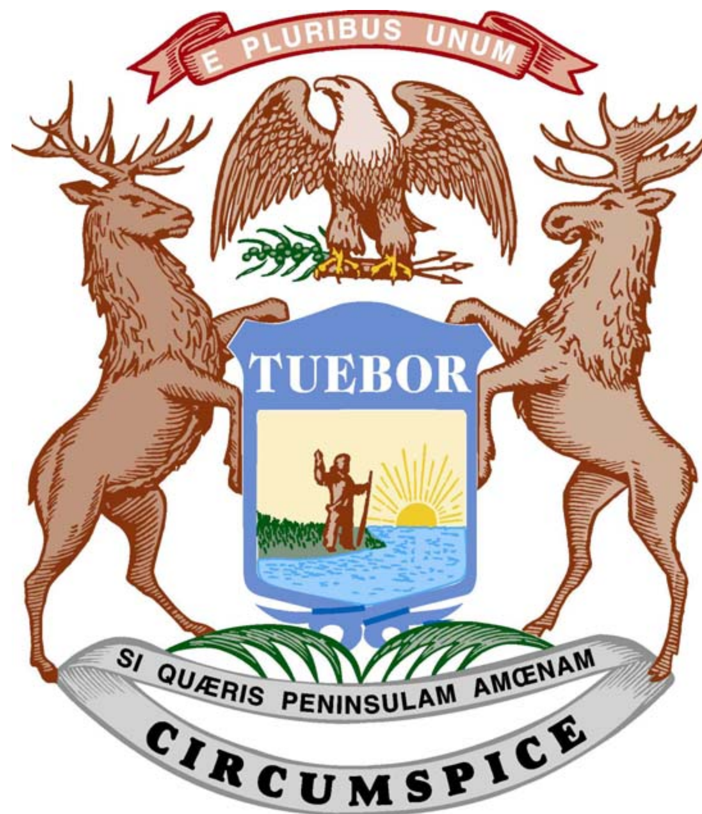
Administration Estimates Michigan Economic and Revenue Outlook



FY 2011-12, FY 2012-13 and FY 2013-14

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Table of Contents

Administration Estimates--Executive Summary 1

Revenue Review and Outlook 1

2012, 2013 and 2014 U.S. Economic Outlook 1

2012, 2013 and 2014 Michigan Economic Outlook 2

Forecast Risks 3

Economic Review and Outlook 4

Current U.S. Economic Situation 4
Summary 4
Housing Market 5
House Prices 7
Repercussions 7
Monetary Policy 10
Interest Rates 10
Additional Recent Federal Reserve Bank Actions 10
Fiscal Policy 11
Inflation 13
Major Economic Indicators 14
Employment 18
Vehicle Sales and Production 21

Current Michigan Economic Conditions 23
Vehicle Production 23
Employment 24
Housing Market 25
Personal Income 26

2012, 2013 and 2014 U.S. Economic Outlook 27
Summary 27
Assumptions 29
Forecast Risks 29

2012, 2013 and 2014 Michigan Economic Outlook 31

Fiscal Year Economics 35

Administration Revenue Estimates 37

Revenue Estimate Overview 37

FY 2011 Revenue Review 38

FY 2012 Revenue Outlook 39

FY 2013 Revenue Outlook 40

FY 2014 Revenue Outlook 41

Constitutional Revenue Limit 42

Budget Stabilization Fund Calculation 42

School Aid Fund Revenue Adjustment Factor 45

Revenue Detail 47

List of Tables

Table 1 **Administration Economic Forecast** 34

Table 2 **FY 2010–11 Administration Revenue Estimates** 38

Table 3 **FY 2011–12 Administration Revenue Estimates** 39

Table 4 **FY 2012–13 Administration Revenue Estimates** 40

Table 5 **FY 2013–14 Administration Revenue Estimates** 41

Table 6 **Administration Constitutional Revenue Limit Calculation** 42

Table 7 **Budget and Economic Stabilization Fund Calculation, Based on CY 2012 Personal Income Growth, Administration Calculation** 43

Table 8 **Budget and Economic Stabilization Fund Calculation, Based on CY 2013 Personal Income Growth, Administration Calculation** 44

Table 9 **Budget and Economic Stabilization Fund Calculation, Based on CY 2014 Personal Income Growth, Administration Calculation** 45

Table 10 Administration School Aid Revenue Adjustment Factor for FY 2013 46

Table 11 Administration School Aid Revenue Adjustment Factor for FY 2014 46

Table 12 Administration General Fund General Purpose Revenue Detail 48

Table 13 Administration School Aid Fund Revenue Detail 49

Table 14 Administration Major Tax Totals 49

ADMINISTRATION ESTIMATES
EXECUTIVE SUMMARY
January 13, 2012

Revenue Review and Outlook

- FY 2011 General Fund-General Purpose (GF-GP) revenue totaled $8,813.0 million, a 14.8 percent increase from 2010. FY 2011 School Aid Fund (SAF) revenue rose 4.0 percent to $11,248.2 million.

- FY 2012 GF-GP revenue is forecast to increase 1.0 percent to $8,897.0 million, up $144.5 million from the May 2011 Consensus estimate. FY 2012 SAF revenue is forecast to decrease 3.8 percent to $10,824.5 million, which is $199.2 million above the May 2011 Consensus estimate. Tax restructuring and elimination of the Michigan Business Tax earmarking to the School Aid Fund is the primary reason for the decline in revenue.

- FY 2013 GF-GP revenue is forecast to increase 1.4 percent to $9,019.6 million, up $111.5 million from the May 2011 Consensus estimate. FY 2013 SAF revenue is forecast to increase 3.0 percent to $11,149.8 million, up $184.6 million from the May 2011 Consensus estimate.

- FY 2014 GF-GP revenue is forecast to increase 2.5 percent to $9,240.2 million. FY 2014 SAF revenue is forecast to increase 2.9 percent to $11,474.0 million.

2012, 2013 and 2014 U.S. Economic Outlook

- After increasing an estimated 1.8 percent in 2011, real gross domestic product will accelerate gradually over the forecast period with 2.2 percent growth in 2012, a 2.4 increase in 2013 and a 2.9 percent increase in 2014.

- In 2011, U.S. wage and salary employment is estimated to have risen 1.0 percent. Employment is then forecast to increase 1.1 percent in 2012, 1.4 percent in 2013 and 1.6 percent in 2014. The national labor market is expected to regain 5.9 million jobs between the end of 2011 and the end of 2014.

- The U.S. unemployment rate is forecast to decline each quarter over the forecast horizon. The unemployment rate is expected to average 9.0 percent in 2012. In 2013, the unemployment rate is projected to fall to 8.8 percent and then decrease to 8.3 percent in 2014.

- In 2009, housing starts fell to a 50-year low (554,000 units) and then rose modestly in 2010. While growing only slightly in 2011, starts are expected to grow sharply in 2012 (21.1 percent) and in 2013 (23.5 percent). In 2014, starts are forecast to rise 10.4 percent to 987,000 units, which would still be the seventh straight year with starts below 1.0 million.

- Light vehicle sales are expected to post significant growth across the forecast. In 2012, sales are forecast to rise in 2011 to 13.8 million units from 12.7 million units. Sales in 2013 are expected to increase to 14.6 million units. At 15.3 million units in 2014, light vehicle sales are expected to rise above 15.0 million units for the first year since 2007.

- In 2011, consumer prices are estimated to have risen 3.2 percent. Prices are expected to increase 2.3 percent in 2012. Inflation is expected to slow to 2.1 percent in 2013 and 2014.

2012, 2013 and 2014 Michigan Economic Outlook

- In 2009, Michigan wage and salary employment plummeted 7.0 percent – the largest drop in over 50 years. After declining just 0.3 percent in 2010, employment posted an estimated 1.7 increase, an increase of 66,000 jobs, in 2011 – marking the first increase since 2000. Employment is forecast to grow 0.8 percent in 2012, 1.0 percent in 2013 and 1.3 percent in 2014.

- The Michigan unemployment rate is estimated to have dropped from 12.5 percent in 2010 to 10.7 percent in 2011. The rate is expected to decline to 10.3 percent in 2012, to 10.0 percent in 2013 and to 9.7 percent in 2014.

- After dropping a record 8.2 percent in 2009, wages and salaries increased 1.7 percent in 2010 and rose an estimated 5.9 percent in 2011. Wages are expected to grow 3.3 percent in 2012, 4.2 percent in 2013 and 3.8 percent in 2014.

- Michigan personal income fell 5.4 percent in 2009 – marking the first annual Michigan income drop since 1958. Income increased 3.3 percent in 2010 and rose an estimated 5.8 percent in 2011. Personal income is forecast to grow 3.1 percent both in 2012 and in 2013 and then increase 4.4 percent in 2014.

- Disposable income is forecast to rise 3.0 percent in FY 2012, 2.6 percent in FY 2013 and 3.2 percent in FY 2014.

Forecast Risks

- Europe’s growing financial crises may severely weaken the continent’s economic growth and have extremely negative financial and economic impacts on the U.S. economy.

- Conflict with Iran over access to the Strait of Hormuz is the latest risk to the supply of oil. Higher than forecast oil prices would lower consumers’ discretionary income, increase many businesses costs and depress economic activity.

- Higher than forecast oil prices would depress economic activity by lowering consumer’s discretionary income and increasing the likelihood of anti-inflation monetary policy. Lower than forecast oil prices would help boost economic activity.

- Unrest throughout the Middle East could seriously impact economic growth. Geopolitical factors, such as a domestic terrorist attack, would depress economic activity.

- A stronger (weaker) housing market would boost (depress) the economy more than forecast.

- Continued and greater division among federal policymakers could substantially weaken consumer and investor confidence. Increased polarization also substantially limits the federal government’s ability to respond to negative financial and macroeconomic shocks. In addition, the Federal Reserve has moved to less aggressive policies – reducing the Fed’s effectiveness to address financial crises. On the other hand, the Fed may respond with more aggressive policies such as a third round of quantitative easing.

- Continued and strong job growth remains central to sustaining recent gains across the economy and to combating dampening factors such as weak consumer confidence.

- The Great Recession may have a more longer term persistent negative effect on confidence than assumed.

ECONOMIC REVIEW AND OUTLOOK
January 13, 2012

Current U.S. Economic Situation

Summary

In June 2009 (2009Q2), the longest economic downturn (18 months/6 quarters) since the Great Depression ended – as determined by the National Bureau of Economic Research. Over the recession's six quarters, real GDP fell 5.1 percent – the greatest recessionary decline on record (dating back to 1948).

Real GDP has grown each quarter since the recession's end (2009Q3 – 2011Q3). After reporting modest growth in 2009Q3, the U.S. economy reported strong growth over the following three quarters with annualized growth averaging 3.8 percent. The growth rate averaged 2.4 percent over the second half of 2010. Growth then slowed substantially to a 0.4 percent annual rate in 2011Q1. While growth accelerated over the next two quarters, the economy registered just 1.8 growth in 2011Q3. Consequently, it required nine quarters into the recovery before the U.S. economy grew larger than at the beginning of the Great Recession. In the previous ten recessions, it had taken no more than three quarters for post-recession real GDP to exceed real GDP at the recession's outset. Real GDP in 2011Q3 was 5.5 percent larger than at the end of the Great Recession (2009Q2).

During the recovery to date, greater equipment investment and inventory accumulation taken together account for 65.6 percent of the overall net real GDP gain. Consumption increases equal 63.0 percent of the overall real GDP gain. At the same time, continued declines in investment in residential and non-residential structures (-7.4 percent) and a worsening trade deficit (-10.3 percent) have detracted from growth. Federal government spending has added to real GDP growth (+5.0 percent) while lower state and local government spending has subtracted from growth (-10.2 percent).

Over the course of the recession, U.S. wage and salary employment shrank by 5.4 percent – the greatest recessionary employment decline since 1945. In addition, employment declined in the first eight months of the current recovery. As a result, between December 2007 and February 2010, the U.S. lost a net 8.7 million jobs (-6.3 percent). In early 2010, wage and salary employment recorded substantial gains between March and May (totaling 927,000 jobs) -- boosted significantly by temporary Census worker hiring. However, in part depressed by the end of many temporary Census jobs, the economy lost a net 329,000 jobs between June and September.

Employment has risen each month since October 2010. Consequently, U.S. wage and salary employment increased 940,000 jobs over the course of 2010. The 2010 employment gain stands in sharp contrast to the economy's net loss of 5.1 million jobs in 2009. In 2011, the U.S. gained an additional 1.6 million jobs. Thus, the U.S. labor market has gained a net 1.2 million jobs

since the recession's end, but December 2011 jobs still remain 6.1 million lower than at the beginning of the Great Recession.

Housing Market

The housing market remains little improved from the record lows to which the market fell. The market was buoyed by the homebuyer credit but worsened considerably directly following the credit's April 30, 2010 expiration. The market has regained only slight ground since its post-credit decline and shows little indication of having the strength to return anywhere close to its historic norms. In its November 2011 *Beige Book,* the Federal Reserve characterized both residential and commercial real estate markets as remaining "sluggish." RealtyTrac sees an impending jump in foreclosures:

> Despite a seasonal slowdown similar to what we've seen in each of the past four years, November's [2011] numbers suggest a new set of incoming foreclosure waves, many of which may roll into the market as REOs (bank-owned homes) or short sales sometime early next year.

In calendar year 2008, housing starts fell below 1.0 million units (905,500 units) for the first time on record. The housing market then worsened considerably in 2009, falling 38.8 percent to only 554,000 units. Starts rose only slightly in 2010 to 586,900 units (5.9 percent). This performance stands in sharp contrast to the 2.1 million unit pace in 2005 or even the 1.8 million units and 1.4 million units in 2006 and 2007, respectively. With the impending end of the home buyer credit, annualized April 2010 housing starts were up 43.7 percent from a year earlier when starts had fallen to a record low (478,000 units annualized rate). At 687,000 units, April 2010 starts represent the highest starts have been since the end of the recession. Since the home buyer credit's expiration, starts have moderated -- averaging 585,000 units. However, in the past six months, starts have averaged 629,000 units with November recording the second highest starts rate since the Great Recession (685,000 units).

In December 2011, the National Association of Realtors (NAR) revised historical existing home sales between January 2008 and October 2011. The revisions show that Great Recession sales were substantially worse than previously estimated. The NAR revised 2008 existing home sales down 16 percent from 4.91 million units to 4.11 million units. In addition, recent sales estimates were revised down. In particular, existing home sales in the first ten months of 2011 were revised down 14 percent to an average annual rate of 4.25 million units. Nevertheless, revised sales estimates in each month between July 2011 and November 2011 were up substantially with year-over-year increases exceeding 10 percent each month.

In its November 2011 sales release, the National Association of Realtors commented:

> Sales reached the highest mark in 10 months and are 34 percent above the cyclical low point in mid-2010 – a genuine sustained sales recovery appears to be developing. We've seen healthy gains in contract activity, so it looks like more people are realizing the great opportunity that exists in today's market for buyers with long-term plans.

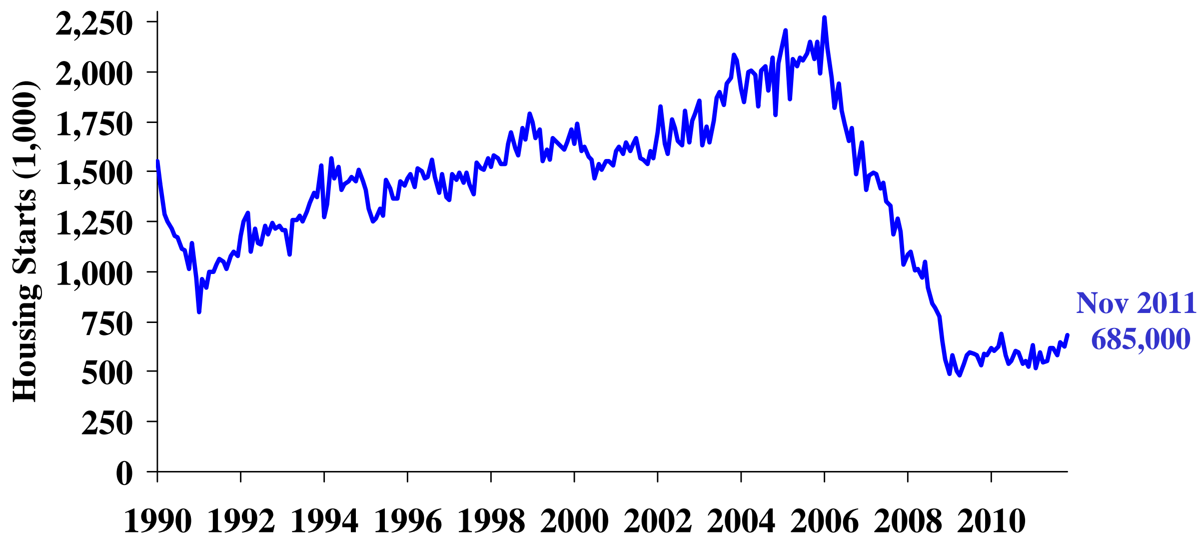
In December 2011, the average 30-year mortgage rate fell to 3.96 percent (a record low with records going back to 1971). A year ago, the rate was 4.30 percent. In mid-December 2011, the weekly average rate dropped to 3.94 percent – a new weekly low.

Compared to a year ago, the Mortgage Bankers Association's weekly market composite index has risen 37.4 percent. However, a large increase in the refinancing sub-index (60.1 percent) accounts for more than all of the composite index increase. The purchase sub-index is down 7.0 percent.

In December 2011, the National Association of Home Builders (NAHB) sentiment index was up two points from a month ago and five points higher than December 2010. At 21, the index stands at its highest level since early 2008. However, the November 2011 reading remains well below 50.0 – indicating substantial and widespread builder pessimism.

In 2009, the National Association of Realtors pending home sales index (a housing market leading indicator) increased 9.0 percent from 2008 to 95.0. However, the index dropped 5.9 percent in 2010 to 89.3. Through the first eleven months of 2011, the index has averaged 89.9 – slightly higher than the 2010 calendar year reading. After three straight monthly declines, the index rose sharply in both October and November. As a result, November's reading was up 5.9 percent from last November – rising to 100.1 – the index's highest level since April 2010 (the last month of the homebuyer tax credit).

Housing Starts Remain
Little Changed from Record Low



Source: U.S. Census Bureau. Seasonally adjusted annual rate.

House Prices

Between October 2010 and October 2011, the Federal Housing Finance Agency's (FHFA) purchase-only home price index (HPI) fell 2.8 percent. Since the May Consensus Conference, year-over-year declines have lessened – easing from mid-year 2011 declines averaging 6.0 percent. However, compared to the index's all-time peak (April 2007), the October 2011 reading is down 19.2 percent.

The Census Bureau's November 2011 median new home sales price was down 2.5 percent from a year ago. In comparison, the median price *rose* 7.9 percent between April 2010 and April 2011 (the last month available prior to the May Conference). According to the National Association of Realtors, the median existing-house price was down 3.5 percent between November 2010 and November 2011 compared to a 6.5 percent year-over-year decrease in April 2011. Through November 2011, the year-to-date 2011 median existing home price was 4.6 percent below last year.

The S&P/Case Shiller 20-city home price index (seasonally adjusted) reported month-to-month decreases in 16 of the past 17 months (June 2010-October 2011). Over this time period, the home price index fell 6.2 percent. Compared to a year ago, the index (non-seasonally adjusted) was down 3.4 percent -- marking the 13th straight year-over year decline. However, the year-to-year decline has shrunk in each of the past five months.

Repercussions

The depressed housing market and concomitant home price declines -- along with a poor jobs market – have had serious repercussions including high delinquency and foreclosure rates, sharp drops in homeowner equity and consumer net worth and lower stock prices. While many of these factors are still poor, some have recently improved significantly.

The most recent Mortgage Bankers Association's (MBA) National Delinquency Survey released in November 2011 provided a mixed picture of the home mortgage market. MBA reported that the mortgage delinquency rate for mortgage loans decreased to a seasonally adjusted rate of 7.99 percent of all loans outstanding in 2011Q3, down 45 basis points from 2011Q2, and a decrease of 114 basis points from one year ago. The 7.99 percent is the lowest delinquency rate in nearly three years (2008Q4). The 2011Q3 seriously delinquency rate, the percentage of loans that are 90 days or more past due or in the process of foreclosure, was 7.89 percent, an increase of four basis points from 2011Q2, but a decrease of 81 basis points from 2010Q3.

Further, looking at relatively new delinquencies, the MBA is encouraged: "The thirty day delinquency rate, the measure of early stage delinquency, reached its lowest level since the second quarter of 2007, a sign that new mortgage delinquencies have slowed." However, the percentage of loans on which foreclosure actions were started during the third quarter was 1.08 percent, up 12 basis points from last quarter and down 26 basis points from one year ago. Despite the year-over-year decline, the MBA sees reason for concern about the increase from last quarter: "Foreclosure starts, however, increased this quarter, the first increase in a year after

declining for three straight quarters, and is now back up to the levels of the first quarter of 2011. This is largely driven by loans leaving the loss mitigation process and the ending of state remediation programs and foreclosure moratoria."

Declining home prices have meant lower homeowner equity (house value less mortgage debt). Each quarter between 2007Q1 and 2009Q1, inclusive, the *amount* of homeowner equity fell. Over this period, the amount of homeowner equity fell by $6.6 trillion (-51.6 percent). As a result, the homeowner equity rate (the amount of homeowner equity/homeowner real estate value) dropped by 19.3 percentage points falling from 56.6 percent to 37.2 percent. Prior to the current housing bust, the homeowner equity rate had never fallen below 50 percent.

Each quarter between 2009Q2 to 2010Q1 (inclusive), the amount of homeowner equity rose. As a result, $781.1 billion in homeowner equity was recouped. However, in the last six quarters, homeowner equity, on net, has given up nearly all (97.1 percent) of the equity that had been gained in the prior four quarters. Between 2009Q2 and 2011Q3, homeowner equity increased a net $22.6 billion and the homeowner equity rate rose 1.5 percentage points to 38.7 percent. This slight net gain still leaves homeowners with $6.6 trillion less in homeowner equity than at the end of 2006 and a 17.8 percentage point decline in the homeowner equity rate.

According to CoreLogic, 22.1 percent of residential properties with mortgages in 2011Q3 were "under water" (borrowers owe more on their mortgages than their homes are worth). Near negative equity properties (less than five percent equity) accounted for another five percent of residential properties. In 2011Q3, 10.7 million residential properties were underwater -- down from 10.9 million properties in the prior quarter. As a result, the "underwater" properties rate fell from 22.5 percent to 22.1 percent. Nevertheless the share of underwater properties remains historically high. In addition, the recent declines are largely attributable to a rise in foreclosures.

One positive repercussion from lower housing prices is that overall housing affordability has improved to record levels. According to Case-Shiller "The monthly mortgage payment for a median-priced single-family home is now $700, compared to $1,140 in 2006 — a decline of nearly 40 percent. Nationally, purchase mortgage payments now account for only 13 percent of monthly median family income, the lowest percentage on record (since 1971), and compared to 23 percent in the first quarter of 2006."

According to the Federal Reserve, the overall real estate loan delinquency rate has fallen over the past six quarters by 1.72 percentage points to 8.52 percent in 2011Q3. However, the rate remains well above the 2.35 percent in 2007Q3 – the quarter directly prior to the recession. Similarly, the residential property loan delinquency rate has dropped by 1.28 percentage points to 10.08 percent over the past six quarters. However, the rate remains well above the 2.73 percent rate directly prior to the recession.

According to the Federal Reserve Senior Loan Officer Opinion Survey, in each of the past eight quarters, more banks reported loosening lending standards for large and mid-sized firms than reported tightening standards. In 2011Q3, a net 21.8 percent of banks reported loosening standards – the highest net percent loosening since 2005Q2. However, net loosening fell to 5.9 percent in 2011Q4.

While households borrowed at a $715.9 billion annual rate in 2007Q4, that rate dropped by 36.3 percent in 2008Q1. In 2008Q3, households, on net, *reduced* their debt levels (seasonally adjusted) for the first time in the series' history dating back to 1952. Through 2011Q3, households continued to pay down their debt levels. Between 2008Q1 and 2011Q3, households reduced their debt levels by $688.5 billion (5.0 percent) to their lowest levels since 2007Q1.

The annual savings rate rose substantially between 2007 and 2008 from 2.4 percent to 5.4 percent – the highest annual savings rate since 1993. The savings rate fluctuated slightly in 2009 (5.1 percent) and 2010 (5.3 percent). Between 2008Q4 and 2011Q2, the savings rate exceeded 4.0 percent each quarter. However, the rate fell to 3.9 percent in 2011Q3. Further, in each of the past four quarters (2010Q4- 2011Q3), the savings rate has fallen – reducing the rate from 5.6 percent to 3.9 percent.

Between 2007Q3 and 2009Q1, overall consumer net worth fell each quarter compared to the prior quarter. Over this period, net worth declined by $16.3 trillion (24.5 percent). Prior to these declines, net worth had never fallen for more than two straight quarters in a history dating back to 1952. Each quarter between 2009Q2 and 2010Q1, net worth increased from the prior quarter. As a result, net worth regained $6.0 trillion of the $16.3 trillion that it had lost. After falling $1.2 billion in 2010Q2, net worth rose in the following five quarters between 2010Q2 and 2011Q3. Consequently, 2011Q3 net worth ($57.4 trillion) stood $6.9 trillion higher than in 2009Q1. However, 2011Q3 net worth is still 14.1 percent ($9.4 trillion) less than its all-time peak reached in 2007Q2 level.

Spillover into broader financial markets meant sharp declines in stock prices along with the sharp house price declines. The U.S. stock market plummeted following Lehman Brother's declaring bankruptcy in mid September 2008. From the last trading day before the Lehman bankruptcy (September 12, 2008) and the market's March 9, 2009 trough, the Wilshire 5000 index lost nearly half (46.3 percent) of its value. The market trended upward through April 2010. Between late April 2010 and mid July 2010, the market lost 13.2 percent. Then, between early July 2010 and late April 2011, the market rose 35.5 percent. After stumbling over the next few months and recording substantial losses between late July and mid-August, the Wilshire 5000 hit its trough for 2011 in early October with the index down 13.3 percent for the year. The market fluctuated through mid-November but then fell significantly over the second half of month. However, the market trended upward in early December before fluctuating over the remainder of the year. At the end of calendar year 2011, the market was down 1.4 percent from the end of 2010 and was off 9.2 percent from its 2011 peak (April 29).

There have been some indications that investor worries remain well below late 2008 levels but have grown recently in the midst of federal government paralysis and the European debt crisis.

In fall 2008, at the height of the financial crisis, banks were extremely wary of lending to each other. However, this wariness has lessened considerably. The TED spread (the difference between the three-month LIBOR rate, a benchmark for the rate banks charge each other to borrow from one another, and the 90-day Treasury bill rate) provides a good measure of banks' wariness to lend to one another. In mid-October 2008, the TED spread rose to a record 4.63

percentage points. However, by late December, the spread had fallen to its prior low level (0.20 percentage point) in late December 2009. In early March 2010, the spread dropped to a new record low (0.10 percentage points). The European credit crisis and U.S. government deadlocks increased the spread. As a result, by the end of November 2011, the spread had risen to 0.48 percentage point.

The junk (below investment grade) corporate bond market provides an indication of the bond market's lending wariness. In mid-December 2008, at the height of the financial crisis and credit freeze, those buying junk corporate bonds were demanding a record 21.8 percentage points higher interest rate (a 21.8 percentage point spread). By late July 2011, the spread dropped to 4.25 points – a full point lower than the average spread since 1984. The substantial junk bond issuance also highlights investors' reduced risk aversion. Junk bond issuance rose to a record high in 2011Q3. However, by early December 2011, the spread had increased substantially – rising to 7.79 points.

Monetary Policy

Interest Rates

Faced with credit market tightening, turmoil in the financial markets and the floundering housing market, the Federal Open Market Committee (FOMC) began cutting the target federal funds rate in September 2007. At its December 16, 2008 meeting, the FOMC took an unprecedented step and lowered the target federal funds rate range to 0.00 percent to 0.25 percent. At the same time, the FOMC cut the discount rate to 0.50 percent, its lowest level since the 1940s. Between September 2007 and December 2008, the Federal Reserve cut the target federal funds rate ten times and the discount rate eleven times. As a result, the target federal funds rate was cut a total of 500-525 basis points and the discount rate was cut 525 basis points.

Prior to its July 2011 meeting, the Fed stated that it would keep rates low "for an extended period of time." Beginning in July, the FOMC made explicit that it will leave rates low at least through mid-2013. The FOMC stated at its December 13, 2011 meeting:

> The Committee also decided to keep the target range for the federal funds rate at 0 to 1/4 percent and currently anticipates that economic conditions--including low rates of resource utilization and a subdued outlook for inflation over the medium run--are likely to warrant exceptionally low levels for the federal funds rate at least through mid-2013.

Additional Recent Federal Reserve Bank Actions

In addition to dramatically lowering its key interest rates to record low levels, the Federal Reserve (Fed) also addressed the financial and economic crises by injecting substantial liquidity into financial markets. Between mid-September 2008 and mid-December 2008, Federal Reserve Bank credit more than doubled from $891.5 billion to $2,236.9 billion.

In August 2010, the Fed announced that it would keep its securities holdings essentially unchanged by reinvesting the principal payments from the agency debt and agency mortgage-backed securities in longer-term Treasury securities and rolling over the Treasuries as they mature. The Fed has continued rolling over maturing Treasuries and reaffirmed at its most recent meeting (mid-December 2011) that it would continue the practice. In a second round of quantitative easing (QE2), the Fed purchased an additional $600 billion of longer-term Treasuries between November 2010 and June 2011. At the end of December 2011, Federal Reserve Bank credit stood at $2,920.3 billion – more that three times Fed credit in mid-2008 and a record high.

At its September 2011 meeting, the Fed announced that, by June 2012, it would purchase $400 billion of longer-term Treasuries while selling $400 billion in shorter-tem Treasuries (Operation Twist) over the same time period. In doing so, the Fed is aiming to depress longer-term interest rates and, thus "contribute to a broad easing in financial market conditions that will provide additional stimulus to support the economic recovery."

Fiscal Policy

Averting a partial government shutdown and federal government default, Congress and the President reached an agreement, in early August 2011, to raise the federal debt ceiling by $900 billion of which $400 billion was immediately available (Budget Control Act of 2011). In exchange for the $900 billion ceiling increase, the Act specified $917 billion of cuts over 10 years with less than three percent of the cuts in FY 2012. In addition, the Act established a Joint Select Committee on Deficit Reduction (Super Committee). Composed of six Democratic legislators and six Republican legislators, the Committee was charged with producing legislation to cut at least $1.5 trillion over the next 10 years. Failure by the Committee to produce the legislation by November 23, 2011 would trigger "across the board" $1.2 trillion cuts over the next ten years.

Despite the Act's enactment, Standard and Poor's — for the first time in the agency's history -- downgraded the federal government bond rating from AAA to AA+ only days after the Act's enactment. Explaining the downgrade, the S&P stated that it was "pessimistic about the capacity of Congress and the administration to be able to leverage their agreement this week into a broader fiscal consolidation plan that stabilizes the government's debt dynamics anytime soon." The other two major rating agencies maintained the federal government's AAA status, but put the federal government on negative outlook.

The Super Committee failed to produce deficit reduction legislation. However, considerable uncertainty surrounds the composition and timing of the "automatic" cuts. For example, questions have been raised about the automatic defense budget cuts.

In late December, Congress and the President reached an agreement on a two-month extension of some elements of the American Recovery and Reinvestment Act due to expire at the end of calendar year 2011 including the two percentage point reduction in the employee portion of the Social Security payroll tax rate from 6.2 percent to 4.2 percent and the expansion of

unemployment benefits from 26 weeks to 99 weeks. Uncertainty remains as to whether these provisions will be extended further.

Questions also remain about whether to extend still further Bush tax cuts that are now scheduled to expire at the end of 2012. These tax cuts include:

- Lower individual income tax rates enacted in 2001. Without further extension, income tax rates will revert to higher rates in effect prior to the original 2001 legislation.
- Lower capital gains/dividends tax rates.
- $1,000 child tax credit (due to revert to $500).

In addition, uncertainty remains surrounds whether the Alternative Minimum Tax patch or enhancement to the earned income tax credit, that ARRA enacted through the end of 2012, will be extended further. Considerable uncertainty remains surrounding what compromises/deals might have to be made to garner any of the extensions.

In 2011, federal policymakers frequently engaged in political brinkmanship highlighted by the federal government narrowly averting a government shutdown in April, summer's near-default of the U.S. government and another narrowly missed government shutdown in December. The events' impact is highlighted by the federal government credit downgrade, a highly volatile stock market and the federal policymakers' record low approval ratings. If the fierce partisanship which characterized 2011 continues, the resultant rancor, paralysis and pessimism will very likely have an even greater negative economic and financial impact.

The U.S. military's withdrawal from Iraq and troop scale back in Afghanistan will significantly reduce federal spending. The winding down of various ARRA spending programs will also lower federal spending compared with earlier years.

In late December 2009, the U.S. Treasury said it would cover an unlimited amount of losses at mortgage giants Fannie Mae and Freddie Mac through 2012. The U.S. government now, directly or indirectly, underwrites nine of every 10 new residential mortgages, nearly twice the percentage before the crisis.

Inflation

Between June 2008 and February 2009, oil prices fell from a record $133.93 per barrel to $39.16 per barrel. However, primarily the result of unrest throughout the Middle East, oil prices have risen substantially. In March 2011, oil prices rose above $100 per barrel for the first time since 2008 – rising to $102.94. Oil prices rose further in April – increasing to $110.04. Between May and October, oil prices trended downward but rose substantially in November to $97.21. Oil prices then rose further – increasing to $98.57 in December.

Following oil prices down, the average price of gasoline fell from a record $4.05 a gallon in early July 2008 to $1.59 a gallon by late December 2008 (Energy Information Administration, conventional regular U.S. average). However, by May 2011, gasoline prices had risen to $3.91 a gallon. Since May, prices have trended downward. In late December, prices fell to $3.21 a gallon – their lowest level since mid-February.

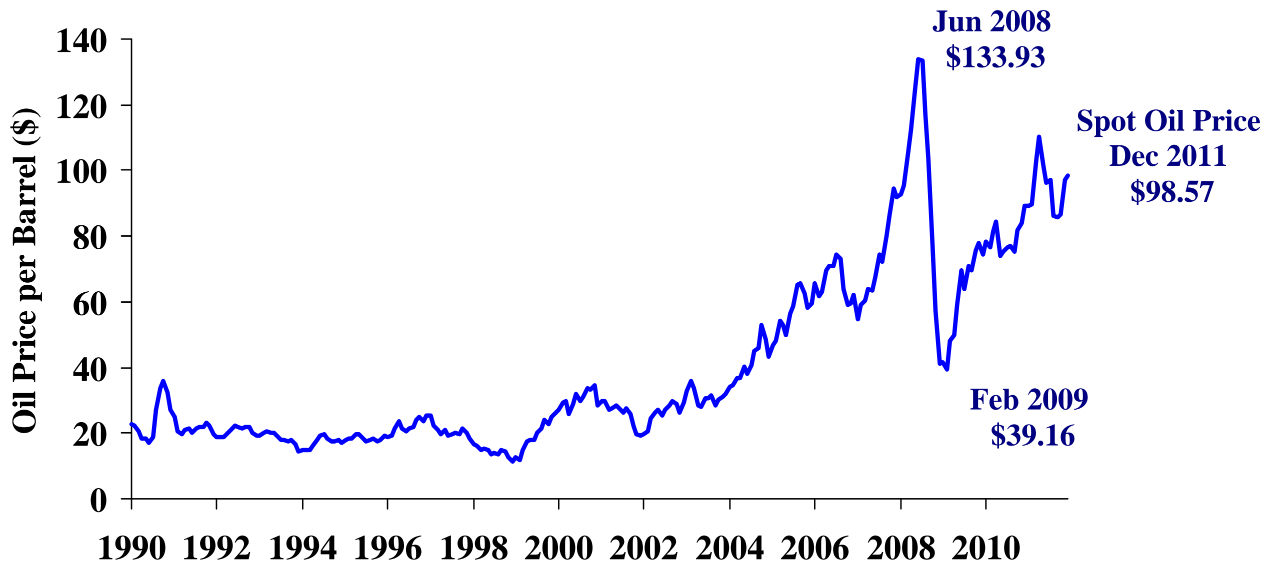
In July 2008, natural gas prices rose to their second highest level in history, but then dropped substantially. By July 2009, natural gas prices had fallen 69.1 percent compared to a year ago. Between January 2010 and October 2010, natural gas prices were up, each month, compared to a year ago. However, between November 2010 and March 2011, natural gas prices were below their year-ago levels. In March 2011, natural gas prices were down 19.2 percent from a year earlier and off 66.3 percent from their July 2008 peak. Since April 2011, year-over-year changes have ranged between a 5.8 percent decline and a 7.1 percent increase. In November, gas prices were up 3.9 percent from a year ago.

At the Federal Open Market Committee's (FOMC) last meeting prior to the May 2011 Consensus Conference (April 2011), the Committee characterized higher inflation due to rising energy and input prices as temporary: "Increases in the prices of energy and other commodities have pushed up inflation in recent months. The Committee expects these effects to be transitory, but it will pay close attention to the evolution of inflation and inflation expectations."

Still more, at its most recent meeting (December 13, 2011), the FOMC -- without reference to energy or other input prices -- stated:

> The Committee also anticipates that inflation will settle, over coming quarters, at levels at or below those consistent with the Committee's dual mandate. However, the Committee will continue to pay close attention to the evolution of inflation and inflation expectations.

Oil Prices Up Sharply from Early 2009



Source: Federal Reserve Bank of St. Louis.

The Economic Cycle Research Institute's (ECRI) future inflation gauge (FIG) rose slightly from 98.4 to 98.6 in December 2011. However, since a cyclical peak in March 2011 (104.7), the FIG has been trending lower. Furthermore, the FIG remains low by historical standards. The average FIG since 2000 exceeds 110.

Major Economic Indicators

Recent trends in many major economic indicators point to future continued growth. However, many key indicators remain near historically low levels -- pointing to significant downward risks to the economy and financial markets.

While not increasing every month, **the ISM manufacturing index (PMI)** trended upward between September 2009 and March 2010 when the index reported its highest reading since June 2004 (60.4). Over the next four months, the index fell each month – losing a combined 5.3 points. The index then increased in each of the following seven months (August 2010- February 2011). Over the seven months, the index rose 6.3 points to 61.4 – the PMI's highest reading since December 1983. However, the PMI fell in five of the next six months (March 2011-August 2011) – losing a net 10.8 points and falling to 50.6 – the lowest PMI since July 2009. In December 2011, the PMI rose to 53.9. The PMI has indicated an expanding sector for 29 straight months. Still more, the 53.9 reading is substantially higher than the Great Recession low (33.3), which represented the lowest reading since June 1980.

Midway through the 2007-2009 recession, in November 2008, the **ISM non-manufacturing index (NMI)** fell to 37.6 -- its lowest reading in at least 11 years. Then – albeit haltingly – the

NMI increased to 50.1 by September 2009. September 2009 marked the first month that the index signaled sector growth in just over a year. Between September 2009 and December 2011, the index has signaled growth in each month except November 2009 when the index fell just below 50.0 (49.9). In February 2011, the NMI rose to 59.7 – the index's highest published or calculated value since August 2005. In November 2011, the NMI fell to 52.0 – its lowest reading since January 2010, before rising to 52.6 in December.

Industrial production worsened considerably between mid-2008 and mid-2009. The three-month average of industrial production fell an astounding 14.6 percent between June 2008 and June 2009. The June 2009 decline was the largest decline since the sharp downturn in 1946, following the end of World War II. Between June 2009 and February 2010, the rate of decline became progressively smaller so that by February 2010, the average was down only 0.5 percent compared to a year earlier. Compared to a year ago, the average rose each month between March 2010 and November 2011. However, after accelerating to 7.5 percent in July 2010, the increases have slowed. In November 2011, the average was up 3.8 percent from November 2010. November 2011's three-month average of industrial production was still 5.7 points less than the pre-recession peak (November 2007).

As industrial production fell in 2008 and 2009, so too did **capacity utilization**. Between February 2008 and July 2009, the three-month average of capacity utilization fell every month compared to the prior month. As a result, the average fell to a record low (67.7 percent) for the series which dates back to 1967. Between August 2009 and November 2011, the average rose in all but two months with a net increase totaling 10.1 points. Compared to a year ago, the November 2011 reading was 2.1 points higher. However, compared to the June 2007 pre-recession peak, capacity utilization is still down 3.3 points.

Calendar year 2009 saw double-digit percentage year-ago declines in the three-month average of **new durable goods orders** in every month. In sharp contrast, the average has risen each month since February 2010. In November 2011, the average was up 8.3 percent from a year earlier. Similarly, the core new capital goods orders average has increased in each of the past 22 months. However, year-over-year increases have slowed. While year-over-year increases had exceeded 15.0 percent each month between April 2010 and February 2011, increases have slowed to 8.3 percent in November 2011.

In November 2008, the three-month average of **retail sales**, excluding motor vehicle and gasoline sales, fell compared to a year ago for the first time in a history extending back to 1992. Each month over the next year, the average fell compared to a year ago. However, declines lessened beginning in the second half of 2009. By December 2009, the average was down only 0.3 percent compared to a year ago. Throughout 2010, the year-ago increase trended upward so that by December 2010, the average was up 5.7 percent. Between January 2011 and November 2011, year-over-year increases ranged between 5.2 percent and 6.3 percent. In addition, over the past five months, the increases have equaled or exceeded 6.0 percent.

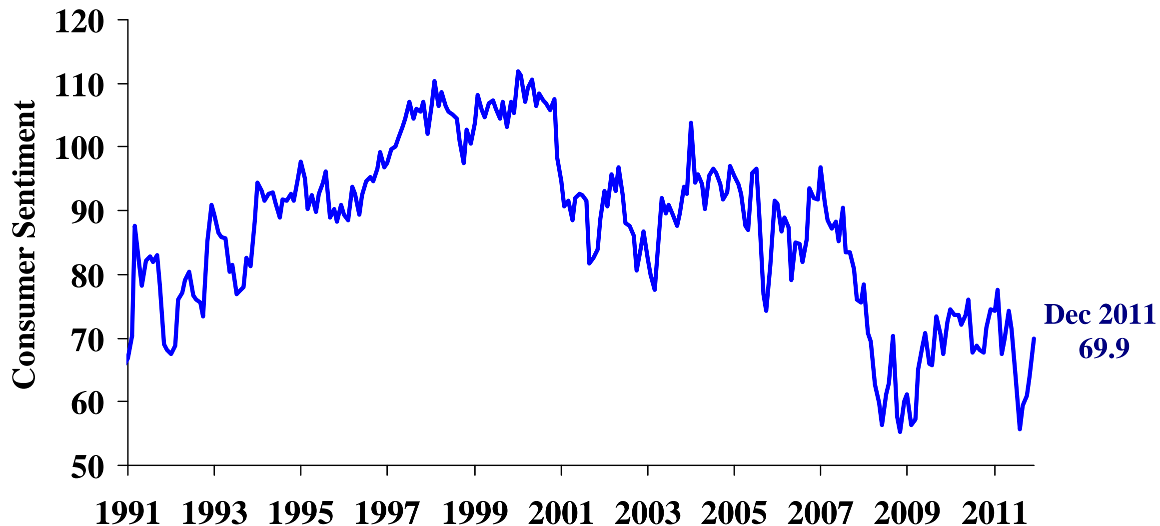
Similarly, the motor vehicle and parts dealers' retail sales average fell, compared to a year ago, each month between December 2007 and November 2009 with double-digit declines each month between mid-2008 and mid-2009. Since December 2009, the average has seen year-over-year

increases each month. Between November 2010 and April 2011, vehicle sales saw double-digit increases each month. Increases have since slowed but remain sizeable ranging between 7.6 percent and 9.1 percent. In November 2011, the average was up 8.1 percent from last November.

With the sharp increase in gasoline prices, retail gasoline sales have risen substantially with double-digit year-over-year increases in all but one month since January 2010. In November 2011, gasoline sales (three-month average) were up 15.9 percent from the prior year and up 28.1 percent from November 2009.

The **Conference Board index of consumer confidence** plummeted to a record low 25.3 in February 2009 – 51.1 points lower than a year earlier. The index rose sharply in April and May, increasing to 54.8. Between May 2009 and November 2010, the index largely moved within a 10-point range between the mid 40's and the mid 50's. In May 2010, the index jumped to 62.7, but then fell back to the mid 50's in June. However, between November 2010 and February 2011, the index rose substantially – rising from 57.8 to 72.0. Between March 2011 and October 2011, the index trended downward – falling to 40.9 in October. However, the index rose sharply in both November to 55.2 and in December 2011 to 64.5 – the index's highest reading since April 2011.

In November 2008, the **University of Michigan index of consumer sentiment** fell to 55.3 – a 28-year record low. The index rose in December before falling back nearly to November's low in February 2009. Between March 2009 and June 2009, the index rose each month – rising to 70.8 in June. After falling to 65.7 in August 2009, the index trended upward in a saw-toothed fashion through June 2010. By June, the index had risen to 76.0. The index then fell sharply in July to 67.8 around which the index fluctuated through October. The index then trended upward into February 2011 when sentiment rose to a three-year high (77.5). The index trended downward through August 2011 in which the index fell to 55.7 – a 33-month low. Over the last four months, the index has regained around two-thirds of its losses between March and August. As a result, the index stood at 69.9 in December 2011. Nonetheless, the index remains at historically low levels. The December 2011 reading is almost twenty-five points lower than the index's average over the ten years directly prior to the Great Recession.



Source: University of Michigan Survey of Consumers.

The Conference Board Measure of CEO Confidence, which had declined in the second quarter, fell further in the third quarter. The 2011Q3 measure stood at 42, down from 55 in 2011Q2 (a reading of more than 50 points reflects more positive than negative responses). According to the Conference Board: "CEO Confidence has declined substantially in the last two quarters and is now at its lowest level in over two years. Clearly, this prolonged period of slow growth is taking a toll on confidence, and expectations are that these lackluster conditions will persist through early 2012."

The **Conference Board index of leading economic indicators (LEI)** reported monthly increases each month between May 2011 and November 2011. Consequently, the LEI is up 5.9 percent from a year ago and has grown at a 6.3 percent annual rate over the past three months.

Between August 2010 and April 2011, the **Economic Cycle Research Institute (ECRI) weekly leading index** pointed to an economy which was regaining traction. However, the index indicated worsening conditions from mid-April through late October 2011. By mid-August 2011, the growth rate had turned negative pointing toward a contracting economy. The growth rate continued to worsen until late October 2011. The index's rate of decline slowed modestly between late October and mid November. Since mid-November, there has been little change in the rate of decline until the last week of December when the decline accelerated modestly. The index's growth rate has now been negative for 20 straight weeks.

Employment

Since the May 2011 Consensus Conference, most employment data point to an improved labor market – albeit one still significantly smaller than prior to the Great Recession.

Between late February 2011 and mid April 2011, the four-week average of initial unemployment claims remained below the key 400,000 initial claims level. The average then rose above 400,000, where it stayed until mid-November. However, since mid-November, the average has stayed below 400,000. In late December, the average (373,250) fell to its lowest level since June 2008.

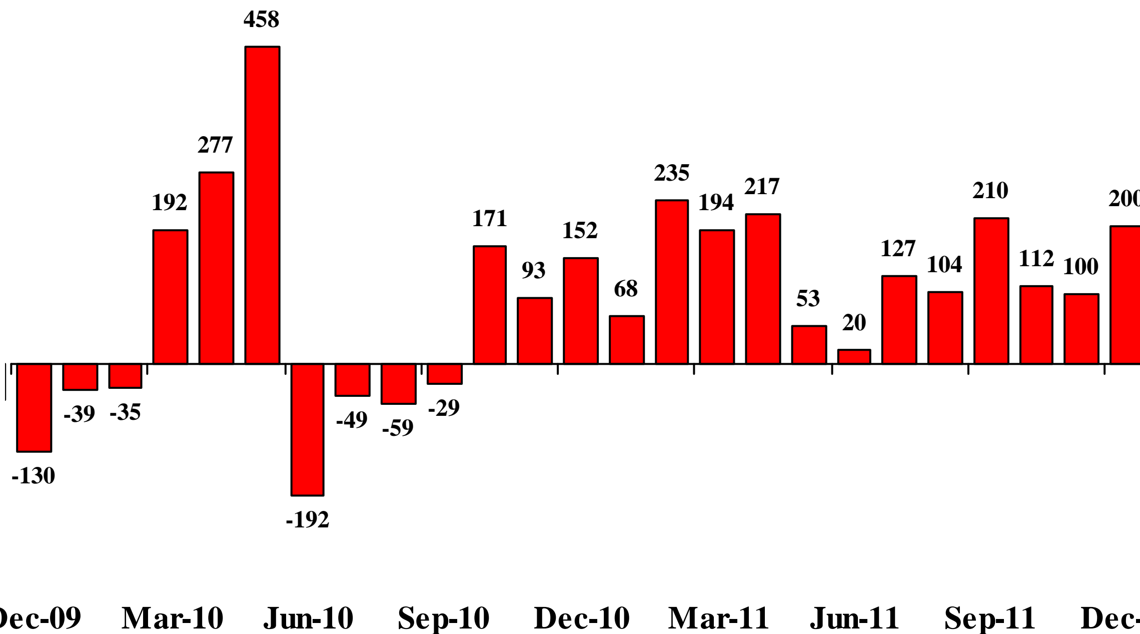
The U.S. unemployment rate rose sharply between April 2008 and October 2009. Over this period, the unemployment rate doubled, rising from 5.0 percent to 10.0 percent – the highest monthly rate since April 1983. The rate then trended downward through mid-2010 with the rate falling to 9.4 percent in June 2010. After trending upward to 9.8 percent by November, the rate dropped in each of the next four months with substantial declines both in December 2010 (-0.4 percentage point) and in January 2011 (-0.3 percentage point). Consequently, the rate fell to 8.9 percent in March 2011. The rate then fluctuated within a narrow range (9.0 percent to 9.1 percent) over the next six months (April 2011-September 2011). In December, the unemployment rate dropped to 8.5 percent – 0.9 percentage point lower than last December and the lowest rate since February 2009.

December 2011 marked the 16th straight month in which household employment was higher than a year earlier. The December 2011 employment level was 1.6 million persons above a year earlier. However, the December 2011 employment level was 5.5 million persons lower than December 2007 (first month of the Great Recession). The December 2011 unemployment level was 1.3 million persons lower than a year earlier but 5.5 million persons higher than four years ago. The December 2011 employment level was 787,000 persons higher than in June 2009 (the last month of the recession). In December, about 1.6 million fewer persons were classified as unemployed than in June 2009. Slightly more than sixty percent of the unemployment drop was accounted for by the decline in the labor force of 843,000 persons since the recession's end.

In 2011, the number of announced job cuts (Challenger Report) totaled 606,082 – 14 percent above a year ago. The increase is mostly accounted for by sizeable public sector job cuts.

Between February 2008 and February 2010, wage and salary employment fell every month, declining 8.8 million jobs to its lowest level since July 1999. In part boosted by Census worker hiring, wage and salary employment rose each month between March 2010 and May 2010 with gains averaging 309,000 jobs per month. With Census worker employment falling, overall employment dropped the next four months with an average loss of 82,000 jobs per month. Employment has increased in each of the past 15 months with a cumulative gain of 2.1 million jobs. December 2011 employment is up a 1.5 million jobs compared to a year ago. However, employment gains have averaged just 125,000 jobs per month since the May Consensus Conference.

Compared to June 2009 (the last month of the recession), December 2011 wage and salary employment is up by 1.4 million jobs. Nevertheless, December 2011 employment remains 6.1 million jobs below employment in December 2007 (the recession's first month).



Source: Bureau of Labor Statistics, U.S. Department of Labor.

Between July 2006 and December 2009, manufacturing sector employment fell in all but one month (when sector employment rose by only 2,000 jobs). Over this period, the sector lost 2.8 million jobs. Manufacturing employment job losses were particularly severe between late 2008 and the first half of 2009. However, like the overall labor market, manufacturing employment job losses slowed over the second half of 2009. Between January 2010 and July 2010, manufacturing employment rose in all but one month. Over these seven months, the sector gained a net 124,000 jobs. After having fallen in each of the next three months, sector employment increased each month between November 2010 and July 2011 – rising 219,000 jobs over these nine months. Between August 2011 and November 2011, manufacturing sector employment barely changed -- rising by just 9,000 jobs. However, manufacturing employment rose by 23,000 jobs in December. Compared to a year ago, manufacturing employment has increased by 225,000 jobs. Since the end of the Great Recession, manufacturing employment is up 62,000 jobs. However, compared to December 2007, sector employment is down almost 2.0 million jobs (-14.2 percent).

The bursting housing bubble and credit crunch have exacted an enormous toll on the construction industry. Construction employment fell every month between July 2007 and February 2010 with job losses totaling 2.2 million jobs (-28.0 percent). Sector job losses were particularly severe in late 2008 and the first half of 2009. Sector job losses worsened in January and February 2010. After rising in March and April 2010, construction employment fell in eight of the following nine months. Sector employment then rose substantially in February 2011 and rose very slightly in March, April and May 2011. Since the May Consensus Conference, construction employment, on net, has changed little (-4,000 jobs). As a result, over the past year, construction sector employment has risen by 18,000 jobs (0.3 percent). Since the end of the recession (June 2009), construction employment is *down* by 459,000 jobs. Still more, construction employment is off by 1.9 million jobs (-26.0 percent) compared to December 2007.

The ISM manufacturing employment index has improved dramatically from early 2009. In 2009Q1, the index averaged 28.2 (a record low for a series that dates back to 1948). In 2011Q1, the index averaged 63.1 – the highest quarterly reading since 1973Q1. Furthermore, the index has signaled an improving sector employment picture every month since October 2009. However, the index has fallen since early 2011. In the second half of 2011, the employment index averaged 54.2 with August and November registering the lowest monthly reading in two years (51.8) but December seeing the highest 2011H1 monthly reading (55.1) .

In each month from January 2008 and June 2010, the ISM non-manufacturing employment index signaled worsening employment in the services sector (reading under 50.0). However, in each of the first six months of 2010, the index recorded a reading in the upper 40's – a substantial improvement from its November 2008 record low (31.5). Between September 2010 and August 2011, the index signaled growing sector employment each month. However, in three of last four reported months (September 2011-December 2011), the index has indicated worsening sector employment.

In September 2011, the Job Openings and Labor Turnover Survey number of job openings rose to 3.4 million – the highest post-recession level and up 22.5 percent from a year ago. Openings fell to 3.3 million in October (12.5 percent higher compared to October 2010). In contrast, October 2010 openings were up 25.9 percent compared to October 2009. The hires rate has changed little over the first 10 months of 2011 – ranging between 2.9 percent and 3.2 percent. October 2011 reported a 3.1 percent hires rate. However, the rate remained substantially below the pre-recession average rate (3.9 percent in November 2007). Year over year, the October 2011 hires level was up 4.5 percent compared to a 7.9 percent increase between October 2009 and October 2010. The October 2011 hires level (4.0 million) remains 1.2 million below the pre-recession average (5.2 million).

According to the National Federation of Independent Businesses (NFIB), the November 2011 net percent of small businesses planning to increase employment was seven percent (percent planning to expand minus percent planning to scale back) – up three percentage points from November 2010 and the highest level since late 2008. Further, November 2011 marked the sixth consecutive monthly positive net percentage of small businesses planning to increase employment. However, the NFIB, reviewing the data, states that "during an expansion plans to hire should be in the double digit levels."

According to the December 2011 Conference Board Survey, the share of consumers viewing jobs plentiful has risen 2.5 percentage points since December 2010 to 6.7 percent. Similarly, the percentage of those who find jobs scarce decreased 5.2 percentage points to 41.8 percent. However, the share finding jobs plentiful is substantially below pre-recession readings exceeding 25 percent.

The Conference Board Employment Trends Index (ETI) increased in November to 103.7, up 6.4 percent from the same month a year ago.

Vehicle Sales and Production

Calendar year (CY) 2009 light vehicle sales totaled slightly over 10.4 million units – the worst annual sales year since 1982 when sales came in just under 10.4 million units. In 2010, sales rose to 11.6 million units. In 2011, light vehicle sales rose to 12.7 million units. Nevertheless, 2011 sales were below the 13.2 million units sold in 2008 and substantially less than the 16.1 million unit sales in 2007. Further, 2011 marked the fourth year of sub 10 million domestic vehicle sales – the first such string since the early 1980s.

In early 2009, light vehicle sales fell off considerably, compared to 2008, to historic lows. Between February 2008 and February 2009, sales fell from a 15.5 million unit rate to a 9.3 million unit rate – the lowest light vehicle sales rate since December 1981. Adjusting for population, the February 2009 sales rate was the lowest since at least 1967. Vehicle sales rebounded slightly but remained below a 10.0 million unit rate through June 2009. With the enactment of the federal government "Cash for Clunkers" program, vehicle sales rose above a 10.0 million unit rate in July and increased substantially in August, rising to its highest sales rate in over a year (14.2 million unit rate). Following the incentive program, sales retreated in September before rising gradually over the balance of 2009.

After falling in January 2010 and February 2010, sales rose to 11.7 million units in March. Sales then fluctuated between 11.3 million and 11.8 million through September. Between September 2010 and February 2011, the light vehicle sales rate rose each month. The February 2011 sales rate (13.2 million units) represented the highest sales rate since August 2009 when Cash for Clunkers boosted sales. The sales rate dropped to 13.0 million units in March 2011 before rising to just over a 13.1 million unit rate in April 2011. Sales then dropped in three of the next four months – falling to a 12.1 million rate in August. Between September 2011 and November 2011, sales rose each month before falling to a 13.5 million rate in December.

Beginning in mid-2008, vehicle sales flagged under the weight of weaker employment, substantially tighter credit markets and dramatic declines in household assets. The Big Three's difficult situation seriously harmed Michigan's economy, which is tightly linked to the Big Three. As a result, both Chrysler and General Motors fell into brief periods of bankruptcy. Chrysler emerged from bankruptcy in June 2009 and General Motors came out of bankruptcy in July 2009.

Recent events indicate that General Motors' and Chrysler's respective financial situations have improved and are continuing to improve. Between July 10, 2009, when GM came out of bankruptcy, and the end of 2009, the company lost $4.3 billion. In contrast, General Motors reported a $4.7 billion profit in 2010 – its first calendar year profit since 2004 and its highest annual profit in more than a decade. In addition, GM posted quarterly profits in each of the first three quarters of 2011 with quarterly profits of $3.2 billion, $2.5 billion (Q2) and $1.7 billion, respectively.

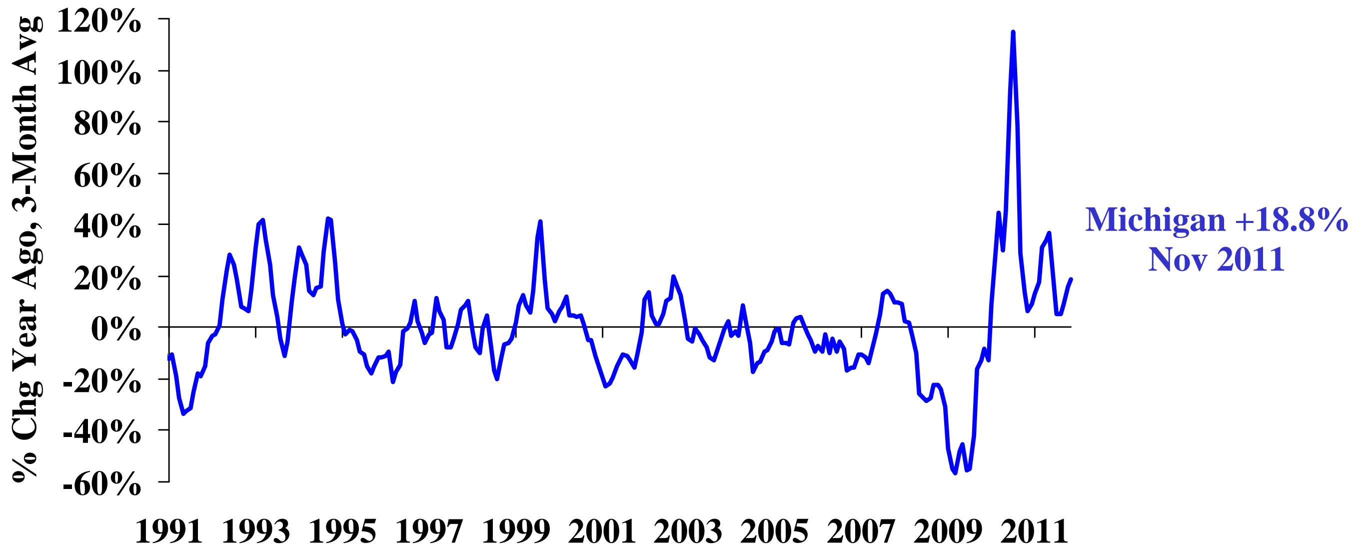
Between June 10, 2009, when Chrysler emerged from bankruptcy, and the end of 2009, the company posted losses totaling $3.8 billion. However, for all four quarters of 2010 combined, Chrysler reported only a $652 million loss. In 2011, Chrysler reported a $116 million profit in Q1 (the company's first quarterly profit since 2006), a loss of $370 million in Q2 and a profit of $212 million in Q3. Chrysler's second quarter loss was largely due to the company's aggressive efforts to pay off federal government bailout loans. Excluding the payoff amounts, Chrysler would have registered a $181 million second-quarter profit.

As a result of the severe recession and flagging vehicle sales, U.S. vehicle production dropped sharply in 2009. In 2009, vehicle production dropped 34.2 percent – falling from 8.8 million units to 5.8 million units. However, with the recovery, production recovered two-thirds of its 2009 losses in 2010 as production rebounded to 7.7 million units. Through November, year-to-date 2011 production was up 10.6 percent from 2010. However, compared to production in the first eleven months of 2007, year-to-date 2011 production is down 22.2 percent.

Current Michigan Economic Conditions

Vehicle Production

Following national trends, Michigan vehicle production fell 20.9 percent in 2008 and an additional 37.9 percent in 2009. However, in 2010, Michigan production regained only 36.4 percent of its losses from the two prior years. As result, while 2010 Michigan vehicle production was up 37.7 percent from 2009, 2010 production was down 32.4 percent compared to 2007 production. However, through November 2011, year-to-date Michigan vehicle production rose 19.8 percent from last year compared to a 10.6 percent increase nationally. Year-over-year increases were particularly strong in the first five months of 2011 with increases ranging from 20.7 percent and 47.6 percent. June and July saw year-over-year declines, but production has risen compared to last year in each of the past four months with a 39.0 percent increase in November. Consequently, November 2011 marked the 21st year-over-year increase in the last 23 months. Year-to-date, State auto production was up 21.0 percent from a year ago while Michigan truck production rose 19.2 percent.



Source: Automotive News and Michigan Department of Treasury.

Employment

Michigan's economy relies heavily on the performance of the manufacturing sector in general and the auto industry specifically. Most of the past decade has been marked by weak manufacturing employment performance, declining vehicle production, continued declines in Big Three market share and continued supply rationalization among vehicle suppliers. As a result, Michigan's employment performance has been below the national average. Substantial productivity gains in the vehicle industry have also contributed to Michigan's weaker employment performance.

From Michigan's employment peak in April 2000 to November 2011, Michigan lost a net 761,200 jobs (-16.2 percent). Since April 2000, Michigan manufacturing employment has fallen by 405,600 jobs, a loss of nearly half (-44.8 percent) of the jobs in that sector at the state's overall employment peak. The manufacturing employment drop accounted for 53.3 percent of the State's overall employment loss.

In 2009, Michigan lost 7.0 percent (289,900) of its wage and salary jobs. The 7.0 percent decline represented Michigan's sharpest annual employment drop in over 50 years. In 2009, Michigan manufacturing employment plummeted, dropping 19.0 percent. Construction employment declined 16.9 percent.

However, Michigan's employment declines slowed considerably in 2010. In 2010, the state lost only a net 10,900 jobs (-0.3 percent). While 2010 marked the tenth straight year that Michigan employment fell, the 2010 decline was second -- only to the 0.2 percent decline in 2005 -- as the least severe drop over the past decade. In addition, Michigan manufacturing employment actually increased in 2010 with the state gaining a net 9,600 manufacturing jobs (2.1 percent gain).

Through November, year-to-date 2011 overall employment is *up* 1.6 percent with manufacturing employment up 5.0 percent and construction employment 5.9 percent higher. Four sectors in Michigan saw year-to-date declines: Retail (-0.1 percent), Information (-1.3 percent), Leisure and Hospitality (-1.1 percent) and Government (-2.4 percent).

Between December 2008 and October 2011, Michigan's unemployment rate remained in double-digits. Over this time, the State's unemployment rate peaked in August and September 2009 at 14.1 percent – the state's highest rate since July 1983. Through April 2011, the unemployment rate trended downward – falling to 10.2 percent. The State's rate then rose slightly between May 2011 and August 2011 (11.2 percent). The State's unemployment rate has fallen over the past three months with large drops in both October and November. As a result, Michigan's unemployment rate fell to 9.8 percent in November – marking the State's first rate below 10.0 percent in three years and the State's lowest rate since October 2008. Compared to a year ago, the November 2011 rate was down 1.6 percentage points and 4.3 percentage points lower than the recent 14.1 percent peak.

Between April 2011 and August 2011, Michigan household employment fell by 89,600 persons. However, over the past three months, the State's household employment has grown by 32,600 persons. Compared to a year ago, April 2011 Michigan household employment was up 72,000

persons. However, year-over-year, household changes shrank over the next five months – turning negative in July. In September the year-over-year drop equaled 30,600 persons, but shrank to an 11,900 persons decline in November.

The State's labor market has seen modest improvement since April 2011 (the last month reported before the May Consensus Conference). Compared to April 2011, the November 2011 Michigan unemployment rate is down 0.4 percentage point. The State's November 2011 wage and salary employment is up 0.4 percent from April 2011.

Housing Market

Despite not being one of the major participants in the housing boom, with skyrocketing home prices and rising housing starts, Michigan was hit disproportionately hard by the housing bust due to sharply declining employment. Nevertheless, the State's housing market has recently seen some signs of improvement.

Between 2005 and 2009, Michigan housing unit authorizations fell 85.1 percent, declining from 46,989 units to 6,984 units. Nationally, authorizations dropped 73.4 percent over this period. In 2010 Michigan authorizations rose 32.5 percent from 2009. Nevertheless, 2010 Michigan authorizations were 81.6 percent below the State's 1996-2005 average (50,324 units). Year-to-date through November 2011, Michigan authorizations (8,569 units) were essentially unchanged from a year ago (-1.1 percent) while U.S. authorizations were up 1.9 percent.

In October 2011, according to Case-Shiller house price measures (seasonally adjusted), the Detroit MSA recorded a 2.5 percent year-over-year house price increase, compared to a 3.4 percent average decrease for the twenty U.S. metro areas surveyed for the measure. However, the November 2011 Detroit price measure was 45.4 percent below Detroit's peak measure (March 2006). In comparison, the 20-city reading was 33.0 percent below its peak reading (April 2006).

In 2010, foreclosure sales accounted for one-third of all Michigan housing sales according to RealtyTrac. In 2011Q3, Michigan foreclosures fell 7 percent from 2011Q2 and were down 32 percent from a year ago. However, as is the case nationally, backlogged paperwork likely plays a substantial role in reducing Michigan foreclosure activity. In 2011Q3, Michigan ranked fifth among U.S. states in the number of foreclosures (31,179). In addition, in 2011Q3, Michigan ranked seventh with one foreclosure for every 146 housing units – compared to one for every 213 units nationally.

The share of mortgage properties underwater in Michigan is substantially higher than the national average. In 2011Q3, 22.1 percent of residential properties with mortgages were underwater nationally. In Michigan, 34.5 percent of such properties were underwater – placing Michigan fourth among the fifty states behind Nevada (58.3 percent), Arizona (47.1 percent) and Florida (43.9 percent). Furthermore, the loan amount as a percent of house value in Michigan is 83.4 percent – again ranking fourth highest among the fifty states behind Nevada (110.2

percent), Arizona (92.0 percent), Florida (86.7 percent). Nationally, loan amount as a percent of house value was 69.8 percent.

Personal Income

In 2009, Michigan personal income fell in every quarter compared to a year earlier. In the first three quarters of 2009, the declines ranged narrowly from 5.7 percent to 6.1 percent. In 2009Q4, the decline shrank to 4.2 percent. Michigan personal income has grown in every quarter between 2010Q1 and 2011Q3 (the latest quarter released). Year-over-year increases accelerated between 2010Q1 (1.0 percent) and 2011Q1 (6.9 percent). Increases have slowed over the past two quarters with 2011Q3 reporting 3.7 percent growth-- slightly slower than national income (4.1 percent) and ranking 30th among the fifty states.

In each of the quarters between 2008Q3 and 2010Q1, Michigan wage and salary income fell compared to a year ago, with all four drops in 2009 being sizeable – ranging between -6.5 percent and -9.6 percent. Wages and salaries fell only slightly (-1.4 percent) in 2010Q1 and have risen every quarter between 2010Q2 and 2011Q3. However, growth has slowed markedly over the first three quarters of 2011 – slowing from 7.3 percent to 2.6 percent. Michigan's 2011Q3 increase (2.6 percent) was slightly slower than national growth (2.9 percent).

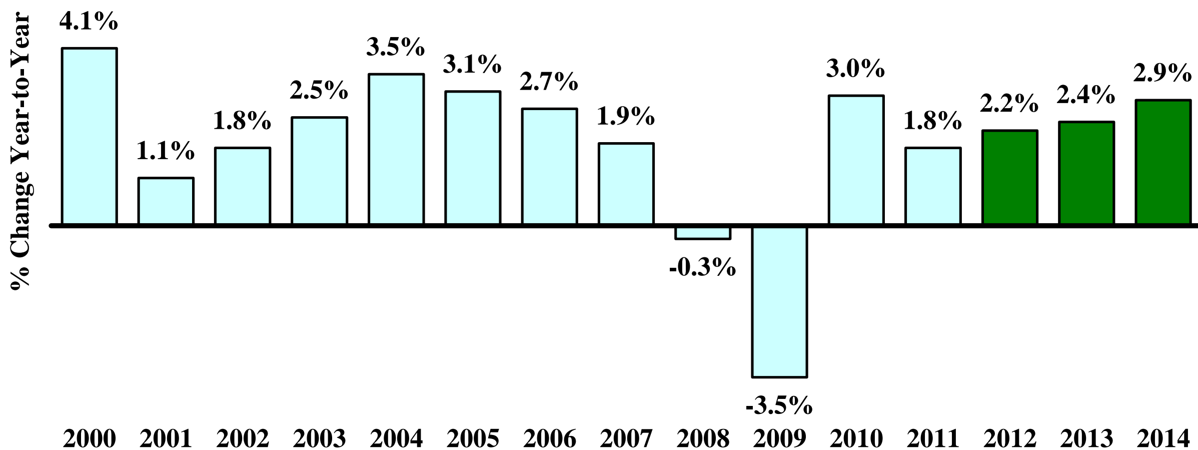
Michigan manufacturing wages and salaries reported declines compared to year-ago levels in twelve straight quarters between 2007Q2 and 2010Q1. As with overall wages and salaries, 2009 saw the four largest sector drops – ranging between -14.8 percent and -22.2 percent. The 2010Q1 decline was very slight (-0.1 percent). Manufacturing wages and salaries have increased in the last six reported quarters. Manufacturing wage growth peaked in 2011Q1 (16.1 percent) but has since slowed substantially with 2011Q3 growth of 5.2 percent – significantly faster than national growth (2.9 percent).

2012, 2013 and 2014 U.S. Economic Outlook

Summary

After declining 3.5 percent in 2009, real GDP rose 3.0 percent in 2010. After slowing in 2011, economic growth is expected to accelerate gradually over the forecast horizon with 2.2 percent growth in 2002, 2.4 percent growth in 2013 and 2.9 percent growth in 2014.

Real GDP Accelerates Gradually Throughout Forecast



Source: Bureau of Economic Analysis, U.S. Department of Commerce, and Administration Forecast, January 2012.

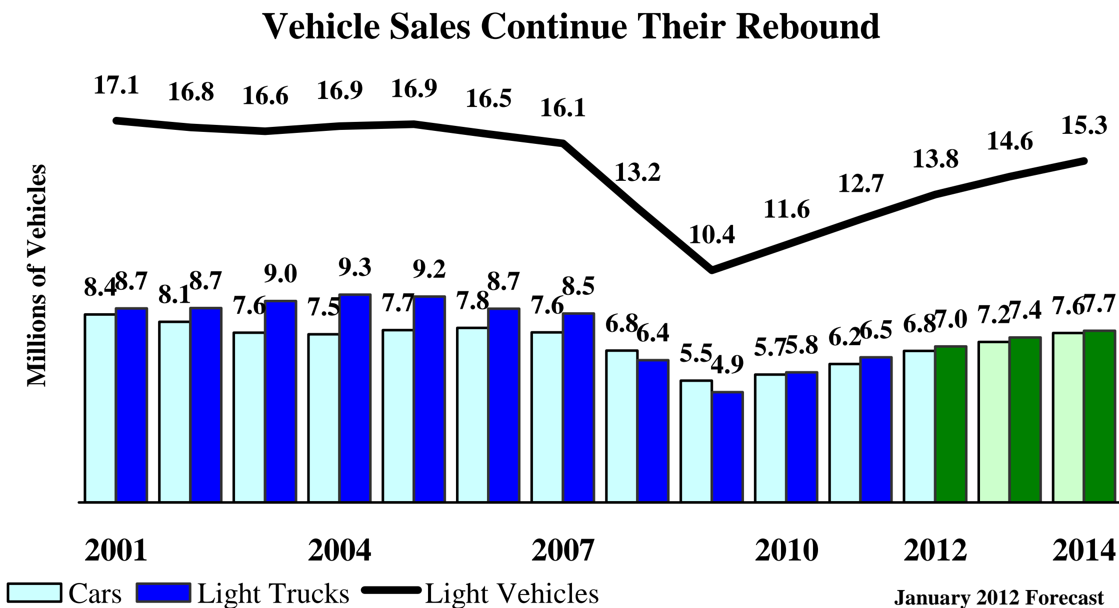
The U.S. economy contracted severely over the second half of 2008 and 2009Q1 (-6.4 percent average annual rate). After falling slightly in 2009Q2, real GDP reported solid growth over the next three quarters (3.8 percent average annual growth). Real GDP then grew modestly over the second half of 2010 before slowing dramatically in 2011Q1 to a 0.4 percent annual growth rate. Economic growth accelerated over the balance of 2011 (estimated 2.0 percent annual growth rate). In 2012 and 2013, real GDP growth is expected to fluctuate between 1.9 percent and 2.8 percent. The economy is expected to strengthen in 2014 with growth exceeding a 3.0 percent rate each quarter between 2014Q2 and 2014Q4.

Light vehicle sales totaled an estimated 12.7 million units in 2011. Light vehicle sales are forecast to increase each year of the forecast. Vehicle sales are projected to total 13.8 million units in 2012, 14.6 million units in 2013 and 15.3 million units in 2014 -- the first year that sales will have exceeded 15.0 million units since 2007.

The U.S. unemployment rate rose to a 9.6 percent rate in 2010 – just below the record high 9.7 percent rate set in 1982 (going back to 1947). The rate is expected to be 9.0 percent in 2012, 8.8 percent in 2013 and 8.3 percent in 2014.

After falling at its fastest rate since at least 1940 in 2009 (-4.4 percent), U.S. wage and salary employment fell modestly in 2010 (-0.8 percent). In 2011, employment rose an estimated 1.0 percent. Employment is then forecast to increase 1.1 percent in 2012, rise 1.4 percent in 2013 and increase 1.6 percent in 2014. After accelerating to an estimated 3.2 percent annual rate in 2011, inflation is expected to moderate over the forecast horizon with price increases ranging between 2.1 percent and 2.3 percent.

In 2009, the short-term Treasury bill rate averaged 0.2 percent – down substantially from 1.4 percent reported in 2008. The rate has averaged 0.1 percent in both 2010 and 2011. The Treasury bill rate is expected to average 0.1 percent in 2012 also before rising to 0.2 percent in 2013. The rate is forecast to average 0.6 percent in 2014 during which the quarterly average rate is expected to rise from 0.2 percent (2014Q1) to 1.0 percent (2014Q4). After falling from 4.7 percent in 2011 to 4.0 percent in 2012, corporate interest rates are forecast to change slightly over the forecast horizon. The rate will rise to 4.2 percent in 2013 before increasing to 4.4 percent in 2014. Down from 5.0 percent in 2009, mortgage rates averaged 4.7 percent in 2010 and 4.5 percent in 2011. Mortgage rates are expected to fall to 4.1 percent in 2012 before rising to 4.3 percent in 2013 and to 4.8 percent in 2014.



Source: Bureau of Economic Analysis, U.S. Department of Commerce, and Administration Forecast, January 2012.

Assumptions

For the most part, oil prices per barrel are expected to rise modestly – increasing from $93 at the end of 2011 to $108 at the end of 2014. Natural gas prices are expected to drop 1.8 percent in 2012 before rising 3.0 percent both in 2013 and in 2014.

Throughout the forecast horizon, the housing market is expected to strengthen but to remain historically weak. Starts are forecast to increase each year. Consequently, housing starts in 2014 (987,000 units) will be 65.0 percent higher than estimated 2011 starts. Nevertheless, 2014 starts will remain well below the average 1.7 million annual starts in the ten years before the housing bust.

Consistent with recent FOMC statements, the Fed is expected to keep the federal funds rate within the record low 0.00-0.25 percent range through the end of 2013. The Fed is then assumed to increase the federal funds rate over the course of 2014 with the rate rising to 1.0 percent by the end of the year.

Economic growth among major U.S. trading partners is expected to accelerate modestly in early 2012 before rising only very slightly over the balance of the forecast horizon.

The savings rate is assumed to fluctuate around a narrow range in 2012 (3.8 percent to 3.9 percent). The rate is then expected to drop to an average 3.2 percent in 2013 and to a 2.9 percent rate in 2014.

Forecast Risks

The economic recovery continues to face significant challenges.

Great Recession. The Great Recession did serious damage to household balance sheets and psyches, and significantly tightened credit conditions. Recent economic data suggests that the Great Recession's negative impacts are softening in all respects. Nevertheless, substantial uncertainty surrounds the recession's negative impact on consumer and investor sentiment. Recent employment gains are encouraging, but the labor market remains at risk of being significantly harmed by a negative economic shock.

Fiscal Policy. There remains a growing risk of a federal stalemate. Greater polarization among federal policy makers would worsen consumer and investor confidence and, hence, have substantially negative impacts on financial markets and the overall economy. In addition, the substantial divisions among the House, Senate and President reduce the federal government's ability to counter negative financial and macroeconomic shocks to the economy.

The forecast assumes moderate and slowing federal government spending declines across the forecast horizon with annual declines of 2.9 percent (2012), 2.1 percent (2013) and 1.8 percent (2014). The impact of greater (or smaller) cuts remains uncertain. Extremely greater cuts would likely curtail economic growth below forecasted levels. At the same time -- though more a far

term risk -- failure to agree to cut spending sufficiently could impair the federal government's credit rating with negative impacts for the broader economy (including higher interest rates and a lower value of the dollar).

Monetary Policy. The Federal Reserve completed its second round of quantitative easing at the end of June 2011. The Fed is now engaged in Operation Twist designed to the increase the average maturity of its portfolio. Given that Operation Twist is designed to leave the size of the Fed's portfolio essentially unchanged (unlike quantitative easing), the Operation will likely be less effective than its two rounds of quantitative easing. On the other hand, more severe crises may lead the Fed to implement a third round of quantitative easing. Furthermore, the FOMC has now explicitly stated that it will maintain its historically low interest rates at least through the end of 2013 -- providing greater certainty for financial markets.

Housing Market. Projected 2013 starts are more than 65 percent higher than in 2010. If the housing market fails to pick up as forecasted, the U.S. and Michigan economies would be weaker than expected. However, despite the large projected increases, forecasted 2013 starts still total 987,000 units -- marking the seventh straight sub-1.0 million unit annual total. In a history dating back to 1959, 2008 marked the first year that annual starts *ever* fell below 1.0 million units. A stronger than forecasted housing market would boost the overall economy.

Europe Debt Crisis. Europe is in the midst of credit crisis spurred by the need for European banks and governments to refinance or sell substantial amount of debt – raising serious concerns that there will not be enough demand to buy such a tremendously large amount of debt. Greece is on the verge of government default. Italy, the third largest economy in the eurozone, faces a massive debt. Particularly vulnerable European nations also include Ireland, Portugal and Spain. Depending upon the eventual magnitude and severity of the credit problems, these strains could spread to other nations' financial markets and economies including the U.S. A flight to safety would raise the value of the dollar – making U.S. exports more costly.

Complicating the crisis, austerity measures (spending cuts, tax hikes) represent a major tool employed to address a nation's debt problems. However, austerity measures hamper a nation's economic growth. Given the ill effects of a nation's massive indebtedness on the one hand and of austerity measures on the other, the forecast's assumed modest growth among the United States' major trading partners may be too optimistic.

Oil Prices. Geopolitical concerns, increased demand, or a major supply disruption could raise prices well above the assumed range ($96-$108 a barrel). Still higher oil prices (and consequently higher gasoline prices) would retard domestic growth by depressing consumer sentiment, reducing households' discretionary income and increasing input costs to businesses. Higher oil prices may lead the Federal Reserve to hike rates sooner and more than expected. This risk is heightened as many other countries around the world recover and thus boost demand. Alternatively, if Asian oil demand decreases due to lower and more sustainable growth rates in China or European demand weakens as a result of financial crises, prices could be lower than assumed.

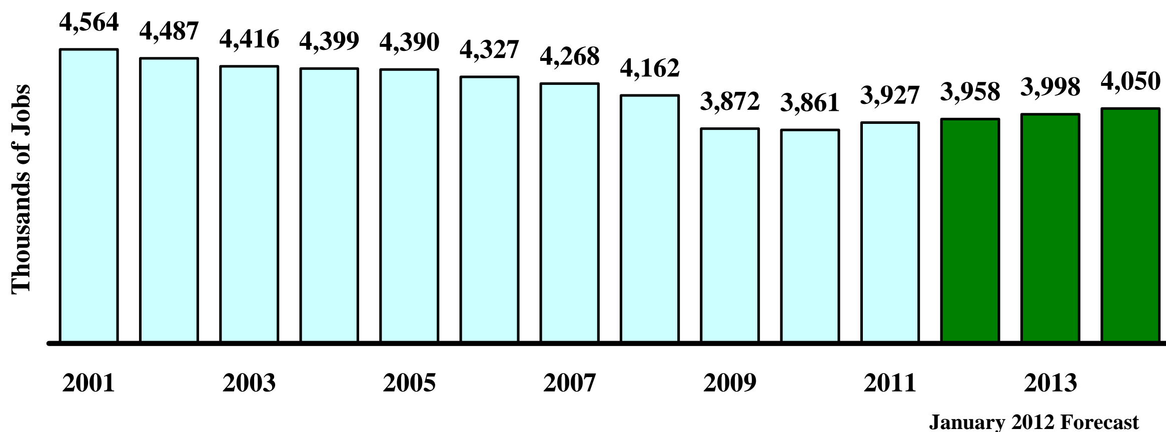
Other Factors. Geopolitical factors (such as a domestic terrorist attack) remain a downside risk to the baseline forecast.

2012, 2013 and 2014 Michigan Economic Outlook

Michigan employment fell 7.0 percent in 2009 – its sharpest decline since 1958. State employment dropped another 0.3 percent in 2010, but is estimated to have increased 1.7 percent in 2011 – marking the first calendar year Michigan employment increase since 2000. State employment is then projected to rise 0.8 percent in 2012, to increase 1.0 percent in 2013 and grow 1.3 percent in 2014. Compared to 2000, 2014 employment is down by 625,800 jobs (-13.4 percent).

Private non-manufacturing employment is estimated to have risen by 54,100 jobs in 2011. The sector's growth is projected to slow to 28,700 jobs in calendar year 2012 before rising by 35,700 jobs in 2013 and growing by 47,500 jobs in 2014. After rising 5.2 percent in 2011, manufacturing employment growth is forecast to slow to 2.8 percent in 2012. Manufacturing employment growth is expected to slow further over the balance of the forecast horizon with a 2.1 percent increase in 2013 and 1.9 percent growth in 2014. Between CY 2011 and CY 2014, manufacturing employment is projected to rise by 34,600 jobs.

Michigan Wage and Salary Employment Rises Slightly



Source: Michigan Department of Labor and Economic Growth, U.S. Bureau of Labor Statistics, and January 2012 Administration Forecast.

Michigan transportation equipment employment rose an estimated 4.1 percent in 2011. The sector is expected to increase each year between 2012 and 2014 with increases slowing over the forecast horizon: 3.2 percent (2012), 2.7 percent (2013) and 2.6 percent (2014). Despite the

increases, forecasted 2014 transportation equipment employment (148,700 jobs) is down 56.7 percent from the sector's 2000 employment (346,100 jobs).

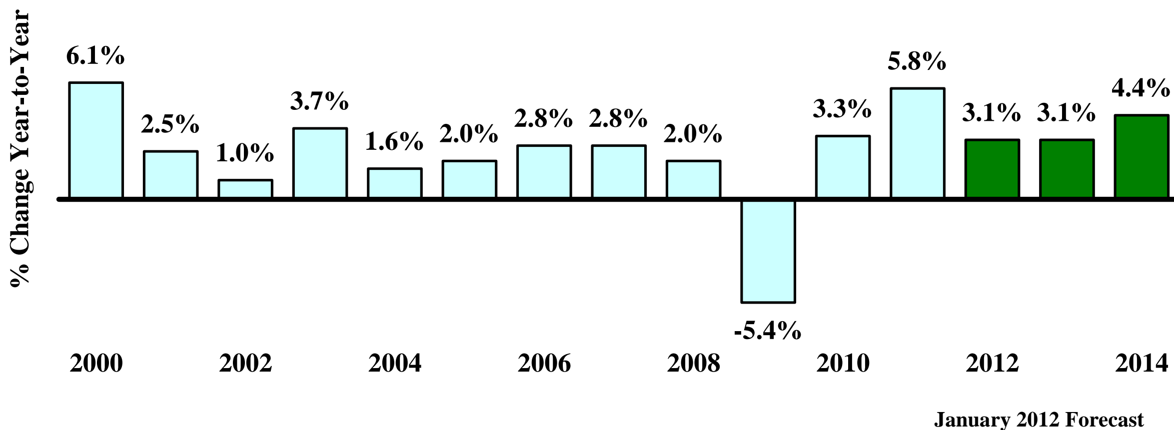
State household employment is forecast to rise each quarter of the forecast horizon. After soaring from 8.3 percent to 13.3 percent in 2009 (highest rate since 1983), Michigan's unemployment rate declined to 12.5 percent in 2010 and to an estimated 10.7 percent in 2011. Michigan's unemployment rate is expected to fall further over the forecast horizon with the rate dropping to 10.3 percent in 2012, 10.0 percent in 2013 and 9.7 percent in 2014.

After falling a record 8.2 percent in 2009, Michigan wages and salaries rose 1.7 percent in 2010. State wages and salaries are estimated to have risen 5.9 percent in 2011. Wage growth is expected to fluctuate over the forecast horizon with wages growing 3.3 percent in 2012, 4.2 percent in 2013 and 3.8 percent in 2014.

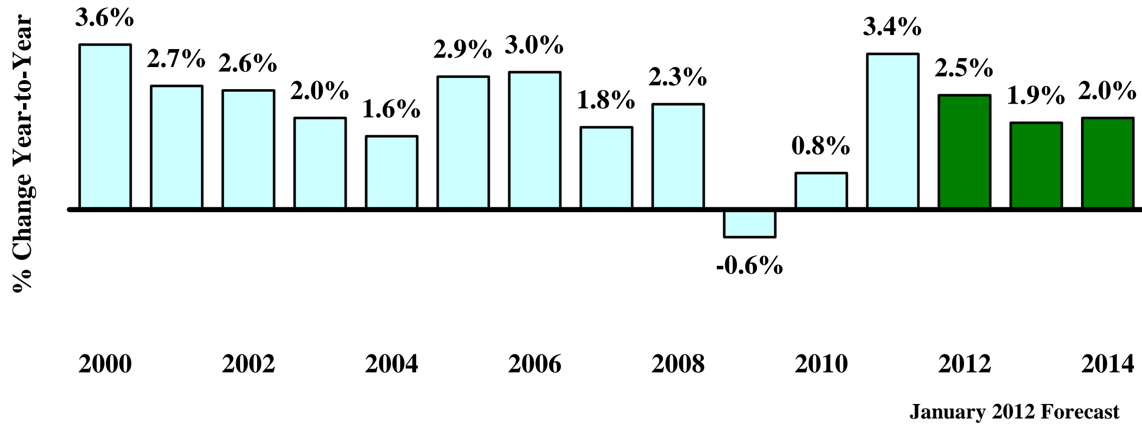
In 2009, overall Michigan personal income declined 5.4 percent – the largest Michigan personal income decline since 1938. Personal income rose 3.3 percent in 2010. Personal income is estimated to have risen 5.8 percent in 2011. Income is forecast to rise 3.1 percent both in 2012 and in 2013. In 2014, personal income is expected to rise 4.4 percent.

The overall CY price level, as measured by the Detroit CPI, is estimated to have increased 3.4 percent in 2011. Detroit CPI inflation is expected to be 2.5 percent in 2012, 1.9 percent in 2013 and 2.0 percent in 2014. Real (inflation adjusted) Michigan personal income is forecast to rise 0.6 percent in 2012, increase 1.2 percent in 2013 and grow 2.4 percent in 2014.

Michigan Personal Income Reports Solid Growth



Source: Bureau of Economic Analysis, U.S. Department of Commerce, and Administration Forecast, January 2012.



Source: U.S. Bureau of Labor Statistics and Administration Forecast, January 2012.

Table 1

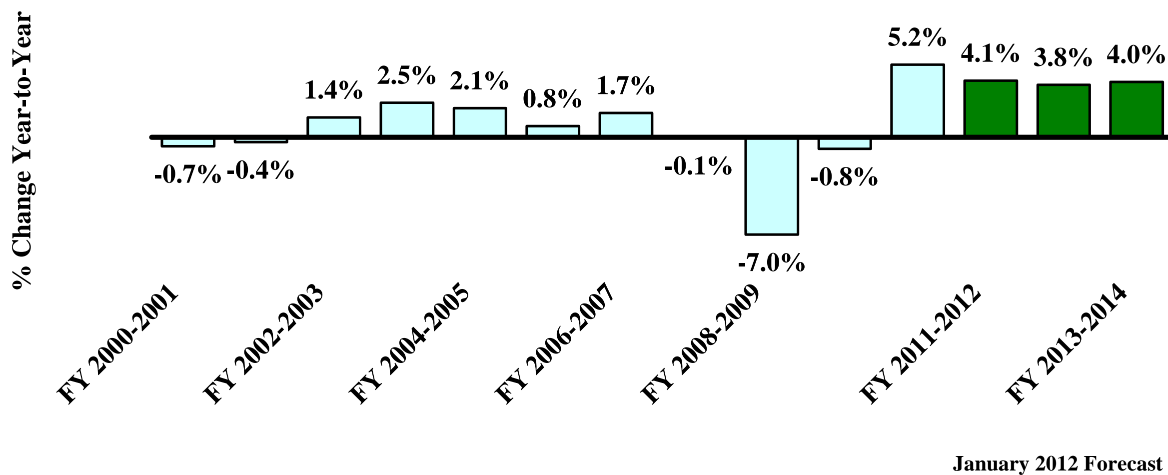
Administration Economic Forecast

December 2011

	Calendar 2010 Actual	Percent Change from Prior Year	Calendar 2011 Forecast	Percent Change from Prior Year	Calendar 2012 Forecast	Percent Change from Prior Year	Calendar 2013 Forecast	Percent Change from Prior Year	Calendar 2014 Forecast	Percent Change from Prior Year
United States										
Real Gross Domestic Product (Billions of Chained 2005 Dollars)	$13,088	3.0%	$13,324	1.8%	$13,617	2.2%	$13,944	2.4%	$14,348	2.9%
Implicit Price Deflator GDP (2005 = 100)	110.7	1.1%	113.1	2.2%	115.1	1.8%	117.3	1.9%	119.4	1.8%
Consumer Price Index (1982-84 = 100)	218.1	1.6%	225.0	3.2%	230.2	2.3%	235.0	2.1%	239.9	2.1%
Consumer Price Index - Fiscal Year (1982-84 = 100)	217.4	1.7%	223.3	2.7%	229.3	2.7%	233.9	2.0%	238.8	2.1%
Personal Consumption Deflator (2005 = 100)	111.1	1.8%	113.9	2.5%	115.8	1.7%	117.7	1.6%	119.7	1.7%
3-month Treasury Bills Interest Rate (percent)	0.1		0.1		0.1		0.2		0.6	
Aaa Corporate Bonds Interest Rate (percent)	4.9		4.7		4.0		4.2		4.4	
Unemployment Rate - Civilian (percent)	9.6		8.9		9.0		8.8		8.3	
Housing Starts (millions of starts)	0.587	6.0%	0.598	1.9%	0.724	21.1%	0.894	23.5%	0.987	10.4%
Light Vehicle Sales (millions of units)	11.6	11.5%	12.7	9.5%	13.8	8.7%	14.6	5.8%	15.3	4.8%
Passenger Car Sales (millions of units)	5.7	3.6%	6.2	8.8%	6.8	9.7%	7.2	5.9%	7.6	5.6%
Light Truck Sales (millions of units)	5.8	18.4%	6.5	12.1%	7.0	7.7%	7.4	5.7%	7.7	4.1%
Big 3 Share of Light Vehicles (percent)	44.2		46.2		45.0		45.0		45.0	
Michigan										
Wage and Salary Employment (thousands)	3,861	-0.3%	3,927	1.7%	3,958	0.8%	3,998	1.0%	4,050	1.3%
Unemployment Rate (percent)	12.5		10.7		10.3		10.0		9.7	
Personal Income (millions of dollars)	$342,663	3.3%	$362,538	5.8%	$373,776	3.1%	$385,363	3.1%	$402,319	4.4%
Real Personal Income (millions of 1982-84 dollars)	$167,083	-0.7%	$170,928	2.3%	$171,930	0.6%	$173,979	1.2%	$178,096	2.4%
Wages and Salaries (millions of dollars)	$173,642	1.7%	$183,887	5.9%	$189,955	3.3%	$197,933	4.2%	$205,455	3.8%
Detroit Consumer Price Index (1982-84 = 100)	205.1	0.8%	212.1	3.4%	217.4	2.5%	221.5	1.9%	225.9	2.0%

Fiscal Year Economics

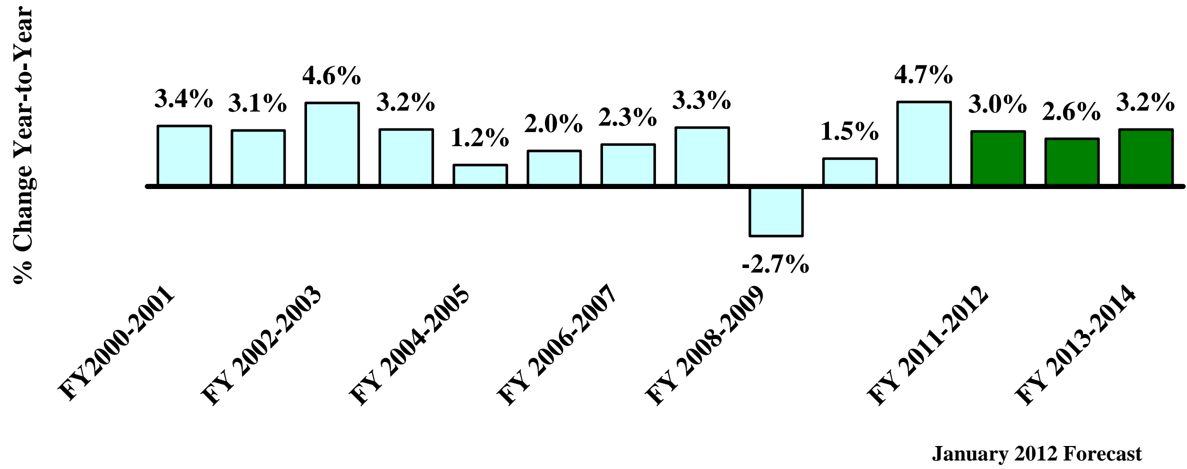
Michigan's largest taxes are the individual income tax ($6.4 billion in FY 2011), which includes refunds, and sales and use taxes ($7.8 billion). Income tax withholding is the largest income tax component. Withholding ($7.2 billion) is most affected by growth in wages and salaries. Michigan wages and salaries are expected to rise 4.1 percent in FY 2012, to increase 3.8 percent in 2013 and grow 4.0 percent in FY 2014.



Source: Bureau of Economic Analysis, U.S. Department of Commerce, and Administration Forecast, January 2012.

Sales and use taxes depend primarily on Michigan disposable (after tax) income and inflation. Disposable income is expected to rise 3.0 percent in FY 2012, 2.6 percent in FY 2013 and 3.2 percent in FY 2014. Prices, as measured by the Detroit CPI, are forecast to increase 3.0 percent in FY 2012, rise 1.8 percent in FY 2013 and grow 2.0 percent in FY 2014.

Michigan Disposable Income Increases
Basis for Sales and Use Tax Collections



Source: Research Seminar in Quantitative Economics, University of Michigan, and Administration Forecast, January 2012.

ADMINISTRATION REVENUE ESTIMATES

January 13, 2012

Revenue Estimate Overview

The revenue estimates presented in this section consist of baseline revenues, revenue adjustments, and net revenues. Baseline revenues provide an estimate of the effects of the economy on tax revenues. For these estimates, FY 2011 is the base year. Any non-economic changes to the taxes occurring in FY 2012, FY 2013 and FY 2014 are not included in the baseline estimates. Non-economic changes are referred to in the tables as "tax adjustments". The net revenue estimates are the baseline revenues adjusted for tax adjustments.

This treatment of revenue is best illustrated with an example. Suppose tax revenues are $10.0 billion in a given year, and that based on the economic forecast, revenues are expected to grow by 5.0 percent per year. Baseline revenue would be $10.0 billion in Year 1, $10.5 billion in Year 2, and $11.0 billion in Year 3. Assume a tax rate cut is in place that would reduce revenues by $100 million in Year 1, $200 million in Year 2, and $300 million in Year 3. If Year 1 is the base year, the revenue adjustments for Year 1 would be $0 since the tax cut for this year is included in the base. The revenue adjustments for Year 2 would be $100 million, and the revenue adjustments for Year 3 would be $200 million, since the revenue adjustments are compared to the base year.

In the example above, the baseline revenues would be $10.0 billion, $10.5 billion, and $11.0 billion, for Years 1 through 3, respectively. The revenue adjustments would be $0 in Year 1, $100 million in Year 2, and $200 million in Year 3. The $200 million in Year 3 represents the tax cuts since Year 1. Net revenue would be $10.0 billion in Year 1, $10.4 billion in Year 2, and $10.8 billion in Year 3.

The following revenue figures are presented on a Consensus basis. Generally speaking, the Consensus estimates do not include certain one-time budget measures, such as withdrawals from the Budget Stabilization Fund, the sale of buildings, and so on. The figures also do not include constitutional revenue sharing payments to local governments from the sales tax. In addition, the estimates only include enacted legislation and do not include the effects of any proposed changes. The School Aid Fund estimates consist of taxes plus the transfer from the State Lottery Fund.

FY 2011 Revenue Review

FY 2011 GF-GP revenue totaled $8,813.0 million. For the January 2012 revenue estimates, new items have been added that were previously carried on the overall balance sheets for the General Fund and School Aid Fund. These new items include non-constitutional revenue sharing sales tax revenue, tax amnesty revenue, unclaimed property one-time revenue, and the revenue from liquor reforms. Fiscal year 2011 GF-GP revenue grew 14.8 percent compared to FY 2010 final revenue on a comparable basis. Compared with the adjusted May 2011 consensus estimate, GF-GP revenue was up $117.2 million. School Aid Fund revenue for FY 2011 grew 4.0% from the comparable final level for FY 2010 and was up $110.6 million from the adjusted May 2011 consensus estimate. FY 2011 SAF revenues totaled $11,248.2 million (See Table 2).

Table 2

FY 2010-11 Administration Revenue Estimates

(millions)

	Consensus May 16, 2011		Preliminary FY 2011		
	Amount	**Growth**	**Amount**	**Growth**	**Change**
General Fund - General Purpose					
Net Resources May '11 Basis	$7,524.1	10.9%	$7,628.5	12.4%	$104.4
New Items*	$1,171.7		$1,184.5		$12.8
Adjusted Net General Fund	$8,695.8	13.2%	$8,813.0	14.8%	$117.2
School Aid Fund					
Net Resources May '11 Basis	$11,111.5	2.7%	$11,234.9	3.9%	$123.4
New Items*	$26.1		$13.3		($12.8)
Adjusted Net General Fund	$11,137.6	3.0%	$11,248.2	4.0%	$110.6
Combined					
Net Resources May '11 Basis	$18,635.6	5.9%	$18,863.4	7.2%	$227.8
New Items*	$1,197.8		$1,197.8		$0.0
Adjusted Net General Fund	$19,833.4	7.2%	$20,061.2	8.5%	$227.8

* New items include non-constitutional revenue sharing sales tax revenue, amnesty revenue, unclaimed property one-time revenue and liquor reform revenue. Those items were previously included as line itmes on the General Fund and School Aid Fund balance sheets and therefore were not included in the consensus estimates.

Prepared By: Office of Revenue and Tax Analysis, Michigan Department of Treasury

FY 2012 Revenue Outlook

FY 2012 GF-GP revenue is forecast to be $8,897.0 million, a 1.0 percent increase compared to FY 2011. The FY 2012 estimate is $144.5 million above the May 2011 Consensus estimate.

SAF revenue is forecast to be $10,824.5 million, representing a 3.8 percent decline compared to FY 2011. The FY 2012 SAF estimate is $199.2 million above the May 2011 Consensus estimate (See Table 3).

Table 3

FY 2011-12 Administration Revenue Estimates

(millions)

	Consensus May 16, 2011		Administration January 13, 2012		
	Amount	**Growth**	**Amount**	**Growth**	**Change**
General Fund - General Purpose					
Net Resources May '11 Basis	$7,805.7	3.7%	$7,888.6	3.4%	$82.9
New Items*	$946.8		$1,007.8		$61.0
Adjusted Net General Fund	$8,752.5	0.7%	$8,897.0	1.0%	$144.5
School Aid Fund					
Net Resources May '11 Basis	$10,645.4	-4.2%	$10,836.8	-3.5%	$191.4
New Items*	($20.1)		($11.7)		$8.4
Adjusted Net School Aid Fund	$10,625.3	-4.6%	$10,824.5	-3.8%	$199.2
Combined					
Net Resources May '11 Basis	$18,451.1	-1.0%	$18,725.4	-0.7%	$274.2
New Items*	$926.7		$996.1		$69.4
Adjusted Net Resources	$19,377.8	-2.3%	$19,721.5	-1.7%	$343.7

* New items include non-constitutional revenue sharing sales tax revenue, amnesty revenue, unclaimed property one-time revenue and liquor reform revenue. Those items were previously included as line itmes on the General Fund and School Aid Fund balance sheets and therefore were not included in the consensus estimates.

Prepared By: Office of Revenue and Tax Analysis, Michigan Department of Treasury

FY 2013 Revenue Outlook

FY 2013 GF-GP revenue is estimated to be $9,019.6 million, a 1.4 percent increase compared to FY 2012. The FY 2013 GF-GP revenue estimate is up $111.5 million above the May 2011 Consensus estimate. SAF revenue is forecast to be $11,149.8 million; representing a 3.0 percent increase compared to FY 2012. The FY 2013 SAF estimate is $184.6 million above the May 2011 Consensus estimate (see Table 4).

Table 4

FY 2012-13 Administration Revenue Estimates

(millions)

	Consensus May 16, 2011		Administration January 13, 2012		
	Amount	**Growth**	**Amount**	**Growth**	**Change**
General Fund - General Purpose					
Net Resources May '11 Basis	$7,955.2	1.9%	$8,034.2	1.8%	$79.0
New Items*	$952.9		$985.4		$32.5
Adjusted Net General Fund	$8,908.1	1.8%	$9,019.6	1.4%	$111.5
School Aid Fund					
Net Resources May '11 Basis	$10,964.3	3.0%	$11,159.2	3.0%	$194.9
New Items*	$0.9		($9.3)		($10.2)
Adjusted Net School Aid Fund	$10,965.2	3.2%	$11,149.8	3.0%	$184.6
Combined					
Net Resources May '11 Basis	$18,919.5	2.5%	$19,193.3	2.5%	$273.8
New Items	$953.8		$976.1		$22.3
Adjusted Net Resources	$19,873.3	2.6%	$20,169.4	2.3%	$296.1

* New items include non-constitutional revenue sharing sales tax revenue, amnesty revenue, unclaimed property one-time revenue and liquor reform revenue. Those items were previously included as line itmes on the General Fund and School Aid Fund balance sheets and therefore were not included in the consensus estimates.

Prepared By: Office of Revenue and Tax Analysis, Michigan Department of Treasury

FY 2014 Revenue Outlook

FY 2014 GF-GP revenue is estimated to be $9,240.2 million, a 2.4 percent increase compared to FY 2013. The FY 2013 GF-GP revenue estimate is $220.6 million above the current FY 2013 GF-GP estimate. SAF revenue is forecast to be $11,474.0 million; representing a 2.9 percent increase compared to FY 2013. The FY 2014 SAF estimate is $324.1 million above the current FY 2013 SAF estimate (see Table 5).

Table 5

FY 2013-14 Administration Revenue Estimates

(millions)

	Administration January 13, 2012	
	Amount	**Growth**
General Fund - General Purpose		
Net Resources May '11 Basis	$8,234.9	2.5%
New Items*	$1,005.3	
Adjusted Net General Fund	$9,240.2	2.4%
School Aid Fund		
Net Resources May '11 Basis	$11,483.8	2.9%
New Items*	($9.8)	
Adjusted Net School Aid Fund	$11,474.0	2.9%
Combined		
Net Resources May '11 Basis	$19,718.7	2.7%
New Items	$995.5	
Adjusted Net Resources	$20,714.2	2.7%

* New items include non-constitutional revenue sharing sales tax revenue, amnesty revenue, unclaimed property one-time revenue and liquor reform revenue. Those items were previously included as line itmes on the General Fund and School Aid Fund balance sheets and therefore were not included in the consensus estimates.

Prepared By: Office of Revenue and Tax Analysis, Michigan Department of Treasury

Constitutional Revenue Limit

Article IX, Section 26, of the Michigan Constitution establishes a limit on the amount of revenue State government can collect in any given fiscal year. The revenue limit for a given fiscal year is equal to 9.49 percent of the State's personal income for the calendar year prior to the year in which the fiscal year begins. For example, FY 2009 revenue is compared to CY 2007 personal income. If revenues exceed the limit by less than 1 percent, the State may deposit the excess into the Budget Stabilization Fund (BSF). If the revenues exceed the limit by more than 1 percent, the excess revenue is refunded to taxpayers.

FY 2010 revenues were $7.6 billion below the revenue limit. State revenues will also be well below the limit for FY 2011 through FY 2014. FY 2011 revenues are expected to be $6.2 billion below the limit, FY 2012 revenues $6.2 billion below the limit, FY 2013 revenues $7.5 billion below the limit, and FY 2014 revenues $7.8 billion below the limit (See Table 6).

Table 6

Administration Revenue Limit Calculation

(millions)

	FY 2010	FY 2011	FY 2012	FY 2013	FY 2014
	Final June 2011	Admin Jan 2012	Admin Jan 2012	Admin Jan 2012	Admin Jan 2012
Revenue Subject to Limit	$25,572.6	$26,333.5	$26,284.8	$26,929.3	$27,709.9
Revenue Limit	**CY 2008**	**CY 2009**	**CY 2010**	**CY 2011**	**CY 2012**
Personal Income	$349,612	$342,302	$342,663	$362,538	$373,776
Ratio	9.49%	9.49%	9.49%	9.49%	9.49%
Revenue Limit	$33,178.2	$32,484.5	$32,518.7	$34,404.9	$35,471.3
Amount Under (Over) Limit	**$7,605.6**	**$6,151.0**	**$6,233.9**	**$7,475.6**	**$7,761.5**

Budget Stabilization Fund Calculation

The Management and Budget Act contains provisions for calculating a recommended deposit or withdrawal from the BSF. The calculation looks at personal income net of transfer payments. The net personal income figure is adjusted for inflation. The change in this figure for the calendar year determines whether a pay-in or pay-out is dictated. If the formula calls for a deposit into the BSF, the deposit is made in the next fiscal year. If the formula calls for a withdrawal, the withdrawal is made during the current fiscal year.

If real personal income grows by more than 2 percent in a given calendar year, the fraction of income growth over 2 percent is multiplied by the current fiscal year's GF-GP revenue to determine the pay-in for the next fiscal year. If real personal income declines, the percentage

deficiency under zero is multiplied by the current fiscal year's GF-GP revenue to determine the withdrawal available for the current fiscal year. If the change in real personal income is between 0 and 2 percent, no pay-in or withdrawal is indicated.

Real calendar year personal income for Michigan is expected to decrease 0.2 percent in 2012. Thus, the formula has a pay-out for FY 2012 of $17.8 million (See Table 7). In 2013, real calendar year personal income for Michigan is forecast to increase 1.2 percent, so the formula calls for no pay-in or pay-out for FY 2013 (See Table 8). In 2014, real calendar year personal income for Michigan is forecast to increase 2.0 percent, so the formula calls for no pay-in or pay-out for FY 2014 (See Table 9).

Table 7

Budget and Economic Stabilization Fund Calculation
Based on CY 2012 Personal Income Growth
Administration Calculation

	CY 2011	CY 2012
Michigan Personal Income	$ 362,538 [1]	$ 373,776 [1]
less Transfer Payments	$ 82,724 [1]	$ 84,732 [1]
Income Net of Transfers	$ 279,814	$ 289,044
Detroit CPI	2.080 [2]	2.153 [3]
for 12 months ending	(June 2011)	(June 2012)
Real Adjusted Michigan Personal Income	$ 134,526	$ 134,252
Change in Real Adjusted Personal Income		-0.2%
Amount Under 0%		-0.2%
GF-GP Revenue Fiscal Year 2011-2012		$ 8,897.0
		FY 2011-2012
BSF Pay-Out Calculated for FY 2012		$ (17.8)

Notes:

[1] Personal Income and Transfer Payments, Administration Forecast, January 2012.

[2] Detroit Consumer Price Index, Average of 6 monthly values reported by BLS for each 12-month period.

[3] Detroit Consumer Price Index, Administration Forecast, January 2012.

Table 8

Budget and Economic Stabilization Fund Calculation
Based on CY 2013 Personal Income Growth
Administration Calculation

	CY 2012	CY 2013
Michigan Personal Income	$373,776 [1]	$385,363 [1]
less Transfer Payments	$ 84,732 [1]	$ 87,302 [1]
Income Net of Transfers	$ 289,044	$ 298,061
Detroit CPI	2.153 [2]	2.193 [2]
for 12 months ending	(June 2012)	(June 2013)
Real Adjusted Michigan Personal Income	$ 134,252	$ 135,915
Change in Real Adjusted Personal Income		1.2%
Between 0 and 2%		0.0%
GF-GP Revenue Fiscal Year 2012-2013		$ 9,019.6

	FY 2012-2013
BSF Pay-In/Pay-Out Calculated for FY 2013	NO PAY-IN OR PAY-OUT

Notes:

[1] Personal Income and Transfer Payments, Administration Forecast, January 2012.

[2] Detroit Consumer Price Index, Administration Forecast, January 2012.

Table 9

Budget and Economic Stabilization Fund Calculation
Based on CY 2014 Personal Income Growth
Administration Calculation

	CY 2013	CY 2014
Michigan Personal Income	$ 385,363 [(1)]	$ 402,319 [(1)]
less Transfer Payments	$ 87,302 [(1)]	$ 92,065 [(1)]
Income Net of Transfers	$ 298,061	$ 310,254
Detroit CPI	2.193 [(2)]	2.237 [(2)]
for 12 months ending	(June 2013)	(June 2014)
Real Adjusted Michigan Personal Income	$ 135,915	$ 138,692
Change in Real Adjusted Personal Income		2.0%
Excess over 2%		0.0%
GF-GP Revenue Fiscal Year 2013-2014		$ 9,240.2

	FY 2013-2014
BSF Pay-Out Calculated for FY 2014	NO PAY-IN OR PAY-OUT

Notes:

[(1)] Personal Income and Transfer Payments, Administration Forecast, January 2012.

[(2)] Detroit Consumer Price Index, Administration Forecast, January 2012.

School Aid Fund Revenue Adjustment Factor

The School Aid Fund (SAF) revenue adjustment factor for the next fiscal year is calculated by dividing the sum of current year and subsequent year SAF revenue by the sum of current year and prior year SAF revenue. For example, the FY 2013 SAF revenue adjustment factor is calculated by dividing the sum of FY 2012 and FY 2013 SAF revenue by the sum of FY 2011 and FY 2012 SAF revenue. The SAF revenue totals are adjusted for any change in the rate and base of the SAF taxes. The year for which the adjustment factor is being calculated is used as the base year for any tax adjustments. For FY 2013, the SAF revenue adjustment factor is calculated to be 1.0284 (See Table 10). For FY 2014, the SAF revenue adjustment factor is calculated to be 1.0286 (See Table 11).

Table 10

Administration School Aid Revenue Adjustment Factor

For Fiscal Year 2013

	FY 2011	FY 2012	FY 2013
Baseline SAF Revenue	$11,261.5	$11,559.2	$11,868.7
Balance Sheet Adjustments	($13.2)	($734.7)	($718.9)
Net SAF Estimates	$11,248.3	$10,824.5	$11,149.8
Subtotal Adjustments to FY 2013 Base	($705.7)	$15.8	$0.0
Baseline Revenue on a FY 2013 Base	$10,542.5	$10,840.3	$11,149.8

School Aid Fund Revenue Adjustment Calculation for FY 2013

Sum of FY 2011 & FY 2012	$10,542.5	+	$10,840.3	=	$21,382.8
Sum of FY 2012 & FY 2013	$10,840.3	+	$11,149.8	=	$21,990.1

FY 2013 Revenue Adjustment Factor	**1.0284**

Note: Factor is calculated off a FY 2013 base year.

Table 11

Administration School Aid Revenue Adjustment Factor

For Fiscal Year 2014

	FY 2012	FY 2013	FY 2014
Baseline SAF Revenue	$11,559.2	$11,868.7	$12,189.0
Balance Sheet Adjustments	($734.7)	($718.9)	($715.1)
Net SAF Estimates	$10,824.5	$11,149.8	$11,473.9
Subtotal Adjustments to FY 2014 Base	$19.6	$3.9	$0.0
Baseline Revenue on a FY 2014 Base	$10,844.2	$11,153.6	$11,473.9

School Aid Fund Revenue Adjustment Calculation for FY 2014

Sum of FY 2012 & FY 2013	$10,844.2	+	$11,153.6	=	$21,997.8
Sum of FY 2013 & FY 2014	$11,153.6	+	$11,473.9	=	$22,627.5

FY 2014 Revenue Adjustment Factor	**1.0286**

Note: Factor is calculated off a FY 2014 base year.

Revenue Detail

The estimated tax and revenue totals include the effects of all enacted tax changes except sales tax savings resulting from reductions in revenue sharing payments to local units. The revenue totals by tax are presented separately for GF-GP and for the SAF (See Tables 12 and 13). Tax totals for the income, sales, use, tobacco and casino taxes for all funds are also included (See Table 14).

Table 12

Administration General Fund General Purpose Revenue Detail

(millions)

	FY 2012		FY 2013		FY 2014	
	Amount	**Growth**	**Amount**	**Growth**	**Amount**	**Growth**
GF-GP Tax Amounts						
Income Tax	$4,856.9	9.3%	$5,659.4	16.5%	$5,910.8	4.4%
Sales	$1,093.3	2.5%	$1,123.5	2.8%	$1,159.4	3.2%
Use	$805.4	9.7%	$844.0	4.8%	$877.3	3.9%
Cigarette	$188.7	-3.6%	$185.3	-1.8%	$180.4	-2.6%
Beer & Wine	$49.0	4.0%	$50.0	2.0%	$51.0	2.0%
Liquor Specific	$40.0	1.3%	$41.0	2.5%	$41.5	1.2%
Single Business Tax	$0.0	NA	$0.0	NA	$0.0	NA
Insurance Co. Premium	$280.0	3.2%	$286.9	2.5%	$292.4	1.9%
MBT/CIT	$1,058.5	-21.9%	$368.1	-65.2%	$278.6	-24.3%
Telephone & Telegraph	$57.0	1.6%	$56.0	-1.8%	$55.0	-1.8%
Oil & Gas Severance	$65.6	9.7%	$69.0	5.2%	$73.0	5.8%
GF-GP Other Taxes	$1.2	-95.0%	$13.0	983.3%	$16.0	23.1%
Total GF-GP Taxes	$8,495.6	2.7%	$8,696.2	2.4%	$8,935.4	2.8%
GF-GP Non-Tax Revenue						
Federal Aid	$20.0	15.6%	$20.0	0.0%	$20.0	0.0%
From Local Agencies	$0.4	-83.3%	$0.4	0.0%	$0.4	0.0%
From Services	$9.5	-20.2%	$9.5	0.0%	$9.5	0.0%
From Licenses & Permits	$20.0	29.9%	$20.0	0.0%	$20.0	0.0%
Miscellaneous	$20.0	177.8%	$25.0	25.0%	$25.0	0.0%
Driver Responsibility Fees	$103.0	1.0%	$91.0	-11.7%	$81.0	-11.0%
Interfund Interest	($8.1)	24.6%	($9.2)	13.6%	($18.8)	104.3%
Liquor Purchase	$154.1	-6.2%	$156.1	1.3%	$157.1	0.6%
Charitable Games	$11.5	23.7%	$11.5	0.0%	$11.5	0.0%
Transfer From Escheats	$71.0	-67.0%	($1.0)	-101.4%	($1.0)	0.0%
Other Non Tax	$0.0	0.0%	$0.0	0.0%	$0.0	0.0%
Total Non Tax	$401.4	-25.5%	$323.3	-19.5%	$304.7	-5.8%
Total GF-GP Revenue	$8,897.0	1.0%	$9,019.6	1.4%	$9,240.2	2.4%

Table 13

Administration School Aid Fund Revenue Detail

	FY 2012		FY 2013		FY 2014	
	Amount	Growth	Amount	Growth	Amount	Growth
School Aid Fund						
Income Tax	$2,123.3	7.6%	$2,256.1	6.3%	$2,356.7	4.5%
Sales Tax	$5,041.9	3.3%	$5,176.0	2.7%	$5,333.4	3.0%
Use Tax	$402.7	9.7%	$422.0	4.8%	$438.7	3.9%
Liquor Excise Tax	$40.0	2.3%	$41.0	2.5%	$41.5	1.2%
Cigarette & Tobacco	$364.0	-3.2%	$353.1	-3.0%	$341.7	-3.2%
State Education Tax	$1,818.5	-1.4%	$1,840.0	1.2%	$1,869.5	1.6%
Real Estate Transfer	$132.9	7.9%	$148.8	12.0%	$166.8	12.1%
Michigan Business Tax	$0.0	-100.0%	$0.0	NA	$0.0	NA
Industrial Facilities Tax	$43.9	0.7%	$45.4	3.4%	$47.4	4.4%
Casino (45% of 18%)	$109.8	-3.7%	$104.0	-5.3%	$105.0	1.0%
Commercial Forest	$3.1	3.3%	$3.1	0.0%	$3.1	0.0%
Other Spec Taxes	$14.0	-28.2%	$14.0	0.0%	$14.0	0.0%
Subtotal Taxes	$10,094.0	-4.1%	$10,403.3	3.1%	$10,718.0	3.0%
Lottery Transfer	$730.5	0.5%	$746.5	2.2%	$756.0	1.3%
Total SAF Revenue	$10,824.5	-3.8%	$11,149.8	3.0%	$11,474.0	2.9%

Table 14

Adminstration Major Tax Totals

	FY 2012		FY 2013		FY 2014	
	Amount	Growth	Amount	Growth	Amount	Growth
Major Tax Totals (Includes all Funds)						
Income Tax	$6,981.1	8.8%	$7,916.5	13.4%	$8,268.5	4.4%
Sales Tax	$6,933.9	3.4%	$7,117.1	2.6%	$7,332.1	3.0%
Use Tax	$1,208.1	9.7%	$1,266.0	4.8%	$1,316.0	3.9%
MBT/CIT	$1,058.5	-49.4%	$368.1	-65.2%	$278.6	-24.3%
Cigarette and Tobacco	$938.0	-3.1%	$919.0	-2.0%	$893.8	-2.7%
Casino Tax	$109.8	-3.7%	$104.0	-5.3%	$105.0	1.0%