Center for COMPETITIVE FLORIDA
FLORIDA TAXWATCH

ECONOMIC COMMENTARY
A monthly look at Florida's Economy

The Disproportionate Effect of Sequestration on Florida

Brace yourself, Florida. This Friday, March 1, when federal spending cuts automatically kick in (i.e. the budget sequestration), defense spending will be cut by $500 billion over the next decade. The immediate cuts to the budget authority are $85 billion, and the Congressional Budget Office has indicated that spending will be reduced by $44 billion by the end of September 2013. This Economic Commentary details some of the effects of these automatic federal spending cuts on Florida.[1]

Besides direct effects on the military, these cuts will affect agencies such as the U.S. Customs and Border Patrol, the Federal Aviation Administration, and the Transportation Security Administration. The state of Florida, home to some of the largest ports of entry in the country and a large military sector employing nearly 100,000 active and reserve military, as well as 11,000 National Guard soldiers and airmen, will be highly affected by these cuts. It is incredibly important that everyone understands how detrimental these cuts will be to U.S.'s fourth largest economy and to its recovery from the Great Recession. Furthermore, the longer Congress waits to resolve this situation, the more uncertainty and volatility will be introduced into the market, and the more likely our economy will experience another recession, ultimately costing Florida jobs, making it more difficult for Florida's companies, and impacting Florida's budget.

People can't spend money in Florida when they're still in the Customs line.
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Direct Effects on Florida

There are three main effects that Florida should expect from the sequester: cuts to the payroll of Federal employees in our state; cuts to defense spending; and the direct and indirect effects of federal agency funding cuts on Florida's tourism industry.

Paychecks for more than 130,000 Federal employees in our state, which makes up approximately 12 percent of the total government employment in Florida, will be affected. Several federal agencies are planning on cutting jobs and imposing furloughs. As consumers, these employees will likely decrease their spending in times when consumer confidence is already sluggish.

[1] Florida TaxWatch previously addressed certain aspects of this issue in a December 2012 Special Edition of Florida CFO Jeff Atwater's publication *Florida's Bottom Line* article called "Navigating the Fiscal Cliff". The authors were Florida TaxWatch Chief Economist Jerry D. Parrish, Ph.D. and Florida TaxWatch Vice President for Tax Research Kurt Wenner.

The effect on the Florida defense industry will be larger. According to the 2010 Florida Defense Industry Economic Impact Analysis report by the Haas Center at the University of West Florida, defense-related spending (including both direct and indirect spending) was estimated to be responsible for more than $64.8 billion in Gross State Product (GSP) in 2010, and would total $67.7 billion in 2013, which is about 9 percent of the Florida economy. A national estimate by the 2012 Center for Regional Analysis of direct job losses due to the potential defense budget cuts shows that Florida will lose 41,905 jobs. Worse still, these cuts will place substantial pressure on Florida-based defense contractors and their subcontractors, many of whom operate small businesses that could be put out of business.

Some regions of Florida are more dependent upon military spending than others. Approximately 25 percent of Northwest Florida's regional output is driven by defense spending, compared to 13.7 percent in Northeast Florida, 5.3 percent in Central Florida and 2.8 percent in South Florida. Therefore, depending upon which areas of military spending are cut, the effect could be significant and have a much higher impact in some areas of Florida than others.

The sequester will also have direct negative effects on tourism. As the recent Florida TaxWatch Report *Investing in Tourism* points out, there are more than 1 million Floridians employed in our tourism industry. The effects on the airline industry and customs clearance alone may have significant effects on Florida's tourism industry. Janet Napolitano, current Secretary of Homeland Security, recently explained to the Senate Appropriations Committee that these cuts will translate into longer wait times and less security at Florida points of entry. Both factors are likely to decrease visitation to our state.

Percentage of Overnight Visitors from Foreign Countries

YEAR	To FLORIDA	To MIAMI
2009	9.6%	47.6%
2010	11.1%	48.1%
2011	12.6%	48.3%

Source: Visit Florida, available at http://media.visitflorida.org/research.php

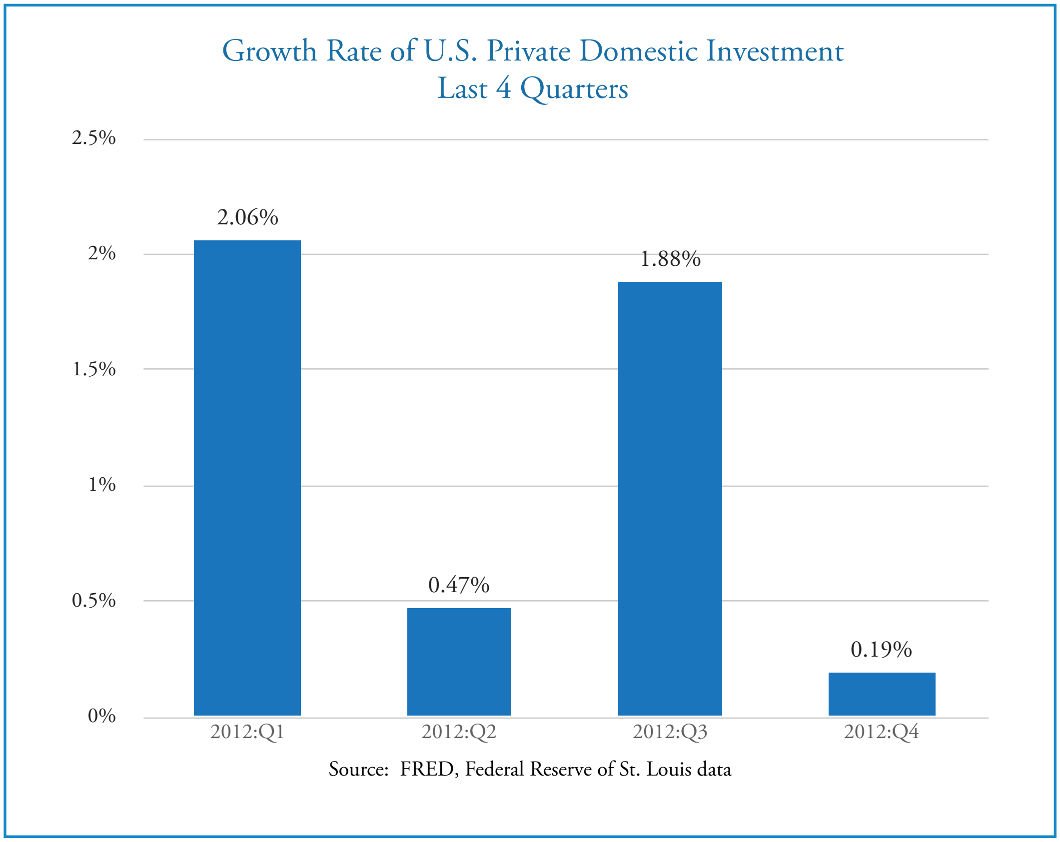
Miami Loses the Most in Tourism

Without a doubt, the hardest-hit area for Florida's tourism industry will be Miami. According to the Greater Miami Convention and Visitors Bureau, 97 percent of all overnight visitors to Miami and the beaches arrive by air. Even more affected could be our international guests, whose "welcome" to Florida may include substantial waiting times to clear customs. More than 48 percent of overnight visitors to Miami are international visitors–a far higher percentage than the state average, as shown in the table.

Indeed, Miami has the highest percentage of foreign visitors of any destination in the U.S. There are already issues in some Florida venues of significant waits to clear customs – further cutbacks may possibly make these worse, thus defeating our efforts to have visitors "spread the word" to their neighbors in their home country of their positive experiences of traveling to Florida.

Effects on Investment

As the previous sections show, several of Florida's largest industries will be affected by the automatic federal budget cuts. Additionally, in its national economic forecast, Florida's Revenue Estimating Conference stated that the current situation is already eroding business confidence and that consumer confidence is likely to follow. When adding in the financial market uncertainty associated with the U.S. reaching the upcoming debt limit, volatility in the financial markets is likely to spike, resulting in seriously restricted capital investment. Given what we know about recovery from recessions, there cannot be a significant recovery without an increase in personal domestic investment in our economy. The chart below shows that the most recent growth rate of U.S. Private Domestic Investment was barely positive, showing a less than 0.2 percent increase in the fourth quarter of 2012. This coincides with a negative GDP number for that quarter.



Conclusion

In addition to the drop in Private Domestic Investment, there will likely be a drop in consumer spending associated with the sequester, making it possible that the U.S. economy will head back into recession, thereby causing an increase in unemployment levels in both the U.S. and Florida.

Recent Florida TaxWatch reports show that Florida's growth rate has been less than the U.S. growth rate coming out of the last recession. Therefore, failing to address the sequester will make any significant recovery from the Great Recession less likely, and could send Florida into another recession.

Florida TaxWatch Center for Competitive Florida Advisory Board

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