows the ISM Index, a composite index of five economic indicators used to measure economic vitality beginning with January 2004. An index number above 50 indicates a growing manufacturing sector; a number below 50 suggests that the manufacturing sector is contracting. A number below 42.7 indicates that the economy as a whole is contracting.

Figure 4



The ISM index began January 2004 at a 20-year high of 63.3. This was followed by a 16-month slide that saw the index decline to 51.4 in May 2005. The ISM index rose in three of the next four months—reaching a level of 59.4 in September 2005—before beginning a four-month decline to 54.8 in January 2006; for the next 30 months, the index generally remained between 50 and 55. The ISM index has dropped in each of the past six months, and the December 2008 level of 32.4 is the lowest since the July 1980 level of 30.3.

Index of Consumer Sentiment

Consumer sentiment can be a strong motivator of personal consumption expenditures, which comprise almost two-thirds of GDP. **Figure 5** shows the University of Michigan Index of Consumer Sentiment beginning with January 2004.

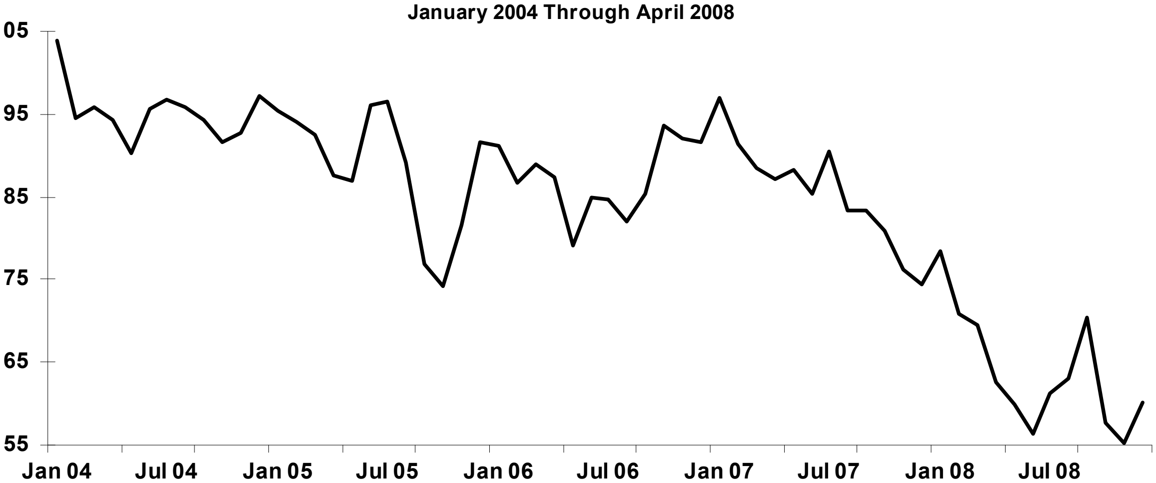
Although the Index of Consumer Sentiment began January 2004 at a level over 100 for the first time in more than three years, it dropped in February and remained in the low- to mid-90s before ending 2004 with two consecutive monthly increases. Following this brief uptick, consumer sentiment declined in each of the next five months due, in part, to concerns about high gas prices and the possibility that the economy may be weakening.

In the wake of hurricanes Katrina and Rita in 2005, the Index of Consumer Sentiment plunged to 72.4 in October, rose to 91.5 in December, and then dropped in six of the first eight months of 2006 as consumers expressed concerns over rising gas prices and interest rates. After reaching a low of 82.0 in August, the index concluded 2006 at 91.7. Consumer sentiment has declined steadily since 2007, and the index finished 2007 at 74.5. By November 2008, the Index of Consumer Sentiment had fallen to 55.3, the lowest level in almost 28 years.

Figure 5

University of Michigan Index of Consumer Sentiment

January 2004 Through April 2008

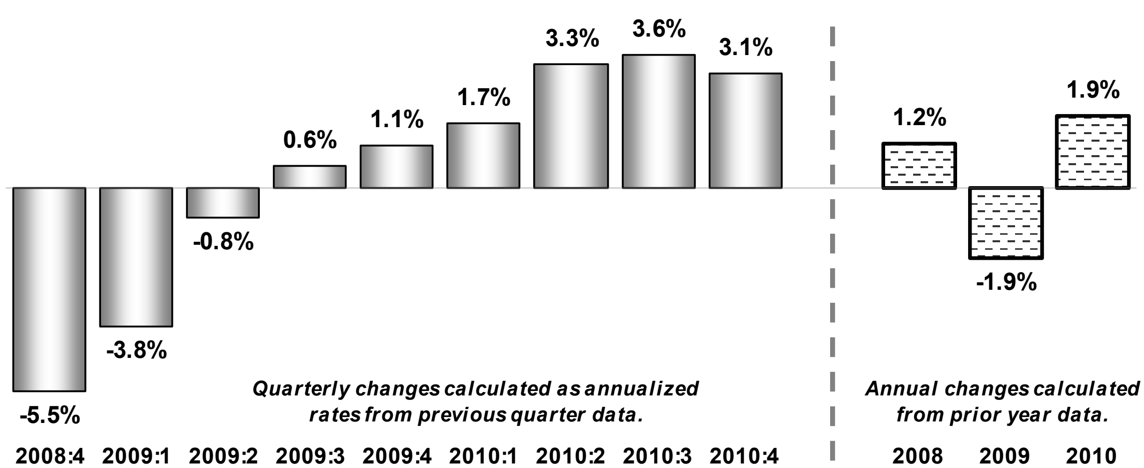


Real GDP

Figure 6 shows the estimated percent change in U.S. Real GDP for CY 2008, CY 2009, and CY 2010.

Figure 6

Percent Change in U.S. Real GDP



After declining 0.5% during the third quarter of 2008, real GDP is anticipated to fall by 5.5% in the fourth quarter. Real GDP growth, which was 2.0% in CY 2007, is forecast to be 1.2% in CY 2008, −1.9% in CY 2009, and 1.9% in CY 2010.

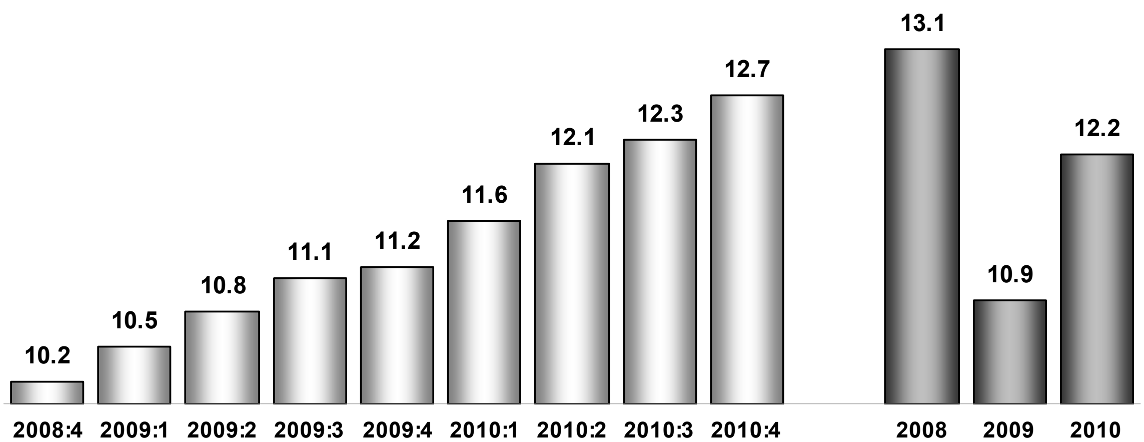
GDP growth over the past year was sustained primarily by business investment and federal government purchases. Due to a weak housing market and failures in the financial sector, however, both business and residential investment are forecast to decline in CY 2009. Gross private domestic investment is forecast to fall by 14.5% in CY 2009 before growing at a modest 4.2% rate in CY 2010 as business investment starts to increase.

Personal consumption is expected to increase by only 0.3% during CY 2008. As the economy continues to decline, growth in personal consumption is predicted to decline 1.2% in CY 2009 before increasing 1.1% in CY 2010.

Light Vehicle Sales

Figure 7 shows estimated light vehicle sales for CY 2008, CY 2009, and CY 2010.

Figure 7
Light Vehicle Sales
(Millions of Units)



Sales of light motor vehicles are expected to total 13.1 million units in CY 2008 before falling dramatically to just 10.9 million units in CY 2009. Light motor vehicle sales are forecast to recover slightly to 12.2 million units in CY 2010.

Over the past few years there has been a shift in vehicle sales away from light trucks and toward cars. Light truck sales, which accounted for 52.9% of total light vehicle sales in CY 2007, are expected to decrease to 48.9% in CY 2008 before increasing slightly to 49.0% in CY 2009. Light truck sales as a percent of total light vehicle sales are expected to drop to 48.3% in CY 2010.

The import share of total light vehicle sales was 23.3% in CY 2007; it is forecast to increase to 25.4% in CY 2008, 25.6% in CY 2009, and 25.9% in CY 2010.

Inflation

U.S. Inflation

Input prices (e.g., wages and import prices) have remained moderate and have held down production costs. Crude oil and natural gas prices, which have experienced volatile price fluctuations over the past several months, will continue to impact almost all sectors of the economy.

Benchmark West Texas intermediate crude—which averaged over $72 per barrel in CY 2007—began 2008 at over $90 per barrel, reached a high of $145 in July, and then fell to less than $50 by the end of the year. Although there is always concern over the stability of the oil supply, world demand is expected to be subdued as economic growth remains sluggish. It is anticipated that oil prices will stabilize somewhat during the forecast period and average about $55 per barrel during CY 2009 and $68 per barrel in CY 2010.

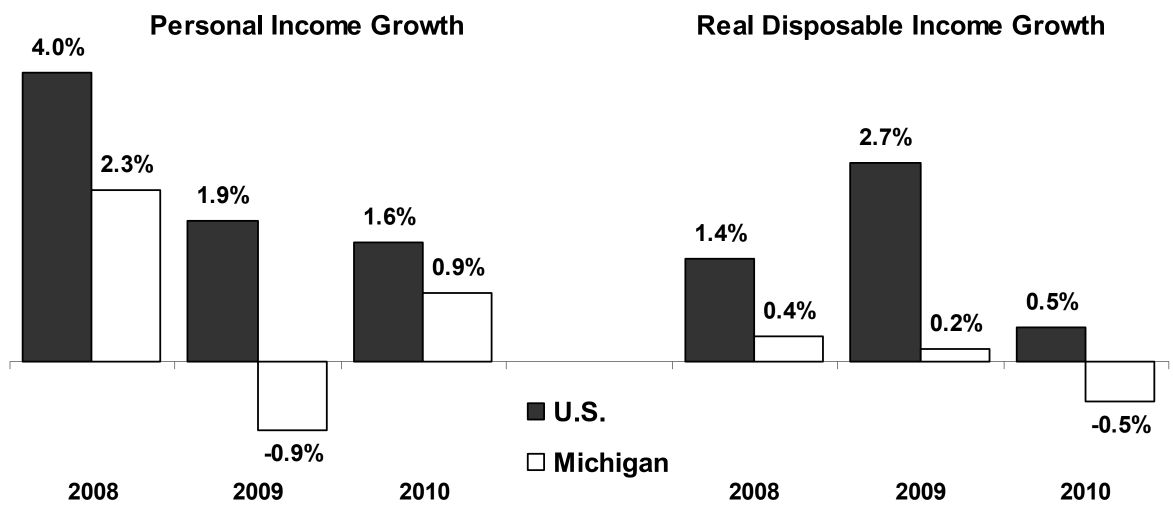
The annual rate of inflation, as measured by the percentage change in the U.S. Consumer Price Index-Urban (CPI-U), was 2.8% in CY 2007; it is expected to rise to 4.1% in CY 2008—reflecting, in part, the spike in oil prices—before dropping to 0.5% in CY 2009 and then rising to 2.5% in CY 2010.

Michigan Inflation
The cost of living in Michigan is measured by the Detroit Consumer Price Index for Urban Consumers (Detroit CPI-U). Michigan's average inflation rate was 1.9% in CY 2007, and inflation in Michigan should remain relatively low throughout the forecast period. The Detroit CPI-U is expected to increase 2.7% in CY 2008, 0.2% in CY 2009, and 2.2% in CY 2010.

Income Growth

Figure 8 shows personal and real disposable income growth for the U.S. and for Michigan.

Figure 8



U.S. Income Growth
Total U.S. personal income grew 6.1% in CY 2007. Personal income growth is forecast to increase 4.0% in CY 2008, 1.9% in CY 2009, and 1.6% in CY 2010.

Slightly higher inflation contributed to a modest 2.8% growth in U.S. real disposable income in CY 2007. U.S. real disposable income is forecast to grow 1.4% in CY 2008, 2.7% in CY 2009, and 0.5% in CY 2010.

Michigan Income Growth

Michigan's total state personal income growth was 4.0% in CY 2007. Michigan personal income is forecast to increase 2.3% in CY 2008, decline 0.9% in CY 2009, and then increase 0.9% in CY 2010.

Michigan real disposable income increased 1.6% in CY 2007; it is forecast to increase 0.4% in CY 2008, 0.2% in CY 2009, and then decline 0.5% in CY 2010.

Employment

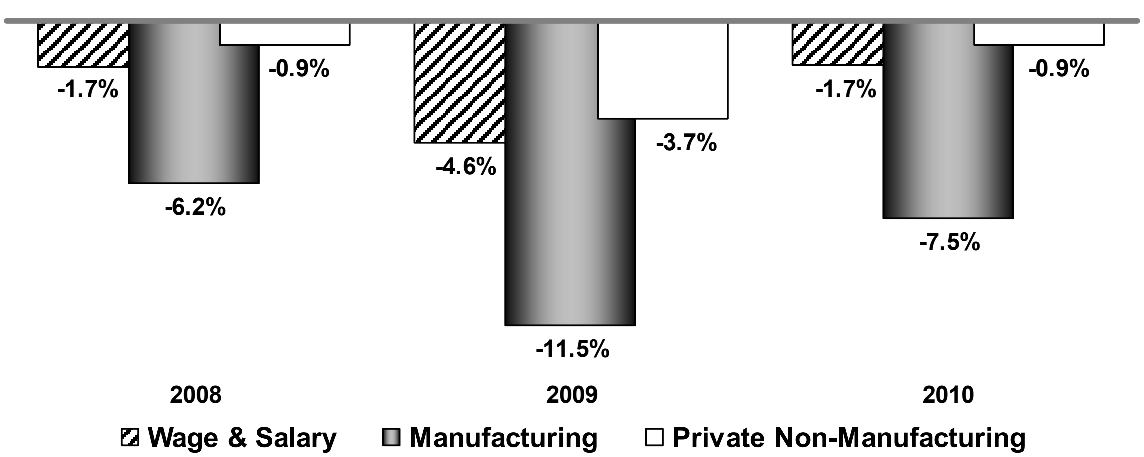
Figure 9 shows Michigan wage and salary, manufacturing, and private non-manufacturing employment growth.

U.S. Employment

Nationally, total non-farm employment has experienced average losses in excess of 173,700 per month during the first 11 months of 2008—a 1.4% overall decline. Total non-farm employment is projected to decrease 0.2% in CY 2008, 2.3% in CY 2009, and 0.5% in CY 2010 as the economy continues to slow.

Figure 9

Michigan Employment Growth



Michigan Employment

The Michigan economy has continued to endure a weak labor market. Michigan wage and salary employment declined by about 66,000 workers in CY 2007 and is estimated to decline by more than 73,000 workers in CY 2008, by 191,700 workers in CY 2009, and by 67,000 workers in CY 2010. The forecast calls for continued quarterly job losses through the fourth quarter of CY 2010.

Michigan wage and salary employment fell 1.5% in CY 2007, and is forecast to fall 1.7% in CY 2008, 4.6% in CY 2009, and 1.7% in CY 2010. Over the past 25 years, Michigan wage and salary employment has grown at an average annual rate of about 1.1%.

Michigan manufacturing employment dropped 5.2% in CY 2007, and is forecast to decrease 6.2% in CY 2008, 11.5% in CY 2009, and 7.5% in CY 2010. Although the most significant declines are concentrated in the motor vehicle industry, employment declines also appear throughout the entire manufacturing sector.

Michigan private non-manufacturing employment fell 0.8% in CY 2007; it is expected to decline 0.9% in CY 2008, 3.7% in CY 2009, and 0.9% in CY 2010.

Unemployment

U.S. Unemployment

As of December 2007, total non-farm employment had increased for 52 consecutive months. Monthly job losses through all of 2008, however, have increased the unemployment rate.

The U.S. unemployment rate was 4.6% in CY 2007; it is forecast to rise to 5.8% in CY 2008, 8.2% in CY 2009, and 8.7% in CY 2010.

Michigan Unemployment

Employment in Michigan remains a major concern as employment growth has fallen during each of the past eight years. Michigan's wage and salary employment is forecast to continue declining throughout 2009 and 2010. As a result, the unemployment rate is expected to remain relatively high through 2010 as the labor force decreases and the number of unemployed workers increases.

Michigan's unemployment rate was 7.2% in CY 2007; it is expected to increase to 8.4% in CY 2008, 11.3% in CY 2009, and 11.4% in CY 2010.

Table 4
ECONOMIC FORECAST VARIABLES

	Calendar 2007 Actual	Calendar 2008 Estimated	% Change from Prior Year	Calendar 2009 Estimated	% Change from Prior Year	Calendar 2010 Estimated	% Change from Prior Year
United States							
Real Gross Domestic Product (Billions of 2000 dollars)	$11,523.9	$11,658.1	1.2%	$11,433.8	–1.9%	$11,654.1	1.9%
Implicit Price Deflator GDP (2000 = 100)	119.8	122.8	2.5%	126.1	2.6	128.2	1.7%
Consumer Price Index (1982-84 = 100)	207.4	215.8	4.1%	216.7	0.5%	222.1	2.5%
Personal Consumption Deflator (2000 = 100)	117.7	121.6	3.3%	122.2	0.5%	124.5	1.9%
3-month Treasury Bills Interest Rate (Percent)	4.4%	1.4%		0.4%		1.0%	
Aaa Corporate Bonds Interest Rate (Percent)	5.6%	5.7%		4.8%		4.7%	
Non-Farm Employment (Millions)	137.6	137.3	–0.2%	134.1	–2.3%	133.4	–0.5%
Unemployment Rate—Civilian (Percent)	4.6%	5.8%		8.2%		8.7%	
Light Vehicle Sales (Millions of units)	16.1	13.1	–18.5%	10.9	–16.8%	12.2	11.7%
Passenger Car Sales (Millions of units)	7.6	6.7	–11.6%	5.6	–16.8%	6.3	12.6%
Light Truck Sales (Millions of units)	8.5	6.4	–24.7%	5.3	–16.5%	5.9	10.0%
Import Share of Light Vehicles (Percent)	23.3%	25.4%		25.6%		25.9%	
Personal Income (Billions of current dollars)	$11,663.3	$12,125.5	4.0%	$12,360.7	1.9%	$12,562.7	1.6%
Real Disposable Income (Billions of 2000 dollars)	$8,644.1	$8,766.5	1.4%	$9,004.6	2.7%	$9,047.9	0.5%
Michigan							
Wage and Salary Employment (Thousands)	4,261.4	4,188.0	–1.7%	3,996.3	–4.6%	3,929.3	–1.7%
Unemployment Rate (Percent)	7.2%	8.4%		11.3%		11.4%	
Personal Income (Millions of current dollars)	$345,886	$354,005	2.3%	$350,759	–0.9%	$354,049	0.9%
Real Personal Income (Millions of 1982-84 dollars)	$172,727	$172,119	–0.4%	$170,168	–1.1%	$168,035	–1.3%
Real Disposable Income (Millions of 1982-84 dollars)	$151,774	$152,329	0.4%	$152,608	0.2%	$151,780	–0.5%
Wage and Salary Income (Millions of current dollars)	$188,062	$188,678	0.3%	$181,390	–3.9%	$181,991	0.3%
Detroit Consumer Price Index (1982-84 = 100)	200.3	205.7	2.7%	206.1	0.2%	210.7	2.2%
Detroit CPI (FY) (1982-84 = 100)	199.0	204.8	2.9%	205.6	0.4%	209.5	1.9%

RISKS AND UNCERTAINTIES

An economic forecast is based on the best information available at the time the forecast is prepared. Because information and foresight are not perfect, risks and uncertainties are inherent in any forecast. Key risks in this forecast stem predominantly from uncertainties surrounding fiscal and monetary policy, household finances, housing, economic growth in foreign countries, and Michigan's motor vehicle industry.

Fiscal and Monetary Policy

- **Fiscal Policy**
  Included in the forecast is a significant federal stimulus totaling about $600 billion over three years. The fiscal policy is assumed to be roughly evenly split between tax cuts and spending, and to be tilted towards CY 2009 and CY 2010. The timing, composition, and requirements attached to the federal funds are all key to assessing the effect of the stimulus on the national and state economies and budgets.

- **Monetary Policy**
  Although the Federal Reserve is designated as the primary driver of monetary policy through setting interest rates and instilling confidence, the credit crisis has necessitated action by other federal entities to ease the flow of credit.

  The Federal Funds rate—the rate banks charge on short-term loans made to other banks—was lowered from 2.0% to 1.5%, then to 1.0% on October 28th. On December 16, 2008, the Federal Reserve issued a statement to float the Federal Funds rate between 0 and 25 basis points (0.25%). In addition, the Federal Reserve expanded its balance sheet by $1.4 trillion to provide liquidity to banks, commercial paper issuers, and other financial firms. The Federal Reserve seems to be prepared to inject liquidity through non-traditional means if needed.

  The U.S. Treasury is injecting new capital to banks under the $700 billion Troubled Asset Relief Program (TARP). Under TARP, the Federal Reserve, Federal Deposit Insurance Corporation (FDIC), and Federal Housing Finance Agency are directed to implement measures to help reduce the number of foreclosures on residential loans—including restructuring mortgages by extending terms and reducing monthly payments.

Containing further economic damage and repairing the financial markets are key elements in restoring a smooth-running economy. The degree of success and timing of efforts to restore the U.S. economy are major uncertainties in this forecast.

Household Finances and Housing

Personal consumption expenditures comprise almost two-thirds of total economic activity. Declining home values, high debt levels, and mounting job losses will keep personal consumption expenditures low.

Low mortgage rates, creative financing, and speculative buying helped support a strong housing market through the middle of CY 2006, and the vibrant housing market supported strong consumption growth and allowed for a low savings rate. National income growth was supplemented with mortgage equity withdrawals, which allowed consumers to spend more than income alone would allow. As the housing market contracted sharply, consumers pulled back on spending as mortgage equity withdrawals ended and the value of investments eroded.

National non-farm payroll employment is forecast to post declines throughout the forecast horizon: down 2.3% in CY 2009, and 0.5% in CY 2010. Consumption is forecast to fall 1.2% in CY 2009, then increase 1.1% in CY 2010.

Exports to Foreign Countries

Exports to foreign countries grew much higher than the domestic economy in the first several months of CY 2008. However, the economies of major U.S. trading partners are now falling rapidly. The value of the U.S. dollar is expected to appreciate in CY 2009, then depreciate slightly in CY 2010. In general, a stronger dollar makes imports more attractive and exports less attractive, while a weaker dollar makes imports less attractive and exports more attractive.

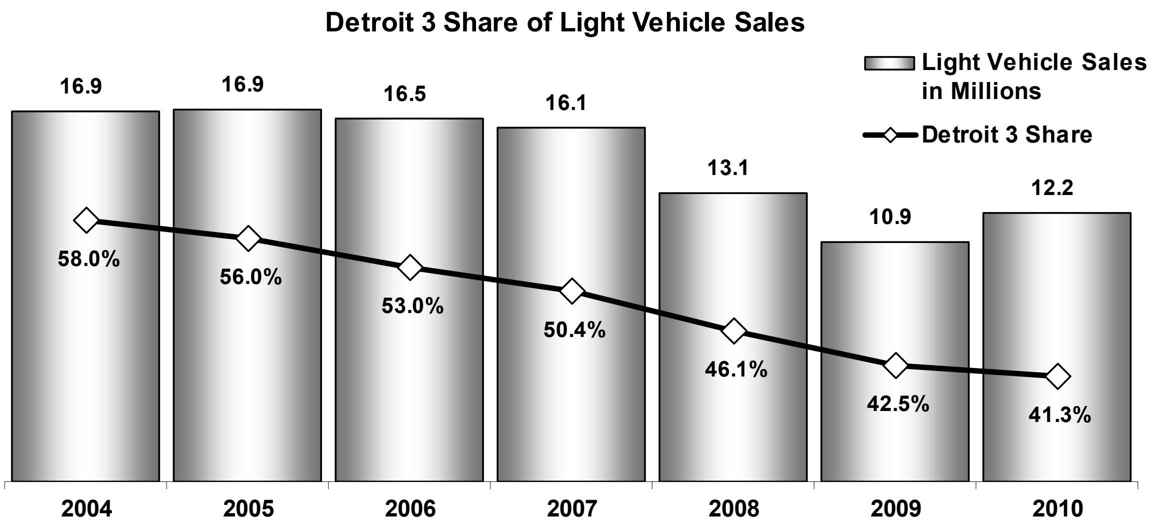
After increasing 7.9% in CY 2008, exports are expected to fall 0.2% in CY 2009 before advancing 4.0% in CY 2010.

Michigan's Motor Vehicle Industry

The level and composition of light motor vehicle sales is a key component of Michigan's economy. Light vehicle sales were 16.1 million units in CY 2007 and are forecast to be 13.1 million in CY 2008 and 10.9 million in CY 2009. As the national economy starts to improve, light motor vehicle sales are forecast to increase to 12.2 million units.

As shown in **Figure 10**, the market share of the Detroit three auto manufacturers is expected to decline to 46.1% in CY 2008. Imports and transplants (vehicles with a foreign nameplate that are made in the U.S.) have steadily gained in market share over the past several years.

Figure 10



The extent to which the domestic nameplates can retain market share will have a direct impact on Michigan's economy. This forecast assumes that the Detroit three market share will decline to 42.5% in CY 2009 and 41.3% in CY 2010.

In mid-December 2008, the federal government approved bridge loans for General Motors and Chrysler. Both automakers must demonstrate viability by March 31, 2009, or immediately repay the loans; the current credit and economic environment may make the task more difficult. The incoming federal administration will need to address the automakers' situation early in CY 2009.

After a decline of 14.0% in CY 2008, Michigan transportation equipment employment is forecast to decline 23.4% in CY 2009 and 16.7% in CY 2010. The CY 2010 estimated level of transportation equipment employment of 112,000 is only about one-third of the 346,000 peak in CY 2000. If the Michigan-produced market share of motor vehicles is greater or less than anticipated, Michigan's economy and revenue growth will be higher or lower than estimated.

GF/GP AND SAF REVENUE

Revenue estimates are based on economic performance of the components of national and state economies discussed in the previous section. This section explains January 2009 House Fiscal Agency revenue estimates for GF/GP (**Table 5**) and SAF (**Table 6**) revenue by major revenue sources. It provides revenue estimates, year-end balances for the major funds and the budget stabilization fund, and the state revenue limit calculation.

Table 5

GF/GP REVENUE ESTIMATES
(Millions of Dollars)

	Preliminary Final FY 2007-08	FY 2008-09	FY 2009-10	Change From FY 2008-09 to FY 2009-10	
Income Tax	$5,106.6	$4,569.8	$4,216.3	($353.5)	−7.7%
Sales and Use Taxes	988.2	908.1	961.2	53.0	5.8%
MBT/SBT/Insurance Taxes	2,348.6	2,035.7	2,057.6	21.9	1.1%
Other Taxes	542.7	479.8	471.5	(8.3)	−1.7%
GF/GP Tax Revenue	**$8,986.0**	**$7,993.4**	**$7,706.6**	**($286.8)**	**−3.6%**
Non-Tax Revenue	373.7	347.0	347.0	0.0	0.0%
Total Net GF/GP Revenue	**$9,359.8**	**$8,340.4**	**$8,053.6**	**($286.8)**	**−3.4%**

NOTE: Numbers may not add due to rounding.

GF/GP Revenue by Source

GF/GP Tax Revenue

GF/GP tax revenue totaled $8,986.0 million in FY 2007-08; it is estimated to decrease by $992.6 million (11.0%) to $7,993.4 million in FY 2008-09, and decrease by $286.8 million (3.6%) to $7,706.6 million in FY 2009-10. Declining employment and income, as well as the phase-in of the Earned Income Tax Credit or EITC are the main reasons for reduced GF/GP tax revenue.

Total Net GF/GP Baseline Revenue

Total net GF/GP revenue includes tax revenue and non-tax revenue such as federal aid, licenses and permits, and transfers from the liquor purchase revolving fund. Total GF/GP net revenue was $9,359.8 million in FY 2007-08; it is estimated to decrease by $1,019.4 million (10.9%) to $8,340.4 million in FY 2008-09, and by $286.8 million (3.4%) to $8,053.6 million in FY 2009-10.

Table 6
SCHOOL AID FUND REVENUE ESTIMATES
(Millions of Dollars)

	Preliminary Final FY 2007-08	FY 2008-09	FY 2009-10	Change From FY 2008-09 to FY 2009-10	
Sales and Use Tax	$5,387.4	$5,142.5	$5,164.4	$22.0	0.4%
Income Tax Earmark	2,117.7	2,015.8	1,973.0	(42.8)	−2.1%
State Education Tax	2,079.7	2,005.5	1,945.5	(60.0)	−3.0%
Lottery/Casino Wagering	852.8	830.2	810.3	(19.9)	−2.4%
MBT	341.0	729.0	743.6	14.6	2.0%
Tobacco Taxes	424.7	413.3	402.0	(11.2)	−2.7%
Real Estate Transfer Tax	169.8	125.0	115.0	(10.0)	−8.0%
Other Taxes	139.8	119.7	114.7	(5.0)	−4.2%
Net SAF Revenue	**$11,512.9**	**$11,381.0**	**$11,268.5**	**($112.5)**	**−1.0%**
Adjustments	1,561.7	1,624.8	1,862.5	237.7	14.6%
Total Net SAF Revenue	**$13,074.6**	**$13,005.8**	**$13,131.0**	**$125.2**	**1.0%**

NOTE: Numbers may not add due to rounding.

SAF Revenue by Source

Net SAF Revenue

Net SAF revenue, which takes tax changes into account, totaled $11,512.9 million in FY 2007-08; it is forecast to decrease by $131.9 million (1.1%) to $11,381.0 million in FY 2008-09, and by $112.5 million (1.0%) to $11,268.5 million in FY 2009-10.

The decline in revenue from FY 2007-08 to FY 2008-09 and FY 2009-10 would be even greater without the MBT-related property tax changes and the MBT surcharge. The SAF received $341.0 million from the MBT earmark in FY 2007-08 and will receive $729.0 million from the MBT earmark in FY 2008-09. Although the MBT-related personal property tax cuts reduce local revenue for schools (18-mills), the SAF earmark from the MBT will hold the schools harmless from state and local school property tax cuts.

Total Net SAF Revenue

Total net SAF revenue includes net SAF revenue and adjustments (federal aid and the beginning balance). Total Net SAF revenue totaled $13,074.6 million in FY 2007-08; it is forecast to decrease $68.8 million (0.5%) to $13,005.8 million in FY 2008-09, and increase $125.2 million (1.0%) to $13,131.0 million in FY 2009-10.

HFA Estimates of Year-End Balances

Table 7 reports House Fiscal Agency estimates of year-end balances for GF/GP, the SAF, and the BSF.

Fiscal Year 2007-08 estimates are based on year-to-date appropriations and HFA revenue estimates. Final FY 2006-07 and FY 2007-08 figures are included.

Budget Stabilization Fund estimates are based on current balance estimates provided by the Michigan Department of Treasury and HFA estimates of future deposits and interest earned.

Table 7

YEAR-END BALANCE ESTIMATES

(Millions of Dollars)

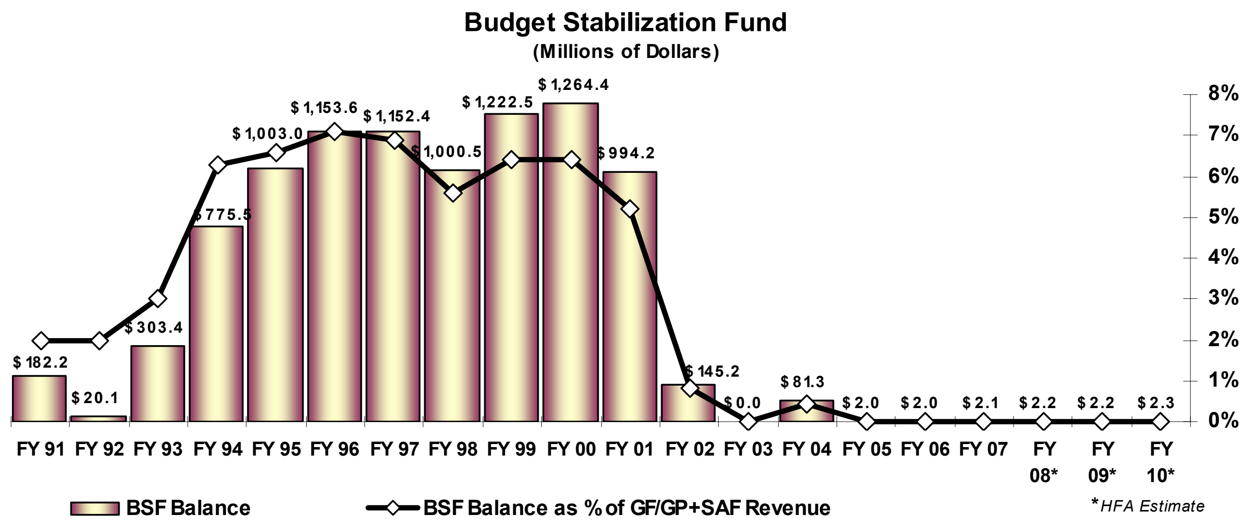
	Final FY 2006-07	Preliminary Final FY 2007-08	Estimated FY 2008-09
General Fund/General Purpose	$259.1	$458.0	$0.0
School Aid Fund	$82.4	$247.0	$0.0
Budget Stabilization Fund	$2.1	$2.2	$2.2

SAF revenue is restricted; any year-end balance is carried forward to the subsequent year.

BSF Year-End Balance

The Counter-Cyclical Budget and Economic Stabilization Fund (BSF), the state's rainy day fund, is a reserve of cash to contribute to or withdraw from throughout economic and budget cycles. **Figure 11** shows the BSF fund balance and the BSF fund balance as a percent of total GF/GP and SAF revenue. **Table 8** details deposits, withdrawals, interest earnings, and the year-end balance from FY 1990-91 through FY 2009-10.

Figure 11



The BSF ending fund balance for FY 2007-08 is expected to be $2.2 million. The BSF trigger calculation—based on Michigan personal income less transfer payments adjusted for inflation and actual or net GF/GP revenue—indicates a $363.6 million withdrawal for FY 2008-09 and a $71.9 million withdrawal for FY 2009-10. The estimated BSF ending fund balance for FY 2008-09 is $2.2 million; the estimated BSF ending fund balance for FY 2009-10 is $2.3 million.

Table 8
BUDGET STABILIZATION FUND HISTORY
(Millions of Dollars)

Fiscal Year	Deposits	Withdrawals	Interest Earned	Balance
1990-91	$0.0	$230.0	$27.1	$182.2
1991-92	$0.0	$170.1	$8.1	$20.1
1992-93	$282.6	$0.0	$0.7	$303.4
1993-94	$460.2	$0.0	$11.9	$775.5
1994-95	$260.1	$90.4	$57.7	$1,003.0
1995-96	$91.3	$0.0	$59.2	$1,153.6
1996-97	$0.0	$69.0	$67.8	$1,152.4
1997-98	$0.0	$212.0	$60.1	$1,000.5
1998-99	$244.4	$73.7	$51.2	$1,222.5
1999-2000	$100.0	$132.0	$73.9	$1,264.4
2000-01	$0.0	$337.0	$66.7	$994.2
2001-02	$0.0	$869.8	$20.8	$145.2
2002-03	$0.0	$156.1	$10.9	$0.0
2003-04	$81.3	$0.0	$0.0	$81.3
2004-05	$0.0	$81.3	$2.0	$2.0
2005-06	$0.0	$0.0	$0.0	$2.0
2006-07	$0.0	$0.0	$0.1	$2.1
2007-08*	$0.0	$0.0	$0.1	$2.2
2008-09*	$0.0	$0.0	$0.1	$2.2
2009-10*	$0.0	$0.0	$0.1	$2.3

** HFA Estimate*
NOTE: Numbers may not add due to rounding.

Compliance With the State Revenue Limit

Article IX, Section 26 of the *Michigan Constitution,* which was approved by the vote of the people in 1978, sets a limit on the amount of revenue collected by the state in any fiscal year. As provided for in the Constitution, the revenue limit is calculated as 9.49% of total state personal income (which is the broadest measure of state economic activity) in the previous full calendar year prior to the fiscal year in which the revenues are measured.

The revenue to be considered in the revenue limit includes not only state taxes, but also fees, licenses, and interest earned. Federal aid is not included in the revenue limit calculation. Article IX, Section 26, *Constitution of the State of Michigan*, provides that:

> . . . For any fiscal year in the event that Total State Revenues exceed the limit established in this section by 1% or more, the excess revenues shall be

refunded pro rata based on the liability reported on the Michigan income tax and single business tax (or its successor tax or taxes) annual returns filed following the close of such fiscal year. If the excess is less than 1%, this excess may be transferred to the State Budget Stabilization Fund . . . .

Furthermore, the state is prohibited from spending any current-year revenue in excess of the limit established in Section 26 by Article IX, Section 28.

As shown in **Table 9, Figure 12,** and **Table 10**, the preliminary final FY 2007-08 revenue limit calculation indicated that state revenue collections were $4.78 billion below the revenue limit. For FY 2008-09 and FY 2009-10, state revenue is estimated to be substantially below the revenue limit—by $6.39 billion and $7.46 billion, respectively.

Table 9

COMPLIANCE WITH THE STATE REVENUE LIMIT

(Millions of Dollars)

Revenue Limit Calculations	**Final FY 2006-07**	**Estimated FY 2007-08**	**Estimated FY 2008-09**	**Estimated FY 2009-10**
Personal Income				
Calendar Year	CY 2005	CY 2006	CY 2007	CY 2008
Amount	$331,304	$341,075	$345,886	$354,005
X Limit Ratio	9.49%	9.49%	9.49%	9.49%
State Revenue Limit	**$31,440.7**	**$32,368.0**	**$32,824.5**	**$33,595.1**
Total Revenue Subject to Revenue Limit	$26,118.4	$27,590.6	$26,434.2	$26,130.3
Amount Under (Over) State Revenue Limit	**$5,322.3**	**$4,777.5**	**$6,390.3**	**$7,464.8**

NOTE: Numbers may not add due to rounding.

Figure 12

Constitutional Revenue Limit

Amount Under or Over Limit (Billions of Dollars)

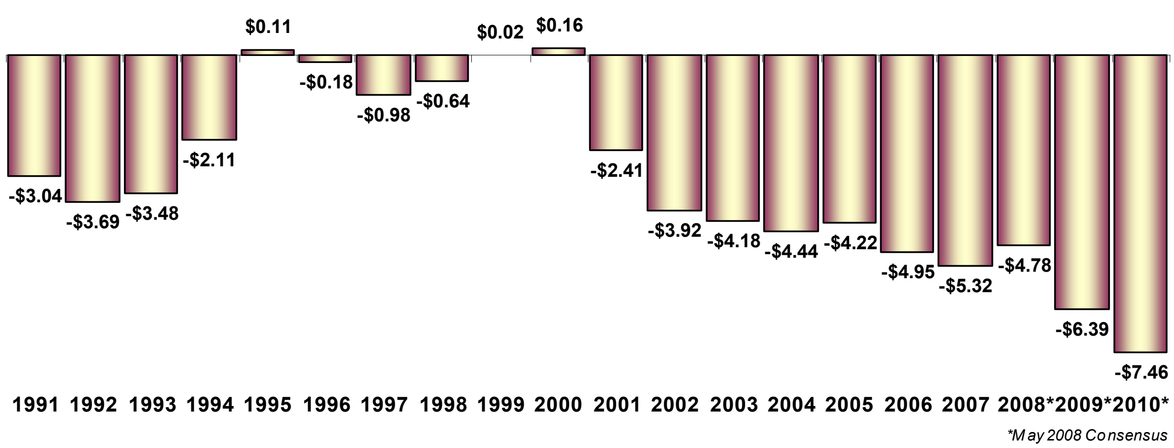


Table 10

CONSTITUTIONAL REVENUE LIMIT HISTORY
(Billions of Dollars)

Fiscal Year	(Under) or Over Limit
1990-91	($3.04)
1991-92	($3.69)
1992-93	($3.48)
1993-94	($2.11)
1994-95	$0.11
1995-96	($0.18)
1996-97	($0.98)
1997-98	($0.64)
1998-99	$0.02
1999-2000	$0.16
2000-01	($2.41)
2001-02	($3.92)
2002-03	($4.18)
2003-04	($4.44)
2004-05	($4.22)
2005-06	($4.95)
2006-07	($5.32)
2007-08*	($4.78)
2008-09*	($6.39)
2009-10*	($7.46)

**HFA Estimate*

HOUSE FISCAL AGENCY

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