Marc Elrich
County Executive

Michael J. Coveyou *Director*

DEPARTMENT OF FINANCE

M E M O R A N D U M

February 15, 2024

TO: Marc Elrich, County Executive

FROM: Michael Coveyou, Director
Department of Finance

SUBJECT: Revenue Estimating Group Report for February 15, 2024

As chairperson of the Revenue Estimating Group, I am pleased to transmit to you the Group's February 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 February 15th report focuses on fiscal 2024 year-to-date tax revenues through the end of December and the economic assumptions to be used for the fiscal year 2025 recommended budget.

The next report is due in May and will review the fiscal year 2025 recommended budget tax revenue forecast. 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 my 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
Todd Fawley-King, Fiscal Policy Analyst, Division of Fiscal Management
Josh Watters, 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
Craig Howard, Deputy Director, County Council Staff
Aron Trombka, Senior Legislative Analyst, Office of Legislative Oversight
Stephen Roblin, Performance Management and Data Analyst, Office of Legislative Oversight

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Michael J. Coveyou *Director*

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Montgomery County Maryland Revenue Estimating Group
Quarterly Report
February 15, 2024

Executive Summary

- Economic assumptions for Fiscal Year 2025 ("FY25") continue to assume a mild recession, consistent with the assumptions in the Fiscal Year 2024 ("FY24") approved budget and retained in the December Fiscal Plan presented to the County Council on December 12, 2023.
- In the December Fiscal Plan, the revised total tax revenues were forecast to exceed the approved budget by $208.7 million (+5.0%) primarily due to income and property taxes exceeding forecast. As of the end of December total tax revenues are on track to meet revised estimates.
- Economic assumptions for FY25 assume a mild recession begins during 2024. A review of economic assumptions from Moody's Analytics indicates that a mild recession in 2024 may decrease 2024 resident employment by 1.9%, while total personal income continues to grow at moderate pace of 2.6%. The forecast for resident employment in 2025 is effectively unchanged from 2024 assuming an increase of 0.1% but total personal income growth increases to 3.3%.
- Economic assumptions that affect real estate related taxes include the sales volume and median price of single-family homes. The assumption for the volume of single-family home sales in 2024 and 2025 has been revised to be weaker than had been previously assumed, with home sales estimated to decrease -14.9% in 2023 compared to -8.5% in December and then decrease an additional -15.1% in 2024. The Federal Reserve has indicated that they are not yet ready to cut the Federal Funds rate, therefore continued elevated interest rates are suppressing the supply of homes for sale. Low supply has kept the median price high through 2023 with a small decrease of -1.3% assumed in 2024.

Year to Date for the Period Ended December 31, 2023

Income tax receipts for the first half of FY24 were approximately 30% of the forecast in the December Fiscal Plan update.[1] At this half-way point in the fiscal year income tax receipts are consistent with fiscal years 2012- 2022 when income tax receipts for the same period averaged 31%.

[1] Income tax receipts are accounted for on a modified accrual basis on an August through July fiscal year. Income taxes collected through December 31 reflect 5 months from August through December. Other taxes shown in the table are on a cash basis on a July through June fiscal year.

Starting in FY22 the State Comptroller's office had difficulty processing all the complex income tax returns from pass-through-entities (i.e. S-Corps, partnerships) ("PTE's") in time to distribute the related income taxes to counties in November and January, as it had in the past. Following FY22 and FY23's income tax return processing and reconciliation delays of PTE filings, the Maryland Comptroller's office has indicated that their current tax return processing has exceeded prior years' rates and appears to be returning to a more normal processing pattern. The final 'additional payments' distribution in January 2024 represents the last of the tax year 2022 tax return payments.

As part of the County's normal end-of-January income tax distribution in 2024 (and not shown in the table below), the State Comptroller distributed $63.2 million to the County, of which $53.2 million was the tax year 2022 final reconciling income tax distribution. For full-year FY24 the December Fiscal plan income tax forecast included $235.7 million from tax year 2022 reconciliation revenue, which was a decrease of $15.2 million from tax year 2021. Reconciliation distributions are historically among the most volatile and difficult to anticipate. While the tax year 2022 reconciling distribution was lower than expected, total income tax collections through December were $152 million above the FY24 Approved Budget and other revenues, including property taxes, are expected to continue their strong collection patterns and result in tax revenues approaching the revised December tax revenue forecast.

TAXES	Year-to-Date (through December) (1)	FY24 Approved Budget	Fiscal Update December '23	YTD Share FY24 Approved	YTD Share Fiscal Update
Property Tax (includes MNCPPC)	$2,070,682,491	$2,107,033,865	$2,205,109,559	98.3%	93.9%
Income Tax	$604,125,803	$1,925,076,241	$2,069,456,972	31.4%	29.2%
Transfer Tax	$47,644,392	$118,050,247	$95,512,376	40.4%	49.9%
Recordation Tax (G.F.)	$23,252,174	$56,501,236	$45,253,282	41.2%	51.4%
Fuel and Energy Tax	$83,450,201	$193,151,409	$189,754,678	43.2%	44.0%
Telephone Tax	$27,661,894	$55,641,296	$55,870,507	49.7%	49.5%
Hotel/Motel Tax	$11,864,388	$22,067,616	$23,023,429	53.8%	51.5%
Admissions Tax	$1,109,894	$3,904,620	$4,691,862	28.4%	23.7%
E-Cigarette Tax	$376,375	$1,048,651	$815,820	35.9%	46.1%
TOTAL	$2,870,167,612	$4,482,475,181	$4,689,488,486	64.0%	61.2%

NOTE (1): data from MoCo accounting systems; provided by the Treasury Division, Department of Finance

Property taxes collected to date are near 94% of the December Fiscal Plan revised forecast since the final regular property tax due date passed on December 31, 2023. During the second half of the fiscal year ad valorem property taxes that may be received include delinquent payments, taxes for construction projects in process or recently completed and personal property taxes. The County has a long history of collecting over 99%[2] of its property taxes each year.

Transfer and recordation taxes

[2] See Montgomery County Annual Comprehensive Report, Fiscal Year Ended June 30, 2023, Statistical Table 13 https://www.montgomerycountymd.gov/Finance/Resources/Files/data/financial/acfr/FY2023_ACFR.pdf

At the end of December recordation and transfer tax collections were approximately 51% and 50%, respectively, of the reduced December Fiscal Plan estimates. Year-over-year transfer taxes are down 22% and volume is down 20% while recordation tax revenue is down 24% and volume is also down 24%. The current high federal funds rate, interest rates and mortgage rates have had a negative impact on these real estate-based taxes.

Other tax revenues collected through December 31 are on target considering expected seasonality and recovery from pandemic lows. Fuel energy tax and telephone tax collections were approximately 44% and 50%, respectively of the December Fiscal Plan estimates. Hotel/motel tax collections are approximately 54% of the approved budget and 52% of the December Fiscal Plan estimate. Hotel/motel tax is seasonal, typically with higher receipts after the winter season. In December the annual estimate was increased from $22.1 million to $23.0 million due to improved business travel, room rates and occupancy than assumed in the approved budget.

Economic Assumptions

2024-30 Economic Assumptions

The economic assumptions that will be applied to develop the FY25 budget revenue forecast are shown below. The economic assumptions that will be used to develop the FY25 recommended budget revenue forecast and FY26-FY30 revenue forecasts assume a mild recession beginning sometime in 2024. The FY24 approved budget assumed a mild recession would occur in 2023. While economic conditions were better than anticipated in 2023, the risk factors for a recession remain and our economic assumptions continue to assume a mild recession in 2024.

Resident Employment is a key component in forecasting income tax revenue. For 2024-30 resident employment is assumed to grow at a similar pace as was assumed in the December Fiscal Plan. Resident employment is expected to have positive growth rates in all years, except 2024, when a -2.4% decrease is assumed. The forecast for resident employment in 2025 is effectively unchanged from 2024. It assumes an increase of 0.1%, but then increases 1.2% in 2026, with subsequent years mostly below 1% per year. Average annual growth from 2025-2030 is 0.6%.

Total Personal Income is also a key component in forecasting income tax revenue. The assumption for total personal income growth remains positive in all years of the forecast, averaging 3.7% per year from 2024-2030. The growth rate in 2024 of 2.6% is the same as the December forecast, following a 2023 growth rate estimate of 3.4% which was stronger than the previous assumption of 3.1%.

Sales of existing single-family homes and median sales price of single-family homes are key components in forecasting property tax and transfer and recordation tax revenues. The assumption for the volume of single-family home sales in 2024 and 2025 has been revised to be weaker than previously assumed. Home sales are estimated to decrease 14.9% in 2023 compared to -8.5% in December and then decrease an additional 15.1% in 2024. Home sales begin to recover in 2025 by 2.2%. and 14.6% in 2026. Smaller increases from 2027-2030 average 4.6% per year. Despite the decreases in the volume of home sales, the median price of homes is estimated to have increased by 3.2% in 2023 and is forecast to decrease by -1.3% in 2024 before returning to annual increases of .4% to 3.3% during 2025-2030 with an average increase of 2.5%. Transfer and recordation taxes are derived from both residential and nonresidential transfer activity. The recordation tax is also applied to other instruments that are recorded in land records.

FY25 Budget - Key Economic Assumptions

				Percentage change Year-Over-Year						
	2022	**2023 (est.)***	**2024 forecast**	**2024**	**2025**	**2026**	**2027**	**2028**	**2029**	**2030**
Resident Employment (000's)	530.9	541.4	528.6	-2.4	0.1	1.2	0.6	0.5	0.5	0.4
December 2023	530.9	537.4	529.1	-1.6	0.9	1.0	0.6	0.5	0.5	
Total Personal Income ($bn)	98.3	101.6	104.3	2.6	3.0	4.6	4.4	4.1	3.6	3.3
December 2023	98.3	101.3	104.0	2.6	3.3	4.6	4.3	3.9	3.4	
Median Existing Home Sales (000's)	12.0	10.2	8.7	-15.1	2.2	14.6	8.1	5.5	4.5	0.4
December 2023	10.7	9.8	8.9	-9.5	15.1	6.0	-0.9	6.1	4.6	
Median Sales Prices ($)	620,053	640,176	631,911	-1.3	0.4	2.3	2.8	3.0	3.3	3.1
December 2023	624,996	644,495	621,774	-3.5	1.3	1.9	2.8	2.9	3.5	
				Forecast (%)						
CPI-U Washington MSA (%)	6.6	3.1	2.7		2.1	2.3	2.2	2.2	2.3	2.3
December 2023	6.6	3.0	2.0		2.2	2.2	2.2	2.3	2.3	2.3

*2023 data is estimated and 2024-2030 are forecasts

Risks to the Economic Assumptions

Any forecast is subject to both positive and negative risk factors. The County's budget assumptions and revenue forecast are no exception.

There are developments that could have a positive impact on economic activity in the future and result in revenues exceeding revised budget assumptions.

- The Fed may successfully engineer a "soft landing" of the national economy, which would prevent a recession and lead to rapid decrease in interest and mortgage rates that contribute to strengthening real estate activity
- Strong capital gains due to recent record setting stock market valuations
- Improvement in Montgomery County specific economic activities that are revenue drivers, including increased resident employment, personal income, and capital gains
- Further diminution of the COVID-19 pandemic contributing to improvement in labor force participation and broad-based wage gains
- Increases in employment due to stabilizing (or calming) geopolitical events

There are several key economic risks that could negatively impact the County in 2024 and beyond.

- A recession that is deeper and/or longer than the mild recession assumed in the FY24 budget and December Fiscal Plan
- Material deviation of the Washington DC Region and/or Montgomery County economic conditions from the broader national economy resulting in slower local economic growth
- Unstable or declining employment due to events such as:
    - a recession causing greater than expected employment losses
    - global economic instability due to the Russia/Ukraine war and food and fuel shortages
    - expansion of the Israel-Hamas war

- hostilities in other parts of the world impact the U.S. directly or indirectly including additional supply chain disruptions
    - the resurgence of COVID-19 or occurrence of another pandemic illness
- Slower personal income growth due to:
    - reduced corporate profitability and persistent inflation that does not retreat to the Federal Reserve's 2% target during CY24-25
    - weak capital gains due to financial market volatility
- Assessed values grow more slowly than forecast due to:
    - persistent high mortgage rates causing reduced housing affordability and reduced home sales
    - uncertainty of commercial property assessments and appeals, as well as new construction as offices downsize with remote work becoming structurally more permanent
- A financial crisis due to US Federal fiscal conditions related to the growing debt to GDP ratio or Congressional action that adversely affects the national economy

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.