County of Fairfax, Virginia

Financial Forecast

This section includes:

FY 2009
Adopted Budget Plan

Financial Forecast Summary

The following forecast provides preliminary revenue and disbursement projections for FY 2010 through FY 2012. The forecast assumes no change in the Real Estate Tax rate of $0.92 per $100 of assessed value. Economic assumptions used to develop the forecast are detailed below. The current forecast projects that County General Fund revenue in 2010 will decline 3.4 percent, primarily as a result of an estimated 10 percent decrease in residential assessments. Revenue growth is projected to rise less than 1 percent in FY 2011 and less than 2.0 percent in FY 2012. These modest rates of growth are due to a continued decline in residential real estate property assessments in FY 2011 and no change in residential values in FY 2012. Excluding Real Estate Tax revenue, all other categories are anticipated to increase 1.7 percent in FY 2010, 1.9 percent in FY 2011 and 2.2 percent in FY 2012.

Assuming funding for basic compensation and inflationary adjustments as well as support of County obligations in debt service, Metro and other transfers, County disbursements are anticipated to require funding increases of 4 to 5 percent annually. As a result, without changes in spending and/or revenue enhancements, this forecast indicates that shortfalls of $350 million would occur in each year.

Revenue Forecast

Overall Economic Assumptions

There is much uncertainty regarding the length and extent of the current economic slowdown. National real economic growth of 0.6 percent in the fourth quarter of 2007 was the weakest since 2002. The economy faired just slightly better in the first quarter of 2008, advancing 0.9 percent adjusting for inflation. Because Real Estate Tax revenue comprises over 62 percent of total County General Fund revenues and residential real estate makes up nearly three quarters of the total real estate base, assumptions as to when the housing market and general economy turn around is critical to this forecast. Economic projections for the national and local economies were reviewed from a variety of sources in the development of these revenue estimates such as the Blue Chip Economic Forecasts that incorporates economic projections from a panel of approximately 50 forecasters, Kiplinger, Global Insight, National City and the National Association of Realtors. Fairfax County specific projections are obtained from Moody's Economy.com and George Mason University's Center for Regional Analysis.

Moody's Economy.com predicts that Fairfax County's economy will be at a standstill in 2008 and experience modest growth in 2009 through 2012. Dr. Stephen Fuller from the Center for Regional Analysis forecasts that the County's economy will expand in 2008 albeit at the slowest pace since 2002. Dr. Fuller predicts moderate growth through the remainder of the forecast period. Job growth is expected to slow considerably in 2008 on the national and local level. Economy.com predicts slight job gains in Fairfax County for 2008 and 2009. Job growth is projected to be strong in 2010 as the economy improves and proposed facility changes from Base Realignment and Closure (BRAC) should be well underway. In August 2007, the Army signed a decision that authorizes more than 4,200 jobs at Fort Belvoir and 8,500 at the Engineering Proving Ground by 2011.

Residential Housing Market

The slowdown in the County's residential housing market which began in mid-2006 worsened in 2007. The number of homes sold dropped to 13,557 from 16,314 in 2006. Based on Metropolitan Regional Information System (MRIS) data, the overall average sales price fell 0.2 from 2006. While this information provides a gauge of the housing market, changes in the average price are affected by the mix of homes sold during the year. Another measure of the housing market indicates a steeper decline for the area. The S&P Case-Shiller Home Price Index for Fairfax County showed a decline in the prices for existing single family homes of over 7 percent compared to 2006. This index uses a repeat sales price technique that matches each price change of the same home over a 20-year period.

The number of homes for sale stabilized in 2007. On average, there were approximately 7,300 homes for sale each month of 2006 and 2007. This level represents over twice as many homes for sale compared to 2005. On average 7,800 homes were for sale in the first four months of 2008. As of April 2008, there was estimated to be an 8-month supply of homes on the market. It continues to take longer to sell a house in the County. In 2007, a home in Fairfax County was on the market an average of 88 days according to MRIS, compared to 63 days in 2006 and to just 21 days in 2005. Homes that sold in April 2008 were on the market for 107 days versus 84 day in April 2007.

A record 4,527 homes were foreclosed in Fairfax County in CY 2007, up from just 198 properties in 2005 and nearly eight times the number foreclosed in 2006. Based on market activity in 2007, residential assessments fell 3.38 percent in FY 2009. Foreclosures were not a dominate factor in the market in 2007 but have become a larger share of total homes sold. During the first quarter of 2007, foreclosures comprised just 9.5 percent of total homes sold, but by the fourth quarter of 2007 foreclosures made up nearly 42 percent of homes sold in the County. Through April 2008, the 4,922 foreclosures already exceed the total foreclosures of 2007. Consequently, distress sales and foreclosures will have a much greater impact on residential assessments beginning in FY 2010 and potentially lingering in FY 2011. As such, this forecast includes a projected drop of 10.0 percent in the value of residential property in FY 2010 and a further decline of 2.0 percent in FY 2011. Assessments are projected to stabilize in FY 2012. Mortgage interest rates are expected to remain relatively low on a historical basis throughout the forecast period and are not expected to affect the affordability of homes.

Nonresidential Real Estate

The nonresidential real estate market began to soften in 2007. Leasing activity in 2007 was the lowest in five years, down 13 percent from 2006. Nearly 2.5 million square feet of office space was delivered in 2007 bringing the total County inventory to 107.2 million square feet. Due to the additional office space, the County's direct office vacancy rose from the year-end 2006 rate of 7.7 percent to 9.2 percent at year-end 2007. Including sublet space, the 2007 overall office vacancy rate was 10.9 percent, up 1.7 percentage points over the 9.2 percent at year-end 2006. An additional 4.3 million square feet of new space in 26 buildings was under construction at the end of 2007 and the office vacancy rate is likely to rise further as this space comes on-line. According to the Economic Development Authority (EDA), 14 of the 26 buildings under construction were 100 percent speculative. EDA anticipates that new building starts will be limited to build-to-suit, or pre-leased projected until most of the current speculative building is absorbed. A rise in vacancy rates and an abundance of office space in Fairfax County and the Northern Virginia area will thwart the growth in nonresidential property values over the forecast period. Nonresidential values are projected to experience no change in value in FY 2010, after rising 7.00 in FY 2009. Nonresidential values are expected to advance at a 1.00 percent pace in FY 2011 and 3.00 percent in FY 2012 as current office space is absorbed and vacancy rates decline.

New Construction

The Real Estate Tax base will also be impacted by new construction in the County. Normal Growth or new construction increased the tax base by 1.53 percent in FY 2009. Building permits issued, an indicator of future construction, have declined approximately 23 percent during the first ten months of FY 2008 compared to the same time the prior year. Residential construction is projected to slow during the forecast period resulting from low demand based on declining job growth and the current oversupply of homes on the market. There are 25 office buildings that are scheduled to be completed in calendar year 2008 affecting the nonresidential growth component of the FY 2010 real estate base. Office construction has already slowed and nonresidential growth is projected to be lower in FY 2011 and FY 2012. At year-end 2007, only one building with approximately 300,000 square feet of space was under construction with completion expected in 2009 (FY 2011). Overall, increases to the Real Estate Tax base due to new construction are projected to be 1.0 percent in FY 2010 and 0.90 percent in FY 2011 and FY 2012.

Total Real Estate

In FY 2009, the total Real Estate Tax base rose by a modest 0.51 percent as the increases in nonresidential property values and the impact of new construction more than made up for the decrease in residential property values. In FY 2010, the total Real Estate Tax base is expected to drop 6.50 percent due to the projected significant decline in residential assessments and no growth in nonresidential property values. The real estate base is anticipated to decline 0.30 percent in FY 2011. As the housing market stabilizes, the overall real estate tax base is projected to rise 1.75 percent in FY 2012.

Personal Property Taxes

Personal Property Tax revenue, which represents 15.5 percent of total General Fund revenue, is anticipated to experience a drop of 0.77 percent in FY 2009 primarily due to a decline in vehicle purchases The Virginia Automobile Dealers Association reported that new model vehicle registrations in Fairfax County fell 8.8 percent in 2007. Consumers are less able to finance vehicles with home equity lines of credit or mortgage refinancing due to the housing downturn. Nationwide, fewer vehicle sales are projected for calendar year 2008 by the Blue Chip Economic Forecast. In addition, the National Automobile Dealers Association's economist, Paul Taylor has indicated that Northern Virginia could see a drop of 1 percent in vehicle sales in calendar year 2008 which will impact FY 2010 receipts. Personal Property Tax revenues are expected to decline 0.5 percent in FY 2010. As the economy improves, slight growth is anticipated in FY 2011 of 0.75 percent and 1.50 percent in FY 2012.

Other Major Revenue Categories

Business, Professional and Occupational License revenue is projected to increase 4.5 percent in FY 2009 and FY 2010. Growth in FY 2011 is expected to rise to 5.0 percent based on employment growth during calendar year 2010 and remain at 5.0 percent in FY 2012. Sales Tax receipts are projected to rise 2.5 percent in FY 2010 and 3.0 percent in FY 2011 and FY 2012 based on Economy.com's estimated growth in Fairfax County retail sales. Recordation and Deed of Conveyance taxes, which are paid for recording deeds are anticipated to remain at the FY 2009 level for the duration of the forecast period.

Revenue from Land Development Services Building and Permit fee revenue is projected to fall over 12 percent in FY 2008 based on current collection trends. Construction activity is anticipated to decline in FY 2009, and revenue is projected to decrease 1.0 percent. Construction activity and revenue are forecasted to stabilize in FY 2010 and rise a modest 1.0 percent in FY 2011 and FY 2012. Other Permit and Fees and Regulatory Licenses categories are expected to experience modest growth throughout the forecast period.

Since the beginning of 2008, the Federal Reserve has cut the federal funds rate 2.25 percentage points from 4.25 percent to 2.00 percent as of May 2008. The yield earned on County investments is projected to be 1.50 percent in FY 2009. The Fed is expected hold rates steady in the short-term and gradually raise interest rates to keep inflation low. County investments are projected to earn an average annual yield of 2.25 percent in FY 2010 and increase 0.25 percentage points each year to 2.50 percent in FY 2011 and 2.75 percent in FY 2012.

Due to a budget shortfall, the Commonwealth of Virginia significantly reduced funding to localities in FY 2009. Based on preliminary information, the County's funding will be cut $6.0 million in FY 2009 from the Commonwealth's earlier estimates. The level of state funding throughout the forecast is maintained at the reduced FY 2009 level. Revenue from the Federal government is also expected to remain level with FY 2009 throughout the forecast period. Since the majority of the revenue from the state and federal governments are reimbursements associated with expenditure requirements, any additional increase in revenue is expected to be more than offset with expenditure increases. There are several downside risks to this projection. Depending on the timing of the economic recover, the Commonwealth's budget situation could potentially worsen and additional locality cuts may be required. Also, the spending priorities of a new federal administration beginning in 2009 may impact Fairfax County's funding directly and indirectly through federal procurement spending.

Based on the assumptions and estimates detailed above, General Fund revenues are projected to experience a decline of 3.35 percent in FY 2010 and rise just 0.60 percent in FY 2011. As the housing market stabilizes in calendar year 2010, FY 2012 receipts are expected to rise 1.95 percent. Revenue growth rates for individual categories are shown in the following table:

PROJECTED REVENUE GROWTH RATES

Category	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012
Real Estate Tax - Assessment Base	4.15%	0.51%	-6.50%	-0.30%	1.75%
Equalization	2.47%	-1.02%	-7.50%	-1.20%	0.85%
Residential	-0.33%	-3.38%	-10.00%	-2.00%	0.00%
Nonresidential	13.57%	7.00%	0.00%	1.00%	3.00%
Normal Growth	1.68%	1.53%	1.00%	0.90%	0.90%
Personal Property Tax - Current[1]	0.21%	-0.77%	-0.50%	0.75%	1.50%
Local Sales Tax	2.36%	2.34%	2.50%	3.00%	3.00%
Business, Professional and Occupational, License (BPOL) Taxes	4.80%	4.50%	4.50%	5.00%	5.00%
Recordation/Deed of Conveyance	-33.70%	20.59%	0.00%	0.00%	0.00%
Interest Rate Earned on Investments	4.29%	1.50%	2.25%	2.50%	2.75%
Building Plan and Permit Fees	-12.15%	-1.00%	0.00%	1.00%	1.00%
Charges for Services	0.25%	7.28%	2.00%	2.00%	2.00%
State/Federal Revenue[1]	-1.05%	-12.45%	0.00%	0.00%	0.00%
TOTAL REVENUE	**1.55%**	**1.03%**	**-3.35%**	**0.60%**	**1.95%**

[1] The portion of the Personal Property Tax reimbursed by the Commonwealth as a result of the Personal Property Tax Relief Act of 1998 is included in the Personal Property Tax category for the purpose of discussion in this section.

Disbursement Forecast

Anticipated growth in expenditure requirements will exceed revenue projections during the forecast period. Inflationary pressures alone are expected to outstrip revenue growth projections in FY 2010 through FY 2012. Rising health care and energy costs are expected to further strain the County's budget. Budgetary measures will be necessary in order to fund these and other basic costs of operating County government such as pay for performance for employees, market rate adjustments for contractors, and required contributions for retirement. Based on requirements for basic operations including but not limited to compensation and benefits, contract inflationary adjustments, fuel, utilities, and debt service the forecasted disbursement increase for FY 2010 is between 4 and 5 percent. In addition, based on requirements for School operations the transfer to Schools is also forecasted to increase between 4 and 5 percent in FY 2010. The annual increase of 4 to 5 percent for disbursements in combination with the need to fund recurring offsets to the approximately $60 million in one-time reserves utilized to balance the FY 2009 budget and the projected decline in FY 2010 revenue results in a forecasted FY 2010 shortfall of approximately $350 million. The projected shortfalls in FY 2011 and FY 2012 are also projected to be approximately $350 million based on expenditure requirements and projected revenue growth.