

Pennsylvania's Economic and Budget Outlook

FY 2014-15 to FY 2019-20

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The Economic and Budget Outlook

➤ Provide Five-Year Projections For:

- Pennsylvania Demographics
- Pennsylvania Economics
- General Fund Revenues
- General Fund Expenditures

➤ Why Do We Do It?

- Establish a neutral baseline to assess fiscal situation.
- Identify long-term budget trends.
- Alert policymakers to structural imbalances.

Demographic Outlook

Age Distribution

Life Expectancy and Median Age
Age of Workforce

Labor Force Participation Rates
Components of Population Change

All Data from Pennsylvania State Data Center

Broad Demographic Trends

	<u>2010</u>	<u>2015</u>		<u>2020</u>	
	Number	Number	Growth	Number	Growth
PA (000s)					
0 – 19	3,173	3,128	-1.4%	3,092	-1.2%
20 – 64	7,575	7,609	0.4%	7,571	-0.5%
<u>>= 65</u>	<u>1,963</u>	<u>2,212</u>	<u>12.7%</u>	<u>2,540</u>	<u>14.9%</u>
Total	12,711	12,949	1.9%	13,203	2.0%
US (millions)					
0 – 19	83.2	83.4	0.3%	84.7	1.6%
20 – 64	185.7	190.3	3.1%	193.2	1.5%
<u>>= 65</u>	<u>40.4</u>	<u>47.7</u>	<u>17.8%</u>	<u>56.0</u>	<u>17.3%</u>
Total	309.3	321.4	4.3%	333.9	3.9%

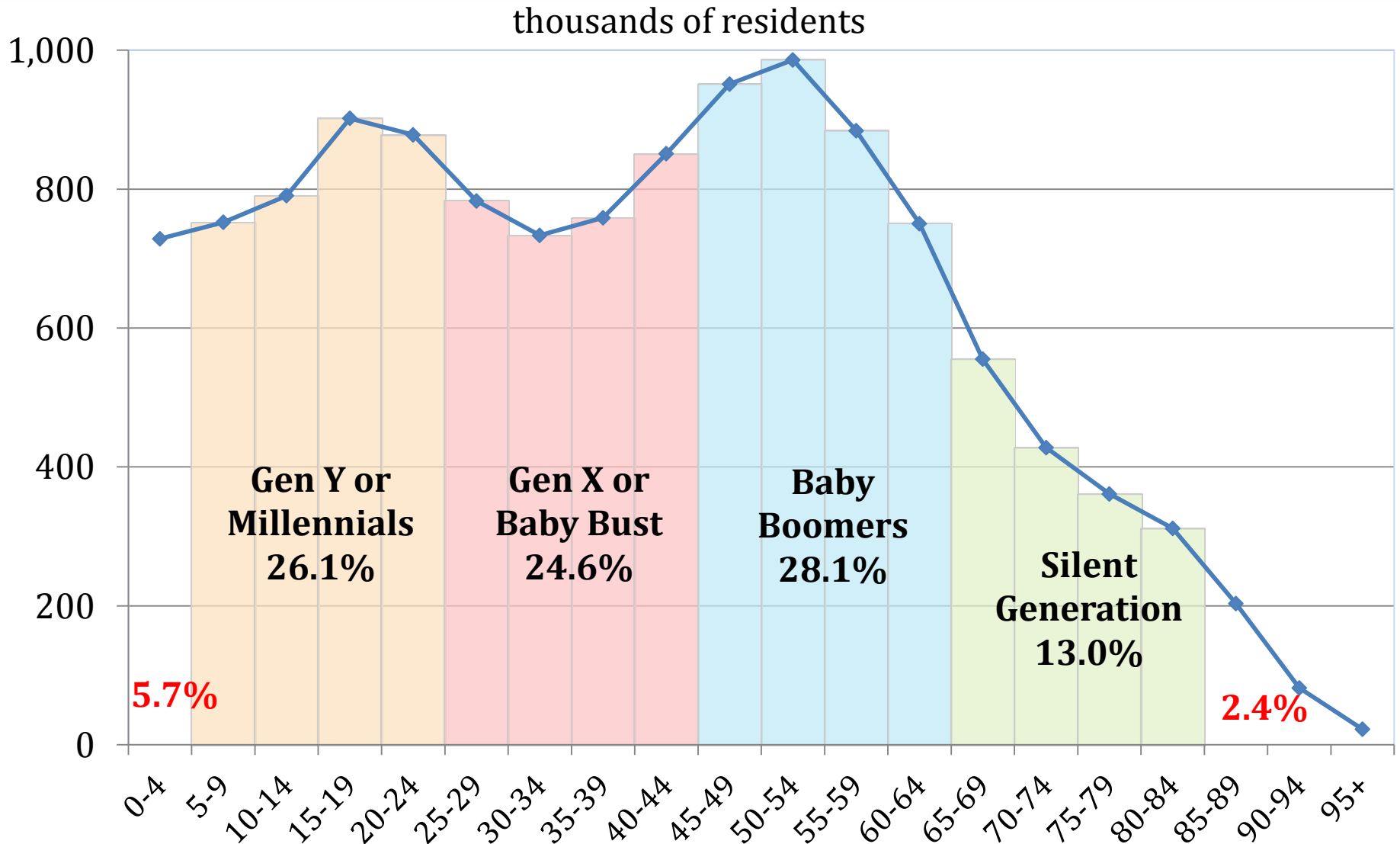
half the rate of increase

Sources: U.S. Census Bureau and Pennsylvania State Data Center.

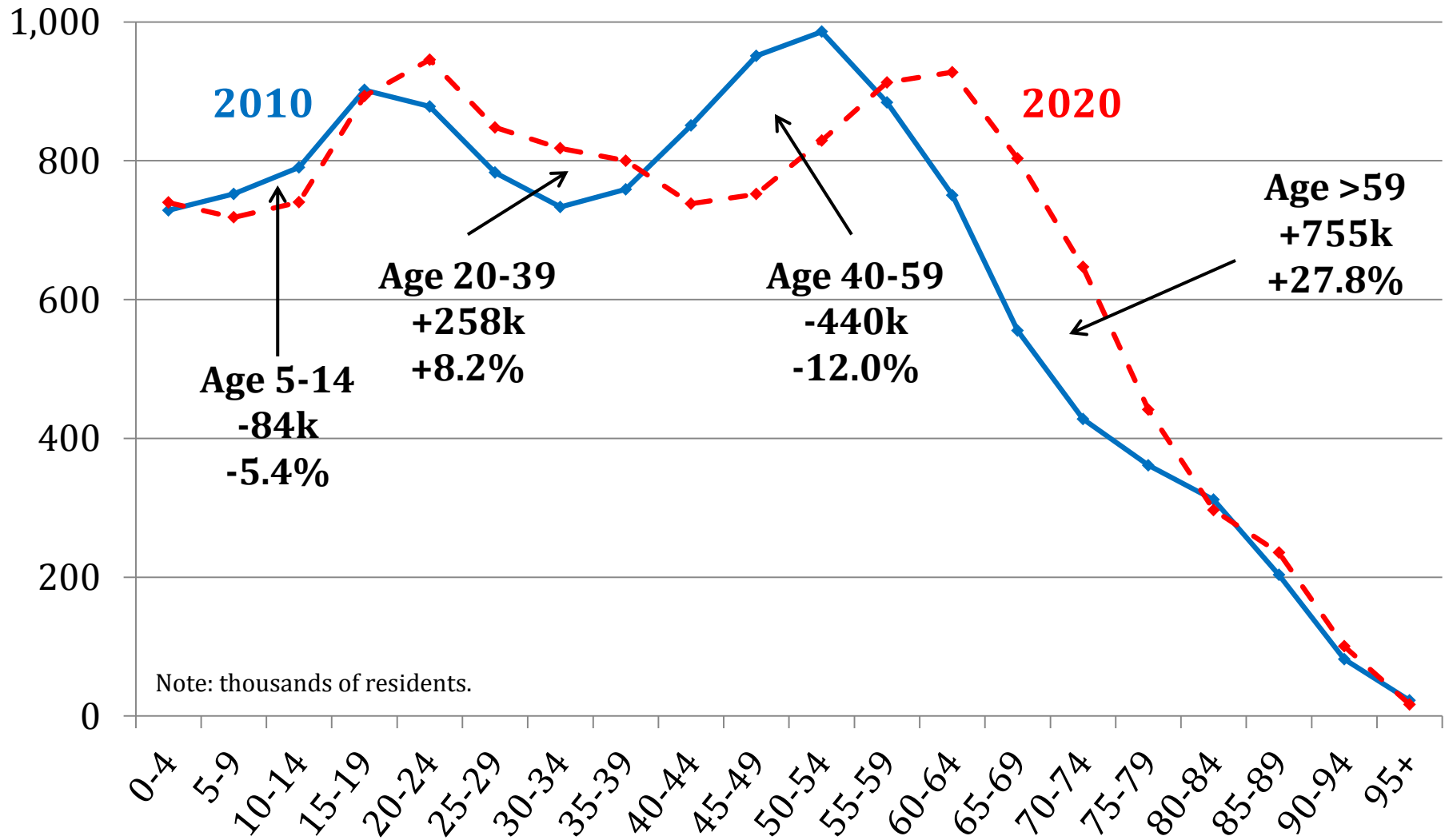
Demographic Waves Drive Trends

- **Baby Boomers: Born 1946 to 1964.**
 - Retirements reduce the potential labor force.
 - Oldest reach typical retirement age (65) in 2011.
 - Many now continue to work past age 65.
- **Generation X or Baby Bust: Born 1965 to 1984.**
 - Unusual exits from labor force. What is the cause?
- **Generation Y or Millennials: Born 1985 to 2004.**
 - Student loan debt and household formation.

PA Demographics 2010



PA Demographics: 2010 vs. 2020



PA Labor Force Participation Rates

Year	Total	<u>Age Group</u>			
		25-44	45-54	55-64	65+
2000	64.3	84.3	83.8	59.9	10.9
2005	64.4	83.6	83.1	65.2	12.4
2010	63.2	83.6	81.9	65.4	16.5
2013	63.4	82.8	80.3	66.1	17.6
2014	62.7	n.a.	n.a.	n.a.	n.a.

Changes from 2000 to 2014:

 Total: -1.6 ppt

 25-44: -1.5 ppt

 45-54: -3.5 ppt

 55-64: +6.2 ppt

 65+: +6.7 ppt

Source: Current Population Survey (U.S. Census Bureau) and PA Department of Labor and Industry, CWIA.

International Migration Fuels Growth

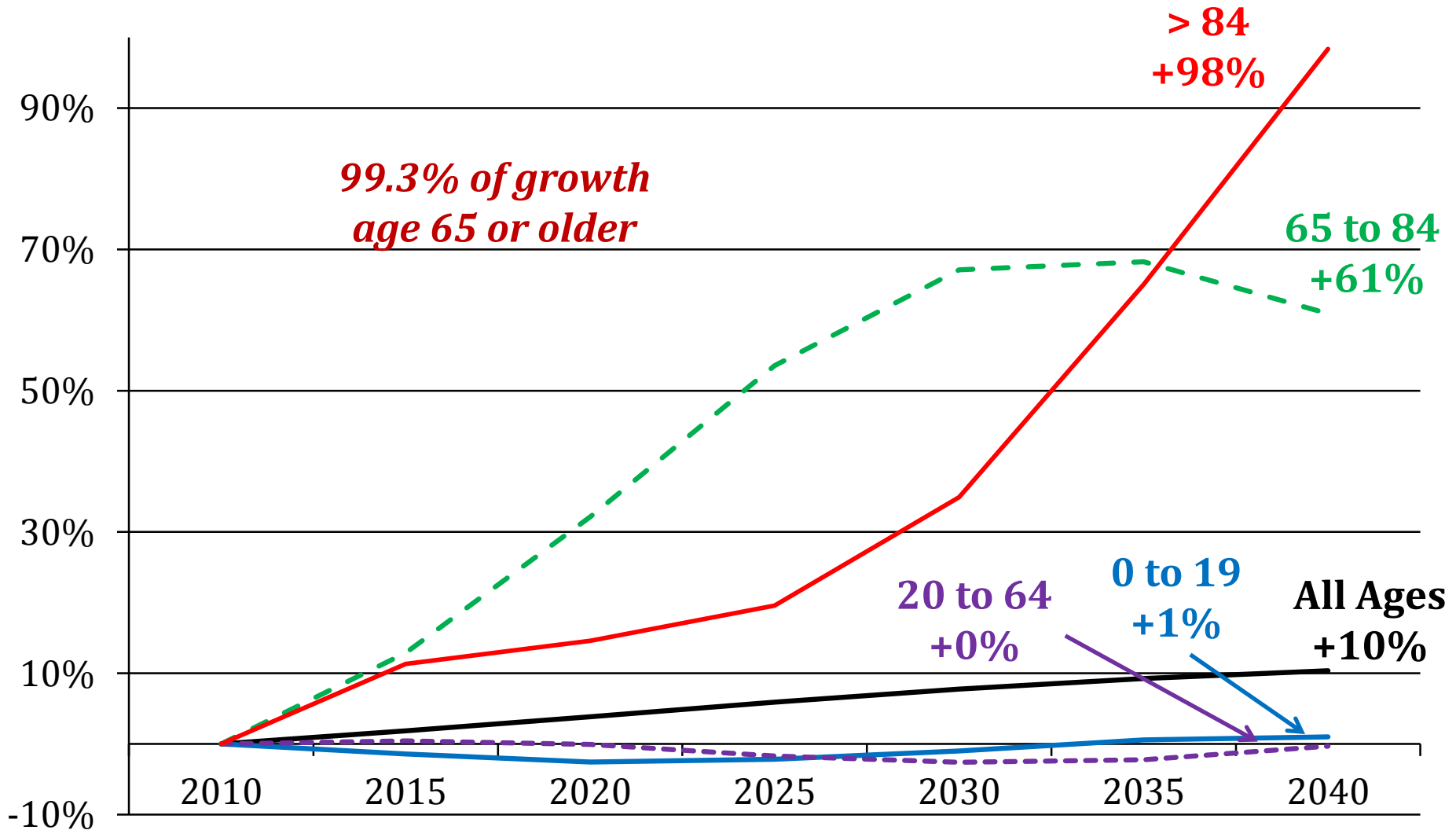
components of population change (000s)

	<u>2010-20</u>	<u>2020-30</u>	<u>2030-40</u>
Start of Decade	12,711	13,203	13,701
Births less Deaths	230	→ 174	→ -32
Net Domestic Migration	29	29	31
Net Int'l Migration	<u>232</u>	<u>296</u>	entire gain <u>331</u>
End of Decade	13,203	13,701	14,032
Decade Growth Rate	3.9%	3.8%	slow down 2.4%

Source: Pennsylvania State Data Center.

Cumulative Growth Rates Through 2040

by age cohort



Economic Outlook

A Reversion to Historical Growth
The Pennsylvania Labor Market

The Economic Outlook



➤ Economic Forecast Provides Neutral Benchmark.

- Assumes growth rates return to historical averages.
- Reflects non-recession years only.
- Really, a budget simulation exercise.

➤ Some Positives and Negatives.

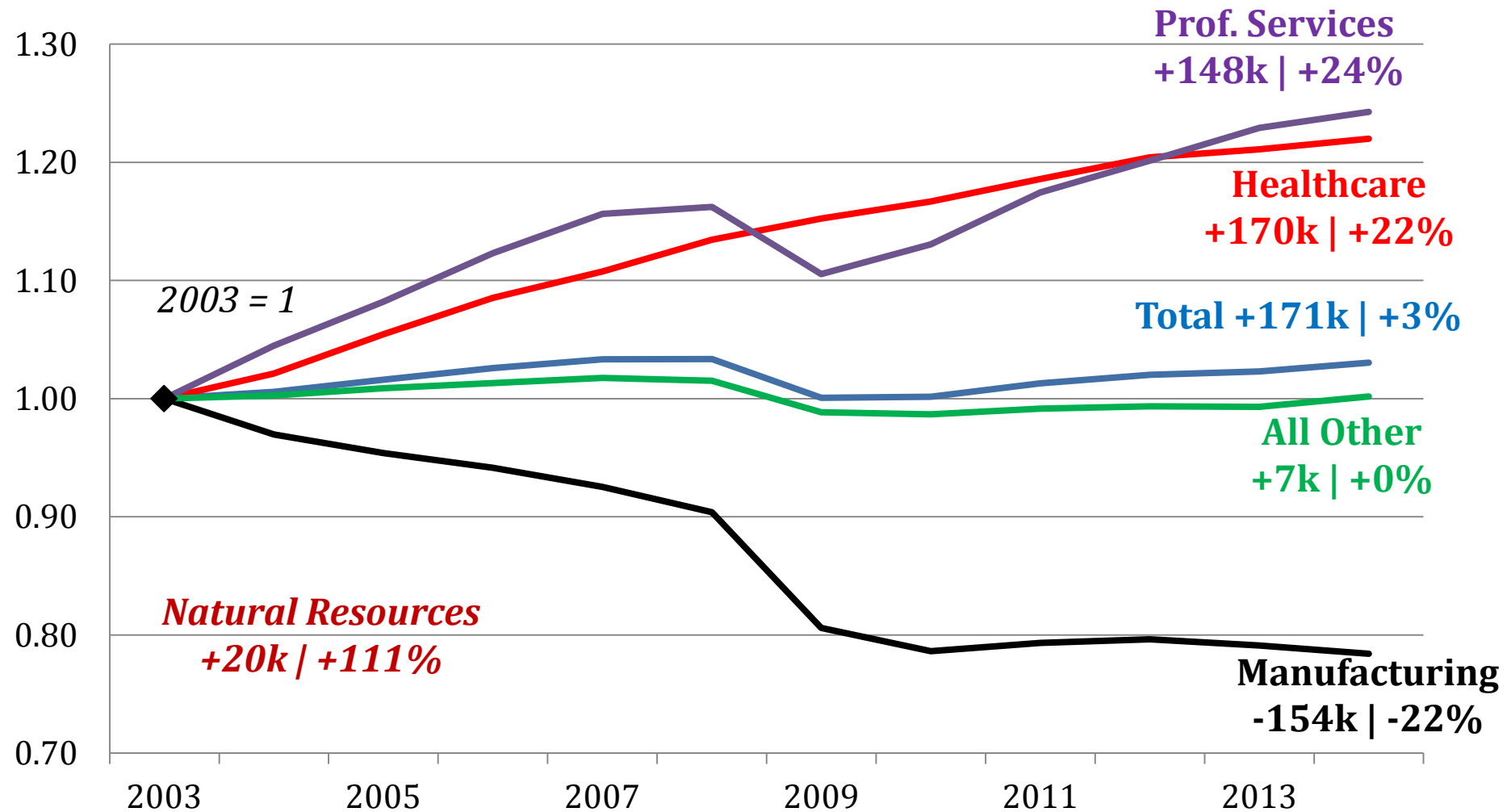
- Energy prices very low. Inflation and interest rates low.
- Flat wage growth. Many wage earners essentially treading water.
- Housing recovery less robust than assumed.

Pennsylvania Economic Forecast

	<u>Average Annual Growth Rate</u>		
	2002-08	2008-14	2014-20
Real State GDP	1.5%	0.8%	1.9%
Nominal State GDP	4.4%	2.5%	3.9%
Wages and Salaries	4.1%	2.1%	 4.0%
Consumer Price Index	3.3%	1.4%	1.9%
Average Job Gains (000s)	26.2	-2.7	 52.1

Source: Historical data from U.S. Bureau of Economic Analysis and U.S. Bureau of Labor Statistics.
Forecast by IFO based on published data through August 2014.

Change in Employment: 2003 to 2014



Source: U.S. Bureau of Labor Statistics. 2014 Q4 projection by Independent Fiscal Office.

A Continuation of Broad Trends

- **Expansion for Healthcare and Professional Service Sectors.**
 - Healthy PA to add 600,000 new enrollees.
 - Some uncertainty over the ACA.
- **Continued Contraction for Government Sector.**
 - Federal government sheds Postal Service jobs.
 - Local gov't contracts due to shrinking pupil base and pensions.
- **Exception: Labor Force Participation Rates.**
 - Forecast assumes a small increase for younger workers.

Fiscal Outlook

Year-to-Date Revenues
Long-Term Fiscal Imbalance
Tax Base Erosion

Fiscal Year-to-Date Revenues Strong

	FYTD Nov-13	FYTD Nov-14	Dollar Change	Percent Change	
General Fund	\$9,894	\$10,362	\$468	4.7%	← +3.7% adjusted
PIT – Withholding	3,504	3,624	121	3.4	
PIT – Other	566	570	4	0.7	
Sales and Use	3,808	3,998	190	5.0	← Motor Vehicle +8.1%, but moderating
Corporate Income	653	730	77	11.8	
Inheritance	355	450	95	26.8	←
All Other Tax	932	904	-28	-3.0	← +\$100 m. EP
All Non-Tax	77	87	9	12.0	← Cigs -\$32 m.

Note: millions of dollars. PIT is Personal Income Tax. FYTD is fiscal year-to-date.

Note: FY 2014-15 excludes \$227 million of transfers made in July from various funds.

Revenues Exceed IFO Projections

	IFO Forecast thru Nov-14	Actual thru Nov-14	Dollar Difference	
General Fund	\$10,227	\$10,362	\$135	← <i>\$109 relative to Admin. forecast</i>
PIT – Withholding	3,633	3,624	-9	
PIT – Other	590	570	-21	← <i>possible weakness</i>
Sales and Use	3,927	3,998	71	
Corporate Income	654	730	76	
Inheritance	354	450	95	← <i>one-time payment</i>
All Other Tax	895	904	8	
All Non-Tax	173	87	-86	← <i>\$80 liquor store profits</i>

Note: millions of dollars. PIT is Personal Income Tax.

Note: FY 2014-15 excludes \$227 million of transfers made in July from various funds.

FY 14-15 Revenues Remain Unclear

Description	Amount
Gains Through November Relative to IFO Estimate	\$135
Plus: Delayed Liquor Store Profits Deposit	80
Less: Projected Casino Fees	<u>-75</u>
Adjusted Revenue Gain	140
At Risk: Oil and Gas Lease Fund Transfer	95
Potential Net Gain	45

Note: millions of dollars.

Five-Year Outlook: Two Time Frames

- **The Snapback: FY 2014-15 to FY 2015-16.**
 - One-time revenues (FY 2014-15): \$572 million.
 - One-time savings: \$619 million.
 - One-time transfers: \$332 million.

- **Return to Trend: FY 2016-17 to FY 2019-20.**
 - Growth in pension contributions moderates.
 - By FY 2019-20, revenues and expenditures grow at roughly same rate (3.2 percent).

Long-Term Structural Imbalance

General Fund Balance Sheet (\$ millions)

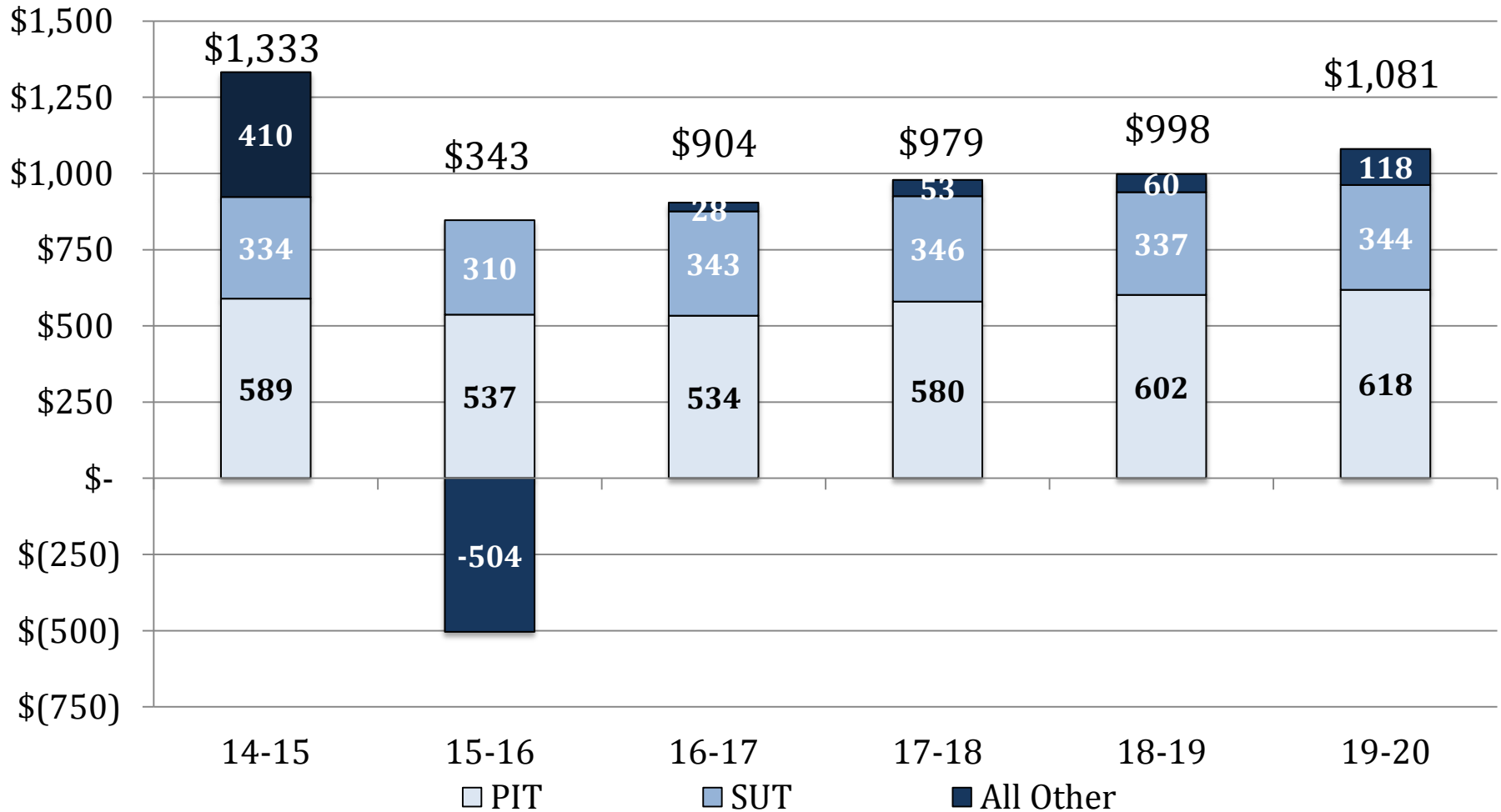
	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
Beginning Balance	\$81	\$--	\$--	\$--	\$--	\$--
Available Revenue	28,700	29,023	29,897	30,836	31,794	32,835
State Expenditures	-29,027	-30,777	-32,079	-33,280	-34,358	-35,464
Current Year Balance	-327	-1,754	-2,182	-2,444	-2,564	-2,629
Lapses and Supplementals	<u>75</u>	<u>75</u>	<u>75</u>	<u>75</u>	<u>75</u>	<u>75</u>
Ending Balance	-171	-1,679	-2,107	-2,369	-2,489	-2,554

FY 14-15 Non-Recurring Revenues

Description	Amount
Transfers from special funds (\$95 at risk)	\$322
Reduce holding period for unclaimed property (escheats)	150
Inheritance tax payment	<u>100</u>
Total	572

Note: millions of dollars.

Dollar Change in Revenues



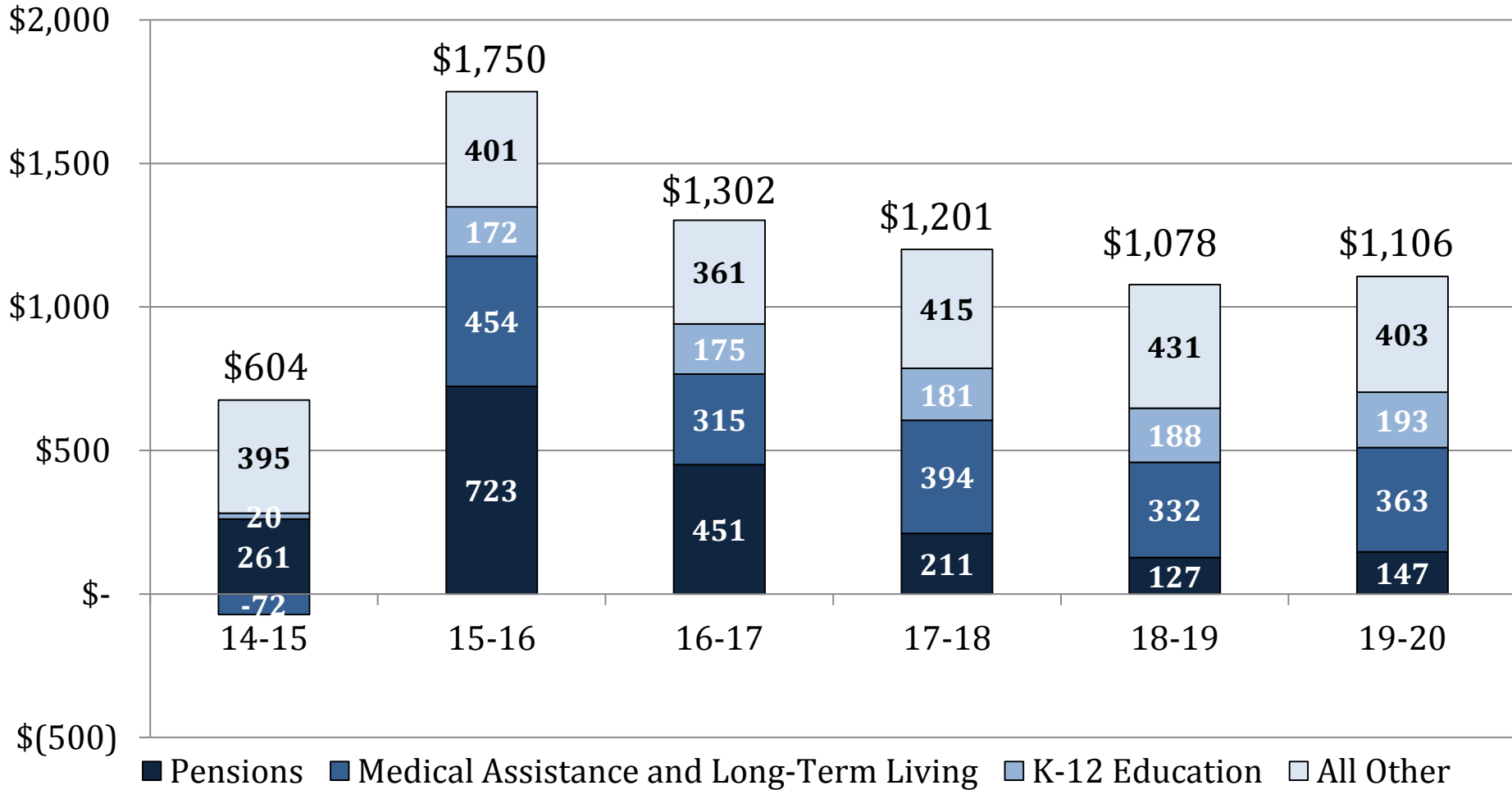
Note: millions of dollars.

FY 14-15 Non-Recurring Savings and Shifts

Description	Amount
Delay payments to managed care organizations	\$394
Transfer tobacco settlement investments to PSERS	<u>225</u>
Total Savings	619
From Tobacco Fund (to DHS)	\$144
From Lottery Fund (to DHS)	172
From Oil and Gas Lease Fund (to DCNR)	<u>16</u>
Total Shifts	332

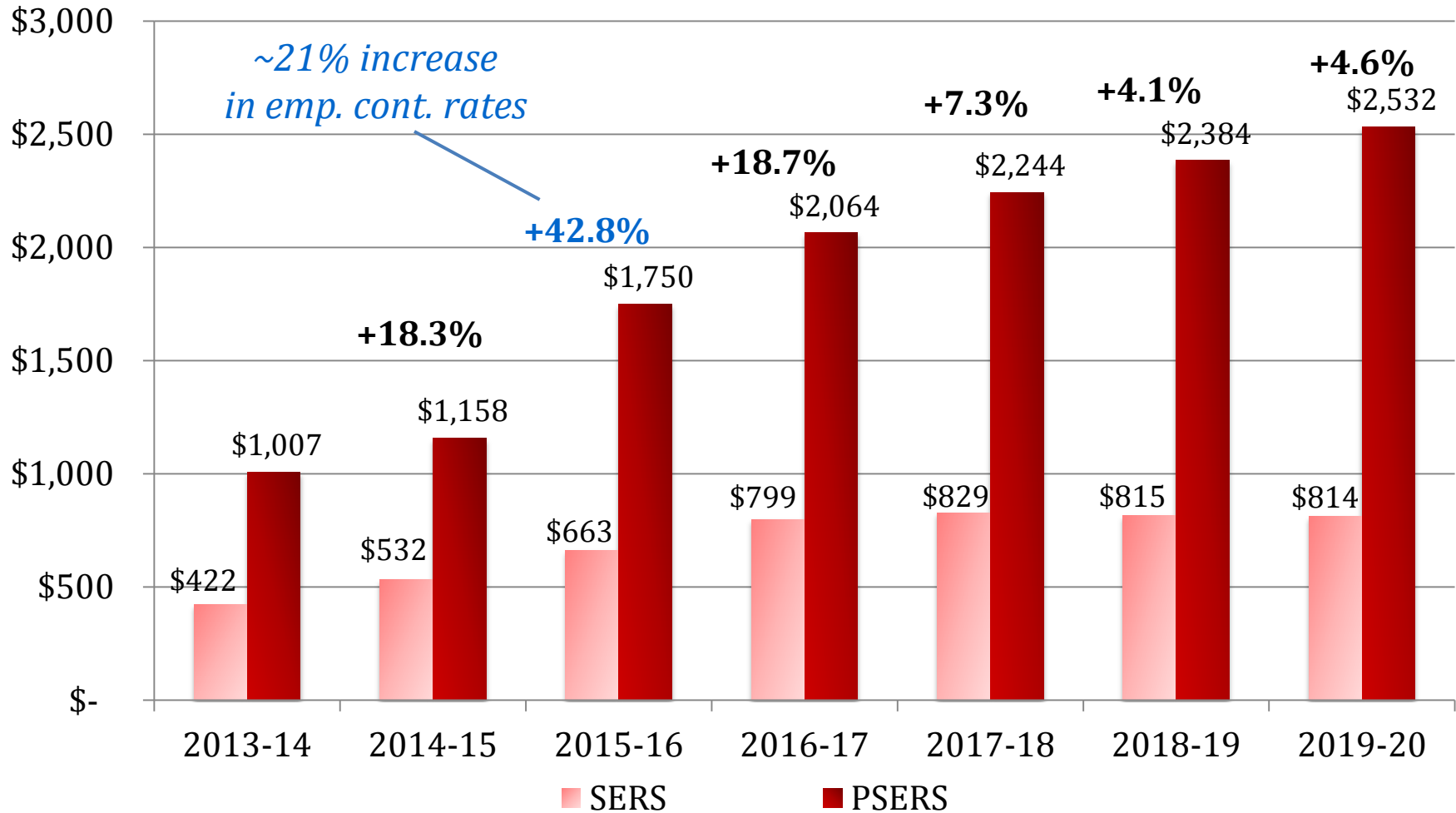
Note: millions of dollars.

Dollar Change in Expenditures



Note: millions of dollars.

Growth in Pension Contributions



Note: millions of dollars.

Tax Base Erosion

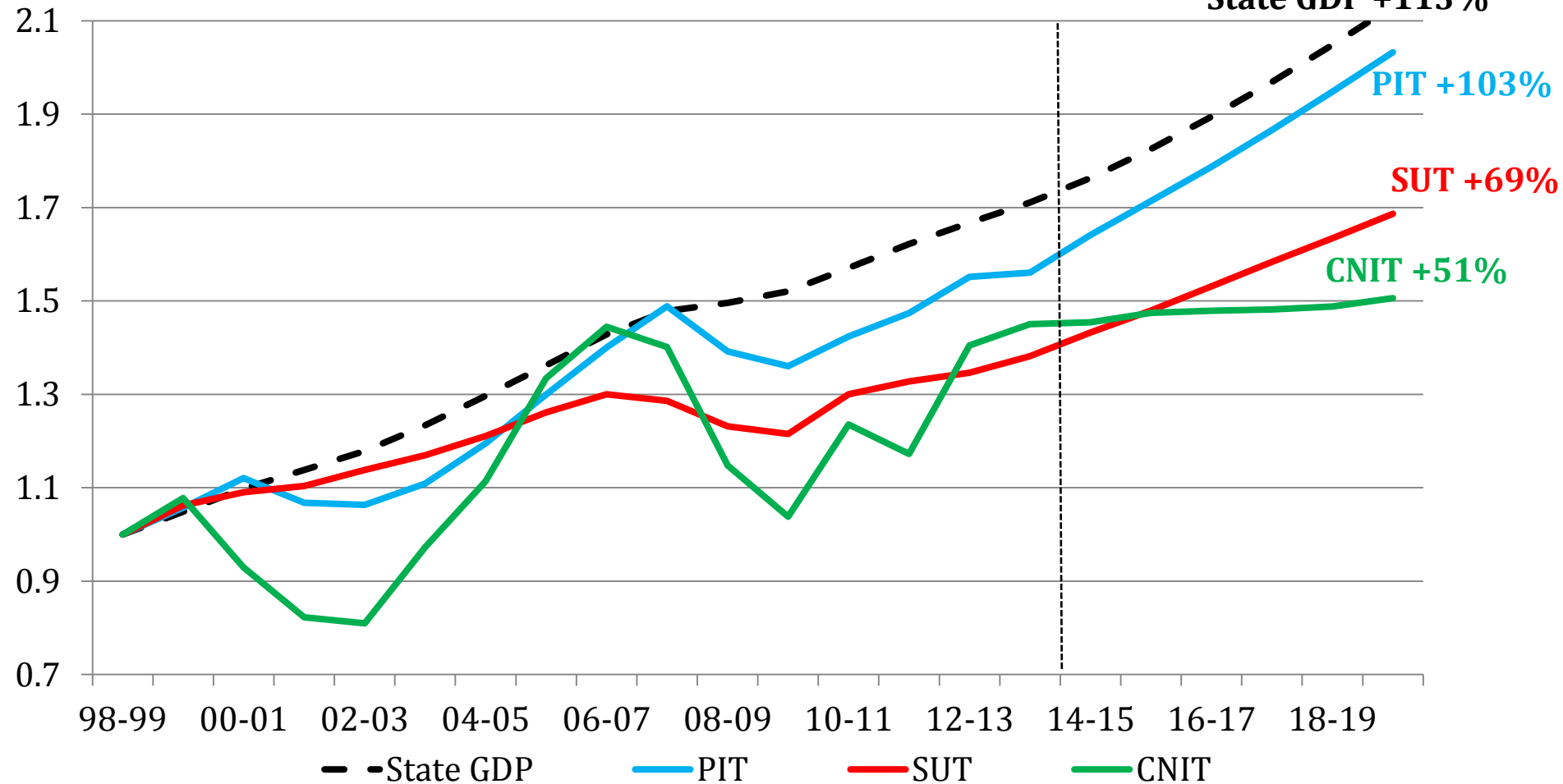
Cumulative Growth

State GDP +113%

PIT +103%

SUT +69%

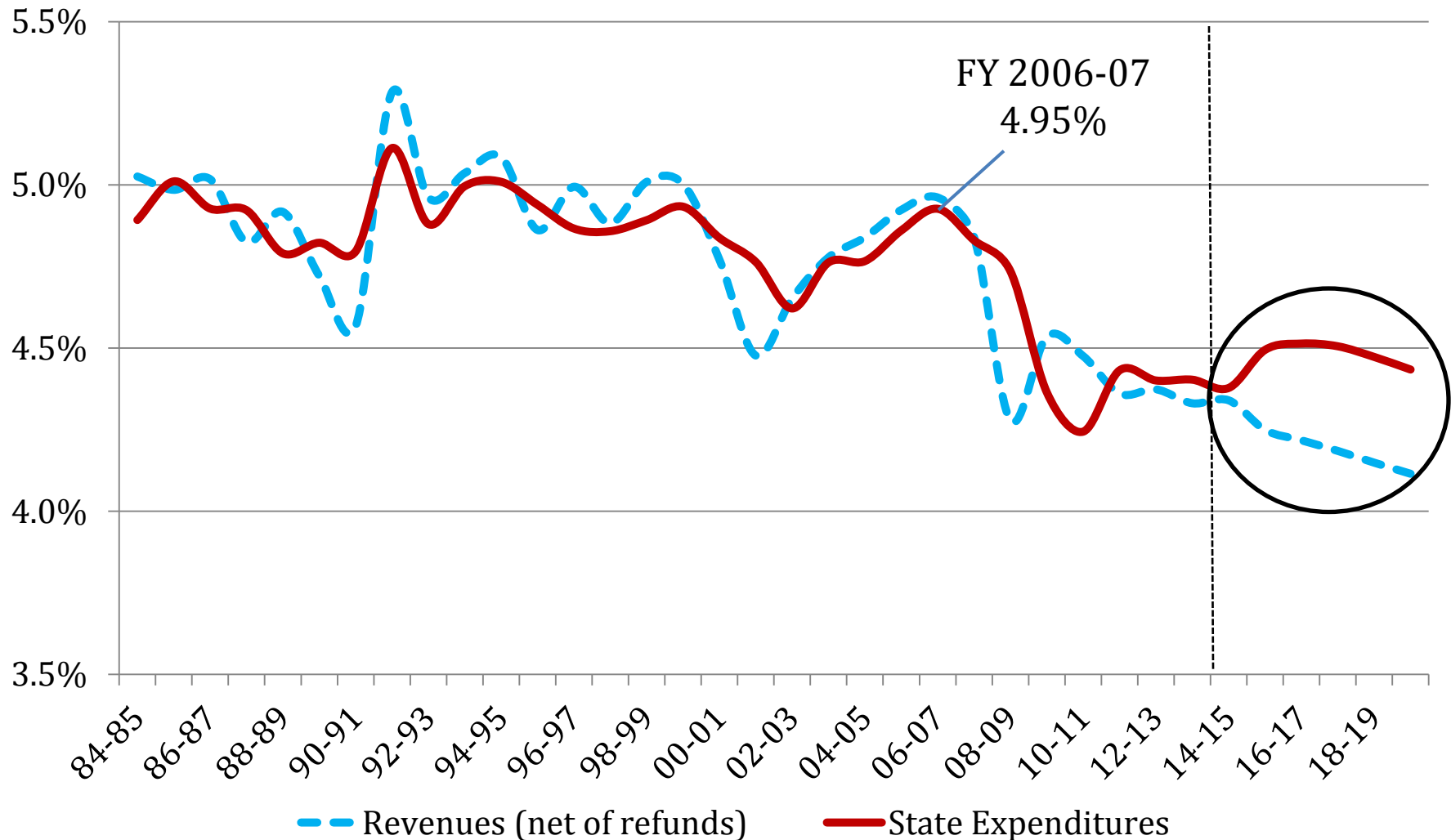
CNIT +51%



Note: PIT is adjusted for tax rate increase in 2004.

Relative Size of State Government

General Fund Revenues and Expenditures as a Share of State GDP



Wrap Up

- **Short and Long-Term Challenges for PA Budget.**
 - Short-Term: ~ \$1.5 billion of shifts/savings in FY 14-15.
 - Mid-Term: strong pension growth and policy changes.
 - Long-Term: moderate economic growth, aging populace and eroding tax base.

- **A Return to “Normal” Growth Does Not Help.**
 - Many problems are structural.
 - Will require very difficult policy choices.
 - All at once? Or many bites at the apple?