

State Revenues Exceed November Forecast

Minnesota's net general fund receipts totaled \$3.695 billion during the months of November and December of 2015, \$43 million (1.2 percent) more than projected in November 2015's Budget and Economic Forecast. Net receipts from the individual income tax, corporate tax, and other revenues were above forecast, offsetting lower than expected net sales tax receipts. The positive variance for the period was generated in December, as November receipts fell slightly below forecast. (See page 4 for details.)

Summary of Tax Revenues: November – December, 2015

| (\$ in millions) | November 2015 Forecast | Actual | \$ Difference | % Difference |
|-------------------------|---------------------------|----------------|---------------|--------------|
| Individual Income Tax | \$1,687 | \$1,715 | \$28 | 1.6% |
| General Sales Tax | 855 | 841 | (14) | (1.7) |
| Corporate Franchise Tax | 284 | 299 | 14 | 5.1 |
| Other Revenues | 825 | 841 | 16 | 1.9 |
| Total Revenues* | \$3,652 | \$3,695 | \$43 | 1.2% |

* Totals may not add due to rounding.

Net individual income tax receipts during the last two months of 2015 were \$28 million (1.6 percent) above forecast. Gross income tax payments nearly matched the forecast, as estimated tax payments (declarations) in excess of forecast offset lower than expected withholding and miscellaneous payments. Consequently, the positive net income tax variance was due to lower than expected income tax refunds. MMB economists expect the refund variance to dissipate as processing of tax year 2014 returns is completed.

Estimated tax payments were \$32 million ahead of forecast. Even though fourth quarter estimated tax payments are not due until January 15, many taxpayers make early payments on or before December 31 so they can deduct them on their federal returns for the tax year that just ended. Therefore, combining estimated tax receipts for December and January provides a more accurate picture of fourth quarter payments than December alone.

Withholding payments were \$30 million below forecast. This appears to be due to the timing of payments at the end of the calendar year and is expected to resolve in coming weeks.

Gross corporate tax payments in excess of forecast more than offset larger than expected corporate refunds to produce a \$14 million (5.1 percent) variance in net corporate receipts for November and December. A one-time corporate tax payment in December generated all of the positive variance in gross receipts. Without this payment, net corporate receipts would be short of forecast for November and December.

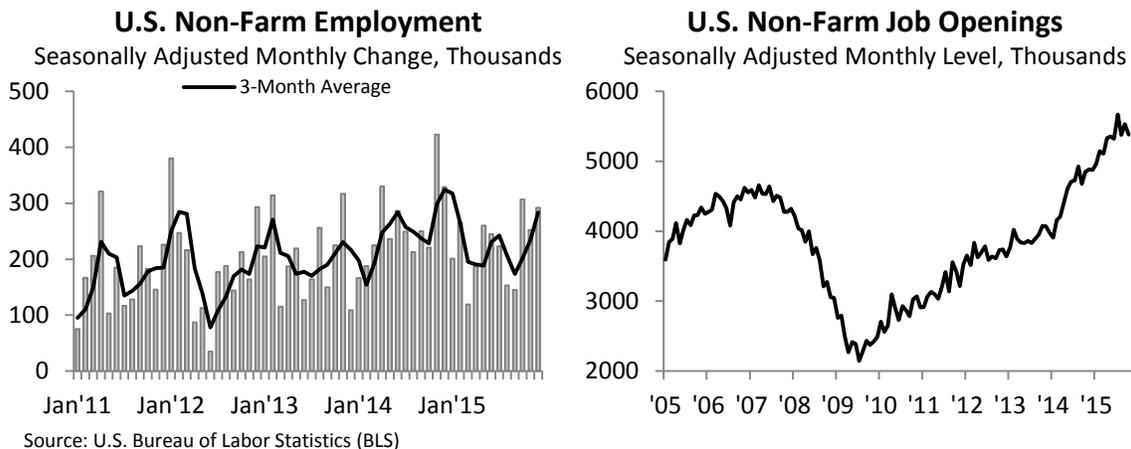
Net sales tax receipts in November and December were \$14 million (1.7 percent) less than forecast. This was due to larger than forecast sales tax refunds. Other revenues exceeded forecast for the period by \$16 million (1.9 percent). The estate tax generated the largest amount of additional revenue in this category, \$9 million.

Federal Reserve Ends Zero-Rate Era; Signals Confidence in U.S. Economy

The Federal Reserve raised short-term interest rates in mid-December for the first time in almost a decade. The widely anticipated action — the central bank lifting its benchmark rate by a quarter of a percentage point — signals the end of an extraordinary seven-year period of record low borrowing rates and reflects confidence in the strength of the U.S. economy. Most Fed officials expect the pace of subsequent rate hikes to be gradual, by about one percentage point each year for the next three years, and dependent on incoming economic data.

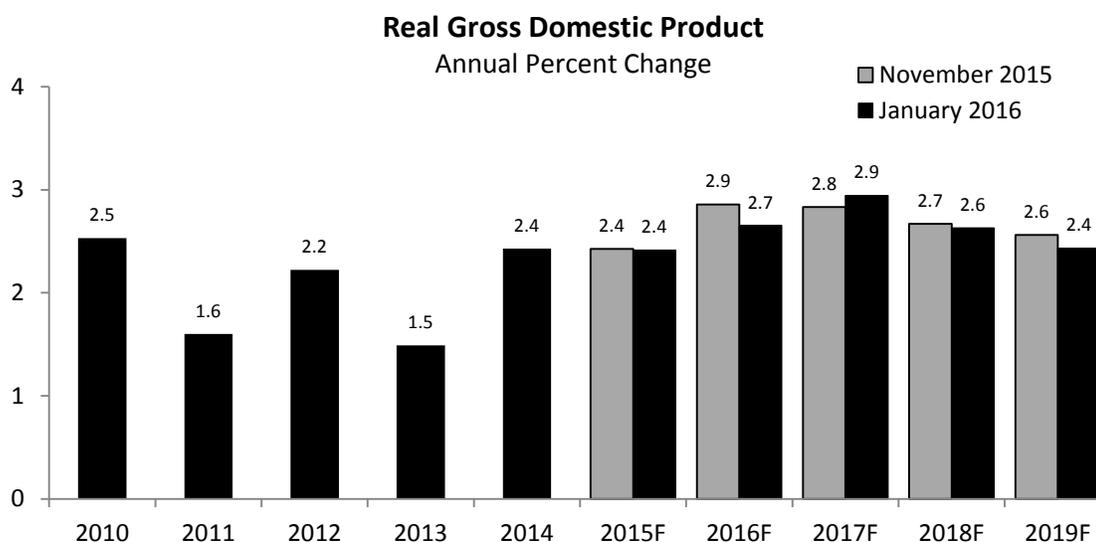
The Fed’s decision to raise its key rate was motivated in part by improving economic activity. Recent data confirm that consumer spending and business investment have been solid, with the exception of capital expenditures by firms exposed to international competition, low oil prices, and falling agriculture prices. Real GDP rose at a 2.0 percent annual rate in the third quarter of 2015, well below the 3.9 percent gain in the second quarter. A sizeable inventory correction and foreign trade were the main drags. If inventories and trade are excluded, real final sales to domestic purchasers rose a solid 2.9 percent, following a similar increase of 3.7 percent in the second quarter.

A range of labor market indicators also show considerable improvement. The U.S. economy added a solid 2.7 million jobs in 2015, about the same gain as in the past two years. Consistently strong job gains have helped quickly absorb the unemployed and underemployed, and push down the U.S. jobless rate to 5.0 percent in December, from 5.7 percent at the start of the year. Perhaps most encouraging is that the number of available jobs



across the country has surged. The ratio of job seekers to open positions is near its lowest value since 2001. Openings are widespread among industries, especially in healthcare and professional services. U.S. layoff announcements are also extraordinarily low.

The Fed’s expectations about the durability of the U.S. economy are consistent with those of IHS Economics (IHS) — Minnesota Management and Budget’s macroeconomic consultant. The IHS January 2016 baseline calls for real GDP growth of 2.4 percent in 2015, followed by 2.7 percent growth in 2016 and 2.9 percent growth in 2017. The November 2015 baseline projected very similar growth of 2.4 percent in 2015, followed by an increase of 2.9 percent growth in 2016 and 2.8 percent in 2017. The IHS January baseline forecast for 2016 and 2017 is at the high end of a range of estimates from the Blue Chip survey of about 50 top business forecasters. The latest Blue Chip Consensus forecast is for 2.5 percent growth in both 2016 and 2017.



Source: U.S. Bureau of Economic Analysis (BEA), IHS Economics (IHS)

Inflation continues to run well below the Federal Reserve’s 2 percent objective, partly reflecting downward pressures from lower energy prices and the prices of non-energy imports — due to the stronger dollar. The January 2016 baseline from IHS expects consumer prices (CPI) to have risen just 0.1 percent in 2015. The November 2015 baseline anticipated flat prices — or 0.0 percent inflation. Even so, the Fed’s statements show that officials are reasonably confident inflation will return to 2 percent over the medium term, as transitory effects dissipate and the labor market strengthens further. IHS agrees. Their January baseline has CPI rising 1.2 percent in 2016 and 2.6 percent in 2017, similar to the 1.4 and 2.7 percent growth IHS expected last November.

There have been no changes in the probabilities assigned to the baseline or alternative forecast scenarios since November. IHS continues to assign a probability of 65 percent to their January 2016 baseline. A more pessimistic scenario in which contractions in international markets and the U.S. construction sector trigger a two-quarter U.S. recession in 2016 is assigned a probability of 20 percent. A more optimistic scenario where higher-than-expected productivity growth, household formation, and foreign growth deliver a boost to the U.S. economy in early 2016 is assigned probability of 15 percent.

Comparison of Actual and Forecast Non-Dedicated Revenues

(\$ in thousands)

| | Fiscal Year-to-Date 2016 | | | November – December 2015 | | |
|-------------------------------------|--------------------------|--------------------|---------------------------|--------------------------|--------------------|---------------------------|
| | (July-December, 2015) | | | | | |
| | FORECAST REVENUES* | ACTUAL REVENUES | DIFFERENCE ACTUAL-FCST | FORECAST REVENUES* | ACTUAL REVENUES | DIFFERENCE ACTUAL-FCST |
| Individual Income Tax | | | | | | |
| Withholding | 3,915,843 | 3,885,370 | (30,474) | 1,420,900 | 1,390,426 | (30,474) |
| Declarations | 757,000 | 789,067 | 32,067 | 281,156 | 313,223 | 32,067 |
| Miscellaneous | 269,734 | 268,480 | (1,254) | 59,400 | 58,146 | (1,254) |
| Gross | 4,942,577 | 4,942,917 | 339 | 1,761,455 | 1,761,795 | 339 |
| Refund | 140,820 | 113,583 | (27,237) | 74,230 | 46,993 | (27,237) |
| Net | 4,801,757 | 4,829,334 | 27,577 | 1,687,225 | 1,714,802 | 27,577 |
| Corporate Franchise Tax | | | | | | |
| Declarations | 617,960 | 612,535 | (5,425) | 260,223 | 254,798 | (5,425) |
| Miscellaneous | 205,898 | 228,553 | 22,655 | 58,231 | 80,885 | 22,655 |
| Gross | 823,858 | 841,088 | 17,230 | 318,453 | 335,683 | 17,230 |
| Refund | 58,059 | 60,901 | 2,843 | 34,288 | 37,131 | 2,843 |
| Net | 765,799 | 780,186 | 14,387 | 284,165 | 298,553 | 14,387 |
| General Sales and Use Tax | | | | | | |
| Gross | 2,648,149 | 2,647,332 | (817) | 894,720 | 893,903 | (817) |
| Mpls. sales tax transferred to MSFA | 861 | 862 | 1 | 312 | 313 | 1 |
| General Sales Tax Gross | 2,649,010 | 2,648,194 | (816) | 895,032 | 894,216 | (816) |
| Refunds (including Indian refunds) | 98,867 | 112,514 | 13,646 | 39,646 | 53,292 | 13,646 |
| Net | 2,550,143 | 2,535,680 | (14,463) | 855,386 | 840,924 | (14,463) |
| Other Revenues: | | | | | | |
| Net Estate Tax | 92,279 | 100,957 | 8,677 | 24,940 | 33,617 | 8,677 |
| Net Liquor/Wine/Beer Taxes | 39,930 | 38,865 | (1,065) | 14,552 | 13,487 | (1,065) |
| Net Cigarette/Tobacco Tax | 291,114 | 295,736 | 4,622 | 127,669 | 132,291 | 4,622 |
| Deed and Mortgage Taxes | 107,548 | 106,787 | (762) | 37,415 | 36,653 | (762) |
| Net Insurance Premiums Taxes | 168,118 | 168,451 | 334 | 82,104 | 82,438 | 334 |
| Lawful Gambling Taxes | 19,295 | 21,945 | 2,650 | 6,121 | 8,771 | 2,650 |
| Health Care Surcharge | 89,570 | 92,270 | 2,699 | 51,758 | 54,458 | 2,699 |
| Other Taxes | 519 | 515 | (3) | 106 | 103 | (3) |
| Statewide Property Tax | 385,204 | 388,433 | 3,229 | 190,772 | 194,001 | 3,229 |
| DHS SOS Collections | 22,181 | 21,409 | (772) | 7,508 | 6,736 | (772) |
| Investment Income | 6,545 | 7,733 | 1,188 | 1,818 | 3,006 | 1,188 |
| Tobacco Settlement | 162,370 | 162,330 | (40) | 162,270 | 162,230 | (40) |
| Dept. Earnings & MSOP Recov. | 96,535 | 98,443 | 1,907 | 44,188 | 46,096 | 1,907 |
| Fines and Surcharges | 32,255 | 37,114 | 4,858 | 11,568 | 16,426 | 4,858 |
| Lottery Revenues | 21,206 | 18,696 | (2,510) | 8,651 | 6,141 | (2,510) |
| Revenues yet to be allocated | 1,297 | 88 | (1,209) | - | (1,209) | (1,209) |
| Residual Revenues | 90,271 | 82,282 | (7,989) | 53,339 | 45,350 | (7,989) |
| County Nursing Home, Pub Hosp IGT | 3,396 | 2,830 | (566) | 1,698 | 1,132 | (566) |
| Other Subtotal | 1,629,634 | 1,644,883 | 15,249 | 826,479 | 841,728 | 15,249 |
| Other Refunds | 2,773 | 2,396 | (377) | 1,600 | 1,223 | (377) |
| Other Net | 1,626,862 | 1,642,488 | 15,626 | 824,879 | 840,505 | 15,626 |
| Total Gross | 10,045,080 | 10,077,082 | 32,002 | 3,801,420 | 3,833,422 | 32,002 |
| Total Refunds | 300,519 | 289,394 | (11,125) | 149,764 | 138,639 | (11,125) |
| Total Net | 9,744,561 | 9,787,688 | 43,127 | 3,651,656 | 3,694,783 | 43,127 |

* November 2015 Budget & Economic Forecast.