HdL Companies

SEPTEMBER 2021

CALIFORNIA FORECAST

SALES TAX TRENDS AND ECONOMIC DRIVERS

Shasta County, CA

Delivering Revenue, Insight and Efficiency to Local Government Since 1983

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.

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STATEWIDE SALES TAX TRENDS

HdL Companies

	2021/22 | 2022/23
TOTAL	10.2% | 4.0%

2021/22 | 2022/23

Autos/Transportation 2.4% | 2.4%

Receipts from auto and transportation related sales soared in the second quarter of 2021 with demand strengthened by low financing rates, a year plus of curtailed spending opportunities, government stimulus payments, and borrowing from unexpected found equity in the rising value of real estate and financial assets. Meanwhile, the supply of vehicles has been constrained by chip shortages and other production issues. Recent reports indicate the inventory shortfall is having a significant negative impact on sales, though our projection is that the strong 4th of July holiday at the beginning of the quarter, coupled with higher vehicle pricing, will offset these losses. Some sales are expected to slip during the fourth quarter, with normal gains projected going forward into 2022.

Building/Construction 7.1% | 0.5%

This forecast period follows one in which lumber prices hit record highs in May, only to plunge dramatically immediately afterward. Supply is matching demand for the moment. Further price declines are expected by the end of 2021 as China dumps vast amounts of its lumber reserves on the market. During the second quarter, building permit values climbed higher for the first time in 2.5 years, led by Single and Multi Family Residence projects while nonresidential construction was largely dormant. Office and general retail developers are still waiting for the market to signal that more space is needed before launching projects. Warehouse space is still lagging demand. The surge in permit issuance means future work for contractors and expanded demand for materials. Fire scarred areas will see an increase in supplies purchased to handle board up and roof patching ahead of wet weather.

2021/22 | 2022/23

Business/Industry 11.7% | 4.5%

Fulfillment centers were a large portion of this category's 26% growth as online sales swelled and a taxpayer's reporting change shifted 37% of their revenues from countywide pools to agencies with in-state fulfillment centers. With companies adapting to new ways of doing work, business services and technology activity spiked. While agriculture, farm, and construction equipment sales jumped, it is unknown how the continued drought and wildfires could impact future remittances. Various industries still struggle with challenges such as raw material and qualified worker shortages. Overall, returns are nearing pre-pandemic levels. The overall short-term outlook is modest gains; expect results to vary by region and segment depending upon each jurisdiction's composition of companies within this group.

Food/Drugs 2.0% | 2.0%

Brought about by worker shortages and supply shipping interruptions, inflation has driven up the cost of products in local grocery and drug stores. Prices rose over the past two years and are expected to stabilize in 2022 to a normal level of increase. Areas of the state that have seen housing expansion and/or population gains should experience new outlets built which both meet customer needs and add to the municipality's tax base. Permitted expansions of cannabis merchants has slowed; however, demand remains strong with expected greater sales volumes contributing to the steady improvement of taxes by this sector.

HDL CONSENSUS FORECAST – SEPTEMBER 2021

STATEWIDE SALES TAX TRENDS

HdL Companies

	2021/22 | 2022/23
TOTAL	10.2% | 4.0%

2021/22 | 2022/23

Fuel/Service Stations 23.1% | 2.8%

This industry experienced upward price pressure on sales taxes received through June. Concern for recent spikes in the COVID-19 variant has not significantly reduced demand for fuel in California. The average cost of a gallon of gas is at the highest level since the all-time record of $4.73 set in October 2012. Oil barrel prices are in the low $70 range and a temperate resurgence of air travel boosted recent jet fuel prices up to pre-pandemic levels. Our forecast projects consumption of fuel to trend positively through all of fiscal year 2021/2022. By the end of that year, much of the taxes lost during the worst periods of 2020 should be largely recovered.

General Consumer Goods 9.1% | 1.8%

Consumers continued to show resiliency with respect to spending in the second quarter of 2021, rebounding from the depths of the pandemic's impacts one year prior. Statewide, second quarter local tax receipts improved five percent above pre-pandemic levels. Spurred by federal stimulus, pent-up demand and a wider opening of the state economy, retailers across the boards rang up more transactions. Looking ahead, this group is expected to perform well despite a rise in Delta variant infections, recovering supply chains and decreased stimulus support. Trending back to in-person shopping, consumer demand remains healthy proven by recent data amid elevated prices. HdL expects to see positive trends endure through the remainder of the year fueled by a strong back to school shopping season and a robust holiday season that should be supported by the addition of monthly child tax credit payments.

2021/22 | 2022/23

Restaurants/Hotels 29.5% | 6.0%

Restaurants/hotels were one of the hardest hit industry groups during the beginning of the COVID-19 health crisis. In the second quarter of 2021 as restrictions were lifted and pent-up demand was released, the numbers, compared to the lowest quarter of the pandemic, strongly rebounded. Quick service receipts surpassed pre-pandemic levels while other restaurant segments neared 2019 comparable period results. Hotels began to rebound, but regional differences, a slow return for business travel and the lack of international travelers caused this group to lag behind restaurants. The 2021/22 percentage gain is sizable, mostly linked to recovery of what was lost in the preceding two fiscal years when many establishments were closed or had limited operations for weeks at a time.

State and County Pools 7.1% | 8.0%

The continual transference in consumer spending moving away from in-store purchases to the considerable ease and humongous inventory options accessible through mobile apps accelerated again as the state's economy rebounds from retailers' COVID-19 impacts last spring. Interestingly, recent returns reported a modest 10% climb, even after accounting for one company's change in return filing that redirected about one-third of use taxes collected to date for 2021 away from the pools and to local agencies with facilities that ship directly to customers. Many economic experts forecast e-commerce/m-commerce to capture a larger share of total retail sales in the coming years. Working from home and other changes brought about by COVID-19 suggest households' future spending aligns with these lifestyle patterns. Pools growth is forecasted to produce gains aligned closer to historic levels dating back to 2019 and prior years.

Proposition 172 projections vary from statewide Bradley-Burns calculations due to the state's utilization of differing collection periods in its allocations to counties. HdL forecasts a statewide increase of 9.6% for Fiscal Year 2021/22 and 4.0% for 2022/2023.

NATIONAL AND STATEWIDE
ECONOMIC DRIVERS

Beacon Economics

2020/21 | 2021/22

U.S. Real GDP Growth 13.0% | 4.0%

With stellar growth in the first half of 2021, U.S. GDP surpassed pre-pandemic levels despite having 5 million fewer workers than early last year. More people are expected to rejoin the workforce as wages rise, but a smaller workforce will not necessarily mean slower economic growth if recent productivity increases can be sustained. Businesses are investing heavily in this. Capital expenditures are up by $600 billion (9.2%) from the pre-pandemic peak. Meanwhile, highly effective vaccines have substantially decreased the economic risks from COVID-19. Temporary surges in cases will simply push growth to the following quarter rather than leave any lasting impact. The greater risk in the medium term is the coming unwinding of monetary stimulus from the U.S. Federal Reserve, which will increase the cost of servicing debt for public and private entities.

U.S. Unemployment Rate 6.9% | 4.4%

The rapid decline of unemployment to 5.2% in August reflects improving economic conditions but obscures the rocky recovery in the labor market. Total employment remains depressed because of a confluence of factors, including mass retirements of baby boomers and generous unemployment support. The expiration of COVID-related unemployment benefits in September, along with rising wages, will entice more people to seek work. But do not expect a complete return to the status quo. Higher labor costs will continue to fundamentally alter segments of the economy. Companies will be forced either to close or innovate through automation, retraining or pivoting to other business offerings. This will particularly impact the service sector, including restaurants and hotels.

CA Total Nonfarm Employment Growth -5.5% | 6.2%

Following the broad national trend, California's recovery has been rapid but with far fewer workers. This trend was evident before pandemic restrictions lifted, with the state clawing back to within 98.5% of its pre-pandemic size by the first quarter of 2021 (the latest available data). As a result, the economy is now almost certainly larger than pre-pandemic levels. Despite this trend, total nonfarm employment remains 1.2 million jobs (7%) smaller than before the pandemic. On the one hand, this underscores the considerable leaps in productivity achieved to sustain the recovery with far fewer workers. On the other hand, the dearth of workers could devastate some small businesses, particularly in retail and entertainment, whose existence and profit margins depend on staffing. Expected higher wages will eventually attract more workers, but California's labor market will not return to pre-pandemic levels until the fourth quarter of 2022.

2020/21 | 2021/22

CA Unemployment Rate 7.6% | 4.8%

The unemployment rate in California has already dropped by more than half since the depths of the pandemic. Part of this improvement is a function of the huge increase in the number of people not seeking work, a category not counted as unemployed in government surveys, but not all of these workers have left the labor force indefinitely. As a result, the lower unemployment rate tends to confuse the complex labor market recovery, which is better demonstrated by total nonfarm employment. Higher unemployment rates may even be a welcome sign that hot economic conditions are inducing workers to look for work after having temporarily dropping out of the workforce. Unemployment should continue to steadily decline into next year.

CA Median Existing Home Price $626,187 | $669,232

The eye-popping 18% increase in housing prices in the past year has been fueled by extremely low inventories, currently at a historic low of 1.8 months' supply. Ample household savings, rising asset prices, and low interest rates have further driven the housing boom. This has powered a broad increase in prices across the state. The Case-Shiller Index for Los Angeles and San Francisco increased over 37% and 20% on a month-over-month annualized basis in June, but these remain far from historic high increases for each of these municipalities. Although the market will cool slightly in the fall, housing prices are expected to increase 6% on a year-over-year basis in the coming quarters. Prices are more likely to come under control as interest rates rise in 2022.

CA Residential Building Permits 126,181 | 135,285

The recent passing of California's Senate Bill 9, which compels local governments to allow high-density housing, will help alleviate the ongoing housing crisis caused by inadequate supply. The law could increase the number of building permits in the coming years. In the meantime, permits are expected to continue to rise into next year, topping 120,000 for the first time since 2007.

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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.

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Beacon Economics has proven to be one of the most thorough and accurate economic research/analytical forecasting firms in the country. 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 and HdL helps both companies enhance the accuracy of the work that they perform for their respective clients.

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