

Massachusetts Economic and Fiscal Outlook FY 2020-2021

Senate Committee on Ways and Means

Sen. Michael J. Rodrigues, Chair

Agenda

- Economic Variables
 - Unemployment
 - Gross Domestic Product
 - Shape of the Recovery
 - Role of the Federal Government
- FY 2020 Tax Revenue Forecasts
- FY 2021 Tax Revenue Forecasts
- Historical Context
- Strengths and Weaknesses of Massachusetts

Virtual Economic Roundtable

- On Tuesday, April 14th, the Chairs of the Joint Committee on Ways and Means and the Secretary of Administration and Finance hosted a number of economists, academics and think tanks to provide their perspectives on the economic and fiscal impacts of the COVID-19 pandemic on Massachusetts.
- Our guests included:
 - Treasurer Deborah Goldberg
 - Eileen McAnneny, Massachusetts Taxpayers Foundation
 - David Tuerck and William Burke, Beacon Hill Institute
 - Marie-Frances Rivera, Massachusetts Budget and Policy Center
 - Evan Horowitz, Center for State Policy Analysis at Tufts University
 - Michael Goodman, University of Massachusetts Dartmouth
 - Alan Clayton-Matthews, Northeastern University
 - Beth Ann Bovino, S&P Global
 - Nick White, Moody's Analytics

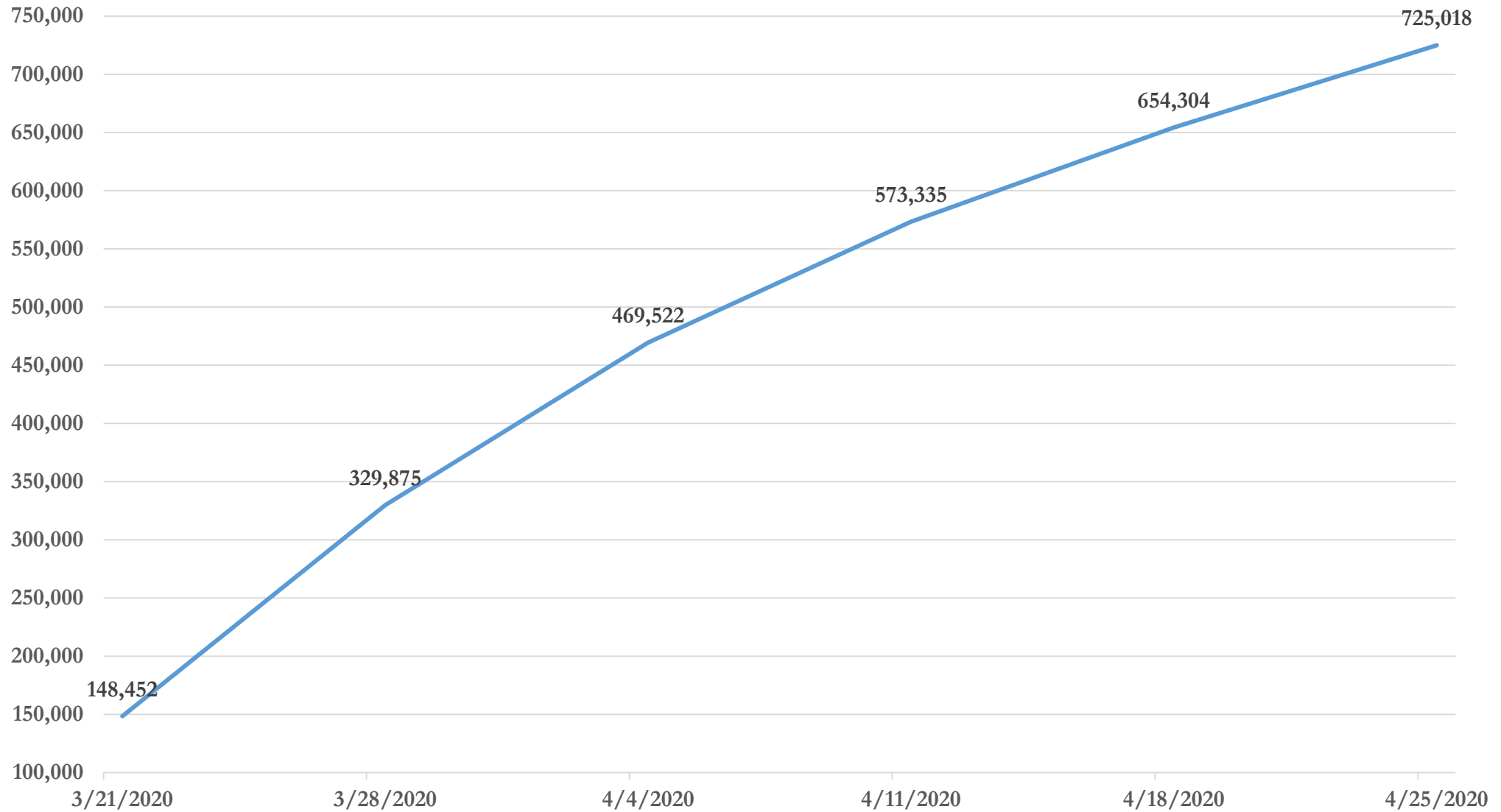
Economic Variables

- Before diving into our experts' tax revenue forecasts, it is important to look at some of the economic variables we are monitoring throughout the pandemic.
- The items listed below touch on some of the issue areas discussed during the roundtable:
 - Unemployment
 - Gross Domestic Product
 - Shape of the Recovery
 - Role of the Federal Government

Unemployment

- Between March 15th and April 25th, U.S. unemployment claims skyrocketed to over **30M**.
- In Massachusetts, the same six-week period saw more than **720K** initial unemployment claims filed.
- This data does not include previously ineligible workers, such as contractors and self-employed individuals – which is estimated to add another **172K** workers to the unemployment insurance system.
- Several of our roundtable experts projected highs in unemployment of between **15-18%** - however, our estimated claims from last week's data suggest somewhere between **24-26%** of the workforce is unemployed or furloughed during the peak of the public health crisis.

Bureau of Labor Statistics: MA Cumulative Unemployment Claims (Weeks of 03/21-04/18)



Gross Domestic Product: Quarter 1 2020

- According to estimates released by the U.S. Bureau of Economic Analysis, U.S. real GDP for the first quarter of 2020 contracted at a **4.8% annualized rate** – the worst contraction for the U.S. since the 2008 financial crisis.
 - The economic indicators used to estimate growth for the quarter primarily occurred **before** the non-essential business closures, massive layoffs and furloughs, and stay-at-home advisories.
 - In fact, Goldman Sachs believes the true U.S. decline for the quarter to be **closer to 8.25%**.
- MassBenchmarks estimates that Massachusetts real GDP declined by **6.1%** over the same period.

Gross Domestic Product: Remainder of 2020

- Our experts cited that, while Q1 2020 will be bad, some of the larger financial institutions predict that **Q2 2020 will be dramatically devastating for the United States and lead to historic losses in GDP for the year:**

Financial Institution	2020 Quarter 2 Est. Change	2020 Annual Est. Change
Bank of America	-30%	-10.4%
Goldman Sachs	-34%	-6.2%
Morgan Stanley	-38%	-5.5%

- These estimated annual declines would all represent **the worst annual contraction since 1946.**
- Based on current unemployment levels, Prof. Clayton-Matthews believes “the actual decline in Massachusetts gross domestic product in the second quarter is expected to be on the order of **25-50%** on an annualized basis.”

Shape of the Recovery

- As Dr. Anthony Fauci has said, **“you don’t make the timeline, the virus makes the timeline.”**
- This point was emphasized by our experts in terms of the timeline for an economic recovery.
- Modeling has become extremely challenging due to unknown variables like the peak of the virus, consumer confidence, and the odds of reoccurring infections.
- Our experts articulated that the shape of this economic recovery is particularly bound to the cause of our recession – the virus.

Shape	Characteristics
V	<ul style="list-style-type: none"> •Most optimistic recovery model; •Starts with sharp decline in GDP and spike in unemployment; •COVID-19 peak occurs in April/May and the recovery begins in the summer; •Federal programs to help businesses avoid layoffs are successful, helping production, manufacturing and services to start up immediately; •Pent up demand brings economic output back to pre-COVID-19 levels by end of 2020.
U	<ul style="list-style-type: none"> •More elongated recovery model; •Starts with sharp decline in GDP and spike in unemployment; •COVID-19 peak extends into the summer with stabilization/recovery in the second half of 2020; •Consumers are not totally confident, despite pent up demand; •Businesses and factories do not immediately return to full capacity and not every job lost due to the crisis is won back; •Recovery would occur more gradually between late 2020 and early 2021.
W	<ul style="list-style-type: none"> •Up and down recovery model; •Starts with sharp decline in GDP and spike in unemployment; •COVID-19 peak appears to be controlled, leading to loosening of stay-at-home advisories, business shutdowns and economic growth; •COVID-19 infections reemerge, leading to a second wave of stay-at-home advisories, business shutdowns and economic contraction; •Cycle continues until there is a widely available vaccine or other medical means of reducing the severity and spread of the virus.
L	<ul style="list-style-type: none"> •Sharp decline in GDP and spike in unemployment persists due to continued threat of COVID-19 into second half of 2020; •Extension of stay-at-home advisories and business closures disallows recovery; •Consumers demonstrate little confidence and largely limit spending; •Debts built before or during the crisis become more difficult to pay off, causing defaults and business bankruptcies.
✓	<ul style="list-style-type: none"> •Recovery model characterized by slow and steady recovery through 2021; •Starts with sharp decline in GDP and spike in unemployment; •Loosening of stay-at-home advisories and business closures is done slowly, gradually and methodically; •Consumers remain cautious, causing gradual return to pre-crisis economic levels.

Role of the Federal Government

- The federal government has provided more than **\$2.6 trillion** in multiple economic and public health assistance bills.
- The series of bills – the largest being the **\$2 trillion** CARES Act – projects to provide Massachusetts with over **\$5.7B** for COVID-19 supports, including:
 - **\$2.67B** from the Coronavirus Relief Fund
 - **\$1.2B** from the Federal Transit Administration
 - **\$546M** from the Department of Education
- Also, MA is one of only 9 states receiving more than **\$10B** from the Small Business Administration's Payroll Protection Program.
- Additionally, the Federal Reserve has been and must continue to be active in order to assist with the recovery.
 - To date, it has made up to **\$2.3B** available in relief loans for businesses and state and local governments.
 - It also lowered its **target interest rate to a range of 0 to 0.25%** at the start of March to promote borrowing.

Challenges:

- In many ways, the current federal assistance bills are restrictive on allowable spending, particularly **disallowing funds from being used to backfill revenue losses**. Federal funds during the Great Recession were much more flexible.
 - As an example, we were able to use enhanced Federal Medical Assistance Percentages (FMAP) funds to backfill revenue losses.
 - The CARES Act explicitly prohibits states from using the Coronavirus Relief Fund for the state share of Medicaid – thus removing a valuable tool.

FY 2020 Tax Revenue Impact: Current Performance

Tax Type	Total April Collections	\$ Comp. to April Benchmark	Year-to-Date Collections	\$ Comp. to YTD Benchmark
Income	\$1,122	-\$1,895	\$12,609	-\$1,944
Income Withholding	\$1,053	-\$34	\$11,521	\$2
Income Non-Withholding	\$69	-\$1,860	\$1,088	-\$1,946
Sales & Use	\$469	-\$139	\$5,791	-\$174
Corporate & Business	\$209	-\$111	\$2,434	\$101
Other	\$181	-\$23	\$2,212	\$85
Total	\$1,981	-\$2,168	\$23,045	-\$1,932

FY 2020 Tax Revenue Forecasts

- The majority of our experts refrained from providing FY 2020 tax revenue forecasts due to the extreme uncertainty of COVID-19.
- A 2% revenue loss from benchmark between March and June is much more significant, as the state does not have as many tools at its disposal to close a budget gap as it would at the start of the year.

Expert	FY20 Est.	\$ Diff. from Bench.	% Diff. from Bench.
FY 2020 Benchmark: \$30,288.00			
Center for State Policy Analysis at Tufts (average)	\$29,663.00	-\$625.00	-2.1%
Alan Clayton-Matthews	\$29,692.00	-\$596.00	-2.0%
Average	\$29,677.50	-\$610.50	-2.0%

FY 2021 Tax Revenue Forecasts

- Some of the biggest challenges in forecasting the upcoming fiscal year is once again the uncertainty of the timing and reemergence of the virus' peak, consumer confidence, as well as the impacts of federal stimulus bills.
- It is worth keeping in mind that these estimates were provided in mid-April. Given the continued shutdown and spread of the virus, more pessimistic economic outlooks are most certainly likely.

Expert	FY21 Est.	\$ Diff. from CR	% Diff. from CR
FY 2021 Consensus Revenue Agreement: \$31,151.00			
MassBudget (average)	\$25,801.00	-\$5,350.00	-17.2%
Alan Clayton-Matthews	\$26,112.00	-\$5,039.00	-16.2%
Mass. Taxpayers	\$26,756.00	-\$4,395.00	-14.1%
Center for State Policy Analysis at Tufts	\$28,970.00	-\$2,181.00	-7.0%

Historical Context

- To put these estimated revenue losses into perspective, consider the tax revenue declines experienced during the first two fiscal years of the Great Recession:
 - Over the course of FY 2009 and 2010, the Commonwealth saw an aggregated tax revenue decrease of **\$4.14B** compared to the two respective consensus revenue agreements.
 - Based on our experts' testimony, FY 2021 tax revenues will likely eclipse those aggregated losses in one year.

FY	CR Agreement	Actual Collections/ Projected Estimate	Difference	% Change
2009	\$21.23	\$18.26	-\$2.97	-14.0%
2010	\$19.71	\$18.54	-\$1.17	-5.9%
Total Difference			-\$4.14	-10.1%
2021	\$31.15	\$26.43	-\$4.72	-15.1%

*FY 2021 projected estimate is based on the average updated forecasts from annual consensus revenue hearing participants.

Historical Context

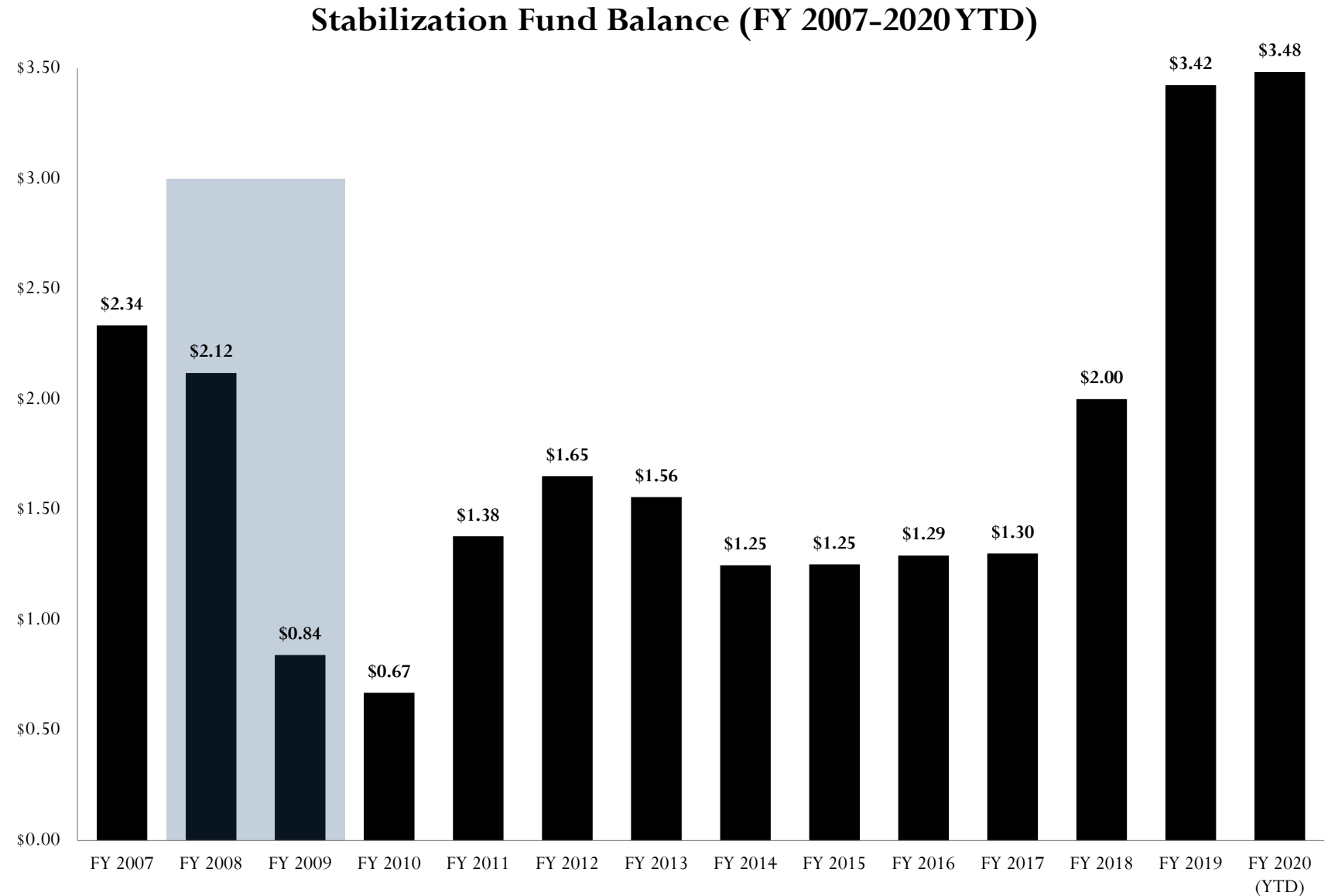
- The Great Recession, while different in terms of the root cause of the economic downturn, can provide us with some important context relative to the challenging budget decisions ahead of us.
- Over the course of FY09-10, some of the difficult cuts and policy solutions made by the Legislature and Governor included:
 - **\$378M (28.8%)** for UGGA;
 - **\$195M (29.7%)** for institutions of higher education;
 - **\$96.9M (42.1%)** for Special Education Circuit Breaker;
 - **\$20.8M (30.5%)** for Regional School Transportation;
 - **\$18.5M (31.7%)** for Regional Transit Authorities;
 - **\$20.5M (10%)** for energy and environment programs;
 - **\$48.4M (8%)** for the Trial Court;
 - Increasing the sales and use tax from **5%** to **6.25%**;
 - Increasing state employees' health insurance premium contributions by 5% with the highest contributions rising from **20%** to **25%**;
 - Extending the state pension schedule by two years;
 - Layoffs of more than 1,600 state employees and furloughs across state government.

Strengths and Weaknesses of Massachusetts

- Moody's Analytics has run state "stress test" models and indicates that Massachusetts has typically performed well in tougher economies due to robust healthcare and education industries – given historical data, their model still suggests that we will be buoyed by those sectors.
- Professor Goodman agrees, saying that **"even through some of the worst economic experiences that we've had, our health care institutions have grown and added jobs. Similarly, higher education has had its challenges during downturns, but both have been stalwart counter-cyclical employment stabilizers."**
 - However, Professor Goodman notes that, given the public health crisis, hospital systems have been forced to cancel elective procedures, forgoing billions of dollars.
 - Similarly, institutions of higher education are in a state of complete unknowing in terms of enrollment, revenue streams and simply the ability to house students on campus in the fall.
- All of these points return to the fact that this pandemic is unlike anything we have ever seen in terms of the public health implication, as well as the economic ramifications.

Strengths of Massachusetts

- **Stabilization Fund:** since FY 2017, we have added **\$2.18B** to our reserves.
- While this seems substantial, keep in mind that between FY 2007-2010 we drew down the fund from **\$2.34B to \$670M**.
- **Tax Structure:** Moody's notes that MA has a stable tax revenue base compared to other states, and has done a fair job de-risking our budgeted tax revenue sources by not overly relying on volatile collections like capital gains.



Weaknesses of Massachusetts

- Massachusetts has been one of the most severely impacted states by COVID-19. Based on the magnitude of the public health crisis here, it is fair to assume that we will lag behind the nation in terms of our economic recovery.
- Moody's Analytics lists **Massachusetts as one of the most vulnerable states**, based on some of the following demographic features:
 - **Exposure to the virus** – calculated by the number of infections, as well as the level of international travel
 - **Demographics** – based on population density, portion of population ages 65 and older, and levels of migration
 - **Global interconnectedness** – number of airline passengers and percent of export trade
 - **Finance** – reliance on securities industry, as well as investment income share
 - **Tourism** – levels of employment in accommodations
- **Bottom line:** the public health aspect of this recession potentially positions Massachusetts in a worse position than historic recessions, meaning the playbook on how to counter this economic downturn will likely need to be revamped.

Questions?