July 2009 Economic Update

MINNESOTA Management & Budget

July 2009

FY2009 Revenues $150 Million Below Forecast

Minnesota's net general fund revenues for FY 2009 are now estimated to total $14.843 billion, $150 million (1.0 percent) less than February's forecast. Individual income tax receipts were the primary source of the shortfall, down $232 million (3.2 percent) from forecast. Receipts from the corporate income tax, the motor vehicle sales tax, and other taxes and revenues exceeded projections by a combined $98 million. This revenue shortfall reduces the balance carried forward to the 2010-11 biennium.

Summary of Revenues: (Fiscal Year 2009)

	Estimate	Actual	Variance	Percent
	-----------------	($ in millions)	------------------	
Income	$7,244	$7,012	$(232)	(3.2)
Sales	4,394	4,378	(16)	(0.4)
Corporate	657	710	53	8.1
Motor Vehicles	107	116	9	8.4
Other	2,591	2,627	36	1.4
Total	$14,993	$14,843	$(150)	(1.0)

All parts of Minnesota's individual income tax underperformed February's forecast. Withholding tax receipts were $108 million (1.8 percent) less than anticipated and individual estimated payments, excluding extension payments, $100 million below forecast. Combined tax year 2008 settle-up payments, extension payments, and refunds fell short of projections by $24 million. While some of the lost withholding revenue appears to reflect smaller than anticipated bonus payments made in early 2009, withholding receipts in April, May, and June averaged more than $20 million per month below projections, consistent with weaker wage and employment growth than anticipated in February's forecast.

The negative variance for gross sales tax receipts observed earlier this year has been reduced, but not eliminated in the last three months. Taxes paid on sales in April, May, and June totaled $10 million more than projected, reducing the shortfall in gross sales tax receipts to $10 million. Sales tax refunds were $6 million more than forecast due to changes in year-end accounting procedures.

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All FY 2009 results are preliminary and subject to change. As in past years forecasts for some revenue sources were adjusted to reflect anticipated accruals in this first report of receipts for the entire fiscal year. Individual income tax refunds paid in FY 2009 could change materially before closing due to processing of amended returns filed by individuals victimized by Ponzi schemes. A complete accounting of FY 2009 revenues reflecting final closing will be published in the October *Economic Update*.

Real GDP Growth Expected by Fall …. But Job Losses Continue until Spring 2010

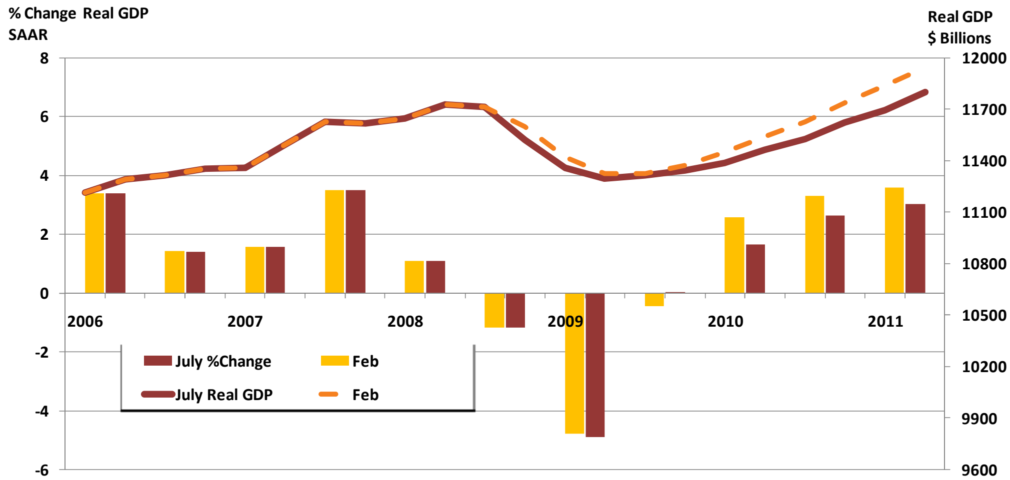
The past year has been a difficult one for the U.S. economy. Real GDP has fallen by an estimated 3.7 percent and we have lost nearly 6.5 million jobs. The unemployment rate is now at 9.5 percent, the average workweek for production and supervisory workers has fallen to the lowest level since the data were first collected in 1964, and average weekly earnings have grown by less than one percent over the past 12 months. We are in the longest recession since the great depression, and while most expect real GDP growth to return by fall, this recession is also likely to be the deepest in the postwar period. In recent months analysts have been searching so hard for signs of an economic turnaround that data which in normal times would signify major economic problems (such as May's loss of more than 300,000 jobs) have been welcomed by some pundits as "green shoots" heralding an approaching recovery.

Most forecasters expect that the tax cuts and spending increases provided in the federal stimulus package, combined with an end to inventory draw downs and modest increases in auto production will lift real output into positive territory this fall. But, most also have reduced their mid-year projections considerably from forecasts made at the start of this year. For example, February's Blue Chip consensus called for real GDP to fall by 1.9 percent in 2009; the July consensus forecast expects a 2009 decline of 2.6 percent. Almost all forecasts show job losses and unemployment rate increases extending well into 2010.

Global Insight (GII), Minnesota's national macroeconomic consultant, has grown modestly more optimistic in recent months, but their July baseline still shows a weaker economy through the end of the 2010-11 biennium than they forecast in February. GII now calls for real GDP to drop by 1.6 percent in fiscal 2009, and by 0.8 percent in fiscal 2010. In fiscal 2011 growth at a 2.5 percent annual rate is anticipated. February's baseline projected real GDP declines of 1.2 percent and 0.8 percent in fiscal 2009 and fiscal 2010, followed by 3.2 percent growth in fiscal 2011.

Oil is expected to remain in the $60 to $70 per barrel range through early 2011. Those higher than previously projected prices produce only a small change in projected inflation. CPI increases of 0.4 percent and 2.2 percent are forecast for fiscal 2010 and fiscal 2011. February's baseline called for a CPI decline of 0.7 percent followed by an increase of 2.3 percent.

Weaker Outlook for 2010-11 Biennium



Global Insight assigns a probability of 60 percent to their July baseline forecast. A more optimistic scenario, in which the economy rebounds more rapidly from its current lows is assigned a probability of 20 percent as is a scenario in which the economy's downward spiral does not end until the spring of 2010.

Economic Data Show U.S. Economy Weaker than Minnesota's in 2008

Minnesota has lagged slightly behind the U.S. economy in per capita GDP and per capita personal income growth since 2005. Employment also has grown more slowly in Minnesota and our unemployment rate appears to have shifted from its historical pattern of being well below the U.S. rate to a new pattern more closely tied to the national rate. Per capita personal income in Minnesota was more than 9 percent above the U.S. average in 2003 and 2004. In 2005 and 2006, per capita personal income grew much more slowly than the U.S. average, and the state average fell to 5.8 percent above the U.S. In 2006 per capita GDP fell by 0.3 percent while the U.S. average grew 1.8 percent. Even though Minnesota's subpar economic performance extended for just three years, there has been concern that the state's recent performance might be an early warning of longer term problems.

Economic conditions were far from normal in both Minnesota and nationally in 2008. But, according to preliminary data released by the U.S. Department of Commerce, Minnesota grew faster than the U.S. averages in both per capita GDP and per capita personal income. Last year real GDP per capita in Minnesota grew by 1.25 percent, the best since 2004. Nationally, real GDP per capita fell by 0.2 percent. And, per capita personal income grew by 4.1 percent in Minnesota, considerably stronger than the 2.9 percent growth observed nationally. Minnesota's per capita personal income is now 7.6 percent above the national average. The relative improvement also carried forward to the employment statistics. When compared to the end of 2007 employment in Minnesota fell by 2.0 percent by the end of 2008. Nationally, payroll employment fell by 2.2 percent.

Comparison of Actual and Estimated Non-Restricted Revenues

($ in thousands)

	F2009 Fiscal Year-to-Date			April - June 2009		
	FORECAST REVENUES	ACTUAL REVENUES	VARIANCE ACT-FCST	FORECAST REVENUES	ACTUAL REVENUES	VARIANCE ACT-FCST
Individual Income Tax						
Withholding	6,105,900	5,998,087	(107,813)	1,464,200	1,401,038	(63,162)
Declarations	1,441,700	1,359,180	(82,521)	597,800	517,635	(80,165)
Miscellaneous	903,220	941,170	37,950	712,143	750,094	37,950
Gross	8,450,820	8,298,436	(152,384)	2,774,143	2,668,767	(105,377)
Refund	1,207,600	1,286,825	79,225	1,009,686	1,088,911	79,225
Net	7,243,220	7,011,612	(231,608)	1,764,457	1,579,856	(184,601)
Corporate & Bank Excise						
Declarations	731,125	751,050	19,925	139,290	163,655	24,364
Miscellaneous	167,860	176,925	9,065	(2,674)	9,840	12,514
Gross	898,985	927,975	28,990	136,617	173,494	36,878
Refund	241,600	217,549	(24,051)	33,634	21,808	(11,826)
Net	657,385	710,426	53,041	102,983	151,686	48,703
Sales Tax						
Gross	4,640,799	4,630,803	(9,996)	1,300,867	1,310,625	9,757
Refunds	246,199	252,425	6,226	63,465	64,921	1,456
Net	4,394,601	4,378,378	(16,223)	1,237,403	1,245,704	8,301
Motor Vehicle Sales Tax	107,336	116,170	8,834	27,165	32,654	5,489
Other Revenues:						
Estate	121,000	135,945	14,945	23,411	33,124	9,714
Liquor/Wine/Beer	75,477	76,068	591	23,694	25,082	1,388
Cigarette/Tobacco/Cont Sub	187,160	180,000	(7,160)	27,153	26,434	(720)
Deed and Mortgage	158,600	160,855	2,254	53,648	55,709	2,061
Insurance Gross Earnings	275,800	285,508	9,708	53,343	64,768	11,425
Lawful Gambling	44,090	43,659	(430)	15,096	15,521	425
Health Care Surcharge	214,976	219,337	4,361	56,877	49,343	(7,534)
Other Taxes	9,738	24,122	14,384	8,841	23,570	14,729
Statewide Property Tax	742,263	728,425	(13,838)	408,631	394,688	(13,943)
DHS SOS Collections	40,460	40,212	(248)	12,527	10,681	(1,846)
Income Tax Reciprocity	75,880	75,880	0	0	0	0
Investment Income	28,000	40,183	12,183	(862)	5,585	6,447
Tobacco Settlement	176,982	179,854	2,872	0	2,872	2,872
Departmental Earnings	248,182	243,320	(4,862)	43,971	41,602	(2,370)
Fines and Surcharges	93,461	91,003	(2,458)	30,635	29,281	(1,354)
Lottery Revenues	45,773	44,869	(904)	12,304	12,279	(25)
Revenues yet to be allocated	(0)	43	43	(1,116)	(965)	151
Residual Revenues	96,036	110,815	14,779	23,892	27,642	3,750
Sales Tax Rebates (all years)		0	0	0	0	0
County Nursing Home, Pub Hosp	5,610	5,610	0	516	516	0
Other Subtotal	2,639,489	2,685,708	46,219	792,560	817,732	25,172
Other Refunds	48,325	58,934	10,609	17,825	25,228	7,404
Other Net	2,591,164	2,626,774	35,610	774,735	792,503	17,768
Total Gross	**16,737,429**	**16,659,092**	**(78,337)**	**5,031,353**	**5,003,271**	**(28,082)**
Total Refunds	**1,743,724**	**1,815,732**	**72,009**	**1,124,610**	**1,200,868**	**76,259**
Total Net	**14,993,705**	**14,843,359**	**(150,346)**	**3,906,743**	**3,802,403**	**(104,340)**