Looking Back, Looking Forward: Budget Lessons from Midwest States

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Evidence-Based Budgeting: Making Decisions to Move Wisconsin Forward
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Outline

- Relationship between economic and fiscal health
- What happened during the last decade?
- What can we expect over the next decade?
- Long run strategies for effective fiscal management
- Budgeting in periods of fiscal stress
- Special considerations for Midwestern states

Relationship between economic and fiscal health

- Recessions and fiscal health
  - State revenue falls when unemployment rises
    - Severe drop in both 2001 and 2007 recessions (policy change also played a part).
    - After 2001 recession revenues rose very slowly.
    - Too early to tell in 2007-09 recession but slow increase in revenues.
  - Demand for state spending rises in recessions
    - Medicaid enrollments typically rise with a lag after the recession ends.
    - In three past recession (1980-82, 1990-91 and 2001) state education expenditures also rose rapidly.
    - Too early to tell in 2007-09 recession but large increase in Medicaid rolls.
- Long-term economic growth and fiscal health
    - A high standard of living and fiscal balance can be maintained without rapid population growth.

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What happened during the last decade (through 2008)?

- Nationally state revenues and expenditures have risen faster than inflation.
- Wisconsin revenues, taxes and expenditures have risen slower than the national average.
- Wisconsin has lagged behind other states in getting federal revenues.
- Wisconsin had less increase in Medicaid costs than other states.

Figure 1: State Total General Revenue

Real 2005 dollars per capita

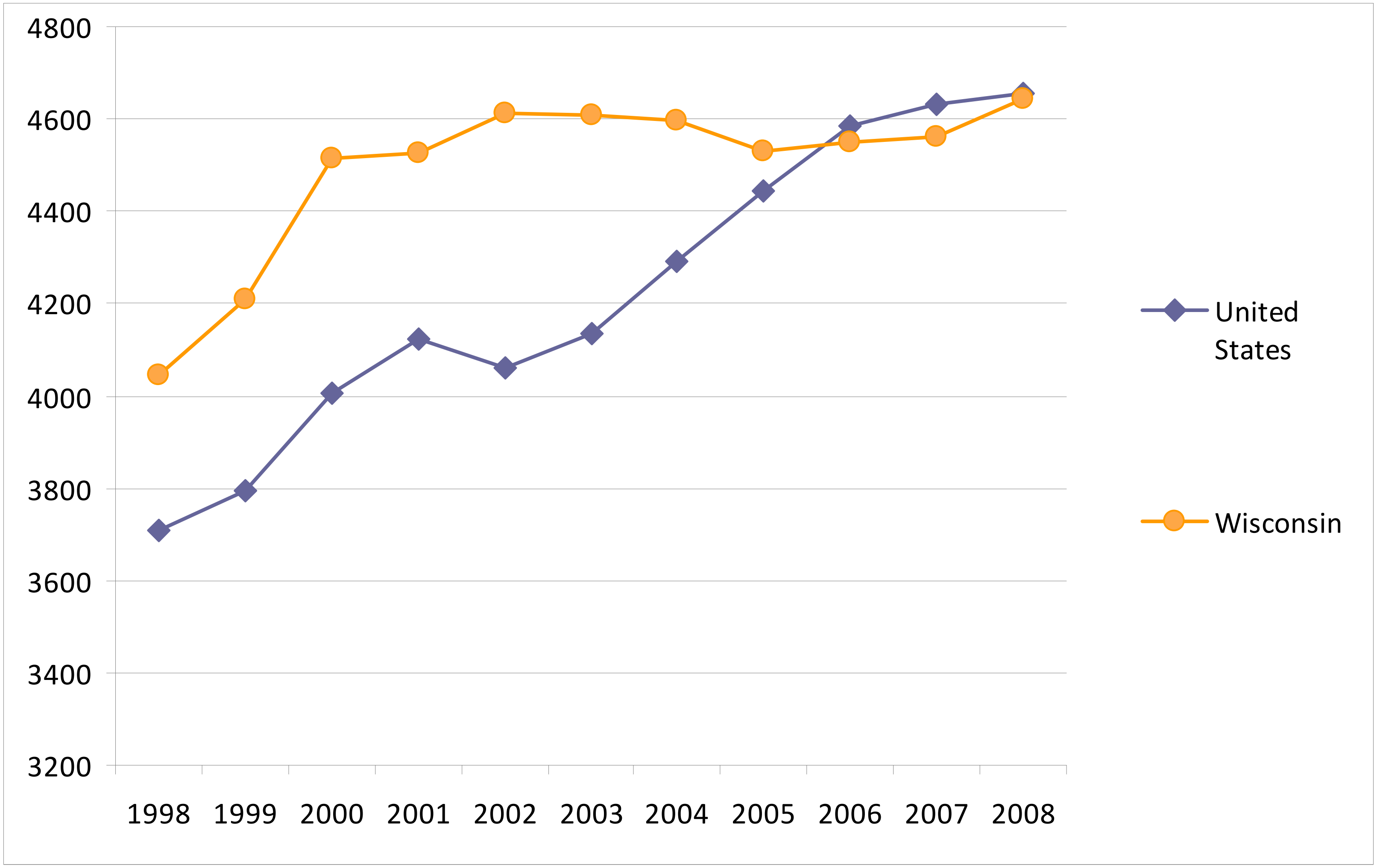


Figure 2: State Total Tax Revenue

Real 2005 dollars per capita

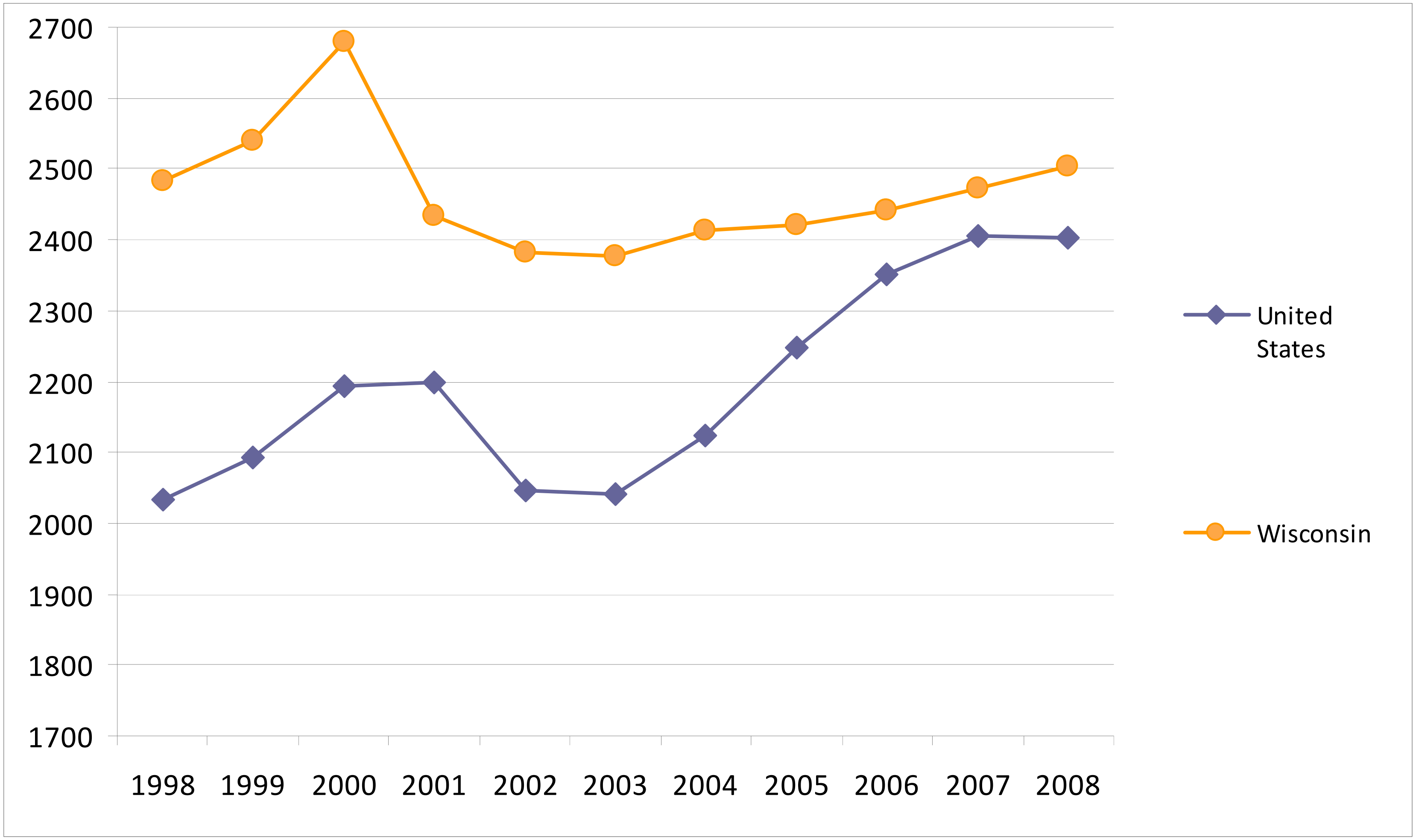


Figure 3: Intergovernmental Revenue from Federal Sources

Real 2005 dollars per capita

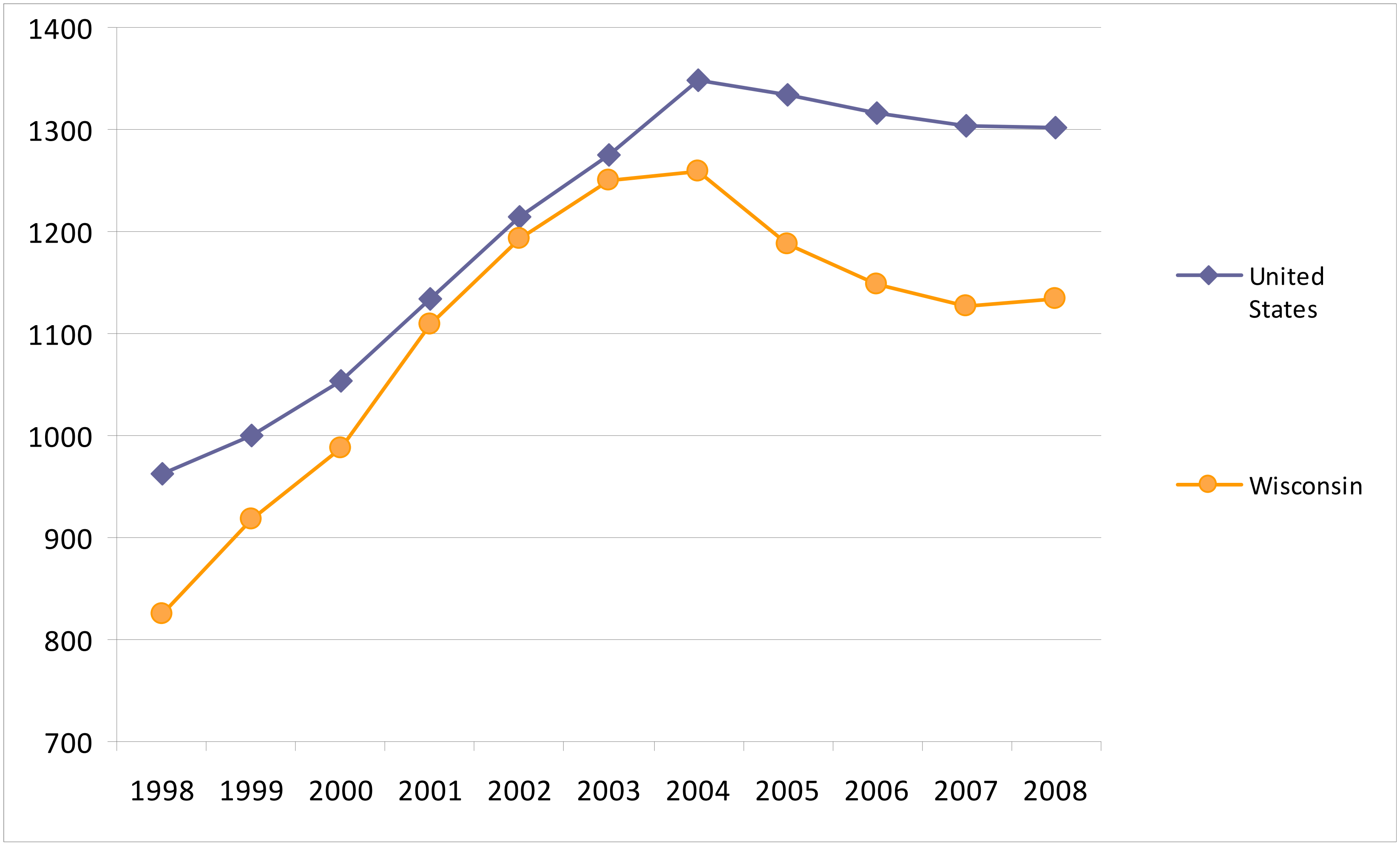


Figure 4: Total General Expenditure

Real 2005 dollars per capita

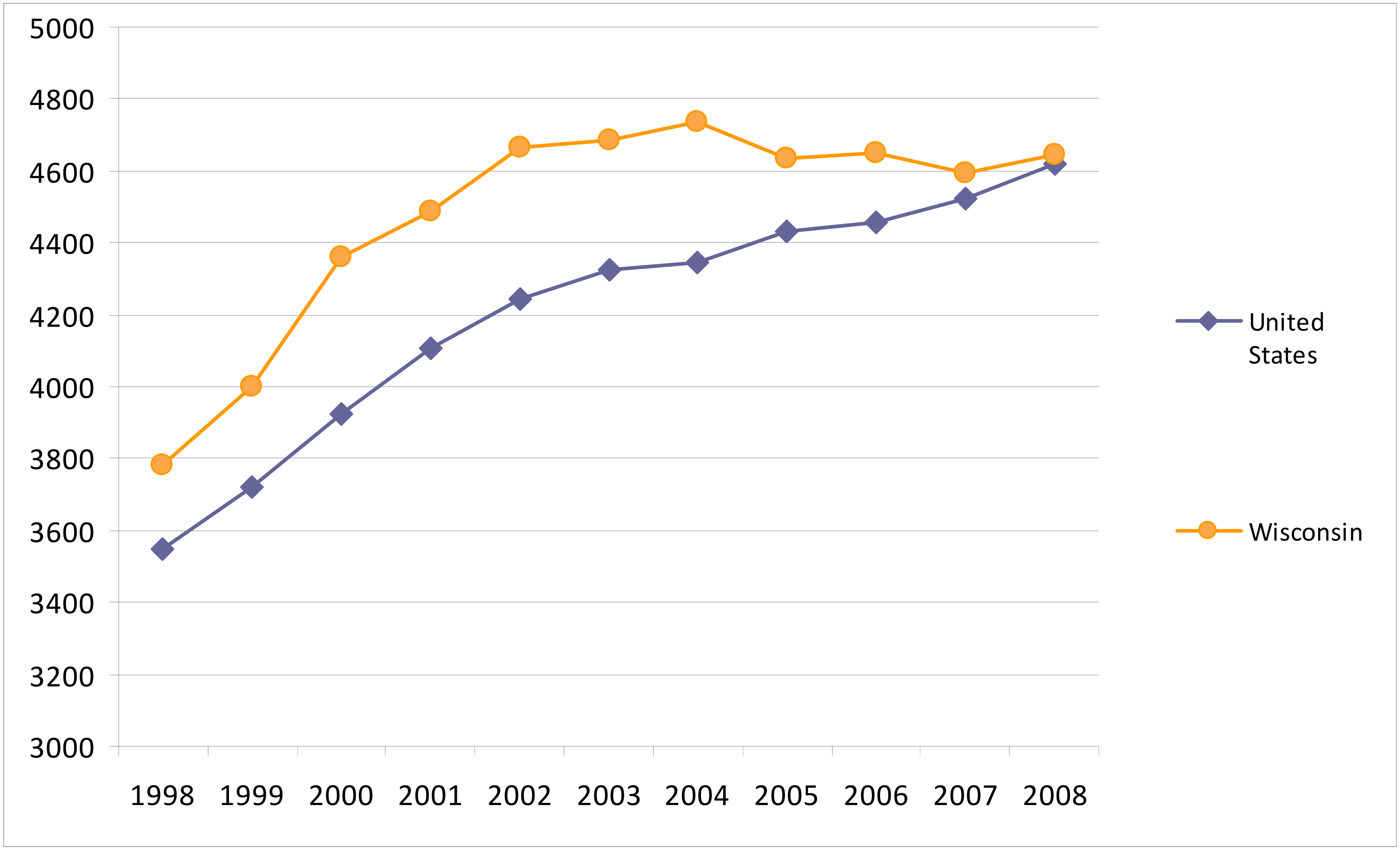
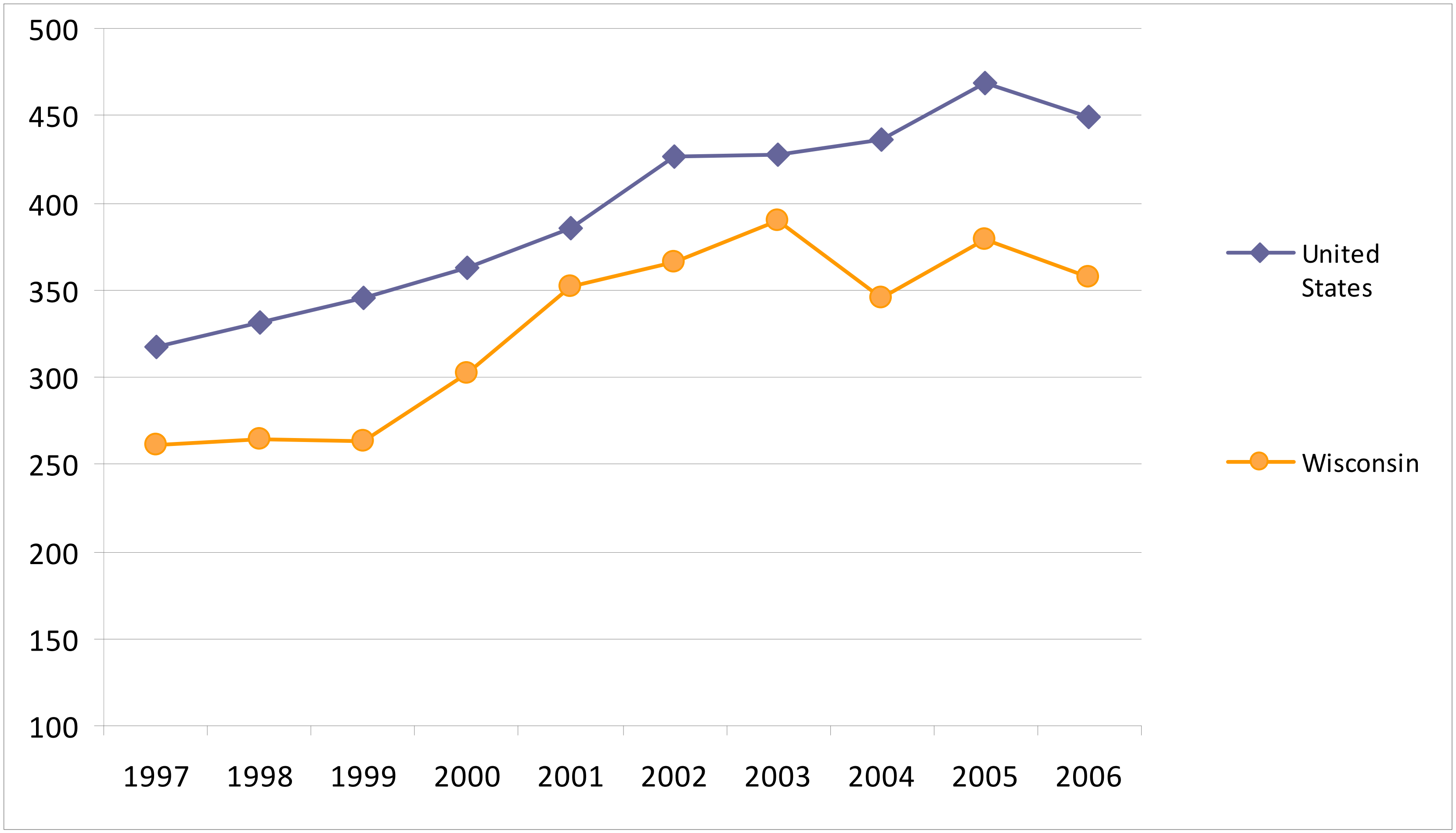


Figure 5: Medicaid Expenditure
Real 2005 dollars per capita

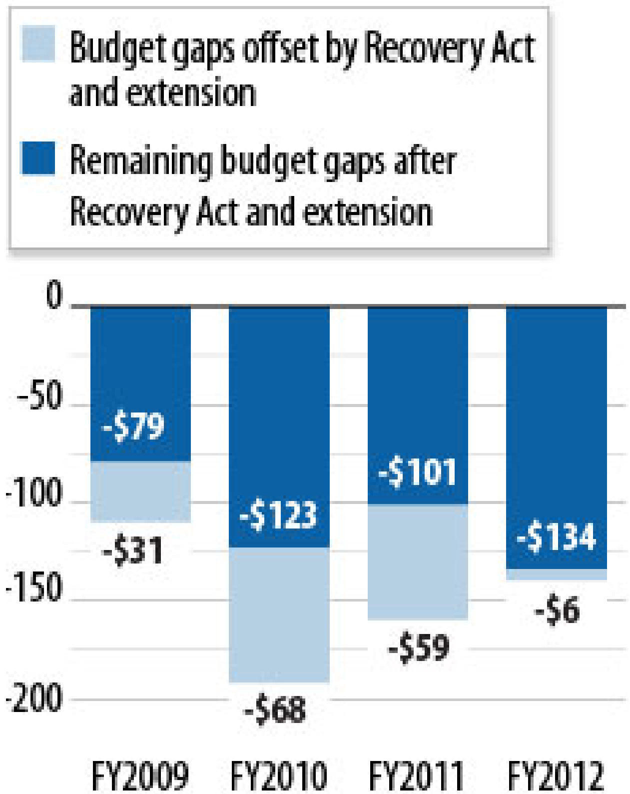


What can we expect over the next decade?

- Short-term
  - Unemployment rates will remain high for several years and state revenue growth will be sluggish.
  - Financial markets may be less willing to loan to states and may require higher interest rates.
- Longer-term (US Government Accountability Office projects major imbalances in state & local sectors)
  - Demographic transition (especially health care) will strain state budgets.
  - Sales tax revenue growth will lag behind economic growth.
  - Medicaid and other health care costs will rise rapidly.
  - Inflation-adjusted federal aid will not rise and may fall.

2012 Could Be Worst Year Yet for States

Budget shortfalls in billions



Source: CBPP analysis using data from U.S. Department of Health and Human Services, U.S. Department of Education, Congressional Budget Office, and state budget documents. Revised September 2010

Center on Budget and Policy Priorities | cbpp.org

Long run strategies for effective fiscal management

- Things to avoid
  - One time fixes (asset sales, tax amnesties).
  - Stagnant/antiquated revenue sources (e.g. narrow sales tax).
  - Uncontrollable spending commitments (e.g. health care spending for retirees).
  - Concealed cost or burden shifting to local government.
  - Borrowing to pay recurring expenses.

Long run strategies for effective fiscal management

- Things to consider
  - Budget transparency
    - Report budget categories on consistent basis over time.
    - Identify one-time and recurring revenues and expenses.
    - Publish multi-year spending and revenue forecasts.
    - Independent analyses of revenue, spending, and long-term obligations.
  - Enforceable and transparent budget rules.
  - Regular reports on structural deficits and cyclical deficit
  - Build rainy-day funds during boom periods.

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Budgeting in periods of fiscal stress

- Use data to anticipate future fiscal stress and begin early discussion of options.
- Understand that fiscal stress may persist long after an economic downturn ends.
- Use a comprehensive budgeting process (budget rules) that encourages explicit trade-offs.
- Use evidence-based studies to prioritize competing categories.

Protecting vulnerable children and Families in an era of fiscal stress

When spending cuts are necessary consider:

- Categorizing by policy rather than political criteria (e.g. families vs single adults rather than North vs South).
- Better targeting of existing spending (e.g. reductions in school aid to high property wealth districts).
- Small targeted increases in spending (e.g. subsidies for child care for low income families) that offset spending cuts.
- Targeted reductions in relatively ineffective tax expenditures (e.g. sales tax exemption for food).

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Special considerations

- Midwestern states
  - Continue to lose population relative to the rest of the nation.
  - Are aging rapidly—this has important implications for both the kind of public services needed and sales, property and income tax bases.
  - Are highly interdependent. About 1/3 of Wisconsin's out-of-state trade is with IL, IN, MI and Ohio. By comparison, only 10% involves foreign countries.

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