



Minnesota

Department of Finance

October 2001

State Revenues \$99 Million Below Forecast in First Three Months of Biennium

Net general fund revenues totaled \$2.726 billion during the first quarter of FY 2002, \$99 million (3.5 percent) less than end-of-session estimates. Receipts from the individual income tax, the sales tax, and the corporate income tax all were less than forecast. The motor vehicle sales tax and other taxes and receipts were above end-of-session estimates. September 11th's events had almost no impact on these revenue variances. Since tax payments lag the taxable transactions, these collections largely reflect economic activity in July and August. The first data on Minnesota tax revenues, post September 11th, will not be available until early November.

Summary of Tax Receipts: (July - September 2001)

	Forecast	Actual	Variance	Percent
	-----(\$ in millions)-----			
Income	1,433	1,363	(70)	(4.9)
Sales	855	836	(19)	(2.2)
Corporate	197	150	(47)	(23.9)
Motor Vehicles	92	103	11	12.0
Other	<u>248</u>	<u>274</u>	<u>26</u>	<u>10.5</u>
TOTAL	2,825	2,726	(99)	(3.5)

Individual income tax receipts were \$70 million (4.9 percent) below forecast. Estimated tax payments and withholding tax receipts were \$29 million and \$37 million below expected levels (see page 4). Net corporate income tax receipts were nearly 24 percent less than forecast reflecting the substantial weakening in corporate profits which has been reported in recent months. Since some corporate estimated payments appear to have been co-mingled with final payments in September, only the combined variance is meaningful.

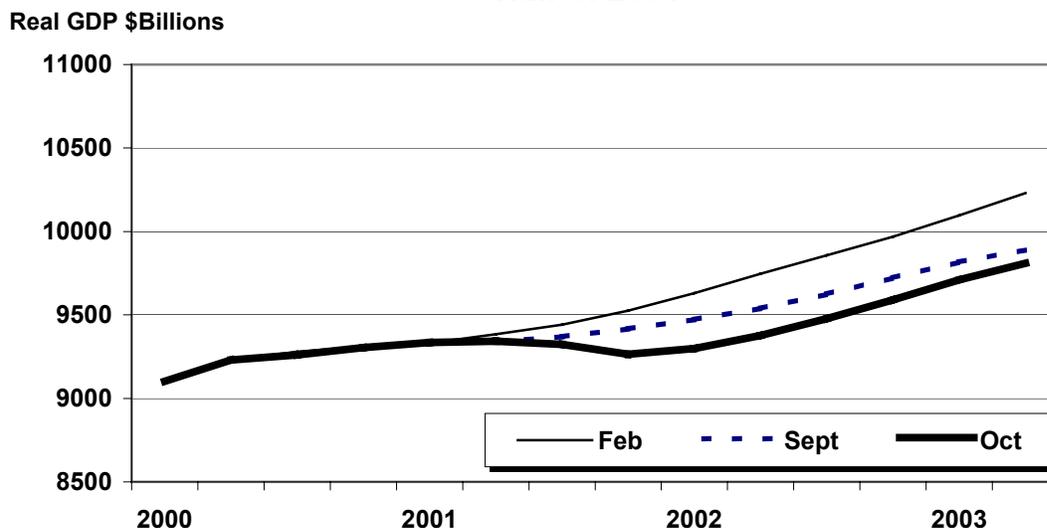
Net sales tax receipts in Minnesota were off just \$19 million in July, August, and September, and gross sales tax receipts (excluding sales tax refunds) were down by just \$12 million. Motor vehicle sales tax collections were \$11 million above forecast, reflecting the continued strength in auto sales. Continued strong housing sales and refinancing boosted mortgage and deed tax receipts by nearly \$12 million, accounting for about one half of the \$26 million positive variance in other revenues.

The Longest Economic Expansion in U.S. History Has Come to an End

The U.S. economy was weak in August, teetering on the edge of recession. Although economists believed a recession could be avoided, few believed the economy could withstand a major shock. Help was on the way from the Federal Reserve's interest rate cuts and the federal tax rebate, but there was widespread concern that consumer spending might weaken before that monetary and fiscal stimulus could take hold. September's employment report, which showed that U.S. payrolls fell by 199,000 in the month prior to the terrorist attacks, and early September's drop in consumer sentiment, confirmed the legitimacy of the pre-September 11th concerns.

Now, one month after the terrorist attacks, nearly all forecasters believe a recession is underway. The consensus expects consumer spending and economic growth to rebound in early 2002, but a sizeable minority believes the downturn could continue for one or two additional quarters. Ultimately, the severity of this downturn will depend on how quickly consumer confidence recovers. Here historical data offers little guidance since there has been nothing comparable to September's events. October's Control forecast from DRI-WEFA, Minnesota's national economic consultant, is the consensus outlook, calling for a relatively shallow, two-quarter recession in 2001. The economy begins to grow again in early 2002. DRI expects consumer confidence to rebound quickly over the next few months, and they anticipate that the proposed federal stimulus package will provide a substantial economic boost in early 2002.

A Two Quarter Recession Is Now Forecast for the Second Half of 2001



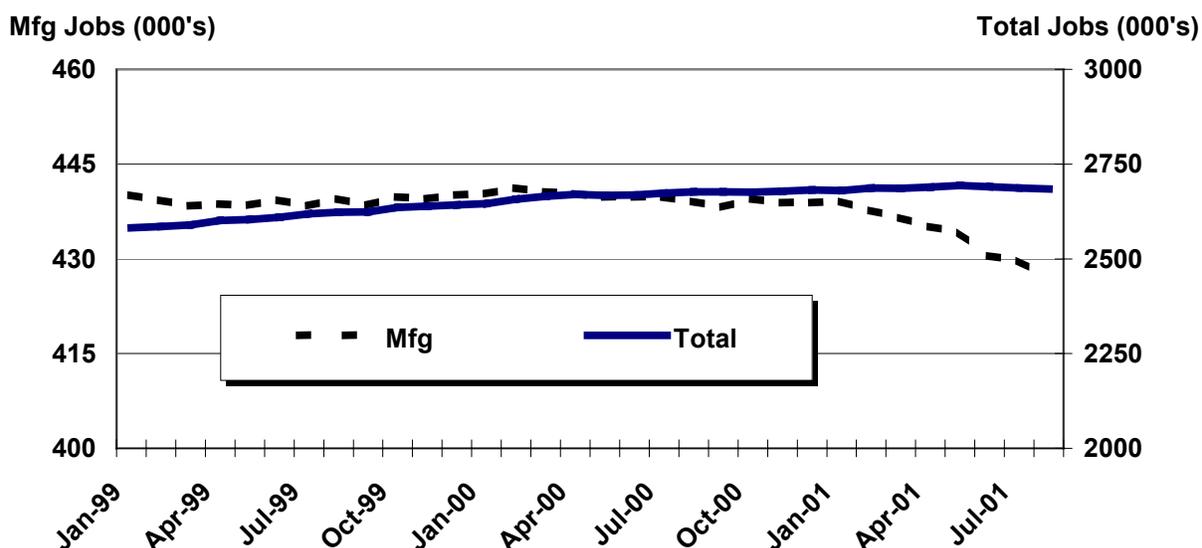
Not all of the change in the forecast since February was caused by the terrorist attack. Even in early summer, DRI's February Control was looking too optimistic. Their September Control, issued prior to September 11, projected real GDP growth rates for each year of the next biennium which were more than 1.3 percentage points lower than those used in February's revenue forecast. October's Control is even more pessimistic, calling for no growth in real GDP in

FY 2002 and 3.6 percent growth in FY 2003. In February, real growth rates of 2.8 percent and 4.7 percent were anticipated. DRI-WEFA assigns a 50 percent probability to the Control forecast. A 40 percent probability is assigned to a scenario containing a four-quarter recession. DRI assigns a 10 percent probability to a scenario in which a recession is avoided.

Minnesota Payroll Employment Declined in August

The weakness in the U.S. economy prior to September’s terrorist attacks was also visible in Minnesota. Seasonally adjusted payroll employment in Minnesota is up by less than 4,000 jobs since January, and manufacturing employment has fallen below January’s levels. Minnesota’s unemployment rate continues to remain well below the national average, but at 3.6 percent seasonally adjusted, it is now a full 0.6 percentage points above January’s 3.0 percent rate.

Minnesota Manufacturing Employment Has Fallen by 12,000 Jobs Since January



Minnesota employment reached its peak for this cycle on a seasonally adjusted basis in May. Since then, payrolls have fallen by more than 9,000. Seasonally adjusted state employment data indicates that 2,700 manufacturing jobs were lost in August alone, and in that month Minnesota payroll employment fell by a total of 3,200.

Comparison of Actual and Estimated Non-Restricted Revenues
July - September 2001
(\$ in thousands)

<u>Four Major Revenues:</u>	<u>Forecast</u>	<u>Actual</u>	<u>Variance</u>
	<u>Revenues</u>	<u>Revenues</u>	<u>Act-Fcst</u>
Individual Income Tax			
Withholding	1,173,200	1,135,834	(37,366)
Declarations	249,412	219,934	(29,478)
Miscellaneous	40,000	42,970	2,970
Gross	1,462,612	1,398,738	(63,874)
Refunds	30,065	35,939	5,874
Net	1,432,547	1,362,799	(69,748)
Corporate & Bank Excise			
Declarations	183,500	98,164	(85,336)
Miscellaneous	23,500	64,457	40,957
Gross	207,000	162,622	(44,378)
Refunds	9,600	11,765	2,165
Net	197,400	150,857	(46,543)
Sales Tax			
Gross	904,529	892,467	(12,062)
Refunds	49,648	56,868	7,220
Net	854,881	835,599	(19,283)
Motor Vehicle Sales			
	91,887	102,723	10,836
<u>Other Revenues:</u>			
Inherit/Gift/Estate	23,140	13,010	(10,130)
Liquor/Wine/Beer	11,776	11,789	13
Cigarette/Tobacco/Cont. Sub.	38,331	40,014	1,683
Deed and Mortgage	42,164	53,792	11,628
Insurance Gross Earnings	2,190	2,567	377
Lawful Gambling	13,865	12,176	(1,689)
Health Care Surcharge	29,190	29,799	609
Other Taxes	1,250	287	(963)
DHS RTC Collections	12,782	12,511	(271)
Income Tax Reciprocity	0	0	0
Investment Income	18,747	24,399	5,652
Tobacco Settlement	0	0	0
1999 Sales Tax Rebates	0	0	0
2000 Sales Tax Rebates	0	(32)	(32)
2001 Sales Tax Rebates	0	9,944	9,944
Other and Unallocated	58,182	68,912	10,729
Other Subtotal	251,616	279,168	27,552
Other Refunds	3,265	5,348	2,083
Other Net	248,351	273,820	25,469
Total Gross	2,917,645	2,835,717	(81,928)
Total Refunds	92,578	109,920	17,342
Total Net	2,825,067	2,725,797	(99,270)