COMMONWEALTH of VIRGINIA

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MEMORANDUM

TO: The Honorable Glenn Youngkin

THROUGH: The Honorable John Littel

FROM: Stephen E. Cummings

SUBJECT: August Revenue Report

August consists mainly of payroll withholding and sales tax collections and generally is not a significant month for other sources such as corporate income, nonwithholding taxes, and refunds. The first quarterly estimated payments from individuals and corporations are due in September which will provide a better indicator of general fund revenue trends.

This month's revenue report compares actual collections to the official revenue forecast for Fiscal Year 2025 assumed in the 2024 Appropriation Act, Chapter 2, 2024 Special Session I, adopted on May 13, 2024. The Fiscal Year 2025 revenue forecast reflects the economic and revenue outlooks developed in the fall of 2023 which anticipated a mild recession in the second half of Fiscal Year 2024. The forecast is unchanged except for minor adjustments directly tied to legislative actions adopted during the 2024 regular and special legislative sessions.

Despite having one fewer deposit day than in August of last year, total general fund revenues increased 2.0 percent ($38.2 million) for the month versus the same period last year. The year-over-year increase was driven primarily by higher individual income tax nonwithholding payments and lower individual income tax refunds. The positive year-over-year variance was partially offset by lower net corporate income tax collections and lower payroll withholding collections. On a year-to-date basis, general fund revenues increased 8.0 percent ($303.3 million) through the first two months of Fiscal Year 2025.

Among the major revenue sources, payroll withholding collections decreased 1.3 percent ($17.9 million) for the month compared to last year, reflecting the impact of fewer deposit days relative to last year. Year-to-date, withholding revenue is up 6.1 percent ($158.3 million) versus last year. Nonwithholding collections increased by 53.4 percent ($63.0 million) compared to August last year, and refunds were down 10.6 percent ($14.0 million). Net corporate income tax collections were negative $15.2 million for the month of August, reflecting refund activity in a month when few corporate taxpayers submit estimated payments. On a year-to-date basis, corporate income tax revenues are 63.4 percent below last year ($67.2 million). Sales and use tax revenues were up 1.8 percent ($7.1 million) versus last August. General fund interest income was essentially flat to last year at $97.0 million in August.

Compared to the official forecast assumed in Chapter 2 and accounting for monthly variations in tax collections, revenues exceeded projections for the month by 6.2 percent ($114.0 million) and are ahead of forecast by 5.3 percent ($205.7 million) year-to-date. Excluding nonwithholding and refunds, year-to-date collections in core revenue sources are ahead of the forecast by 3.9 percent ($150.0 million).

Withholding revenues exceeded projections by 10.2 percent ($123.6 million) in August and are ahead of the official forecast by 6.1 percent ($157.8 million) year-to-date. Corporate tax collections were below forecast for the month of August by $39.2 million and are $43.9 million below projections year-to-date. Sales tax revenues, reflecting July sales, were higher than projections by 2.3 percent ($8.9 million) and are ahead of forecast by 2.7 percent ($21.1 million) on a year-to-date basis. Wills, Suits, and Deeds (mainly recordation) revenues were essentially flat to last year in August and are below projections for the year by 4.6 percent ($3.9 million).

Collections from other sources of revenues are discussed in more detail in the following sections.

Economic Review

- U.S. real GDP growth for the second quarter of 2024 was revised upward from an annual rate of 2.8 percent to 3.0 percent according to the ‘second’ estimate released by the Bureau of Economic Analysis in August. In the first quarter, real GDP increased 1.4 percent. The increase in the second quarter primarily reflected increases in consumer spending, private inventory investment, and nonresidential fixed investment.

- In August, the University of Michigan’s U.S. Consumer Sentiment Index rose by 1.5 points to 67.9, a 2.3 percent month-over-month rise. Compared to the same period last year, the index was down 2.2 percent.

- Inflation is nearing the Fed’s target. The twelve-month percentage increase in the Consumer Price Index (CPI) for all items fell from 2.9 percent in July to 2.5 percent in August, the lowest point since early 2021. The year-over-year percentage increase in “core” CPI, which excludes food and energy, remained unchanged at 3.2 percent. The twelve-month percentage change in the “core” Personal Consumption Expenditure Price Index, the Fed’s preferred inflation measure, remained unchanged at 2.6 percent in the most recent reading for July.

- The Fed is widely expected to lower rates at the September 17-18 meeting. In recent remarks, Federal Reserve Chair Jerome Powell expressed confidence that inflation is within reach of the central bank’s 2-percent target, suggested that rate cuts are imminent, and emphasized the Fed’s intent to focus on maintaining a strong labor market.

- Employment growth continues to slow. U.S. nonfarm payroll employment increased by 142,000 in August, and the unemployment rate edged down slightly from 4.3 percent to 4.2 percent. Employment growth in August was in line with average job growth in recent months but was below the average monthly gain of 202,000 over the prior 12 months. The largest gains were in leisure and hospitality (+46,000), construction (+34,000), and health care (+31,000). The largest decline was in manufacturing (-24,000). The June estimate was revised down by 61,000, from +179,000 to +118,000, and the change for July was revised down by 25,000, from +114,000 to +89,000.

- Job openings took a further step back in July, falling from a downwardly revised 7.9 million in June to 7.7 million in July. Openings are at their lowest level since January 2021 and have been on a clearly downward trend for two years.

- In July, the most recent month for which data are available, Virginia's nonagricultural employment, from the monthly establishment survey, increased by 4,800 from June to July. Compared to July of last year, Virginia employment was 2.0 percent higher. June's preliminary estimate was revised downward by 9,500. Virginia's unemployment rate in July remained unchanged at 2.7 percent August employment data for Virginia will be released later this month.

- Virginia housing market improved modestly in July. There were 9,947 homes sold statewide in July 2024, 962 more than a year ago, a 10.7% increase. The increase in sales reflects the improvement in mortgage rates and more supply in the market. The statewide median sales price was $426,000, a 6.5% increase from July of last year.

- Congress returned to session last week to consider a potential short-term continuing resolution before the end of the federal fiscal year on September 30. The federal government may face a temporary shutdown if no agreement is reached.

August Revenue Collections

General fund revenues increased 2.0 percent year-over-year for the month of August. Fiscal year-to-date through August 31, general fund revenues are up 8.0 percent over the prior year.

Net Individual Income Tax (67% of FY 2025 general fund revenues): Revenues increased 4.4 percent ($59.1 million) for the month compared to last year. Year-to-date net individual income tax collections are up 12.5 percent ($313.1 million). Compared to the forecast, year-to-date net individual income tax collections are ahead of projections by 8.2 percent ($213.4 million), driven mainly by higher-than-forecasted withholding and nonwithholding receipts.

Performance in each component of individual income tax is as follows:

> ***Individual Income Tax Withholding (58% of FY 2025 general fund revenues)***: With one fewer deposit day this month, collections of payroll withholding taxes were 1.3 percent lower ($17.9 million) for the month compared to last August, but ahead of projections by 10.2 percent ($123.6 million). Withholding collections are up 6.1 percent year-to-date and ahead of projections by $157.8 million year-to-date.
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> ***Individual Income Tax Nonwithholding (20% of FY 2025 general fund revenues)***: August collections increased 53.4 percent ($63.0 million) year-over-year and are up 31.4 percent

($69.4 million) for the year. August is not a significant month for this source and typically accounts for less than two percent of full year collections. Through August 31, nonwithholding receipts are 52.6 percent ($100.1 million) ahead of forecast.

Individual Income Tax Refunds (-11% of FY 2025 general fund revenues): During the month of August, refunds totaled $117.9 million versus $132.0 million last August, a decline of 10.6 percent. August is not a significant month for individual income tax refunds, normally accounting for two to three percent of the full year total. Year-to-date, the Department of Taxation has issued $213.3 million in refunds compared with $298.6 million over the same period last year, a decrease of 28.6 percent.

Sales Tax (16% of FY 2025 general fund revenues): Collections of sales and use taxes, reflecting July sales, increased 1.8 percent ($7.1 million) in August and are up 2.2 percent ($17.4 million) year-to-date. Fiscal-year-to-date, sales and use tax revenues are 2.7 percent ($21.1 million) above projections.

Corporate Income Tax (7% of FY 2025 general fund revenues): Net corporate income tax collections were negative $15.2 million in August, reflecting refund activity in a month when few corporate taxpayers submit estimated payments. August is not a significant month for this source and typically accounts for approximately one percent of full year collections. On a year-to-date basis, corporate income tax revenues are 63.4 percent ($67.2 million) below last year and 53.1 percent ($43.9 million) below the forecast assumed in the current appropriations act.

Wills, Suits, Deeds, Contracts (2% of FY 2025 general fund revenues): Collections of wills, suits, deeds, and contracts – mainly recordation tax collections – were 0.1 percent lower in August compared to the previous year. On a fiscal-year-to-date basis, collections are up 9.4 percent ($7.0 million). Compared to the forecast, collections in this source are behind projections by 4.6 percent ($3.9 million).

Insurance Premiums (2% of FY 2025 general fund revenues): Monthly collections of insurance company premiums license taxes are being transferred to the Commonwealth Transportation Fund per Chapter 986, 2007 Acts of the Assembly, until the required amount of $228.7 million has been deposited.

Other Revenue Sources

The following provides growth data on collections through August for other revenue sources:

	Year-to-Date	**Annual Estimate**
Interest Income (3% of FY 2025 GF revenues)	(6.1%)	3.5%
ABC Taxes (1% of FY 2025 GF revenues)	(30.4%)	7.3%

General fund interest income totaled $211.1 million through August compared to $224.9 million for the same period of the prior fiscal year. Interest is earned monthly in the general fund and credited to nongeneral funds on a quarterly basis in October, January, April, and June.

All Other Revenue (2% of FY 2025 general fund revenues): On a year-to-date basis, collections of All Other Revenue increased by 77.0 percent to $114.3 million fiscal year-to-date compared with $64.6 million a year ago.

Summary

July and August are not significant months for revenue collections, with collections mainly from withholding, sales taxes, and other sources that have regular monthly payments.

Through the first two months of Fiscal Year 2025, general fund revenues are up 8.0 percent year-over-year, driven mainly by growth in individual income and sales tax receipts. Relative to the official forecast developed in the fall of 2023, which is predicated on the assumption of a mild recession in Calendar Year 2024 that has not materialized, revenues to date are $205.7 higher than projected.

The ongoing strength of the Virginia economy indicated by a strong labor market, strong consumer spending and better than forecasted nonwithholding revenues support a positive near-term outlook for revenues. Additionally, inflation is moderating while the U.S. job market continues to slow. The Fed has indicated confidence that inflation is under control, and the primary focus is shifting to maintaining a healthy labor market where there are signs of weakness. In response, the Fed has signaled that rates may be reduced in their upcoming September meeting.

While it is expected that the Fed will begin to lower rates, broader economic risks remain, including the potential for a weaker than expected job market, geopolitical concerns, and the possibility of federal government dysfunction. These risks and the upcoming elections, which will have a significant impact on the outlook for our economy, will be reflected in the December forecast.