

Economic and Revenue Forecast October 2024

**Forecast Council and Select Budget Committee
October 22, 2024**

**Office of Economic and Revenue Forecasts
&
City Budget Office**

Outline

Part I: Update on recent economic developments and summary of the October economic forecasts

- S&P Global's U.S. economic forecast
- Forecast Office's regional economic forecast for Seattle Metropolitan Division (King and Snohomish counties)

Part II: Summary of the October revenue forecast

- General Fund Revenues
- Selected Other Government Revenues

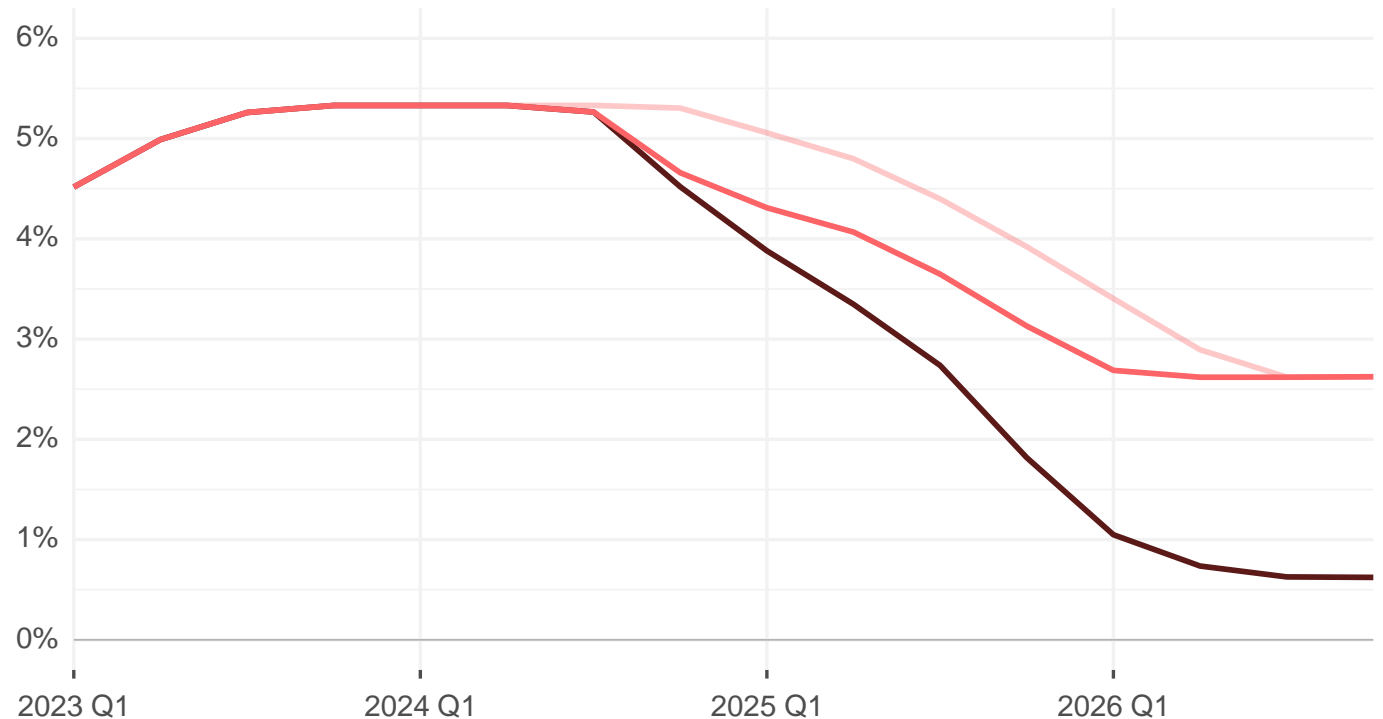
Economic Outlook for U.S. and Seattle MD Area

Faster monetary policy easing is now expected

- Recession fears resurfaced in early August, after weak reports on hiring, jobs creation, and unemployment in July
- This led to expectations that Fed will cut interest rates more aggressively to avoid a hard landing
- **Fed has indeed started monetary policy easing with a 0.5% rate cut in September**
- **S&P Global expects additional 0.25% cuts in November and December this year, followed by 0.25% cuts at each FMOOC meeting in 2026**
- This would bring the Fed's interest rate to the 2.75%-3.00% range by year end 2026

Federal Funds Interest Rate Forecast

Jul 2024 Baseline Oct 2024 Baseline Oct 2024 Pessimistic



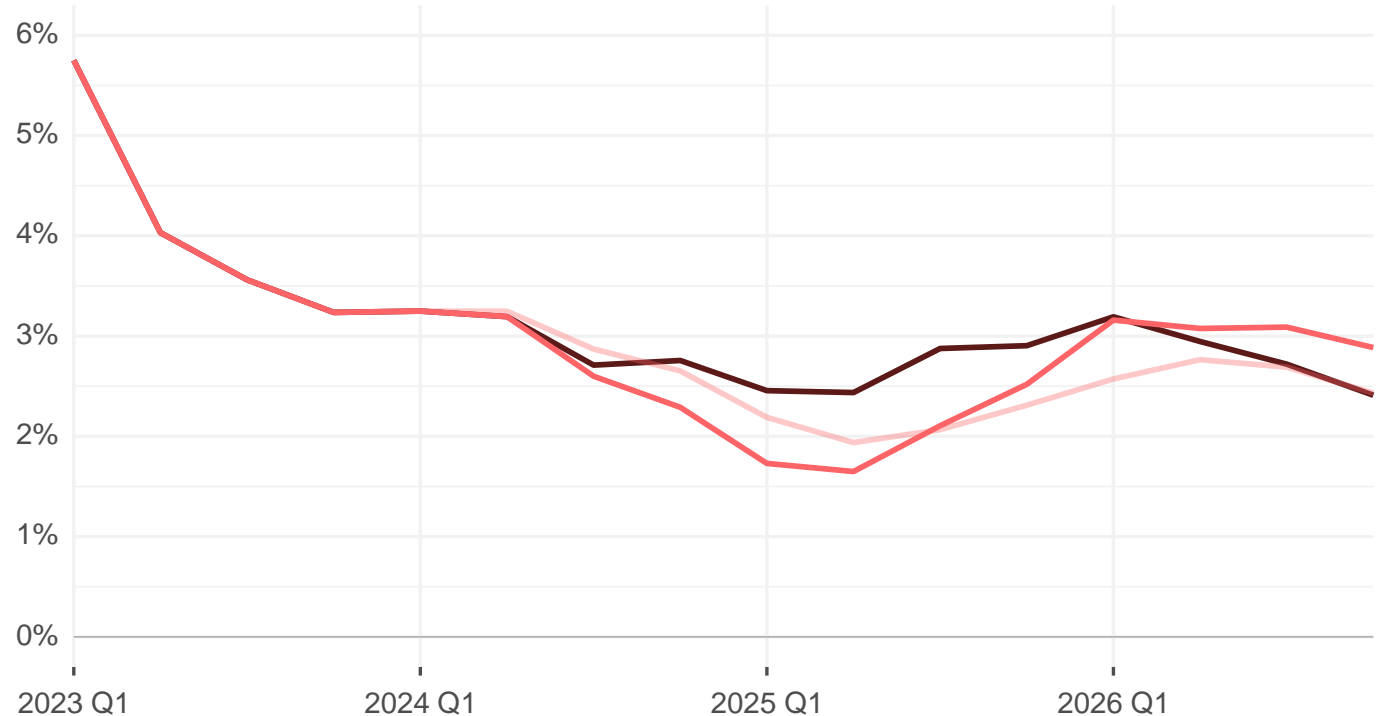
Source: S&P Global Market Intelligence

U.S. inflation forecast is lower first, but higher later

- Demand and supply in the national labor market continue to move back to balance, thus easing price pressures.
- With national housing market cooling as well, U.S. inflation continues to moderate.
- **S&P Global’s revised baseline scenario forecast for inflation is lower for the period until 2025 Q3, then higher through year-end 2026.**
- In the pessimistic scenario, conflicts in the Middle East and Ukraine lead to higher oil and energy prices, and higher inflation in general.

U.S. CPI-U Inflation Forecast

Jul 2024 Baseline Oct 2024 Baseline Oct 2024 Pessimistic

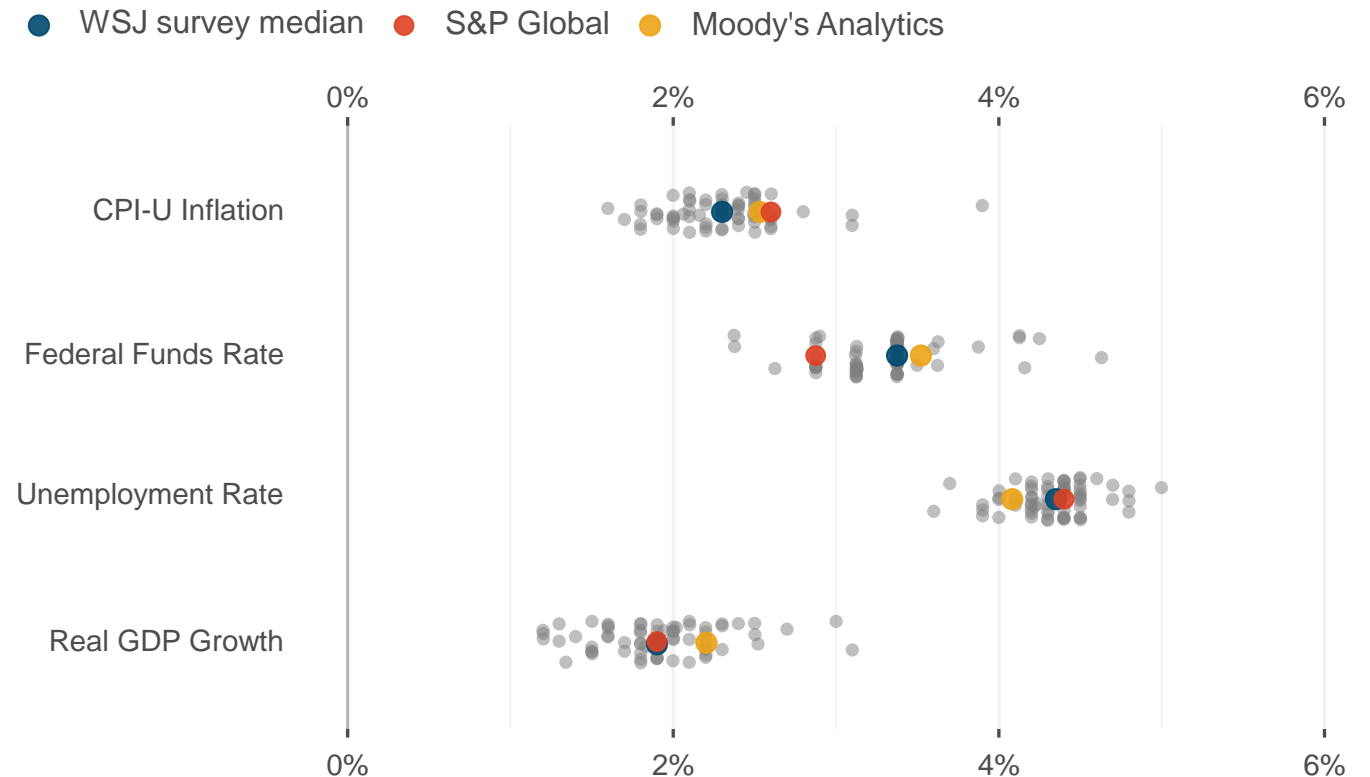


Source: S&P Global Market Intelligence

U.S. economic forecast

- Forecast for U.S. economy from S&P Global serves as one of the main inputs when our office develops the regional economic forecast for Seattle Metropolitan Division (King and Snohomish counties).
- **S&P Global's October baseline scenario forecast is overall somewhat more conservative than the forecast from Moody's Analytics and the median forecast in the October 2024 Wall Street Journal Survey of economic forecasters.**
- In that survey, the average across the participants for the estimated probability of a recession within 12 months was 26%, about same as in July.

U.S. economic forecast for year-end 2025



Source: Wall Street Journal Economic Forecasting Survey, October 2024

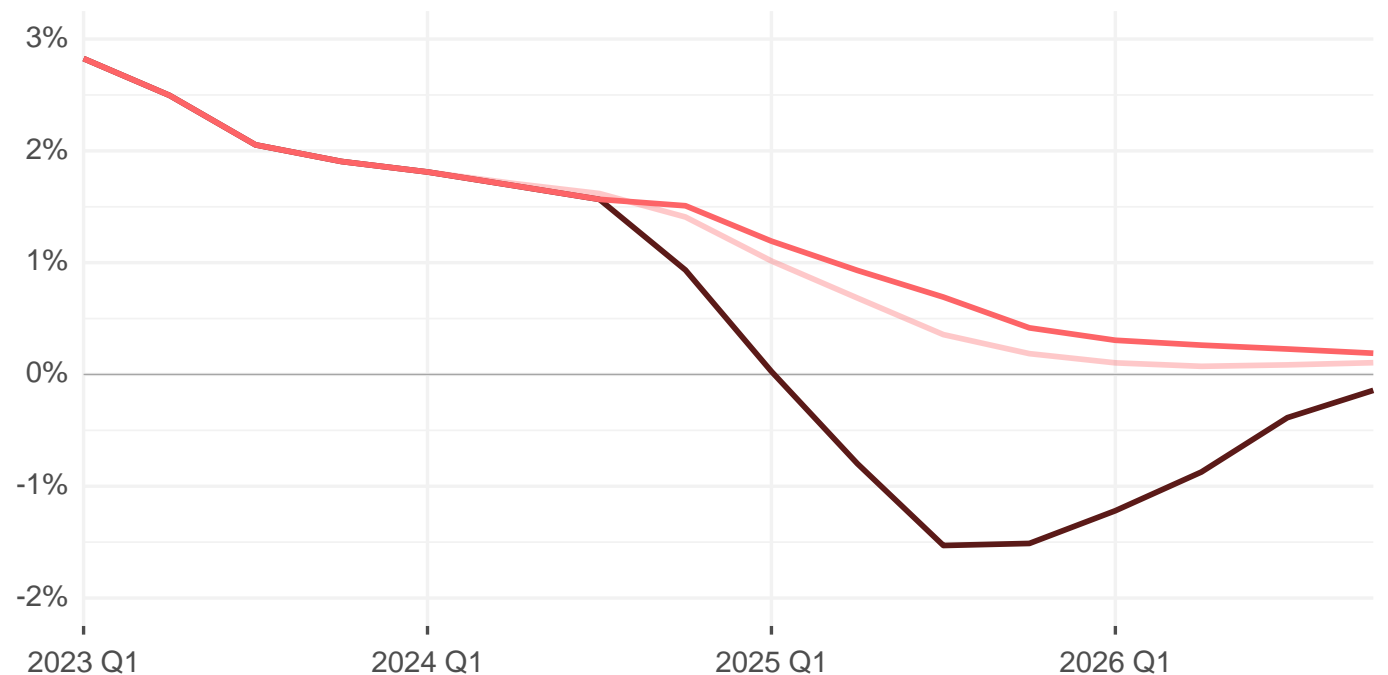
U.S. labor market forecast has been revised up yet again

- U.S. labor market has continued to moderate
- Fears of significant deterioration have however subsided after strong job gains in September and upward revision of July employment estimates.
- S&P Global has revised their baseline scenario forecast for employment growth in 2025 slightly, from 0.6% to 0.8%.
- In the pessimistic scenario a shallow recession causes employment to fall by 2% while unemployment rate rises to 6.5% by mid-2026.

U.S. Employment Forecast

Year-over-year % change

Jul 2024 Baseline Oct 2024 Baseline Oct 2024 Pessimistic



Source: S&P Global Market Intelligence

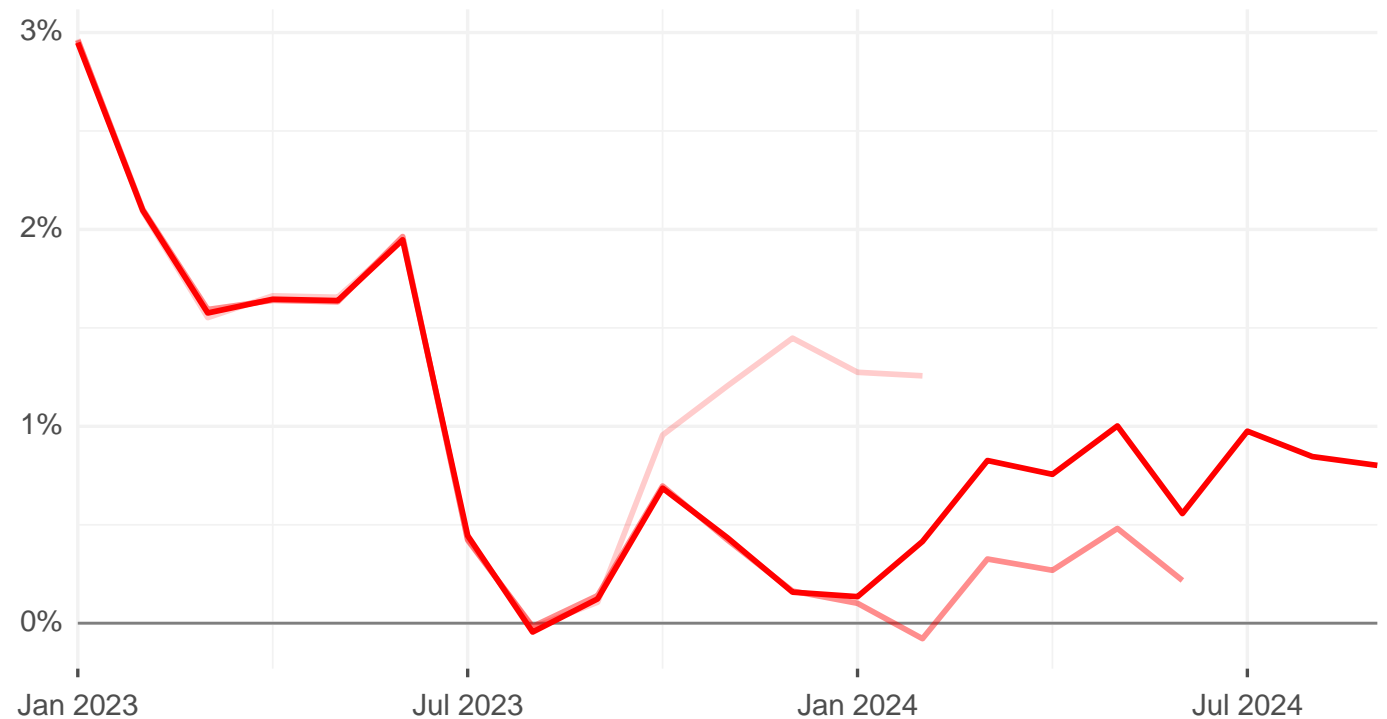
Total employment in Seattle MD has been revised up...

- Our employment forecasts are based on employment data from Washington State Employment Security Department (ESD).
- Employment data is subject to regular and occasionally large revisions.
- ESD has recently revised up their estimates for Seattle metro area employment
- Based on their October estimates, regional employment has in 2024 grown on average 0.7% on the year-over-year basis, which is about 0.5% higher than estimated in July.

Seattle Metropolitan Division Employment Growth

Employment Security Department (ESD) Estimates

■ March 2024 ESD estimates ■ July 2024 ESD estimates ■ October 2024 ESD estimates



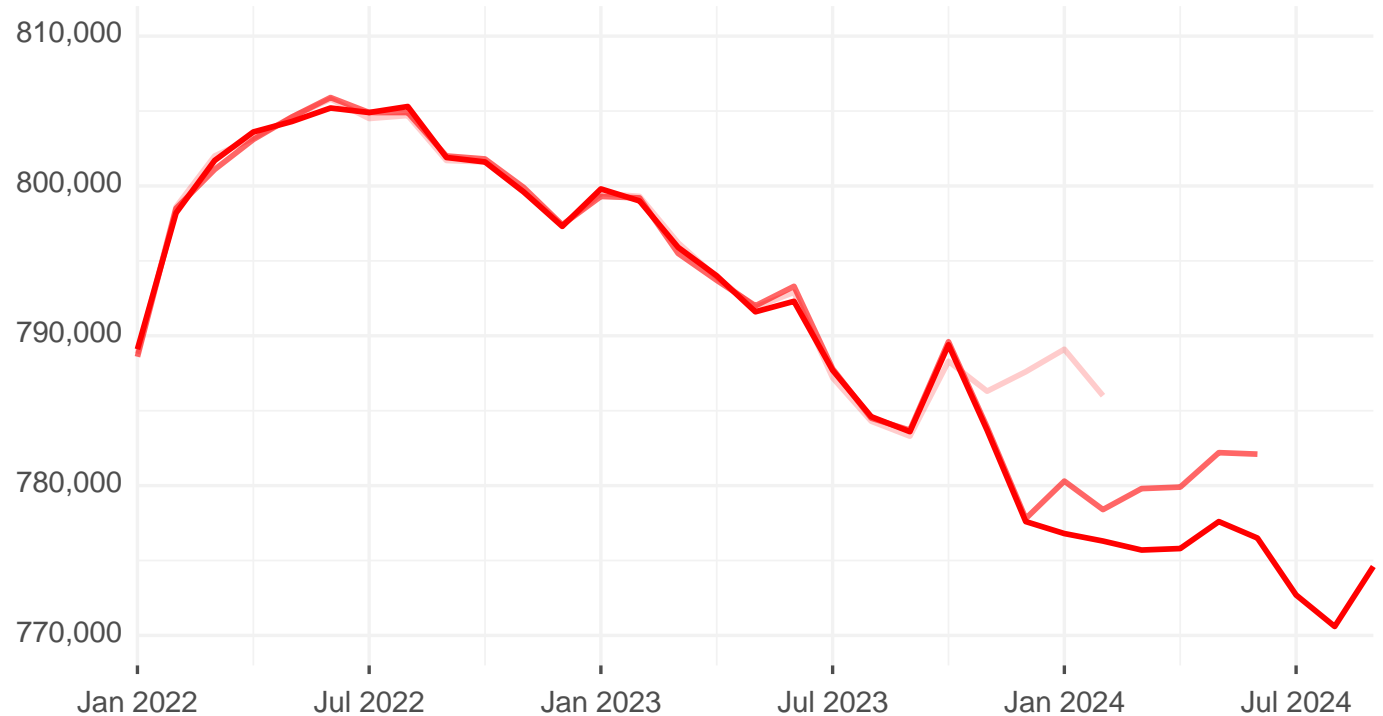
...but employment in important industries has been revised down

- Seattle MD employment in trade, information, financial activities, professional and business services has been however revised down by ESD.
- Employment in these sectors declined by about 30,000 (or 3.8%) since June 2022.
- **These sectors account for about 43% of total regional employment and about 70% of total Business & Occupation, Sales Tax and Payroll Expense Tax revenues collected by the City.**

Seattle Metropolitan Division Employment

Trade, Information, Financial Activities, Professional and Business Services

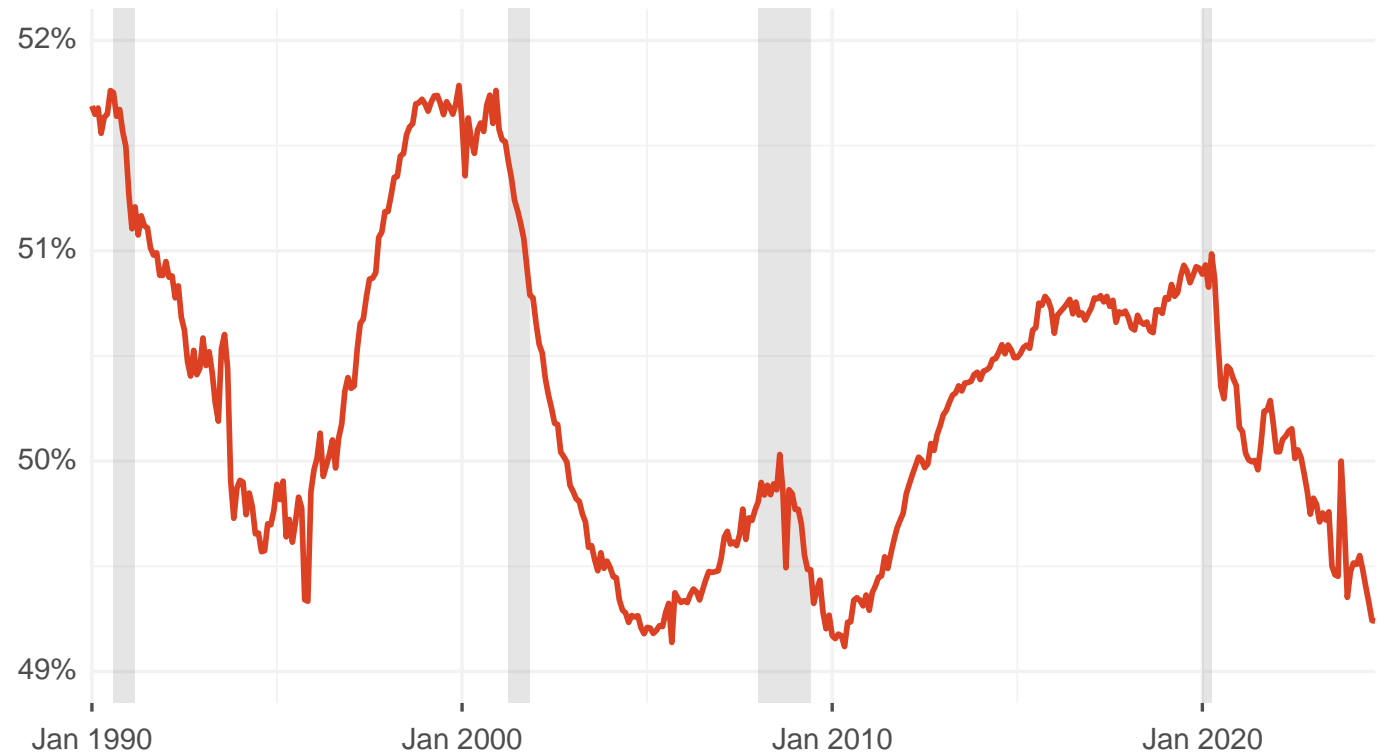
■ March 2024 ESD estimates ■ July 2024 ESD estimates ■ October 2024 ESD estimates



Seattle MD employment declines as share of Washington State total

- Since 2020, growth in the regional labor market has been weaker than the employment growth in the U.S. labor market, and in the Washington State labor market.
- Employment in Washington State has increased cumulatively by about 4% since February 2020.
- Over the same time, employment grew only 0.5% in Seattle Metropolitan division.
- As a result, Seattle Metropolitan Division area's share in the total state employment is now has dropped from 51% to 49.2%.

Seattle Metropolitan Division share of total Washington State's employment
Employment Security department (ESD) Estimates



Note: Shaded areas denote recessions.

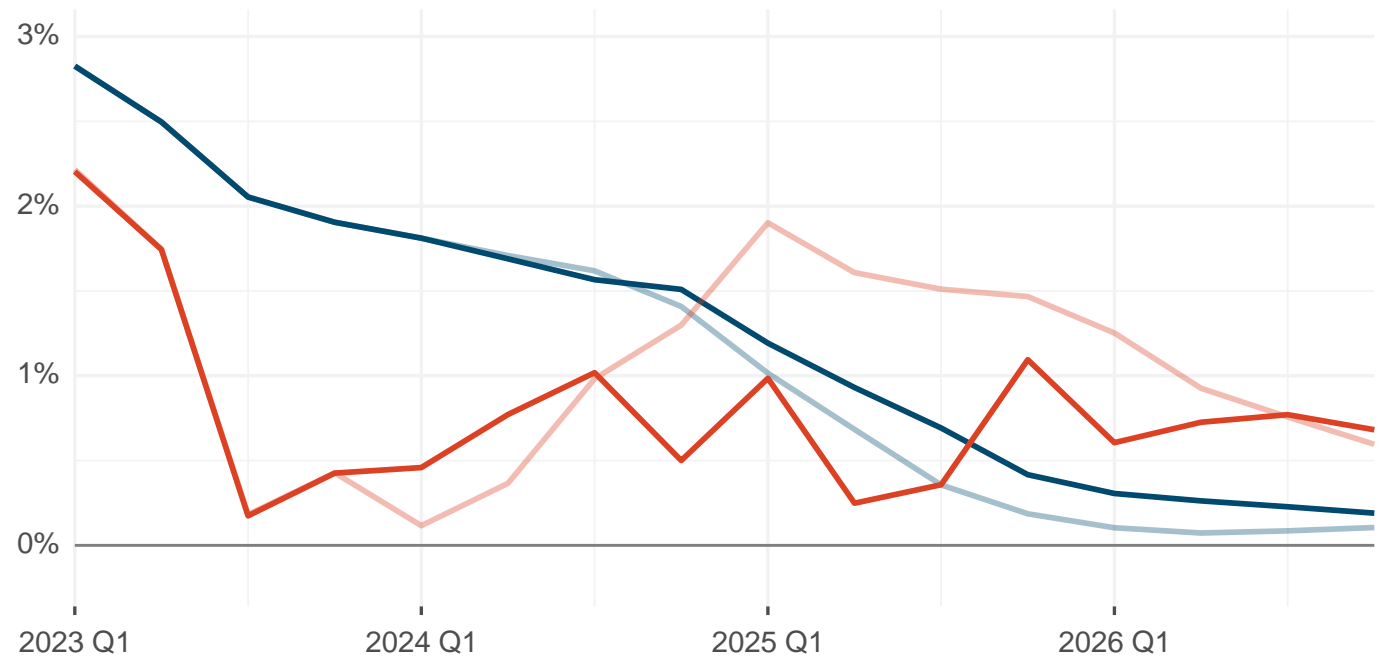
Employment Growth Forecast, United States vs Seattle MD

- Regional employment growth forecast has been revised down for the second half of 2024 and for 2025
- The updated forecast accounts for
 - ESD employment data revisions
 - strike and layoffs at Boeing
- Baseline scenario average employment growth forecasts for 2024-2026:
 - S&P Global: 0.9% for United States
 - OERF: 0.7% for Seattle metro area

Employment Growth Forecast

Year-over-year % change

- United States, July 2024
- Seattle MD, July 2024
- United States, October 2024
- Seattle MD, October 2024



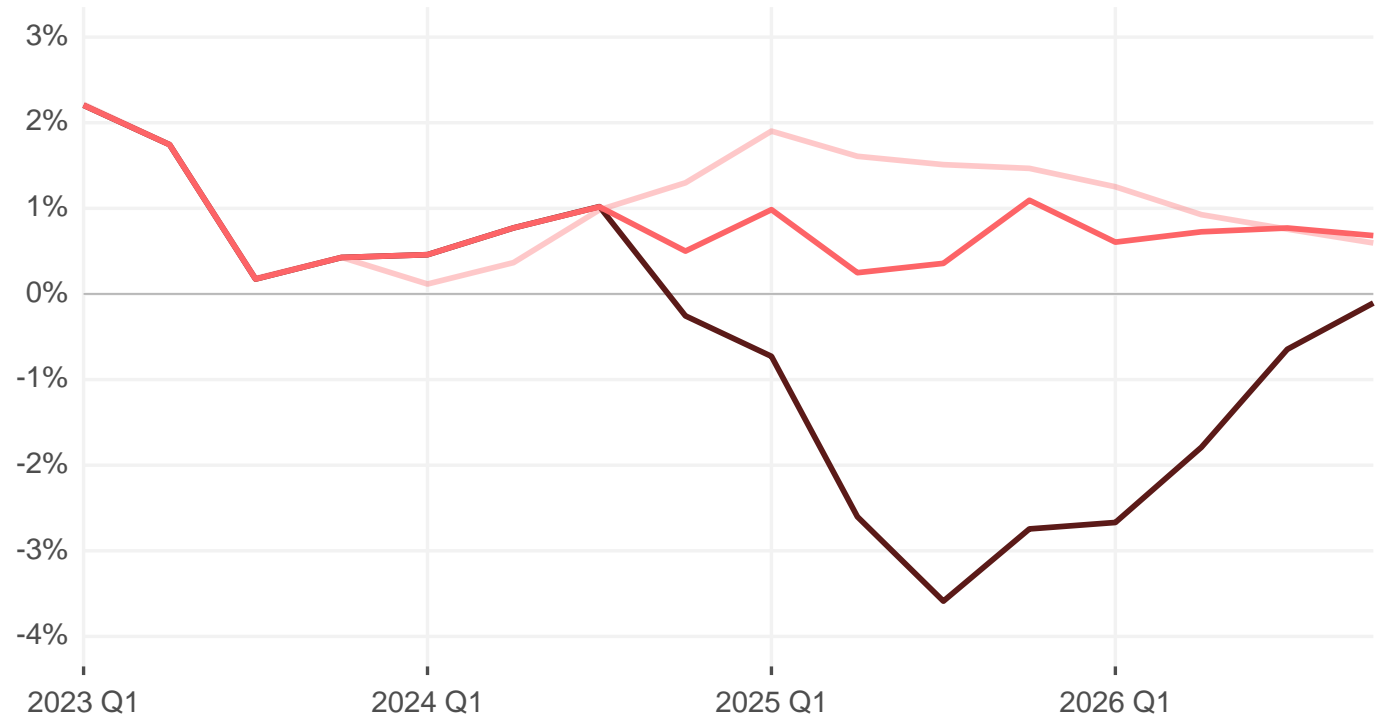
Regional employment forecast for Seattle Metropolitan Division

- S&P Global currently assigns 55% probability to their baseline scenario, 25% to the pessimistic scenario, and 20% to the optimistic scenario.
- Under the pessimistic scenario, a recession begins in 2025, by summer 2026 it would lead to about 4.3% fewer jobs in Seattle area compared to the current employment
- Full employment recovery would occur in 2029 Q1
- This recession would be thus somewhat milder and shorter than the 2001 recession

Regional Employment Forecast for Seattle MD

Year-over-year change

Jul 2024 Baseline Oct 2024 Baseline Oct 2024 Pessimistic

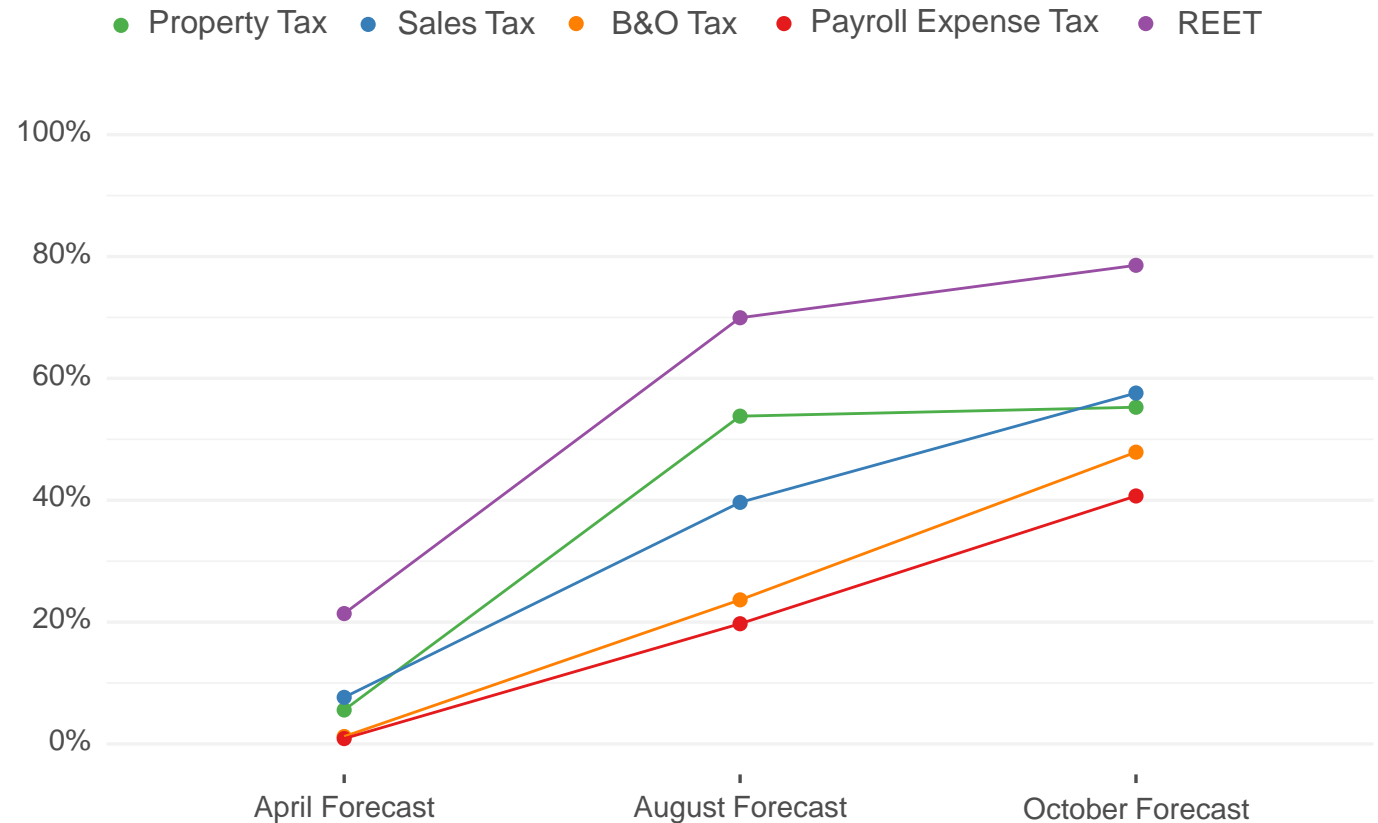


Revenue Forecast for 2024-2026

Updated revenue forecast incorporates 2024 Q2 revenues

- New tax information since August forecast
 - 2024 Q2 Business & Occupation tax returns
 - August and September Sales Tax distributions from Washington State Department of Revenue
 - August and September REET
- Typically, about half of the total annual General Fund revenues are collected by the time of the October forecast update.
- The share of total annual revenues collected by the time of October update however varies a lot by revenue stream.
- In 2023, almost 80% of REET revenues had been collected by that point, but just 40% of Payroll Expense Tax revenues.

Share of revenues collected in 2023 by the time of forecast updates

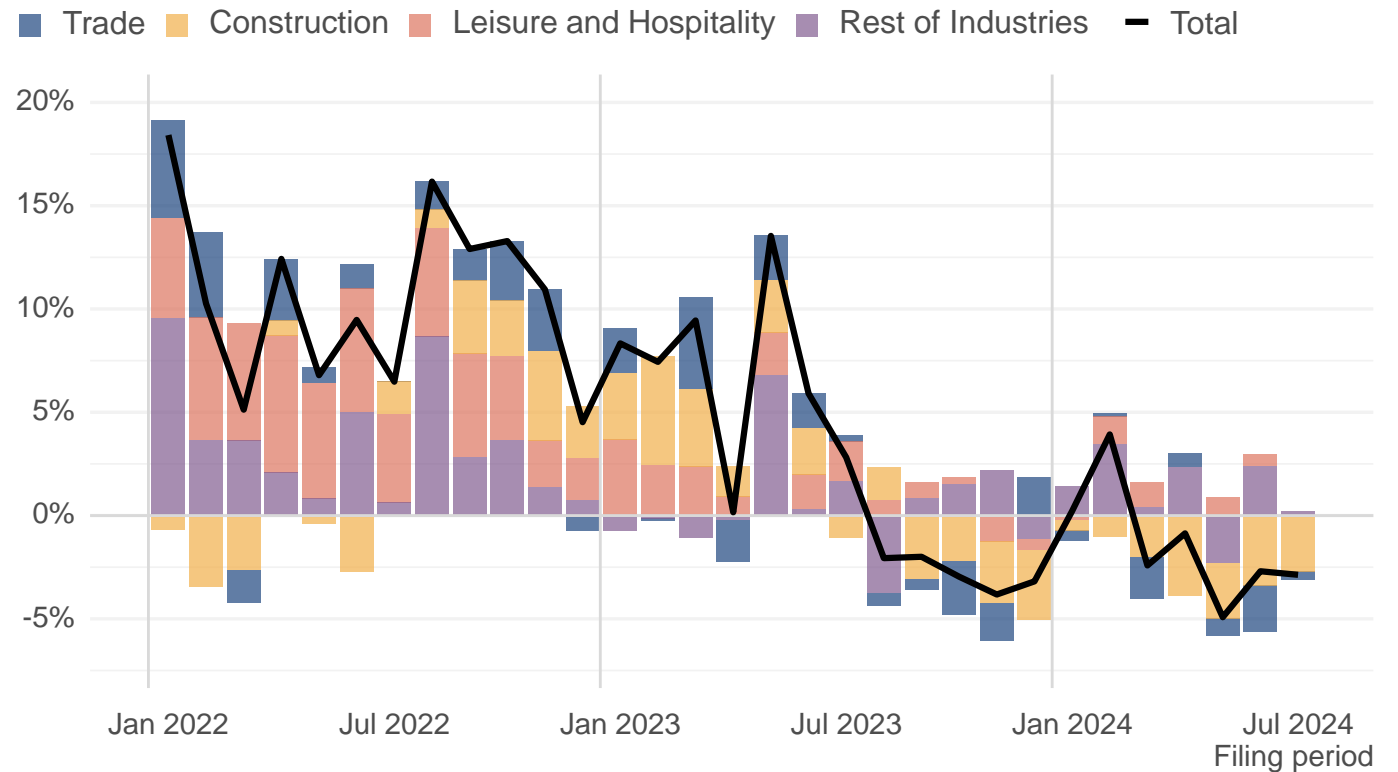


Sales tax

- Sales tax revenue collection has been weak since the second half of 2023.
- Taxable sales in trade sector declined year-over-year in the last couple of months.
- Downturn in the construction sector weighs down quite notably on overall tax collection.
- Lower demand for new construction can be also seen in the value of construction permits issued by SDCI, which has declined from \$3.8 billion in 2021 to \$2.8 billion in 2023.
- For the 12 months ending September 2024, the value of permits issued was \$2.6 billion, so about \$1.7 billion or 40% lower than the 2016-2019 average of \$4.3 billion.

Sales Tax Revenue

Total year-over-year % change and decomposition by industry



General Fund Revenues - Baseline Scenario Forecast (\$ millions)

Revenue Source	Actual 2023	October Forecast			Difference from 2025-2026			3 Year Total Difference
		2024	2025	2026	2024	2025	2026	
Property Tax (Including Medic One Levy)	\$377.8	\$382.9	\$388.3	\$403.0		-\$1.2	-\$6.3	-\$7.5
Sales & Use Tax	\$339.9	\$338.1	\$344.0	\$351.0	-\$1.9	-\$4.3	-\$7.5	-\$13.7
Business & Occupation Tax	\$356.3	\$354.0	\$369.5	\$394.6	-\$4.3	-\$10.5	-\$9.7	-\$24.5
Utility Tax - Private	\$43.2	\$37.4	\$34.5	\$33.0	-\$0.3	-\$0.8	-\$0.9	-\$2.0
Utility Tax - Public	\$185.7	\$214.8	\$214.9	\$222.6				
Payroll Tax - 2021 obligations	\$3.6	-\$0.8	\$0.0	\$0.0	\$1.4			\$1.4
Other City Taxes	\$14.1	\$13.5	\$13.8	\$14.3	\$0.1			\$0.1
Parking Meters	\$37.0	\$39.3	\$40.7	\$42.9	-\$0.5	-\$1.0	-\$1.0	-\$2.5
Court Fines	\$24.0	\$18.9	\$24.1	\$24.1	-\$0.8	-\$0.8	-\$0.9	-\$2.5
Licenses, Permits, Interest Income and Other	\$77.5	\$76.1	\$74.0	\$76.7	-\$0.4	\$1.8	\$1.1	\$2.5
Revenue from Other Public Entities	\$19.1	\$19.6	\$20.0	\$20.5				
Service Charges & Reimbursements	\$76.2	\$81.7	\$82.1	\$85.6				
Grants	\$34.1	\$67.8	\$14.7	\$14.7				
Fund Balance Transfers	\$80.5	\$96.1	\$296.9	\$233.4				
Total	\$1,669.1	\$1,739.4	\$1,917.6	\$1,916.3	-\$6.5	-\$16.9	-\$25.2	-\$48.6
Total w/o Grants and Transfers	\$1,554.4	\$1,575.6	\$1,605.9	\$1,668.2	-\$6.5	-\$16.9	-\$25.2	-\$48.6

Note: Revenues highlighted blue are in the purview of the Office of Economic and Revenue Forecasts, forecasts for remaining revenues come from City Budget Office.

General Fund Revenues - Baseline Scenario Forecast

- General Fund revenues were in total revised down by \$48.6 million
 - \$6.5 million (0.4%) for 2024
 - \$42.1 million (1.1%) for the 2025-2026 biennium
- The overall change for the 2025-2026 biennium is negative in large part due to the \$32.1 million lower forecast for Sales and Use Tax and Business & Occupation Tax.
- The downward revisions for these revenue streams are driven by lower forecast for construction activity and slower projected regional employment growth, which leads to lower income and spending as well.

Selected Other Revenues - Baseline Scenario Forecast (\$ millions)

Revenue Source	Actual 2023	October Forecast			Difference from Proposed			3 Year Total Difference
		2024	2025	2026	2024	2025	2026	
Payroll Expense Tax - w/o 2021 obligations	\$315.2	\$406.8	\$440.5	\$466.1	\$2.4	\$10.5	\$14.6	\$27.4
REET	\$47.9	\$58.9	\$66.5	\$85.7	\$1.7	\$2.6	\$5.5	\$9.9
Admission Tax	\$25.3	\$25.7	\$26.5	\$27.2	-\$0.5	-\$0.5	-\$0.5	-\$1.6
Sweetened Beverage Tax	\$21.5	\$20.9	\$21.3	\$21.8				
Short Term Rental Tax	\$11.4	\$11.9	\$12.4	\$13.2	\$0.6	\$0.6	\$0.8	\$2.0
STBD Sales Tax	\$53.1	\$52.8	\$53.7	\$54.8	-\$0.3	-\$0.7	-\$1.2	-\$2.1
STBD Vehicle License Fee	\$16.5	\$19.5	\$20.9	\$21.2				
Commercial Parking Tax	\$51.7	\$52.4	\$54.0	\$54.6				

Note: Revenues highlighted blue are in the purview of the Office of Economic and Revenue Forecasts, forecasts for remaining revenues come from City Budget Office.

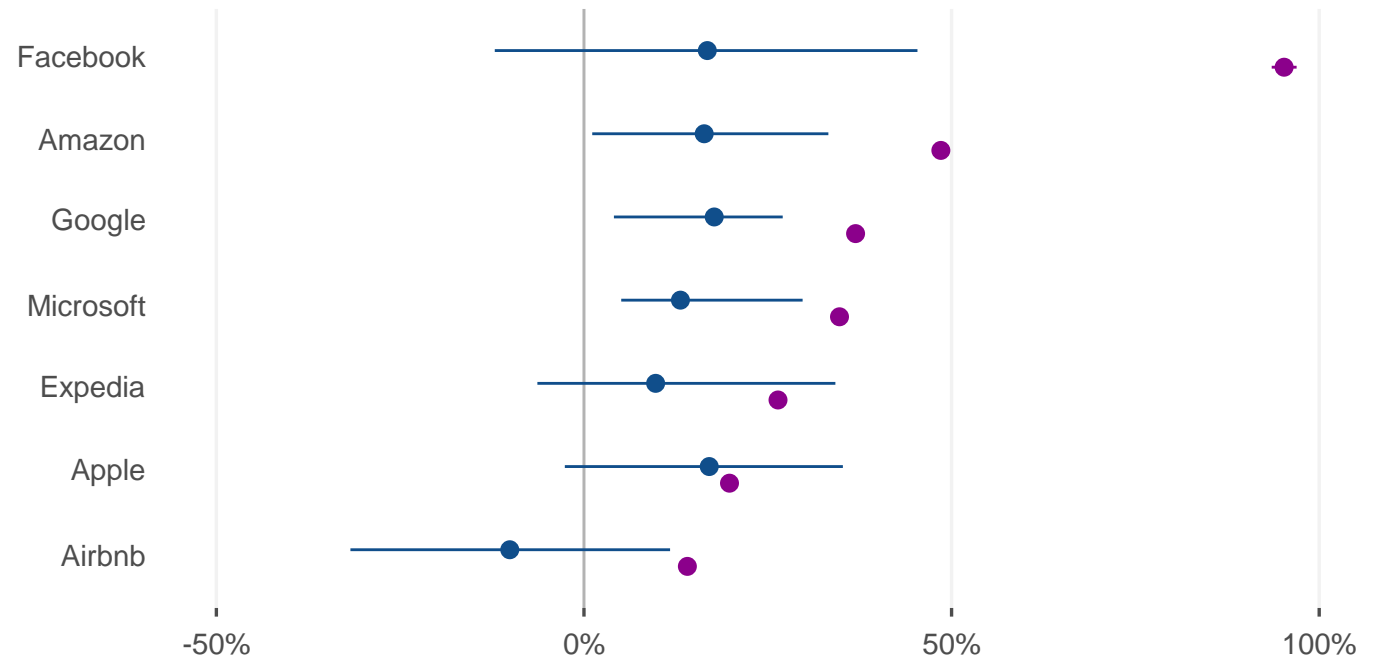
Payroll Expense Tax Forecast

- Payroll Expense Tax forecast was revised up.
- Rising stock prices of tech companies are increasing value of stock grants that are subject to the tax.
- As in past, this continues to dominate the effects of employment changes - due to layoffs since 2022, as well as the reported 17% decline in Amazon's headcount in Seattle city from its peak in 2020.
- S&P Global expects the S&P 500 index to grow 25.8% in 2024 in the baseline scenario. Stock market is then expected to grow only 5.4% in 2025 and decline 3.6% in 2026.
- In the pessimistic scenario the S&P 500 index grows 1.3% in 2025, declines 2.3% in 2026.

Predicted stock price changes

Year-over-year expected change in stock price; low, average and high estimates

● 2024 ● 2025



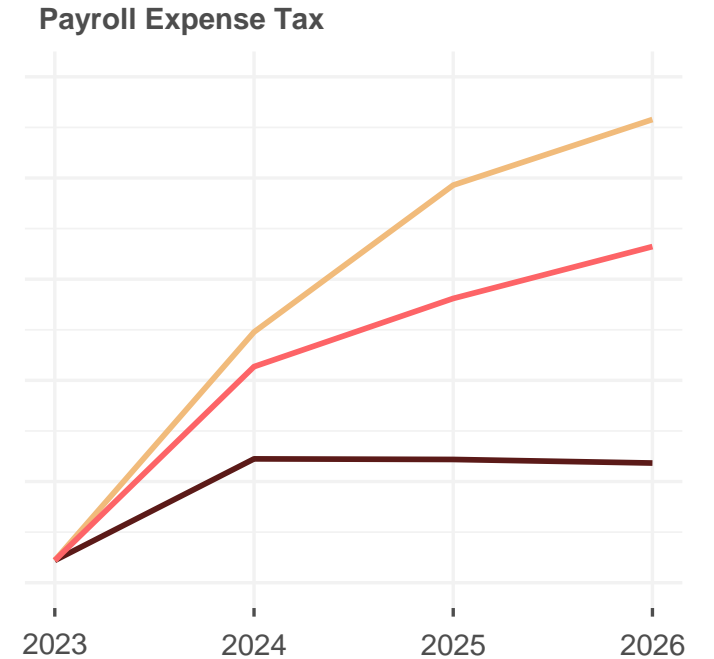
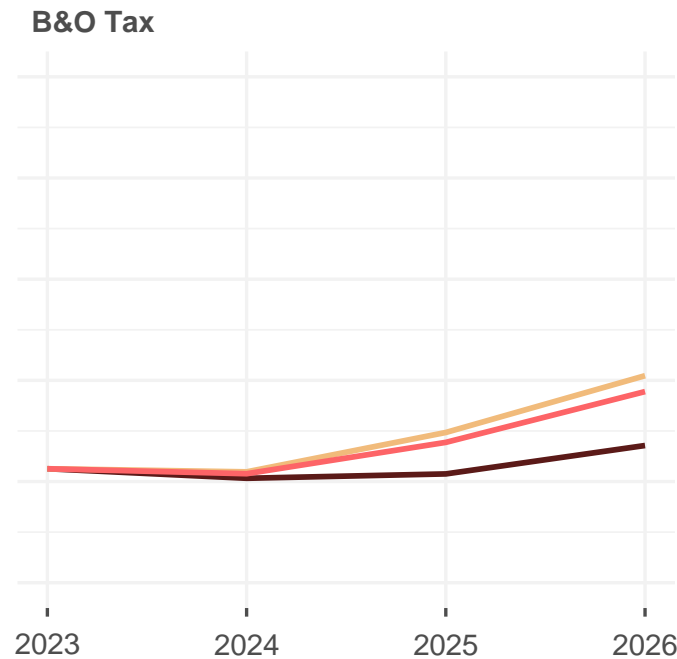
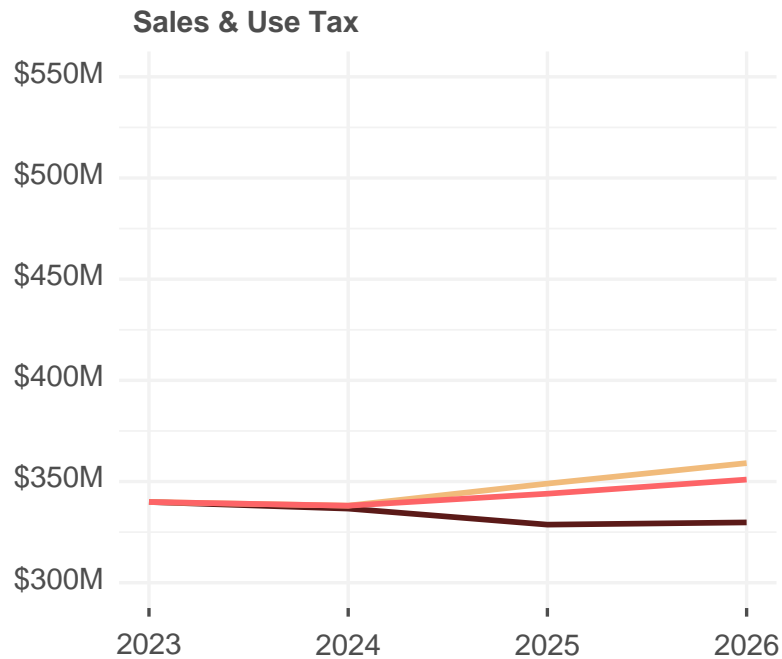
Source: Wall Street Journal, stock price targets from analyst ratings

How Do Forecasts Vary Across Scenarios?

Tax Revenue Forecasts, Scenario Comparison

Millions of dollars

■ Baseline ■ Optimistic ■ Pessimistic



Alternative scenarios – forecast differences from baseline (\$ millions)

- The most significant differences between the scenarios are in Sales tax, B&O taxes, Payroll Expense Tax and REET
- The high level of uncertainty regarding payroll expense tax revenue estimates reflects the underlying tax base uncertainty due to stock price movements as well as forecasting uncertainty due to short collection history

	Difference - Pessimistic			Difference - Optimistic		
	2024	2025	2026	2024	2025	2026
Sales & Use Tax	-\$1.4	-\$15.3	-\$21.2	\$0.0	\$5.0	\$8.1
Business & Occupation Tax	-\$2.3	-\$15.6	-\$26.7	\$1.0	\$4.9	\$7.9
Utility Taxes	-\$10.3	-\$11.2	-\$11.6	\$11.1	\$12.4	\$13.2
Total General Fund	-\$17.3	-\$48.8	-\$69.1	\$17.3	\$28.9	\$37.0
Payroll Expense Tax - w/o 2021 obligations	-\$45.6	-\$79.6	-\$107.0	\$17.1	\$56.0	\$62.8
REET	-\$0.8	-\$8.8	-\$10.2	\$0.3	\$2.4	\$1.5

Forecast risks and scenario recommendation

Summary and Context

- S&P Global assigns a 55% probability to their October baseline scenario forecast and 25% to the pessimistic scenario.
- Their forecast for the national economy is slightly more conservative than the October forecast from Moody's Analytics and the median in the October Wall Street Journal Survey of economic forecasters.
- Outlook for regional employment growth is weaker due to layoffs at Boeing, employment data revisions.

Forecast Risks

- Higher uncertainty regarding the economic outlook due to elections
- Uncertain outlook for commercial real estate, construction sector slowdown
- Weak regional employment growth in sectors with outsized impact on revenues
- Rising office vacancy rates and I-137 Proposition 1A pose additional risks to the job growth and City's revenues.

While acknowledging these risks, we consider the baseline scenario for regional economic and revenue forecasts as the scenario that is most likely to be closest to the actual outcomes in 2024-2026.

Conclusion

The Forecast Office recommends using the baseline scenario for the October 2024 Revenue Forecast.

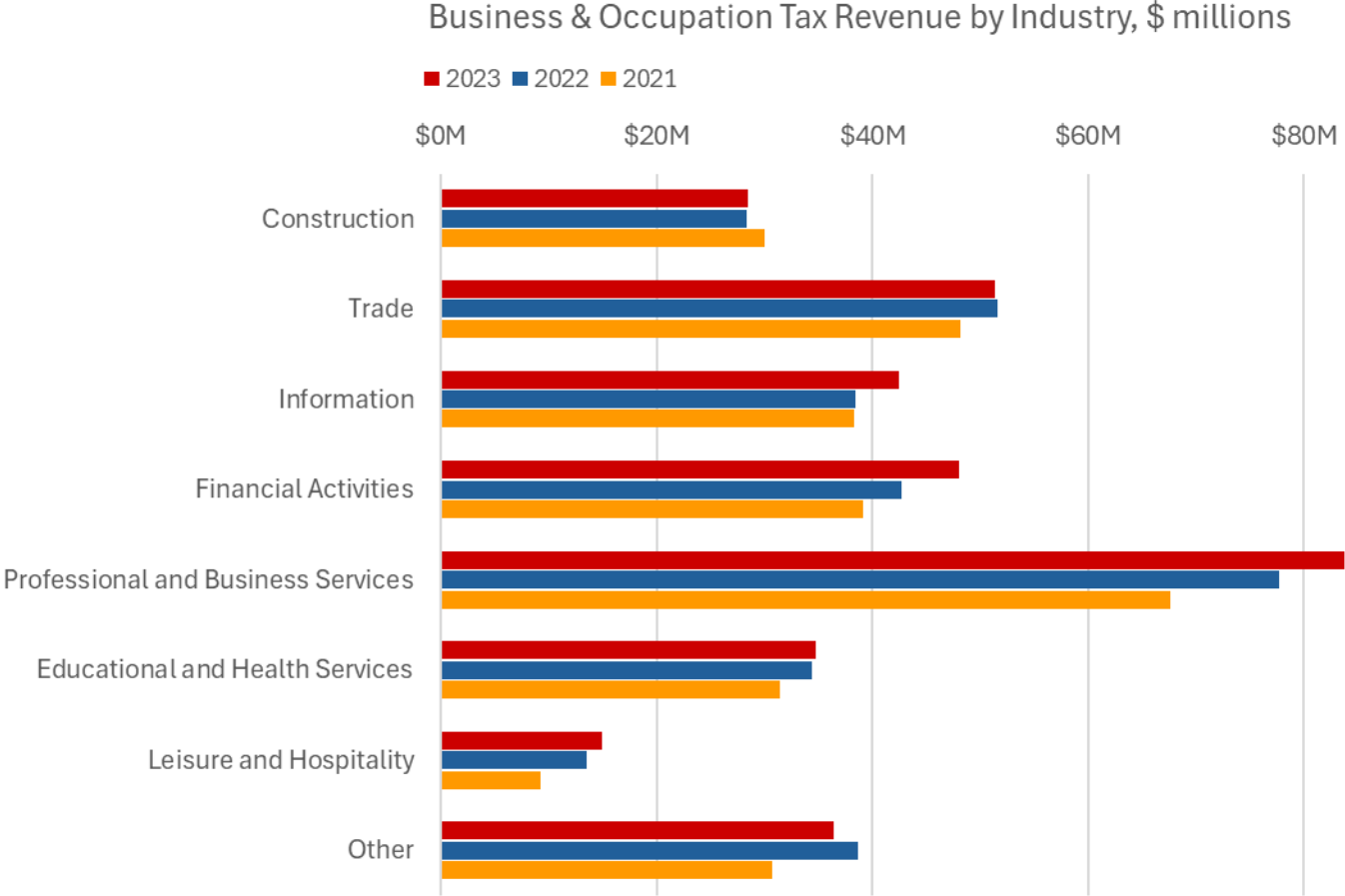
Questions?



Appendix

Business and Occupation Tax

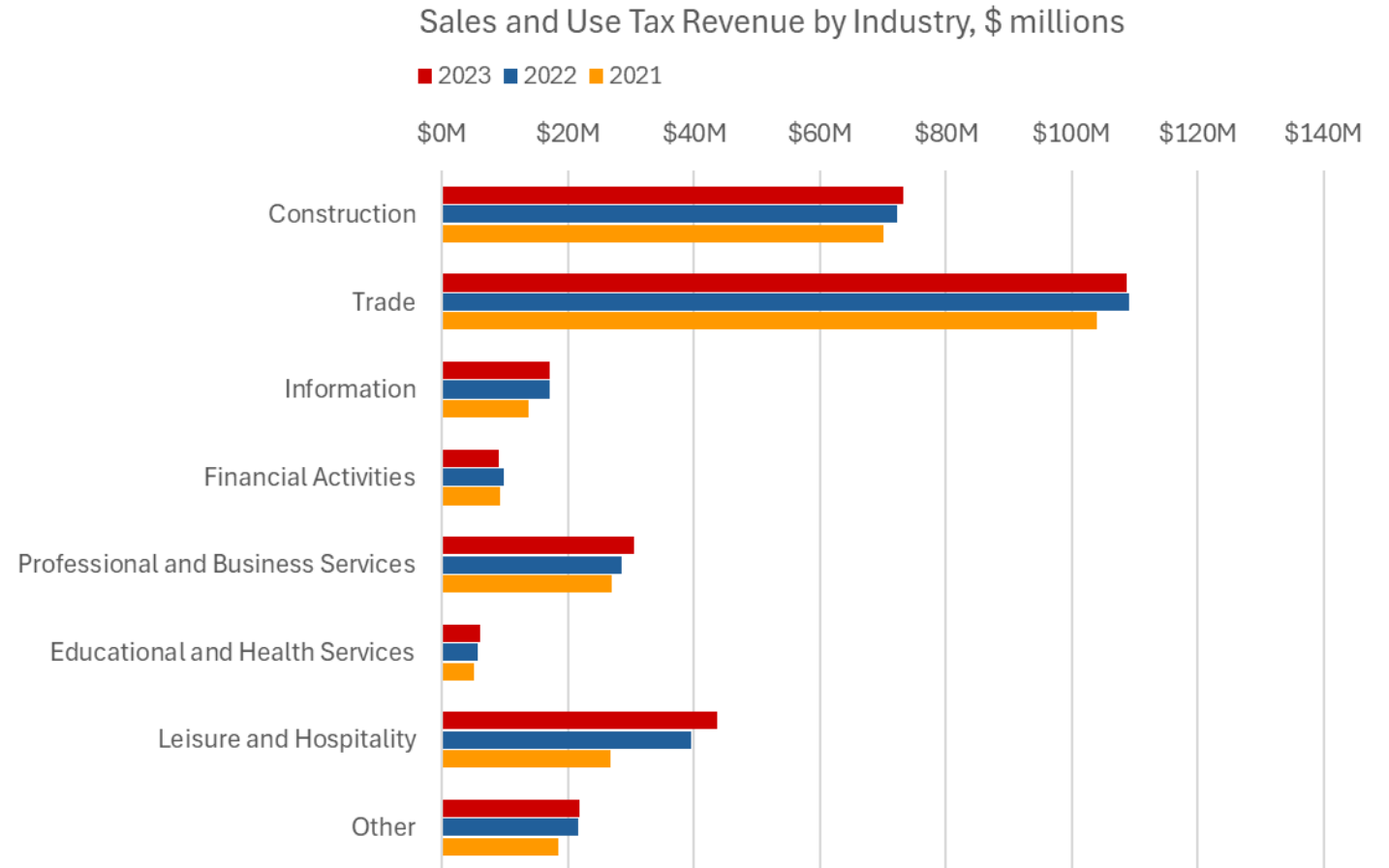
- Tax base for B&O is well diversified, though professional and business services constitute a notably bigger share than other sectors.
- B&O tax is paid by more than 21,000 businesses in 2023.
- Top 10 taxpayers accounted for about 19% of all B&O revenues.



Sales and Use Tax

Tax base for sales tax revenue much less diversified than B&O tax base.

- Trade accounts for one third of total revenue.
- About one quarter of sales tax revenue was in previous years generated by construction sector.
- In 2023 approximately 72,000 taxpayers remitted sales and use tax
- Top 10 taxpayers accounted for about 11% of all sales and use tax revenues in 2023.



Payroll Expense Tax

- Payroll expense tax is paid by less than 500 companies and is highly concentrated at the top
- In 2023, top 100 companies accounted for more than 90% of the tax revenue
- About 70% was generated from just ten companies, with eight of these ten companies operating in the tech sector.

