MEMORANDUM

City of Campbell

Finance Department

To: City Council

Date: November 8, 2021

From: Will Fuentes, Finance Director

Via: Brian Loventhal, City Manager

Subject: Monthly Fiscal Update for October 2021

BACKGROUND

The current report before City Council is in a series of monthly fiscal updates that was recommended by staff during the Fiscal Year (FY) 2022 budget preparation process and is similar to report provided to Council during FY 2021. A prior monthly update was presented to Council at a regular meeting on September 21, 2021. The current report will provide the following:

- An update on Property Tax for FY 2022
- An industry sector by industry sector update on Sales Tax for Quarter 4 (Q4) (April to June) of FY 2021
- A current update on Transient Occupancy Tax through August 2021
- An economic update

This report is being presented as an informational memo only since limited financial data is available at this time for FY 2022. A full monthly fiscal update will be provided to Council at the February 1, 2022 regular meeting and will largely discuss mid-year fiscal results. The last full monthly report was again provided to Council at the September 21 regular meeting and largely discussed un-audited year-end results for FY 2021. All other monthly fiscal updates will be provided as informational memos or integrated into reporting for the FY 2023 budget process. Staff is also working this fiscal year to implement an online financial reporting module and will notify Council when it is available to view.

DISCUSSION

FY 2022 Property Tax Update[1]

Property Tax is the City's largest revenue source and as shared on September 21, Un-audited year-end Property Tax for FY 2021 equaled $17.95 million; $686,000 greater than previous estimates and $702,000 or 4.07% greater than FY 2020. This was caused by a strong housing market, increasing sales prices, increased sales activity, and better than

[1] Data and information provided through a consulting services with HdL Coren & Cone (HdLCC) - https://www.hdlcompanies.com/services/property-tax

expected Educational Revenue Augmentation Fund (ERAF) monies sent to the City by Santa Clara County via Property Tax payments.

In FY 2022, the City of Campbell experienced a net taxable value increase of 4.8% for the FY 2022 tax roll and this is reflected in the FY 2022 Adopted Budget. The increase also mirrored the increase experienced countywide at 4.6%. The assessed value increase between FY 2021 and FY 2022 was $564 million. The change attributed to the 1.036% Proposition 13 inflation adjustment was $110 million. That accounted for 19% of all growth experienced in the City. Please note that annual Proposition 13 inflation adjustments are normally set at a maximum rate of 2.0%, but the adjustment for FY 2022 is less due to a Consumer Price Index (CPI) adjustment that was less than 2.0% when the tax roll for FY 2022 was finalized. Based on current inflationary factors, staff feels that the Proposition 13 adjustment will be set at the maximum of 2.0% for FY 2023.

The largest secured roll increases were reported on two parcels owned by 675 Creekside Owner LLC. at 675 Creekside Way and a vacant site at 705 Creekside Way with a combined positive change of $35.9 million after this property transferred ownership in 2020 on a sale price of $139 million. The commercial property is office space where 8X8 leases the site as its corporate headquarters. Commercial property at 1995 S Bascom Avenue owned by Campbell Foothills Venture LLC posted an increase of $19.3 million after additional improvement and personal property assets were added to this location between tax years. This is the location of the DoubleTree Hotel by Hilton. Residential property owned by Robson Homes LLC at 16179 E Mozart Avenue reported an increase of $13.8 million after this property was purchased last year for $14.0 million. This is a vacant site with plans to develop 25 single family residential homes.

The largest reduction was posted on commercial property at 1660 S Winchester Blvd owned by JMM Winchester Hamilton, which declined $1.8 million. This is the location of the Walgreens Drug Store. There are appeals pending on this location which may have been stipulated for this reduction.

Growth in home sales strengthened in the summer of 2020 and many cities saw an increase in properties for sale. Sales price increases in 2020 were reflected on the FY 2022 tax rolls. North Bay counties saw mild declines in median prices in late 2019 and early 2020 and Southern California counties saw a flattening of prices in many areas. Homes prices increased in the second half of 2020. Sale prices grew due to low inventory and the declining mortgage rates. These conditions have continued to cause prices to rise in 2021. The median sale price of a detached single family residential home in Campbell from January through August 2021 was $1,647,500. This represents a $197,500 (13.62%) increase in median sale price from 2020. ***Table A*** below provides a history of sales and median price for detached single family residential homes from calendar year 2015 to 2021:

Table A – History of Detached Single Family Residential (SFR) Home Sales 2015 to 2017

Year	Sales Quantity	Median Price	% Change
2015	325	$1,025,000	
2016	283	$1,125,000	9.76%
2017	365	$1,300,000	15.56%
2018	283	$1,450,000	11.54%
2019	256	$1,375,000	(5.17%)
2020	263	$1,450,000	5.45%
2021	250	$1,647,500	13.62%

While a reduction in the number of single-family home sales was experienced in many areas and sales price changes reflected modest declines or increases in 2019 and early 2020, these market trends were impacted by COVID-19 beginning in March 2020. The number of home sales plummeted as potential buyers stayed home. After major reductions in the number of sales in April and May, sales of detached SFR rebounded and statewide the number of sales increased by 3.5% over 2019. Statewide, the median sales prices for July 2021 increased by 21.74% over July 2020 and were up by 33.42% over July 2019. The statewide median time on the market for detached SFR was 8 days in July 2021. The 30-year, fixed-mortgage interest rate averaged 2.71% as of September 2, 2021 down from 3.16% in June 2020.

The COVID-19 pandemic inhibited property sales in the first quarter of 2020, but for most communities it did not significantly impact FY 2022 assessed value growth from transfers of ownership. The stay-at-home orders, business closures, and other economic impacts affected FY 2022 growth by reducing the annual CPI adjustment from the maximum 2% to 1.036%. New construction already underway did not see a decline, however, the shortages of building materials affected new construction starts in the second half of the 2020 and into 2021.

For reference, ***Table B*** below shows the Top 10 Property Owners within Campbell for FY 2022. Unlike business specific sales tax data, this information is not confidential:

Table B – Top 10 Property Owners

Rank	Owner	Net Taxable Value	% of Total	Use Type
1	PRUNEYARD REGENGY LLC	$214,701,500	1.74%	Commercial
2	PRUNEYARD OFFICE INVESTORS LLC	$162,005,163	1.31%	Commercial
3	AG-SW HAMILTON PLAZA OWNER LP	$149,829,510	1.21%	Commercial
4	675 CREEKSIDE OWNER LLC	$140,440,038	1.14%	Commercial
5	REVRES LLC	$124,958,985	1.01%	Residential
6	PARC RESIDENCES LLC	$110,931,615	0.90%	Residential
7	KW FUND VI VASONA MEDICAL TECHNOLOGY PK	$110,931,615	0.83%	Industrial
8	CAMPBELL TECHNOLOGY PARK LLC	$85,894,673	0.69%	Industrial
9	RAILWAY CAMPBELL LLC	$70,499,682	0.57%	Residential
10	SHI-III CAMPBELL LP	$70,497,287	0.57%	Recreational
	Top Ten Total	$1,232,820,092	**9.96%**	

FY 2021 Q4 Business Sector Sales Tax Update

The City receives Sales Tax payments from the California Department of Tax and Fee Administration (CDTFA) over the course a fiscal year through various monthly advances and quarterly cleanup payments. As illustrated in ***Table C*** below, Sales Tax payments owed to the City for Q4 of FY 2021 were fully remitted to the City by the end of August 2021; including any payments that the Governor allowed to be deferred until July 31, 2021 due to economic hardships caused by COVID-19:

Table C – Timing of Sales Tax Activity and Payments for FY 2021 and FY 2022

Quarter	Sales Activity	Final Cleanup Payment	Business Sector Details Avail.
Q3 FY 2021	Jan – Mar 2021	Late May 2021	Jul 2021
Q4 FY 2021	Apr – Jun 2021	Late August 2021	Oct 2021
Q1 FY 2022	Jul – Sep 2021	Late November 2021	Jan 2022
Q2 FY 2022	Oct – Dec 2021	Late February 2022	Apr 2022

As reported on September 21, through the end of FY 2021, the City recorded $14.4 million in total Sales Tax revenues. This was comprised of:

1.00% City Share of Base Sales Tax:	$11,203,345
0.25% City Sales Tax Add On:	2,872,069
City Share of Prop 172 Public Safety Sales Tax:	402,635
Total of Sales Tax Receipts:	**$14,478,049**

Sales Tax receipts for FY 2021 were approximately 7% higher than Sales Tax receipts for FY 2020; which were significantly and negatively impacted by the COVID-19 pandemic in the last quarter of that fiscal year.

Table D below provides an industry sector by industry sector comparison for the City's share of base sales tax for Q4 FY 2021 and largely represents brick-and-mortar business activity within Campbell for that period:

Table D – Industry Sector Comparison of Base Sales Tax for Q4 FY 2021[2]

Business Sector	Count	Q4 FY 2021	Q4 FY 2020	Q over Q $∆	Q over Q %∆
TOTAL	**1,998**	**$2,970,520**	**$2,021,943**	**$948,577**	**46.9%**
State and County Pools	N/A	$586,775	$508,988	$77,787	15.3%
Restaurants and Hotels	210	$492,781	$238,498	$254,284	106.6%
Building and Construction	98	$480,907	$353,668	$127,239	36.0%
Business and Industry	624	$457,969	$317,555	$140,414	44.2%
General Consumer Goods	758	$426,066	$219,862	$206,204	93.8%
Fuel and Service Stations	22	$208,703	$121,629	$87,074	71.6%
Autos and Transportation	194	$161,227	$109,055	$52,172	47.8%
Food and Drugs	48	$149,290	$151,041	($1,751)	-1.2%
Transfers & Unidentified	44	$6,801	$1,646	$5,154	313.1%

As could be expected due to shelter in place orders, business closures, and decreased driving during Q4 FY 2020, Q4 FY 2021 was significantly better than one year ago in all industry sectors, with the exception of Food and Drugs, which saw a slight 1.2% decrease. Economic growth, fueled by pent up demand, rising consumer confidence, business re-openings, COVID-19 vaccines and other therapeutics, and government assistance, was evident for most all industry sectors within Campbell in Q4 FY 2021.

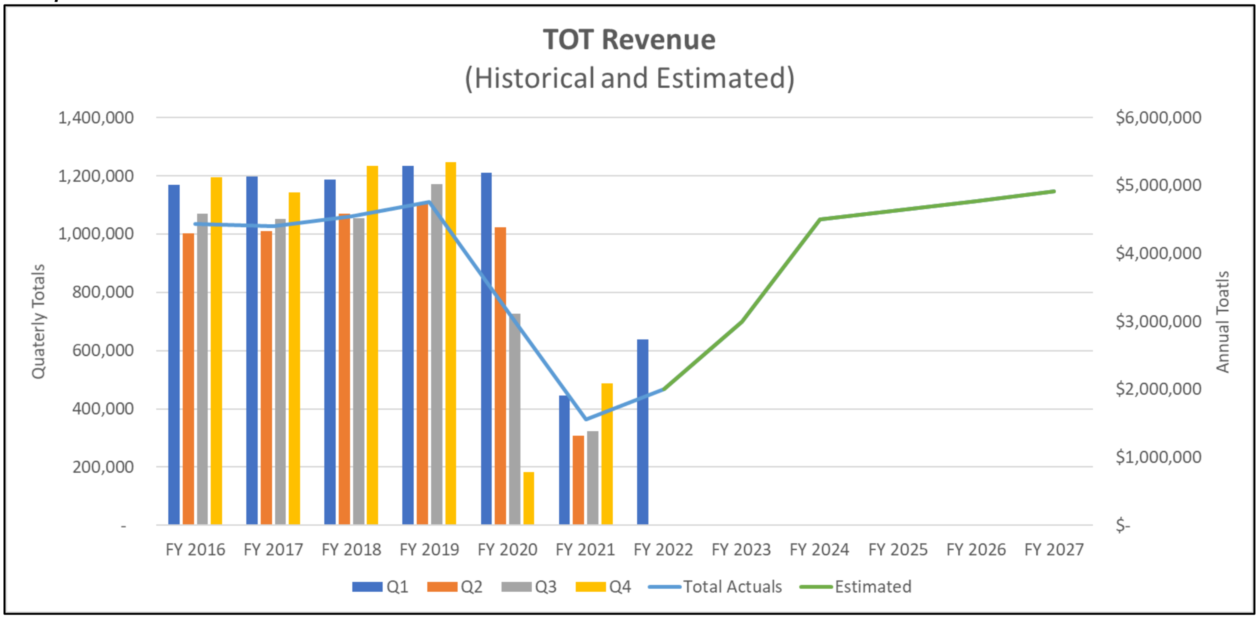
Transient Occupancy Tax (TOT) Update through August 2021

As has been previously discussed with Council, TOT is and remains one of the City's most vulnerable revenue sources due to COVID-19. Similar to hotels nationwide, Campbell hotels have seen a decline in recreational and business travel since March 2020. At the end of FY 2019, TOT revenue within Campbell equaled $4.8 million. However, by the end of FY 2020, those revenues had declined to $3.1 million. And by the end of FY 2021, TOT revenues had declined to $1.6 million. This was entirely due to the impacts of COVID-19 on travel and hotel stays within the period of March 2020 through June 2021, though some decline was happening even before this time as many companies started to restrict business travel in January and February 2020. And for FY 2022, the Adopted Budget includes estimated TOT of $2.0 million; a decline of approx. 58.3% since FY 2019.

Graph A below shows a year-by-year and quarter-by-quarter comparison of City TOT revenue since FY 2016:

[2] Data and information provided through a consulting services with HdL - https://www.hdlcompanies.com/services/sales-tax

Graph A – Historical and Estimated TOT Revenue



Nevertheless, while current TOT revenue is significantly lower than normal, it has seen a slight rebound in recent months. In Q1 FY 2022, City TOT revenue equaled $636,948. This was a 30.7% increase from Q4 FY 2021 TOT revenue, which equaled $487,199. And it was a 43.3% increase from the same period of Q1 in FY 2021, which equaled $444,371. While TOT remains an area of significant concern and will continue to be closely monitored by staff, there are some signs of recovery in the hospitality industry.

TOT revenue for FY 2022 was estimated to be $2.0 million in the Adopted Budget. Additionally, in the City's Seven-Year Financial Forecast, staff assumed a slow return to normal for TOT as shown in ***Table E*** below:

Table E – Forecasted TOT Revenue FY 2022 to FY 2028

	FY 2022	FY 2023	FY 2024	FY 2025	FY 2026	FY 2027	FY 2028
TOT	2,000,000	3,000,000	4,500,000	4,635,000	4,774,100	4,917,300	5,064,800

In order to meet the City's FY 2022 TOT revenue estimate of $2.0 million, TOT receipts will need to average $167,000 monthly. In FY 2019, the last normal year of TOT receipts, they averaged $397,000 monthly. Staff feels that FY 2022 TOT estimates are realistic given that Q1 FY 2022 receipts averaged $212,000 per month. Thus, staff does not recommend revising year-end projections at this time, but may during the mid-year fiscal update if actual results and trends are better or worse than expected.

Economic Update

The pace of economic growth appears to be moderating from a very high level, but the outlook for economic growth remains strong. Some economists have recently tempered their forecasts for economic growth through calendar 2021 year-end and 2022. The current Bloomberg consensus estimates for 2021 and 2022 US GDP growth are 5.7%

and 4.0%, respectively, which remain consistent with strong economic growth, and are well above the long-run trend growth rate of about 1.8%. Staff believes ongoing supply chain disruptions and the lingering impact of the pandemic are largely the reasons that GDP estimates have moderated, as these issues are now widely expected to persist into 2022. The Conference Board expects economic growth to remain strong but lowered their GDP forecasts last week and now expect 5.7% GDP growth for 2021 and 3.8% GDP growth in 2022 (down from 6.0% and 4.0%, respectively, last month). The Conference Board's Leading Economic Index (LEI) increased 0.2% month-over-month in September (below expectations), following a 0.8% increase in August. According to the Conference Board, the LEI's slower rate of growth in recent months suggests the economy is on a more moderate growth trajectory compared to the first half of the year.

Housing demand in the US appears to remain strong, but staff believes supply chain bottlenecks and high materials and input costs have recently held back the pace of new starts. Total housing starts nationwide declined 1.6% in September to an annual pace of 1,555,000. Permits nationwide also declined 7.7% in the month. Single-family starts nationwide were flat in September while multi-family starts nationwide fell 5.0%, month-over-month. Meanwhile, existing home sales nationwide rose 7.0% in September to a seasonally adjusted rate of 6.29 million units, exceeding expectations, following a 2.0% decline in August. The median resale price eased slightly in September which may have provided a boost to sales in the month, though prices nationwide were still up 13.3% year-over-year. Staff believes tight inventory remains supportive of home prices, despite a recent uptick in mortgage rates. The supply of existing homes for sale nationwide was down 13.0% year-over-year in September. The NAHB/Wells Fargo Housing Market Index rose to 80 in October from 76 in September, exceeding expectations, which indicates that homebuilder optimism remains strong.

While the increase in US GDP is welcome news, pricing pressures continue to run hot and staff anticipates the upward pressure on inflation from supply chain bottlenecks and pandemic-related disruptions is likely to remain elevated over the near-term. The Consumer Price Index (CPI) was up 5.4% year-over-year in September 2021, a bit higher than expected, versus up 5.3% year-over-year in August 2021. Core CPI (CPI less food and energy) was up 4.0% year-over-year in September 2021, unchanged from August 2021. Meanwhile, the Producer Price Index (PPI – Final Demand) was up 8.6% year-over-year in September 2021 (the highest year-over-year rate of the pandemic thus far), versus up 8.3% in August 2021. U.S. West Texas Intermediate (WTI) crude oil rose to over $80/per barrel the second week of August 2021 for the first time since 2014 and is up 100% year-over-year. Meanwhile, according to the Energy Information Administration (EIA), average regular retail gas prices jumped 2.5% in mid-August 2021 and are up more than 50% year-over-year. While the EIA expects gas prices to moderate through calendar year-end, they expect prices for all major home heating fuels will significantly increase this winter. Overall, prices across a broad spectrum of goods remain elevated. While plans to ramp-up operations and expand hours at the ports of Long Beach and Los Angeles should help to alleviate some of the supply chain bottlenecks that have put upward pressure on the price of many goods, it will take time for backlogs to ease.

Job growth was weaker than expected in September 2021, but the nationwide unemployment rate fell below 5% for the first time since March 2020. U.S. nonfarm payrolls increased by 194,000 in September, versus the consensus forecast of 500,000. However, July and August 2021 payrolls were revised up a total of 169,000. On a trailing 3-month and 6-month basis, payrolls increased at a solid pace, up an average of 550,000 and 582,000 per month, respectively. The U-3 unemployment rate declined to 4.8% in September 2021 from 5.2% in August 2021, a bigger decline than expected. The labor participation rate declined slightly to 61.6% in September 2021 and remains lower than the pre-pandemic level of 63.4%. The employment-population ratio increased modestly to 58.7%, but also remains below the pre-pandemic level of 61.1%. The U-6 underemployment rate, which includes those who are marginally attached to the labor force and employed part time for economic reasons, declined to 8.5% in September 2021 from 8.8% in August 2021 (versus 7.0% in February 2020). Annualized average hourly earnings were up by 4.6% in September 2021 versus 4.0% in August 2021, reflecting strong wage growth driven in part by the ongoing imbalance in the supply and demand for labor. Although labor force participation has been slow to recover and more than 7.6 million people remain unemployed in the US, the labor market has made significant progress over the past year.

In California, total nonfarm employment in the state increased by 47,400 jobs over the month of September 2021. Additionally, statewide unemployment stayed steady at a rate of 7.5% in September 2021; unchanged from August 2021 and down from 10.6% in September 2020. In Santa Clara County, the rate decreased to 3.9% in September 2021; down from 4.8% in August 2021, and down from 7.4% in September 2020. And in Campbell, the rate decreased to 3.5% in September 2021; down from 4.3% in August 2021 and down from 6.9% in September 2020. At its pandemic high point in April 2020, the Campbell unemployment rate had reached 11.7%. While the current Campbell unemployment rate is not at the ten-year low of 2.0% seen in May 2019, there has still been considerable improvement since the start of the pandemic.