

News Release

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MTF Forecast: Improving But Still Slow Revenue Growth in Fiscal 2014

Fiscal 2014 tax revenues will grow by \$835 million, or 3.9 percent, to \$22.37 billion, according to a new forecast released today by the Massachusetts Taxpayers Foundation.

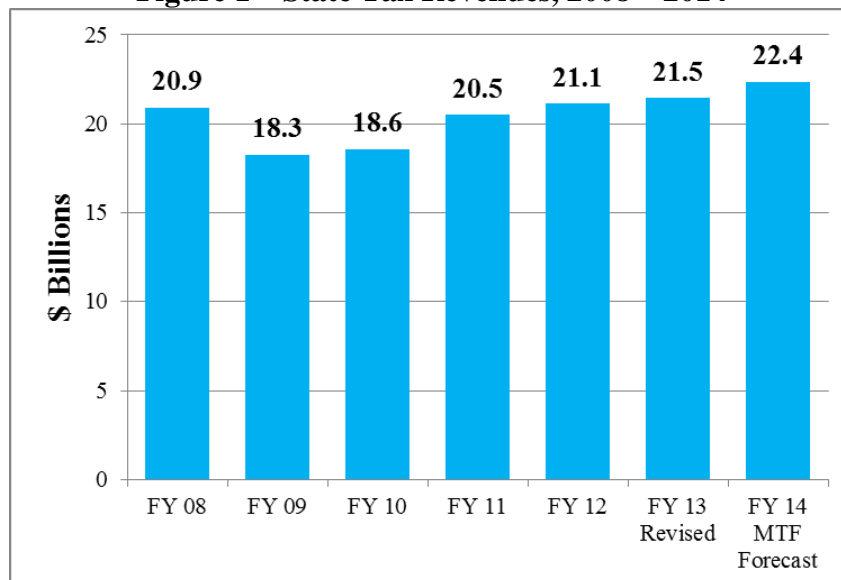
The Foundation projects tax collections of \$21.53 billion for fiscal 2013, virtually identical with the administration's recently revised estimate of \$21.47 billion, an increase of only \$420 million or 2 percent over fiscal 2012 revenues.

MTF President Michael J. Widmer presented the Foundation's economic and revenue forecast to members of the House and Senate Ways and Means Committees and the Secretary of Administration and Finance at their annual consensus revenue hearing at the State House today.

"While fiscal 2014 shows an improving revenue picture, we are still a long way from experiencing the level of revenue growth of prior economic recoveries," Widmer said.

As shown in Figure 1, fiscal 2014 is the first year in which state tax revenues exceed the pre-recession peak of \$20.9 billion in 2008 (after adjusting for the increase in the sales tax rate from 5 to 6.25 percent in 2010 which added roughly \$1 billion in tax revenues annually).

Figure 1 – State Tax Revenues, 2008 – 2014



The Massachusetts economy slowed sharply in the third quarter of 2012, falling behind a slackening U.S. recovery, and forcing the administration's downward revision of revenues by \$515 million. The weakness in 2013 revenues is due in large part to anemic job growth. The state has added only 7,000 jobs through October, and the Foundation projects an increase of 15,000 jobs, less than one-half of 1 percent, in all of fiscal 2013.

The Foundation's fiscal 2014 forecast anticipates a slightly better revenue picture due to an improving national economy as real U.S. GDP growth is projected to double from 1.8 percent in 2013 to 3.9 percent in 2014. However, while national employment is expected to grow by nearly 2 percent in fiscal 2014, the Foundation projects that state employment will increase by less than 1 percent, adding roughly 20,000 jobs.

While 3.9 percent revenue growth in 2014 is nearly double the rate in fiscal 2013, it is well below the 5.8 percent average annual growth in total tax collections – excluding capital gains taxes – from fiscal 2003 to 2008 following the last recession and half the 8 percent average annual growth rate from 1990 to 2008.

Income taxes continue to drive overall growth in tax collections as sales, corporate and other sources have been relatively flat for the past decade. According to the Foundation's forecast, over 80 percent of the state's 2014 revenue growth will come from personal income taxes, which are projected to rise by 5.6 percent or \$693 million based on an anticipated 5.7 percent expansion in wages and salaries (Table 1).

Sales tax revenues are projected to grow by \$50 million, or 1 percent, to \$5.24 billion. Although the slow growth can be attributed to ongoing weakness in employment and consumer spending, it reflects a long-term trend that has seen sales taxes average roughly 1 percent annual growth from 2001 to 2012. Several factors that have curtailed personal consumption spending over the past decade are likely to continue unabated for the foreseeable future, including lackluster growth in personal income, increased personal savings, the paying down of personal debt, and restricted access to credit.

Table 1 – State Tax Revenues by Category
(\$ millions)

| | FY 11 | FY 12 | FY 13 Original | FY 13 Revised | MTF FY 13 | MTF FY 14 | \$ Change 14 vs. 13 | % Change |
|----------------------|---------------|---------------|-------------------|------------------|---------------|---------------|------------------------|-------------|
| Income | 11,576 | 11,911 | 12,720 | 12,463 | 12,463 | 13,156 | 693 | 5.6% |
| Sales | 4,905 | 5,059 | 5,310 | 5,176 | 5,192 | 5,242 | 50 | 1.0% |
| Corporate & Business | 2,251 | 2,344 | 2,124 | 2,062 | 2,097 | 2,145 | 48 | 2.3% |
| All Other | 1,784 | 1,800 | 1,856 | 1,794 | 1,781 | 1,825 | 44 | 2.5% |
| Total | 20,517 | 21,115 | 22,010 | 21,496 | 21,533 | 22,368 | 835 | 3.9% |

Employment

The Foundation forecasts Massachusetts will add a paltry 15,000 jobs in fiscal 2013 and 20,000 jobs in 2014 due to continued weakness in the U.S. and global economies. Through October 2012, Massachusetts is still down 130,000 jobs or 4 percent from January 2001, ranking it among the bottom 15 states over the past decade.

The jobs outlook would worsen considerably if a projected \$1.2 trillion reduction over 10 years in federal defense and discretionary domestic spending takes effect in January 2013. Massachusetts could lose 30,000 to 40,000 defense related jobs alone, according to studies by the Donahue Institute at the University of Massachusetts.

Personal Income

The Foundation projects personal income growth to fall from 3.5 percent in fiscal 2012 to 2.6 percent in fiscal 2013, climbing to 4.7 percent in 2014. This compares to an annual average of 6.3 percent between 2005 and 2008.

Capital Gains

Capital gains tax revenues are forecasted to grow to \$1.2 billion in fiscal 2013 due to an expected increase in sales of assets in late 2012 in anticipation of a potential hike in the federal capital gains tax rate in January 2013. Capital gains taxes are projected to decline to roughly \$1 in fiscal 2014.

Sales Taxes

The anemic sales tax growth projected for fiscal 2013 and 2014 reflects a decade-long trend in which sales taxes in Massachusetts have grown at less than the rate of inflation. It is estimated that Massachusetts would receive between \$200 and \$300 million in additional sales taxes if federal law were changed to permit states to tax all Internet and remote sales.

Corporate and Business Taxes

MTF projects \$2.15 billion in corporate and business taxes in 2014, a \$48 million increase over fiscal 2013. The Foundation does not include any one-time tax settlements in its fiscal 2014 forecast. One-time tax settlements in excess of \$10 million, which are deposited into the state's stabilization fund, totaled \$335 million in fiscal 2012. Such settlements total \$25 million through the first five months of fiscal 2013 are included in the Foundation's 2013 forecast.

National and Global Risks

The Foundation's forecast assumes an orderly resolution to the 'fiscal cliff' avoiding much, but not all, of the \$1.2 trillion in sequestration cuts to defense and discretionary spending. If unresolved, state tax collections could be negatively impacted by \$300 million in fiscal 2013 and \$1 billion in fiscal 2014.

The national estimates from Moody's Analytics are based on the following assumptions: the 2 percent payroll tax cut and emergency unemployment benefits expire in January, tax cuts for couples making \$250,000 or less remain in place, Congress extends the inflation adjustment for the alternative minimum tax (AMT), and Washington leaders solve the pending debt ceiling debate with minimal drama.

Global risks to the U.S. economy and this forecast include an unresolved financial crisis with one or more nations defaulting on their debt, expansion of Middle East hostilities into a regional conflict, or a collapse of China's economy, any of which could lead to a global recession.

MASSACHUSETTS TAXPAYERS FOUNDATION

FISCAL YEAR FORECAST SUMMARY

MOODY'S ANALYTICS NATIONAL FORECAST

| December 2012 | | | | <<< History | | Forecast >>> | |
|---|--------|-------|-------|-------------|--------|--------------|--------|
| | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 |
| Personal Income (billions of 2000 \$) | 10,026 | 9,758 | 9,571 | 9,913 | 10,076 | 10,226 | 10,566 |
| % change | 3.4 | -2.7 | -1.9 | 3.6 | 1.6 | 1.5 | 3.3 |
| Employment (millions) | 137.7 | 133.9 | 129.7 | 130.5 | 132.3 | 134.0 | 136.2 |
| % change | 0.6 | -2.8 | -3.2 | 0.7 | 1.4 | 1.3 | 1.6 |
| Unemployment Rate | 5.0 | 7.6 | 9.7 | 9.3 | 8.6 | 7.9 | 7.6 |
| CPI (% change) | 3.7 | 1.0 | -0.8 | 2.0 | 1.9 | 2.3 | 2.7 |
| PPI (% change) | 9.0 | -2.2 | -7.9 | 6.2 | 5.3 | 3.2 | 4.1 |
| Federal Discount Rate | 4.3 | 1.2 | 0.5 | 0.8 | 0.8 | 0.9 | 1.1 |
| Prime Commercial Rate | 6.7 | 3.9 | 3.3 | 3.3 | 3.2 | 3.2 | 3.2 |
| Standard & Poor's 500 Index (% change*) | 12.7 | -17.3 | -36.5 | 20.3 | 11.4 | 8.0 | 6.9 |

| MTF MASS. ECONOMIC FORECAST | | | | <<< History | | Forecast >>> | |
|--|-------|-------|-------|-------------|-------|--------------|-------|
| | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 |
| Personal Income (billions of current \$) | 331.0 | 329.5 | 327.0 | 345.5 | 357.5 | 366.8 | 384.1 |
| % change | 5.3 | -0.4 | -0.8 | 5.7 | 3.5 | 2.6 | 4.7 |
| Personal Income (billions of 2000 \$) | 270.4 | 264.3 | 260.6 | 270.2 | 274.0 | 275.8 | 282.8 |
| % change | 2.9 | -2.3 | -1.4 | 3.7 | 1.4 | 0.6 | 2.5 |
| Total Employment (000s) | 3,294 | 3,240 | 3,175 | 3,201 | 3,223 | 3,238 | 3,258 |
| % change | 1.0 | -1.6 | -2.0 | 0.8 | 0.7 | 0.5 | 0.6 |
| Unemployment Rate | 4.6 | 6.9 | 8.6 | 7.8 | 6.8 | 6.3 | 6.2 |

| MTF MASS. TAX FORECAST | | | | <<< History | | Forecast >>> | |
|---------------------------|--------|--------|--------|-------------|--------|--------------|--------|
| | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 |
| Income Tax (millions \$) | 12,498 | 10,593 | 10,128 | 11,570 | 11,911 | 12,463 | 13,156 |
| % change | 9.7 | -15.2 | -4.4 | 14.2 | 3.0 | 4.6 | 5.6 |
| Sales Tax | 4,088 | 3,870 | 4,626 | 4,909 | 5,059 | 5,192 | 5,242 |
| % change | 0.5 | -5.3 | 19.5 | 6.1 | 3.1 | 2.6 | 1.0 |
| Corporations Tax | 2,285 | 1,916 | 1,936 | 2,051 | 2,344 | 2,097 | 2,145 |
| % change | -3.4 | -16.2 | 1.1 | 5.9 | 14.3 | -10.5 | 2.3 |
| TOTAL TAXES** | 20,645 | 18,088 | 18,392 | 20,346 | 21,114 | 21,533 | 22,367 |
| % change | 5.2 | -12.4 | 1.7 | 10.6 | 3.8 | 2.0 | 3.9 |
| TOTAL TAXES FOR BUDGET*** | 17,724 | 15,225 | 15,657 | 17,493 | 18,158 | 18,515 | 19,226 |
| % change | 4.3 | -14.1 | 2.8 | 11.7 | 3.8 | 2.0 | 3.8 |

* Percent change in index for prior calendar year.

** Includes collections from other tax sources not detailed above.

*** Tax revenues available for appropriation in the budget exclude a portion of sales tax receipts dedicated to the MBTA and school building construction, tax revenues dedicated to pension funding, and net revenues in excess of permissible tax revenues.