



COMMONWEALTH of VIRGINIA

Office of the Governor

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Secretary of Finance

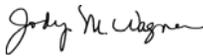
P.O. Box 1475
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February 13, 2008

MEMORANDUM

TO: The Honorable Timothy M. Kaine

THROUGH: The Honorable Wayne M. Turnage

FROM: Jody M. Wagner 

SUBJECT: January Revenue Data

January is a significant month for revenue collections. Individual estimated payments, sales taxes on December sales, and corporate income tax payments from large retailers are due this month. General fund revenues grew 3.5 percent in January 2008 compared to January 2007. On a year-to-date basis, aggregate revenues grew 3.3 percent over the same period last year, equal to the annual forecast of 3.3 percent. Individual withholding is tracking its forecast, while sales, individual nonwithholding, corporate, and recordation tax collections are all trailing their respective forecasts.

For this month's report, the December 2007 forecast is the basis for comparing actual collections. This forecast is also the basis for the revenue estimates included in the Governor's introduced budgets to the 2008 General Assembly. (HB/SB 29 and HB/SB 30). The March revenue letter will use the February 2008 revised forecast to compare with actual collections.

National Economic Indicators

Recent indicators depict deteriorating economic conditions, as the housing shock and credit crunch spread through the economy. In response to the slowing economy, the federal government passed a \$168 billion fiscal stimulus plan.

- Real GDP grew just 0.6 percent in the fourth quarter, about half as fast as consensus expectations.
- The job market weakened significantly in January – payroll employment fell by 17,000 jobs for the month, the first decline since August 2003. The December gain of 18,000 jobs, however, was revised up to 82,000. In a separate report, the unemployment rate inched down from 5.0 to 4.9 percent.
- Initial claims for unemployment dropped by 22,000 to 356,000 during the week ending February 2. The four-week moving average increased from 326,500 to 335,000.

- Inflation remained tame in December as the Consumer Price Index increased only 0.3 percent. Core inflation, excluding food and energy, rose by 0.2 percent in December, resulting in growth of 2.4 percent over the same period last year.
- The manufacturing sector remained weak in January. The Institute of Supply Management index rose from 48.4 to 50.7, barely above the expansionary level. The sluggishness in the index is consistent with a stalled economy.
- The Conference Board's index of leading indicators fell 0.2 percent to 136.5 in December, the third consecutive monthly decline. The index is at its lowest level since Hurricane Katrina. Generally, a negative reading for six to nine months is indicative of a recession. The index has declined in four of the last six months, falling at an annualized rate of 1.6 percent.
- The Conference Board's index of consumer confidence fell from 90.6 to 87.9 in January, essentially reversing the December gain. The expectations component caused the decline, as the current conditions component increased. The index remains at a very low level, but appears to have stabilized over the last three months.
- At its January 30 meeting, the Federal Reserve lowered the federal funds rate by 50 basis points. This came after the emergency meeting rate cut of 75 basis points in the previous week. Since it began to loosen monetary policy in September, the Federal Reserve has lowered the rate from 5.25 percent to 3.0 percent.

Virginia Economy

In Virginia, payroll employment grew 1.7 percent in December. Jobs grew by 2.1 percent in Hampton Roads, 1.5 percent in Northern Virginia, and 1.6 percent in the western MSAs. Employment was essentially flat in Richmond-Petersburg, with 0.2 percent growth. The unemployment rate rose slightly, from 3.0 percent to 3.3 percent in December.

The Virginia leading index advanced 0.5 percent in December, its first increase in five months. Two of the three components of the index – auto registrations and initial unemployment claims -- contributed to the growth in December. The regional indices rose in all eleven of Virginia's metropolitan areas in December. Northern Virginia saw the largest increase.

January Revenue Collections

General fund revenues grew 3.5 percent in January 2008 compared to January 2007. On a year-to-date basis, revenues grew 3.3 percent over the same period last year, equal to the annual forecast.

Net Individual Income Tax (65% of general fund revenues): Year-to-date net individual income

tax growth is 6.3 percent, slightly below the projected annual growth rate of 6.5 percent, due to the lagging collections of nonwithholding taxes. Performance in each component of individual income tax is as follows:

Individual Income Tax Withholding (56% of general fund revenues): Collections of payroll withholding taxes grew 7.2 percent in January. Year-to-date withholding growth is 5.8 percent, close to the projected annual growth rate of 5.6 percent. This growth rate is supported by payments made in January that normally would not be made until February by some large employers.

Individual Income Tax Nonwithholding (19% of general fund revenues): Collections of nonwithholding in January 2008 increased 12.2 percent from January 2007. Year-to-date, collections in this source are 8.0 percent above the same period last year, lagging the estimate of a 10.0 percent increase.

December and January are significant months for collections in this source, and growth can be distorted by the timing of payments. The two month total in receipts shows a 3.4 percent increase and a significant slowdown from September's 8.1 percent increase.

Individual Income Tax Refunds: TAX issued \$83.8 million in individual refunds in January 2008, compared with \$79.4 million in January 2007. Year to date, refunds are 4.0 percent ahead of the same period last year, trailing the annual forecast of a 7.7 percent increase.

Sales Tax (19% of general fund revenues): Collections of sales and use taxes, reflecting December sales, fell 12.4 percent in January. It appears that a significant amount of the holiday shopping occurred in November, since November sales tax collections were up 16.0 percent. On a year-to-date basis, collections of sales and use taxes have increased 1.7 percent, trailing the forecasted growth rate of 2.8 percent. The main holiday shopping season as represented by the two month total, actually fell 0.6 percent for the first time since fiscal year 2003. This marks only the third time since fiscal year 1991 that the two month total was down from the prior year. A more complete picture of the holiday season will be available once February receipts, which reflect January post holiday sales and gift card redemptions, are available.

Corporate Income Tax (5% of general fund revenues): For the first seven months of the year, corporate income tax collections have fallen 22.3 percent from the same period last year, behind expectations of a 15.0 percent decline. Lower corporate estimated payments and a substantial increase in refund activity contributed to the decline.

Wills, Suits, Deeds, Contracts (3% of general fund revenues): Wills, suits, deeds, and contracts – mainly recordation tax collections – fell 23.5 percent in January as the housing market continued to slow. On a year-to-date basis, collections in this source declined 18.1 percent from last year, compared with the estimate of a 10.7 percent annual decline.

Other Revenue Sources

The following list provides data on January collections for other revenue sources.

	<u>Year-to-Date</u>	<u>Annual Estimate</u>
Insurance Premiums Taxes (2% GF revenues)	13.4%	4.8%
Interest Income (1% GF revenues)	19.9%	-0.6%
ABC Taxes (1% GF revenues)	2.0%	5.0%

All Other Revenue: Receipts in All Other Revenue grew 5.5 percent in January – \$59.4 million compared with \$56.3 million in January 2007. Most of the increase was in inheritance, gift, and estate taxes -- \$19.7 million compared with \$14.6 million in January 2007. For the fiscal year-to-date, collections of All Other Revenue are 7.6 percent ahead of the same period in fiscal year 2007, ahead of the annual estimate of a 5.5 percent decline.

Lottery Revenues: Net income totaled \$29.9 million in January 2008 or \$0.7 million less than January 2007. January 2008 was 2.2 percent behind January 2007 as prize payouts were higher than expected. Year-to-date, net income is up 10.7 percent compared to the annual forecast of a 3.7 percent increase. Comparisons to last year are affected because products currently offered (Fast Play Bingo, additional daily games' drawings) were not offered or included in sales and net income results from last year. In addition, jackpot sales were significantly depressed last year because of unusually low advertised jackpots.

Summary

General fund revenues grew 3.5 percent in January 2008 compared to January 2007. On a year-to-date basis, aggregate revenues grew 3.3 percent over the same period last year, equal to the annual forecast of 3.3 percent. Individual withholding is tracking its forecast, while sales, individual nonwithholding, corporate, and recordation tax collections are all trailing their respective forecasts. April and May are the next significant collection months for corporate and individual payments.

Although total general fund revenue collections through January are equal to the annual estimate, the forecast anticipates further weakness in individual and corporate income tax payments, a continued slowdown in sales tax receipts, and continued soft recordation tax receipts as the housing market

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remains stalled. The source of most concern is individual nonwithholding payments. These payments were weaker than expected in the December-January timeframe. Using historical collection patterns as a guide, receipts in these sources are not within the bounds of what is required to attain the annual forecast.

Given revenue collections and the deteriorating economic conditions, in early February, the Governor convened special interim meetings of the Governor's Advisory Board of Economists and the Governor's Advisory Council on Revenue Estimates. The results of these meetings were the basis for the changes included in the February midsession revenue forecast released by the Governor on February 12, 2008. The March revenue letter will incorporate that revised revenue forecast.