City of Portland

General Fund Forecast

FY 2019-20 through FY 2023-24

City Budget Office

December 2018

I. Forecast Summary

Though growth has slowed, the City's General Fund revenue sources continue to hit record highs, resulting in $12.8 million in additional resources in FY 2019-20 above what is necessary to continue ongoing City programs. Expense pressures from escalating inflation and PERS costs, as well as increased demand for City services, means that the additional resources will only be available in the near term. In the long-run, the City will need all available revenue to fund the ongoing personnel and program costs that exist today.

City financial practice requires that the City balance its budget over the entire five-year forecast. This means that, to the extent forecasted revenues in year five of the forecast are insufficient to cover expected costs in the same year, budget cuts must be enacted in year one of the forecast to set the budget on a sustainable course. This forecast serves as the initial planning forecast for the FY 2019-20 budget. The final forecast for the FY 2019-20 budget will be issued near the end of April 2019.

Table 1 summarizes discretionary General Fund resources and expenses through FY 2023-24. As shown in Table 1, the City will have $2.9 million in unallocated ongoing General Fund resources, and $9.9 million in one-time resources above projected expenditures. City financial policy states that at least 50% of the one-time funds be spent on major maintenance and replacement of City assets.

Forecast Highlights

New Ongoing: $2.9 million

New One-Time: $9.9 million

Significant Changes Since April:

- Minor changes to revenue and expense forecasts
- Increased forecast for business license taxes to reflect higher tax rate
- Higher inflation-related forecasts, but slightly lower forecast for PERS-related expenses

Local Economic Highlights

- Home prices and rent growth abating, some turning negative
- Local unemployment rate remains near record low
- Local construction pipeline drying up

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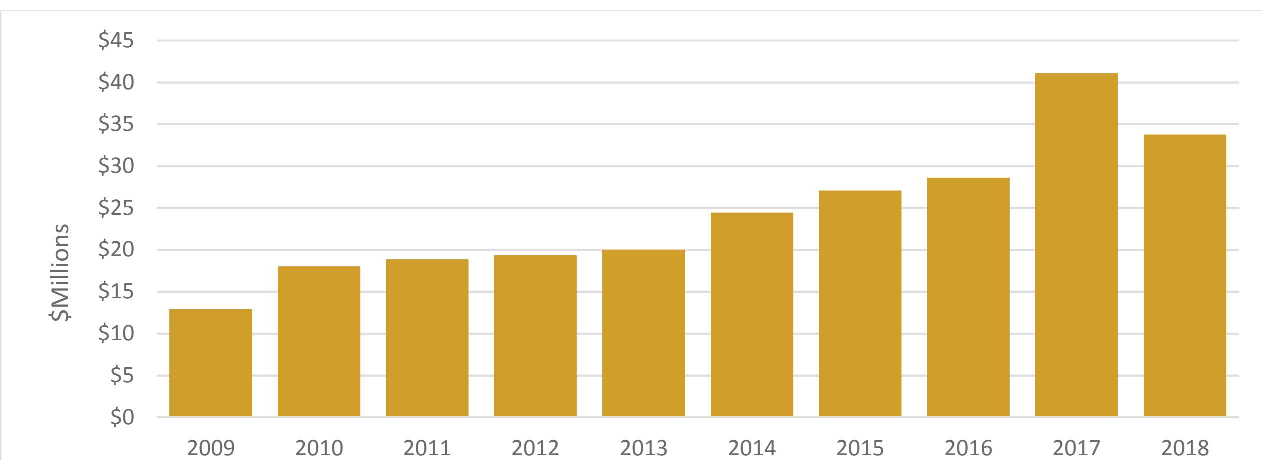
TABLE 1. Discretionary General Fund Five-Year Forecast ($millions)

	Fiscal Year					
Budget Category	**2018-19**	**2019-20**	**2020-21**	**2021-22**	**2022-23**	**2023-24**
Total Resources	**$565.6**	**$570.3**	**$576.5**	**$598.1**	**$618.0**	**$638.7**
Total Expenses	**$565.6**	**$557.4**	**$575.9**	**$598.1**	**$614.9**	**$638.7**
Available Ongoing		$2.9	$0.0	$0.0	$0.0	$0.0
Available One-Time		$9.9	$0.6	$0.0	$3.1	$0.0
Total Expenses with Adds & One-Time Spending	**$565.6**	**$570.3**	**$576.5**	**$598.1**	**$618.0**	**$638.7**
Note: Totals may not add due to rounding. FY 2018-19 figures are for the Adopted Budget.						

For FY 2019-20, the City Budget Office was directed to hold back 1% of each General Fund bureau's ongoing expenses in order to allow City Council flexibility in the budget process. That action created about $5.5 million in ongoing resources. Meanwhile, subsequent Council actions have obligated almost $4 million in new ongoing expenses.

On net, there was little changed from the April 2018 budget forecast. That said, there is significant uncertainty for this time of year as it relates to several revenue forecasts. Business license taxes are always difficult to anticipate at this time of year, but, unlike in most prior years, collections year-to-date are well below those of a year ago.

FIGURE 1. Business License Taxes Stay on Trend, But Below Last Year (Y-o-Y Growth, July to November)



The was also an unusual result in the current year property tax data. Based on figures form the Multnomah County Assessor's Office, assessed value growth for FY 2018-19 was lower than expected. It appears that is the result of the prior year assessed values being artificially high. Following the certification of values in the fall, several large taxpayers made successful appeals that lowered their taxable values. Ultimately, this had the effect of overstating assessed value growth last year and then understating it this year. It will result in FY 2018-19 property tax collections being about $1.5 million below what was budgeted.

II. Forecasts Changes/Assumptions

Significant Changes. Other than the adjustment to the business license tax forecast in order to reflect the higher tax rate enacted as part of the FY 2017-18 Adopted Budget, changes to the forecast were minor. Small increases in the forecasts for lodging taxes and state shared marijuana tax revenue were largely offset by a decrease in the forecast for property taxes. With respect to the expense forecast, an increase in inflation expectations was mitigated by PERS employer rates that will be slightly lower than expected.

Major Assumptions. This forecast assumes that local economic growth will continue to slow, but remain positive, with the exception of the construction industry. Though there are enough projects in the pipeline to extend the current level of activity through at least the end of 2019, it is clear through recent activity at the City's construction permitting bureau (Bureau of Development Services), that there are fewer projects initiating development for 2020 and beyond. Though there is some fear that this may unfortunately coincide with other business cycle and fiscal policy indicators (i.e., rising interest rates and the waning impact of the federal tax cuts), it is all but impossible to accurately forecast a recession 18 to 24 months out. That said, a recession does not appear imminent. Migration to Portland remains relatively high, though also at lower rates than the height of the expansion.

Major Forecast Risks

Increasing Personnel Costs – Between a relatively high inflationary environment driving higher cost-of-living allowances and two City and State policies – non-rep class compensation study for the City and pay equity from the State – City bureaus are like to feel greater than usual budgetary pressures over the next one to three years. The two most obvious solutions to these pressures, Council providing additional funds and/or City supervisors more actively managing their personnel budgets, both present challenges.

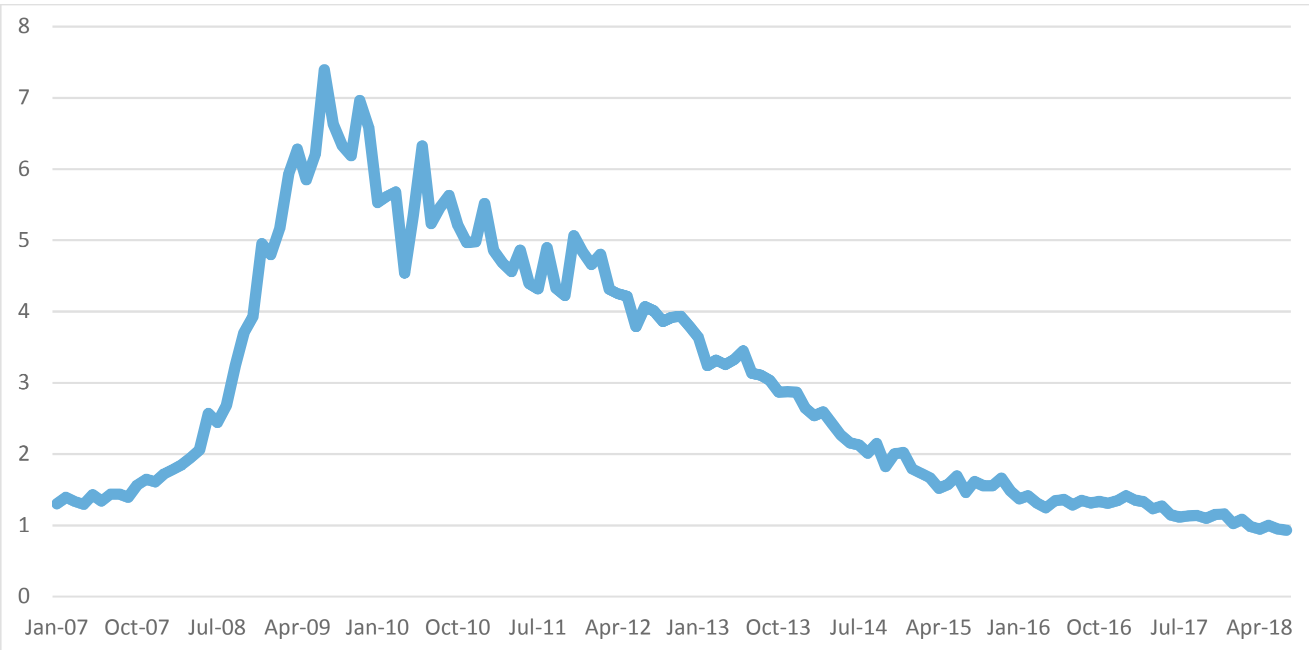
Business License Taxes – There is greater uncertainty around the forecast for business license taxes than at any time during the current expansion. Federal tax policy, an increased tax rate, and a new clean energy tax will all contribute to the uncertainty over the two years, regardless of the underlying economic environment. Given that this tax makes up almost 25% of General Fund discretionary revenue, even a modest dip in collections would cause a significant drop in revenue.

III. Current Economic Conditions

As 2019 arrives, the current economic expansion is poised to be the longest in the post-World War II era. The local economy continues to see healthy job growth, albeit slower than the expansion's peak, and record low unemployment. Though, it should be noted, that weakness is emerging in some sectors, in particular the construction sector. Table 2 at the end of the document shows many area economic indicators, the relative strength compared to a year ago, and a description of the trend regarding the most recent data points.

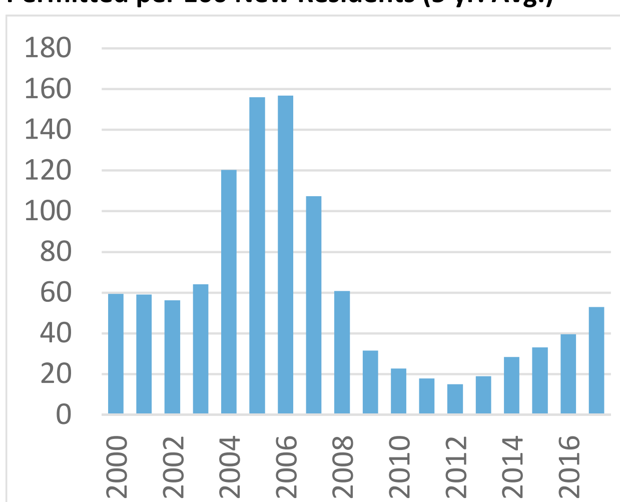
Employment. The tight labor market continues to make it difficult for firms to find workers. This tightness is pushing wages higher and/or leading to firms providing more on the-job training for new hires. Adjusted for age, labor force participation (the percentage of working age adults either employed or looking for a job) is back to where it was prior to the Great Recession. Figure three illustrates the broad tightness in the labor market as there are now approximately one million more jobs available than there are unemployed workers. Though the numbers in Figure 2 are nationwide, anecdotal evidence suggests that local figures may be even more askew.

FIGURE 2. Unemployed Workers Per Available Job



Real Estate. For the first time in this expansion, cracks are beginning to show in the markets for both owner-occupied and rental housing. In addition to the slowing of land use applications for new construction, rents are dropping for significant portion of the market, especially when landlord concessions are taken into account. Meanwhile, though the market for single family homes continues to see modest price increases, the inventory of available homes for sale also continues to expand. Finally, it is important to remember, that even with the record-setting construction of housing units over the last few years, the region has not built enough new units to accommodate new residents moving into the metro area. Figure 3 shows the number of housing units permitted per 100 new residents. The data of

FIGURE 3. Multnomah County Housing Units Permitted per 100 New Residents (5 yr. Avg.)



the last decade would suggest an average household size of about three people, whereas we know it is actually closer to 2.25 people. This is illustrative of a housing market in which demand outstrips supply, increases prices and pushes lower-income households toward less expensive housing further away from employment centers.

Commerce. As shown in Figure 4, the City has seen a dramatic increase in the number of active business tax accounts. While certainly at least partially a result of the expanding economy, the roughly 50% increase in the number of accounts is also a reflection of the expanded use of contractors, in particular those involved in industries like ride-sharing.

FIGURE 4. Active Business License Tax Accounts

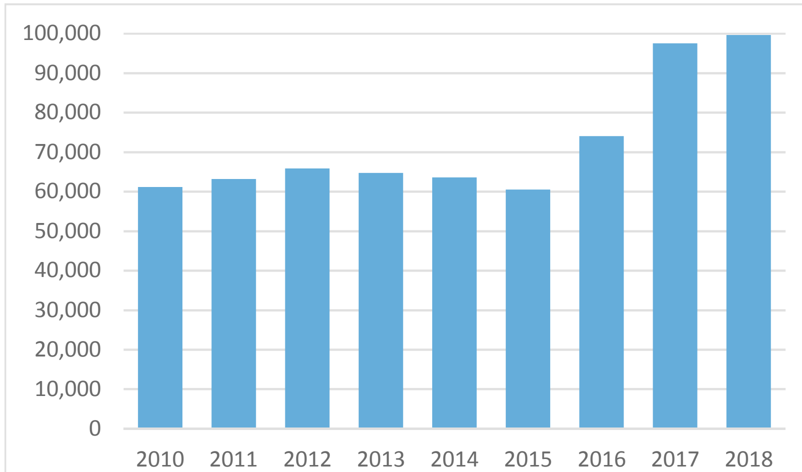


TABLE 2. Selected Portland Economic Indicators

Indicator	Most Recent	Value	Year Ago Change	Recent Trend
Economy				
Total Employment, Portland MSA	10/2018	1,205,700	2.3%	Positive
Multnomah County Unemployment Rate	10/2018	3.5%	-0.1%	Positive
Consumer Price Index, West-Size A	10/2018	263.924	3.8%	Neutral
Real Estate				
Median Home Price, Portland Metro	10/2018	$395,000	3.9%	Positive
Portland Metro Industrial Vacancy Rate	2Q-2018	4.0%	0.8%	Neutral
Portland Office Vacancy Rate	2Q-2018	9.7%	0.1%	Neutral
Multnomah County Multi-Family Vacancy Rate	2Q-2018	6.9%	1.2%	Neutral
Commerce				
Total Air Passengers (Y-T-D)	10/2018	16,686,407	4.4%	Positive
Hotel Average Revenue Per Available Room	2Q-2018	$106.44	-1.7%	Neutral

[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] Colliers International, Year Ago Change is percentage point increase/decrease.

[5] Port of Portland, Aviation Statistics

[6] CBRE Hotels