



ECONOMIC AND REVENUE REVIEW AND UPDATE

A BRIEFING FOR THE MONEY COMMITTEES

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TOPICS FOR DISCUSSION

OCTOBER YEAR-TO-DATE REVENUE COLLECTIONS, FISCAL YEAR 2023

ECONOMIC REVIEW

KEY DATES AND NEXT STEPS

SUMMARY

- Adjusting for timing issues and taxpayer rebates, general fund revenues grew 10.3 percent year-over-year in October. On an unadjusted basis, general fund revenues increased 3.0 percent for the month.
- Gains in nonwithholding and sales and use taxes were offset by the issuance of \$88.0 million in taxpayer rebates.
- After adjustments are made, total general fund revenues rose 8.3 percent on a fiscal year-to-date basis versus the 14.0 percent decline assumed in the current budget.
- October marks the first month in which new withholding tables were implemented to reflect the enactment of a higher standard deduction. The impact of the increased standard deduction is expected to reduce withholding by 3.5 - 4.0 percent or \$50.0 million per month starting in October.
- October is generally not a significant month for revenue collections. Regular monthly collections are due in withholding, sales taxes, and most minor sources. Individual income tax extension return processing began in October as they are due November 1.
- Aggressive actions by the Federal Reserve to halt inflation are likely to result in an economic downturn that will place meaningful risk to revenues in Q3 and Q4 of the current fiscal year.

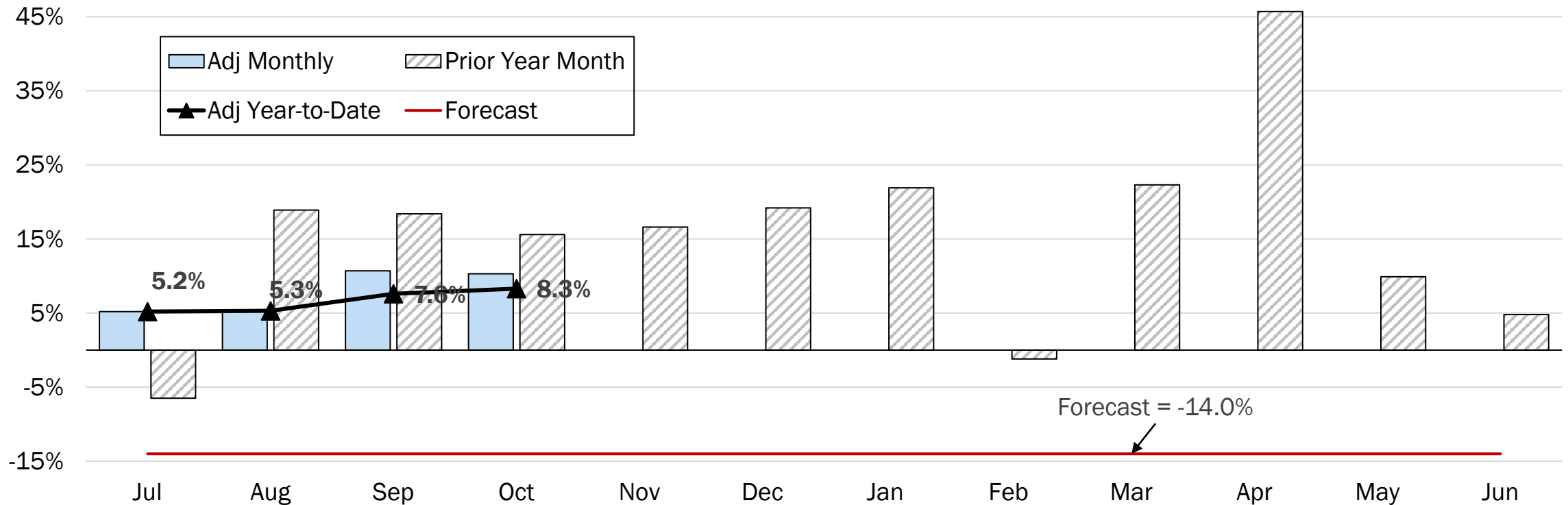
ADJUSTED FOR POLICY CHANGES, GF REVENUES WERE UP 10.3 PERCENT

General Fund Revenue Collections
(in millions of dollars)

| Revenue | FY 2023 | Pct Chg | Percent of | October | | | | Fiscal Year-To-Date | | | | Year-To-Date |
|---|-------------------|---------------|---------------|------------------|------------------|----------------|--------------|---------------------|------------------|------------------|--------------|---------------|
| | Ch 2 Estimate | Req by Est | GF Rev | FY 2022 | FY 2023 | Change | % Change | FY 2022 | FY 2023 | Change | % Change | % of Total |
| Withholding | \$15,319.9 | -0.1% | 61.6% | \$1,233.6 | \$1,285.1 | \$51.5 | 4.2% | \$4,704.4 | \$5,090.6 | \$386.2 | 8.2% | 67.3% |
| Nonwithholding | 5,213.6 | -23.4% | 21.0% | 207.6 | 283.9 | 76.3 | 36.7% | 1,070.4 | 1,211.8 | 141.4 | 13.2% | 16.0% |
| Refunds | (3,800.9) | 118.4% | -15.3% | (87.7) | (194.7) | (107.0) | 121.9% | (262.9) | (1,243.6) | (980.7) | 373.0% | -16.4% |
| Sales and Use Tax | 4,497.8 | -1.3% | 18.1% | 383.3 | 418.9 | 35.6 | 9.3% | 1,352.5 | 1,585.4 | 232.9 | 17.2% | 21.0% |
| Corporate Income Tax | 1,737.0 | -12.2% | 7.0% | 50.5 | 56.7 | 6.2 | 12.3% | 509.0 | 491.5 | (17.5) | -3.4% | 6.5% |
| All Other Sources | 1,903.9 | -4.2% | 7.7% | 98.2 | 92.6 | (5.6) | -5.7% | 434.2 | 431.7 | (2.5) | -0.6% | 5.7% |
| Total GF Revenues | \$24,871.3 | -14.0% | 100.0% | \$1,885.5 | \$1,942.5 | \$57.1 | 3.0% | \$7,807.6 | \$7,567.4 | (\$240.2) | -3.1% | 100.0% |
| Adjusted Sales | | | | | | | | \$1,555.9 | \$1,658.6 | \$102.7 | 6.6% | |
| Adjusted Withholding | | | | \$1,233.6 | \$1,335.1 | \$101.5 | 8.2% | \$4,704.4 | \$5,140.6 | \$436.2 | 9.3% | |
| Adjusted Refunds | | | | (\$87.7) | (\$106.6) | (\$18.9) | 21.6% | (\$262.9) | (\$259.7) | \$3.2 | -1.2% | |
| Total GF Revenues, Adjusted for AST, Withholding and Refunds | | | | \$1,885.5 | \$2,080.6 | \$195.1 | 10.3% | \$8,011.0 | \$8,673.6 | \$662.6 | 8.3% | |

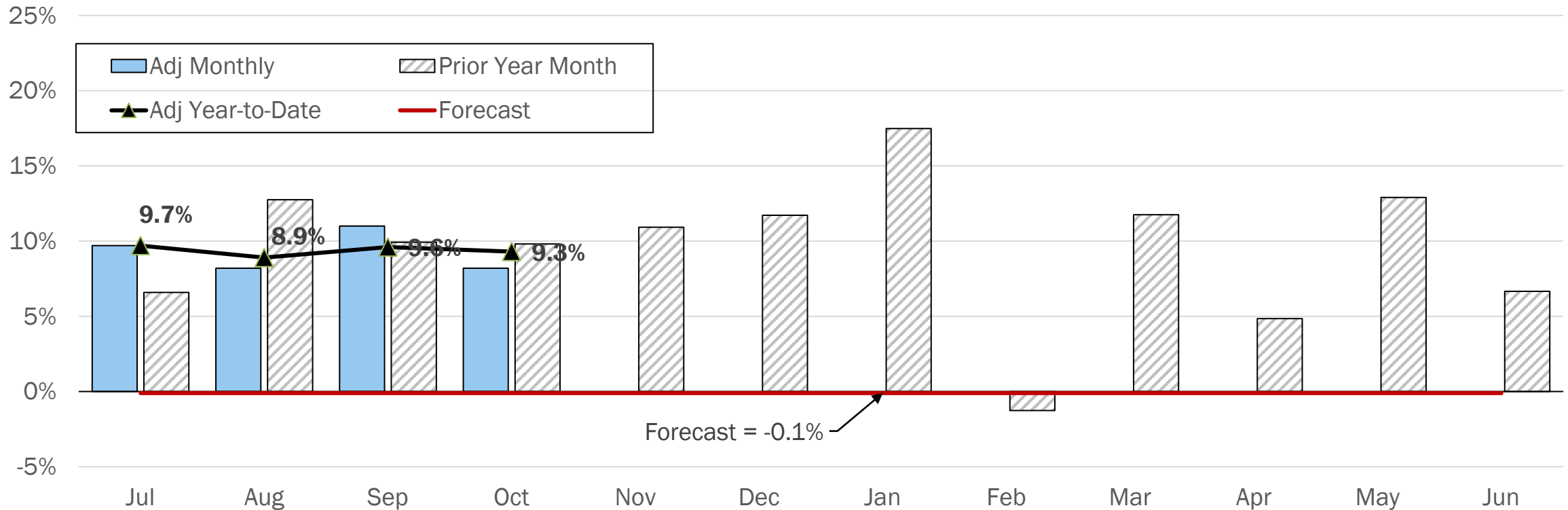
- With one-third of the fiscal year completed, general fund revenues are up 8.3 percent, adjusted for policy and timing impacts. On an unadjusted basis, total GF revenues are down 3.1 percent fiscal year-to-date, ahead of the Chapter 2 estimate of a 14 percent decline.
- Budgeted revenues are disproportionately dependent on fourth quarter collections, which account for more than a third of full-year revenues.

ADJUSTED FOR POLICY CHANGES AND TIMING ISSUES, PRELIMINARY GF REVENUES ARE UP 8.3 PERCENT THROUGH THE FIRST FOUR MONTHS OF FISCAL YEAR 2023



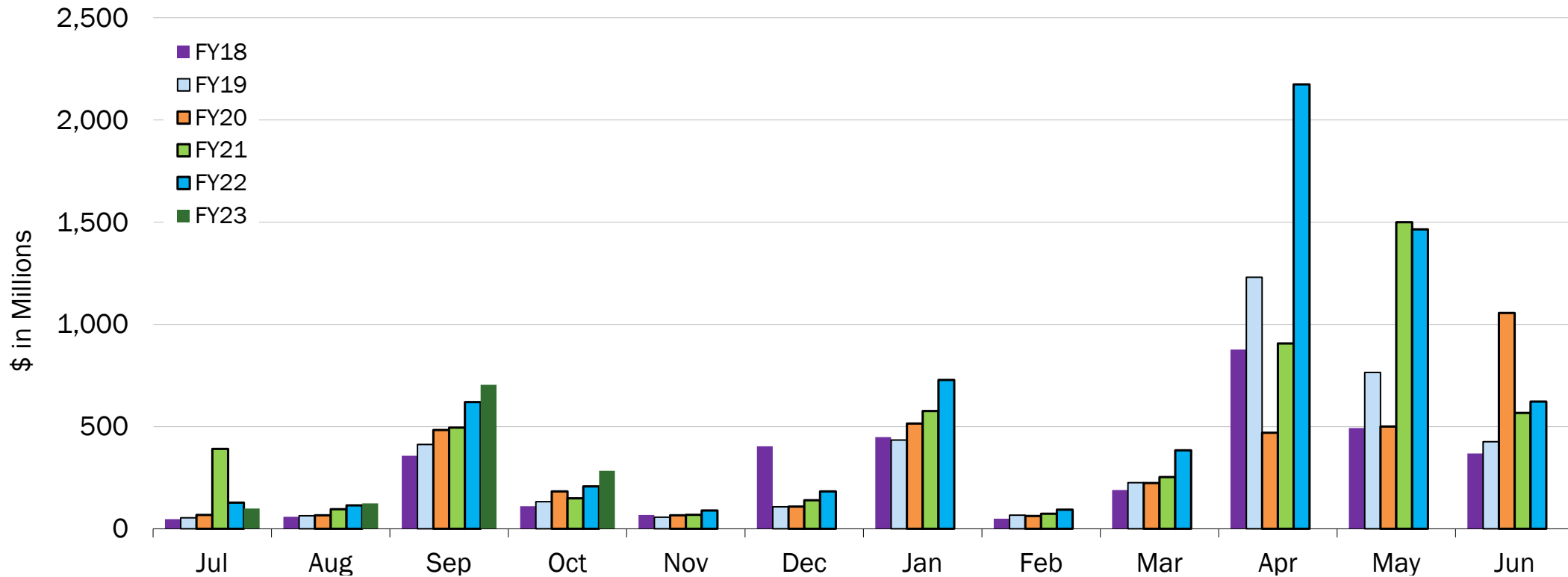
- Adjusting for AST and taxpayer rebates, total GF revenues are up 8.3 percent year-to-date.
- Coming months are expected to be more challenging as compared to prior year pandemic recovery growth rates as the impacts of inflation and aggressive Fed action take further effect.

COMPETITIVE LABOR MARKET HAS UNDERPINNED CONTINUED GROWTH IN WITHHOLDING TAX COLLECTIONS



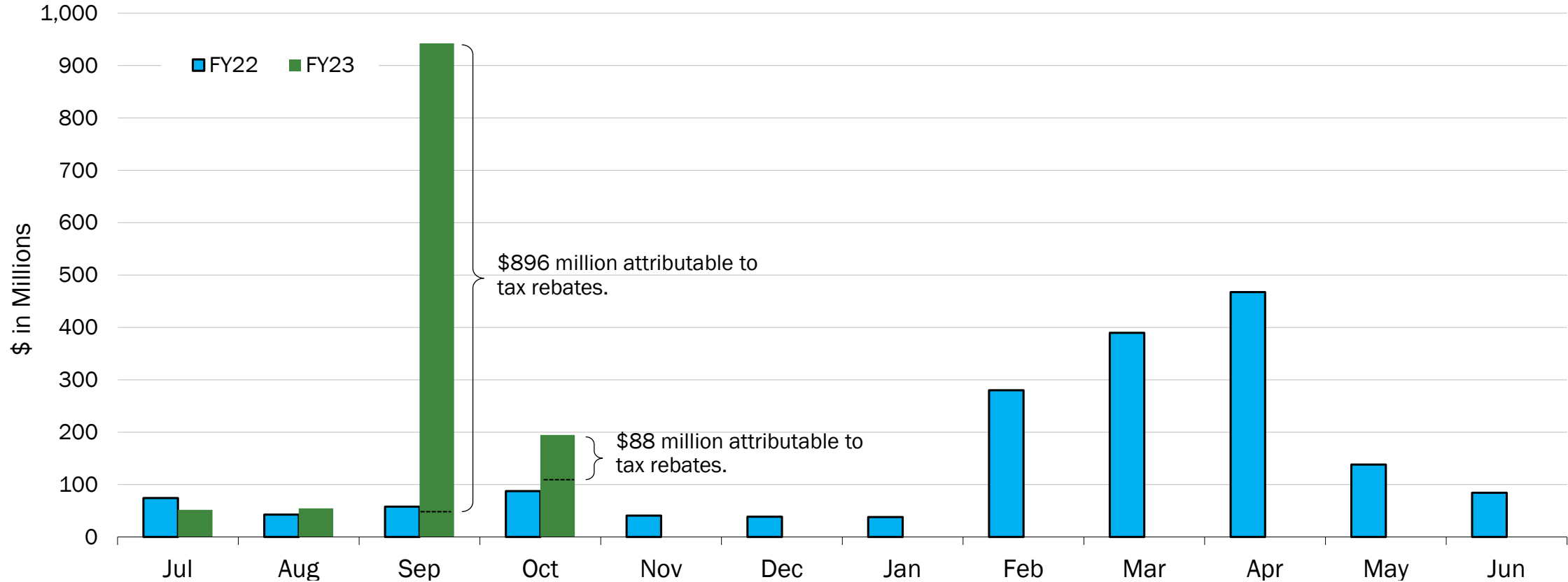
- October collections increased 4.2 percent for the month.
- Year-to-date, withholding collections have increased 8.2 percent compared with the same period last year, compared to the projected annual decline of 0.1 percent.
- Federal Reserve has indicated it is willing to sacrifice jobs to tame inflation.

NONWITHHOLDING TAX COLLECTIONS



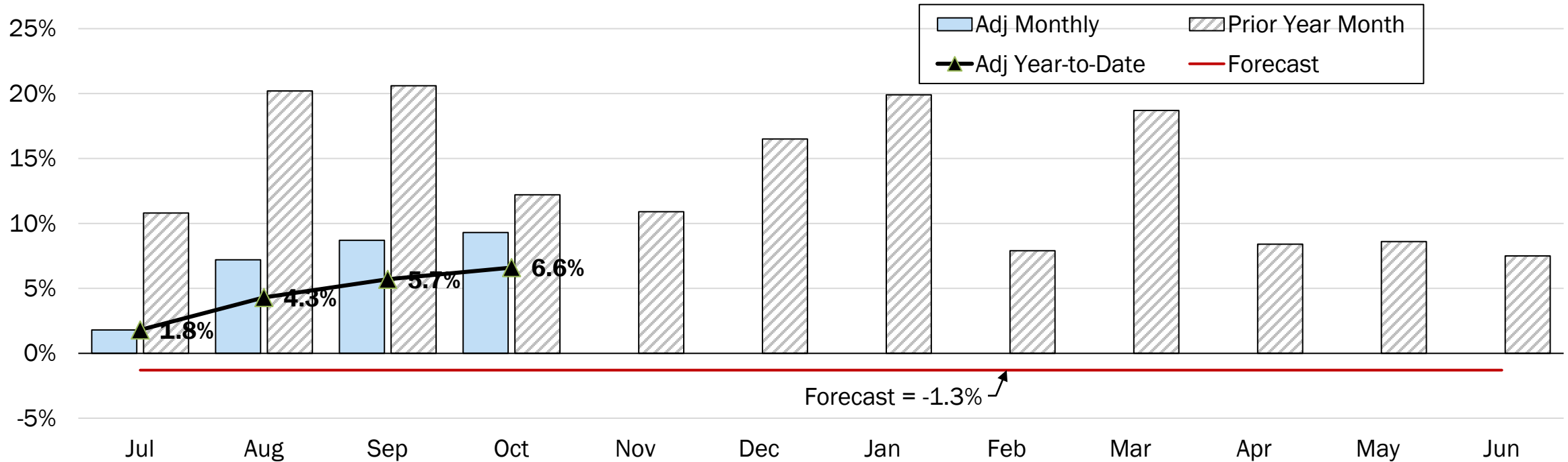
- October nonwithholding collections were \$283.9 million, up 36.7 percent above a year ago. Through the first four months of the fiscal year, collections were \$1,211.8 million compared with \$1,070.4 million a year ago, a 13.2 percent gain.
- Estimated payments YTD are based on safe harbor provisions linked to last year’s tax liability. Taxpayers reconcile their liability in April or November of the following year. YTD collections reflect the stock market’s strong performance of 2021 and not this year’s downturn.
- “Fed put” has been taken away.
- \$4.3 billion, or 63 percent of FY 2022 nonwithholding revenues, was collected in Q4 of FY 2022.

INCOME TAX REFUNDS



- Income tax refunds normally run close to \$55 million in September; however, this September was much higher at \$942.5 million, due to the issuance of \$895.9 million of taxpayer rebates.
- Typically, October income tax refunds run close to \$93 million; however, this October came in at \$283.9 million, due to the issuance of \$88.0 million of taxpayer rebates.

SALES TAX COLLECTIONS WERE UP 9.3 PERCENT FOR THE MONTH



- Adjusted for AST, fiscal year-to-date collections grew 6.6 percent.
- Sales tax increases continue to be driven by higher inflation as well as the continued post-pandemic rebound in the accommodation sectors of the economy which increased 9.6 percent year-over-year in September.
- Consumer demand is expected to weaken as the economy softens and jobs/wages come under pressure.

OTHER SOURCES

Net Corporate Income Tax

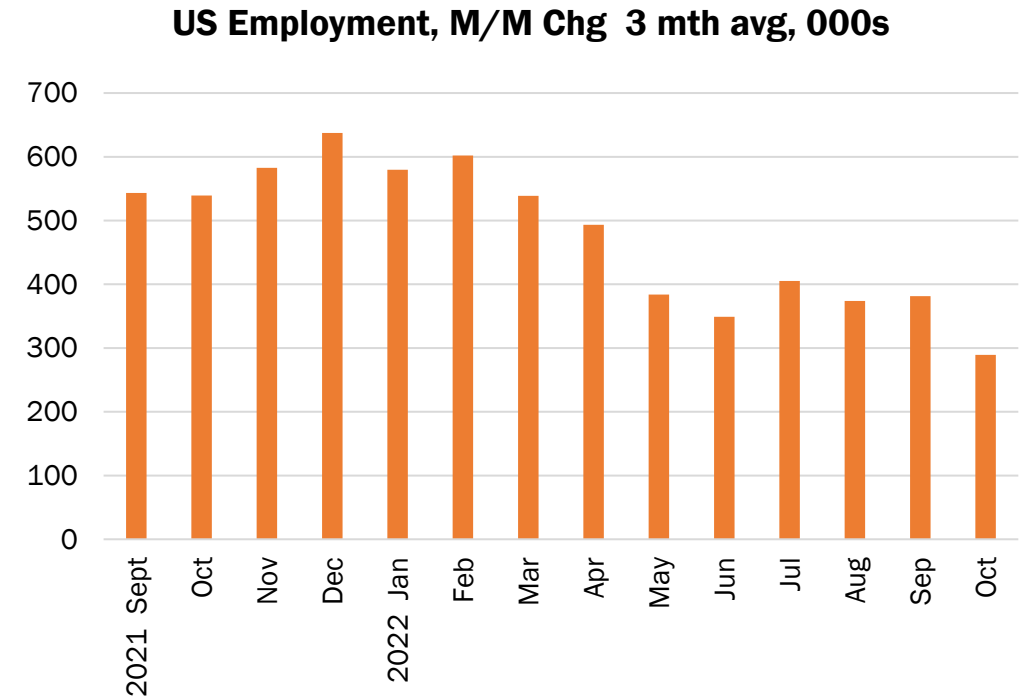
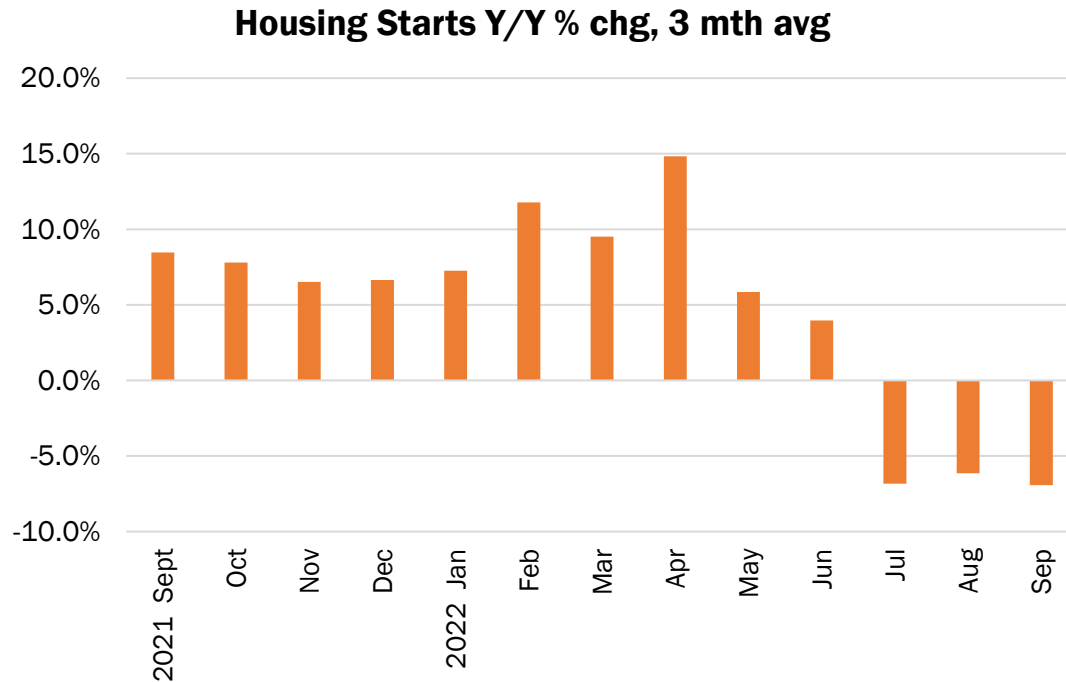
- October collections were up 12.2 percent for the month.
- Through October, collections for corporate income taxes were \$491.5 million compared with \$509.0 million in the same period last year, a decrease of 3.4 percent.
- Corporate profits will be under pressure as demand drops.

Recordation

- In October, collections decreased 36.2 percent compared to last year.
- YTD collections have decreased 27.7 percent compared to last year, behind the forecast for a 9.2 percent decline.
- Higher interest rates will continue to depress real estate transactions.

US CURRENT ECONOMIC CONDITIONS

Some signs of slowing growth

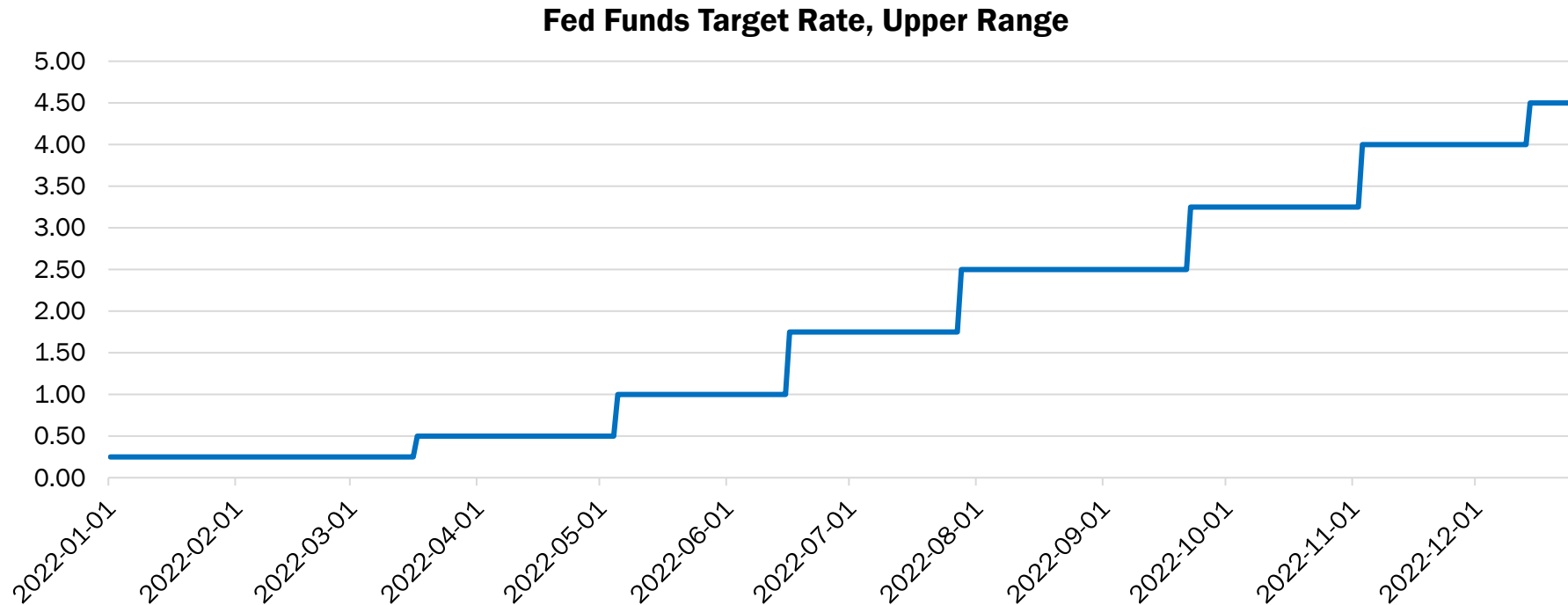


- Interest rate sensitive sectors of economy have already been impacted by recent Fed hikes.
- Labor markets are beginning to soften though not as quickly as anticipated.

Source: U.S. Census Bureau; Bureau of Labor Statistics.

FED POLICY

Further slowing in the economy is expected to occur in 2023-2024 as the impact of aggressive Fed rate hikes takes hold

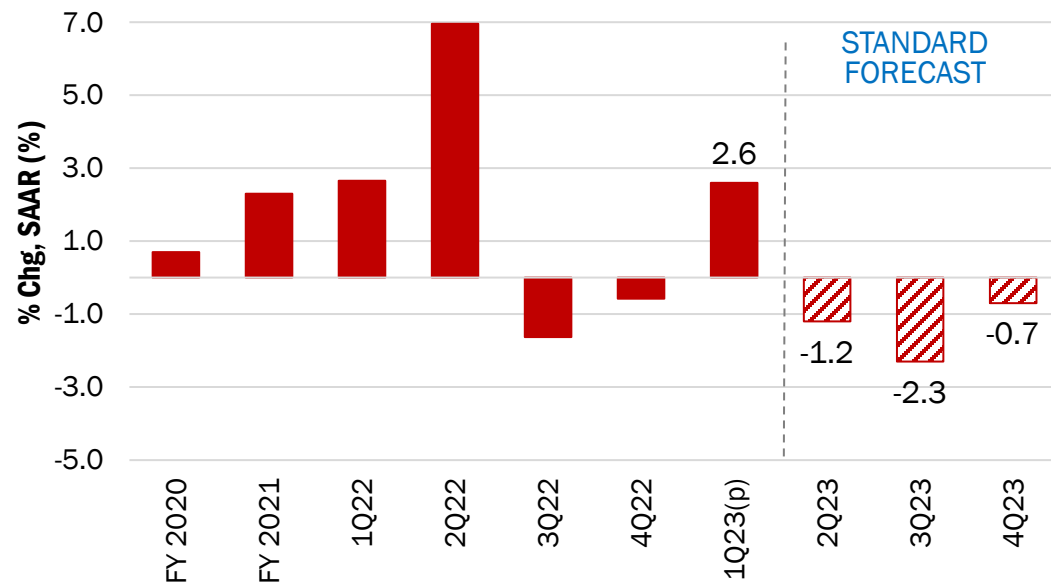


- A 50-basis point rate hike is still the consensus estimate for the December meeting.
- Some market observers project a 6 percent federal funds rate before rate hikes are through.

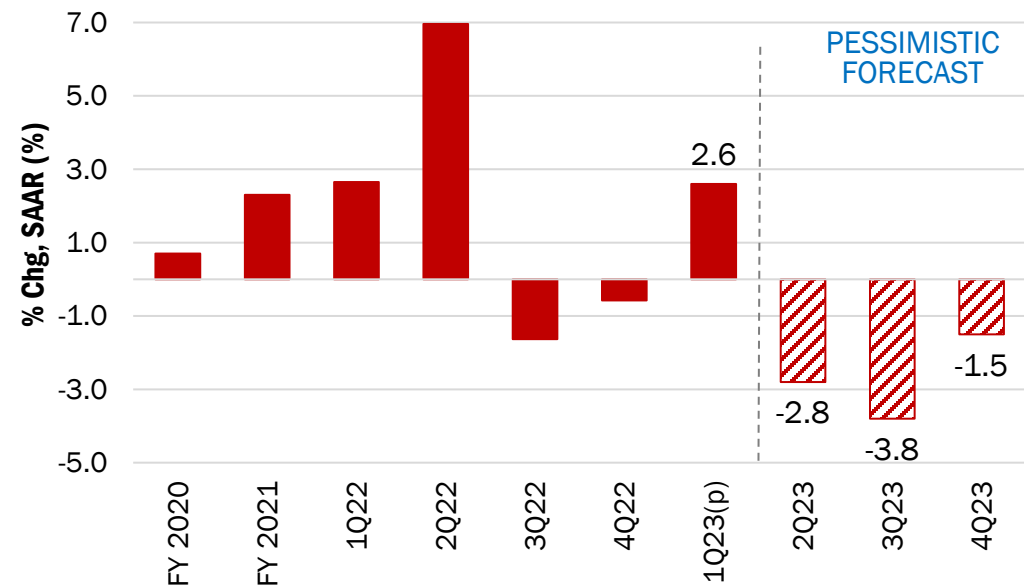
US CURRENT ECONOMIC CONDITIONS

U.S. recession risk continues to grow

U.S. Real GDP Growth Forecast, State Fiscal Quarter
IHS Markit Standard Forecast



U.S. Real GDP Growth Forecast, State Fiscal Quarter
IHS Markit Pessimistic Forecast



- The IHS October forecast anticipates a recession in the current fiscal year, with growth resuming in FY 2024.

Source: IHS Markit, October Forecast.

CONCLUSION

- Adjusting for the taxpayer rebates, general fund revenues grew 10.3 percent. On an unadjusted basis, October year-over-year General Fund revenues increased 3.0 percent for the month.
- Adjusting for taxpayer rebates, the AST and the new withholding tables, total general fund revenues rose by 8.3 percent on a fiscal year-to-date basis versus the 14.0 percent decline assumed in the current budget.
- Unadjusted withholding collections reflect the impact of the increase in the standard deduction, but on an adjusted basis, collections currently are growing.
- Healthy consumer balance sheets have supported year-over-year growth in sales tax collections to date, but the impact of sustained inflation and aggressive Fed actions are expected to reduce demand and jobs.
- Nationally, employment growth has begun to slow and Fed policy impacts are evident and growing.
- Changing economic conditions, Fed policy, and geopolitical risks are heightening our concerns about growth in the second half of the fiscal year. 63 percent of nonwithholding revenues, and 36 percent of total GF revenues were collected in the fourth quarter of FY 2022.
- The revenue forecast will be adjusted to account for current trends with the advice of the Joint Advisory Board of Economists and the Governor's Advisory Council on Revenue Estimates.

KEY DATES AND NEXT STEPS

- **November 1:** Individual income tax extension returns due.
- **November 21:** Governor's Advisory Council on Revenue Estimates (GACRE) reviews revenue outlook for the 2022 - 2024 biennium.
- **December 15:** General Fund revenue forecast finalized; Governor Youngkin's amendments to the 2022 - 2024 biennial budget are presented at the Joint Money Committee meeting.