



Minnesota Department of Finance

January 2004

State Revenues On Forecast

Net general fund revenues totaled \$2.469 billion during November and December, \$2.8 million (0.1 percent) less than forecast. Income, sales and motor vehicle sales tax receipts were slightly below projections, while corporate income tax revenue and other tax and non-tax revenues exceeded predicted levels. Variances for all taxes were small and well below historical levels.

Summary of Tax Receipts: (November-December, 2003)

| | <u>Estimate</u> | <u>Actual</u> | <u>Variance</u> | <u>Percent</u> |
|----------------|------------------------------|---------------|-----------------|----------------|
| | ----- (\$ in millions) ----- | | | |
| Income | 902.6 | 900.7 | (1.9) | (0.2) |
| Sales | 657.0 | 651.0 | (6.0) | (0.9) |
| Corporate | 108.4 | 114.4 | 6.0 | 5.5 |
| Motor Vehicles | 43.6 | 37.9 | (5.7) | (13.1) |
| Other | <u>760.6</u> | 765.4 | <u>4.8</u> | <u>0.6</u> |
| Total | 2,472.2 | 2,469.5 | (2.8) | (0.1) |

Differences between projected and actual receipts for components of the major taxes were also small, but there were shortfalls in several key revenue sources. Fourth quarter estimated corporate income tax payments, were \$33 million, (22 percent), below forecast. (see page 4). The state's two largest sources of revenue, withholding tax receipts and gross sales tax receipts were also below forecast, with negative variances of \$10 million and \$17 million respectively. The largest sources of positive variances, corporate refunds, sales tax refunds, and individual estimated payments were all items where the timing of receipts and payments is less predictable.

Fourth quarter revenue comparisons should always be viewed with caution since those variances often reflect timing differences, not changes in the underlying economy. For example, even though individual estimated payments are not officially due until January 15, many taxpayers find it to their benefit to remit fourth quarter estimated state income tax payments before the end of the calendar year. In addition, retailers do not remit sales taxes collected during December's Christmas shopping season until late January. Only sales taxes collected by businesses through November are included in this report. Fiscal year-to-date collections through January will provide a better measure of how well Minnesota's revenues are tracking November's forecast, and that data will be used in preparing February's revenue forecast.

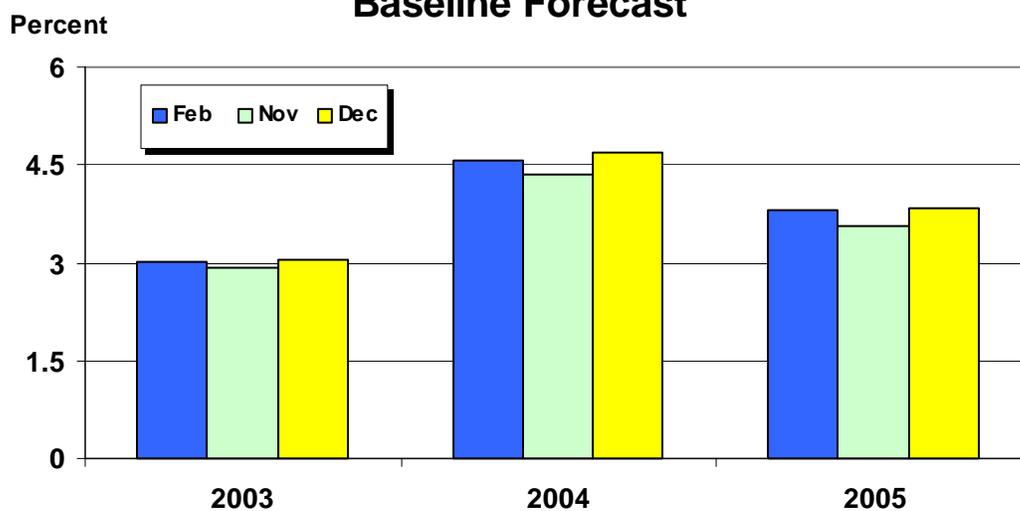
What A Difference A Year Makes

At the start of last year the economy just did not feel right. Many worried about the impact a potential war with Iraq would have on consumer and business spending, and the likely need for further fiscal stimulus was on every forecaster's mind. The official figures said the economy was growing, but employment was declining and the stock market was down for the third straight year. The combination of geo-political uncertainty and economic uneasiness was projected to lower expectations and limit spending by both consumers and businesses. The result was a forecast for relatively slow growth through mid summer of 2003.

Now, times seem better, even though there have been several substantial additions to the list of potential longer-term economic problems. The stock market is up, and, even though we ended the year with fewer jobs than in January 2003, there have been small monthly increases in payroll employment since mid-summer. The worsening trade deficit and the likelihood of substantial federal budget deficits far into the future are reasons for concern, but those concerns seem unlikely to affect near term spending by consumers or businesses. The consensus forecast is for economic growth to be strong enough this year that year-end employment levels will exceed those when the recession started in 2001. But, December's much weaker than expected employment report may dampen those expectations.

The December baseline forecast for 2004 from Global Insight Inc., (GII), Minnesota's national economic consultant, is very similar to the consensus forecast. GII expects real GDP growth of 4.7 percent in 2004 and 3.8 percent in 2005, up modestly from the growth rates of 4.3 percent and 3.6 percent projected in November. GII sees no reason for concern about inflation over the short term. They forecast CPI growth of just 1.3 percent during 2004 and 1.6 percent in 2005, down 0.1 percentage points in both years from their November estimate. The Blue Chip Panel's January consensus is for 4.6 percent growth and 1.7 percent inflation in 2004, followed by 3.7 percent real GDP growth and 2.1 percent increase in the CPI in 2005.

Continued Strong Real GDP Growth in Baseline Forecast

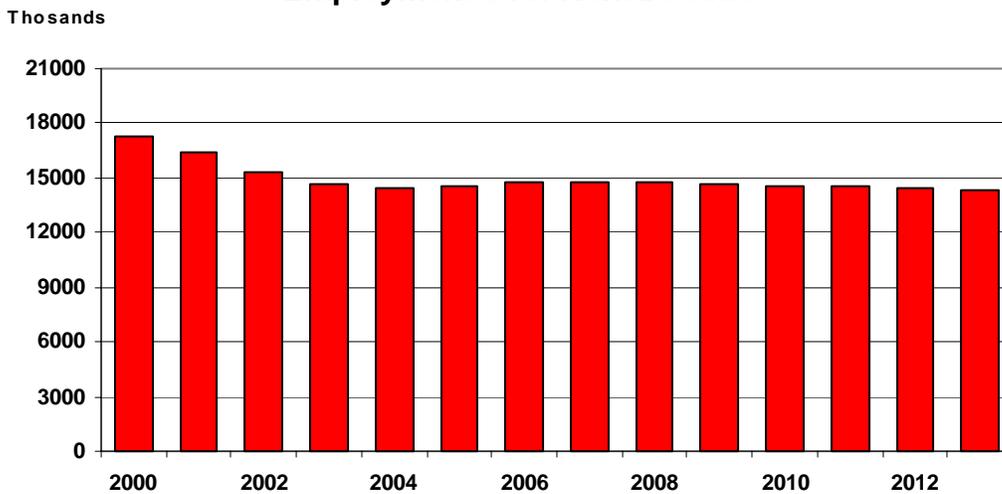


Global Insight assigns a 60 percent probability to their December baseline. A near-term boom scenario, which has 5.3 percent real GDP growth in 2004 and 4.0 percent growth in 2005 was given a 20 percent probability, as was a more pessimistic scenario. GII's more pessimistic scenario, however, is not terribly pessimistic. That scenario contains no recession, and 2004's real GDP growth rate exceeds that observed in 2003.

No Rebound in Manufacturing Employment in Sight

U.S. manufacturing employment fell by 16 percent, or nearly 2.8 million jobs between March of 2000 and November 2003. The decline began before the start of the 2001 recession, and few expect any material growth in manufacturing jobs in the foreseeable future. The December baseline forecast from Global Insight shows U.S. manufacturing employment shrinking slightly in 2004, then stabilizing. But by 2013 approximately 400,000 more manufacturing jobs will have disappeared and manufacturing employment will account for under 10 percent of all employment. In 1998 manufacturing jobs were 14 percent of U.S. employment.

No Growth Expected in U.S. Manufacturing Employment Over Next Decade



Manufacturing employment in Minnesota has fared better than that elsewhere in the U.S. During the 1980's and 1990's the number of manufacturing jobs in the state grew by nearly 20 percent even though US manufacturing employment was declining. And, while just over 50,000 manufacturing jobs have been lost in Minnesota since March 2000, that 14.5 percent decline is less than the national decline of 16 percent. In recent months Minnesota's outlook has improved modestly, with 2,500 manufacturing jobs being added since the economic recovery began to take hold in the June. It is unlikely, however, that there will be strong sustained growth in manufacturing employment in Minnesota over the next decade.

Comparison of Actual and Estimated Non-Restricted Revenues

(\$ in thousands)

| | 2004 Fiscal Year-to-Date | | | November-December 2003 | | |
|------------------------------------|--------------------------|------------------|-------------------|------------------------|------------------|-------------------|
| | Forecast Revenues | Actual Revenues | Variance Act-Fcst | Forecast Revenues | Actual Revenues | Variance Act-Fcst |
| Four Major Revenues: | | | | | | |
| Individual Income Tax | | | | | | |
| Withholding | 2,462,491 | 2,452,778 | (9,713) | 824,000 | 814,287 | (9,713) |
| Declarations | 303,875 | 312,612 | 8,736 | 84,228 | 92,964 | 8,736 |
| Miscellaneous | 94,902 | 93,542 | (1,360) | 25,968 | 24,608 | (1,360) |
| Gross | 2,861,268 | 2,858,931 | (2,337) | 934,196 | 931,859 | (2,337) |
| Refund | 74,400 | 74,007 | (393) | 31,540 | 31,147 | (393) |
| Net | 2,786,868 | 2,784,924 | (1,944) | 902,656 | 900,712 | (1,944) |
| Corporate & Bank Excise | | | | | | |
| Declarations | 328,500 | 295,523 | (32,976) | 149,400 | 116,424 | (32,976) |
| Miscellaneous | 55,835 | 70,190 | 14,354 | 24,000 | 38,354 | 14,354 |
| Gross | 384,335 | 365,713 | (18,622) | 173,400 | 154,778 | (18,622) |
| Refund | 86,510 | 61,861 | (24,649) | 65,000 | 40,351 | (24,649) |
| Net | 297,825 | 303,852 | 6,027 | 108,400 | 114,427 | 6,027 |
| Sales Tax | | | | | | |
| Gross | 2,005,090 | 1,988,100 | (16,990) | 692,816 | 675,826 | (16,990) |
| Refunds | 103,031 | 91,991 | (11,040) | 35,878 | 24,838 | (11,040) |
| Net | 1,902,059 | 1,896,109 | (5,950) | 656,939 | 650,988 | (5,950) |
| Motor Vehicle Sales | 145,215 | 139,559 | (5,656) | 43,568 | 37,911 | (5,656) |
| Other Revenues: | | | | | | |
| Inherit/Gift/Estate | 45,627 | 49,673 | 4,046 | 11,458 | 15,503 | 4,046 |
| Liquor/Wine/Beer | 34,346 | 33,612 | (734) | 11,397 | 10,662 | (734) |
| Cigarette/Tobacco/Cont Sub | 85,925 | 83,147 | (2,778) | 27,608 | 24,831 | (2,778) |
| Deed and Mortgage | 183,667 | 188,770 | 5,103 | 51,324 | 56,427 | 5,103 |
| Insurance Gross Earnings | 104,210 | 109,485 | 5,275 | 48,700 | 53,975 | 5,275 |
| Lawful Gambling | 25,025 | 23,437 | (1,588) | 9,105 | 7,517 | (1,588) |
| Health Care Surcharge | 110,202 | 112,697 | 2,495 | 37,319 | 39,815 | 2,495 |
| Other Taxes | 1,096 | 1,018 | (79) | 200 | 121 | (79) |
| state wide property tax | 268,290 | 267,513 | (777) | 268,171 | 267,394 | (777) |
| DHS RTC Collections | 21,529 | 21,880 | 351 | 7,214 | 7,565 | 351 |
| Income Tax Reciprocity | 46,242 | 46,242 | 0 | 46,242 | 46,242 | 0 |
| Investment Income | 8,144 | 7,721 | (424) | 2,616 | 2,192 | (424) |
| Tobacco Settlement | 168,656 | 168,467 | (189) | 168,556 | 168,367 | (189) |
| Departmental Earnings | 140,226 | 133,191 | (7,035) | 57,986 | 50,951 | (7,035) |
| Lottery Revenues | 14,738 | 15,362 | 624 | 6,110 | 6,734 | 624 |
| Revenues yet to be allocated | 2,092 | 1,967 | (125) | 0 | (125) | (125) |
| Residual revenues | 120,318 | 123,644 | 3,326 | 12,974 | 16,299 | 3,326 |
| Sales Tax Rebates (all years) | (6) | (5) | 2 | 0 | 2 | 2 |
| Other Subtotal | 1,380,328 | 1,387,821 | 7,493 | 766,978 | 774,472 | 7,493 |
| Other Refunds | 13,009 | 15,728 | 2,719 | 6,333 | 9,052 | 2,719 |
| Other Net | 1,367,319 | 1,372,093 | 4,774 | 760,645 | 765,420 | 4,774 |
| Total Gross | 6,776,236 | 6,740,124 | (36,112) | 2,610,958 | 2,574,846 | (36,112) |
| Total Refunds | 276,949 | 243,587 | (33,362) | 138,750 | 105,388 | (33,362) |
| Total Net | 6,499,287 | 6,496,537 | (2,750) | 2,472,207 | 2,469,458 | (2,750) |