Minnesota
Department of Finance

October 2008

FY 2008-09 Revenues Continue to Exceed Forecast, But Economic Outlook Has Weakened

Net non-dedicated general fund revenues totaled $3.484 billion during the first quarter of fiscal 2009, $58 million (1.7 percent) more than end-of-session estimates. Individual income tax receipts, up $52 million (2.9 percent) from forecast, and corporate income tax receipts, up $23 million (11.1 percent), were the primary sources of additional revenue.

Summary of Tax Receipts
(July - September 2008)

	Estimate	Actual	Variance	Percent
	---------------- ($ in millions) ----------------			
Income	$1,801.8	$1,853.6	$51.8	2.9
Sales Tax	1,012.0	991.9	(20.1)	(2.0)
Corporate	210.6	233.3	22.8	10.8
Motor Vehicle	30.8	34.3	3.4	11.1
Other	370.6	370.9	0.3	0.1
Total	$3,425.8	$3,484.0	$58.2	1.7

Stronger than anticipated withholding tax receipts accounted for $42 million of the positive variance in the individual income tax. Minnesota withholding collections have remained strong over the past year even though employment has declined modestly. Individual estimated income tax payments also were above forecast. The generally positive news from the individual income tax was countered by very weak sales tax collections. Gross sales tax receipts in the first quarter of FY 2009 were $8 million less than in the first quarter of FY 2008. They were also $8 million less than forecast. Sales tax refunds were $12 million more than anticipated adding to the negative sales tax variance.

Net non-dedicated general fund revenues for the recently completed 2008 fiscal year are now reported to be $391 million above forecast, $2 million more than reported in July's *Economic Update*. Small reductions in corporate and sales tax receipts were more than offset by an increase in insurance gross premiums tax receipts.

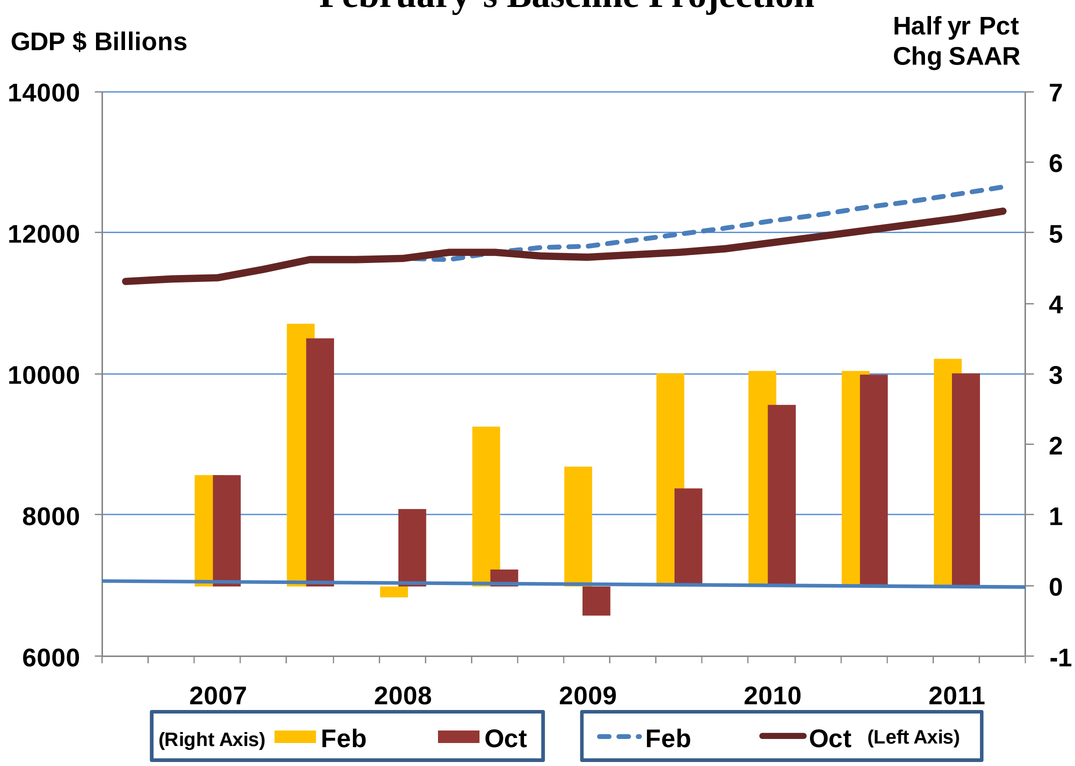
October Baseline Forecast Says U.S. Economy is in a Recession

The problems facing the U.S. economy have intensified since early July. Global credit markets have seized up, the U.S. unemployment rate is now 6.1 percent, payroll employment is down an additional 300,000, and consumer spending has fallen. There is now little doubt that the U.S. economy is in a recession. The only debate is over how long the recession will last and how deep it will be.

While most forecasters believe this economic downturn will be significantly more painful than the 2001 and 1990-91 recessions, the consensus (to this point) is that times will not be as difficult as in the early 1980s when the U.S. unemployment rate exceeded 10 percent for 10 consecutive months. Unless conditions in financial markets change dramatically for the better, however, this recession will be the most severe faced by U.S. residents in the past 25 years.

October's baseline forecast from Global Insight Inc (GII), Minnesota's national economic consultant, shows real GDP declining through early next spring. GII now expects real GDP to grow at a 1.5 percent annual rate in 2008 but at only a 0.2 percent rate in 2009. Their February baseline forecast called for real growth rates of 1.4 percent and 2.2 percent. While the economy was stronger than projected during the first half of 2008, a much weaker economy is expected for the remainder of 2008 and all of 2009. Global Insight also notes, "Since our (*October*) forecast was concluded conditions in the financial markets have worsened even more dramatically."

Real GDP Now Expected To Fall Well Below February's Baseline Projection



Global Insight assigns a probability of 60 percent to the baseline forecast. A more pessimistic scenario in which economic growth falls by 2 percent in 2009 is assigned a probability of 25 percent. A more optimistic scenario in which the economy declines only in the fourth quarter of 2008 is assigned a probability of 15 percent.

Financial Sector Provides 6 percent of Minnesota Payroll Employment.

Minnesota is a regional financial center and the finance and insurance industry is an important contributor to the state's economy. Recent news about problems faced by the global financial sector has raised questions about the extent of the direct impact of that sector in Minnesota. In the November forecast, the direct impacts will be estimated using the Department of Management and Budget's model of the Minnesota economy. That model predicts Minnesota employment, wages, and bonuses for the financial sector based on Global Insight's national baseline forecast.

Nearly 138,000 Minnesotans were employed in that sector in the first quarter of 2008 and employment in the sector has been relatively constant for the last three years. About 65 percent of that employment is located in Hennepin and Ramsey Counties. While the proportion of Minnesota jobs in the financial sector exceeds the national average of 5.3 percent, we are not as dependent on that sector as Delaware, Connecticut, and New York. In Delaware, the finance and insurance sectors makes up 10.6 percent of state employment.

The financial sector has three major components—credit intermediation (banking), securities and investments, and insurance. The banking sector accounts for about 2.5 percent of employment in both Minnesota and nationally. Securities and investment firms account for about 0.75 percent of U.S. employment. In Minnesota, 0.9 percent of employment is in that sector. Insurance carriers in Minnesota account for about 2.5 percent of statewide employment, while nationally they account for 1.9 percent. Minnesota has a much heavier concentration of employment in the health and medical care insurance industry.

Wages and salaries, including bonuses, are larger in the finance and insurance sector than the statewide average. In 2007 the average weekly wage in finance and insurance was $1519, about 80 percent above the statewide average of $853. The sector accounted for 9 percent of total state wages. All three of the sub-sectors had higher wages than the statewide average. The average wage in the securities and investment sub-sector was nearly triple Minnesota's average wage in 2007.

Comparison of Actual and Estimated Non-Restricted Revenues

($ in thousands)

	2009 Fiscal Year-to-Date			Fiscal Year 2008		
	FORECAST REVENUES	ACTUAL REVENUES	VARIANCE ACT-FCST	FORECAST REVENUES	ACTUAL REVENUES	VARIANCE ACT-FCST
Individual Income Tax						
Withholding	1,441,450	1,483,327	41,877	5,988,567	6,062,705	74,138
Declarations	322,792	333,757	10,965	1,597,200	1,662,520	65,320
Miscellaneous	72,261	71,754	(507)	1,036,133	1,154,165	118,032
Gross	1,836,504	1,888,838	52,334	8,621,900	8,879,391	257,491
Refund	34,661	35,192	530	1,038,900	1,120,182	81,282
Net	1,801,843	1,853,646	51,804	7,583,000	7,759,209	176,209
Corporate & Bank Excise						
Declarations	210,453	179,571	(30,882)	916,078	955,665	39,586
Miscellaneous	29,178	88,739	59,562	198,007	250,273	52,265
Gross	239,631	268,310	28,680	1,114,085	1,205,937	91,852
Refund	29,060	34,938	5,878	213,300	185,756	(27,543)
Net	210,571	233,372	22,802	900,786	1,020,181	119,395
Sales Tax						
Gross	1,061,444	1,053,654	(7,790)	4,824,825	4,814,551	(10,274)
Refunds	49,465	61,777	12,312	249,579	243,703	(5,876)
Net	1,011,979	991,878	(20,101)	4,575,246	4,570,849	(4,398)
Motor Vehicle Sales Tax	30,838	34,264	3,426	176,465	185,820	9,355
Other Revenues:						
Estate	30,750	36,450	5,700	120,000	121,349	1,349
Liquor/Wine/Beer	14,851	14,999	148	74,205	73,108	(1,097)
Cigarette/Tobacco/Cont Sub	45,629	50,388	4,759	186,330	173,479	(12,851)
Deed and Mortgage	34,111	33,898	(212)	182,600	198,701	16,102
Insurance Gross Earnings	61,016	69,436	8,420	253,300	291,890	38,591
Lawful Gambling	10,386	8,810	(1,576)	49,966	47,939	(2,028)
Health Care Surcharge	54,018	52,888	(1,130)	210,766	214,975	4,209
Other Taxes	219	173	(47)	8,546	12,351	3,805
Statewide Property Tax	104	25	(79)	702,517	704,246	1,729
DHS SOS Collections	18,010	7,644	(10,366)	60,859	62,649	1,790
Income Tax Reciprocity	0	0	0	69,050	69,050	0
Investment Income	15,821	11,772	(4,049)	108,679	97,259	(11,420)
Tobacco Settlement	0	100	100	182,004	184,411	2,407
Departmental Earnings	48,846	49,517	671	219,000	247,927	28,927
Fines and Surcharges	16,872	16,016	(856)	76,545	81,273	4,728
Lottery Revenues	7,335	4,688	(2,647)	51,979	51,138	(840)
Revenues yet to be allocated	0	1,043	1,043	0	2	2
Residual Revenues	20,224	17,761	(2,463)	84,323	95,067	10,745
Sales Tax Rebates (all years)	0	0	0	0	0	0
County Nursing Home, Pub Hosp IGT	1,124	1,698	574	21,582	23,079	1,497
Other Subtotal	379,316	377,306	(2,010)	2,662,250	2,749,893	87,643
Other Refunds	8,745	6,451	(2,293)	52,428	49,796	(2,632)
Other Net	370,571	370,855	284	2,609,822	2,700,097	90,274
Total Gross	**3,547,732**	**3,622,373**	**74,641**	**17,399,526**	**17,835,592**	**436,066**
Total Refunds	**121,931**	**138,358**	**16,427**	**1,554,206**	**1,599,437**	**45,231**
Total Net	**3,425,801**	**3,484,015**	**58,214**	**15,845,320**	**16,236,155**	**390,835**