

MAINE ECONOMIC OUTLOOK

The outlook for Maine economic growth is largely unchanged from recent forecasts: still very slow employment growth through the next 12 months with the prospect of a pickup in pace in the 12-36 month horizon, then a return to long term trend. Maine has been struggling to get three consecutive quarters of employment growth since the recovery from the Great Recession began, a milestone which may have been reached in 2013. The housing market is recovering, though the only measure that will return to pre-recession levels is median house price. But Maine's economy is facing yet another significant headwind as an aging population will require much more net in-migration than recent trends would support. After the U.S. growth rate, Maine's net in-migration is becoming the principal determinant of growth prospects.

Maine's relationship to Boston is a combination of integration and differentiation. Over the past 40 years, Maine has actually grown faster in employment than Massachusetts, particularly in Southern Maine. This reflected the increasing diversification of Maine's economy as Maine grew to resemble Boston more closely. It also reflected import substitution development in Maine relative to Boston, particularly in the health care sector. Maine's biotechnology sector is a growing part of the New England biotechnology sector headquartered in Boston, and Boston remains a major source of Maine's tourist trade.

1. Maine Outlook

At the end of 2013, Maine has managed to claw back about 8,000 of the 28,000 wage and salary jobs lost in the Great Recession. It has taken nearly four years to achieve that level of growth, meaning an average of about 2,000 jobs a year. Over the five years from 2007 to 2012, employment declines outpaced growth so that average annual growth rates over this period averaged -0.7%. Over 2012 and the first half of 2013 average growth has only been 0.1% per quarter.

Since 2010, Maine has only managed to have two consecutive quarters of employment growth three times, once at the end of 2010 to the beginning of 2011 and in the first half of both 2012 and 2013. The big question in the fall of 2013 is can Maine break this two-quarter limit and extend to three, four, or maybe even sustained employment growth. July 2013 gained 3,000 jobs over June on a seasonally adjusted basis, but August saw a loss of 500 jobs, so the third quarter depends on September numbers, which are delayed because of the federal shutdown.

Nonetheless, the prospect is the third quarter will come through as possible, marking the first break with the two-quarter limitation. The forecast, in fact, is for positive employment growth in all quarters through the period, though of course this is partly an artifact of the model, which cannot predict future crises that may occur. The most immediate threat is obviously the fourth quarter of 2013 when the effects of the shutdown/debt ceiling crisis will be concentrated. The forecast shows continued growth in the fourth quarter, but it is a mere 700 jobs, so it will be a near run thing if growth manages to be sustained through the end of 2013.

The outlook for mid-2013 to the end of 2017 is for sustained growth, averaging 0.7% per quarter or about 1,000 jobs on average. The forecast is for 617,000 jobs at the end of 2017, which would not bring Maine back to the pre-recession level of 620,000 jobs. Leading sectors in the recovery will be professional & business services and leisure & hospitality. Much of the growth in the latter category will be in Portland, where three major hotels are under construction for opening in early 2014. Manufacturing will continue to struggle, though there is a possibility that the

projected slight decline could turn into a slight positive if housing construction in the northeast could pick up enough to increase demand for lumber.

Three sectors show significant weakness relative to past forecasts. Government will continue to shed employees, particularly at the local level as the state ends revenue sharing and cuts aid to local schools. Retail trade employment will only grow by a little more than 2000 jobs, a relatively meager growth in a sector with more than 80,000 employees. This reflects national growth trends in retail, which is local retail is increasingly challenged by internet sales and the era of big box expansion (which came late to Maine) is essentially over.

The other major sector showing much slower growth than expected is education and health, which is primarily composed of the health care and social assistance industries. This has been the major jobs-producing sector for Maine (as elsewhere) and so the slow growth projected here represents a real change of pace. The outlook partly reflects a reversal of employment growth in hospitals (consistent with national trends), particularly in smaller hospitals, and partly a slowing of growth from demographic factors (discussed below). The Affordable Care Act implementation will expand the market for health care, as will an aging population, but the effects of the former are uncertain at this point (particularly since Maine is one of the states that has rejected the Medicaid expansion), while the major effects of an aging population on health care will begin to really manifest themselves just past the forecast period.

As with the U.S., the housing sector is a key part of the recovery prospects. The good news is that the existing homes market is definitely on the mend, with a fairly steady rise in median home prices already underway and projected to continue through the forecast period. Existing home sales have returned to near 2006 levels and, while these will slow somewhat as the lingering supply and demand effects of the crash are worked through, existing home sales should be fairly active, although population growth will limit further growth in existing home markets.

New home construction, as measured by construction permits, have also come off the bottom. New home construction fell by more than 60% from the peak in early 2006, and has begun to recover. The forecast is for return to a level of new housing permits at about historic levels of 4,500-5,000 per year, a level still 20% below peaks. National trends show a slowing of housing construction from 2015 on and these are reflected here.

The rate of new housing construction growth exceeds that of existing housing sales, which may seem somewhat surprising given the slow population growth forecast, but there are two reasons for this. One is the severe drop in construction during the recession, which was far below historic norms and thus called forth a somewhat robust rate of growth in the early recovery period. A second reason is the relatively large proportion of housing in Maine built for seasonal occupancy, which tends to support a housing construction in excess of that needed for population growth.

The prolonged period of weak employment growth is having an effect on the Maine economy in that the weak labor market is contributing to very weak income growth, restraining growth in many local industries. Over the forecast period, wage & salary growth will accelerate from 1.1% per year to 3.3% per year, but this still well behind the 4.1% per year growth prior to the recession. The result is that the share of personal income at the end of 2017 will be well below that in 2006 and still below that of the middle of the recession in 2010.

The component of personal income that is projected to grow is dividends, interest, and rent, which increases its share of personal income by 2% points. Much of this growth will be from the imputed rents of increasing housing prices. Transfer payments will increase drop its share of

income from 2010 to 2017, but only by a little more than 0.5%. This is perhaps the clearest signal of the prolonged weakness in the Maine economy which will continue to burden the state, most likely through the rest of this decade.

This prolonged weakness of the Maine economy imposed on it by a weak national economy is made all the more difficult because it is coming at a time when Maine is beginning to undergo a significant demographic transition, with the baby boom generation, which dominates Maine's age structure as in no other state, hitting the age for retirement and more than two decades of weak growth among younger people from outmigration and low birth rates yielding too few people to grow the workforce. In a way, the prolonged weakness in the labor market from cyclical factors will give Maine a little breathing room in terms of labor supply, but it will be very little room and it will be very temporary.

Most of this demographic transition will have its most profound effects beyond the current forecast horizon, but its significance is apparent even within the forecast period. Maine as a whole has not yet moved into a period of natural population decrease, though 14 of Maine's 16 counties have. Within five years the only population growth in Maine will come from net in-migration, and this will have significant implications because it will require a complete reversal of recent in-migration trends.

Net migration to Maine is heavily dependent on overall employment growth. There are occasional periods such as the late 1980s and the early 2000s when net migration substantially exceeds employment growth but the two have matched each other very closely since the bottom of the recession. In the forecast, the model projects that the economy will need an average of 3,400 people per year to move to Maine (net) over the next four years, but recent experience has been migration under 1,000 per year.

A midpoint estimate of net migrants equal to 2,400 net migrants per year is chosen for the forecast, which yields an employment forecast of 617,800 at the end of 2017. This leaves the Maine economy still short of the 620,000 job pre-recession level. Obviously the precise estimates are uncertain, but the implications of the analysis are that even a significant increase (more than doubling) in current migration patterns still does not yield a return to pre-recession employment levels. This issue will only grow in importance as the decade progresses.

2. Maine and Boston

Even today in parts of the Maritime Provinces of Canada, Maine and the rest of New England are known as the "Boston States", a term that originated in the 18th century when Boston really was the only community of economic importance in New England and Boston vied with Halifax for the leadership of British North America. Accounting for more than 40% of the gross output of the entire New England region, the Boston metropolitan area clearly has a key role in the entire region. But, at least from Maine's perspective, it is a changing role in which Maine has become both more integrated with and more separate from the Boston economy.

Maine as a whole and Boston's closest neighbors in Maine have consistently outpaced Boston in terms of employment growth over a period now extending back more than forty years. This is largely the maturing of the Maine, particularly southern Maine economy as Maine has evolved from being an economy heavily dependent on low-wage manufacturing and natural resources to a diverse post-industrial economy.

It is also a matter of Maine's economy providing more and more services within its economy that may once have been provided from Boston. This includes the increasingly diverse and competitive professional and business services sector, the spread of national retailers to Maine, and in particular, the health care sector.

All three areas kept pace with each other through the early part of the last decade, but both Cumberland County and Boston pulled ahead in the latter part of the decade. Health care in Cumberland County was more affected by the recession than in Boston, but in 2011 both had grown over 2001 by nearly 25%. In Cumberland County this growth has come about by the opening of new specialized health centers, such as the Barbara Bush Children's Hospital, which brought to Maine services previously only available in Boston. Also important was the growth of a small but rapidly growing health research sector at such institutions as the Maine Medical Center. Portland does not have anywhere near the research strength of Boston, but it has significantly diversified its health sector to make it a regional center for northern New England.

The health-biomedical sector points to both aspects of the Maine-Boston relationship. The employment change data tells the story of how Maine has separated from Boston. But the growth of biomedical research in Maine is also part of the emergence of a biotechnology sector in Maine that is both distinct and an important part of the Boston biotechnology sector. The single largest area of research production in Maine is genetics and genomics, which is primarily the product of The Jackson Laboratory in Bar Harbor. Researchers and biomedical companies in Maine both compete and collaborate with researchers and companies in Massachusetts and beyond.

Maine remains connected to Boston as part of population change and tourism. A lot of people move between the Boston area and Maine in the summer; it is still our largest market for tourists as it has been since the 19th century.

Charles S. Colgan
Professor of Public Policy & Management
Muskie School of Public Service
University of Southern Maine
Portland, Maine 04104
207-780-4008
colgan@maine.edu