

City of Portland

Quarterly General Fund Budget and Economic Tracking Report

FY 2012-13 Year-End & Outlook City Budget Office

INTRODUCTION

This document summarizes the City's current General Fund financial position and the current economic environment. The first section discusses the circumstances influencing the City's FY 2012-13 General Fund ending balance. The second section briefly discusses the City's General Fund outlook as it begins the process of developing the FY 2014-15 budget. It is important to note that this is not an official forecast and simply represents the most current information available. Though the fiscal year has ended, the following information may be subject to significant variation due to a variety of accruals and accounting adjustments that will be completed over the next month. Additionally, to the extent that bureau submissions for the Fall Budget Monitoring Process (BMP) do not include encumbrances made at the end of FY 2012-13, or City Council decides not to fund those asked for, additional one-time resources will become available as part of the Fall BMP.

FY 2012-13 YEAR-END

The City's Adopted Budget always assumes a certain level of discretionary General Fund beginning balance. To the extent that the prior year's ending balance exceeds this amount, the City has "excess" balance to spend on a one-time basis. Current City financial policy states that 25% of the excess should be spent on capital projects, while the remaining 75% should be held for the next fiscal year budget. Historically, the City has usually ended up with excess balance as a result of the conservative forecasting practice described in the citywide financial policies. During the housing boom, excess balance amounts rose to nearly \$30 million. Currently, it appears that the excess balance will likely be between \$8 million and \$11 million once all of the revenues and expenses reflect all of the appropriate accruals and adjustments. For context, given that there are nearly \$1 billion in combined General Fund revenues and expenses, a forecast that comes in 1% off will generate excess balance of almost \$10 million. The current situation is likely the case for several reasons:

• The most likely reason that we will see a higher-than-expected ending balance is the dramatic reduction in external materials and services spending (EM&S) that has occurred since March. Figure 1 is a graph of the last several years for EM&S spending for the period of March through May each fiscal year. Following a memo sent by the Mayor's Office in March, it appears that bureaus significantly reduced materials and services spending. EM&S spending in the three

months between March and May was the lowest EM&S spending the City had seen in at least six years. Potential savings from those three months alone (assuming typical spending in other months) could result in more than \$5 million in unexpected ending balance for FY 2012-13.

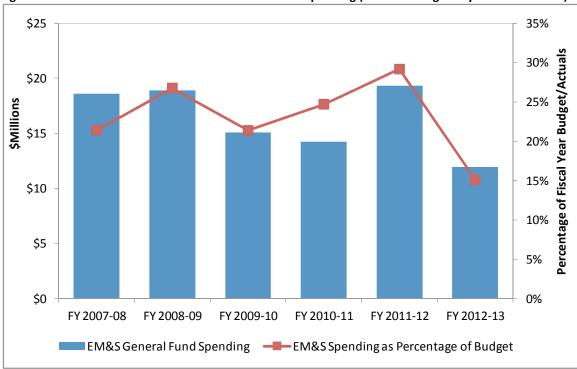


Figure 1. General Fund External Materials and Services Spending (March through May each Fiscal Year)

- Personnel Services also waned in the final months of FY 2012-13. For much of the year, trends showed that the City would spend at least \$315 million in General Fund on personnel services; the budget, after accounting for compensation set-aside requests was \$316.8 million. However, the City ended the year with less than \$314 million spent on personnel services with nearly half of the underspending coming in the Fire Bureau and OMF. It should be noted that both the Fire and Police bureaus were directed to reduce overtime spending as part of City Council's subcommittee process in April.
- The April forecast assumed the minimum impact (\$3 million) from increased telecom taxes. Following the legal victory over CenturyLink, it appears that revenue from the increased taxes will be closer to the higher end (\$4 million to \$5 million) of Revenue Bureau estimates.
- All five major General Fund revenue sources reached record highs in FY 2012-13, with the largest jump coming in transient lodging taxes, which saw a more than 21% increase compared with FY 2011-12. Also, business license taxes were estimated in April to end the year at \$76.1 million. However, after the final figures were tabulated, revenues came in nearly \$2 million higher than expected.

FY 2013-14 General Fund Outlook

As the City looks ahead, it is important to remember that the City would have been adding to its ongoing expenses rather than cutting the FY 2013-14 budget if the only thing affecting the forecast was the economy. However, the budget impacts from the formation of the County Library District, costs associated with the Department of Justice agreement, and the conversion of previously one-time funded programs to the ongoing base, forced the City to make large ongoing cuts. The underlying economic conditions, though, have improved slightly, especially as it relates to the City's revenue streams. This is consistent with the current point in the business cycle and will likely persist in the near term. The graph below looks at annual growth in the City's five largest General Fund revenue streams – property taxes, business license taxes, utility license taxes/franchise fees, transient lodging taxes, and state-shared liquor and cigarette tax revenue.

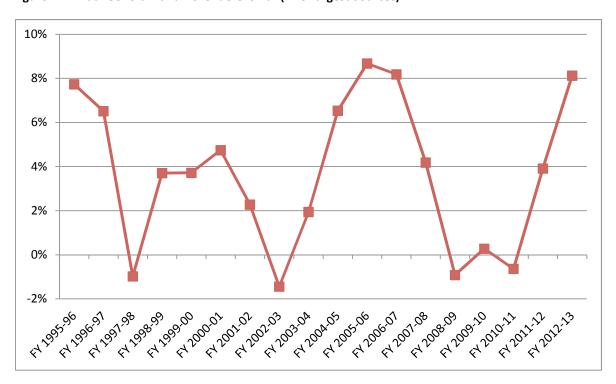


Figure 2. Annual General Fund Revenue Growth (Five Largest Sources)

As the graph illustrates, the City is in a period of the business cycle that generates above average revenue growth. This will likely persist through at least FY 2014-15 (after accounting for the impact of the library district formation) because property values have been rising significantly. The rise in values, particularly in southwest Portland, will ease the impact of property tax compression, resulting in above average property tax growth. Though we expect value growth to flatten over the next six to twelve months, the more than 15% growth seen thus far in 2013 will significantly increase the January 1, 2014 property values on which the FY 2014-15 property taxes are collected.

Along with increases in property taxes, the City is seeing its volatile revenue sources (business license and transient lodging taxes) experience record highs and substantial growth. Furthermore, the FY 2013-14

Adopted Budget included ongoing reductions that were almost \$2 million higher than were necessary in order to fund certain one-time priorities. As a result, even if the underlying economic and revenue conditions assumed in the April forecast held perfectly, the City still would be in a position to add ongoing programs in FY 2014-15. Depending on a variety of conditions and the results of pending information, such as the property tax assessments in October, the City may be in a position to add significantly to its ongoing General Fund program base beginning in FY 2014-15.

CURRENT ECONOMIC CONDITIONS

Economic conditions, while improved slightly from a year ago, remain mired in a "two steps forward, one step back" economic recovery. Even as the housing market begins to see healthy price appreciation, the job market, particularly in the public sector, is barely keeping its head above water – job growth has largely matched what one would expect in order to simply keep up with population increases. Of course, as it relates to the City's revenue streams, the uptick in housing is much more significant than the steady, but mediocre, job growth.

Locally, the employment data has steadily improved. Unemployment continues to tick lower, down to 7.3% in July, its lowest level in nearly five years. Meanwhile, Multnomah County¹ had roughly 10,000 more jobs in July 2013 than in July 2012, despite losing several hundred government jobs during the year. The growth was relatively broad based in the private sector, with the largest percentage growth in construction and professional and business services.

Home sales activity appears to be waning slightly after a very robust beginning of 2013. Prices were essentially flat this summer as inventory increased. This should be expected to some extent, as price appreciation eventually yields more supply, slowing price growth. Many homeowners that either delayed moving or were unable to move due to negative equity positions will begin to enter the market as their positions change. Additionally, rising mortgage rates will serve to cool the market in the near term. This "stair step" pattern of home price increases and new inventory flooding the market will likely persist for several years. In spite of the recent growth, according to the CoreLogic, Portland prices remain more than 15% below the peak pre-recession level.

¹ The county level is the smallest geographic area for which jobs data are available.

Table 3 summarizes current selected economic indicators and forecasts that helped inform the General Fund forecast. Though the data remains nearly universally positive for the first time since the recovery began, it is important to note that employment – along with many other indicators – still remains well below pre-recession levels.

TABLE 3. Selected Portland Economic Indicators

	Most		Year Ago	Recent
Indicator	Recent	Value	Change	Trend
Economy				
Total Employment, Portland MSA ¹	7/2013	1,032,800	3.0%	Positive
Portland MSA Unemployment Rate ¹	7/2013	7.3%	-0.9%	Positive
Consumer Price Index, Portland-Salem ²	1H-2013	228.0	1.9%	Neutral
Real Estate				
Median Home Price, Portland Metro ³	7/2013	\$280,000	14.3%	Positive
Housing Units Permitted (Y-T-D) ⁴	7/2013	2,267	38.3%	Positive
Portland Metro Industrial Vacancy Rate ⁵	2Q-2013	10.1%	N/A	Positive
Portland Office Vacancy Rate ⁵	2Q-2013	9.7%	N/A	Positive
Commerce				
Total PDX Air Passengers (Y-T-D) ⁶	7/2013	8,452,908	4.1%	Positive
Total PDX Freight (Y-T-D in Tons) ⁶	7/2013	119,717	-0.3%	Neutral
Total Port of Portland Marine Freight (Y- T-D in Tons) ⁶	7/2013	6,953,973	-5.2%	Neutral
Hotel Average Revenue Per Available Room ⁷	2Q/2013	\$79.26	13.7%	Positive

¹ Oregon Employment Department, Unemployment Rate is seasonally-adjusted, Year Ago Change is percentage point increase/decrease

² Bureau of Labor Statistics. CPI-W. Portland-Salem, OR-WA

³ Market Action, Publication of RMLS

⁴ U.S. Census Bureau

⁵ Norris, Beggs, & Simpson, Market Research, Year Ago Change is percentage point increase/decrease. Note: Methodological change beginning 1st Qtr., 2013

⁶ Port of Portland, Aviation & Marine Statistics

⁷ PFK Hospitality Research, LLC