

CITY OF SAN JOSE
2024-2025 PROPOSED OPERATING BUDGET
GENERAL FUND OVERVIEW

Introduction

For 2024-2025, General Fund revenue estimates (excluding Fund Balance) total \$1.4 billion, representing a 1.7% increase from the 2023-2024 Adopted Budget level. When the Fund Balance-Carryover is included, General Fund resources total \$1.5 billion, which is 24.9% below the prior year. This comparison, however, is misleading as the Proposed Budget does not yet contain estimates for carryover rebudget funding, which was a significant portion of the 2023-2024 Adopted Budget Fund Balance total. Rebudgets for the 2024-2025 budget will be brought forward later in the budget process.

Estimates for the 2024-2025 Beginning Fund Balance and for over 450 separate General Fund revenue accounts were formulated as part of the 2025-2029 Five-Year Forecast that was released at the end of February 2024. These estimates have been reviewed continually since the Forecast document was released and have been revised, as appropriate, in the Proposed Budget based on updated information. Estimates for each account are based upon a careful examination of the collection history and patterns as they relate to such factors as seasonality and performance in the economic environment that the City is most likely to encounter in the coming year. Most estimates involve two projections: an estimate for the amount to be collected in 2023-2024; and an estimate for the increase or decrease in activity, resulting in the anticipated receipts for 2024-2025. Each source of revenue can be influenced by external (outside of the City’s control) and/or internal factors. The 2024-2025 General Fund revenue estimates are summarized below and discussed in detail in the material that follows.

Revenue Category	1 2022-2023 Actuals	2 2023-2024 Adopted	3 2024-2025 Forecast	4 2024-2025 Proposed	2 to 4 % Change	% of Total
Property Tax	\$ 449,014,347	\$ 460,400,000	\$ 492,000,000	\$ 492,000,000	6.9%	32.1%
Sales Tax	343,472,084	336,400,000	344,000,000	344,000,000	2.3%	22.5%
Transient Occupancy Tax	14,936,816	16,000,000	16,000,000	16,000,000	0.0%	1.0%
Franchise Fees	44,823,852	51,825,008	54,445,008	55,022,632	6.2%	3.6%
Utility Taxes	124,266,765	126,550,000	136,000,000	136,000,000	7.5%	8.9%
Business Taxes	89,626,955	87,500,000	87,000,000	87,000,000	(0.6%)	5.7%
Real Property Transfer Tax	56,279,648	50,000,000	0	0	N/A	0.0%
Telephone Line Tax	21,093,889	22,000,000	22,000,000	22,000,000	0.0%	1.4%
Licenses and Permits	17,756,820	22,005,622	21,314,491	22,179,390	0.8%	1.4%
Fees, Rates, and Charges	23,595,906	22,372,680	25,806,133	26,740,860	19.5%	1.7%
Fines, Forfeitures and Penalties	17,352,624	15,080,000	16,804,797	17,604,797	16.7%	1.2%
Rev. from Money and Property	19,157,555	14,864,000	18,735,000	18,735,000	26.0%	1.2%
Rev. from Local Agencies	25,497,190	18,975,403	17,371,268	17,951,649	(5.4%)	1.2%
Rev. from State of California	19,912,631	22,110,719	13,100,000	29,100,000	31.6%	1.9%
Rev. from Federal Government	4,962,143	7,391,504	0	1,384,000	(81.3%)	0.1%
Other Revenue	291,249,120	10,257,667	8,738,257	9,050,067	(11.8%)	0.6%
Transfers and Reimbursements	140,748,332	125,768,078	138,987,687	139,014,498	10.5%	9.1%
Subtotal	\$ 1,703,746,677	\$ 1,409,500,681	\$ 1,412,302,641	\$ 1,433,782,893	1.7%	93.6%
Fund Balance-Carryover ⁽¹⁾	639,359,298	629,626,855	89,217,944	96,871,142	(84.6%)	6.4%
Total General Fund Sources	\$ 2,343,105,975	\$ 2,039,127,536	\$ 1,501,520,585	\$ 1,530,654,035	(24.9%)	100.0%

⁽¹⁾ The Fund Balance figure does not include the Reserve for Encumbrances.

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Economic Performance

The following is a discussion of both the national and local economic outlooks used to develop the 2024-2025 revenue estimates. Various economic forecasts and models were reviewed in the development of the 2024-2025 revenue estimates. The City also uses an economic forecasting consultant and consultants that focus on particular revenue categories, such as Sales Tax and Transient Occupancy Tax, to assist in the development of the revenue estimates and provide information on the future outlook in these areas. A more detailed discussion on forecasted economic conditions can be found in the 2025-2029 Five-Year General Fund Forecast.

National Outlook

The U.S. economy remains remarkably resilient despite the prevailing high interest rate environment. One year ago, there were widespread concerns of an impending recession, yet a recession never materialized. Currently, the economy continues to expand at a modestly positive pace, with recent indicators showing no imminent signs of recession. Policy wise, the economy is transitioning from a period of Federal Reserve interest rate hikes to a more stable rate environment, with expectations of rate cuts in the coming months. Although economic growth remains subdued compared to recent historical standards, the latest GDP estimate indicates a 3.3% annual rate, with an overall rate hovering around 2.5% for the past year.

Much of the ongoing economic strength can be attributed to substantial deficit spending by the federal government, injecting billions of dollars into the economy annually. Besides regular social spending, the spending has notably increased investments in alternative energy and infrastructure. However, concerns are rising as deficits approach unsustainable levels, nearing \$2 trillion annually. While domestic fiscal and monetary policies remain stable, global uncertainties, particularly the conflicts in Ukraine and the Middle East, pose significant threats to the national economic outlook.

United States economic growth is anticipated to slow down enough to mitigate inflationary pressures without precipitating a recession. Inflation and interest rates are anticipated to remain lower compared to recent years, with the lower interest rates anticipated to stabilize the housing sector and bolster the economy's resilience against recessionary pressures. However, despite the absence of a recession, economic growth is anticipated to be sluggish. Gross Domestic Product (GDP) is expected to hover around 1% for most of 2024, then modestly grow to 2% in 2025 and 2026.

As of December 2023, per the U.S. Bureau of Labor Statistics, the national unemployment rate of 3.5% has shown little net movement since early 2023. As a recession is not anticipated to occur, unemployment levels are anticipated to remain low, between 3.5%-4% over the next several years.

On a national level, consumer confidence increased in December after experiencing a decline in November. According to Dana Peterson, Chief Economist at The Conference Board, "December's increase in consumer confidence reflected more positive ratings of current business conditions and job availability, as well as less pessimistic views of business, labor market, and personal income prospects over the next six months."¹

¹ The Conference Board, Consumer Confidence Survey, December 2023.

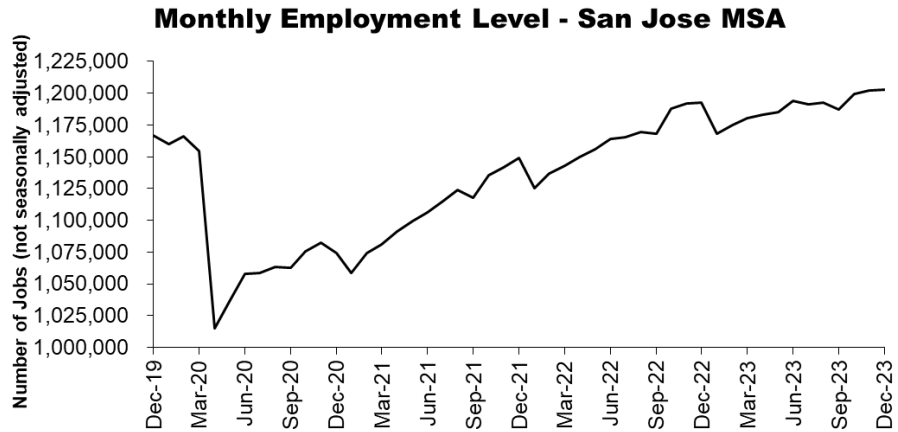
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Economic Performance

City of San José Outlook

While Silicon Valley continues to show an overall positive economic performance, there are several areas that have shown signs of concern. Over the last year, layoff notices in the technology sector were consistently being publicized, indicating a slowdown in Silicon Valley's economy. In addition, due to interest rates consistently raising, transactions in the local real estate market have been sluggish.

The December 2023 employment level of 1.20 million in the San José-Sunnyvale-Santa Clara Metropolitan Statistical Area (San José MSA) grew by 10,500 jobs, or 0.9%, from the December 2022 level of 1.19 million. This increase includes private education and health services adding 10,900 jobs; leisure and hospitality growing by 8,500 jobs; manufacturing decreasing by 3,600 jobs; the information sector eliminating 3,500 jobs; construction dropping 2,600 jobs, and financial activities decreasing by 2,400 jobs.²



Unemployment Rate (Unadjusted)			
	Dec. 2022	Nov. 2023	Dec. 2023**
San José Metropolitan Statistical Area*	2.4%	3.9%	4.0%
State of California	3.9%	4.9%	5.1%
United States	3.3%	3.5%	3.5%
* San Benito and Santa Clara Counties Source: California Employment Development Department. ** December 2023 estimates are preliminary and may be updated.			

The local unemployment rate for December 2023 was 4.0%, which is slightly higher than the November 2023 rate of 3.9% and is significantly higher than the prior year unemployment rate of 2.4%. While the December 2023 San José Metropolitan Statistical Area unemployment rate continues to be lower than the unadjusted unemployment rate for the State (5.1%), it is higher than the national rate (3.5%).

Overall construction activity through December 2023 decreased 8.7% from prior-year levels primarily due to activity for the commercial and industrial land use categories experiencing significant year-over-year decreases. The decrease would be more prominent if it were not for the significant increase in residential construction, which is showing a 90.8% increase when compared to the prior year. If current trends continue, construction activity will underperform the activity projected by the Planning, Building and Code Enforcement Department in the 2024-2028 Five-Year Forecast, which was released in February 2023.

² State of California Employment Development: Labor Market Information Division Press Release, January 19, 2024.

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City of San José Outlook

Through December, residential permit valuation has increased 90.8% from prior-year levels, primarily driven by a 137% increase in new construction (\$156.2 million in 2023-2024 from \$65.9 million in 2022-2023). Residential activity through December included 739 multi-family units and 241 units of single-family construction for a total of 980 units (45% increase). Notable projects for November and December include permits for a 64-unit affordable residential project located on North Bascom Avenue, near the intersection with Heatherdale Avenue, a 90-unit 100% affordable residential project located on Race Street, between West San Carlos Street and Park Avenue, and an 81-unit 100% affordable project including 17,000 square feet of social services (Parkmoor Hub Youth Center) located at the corner of Parkmoor Avenue and Meridian Avenue.

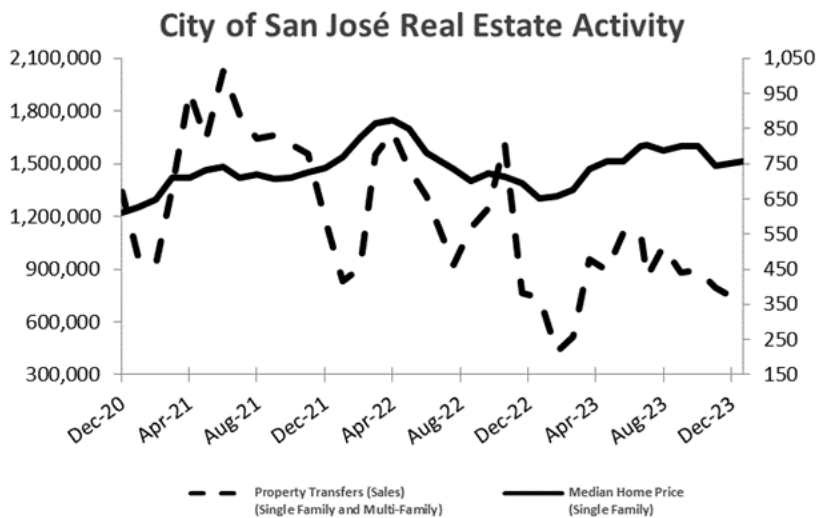
Private Sector Construction Activity (Valuation in \$ Millions)			
	YTD Dec. 2022	YTD Dec. 2023	% Change
Residential	\$ 121.4	\$ 231.7	90.8
Commercial	\$ 363.6	\$ 221.0	(39.2%)
Industrial	\$ 184.7	\$ 159.0	(13.9%)
	\$ 669.8	\$ 611.8	(8.7%)

Commercial valuation through December 2023 was 39.2% lower than the 2022-2023 level, led by a 62% drop in new construction (\$50.4 million in 2023-2024 from \$131.1 million in 2022-2023). Alterations accounted for 77% (\$170.6 million) of the commercial activity through December. A notable project for November and December includes a permit issued for a new service station located on Evergreen Loop, west of East Capital Expressway.

Industrial construction valuation through December was 13.9% lower than prior-year levels. Alterations accounted for 80% of activity through December (\$127.8 million).

According to data from the Santa Clara County Association of Realtors, in December 2023, the median single-family home price totaled \$1.5 million, which is 16.5% above the December 2022 price of \$1.3 million. In addition, these more expensive homes are selling at a quicker rate. The average days-on-market through December 2023 totaled 19 days, while the average days through December 2022 totaled 25 days.

Conversely, through the first half of the fiscal year, property transfers have fallen almost 20% from the prior year's level. On a positive note, the pace of decline has lessened, with November and December transactions showing only single digit percentage declines, as opposed to double digit year-over-year drops over the prior year.



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Revised General Fund Forecast

Between the issuance of the Five-Year Forecast in February 2024 and the release of the Proposed Budget in May 2024, revenue collections for 2024-2025 continued to be reviewed and updated. Based on this analysis, several of the revenue estimates presented in the February Forecast were revised in this budget to reflect more recent information. These adjustments resulted in a net \$42.2 million reduction to the General Fund Forecast, decreasing the revenue estimate from \$1.54 billion to \$1.50 billion (including fund balance). Below is a summary table of the changes incorporated into the Revised Forecast, which were used as the starting point in preparing the 2024-2025 Proposed Budget.

Category	\$ Change	Description
Beginning Fund Balance	\$ 4,043,944	Increase of \$4.0 million reflects savings from various Measure E appropriations that are not anticipated to be expended by the end of 2023-2024 and will be rebudgeted to 2024-2025 and then transferred to the Real Property Transfer Tax Fund.
Transfers and Reimbursements	2,685,313	Net increase of \$2.7 million reflects updated overhead reimbursements from capital and operating funds based on the final 2024-2025 base budget and overhead rates (\$1.9 million) and higher transfers and reimbursements to the General Fund (810,719).
Fees, Rates, and Charges	1,265,218	Increase of \$1.3 million aligns revenues with estimated base costs and activity levels for Miscellaneous fees (\$545,218), Parks, Recreation and Neighborhood Services Department fees (\$500,000), and Police Department fees (\$220,000).
Other Revenue	110	Increase of \$110 aligns revenues with the estimated base costs and activity levels for reimbursement revenue.
Real Property Transfer Tax	(50,000,000)	Decrease of \$50.0 million reflects the movement of the Real Property Transfer Tax revenue from the General Fund to the Real Property Transfer Tax Fund; the revenue estimate itself remains unchanged. The associated expenditures have also been transferred to the Real Property Transfer Tax Fund as part of the Revised General Fund Forecast.
Revenue from Local Agencies	(215,000)	Decrease of \$215,000 reflects a reduction of payments from other agencies for Animal Care Services as the Town of Los Gatos has opted to not renew their contract with the City of San José.
Total	<u>(\$ 42,220,415)</u>	

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Changes from Revised Forecast to Proposed Budget

From the Revised Forecast of \$1.50 billion, a net increase of \$29.1 million to the General Fund revenue estimates is included in the Proposed Budget, bringing the 2024-2025 revenue estimate to \$1.53 billion (including fund balance). The components of this change include an increase to the estimate for the 2023-2024 Ending Fund Balance/2024-2025 Beginning Fund Balance (\$7.7 million) and an increase to various revenue categories (\$21.5 million). The revenue changes are summarized in the table below.

<u>Category</u>	<u>\$ Change</u>	<u>Description</u>
Revenue from the State of California	\$ 16,000,000	Increase of \$16.0 million reflects new grant funding that is anticipated to be received in 2024-2025 from the State of California to support the City's Interim Housing Portfolio.
Beginning Fund Balance	7,653,198	Increase of \$7.7 million reflects various adjustments, including: fund balance from additional revenue and expenditure savings that is anticipated to be received in 2023-2024 and be available for use in 2024-2025 (\$5.0 million); the liquidation of carry-over encumbrances (\$1.3 million); the liquidation of the Solid Waste Code Enforcement Reserve (\$680,000); and the rebudget of funds for expenditure-related items that are not anticipated to occur until 2024-2025 (\$647,830).
Revenue from Federal Government	1,384,000	Increase of \$1.4 million reflects two new federal grants that are anticipated to be received in 2024-2025, including Transportation, Housing and Urban Development funding for the Rue Ferrari Emergency Interim Housing Site Expansion (\$1.0 million) and Clean Creeks, Healthy Watersheds program (\$384,000).
Fees, Rates, and Charges	934,727	Net increase of \$934,727 reflects various fee changes to align revenues with estimated activity levels, reflect fee revisions, and maintain cost recovery levels for Miscellaneous fee revenue (\$1.0 million), Transportation Department fee revenue (\$80,273), Police Department fee revenue (\$15,963), and Parks, Recreation, and Neighborhood Services department fee revenue (-\$174,917).
Licenses and Permits	864,899	Net increase of \$864,899 reflects various license and permit changes to align revenues with estimated activity levels, reflect fee revisions, and maintain cost recovery levels for the Fire Department (\$469,700) and other licenses and permits (\$395,199).

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Changes from Revised Forecast to Proposed Budget

Category	\$ Change	Description
Fines, Forfeitures, and Penalties	\$ 800,000	Increase of \$800,000 reflects a revision to the parking fines program that will result in increased revenue generation.
Revenue from Local Agencies	580,381	Increase of \$580,381 reflects a new local agency reimbursement that is anticipated to be received in 2024-2025 from Valley Water for the Regulatory Compliance and Purified Water program.
Franchise Fees	577,624	Increase of \$577,624 reflects an increase in the Commercial Solid Waste fees by 4.1% based on cost changes including a Consumer Price Index adjustment.
Other Revenue	311,810	Increase of \$311,810 reflects revenue anticipated to be received from the Accounts Receivable Amnesty Program that will be conducted by the Finance Department (\$300,000), and reflects various fee changes to align revenues with estimated activity levels, reflect fee revisions, and maintain cost recovery levels for the Transportation Department (\$11,810).
Transfers and Reimbursements	26,811	Net increase of \$26,811 reflects a transfer from the Construction Excise Tax Fund to the General Fund (\$300,000) and reduced overhead from budget actions that change the staffing levels funded by special and capital funds (-\$273,189).
Total	\$ 29,133,450	