

February 09, 2025

MEMORANDUM

TO: Representative Nathan Small, Chair, House Appropriations and Finance Committee
Senator George Muñoz, Chair, Senate Finance Committee

FROM: Staff Economists of the Department of Finance and Administration, Legislative Finance Committee, Taxation and Revenue Department, and Department of Transportation

THROUGH: Secretary Wayne Propst, Department of Finance and Administration
Secretary Stephanie Schardin Clarke, Taxation and Revenue Department
Director Charles Sallee, Legislative Finance Committee

SUBJECT: Consensus Revenue Estimating Group – 2025 Mid-Session Review of Revenues

Prior to the mid-point of each legislative session, the Consensus Revenue Estimating Group (CREG) meets to review updated economic indicators and the most recent tax receipt data to determine whether the consensus revenue estimate warrants updating. This memorandum summarizes the work and conclusions of the CREG, comprised of economists from the Legislative Finance Committee (LFC), the Department of Finance and Administration (DFA), the Taxation and Revenue Department (Tax & Rev), and the Department of Transportation (DOT).

After careful review of new economic data available since the December 2024 forecast, the CREG reached consensus to make no changes to the revenue estimate. The CREG would caution that revenue volatility remains a major forecasting challenge.

December 2024 Consensus General Fund, Recurring Revenue Outlook (in millions)

<u>FY24</u>	<u>FY25</u>	<u>FY26</u>
\$13,050.2	\$13,263.9	\$13,614.4

In the December 2024 revenue forecast, FY25 ending reserve balances were projected to be 38.4 percent pending 2025 regular session appropriations, and FY25 “total new money” – defined as FY26 recurring total revenues less total FY25 appropriations – was estimated at \$892.3 million.

To determine potential changes in the forecast, the CREG reviewed estimates for gross receipts and compensating tax, income taxes (both personal and corporate income tax), severance taxes, interest earnings, and rents and royalties.

The CREG also reviewed two additional months of actual receipts data and considered revised national and local economic indicators including gross domestic product (GDP), inflation rates, commodity prices, active oil drilling rigs, wages, employment, personal income, and the federal funds rate.

Moody’s Analytics and S&P Analytics made minimal changes to their macroeconomic forecasts, with changes to interest rate expectations to remain higher for longer and GDP expectations mostly unchanged. Although the probability of risks to the forecast have changed since December, the current revenue environment reflects a mostly similar environment to what was considered in December 2024.

Changes in forecasts for oil and natural gas volumes and prices were considered in the review. Oil prices and production expectations remain on target for the current and budget years from the December estimate. The combined effect would be small reductions in oil and gas direct revenues, but because of insulating measures enacted over the last several years, the general fund is largely shielded from the declines.

Investment revenue expectations in FY25 are lower based on two additional months of receipts, specifically due to market valuations of the State Treasurer's general fund investment pool. However, significant uncertainty in market expectations of interest rates warrants caution. The likelihood of federal reserve action on interest rates, the unpredictability of such actions, and market reactions to those announcements remain areas of significant risk especially as rates are expected to remain higher than previously forecasted in the near term.

In the gross receipts tax, two additional months of collections show revenues for the source are tracking with the December estimate. Yet, a comparison of year-to-date revenue through November compared to the same period in the prior fiscal year illustrates revenue growth is moderating. Similarly, a maturing labor market, changing monetary policy, and potentially large impacts to the labor force from changing federal immigration enforcement counterbalance personal income tax strength this year. Such expectations in personal income and gross receipts tax revenue, despite these evolving risks, were largely similar to forecasts for each source as in December.

For these reasons, the CREG determined the December 2024 consensus forecast remains a valid estimate of projected revenues. The various increases and decreases largely negate each other, and any remaining difference would be negligible compared with total revenues and inappropriate when considering the uncertain economic conditions.

Despite the unchanged estimate, various risks to the forecast remain— both on the upside and downside.

Oil and Natural Gas Variance. The state's considerable dependence on oil- and gas-related revenues means the forecast is sensitive to changes in commodity prices and produced volumes that directly or indirectly affect revenues from severance taxes, federal royalty payments, gross receipts tax, personal income tax, and corporate income tax. This adds significant uncertainty to the revenue forecast. Regarding prices, a \$1 change in the annual average price of New Mexico's oil has about a \$50.4 million impact on the severance tax and royalties, and a 10-cent change in the annual average prices of New Mexico's natural gas has about a \$36.7 million impact. Oil and gas prices are inherently volatile and difficult to predict as is estimating production, which heavily depends on prices.

Recession Risks. Major forecasting agencies continue to have U.S. growth projections for 2025. However, the U.S. economy could fall into a recession and experience a slower recovery due to broadening conflicts globally, shocks to labor supply and demand, the threat of global trade wars hampering economic growth, sustained high inflation, slowing consumer spending, and rising defaults in commercial lending. Otherwise, tightening employment conditions, tightening monetary policy, and inflation remain significant risks that could significantly hamper economic recovery.

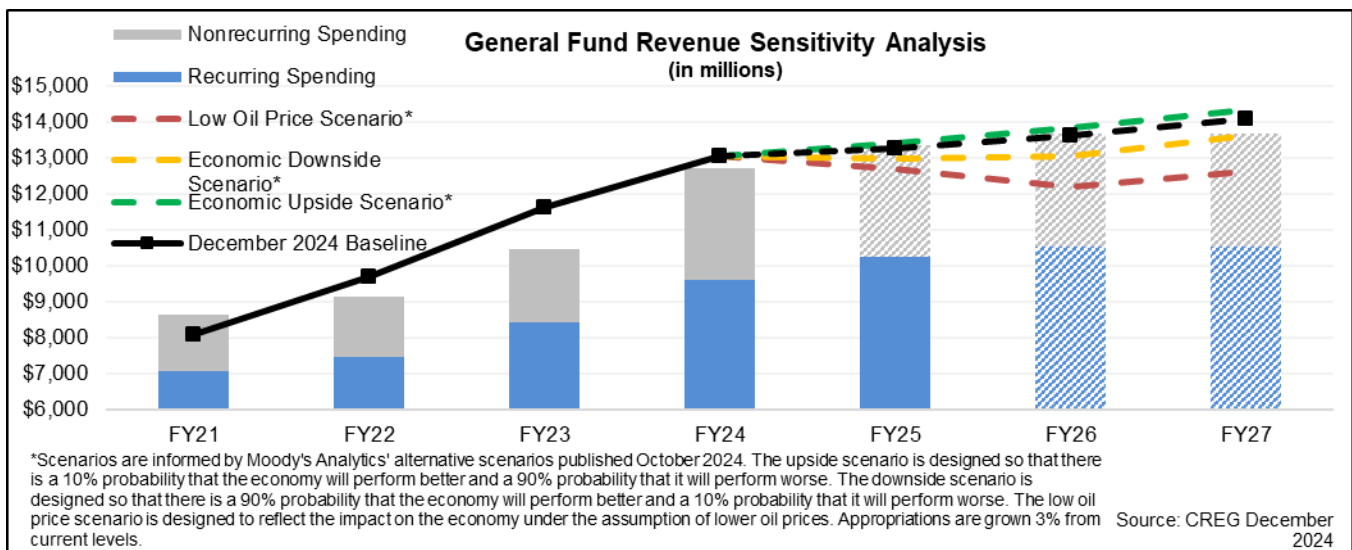
Other Significant Risks. Additional forecast risks include potential for uncapped growth in film tax credit payments due to New Mexico film partners, changes from the expected impacts of destination sourcing, taxpayer amendments, state and federal regulatory changes that could affect oil and gas, upcoming changes to the federal Tax Cuts and Jobs Act, outstanding tax protest claims at Tax & Rev that could result in large general fund losses if decided in favor of the taxpayer, volatility in government spending, and uncertainties surrounding federal interest rate decisions, trade tariffs, and immigration enforcement policy shifts.

Because the revenue estimates are a baseline forecast, they are not intended to account for the various forecast risks. Instead, policymakers can prepare for risks by maintaining appropriate general fund reserve levels. To inform policymakers, the CREG produces stress tests which help to gauge the appropriate general fund reserve level.

Stress-Testing. The CREG reviewed changes in underlying assumptions in the December 2024 estimate to determine the sensitivity of select revenues – including severance taxes, federal mineral leasing payments, personal income taxes, and gross receipts taxes – based on three scenarios: (1) low oil price and low production, (2) moderate recession, and (3) stronger near-term economic growth.

On the upside, the cumulative effect of the stronger near-term growth scenario on the general fund for FY25 through FY27 is an additional \$578 million above the current estimate. Conversely, the cumulative effect of the low oil prices scenario on the general fund for FY25 through FY27 is \$3.5 billion below the current estimate, and the effect of the moderate recession scenario for the same period is \$1.4 billion.

While the revenue estimates cannot reasonably account for the various forecast risks, policymakers can prepare for these risks by maintaining appropriate general fund reserve levels.



Scenario	S8: Low Oil Price			S3: Economic Downside			S1: Economic Upside		
	FY25	FY26	FY27	FY25	FY26	FY27	FY25	FY26	FY27
1 Severance Taxes to GF	-\$123	-\$320	-\$254	-\$24	-\$29	-\$19	\$5	\$15	\$14
2 Federal Mineral Leasing to GF	\$0	-\$266	-\$227	\$0	\$0	\$0	\$0	\$0	\$0
3 Gross Receipts Taxes	-\$294	-\$519	-\$618	-\$162	-\$338	-\$267	\$93	\$117	\$116
4 Corporate Income Taxes	-\$90	-\$174	-\$211	-\$45	-\$115	-\$122	\$18	\$24	\$24
5 Personal Income Taxes	-\$88	-\$139	-\$164	-\$56	-\$111	-\$77	\$25	\$59	\$68
6									
7 General Fund Difference from Baseline	-\$595	-\$1,418	-\$1,474	-\$287	-\$593	-\$485	\$141	\$215	\$222
8 General Fund Percent of Total Impact	29%	42%	39%	32%	31%	34%	44%	43%	46%
9									
10 Severance Taxes to TSR or ECE	-\$377	-\$277	-\$187	-\$289	-\$277	-\$187	\$86	\$104	\$61
11 Severance Taxes to STPF	-\$257	-\$501	-\$733	0	-\$281	-\$175	0	\$17	\$42
12 Federal Mineral Leasing to ECE	-\$694	-\$480	-\$277	-\$334	-\$480	-\$277	\$91	\$150	\$107
13 Federal Mineral Leasing to STPF	-\$123	-\$718	-\$1,125	\$0	-\$272	-\$293	\$0	\$18	\$52
14 TSR/ECE Transfers Diff. from Baseline	-\$1,451	-\$1,976	-\$2,322	-\$623	-\$1,310	-\$932	\$177	\$289	\$262
15 TSR/ECE/STPF Transfers Percent of Total Impact	71%	58%	61%	68%	69%	66%	56%	57%	54%
16 Total Difference from Baseline	-\$2,046	-\$3,394	-\$3,796	-\$910	-\$1,903	-\$1,417	\$318	\$504	\$484

Note: in millions