SPENDING AFFORDABILITY COMMITTEE
Anne Arundel County
January 31, 2022

The Hon. Steuart Pittman, County Executive
The Hon. Lisa Rodvien, Chair, County Council
Mr. Matt Power, Chief Administrative Officer
Mr. Chris Trumbauer, Budget Officer
Ms. Karin McQuade, Controller
The Arundel Center, 44 Calvert Street
Annapolis, Maryland 21401

This report of the Spending Affordability Committee (SAC) for Fiscal 2023 is hereby submitted in accordance with Section 610 of the Anne Arundel County Charter. This section requires in part that "The Committee shall make advisory recommendations to the Office of the Budget, the County Executive, and the County Council relating to spending affordability including County spending levels to reflect the ability of the taxpayer to finance County services and long-term debt." Section 610 also tells the Spending Affordability Committee to "…examine current capital projects, the five-year capital improvement program, per capita wealth, debt service, pay-as-you-go funding and alternative sources of funding."

Committee Recommendation

The SAC has followed the practice of previous Committees that "spending affordability" can best be determined by estimating the growth in personal income of County residents. The Committee analyzes personal income growth on both a year-over-year and long-term basis. The Committee uses the definition of personal income provided by the U.S. Department of Commerce, Bureau of Economic Analysis (BEA), which is "income received by persons from all sources" (e.g., wages, employment benefits, business income, and investment income) whether taxable or not. To avoid placing additional financial burden on County residents, spending growth should remain in-line with personal income growth. Simply put, if County spending were to increase faster than personal income, additional taxes and fees from County residents would likely be needed at some point to support that spending.

Using personal income as a benchmark to guide our analysis, the SAC recommends a Fiscal 2023 spending increase of 3.5% vs. the Fiscal 2022 adjusted base budget. As shown in the table below, this results in a recommended Fiscal 2023 Current Expense (General Fund) budget of $1,809,032,099. This represents a $94.9 million increase (5.5%) over the SAC's Fiscal 2022 recommendation. The Fiscal 2022 recommendation was conservative and reflected the significant uncertainty regarding the financial impacts of coronavirus disease 2019 (COVID-19) on the County. Our Fiscal 2023 recommendation is based in part on better-than-expected County revenues and personal income projections for Fiscal 2021 and 2022.

With respect to the Capital Budget, County budget policy stipulates that the General Fund Debt Limit be less than 4% of forecasted personal income.[1] Applying the Committee's 3.5% budget growth recommendation to the average of current personal income estimates for Fiscal 2022 results in a forecasted Fiscal 2023 County personal income of $45,460,241,849. Applying the 4% limit to this personal income forecast results in a recommended General Fund Debt Limit of $1,818,409,674. This represents a $95.9 million increase over the SAC's Fiscal 2022 recommendation.

Anne Arundel County Spending Affordability Committee Recommendations For Fiscal Year 2023	
Current Expense Budget Recommendation	
(Adjusted Base Budget for Current Year x Estimated Personal Income Growth Rate for Budget Year)	
Approved Fiscal 2022 Budget	$1,873,082,300
- Appropriated Fund Balance	(114,225,200)
- Rainy Day Fund Contribution	(11,000,000)
Committee's Adjusted Base Budget - Fiscal 2022	$1,747,857,100
Estimated Increase in County Personal Income (Fiscal 2022 to Fiscal 2023)	3.5%
FY2023 General Fund Appropriation Limit (customary manner)	**$1,809,032,099**
Capital Budget Recommendation	
(Personal Income Forecast for Current Year x Estimated Personal Income Growth Rate for Budget Year x Standard)	
Average of Regional Economic Studies Institute (RESI) of Towson University and Moody's Analytics Forecasts for County Personal Income - Fiscal 2022	$43,922,938,985
Estimated Increase in County Personal Income (Fiscal 2022 to Fiscal 2023)	3.5%
Forecast Personal Income - Fiscal 2023	$45,460,241,849
Standard Applied in County's Debt Affordability Model	4.0%
Fiscal 2023 General Fund Debt Limit (customary manner)	**$1,818,409,674**

Background

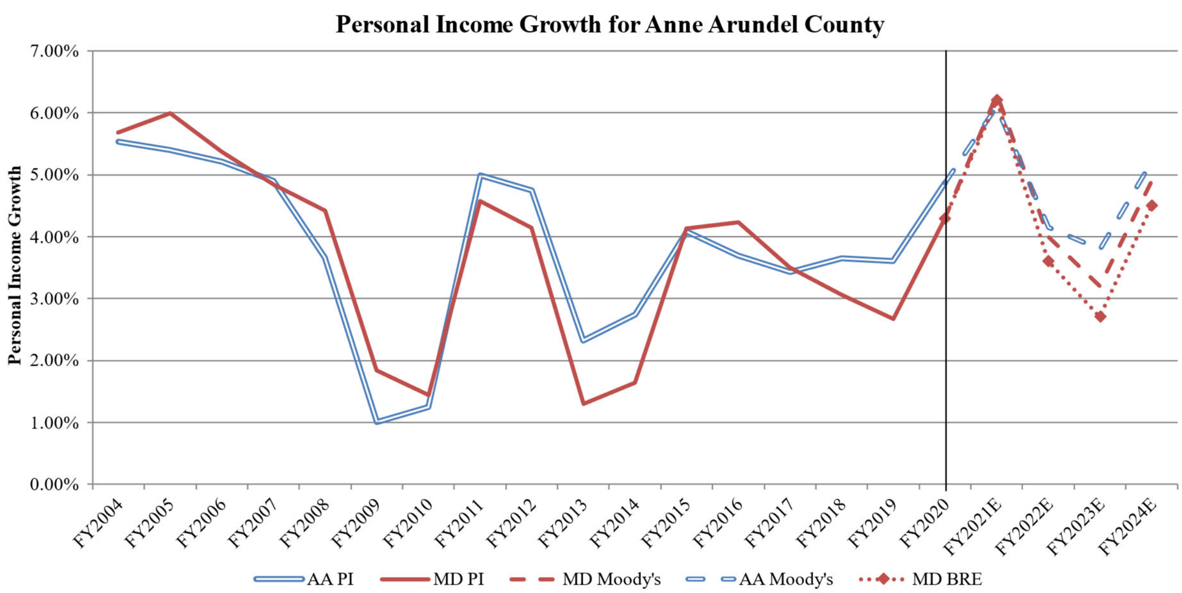
The State of Maryland contracts with four firms (Sage Policy Group, Moody's, IHS Markit-Global Insight, and the Regional Economic Studies Institute [RESI] of Towson University) to provide economic data and personal income forecasts. In addition, the State Board of Revenue Estimates (BRE) makes its own forecast for Maryland. To supplement this data, the County Budget Office obtained Anne Arundel-specific data and Fiscal 2023 forecasts from RESI and Moody's. This is a change from previous years, in which the County only contracted with RESI for Anne Arundel-specific forecasts. The SAC requested this change to provide additional data to inform our recommendations.

The RESI and Moody's estimates are informed by personal income data from the BEA, employment data from the Bureau of Labor Statistics, and population data from the U.S. Census Bureau. The following table summarizes the most recent personal income growth estimates for Maryland and Anne Arundel County. On average, these estimates project a 2.7% personal income growth rate for Maryland and a 2.8% growth rate for Anne Arundel County for Fiscal 2023. As shown in the table, the RESI estimates are significantly lower than those provided by the other analysts.

[1] Page 21, Approved Current Expense Budget and Budget Message for Fiscal Year 2022.

Comparison of Personal Income Forecasts Fiscal Year 2021 – 2024 (date of estimate)					
		2021	2022	2023	2024
State of Maryland	Board of Revenue Estimates (Dec 2021)	6.2%	3.6%	2.7%	4.5%
	Sage Policy Group (Nov 2021)	6.3%	3.8%	2.8%	4.3%
	Moody's (Nov 2021)	6.3%	4.0%	3.2%	4.9%
	IHS-Global Insight (Nov 2021)	6.2%	3.7%	3.0%	4.8%
	RESI of Towson University (Dec 2021)	1.8%	1.8%	1.8%	3.6%
	Average	**5.3%**	**3.4%**	**2.7%**	**4.4%**
Anne Arundel County	Moody's (Dec 2021)	6.1%	4.2%	3.8%	5.2%
	RESI of Towson University (Dec 2021)	1.8%	1.8%	1.8%	3.6%
	Average	**4.0%**	**3.0%**	**2.8%**	**4.4%**

The following graph shows the actual annual growth rates in personal income from Fiscal 2004 to Fiscal 2020 for Maryland and Anne Arundel County as reported by the BEA, along with the Moody's and BRE forecasts for Fiscal 2021 and beyond. If viewing in black and white, the lower (blue double) line in 2005 is Anne Arundel County and the higher (red solid) line in 2005 is Maryland. In 2023, the higher (blue double) dashed line is Anne Arundel County. For the most recent year where data is available (Fiscal 2020), the BEA currently reports that the personal income growth rate in Anne Arundel County was 4.86%. Note that this data is subject to potential updates by the BEA in future reports. The chart below shows the most recent updates for all years, and supersedes any data presented in previous Committee reports.



Summary of SAC Analysis and Discussions

The SAC members applied our collective experience and background in business, economics, finance, and Federal/State/Local government to assess the forecasts provided by the State's four econometric modeling firms. Because full year personal income reporting is only available from the BEA through Fiscal 2020, projections for Fiscal 2023 are based on 2 years of estimated data. These estimates are continuously revised as new data becomes available. In some cases, the actual reported data is also revised. These revisions are typically downward, meaning that County economic growth was slower than originally forecast.

Further complicating this analysis for Fiscal 2023 are the widely varying estimates provided by RESI and Moody's. In their presentation to the SAC on 8 December 2021, RESI presented a very conservative outlook for economic growth in both the County and the State. Their Fiscal 2023 personal income estimate for Anne Arundel is approximately $44.3 billion. In contrast, Moody's growth estimates are more in line with those of other analysts, and their Fiscal 2023 personal income estimate for Anne Arundel is approximately $46.1 billion. There are similar differences in the estimates for Fiscal 2021 and Fiscal 2022. For the purposes of this report, the Committee's recommendation on debt affordability uses the average of the RESI and Moody's Fiscal 2022 estimates.

As noted above, the SAC recommends a 3.5% growth in the Fiscal 2023 budget vs. Fiscal 2022. In our deliberations, individual SAC members advocated for growth rates ranging from 2.0% to 3.8%. Members advocating for a lower recommendation primarily expressed concern over the tax burden on lower-income County residents who have been disproportionately affected by COVID-19. Members advocating for a mid-range recommendation expressed concern that long-term spending has significantly outpaced County economic growth in recent years, along with concern that spending increases based on near-term revenue windfalls may be detrimental in future years. Members advocating for higher growth rates cited the Moody's analysis and current job market (e.g., large numbers of unfilled positions, with employers offering significant wage increases to attract employees). All these arguments have merit. Ultimately, the Committee voted to adopt a 3.5% recommendation. The following paragraphs provide additional details regarding each of the positions outlined above.

Concerns Regarding the Ongoing Economic Impacts of COVID-19

At the macro level, Anne Arundel County remains largely insulated from the economic impacts of COVID-19 due to our large number of Federally funded jobs, in particular at Ft. Meade. However, the ongoing economic impact of COVID-19 coupled with rising inflation at the national level disproportionately affects lower income County residents. There are some signs of recovery, with approximately 22,000 jobs added in the County in calendar year 2021 vs. 2020. However, the total number of non-farm jobs in the County (approximately 258,000, excluding Ft. Meade) remains below pre-pandemic levels (approximately 269,000 in 2019). Further, Maryland unemployment (5.7%) is slightly higher than the collective Mid-Atlantic Region unemployment rate (5.5%), and well above the pre-pandemic level of 3.4%. Most jobs added in 2021 were in lower paying industries (such as hospitality, eating and drinking establishments, retail, and personal services). There were virtually no net jobs added in 2021 in higher paying industries such as technical and professional services. Essentially, County residents re-entering the workforce are doing so in low paying jobs. At the same time, these residents are seeing an increased cost of living due to inflation. Compounding this issue is the fact the Federal Pandemic Unemployment Compensation program ended in September 2021. As such, the Committee is concerned that large increases in spending may drive the need for increased taxes and fees in future years, which would disproportionately impact County residents who are still recovering from the economic impact of COVID-19.

Concerns Regarding Long Term County Spending Trends

Since Fiscal 2002, the Committee has used personal income as the metric by which to assess spending affordability. Using this standard, the Committee is concerned that County spending is significantly outpacing personal income growth. In other words, spending is growing faster than the County economy (using personal income as a proxy). Specifically, over the past 10 years, Budget Office analysis shows that the compound annual growth rate (CAGR) of County spending is 4.25%. Over the same period, personal income grew at a CAGR of 3.65%. In the past 5 years, the CAGR of County spending is even higher at 4.54%. Moreover, analysis shows that spending growth outpaced personal income growth on a year-over-year basis in 6 of the last 8 years for which actual data is available (see Attachment A). The Committee first noted our concern over long-term spending growth in our Fiscal 2022 report.

Our concern is not a matter of whether expected County revenues support proposed spending. Based on data presented to the Committee by the Budget Office, we are confident that County Revenues for Fiscal 2023 will be strong, with an estimated growth of $108 million or 6% vs. the Fiscal 2022 approved budget. However, this increase is largely due to recent changes in Federal tax policy concerning pass through entities, which had the effect of accelerating State and County tax filings and payments. Further, as the Committee noted in our report for Fiscal 2022, we believe recent revenue increases are due at least in part to Federal stimulus in response to COVID-19. The County is also benefitting from the current real estate market, with steady growth in property tax revenue and better than usual recordation and transfer taxes. Finally, there is a significant fund balance based on better-than-expected revenues in Fiscal 2021 and 2022.

That said, Committee members expressed concern that the revenue increases noted above may be transitory, and the County Council may enact “permanent” spending programs based on projected revenues and available fund balance. This in turn may lead to structural deficits in future years. In the event of a future revenue downturn, this could force the Council to either decrease County services, enact tax increases beyond the changes introduced in Fiscal 2020, or freeze future spending growth. The burden of any of these outcomes would fall on County residents.

The Committee encourages the County Council to take a strategic, long-term view regarding the County economy and budget. Personal income data from BEA makes it clear that County economic growth is slowing. In past years, it was safe to assume an average Anne Arundel personal income growth of approximately 4% each year. However, in six of the last eight years for which actual data is available (2013 – 2020), personal income growth was less than 4% (see Attachment A). There are many factors driving slower growth, among them an aging County population, a decline in overall population growth year-over-year, and flat growth when it comes to higher paying jobs. As such, the Committee believes future personal income growth for the County will be closer to 3.5% per year.

Near Term Outlook

While long-term County growth appears to be slowing, there is reason to believe that near-term growth will be strong and the 3.8% growth projection by Moody’s is accurate. As noted above, the number of jobs in the County has still not returned to pre-pandemic levels. Further, the labor force participation rate for calendar year 2021 was 65.43%, vs. a pre-pandemic level of 69.16%. It is well documented in the media that businesses across the board have large numbers of job openings and are offering substantial salaries (as compared to pre-pandemic levels) to attract employees. Therefore, as COVID-19 restrictions are lifted it is reasonable to expect that County residents will continue to re-enter the workforce and that average wages will increase, positively impacting personal income and tax revenue.

Conclusion

Based on the analysis presented above, the SAC recommends an increase of 3.5% in the Fiscal 2023 General Fund budget as compared to Fiscal 2022. This recommendation is less than the personal income growth rate currently forecasted by Moody's for Anne Arundel County (3.8%), but greater than the forecast provided by RESI (1.8%). The Committee believes the Moody's estimate is more accurate. However, there remains significant uncertainty over the impacts of COVID-19 which makes it difficult to draw any long-term conclusions. Moreover, the Committee is concerned over County spending growth in recent years. This, coupled with analysis that shows County economic growth is steadily slowing, suggests a budget increase that is less than Moody's personal income growth prediction. As we have noted in previous reports, the Committee encourages a more conservative approach, allowing budget and policy flexibility in future years.

The Committee once again extends its heartfelt appreciation to our County employees, especially to Budget Administrator Hujia Hasim and Budget and Management Analyst Hannah Dier. The quality of governmental services that they provide is second to none. We sincerely hope that the evidence assembled for this report will help manage expectations and inform fair and just analysis of the difficult choices facing our elected leaders.

Sincerely,

David G. James, Chair

Spending Affordability Committee Membership for Calendar 2021 to 2022:

District	Name	Resolution #	Appointed on	Term Expires
1	Nicole Butler	34-19	9/16/2019	12/1/2022
2	Ejaz Younas, Vice Chair	19-17	5/1/2017	12/1/2020
3	Deborah Ritchie	34-19	9/16/2019	12/1/2021
4	Open			
5	Mary Clapsaddle, Secretary	34-19	9/16/2019	12/1/2022
6	David Juppe	34-19	9/16/2019	12/1/2022
7	David James, Chair	45-17	10/16/2017	12/1/2021

Attachment A
Approved Budgets vs. Reported Personal Income Growth

Fiscal Year	Spending Affordability Committee Budget Growth Recommendation	General Fund Approved Budget ($ millions)	Year-Over-Year Budget Growth	Actual Personal Income ($ thousands)*	Year-Over-Year Personal Income Growth
2008	5.50%	1,160.3		27,483,266	
2009	5.00%	1,173.6	1.15%	27,758,138	1.00%
2010	0.00%	1,180.8	0.61%	28,103,186	1.24%
2011	1.50%	1,169.4	-0.97%	29,504,352	4.99%
2012	4.40%	1,155.6	-1.18%	30,903,248	4.74%
2013	3.50%	1,218.9	5.48%	31,622,453	2.33%
2014	4.50%	1,238.3	1.59%	32,490,391	2.74%
2015	4.75%	1,309.7	5.77%	33,816,515	4.08%
2016	4.50%	1,346.5	2.81%	35,065,139	3.69%
2017	3.00%	1,406.7	4.47%	36,268,040	3.43%
2018	3.50%	1,460.8	3.85%	37,593,304	3.65%
2019	3.75%	1,524.9	4.39%	38,950,416	3.61%
2020	3.75%	1,637.6	7.39%	40,844,871	4.86%
2021	3.70%**	1,680.5	2.62%	TBD***	
2022	2.00%	1,747.9	4.01%	TBD	

*Based on data available from the BEA (https://apps.bea.gov/iTable/index_regional.cfm) as of January 2022. This data is subject to change in future BEA reporting. Also, it should be noted that the BEA reports county and metropolitan area personal income on a Calendar Year basis. Quarterly data is only available at the state level. For analysis purposes, the Budget Office converted this data to a County Fiscal Year basis by averaging the Calendar Year data. For example, the personal income shown above for Fiscal 2020 is the average of the BEA reported data for Calendar 2019 and 2020.

**The Fiscal 2021 recommendation was made in January 2020, prior to onset of the COVID-19 pandemic.

***Data for Calendar 2021 and 2022 is not yet available from BEA as of the date of this report.