

Finance MEETING

12/06/2022

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FY 2024 – FY 2033 LONG RANGE FINANCIAL FORECAST

Finance Committee Item #4

DECEMBER 6, 2022

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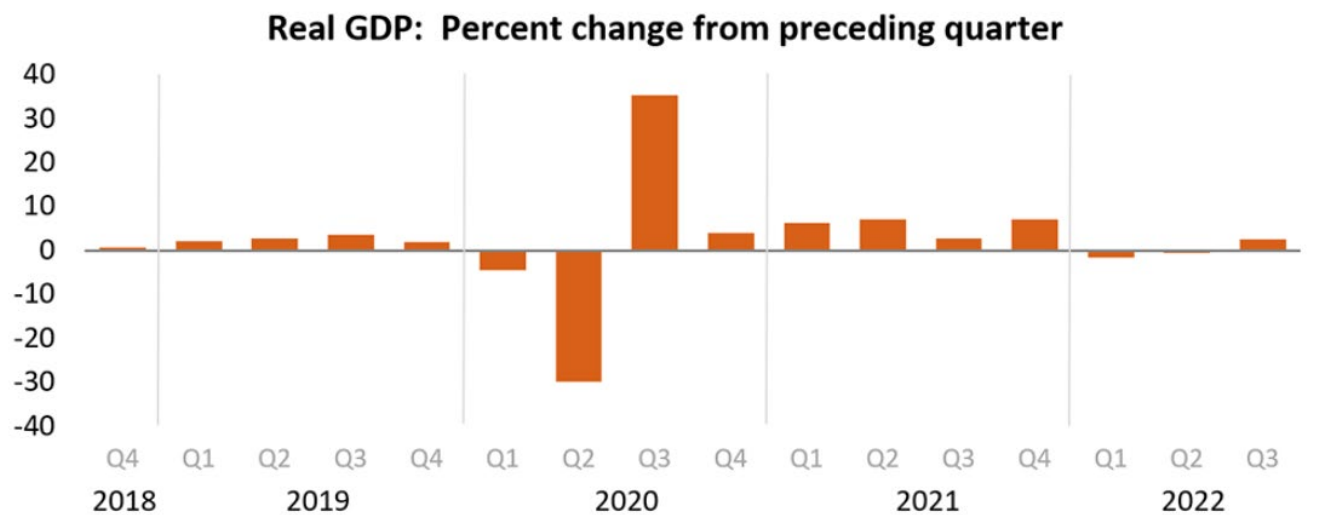
OVERVIEW

- Stagnant economy assumed for major tax revenues
 - Some tax categories remain below pre-pandemic levels
- Both Measure L (natural gas transfer) and K (new business tax) are expected to be successful in gaining voter approval
 - Measure L: IS assumed in the Base Case
 - Measure K: IS NOT assumed in Base Case, this is an alt scenario
- Expense projections based on current approved service levels
 - Assumes 2 yr budget strategy adopted transitions to ongoing
 - Cost of labor and priority service restorations are key factors in budget development
- One-time surplus in FY 2022 and estimated in FY 2023
 - New ballot measure revenues are key to ensure fiscal stability

THE ECONOMY

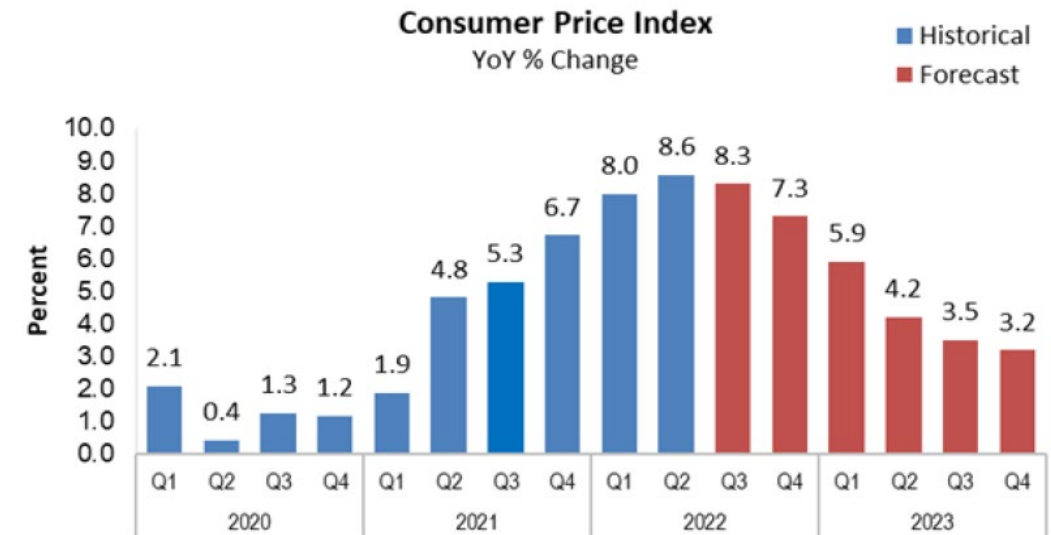
Local economy continues to show strong performance in the latter half of calendar year 2022 though signs of “headwinds” are growing that would stall the economy.

California Legislative Analyst's Office (LOA) forecasting in line with Palo Alto between a pessimistic view, recession caused by inflation and high interest rates, and optimistic view, "soft landing" created by interest rates taming the inflation.



U.S. Bureau of Economic Analysis

Seasonally adjusted annual rates



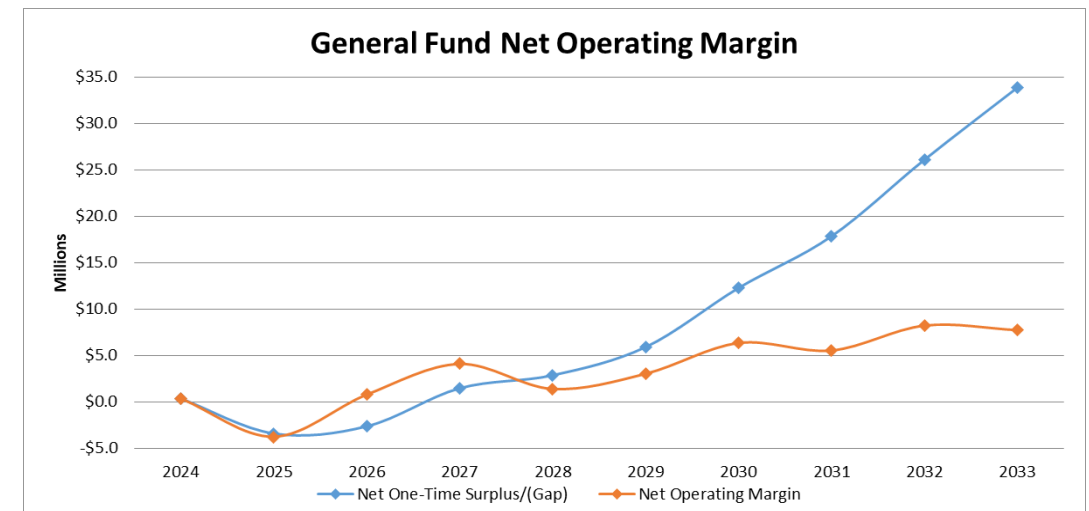
Source: US. Bureau of Labor Statistics; BOTW Economics

FISCAL YEAR 2024 - 2033 BASE CASE FORECAST

BASE CASE

	Actual 2022	Adopted 2023	Projected 2023	2024	2025	2026	2027	2028	2029	2030	2031	2032	2033
Total Revenue	\$238,735	\$237,751	\$238 - 244M	\$251,177	\$261,671	\$272,065	\$282,203	\$290,671	\$302,477	\$313,495	\$325,552	\$337,689	\$351,101
BSR Contribution (One-Time)	-	\$9,670	\$9,670	-	-	-	-	-	-	-	-	-	-
Total Source of Funds	\$238,735	\$247,421	\$247 - 253M	\$251,177	\$261,671	\$272,065	\$282,203	\$290,671	\$302,477	\$313,495	\$325,552	\$337,689	\$351,101
<i>Year over Year increase (revenue only)</i>				5.6%	4.2%	4.0%	3.7%	3.0%	4.1%	3.6%	3.8%	3.7%	4.0%
Total Expenditures	\$197,963	\$247,421	\$247,421	\$250,814	\$265,083	\$274,694	\$280,726	\$287,794	\$296,558	\$301,197	\$307,685	\$311,557	\$317,193
Total Use of Funds	\$197,963	\$247,421	\$247,421	\$250,814	\$265,083	\$274,694	\$280,726	\$287,794	\$296,558	\$301,197	\$307,685	\$311,557	\$317,193
<i>Year over Year increase</i>				1.4%	5.7%	3.6%	2.2%	2.5%	3.0%	1.6%	2.2%	1.3%	1.8%
Net One-Time Surplus/(Gap)	\$40,772	(\$0)	\$0 - 6M	\$364	(\$3,412)	(\$2,629)	\$1,478	\$2,877	\$5,919	\$12,298	\$17,867	\$26,132	\$33,908
Cumulative Net Operating Margin (One-Time)													\$94,803
Net Operating Margin				\$364	(\$3,776)	\$783	\$4,107	\$1,399	\$3,042	\$6,379	\$5,570	\$8,265	\$7,776
Cumulative Net Operating Margin													\$33,908

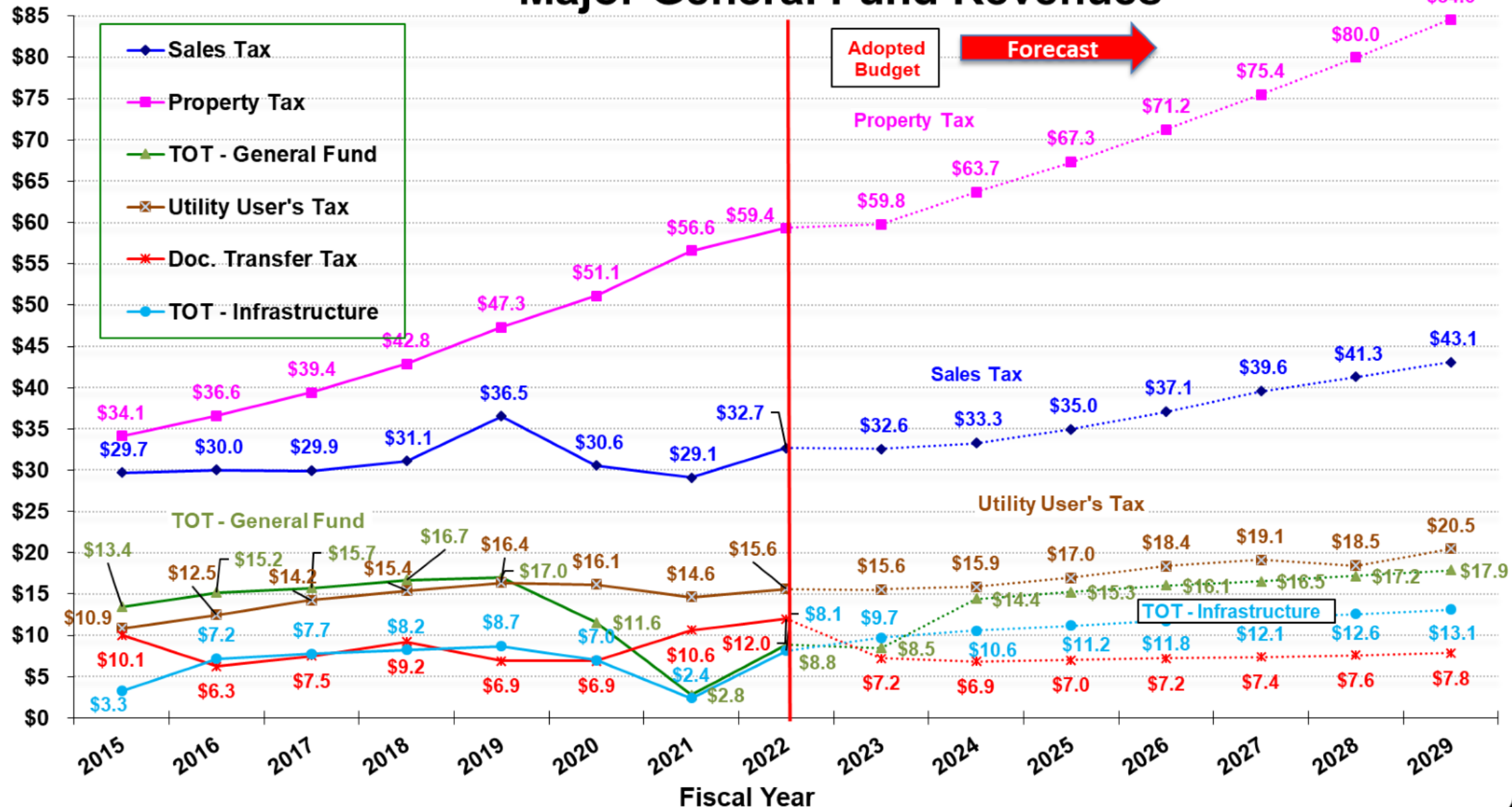
- Fluctuation stabilizes in FY 2027
- Mild 18-month stagnation at start of forecast
- Measure L (natural gas transfer) included along with services to be funded by these revenues
- One-time resources that have boosted the financial outlook are eliminated



MAJOR TAX REVENUE PROJECTIONS

Millions

Major General Fund Revenues





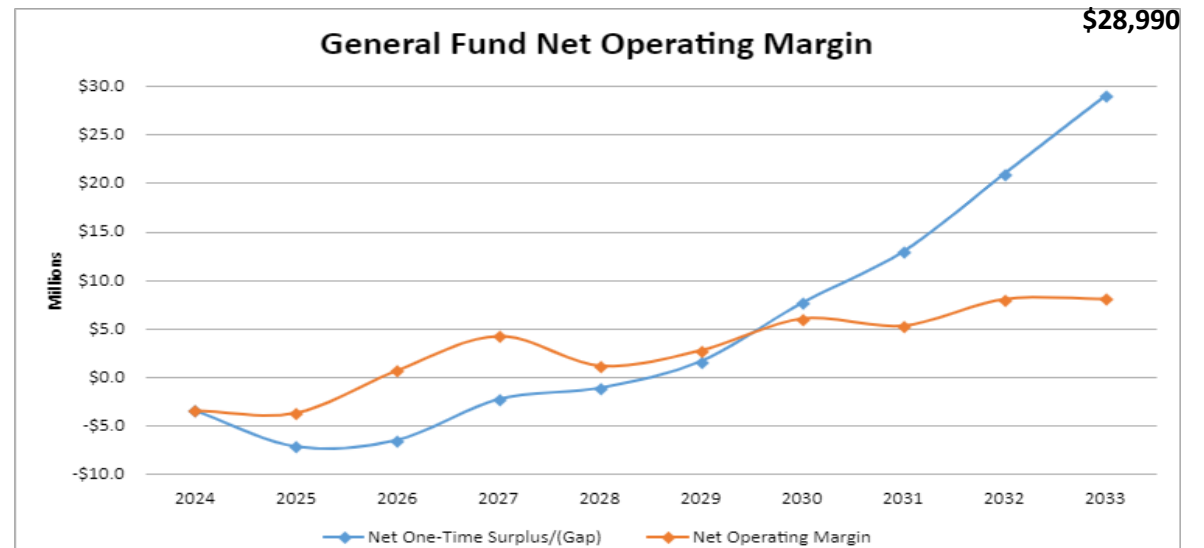
ASSUMPTIONS NOT INCLUDED IN FORECAST

- Restoration of Services to Pre-Pandemic Levels
- Labor Negotiations (all contracts near expiration); LRFF includes an estimated level of reserve to reach target market placement
- Capital Improvements: Parks Master Plan, Animal Shelter Rebuild, Railroad Grade Separation, Fire Training Center
- Cubberley Community Center Concept Plan and Gym Repair
- Increased Resources for Council Priority Items:
 - Sustainability and Climate Action Plan (S/CAP)
 - Project Homekey
 - Racial Equity Work
 - Permanent Parklet Program

ALTERNATE SCENARIO A: MODERATE RECESSION

	Actual 2022	Adopted 2023	Projected 2023	2024	2025	2026	2027	2028	2029	2030	2031	2032	2033
Total Revenue	\$238,735	\$237,751	\$238 - 241M	\$247,033	\$257,588	\$267,881	\$278,113	\$286,327	\$297,822	\$308,476	\$320,223	\$332,101	\$345,783
BSR Contribution (One-Time)	-	\$9,670	\$9,670	-	-	-	-	-	-	-	-	-	-
Total Source of Funds	\$238,735	\$247,421	\$247 - 250M	\$247,033	\$257,588	\$267,881	\$278,113	\$286,327	\$297,822	\$308,476	\$320,223	\$332,101	\$345,783
<i>Year over Year increase (revenue only)</i>				3.9%	4.3%	4.0%	3.8%	3.0%	4.0%	3.6%	3.8%	3.7%	4.1%
Total Expenditures	\$197,963	\$247,421	\$247,421	\$250,507	\$264,764	\$274,361	\$280,385	\$287,445	\$296,196	\$300,826	\$307,298	\$311,154	\$316,793
Total Use of Funds	\$197,963	\$247,421	\$247,421	\$250,507	\$264,764	\$274,361	\$280,385	\$287,445	\$296,196	\$300,826	\$307,298	\$311,154	\$316,793
<i>Year over Year increase</i>				1.2%	5.7%	3.6%	2.2%	2.5%	3.0%	1.6%	2.2%	1.3%	1.8%
Net One-Time Surplus/(Gap)	\$40,772	\$0	\$0 - 3M	(\$3,474)	(\$7,176)	(\$6,481)	(\$2,272)	(\$1,118)	\$1,626	\$7,650	\$12,925	\$20,947	\$28,990
Cumulative Net Operating Margin (One-Time)													\$51,617
Net Operating Margin				(\$3,474)	(\$3,703)	\$696	\$4,209	\$1,154	\$2,745	\$6,023	\$5,275	\$8,022	\$8,043
Cumulative Net Operating Margin													\$28,990

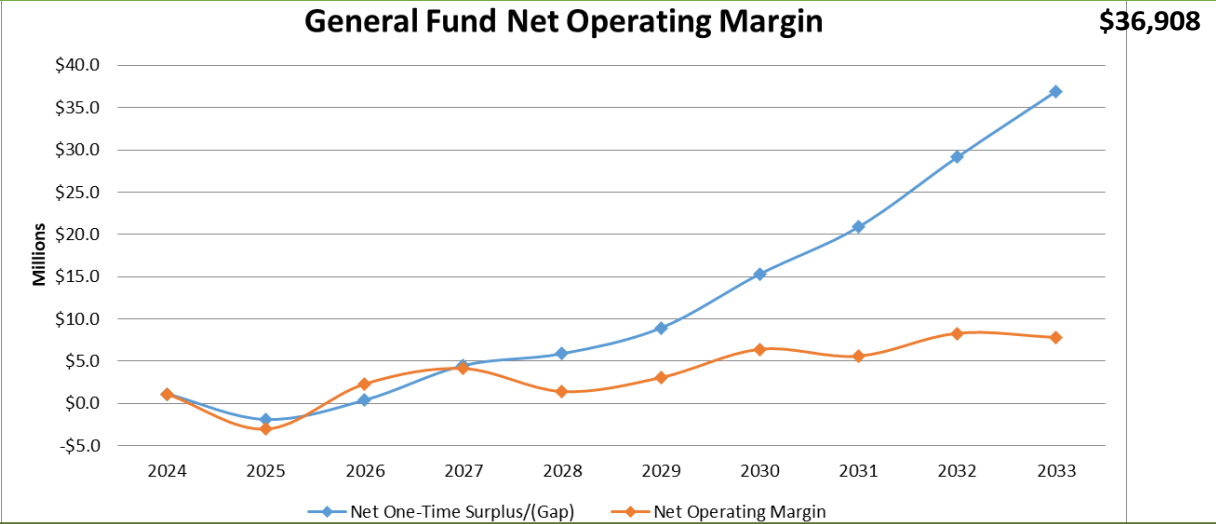
Models the impact of a moderate recession that assumes slower growth of major tax revenues.



ALTERNATE SCENARIO B: MEASURE K FUNDING

	Actual 2022	Adopted 2023	Projected 2023	2024	2025	2026	2027	2028	2029	2030	2031	2032	2033
Total Revenue	\$238,735	\$237,751	\$238 - 244M	\$251,177	\$261,671	\$272,065	\$282,203	\$290,671	\$302,477	\$313,495	\$325,552	\$337,689	\$351,101
BSR Contribution (One-Time)	-	\$9,670	\$9,670	-	-	-	-	-	-	-	-	-	-
Measure K (eligible funds)	-	-	-	\$750	\$1,500	\$3,000	\$3,000	\$3,000	\$3,000	\$3,000	\$3,000	\$3,000	\$3,000
Total Source of Funds	\$238,735	\$247,421	\$247 - 253M	\$251,927	\$263,171	\$275,065	\$285,203	\$293,671	\$305,477	\$316,495	\$328,552	\$340,689	\$354,101
Year over Year increase (revenue only)				5.6%	4.2%	4.0%	3.7%	3.0%	4.1%	3.6%	3.8%	3.7%	4.0%
Total Expenditures	\$197,963	\$247,421	\$247,421	\$250,814	\$265,083	\$274,694	\$280,726	\$287,794	\$296,558	\$301,197	\$307,685	\$311,557	\$317,193
Total Use of Funds	\$197,963	\$247,421	\$247,421	\$250,814	\$265,083	\$274,694	\$280,726	\$287,794	\$296,558	\$301,197	\$307,685	\$311,557	\$317,193
Year over Year increase				1.4%	5.7%	3.6%	2.2%	2.5%	3.0%	1.6%	2.2%	1.3%	1.8%
Net One-Time Surplus/(Gap)	\$40,772	\$0	\$0 - 6M	\$1,114	(\$1,912)	\$371	\$4,478	\$5,877	\$8,919	\$15,298	\$20,867	\$29,132	\$36,908
Cumulative Net Operating Margin (One-Time)													\$121,053
Net Operating Margin				\$0	\$1,114	(\$3,026)	\$2,283	\$4,107	\$1,399	\$3,042	\$6,379	\$5,570	\$8,265
Cumulative Net Operating Margin													\$7,776
													\$36,908

Assumes the use of approximately 30% of revenues generated from Measure K (Business Tax Funding) to offset known eligible expenses.



FY 2024 BUDGET DEVELOPMENT GUIDELINES

- Develop a structurally balanced budget that aligns ongoing revenues and expenses and allocates one-time resources for one-time needs.
- Ensure appropriate resource allocation for City Council's identified priorities.
- Focus on business process redesign and explore alternative service delivery models to minimize overlap, maximize cost share, and effectively use resources.
- Examine the use of existing revenue sources to fund current services and incorporate the addition of new revenue sources as directed by the City Council.
- Continue to prioritize proactively funding long term liabilities including but not limited to debt obligations, pension obligations, and capital infrastructure.

CONCLUSION AND NEXT STEPS

- Revenue trends indicate continued economic recovery; however, signs of recession are looming
- City is positioned to manage the uncertain outlook; base case & alternative scenarios are key to assist in organization planning
 - Focus on investing only in key areas of priority or urgent needs
 - Moderate Recession causes longer gap through FY 2028
 - Measure K Funding and one-time surpluses are critical to manage the near- and long-term fiscal sustainability
- FY 2023 Mid-Year will include recommendations for addition of key resources and appropriation of funds as directed by Council

Next Steps Annual Budget Process

- *Jan 2023:* Council review LRFF
- *Feb 2023:* FY 2023 Mid-Year Budget
- *May 2023:* FY 2024 Proposed Budget

RECOMMENDED ACTION

Staff recommends that the Finance Committee:

Review and recommend that the City Council accept the Fiscal Year 2024 – 2033 Long Range Financial Forecast Base Case and the FY 2024 Budget Development Guidelines (Attachment A).

Direct staff to use this forecast as a starting point for the FY 2024 budget process.



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