



COMMONWEALTH of VIRGINIA

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MEMORANDUM

TO: The Honorable Glenn Youngkin

THROUGH: The Honorable John Littel

FROM: Stephen E. Cummings

SUBJECT: October Revenue Report

October collections consist 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.

Year-to-date general fund revenues are ahead of last year by 8.6 percent (\$731.8 million), driven by a year-over-year increase in net individual income taxes of 14.2 percent (\$809.8 million). These gains are tempered by a decline in net corporate income tax, which is down 24.6 percent (\$150.5 million) year-to-date. Other revenue sources were modestly higher than last year on a year-to-date basis.

For the month of October, revenues increased 4.1 percent (\$75.4 million) compared to the same month last year. The primary driver of the gain was payroll withholding taxes which grew 17.0 percent (\$223.9 million) year-over-year and included an additional deposit day. The increase was partially offset by year-over-year declines in corporate income tax revenues of 43.3 percent (\$41.3 million), a decline in net interest income of \$31.7 million, and a decline in sales tax revenues of 2.8 percent (\$11.1 million).

Compared to the official forecast assumed in the current appropriations act (Chapter 2) and accounting for monthly variations in tax collections, revenues fell short of projections for the month by 9.3 percent (\$198.2 million). October's variance mainly reflects the timing of payments and refunds and is not indicative of a shift in underlying economic fundamentals. Fiscal year-to-date, general fund revenues are ahead of forecast by 4.6 percent (\$403.3 million). Compared to the

year-to-date forecast, nonwithholding revenues are up 42.0 percent (\$467.3 million), withholding revenues are up 4.5 percent (\$238.2 million), and sales and use taxes are up 0.9 percent (\$14.0 million). Corporate tax collections were above forecast for the month of October by 152.7 percent (\$32.7 million) but are 11.0 percent (\$56.8 million) below projections year-to-date.

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

Economic Review

- The U.S. economy continues to grow. Real GDP rose at an annual rate of 2.8 percent in the third quarter of calendar year 2024, just shy of the 3.0 percent annualized growth experienced in the second quarter. The largest positive contributor to growth in the third quarter came from personal consumption.
- During its September meeting, the Federal Reserve lowered the target for the federal funds rate for the first time since March 2020, to a range of 4.75% to 5.0%, a 50 basis-point cut citing progress on lowering inflation, regulating the job market, and an overall expansion of economic activity. This was followed in November with a 25 basis-point cut, bringing the federal funds rate to a target range of 4.50% to 4.75%.
- In October, the Consumer Price Index (CPI) was up 2.6 percent year-over-year, up slightly from September's reading of 2.4 percent. Core CPI, which excluded food and energy, rose 3.3 percent over the last 12 months which was unchanged from September.
- The Federal Reserve's preferred inflation measure, the year-over-year change in the personal consumption expenditure (PCE) price index fell from 2.3 percent to 2.1 percent in September, versus the Fed's 2-percent target. The 12-month change in the Core PCE was unchanged at 2.7 percent.
- U.S. payroll employment rose by 12,000 for October, weighed down by the impacts of hurricanes Helene and Milton, and the now-ended Boeing strike.
- The U.S. unemployment rate climbed to 4.1 percent in October as both the labor force and employment dropped.
- In September, payroll employment in Virginia was 1.5 percent higher than prior year. Total nonagricultural employment, from the monthly establishment survey increased month-over-month by 2,100 to 4.25 million. Private sector employment increased by 1,200 while government employment increased by 900. The largest job gains occurred in Leisure and Hospitality (+2,200) and Professional and Business Services (+1,100).
- Virginia's unemployment rate increased slightly to 2.9 percent in September, 1.2 percentage points below the nationwide rate.

October Revenue Collections

General fund revenues grew by 4.1 percent (\$75.4 million) for the month of October. Year-to-date, general fund revenues are up 8.6 percent (\$731.8 million) over the prior year. Revenues are ahead of the forecast assumed in Chapter 2 by 4.6 percent (\$403.3 million) year-to-date.

Net Individual Income Tax (67% of general fund revenues): Revenues grew by 11.3 percent (\$147.9 million) for the month compared to last year. Year-to-date net individual income tax collections are up 14.2 percent (\$809.8 million). Compared to the forecast assumed in Chapter 2, year-to-date net individual income tax collections are ahead of projections by 7.2 percent (\$439.2 million), driven by better-than-forecasted withholding and non-withholding receipts.

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

Individual Income Tax Withholding (58% of FY 2025 general fund revenues): Collections of payroll withholding taxes increased 17.0 percent (\$223.9 million) for the month compared to October last year, driven partially by having one additional deposit day compared to last October. Fiscal-year-to-date, collections are 8.4 percent (\$434.2 million) higher than the same period last year. Compared to the Forecast assumed in Chapter 2, withholding revenues are ahead by 4.5 percent (\$238.2 million) year-to-date.

Individual Income Tax Non-withholding (20% of FY 2025 general fund revenues): October is not a significant month for non-withholding receipts. October collections decreased by 20.2 percent (\$58.8 million) compared to October of last year but are up 22.3 percent (\$288.1 million) year-to-date. Through the first four months of the fiscal year, non-withholding receipts are 42.0 percent (\$467.3 million) ahead of the Chapter 2 forecast.

Individual Income Tax Refunds (-11% of FY 2025 general fund revenues): In October, individual income tax refunds were up 5.8 percent (\$17.3 million). Compared to the Chapter 2 forecast, individual tax refunds were up 119.6 percent (\$170.2 million). This overperformance relative to the forecast is a result of retroactive tax year 2021 Pass-Through Entity Tax (PTET) payments increasing non-withholding revenues in September, which will lead to greater refunds through the rest of the fiscal year.

Sales Tax (16% of FY 2025 general fund revenues): Collections of sales and use taxes, reflecting September sales, declined by 2.8 percent (\$11.1 million) in October but are up 0.4 percent (\$6.5 million) year-to-date. Collections are 0.9 percent (\$14.0 million) higher year-to-date, compared to the forecast assumed in Chapter 2.

Corporate Income Tax (7% of FY 2025 general fund revenues): October collections decreased by 43.3 percent (\$41.3 million) and year-to-date declined 24.6 percent (\$150.5 million). Compared to forecast, corporate income tax collections are below expectations by 11.0 percent (\$56.8 million) year-to-date.

Wills, Suits, Deeds, Contracts (2% of FY 2025 general fund revenues): Collections of wills, suits, deeds, and contracts – mainly recordation tax collections – were up 33.1 percent (\$10.5 million) in October compared to the previous year. On a fiscal-year-to-date basis, collections are up 15.6 percent (\$21.3 million). Compared to the forecast, collections of this source are behind projections by 2.7 percent (\$4.4 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 list provides growth data on collections through October for other revenue sources:

	<u>Year-to-Date</u>	<u>Annual Estimate</u>
Interest Income (2.5% GF revenues)	-3.5%	3.5%
ABC Taxes (1% GF revenues)	-18.0%	7.3%

October marks the first quarterly distribution of interest to non-general fund accounts. Net general fund interest income, after distributions, was -\$74.1 million in October, considerably lower than the -\$42.4 million last October.

All Other Revenue (2% of general fund revenues): October receipts grew by a modest 2.2 percent (\$1.2 million) compared to October last year. On a year-to-date basis, collections of All Other Revenue grew by 32.2 percent (\$54.7 million) to \$224.5 million.

Summary

Through the first four months of Fiscal Year 2025, year-to-date general fund revenues are up 8.6 percent (\$731.8 million) compared to last year and are running ahead of projections assumed in the Chapter 2 forecast by 4.6 percent (\$403.3 million). Notable deviations from projections include non-withholding receipts (up 42.0 percent), individual income tax refunds (up 69.2 percent), corporate income tax (down 11.0 percent), and interest income (down 10.2 percent).

Through the first four months of the fiscal year, the U.S. and Virginia economies remained on a growth trajectory, supported by continued, but slowing growth in the labor market, strong consumer spending, declining interest rates, and better than forecasted nonwithholding revenues. These indicators support a positive near-term outlook for revenues. Inflation has continued to moderate sufficiently to give the Federal Reserve confidence that inflation is under control and on path toward its two-percent target which has led to the Fed's second rate cut for the year, bringing the total reduction in the federal funds rate to 75 basis points for the year, with one additional 25 basis point cut expected in December.

The fall revenue forecasting season that began with a meeting of the Governor's Advisory Council on Revenue Estimates on July 31, continued with the Joint Advisory Board of Economists meeting on October 8. The second meeting of the Governor's Advisory Council on Revenue Estimates will be on November 25. A revised forecast for fiscal years 2025 and 2026 will accompany the Governor's proposed budget which will be released on December 18.