



CITY OF PALO ALTO OFFICE OF THE CITY AUDITOR

June 29, 2015

The Honorable City Council
Palo Alto, California

City of Palo Alto Sales Tax Digest Summary Fourth Quarter Sales (October - December 2014)

The following files are attached for this informational report for which no action is required.

ATTACHMENTS:

- Attachment A: Sales Tax Digest Summary - Background and Discussion(PDF)
- Attachment B: MuniServices Sales Tax Digest Summary (PDF)
- Attachment C: Economic Categories and Segments (PDF)
- Attachment D: MuniServices Economic Overview (PDF)

Department Head: Harriet Richardson, City Auditor



CITY OF
**PALO
ALTO**

Office of the City Auditor

Sales Tax Digest Summary – Fourth Quarter Sales (October – December 2014)

Informational Report to the City Council

BACKGROUND

Sales and use tax represents about 15 percent, or \$26 million, of projected General Fund revenue in the City's Adopted Operating Budget for fiscal year 2015. This revenue includes sales and use tax for the City of Palo Alto and pool allocations from the State and Santa Clara County.¹

The Office of the City Auditor contracts with MuniServices LLC (hereafter MuniServices), the City's sales and use tax consultant, to obtain sales and use tax recovery services and informational reports. The Office of the City Auditor uses the recovery services and informational reports to help identify misallocation of tax revenue owed to the City, and to follow up with the State Board of Equalization to ensure the City receives identified revenues. The Office of the City Auditor includes information on sales and use tax recoveries in our quarterly reports to the Policy and Services Committee.

The California Revenue and Taxation Code, Section 7056, requires that sales and use tax data remain confidential. As such, the City may not disclose amounts of tax paid, fluctuations in tax amounts, or any other information that would disclose the operations of a business. This report, including the attached Sales Tax Digest Summary, includes certain modifications and omissions to maintain the confidentiality of taxpayer information.

The Office of the City Auditor also shares the information provided by MuniServices with the Administrative Services Department (ASD) for use in revenue forecasting and budgeting, and with Economic Development for business outreach strategies. We coordinated this informational memo with them.

DISCUSSION

The attached report (Attachment B) was prepared by MuniServices and covers calendar year 2014 fourth quarter sales (October through December 2014). These funds are reported as part of the City's fiscal year 2015 revenue. In June, ASD should receive information from the State on aggregate sales and use tax receipts for first quarter 2015.

¹ See definitions on page 4.

Following are some highlights of the sales and use tax information we received:

- In Palo Alto, overall sales and use tax revenue (cash receipts) for the fourth quarter ending December 2014 decreased by approximately \$106,000, or 1.4 percent, including pool allocations, compared to the fourth quarter ending December 2013. For all jurisdictions in Santa Clara County, sales and use tax revenue for the fourth quarter ending December 2014 increased by \$5.7 million, or 5.6 percent, compared to the fourth quarter ending December 2013.
- Statewide, almost every region in California experienced an increase in sales and use tax revenue for the year ending December 2014. Statewide sales and use tax revenue has shown growth of 4.0 percent during the fourth quarter ending December 2014 compared to the fourth quarter ending December 2013.
- In Palo Alto, sales and use tax revenue totaled \$25.6 million for the year ending December 2014, a decrease of 10.2 percent from \$28.5 million in the prior year ending December 2013. This change is due in part to an unexpectedly high and one-time flow of revenue in FY 2013 and not from a decrease in base receipts. This amount includes sales and use tax for the City of Palo Alto and pool allocations from the State and Santa Clara County.
- Excluding pool allocations and adjusting for prior period and late payments, Palo Alto's sales and use tax revenue for the fourth quarter ending December 2014 decreased by 2.7 percent compared to the fourth quarter ending December 2013. On a yearly basis, Palo Alto's sales and use tax revenue for the year ending December 2014 decreased by 11.8 percent compared to the prior year ending December 2013. The explanation for this decrease is provided in the previous bullet.

More detailed information is shown in Attachment B.

Economic Influences on Sales and Use Tax

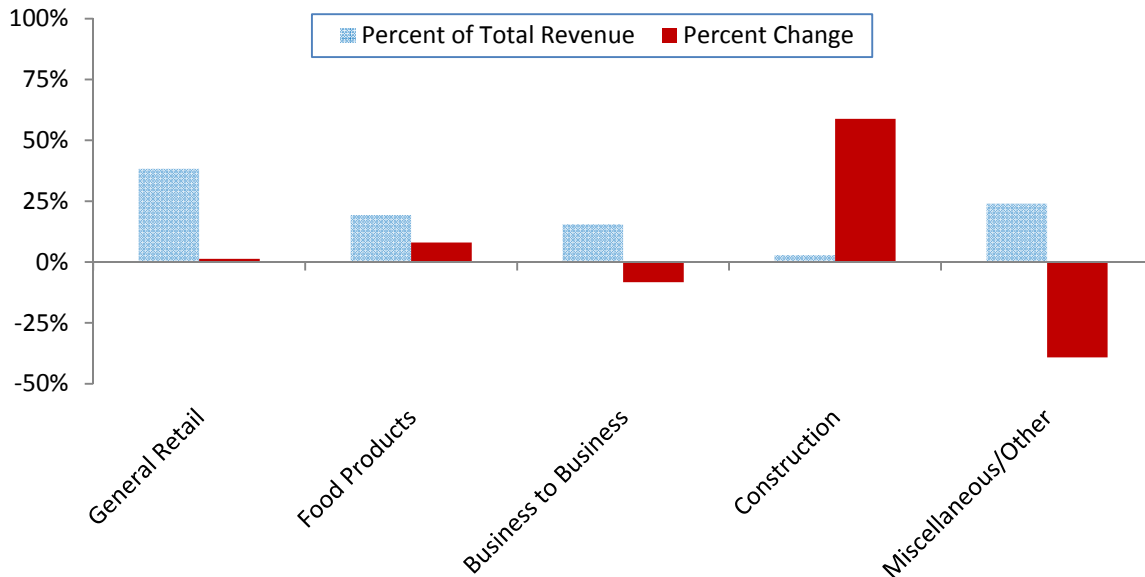
In its Economic Overview & News (Attachment C), MuniServices discusses economic influences, including national and state economic trends, the job market, retail and auto sales, and forecast information that may affect the City's sales and use tax revenue.

Preliminary estimates from the State of California Employment Development Department show that the March 2015 unemployment rate, which is not seasonally adjusted, is 4.1 percent in Santa Clara County and 2.8 percent in Palo Alto.

Economic Category Analysis

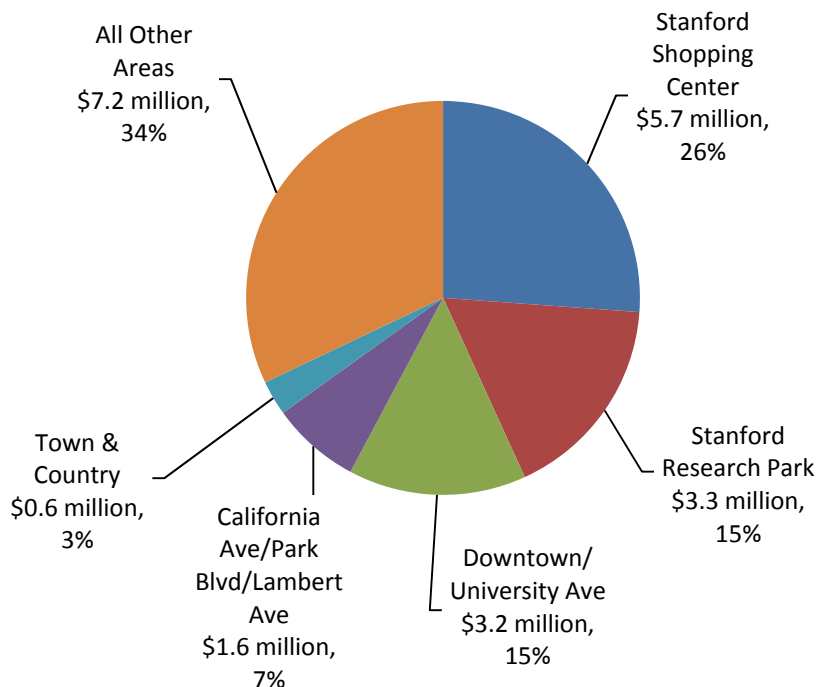
MuniServices' analysis of economic categories for the year ending December 2014 shows that General Retail comprised 38.3 percent of Palo Alto's sales and use tax revenue and increased by 1.3 percent compared to the prior year. Food Products comprised 19.3 percent of total revenues and increased by 8.0 percent. Business to Business comprised 15.5 percent of total revenues and decreased by 8.3 percent.

Exhibit 1 - Comparison of Palo Alto's Sales and Use Tax Revenue and Percent Change by Economic Category for the Year Ending December 2014



The following chart shows sales and use tax revenue by geographical area based on information provided by MuniServices.

Exhibit 2 – Palo Alto's Sales and Use Tax Revenue by Geographical Area For the Year Ending December 2014 (Amounts include tax estimates and exclude pool allocations)



DEFINITIONS

In California, either sales tax or use tax may apply to a transaction, but not both. The sales and use tax rate in Palo Alto is 8.75 percent.

Sales tax – imposed on all California retailers; applies to all retail sales of merchandise (tangible personal property) in the state.

Use tax – generally imposed on consumers of merchandise (tangible personal property) that is used, consumed, or stored in this state; purchases from out-of-state retailers when the out-of-state retailer is not registered to collect California tax, or for some other reason does not collect California tax; leases of merchandise (tangible personal property).

Countywide/statewide pools – mechanisms used to allocate local tax that cannot be identified with a specific place of sale or use in California. Local tax reported to the pool is distributed to the local jurisdiction each calendar quarter using a formula that relates to the direct allocation of local tax to each jurisdiction for a given period.

Examples of taxpayers who report use tax allocated through the countywide pool include construction contractors who are consumers of materials used in the improvement of real property and whose job site is regarded as the place of business, out-of-state sellers who ship goods directly to consumers in the state from inventory located outside the state, and California sellers who ship goods directly to consumers in the state from inventory located outside the state.

Other examples of taxpayers who report use tax through the pools include auctioneers, construction contractors making sales of fixtures, catering trucks, itinerant vendors, vending machine operators and other permit holders who operate in more than one local jurisdiction but are unable to readily identify the particular jurisdiction where the taxable transaction takes place.

Respectfully submitted,



Harriet Richardson
City Auditor

Sources: MuniServices; California State Board of Equalization; State of California Employment Development Department; City of Palo Alto Fiscal Year 2015 Adopted Operating Budget

Audit staff: Lisa Wehara

City of Palo Alto
Sales Tax Digest Summary
Collections through March 2015
Sales through December 2014 (2014Q4)

California Overview

The percent change in cash receipts from the prior year was 4.5% statewide, 4.8% in Northern California and 4.2% in Southern California. The period's cash receipts include tax from business activity during the period, payments for prior periods and other cash adjustments. When we adjust for non-period related payments, we determine the overall business activity increased for the year ended 4th Quarter 2014 by 3.9% statewide, 4.0% in Southern California and 3.8% in Northern California.

City of Palo Alto

For the year ended 4th Quarter 2014, sales tax cash receipts for the City declined by -10.2% from the prior year. On a quarterly basis, sales tax revenues decreased by -1.4% from 4th Quarter 2013 to 4th Quarter 2014. The period's cash receipts include tax from business activity during the period, payments for prior periods and other cash adjustments.

Excluding state and county pools and adjusting for anomalies (payments for prior periods) and late payments, local sales tax decreased by -11.8% for the year ended 4th Quarter 2014 from the prior year. On a quarterly basis, sales tax activity declined by -2.7% in 4th Quarter 2014 compared to 4th Quarter 2013.

Regional Overview

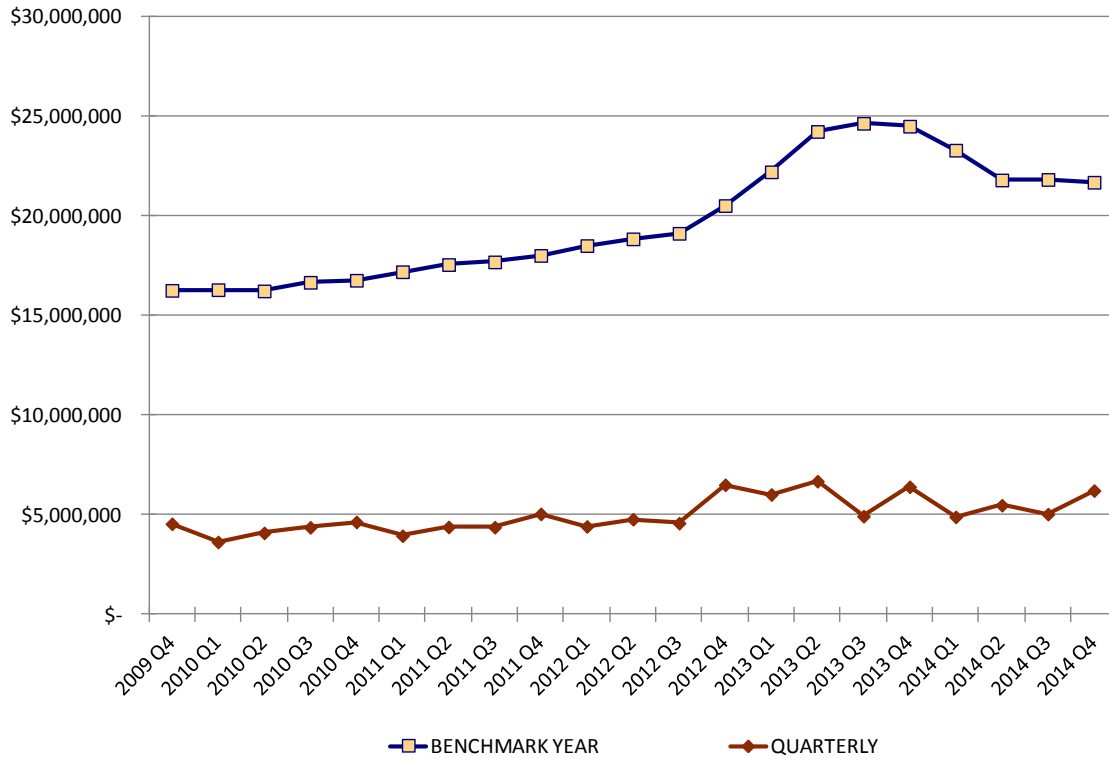
This seven-region comparison includes estimated payments and excludes net pools and adjustments.

CITY OF PALO ALTO

BENCHMARK YEAR 2014Q4 COMPARED TO BENCHMARK YEAR 2013Q4

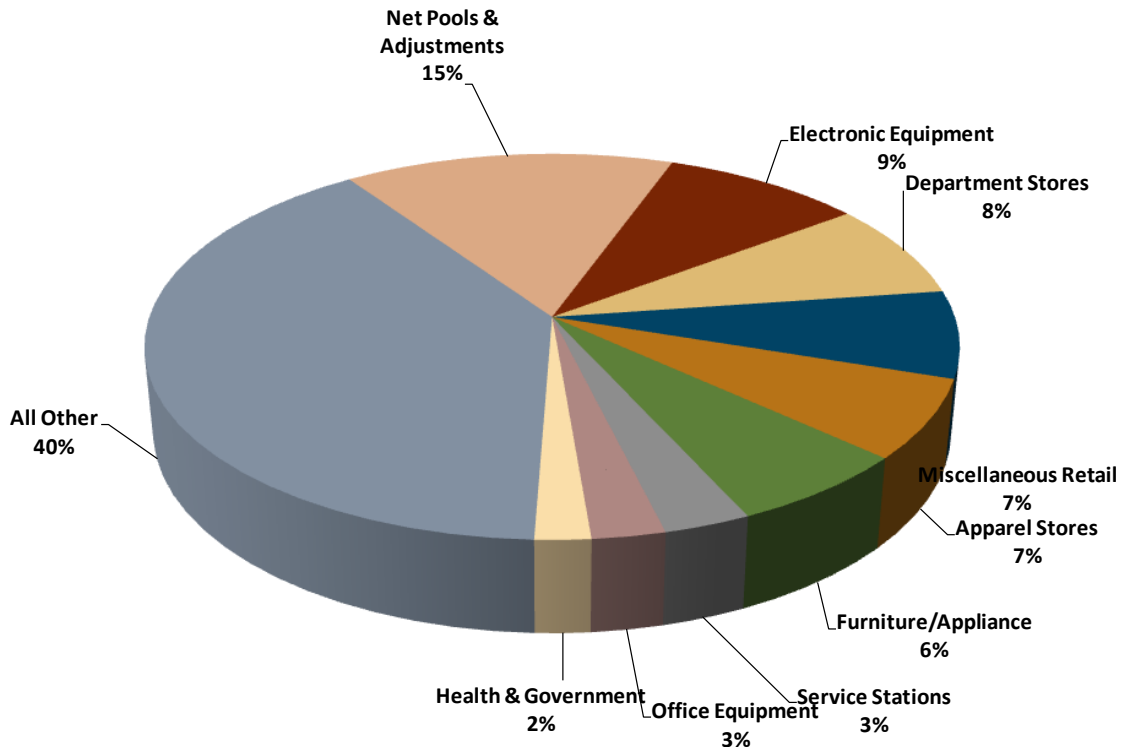
ECONOMIC CATEGORY ANALYSIS FOR YEAR ENDED 4th QUARTER 2014									
% of Total / % Change	City of Palo Alto	California Statewide	S.F. Bay Area	Sacramento Valley	Central Valley	South Coast	Inland Empire	North Coast	Central Coast
General Retail	38.3 / 1.3	28.3 / 2.2	27.3 / 1.7	28.1 / 0.7	30.4 / 3.5	28.8 / 2.1	26.8 / 3.6	28.0 / 0.1	31.8 / 0.5
Food Products	19.3 / 8.0	19.7 / 5.8	21.0 / 6.6	16.6 / 4.4	15.9 / 3.7	20.6 / 5.8	16.9 / 6.3	18.5 / 3.1	30.6 / 0.8
Construction	2.9 / 58.8	9.1 / 5.9	9.1 / 4.6	10.8 / 3.7	11.4 / 6.9	7.9 / 6.9	11.0 / 5.9	12.4 / -0.1	9.2 / 4.1
Business to Business	15.5 / -8.3	17.0 / 4.8	19.7 / 6.3	13.9 / 2.1	14.2 / 4.1	17.1 / 4.8	15.6 / 3.5	9.1 / 5.5	5.5 / 3.8
Miscellaneous/Other	24.0 / -39.2	26.0 / 3.2	23.0 / 2.5	30.5 / 3.2	28.1 / 3.4	25.5 / 2.7	29.8 / 5.6	32.0 / 0.8	22.9 / 3.0
Total	100.0 / -11.8	100.0 / 3.9	100.0 / 4.0	100.0 / 2.6	100.0 / 4.0	100.0 / 3.8	100.0 / 4.9	100.0 / 1.3	100.0 / 1.6
ECONOMIC SEGMENT ANALYSIS FOR YEAR ENDED 4th QUARTER 2014									
	City of Palo Alto	State Wide	S.F. Bay Area	Sacramento Valley	Central Valley	South Coast	Inland Empire	North Coast	Central Coast
Largest Segment	Restaurants	Restaurants	Restaurants	Auto Sales - New	Department Stores	Restaurants	Service Stations	Service Stations	Restaurants
% of Total / % Change	17.2 / 9.0	13.7 / 6.9	14.7 / 7.4	12.1 / 7.1	13.6 / 1.4	14.8 / 6.7	11.7 / 0.3	13.6 / -1.0	21.9 / 4.9
2nd Largest Segment	***	Auto Sales - New	Auto Sales - New	Department Stores	Service Stations	Auto Sales - New	Department Stores	Department Stores	Misc. Retail
% of Total / % Change	*** / ***	10.6 / 8.1	10.2 / 6.7	11.3 / 0.4	10.8 / -2.7	10.8 / 8.2	11.0 / 1.5	11.2 / -0.7	9.8 / 2.6
3rd Largest Segment	Department Stores	Department Stores	Department Stores	Restaurants	Auto Sales - New	Department Stores	Restaurants	Auto Sales - New	Service Stations
% of Total / % Change	10.9 / -3.5	9.9 / 0.5	8.3 / 0.5	10.7 / 5.3	10.2 / 11.2	9.6 / 0.1	10.7 / 7.7	10.3 / 4.8	9.7 / 2.5
	*** Not specified to maintain confidentiality of tax information								

Gross Historical Sales Tax Performance by Benchmark Year and Quarter (Before Adjustments)



Net Cash Receipts for Benchmark Year 4th Quarter 2014: \$25,596,038

*Benchmark year (BMY) is the sum of the current and 3 previous quarters (2014Q4 BMY is sum of 2014 Q4, Q3, Q2, Q1)

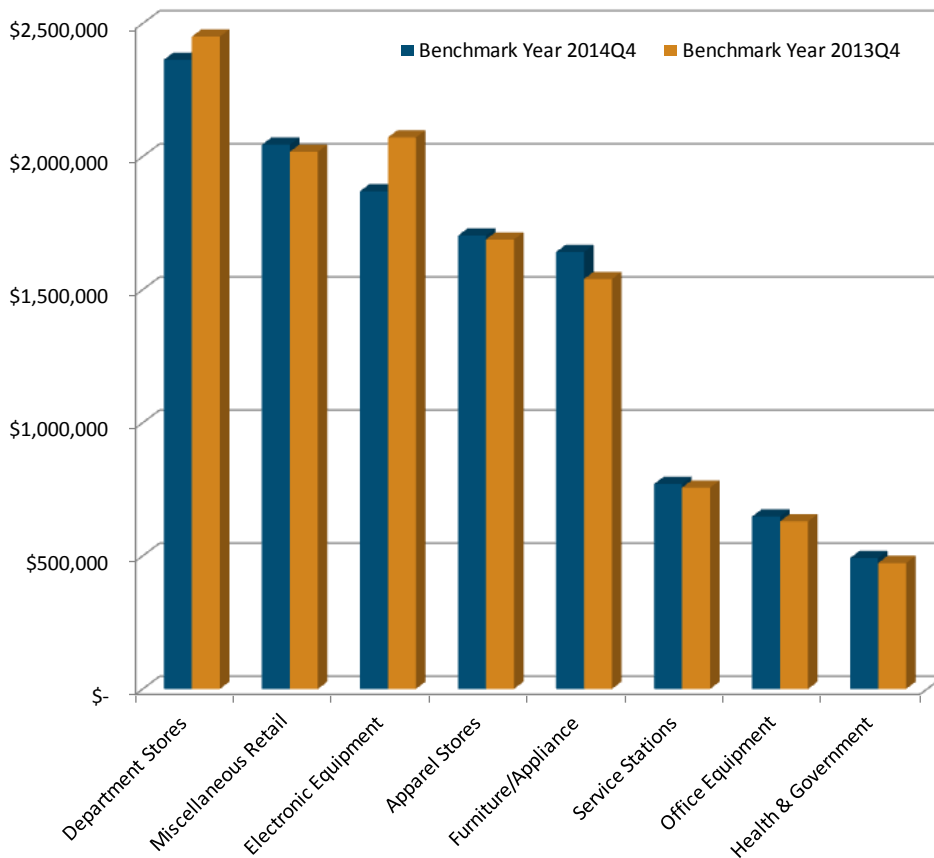


TOP 25 SALES/USE TAX CONTRIBUTORS

The following list identifies Palo Alto’s Top 25 Sales/Use Tax contributors. The list is in alphabetical order and represents the year ended 4th Quarter 2014. The Top 25 Sales/Use Tax contributors generate 49.8% of Palo Alto’s total sales and use tax revenue.

Anderson Honda	Keeble & Shucat Photography	Tesla Motors
Apple Stores	Loral Space Systems	Tiffany & Company
Audi Palo Alto	Macy's Department Store	Urban Outfitters
Bloomingtondale's	Magnussen's Toyota	Valero Service Stations
CVS/Pharmacy	Neiman Marcus Department Store	Varian Medical Systems
Eat Club	Nordstrom Department Store	Volvo Palo Alto
Fry's Electronics	Pottery Barn Kids	Wilkes Bashford
Hewlett-Packard	Shell Service Stations	
Integrated Archive Systems	Stanford University Hospital	

Sales Tax from Largest Non-confidential Economic Segments



Historical Analysis by Calendar Quarter

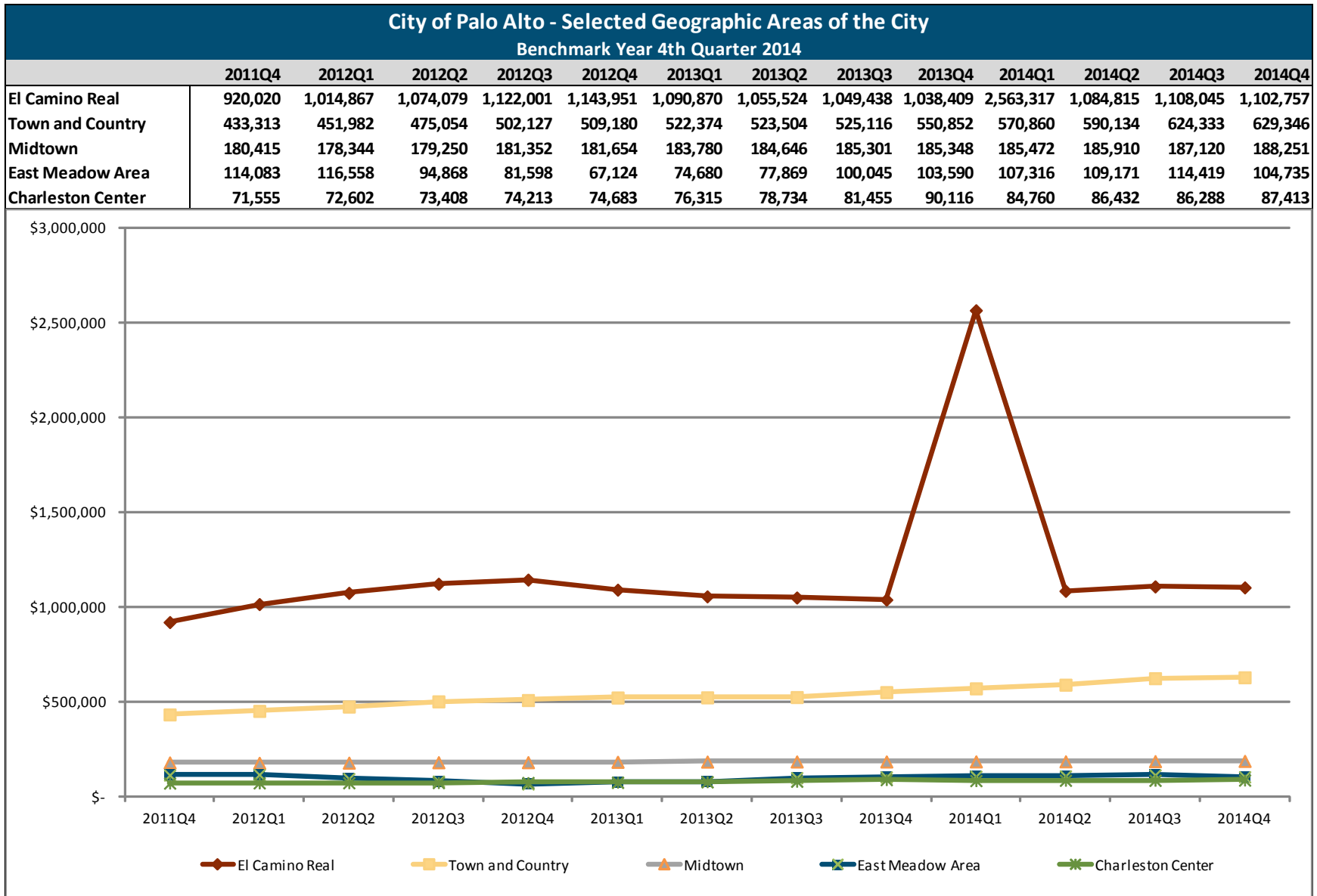
Economic Category	%	2014Q4	2014Q3	2014Q2	2014Q1	2013Q4	2013Q3	2013Q2	2013Q1	2012Q4	2012Q3	2012Q2
General Retail	35.0%	2,591,589	1,994,264	2,032,155	1,791,298	2,585,931	1,945,413	1,959,201	1,759,098	2,444,528	1,913,125	2,009,452
Miscellaneous/Other	22.3%	1,655,225	1,400,415	1,437,507	1,283,210	1,553,169	1,196,569	2,974,293	2,796,863	2,067,125	958,899	899,455
Food Products	14.8%	1,096,087	1,054,462	1,051,681	972,997	1,009,848	950,359	966,208	882,949	905,156	877,520	886,852
Business To Business	12.0%	885,327	596,226	970,762	858,119	1,268,059	848,634	800,341	592,136	1,101,068	843,770	993,147
Net Pools & Adjustments	15.9%	1,178,482	945,653	786,945	1,013,633	1,095,801	924,963	1,227,552	1,162,968	1,155,841	603,635	840,789
Total	100.0%	7,406,710	5,991,020	6,279,050	5,919,257	7,512,808	5,865,938	7,927,595	7,194,014	7,673,718	5,196,949	5,629,695

Economic Segments	%	2014Q4	2014Q3	2014Q2	2014Q1	2013Q4	2013Q3	2013Q2	2013Q1	2012Q4	2012Q3	2012Q2
Miscellaneous/Other	39.2%	2,906,134	2,211,697	2,577,014	2,328,959	3,184,808	2,230,000	3,943,660	3,584,353	3,451,258	1,967,348	2,091,371
Restaurants	13.0%	962,018	936,160	940,540	870,158	890,739	833,865	845,107	771,596	782,184	760,929	780,314
Miscellaneous Retail	8.5%	628,099	508,061	514,133	481,305	661,268	458,124	471,954	393,506	584,169	429,989	456,771
Department Stores	10.1%	750,481	548,595	591,500	472,857	762,760	574,389	603,773	509,699	779,973	584,178	608,894
Apparel Stores	6.9%	507,843	398,747	429,748	365,777	515,296	400,201	404,202	372,909	496,073	383,337	402,471
Service Stations	2.3%	166,861	203,484	215,162	184,185	177,096	214,276	196,568	187,333	182,060	198,973	198,604
Food Markets	1.6%	117,245	105,600	98,705	90,272	104,592	104,815	106,760	99,711	110,625	106,652	95,807
Business Services	1.8%	131,505	66,163	62,060	63,768	61,832	57,139	67,759	63,791	73,619	69,722	71,828
Recreation Products	0.8%	58,042	66,860	63,243	48,343	58,616	68,166	60,260	48,148	57,916	92,186	82,846
Net Pools & Adjustments	15.9%	1,178,482	945,653	786,945	1,013,633	1,095,801	924,963	1,227,552	1,162,968	1,155,841	603,635	840,789
Total	100.0%	7,406,710	5,991,020	6,279,050	5,919,257	7,512,808	5,865,938	7,927,595	7,194,014	7,673,718	5,196,949	5,629,695

*Net Pools & Adjustments reconcile economic performance to periods' net cash receipts. The historical amounts by calendar quarter: (1) include any prior period adjustments and payments in the appropriate category/segment and (2) exclude businesses no longer active in the current period.

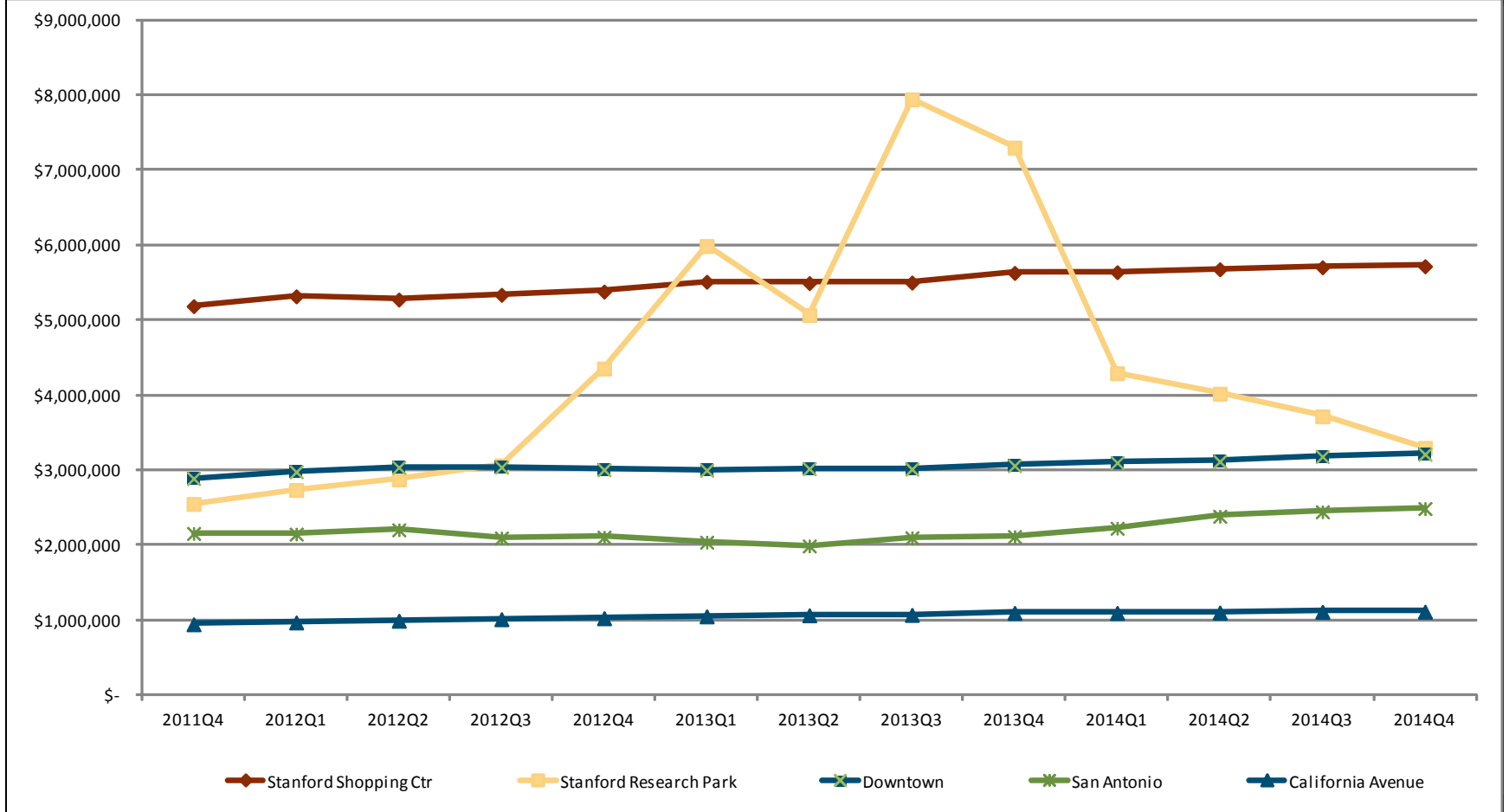
Quarterly Analysis by Economic Category, Total and Segments: Change from 2013Q4 to 2014Q4

	General Retail	Food Products	Construction	Business to Business	Misc/Other	2014/4 Total	2013/4 Total	% Chg	Largest Gain	Second Largest Gain	Largest Decline	Second Largest Decline
Campbell	1.7%	5.4%	-7.9%	48.6%	-7.6%	2,399,714	2,282,495	5.1%	Business Services	Restaurants	Service Stations	Bldg.Matls-Whsle
Cupertino	-3.8%	11.9%	523.4%	8.5%	-8.8%	8,188,983	6,733,016	21.6%	Bldg.Matls-Whsle	Business Services	Department Stores	Service Stations
Gilroy	1.0%	7.8%	12.7%	13.0%	12.7%	3,586,038	3,384,654	5.9%	Auto Sales - New	Heavy Industry	Service Stations	Energy Sales
Los Altos	-16.1%	14.7%	-19.1%	-6.2%	-16.8%	554,549	578,398	-4.1%	Food Markets	Restaurants	Miscellaneous Retail	Service Stations
Los Gatos	-6.0%	2.2%	8.0%	2.3%	-13.8%	1,853,280	1,943,972	-4.7%	Furniture/Appliance	Light Industry	Miscellaneous Retail	Auto Sales - New
Milpitas	2.2%	2.2%	77.8%	27.9%	3.5%	4,669,934	4,188,216	11.5%	Office Equipment	Bldg.Matls-Whsle	Department Stores	Light Industry
Morgan Hill	-3.7%	6.5%	-6.6%	-4.5%	-3.8%	1,728,834	1,767,661	-2.2%	Auto Sales - New	Restaurants	Service Stations	Electronic Equipment
Mountain View	-1.6%	8.9%	-10.9%	42.2%	-0.2%	4,170,047	3,825,474	9.0%	Light Industry	Restaurants	Service Stations	Apparel Stores
Palo Alto	0.7%	6.1%	45.7%	-31.5%	5.9%	6,228,227	6,398,613	-2.7%	Health & Government	Bldg.Matls-Whsle	Electronic Equipment	Miscellaneous Other
San Jose	2.3%	9.9%	10.6%	-0.5%	0.1%	39,169,454	37,980,147	3.1%	Restaurants	Office Equipment	Service Stations	Electronic Equipment
Santa Clara	5.5%	9.1%	-22.4%	-0.9%	0.8%	10,544,602	10,597,155	-0.5%	Office Equipment	Department Stores	Bldg.Matls-Whsle	Electronic Equipment
Santa Clara Co.	3.2%	4.9%	-8.2%	-32.8%	-6.3%	1,025,330	1,073,698	-4.5%	Apparel Stores	Service Stations	Light Industry	Auto Sales - Used
Saratoga	-3.1%	4.3%	-16.3%	-25.1%	-14.8%	247,016	253,899	-2.7%	Restaurants	Food Markets	Service Stations	Office Equipment
Sunnyvale	-2.6%	1.8%	-2.7%	-15.0%	-1.1%	6,711,986	7,213,277	-6.9%	Auto Sales - New	Restaurants	Office Equipment	Electronic Equipment



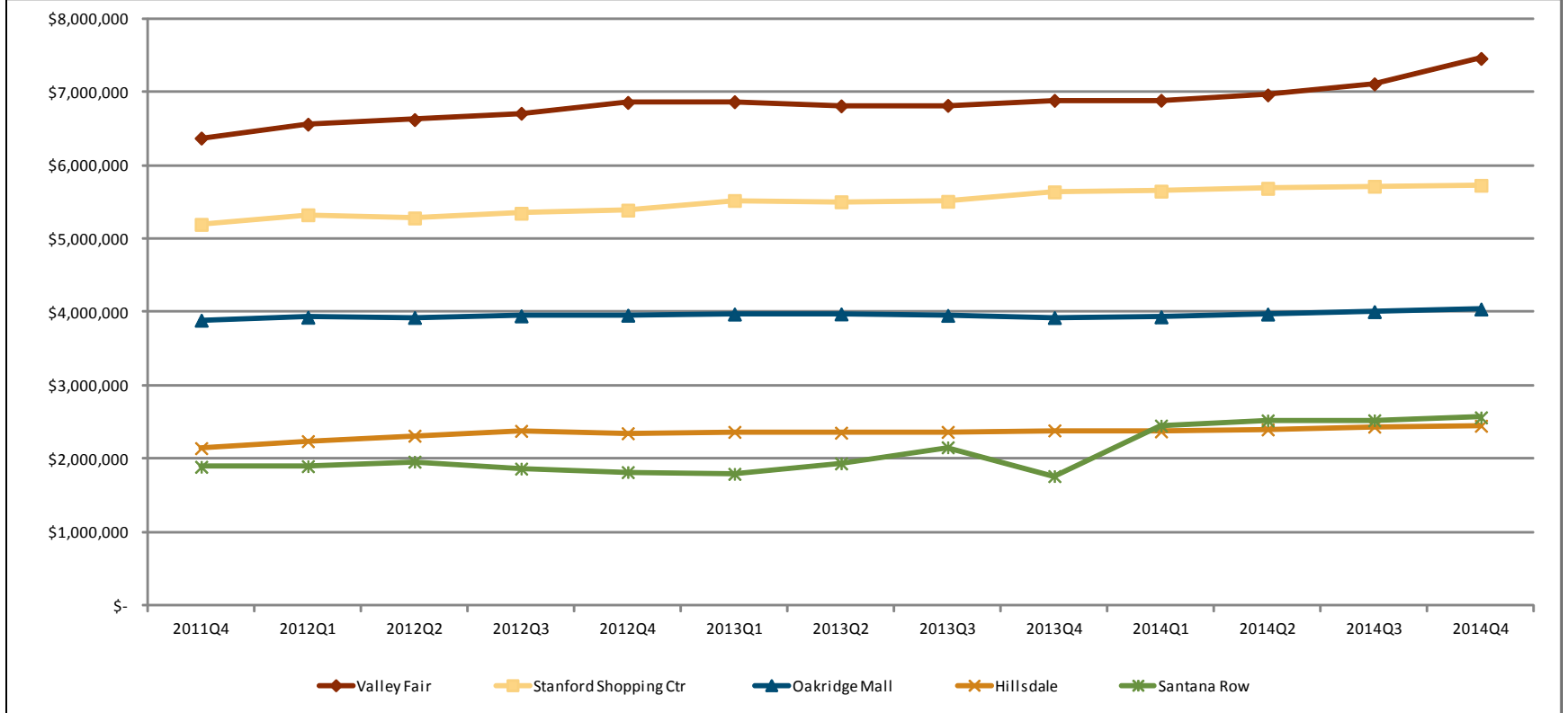
**Benchmark year (BMY) is the sum of the current and 3 previous quarters (2014Q4 BMY is sum of 2014 Q4, Q3, Q2, Q1)*

City of Palo Alto - Selected Geographic Areas of the City													
Benchmark Year 4th Quarter 2014													
	2011Q4	2012Q1	2012Q2	2012Q3	2012Q4	2013Q1	2013Q2	2013Q3	2013Q4	2014Q1	2014Q2	2014Q3	2014Q4
Stanford Shopping Ctr	5,194,491	5,325,435	5,281,772	5,345,618	5,388,747	5,519,326	5,501,836	5,508,513	5,637,256	5,647,210	5,685,894	5,713,169	5,726,273
Stanford Research Park	2,557,399	2,744,058	2,884,600	3,073,009	4,362,778	5,995,489	5,075,848	7,949,998	7,307,557	4,299,015	4,027,889	3,724,671	3,304,003
Downtown	2,897,003	2,986,093	3,044,755	3,047,356	3,013,183	3,007,123	3,027,279	3,022,194	3,068,553	3,108,592	3,124,224	3,189,273	3,220,248
San Antonio	2,164,335	2,155,721	2,212,977	2,103,881	2,114,306	2,047,925	1,997,654	2,106,291	2,122,586	2,234,235	2,393,463	2,453,548	2,495,915
California Avenue	952,300	976,897	999,421	1,020,704	1,034,151	1,058,098	1,072,925	1,078,153	1,104,341	1,104,237	1,109,685	1,119,047	1,120,996



**Benchmark year (BMY) is the sum of the current and 3 previous quarters (2014Q4 BMY is sum of 2014 Q4, Q3, Q2, Q1)*

City of Palo Alto - Regional Shopping Mall Comparison													
Benchmark Year 4th Quarter 2014													
	2011Q4	2012Q1	2012Q2	2012Q3	2012Q4	2013Q1	2013Q2	2013Q3	2013Q4	2014Q1	2014Q2	2014Q3	2014Q4
Valley Fair	6,370,656	6,559,394	6,621,598	6,708,343	6,855,987	6,865,443	6,808,919	6,815,517	6,883,838	6,885,378	6,958,214	7,108,448	7,455,179
Stanford Shopping Ctr	5,194,491	5,325,435	5,281,772	5,345,618	5,388,747	5,519,326	5,501,836	5,508,513	5,637,256	5,647,210	5,685,894	5,713,169	5,726,273
Oakridge Mall	3,888,402	3,928,855	3,925,454	3,947,751	3,957,195	3,972,739	3,974,067	3,954,094	3,924,360	3,934,469	3,972,556	4,005,370	4,040,521
Hillsdale	2,145,957	2,241,553	2,315,120	2,381,548	2,348,668	2,367,315	2,356,855	2,367,935	2,387,185	2,374,185	2,401,370	2,438,295	2,450,278
Santana Row	1,892,070	1,900,328	1,961,561	1,867,513	1,819,616	1,795,942	1,938,742	2,156,984	1,765,101	2,453,638	2,523,193	2,525,349	2,565,665



**Benchmark year (BMY) is the sum of the current and 3 previous quarters (2014Q4 BMY is sum of 2014 Q4, Q3, Q2, Q1)*

Economic Categories and Segments		
Economic Category	Economic Segment	Description
Business to Business - sales of tangible personal property from one business to another business and the buyer is the end user. Also includes use tax on certain purchases and consumables.	Business Services	Advertising, banking services, copying, printing and mailing services
	Chemical Products	Manufacturers and wholesalers of drugs, chemicals, etc.
	Electronic Equipment	Manufacturers of televisions, sound systems, sophisticated electronics, etc.
	Energy Sales	Bulk fuel sales and fuel distributors and refiners
	Heavy Industry	Heavy machinery and equipment, including heavy vehicles, and manufacturers and wholesalers of textiles and furniture and furnishings
	Leasing	Equipment leasing
	Light Industry	Includes, but is not limited to, light machinery and automobile, truck, and trailer rentals
	Office Equipment	Businesses that sell computers, and office equipment and furniture, and businesses that process motion pictures and film development
Construction	Building Materials – Retail	Building materials, hardware, and paint and wallpaper stores
	Building Materials - Wholesale	Includes, but is not limited to, sheet metal, iron works, sand and gravel, farm equipment, plumbing materials, and electrical wiring
Food Products	Food Markets	Supermarkets, grocery stores, convenience stores, bakeries, delicatessens, health food stores
	Food Processing Equipment	Processing and equipment used in mass food production and packaging
	Liquor stores	Stores that sell alcoholic beverages
	Restaurants	Restaurants, including fast food and those in hotels, and night clubs

Economic Categories and Segments		
Economic Category	Economic Segment	Description
General Retail – all consumer focused sales, typically brick and mortar stores	Apparel Stores	Men's, women's, and family clothing and shoe stores
	Department Stores	Department, general, and variety stores
	Drug Stores	Stores where medicines and miscellaneous articles are sold
	Florist/Nursery	Stores where flowers and plants are sold
	Furniture/Appliance	Stores where new and used furniture, appliances, and electronic equipment are sold
	Miscellaneous Retail	Includes, but is not limited to, stores that sell cigars, jewelry, beauty supplies, cell phones, and books; newsstands, photography studios; personal service businesses such as salons and cleaners; and vending machines
	Recreation Products	Camera, music, and sporting goods stores
Miscellaneous/Other	Miscellaneous/Other	Includes but not limited to health services, government, nonprofit organizations, non-store retailers, businesses with less than \$20,000 in annual gross sales, auctioneer sales, and mortuary services and sales
Transportation	Auto Parts/Repair	Auto parts stores, vehicle and parts manufacturing facilities, and vehicle repair shops
	Auto Sales - New	New car dealerships
	Auto Sales - Used	Used car dealerships
	Miscellaneous Vehicle Sales	Sale and manufacture of airplanes and supplies, boats, motorcycles, all-terrain vehicles, trailers and supplies
	Service stations	Gas stations, not including airport jet fuel

Economic Overview & News

April 2015 Edition



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- **RETAIL SALES/ LUXURY TRENDS & "HENRY"** (consumer preferences)
- **SERVICES SPENDING AND ESTIMATES** (a focus on "services spending" and revenue estimates)
- **RESTAURANT SALES AND NOTABLE TREND** (increase in spending and fast-casual trend)
- **GROCERY STORE NEWS** (expansion and consumer preference)
- **RETAIL NEWS** (selected closers and openings)
- **AUTO SALES** (2015 Economic Impact Report by CNCDA and tax revenues)
- **GASOLINE** (costs and trends)

STUDIES AND WORKSHOPS**California Road Usage Charge Alternatives to the Gas Tax**

SB 1077 (Chapter 835/ 2014) created the California Road Usage Charge Pilot Program and tasked the Chair of the Commission, in consultation with the California State Transportation Agency (CalSTA) to convene a fifteen member Technical Advisory Committee (TAC) to study road usage charge alternatives to the gas tax, gather public comment, and make recommendations to CalSTA regarding the design of a road usage charge pilot program. Future meetings are 5/27-28 (Fresno) and 6/24-25 (Sacramento). Refer to the CATC for details and other dates. *Source: www.catc.ca.gov*

"Sharing Economy" and the FTC

On June 9 the FTC will host a workshop to include examining economic issues of online and mobile peer-to-peer business platforms for certain sectors of the economy. Among the questions addressed include: How can state and local regulators meet legitimate regulatory goals (such as protecting consumers, and promoting public health and safety) in connection with their oversight of sharing economy platforms and business models, without also restraining competition or hindering innovation? Comments will be accepted on or before May 26, 2015, but the record will be held open to receive comments until August 4, 2015. *Source: www.ftc.gov*

Please contact your Client Services Manager for a local perspective on economic trends, or with questions or comments regarding this report.

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GLOBAL AND THE U.S. ECONOMY

Economic Indicators

Source: Bureau of Economic Analysis (March 2015)

Gross domestic purchases (purchases by U.S. residents of goods and services wherever produced) increased 3.2 percent in the fourth quarter, compared with an increase of 4.1 percent in the third.

Gross national product (the goods and services produced by the labor and property supplied by U.S. residents) increased 1.4 percent in the fourth quarter, compared with an increase of 5.3 percent in the third.

Current dollar GDP (the market value of the production of goods and services in the U.S.) increased 2.4 percent, or \$103.9 billion, in the fourth quarter to a level of \$17,703.7 billion.

Gross domestic income (measures the value of the production of goods and services in the U.S. as the costs incurred and the incomes earned in production) increased 3.1 percent in the fourth quarter, compared with an increase of 5.2 percent in the third.

CALIFORNIA'S ECONOMY

UCLA Anderson Forecast and Forecast L.A. Highlights

Source: www.caeconomy.org

Outlook: Healthy California and U.S. economic growth between 2015-2020 (Beacon Economics), or 2015-2017 (UCLA Anderson Forecast), with the U.S. economy growing 3 percent or more over the next two to three years.

Jobs: The state's falling unemployment is due to genuine improvements in labor markets rather than more workers giving up on their job search, which is a positive sign. Jobs will increase 2-3 percent over the next couple years.

Employment: California's economy created 216,000 more jobs in 2014 than previously thought because of yearly data revisions in early 2015 that painted a healthier picture. This bodes well for future growth. Workers across the state will watch their incomes rise 4.2 percent on average during the next three years.

Home building: 100,000 housing units are expected to be permitted in California during 2015, a 22 percent increase over 2014 and the highest level since the Great Recession. This will be dwarfed by 120,000 units in 2016 and 137,000 in 2017.

Housing: Even with California home prices rising much higher than other regions across the nation, a so-called asset bubble isn't here today and isn't anticipated in the near future.

Venture investment: In 2014, California hit a record level for venture capital investments. More than \$19 billion had been placed in firms, a 73 percent increase over 2013.

Taxes and regulations: California's geographic and diverse benefits will continue outweighing the costs to most corporations with respect to its strict business climate.

Skilled manufacturing: While California's business climate is not palatable for manufacturers in general, several key high-skilled manufacturing sectors are experiencing a robust uptick in activity and jobs.

Government defense spending: The negative U.S. trend from 2011-2014 will reverse between 2015-2017 and experience higher spending, a good sign for California.

Inflation: Currently low annual U.S. inflation will normalize to about 3 percent yearly by 2016 and most likely remain stable.

California's Department of Finance Economic Update (*Extrapolated*)

Source: *Department of Finance (April 2015)*

- **Job Growth:** California continues to add jobs at a faster pace than the nation. The difference between the California and U.S. unemployment rate has narrowed to its smallest since January 2008.
- **Real Estate:** Real estate markets and home building are improving at a slow and somewhat uneven pace.
- **Personal Income:** California personal income growth increased by 4.7 percent in 2014 compared with 2.8% in 2013.
- **Non-Farm Jobs:** California added 29,400 nonfarm jobs in February, following a revised 59,100 job gain in January. This is the 44th consecutive month of job gains—averaging about 37,000 new jobs per month.
- **Industry Sector Jobs:** Eight industry sectors gained jobs while three lost jobs. The largest job gain was in leisure and hospitality (12,600), followed by construction (11,200), professional and business services (9,200), manufacturing (4,200), trade, transportation, and utilities (2,800), educational and health services (2,100), financial activities (1,200), and mining and logging (200). Sectors that lost jobs were government (8,400, mostly in local government), information (5,000), and other services (700).

RETAIL SALES/ LUXURY TRENDS & "HENRY"

U.S. Consumers - Opening Their Wallets

Source: *Kiplinger and Wall Street Journal (April 2015)*

Excluding gasoline, retail sales will climb about 4.5% this year, compared with a 4% increase in 2014. Low prices at the pump will continue to keep a lid on gas station revenue, slowing total retail sales growth to about 2.5% for the year. The lower price for a gallon of gasoline, coupled with a strengthening economy, will nudge consumers to dig deeper into their pockets. Continued strong growth for restaurants and bars is about 8%. Furniture firms should see sales bump up about 4% as first-time home buyers decorate. Sales of building materials will grow by 5%, (tied to new-home sales.)

Luxury Sales Moving Online, Study Says

Source: <http://www.jckonline.com/2015/04/21/luxury-sales-moving-online-study-says>

A new report from L2, the retail researcher and think tank, suggests that the number of luxury sales that start online, through research, or end online, through e-checkout, could grow by 40 percent by 2020. Currently, just 5 percent of total luxury sales are online. But nearly 50 percent of luxury sales are "triggered or influenced" by online experiences.

The definition of luxury retail is being 'shattered'/ HENRY: "Higher-Earner Not Rich Yet"

Source: *Washington Post*

As recently as 10 years ago, the profile of a luxury shopper was fairly clear-cut: It was the kind of man or woman who owned a lavish penthouse condo, had a fat investment portfolio and freely threw down cash on pricey Chanel handbags or Louis Vuitton luggage. The experts said that many of today's millennial luxury shoppers fall into a category of customer known in industry jargon as a "HENRY" — an acronym for a person who is a "high-earner not rich yet." Because they have steady cash flow but little accumulated wealth, their spending patterns are different, according to Ken Nisch, chairman of retail design firm JGA. For example, Nisch said that over 50 percent of luxury cars in the United States are being leased, not bought. They're turning to services such as Rent the Runway and Uber that allow them to have an upscale experience at a fraction of the cost.

Duty Free Retailing Market Sales Worth \$73.6 Billion by 2019

Source: www.prnewswire.co.uk

The Global Duty Free Retailing reports key findings of airport retail and luxury trends: a) Overall, 60% of travelers spend 15 min or less per visit to a duty paid airport retail outlet; b) The majority of respondents aged more than 45 years bought magazines and newspapers from airport retail outlets in the last year (2014); c) Respondents incurred significant expenditure on precious jewelry, briefcases, men's bags, and handbags during their visits to airport retail outlets; d) 92% of travelers intend to buy Dior products at an airport departure/duty-free area over the next year (2015); and e) Competitive prices and the availability of luxury brands at discounted prices are key factors motivating travelers to purchase at airport retail stores.

SERVICES SPENDING AND ESTIMATES**Services Spending Rises At Fastest Pace Since 2000**

Source: *Wall Street Journal* (March 2015)

U.S. consumer spending rose at a 4.4% annual pace in the fourth quarter, up from an earlier estimate of 4.2% and the fastest pace since the first quarter of 2006. Spending on goods rose at a 4.8% rate versus an earlier estimate of 4.5%. Spending on services grew at a 4.3% pace, up from the earlier estimate of 4.1% and the fastest pace since the second quarter of 2000.

The Quarterly Services Survey (QSS)

Source: <http://www.census.gov/econ/overview/se0600.html>

The QSS is the only source of service industry indicator performance providing timely estimates of revenue and expenses for selected service industries. The United States Code, Title 13, authorizes this survey and provides for voluntary responses. The report a source of hard data on how much consumers are spending on services.

Estimate of Potential Revenue from the Taxation of Currently Non-Taxable Services

Source: <http://www.boe.ca.gov/legdiv/pdf/ServicesRevEstimate.pdf>

The California State Board of Equalization (BOE) released an estimate indicating that California's state and local governments may receive approximately \$122.6 billion in new revenue if tax was collected on services that are currently non-taxable. Of that amount, \$60.9 billion could go to the state, with \$61.7 billion for city, county, and other local government entities. The estimate assumes a statewide average sales tax rate of 8.42 percent.

RESTAURANT SALES AND TREND FOR FAST CASUAL

Restaurants lead U.S. March sales increase

Source: *International Council of Shopping Centers (April 14, 2015)*

Consumer confidence appeared to thaw last month, with more shoppers visiting restaurants, bars and home improvement stores. U.S. retail sales increased by 0.9 percent in March compared to the previous month and by 1.3 percent compared to March 2014, the U.S. Department of Commerce reported. That's the largest gain in a year, the agency says. Sales at food service and drinking establishments grew 7.7 percent year on year. Meanwhile building material and garden supply retailers reported a 6.3 percent increase year on year

Fast casual success attributed to speed, cost, nutrition

Source: *www.fastcasual.com (April 17, 2015)*

The fast casual sector has grown by more than 550 percent since 1999, according to the Village Voice, and Americans spent more than \$21 billion at fast casual stores in 2014.

GROCERY STORE NEWS

Several clients have raised questions on various grocery stores in the State. The following was extrapolated from noted reports for informational purposes. Please ask your Client Services Manager for specific local impact.

Safeway Acquisition is Complete

Source: *Associated Press*

The combined company (Safeway) will include 2,230 stores, 27 distribution facilities and 19 manufacturing plants with more than 250,000 employees across 34 states and the District of Columbia. It will have corporate offices in Pleasanton; Phoenix, Arizona; and Boise, Idaho. Safeway has more than 1,300 U.S. locations under names including Safeway, Vons, Pavilion's, Randall's, Tom Thumb and Carrs. Safeway will no longer list on the New York Stock Exchange.

Haggen Grocery Chain

Source: *LA Times*

Despite the retrenchment by Fresh & Easy, which is closing 30 Southland stores, the region bristles with food purveyors. Farmers' markets and ethnic shops are sprouting in the shadow of stalwarts Ralphs and Albertsons. Smaller chains, including Trader Joe's, are expanding as Wal-Mart and Target pump up their food offerings. Then there are online players Amazon.com and Google, which are pushing into grocery delivery. Haggen Inc., a small Pacific Northwest chain that will soon become a familiar sight in the region. The Bellingham, Wash., company said in December that it was buying 146 Albertsons, Vons, Pavilions and Safeway stores, including 83 in California, almost all in the south. The Federal Trade Commission ordered Albertsons and Safeway to sell those stores as part of their recent merger. Haggen plans to convert its California stores by the end of June. Its first spot opened in Carlsbad two weeks ago. Haggen stores are known for carrying a greater array of organic produce and higher-quality meats and seafood than can be found at a typical supermarket, Shaner said, but with similar prices.

RETAIL NEWS

Source: *www.plainvanillashsell.com (April 2015)*

Nordstrom, Macy's see benefits from keeping their discount stores close: The off-price/outlet route also has proved useful. In its most recent fiscal year, Nordstrom sales at its full-line stores open at least a year - an industry benchmark known as same-store sales - slipped 0.5 percent. Same-store sales at its Rack stores rose 3.8 percent over the same period. The Seattle retailer, which now has 173 Rack locations, has set a target of opening 300 by 2020.

Remodeling, expanded assortments boost **99 Cents Only** results: The company opened a record 40 new stores during the fiscal year and said it expects to open between 30 and 40 stores this year in California, Arizona and Texas.

Wok Box: Will develop 37 restaurants throughout Northern California over the next 10 years. Under the agreement, which marks Wok Box's entry into California, the 37 restaurants will be developed from Kern County up to the Oregon border, with the first slated to open in the San Francisco Bay Area in the first half of 2015.

Why **Wal-Mart** Is Betting Big On Being Your Local Urban Grocer: Wal-Mart made its name by going big: massive supercenters with gallon jars of pickles and rows and rows of lawn chairs and tires. Its future may depend a lot on going small. It's investing in smaller stores in densely populated urban neighborhoods, where customers buy fewer items at a time.

Leslie's Swimming Pool Supplies to Open 15 Stores: In total, Leslie's plans to open 41 new stores this year (many in California) between March and May.

Pier 1: After a disappointing fourth-quarter earnings report, Pier 1 Imports said Wednesday that it will close about 100 stores over the next three years.

Walgreens to close 200 stores.

CREAM, a San Francisco-based dessert franchise that specializes in high quality ice cream sandwiches and other confections, has inked a franchise deal that will bring 13 new locations to various uncharted parts of Northern California, including Fairfield, Vacaville, Marin County, Chico, Santa Cruz and Napa, among others.

Frederick's of Hollywood has closed all of its stores and will do business only online.

Dick's Sporting Goods forecasts \$9 billion in sales by 2017. Expects sales of up to \$9 billion annually by 2017 and plans to open between 135 and 150 stores in the next three years, for a total of about 735 to 750 stores nationwide.

AUTO SALES

Annual Contributions of California's New Car Dealers (extrapolated from the CNCDA's 2015 Economic Impact Report)

Source: California New Car Dealers Association

Total sales: \$105.12 billion

Average sales per dealership: \$77.42 million

Percent of total Statewide sales tax collected: 12.5%

Number of new car dealerships 1,358

Total taxes collected or paid: \$8.82 billion

Total spent for products and services from other California businesses: \$2.4 billion

New vehicles sold 1,848,254 and Used retail vehicles sold 691,189

Total new and used vehicles sold 2,539,443

GASOLINE PRICES

Gas Prices in California

Source: LA Times (April 3, 2015)

On January 30, 2015 Californians paid an average of \$2.43 for a gallon of gasoline, the lowest since May 2009, according to fuel tracking group GasBuddy.com. It shot up 93 cents in a month and has since been fluctuating around \$3.20, nearly 80 cents more than the national average. The price uptick began shortly after Tesoro Corporation idled its Martinez plant amid a nationwide walkout by union members. Oil companies said market conditions such as supply and demand guide pump prices. Before California adopted its special gasoline blend, refinery-level wholesale prices in the state averaged an inflation-adjusted 6 cents above the national average. From 1996 to 2014, they averaged 16 cents higher. Early each year, California refineries also transition from making winter blend gasoline to a cleaner-burning, pricier summer blend. The facilities also temporarily scale back production during planned maintenance. Taxes, among the highest in the country, also lift the price of the fuel. As of Jan. 1, California retail gasoline taxes accounted for 63.8 cents per gallon, 15 cents higher than the nationwide average. Toward the end of last year, when a gallon of regular gasoline cost an average of \$2.68, fees and taxes accounted for nearly a quarter of the cost, according to the California Energy Commission. Nearly half of the total cost was attributed to the cost of crude oil, 16.5 percent covered dealer and distributor costs, and 12 percent went to refiners.