

January 16, 2001

**MEMORANDUM**

TO: The Honorable James S. Gilmore, III

THROUGH: The Honorable M. Boyd Marcus, Jr.

FROM: Ronald L. Tillett

SUBJECT: December Revenue Data

This month's revenue report displays the revised forecast released with your budget on December 20 in the first column and the required growth rates in the last column.

Revenue collections through the first half of fiscal year 2001 grew 0.2 percent above last year's extraordinary performance. While November far exceeded our expectations, December collections are more consistent with projections. As such, we are in line with the economic assumptions and revenue collections assumed in your budget amendments submitted on December 20, 2000.

As expected, December's receipts were 11.1 percent less than December last year mainly due to two fewer deposit days and a few extraordinary large individual estimated payments received last December. Notwithstanding the above-mentioned temporal factors, sales tax receipts, and corporate income tax estimated payments showed some weakness. We await the main holiday shopping receipts and individual income tax estimated payments due in January.

National indicators show that the economy has cooled considerably over the last month. The Federal Reserve's surprise fifty basis point cut on January 3 suggests that the Fed is postured to preempt an excessive slowdown in economic growth. The nation's payrolls grew by a moderate 105,000 jobs in December and the unemployment rate remained at 4.0 percent. The manufacturing sector is feeling the brunt of the slowdown. Employment in the goods-producing industries fell by 78,000 in December and the NAPM index fell to 43.7 percent, a level consistent with zero growth in the aggregate economy. The Index of Leading Economic Indicators fell 0.2 percent in November, the fifth decline in the past six months. Consumer confidence fell in December for the third consecutive month and the fifth monthly decline in the past seven months.

In Virginia, job growth remained healthy, increasing 2.0 percent in November compared with last year. The November unemployment rate was 2.0 percent -- the lowest November rate in 48 years.

**Individual Income Taxes**

Net individual income tax collections dropped in December, declining by 10.1 percent over last year. For the first half of the fiscal year, collections grew at 1.4 percent, lagging the revised annual forecast of 6.3 percent growth.

**Withholding:** Withholding collections fell by 1.0 percent compared to last December, mainly due to two fewer deposit days. Year-to-date growth of 5.1 percent is three percentage points behind the revised

estimate of 8.1 percent growth. December 2000 marks the final month when withholding receipts will be compared to the stock options surge, which took place throughout calendar year 1999. Monthly growth rates are expected to bounce back considerably over the next several months. Underlying withholding growth (adjusted for stock option activity in the first half of fiscal year 2000) for the first half of the fiscal year is a solid 9.0 percent.

Nonwithholding: Nonwithholding receipts for December declined by 43.5 percent. This sizeable drop can be attributed to several large anomalous payments received last December along with an increased number of early payments believed to be related to Y2K planning last year. Since the final individual estimated payment for taxable year 2000 is not due until January 15, 2001, it is not reasonable to assess nonwithholding receipts until all payments are received by the end of January. On a year-to-date basis, the 7.0 percent decline is lagging the revised forecast of 9.1 percent growth.

Refunds: Refunds this month were \$16.2 million compared with \$14.2 million in December of last year. About 85 percent of refunding activity takes place in the second half of the fiscal year.

### Sales

December sales tax collections, which represent November activity, fell by 6.3 percent. Year-to-date growth in this source stands at 2.9 percent, 1.5 percentage points behind the revised forecast of 4.4 percent.

Several factors account for the slow 2000 holiday shopping season. Higher fuel prices, the turmoil surrounding the presidential election, and the stock market plunge have all contributed to the disappointing sales results. In Virginia, January sales tax collections should contain the bulk of holiday sales receipts. Consequently, it is impossible to fully assess the Christmas shopping season until January. The revised forecast anticipates a 5 percent increase in November and December sales tax collections.

### Corporate Income Tax

Corporate receipts in December fell by 66.3 percent. The decline in December receipts, which include the second quarterly estimated payment, were primarily because of both a 27 percent decline in estimated payments and a 111 percent increase in corporate refunds. Although December's weak collections were somewhat overstated by several unusually large refunds, the weakness in the corporate sector estimated payments is broad-based. The year-to-date decline of 30.9 percent is well behind the annual forecast of a 15.8 percent decrease.

### Public Service Corporations

December's estimated payments represent the final estimated payments to be received from electric and gas utilities as deregulation of these industries begins in January 2001. Beginning in March 2001, quarterly estimated payments will be replaced by a monthly consumption tax. December's collections were up 0.8 percent over last December. For the year, receipts are up 1.5 percent compared with the revised forecast of a 16.1 percent decline.

### Insurance Company Premiums

December collections of insurance company premiums, which represent the second quarterly payment from insurance companies, declined by 0.6 percent over last year. Year-to-date growth of 3.1 percent is

slightly behind the revised forecast of 3.4 percent growth.

### Interest

During December, interest income increased by 39.2 percent over last year (\$19.9 million versus \$14.3 million). Year-to-date growth of 20.4 percent is well ahead of the revised forecast of 6.8 percent growth.

### ABC Taxes

ABC taxes (Beer and Beverage excise only) fell by 2.4 percent in December over last year. Year-to-date growth of 5.2 percent is ahead of the revised forecast of 4.2 percent growth.

### Lottery Revenues

Lottery net income was \$22.6 million, \$4.7 million or 17.3 percent lower than December last year mainly due to high Pick 3 prize payouts. Last year's Pick 3 payout rate for the month was a low 38.8 percent, while this year's was 60.6 percent due draws on some of the most popular numbers -- 111, 777, 411, and 233.

On a year-to-date basis, Lottery net income is down 0.7 percent, slightly ahead of the required annual growth rate of a 2.9 percent decline.

### All Other Revenue

Revenue from all other sources grew by 17.7 percent in December. Most of December's increase was due to collections of the volatile inheritance, gift and estate taxes (up 92.9 percent). On a year-to-date basis, all other revenue is down 8.0 percent, slightly trailing the revised forecast of a 6.4 percent decline.

### Summary

Revenue collections through the first half of fiscal year 2001 were influenced by a slow December. However, December's collections should not be considered a bellwether for future revenue receipts nor does it serve as evidence of an excessive slowing of the Virginia economy. Two fewer deposit days and the comparison to last December's anomalous nonwithholding collections seriously skew this month's performance. December's revenues are generally consistent with expectations, given last year's stellar performance.

Withholding collections should rebound sharply over the next six months as December, 2000 marks the final month when withholding receipts are compared to the stock option surge of calendar year 1999. An evaluation of individual nonwithholding or sales tax collections at this point could result in highly misleading conclusions. The final taxable year 2000 individual estimated payments are not due until January 15. In addition, the majority of sales tax receipts for the holiday shopping season will not be received until the end of January. However, revenue collections are expected to bounce back significantly over the next several months.