

Marc Elrich
County Executive




Michael J. Coveyou
Director

DEPARTMENT OF FINANCE

MEMORANDUM

February 15, 2022

TO: Marc Elrich, County Executive

FROM: Michael Coveyou, Director 
Department of Finance

SUBJECT: Revenue Estimating Group Report for February 15, 2022

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 includes a review of tax collections for the second quarter of fiscal year 2022 ended December 31, and revised economic assumptions to be used to develop the revenue forecast for the Fiscal Year 2023 ("FY23") recommended budget that you will transmit to Council on March 15, 2022.

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. As described in the previous transmittal letter, the revenue forecast for the recommended budget was not expected to be ready by February 15, however, the economic assumptions that will be used to develop the revenue forecast are included herein. In the May 15th report we expect to review the FY23 revenue forecast and revenue collections through the third quarter of fiscal year 2022. 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 Administrative 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

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**Montgomery County Maryland Revenue Estimating Group
Quarterly Report
February 15, 2022**

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 February 2022 Report is the third report from the Group. It covers revenue collections during the period ended December 31, 2021 and preliminary economic assumptions to be used to develop the revenue forecast for the Fiscal Year 2023 (“FY23”) recommended budget that the County Executive will transmit to Council on March 15. Due to the timing of income tax distributions from the State, this report does not revise the revenue estimates from the December 2021 report. The Group plans to meet and review the revenue estimates prior to the Executive’s recommended budget on March 15.

Executive Summary

- Fiscal year 2022 (“FY22”) tax collections for the second quarter, which ended on December 31, 2021, were on target with the December Fiscal Plan, taking into account expected seasonality and recovery trajectories from pandemic lows.
- Property tax collections were 92.4% of the December Fiscal Plan annual estimate.
- Income tax collections were 32.5% of the December Fiscal Plan annual estimate. Income tax collections are higher in the second half of a fiscal year and are expected to meet the December Fiscal Plan annual estimate.
- Economic conditions have not changed materially from the December 15, 2021 report except as described below, including multiple Federal Reserve Bank increases in the federal funds rate and volatility in the capital markets.
- Economic assumptions to be used to develop the FY23 revenue forecast are similar to those used for the December Fiscal Plan.
- There continue to be risks to the economy including higher inflation, more rapid and higher fed rate increases, a weaker real estate market and major COVID-19 outbreaks that result in dramatic drops in economic activity.

Year to Date for the Period Ended December 31, 2021

The second quarter of FY22 ended on December 31, 2021. The Group reviewed the available cash-based revenue collection information for the second quarter, including data from the Montgomery County

Department of Finance, Division of Treasury, and the Maryland Office of the Comptroller. Property and income taxes are the primary tax revenues for the County, accounting for approximately 88% of tax revenues in the December Fiscal Plan. As shown in Table #1, property taxes collected through December 31 are \$1753.0 million, 92% of the December Fiscal Plan annual estimate. Additional property taxes are expected to be received during the remainder of FY22 as late payments received after December 31 are processed, new construction is billed during the first half of calendar year 2022, personal property taxes are received, penalties and interest are collected, and the annual tax sale is completed in June 2022. Income taxes collected through December 31 totaled \$553.1 million, 33% of the December Fiscal Plan annual estimate.¹ Income tax revenues are received from the State of Maryland on a schedule that tends to have larger distributions in the second half of the fiscal year, with February tending to be the largest distribution in this period and it is also one of the largest distributions of the year. Due to this schedule, it is not unusual for income tax revenues to be below 50% of the December Fiscal Plan annual estimate as of December 31st.

Table #1 PROPERTY AND INCOME TAX COLLECTIONS

Property and Income Taxes Collected through December 31, 2021

	FY22 YTD 12/31	FY22 Budget	FY22 Dec Fiscal Plan Update	% of Budget	% of Dec Fiscal Plan Update
Property taxes	1,753,018,917	1,884,667,305	1,898,080,584	93.0%	92.4%
Income taxes*	553,062,409	1,708,841,800	1,703,300,950	32.4%	32.5%

source: Division of Treasury, YTD collections are on a cash basis

*The budget and fiscal plan reflect income taxes 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 tax revenues collected through the end of the second quarter are on target taking into account expected seasonality and recovery trajectories from pandemic lows. As shown in Table #2, fuel/energy tax and telephone tax cash-based collections were approximately 49% of the annual December Fiscal Plan estimates. At the end of the second quarter, recordation and transfer tax collections were approximately 65% of the higher annual December Fiscal Plan estimates. Due to the strength of the recordation and transfer taxes collected in the first quarter of FY22 and the economic outlook for the remainder of the fiscal year, estimated recordation and transfer taxes were increased in the December Fiscal Plan. These two taxes are strongly related to real estate market activity and tend to be seasonal with higher activity in warmer months and slower activity in winter months. As noted in the December 15, 2021 Revenue Estimating Group Report, the December Fiscal Plan considered the very strong first quarter collections in FY22 but assumed a moderation in activity through the remaining months of the fiscal year. Hotel/motel tax collections are approximately 54% of the annual budget, but only 38% of the December Fiscal Plan annual estimate. In December the annual estimate was increased from \$11.8

¹ The budget and fiscal plan reflect income taxes on a modified accrual basis on an August through July fiscal year. The income taxes collected through December 31 reflect the 5 months from August through December.

million to \$16.9 million due to the accelerating monthly trend of revenues and the economic outlook for the remainder of the fiscal year. Hotel/motel taxes tend to have seasonal variations, with winter months typically having the lowest revenues.

Table #2 SELECTED TAX REVENUE COLLECTIONS

Selected Tax Revenues Collected through December 31, 2021

	FY22 YTD 12/31	FY22 Budget	FY22 Dec Fiscal Plan Update	% of Budget	% of Dec Fiscal Plan Update
Fuel Energy Tax Revenue	85,735,910	175,651,251	188,692,815	48.8%	45.4%
Recordation Tax - General Fund	44,568,043	52,665,091	69,294,352	84.6%	64.3%
Transfer Tax	94,256,313	117,155,198	144,599,748	80.5%	65.2%
Telephone Tax	26,812,473	55,072,985	54,713,330	48.7%	49.0%
Hotel/Motel Tax	6,433,197	11,837,621	16,978,230	54.3%	37.9%

source: Division of Treasury, YTD collections are on a cash basis

Economic Conditions

The economic assumptions discussed in this Group's December 15, 2021 report and upon which the December Fiscal Plan revisions were based, are tracking close to expectations. We previously noted the omicron variant of COVID-19 as an economic risk factor that had yet to be specifically incorporated into the economic assumptions. In the two months that have elapsed since the Fiscal Plan was updated, some economic data for the now completed calendar year 2021 has become available that impacts the economic assumptions. Looking forward to FY23 which will begin on July 1, 2022, the economic assumptions that will be used to develop the County Executive's Recommended Budget will change slightly from the prior assumptions to reflect some revised expectations including:

- i) COVID-19 may become endemic, with the risk of potential spikes
- ii) The Federal Reserve will increase the fed funds rate by .25% at least 3-5 times in calendar year 2022, some of which will occur in FY23
- iii) Inflation will moderate after 2022 as supply chain disruptions abate
- iv) January volatility in the capital markets may translate into a decrease in stock prices
- v) Home sales and prices will continue to be strong, but volume and prices will moderate

These changes in expectations should not leave the impression that there are no risks to the County economy. The level of volatility in the economy is currently below that experienced at the start of COVID-19 in early 2020, but volatility and the risk of sharp turns in economic activity are still higher than had been the case pre-COVID.

As shown in Table #3 below, the 2023 assumption for resident employment, a key driver of the County's income tax revenues, is slightly lower than in December. This change reflects updated data for recently completed 2021 and updates for 2022 and future years built off the lower 2021 base. The annual growth rates for resident employment remain approximately the same as in the December Fiscal Plan, slowing

in each year after 2022. Total personal income² for 2023 is lower than in December, reflecting revisions to 2021 following the end of the year and forecasts for 2022 and future years built off that lower base. The wage and salary income component, which accounts for approximately 48% of the County's total personal income, is higher than the December forecast also building off higher forecasts for prior years, while the non-wage components are slightly lower reflecting updated forecasts for transfer payments following the end of many federal and state stimulus programs and lower expectations for dividends, interest and rental income. Home sales are expected to grow at a slightly slower rate because of higher prices and low supply. Additionally, affordability may be negatively impacted by increased mortgage rates that will likely occur as the Federal Reserve begins to increase the fed funds rate.

Table #3 ECONOMIC ASSUMPTIONS

FY23 Budget - Key Economic Assumptions

	2021 (est.)	2022 (est.)	2023 forecast	Percentage change Year-Over-Year						
				2022	2023	2024	2025	2026	2027	2028
Resident Employment	510,548	529,137	540,819	3.6	2.2	1.5	1.0	0.8	0.8	0.7
December 2021	511,335	530,472	541,963	3.7	2.2	1.4	0.9	0.8	0.8	0.7
Total Personal Income (\$mm)	99,813	102,528	107,507	6.0	2.7	4.9	4.8	4.8	4.7	4.5
December 2021	105,324	107,033	111,971	1.6	4.6	4.9	4.9	4.3	4.2	4.3
Median Existing Home Sales (thousands)	13.807	13.143	13.340	-3.3	1.5	10.7	-3.2	-8.9	-5.9	0.0
December 2021	13.572	13.125	13.715	-3.3	4.5	5.3	-5.0	-7.4	-4.8	1.8
Median Sales Prices (\$)	547,429	580,710	598,526	6.1	3.1	2.4	2.2	1.7	1.3	1.3
December 2021	557,225	569,957	581,437	2.3	2.0	1.7	1.9	2.0	1.7	1.7
					Forecast (%)					
CPI-U Washington MSA (%)	4.0	4.7	2.3			2.3	2.4	2.4	2.2	2.2
December 2021	2.1	4.0	3.3			2.4	2.4	2.4	2.3	2.2

Risks to the Economic Assumptions for 2023

Deviations from the economic assumptions that will support the revenue forecast for the FY23 recommended budget could have an impact, either positive or negative, on revenues. While there are many economic variables that are used to develop the revenue forecast, those that effect property and income taxes are the most significant due to the budget's dependence on these two major tax revenues. Some of the largest risks to the forecast include higher inflation, more rapid and/or higher fed rate increases, a weaker real estate and capital markets and significant COVID-19 outbreaks that result in dramatic drops in economic activity.

² Total personal income includes i) wage and salary income ii) proprietor's income iii) dividends, interest and rent and iv) transfer payments