MINUTES

BALTIMORE COUNTY SPENDING AFFORDABILITY COMMITTEE MEETING

January 26, 2023

The second meeting of the Spending Affordability Committee (SAC) for FY 2024 was held at 3:30 p.m. on Thursday, January 26, 2023. Committee members, staff, consultant, and other County government officials in attendance were:

Chairman:	Honorable Julian E. Jones, Jr.
Members:	Honorable David Marks
	Honorable Pat Young
	Edwin Crawford
	Dr. Deborah Carter
Committee Staff:	Lauren Smelkinson
	Elizabeth Irwin
	Carrie Vivian
	Michael Walther
	Ronit Rubin
	Rayven Vinson
Consultant:	Dr. Anirban Basu
Other Participants:	Honorable Izzy Patoka
	Stacy Rodgers
	Kevin Reed

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

Approval of the Minutes from Meeting of January 4, 2023

Councilman Young moved that the minutes from the meeting of January 4, 2023 be approved, Councilman Marks seconded the motion, and the motion passed unanimously.

Consultant: Economic Analysis and Personal Income Forecast Update

Dr. Basu stated that Sage's County personal income growth forecasts are 3.8% for FY 2023, 3.3% for FY 2024, and 3.7% for FY 2025; the forecasts are based on the notion that as the country heads toward FY 2024, there likely will be a recession. He reported that although retail sales and industrial production have been decreasing, nationally, the labor market remains strong with 10.5 million available unfilled jobs and an unemployment rate of 3.5%; this week, it was announced that initial unemployment claims for December were 186,000 – a low not seen since the 1960s. Dr. Basu noted that recently announced tech industry layoffs may not be reflected in the data for several months.

Dr. Basu noted that inflation remains an issue; however, it is down to 6.5% from 9% in June 2022. While supply chain issues have been increasingly resolved and other contributors to inflation such as the price of energy (e.g., oil and natural gas) are in decline, the major issue remains the strength of the labor market. With national unemployment near 3.5% and wage growth at 5%, reaching the Federal Reserve's goal of 2% inflation is not possible. Dr. Basu stated that further interest rate increases are likely.

Dr. Basu stated that he expects FY 2025 to be a year of economic recovery, but he emphasized that the County needs to increase its base of residents with jobs, as there are 20,000 fewer residents with jobs than there were pre-pandemic.

Chairman Jones asked Dr. Basu to define the largest area of concern for the County should there be a recession in the upcoming fiscal year, and Dr. Basu replied that the biggest issue from a public policy perspective is household financial stress. Nationally, while individuals had previously saved money during the height of the pandemic with the help of federal stimulus funds, wage growth, and delayed spending (e.g., on travel and dining), the U.S. is now experiencing a collapsing personal savings rate. Additionally, households are accumulating more credit card debt. These factors will worsen exponentially if there are substantial job losses during a recession.

Councilman Young asked Dr. Basu how the County could prepare for a recession to ease its impact. Dr. Basu reminded the Committee that the County secured a significant amount of funds through the American Rescue Plan Act, so there will be a deviation between personal income and County resources, resulting in the County having more resources to spend to offset upcoming economic weakness than it typically would have. Dr. Basu also stated that the County should become more aggressive from an economic development perspective in terms of recruiting and retaining high-growth businesses, and the County needs a housing policy to attract young families in order to add taxpayers. Ultimately, he stated, there are no short-term solutions.

Dr. Carter asked for additional details regarding Dr. Basu's thoughts on needed changes to the County's housing policy. Dr. Basu stated that the County is in need of prime-age taxpayers because the County's demographics are currently unbalanced (skewing older). He also noted the lack of residentially-zoned developable land that is contributing to the County's difficulty attracting commercial enterprises, which are seeking jurisdictions with an ample supply of housing available to attract workers.

General Fund Fiscal Update

Ms. Smelkinson stated that the Office of the County Auditor (OCA) has made some minor adjustments to revenue projections.

For FY 2023, the OCA is projecting General Fund revenues will total approximately $2.5 billion, slightly exceeding FY 2022 collections. The current projection is below FY 2023 budgeted revenues, and represents a modest increase from the OCA's prior forecast.

- The FY 2023 revenue projection is primarily constrained by property-related transaction taxes (transfer and recordation). Following a period of record-low levels, mortgage interest rates have climbed as the Federal Reserve has increased its target rate to combat inflation (range of 4.25% - 4.5% as of December 2022). A continued low available inventory of homes has combined with increased interest rates to drive down both sales and home sales growth. The OCA is expecting these revenues to decrease by $66 million, or 36%, from FY 2022.
- Further constraining FY 2023 growth are conservatively estimated income tax collections, which are not projected to show growth over FY 2022 collections. Factors that drove FY 2021 and FY 2022 income tax growth are expected to moderate and/or dissipate from underlying growth (however, collections this year are benefitting from a one-time large distribution of delinquent TY 2020 filings, which the County received in October).
- Buoying projected FY 2023 revenues are property taxes, which are expected to increase by approximately $34 million, or 3.2%, over FY 2022.
- Budgeted revenues include an additional $28 million in other miscellaneous revenues, including a one-time $25 million transfer from BCPS's fund balance for school capital projects, as well as an increase in Medicaid reimbursements for EMS transportation.

After the expected moderation in FY 2023 revenues, the OCA expects that FY 2024 revenues will rebound modestly. The OCA's preliminary General Fund revenue forecast totals approximately $2.51 billion, an increase of approximately $35 million, or 1.4%, over the OCA's FY 2023 projection. Anticipated revenue growth primarily reflects:

- continued growth in property taxes, which are expected to increase by $43 million, or 3.9%;
- a slight increase in income tax collections. Wages are expected to grow modestly; however, job growth is more uncertain due to the potential of an upcoming recession; and
- a modest increase in State aid to the General Fund proposed in the Governor's FY 2024 budget, primarily through Highway User Revenues.

Revenue growth is partially offset by a decrease of $28 million in one-time FY 2023 revenues. Property-related transaction taxes are also anticipated to fall slightly further following a large drop-off during FY 2023. Home sales are expected to remain curtailed for the near future. However, Federal Reserve interest rate increases are expected to moderate, leading to a plateau in mortgage interest rates and potentially driving prospective homebuyers back into the market during the latter half of CY 2023.

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 a floor level of surplus funds at 7%.
- The County Executive avoid underfunding essential operating budget items, including retiree health care, in order to fund other initiatives.
- 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.

Councilman Young requested more information about the projected decline in transfer and recordation tax revenues. Ms. Smelkinson discussed the effects of rising interest rates, which have led to a low inventory of existing homes for sale. Ms. Irwin added that the projection takes into consideration the year-to-date collections that have been posted to the County's financial system, and she noted that the projected decline in FY 2023 and FY 2024 is from a very elevated (historically high) collection level in FY 2022 (large swings in these revenue streams are not-at-all unusual).

Discussion of the FY 2024 Spending Guideline

Ms. Smelkinson stated that the preliminary spending guideline discussed at the Committee's last meeting is updated to reflect Sage's January 15, 2023 forecast, resulting in a personal income growth 4-year average of 3.88% (down from the October average of 4.20%), multiplied by FY 2023 estimated base spending. This yields a preliminary FY 2024 spending guideline of $2.47 billion and maximum spending growth of approximately $92 million over FY 2023 spending. Ms. Smelkinson noted that the schedule includes two placeholders, reflective of the Committee's consideration last year of providing a guideline exclusion opportunity, allowing for an infusion of funding into the Pension Trust Fund and into the OPEB Trust Fund – which would not represent a multi-year ongoing commitment – but would help to reduce cost pressures and to sustain the financial stability of the respective Trust Funds.

The Committee members discussed expected changes in spending priorities due to the new gubernatorial administration, and Councilman Patoka raised the question of how those changes may result in shifts in State aid to the County. Ms. Smelkinson advised that it has been the County Administration's practice to take into account the State's budget when crafting the County's proposed budget, as the State budget will have been passed by the time the County's proposed budget is presented. Ms. Irwin explained that FY 2024 General Fund revenue projections are at this point preliminary; they will be revised throughout the budget process. The bulk of State aid to the County flows into Special Fund restricted grant programs. Chairman Jones proposed holding another SAC meeting next week to provide time for the State to release additional information, which the Committee can take into consideration prior to finalizing its own guidelines for FY 2024.

Mr. Crawford observed the potential for variability in the State Comptroller's revenue assumptions, and he asked how OBF's financial assumptions compare to Sage's forecast. Mr. Reed stated that OBF utilizes analysis from Moody's, which is currently projecting a 4-year personal income average of 4.72% for the County. Mr. Reed added that the Administration is in the midst of labor negotiations and will need to consider how to address inflationary pressures felt by employees within the proposed FY 2024 budget, in the context of other counties being aggressive with efforts to attract workers, and given an historic County fund balance.

Presentation of the FY 2024 Debt Guidelines

Ms. Smelkinson presented the FY 2024 debt guidelines for the Committee's consideration. First, total debt outstanding should not exceed 2.5% of total assessed property value of $102.6 billion, resulting in a guideline of $2,563,903,500. Second, debt service should not exceed 9.5% of General Fund revenues; accordingly, debt service expenditures should not exceed approximately $238 million based on projected FY 2024 revenues of $2.51 billion.

Plans to Reconvene, Additional Discussion, and Adjournment

The Committee decided to reconvene next week, tentatively February 1 or 2, 2023. Ms. Smelkinson reminded the Committee that the SAC report will contain an updated economic and fiscal analysis, the approved spending and debt guidelines, as well as the Committee's spending policy recommendations. The statutory report deadline is February 15 (Wednesday), and the OCA will issue a draft report to the Committee members prior to that date.

Mr. Crawford cautioned that surplus can disappear quickly – especially in light of the significant pension costs associated with the change in wage base. He also strongly advised against the off-budget reliance on bond premium proceeds to offset debt service interest costs.

Mr. Crawford moved to adjourn the meeting, Mr. Marks seconded the motion, and the motion was approved unanimously.