Outlook Outline

• National Economic Trends
• Planning District Recent Economic Performance
• Planning District Tax Revenue Trends
• The Fiscal Cliff
• State Fiscal Cliff Impacts
• Planning District Fiscal Cliff Impacts
• Conclusions
National Economic Trends
Gross Domestic Product Components

• Gross Domestic Product (GDP). Total Value of Goods and Services Produced in the United States
• GDP=C+I+G+(X-M)
  • C= Personal Consumption
  • I=Investment
  • G=Government Expenditures
  • X-M= Net Exports
Components of GDP Growth

Source: Bureau of Economic Analysis
Contribution of Residential Investment to GDP Growth

Source: Bureau of Economic Analysis
Contribution of Federal Government Expenditures to GDP Growth

Source: Bureau of Economic Analysis
Contribution of Personal Consumption Expenditures to GDP Growth

Source: Bureau of Economic Analysis
Federal Reserve Assets

Source: Federal Reserve
Treasury Yields and Consumer Interest Rates
Private Balance Sheet Repair

- Household debt has decreased
  - Debt payoff
  - Defaults
- Asset values have increased
  - Real Estate is no longer a drain on wealth
  - Stock and bond markets have been relatively buoyant
Absence Major Reforms, Federal Debt reaches 90 percent of GDP in 2021
- Reinhart and Rogoff (2011). Above 90 percent, median growth roughly 1 percent lower; average growth almost 4 percent lower
- Federal Debt reaches 100 percent of GDP in 2024
- Budget Control Act of 2011 (Sequestration) alone doesn’t control the debt
Thomas Jefferson Planning District Recent Performance
Employment Growth

Charlottesville MSA trough not as deep.
Rebound is similar to state and nation.

Unemployment Rate

TJPD unemployment rate spread with Virginia has grown in recovery.

Source: Bureau of Labor Statistics (last point in October 2012)
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Unemployment and Poverty Rates

Source: Bureau of Labor Statistics and U.S. Census Bureau
Population Growth

% change

Source: Bureau of Economic Analysis
Per Capita Income Compared to U.S

% of U.S.

Source: Bureau of Economic Analysis
Intraregional Per Capita Income Convergence

% of U.S.

Source: Bureau of Economic Analysis
Retail Sales: Local Option Sales Tax

Retail sales rebound.

Source: Virginia Department of Taxation, 12 month moving average
Building Permits

% of 2000 Census single-unit detached housing units

Housing construction pickup not as pronounced as VA, US

Source: U.S. Census Bureau (2012 estimated based on Jan.-Oct.)
Building Permits by Locality

Source: U.S. Census Bureau (2012 estimated based on Jan.-Oct.)
Building Permits by Locality

% of District Total

Source: U.S. Census Bureau (2012 estimated based on Jan.-Oct.)
Housing Price Changes

Housing prices are stabilizing

Source: Federal Housing Finance Agency
TJPD Employment Change, 2006-2011

Economy is less diversified

Source: Bureau of Economic Analysis

*Size represents total employment
Eds and Meds Economic Footprint

- Eds and Meds
  - Eds (higher education--2 year college and university)
  - Meds (hospitals, ambulatory care, doctor’s offices, nursing homes, home health)

- Economic Footprint
  - 33,000 direct jobs
  - 52,000 total (direct, indirect, and induced)
  - 52,000 economic footprint/147,000 total jobs=35%
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District Revenue Trends
Sources of TJPD Local Revenue, FY 2011

Sources of Local Government Revenue
- Local: 64%
- State aid: 28%
- Federal aid: 8%

Sources of Local Tax Revenue
- Real property: 61%
- Personal property: 10%
- Local sales and use: 7%
- Public service corporation property: 6%
- Business license: 4%
- Restaurant meals: 3%
- All other: 9%

Source: Virginia Auditor of Public Accounts
TJPD Sources of Local Government Revenue, FY 2001 to FY 2011

Source: Virginia Auditor of Public Accounts
TJPD Change in Sources of Local Government Revenue

% change

Source: Virginia Auditor of Public Accounts
TJPD Local Government Revenue from Taxes and Nontax Sources

Source: Virginia Auditor of Public Accounts
TJPD Local Government Revenue from Tax Sources

Source: Virginia Auditor of Public Accounts
TJPD Per Capita Local Tax Revenue in Constant Dollars

Source: Virginia Auditor of Public Accounts
TJPD Consumer Taxes

Source: Virginia Auditor of Public Accounts and Bureau of Economic Analysis
TJPD Consumer Tax Revenue and Personal Income Growth

% change


Tax Revenue (Sales and Use, Restaurant and Food)

Personal Income

Source: Virginia Auditor of Public Accounts and Bureau of Economic Analysis
The Fiscal Cliff
Components of Fiscal Cliff, FY 2013

- “Fiscal Cliff” term coined by Fed Chair Ben Bernanke
- Spending Decreases (1/5)
  - Sequestration
  - Expiration of Emergency Unemployment Benefits
  - “Doc Fix”
- Tax Increases (4/5)
  - AMT (Alternative Minimum Tax) expansion
  - Tax Extenders Expiration
  - Payroll Tax Increase
  - Taxes in Affordable Care Act

Source: Congressional Budget Office (May)
Fiscal Cliff Hype versus Reality

- Many cuts/tax increases have routinely been deferred (e.g., Doc Fix, AMT, “Tax Extenders”)
- Fiscal Cliff type policies are already occurring
  - The first phase of sequestration imposed discretionary spending caps that began in FY12
  - Affordable Care Act spending decreases already implemented
- Some components will be spread out throughout this fiscal year and next
- Fiscal Cliff has already affected business activity
  - Companies have been delaying or decreasing business investment and hiring
“Sequestration” ($103 Billion)

- Budget Control Act (BCA) of 2011
  - Provided increases in debt limit in return for budget caps and cuts later ($2.1 million savings).
  - Sum over 10 years is equal to debt limit increase.
  - Cuts divided evenly between defense and nondefense.
  - Cuts needed because of failure of “Supercommittee”
  - Some expenditures are exempt (e.g. social security, most unemployment payments, veterans benefits, Medicaid)
Unemployment Insurance Benefits ($26 Billion)

- Emergency Unemployment Compensation (EUC) created by and American Recovery and Reinvestment Act (“Fiscal Stimulus”)
  - Extended one year by The Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010
  - Extended again by Middle Class Tax Relief and Job Creation Act of 2012

Source: Congressional Budget Office
Sustainable Growth Rate ($11 Billion)

- **Sustainable Growth Rate (SGR) “Doc Fix”**
  - Enacted by the Balanced Budget Act of 1997 to control health care costs
  - Physician service costs are growing at twice the rate allowed by SGR
  - Medicare physician payment rates would be reduced by 27 percent.
  - Congress routinely cancels cuts
  - The adjustment becomes more expensive each time

Source: Congressional Budget Office
Bush Tax Cuts and Alternative Minimum Tax (AMT) ($221 Billion)

  - Bush Tax Cuts were passed using “reconciliation process”. They are subject to 10 year window imposed by Byrd Rule.
- Cliff Components
  - Raise individual income tax rates
  - Raise tax rates on long-term capital gains and dividends
  - Reduce child tax credit and earned income tax credit
  - Lower estate threshold and raise tax rate
- Extended 2 years by Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010

A Comparison of 2013 Income Tax Brackets
Married Filing Jointly

<table>
<thead>
<tr>
<th>Taxable Income</th>
<th>Bush Tax Cuts In Place (tax rate)</th>
<th>Bush Tax Cuts Expired (tax rate)</th>
</tr>
</thead>
<tbody>
<tr>
<td>$0 - $17,800</td>
<td>10%</td>
<td>15%</td>
</tr>
<tr>
<td>$17,800 - $60,350</td>
<td>15%</td>
<td>15%</td>
</tr>
<tr>
<td>$60,350 - $72,300</td>
<td>15%</td>
<td>28%</td>
</tr>
<tr>
<td>$72,300 - $145,900</td>
<td>25%</td>
<td>28%</td>
</tr>
<tr>
<td>$145,900 - $222,300</td>
<td>28%</td>
<td>31%</td>
</tr>
<tr>
<td>$222,300 - $397,000</td>
<td>33%</td>
<td>36%</td>
</tr>
<tr>
<td>$397,000-</td>
<td>35%</td>
<td>39.6%</td>
</tr>
</tbody>
</table>

Source: Joint Committee on Taxation
Alternative Minimum Tax (AMT)

- AMT designed so high earners would pay some minimum level of taxes
  - Add back in tax preferences. Use basic exemption and apply tax rate. Pay larger of regular income tax or AMT
  - Basic exemption not indexed for inflation. More taxpayers affected.
- Basic exemption raised many years to avoid affecting more taxpayers
  - 1997: 605,000 taxpayers (1% of all taxpayers)
  - 2009: 3.8 million (2.7% of all taxpayers)
  - 2012: 34 million (20% of all taxpayers)
  - 2022: 58 million
- AMT patch becomes more expensive over time
  - Repealing AMT without Bush tax cuts costs $1.3 trillion 2013-2022, with tax cuts $4.1 million

Source: Congressional Research Service
Payroll Tax Increase ($95 Billion)

- Created by Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 ("Obama-GOP Tax Deal")
  - Reduced employee’s payroll tax rate from 6.2% to 4.2%
  - Lost SS Trust Fund revenue made up with transfers from the general fund
- Extended to 2012 by The Middle Class Tax Relief and Job Creation Act of 2012

Source: U.S. Social Security Administration
Other Expiring Tax Provisions ($65 billion)

- **Tax Extenders**
  - Individual deductions
  - Business deductions and credits (R&D, foreign source income, depreciation)
  - Charitable giving
  - Energy
  - Community Development
  - Disaster Relief

- **ARRA tax cuts**
  - American Opportunity Tax credit

**Number of Federal Tax Provisions Expiring**

Source: American Enterprise Institute
Affordable Care Act Taxes ($18 Billion)

- Budgetary stimulus effects vary over FY 2010-2019 period
  - Early cuts in expenditures and steady increase in revenues.
  - Real spending impetus begins in 2014.
- 2013 Provisions
  - 0.9% increase in Medicare HI (hospital insurance) payroll tax for higher earners and 3.8 percent increase on investment income
  - 2.3% excise tax on medical devices

Source: Congressional Budget Office (2010)
What Effect will the Fiscal Cliff have in on the Economy in the Short Run?

- Fiscal contraction of this size (3-5% of GDP) is very unusual:
  - Revenue and Expenditure Control Act (1968).
    - 10% surcharge on income taxes. Social security payroll tax hike.
      Increase in phone and auto excise taxes (3.1% of GDP)
    - From GDP growth pace of 5% and 4% unemployment into recession
    - Recession was very mild and short (11 months duration)

- Most forecasts show that fiscal cliff will push economy into recession.
  - Forecasts of magnitude and length of recession vary
    - Different types of models (underlying features)
    - Different input data (types of scenarios modeled, estimates of magnitude of fiscal cliff components)
## Fiscal Cliff Forecasts, 2013

<table>
<thead>
<tr>
<th>Organization</th>
<th>Budgetary Impact (% of GDP)</th>
<th>Economic Impact (% of GDP)</th>
<th>Policies Included</th>
</tr>
</thead>
<tbody>
<tr>
<td>CBO</td>
<td>3.3%</td>
<td>0.3% to 2.9%</td>
<td>Tax cuts, AMT, jobs measures, sequester</td>
</tr>
<tr>
<td>CRFB</td>
<td>4.2%</td>
<td>2.2%</td>
<td>Tax cuts, AMT, sequester, doc fix, ACA, jobs measures</td>
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<tr>
<td>Moody’s</td>
<td>4.2%-4.5%</td>
<td>3.6%</td>
<td>Tax cuts, AMT, sequester, doc fix, ACA, jobs measures</td>
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<tr>
<td>Morgan Stanley</td>
<td>5%</td>
<td>2.5% to 7.5%</td>
<td>Tax cuts, jobs measures, sequester, war drawdown, ACA</td>
</tr>
<tr>
<td>Goldman Sachs</td>
<td>4%</td>
<td>4%</td>
<td>Tax cuts, sequester, jobs measures</td>
</tr>
<tr>
<td>Bank of America</td>
<td>4.6%</td>
<td>N/A</td>
<td>Tax cuts, AMT, jobs measures, sequester, doc fix, BCA</td>
</tr>
<tr>
<td>Merrill Lynch</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Source: Committee for a Responsible Federal Budget (CRFB)
Virginia is More Vulnerable to Federal Cuts

Federal Nondefense Workforce as % of Total
Nondefense Spending as % of GDP
Defense Spending as % of GDP
Federal Spending as % of GDP
Federal Grants Subject to Sequester as % of State Revenue

Source: Pew Center on the States

Note: DC, MD, and VA combined because of common commuting area.
Some Virginia Results

• Sequestration
  • Center for Regional Analysis (George Mason University) and Chmura Analytics.
    • *The Economic Impact of the Budget Control Act of 2011 on DOD and non-DOD Agencies* (for the Aerospace Industries Association)
      • 207,571 job losses in FY 2013
    • *Assessing the Impact of the Federal Budget Cuts on the Virginia Economy* (for the Virginia Economic Development Partnership)
      • 164,225 cumulative job year losses FY 2012-2013
  • Hampton Roads Planning District Commission.
    • Total job impact in Hampton Roads region —26,500 (2014)

• Fiscal Cliff
  • American Action Forum. *The Fiscal Cliff: What you need to know and how to avoid it.*
    • 35,700 to 223,400 total jobs
State Fiscal Cliff Impacts
Methodology

• Regional Economic Models Inc. Policy Insight (REMI PI+) Model for Virginia
• Model is well respected with solid theoretical foundation
• Components of Fiscal Cliff expenditure and tax changes were mapped onto REMI policy variables
• Input data were drawn from Congressional Budget Office (2013) and National Association of Manufacturers (2014-2022)
Economic Impact Scenarios

- Three Economic Impact Scenarios
  - #1: Health care tax implementation, payroll tax holiday suspension, emergency unemployment insurance benefit suspension
  - #2: +Sequestration
  - #3: Fall off the fiscal cliff
Virginia Employment Under Scenarios

Source: Weldon Cooper Center, Virginia REMI Model
Virginia Employment Growth Under Scenarios

% change

Contraction is sharper and deeper than Great Recession for VA

Source: Weldon Cooper Center, Virginia REMI Model
Virginia Employment Impacts under Scenarios

-226,755
-256,840
-252,911
-249,705
-244,712

-300,000
-250,000
-200,000
-150,000
-100,000
-50,000
0

2013 2014 2015 2016 2017 2018

Scenario I
Scenario II
Scenario III
Virginia versus U.S. Employment Growth with Fiscal Cliff

% change

Source: Weldon Cooper Center, Virginia REMI Model
Longer Run Trends

Source: Weldon Cooper Center, Virginia REMI Model
State Revenue, Actual and Forecast by Calendar Year

Governor’s Revenue Estimates will be released with budget on December 17

Source: U.S. Census Bureau, State Government Finances; Weldon Cooper Center, Virginia REMI Model
Other State Revenue Effects

• Virginia tax code is linked to the federal tax code
  • Reduction in federal tax credits (Earned Income Tax Credit, Child and Dependent Care Credit) Reduction in federal business deductions
  • Decrease in federal corporate income deductions (e.g. enhanced expensing and bonus depreciation rules)
  • Change in treatment of Estate Taxes

THE IMPACT OF THE FISCAL CLIFF ON THE STATES
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District Fiscal Cliff Impacts
Virginia versus U.S. Growth with Fiscal Cliff

% change

-3 -2 -1 0 1 2 3 4

Source: Weldon Cooper Center, Virginia REMI Model

Less severe for TJPD here

More severe than US but less than VA here
TJPD Employment Growth

4/5ths as deep as Great Recession and half as long

Source: Weldon Cooper Center, Virginia REMI Model
TJPD Employment

Source: Weldon Cooper Center, Virginia REMI Model
Consumer Tax Revenue and Personal Income Growth

% change

Taxes
Personal Income

Source: Weldon Cooper Center, Virginia REMI Model
List of Federal Grants/Programs on Sequestration Chopping Block

- Community Development Block Grants (CDBG) and USDA Rural Development Programs
- U.S. Economic Development Administration (EDA)
- Home Investment Partnership Program (affordable housing)
- Section 8 Housing
- Department of Justice State and Local Law Enforcement Assistance Grants and The Community Oriented Policing Services (COPS) Program
- EPA State and Local Grants
- The Department of Labor Training and Employment Services account
- The Department of Education Accelerating Achievement and Ensuring Equity Account
- FEMA State and Local Programs, which include Urban Area Security Initiative grants and the State Homeland Security Grant program
- AMTRAK funding
- Federal Transit Capital Investment Grants
- Rebate payments on Build America Bonds

Source: National League of Cities based on Office of Management and Budget
Conclusions
Conclusions

• TJPD has weathered the recent five years as well as the state and better than the nation.
• There is much uncertainty about how severely Sequestration would affect Virginia. The composition and geographical distribution of the cuts is undetermined. But, it will undoubtedly be more severe than other states.
• A Fiscal Cliff induced recession SHOULD be less deep and of shorter duration than the Great Recession for TJPD. For the state, it will be deeper but shorter than Great Recession.
• Even if Fiscal Cliff is avoided, nation, state, and region face slower growth than easy money induced growth of 90s and 2000s. Adapting to new era of lower expectations may be difficult.
e-REMI

http://data.eremi.com
Username: demo
Password: demo