SPENDING AFFORDABILITY COMMITTEE

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Report of the Spending Affordability Committee

Fiscal Year 2022

Baltimore County, Maryland

February 12, 2021

BALTIMORE COUNTY SPENDING AFFORDABILITY COMMITTEE

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Councilman, 5th District

Honorable Todd Crandell
Councilman, 7th District

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SPENDING AFFORDABILITY COMMITTEE

February 12, 2021

Honorable Members of the Baltimore County Council
Honorable John A. Olszewski, Jr., County Executive

I am pleased to submit the report of the Spending Affordability Committee, reflecting the Committee's fiscal policy recommendations for Baltimore County for Fiscal Year (FY) 2022.

For FY 2022, the Committee recommends a base spending guideline of $2,250,922,502, derived from a 4-year average personal income growth rate of 3.86% and FY 2021 base spending of $2,167,266,033. This guideline provides maximum spending growth of $83,656,469 over the FY 2021 adjusted base spending amount and allows for maximum spending growth of $103,656,469 over the FY 2021 budgeted base spending amount of $2,147,266,033. The Committee further recommends that total debt outstanding not exceed 2.5% of FY 2022 estimated assessed property value and that debt service not exceed 9.5% of FY 2022 estimated General Fund revenues. Committee guidelines intend to limit spending such that growth in the cost of County government services does not exceed the growth in the County's economy. In making these recommendations, we emphasize that our guidelines do not represent targets, but rather maximum "should not exceed" levels. In the event that an adopted budget exceeds Committee guidelines, the County Council must provide an analysis of the over-the-guideline amount and explain the rationale for the decision. This situation occurred with the adoption of the FY 2020 budget in May 2019, when both the executive and legislative branches acknowledged that the General Fund's revenue structure was insufficient to support the County's pressing needs and took the serious step of amending the tax structure to meet those needs. Accordingly, last year, the Spending Affordability Committee adjusted its FY 2021 spending guideline calculation to account for a portion of the adopted tax enhancement and in doing so recommended maximum growth of $131 million over the FY 2020 guideline.

As the COVID-19 pandemic took a hold on the economy in the weeks leading up to the County Executive's FY 2021 budget submission in April and the County Council's budget adoption in May, both branches of government agreed that funding a budget at the FY 2021 spending guideline level would impose too great a financial risk. Accordingly, both the Executive and the Council made significant expenditure reductions, and the portion of the adopted budget subject to the spending guideline fell $63 million below the recommended level. Federal coronavirus relief aid, appropriated outside the County's General Fund and not affecting compliance with the spending guideline, was essential to the County's pandemic response; without it, the pressure on the County's General Fund would have forced difficult tradeoffs and/or exhausted rainy day funds. Federal relief funds also were critical to the economy's resilience; without them, the massive levels of lost individual and business income would have devastated households and permanently shuttered companies – and would have severely affected the County's revenue collections. In particular, supplemental unemployment and payroll protection programs sustained several General Fund revenue streams – most importantly income tax. In the early months of the pandemic, we did not know how successful the federal stimulus would be. In retrospect, it was a game-changer, and without it, our County would be confronting a vastly different fiscal outlook.

Due to the success of the federal fiscal stimulus, and the resultant sustained personal income and General Fund revenue growth, this year's Committee process was relatively uncomplicated. The Committee's economic consultant, Dr. Anirban Basu, estimates that personal income grew by more than 7.7% in the second quarter of 2020 and sustained pre-pandemic levels for the remainder of the calendar year. For 2021, personal income is seeing another boost in the first quarter and according to the consultant is likely to return to steady growth by the second half of the year. The consultant's fiscal year projections are for 4.45% growth in FY 2021 and 3.15% growth in FY 2022; the 4-year average growth rate for the FY 2019-FY 2022 period is 3.86%. While Dr. Basu reported that the "V" shaped economic recovery has evolved into a "W," with the second downward slant resulting from the widespread wave of late fall/early winter COVID-19 infections, he remained upbeat for the prospect of "jaw-breaking" growth in the second half of 2021, driven by high levels of savings and pent-up demand to spend on the part of economically secure households. Maryland Board of Revenue Estimates Chairman Andrew Schaufele was similarly upbeat in his December analysis for the State, noting that "[d]espite the severity of the contraction, earned income, consumption, and therefore tax revenue, held up well" and anticipating that the recovery will "slow over the winter months as the pandemic worsens" and "improve in the spring as the current wave dissipates and vaccination begins." Both economists have noted that pandemic job losses have been most severe in lower-wage industries, resulting in a lesser revenue impact than would be the case if higher-wage industries were suffering; rather, higher-wage industries are continuing to show growth, while many unemployed lower-wage workers are collecting unemployment transfer payments that do not deviate significantly from (and in some cases exceed) their pre-pandemic wage compensation. Capital gains income also has been strong, and expectations are for it to remain strong as the federal stimulus continues to circulate in the economy and as investors continue to anticipate higher future prices.

This year, Committee staff again met with the County's budget leadership team to compare and discuss projections. Both offices agreed that taking a moderately conservative revenue forecasting approach for FY 2022 makes sense in light of economic uncertainties and other looming fiscal concerns. Staff continued the discussion regarding structural budgetary imbalance—namely, the off-budget spending for ongoing operational purposes that when viewed collectively with budgeted resources and commitments results in recurring expenditures that exceed budgeted revenues. Everyone continues to agree that the General Fund insurance budget, not the OPEB Trust Fund, should be covering the County's share of the current retiree health care bill, and all are aware that the General Fund debt service budget is presently affordable only because low interest rates have enabled the County to reap debt premiums (which, instead of being recognized as General Fund revenues, have been applied off-budget to lower debt service interest charges hitting the budget). This year, further consensus resulted in a plan to place these issues on the agenda for in-depth discussion during the FY 2023 Committee deliberations process, with the expectation that the Administration will provide, prior to the discussion, all relevant data and consultant analysis.

At this time last year, it appeared that new revenues resulting from the FY 2020 tax enhancement package would be insufficient to cover the County's unbudgeted cost burdens while also meeting scheduled obligations (e.g., rapidly rising retirement system contributions) and a new stream of needs identified by the County Executive. However, the FY 2020 experience was significantly better than expected, due largely to pandemic-related savings, but also due to an over-attainment of revenues, and the result was a structurally balanced outcome, where ongoing revenues were sufficient to cover both on-budget and off-budget recurring costs. This positive outcome was yet unknown during the FY 2021 budget formulation process, when executive branch revenue estimates exceeded legislative branch estimates by more than $192 million. By budget adoption time, the executive branch had lowered its revenue forecast by $69 million and provided assurance that it would reassess budgeted expenditures mid-year for affordability. Employee labor groups stepped up to the table and agreed to some modest budgetary adjustments to enable a balanced budget. During the budget review process, legislative analysts had prepared an extensive analysis of cost-cutting measures that the County could implement should such difficult choices become necessary. Meanwhile – understandably – the FY 2021 budget conservatively (from a fund balance standpoint) maintained reliance upon off-budget funding sources (OPEB Trust Fund and debt premiums) to cover ongoing costs. As the County breathes a collective sigh of relief that difficult, mid-FY 2021 choices do not appear to be on the horizon, the Committee persists in advocating for at least gradual progress toward the goal of bringing all recurring cost commitments on-budget.

In addition to the nagging need to cover retiree health care and full debt service costs on-budget, other impending pressures cast more clouds over the improved General Fund revenue outlook. These pressures include costs to implement Kirwan (Blueprint for Maryland's Future) education legislation should the General Assembly overturn the Governor's veto of it, as well as cash or debt financing needed to upgrade critical infrastructure in response to worsening climate-driven events and school facility needs spanning every geographic area of the County. According to the County's financial consultant, the County will not be able to meet its debt service targets in future years, even without the stepped-up commitments that most elected officials agree are necessary. These challenges require increased commitments from the State, alongside a renewed spirit of fiscal prudence locally.

As I often repeat, if we want things, we must pay for them. The Baltimore County Charter requires us to balance the budget. New budgetary initiatives can subtract from recently enhanced revenue streams and put the County back into a position of needing major budget cuts or increased revenues. While some spending is clearly necessary and justified, it is critical to consider the everyday taxpayer, who cannot afford to pay more in taxes. I appreciate the willingness expressed by many taxpayers – and by employee bargaining groups – in helping to shoulder the fiscal burdens faced to date. This Committee looks forward to continued communication with the County Executive and his team on all of these important budgetary matters, and we urge both promptness and full transparency in those communications.

As always, I would like to thank my fellow Committee members – the Honorable David Marks, the Honorable Todd Crandell, Mr. Edwin Crawford, and Dr. Deborah Carter – for their contributions to this year's process. Thanks also to the Committee's staff including Auditor Lauren Smelkinson, Deputy Auditor Elizabeth Irwin, and the Fiscal and Policy Analysis unit within the Auditor's Office, executive branch staff, the members of the Baltimore County Economic Advisory Committee, and that panel's chairman and economic consultant to this Committee, Dr. Anirban Basu. Thanks to all participants for the shared and steadfast commitment to fiscal responsibility.

As in the past, for FY 2022, we are hopeful that this report will receive careful consideration during the development and review of the County's operating and capital budgets.

Sincerely,

Tom Quirk
Chairman, Spending Affordability Committee
Councilman, 1st District, Baltimore County Council

INTRODUCTION

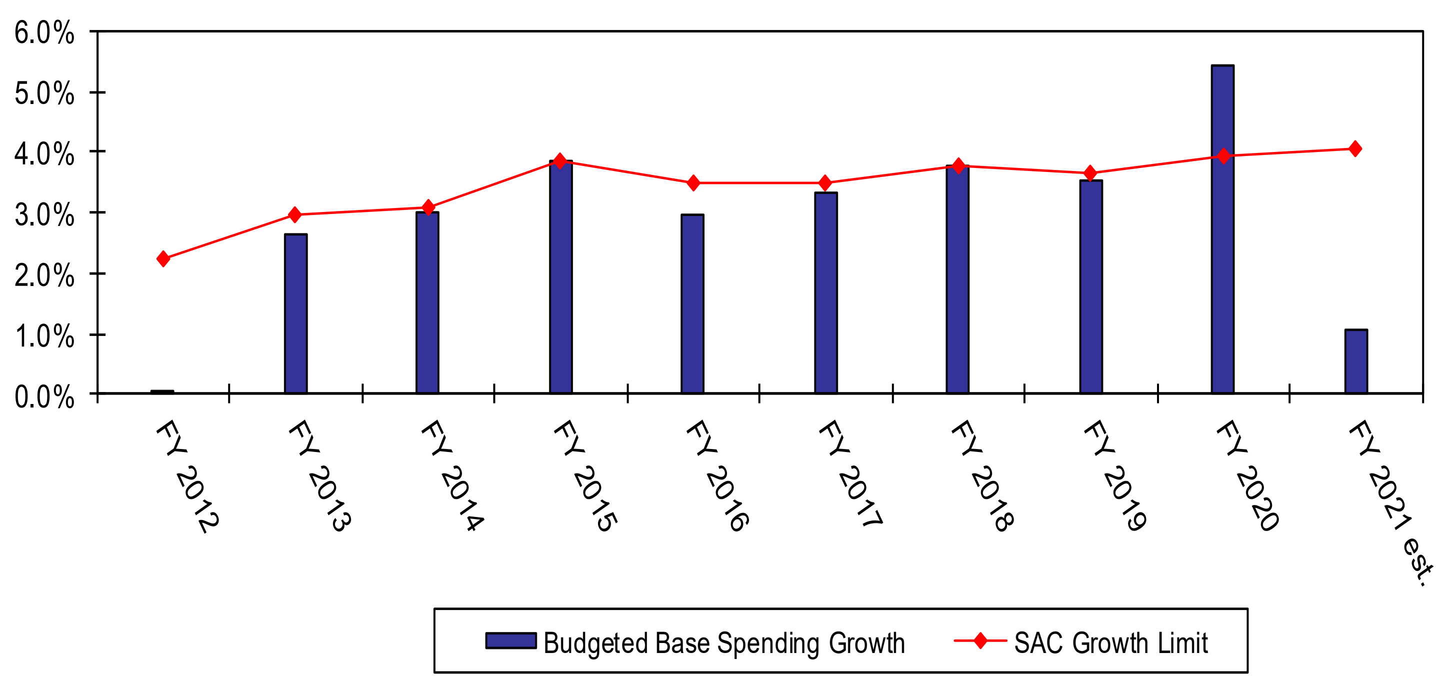
The Baltimore County Spending Affordability Committee was established in order to limit growth in County government spending to a level that does not exceed the growth of the County's economy.

In March 1990, the Baltimore County Council enacted legislation (Bill 33-90) that established a spending affordability law for Baltimore County to ensure that growth in County spending does not exceed the rate of growth of the County's economy (Baltimore County Code, Sections 2-3-101 to 2-3-107). The law mandates that the Spending Affordability Committee make a recommendation each fiscal year on a level of County spending that is consistent with the County's economic growth. The Committee has implemented this law by establishing both spending and debt guidelines. The spending guideline is a recommendation for the maximum level of General Fund spending for ongoing purposes. The debt guidelines are based on two commonly utilized debt affordability indicators.

The Spending Affordability Committee submits its report by February 15 of each year in order to provide timely input into the budgeting process.

By law, the Spending Affordability Committee must submit its report to the County Council and County Executive by February 15 of each year. This reporting date allows the County Executive ample time to consider the Committee's recommendations before submitting the proposed budget to the County Council on or before April 16 of each year. The purpose of this report is to provide formal input to the County Council and the County Executive relative to the formulation of the County budget. Committee guidelines are intended to set recommended maximum amounts or growth levels for County spending that should not be exceeded (Figure 1); however, the law states that the County Council may exceed the Committee's recommendations if it provides a rationale for doing so. In Fiscal Year (FY) 2020, the final adjusted budget exceeded the spending guideline by approximately $29.4 million; the County Council justified its decision to exceed Committee recommendations based on the County's extraordinary operational and infrastructure needs, paired with the establishment of new and enhanced revenue streams. Actual expenditures for FY 2020 fell under the spending guideline, as the County confronted the COVID-19 pandemic and was able to revert more than $64 million to fund balance by fiscal year-end.

Figure 1. Budgetary Compliance with SAC Spending Guideline



SPENDING GUIDELINE

The Committee recommends that base spending growth not exceed 3.86%, bringing the recommended FY 2022 spending limit to $2,251 million.

The spending guideline for a given fiscal year is calculated by multiplying the previous fiscal year's estimated base spending level (as defined by the Committee) by the spending affordability growth factor (Figures 2 and 3). **For FY 2022, the Committee recommends that base spending not exceed $2,250,922,502, calculated by applying an estimated County personal income growth rate of 3.86% to FY 2021 base spending of $2,167,266,033.** This guideline allows for maximum spending growth of $83,656,469 over the FY 2021 adjusted base spending amount. The FY 2022 guideline allows for maximum growth of $103,656,469 over the FY 2021 budgeted base spending amount, which totaled $2,147,266,033 (Figure 3).

To calculate the FY 2022 spending guideline, the Committee added $20 million to the FY 2021 budgeted base spending amount, and multiplied the sum by the personal income growth factor.

Committee policy provides that base spending should reflect all approved and planned spending, less exclusions (see Figure 4), or in other words, "estimated final spending," for the fiscal year. Because the FY 2021 adopted budget fell more than $63 million below the FY 2021 spending guideline, the Committee adjusted FY 2021 base spending by adding to it a portion ($20,000,000, or less than 25%) of the ongoing structural revenue enhancements that were adopted as part of the FY 2020 budget process (such enhancements are expected to total more than $100 million annually, including more than $90 million from the income tax rate change, once they are fully realized).

The Committee continued to utilize a 4-year average of annual personal income growth rates to determine its personal income growth factor.

For FY 2022, the Committee maintained its use of an average personal income growth rate as its measure of growth in the County's economy. The average is calculated based on the annual growth forecasts for the current and upcoming fiscal years and the annual growth estimates for a designated number of preceding fiscal years. The FY 2022 growth factor, like recent years' growth factors, is based on the 4-year average, which includes two preceding fiscal years. Prior to FY 2010, in determining its growth factor, the Committee utilized a single-year forecast, applicable only to the upcoming fiscal year; through FY 2017, the growth factor was based on the 5-year average that included three preceding fiscal years.

Certain appropriations are not subject to the Committee's spending guideline because they do not represent ongoing County program obligations.

A budget's compliance with the spending guideline is determined by calculating the budget's base spending amount, which excludes certain appropriations, and by comparing it to the guideline amount. Appropriations that are one-time/non-recurring in nature (such as certain contributions to the capital budget) or that are required to support a state or federal program (such as local share matching appropriations) are excluded from the base spending amount. Similarly, appropriations that represent only a reserve of funds and not an earmarked expenditure, are excluded from base spending. Historically, the Committee's rationale for excluding certain appropriations has been that the growth in such appropriations should not be tied to growth in the County's economy but should instead be guided by some other factor, such as available surplus or projected revenues. Accordingly, such appropriations are not subject to the Committee's spending guideline (Figure 4).

Figure 2. Calculation of the Spending Guideline

The spending guideline for the upcoming fiscal year is calculated by applying the spending affordability growth factor to the current year's estimated base spending (as defined by the Committee). Specifically, the recommended spending limit is calculated as follows:

FY 2021 Base Spending (budgeted base spending + adjustment reflecting income tax rate effective January 1, 2020)
x Personal Income Growth Factor
FY 2022 Spending Guideline (applicable to base spending only)

Figure 3. FY 2022 Spending Guideline

FY 2021 Estimated Base Spending		$ 2,147,266,033	(A)
Ongoing Revenues Resulting from Structural Adjustment		20,000,000 **	
FY 2021 Estimated Base Spending (As Adjusted)		2,167,266,033	(B)
Personal Income Growth 4-Year Average (FY 2019 - FY 2022)	x	1.0386	
FY 2022 Spending Guideline		$ 2,250,922,502	(C)
Maximum Growth Over FY 2021 Adjusted Base Spending (C - B)		***$ 83,656,469***	
Maximum Growth Over FY 2021 Adopted Base Spending (C - A)		***$ 103,656,469***	

** Base Adjustment, conservatively less than 1/4 of the estimated total CY 2020 income tax enhancement

Figure 4. Spending Affordability Committee Definition of Base Spending

Base Spending: General Fund spending less appropriations not subject to personal income growth, as itemized below.

Appropriations not subject to personal income growth:

Local Matching Appropriations:

- Local Share—State and Federal Grants. The total required County General Fund match for all anticipated grants is based on the level (and match provisions) of grant funding. These funds support state and federal programs (not County programs).
- Education—Federal/Restricted Program. The required County General Fund match for such funds in the Department of Education is similarly based on the level (and match provisions) of grant funding. These funds support federal or other restricted programs (not County programs).

Capital Project Appropriations:

- The General Fund contribution to the capital budget, if any, is determined annually based on funds that are available and not otherwise committed to supporting County services. Thus, such expenditures may be viewed as one-time outlays, not subject to personal income growth, provided these contributions are not dedicated to funding operating expenses.

Certain Reserve Fund Appropriations:

- Appropriations to the Revenue Stabilization Reserve Account (RSRA) do not represent expenditures but rather a reserve of funds available in case of an operating deficit. These funds are legally required to equal at least 10% of budgeted General Fund revenues (with an allowable temporary 7% floor).
- Contingency Reserve appropriations are excludable to the extent they represent a reserve for unforeseen needs (e.g., emergencies) and are not earmarked for a specific purpose or program unless the specific purpose or program meets one of the other criteria for exclusion. If Contingency Reserve funds are spent, the nature of the expenditure must be examined to determine its effect on base spending (i.e., one-time vs. ongoing).

One-Time-Only Appropriations:

- Specific exclusions for extraordinary or special items that represent one-time, non-recurring costs or revenues (such as spending by the Department of Education for items excluded from the State's maintenance of effort requirement) are determined on a year-to-year, case-by-case basis.

SPENDING POLICY RECOMMENDATIONS

The Committee's policy recommendations are that the County maintain a sufficient reserve on hand in case an unexpected revenue shortfall occurs, that the County Executive avoid underfunding essential items, and that the budget minimize its reliance on one-time revenue sources to fund ongoing expenses.

The Committee reaffirmed its conservative fiscal policy recommendations, as follows:

- The Committee recommends that the County maintain a sufficient reserve on hand in case an unexpected revenue shortfall occurs. Accordingly, the Committee endorses the County's policy of requiring that the Revenue Stabilization Reserve Account (RSRA) equal 10% of budgeted General Fund revenues and that the ratio of General Fund balance to revenues does not fall to the floor level of 7% for two consecutive years.
- The Committee recommends that the County Executive avoid underfunding essential operating budget items, including retiree health care, in order to fund other initiatives.
- The Committee recommends that 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. Specifically, the Committee advises against using debt premium funds to offset debt service interest costs, noting that the avoidance of this practice would result in a lower financing cost for County debt, in addition to being a more sustainable budgeting practice.

The Committee's recommendations are designed to ensure that the County's General Fund budget is structurally balanced and fiscally sustainable.

These spending policy recommendations, along with the Committee's spending guideline (see pages 2-3) and usual review of General Fund revenues performance (see pages 9-10), are designed to ensure that the County's General Fund budget is structurally balanced and fiscally sustainable. Specifically, the reserve policy is designed to protect against unanticipated costs or revenue shortfalls. The underfunding policy is designed to ensure that essential costs are not deferred in a given budget year in order to incur new obligations, which when added to the full balance of existing obligations would be unaffordable. The one-time funding policy is designed to ensure that recurring costs are supportable by ongoing streams of revenue. Failure to abide by these recommendations can lead to structural budgetary imbalance, which is not sustainable over the long term.

In FY 2018 and FY 2019, revenue levels were insufficient to keep pace with both budgeted and off-budget recurring expenses. The budgetary decisions leading to this outcome constituted violations of the Committee's (non-binding) policy recommendations. The FY 2020 budget took steps to reduce the gap between total ongoing revenues and total recurring expenses, and the outcome (due in part to pandemic-related savings) was to close the full gap. The FY 2021 budget was conservatively formulated and anticipated resumed reliance on off-budget funding sources.

After several years of budgetary non-compliance with the Committee's (non-binding) policy recommendations, the County's management practices resulted in a structural financial imbalance beginning in FY 2018. Specifically, in January 2019, audited FY 2018 data revealed that ongoing General Fund revenues were insufficient to fund the County's ongoing operating expenses (inclusive of both on-budget and off-budget recurring expenses). The structural financial imbalance persisted in FY 2019. Although the FY 2020 adopted operating budget did not anticipate a return to structural financial balance, due to an over-attainment of revenues and budget savings largely attributable to the pandemic, FY 2020 ongoing General Fund revenues exceeded ongoing operating expenses (inclusive of both on-budget and off-budget recurring expenses). For FY 2021, base spending appropriations are $63 million below the spending guideline, but the adopted budget again anticipated structural imbalance. Specifically, in FY 2021, recurring off-budget commitments are estimated to total at least $89.6 million (the General Fund retiree health care contribution is $67.7 million underfunded based on the Administration's budget projections, and the General Fund budget does not cover $21.9 million in debt service interest costs that will be paid using debt premium funds).

The Committee urges the Administration to resolve the persisting structural budgetary gap as soon as possible, and to present with the FY 2022 budget a comprehensive plan for correcting and addressing any deviations from Committee policy recommendations, to minimize the detrimental effects of such.

During the FY 2020 and FY 2021 budget processes, the Administration acknowledged the structural concerns raised by the Committee but did not present a comprehensive plan to address and correct deviations from the Committee's policy recommendations. The Committee continues to urge the Administration to present a reasonable and responsible plan for correcting or addressing any deviations from Committee policy recommendations, to minimize the detrimental effects of such. Such a plan should chart the County's course to bringing current retiree health care costs entirely back into the General Fund budget (where they were fully funded as recently as FY 2015), to eliminating reliance upon debt premium funds to pay debt service interest costs, and to meeting the County's other needs (e.g., refuse disposal).

Ongoing revenues should be sufficient to fund budgeted expenses in FY 2021 and guideline expenses in FY 2021; however, the Committee continues to urge fiscal restraint due to significant cost pressures both within and outside the budget. The Committee urges the Administration to use excess FY 2021 revenues to lessen the drawdown of the OPEB Trust Fund balance.

Ongoing County revenues are projected to be sufficient to fund budgeted recurring and non-recurring expenses in FY 2021 (see pages 9-10). The Committee urges the Administration to use excess revenues to cover recurring expenses that are presently being funded off-budget—particularly, retiree health care costs that are drawing upon the OPEB Trust Fund balance. FY 2022 ongoing revenues (also see pages 9-10) are projected to be sufficient to fund all guideline (budgeted recurring) spending. It is not the Committee's role to prescribe how the Executive should comply with the Committee's spending guideline and other policy recommendations; however, the Committee continues to urge fiscal restraint due to significant cost pressures both within and outside the General Fund budget, and in light of economic uncertainty given the unprecedented level of federal fiscal stimulus that will at some point dematerialize.

ECONOMIC GROWTH

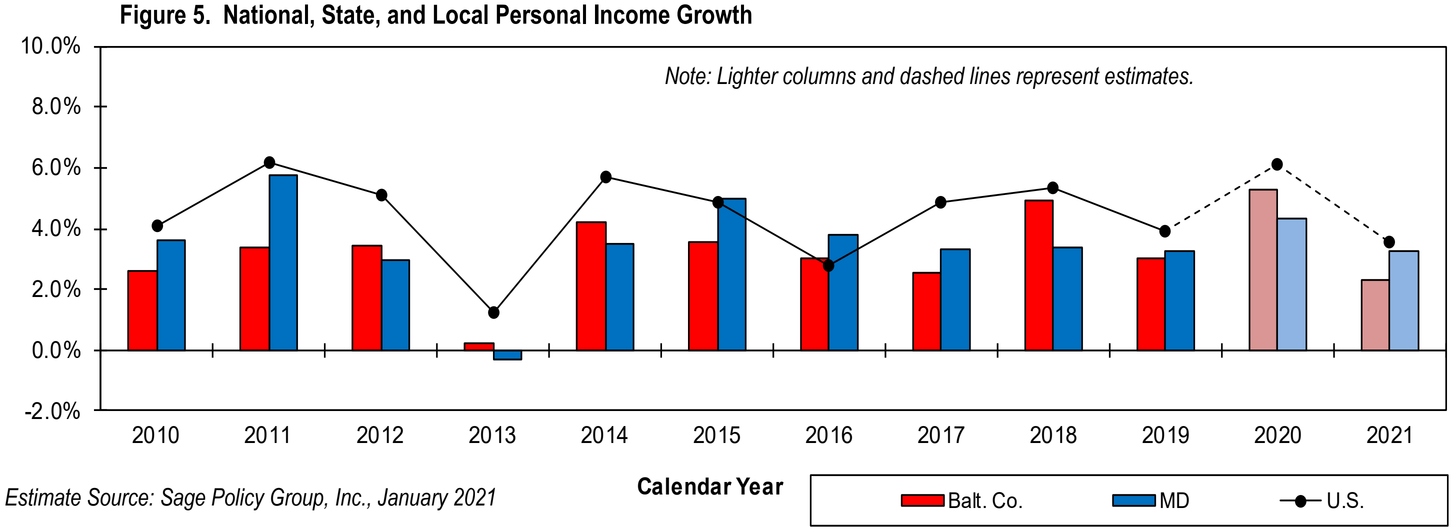
Personal income in the County is projected to increase by 4.45% in FY 2021 and by 3.15% in FY 2022.

Prior to adopting its FY 2022 personal income growth rate of 3.86%, based upon 4-year average growth, the Committee reviewed current and projected economic conditions to gain an understanding of the consultant's personal income estimates and forecast (dated January 15, 2021). The consultant, Sage Policy Group, Inc., predicts that in FY 2021, Baltimore County personal income will grow 4.45%, slightly below a 4.54% forecast for Maryland, following projected growth of 4.40% and 4.42%, respectively, during FY 2020. Over the 2010 to 2019 period, County personal income increased at an average annual rate of 3.09%, compared to 3.42% in Maryland and 4.41% in the U.S. (Figure 5). Although the FY 2020 and FY 2021 forecasts reflect strong growth, much of this growth is driven by a substantial amount of federal stimulus pumped into the U.S. economy to combat economic losses stemming from the COVID-19 pandemic. The stimulus mainly affected 2020:Q2 and 2021:Q1, when personal income is estimated to increase by 7.78% and 4.08%, respectively. For FY 2022, the consultant predicts decelerated growth in both the County (3.15%) and the State (3.29%).

Baltimore County Economic Advisory Committee members expressed concern about the state of the local economy noting that some sectors continue to struggle even as others have held up relatively well.

The January 11, 2021 meeting of the Baltimore County Economic Advisory Committee provided in-depth insight into local economic conditions. The Committee's chairman noted that many sectors of the economy have held up better-than-expected through the pandemic, but he also noted a disparity in the recovery across sectors. The leisure and hospitality sector and a majority of the retail sector have been particularly hard-hit by the pandemic, which has translated into significant job loss among lower-wage workers. Other sectors, such as financial activities and professional and business services, were able to quickly adapt and transition to remote work, lessening the severity of job loss in those typically higher-wage industries. Committee members reported that many small retailers, particularly restaurants, are struggling or have closed. These closures, combined with a surge in remote work that will drive businesses to reevaluate office space needs, could put tremendous pressure on the County's commercial real estate industry. On the residential real estate side, County home values and sales prices have surged, but a rapidly shrinking housing inventory could constrain the number of sales in the near term. Still, the Committee expressed confidence in the spring buying season, as homebuyers continue to seek additional space to fit their new lifestyles and record-low interest rates drive demand. The Committee's chairman foretold that the initially "V" shaped economic recovery has since evolved into a "W," and he expects that the second downturn (recession) likely began in November or December 2020 when retail sales sharply decreased.

Figure 5. National, State, and Local Personal Income Growth



Estimate Source: Sage Policy Group, Inc., January 2021

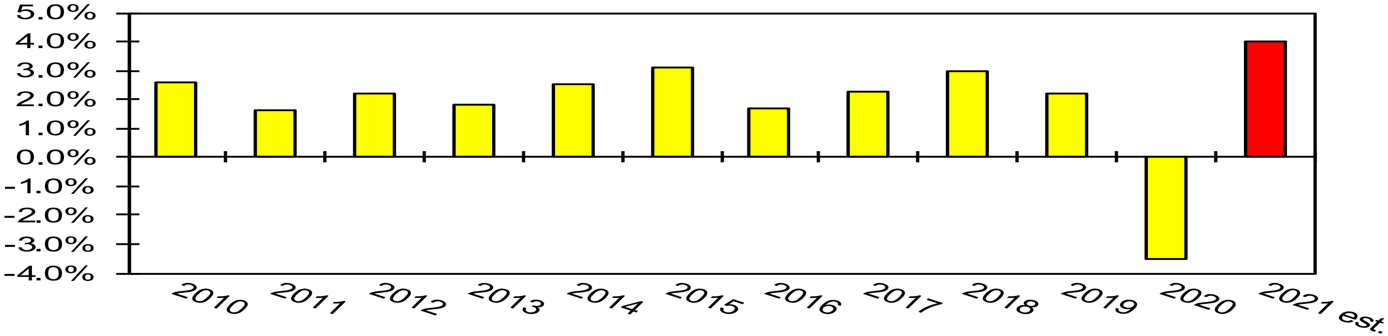
For CY 2021, real GDP is projected to increase by 4.0%, rebounding after a substantial decrease of 3.5% during CY 2020.

Projections for the local economy are influenced, to a large degree, by the underlying performance of the national and state economies. After undergoing the longest economic expansion in U.S. history, real Gross Domestic Product (GDP) began CY 2020 with two consecutive quarterly contractions, including posting the steepest quarterly contraction on record in 2020:Q2, as the economy plunged into recession. Most of these losses were recovered in 2020:Q3, but GDP growth in 2020:Q4 was not strong enough to prevent an annual contraction, as federal stimulus effects waned and the spread of the coronavirus accelerated. During CY 2020, GDP decreased by 3.5%, the first full year of contraction since 2009, and the largest yearly contraction since 1946. Consumer spending, which drove the expansionary period, was the primary driver of the contraction during CY 2020. Gross private investment, specifically nonresidential investment, and reductions in state and local government expenditures also contributed to the GDP contraction. Most recently, in 2020:Q4, GDP increased by 4.0% on an annualized basis. Over the last decade, real GDP grew by an average of 1.7% annually from CY 2011 to CY 2020. GDP is projected to rebound in CY 2021 and increase by 4.0%, according to the Federal Reserve Bank of Philadelphia's November 2020 *Survey of Professional Forecasters*. However, many sectors continue to struggle, and newly filed unemployment claims have begun to increase again. Fortunately, the recently approved Coronavirus Response and Relief Supplemental Appropriations Act of 2021 (CRRSA) provides $900 billion in federal stimulus, including additional unemployment benefits and direct payments to individuals, and should provide a much-needed short-term economic boost.

Employment in the State and County plummeted early in CY 2020 but has begun to recover, albeit at a diminishing pace. Employment growth is expected to continue at a decelerated rate during CY 2021.

Employment decreased by 5.4% among Baltimore County residents, by 5.3% among Maryland residents, and by 5.7% nationally on an annual average basis from CY 2019 to CY 2020—decreasing for the first time after ten consecutive increases for the State and nine consecutive increases for the County and the nation. Regionally, the labor market has added back some of the massive job losses suffered in the spring, but the pace of growth has slowed substantially. The regional labor market has held up comparatively well to the national labor market, with fewer losses due to an abundance of government, health care, and education jobs. However, the economy still supports 30,033 and 227,886 fewer jobs in the County and Maryland, respectively, as of December 2020 compared to the prior year. Baltimore County's and Maryland's unemployment rates surged in April, peaking at 10.5% and 9.8%, respectively, before gradually falling to their most recent rates of 5.9% and 6.0%, respectively, in December 2020. The unemployment rates in the County and Maryland averaged 6.6% and 6.8%, respectively, for all of CY 2020. For CY 2021, Sage Policy Group, Inc. projects that County employment will grow 0.9%, while State employment will decrease by 0.2%. These projections suggest that it will take some time for the local economy to recover to pre-pandemic employment levels.

Figure 6. Real Gross Domestic Product: Annual Percentage Change



Estimate Source: Federal Reserve Bank of Philadelphia's Survey of Professional Forecasters*, November 2020*

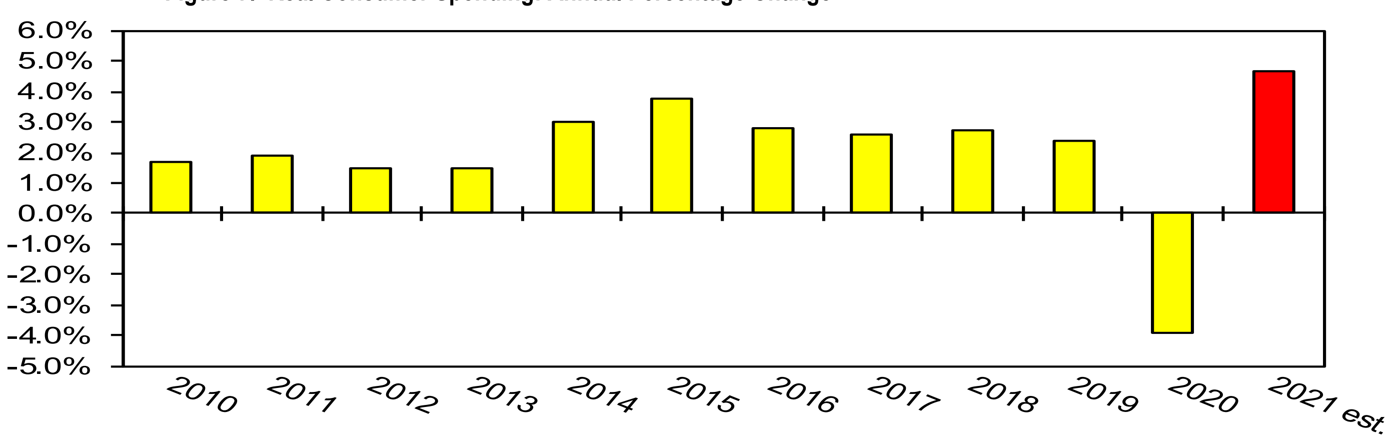
Consumer spending decreased at a rate of 3.9% in CY 2020, the first such decrease after ten consecutive yearly increases.

Consumer spending, which typically accounts for slightly more than two-thirds of all U.S. economic activity, is the primary determinant of future economic performance (Figure 7). Consumer spending decreased at a rate of 3.9% in CY 2020, the first full-year decrease since 2009, but most recently it posted a 2.5% annualized increase in 2020:Q4. Consumer spending is expected to rebound in CY 2021 as the labor market recovers and further federal stimulus combines with pent-up demand to fuel consumption. Consistent with the unsettled state of the present economy, based on a survey of 5,000 U.S. households by the Conference Board, consumer confidence increased slightly in January 2021, with the "Expectations Index" responsible for the increase, slightly offset by a decrease in the "Present Situation Index." The Conference Board reported that "[c]onsumers' appraisal of present-day conditions weakened further in January, with COVID-19 still the major suppressor." However, "[c]onsumers' expectations for the economy and jobs...advanced further, suggesting that consumers foresee conditions improving in the not-too-distant future."

The U.S. economy suffered through CY 2020 as the nation dealt with numerous challenges during a global pandemic. The Committee's consultant warns of challenges in the near term but expects significant growth in the latter half of CY 2021.

At this point last year, the U.S. economy was in the midst of its longest expansion period ever. Soon thereafter, COVID-19 was declared a pandemic, and the U.S. economy went into a tailspin and shed a tremendous number of jobs as various measures attempting to slow the spread of the virus were implemented. The national and local economies' most significant challenges in the coming months are bouncing back from what is likely another recession, adding back the jobs that were lost, easing strains on supply chains, and managing growing business and government debt. The Federal Reserve Bank of Philadelphia's November 2020 *Survey of Professional Forecasters* projects 6.3% unemployment during CY 2021, down from CY 2020, but still much higher than pre-pandemic lows, which also included a significantly larger labor force. The *Survey* further anticipates solid growth in GDP as the economy recovers from a contraction in CY 2020 and suggests a rebound in consumer spending in CY 2021. The Committee's consultant observed, as of January 15, 2021, that the U.S. economy faces several near-term risks including additional business closures, rising interest rates, and some concern that not enough people will be vaccinated to create herd immunity. However, the expectation remains that the economy will experience rapid growth in the back half of CY 2021, similar to the surge seen in summer 2020 when the economy first reopened. The Maryland and Baltimore County economies are likely to follow a similar trend as the national economy, with the potential for accelerated growth during the latter half of 2021.

Figure 7. Real Consumer Spending: Annual Percentage Change



Estimate Source: Federal Reserve Bank of Philadelphia's Survey of Professional Forecasters, November 2020

GENERAL FUND REVENUES AND SURPLUS

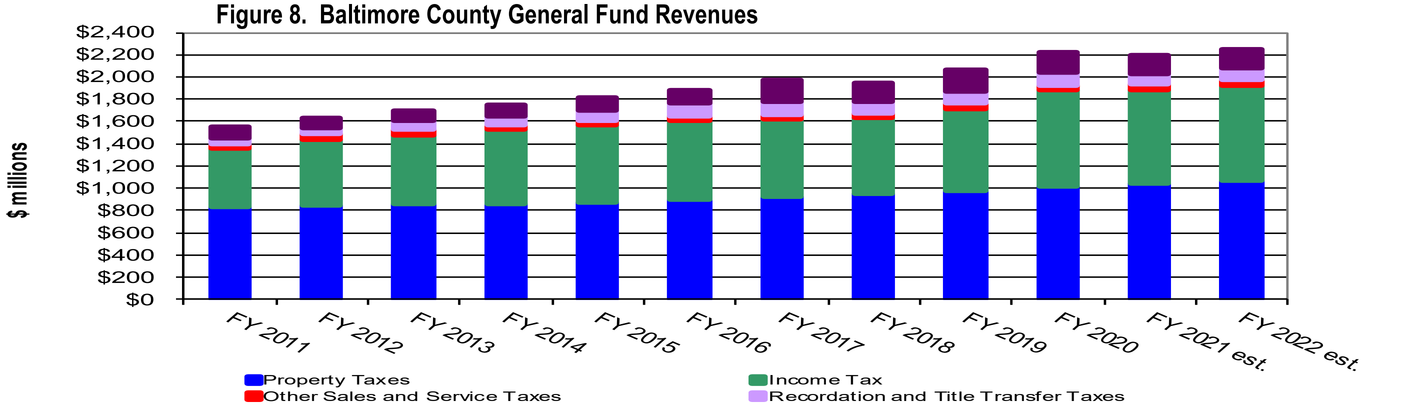
FY 2021 General Fund revenues are projected to decrease by $28.2 million, or 1.3%, from FY 2020 totals, but they are $29.6 million higher than budgeted revenues.

FY 2021 projected revenues total $2,191.3 million, a decrease of $28.2 million, or 1.3%, from FY 2020 revenues (Figures 8 and 9). This projection is $29.6 million, or 1.4%, more than budgeted revenues. The projected decrease (and the resulting modest operational surplus) is vastly improved from the original revenue outlook last spring, when the COVID-19 pandemic had just began its spread in the U.S. Income tax collections have been preserved by substantial federal stimulus, including enhanced unemployment benefits and assistance to businesses designed to keep employees on payrolls. Growth in quarterly withholdings and estimated income tax distributions has been partially offset by a decrease in the highly volatile November 2020 reconciling distribution following a significantly higher-than-normal amount received in November 2019. Income tax collections have been buoyed by an increase to the County's income tax rate that went into effect January 1, 2020. FY 2021 projected income tax collections still represent a decrease of $19.2 million, or 2.2%, from the strong FY 2020 total. The projected FY 2021 overall revenue decrease is moderated by continued strong growth in property tax revenues, which are expected to increase by $29.5 million, or 2.9%. Notably, this forecast does not include impacts that would stem from the Governor's proposed RELIEF Act, which would waive income taxes on unemployment payments. Should this legislation be enacted in its present form, the County would take a $28 million income tax revenue hit, according to analysis provided by the State's Department of Legislative Services.

FY 2022 General Fund revenues are projected to increase by approximately $59.9 million, or 2.7%, over the current (revised) FY 2021 estimate.

FY 2022 General Fund revenues are projected to reach $2,251.2 million, up approximately $59.9 million, or 2.7%, from the current (revised) FY 2021 revenue estimate, and up approximately $89.5 million, or 4.1%, from FY 2021 budgeted revenues. The FY 2022 revenue increase primarily stems from property tax revenues, which are expected to show continued strong growth due to the State's recent reassessment of the County's east region, which is the eighth consecutive reassessment showing positive growth. Property tax revenues are expected to total $1,070.9 million, an increase of $28.4 million, or 2.7%. In addition, income tax collections are expected to increase by $12.9 million, or 1.5%, based on an expectation that economic growth will accelerate as vaccines become more widely available. The projected increase would be more if not for the aforementioned federal stimulus measures, which have bolstered FY 2021 collections. Property-related transaction tax revenues are expected to increase as interest rates remain historically low, home prices continue to rise, and prospective buyers gain confidence in their sustained income prospects. State aid received by the County's General Fund is expected to increase slightly in FY 2022, with modest increases expected in transportation and local health revenues. Notably, the General Assembly is considering a further shift of SDAT costs to the counties; however, similar measures have been defeated in recent years.

Figure 8. Baltimore County General Fund Revenues



Sources: FY 2011 to FY 2020 Baltimore County Comprehensive Annual Financial Reports

Figure 9. General Fund Revenue Forecast, FY 2021-FY 2022

($ Million)

REVENUE SOURCE	FY 2020 Actual	FY 2021 Budget	FY 20 - FY 21 Bud.	FY 2021 Revised	FY 20 - FY 21 Rev.	FY 2022 Estimate	FY 21 Bud.- FY 22	**FY 21 Rev.- FY 22**
Property taxes	$1,013.0	$1,043.5	3.0%	$1,042.5	2.9%	$1,070.9	2.6%	2.7%
Income taxes	862.7	811.2	-6.0%	843.5	-2.2%	856.4	5.6%	1.5%
Recordation & title transfer taxes	114.4	89.3	-21.9%	96.0	-16.1%	105.6	18.3%	10.0%
Other Sales and Service taxes	50.6	50.3	-0.6%	46.9	-7.3%	51.6	2.6%	10.0%
Intergovernmental aid	49.7	51.3	3.2%	50.4	1.4%	50.5	-1.6%	0.2%
Service charges	54.2	53.6	-1.1%	50.4	-7.0%	53.6	0.0%	6.3%
Licenses & permits	5.5	5.3	-3.6%	5.0	-9.1%	5.5	3.8%	10.0%
Fines, forfeitures & penalties	5.1	5.5	7.8%	4.4	-13.7%	5.1	-7.3%	15.9%
Interest on investments	8.2	0.5	-93.9%	1.0	-87.8%	1.0	100.0%	0.0%
Other	56.1	51.2	-8.7%	51.2	-8.7%	51.0	-0.4%	-0.4%
TOTAL	**$2,219.5**	**$2,161.7**	**-2.6%**	**$2,191.3**	**-1.3%**	**$2,251.2**	**4.1%**	**2.7%**

The FY 2022 revenue projection is essentially equal to the Committee's recommended FY 2022 spending guideline.

The FY 2022 revenue projection is level with the Committee's recommended FY 2022 spending guideline. Any potential excess funds, together with the unassigned General Fund balance (surplus), can be used for spending not subject to the guideline, including local share matching funds and one-time expenditures such as PAYGO contributions to the capital budget (which may reduce programmed borrowing).

The FY 2020 surplus totaled $128.2 million, excluding $215.6 million in the RSRA.

As of June 30, 2020, the budgetary surplus balance totaled $128.2 million, not including $215.6 million in the Revenue Stabilization Reserve Account (RSRA). Together, these amounts total $343.8 million, or 15.9% of FY 2021 budgeted General Fund revenues. Effective July 1, 2018, the legally required RSRA balance was increased from 5% to 10% of budgeted General Fund revenues.

The FY 2021 RSRA is currently projected to total $220.8 million, with an additional $124.5 million available in surplus.

The projected June 30, 2021 budgetary surplus, assuming revenues of $2,191.3 million, no supplemental appropriations, and no actions by the Administration to revert appropriations and/or liquidate and release other (e.g., capital projects) funds, totals $124.5 million, or 5.8% of FY 2021 budgeted revenues (Figure 10). This amount does not include an estimated $220.8 million in the RSRA, or 10.2% of FY 2021 budgeted revenues. The FY 2021 adopted operating budget projected a FY 2021 budgetary surplus of $0.5 million, excluding a projected $220.8 million in the RSRA.

Figure 10. Estimated General Fund Budgetary Surplus, FY 2021

		($ in Millions)
FY 2020 General Fund Budgetary Surplus (excluding RSRA funds)		**$ 128.2**
FY 2021 Revenue Estimate (per Adopted Budget)	2,161.7	
FY 2021 Revision	29.6	
FY 2021 Revised Revenue Estimate		2,191.3
FY 2021 Adopted Budget		(2,189.8)
FY 2021 Transfer to the RSRA		(5.2)
FY 2021 Estimated General Fund Budgetary Surplus		**$ 124.5**

DEBT GUIDELINES

The Committee adopts two debt guidelines, one pertaining to total debt outstanding and the other to debt service.

The Committee's debt affordability recommendations provide an enhanced system of checks and balances, further demonstrating the County's fiscal responsibility to its citizens, bond-rating agencies, and others in the financial community. The debt guidelines are based on: (1) the County's total debt outstanding as a percentage of total assessed property value, and (2) the County's level of debt service as a percentage of total General Fund revenues.

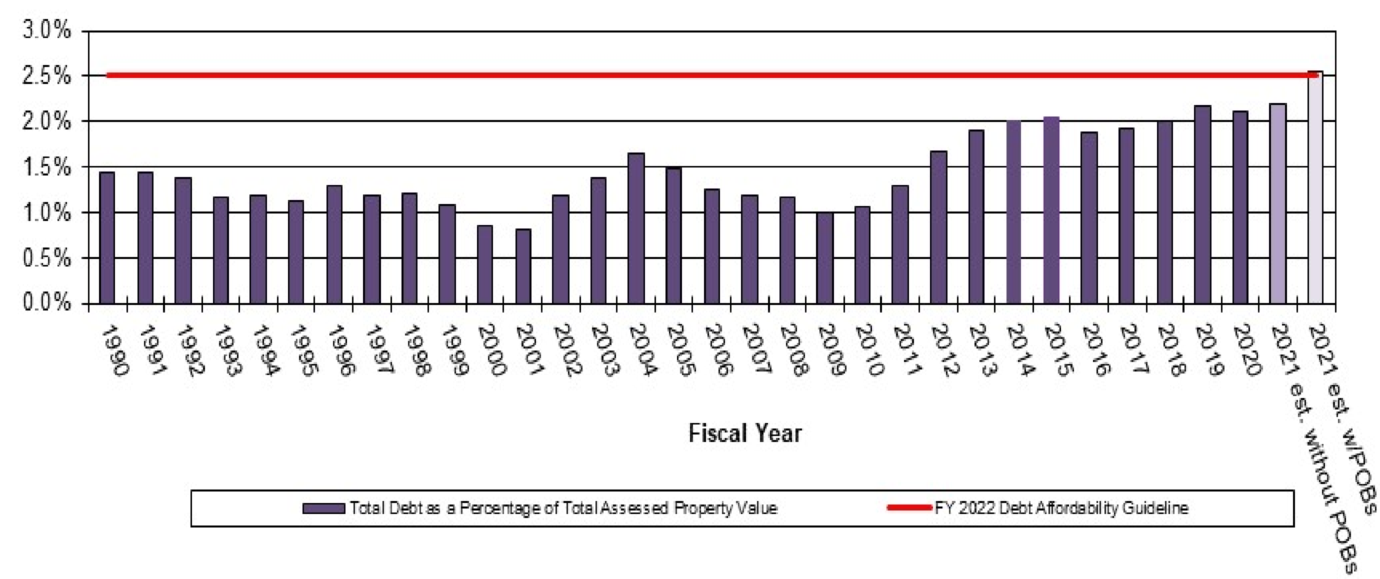
Based on an issuance of up to $240.0 million in new consolidated public improvement (CPI) debt during FY 2021 as authorized by Bill 114-20, the amounts of total debt outstanding and debt service expenditures are expected to continue to remain below both the Committee's and the Administration's guidelines through FY 2021.

Total Debt Outstanding Guideline

The Committee recommends that total debt outstanding not exceed $2,384,246,075, or 2.5% of total assessed property value of $95,369,843,000.

The ratio of total debt outstanding to total assessed property value is a measure of debt affordability. Total assessed property values have continued to increase at a steady pace over the last several years. At the same time, the County's level of total debt outstanding is estimated to increase from $1.9 billion in FY 2020 to $2.0 billion in FY 2021. For FY 2021, the total debt outstanding ratio is estimated at 2.2%, an increase from 2.1% in FY 2020, as assessed property values continue to increase but at a lesser pace than the level of the County's total debt outstanding. The inclusion of pension obligation bond (POB) debt, which is being shown for informational purposes only, would increase the ratio above the guideline, to 2.6% (Figure 11). The Committee's recommended limitation on total debt outstanding currently stands at 2.5% of total assessed property value. **Accordingly, the Committee recommends that total debt outstanding during FY 2022 not exceed $2,384,246,075, or 2.5% of total assessed property value of $95,369,843,000.**

Figure 11. Total Debt Outstanding as a Percentage of Total Assessed Property Value



Note: Excludes debt related to pension obligation bonds (POBs), Metropolitan District bonds, and component unit capital leases not budgeted under Primary Government except for FY 2021, which is shown (for informational purposes) with and without POBs, which were issued in Fiscal Years 1988, 2013, and 2017. FY 2021 debt outstanding is an estimate.

Sources: Baltimore County Comprehensive Annual Financial Reports; Baltimore County Office of Budget and Finance; Maryland Department of Assessments and Taxation.

Debt Service Guideline

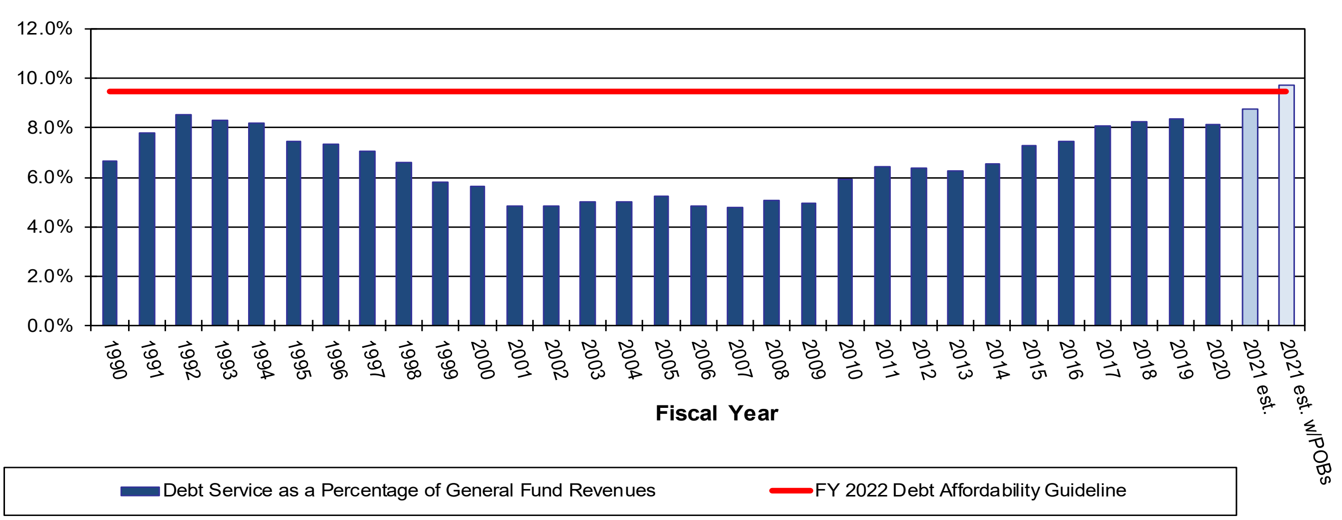
The Committee recommends that debt service not exceed $213.9 million, based on applying a 9.5% guideline to projected revenues totaling $2,251.2 million.

The ratio of debt service to total General Fund revenues is a debt affordability indicator used not only by Baltimore County but by many other jurisdictions. Credit analysts generally concur that a ratio higher than 1:10 (i.e., over 10%) suggests that the debt burden is too heavy. With the exception of FY 2020, when revenues were particularly strong due to increased income tax collections, the ratio of the County's debt service as a percentage of its total General Fund revenues has been increasing steadily since FY 2013. For FY 2021, this ratio is estimated at 8.7%, an historic high. As debt service continues to rise steadily, FY 2021 revenues are expected to decline, largely a result of the impact from the ongoing pandemic. The inclusion of Pension Obligation Bonds (POBs) debt, which is being shown for informational purposes only, would increase the ratio above the guideline level (Figure 12). The Committee's limitation on debt service currently stands at 9.5% of total General Fund revenues. **Accordingly, the Committee recommends that debt service expenditures for FY 2022 not exceed $213.9 million, based on projected revenues totaling $2,251.2 million.**

Budgeted debt service in recent years has not reflected the full amount of the County's debt service cost due to the use of debt premium funds to pay interest costs, which occurs off budget. The Committee discourages this practice and recommends that the County develop a plan to discontinue it.

The ratio of debt service to total General Fund revenues from FY 1990 to estimated FY 2021 is shown below in Figure 12. The decrease in this ratio, beginning in the mid-1990s, is not reflective of a reduction in County capital spending, but rather is the result of increased usage of PAYGO operating budget funds to finance the County's capital budget. Such PAYGO usage also allowed the ratio to remain steady, hovering at around 5%, from FY 2001 to FY 2009, despite a substantial capital budget over that period. As previously noted, in recent years, the ratio has continued to rise, largely a result of the aggressive capital program for school projects. It is noteworthy that budgeted debt service in recent years has not reflected the full amount of the County's debt service cost due to the use of debt premium funds to pay interest costs, which occurs off-budget.

Figure 12. Debt Service as a Percentage of Total General Fund Revenues



Note: Excludes debt service related to pension obligation bonds (POBs), Metropolitan District bonds, and component unit capital leases not budgeted under Primary Government except for FY 2021, which is shown (for informational purposes) with and without POBs, which were issued in Fiscal Years 1988, 2013, and 2017. FY 2021 ratio is an estimate.

Sources: Baltimore County budget documents; Baltimore County Comprehensive Annual Financial Reports; Baltimore County Office of Budget and Finance; Baltimore County Office of the County Auditor.