Revenue Estimating Conference
Minutes
December 10, 2015

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

Mr. Roederer called the Revenue Estimating Conference to order at 10:00 a.m.

Mr. Roederer began by stating that the Code of Iowa establishes a three member panel, which is required to meet three times per year. The Governor is required to put his budget together based on the December Revenue Estimate. The three-person panel consists of representative from Legislative Service Agency, which is Holly Lyons, someone that is not in the immediate branches of government which is represented by Dave Underwood, and the Executive Branch has a representative that the Governor appoints and that is me, Dave Roederer, Director of the Department of Management. While the Governor must put his budget together based on the December revenue estimate, the legislature must use the lesser of the two between the December and the March estimate. If March is lower than the December estimate, the legislature must base their budget on the March and if it is higher in March, they must use the December number.

Approval of the October 13, 2015 agenda

Mr. Roederer called for a motion to approve the October 13, 2015 agenda. Ms. Lyons made the motion to approve the agenda and Mr. Underwood seconded the motion. All voted in favor and the motion was carried unanimously.

Ms. Lyons began by stating that not a lot had changed since the October meeting. There is continued modest to moderate growth on the national level, but more mixed signals are being received in Iowa and that has the LSA reducing their projection for FY2016 and F Y2017 from the levels set by the October REC. The turbulence noted in October seems a bit more real, thus the LSA is a little more cautious in their estimate.

At the national level, there is continued strength in employment, with unemployment rates reaching an all-time low of 5%. Initial unemployment claims, a key indicator of a recession, are at an all-time low, which is a good thing. U.S. employment wage growth is coming off its post-recession highs but still hovering around 4%. Nationally, economic forecasters are predicting that the economy may reach full employment by the middle of 2016. Full employment, or a tightened labor market, usually means that markets will see wage increases, which in turn fuels income tax revenue.

While employment looks good, some potentially negative factors are the weak global economy and stronger U.S. dollar reducing exports, increasing inventories, and slower capital investment due to falling oil prices. The presumed increase in interest rates by the Federal Reserve is expected to happen this month, as well, and some volatility of the financial markets is likely to occur as a result, and that impact is unpredictable.

Turning to Iowa, there are a few indicators that suggest caution. There has been an uptick in the past four weeks in Iowa's initial unemployment claims. Some of this may be due to seasonal employment changes, but the uptick was dramatic enough to take notice, and it may be an early indicator of job reductions.

The November Mid America Business Condition Index, issued by Creighton University, shows that the Iowa score has declined for the last 5 months and with a score of 42.3, it is well below the index of 50 which is considered an expansionary economy. It has dropped 10 points in the last year.

The Department of Revenue's Leading Indicator's Index is considered to be an indicator of the direction of the Iowa economy and is comprised of 8 components. It has declined for the last 10 months. A contraction in the Iowa economy is indicated when two conditions are met: 1) The index declines by at least two percent over a 6 month period, and 2) a majority of the 8 individual components decline over those six months. Both of those conditions have been met.

Declining corn and soybean prices continue to be a drag on the Iowa economy, affecting personal income and durable goods manufacturing. Iowa experienced record yields but the low prices keep farm income down. This continues to work its way through the Iowa economy.

Iowa Sales & Use Tax is also a concern – it has been flat the last few months, partly due to increased tax refunds and the required transfer to the flood mitigation fund.

Ms. Lyons concluded that growth is expected, just a bit weaker than originally anticipated. A normal growth year would be in the 5 to 6% range. The LSA estimate calls for growth in net receipts after transfers of 3.0% for FY 2016 and 3.8% for FY 2017. In dollars, that's a reduction of $28.9 million from the REC estimate for FY 2016 and $55.8 million from FY 2017.

Mr. Underwood began by stating that Ms. Lyons mentioned most of the items that are of concern to him. Employment is still the biggest issue in Iowa, and it is the lack of people to do the work. Winnebago just announced that they were moving some production outside of the state because they were having trouble finding production workers; Curries manufacturing just announced some new automation coming in to offset their difficulty in hiring. Those are the kinds of things seen all the time and the help wanted ads are up all over the place. So it is very difficult to see significant employment growth, except maybe in the Des Moines area.

Mr. Underwood stated that Ms. Lyons had pointed out the difficulty in the farming economy, and he state that not much opportunity is seen for growth in any of the sectors of the farming economy.

The interest rate uncertainties will probably not significantly impact the 2016 fiscal year but most likely will start to trickle down into Iowa more in the 2017 fiscal year. As higher interest rates come in for the borrowing and hopefully a little bit of that trickles down to the savings side to offset that somewhat. The stock market continues to be confusing as to where that is headed and so many of the international issues are impacting the stock market currently.

Generally speaking, Ms. Lyons brought up a lot of the indexes sitting out there, but an additional one is the Wells Fargo Small Business Survey, which is the national survey, indicated a decline in confidence, which is what Mr. Underwood is hearing from small businesses in Iowa.

One thing relied on significantly for growth in the General Fund is general wage increases. They appear to be continuing at low levels. Many that Mr. Underwood has spoken with are not looking for significant increases to wages and a lot of that has to do with higher healthcare costs. The businesses that will be kicking in after the first of this year and that will significantly slow wage growth at a number of companies.

A red flag is our Iowa Leading Indicators. If we really believe our economists, it is definitely troubling. Looking at it historically, when it starts to decline at the current magnitude that is certainly a red flag that things are slowing. That has never really been put to the test yet. It was developed during the last recession so it will be interesting to see how that plays out and how it really does impact the General Fund. Mr. Underwood is struggling with the numbers, even though LSA has come in with lower numbers they still appear to be on the optimistic side. It is a matter of how significant the decline will be. Mr. Underwood believes the numbers will actually come in lower than the REC's last estimate.

Mr. Roederer began by speaking about the international sector, stating it is tense. What could happen there may very well impact the whole world economy and it could completely change the way the world economy is going today.

Iowa continues to grow. Things need to be put in perspective that when Iowa was growing at a much greater rate or a normal rate, Ms. Lyons discussed 3.0%, there has been an average of about 4.0% over a decade period of time, but still within the ballpark. There was mention of the skilled workforce; it is still an issue of this state, but the fact that companies are still looking for workers indicates that they plan on continuing to do what they are doing. It does pull back the growth if there were more of the skilled workers, but it is a much better situation than people saying there are more workers than are needed. Long term, Mr. Roederer believes that they are still looking in the mode of hiring people. It may not be at quite the rate it was at one time, but they are also looking at alternatives as to how to train workers to get them the skills. In looking at the unemployment rate, going to 3.5% in October which was down from about 4.3% a year prior to that, wages are continuing to grow. There are a number of projects that have been postponed simply because contractors are booked with business and they are looking for that to continue into next year as well. From that aspect, Mr. Roederer believes that things will continue to go on at the rate they are.

Obviously the agricultural sector is a major concern. One of the things we've never been able to do is pinpoint if price of corn is such and such and soybeans is at a certain amount, what that impact is going to be throughout the whole economy. Part of the reason for that is because of the dynamic change you have in the economy. If you look at what the models were set up with, what the economy was then and what kind of companies we have now, it's a different mix. On the positive side, Mr. Roederer does not look for interest rates to increase exceptionally high because the federal government cannot afford to have it go that high. As the interest rate goes up, they have to pay that interest on their debt. So whether or not it is being artificially held down or not, Mr. Roederer does not believe it is going to go too high.

The global economy and the strength of the dollar are two things to look for. The strength of the dollar is going to have a big impact because the higher the dollar the more costly it is for other countries to buy our products. What will happen on federal trade and agriculture policy is obviously a big factor. By the numbers, Mr. Roederer does not think things have changed that much since the last REC meeting in October. There are cautionary signals, but he also thinks there is also counterbalancing. Mr. Roederer met with the Iowa Business Council and they were very positive about what they see happening in their business and in the coming year. While the total dollars are significant, when you look at the percentages we are still less than 1.0% between what LSA's numbers are and what the Governor's appointee's numbers are.

Review Fiscal Year 2016 General Fund Estimates, Accruals, Refunds, School Infrastructure Transfer, and Lottery and Other Transfers

Ms. Lyons suggests adding $20 million to LSA's number. Mr. Underwood stated that personal income tax last year there was a 3.0% increase. The Governor's appointee is at 6.5% and LSA is at 7.0%. There were some legislative changes that may be through 2.0% additional revenue so even if you add that onto the 3.0% increase from last year, add consistent growth and employment, the potential for some of these projections to actually show a decline during some months next year. That hopefully will not happen. Looking at the 7.0% growth in fiscal year 2016 on personal income tax, Mr. Underwood is not sure where this would come from and seems significantly higher than what could be expected. There is some potential in sales tax for growth of that number a little bit, but not significantly.

Mr. Roederer stated that he would support the additional amount to the sales tax. Ms. Lyons responded to Mr. Underwood's concern about the 7.0% in personal income by stating that through today's date, personal income is up by 5.7% for the year. Income tax return season hasn't really been hit yet. This is one of the reason's LSA believes it will be a strong personal income tax revenue.

Mr. Underwood is comfortable with 5.0% growth. Ms. Lyons is pretty confident it is going to be more than 5.0%.

Mr. Underwood made a motion to move LSA's fiscal year 2016 number by increasing sales tax by an additional $20 million. Ms. Lyons seconded the motion. With no further discussion, all voted in favor and the motion was passed unanimously. Bottom line net receipts plus transfers is $7,045.6 million, which is 3.3% growth.

Estimate Fiscal Year 2017 General Fund Estimates, Accruals, Refunds, School Infrastructure Transfer, and Lottery and Other Transfers

Ms. Lyons stated that the major differences between the LSA and the Governor's appointee are again, Sales Tax, Refunds and Personal Income. Ms. Lyons suggested taking the fiscal year 2016 number, with 4.0% growth for fiscal year 2017. This would make the bottom line number $7,327.4 million. Mr. Roederer stated he would be in agreement. Mr. Underwood commented that if the LSA's 3.8% is used, that is within $14 million, but stated he would be in agreement with the 4.0% growth.

Ms. Lyons made a motion to take the agreed to estimate for fiscal year 2016 of $7,045.6 million and add 4.0% growth to that, to come up with a new figure of $7,327.4 million for fiscal year 2017 for sales tax. Mr. Underwood seconded the motion. With no further discussion, all voted in favor the motion passed unanimously.

Fiscal Year 2016 and 2017 Gambling Revenues Transferred to Other Funds and Interest Earned on Reserve Funds (transferred to Rebuild Iowa Infrastructure Fund)

Mr. Underwood made a motion to carry the Governor's appointee's numbers as presented for FY 2016 and FY 2017 Gambling Revenues and Ms. Lyons seconded the motion. With no further discussion, all voted in favor and the motion was carried.

Other Business

With no further business, Mr. Roederer called the meeting adjourned at 10:29 a.m.

Respectfully submitted,

Tammy Winters