

# Revenue and Economic Update

July 10, 2020

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## Revenues Above May 2020 Projection

Minnesota’s net general fund receipts for FY 2020 are now estimated to total \$21.798 billion, \$168 million (0.8 percent) more than projected in the May 2020 *Interim Budget Projection*. Net tax receipts exceeded the projection for income, corporate, and sales taxes, more than offsetting net revenues from other taxes that were lower than projected. State revenues in the final quarter of FY 2020 were \$168 million (2.9 percent) more than projected in May. (See page 4 for details.)

Net individual income tax receipts are estimated to end the year \$75 million (0.7 percent) more than forecast. Gross income tax receipts were \$16 million above the projection, and refunds were \$59 million less than expected. Because this year taxpayers were allowed to make their final tax year 2019 payments on July 15, our estimate of those payments is excluded from the net income tax projection. This is further explained below when we discuss revenue accruals. We will not know final tax year 2019 income tax liability until extension returns are filed, and processing is complete. This will likely be mid-January 2021.

Income tax withholding receipts exceeded the projection by \$93 million, however, this is the result of timing of receipts and not higher than projected economic activity. We expect the positive variance to be offset by lower than projected withholding receipts in July.

Estimated income tax payments (labeled declarations on page 4) includes \$29 million of extension payments for tax year 2019 paid ahead of the July 15 deadline. On net, estimated payments were \$49 million below the projection. This may be due—in part or in whole—to a change in the safe harbor rule that allows taxpayers to avoid penalty, interest, or additional tax charges on their 2020 balance due by paying at least 75 percent of their 2018 liability.

Net general sales tax receipts are estimated to end FY 2020 \$87 million (1.5 percent) above the projection. Gross sales tax payments were above the projection, and refunds were lower than expected. Net corporate receipts were \$29 million (1.9 percent) more than projected. Gross corporate tax payments were above the projection, and refunds were lower than expected. Other revenues were \$24 million (0.7 percent) lower than expected.

All FY 2020 results are preliminary and subject to change. The state’s fiscal year that ended June 30, 2020, will officially close on August 21. Values in the estimated closing column on page 4 reflect actual revenues attributable to FY 2020 as well as estimates of revenue accruals through closing and other pre-close adjustments. Tax year 2019 income tax payments—which are not due until July 15 this year—are attributable to FY 2020. We have excluded our estimate of those payments from our accruals estimate, and we have excluded our projection

## Summary of Revenues: Fiscal Year 2020

(\$ in millions)	May 2020 Projection	Estimated	\$ Difference	% Difference
		Closing Revenues		
Individual Income Tax	\$10,959	\$11,034	\$75	0.7%
General Sales Tax	5,675	5,762	88	1.5
Corporate Franchise Tax	1,555	1,584	29	1.9
Other Revenues	3,441	3,417	(24)	(0.7)
<b>Total Revenues<sup>1</sup></b>	<b>\$21,630</b>	<b>\$21,798</b>	<b>\$168</b>	<b>0.8%</b>

1. Totals may not add due to rounding.

for TY 2019 net income tax payments from the projected revenues column. We will report actual tax year 2019 income tax receipts in a special memo at the end of July.

As of June 30, total FY 2020 revenue was \$21.814 billion. Estimated accruals and pre-close adjustments—other than tax year 2019 individual income tax payments due July 15—subtract about \$16 million. The subtraction is primarily due to corporate and sales tax refunds attributable to FY 2020 that are expected to be paid out prior to the close. A complete reporting of FY 2020 revenues will be part of October’s *Revenue and Economic Update*.

## U.S. Economic Outlook Worsens Amid Surging COVID-19 Cases

The ongoing COVID-19 pandemic continues to challenge the U.S. economy, and a surge of new infections in June caused several states to pause or reverse their plans to reduce restrictions on activity. The outlook for U.S. real GDP growth in 2020 has weakened since MMB’s *Interim Budget Projection* was released in May. The Bureau of Economic Analysis (BEA) estimates that real GDP decreased at an annual rate of 5.0 percent during the first quarter of 2020. IHS Markit (IHS), Minnesota’s macroeconomic consultant, is now forecasting a 6.1 percent decline in real GDP in 2020, down from a 5.4 percent decline in their April forecast, which informed our *Interim Budget Projection*. The change is primarily due to a lower forecast for real consumer spending and state and local government budget cuts to address revenue shortfalls.

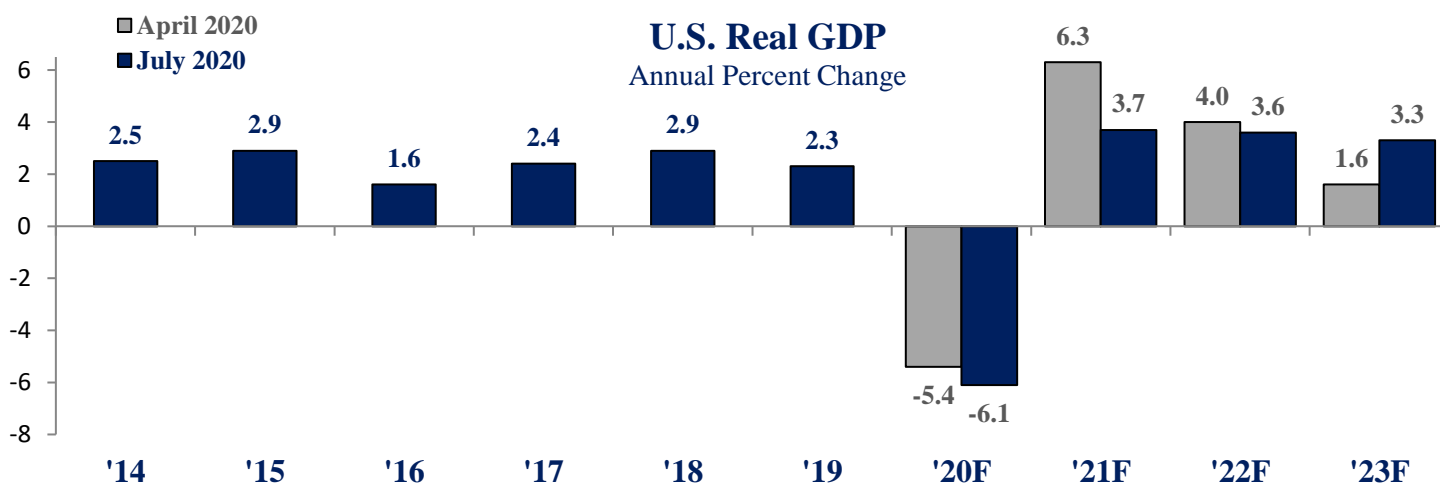
IHS expects the recent increase in infections to renew caution by consumers and businesses. Combined with heightened financial burdens on households, as delayed rent and mortgage payments become due and federal fiscal support expires, this leads to a forecast decline in 2020 real consumer spending of 5.8 percent, down from a 5.4 percent decline in IHS’ April outlook.

The July outlook includes the impact of \$3.0 trillion from four federal stimulus packages enacted this year. Without additional federal support, state and local governments face substantial revenue shortfalls in the coming fiscal years. IHS has reduced their forecast of state and local government spending in their July outlook.

IHS expects real GDP growth to turn positive in the third quarter, and they forecast 3.7 percent annual growth in 2021. They expect real GDP to reach its pre-recession level in 2022. The recession is expected to dampen business investment, and slower growth in capital services will limit economic growth. Consequently, while the U.S. is forecast to regain full employment in 2024, IHS expects GDP in that year to remain slightly below the pre-pandemic potential GDP forecast.

Oil prices remain below early-2020 levels and continue to dampen U.S. real GDP growth through reduced production and diminished investment in equipment and structures in the U.S. energy sector. IHS expects oil prices to gradually rise, reaching the level at which U.S. drilling and production can stabilize by late 2021.

The IHS July baseline forecast is similar to the Blue Chip Consensus, the median of 50 business and academic forecasts. IHS expects real GDP to decline 6.1 percent in



Source: Bureau of Economic Analysis and IHS Markit.

2020, a larger contraction than the Blue Chip Consensus of -5.5 percent for this year. The Blue Chip Consensus calls for 4.0 percent growth in 2021, above IHS' 3.7 percent forecast for that year.

The Bureau of Labor Statistics (BLS) reports that in June the seasonally adjusted U.S. unemployment rate was 11.1 percent, down from 14.7 percent at the peak of unemployment reported in April, when most of the country was under stay at home orders. IHS expects that unemployment will remain above 8 percent through 2020 before gradually drifting back down to pre-COVID19 levels in 2024. The labor force participation rate was 61.5 percent in June, up from 60.8 in May, but still much lower than 63.0 percent one year ago. The BLS also reported that U.S. employers added 4.8 million jobs in June, but there were still 15 million fewer jobs in June than in February. The monthly jobs data were better than expected; however, the data was collected in mid-June, prior to surging daily cases in Arizona, Florida, Texas, and several other states.

In an attempt to keep financial markets stable, the FOMC cut rates by 50 basis points on March 3 and further by 100 basis points on March 16, bringing the effective target federal funds rate to zero. IHS expects the federal funds rate to remain near zero until late 2026.

IHS assigns a 50 percent probability to the July baseline outlook. They assign a 30 percent probability to a more pessimistic scenario, in which the COVID-19 outbreak causes a deeper recession and a slower recovery than the baseline. In this scenario, both the pace of reopening is slower than the baseline due to widespread infections, and the decline in consumer spending in April-June was lower than estimated in the baseline. In their more optimistic scenario, IHS assumes a faster, "V-shaped" recovery. The underlying assumption for this scenario is that the spread of COVID-19 and its health ramifications are less severe than estimated in the baseline, and the number of daily cases begins a steep decline. This scenario receives a 20 percent probability. IHS notes that, because economic outcomes depend on the pandemic's course, all forecasts remain highly uncertain.

# Comparison of Actual and Projected Non-Dedicated Revenues

(\$ in thousands)

	Fiscal Year 2020			April-June 2020		
	PROJECTED	ESTIMATED	VARIANCE	PROJECTED	ACTUAL	VARIANCE
	REVENUES <sup>1</sup>	CLOSING REVENUES	ACT-FCST	REVENUES	REVENUES	ACT-FCST
<b>Individual Income Tax</b>						
Withholding	9,603,939	9,697,081	93,143	2,284,700	2,377,843	93,143
Declarations	1,896,964	1,847,480	(49,484)	652,256	602,773	(49,484)
Miscellaneous	1,261,105	1,233,189	(27,916)	554,167	526,251	(27,916)
Gross	12,762,008	12,777,751	15,743	3,491,124	3,506,866	15,743
Refund	1,802,600	1,743,417	(59,183)	577,691	518,508	(59,183)
Net	10,959,408	11,034,333	74,926	2,913,433	2,988,358	74,926
<b>Corporate Franchise Tax</b>						
Declarations	1,580,720	1,585,090	4,370	441,917	446,287	4,370
Miscellaneous	207,370	214,463	7,093	(53,331)	(46,237)	7,093
Gross	1,788,090	1,799,554	11,463	388,586	400,049	11,463
Refund	233,267	215,381	(17,886)	41,250	23,364	(17,886)
Net	1,554,823	1,584,173	29,350	347,336	376,686	29,350
<b>General Sales and Use Tax</b>						
Gross	5,858,497	5,938,347	79,850	1,526,151	1,606,001	79,850
Mpls. sales tax transferred to MSFA	2,120	2,120	(0)	466	466	(0)
Sales Tax Gross	5,860,617	5,940,467	79,849	1,526,617	1,606,467	79,849
Refunds (including tribal refunds)	186,102	178,207	(7,895)	83,092	75,197	(7,895)
Net	5,674,515	5,762,260	87,745	1,443,525	1,531,270	87,745
<b>Other Revenues:</b>						
Net Estate	163,900	147,184	(16,715)	51,662	34,947	(16,715)
Net Liquor/Wine/Beer	95,260	94,321	(939)	32,086	31,147	(939)
Net Cigarette/Tobacco	577,270	582,235	4,964	185,913	190,877	4,964
Deed and Mortgage	291,633	304,951	13,318	83,756	97,074	13,318
Net Insurance Premiums Taxes	421,727	417,017	(4,710)	94,881	90,171	(4,710)
Net Lawful Gambling	79,750	79,446	(305)	7,309	7,004	(305)
Health Care Surcharge	303,777	266,716	(37,061)	133,578	96,517	(37,061)
Other Taxes	19,755	15,707	(4,048)	19,486	15,438	(4,048)
Statewide Property Tax	726,660	753,318	26,657	353,454	380,111	26,657
DHSSOS Collections	78,650	92,756	14,106	7,488	21,595	14,106
Investment Income	70,000	74,178	4,178	8,541	12,719	4,178
Tobacco Settlement	154,254	152,282	(1,972)	9,785	7,813	(1,972)
Dept. Earnings & MSOP Recov.	221,251	224,913	3,662	60,665	64,327	3,662
Fines and Surcharges	74,965	64,983	(9,982)	25,727	15,745	(9,982)
Lottery Revenues	61,500	65,107	3,608	25,503	29,111	3,608
Revenues yet to be allocated	(0)	1,420	1,420	(1,971)	(551)	1,420
Residual Revenues	106,642	86,235	(20,407)	25,529	5,123	(20,407)
Other Subtotal	3,446,994	3,422,768	(24,226)	1,123,393	1,099,167	(24,226)
Other Refunds	6,003	5,675	(328)	1,587	1,259	(328)
Other Net	3,440,991	3,417,093	(23,899)	1,121,806	1,097,907	(23,899)
<b>Total Gross</b>	<b>23,857,710</b>	<b>23,940,539</b>	<b>82,829</b>	<b>6,529,720</b>	<b>6,612,549</b>	<b>82,829</b>
<b>Total Refunds</b>	<b>2,227,973</b>	<b>2,142,681</b>	<b>(85,292)</b>	<b>703,620</b>	<b>618,328</b>	<b>(85,292)</b>
<b>Total Net</b>	<b>21,629,737</b>	<b>21,797,858</b>	<b>168,121</b>	<b>5,826,100</b>	<b>5,994,222</b>	<b>168,121</b>

1. May 2020 Interim Budget Projection.