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COLORADO'S REVENUE PICTURE SUGGESTS A NEED FOR AT LEAST \$800 MILLION IN SMART BUDGET REDUCTIONS

PART 1 OF A MULTI-SERIES DISCUSSION OF THE STATE'S FINANCES

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ABOUT THE AUTHORS



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ABOUT COMMON SENSE INSTITUTE

Common Sense Institute is a non-partisan research organization dedicated to the protection and promotion of Colorado's economy. CSI is at the forefront of important discussions concerning the future of free enterprise and aims to have an impact on the issues that matter most to Coloradans. CSI's mission is to examine the fiscal impacts of policies, initiatives, and proposed laws so Coloradans are educated and informed on issues impacting their lives. CSI employs rigorous research techniques and dynamic modeling to evaluate the potential impact of these measures on the economy and individual opportunity.

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CSI is committed to independent, in-depth research that examines the impacts of policies, initiatives, and proposed laws so that Coloradans are educated and informed on issues impacting their lives. CSI's commitment to institutional independence is rooted in the individual independence of our researchers, economists, and fellows. At the core of CSI's mission is a belief in the power of the free enterprise system. Our work explores ideas that protect and promote jobs and the economy, and the CSI team and fellows take part in this pursuit of academic freedom. Our team's work is informed by data-driven research and evidence. The views and opinions of fellows do not reflect the institutional views of CSI. CSI operates independently of any political party and does not take positions.

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INTRODUCTION

Economic headwinds may not blow in the direction of a growing Colorado budget.

On paper, Colorado's budget looks reasonably strong. Policymakers already dealt with a \$1.2 billion income tax shortfall in May. Then, during a special session in August, they addressed another \$1.2 billion shortfall caused by the "One Big Beautiful Bill Act."

To handle these gaps, the state has taken a mix of steps, including bringing in more tax revenue and a vague plan to trim \$300 million in spending.

A new budget cycle has just begun. Governor Polis just released his FY 2026-27 Budget Request, which encompasses an overall budget of \$50.7 billion, including \$18.6 billion from the General Fund.ⁱ

Among the Governor's priorities are increasing per-pupil spending to \$12,272, adding \$14.3 million for universal preschool, putting a ceiling on higher education tuition increases of 2.6%, increasing spending on emergency preparedness by \$7.1 million, capping Medicaid growth, and increasing staff for new state park areas. Overall, the governor's office is recommending additional spending of \$2.7 billion in total funds and \$426 million in General Fund. How can the state afford an additional \$426 million in spending with the national economy weakening? Is this setting policymakers up to do a repeat of 2025, where they dealt with not one, but two \$1.2 billion shortfalls?

In this multi-part budget series, here's a look at the revenue side of the state's balance sheet, with an explanation of why the state may be well-served looking at ways to reduce spending by \$800 million as opposed to boosting it by \$426 million going into the 2026-27 fiscal year.

KEY POINTS

- As a start to the new budget discussion, the governor released his FY 2026-27 budget recommendations, requesting \$2.7 billion in additional spending of which \$426 million would come from the General Fund.
- If revenue drops below trend by 5% in FY 2027, policymakers will have a **\$2.1 billion budget hole.**
- The **state may be well-served looking for ways to smartly reduce spending by at least \$800 million as opposed to boosting expenditures by \$426 million.**
- If the state opts to adopt revenue projections and the associated \$426 million boost to spending from the General Fund for FY 2027, they may be coming back later this year to address a bigger budget hole created by this session's larger spending.

THE REVENUE PICTURE

Recent Colorado revenue projections have been shifting, which complicates budget discussions. In the course of just one year, Colorado's revenue expectations had dropped by over \$3.4 billion for FY 2025 and FY 2026. Now, revenue projections are rising again.

Every quarter, the Joint Budget Committee reviews economic and revenue forecasts prepared by Legislative Council Staff. These projections help guide budget decisions. In March 2024, forecasters projected General Fund revenue of \$18.7 billion in FY 2025 and \$19.7 billion in FY 2026. Fast forward to March 2025, revenue forecasters projected FY 2025 revenue would reach \$17.0 billion and FY 2026 revenue would be \$17.9 billion.

Projections reversed course in June 2025. The FY 2025 revenue came in a little better than expected, with the state having a \$138 million revenue surplus. The FY 2026 forecast, though, had weakened further to \$16.8 billion. The forecast for FY 2027 was updated to \$18.5 billion, an increase of \$1.7 billion.

Most recently, the September 2025 forecasts for FY 2026 and FY 2027 see revenue continuing to grow, reaching \$18.4 billion in FY 2027 and \$19.5 billion in FY 2028.

In light of previous years, it is imperative legislators understand what may happen if new, rosy revenue projections do not materialize. Will spending an additional \$426 million in FY 2027 make it easier later this year or the next to make budget adjustments?

The State is Doing OK, But Won't Avoid U.S. Economic Headwinds

National trends give a broad view of which direction Colorado's economy may head. The U.S. unemployment rate, at 4.3%, is slightly above Colorado's 4.2%.^{ii iii} As one would expect given Colorado's diversified economy, the state's economy follows national trends.

In 2024, the Joint Budget Committee (JBC) projected statewide Gross Domestic Product (GDP) growth of 2.2% for 2025 and 2.0% for 2026. Fast forward to September 2025, and the JBC now expects GDP growth to be 1.6% and 1.4%, respectively (see Figure 1 below). This expected weakness stems from

slower consumer spending and reduced investment activity in both the commercial and residential sectors.^{iv}

As one would expect, a weaker national economy translates into weaker revenue collections for the state. Figure 2 shows General Fund collections based upon the revenue forecasts presented in March, June, and, most recently, September 2025. The blue line captures the March 2025 forecast for fiscal years 2025 and 2026. The red line captures the revenue forecast for fiscal years 2026 and 2027 (2025 actuals were available at the time these estimates were released). The black line captures the most recent September 2025 revenue forecast for fiscal years 2026 through 2028.

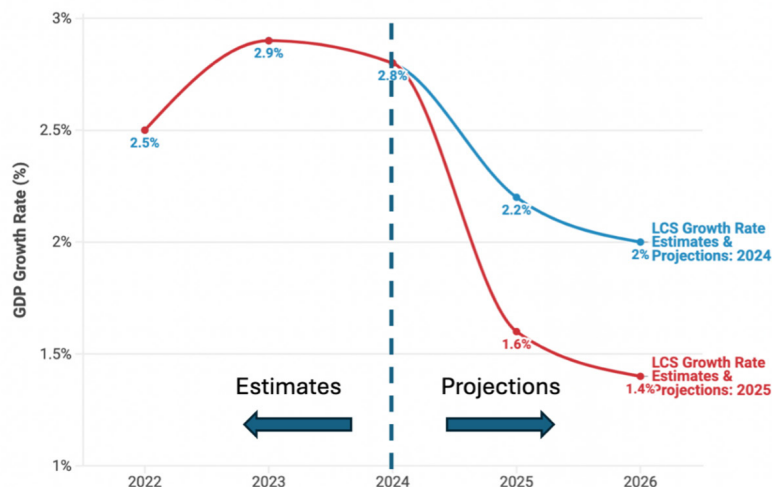
The most recent forecast does not have the type of drop the March and June forecasts had. Instead, the September forecast has revenue mostly flat from fiscal years 2025 to 2026 and then rising quickly in fiscal years 2027 and 2028. Although part of this shift is due to the One Big Beautiful Bill Act, it's clear to see by comparing the black line to the blue line that revenue projections are weaker than just nine months ago.

Perhaps more important than comparing the different colored lines is this question: **What happens if revenue doesn't keep growing?** What if revenue declines? Would assuming that the economy will be fine make it easier to reduce spending if revenue declines? No, of course, boosting spending now assuming revenue will be fine will make the budget situation even more difficult if the economy enters a recession.

FIGURE 1.

Percent Change in Real GDP: 2025 Forecast vs. 2024 Forecast

The Legislative Council Staff's 2024 forecast had a more optimistic outlook for Gross Domestic Product (GDP) in 2024 relative to 2025

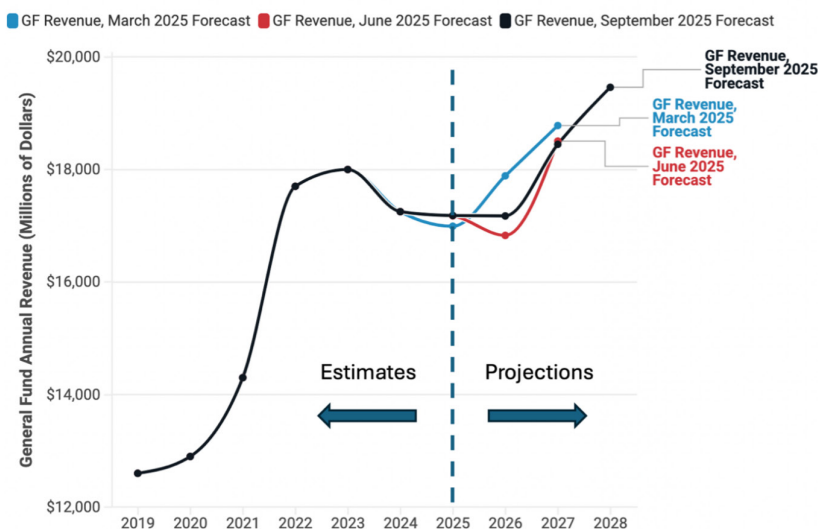


Sources: Colorado Legislative Council Staff, U.S. Bureau of Economic Analysis, 2025



FIGURE 2.

Colorado's General Fund Revenue Forecast, 2019 - 2028



Source: Colorado Legislative Council Staff (LCS), 2025



LOOKING AT THE REVENUE PICTURE FROM A LONGER-TERM PERSPECTIVE

As shown in the previous Figure 2, the current revenue picture assumes revenue will continue to grow. Revenue, however, is cyclical, just like the economy. It goes up in good times and down in bad economic times.

To show that revenue is cyclical – as opposed to just continuing to grow – the following Figure 3 shows revenue collections from FY 2000 through projected FY 2028. The figure adds a green trendline to the forecast that articulates a simple linear regression trend over the period 2000 through 2025.^v As shown, revenue goes up and down. Revenue declined slightly from 2002 to 2003, again from 2009 to 2010, and again from 2024 through projected 2026. The green trendline shows that, generally, one can expect revenue to continue to grow. Just like the stock market or most any other economic measure, that growth is never a steady 5.5%.

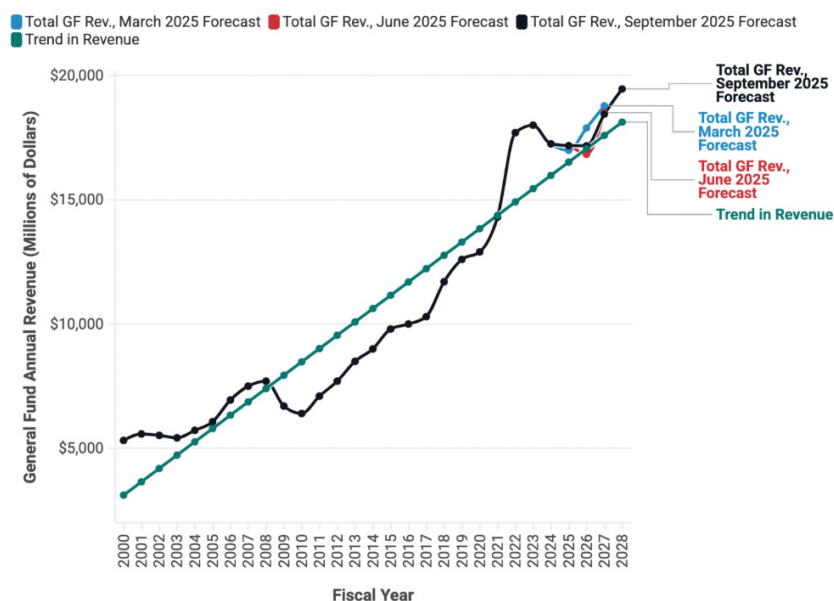
Most important for this discussion are two lines – the black September 2025 revenue forecast for FY 2027 and 2028 and the green forecast for 2027 and 2028. Notice that the black line is projected to be above trend for FY 2027 and FY 2028.

That's a problem if you think the economy is slowing down. Why? Because if the economy does slow down, then General Fund revenue won't reach its all-time high or won't be that much ahead of its all-time high.

The difference between the trend revenue and the currently projected revenue is enormous. The trend revenue forecast would be \$17.6 billion for FY 2027 and \$18.1 billion for FY 2028. The current forecasts have revenue expectations much higher at \$18.4 billion and \$19.5 billion, respectively.

FIGURE 3.

Colorado's General Fund Revenue Forecast, 2000 - 2028



Source: Colorado Legislative Council Staff (LCS), 2025, Common Sense Policy Institute

Since the discussion this year is on the FY 2027 budget, the figure that matters is the \$800 million difference between projected revenue and trend revenue.

If revenue drops below trend by 5% in FY 2027, policymakers will have a **\$2.1 billion budget hole**. In this case, policymakers would be better off addressing the budget hole now. Coming back next year to rescind spending adopted this legislative session is more difficult than simply addressing budget items now.

BOTTOM LINE

With budget season upon us, the discussion now shifts to the Legislature's response to the Governor's proposed budget. The Governor has proposed an additional \$2.7 billion in total spending for FY 2027, of which an additional \$426 million comes from the General Fund. The proposal assumes revenue will continue to expand into FY 2027. Should revenue collections weaken, then spending more money now creates a bigger budget hole in the future – a situation that is becoming increasingly likely.

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- ii. U.S. Bureau of Labor Statistics, "Civilian Unemployment Rate" (chart), accessed [access date], <https://www.bls.gov/charts/employment-situation/civilian-unemployment-rate.htm>
- iii. U.S. Bureau of Labor Statistics, "Local Area Unemployment Statistics (LAUS) — Unemployment Rate, Strike-Affected Workers, 2025," accessed [access date], <https://www.bls.gov/web/laus/laumstrk.htm>
- iv. Colorado Legislative Council Staff (LCS), *"Economic and Revenue Forecast,"* September 2025. <https://leg.colorado.gov/sites/default/files/images/sept2025forecast.pdf>
- v. For simplicity, a simple linear trend is used here. More sophisticated analyses might employ a method like the Hodrick-Prescott Filtering Method. Both would generally show current forecasts above their historical trends.