

July 2013

**FY 2013 Revenues Exceed Forecast by \$463 Million;
Closing Balance will be Allocated to School Shift Buy Back**

Minnesota's net general fund receipts for FY 2013 are now estimated to total \$17.927 billion, \$463 million (2.7 percent) more than February's forecast. State revenues for the final quarter of FY 2013 were \$318 million more than forecast. (See page 4) Both individual and corporate income tax receipts exceeded forecast in fiscal 2013, while sales tax receipts fell below projections. Other tax and non-tax revenues were also above forecast. About 70 percent of the fiscal 2013 forecast variance was from the individual income tax. General fund revenues in fiscal 2013 are now estimated to be 9.2 percent greater than in fiscal 2012.

Summary of Non-Dedicated Revenues

Preliminary

(Fiscal Year 2013)

	<u>Estimate</u>	<u>Actual</u>	<u>Variance</u>	<u>Percent</u>
	----- (\$ in millions) -----			
Income	\$8,622	\$8,957	\$335	3.9
Sales Tax	4,833	4,800	(33)	(0.7)
Corporate	1,237	1,361	124	10.0
Other	<u>2,772</u>	<u>2,809</u>	<u>37</u>	<u>1.3</u>
Total	\$17,464	\$17,927	\$463	2.7

Actions taken in the 2013 Legislative session require that Minnesota Management and Budget estimate the FY 2013 closing balance by September 30, 2013. The entire closing balance, which includes both final revenue and expenditure variances, is then to be used to reduce the \$874 million in school shifts currently outstanding. Before the action by the 2013 Legislature any school shift buy back would not have occurred until after November's official budget forecast and been based on the projected ending balance for the 2014-15 biennium.

More than one-half of the \$335 million individual income tax variance appears to come from higher than anticipated tax year 2012 liability. Payments accompanying extensions were \$136 million more than projected and tax year 2012 individual income tax refunds, \$60 million less than anticipated. Stronger than expected economic growth in late 2012 likely explains some of the additional 2012 liability. But, much of the observed increase is believed to be attributable to high income taxpayers choosing to move even more income into 2012 than was projected in February's forecast.

The income shift into 2012 was triggered by the anticipation of higher federal income tax rates on the earnings and capital gains of upper income taxpayers. Moving income from future years into 2012 to benefit from lower tax rates does not produce a permanent gain for state revenues. Other things equal the acceleration produces one-time, additional state income tax revenue in fiscal 2013, followed by offsetting reductions in later years. Withholding through June was \$90 million (1.3 percent) above forecast. Individual estimated payments for the month of June were \$47 million (21 percent) more than projected.

Gross sales tax receipts ended fiscal 2013 \$52 million (1.0 percent) below forecast. Some of that gap may be timing related, since June payments were the source of much of the shortfall. Lower than projected sales tax refunds partially offset the lower sales tax revenues leaving net sales tax receipts \$33 million below forecast. Corporate tax receipts, buoyed by generally strong corporate profits exceeded forecast by \$124 million or 10.0 percent. The insurance gross premiums tax, the estate tax, and departmental earnings were the sources of much of the positive variance in other tax and fee revenues.

All FY 2013 results are preliminary and subject to change. As in past years the forecast for some revenue sources have been adjusted to reflect anticipated accruals. A complete reporting of FY 2013 revenues will be part of October's *Economic Update*. The next official forecast will be released in December, 2013.

Economic Outlook for FY 2014-15 Is Much the Same as in February

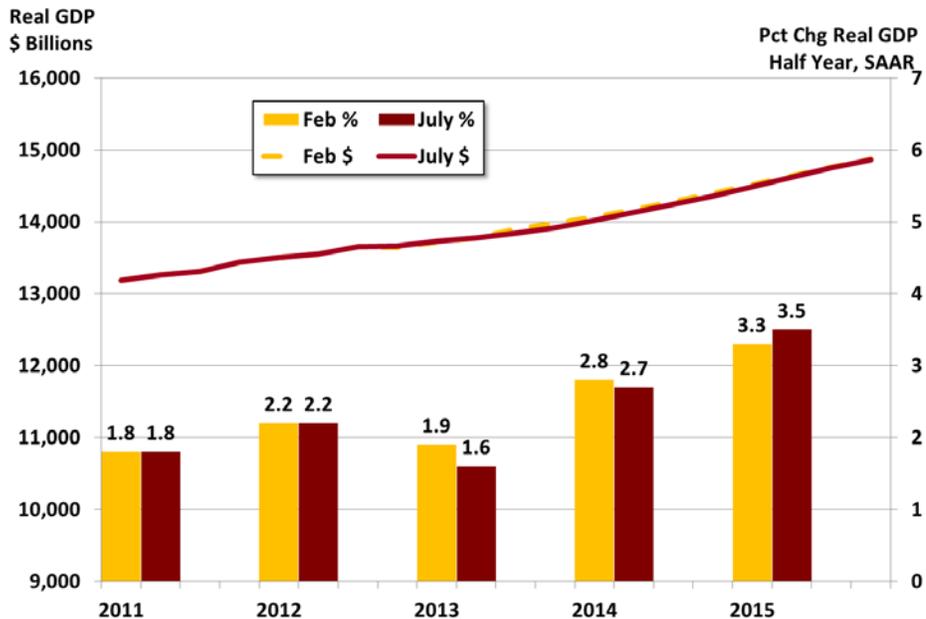
The U.S. economy continues to struggle to break out from the slow growth path it has been on since the end of the Great Recession. Signs of strength are certainly evident in recent months. Employment reports show good job growth, with job increases averaging nearly 200,000 per month during the past three months. Housing is rebounding from its 5 year crash. The auto industry continues its recovery with light vehicle sales in 2013 now projected to be the highest since the slump in 2008. And, consumer sentiment is back in its normal range after more than five years of recession-like readings. But, real GDP growth continues to be disappointing. Real growth in the first quarter is now reported to have been at a sluggish 1.8 percent rate, and economists expect the second quarter growth rate to be well below the 2.5 to 3.0 percent range generally considered to be sustainable for the U.S. economy over the long term. Most forecasters expect that slow growth pattern to continue through the second half of 2013 as the fallout from federal fiscal policy decisions made in late 2012 restrains economic activity. January's payroll tax increase and the federal spending reductions required by the sequester are generally believed to be reducing real GDP growth in 2013 by about one percent. The short-term (12 to 18 month) outlook is further clouded by ambiguities surrounding future actions by the Federal Reserve, particularly when it will begin tapering its bond purchasing program and the impact that tapering will have on the U.S. and global economies.

Global Insight Inc. (GII), Minnesota's macro-economic consultant, is only slightly less optimistic about the short term outlook than they were in February, modestly lowering their outlook for 2013 and 2014. The GII July baseline now calls for real GDP growth rates of 1.6 percent in 2013 and 2.7 percent in 2014. In February growth rates of 1.9 percent and 2.8 percent were projected. Differences between the GII baseline and the Blue Chip Consensus

are small. For 2013 the Blue Chip panel expects real growth of 1.8 percent; for 2014 a 2.7 percent growth rate is projected. Both GII and the Blue Chip panel see no problems from inflation. Global Insight’s July baseline calls for CPI growth to remain below two percent through 2018.

Global Insight assigns a probability of 65 percent to their July baseline scenario. In February the baseline was given a 60 percent probability. A more pessimistic scenario in which the economy barely avoids a recession in 2014 is given a probability of 20 percent, while a more optimistic scenario is given a probability of 15 percent. In February both alternatives were set at 20 percent.

Little Change in Economic Outlook



Comparison of Actual and Estimated Non-Restricted Revenues

(\$ in thousands)

	2013 Fiscal Year-to-Date			April - June 2013 – FY 2013		
	FORECAST REVENUES	ACTUAL REVENUES	VARIANCE ACT-FCST	FORECAST REVENUES	ACTUAL REVENUES	VARIANCE ACT-FCST
Individual Income Tax						
Withholding	6,937,500	7,027,433	89,934	1,663,559	1,695,178	31,618
Declarations	1,633,080	1,799,718	166,638	712,000	879,595	167,595
Miscellaneous	1,305,721	1,323,623	17,902	1,113,613	1,131,515	17,902
Gross	9,876,300	10,150,774	274,474	3,489,172	3,706,288	217,116
Refund	1,254,400	1,193,971	(60,429)	1,156,213	1,095,784	(60,429)
Net	8,621,900	8,956,803	334,903	2,332,960	2,610,504	277,545
Corporate & Bank Excise						
Declarations	1,101,910	1,197,609	95,699	267,001	348,018	81,017
Miscellaneous	303,140	318,744	15,604	71,241	59,449	(11,792)
Gross	1,405,050	1,516,352	111,302	338,242	407,466	69,225
Refund	168,449	155,678	(12,772)	28,740	21,270	(7,470)
Net	1,236,600	1,360,675	124,074	309,501	386,197	76,695
Sales Tax						
Gross	5,068,901	5,017,200	(51,701)	1,511,344	1,454,468	(56,876)
Refunds	236,122	217,496	(18,627)	51,385	49,140	(2,245)
Net	4,832,778	4,799,704	(33,074)	1,459,959	1,405,328	(54,631)
Other Revenues:						
Estate	156,000	167,461	11,461	35,773	45,243	9,471
Liquor/Wine/Beer	84,630	83,248	(1,382)	25,424	24,731	(693)
Cigarette/Tobacco/Cont Sub	191,060	189,060	(2,000)	47,879	37,515	(10,364)
Deed and Mortgage	204,900	215,515	10,615	60,099	68,419	8,321
Insurance Gross Earnings	304,900	332,808	27,908	69,500	77,402	7,902
Lawful Gambling	42,800	38,908	(3,892)	17,391	14,537	(2,853)
Health Care Surcharge	230,850	225,009	(5,841)	65,194	62,881	(2,314)
Other Taxes	19,418	22,988	3,570	18,431	22,005	3,574
Statewide Property Tax	816,701	809,768	(6,933)	436,391	429,435	(6,957)
DHS SOS Collections	47,900	51,326	3,427	9,536	11,602	2,066
Income Tax Reciprocity	0	0	0	0	0	0
Investment Income	3,600	3,044	(556)	647	(384)	(1,030)
Tobacco Settlement	165,144	170,060	4,917	0	4,916	4,916
Departmental Earnings	247,899	267,954	20,055	41,275	65,450	24,175
Fines and Surcharges	78,131	80,737	2,606	24,932	29,268	4,336
Lottery Revenues	51,854	55,081	3,227	13,043	16,605	3,562
Revenues yet to be allocated	0	805	805	291	392	101
Residual Revenues	178,608	164,851	(13,757)	32,895	16,147	(16,748)
County Nursing Home, Pub Hosp IGT	6,792	6,226	(566)	2,264	1,698	(566)
Other Subtotal	2,831,186	2,884,849	53,663	900,964	927,865	26,901
Other Refunds	59,258	75,404	16,146	14,463	22,933	8,470
Other Net	2,771,928	2,809,445	37,517	886,502	904,932	18,431
Total Gross	19,181,437	19,569,176	387,738	6,239,722	6,496,087	256,365
Total Refunds	1,718,230	1,642,549	(75,681)	1,250,801	1,189,126	(61,675)
Total Net	17,463,207	17,926,627	463,420	4,988,921	5,306,961	318,039