DEPARTMENT OF FINANCE

Isiah Leggett
County Executive

Alexandre A. Espinosa
Director

March 23, 2017

Honorable County Executive, and
Members of the Montgomery County Council

Ladies and Gentlemen:

I am pleased to present the findings of the Eighteenth Annual Business Advisory Panel that was convened on February 22, 2017. The enclosed report was prepared by the County's Department of Finance pursuant to Article XI, Section 20-61 of the Montgomery County Code.

The report consists of a summary of the panel's advice, a list of the panelists, the information package that the Department of Finance sent to the panelists in advance of the meeting, and a presentation prepared for the Panel by Andrew Schaufele, Director, Bureau of Revenue Estimates, Office of the Comptroller of Maryland. The information package includes the agenda for the meeting, concise statements by the Department on the economic outlook, and a framework for discussion.

I believe that the accompanying material accurately reflects the economic advice given by the Business Advisory Panel.

Sincerely,

Alex Espinosa

Alexandre A. Espinosa, Director
Department of Finance

Attachments

Office of the Director

101 Monroe Street, 15th Floor • Rockville, Maryland 20850 • 240-777-8860 • 240-777-8857 FAX
montgomerycountymd.gov

FINDINGS OF THE EIGHTEENTH ANNUAL BUSINESS ADVISORY PANEL FEBRUARY 22, 2017

Pursuant to Article XI, Section 20-61, of the Montgomery County Code, the Department of Finance (Finance) convened a meeting of the Business Advisory Panel (BAP) on February 22, 2017. The County Council of Montgomery County established the BAP in 1999 to seek the advice of industry experts in key sectors of the County's business community concerning the current and future state of the County's economy. The law requires that the Director of Finance convene the panel annually and relay the panel's advice to the County Executive and County Council. This report provides such advice.

The BAP members representing real estate, finance, bioresearch, health services, government, and trade associations, were joined by the County Executive Isiah Leggett and County Councilmember Hans Riemer.

The meeting was structured to allow all participants to provide a briefing on the local, state, and regional economic trends and to share their insights about future economic prospects in the County. The participants also discussed Finance's economic assumptions for the next six fiscal years. For purposes of this report, the results of the discussions are presented in two parts. The first part discusses the participant's professional judgment about the County's economy and Finance's economic assumptions. The second section discusses the participant's view of their respective industry sector.

The County Executive opened the meeting and expressed uncertainty regarding public policies at the state level, changes at the national level with the new president, and the status of federal employment. Issues that are important to the County include transportation and infrastructure spending. The County Executive addressed the issue of immigration and reviewing limitations on immigration authority. Finally, the County Executive discussed the economic consequences of the Purple Line, the location of the Federal Bureau of Investigation headquarters, and the expansion of the Food and Drug Administration.

I. Current Economic Conditions and Future Economic Assumptions

Finance asked the participants to provide comments to a paper prepared by staff that analyzed the County's economy and provided assumptions about the economic outlook for the next six years. The paper analyzed a number of economic indicators including employment, personal income, real estate, inflation, construction, and interest rates. A detailed report on the County's economy and economic assumptions follows these findings. The following is a summary of those assumptions are:

- ***Payroll Employment.*** Payroll employment will continue to increase from calendar year 2016 (CY2016) to CY2023 and grow at an average annual rate of 0.8 percent over that period. This is slightly below the average annual growth rate of 0.9 percent experienced between CY2009 and CY2016.

- ***Resident Employment.*** Resident employment will also increase at an average annual rate of 0.8 percent from CY2016 to CY2023. That rate is slightly below the average annual rate of 1.1 percent between CY2009 and CY2016.

- ***Wage and Salary Income.*** Wage and salary income is estimated to grow at an average annual rate of 4.2 percent between CY2015, the latest date for which actual data are available from the Bureau of Economic Analysis, U.S. Department of Commerce, and CY2023. Total wage and salary income is estimated to reach $49.8 billion by CY2023.

- ***Personal Income.*** Total personal income in Montgomery County is estimated to grow at an average annual rate of 4.4 percent from CY2015 to CY2023. By CY2023, total personal income will reach $112.5 billion.

- ***Inflation (annual average).*** Overall regional inflation index will gradually increase from 1.18 percent in CY2016 to 2.20 percent in CY2017, 2.30 percent in CY2018 and CY2019, and peak at 2.50 percent from CY2021 to CY2023.

- ***Interest Rates.*** The County is expecting to earn an average of 0.70 percent in investment income on its short-term portfolio for fiscal year (FY) 2017 with increases from 1.20 percent in FY2018 to 3.00 percent by FY2022 and FY2023.

Maryland Economy

The Director of the Bureau of Revenue Estimates (BRE), Office of the Comptroller of Maryland, presented an economic outlook on the national economy, the Maryland economy, BRE's economic forecast for the Maryland economy, and selected income tax data to the County Executive, County Councilmember, and the participants. A copy of BRE's presentation is included in this report. Highlights of BRE's presentation:

- ***Income Tax Data.***

    - 2,751 Maryland taxpayers represent 0.1 percent of the total number of statewide taxpayers and pay 9.0 percent of the state's income tax.

    - 137,588 Maryland taxpayers represent 5.0 percent of the total number of statewide taxpayers and pay 40.6 percent of the state's income tax.

    - 485 Montgomery County taxpayers represent 0.1 percent of the total number of County taxpayers and pay 8.6 percent of the County's state income tax.

    - 19,411 Montgomery County taxpayers represent 5.0 percent of the total number of County taxpayers and pay 42.1 percent of the County's state income tax.

- Withholdings account for 92 percent of the total income tax component and estimated payments account for 14 percent of the total (includes refund share of -7 percent).

- Between 2009 and 2013, an average of forty-one percent of capital gains in the state are concentrated in the top 0.01 percent of taxpayers.

- Because of the concentration of income tax revenues from the small percentage of the taxpayers and capital gains, there are legislative proposals and policy initiatives (HB430 and SB306 – Governor's bills, HB503 and SB371 – Legislative bills) to address the impact of such concentration and subsequent revenue volatility on the state's budget.

- ***Economic and Demographic Data***

  - The post Great Recession recovery and expansion has experienced an unprecedented slow growth in gross domestic product (GDP) compared to the previous post-recession recoveries and expansion cycles.

  - Between 2010 and 2016, the growth rates in the national labor force and productivity are the lowest compared to the previous seven decades starting in 1950.

  - The percentage of the total population aged 65 and over will increase from 13.1 percent in 2010, to 17.3 percent by 2020, and to 21.6 percent by 2030.

  - The State of Maryland is not benefitting from international trade

  - BRE's forecast for selected economic indicators are:

    - ***Personal income:*** 3.3 percent (CY2016); 4.0 percent (CY2017); 4.2 percent (CY2018); 4.1 percent (CY2019); and 4.1 percent (CY2020)

    - ***Payroll employment:*** 1.6 percent (CY2016); 1.0 percent (CY2017); 0.8 percent (CY2018); 0.5 percent (CY2019); and 0.6 percent (CY2020).

II. Specific Industry Sectors

Representatives from the Washington regional associations discussed the state of the economy in the Washington metropolitan area and Montgomery County. The representative from the real estate market stated that new listings have increased 16 percent the past year. The market had a very good year in 2016 but high-end priced homes are selling at a slower rate. The average and median selling prices are expected to increase 5 percent this year. There were also three topics mentioned by the representative: 1) the lack of affordable housing, 2) the quality of life is an important issue in the purchase of a home in the County, and 3) people are moving close to transit centers.

The representative from the Health Care industry noted the uncertainty within the health care industry. Approximately 32,000 County residents are enrolled through the Affordable Care Act (ACA) and the uncertainty stems from the possible changes through the ACA by the federal government. There is instability in the insurance program and it has become less affordable. Medicaid costs have increased from 116 percent to 138 percent of per capita income. The State of Maryland pays hospitals differently compared to other states, and per capita hospital expenses are capped between 4 and 6 percent with a target profit margin of approximately 3.5 percent. Because of the fixed budget in the state, hospitals work cooperatively to avoid unnecessary utilization to help manage their budgets.

A representative from the bio-health industry stated that the industry has no excess capacity. There is no small-size wet lab space and no space for emerging technology. The representative suggested that there is retrenchment in economic development in the State of Maryland. There is not sufficient state capital for early development as a bridge to venture capital funding. The region needs to develop the concept of "clusters" among bio-health firms such as a Greater Washington Partnership rather than "stealing" among current firms.

The representative from the Chamber of Commerce discussed the major issue of retention of federal jobs in the County. The second issue is the growth of the health information technology sector. Finally, the third issue is to increase sales by small businesses to the federal government. Other issues discussed by the representative is the need and supply of affordable housing, the need to retain well-trained talent in the County, the initiative to address customer care issues, and the uncertainty of the County rules on employment and regulations.

Participants representing economic development stated that METRO is not functioning, and that there is a lack of regional prioritization for transportation. There is an image both within and outside the region that METRO is not a reliable system. The representatives also concurred with the Chamber of Commerce representative of the goal to obtain and retain talent and the need for affordable housing. Other issues include an outreach program to the entrepreneurial sector by providing equity funding through foundations and collaboration and the Montgomery 365 initiative - theme also discussed by the representative of the bio-health industry. Finally, there is an excess capacity of office space and rents have stagnated.

Representatives from the real estate development industry stated that businesses are leasing and that there is some flexibility in tech space. However, costs of investment are higher. There is a small-sized market because of costs and a drop rent, that is, there is a demand for smaller work spaces for employees. One company is working with the Department of Defense for a health facility in the County. The challenge in the County is to obtain more businesses and therefore more jobs.

Representatives for the financial industry stated there are not many requests for rental space and that the Regus™ model is the future for office space. Developers are finding investments through bridge loans. There is a growing number of residential contracts with more initial equity funding. Income from capital gains is expected to increase since the loss carry forward has expired. However, there is no big shift of income.

The representative from the information technology industry stated that the company is adding more customer service through the launch of a satellite that will provide service to Latin America. The company added jobs in 2016 and expects to add an additional 60 to 100 jobs in 2017. Because of the increase in jobs, the company has renewed two large leases in the County and added 15,000 square feet of space.

The representative from the Hotel-Motel industry stated that the hotel-motel sector was not affected by National Harbor and that the industry plans to add 150 rooms in the County. An important policy issue for the industry is with AirBNB regulations.

Finally, the representative from the regional government organization stated that METRO is a major priority for the region. Jobs in the region are growing but at a much slower pace. There is very little growth in commercial space and only 7.4 million square feet of space has been added – the lowest construction activity in year - and a 15 percent vacancy rate among commercial property. The regions' economy should develop a more global focus and less reliance on the federal government. Regarding workforce development, there could be more demand for the traditional "blue-collar" well-paying jobs.

III. Conclusion

The representatives expressed cautious optimism regarding the region's and County's economy. The major issues discussed by the representatives are the lack of space for the bio-health industry, the lack of regional prioritization for transportation, the need for obtaining and retaining talent and customer service, the need for affordable housing, the focus on business development should be a regional focus and with less reliance on the federal government. A number of representatives discussed that METRO currently is not a reliable transit system. Finally, the representative from the County Executive's staff stated that they are working to improve the culture and customer service for businesses, addressing the issue of "dying" office parks, and working with the bio-tech association to address the problem of lack of space for bio-health companies.

Attendees
Business Advisory Panel
February 22, 2017

Mr. Isiah Leggett
Montgomery County Executive

Honorable Hans Riemer
Vice President
Montgomery County Council

Mr. Alexandre A. Espinosa
Director
Montgomery County Department of Finance

Mr. Brian E. Barkley, Esquire
Vice President for Legislation of the
Rockville Chamber of Commerce

Mr. Richard Bendis,
President and Chief Executive Officer
BioHealth Innovation

Mr. Bob Buchanan
Chairman
Montgomery County Economic
Development Corporation

Mr. Paul N. Chod
President
Minkoff Development Corporation

Ms. Annice Cody
President
Holy Cross Health Network
Holy Cross Health

Mr. Michael Coveyou
Chief, Division of Treasury
Montgomery County Department of Finance

Mr. Paul DesJardin, Director
Community Planning and Services
Metropolitan Washington Council of Governments

Ms. Georgette Godwin
President and Chief Executive Officer
Montgomery County Chamber of Commerce

Ms. Kelly Groff
President and Chief Executive Officer
Visit Montgomery

Mr. Edward Harrington
Regional President MD/DC
John Marshall Bank

Mr. Michael Moran
Chief Executive Officer
Greater Capital Area Association of Realtors

Mr. James G. Muir, III
Vice President
EchoStar – Corporate Real Estate Program
Hughes – an EchoStar Company

Mr. David Petr
Chief Executive Officer
Montgomery County Economic Development Corporation

Mr. David Platt
Chief Economist
Montgomery County Department of Finance

Ms. Lily Qi
Assistant Chief Administrative Officer
(Economic and Workforce Development)
Montgomery County
Office of the County Executive

Mr. Lawrence N. Rosenblum, CPA
Partner
Grossberg Company, LLP

Mr. Roberto Ruiz
Research Manager
Research and Special Projects Division
M-NCPPC

Andrew Schaufele, Director
Bureau of Revenue Estimates
Comptroller of Maryland

Gene Smith
Legislative Analyst
Montgomery County Council

Mr. James A Soltesz
President and Chief Executive Officer
Soltesz Associates, Inc.

MONTGOMERY COUNTY

18TH ANNUAL

BUSINESS ADVISORY PANEL

FEBRUARY 22, 2017

MEETING

WHERE:	COUNTY EXECUTIVE'S CONFERENCE ROOM EXECUTIVE OFFICE BUILDING 2nd FLOOR 101 MONROE STREET ROCKVILLE, MARYLAND 20850 (240) 777-8877
WHEN:	WEDNESDAY, FEBRUARY 22, 2017

AGENDA

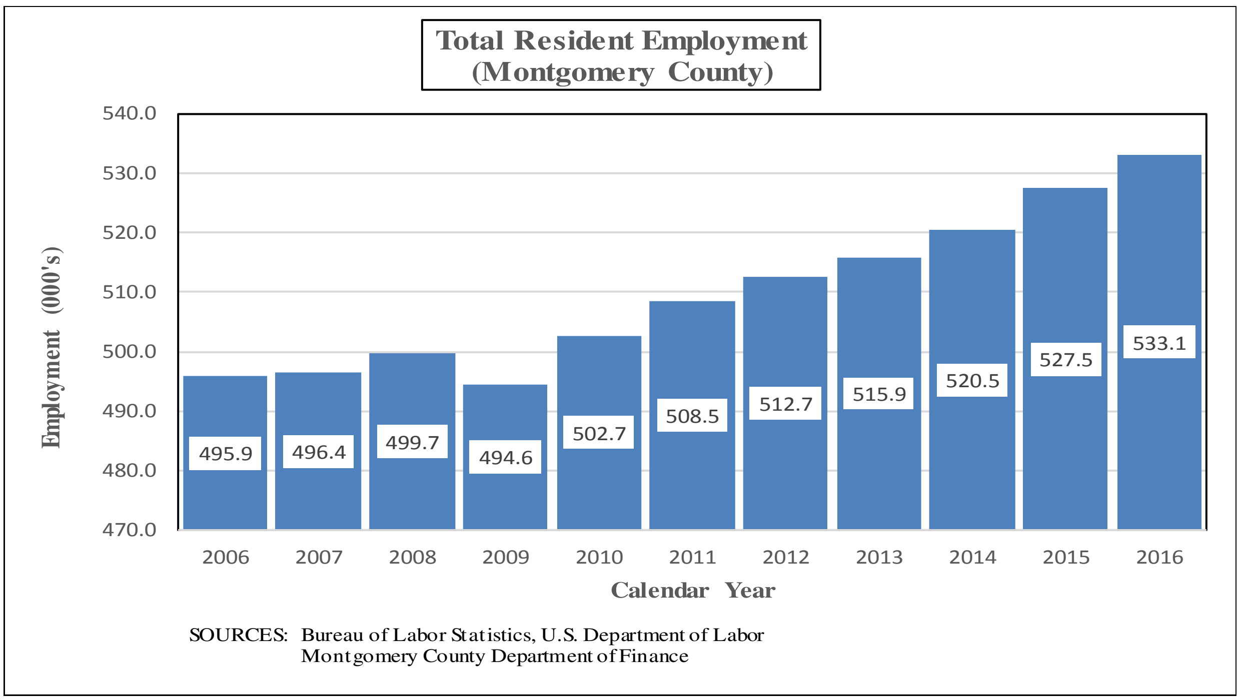
9:00 A.M.	Introduction, Alexandre Espinosa, Director, Montgomery Department of Finance
9:05 A.M.	Opening Remarks by Isiah Leggett, County Executive
9:20 A.M.	Presentation of Department of Finance economic assumptions
9:30 A.M.	Presentation by Andrew Schaufele, Director, Bureau of Revenue Estimates, Comptroller of Maryland
10:00 A.M.	Roundtable discussion by participants
11:30 A.M.	Adjournment

ECONOMIC CONDITIONS AND OUTLOOK

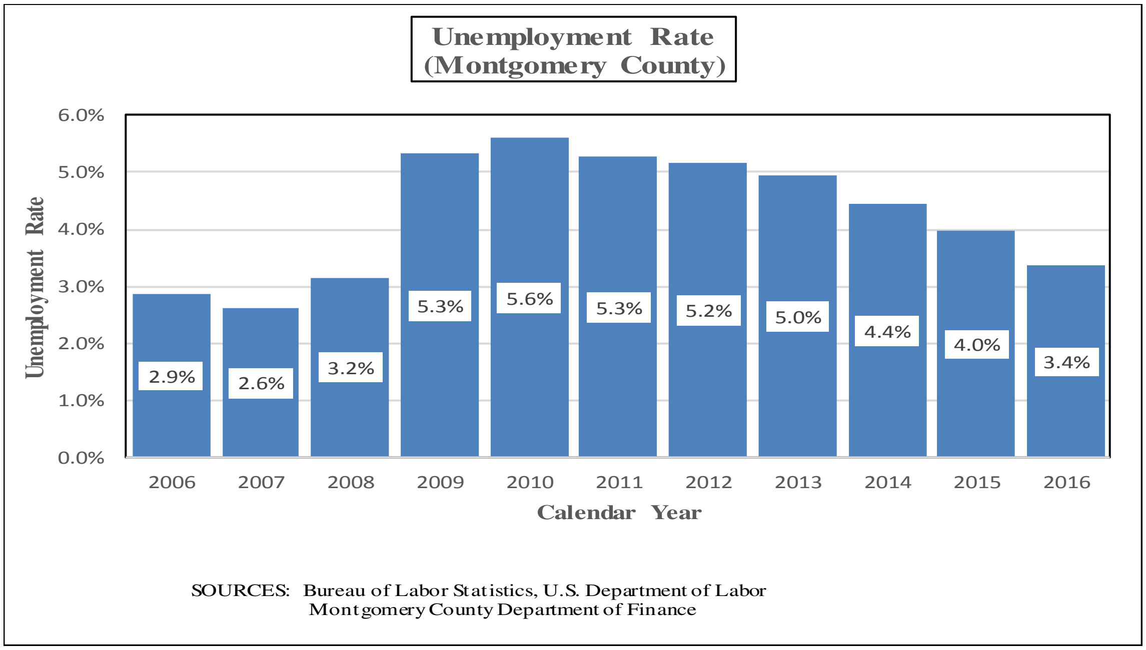
Montgomery County's economy experienced positive economic performance during 2016. Some of the areas of strength included an increase in resident employment, a decline in the unemployment rate, an increase in the sale of existing homes, an increase in the median sales price for an existing home, and an increase in the value of non-residential construction. However, offsetting those increases, the County experienced a decline in the construction of residential properties.

Employment Situation

Based on data from the Maryland Department of Labor, Licensing and Regulation (DLLR) and the Bureau of Labor Statistics, U.S. Department of Labor, resident employment (labor force series and not seasonally adjusted) in 2016 increased by nearly 5,600 from 2015 (↑1.1%).

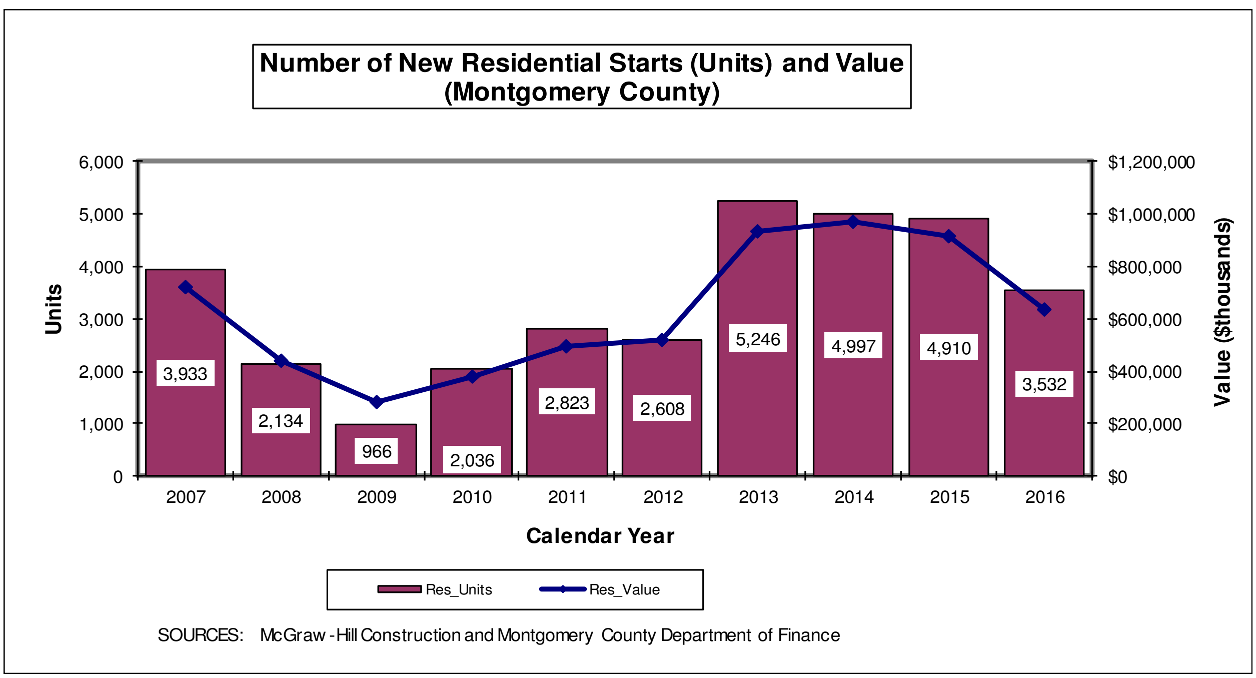


The County's unemployment rate declined to 3.4 percent compared to 4.0 percent in 2015 and is the lowest in eight years. The decline in the unemployment rate is attributed to a larger percentage increase in resident employment (↑1.1%) than in the labor force (↑0.4%).



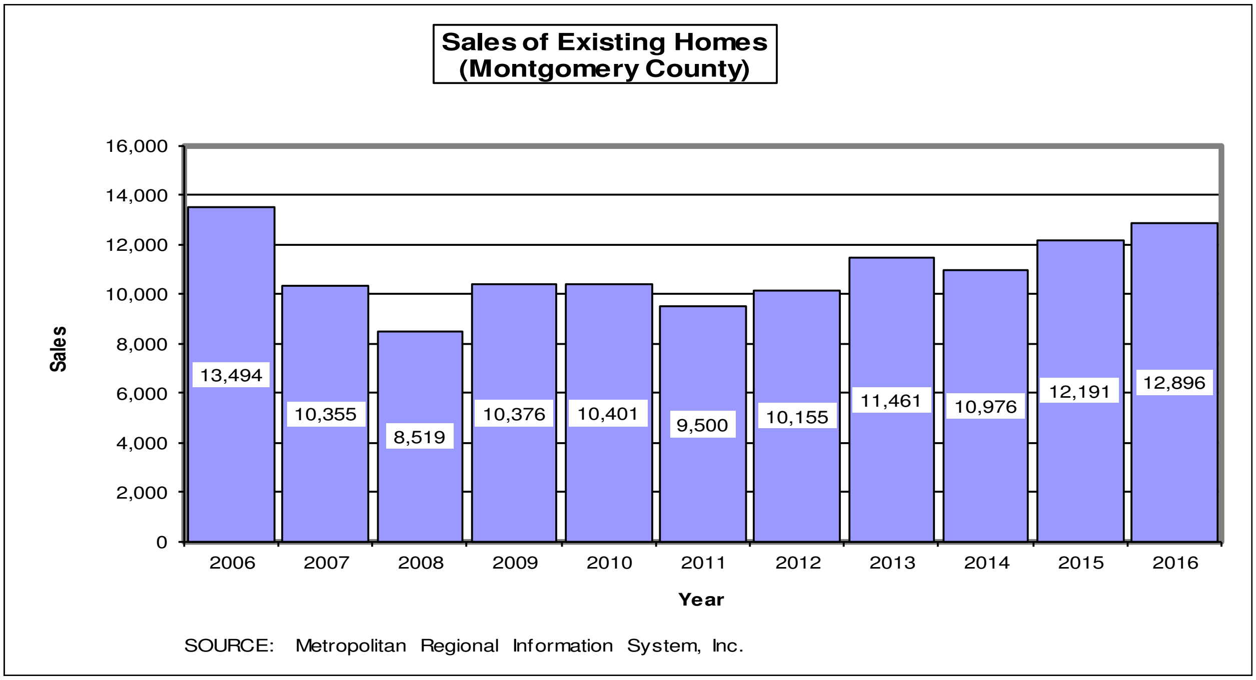
Construction Activity

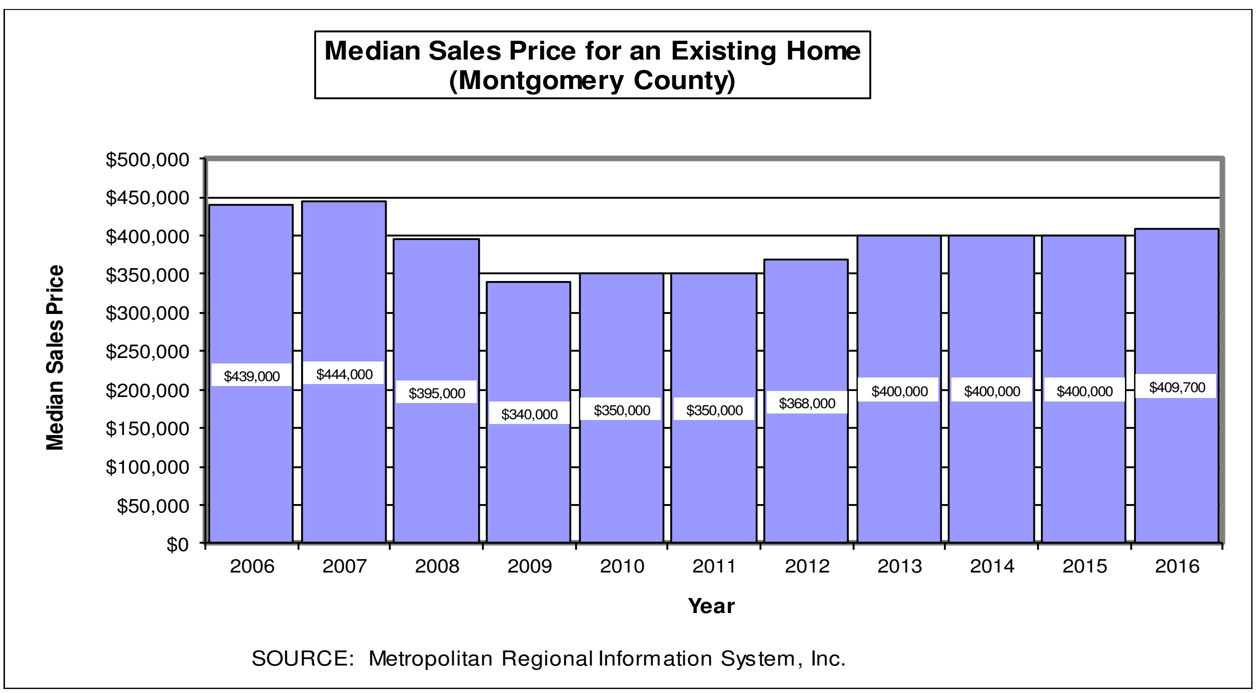
After experiencing an increase of over 100 percent in 2013, the construction of new residential units declined 4.8 percent in 2014, 1.7 percent in 2015, and 28.1 percent in 2016. The decrease in 2016 was attributed to the decline in the construction of multi-family units (↓41.8%). Construction of single-family units were up 17.8 percent in 2016. Total value added decreased from a total of $913.4 million in 2015 to $634.1 million in 2016 (↓30.6%). The number of non-residential construction projects increased from 157 projects in 2015 to 201 in 2016 (↑28.0%), the total value added increased from $729.6 million to $1,108.6 million (↑51.9%).



Residential Real Estate

During calendar year 2016, existing home sales increased 5.8 percent from 2015 which followed an 11.1 percent increase in 2015. The average sales price for existing homes increased a modest 0.8 percent in 2016 while the median sales price increased 2.4 percent after remaining at $400,000 the previous three years.





Retail Sales

Using sales tax receipts as a measure of retail sales activity in the County, retail sales, including assessment collections, increased 1.1 percent in 2016. Purchases of nondurable goods, which include food and beverage, apparel, general merchandise, and utilities and transportation, increased 0.8 percent during this period while sales of durable goods were up 1.7 percent. The increase in nondurable goods purchases was largely attributed to the increase in apparel items (↑11.4%), while the increase in purchases of durable goods was largely attributed to an increase in automobile sales and products (↑3.2%) and building and industrial supplies (↑5.3%).

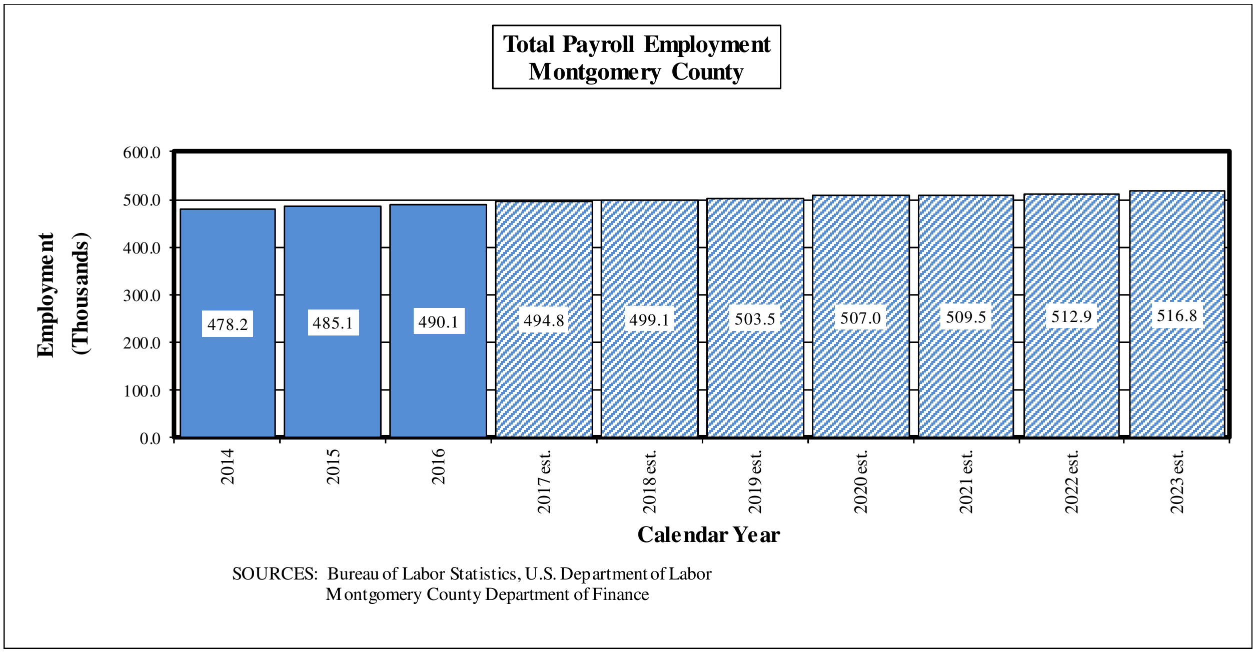
CONCLUSION

The major economic indicators confirm that the County's economy experienced positive performance during 2016. That performance include an increase in residential employment, a decline in the unemployment rate, an increase in existing home sales, an increase in the median sales price for an existing home, and an increase in the value added for non-residential construction, but partially offset by a decline in the construction and value added of new residential construction.

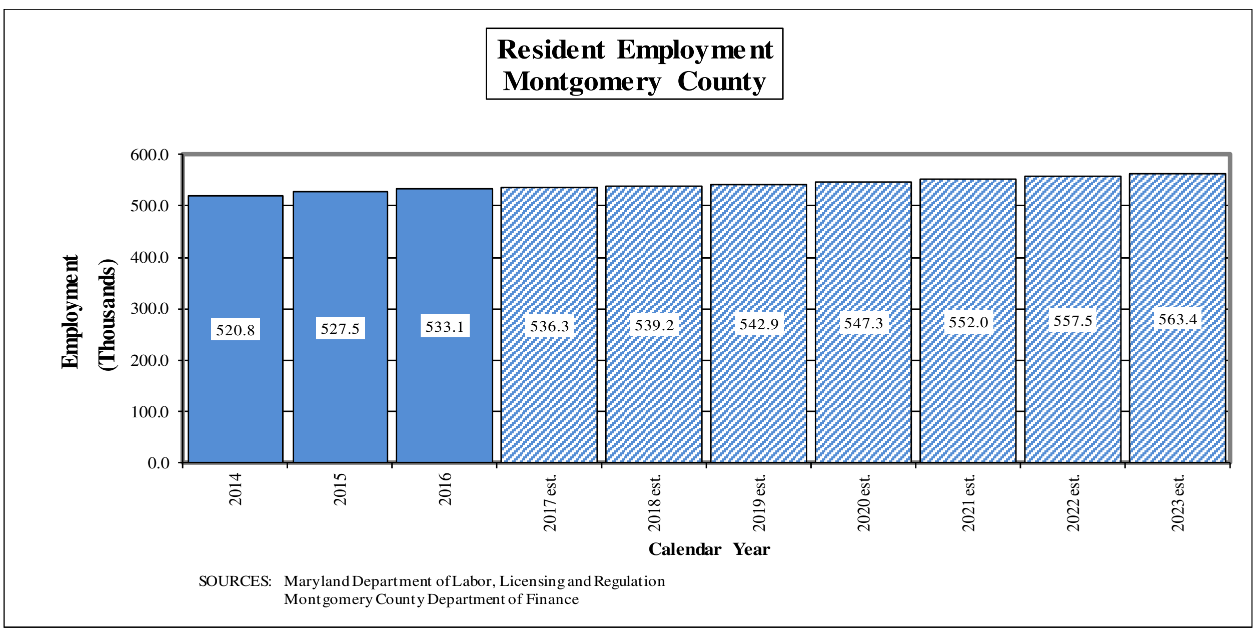
ECONOMIC OUTLOOK

The Department of Finance (Finance) forecasts that the Montgomery County's economy will continue to improve through the next six years.

Employment. Finance assumes payroll employment will continue to increase from CY2016 to CY2023 and grow at an average annual rate of 0.8 percent over that period. This is slightly below the average annual rate growth rate of 0.9 percent experienced between CY2009 and CY2016.



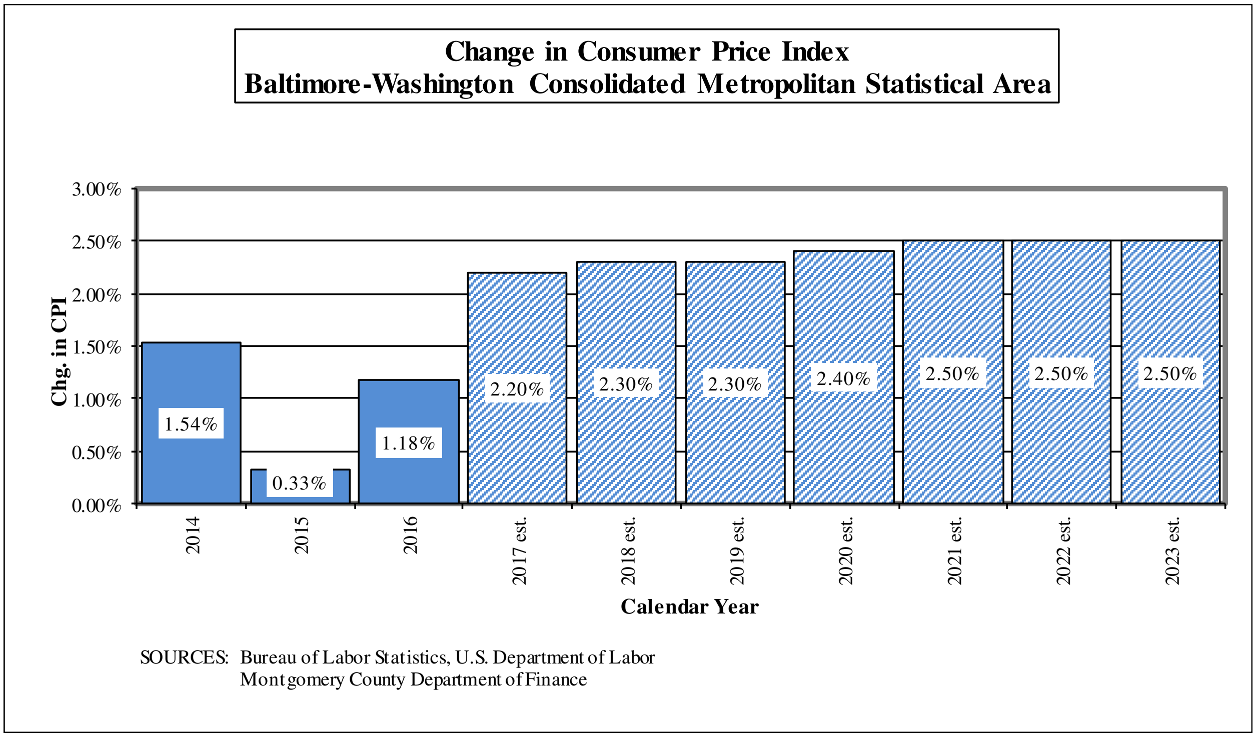
Finance assumes that resident employment will increase at an average annual rate of 0.8 percent from CY2016 to CY2023. However, that rate is slightly below the average annual rate of 1.1 percent between CY2009 and CY2016.



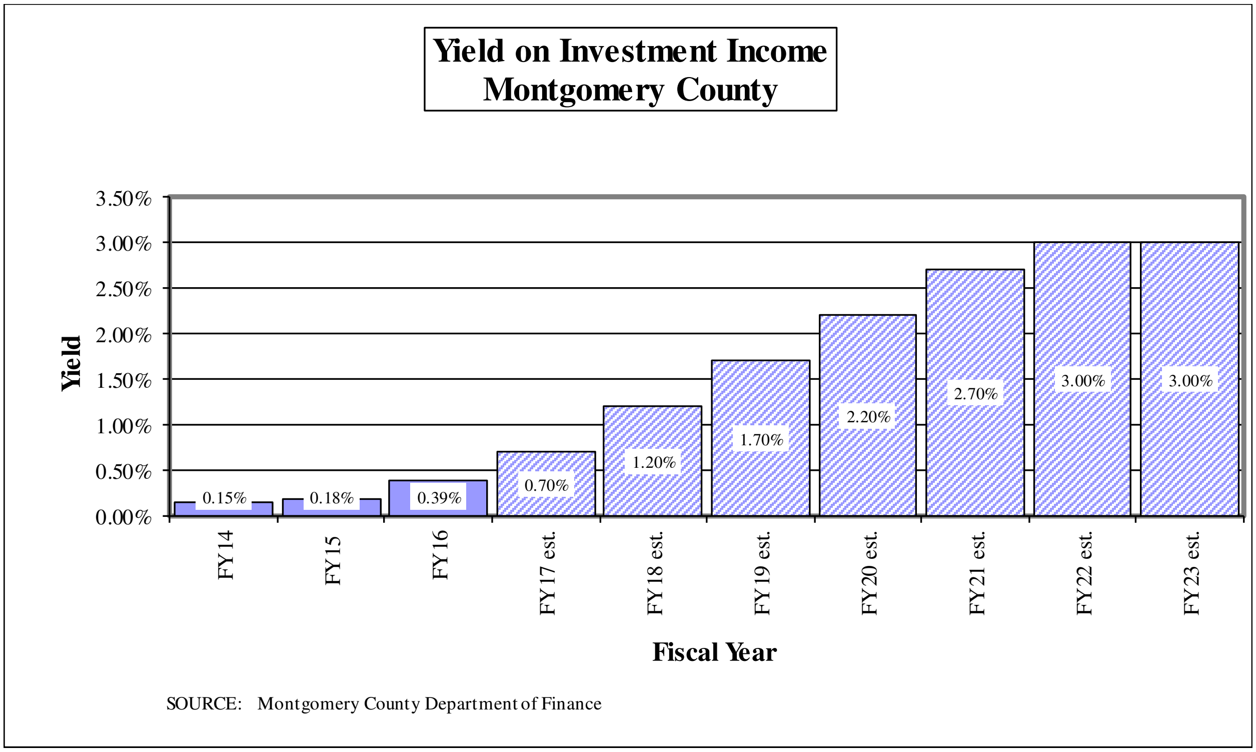
Finance assumes wage and salary income to grow at an average annual rate of 4.2 percent between CY2015, the latest date for which actual data are available from the Bureau of Economic Analysis, U.S. Department of Commerce, and CY2023. Total wage and salary income is estimated to reach $49.8 billion by CY2023.

- ***Personal Income.*** Finance assumes that total personal income in Montgomery County will grow at an average annual rate of 4.4 percent from CY2015 to CY2023. By CY2023, total personal income will reach $112.5 billion.

- ***Inflation (annual average).*** Finance assumes that the overall regional inflation index will increase from 1.18 percent in CY2016 to 2.20 percent in CY2017, 2.30 percent in CY2018 and CY2019, 2.4 percent in CY2020, and peak at 2.50 percent from CY2021 to CY2023.



- ***Interest Rates.*** From September 2007 to December 2008, the Federal Reserve Board, through its Federal Open Market Committee (FOMC, Committee), aggressively cut the target rate on federal funds from 5.25 percent to a range of 0.00-0.25 percent. The targeted federal funds rate set by the FOMC remained at the 0.00-0.25 range until December 2015. At its December 2015 meeting, the FOMC increased the range to between 0.25 and 0.50 percent and between 0.50 and 0.75 percent in December 2016. The target rate was unchanged at its meeting in February of this year. Since the yield on the County's short-term investments are highly correlated with the federal funds rate, The County earned an average of 0.39 percent in investment income on its short-term portfolio for fiscal year (FY) 2016 with estimated increases to 0.70 percent in FY2017 and 1.20 percent to 3.00 percent from FY2018 to FY2022 and FY2023. This assumption is based on two rate increases in the targeted federal funds rate by the FOMC each year between FY2018 and FY2021, a modest increase in FY2022 and no increase in FY2023. The assumption of future rates increases is based on the 30-day federal funds futures market from the Chicago Mercantile Exchange.


Yield on Investment Income
Montgomery County
3.50%
3.00%
2.50%
2.00%
1.50%
1.00%
0.50%
0.00%
Yield
0.15%
0.18%
0.39%
0.70%
1.20%
1.70%
2.20%
2.70%
3.00%
3.00%
FY14
FY15
FY16
FY17 est.
FY18 est.
FY19 est.
FY20 est.
FY21 est.
FY22 est.
FY23 est.
Fiscal Year
SOURCE: Montgomery County Department of Finance

DISCUSSION FRAMEWORK

The economic assumptions provide a framework for the Department of Finance's revenue projections for FY2018 through FY2023. The following issues create the framework for the discussion that is the focus of the Business Advisory Panel. In order to gain a better understanding of the direction of the major industrial sectors in our county and region, it would be helpful if the participants of the Business Advisory Panel comment on our assumptions and discuss the major economic trends in the next six years that affect their industry sector. The following list of items, if applicable to your sector, may be used to focus your discussion:

Real Estate

- Residential construction
- Commercial construction
- Prices/rents
- Vacancy rates
- Loan conditions – residential and commercial sectors

Income

- Capital gains
- Estimated payments
- Tax Policy Changes: Federal and State
- Wynne decision

Industry Sectors

- Business activity
- Employment outlook
- Consumer spending
- Federal government spending and employment
- Transportation
- Biotechnology
- Information Technology
- Retail
- Other Professional Services

Risk to the Forecasts (Assumptions)

- Federal and state government fiscal policies
- Employment, both government and private
- Interest rates
- Inflation
- Domestic stock market volatility attributed to current and future international economic and commodities
- Residential/commercial development
- Health insurance changes

MARYLAND REVENUE ESTIMATES

REVENUES & ECONOMICS

Office of the Comptroller
State of Maryland

Andrew Schaufele: Director, Bureau of Revenue Estimates
February 22, 2017

Disclaimer

- I represent myself today
- Not the Comptroller, not the Board of Revenue Estimates

Agenda

- September Estimates – Large Reduction
- Revenue Volatility in the Income Tax
- Economic Outlook – Focus on Demographics

September GF Write-Down

Tax Type	Approx Share GF	FY 2016 Closeout Variance	FY 2017 September Reduction
Personal Income Tax	54%	-261,532	-306,549
Sales Tax	28%	-5,202	-26,699
Other	18%	+16,623	-31,808
Total Ongoing General Fund	100%	-250,111	-365,056
Change From Previous Estimate		-1.5%	-2.2%
Note: Dollars in Thousands			

- The FY16 Variance Accounts for ~ 70% of the Reduction in FY17

Other Impacts – Before Moving On

- Other revenues swing from +$16.6 million to -$31.8 million
- Two drivers
  - Corporate Income Tax +$7.8 million to -$10.9 million
    - Reduction in outlook for corporate profits (more on this later)
  - State Lottery (not Casinos) +$9.4 million to -$6.8 million
    - Payouts were very favorable to the State in fiscal year 2016

Income Tax Always Paramount

Income Tax Component	Approx Share Net	FY 2016 Closeout Variance	FY 2017 September Reduction
Withholding	92%	-140	-103
Estimated	14%	-67	-146
Fiduciary	1%	-12	-17
Net Final Payments & Refunds	-7%	-202	-238
Total Net Receipts	100%	-421	-504
Change From Previous Estimate		-3.1%	-3.4%
Notes: Dollars in Millions; Includes State and Local Tax, not just GF			

Economic Outlook is Reduced, but Prior Variance Most Significant

SO WHAT HAPPENED IN FISCAL YEAR 2016??

Undiversified Tax Base – State TY14

Percentile	# Tax Payers	Net Maryland Tax ($)	Average Federal Gross Income ($)	Share State Net Tax (%)	Cum Share State Net Tax (%)
<=0.1%	2,751	624,673	4,658	9.0	9.0
>0.1% & <=1.0%	24,766	874,206	751	12.6	21.6
>1.0% & <=5.0%	110,071	1,318,212	280	19.0	40.6
>5.0% & <=10.0%	137,588	952,179	177	13.7	54.3
>10.0% & <=25.0%	412,766	1,678,376	114	24.2	78.5
>25.0% & <=50.0%	687,942	1,321,466	62	19.0	97.5
>50.0% & <=75.0%	687,942	347,158	29	5.0	102.5
>75.0% & <=100.0%	687,943	-173,906	12	-2.5	100.0
Total	2,751,769	6,942,365	75	100	100

Notes: (1) Dollars in Thousands; (2) Ordered by State Net Tax

Undiversified Tax Base – MoCo TY14

Percentile	# Tax Payers	Net Local Tax ($)	Average Federal Gross Income ($)	Share State Net Tax (%)	Cum Share State Net Tax (%)
<=0.1%	485	109,732	7,803	8.6	8.6
>0.1% & <=1.0%	4,367	176,237	1,395	13.8	22.4
>1.0% & <=5.0%	19,411	252,266	455	19.7	42.1
>5.0% & <=10.0%	24,263	169,329	252	13.2	55.3
>10.0% & <=25.0%	72,789	291,259	155	22.8	78.1
>25.0% & <=50.0%	121,315	215,194	78	16.8	95.0
>50.0% & <=75.0%	121,315	64,461	35	5.0	100.0
>75.0% & <=100.0%	121,315	2	7	0.0	100.0
Total	485,260	1,278,481	104	100	100

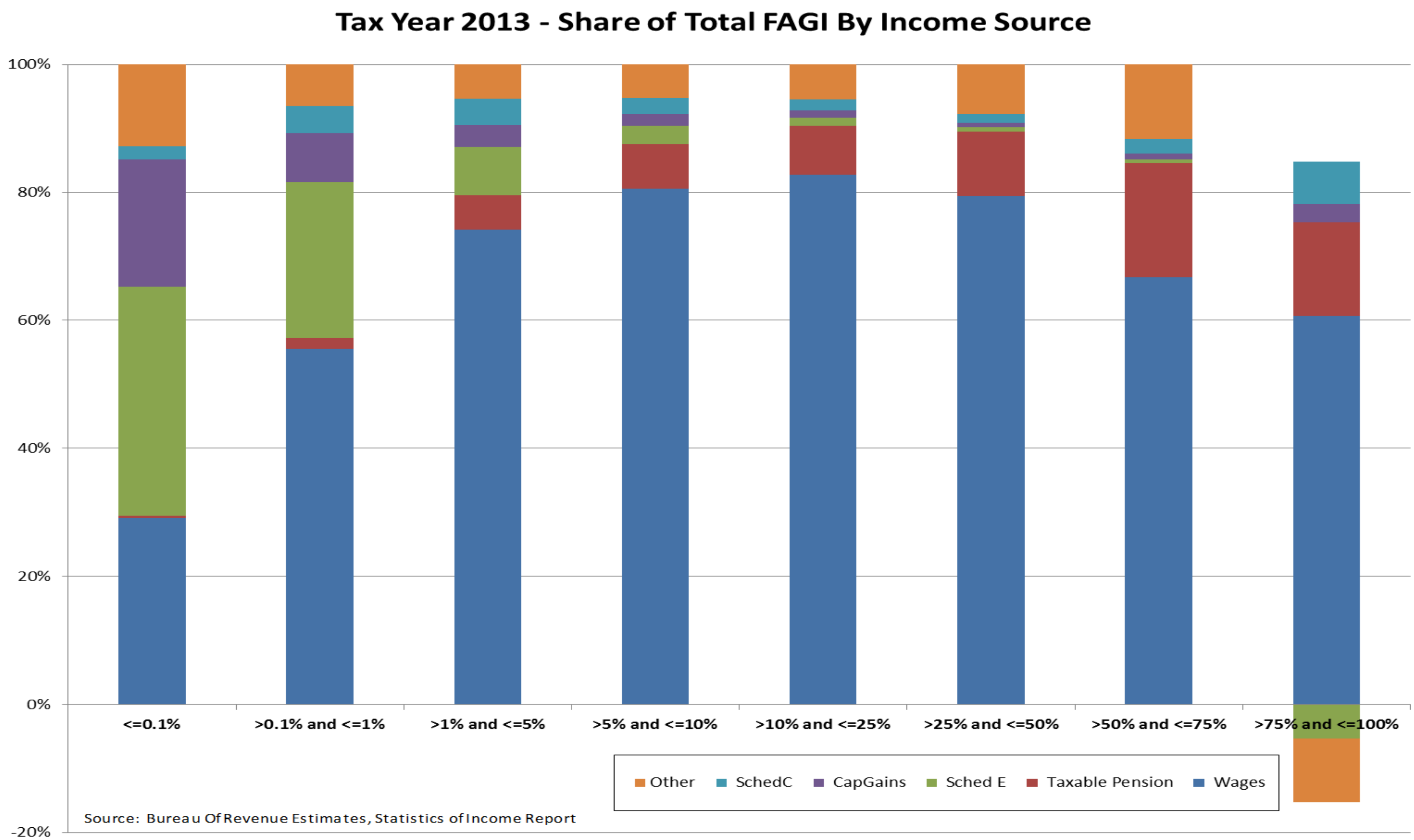
Notes: (1) Dollars in Thousands; (2) Ordered by Net Local Tax

Undiversified Tax Base

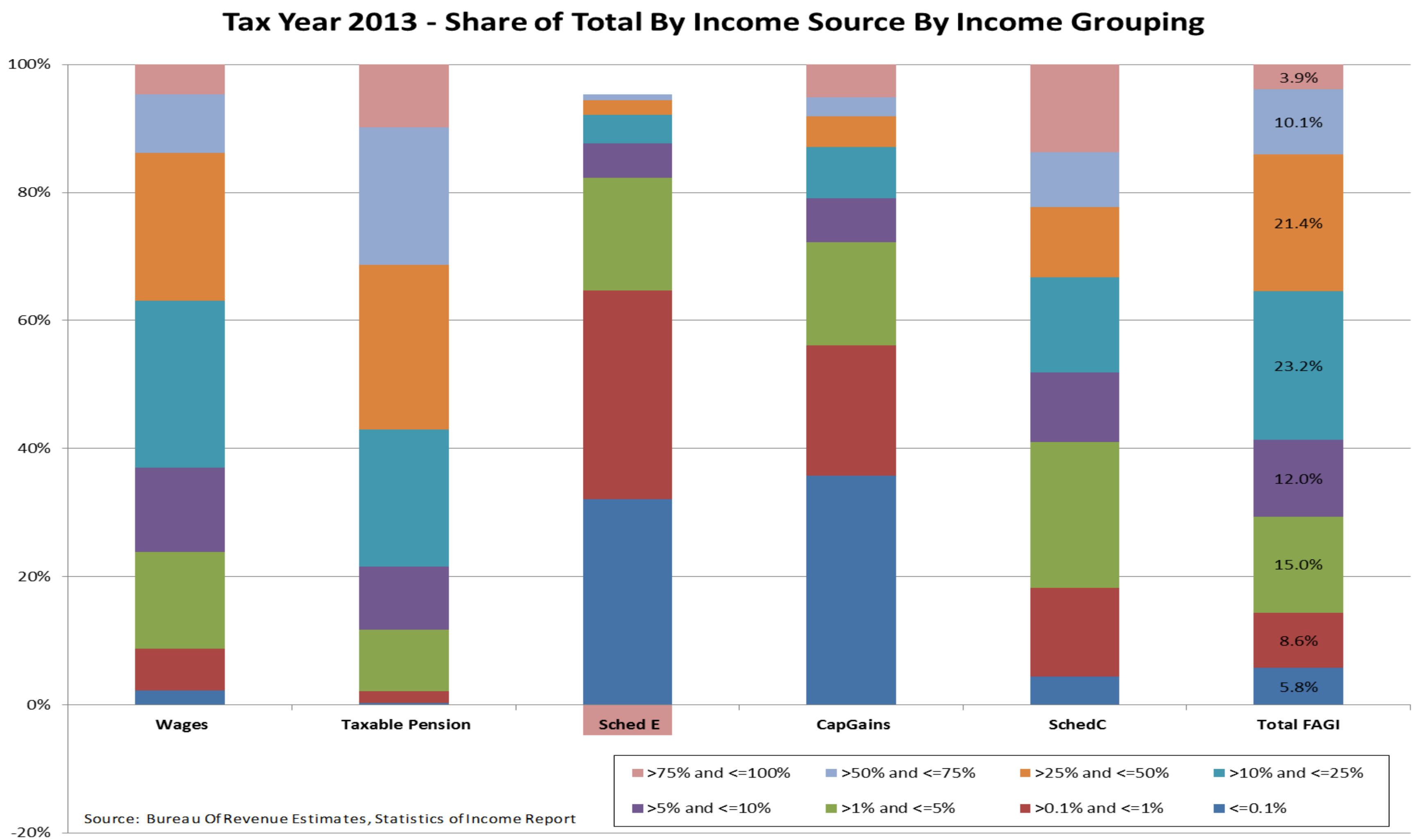
- 2,751 (0.1%) taxpayers pay 9.0% of the income tax
  - The income tax is ~ 50.0% of the general fund
    - Therefore, 4.5% of total general fund from 2,751 taxpayers
- 137,588 (5.0%) taxpayers pay 40.6% of the income tax
  - The income tax is ~ 50.0% of the general fund
    - Therefore, 20.3% of total general fund from 137,588 taxpayers

Lack of Diversity Results in Volatility

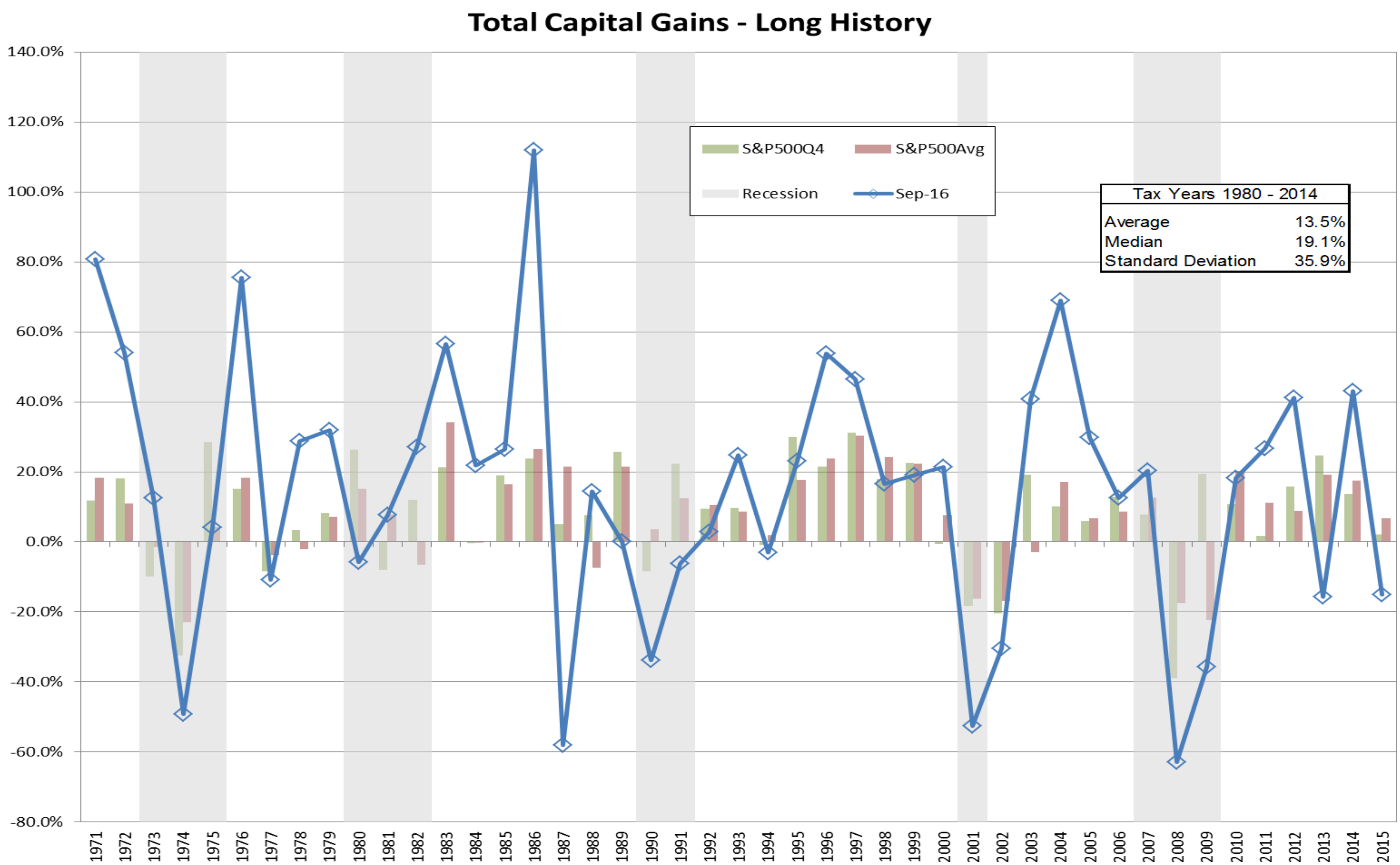
Sources of Income By Percentile



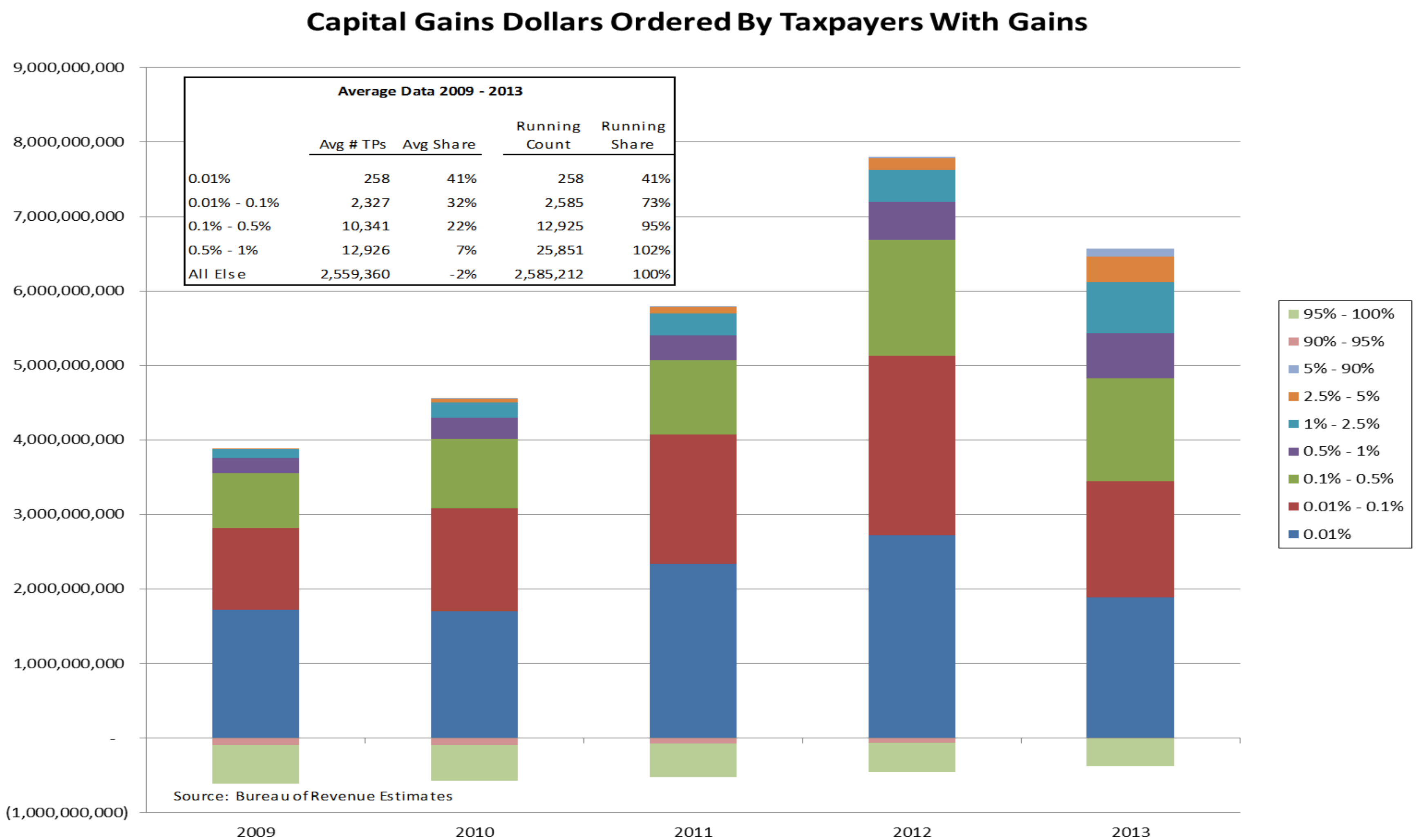
Percentile Share of Income Source



CAPITAL GAINS!!!!



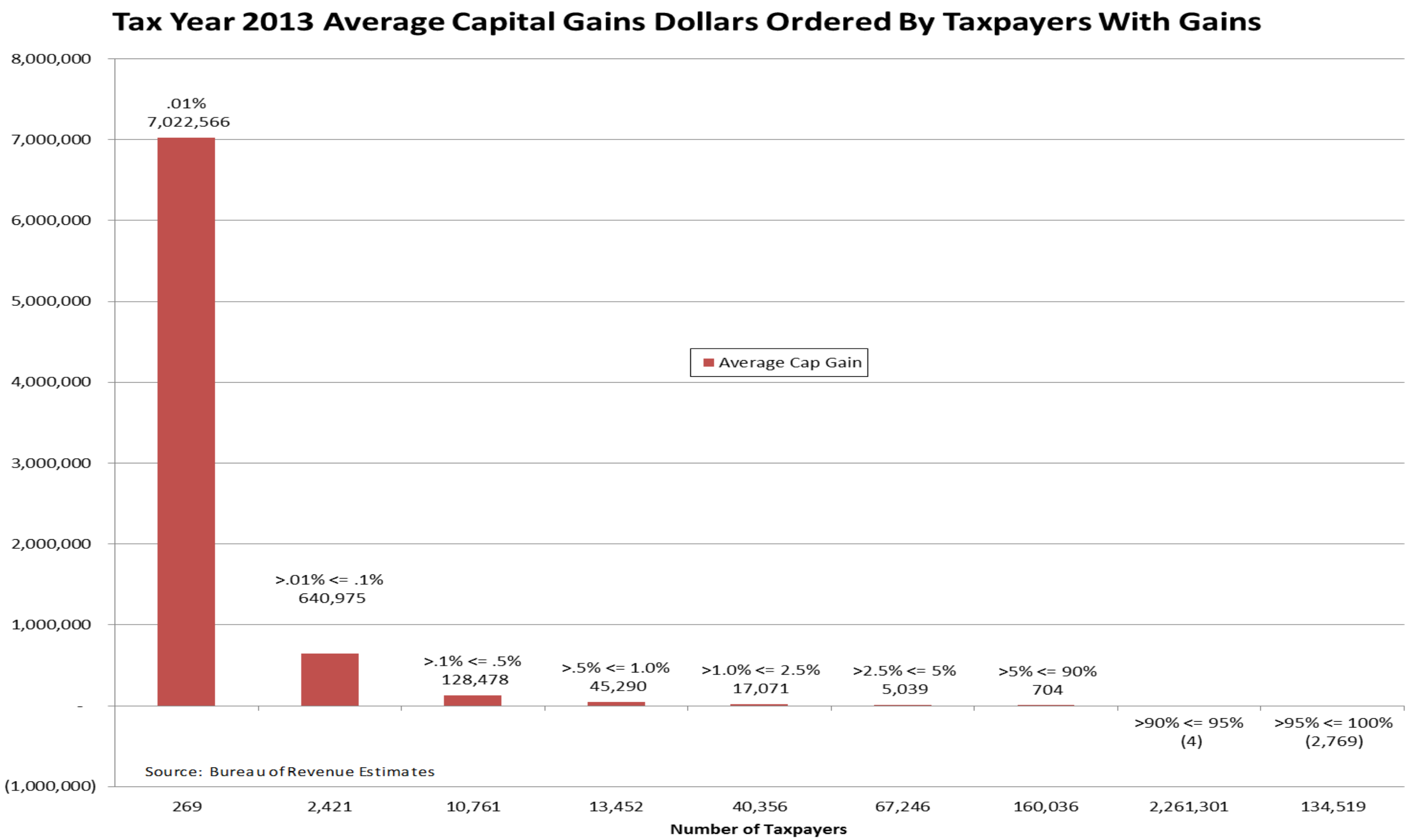
Extreme Concentration in CapGains



Average Data 2009 - 2013

	Avg # TPs	Avg Share	Running Count	Running Share
0.01%	258	41%	258	41%
0.01% - 0.1%	2,327	32%	2,585	73%
0.1% - 0.5%	10,341	22%	12,925	95%
0.5% - 1%	12,926	7%	25,851	102%
All Else	2,559,360	-2%	2,585,212	100%

Extreme Concentration in CapGains



Capital Gains Summary

- Only ~ 5% of the total general fund
- Between 1980 and 2014
  - Average growth was 13.5%
  - Median growth was 19.1%
  - Standard Deviation was 35.9%!!!
    - Therefore 2/3rds of the time gains between +49.0% and -22.0%
    - What about the other 1/3rd??? (rhetorical)

Tax Year	Total Cap Gains $	~ State Tax $
2007	15,614	820
2009	3,729	196
2014	9,508	499
Dollars in millions		

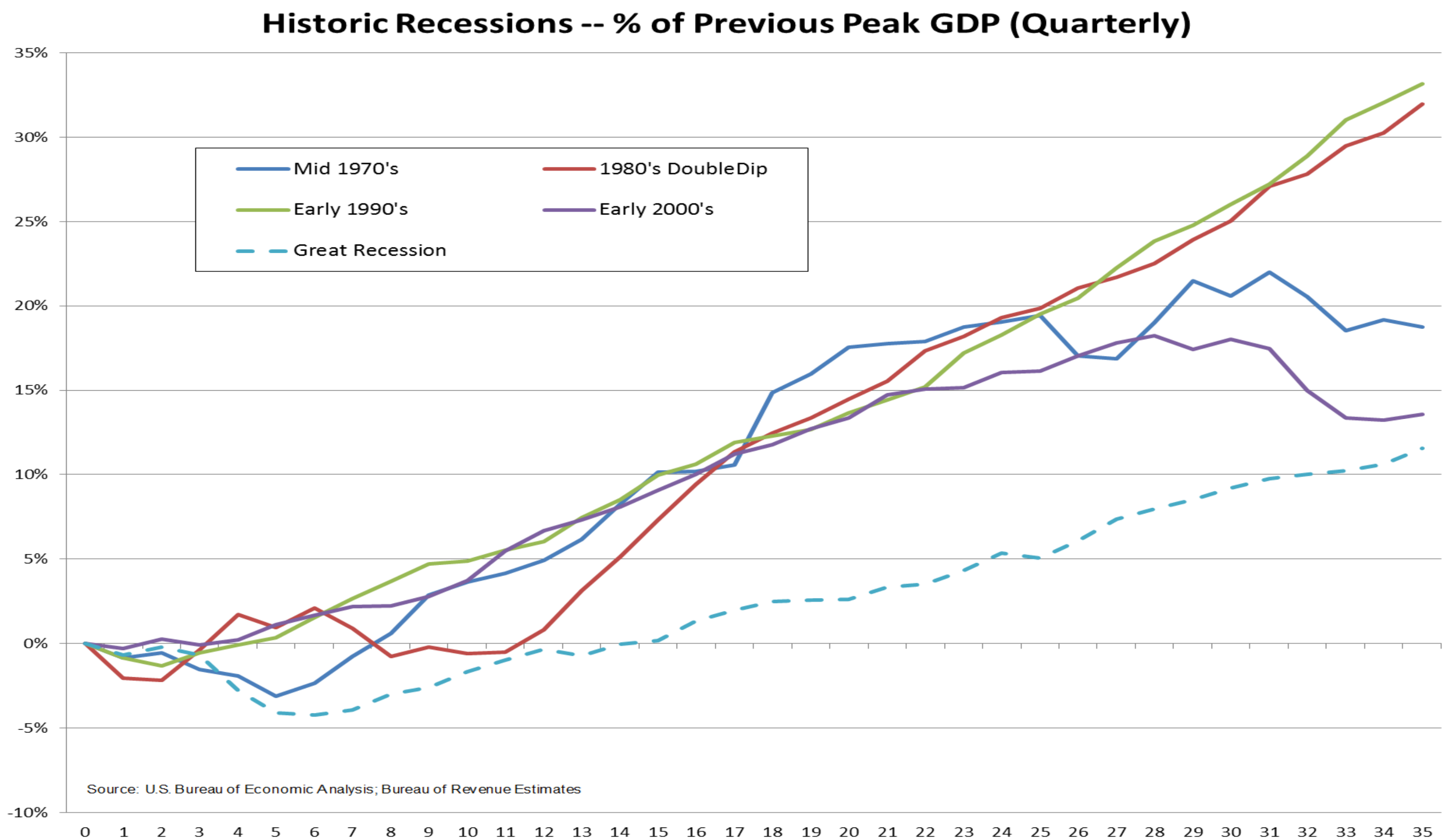
Policy Response

- HB430 & SB306 – Governor's Bills
- HB503 & SB371 – Legislative Bills

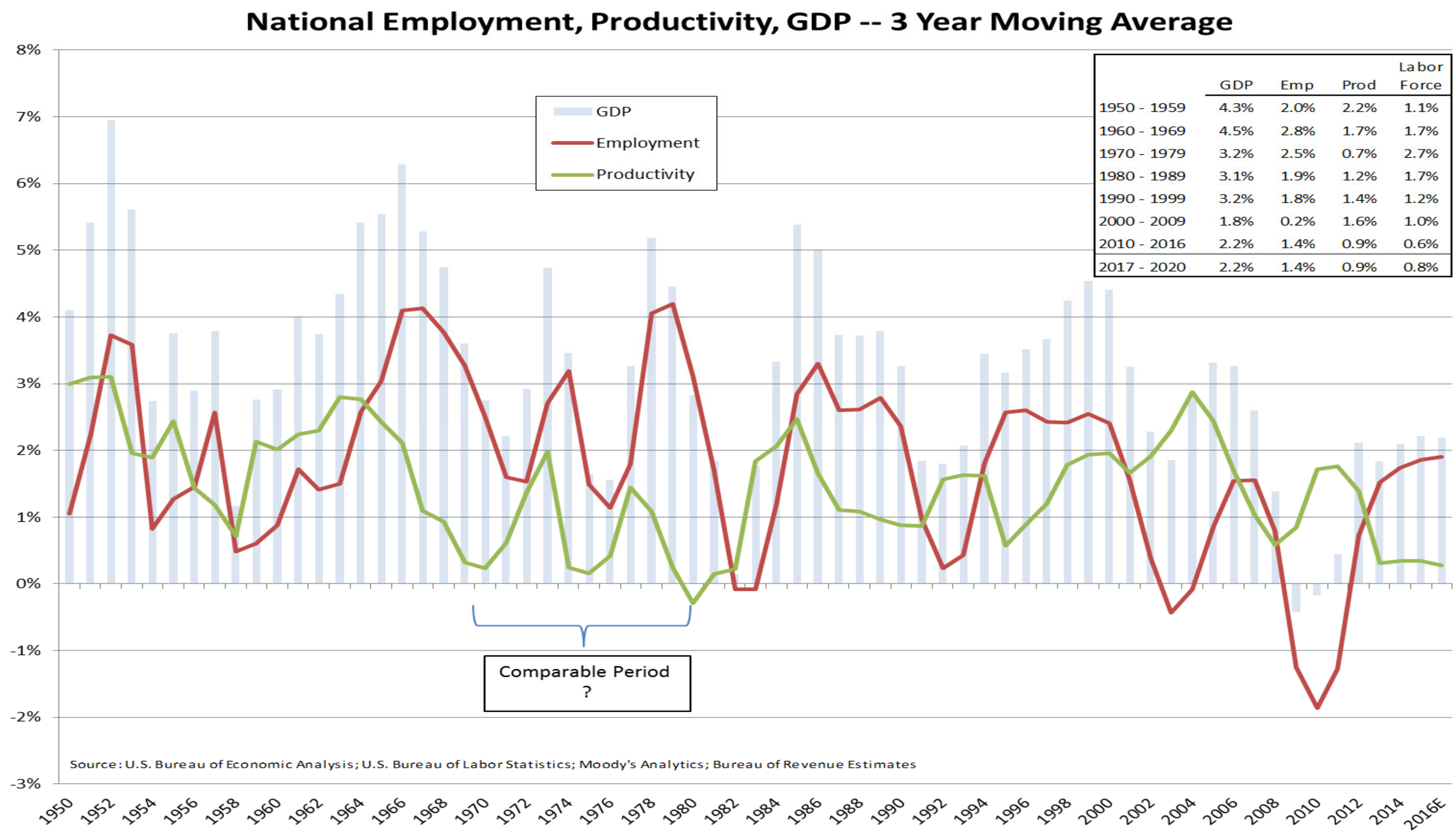
- Policy responses derived from DLS/COM/DBM report in interim found here
    - Report on Revenue Volatility and Approaches to Reduce Risk to the State Budget
- Recommendations
    - Collar non-withholding revenue growth in estimate
    - When collared revenue is exceeded apply to reserve account until adequately funded (10%)
    - After reserve is funded, then apply to unfunded liabilities and pay-go capital

ECONOMIC OUTLOOK

Unprecedented Recovery/Expansion

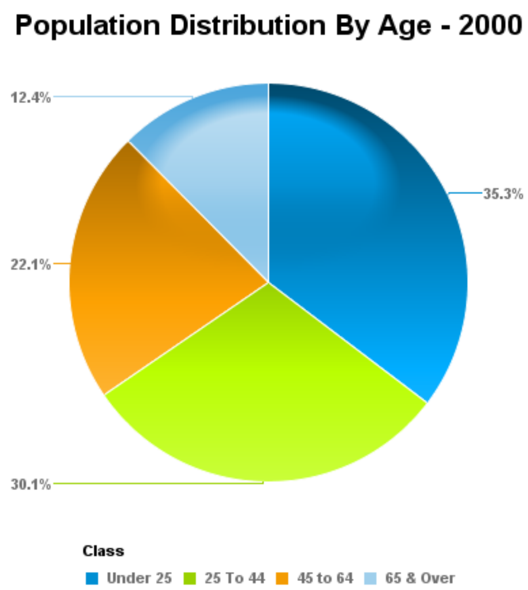


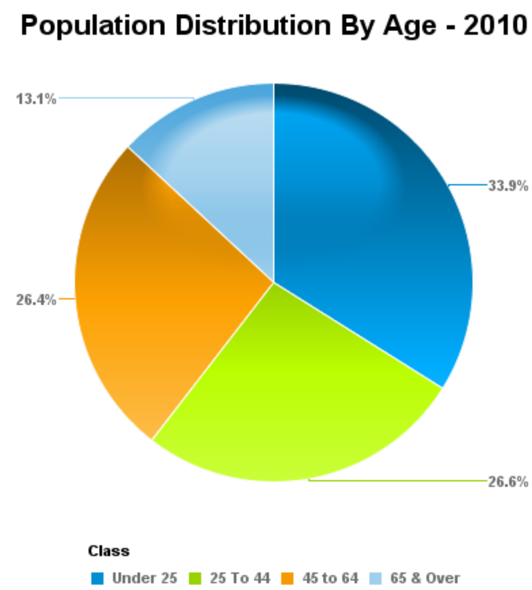
Labor Force Slowing & Productivity Issues

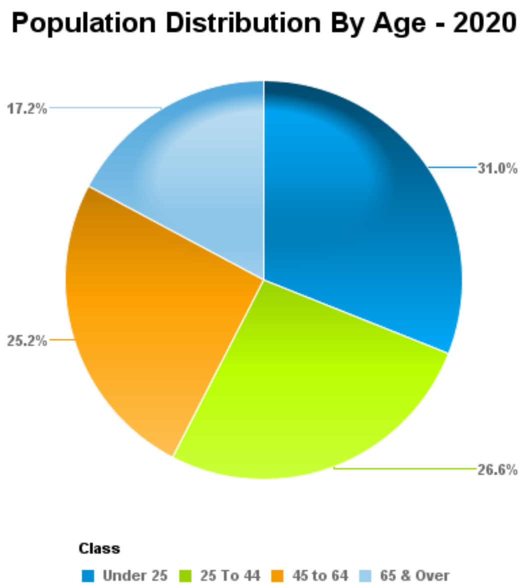


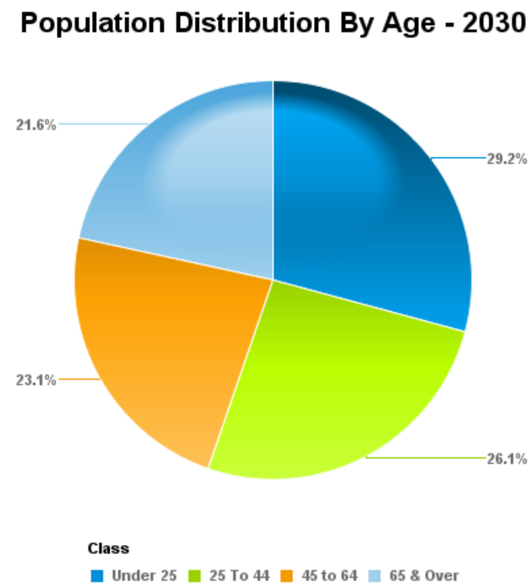
	GDP	Emp	Prod	Labor Force
1950 - 1959	4.3%	2.0%	2.2%	1.1%
1960 - 1969	4.5%	2.8%	1.7%	1.7%
1970 - 1979	3.2%	2.5%	0.7%	2.7%
1980 - 1989	3.1%	1.9%	1.2%	1.7%
1990 - 1999	3.2%	1.8%	1.4%	1.2%
2000 - 2009	1.8%	0.2%	1.6%	1.0%
2010 - 2016	2.2%	1.4%	0.9%	0.6%
2017 - 2020	2.2%	1.4%	0.9%	0.8%

Focus on Demographics



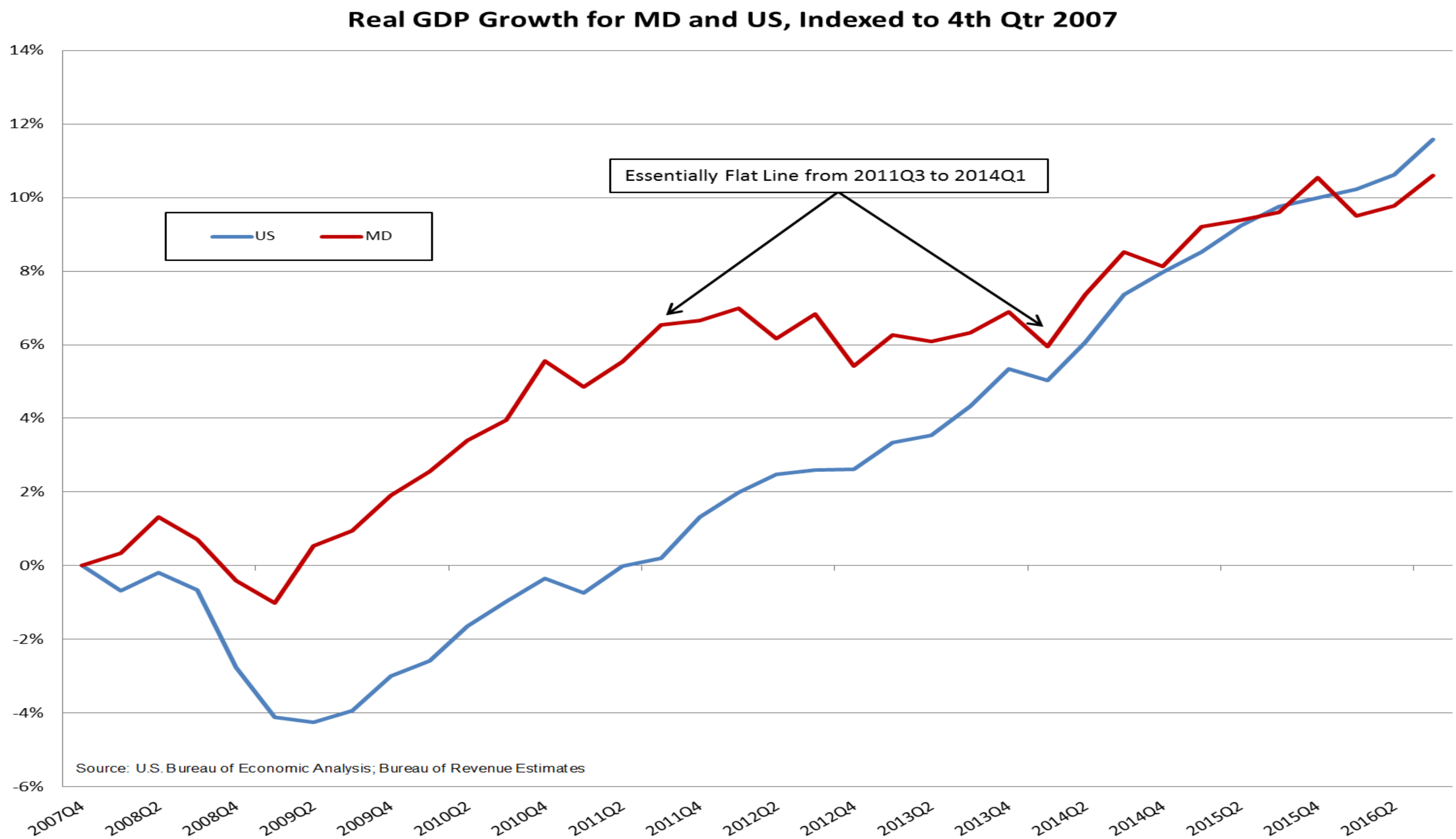




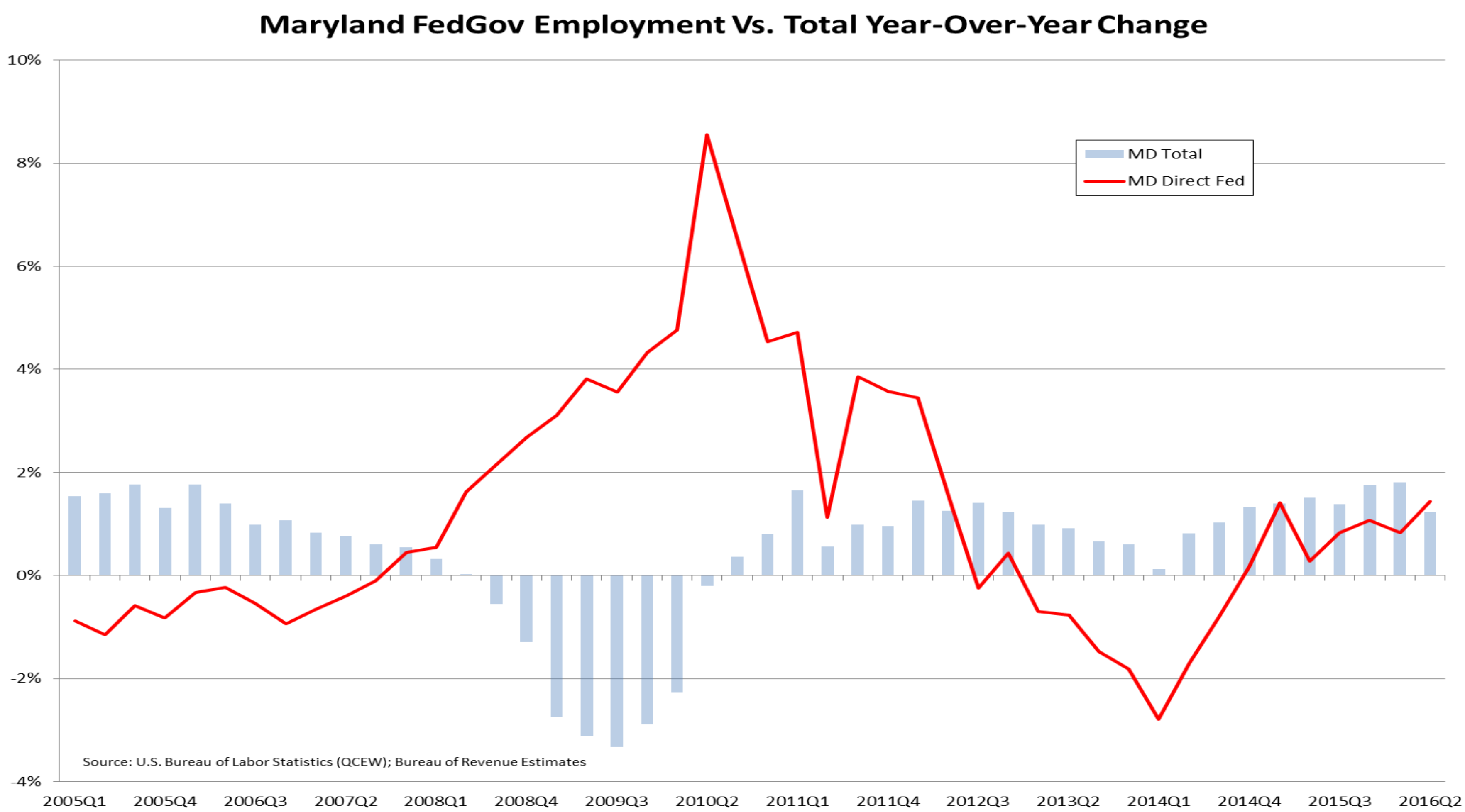


Source: US Census; Moody's Analytics

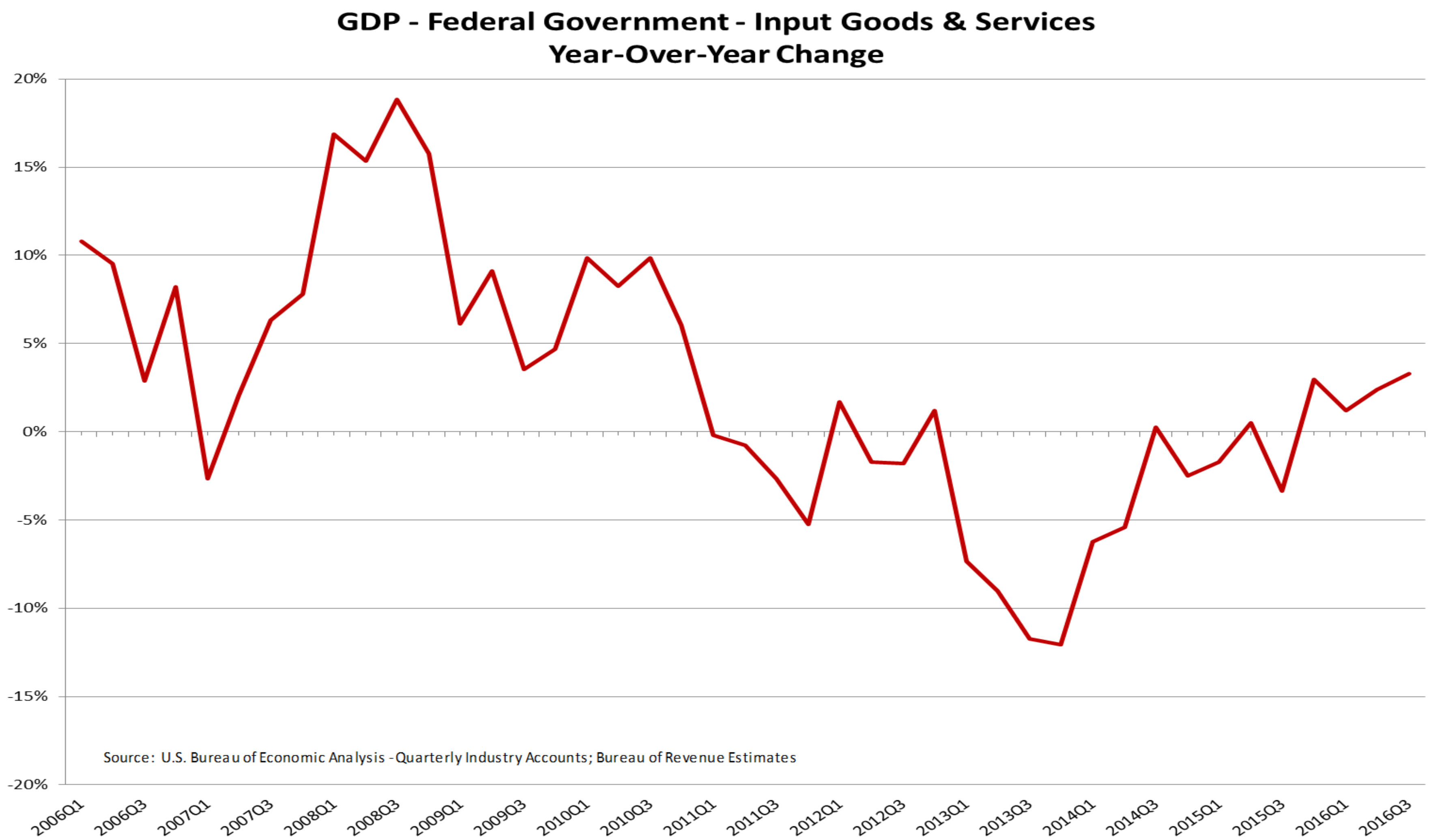
Catching Up to National Growth



Sequester Drag Diminishing – For Now



Private Sector Benefiting As Well



What Impact Will President Trump Have?

Federal Hiring Freeze Information

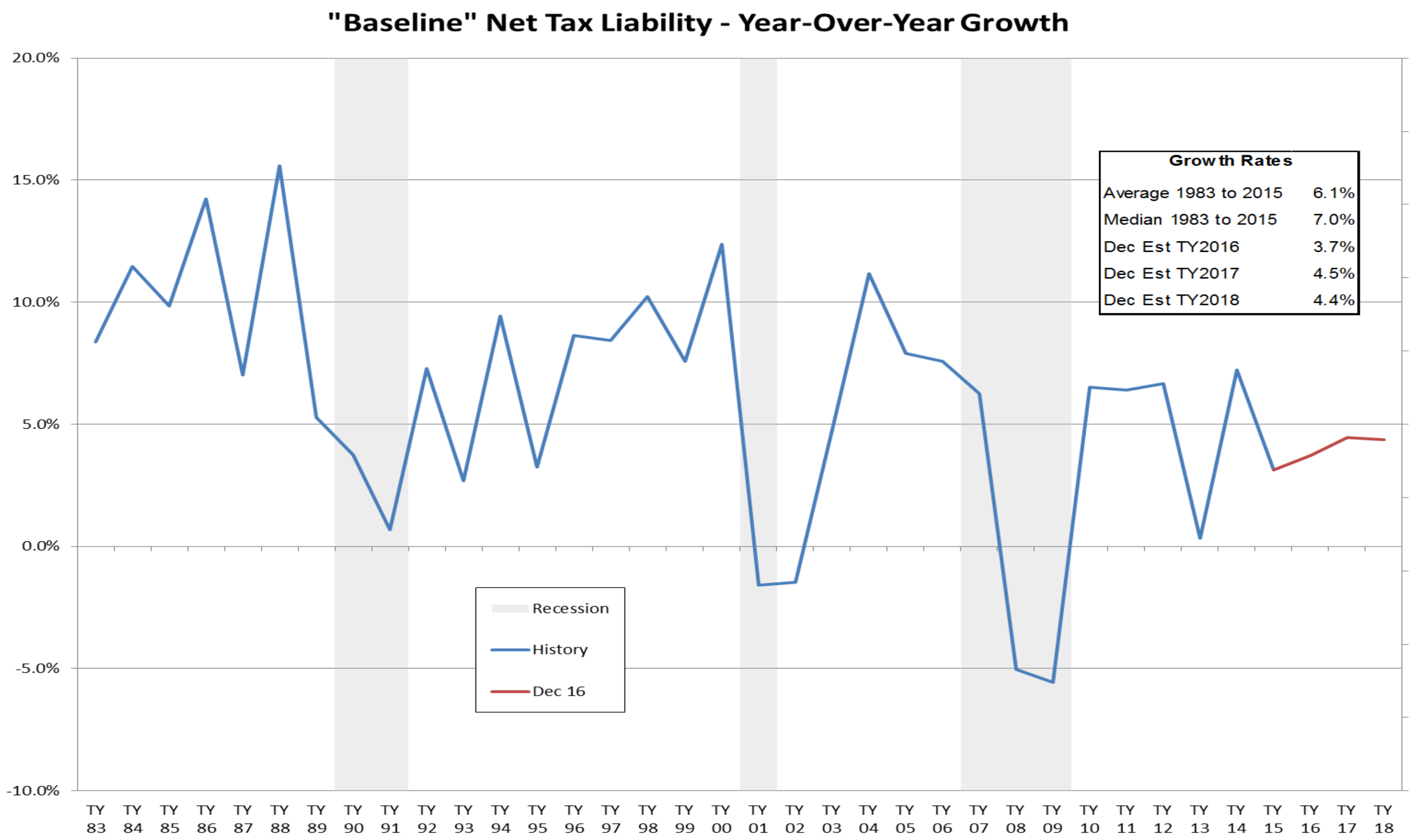
- Used real withholding data to identify federal risks
  - In fiscal year 2016, ~ $1.9 billion (15% of all withholding) was from federal accounts
    - $873 million of that was defense related (7% of all withholding)
    - $1.0 billion of that was civilian related (8% of all withholding)

- 2016Q1 to 2016Q3 civilian withholding increased 4.2%
  - If civilian withholding slowed to -2.0% for a full year, it would shave 0.5% from total annual withholding growth
  - That would cost the general fund ~ $44 million
  - That would be worse than sequester

- Relevant Notes/Thoughts:
  - Impact likely to be gradual as turnover occurs – would take some time to hit a $44 million impact in one year
    - Possible to have little impact this current fiscal year and a portion of the $44 million in next year
  - Demographics not in State's factor as federal workforce is presumably baby boomer heavy
  - Very likely to have offsetting impacts from increased defense spending or private sector outsourcing

- *This is not an official estimate – it is working information*

Subdued Receipts Relative to Pre-GR



Thank You

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