

**Revenue Estimating Conference
Minutes
December 13, 2018**

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

Mr. Roederer called the Revenue Estimating Conference to order at 1:00 p.m.

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 utilized for the most current revenue activity at the time. The Governor is required to submit her budget based on the December revenue estimate and the Legislature is to use the lower estimate of the December and March. Today the Conference will update the estimate for the current fiscal year, which is fiscal year 2019, and then update the estimate for Fiscal Year 2020 which will begin in July.

Approval of the December 13, 2018 agenda

Mr. Roederer called for a motion to approve the agenda for the December 13, 2018 meeting

Motion: Ms. Lyons

Second: Mr. Underwood

All voted in favor and the motion was carried unanimously.

Approval of the October 16, 2018 minutes

Mr. Roederer called for a motion to approve the minutes for the October 16, 2018 meeting

Motion: Mr. Underwood

Second: Ms. Lyons

All voted in favor and the motion was varied unanimously.

Ms. Lyons began by stating that in the eight weeks since the last meeting, little has changed economically; the underlying fundamentals of the national and state economy remain sound. The economy continues to be in mid-expansion with nothing on the immediate horizon that suggests a serious downturn or recession.

The pace of U.S. employment growth has slowed over the past two years, and is now running at about 1.6 percent year over year. Nationally, the unemployment rate remains extremely low at 3.7% and is expected to go lower. The Iowa unemployment rate is the lowest ever, at 2.4%. Unemployment claims, both initial claims and continuing claims, are at the lowest levels since the 1970's — although there has been a very slight increase both at the national and state levels in the last few weeks. Wage growth is gradually accelerating, although the state growth rate is below the national rate of growth. The shortage of qualified workers continues to

hamper economic growth. Interest rates, although rising, remain historically low and while CPI inflation is increasing, inflation growth that excludes food and energy has been relatively stable and is currently about 2.2%. National retail sales growth is currently about 5.4%, the highest growth rate in almost 6 years.

As mentioned at the October meeting, the price of corn is well off the highs experienced in 2013, but it has stabilized and world supplies are low which is positive for the Iowa economy.

Some things to watch at the national level that will impact Iowa include:

- The effect of agricultural tariffs from trade wars with China, and just the general uncertainty surrounding international trade policy.
- Soybean prices – the prices have fallen somewhat, and the global supply is high resulting in a potential negative impact on Iowa farmers.
- Additional interest rate hikes by the Federal Reserve could have a constraining effect on the economy.
- Recent stock market volatility is concerning if it continues at the magnitude experienced the last two months.
- Global issues: Brexit impact on Europe, the Chinese economy, declining oil prices...

I've said before that forecasting state revenues 18 months or more into the future is beyond difficult, and this year is no exception with the extraordinary circumstance of both federal and state tax reductions impacting the Iowa economy and our estimates. The main revenue enhancing impact of the federal tax bill from last December has already been realized by way of growth in withholding income due to the federal deductibility tax increase (if federal taxes decrease, Iowa state revenue increases). That will stop boosting Iowa income tax revenue year over year in February. The state income tax rate reduction and the reduction in income tax withholding rates do not start until January.

The new state tax law also includes an increase to the sales tax base to include additional types of items and services such as digital goods and online marketplaces. This change is also effective in January. That would affect revenues positively, but the reduction in withholding tax receipts is expected to be larger than the sales tax base increase, so we're very likely to see slowing from our current rate of growth. Withholding tax is the most stable component of personal income tax and provides a steady stream of deposits, but at least for the near term, due to the new tax law changes, it has become extremely difficult to predict.

To summarize, the underlying economy remains solid and is still in mid-expansion with no serious signs of downturn. There is just more "noise", or variables, when looking at this particular December estimate which is why the LSA estimate is a bit more on the cautious side of optimistic than the October estimate. LSA is estimating a growth rate of 4.5% in FY 2019 and 1.5% for FY 2020.

Mr. Underwood states that most headlines attribute the rise in the capital market weaknesses to skepticism about US/China trade negotiations, Brexit back and forth, rising interest rates, fears about inverting US steel, falling oil prices, stock specific woes impact, even threats of the US government shutdown. But Mr. Underwood believes the current volatility hinges more on overblown sentiment based fears and old news that lacks the material scale, or the real surprise power, to derail the growing economy. A lot of the discussion is what is going to be the growth rate and how does it relate to Iowa after looking at the world. Today's fears have been rehashed for months, and in some cases for years, what has been referred to as "cows chewing cud". Still, strong fundamentals are currently underappreciated; corporate earnings and revenues reflect, in many cases, brisk growth; leading economic indexes are, to most extents, positive; and purchasing managers indexes remain expansionary. All largely ignored in favor of headline fears. Plus the one thing that has changed since the October meeting, we will have divided Congress which means that most likely nothing will happen, and that is generally good for the economy. The most prudent course of action is to remain patient and disciplined in what we do, as well as conservative; watchful for the signs of the recession that will come someday.

Mr. Roederer stated that the indicators are showing a good growth, although there is going to be constant volatility especially with what is going on in the international markets. Revenues are strong; currently today, they are running greater than estimated. Congress passed the farm bill which eliminated one unknown, so that will help stabilize a little bit on the agriculture sector. Mr. Roederer's concerns are still in the agriculture area, not fundamentally as far as values of land, which is one thing to always be cognizant of because that can always change the health of farming considerably.

The NAFTA impact is a big impact in Iowa, where nearly 50% of exports go to Canada and Mexico. Renewable Fuels Standards have also been helpful as looking at today's economy, but still seeing a weakness in products, in what is going to happen with the price of corn and soybeans. Soybeans have been ticking up a little bit after the President of the United States and the President of China met and appears the Chinese government is looking to purchase anywhere from 15-20 million bushels of soybeans.

Internationally, the Koreans are an area that seems to be making progress one day, the next day not so good. So if that heats up, that could change the map quite a bit. Saudi Arabia, as mentioned last time, went through leadership change and obviously with what is going on over there is also an area that is very volatile and any drastic move in that country could have a big impact on the Middle East, which will greatly impact the price of oil. China is one of the key countries that needs to be watched very carefully. If the tariff situation improves, it depends on how it improves. On the one hand, it could be very helpful to agriculture but on the other hand, the intellectual property issue must be resolved for the future of manufacturing in the United States.

The online sales transition that is taking place is working very smoothly, which is a good indicator that the online companies are coming forward and working well with the Department

of Revenue. There is a little concern about construction. It was a very wet season and while there will be a lot of work available next year, there wasn't as much that got done this year and that could impact somewhat on income. Federal tax reform, which has been mentioned and Mr. Underwood pointed out how that all gets put together and how it all works out, where we think we've got a good handle on what is going to happen but we really don't know until the tax returns start coming in. As Mr. Underwood has been talking about for some time, there are still a lot of companies in this state that would like to expand but are having a challenge finding the workers they need. If there is a good side to that story, many other states are doing the same thing so it isn't like everyone can just pack up and go to another state.

Review Fiscal Year 2019 General Fund Estimates, Accruals, Refunds, School Infrastructure Transfer, and Lottery and Other Transfers

Motion: Made by Mr. Underwood to move Governor's Appointee's numbers,

Second: Mr. Roederer

Discussion: Mr. Underwood suggested reducing Personal Income Tax by \$12 million, which would take the net receipts to \$7,728.6, a 4.7% change

All voted in favor and the motion was carried unanimously.

Review Fiscal Year 2020 General Fund Estimates, Accruals, Refunds, School Infrastructure Transfer, and Lottery and Other Transfers

Motion: Made by Ms. Lyons to move the Governor's Appointee's numbers

Second: Mr. Roederer

Discussion: In light of what was done in FY19, the new growth would be 1.8%.

All voted in favor and the motion was carried unanimously.

Fiscal Years 2019 and 2020 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 move the numbers as written

Second: Ms. Lyons

All voted in favor and the motion was passed unanimously.

Summary: Growth for 2019 - \$344.7 million

Growth for 2020 - \$139.8 million

Other Business

With no further business, Mr. Roederer called the meeting adjourned at 1:24 p.m.

*These minutes were approved at the March 15, 2019 meeting
Mr. Underwood made a motion to approve the minutes of the December 13, 2018 meeting and the motion was seconded by Ms. Lyons. All members voted in favor of the motion and it was carried unanimously.*

Respectfully submitted,

Tammy Winters