ECONOMIC OUTLOOK
AND
REVENUE ESTIMATES
FOR MICHIGAN

FISCAL YEARS

2003-04 AND 2004-05

HOUSE FI$CAL AGENCY

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FOREWORD

The House Fiscal Agency (HFA) is pleased to present this report to members of the Michigan House of Representatives. The purpose of the report is to inform members of the final General Fund/General Purpose and School Aid Fund revenue for fiscal year (FY) 2002-03, and the revised revenue estimates for FY 2003-04 and FY 2004-05. The estimates reported herein will be presented to the Consensus Revenue Estimating Conference on May 18, 2004, and will be used to facilitate the consensus estimating process.

This report includes HFA analyses of important factors that will affect state and national economies through the year 2005, estimates of the Countercyclical Budget Stabilization Fund, state compliance with the Constitutional State Revenue Limit, and year-end balance estimates for General Fund/General Purpose and the School Aid Fund.

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EXECUTIVE SUMMARY

According to the National Bureau of Economic Research, the national economic recovery started at the end of 2001. Since the recovery began, high productivity gains have outpaced economic growth, and this has dampened national employment. During the first four months of 2004, however, national employment posted an average gain of 217,000—the best four-month performance since the beginning of the recovery.

Michigan's wage and salary employment has generally trended downward since the beginning of 2001. In March, Michigan's wage and salary employment grew only by 6,000, but the growth was broad based.

U. S. Forecast

Real GDP growth is forecast to increase 4.5% in CY 2004, up from 3.1% in CY 2003. Real GDP is forecast to grow 4.0% in CY 2005.

Inflation, as measured by the Consumer Price Index (CPI), is forecast to increase from 2.3% in CY 2003 to 2.4% in CY 2004, then decelerate to 2.2% in CY 2005.

Light vehicle sales totaled 16.7 million units in CY 2003 and are forecast to fall to 16.6 million units in CY 2004, then increase to 16.9 million units in CY 2005. The import share of light vehicles is forecast to be 20.0% in CY 2004 and 20.2% in CY 2005.

The *national unemployment rate*, which was 6.0% in CY 2003, is forecast to decrease to 5.7% in CY 2004, then fall to 5.3% in CY 2005.

Interest rates on three-month T-bills averaged 1.0% in CY 2003 and are forecast to increase to 1.1% in CY 2004 before increasing to 2.4% in CY 2005.

Michigan Forecast

Michigan personal income increased 2.5% in CY 2003. The rate of growth will pick up to 3.8% in CY 2004 and 6.0% in CY 2005.

Michigan's unemployment rate was 7.3% in CY 2003 and is forecast to decrease to 6.9% in CY 2004 and 6.4% in CY 2005.

Inflation, as measured by the Detroit Consumer Price Index, was 2.0% in CY 2003; it is forecast to increase to 2.3% in CY 2004, then decelerate slightly to 2.2% in CY 2005.

■ ***State Revenues***

Final *total baseline GF/GP and SAF revenues* were $18.2 billion in FY 2002-03, and are forecast to increase 2.3% to $18.6 billion in FY 2003-04, followed by an increase of 3.9% to $19.3 billion in FY 2004-05. Baseline revenues do not include prior-year fund balances or reflect the effects of recent tax policy changes.

Final total actual GF/GP and SAF revenues were $18.7 billion in FY 2002-03 and are forecast to decrease $186.4 million or 0.1% in FY 2003-04 and increase $380.0 million or 2.1% to $18.9 billion in FY 2004-05. Actual revenues are resources available.

■ *State Revenue Limit*

Final total state revenues are expected to be below the state revenue limit by $4.4 billion in FY 2002-03 and are estimated to be under the limit by $5.1 billion in FY 2003-04 and $5.0 billion in FY 2004-05. Final calculation of the state revenue limit is performed by the Auditor General.

■ *Year-End Fund Balances*

The *year-end GF/GP balance* was $174.0 million in FY 2002-03. No year-end balance is estimated for FY 2003-04.

The *School Aid Fund year-end balance* was $113.7 million in FY 2002-03. No year-end balance is estimated for FY 2003-04.

The *Countercyclical Budget Stabilization Fund year-end balance* was $0.0 in FY 2002-03 and is forecast to be $0.0 in FY 2003-04 and $154.0 million in FY 2004-05.

■ *Baseline and Actual Revenue Estimates*

Table 1 reports GF/GP and SAF revenues in terms of baseline and actual revenues.

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

Actual GF/GP revenues capture the effects of all policy changes and represent resources actually available. *Actual SAF revenues* do not include beginning fund balances or transfers from the BSF or GF/GP.

Tables 2 and 3 report HFA's recommended GF/GP and SAF revisions for FY 2003-04 and FY 2004-05.

Table 1

HFA REVENUE ESTIMATES (Millions of Dollars)

	Final FY 2002-03	HFA Estimate FY 2003-04	HFA Estimate FY 2004-05
BASELINE			
GF/GP	$7,944.8	$8,129.9	$8,449.3
SAF	10,255.7	10,483.3	10,896.4
TOTAL	**$18,200.5**	**$18,613.2**	**$19,345.7**
ACTUAL			
GF/GP	$7,958.9	$7,915.2	$7,890.5
SAF	10,714.8	10,572.2	10,976.9
TOTAL	**$18,673.8**	**$18,487.4**	**$18,867.4**

NOTE: Numbers may not add due to rounding.

Table 2

FISCAL YEAR 2003-04 HFA RECOMMENDED REVISIONS (Millions of Dollars)

	January 2004 Consensus	HFA May 2004 Recommendation	Recommended Revision
BASELINE			
GF/GP	$8,045.5	$8,129.9	$84.4
SAF	10,495.4	10,483.3	(12.1)
TOTAL	**$18,540.9**	**$18,613.2**	**$72.3**
ACTUAL			
GF/GP	$7,857.5	$7,915.2	$57.7
SAF	10,584.3	10,572.2	(12.1)
TOTAL	**$18,441.9**	**$18,487.4**	**$45.5**

NOTE: Numbers may not add due to rounding.

Table 3

FISCAL YEAR 2004-05 HFA RECOMMENDED REVISIONS (Millions of Dollars)

	January 2004 Consensus	HFA May 2004 Recommendation	Recommended Revision
BASELINE			
GF/GP	$8,369.3	$8,449.3	$80.0
SAF	10,917.9	10,896.4	(21.5)
TOTAL	**$19,287.3**	**$19,345.7**	**$58.4**
ACTUAL			
GF/GP	$7,822.8	$7,890.5	$67.7
SAF	10,998.5	10,976.9	(21.6)
TOTAL	**$18,821.3**	**$18,867.4**	**$46.1**

NOTE: Numbers may not add due to rounding.

ECONOMIC REVIEW AND FORECAST

This section presents the economic forecast used by the House Fiscal Agency to produce its updated revenue forecast for FY 2003-04 and FY 2004-05.

The longest U.S. economic expansion on record ended in March 2001 as the economy slid into a brief, eight-month recession that ended in November 2001. Although the recession was modest, economic growth remained weak throughout CY 2002 and the early part of CY 2003.

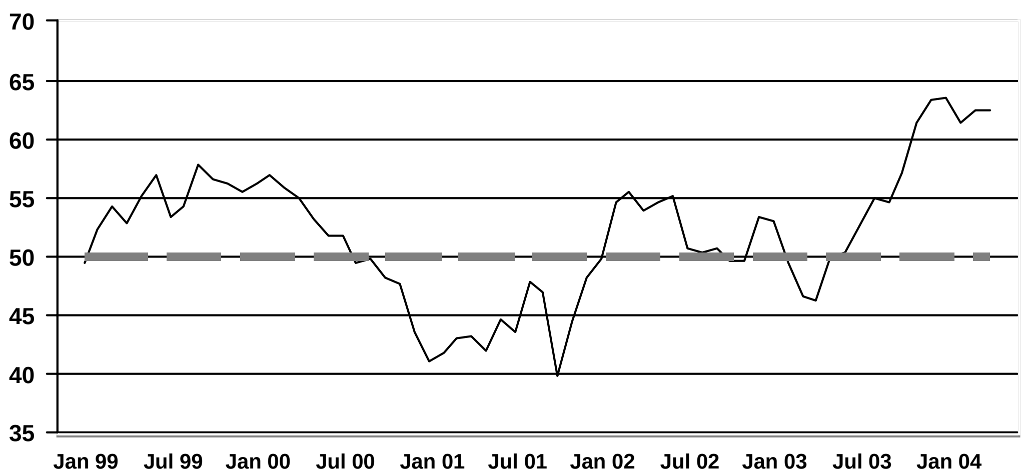
During CY 2003, real GDP grew at annual rates of 8.2% during the third quarter and 4.1% during the fourth quarter. For the year as a whole, real GDP grew 3.1%.

As economic growth begins to accelerate, it is forecast that real GDP will grow by 4.5% in CY 2004 and 4.0% in CY 2005.

Figure 1 shows the Institute for Supply Management (ISM) Index beginning with January 1999. An index number above 50 indicates a growing manufacturing sector, while a number below 50 suggests that the manufacturing sector is contracting.

Figure 1

Institute for Supply Management (ISM) Index



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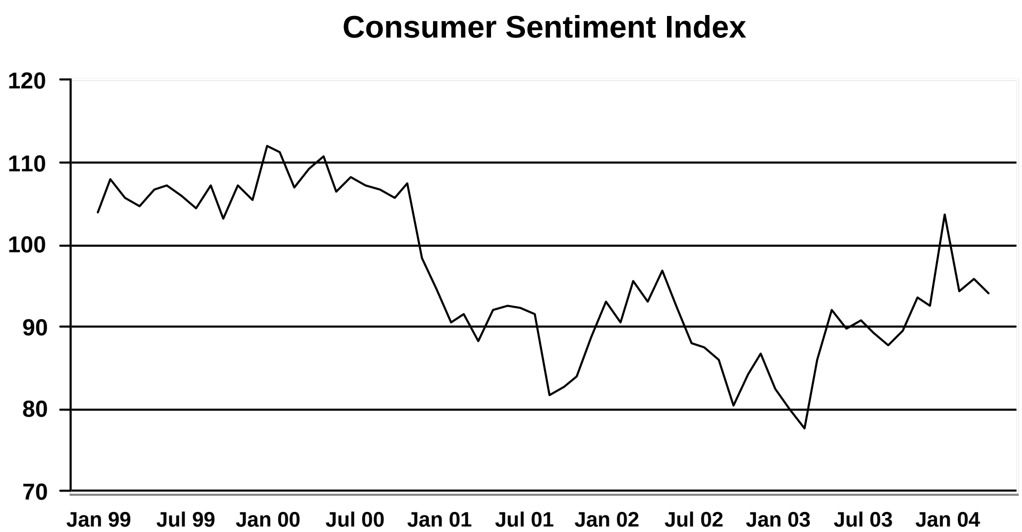
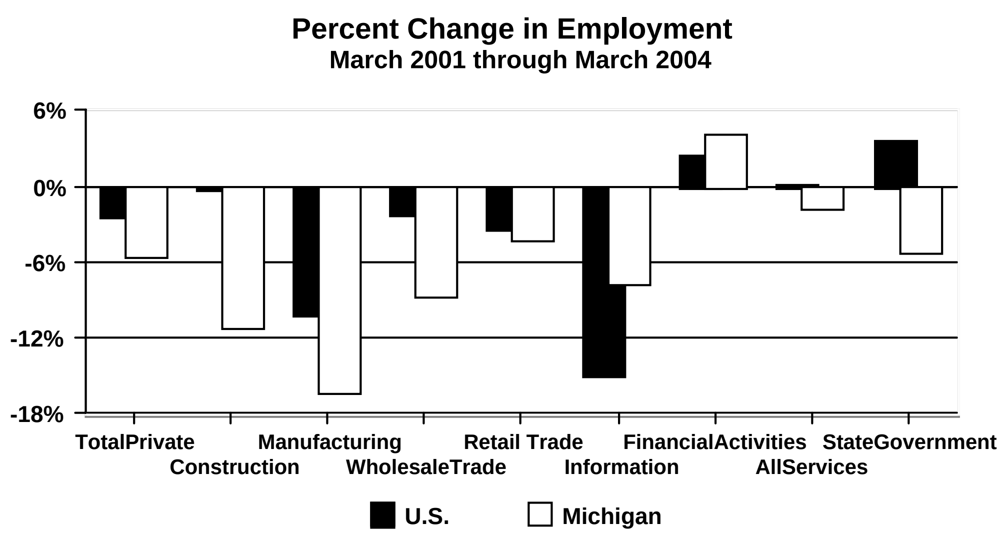


Figure 3



The index reached a peak in December 1999, then fell below 50 in August 2000 and remained below 50 until February 2002. After peaking in June 2002, the index began to drop, and by September it had fallen below 50, where it remained before jumping to 54.7 in December.

The ISM index started 2003 by falling for four consecutive months, then began a strong upward trend and finished the year at a 20-year high before settling back somewhat in February and March 2004.

A somewhat similar story is portrayed in **Figure 2**, which shows the University of Michigan Index of Consumer Sentiment. Consumer sentiment is a driving force behind personal consumption expenditures, which represent almost two-thirds of

GDP. Thus, even though the ISM index began to fall in early 2000, consumers remained cautiously optimistic about the economy.

Although the consumer sentiment index remained at historically high levels throughout most of CY 2000, it dropped in December 2000 and continued falling until February 2001. Like the ISM index, consumer sentiment rebounded somewhat through August 2001 before plunging again in September 2001.

The index of consumer sentiment began 2003 with a three-month drop before rebounding in April and May. Since then, consumer sentiment has remained mixed, and the index has generally followed an upward trend comprised of small monthly changes.

Unlike the ISM index, consumer sentiment has not risen dramatically over the past few months. Thus, while the business sector remains poised to continue expanding the economy, consumers appear to be uncertain about overall economic conditions, and are reacting with caution. This divergence probably can be traced to the performance of the labor market beginning with the onset of the 2001 recession.

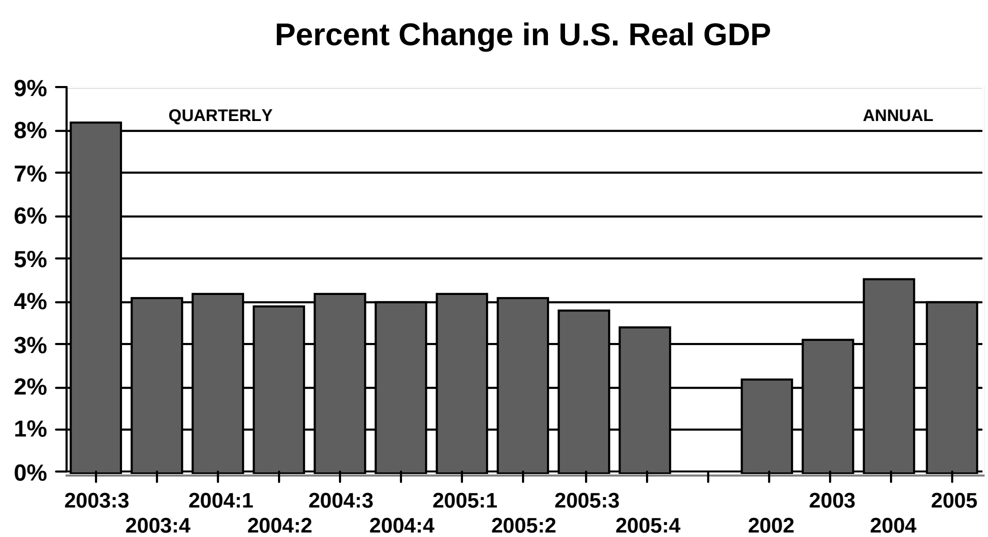
Figure 3 shows the percentage change in employment over the past three years for all private workers, as well as several important sectors of the economy for both the U.S. and Michigan. Of the more than 2.5 million job losses in the U.S. over this period, 213,600 (8.5%) can be attributed to Michigan, and of these losses, slightly more than 64.1% were in the Manufacturing sector.

Both Michigan and the U.S. have endured declines in Construction, Manufacturing, Wholesale and Retail Trade, and Information, and with the exception of the Information sector, Michigan's rates of decline have exceeded those of the U.S.

Overall employment growth for the U.S. has been positive in the Financial Activities, Services, and State Government sectors. In contrast, Michigan has experienced employment declines in all but the Financial Activities sector, which gained just over 8,000 jobs.

Recent employment reports at the national level have been positive, and there are signs that the labor market is beginning to recover. Although this has not yet produced significant employment growth at the state level, Michigan's recovery in the labor market is expected to accelerate in the third quarter of 2004.

Figure 4



■ *Real GDP*

After rising by 8.2% during the third quarter of 2003, real GDP grew by 4.1% in the fourth quarter, and averaged a modest 3.1% growth for all of CY 2003.

Real GDP growth in CY 2004 is forecast to be 4.5% before increasing by 4.0% in CY 2005.

Personal consumption advanced 2.2% during CY 2003. As the economy picks up, this rate is estimated to grow by 4.0% in CY 2004. Personal consumption is predicted to increase by 3.9% in CY 2005.

The GDP component showing the most significant improvement in CY 2003 was private investment. After falling 0.2% during CY 2002, gross private domestic investment rose by 0.6% in CY 2003, and is expected to increase by 10.1% in CY 2004 and 7.3% in CY 2005. Much of the expected growth can be attributed to increased expenditures on producers' durable equipment and information processing equipment. Inventory rebuilding is also anticipated.

■ *Light Vehicle Sales*

Rebates and special financing offers that began in the latter half of CY 2001 continued well into CY 2002. Despite incentives, sales of light motor vehicles in CY 2003 totaled 16.7 million units—well below CY 2000's record level of 17.2 million units. *Light vehicle sales* are anticipated to total 16.6 million units in CY 2004 and 16.9 million units in CY 2005.

Over the past several years, there has been a shift in sales away from cars and toward light trucks. This trend is expected to stabilize, and the share of light trucks is expected to remain roughly constant throughout the forecast period. *Light trucks* are expected to account for 55.0% of total sales in both CY 2004 and CY 2005.

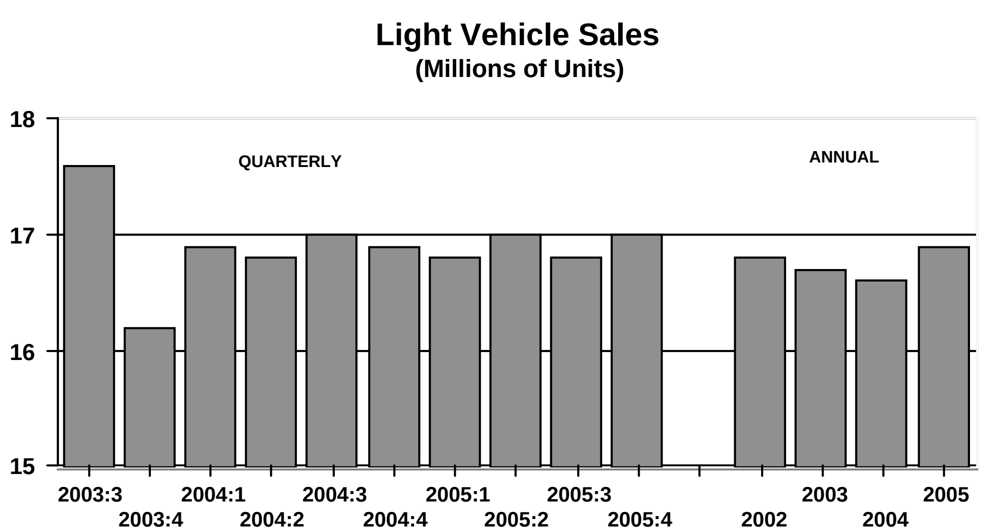
The *import share of total light vehicle sales* rose to 19.9% in CY 2003, and is forecast to increase slightly to 20.0% in CY 2004 and 20.2% in CY 2005.

■ *Inflation: U.S.*

The overall increase in input prices (such as energy prices, wages, and import prices) has generally remained moderate and has helped to hold down production costs. Inflation is expected to remain low, by historical standards, through the forecast period.

Crude oil prices have jumped significantly over the past few months. Benchmark West Texas intermediate crude, which began 2003 near $33 per barrel, spent most of the year hovering at about $30 per barrel. Continued concern over the stability of the oil supply caused oil prices to reach an all-time high of more than $41 per barrel in May 2004.

Figure 5



It is anticipated that oil prices will slowly drop throughout the forecast period, and average about $35 per barrel during CY 2004 and about $30 per barrel in CY 2005.

Annual rates of inflation, as measured by the percentage change in the *U.S. Consumer Price Index-Urban* (CPI-U), are expected to be 2.4% in CY 2004 and 2.2% in CY 2005.

■ ***Inflation: Michigan***

The cost of living in Michigan is measured by the *Detroit Consumer Price Index for Urban Consumers* (Detroit CPI-U). Michigan's average inflation rate was 2.0% in CY 2003. Inflation in Michigan is forecast to increase by 2.3% in CY 2004 and 2.2% in CY 2005.

■ ***Income Growth: U.S.***

Total *U.S. personal income* grew by 3.3% in CY 2003. Personal income growth is forecast to increase by 5.2% in CY 2004 and 6.4% in CY 2005.

Moderate growth in inflation contributed to a 2.6% growth of *U.S. real disposable income* in CY 2003. It is forecast that U.S. real disposable income growth will increase by 3.1% in CY 2004 and 3.6% in CY 2005.

■ ***Income Growth: Michigan***

Michigan's total *state personal income* growth was 2.5% in CY 2003. It is forecast that Michigan personal income will increase by 3.8% in CY 2004 and by 6.0% in CY 2005.

Michigan real disposable income grew 1.8% in CY 2003 after a 1.5% increase posted in CY 2002. In CY 2004, real disposable income is forecast to grow by 1.9% before picking up to 2.7% in CY 2005.

■ ***Employment: U.S.***

One critical factor underscoring the difference in income growth between the U.S. and Michigan is overall job growth. When indexed to the first quarter of 2000, wage and salary employment in the U.S. increased slightly before tapering off in the fourth quarter of 2001. It has remained essentially flat through the last quarter of 2003.

National employment posted an average gain of 217,000 during the first four months of 2004.

Figure 6

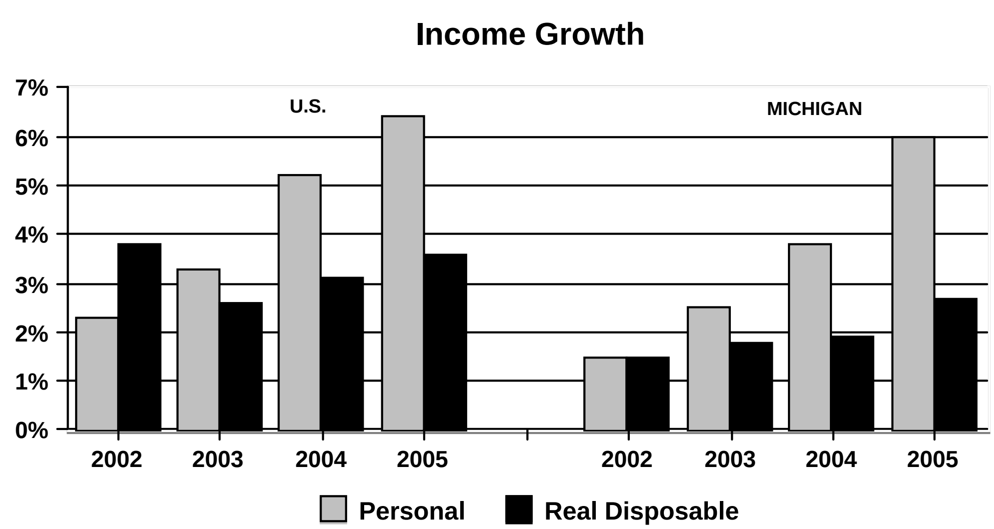
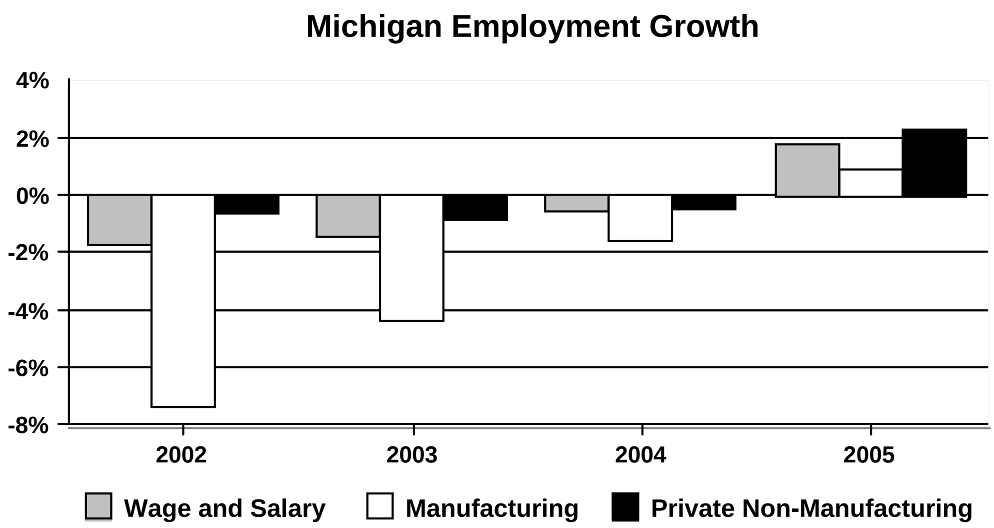


Figure 7



■ ***Employment: Michigan***

The Michigan economy continued to endure a weak labor market throughout CY 2003. Wage and salary employment dropped by 1.4%; private nonmanufacturing employment fell by 0.8% and manufacturing employment declined by 4.3%.

The first quarter of 2004 saw a loss of 29,200 jobs. The forecast calls for employment to begin growing slowly during the second quarter, then accelerating to a quarterly average gain of 21,000. This growth, however, will not be enough to prevent a net loss of jobs for the year as a whole.

Michigan wage and salary employment is forecast to fall by 0.5% in CY 2004 before growing by 1.8% in CY 2005.

Michigan manufacturing employment is forecast to drop by 1.5% in CY 2004 before rebounding 0.9% in CY 2005. Although the most significant declines are concentrated in the motor vehicle industry, employment declines are also spread throughout the manufacturing sector.

Michigan private nonmanufacturing employment is expected to decline by 0.4% in CY 2004 before growing by 2.3% in CY 2005.

■ ***Unemployment: U.S.***

Non-farm payroll employment decreased in both CY 2002 and CY 2003, resulting in an increase in the unemployment rate.

The *U.S. unemployment rate* was 6.0% in CY 2003, and is forecast to decrease to 5.7% in CY 2004 and 5.3% in CY 2005.

■ ***Unemployment: Michigan***

As in the U.S., unemployment in Michigan is a concern as job growth has fallen during the past two years. However, the combination of unemployed workers leaving the labor force and the aforementioned job growth should help to reduce the unemployment rate throughout the forecast period.

Michigan's unemployment rate was 7.3% in CY 2003 and is forecast to drop to 6.9% in CY 2004 before settling back to 6.4% in CY 2005.

Table 4

ECONOMIC FORECAST VARIABLES

	Calendar 2002 Actual	Calendar 2003 Actual	% Change from Prior Year	Calendar 2004 Estimated	% Change from Prior Year	Calendar 2005 Estimated	% Change from Prior Year
United States							
Real Gross Domestic Product (Billions of 2000 dollars)	$10,083.1	$10,398.0	3.1%	$10,868.5	4.5%	$11,305.1	4.0%
Implicit Price Deflator GDP (2000 = 100)	103.9	105.7	1.7%	107.8	2.0%	110.2	2.3%
Consumer Price Index (1982-84 = 100)	179.9	184.0	2.3%	188.4	2.4%	192.5	2.2%
Personal Consumption Deflator (2000 = 100)	103.4	105.3	1.8%	107.6	2.2%	109.8	2.0%
3-month Treasury Bills Interest Rate (Percent)	1.6%	1.0%		1.1%		2.4%	
Aaa Corporate Bonds Interest Rate (Percent)	6.5%	5.7%		5.8%		6.1%	
Unemployment Rate - Civilian (Percent)	5.8%	6.0%		5.7%		5.3%	
Light Vehicle Sales (Millions of units)	16.8	16.7	-0.6%	16.6	-0.6%	16.9	1.9%
Passenger Car Sales (Millions of units)	8.1	7.6	-5.7%	7.5	-1.6%	7.6	1.3%
Light Truck Sales (Millions of units)	8.6	9.0	4.4%	9.1	1.3%	9.3	2.0%
Import Share of Light Vehicles (Percent)	19.7%	19.9%		20.0%		20.2%	
Personal Income (Billions of current dollars)	$8,910.3	$9,203.7	3.3%	$9,684.6	5.2%	$10,302.6	6.4%
Real Disposable Income (Billions of 2000 dollars)	$7,596.8	$7,797.9	2.6%	$8,041.9	3.1%	$8,329.3	3.6%
Michigan							
Wage and Salary Employment (Thousands)	4,477.5	4,415.3	-1.4%	4,394.8	-0.5%	4,472.9	1.8%
Unemployment Rate (Percent)	6.2%	7.3%		6.9%		6.4%	
Personal Income (Millions of current dollars)	$299,449	$306,820	2.5%	$318,542	3.8%	$337,764	6.0%
Real Personal Income (Millions of 1982-84 dollars)	$167,318	$168,121	0.5%	$170,617	1.5%	$176,979	3.7%
Real Disposable Income (Millions of 1982-84 dollars)	$147,512	$150,151	1.8%	$152,974	1.9%	$157,062	2.7%
Wages and Salary Income (Millions of current dollars)	$173,529	$175,779	1.3%	$179,074	1.9%	$187,270	4.6%
Detroit Consumer Price Index (1982-84 = 100)	179.0	182.5	2.0%	186.7	2.3%	190.9	2.2%

RISKS AND UNCERTAINTIES

An economic forecast is based on the best information available at the time the forecast is made. Because information and foresight are not perfect, risks and uncertainties are inherent in any forecast. The key risks in this forecast stem predominantly from uncertainties surrounding the labor market and productivity, inflation, the manufacturing sector, and Michigan's motor vehicle industry.

Labor Market and Productivity

Recovery from the most recent national recession has been characterized by relatively weak economic growth and high productivity gains with ongoing losses in the job market. National employment posted an average gain of 217,000 during the first four months of 2004; this marks the best four-month performance since the beginning of the recovery.

Michigan's wage and salary employment has generally declined since the first quarter of CY 2001—the most recent data indicate a decline of 29,200 in the first quarter of CY 2004. In March, the state's wage and salary employment grew by 6,000—which was weak, but broad-based growth.

Productivity increased 2.4% on average between 1996 and 2001. After increasing at 4.9% in CY 2002 and 4.4% in CY 2003, output per hour is estimated to increase 3.7% in 2004 and 2.4% in 2005. Businesses will continue to push for productivity increases, but increased hiring is expected to take over as the main factor in producing more output.

This forecast assumes that the national labor market will continue to improve while the Michigan labor market will post modest employment gains beginning in the second quarter of 2004. If the labor market does not turn around as estimated, both the national economy and Michigan's economy could grow more slowly than anticipated and revenue growth would be adversely affected.

Prices

Another forecast risk is the prospect of unanticipated price increases. If consumer and/or producer prices were to experience unexpected increases, this could, potentially, put a damper on an economic recovery.

Over the past three years, producer prices have increased at an average annual rate of just 1.3%; consumer prices have increased at an average rate of 2.2% per year. Although both producer and consumer prices are expected to increase over the forecast period, the increases should be modest.

Anything that disrupts consumer confidence, for example, an increase in energy prices or healthcare costs, could cause consumers to become more cautious and reduce consumption.

If energy prices were to increase, producer prices could also be affected, given that higher energy prices impact almost all sectors of the economy.

Producer prices are also highly dependant on labor costs. Over the past three years, productivity increases and a soft labor market have helped to contain wage and salary increases. As firms begin to expand and increase output, the demand for additional labor also increases, which drives up wages and producer prices.

Unexpected increases in prices could also result in Federal Reserve intervention. The forecast assumes that the FED will increase the discount rate by 0.75% (25 basis points in June, November, and December) in CY 2004 and by an additional 1.5% in CY 2005. Should prices jump unexpectedly, the FED might further increase key interest rates in an attempt to constrain inflation, which could inhibit consumer spending by making credit more expensive.

Manufacturing Sector

The manufacturing sector has improved over the last several months at the national level and in the Midwest.

Exports affect the manufacturing sector, and the value of the dollar relative to other currencies affects the competitiveness of U.S. manufacturers in the world market. This forecast assumes that as the economy improves and the value of the dollar declines, the manufacturing sector at both the national and state level will improve.

Michigan manufacturing employment is forecast to decline in CY 2004 and improve somewhat in CY 2005. If the manufacturing sector improves sooner than forecast, Michigan's employment and revenue will be higher than estimated.

Michigan's Motor Vehicle Industry

A significant component of Michigan's economy is the level and composition of light motor vehicle sales. Light vehicle sales were 16.7 million units in CY 2003 and are forecast to be 16.6 million in CY 2004 and16.9 million in CY 2005.

The import share of light vehicles was 20% in CY 2003 and is forecast to remain close to 20% in CY 2004 and in CY 2005. The value of the dollar relative to other currencies is expected to continue to decline, which will make import vehicles less attractive.

Although a higher level of domestically-produced motor vehicle sales would generally be considered positive for Michigan, the benefit to Michigan may be muted. As reported by the *Detroit News*, the 2003 market share of the big three auto manufacturers—General Motors, Ford, and DiamlerChrysler—declined to an all-time low 60.3%. In addition, Michigan motor vehicle production declined 3.7% in FY 2002-03.

Transplants (vehicles with a foreign nameplate that are made in the U.S.) have steadily gained in market share over the past several years. These transplants are expected to increase production capacity in the next few years, while the big three are expected to reduce capacity.

If the Michigan-produced market share of motor vehicles is less than anticipated, then Michigan's economy and revenue growth would be lower than estimated.

In addition to the above-mentioned risks, the U.S. economy could be negatively affected by external factors completely beyond the ability of forecasters to predict—such as terrorism or the impact of additional corporate scandals on the equity markets.

GF/GP AND SAF REVENUES

Revenue estimates are based on the economic performance of key components of national and state economies discussed in the preceding section. This section explains May 2004 House Fiscal Agency revenue estimates for GF/GP and School Aid Fund (SAF) revenue by major revenue sources. It provides revenue estimates, year-end balances for the major funds and the budget stabilization fund, and the state revenue limit calculation.

GF/GP Revenue by Source

■ GF/GP Baseline Tax Revenues

Baseline GF/GP tax revenues totaled $7,652.1 million in FY 2002-03; they are estimated to increase $237.0 million or 3.1% to $7,889.1 million in FY 2003-04, and increase $371.4 million or 4.7% to $8,260.5 million in FY 2004-05.

■ Total GF/GP Baseline Revenues

Total baseline GF/GP revenues include baseline tax revenues and non-tax revenues. *Total GF/GP baseline revenues* were $7,944.8 million in FY 2002-03; they are estimated to increase 2.3% to $8,129.9 million in FY 2003-04, and increase 3.9% or $319.4 million to $8,449.3 million in FY 2004-05.

■ Actual GF/GP Revenues

Actual GF/GP revenues take tax changes into account and are available for expenditure each year. Final *actual GF/GP revenues* were $7,958.9 million in FY 2002-03; they are forecast to decline 0.5% or $43.7 million to $7,915.2 million in FY 2003-04, and decrease 0.3% or $24.7 million to $7,890.5 million in FY 2004-05.

SAF Revenue by Source

■ Total SAF Baseline Revenues

Total *SAF baseline revenues* were $10,255.7 million in FY 2002-03; they are forecast to increase $227.6 million or 2.2% to $10,483.3 million in FY 2003-04, and $413.1 million or 3.9% to $10,896.4 million in FY 2004-05.

■ Actual SAF Revenues

Actual SAF revenues take tax changes into account. *Actual SAF revenues* totaled $10,714.8 million in FY 2002-03; they are forecast to decrease $142.7 million or 1.3% to $10,572.2 million in FY 2003-04 and increase $404.7 million or 3.8% to $10,976.9 million in FY 2004-05.

Table 5

GF/GP REVENUE ESTIMATES (Millions of Dollars)

	Final FY 2002-03	FY 2003-04	FY 2004-05	Fiscal Year 2004-05 over 2003-04 %Change	$Change
Personal Income Taxes	$3,955.8	$4,067.1	$4,288.0	5.4%	$220.9
Sales and Use Taxes	883.3	963.7	1,006.0	4.4%	42.2
SBT and Insurance Taxes	2,114.0	2,150.8	2,257.0	4.9%	106.2
Other Taxes	699.0	707.5	709.6	0.3%	2.1
GF/GP Baseline Tax Revenues	**$7,652.1**	**$7,889.1**	**$8,260.5**	**4.7%**	**$371.4**
Non-Tax Revenue	292.7	240.8	188.8	-21.6%	(52.0)
Total GF/GP Baseline Revenues	**$7,944.8**	**$8,129.9**	**$8,449.3**	**3.9%**	**$319.4**
Adjustments to Baseline	14.1	(214.7)	(558.8)	**160.3%**	**($344.1)**
Actual GF/GP Revenues	**$7,958.9**	**$7,915.2**	**$7,890.5**	**-0.3%**	**($24.7)**

NOTE: Numbers may not add due to rounding.

Table 6

SCHOOL AID FUND REVENUE ESTIMATES
(Millions of Dollars)

	Final FY 2002-03	FY 2003-04	FY 2004-05	Fiscal Year 2004-05 over 2003-04 % Change	$ Change
Sales and Use Tax	$5,091.6	$5,181.5	$5,400.1	4.2%	218.7
Income Tax Earmark	1,847.0	1,913.8	2,005.3	4.8%	91.5
State Education Tax	1,673.2	1,710.8	1,820.5	6.4%	109.7
Lottery and Casino Wagering	676.9	684.5	687.3	0.4%	2.8
Tobacco Taxes	489.1	479.6	472.7	-1.4%	(6.9)
Real Estate Transfer Tax	275.5	305.0	297.0	-2.6%	(8.0)
Other Taxes	202.4	208.1	213.4	2.5%	5.3
Baseline SAF Revenues	**$10,255.7**	**$10,483.3**	**$10,896.4**	**3.9%**	**$413.1**
Adjustments to Baseline	459.2	88.9	80.5	-9.4%	($8.4)
Actual SAF Revenues	**$10,714.8**	**$10,572.2**	**$10,976.9**	**3.8%**	**$404.7**

NOTE: Numbers may not add due to rounding.

Table 7

YEAR-END BALANCE ESTIMATES
(Millions of Dollars)

	Final FY 2001-02	Final FY 2002-03	Estimated FY 2003-04
General Fund/General Purpose	$114.5	$174.0	$0.0
School Aid Fund	$237.0	$113.7	$0.0
Budget Stabilization Fund	$145.2	$0.0	$0.0

HFA Estimates of Year-End Balances

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

Fiscal Year 2003-04 estimates are based on year-to-date appropriations and HFA revenue estimates. Final FY 2001-02 and FY 2002-03 figures are included.

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

School Aid Fund revenues are restricted; hence, any year-end balance is carried forward to the subsequent year.

BSF Year-End Balances

The Counter-Cyclical Budget and Economic Stabilization Fund (BSF), or the state's rainy day fund, is a reserve of cash to contribute to or withdraw from throughout the economic cycles. **Table 8** shows deposits, withdrawals, interest earnings, and the year-end balance from FY 1989-90 through FY 2002-2003. It also includes HFA estimates for FY 2003-04 and FY 2004-05. **Figure 8** depicts the BSF fund balance and fund balance as a percent of total GF/GP and SAF revenues from FY 1990-91 through FY 2004-05.

- ***FY 2002-03***

The BSF balance was eliminated at the end of FY 2002-03. Withdrawals consisted of the following: $32.0 million to the SAF for the Durant settlement and $124.1 million to GF/GP.

- ***FY 2003-04 and FY 2004-05***

The BSF trigger calculation, which is based on Michigan personal income less transfer payments adjusted for inflation, indicates no pay-in or withdrawal for FY 2003-04 or FY 2004-05. In addition, under the Tobacco Products Tax Act, 17.808% of the cigarette tax and 18.4% of the other tobacco products tax is earmarked to the BSF for FY 2004-05 through FY 2006-07. This pay-in is estimated at $154.0 million in FY 2004-05.

Figure 8

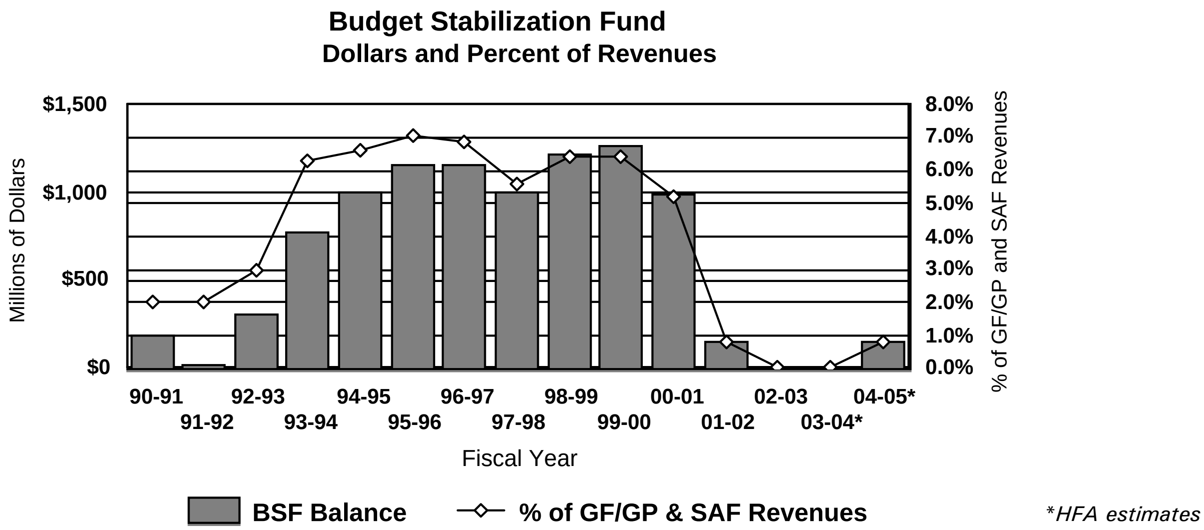


Table 8

BUDGET STABILIZATION FUND HISTORY
(Millions of Dollars)

Fiscal Year	Deposits	Withdrawals	Interest Earned	Balance
1989-90	$0.0	$69.9	$35.8	$385.1
1990-91	0.0	230.0	27.1	182.2
1991-92	0.0	170.1	8.1	20.1
1992-93	282.6	0.0	0.7	303.4
1993-94	460.2	0.0	11.9	775.5
1994-95	260.1	90.4	57.7	1,003.0
1995-96	91.3	0.0	59.2	1,153.6
1996-97	0.0	69.0	67.8	1,152.4
1997-98	0.0	212.0	60.1	1,000.5
1998-99	244.4	73.7	51.2	1,222.5
1999-2000	100.0	132.0	73.9	1,264.4
2000-01	0.0	337.0	66.7	994.2
2001-02	0.0	869.8	20.8	145.2
2002-03	0.0	156.1	10.9	0.0
2003-04*	0.0	0.0	0.0	0.0
2004-05*	154.0	0.0	0.0	154.0

** HFA Estimates*

NOTE: Numbers may not add due to rounding

Compliance with the State Revenue Limit

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

The revenue to be considered in the revenue limit includes not only state taxes, but also fees, licenses, and interest earned. Federal aid is not included in the revenue limit calculation.

Implications of Exceeding the State Revenue Limit

Article IX, Section 26, *Constitution of the State of Michigan*, provides that:

> . . . For any fiscal year in the event that Total State Revenues exceed the limit established in this section by 1% or more, the excess revenues shall be refunded pro rata based on the liability reported on the Michigan income tax and single business tax (or its successor tax or taxes) annual returns filed following the close of such fiscal year. If the excess is less than 1%, this excess may be transferred to the State Budget Stabilization Fund . . . .

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

The final FY 2001-02 revenue limit calculation indicated that state revenue collections were $3.92 billion below the revenue limit. In addition, for FY 2002-03 through FY 2004-05, state revenues are estimated to be substantially below the revenue limit, by $4.43 billion, $5.08 billion, and $5.00 billion respectively.

Table 9

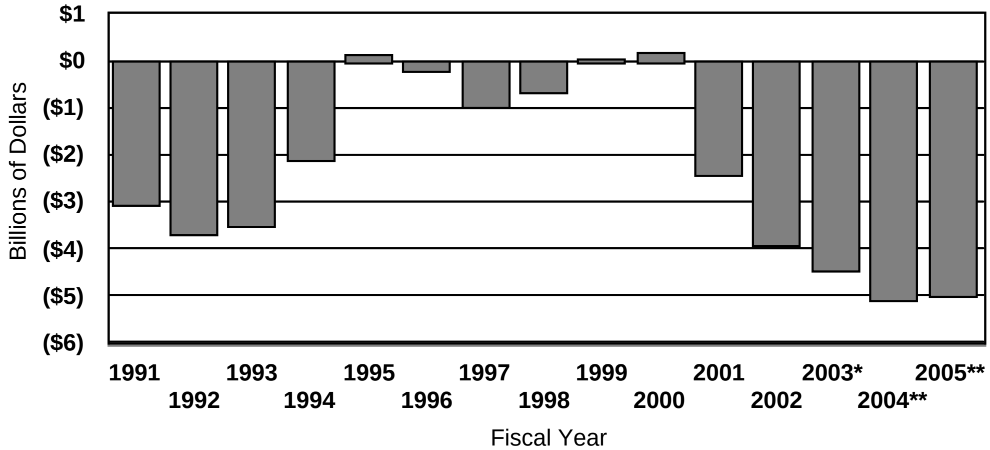
COMPLIANCE WITH THE STATE REVENUE LIMIT
(Millions of Dollars)

Revenue Limit Calculations	Final FY 2001-02	Preliminary Final FY 2002-03	FY 2003-04	FY 2004-05
Personal Income				
Calendar Year	CY 2000	CY 2001	CY 2002	CY 2003
Amount	$289,390	$297,609	$303,745	$306,820
X Limit Ratio	9.49%	9.49%	9.49%	9.49%
State Revenue Limit	**$27,463.1**	**$28,243.1**	**$28,825.4**	**$29,117.2**
Total Revenues Subject to Revenue Limit	23,546.0	23,808.2	23,743.2	24,131.8
Amount (Under) Over State Revenue Limit	**($3,917.1)**	**($4,434.9)**	**($5,082.2)**	**($4,985.4)**

NOTE: Numbers may not add due to rounding.

Figure 9

Constitutional Revenue Limit
Amount Under or Over Limit



Preliminary Final
** *HFA Estimate*

Table 10

CONSTITUTIONAL REVENUE LIMIT HISTORY
(Billions of Dollars)

Fiscal Year	(Under) or Over Limit	Fiscal Year	(Under) or Over Limit
1979-80	($0.53)	1992-93	($3.48)
1980-81	($1.17)	1993-94	($2.11)
1981-82	($1.41)	1994-95	$0.11
1982-83	($1.32)	1995-96	($0.18)
1983-84	($0.24)	1996-97	($0.98)
1984-85	($0.01)	1997-98	($0.64)
1985-86	($0.37)	1998-99	$0.02
1986-87	($0.84)	1999-2000	$0.16
1987-88	($1.35)	2000-01	($2.41)
1988-89	($1.03)	2001-02	($3.92)
1989-90	($1.76)	*2002-03	($4.43)
1990-91	($3.04)	**2003-04	($5.08)
1991-92	($3.69)	**2004-05	($5.00)

* *Preliminary Final*
***HFA Estimate*

Additional copies of this report are available at www.house.mi.gov/hfa

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