CITY OF SCOTTSDALE

MONTHLY FINANCIAL UPDATE

DECEMBER 2008

REPORT HIGHLIGHTS

- We continue to see economic declines in City revenues and November returns were no exception. Based on these returns, we have revised our forecasts and now estimate the FY08/09 deficit near $40M and FY09/10 deficit at approximately $50M (all funds). To be clear, these estimates do not consider any actions or recommended plans (to-date) to close the gap and balance our budget. Staff have been actively working on many initiatives to address the revenue declines and adjust our spending plans. We expect to meet with City Council on our progress to-date in early January and have planned a Special Council Meeting on 1/20/09 for a complete update.
- As the single greatest revenue source for the General Fund, fiscal year-to-date Sales Tax revenues are down 15% or $6.7 M. compared to prior fiscal year. The current Sales Tax annualized forecast has been revised down $22.3 M. from the adopted budget plan.
- Development Permits and Fees fiscal year-to-date revenues are down 47% or $2.8 M. compared to prior year and our current annualized forecast predicts a $6 M. decrease in building permits this fiscal year.
- The continued widespread deterioration in the U.S. leading index suggests that the recession that began in December 2007 will continue into the new year and the contraction in economic activity could deepen further in the near term.

FY 2008/09 GENERAL FUND ESTIMATED YEAR END BALANCE

The following table compares the FY08/09 budget plan to the current General Fund balance forecast, incorporating the latest economic estimates and impacts of economic contingency plans.

Estimated Fiscal Year End 2009 GENERAL FUND Balance (In Millions)	**FY08/09 Approved Budget**	**FY08/09 Current Forecast**	**Variance Favorable/ (Unfavorable)**
Actual Beginning Balance July 1, 2008	$ 40.6	$ 44.2	$ 3.6
Sources of Funds	286.8	256.2	(30.6)
Uses of Funds (Operating Expenses)	259.1	259.1	-
Transfers Out	22.9	19.9	3.0
Debt Service	6.0	3.7	2.3
***Estimated* Ending Balance June 30, 2009:**			
Operating Contingency	4.8	4.8	-
Photo Enforcement Loop 101	0.6	-	(0.6)
General Fund Reserve	29.9	29.9	-
Unreserved Fund Balance	4.1	(17.0)	(21.1)
***Estimated* Ending Fund Balance June 30, 2009**	**$ 39.4**	**$ 17.7**	**$ (21.7)**

Table may display minor rounding variances in the aggregate due to reflecting amounts in millions.

Estimated Ending Fund Balance

Scottsdale is experiencing an unprecedented recessionary impact across revenue categories, with the most significant factors including retail sales, construction, and auto dealers. The current revenue forecast for FY08/09 is included in the General Fund summary table above but the Estimated Ending Balance does not (yet) take into consideration budget balancing strategies currently being discussed/evaluated by City management and staff. Based upon the prognosis that the economy will not achieve any significant recovery or growth in the near term our current overall deficit projection is in the $40 M. - $50 M (all funds) range for the next 12-24 months. Budget balancing strategies will be aimed at providing current benefit/relief from lower revenues, as well as structural changes to help address our deficit prognosis and balance the budget in FY09/10 and beyond. As these strategies are evaluated and implemented, their estimated results will be reflected in future financial reports as the budget is balanced (see Budget Update section on page 3 for an update on the FY08/09 budget review process).

GENERAL FUND REVENUE – FY2008/09 FORECAST

The following table summarizes key revenues that affect the City's General Fund. The table compares year end revenue forecast to the budget plan. The latest adjustments to forecast are reflected in the table. The current net impact of these adjustments to the revenue bottom line is ($30.6) million under the FY08/09 budget plan, reflecting ongoing recessionary forces at the national and local level, factors related to the financial market turmoil, a depressed housing market, and dropping retail, automotive, and construction activity. We will continue to closely monitor revenues and make further adjustments to forecast as necessary.

FY 2008/09 General Fund Revenues (In Millions)	FY08/09 Adopted Budget	FY08/09 Current Forecast	Variance Favorable/ (Unfavorable)
Transaction Privilege (Sales) Tax (1)	$ 116.6	$ 94.3	$ (22.3)
Transient Occupancy (Bed) Tax (1)	2.0	1.6	(0.4)
Property Tax	22.4	22.1	(0.3)
State Shared Sales Tax	22.0	20.8	(1.2)
State Shared Income Tax	34.0	35.1	1.1
Auto Lieu Tax	9.7	7.7	(2.0)
Business Licenses & Fees	1.8	1.8	-
Building Permit Fees & Charges	14.5	8.5	(6.0)
Interest Earnings	4.5	3.5	(1.0)
Other	47.6	49.1	1.5
Total Revenue	**$ 275.1**	**$ 244.5**	**$ (30.6)**
Transfers In	11.7	11.7	-
Total Sources of Funds(2)	$ 286.8	$ 256.2	$ (30.6)

Table may display minor rounding variances in the aggregate due to reflecting amounts in millions.

(1) Privilege & Use Tax and Transient Occupancy Tax collections lag by one month (October activity reported in November results).

(2) Reconciles to Sources of Funds line item in "General Fund Balance" table, page 2.

Below are highlights related to the table above.

Sales Tax

As the single greatest revenue source for the General Fund, fiscal year-to-date revenues are down 15% or $6.7 M. compared to prior fiscal year. An expected dismal holiday shopping season for retailers, coupled with significant drops in construction activity, auto sales, and related dealership closings and relocations, have resulted in Financial Services staff revising the current Sales Tax forecast down $22.3 M. from the adopted budget plan. We will continue to closely monitor sales tax activity and make additional revisions as necessary. Category fiscal year-to-date changes over prior year: automotive -30.2%, construction -22.4%, food stores -4.4%, hotels and motels -10.2%, major department stores -14.6%, miscellaneous retail -19.9%, other taxable activity +11.6%, rental -3.0%, restaurants -13.9%, utilities +2.4%.

Bed Tax

Fiscal year-to-date revenues are down 14% or $0.1 M. compared to prior fiscal year. Staff has reduced the current forecast by $0.4 M. The outlook for hoteliers and the travel industry as a whole remains dim until the economy starts showing signs of a significant turnaround.

Property Tax

Variance reflects recent utility settlement.

State Shared Revenues

Adjustments reflect latest state shared estimates provided by the Arizona Department of Revenue.

Development Permits and Fees
Fiscal year-to-date revenues are down 47% or $2.8 M. compared to prior year. Coinciding with a decline in the City's construction sales tax revenues, the real estate market bust is causing a drop in building permit revenues. Our current forecast takes into consideration two plus years of double-digit decreases in development activity as measured by permits issued and property valuations and predicts a $6 M decrease in building permits for this fiscal year.

Interest Earnings
$(1.0) M. unfavorable variance reflects revised forecast based on latest financial market forces.

Other Revenue
Adjustments to forecast for Other Revenue category include projected minor increases to parking and court fines, light and power franchise fees, and intergovernmental revenue, and the City's portion of $29 M. legislative proposed rebate ($730K Scottsdale share) to the State's General Fund.

BUDGET UPDATE

Budget Process Update:

The Financial Services staff continues to estimate a revenue decline of 10% over the prior fiscal year actuals, with a deficit impact range of $40 M. - $50 M. (all funds) for this year and into FY09/10.

During the month of November, senior management completed their review of the departments' proposed 10% budget reductions. The 10% budget reductions provided by the departments equals approximately $18 M. for FY08/09.

Additionally, staff from the City Manager's Office, Human Resources, and Financial Services continue to meet every other week to review vacant positions. The objective is to ensure filling a vacant position is consistent with only our highest service needs and priorities. The strategic management of vacant positions is a key component of mitigating the impact of the revenue reduction while considering service delivery impacts to our citizens.

The staff continues to review the "pay as you go" existing Capital Improvement Plan (CIP) and identifying areas of possible changes, such as reducing short-term funding for maintenance projects. Examples of other solutions being looked at include use of reserves, reducing fuel consumption, and overhead cost allocations to CIP projects.

As these solutions materialize, staff will provide timely updates to the City Council, citizens, employees, other stakeholders, and the media. Finally, because these modifications will be necessary to balance this year's budget as well as deal with longer–term economic downturn, our objective is to simultaneously achieve a balanced FY09/10 Budget proposal.

Contingency Budget Update:

- General Fund Operating Budget Contingency. During the fiscal year, Financial Services staff monitors the $5,000,000 General Fund Operating Budget Contingency. The City Council has approved the following uses of cash from the General Fund Operating Budget Contingency:

    - July 8, 2008: $208,000 WestWorld – to bring feed and bedding program in-house.

  The total FY2008/09 General Fund Operating Budget Contingency approved by City Council to date is $208,000, leaving a cash balance of $4,792,000.

- Capital Budget Contingency. During the fiscal year, Financial Services staff monitors the use of the $4,500,000 million Capital Budget Contingency. The City Council has approved the following uses of cash from the Capital Budget Contingency:

    - September 9, 2008: $236,000 Camelback Park – funds required to cover additional costs.
    - October 7, 2008: $241,873 Traffic Signal Program – funds required to close-out two projects (Y0723 and Y0823) and to record the related projects in the City's fixed asset records.
    - December 9, 2008: $1,661,660 Scottsdale Center for the Performing Arts (D0604) – funds required to cover additional project costs.
    - December 9, 2008: $14,417 Mid-year CIP close-out of projects with nominal negative balances.

- December 9, 2009: $185,000 Downtown Restrooms (D0602) – funds required to complete project.
- December 9, 2008: $150,000 Stetson Plaza/South Canal Bank Project – needed to create new CIP project for sales tax rebate.

The total FY08/09 total Capital Budget Contingency approved by City Council to date is $2,488,950, leaving a cash balance of $2,011,050.

NATIONAL, STATE, AND LOCAL ECONOMIC TRENDS

The following table summarizes some key national and state economic indicators, compares the results to previous actual or forecast, and provides a positive, negative, or neutral trend. Unless otherwise indicated, previous and current values represent a month-to-month comparison in the same year.

Economic Indicators	Month or Quarter	Current Value	Overall Trend***	2008 Estimate
National **– Leading Economic Index**	November	99.0	Negative	-
Consumer Confidence	November	44.9	Negative	-
Consumer Price Index	November	212.425	Negative	-
Unemployment Rate	November	6.7%	Negative	-
State **– Business Leader Confidence Index**	Q4 2008	42.4	Negative	-
Retail Sales Growth	Forecast*	-3.0	Negative	1.0
Personal Income Growth	Forecast*	3.6	Negative	3.5
Wage and Salary Employment Growth	Forecast*	-1.2	Negative	0.0
Single Family Housing Permits	Forecast*	-37.3	Negative	-0.1
Population Growth	Forecast*	2.0	Negative	2.0
Hotel/Motel Room Rate (Scottsdale)	October**	$171.54	Neutral	-
Hotel/Motel Occupancy Rate (Scottsdale)	October**	63%	Negative	-

*Reflects Arizona Blue Chip Consensus Economic Forecast annual percent change 2008 from 2007 and projected 2009 from 2008, as of December 2008.
**Reflects over-the-year comparison.
***Overall Trend considers performance of indicators over a three-to-six-month period, not necessarily a month-to-month comparison.

NATIONAL:

Economic Growth

- **The leading index continued to fall in November, due mainly to large declines in building permits, stock prices, and initial unemployment claims.** Without the very large increases in inflation-adjusted money supply since September, the leading index would have been significantly weaker. The six-month change in the leading index has continued to fall to -2.8 percent (a -5.6 percent annual rate) in the period through November, down from -0.9 percent (a -1.7 percent annual rate) during the previous six months. The rates of the six-month decline have picked up in recent months and are now the largest since 1991. The continued widespread deterioration in the index suggests that the recession that began in December 2007 will continue into the new year and the contraction in economic activity could deepen further in the near term.
- **Real Gross Domestic Product contracted at a 0.5 percent annual rate in the third quarter of 2008**, down from a 1.8 percent average annual rate of growth for the first half of the year.

Employment

- **Nonfarm payroll employment fell sharply (-533,000) in November, and the unemployment rate rose from 6.5 to 6.7 percent.** November's drop in payroll employment followed declines of 403,000 in September and 320,000 in October. Job losses were large and widespread across the major industry sectors in November.

Consumer Confidence

- **The Consumer Confidence Index, which had declined to an all-time low in October, improved moderately in November** and now stands at 44.9 (1985=100), up from 38.8 in October. Inflation expectations, which have been at historically high levels in recent months, subsided considerably as a result of falling gas prices. But despite the improvement, consumers remain extremely pessimistic and the possibility that economic growth will improve in the first half of 2009 remains highly unlikely.

Inflation

- **The Consumer Price Index for All Urban Consumers (CPI-U) decreased 1.9 percent in November**, before seasonal adjustment. The November level of 212.425 (1982-84=100) was 1.1 percent higher than in November 2007. The energy index fell 17.0 percent in November. The decrease was about twice the October decline and energy prices are now 32.4 percent below the July peak earlier this year. The gasoline index fell 29.5 percent in November and gas prices are now 47.0 percent below their July peak.

Economic Predictions

- **Latest on the economy from the W. P. Carey School's Western regional Blue Chip**: "The outlook for the fourth quarter of 2008 turned from bad to worse this month as unfavorable economic news continued to accumulate. The two persistent questions about this downturn are (1) how deep it will be and (2) how long it will last. The revised forecast now calls for real GDP to decline by 4.5 percent in the fourth quarter, and by an additional 3.0 percent in the first quarter of 2009. The economy bottoms out in the second quarter and modest positive growth is expected in the second half of the year.

  Consumer spending will fall by 4.0 percent in the fourth quarter of 2008 and does not recover until the third quarter of 2009. Nonresidential building is projected to contract at an increasing rate through the first three quarters of 2009. The expectation among analysts is that the combination of weak consumer spending, negative job creation, and the ongoing credit crisis will inhibit office, commercial, warehousing, and other nonresidential structures.

  Exports will fall in the current quarter and through 2009 as the global slowdown intensifies. The dollar seems to be giving back some of its recent gains, but a weaker dollar will not make up for sluggish demand in international markets. Analysts expect that GDP growth will be negative next year for major nations including the UK and Germany, and China's real growth will dip out of the double-digit range.

  The current U.S. recession began one year ago, so the downturn already exceeds the postwar average of 10 months. It is becoming increasingly evident that this recession will be among the worst in the postwar period, and before it is over, it may hold that dubious distinction without quarrel from anyone."

ARIZONA:

- **The *Blue Chip Western Economic Forecast* reports the following economic news for Arizona**: "According to the 2008 consensus forecast for population growth, there aren't gong to be as many new Arizona residents as in the past. Reports from Arizona hospitals indicate births are down, typical in an economic contraction. Moreover, both births and population outflows may have been affected by tighter restrictions on undocumented workers, as some chose to leave the state.

  But the main factor underlying slower population growth is the downward spiral in Arizona labor markets. Arizona's population growth outpaces most of the rest of the nation for many reasons, but the typically dynamic job market in the state should be near the top of that list. And just two years ago at year-end, Arizona ranked fifth in job growth among all states. But last year, as the national recession officially started, the Grand Canyon State had dropped to 46th position, and this year the ranking has worsened, to 49th.

For the year as a whole, the state will likely lose 40,000 jobs. As comparison, in spite of much teeth-gnashing about the “jobless recovery” following the recession of 2001, the Arizona economy didn’t actually lose any jobs in that downturn, on an annual basis.

Retail sales are down in the state because Arizona consumers are feeling the same loss of confidence as households everywhere. A recession is a time for belt-tightening, not committing to big-ticket or spontaneous spending. And sluggish growth in personal income is not helping purchasing power. The consensus is that Arizona personal income will be up by less than 4 percent in 2008, a figure similar to that recorded in the post 9/11 year, 2002.

With weak growth figures across the board for 2008, the current consensus outlook from the Arizona Blue Chip forecast panel calls for a bottoming out in 2009. The forecasters are evenly split on the prospects for Arizona employment growth next year; half expect an increase and half a decline, with a consensus forecast of 0.0 percent for 2009.

Both single-family and multifamily permits will be flat, population growth will be about the same, and retail sales will remain subdued.

The current outlook is that the first half of 2009 will bring more bad news at the national level, including negative growth in Gross Domestic Product along with higher unemployment rates. Two drivers of the national economy in 2008, exports and non-residential building, are expected to weaken, leaving only the government sector as a possible source of expanded demand.

The capsule conclusion is that 2009 is not positioned to bring a real turnaround. The recession may register a trough after mid-year, with some modest gains after that. But the overall pattern of growth for Arizona will be “bumping along the bottom,” not a significant rebound.”

SCOTTSDALE BUSINESS ACTIVITY (PROVIDED BY ECONOMIC VITALITY)

- The **U.S. Department of Commerce** opened an export assistance office at **SkySong**. The federal trade agency already has offices in Tucson and Phoenix and is focused on helping U.S. businesses expand and export into new international markets.
- **iCrossing**, headquartered in Scottsdale, has formed a partnership with China-based search engine marketing agency Beijing Gridsum Technology Co., Ltd. Together, the companies will manage and develop international search marketing campaigns for global brands in Asian markets.
- **First Western Trust Bank**, a boutique bank and trust company based in Denver, has expanded its operations to Arizona with the recent opening of a state-chartered bank in Scottsdale. First Western provides private banking, investment management, personal trust and wealth planning for wealthy individuals, their families and foundations.
- Scottsdale-based **GoDaddy.com** made the *Phoenix Business Journal* list of “Best Places to Work" for the fifth consecutive year, ranking 19th in the category for large Valley companies. The “Best Places to Work" ranking is based on employee surveys, which measure retention rate, manager effectiveness, team effectiveness, employee alignment with company goals, trust in senior leadership and trust in fellow coworkers, among other performance categories.
- **Hypercom**, headquartered in Scottsdale, signed an agreement with TASQ Technology, a Canadian company, to distribute/market its new 32-bit Optimum T4205 to the Canadian marketplace. The T4205 is a sleek entry-level electronic payment device that is the ideal terminal for small independent merchants throughout Canada.
- Scottsdale-based **ECOtality**, **Inc.**, a leader in clean electric transportation and storage technologies, announced 3rd quarter revenues of $2.9 million. ECOtality’s subsidiaries, which include Electric Transportation Engineering Corporation (eTec), Innergy Power Corporation, and Fuel Cell Store, all reported positive operating income for the year to date. According to their website, ECOtality accelerates the market applicability of advanced electric technologies to replace carbon-based fuels through innovation, acquisitions, and strategic partnerships.