



# Oklahoma Economic Report™

News and analysis of Oklahoma's economy

A publication of the Office of the State Treasurer • Treasurer Ken Miller, Ph.D.

## Texas envy?

When the Texas governor tossed his cowboy hat in the ring for president, he touted his state's unique and enviable position as the fastest job-creating state in the nation. And now the national spotlight is on Texas, with policymakers examining why its economy is booming and if its success can be replicated elsewhere.

Oklahoma is familiar with the over-the-shoulder glances to the south. For decades state leaders have admired the economic strengths of our neighbor and sought to make Oklahoma more competitive with Texas. In addressing

policy issues such as right-to-work, worker's compensation, tort reform, tax reform, teacher pay, and business incentives, state leaders have called for "Texas-plus" plans. Governor Frank Keating led the charge 11 years ago in his State of the State address with the political rally cry to beat Texas in something other than athletics. Similar calls are still made today.

Depending on one's perspective, Texas has either been a thorn in Oklahoma's side or a burr beneath its saddle – an annoyance or a motivator. Some have questioned the efficacy of modeling

policy after a state so dissimilar in population and geography. Others contend the competition with Texas has spurred Oklahoma to be more prosperous.

While all states compete against each other in attracting business and residents, the competition grows a bit fiercer among states sharing borders. Considering the ease in which former Oklahoma-based companies have relocated to Texas, our state's interest in Texas and its policies can be justified.

While the pundits debate the applicability of Texas' success to the rest of the nation, Oklahoma policymakers know Texas' ability to create new jobs is

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### By the numbers: Oklahoma vs. Texas

#### Taxes & Economy

|  | <u>OK</u>               | <u>TX</u>               |
|--|-------------------------|-------------------------|
| Population:                                | 3,751,351               | 25,145,561              |
| Gross state product (GSP):                 | \$147.5 b               | \$1.207 t               |
| State and local gov't spending (% of GSP): | 18.6                    | 15.6                    |
| State and local tax burden (% of income):  | 37 <sup>th</sup> lowest | 45 <sup>th</sup> lowest |
| Property tax collections per capita:       | \$582                   | \$1,393                 |
| Annual personal income per capita:         | \$35,969                | \$38,953                |

#### Education

|   |         |         |
|---|---------|---------|
| Percent of state budget to K-12:        | 35      | 41.7    |
| K-12 percent of revenue from state:     | 53.7    | 46.4    |
| Public school expenditure per pupil:    | \$8,348 | \$9,288 |
| Average ACT scores of tested graduates: | 20.7    | 20.8    |

#### Health & Welfare

|  |      |      |
|--|------|------|
| Percent without health insurance for 1 year: | 18.1 | 26.1 |
| Active physicians per 10,000 population:     | 17.3 | 21.4 |
| TANF recipients as percent of population:    | 0.57 | 0.46 |

Sources: U.S. Department of Commerce; Bureau of Economic Analysis; U.S. Census Bureau; NEA Estimates Database, 2009; Taxpayers Network; Taxpayer Foundation; Administration for Children & Families



## Treasurer's Commentary By Ken Miller, Ph.D.



### Shaken or stirred

Today, Oklahoma continues to embrace recovery while our nation continues to stall. Our state has outperformed throughout the upturn, but cannot swim against tide forever. Oklahoma needs a strong national economy, just as the nation needs a resilient global economy.

Persistent economic weakness has prompted discussion of another round of “stimulus.” Such thinking is counter to the fundamentals of capitalism. The private sector is meant to play the primary role in job creation while the public sector is to cultivate an environment conducive to entrepreneurship, investment and growth.

Stimulus III again calls for extending temporary payroll tax cuts, prolonging unemployment benefits and increasing government spending. Granted, fiscal maneuvers are limited to only two tools: taxing and spending. But, how these tools are used can vary greatly depending on whether one adheres to the ideology of either Keynes or Friedman.

Keynesians believe government spending initiatives stimulate an economy back to its potential by impacting demand. Friedmanites reject this notion, believing

only permanent changes in income adequately influence demand and instead rely on monetary policy to influence economic activity.

Bureau of Economic Analysis data on the 2008 tax rebates bolsters Friedman’s argument. The spike in disposable personal income derived from the rebates resulted in a slight temporary bump in consumer spending. Regrettably, Oklahoma embraced this folly in 2005 by issuing \$45 individual tax rebates rather than addressing significant issues like tax reform, dilapidated infrastructure or debt.

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**“The private sector is meant to play the primary role in job creation...”**

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The world has changed considerably in the 60 plus years since John Keynes and Milton Friedman developed their theories. Today the global economy is increasingly complex, interdependent,

dynamic and technological, trading more than ever on expectations—which underscores why confidence is an economic determinant and why markets perform best under certainty or at least predictability.

Although recent data, economic evolution, and consumer behavior appear more congruent with Friedman, it would be disingenuous to suggest that the trillions injected into the economy have produced zero short-term benefit, even if it is long-term prosperity that we should seek.

It is unlikely even the purest of ideologues would take responsibility for certain depression had there been no policy intervention. Surely an economy based on free market principles would eventually return to equilibrium, but at what costs in jobs, wealth and productivity in the interim? It seems the rational debate should center on what type of policy intervention would be most beneficial to a market-based economy, rather than if there should be any at all.

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## Shaken

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From the onset of the recession, there has been no cohesive, long-term economic strategy. It is time for policymakers to return the lead role to the private sector by stirring it into action with consistent pro-growth tax policies, sustainable budget policies, efficient capital markets and a stable regulatory environment.

Churchill stated that America can always be counted on to do the right thing after it has exhausted all else. Having already shaken our markets with many erratic and desperate attempts to kick-start the economy, perhaps policymakers will now realize that stirred is preferred.

## Envy

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in direct competition with our own.

### Phenomenon or fluke?

The so-called “Texas Miracle” refers to the state’s post-recession strength that has accounted for 47 percent of the nation’s job creation since June 2009.

According to the Bureau of Labor Statistics (BLS), more than 90 percent of those jobs were created in the private sector. Of the 328,000 new jobs, only 31,000 were in the public sector.

Over the last decade, Texas added more jobs than all other states combined.

Detractors contend the jobs created aren’t high-paying quality jobs and cite statistics ranking Texas as home to the highest percentage of minimum-wage

workers in the nation. BLS reflects Texas’ median hourly wage is \$15.14 compared with the national median of \$16.27.

In an attempt to show that Texas’ policies are not driving economic growth, it’s been pointed out that Texas’ current unemployment rate of 8.2 percent, while almost a percentage point below the national average, ranks behind states like New York that have opposing governing policies.

Texas policy advocates rebut that while New York’s unemployment is slightly lower than Texas’, New York has lost more than 1.5 million residents while Texas has gained nearly 900,000. Texas’ unemployment rate has been at or below the national average for 55 consecutive months, as reported by the state’s comptroller.

Defenders of Texas policy say the real “Texas Miracle” is that the state’s unemployment rate has remained below the national average despite absorbing other states’ unemployed who are migrating to Texas in hope of better opportunities.

Critics of the Texas model say job creation alone is far too simplistic to measure the success of a state’s economy. They contend that median wages, skill of workforce, number of start-ups, availability of capital and quality-of-life measures such as health care and education should be considered alongside actual job growth in judging the success of a state’s economic policies.

### The Texas Model

Texas policymakers credit the state’s success to long-standing adherence to low taxes and limited government,

principles historically popular with both Texans and Oklahomans.

But Texas has also created incentive programs that have successfully lured businesses and new jobs to the state, contributing to household income and state revenue. Like Oklahoma, where raising taxes is not a viable option, economic policy largely revolves around spending priorities.

**“ . . . Texas’ ability to create new jobs is in direct competition with our own.”**

The bulk of the state’s solution to its approximate \$20 billion budget shortfall was to cut spending.

Texas’ history of providing a low-tax, low-regulatory environment and its pro-business attitude provide confidence to businesses that relocate or to new startups.

The Small Business & Entrepreneurship Council’s 2010 Small Business Survival Index ranks Washington D.C. as the least-friendly for entrepreneurship, based on the costs and burdens governments place on small business and entrepreneurs. New Jersey and New York are behind D.C. The council ranks Texas as the third most friendly state

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## August gross receipts & General Revenue Fund comparison

A comparison of the Treasurer's September 6 Revenue Report and State Finance's September 12 General Revenue Fund (GRF) allocation report illustrates key differences.

August gross receipts totaled \$842.9 million, while the GRF received \$414.8 million or 49.2 percent of the total. In July, the GRF received 45.5 percent of the gross.

The differences are due to variances in the transfer of funds for rebates and dedicated funding.

In August, the GRF received:

- 69.2 percent of personal income tax
- No corporate income tax revenue of more than \$5 million collected
- 44.9 percent of sales tax receipts
- 79 percent of the gross production (GP) tax on natural gas
- No GP oil tax revenue of \$55.6 million collected.
- 33.1 percent of motor vehicle tax collections
- 43.6 percent of other revenue sources

Collections from tribal gaming generated \$11.3 million during the month.

Insurance premium taxes generated \$2.5 million in July.

Energy industry and income collections fuel growth

## Economy hot in August

Oklahoma's economy matched the temperatures in August, as revenue collection grew at a double-digit pace in spite of concerns of a worldwide slowdown, State Treasurer Ken Miller said as he released the state's monthly revenue report.

August collections were 15.2 percent higher than in August of last year, nearly matching the year-over-year growth of 15.5 percent recorded in June. Monthly collections moderated slightly in July at 6.8 percent growth from the prior year.

Miller said collections over the past 12 months total \$10.37 billion, the highest level since July 2009 when 12-month collections totaled \$10.402 billion.

"During the prolonged recession, 12-month collections in Oklahoma dropped by more than \$1.9 billion between December 2008 and February

2010," he said. "As of August, we have recovered \$1 billion, or more than 50 percent of that lost economic activity."

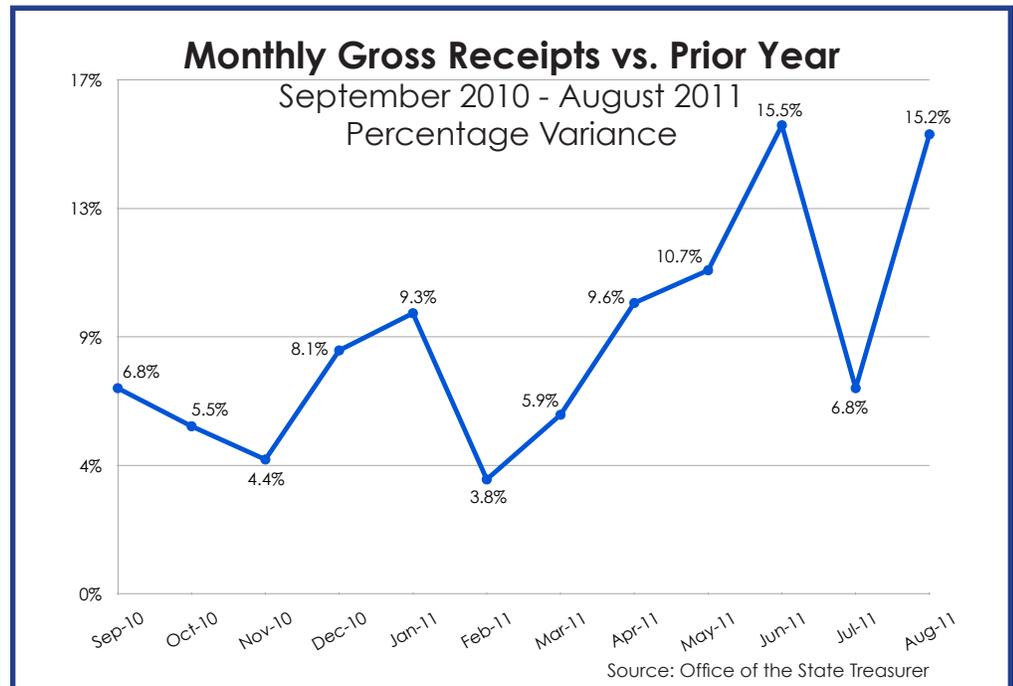
### State economic signs remain positive

Miller said other recent data signal a positive economic outlook for Oklahoma, albeit somewhat subdued.

The August Oklahoma Business Conditions Index shows expected growth in the coming months. However, the index at 56.8 is down from July's rate of 61.9, showing consumer confidence has waned. A number above 50 indicates economic growth, while a lower number anticipates contraction.

"Understandably, people are concerned about what they're hearing on the news about the credit downgrade, sovereign

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## Revenue

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debt problems, geopolitical events and volatility in the stock market,” Miller said. “However, many Oklahomans recognize that the economy here has performed much better than elsewhere.”

July statewide unemployment rose to 5.5 percent, or by one-tenth of one percent from June, while county-by-county unemployment rates dropped in all but five of Oklahoma’s 77 counties.

Gross production taxes on oil and natural gas are showing the biggest gains in revenue collections, measured

both over the past 12 months and for August, but some slowdown is expected in the coming months.

Gross production taxes, also known as severance or extraction taxes, are paid two to three months after the production occurs. Three months ago, crude oil was selling for 10 to 15 percent more than today’s prices, which means gross production collections in August are reflective of those higher prices.

“While natural gas prices have remained steady over the past several months, the drop in crude oil prices is expected to be reflected in state collections,” Miller said. “Unless crude oil production volume was increased when the price

“**... many Oklahomans recognize that the economy here has performed much better than elsewhere.**”

dropped, less gross production revenue will be paid to the state during the next quarter.”

## Envy

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to entrepreneurs. Oklahoma ranks 21<sup>st</sup> among the 50 states and D.C.

Texas is also one of the few states with no income tax. According to the Tax Foundation, Texas has the 45<sup>th</sup> lowest state and local tax burden as a percentage of state income among the 50 states. Resident-losing states like New Jersey and New York rank 1<sup>st</sup> and 2<sup>nd</sup> highest in state and local tax burdens, respectively.

The pro-business rankings coupled with personal tax burden ratings suggest policy impacts a state’s ability to create jobs by signaling to job creators a higher likelihood of success.

Tax structure alone cannot be credited for a state’s level of economic success – each state’s economy has unique variables. For example, Texas and

Oklahoma have abundant natural resources, particularly oil and gas, but Oklahoma lacks Texas’ geographical mass, population density, coastline and capital.

In 2008 the Texas Public Policy Foundation published a comparison of Texas to California, the two most populous states and “economic heavyweights” with sizeable geographical strengths, and found that tax, fiscal and regulatory policies resulted in two very different outcomes.

The study, conducted by Arduin, Laffer & Moore Econometrics, predicted Texas’ policies would make it “more resilient” to the economic downturn and “provide powerful tailwinds for the Texas economy going forward.”

They also surmised that California’s rising spending, regulatory burdens and taxes would result in weaker economic performance and less relative wealth growth. Their predictions appear to be on target.

### Lessons for Oklahoma

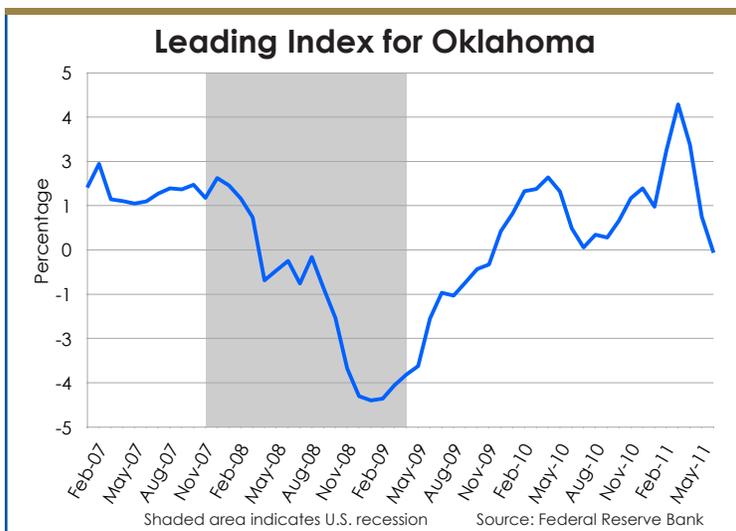
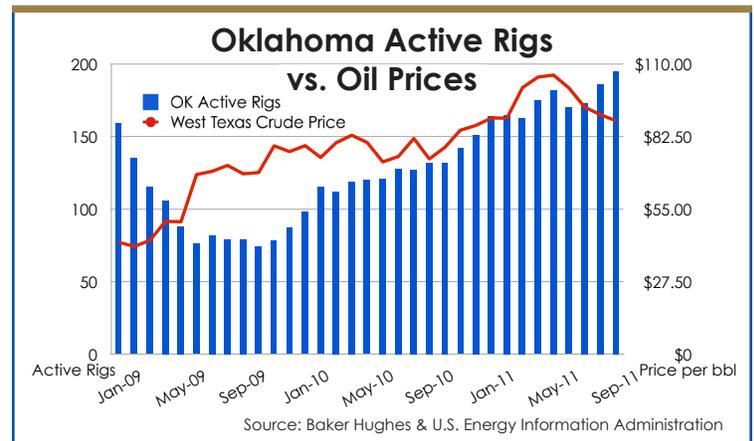
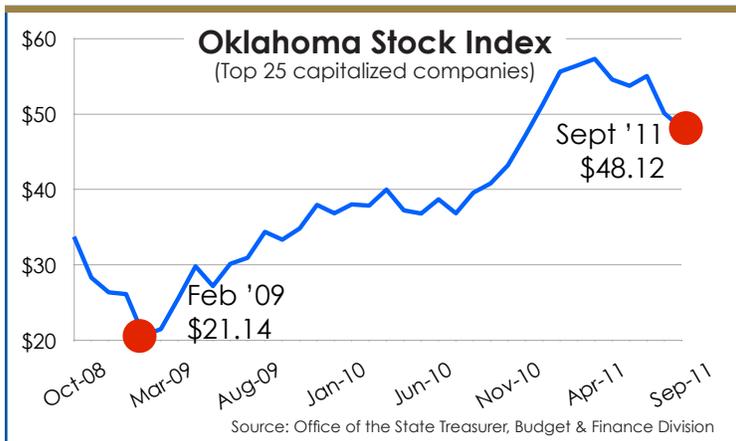
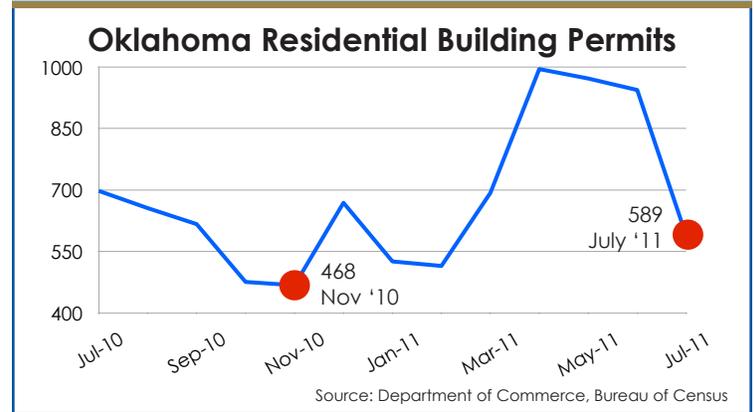
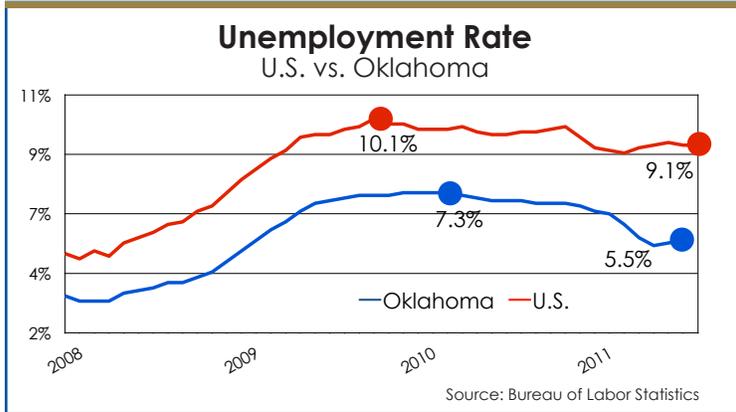
States such as Texas and Oklahoma are weathering the economic storm better than the rest of the nation due, in large part, to their natural endowments of oil and gas. However, there is more to the story.

Other states, including California, also have abundant natural oil and gas reserves. According the U.S. Bureau of Land Management, California has some of the most productive oil fields in the nation. Yet, California is among those states faring poorly during the recession’s recovery. Even the advantage of natural resources cannot keep a state afloat if its policies don’t encourage development of those resources.

Comparative evidence of states’ performances during and after the recession indicates correlation between economic performance and public policy. And while fiscal policy cannot and should not be created in a vacuum, the policies of competitors must be part of the conversation.



## Economic Indicators



### Interest Rate Forecast

68 Economists

|                            | 3Q 2011 | 4Q 2011 | 1Q 2012 | 2Q 2012 | 3Q 2012 | 4Q 2012 |
|----------------------------|---------|---------|---------|---------|---------|---------|
| <b>Fed Funds Target</b>    | 0.25%   | 0.25%   | 0.25%   | 0.25%   | 0.25%   | 0.25%   |
| <b>3-M LIBOR</b>           | 0.30%   | 0.33%   | 0.34%   | 0.35%   | 0.40%   | 0.40%   |
| <b>Treasury Notes</b>      |         |         |         |         |         |         |
| <b>2-Year</b>              | 0.20%   | 0.30%   | 0.35%   | 0.45%   | 0.55%   | 0.65%   |
| <b>10-Year</b>             | 2.20%   | 2.35%   | 2.52%   | 2.75%   | 2.80%   | 2.95%   |
| <b>Treasury Bonds</b>      |         |         |         |         |         |         |
| <b>30-Year</b>             | 3.57%   | 3.65%   | 3.81%   | 4.00%   | 4.06%   | 4.25%   |
| <b>Economic Indicators</b> |         |         |         |         |         |         |
| <b>Real GDP</b>            | 2011    |         | 2012    |         | 2013    |         |
|                            | 1.60%   |         | 2.20%   |         | 2.50%   |         |
| <b>Unemployment</b>        | 9.00%   |         | 8.80%   |         | 8.30%   |         |

Source: Media forecasts for key economic indicators as surveyed by Bloomberg, September 14, 2011