

JCA Revenue Update – July 2023

Inflation

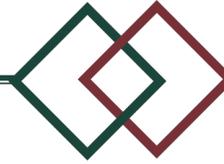
Economic Outlook

Sales Tax Growth

Revenue Outlook for FY2024



Inflation: Remains Elevated



- Overall, June 2023 CPI at 3.1% Y/Y

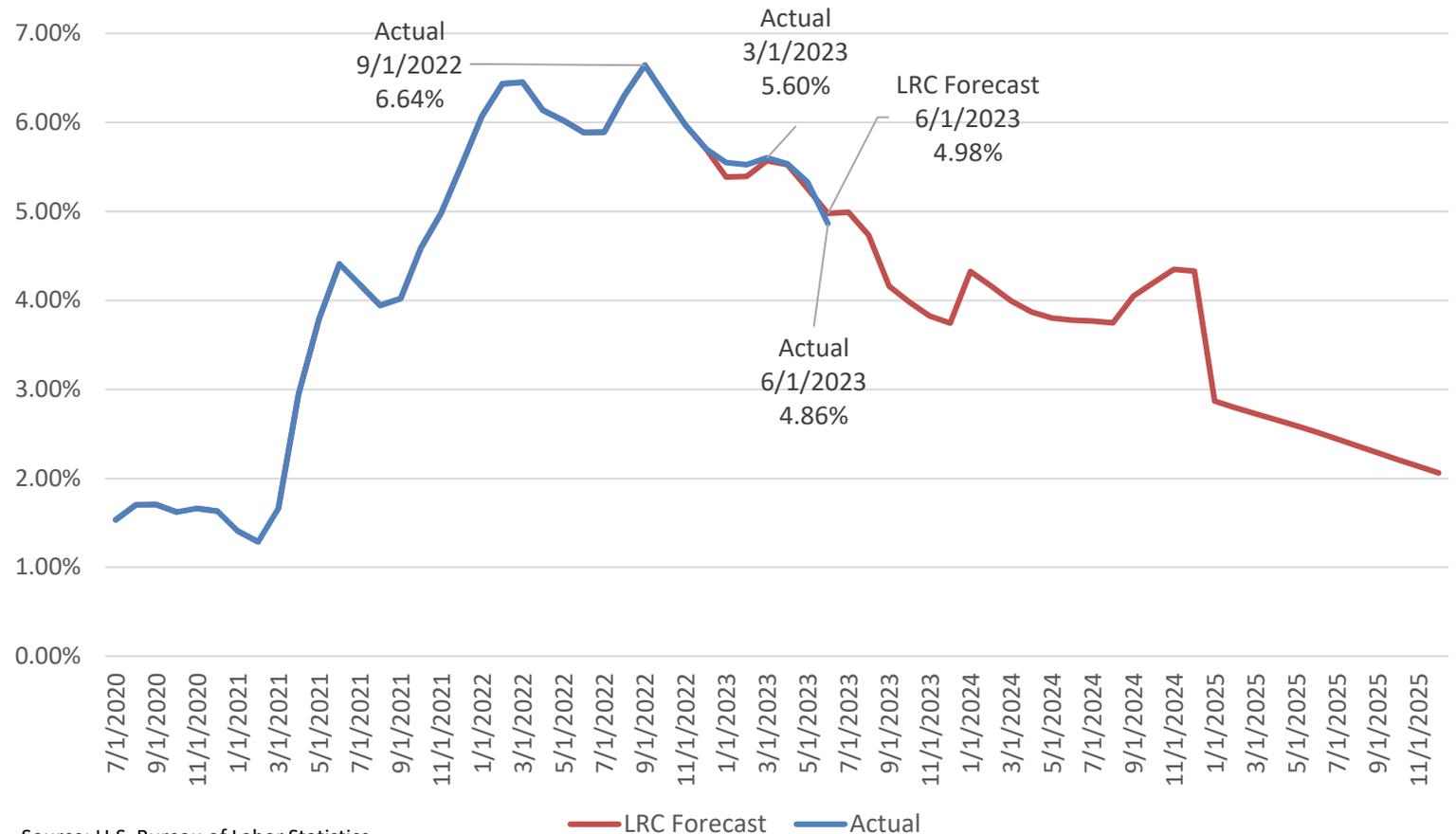
Driven mainly by core inflation and food

- June 2022 CPI was 8.9% Y/Y
- The 12-month change in food inflation is 5.7%. June 2022 growth was 10.1%.
- The 12-month change in energy inflation is (16.5%). June 2022 growth was 41.3%.

- June Core Inflation at 4.86% Y/Y

- Increases in goods and services are not seeing the disinflation like food and energy.
- June 2022 growth was 5.88%
- An elevated core inflation will result in higher prices and more sales tax revenue for the state.

Core Inflation (Inflation Less Food and Energy)



Source: U.S. Bureau of Labor Statistics

Economic Outlook: Recession Risk



- The chances of a recession occurring in the next 12 months is down. Economists are seeing a 25% chance of a recession, down from 35% back in March. South Dakota typically lags a national recession by 6-8 months.

Reasons Against a Recession

- Softer Landing by the Fed
- Low unemployment
 - US 3.6%
 - SD 1.8%, historically low
- Growth in Real Disposable Income
 - May: 4% growth Y/Y
 - Jan-May 3.2% average growth
 - On par with pre-COVID levels
- Inflation declining
 - Food and energy inflation significantly lower than a year ago.
- Banking sector risk easing
- Supply chain issues easing

Reasons For a Recession

- When the Fed raises interest rates, the US economy went into recession 4 of the last 6 times.
- Core Inflation remains elevated
 - June 2023 Core inflation 4.9%
 - August 2022 Core inflation 6.3%
- Potential for more interest rate increases

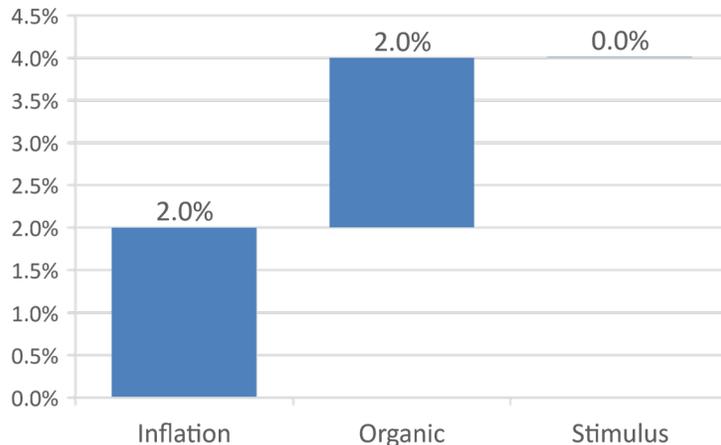
Sales Tax Growth: Components



- Sales tax growth is represented by three components:
 1. Inflation: growth in the cost of goods and services.
 2. Organic: growth in consumer spending.
 3. Stimulus: growth in consumer spending because of fiscal policy.

- Higher inflation can lead to growth in sales tax even when organic growth is negative
- Tables represent examples of what the growth components could look like.

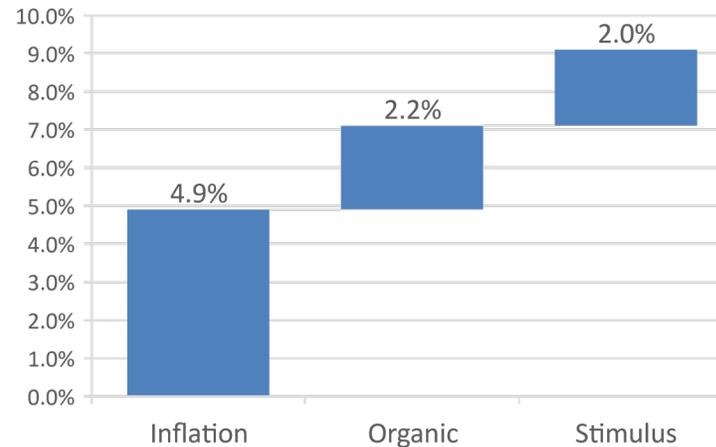
Estimated Sales Tax Growth by Component for Typical Year



Note: The sales tax growth by component is example of what likely occurred. The data does not exist to specifically identify the growth of each component. The graph is for illustrative purposes.

■ Increase ■ Decrease ■ Total

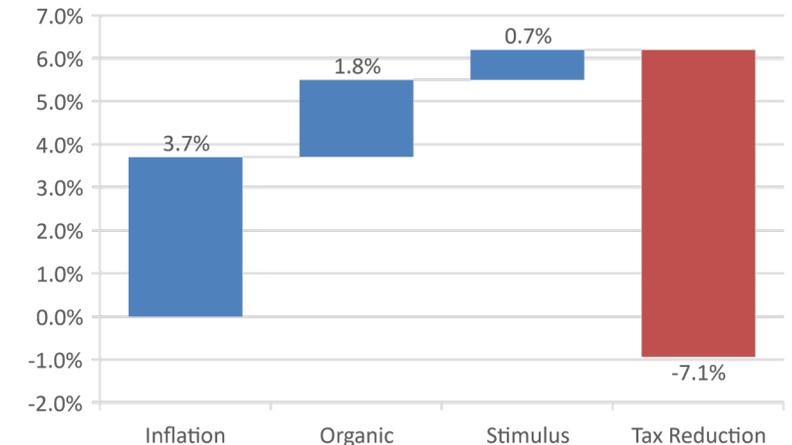
Estimated Sales Tax Growth by Component for FY2023



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■ Increase ■ Decrease ■ Total

Estimated Sales Tax Growth by Component for FY2024



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■ Increase ■ Decrease ■ Total

Revenue Outlook for FY2024



Reasons for higher state revenues in FY2024

- Wage Growth
 - Teachers receive 7% increases
 - State employees receive 7% + target pay
 - Providers to 100% of methodology, with 20%+ increases
 - Wage growth to outpace inflation in FY2024
- Population growth
 - Governor Noem's workforce recruitment campaign
 - Historically low unemployment
- Federal Stimulus Dollars
 - Water and wastewater projects are underway
 - Housing infrastructure dollars starting to flow
 - Infrastructure Investment & Jobs Act (IIJA) dollars starting to flow
 - Fed dollars spent in FY23: \$2.14 billion
 - Pre-COVID 10YR average: \$1.46 billion

Reasons lower state revenues in FY2024

- Decades low workforce participation rate
 - May 2023: 67.8%
 - May 2019: 69.3%
 - May 2004: 73.1%
- Higher core inflation
 - High inflation leads to decreased or negative consumer spending.
 - June Core Inflation 4.86% Y/Y

Revenue Outlook for FY2024



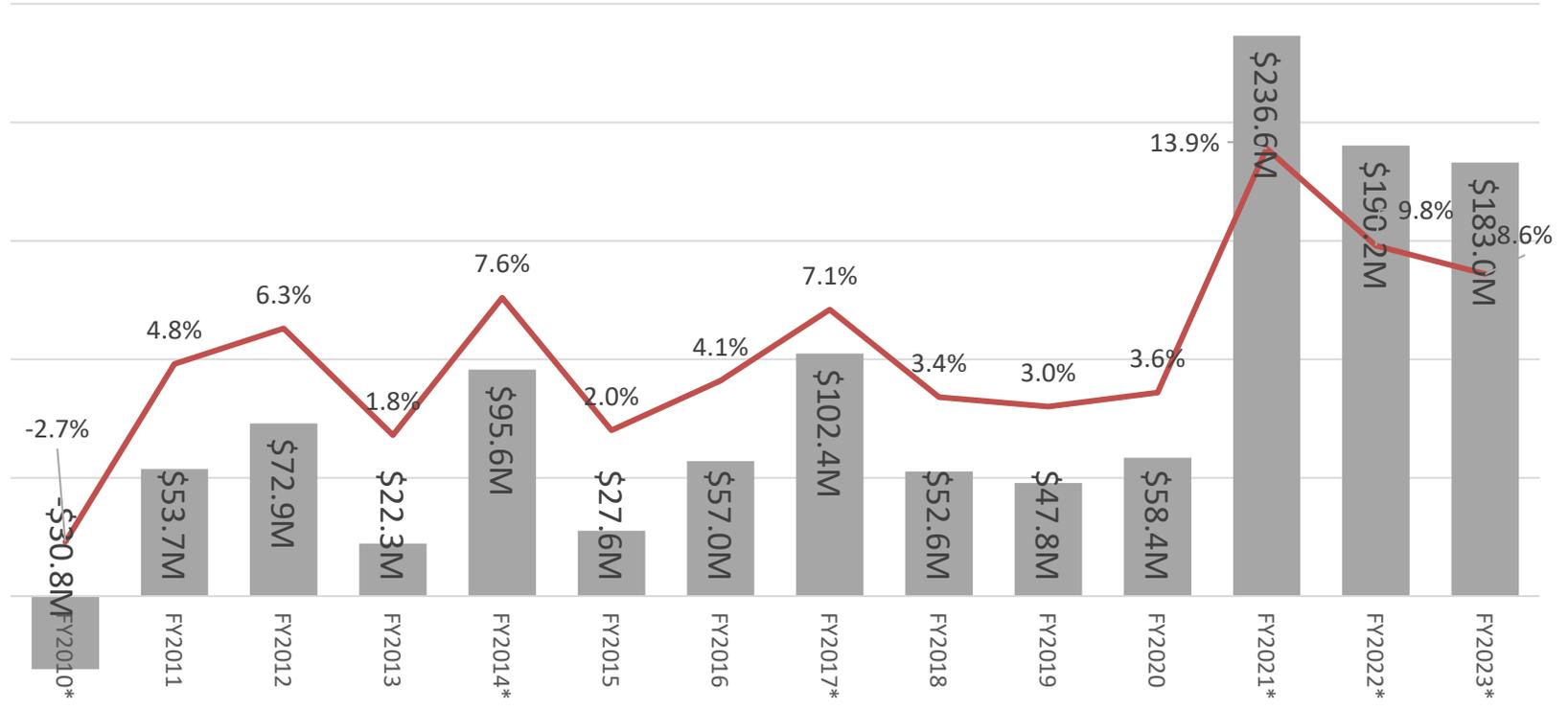
- Sales tax: Consumer demand remains strong, inflation remains elevated
 - LRC July Forecast: \$1,467.9 million; (0.9)% growth
 - Considers reduction in sales tax, 6.2% growth pre-reduction
- Contractor's excise tax to remain strong due to demand, inflation, and state stimulus dollars.
 - LRC July Forecast: \$203.3 million; 7.3% growth
- Lottery revenues likely to increase as wage growth outpaces inflation.
 - LRC July Forecast: \$187.0 million; 5.9% growth
- Insurance company tax receipts to remain elevated mainly because of inflationary pressures.
 - LRC July Forecast: \$117.8 million; 5.1% growth
- Tobacco revenues expected to continue to decline
 - LRC July Forecast: \$45.8 million; (2.7%) growth
- Unclaimed property revenue expected too higher than normal.
 - LRC July Forecast: \$66.3 million; (22.5%) growth
- LRC July on-going general fund revenue forecast of **\$2,346.2 million**.
- **1.6%** growth in on-going revenue over actual FY2023 when accounting for the reduction in sales tax.
- Pre-reduction growth rate of **6.2%** for on-going revenue over FY2023 actual.
- LRC July forecast is **\$12.1 million** more in total on-going revenue than the LRC Feb. forecast or a difference of 0.5%.
- Based on the updated revenue forecast, there is estimated to be **\$61.6 million** more dollars available to spend during the 2024 legislative session.

Revenue Outlook for FY2024



Yearly Growth of On-going General Fund Receipts

History of Actual On-going General Fund Receipts	\$ Y/Y Growth	% Y/Y Growth
FY2010*	(30.8)	-2.7%
FY2011	53.7	4.8%
FY2012	72.9	6.3%
FY2013	22.3	1.8%
FY2014*	95.6	7.6%
FY2015	27.6	2.0%
FY2016	57.0	4.1%
FY2017*	102.4	7.1%
FY2018	52.6	3.4%
FY2019	47.8	3.0%
FY2020	58.4	3.6%
FY2021*	236.6	13.9%
FY2022*	190.2	9.8%
FY2023*	183.0	8.6%
10-year avg.	105.1	6.3%
Average w/o Outliers	49.0	3.6%
FY2024 JCA Adopted	(60.3)	-2.8%
FY2024 Feb. LRC Forecast	129.5	5.6%
FY2024 July LRC Forecast	141.6	6.2%



*Outlier year

Amounts not adjusted for inflation
pre-reduction in sales tax

FY22 & FY23 Actuals and FY23 Estimate								FY24 Estimate				
Ongoing Receipts	FY22 Actual	Legislative Revised Adopted FY23 Estimate	FY23 Actual	FY23 Actual Over / (Under) Estimate	FY23 Actual % Over / (Under) Estimate	Adopted Growth over FY22	Actual Growth over FY22	Legislative Adopted (02/2023)	LRC Interim Revenue Estimate	LRC % Difference from Adopted	Legislative Adopted Growth % over FY23 Actual	LRC July Updated Revenue Growth % over FY23 Actual
Sales and Use Tax	1,356,844,793	1,487,500,000	1,480,572,850	(6,927,150)	(0.5%)	9.6%	9.1%	1,457,750,000	1,467,875,144	0.7%	(1.5%)	(0.9%)
Lottery	171,609,682	179,396,470	176,663,767	(2,732,703)	(1.5%)	4.5%	2.9%	185,788,211	187,076,913	0.7%	5.2%	5.9%
Contractor's Excise Tax	155,823,772	188,220,515	189,407,586	1,187,071	0.6%	20.8%	21.6%	195,000,000	203,262,868	4.2%	3.0%	7.3%
Insurance Company Tax	103,995,420	109,756,754	112,141,293	2,384,539	2.2%	5.5%	7.8%	114,432,223	117,813,522	3.0%	2.0%	5.1%
Unclaimed Property	65,097,628	71,281,179	85,536,039	14,254,860	20.0%	9.5%	31.4%	57,185,445	66,320,479	16.0%	(33.1%)	(22.5%)
Licenses, Permits & Fees	75,077,171	76,820,106	77,636,494	816,388	1.1%	2.3%	3.4%	77,267,444	79,610,039	3.0%	(0.5%)	2.5%
Tobacco Taxes	49,385,379	48,043,012	47,074,649	(968,363)	(2.0%)	(2.7%)	(4.7%)	46,560,484	45,797,260	(1.6%)	(1.1%)	(2.7%)
Trust Funds	43,495,271	46,540,322	46,259,458	(280,864)	(0.6%)	7.0%	6.4%	48,538,231	48,408,904	(0.3%)	4.9%	4.6%
Net Transfers In	25,279,507	24,354,780	25,652,534	1,297,754	5.3%	(3.7%)	1.5%	23,891,068	24,354,780	1.9%	(6.9%)	(5.1%)
Alcohol Beverage Tax	9,203,968	8,875,647	8,939,732	64,085	0.7%	(3.6%)	(2.9%)	9,272,874	9,020,694	(2.7%)	3.7%	0.9%
Bank Franchise Tax	22,511,850	19,110,103	20,425,082	1,314,979	6.9%	(15.1%)	(9.3%)	19,927,443	20,685,011	3.8%	(2.4%)	1.3%
Charges for Goods and Services	14,804,251	14,866,510	13,473,405	(1,393,105)	(9.4%)	0.4%	(9.0%)	15,273,363	13,592,045	(11.0%)	13.4%	0.9%
Telecommunications Tax	2,688,458	2,363,947	2,466,873	102,926	4.4%	(12.1%)	(8.2%)	2,047,035	2,153,806	5.2%	(17.0%)	(12.7%)
Severance Taxes	8,033,942	6,939,293	5,657,605	(1,281,688)	(18.5%)	(13.6%)	(29.6%)	8,170,526	7,875,676	(3.6%)	44.4%	39.2%
Investment Income and Interest	19,648,565	13,970,769	14,000,549	29,780	0.2%	(28.9%)	(28.7%)	20,334,000	49,207,968	142.0%	45.2%	251.5%
Alcohol Beverage 2% Wholesale Tax	2,909,711	3,089,592	2,936,973	(152,619)	(4.9%)	6.2%	0.9%	3,202,359	3,155,886	(1.5%)	9.0%	7.5%
Total Ongoing Receipts	2,126,409,366	2,301,128,999	2,308,844,888	7,715,889	0.3%	8.2%	8.6%	2,284,640,706	2,346,210,995	2.7%	(1.0%)	1.6%

4-8A-16. Submission of independent projections by Bureau of Finance and Management and Legislative Research Council--Proposals for eliminating shortfall. The Bureau of Finance and Management and the Legislative Research Council shall prepare and submit, no later than July thirtieth of each year, independent projections that conform with the provisions of subdivisions 4-7-10(2) and (5) to the Governor or the Governor's designee and the committee created by this chapter. Notwithstanding the provisions of subdivisions 4-7-10(2) and (5), the projections shall contain information of actual revenue for each of the two fiscal years last concluded and the estimated revenue of the current fiscal year.