



COMMONWEALTH of VIRGINIA

Office of the Governor

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On the surface, revenue collections for August increased 11.7 percent, bringing year-to-date growth to 10.2 percent. However, those totals are misleading. Final accounting for accelerated sales tax payments and receipt as revenue of one quarter's enhanced federal reimbursement for Medicaid (FMAP funding) significantly distorted the nominal totals.

Once these distortions are corrected, August monthly revenue collections grew about 5.0 percent, with year-to-date growth of 6.6 percent. Revenue growth required to meet the fiscal year 2004 forecast, once the small fiscal year 2003 surplus is factored in, is 4.6 percent.

August had one less deposit day this year than last year.

National Economic Indicators

Although the job market remains very weak, most recent indicators suggest that the national economy is gaining strength.

- Payroll employment fell by 93,000 jobs in August, the seventh consecutive monthly drop. The unemployment rate fell 0.1 percent to 6.1 percent. Temporary employment, which generally picks up prior to sustained job growth, has increased for the last four months - a positive sign.
- Initial claims for unemployment rose to 413,000 during the last week of August, pushing the four-week average above the benchmark level of 400,000. Despite the August increase, the number of initial claims has been trending down since peaking at 450,000 in May, 2003.
- The manufacturing sector is showing signs of growth. The Institute of Supply Management index rose to 54.7 in August, the fourth consecutive increase and the second consecutive month above the break-even 50.0 level.
- The Conference Board's index of leading indicators rose 0.4 percent in July, the fourth month in a row that the index has increased. The growth indicates the economy is improving, although only five of the index's ten components improved. The lack of broad-based strength suggests some continuing economic weakness.
- Prices remain stable as the Consumer Price Index rose 0.2 percent in July.
- The Conference Board's index of consumer confidence rose moderately in July, as consumers' expectations for the future improved.
- The Federal Reserve left interest rates unchanged at its August meeting.

Virginia Economy

The Virginia Leading Index rose 1.4 percent in July -- its third consecutive monthly gain. All four components of the index increased, suggesting economic growth in the Commonwealth will continue for the next three to six months. The leading indices for all seven of the major metropolitan areas also increased in July.

August Revenue Collections

Revenue collections grew 11.7 percent in August, but were distorted by collections timing and the receipt as revenue of a significant infusion of federal Medicaid reimbursements for FY 2003. When the effects of these factors are removed, monthly growth for August was about 5.0 percent, and year-to-date growth stands at 6.6 percent.

Individual Income Tax Withholding (62% of general fund revenues): With one less deposit day, collections in withholding grew 2.8 percent above last August. Year-to-date withholding growth is 4.9 percent - below the 6.5 percent growth required to meet the estimate.

Individual Income Tax Refunds: Refunds this month totaled \$35.4 million, compared with \$35.2 million paid in August of last year. Most of this total results from taxpayers who had requested extensions and are now filing returns for tax year 2002.

Fiscal year-to-date, \$65.6 million in refunds have been issued, compared to \$88.0 million for the same period last year -- a decline of 25.4 percent.

Individual Income Tax Nonwithholding (12% of general fund revenues): The first individual estimated payment of fiscal year 2004 is due in September. Therefore, collections trends in this source are not yet significant. Year-to-date collections are 5.0 percent ahead of collections for the same period last year - and ahead of the forecast of a 4.8 percent decline.

Sales Tax (22% of general fund revenues): Collections of sales and use taxes increased by 20.0 percent in August, although growth was distorted by the processing of accelerated sales tax payments. Last year, it took until September to finalize processing of these payments. As a result, sales tax receipts for last August were down 11.9 percent. This year, processing was completed in August, creating the appearance of substantial sales tax growth.

If the timing of accelerated sales tax payments is factored in, year-to-date collections in sales taxes have increased about 3.0 percent through August.

Other Revenue Sources

The following list provides data on August collections of other key taxes:

	Year-to-Date	Required to Meet Estimate
Corporate Income Tax (3% GF revenues)	59.9 %	-8.0%
Insurance Premiums Tax (3% GF revenues)	-38.7 %	0.9%
ABC Taxes (1.1% GF revenues)	15.9%	-0.5%
Public Service Corporations (0.7% GF revenues)	-27.9%	-8.2%
Interest Income (0.7% GF revenues)	-22.7%	-2.1%

All Other Revenue. Revenue from all other sources increased 93.3 percent in August -- \$97.0 million compared with \$50.2 million in August of last year. Collections of wills, suits, deeds and contract fees (primarily recordation taxes) continued its strong growth.

The largest portion of the increase in All Other Revenue came from federal Medicaid payments. In August, Virginia received as revenue one quarter's enhanced federal reimbursement for Medicaid (about \$31 million), which comes as a result of the fiscal relief package approved by Congress last spring. Because the reimbursement involved payment for a prior year's expenses, accounting rules require that it be treated as revenue.

On a year-to-date basis, collections of all other revenue are 58.7 percent above the same period last year - well ahead of the annual forecast of a 2.7 percent decline.

Lottery Revenues. In August, Lottery net income increased 16.4 percent over last year - primarily because prize payouts were lower than expected. On a year-to-date basis, growth of 1.2 percent is slightly above the annual revenue estimate of -1.0 percent.

Summary

Revenue collections grew 11.7 percent in August. For the first two months of the fiscal year, total general fund revenue collections are up 10.2 percent -- well ahead of the estimate of 4.6 percent growth. Two principal factors distorted this month's revenue - a large federal Medicaid payment, and the timing of accelerated sales tax payments. Adjusting for these distortions, revenues grew about 5.0 percent for the month, with year-to-date growth of 6.6 percent.

The first estimated payments of the fiscal year in most major sources are due in September. Therefore, September will provide the first opportunity to assess revenue collections for the year.

The fall revenue forecasting process has begun. The Governor's Advisory Board of Economists will meet in October as the first step in assessing the outlook for the Virginia economy over the remainder of this fiscal year as well as the next biennium. This forecast will serve as the basis for the revised revenue forecast, which will be released in December.