



COMMONWEALTH of VIRGINIA
Office of the Governor

Richard D. Brown
Secretary of Finance

PO Box 1475
Richmond, VA. 23218

February 13, 2009

MEMORANDUM

TO: The Honorable Timothy M. Kaine

THROUGH: The Honorable Wayne M. Turnage

FROM: Richard D. Brown *Richard D. Brown*

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. January revenues fell 15.0 percent as compared to January 2008 mainly due to an historic drop in individual estimated payments (-26.1 percent) due January 15. In addition, payroll withholding fell by 10.6 percent, in part attributable to two fewer deposit days. On a year-to-date basis, total revenues fell 5.5 percent, dropping below the annual (budget) forecast of a 4.8 percent decline.

The 5.5 percent decline in revenue collections through January represents the largest drop on record. Adjusted for tax policy changes, collections are down by 2.7 percent – more than a percentage point larger than the fiscal year 2002 decline and almost two percentage points larger than fiscal year 1991. All major sources are trailing their respective forecasts.

This month's report compares actual revenue collections to the revenue estimates prepared in December 2008 and was included in the Governor's budget introduced to the 2009 General Assembly. The March revenue report will incorporate any mid-session revisions to the official revenue forecast released in December.

National Economic Indicators

National economic indicators continue to depict a deepening recession.

- Real GDP fell at an annual rate of 3.8 percent in the fourth quarter of 2008, according to the advance estimate. Although it was better than the projected 5.4 percent drop, it was the largest quarterly contraction since the first quarter of 1982. Consumer spending, business investment, and investment in housing all declined in the fourth quarter.
- Payroll employment declined by 598,000 jobs in January, the largest one-month decline since December 1974. Over the last three months, nearly 1.8 million jobs have been lost, the worst three-month loss since 1945. Since employment began declining in January of last year, the economy has lost 3.6 million jobs. In a separate report, the unemployment rate rose to 7.6 percent from 7.2 percent, the highest rate since 1992.
- Initial claims for unemployment grew by 35,000 to 626,000 during the week ending January 31. The four-week moving average increased from 543,000 to 582,000, a level indicative of persistent weakening in the labor market.
- Consumer confidence continues to deteriorate -- the Conference Board's index of consumer confidence fell in January from 38.6 to 37.7, a historic low. Both the current conditions and expectations components fell.
- Conditions in the manufacturing sector slightly improved in January. The Institute of Supply Management index rose 2.7 points to 35.6. However, it remains at a very low level, indicating the sector is still contracting.
- The Conference Board's index of leading indicators rose 0.3 percent to 99.5 in December, the first increase since last April and the largest monthly gain since July 2007. The increase, however, was driven by a sharp increase in the money supply engineered by the Federal Reserve to stimulate the economy.
- At its January meeting, the Federal Reserve left the federal funds target rate in the range of 0.0 percent to 0.25 percent, stating that, the "economy has weakened further" from the previous meeting.

Virginia Economy

After very little growth in November, the Virginia labor market contracted in December, losing 31,100 jobs compared with December of last year. This was the first month of negative year-over-year job growth in the Commonwealth since June 2003. Payroll employment fell 0.8 percent for the month. Northern Virginia posted a decline of 0.1 percent in December, while employment grew by 1.0 percent in Hampton Roads. Employment in the Richmond-Petersburg area fell 1.0 percent, registering a third

consecutive monthly decline. The unemployment rate in Virginia rose from 4.6 percent to 5.2 percent in December. In December of 2007, the unemployment rate was 3.2 percent.

The Virginia Leading Index fell 0.5 percent in December, the eighth decline in the last twelve months. All three components – auto registrations, building permits, and initial unemployment claims – contributed to the decline.

January Revenue Collections

In January, individual estimated payments, sales taxes on December sales, and corporate income tax payments from large retailers are due making this a significant month for revenue collections. January revenues fell 15.0 percent mainly due to an historic drop in individual estimated payments due January 15 and a 10.6 percent decline in payroll withholding. On a year-to-date basis, total revenues fell 5.5 percent, falling below the annual forecast of a 4.8 percent decline.

Net Individual Income Tax (67% of general fund revenues): Year-to-date collections of net individual income tax fell 0.5 percent, close to the annual estimate of a 0.7 percent decline. Performance in each component of individual income tax is as follows:

Individual Income Tax Withholding (62% of general fund revenues): Growth in this source slowed considerably, particularly in the last half of the month. With two fewer deposit days, collections of payroll withholding taxes fell 10.6 percent in January. December had two extra deposit days, so the two months must be analyzed together to accurately assess growth in this source. Taken together, growth was 0.4 percent over December and January of last year, matching the prior weakest December-January period in fiscal year 1990. Year-to-date withholding growth is 3.0 percent, trailing the projected annual growth rate of 3.4 percent.

Individual Income Tax Nonwithholding (17% of general fund revenues): Collections in this source fell 26.1 percent in January. December and January are significant months for collections in this source, and growth can be distorted by the timing of payments. Receipts for the two-month period show a 20.3 percent decline – exceeding the declines experienced in the last two recessions in fiscal years 1990 and 2002. Year to date through January, collections fell 11.1 percent compared with the annual estimate of an 8.4 percent decline.

Individual Income Tax Refunds: TAX issued \$108.2 million in refunds in January compared with \$83.8 million last January. The main filing season will begin in February.

Sales Tax (20% of general fund revenues): Collections of sales and use taxes, reflecting December sales, fell 0.9 percent in January. On a year-to-date basis, collections have fallen 4.6 percent, below the annual estimate of a 2.1 percent decline.

This holiday shopping season is shaping up to be the worst on record. Taken together, collections of sales taxes in December and January fell 8.8 percent compared with the forecast of a 3.0 percent drop, and national expectations of a 2.5 percent decline. A more complete picture will be available once February receipts, which represent January post-holiday sales and gift card redemptions, are available.

Corporate Income Tax (5% of general fund revenues): Through January, collections in corporate income taxes have fallen 18.6 percent from the same period last year, slightly trailing expectations of a 15.2 percent decline.

Wills, Suits, Deeds, Contracts (2% of general fund revenues): Collections of wills, suits, deeds, and contracts – mainly recordation tax collections – fell 40.1 percent in the month of January, and are down 36.2 percent on a year-to-date basis. Adjusted for the transfer of 3 cents of the 25 cents per \$100 recordation tax to the Commonwealth Transportation Fund, year-to-date collections are down 29.1 percent

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 (2% GF revenues)*	-54.3%	-35.1%
Interest Income (1% GF revenues)	-36.5%	-36.2%
ABC Taxes (1% GF revenues)	2.1%	3.6%

**Monthly collections of insurance premiums have been transferred to the Transportation Trust Fund per HB 3202 to meet the required \$132.3 million.*

All Other Revenue (3% of general fund revenues): Receipts in All Other Revenue fell 30.2 percent in January – \$41.5 million compared with \$59.4 million last January. For the fiscal year-to-date, collections of All Other Revenue fell 27.4 percent from the same period in fiscal year 2008, close to the annual estimate of a 24.2 percent decline. The large decline in year-to-date collections and the annual forecast is attributable to the repeal of the estate tax. The General Assembly repealed the tax effective July 1, 2007, and estates from deaths prior to that date had up to nine months to file.

Lottery Revenues: Net income for January 2009 totaled \$35.4 million, an increase of \$4.9 million from January 2008. Year-to-date, net income is down 5.8 percent, trailing the annual estimate of a 5.4 percent decline. The increase in net income was a result of lower prize rates this January as compared to January 2008.

Summary

Because January is a significant month for revenue collections, analysis of the actual collection data relative to the growth required by the December forecast in the introduced budget will form the basis of any recommended mid-Session forecast adjustments. Collections overall declined 15.0 percent in January, with many of the major revenue sources deteriorating significantly from the prior months. For example, payroll withholding declined by 10.6 percent in January and sales tax collections for the holiday shopping season fell well beyond any other comparable period on record. On a year-to-date basis, total revenues fell 5.5 percent, below the annual forecast of a 4.8 percent decline. Based on this preliminary analysis, a February mid-session revenue forecast will be necessary.