MINUTES

BALTIMORE COUNTY SPENDING AFFORDABILITY COMMITTEE MEETING

January 2, 2024

The first meeting of the Spending Affordability Committee (SAC) for FY 2025 was held on Tuesday, January 2, 2024 at 3:30 p.m. Committee members, staff, consultant, and other participating County government officials in attendance were:

Chairman:	Honorable Pat Young
Members:	Honorable David Marks
	Honorable Julian E. Jones, Jr.
	Edwin Crawford (virtual)
	Dr. Deborah Carter
Committee Staff:	Lauren Smelkinson
	Elizabeth Irwin
	Carrie Vivian
	Ronit Rubin
	Marie Jeng
	Rayven Vinson
	Reginald Sullivan
Consultant:	Dr. Anirban Basu
Other Participants:	Honorable Izzy Patoka
	Kevin Reed

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

Consultant: Economic Analysis and Personal Income Forecast Update

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

2023 was a surprising year in terms of the country's economic strength. With the Federal Reserve's increases in interest rates beginning in March 2022 and lasting until July 2023 (for a total increase of 5 percentage points from 0.25% to 5.25%), as well as the resulting increase in mortgage costs, many economists expected a slowdown in 2023; however, this did not occur. On the contrary, the economy seemed to get stronger, with GDP growth of 4.9% in 2023:Q3, largely driven by consumer spending. While 2023:Q4 GDP data are not yet available, the consumer still was quite active in 2023:Q4, with record sales both on Black Friday and Cyber Monday.

The labor market has also been surprisingly strong, with an unemployment rate of 3.7% at the national level in November, and State and County unemployment levels of 2% and 2.2%, respectively, in October. The recent strength in the economy provides momentum going into 2024, and it appears that the Federal Reserve has succeeded in engineering a “soft landing,” reducing inflation to 3.1% without triggering a recession. Factors contributing to the soft landing include an abundance of money flowing through the U.S. economy, improvement of the supply chain, and a weak global economy.

The stronger-than-anticipated economy in 2023 did not impact Sage’s personal income (PI) forecast for Baltimore County due to the County’s limited capacity to absorb growth (e.g., low unemployment, decline in population, shrinking labor force). PI performance was strong due to the significant 8.7% Social Security cost-of-living increase for 2023; however, the 2024 increase was only 3.2%, so no matter how well the economy performs in FY 2025, the PI growth forecast will be less.

With regard to 2024, Dr. Basu expressed that he still remains pessimistic, referring to research that indicates that it takes 18 months to 2 years or more for tighter monetary policy/higher interest rates to impact the economy. He pointed out that banks are starting to see more delinquencies on credit card accounts, auto loans, and mortgage loans. Americans accumulated $2.1 trillion in savings during the COVID-19 pandemic, and this savings has now been exhausted. He believes that the first half of 2024 could be weak economically because the lagging effect of the interest rate increases will be felt. Still, he noted that his next forecast, due on January 15th, will be slightly more upbeat than his October forecast, still with some room for caution.

Discussion:

Councilman Jones asked about the impact of borrowers not making their student loan repayments since the end of pandemic-era forbearance. Dr. Basu responded that data indicate that many borrowers had been making their payments during the moratorium, so the impact was not as great as one might have expected. However, for those who weren’t paying down their loans, he said this situation may change at some point in the future. As interest continues to accrue and penalties begin to hit their accounts, people may realize that their credit ratings and ability to borrow are affected by their missed payments, but it is too early to tell what the impact will be.

Councilman Marks asked Dr. Basu for his thoughts on a recent *Wall Street Journal* article, “The Great American Warehouse Boom is Over,” in the context of the County’s Middle River area and Tradepoint Atlantic development. Dr. Basu responded that this question relates to the industrial market, and there were indications that this boom was ending 18 months ago (Amazon, Walmart). He noted that a number of retailers struggled last year, discounting merchandise in order to move it, and he further noted that the supply chain is slowing down, which ultimately translates to less demand for distribution space. Dr.

Basu doesn't expect this type of development activity to be consistent with the level experienced during the last few years.

Chairman Young asked Dr. Basu to discuss the cause of the decline in the labor force and the low unemployment rate. Dr. Basu stated that he believes the cause is demographics; Baltimore County saw a vast number of early retirements due to the pandemic, so now the County has more people living here who are not working, which reduces the number of people available to expand the economy. He expects this situation to change when older residents decide to move, opening up housing opportunities for presumably younger demographic groups. He predicts this change will occur over the next couple of years when mortgage rates fall and both sellers and buyers are prepared to transact.

Chairman Young asked Dr. Basu if he had any policy recommendations to address the topics that had so far been discussed. Dr. Basu responded that the County needs to grow its population and workforce opportunities in order to grow the County's economy, and he noted the importance of expanding housing options to attract both major employers and workers.

Dr. Carter asked about developable land, and further discussion ensued regarding housing. Councilman Marks stressed the crucial role of schools and education policy in attracting young workers with families to the County. He also mentioned the importance of a thoughtful County transportation plan.

Councilman Patoka discussed a three-pronged economic development strategy, including business retention, business attraction, and workforce development; he noted that the County has done well with the latter because there is federal funding for workforce development, as well as County partnerships with CCBC, and he asked Dr. Basu about potential funding sources in order to ramp up business attraction and retention. Dr. Basu agreed that the County does a good job at workforce development, but he advised that the County needs better messaging that speaks to the "heavy hitters" (Intel, Apple, Micron Technologies, etc.) in order to put the County in line for the "next big transformative investment." Councilman Patoka observed the importance of having a County economic development strategy.

Councilman Marks asked if there were any non-Sunbelt cities to which the County could look for policy inspiration. Dr. Basu referred to Madison, Wisconsin; Ann Arbor, Michigan; Indianapolis, Indiana; Boston, Massachusetts; and Boise, Idaho as examples of cities that have experienced exceptional growth in both population and business attraction.

<u>Approval of the Minutes from the Meetings of January 26, 2023 and February 2, 2023</u>

Councilman Marks moved that the minutes from the meeting of January 26, 2023 and February 2, 2023 be approved, and the motion passed unanimously.

General Fund Fiscal Update

Ms. Smelkinson reported that FY 23 General Fund revenues (based on unaudited financial records as of December 2023) totaled approximately $2.63 billion, an increase of $152 million, or 6.1%, over FY 22 revenues. This total reflects an upward revision of $87.5 million from the OCA's forecast provided during the FY 24 budget development process and a surplus of approximately $131 million, or 5.2%, over FY 23 budgeted revenues. FY 23 revenue growth was primarily attributable to income tax collections, which increased by $96.2 million, or 9.7%, over FY 22 collections. This increase was driven primarily by the State's final reconciling distribution for Tax Year 2021 and was also partially due to a large delinquency distribution for Tax Year 2020. The County's investment income also contributed to FY 23 revenue growth, increasing from $1.2 million in FY 22 to $35.7 million in FY 23 due to an elevated fund balance and recent interest rate increases. On the other hand, recent interest rate increases have led to higher mortgage interest rates, which resulted in a reduction of recordation and title transfer tax revenues in FY 23. These revenues decreased by $51.4 million, or 28.1%, from the historically high FY 22 collections. Total FY 23 revenue growth also reflects continued strong and steady property tax growth due to ongoing assessment growth.

In regard to FY 24 revenues, Ms. Smelkinson reported that the OCA's current, unofficial FY 24 revenue projection is $2.56 billion, a decrease of approximately $64 million, or 2.4%, from projected FY 23 collections. Even with the OCA's more tempered outlook, this projection still reflects an increase of $18.6 million over budgeted FY 24 revenues due to slightly increased projections for income and property-related transaction taxes. The OCA's forecast provided during the FY 24 budget development process was in line with the budget forecast. The decrease from projected FY 23 revenues is primarily attributable to an anticipated decline in income tax collections. Varying factors that drove FY 23 income tax revenue growth are expected to moderate and/or dematerialize from underlying growth, resulting in an anticipated decline of $57.9 million, or 5.3%. In addition, property-related transaction tax revenues are expected to decline again in FY 24. Sustained inflation has constrained household incomes, while measures to reduce the pace of inflation by the Federal Reserve have continued to increase mortgage interest rates. As a result, FY 24 recordation and title transfer tax revenues are expected to decline by $13.9 million, or 10.6%, following a decline of 28.1% in FY 23. Slightly offsetting the projected revenue decrease are property taxes, which are expected to increase by approximately $27 million, or 2.5%, over FY 23.

Ms. Smelkinson stated that the OCA is working on a preliminary FY 25 revenue forecast.

Preliminary FY 25 Spending Guideline

The Committee's spending guideline is a recommendation for the maximum level of General Fund spending for ongoing purposes. The OCA is currently working on preparation of the preliminary FY 25 spending guideline.

Therefore, the following is the related guideline policy. The spending guideline typically is calculated by multiplying the previous year's estimated base spending by a multi-year average personal income growth factor. Last year, the Committee utilized a 5-year blended average of Sage's and Moody's County-level personal income forecasts.

In prior years, the Committee typically relied on a 4-year average of the Sage forecast alone. Using Sage's most recent report (October 15, 2023), the preliminary 4-year average (FY 22 - FY 25) personal income growth rate factor for FY 25 is 3.61%. The next forecast from Sage is due January 15, 2024, and the OCA will revise the growth rate factor accordingly.

Preliminary FY 25 Debt Guidelines

The debt guidelines are based on two commonly utilized debt affordability indicators. The policies for the County's two debt guidelines are as follows. Debt Service should not exceed 9.5% of total General Fund revenues, and Total Debt Outstanding should not exceed 2.5% of total assessed property value. These are the guidelines that will be considered at the Committee's next meeting.

Policy Discussion

The Committee also considers spending policy recommendations and has repeatedly reaffirmed its conservative fiscal policy recommendations, which are as follows: that the County maintain a sufficient reserve on hand in case an unexpected revenue shortfall occurs; that, as established by Bill 35-18, the Rainy Day account must equal 10% of budgeted General Fund revenues with a floor level of surplus funds at 7%; that the County Executive avoid underfunding essential operating budget items in order to fund other initiatives; and that the County strive to submit a General Fund budget that minimizes reliance on one-time sources of funding, such as surplus funds, for ongoing operating expenses.

Next Meeting

At the Committee's next meeting[1], staff will provide updated Sage forecast and spending guideline information.

Other Discussion

Mr. Reed shared that the Office of Budget and Finance has been considering other metrics besides Sage's PI growth factor in planning the County's budget growth.

Chairman Young motioned to adjourn the meeting, Councilman Jones seconded the motion, and the motion passed unanimously.

[1] Subsequent to the meeting, the January 29, 2024 meeting at 4:30 p.m. was rescheduled to January 30, 2024 at 3:00 p.m. and an additional meeting was scheduled for January 23, 2024 at 2:00 p.m.