

COMMONWEALTH OF PENNSYLVANIA
HOUSE OF REPRESENTATIVES
APPROPRIATIONS COMMITTEE HEARING
BUDGET HEARING

STATE CAPITOL
MAJORITY CAUCUS ROOM
HARRISBURG, PENNSYLVANIA

THURSDAY, FEBRUARY 21, 2008, 10:00 A.M.

VOLUME I OF III

PRESENTATION ON
ECONOMIC OUTLOOK/GLOBAL INSIGHT

BEFORE:

HONORABLE DWIGHT EVANS, CHAIRMAN
HONORABLE MARIO J. CIVERA, JR., CHAIRMAN
HONORABLE STEPHEN E. BARRAR
HONORABLE H. SCOTT CONKLIN
HONORABLE CRAIG A. DALLY
HONORABLE BRIAN ELLIS
HONORABLE DAN B. FRANKEL
HONORABLE JOHN T. GALLOWAY
HONORABLE WILLIAM F. KELLER
HONORABLE THADDEUS KIRKLAND
HONORABLE TIM MAHONEY
HONORABLE KATHY M. MANDERINO
HONORABLE MICHAEL P. MCGEEHAN
HONORABLE FRED McILHATTAN
HONORABLE RON MILLER
HONORABLE JOHN MYERS
HONORABLE CHERELLE PARKER
HONORABLE JOSEPH A. PETRARCA
HONORABLE DAVE REED
HONORABLE DOUGLAS G. REICHLEY

1 BEFORE (cont.'d):
2 HONORABLE DANTE SANTONI, JR.
3 HONORABLE MARIO M. SCAVELLO
4 HONORABLE JOSHUA D. SHAPIRO
5 HONORABLE JOHN SIPTROTH
6 HONORABLE MATTHEW SMITH
7 HONORABLE GREGORY S. VITALI
8 HONORABLE DON WALKO
9 HONORABLE JAKE WHEATLEY, JR.

10 ALSO PRESENT:
11 MIRIAM FOX
12 EDWARD NOLAN

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14 DEBRA B. MILLER
15 REPORTER
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I N D E X
TESTIFIER

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1 CHAIRMAN EVANS: It is now 10 o'clock. I
2 would like to convene the House Appropriations
3 Committee.

4 Today we have Global Insight before us to
5 talk a little bit, obviously, about the economy and
6 the future of the Commonwealth of Pennsylvania.

7 So what I will do is let you give us some of
8 your thoughts, and then we will get right into some
9 questions.

10 MR. DIFFLEY: Good morning, everyone. Thank
11 you, Chairman Evans.

12 As per your request---

13 CHAIRMAN EVANS: Can you introduce yourself
14 for the record, so we know?

15 MR. DIFFLEY: Sure. James Diffley. I'm the
16 Group Managing Director, U.S. Regional Services, at
17 Global Insight, Inc., located near Philadelphia in
18 Eddystone, PA.

19 As per your request, I did not prepare
20 extensive opening comments. I will, I guess, take
21 Chairman Evans's suggestion, though, and give a brief
22 overview.

23 Certainly the U.S. economy, in particular,
24 has taken a turn for the worst in the last few
25 months. We had expected for at least the last 6

1 months that the first half of 2008, this year, would
2 exhibit very slow growth, hardly any growth at all in
3 the U.S. The first half of this year, of course,
4 coincides with the last half of your current fiscal
5 year. But by the second half of the year, again
6 coinciding with your fiscal year '09, the economy
7 would pick up again.

8 We are in for a slowdown, primarily caused
9 by the very deep recession in housing and the
10 extension of that in the last 6 months to a credit
11 crunch that has affected in some way virtually all
12 sectors of the economy.

13 We now believe, based on recent data through
14 January, that it is likely that the economy will
15 actually exhibit a recession, a mild recession to be
16 sure, but a recession is defined by negative growth,
17 very slight negative growth, in the first half of
18 2008.

19 It is not a large change in our forecast
20 outlook, because we already anticipated very slow
21 growth in the first half anyway, but we now think
22 that there's a good chance, better than a 50-percent
23 chance, that it will be in fact slightly negative.

24 By the second half of the year, again, the
25 first part of your fiscal year '09, the economy

1 should be on the upswing again, in large part helped
2 by very aggressive action by the Federal Reserve and
3 monetary policy and also very aggressive and timely
4 action, on the fiscal side, by Congress and the
5 President to get a stimulus package to consumers
6 that, because of the lags in government
7 implementation, tax rebates, et cetera, will take
8 about until late, very late in the second quarter and
9 the beginning of the third quarter to actually work
10 its way into spending in the economy.

11 Briefly on Pennsylvania, Pennsylvania, as
12 it has in past recessions and as it did in the most
13 recent business cycle, has more moderate swings, has
14 had more moderate swings in the economy. It slowed
15 down less in 2007 than most of the rest of the
16 country, than a lot of the rest of the country,
17 largely because while Pennsylvania did have a bit of
18 a housing boom, certainly in the eastern part of the
19 State, it nowhere near had the overexuberance in
20 housing and the housing bubble that many regions of
21 the country did in the northeast, the southeast, the
22 southwest, and the West Coast in particular.

23 So the turnaround, the dramatic negative
24 turnaround in housing does not have as negative an
25 impact on Pennsylvania. We think this carries

1 through into the first half of 2008, that while
2 Pennsylvania will slow with the rest of the country,
3 as it naturally must, it will not slow by as much as
4 the rest of the country.

5 Pennsylvania is also aided by the one strong
6 part in the U.S. economy, and that is exports, and
7 that is, as you no doubt know, due to the very weak
8 dollar, but that aids exporters, and in Pennsylvania,
9 manufacturing continues to be a strong exporting
10 State.

11 So with that, I will take any questions you
12 have.

13 CHAIRMAN EVANS: Thank you very much.

14 I would like to spend a little bit of time
15 talking about economic stimulus, because the Governor
16 proposed an economic stimulus program here. I don't
17 know if you are aware of it. He talked about a
18 couple of things.

19 He talked about directly putting money in
20 the hands of 475,000 working families. It could go
21 up to \$400 with kids.

22 Secondly, he talked about accelerating
23 something called the redevelopment assistance in
24 terms of projects that are shovel ready between here
25 and December.

1 He talked about increasing the job tax
2 credit program from \$1,000 to \$3,000.

3 He talked about accelerating money on
4 building bridges, infrastructure, and that was almost
5 2, 3 weeks ago that he talked about those things to
6 us as a General Assembly.

7 You brought up Washington, DC, when you
8 talked about how quickly they move. You talked about
9 Federal Reserve policy, you talked about fiscal
10 policy, those things, and how quickly they have
11 moved. And then you said that this slowdown has come
12 about because of housing, the credit crunch, is what
13 you have basically talked about where we are. And
14 then you said we are somewhat in a mild recession.
15 That is kind of basically what you have said.

16 Give me, if you can, and I don't know if you
17 looked at the Governor's economic stimulus program,
18 if you have or you have not, talk about what you
19 think principally Governor Rendell is trying to do in
20 terms of his economic stimulus program, piggybacking
21 in on the Feds. Can you give me some reaction to
22 that?

23 MR. DIFFLEY: Sure. I am aware generally of
24 the Governor's proposals and particularly the \$400 or
25 so of assistance to low-income working families.

1 The important thing in a short-term stimulus
2 package, all right, is to -- and I think this was
3 accomplished largely by the U.S. Congress, also
4 accomplished by Governor Rendell's proposal -- is to
5 get money quickly into the hands of people who will
6 spend it, because the temporary recessionary
7 conditions in the economy are due to a lack of
8 demand, all right?

9 When tax rebates, tax cuts, et cetera, are
10 realized in the economy, different groups have
11 different propensities to spend that right away. If
12 they save -- for instance, a tax rebate goes to
13 somebody who will save the money -- that is good for
14 them, of course, but it is not a stimulus to the
15 economy. If it goes instead to somebody who will
16 spend the money immediately, and we economists
17 believe, both at the Federal level and it applies to
18 Pennsylvania, that generally lower-income people have
19 a larger, higher propensity to spend. That is, they
20 will spend more of the immediate rebate they get.
21 That is a direct infusion into the local economy.

22 Now, obviously it is a nationwide problem to
23 the extent that Governor Rendell's rebates are spent
24 locally. It is a direct benefit with multiplier
25 impacts to the local economy of the individuals who

1 are spending.

2 CHAIRMAN EVANS: The aspect of
3 infrastructure, bridges, things of that nature, as
4 you know, obviously you know about the Minnesota
5 situation that we had.

6 MR. DIFFLEY: Sure.

7 CHAIRMAN EVANS: There are a lot of problems
8 with our bridges that he was talking about. What is
9 your view on the infrastructure aspect as part of
10 that equation?

11 MR. DIFFLEY: Long term, of course,
12 infrastructure is a very important problem in the
13 U.S., a very important problem in Pennsylvania. I
14 have emphasized over the past that particularly the
15 Northeast and Midwestern sections of the country are
16 at a disadvantage in terms of deteriorating
17 infrastructure, and for long-term economic
18 competitiveness, that should be addressed, and it
19 would be a very wise investment that States and
20 regions and localities make.

21 But for a short-term impulse, again,
22 government spending adds to demand in the economy,
23 creates jobs and construction work. As you know, due
24 to the housing bust, there are now a lot of
25 construction workers. Infrastructure programs

1 address that. And it does have, to the extent that
2 you just mentioned shovel-ready sites, I don't know
3 the details of the program, but money that can be
4 spent immediately has immediate positive impacts on
5 the economy, again with multiplier impacts, as those
6 people who are paid income or fees then spend it
7 themselves and on and on.

8 CHAIRMAN EVANS: In this General Assembly,
9 we always have a constant debate over the issue of
10 tax cuts, you know, in terms of the effects of a tax
11 cut.

12 Obviously we have in our Rainy Day Fund
13 something like \$700 million. That is currently what
14 we have in our Rainy Day Fund. It is forecast that
15 the revenue picture will maybe be in the ballpark of
16 \$500 million, and we constantly have a debate about
17 the reduction of our personal income tax, and that is
18 always the question of, you know, is it a question of
19 rebates or is it a question of tax cuts or is it
20 both? Is it either/or? Is it an either/or
21 proposition or is it one versus the other?

22 MR. DIFFLEY: Well, as a longer term
23 competitiveness issue per se, tax cuts are important
24 and significant, of course.

25 In a medium- to long-term analysis, the

1 impacts of a rebate and a tax cut are pretty much
2 identical, but in terms of a short-term stimulus,
3 when the economy is, as it is now, we believe in the
4 first half of 2008 in particular, hurting, a rebate
5 is actually more effective in pushing the money out
6 into the demand system more quickly.

7 CHAIRMAN EVANS: Okay.

8 Chairman Mario Civera.

9 CHAIRMAN CIVERA: Thank you, Mr. Chairman.
10 Good morning, and thank you.

11 It was stated in the Governor's budget that
12 the employment growth in the Commonwealth during 2007
13 ranked 33rd among the 50 States. This improvement in
14 Pennsylvania typically ranked 40th or below in
15 employee growth in prior years. And when I look at
16 this chart that we have here, that Pennsylvania ranks
17 46th, and based on the programs that the Governor has
18 put in his budget, the stimulus programs over the
19 years, could you tell me why we are at 46th on this
20 chart here? Could you give me an idea why, because
21 with all the programs that the Governor has put in
22 his previous budgets, this budget, the forecasters
23 show that we will be at number 46 as far as in job
24 growth.

25 MR. DIFFLEY: It is a reflection, the low

1 performance of Pennsylvania relative to other States,
2 is largely a reflection of low demographic growth,
3 that population growth is barely positive, labor
4 force growth is barely positive, so that--- And this
5 is an affliction, if you will, of much of the
6 Northeast and Midwest. Pennsylvania actually is
7 running very slow in terms of population growth for
8 demographic reasons. So in our longer term and in
9 any longer term forecasting, that is, you know, a
10 driving factor.

11 If you look at performance indicators such
12 as per capita income growth, Pennsylvania ranks much
13 better. In other words, it is a question of a slower
14 growth economy certainly relative to the areas of the
15 Sun Belt, which continue to attract migration and
16 movement and have younger populations with higher
17 birthrates and the like and attract business.

18 So income-wise and per-capita-wise, in terms
19 of growth, Pennsylvania is not performing nearly as
20 bad as those indicators indicate. However, given the
21 demographics, Pennsylvania's performance is going to
22 rank in the lower 10 consistently.

23 CHAIRMAN CIVERA: So if a corporate---

24 MR. DIFFLEY: And we don't see that turning
25 around.

1 CHAIRMAN CIVERA: If a major corporate
2 company looks at this chart---

3 MR. DIFFLEY: Yeah.

4 CHAIRMAN CIVERA: ---and sees us at 46th,
5 the answer that you just answered me would resolve
6 that from, they would then overlook that and say,
7 "Well, you know what? Pennsylvania is not a bad
8 idea." Is that what you are saying? I mean, how do
9 you---

10 MR. DIFFLEY: They could---

11 CHAIRMAN CIVERA: Once those numbers get out
12 there -- and I don't mean to interrupt -- once those
13 numbers get into the corporate sector or any kind of
14 business mind, we are on the downswing, and what my
15 point is is that over the budgets that we have
16 passed, the programs that we have added into the
17 previous budgets, I do not believe that we should be
18 there.

19 I understand what you are saying about the
20 demographics and what goes on in the Northeast
21 corridor, but that has me--- Because we are not only
22 competing with the South, we are competing in a
23 global situation. We are competing with different
24 countries now.

25 So that bothers me, because my take on this

1 is the investment that we have put in our previous
2 budgets, we should not be at that number. But you
3 are saying that because of the demographics and the
4 way it swings, that is why it leads into that
5 direction. Is that what you are saying?

6 MR. DIFFLEY: That is correct; that is
7 correct. And I must say that for the last few years,
8 Pennsylvania on those grounds has overperformed,
9 outperformed, what the demographics would seem to
10 have dictated.

11 One thing that corporations in terms of
12 business location are looking for, very importantly,
13 is workforce availability, all right? And a quality
14 workforce is one thing, and that Pennsylvania is
15 relatively in good shape in, the Philadelphia area
16 and the Pittsburgh area in particular.

17 But in terms of a vast number of young
18 people entering the labor market, we, Pennsylvania,
19 are at a disadvantage, to be sure.

20 CHAIRMAN CIVERA: Thank you, Mr. Chairman.

21 CHAIRMAN EVANS: Representative Dan Frankel.

22 REPRESENTATIVE FRANKEL: Thank you, Mr.
23 Chairman.

24 Good morning. Welcome back.

25 MR. DIFFLEY: Good morning. Thank you.

1 REPRESENTATIVE FRANKEL: We are reading and
2 experiencing here in Pennsylvania also some
3 challenges within the student loan business because
4 of the capital markets---

5 MR. DIFFLEY: Yes.

6 REPRESENTATIVE FRANKEL: ---and it is, in
7 many instances, a little difficult to get our hands
8 around this problem. There is a meeting today, a
9 summit meeting today, of our facility, PHEAA, the
10 Pennsylvania Higher Education Assistance Agency, and
11 the many challenges facing it.

12 What is going on in the capital markets,
13 particularly with respect to, and this is a national
14 problem that is creating this pressure, particularly
15 in the student loan business?

16 MR. DIFFLEY: This has been the problem in
17 the last, really since August, in the last 6 months,
18 with the depths of the exposure that the banking
19 system had to the subprime mortgage crisis.

20 The Federal Reserve was unprepared for it.
21 They didn't understand how much exposure the banks
22 had, not only to subprime but the exotic vehicles
23 they had set up, and once this type of credit
24 question enters the market where, one, you know, if I
25 have a subprime mortgage in my portfolio, right, and

1 they are tanking, well, the other lenders to me,
2 people who hold my assets, are now questioning my
3 viability, and similar to them, chain to chain to
4 chain, and all other or many other credit instruments
5 are caught up in that loop, student loans being one
6 of them. So it all stemmed from that large contagion
7 in credit markets.

8 There is now a very high pricing on risk,
9 whereas prior to last year, there was probably an
10 underpricing of risk by financial markets. We are
11 looking for the credit situation to shake out by the
12 second half of the year, and have been, but there are
13 many more stones to be unturned, if you will.

14 You have heard about the auction rate
15 securities markets; you have heard about bond
16 insurance firms being exposed and the like. It is
17 all part of one large linked, very intensively linked
18 set of borrowing-and-lending relationships,
19 debit-and-credit relationships, within the banking
20 system.

21 REPRESENTATIVE FRANKEL: Thank you, Mr.
22 Chairman.

23 CHAIRMAN EVANS: Representative Brian Ellis.
24 Do you feel much better today?

25 REPRESENTATIVE ELLIS: Yes, Mr. Chairman, I

1 feel much better today. Thank you.

2 Thank you for coming to testify today. I
3 have been in the Legislature for 3 years, and during
4 that 3 years we saw the capital stock and franchise
5 tax being phased out.

6 Originally, you know, back in '91 we were at
7 .13 mills; we are at 2.89 right now. How does that
8 compare to other States?

9 MR. DIFFLEY: One of the long-term
10 disadvantages Pennsylvania has in terms of business
11 tax competitiveness and competitiveness overall has
12 been the existence of that franchise tax. Only a few
13 States still have such a beef. So it has been an
14 important aspect of policies for the last, I guess,
15 three administrations at least, at least two that I'm
16 sure of, to diminish the burden of that tax, and it
17 has been and it is important. I think the business
18 community realizes that it is on its way out. I
19 think it is scheduled to be gone by 2010 or '11?

20 REPRESENTATIVE ELLIS: Yeah.

21 Well, interestingly enough, the Governor
22 this year chose to slow down the phase-out of it in
23 his proposal to the 2.49, which would actually be a
24 32-percent increase on the taxes that the businesses
25 were anticipating paying this year. So obviously

1 that is going to be an area for debate, I think, as
2 we get into the budget season certainly.

3 What do you think as far as even at a lower
4 rate of 2.49 versus the 1.89 it was supposed to be?
5 Is that still deterring businesses from making
6 long-term decisions to come to Pennsylvania?

7 MR. DIFFLEY: No. I think as long as
8 businesses are convinced that the tax is ultimately
9 and relatively quickly to be eliminated under some
10 schedule, that they take that into account, and I
11 think it continues to be a positive.

12 REPRESENTATIVE ELLIS: So---

13 MR. DIFFLEY: It would be a concern to
14 business, for instance, if they heard that the whole
15 scale of reductions was being stopped, and that, it
16 is my understanding, is not occurring, right?

17 REPRESENTATIVE ELLIS: Yeah. I mean, we are
18 still scheduled for, you know, the year 2011 and
19 thereafter with the slowdown.

20 But you know what? I have heard from a lot
21 of people in the business community that they are
22 concerned that we are going to slow it down this year
23 and continue to slow it down and then keep it
24 forever.

25 MR. DIFFLEY: Well---

1 REPRESENTATIVE ELLIS: That, obviously in
2 your opinion, would be a very bad policy decision for
3 Pennsylvania to make?

4 MR. DIFFLEY: Right.

5 REPRESENTATIVE ELLIS: Okay.

6 Thank you very much, Mr. Chairman.

7 CHAIRMAN EVANS: Representative Mario
8 Scavello.

9 REPRESENTATIVE SCAVELLO: Just in time.

10 Thank you, Mr. Chairman, and good morning.

11 In your most recent forecast of the U.S.
12 economy, you had said it was, for the second quarter
13 and the first quarter of 2008, .04 and .05, and then
14 earlier you said that they will be negative numbers
15 now respectively?

16 MR. DIFFLEY: Right.

17 REPRESENTATIVE SCAVELLO: Global Insight
18 produces a baseline forecast, an alternative
19 forecast, and in your February baseline forecast, you
20 gave a real gross State product increasing by 1.4 in
21 2008 and 2.2 in 2009. Are those numbers still about
22 where you expect to be?

23 MR. DIFFLEY: We have in our--- You said
24 1.4 in 2008---

25 REPRESENTATIVE SCAVELLO: '08, and 2.2 in

1 2009.

2 MR. DIFFLEY: Our current forecast, baseline
3 forecast, for a GSP is 1.3.

4 REPRESENTATIVE SCAVELLO: 1.3.

5 MR. DIFFLEY: So there's a slight revision
6 there.

7 REPRESENTATIVE SCAVELLO: Okay.

8 The Governor uses a forecast to grow to 2.7
9 for 2008 and 3.7 for 2009 in preparing the revenue
10 estimates included in his budget, and looking at your
11 alternative forecast entitled "Touch and Go," which
12 is the optimistic scenario portraying renewed
13 strength in the economy, I noticed that the gross
14 State product rose, in that scenario, in 2008 is
15 estimated about 2.2 and 3.0 in 2009. These
16 optimistic forecasts are significantly below the
17 forecasts used by the Governor in preparing his
18 budget.

19 That being said, how would you characterize
20 the forecast scenario that the Governor is using for
21 his budget?

22 MR. DIFFLEY: Well, it is slightly more
23 optimistic than our current scenario. I did,
24 however, check the publication, the budget
25 publications from the Governor in terms of employment

1 and in terms of personal income, and the differences
2 are within just a couple of tenths of a percent in
3 those important issues and indicators.

4 REPRESENTATIVE SCAVELLO: Yeah, but the
5 overall forecast in growth is a half a percent for
6 2008 and .7 percent more for 2009. Would you say
7 that is highly unlikely, or are you saying that it
8 possibly can be those numbers?

9 MR. DIFFLEY: Oh, it could be those numbers,
10 and I believe those numbers are derived from, you
11 mentioned alternative scenarios that we provide,
12 Global Insight provides on the U.S. level and the
13 State level, and I believe they are in fact more
14 optimistic scenarios. So I think we assign about a
15 25-percent probability on those scenarios.

16 REPRESENTATIVE SCAVELLO: On that 2.2 and
17 the 3.0?

18 MR. DIFFLEY: Right.

19 REPRESENTATIVE SCAVELLO: Okay. Thank you.

20 CHAIRMAN EVANS: I would like to follow up a
21 little bit---

22 MR. DIFFLEY: Also could I follow up on
23 that?

24 The other important point is there's a big
25 difference in the projections that occur now in the

1 first half of 2008. So in terms of the fiscal year
2 forecasting, fiscal '08-'09, the numbers are far more
3 similar.

4 CHAIRMAN EVANS: Couldn't that also be--- I
5 want to follow up a little bit on that.

6 Couldn't that also be why the Governor was
7 suggesting, he used the term called "protecting
8 Pennsylvania's progress," and he has talked about the
9 element of using an economic stimulus to, you know,
10 augment the economy a little bit, you know, put money
11 in people's pocket and accelerate construction,
12 things of that nature. Couldn't it be, when you said
13 there is only a very small percentage difference in
14 what the gentleman was expressing versus the
15 Governor, couldn't he be trying to ensure that, you
16 know, we get that kind of growth by using the
17 economic stimulus?

18 REPRESENTATIVE SCAVELLO: Mr. Chairman,
19 could I finish up also?

20 CHAIRMAN EVANS: Excuse me.

21 REPRESENTATIVE SCAVELLO: Okay; go ahead.

22 CHAIRMAN EVANS: Excuse me; I was just
23 following up on your question.

24 Go ahead.

25 MR. DIFFLEY: I'm sure he is. I don't know

1 that they are making an assumption that those
2 stimulus packages have a noticeable result in the
3 forecast. I think they are taking our forecast as
4 given and also providing a stimulus on top of that.

5 CHAIRMAN EVANS: But the stimulus in
6 conjunction with the Federal stimulus, too -- both.

7 MR. DIFFLEY: Oh, it's important.

8 CHAIRMAN EVANS: Yeah.

9 MR. DIFFLEY: It is definitely a positive.

10 CHAIRMAN EVANS: Yeah; trying to use both as
11 well. Right.

12 MR. DIFFLEY: We think that the Federal
13 stimulus, which is more than the size of the rebates
14 coming in the middle of this year, is more than 1
15 percent of gross domestic product, for instance, so
16 there's a significant amount.

17 CHAIRMAN EVANS: Okay.

18 Representative Scavello.

19 REPRESENTATIVE SCAVELLO: First, just to go
20 back, you know, you were projecting first .04 and now
21 you are projecting a negative number for 2008, so is
22 it---

23 MR. DIFFLEY: Are you speaking for the U.S.?

24 REPRESENTATIVE SCAVELLO: For the U.S.
25 economy, correct? And then your baseline forecast

1 you said for 2008 is 2.2. Are you saying that that
2 is going to be even lower now, because you are
3 starting out the year lower.

4 MR. DIFFLEY: Our U.S. projection for GDP
5 for the year is, I believe -- I'll give you the right
6 number here in a moment -- it is 1.3 or 1.4, I
7 believe.

8 REPRESENTATIVE SCAVELLO: Yes; about 1.4,
9 correct.

10 MR. DIFFLEY: You got that; okay.

11 REPRESENTATIVE SCAVELLO: In 2008, and 2.2
12 in 2009. So is that 1.4 number, are you going to
13 downsize that number or do you think you are going to
14 recapture that after the second quarter, because you
15 are---

16 MR. DIFFLEY: No, we're not going to do
17 that. I don't know what you mean by downsize that
18 number.

19 REPRESENTATIVE SCAVELLO: That is your
20 number.

21 MR. DIFFLEY: That is already occurring.

22 Over the last couple of months, if you
23 followed this, as some of you have, we have lowered
24 our forecast projections, as others have, and as you
25 noticed, the Federal Reserve announced it yesterday

1 and others did.

2 REPRESENTATIVE SCAVELLO: Yes.

3 MR. DIFFLEY: And they are, by the way,
4 higher than our numbers right now.

5 So that is, we think, a solid number. We
6 don't expect to be lowering that any further.

7 REPRESENTATIVE SCAVELLO: The difference
8 between yours and the Governor's projection, in
9 dollars, what is that? For example, for 2008, you
10 are saying 2.2 and the Governor is saying 2.7. That
11 half a percent, in dollars, what are we talking
12 about?

13 MR. DIFFLEY: You are talking about gross
14 State product growth?

15 REPRESENTATIVE SCAVELLO: Yeah.

16 MR. DIFFLEY: Well, to do the math, if you
17 want, gross State product for Pennsylvania is about
18 half a trillion dollars, \$500 billion.

19 REPRESENTATIVE SCAVELLO: So how many
20 million are we--- What is it, about 20---

21 MR. DIFFLEY: I hesitate to be put on the
22 spot and do that simple calculation.

23 REPRESENTATIVE SCAVELLO: Yeah. It's a lot
24 of money.

25 MR. DIFFLEY: Yeah.

1 REPRESENTATIVE SCAVELLO: Okay. Thank you.

2 CHAIRMAN EVANS: Representative Jake
3 Wheatley.

4 REPRESENTATIVE WHEATLEY: Good morning. I'm
5 over here.

6 MR. DIFFLEY: Good morning.

7 REPRESENTATIVE WHEATLEY: How are you doing?

8 MR. DIFFLEY: Great.

9 REPRESENTATIVE WHEATLEY: Thank you, Mr.
10 Chairman.

11 Last year you came before us and I asked you
12 a question around trying to get a better sense
13 geographically and demographically how our
14 Commonwealth economy and the future looks as it
15 relates to various different populations of people,
16 and I always say whenever we have these broad
17 conversations, it is hard to really as a policymaker
18 know if what we are doing is working, because you can
19 say that right now our economy seems to be sound and
20 secure compared to the nation, but there are
21 individuals inside of this Commonwealth, in
22 populations and pockets inside of this Commonwealth,
23 that are not doing so well no matter how you compare
24 them. And we have seen with the catastrophe of
25 Katrina that many times we have poor and poor

1 individuals around our cities and places that really
2 are not prepared to live a quality life.

3 So when I look at this unemployment rate,
4 can you tell me, I don't know if you have it or not,
5 but can you share with me what it looks like for an
6 African-American across the Commonwealth or a Latino
7 across the Commonwealth compared to this 4.7, I guess
8 is what you are projecting?

9 MR. DIFFLEY: I don't have the exact figures
10 in front of me. I can tell you it is probably
11 double---

12 REPRESENTATIVE WHEATLEY: It is probably
13 double.

14 MR. DIFFLEY: ---for an African-American.

15 I will let you know, if you have not seen it
16 -- I know Chairman Evans has -- for instance, we did
17 a report during the fall of 2007 for the Urban League
18 of Philadelphia that they published in a publication
19 we provided the statistics for, an analysis called
20 "The State of Black Philadelphia," where we
21 documented the relative condition in Philadelphia
22 city only of blacks versus whites in the city, and we
23 came up with a socioeconomic index of equality, if
24 you will.

25 REPRESENTATIVE WHEATLEY: Well, I would love

1 to see one done across the Commonwealth, the state of
2 black and brown persons across the Commonwealth. It
3 would be helpful, probably, to understand.

4 MR. DIFFLEY: Yeah, and we have a proposal
5 to do one also by gender.

6 REPRESENTATIVE WHEATLEY: Well, could you
7 share with me maybe this income growth that you are
8 projecting, or I guess it was 6.1 in 2007 and it will
9 be 4.5 in 2008. Can you tell me what that looks like
10 for persons of color across the Commonwealth? Is
11 that the same or is that just a broad---

12 MR. DIFFLEY: No; that is a broad average.
13 We do not literally forecast income growth in that
14 regard. However, it is the case historically; as the
15 economy slows, that there is very often a last-in,
16 first-out movement in the labor market, and so one
17 would expect that the less experienced workers will
18 do more poorly than average.

19 REPRESENTATIVE WHEATLEY: So that leads me
20 to my final question. I guess with the labor force
21 numbers that you are projecting and the industries,
22 the growth in areas, do you have that broken out to
23 what that may mean as opportunities for people of
24 color across the Commonwealth? I mean, are you
25 projecting that you will see more persons of color

1 being able to come into the labor force market, be it
2 through the technological arm or through the higher
3 ed, through the educational fields or health fields?
4 Are you projecting those numbers?

5 MR. DIFFLEY: I think generally, I am not
6 projecting numbers on a quantitative basis, but I
7 think generally it is the case. The tight labor
8 market conditions in Pennsylvania, that is, a
9 slow-growing labor force, bodes well for those
10 persons of color who are in competition for jobs,
11 yes.

12 REPRESENTATIVE WHEATLEY: You say bodes
13 well, and why would you say it bodes well for them?

14 MR. DIFFLEY: In the sense that there is
15 less competition for those jobs.

16 REPRESENTATIVE WHEATLEY: Oh, okay.

17 MR. DIFFLEY: Employers need to come to
18 them, they need to broaden their horizons, and with
19 sufficient skill training and the like and skill
20 acquisition, there can be a prosperous future.

21 REPRESENTATIVE WHEATLEY: Well, and again I
22 will just make this caveat to you as you come before
23 us in future years, if you would provide some of
24 those things. It would be helpful to me as a member
25 of this committee just to make sure the things that

1 we are pushing for have broad range implications for
2 all of our citizens in Pennsylvania, and so we can
3 tell the story of all of our citizens as well as the
4 broader story of how we are doing overall.

5 Thank you, Mr. Chairman. Thank you.

6 MR. DIFFLEY: Point well taken.

7 CHAIRMAN EVANS: Representative Barrar.

8 REPRESENTATIVE BARRAR: Thank you, Mr.
9 Chairman.

10 I have a question to follow up on the \$400
11 rebate that we had been discussing earlier.

12 The Administration is suggesting that the
13 rebate could possibly have a 6- to 8-percent
14 multiplying effect on the return of money to the
15 Commonwealth in the short term. Would you agree with
16 that?

17 MR. DIFFLEY: I have not done the numbers as
18 to what the quantitative level of the multiplier
19 would be. I mean, normally the way a multiplier like
20 that works is if I spend \$100, if I'm one of the
21 recipients and I spend \$100, the person I'm paying in
22 some way, say a local restaurant, turns around and
23 spends, say, \$80, all right? Say they save some or
24 whatever, or some of it goes out of State for
25 supplies or something like that. When they spend the

1 \$80, the next person might spend \$60, and depending
2 upon that deterioration, you get a multiple of some
3 fraction, which is actually, for those of you who
4 remember introductory macroeconomics, it is 1 divided
5 by 1 minus the marginal propensity to consume in the
6 State.

7 So I don't have a good estimate of that. It
8 relies on, of course, resources being available,
9 which is what happens in a mild recession, et cetera,
10 and relies on spending being in State or in the
11 locality.

12 REPRESENTATIVE BARRAR: I know other States
13 that do---

14 MR. DIFFLEY: But there is a multiplier, to
15 be sure.

16 REPRESENTATIVE BARRAR: But I would think
17 that a 6 to 8 times multiplier is a little bit of a
18 stretch at this point, especially when you are
19 targeting Pennsylvania's lowest income families at
20 this point. Can you really sit there and say that?

21 MR. DIFFLEY: Well, again, the key, by the
22 way---

23 REPRESENTATIVE BARRAR: What areas would you
24 suggest that might be---

25 MR. DIFFLEY: The key, by the way, about the

1 lowest income families, again, is to get that sort of
2 first round of spending as high as possible. In
3 other words, they don't save anything and they spend
4 it locally. So that increase is what the multiplier
5 would be.

6 Again, I do not have a number. Is 6 to 8
7 too high? You know, I would have guessed 4 to 5
8 maybe, 3 to 5, if I had to give it off the top of my
9 head.

10 REPRESENTATIVE BARRAR: I think if you look
11 at the studies that the Administration is citing,
12 most of them deal with rebates that were, in other
13 States, that were much broader and also a lot more
14 expensive for the States to give out.

15 With the Federal package being pretty much
16 very comprehensive and touching a lot more families
17 and should have a very positive, short-term effect,
18 wouldn't the State, wouldn't we be better off looking
19 long term and trying to reduce the overall tax
20 burden, the income tax rate on all Pennsylvania's
21 citizens, especially the group we are currently
22 targeting today that pays no State income taxes?
23 Wouldn't we be better off looking at the
24 higher-income workers and looking at reducing their
25 tax burden, which is, I think, probably what most of

1 us in this room hear more than anything, is the tax
2 burden that is hurting the people of Pennsylvania.

3 MR. DIFFLEY: Well, as I mentioned earlier,
4 I think if you are trying to address a long-term
5 problem, the tax burden is relatively more important.
6 But if you are trying to address a short-term
7 problem, that tax burden is not the thing that is
8 going to help in 2008 immediately.

9 There is a tradeoff, and this is very much
10 in place at the Federal level, where of course this
11 stimulus package, \$150 or \$160 billion at the Federal
12 level, adds to the deficit, which by itself is not a
13 good thing long term, but it is aimed at a short-term
14 problem. I think the Administration is in the same
15 boat in terms of balancing a short-term objective
16 versus a longer term strategy.

17 REPRESENTATIVE BARRAR: In your report here
18 you refer to, I think at one point, the recession of
19 2001. We got through that pretty well, pretty
20 quickly, without any type of a rebate or even a tax
21 reduction program. Would you suggest that we just
22 stay the course where we are now, just use the rebate
23 and just stay the course, not raise taxes, not lower
24 taxes? Would that be a better economic policy, or
25 does it make sense to forgo a payment into the Rainy

1 Day Fund where, if your projections are wrong or most
2 of the economists and it is a longer term recession,
3 we may have to go into that Rainy Day Fund. Does it
4 make sense to spend it today when we really, I think
5 most of us here who are somewhat fiscally
6 conservative, feel that, hey, that is money we
7 promised the taxpayers we would put away every year
8 and we are going to forgo that payment?

9 MR. DIFFLEY: First of all, when you refer
10 to the 2001 recession, you are referring to the lack
11 of a State rebate package---

12 REPRESENTATIVE BARRAR: Right.

13 MR. DIFFLEY: ---because there was one at
14 the Federal level.

15 REPRESENTATIVE BARRAR: Right, and we came
16 through that very quickly.

17 MR. DIFFLEY: During the Bush
18 Administration, right.

19 You know, I don't have an answer. There is
20 not a correct answer in terms of the policy call
21 there.

22 I don't think, you know, Pennsylvania is
23 fiscally, if you have seen reports coming out of
24 California and New Jersey and other States, fiscally
25 in very good shape compared to other States in terms

1 of having and being able to deal with the Rainy Day
2 Fund and relatively low debt and the like and not
3 experiencing the same sort of shortfalls that they
4 are.

5 You know, there is not a correct answer to
6 that. The Rainy Day Fund, there is always a question
7 of how big a downturn should there be before you dip
8 into the Rainy Day Fund? What after all is it for?

9 REPRESENTATIVE BARRAR: Okay.

10 One last question. Maybe the Chairman will
11 want to answer this one. It is one that Mario
12 Scavello wanted to know.

13 Is it true that Philadelphia is getting most
14 of the money on this? No, I am teasing on that one.

15 Thank you, Mr. Chairman.

16 CHAIRMAN EVANS: You turned away from the
17 mike a little bit when you said---

18 MR. DIFFLEY: I'm sorry.

19 CHAIRMAN EVANS: ---you turned away from the
20 mike when you said relatively low debt. Can you
21 repeat that again? You said Pennsylvania has
22 relatively low debt?

23 MR. DIFFLEY: Well, compared to the States
24 that are known to be in the problems with the ratings
25 agencies, California---

1 CHAIRMAN EVANS: That is why I wanted you to
2 say that directly, because when you turned away a
3 little bit, I don't know if my colleague heard---

4 MR. DIFFLEY: Oh, okay.

5 CHAIRMAN EVANS: ---when you said relatively
6 low debt. You said great Rainy Day Fund. You said
7 that, but you said low debt. You turned away and
8 said low debt. I wanted to make sure he heard it.

9 But I want to tell you my theory. I just
10 told the Chairman. This is my theory about the
11 rebates.

12 See, it is really our back-door way of
13 helping the Republican small business guy, you know,
14 somebody who owns a delicatessen, right? You put
15 that hundred dollars in their pocket, and they go buy
16 that corned beef sandwich, and that is what we are
17 trying to do.

18 So we know Republicans control the little
19 small businesses -- you got delicatessens and all
20 those different things. So we figure if we put \$100
21 in an individual's pocket, a Democrat, he in return
22 will go to that Republican small business and buy a
23 corned beef sandwich.

24 MR. DIFFLEY: That is, by the way, the way
25 it should work in terms of economics.

1 CHAIRMAN EVANS: That is the way it should
2 work, right? I want to do that; yeah.

3 CHAIRMAN CIVERA: As a Republican small
4 business man, I need to keep the debt small. We
5 don't need to catch up with the other States.

6 CHAIRMAN EVANS: Representative Dante
7 Santoni.

8 REPRESENTATIVE SANTONI: Thank you, Mr.
9 Chairman, and good morning.

10 I just have a question. I know that there
11 are some of us, some of my colleagues, that are
12 looking at, you know, cutting across the board
13 10-percent funding that goes to all of the
14 departments, and of course with that goes, you know,
15 cutting funding for education, cutting funding for
16 transportation, cutting funding from the Department
17 of Community and Economic Development, which provides
18 funding to bring business in and provides incentives
19 for businesses to stay and grow in Pennsylvania.

20 My question to you is, when businesses are
21 looking to come into Pennsylvania and they see that
22 the General Assembly is sort of willy-nillying
23 across-the-board tax funding cuts, what do they think
24 about that?

25 MR. DIFFLEY: Well, I will point out, and

1 obviously businesses have different favorites in
2 terms of government spending, but it is important to,
3 when we talk about competitiveness of a State, to
4 understand that if low taxes by themselves are better
5 and look favorably, but low provision of government
6 services by themselves are looked at unfavorably --
7 think about infrastructure, education, for instance,
8 as obviously ones that depreciate -- that low
9 spending would, that is -- depreciate the
10 Commonwealth's or a State's competitiveness, so you
11 need to look at the whole package, the spending
12 package and the tax package, to be sure.

13 REPRESENTATIVE SANTONI: Thank you. But
14 aren't targeted cuts a little bit more productive and
15 what businesses look at a little bit more favorably
16 than just across the board we are just going to cut
17 everything and forget about the consequences?

18 MR. DIFFLEY: Well, I don't claim to be a
19 government cost expert and can't really evaluate the
20 spending in the State to understand, you know, the
21 implications of targeted versus general cuts.

22 REPRESENTATIVE SANTONI: Thank you.

23 Thank you, Mr. Chairman.

24 CHAIRMAN EVANS: Representative David Reed.

25 REPRESENTATIVE REED: Thank you, Mr.

1 Chairman.

2 My first question is really just a followup
3 to one of your responses to a question that Chairman
4 Evans posed about the rebate program, and I guess
5 fist off, the "rebate" term is a little generous; it
6 is more of a taxpayer paid-for bonus program in
7 essence.

8 But when you look at the rebate program,
9 your response in comparing permanent tax cuts to a
10 one-time rebate was that in the mid- to long-term
11 prospects for the economy, there was very little
12 difference, and I was wondering if you could clarify
13 that statement, because a one-time check imports
14 money into the economy one time, whereas a tax cut is
15 permanent, putting money into the economy year after
16 year after year after year after decade, really, so
17 that stimulus effect occurs each and every year. How
18 can that have the same mid- to long-term impact on
19 the economy?

20 MR. DIFFLEY: No, I did not mean to imply
21 that.

22 The point is that if you compare the size of
23 the rebate with the same sized tax cut. So I would
24 not be thinking of a one-time rebate versus a
25 continual tax cut. The tax cut would be favored over

1 the long-term, right.

2 REPRESENTATIVE REED: Okay. Thank you.

3 My second question would be, in the last
4 couple years when we have looked at economic
5 development spending, stimulus packages, whatever the
6 term is used on any given year -- we have had a
7 number of different terms used to describe it -- most
8 of the economic development programs that have come
9 out of this Administration have focused on government
10 collecting tax dollars and then redistributing those
11 tax dollars in the form of checks to individual
12 companies or individual projects.

13 In the long term, is that a preferable
14 system for long-term economic prosperity, or is a
15 more broad based tax-policy approach more conducive
16 to producing long-term prosperity?

17 MR. DIFFLEY: The reality of State and local
18 fiscal policy or economic development policy across
19 the country in the last generation has been movement
20 and extensive use of these targeted sort of efforts,
21 you know, directed toward particular industries --
22 high tech, biotech, et cetera -- and there is some
23 logic to that.

24 Generally, economists step back from that
25 and say, well, governments don't do a very good job

1 or we can't expect governments in general -- it is
2 not a comment about Pennsylvania at all -- to do a
3 very good job picking winners and losers in the new
4 economy, and that it would be better spent if you
5 took the tax expenditures that take place on those
6 targeted programs and use that money to generally
7 reduce taxes.

8 REPRESENTATIVE REED: Okay.

9 My final question deals with the Governor's
10 estimate of real GDP growth in the first quarter of
11 2008.

12 In his Budget Book, they are looking at
13 about a 1.8-percent GDP growth in the first quarter.
14 Your estimates have been a bit lower than that. In
15 fact, you guys have actually looked at some negative
16 numbers, possibly putting us into a mild recession
17 before we recover in the second half of the fiscal
18 year.

19 Have your numbers changed at all, or do you
20 believe the Governor's numbers are accurate, or is he
21 perhaps on the higher end of the optimistic side?

22 MR. DIFFLEY: Well, as I said, he was on the
23 higher end of our most current forecast, not by much.

24 I would be glad to provide you with a direct
25 comparison of what our current forecast is with what

1 the Governor has forecasted. I don't have those
2 details right in front of me. As I mentioned
3 earlier, I compared from the budget materials the
4 employment growth and the income growth, and it was
5 only a couple tenths of a percent lower.

6 I haven't actually seen the GSP numbers that
7 we have been talking about, but I would be glad to
8 lay them out, and you can see the exact comparison.

9 REPRESENTATIVE REED: Okay. Thank you.

10 CHAIRMAN EVANS: Let us clarify something
11 for the record.

12 You said taxpayers' bonuses. Those 475,000
13 people do pay taxes. They pay sales tax; they pay
14 gas tax. They pay some taxes. Whatever they pay,
15 they pay taxes. So, you know, it is only--- And I
16 think the difference is that you were responding to
17 the question that was framed around a recession---

18 MR. DIFFLEY: Yeah.

19 CHAIRMAN EVANS: ---specifically the
20 question that was asked to you. You were not asked a
21 question about the long-term aspect of the economy.
22 So I think if you are going to put a caveat in there,
23 you put the caveat in there that you were responding
24 to the economy, the slow growth, and what we could do
25 based now, no more different than President Bush who

1 led the charge to do a \$150 billion in our economy.

2 Even though we have the largest deficit in
3 the history of America, he is even putting \$150
4 billion immediately, because one of the basic
5 principles that he and his Treasury Secretary talked
6 about was as long as it is principally short term and
7 not long term, because if it was long term, then they
8 should have went for the tax cuts that they have to
9 be permanent, right?

10 MR. DIFFLEY: You are correct.

11 CHAIRMAN EVANS: They should have gone for
12 that.

13 MR. DIFFLEY: That's right.

14 CHAIRMAN EVANS: But they didn't choose to
15 go for that.

16 MR. DIFFLEY: Right.

17 CHAIRMAN EVANS: They chose to go for a
18 short-term, narrow period of time. That is what they
19 chose, correct?

20 MR. DIFFLEY: And that---

21 CHAIRMAN EVANS: So I think it is important
22 to clarify for when you leave here, so people will
23 not leave here thinking that there is a difference
24 between a mild recession and a long-term
25 restructuring of the economy. I was not talking

1 about that. I was only piggybacking on the
2 principle. So I am saying we should be clear on what
3 I said.

4 Representative Kathy Manderino.

5 REPRESENTATIVE MANDERINO: Thank you, and
6 thank you very much for being here.

7 In your opening remarks you talked about how
8 much of the economic depression -- I cannot think of
9 the right word I want to use -- that we are
10 experiencing nationwide is due to what has happened
11 in housing, and I have to admit that I really have a
12 hard time understanding the problem in housing and
13 some of the proposed public policy solutions, both at
14 the Federal level, you know, the Congress kind of
15 tried to pass some sort of homeowners' program. In
16 Pennsylvania yesterday, we heard from, or yesterday
17 or the day before we heard from our Pennsylvania
18 Housing Finance Agency, which has two very modest
19 programs trying to kind of get to the point of
20 stabilizing folks who have become most vulnerable
21 because of this.

22 But what I hope you can help me understand
23 is, it seems to me from what I know and what I read,
24 there are two problems out there. There are folks
25 who have got caught, maybe in an uneducated way, in a

1 predatory lending type of situation, and then folks
2 who may have very, you know, maybe you could say that
3 while they may be more educated folks, they may not
4 have used that education wisely to get caught into
5 kind of fancy products that were no-interest-only
6 products or inflatable adjustable mortgage rates or
7 balloon payments or whatever.

8 But when you look at that whole spectrum
9 then of folks who are being affected by these
10 financing mechanisms in the housing market and you
11 try to look at government policies that would
12 stabilize that, both for the sake of maybe the family
13 and for the sake of the overall health of our
14 nation's or our State's economy, do you have any
15 insights, observations, or guidance that you can give
16 to us about what is a sound fiscal public policy?

17 You know, I mean, I struggle with whether or
18 not it is my responsibility as a taxpayer to bail out
19 somebody who is being irresponsible with their money
20 versus the impact that is going to have on the whole
21 economy, and my heart would rather protect those
22 folks who kind of were unwittingly drawn into
23 something through no fault of their own. But I'm not
24 quite sure how to distinguish that, and that is just
25 an individual opinion versus what is a good public

1 policy opinion.

2 MR. DIFFLEY: It a very, very vexing
3 problem. I think your last sentence captured it, in
4 fact. You said it was individual, but that is
5 exactly the problem.

6 In order to bail out, I mean, we would like
7 to bail out those who inadvertently are in a position
8 where suddenly they have got this balloon mortgage
9 payment coming up but a very high adjustable reset
10 that they were unprepared for, but in bailing them
11 out, we are also going to bail out, say, the not so
12 deserving folks who thought they could flip a house
13 every 6 months, all right, and were in it for a quick
14 buck and lost some money. Well, that's the way the
15 market works.

16 We also do not want to interfere in forcing,
17 say, banks to reset or lenders to reset mortgages at
18 a lower rate. We don't want to interfere with the
19 future provision of mortgages by the banking system.
20 Some of the things we could do -- and we have avoided
21 this thus far -- would have the perverse effect, for
22 instance, if you didn't let mortgage rates go up,
23 would have the perverse effect of decreasing credits
24 for mortgages in the future, which just deepens the
25 problem going forward, and you do not want to do that

1 either, and yet on the other hand you do want to help
2 out deserving people.

3 Here is the fundamental problem, and we
4 still don't know the answer to this: How much of an
5 adjustment will there be in home prices across the
6 country, across Pennsylvania to be sure? We see
7 decreases out in home prices actually over the last
8 year in western Pennsylvania, not so much in eastern
9 Pennsylvania where there was in fact a significant
10 appreciation, but we might still see an adjustment in
11 the Philadelphia area, for instance, that is
12 significant, and it is precisely that uncertainty
13 around the current dynamics of the housing market.

14 You all know that nothing is selling now
15 virtually, right? It has buyers and sellers on both
16 sides wondering which way they should go. If prices
17 come down another 10 percent, that puts that many
18 more people in deep difficulty.

19 The reason we got caught up -- we, you know,
20 as a group of people -- got caught up in the bad
21 mortgages and the like was this expectation that
22 prices would continue, home values and equity would
23 continue rising at 10 and 20 percent per year, and
24 once that was taken away, you know, the pyramid
25 collapsed or whatever, the balloon burst.

1 It is a very vexing problem as to how to go
2 about fixing it. As a result, I think the initial
3 response by Treasurer Paulson at the U.S. level was
4 about the best that could be done, but because it was
5 limited, it was going to have a relatively small
6 effect. We are still seeing the issue play out.

7 Very, very vexing. I don't have good
8 advice, in other words.

9 REPRESENTATIVE MANDERINO: So, for example,
10 on the economic stimulus, meaning getting checks,
11 actual cash, into folks' hands, we have a model,
12 because we have done that in the past, where we can
13 kind of predict what effect that will have.

14 MR. DIFFLEY: Correct. Right.

15 REPRESENTATIVE MANDERINO: On this housing
16 stuff, we don't really have the model, so, I mean, is
17 that--- Have we tried to do something? I mean, I
18 don't know in my recollection that we have ever kind
19 of tried to---

20 MR. DIFFLEY: Yeah.

21 REPRESENTATIVE MANDERINO: I mean, except
22 for the Feds and their, you know, adjusting the
23 interest rate, I don't know that we have a historic
24 framework to look back and say, government tried this
25 way of stabilizing the housing market and it worked

1 or it didn't work.

2 MR. DIFFLEY: You see, the assets involved,
3 the trillions and trillions of dollars in assets
4 involved in housing, make it prohibitively expensive
5 for the government really to do anything. So you
6 have to be careful, you know, what you advise, and
7 that is really the crux.

8 It is not so much that we don't have a model
9 as we have a model and it tells us to be careful of,
10 you know, whatever interference we put in the normal
11 market conditions, even though clearly there has been
12 market failure at this point.

13 REPRESENTATIVE MANDERINO: Thank you.

14 Thank you, Mr. Chairman.

15 CHAIRMAN EVANS: Representative Fred
16 McIlhattan.

17 REPRESENTATIVE McILHATTAN: Thank you, Mr.
18 Chairman.

19 Now, your projections show the economy
20 slowing and maybe even going into a mild recession.
21 You show employment growth very slow, if at any.

22 MR. DIFFLEY: Right.

23 REPRESENTATIVE McILHATTAN: Now, the
24 Governor builds his budget this year, the one he
25 presented to us, on a projection of a personal income

1 tax increase in the amount there of about 5.2
2 percent, and he shows the sales tax growth of 3.4
3 percent. Based upon your projections of what is
4 going on in the economy, is this growth in the income
5 tax and in the sales tax going to be there?

6 MR. DIFFLEY: It seems to me in looking at
7 it, and you are talking about the fiscal '08-'09
8 projections?

9 REPRESENTATIVE McILHATTAN: Yeah.

10 MR. DIFFLEY: That I have seen, and I don't
11 analysis the revenue structure specifically, but
12 those big tax of sales, income, and I have seen the
13 corporate tax, look to me to be, if anything,
14 conservative estimates, all right?

15 REPRESENTATIVE McILHATTAN: Okay.

16 MR. DIFFLEY: Even though the budget, even
17 accounting for my slightly lower baseline economic
18 growth, so.

19 REPRESENTATIVE McILHATTAN: Because you have
20 the 5-percent growth in personal income revenue and
21 the 3.4-percent growth in sales tax revenue, in your
22 opinion, they are very safe. So is that what you are
23 telling me?

24 MR. DIFFLEY: Right. They don't strike me
25 as aggressive. That is correct.

1 REPRESENTATIVE McILHATTAN: Okay. Thank
2 you.

3 CHAIRMAN EVANS: Representative Bill Keller.

4 REPRESENTATIVE KELLER: Thank you, Chairman
5 Evans, and good morning, Mr. Diffley.

6 I read a report from Paul F. Richardson
7 Associates. It says that imports in the United
8 States will increase 100 percent over the next 10
9 years.

10 MR. DIFFLEY: Yes, sir.

11 REPRESENTATIVE KELLER: And also that the
12 manufacturing that is now based in China will move
13 into India. It will follow the cheaper labor into
14 India.

15 MR. DIFFLEY: Yes.

16 REPRESENTATIVE KELLER: That opens up the
17 possibility that to save transportation costs, they
18 can now ship through the Suez Canal. If it goes
19 through the Suez Canal, Pennsylvania is perfectly
20 placed to receive a lot of that new shipping.

21 Do you have any numbers on how that would
22 impact economic development and job growth in
23 Pennsylvania?

24 MR. DIFFLEY: I don't have any numbers on
25 that, but you are quite correct that the shipping

1 through the New York and New Jersey ports has been
2 very beneficial to northern New Jersey and indeed to
3 the Allentown area, which serves as a warehouse and
4 logistical center now and down through York and the
5 like. And shipping up through the Baltimore and
6 Philadelphia ports would do so as well, by all means.

7 REPRESENTATIVE KELLER: One more question.

8 I know everyone talks about the brain drain
9 and that, you know, we follow kids that have college
10 degrees and most of them have to move to the Sun Belt
11 to chase jobs.

12 MR. DIFFLEY: Right.

13 REPRESENTATIVE KELLER: But just, I have
14 been watching locally in Philadelphia. The
15 stagehands' union is talking about a very large group
16 of apprentices this year. They believe, because of
17 the film tax credit, that there are going to be a lot
18 of jobs that can't go South, because to make a movie,
19 you have to have certain, you know, housing stock and
20 different areas and different seasons, which they
21 can't get down South.

22 Is there anyone following the job growth for
23 those kids, the kids that will take over the
24 blue-collar jobs? We hear a lot about the brain
25 drain, but the blue-collar jobs, from what I see,

1 have the possibility to explode.

2 MR. DIFFLEY: Agreed, and, you know, if you
3 talk to the manufacturers, as I did recently in the
4 Philadelphia region, their biggest problem is
5 shortages of labor, and we are talking about
6 high-tech manufacturing jobs, advanced manufacturing.
7 There is an opportunity there, to be sure.

8 REPRESENTATIVE KELLER: So things are pretty
9 good in that area? We have some room for growth in
10 the blue-collar area?

11 MR. DIFFLEY: Yes, we do.

12 REPRESENTATIVE KELLER: Thank you very much.

13 CHAIRMAN EVANS: Who said Keller only knew
14 about the port? He also knows about movie stars,
15 too.

16 Representative Josh Shapiro.

17 REPRESENTATIVE SHAPIRO: Thank you, Mr.
18 Chairman.

19 Thank you for your testimony today. I want
20 to just focus on the issue of health care briefly and
21 the economic impact of the uninsured and the soaring
22 costs of health insurance in the Commonwealth.

23 We in the House are planning on having a
24 pretty significant debate on health care coming up in
25 the next few weeks or months, and the number that the

1 Governor uses, the number that I have heard, is that
2 there are 800,000 uninsured Pennsylvanians that are
3 placing a burden, at the very least, on our hospitals
4 through receiving their primary health care through
5 emergency rooms.

6 At the same time, we have small businesses
7 who are either offering less generous health
8 insurance plans to their employees or not offering
9 health insurance at all because they simply can't
10 afford the escalating rates of health insurance.

11 Anecdotally I'm aware of many examples of
12 this playing out in Pennsylvania. Can you provide
13 any empirical data about how the uninsured and how
14 those working who are paying more for their health
15 care is impacting the Pennsylvania economy?

16 MR. DIFFLEY: No, I cannot give any
17 estimates, I don't have any estimates at my disposal,
18 but it is certainly an issue, and it is an issue that
19 not only Pennsylvania but other States are grappling
20 with.

21 The cost of health care is a very important
22 issue, not just for individuals but a very costly
23 factor in the cost of doing business, and States, as
24 you are well aware, are devising their own programs
25 in, I guess in the absence of real Federal

1 initiatives in this regard.

2 It is certainly an important factor, and the
3 U.S. economy will continue to be more important, more
4 and more important going forward.

5 REPRESENTATIVE SHAPIRO: But there are no
6 specific indicators that one could look at? Is there
7 any research that can be done to try and put an
8 empirical value on the lack of health insurance or
9 affordable health insurance?

10 MR. DIFFLEY: Oh, there is, or should be. I
11 haven't done it or Global Insight has not done it per
12 se, and I am not aware of quality work, say, done on
13 Pennsylvania itself. But it could be done. I mean,
14 it could be quantified. I don't mean to imply it
15 couldn't be. I just would hesitate to put a number
16 on it myself.

17 REPRESENTATIVE SHAPIRO: Okay.

18 Thank you, Mr. Chairman.

19 CHAIRMAN EVANS: Thank you very much.

20 Representative John Myers.

21 REPRESENTATIVE MYERS: Thank you, Mr.
22 Chairman.

23 Good morning.

24 MR. DIFFLEY: Good morning.

25 REPRESENTATIVE MYERS: I'm losing track of

1 time.

2 Actually, I wasn't going to ask you
3 anything, but something came to my mind, when you
4 talked about, you know, industry watching around
5 energy, and, you know, one of the proposals that is
6 being pushed forward is alternative energy.

7 Do you have any sense how long it will be
8 before cellulose fuel can become a product that folks
9 can buy? That is one, because I know it is down the
10 line. I don't think we even have a refinery in the
11 Commonwealth that can even do cellulose yet.

12 MR. DIFFLEY: No.

13 REPRESENTATIVE MYERS: So I wonder how long
14 that is going to take.

15 Once we get there, what regions of the
16 Commonwealth most likely will process and manufacture
17 this alternative fuel? If you can give us an idea of
18 what jobs are going to be created. And are these
19 jobs going to be blue-collar jobs or high-income-type
20 jobs?

21 And the other question to that that actually
22 I'm really trying to figure out, what impact is this
23 going to have on existing refineries? I mean, for
24 example, does that mean that Sunoco is going to
25 switch gears and go from fossil fuel to cellulose

1 fuel, or would they try to make it a part of their
2 product mix?

3 Do you have any idea? Do you know what this
4 industry is going to look like?

5 MR. DIFFLEY: Sure. Well, I have an idea.
6 I'm not an energy expert.

7 The recent move to ethanol and cellulose has
8 really taken steam. I don't know how long lasting it
9 will be. In other words, I would hope better
10 alternatives appear relatively soon.

11 The answer about, you know, the current
12 refineries, probably to a mix to some extent.

13 I think the bolder and more substantial
14 gains in the future, particularly for Pennsylvania,
15 are not in ethanol or cellulose but in other types of
16 green technology developing, be it solar cells, wind
17 power, et cetera, and there we can talk about
18 high-tech jobs, high-value-added jobs, that can
19 contribute a lot going forward if the country
20 ultimately moves to greener and cleaner energy.

21 I think Pennsylvania is well positioned for
22 that type of research and another example of new
23 high-tech, manufacturing-type jobs available.

24 REPRESENTATIVE MYERS: All right.

25 Thank you, Mr. Chairman.

1 CHAIRMAN EVANS: I would like to thank you,
2 as usual, for coming before this committee and
3 providing your insight to all of us, to help all of
4 us.

5 And I want to say to all of the members, I'm
6 proud of all of the members' questions and comments.
7 We -- we, collectively -- have a lot of work to do,
8 short term and long term, to address these issues
9 that we face today.

10 And it is about the economy. You know,
11 ultimately, for all of us, no matter what perspective
12 we come from, we can't do anything about the economy
13 if people don't have confidence in the economy and
14 what we do. So we do really need to work together to
15 order to address the issues that we face today.

16 I don't think it is a quick answer. I don't
17 think either party has the answer. I think we
18 collectively have to come up with some way to figure
19 out what we are doing, and your insight helps us. I
20 mean, it really does, I know at least in my case
21 personally you helping us as an outsider, because
22 sometimes I think we get lost in the major and in the
23 minor and forget about the big picture. But you help
24 us, so again I want to thank you for coming before
25 this committee.

1 This committee is recessed for 5 minutes,
2 and then we have the Historical and Museum Commission
3 in 5 minutes.

4 We will recess for 5 minutes.

5 MR. DIFFLEY: Thank you, and I appreciate
6 the remarks, Mr. Chairman. My pleasure, and good
7 luck to all of you.

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9 (The hearing concluded at 11:10 a.m.)

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1 I hereby certify that the proceedings and
2 evidence are contained fully and accurately in the
3 notes taken by me on the within proceedings and that
4 this is a correct transcript of the same.

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Debra B. Miller, Reporter

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