GOVERNMENT OF THE DISTRICT OF COLUMBIA
OFFICE OF THE CHIEF FINANCIAL OFFICER

Jeffrey S. DeWitt
Chief Financial Officer

July 1, 2014

The Honorable Vincent C. Gray
Mayor of the District of Columbia
1350 Pennsylvania Avenue, NW – 6th Floor
Washington, DC 20004

The Honorable Phil Mendelson
Chairman
Council of the District of Columbia
1350 Pennsylvania Avenue, NW – Suite 504
Washington, DC 20004

RE: Quarterly Revenue Certification Update

Dear Mayor Gray and Chairman Mendelson:

I would like to inform you that the revenue estimates for FY 2014 - FY 2018 remain unchanged from the February 2014 certification.

Table 1: June 2014 Revenue Estimate

Local Fund Revenue Estimate ($ millions)	**Estimate** FY 2014	**FY 2015**	**Projected** FY 2016	**FY 2017**	**FY 2018**
February 2014 Estimate	**$6,334.1**	**$6,690.7**	**$6,896.3**	**$7,119.5**	**$7,276.2**
June 2014 Estimate*	**$6,334.1**	**$6,690.7**	**$6,896.3**	**$7,119.5**	**$7,276.2**
Annual % Change	*2.1%*	*5.6%*	*3.1%*	*3.2%*	*2.2%*

**The June revenue estimates do not reflect pending legislative changes*

Overview

There is no change to the revenue forecast as strengths in the withholding component of income and property related taxes have been offset by weaknesses in the capital gains portion of the individual income tax, the business income taxes, and fines from automated traffic enforcement. The causes for weaknesses in collections are largely behind us and more recent data on tax collections indicates increasing momentum that should put revenues on track to meet the February estimate. Furthermore, there are no significant changes in the economic outlook for subsequent fiscal years that would warrant changes to the February estimates for fiscal years FY 2015 through FY 2018.

Revenue Highlights

The two largest revenue sources, the withholding component of personal income tax and the property tax, which account for approximately 60 percent of local fund revenue, are on track to meet or exceed the forecast. The withholding component of income, an important barometer of the condition of the District's economy, is growing at a 5.1 percent annual rate, a full percentage point higher than anticipated. Property taxes are on track to rebound by 4.4 percent. The strength of the real estate market is also reflected in collections of deed transfer and recordation taxes. These were anticipated to decline by more than 14 percent but are currently running 4 percent higher on a year-over year basis, and in recent months have accelerated even further.

These positive factors are offset, however, by weaker than expected performance of several other revenue sources. First, final income tax payments in April were much lower than expected because of sharply reduced receipts from the capital gains portion of the income tax. This did not just affect the District; states across the nation had significantly reduced revenue due to declines in capital gains. The February revenue estimate anticipated lower capital gains revenue because of federal tax law changes at the beginning of 2013 that caused investors to accelerate income tax payments in 2012, but the level of decline was far greater than what was forecast. Next, larger than anticipated refunds, a result of overpayments made when the District implemented combined reporting, reduced business franchise tax collections below receipts from previous year. There was also the loss of economic activity in the District several days in the fall and winter because of the government shutdown and harsher than usual winter weather. As a result, sales tax growth so far this fiscal year is below forecast. Finally, traffic fines receipts year to date are lower than the previous year because the rollout of the additional equipment has been slower than anticipated.

These negative factors are largely behind us and the trends over the past quarter show an acceleration in revenue growth. The recent momentum in collections, barring any additional negative economic shocks, puts revenue collections on track to meet the estimate.

National and Regional Economies

The fundamentals underlying the national economy continue to improve. National forecasts expect growth in FY 2014 and FY 2015 to exceed that of FY 2013.

- Since the official end of the U.S. recession in June 2009, real GDP has increased in 17 of the past 19 quarters. For the entire 2013 fiscal year the growth rate averaged 1.7 percent. Although the economy appears to have actually contracted at an annual rate of 2.9 percent in the first quarter of calendar year 2014, growth has still averaged 2.1 percent for the entire first half of FY 2014.
- U.S. employment added 2.2 million jobs (1.6%) from April 2013 to April 2014, and has generally returned to the level of employment that existed before the recession began in December 2007. Currently, all growth in national employment is in the private sector.
- The U.S. unemployment rate (seasonally adjusted) fell to 6.3 percent in April 2014. One year earlier the rate was 7.5 percent.
- U.S. Personal Income in the March 2014 quarter was 3.2 percent above a year ago.
- The Standard & Poor's 500 stock market index in April 2014 was 2.3 percent above its level three months ago, and 18.7 percent more than a year ago.
- In the three-month period ending April 2014, wage and salary jobs in the Washington metropolitan area grew by 5,467 (0.2%) compared to a year earlier. All of the net increase was in the private sector. The rate of growth of metropolitan area employment has been below the U.S. average for most of the last two years.
- The metropolitan area unemployment rate was 4.5 percent in April (not seasonally adjusted), down from 5.1 percent a year earlier.
- In May 2014, the consensus of fifty economists contributing to the Blue Chip Economic Indicators continued to forecast slow, steady growth in real GDP. Growth in real GDP in FY 2014 is expected to be 2.4 percent (up from 1.7 percent in FY 2013), and nominal growth is 4.0 percent. For FY 2015, the real and nominal growth rates are expected to rise to 2.9 percent and 4.9 percent, respectively. Two economic forecasting services, IHS Global Insight and Moody's Economy.com, anticipate that the annual growth rate in real GDP in FY 2015 will be 2.7 percent and 3.6 percent, respectively.

The District of Columbia Economy

Recent trends in the D.C. economy include slowing job growth, increases in population and a strong housing market.

Population growth has been a major factor in increasing the District's income and sales tax bases, and is also a major driving force behind rising home values. In the last five years (2008 to 2013) the District's population has grown by 62,213 (11.4%), an increase that has averaged more than 1,000 net new residents per month over this time. Natural increase (births minus deaths) now accounts for about one third of the population gain.

Federal Spending and Austerity Measures

Approximately 25 percent of employed D.C. residents work for the federal government. Federal civilian employment accounts for about 27 percent of all jobs located in the District of Columbia and 32 percent of the wages and salaries that are generated in the city. Federal contracting also accounts for additional jobs and income. Because the federal government is such a dominant presence in the District's economy, trends in federal spending have a major impact on the District of Columbia's economy and revenues.

In 2013 Congress enacted legislation resolving certain short-term federal budget and fiscal matters: the Bipartisan Budget Act of 2013 set limits for FY 2014 and FY 2015 for defense and non-defense discretionary federal spending; the Consolidated Appropriations Act of 2014 appropriated funds for the balance of the fiscal year; and the debt limit was raised. Sufficient detail is not yet available concerning all the ramifications of these laws for the District of Columbia, but it is likely to be of benefit in two ways—first, relaxation of some of the most stringent federal spending restrictions, and second, reduction in fiscal policy uncertainty that may have contributed to the economic slowdown in the District.

Still, federal austerity remains a continuing factor affecting the District's economy. While more federal spending has been approved for FY 2014 (a 2.9% increase in domestic discretionary spending over the FY 2013 level) there is almost no additional growth for FY 2015 and FY 2016. Domestic discretionary spending in FY 2016 will be less than it was in FY 2012.

Trend highlights

- In the three months ending April 2014, there were 3,600 more wage and salary jobs located in the District than a year earlier. Of particular note, there were 5,900 fewer federal government jobs in April than there were a year earlier. Private sector growth continues—the number of jobs in the District was 8,500 (1.7%) higher in April than a year ago.
- Seasonally adjusted employment in April was about the same as it was in October.
- District resident employment in the three months ending April 2014 was 532 (0.2%) less than a year earlier.
- The April unemployment rate fell to 7.5 percent (seasonally adjusted rate), a decrease from 8.5 percent a year ago.
- Wages earned in the District of Columbia grew 0.6 percent in the December 2013 quarter compared to the same quarter a year ago. D.C. personal income was 1.1 percent higher. As D.C.'s population has grown a greater share of income earned in the District is retained here.
- Home sale prices generally continue to show significant gains. Single family sales for the three-month period ending April 2014 were down 5.8 percent from a year ago, but there was a 10.5 percent increase in the average selling price. Condominium sales were up 4.8 percent and the average price was 5.0 percent higher. The value of settled contracts for home sales for the three-month period ending April was 6.3 percent more than a year ago.

- Occupied commercial office space in March 2014 was up by 0.2 percent from a year ago, and the vacancy rate rose slightly over the past year to 13.0 percent from 11.9 percent. Rents continued to edge downward over the past year.
- Hotel room-days sold for the three months ending April 2014 were 1.5 percent below the prior year, and hotel room revenues were also down by 1.5 percent.

Outlook and Risks

Although the current revenue estimate includes the impact of the recent federal budget agreements on the District, the estimate is of necessity based on limited information about the specific effects this has on the city's employment and income. If federal austerity is more severe than this estimate assumes, the impact on the District's fiscal outlook could be much higher.

Federal cutbacks are not the only risk that the District faces. Other downside risks include the possibility of a slowing down or reversal of national economic growth, declines in the stock market, increases in interest rates, and additional financial market problems as the Federal Reserve phases out some of its monetary stimulus activities. Possible disruptions to oil supplies or other developments arising from uncertainties in the Middle East and national security events also add to uncertainty.

Many economic development initiatives are underway in the District of Columbia, such as CityCenterDC. This, and other ongoing developments, will contribute to increasing the District's tax base, but the timing of gains to employment and income is uncertain. Nor is it clear what impact, if any, the recent slowdown in employment located in the District of Columbia and in resident employment may have on population dynamics.

If you have any questions regarding this matter, please do not hesitate to contact me.

Sincerely,

Jeffrey S. DeWitt

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