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Missouri General Revenue Report for February, Fiscal Year 2009

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Missouri General Revenue Growth Through March Continues to be Negative for Fiscal Year 2009

Missouri General Revenue Collections, after refunds, increased 6.3 percent in March, which resulted in an overall decrease of 0.6 percent for the first nine months of State Fiscal Year 2009 (FY 2009) to date. It is important to note at the outset of this report that the March increase was due in large part to a 22 percent decline in GR refunds paid compared to March of last year. This, in turn, was the result of slower refund processing that has come about because the Department of Revenue has hired fewer seasonal tax processing workers due to budget constraints. Thus, the improvement in net GR growth seen in March is largely an administrative phenomenon.

The decline in State General Revenue (GR) over the last nine months, coupled with the generally weak economic situation, makes it clear that the state faces a very difficult budget situation now and in the foreseeable future. While there has been a scattering of positive economic developments over the last month, it seems clear nonetheless that the state should focus on maximizing the financial assistance that has become available from the Federal government so as to avoid severe cutbacks in many vital areas of the state budget.

Two of Missouri's three most significant revenue sources performed poorly in the month of March. While Sales and Use Tax staged a rally in March, gross Individual Income Tax collections fell 4.9 percent. Gross Corporate tax also fell 23.6 percent. With the March results in, it can be seen that for FY 2009 to date, gross Individual Income tax has grown only 2.2 percent. This is critical in view of the fact that Individual Income Tax collections generate about 65 percent of all state general revenue collections.

Despite the March rally, Sales and Use Tax collections have struggled over the last three months. For the quarter ending March 31st, net Sales tax collections declined 5.9 percent. This reflects both a generally weak economy and a relatively slow Christmas shopping season. Finally, State Corporate Income and Franchise Tax collections (net of refunds) have *declined* 17.7 percent overall during the first eight months of the fiscal year.

Highlights from this Report:

- Missouri's net General Revenue grew by 6.3 percent for March, resulting in a net decrease of 0.6 percent for the first nine months of Fiscal Year (FY) 2009.
- After nine months, Individual Income Tax (IIT) withholding is up 2.9 percent, despite falling 2.8 percent over the last three months.
- Despite the March rally, sluggish Sales Tax growth continues to be the main drag on overall general revenue (GR) growth. Regular sales tax has dropped 3.4 percent for the first nine months of FY 2009.
- Net Corporate Income/Franchise Tax gross collections remain slow and have declined 17.7 percent for FY 2009 thus far.
- GR Refunds fell 22.4 percent in March for administrative reasons. Substantial growth in GR Refunds over the next three months is a near certainty.

Detailed Revenue Analysis:

Missouri General Revenue (GR) collections in March of 2009 totaled \$737.7 million, 2.3 percent less than collections for March of 2008. For the month of March, General Revenue refunds fell 22.4 percent compared to March of last year. As a result, net GR in March increased 6.3 percent for the month. For FY 2009 overall, net GR collections are 0.6 percent below those of FY 2008 after nine months.

Individual Income Tax (ITT) collections fell 4.9 percent in March, but remain up 2.2 percent for FY 2009 overall. March saw Individual Income Tax (IIT) Withholding decline 4.5 percent. In a like manner, March Declarations/Estimated payments also declined about 21 percent. Nonetheless, IIT withholding is still up 2.9 percent for FY 2009 to date. There is little question that the weakness in March IIT withholding is bad news. For the quarter ending March 31st, IIT withholding is down 2.8 percent - a sharp decline from the previous quarter (See Table 2). Through March 31st, IIT Refunds are down 2.6 percent. As noted earlier, this is due to slower refund processing.

During the April through June quarter, the state will need to brace for a sharp increase in refunds along with reduced remittance payments that are likely to result from both the accumulating backlog and the stock market decline that occurred in 2008.

The recent IIT withholding collection decline was not unexpected as the latest Missouri total employment data is grim. The latest statistics, which now include February, show that Missouri is experiencing a severe decline in total employment. From February of 2008 through February of 2009, Missouri has lost over 80,000 jobs and the February Unemployment rate was 8.3 percent. Needless to say, job loss numbers of this magnitude are apt to lead to sustained weakness in withholdings over the next few months and could certainly spell more trouble on into FY 2010. (See Table 3 for Recent Trends in Missouri Employment)

The following tables examine more closely recent trends in Missouri wage and salary growth. The new 2008 4th Quarter data shows that the Missouri Wage and Salary growth rate fell rather sharply. Note that dollar amounts are in millions:

Table 1: Missouri Wage and Salary Growth

Year and Quarter MO Wages and Salaries (In Millions) Percent Change

2006 Quarter 1 \$105,836 5.8%

2006 Quarter 2	\$106,117	5.1%
2006 Quarter 3	\$106,315	3.7%
2006 Quarter 4	\$108,135	4.1%
2007 Quarter 1	\$109,919	3.9%
2007 Quarter 2	\$110,514	4.1%
2007 Quarter 3	\$111,945	5.3%
2007 Quarter 4	\$113,924	5.4%
2008 Quarter 1	\$114,820	4.6%
2008 Quarter 2	\$115,332	4.4%
2008 Quarter 3	\$115,995	3.6%
2008 Quarter 4	\$115,806	1.7%

Source: U.S. Dept of Commerce: Bureau of Economic Analysis

Table 2: Missouri Individual Income Tax Collections

Missouri Individual Income Tax Collections Growth Rates Fiscal Years 2004-2008

<u>Year and Quarter</u>	<u>Individual Income Tax Withholding Percent Change</u>
2004. Quarter 3	1.7%
2004. Quarter 4	4.7%
2005. Quarter 1	1.8%
2005. Quarter 2	6.5%
Total Fiscal Year 2005	3.6%
2005. Quarter 3	7.1%
2005. Quarter 4	6.7%
2006. Quarter 1	8.0%
2006. Quarter 2	6.2%
Total Fiscal Year 2006	7.0%
2006. Quarter 3	6.3%
2006. Quarter 4	4.4%
2007. Quarter 1	4.0%
2007. Quarter 2	6.0%
Total Fiscal Year 2007	5.1%
2007. Quarter 3	5.2%
2007. Quarter 4	8.2%
2008. Quarter 1	7.4%
2008. Quarter 2	2.8%
Total Fiscal Year 2008	6.0%
2008. Quarter 3	3.2%
2008. Quarter 4	9.0%
2009. Quarter 1	-2.8%

Source: MO Office of Administration

Table 3: Missouri Employment Trends 2004 through 2008

<u>Calendar Year</u>	<u>Total Employment</u>	<u>Unemployment Rate</u>
2004	2,813,961	5.8%
2005	2,836,354	5.4%
2006. Quarter 1	2,861,525	4.7%
2006. Quarter 2	2,869,933	4.7%
2006. Quarter 3	2,875,413	4.9%
2006. Quarter 4	2,878,462	4.9%
2007. Quarter 1	2,879,147	4.8%
2007. Quarter 2	2,878,887	4.8%
2007. Quarter 3	2,878,179	5.2%
2007. Quarter 4	2,877,381	5.3%
2008. Quarter 1	2,860,513	5.5%
2008. Quarter 2	2,849,226	5.6%
2008. Quarter 3	2,815,539	6.5%
2008. Quarter 4	2,809,126	6.8%
February 2009	2,768,707	8.3%

Source: U.S. Bureau of Labor Statistics

With the decline in withholding, the near term outlook for this tax source is not good. The sharply weakening economy, as shown with the above job loss figures, is likely to stifle growth in this tax for the rest of FY 2009 and perhaps well into FY 2010. A key to any sustained recovery in overall state GR collections will be a turnaround in this area. This is because IIT accounted for 65 percent of the Missouri GR fund in FY 2008.

Sales and Use Tax collections rose 13.3 percent in March, but have declined 4.6 percent for the first nine months of FY 2009. For these nine months, Regular Sales tax fell 3.4 percent and Motor Vehicle Sales tax fell 95 percent. (As of July 1st all MV Sales tax is being allocated to Highways and Transportation)

As regular readers of this report know, monthly Sales and Use tax growth rates of ten show substantial fluctuations that are generally not the result of economic factors. (Sales and Use tax collections in March of 2008 *fell* about 15 percent). To be sure, the March rally is welcome news, but sales tax results for the quarter ending March 31st remain grim, with Regular Sales tax down 5.2 percent for this period.

Looking for good news:

- It is noted that gasoline prices remain sharply lower than the prices seen last summer.
- Most wage/salary workers have begun to receive the benefit of higher “take home” pay as a result of the Federal Stimulus bill signed into law in February.

Other things being equal, this will leave some additional monies with consumers and may help mitigate the decline in this area. These positives, however, will probably not be sufficient to overcome the other economic negatives and return the state to a period of growth in this area. Also worth noting is that sales tax refunds rose about 20 percent in the first nine months of FY 2009.

Looking at the long term trend in Missouri sales tax collections, there can be little question that the outlook is bleak. The following summarizes sales tax collections over time:

FY 2006 - \$1,885.6

FY 2007 - \$1,889.3

FY 2008 - \$1,901.2

As indicated above, over the last three years, net sales tax has grown less than 1 percent. Looking ahead, with the economic slowdown taking hold, this is unlikely to improve.

See below for the latest quarterly trends in sales tax growth.

Table 4: Missouri Sales Tax Growth Rates Fiscal Years 2004-2008

	<u>Regular Sales Tax</u>	<u>Motor Vehicle Sales Tax</u>
2003. Quarter 3	2.5%	1.5%
2003. Quarter 4	4.8%	2.5%
2004. Quarter 1	7.9%	9.1%
2004. Quarter 2	7.2%	0.9%
Total Fiscal Year 2004	5.6%	3.3%
2004. Quarter 3	3.5%	-4.4%
2004. Quarter 4	1.3%	-3.4%
2005. Quarter 1	3.5%	-2.0%
2005. Quarter 2	5.3%	0.6%
Total Fiscal Year 2005	3.6%	-2.0%
2005. Quarter 3	3.3%	-25.8%
2005. Quarter 4	4.2%	-40.7%
2006. Quarter 1	5.3%	-38.8%
2006. Quarter 2	4.5%	-42.9%
Total Fiscal Year 2006	4.3%	-36.7%
2006. Quarter 3	1.7%	-41.3%
2006. Quarter 4	3.4%	-13.9%
2007. Quarter 1	4.9%	15.4%
2007. Quarter 4	2.6%	-6.8%
Total Fiscal Year 2007	3.2%	-14.4%
2007. Quarter 3	4.0%	-45.1%
2007. Quarter 4	-0.3%	-53.9%
2008. Quarter 1	-2.9%	-66.5%
2008. Quarter 2	-2.0%	-57.7%
Total Fiscal Year 2008	-0.4%	-56.8%
2008. Quarter 3	-2.3%	-95.8%
2008. Quarter 4	-2.5%	-94.8%
2009. Quarter 1	-5.2%	-95.9%

Corporate Income and Franchise Tax collections fell 24 percent in March, and are down 9.9 percent for FY 2009 to date. Looking at the sub-components for the first nine months of FY 2009, there is weakness in both areas. Both Declarations and Final Payments fell during the last nine months, 11.2

percent and 7.9 percent respectively. Despite the refund slowdown, corporate refunds are 6.1 percent FY 2009 to date. As a result, net corporate collections have declined 17.7 percent.

Looking ahead, FY 2009 is not likely to see strong growth in this area. In addition to the economic slowdown that is taking place, there are the bonus depreciation allowances that are part of the Federal Economic stimulus bill signed by President Bush in February of 2008. There are also probably substantial tax credits that have been issued awaiting redemption. All things considered, FY 2009 and FY 2010 may be a difficult period for this tax source.

Other Revenue Sources: Notable developments in the smaller revenue sources include:

General Revenue Interest earnings continue to decline. For FY 2009 to date, they are down about 45 percent. With interest rates extremely low, this source is not likely to generate much revenue over the coming months.

County Foreign Insurance continues to be something of a bright spot with collections up 5.1 percent for FY 2009 to date.

General Revenue Refunds: General Revenue refunds declined 22.4 percent in March, which brought the FY 2009 growth rate to 0.8 percent. As noted earlier, this decline is largely the result of a slowdown in refund processing. Individual and Corporate Income Tax refund growth is almost sure to accelerate in the remaining months of FY 2009.

Summary and Outlook

The national economy has shown some signs of life over the last month. Most notably, the stock market as measured by the *Standard and Poors 500 Stock Index* has risen about 26 percent from March 9th through April 9th. While this may signal better times ahead, there's no doubt that revenue growth in Missouri of late has generally been anemic. This lack of revenue growth, coupled with the likelihood of a struggling economy (for at least the rest of calendar year 2009), does not bode well for Missouri's near term or long term budget future. In addition to going through a full nine months with a decline in net GR (-0.6 percent), the generally unfavorable economic news seems to keep on coming, meaning the worst is probably not over. Furthermore, the sluggish collection trends mean that we have not yet felt the full force of the job losses, which have kept piling up in recent months. At this point, there seems to be little cause for optimism for FY 2009 and beyond. In addition to the struggling economy the major reasons are:

- Net GR collections declined 1.5 percent for the quarter ending March 31st, despite the refund processing delays.
- Both Sales and Use and Corporate Income/Franchise taxes (gross) declined in FY 2008 and have declined thus far in FY 2009.
- In FY 2009, the GR Fund no longer receives *any* Motor Vehicle Sales tax.
- The decline in the 2008 stock market will almost certainly lead to much reduced Missouri tax collections during the last quarter of FY 2009 that would have come from capital gains. This was a major factor in the budget shortfall seen in fiscal years 2002 and 2003.
- Employment is generally declining both at the national level and in Missouri. The national economy lost about 663,000 payroll jobs in March alone and about 5.1 million since December of 2007.
- At this juncture, Missouri and indeed the nation must hope that the Economic Stimulus bill signed into law by President Obama will be effective in bringing about an economic recovery. In view of sluggish revenue collections, Missouri policy makers would be well advised to take maximum advantage of the Federal aid that is now available.

(See next page for the March and FY 2009 General Revenue Collection table)

Table 5: March Collections and Refunds

Tax Source (\$\$\$ in Thousands)	Mar. FY 2008	Mar. FY 2009	Percent Change	FY 2008 YTD	FY 2009 YTD	Percent Change
Individual Income						
Withholding	379,411	362,286	(4.5)	3,317,552	3,414,581	2.9
Declarations	12,723	10,066	(20.9)	536,686	524,945	(2.2)
Remittances	68,052	66,148	(2.8)	191,619	192,466	0.4
Fiduciaries	3,396	2,166	(36.2)	14,124	16,163	14.4
Total	463,617	440,676	(4.9)	4,060,054	4,148,224	2.2
Sales and Use						
Regular	141,662	163,467	15.4	1,481,657	1,421,339	(3.4)
Motor vehicle	2,314	70	(97.0)	20,528	990	(95.2)
Total	144,404	163,587	13.3	1,503,902	1,434,348	(4.6)
Corporate Tax						
Declarations	25,580	13,589	(46.9)	237,918	211,285	(11.2)
Remittances & Corp Franchise	46,463	41,482	(10.7)	150,302	138,448	(7.9)
Total	72,044	55,071	(23.6)	388,220	349,733	(9.9)
Estate	129	0	(100.0)	789	2,317	193.7
Interest	7,791	2,287	(70.6)	50,991	28,229	(44.6)
Liquor	1,640	1,802	9.9	16,818	16,883	0.4
Beer	674	670	(0.6)	6,240	6,607	5.9
County Foreign Insurance	41,576	42,481	2.2	125,741	132,176	5.1
Federal Reimbursements	6,658	7,640	14.7	54,715	62,583	14.4
All other revenues	16,458	23,486	42.7	105,778	106,264	0.5
Gross GR collections	754,987	737,702	(2.3)	6,313,249	6,287,364	(0.4)
GR Refunds						
Individual Income	183,898	138,164	(24.9)	615,315	599,234	(2.6)
Corp. Income&Franchise	10,902	3,917	(64.1)	127,617	135,344	6.1
Senior Citizen Property	24,056	28,803	19.7	73,674	86,194	17.0
Sales	6,826	4,246	(37.8)	44,764	53,584	19.7
All other	848	707	(16.6)	22,127	16,504	(25.4)
Total GR Refunds	226,530	175,837	(22.4)	883,497	890,860	0.8
Net General Revenue	528,456	561,866	6.3	5,429,753	5,396,504	(0.6)

Source: Missouri Office of Administration

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