# *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

This month's revenue report incorporates changes to the official revenue forecast included in the amended FY 2024 budget, Chapter 1, 2024 Special Session I, which was signed into law on May 13th and includes an additional $546.8 million in general fund revenues anticipated to be collected in FY 2024. These revisions to the official revenue forecast reflect technical adjustments and a portion of excess revenues received through April 30. Aside from these changes, our underlying outlook for FY 2024 is unchanged. Similarly, the revenue outlook for the upcoming 2024-26 biennium remains unchanged except for adjustments directly tied to legislative actions adopted during the 2024 regular and special legislative sessions.

Year-to-date, general fund revenues are up 5.9 percent ($1.48 billion) through the first 11 months of Fiscal Year 2024 and are ahead of the revised forecast by $1.09 billion. Adjusting for the effects of the elective Pass-Through Entity Tax (PTET) collections and refunds, and the associated timing of enacted policy actions to better reflect underlying economic trends, revenue collections are up 8.8 percent year-to-date.

For the month of May, total general fund revenues increased 14.2 percent ($360.0 million) versus the same period last year and exceeded projections for the month by $394.6 million. The year-over-year increase was driven primarily by higher net individual income tax collections. The positive year-over-year variance was partially offset by lower net corporate income tax collections, primarily attributable to the timing of corporate refund issuances from prior taxable years.

Among the major revenue sources, withholding collections increased 20.9 percent ($263.2 million) for the month compared to last year. Nonwithholding collections increased by 5.1 percent ($39.5 million) compared to May last year, and refunds were down 15.7 percent ($30.2 million) compared to last year. Corporate income tax revenues declined 92.5 percent in May ($54.1 million), and sales and use tax revenues were up 2.6 percent ($10.0 million). General fund interest income was $124.7 million in May compared to $82.3 million in May 2023.

Compared to the revised forecast assumed in Chapter 1 and accounting for monthly variations in tax collections, May revenues exceeded projections by $394.6 million, and year-to-date revenues are ahead of projections by $1.09 billion. Excluding nonwithholding and refunds, year-to-date collections in core revenue sources are ahead of the revised forecast by $199.0 million, a variance of 0.9 percent.

Withholding revenues exceeded projections by 11.2 percent ($152.9 million) in May and are ahead of the revised forecast by 1.0 percent ($152.9 million) year-to-date. Corporate tax collections were below forecast for the month of May by $57.1 million are $191.3 million below projections year-to-date. Sales tax revenues, reflecting April sales, were higher than projections by 10.4 percent ($36.6 million) and are ahead of forecast by 3.9 percent ($162.1 million) on a year-to-date basis. Wills, Suits, and Deeds (mainly recordation) revenues increased year-over-year in May but are below projections for the year by 4.2 percent ($16.0 million).

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

**Economic Review**

- U.S. Real Gross Domestic Product (GDP) growth for the first quarter of 2024 was revised lower to a 1.3 percent annual rate, according to the "second" estimate released by the Bureau of Economic Analysis. In the prior estimate, the increase in real GDP was 1.6 percent. The update primarily reflected a downward revision to consumer spending from a 2.5 percent annual rate to a 2.0 annual rate.

- The University of Michigan’s Consumer Sentiment index fell by 10 percent this May to its lowest level in six months. This is following three consecutive months of very little change. Consumers expressed particular concern over labor markets and continued high interest rates.

- U.S. retail sales for April were flat month-over-month and were up 3.0 percent compared to April 2023, according to the “advance” monthly sales report published by the U.S. Census Bureau. The February to March percent change was also revised downward, from up 0.7 percent to up 0.6 percent. On a year-over-year basis, sales for non-store retailers, which includes internet sales, were up 7.5 percent in April, and sales at restaurants and bars were up 5.5 percent. The biggest year-over-year declines were in furniture stores and sporting goods and hobby stores.

- U.S. nonfarm payrolls increased by 272,000 in May, higher than the average monthly gain of 232,000 over the prior 12 months. On a year-over-year basis, May payrolls were 1.8 percent higher compared to last year. In May, employment continued to trend up in several industries, led by Health Care (+68,000); Government (+43,000); Leisure and Hospitality

(+42,000); and Professional, Scientific, and Technical Services (+32,000). The employment change for March was revised down by 5,000, and the change for April was revised down by 10,000. With these revisions, employment in March and April combined is 15,000 lower than previously reported.

- The U.S. unemployment rate changed little at 4.0 percent in May. A year earlier, the jobless rate was 3.7 percent.

- In April, Virginia's nonagricultural employment, from the monthly establishment survey, increased by 3,400 to 4,233,400, a year-over-year increase of 1.8 percent. The largest job gains occurred in Education and Health Services (+2,500) and Professional and Business Services (+1,800). In addition, March's preliminary estimate of employment was revised up by 1,700, from a 16,500 month-over-month increase to an over-the-month increase of 18,200.

- In April, Virginia's seasonally adjusted unemployment rate decreased 0.1 percentage points to 2.8 percent. The number of employed residents increased by 517 to 4,455,081, and the Commonwealth's labor force participation rate decreased by 0.1 percentage points to 66.4 percent.

- The Consumer Price Index (CPI) for all items was unchanged month-over-month in May, and the twelve-month change declined from 3.4 percent to 3.3 percent. The twelve-month change in "core" CPI, which excludes food and energy, also fell from 3.6 percent to 3.4 percent.

- The twelve-month change in the Personal Consumption Expenditure Price Index, excluding food and energy (core PCE), the Fed's preferred inflation measure, remained at 2.8 percent for the third month in a row in April, above the Fed's target of two percent.

- The Federal Reserve's Federal Open Market Committee (FOMC) left the target for the federal funds rate at a range of 5.25 percent to 5.50 percent at its June 11-12 meeting. The FOMC has kept rates steady since July 2023. The FOMC noted that there has been modest further progress toward the Fed's 2-percent inflation target, and policymakers signaled that just one rate cut was likely before year-end.

- Virginia's housing market picked up in April. The number of closed sales increased 14.1 percent year-over-year, and total dollar volume increased 22.8 percent compared to April 2023. However, while higher than last year, housing market activity remains low compared to recent years.

**May Revenue Collections**

General fund revenues increased 14.2 percent year-over-year for the month of May on an unadjusted basis. Fiscal year-to-date through May 31, general fund revenues are up 5.9 percent over the prior year.

***Net Individual Income Tax (67% of general fund revenues)***: Revenues increased 18.1 percent for the month compared to last year ($332.9 million). Year-to-date net individual income tax collections are up 6.8 percent. Compared to the forecast, year-to-date net individual income tax collections are ahead of projections by $1.05 billion, driven by higher-than-expected withholding and nonwithholding, and lower than anticipated refunds.

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

> ***Individual Income Tax Withholding (59% of general fund revenues)***: Collections of payroll withholding taxes were 20.9 percent higher for the month and up 5.5 percent year-to-date on an unadjusted basis. Compared to the revised forecast, withholding revenues are ahead by $152.9 million year-to-date.
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> ***Individual Income Tax Nonwithholding (21% of general fund revenues)***: May collections increased 5.1 percent year-over-year and are down 2.7 percent for the year, both on an unadjusted basis. Through May, nonwithholding receipts are $575.8 million ahead of forecast.
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> ***Individual Income Tax Refunds (-12% of general fund revenues)***: During the month of May, refunds totaled $162.9 million versus $193.1 million last May, a decline of 15.7 percent. Year-to-date, the Department has issued $2,879.3 million in refunds compared with $3,417.4 million over the same period last year, a decrease of 15.7 percent.

***Sales Tax (16% of general fund revenues)***: Collections of sales and use taxes, reflecting April sales, increased 2.6 percent in May and are down 0.7 percent year-to-date. Fiscal-year-to-date, sales and use tax revenues are $162.1 million above projections. Adjusting for the elimination of the State sales tax on grocery and the end of Accelerated Sales Tax, sales tax collections are up 1.3 percent year-to-date.

***Corporate Income Tax (8% of general fund revenues)***: Net corporate income tax collections were down year-over-year 92.5 percent in May. The decline is mainly attributable to the timing of the issuance of corporate income tax refunds. May is not a significant month for this source and typically accounts for less than three percent of full year collections. On a year-to-date basis, corporate income tax revenues are down 4.7 percent. Compared to the revised forecast, corporate income tax collections are below plan by $191.3 million year-to-date.

***Wills, Suits, Deeds, Contracts (2% of general fund revenues)***: Collections of wills, suits, deeds, and contracts – mainly recordation tax collections – were 11.9 percent higher in May compared to the previous year. On a fiscal-year-to-date basis, collections are down 5.4 percent. Compared to the forecast, collections in this source are behind projections by $16.0 million.

***Insurance Premiums (2% of general fund revenues)***: Year-to-date collections are up 6.1 percent versus a forecasted decline of 1.0 percent.

## Other Revenue Sources

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

| | **Year-to-Date** | **Annual Estimate** |
|---|---|---|
| Interest Income (2% GF revenues) | 96.0% | 84.2% |
| ABC Taxes (1% GF revenues) | 2.0% | 5.4% |

General fund interest income totaled $769.9 million through May compared to $392.8 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 general fund revenues)***: On a year-to-date basis, collections of All Other Revenue increased by 7.4 percent to $511.7 million fiscal year-to-date compared with $476.4 million a year ago.

**Summary**

Results to date exceed the revised forecast which reflects the changes assumed in the amended budget enacted on May 13th, including an additional $546.8 million in anticipated FY 2024 revenues.

For the month of May, total general fund revenues increased 14.2 percent versus the same period last year and exceeded projections for the month by $394.6 million. With one month remaining in FY 2024, general fund revenues are up 5.9 percent compared to last year and are running ahead of the revised official forecast by $1.09 billion, driven primarily by higher than projected net individual income tax collections.

Revenue growth has exceeded expectations throughout FY 2024, supported by stronger than expected economic fundamentals which gives us confidence in the near term. However, the path of future economic growth and resulting revenue collections will depend in large part on inflation and the Fed's efforts to bring it under control. Additionally, declining savings rates, lower consumer sentiment, and rising credit card delinquencies suggest consumer spending may weaken in coming months. Given the current interest rate environment, with inflation persisting above Fed targets and other uncertainties, our underlying outlook remains cautious.