The Minnesota Economy: Economic Powerhouse?

Regional Council of Mayors
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Economic Powerhouse

“Minnesota has emerged as an economic powerhouse as shakier finances and slumping prices for oil and agricultural commodities jolt the budgets of neighboring states.”*

MN Jobs vs. US Jobs

• Movements in the Minnesota economy are highly correlated with movements in the US economy—it could hardly be otherwise!

• Minnesota employment did not decline as much as US employment did during the Great Recession, and it recovered much faster.

• However US employment growth has now caught up with Minnesota’s.
Total Nonfarm Employment: MN vs. US
Cumulative % Change of Jobs from the Business Cycle Peak

Sources: BLS and DEED
MN Unemployment vs. US Unemployment

• Historically the Minnesota unemployment rate was about 1.5% lower than the US rate, but the spread declined during the first decade of this century.

• In recent years the spread has returned—and it’s a good thing! If Minnesota had the US unemployment rate, almost 40 thousand jobs would be lost.

• Renewed growth of the labor force is encouraging, but neither the US nor Minnesota has yet achieved full employment.
Civilian Unemployment Rate (%): US vs. MN

Sources: BLS and DEED
Critical Policy Choices

• For a long time Minnesota has emphasized investment in “human capital”—i.e., education. This is far more fundamental than a “diverse” economy.

• More recently Minnesota has made some important reforms to budget policy.
Human Capital

- Minnesota has a huge advantage in education, relative to the US and also the neighboring states in the Upper Midwest.
- Minnesota leads the neighbors only slightly in high-school education. But it has a massive lead in higher education. Almost certainly this is the main driver of the “powerhouse.”

### Educational Attainment

**Age 25+ Years**

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<tr>
<th></th>
<th>IA</th>
<th>MN</th>
<th>ND</th>
<th>SD</th>
<th>WI</th>
<th>US</th>
</tr>
</thead>
<tbody>
<tr>
<td>HS Graduate or Higher</td>
<td>91.3</td>
<td>92.3</td>
<td>91.3</td>
<td>90.7</td>
<td>90.8</td>
<td>86.3</td>
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<tr>
<td>BA Degree or Higher</td>
<td>26.4</td>
<td>33.2</td>
<td>27.3</td>
<td>26.7</td>
<td>27.4</td>
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Budgeting

• Unlike past years, Minnesota now uses a statistically rigorous procedure to determine the budget-reserve target and an automatic allocation to the reserve when forecast surpluses arise and the actual reserve is less than the target.

• Accordingly, earlier this month $594 million was allocated to Minnesota’s budget reserve, raising it to $1.597 billion—an all-time high. At 3.8% of FY 2016-7 general fund non-dedicated revenues, this is only 1.0% short of the 4.8% target.

• As a result a recent study by the Pew Charitable Trusts cited Minnesota as having the most rigorous process of any of the states for setting a reserve target and for achieving it.*

Better Budgeting

• Unfortunately budget forecasts for “out-years” continue to bias the balance toward a surplus by including inflation in revenue projections while (mostly) excluding it from expenditure projections.

• In the official forecast released on December 3, FY 2018-19 is projected to have a $2.046 billion surplus—but $1.694 billion is due to the inflation bias.
Challenges

• The outlook for the US economy looks good for the next year or two—modest growth, extremely low inflation, and no recession in sight.

• But expansions rarely last as long as this one has.

• Minnesota’s new budget procedures are the best in the US....

• But the inflation bias makes a future fiscal crisis more likely than it should be.