

**Revenue Estimating Conference
Minutes
March 19, 2015**

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

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

Mr. Roederer began by stating that the Code of Iowa establishes a three member panel to make revenue projections for the state. Holly Lyons represents the Legislative Branch, Dave Underwood represents the public and the citizens of the state and Mr. Roederer represents the Executive Branch. The Conference is required to meet three times per year. The Governor is required to use the December revenue estimate to present his budget to the legislature. The legislature is required to use the lower of the December or March estimates. The members of the panel independently review various data and are required to come to a consensus. The Department of Revenue gives a presentation which gives the current situation of where the taxes are, but then each conference member independently comes up with the numbers for this meeting. A variety of sources are used and each member may look at numbers differently, but they come together and come to a consensus. Today the panel will go through the current fiscal year, which is FY15 on the sheet and ends on June 30th; then review the next fiscal year, which is FY16 and begins July 1st.

Approval of December 12, 2014 Minutes

Mr. Roederer called for a motion to approve the December 12, 2014 minutes as they are written. Ms. Lyons made the motion to approve the minutes and Mr. Underwood seconded the motion. All voted in favor and the motion was carried unanimously.

Ms. Lyons stated that economic growth in the U.S. and Iowa remains solid. There seems to be a slowing in national growth forecast as we move from 2015 to 2016 and 2017, but growth is still more on the side of modest than moderate; in the 4-5% range. Ms. Lyons describes modest as a touch weaker than moderate. Overall there is certainly no cause for alarm or concern at this time. Job growth is strong in the U.S., with more than three million jobs created in the past year and the U.S. unemployment rate dropped to 5.7%. In Iowa, non-farm employment is expanding at about 20,000 jobs per year. Three thousand one hundred jobs were added in January and the unemployment rate decreased to 4.2%.

There are a couple of areas to watch; manufacturing employment in Iowa is down about 700 jobs since last May, but overall Iowa employment increased by 15,000 jobs over the same time period. Agriculture machinery manufacturing employment is also down slightly from last year at this time. Initial unemployment claims continue to decline, which is a positive sign.

Employment growth is critical to Iowa's economic stability as jobs generate income tax and sales tax, the two key components of Iowa's General Fund Revenue. Recently, employment

wage growth appears to be growing; all components look good- employment, hourly wage, and hours worked, but it is still not near the 2008 pre-recession peak. Other economic indicators are positive in Iowa, as they are nationally. This includes steadily increasing retail sales, rising GDP and increasing corporate profits. Lower gas prices should mean more disposable income for consumers, but it is not clear if that can be seen working itself into the economy yet. Some research indicates that consumers may be using the extra cash to pay off debt or to save.

Iowa Business Council Survey index remains strong and business council members in Iowa expect a strong year in sales and capital spending. Some of the indicators have shown some recent downward ticks, such as the Iowa Leading Indicators Index, where only two of the eight components of that index experienced a positive change in January, down from six in December. This is something to keep an eye on, particularly since it is meant to be a leading indicator, but it is certainly not a major concern at this time. The Rural Main Street Index fell below a growth neutral rate in February, indicative of the declining farmland prices and declining farm equipment sales. A strong dollar in the global economy could become an issue for exports since Iowa is an export state. There is also the ever present concern about Federal Reserve Board action and the impact on interest rates and inflation.

Turning to the LSA estimate for the current year, fiscal year 2015 and the fiscal year that will begin in July, fiscal year 2016, the estimate is optimistic with just a bit of concern. There are more positives than negatives on the horizon. The LSA estimate for fiscal year 2015 is lower than the December estimate for the sole reason that the legislature made a law change in February. Senate File 126, the IRC Update Bill. IRC stands for Internal Revenue Code and the bill conforms Iowa tax law to federal changes enacted between January 2014 and January 2015. The bill was signed by the Governor and will lower Iowa revenue in fiscal year 2015. The LSA estimate simply incorporates that law change into the estimate. Essentially, the bill extends some tax exemptions and credits and that has a negative impact on Iowa revenue of approximately \$99 million. The fiscal year 2016 estimate is also adjusted for this change, which is expected to be positive in that year. Comparing the LSA 2016 estimate to the revised REC 2016 estimate reflects a very slight decrease of less than three-tenths of one percent. LSA is generally optimistic. There are a couple of state indicators that need to be watched, but overall nothing to be concerned about at this time. The recovery continues in Iowa with steady modest growth.

Mr. Underwood stated that most of his comments were very similar to those made in December. Some substantive information is what is happening on the early tax returns being timely filed by Iowans. Over 90% of the taxpayers are filing electronically, which allows some really good analysis and those indicators at this early stage indicate that farm income is about 30% less than last year for farmers that have filed so far. They now have an extension until the end of April to file so it delays a little bit some of that comparative information. The other thing that is down is interest income. Other than that, most other reported items so far are coming in on a positive basis. Withholding is very strong in Iowa and that is certainly opening things up in the number of people employed and the manufacturing overtime hours continue to be in that 42 hour week range, which is kind of a historical peak. There are a lot of positive things.

The impact on the farm economy is still a little bothersome. The new numbers for current year projections out of the USDA would indicate another 30% drop in farm income on average during this year. That level of drop is not tremendously significant to the state individual income taxes. At this point in time, Mr. Underwood is cautious and he agrees that Iowa Leading Indicators are kind of disturbing in that they are dropping down just a little bit. There are certainly some good indicators in the economy overall that help buoy the Iowa economy. The one complaint that Mr. Underwood continues to hear is that it is hard to find people to go to work, even though a lot of jobs have been added in Iowa. The biggest challenge right now for Iowa's growth is getting enough people to move here and take those jobs, or convince people that are not working that it would be a good thing to go back to work.

Mr. Roederer began with the international front, with the focus mainly on the Middle East. OPEC is driven pretty much by Saudi Arabia overproducing oil. The worldwide demand does not call for the production levels that are occurring and it appears that it is going to continue at least for a while. As a result, that is lowering the price of fuel significantly. Where this is having the impact is on two countries – Iran because of the sanctions that have been placed on them and their inability to be able to sell worldwide the oil that they continue to produce even though they have the sanctions; and Russia's economy – it is impacting their desire to increase their footprint and it is focused on the Ukrainian effort. This is the focus of the international attention and no one knows at this point where it can lead. If the sanctions were to be loosened on Iran, they have millions of barrels of oil that they already have in tankers, but the tankers are not allowed to go anywhere. So if that happens, there will be another big glut of millions of barrels that will go onto the oil market, which are going to suppress the price even further. The problem is, it is unknown how long that will last and it is purely speculative as to how far and what the impact is going to be. Most economists will say that if we go through calendar year 2015 with lower oil prices, it is going to start impacting the inputs that people are having. As we know, especially in agriculture, when you're talking about fertilizer and other components that go into putting on the crop, it is going to lower their cost. The problem is, it will probably take a while for that to work through. When you know that countries are overproducing oil, they can always slow that down and so prices can flip quite a bit. When looking at projections, long term oil decrease was not factored in.

Mr. Roederer stated that he concurs with Ms. Lyons and Mr. Underwood on their assessment of what is happening in Iowa. The economy continues to grow, but probably at a slower rate than one might think of when coming out of a national recession and that is because the national growth is also somewhat stunted. Most of the fundamentals are in pretty good shape. The agriculture sector is the one that would be classified as the major caution. Mr. Roederer agrees with Mr. Underwood's analysis of the concern. One of Mr. Roederer's concerns is the price of corn. It is down 43% from the highs in the 2011-2013 range. Currently corn prices are at about the \$3.60 cent range. What is causing that is an oversupply throughout the country and somewhat in Brazil and Argentina. It will take approximately 2-3 years to get through this oversupply. Price of land is trending downward and may continue that way for a little while. The biggest unknown in the agriculture sector is what the spinoff is in local economy. That has

never been able to be measured directly. The other factor is the value of the dollar. The stronger the dollar is, the less attractive our exports are to other countries.

On the positive side, still many producers are at a break even or even a little profit, with corn at \$3-\$3.60 per bushel, depending on the producer – the debt load they might have, whether or not they own the land they are farming and whether or not they are a lower cost producer. When corn prices were at \$7, producers were not borrowing money, based on the fact that they thought corn prices were always going to be at that level. Our debt is still compared to where we were during the 80s. Another factor involved in that is that lenders learned through the 80s that it was not best to loan money based on the total assets of a particular producer. So most of them are now lending on a cash flow basis. Therefore, all this debt has not been built up. Even if interest rates start going back up, keep in mind that the producers today have locked in a lower interest rate, so the current land they have is not going to be jeopardized by the value on that because their interest rate is going to change. Where the interest rate will have an impact will be on operating loans they are getting on this year's crops and any new land which they produce.

The pork industry is still strong. USDA is predicting that will start dropping. Oil prices will have a significant impact if the lower prices continue. In the Ag sector, we look at approximately 20 different factors that we believe has an impact. The three trends being watched most carefully and that is the global economy, specifically China- what activity they have and what purchasing they are doing as their economy has leveled off. We believe it will be in the steady growth in China. The strength of the dollar will also have a big impact on exports, which will make a difference on what the value of products are and what will happen to the price of corn. Federal trade and agriculture policy will also be a big factor.

Mr. Roederer agrees with Ms. Lyons in regards to the United States. Mr. Roederer would add that congress's year-by-year extensions of the tax code create great uncertainty. The U.S. economy is very resilient as long as it knows what the rules are. If you know the rules will be changed every year simply because there is an extension one year at a time, that will create a question mark.

Mr. Roederer than explained the spreadsheet handed out by LSA.

Review Fiscal Year 2015 General Fund Estimates, Accruals, Refunds, School Infrastructure Transfer, and Lottery and Other Transfers

Ms. Lyons made a motion to move the LSA numbers for Fiscal Year 2015 and Mr. Underwood seconded the motion. Mr. Underwood stated that there is not much difference between the two numbers, so he is comfortable with either number and Mr. Roederer concurred. Mr. Underwood stated that the only number he struggled with a little was the level of refunds. Mr. Underwood suggested that LSA increase their refunds by \$16 million and Ms. Lyons concurred. Ms. Lyons amended the motion to increase the amount of LSA's expected refunds by \$16 million. With no further discussion, all voted in favor and the motion was carried. This will

raise the 2015 refund number to \$937 million. The bottom line net receipts plus transfers will move to \$6,767.4 and the percentage increase is 4.3%.

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

Mr. Underwood suggested keeping the LSA numbers and Mr. Roederer concurred. Mr. Underwood made a motion to increase the refunds by \$20 million, to take it to \$953 million. Ms. Lyons seconded the motion. With no further discussion, all voted in favor and the motion was carried. The new 2016 refund number is \$953 million and the bottom line net receipts plus transfers moves to \$7,175.5 million, which is a 6% increase over the new 2015 estimate.

Fiscal Year 2015 and 2016 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 numbers as presented for Fiscal Year 2015 Gambling Revenues and Ms. Lyons seconded the motion. With no discussion, all voted in favor and the motion was carried.

Other Business

Ms. Lyons stated there is a new page on LSA's website called Economic Trends. There are 13 economic indicators that can be followed. The page explains the indicator and is updated monthly, quarterly or annually. There are also links to the source to the indicator and a database where it can be pulled off into Excel to view.

With no further business, Mr. Roederer called the meeting adjourned at 1:31 p.m.

These minutes have not been approved as of the transcription of these minutes.

Respectfully submitted,
Tammy Winters