ALLEGHENY INSTITUTE FOR PUBLIC POLICY

November 2, 2016 **Policy Brief: Volume 16, Number 47**

State Jobs and Revenue Gains Very Weak in Recent Months

Summary: The State's fiscal situation is closely tied to its economic growth. As the economy grows jobs, tax receipts from firms and individuals grow. This *Policy Brief* looks at the recent dramatic slowing in job gains in the Commonwealth and the accompanying weakness in state tax revenue.

The Pennsylvania economy has been plodding slowly along as evidenced by the weakening jobs numbers since March of this year. Job growth is not only a measure of the economic wellbeing of the Commonwealth; it also affects the amount of tax revenue the State can expect to collect. When job gains weaken, so will tax collections. For the first quarter of the current fiscal year (2016-17), Pennsylvania's revenues have borne out this relationship as total general fund revenues, and many of the subcategories such as corporate net income, and personal income, are running behind the year earlier pace. And, more importantly they are coming in below the State's official estimates for the current fiscal year.

Recently released labor data for September put the seasonally adjusted unemployment rate at 5.7 percent, up almost a percentage point from the March rate of 4.9 percent and a full point since January's 4.6 percent rate. Over the same six month period, the household survey data show the number of people reporting they were working had fallen by 34,000.

The establishment survey payroll data show a similar pattern. Over the last six months, nonfarm employment was essentially flat rising very slightly from March (5,894.6 thousand) to September (5,895.2 thousand). Meanwhile, private sector jobs fell by 3,000 during that time. In contrast, in the preceding six months from September 2015 to March 2016, private employment rose by 51,000. It is important to note that Pennsylvania's private employment in September was only a tiny 2.8 percent higher than the pre-recession level of September 2007. It took seven years for employment to recover to pre-recession levels.

It is virtually axiomatic that a slowing in job gains will translate to weaker revenue growth for taxing bodies. Indeed, in the first quarter of the State's current fiscal year (July through September) total general fund revenues fell slightly compared to the same quarter of the previous fiscal year (-0.21 percent). Of the three most important revenue streams (corporate net income, personal income, and sales and use taxes) only the sales and use tax amount is ahead of last year's pace (0.19 percent). The personal income tax, the largest of the three, is trailing last year's collections by 2.4 percent while the corporate net income tax is down 7.6 percent. The corporate tax is problematic because it is a tax on corporate profits and if profits are down, hiring new employees is less likely, and the firm may be in danger of having to do layoffs. Note that a sizable jump in the cigarette tax (owing to the dollar per pack tax hike) has kept the general fund revenue decline from being even greater.

Even more problematic for the Commonwealth is that actual revenue collections are significantly below estimated figures prepared for the budget. Through the first quarter of the current fiscal year total general fund revenues were $6.614 billion. The State's estimate was for collections of $6.833 billion resulting in a $219 million shortfall relative to forecast. Corporate net income taxes are off by more than $67 million ($529.2 million actual vs. $596.9 million estimated). The estimates were a little closer for the personal income tax with $2.731 billion actual vs. $2.786 billion estimated, and for the sales and use tax, revenue was overestimated by $72.4 million ($2.495 billion actual vs. $2.567 billion estimated). Obviously, unless the first quarter performance is dramatically improved in the months ahead there will be a major budget problem early in 2017.

The cigarette tax had the largest revenue increase compared to the first quarter of the previous fiscal year owing to the $1 per pack boost from $1.60 to $2.60. For the first quarter of the current fiscal year, the State has collected $279.7 million, up by $32 million from a year earlier. However, the collections are below the State's estimate of $289.4 million, a shortfall of about $10 million.

The July to September quarter slowing compared to a year ago is not a recent problem either. Looking at these revenues over the last six months shows a similar pattern. Total general fund revenues for April 2016 through September 2016 are $15.28 billion. Last year during that six month span they were $15.51 billion. In our *Policy Brief* from early July (*Volume 16, Number 29*) we noted that "The slowdown has been underway for some time but has become pronounced in the last several months. Fiscal Year to date total revenue gains for each month of 2016 have fallen well short of the increases posted for January through May in 2015. For January to May 2016, the average Fiscal Year to date rise was 1.4 percent with the May cumulative fiscal year to date a meager 0.6 percent. For the same period in 2015, the average increase was 7 percent and for May of 2015 it was 7.3 percent."

The caution lights are flashing. Pennsylvania's job growth is flagging and that is translating into weaker collections of tax revenues. This has the potential to become a sizable problem as the fiscal year progresses if the economy and jobs do not return to significantly faster growth—and soon. In light of the decade of anemic employment gains, it would seem apparent that Pennsylvania must adopt policies that promote strong economic growth and move away from its tradition of fealty to public sector unions and its regulatory environment that hamstring businesses.

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