



COMMONWEALTH of VIRGINIA

Office of the Governor

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March 14, 2006

MEMORANDUM

TO: The Honorable Timothy M. Kaine

THROUGH: The Honorable William H. Leighty

FROM: Jody M. Wagner

SUBJECT: February Revenue Data

This month's revenue report incorporates the revised general fund revenue forecast provided to the General Assembly on February 14, 2006. The mid-session forecast increased projected fiscal year 2006 revenues by \$177.1 million, moving the annual growth rate up to 7.4 percent. Net of tax policy changes, economics-based revenue growth in fiscal year 2006 is projected to be 9.9 percent.

February is not typically a significant month in revenue collections, other than marking the beginning of the individual income tax filing season. Total general fund revenue grew 4.5 percent in February. Most of the February revenue growth was due to solid growth in individual withholding payments. Through February, revenues grew 10.6 percent over the same period last year.

National Economic Indicators

Current indicators suggest the national economy is beginning the year on a strong note.

- Payroll employment added 243,000 jobs in February, far above expectations. However, January's gain of 193,000 jobs was revised down to 170,000. The strength in February was broad-based, with the largest gains in construction, education and healthcare and business services. The unemployment rate rose slightly to 4.8 percent.
- Initial claims for unemployment rose to 303,000 during the week ending March 4. The four-week moving average rose to 293,500 – consistent with an expanding job market. Although claims have been trending up, it is probably a result of the unseasonably mild weather in January causing claims to be much lower than normal.
- Personal income grew 0.7 percent in January. Growth was somewhat distorted as government transfer payments -- such as Social Security -- included cost of living adjustments. However, wages and salaries rose a solid 0.7 percent, the strongest gain since July 2005.
- The Conference Board index of leading indicators rose 1.1 percent in January. Further, the Board revised December growth in the index upward from 0.1 percent to 0.3 percent. Six of the ten components contributed positively to the index. The current reading indicates an acceleration of economic growth in the near term.
- Increasing energy prices pushed the Consumer Price Index up 0.7 percent in January. Core inflation, however, remains tame with a 0.2 percent increase for the month, bringing the annual rate of core inflation to 2.1 percent.

- The manufacturing sector continues to expand. The Institute of Supply Management index rose 1.9 percentage points to 56.7 in February.
- The Conference Board's index of consumer confidence fell to 101.7 in February, contrary to expectations. This was the first monthly decline since October 2005.

Virginia Economy

The Virginia Employment Commission released re-benchmarked employment data for calendar years 2004 and 2005. The revised data indicates that Virginia payroll employment is growing faster than previously reported. Year over year employment in Virginia grew 2.5 percent in January. In Northern Virginia, employment grew by 3.9 percent. In Richmond-Petersburg, jobs grew by 2.3 percent, followed by the western MSAs with 2.5 percent, and Hampton Roads with 1.7 percent growth. The unemployment rate fell slightly to 3.0 percent in January.

The Virginia Leading Index fell 0.2 percent in January after rising 0.7 percent in December. A decline in auto registrations and an increase in initial claims for unemployment offset a rise in building permits. The indexes in the Northern Virginia, Bristol, Charlottesville, Danville, Lynchburg and Winchester metropolitan areas fell in January, while Roanoke was unchanged. Several metropolitan areas posted increases in the index: Harrisonburg, Blacksburg, Richmond, and Hampton Roads.

February Revenue Collections

February is not typically a significant month in revenue collections, other than marking the beginning of the individual income tax filing season. Total general fund revenue grew 4.5 percent in February. Most of the February revenue growth was due to solid growth in individual withholding payments. Through February, revenues grew 10.6 percent over the same period last year.

Individual Income Tax Withholding (54% of general fund revenues): Reflecting the healthy job market, collections of payroll withholding taxes grew a solid 7.9 percent in February. Year-to-date withholding growth is 6.2 percent – exactly the projected growth rate for the fiscal year.

Individual Income Tax Nonwithholding (17% of general fund revenues): February is not a significant month for nonwithholding receipts. A total of \$48.1 million was collected in February, compared with \$35.4 million in February of last year.

To date, TAX has collected about 42 percent of the nonwithholding forecast, and collections are 19.8 percent above last year. The majority of the remaining collections in this source will occur in April and May, with both final payments for tax year 2005 and estimated payments for the current year due May 1.

Individual Income Tax Refunds: This month, TAX issued \$301.1 million in refunds compared with \$260.7 million in February of last year. Fiscal year-to-date, \$450.0 million in refunds have been issued compared to \$466.4 million in the same period last year. For the filing season beginning January 1, TAX issued about 845,000 refunds, compared with 840,000 issued in the same period last year.

Sales Tax (19% of general fund revenues): Collections of sales and use taxes fell 6.0 percent in February. Adjusting for the effects of tax relief on food, growth was 0.5 percent for the month. February collections represent January sales, completing the holiday shopping season (November through January). This year, seasonal sales were 6.1 percent above last year.

Year-to-date growth stands at 3.9 percent through February, ahead of the estimate of a 3.9 percent decline. Collections are expected to remain ahead of forecast until June, when the reduced Accelerated Sales Tax program will decrease collections by \$200.1 million.

Corporate Income Tax (6% of general fund revenues): As with individual nonwithholding, February is not a significant month for corporate income tax collections. Corporate income tax collections totaled \$17.7 million in

February, compared with \$8.6 million last February.

Other Revenue Sources

The following list provides data on February collections for other revenue sources:

| | Year-to-Date | Required to Meet Estimate |
|--|--------------|---------------------------|
| Insurance Premiums Taxes (3% GF revenues) | 1.9% | 5.1% |
| ABC Taxes (1.0% GF revenues) | 6.2% | -0.5% |
| Public Service Corporations (0.6% GF revenues) | 7.4% | 2.6% |
| Interest Income (0.7% GF revenues)* | 38.9% | 20.9% |

*Approximately 60% (\$20.0 million) of the interest for the current quarter is due to nongeneral funds and will be transferred in April.

All Other Revenue: Receipts in All Other Revenue were flat in February -- \$62.7 million compared with \$62.5 million in February of last year. Unprecedented growth in the largest component of all other revenue – wills, suits, deeds, and contract fees (mostly recordation tax receipts) – has driven growth in this source over the last few years. In February, growth in wills, suits, deeds, and contract fees (mostly recordation tax receipts) declined by 0.6 percent – the first decline in monthly growth in over a year. Year-to-date growth in this source stands at 33.1 percent, ahead of the estimate of 21.3 percent growth. For the fiscal year, collections of All Other Revenue are 8.6 percent above fiscal year 2005, ahead of the annual estimate of 4.0 percent growth.

Lottery Revenues: Lottery net profits increased 43.2 percent for the month. Sales for the Mega Millions jackpot growing to \$270 million by the February 28th drawing and significantly lower than expected payouts in the Pick 3 and Pick 4 games fueled the increase.

With the strong sales growth so far, the year-to-date net income growth rate of 14.8 percent is well ahead of the projected 2.4 percent annual rate. The Lottery Department reports that comparisons to prior periods are greatly influenced by the size of advertised jackpots and prize expense rates that fluctuate with the “luck of the draw.” Also, the kick-off of the North Carolina lottery later this fiscal year is expected to slow the overall sales growth. Both factors are incorporated into the Lottery’s revised net income projections for the current fiscal year and the upcoming biennium.

Summary

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Total general fund revenue grew 4.5 percent in February. Most of the February revenue growth was due to solid growth in individual withholding payments. Through February, revenues have grown 10.6 percent over the same period last year.