Marc Elrich
County Executive

Michael J. Coveyou
Director

DEPARTMENT OF FINANCE

MEMORANDUM

May 15, 2022

TO: Marc Elrich, County Executive

FROM: Michael Coveyou, Director
Department of Finance

SUBJECT: Revenue Estimating Group Report for May 15, 2022

As chairperson of the Revenue Estimating Group, I am pleased to transmit to you the Group's May report. The Revenue Estimating Group was established in March 2021 per Bill 6-21 and requires the Group to provide quarterly reports to the County Executive and County Council each year on February 15, May 15, September 15 and December 15. This May 15th report includes an overview of the revenue forecast included in the Fiscal Year 2023 Recommended Budget ("FY23 Rec") and a review of economic conditions and potential risk factors.

We expect that each quarterly report will have a different focus depending upon the information available and the timing of the report within the budgetary cycle and the fiscal year. The next report will be due in September and will be the first report following the approval of the FY23 budget. The September report is expected to discuss the prelimary operating results for FY22 and provide updated economic information for the period subsequent to the FY23 Recommended Budget. We welcome your feedback on the contents and format of this report and future reports. Please feel free to contact me with any questions that you may have at 240-777-8870.

MC/nbf
Enclosure

cc: Members of the Revenue Estimating Group (Addendum I attached)

ADDENDUM I

Members of the Revenue Estimating Group

Michael J. Coveyou, Director, Department of Finance
Richard Madaleno, Chief Adminstrative Officer, Office of the County Executive
Jennifer R. Bryant, Director, Office of Management and Budget
Marlene Michaelson, Executive Director, Office of the County Council
Chris Cihlar, Director of the Office of Legislative Oversight

Designees and Technical Committee members:
Nancy B. Feldman, Chief, Division of Fiscal Management (Dept. of Finance)
Dennis Hetman, Fiscal Manager, Division of Fiscal Management
David Platt, Chief Economist, Division of Fiscal Management
Jake Weissman**,** Assistant Chief Administrative Officer, Office of the County Executive
Josh Watters, Acting Deputy Director, Office of Management and Budget
Chris Mullin, Budget Manager, Office of Management and Budget
Mary Beck, Capital Budget Manager, Office of Management and Budget
Gene Smith, Legislative Analyst, County Council Staff
Aron Trombka, Senior Legislative Analyst, Office of Legislative Oversight
Stephen Roblin, Performance Management and Data Analyst, Office of Legislative Oversight
Todd Fawley-King, Fiscal Policy Analyst, Division of Fiscal Management

Marc Elrich
County Executive

Michael J. Coveyou
Director

DEPARTMENT OF FINANCE

M E M O R A N D U M

May 15, 2022

TO: County Council

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Department of Finance

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Montgomery County Maryland Revenue Estimating Group

Quarterly Report, May 15, 2022

FY23 Recommended Budget Tax Revenue Forecast

The economic recovery from the pandemic has accelerated beyond initial expectations with broad based strength in wage and salary income, business income, capital gains,[1] and housing values, leading to higher expected tax revenue growth in Montgomery County. The FY23 recommended budget revenue forecast series ("FY23 Rec") anticipates continuation of the strong growth in income taxes and real estate-based taxes, building on the strength experienced in FY22. This forecast reflects the facts and economic assumptions at the time revenue estimates were developed in February 2022 and published in the February REG Report.[2] Despite projecting continued growth, the FY23 Rec's estimated growth rate from FY22 to FY23 of Montgomery County's income tax revenue (a key driver of overall revenue growth) is less than the State of Maryland's income tax rate of growth projected by the Bureau of Revenue Estimates (BRE),[3] while simultaneously accounting for the County's unique strengths.

- The FY23 Rec tax revenue estimate for FY23 of $4.306 billion is expected to exceed the FY22 Approved Budget forecast for FY23 by approximately 4.3% ($177 million). Tax revenues are forecast to grow at a healthy pace in the FY23 Rec, increasing 3.1% from FY22 to FY23 and growing annually by rates ranging between 3.1% and 4.1% from FY24 to FY28 (see Chart 2 and Table 1). The year-over-year rate of growth in the FY23 Rec is similar to the FY22 approved year-over-year rate of growth (see chart 2), but starts from a higher base due to improved economic conditions as compared to expected.

- The March 2022 estimates of FY22 tax revenues are higher than expected in the FY22 Approved Budget, bolstering expectations of elevated future growth; the FY23 Rec and the 6-year fiscal plan forecast increase tax revenues in FY23 by 4.3% over the FY22 Approved Budget forecast and are between 3.0% to 4.8% annually from FY24 to FY28 (see Chart 1, and Table 1).

- The FY23 Rec forecasts strong revenue growth as compared to actual growth rates experienced in recent years, consistent with growth rates that have been attained historically; the FY23 Rec growth rates and tax revenue are forecast at a reasonably expected level.

- The strength in the FY23 Rec tax revenues is partly driven by income tax estimates exceeding prior expectations in FY22 resulting in a higher income tax base to start the fiscal year. Additionally, income tax growth is a result of broad-based wage and salary income growth particularly for high earning occupations including science and technology, finance, health care, engineering, and government positions.[4] While the data on this growth in wages for high

[1] Maryland Revenue Estimates Revenues & Economics March 2022 (marylandtaxes.gov) - Page 9
[2] REG Report February 15, 2022 – Page 4
[3] Maryland Revenue Estimates Revenues & Economics March 2022 (marylandtaxes.gov) - Page 2
[4] Maryland Revenue Estimates Revenues & Economics September 2021 (marylandtaxes.gov) – Page 12

earning occupations is for the entirety of Maryland, Montgomery County comprises a notable portion of the state's employment within these industries.

- Transfer and Recordation taxes were strong over the past two years as historic strength in housing occurred in the County and nationally and is forecast to continue into FY23. The FY23 Rec transfer tax estimates for FY23 exceed the FY22 Approved Budget forecast by approximately 26% ($32 million) while estimates for the recordation tax for the same period exceed the FY22 Approved Budget by approximately 34% ($19 million). The transfer and recordation tax forecast has broad underlying support as low housing supply and historically low interest rates (despite recent increases) contribute to price stability.

- The evidence indicates that the County's economy has rebounded strongly from the depths of the pandemic: Montgomery County gained 41,221 jobs between April of 2020 and September of 2021 (the latest date of Bureau of Labor Statistics Quarterly Census of Employment and Wages data for the County).[5] This reflects a gain of 72.5% of the jobs lost between April and May of 2020. The unemployment rate has continually decreased from a May 2020 pandemic high of 8.6% to its March 2022 rate of 3.9% but has still not yet reached the pre-pandemic December 2019 low of 2.4%.[6]

- For additional details on the FY23 Rec tax revenues and the growth of specific revenue sources, see Chart 1, Chart 2, and Table 1 below.

Economic Conditions & Risks

The State of Maryland believes that while economic and tax revenue growth are currently elevated due to the continued flow-through of federal stimulus efforts, the pace of growth will eventually decline to rates more consistent with historic trends. The County's economic assumptions align with the State of Maryland's regarding the eventual decline of growth rates. The exact timing of this shift from elevated growth to a slower pace is uncertain and depends on numerous complex and unpredictable factors.

- The post-pandemic growth trend for Montgomery County revenues is expected to be marginally higher than the pre-pandemic trend due to the Federal Reserve's elevated inflation target and due to millennials, the largest cohort in the labor force, becoming more productive as they gain experience. This expectation is reflected in the growth of the projected revenues in the FY23 Rec out-years.

- Assuming the Federal Reserve achieves its inflation target of 2%, inflation will be higher than it was after the Great Recession when the Fed routinely undershot its inflation target. As revenue is collected in nominal dollars this inflation may result in higher collections and a higher growth trend.

- The economy should settle into this longer run trend once the pandemic is no longer a significant disruption to the economy. The end of significant pandemic disruptions should allow

[5] BLS QCEW Data Series ID ENU2403110010, All covered Montgomery County employees in all industries. https://www.bls.gov/data/#employment

[6] St. Louis Federal Reserve Economic Data. https://fred.stlouisfed.org/series/MDMONT0URN

for an expansion of supply of goods and services and reduced inflationary pressures, which could lead to another short-run increase in growth before the pace of economic expansion settles to a slower pace consistent with historic trends.

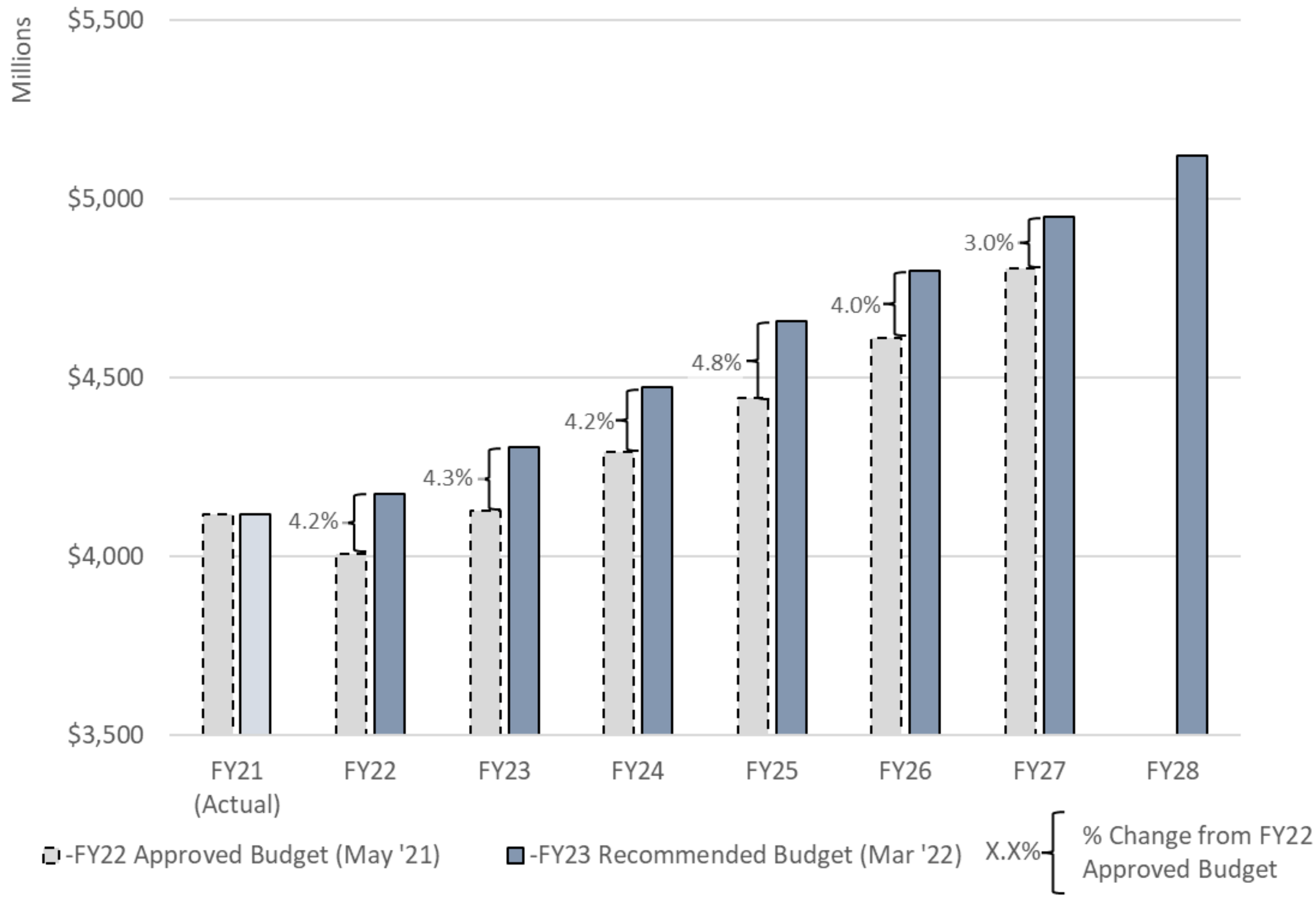
Nonetheless, as noted in prior Revenue Estimating Group reports, there are ongoing risks, both positive and negative, to revenue forecasts that the Department of Finance is monitoring.

- The risks include higher inflation, geopolitical implications of the Russian invasion of Ukraine, more rapid and higher Fed rate increases, a real estate market returning to historical (and slower) growth rates more quickly than forecast, and the threat of new COVID-19 variant outbreaks that could result in drops in economic activity.
- Volatility in capital markets is a factor that influences income tax revenues due to the capital gains component. It is not possible to forecast the periodic swings in capital markets with any precision. As Montgomery County comprises a disproportionately large share of Maryland capital gains income, the County is always at risk for inevitable downturns.
- Despite notable risks noted above, the national, regional, and county economy is in a position of strength given low unemployment, strong wage and salary growth and the strength of household balance sheets.[7]

The Revenue Estimating Group
Section 20-84 was added to the Montgomery County Code in March 2021 pursuant to Bill 6-21. Section 20-84 established a Revenue Estimating Group (the "Group") to review and forecast County revenues and provide for the membership and duties of the Group. The Group must submit reports to the County Executive and the County Council on revenue projections and quarterly attainment of revenue on February 15, May 15, September 15, and December 15. This May 2022 Report is the fourth report from the Group. It covers the revenue estimates during the period ending March 31, 2022 that were used to develop the revenue forecast for the Fiscal Year 2023 recommended budget that the County Executive transmitted to Council on March 15.

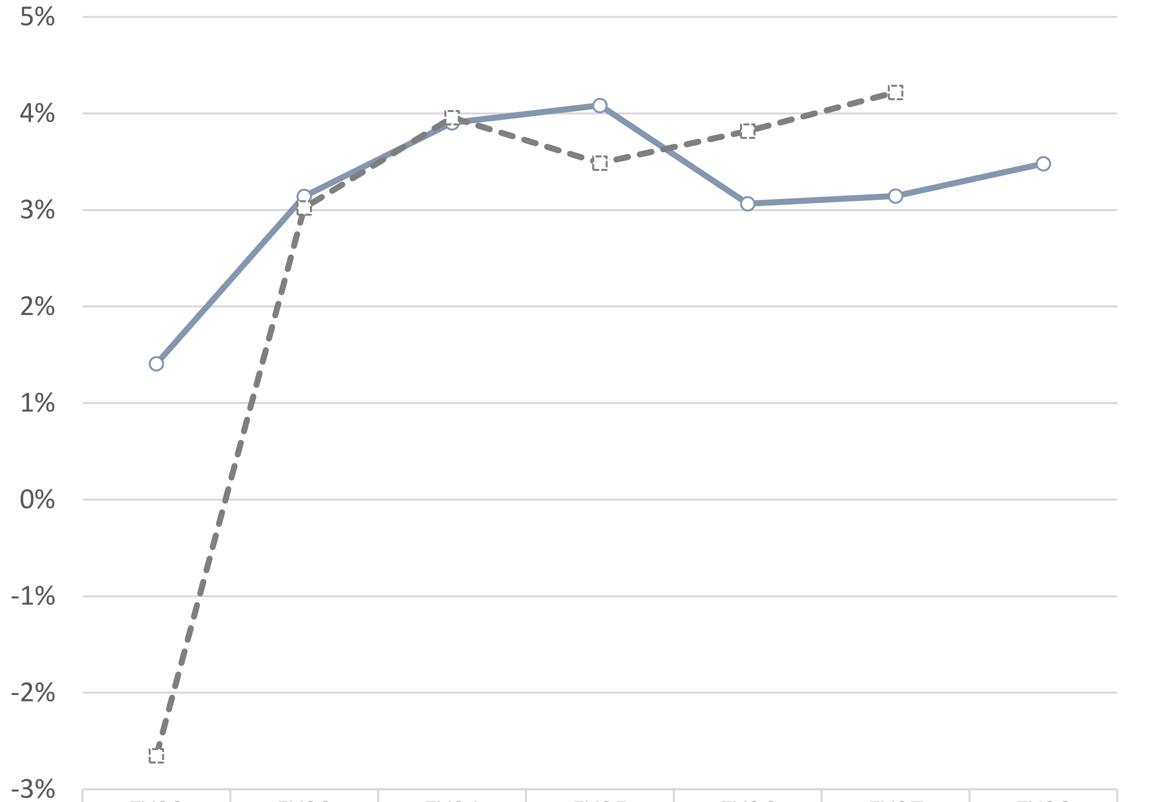
[7] https://www.federalreserve.gov/releases/z1/dataviz/z1/balance_sheet/chart

Chart 1: FY23 Recommended Budget Tax Revenue Forecast Compared to the FY22 Approved Budget[8]



[8] FY23 Rec estimate for FY22 is the latest estimated revenues for that fiscal year that is included in the FY23 Rec

Chart 2: FY23 Rec Year-over-Year Percent Change in Tax Revenues Compared to FY22 Approved[9]



	FY22	FY23	FY24	FY25	FY26	FY27	FY28
FY 23 Rec year-over-year percent change	1.4%	3.1%	3.9%	4.1%	3.1%	3.1%	3.5%
FY 22 Approved year-over-year percent change	-2.7%	3.0%	4.0%	3.5%	3.8%	4.2%	

[9] FY23 Rec estimate for FY22 is the latest estimated revenues for that fiscal year that is included in the FY23 Rec

Table 1: Detailed Tax Revenue Budget Comparison[10]

	FY21	FY22	FY23	FY24	FY25	FY26	FY27	FY28
INCOME TAX	**Actual**							
-FY22 Approved Budget (May '21)	$1,820.179	$1,708.842	$1,769.072	$1,865.212	$1,947.832	$2,049.082	$2,171.052	
-FY23 Recommended Budget (Mar '22)	$1,820.179	$1,794.219	$1,859.046	$1,954.670	$2,054.817	$2,138.883	$2,236.238	$2,344.945
Difference from FY22 Approved Budget		$85.377	$89.974	$89.459	$106.985	$89.802	$65.186	$71.613
FY23 Year-over-Year percent change		-1.4%	3.6%	5.1%	5.1%	4.1%	4.6%	4.9%
% difference from FY22 approved budget		5.0%	5.1%	4.8%	5.5%	4.4%	3.0%	
PROPERTY TAX								
-FY22 Approved Budget (May '21)	$1,857.596	$1,884.667	$1,931.036	$1,984.367	$2,040.451	$2,098.030	$2,157.800	
-FY23 Recommended Budget (Mar '22)	$1,857.596	$1,899.988	$1,951.354	$2,005.331	$2,071.999	$2,134.415	$2,195.587	$2,258.620
Difference from FY22 Approved Budget		$15.320	$20.318	$20.964	$31.548	$36.385	$37.787	$38.849
FY23 Year-over-Year percent change		2.3%	2.7%	2.8%	3.3%	3.0%	2.9%	2.9%
% difference from FY22 approved budget		0.8%	1.1%	1.1%	1.5%	1.7%	1.8%	
TRANSFER TAX								
-FY22 Approved Budget (May '21)	$132.289	$117.155	$122.825	$129.745	$136.545	$143.165	$149.905	
-FY23 Recommended Budget (Mar '22)	$132.289	$149.500	$154.750	$166.880	$176.150	$173.040	$167.780	$168.010
Difference from FY22 Approved Budget		$32.345	$31.925	$37.135	$39.605	$29.875	$17.875	$11.265
FY23 Year-over-Year percent change		13.0%	3.5%	7.8%	5.6%	-1.8%	-3.0%	0.1%
% difference from FY22 approved budget		27.6%	26.0%	28.6%	29.0%	20.9%	11.9%	
RECORDATION TAX (GENERAL FUND)								
-FY22 Approved Budget (May '21)	$60.573	$52.665	$55.216	$58.329	$61.391	$64.369	$67.401	
-FY23 Recommended Budget (Mar '22)	$60.573	$71.642	$74.158	$79.977	$84.421	$82.928	$80.406	$80.515
Difference from FY22 Approved Budget		$18.976	$18.942	$21.648	$23.030	$18.559	$13.005	$10.036
FY23 Year-over-Year percent change		18.3%	3.5%	7.8%	5.6%	-1.8%	-3.0%	0.1%
% difference from FY22 approved budget		36.0%	34.3%	37.1%	37.5%	28.8%	19.3%	

[10] All revenue numbers in $ millions.

Table 1: Detailed Tax Revenue Budget Comparison(continued)

	FY21	FY22	FY23	FY24	FY25	FY26	FY27	FY28
FUEL / ENERGY TAX	**Actual**							
-FY22 Approved Budget (May '21)	$184.420	$175.651	$178.533	$178.805	$179.020	$179.192	$179.332	
-FY23 Recommended Budget (Mar '22)	$184.420	$185.298	$186.480	$186.711	$186.947	$187.114	$187.254	$187.374
Difference from FY22 Approved Budget		$9.646	$7.947	$7.906	$7.928	$7.922	$7.923	$7.842
FY23 Year-over-Year percent change		0.5%	0.6%	0.1%	0.1%	0.1%	0.1%	0.1%
% difference from FY22 approved budget		5.5%	4.5%	4.4%	4.4%	4.4%	4.4%	
OTHER EXCISE TAXES								
-FY22 Approved Budget (May '21)	$61.797	$68.719	$72.110	$75.748	$76.668	$77.596	$80.545	
-FY23 Recommended Budget (Mar '22)	$61.797	$74.160	$80.142	$80.503	$82.456	$83.162	$83.246	$83.356
Difference from FY22 Approved Budget		$5.441	$8.032	$4.755	$5.788	$5.566	$2.701	$0.355
FY23 Year-over-Year percent change		6.1%	8.1%	0.5%	2.4%	0.9%	0.1%	0.1%
% difference from FY22 approved budget		7.9%	11.1%	6.3%	7.5%	7.2%	3.4%	

	FY21	FY22	FY23	FY24	FY25	FY26	FY27	FY28
TOTAL REVENUES INCLDUING ALL EXCISE TAXES	**Actual**							
-FY22 Approved Budget (May '21)	$4,116.854	$4,007.700	$4,128.792	$4,292.206	$4,441.906	$4,611.434	$4,806.034	
-FY23 Recommended Budget (Mar '22)	$4,116.854	$4,174.805	$4,305.929	$4,474.072	$4,656.790	$4,799.543	$4,950.512	$5,122.820
Difference from FY22 Approved Budget		$167.105	$177.137	$181.866	$214.884	$188.109	$144.477	$139.960
FY23 Year-over-Year percent change		1.4%	3.1%	3.9%	4.1%	3.1%	3.1%	3.5%
% difference from FY22 approved budget		4.2%	4.3%	4.2%	4.8%	4.1%	3.0%	
FY23 Rec. YoY % change from FY22 Approved		1.2%	7.4%	8.4%	8.5%	8.1%	7.4%	6.6%