

April 2017

California Forecast: Sales Tax Trends and Economic Drivers

HdL provides relevant information and analyses on the economic forces affecting California's local government agencies. In addition, HdL's Revenue Enhancement and Economic Development Services help clients to maximize revenues.

HdL serves over 400 cities, counties and special districts in California and across the nation.





	2016/17	2017/18
Autos/Transportation	4.9%	2.3%
<p>Automakers continue to produce cars at a near-record clip amid softening demand. Although sales of new vehicles are expected to plateau in 2017, consumers are taking advantage of generous manufacturer's incentives by leasing and purchasing more expensive crossovers, SUV's and pickup trucks. However, analysts have concerns about the number of unsold new vehicles clogging many dealer's lots. Future federal interest rate hikes may dampen buyer enthusiasm in the months ahead. Last year's RV sales were a bright spot for some agencies, shipments to dealers were up again in January.</p>		
Building/Construction	1.7%	2.5%
<p>Despite challenging winter weather, property owners continue to buy building materials and supplies for home renovation projects. The weather also created a backlog of permitted residential and commercial projects, including several large regional projects; commencement of construction on these projects will increase sales this spring. Labor shortages are causing some contractors to use drones, a trend that is expected to expand in 2017.</p>		
Business/Industry	-0.9%	0.0%
<p>Analysts note U.S. companies are more optimistic about growth; many are preparing to increase business investment after years on the sidelines. California's merchandise exports started the year with a strong showing. However, recent federal policy proposals in the areas of immigration, tax reform, health care, trade and regulation may lead to lower capital expenditures. Medical, biotech and food service companies are anticipating new equipment acquisitions. Sellers of office supplies will continue to see customers shift to online purchases.</p>		
Food/Drugs	2.3%	2.0%
<p>Competition among specialty grocery store chains, big box retailers with small store alternatives and a budding demand for home delivery keep this segment in flux. Results from grocery chains that include gasoline sales on their tax returns could skew comparisons if fuel prices become volatile. The passage of Proposition 64 last November could boost revenues for communities electing to permit and tax cannabis.</p>		
Fuel/Service Stations	-6.8%	8.5%
<p>Fuel price increases, coupled with California's seasonal transition to summer blends, will boost receipts from gasoline and diesel sellers but price gains will be moderate while supplies remain robust. Production caps by OPEC countries have helped to stabilize prices but it is unclear whether non-OPEC producers will participate; prices could dip if they do not. In addition China and India have been stockpiling crude while prices are low. As storage capacity diminishes, more oil in the marketplace could lead to lower prices.</p>		
General Consumer Goods	0.6%	0.5%
<p>General consumer sales in 2016's final quarter belied media reports about rising consumer confidence and were little-changed from a year earlier. Heavy discounting was a factor as brick-and-mortar stores vied with online sellers to capture market share. Higher costs for health care, transportation and housing, plus increased spending on services, is siphoning away dollars that might otherwise have been spent on taxable goods. Recent layoffs and store closures at major department stores and specialty chains mean industry belt-tightening in this sector is well underway.</p>		
Restaurants/Hotels	4.9%	4.0%
<p>Forecasted trends are moderate due to the ongoing deceleration in consumer spending and the significant headwinds (e.g. higher labor costs) facing the industry. Most recently, the Federal Reserve noted that the hospitality industry is threatened by the executive actions banning some international travel as this may damage the perception of the United States as a welcoming destination. Travel statistics indicate slightly weaker activity early this year, though advanced bookings for Southern California hotels shows improvement for the summer months.</p>		
State and County Pools	7.3%	5.2%
<p>Growth in countywide pool allocations is expected to trend upward. Over time, bargain hunting at malls and retail centers is being replaced by the convenience of e-commerce. This behavioral shift in online shopping for clothing, electronics and other consumer merchandise delivered from out-of-state, along with increased private vehicle transactions registered at the DMV, is boosting pool allocations for many jurisdictions.</p>		
TOTAL	1.9%	2.7%
<p>Proposition 172 projections vary from statewide Bradley-Burns calculations due to the state's utilization of differing collection periods in its allocation to counties. A recent change in how the Board of Equalization calculates its true-ups skews monthly comparisons with prior years. HdL forecasts a statewide increase of 2.91% for Fiscal Year 2016-17 and a gain of 2.79% in 2017-18. Percentage shares for counties are based on their portion of statewide sales in the prior calendar year.</p>		



	2016/17	2017/18
U.S. Real GDP Growth	2.1%	2.3%

The U.S. economy continues to chug along at a steady, but somewhat slow, pace. Gross domestic product (GDP) grew by 1.9% in the fourth quarter of 2016, roughly in line with the post-recession average of 2.1%. The first two months of President Trump's administration have not yet produced any policies that would derail or stimulate the current economic expansion, which is approaching seven and a half years, making it one of the longest on record.

U.S. Unemployment Rate	4.7%	4.6%
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The U.S. unemployment rate held at post-recession lows last quarter as the national labor market essentially reached full employment. During the first two months of 2017, the U.S. unemployment rate has averaged 4.75%, down slightly from an average of 4.85% throughout 2016. The drop in the unemployment rate comes amid an expanding labor force, indicating that the economy is creating jobs more rapidly than people entering the labor market and not because people are dropping out of the labor force.

California Total Nonfarm Employment Growth	2.2%	1.9%
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The California EDD's annual benchmark revision of the state's employment figures only slightly changed previous estimates but included some notable industry adjustments. The EDD release showed a slight upward revision in California's 2016 annual rate of job growth from 2.56% to 2.63%. Sectors that saw the largest upward revisions compared to previously released figures include Information (2.7% to 7.6%), Transportation, Warehouse, & Utilities (2.7% to 5.4%), and Finance and Insurance (0.8% to 2.8%). Sectors that saw the largest downward revisions in job growth included Educational Services (6.2% to 2.7%), Management (1.7% to -1.0%), and the Professional, Scientific, and Technical sector (4.2% to 2.6%). The California economy is expected to grow this year, but because the labor market is essentially at full employment, it's unlikely that any policies emanating from Washington, D.C. or Sacramento will accelerate the pace of growth.

California Unemployment Rate	5.2%	5.1%
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The California unemployment rate ticked down to 5.1% in January 2017, a new post-recession low and the lowest rate in nearly 10 years (since April of 2007). Like the national picture, the decline in unemployment comes amidst an expanding labor force. The state's unemployment rate is not expected to fall much more over the next year as it is already near record lows. Since 1990, the earliest data available from the EDD, the lowest unemployment rate on record is 4.7% from December 2000.

California Median Existing Home Price	\$456,065	\$463,176
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Home prices in California continue to rise, albeit at a more moderate pace than during the years immediately following the Great Recession when prices grew by double digit percentages. The median price of an existing single-family home in the state came in at \$426,887 in the fourth quarter of 2016 on a seasonally adjusted basis, a 5.8% increase over the same time one year prior. The inventory of homes on the market remains tight which will support continued growth in home prices across the state in the near future.

California Residential Building Permits	110,600	114,900
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Permitting activity increased in 2016 but at a slower pace compared to the year prior. This was primarily due to a drop in permits for multifamily properties in the first half of the year. The second half of the year saw much better results as permitting for single-family and multifamily properties accelerated. The total number of residential units permitted in 2016 reached 102,000, a 7.3% increase over 2015 levels. With home prices and rents on a steady uptrend due to the low supply of housing in the state, permitting activity is expected to continue to grow over the next few years but will remain below the levels needed to accommodate growth in California's population and number of households.



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California's allocation data trails actual sales activity by three to six months. HdL compensates for the lack of current information by reviewing the latest reports, statistics and perspectives from fifty or more economists, analysts and trade associations to reach a consensus on probable trends for coming quarters. The forecast is used to help project revenues based on statewide formulas and for reference in tailoring sales tax estimates appropriate to each client's specific demographics, tax base and regional trends.



"Good information leads to good decisions."



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Beacon Economics, LLC has proven to be one of the most thorough and accurate, economic research/analytical forecasters in the country. They regularly provide national, state, regional, and sub-regional economic analysis/forecasting to clients ranging from the State of California to private hedge funds to major universities. Their evaluation of the key drivers impacting local economies and tax revenues provides additional perspective to HdL's quarterly consensus updates. The collaboration and sharing of information between Beacon Economics and HdL helps both companies enhance the accuracy of the work that they perform for their respective clients.