

October 2015

State Revenues above February Forecast for First Quarter of Fiscal Year 2016

Minnesota's net general fund receipts totaled \$4.428 billion during the months of July through September 2015, or \$136 million (3.2 percent) more than projected in the February 2015 *Budget and Economic Forecast* adjusted for legislative changes. Receipts from all major tax types exceeded the forecast. The positive variance for the quarter was generated in July and August, as September receipts fell slightly below forecast.

Summary of Tax Revenues: July – September, 2015

(\$ in millions)	February 2015 Forecast ¹	Actual	\$ Difference	% Difference
Individual Income Tax	\$2,288	\$2,341	\$52	2.3%
General Sales Tax	1,181	1,214	32	2.7
Corporate Franchise Tax	395	436	42	10.6
Other Revenues	427	437	10	2.3
Total Revenues²	\$4,291	\$4,428	\$136	3.2%

1. February 2015 *Budget and Economic Forecast* adjusted for legislative changes.

2. Totals may not add due to rounding.

About half of the \$52 million (2.3 percent) net individual income tax variance was due to higher than expected withholding payments. (See page 4 for details.) MMB economists attribute the withholding variance to the timing of receipts and expect it to dissipate over the next quarter. Larger than anticipated estimated tax payments (declarations) and payments with final returns added to the positive net income tax variance.

Net sales tax receipts were \$32 million (2.7 percent) above the forecast, driven by higher than expected gross sales tax payments. Some of the higher gross receipts may be due to uncertainty about the effect of a major sales tax law change taking effect in August. However it appears that most of the sales tax variance is due to stronger than forecast taxable sales.

Net corporate tax receipts exceeded the forecast by \$42 million (10.6 percent). One-time settle-up payments in August generated this positive variance, as net corporate receipts in July and September nearly matched the forecast.

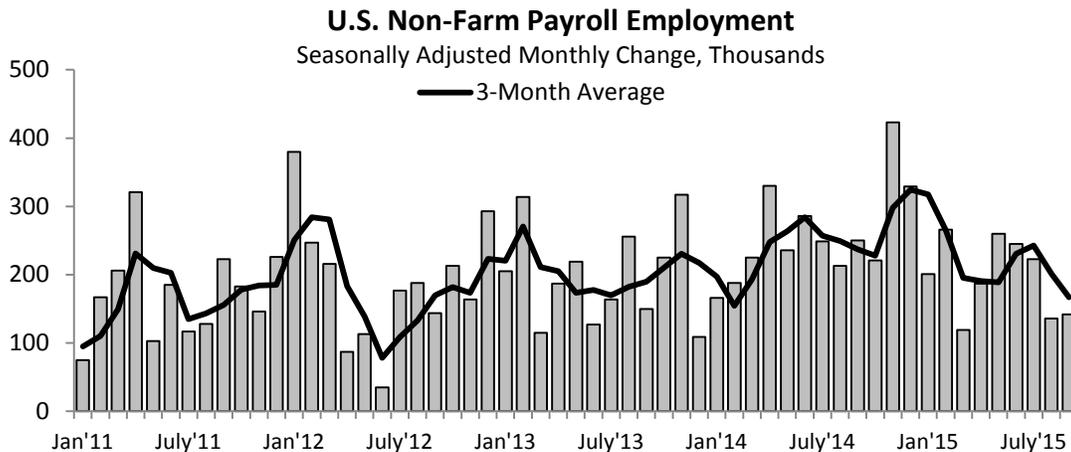
Fiscal Year 2015 Revenues End \$531 Million above February Forecast

Net general fund revenues for the fiscal year that ended June 30, 2015, are now \$531 million more than forecast in February, producing a variance that is \$24 million less than the \$555 million originally reported in the July 2015 *Revenue and Economic Update*. The decrease in the fiscal year 2015 revenue variance is due to higher than expected individual income and sales tax refunds paid out between the end of the fiscal year and the official close. Those changes are partially offset by lower than expected corporate refunds paid prior to the fiscal year close.

U.S. Economy Keeps Chugging Along

The U.S. economy continues to perform well. The unemployment rate is trending downward toward 5 percent, low gasoline prices are affording consumers extra spending money, and home and vehicle sales ratcheted up earlier this summer. The Bureau of Economic Analysis (BEA) estimates that real GDP grew at an annual rate of 3.9 percent in the second quarter of 2015, up from 0.6 percent growth in the first quarter. Broad-based consumer spending across all major categories was the main driver of growth. Foreign trade provided a modest positive contribution, after being a substantial drag the previous two quarters.

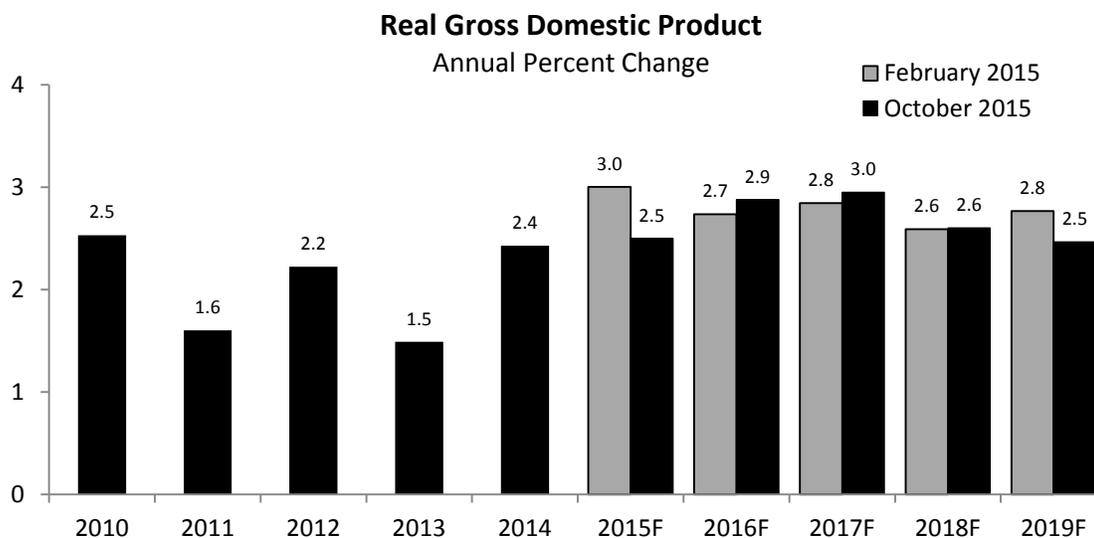
Still, there are concerns. The stronger dollar and weak global demand have been undercutting net exports, which combined with an inventory correction in the third quarter is taking a toll on U.S. manufacturing. U.S. wage growth remains stubbornly low, and recent financial market volatility is weighing on confidence. The Federal Reserve noted these risks in September when it decided to hold off on beginning to normalize interest rates. Finally, job growth unexpectedly downshifted during the past two months.



Source: U.S. Bureau of Labor Statistics. (BLS)

Nonetheless, the evident strength of final domestic demand, and of consumers in particular, supports the case for sustained economic growth in the second half of 2015. MMB’s macroeconomic consultant IHS Economics (IHS) sees annualized real GDP growth of about 2.6 percent for the remainder of the year, as strong gains in consumer spending offset higher imports and an inventory deceleration that is expected to be a drag on growth in the third and fourth quarters.

Continued improvement in U.S. economic growth is expected through at least 2016, with modest gains in labor supply and productivity. The October 2015 baseline from IHS now calls for real GDP growth of 2.5 percent in 2015, followed by 2.9 percent growth in 2016 and 3.0 percent growth in 2017. The February 2015 baseline projected stronger growth this year of 3.0 percent, followed by 2.7 percent in 2016 and 2.8 percent in 2017. The IHS October baseline forecast is very similar to the Blue Chip Consensus, the median of 50 business and academic forecasts. The Blue Chip forecast is for 2.5 percent growth in 2015, followed by an increase of 2.7 percent in 2016.



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

Inflation is following an expected lower path this year, as lower-priced gasoline, industrial commodities, and imported consumer goods have put further downward pressure on already low inflation. The IHS October 2015 baseline anticipates consumer prices (CPI) in 2015 to be flat—or 0.0 percent inflation. The February 2015 baseline projected a decline of 0.7 percent in 2015. Even so, IHS continues to believe downward inflation pressures are transitory and will correct in the near-term. Thus inflation is expected to gradually move higher. The October baseline has CPI rising 1.8 percent in 2016, similar to the 2.3 percent growth expected last February.

IHS assigns a probability of 65 percent to the October baseline forecast. A more pessimistic scenario in which the recent panic in global equity markets turns out to be more than just financial contagion is assigned a probability of 20 percent. A more optimistic scenario where higher-than-expected household formation, productivity, 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-Restricted Revenues

(\$ in thousands)

	Fiscal Year-to-Date 2016 (July-September, 2015)			Fiscal Year 2015 Close		
	FORECAST REVENUES*	ACTUAL REVENUES	DIFFERENCE ACTUAL-FCST	FORECAST REVENUES*	ACTUAL REVENUES	DIFFERENCE ACTUAL-FCST
Individual Income Tax						
Withholding	1,775,600	1,802,613	27,013	7,906,292	7,938,966	32,673
Declarations	423,769	444,711	20,942	2,170,600	2,294,844	124,244
Miscellaneous	112,237	125,207	12,969	1,390,595	1,558,447	167,852
Gross	2,311,607	2,372,530	60,924	11,467,487	11,792,256	324,769
Refund	23,258	31,735	8,477	1,421,990	1,388,775	(33,214)
Net	2,288,348	2,340,795	52,447	10,045,497	10,403,481	357,984
Corporate & Bank Excise						
Declarations	345,482	323,570	(21,912)	1,296,033	1,366,062	70,029
Miscellaneous	65,872	125,097	59,225	229,757	244,509	14,752
Gross	411,354	448,667	37,313	1,525,790	1,610,571	84,781
Refund	16,754	12,215	(4,539)	208,678	155,295	(53,383)
Net	394,600	436,452	41,852	1,317,112	1,455,275	138,164
Sales Tax						
Gross	1,212,991	1,252,908	39,917	5,514,596	5,549,415	34,819
Mpls. sales tax transferred to MSFA	-	412	412	1,960	1,361	(600)
Sales Tax Gross	1,212,991	1,253,320	40,329	5,516,556	5,550,775	34,219
Refunds (including Indian refunds)	31,726	39,765	8,039	354,850	419,297	64,447
Net	1,181,265	1,213,554	32,289	5,161,706	5,131,478	(30,228)
Other Revenues:						
Net Estate & Gift Tax	38,124	45,667	7,543	136,500	145,292	8,792
Net Liquor/Wine/Beer	16,147	17,174	1,027	84,870	84,265	(604)
Net Cigarette/Tobacco	103,031	108,921	5,890	592,010	622,045	30,035
Deed and Mortgage	37,081	49,887	12,806	198,204	207,354	9,149
Net Insurance Gross Earnings	89,383	85,704	(3,679)	366,889	350,890	(15,998)
Lawful Gambling	11,949	10,015	(1,934)	46,350	49,007	2,657
Health Care Surcharge	20,814	17,003	(3,811)	286,423	287,915	1,492
Other Taxes	188	355	167	17,026	17,372	346
Statewide Property Tax	16,654	14,279	(2,375)	824,287	838,080	13,794
DHS SOS Collections	13,389	11,763	(1,626)	60,550	70,795	10,245
Investment Income	2,500	3,266	766	10,000	13,610	3,610
Tobacco Settlement	100	100	-	162,823	170,747	7,924
Dept. Earnings & MSOP Recov.	35,726	36,341	616	198,095	206,723	8,627
Fines and Surcharges	13,793	13,802	8	81,826	80,260	(1,566)
Lottery Revenues	8,491	4,060	(4,431)	57,269	66,270	9,001
Revenues yet to be allocated	-	963	963	(0)	0	0
Residual Revenues	18,684	17,534	(1,150)	159,872	137,906	(21,966)
County Nursing Home, Pub Hosp IGT	1,698	1,132	(566)	6,792	6,327	(465)
Other Subtotal	427,753	437,967	10,214	3,289,786	3,354,859	65,073
Other Refunds	847	1,172	325	5,855	5,800	(55)
Other Net	426,906	436,795	9,888	3,283,932	3,349,060	65,128
Total Gross	4,363,705	4,512,483	148,779	21,799,619	22,308,462	508,843
Total Refunds	72,586	84,888	12,302	1,991,372	1,969,168	(22,205)
Total Net	4,291,119	4,427,596	136,476	19,808,246	20,339,294	531,048

* February 2015 Budget & Economic Forecast adjusted for legislative changes.