

CITY OF RIVERSIDE FISCAL UPDATE



EXECUTIVE SUMMARY

The conclusion of Fiscal Year (FY) 2022/23 resulted in a favorable outcome for the General Fund, generating a one-time budget surplus. This success was primarily driven by a surge in sales tax revenue, attributed to inflationary factors, and personnel savings arising from a persistently high vacancy rate amid ongoing challenges in recruitment, retention, and hiring to fill vacant positions. The surplus reserves in the General Fund for FY 2022/23 will enable the City to implement long-term fiscal strategies. These strategies include increasing funding in the Section 115 Pension Trust to ensure the funding of pension-related costs, freeing up limited General Fund resources to sustain critical programs and services, and bolstering Infrastructure reserves to address ongoing maintenance and the replacement of capital assets. Such a strategy contributes to the long-term financial health of the General Fund.

Despite a two-year shift in sales-tax revenues prompted by the pandemic and changes in consumer spending, establishing a new, higher baseline for the City's General Fund revenues, FY 2023/24 presents challenges. These challenges include the \$8.57 million set-aside of the Water General Fund Transfer (GFT) revenues, the fiscal impact of recent labor negotiations, and the impact of the Federal Reserve's actions on the economy's trajectory. The economy strongly influences the General Fund's revenue performance and its financial health. While concerns about a recession have diminished, an expected economic slowdown could lead to the cost of doing business outpacing revenue growth, potentially reducing or eliminating the originally anticipated adopted budget surplus.

Key economic indicators affecting the local economy in and around the City encompass inflation, unemployment, income, and the housing market. A comprehensive review of these indicators, coupled with the Federal Reserve's recent decision in December 2023 to cease rate hikes and predict three rate cuts in 2024, has prompted the City to anticipate that overall revenue performance will align with budgeted expectations.

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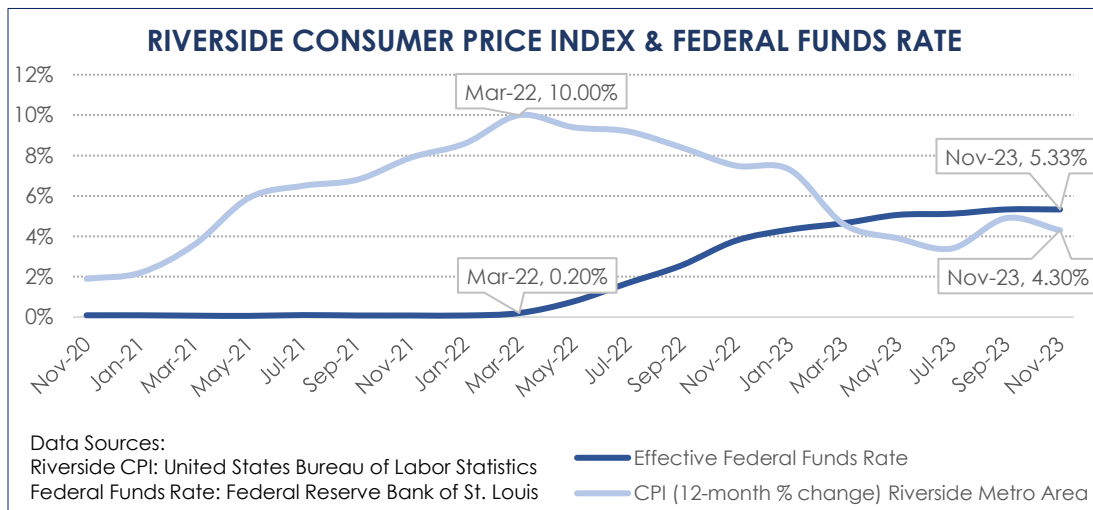
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KEY ECONOMIC INDICATORS

INFLATION

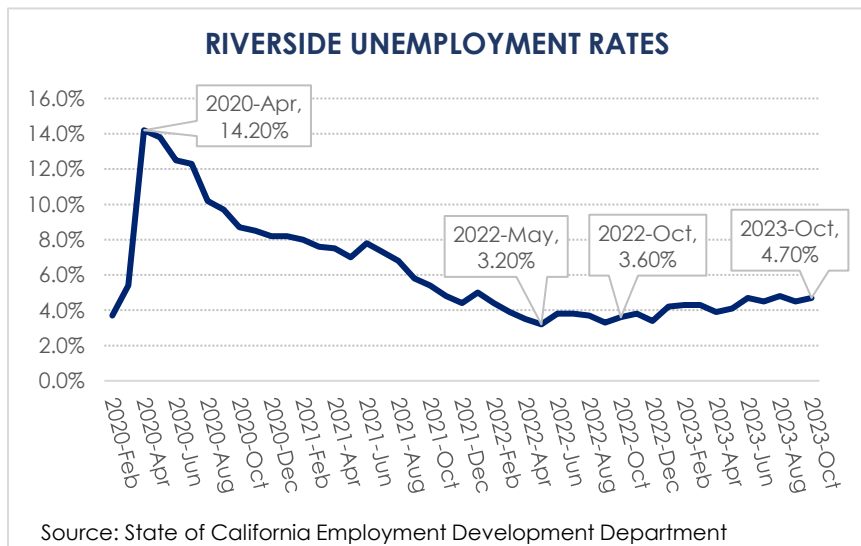
Over the past year, the Federal Reserve (Fed) has diligently pursued its goal of stabilizing prices for Americans. To counter the most painful inflation Americans had experienced since 1981, the Fed raised its benchmark short-term interest rate, the federal funds rate, aiming to achieve a target inflation of 2%. Increases in this crucial rate influences various interest rates, impacting borrowing costs for consumers and businesses and, consequently, economic slowdown through its adverse effects on unemployment and production. In the chart below, the 12-month percent change in the Consumer Price Index (CPI) is plotted against the Federal Funds Rate, demonstrating the Fed's actions on inflation. In March 2022, the Fed initiated rate hikes to address soaring inflation, peaking at an alarming 10.0% in the Riverside Metropolitan area. Persistent inflation, attributed to supply chain issues, a shift in consumer spending, and a tight labor market, led to 11 interest rate increases by the Fed, with the last hike in July 2023, bringing the federal funds rate to a target range of 5.25% to 5.5%—the highest in over two decades. As a result of Fed's interest rate hikes, the average 30-year U.S. mortgage rate, according to Freddie Mac, climbed from a low of 3.76% in March 2022 to 7.79% in October 2023, dampening housing market activity by reducing affordability. According to data from the Federal Reserve Economic Data (FRED), the prime rate, which influences rates on car loans, credit cards, home equity loans, and lines of credit, increased from 3.25% in March 2022 to 8.5% in July 2023, curbing consumer demand for goods and services.



As of November 2023, inflation has eased to 4.30%, and the Fed's aggressive rate hikes appear to be successfully addressing inflation without the predicted surge in unemployment and a deep recession. During the December 14, 2023, Federal Open Market Committee (FOMC) meeting, the central bank indicated that, following its prolonged tightening campaign against decades-high inflation, U.S. economic growth has slowed, job growth has moderated, and "inflation has eased over the past year but remains elevated. The Fed projected three rate cuts in

2024, and while some consumer prices are decreasing, overall price levels are not. Despite rising real wages outpacing inflation, Fed Chair Jerome Powell acknowledged that people are still feeling the effects of inflation.

LABOR MARKETS



The table to the left displays the unemployment rates for the City of Riverside from before the pandemic to October 2023. As demonstrated in the table, unemployment in the City reached a double-digit high of 14.2% in April 2020, due to the pandemic shutdowns. Since the pandemic recovery, labor markets have remained tight with reports of easing. As of October 2023, the state's unemployment rate reached 4.8%, surpassing the national rate of 3.6%. Concurrently, the City's unemployment rate rose to 4.7% in October 2023 from 3.6% in the same month last year, after reaching a post-pandemic low of 3.2% in May 2022.

According to the state's Employment Development Department (EDD), the number of employed people in the City declined by 1,600 from October 2022, with 200 people entering the labor force. Higher unemployment rates may carry economic implications, as individuals

facing financial constraints tend to cut back on non-essential purchases, potentially leading to a decline in sales for local businesses.

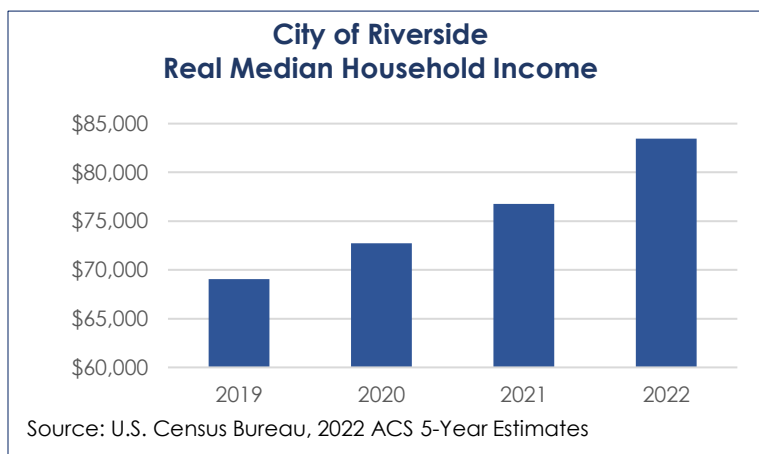
The graphic to the right illustrates employment changes for industries in the Riverside-San Bernardino-Ontario Metropolitan Statistical Area (Riverside Metro), focusing on jobs by "place of work." It excludes the self-employed, unpaid family workers, and private household employees but includes jobs within the Riverside Metro area, irrespective of workers' residence. Analyzing these employment changes across industries is vital for assessing the Riverside Metro area's economic health and growth potential. Despite higher unemployment in the region, total nonfarm employment increased by 23,100, or 1.4%, during the period. The robust growth in private education and health services (13,600 jobs) reflects an expanding healthcare and social assistance industry, meeting increased demand. Public sector expansion of 9,900 was driven by growth in employment within local city government jobs and public education, enhancing the quality of life for residents. The construction sector's addition of 7,500 jobs signifies ongoing development and infrastructure projects within the region. However, the decline in manufacturing, notably in durable goods, suggests a potential slowdown in consumption of automobiles, appliances, and machinery. Similarly, the 7,200 decline in the trade, transportation, and utilities sector, indicates possible economic challenges.

Riverside metro area employment (number in thousands)	Oct. 2023	Change from Oct. 2022 to Oct. 2023	
		Number	Percent
Total nonfarm	1,703.9	23.1	1.4
Mining and logging	1.6	0.0	0.0
Construction	126.2	7.5	6.3
Manufacturing	97.7	-2.3	-2.3
Trade, transportation, and utilities	461.0	-7.2	-1.5
Information	9.8	-0.4	-3.9
Financial activities	45.9	-1.5	-3.2
Professional and business services	184.5	3.3	1.8
Education and health services	284.3	13.6	5.0
Leisure and hospitality	179.2	-0.4	-0.2
Other services	49.4	0.6	1.2
Government	264.3	9.9	3.9

Source: U.S. BLS, Current Employment Statistics.

Despite the recent uptick in unemployment, both the state and the city continue to maintain relatively low unemployment rates. While certain industries in the Riverside Metro area show signs of declining employment, overall job opportunities are significantly up in key sectors. Similar to the nation, the City's robust labor market contributed to rising inflation within the City. Although the rate increases have been painful for businesses and consumers, especially homebuyers, the strong labor market enabled the Fed to raise rates to cool the economy and tighten labor markets, without the anticipated economic collapse. With inflation easing and the Fed signaling potential interest rate cuts in 2024, relief is anticipated for consumers and businesses, promising positive future impacts on the City's economy. However, the Fed remains cautious, opting to assess the sustained direction of inflation before committing to the timing of any interest rate decreases.

MEDIAN HOUSEHOLD INCOME



The table to the right displays the City of Riverside's inflation-adjusted median household income based on the U.S. Census Bureau's 2022 American Community Survey 5-Year Estimates data. From 2019 to 2022, the median household income rose by 20.9%, indicating a thriving local economy and a robust job market with growing wages as employers competed for skilled and educated workers. In 2022, the median household income rose to \$83,448, an increase of 8.7%, from \$76,755 in 2021. The significant increase in the City's median household income indicates improved financial well-being and purchasing power for a substantial portion of its citizens, fostering strong consumer spending. As evidenced in the post-pandemic period, the City has experienced strong economic growth. Additionally, rising real income amid an inflationary economy provides consumers with increased purchasing power, allowing them to maintain their

standard of living and meet essential needs. This financial resilience can mitigate the impact of rising prices on household budgets and contribute to economic stability.

Furthermore, the boost in median household income can enhance the City's competitiveness and local economy, potentially luring new businesses to establish themselves in the City, as demonstrated by the City's recent economic growth. Moreover, the increased purchasing power of residents with higher median incomes may spur new construction and housing development projects, meeting the growing demand for diverse housing options. In light of the Federal Reserve's efforts to combat inflation, the increase in median household income also serves as a stabilizing force, offsetting impacts from rising borrowing costs and associated economic impacts.

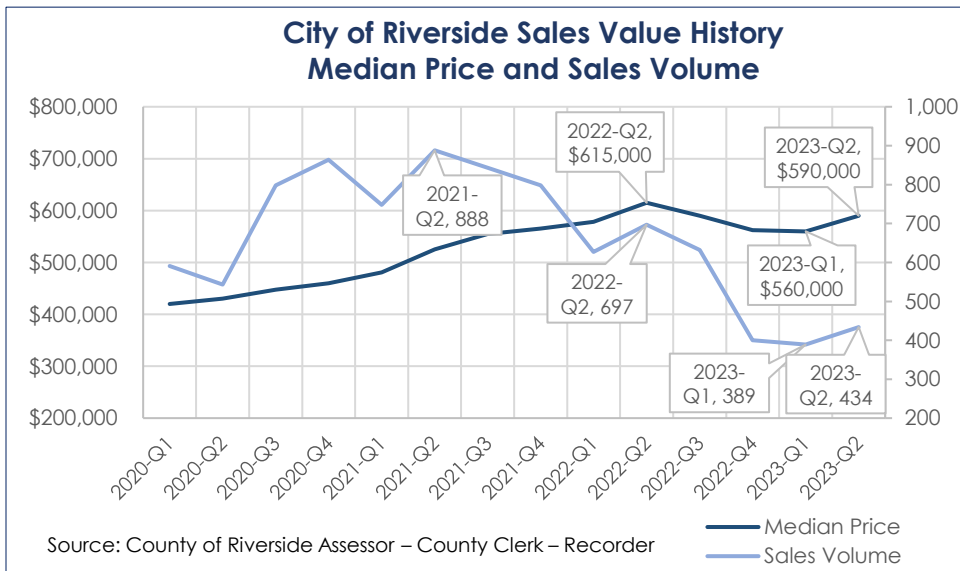
HOUSING MARKET

"Continued strong demand for real estate and a resilient economy, overcoming interest rate hikes, led to a 9% increase in assessment valuation in Riverside County going into 2023," was reported by the County of Riverside Assessor – County Clerk – Recorder in July 2023. The City witnessed an overall \$3.12 billion, or 8.2%, increase in assessed property values for 2022, which will be reflected in FY 2023/24 tax rolls. The growth in FY 2023/24 is approximately \$123 million higher than last year and is attributed to increases in property values across residential, industrial, and agricultural sectors due to property sales, construction, and development. Higher mortgage rates should send housing prices lower. According to Beacon Economics, "rapidly rising interest rates have further exacerbated California's housing shortage, as existing homeowners locked into historically low 2% to 3% mortgage rates are either unwilling or financially unable to sell." This mortgage rate lock-in effect, coupled with increased mortgage costs pricing many potential homebuyers out of the market, will continue to depress home sales volume. As indicated in the chart below, the U.S. average 30-year fixed rate mortgage increased dramatically to a high 7.79% in October of 2023. As of December 2023, mortgage rates have slightly retreated due to the Fed announcing the end of its rate hikes and the taming of inflation.

Illustrated in the Sales Value History chart below for the City of Riverside, home sales for detached single-family residential homes have witnessed a decline since reaching a peak in the spring of 2021. As of the second quarter of 2023, sales have decreased by 37.7% from the same quarter in 2022 but have seen a 5.4% decline from the first quarter of 2023. Riverside's median home price of \$590,000 decreased by 4.1% year-over-year, but it is up by 5.4% from the previous quarter. The City's experience in home sales activity mirrors the state's situation. Due to the shortage of homes on the market resulting from the rate lock-in effect, the depreciation of home prices has been limited.

The Beacon Outlook California Fall 2023

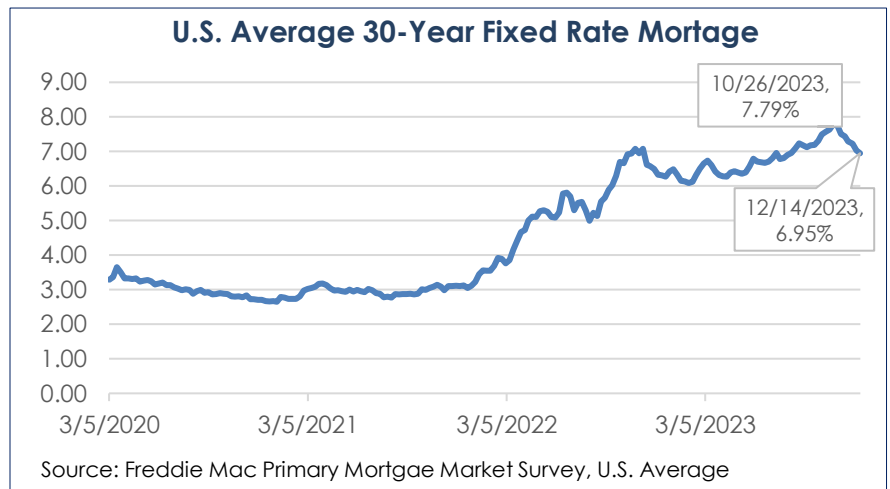
Despite the decline in home sales activity, there is less than 2 months of housing supply available in California. In other words, if no new units were added to the housing market, based on current sales activity thus far in 2023, the number of single-family homes for sale would be exhausted in about 7 weeks. A healthy housing market is typically considered to be one that has six months of supply. The long-term problem is, of course, that California does not build enough housing.



Moreover, as a result of the City's affordable housing costs in comparison to the rest of Southern California, its expanding economy, well-rounded community, and central location, the City is drawing in consumers with high household incomes and strong balance sheets. This has resulted in a robust demand for housing relative to the available housing supply.

After the pandemic surge in home sales prices, a major correction in the housing market was anticipated by many economists. As of the second quarter of 2023, home sales are still approximately 51.1% from the peak in the second quarter of 2021. However, home sales prices in the City have been relatively flat since peaking in the second quarter of 2022, due to the shortage of homes and relatively strong demand.

Beacon Economics does not foresee a housing collapse in California but rather a housing correction. The recent growth in California home prices indicates that the housing correction may have already run its course. Additionally, according to Beacon Economics, with the current pace of recent growth, California is expected to surpass its pandemic peak in the first quarter of 2024. The City's housing market mirrors the California market and should continue to see future growth in assessed property values, especially considering the Fed's recent announcement to halt rate hikes and forecasting rate cuts in 2024.

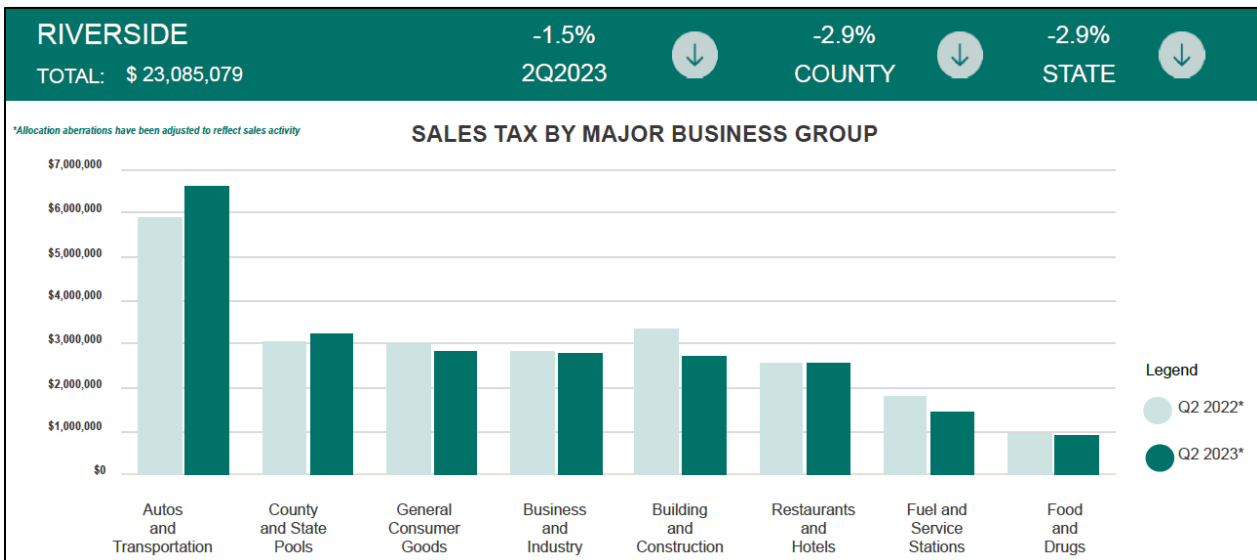


GENERAL FUND REVENUE

As of the first quarter ending September 30, 2023, first quarter analysis of the General Fund revenues indicates that, while individual revenue streams may vary – with some meeting budgetary expectations and others falling below or exceeding the budget – the overall revenue performance aligns with budgeted expectations.

During the first quarter of FY 2023/24, the City Council approved a budget adjustment for a \$900,000 draw from General Fund insurance reimbursement reserves to cover costs of construction for the temporary parking lot at 3460 Orange Street. The following outlines trends for the performance of key revenue streams:

- Property Taxes** – Over the past decade, the City of Riverside has experienced substantial growth in assessed property values. This growth has translated into significant increases in the City’s property tax revenues, which constitute approximately 25% of General Fund revenues. According to the County of Riverside Assessor – County Clerk – Recorder, the City witnessed an 8.2% increase in assessed property values for FY 2023/24. This growth is attributed to increases in property values across residential, industrial, and agricultural sectors due to property sales, construction, and development. Consequently, the City’s property tax consultant, HdL, projects current real and secured property taxes will be 3.15% higher than budgeted, for projected growth of 7.1% over the prior year actuals.
- Sales and Use Tax** – The first-quarter analysis indicates that the economy is now experiencing the repercussions of the Federal Reserve’s efforts to combat inflation through interest rate hikes, affecting both households and businesses. As outlined in the table below, as of the second quarter of 2023, sales taxes have decreased by 1.5% for the City and 2.9% for Riverside County and the state. This decline reflects households navigating tighter budgets and businesses contending with challenges such as elevated labor costs, inventory issues, and heightened competition. The City’s sales tax consultant, HdL, foresees sales tax continuing its recent trend of moderate declines throughout the remainder of 2023, stabilizing by early 2024. Due to the cooling of the labor market and high costs of credit, the upcoming holiday shopping period may be lackluster. Additionally, if inflation begins to tick up again, this could delay the Fed’s timing of rate cuts. In response to these factors, HdL has revised sales tax revenue projections, reflecting a 4.93% reduction compared to the budget, and a projected decrease of 4.3% from the previous year actuals.



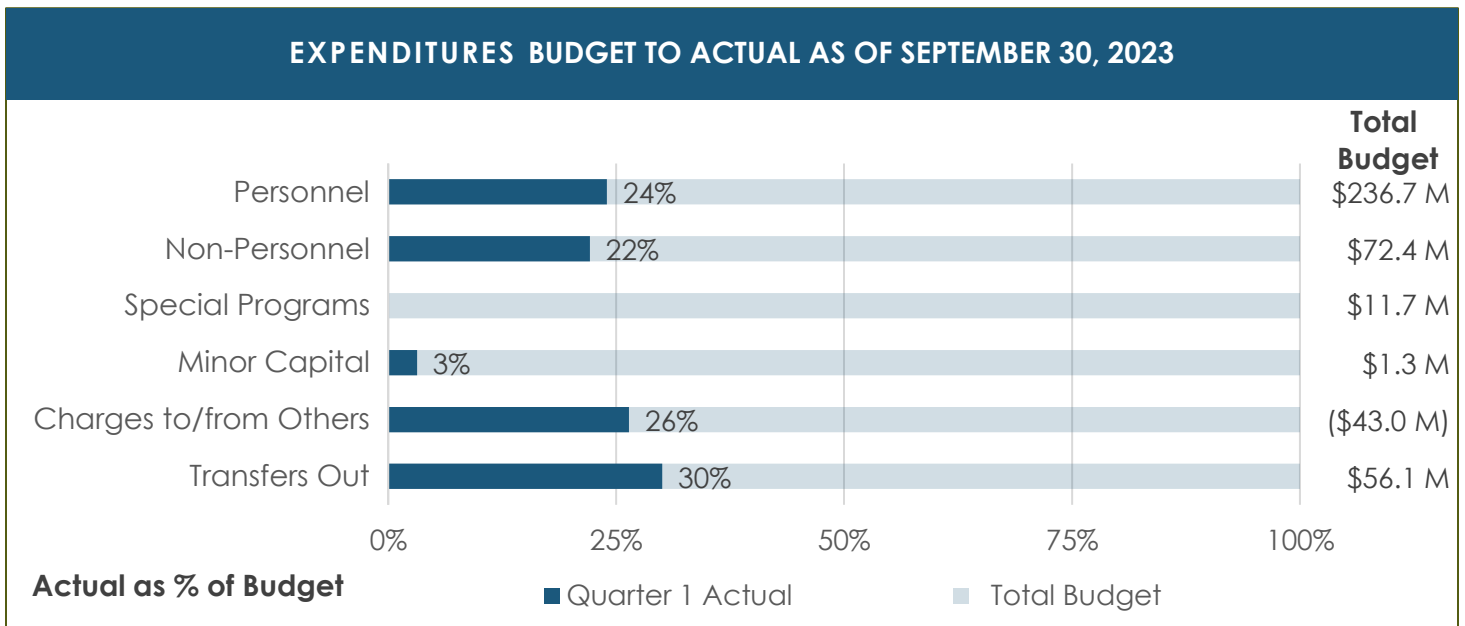
- Franchise Fees** – At the conclusion of FY 2022/23, franchise tax revenues reached \$6.42 million, marking a notable 7.8% increase compared to the previous fiscal year. This significant increase is attributed to the Year 2 increase in solid waste rates, impacting franchise fees for waste haulers. Additionally, escalating energy costs increased franchise fee collections from SoCal Gas and Edison. Although the FY 2023/24 budget designates \$5.84 million for franchise tax revenues, it is anticipated that the current year’s franchise tax revenues will meet or surpass the FY 2022/23 figure, potentially representing at least a 10% increase over the current budgeted amount.

GENERAL FUND EXPENDITURES

As of the first quarter, overall expenditures are trending lower as compared to the first quarter of the prior fiscal year. It's important to note, however, that expenditures in certain categories cannot be directly compared in a quarter-over-quarter analysis between fiscal years. For example, professional service expenditures in the non-personnel category may vary due to services being contracted on an 'as-needed' basis or timing of project implementations.

The personnel expenditures budget includes a 5% attrition rate (equal to about \$12 million) within a non-departmental fund account, which freed up funds for allocation to City priorities during amendment of the originally adopted budget. However, all positions are fully budgeted within their respective departments, indicating the City's commitment to filling these positions. In FY 2023/24, 41.75 full-time equivalent (FTE) positions were added compared to the total FTE positions in FY 2022/23, resulting in an increase in the vacancy rate from 11.5% at the end of FY 2022/23 to 13.5% at the beginning of the new fiscal year. At the close of the first quarter, the General Fund maintained a high vacancy rate of 12.5%, which decreased to 11.7% by December 2023. If the current trend of filling positions continues throughout the fiscal year, the projected vacancy rate at year-end is estimated to be 9.6%, resulting in an average annual projected vacancy rate of 11.5%. This would yield personnel savings at fiscal year-end exceeding the programmed 5% attrition rate, creating budgetary flexibility that will help mitigate the current fiscal challenges faced by the General Fund; however, the goal remains to fill all budgeted positions.

The chart below displays FY 2023/24 year-to-date actual expenditures against the total adjusted budget, as of September 30, 2023. The total adjusted budget includes prior fiscal year encumbrances and carryovers posted in the first quarter.

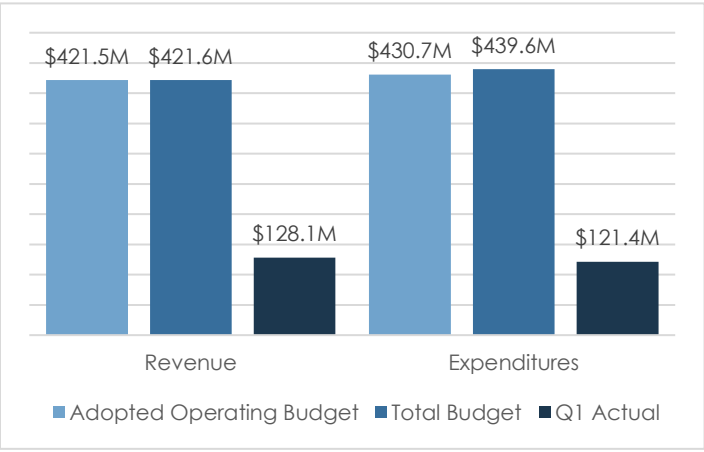


GENERAL FUND SUMMARY: Despite a two-year shift in sales-tax revenues caused by the pandemic and changes in consumer spending, establishing a new, higher baseline for the City's General Fund revenues, the City faces ongoing fiscal challenges, notably the \$8.57 million loss from the Water General Fund transfer. If overall revenue performance aligns with budgeted expectations, projected FY 2023/24 personnel savings are anticipated to mitigate the impacts of the Water General Fund transfer loss and tackle challenges arising from current labor contract negotiations. City staff will actively monitor economic impacts on the City's revenues and present updated projections in the second-quarter report to the Council, along with any recommended adjustments to address budgetary issues.

ENTERPRISE FUNDS

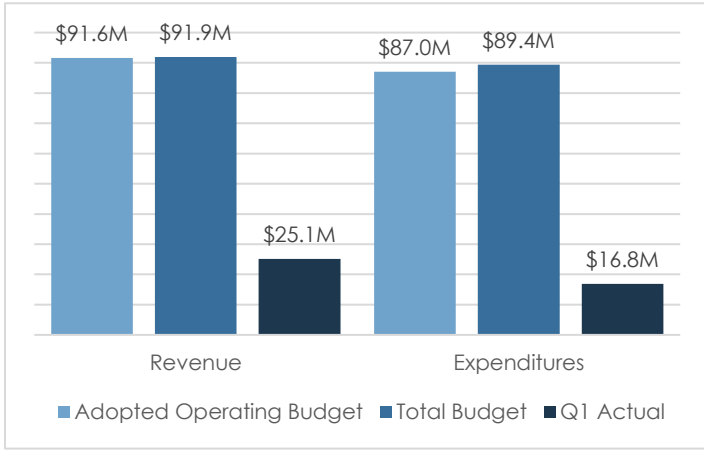
Electric Fund

The adopted amended budget for the Electric Fund now projects a \$9.12 million operating loss due to a planned draw on reserves to minimize rate increases. Retail sales 6.1% lower-than-anticipated and operating expenditures at 28.4% of total budget. Electric consumption is down due to milder temperatures through the first quarter of the fiscal year. Personnel savings are anticipated due to a 15.2% vacancy rate. Power supply costs are trending 2% over budget due to significantly higher-than-expected increases in market energy and natural gas prices.



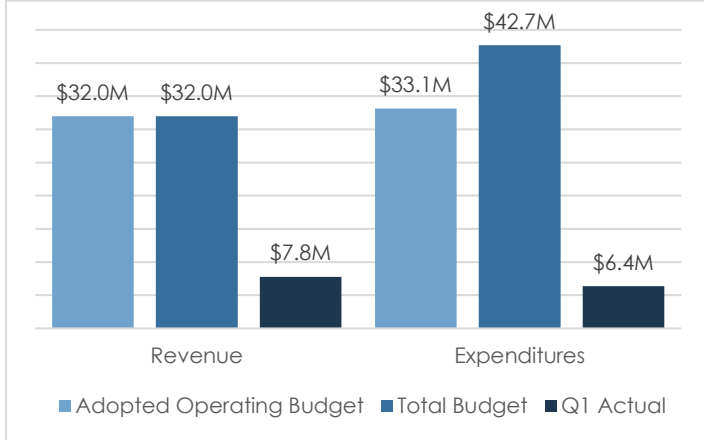
Water Fund

The amended budget for the Water Fund projects a net operating gain that is \$4.59 million. Residential revenues and consumption are both 13.5% lower-than-anticipated as decreased water consumption driven by milder temperatures and increased precipitation. Operating expenditures are 20.1% of budget. The personnel vacancy rate is 13.9%. Overall, water expenditures are projected to remain within the budgeted appropriation limit at fiscal year-end.



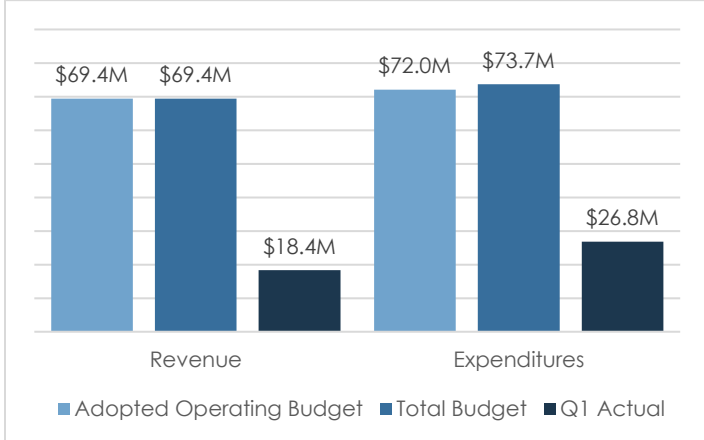
Refuse Fund

The amended Refuse Fund budget anticipates a net operating loss of \$1.16 million, reflecting reduced recycling revenues from declining industry demand, higher recycling costs, increased tonnage, and new state mandates. The fund began the fiscal year with \$6.19 million in fund reserves (net of prior year encumbrances) and a combined \$11.00 million from General Fund contributions and ARPA funding. The Refuse Fund faces challenges like staffing shortages and increased maintenance costs for an aging fleet. Overtime costs are expected to rise but will be offset by personnel savings. To address these issues, efforts are underway to intensify hiring and replace vehicles.



Sewer Fund

The amended budget for the Sewer Fund projected an operating loss of \$2.65 million. Operating revenues are anticipated to exceed budget projections due to the unanticipated growth in planned development. Operating expenditures are 17.0% of budget. The Sewer Fund had a personnel vacancy rate of 21.2%, which required staff to cover shifts and manage increased workloads. Savings are anticipated to offset projected Overtime overages.

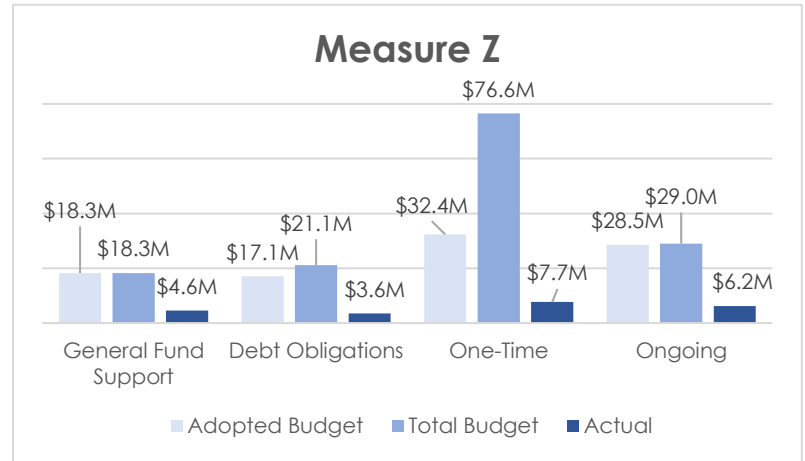


OTHER FUNDS

Measure Z

Based on the spending items approved to date and slowing tax revenue performance, Measure Z is projected to end the fiscal year with approximately \$47.19 million in fund reserves (refer to Attachment 2). Separately, \$5.00 million is held in contingency reserves per the adopted Measure Z Reserve Policy to ensure sufficient funding for ongoing costs in the event of under-performing revenues.

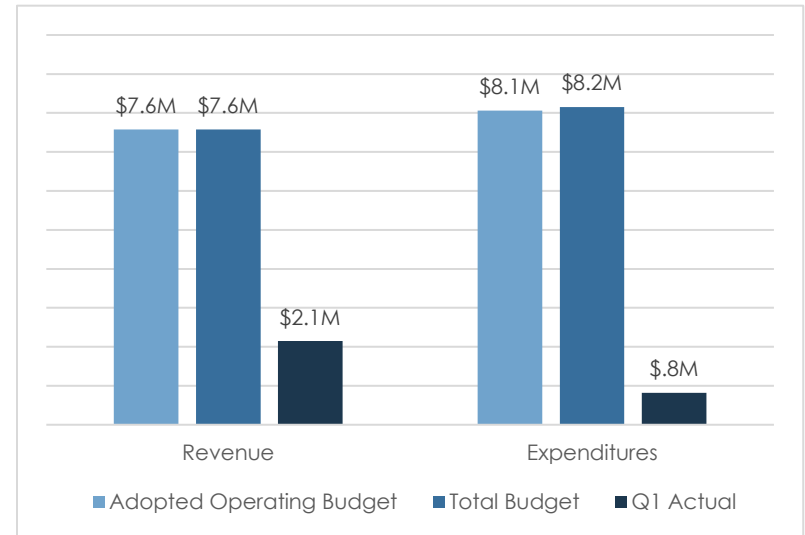
The chart to the right displays the spending status as of September 30, 2023, of approved spending items of various types. Total budget also reflects encumbrances and capital carryovers from FY 2022/23.



Public Parking Fund

The FY 2023/24 adopted amended budget for the Public Parking Fund anticipates a draw on fund reserves of approximately \$0.48 million. Parking revenues in the original FY 2022-2024 adopted budget included new parking rates, which were subsequently rescinded. On April 18, 2023, the City Council approved a new Parking Rate and Hour Schedule, with revenue and expenditure adjustments incorporated into the FY 2023/24 adopted amended budget.

Downtown parking saw a 56.1% increase in revenue during the first quarter compared to the prior year, due to the new Parking Your Way program. This program includes improvements like more accessible free parking, extended operational hours, new monthly parking options, the Park Riverside app, and the installation of Parking Access Revenue Control Systems (PARCS) in the garages.



FY 2024-2026 Biennial Budget Process

The City of Riverside adopts a biennial budget and a five-year planning process to provide a more informative, long-term outlook on the city's finances. Public engagement is encouraged at numerous meetings during which budget presentations and discussion will be conducted and feedback will be received. The final budget will be presented at two meetings, with a public hearing at the City Council meeting. Get the latest information on public meetings by visiting the City's budget website at <https://riversideca.gov/finance/budget.asp>.

Date	Time	Meeting Body	Subject Matter
April 8	5:00 PM	Board of Library Trustees	Library Department Budget
April 8	6:30 PM	Board of Public Utilities	Public Utilities Preliminary Budget
April 11	5:00 PM	Budget Engagement Commission	Budget Workshop
April 15	6:30 PM	Park & Recreation Commission	Parks, Recreation, & Community Services Department Budget
April 18	9:00 AM	Planning Commission	Proposed CIP Conformance to General Plan
April 24	3:00 PM	Museum of Riverside Board	Museum Preliminary Budget
May 9	5:00 PM	Financial Performance & Budget Committee (Special Meeting)	Budget Workshop
May 21	1:00 PM	City Council	Proposed Budget
June 25	6:15 PM	City Council – Evening Session	Public Hearing and Final Budget Adoption