Economic Summary; Volume IX

Week of June 12, 2020

Tennessee Economy in General

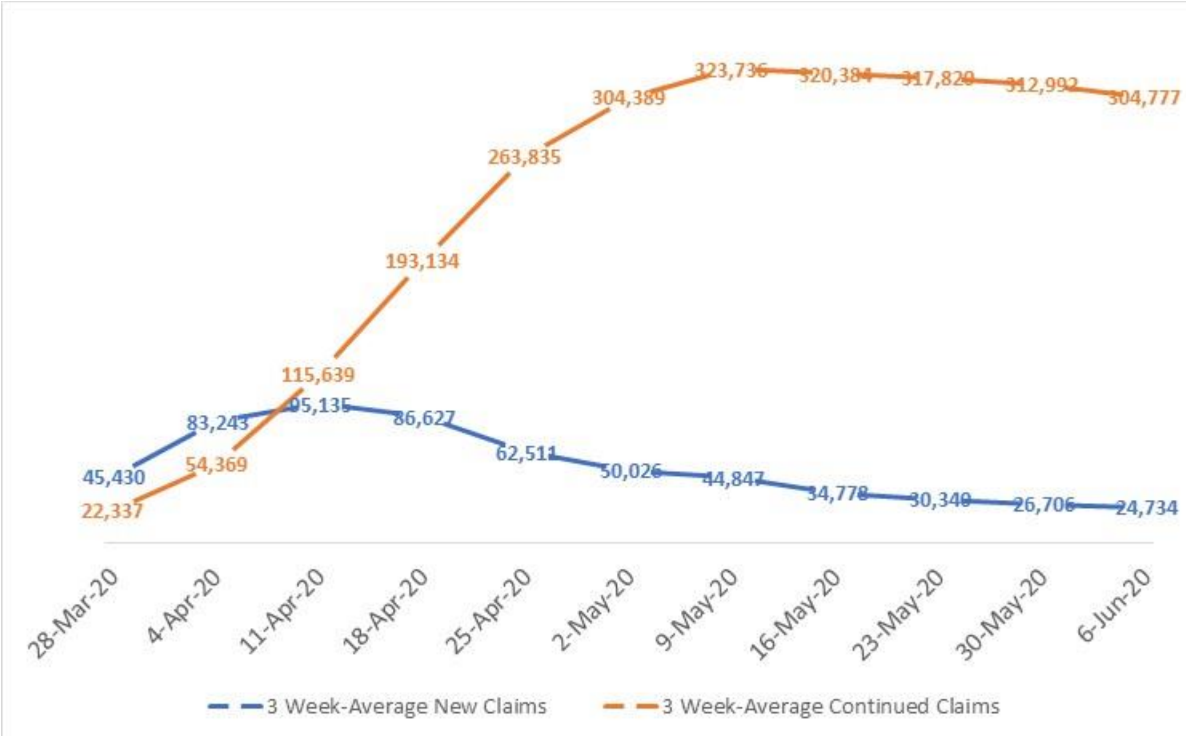
The state released May revenue collections (representing April activity) this week. This report revealed the depths of the pandemic's impact on tax revenues and retail purchases. Revenues fell dramatically. Each major fund under-collected expectations. The general fund was short 15%; the highway fund was short nearly 33%; and the city-county (state shared revenue) fund, which is largely driven by sales and fuel taxes, was short by 27%.

Year-to-date, year-over-year revenues were effectively flat. The $308 million general fund shortfall was almost entirely driven by large under-collections in the two business taxes and the Hall Income tax which are collectively short by nearly $347 million. The state delayed collection of these three tax sources until July 15 so much of this variance may eventually be collected; however, business tax revenue collection may depend on whether businesses resume operations. Collectively, the Highway Fund fuel tax revenue sources (gasoline and motor fuel/diesel) increased by nearly 5.8% to-date.

The State Senate passed an amended budget this week. The spending plan for the fiscal year beginning July 1, 2020 and ending June 30, 2021 was reduced by nearly $500 million from the revised plan passed in mid-March. State pay increases for state, higher education and local education employees were eliminated, and the legislature provided a $50 million one-time appropriation for an employee buy-out program. Additional cuts were not specified and will likely be the product of the operational efficiency review of state agencies. The House of Representatives is expected to act next week.

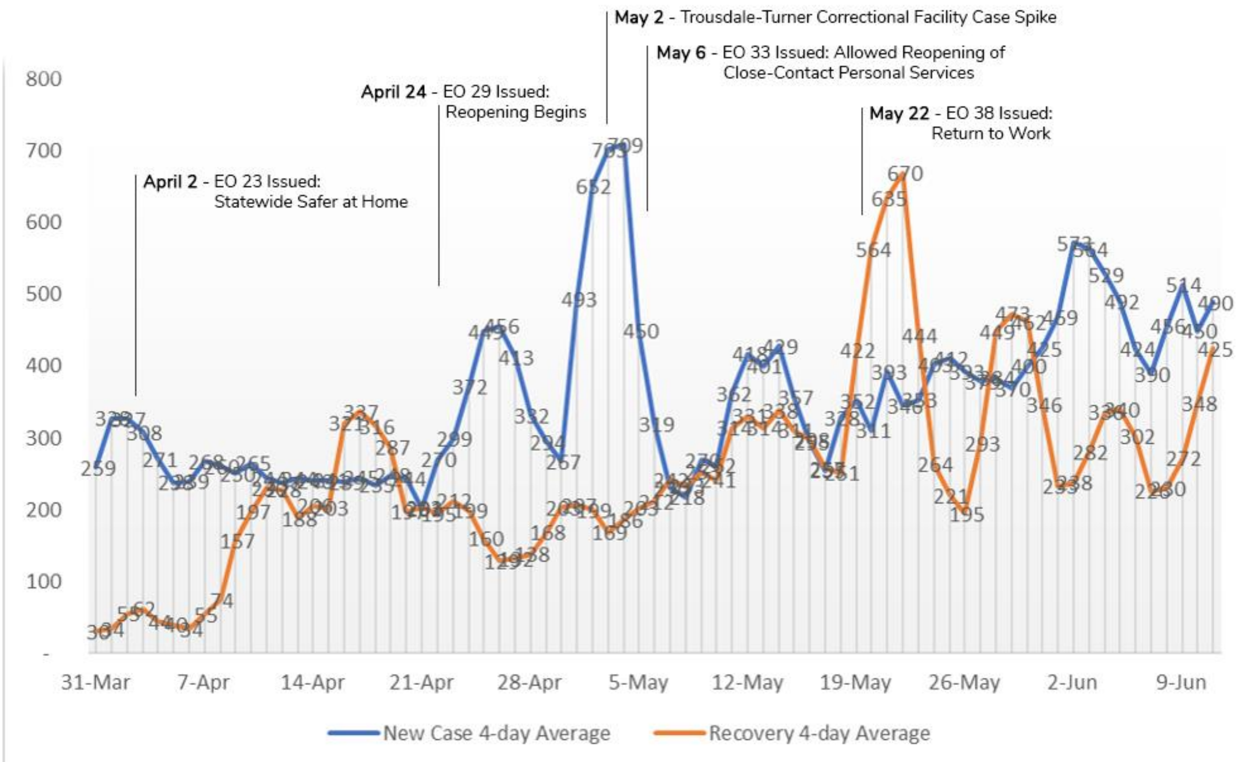
Last week's data suggested that new unemployment claims have moderated and continuing claims flatlined. The Tennessee Department of Labor and Workforce Development Weekly New Unemployment Claims reported a slight week over week reduction in new claims. New unemployment claims increased by 21,417 for the week of June 6 compared to 22,784 for the week prior. Chart 1 shows that average Continuing Claims fell slightly again as the labor market appears to be re-hiring.

Chart 1: Three-Week Moving Average New and Continued Claims



COVID-19 cases increased dramatically last week. According to statistics from the Tennessee Department of Health and COVID-19 Unified Command, the state confirmed 3,220 new cases and 2,279 recoveries during the 7-day period ending May 14. Over a 14-day period, new cases exceeded new recoveries by more than 55% (6,661 new cases vs 4,290 recoveries). Since the beginning of March, over 535,000 have been tested. The University of Tennessee's CORE-19 team estimated that active cases increased week over week from 8,115 to a new all-time high of 8,977 which is approximately 1.31 per 1,000 Tennessee residents, effectively a week over week increase of one active case for every 10,000 residents. In addition, the 7-day average positivity rate remained 6% as of June 11. Chart 2 shows that cases continue increasing faster than recoveries.

Chart 2: 4-Day Average New Case and Recovery Data with Key Dates



Local Government Revenues and Budgeting

The Tennessee State Senate passed an amended budget this week. This amended budget included the $200 million grant program for local governments from the March budget amendment (split 50/50 between cities and counties). Despite some opposition, the legislature effectively removed all prior proceed usage restrictions from the program. The grant program proceeds may now be used to offset revenue shortfalls from COVID. This may be a welcome change for many cities and towns as the May Collections Summary showed deep losses and under-collections for many tax sources in many county areas. Each city and town's allocation may be found HERE.

Sales and Business Taxes

According to the Department of Revenue's May Collections Summary, local government revenue collections did not perform much differently from the state. The local option sales tax fell by $19.4 million, or nearly 8.2%; the local business tax fell by $5.6 million, or more than 13%; and, local highway fund revenues (gasoline and motor fuel/diesel taxes) fell by an estimated 28%.

State collected local revenues fell in many counties. April 2020 local option sales tax revenue fell in eleven counties when compared to April 2019. Year to date, only one county collected less local option sales tax revenue than the year prior. When adjusted for reductions in the "Out-of-State" situs, the number of counties with year over year reductions was higher. April 2020 business tax collections fell in 46 counties compared to April 2019. Year to date, 90 counties collected less business tax revenue than the same time in 2019. The state delayed collection of the business taxes until July 15 so much of this negative variance may eventually be collected in many counties; however, business tax revenue collection may depend on whether businesses resume operations. Municipal level collections information is not currently available and will be discussed in future economic summaries.

Hotel-Motel Taxes

State sales tax collections attributed to hotel and lodging sales fell by more than $22.5 million, or nearly 84%, for the month of May (April activity). Thus, local governments lost local option sales tax revenues on hotel stays; and, as discussed in a prior Economic Summary, local governments lost hotel-motel tax revenues as many levy a 5% tax on lodging stays. As Table 1 shows, for the months of March and April, local governments lost an estimated $40 million in sales and lodging tax revenues.

Table 1: Total Revenue Loss on Lodging Stays, March 2020 & April 2020

March 2020

	Sales Tax Collections	Sales Rate	Estimated Sales	Hotel-Motel Rate	Estimated Hotel-Motel	Total Difference
State Collections	(14,188,313)	7%	(202,690,186)	0.00%	-	(14,188,313)
Local Collections	(5,573,980)	2.75%	(202,690,186)	5.00%	(10,134,509)	(15,708,489)

April 2020

	Sales Tax Collections	Sales Rate	Estimated Sales	Hotel-Motel Rate	Estimated Hotel-Motel	Total Difference
State Collections	(22,535,049)	7%	(321,929,266)	0.00%	-	(22,535,049)
Local Collections	(8,853,055)	2.75%	(321,929,266)	5.00%	(16,096,463)	(24,949,518)

Anecdotal evidence and public statements suggest that the lodging industry may not recover quickly. Many hotels were closed through May, and some remain closed today. Next month’s report reflecting May activity may reveal additional loss. Local governments should anticipate minimal lodging revenues for the current quarter and dramatically lower-than-normal lodging revenues in subsequent quarters as travel appetite may be diminished.

Eating and Drinking Taxes

COVID-19 closed restaurants and bars across the state. The dining industry was effectively crippled for weeks. Some of these purchases migrated over to food store purchases; however, many disappeared and to some extent multiple revenue sources were impacted as state and local governments collect sales tax on purchases as well as liquor by the drink tax on mixed drink purchases.

As discussed in prior summaries, the liquor-by-the-drink (LBD) or mixed drink tax is an elective revenue source for local governments with 75% of revenues dedicated to education (half stays with the state and one-half of the second-half goes to the local education agency). The collections summary was bleak. Year over year, May’s 2020 LBD collections were 90% below May of 2019. This reduction was on top of the 60% reduction in April. Total year over year LBD revenue reductions exceeded $18 million. Table 2 suggests that nearly $121 million less was spent on mixed drinks in March and April of 2020 than was spent in March and April of 2019.

Table 2: Cumulative Liquor-by-the-Drink Tax Revenue Summary for April and May

	LBD Revenue Losses
April '20 Over (Under) April '19.......................	(7,710,524.13)
May '20 Over (Under) May '19........................	(10,433,610.02)
Total Two-Month Over (Under).......................	(18,144,134.15)
First Half to BEP...	(9,072,067.08)
One-half of Second Half to LEA........................	(4,536,033.54)
One-half of Second Half to Situs......................	(4,536,033.54)
Estimated LBD Actual Sales Lost (15% rate).......	(120,960,894.33)

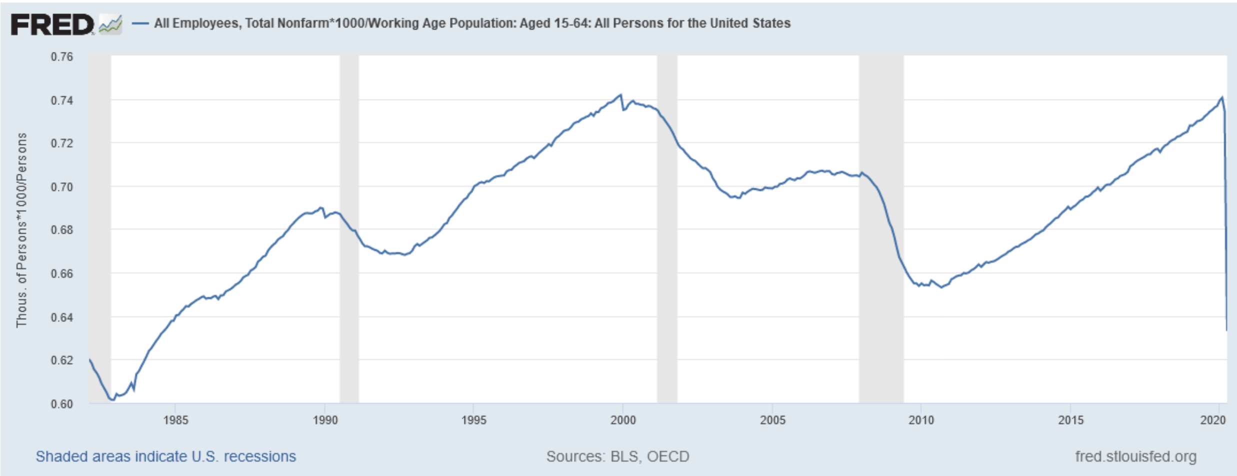
The liquor-by-the-drink tax is a situs-based tax so some municipalities (and thus either city or county school systems) will experience dramatic revenue shortfalls while other municipalities may not lose much revenue. Additionally, the tax rate is prescribed in state law and cannot be reduced. It should be noted that these potential revenue losses would be solely attributed to the economic circumstances and independent of any local decisions.

Macro-economic Commentary

In the wake of last Friday's news that the U.S. economy added 2.5 million jobs in May and that the unemployment rate dropped from 14.7% to 13.3%, Republicans in the U.S. Senate have coalesced around the idea of delaying further consideration of additional coronavirus relief legislation. Senate Republicans contend more time is needed to evaluate the impact of the nearly $3 trillion already obligated and its' effect on businesses, the workforce and the overall economy. On Tuesday, several pivotal Republican senators echoed one another's predictions that the next bill won't happen until late July. Republican leaders also indicated that prior to the commencement of any negotiations with Democrats on another relief package, they must first reach agreement within their caucus on the questions of unemployment insurance and financial assistance for state and local governments.

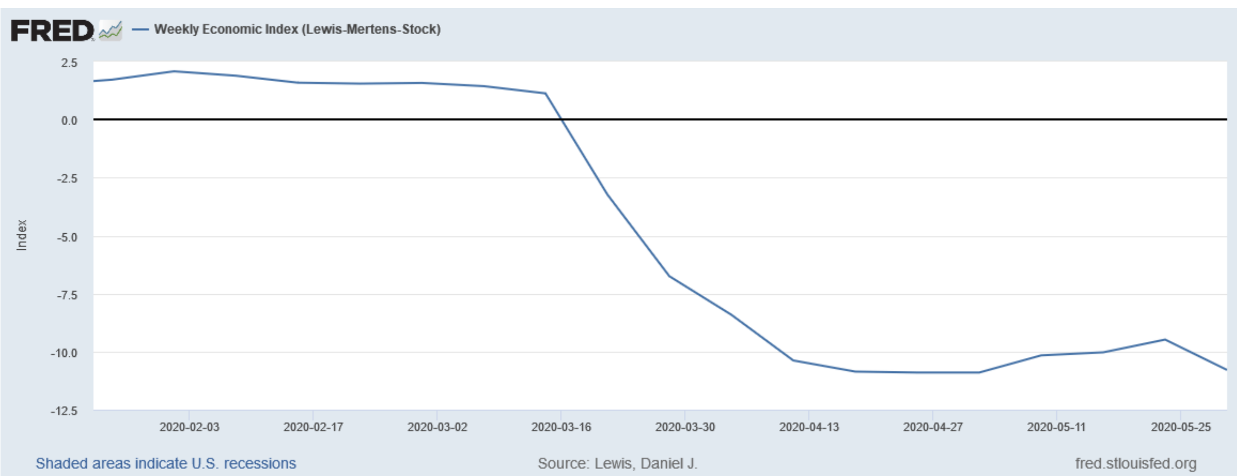
Weekly new unemployment claims continued at unprecedented levels. The U.S Department of Labor reported another 1.5 million new weekly claims for the week ended June 6. The total number of people claiming unemployment benefits from all programs for the week ending May 23 fell by 662,256 to 29.5 million. In addition, Chart 3 shows the true depths of the employment situation as the employed share of working age people fell from the second highest all-time reading of 0.7405 to a nearly 40 year low of 0.633 in one month.

Chart 3: All Employees as a Percent of All Working Age Population (Ages 15-64)



The Weekly Economic Index (WEI) fell and nearly matched a historic low this week. The Federal Reserve Bank of New York stated that the decline was driven by falling retail sales and a decrease in consumer confidence. The WEI is a real-time estimate of the potential annualized GDP growth rate. Thus, as Chart 4 shows, last week's data series suggested that GDP will fall by 10.8% this year. A decline of that magnitude would exceed any reading post-1932.

Chart 4: Weekly Economic Index



Understandably, COVID weighed heavily on international trade. Both United States imports and exports fell by the largest amounts in recorded history in April. April was the worst month for goods exports since September 2009, service exports since January 2012, and total imports since July 2010. As Chart 5 shows when adjusted for inflation (Consumer Price Index), the April 2020 seasonally adjusted exports were roughly equivalent to pre-February 2006 levels (absent a one-time reading in April 2009). As world economies re-open, businesses and governments anticipate trade to return and supply chain issues to alleviate.

Chart 5: Seasonally Adjusted Monthly U.S. Exports and Imports, Adjusted for Inflation