



CITY OF KIRKLAND
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MEMORANDUM

To: Kurt Triplett, City Manager

From: Michael Olson, Director of Finance & Administration
 Chip Corder, Temporary 2021-2022 Budget Development Staff
 Kevin Lowe Pelstring, Budget Analyst
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Date: November 25, 2020

Subject: October 2020 Sales Tax Revenue

Background

The Financial Planning Division prepares a monthly sales tax revenue memo analyzing monthly and year-to-date activity by business sector, forecasting sales tax revenue in the current year, and tracking key economic indicators to provide additional context for the state of the economy. The general retail sales tax is the City's largest single revenue source, accounting for 18 percent of total budgeted revenues in the General Fund and funding, along with property tax and utility taxes, public safety and other general government (i.e., non-utility) services. It is also more sensitive to economic cycles than other tax revenues. Accordingly, it is monitored closely by staff—even more so given the economic disruption and uncertainty caused by COVID-19.

There is a two-month lag between when sales tax is generated and when it is distributed to the City by the Washington State Department of Revenue (DOR). Accordingly, October sales tax revenue relates to August retail activity in Kirkland.

October 2020 vs. October 2019

Business Sector Group	October		Dollar Change	Percent Change	Percent of Total	
	2019	2020			2019	2020
Services	314,014	286,424	(27,590)	-8.8%	13.8%	12.6%
Contracting	692,885	550,815	(142,070)	-20.5%	30.4%	24.2%
Communications	37,363	32,982	(4,381)	-11.7%	1.6%	1.5%
Retail:						
Auto/Gas Retail	356,379	467,794	111,415	31.3%	15.6%	20.6%
Gen Merch/Misc Retail	216,940	244,627	27,687	12.8%	9.5%	10.8%
Retail Eating/Drinking	173,216	123,617	(49,599)	-28.6%	7.6%	5.4%
Other Retail	272,745	304,366	31,621	11.6%	12.0%	13.4%
Wholesale	90,013	101,215	11,202	12.4%	4.0%	4.5%
Miscellaneous	124,074	162,110	38,036	30.7%	5.4%	7.1%
Total	2,277,629	2,273,950	(3,679)	-0.2%	100%	100%

Comparing October 2020 to October 2019, **sales tax revenue is down \$3,679, or 0.2 percent.**

Looking at business sectors, the most significant growth occurred in Auto/Gas retail (up \$111,415, or 31.3 percent), Miscellaneous (up \$38,036 or 30.7 percent), Other Retail (up \$31,621, or 11.6 percent), and General Merchandise/Miscellaneous Retail (up \$27,687, or 12.8 percent).

Noteworthy declines occurred in Contracting (down \$142,070, or 20.5 percent), Retail Eating/Drinking (down \$49,599, or 28.6 percent), and Services (down \$27,590, or 8.8 percent).

YTD 2020 vs. YTD 2019

Business Sector Group	YTD		Dollar Change	Percent Change	Percent of Total	
	2019	2020			2019	2020
Services	2,842,040	2,928,434	86,394	3.0%	12.9%	13.8%
Contracting	5,462,411	5,445,988	(16,423)	-0.3%	24.8%	25.8%
Communications	623,829	393,458	(230,371)	-36.9%	2.8%	1.9%
Retail:						
Auto/Gas Retail	4,272,161	3,820,289	(451,871)	-10.6%	19.4%	18.1%
Gen Merch/Misc Retail	2,252,479	2,404,551	152,072	6.8%	10.2%	11.4%
Retail Eating/Drinking	1,548,762	1,226,359	(322,403)	-20.8%	7.0%	5.8%
Other Retail	2,589,090	2,803,986	214,896	8.3%	11.8%	13.3%
Wholesale	954,285	959,686	5,401	0.6%	4.3%	4.5%
Miscellaneous	1,489,381	1,163,431	(325,950)	-21.9%	6.8%	5.5%
Total	22,034,438	21,146,183	(888,255)	-4.0%	100%	100%

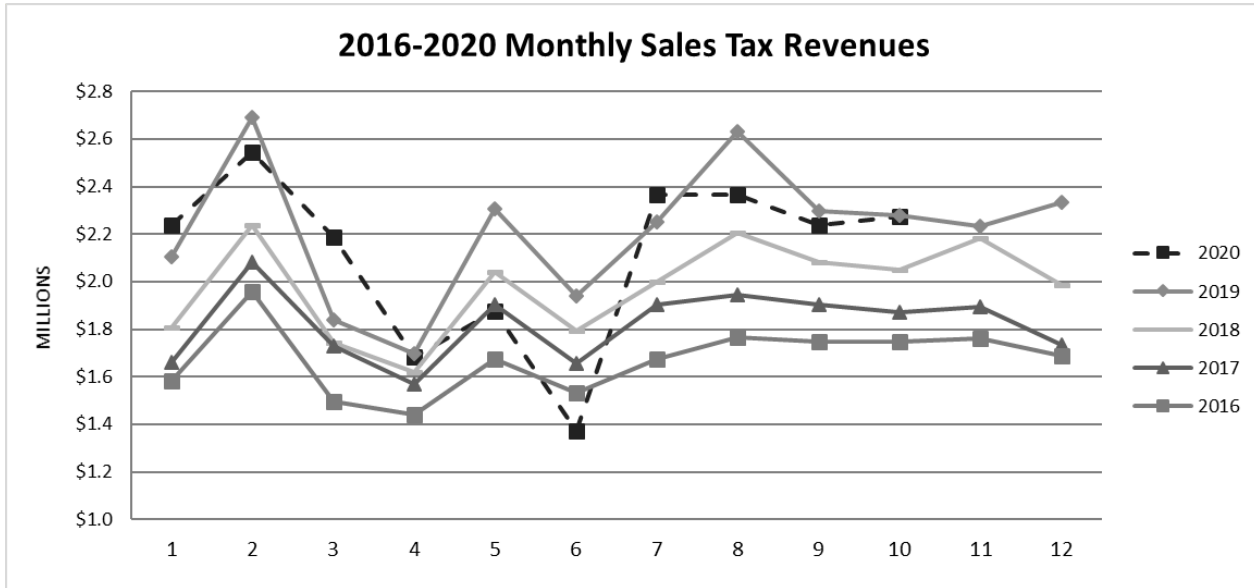
Comparing 2020 to 2019, year-to-date (YTD) sales tax revenue is **down \$888,255, or 4.0 percent**. However, 2019 includes two large back tax payments totaling \$458,733 from the Communications and Miscellaneous business sectors. **Factoring out these one-time payments**, YTD sales tax revenue is **down 2.0 percent** relative to the same period in 2019.

Looking at business sectors, the most significant growth occurred in Other Retail (up \$214,896, or 8.3 percent) and General Merchandise/Miscellaneous Retail (up \$152,072, or 6.8 percent). The growth in Other Retail has been led by the Electronics, Health & Personal Care, Building & Garden, and Sporting Goods sub-sectors.

Noteworthy declines occurred in Auto/Gas Retail (down \$451,871, or 10.6 percent), Miscellaneous (down \$325,950, or 21.9 percent), Retail Eating/Drinking (down \$322,403, or 20.8 percent), and Communications (down \$230,371, or 36.9 percent). The significant decreases in Miscellaneous and Communications respectively relate to back tax payments of \$248,522, which was received in February 2019, and \$210,211, which was received in July 2019. Retail Eating/Drinking is down due to the Governor's stay-at-home order, which was in effect from March 25th to May 31st, and social distancing requirements, which limit the number of customers that can be served.

In response to the recent rapid spread of the COVID-19 virus in Washington state and across the country, the Governor announced a four-week statewide set of restrictions, which will negatively impact many businesses, including restaurants and bars, through December 14th. Because of the two-month lag noted above, the sales tax impact of these restrictions will not be felt until January 2021.

The chart below shows Kirkland’s monthly sales tax revenue through October 2020 compared to the prior four years.



2020 Sales Tax Forecast Scenarios

Given the continuing high level of economic uncertainty through the balance of the year, two forecast scenarios are provided in the following table for 2020 sales tax revenue. Note that the 2020 budget of \$23,130,166 reflects the City’s modified two-year sales tax lag policy (2020 budget = 2018 estimate).

Forecast Scenario	2020 Forecast	2020 Budget	Surplus (Deficit)	Staff Forecast Assessment
2020 forecast is 4% below 2019 actual*	\$25,528,064	\$23,130,166	\$2,397,898	Likely
2020 forecast is 6% below 2019 actual*	\$24,996,229	\$23,130,166	\$1,866,063	Pessimistic

*2019 actual sales tax revenue = \$26,591,733.

As previously noted, sales tax revenue through October 2020 is down 4.0 percent relative to the same period in 2019. This is significantly better than the following two September 2020 forecasts of annual taxable retail sales growth in King County in 2020:

- King County Office of Economic and Financial Analysis: **11.6 percent decline** in 2020
- Puget Sound Economic Forecaster: **8.7 percent decline** in 2020

The key **“takeaway”** from these two forecast scenarios is that **2020 budgeted sales tax revenue is 13 percent below 2019 actual sales tax revenue**. That provides a significant “buffer” in 2020, reducing the financial impact of these two scenarios accordingly.

To help frame staff’s assessment of these two forecast scenarios, the following two tables identify how much sales tax revenue would have to decline in the last two months of 2020 relative to the last two months of 2019 to end the year 4 percent and 6 percent below 2019 actual sales tax revenue.

2020 Forecast is 4% below 2019 Actual (Staff Forecast Assessment: Likely)

Sales Tax Revenue	2019	2020	\$ Change	% Change
January-October (actual)	\$22,034,438	\$21,146,183	(\$888,255)	-4.0%
November-December (2019 actual & 2020 forecast)	\$4,557,295	\$4,381,881	(\$175,414)	-3.8%
Total	\$26,591,733	\$25,528,064	(\$1,063,669)	-4.0%

2020 Forecast is 6% below 2019 Actual (Staff Forecast Assessment: Pessimistic)

Sales Tax Revenue	2019	2020	\$ Change	% Change
January-October (actual)	\$22,034,438	\$21,146,183	(\$888,255)	-4.0%
November-December (2019 actual & 2020 forecast)	\$4,557,295	\$3,850,046	(\$707,249)	-15.5%
Total	\$26,591,733	\$24,996,229	(\$1,595,504)	-6.0%

Sales tax revenue would have to decline 3.8 percent and 15.5 percent respectively in November-December 2020 to end the year 4.0 percent and 6.0 percent below 2019 actual sales tax revenue. The latter reduction scenario is very unlikely due to the two-month sales tax lag.

Key Economic Indicators

Information about wider trends in the economy provides a mechanism to help understand current results in Kirkland and to predict future performance. The combination of consumer confidence, unemployment levels, housing data, inflation, and auto sales provides a broader economic context for key factors in sales tax revenues. Since the sales tax figures reported above are from two months prior, some of the figures in the table below can function as leading indicators for where sales taxes may go in future reports.

Indicator	Most Recent Month of Data	Unit	Month			Yearly Average	
			Previous	Current	Change	2019	2020
Consumer Confidence							
Consumer Confidence Index	October	Index	101.3	100.9	(0.4)	128.1	103.2
Unemployment Rate							
National	October	%	7.9	6.9	(1.0)	3.7	8.4
Washington State	September	%	8.4	8.3	(0.1)	4.5	9.1
King County	September	%	7.2	7.0	(0.2)	3.0	8.0
Kirkland	September	%	5.7	5.5	(0.2)	2.9	6.7
Housing							
New House Permits (WA)	September	Thousands	39.2	50.9	11.7	48.7	44.6
Case-Shiller Seattle Area Home Prices	August	Index	273.9	277.0	3.1	252.2	268.3
Inflation (CPI-W)							
National	October	% Change	1.5	1.3	(0.2)	1.7	1.2
Seattle	October	% Change	2.4	2.1	(0.3)	2.1	1.9
Car Sales							
New Vehicle Registrations	October	Thousands	21.7	23.3	1.6	23.7	19.0

The **Consumer Confidence Index** slightly decreased from 101.3 in September to 100.9 in October. The 2020 average is 24.9 points below the 2019 average.

The national **Unemployment Rate** dropped from 7.9 percent in September to 6.9 percent in October while the Washington State unemployment rate decreased slightly from 8.4 percent in August to 8.3 percent in September, after hitting a high of 16.1 percent in April. King County's unemployment rate dropped from 7.2 percent in August to 7.0 percent in September, and Kirkland's unemployment rate fell from 5.7 percent in August to 5.5 percent in September.

New Housing Permits in Washington State have increased significantly from 39,200 in August to 50,900 in September, but the 2020 average sits 4,100 below the 2019 average. The **Case-Shiller Home Price Index** saw an increase of 3.1 points in August, and the 2020 average is 16.1 points above the 2019 average, reflecting a strong housing market despite the pandemic.

Inflation, as measured by the CPI-W, in the U.S. decreased slightly from 1.5 percent in September to 1.3 percent in October, after going negative in May. For the Seattle-Tacoma-Bellevue region, the CPI-W decreased from 2.4 percent in September to 2.1 percent in October.

New Vehicle Registrations increased by 1,600 from September to October, but the 2020 average is 4,700 below the 2019 average.