

MAINE STATE LEGISLATURE

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**Report of the
MAINE CONSENSUS ECONOMIC FORECASTING COMMISSION
October 17, 2005**

Commissioners present:

Charlie Colgan, Muskie School, USM, Chair
Michael Donihue, Colby College
John Davulis, CMP
Charles Lawton, Planning Decisions

Staff Support present:

Michael Allen, (MRS), Dana Evans (DOL), John Nyada, (MRS), Galen Rose, (SPO),
Jerome Stanhope, MRS

The Commission met on October 13, 2005 to discuss whether their January 2005 forecast should be revised before the Revenue Forecasting Committee meets in November. The Commission made substantial changes to the previous forecast, based on changes in current national and State economic conditions and updated forecasts for Maine from the State Planning Office, the New England Economic Partnership, Global Insight, Inc., and Colby College. The table below summarizes those changes for wage and salary employment growth, personal income growth, and the US Consumer Price Index.

| | <u>2005</u> | <u>2006</u> | <u>2007</u> | <u>2008</u> | <u>2009</u> |
|--|-------------|-------------|-------------|-------------|-------------|
| • W&S Employment (Annual Percentage Change) | | | | | |
| > Consensus 1/2005 | 1.7 | 1.5 | 1.1 | 1.3 | 1.3 |
| > Consensus 10/2005 | 0.8 | 0.9 | 0.7 | 0.8 | 0.8 |
| • Personal Income (Annual Percentage Change) | | | | | |
| > Consensus 1/2005 | 4.0 | 4.0 | 4.0 | 4.0 | 4.0 |
| > Consensus 10/2005 | 5.5 | 5.5 | 5.0 | 5.0 | 5.0 |
| • CPI (Annual Percentage Change) | | | | | |
| > Consensus 1/2005 | 2.0 | 2.0 | 2.0 | 2.0 | 2.0 |
| > Consensus 10/2005 | 3.2 | 2.8 | 2.5 | 2.2 | 2.2 |

Four forecasts formed the basis for much of the discussion. These were the State Planning Office (SPO) and New England Economic Project (NEEP) forecasts, which were based on underlying U.S. forecasts and a Maine model prepared by Economy.com, a Global Insight (GI) forecast, and a forecast generated by Colby College using its own model. The four underlying employment forecasts differed significantly only for the years 2006 and 2007, with the SPO forecast showing much stronger employment growth than the others in 2006, and the Global Insight forecast showing stronger growth than the others in 2007.

The Commission concluded the most reasonable forecast would call for employment growth slightly slower than the GI, NEEP, and Colby forecasts, and personal income growth approximating the GI forecast.

In terms of personal income, the SPO forecast showed significantly stronger growth for 2005 and 2006 than the other forecasts, while the Colby forecast showed much weaker growth than the others for those years (the NEEP forecast was discounted since it was run before historical personal income data was published in late September). The final Consensus forecast conforms very closely with the mid-range GI forecast.

The current Consensus employment forecast was adjusted downward significantly from the January forecast largely because employment growth through 2004 and the first two-thirds of 2005 was much weaker than expected, and all of the models consulted projected a continuation of this general trend.

The current personal income forecast was adjusted upward by 1 to 1.5 percentage points each year over the forecast horizon, resulting largely from the effects on the models of recent upward revisions to the historical data published by the US Bureau of Economic Analysis.

The table on the following page shows the Commission's complete forecast.

Maine Consensus Economic Forecasting Commission
Forecast of October 2005

| | HISTORY | | | | | | | FORECAST | | | | |
|---|----------|----------|----------|---------|--|----------|---------|----------|---------|---------|---------|---------|
| | 1998 | 1999 | 2000 | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 | 2007 | 2008 | 2009 |
| CPI-u (Ann. Growth Rate) | 1.6% | 2.2% | 3.4% | 2.8% | 1.6% | 2.3% | 2.7% | 3.2% | 2.8% | 2.5% | 2.2% | 2.2% |
| Me. Unemployment Rate | 4.4% | 4.1% | 3.4% | 4.0% | 4.4% | 5.0% | 4.6% | 4.7% | 4.7% | 4.8% | 4.6% | 4.4% |
| 3-Month Treasury Bill Rate | 4.9% | 4.8% | 6.0% | 3.5% | 1.6% | 1.0% | 1.4% | 3.1% | 4.5% | 4.5% | 4.4% | 4.4% |
| 10-Year Treasury Note Rate | 5.3% | 5.6% | 6.0% | 5.0% | 4.6% | 4.0% | 4.3% | 4.4% | 5.8% | 5.8% | 5.6% | 5.8% |
| Maine Agricultural Empl.(1,000's) | 16.0 | 13.0 | 19.8 | 17.1 | 18.8 | 16.1 | 14.0 | 18.6 | 17.0 | 17.0 | 17.0 | 17.0 |
| Employment Levels (1,000's) | | | | | | | | | | | | |
| Maine Wage & Salary Employment | 569.1 | 586.3 | 603.5 | 608.2 | 606.4 | 606.7 | 613.6 | 618.5 | 624.0 | 628.4 | 633.6 | 638.8 |
| Natural Resources | 2.7 | 2.7 | 2.7 | 2.7 | 2.6 | 2.5 | 2.6 | 2.6 | 2.7 | 2.7 | 2.7 | 2.7 |
| Construction | 25 | 27.8 | 29.2 | 29.9 | 29.4 | 30.5 | 31.0 | 31.5 | 30.5 | 30.2 | 30.4 | 30.6 |
| Manufacturing | 81.1 | 80.6 | 79.5 | 74.7 | 68.0 | 64.1 | 63.1 | 62.0 | 61.6 | 61.0 | 60.3 | 59.9 |
| Trade/Transp//Publ. Utils. | 115.9 | 119.5 | 122.7 | 123.6 | 123.3 | 123.2 | 125.7 | 126.7 | 127.7 | 128.0 | 127.8 | 128.1 |
| Information | 11.1 | 11.7 | 12.1 | 12.1 | 11.6 | 11.3 | 11.6 | 12.0 | 12.2 | 12.3 | 12.5 | 12.5 |
| Financial Activities | 31.2 | 32.8 | 34.1 | 35.1 | 35.1 | 35.1 | 34.9 | 34.3 | 34.6 | 34.8 | 35.2 | 35.5 |
| Prof. & Business Services | 46.6 | 48.3 | 51.8 | 51.8 | 51.4 | 50.3 | 49.6 | 49.8 | 50.5 | 51.3 | 52.3 | 53.1 |
| Education & Health Services | 90 | 94.2 | 97.5 | 100.8 | 104.9 | 107.3 | 111.2 | 113.6 | 116.2 | 118.3 | 120.8 | 123.2 |
| Leisure & Hospitality Services | 53.2 | 54.3 | 55.9 | 56.5 | 57.3 | 58.5 | 59.3 | 60.6 | 61.9 | 63.2 | 64.5 | 65.7 |
| Other Services | 17.7 | 18 | 18.3 | 19.1 | 19.8 | 20.3 | 20.0 | 20.0 | 20.3 | 20.6 | 20.8 | 21.0 |
| Government | 94.6 | 96.7 | 99.5 | 102.0 | 103.1 | 103.7 | 104.9 | 105.4 | 105.8 | 106.0 | 106.3 | 106.5 |
| Annual Growth Rates | | | | | | | | | | | | |
| Maine Wage & Salary Employment | - | 3.0% | 2.9% | 0.8% | -0.3% | 0.1% | 1.1% | 0.8% | 0.9% | 0.7% | 0.8% | 0.8% |
| Natural Resources | - | 0.0% | 0.0% | -1.4% | -1.9% | -2.6% | 3.0% | -0.7% | 3.9% | -0.1% | 0.0% | 0.0% |
| Construction | - | 11.2% | 5.2% | 2.1% | -1.4% | 3.5% | 1.8% | 1.5% | -3.1% | -1.0% | 0.7% | 0.7% |
| Manufacturing | - | -0.6% | -1.3% | -6.1% | -8.9% | -5.8% | -1.6% | -1.7% | -0.6% | -1.0% | -1.1% | -0.7% |
| Trade/Transp//Publ. Utils. | - | 3.1% | 2.7% | 0.8% | -0.3% | -0.1% | 2.0% | 0.8% | 0.8% | 0.2% | -0.2% | 0.2% |
| Information | - | 5.4% | 3.6% | 0.2% | -4.7% | -2.0% | 2.2% | 3.5% | 1.7% | 0.8% | 1.6% | 0.0% |
| Financial Activities | - | 5.1% | 3.9% | 3.0% | 0.0% | -0.1% | -0.5% | -1.7% | 0.9% | 0.6% | 1.1% | 0.9% |
| Prof. & Business Services | - | 3.6% | 7.3% | 0.0% | -0.9% | -2.1% | -1.3% | 0.3% | 1.4% | 1.6% | 1.9% | 1.5% |
| Education & Health Services | - | 4.7% | 3.5% | 3.4% | 4.2% | 2.3% | 3.6% | 2.2% | 2.3% | 1.8% | 2.1% | 2.0% |
| Leisure & Hospitality Services | - | 2.1% | 2.9% | 1.0% | 1.5% | 2.0% | 1.4% | 2.2% | 2.2% | 2.1% | 2.1% | 1.9% |
| Other Services | - | 1.7% | 1.9% | 4.1% | 3.5% | 2.5% | -1.4% | 0.2% | 1.4% | 1.4% | 0.9% | 1.2% |
| Government | - | 2.2% | 2.9% | 2.5% | 1.0% | 0.7% | 1.1% | 0.5% | 0.4% | 0.2% | 0.3% | 0.2% |
| Million \$ - at Seas. Adjusted Annual Rates | | | | | | | | | | | | |
| Personal income | 29709.75 | 31016.25 | 33173.25 | 35107 | 35964.5 | 37251.25 | 39481.8 | 41662.1 | 43934.3 | 46113.7 | 48404.0 | 50809.5 |
| Wage and salary disbursements | 15204 | 16234.0 | 17194.8 | 17982.8 | 18551.8 | 19249.8 | 20191.5 | 21140.5 | 22155.2 | 23174.4 | 24240.4 | 25355.5 |
| Supplements to Wages & Salaries | 3359.75 | 3554 | 3772.75 | 4058.5 | 4422.5 | 4630.75 | 5036.0 | 5368.4 | 5733.4 | 6111.8 | 6515.2 | 6945.2 |
| Non-farm Proprietors' income | 2,131 | 2227.5 | 2347.0 | 2768.3 | 2630.8 | 2773.3 | 3027.8 | 3270.0 | 3538.1 | 3757.5 | 3982.9 | 4221.9 |
| Farm Proprietors' income | 55.5 | 77.0 | 57.0 | 27.5 | -59.8 | -23.3 | -26.3 | 41.4 | 43.0 | 44.8 | 46.6 | 48.5 |
| Dividends, interest, and rent | 5745 | 5618.5 | 6178.5 | 6338.3 | 6089.3 | 5834.0 | 6078.0 | 6333.3 | 6624.6 | 6783.6 | 6966.8 | 7147.9 |
| Transfer payments | 5122 | 5279.3 | 5588.3 | 6017.8 | 6477.3 | 7021.5 | 7499.0 | 7978.9 | 8473.6 | 8982.0 | 9521.0 | 10092.2 |
| less: Personal contrb. for social insur. | 2418 | 2554.8 | 2665.8 | 2811.8 | 2857.5 | 2941.0 | 3079.3 | 3242.5 | 3414.3 | 3557.7 | 3721.4 | 3892.5 |
| Adjustment for residence | 511 | 580.3 | 700.5 | 726.5 | 710.3 | 705.8 | 755.5 | 772.1 | 780.6 | 817.3 | 852.4 | 890.8 |
| Farm Income | 138 | 153.8 | 145.8 | 111.5 | 46.5 | 68.5 | 72.0 | 83.3 | 87.9 | 92.3 | 96.9 | 101.7 |
| Annual Growth Rates | | | | | | | | | | | | |
| Personal income | - | 4.4% | 7.0% | 5.8% | 2.4% | 3.6% | 6.0% | 5.5% | 5.5% | 5.0% | 5.0% | 5.0% |
| Wage and salary disbursements | - | 6.8% | 5.9% | 4.6% | 3.2% | 3.8% | 4.9% | 4.7% | 4.8% | 4.6% | 4.6% | 4.6% |
| Supplements to Wages & Salaries | - | 5.8% | 6.2% | 7.6% | 9.0% | 4.7% | 8.8% | 6.6% | 6.8% | 6.6% | 6.6% | 6.6% |
| Non-farm Proprietors' income | - | 4.5% | 5.4% | 17.9% | -5.0% | 5.4% | 9.2% | 8.0% | 8.2% | 6.2% | 6.0% | 6.0% |
| Farm Proprietors' income | - | 38.7% | -26.0% | -51.8% | ----- Not Available - negative base values ----- | ----- | ----- | 3.9% | 4.2% | 4.0% | 4.1% | 4.1% |
| Dividends, interest, and rent | - | -2.2% | 10.0% | 2.6% | -3.9% | -4.2% | 4.2% | 4.2% | 4.6% | 2.4% | 2.7% | 2.6% |
| Transfer payments | - | 3.1% | 5.9% | 7.7% | 7.6% | 8.4% | 6.8% | 6.4% | 6.2% | 6.0% | 6.0% | 6.0% |
| less: Personal contrb. for social insur. | - | 5.7% | 4.3% | 5.5% | 1.6% | 4.7% | 5.3% | 5.3% | 5.3% | 4.2% | 4.6% | 4.6% |
| Adjustment for residence | - | 13.5% | 20.7% | 3.7% | -2.2% | -0.6% | 7.0% | 2.2% | 1.1% | 4.7% | 4.3% | 4.5% |
| Farm Income | - | 11.4% | -5.2% | -23.5% | -58.3% | 47.3% | 5.1% | 15.7% | 5.5% | 5.0% | 5.0% | 5.0% |

In deliberating its October 2005 forecast, the Commission considered the following:

1) The State Planning Office reported that the Maine economy had grown very slowly through the summer, with some improvements only in the real estate and construction sectors.

US real Gross Domestic Product growth through the first half-year was solid, though somewhat slower than during the previous year. National job growth has been slow.

Personal income growth in the second quarter in Maine was 1.3%, while the nation's income grew 1.5%: this is the latest published data. Maine's growth rate for the quarter was 47th among the 50 states. Similarly, in Maine, the Coincident Economic Index (a surrogate for gross state product growth) for the June through August period grew at an annual rate of 0.9% over the previous 3-month period, for a ranking of 41st among the 50 states.

The Maine Department of Labor reported that wage and salary employment for the first 8 months of the year was up only 0.8% over the same period of last year. Most of the job growth was in education and health services (2,300), leisure and hospitality (1,000), construction (900), and the trade-transportation-utilities group (900). The largest declines were in manufacturing (-1,800) and financial services (-300). The State's seasonally adjusted unemployment rate rose from 4.6% in December to 5% in August, while the national rate fell from 5.4% to 4.9%. Prior to August, Maine's unemployment rate had been below the national average for nearly seven years.

While housing unit permits had faltered a bit earlier in the year, permits for the June through August period were up 8.8% over the same period of last year. The value of residential construction contracts also increased fairly strongly through those summer months, gaining 9.4% over the summer of 2004. Conversely, unit sales of pre-owned homes (seasonally adjusted) declined by about 1% from the first quarter. Home sale prices continued to rise rapidly in the second quarter, however, increasing at an annual rate of 14.1%.

While economic growth clearly has been slower this year than last, there are yet a few positives such as significant improvements in the housing permit and residential construction numbers. The timing of the scheduled closing of Brunswick Naval Air Station is unclear, but it may effect the last year of the forecast horizon, depending on precisely how the closure is to be carried out, but not sooner. In the near-term, stronger broad-based growth in the Maine economy appears unlikely while gasoline and other energy prices continue to place a drag on growth.

2. Maine Revenue Services (MRS) reported that General Fund revenues through the first 3 months of the fiscal year were \$51.5 million over budget, but several special factors indicate that this overstates the apparent health of the economy. Individual income tax revenues were \$33.8 million over budget, but Revenue Services economists reported that much of this was due to timing issues involving slow refunds for the circuit breaker and BETR programs. Adjusting for these factors would leave a surplus of roughly \$6 million. Sales tax revenues were \$5.7 million (3%) under budget. Exceptionally high home heating fuel prices this winter are expected to contribute further to the shortfall through the winter. Corporate income tax revenues were \$12.2 million (42.6%) over budget, and MRS economists noted that corporate profits have been very strong nationwide. Also, the estate tax was 12.5 million over budget, but this was largely due to one estate.

3. Commissioners noted a number of positive trends which may impact the Maine economy going forward. These included:

- a. The rebuilding efforts resulting from hurricanes Katrina and Rita should provide significant national economic stimulus next year.
- b. US monetary and fiscal policies are still stimulative, which is helping to maintain strong consumer spending.

4. Several important negative trends were also noted by Commissioners. These included:

- a. US labor market job openings and turnover rates are still weak, with no positive signs.
- b. World oil prices have been volatile and extremely high in recent months, and currently topping \$60 per barrel. While the national forecasts studied suggest prices will fall somewhat, to the \$40 to \$45 per barrel range over the next couple years, this level is still well above the norm of the past few years.
- c. Increasing current account deficits may cause a sharp drop in the value of the dollar as foreign creditors worry about repayment of their debt; the result would likely be a sharp rise in US short and long term interest rates to compensate foreign creditors for their risks. The rise in interest rates would reduce borrowing and economic activity in the US, particularly in the housing sector.
- d. The current level of housing activity is already slowing due to rising interest rates, and this will likely continue through the forecast period.
- e. The Base Realignment and Closure Commission (BRAC) has determined that Brunswick Naval Air Station will be closed. This will have serious negative impacts on the economies of Cumberland and Sagadahoc counties, and hence the state as a whole, but closure will likely not begin until 2009.