



North Carolina Highway Fund and Highway Trust Fund Revised Revenue Consensus Forecast

FORECAST HIGHLIGHTS

■ The Consensus Forecast Expects Growth for the Biennium

The forecast assumes that significant growth in transportation revenues will be sustained throughout the upcoming biennium.

■ Increasing Revenues

Transportation revenues are expected to increase by \$850 million over the biennium and reach \$5.6 billion by the end of FY 2024-25.

■ Current Year Revenue Is In Line With Expectations

With 7 months of data available, FY 2022-23 transportation revenue appears in line with this year's forecast of just under \$4.8 billion.

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The Fiscal Research Division and the Office of State Budget and Management have reached consensus on the Highway Fund and Highway Trust Fund revenue forecast for the 2023-25 biennium. This report summarizes the forecast for transportation.

Forecast Summary

The Highway Fund and Highway Trust Fund revenue forecast anticipates FY 2022-23 collections to be in line with the April 2022 forecast, with projected overcollections of \$17.6 million (0.4%). The forecast expects significant increases in the upcoming biennium as the share of sales tax revenue transferred from the General Fund to the Highway Fund and Highway Trust Fund increases. Increases in FY 2024-25 are also due to an inflationary rate adjustment to license and registration fees. Due to rising interest rates, investment income is projected to increase significantly. Lastly, motor fuels and highway use tax collections are projected to grow modestly in both years of the biennium. The forecast projects growth in the combined Highway Fund and Highway Trust Fund at an average rate of 9.3% per year compared to FY 2021-22.

Highway Fund and Highway Trust Fund Consensus Summary (\$ in millions)

Fiscal Year	Revenue	Year/Year Change
2021-22	\$4,325.0	n/a
2022-23 (est.)	\$4,791.3	\$466.3
2023-24 (est.)	\$5,159.6	\$368.3
2024-25 (est.)	\$5,641.2	\$481.6

Forecast Detail

Major factors affecting transportation revenue over the past year have included the Russia-Ukraine war and related spikes in motor fuels prices, supply chain constraints reducing the quantity of passenger vehicles for sale, and the transition to a vehicle fleet with higher average fuel economy. These uncertainties, along with the overall tepid forecast for economic growth, suggest caution for transportation revenue. However, North Carolina's population growth and continued economic development point to resilience in weathering nationwide economic issues.

Forecasted growth is largely the result of statutory requirements rather than optimism on the underlying fundamentals. The transfer of 4% of sales tax revenue in FY 2023-24 and 6% in FY 2024-25, required by S.L. 2022-74, 2022 Appropriations Act, accounts for 51% of the forecasted growth over the biennium. Additionally, the Division of Motor Vehicles (DMV) is required by law to adjust various fees every four years based on the rate of inflation over the prior four-year period. The significant actual and forecasted inflation from 2019 to 2023 predicts a 19.1% increase in these fees in FY 2024-25, as compared to the 7.9% adjustment in FY 2020-21. While rising interest rates create uncertainty in the economy, they point to higher investment returns on the cash balance in the Highway Fund and Highway Trust Fund, which is currently over \$2.2 billion.

The **transfer of sales tax revenue** provides a new source of transportation funding, increasing revenue in each year of the forecast.

DMV fees are estimated to grow because of an adjustment to license and registration fees for inflation required every four years.

Investment income rises due to higher interest rates and the cash balances in each transportation fund.

Motor fuels taxes on gasoline and diesel consumption are slowing due to more fuel-efficient vehicles. Population growth continues to build the tax base, resulting in slightly increased collections.

Highway use tax on the sale of vehicles and long-term leases is impacted by price declines, but projected increases in vehicle sales compared to 2022 cause slight increases in revenue.

Motor Fuels Taxes: Nationwide, motor fuels consumption is projected to flatten, despite an increase in vehicle miles traveled, due to increasing fleet efficiency. However, North Carolina is expected to see a modest increase due to increases in population and vehicles registered in the State. Gasoline and diesel prices gradually declining from the peaks seen in summer 2022 is also expected to increase motor fuels consumption compared to FY 2022-23. The motor fuels tax rate, which is set via the formula in G.S. 105-449.80, is projected to fall slightly to 40.4 cents in 2024 due to declines in energy prices from 2022 levels, but then rise again to its current level of 40.5 cents in 2025 due to flat energy prices and an increase in population.

Highway Use Tax: As a function of both vehicle prices and quantity sold, revenue from this tax is projected to increase slightly. This increase is despite forecasted declines in auto prices, particularly in the used market, as quantity of vehicles sold is projected to rise. Rising interest rates for auto loans due to Federal Reserve policy is projected to decrease demand, while supply chain issues ease, increasing supply. The net impact on increased quantity is expected to slightly outweigh the impact on prices, leading to modest increases in revenue growth in each year of the biennium.

License and Registration Fees: Modest increases in the total number of fees paid for driver licenses, truck licenses, vehicle registrations, and vehicle titling in FY 2023-24 should result from population growth. The quadrennial fee increase required in G.S. 20-4.02, beginning July 2024, leads to a significant projected increase in revenue for the second year of the biennium. Most fees are adjusted for inflation except International Registration Plan fees for interstate truck drivers. Total license and fee revenue is projected to increase by \$187 million (18%) in FY 2024-25.

Sales Tax Transfer: Prior to the current fiscal year, sales tax revenues were not a part of North Carolina's transportation funding. S.L. 2022-74 altered this, transferring 2% of FY 2022-23 sales tax revenues to transportation, increasing to 4% in FY 2023-24 and 6% in FY 2024-25. In dollar terms, these increases result in a forecasted \$207.6 million, \$419.6 million, and \$643.5 million of total revenue in each respective year. In FY 2024-25, sales tax revenues are projected to comprise 11.4% of the Department of Transportation's total funding.

Investment Income: Revenue is a function of the cash balances of the Highway Fund and the Highway Trust Fund and the return earned by the Department of State Treasurer on those balances. The current cash balance is over \$2.2 billion between the two funds, and the return has increased as interest rates rise. The investment income revision for FY 2022-23 is \$52.2 million, a 1700% increase over the April 2022 forecast. Over the biennium, the rate of return is projected to continue to rise, offset by a modest decrease in cash balances due to increased maintenance and construction expenditures in the Highway Fund and Highway Trust Fund. The net result is a projected total of \$69.6 million in FY 2023-24 and \$61.0 million in FY 2024-25.

Recap

With collections on target for the current fiscal year, State-specific factors support modest growth in projected Highway Fund and Highway Trust Fund revenue despite uncertainty for motor fuels and highway use taxes through the upcoming biennium. Statutorily required transfers from the General Fund and rate increases for auto-related fees are the main drivers of significant year-over-year increases to the Highway Fund and Highway Trust Fund.