



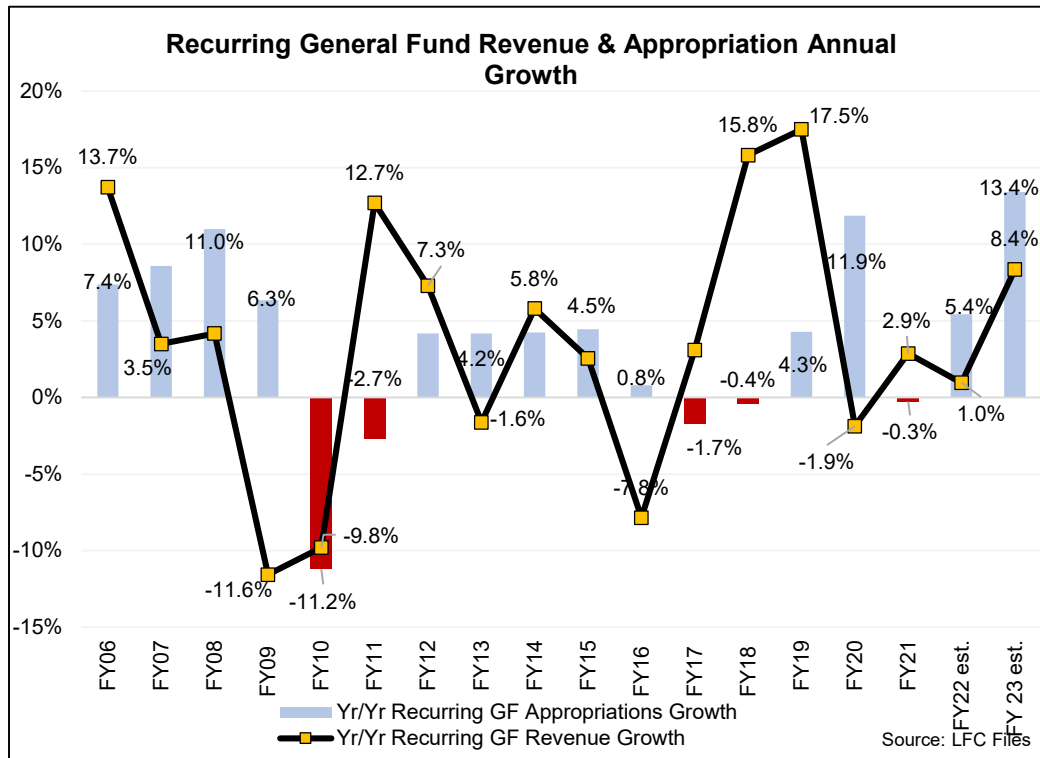
NEW MEXICO
LEGISLATIVE
FINANCE
COMMITTEE

Mid- to Long-term Revenue Options

July 20, 2022

Presentation to the Legislative Finance
Committee

The Legislature has prioritized stabilizing revenues, preserving existing programming, and balancing budgets within recurring revenues.

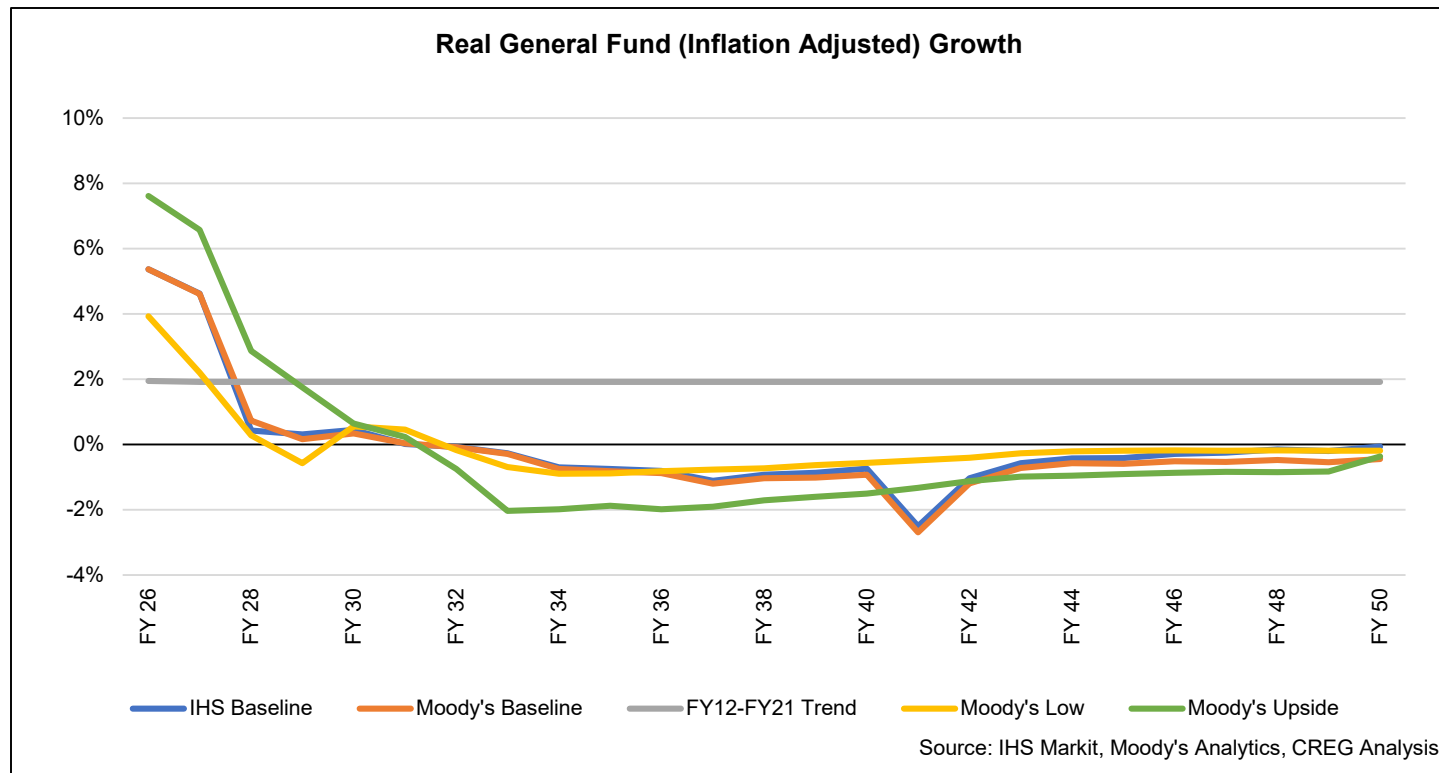


Progress along these priorities include:

- Creating a “Tax Stabilization Reserve” or true rainy day fund,
- Creating the excess distributions above a 5-year average for oil and gas revenues,
- Higher reserves to match increased volatility, and
- Prefunding and endowing programs across the budget.



Long-term revenue growth may be insufficient to maintain current levels of government services.



FY21-FY25 General Fund Recurring Appropriation Outlook
(in millions)

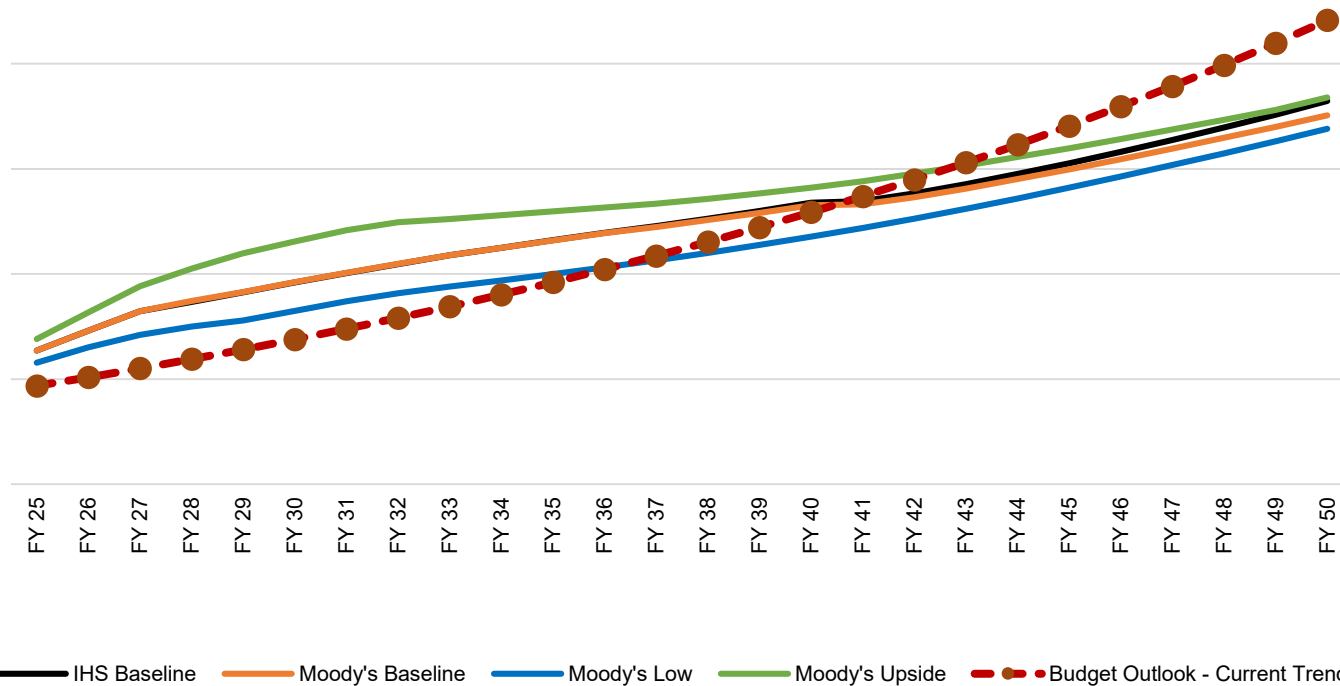
	Operating Budget FY22	2022 GAA FY23	Outlook FY24	Outlook FY25
December 2021 Consensus	\$ 8,163.1	\$ 9,049.1	\$ 9,643.2	\$ 10,178.8
2022: HB 163 Tax Package		\$ (201.2)	\$ (390.0)	\$ (408.0)
2022: HB 68 Criminal Code Changes (LEPF)			\$ (14.0)	\$ (15.5)
2022: Other		\$ (2.5)	\$ (4.2)	\$ (4.3)
Total Recurring Revenue	\$ 8,163.1	\$ 8,845.4	\$ 9,235.1	\$ 9,751.0
Year-to-Year Percent Change	1.0%	8.4%	4.4%	5.6%
Recurring Appropriations				
Legislative	\$ 21.9	\$ 24.1	\$ 24.7	\$ 25.3
<i>Feed Bill</i>	\$ 17.5	\$ 19.5	\$ 20.0	\$ 20.5
<i>Legislative</i>	\$ 4.3	\$ 4.6	\$ 4.7	\$ 4.8
Judicial	\$ 327.8	\$ 345.2	\$ 355.6	\$ 366.2
General Control	\$ 158.8	\$ 166.4	\$ 170.6	\$ 174.9
Commerce, Industry	\$ 65.6	\$ 77.1	\$ 79.0	\$ 81.0
Agriculture, Energy and Natural Resources	\$ 79.0	\$ 91.0	\$ 93.3	\$ 95.6
Medicaid	\$ 1,031.7	\$ 1,283.7	\$ 1,386.4	\$ 1,497.3
Other Health, Hospitals and Human Services	\$ 946.8	\$ 1,017.9	\$ 1,053.5	\$ 1,090.4
Public Safety	\$ 476.6	\$ 491.5	\$ 506.3	\$ 521.5
Other Education	\$ 35.0	\$ 56.7	\$ 58.1	\$ 59.6
Higher Education	\$ 894.7	\$ 939.1	\$ 967.2	\$ 996.2
Public School Support	\$ 3,411.3	\$ 3,812.9	\$ 3,984.5	\$ 4,163.8
Recurring Compensation (excl. public education)	\$ 0.5	\$ 178.6	\$ 183.1	\$ 187.7
Subtotal - Recurring Appropriations	\$ 7,449.7	\$ 8,484.3	\$ 8,862.3	\$ 9,259.5
Year-to-Year Percent Change, pre-adjustment	3.3%	13.9%	4.5%	4.5%
Adjustment Scenario				
- Replace TANF Fund Balance for Pre-K Programs			\$ 17.6	\$ 17.6
- DD/Eliminate Waitlist and replace enhance FMAP				\$ 76.6
- Opportunity Scholarship			\$ 115.1	\$ 125.9
- Nursing Program Enhancement			\$ 15.0	\$ 15.0
- Hospital and Nursing Home Costs - ARPA Backfilling			\$ 18.0	\$ 18.0
- Public Family Income Index			\$ 15.0	\$ 15.0
- GSD Risk Management Health Insurance Deficit - GF 5% increase for state agencies			\$ 4.3	\$ 4.3
- Teacher Residency			\$ 15.5	\$ 15.5
- Backfill Irrigation Works Construction Fund			\$ 5.0	\$ 5.0
- Public Education Reform Fund Below-the-line Backfilling			\$ 8.5	\$ 8.5
- Additional Increase to ERB Contributions			\$ 26.0	\$ 26.0
- SB 48 Supplemental General Appropriations (Junior)	\$ 25.2		\$ 26.3	\$ 27.5
Subtotal - Adjustment Scenario	\$ -	\$ 25.2	\$ 266.3	\$ 354.9
Total Recurring Appropriations + Adj Scenario	\$ 7,449.7	\$ 8,509.5	\$ 9,128.6	\$ 9,614.4
Year-to-Year Percent Change	5.5%	14.2%	7.3%	5.3%
Surplus/(Deficit)	\$ 713.4	\$ 335.9	\$ 106.5	\$ 136.6
Notes:	1) Annual appropriation growth FY23-FY25 (with FY22 as base) calculated 3) Some bills have assumed operating budget impacts beginning in FY23			
	Public School Support 4.5%	Health, Hosp. & Hum. 4.0%		
	Higher Education 3.0%	Medicaid 8.0%		
	Public Safety 3.0%	Other HHHS 3.5%		
	Judicial 3.0%	Other State Agencies 2.5%		
	2) Compensation assumed at 2.5 percent growth			

Recurring
appropriation
growth has
averaged about
4.2 percent since
FY16, nearly the
same as the
current long-
term recurring
revenue trend.

* totals may not foot due to rounding

The current budget and revenue outlook – assuming appropriations are not grown faster and revenues are not reduced – may result in a recurring deficit in 12 to 18 years.

General Fund Recurring Revenue and Recurring Appropriation Outlook



Source: IHS Markit, Moody's Analytics, CREG Analysis



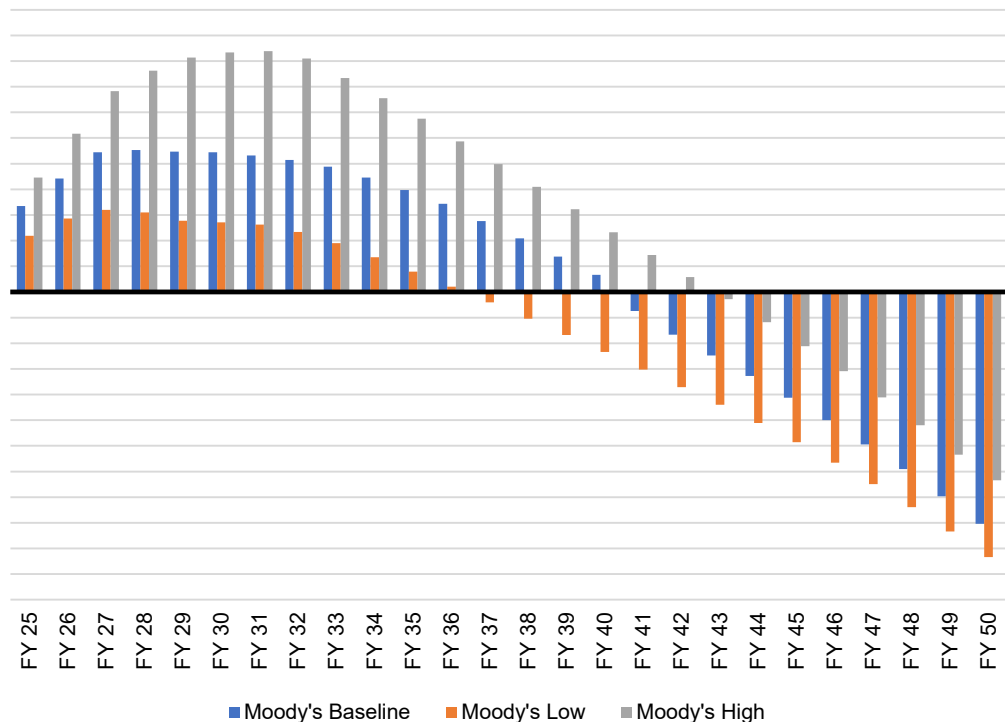
How can the state improve the long-term revenue outlook?

- Foster economic growth to beat current expectations.
- Resist spending all recurring revenues on recurring uses, now and in the future.
- Invest short-term, peak production revenues for future use. E.g. endowments and trust funds.
- Extend five-year average protections on oil and gas revenues to delay the decline in recurring revenues.
- Use short-term, peak production revenues for nonrecurring uses.



In the short- to medium-term, revenues are expected to exceed appropriations providing opportunities to change the long-term trajectory.

Recurring Revenues less Recurring Appropriation Outlook



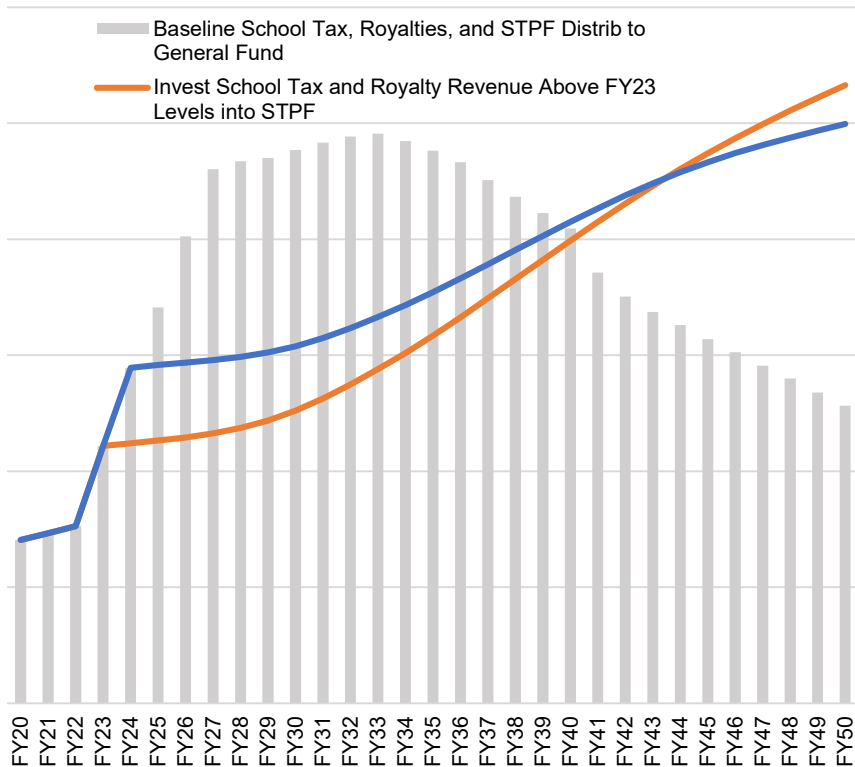
Source: Moody's Analytics, CREG Analysis

- Investments in education and workforce development can grow wages and may take significant time to materialize.
- Competitive business and tax climate may encourage business recruitment and growth.
- Long-term planning and performance-based economic development programs could keep the state on track.

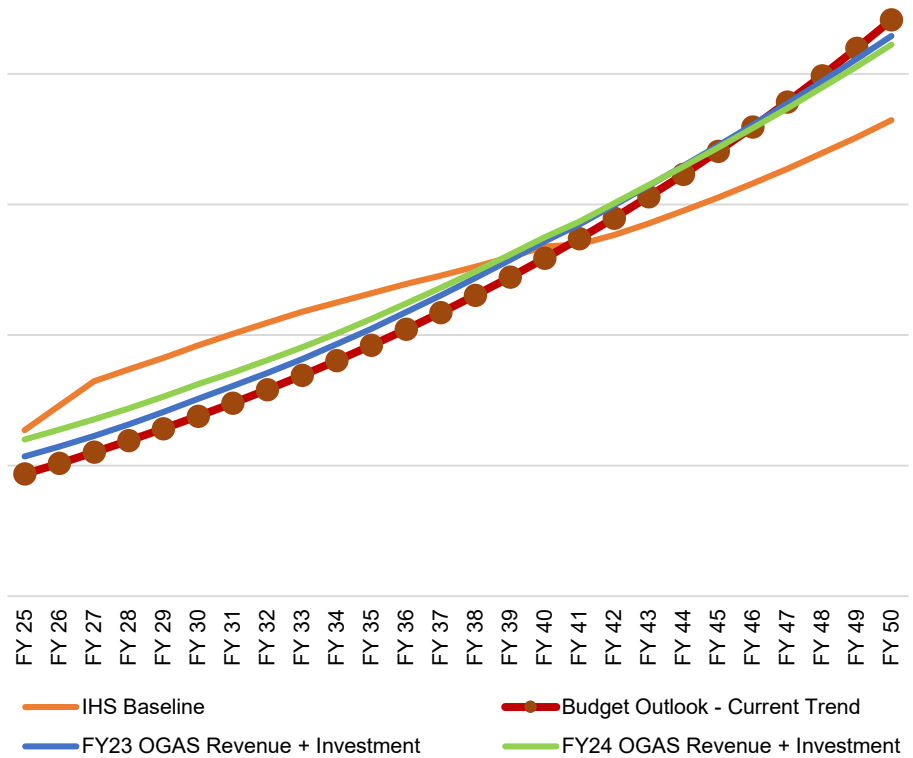


Investing short-term, peak production revenues for future use nearly eliminates the out-year deficit.

Effect of Investing Additional Oil and Gas Revenue



General Fund Recurring Revenue and Recurring Appropriation Outlook



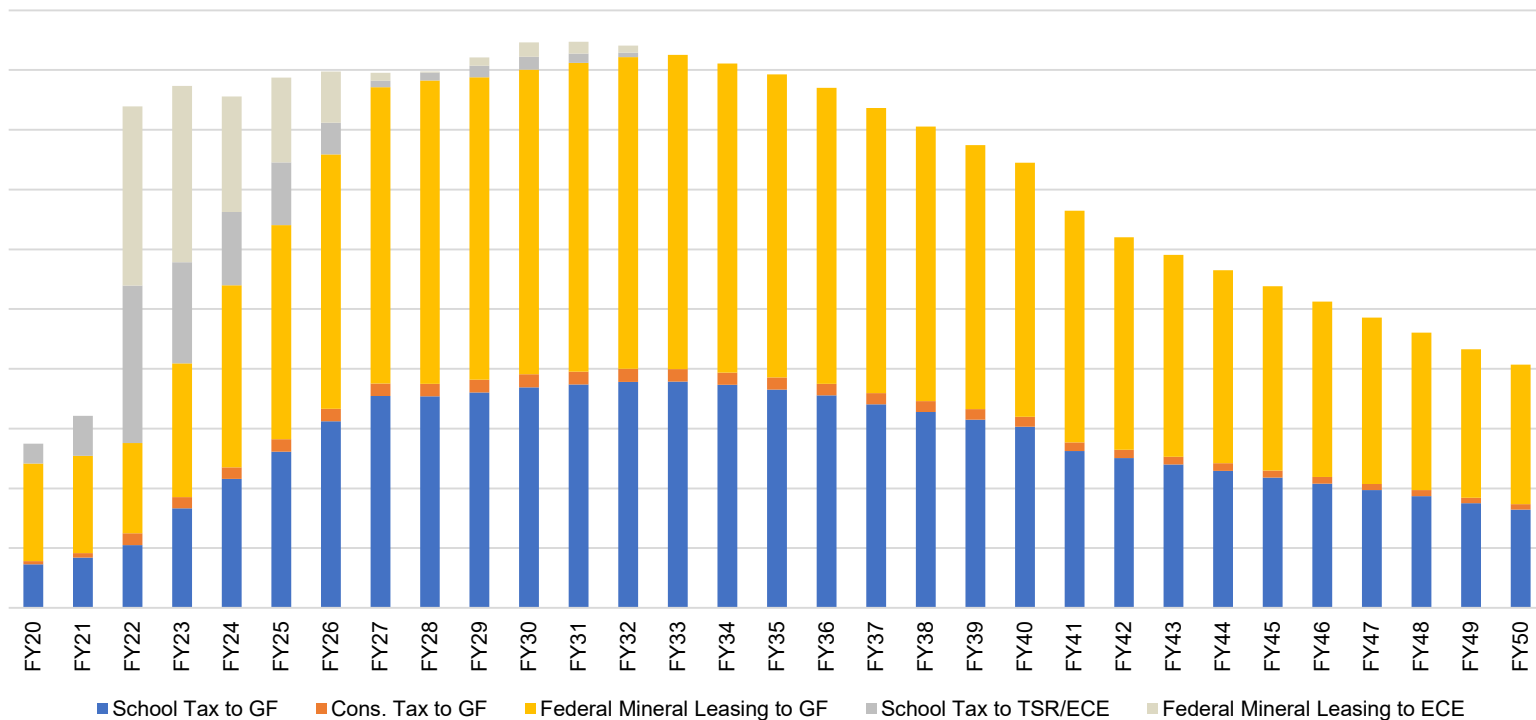
Note: Scenarios reflect the sum of funds distributed to the general fund from oil and

Source: IHS Markit, Moody's Analytics, CREG Analysis



Short-term production spikes are bumping up the 5-year average and weakening the smoothing effect of stabilization measures.

New Mexico General Fund Oil and Gas Revenue Outlook

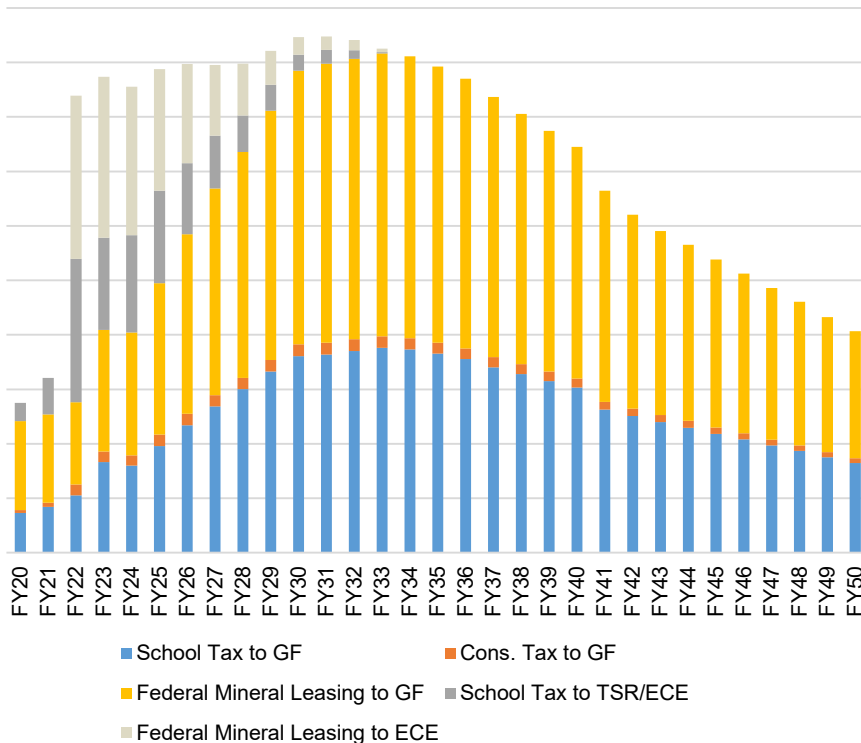


Note: Scenarios assume oil and gas price and production estimates as of July 2022.

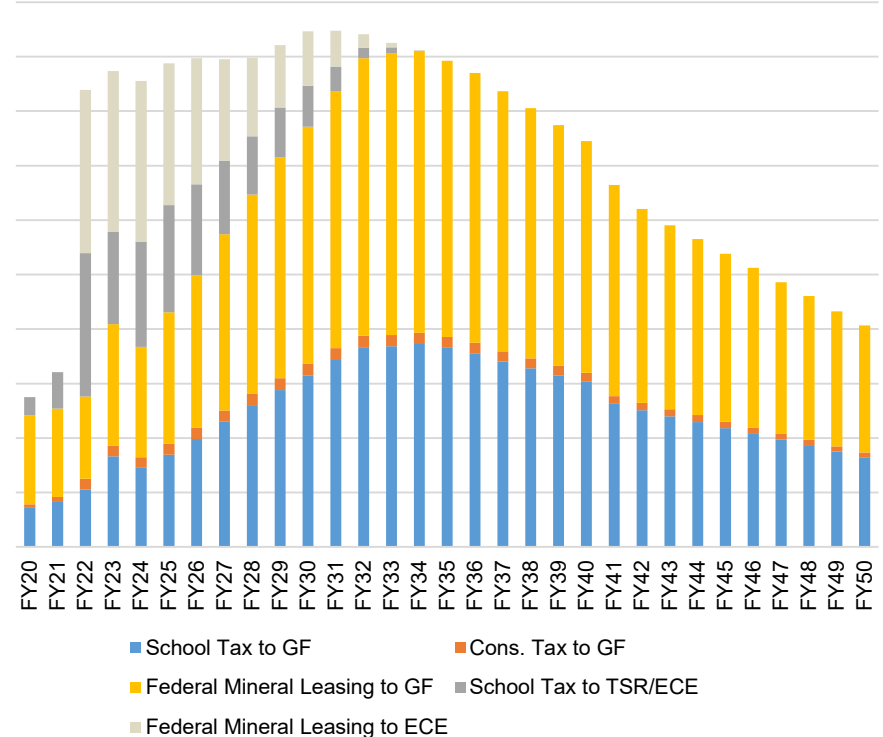


Extending the 5-year average better insulates the general fund and delays revenue declines for 3-5 years.

Oil and Gas Related Revenue with 8-Year Average



Oil and Gas Related Revenue with 10-Year Average



Note: Scenarios assume oil and gas price and production estimates as of July 2022.



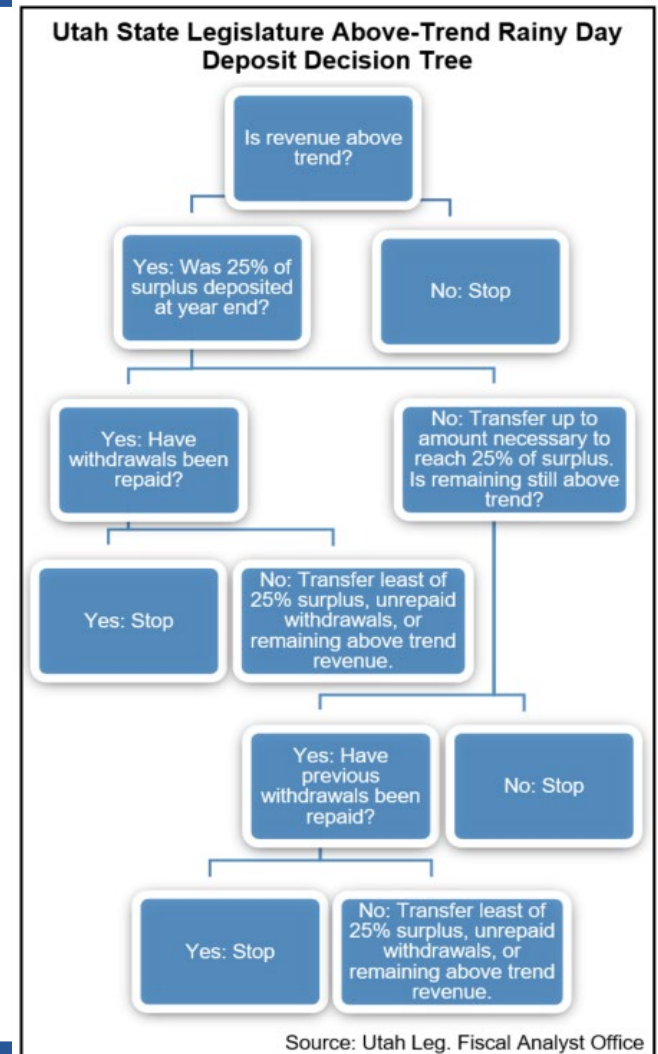
Mechanisms that sort above-trend revenues for nonrecurring purposes have proved useful in other states and could prevent acceleration of out-year deficits.

- Virginia – when general fund revenue growth exceeds the 6-year average, half is deposited into the rainy day fund.
- Louisiana – requires nonrecurring revenues to be spent on retiring bonds, payments against unfunded pension liability, capital outlay projects, making deposits into the budget stabilization fund, or funding highway construction.

Example of Bill Mechanisms using FY19 General Fund Revenue			
Total General Fund Revenue	General Fund Revenue Growth	Previous 10-Year Average Revenue Growth	5% Above Previous 10-Year Trend
\$ 7,910.3	15.0%	1.5%	\$ 581.0
Distribution of Excess Revenue		Percent	Amount
College Affordability Fund		30%	\$ 174.3
Teacher Affordability Scholarship Fund		20%	\$ 116.2
Early Childhood Education and Care Fund		20%	\$ 116.2
State Road Fund		10%	\$ 58.1
Severance Tax Permanent Fund		10%	\$ 58.1
Rural Libraries Endowment Fund		10%	\$ 58.1

Note: dollars in millions

SB 392
(2021
Regular
Session)



QUESTIONS?





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Balancing Short and Long Term Revenues with Budget Needs

Charles Sallee, Deputy Director for Budget

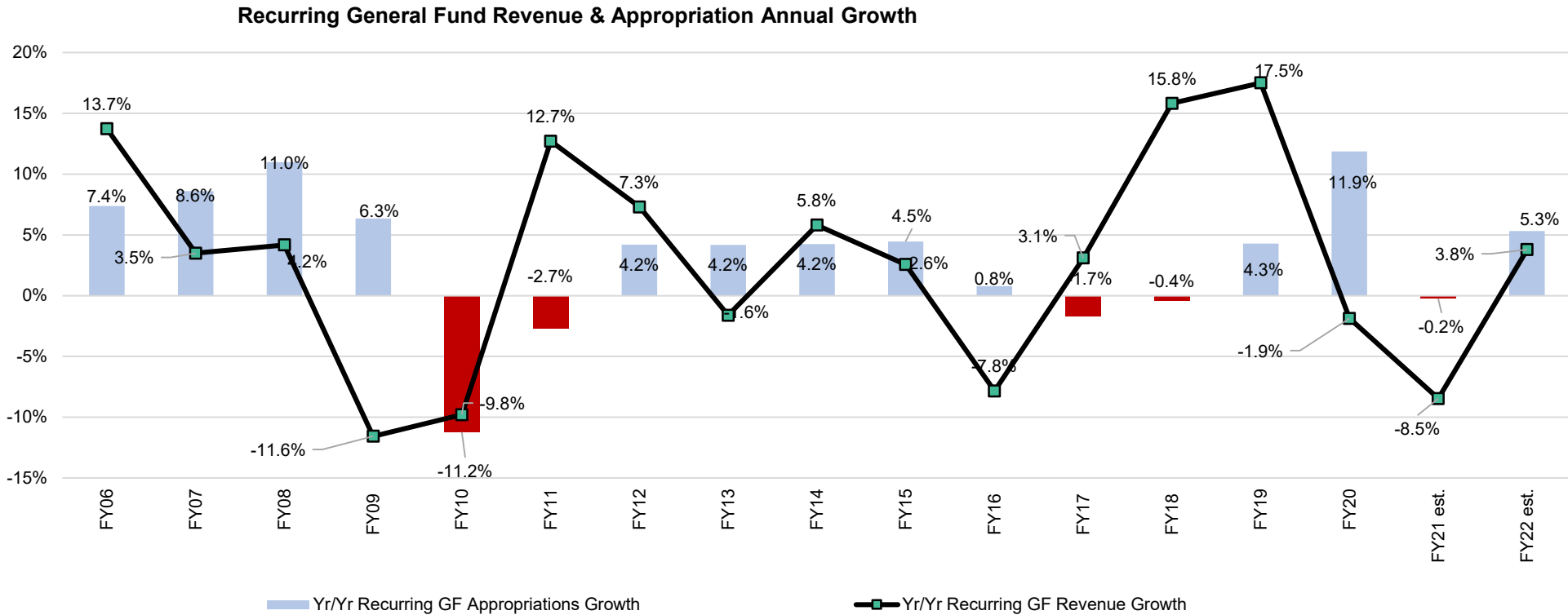
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Roller Coasters Aren't Always Fun



Actual General Fund Roller Coaster



Source: LFC Files, 2021 Sessions pre-veto



Long Term Fiscal Planning

- Organizations such as the Pew Charitable Trust State Fiscal Health project, and the Government Finance Officers Association, encourage states to engage in more long-term financial planning.
- Why engage in long term planning for an annual budget cycle?
 - Avoid budgeting by crises and surprises
 - Strategically implement services or tax changes that benefit New Mexicans
 - Avoid committing to unsustainable spending
 - Understand full scope of upcoming liabilities and competing budget priorities



Examples of Existing Long Term Fiscal Planning Information

- Multi-year consensus revenue estimates
- Revenue stress tests
- Multi-year budget forecasts, including public schools
- Multi-year fiscal impact reports



Key Fiscal Planning Questions

- Do we have a structurally balanced budget? Yes, for now.
 - *Are recurring revenues covering recurring costs? Yes.*
 - *What new recurring future spending has been created with nonrecurring revenue? A lot. DD waiver, Opportunity Scholarship among others*
- How prepared is the state for a fiscal downturn/upturn?
 - *What/if stress tests inform reserve targets? Yes.*
 - *Does the state have a tool kit ready to address insufficient revenue? Yes, but not formally published. Toolkit for excess revenue?*
- Which emerging challenges need to be addressed? Lots
 - *What does changing state demographics mean for finances? Big challenges*

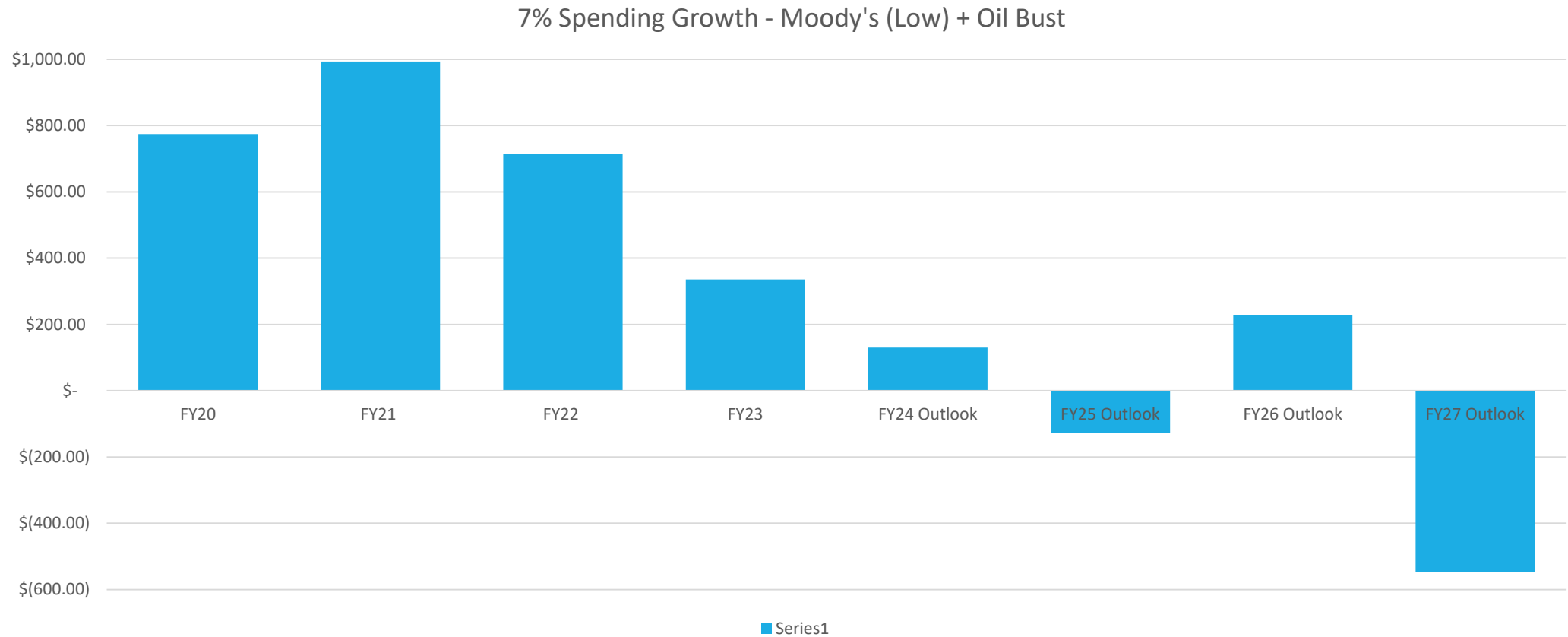


New Mexico Has Volatile Revenues But Strong Fiscal Position

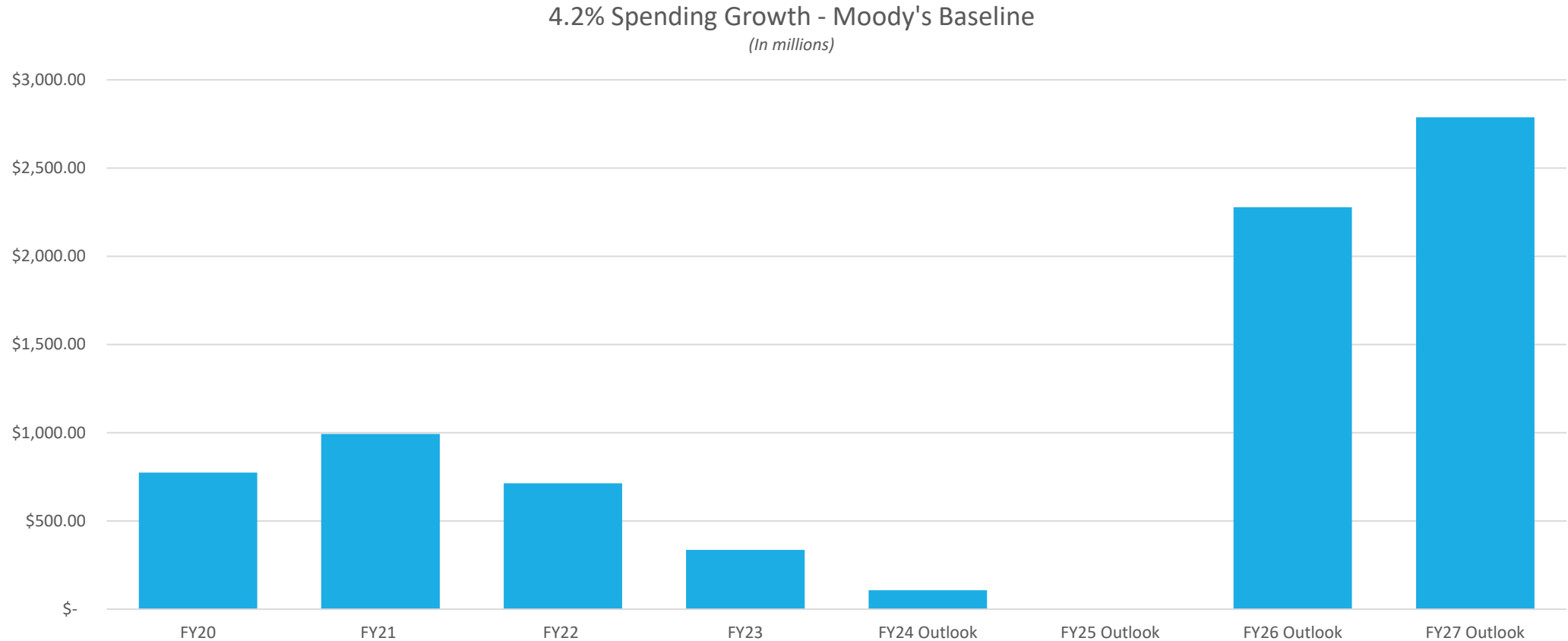
- Projected FY23 ended reserves of over \$2.1 billion (25%) – likely will be higher,
 - *Operating reserve (easy to use for shortfalls) projected at only \$87 million.*
 - *“Rainy Day” Fund at 17% or \$1.5 billion*
 - *Little desire to tap corpus of \$333 million Tobacco Settlement Fund.*
 - *Revenue tracking indicates “up-side” risk*
- Millions appropriated in multi-year spending plans or growing in agency account cash balances.
- Budgeted cash balances in key government sectors – public schools and higher education – at all time highs.
- Additional extra reserves, such as early childhood trust fund, projected to have balances far in excess of financial goals. Could use more trust funds for other beneficiaries.
- Strong oil production, at least for next 10-15 years, provides potential game changing opportunities (if done right) for New Mexico’s economy.



Budget Stress Test – Low Revenue/Oil Bust Scenario “New Money” Outlook. Robust Spending And Reserves Can Handle A Bust (Bust in FY26/FY27)

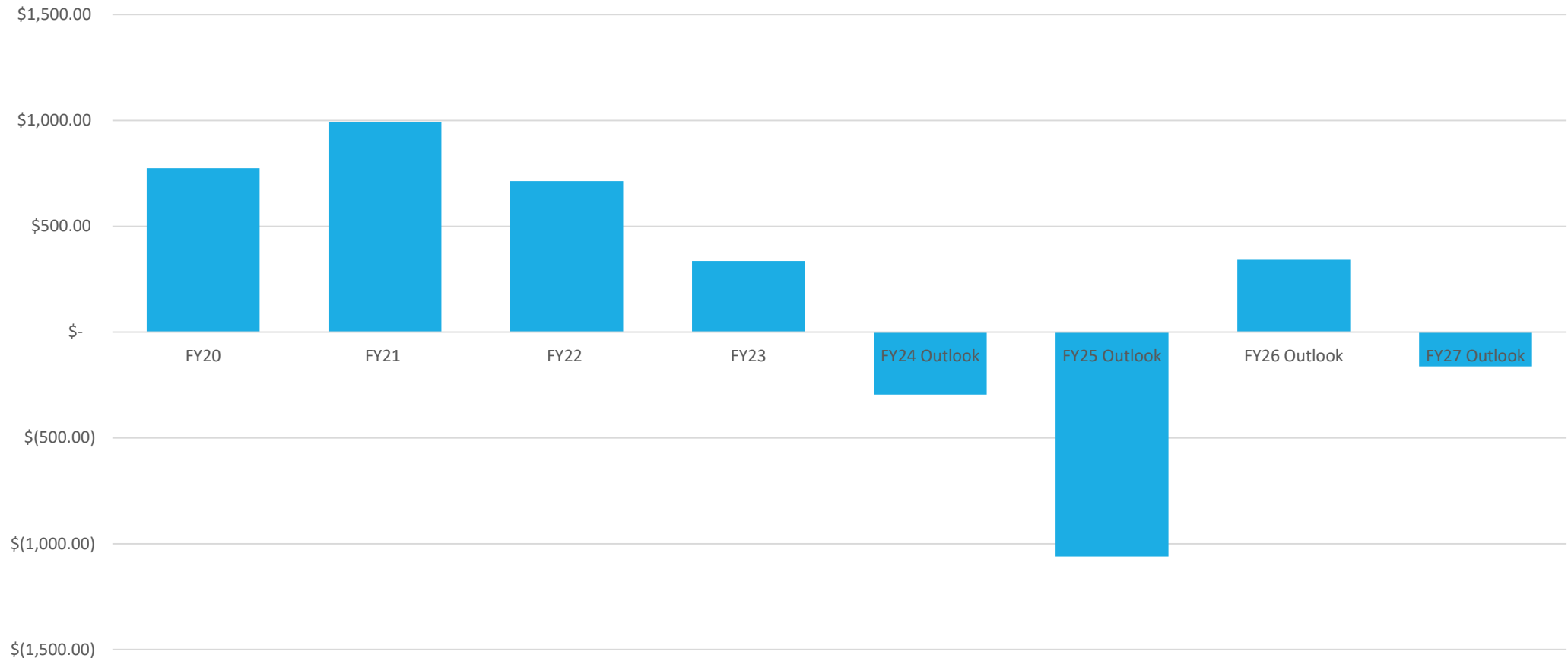


Budget Stress Test – Baseline “New Money” Outlook. Too Much Revenue, Not Enough Spending.

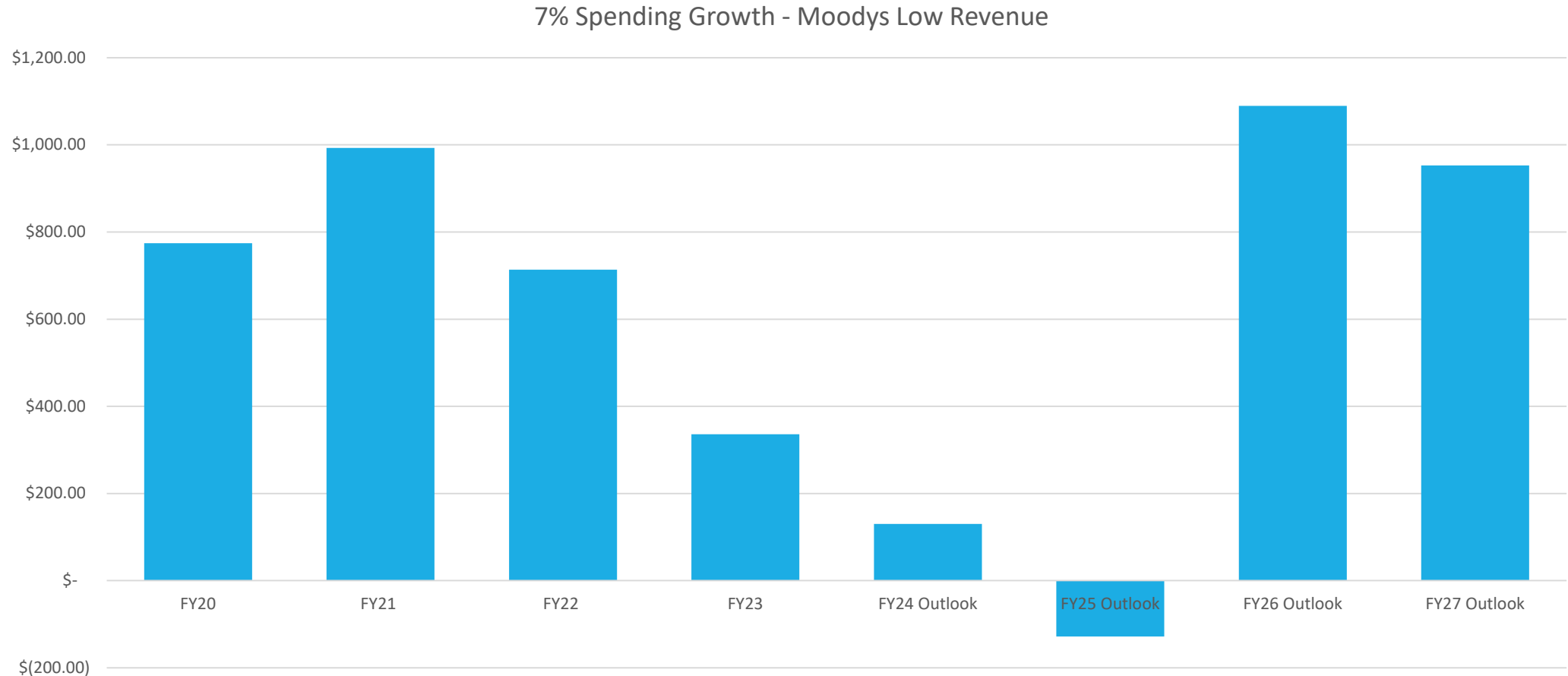


Budget Stress Test – Very High Spending Baseline Revenue “New Money” Outlook. Too Much Spending.

12% Spending Growth - Moody's Baseline



Budget Stress Test – High Spending Growth Low Revenue “New Money” Outlook. Still Too Much Revenue, Spending Solid.



Fiscal CHALLENGE “Playbook”

- Tap reserves – but likely will require special sessions.
- Swap revenues and sweep cash balances strategies.
- Cancel stalled or out-year appropriations.
- Some form of federal fiscal relief.
- Lots of “on-the-shelf” information on government efficiency (funded vacant positions and half empty but open prisons as examples)
- No need for “slash and burn” agency cuts, nor for across the board cuts or layoffs if State maintains preparedness.
- Lot’s of performance and evidence-based information to prioritize and protect high priority investments.
- Need a more robust Fiscal OPPORTUNITY “Playbook”



Conclusion

- State has taken many actions to prepare for revenue volatility. Even though oil/gas makes up 35% of GF – volatility can be managed.
- Near and long-term fiscal outlook remains strong (knock on wood now, please). Seriously, we should look at oil/gas revenue as an opportunity.
- State revenue outlook likely strong enough to reassess how much money should be allocated to the public sector (government) versus private sector (people and business).
 - Might consider major tax adjustments with triggers/sunsets in 10-15 years if concerned over future revenue.
 - Tax adjustments, especially new ones, will need to be effective.
- LFC may want to consider additional revenue AND budget stress testing and long-term financial planning and preparation.





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For More Information

- <http://www.nmlegis.gov/lcs/lfc/lfcdefault.aspx>
 - Session Publications – Budgets
 - Performance Report Cards
 - Program Evaluations

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