## General Fund Financial Forecast 2013-2018

**Executive Summary:**

- The 2013-14 forecast is balanced over the Biennium, with revenues substantially covering existing service levels.
- The revenue forecast assumes no changes in rates for major tax components such as sales tax, B&O tax, and utility taxes.
- Revenue collections are projected to see modest increases through the forecasted period
    - Sales tax and B&O tax are growing again, but at a very modest pace. The main factor preventing a stronger recovery in Sales and B&O tax is the construction sector.
- Expenses are forecasted at existing levels of service.
    - Due to the fact that personnel costs are the largest component of General Fund expenditures, increases in personnel drive the overall costs.
- The General Fund Balance is forecasted below the 15% target, at approximately 12.9% in 2013, and remains stable over the forecast period.
- There are few changes from the April 2013-2014 Forecast:
        - I-1183 Liquor Privatization went into effect, increasing In Liquor Profit of $290,000 per year
        - Elimination of $660,000 of Liquor Excise Tax due to State reductions
        - Net reduction of $370,000 per year.
    - The actual Consumer Price Index for wage earners (CPI-W) was 2.7%, 0.2% lower than the forecasted 2.9%. This change revised costs down by $150,000 per year.

**Historical Reductions:**

The after effects of the Great Recession continue to present some degree of economic uncertainty, and the City has realigned organizational capacity to match the current economic climate. Since the 2011-2012 Adopted Budget, City management's strong actions have brought expenditures closer in line with revenues. The organization continues to work diligently to address the slow recovery through continued management actions, and implementing organizational best practices, including identifying new process improvements and efficiencies to control expenditures. Great efforts have been made to reduce impacts to frontline services and to the public.

- During the 2011-2012 Budget (adopted in December 2010), the General Fund budget was reduced by just over $18 million from the previous biennial budget. This included the elimination of 54 FTEs.
- In late 2011, during the Mid-Biennial Budget update, the 2012 General Fund budget was reduced by another $6.5 million, and included elimination or freezing of a further 31 FTEs; and
- In late 2011, during the Mid-Biennial Budget Update, Development Services reduced their budget by 15 FTEs to reflect the depressed construction market.

**Overview & Forecast Results:**
The General Fund forecast shows that revenues and expenditures are growing at nearly the same rate over the next few years. Past recessions have shown that the recoveries are generally marked by the higher than average rate of economic growth, followed by a more moderate growth. The Great Recession has proved to be an exception to that rule, where the recovery has been very weak and fraught with setbacks. Regional economists are generally in agreement that the recovery will remain weak for the next few years, but reserve caution about the outlook because of several possible risks to the economy's ongoing health.

**2013-2014 Financial Forecast**
**General Fund**
**(in $000)**

| | 2012 Estimated | 2013 Forecast | 2014 Forecast | 2015 Forecast | 2016 Forecast | 2017 Forecast | 2018 Forecast |
|---|---|---|---|---|---|---|---|
| **RESOURCES** | | | | | | | |
| Property Tax | $30,300 | $30,681 | $31,043 | $31,499 | $31,912 | $32,317 | $32,728 |
| Sales Tax | 34,422 | 35,956 | 37,447 | 39,566 | 41,717 | 43,861 | 46,027 |
| Business & Occupation Tax | 19,038 | 19,878 | 20,615 | 21,489 | 22,321 | 23,152 | 23,931 |
| Utility Tax | 25,072 | 26,744 | 28,006 | 29,283 | 30,440 | 31,714 | 32,889 |
| Miscellaneous Revenue | 42,906 | 44,527 | 45,673 | 46,679 | 47,881 | 49,122 | 50,399 |
| Estimated Annexation Revenue | 0 | 2,632 | 2,364 | 2,429 | 2,490 | 2,555 | 2,620 |
| Total Revenue | $151,738 | $160,418 | $165,147 | $170,945 | $176,761 | $182,720 | $188,594 |
| Total Revenue % Growth | | 5.7% | 2.9% | 3.5% | 3.4% | 3.4% | 3.2% |
| Revenue Growth less Annexation | | 4.0% | 3.2% | 3.5% | 3.4% | 3.4% | 3.2% |
| **EXPENDITURES** | | | | | | | |
| Personnel | $95,972 | $99,783 | $102,929 | $106,619 | $110,351 | $114,213 | $118,211 |
| Maintenance & Operations | 55,478 | 58,309 | 60,355 | 61,804 | 63,247 | 64,791 | 66,382 |
| Estimated Annexation Expenses | 0 | 2,487 | 2,215 | 2,284 | 2,354 | 2,427 | 2,502 |
| Expenditures at Existing Service Levels | $151,450 | $160,579 | $165,499 | $170,701 | $175,939 | $181,413 | $187,070 |
| Total Expenditure Growth | | 6.0% | 3.0% | 3.1% | 3.0% | 3.1% | 3.1% |
| Expenditure Growth less Annexation | | 4.4% | 3.3% | 3.1% | 3.1% | 3.1% | 3.1% |
| (Gap)/Surplus | $288 | ($161) | ($351) | $243 | $822 | $1,307 | $1,523 |
| Ending Fund Balance | $20,457 | $20,296 | $19,945 | $20,188 | $21,010 | $22,317 | $23,841 |
| % Ending Fund Balance | 13.5% | 12.9% | 12.3% | 12.0% | 12.1% | 12.4% | 12.9% |

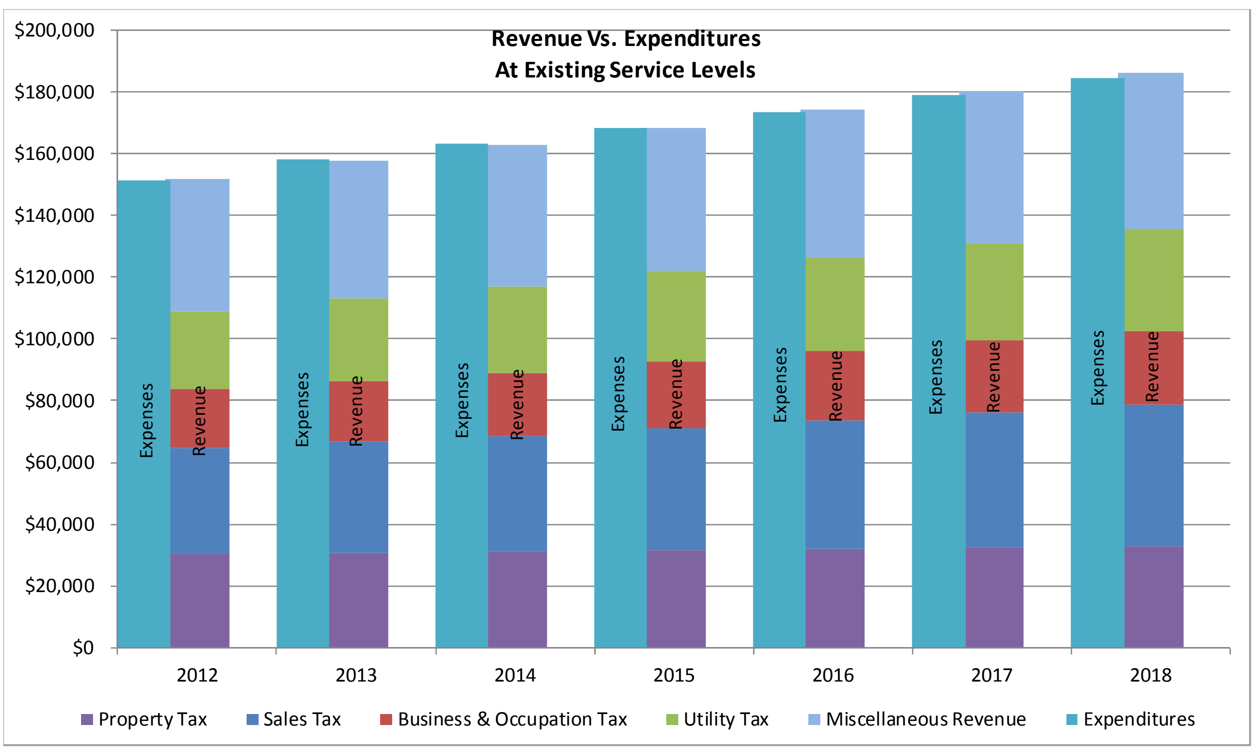
Note: Percentage changes are shown both as total gross changes and net of annexation to enable further comparisons of growth in existing services and revenues. The chart below shows the existing services' growth levels by line item net of the annexation.

Council Budget Workshop

July 30, 2012

**2013-2014 Financial Forecast**
**General Fund**
**(%Δ)**

| | 2013 Forecast | 2014 Forecast | 2015 Forecast | 2016 Forecast | 2017 Forecast | 2018 Forecast |
|---|---|---|---|---|---|---|
| **RESOURCES** | | | | | | |
| Property Tax | 1.3% | 1.2% | 1.5% | 1.3% | 1.3% | 1.3% |
| Sales Tax | 4.5% | 4.1% | 5.7% | 5.4% | 5.1% | 4.9% |
| Business & Occupation Tax | 4.4% | 3.7% | 4.2% | 3.9% | 3.7% | 3.4% |
| Utility Tax | 6.7% | 4.7% | 4.6% | 4.0% | 4.2% | 3.7% |
| Miscellaneous Revenue | 3.8% | 2.6% | 2.2% | 2.6% | 2.6% | 2.6% |
| Total Revenue Net of Annex. | 4.0% | 3.2% | 3.5% | 3.4% | 3.4% | 3.2% |
| **EXPENDITURES** | | | | | | |
| Personnel | 4.0% | 3.2% | 3.6% | 3.5% | 3.5% | 3.5% |
| Maintenance & Operations | 5.1% | 3.5% | 2.4% | 2.3% | 2.4% | 2.5% |
| Total Expenditures Net of Annex. | 4.4% | 3.3% | 3.1% | 3.1% | 3.1% | 3.1% |



**Economic Outlook:**
The economy is still in a fragile state, with the recovery at times looking to take a turn for the worse. Since the recession officially ended, the possibility of economic destabilizing events has been almost worse for economic health than any of the risks that actually materialized. The progression of globalization has caused national and local economies to be more and more intertwined.

Global and National risks on the horizon:

- The European Union's sovereign debt crisis has continued to be a looming risk to the global economy. The global economic recession caused several highly-leveraged EU countries to become undercapitalized to the point of being in danger of defaulting on their national debt. Unfortunately the political structure of the Euro Zone has caused this problem to be harder to sort out than in non-Euro Zone countries.

- The Middle East is a constant risk to our economic stability. The recent "Arab Spring" uprisings and threats from Iran to close the Strait of Hormuz to international shipping have caused greater than usual instability in the region. This region's stability is closely linked to our economy because of our dependence on oil. The United States imports approximately half of the oil it consumes and a large portion of that comes from the Middle East. High oil prices translate into less free cash flow for consumers and higher shipping costs for goods.

- The "Fiscal Cliff" refers to expiration of several federal financial policies, the expiration of the Bush tax cuts, extension of unemployment benefits and automatic spending cuts across the federal budget. The Congressional Budget Office has said that, if these policies are not extended, the country is likely to face a retraction of the economy of 1.3% and another recession.

Local Economy:
On the local level the economy is acting like the "Little Engine That Could". Despite all the risks, the local economy keeps trudging along at a slow but steady pace.

- The Puget Sound region has traditionally performed better than the national economy. This is due to the success of the many businesses that call the region home, such as Boeing, Microsoft, Starbucks, and Amazon to name a few. Ultimately, the main driver to any local economy is employment and the Puget Sound area has outpaced the nation in the recovery.

- Consumer demand is improving but has not reached pre-recession levels. Tepid consumer demand is likely most closely attributable to the lack of recovery in the construction and housing markets. Construction has been an integral component of our economy over past years, as well as a big component in our tax collections. A recovery in construction is dependent, largely, on the housing market, and the housing market has been overloaded with inventory, driving down costs and making it less profitable to construct new homes. A bright spot in all of this is that, due to the increased demand for apartments, rents have started to climb and that, coupled with the bottomed out housing prices, make it more cost effective for people to buy a home rather than rent one. Once the housing inventory is reduced through sales, home prices are expected to also rebound, thus creating a more profitable environment for home building to resume. Unfortunately this situation will take some time to work itself out, and it may still take a few years to get back to prerecession levels.

Overall, the City's forecast assumes a modest recovery of tax revenue for the next few years recognizing that the Puget Sound will continue to grow slowly as consumer demand returns. It should be noted that the above-mentioned global and federal risks are not factored into the forecast at this time.

**Resource Drivers:**

The General Fund's main sources of revenue are sales, property, Business and Occupation (B&O), and utility taxes. Overall, the most sensitive of these revenue sources due to economic conditions are sales and B&O taxes. These taxes are directly linked to business transactions. Property tax rates are directed by Council policies and annual legislative actions, and Utility tax is dependent on utility rates, residential usage and, to a lesser degree, business activity.

The City's sales tax collections hit bottom from the recession in 2010 and have since started to grow again at a modest rate, with a 2.9% increase in 2011. Sales tax is the most volatile revenue source the City has. Year-to-date tax collections are now coming in at forecast, with a year to date percent of 4.5% increase over the same period in 2011. As sales tax has begun to grow in the last year and a half, the missing piece has been construction sales tax. As stated previously, construction has been slow to recover, and the City's forecast assumes a continued slow recovery with retail sales as the main recovery driver. The forecast assumes a 4.5% increase in 2013 and 4.1% in 2014, overall.

Business & Occupation Tax also bottomed out in 2010 and has seen a moderate recovery in the last year and a half, with a 6.5% increase in 2011 and an estimated 3.7% increase in the last six months. B&O tax is a little less volatile than Sales Tax.

**Changes since April Forecast:**

- Beginning in 2013, additional revenue from the newly annexed areas of Eastgate, Tamara Hills, Horizon View and Hilltop will be included in the Forecast.
- The City's portion of the Liquor Excise Tax was eliminated reducing the forecast by $660,000. Liquor Profit was increased by approximately $290,000.

**Expenditure Drivers:**

Personnel, including health benefits, constitute two thirds of the General Fund budget, making it the biggest driver of costs for the City. Personnel costs are made up of two main components, salaries/wages and benefits. The City's salaries/wages costs are aligned to the regional jobs market and influenced by the Seattle-Tacoma Bremerton Consumer Price Index for Wage Earners (CPI-W) measured June to June. For 2013 the City CPI-W estimate was at 2.9% under the assumption that fuel costs would again push the CPI-W to the normally expected upper bounds of CPI. Actual CPI-W from June to June was only 2.7%, creating additional savings of approximately $150,000. The 2014 CPI-W estimate is projected to be 2.2%.

Please see White Paper titled Compensation, Pension, and Health Benefits found in the Operating Appendices for additional information on health benefits, COLA, and pensions.