

MEMORANDUM FOR THE RECORD

DATE: October 18, 2018
Room 112, Solomon Blatt Building
10:50am

SUBJECT: Minutes of Board of Economic Advisors Meeting

ATTENDEES: *Board Members* –Edward Grimball-Chairman, Howell Clyborne, Emerson Gower, Hartley Powell; *Executive Director*, Frank Rainwater; *Staff* – Robert Martin, Karen Rhinehart, Lisa Jolliff, Ellen Mitchell, Allyn Powell, Gordon O. Shuford, Kenneth Harris, Sidra Nelson, Mary K. Miller, Sandra Kelly, David Patterson, Paul Athey. *Guests* – John Barfield, Michael Moore, Kathy Johnson, Eddie Gunn (Comptroller General’s Office); Kevin Kibler (State Treasurer’s Office); A.J. Newton, Sarah Hearn (Ways and Means); Don Hottel (House Research); Meredith Cleland, Tim Derrick (Department of Revenue); Craig Parks (USC).

Press:

- I. Chairman Grimball welcomed everyone to the meeting at 11:05am.
- II. Chairman Grimball presented the meeting minutes for September 25, 2018 which had previously been shared with the Members and asked if any Member had additions or corrections. There were no comments from the Members and Chairman Grimball declared the minutes approved as presented. *(See attached)*
- III. Frank Rainwater presented an overview of first quarter results. **His major comments were:** *(See Attached)*
 - **Through the first quarter of FY 2018-19, General Fund Revenues grew 8.4 percent and exceeded the first quarter estimate by \$94.6 million.**
 - **Growth was driven by biennial licensing collections, audits, and timing issues.**
 - **The FY 2017-18 revenue surplus is contributing to the current revenue excess but any adjustment to the forecast will be made in November when all economic and fiscal issues will be considered.**

IV. Robert Martin presented an economic outlook. His major comments were:
(See Attached)

Preliminary FY 2019-20 General Fund Revenue Forecast

- Review of General Fund Revenues – September 2018
- Review of Base Economic Assumptions for FY 2018-19 (Current FY)
- Economic Assumptions for Revised Forecast (FY 2018-19) and FY 2019-20 General Fund Revenue Forecast
 - Economic Growth
 - Personal Income
 - Employment
 - Contingencies
 - Legislative Offsets/Adjustments

Total General Fund Revenue

- General Fund Revenue increased 8.3 percent during the month of September 2018 from September 2017
 - Biennial collection of insurance agent’s licenses.
 - A large increase in Corporation Income Tax declarations.
 - Strong showing in a variety of Other Revenues due to comparisons with one year ago when the Department of Revenue transitioned to a new computer system.
- Revenues have grown 8.8 percent year-to-date.

Sales Tax Revenue

- Sales and Use Tax revenue increased 5.7 percent for the month of September resulting in year-to-date-growth of 5.0 percent.
- The retail sales tax posted its best monthly mark since this past holiday season nine months ago.
- The cumulative Sales and Use Tax revenue growth through September is running ahead of the 3.7 percent revenue forecast for FY 2018-19.

Individual Income Tax Revenue

- The Individual Income Tax revenue decreased 0.6 percent during the month of September mainly from two events:
 - A \$7.1 million transfer out of the Individual Income Tax withholdings to the Department of Commerce for the State Rural Infrastructure Fund occurred in September 2018. This same transfer occurred last year in August 2017.
 - Also, the Department of Revenue transitioned to a new Individual Income Tax computer system in September 2017. During that month, the number of Individual Income Tax refunds processed and paid to taxpayers during the month of September 2017 were constrained. This resulted in an unusually large refund comparison in September

2018 causing the Individual Income Tax revenue category to be understated.

- Total Individual Income Tax revenue growth is 4.8 percent year-to-date through September and is well above the 0.4 percent revenue forecast for FY 2018-19.

Corporate Income Tax Revenue

- Corporate Income Tax revenue increased 43.8 percent in September
- Increase in Corporation Income Tax declaration payments of \$21.6 million
- The Corporation Income Tax has increased 68.4 percent through the first quarter of FY 2018-19, primarily from the settlement of a single audit payment for \$11.4 million received in August and stronger than expected tax declarations in September.

Other Tax Revenues

- Other Revenues were also largely affected by the transition and implementation of a new computer system at the Department of Revenue in September 2017 that caused many of the Other Revenue categories to be artificially understated.
- This caused artificially large comparisons in September 2018. These large monthly swings in Other Revenues should become ameliorated in coming months.
- Other Revenues increased 42.1 percent in September 2018 from one year ago, and have increased 32.8 percent year-to-date from a variety of sources and timing of receipts.
- The licensure of insurance agents and brokers are paid every two years with the majority of the licenses coming due in odd-numbered fiscal years. This was the case this fiscal year with Insurance Tax revenue up 35.0 percent through the first quarter of the fiscal year.
- Other Revenues have also benefitted from continued strong Interest Earnings on state General Fund investments, the documentary stamp tax (real estate deed tax), and the bank tax.

September 2018 Summary

- Through the first three months of FY 2018-19, General Fund revenues have increased 8.8 percent and are trending above the growth rate of 1.5 percent needed to meet the estimate for FY 2018-19.
- Pursuant to Section 11-9-890, total General Fund revenue collections through the first quarter of FY 2018-19 have exceeded the quarterly revenue estimate. At this time, no adjustments are warranted.
- The current Board of Economic Advisors' (BEA) revenue forecast is based upon an employment growth rate of 1.8 percent and a personal income growth rate of 4.25 percent in FY 2018-19.

- Revised state personal income figures released in September exhibited more strength than in previous income estimates supporting that the economy is somewhat stronger than previously believed.
- The BEA will meet with its Regional Advisory Committee in October 2018 to receive input concerning the health of the state economy and tax revenues from a group of business leaders and academics.
- The BEA will then adopt and release a revised General Fund revenue forecast for FY 2018-19 and a preliminary General Fund revenue forecast for FY 2019-20 in November 2018.

Contingencies and Other Items of Concern

- Legal Decisions
 - Tax conformity
 - Wayfair decision (internet sales)
 - Sports betting (no legislation has been filed)
- Revenue and Economic Issues of Concern
 - Capital gains and the stock market
 - Effect of Trump tax change
 - Oil prices and OPEC
 - Tariffs (China retaliation; doubling tariffs for Turkey)
 - European debt crisis
 - Value of dollar
 - Retail sales
 - Housing market
 - Flattening of the yield curve spread
 - Disaster tax relief for Hurricanes Florence and Michael

Base Economic Assumptions for FY 2018-19 and FY 2019-20

- Gross Domestic Product
- South Carolina Personal Income
- South Carolina Employment
- Inflation
- Federal Reserve meeting – next meeting on November 7th – 8th

~Mr. Martin commented that the change in the labor force in South Carolina is the cornerstone of his forecast. Full-employment has already been achieved and the rate of growth is beginning to slow. There needs to be an increase in better jobs for people to move in to- there is a skills problem and a large amount of under-employed people in the state.

Legislative Offsets

- Legislative Offset and Adjustments to General Fund Revenue Estimates in FY 2018-19 and FY2019-20
- See attachment (preliminary)

~Mr. Martin commented that it has been ten years since the last recession-the longest expansion on record. All interest rates are beginning to rise-possibly as much as one percent more. This expansion will start to come to an end - possibly in 2020. Global growth is beginning to slow as well.

V. Other Business

There was no further business or comments from the Working Group Members.

Chairman Grimball recessed the meeting for a lunch break which will be followed by the Annual Regional Advisory Committee Meeting beginning at 12:45pm.

The next scheduled BEA Meeting is Thursday, November 8, 2018 at 2:00pm.

Attachments: Agenda, Meeting Materials

Public Notice of this meeting was posted at <http://www.rfa.sc.gov/calendar>

These minutes were approved on 11/8/18.

Karen Rhinehart
Karen Rhinehart

MEMORANDUM FOR THE RECORD

DATE: October 18, 2018
Room 112, Solomon Blatt Building
12:45pm

SUBJECT: Board of Economic Advisors Annual Regional Advisory Meeting

ATTENDEES: *Board Members* - Edward Grimball - Chairman; Howell Clyborne, Emerson Gower, Executive Director, Frank Rainwater; *Staff* - Robert Martin, Lisa Jolliff, Karen Rhinehart, David Patterson, Paul Athey, Amanda Martin, Sandra Kelly, Mary K. Miller, Sidra Nelson, Lisa Wren, Ellen Mitchell, Kenneth Harris, Gordon O. Shuford; *Guests* - Eddie Gunn, Michael Moore, John Barfield, Kathy Johnson (Comptroller General's Office), AJ Newton, Sarah Hearn (W&M), Joe Boyle, Brian Ford (SC Education Lottery), Kevin Kibler (Treasurer's Office), Andy Beeson, Samantha Allen, David Good, Ashley Harwell-Beach (Legislative Council), Ted Pitts (SC Chamber of Commerce), Russ Sobel-The Citadel, Joe Von Nessen-USC, Matt Martin-Federal Reserve Bank, Frank Hefner-College of Charleston (Regional Economic Advisors).

- I. Chairman Grimball called the meeting to order at 12:48pm.
- II. Frank Rainwater provided a review of SC personal income growth and introduced this year's Regional Advisory Committee speakers. *(See Attached)*
- III. Presentations were given by Regional Advisory Committee Members. *(See attached)* Their key forecast assumptions were:

Dr. Matthew Martin - *Regional, Banking*
Senior Vice President, Federal Reserve Bank of Richmond
Dr. Martin's estimates were:

Personal Income	FY 2018-19 - 4.30%	FY 2019-20 - 4.00%
Employment	FY 2018-19 - 1.80%	FY 2019-20 - 1.50%
Inflation	FY 2018-19 - 2.30%	FY 2019-20 - 2.10%

~During Dr. Martin's presentation, he stated that he sees a gradual deceleration in the growth rate of e GDP ending the year at 3 percent. This is due to consumer spending and income and growth in core capital goods. He also said that the labor force participation is dropping off for South Carolina - it's harder to find workers.

~He sees inflation at a 2 percent target. This is due to energy prices and tariffs and may run over the 2 percent target over the next year.

~There will be a gradual slowing of the economy and labor market.

**Chairman Grimball asked if Dr. Martin views each state differently. Dr. Martin replied that South Carolina is heavy on manufacturing with significant exports but the trade situation needs to be monitored as it is a stand-out.*

~He does not see any significant sleeper issues.

Mr. Mark Vitner - *Regional, Banking*
Managing Director and Senior Economist - Wells Fargo Securities
***Mr. Vitner was unable to attend - Robert Martin presented Mr. Vitner's information**
***No regional information was provided**

- ~Regarding the U.S. outlook, the economy will be at full employment before gradually losing momentum in 2020.
- ~The GDP growth will be 2.9 percent in 2018, 2.8 percent in 2019, and dropping to 2.2 percent in 2020. The forecasted real GDP will be 3.3 percent in the third quarter of 2018.
- ~Consumer spending is strong and consumer confidence remains high.
- ~Regarding international trade, the second quarter of 2018 export growth added to the GDP growth.
- ~With the strong labor market and inflation above the 2 percent target, the Federal Reserve will increase the federal funds rate one quarter point in each of the next four quarters. Economic growth will slow.
- ~The global growth is solid and steady. The second quarter of 2018 for G20 countries is at 3.9 percent. Global growth will be 3.7 percent in 2019, and 3.4 percent in 2020.
- ~Two visible problems are trade tensions with China, and other G7 countries' economies are slowing. A point of optimism is the U.S., Canadian, and Mexican trade deal.
- ~The U.S. growth has been strong boosted by tax cuts.

Dr. Joseph Von Nessen - *Regional, Academia*

Research Economist, University of South Carolina, Darla Moore School of Business

Dr. Von Nessen's estimates were:

Personal Income	FY 2018-19 – 4.20%	FY 2019-20 – N/A
Employment	FY 2018-19 – 1.70%	FY 2019-20 – N/A
Inflation	FY 2018-19 – 2.50%	FY 2019-20 – N/A

- ~During Dr. Von Nessen's presentation, he shared more of a local rather than a national perspective.
- ~The U.S. and S.C. economies are stable overall. Looking ahead to a GDP growth rate of 4.2 percent- this will continue. Personal consumption expenditures are fairly stable which is the largest share of GDP. For 2019, he would like to see private investment growth of 3.0 percent. Private investments are growing as a result of the tax cuts. Small business confidence is very high. There is also an uptick in labor force participation.
- ~In S.C., the employment growth is the best measure to use for the health of the state's economy and is comparable to the GDP on a national level. Labor and lumber are concerns in construction but the housing demand is still strong due to steady wages, growth, and employment. The automotive industry is significant in S.C. and the tariffs could have an effect-not certain at this point. United States, Mexico, Canada Agreement (USMCA) may mean more production at home and less shipping.
- ~Companies are moving towards using bonuses to reward employees instead of raises. Employees can be retained longer and layoffs avoided if there is a downturn when bonuses are used.
- ~Overall, there is strong national growth, consistent consumer spending, and broad growth across S.C. sectors.

Dr. Frank Hefner - *Regional, Academia*

Professor of Economics, Director of Office of Economic Analysis, College of Charleston

Dr. Hefner's estimates were:

Personal Income	FY 2018-19 – 4.25%	FY 2019-20 – 4.25%
Employment	FY 2018-19 – 1.80%	FY 2019-20 – 1.80%
Inflation	FY 2018-19 – 2.50%	FY 2019-20 – 2.70%

- ~Dr. Hefner presented his information from a different perspective. He compared the economy in the 1960's to the economy of today. He feels our economy accommodates random policy behavior and that it is not as fragile as he once thought. For example, the second NAFTA version has not affected the U.S. economy much differently than the first version. Hurricanes have not changed the economy of S.C.

~According to the Wall Street Journal, the unemployment rate is the lowest it has been in 50 years. However, in S.C. there are labor issues. It is difficult to find individuals to work in the food industry.
 ~He compared 1968 and 2018. In 1968 “foreign companies” were from other states; now companies that invest in the U.S. are truly international. There are more tariff issues and trade problems. In the 1960’s inflation was 6 percent; inflation at this time is modest. In the 1960’s the U.S. was fighting the Vietnam war and the war on poverty; now the U.S. does not have those particular issues.

**Chairman Grimball paused the meeting at 2:13 for a 10-minute break following Dr. Hefner’s presentation.*

**The meeting resumed at 2:20 and Dr. Sobel presented his information.*

Dr. Russell S. Sobel - *Regional, Academia*

Professor of Economics and Entrepreneurship, The Citadel

Dr. Sobel’s estimates were:

Personal Income	FY 2018-19 – 5.10%	FY 2019-20 – 4.70%
Employment	FY 2018-19 – 1.82%	FY 2019-20 – 1.56%
Inflation	FY 2018-19 – 2.28%	FY 2019-20 – 2.30%

~The final Advisory Committee Member to present information was Dr. Russell Sobel.

~Dr. Sobel began by stating that forecasting is a science. Different forecast methods are used and the average is used to create the forecast. He uses two different methods: the simple average (mean average) and the Olympic average (discarding the high and low forecasts). Last year, the Olympic average came closer to 3 of 5 variables. The average is more accurate than each individual forecast. Economists forecast real variables and revenue is based on the dollar value of sales.

~The S.C. economy is tied to the U.S. economy and relies on three major forecasts: IMF World Economic Outlook, Federal Reserve Bank of Philadelphia’s Livingston Survey, and the Survey of Professional Forecasters. Dr. Sobel looked at his forecast and the forecast of the other Advisory Committee Members, but did not review the BEA information.

~He feels that the chances of a recession are much the same as last year: 1 in 5.

**Chairman Grimball asked Dr. Sobel why he was more optimistic than the other Advisory Committee Members. Dr. Sobel responded that his forecast is higher due to the way he computes his model but he has the same concerns as the other Advisory Committee Members. He uses the nominal GDP growth rate not a real growth rate.*

Mr. Robert Martin, *Staff Chief Economist*, Board of Economic Advisors

Mr. Martin’s estimates were:

Personal Income	FY 2018-19 – 4.75%	FY 2019-20 – 4.25%
Employment	FY 2018-19 – 1.50%	FY 2019-20 – 1.40%
Inflation	FY 2018-19 – 2.90%	FY 2019-20 – 2.50%

~BEA Chief Economist, Robert Martin concluded the presentations. He shared that the revenue base will be adjusted by \$177 million going forward due to the surplus in capital gains. He also stated that the economy is most likely at the top of the business cycle and he is expecting a slow-down in 2020.

~The S.C. real GDP has been running a little higher than the U.S. GDP. There has also been an income slow down and he is looking for wage increases to occur.

~The S.C. legislature passed several pieces of legislation which will cause a reduction in the General Fund for FY 2018-19 and FY 2019-2020. Due to these offsets, even with growth occurring, there will only be moderate growth. In FY 2020, growth will be slower and global growth is expected to slow as well.

Panel Discussion:

~All forecast predictions were reviewed and compared by the BEA staff and Board members.

**Mr. Rainwater stated that there seemed to be a difference among the panel as to whether the forecast for the personal income category for the current fiscal year should be 4.25 percent or be higher.*

**Dr. M. Martin stated that his difference is based on the inflation information.*

**Mr. R. Martin shared that his inflation forecast hinges on oil prices and he also believes his personal income number is high after listening to other panel members. Dr. Von Nessen's presentation concerning using bonuses to retain employees versus providing raises explains why wage growth is not occurring. He feels more study is needed on this subject.*

**Dr. Sobel feels that the Olympic model best evaluates data. He also believes that the comparison between this year and next year suggests a modest slow-down.*

**Chairman Grimball asked if the BEA numbers reflect the projected slow-down to which Mr. Rainwater responded that the numbers are close.*

**Mr. Clyborne asked what percentage of the net capital gains will remain. Mr. R. Martin responded that the ratio of net capital gains to individual income tax revenue in S.C. over the last twenty years represents 5.35 percent.*

**Chairman Grimball asked if the difference is twenty million between the current forecast and what will be forecasted; should the estimate be changed? Mr. Rainwater explained that the estimate will change significantly as there has been at least 100 million increase in the base and it also depends on the estimates in other categories. Mr. R. Martin will run projections for this coming year and the next year based on 4.25 and 4.50 percent and the results will be reviewed. Mr. Clyborne asked if the estimate would change as a result of a percentage or legislative issue. Dr. Hefner replied that he is not sure that there will be a slow-down in the national economy due to too much uncertainty. Underlying growth comes from the size of the federal register which has been reduced over the last few years due to fewer regulations. Dr. M. Martin stated that over the course of time, real growth will put more people in the workforce. Mr. Gower asked what is driving productivity gains to which Dr. Hefner replied it was less regulation.*

There were no other questions or comments from the Members or Working Group.

The meeting adjourned at 3:28pm (Mr. Gower motioned, Mr. Clyborne, seconded; all voted aye).

The next scheduled meeting is Thursday, November 8, 2018.

Attachments: Agenda, Meeting Materials

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These minutes were approved on 11/8/18.

Karen Rhinehart
Karen Rhinehart