North Carolina General Fund Revenue Consensus Forecast: June Revision

Forecast Highlights

Forecast Revised Upwards
The revised forecast is more positive than the February forecast on all fronts, projecting revenue increases in the current fiscal year and in both years of the biennium

FY 2020-21 Revenue
Current year revenue is expected to be $1.9 billion over the projections from February.

Recent Revenue Surge
Most sources of revenue have strongly exceeded expectations in the current fiscal year. Additional Federal stimulus, falling COVID-19 infections, and easing of business restrictions have contributed to the surge.

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The Fiscal Research Division and the Office of State Budget and Management have reached a consensus on a revised revenue forecast for the 2021 biennium.

Revenue collections have surged since the February 2021 forecast. This June 2021 forecast expects FY 2020-21 collections to be $29.5 billion, which is $1.9 billion higher than the prior forecast. With this increase, current year General Fund revenue is expected to be 23.3% greater than FY 2019-20 collections. Some of the increase is due to the delayed payment and tax filing deadlines in calendar year 2020, which shifted an estimated $1.1 billion in tax collections from FY 2019-20 into FY 2020-21. After controlling for this shift, the forecast expects growth of 13.6% in the current fiscal year.

We expect solid revenue growth of 8.0% over the upcoming biennium. The February forecast expected growth of 7.3% over that period, with 3.1% growth in the first year (after adjusting for the delayed payments in 2020) and 4.1% in the second. We now expect faster growth in the first year (4.5%), and slower growth in the second (3.4%). The acceleration in expected growth comes from a faster than expected economic recovery.

June 2021 Revised General Fund Consensus Summary ($ in Millions)

Fiscal Year	February 2021 Forecast	June 2021 Revised Forecast	Change
2019-20 (actual)	$23,939.3	n/a	n/a
2020-21	$27,602.6	$29,509.3	$1,906.7
2021-22	$27,350.6	$29,705.4	$2,354.8
2022-23	$28,461.5	$30,707.2	$2,245.7

Current Fiscal Year Revenue

Revenue collections for FY 2020-21 are projected to surpass the February 2021 forecast by $1.9 billion (6.9%), with most sources of revenue strongly exceeding expectations. The February forecast already anticipated overcollections of $4.1 billion for this fiscal year, bringing total overcollections for FY 2020-21 to a stunning $6.0 billion relative to the May 2020 forecast. The rapid onset of the revenue surge and the unprecedented nature of the recent pandemic-driven downturn make it difficult to identify the cause of the significant surplus, but we believe several factors contributed:

- COVID-19 infections have fallen and business restrictions have been loosened more quickly than expected.
- The February forecast anticipated another round of federal relief, but the timing and size of that relief was unknown. The actual relief package passed by Congress in March 2021 was larger than we expected.

- North Carolina continues to experience a "K-shaped" recovery, in which higher-income households have fared better than lower-income households. This type of recovery, which we described in the February report, has led to a smaller revenue drop than under a typical economic downturn; tax revenue now appears to have been even more resilient than anticipated.

K-Shaped Recovery Continues
Higher-income households have fared better than lower income households, leading to tax revenues that have been more resilient than anticipated.

As we noted in February, personal income tax collections from final payments–typically due in mid-April–are difficult to predict because income from dividends, capital gains, and businesses can result in sizable swings in collections, which we refer to as the "April surprise." This year, we had a very large "surprise," with final payments exceeding expectations by over $400 million. Because the tax filing deadline was postponed to mid-May, it was more of an "April to May surprise."

"April/May Surprise"
Final personal income tax payments exceeded expectations by over $400 million.

Personal income tax withholding on wages and salaries and first quarter estimated payments also greatly exceeded expectations. Through January, withholding revenue was up 4.2%, and the last forecast expected that trend to continue; however, withholdings are up 7.5% through May. Further, collections data show significant strength in corporate income tax revenue compared to the February estimates. For the current fiscal year, we are now projecting 58.0% growth in shift-adjusted corporate income tax collections.

Rebound in Spending
Sales tax collections are stronger than expected due to a quicker and larger rebound in consumer spending.

The rebound in consumer spending has come sooner and has been larger than we expected, leading to sales tax collections that are considerably stronger than anticipated. We believe this rebound has been fueled, at least in part, by federal stimulus payments distributed in March.

Outlook for the Upcoming Biennium

Economic Outlook
Short-term economic growth outlook has improved as the pace of the economic recovery has quickened.

The State's economy remains in the recovery phase of the business cycle, but the short -term growth outlook has improved. This forecast projects a faster economic recovery than the February forecast. The increased pace of recovery should positively impact most revenue sources over the biennium. Overall, this forecast increases the February forecast by $2.35 billion for the first year of the biennium and $2.25 billion for the second year of the biennium.

Biennium Forecast
Growth in revenue over the biennium is forecasted at 8.0%, up from 7.3% in February's forecast.

Sales tax collections are a major driver in the revised forecast for the biennium. Consumers, at least in aggregate, have accumulated significant savings since the pandemic began. This forecast expects consumers to spend down their savings, providing a boost to sales tax revenue. Compared to the February forecast, this forecast estimates an accelerated recovery in consumer spending in FY 2021-22, with slower growth in FY 2022-23. Relative to the previous sales tax estimates, these estimates are higher by $790.6 million in FY 2021-22 and $607.8 million in FY 2022-23.

Due to the unexpectedly large growth in corporate income tax collection in the current year, future year revenue will be growing from a higher starting point. Thus, we have increased expected corporate income tax growth in the first year of the biennium, with collections now expected to exceed the February forecast by $433.0 million in FY 2021-22 and $433.1 million in FY 2022-23.

Growth rates for personal income tax are expected to be only marginally higher in both years of the biennium when compared to the February forecast. But because personal income tax is such a large source of revenue, small percentage gains lead to significant collection increases. These estimates have been increased by $931.8 million in the first year of the biennium and $1,044.3 million in the second year of the biennium, relative to the previous estimates.