

**Children's Issues Briefing**  
**February 21, 2008**  
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Last week, Governor Pawlenty gave his state of the state speech in St. Cloud, and he said that “our ambition as leaders should be to make this state the best place in America – the best place in the world – to live, work and raise a family.”

I think we can all agree with that statement. Where we may disagree is in how we achieve that goal.

All of you are here because you see our children and our youth as your top priority – and a key to making this state great. But there are others who – for equally valid reasons – are focused on jobs, or the elderly, or health care, or the environment, or transportation, or higher education, or any other number of issues – as the key to a successful state.

And all of you are basically competing for the same limited resources in the same challenging economic environment.

Today you are talking about a lot of great policy ideas to help our children and our youth...policies that would truly make this state a better place.

But legislators are surely going to tell you to keep your expectations realistic because the state is facing a deficit and we'll be lucky if we can keep current programs whole. And that's a valid point.

But I feel like that is where the conversation has been stuck for the last five or six years. Great ideas hitting a frustrating reality...and we slip further away from Pawlenty's vision – and our vision – of making this the best place in America.

So, I have a different challenge for you. And it's actually the same challenge I would issue standing here – or in front of a group of environmentalists – or in front of the chamber of commerce. Which is to act beyond this biennium and this deficit. And to act beyond even the next biennium and the deficit that awaits us there. And note that I say “act” – not think – but act.

Pawlenty spoke in his state of the state about Minnesota and how well it does on so many rankings. But we aren't a leader because of the choices we made today, or because of the rhetoric of policymakers in the past...We have been thriving as a state because decades ago – people had a vision and they acted on it.

Paul Anton – the chief economist at Wilder Research – pointed out a hearing the other day that it will take us too long to find out if we are losing our competitive edge. By the time we see the evidence, it's too late to make a change. So we should stop measuring our success against the rankings, and start measuring it against our own expectations and aspirations.

So, what does that mean this session? How can we act beyond this deficit?

Well, the cold hard facts are that when the February Forecast comes out next Thursday, the state will be facing a deficit for this biennium even larger than the \$373 million predicted last November. And we will be looking at a growing deficit for the next biennium. Last November, the deficit was already projected to be \$200 million – without considering the impact of inflation.

But there are three things we can do to solve these immediate problems in a long-term way. We can maintain current levels of investments, use our reserves wisely, and we can put inflation back in the state's economic forecasts. Let me walk through these in more detail.

### **Maintain current levels of investment**

First, we should at least maintain current levels of investments. The first inclination in times of deficit is to cut government spending to bring the budget back into balance. But significant budget cuts are not a good idea – both in the short-term and the long-term.

In the short-term – we need that government spending to help stimulate our economy. It's about the only thing state government can do to help us through this rough patch...because every dollar that government collects goes right back out the door.

If you cut spending to fix a deficit, you are pulling those dollars away from services that were going to use those funds. And even more importantly, they were likely to spend those dollars in Minnesota. Two very prominent economists – a nobel prize winner and the current director of the Congressional Budget Office – have argued that during an economic downturn it is better to raise taxes in order to maintain government spending – particularly if you raise taxes on higher-income households. Those folks are likely to compensate by spending the same amount, but perhaps saving less. So then you hopefully preserve the stimulus effect of both government spending and consumer spending.

In the long-term, cutting spending is a bad idea because we need those public investments. Since the large deficits of 2003, I feel like Minnesota is a state suffering from “failure to thrive.” I don't think we are meeting our own expectations of growth and health – and we have yet to see how much permanent damage we will suffer as a result.

You have certainly experienced this problem in services for our children and youth – significant cuts to child care and other early childhood programs, K-12 funding struggling to keep up with inflation, tens of thousands of children without access to affordable health insurance, and state funding to help at-risk youth disappearing. We keep trying to make up some of that ground...but making progress is hard work.

It's for the sake of these kinds of services – and so many others that are critical to keeping this a great state – that we need to do what we can to at least maintain our current levels of investments rather than resorting to significant spending cuts as the main way of fixing our deficit.

I am not trying to defend every dollar the state spends. It may be wise to shift some funding around. But we should be slow to shrink the size of the pie we have to work with.

### **Use our reserves wisely**

The second thing we can do is to use our budget reserves wisely. The state currently has just over \$1 billion in reserves – which is about 3% of our total general fund budget.

The purpose of building up a healthy level of reserves is to allow policymakers time to make good budget decisions in the face of challenging economic circumstances. So, instead of having to make drastic choices to balance the budget – policymakers can respond in a more deliberative way.

And reserves can buy time to implement a comprehensive solution. For example, even if you raise revenues to fill a budget gap, it will take time for those dollars to start flowing in. Reserves can be used to temporarily fill the gap until the new revenues arrive.

It is a rainy day – it does make sense to use some our rainy day funds. But not as a way of avoiding making the tough decisions. Not just to delay the trouble until the next legislative session. Using reserves cannot solve our problem...but they can buy us time to implement a real solution.

### **Restore inflation in the forecast**

The third thing we can do to act beyond this deficit is to restore inflation in the state's economic forecasts. As I've mentioned already, the Department of Finance prepares these major forecasts twice a year to give us a sense of our state's fiscal health. And, although the forecast does include the impact of inflation on the state's revenues...the 2002 Legislature passed a law which prohibits including the influence of inflation on the spending side. But leaving out inflation gives policy makers and the public an unrealistic idea of where we are.

For example, just think back to one year ago. The headlines after last year's February Forecast proclaimed that the state had a \$2 billion surplus. It's not surprising that some people thought that happy days were here again.

But, \$1 billion of that surplus was just one-time revenue – we couldn't use it to fund on-going services. And the other \$1 billion? Well, that was just about enough to cover the cost of inflation. In other words, just enough to keep up with the investments we were already making.

If last year's forecast had included inflation – the headlines would not have painted such a rosy picture. We would have seen that surpluses weren't going to last long into the future. Adding inflation forces legislators to consider whether budget choices – be they spending increases or tax cuts – are sustainable into the future based on our current level of revenues. Granted, including inflation might not have prevented the deficit we face now – but it could have signaled to us to take a more cautious strategy about the future.

Remember adding inflation back into the forecast doesn't commit us to spending that money. But it does give policymakers the information they need to make sustainable budget choices.

### **Conclusion**

I know we're here today to talk about children's issues – and maybe this felt like a diversion from that. But I think you all recognize that your issues are being debated in a larger context...and if you aren't aware of and influencing this context, you're going to have a tough time making progress.

So, if we could get policymakers

...to recognize the short-term and long-term value of – at a minimum - sustaining current public investments

...encourage them to use the reserves only to buy time to implement long-term solutions, and

...get them to restore inflation in the forecast to provide us all with a more accurate assessment of our state's future fiscal health

then we might start to make some sustained progress on the issues important to all of you.

Of course, these are principles – and some may even call them ideals. But we are allowed to have principles and ideals – and we should be talking about them.

I'm not naïve – I know we face real challenges. In the short-term, we face a possible recession. In the longer-term, we need to overcome growing racial disparity and income inequality...Greater Minnesota is struggling to keep jobs and people...and those baby-boomers keep getting older.

But previous generations of policymakers faced challenges too and were able to make choices – like heavy investments in education – that laid the groundwork for our recent economic prosperity. And generations to come will look back at the choices made by current policymakers. Like Pawlenty challenged us in his state of the state – are we leaders who will keep this state great? Can we make choices that not only meets these challenges – but maybe even turns them to our advantage in the future? I think we can - but not if our vision only extends from one deficit to the next.