City of Tracy
Mid-Year Budget Workshop
FY 07-08

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Introduction

Zane Johnston, Finance Director

Fiscal Overview in Four Categories

- ► Background and Current Economic Environment
- ► FY 07-08 Mid-Year General Fund Review
- ► 3 Year Projection of General Fund Budgets
- ► Short and Long Term Fiscal Strategy to Address Budget Deficit

1. Background and the Current Economic Environment

City Has Enjoyed Strong Growth

	1999-2006	2007-2008
Property Tax Growth	15.1%	<2%>
Sales Tax Growth	12.4%	<6%>

- Growth would not last (Measure A)
- Created Reserve for Economic Uncertainty Fund
- Combination of increased labor costs, additional positions, new programs/facilities coupled with revenue slow down results in structural budget deficit

San Joaquin, Stanislaus, & Merced County "Top 3 Counties in the Country" for home foreclosures

Area worst in foreclosures — again

San Joaquin, Stanislaus, Merced tops; national rate is improving

By CHRISTINA SALERNO

San Joaquin, Stanislaus and Merced counties again topped the list for the areas with the highest foreclosure rates in the nation, according to statistics released Wednesday.

RealtyTrac's November statistics show San Joaquin County leading the nation in foreclosure filings, followed by Stanislaus County at No. 2 and Merced County at No. 3.

Foreclosure filings include notices of default, notices of trustee sale and properties repossessed by lenders.

One out of every 99 San Joaquin County households had foreclosure filings last month — more than six times the national average.

The numbers aren't much better in Stanislaus County, with one foreclosure filing for every 104 households. In Merced County, it's one for every 106 households.

The Northern San Joaquin Valley counties have been at or near the top of the foreclosure ranking every month for about a year. In October, Merced County ranked first, with San Joaquin second and Stanislaus third.

The bright spot in November's data is that national foreclosures filings are down 10 percent from the previous month. The national foreclosure rate for the month was one foreclosure filing for every 617 households.

"The 10 percent drop in November is the first double-digit monthly decrease we've seen since April 2006," said James J. Saccacio, chief executive officer of RealtyTrac, in a news release.

That could be an indication that foreclosure activity has topped out for the year, he said, but experts are anticipating a "seasonal surge" early next year with another wave of resetting mortgages.

California recorded 39,992 properties with foreclosure filings in November. That's more than any other state, ... a 21 percent decrease from the previ...

Nationwide, there ... with foreclosure fili...

To comment, click on ... modbee.com. See ... be reached at csal...

HOUSING

IN Turmoil

For coverage of the ...

County braces for drop-off in property taxes

By Zachary K. Johnson

STOCKTON - Years of growth in property tax revenue appears to be grinding to a halt as the slowed housing market and mortgage crisis have ...

Flat home prices – less property tax to cities and counties

Economists project a 50% chance of recession in 2008

Economic Commentary

mbia

Market Commentary for November 2007

Although the U.S. economy grew at a faster than expected pace in the third quarter gross domestic product was revised upward from 3.9 percent to 4.9 percent), the risk of an economic slowdown is increasing. Even the increased growth rate carries with it some negative news, as most of the surge was attributable to a jump in exports driven by a weaker dollar. Forecasts for fourth quarter growth are down substantially, in the 1 percent range.

Prior concerns regarding a weaker consumer remain and have been augmented by deteriorating news on the previously strong business front. Combined, these concerns have caused economists to raise their estimates for the likelihood of a recession to nearly 50 percent. On the consumer front, housing woes, high energy costs, and increasing financing costs have caused confidence to dip to its lowest level since late 1992. Although under pressure, the consumer is not dead yet as consumer spending and retail sales increased modestly in October (0.2 percent), and personal income grew by the same amount. The employment situation has held up reasonably well so far, but recent figures have exhibited weakness around the edges.

Reinforcing the concerns on the consumer front, corporate profits have already entered into recessionary territory, with third quarter profits for S&P 500 firms falling almost 25 percent on a per-share basis (annual rate of $19.3 billion).

The deteriorating housing situation has been negatively impacting both the consumer and corporate America, particularly the financial industry. Existing home sales and new home sales were down 21 percent and 24 percent, respectively on a year-over-year basis. Inventories of existing homes, at 11 months, are at an all time high, while prices on new homes are down 13 percent year-over-year. Most forecasters are calling for a further 10 to 15 percent decline in housing prices before a trough is reached.

Homeowners are stressed in this environment with 12 percent of subprime mortgages in the US being delinquent by at least 60 days and 7 percent in foreclosure. These levels will likely rise as most subprime mortgages have not yet hit their interest rate resets, with most resetting in the first half of 2008.

Help on the way?

Top officials at the Federal Reserve have recently made public statements that have led investors to believe that they will cut interest rates again next month, despite signaling that they would hold off on further rate cuts in a late October Federal Open Market Committee (FOMC) statement. Fed Chairman Ben Bernanke acknowledged in November that there has been "renewed turbulence in financial markets, which has partially reversed the improvement that occurred in September and October." He also noted that the Fed was paying "particular attention to the question of how strains in financial markets might affect the broader economy." Helping the Fed consider a rate ease, inflationary indicators have all been muted, with the 12-month core personal consumption expenditures (PCE) index remaining under 2 percent (1.9 percent in October). And although the dollar hit an all-time low vis-a-vis the euro, it has not had a marked effect on inflation.

On the subprime mortgage front, Treasury Secretary Henry Paulson recently expressed confidence that a government-bank co-sponsored mortgage bailout will be structured in the first half of December, hopefully easing mortgage defaults. It is anticipated that many of the adjustable rate mortgages that are reaching resets will be locked at, or near, their current levels.

Spin off effects of real estate market being felt across industries – For Tracy – this has resulted in a decline in sales tax

NEW YORK (CNNMoney.com) -- The United States is deep in its worst housing slump since the Great Depression, and according to a new report, it's not going to get better any time soon.

In a new survey, Moody's Economy.com says many metro areas will record losses of 20 percent or more during the downturn, with the national median price for single-family homes dropping 13 percent through 2009. Factoring in discount offers from sellers, the actual price decline would be well over 15 percent.

Eighty of the 381 metro areas covered by the report will record double-digit losses, according to the report. Most of the worst-hit markets are in once high-flying areas, such as California and Florida.

The steep losses were bound to arrive sometime. Throughout the housing slump, which began in the Spring of 2006, experts kept expecting prices to tumble, but it wasn't until recently that they dropped substantially according to Mark Zandi, chief economist for Moody's Economy.com.

"There has been a sea change in seller psychology since the subprime shock this summer," he said. "Some now realize they have to drop their prices to make a sale and prices are coming down very rapidly in some markets.“

Pain Street USA: ’08 housing outlook

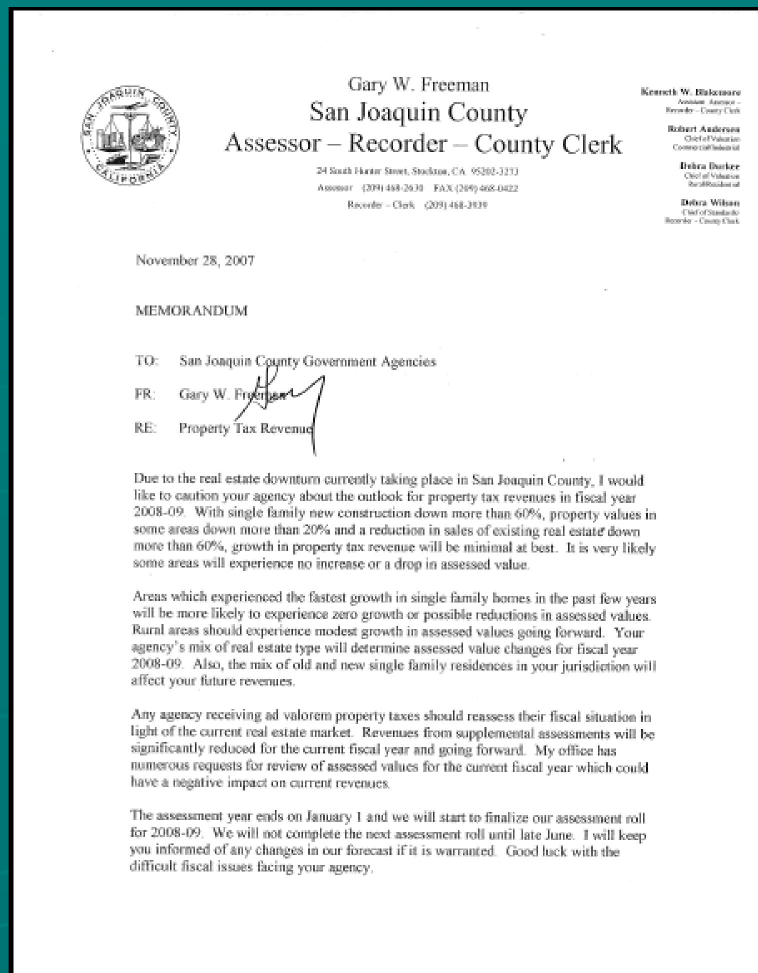
The forecast is for a longer, deeper home-price slump than previously expected, with double-digit declines in many markets. By Les Christie, CNNMoney.com staff writer

The housing slump will have a substantial impact on the overall economy, according to Moody's, which will depress real gross domestic product by more than a percentage point this year and by 1.5 percentage points in 2008.

Home prices are being pulled down by an even more severe decline in home sales, which Moody's expects to bottom out in early 2008, when unit sales will be down more than 40 percent from their peak. Home builders continued to add to inventory even as the slump got well under way, contributing to what an 11-month back-log of homes for sale, according to the National Association of Realtors. Many of these homes are sitting completely empty: The Census Bureau reported a total of 2.1 million v homes for sale. Vacant homes add pressure on prices because owners of these houses are usually more willing to slash prices to move the properties. They cost out-of-pocket cash each month while providing neither income nor shelter. Even though home construction has now contracted severely - the Census Bureau reported Tuesday that housing starts were down to an annualized rate of 1.187 million units in November, the lowest in 16 years yet it will take time to work through the excess inventory.

Other metro areas expected to go through crushing price drops include: Stockton, Calif., where prices are forecast to drop 31.6 percent, Modesto, Calif. (-31.3 percent), Fort Walton Beach, Fla. (-30.4 percent) and Naples, Fla. (-29.6 percent).

County Assessor – Warns that property tax revenue will be flat or will fall due to declining home valuations



Gary W. Freeman
San Joaquin County
Assessor – Recorder – County Clerk

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Kenneth W. Blakemore

Robert Anderson

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Debra Wilson

November 28, 2007

MEMORANDUM

TO: San Joaquin County Government Agencies

FR: Gary W. Freeman

RE: Property Tax Revenue

Due to the real estate downturn currently taking place in San Joaquin County, I would like to caution your agency about the outlook for property tax revenues in fiscal year 2008-09. With single family new construction down more than 60%, property values in some areas down more than 20% and a reduction in sales of existing real estate down more than 60%, growth in property tax revenue will be minimal at best. It is very likely some areas will experience no increase or a drop in assessed value.

Areas which experienced the fastest growth in single family homes in the past few years will be more likely to experience zero growth or possible reductions in assessed values. Rural areas should experience modest growth in assessed values going forward. Your agency's mix of real estate type will determine assessed value changes for fiscal year 2008-09. Also, the mix of old and new single family residences in your jurisdiction will affect your future revenues.

Any agency receiving ad valorem property taxes should reassess their fiscal situation in light of the current real estate market. Revenues from supplemental assessments will be significantly reduced for the current fiscal year and going forward. My office has numerous requests for review of assessed values for the current fiscal year which could have a negative impact on current revenues.

The assessment year ends on January 1 and we will start to finalize our assessment roll for 2008-09. We will not complete the next assessment roll until late June. I will keep you informed of any changes in our forecast if it is warranted. Good luck with the difficult fiscal issues facing your agency.

Neighboring cities have already experienced significant impacts

–

taking serious measures to address budget deficits

Cops and fire staff take city budget hit

Workers compensation and cable fee targeted as council seeks $8.6M savings

Police, fire and parks staffing will diminish through attrition to shore up Modesto's budget with $8.6 million in cuts to city departments. The Police Department will lose 25 officers and nine civilian posts, drawing down its sworn ranks to about 260.

2. General Fund Review at Mid-Year

	FY 07-08 Budget	Mid-Year Estimate
Beginning Fund Balance	$19,987,090	$19,111,270
Revenues exclusive of transfer in	$48,658,380	$46,821,130
Transfers in (Economic Uncertainty)	$5,733,000	$5,733,000
Expenses	-$54,391,330	-$52,713,618
Ending Fund Balance	$19,987,140	$18,951,782

Major Concerns for FY 07-08

- Revenues are down $3 million
- Partially offset by one time GASB 31 adjustment
- Expenses less than budget help
- Final result, City will spend $6 million more than it takes in during FY 07-08 ($7.5 million more if GASB 31 were not counted)
- Economic Uncertainty will drop from $19 to $13 million

3. Three Year Projection of General Fund Budgets

	FY 08-09	FY 09-10	FY 10-11
Beginning G. F. Bal	$18,951,780	$18,951,780	$11,005,077
Beginning E. U. Fund Bal	$13,300,000	$ 3,651,600	$ 0
Revenues	$47,279,230	$47,846,500	$48,749,400
Expenses	$56,927,630	$59,444,803	$62,374,263
Deficit	$ 9,648,400	$11,598,303	$13,624,863
Ending G. F. Bal	$18,951,780	$11,005,077	-$2,619,786
Ending E. U. Fund Bal	$ 3,651,600	$ 0	$ 0

- Continuing with existing base City budget results in structural budget deficit
- Because revenues are flat structural budget deficit grows each year
- Both General Fund Reserve and Economic Uncertainty fund would be exhausted within 3 years

Review of Property and Sales Tax

	FY 88-89	FY 89-90	FY 90-91	FY 91-92	FY 92-93	FY 93-94
Property Tax	$2,295,047	$2,798,779	$3,545,389	$3,999,515	$3,944,625	$4,067,714
Sales Tax	$1,994,746	$2,314,591	$2,379,017	$2,213,747	$2,478,392	$2,598,885

Similar 90-91 Rebound Not Likely

- In 90-91 property tax growth came back as a result of new residential construction
- Measure A limits will prevent similar rebound
- In 90-91 new construction also resulted in new commercial (sales tax) development
- Gruen and Gruen Economic Report notes link between non-growing community and commercial investment
- City has to compete with surrounding communities for sales tax

4. Short and Long Term Strategy to Address City's Structural Budget Deficit

Benefit of Strategy

- Every action taken today has a beneficial ripple effect in years to come
- Steps taken today do not have to be draconian
- Without action taken at present will mean far more draconian actions necessary later

Assumptions

- Inflation and labor costs drive base budget at faster pace than increase to revenues
- Available reserves exhausted within 3 years
- Property tax remains static for next 3 years
- Limited sales tax growth potential
- Real estate and related mortgage issues and foreclosures and their effects are unknown

Short Term Strategy

- 1st priority - existing services and service levels
- No new programs and no expansion of existing programs or new full time staffing
  - Unless corresponding reduction is made
- Historical spending averages (i.e. vacancies) may be considered
- City Manager to manage personnel resources
  - Case by case basis for non-public safety positions
  - Public safety positions continued to be filled

Without implementing short term budget strategy measures:

	FY 08-09	FY 09-10	FY 10-11
Deficit	-$ 9,648,400	-$11,598,303	-$13,624,863
Ending E.U. Fund Bal	$ 3,651,600	$ 0	$ 0
Ending G.F. Bal	$18,951,780	$11,005,077	-$ 2,619,786

With implementing short term budget strategy measures:

	FY 08-09	FY09-10	FY 10-11
Deficit (estimated/actual)	-$ 5,748,530	-$ 7,519,908	-$9,304,688
Ending E.U. Fund Bal	$ 7,551,470	$ 31,562	$ 0
Ending G.F. Bal	$18,951,780	$18,951,780	$9,678,654

Long Term Strategy
Internal Budget Committee will examine:

- Revenue strategies such as fee studies
- Examine current service delivery models
- Review high cost, low participatory programming
- Review capital improvement projects for future operating costs
- Review expenditure controls and funding
- Use Reserve for Economic Uncertainty Fund first over next 3 years minimizing any impact to General Fund Reserves
- Establish a minimum General Fund Reserve

CONCLUSION

- Long term actions will be necessary to address the General Fund structural budget deficit and to address new community needs such as public safety
- Short term actions will be necessary to avoid potential draconian actions later