

**Revenue Estimating Conference
Minutes
December 11, 2017**

Members Present: Dave Roederer, Holly Lyons, David Underwood.

Mr. Roederer called the Revenue Estimating Conference to order at 2:00 p.m.

Approval of the December 11, 2017 agenda

Mr. Roederer called for a motion to approve the agenda for the December 11, 2017 meeting

Motion: Mr. Underwood

Second: Ms. Lyons

All voted in favor and the motion was carried unanimously.

Approval of the October 19, 2017 minutes

Mr. Roederer called for a motion to approve the October 19, 2017 minutes

Motion: Mr. Underwood

Second: Ms. Lyons

All voted in favor and the motion was carried unanimously.

Mr. Roederer reiterated that the Code of Iowa establishes a three member panel consisting of the Legislative Branch represented by Ms. Lyons, the state represented by Mr. Underwood, and himself representing the Executive Branch. The Conference is required to meet at least three times per year, where it is required to reach a consensus. Projections are developed independently of each other, using a variety of sources. The Department of Revenue is relied upon heavily. The Governor is required to submit her budget based on the December estimate. The Legislature is to use the lower of the two estimates between December and March. The Conference will update estimates Fiscal Year 2018 and Fiscal Year 2019.

Ms. Lyons began by stating since the October meeting less than two months ago, little has changed in the national economy. Many economists and resources indicate the U.S. economy keeps progressing at a modest to moderate pace with job growth, low unemployment, and consumer confidence fueling growth. According to the Bureau of Labor Statistics, earnings are slowly improving with average hourly earnings of private sector employees increasing 2.4 percent over the trailing twelve months ending in October. The stock market is at an all-time high, and consumer confidence going into the holiday shopping season was strong. One area of considerable uncertainty continues to be the impact of potential fiscal, tax, or trade policy if enacted by Congress and the subsequent impact on the economy. In particular, federal tax law changes could impact revenue collections in Iowa because of federal deductibility. In global news, the world economy is showing more strength and steady U.S. demand fuels import

growth. Uncertainty remains about U.S. trade policy with the delay in NAFTA talks, but a stronger global economy is a positive factor for the Iowa economy.

Forecasting state revenues 18 months or more into the future is always risky, and one thing is certain, we know that we will always be wrong – either too high or too low. But with a federal tax change very likely, and the details still largely unknown, it's even more challenging and more likely that revisions will need to be made, particularly to the out-year estimate, FY 2019, which is a critical estimate at this meeting since the Governor and the Legislature must use that estimate in preparing and adopting the state budget this spring.

Iowa revenues, while still growing, are disappointing for the first five months of the fiscal year. There is nothing, however, to indicate that the revenue growth will turn negative, but growth is very slow; slower than the Revenue Estimating Conference forecasted last October.

Most Iowa economic indicators would suggest slow but steady growth. The Iowa Leading Indicators Index increased the last two months, with all eight index components contributing positively for the first time since 2010. Iowa's unemployment rate is the lowest since 2001 at 3.0%. Initial unemployment claims are low and have been for three years. These numbers continue to indicate that the economy is strong and also indicate a tightening of the labor market. As Mr. Underwood has stated before, a lack of qualified employees is a concern, and worker shortages could reach the point of constraining business growth.

The USDA indicates that net cash farm income, a measure of overall farm profitability, is expected to increase in 2017 by 3.9% after declining in each of the three previous years. According to ISU farm economists, corn and soybean yields were better than expected, which is good news.

The economic conditions would seem to indicate better growth in state revenues than what we're experiencing. However, a significant number of the Iowa specific economic and tax revenue indicators are showing the lowest growth rates experienced in the last 4 to 9 years. For example, the growth in wage and salaries, a key driver of personal income tax, was at 1.9% growth in FY 2017; slightly more than half the growth rate experienced in FY 2016 and much less than half of what was experienced in FY 2015. Sales tax net revenue, with FY 2017 growth of 0.4%, was the lowest growth since FY 2010.

As of last Friday, net general fund receipts, which are fiscal year to date gross receipts less refunds, had a growth rate of 0.3%. Personal income tax, the largest source of state tax revenue, has three components. Withholding tax which is collected and submitted by employers, estimated tax payments which are made by some taxpayers, and payments with final returns. Withholding tax is the most stable component of personal income tax and provides a steady stream of deposits. Estimate payments are made quarterly and most payments with final returns are received in the spring. Through Friday, the most stable component, withholding tax, on a fiscal year basis is flat in terms of growth. Personal income

tax, the largest category of General Fund receipts is up only 0.4%. Sales & use tax is showing flat growth at 0.2%. All of this is concerning given that we're in the 6th month of the fiscal year. There is still time to realize growth from retail sales tax, personal income from a positive tax return season, and/or income from capital gains and other investment income, but at this point it is believed that a slight downward revision in revenue estimates are appropriate. This situation is not unique to Iowa; our neighbors to the west, Nebraska, and to the north, Minnesota have recently made downward adjustments to revenue forecasts. Again, growth continues to be positive, just at a lower level.

The LSA is reducing their FY 2018 estimate for net General Fund receipts to 2.3% growth, down from the REC October estimate of 2.4%. This represents a slight reduction or \$5.0 million.

The LSA is reducing their FY 2019 estimate for net receipts to 3.6% down from the REC October estimate of 4.2% growth, a modest reduction of \$44.2 million.

Mr. Underwood began by stating that one of the biggest unknowns right now is the impact of federal tax law changes. Assuming something is passed, it could very well go out beyond FY 2019 before any impacts are really felt within Iowa's general fund receipts. With that unknown, none of that prediction can be put into the estimates.

The big impact continues to be the farm economy, the NAFTA crop prices. If it rains in Argentina, there go the soybean prices back down again. Somehow, farmers had enough reserves built up when prices were good that they were able to survive a couple years of down commodity prices and fluctuations in cattle and hog prices. Just recently, bankers have been talking about farmers really being in trouble now. They have been able to keep it together, but there are some that are very definitely in big trouble. A lot of discussions with other bankers show that they are starting to see that "trouble" farmer become a "big trouble" farmer now. That has not been seen, but Mr. Underwood is sure it will impact Iowa businesses that are associated with farming over the next two years.

If NAFTA is no longer, it will certainly be a huge impact. Mr. Underwood assumes there will be some trade agreements with Mexico and Canada and trade will continue to be done there, but if something is not resolved it will certainly be disastrous to Iowa's farmers.

Mr. Roederer stated there are three areas that make the estimate very challenging. Both Ms. Lyons and Mr. Underwood had mentioned NAFTA, which can have a big impact. NAFTA deals primarily with Canada and Mexico and they happen to be our two largest export markets. Any disruption there is going to have a significant impact on agricultural products as well as manufacturing products, which are tied together. Another area mentioned was tax reform. Estimates are done by looking at which laws are passed or look like they are about to be passed. Tax reform does not necessarily fall in that category, so that has not been factored into the estimates. The third area that is watched very carefully is the farm bill. The farm bill is obviously already in place for this year, but what impact it might have down the road and what people may or may not do depending on what it appears may or may not happen in

Washington on the farm bill is unknown. Farm Bill Iowa receives approximately \$2.6 billion in one form or another. The producers receive \$1 billion of the \$2.6 billion, which is primarily in the crop support payment program and the insurance program. That is a big factor that can influence the economy in Iowa.

It has been mentioned that Iowa has a low unemployment rate, but there still has not been quite the movement one might expect in wages. In talking to some manufacturers, they are starting to see some of those rise. The encouraging news on the employment front is that manufacturing is starting to hire, both large and small, and manufacturing represents on the wage basis approximately 22-25% of the wage income that comes into the state. That is one of the reasons the Governor's Appointee is a little more positive in this current fiscal year than what Ms. Lyons had indicated from LSA.

The other area where it is believed additional revenue will be seen is from the dividend side. In looking at corporations, they are paying dividends and those dividends are going to have to be realized. Obviously the stock market is continuing to increase. Last year, there was a very small amount that came in on Capital Gains and it is believed that is going to be increasing this year or next.

The Ag economy, as Mr. Underwood pointed out, still appears to be the main driver. Land prices have stabilized, maybe inching up a little but at least not decreasing. In checking with the Superintendent of Banking, as well as the Farm Credit out of Omaha (which is the region that Iowa is in and they account for approximately half the loans in the state), they are still pretty confident in the ability of their producers to go forward. There are different types of producers- those who own their land will probably be alright, those who do not own land are the ones that people are most concerned about.

Another positive is the online sales. We are seeing an increase in Use Tax, which is going along with a trend that has been throughout the country for some time. But on the downside, it also is a softness that we are having in the sales tax.

Review FY2018 General Fund Estimates, Accruals, Refunds, School Infrastructure Transfer, and Lottery and Other Transfers

Motion: Made by Mr. Underwood to keep the estimate that was made in October for the current fiscal year.

Second: Ms. Lyons.

Discussion: Mr. Roederer stated that the October estimate for Net Receipts Plus Transfers was \$7,237.75 billion.

All voted in favor and the motion was carried unanimously.

Review FY2019 General Fund Estimates, Accruals, Refunds, School Infrastructure Transfer, and Lottery and Other Transfers

Motion: Ms. Lyons made a motion to move the \$7,527.0 billion, a 4.0% growth rate.

Second: Mr. Underwood.

Discussion: Mr. Roederer stated that the October number was \$7,536.3. LSA is recommending that number be \$7,492.1 billion and the Governor's Appointee's estimate is \$7,575.6 billion, a difference of \$83.5 million. Mr. Roederer explained that both are estimating growth, just a difference of how much or how fast. Mr. Underwood stated that he would be very comfortable with a 4.0% growth rate, which is just about where the October estimate was (4.1%). A 4.0% growth rate would put it at \$7,527.0 billion, \$11 million less than the October estimate. But Mr. Underwood could live very easily with the October estimate of \$7,536.3 billion. Ms. Lyons stated she could agree with the \$7,527.0 billion.

All voted in favor and the motion was carried unanimously.

Fiscal Years 2018 and 2019 Gambling Revenues Transferred to Other Funds and Interest Earned on Reserve Funds (transferred to Rebuild Iowa Infrastructure Fund)

Motion: Mr. Underwood made a motion to utilize the numbers without change.

Second: Ms. Lyons.

All voted in favor and the motion was passed unanimously.

Other Business

With no further business, Mr. Roederer called the meeting adjourned at 2:28 p.m.

These minutes were approved at the March 09, 2018 meeting.

Ms. Lyons made a motion to approve the minutes of the December 11, 2017 meeting, as well as the January 05, 2018 and February 09, 2018 special meetings, and the motion was seconded by David Underwood. All members voted in favor of the motion and it was carried unanimously.

Respectfully submitted,

Tammy Winters