



COMMONWEALTH of VIRGINIA

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MEMORANDUM

TO: The Honorable Glenn Youngkin

THROUGH: The Honorable Jeff Goettman

FROM: Stephen E. Cummings

SUBJECT: May Revenue Report

Total general fund revenues rose by 9.9 percent in May, but as discussed last month, timing distortions related to last year's delayed federal tax filing date from April 15 to May 17, 2021, require the consideration of April and May collections together. Total general fund revenues for April and May combined grew by more than \$1.5 billion over the same period last year, an increase of 27.3 percent, and 18.1 percentage points higher than the mid-session forecast growth rate of 9.2 percent.

On a fiscal year-to-date basis, total revenue collections have risen 17.8 percent. With one month to go, we have collected 95 percent of the total general fund revenues anticipated in the February revised forecast.

For the month, payroll withholding increased by 12.9 percent. May included an additional deposit day. Without the extra deposit day, collections still increased a strong eight percent for the month. A strong labor market, which has produced 61,000 jobs in the three months since January, drove growth in payroll withholding.

There were 113,000 more Virginians employed in April 2022 than there were in April 2021, an increase of 2.7 percent year-over-year. In a separate survey of business establishments, payroll employment was estimated to have grown 3.2 percent in April versus the prior year. While Virginia has underperformed the nation in jobs recovered since the pandemic, ranking 47th overall, momentum is building. For the first four months of the year, Virginia ranked 16th among the states for employment growth.

The outlook for continued job growth is positive as Virginians who were previously not participating in the labor market are returning to the workforce. After having fallen much more than the nation as a whole during the pandemic, Virginia's labor force participation rate has increased 0.9 percentage points since December. However, although recent trends are encouraging, Virginia has yet to recover more than 151,000 jobs that were lost during the pandemic (now at 96.5 percent of pre-pandemic levels) while our key competitor states – North Carolina, South Carolina, Georgia, Tennessee, Texas and Florida – have all exceeded pre-pandemic employment levels. More improvement in this area is needed and we are optimistic that, with the current trends, that gap will continue to close.

As explained previously, individual nonwithholding collections declined 2.3 percent for the month, but due to the timing distortions related to the delayed federal tax filing date from April 15 to May 17, 2021, combined results for April and May must be compared for year-over-year comparisons of nonwithholding collections. The majority of last year's final payments were collected in May (versus April this year), making single month-over-year comparisons of nonwithholding and individual income tax refunds misleading. On a combined basis, April and May nonwithholding collections grew 51.2 percent, more than \$1.2 billion over the same period last year and well ahead of the forecast of 2.5 percent annual growth.

Additionally, fewer refunds were issued in May as we returned to the normal federal and state tax filing deadlines. Refunds were down 56.7 percent for the month as compared to last year when the filing date was mid-May. For April and May combined, refunds were down \$41.8 million, or 6.5 percent versus the same two-month period in fiscal year 2021.

Sales tax collections reflect continued growth in inflation-driven consumer spending, increasing by 8.6 percent for the month of May which is based upon April sales transactions. Fiscal year-to-date growth of 13.8 percent remains solidly ahead of the 11.4 percent annual growth forecast.

Corporate tax receipts were down 36.5 percent compared to May 2021, but on a year-to-date basis, is within one-tenth of one percent of the forecast at 32.7 percent versus a forecast of 32.6 percent. May is not a significant month for corporate income tax collections.

Looking ahead to the remainder of the current fiscal year, Finance staff anticipate total general fund revenues will exceed the revenue projections contained in the February mid-session forecast by more than \$1.2 billion, supported by better than expected final nonwithholding tax payments, lower than expected individual income tax refunds, and continued growth in withholding and sales taxes.

Monitoring national and global issues that may impact our future revenue streams remains a top priority. Employment growth continues, and the unemployment rate remains low. However, volatility in the financial markets, rising interest rates and persistent high inflation have the potential to cause consumers to tighten spending. Wage growth is moving in a positive direction, but the effects of inflation will begin to squeeze consumers. The consumer price index has increased more than wages, and critical products like gasoline, other energy related expenditures

and food at home have risen double-digit percentages, significantly outpacing average wage growth.

Given uncertainties in the outlook at the time of the mid-session forecast adjustment in February, the decision was made not to adjust fiscal year 2023 and 2024 revenue projections. Given the current environment, the Finance staff remains confident in that decision and looks forward to revisiting revenue projections during the fall consensus forecasting process.

Economic Review

Recent economic data are generally positive with continued job growth but continued high inflation and rising interest rates are beginning to undermine consumer confidence.

- The U.S. labor market added 390,000 jobs to payrolls in May. The gains were broad-based across sectors and exceeded consensus expectations. In a separate report, the unemployment rate remained steady at 3.6 percent even as more workers entered the labor force.
- Initial claims for unemployment fell by 11,000 to 200,000 during the week ending May 28. The four-week moving average was little changed at 206,500. In a healthy economy, new filings are typically below 250,000, suggesting the labor market is tight and layoffs are low.
- The Conference Board's index of leading indicators fell 0.3 percent in April to 119.2, and followed growth of 0.1 percent in March.
- The Conference Board's index of consumer confidence fell from 108.6 to 106.4 in May. Both the current conditions and the expectations components declined for the month.
- The Institute of Supply Management index rose from 55.4 to 56.1 in May, and remains above the neutral threshold of 50.0. Supply chain disruptions continue to weigh on the industry.
- The CPI rose 0.3 percent in April and stands 8.3 percent above April of last year. Core inflation (excluding food and energy prices) rose 0.6 percent and stands 6.2 percent above a year ago.
- At its May meeting, the Federal Reserve raised the federal funds target rate by 50 basis points to the range of 0.75 to 1.0 percent. It is well communicated that there will be continued increases in the federal funds target rate in order to gain control of inflation.
- In Virginia, payroll employment rose 3.2 percent in April from April of last year. Employment in Northern Virginia rose by 3.0 percent; Hampton Roads rose 1.8 percent, and Richmond-Petersburg rose 2.1 percent. The seasonally adjusted unemployment rate was unchanged at 3.0 percent and stands 1.3 percentage points below a year ago.
- The Virginia Leading Index jumped 2.1 percent in April after rising 2.0 percent in March. Auto registrations, initial claims, and future employment improved in April, while the U.S. Leading Index declined. The indexes for all eleven metro areas increased in April.

May Revenue Collections

Total general fund revenue collections rose 9.9 percent in May compared with May of last year. However, as previously stated, given the change in the federal filing date from mid-May in 2021 back to the normal April date in 2022, total general funds, individual nonwithholding and tax refunds must be viewed on a combined basis for April and May and, when looking at them together, they grew by more than \$1.5 billion over the same period last year, an increase of 27.3 percent.

Net Individual Income Tax (68% of general fund revenues): Through May, collections of net individual income tax rose 18.9 percent from the same period last year, ahead of the annual estimate of 7.3 percent growth. 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 rose by 12.9 percent for the month. Adjusted for the extra day this year versus last year, growth was a strong eight percent. Year-to-date, collections have risen 9.7 percent from the same period last year, ahead of the annual estimate of 9.0 percent growth.

Individual Income Tax Nonwithholding (20% of general fund revenues): May is typically a significant month for collections in this source, with final payments for tax year 2021 and the first estimated payment for tax year 2022 both due May 1. Collections in nonwithholding were \$1.47 billion compared with \$1.50 billion in May of last year, a decrease of 2.3 percent. Comparing April and May combined collections this year to April and May collections last year, nonwithholding collections grew \$1.23 billion or 51.2 percent. Year-to-date, collections grew by 33.1 percent, ahead of the annual estimate of a 2.5 percent increase.

Individual Income Tax Refunds: The Department of Taxation issued \$138.2 million in refunds in May, compared with \$319.1 million in May of last year, a decrease of 56.7 percent. For April and May combined, refunds were down \$41.8 million, or 6.5 percent. For the filing season, TAX has issued 2.25 million refunds, compared with 2.35 million last year. On a fiscal year basis, TAX has issued \$1.7 billion in refunds through May compared with \$1.8 billion through the same period last year, a decline of 8.8 percent.

Sales Tax (17% of general fund revenues): Collections of sales and use taxes, reflecting April sales, rose 8.6 percent in May. On a year-to-date basis, collections of sales and use taxes have risen 13.8 percent, ahead of the annual estimate of 11.4 percent growth.

Corporate Income Tax (7% of general fund revenues): May is not typically a significant month for collections in this source, as final or extension payments are mainly due only from retailers who usually have a January 31 close to their fiscal year. Such payments vary significantly from year to year. Collections of corporate income taxes were \$52.2 million in May, compared with receipts of \$82.3 million in May of last year. On a year-to-date basis, collections have increased 32.7 percent compared with the forecast of 32.6 percent growth.

Wills, Suits, Deeds, Contracts (2% of general fund revenues): Collections of wills, suits, deeds, and contracts – mainly recordation tax collections – were \$58.2 million in May, compared with

\$57.9 million in May of last year, rising by 0.6 percent. On a year-to-date basis, collections are down 2.4 percent, ahead of the annual forecast of a 4.3 percent decline.

Insurance Premiums (2% of general fund revenues): May is not a significant month for collections in this source. Collections were \$28.2 million compared with \$20.7 million last year. Year-to-date collections were \$296.7 million through May, compared with \$242.0 million in the same period last year. Estimated payments for insurance companies are again due in June.

Other Revenue Sources

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

	<u>Year-to-Date</u>	<u>Annual Estimate</u>
Interest Income (0.4% GF revenues)	-2.4%	6.7%
ABC Taxes (1% GF revenues)	0.4%	1.4%

All Other Revenue (2% of general fund revenues): Receipts in All Other Revenue fell 3.8 percent in May, \$46.8 million compared with \$48.7 million a year ago. On a year-to-date basis, collections of All Other Revenue rose 9.5 percent from the same period last year, above the annual estimate of a 3.1 percent increase.

Summary

Total general fund revenue collections rose 9.9 percent in May compared with May of last year, driven by payroll withholding, and sales tax collections. Comparing April and May to account for the delayed filing deadline in 2021, revenues for the two months combined grew 27.3 percent over the same period last year. Additionally, fewer individual income tax refunds were issued in May as we returned to the normal federal April filing date and May 1 Virginia date as compared to last year when the filing deadline was mid-May. Comparing April and May refunds to April and May of last year, refunds decreased 6.5 percent for the two-month period.

On a fiscal year-to-date basis, total revenue collections rose 17.8 percent through May, ahead of the annual forecast of 9.2 percent growth. With one month to go, we have collected 95 percent of the total general fund revenues anticipated in the February revised forecast. Estimated payments from corporations and individuals are again due in June. Finance staff anticipate total general fund revenues will exceed the revenue projections contained in the February mid-session forecast by more than \$1.2 billion.