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Michigan’s COVID-19 Fiscal Wounds Less Severe Than Previously Forecast

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Michigan trimmed about $3 billion off its projected COVID-19-driven deficits between fiscal 2020 and 2022 after federal relief helped soften the economic blow.

The state's revised revenue projections are down by $5.106 billion for fiscal 2020, 2021 and 2022 from its formal January estimates. The good news is that’s down from a collective $8.37 billion revenue loss projected in May.

"Federal stimulus programs played a critical role in indirectly supporting state revenues, albeit still quite a bit less than we would have likely generated had it not been for the pandemic,” said state Treasurer Rachael Eubanks.

State officials cautioned against any celebration. “While today’s updated revenue picture is better than the forecast in May, it’s still far worse than the January forecast and we are still looking at dramatic revenue losses in fiscal years 2021 and 2022, totaling nearly $4.2 billion,” said state Budget Director Chris Kolb.

The improvement was due in part to the various forms of federal relief from the CARES Act signed March 27 and other programs. The estimates don’t bank on any relief to make up for tax losses in a new federal package as negotiations remain stalled in part over the inclusion of aid for local and state governments, which is opposed by Republicans.

“Federal stimulus programs played a critical role in indirectly supporting state revenues, albeit still quite a bit less than we would have likely generated had it not been for the pandemic. As we move forward, we have not assumed additional federal assistance will be available due to the delay in its enactment, which is the main driver for the precipitous drop in revenues for fiscal year 2021,” said state Treasurer Rachael Eubanks.

In January, the state anticipated $24.94 billion of general fund and school aid revenues for fiscal 2020, $25.51 billion for fiscal 2021, and $26.16 billion for fiscal 2022. With sales and income tax tanking amid the state-mandated economic shutdown, forecasters warned during a May conference of a $3.23 billion revenue hit for fiscal 2020, a $3.05 blow in fiscal 2021, and a $2.09 billion decline in fiscal 2022.

On Monday, the group scaled back the projected gaps, trimming the 2020 gap to $926 million while warning of a $2.47 billion hole next year and a $1.71 billion gap in 2022 based the most recent economic projections and forecasting models.

The projections came during a special consensus revenue estimating conference called to provide fresh data as the state works on a budget for fiscal year beginning Oct. 1. The conference members include Eubanks, Kolb, Senate Fiscal Agency Director Chris Harkins and House Fiscal Agency Director Mary Ann Cleary.

Forecasters said some consumer spending patterns were surprising and while more clear now than in May much uncertainty looms and will depend on the case spikes, future potential economic shutdowns, and consumer reactions on spending.

"We are apprehensive and view those positive developments cautiously," said Treasury economist Eric Bussis.

Between April and July key economic indicators like payroll jobs declined but withholding actually increased by $130 million due to an “unprecedented” withholding on unemployment benefits. Sales taxes dropped $270 million or 9.6%.

“The May economic forecast was essentially on target, but fiscal year 2020 state revenue forecasts were significantly too low,” the forecast reads. Delayed payments for individual and corporate income taxes were stronger, which accounts for $200 million. Manufacturing and automotive production recovered more rapidly than expected and the impact of the CARES Act on revenue was underestimated while spending on taxable goods came in higher than expected.

“Consumer reaction to the pandemic increased collections, including shifts from nontaxable services and increases from remote sellers and marketplaces,” the report reads.

The CARES Act pumped nearly $43.3 billion into the Michigan economy during the second quarter through the Paycheck Protection Program, Economic Impact Payments and supplemental unemployment insurance benefits. That’s in addition to the $3.9 billion in direct state aid for pandemic related expenses the state received. About $800 million goes to eligible local governments.

While sales taxes were down from April to July, the numbers are not as bad as expected. Restaurants have recovered slightly since the early stages of the crisis and the spring months have seen strong growth at stores that sell building materials and garden supplies while sales tax from remote sellers accelerated after the pandemic.

“Risks surround how Michigan’s economy, population, and workforce recover from the recession,” the report warns.

Gov. Gretchen Whitmer and lawmakers previously agreed to a plan that relies on $350 million in reserve use and local government and education cuts and other measures to wipe out the projected fiscal 2020 gap so that eases the burden heading into fiscal 2021.

S&P Global Ratings recently moved its outlook on Michigan’s AA rating to negative.

"Our negative outlook also reflects difficult fiscal decisions ahead for Michigan as it deliberates the fiscal 2021 budget and beyond," said S&P analyst Ladunni Okolo in the report. S&P praises the state for using the latest period of expansion to build reserves so it’s “well positioned” with a strong cushion in the form of a

$1.15 billion reserve. The state also benefits from strong liquidity, including $6.7 billion in pooled cash.

Fitch Ratings rates the state AA with a stable outlook. Moody's Investors Service rates it Aa1 with a stable outlook.

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