Revenue Update

Part 1: Tax Collections

General Fund/Education Fund revenue ended FY 2010 $45 million below the consensus February forecast. Based upon current collection rates and economic indicators updated in November, we expect General Fund/Education Fund revenue to be $6.4 million above the FY 2011 February consensus ($.9 million General Fund/$5.5 million Education Fund).

Transportation Fund revenue ended FY 2010 $3.0 million below the consensus February forecast. Based upon November economic indicators and four months of collections, we expect Transportation Fund revenue to be $11.0 million above the FY 2011 February forecast.

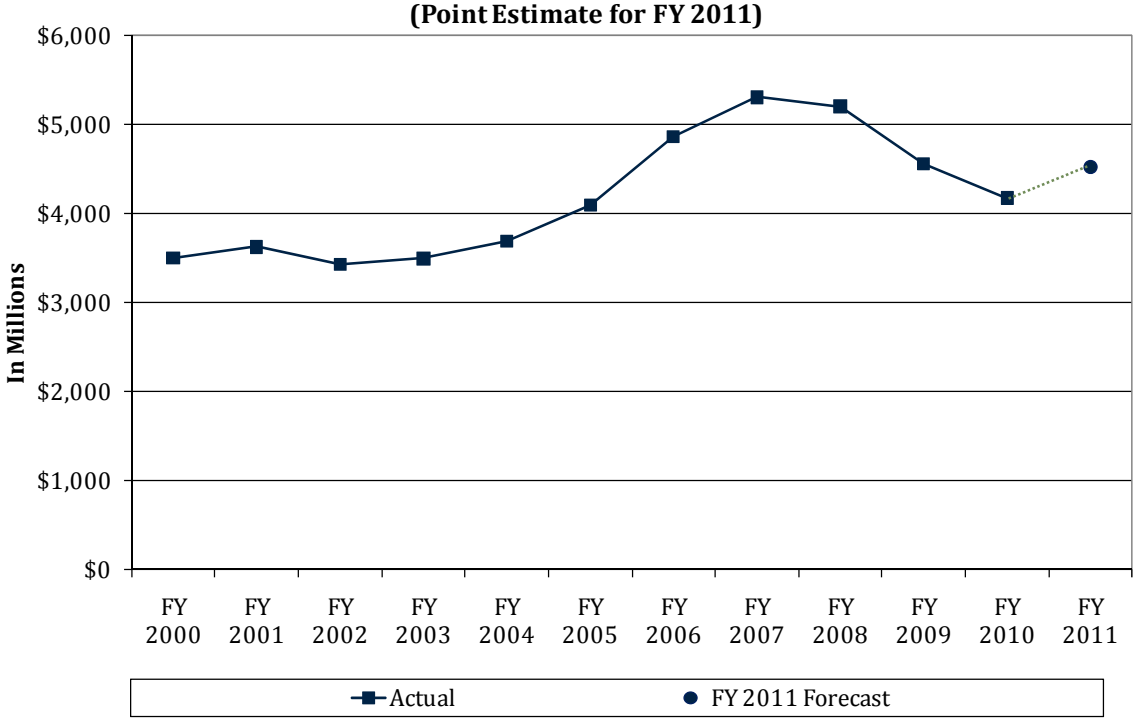
Although there are conflicting signs regarding the strength and direction of future economic activity, we expect slow, revenue growth for the coming two fiscal years. The growth is largely contingent upon a recovering consumer, increasing wages, and accelerating growth in business income and passive income.

While a tepid recovery is taking place, there are credible risks, headwinds, and signs that the recovery could be short lived. Among the headwinds and risks are the housing and nonresidential construction markets, generally tight credit conditions, continued evidence regarding lack of consumer and business confidence, weakness of the dollar in world currency markets, insufficient labor market growth, and overall slack in final demand.

The expected improvement in the State's economic outlook also contains some upside potential. Potential pent-up demand could increase housing demand, spending and income beyond that which is incorporated in the current forecast. A greater than expected return of confidence could increase business investment and consumer risk, and, by so doing, increase revenue beyond that which is expected.

All in all, we expect measured economic and revenue growth in FY 2011.

CHART 1: Combined General and Education Fund Revenue
(Point Estimate for FY 2011)



Tax Revenue *(In Millions of Dollars)*	FY 2010 Forecast	FY 2010 Actual	Difference	FY 2011 February*	FY 2011 November*	FY 2011 Difference
General Fund	$1,763.43	$1,762.51	($0.92)	$1,866.90	$1,867.75	$0.85
Education Fund	2,456.68	2,412.23	($44.45)	2,539.55	2,545.03	$5.47
Total	**$4,220.10**	**$4,174.74**	**($45.37)**	**$4,406.45**	**$4,412.78**	**$6.33**

***Not including one-time deposits for H.B. 440 - Transportation Modifications ($113m) and H.B. 464 - Tobacco Trust Fund ($11.3m)**
Source: LFA, USTC, DOF

LFA
Legislative Fiscal Analyst

Sales tax, the largest portion of revenue to the General Fund, ended FY 2010 $28 million below expected collections. The underperformance of the sales tax was largely due to late payments and lower than expected taxable sales in food stores, restaurants, electric & gas, communications, auto repair, business services, wholesale-nondurables, and mining.

For the past three years, consumers have generally withheld their spending. Primarily to reduce debt or the inability to take on more debt, many individuals have increased their savings rates over the past few years. Given the higher than anticipated collection rate in the first quarter of 2010, the elevated savings behavior appears to have moderated somewhat, with consumers now starting to accept a somewhat diminished savings rate though it is one that is still high by historical standards.

Beer, cigarette, and tobacco taxes, now the second largest source to the General Fund, are expected to come in about $2 million above the previous FY 2011 target, as short-term consumption slightly outpaces a long-term declining base.

As demand flattened out, the third largest source to the General Fund, insurance premiums, ended FY 2010 $6.2 million below the February consensus. We expect insurance premiums to come in $3.6 million below the February FY 2011 target.

Although severance taxes are not expected to reach the levels that would require a transfer to the State's trust fund, severance taxes are expected to grow by $10.2 million over the FY 2010 close. The generally healthy growth in oil & gas and mining severance taxes this fiscal year is due to generally higher prices for natural resources.

Sector	*FY 2010 Taxable Sales (Billions)*	*Change FY 07-FY10*	*Change FY 08-FY10*	*Change FY 09-FY10*
Retail-Gnrl Merch.	$5.981	19%	9%	5%
Retail-Motr. Veh.	$3.797	-28%	-25%	-4%
Retail-Food Stores	$3.631	2%	-8%	-5%
Whlesle-Durable	$2.770	-37%	-6%	-1%
Retail-Restaurants	$2.917	0%	-17%	-7%
Retail-Misc.	$2.880	-15%	-34%	-13%
Retail-Bldg.,Gardn	$1.788	-37%	2%	5%
Electric & Gas	$1.951	7%	-26%	-15%
Manufacturing	$1.851	-30%	-24%	-3%
Communications	$1.660	-32%	7%	-3%
Services-AutoRep.	$1.560	-3%	-2%	-5%
Services-Business	$1.361	-9%	-13%	-5%
Retail-Apparel	$1.254	1%	-3%	2%
Retail-Furniture	$1.230	-39%	-36%	-19%
Services-Hotels	$0.953	22%	-1%	3%
Services-Recrea.	$0.817	-13%	-7%	-3%
Private MV Sales	$0.736	-10%	-18%	0%
Whlesle-Nondur.	$0.651	-28%	-26%	-16%
Mining	$0.621	49%	6%	-15%
Construction	$0.526	-31%	-27%	-8%

Sources: Economic & Statistical Unit, USTC; LFA

Percentage of Revenue to the General Fund			
Fiscal Year	*Beer, Cig., Tob.*	*Insurance Premium*	*Severance taxes*
2011 (f)	5.07%	4.21%	4.38%
2010	3.33%	4.54%	4.37%
2009	3.13%	4.29%	4.42%
2008	2.90%	3.57%	4.25%
2007	2.72%	3.13%	3.88%
2006	2.78%	3.26%	4.05%
2005	3.20%	3.48%	3.35%
2004	3.56%	3.54%	2.42%
2003	3.18%	3.47%	1.91%
2002	3.59%	3.38%	1.43%
2001	3.39%	2.69%	2.67%
2000	3.51%	3.16%	1.39%

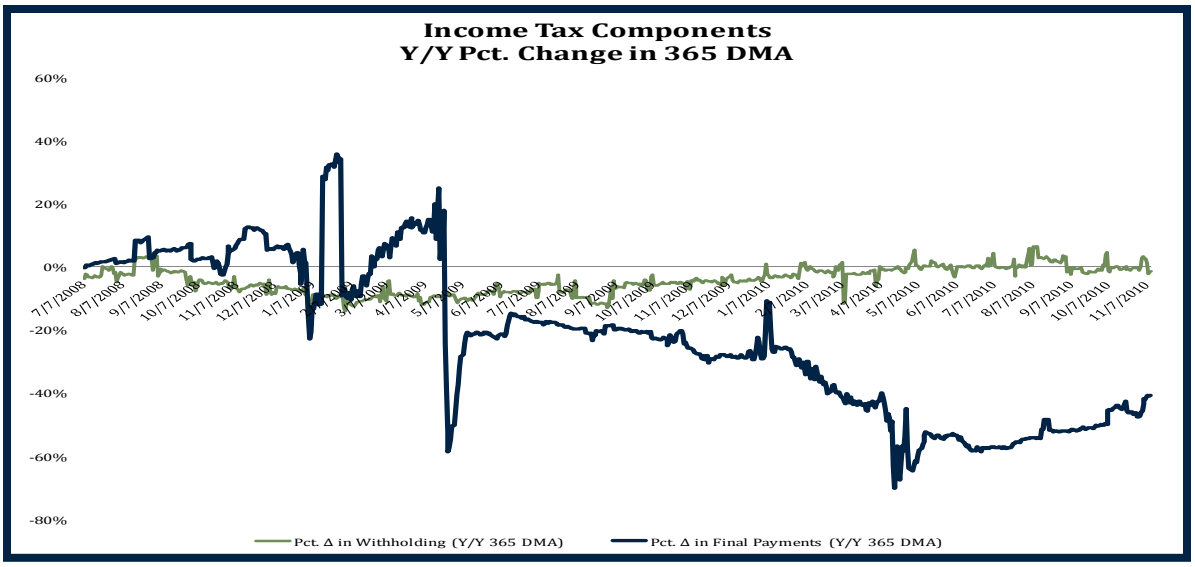
Source: LFA

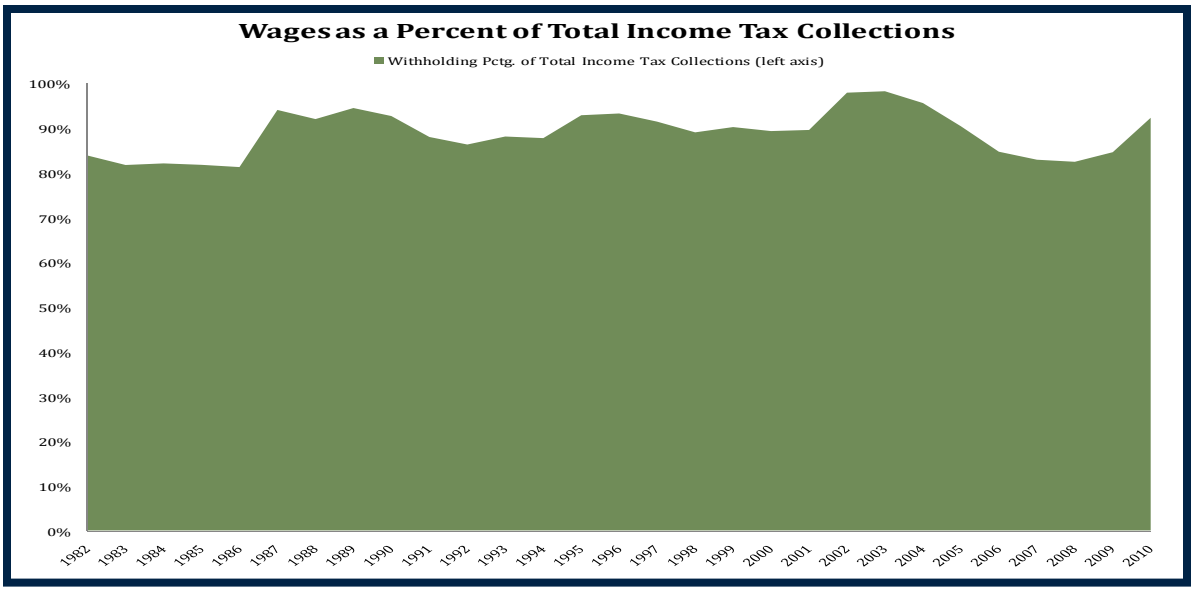
Education Fund

The tax on wages represents the largest source of revenue to the Education Fund, with the percentage of income tax revenue stemming from withholding reaching 92.3% in FY 2010, an increase of 9.1% over the FY 2009 withholding percentage. Based upon the consensus revenues and updated economic indicators, a corresponding drop in final payments is expected to recover in FY 2011 by about 26% from the FY 2010 close. Proprietorship income, S-corporation income, bonus income, and capital gains pick are expected to pick up from the FY 2010 low. Final payments, though, may not materialize if capital gains and business income are shifted further down the economic recovery timeline.

Corporate income tax revenue finished FY 2010 above the February FY 2010 target. The corporate income tax performance was due to top-of-the-line revenue growth and reductions in labor costs. We expect corporate profits to grow by 3.0% in CY 2011 from CY 2010 and by 3.3% in CY 2012 over CY 2011. The expected slowdown in corporate profit growth in CY 2012 is largely due to the expectation that labor costs and other corporate input costs will begin to rise. With that said, the corporate income tax forecast contains upside risks of continued productivity growth, automation, and a better than expected recovering consumer.

Some downside risks for corporate collections are the fact that corporations do not appear to have much confidence in demand, and therefore continue to have soft hiring freezes. Corporations also are cautious due to instability in the global markets and are therefore delaying investments.





Sources for these two charts: LFA, USTC

WAGES & EMPLOYMENT

Employment continues to lag the economic recovery, with this time around being slower than historical experience. Based upon the November economic indicators, we expect job findings to exceed job separations by 1.4% in CY 2011 and 2.3% in CY 2012, or, on average, 16,500 more individuals possessing nonfarm jobs in CY 2011 than did in CY 2010 and 27,800 more individuals possessing nonfarm jobs in CY 2012 than did in CY 2011.

Coupled with the expectation that the employment picture will improve, we anticipate the State's unemployment rate to decline from a projected CY 2010 average of 7.6% to 7.1% in CY 2011 and 6.1% in CY 2012. The decline is good news, although part of the decline assumes that some of the structurally unemployed, younger individuals, and others will forego entering the labor market, thus making the unemployment picture look better than what historical evidence would indicate.

Total wages and income declined in 83% of the State's zip codes in FY 2010 over FY 2009, with the largest portion of the income drop being concentrated in Salt Lake County and some areas where oil and real estate boom periods abruptly ended. We expect FY 2010 to represent the recent low of income tax collections, as indications are that wages are improving somewhat.

Based on the most recent economic indicators, average wage is expected to grow by 2.3 percent in CY 2011 and by 2.2 percent in CY 2012, with a good portion of this recovery happening along the Wasatch Front and in some regionally important industries.

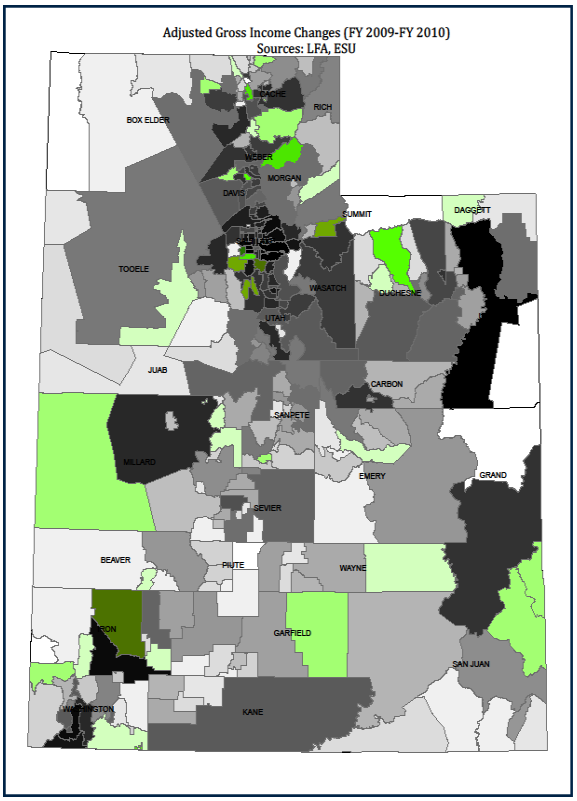
The State of Utah graphic below represents the change in Federal Adjusted Gross Income (FAGI) zip code. Black and grey areas are zip codes with negative Federal Adjusted Gross Income FAGI growth; green areas experienced positive FAGI growth. The more black the area, the larger the drop in income; the darker the green, the better performance of FAGI on a Y/Y basis.

While we expect that the signs of a modest recovery in employment and wages are indicative of the likely labor market picture for the coming two years, risks remain. On the upside, pent-up demand could further expand the need for workers. Alternatively, business confidence and uncertainty, coupled with consumer restraint, could worsen the labor market outlook.

Labor Market Expectations for 2011 & 212

Industry	2009 Year End	2002-2009	2010 Gain (2009 to 2010	2011 Gain (2010 to 2011)	2012 Gain (2011 to 2012)
Mining	10,694	3,522	-494	-200	400
Const.	70,492	1,264	-5,992	1,800	2,800
Mfg.	112,874	-594	-3,074	1,800	1,600
Trade, Trans., Uti.	234,097	22,629	-4,397	1,800	3,100
Info.	29,558	-1,304	-358	100	400
Financial	71,075	6,753	-3,375	500	1,900
Prof. Srvs.	149,517	34,296	4,083	4,300	8,300
Edu.&	150,874	51,804	4,626	5,200	4,800
Leisure	110,852	29,299	48	500	1,900
Other Srvs.	34,024	1,526	-524	300	600
Gvrnment	214,679	22,554	721	400	2,000

Source: RAC, DWS



Demographics

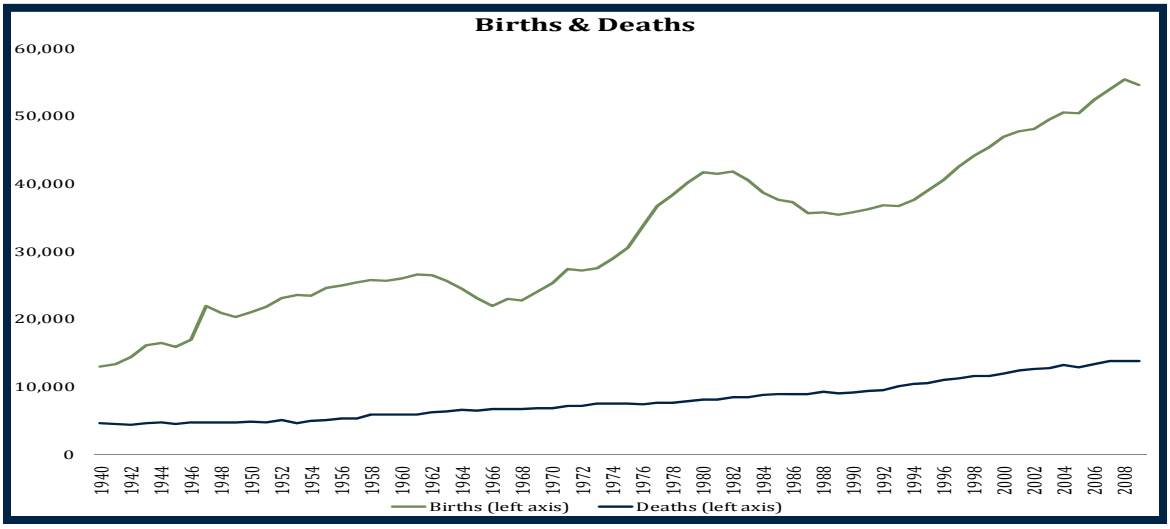
Demographics (births, deaths, migration, household size) affect directly or indirectly most revenue sources to the General Fund and Education Fund. Utah's population tends to be younger (28 years vs. national median of 36.7 years), lives longer (79.5 years vs. national average of 78.0 years), has higher fertility rates (20.8 births vs. national average of 14.3 births) and more persons per household (3.13 persons vs. national average of 2.59).

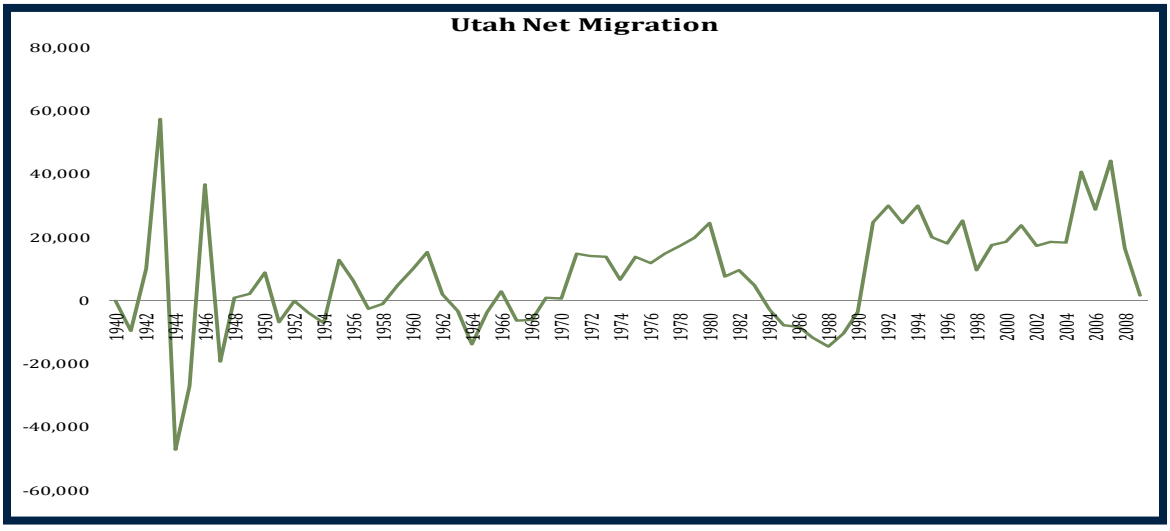
Births during CY 2010 are projected to come in 0.8% below CY 2009. Part of the decline is due to the echo baby boom and the other part is due to the recession's impact on a given family's ability and choice to support children. The employment downturn and slow upturn over the next two years is expected to decrease the number of births by about 920.

The other part of natural population growth, deaths, are expected to number 34,375 over the next two years. Although the downturn has affected natural population growth, Utah is still expected to have the youngest population in the nation.

Besides having good birth rates and lower death rates, Utah also increases in population size due to migration. From 1950 through 2010, migration has increased the State's population by a projected 563,555 individuals, or 20%. We expect most of the in-migration in the next two years not to expand the demand for housing or to increase household formation, but rather to increase the household size.

Population growth is, at times, a driver of economic growth (population-push). At other times, it is a coincident of good economic times. Still at other times, population growth doesn't induce more demand, but rather shifts spending from other categories of expenditure. Within the coming two years, we expect most of the population growth to be of the shifting type.





Sources for these two charts: LFA, RAC, BEBR

Based upon transaction data, the real estate markets started to experience problems in the third quarter of 2007, a couple months before concrete evidence of the coming financial crisis appeared in December 2007. Real estate transaction value has declined from a high in 2006 of about $16.4 billion to a low of $9.0 billion in 2009. The complete 2010 year is unavailable, but indications are that it will come in below 2009. We expect real estate transactions to pick up slightly in 2011, but not enough for any strong growth in the next few years.

In terms of volume and price, the residential housing market is the biggest reason behind the drop in real estate transaction value. Indications from the supply side are that construction of new homes is slow due to the difficulty builders are having getting land and construction financing. On the demand side there appears to be excess capacity. Coupling the excess capacity with foreclosure rates indicates likely price declines in CY 2010 and CY 2011, followed by 2% home price appreciation in CY 2012.

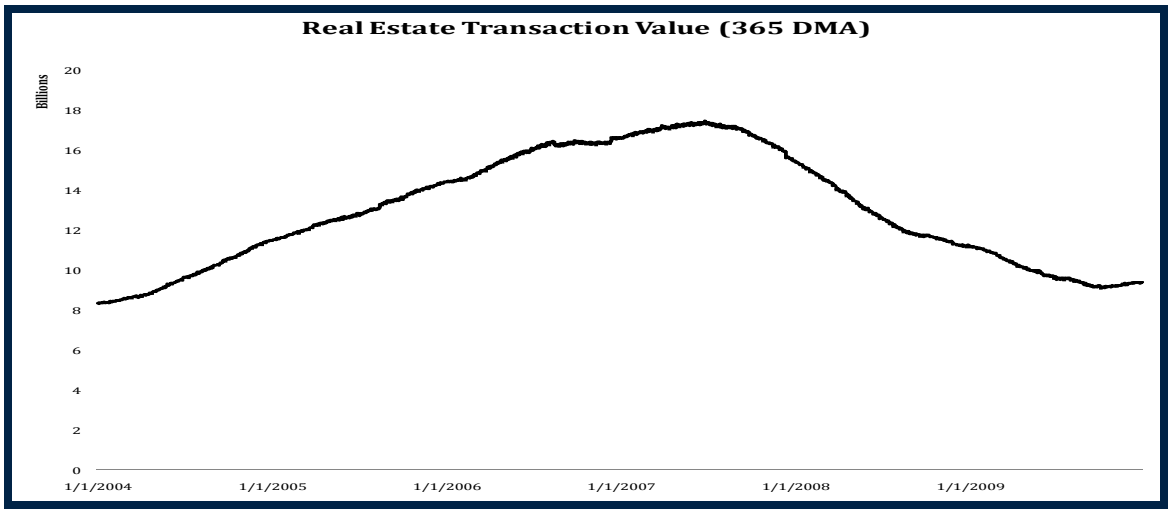
On the upside, single-family permits are up about 26% from a year ago, although the single family permit data is not enough to cover the 40% decline in condominium and new apartment construction. The overall residential construction market is expected to end CY 2010 below CY 2009 values. Modest growth of 1,700 and 2,000 in dwelling units is expected for CY 2011 and CY 2012.

The commercial construction market also remains under pressure. One of the key issues facing the commercial real estate, or non-residential markets, is a cycle of refinancing, which will occur during the next few years. Typically, commercial real estate loans are made for a period of 5-10 years in length. Many loans which were made at the height of the real estate market's valuation are coming due in the 2010-2013 period. With valuations generally lower and credit availability tighter, the ability to refinance these loans will likely be problematic for some borrowers.

In addition to the credit market effects on the non-residential market, reported excess capacity and vacancy rates will probably continue to put further downward pressure in CY 2010. The value of non-residential construction will likely end 2010 around $900 million, with an expected bottom in 2011 at $700 million, followed by a non-impressive rebound to $800 million in CY 2012. One project that will help keep non-residential builders working is the NSA Data Center, which is not included in the permit valuation data.

Indicator	*Units*	*2009*	*2010*	*2011*	*2012*
Dwelling Permits	Thousands	10.5	9.3	11.0	13.0
Res. Permit Value	Millions	1,674	1,700	2,000	2,300
Nonres. Permit Value	Millions	1,054	900	700	800
Additn,Alt.,&Repairs	Millions	660	600	625	650

Sources: RAC, BEBR



Sources: Economic & Statistical Unite, USTC, LFA

National Green, Yellow, and Red Shoots

The State continues to lack immunity from national economic conditions. In the June 2010 revenue update, we mentioned concerns regarding debt financing and the paying down of debt by national governments, the likely possibility of slow growth, labor market slack, and the present effects of uncertainty and lack of confidence. These concerns have been valid and, unfortunately, continue to be valid and are expected to continue to have an effect on the nation's and world's economies in the near term.

National economic signals are generally divided in terms of the direction of future economic activity, although more recent indicators are somewhat more positive. The following table represents the most recent indicators released since November 1st. Although most indicators have indirect effects on the State, the indicators highlighted in grey are more influential in terms of correlation forecasting. Green shoot indicators are indicative of a decent national economic recovery; yellow shoots indicate lackluster performance; and red shoots are indications of problems in the economic outlook.

National Economic Indicator Results Released since November 1st

Indicator	*Released*	*Period of Time*	*Market Expected*[1]	*Actual*	*Green Shoot*	*Yellow Shoot*	*Red Shoot*
Michigan Consumer Sentiment	11/12	Nov.	69.0	69.3		●	
Treasury Budget	11/10	Oct.	-$140.0 B	-$140.4 B			●
Trade Balance	11/10	Sep.	-$44.8 B	-$44.0 B			●
MBA Mortgage Applications	11/10	11/5	+2.0%	+5.8%	●		
Wholesale Inventories	11/9	Sep.	0.6%	1.5%		●	
Continuing Unemployment Claims	11/6	10/23	4386 K	4340 K		●	
Initial Unemployment Claims	11/6	10/30	445 K	457 K		●	
Consumer Credit	11/5	Sep.	-$3.5 B	$2.1 B	●		
Pending Home Sales	11/5	Sep.	2.5%	-1.8%			●
Average Workweek	11/5	Oct.	34.2	34.3		●	
Hourly Earnings	11/5	Oct.	0.1%	0.2%		●	
Unemployment Rate	11/5	Oct.	9.6%	9.6%			●
Nonfarm Payrolls—Private	11/5	Oct.	60 K	159 K	●		
Unit Labor Costs	11/4	Q3	1.0%	-0.1%		●	
Productivity	11/4	Q3	0.9%	1.9%		●	
Truck Sales	11/3	Oct.	5.1 M	5.4 M		●	
Auto Sales	11/3	Oct.	3.8 M	3.7 M		●	
Factory Orders	11/3	Sep.	1.7%	2.1%		●	
ISM Services	11/3	Oct.	53.4	54.3		●	
Construction Spending	11/1	Sep.	-0.7%	0.5%		●	
ISM Index	11/1	Oct.	54.0	56.9		●	
PCE Prices—Core	11/1	Sep.	0.0%	0.0%		●	
Personal Spending	11/1	Sep.	0.4%	0.2%		●	
Personal Income	11/1	Sep.	0.2%	-0.1%		●	

[1] In the case of Initial & Continuing Unemployment Claims and MBA Mortgage Applications, the market expectation is that of LFA economists. All other expectations are based upon surveys of financial market observers.

Sources: BEA, ISM, U.S. Census Bureau, Commerce Dept., Moody's, BLS, NAR, DOL, Yahoo!Finance

Office of the Legislative Fiscal Analyst
State Capitol Complex - House Building, Suite W310
Salt Lake City, Utah 84114-5310

Phone: (801) 538-1034 Fax: (801) 538-1692
Website: www.le.utah.gov/lfa

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Contributors:

Jonathan C. Ball
Director

Dr. Andrea Wilko
Chief Economist

Dr. Thomas Young
Economist

Revenue Collections to Date (EARL)

Tax Revenue *(In Millions of Dollars)*	FY 2010 Final*	FY 2011 Consensus**	FY 2011 Consensus Growth Rate	FY 2010 Year-to-Date (11/14/2009)	FY 2011 Year-to-Date (11/14/2010)	FY 2011 Year-to-Date Growth Rate
Sales & Use Taxes	$1,402.67	$1,557.60	11.0%	$511.58	$562.88	10.0%
Individual Income Tax	2,104.59	2,201.00	4.6%	645.84	688.67	6.6%
Corporate Franchise Tax	258.45	306.48	18.6%	60.53	77.08	27.3%
Beer, Cigarette & Tabacco	58.71	100.95	71.9%	19.84	42.82	115.8%
Insurance Premium Taxes	80.01	83.95	4.9%	37.46	28.49	-24.0%
Severance Taxes	77.07	87.25	13.2%	10.25	18.97	85.1%
Other Sources	193.24	188.60	-2.4%	45.07	40.27	-10.7%
Total - General & Education Funds	**$4,174.74**	**$4,525.83**	**8.4%**	**$1,330.58**	**$1,459.17**	**9.7%**
Motor Fuel Tax	$243.30	$243.10	-0.1%	87.12	85.38	-2.0%
Special Fuel Taxes	94.44	100.45	6.4%	34.08	38.42	12.7%
Other Transportation Fund	73.63	77.70	5.5%	22.28	22.64	1.6%
Total - Transportation Fund	**$411.36**	**$421.25**	**2.4%**	**$143.48**	**$146.44**	**2.1%**

***Does not include $18.8 million pharmacuetical lawsuit settlement.**

****To allow comparison with collections, includes $113 million one-time transfer from Centennial Highway Fund under H.B. 440 and does not include $11.3 million transfer from Tobacco Trust Fund under H.B. 464.**

Source: LFA, USTC, DOF