Forecast of GRF Revenues and Medicaid Expenditures for the FY 2014-FY 2015 Biennial Budget

Testimony before the Conference Committee on H.B. 59

June 13, 2013

Mr. Chairman and members of the Conference Committee, I am Mark Flanders, Director of the Legislative Service Commission (LSC). I am here to update you on LSC's forecasts for General Revenue Fund (GRF) revenues and Medicaid expenditures in fiscal years 2013 through 2015. My testimony will summarize the differences between our June and February forecasts and briefly explain our thinking about the economy. The attachment to my testimony provides more detail about the updated LSC forecasts and the economy. The forecasts are baseline forecasts, LSC's predictions for revenues and expenditures if current law were to remain unchanged throughout the next biennium.

Forecast Summary

Revenues

GRF tax revenue has generally been above estimate since February, such that LSC economists now project that FY 2013 GRF tax revenue will be about $336 million greater than we projected in February. We also now estimate that earnings on investments and license and fee revenue will be higher, adding an additional $25 million to GRF revenue this year, for a total increase in the estimate of about $361 million. The extra revenue that we expect to receive this year, however, is not matched by an increase in our forecasts for the upcoming biennium. The revised GRF tax revenue forecast is lower by $21.8 million (0.1%) in FY 2014, but higher by $11.5 million (0.1%) in FY 2015. Based on the updated forecast, GRF tax revenues are now forecast to increase from FY 2013 to FY 2014 by $170.7 million (0.8%) and by $1.05 billion (4.9%) from FY 2014 to FY 2015.

Medicaid

The revised LSC baseline forecast for Medicaid expenditures is $52 million ($19 million state share) lower in FY 2014, and $260 million ($96 million state share) lower in FY 2015. The forecast was lowered primarily to reflect changes in the projected caseload. The revised forecast includes several more months of Medicaid caseload data and also reflects Global Insight's updated forecast of unemployment projections for Ohio. The monthly caseload forecast for the Covered Families and Children (CFC) and Aged, Blind, and Disabled (ABD) groups was revised downward by about 5,400 and 7,400 in FY 2014 and 14,600 and 15,400 in FY 2015, respectively. However, the monthly caseload forecast for the All Other group was revised upward by about 38,200 in FY 2014 and 35,400 in FY 2015. As a result, the total monthly Medicaid caseload is now projected to be higher by about 25,500 in FY 2014 and 5,300 in FY 2015. While the total caseload is higher, Medicaid expenditures are projected to be lower, since ABD and CFC are more costly than the All Other group. The All Other group is the least costly among the three groups since Ohio Medicaid only pays for cost sharing or limited benefits for the individuals.

For FY 2013, the revised forecast is $130 million ($47 million state share) higher than what was forecasted in February. However, the revised forecast of total Medicaid expenditures for FY 2013 of $15.34 billion is still well below the originally estimated expenditures for the year of $16.01 billion.

The Economy

The relative lack of change in revenue forecasts for the upcoming biennium may seem surprising given recent positive experience with tax receipts. The forecast for the upcoming biennium depends heavily on an economic forecast, produced in May, from Global Insight, an economic forecasting firm. The forecast for May was not as optimistic as the forecast that they produced in January, which was the basis for the February forecast. Other factors, such as revisions to the effects of policy changes (related to Medicaid health insuring corporations) already enacted on revenue from the nonauto sales and use tax and the domestic insurance tax, served essentially to offset the effects of the more pessimistic economic forecast. A review of events since January might be helpful in assessing the less optimistic slant from the more recent forecast.

In their January forecast, Global Insight correctly anticipated that a deal would be reached to avoid hitting the federal government's debt limit in March, but they incorrectly anticipated that the federal sequester of funds would also be avoided, or at least that it would quickly be reversed. The federal sequester, involving a reduction of $85 billion in budget authority this federal fiscal year, actually went into effect March 1. Global Insight estimates that the reduction in budget authority corresponds to a $44 billion reduction in actual spending this year. So far, the effects of the sequester have been minimal, but they are expected to grow: for example, in coming months we will see the effects of furlough days on federal employees located in Ohio, which effects will show up in income tax withholding receipts. The sequester will also show up in terms of spending on goods produced by Ohio's defense contractors, for example General Electric in Evendale, and the Lima tank plant. The reductions will continue in future fiscal years while the sequester continues, but Global Insight's May forecast viewed it likely that the sequester will end by September 30, the end of the federal fiscal year.

Other events since January include the U.S. Bureau of Economic Analysis releasing an estimate of growth in inflation-adjusted, or "real," gross domestic product (GDP), that initially showed a decrease in the fourth quarter of 2012. The estimated decrease was subsequently revised upward, but only to growth of 0.4%; Global Insight had projected 1.0% growth that quarter. And in May, the Institute for Supply Management reported a slowdown in the national manufacturing sector, based on their surveys of purchasing managers; other economic sectors in the aggregate have continued to grow, according to the survey of purchasing managers in the non-manufacturing sector.

In spite of the generally solid performance of tax revenues since February, indicators such as these have influenced Global Insight to reduce their projections of key economic variables for Ohio, such as personal income and wage and salary disbursements.

Indeed, the strength of growth in state tax revenues has been difficult to reconcile with other economic indicators, some of which imply a recent slowing of economic growth in Ohio. In the year ending in April, employment in Ohio grew by just 4,400, or 0.1%, according to the U.S. Bureau of Labor Statistics and the Ohio Department of Job and Family Services. The unemployment rate has fluctuated between 7.0% and 7.1% since January, and the 21,300 reduction in the number of unemployed Ohio workers since April 2012 is due entirely to people leaving the labor force.

Global Insight's June forecast for Ohio is not yet available, so we have used their May forecast. The U.S. Executive Summary from that forecast is entitled *Another "Spring Swoon,"* reflecting their projections that U.S. economic growth will be weak for the current quarter and the next. That said, their summary early on states their view that "the underlying fundamentals of the private economy remain solid, and growth can be expected to accelerate in the second half of the year." That view is consistent with the views of Moody's economy.com and of the Governor's Council of Economic Advisors.

That does not mean that continued growth is a sure thing, of course. Forecasts are inherently uncertain, so it is all too possible that revenue during the FY 2014-FY 2015 biennium will be less than we are forecasting. In fact since May, Global Insight revised its prediction related to the end of the federal sequester, putting it at the end of calendar year 2013, rather than the end of the federal fiscal year. That would likely result in lower revenue than we forecast, at least for FY 2014. But of course, revenue could also be greater than we are projecting in the coming years.

Mr. Chairman and members of the Committee, thank you for the opportunity to present the LSC forecasts. My staff and I would be happy to answer any questions that you may have.

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ATTACHMENT: FY 2014-FY 2015 BIENNIAL BUDGET FORECAST

SECTION 1: REVENUE FORECASTS

The LSC baseline forecasts for FY 2014 and FY 2015 assume the current statutory tax structure, including tax changes enacted by the 129th General Assembly, in the budget bill for the current biennium, H.B. 153, and in other legislation, most notably H.B. 510 and H.B. 508. The newly created financial institutions tax (FIT), which will yield revenue for the first time in FY 2014, replaces the corporate franchise tax (CFT) and the dealers in intangibles tax (DIT) which will both be eliminated at the end of 2013.

Under permanent law, a portion of GRF tax receipts is transferred to the Local Government Fund (LGF) and the Public Library Fund (PLF). The Tax Commissioner is required to determine, by July 5, 2013, the ratio of FY 2013 transfers to the respective funds to total FY 2013 GRF tax revenues. Transfers to the LGF and the PLF will be based on those respective ratios beginning in FY 2014. Based on experience through May, LSC economists project that both the LGF and the PLF will begin to receive 1.66% of GRF tax revenue in FY 2014.

GRF tax revenue has generally been above estimate since February, such that LSC economists now project that FY 2013 GRF tax revenue will be about $336 million greater than they projected in February. They also now estimate that earnings on investments and license and fee revenue will be higher, adding an additional $25 million to GRF revenue this year, for a total increase in the estimate of about $361 million.

GRF tax revenue under current law is forecast to increase by $170.7 million (0.8%) in FY 2014. The weak growth is due to a projected (slight) decrease in personal income tax revenue, due to one-time factors having increased revenue during the current fiscal year, and having pulled forward some revenue from future years. Other factors behind the weak growth include a good year this year for the CFT and for the DIT, which are both being phased out. They are to be replaced by the FIT. We have no experience of this tax, so LSC economists have relied in substantial part on forecasts of tax revenue done by the Department of Taxation when the changes made by H.B. 510 were introduced. Growth is expected for most tax revenue sources that are continuing, as the economic recovery is expected to continue. The cigarette and other tobacco products tax is a notable exception, as it is expected to continue its steady decline. A projected decline in kilowatt hour tax revenue is due to the growing share of PLF receipts, half of which are debited against this tax, which is forecast to more than offset a small increase in its tax base. The slight decrease in commercial activity tax (CAT) receipts in FY 2014 results from an exclusion of tax revenues from motor fuel sales due to a recent Ohio Supreme Court decision.[1] The estate tax, which ended for deaths after December 31, 2012, is projected to yield GRF tax receipts in FY 2014, but all estates are assumed in this forecast to be settled, and any related payments made, prior to FY 2015. The baseline forecast also includes additional sales and use tax and insurance tax receipts from a delayed implementation of certain Medicaid-related changes included in current law. LSC also forecasts revenue from earnings on investments and from license fees, which are projected to total $86.7 million in FY 2014.

GRF tax revenue under current law is forecast to increase by $1.05 billion (4.9%) in FY 2015. Growth in revenue from the personal income tax and the sales and use tax, the two largest GRF tax sources, is projected to be fairly robust. Revenue from the CAT and the FIT is also expected to show solid growth, and the domestic insurance tax is anticipated to have sizable revenue growth, attributable mostly to increased enrollments in Medicaid health insuring corporations. Except for declining receipts for the tax on cigarettes and other tobacco products, the public utility excise tax, and the kilowatt hour excise tax, the remaining taxes are expected to exhibit smaller rates of revenue growth; as noted above, no revenue from the estate tax is expected in FY 2015. Earnings on investments and license revenue are forecast to total $94.0 million in FY 2015.

Table 1, below, provides an overview of aggregate GRF receipts from taxes, and Table 2 on the following page shows forecasts of receipts by tax, and from state sources including earnings on investments and receipts from charges for licenses and fees. Tables 3 and 4 compare LSC February and June forecasts for FY 2013 through FY 2015.

Table 1: Total GRF Tax Revenue Growth, FY 2009-FY 2015

	FY 2009 Actual	FY 2010 Actual	FY 2011 Actual	FY 2012 Actual	FY 2013 Estimate	FY 2014 Forecast	FY 2015 Forecast
Revenue	$17,093.8	$16,233.6	$17,706.2	$19,005.2	$21,047.6	$21,218.3	$22,264.2
Growth	-12.0%	-5.0%	9.1%	7.3%	10.7%	0.8%	4.9%

[1] On December 7, 2012, the Supreme Court of Ohio ruled that imposing the CAT on gross receipts from the sale of motor vehicle fuel and allocating the revenues to the GRF is unconstitutional. The Court precluded such allocations of those revenues after the date of the decision.

Table 2: LSC Baseline Revenue Forecasts, FY 2014-FY 2015
($ in millions)

GRF	FY 2012 Actuals	FY 2013 Estimates	Growth Rate	FY 2014 June Forecast	Growth Rate	FY 2015 June Forecast	Growth Rate
TAX REVENUE							
Auto Sales & Use	$1,053.5	$1,098.0	4.2%	$1,138.3	3.7%	$1,177.8	3.5%
Nonauto Sales & Use	$7,033.5	$7,347.4	4.5%	$7,700.1	4.8%	$8,216.5	6.7%
Total Sales & Use	$8,087.0	$8,445.4	4.4%	$8,838.4	4.7%	$9,394.3	6.3%
Personal Income	$8,432.9	$9,526.3	13.0%	$9,504.5	-0.2%	$9,959.3	4.8%
Commercial Activity	$417.1	$789.7	89.3%	$782.1	-1.0%	$814.2	4.1%
Corporate Franchise	$117.1	$277.0	136.6%	$0.0	-100.0%	$0.0	--
Financial Institutions	$0.0	$0.0	--	$200.0	--	$209.0	4.5%
Public Utility	$113.9	$96.7	-15.1%	$102.1	5.6%	$98.1	-3.9%
Kilowatt Hour Excise	$294.8	$302.0	2.4%	$296.5	-1.8%	$294.2	-0.8%
Natural Gas Consumption	$60.2	$60.0	-0.3%	$64.0	6.7%	$66.0	3.1%
Foreign Insurance	$266.5	$276.0	3.6%	$286.0	3.6%	$296.0	3.5%
Domestic Insurance	$189.1	$207.7	9.9%	$209.0	0.6%	$238.0	13.9%
Business & Property	$19.9	$35.0	76.1%	$0.0	-100.0%	$0.0	--
Cigarette	$843.2	$830.0	-1.6%	$811.0	-2.3%	$792.0	-2.3%
Alcoholic Beverage	$57.6	$58.3	1.2%	$60.7	4.1%	$61.0	0.5%
Liquor Gallonage	$39.4	$40.5	2.7%	$41.0	1.2%	$42.0	2.4%
Estate	$66.5	$103.0	54.8%	$23.0	-77.7%	$0.0	-100.0%
Total Tax Revenue	**$19,005.2**	**$21,047.6**	**10.7%**	**$21,218.3**	**0.8%**	**$22,264.2**	**4.9%**
NONTAX STATE-SOURCE REVENUE							
Earnings on Investments	$5.4	$8.9	64.3%	$14.1	58.4%	$18.4	30.5%
Licenses and Fees	$65.3	$70.4	7.8%	$72.6	3.1%	$75.6	4.1%

Table 3: FY 2013 Revenue Estimate Comparison
($ in millions)

GRF	February 2013	June 2013	Change
TAX REVENUE			
Auto Sales & Use	$1,080.6	$1,098.0	$17.4
Nonauto Sales & Use	$7,315.4	$7,347.4	$32.0
Total Sales & Use	$8,396.0	$8,445.4	$49.4
Personal Income	$9,263.1	$9,526.3	$263.2
Commercial Activity	$842.7	$789.7	($53.0)
Corporate Franchise	$201.7	$277.0	$75.3
Financial Institutions	$0.0	$0.0	$0.0
Public Utility	$116.4	$96.7	($19.7)
Kilowatt Hour Excise	$298.9	$302.0	$3.1
Natural Gas Consumption	$58.3	$60.0	$1.7
Foreign Insurance	$279.0	$276.0	($3.0)
Domestic Insurance	$206.0	$207.7	$1.7
Business & Property	$25.0	$35.0	$10.0
Cigarette	$820.8	$830.0	$9.2
Alcoholic Beverage	$58.3	$58.3	$0
Liquor Gallonage	$40.1	$40.5	$0.4
Estate	$105.6	$103.0	($2.6)
Total Tax Revenue	**$20,711.8**	**$21,047.6**	**$335.8**
NONTAX STATE-SOURCE REVENUE			
Earnings on Investments	$7.5	$8.9	$1.4
Licenses and Fees	$47.0	$70.4	$23.4

Table 4: Baseline Revenue Forecast Comparison, FY 2014-FY 2015
($ in millions)

	FY 2014			FY 2015		
GRF	**February 2013**	**June 2013**	**Change**	**February 2013**	**June 2013**	**Change**
TAX REVENUE						
Auto Sales & Use	$1,128.0	$1,138.3	$10.3	$1,179.0	$1,177.8	($1.2)
Nonauto Sales & Use*	$7,769.7	$7,700.1	($69.6)	$8,180.3	$8,216.5	$36.2
Total Sales & Use	$8,897.7	$8,838.4	($59.3)	$9,359.3	$9,394.3	$35.0
Personal Income	$9,448.7	$9,504.5	$55.9	$9,952.5	$9,959.3	$6.8
Commercial Activity	$793.8	$782.1	($11.7)	$826.9	$814.2	($12.7)
Corporate Franchise	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0
Financial Institutions	$200.0	$200.0	$0.0	$209.0	$209.0	$0.0
Public Utility	$125.6	$102.1	($23.5)	$138.6	$98.1	($40.5)
Kilowatt Hour Excise	$289.2	$296.5	$7.3	$282.4	$294.2	$11.8
Natural Gas Consumption	$60.4	$64.0	$3.6	$62.4	$66.0	$3.6
Foreign Insurance	$288.0	$286.0	($2.0)	$299.0	$296.0	($3.0)
Domestic Insurance*	$212.9	$209.0	($3.9)	$241.4	$238.0	($3.4)
Business & Property	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0
Cigarette	$799.2	$811.0	$11.8	$778.3	$792.0	$13.7
Alcoholic Beverage	$60.7	$60.7	$0.0	$61.0	$61.0	$0
Liquor Gallonage	$41.0	$41.0	$0.0	$41.9	$42.0	$0.1
Estate	$23.0	$23.0	$0.0	$0.0	$0.0	$0.0
Total Tax Revenue	**$21,240.2**	**$21,218.3**	**($21.8)**	**$22,252.6**	**$22,264.2**	**$11.5**
NONTAX STATE-SOURCE REVENUE						
Earnings on Investments	$8.4	$14.1	$5.7	$11.3	$18.4	$7.1
Licenses and Fees	$48.6	$72.6	$24.0	$50.5	$75.6	$25.1

*February forecast figures shown for the nonauto sales and use tax and for the domestic insurance tax have been adjusted to remove receipts from policy changes that were inadvertently included in the numbers in February.

SECTION 2: MEDICAID EXPENDITURE FORECASTS

The revised LSC baseline forecast for Medicaid expenditures is lower by $52 million ($19 million state share) in FY 2014 and $260 million ($96 million state share) in FY 2015, than was forecasted in February. The forecast was lowered for FY 2014 and FY 2015 primarily to reflect changes in the projected caseload. For FY 2013, the revised forecast is $130 million ($47 million state share) higher than what was forecasted in February. However, the revised forecast of total Medicaid expenditures of $15.34 billion is still well below the estimated expenditures of $16.01 billion.

The Medicaid caseload is generally divided into three groups: (1) Covered Families and Children (CFC), which includes children up to age 19 with family income up to 200% of the federal poverty guideline (FPG), pregnant women with income up to 200% of FPG, and parents with income up to 90% of FPG, (2) Aged, Blind, and Disabled (ABD), which includes the elderly and persons with disabilities of all ages with income up to 64% of FPG, and (3) All Other, which includes individuals such as Medicare beneficiaries whose Medicare premiums, deductibles, and coinsurance are paid by Medicaid, or men and women of any age who are under 200% of FPG receiving family planning and related services.

The monthly caseload forecast for CFC and ABD was revised downward by about 5,400 and 7,400 in FY 2014 and 14,600 and 15,400 in FY 2015, respectively. However, the monthly caseload forecast for the All Other group was revised upward by about 38,200 in FY 2014 and 35,400 in FY 2015. As a result, the total Medicaid caseload is now projected to be higher by about 25,500 in FY 2014 and 5,300 in FY 2015. While the total caseload is higher, Medicaid expenditures are estimated to be lower, since ABD and CFC are more costly than the All Other group. The All Other group is the least costly among the three groups since Ohio Medicaid only pays for their cost sharing or limited benefits.

The revised forecast includes several more months of Medicaid caseload data. For the months of December 2012 through April 2013, CFC and ABD caseloads were lower, on average, by 1,300 and 17,900 per month, respectively. However, during the same period, the All Other caseload was, on average, 7,700 higher per month. In addition, the revised caseload reflects Global Insight's updated forecast of unemployment projections for Ohio. They have increased their projection of the number of unemployed for each quarter during FY 2014 by about 9,000, but have decreased the number for each quarter during 2015 by about 1,000. Four tables at the end of this section detail changes in Medicaid caseload forecasts.

The LSC June baseline expenditure forecast does not include adjustments to items that were part of the February forecast such as the woodwork effect and the physician rate increase as a result of the federal Patient Protection and Affordable Care Act, Health Homes, and the Integrated Care Delivery System. The estimated costs of these items were provided by the Office of Medical Assistance (OMA) and added to LSC's baseline forecast in February. To derive the total estimated Medicaid expenditures for FY 2014 and FY 2015, updated adjustments from OMA will need to be added to the baseline forecast.

Total Medicaid Caseload

	FY 2009 Actual	FY 2010 Actual	FY 2011 Actual	FY 2012 Actual	FY 2013 Estimate	FY 2014 Forecast	FY 2015 Forecast
						February	
Caseload	1,886,843	2,046,072	2,157,607	2,215,915	2,365,545	2,355,105	2,373,789
Growth		8.44%	5.45%	2.7%	6.75%	-0.44%	0.79%
						June	
Caseload	1,886,843	2,046,072	2,157,607	2,215,915	2,379,307	2,380,581	2,379,106
Growth		8.44%	5.45%	2.7%	7.37%	0.05%	-0.06%
						Difference	
					13,762	25,476	5,317
					0.58%	1.07%	0.22%

CFC Medicaid Caseload

	FY 2009 Actual	FY 2010 Actual	FY 2011 Actual	FY 2012 Actual	FY 2013 Estimate	FY 2014 Forecast	FY 2015 Forecast
						February	
Caseload	1,409,641	1,549,040	1,631,408	1,662,607	1,717,770	1,684,802	1,678,743
Growth		9.89%	5.32%	1.91%	3.32%	-1.92%	-0.36%
						June	
Caseload	1,409,641	1,549,040	1,631,408	1,662,607	1,718,537	1,679,399	1,664,120
Growth		9.89%	5.32%	1.91%	3.36%	-2.28%	-0.91%
						Difference	
					766	-5,403	-14,623
					0.04%	-0.32%	-0.88%

ABD Medicaid Caseload

	FY 2009 Actual	FY 2010 Actual	FY 2011 Actual	FY 2012 Actual	FY 2013 Estimate	FY 2014 Forecast	FY 2015 Forecast
						February	
Caseload	384,256	398,593	415,635	422,565	420,572	442,084	459,461
Growth		2.5%	2.2%	4.2%	-0.47%	5.11%	3.93%
						June	
Caseload	384,256	398,593	415,635	422,565	412,795	434,716	444,032
Growth		2.5%	2.2%	4.2%	-2.31%	5.31%	2.14%
						Difference	
					-7,777	-7,368	-15,429
					-1.88%	-1.69%	-3.47%

All Other Medicaid Caseload

	FY 2009 Actual	FY 2010 Actual	FY 2011 Actual	FY 2012 Actual	FY 2013 Estimate	FY 2014 Forecast	FY 2015 Forecast
						February	
Caseload	92,946	98,439	110,563	130,744	227,202	228,219	235,585
Growth		5.91%	12.32%	18.25%	73.78%	0.45%	3.23%
						June	
Caseload	92,946	98,439	110,563	130,744	247,975	266,466	270,954
Growth		5.91%	12.32%	18.25%	89.66%	7.46%	1.68%
						Difference	
					20,713	38,247	35,369
					8.38%	14.35%	13.05%

SECTION 3: ECONOMIC CONDITIONS AND OUTLOOK

State of the Economy

Expansion in U.S. and Ohio economic activity has been underway since 2009, when the last recession ended. Further growth is predicted for both the nation and the state, as summarized in the economic forecast tables below. Overall economic growth has been slow compared with most past recoveries, and unemployment has come down gradually but remains elevated. Nationwide employment has increased, though has not yet reached its pre-recession peak in January 2008. Consumer spending and incomes have been rising. Household debt and payment obligations have been reduced to more manageable levels relative to incomes. Unmet replacement needs are adding to spending on vehicles and other durables. Housing sales and construction are recovering, though activity remains below past peaks. Mortgage rates have been low. Business capital spending has continued to expand in most quarters. Inflation for most finished goods and services is low, though up from even lower rates in 2009 and 2010.

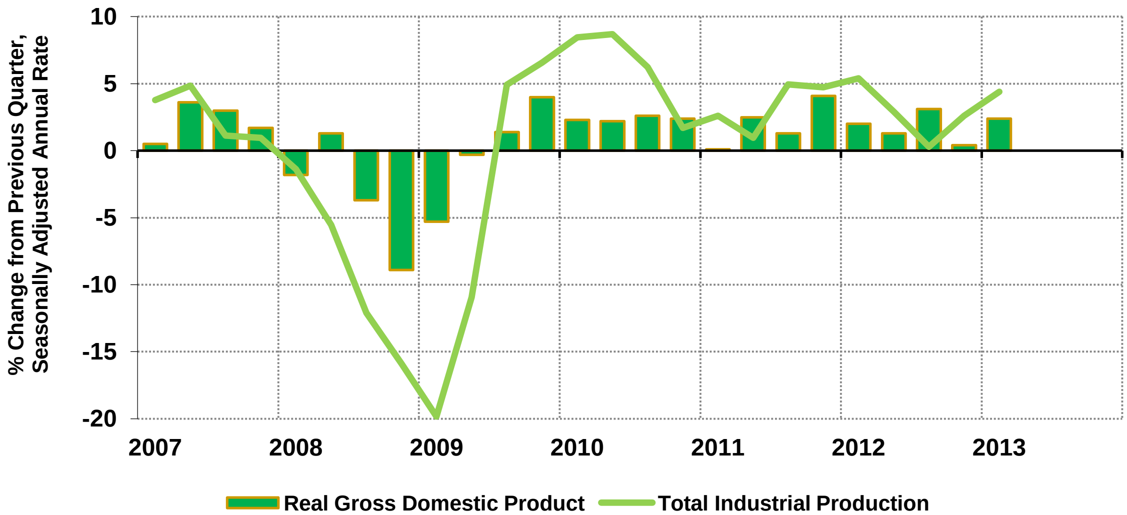
Several developments could adversely affect economic growth later in the year. Global Insight, and a number of other economic forecasters expect that the impacts of sequestration, under which the federal government is reducing spending by about $85 billion from March through September, could lower economic growth rates in the second and third quarters. Though Congress suspended the national debt ceiling in January, allowing the U.S. Treasury to continue to borrow (for purposes other than refinancing bonds previously issued), the debt ceiling could become an issue again later in the year. International economic issues, such as high unemployment and a recession in the Eurozone, slower than expected economic growth in China, and oil price volatility could also slow future growth.

In May, the Federal Open Market Committee of the Federal Reserve indicated it will continue its policy of monetary expansion through purchasing $85 billion in Treasury and mortgage bonds each month in order to help lower borrowing costs, until the national unemployment rate falls to 6.5%, as long as expected inflation is no more than half a percentage point above the 2.0% goal.

National

Growth of the national economy is continuing, but the expansion remains the slowest of the post-World War II period, averaging only a 2.1% annual rate since the 2007-2009 recession. Inflation-adjusted gross domestic product (real GDP), the total output of the economy, reached a new all-time peak at the end of 2011 and rose further in 2012 and early this year. In this year's first quarter, real GDP increased at an annual rate of 2.4%, based on the second estimate released by the U.S. Bureau of Economic Analysis (BEA). Other broad measures of U.S. economic activity, including industrial production, have not yet recovered to their peaks prior to the last recession. Chart 1 shows changes in real GDP and industrial production through the first quarter of this year.

Chart 1: United States Output Measures



Consumer spending, the largest portion of GDP, has grown since the recession trough in the second quarter of 2009, but growth has been slow, partially due to the slow recovery in employment. Since its post-recession low, employment has risen but has not yet reached its previous peak. With rising employment, unemployment has come down gradually: the national unemployment rate decreased in May to 7.6% of the labor force from 7.9% in January. Though employment growth has been slow, other impediments to consumer spending are easing. Incomes of consumers have been supported by increases in average hours worked by those employed. Households have paid down past borrowings and reduced debt service ratios to more manageable levels. Credit availability has eased somewhat, as indicated by surveys. Replacement needs are contributing to increased spending on consumer durable goods. U.S. sales of cars and light trucks in 2012 were at the highest rate in five years, and sales during the first five months of 2013 were 7% higher than during the corresponding months of 2012.

Housing markets are also recovering, though activity remains well below past peaks. In the first four months of this year, construction starts on new housing units were at the highest level since the comparable period in 2008. The upturn was strongest in apartment construction. Sales of new and older homes have increased; though, sales of existing homes have been restrained recently due to low inventories. Housing prices hit bottom in 2011 and have trended upward since, but generally remain below past peaks. Conditions vary widely among local markets.

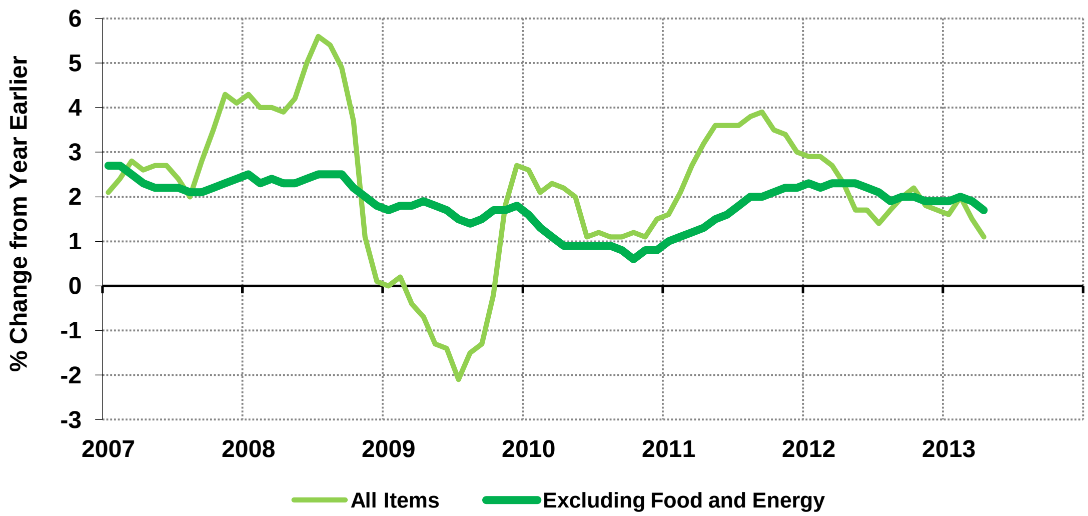
Business investment in equipment and software grew vigorously after the end of the last recession, surpassing pre-recession levels, but increased more slowly last year and in the beginning of this year. In contrast, business investment in structures remained weak following the recession and remains below pre-recession levels.

Inventory rebuilding contributed significantly to production growth during the first year of the economy's recovery, but has generally been less of a factor since then.

Export growth added substantially to demand for U.S. goods and services earlier in the economic recovery but has lagged in recent quarters. Recession in Europe and slower growth in less developed economies restrained growth of American exports last year. U.S. imports from abroad also grew rapidly early in the recovery but have slowed since then.

With significant productive resources still idle, including unemployed labor resources and equipment, inflation for finished goods and services remains low, overall, though up compared with even lower rates in 2010 and with deflation in 2009 (mainly reflecting falling energy prices). Wage inflation is also low. Recent trends in consumer prices for all items and excluding food and energy, which tend to be more volatile, are shown in Chart 2.

Chart 2: Consumer Price Index



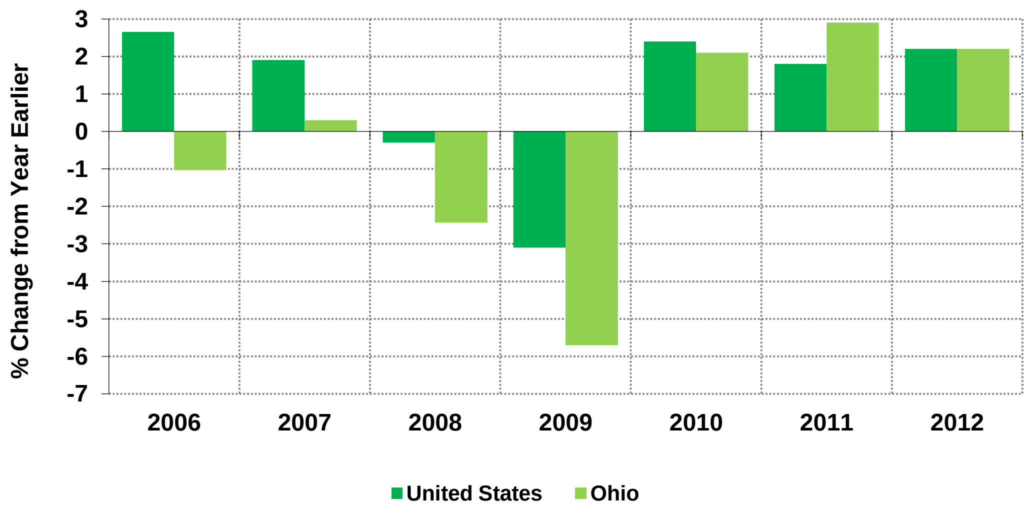
Because unemployment is still high and inflation at the finished goods level has remained low, U.S. monetary policy has held short-term interest rates at very low levels. In addition to keeping its target short-term interest rate, the federal funds rate, in a range of 0% to 0.25%, the Federal Reserve System has been buying U.S. Treasury notes and bonds and federal agency mortgage-backed securities to keep longer-term interest rates low. The central bankers expect to keep the federal funds rate target in this low range at least until the national unemployment rate falls to 6.5%, provided that inflation expectations remain low. Market interest rates remain at exceptionally low levels, but longer-term rates have been edging up in recent months.

Ohio

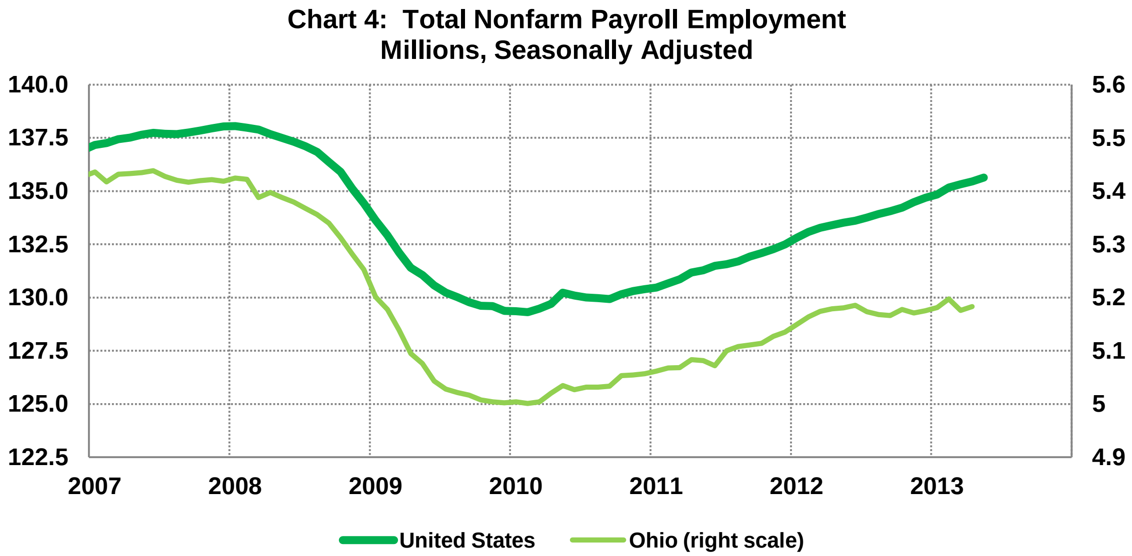
Since the mid-1960s, GDP has risen more slowly in Ohio than nationwide in most years and the state's share of the nation's output has trended lower since then. The 2007-2009 recession was more severe in Ohio, as state real GDP fell 5.7% in 2009 compared with a 3.1% decline in U.S. real GDP (state real GDP also fell more sharply in 2008). Recovery in Ohio initially appeared slightly weaker, with state real GDP increasing 2.1% in 2010 in comparison with U.S. real GDP growth of 2.4%. But growth in Ohio improved relative to the nation in 2011. In 2012, based on initial estimates, Ohio real GDP grew at the same pace as U.S. GDP.

Chart 3 shows annual changes in real GDP in Ohio compared with the U.S. These numbers were updated by the BEA on June 6, based on more complete and detailed information, and therefore differ from numbers reported in LSC's Forecast Book published February 5, 2013. BEA's initial estimate of 2012 Ohio GDP (shown in the chart) will be revised next year when more complete data becomes available.

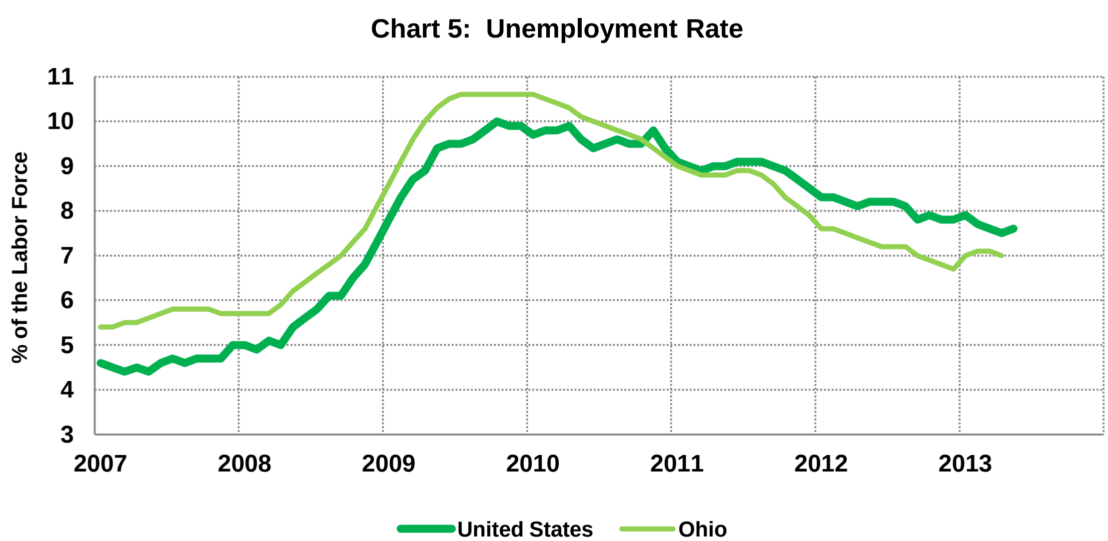
Chart 3: Real Gross Domestic Product



Ohio nonfarm payroll employment reached a low point in February 2010, and since then has recovered by about 182,200 jobs (3.6%) in the three years and two months since then. However, most of that growth occurred in 2010, 2011, and the first few months of 2012; in the past 12 months (April 2012 to April 2013), employment in Ohio has grown by 4,400 jobs (0.1%). U.S. nonfarm payroll employment reached its low point in February 2010, and through May 2013 had risen by 6.3 million jobs (4.9%). In both Ohio and the U.S., total nonfarm payroll employment remains below levels prior to the 2007-2009 recession. Nonfarm payroll employment in Ohio, compared with that in the U.S., is shown in Chart 4.

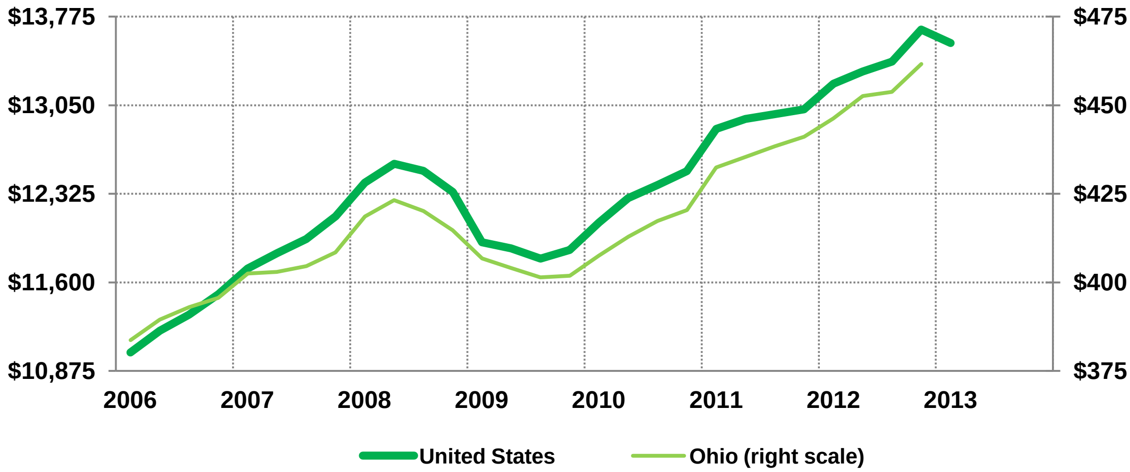


Though employment in this state has grown more slowly than the nation, Ohio's unemployment rate has been lower than the nationwide average since November 2010. Ohio's statewide unemployment rate, the number of people not employed and actively seeking work as a percent of the labor force, declined to 6.7% in December, its lowest level since 2008. In April, Ohio's unemployment rate was 7.0% compared to the U.S. rate of 7.5%. The unemployment rate in Ohio, compared with that in the U.S., is shown in Chart 5.



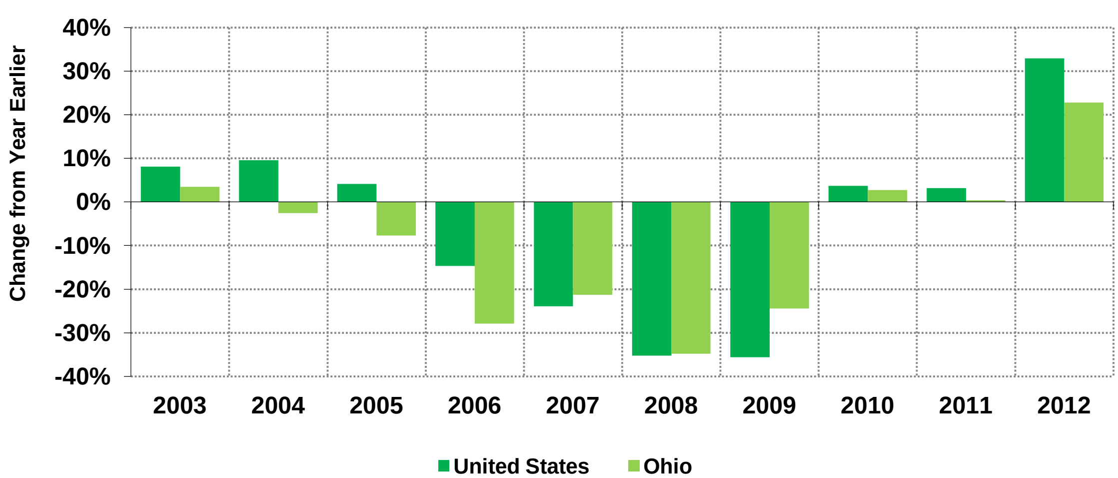
Personal income has been growing in the nation and in Ohio since 2009. From the low point in the third quarter of 2009 to the fourth quarter of 2012, Ohio personal income rose 15%, while U.S. personal income rose about 16%. U.S. personal income fell in the first quarter of 2013, due to one-time factors such as the expiration of the payroll tax cut for employees and the high level of bonuses provided to employees in late 2012. Personal income levels in Ohio and in the U.S. are shown in Chart 6. Both series are shown in dollars of current purchasing power (i.e., with no inflation adjustment). Data on personal income in Ohio in the first quarter of 2013 is not yet available.

Chart 6: Personal Income
Billions of Dollars



Housing construction recovered substantially last year, in Ohio and the nation, as indicated by construction permits for new privately owned units, shown in Chart 7. Nationwide residential building activity is up more sharply than in Ohio. Previously, housing construction activity fell in Ohio for six years through 2009, then edged up in 2010 and 2011. U.S. housing construction fell for four years, from a 2005 peak, and also increased modestly in 2010 and 2011. Residential building activity remains far below past peaks, in Ohio and around the country. Average housing prices have been recovering since 2011, in Ohio and the U.S., after falling from peaks in 2006 and 2007.[2]

Chart 7: New Privately Owned Housing Units
Authorized by Building Permits



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[2] Prices cited here are as reported by the Federal Housing Finance Agency.

Economic Forecasts

The predictions for the economic outlook in the tables that follow are from Global Insight's baseline forecasts released in May 2013. Economic forecasting is inherently uncertain, and projections may turn out to be too optimistic or too pessimistic. LSC's forecasts for state tax revenues, based in part on some of the variables provided by Global Insight, could in consequence also be either too high or too low.

Quarterly changes shown, (the first line in each table except for the unemployment rate tables) are from the preceding quarter. Changes shown in the second line compare average values for the four quarters ending in the second calendar quarter, coinciding with Ohio's fiscal year, with average values for the four quarters one year earlier. The unemployment rate tables show average unemployment rates for the quarters indicated (first line) and for the four quarters ending in the second quarter (second line).

U.S. Gross Domestic Product

Real GDP growth is projected to increase gradually into FY 2014, then rise somewhat more rapidly in FY 2015. Since the recession trough in the second quarter of 2009, through last year's fourth quarter, real GDP growth averaged a 2.1% annual rate.

U.S. Real GDP Growth

	2013				2014				2015			
Forecast	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
	percent change at annual rate											
Global Insight	2.5	1.4	1.8	3.0	3.1	3.2	2.9	3.0	3.3	3.4	3.4	3.0
Global Insight		2.0				2.2				3.1		

Ohio Gross Domestic Product

Economic growth in Ohio is expected to continue through 2015 but at a subdued pace. Predicted growth of real GDP in Ohio averages 1.9% in FY 2014 and FY 2015.

Ohio Real GDP Growth

	2013				2014				2015			
Forecast	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
	percent change at annual rate											
Global Insight	0.4	0.3	1.3	2.8	2.4	2.2	1.9	2.3	2.7	2.8	2.7	2.3
Global Insight		1.9				1.4				2.3		

U.S. Inflation

In Global Insight's May baseline forecast, consumer price inflation remains at a 2.0% annual rate or less, except for one quarter, through 2015.

U.S. Consumer Price Index Inflation

	2013				2014				2015			
Forecast	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
	percent change at annual rate											
Global Insight	1.4	-0.5	2.2	1.6	1.8	1.8	1.6	1.5	1.9	1.7	1.6	1.7
Global Insight		1.6				1.4				1.7		

U.S. Personal Income

Nationwide personal income growth is projected to average 4.5% at an annual rate in FY 2014 and FY 2015. These growth rates are based on the dollar amounts of income, not adjusted for inflation. Weakness shown in the table for the prior quarter reflects the end of the two percentage point reduction in the individual portion of Social Security taxes, which is subtracted in the national income and product accounts in calculating personal income.

U.S. Personal Income Growth

	2013				2014				2015			
Forecast	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
	percent change at annual rate											
Global Insight	-3.2	3.7	4.1	5.3	6.5	4.7	4.6	4.4	5.8	4.6	4.4	4.3
Global Insight		3.4				3.9				5.0		

Ohio Personal Income

Personal income growth in Ohio is also forecasted to grow through 2015, except for the first quarter of 2013 when the end of the temporary reduction in Social Security taxes results in lower total personal income. Growth of Ohio personal income averages 3.9% at an annual rate in FY 2014 and FY 2015, lagging behind growth of personal income nationwide.

Ohio Personal Income Growth

	2013				2014				2015			
Forecast	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
	percent change at annual rate											
Global Insight	-2.6	2.7	3.5	4.5	5.8	4.0	3.9	3.7	5.4	3.8	3.6	3.5
Global Insight		3.2				3.3				4.4		

U.S. Unemployment Rate

Unemployment nationwide is expected to decline slowly through the forecast period shown in the table. As job opportunities continue gradually to improve, additional entrants to the labor force are likely to be attracted, which will slow the decline in the unemployment rate.

U.S. Unemployment Rate

	2013				2014				2015			
Forecast	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
	percent of the labor force											
Global Insight	7.7	7.6	7.6	7.5	7.4	7.2	7.1	7.0	6.8	6.6	6.5	6.3
Global Insight		7.8				7.4				6.9		

Ohio Unemployment Rate

The unemployment rate in Ohio is projected to fall slowly through the end of 2015. The state's unemployment rate is forecasted to remain below that of the nation, until late 2015.

Ohio Unemployment Rate

	2013				2014				2015			
Forecast	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
	percent of the labor force											
Global Insight	7.0	7.0	7.0	6.9	6.8	6.7	6.6	6.6	6.5	6.5	6.4	6.3
Global Insight		7.0				6.9				6.5		