Budget Footnotes

A NEWSLETTER OF THE OHIO LEGISLATIVE SERVICE COMMISSION FEBRUARY 2017

STATUS OF THE GRF

HIGHLIGHTS

– Ross A. Miller, Chief Economist, 614-644-7768

The Governor unveiled the executive budget for the upcoming biennium on January 30. The total FY 2017 GRF tax revenue and program expenditure estimates that accompanied the proposal were revised downward, by about $592 million and $825 million, respectively, from the estimates made by the Office of Budget and Management (OBM) in August 2016. The downward revisions are consistent with revenue and expenditure experiences through the first seven months of FY 2017. The variance analyses in this and future issues of *Budget Footnotes* will continue to be based on the August estimates as OBM did not revise its monthly estimates for the remainder of FY 2017.

Through January 2017, GRF sources totaled $20.00 billion:

- Revenue from the personal income tax was $275.3 million below estimate;
- Sales and use tax receipts were $120.2 million below estimate.

Through January 2017, GRF uses totaled $20.95 billion:

- Program expenditures were $782.7 million below estimate, due primarily to Medicaid ($699.0 million);
- Negative variances in other spending categories were partly offset by a $41.9 million positive variance in primary and secondary education.

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STATUS OF THE GRF

ISSUE UPDATES

TRACKING THE ECONOMY

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Table 1: General Revenue Fund Sources
Actual vs. Estimate
Month of January 2017
($ in thousands)
(Actual based on report run in OAKS Actuals Ledger on February 1, 2017)

STATE SOURCES	Actual	Estimate*	Variance	Percent
TAX REVENUE				
Auto Sales	$102,491	$105,300	-$2,809	-2.7%
Nonauto Sales and Use	$888,075	$900,600	-$12,525	-1.4%
Total Sales and Use Taxes	**$990,566**	**$1,005,900**	**-$15,334**	**-1.5%**
Personal Income	$845,851	$938,200	-$92,349	-9.8%
Corporate Franchise	$143	$0	$143	---
Financial Institution	$53,791	$51,100	$2,691	5.3%
Public Utility	$66	-$100	$166	166.4%
Kilowatt-Hour Excise	$28,679	$28,500	$179	0.6%
Natural Gas Consumption (MCF)	$1,576	$1,700	-$124	-7.3%
Commercial Activity Tax	$52,002	$47,300	$4,702	9.9%
Petroleum Activity Tax	$0	$0	$0	---
Foreign Insurance	$1,709	$100	$1,609	1608.6%
Domestic Insurance	$0	$0	$0	---
Business and Property	$0	$0	$0	---
Cigarette	$77,464	$71,400	$6,064	8.5%
Alcoholic Beverage	$4,295	$3,800	$495	13.0%
Liquor Gallonage	$4,862	$4,700	$162	3.4%
Estate	$33	$0	$33	---
Total Tax Revenue	**$2,061,037**	**$2,152,600**	**-$91,563**	**-4.3%**
NONTAX REVENUE				
Earnings on Investments	$9,868	$8,700	$1,168	13.4%
Licenses and Fees	$2,938	$2,850	$88	3.1%
Other Revenue	$601	$4,230	-$3,629	-85.8%
Total Nontax Revenue	**$13,406**	**$15,780**	**-$2,374**	**-15.0%**
TRANSFERS				
Budget Stabilization	$0	$0	$0	---
Other Transfers In	$60,085	$9,500	$50,585	532.5%
Total Transfers In	**$60,085**	**$9,500**	**$50,585**	**532.5%**
TOTAL STATE SOURCES	**$2,134,528**	**$2,177,880**	**-$43,352**	**-2.0%**
Federal Grants	$781,119	$972,174	-$191,055	-19.7%
TOTAL GRF SOURCES	**$2,915,647**	**$3,150,054**	**-$234,407**	**-7.4%**

*Estimates of the Office of Budget and Management as of August 2016.
Detail may not sum to total due to rounding.

Table 2: General Revenue Fund Sources
Actual vs. Estimate
FY 2017 as of January 31, 2017
($ in thousands)
(Actual based on report run in OAKS Actuals Ledger on February 1, 2017)

STATE SOURCES	Actual	Estimate*	Variance	Percent	FY 2016	Percent Change
TAX REVENUE						
Auto Sales	$791,728	$803,900	-$12,172	-1.5%	$772,102	2.5%
Nonauto Sales and Use	$5,530,536	$5,638,600	-$108,064	-1.9%	$5,422,968	2.0%
Total Sales and Use Taxes	**$6,322,264**	**$6,442,500**	**-$120,236**	**-1.9%**	**$6,195,069**	**2.1%**
Personal Income	$4,833,745	$5,109,000	-$275,255	-5.4%	$5,126,037	-5.7%
Corporate Franchise	-$123	$0	-$123	---	$30,475	-100.4%
Financial Institution	$38,599	$43,100	-$4,501	-10.4%	$35,312	9.3%
Public Utility	$47,621	$51,000	-$3,379	-6.6%	$51,297	-7.2%
Kilowatt-Hour Excise	$211,385	$191,300	$20,085	10.5%	$198,544	6.5%
Natural Gas Consumption (MCF)	$18,505	$18,700	-$195	-1.0%	$18,566	-0.3%
Commercial Activity Tax	$670,716	$687,000	-$16,284	-2.4%	$657,132	2.1%
Petroleum Activity Tax	$2,860	$3,000	-$140	-4.7%	$3,362	-14.9%
Foreign Insurance	$162,740	$156,200	$6,540	4.2%	$146,166	11.3%
Domestic Insurance	$53	$400	-$347	-86.7%	$344	-84.5%
Business and Property	-$678	$0	-$678	---	$42	-1723.5%
Cigarette	$516,369	$514,200	$2,169	0.4%	$539,150	-4.2%
Alcoholic Beverage	$35,026	$32,300	$2,726	8.4%	$31,986	9.5%
Liquor Gallonage	$28,093	$27,100	$993	3.7%	$27,161	3.4%
Estate	$490	$0	$490	---	$918	-46.6%
Total Tax Revenue	**$12,887,667**	**$13,275,800**	**-$388,133**	**-2.9%**	**$13,061,561**	**-1.3%**
NONTAX REVENUE						
Earnings on Investments	$24,067	$17,200	$6,867	39.9%	$16,600	45.0%
Licenses and Fees	$14,951	$13,680	$1,271	9.3%	$12,832	16.5%
Other Revenue	$53,488	$51,818	$1,670	3.2%	$42,841	24.9%
Total Nontax Revenue	**$92,506**	**$82,698**	**$9,808**	**11.9%**	**$72,273**	**28.0%**
TRANSFERS						
Budget Stabilization	$0	$0	$0	---	$0	---
Other Transfers In	$92,187	$31,800	$60,387	189.9%	$189,860	-51.4%
Total Transfers In	**$92,187**	**$31,800**	**$60,387**	**189.9%**	**$189,860**	**-51.4%**
TOTAL STATE SOURCES	**$13,072,360**	**$13,390,298**	**-$317,937**	**-2.4%**	**$13,323,694**	**-1.9%**
Federal Grants	$6,928,319	$7,456,128	-$527,809	-7.1%	$7,231,395	-4.2%
TOTAL GRF SOURCES	**$20,000,679**	**$20,846,425**	**-$845,747**	**-4.1%**	**$20,555,089**	**-2.7%**

*Estimates of the Office of Budget and Management as of August 2016.
Detail may not sum to total due to rounding.

GRF tax revenue was $91.6 million below estimate in January.

FY 2017 GRF tax revenue was $388.1 million below estimate.

Revenues

– *Ross A. Miller, Chief Economist, 614-644-7768*

Overview

GRF tax revenue in January was $91.6 million below the estimate published by OBM in August. Revenue from the personal income tax (PIT) was $92.3 million below estimate, while positive variances from other taxes, primarily the cigarette and other tobacco products (OTP) tax ($6.1 million), the commercial activity tax (or CAT, $4.7 million) and the financial institutions tax ($2.7 million) roughly offset a $15.3 million negative variance for the sales and use tax.

State GRF tax revenue began a trend of weak results around January 2016, but it worsened at the end of the calendar year. Due to recent revenue experience, OBM revised downward its estimate of FY 2017 GRF tax revenue by $592 million when it presented the Governor's budget proposal. Downward revisions were made to the major tax sources: the sales and use tax ($259 million), the PIT ($334 million), and the CAT ($32 million).[1] LSC does not have monthly estimates of revenue based on the new estimates, so comparisons to estimate in this article are made to the original August 2016 estimates.

Compared to the August estimates, FY 2017 GRF tax revenue through January showed a negative variance of $388.1 million. The PIT was below estimate by $275.3 million, and the sales and use tax was below estimate by $120.2 million. Revenue from the CAT was $16.3 million below estimate. On the other hand, revenue from the kilowatt-hour tax exceeded estimate by $20.1 million, and revenue from the foreign insurance tax was above estimate by $6.5 million.

Total GRF sources through January amounted to $20.00 billion,[2] $845.7 million below estimate. In addition to the poor performance of tax revenue, revenue from federal grants has consistently been below estimate during FY 2017, with the cumulative negative variance through January amounting to $527.8 million. Revenue from federal grants is primarily related to the level of spending in the Medicaid program, which was $699.0 million below estimate for FY 2017 through January. State sources of revenue other than taxes have done better this year, with nontax revenue $9.8 million above estimate through January, and

[1] The estimate for the cigarette and OTP tax was left unchanged.

[2] Total GRF sources consist of state-source receipts (tax revenue, nontax revenue, and transfers in) and federal grants.

transfers into the GRF $60.4 million above estimate. January transfers in included $60 million that was identified in OAKS as authorized by section 512.20 of Am. Sub. H.B. 64 of the 131st General Assembly, the current operating budget act; it appears that OBM expected to make these transfers in June, so this variance is likely a matter of timing.

FY 2017 GRF revenue through seven months is also below such revenue during the comparable months of FY 2016. Tax revenue has fallen by $173.9 million. Revenue from the PIT, which is $292.3 million below FY 2016, is almost entirely responsible for the tax revenue decline. Most of the decrease in PIT receipts is due to reduced estimated payments, which is likely a delayed result from income tax changes enacted in H.B. 64 rather than a decline in the tax base; revenue from income tax withholding grew 1.2% from the first seven months of FY 2016 to FY 2017.[3] Revenue from the cigarette and OTP tax was $22.8 million below the FY 2016 figure, though that simply continues a long-term downward trend. Revenue from the sales and use tax increased by $127.2 million and CAT revenue was $13.6 million higher.

FY 2017 income tax withholding grew 1.2% in FY 2017.

Sales and Use Tax

GRF revenue from the sales and use tax was $15.3 million (1.5%) below estimate in January, resulting in revenue during the first seven months of FY 2017 being $120.2 million (1.9%) below estimate. The variance in January resumed an FY 2017 pattern of below-estimate revenue from the tax; December was the only month this fiscal year showing a positive variance from the tax. Revenue from this tax for the first seven months of FY 2017 grew by $127.2 million (2.1%) compared to revenue during the corresponding months of FY 2016.

FY 2017 sales tax revenue was $120.2 million below estimate.

For analysis and forecasting, the sales and use tax is separated into two parts: auto and nonauto. Auto sales and use tax collections generally arise from sales of motor vehicles, but auto taxes arising from leases are

[3] Growth in withholding is weak due to both slow growth in aggregate payrolls statewide and a reduction in the withholding rate that took effect in August 2015. More details about income tax revenue are reported in the personal income tax section of this article.

paid at the lease signing and are mostly recorded under the nonauto tax instead of the auto tax.[4]

Nonauto Sales and Use Tax

Nonauto sales tax revenue was $108.1 million below estimate through January.

Nonauto sales and use tax revenue to the GRF was $888.1 million in January, which was $12.5 million (1.4%) below estimate. Collections from this segment of the tax have been below estimate six of the seven months of FY 2017. Through January, FY 2017 revenue was $5.53 billion, $108.1 million (1.9%) below estimate. Compared to the corresponding months of FY 2016, revenue has grown $107.6 million (2.0%).

A significant part of the tax base for this tax is attributable to premiums paid to Medicaid health insuring corporations (MHICs), which have grown 4.6% from FY 2016 to FY 2017. This portion of sales tax collections is generally correlated with Medicaid spending, rather than broader consumer spending trends. Excluding revenue from MHICs, nonauto sales tax revenue has grown 1.7% from FY 2016 to FY 2017. Growth in consumer spending is fueled by household incomes, which are growing slowly, as implied by data on income tax withholding. The Johnson Redbook index of same-store sales, published weekly, shows year-over-year growth nationally in sales made at discount stores ranging between 1.0% and 2.0% most weeks in January, and decreases most weeks for sales at department stores. Traditional retail stores are experiencing pressure on sales growth due to competition from Internet-based retailers and catalogue sales; many out-of-state companies making such sales to Ohioans do not collect the sales tax.

Auto Sales and Use Tax

GRF revenue from the auto sales and use tax in January amounted to $102.5 million, which was $2.8 million (2.7%) below estimate. Through January, FY 2017 revenue amounted to $791.7 million, $12.2 million (1.5%) below estimate. Revenue through January from this segment of the tax grew by $19.6 million (2.5%) from FY 2016.

Nationwide sales of autos and light trucks continued briskly in January, at a seasonally adjusted annual rate of 17.5 million units. January sales are maintaining the record pace set for calendar years 2015

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[4] Taxes arising from leases are paid immediately upon the lease signing. The clerks of court generally make auto sales and use tax payments on Mondays for taxes collected during the previous week on motor vehicles, watercraft, and outboard motors titled. Therefore auto sales and use tax receipts mostly, but not perfectly, reflect vehicles sold and titled during a given month.

and 2016. The pace for auto sales, at 6.3 million units, was slightly below the 2016 results for autos (6.9 million units), while the pace for light trucks (11.2 million units) was slightly better than 2016 (10.6 million units). January 2017 auto sales tax revenue was $6.4 million (6.6%) higher than revenue the previous year. Ohio's market for sales of autos and light trucks has been somewhat softer than the nationwide market, though, and January's experience continues to exhibit a weaker-than-expected result, though auto sales tax revenue remains at a historically high level.

Personal Income Tax

FY 2017 income tax revenue was $275.3 million below estimate through January, due mostly to withholding.

January GRF revenue from the PIT was $845.9 million, $92.3 million (9.8%) below estimate. Monthly withholding revenue was $28.5 million (3.5%) below estimate, but most of the overall negative variance was attributable to refunds. The GRF paid out $149.1 million in refunds in January, $72.9 million (95.7%) more than expected. January is one of the months that estimated payments are due; estimated payments amounted to $213.1 million, very close to the amount expected.

Year-to-date PIT revenue was $4.83 billion by the end of January, $275.3 million (5.4%) below estimate, and $292.3 million (5.7%) below the amount collected during the first seven months of FY 2016. FY 2017 revenues through January from each component of the PIT relative to estimates and to revenue received in the corresponding period of FY 2016 are detailed in the table below.

FY 2017 Year-to-Date Personal Income Tax Revenue
Estimate Variances and Year-over-Year Changes by Component

Category	Year-to-Date Variance from Estimate		Year-to-Date Changes from FY 2016	
	Amount ($ in millions)	Percentage (%)	Amount ($ in millions)	Percentage (%)
Withholding	-$172.6	-3.4%	$59.0	1.2%
Quarterly Estimated Payments	$6.1	1.2%	-$205.4	-29.2%
Trust Payments	-$5.7	-20.8%	-$10.3	-32.3%
Annual Return Payments	$15.0	17.4%	-$21.6	-17.7%
Miscellaneous Payments	-$7.1	-15.3%	-$1.8	-4.3%
Gross Collections	-$164.3	-2.9%	-$180.1	-3.2%
Less Refunds	$116.8	35.2%	$109.4	32.2%
Less LGF Distribution	-$5.8	-2.5%	$2.8	1.3%
GRF PIT Revenue	-$275.3	-5.4%	-$292.3	-5.7%

Revenue from withholding has grown only 1.2% from FY 2016 to FY 2017, but that is partly attributable to a 3.1% reduction in the withholding rate that went into effect in August 2015 to reflect the reduction in PIT rates enacted in H.B. 64. Withholding revenue was $172.6 million (3.4%) below estimate, though, reflecting slower-than-expected growth in Ohio's aggregate payrolls so far this fiscal year. Weak growth in revenue from withholding has been the primary reason for the negative variance through the first seven months of FY 2017, but refunds have also played a significant role. Refunds were $116.8 million (35.2%) above estimate. With the tax filing season beginning in late January, only about one-fifth of FY 2017 refunds were expected during the first seven months of the year, while over three-quarters of refunds were expected over the next four months. Thus the behavior of refunds relative to estimate over the next four months will be a very important factor in determining how FY 2017 PIT revenue finishes the year.

Cigarette and Other Tobacco Products Tax

Cigarette tax revenue is on target for FY 2017 through January.

Revenue from the cigarette and OTP tax amounted to $77.5 million in January, $6.1 million (8.5%) above estimate. This was partly due to timing; December receipts were $7.6 million below estimate. For FY 2017 through January, receipts were $516.4 million, $2.2 million (0.4%) above estimate, and $22.8 million (4.2%) below FY 2016. Revenue in FY 2016 was boosted by a "floor tax" on cigarettes held in inventory at the beginning of the year when the tax rate rose from $1.25 per pack of cigarettes to $1.60 per pack. Revenue from the cigarette tax tends to decline over time, but the rate increase increased FY 2016 revenue, and the floor tax component made the decline in FY 2017 somewhat sharper than the long-term rate of decrease. FY 2017 revenue attributable to sales of cigarettes was $480.0 million through January, while OTP revenue was $36.3 million.

Commercial Activity Tax

GRF revenue from the CAT amounted to $52.0 million in January, $4.7 million (9.9%) above estimate. January is not one of the months that quarterly taxpayers remit revenue, so revenue for the month tells us little about what to expect for the remainder of the fiscal year. February will be the next month during which quarterly taxpayers remit payments. Revenue received during the first seven months of FY 2017 totaled $670.7 million, $16.3 million (2.4%) less than estimate. That revenue was also $13.6 million (2.1%) above receipts in the corresponding period last fiscal year.

The CAT is the state's third-largest GRF tax revenue source, as well as its broadest-based business tax. The tax base is business' gross receipts, subject to various adjustments. The manufacturing sector accounted for 24% of total CAT liability during FY 2016, while wholesale and retail trade combined accounted for about one-third. Weak growth in this tax base reflects weak growth in business' gross receipts across the Ohio economy, and especially in these sectors.

Table 3: General Revenue Fund Uses
Actual vs. Estimate
Month of January 2017
($ in thousands)
(Actual based on OAKS reports run February 6, 2017)

PROGRAM	**Actual**	**Estimate***	**Variance**	**Percent**
Primary and Secondary Education	$661,905	$695,231	-$33,326	-4.8%
Higher Education	$181,908	$185,269	-$3,361	-1.8%
Other Education	$4,843	$8,837	-$3,994	-45.2%
Total Education	$848,655	$889,337	-$40,681	-4.6%
Medicaid	$1,162,744	$1,457,129	-$294,385	-20.2%
Health and Human Services	$162,648	$159,484	$3,164	2.0%
Total Welfare and Human Services	$1,325,392	$1,616,613	-$291,221	-18.0%
Justice and Public Protection	$184,823	$210,244	-$25,422	-12.1%
General Government	$37,391	$38,128	-$737	-1.9%
Total Government Operations	$222,214	$248,373	-$26,159	-10.5%
Property Tax Reimbursements	$995	$0	$995	---
Debt Service	$106,193	$119,599	-$13,406	-11.2%
Total Other Expenditures	$107,188	$119,599	-$12,411	-10.4%
Total Program Expenditures	**$2,503,449**	**$2,873,922**	**-$370,473**	**-12.9%**
TRANSFERS				
Budget Stabilization	$0	$0	$0	---
Other Transfers Out	$18	$18,918	-$18,900	-99.9%
Total Transfers Out	$18	$18,918	-$18,900	-99.9%
TOTAL GRF USES	**$2,503,467**	**$2,892,839**	**-$389,373**	**-13.5%**

*August 2016 estimates of the Office of Budget and Management.
Detail may not sum to total due to rounding.

Table 4: General Revenue Fund Uses
Actual vs. Estimate
FY 2017 as of January 31, 2017
($ in thousands)
(Actual based on OAKS reports run February 6, 2017)

PROGRAM	**Actual**	**Estimate***	**Variance**	**Percent**	**FY 2016**	**Percent Change**
Primary and Secondary Education	$4,744,916	$4,702,973	$41,943	0.9%	$4,748,335	-0.1%
Higher Education	$1,327,411	$1,340,764	-$13,353	-1.0%	$1,294,460	2.5%
Other Education	$51,142	$53,793	-$2,651	-4.9%	$48,786	4.8%
Total Education	$6,123,470	$6,097,531	$25,939	0.4%	$6,091,582	0.5%
Medicaid	$10,272,922	$10,971,945	-$699,023	-6.4%	$10,628,450	-3.3%
Health and Human Services	$836,447	$885,971	-$49,524	-5.6%	$805,063	3.9%
Total Welfare and Human Services	$11,109,370	$11,857,916	-$748,547	-6.3%	$11,433,512	-2.8%
Justice and Public Protection	$1,292,946	$1,308,329	-$15,383	-1.2%	$1,241,411	4.2%
General Government	$235,914	$248,341	-$12,427	-5.0%	$223,291	5.7%
Total Government Operations	$1,528,860	$1,556,670	-$27,810	-1.8%	$1,464,703	4.4%
Property Tax Reimbursements	$901,983	$919,983	-$18,000	-2.0%	$897,181	0.5%
Debt Service	$1,013,333	$1,027,572	-$14,239	-1.4%	$977,669	3.6%
Total Other Expenditures	$1,915,316	$1,947,555	-$32,240	-1.7%	$1,874,850	2.2%
Total Program Expenditures	**$20,677,015**	**$21,459,672**	**-$782,658**	**-3.6%**	**$20,864,646**	**-0.9%**
TRANSFERS						
Budget Stabilization	$29,483	$29,483	$0	0.0%	$425,500	-93.1%
Other Transfers Out	$238,605	$269,541	-$30,936	-11.5%	$388,260	-38.5%
Total Transfers Out	$268,087	$299,023	-$30,936	-10.3%	$813,760	-67.1%
TOTAL GRF USES	**$20,945,102**	**$21,758,696**	**-$813,594**	**-3.7%**	**$21,678,406**	**-3.4%**

*August 2016 estimates of the Office of Budget and Management.
Detail may not sum to total due to rounding.

Table 5: Medicaid Expenditures by Department
Actual vs. Estimate
($ in thousands)
(Actuals based on OAKS report run on February 3, 2017)

	Month of January 2017				Year to Date Through January 2017			
Department	**Actual**	**Estimate***	**Variance**	**Percent**	**Actual**	**Estimate***	**Variance**	**Percent**
Medicaid	**$1,704,427**	**$1,998,441**	**-$294,014**	**-14.7%**	**$12,655,731**	**$13,510,948**	**-$855,217**	**-6.3%**
GRF	$1,108,243	$1,405,219	-$296,976	-21.1%	$9,888,408	$10,560,316	-$671,908	-6.4%
Non-GRF	$596,184	$593,222	$2,962	0.5%	$2,767,323	$2,950,632	-$183,309	-6.2%
Developmental Disabilities	**$226,184**	**$233,653**	**-$7,469**	**-3.2%**	**$1,471,081**	**$1,549,340**	**-$78,260**	**-5.1%**
GRF	$48,140	$47,299	$841	1.8%	$334,085	$337,630	-$3,544	-1.0%
Non-GRF	$178,044	$186,354	-$8,311	-4.5%	$1,136,995	$1,211,711	-$74,715	-6.2%
Job and Family Services	**$16,392**	**$9,689**	**$6,703**	**69.2%**	**$126,133**	**$172,016**	**-$45,883**	**-26.7%**
GRF	$5,654	$3,985	$1,669	41.9%	$44,135	$68,079	-$23,944	-35.2%
Non-GRF	$10,738	$5,704	$5,034	88.3%	$81,998	$103,936	-$21,939	-21.1%
Health	**$1,669**	**$1,505**	**$164**	**10.9%**	**$15,693**	**$15,732**	**-$38**	**-0.2%**
GRF	$315	$279	$36	12.8%	$2,262	$1,983	$279	14.0%
Non-GRF	$1,354	$1,226	$128	10.4%	$13,432	$13,749	-$317	-2.3%
Aging	**$606**	**$514**	**$92**	**17.9%**	**$4,472**	**$4,737**	**-$266**	**-5.6%**
GRF	$337	$282	$55	19.6%	$2,300	$2,253	$48	2.1%
Non-GRF	$269	$232	$37	15.8%	$2,171	$2,484	-$313	-12.6%
Mental Health and Addiction	**$223**	**$358**	**-$135**	**-37.8%**	**$3,147**	**$2,963**	**$184**	**6.2%**
GRF	$54	$65	-$11	-16.6%	$1,732	$1,685	$47	2.8%
Non-GRF	$168	$293	-$125	-42.5%	$1,416	$1,278	$138	10.8%
Total GRF	**$1,162,744**	**$1,457,129**	**-$294,385**	**-20.2%**	**$10,272,922**	**$10,971,945**	**-$699,023**	**-6.4%**
Total Non-GRF	**$786,757**	**$787,031**	**-$274**	**0.0%**	**$4,003,335**	**$4,283,791**	**-$280,456**	**-6.5%**
Total All Funds	**$1,949,501**	**$2,244,160**	**-$294,660**	**-13.1%**	**$14,276,257**	**$15,255,736**	**-$979,479**	**-6.4%**

*Estimates are from the Department of Medicaid.
Detail may not sum to total due to rounding.

Table 6: All-Funds Medicaid Expenditures by Payment Category
Actual vs. Estimate
($ in thousands)
(Actuals based on OAKS report run on February 3, 2017)

	January				Year to Date Through January 2017			
Payment Category	**Actual**	**Estimate***	**Variance**	**Percent**	**Actual**	**Estimate***	**Variance**	**Percent**
Managed Care	$722,635	$938,997	-$216,362	-23.0%	$5,834,301	$6,311,290	-$476,989	-7.6%
Nursing Facilities	$134,931	$126,154	$8,777	7.0%	$883,059	$861,558	$21,501	2.5%
DDD Services	$221,780	$228,939	-$7,159	-3.1%	$1,425,392	$1,496,722	-$71,329	-4.8%
Hospitals	$89,690	$96,291	-$6,601	-6.9%	$850,778	$948,560	-$97,783	-10.3%
Behavioral Health	$96,905	$115,473	-$18,567	-16.1%	$656,879	$719,146	-$62,267	-8.7%
Administration	$74,339	$74,198	$142	0.2%	$529,203	$663,298	-$134,095	-20.2%
Aging Waivers	$29,068	$29,862	-$794	-2.7%	$198,898	$204,590	-$5,692	-2.8%
Prescription Drugs	$35,578	$43,762	-$8,184	-18.7%	$232,531	$265,740	-$33,209	-12.5%
Medicare Buy-In	$48,705	$41,108	$7,597	18.5%	$361,061	$271,672	$89,389	32.9%
Physicians	$14,230	$18,822	-$4,592	-24.4%	$101,796	$119,205	-$17,410	-14.6%
Medicare Part D	$38,158	$28,063	$10,095	36.0%	$215,159	$194,799	$20,360	10.5%
Home Care Waivers	$11,939	$16,618	-$4,679	-28.2%	$73,001	$101,826	-$28,825	-28.3%
ACA - Managed Care	$337,005	$393,467	-$56,462	-14.3%	$2,356,318	$2,542,127	-$185,809	-7.3%
All Other	$94,538	$92,408	$2,130	2.3%	$557,881	$555,202	$2,679	0.5%
Total All Funds	**$1,949,501**	**$2,244,160**	**-$294,660**	**-13.1%**	**$14,276,257**	**$15,255,736**	**-$979,479**	**-6.4%**

* Estimates are from the Department of Medicaid.

Detail may not sum to total due to rounding.

For the first seven months of FY 2017, GRF program expenditures were below OBM's August 2016 estimate by $782.7 million, of which $699.0 million occurred in Medicaid.

EXPENDITURES

– Russ Keller, Senior Economist, 614-644-1751

– Nicholas J. Blaine, Budget Analyst, 614-387-5418

Overview

Tables 3 and 4 show GRF uses for the month of January and for FY 2017 through January, respectively. GRF uses mainly consist of program expenditures but also include transfers out. Through January, GRF program expenditures totaled $20.68 billion. These expenditures were below the estimate released by OBM in August 2016[5] by $782.7 million (3.6%), of which $699.0 million occurred in Medicaid. The month of January contributed $294.4 million to GRF Medicaid's negative year-to-date variance. A large portion of the Medicaid variance was due to lower than expected managed care rates. Over 90% of Medicaid recipients are enrolled in managed care plans. The section that follows this overview provides more details on Medicaid expenditures.

The Health and Human Services program category had the second largest negative year-to-date variance at $49.5 million (5.6%). This variance occurred entirely in months prior to January. The category's negative year-to-date variance was in fact narrowed somewhat in January as GRF expenditures for Health and Human Services were $3.2 million (2.0%) above the estimate for the month. The positive year-to-date variance of $41.9 million (0.9%) in the Primary and Secondary Education program category also occurred entirely in months prior to January. This category's expenditures in January were $33.3 million (4.8%) below estimate. As reported in prior issues of *Budget Footnotes*, timing accounted for the majority of the variances in these two program categories. More specifically for Primary and Secondary Education, school foundation payments often deviate from their monthly estimates as various data elements used in the formula calculations, including student enrollment and property value, are updated throughout the year.

Other notable program expenditure variances include a negative year-to-date variance of $18.0 million (2.0%) in Property Tax

[5] As indicated in the Highlights section of this report, OBM revised FY 2017 disbursement estimates downward from $35.89 billion to $35.07 billion as part of its executive budget submission on January 30, 2017. However, the variance analyses for this and future Expenditures reports will continue to be based on those compiled by OBM in August 2016.

Reimbursements and another negative year-to-date variance of $15.4 million (1.2%) in Justice and Public Protection. The variance in the Property Tax Reimbursements program category was a result of lower than expected reimbursement payments based on the August 2016 property tax settlement. The first semiannual reimbursement payments were completed at the end of December. The second semiannual payments, which are based on the February 2017 property tax settlement, will be made throughout the second half of FY 2017. GRF expenditures from the Justice and Public Protection category were $25.4 million below estimate in January, which reversed this category's year-to-date variance from a positive $10.0 million at the end of December to a negative $15.4 million at the end of January. The Department of Rehabilitation and Correction, the largest agency within this program category, accounted for $13.4 million of the category's negative year-to-date variance.

In addition to program expenditures, GRF transfers out were $268.1 million through January, $30.9 million (10.3%) below estimate. In January, OBM anticipated an $18.9 million transfer out to the Managed Care Performance Payment Fund (Fund 5KW0), but no such transfer occurred. The transfer was authorized by section 327.80 of H.B. 64, which requires the Ohio Department of Medicaid (ODM) to provide performance payments to Medicaid managed care organizations providing care and services to participants of MyCare Ohio. ODM withholds a percentage of each premium payment it pays to a managed care organization for a program participant. The withheld funds are then transferred from the GRF to Fund 5KW0 for performance payments. The appropriation for GRF appropriation item 651525, Medicaid/Health Care Services, is reduced by the transferred amount.

Medicaid

Medicaid is primarily funded by the GRF although it also receives funding from various non-GRF funds. As a joint federal-state program, both GRF and non-GRF Medicaid expenditures contain federal and state moneys. In recent years, the federal government reimburses about two-thirds of Ohio's all-funds Medicaid expenditures.

Table 5 provides GRF and non-GRF Medicaid expenditures by agency. As seen from the table, all-funds Medicaid expenditures of $1.95 billion in January were below estimate by $294.7 million (13.1%). GRF Medicaid expenditures of $1.16 billion were $294.4 million (20.2%) below estimate while non-GRF Medicaid expenditures of $786.8 million were just $0.3 million below estimate. Through the first seven months of FY 2017, across all funds, Medicaid expenditures totaled $14.28 billion,

Across all funds, Medicaid expenditures were $979.5 million below OBM's August 2016 estimate for the year to date.

For the first seven months of FY 2017, total all-funds spending for managed care (including for traditional covered persons and the ACA expansion group) was $662.8 million below estimate.

$979.5 million (6.4%) below the year-to-date estimate. GRF Medicaid expenditures were $10.27 billion, $699.0 million (6.4%) below estimate, while non-GRF Medicaid expenditures were $4.00 billion, $280.5 million (6.5%) below estimate.

ODM is primarily responsible for administering Medicaid, with the assistance of five other state agencies – Developmental Disabilities, Job and Family Services, Health, Aging, and Mental Health and Addiction Services. As seen from Table 5, through the first seven months of FY 2017, ODM's GRF expenditures totaled $9.89 billion, which was $671.9 million (6.4%) below estimate, and its non-GRF expenditures totaled $2.77 billion, which was $183.3 million (6.2%) below estimate. Across all funds, ODM's expenditures were $855.2 million (6.3%) below the year-to-date estimate. All-funds Medicaid expenditures from the Department of Developmental Disabilities (DDD), the second largest agency within this program category, totaled $1.47 billion through the first seven months of FY 2017, which was $78.3 million (5.1%) below estimate. DDD's GRF Medicaid expenditures of $334.1 million were $3.5 million (1.0%) below the year-to-date estimate while its non-GRF year-to-date expenditures of $1.14 billion were $74.7 million (6.2%) below estimate. Together, ODM and DDD account for about 99% of the Medicaid expenditure total.

Table 6 details all-funds Medicaid expenditures by payment category. As seen from the table, Managed Care had the largest negative variance for the year to date at $477.0 million (7.6%). A significant portion of that variance ($216.4 million) occurred in January. Much of this negative variance can be attributed to lower than forecasted managed care rates. Actual rates are set at the beginning of each calendar year. Actual rates for calendar years 2016 and 2017 are both below the ones used in the estimate. As a result, the negative variance in Managed Care will likely continue to grow in the remaining months of FY 2017. The Managed Care negative variance in January was further augmented by reimbursement of some duplicate payments mistakenly made earlier in the fiscal year. The negative variance in the actual versus forecasted managed care rates is also the main driving force behind the negative year-to-date variance in the ACA-Managed Care category ($185.8 million, 7.3%).

After Managed Care and ACA-Managed Care, the category with the third largest negative year-to-date variance is Administration ($134.1 million, 20.2%). Approximately 40% of Medicaid's administrative spending is driven by service levels. Therefore, variances in spending in Administration often reflect variances in spending in the service categories. Variances in Administration are also driven by timing issues as billing for various contracts can be difficult to predict.

The negative year-to-date variance for Hospitals ($97.8 million, 10.3%) persisted in January due to a mix of over and underspending. ODM is spending more than anticipated on individuals who are dual-enrolled in Medicaid and Medicare. However, this is being more than offset by ODM spending less than anticipated on the aged, blind, and disabled population. In addition, hospital upper payment limit (UPL) payments and hospital-based physician UPL payments are below estimates year to date by about $54.8 million and $5.8 million, respectively. The UPL program allows the state to direct supplemental payments, up to the difference between the Medicare and the Medicaid amounts, to providers.

The Behavioral Health category had a negative variance in January of $18.6 million (16.1%) that increased its year-to-date negative variance to $62.3 million (8.7%). As part of the Department's behavioral health redesign, ODM budgeted additional spending in this category beginning in calendar year 2017. Claims have not come in as quickly as expected, but ODM expects this variance will shrink as providers start to bill more consistently for services.

The overwhelmingly negative year-to-date variances in various Medicaid payment categories are partially offset by the positive year-to-date variance in the Medicare Buy-In category ($89.4 million, 32.9%). This category's positive variance initially resulted from a larger than anticipated increase in Medicare Part B premiums for calendar year 2016; the rates for calendar year 2017 are even more above estimate, meaning the positive variance will likely grow at a faster rate in the second half of FY 2017 than in the first half. The Medicare Buy-in Program pays Medicare premiums, deductibles, and coinsurance for certain low-income Ohioans.

Issue Updates

ODE Works with Early Childhood Education Providers to Increase Utilization of Funded Preschool Slots

– Alex Vitale, Budget Analyst, 614-466-6582

The Ohio Department of Education (ODE) has been working with early childhood education providers across the state to increase utilization of available preschool slots. H.B. 64 increased the funding for early childhood education by $15 million and the number of funded preschool slots by 3,700 to 18,465 for FY 2017. As of late 2016, many of these slots remained unfilled according to enrollment surveys conducted by ODE. Some providers had filled fewer than 50% of their originally allocated slots due partly to the time needed to adjust to a programmatic change made in H.B. 64. Beginning in FY 2017, H.B. 64 limited program eligibility to four-year-old children only instead of both three- and four-year-olds. In an effort to increase utilization, ODE worked with these providers and reallocated about 1,000 open slots in December to providers that, through an ODE canvass, expressed interest in and capacity for additional slots. As of January 2017, early childhood education programs had filled 81%, or about 14,956, of the total slots funded for FY 2017.[6]

Early childhood education grants provide a state funding allocation of $4,000 per child to support programs that offer educational services for eligible children from families with incomes below 200% of the federal poverty level ($40,320 annually for a family of three in 2016). The 3,700 new slots for FY 2017 were targeted to high-need school districts in 12 regions throughout the state according to a district's percentage of economically disadvantaged kindergartners, performance on Ohio's Kindergarten Readiness Assessment, and the percentage of third grade students scoring below proficient levels on the reading portion of the state test in English language arts.

Of the total preschool slots funded in FY 2017, 17,215 (93.2%) are supported by GRF line item 200408, Early Childhood Education, in ODE's budget and 1,250 (6.8%) are supported by casino operator settlement fund moneys appropriated in Fund 5KT0 line item 600696, Early Childhood Education, in the Ohio Department of Job and Family Services (ODJFS) budget. FY 2017 marks the first year that casino operator settlement fund moneys have been used to fund early childhood education grants.

[6] In FY 2016, 89% of the 14,765 available slots were filled.

State Board of Education Recognizes Public Schools and Districts for High Academic Achievement and Student Growth

– Anthony Kremer, Budget Analyst, 614-466-5654

On November 15, 2016, the State Board of Education acknowledged public schools and districts that demonstrated high academic achievement and student growth on the 2015-2016 local report cards. This is the second year the State Board has recognized schools and districts through the All A Award and Momentum Award programs. The All A Award is given to districts and schools that received A's on each of the district or school's applicable report card measures. For the 2015-2016 school year, one district and five schools qualified. In comparison, two districts and 46 schools met the recognition criteria in the 2014-2015 school year. Beginning with the report cards for the 2017-2018 school year, this award will go to any school or district that earns an A on its overall report card grade.[7]

Districts and schools that earn straight A's on each applicable value-added measure on the report cards qualify for the Momentum Award. For the 2015-2016 school year, 54 districts and 169 schools met the criteria for this award. Similar numbers qualified for the award for the previous school year, when 53 districts and 165 schools were recognized. The value-added measure is designed to help educators determine the impact schools and teachers have on students' academic growth and progress in reading and math from year to year. The measure is calculated on an overall basis and for three student subgroups: (1) gifted students, (2) students in the lowest 20% in achievement, and (3) students with disabilities. Districts and schools must have a grade for at least two of the three value-added subgroups of students to qualify for the award. A list of the districts and schools qualifying under both recognition programs is available on the ODE's website.[8]

Department of Health Receives $380,000 for Zika Surveillance

– Jacquelyn Schroeder, Budget Analyst, 614-466-3279

On December 22, 2016, the Centers for Disease Control and Prevention (CDC) awarded two grants, totaling approximately $380,000, to the Ohio Department of Health (ODH) for Zika surveillance activities. The first grant, in the amount of $280,000, will be used to develop a process to rapidly detect microcephaly and other birth defects potentially related to the Zika virus during pregnancy. Specifically, ODH will use the

[7] Due to "safe harbor" provisions in current law, the report cards for the 2017-2018 school year will be the first to include overall letter grades for districts and schools.

[8] http://education.ohio.gov/Topics/School-Improvement/Awards-and-Recognition.

funds to contract with the 15 largest birthing hospitals in Ohio. These hospitals will alert ODH as soon as a baby is born with one of these birth defects, conduct clinical reviews, and consult with ODH staff concerning case specifics. Cases caused by the Zika virus will be reported to the CDC. The second grant, which is for approximately $100,000, will be used to fund an epidemiologist who will investigate and report on Zika virus cases and ensure that infants with congenital Zika virus infections and birth defects are captured in birth surveillance systems, among other duties. The funding will also be used to develop continuing education opportunities for health care professionals. Continuing education topics will include patient education, the professional's role in the screening process, and the resources available within local health jurisdictions and the ODH Laboratory.

These grant dollars were made available by the CDC as part of the Zika Response and Preparedness Appropriations Act of 2016, which allocated $350 million for Zika virus efforts. Of this amount, a total of $184 million was awarded as grants to states, territories, local jurisdictions, and universities. In July 2016, ODH received approximately $480,000 to identify and investigate potential Zika cases, coordinate the response between government and the health care sector, and purchase preparedness supplies such as insect repellents and screens.

Department of Medicaid Releases Expansion Population Assessment

– Nicholas J. Blaine, Budget Analyst, 614-387-5418

On December 30, 2016, the Ohio Department of Medicaid (ODM) released an assessment of the 2014 Ohio Medicaid expansion. The expansion extended coverage to previously uninsured low-income adults aged 19 to 64.[9] The assessment found this population, often referred to as Group VIII, has benefited from expansion through increased access to physical and mental health care (64.3% reported improved access), reduced emergency room use (33.9% used the emergency room less often), improved detection of unaddressed health conditions (27.0% received a chronic condition diagnosis), and reduced medical expenses (83.7% worried less about medical bills). Notably, the uninsured rate among adults aged 19 to 64 dropped from 32.4% in 2012 to 14.1% in 2015, dropping almost entirely due to Medicaid expansion. Approximately 89% of those enrolled in Group VIII had either no insurance prior to enrolling or had lost their employer-based health insurance.

This report was completed to comply with a provision of H.B. 64 that required ODM to report on the impact of Medicaid expansion by the end of calendar year (CY) 2016. Expansion allowed adults up to 138% of the federal poverty level (FPL) to enroll

[9] The full assessment is available on the Department of Medicaid's website: http://medicaid.ohio.gov/Portals/0/Resources/Reports/Annual/Group-VIII-Assessment.pdf.

in Medicaid. During FY 2016, Group VIII caseloads averaged 676,000 per month, of which 590,000 were served by managed care. The Department spent a total of $4.76 billion, including $3.83 billion on managed care plans, for this population. These costs were paid 100% with federal funds. For CY 2017, the state will share in the cost of Group VIII with federal support dropping to 95%.

Development Awards $22.8 Million in Ohio Historic Preservation Tax Credits

– Tom Middleton, Senior Budget Analyst, 614-728-4813

On December 20, 2016, the Development Services Agency (DSA) approved $22.8 million worth of Ohio Historic Preservation Tax Credits (OHPTC) for the rehabilitation of 33 historic buildings under 18 awards. The table below displays the OHPTC awards by region under this announcement, Round 17 of OHPTC awards.

Ohio Historic Preservation Tax Credit Awards by Region, Round 17

Region	Number of Awards	Total Value of Awards ($ millions)	Total Project Costs ($ millions)	Award as % of Total Project Costs
Northeast	4	$7.2	$75.7	9.5%
West	2	$5.2	$47.2	11.0%
Northwest	3	$4.1	$29.1	14.0%
Southwest	6	$3.9	$44.7	8.8%
Central	3	$2.5	$28.9	8.5%
TOTAL	**18**	**$22.8**	**$225.6**	**10.1%**

Note: Detail may not sum to total due to rounding.

The goal of the OHPTC Program is to spur investment within historic areas, restore buildings that will attract new businesses, and generate new jobs. To be eligible, generally a building must be listed on the National Register of Historic Places or designated as a local landmark by a Certified Local Government. Each year, $60 million is allocated to the program; however, an additional amount in tax credits may be awarded if projects that were previously approved under the program have been withdrawn, or if there is a surplus of tax credits from prior fiscal years. The program is administered through a partnership between DSA and the Ohio History Connection. DSA awards two rounds of funding each year. Round 18 project applications were due February 1, and the awards will be announced at the end of June.

Ohio Department of Commerce Launches Compliance Incentive Program for Hotels

– Shannon Pleiman, Budget Analyst, 614-466-1154

In January 2017, the Ohio Department of Commerce's (COM) Division of State Fire Marshal began issuing hotels "Operation Safe Stay" logos to appear in their windows and advertising campaign. The Operation Safe Stay Program was created under H.B. 486 of the 130th General Assembly. The program is intended to provide an incentive for the hotel industry to recognize hotels in Ohio that are consistently in compliance with the Ohio Fire Code and sanitary standards under the Ohio Revised Code. By mid-January, 43 out of the nearly 1,700 licensed hotels have qualified as a Safe Stay Hotel.

In order to qualify as a Safe Stay Hotel, a hotel must maintain a valid annual operating license, renew on time, and comply with sanitation and safety standards under both the Revised Code and the Ohio Fire Code for 24 consecutive months. Furthermore, the hotel cannot be the subject of nuisance findings or findings or convictions for lewdness, assignation, prostitution, or felony drug activity for 60 consecutive months.

The license fee for a new hotel ranges from $2,000 to $4,000. For existing hotels, the license fee is $110 up to 110 rooms plus $1.00 per room thereafter. License fees are deposited into the State Fire Marshal Fund (Fund 5460). In FY 2016, approximately $640,000 was deposited into Fund 5460 from these licenses.

Ohio EPA Awards Just Over $200,000 in Environmental Education and Awareness Project Grants

– Robert Meeker, Budget Analyst, 614-466-3839

In December 2016, the Ohio Environmental Protection Agency (Ohio EPA) announced the award of six environmental education and awareness project grants totaling a little over $200,000 through its Office of Environmental Education's General Grant Program (see table below). Under this program, eligible applicants may receive grants of up to $50,000 for projects that target a specific audience, such as preschool through university students and teachers. Priority is given to projects that focus on either: (1) innovative storm water management, (2) air emissions reductions, (3) habitat restoration, or (4) nutrient pollution reduction in rivers and streams. Grant recipients are required to provide a 10% cash or in-kind match. The grant awards are paid from the Environmental Education Fund (Fund 6A10), which receives one-half of the civil penalties collected by the Ohio EPA for violations of Ohio's air and water pollution control laws.

December 2016 Ohio EPA Environmental Education Grant Program Awards			
Grant Recipient	**County Service Area**	**Project Description**	**Grant Award**
Oberlin College	Cuyahoga, Lorain, Lucas, Summit	Expand curricular integration of Environmental Dashboard technology in four school districts	$49,689
Columbus Green Building Forum	Licking	Create curriculum for high school and adult education students in green building and environmental technologies	$46,332
Earth Day Coalition	Ashtabula, Cuyahoga, Geauga, Lake Lorain, Medina, Portage, Summit	Hold alternative fuel and advance technology workshops for vehicle operations personnel	$42,779
Lake Erie Nature and Science Center	Cuyahoga	Expand Climate Education field trip program	$25,000
Ohio University	Statewide	Implement storm water education program	$23,721
Boardman Glenwood Junior High School	Mahoning	Reduce school cafeteria waste and implement related community compost education	$16,053
		TOTAL	**$203,574**

Controlling Board Releases $4.6 million for County Juvenile Detention Center Renovations

– Maggie Wolniewicz, Senior Budget Analyst, 614-995-9992

On December 19, 2016, the Controlling Board approved the Department of Youth Services' request for the release of $4.6 million in capital funds for renovation and maintenance projects at 12 of the state's 38 county-operated juvenile detention centers. Of this total, $3.6 million will be used to fund a $6 million project to replace the existing Allen County Juvenile Detention Center, a 45-year-old, 16-bed facility, with a new 45-bed facility. The remaining $1.0 million in state capital funds will be used to help fund various maintenance projects, including surveillance cameras, door controls, HVAC equipment and controls, kitchen equipment, generators, roofing, and sprinkler system replacements in juvenile detention centers of the following 11 counties: Fairfield, Logan, Lorain, Marion, Ross, Sandusky, Trumbull, Union, Warren, Williams, and Wood. Juvenile detention centers are secure facilities intended to provide short-term care and custody of alleged and adjudicated juvenile offenders.

Tracking the Economy

– Thomas Kilbane, Economist, 614-714-3218

The material that follows is from the Economic Conditions and Outlook section of the Ohio Legislative Service Commission's February 1 testimony before the House Finance Committee on the pending biennial budget of the 132nd General Assembly. It reflects information available as of that date.

State of the Economy

Slowdown in manufacturing hampered Ohio's economic growth in 2016.

The economic expansion continued in 2016 for both the U.S. and Ohio, though some sectors have slowed. Nationwide, employment grew for 75 straight months through December, and by the end of 2016, wage growth was stronger than at any point since the 2007-2009 recession. This has supported healthy consumer spending, including a record number of light vehicle sales in 2016. Inflation, though still low, is increasing and employment growth was deemed strong enough by the Federal Reserve for a further increase in its target interest rate in December, with more expected in 2017. In contrast, business investment remains soft and exports are struggling under the weight of a strong U.S. dollar, which rose significantly again late in 2016. Nationwide industrial production declined in 2016.

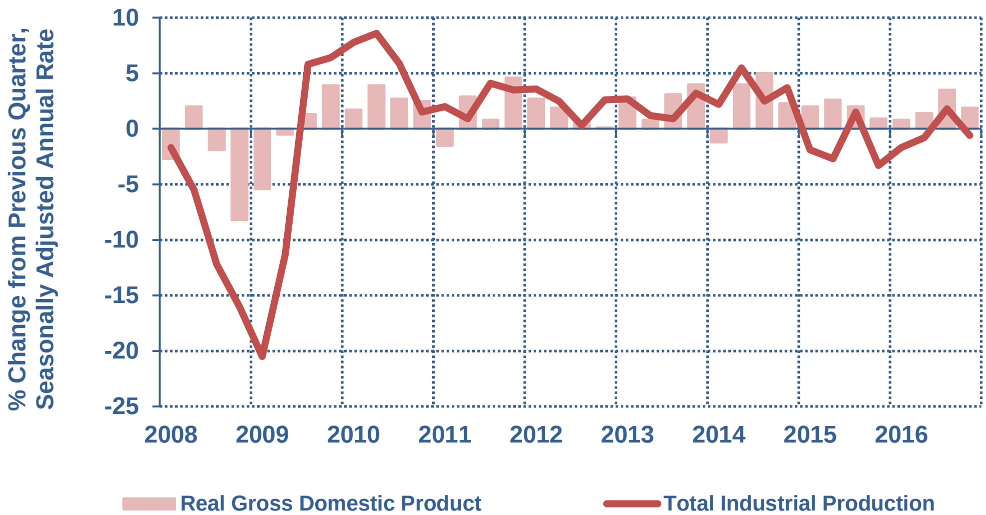
Many of these issues are highlighted in Ohio's economy which features plenty of manufacturing and production for export. Ohio's employment growth slowed significantly in 2016. On the other hand, home sales and real estate investment have been strong in the state and Columbus is one of the fastest growing metropolitan areas in the Midwest. Other statewide sectors have helped to pick up some of the slack too, such as growth in health care. Overall, further growth is predicted nationwide and also in Ohio, though at a bit of a slower pace.

National

The national economy continued to grow in 2016, though at a slowed pace.

The national economy continued to grow in 2016 as measured by total output, though at a slowed pace from 2015. Inflation-adjusted gross domestic product (real GDP) grew by 1.6% in 2016, down from 2.6% growth in 2015. Growth picked up in the second half of 2016 after a weak first half. Output during 2015 and early 2016 was weighed down in part by the oil and gas industry. Industrial production, which includes mining, fell in six of the last eight quarters, including a 0.6% decline in the fourth quarter of 2016. Manufacturing, the largest component of industrial production, was nearly flat in 2016, increasing just 0.1% in the calendar year. Chart 1 illustrates quarterly changes in real GDP and industrial production from 2008 through last year.

Chart 1: United States Output Measures



The current economic expansion is the weakest in the post-WWII era.

The current U.S. economic expansion has been marked by its length and its weakness. December 2016 marked 90 months since the last recession ended in June 2009,[10] which makes it the fourth longest expansion since 1854. However, it has also been the weakest expansion in terms of economic growth in the post-World War II era. Quarterly growth of real GDP averaged a 2.1% annual rate from the 2009 second quarter through the 2016 fourth quarter, while previous post-World War II expansions averaged a 4.6% annual growth rate.

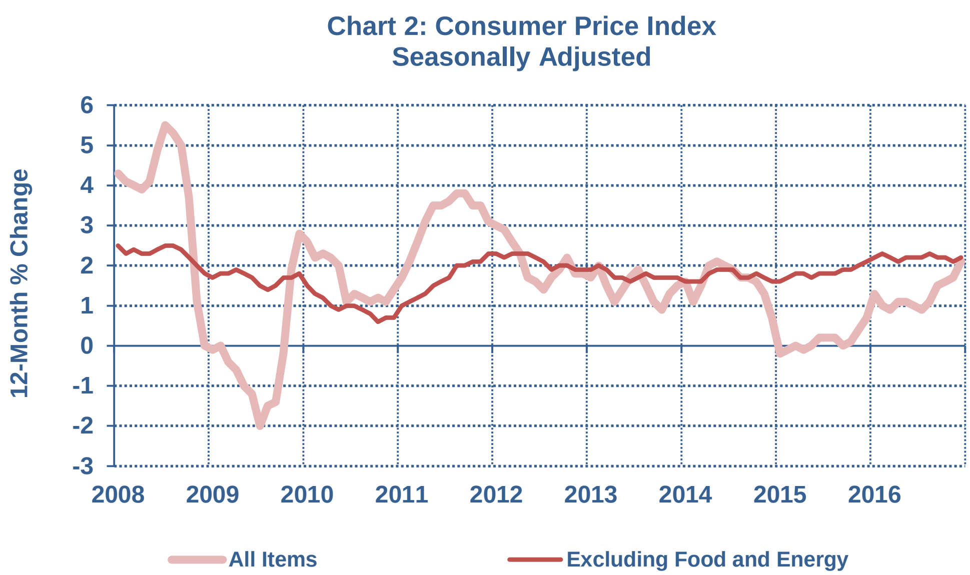
Employment has been among the most consistent sources of growth during the current expansion. The economy added another 2.2 million jobs[11] in 2016, though growth did slow a bit from 2015. December 2016 marked 75 straight months in which the national economy added more jobs than it lost. Wage growth, which has been sluggish throughout the recovery, showed signs of picking up by the end of 2016 as well. By December, average hourly earnings for private, nonfarm workers had grown at a faster pace year-over-year than at any point since the recession.

[10] Business cycle trough and peak dates used in calculating the numbers on which these statements are based are from the National Bureau of Economic Research.

[11] Nonfarm payroll employment.

On the back of employment and wage gains, consumer spending was strong in 2016, driving economic growth despite weakness in other sectors. Consumer durable goods spending grew at a high pace. U.S. sales of cars and light trucks were 17.5 million units in 2016, setting the all-time record for the second straight year. The market share of light trucks and SUVs increased sharply over the last two years, driven in part by low gasoline prices. By the end of 2016 though, auto production had been cut at some domestic plants, based on expectations that demand may have peaked.

Consumer price increases reached the Federal Reserve's 2% target over a 12-month span in December for the first time in over two years, though the measure which excludes food and energy products exceeded that level throughout the year (Chart 2). Overall price inflation was minimal in 2015 and slow to pick up for much of 2016 after a steep drop in energy prices at the end of 2014. Gasoline prices remain low relative to levels during the last ten years, but are no longer declining.



In contrast to consumers, business activity generally softened in 2016. Overall business fixed investment fell after slowing in 2015. Industrial capacity utilization declined in 2016 despite some recovery in mining. Manufacturing capacity utilization had its biggest decline year-over-year since the recession ended. Exporters have been hurt by a strong U.S. dollar.

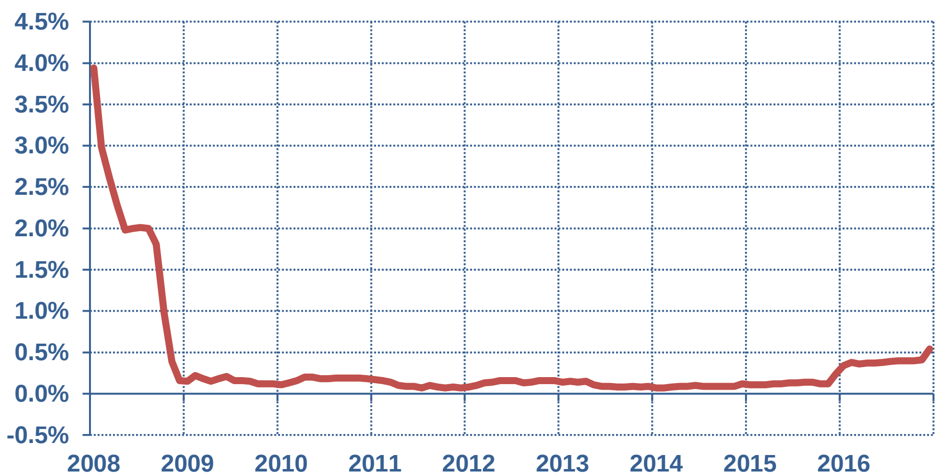
Nationwide business fixed investment declined in 2016.

Nationwide residential fixed investment growth slowed in 2016 after double-digit growth in 2015, although much of the decline was related to apartment construction in the Northeast region of the country. Many regions still experienced healthy investment growth. Housing starts in the Midwest region grew by 17.4% in 2016. Nationwide sales volume of single-family existing homes (the bulk of the residential real estate market) in 2016 was the highest in a decade.[12] Healthy demand in the market, but low supply relative to historical standards, led to rising prices in most regions. Nationwide home prices were up about 6% in 2016 relative to 2015.[13]

More increases in the Federal Reserve's target interest rate are expected in 2017.

The Federal Reserve began raising short-term interest rates in December 2015, and in December 2016 determined economic conditions were strong enough for a second quarter-point increase in the target range. With inflation near (or already at by some measures) the Federal Reserve's 2% target, and employment continuing to increase on a monthly basis nationwide, more increases are expected in 2017. Prior to December 2015, U.S. monetary policy had held short-term interest rates near zero for seven years (Chart 3).

Chart 3: Effective Federal Funds Rate



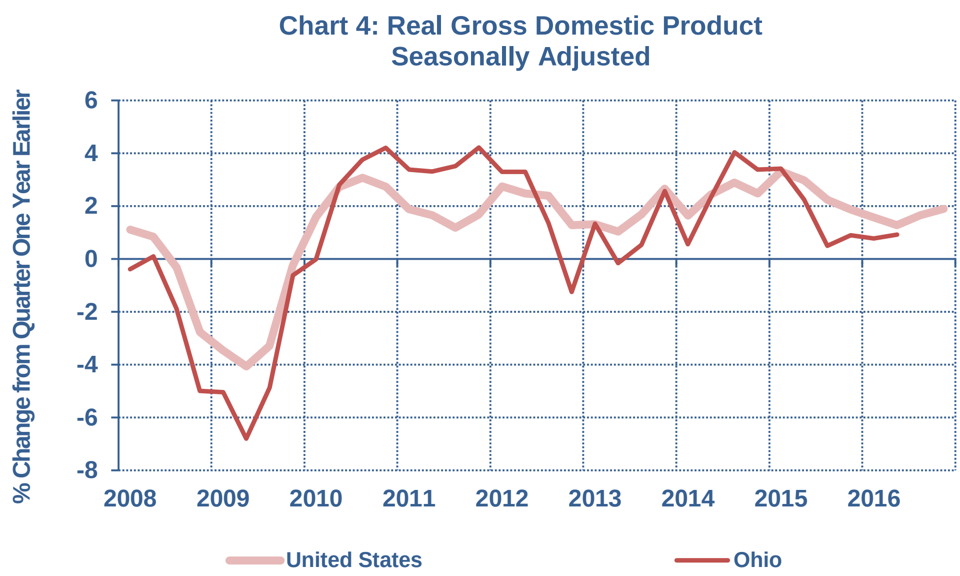
Ohio

The 2007-2009 recession was more severe in Ohio than nationwide, but so was the initial recovery as measured by gross product. By 2015 and the first half of 2016 (the most recent state GDP estimate available), Ohio's growth rate of total output trailed the nation's (Chart 4). During that time period, the national economy experienced declines in industrial production, an outsized portion of which takes place in Ohio. Overall

[12] Data on existing home sales are from the National Association of Realtors.

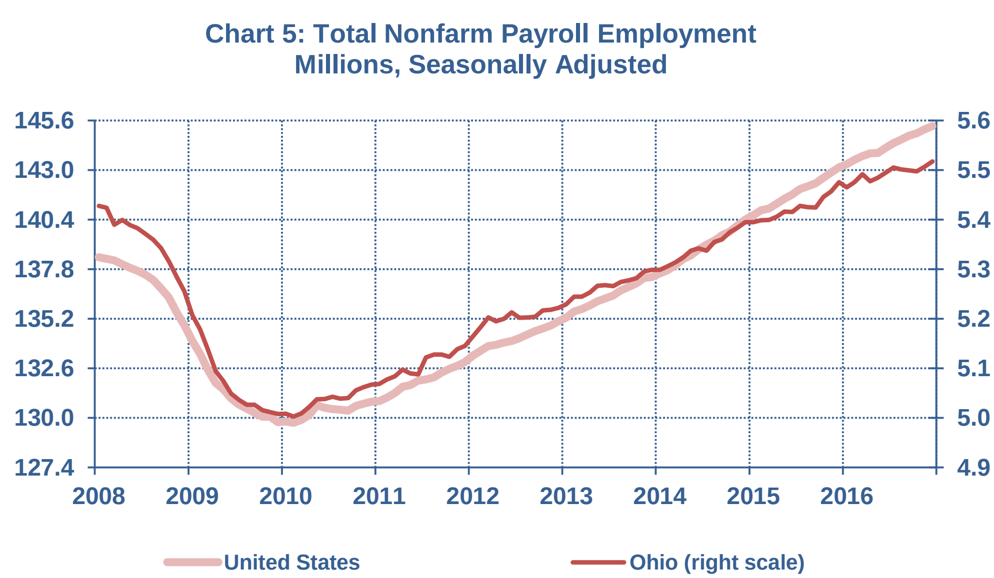
[13] Home prices according to the Federal Housing Finance Agency.

four-quarter output growth in Ohio trailed the nation in each of the five most recently reported quarters.



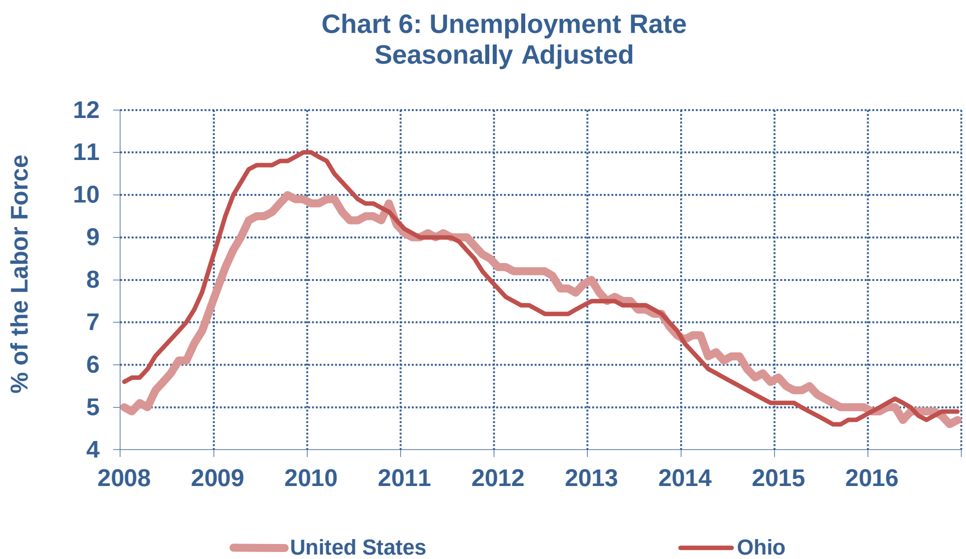
Ohio added fewer jobs in 2016 than in any other calendar year since 2009.

Ohio nonfarm payroll employment has grown each year since reaching a low point in 2010, but the pace of growth slowed considerably in 2016. Ohio added 41,800 jobs in 2016, the lowest total in a calendar year since 2009. The healthcare and social assistance sector added the most jobs in Ohio in 2016, while durable goods manufacturing lost the most. Nationwide nonfarm payroll growth slowed in 2016 as well, though not as much as in Ohio (Chart 5).



Ohio's statewide unemployment rate in December was 4.9%, finishing the year higher than it began for the first time since 2009. It was also the first time since 2013 that Ohio ended the year with a higher unemployment rate than the nation, which finished the year at 4.7% (Chart 6). Labor markets still appear to have more slack than these unemployment rates suggest. Since the end of the 2007-2009 recession, the rate of participation in the labor force[14] has declined steeply, both in Ohio and the U.S. as a whole. Some of the decline is demographic in nature as the baby-boomer generation retires, but the labor force participation rate has declined even among those younger than 65. In December, Ohio's labor force participation rate fell to its lowest level since the 1970s. This reduction in labor force has caused the reported rate of unemployment[15] to correspond to lower levels of actual employment for the population than in past eras. For instance, when Ohio's unemployment rate was 4.9% in October of 2001, 63.8% of its working-age population was employed, whereas in December 2016, Ohio's unemployment rate was the same, but the employment to working-age population percentage was only 59.1%.

59.1% of Ohio's civilian population aged 16 and up was employed in December 2016.



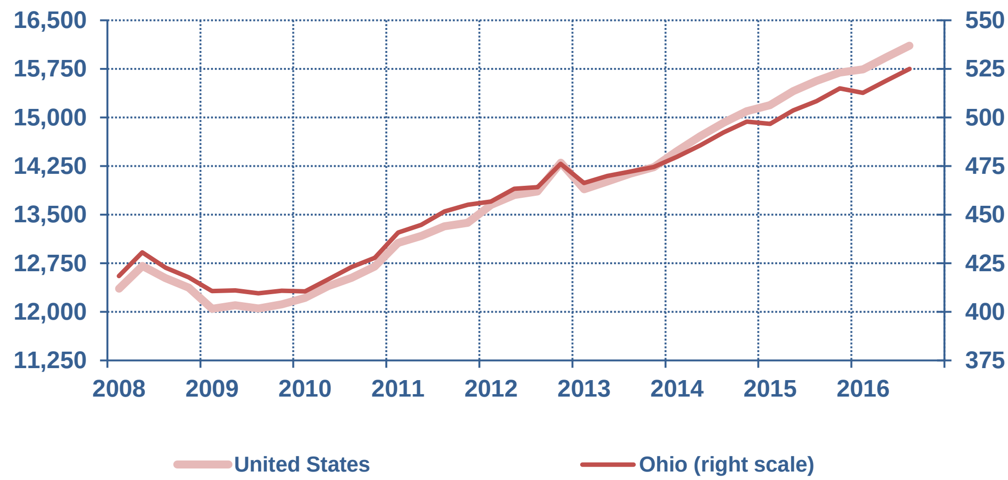
Personal income has generally been growing in Ohio and nationwide since 2009, though Ohio's pace of growth has trailed the nation's (Chart 7). Figures in the chart reflect dollars of current purchasing power. Ohio's personal income grew 3.3% in the most recently reported

[14] The labor force is the number of civilians age 16 and over who are either currently employed or unemployed but looked for work in the last four weeks.

[15] The unemployment rate is the number of people not employed but who have looked for work within the last four weeks as a percent of the labor force.

four quarters (ending in the third quarter of 2016), while personal income in the U.S. rose 3.5%.

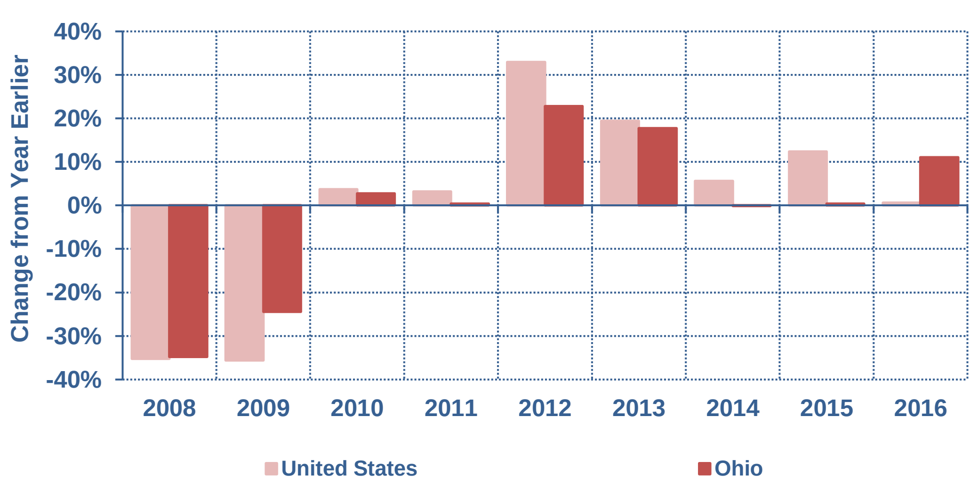
Chart 7: Personal Income
Billions of Dollars, Seasonally Adjusted Annualized Quarters



The number of Ohio homes sold and the average price both rose to all-time highs in 2016.

The Ohio statewide housing market had a very strong 2016. Housing construction growth increased substantially while the nationwide rate slowed, as indicated by building permits data for new privately owned units (Chart 8). Ohio home sales were an all-time high in 2016 by both unit sales and average price.[16] Both measures eclipsed previous records set in 2005. The average home sales price in Ohio was $163,503 in 2016, with all regions experiencing higher prices than in 2015.

Chart 8: New Privately Owned Housing Units
Authorized by Building Permits



[16] Ohio home sales data are from the Ohio Association of Realtors.

Economic Forecasts

The following are forecasts of key economic indicators that serve to illustrate the economic environment in which LSC state revenue forecasts for the next biennium were made. The forecasts are point estimates, which do not indicate the sizable, and varying, uncertainty involved in each forecast. Some of the indicator forecasts were used as direct inputs of various LSC econometric models used to make state revenue forecasts. Therefore, LSC's forecasts for state revenues also reflect the inherent uncertainties of economic indicator forecasts. Economic indicator projections are taken from IHS Economics' baseline forecasts released in December 2016, with the exception of Ohio personal income. Ohio personal income projections are based on an alternative forecast from IHS Economics which takes Ohio's recent personal income tax withholding performance into further account.

The first line in each table contains quarter-by-quarter projected changes of the indicator at an annual rate. The second line contains year-over-year projections of the indicator averaged for the fiscal year. The unemployment rate tables are IHS Economics' unemployment rate projections for the quarters indicated (first line) and the average of the quarters in each fiscal year (second line).

U.S. Gross Domestic Product

U.S. real GDP is projected to increase about 2.5% annually on average in the next biennium, as shown below.

U.S. Real GDP Growth

	2017				2018				2019			
Forecast	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
	------------percent change at annual rate------------											
Quarterly	2.4	2.4	2.2	2.2	3.3	2.6	2.6	2.4	2.4	2.0	2.0	1.9
Fiscal Year		2.0				2.4				2.6		

Ohio Gross Domestic Product

Economic growth in Ohio is expected to continue through 2019 but at a slower pace than the nation. Ohio real GDP is projected to increase about 1.8% annually on average in the next biennium.

Ohio Real GDP Growth

	2017				2018				2019			
Forecast	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
	------------percent change at annual rate------------											
Quarterly	1.8	1.8	1.5	1.6	2.7	1.7	1.8	1.8	1.8	1.5	1.6	1.6
Fiscal Year		1.5				1.7				1.9		

U.S. Inflation

IHS Economics' December baseline forecast projects the consumer price index rate of increase to peak in the third quarter of calendar year 2017, and average about 2.4% annually in the next biennium.

U.S. Consumer Price Index Inflation

	2017				2018				2019			
Forecast	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
	percent change at annual rate											
Quarterly	2.0	2.4	2.9	2.1	2.0	2.6	2.4	2.3	2.5	2.5	2.6	2.6
Fiscal Year		2.0				2.5				2.4		

U.S. Personal Income

Nationwide personal income is projected to grow about 5.2% annually in the next biennium. These growth rates are based on the dollar amounts of income, not adjusted for inflation.

U.S. Personal Income Growth

	2017				2018				2019			
Forecast	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
	percent change at annual rate											
Quarterly	4.5	5.0	4.8	4.9	5.7	5.4	5.1	5.2	5.9	4.8	4.8	4.7
Fiscal Year		4.3				5.0				5.3		

Ohio Personal Income

Income to persons who reside in Ohio also is forecast to grow in the next biennium, at 4.2% annually on average, a reduced pace of growth compared to the U.S. These projections reflect an alternative, slightly more pessimistic forecast from IHS Economics relative to their December baseline forecast.

Ohio Personal Income Growth

	2017				2018				2019			
Forecast	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
	percent change at annual rate											
Quarterly	3.6	4.2	3.8	3.9	4.9	4.4	4.1	4.3	5.2	4.0	4.0	3.9
Fiscal Year		3.1				4.1				4.4		

U.S. Unemployment Rate

IHS Economics' December baseline forecast projects the nationwide unemployment rate will decline slowly through the next biennium.

U.S. Unemployment Rate

	2017				2018				2019			
Forecast	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
	percent of the labor force											
Quarterly	4.7	4.6	4.6	4.5	4.4	4.3	4.2	4.2	4.1	4.1	4.1	4.1
Fiscal Year		4.7				4.4				4.1		

Ohio Unemployment Rate

Ohio's unemployment rate is also projected to decline throughout the next biennium, as shown below.

Ohio Unemployment Rate

	2017				2018				2019			
Forecast	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
	percent of the labor force											
Quarterly	4.7	4.7	4.6	4.6	4.6	4.5	4.4	4.3	4.3	4.2	4.2	4.2
Fiscal Year		4.7				4.6				4.3		