The MISSOURI BUDGET PROJECT

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Adequately Funding State Services is a Critical Component of Restoring Missouri's Economy

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The current economic recession gripping the nation is at least partially responsible for generating significant state budget challenges in Missouri and 43 other states.[1] In December, 2008, Governor-Elect Nixon's office projected a $340 million shortfall in state funding in the current fiscal year. Based on existing data, the Missouri Budget Project further estimates that the size of the state's shortfall could grow to as much as $1 billion by fiscal year 2010, which begins on July 1, 2009.

At the same time, the demand for state services has increased. Missouri's unemployment rate, percent of families living in poverty and number of uninsured have all increased dramatically, particularly when compared to the last economic downturn of 2001. At this time of increased need, critical state services that support Missouri families during times of economic hardship, and that stimulate economic growth in our communities are at risk of being reduced due to the budget shortfall.

As discussed below, how Missouri lawmakers respond to the budget crunch will have a considerable impact on the state's economy. Adequate funding of state services is one of the most critical components of creating job growth in Missouri and stimulating the economy.

The Economic Impact of State Services:

A top priority for state lawmakers of both parties in the 2009 State Legislative Session, that began this past week, is creating sound public policy that will stimulate economic growth in Missouri and pull the state out of recession. Leading national economists agree that preventing cuts to state services during economic downturns is a critical component of Missouri's economic recovery.

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[1] National Budget Shortfall Estimates: *"State Budget Problems Worsen",* Center on Budget & Policy Priorities, *Updated* December 2008, Elizabeth McNichol and Iris Lav, available at www.cbpp.org.
For a more comprehensive discussion of the root of Missouri's Shortfall see, "*Missouri Faces a Critical Budget Cliff*", Missouri Budget Project, July 16, 2008, Amy Blouin, Tom Kruckemeyer & Ruth Ehresman http://www.mobudget.org/MO%20Structural%20Deficit%20Report%20final%20July%202008.pdf

Nobel Prize winning economist Joseph Stiglitz (of Columbia University) and Peter Orszag, director of the Congressional Budget Office, go farther to argue that "spending cuts could actually be more harmful for a state's economy during an economic downturn than tax increases".[2] Stiglitz and Orszag write:

> "Basic economic theory suggests that direct spending reductions will generate more adverse consequences for the economy in the short run than a tax increase …..For states interested in the impact only on their own economy rather than the national economy the arguments made are even stronger. In particular, government spending that would be reduced if direct spending programs are cut is often concentrated among local businesses".[3]

The economists argue that spending reductions would reduce demand in the local economy on at least a dollar for dollar basis. Some of the impact of increased taxes would result instead in reduced savings, and therefore result in a smaller decrease in economic consumption than spending reductions.

Data from the Missouri Economic Research and Information Center (MERIC) of the Missouri Department of Economic Development supports this theory as well. According to MERIC, the second largest contributor to the Missouri's Gross State Product in 2007 was government, which comprised 12.1 percent of the state's economy. Manufacturing resulted in 13.3 percent and real estate resulted in 10 percent of the gross state product in the same year.[4]

The Economic Output of State Services and Maximizing Federal Funds to the State Economy:

Business and civic leaders have also argued that funding for infrastructure, education and health care are critical components of Missouri's local economies. For example, state spending on transportation results in road construction projects, employing thousands of workers. Those workers utilize their incomes to support their families in the local economy, purchasing groceries and paying rent or mortgages, thus "multiplying" the impact of the funding further. In fact, the Missouri Department of Economic Development asserts that the Missouri Statewide Transportation Improvement Plan, implemented in FY 2006, alone supports more than 20,000 jobs per year, and yields an economic return of more than $2 for every dollar invested.[5]

Similarly, state funding for education, health care, child care assistance for low-wage workers and other Missouri services infuses money directly into the state's economy, resulting in the creation of jobs in our local communities at schools, hospitals and

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[2] *"Budget Cuts or Tax Increases at the State Level",* Center on Budget & Policy Priorities, *Updated* November 6, 2008, Nicholas Johnson, available at www.cbpp.org
[3] IBID
[4] MO Economic Research and Information Center of the Missouri Department of Economic Development http://www.missourieconomy.org/indicators/gsp/index.stm
[5] "Economic Impact Analysis for Missouri Statewide Transportation Improvement Plan", http://www.ded.mo.gov/researchandplanning/pdfs/econ_impact_stip.pdf

medical clinics and child care centers. In addition, these services help Missourians attain valuable skills for employment and enhance the ability of Missourians to remain employed in an ever-changing global market.

The Minnesota IMPLAN Group, LLC utilizes information from the bureau of economic analysis of the US Department of Labor to estimate the labor and income impact of state-only spending on services. The following chart indicates the "return" in Missouri in 2007 for each state dollar invested in services.

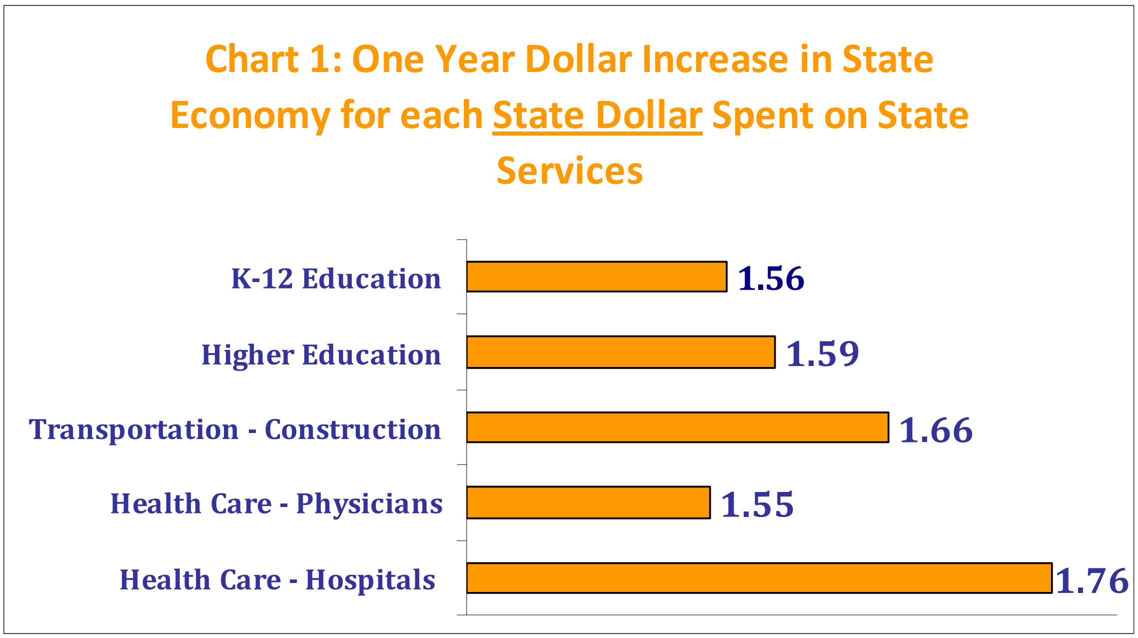

Chart Data Source: IMPLAN www.implan.com

State services that **also draw down federal funding** have even higher returns for Missouri's economy, because they bring in revenue that otherwise would not be available to the state. For example, for each $1 million in funding the state spends on Medicaid, the state receives approximately $1.574 million in federal funds. **The combined funding produces $3.062 million in economic activity in Missouri, or has a "multiplier effect" of 1.95.**[6]

The Counter-Cyclical Nature of State Services:

Several state and federal programs are also particularly crucial during recessions because in addition to providing an economic stimulus, they are designed to provide relief to families when the economy shrinks. Food Stamps, Health Care services including Medicaid and SCHIP (the State Children's Health Insurance Program), Unemployment Insurance Benefits, and TANF (Temporary Assistance for Needy Families) are "counter-

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6 *"The Economic & Health Benefits of Missouri Medicaid",* Missouri Foundation for Health, 2004, Joel Ferber, JD, Legal Services of Eastern Missouri, Inc., Economic Research by Heather L. Bednarek, PhD, Muhammad Q. Islam, PhD, St. Louis University available at www.mffh.org

cyclical" in design, meaning the demand for these services increases specifically when the economy shrinks.

Data from the U.S. Census Bureau indicate that the need for these services is even greater in Missouri today than it was during the last economic downturn:

- **Unemployment** in Missouri reached 6.7 percent in November 2008, much higher than the 4.2 percent rate Missouri had in 2001;
- The number of Missourians living in **poverty** increased to 742,000 people in 2007, a 12 percent increase over the 2006 level of 659,000;
- The number of Missourians accessing **Food Stamps** has doubled since the last economic crisis from 417,028 Missourians in 2000 to 899,322 in June of 2008;
- The number of Missourians who are **uninsured** grew by 3.5 percent since 2001, reaching 729,000 Missourians in 2007; and
- The **median income** in Missouri was $45,924 in 2007 when adjusted for inflation or approximately $5,000 lower than it was in 2001, the second highest decline in the nation.[7]

Cuts to these counter-cyclical services, particularly health care, at a time of increased demand could prolong or even deepen Missouri's recession and should be avoided. Not only do these services provided needed relief, they draw down federal funding, maximizing their benefit to Missouri families and the Missouri economy.

Conclusion:

Missouri faces an estimated state revenue shortfall equal to 3.8 percent of the state general revenue budget in the current year. The amount of the shortfall could grow to a gap of 11 percent by FY 2010. When closing the gap, State lawmakers should take all available options to avoid cuts to state services, particularly those services that have increased demand during an economic crisis. Protecting state services will not only assist Missouri families who are bearing the brunt of the recession, but will stimulate much needed economic growth.

The Mission of the Missouri Budget Project is to advance public policies that improve economic opportunities for all Missourians, particularly low and middle income families, by providing reliable and objective research, analysis and advocacy. Contact the MBP through our website at www.mobudget.org

[7] Poverty, Income and Health Insurance data is from the U.S. Census Bureau 2001 - 2007 data. Food Stamp usage data is from the Missouri Department of Social Services.