Alex Kean, Co-chairman
Dept. of Administration and Information
Economic Analysis Division
2800 Central Avenue
Cheyenne, WY 82002
307-777-5287

Don Richards, Co-chairman
Legislative Service Office
State Capitol Building
Room 213
Cheyenne, WY 82002
307-777-7881

Consensus Revenue Estimating Group

Date: April 22, 2016

To: Governor Matt Mead
Members, 63rd Legislature

From: Don Richards, Co-chairman
Alex Kean, Co-chairman

Subject: April 2016 Revenue Update

Purpose of Update *- This revenue update and the accompanying table, taken in combination with the October Consensus Revenue Estimating Group (CREG) forecast and the January forecast, are intended to provide a quarterly summary of the state's major revenue sources. A similar revenue update is issued in July of each year. The January 14, 2016 CREG report remains the official fiscal forecast and is used to derive the revenue pacing expectations in this update. The March 21, 2016 fiscal profile remains LSO's estimate of projected account balances as of June 30, 2016 and June 30, 2018, after taking into account forecasted revenues, transfers and appropriations. This report does not formally modify those forecasts or estimated ending account balances.* ***However, in the last section of this update, the Co-chairmen of CREG offer a cautionary note along with our collective best indication of the FY 2016 revenue collections should the remainder of the fiscal year continue in a manner comparable to the last few months.*** *The information in this update represents revenue collections received from July 1, 2015 through March 2016.*

General Fund - At the end of this update, a summary table of revenues deposited into the General Fund (GF) and Budget Reserve Account (BRA) is presented. The three largest sources of revenue for the GF (sales and use taxes, investment income and severance taxes) are listed separately. All other revenue sources (franchise taxes, cigarette taxes, charges from sales and service, fees, penalties and interest, etc.) are classified collectively for purposes of this update.

Column A reflects the total FY 2016 CREG projections of revenue by major source. Column B contains the actual year-to-date (YTD) revenue received. Column C represents the forecast through March, and Column D is the difference between the YTD forecast and the actual revenues collected (column B minus column C). Column E is the percentage of the projection that has been received (column B divided by column A). Column F illustrates the percentage of the projection expected at this point in the fiscal year. Column G shows the difference of the actual revenue to date as a percentage of the total amount forecast for FY 2016 minus the FY 2016 forecast year-to-date as a percentage (column E minus column F). Occasionally, percentages may not add due to rounding.

As shown in column G, actual total revenues received and directed to the GF are currently estimated at 0.9 percent below the forecast pace for the year. (See line 10.) All major categories of GF revenues, except for investment income comprised of interest and dividends from the Permanent Wyoming Mineral Trust Fund (PWMTF) and pooled income are falling short of the forecast levels through March 2016. Interest and dividends directed to the GF from the PWMTF and the State Agency Pool are ahead of the forecast pace by 0.6 percent and 7.1 percent, respectively. In contrast, sales and use taxes are

2.0 percent below the forecast pace for the year, while severance tax collections are lagging the forecast pace by 2.8 percent. The “all other” category of state revenues is shy of the forecast pace by $1.4 million (0.9 percent). Of the major revenue components in the “all other” revenue category, charges for sales and services are exceeding the projection by the largest percentage. Penalties and interest, on the other hand, are lagging the forecast by more than a factor of three. Many of these revenue streams do not flow to the State with predictable timing over the course of a fiscal year.

State sales and use tax receipts are less than the January 2016 CREG forecast by $9.3 million at this point in the fiscal year. Year-over-year statewide sales and use tax collections are largely down, with just four counties reflecting growth in sales and use tax collections and nine reporting decreases of more than 20 percent, including Converse County with a decline of more than 55 percent.

The major price indices for Wyoming oil and natural gas have been substantially below the January 2016 CREG forecast for the last few months. Correspondingly, the GF share of severance taxes is falling short of the forecast to date by $6.1 million. A more detailed discussion of this revenue category is included in a subsequent section of this memo.

Investment income in the form of interest and dividends from the PWMTF is $0.9 million ahead of the CREG forecast through March 31, 2016 while interest and dividend income from the State Agency Pool directed to the GF is $6.0 million ahead of the projected levels at this time. The State Treasurer does not distribute net realized capital gains, if any, until the end of the fiscal year. As of this writing, there are $10.2 million in realized, but undistributed, capital losses from investments within the PWMTF and $2.7 million in the GF’s share of realized, but undistributed, capital losses from the State Agency Pool. According to the State Treasurer’s distribution policy, any net realized capital losses at the end of the fiscal year will not be distributed and will be carried forward to be offset by future realized capital gains. Furthermore, while any realized capital gains directed to the GF from the State Agency Pool could offset shortfalls in other GF revenue categories, recall that the first $186,668,258 in net realized capital gains from the PWMTF have already been appropriated by the legislature in section 346 of the 2015 Supplemental Budget Bill (2016 Wyoming Session Laws, Chapter 142) and section 13 of 2016 SF0041, State funded capital construction (2016 Wyoming Session Laws, Chapter 97). Even if substantial capital gains are realized from PWMTF investments in the remainder of FY 2016, the gains would not immediately serve to offset shortfalls in sales and use taxes, severance taxes, or other revenue categories.

Budget Reserve Account - The summary table at the end of this memo also illustrates the two earmarked revenue streams for the BRA: severance taxes and federal mineral royalties (FMRs). Severance tax receipts to the BRA are currently falling short of the January 2016 CREG forecastpace, trailing the estimate year-to-date by $5.9 million (4.0 percent). FMRs directed to the BRA, including an adjustment for the federal fiscal year (FFY) 2015 budget sequester (withholding), are $9.3 million (3.9 percent) below the January CREG forecast through March.

Finally, even though reversions of prior appropriations are not forecast by CREG, they do serve to increase the amount of funds available to the BRA for other purposes. Since January 2016, agencies have completed $10.5 million in reversions from appropriations initiated prior to FY 2015, including $4 million that was previously expected. These funds provide an available cash balance for the State that can dampen the effect of lower than forecast new revenues. There are unlikely to be additional sums of this magnitude of reversions from pre-FY 2015 appropriations to bolster the cash balance of the BRA in the future.

<u>Bottom-line: General Fund/Budget Reserve Account -</u> In total, the actual GF and BRA revenue collections are below the pacing (0.9 percent and 3.9 percent, respectively) of the overall January 2016

CREG estimates through March 2016. Income from forecast investment earnings is currently the sole category exceeding projections.

Mineral Severance Taxes - Applying the pacing estimates through March 2016, total severance tax collections are 2.8 percent below the January 2016 CREG forecast. The average price of Wyoming oil for FY 2016 to date is $35.84/bbl, taking into account somewhat higher prices experienced from July 2015 into the fall of 2015 averaged against the comparatively weak prices from early calendar year (CY) 2016. For example, the computed average price for Wyoming oil production in January was just under $25/bbl. Furthermore, the futures markets are signaling the continuation of comparatively low oil prices, at least over the next few months. Oil and gas rig counts have declined from 26 at the end of October 2015 (of which 12 were oil) to 8 in mid-April 2016 (of which 3 were seeking oil). Natural gas prices received by Wyoming producers are averaging just over $2.57/mcf for the current fiscal year to date, as compared to the CREG forecast price of $2.80/mcf. The arc of natural gas prices over the fiscal year is similar to that of oil prices, with somewhat higher prices enjoyed in the first half of the fiscal year as compared to the beginning of the second half of the fiscal year. Current prices are more than a dollar (40 percent) lower than the CREG estimate. Coal prices to date are in-line with the forecast level of $13.50/ton and coal production was consistent with the CREG forecast through December 2015. In fact, surface coal production for CY 2015 exceeded the January CREG forecast by nearly 4.5 million tons. However, coal production reported to the Department of Revenue in the first month of CY 2016 and estimated by the federal Energy Information Administration (EIA) through the first three months suggests a substantial decline in Wyoming coal production. Reported oil and gas production volumes to date are in rough agreement with the January 2016 CREG forecast, with oil production exceeding the forecast by approximately 4 percent and natural gas production falling just shy of the forecast (less than one percent). Given the absence of oil drilling rigs to replace the natural decline in oil production from existing wells, the production trend may come into alignment with the forecast in the near future.

Section 325 of the 2016 Budget Bill (2016 Wyoming Session Laws, Chapter 31) provided for a diversion of the one percent statutory severance tax from the Permanent Wyoming Mineral Trust Fund (PWMTF) to the GF for the balance of this fiscal year in an effort to address the immediate shortfall. Since this legislative action occurred after the January 2016 CREG meeting, the forecast estimate of this additional revenue has been added to the January CREG revenue forecast for the GF, with a corresponding reduction of revenue to the PWMTF using the same price and production forecasts supporting the January 2016 CREG report. The purpose of this adjustment is to properly account for the new revenue directed to the GF and to recognize that if the January CREG forecast is too optimistic, the estimate for the one percent severance tax diversion will also be too optimistic.

<u>Bottom-line: Severance Taxes -</u> In total, severance tax collections are below the January 2016 CREG estimates. Additionally, the price environment for oil and natural gas for the first part of the fiscal year was stronger than the second half, at least to date. Furthermore, levels of coal production for the first six months of the fiscal year appear to be stronger than more recent monthly and weekly production figures.

Federal Mineral Royalties - Total FMRs to date are $14 million (2.5 percent) behind the forecast pace through March 2016. The phenomena impacting oil, natural gas, and coal receipts (the decline in pricing environments for oil and gas and more recent decline in coal production) that apply to severance taxes mirrors that of FMRs. More importantly, revenue collections attributable to FMRs for the fiscal year are short of projections for the first seven months and were supported by stronger price and production levels in the first part of the fiscal year. If the revenue for the remaining five months of production does not rebound from the experience of the most recent months, the difference between actual collections and the January CREG forecast could grow.

Wyoming's share of coal lease bonus payments, as adjusted by the federal sequester, are also shown in the summary table. Receipt of coal lease bonus payments occur annually over five years beginning at the time the federal government finalizes the lease agreement; therefore, amounts reflected here are not indicative of any price or production trends. Coal lease bonus payments are proceeding as expected.

Other Revenue Issues of Note - Investment income in the form of interest and dividends derived from the Common School Permanent Land Fund (CSPLF) are exceeding the estimate by $1.1 million (1.6 percent) through March 2016. Further, $3.7 million in capital losses from the CSPLF have been realized but are being held until such time net realized gains are available to offset the losses before distributing to the Common School Permanent Land Income Fund and subsequently the School Foundation Program account (SFP). Recall that the first three percent of any investment earnings will be deposited into the SFP. Next, an amount equal to investment earnings in excess of three percent and up to the spending policy amount (five percent) will ultimately be deposited into the School Foundation Program Reserve Account (SFP RA). Finally, an amount equal to investment earnings in excess of the spending policy for CSPLF will be deposited into the CSPLF Spending Policy Reserve Account (CSPLF RA) until it reaches its cap. Given the current pace of investment income and realized capital losses, these distributions will not be triggered. If the fiscal year ended on March 31st, no funds would be deposited into the SFP RA, CSPLF RA or the corpus of the CSPLF.

Conclusions and a Look Ahead - Current revenue collections directed to the GF, BRA and SFP are clearly falling short of January 2016 CREG projections, in total. In direct contrast to the April 2015 Revenue Update, interest and dividends are the single, major category exceeding the projection through March 2016, as opposed to the single category lagging the forecast. Without an improved pricing environment for oil and especially natural gas, total severance taxes and FMR collections will fall short of the January 2016 forecast. Although oil prices are garnering a great deal of attention, the natural gas prices incorporated into the January 2016 CREG forecast are currently diverging from actual prices more than those of oil. An environment of lower oil and natural gas prices and lower coal production could further reduce severance tax and FMR collections, as well as contribute to secondary impacts such as a prolonged, associated reduction in sales and use tax collections. The current trends indicate:

- the total FY 2016 revenue forecasts for the GF, BRA, and SFP are unlikely to be met;
- the contingent appropriations adopted in the 2015 Supplemental Budget from FY 2016 revenues will not be fully funded; and
- the spending policy reserve accounts will not receive additional deposits.

In fact, given the known spot market prices from February through mid-April, the futures markets for the remainder of the fiscal year and the EIA data on coal shipments, the weakness in severance tax and FMR collections is likely to be even worse than suggested in the summary table associated with this update. Recall that as a result of de-earmarking, once the “caps” are met the State (GF, BRA, and SFP) bears the full risk of severance tax and FMR revenue collections ending the year under the forecast. Furthermore, those revenues, using accrual accounting, will not be finalized until September 2016 - three months after the end of the current fiscal year. Put differently, there are five months of accrued revenues from severance taxes and FMRs yet to be added, and three of the five months do not reflect price levels sufficient to meet the January 2016 CREG forecast. Using the most recent posted spot market prices, preliminary production data, and the most recent months of sales and use tax collections, the trend for fiscal year end suggests an even deeper revenue shortfall than indicated by actual collections to date. Based upon a trend analysis and non-state revenue data indicators, actual FY 2016 revenues for the GF and BRA are on annualized pace to fall short of the January CREG forecast by approximately $110 to $130 million, after accounting for reversions received to date. If coal production declines further, if natural gas prices slide further after the completion of the winter withdrawal season, or if oil prices or production decline again in the next three months, the shortfall could be worse.

As always, we will continue to monitor the revenue situation and keep you informed. Let us know if you have any questions.

LSO Budget/Fiscal Division

[As of April 22, 2016]

Fiscal Year 2016 Revenue Update Summary: Actual vs. January 2016 CREG Forecast

		A	B	C	D	E	F	G
	Revenue Sources	CREG Forecast FY16 Total	Actual through March	Forecast through March (1)	Difference YTD $	Actual YTD% of Total	Forecast YTD % of Total	YTD Pace
1	GF - Sales & Use Tax (3)	$466,800,000	$301,554,661	$310,900,000	($9,345,339)	64.6%	66.6%	-2.0%
2	GF - PWMTF from dividends & interest (2)	$143,600,000	$108,610,036	$107,700,000	$910,036	75.6%	75.0%	0.6%
3	GF - PWMTF from capital gains (2)	N/A	$0	N/A	N/A	N/A	N/A	N/A
4	GF - Total PWMTF Income (2)	$143,600,000	$108,610,036	$107,700,000	$910,036	75.6%	75.0%	0.6%
5	GF - Pooled income from dividends & interest (2)	$85,000,000	$69,748,660	$63,750,000	$5,998,660	82.1%	75.0%	7.1%
6	GF - Pooled income from capital gains (2)	N/A	$0	N/A	N/A	N/A	N/A	N/A
7	GF - Total Pooled Income (2)	$85,000,000	$69,748,660	$63,750,000	$5,998,660	82.1%	75.0%	7.1%
8	GF - Severance Tax (4)	$217,500,000	$119,326,953	$125,400,000	($6,073,047)	54.9%	57.7%	-2.8%
9	GF - All Other	$148,400,000	$109,948,769	$111,300,000	($1,351,231)	74.1%	75.0%	-0.9%
10	**General Fund - Total (2)**	**$1,061,300,000**	**$709,189,079**	**$719,050,000**	**($9,860,921)**	**66.8%**	**67.8%**	**-0.9%**
11	**General Fund - Total with capital gains (2)**	**$1,061,300,000**	**$709,189,079**	**$719,050,000**	**($9,860,921)**	**N/A**	**N/A**	**N/A**
12	BRA (from Severance Taxes)	$146,600,000	$35,940,175	$41,850,000	($5,909,825)	24.5%	28.5%	-4.0%
13	BRA (from FMRs)	$240,700,000	$87,786,480	$97,125,000	($9,338,520)	36.5%	40.4%	-3.9%
14	**Budget Reserve Account - Total**	**$387,300,000**	**$123,726,655**	**$138,975,000**	**($15,248,345)**	**31.9%**	**35.9%**	**-3.9%**
15	SFP CSPLF dividends & interest portion of investment income (2)	$72,300,000	$55,322,848	$54,200,000	$1,122,848	76.5%	75.0%	1.6%
16	SFP CSPLF from capital gains (2)	N/A	$0	N/A	N/A	N/A	N/A	N/A
17	Total SFP CSPLF from investment income (2)	$72,300,000	$55,322,848	$54,200,000	$1,122,848	76.5%	75.0%	1.6%
18	SFP FMRs	$209,100,000	$132,610,409	$137,300,000	($4,689,591)	63.4%	65.7%	-2.2%
19	**School Foundation Program - Total (without capital gains) (2)**	**$281,400,000**	**$187,933,257**	**$191,500,000**	**($3,566,743)**	**66.8%**	**68.1%**	**-1.3%**
20	**School Foundation Program - Total (with capital gains) (2)**	**$281,400,000**	**$187,933,257**	**$191,500,000**	**($3,566,743)**	**66.8%**	**68.1%**	**-1.3%**
21	SCCA (from Coal Lease Bonus)	$209,100,000	$183,088,685	N/A	N/A	87.6%	N/A	N/A
22	SCCA (from FMRs)	$5,300,000	$5,346,000	$5,300,000	$46,000	100.9%	100.0%	0.9%
23	**School Capital Construction Account - Total**	**$214,400,000**	**$188,434,685**	**N/A**	**N/A**	**87.9%**	**N/A**	**N/A**
24	**Severance Taxes - Total**	**$625,200,000**	**$345,603,113**	**$363,100,000**	**($17,496,887)**	**55.3%**	**58.1%**	**-2.8%**
25	**Federal Mineral Royalties (without CLB) - Total**	**$561,100,000**	**$331,692,890**	**$345,700,000**	**($14,007,110)**	**59.1%**	**61.6%**	**-2.5%**
26	**Federal Mineral Royalties (including CLB) - Total**	**$779,300,000**	**$523,881,575**	**N/A**	**N/A**	**67.2%**	**N/A**	**N/A**

(1) Year-to-date forecast is determined by using one of three methods: the pace of historical revenues is used for sales & use tax projections, a straight-line pace is applied to PWMTF and pooled income, while severance taxes and federal mineral royalties use a procedure relying on price and production weights, taking into account the impact of the repayment of sequestered, or withheld, FMRs.

(2) Capital gains income from PWMTF, Pooled, and CSPLF investments are not currently part of the CREG projection process.

(3) The Impact Assistance balance at the end of March 2016 was $247,829.73; sales and use tax collections have been reduced by this amount. In addition, sales & use tax collections will be adjusted in May 2016 for the special fuel survey.

(4) The FY2016 forecast of severance tax to the General Fund includes the mineral severance tax diversion adopted in Section 325 of Ch. 31, 2016 Session Laws. This severance tax diversion is estimated at $47.7 million in FY16 and has been added to the January 2016 CREG forecast for tracking purposes.