MINNESOTA Management & Budget

July/August 2011 Economic Update

July/August 2011

FY 2011 Revenues $355 Million Above Forecast; FY 2012 Currently $93 Million Short

Minnesota's net general fund revenues totaled $15.663 billion in fiscal 2011, $355 million (2.3 percent) more than forecast in February. More than one-half of the additional revenue came from payments accompanying 2010 tax returns and payments accompanying extensions. Earlier than anticipated receipt of Wisconsin's final income tax reciprocity payment added $60 million to FY 2011's positive variance but reduced FY 2012 revenues by almost the same amount. February's revenue forecast had assumed Wisconsin's final settle-up payment would be part of fiscal 2012 receipts. Net general fund revenues for the first two months of fiscal 2012 were $93 million (4.4 percent) below forecast. (see page 4)

FY 2011 Revenues $355 Million (2.3%) Above February Forecast

	Estimate	Actual	Variance	Percent
	($ in millions)			
Individual	$7,252	$7,529	$277	3.8
Sales	4,433	4,403	(30)	(0.7)
Corporate	914	925	11	1.2
Motor Vehicle	31	31	- -	- -
Other	2,678	2,775	97	3.6
Total	$15,308	$15,663	$355	2.3

More than 75 percent of the additional fiscal 2011 revenue came from the individual income tax, and more than 60 percent of the positive individual income tax variance came from larger than projected final payments for tax year 2010. Withholding tax receipts were $44 million, (0.7 percent) more than forecast, while final payments and payments accompanying extensions exceeded forecast by a combined $199 million. Income tax refunds were $13 million more than anticipated. Gross sales tax receipts were $42 million short of projections, but that revenue loss was partially offset by lower than anticipated sales tax refunds, leaving net sales taxes in FY 2011 only $30 million (0.7 percent) below February's projections.

As noted above more than 60 percent of the FY 2011 positive variance in other revenues was due to the timing of the receipt of Wisconsin's income tax reciprocity payment. Higher than projected receipts for the mortgage, deed, and insurance gross premiums taxes accounted for much of the remaining revenue gain. Total general fund receipts for fiscal 2011 were 10.5 percent more than in fiscal 2010. Net income tax receipts grew by 15.3 percent over the prior fiscal year while net sales tax revenue was 5.4 percent greater than in fiscal 2010.

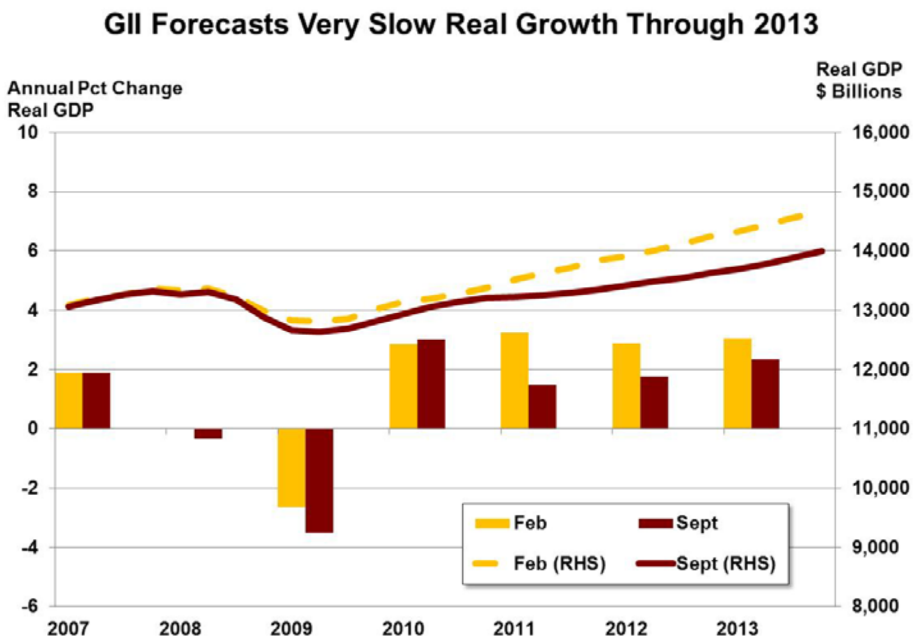
July and August Revenues Appear on Track

Net receipts from the individual income tax, the corporate income tax, and the sales tax modestly exceeded forecast in July and August while other revenues were well below projections. About one-half of that $114 million negative variance is due to the posting of receipt of the income tax reciprocity payment in the 2011 fiscal year. Much of the rest of the variance appears to be attributable to timing differences in processing and posting of receipts caused by July's state-wide shutdown and the start-up of a new state accounting system. The variance for cigarette and tobacco tax revenue was set to zero because of inadequate receipts data. More complete and more timely information on other revenues is expected to be available for inclusion in the regularly scheduled October *Economic Update*.

U.S. Economic Outlook Downgraded – Subpar GDP Growth Expected in 2011 and 2012

There has been a great deal of economic news recently. Unfortunately, almost none of it has been good. Economic growth was slower than anticipated during the first half of 2011 and hiring less than hoped. While some of the weakness could be explained by temporary factors, including bad weather and the U.S. economic fallout from the Japanese earthquake and tsunami, by mid-July most forecasters concluded that the economy was in a much more fragile position than previously suspected. The policy gridlock displayed as the U.S. Congress struggled with what should have been a routine increase in the debt ceiling and major concerns about a widening Eurozone sovereign debt crisis added to perceptions that all was not well, and major revisions to forecasts for economic growth in 2011 and 2012 followed. August's Blue Chip Consensus forecast for real GDP growth in 2011 fell to 1.8 percent as all 45 Blue Chip forecasters substantially dialed back their outlook. July's Consensus– the median of 45 independent forecasts – was 2.5 percent.

Events in August brought no relief. Standard and Poor's reduced America's credit rating to AA+, Europe's credit crisis appeared to worsen further, and several regional surveys showed manufacturing struggling. The steady stream of bad news and a plunging stock market drained consumer confidence, pushing the Thompson Reuters / University of Michigan index down by 20 points over three months to its second lowest reading since 1980. In September the Blue Chip Consensus forecast for 2011 real GDP growth slipped another 0.2 percentage points, dropping to 1.6 percent. And when the August payroll employment report showed zero job growth, concern over a possible recession in late 2011 and early 2012 increased.



The September baseline forecast from Global Insight Incorporated, (GII), Minnesota's macro-economic consultant, projects a much slower growth path for the U.S. economy than was anticipated in February when the most recent Minnesota revenue forecast was completed. GII's September baseline (probability 50 percent) calls for real GDP growth of just 1.5 percent in 2011 and 1.8 percent in 2012. Their February baseline, which was assigned a probability of 65 percent when issued, called for a 3.2 percent increase in 2011 coupled with 2.9 percent real growth in 2012. GII also cutback their outlook for 2013. The cumulative impact of those changes in the forecast is substantial. In February Global Insight expected the U.S. economy to grow by 6 percent over the 2012-13 biennium, September's baseline shows real GDP increasing by just 3.6 percent over that same period. GII's September forecast assumed the current 2 percentage point payroll tax cut and the emergency unemployment benefits scheduled to expire at the end of this year are extended through 2012, but that no additional stimulus programs are approved.

Global Insight characterizes the current state of the U.S. economy as "dangerously close to stall speed," and has assigned a probability of 40 percent to a scenario containing a recession beginning this fall. February's pessimistic scenario, which did not include a recession, was assigned a probability of just 15 percent. Global Insight's concern is that in its current weakened state the U.S. economy is unlikely to be able to withstand a policy mistake in either Washington or the Eurozone. And, given the counterproductive political stalemates observed in both Europe and the U.S. in recent months the risk that policy adjustments will not be made quickly enough to avert another economic downturn is high.

COMPARISON O F ACTUAL AND ESTIMATED NON-RESTRICTED REVENUES

($ IN THOUSANDS)

	NON-RESTRICTED REVENUES FY 2011 Close			COMPARISON OF ACTUAL AND ESTIMATED August YTD, 2011 - FY2012		
	FORECAST REVENUES	ACTUAL REVENUES	VARIANCE ACT-FCST	FORECAST REVENUES	ACTUAL REVENUES	VARIANCE ACT-FCST
Individual Income Tax						
Withholding	6,366,599	6,410,378	43,779	1,016,200	1,024,226	8,026
Declarations	1,257,702	1,330,988	73,286	17,959	23,322	5,364
Miscellaneous	838,715	1,011,874	173,159	38,474	22,920	(15,554)
Gross	8,463,015	8,753,240	290,225	1,072,632	1,070,468	(2,164)
Refund	1,211,300	1,224,036	12,736	12,490	5,475	(7,015)
Net	7,251,715	7,529,204	277,489	1,060,142	1,064,993	4,851
Corporate & Bank Excise						
Declarations	833,157	859,671	26,515	46,275	55,976	9,701
Miscellaneous	189,834	181,569	(8,264)	21,661	24,671	3,010
Gross	1,022,990	1,041,241	18,250	67,936	80,648	12,712
Refund	109,201	116,628	7,427	2,855	1,457	(1,398)
Net	913,790	924,613	10,823	65,081	79,191	14,110
Sales Tax						
Gross	4,657,800	4,615,260	(42,540)	710,541	700,604	(9,937)
Refunds	224,258	211,852	(12,406)	17,900	5,525	(12,375)
Net	4,433,542	4,403,408	(30,134)	692,641	695,079	2,438
Motor Vehicle Sales Tax	31,131	30,578	(553)	0	0	0
Other Revenues:						
Estate	171,500	165,807	(5,693)	26,617	25,299	(1,318)
Liquor/Wine/Beer	76,958	78,422	1,464	8,210	8,072	(138)
Cigarette/Tobacco/Cont Sub	190,750	190,363	(387)	33,017	33,017	0
Deed and Mortgage	141,300	153,416	12,116	14,143	14,150	7
Insurance Gross Earnings	279,702	287,914	8,212	6,056	5,521	(535)
Lawful Gambling	40,300	41,796	1,496	5,459	5,643	184
Health Care Surcharge	238,300	240,033	1,733	39,017	16,887	(22,130)
Other Taxes	16,001	13,518	(2,483)	227	97	(130)
Statewide Property Tax	762,225	766,926	4,701	7,719	18,383	10,664
DHS SOS Collections	47,500	57,142	9,642	7,572	10,960	3,388
Income Tax Reciprocity	0	59,719	59,719	58,697	0	(58,697)
Investment Income	1,500	2,100	599	167	0	(167)
Tobacco Settlement	164,614	169,375	4,761	100	100	0
Departmental Earnings	255,000	254,575	(425)	28,452	10,827	(17,625)
Fines and Surcharges	100,000	96,349	(3,651)	7,802	47	(7,755)
Lottery Revenues	59,593	56,119	(3,474)	4,409	0	(4,409)
Revenues yet to be allocated	0	(6)	(6)	0	14,326	14,326
Residual Revenues	175,675	183,999	8,324	37,193	4,986	(32,207)
County Nursing Home, Pub Hosp IGT	5,216	5,216	0	1,132	566	(566)
Other Subtotal	2,726,133	2,822,783	96,650	285,988	168,880	(117,108)
Other Refunds	48,245	47,836	(409)	4,058	1,018	(3,040)
Other Net	2,677,888	2,774,947	97,059	281,929	167,862	(114,067)
Total Gross	**16,901,070**	**17,263,102**	**362,032**	**2,137,097**	**2,020,599**	**(116,498)**
Total Refunds	**1,593,003**	**1,600,352**	**7,349**	**37,304**	**13,474**	**(23,829)**
Total Net	**15,308,066**	**15,662,749**	**354,683**	**2,099,793**	**2,007,124**	**(92,669)**