Economic Update

Minnesota
Department of Finance

April 2001

State Revenues Below Forecast in February and March

Net general fund revenues totaled $1.869 billion during February and March, $60 million, (3.1 percent) less than forecast. Receipts from the four major taxes were $1.623 billion, $64 million (3.8 percent) less than anticipated. Income tax receipts were slightly above forecast, but net receipts from the sales tax, corporate income tax, and motor vehicle sales tax were all below anticipated levels. Fiscal year 2001 receipts now total $9.183 billion, 5.4 percent above last year's receipts for the first nine months of the fiscal year.

Summary of Tax Receipts: February - March 2001

	Estimate	Actual	Variance	Percent
	---------------($ in millions)---------------			
Income	803.0	814.2	11.2	1.4
Sales	565.7	545.9	(19.8)	(3.5)
Corporate	236.3	185.4	(50.8)	(21.5)
Motor Vehicles	81.7	77.1	(4.6)	(5.6)
Other	241.7	246.1	4.3	1.8
TOTAL	1,928.4	1,868.7	(59.7)	(3.1)

Much of the revenue shortfall occurred in the corporate income tax where net receipts were $51 million below forecast. Corporate estimated payments due in mid-March were $40 million below February's projection, reflecting a weaker than anticipated outlook for corporate profits. Variances for the other major revenue sources were within normal bounds. Minnesota's income tax receipts and gross sales tax receipts continue to track the forecast very closely. (See page 4) Individual withholding receipts were $10 million (1.4 percent) more than forecast. While gross sales tax receipts in March were down $9 million from last year's level, they were just $3.8 million (0.6 percent) below forecast for the two month period. Payment of $16 million more than projected in sales tax refunds caused the large variance.

Individual income tax receipts include only withholding and individual estimated tax payments. Variances in tax year 2000 refunds and final payments are not reported during the tax-processing season. Those variances will be reported after processing of all timely 2000 tax year returns has been completed. The variance for other revenues was adjusted to reflect a timing change in receipt of federal TANF funds.

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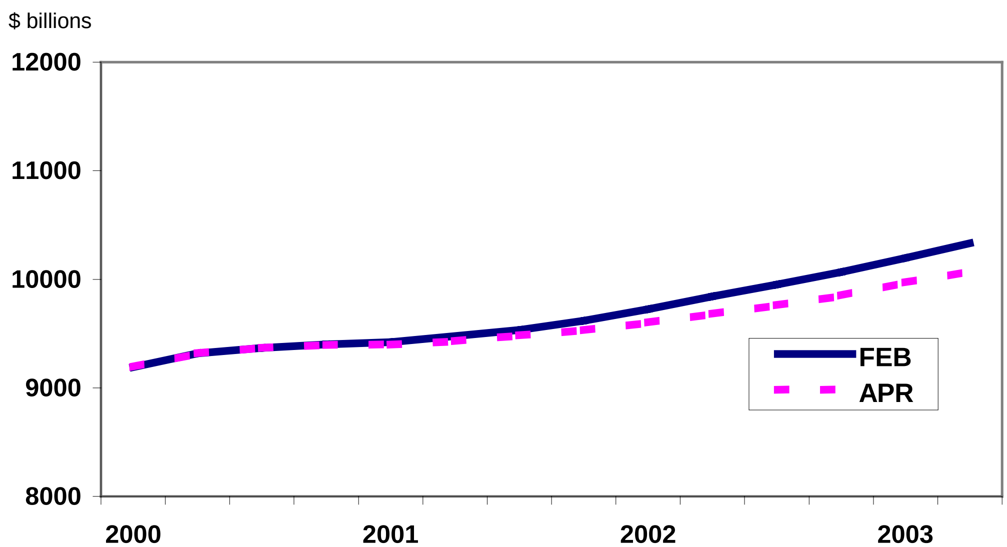
Slower Growth for the U.S. Economy in 2001, 2002, and 2003.

The outlook for the U.S. economy has weakened considerably during the past few months. Everyone knew the real GDP growth rates observed in late 1999 and early 2000 were too strong to be sustainable, even in a "new economy." But, no one suspected that at the end of the first quarter of 2001 economists would be searching for any sign of economic growth. The Federal Reserve tightening, the collapse of a speculative technology bubble, an energy price shock, and a holiday season slump in consumer confidence produced a faster and steeper slowdown than forecasters thought likely as recently as four months ago.

Most economists believe a recession still can be avoided, but there are no guarantees. Fourth quarter real GDP grew at just a 1.0 percent annual rate, and the recently released March employment report provided a sobering reminder of just how fragile the outlook has become. The good news was that unemployment was just 4.3 percent and the U.S economy added 342,000 jobs in the first quarter. The bad news was that March payrolls fell by a seasonally adjusted 86,000 jobs. Since real GDP growth in the first quarter of 2001 is generally acknowledged to have been very weak (and possibly negative), a quick pick-up in job growth will be necessary if the economy is to continue growing.

Consumers appear ready to do their part. Consumer confidence has turned up again, and first quarter spending appears to have increased at an annual rate of about 3 percent. Business spending is the problem. Capital expenditure has gone from the strongest to the weakest part of the economy, and managers appear to see little reason to spend for new equipment until their current productive capacity is more fully utilized. To date, those additional orders are not in sight. An oversupply of only slightly used computer and tele-communications equipment from failed dot coms is only part of the problem. While that must be worked through before the all important tech sector can begin to grow again, non-tech capital spending will also need to recover before the economy is fully back on track.

DRI Cuts Back Real GDP Estimates Through End of Fiscal 2003

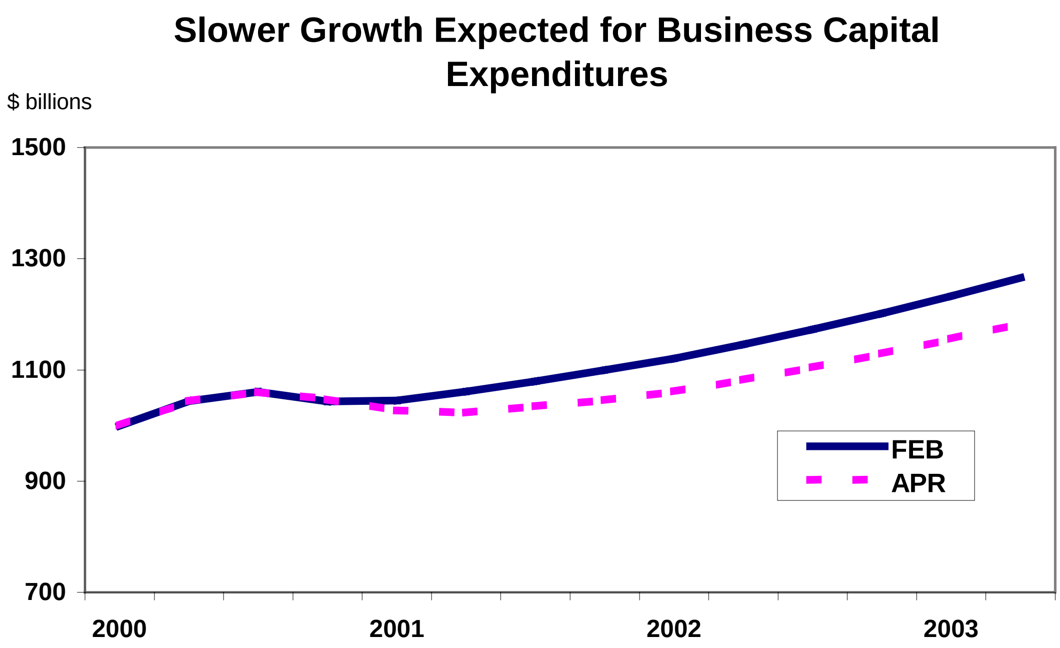


Minnesota's national economic consultant Data Resources Inc. (DRI), continues to believe that the U.S. economy can avoid a recession, but their outlook is nowhere near as rosy as it was earlier this year. February's Control contained a weak first quarter followed by a quick rebound and a strong second half for 2001. Now, DRI Chief David Wyss believes the economy's likely path for the next twelve months to be a "crawl-back" not the quick bounce-back forecast only two months ago. DRI's April Control expects real GDP growth to be just 0.2 percent in the recently completed first quarter of 2001. They now project 1.5 percent growth for all of 2001, followed by growth at annual rates of 2.8 percent growth in 2002 and 4.1 percent in 2003. In February's Control growth rates of 2.1 percent, 4.0 percent and 4.8 percent were forecast for 2001, 2002, and 2003, respectively.

DRI assigns a 50 percent probability to their Control scenario, the same as February. Their pessimistic scenario in which the economy slipped into recession last quarter is given a likelihood of 40 percent. The recession in that scenario is both deeper and longer than those they previously projected. The April Blue Chip consensus sets the odds of a recession in 2001 at 38 percent.

Weaker Economic Growth Would Reduce Fiscal 2002-03 Revenues

If DRI's April forecast holds, state revenues will be lower. Their outlook for spending on producers' durable equipment has, for example, been cut back substantially to reflect their belief that business investment will remain stagnant through 2001. DRI now projects producers' durable equipment spending to grow at only a 1.5 percent annual rate in fiscal 2002, down more than 4 percent from the growth rate forecast in February.



DRI's more restrained outlook for 2002 and 2003 also affects the income tax. Projected wage growth has changed only slightly, but there were significant changes elsewhere in the income tax base. For example, DRI's outlook for stock market growth (which helps determine both capital gains income and pension income) was cut by more than 7 percent per year for both 2001 and 2002.

	2001 Fiscal Year to Date			February – March, 2001		
Four Major Revenues:	**Forecast Revenuues**	**Actual Revenues**	**Variance Act-Fcst**	**Forecast Revenues**	**Actual Revenues**	**Variance Act-Fcst**
Individual Income Tax						
Withholding	3,627,900	3,638,279	10,379	762,812	773,191	10,379
Declarations	734,477	735,323	845	40,200	41,045	845
Miscellaneous	111,740	111,740	0	0	0	0
Gross	4,474,117	4,485,342	11,225	803,012	814,236	11,225
Refunds	69,192	69,192	0	0	0	0
Net	4,404,925	4,416,150	11,225	803,012	814,237	11,225
Corporate & Bank Excise						
Declarations	607,030	567,250	(39,780)	196,100	156,320	(39,780)
Miscellaneous	146,738	129,238	(17,500)	58,200	40,700	(17,500)
Gross	753,768	696,488	(57,281)	254,300	197,019	(57,281)
Refunds	119,500	113,058	(6,442)	18,022	11,580	(6,442)
Net	634,268	583,430	(50,839)	236,278	185,439	(50,839)
Sales Tax						
Gross	2,907,233	2,903,399	(3,835)	596,440	592,605	(3,835)
Refunds	161,803	177,809	16,006	30,691	46,697	16,006
Net	2,745,430	2,725,589	(19,841)	565,749	545,908	(19,841)
1999 Sales Tax Rebates	(493)	(493)	0	0	0	0
2000 Sales Tax Rebates	2,000	2,165	165	(1,282)	(1,117)	165
Motor Vehicle Sales	382,490	377,880	(4,610)	81,700	77,090	(4,610)
Other Revenues:						
Inherit/Gift/Estate	45,373	41,441	(3,933)	12,233	8,301	(3,933)
Liquor/Wine/Beer	41,435	41,021	(414)	9,062	8,648	(414)
Cigarette & Tobacco	124,079	123,685	(394)	26,484	26,090	(394)
Deed and Mortgage	113,010	114,097	1,087	20,355	21,442	1,087
Insurance Gross Earnings	107,482	112,777	5,295	53,709	59,004	5,295
Lawful Gambling	40,206	39,656	(550)	8,923	8,373	(550)
Health Care Surcharge	86,516	86,063	(453)	20,207	19,754	(453)
Other Taxes	904	738	(166)	368	202	(166)
DHS RTC Collections	8,417	7,363	(1,055)	4,704	3,650	(1,055)
Income Tax Reciprocity	42,610	42,610	0	0	0	0
Investment Income	136,250	138,048	1,799	30,931	32,730	1,799
Tobacco Settlement	116,112	116,112	0	0	0	0
Revenues yet to be Allocated	0	3,261	3,261	(1,740)	1,521	3,261
Residual Revenues Less Refunds	225,010	222,058	(2,952)	63,915	60,963	(2,952)
Other Subtotal	1,087,404	1,088,930	1,525	249,152	250,677	1,525
Other Refunds	13,030	10,313	(2,717)	6,237	3,519	(2,717)
Other Net	1,074,375	1,078,617	4,243	242,915	247,158	4,243
Total Gross	9,606,519	9,553,710	(52,809)	1,983,321	1,930,511	(52,809)
Total Refunds	363,525	370,372	6,847	54,949	61,796	6,847
Total Net	9,242,995	9,183,338	(59,656)	1,928,372	1,868,715	(59,656)