MINUTES
BALTIMORE COUNTY SPENDING AFFORDABILITY COMMITTEE MEETING
January 30, 2024

The third meeting of the Spending Affordability Committee (SAC) for FY 2025 was held on Tuesday, January 30, 2024 at 3:00 p.m. Committee members, staff, and other participating County government officials in attendance were:

Chairman:	Honorable Pat Young
Members:	Honorable Julian E. Jones, Jr.
	Honorable David Marks
	Edwin Crawford (virtual)
	Dr. Deborah Carter
Committee Staff:	Lauren Smelkinson
	Elizabeth Irwin
	Carrie Vivian
	Ronit Rubin
	Rayven Vinson
	Reginald Sullivan
	Kris Urs
Consultant:	Dr. Anirban Basu

Chairman Young called the meeting to order and welcomed members and attendees.

Approval of the Minutes from the Meeting of January 23, 2024

Councilman Marks moved that the minutes from the meeting of January 23, 2024 be approved, Councilman Jones seconded the motion, and the motion passed unanimously.

Consultant: Economic Analysis and Forecast Update

Highlights of Dr. Basu's update were as follows.

Since Dr. Basu's prior update to the Committee at the January 2, 2024 meeting, new economic data for December 2023 indicates that the economy continues to move forward aggressively. The number of available job openings in the U.S. is 9.0 million, which represents approximately 1.5 job openings per unemployed American. The County and

State’s unemployment rates of approximately 2% are reflective of a continued lack of available workers, which is the leading constraint on economic growth.

Despite prior predictions from economists that the U.S. would experience a recession, with some economists putting the probability at near 100%, the economy continues to perform well. Per recently available data, preliminary estimates of national GDP growth for 2023:Q4 total 3.3% on an annualized basis, following what was already a blockbuster 4.9% for 2023:Q3. The Atlanta Federal Reserve, which maintains the GDPNow model estimate for real GDP growth, indicates that as of January 26, 2024, the outlook is for the economy to grow another 3.0% on an annualized basis through the current quarter. Additionally, according to the December jobs report, in December the U.S. added 216,000 jobs. Consumer spending remains high, with reported record spending on Black Friday and Cyber Monday, as well as aggressive spending on travel. This momentum will carry the economy through the first half of 2024.

The Sage Policy Group personal income forecast for FY 2024 is 4.5%. Sage forecasts somewhat slower growth in FY 2025 amid concerns that there may be economic weakness later in the year. Some theorists believe that tighter monetary policies can take 18 to 24 months, if not longer, to materially affect the economy and inflation. As the Federal Reserve began raising interest rates in March 2022 (i.e., approximately 22 months ago), it is possible that some of those effects are yet to be felt by the economy, presuming the theory is correct.

Dr. Basu noted that the U.S. is seeing a massive amount of credit card indebtedness and rising delinquencies in credit cards, mortgages, and auto loans. Dr. Basu believes that consumers are increasingly under stress, and both consumer spending and the stress of the debt are unsustainable. Dr. Basu speculated that high consumer borrowing despite high interest rates may be due to strong job security. That is, the lack of added fear of losing a job plus the strong labor market relieves pressures to save money and decrease spending.

Chairman Young asked Dr. Basu to expand on why workers feel more secure in their jobs. Dr. Basu speculated that there are likely multiple factors at play, including the experience of many people who have been shifting from job to job due to aggressive recruitment, messaging about low unemployment, and the strong wage increases across even entry-level positions. Dr. Basu stated that wage data supports this, as wage growth is in excess of 4.0% on a per annum basis. Dr. Basu further noted that as the Federal Reserve meets January 30-31, 2024 and again in mid-March, it continues to aim for a 2% inflation target, and strong wage growth will deter it from cutting interest rates. The Federal Reserve may also defer cutting interest rates due to emerging supply chain

issues connected to military operations against Somali pirates and Houthi rebels in the Gulf of Aden and the Red Sea, water levels in the Panama Canal, and higher oil costs.

Councilman Jones reflected on the ongoing strength in the economy and the continued refrain from economists that "the economy continues to surprise us." That is, despite several years of forecasts indicating that the U.S. would enter a recession, that has not come to pass, and the economy continues to defy expectations. Councilman Jones asked for background for when this pattern began to emerge. Dr. Basu stated that the American consumer and the American employer both contributed to this pattern.

First, the American consumer changed their behavior as a result of the pandemic. According to the San Francisco Federal Reserve, Americans amassed about $2.1 trillion in excess savings, meaning savings above and beyond what would have been expected but for the pandemic. Americans are also now spending the savings they amassed due to forgone consumption (e.g., vacations, restaurants, concerts, etc.), with San Francisco Federal Reserve economists estimating that $1.9 trillion of the $2.1 trillion in excess savings have already been spent; and data reflects that this spend-down has led to strong performances in sectors such as retail sales. Individuals may feel the need to "catch up" on missed experiences. Additionally, Americans who purchased homes when interest rates were at record lows may have also spent more on home goods, furniture, appliances, and investments in home remodeling. Dr. Basu suggested that as consumers, particularly the lowest 50% of income earners, strive to maintain the standard of living that they had become accustomed to during the pandemic, they are increasingly borrowing more via credit card debt and maintaining month-to-month balances despite the currently high interest rates. Credit card companies are starting to respond by pulling back on their once-generous extensions of lines of credit, and it remains to be seen how credit card users will adjust to these changes as they try to maintain their consumption habits.

Dr. Basu continued by stating that American employers have also contributed to the economy's surprising performance. Despite challenges with employee retention in the competitive labor market (e.g., 9.0 million available jobs and unemployment near 3.7%), employers are continuing to expand their workforces and offer competitive wages. Citing the recent announcement by UPS to lay off 12,000 employees, which comes on the heels of a newly negotiated 5-year contract with the Teamsters Union for increased wages and benefits for UPS truck drivers, Dr. Basu believes that the pressure to maintain corporate earnings while resisting further price increases will result in layoffs. He estimated that the current economic momentum will be sustained through 2024:Q1 and 2024:Q2, but this pace may change during the summer subject to the behavior of consumers and employers.

Dr. Basu stated that a third facet contributing to the surprisingly strong economic conditions is employment productivity. Economists previously underestimated the productivity boom taking place, likely due to pervasive narratives minimizing Millennial and Gen Z workers, who are proving to be quite productive in certain settings. Employers can benefit from making adjustments to increase productivity and output per hour among existing staff, which may involve changes to procedures or the utilization of AI and other technologies. The productivity boom could be one explanation for the strength and growth of the economy and the dissipation of inflation.

Dr. Carter agreed with this assessment and speculated that big corporations would continue to utilize AI to increase productivity. Dr. Basu noted that recent layoff announcements may support this point, as many have been from technology firms (e.g., Amazon) and financial services firms. He suggested that advances in technology and, subsequently, productivity may create opportunities for increased leisure time among American workers – some jobs functions may be lost but, on balance, technological innovations will end up creating more jobs overall. The key will be for young professionals to be on the right side of that technology spectrum rather than competing against it or competing against someone more adept at using it. Mr. Crawford agreed with that assessment.

<u>General Fund Revenue Forecast Update</u>

Ms. Irwin stated that while revenues for FY 2023 are not yet final, the Office of the County Auditor (OCA) is projecting revenues to total $2.6 billion, which is $104.4 million above budgeted revenues. Revenues for FY 2024 are projected to come in over $50.0 million above budgeted revenues, which is roughly level to FY 2023 collections. FY 2024 is still showing growth in ongoing collections, though transfer and recordation tax revenues have declined this year due to elevated interest rates and the effect on the housing market. There is growth in ongoing revenues and there are also one-time effects that are impacting projections, such as the one-time nature of certain income tax distributions that were received in FY 2023, which cause income tax growth to appear lower than ongoing revenues would indicate. FY 2025 revenues are conservatively projected to total $2.614 billion, reflecting growth of 0.7%.

<u>Discussion of the FY 2025 Spending Guideline</u>

Chairman Young presented the recommended FY 2025 Spending Guideline.

At the prior SAC meeting, staff presented seven personal income forecasts – three from Sage Policy Group and four from Moody's. Consistent with that discussion and last year's

approach, and in light of the Committee’s goals for FY 2025, the Committee had discussed using a blended average. Chairman Young stated that the Committee will be utilizing Sage’s 5-year average of 3.78% together with Moody’s 3-year average of 4.94% to create a blended average of 4.36%.

In addition to the 4.36% growth rate, the Committee discussed making a $9.6 million adjustment to base spending to recognize that revenue availability in recent years has exceeded the spending guideline while budgets have not fully utilized the allowable growth. Ms. Irwin explained that the differential between the budgeted spending subject to the spending guidelines and the spending guidelines themselves totaled $9.6 million over the FY 2022 through FY 2024 period. In light of revenue growth that has well exceeded spending guideline levels in recent years, OCA staff is comfortable recommending a one-time adjustment to base spending to reflect the committee’s approved spending growth during this period. As the budgets have been $9.6 million in total under the Committee’s guidelines during this period, the adjustment to spending for computing the FY 2025 guideline would be in that amount. Any supplemental appropriations or BATs in FY 2024 would not add to the FY 2025 guideline as the Committee typically allows since the maximum allowable level of spending would already be included in the guideline.

Ms. Irwin continued by stating that increasing the adjusted base spending of $2.5 billion by the blended average growth rate of 4.36% will result in a spending guideline of just under $2.61 billion. As in prior years and consistent with Committee policy, the guideline does not apply to the exclusion items.

Councilman Jones moved that the FY 2025 Spending Guideline of 4.36% be approved, Councilman Marks seconded the motion, and the motion passed unanimously.

<u>Presentation of the FY 2025 Debt Guideline</u>

Ms. Smelkinson presented the FY 2025 debt guidelines for the Committee’s consideration.

First, the total outstanding debt should not exceed 2.5% of total assessed property value of $107.4 billion, resulting in a guideline of $2,684,856,675.

Councilman Jones moved that the total debt outstanding during FY 2025 not exceed $2,684,856,675, or 2.5% of total assessed property value of $107,394,267,000, Councilman Marks and Chairman Young seconded the motion, and the motion passed unanimously.

Second, debt service should not exceed 9.5% of General Fund revenues. Accordingly, debt service expenditures should not exceed approximately $248.3 million, which is based on the projected FY 2025 revenues of $2,614.1 million.

Councilman Jones moved that debt service expenditures for FY 2025 not exceed $248.3 million, based on projected revenues totaling $2,614.1 million, Chairman Young seconded the motion, and the motion passed unanimously.

Policy Discussion

Ms. Smelkinson stated that in recent years, the Committee has repeatedly reaffirmed its conservative fiscal policy recommendations, which are as follows:

- The County maintain a sufficient reserve on hand in case an unexpected revenue shortfall occurs. As established by Bill 35-18, the Revenue Stabilization Reserve Account (Rainy Day account) must equal 10% of budgeted General Fund revenues, with the floor level of surplus funds at 7%;
- The County Executive avoid underfunding essential operating budget items in order to fund other initiatives; and
- The County Executive strive to submit a General Fund budget that minimizes reliance on one-time sources of funding, such as surplus funds, for ongoing operating expenses.

Report Issuance

Ms. Smelkinson stated that the statutory report deadline is Thursday, February 15, 2024. The OCA will issue a draft report to committee members by February 7, 2024 and requests a quick turnaround for feedback.

Chairman Young concluded the meeting by thanking the Administration, the committee, and the committee's staff for their work during the FY 2025 spending affordability process. The meeting was adjourned.