STATE OF MAINE
REVENUE FORECASTING COMMITTEE

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Todd Gabe, Professor of Economics, University of Maine

December 1, 2022

TO: Governor Janet T. Mills
Members, 130th Legislature
Members, 131st Legislature

FROM: Christopher Nolan, Chair
Revenue Forecasting Committee

RE: Revenue Forecast Committee December 1, 2022 Report

The Revenue Forecasting Committee (RFC) has concluded its update of the current revenue forecast to comply with its statutory reporting date of December 1st, to incorporate the new economic forecast released by the Consensus Economic Forecasting Commission (CEFC) on November 1, 2022 and to provide a forecast that reflects revenue performance through the first four months of FY23. Tables showing the changes made to all the funds forecasted by the committee and a detailed presentation that includes the key assumptions made in developing the forecast have been posted to the RFC's web page and are available here. A more complete report will be available next week and added to the web page.

General Fund Summary

	FY22	FY23	FY24	FY25	FY26	FY27
Current Forecast	$5,391,613,569	$4,758,487,167	$4,913,788,247	$5,095,515,994		
Annual % Growth	19.3%	-11.7%	3.3%	3.7%		
Net Increase (Decrease)	$0	$282,766,802	$266,210,985	$222,378,456		
Revised Forecast	$5,391,613,569	$5,041,253,968	$5,179,999,232	$5,317,894,450	$5,557,257,689	$6,037,175,196
Annual % Growth	19.3%	-6.5%	2.8%	2.7%	4.5%	8.6%

In its December 2022 update, the RFC revised General Fund revenue estimates upward by $282.8 million for FY23 and by $488.6 million (4.9%) for the 2024-2025 biennium. The forecasted rate of year-over-year change in General Fund revenue for FY23 is now -6.5%, followed by growth of 2.8% for FY24 and 2.7% for FY25. The December 2022 forecast adds projections for the 2026-2027 biennium, with overall FY26 General Fund revenue projected to grow at a 4.5% rate and FY27 at an 8.6% rate. These growth rates are greater than those projected for the 2024-2025 biennium largely because of the impact of expiring federal tax changes that under current law tax conformity would significantly increase individual income tax revenues starting in tax year 2026.

The RFC has revised Highway Fund revenue estimates upward by $0.6 million for FY23 and reduced estimated revenue by $1.5 million (-0.2%) for the 2024-2025 biennium. The forecasted rate of year-over-year change for Highway Fund revenue for FY23 is -1.5%, followed by growth of 0.4% for FY24 and 0.6% for FY 25. The December 2022 forecast adds projections for the 2026-2027 biennium, with Highway Fund revenue projected to grow at a 0.4% annual rate for FY26 and FY27. The Highway Fund revenue changes are largely the result of forecasted decreases in overall motor fuels revenue, with decreases in estimates for gas tax revenue partially offset by increases in estimates for special fuels tax revenue, and forecasted increases in the motor vehicle registration and fees and other highway fund revenue lines.

Changes to General Fund individual income tax revenue are primarily the result of tax year 2021 net liability growth of more than 22% and more optimistic assumptions of wage and salary growth over the remainder of the forecast period. The November 2022 CEFC forecast assumes that wage and salary income will increase 11.0% during CY22, 6.0% in CY23, 5.0% in CY24, 4.0% in CY25, and 4.3% in CY26 and CY27. The wage and salary forecast results in an increase in forecasted individual income tax liability of $151 million in tax year 2022, $171.1 million in tax year 2023, $179.1 million in tax year 2024 and $186.5 million in tax year 2025. Nonwage sources of income that have contributed to recent monthly surpluses such as capital gains, business, and retirement income are forecasted to increase net tax liability over the forecast period, but at a diminishing rate. Once again, the individual income tax forecast assumes a significant reduction in capital gains realizations in tax year 2022 (-50%), which is consistent with the approach the RFC has taken in forecasting capital gains since the 2002 "April Surprise". A higher inflation forecast by the CEFC has a significant negative impact on revenue through the indexing of various individual income tax parameters (brackets, standard deduction, personal exemption, etc.). The RFC estimates indexing will lower net tax liability by $55.2 million in tax year 2024 and $65 million in tax year 2025 compared to the CEFC's previous economic forecast. Finally, it's important to emphasize that individual income tax revenue growth in FY26 (6.5%) and FY27 (16.3%) is primarily driven by the expiration of federal tax cuts included in the "Tax Cuts and Jobs Act (TCJA)" that the state conformed to in September 2018. Most of the forecasted tax increase is from the expiration of the doubling of the standard deduction amount.

The annual adjustments to the General Fund sales and use tax forecast are relatively minor compared to previous revenue forecasts and reflect a positive variance of $17.2 million through October and the new economic forecast from the CEFC. Beginning in CY23, the November 2022 economic forecast for personal income and saving, combined with a forecast of the composition of personal consumption expenditures results in negative changes to the FY24 and FY25 revenue forecasts for sales and use tax. Personal income adjusted by the saving rate (i.e., personal consumption) falls below the February 2022 economic forecast starting in CY24. In addition, the new economic forecast assumes the shift away from personal consumption on taxable goods toward tax exempt goods (e.g., grocery staples, motor fuels, etc.) increases in early CY23 and the ongoing shift back to consumption of tax excluded services accelerates beginning next year. All of this results in relatively slow growth in sales and use tax receipts over the forecast period.

The revenue changes estimated in this forecast reflect Maine's revenue collection experience through the first four months of FY23 and concerns by many economic forecasters that the global economy is facing a significant slowdown at best, or worse a recession during CY23. However, as noted in recent forecasts, uncertainty continues to be the norm. Most of the short-term risk to the current revenue forecast should continue to be a net positive, while ongoing issues facing the economy (e.g., inflation, stock and real estate market valuations and supply chain and labor force constraints) make the FY24-27 portions of the forecast volatile and susceptible to significant downside risk. The time between this forecast and the next one scheduled for the late spring of CY23 provides time for many of these issues to be resolved or it could result in additional uncertainty, but either way the long-term part of this forecast will remain uncertain until at least later in CY23.

cc: Members, Revenue Forecasting Committee
Members, Consensus Economic Forecasting Commission
Jeremy Kennedy, Chief of Staff, Governor's Office
Kirsten Figueroa, Commissioner, DAFS
Clerk of the House
Secretary of the Senate
Suzanne Gresser, Executive Director, Legislative Council