Financial Forecast

This section includes:

- *Financial Forecast for FY 2008 and FY 2009 (Page 200)*
- *Revenue Assumptions (Page 200)*
- *Disbursement Assumptions (Page 204)*

Financial Forecast

The following forecast provides preliminary projections for FY 2008 and FY 2009 by maintaining the FY 2007 Advertised Budget Plan Real Estate Tax rate of $0.93 and limiting increases in County expenditures to 5.0 percent and the transfer to the Fairfax County Schools to 6.0 percent as directed by Budget Guidelines for FY 2007 adopted by the Board of Supervisors on August 1, 2005. FY 2007 budget decisions made by the Board of Supervisors that have a future year impact could significantly change the projections for FY 2008 and FY 2009. The current forecast projects County total revenue growth of 5.78 percent in FY 2008 and 5.49 percent in FY 2009. These rates of growth are due to projected moderating increases in real estate property values and other revenue categories. Excluding Real Estate Tax revenue, all other categories are anticipated to increase just 1.6 percent and 1.7 percent in FY 2008 and FY 2009, respectively. This forecast shows surpluses of $59.6 million in FY 2008 and $71.6 million in FY 2009. These balances will provide the Board of Supervisors the flexibility to meet increasing service requirements and to provide real estate tax relief.

Revenue Assumptions

Revenue estimates for FY 2008 and FY 2009 are based on a review of current and projected local and national economic conditions. Most economists expect that the national economy will continue to expand during the forecast period but at more moderate rates than 2005. Real economic growth, as measured by the Gross Domestic Product (GDP), increased 3.5 percent in 2005. In the fourth quarter of 2005; however, economic growth slowed to a rate of just 1.1 percent, the weakest pace in three years. After seesawing during 2005, the Consumer Confidence Index, an indicator of future consumer spending, rose in January to its highest level since June 2002. The U.S. Leading Index of Economic Indicators rose slightly in December 2005. During the year, the Leading Index grew at a 1.9 percent average annual rate, down from 6.2 percent in 2004. The trend in the Leading Index indicates that the national economy should continue to expand but at a modest rate.

Growth in the Fairfax County economy, as measured by real Gross County Product (GCP), slowed in 2005 to 5.2 percent from the 6.2 percent experienced in 2004. Dr. Stephen Fuller, the County's economic advisor, projects lower economic growth in each year 2006 through 2009 as economic forces that fueled robust growth in 2004, such as rapid federal spending, and low interest rates are expected to moderate. Dr. Fuller forecasts that the Fairfax County economy will expand at rates of 4.2 percent and 4.1 percent in 2006 and 2007, respectively. During the forecast period, economic growth is expected to moderate further to 3.8 percent in FY 2008 and 3.7 percent in FY 2009. An estimated 24,000 net new jobs were created in Fairfax County in 2005, down from 27,400 in 2004. Dr. Fuller projects that job creation will continue to slow in 2006 to 22,500 and to 21,000 in 2007. This level of job growth still represents one of the strongest job markets in the nation.

Residential equalization, the reassessment of existing property, increased 20.57 percent in FY 2007, the sixth year of double-digit increases in Fairfax County residential assessments. Since FY 2001, the mean assessed value of a home in Fairfax County has risen approximately 160 percent. The combination of strong job growth fueled by federal government spending, a limited supply of homes and historically low interest rates have all contributed to rising home prices and therefore residential assessments. Recent indicators, however, suggest that the housing market may be cooling. While the average sales price continued to rise over 20 percent, the number of homes sold was down 2,439, or 9.8 percent, in 2005 according to the Northern Virginia Association of Realtors (NVAR). In addition, the number of days that a home is on the market has increased. In December 2005, a home in Fairfax County was on the market for an average of 38 days, up from an average of 20 days for all of 2004.

FY 2008 and FY 2009 FINANCIAL FORECAST
(millions)

	FY 2005 ACTUAL	FY 2006 REVISED	FY 2007 ADVERTISED	FY 2008 FORECAST	FY 2009 FORECAST
Available Beginning Balance	$99.26	$120.36	$0.00	$0.00	$0.00
Reserves Balance	53.08	57.17	61.95	63.65	68.97
REVENUE:					
Real Estate Taxes	$1,637.90	$1,770.77	$1,978.88	$2,149.58	$2,318.97
Personal Property Taxes[1]	473.93	492.35	523.08	523.08	523.08
Other Local Taxes	463.17	488.49	506.19	518.62	531.82
Permits, Fees, and Licenses	27.96	32.11	33.55	34.22	34.90
Fines and Forfeitures	15.52	14.97	15.24	15.55	15.86
Revenue from Use of Money/Property	30.20	65.08	70.69	76.67	84.02
Charges for Services	47.54	52.72	55.57	56.68	57.81
Revenue from the Commonwealth[1]	83.91	82.80	85.00	85.54	86.10
Revenue from the Federal Govt.	46.02	44.04	44.05	44.05	44.05
Recovered Costs/Other Revenue	7.25	6.82	7.21	7.21	7.21
TOTAL REVENUE	$2,833.40	$3,050.16	$3,319.45	$3,511.19	$3,703.83
TRANSFERS IN	1.67	2.60	2.41	2.47	2.53
TOTAL RECEIPTS	$2,835.07	$3,052.76	$3,321.86	$3,513.66	$3,706.36
TOTAL AVAILABLE	**$2,987.41**	**$3,230.29**	**$3,383.81**	**$3,577.31**	**$3,775.33**
DIRECT EXPENDITURES:					
Personnel Services	$552.87	$625.24	$670.71	$704.24	$739.45
Operating Expenses	334.70	358.40	344.43	361.66	379.74
Worked Performed for Others	(40.73)	(41.23)	(42.65)	(44.79)	(47.03)
Capital Equipment	5.59	4.14	3.08	3.23	3.39
Fringe Benefits	152.98	176.48	190.99	200.54	210.56
TOTAL DIRECT EXPENDITURES	**$1,005.42**	**$1,123.03**	**$1,166.55**	**$1,224.88**	**$1,286.12**
TRANSFERS OUT:					
Schools	$1,322.37	$1,431.34	$1,517.22	$1,608.25	$1,704.75
G O Debt (County)	98.72	98.72	112.81	119.05	126.65
G O Debt (Schools)	126.53	130.28	142.69	157.80	161.20
CSB	82.07	90.98	96.31	101.12	106.18
Metro	18.14	21.32	21.32	24.51	28.19
Paydown Construction	60.58	41.11	16.15	45.00	45.00
County Transit	21.36	24.15	30.70	32.23	33.84
Other Transfers	51.66	70.45	62.74	65.87	69.17
Stormwater Management Program[2]	0.00	17.90	0.00	0.00	0.00
Housing Flexibility Fund[2]	0.00	17.90	0.00	0.00	0.00
Information Technology	11.42	15.78	16.04	30.00	30.00
Revenue Stabilization	11.62	14.60	0.00	0.00	0.00
Transportation Requirements	0.00	0.00	0.00	20.00	20.00
Increased Utility/Energy Costs	0.00	0.00	0.00	20.00	20.00
TOTAL TRANSFERS OUT	$1,804.46	$1,974.52	$2,015.96	$2,223.84	$2,344.97
TOTAL DISBURSEMENTS	**$2,809.88**	**$3,097.54**	**$3,182.51**	**$3,448.72**	**$3,631.10**
ENDING BALANCE	$177.53	$132.75	$201.29	$128.59	$144.23
Managed Reserve	57.17	61.95	63.65	68.97	72.62
Other Reserves[3]	35.52	70.80	137.64	0.00	0.00
TOTAL AVAILABLE	**$84.84**	**$0.00**	**$0.00**	**$59.61**	**$71.61**

[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.

[2]As of the FY 2007 Advertised Budget Plan, one penny of the Real Estate Tax rate dedicated to these funds will be reflected as revenue in the funds rather than as a transfer from the General Fund.

[3]For more information on Other Reserves, see the FY 2007 Advertised General Fund Statement in the Financial, Statistical and Summary Tables section of this document.

A review of various independent analyses of the Washington Area housing market indicates that the cooling of the housing market is expected to continue. By comparing home prices to incomes, the Local Market Monitor estimated that homes in the Washington Area are overvalued by 37 percent. This is more than double the estimate made last year that indicated the area was 17 percent overvalued. An analysis of the national housing market by National City Corporation and Global Insight agreed that Washington area home prices are overvalued. In their report, *House Prices in America* it was noted "If home prices are overvalued then, by definition, the risk of a price correction is high." A market risk index, published by PMI Mortgage Insurance Company in January 2006, estimates that the Washington Metropolitan Area has a 34.5 percent chance of experiencing home price declines in the next two years. Fiserv Lending Solutions goes so far as to predict a price decline of 1.7 percent in 2006 for the metro area. Analysis by the National Association of Realtors (NAR); however, contradicts this conclusion. In a November 2005 report, *Home Price Analysis for Washington-Arlington-Alexandria*, NAR indicated that due to strong job growth and a limited supply of homes, there is little danger of a housing bust in the area. Local economists and executives that follow the Washington Metropolitan Area were surveyed in February 2006 by *The Washington Post*. Estimates of changes in single family home prices in 2006 varied considerably ranging from -8.3 percent to +13.3 percent. The median of the projections was just 4.6 percent.

Based on current statistics that show a cooling of the housing market and the analyses noted above, staff has been cautious in the projection of home price appreciation in 2006 and 2007 which will impact Real Estate Tax revenue in FY 2008 and FY 2009. The Financial Forecast assumes that residential equalization, the reassessment of existing property, will increase at rates of 7.00 percent in FY 2008 and 6.50 percent in FY 2009. This is down from 20.57 percent in FY 2007.

The nonresidential real estate market continued to improve in 2005. During the first half of 2005, 4.9 million square feet of office space was leased, down from the 5.3 million square feet leased during the last half of 2004 but demand for office space remains strong and total leased space in 2005 is expected to exceed 9.5 million square feet for the third consecutive year. The County's overall office vacancy rate declined from the 8.6 percent at year-end 2004 to 7.6 percent as of mid-year 2005. Including sublet space, the mid-year 2005 office vacancy rate was 10.1 percent, down from 11.6 percent in 2004. In FY 2007, existing nonresidential property assessed values experienced a robust increase of 16.64 percent after a strong increase of 12.74 percent in FY 2006. As a result of improving office vacancy rates and recent sales activity, the value of Office Elevator properties (mid- and high-rises), which comprise 39.3 percent of the nonresidential tax base, rose 24.16 percent in FY 2007. Office vacancy rates are expected to continue to improve during the forecast period as a result of business expansion and job growth. Based on the current rate of absorption, there is only about an 18 month supply of office space available. However, as of year-end 2005, an additional 2.1 million square feet in 24 buildings were under construction.

The value of Hotel property advanced a hearty 25.54 percent in FY 2007 on top of the 15.34 percent increase experienced in FY 2006. Lower rates of growth are projected in Hotel property over the next two years as occupancy rates drop slightly in response to the additional availability of rooms as three new hotels are under construction which will increase hotel room inventory by 478. The Retail and Regional Malls categories rose 18.56 and 42.24 percent, respectively in FY 2007. Growth in these categories is expected to be lower during FY 2008 and FY 2009 in response to slower growth in the economy. Overall, the value of existing nonresidential properties is anticipated to experience moderate increases of 7.50 percent in FY 2008 and 7.00 percent in FY 2009.

In addition to equalization, the remaining increase in Real Estate value is due to new construction or normal growth. New construction is expected to increase at a lower rate during FY 2008 and FY 2009 as a result of diminishing buildable land in the County. Overall, increases due to new construction are projected to be 1.55 percent in FY 2008 and 1.30 percent in FY 2009 compared to an increase of 2.94 percent in FY 2007. Incorporating equalization and new construction, the real estate tax base is expected to experience an overall increase of 8.65 percent in FY 2008 and 7.90 percent in FY 2009 compared to the 22.70 percent increase experienced in FY 2007.

The FY 2008 and FY 2009 Forecast assumes that the projected value of one penny of the Real Estate Tax rate will continue to be dedicated to The Penny for Affordable Housing Fund and the Stormwater Management Program. The estimated value of the penny is $23.7 million in FY 2008 and $25.6 million in FY 2009.

FY 2007 Current Personal Property Tax revenue, which represents 15.8 percent of total FY 2007 General Fund revenue, is anticipated to experience growth of 5.6 percent in FY 2007. Based on the Personal Property Tax Relief Act (PPTRA) of 1998, the Virginia General Assembly approved a plan to eliminate the Personal Property Tax on vehicles owned by individuals. Under the originally approved plan, taxes paid by individuals were to be reduced on the first $20,000 of value over a five-year period ending in FY 2003. However, due to the State's lower than anticipated General Fund revenue growth and the unanticipated growth in required PPTRA funding, the reimbursement rate has remained at 70 percent since FY 2002. The 2004 General Assembly approved legislation that continued a 70 percent reimbursement rate in FY 2006, but capped statewide Personal Property Tax reimbursements at $950 million in FY 2007. Each locality will receive a percentage allocation from this fixed amount determined by the locality's share of statewide tax year 2005 collections. In FY 2007, the effective state reimbursement percentage is expected to be between 60 and 70 percent, thus potentially increasing the taxpayer's share of the tax or reducing revenue to the County. Because the impact of the State cap in FY 2008 and FY 2009 is uncertain, no growth in Personal Property Tax revenue has been assumed for FY 2008 and FY 2009.

Growth in revenue categories that are sensitive to economic conditions such as Business, Professional and Occupational Licenses (BPOL) and Sales Tax is expected to slow from the FY 2007 rate. BPOL revenue and Sales Tax receipts are projected to rise 4.5 percent during the forecast period down from a projected 5.0 percent in FY 2007. Recordation and Deed of Conveyance taxes, which are paid for recording deeds are anticipated to fall in FY 2008 and FY 2009, as the housing market continues to cool down.

Interest earned on investments is expected to rise in FY 2008 and FY 2009 based on a forecast of gradual increases in interest rates and growth in the County's investment portfolio. Since February 2005, the Federal Reserve has raised interest rates nine times, from 2.5 to 4.5 percent as of January 2006. In minutes released from the January meeting, the Federal Reserve indicated that continued increases in interest rates may be necessary in order to provide economic growth and stable prices. Changes in the federal funds rate will directly impact the yield earned on the County's investment portfolio. The average annual yield on investments was just 1.72 percent in FY 2005; however, based on current interest rates, the yield on the County investments is expected to rise to 2.23 percent in FY 2006 and to 3.0 percent in FY 2007. During the forecast period, the yield on investments is expected to continue to increase with projections of 4.3 percent in FY 2008 and 4.5 percent in FY 2009.

Excluding revenues from the Commonwealth of Virginia associated with the reimbursement of Personal Property Taxes, Revenue from the Commonwealth and Federal Government is expected to rise 1.7 percent in FY 2007. Revenue from the Commonwealth and Federal Governments is expected to slightly rise 0.4 percent each year of the forecast. 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.

The Permits, Fees and Regulatory Licenses category is anticipated to increase $4.1 million in FY 2006, primarily due to proposed fee increases in Zoning Fees and Land Development Services (LDS) Fees including issuing building permits and inspections. During FY 2007, the second phase of LDS fee adjustments will be implemented, resulting in an increase of $1.4 million. In FY 2008, LDS fees are projected to remain at their FY 2007 level. It should be noted that the expectation that LDS's Building and Permit fee revenue will not increase assumes a continuation of the same level of building activity projected to be achieved in FY 2007 and should not be viewed as a reduction. Other Permit and Fees and Regulatory Licenses categories are expected to experience modest growth during the forecast period.

In total, General Fund revenues are projected to increase 5.78 percent in FY 2008 and 5.49 percent in FY 2009. Revenue growth rates for individual categories are shown in the following table:

REVENUE GROWTH RATES

Category	FY 2006	FY 2007	FY 2008	FY 2009
Real Estate Tax - Assessment Base	23.49%	22.70%	8.65%	7.90%
Equalization	20.80%	19.76%	7.10%	6.60%
Residential	23.09%	20.57%	7.00%	6.50%
Nonresidential	12.74%	16.64%	7.50%	7.00%
Normal Growth	2.69%	2.94%	1.55%	1.30%
Personal Property Tax - Current[1]	6.55%	5.60%	0.00%	0.00%
Local Sales Tax	7.06%	5.00%	4.50%	4.50%
Business, Professional and Occupational, License (BPOL) Taxes	5.00%	5.00%	4.50%	4.50%
Recordation/Deed of Conveyance	0.00%	0.00%	-5.00%	-5.00%
Interest Rate Earned on Investments	3.80%	4.15%	4.30%	4.50%
Vehicle Decals	2.00%	2.00%	2.00%	2.00%
Building Plan and Permit Fees	16.77%	5.56%	2.00%	2.00%
Charges for Services	10.89%	5.41%	2.00%	2.00%
State/Federal Revenue[1]	-2.37%	1.74%	0.42%	0.43%
TOTAL REVENUE	**7.65%**	**8.83%**	**5.78%**	**5.49%**

[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 Assumptions

Direct Expenditures

As previously mentioned, for the purposes of this forecast, increases in County expenditures have been held to 5.0 percent growth and the transfer to the Fairfax County Public Schools has been set at 6.0 percent. The basic costs of operating County government will have to be accommodated within this overall increase for FY 2008 and FY 2009, such as funding pay for performance for employees, market rate adjustments for contractors and inflationary growth, rising health care and energy costs, and required contributions for retirement. The Board of Supervisors has identified priorities for the next several years, including public safety and gang prevention; affordable housing; environmental protection; strong investment in education; transportation improvements; and revenue diversification to reduce the burden on homeowners. Having these clearly defined priorities will enable the County to focus budget strategies on those initiatives that will result in the greatest return on investment, while balancing the cost to taxpayers.

Transfers Out

School Transfer

The Financial Forecast includes an increase in the School transfer of 6.0 percent in both years, FY 2008 and FY 2009.

Transportation

The transfer requirements of $24.5 million and $28.2 million in FY 2008 and FY 2009, respectively, for Metro Operations and Construction reflect annual increases of 15.0 percent based on projected inflationary increases and regional infrastructure requirements for Metrorail and Metrobus service. Increases in County Transit have been held to 5.0 percent growth in FY 2008 and FY 2009. In addition, $20.0 million has been set aside in FY 2008 and FY 2009 for other transportation requirements to be determined by the Board of Supervisors.

Debt Service
The Debt Service requirements reflect increases required to support the level of bond sales proposed in the FY 2007 – 2011 Advertised Capital Improvement Program (With Future Fiscal Years to 2016).

Paydown
Paydown capital construction includes transfers from the General Fund to support construction and renovation of capital facilities. In FY 2008 and FY 2009, the projected annual transfer for Paydown construction is $45.0 million per year.

Transfer to Fairfax-Falls Church Community Services Board
The General Fund transfer supporting the Fairfax-Falls Church Community Services Board represents growth of 5.0 percent each year.

Information Technology
A transfer of $30.0 million has been included in each of the forecast years for information technology (IT). The County's Information Technology Advisory Group (ITAG), a private sector advisory group established by the County Executive to investigate the condition of the County's IT resources, recommended in the early nineties that annual spending of $15 million to $20 million was required to meet basic IT requirements. The increase over that amount represents inflationary increases and the need for a major renovation of the County's corporate systems that is anticipated in FY 2008 and FY 2009.

Stormwater Management Program and The Penny for Affordable Housing Fund
As of the FY 2007 Advertised Budget Plan, the one penny of the Real Estate Tax rate dedicated to Fund 318, Stormwater Management Program and Fund 319, The Penny for Affordable Housing Fund, will be reflected as revenue in the funds rather than as a transfer from the General Fund.

Increased Utility/Energy Costs
Utility and energy costs are expected to continue to rise over the forecast period. The supply of oil and natural gas will remain tight and the growth in demand is expected to outpace growth in production leading to higher prices. In order to meet rising energy costs, $20 million has been set aside in FY 2008 and FY 2009.

Other Transfers
Transfers to funds other than the ones mentioned above have been increased by 5.0 percent in FY 2008 and FY 2009.