SPENDING
AFFORDABILITY
COMMITTEE

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Report of the Spending Affordability Committee

Fiscal Year 2025

Baltimore County, Maryland

February 15, 2024

BALTIMORE COUNTY SPENDING AFFORDABILITY COMMITTEE

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Honorable Julian E. Jones, Jr.
Councilman, 4th District

Honorable David Marks
Councilman, 5th District

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SPENDING AFFORDABILITY COMMITTEE

February 15, 2024

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 FY 2025.

For FY 2025, the Committee recommends a base spending guideline of $2,609,637,037, derived from a personal income growth factor of 4.36% and FY 2024 adjusted base spending of $2,500,610,423. This guideline provides maximum spending growth of $118,644,641 over the FY 2024 base spending amount. The Committee further recommends that total debt outstanding not exceed 2.5% of FY 2025 estimated assessed property value and that debt service obligations not exceed 9.5% of FY 2025 estimated General Fund revenues. Committee guidelines aim 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 analysis of the over-the-guideline amount and explain the rationale for the decision.

Along with our spending and debt guidelines, we advise that the Administration adhere to our fiscal policy recommendations—most importantly, avoiding underfunding situations where the budget does not fully reflect the needed costs. This Committee had to grapple with that very issue several years ago, before the current Administration took office. I am encouraged at the Olszewski Administration's commitment to funding retiree healthcare, its continued measured approach to adequately funding the County's pension obligations, and its decision to include all new debt service costs in the budget rather than paying for a portion of them outside the budget. I am confident that our adopted spending guideline is sufficient to fund the County's ongoing operating expenses – including any essential costs now supported by federal ARPA grant funds.

This year, the Committee again considered several guideline options – each aligned with revenue availability. We did not lose sight of the budgetary environment, which has been pressured by the ultra-tight labor market and the related costs of filling positions, providing staff coverage, and making efforts to stay competitive in compensating our hardworking employees. As noted, the Committee has decided to select a 4.36% growth factor for FY 2025. Our decision is bolstered by the most recent optimistic testimony of our economist, as well as the economic forecasting community's upwardly adjusted forecasts for GDP, consumer spending, and employment. Inflation at the grocery store and gas pump have been subsiding. Mortgage rates are edging lower, and there is hope that the Federal Reserve will start reducing interest rate targets by summer.

Still, we are aware that many across Baltimore County are struggling: food banks remain busy; rent costs have skyrocketed, as have utility bills; and child care is increasingly difficult to find and secure. As members of this Committee, we recognize that hardworking taxpayers are the ones that are hit hardest by these challenges. We understand that advancements in technology, such as AI and other types of automation in the Manufacturing & Industrial sector, while providing exciting opportunities, could also present heightened economic hurdles for the average citizen. So, it is imperative that we remain fiscally disciplined as a jurisdiction to ensure that we do not overburden our residents.

In assuming the role of Committee Chair, I have invested time in reviewing the recommendations of previous Baltimore County Spending Affordability Committees. I learned that the deficit facing the County five years ago was not a surprise to this oversight body but rather was an avoidable situation. If there had been a budgetary compliance with all of the Committee's recommendations, I believe we could have been better prepared as a County. I also spent additional time alongside staff reviewing the County debt consultant's report, which provides a sobering set of projections about the County's plans to draw down its fund balance over the next several years. The Office of Budget and Finance assured us that these projections are conservatively estimated, but we are cognizant that some of the County's cost pressures and revenue challenges are lurking beneath the surface. For example, on the cost side, the Employees' Retirement System needs additional support each year to stay solvent, and the amount of additional support needed rises more rapidly with each increase to employee salary scales. On the revenue side, the commercial real estate market is at an inflection point. These property values could decline significantly as office leases expire in the next few years. In the debt report, General Fund debt service appears more pressured in the short term because of the County's sound decision to budget the full interest costs of newly issued debt; however, future debt service pressures are real, and we are concerned that the County's capital program does not fully anticipate future project costs. The debt report also sheds light on the County's capacity to fund public infrastructure improvements. We have a finite amount of funding and authority available for maintaining and upgrading our schools, public buildings, roads, water and sewer systems, and stormwater management facilities; unlike the federal government, we have no choice but to remain committed to prudent debt management practices and to comply with our debt guidelines. We, as the Spending Affordability Committee, need to stay cautious and alert to these and other issues while we remain vigilant in our oversight role to ensure that future County budgets remain sustainable. As the County, State, and region move toward a new normal post COVID, we know our partners in the executive branch will be exercising similar diligence in fulfilling their financial management responsibilities.

I would like to thank both the legislative and executive branch teams for their spirit of collaboration during this year's process. Special thanks to: my fellow Committee members, Honorable David Marks, Honorable Julian Jones, Mr. Edwin Crawford, and Dr. Deborah Carter; County Auditor Lauren Smelkinson, Deputy Auditor Liz Irwin, and their Fiscal & Policy Analysis staff; and the Committee's economic consultant, Dr. Anirban Basu of Sage Policy Group, Inc.

As in the past, for FY 2025, we are hopeful that this report will receive careful consideration during the development and review of the County's operating and capital budgets.

Sincerely,

Pat Young

Pat Young
Chair, Spending Affordability Committee
Councilmember, 1st District, Baltimore County Council

INTRODUCTION

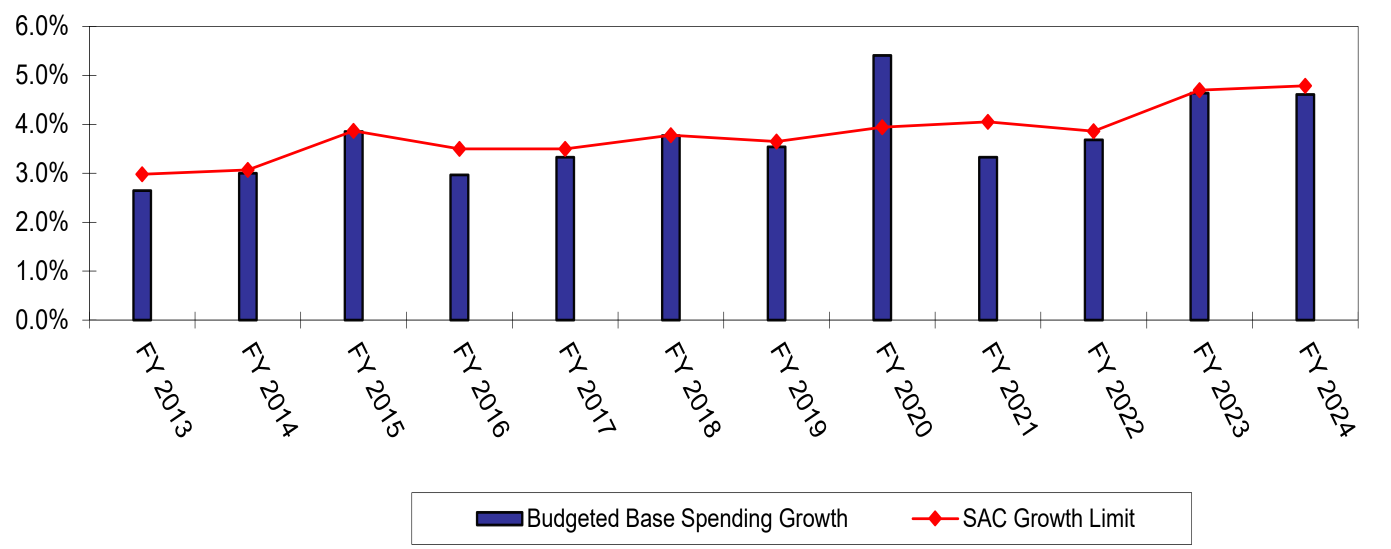
The Baltimore County Spending Affordability Committee was established in order to limit growth in County government spending to a level that does not exceed the growth of the County's economy.

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 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 4.36%, bringing the recommended FY 2025 spending limit to $2,609.6 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 2025, the Committee recommends that base spending not exceed $2,609,637,037, calculated by applying an estimated County personal income growth rate of 4.36% to FY 2024 adjusted base spending of $2,500,610,423.** This guideline allows for maximum spending growth of $118,644,641 over the FY 2024 base spending amount (Figure 4).

The Committee continued to utilize an average of annual personal income growth estimates to determine its personal income growth factor.

For FY 2025, 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 from annual growth forecasts for the current and upcoming periods and estimates for a designated number of preceding periods. The FY 2025 growth factor is based on a blended average of County-level personal income forecasts by Sage Policy Group, Inc. (5-year average) and Moody's Analytics (3-year average). Prior to FY 2010, in determining its growth factor, the Committee utilized a single-year forecast, applicable only to the upcoming fiscal year; from FY 2010 through FY 2017, the growth factor was based on a 5-year average that included three preceding fiscal years; from FY 2018 through FY 2023, the growth factor was based on a 4-year average that included two preceding fiscal years. This year and last, the Committee navigated through the anomalous effects of the heavy infusion of federal transfer payments during FY 2021 by selecting years for inclusion to balance such effects (e.g., this year's 5-year average includes both the "high" year and the "low" year, while the 3-year average includes neither).

The Committee uses an "estimated final spending" methodology to determine base-year spending.

Committee policy provides that base spending should reflect all approved and planned spending, less exclusions (see Figure 3), or in other words, "estimated final spending" for the current fiscal year. This methodology recognizes that certain modifications to planned spending, such as supplemental appropriations, may occur after the budget is adopted. In calculating the FY 2025 guideline, the Committee made a $9.6 million upward adjustment to base spending to account for recent budgets (over the FY 2022 through FY 2024 period) that did not fully appropriate funds at the guideline-allowable levels, despite the availability of ongoing revenues to support such ongoing spending. As a result of this adjustment, the FY 2025 guideline will not be affected by any FY 2024 supplemental appropriations.

Certain appropriations are not subject to the Committee's spending guideline because they do not represent ongoing County program obligations. For FY 2025, the Committee again approved excluding for guideline compliance purposes budgeted Retirement System and OPEB Trust Fund contributions in excess of planned actuarially-determined levels.

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 General Fund 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 3). In recent years, and again for FY 2025, the Committee was in agreement to exclude, for the purpose of assessing guideline compliance, appropriations above the planned actuarially determined contributions for its two retiree-related trust funds, the Pension Benefits Trust Fund and the Other Post-Employment Benefits (OPEB) Trust Fund.

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 - see Figure 3). Specifically, the recommended spending limit is calculated as follows:

General Fund Operating Budget Appropriations (current fiscal year) (1)
- Estimated General Fund Reversion due to detrimental economic events
- <u>Appropriations not subject to growth in personal income</u>

Base Spending (current fiscal year) (2)
x <u>Personal Income Growth Factor</u>

Spending Guideline (upcoming fiscal year)

(1) In calculating the FY 2025 guideline, no supplemental appropriations are added in light of the adjustment to base spending noted below in (2).
(2) In calculating the FY 2025 guideline, an adjustment to base spending is made to account for recent years' ongoing budgets falling below spending guideline levels.

Figure 3. Spending Affordability Committee Definition of Base Spending

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

<u>Appropriations not subject to personal income growth:</u>

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.

Appropriations to Bolster Funded Status of Retiree Trust Funds:

- Pension Benefits Trust Fund contributions above actuarially-recommended levels and OPEB Trust Fund contributions above actuarially-determined funding levels represent non-recurring commitments that are determined on a year-to-year, case-by-case basis.

Figure 4. FY 2025 Spending Guideline

FY 2024 General Fund Appropriations (Original Adopted Budget)	$ 2,710,008,515	
Estimated Final Spending	$ 2,710,008,515	(A)
General Fund Exclusions:		
Local Matching Appropriations		
Local Matching Funds	(11,858,835)	
Capital Project Appropriations		
PAYGO	(173,912,191)	
Reserve Fund Appropriations		
Contingency Reserve	(2,500,000)	
One-Time-Only Appropriations		
Funding for ERS Above Annual Required Contribution	--	
Funding for OPEB Above Actuary's Recommendation	(15,000,000)	
Baltimore County Public Schools[(1)]	(15,745,093)	
Total Exclusions	(219,016,119)	(B)
Base Spending (A - B)	$ 2,490,992,396	(C)
Adjustment to Base Spending [(2)]	9,618,027	
Adjusted Base Spending	$ 2,500,610,423	(C*)
Personal Income Growth Factor	x 1.0436	(D)
FY 2025 Spending Guideline (C* x D)	$ 2,609,637,037	
Maximum Growth in Base Spending	***$ 118,644,641***	

(1) Reflects one-time BCPS costs excluded from the State's maintenance of effort requirement.

(2) Adjusted to align base spending with guideline growth for FY 2022, FY 2023, and FY 2024, in light of available ongoing revenue during that period.

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 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. For example, the Committee advises against using debt premium funds to offset debt service interest costs, noting that the avoidance of this practice results 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 2-4) and usual review of General Fund revenues performance (see pages 10-11), 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 outcomes of the FY 2020 and FY 2021 budget years (due in part to pandemic-related savings) were to close the full gaps between ongoing revenues and expenses. The FY 2022 budget again anticipated reliance on off-budget funding sources, though the gap was again closed (by both a revenue surplus and budget savings).

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 and FY 2021 adopted operating budgets did not anticipate a return to structural financial balance, FY 2020 and FY 2021 General Fund revenues exceeded ongoing operating expenses (inclusive of both on-budget and off-budget recurring expenses) due to an over-attainment of revenues and budget savings largely attributable to the pandemic. For FY 2022, base spending appropriations were below the spending guideline level, but the adopted budget again suggested structural imbalance: specifically, in FY 2022, recurring off-budget commitments were estimated to total more than $60 million (the General Fund retiree healthcare contribution was more than $30 million underfunded based on the Administration's budget projections, and the General Fund budget did not cover $30 million in debt service interest costs that were paid using debt premium funds). Fortunately, a surplus in the Health Insurance Reserve Fund enabled the transfer of $54 million to the OPEB Trust Fund at the close of FY 2022, and General Fund revenue and expenditure experience resulted in a substantial operating surplus.

The FY 2023 and FY 2024 budgets anticipated a reduced reliance on previous off-budget funding sources, but during those years, the Administration utilized the County's established ARPA grant program for certain essential expenses. Still, ongoing revenues are anticipated to be sufficient to sustain ongoing commitments for FY 2023 and FY 2024.

Ongoing revenues also should be sufficient to fund estimated guideline expenses in FY 2025. The Committee endorses the use of any excess revenues and/or General Fund surplus (above legally required and target levels) to cover one-time contributions to the Capital Budget ("PAYGO"), the Employees' Retirement System (Pension Trust Fund), and/or the OPEB Trust Fund (towards future retiree healthcare costs).

For FY 2023, base spending appropriations were below the spending guideline level, recurring off-budget debt service commitments (to be paid with debt premium) totaled more than $20 million, and recurring off-budget employee and retiree healthcare costs (to be paid from health insurance reserve and OPEB Trust Fund balances) totaled more than $10 million, based on projected claims costs. For FY 2024, base spending appropriations were again below the spending guideline level and certain operating expenses were migrating to the General Fund from the Gifts and Grants Fund, after being paid with federal American Rescue Plan Act (ARPA) funds. Recurring off-budget debt service commitments (to be paid with debt premium) total $14.5 million in FY 2024, and the magnitude of ARPA-funded expenses that will migrate back to the General Fund in the near future may be significant. However, it is still anticipated that FY 2023 and FY 2024 ongoing revenues will exceed ongoing expenses (final FY 2023 figures are delayed).

Ongoing County revenues again are projected to be sufficient to cover guideline-level spending in FY 2025 (see pages 10-11). Consistent with Committee policy, any excess revenues and/or fund balance (above the spending guideline and/or sufficient reserve levels, respectively) should be used for one-time purposes such as PAYGO contributions to the Capital Budget. Additionally, the Committee endorses the use of any excess fund balance (above legally required and target levels) to reduce the amount of the unfunded accrued liability from pension and retiree benefit obligations. The Committee is aware that the budgetary consequence associated with having a lower funded status (for pension or retiree benefits) is having a General Fund contribution that is pressured to increase by more from year to year. In this respect, the County's General Fund portion of its Employees' Retirement System (ERS) annual required contribution has more than tripled over the past decade and a half, from less than $50 million in FY 2009, to more than $160 million in FY 2024.

Because it is not the Committee's role to prescribe how the Executive should comply with the Committee's spending guideline, in light of significant cost pressures both within and outside the General Fund budget, and in light of economic challenges including elevated interest rates, the Committee continues to urge fiscal restraint with the use of excess revenues and/or General Fund surplus. Accordingly, the Committee again approves, for guideline compliance purposes, the exclusion of appropriations above planned actuarially determined levels for both the Pension (ERS) and the OPEB Trust Funds. The Committee allows for such guideline exclusions in acknowledgement of County officials' commitment to ensuring solvency of both funds.

ECONOMIC GROWTH

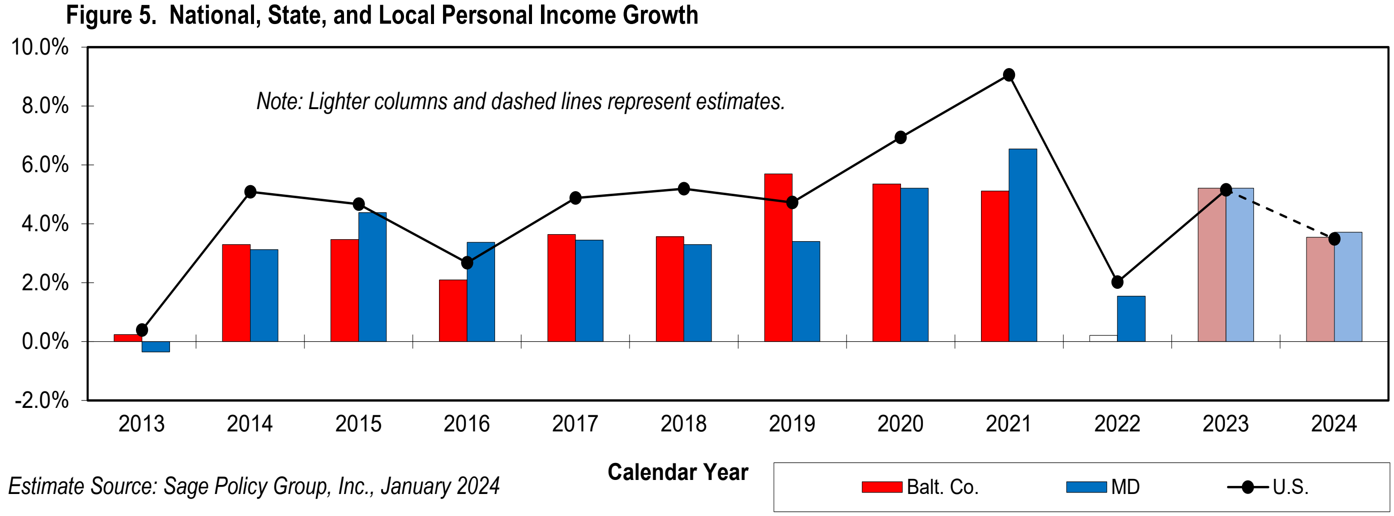
Personal income is projected to continue increasing at an above-average rate in the current and upcoming fiscal years. Growth during the pandemic was unusually elevated due to federal stimulus assistance.

Prior to adopting its FY 2025 growth rate, the Committee reviewed current and projected economic conditions both nationally and locally. As of January 15, 2024, Sage Policy Group, Inc. predicts that in FY 2024, Baltimore County personal income will grow 4.18%, slightly below a 4.26% forecast for Maryland, representing a slight deceleration from growth of 4.26% (estimated) and 4.94%, respectively, during FY 2023. For FY 2025, the consultant anticipates that personal income growth will continue to decelerate in both the County (3.54%) and the State (3.65%). Over the 2013 to 2022 period, County personal income increased at an average annual rate of 3.27%, compared to 3.40% in Maryland and 4.56% in the U.S. (Figure 5).

Baltimore County Economic Advisory Committee members expressed lingering concern regarding the possibility of a looming recession but were generally optimistic about economic prospects in the coming year.

The January 9, 2024 meeting of the Baltimore County Economic Advisory Committee (BCEAC) provided insight into local economic conditions. The BCEAC's economist noted that despite prior, consistent predictions that there would be a recession in 2023, the national economy has been building, rather than losing, momentum, and many economists have accordingly rescinded their recession forecasts. He explained that policy efforts (e.g., interest rate increases) by the Federal Reserve to engineer a "soft landing" have contributed to a steady decline in inflation, while the economy has continued to advance, with real GDP growing at a 4.9% clip during 2023:Q3. Retail sales have continued to climb, and consumer spending on services, such as concerts, events, and travel has been surging. Consumer optimism has been linked to the tight labor market, where workers feel secure in their jobs and future prospects in light of the historically low unemployment rate; the BCEAC's employment representative affirmed such perceptions, observing that local companies are still very interested in hiring. The BCEAC Chairman has repeatedly warned that the County's labor force does not offer much room for employment growth. From the residential real estate vantage point, home prices remain elevated despite slowing demand during the past year – boding well for County property tax revenues – and, as mortgage interest rates decline, hope is emerging for a busier spring and year to come – portending a rebound in title transfer and recordation tax revenues. While commercial real estate concerns related to remote work are less prominent in a predominantly suburban – as opposed to urban – market, the risk to County property tax revenues will become more apparent as office leases expire over the next several years. On another cautionary note, the BCEAC conversation turned several times to the recently reported County population loss – which can adversely affect intergovernmental aid. Other issues and trends of concern to BCEAC members include the high cost of housing, public school test scores, the resumption of student loan repayments, increasing credit card debt and delinquencies, escalating federal debt, geopolitical conflict, the uncertainty surrounding this year's presidential election, and the inevitable revolutionary impact of artificial intelligence on humanity (and the economy).

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



Estimate Source: Sage Policy Group, Inc., January 2024

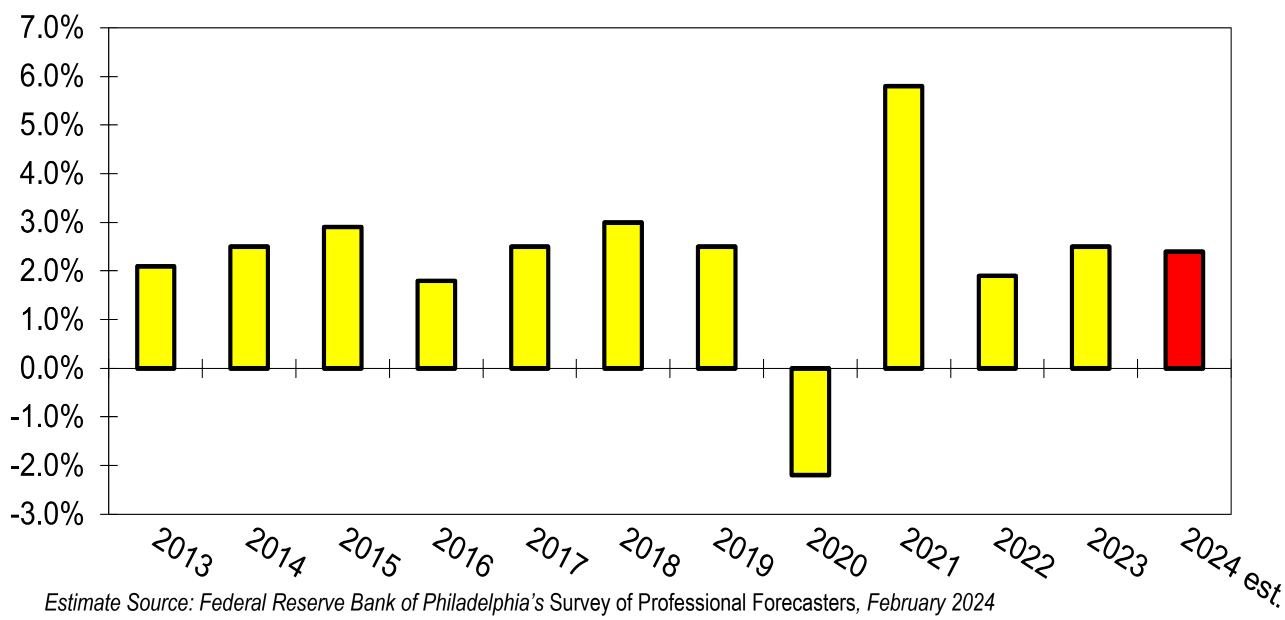
For CY 2024, real GDP is projected to increase by 2.4%, nearly steady from 2.5% growth in CY 2023, and above average growth over the past decade.

Projections for the local economy are influenced, to a large degree, by the underlying performance of the national and State economies. After a rapid see-saw in real Gross Domestic Product (GDP) during the early years of the pandemic, first contracting by 2.2% in CY 2020 and then seeing sky-rocketing expansion of 5.8% in CY 2021, growth in the U.S. economy has somewhat stabilized and exceeded expectations. Real GDP posted a modest increase of 1.9% in CY 2022, and this performance was followed more recently by accelerated growth of 2.5% in CY 2023. Greater consumer spending, particularly on durable goods and services, drove much of the recent economic expansion. Overall, consumer spending decelerated slightly in CY 2023 to 2.2% after growing by 2.5% in CY 2022. Looking ahead, GDP growth is projected to remain nearly steady in CY 2024, advancing by 2.4%, according to the Federal Reserve Bank of Philadelphia's February 2024 *Survey of Professional Forecasters.* Gross private investment, in the face of high interest rates, showed a 1.2% decrease in CY 2023 after posting 4.8% growth in CY 2022, suppressing GDP growth in CY 2023. Over the last decade, real GDP grew by an average of 2.3% annually from CY 2014 to CY 2023.

Employment growth in the County was minimal during CY 2023, attributable to the size of the labor force, which is still significantly shrunken from its pre-pandemic capacity. For 2024, the Committee's consultant projects County employment growth of 1.5%. Unemployment remains at historic lows, with employers actively seeking to hire qualified workers.

CY 2023 continued the pandemic-recovery employment gains made in CY 2022, following years of annual job losses. As of December 2023, the economy supports 16,254 and 136,743 fewer jobs in the County and Maryland, respectively, compared to February 2020. Baltimore County's and Maryland's unemployment rates have fallen to 2.1% and 2.0%, respectively, well below their pre-pandemic lows. Challenges remain as the now positive-trending labor force participation rate, still growing by less than 1.0% in both the County and Maryland, recovers from a three-year decline, reflecting a surge in retirements among older residents and a likely loss of some prime-age workers as well. Most recently, in December 2023, the County and State labor forces provided 23,440 and 187,194 fewer workers, respectively, than at the start of the COVID-19 pandemic. Employment growth is expected to remain subdued as the historically low unemployment rate and slim labor force participation gains continue to squeeze the labor market, which ultimately affects the hiring ability of County businesses. After County and State employment saw just 0.1% and 1.7% growth, respectively, in CY 2023, Sage Policy Group, Inc. projects that in CY 2024, County and State employment will expand by 1.5% and 1.2%, respectively – outperforming expectations for U.S. growth, which Sage expects will slow to less than 1% following greater than 2% growth in CY 2023.

Figure 6. Real Gross Domestic Product: Annual Percentage Change



Estimate Source: Federal Reserve Bank of Philadelphia's Survey of Professional Forecasters*, February 2024*

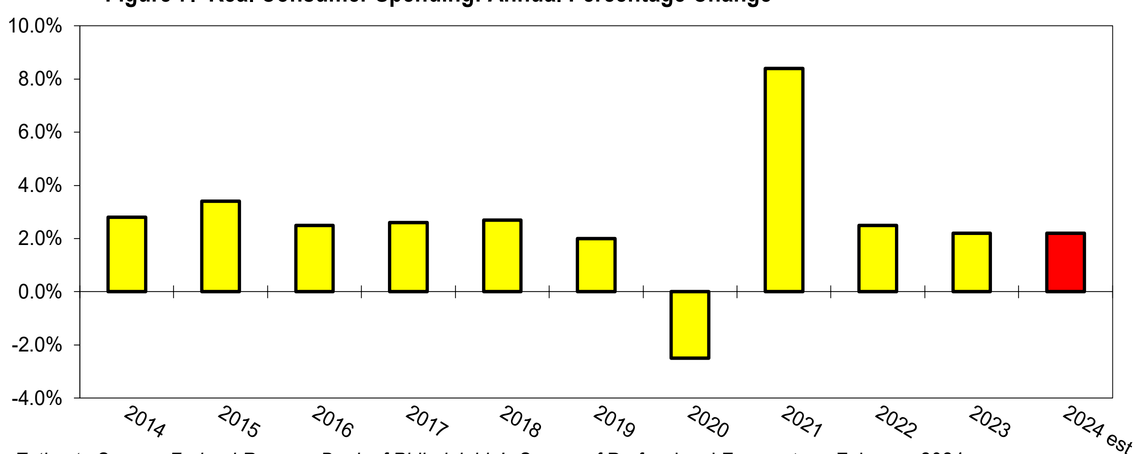
Consumer spending increased at a rate of 2.2% in CY 2023 following growth of 2.5% during CY 2022. Economists expect consumer spending to continue at a similar pace during CY 2024.

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). As noted, consumer spending increased at a rate of 2.2% in CY 2023, a modest deceleration from a 2.5% increase during CY 2022. Most recently, in 2023:Q4, consumer spending slowed from a 3.1% annualized increase during Q3 to a slightly lower 2.8%. Consumer spending is expected to maintain its CY 2023 pace in CY 2024. Further, contrary to expectation, consumer confidence is growing in the short term. A survey of 5,000 U.S. households by the Conference Board found that consumer confidence increased in January 2024, reaching its highest levels since December 2021 and marking its third consecutive monthly increase. Both the "Expectations Index" and the "Present Situation Index" saw increases. The Conference Board reported that the "increase in consumer confidence likely reflected slower inflation, anticipation of lower interest rates ahead, and generally favorable employment conditions as companies continue to hoard labor." Additionally, "[b]uying plans dipped in January, but consumers continued to rate their income and personal finances favorably currently and over the next six months." Further, "[a]verage 12-month inflation expectations fell to 5.2 percent, the lowest since March 2020 (4.5 percent)."

The U.S. economy remained resilient, posting solid growth during CY 2023, but faces several challenges on the horizon. The Committee's consultant anticipates a possible recession during the upcoming year that may be mild from a historical perspective but could nevertheless be noticeable in its local effects.

From a broader perspective, the U.S. economy has continued to beat expectations, maintaining steady growth since the pandemic-induced recession in early 2020. Inflation continues to trend downward, but it will take some time before the U.S. economy hits the Federal Reserve's 2% inflation target, in light of the Federal Reserve signaling that it is unlikely to cut interest rates in the short term. Nationally, job growth remains above expected levels, while unemployment cruises below 4%. Consumer spending similarly remains high and has driven much of the growth in the economy. However, consumers have largely exhausted their accumulated $2.1 trillion in savings accrued during the COVID-19 pandemic. Credit card debt has begun to rise, and banks report seeing more delinquencies on credit card accounts, auto loans, and mortgages. This situation may signal that the pace of consumer spending will slow by 2025, resulting in an adverse impact on the economy. The Federal Reserve Bank of Philadelphia's February 2024 *Survey of Professional Forecasters* projects 3.9% unemployment during CY 2024, up from 3.6% in CY 2023, but still low. The *Survey* further projects steady GDP growth during CY 2024 with somewhat lower growth expected in the following two years. While the economy has managed to avoid recession, bring down inflation, and post higher-than-expected job growth, it is still too soon to say that the U.S. has achieved a "soft landing." In this regard, the Committee's consultant stated, as of January 15, 2024, that it continues to anticipate a possible 2024 recession due to lag effects on the economy from prior interest rate increases. With that said, the forecast notes that a 2024 recession would be "quite mild" and that some economists have dropped recession from their forecasts altogether.

Figure 7. Real Consumer Spending: Annual Percentage Change



Estimate Source: Federal Reserve Bank of Philadelphia's Survey of Professional Forecasters, February 2024

GENERAL FUND REVENUES AND SURPLUS

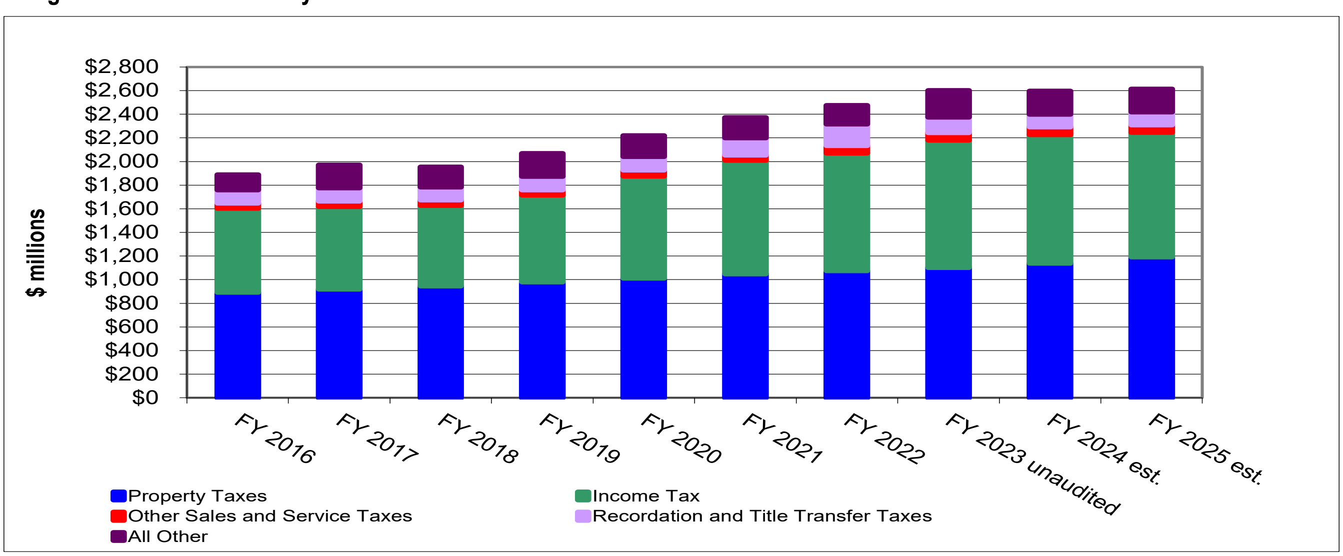
FY 2024 General Fund revenues are projected to decrease slightly, by $3.3 million, or 0.1%, from FY 2023 unaudited totals.

FY 2024 projected revenues total $2,597.2 million, exceeding FY 2024 budgeted revenues by $53.0 million, or 2.1%, and reflecting a decrease of $3.3 million, or 0.1%, from FY 2023 unaudited revenues (Figures 8 and 9). The decrease primarily results from the one-time nature of a $25 million fund balance transfer from Baltimore County Public Schools (BCPS) in FY 2023, as well as the moderation of two higher-than-usual income tax distributions received in FY 2023 that were at least partially unrelated to underlying wage or job growth (e.g., related to delinquent returns and delays in processing following the initial pandemic period). Absent these factors, FY 2024 revenues would show modest growth. Despite the previously mentioned moderation of two prior-tax-year distributions, income tax revenues are projected to total $1,086.7 million in FY 2024, an increase of $7.5 million, or 0.7% over FY 2023 collections. In addition, largely due to the continued effects of the recent interest rate hikes by the Federal Reserve to combat inflation, the housing market remains sluggish; as a result, property-related transaction tax revenues (from title transfer and recordation taxes) are expected to total only $107.2 million, a decrease of $23.1 million, or 17.7%, from FY 2023 collections, further constraining total FY 2024 revenue growth. Meanwhile, continued strong anticipated growth in property tax revenues of $37.5 million, or 3.4%, will serve to bolster the overall FY 2024 revenue position.

FY 2025 General Fund revenues are projected to increase by approximately $16.9 million, or 0.7%, over the current FY 2024 estimate.

FY 2025 General Fund revenues are projected to total $2,614.1 million, an increase of $16.9 million, or 0.7%, over the current FY 2024 revenue estimate, and up approximately $69.9 million, or 2.7%, from FY 2024 budgeted revenues. The FY 2025 projected increase is driven primarily by property tax revenues, which are expected to grow steadily for the eleventh consecutive year with the State's recent reassessment of the County's eastern region. Specifically, projected property tax revenues total $1,191.7 million, an increase of $52.2 million, or 4.6%. This increase in property tax revenues is partially offset by an anticipated decline in income tax revenue, due in part to the continued moderation of elevated non-recurring distributions (noted previously). In addition, consistent with conservative forecasting practices, a slowdown in withholdings growth is assumed, leading to projected income tax revenue totaling $1,054.8 million, a decrease of $31.9 million, or 2.9%. FY 2025 property-related transaction tax revenues are also conservatively expected to remain flat as falling mortgage interest rates slowly encourage prospective homebuyers and sellers to re-enter the market.

Figure 8. Baltimore County General Fund Revenues



Sources: FY 2016 to FY 2022 Baltimore County Annual Comprehensive Financial Reports; Baltimore County Office of the County Auditor

Figure 9. General Fund Revenue Forecast, FY 2023-FY 2025

($ in Millions)

REVENUE SOURCE	FY 2023 Unaudited	FY 2024 Budget	FY 23 - FY 24 Bud.	FY 2024 Revised	FY 23 - FY 24 Rev.	FY 2025 Estimate	FY 24 Bud.- FY 25	**FY 24 Rev.- FY 25**
Property taxes	$1,102.0	$1,187.0	7.7%	$1,139.5	3.4%	$1,191.7	0.4%	4.6%
Income taxes	1,079.2	1,009.1	-6.5%	1,086.7	0.7%	1,054.8	4.5%	-2.9%
Recordation & title transfer taxes	130.3	60.7	-53.4%	107.2	-17.7%	107.2	76.6%	0.0%
Other Sales and Service taxes	62.8	64.6	2.9%	65.5	4.3%	64.0	-0.9%	-2.3%
Intergovernmental aid	60.9	55.9	-8.2%	55.5	-8.9%	55.8	-0.2%	0.5%
Service charges	72.2	85.1	17.9%	72.2	0.0%	72.2	-15.2%	0.0%
Interest on investments	35.7	44.9	25.8%	38.2	7.0%	36.0	-19.8%	-5.8%
Fines, forfeitures & penalties	5.4	3.8	-29.6%	5.4	0.0%	5.4	42.1%	0.0%
Licenses & permits	5.1	4.5	-11.8%	5.1	0.0%	5.1	13.3%	0.0%
Other	46.9	28.6	-39.0%	21.9	-53.3%	21.9	-23.4%	0.0%
TOTAL	**$2,600.5**	**$2,544.2**	**-2.2%**	**$2,597.2**	**-0.1%**	**$2,614.1**	**2.7%**	**0.7%**

The FY 2025 revenue projection is $4.5 million above the Committee's recommended FY 2025 spending guideline.

Projected FY 2025 revenues exceed the Committee's recommended spending guideline by $4.5 million. The County's General Fund unassigned fund balance is expected to total $414.2 million as of June 30, 2023, not including $249.6 million in the Revenue Stabilization Reserve Account (RSRA). Together, these amounts represent $663.8 million, or 26.1% of FY 2024 budgeted General Fund revenues. These figures represent revenue totals taken from the County's financial system and are unaudited.

The FY 2023 surplus is expected to total $414.2 million, excluding $249.6 million in the RSRA.

The FY 2024 surplus is expected to total $296.6 million, excluding $254.4 million in the RSRA.

After appropriating a sizable $173.9 million in one-time General Fund Pay-As-You-Go (PAYGO) Contributions to the Capital Budget in FY 2024, the projected June 30, 2024 budgetary surplus, assuming revenues of $2,597.2 million, no supplemental appropriations, and no actions by the Administration to revert appropriations and/or liquidate other funds, totals $296.6 million, or 11.7% of FY 2024 budgeted revenues (Figure 10). This amount does not include an estimated $254.4 million, or 10.0% of FY 2024 budgeted revenues, in the RSRA. The FY 2024 adopted operating budget projected a FY 2024 budgetary surplus of $274.9 million, excluding a projected $254.4 million in the RSRA. The budgetary surplus will be available as a source of funding for the FY 2025 budget. The remaining amount, after assignment of funds to the FY 2025 budget, will become the unassigned year-end surplus.

Figure 10. Estimated General Fund Budgetary Surplus, FY 2024

		($ in Millions)
FY 2023 General Fund Budgetary Surplus (excluding RSRA funds)		**$ 414.2**
FY 2024 Revenue Estimate (per Adopted Budget)	2,544.2	
FY 2024 Revision	53.0	
FY 2024 Revised Revenue Estimate		2,597.2
FY 2024 Adopted Budget		(2,710.0)
FY 2024 Transfer to the RSRA		(4.8)
FY 2024 Estimated General Fund Budgetary Surplus		**$ 296.6**

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 residents, bond-rating agencies, and members of 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.

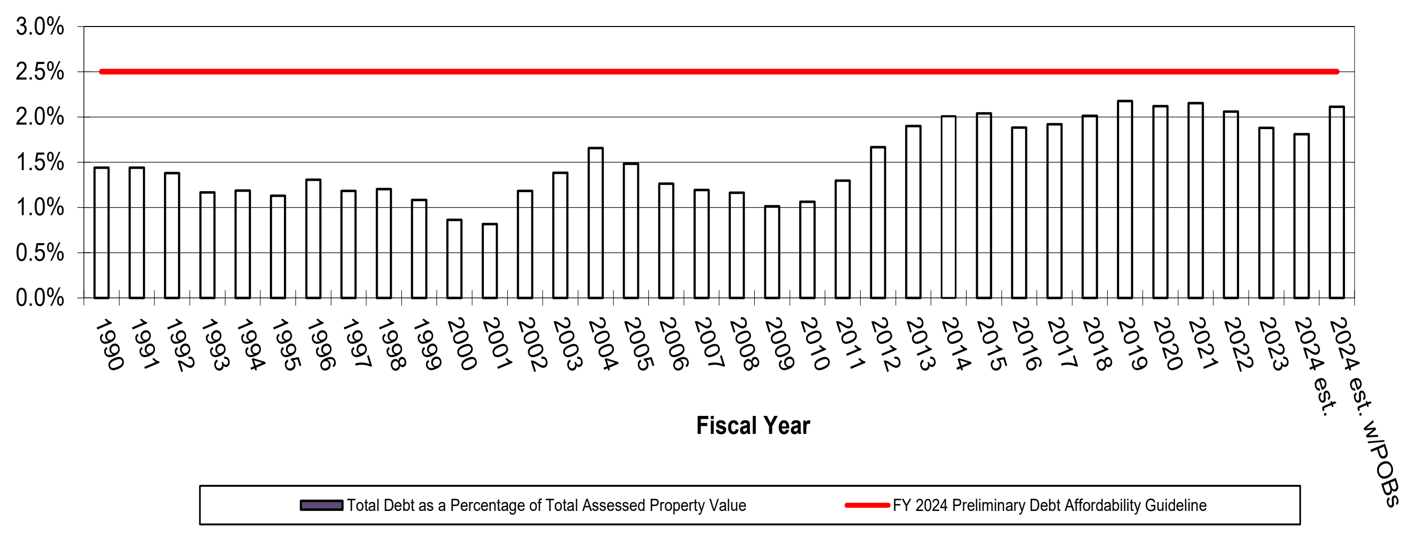
Based on the issuance of up to $140 million in new consolidated public improvement (CPI) debt during FY 2024 as authorized by Bill 93-23, the amounts of total debt outstanding and debt service expenditures are expected to continue to remain below both the Committee's and the Administration's guidelines through FY 2024.

Total Debt Outstanding Guideline

The Committee recommends that total debt outstanding not exceed $2,684,856,675, or 2.5% of total assessed property value of $107,394,267,000.

The ratio of total debt outstanding to total assessed property value is a measure of debt affordability. Total assessed property values have been steadily increasing primarily due to rising home values. At the same time, the County's level of total debt outstanding has been decreasing in recent years, from $2.0 billion in FY 2021 to an estimated $1.8 billion in FY 2024. For FY 2024, the total debt outstanding ratio is estimated at 1.8%, a decrease from 1.9% in FY 2023. The inclusion of pension obligation bond (POB) debt, which is being shown for informational purposes only, would increase the ratio to 2.1% (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 2025 not exceed $2,684,856,675, or 2.5% of total assessed property value of $107,394,267,000.**

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 2024, which is shown (for informational purposes) with and without POBs, which were issued in Fiscal Years 1988, 2013, and 2017. FY 2024 ratios are estimated.

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

Debt Service Guideline

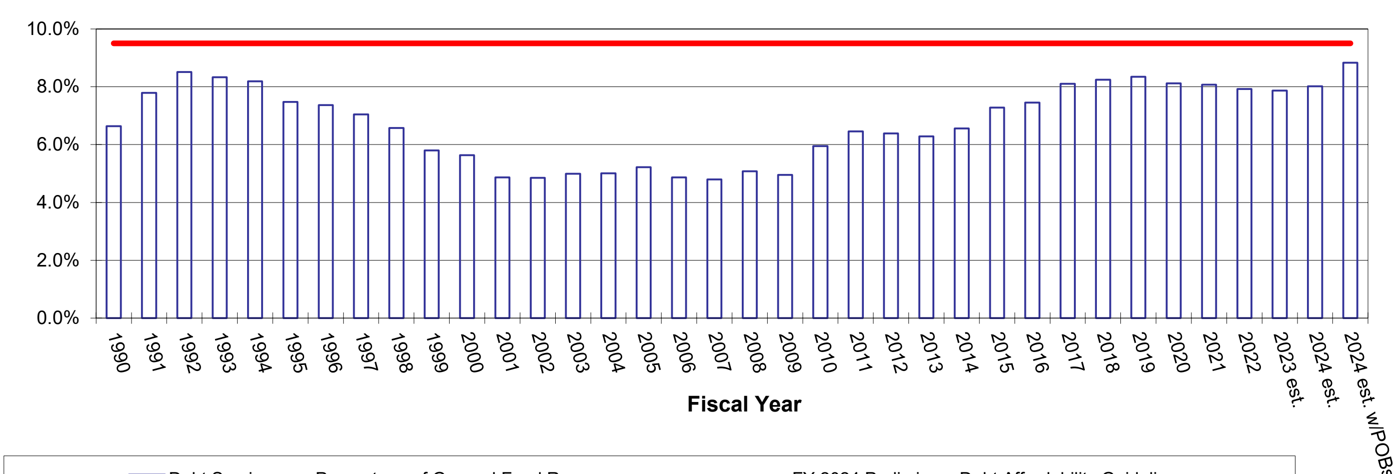
The Committee recommends that debt service not exceed $248.3 million, based on applying a 9.5% guideline to projected revenues totaling $2,614.1 million.

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. From FY 2013 until FY 2019, the ratio of the County debt service as a percentage of total General Fund revenues had been increasing steadily. The ratio then declined in fiscal years 2020 through 2023, largely as a result of increased income tax collections. For FY 2024, this ratio is estimated to increase slightly to 8.0%, as budgeted debt service increases while FY 2024 revenues are expected to remain nearly flat. The inclusion of Pension Obligation Bond (POB) debt, which is being shown for informational purposes only, would increase the ratio to 8.8% (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 2025 not exceed $248.3 million, based on projected revenues totaling $2,614.1 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. In recent years, the Committee has discouraged this practice, recommending that the County develop a plan to discontinue it, and in 2023, the Office of Budget and Finance agreed to phase-out the practice.

The ratio of debt service to total General Fund revenues from FY 1990 to FY 2024 (as estimated) 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, prior to fiscal year 2020, the ratio had been rising steadily, largely a result of the aggressive capital program for school projects. 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 has been managed off-budget. In spring 2023, the Office of Budget and Finance announced its plans to phase-out this practice beginning in FY 2024; projected interest costs that will not be reflected in the FY 2025 General Fund budget total $4.0 million.

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 2024, which is shown (for informational purposes) with and without POBs, which were issued in Fiscal Years 1988, 2013, and 2017. FY 2023 and FY 2024 ratios are estimated.
Sources: Baltimore County budget documents; Baltimore County Annual Comprehensive Financial Reports; Baltimore County Office of Budget and Finance; Baltimore County Office of the County Auditor.