



# Fiscal Outlook & Department Budget Instructions

December 2024

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# Summary



## Fiscal Outlook:

- Rate of expenditure growth far outpaces City's General Fund revenues – creating an **\$876M two-year deficit** (**\$253M** deficit in FY 2025-26, **\$623M** in FY 2026-27)
- **Expenditure growth of \$1.7B far surpasses revenue growth of \$520M** over the next five years

## Budget Instructions to Departments:

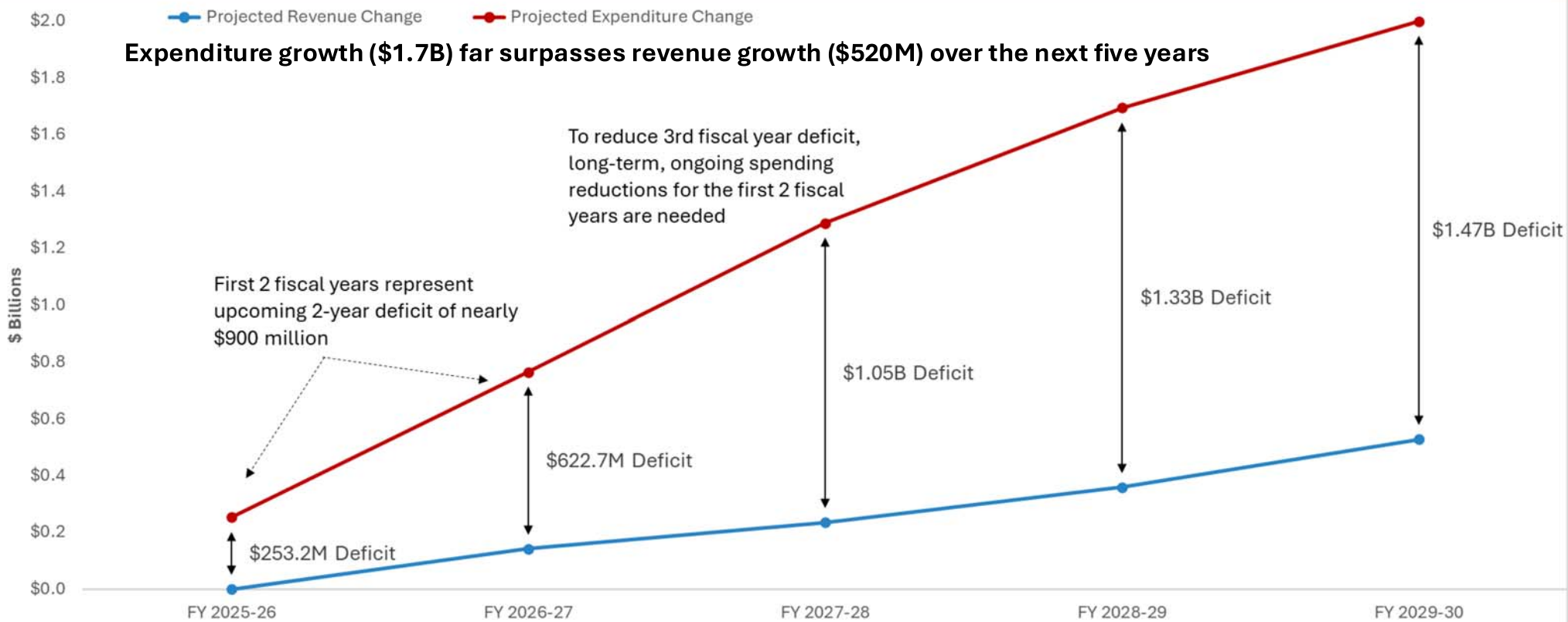
- **Ongoing, permanent spending reductions of 15% starting in FY25-26**



# Fiscal Outlook with Five-Year Financial Plan Update



# Fiscal Outlook: Spending Outpaces Revenue





## Fiscal Outlook: FY26 and FY27

**FY 25-26's \$253M** deficit driven by \$203M revenue reduction

- FY24 year-end fund balance **lower by \$118M**; distributes more evenly across years
- **\$132M reduction** in expected General Fund revenue
  - \$35M in business tax shifts
  - \$30M in Excess ERAF
  - \$40M in Hotel Tax receipts
  - \$10M in DPW & DPH fees due to Prop M fee elimination
- **\$53M increase** in expected DPH revenues

*Estimated changes since June 2024*

**FY 26-27's \$623M** deficit driven by \$705M expense increase

- **\$305M increase** of Salary & Benefit costs
- **\$108M increase** in baseline contributions
- **\$55M in assumed backfill** to one-time funds for ongoing shelter and opioid programming
- **Inflation assumptions** for contracts, materials & supplies, etc.
- **\$50M cost increase** for November 2024 Ballot measure approvals



## Fiscal Outlook: Major Assumptions in the Five-Year Forecast

- **Very modest economic and revenue growth**, does not assume a recession
- **Delayed or revised growth in major tax revenues:** shift of revenue timing for business tax as part of voter approval of Prop M, slower property tax recovery and hospitality sector rebound, reduced availability of one-time sources
- **Salary & Benefits:** CPI growth on all open contracts assumed July 1 from FY 2028-29 onward; 7.2% rate of return on pension investments
- **Citywide & Departmental Costs:** CPI growth on non-personnel costs, full funding of Ten-Year Capital & ICT Plans by FY 2026-27



## Fiscal Outlook: Five-Year Report Summary

| (\$ millions)                                     | Change from | Projection     |                |                  |                  |                  |
|---|-------------|----------------|----------------|------------------|------------------|------------------|
|   | AAO Budget  | 2025-26        | 2026-27        | 2027-28          | 2028-29          | 2029-30          |
| <b>SOURCES Increase / (Decrease)</b>              |             | <b>(203.2)</b> | <b>132.9</b>   | <b>225.8</b>     | <b>350.4</b>     | <b>518.6</b>     |
| Uses:   |             |                |                |                  |                  |                  |
| Baselines & Reserves                              |             | (1.5)          | (147.1)        | (232.1)          | (255.8)          | (254.0)          |
| Salaries & Benefits                               |             | 0.4            | (350.4)        | (607.0)          | (795.3)          | (943.1)          |
| Citywide Operating Budget Costs                   |             | (7.0)          | (125.0)        | (235.4)          | (316.1)          | (392.5)          |
| Departmental Costs                                |             | (41.8)         | (133.1)        | (204.6)          | (317.8)          | (400.2)          |
| <b>USES Decrease / (Increase)</b>                 |             | <b>(50.0)</b>  | <b>(755.7)</b> | <b>(1,279.1)</b> | <b>(1,684.9)</b> | <b>(1,989.8)</b> |
| <b>Projected Cumulative Surplus / (Shortfall)</b> |             | <b>(253.2)</b> | <b>(622.7)</b> | <b>(1,053.3)</b> | <b>(1,334.5)</b> | <b>(1,471.2)</b> |
| <b>Two-Year Deficit</b>                           |             |                | <b>(875.9)</b> |                  |                  |                  |



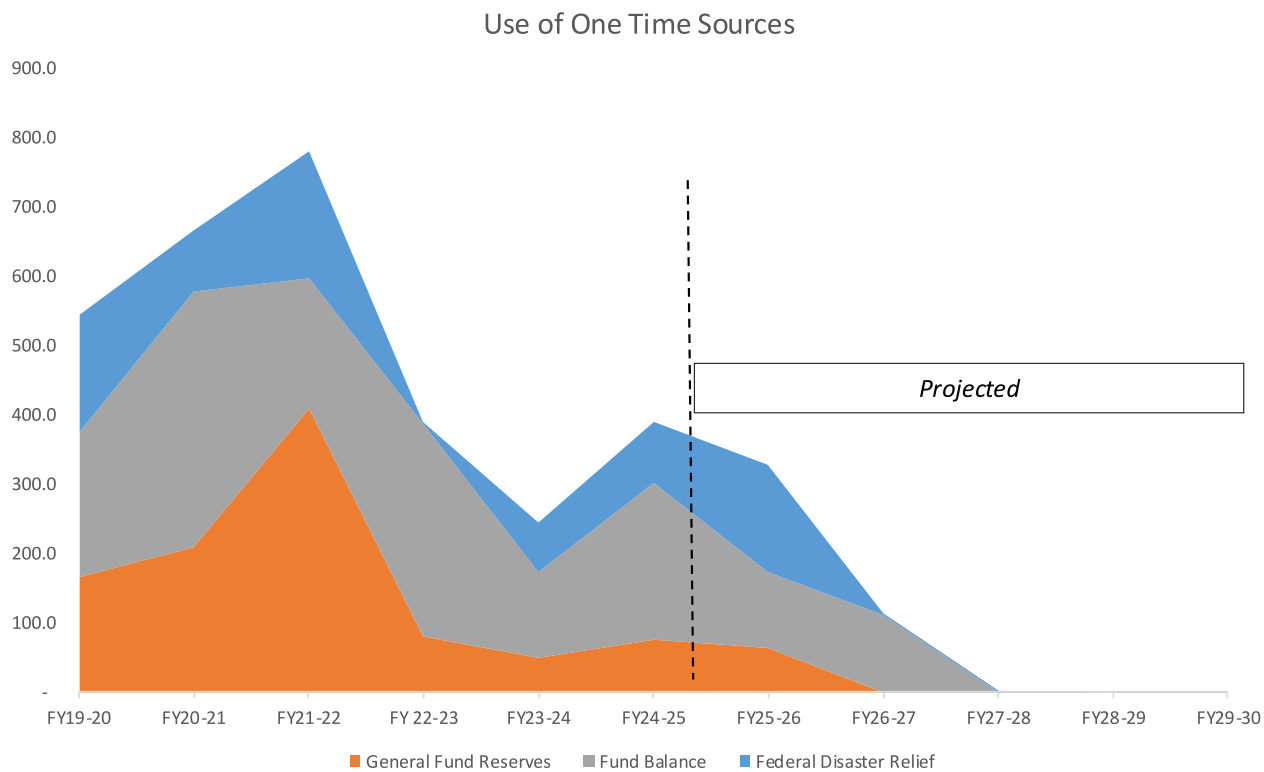


## Fiscal Outlook: What's Changed Since July?

- **Revenue projections revised downward**, including from Excess ERAF and hotel tax. Voter-approved business tax overhaul (Proposition M) reduces revenue initially and grows subsequently
- **Inflationary pressure** on contracts, leases, CBO grants, and materials & supplies costs
- **Voter-approved November 2024 ballot initiatives**, impacting education equity, children's services, housing, retirement, and staffing cost mandates
- **Use of fund balance** spread over a three-year period to ensure long-term financial stability



## Fiscal Outlook: One-Time Sources Depleted by FY28



- Since the COVID public health emergency, the City has relied heavily on one-time sources to close recent budgets
- These sources include federal disaster relief, General Fund reserves and fund balance
- Great uncertainty in unrealized FEMA reimbursements



## Fiscal Outlook: Risks

- **State Budget Shortfall:** Potential revenue loss if proposals like cuts to education-related property taxes return
- **Federal Policies:** Trump-era economic policies have unknown future impacts to the City and National economies. Changes to Medicare and Medicaid may strain local health services. Future FEMA reimbursements (\$244M outstanding) depend on Congressional approval.
  - **Uncertain Federal Grant Disbursement:** Grants may not be awarded or released in the upcoming administration.
- **Assessment Appeals:** Declining property values risk lowering tax revenue with at-risk revenue tied to appeal outcomes
- **Business Tax Risks:** Pending tax appeals threaten over \$400M in business tax revenue

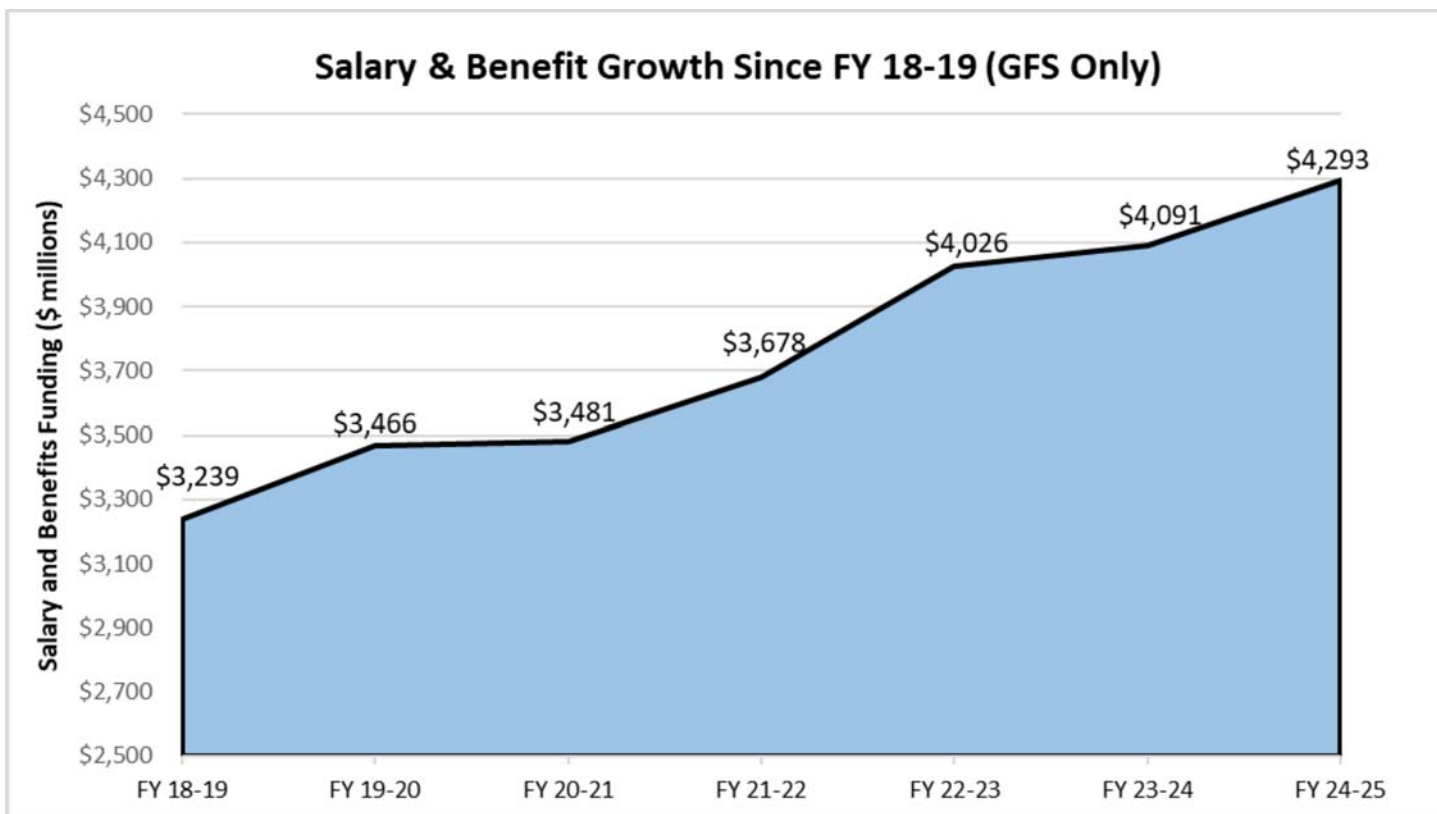


## Fiscal Outlook: Key Expenditures in the Five-Year Projection

- **Salaries and benefits:** Increase by over \$900 million over next five fiscal years
- **Required baseline contributions:** Grow by over \$200 million, including SFMTA and Student Success Fund
- **Citywide operating costs:** Real estate, capital, debt payments, PUC rates, and inflation on non-personnel services and multiyear nonprofit grants
- **Other major costs:** inflation on public health operating costs, IHSS program growth, shelter costs due to expiring state grants, commitments to subsidizing housing for formerly homeless (LOSP)



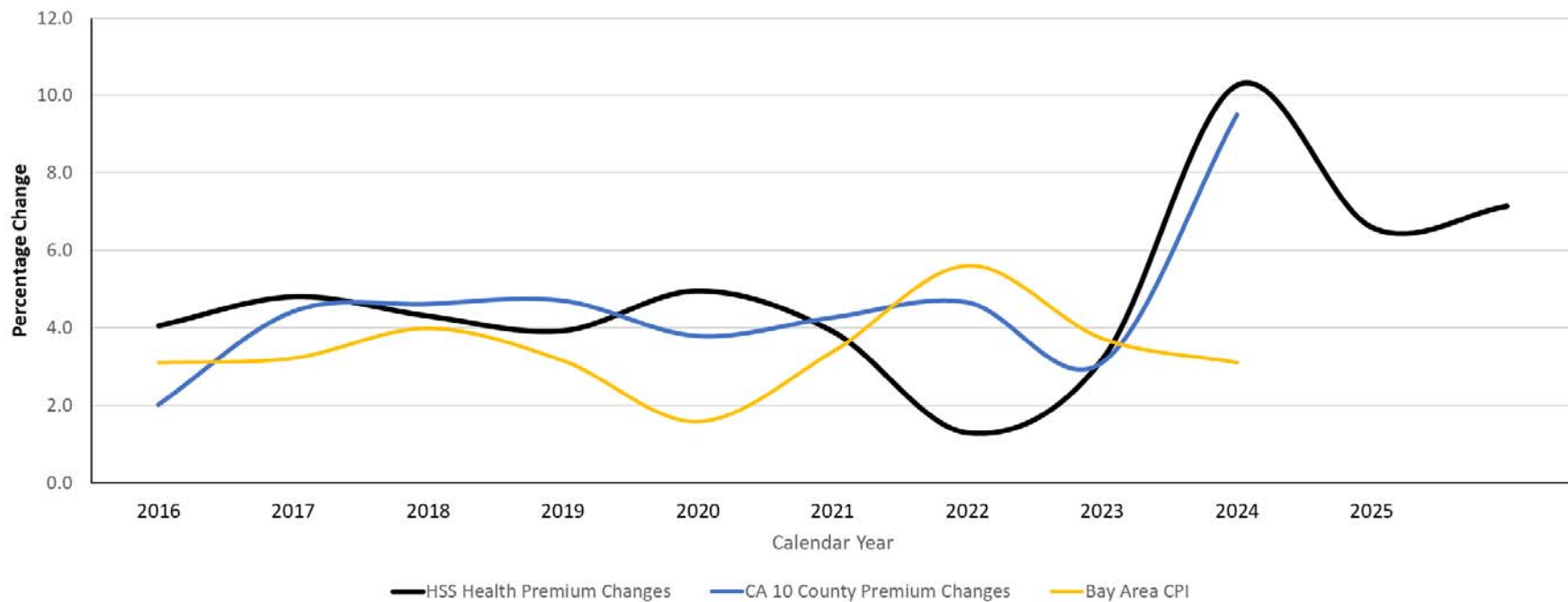
## Fiscal Outlook: Key Expenditures – Salaries & Benefit Costs





# Fiscal Outlook: Health Care Cost Escalation Settling at New 6-7% Levels

### Change in SFHSS Health Rates vs Benchmarks 2016 - 2024 (Calendar Year)

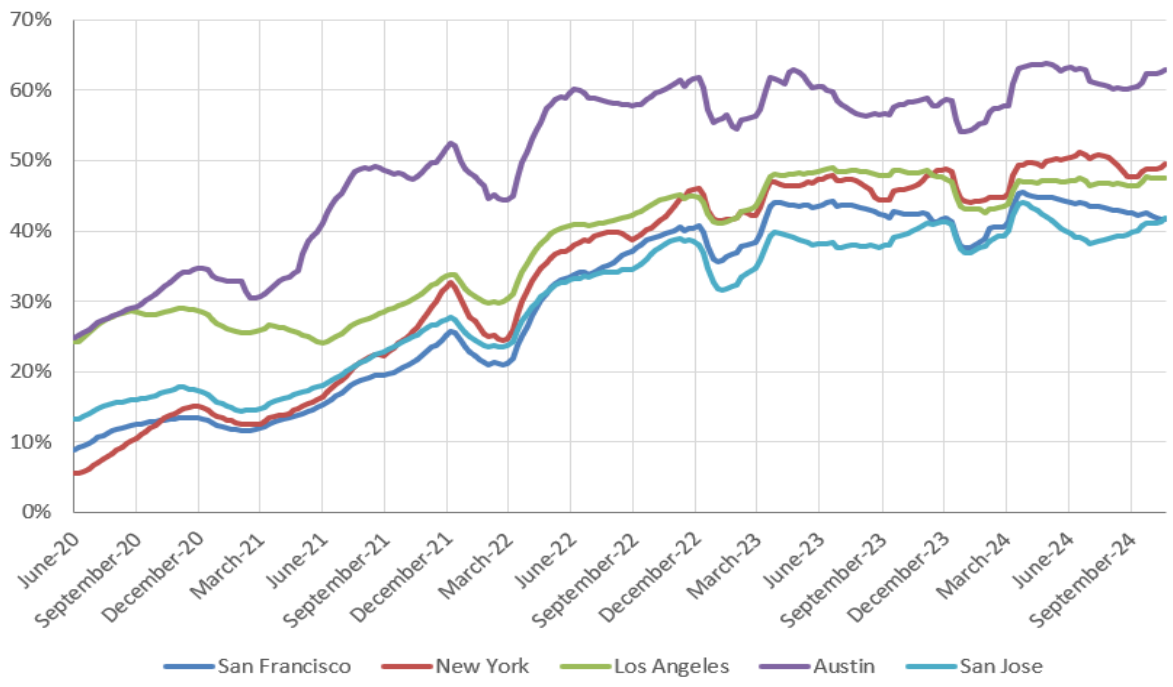




# Fiscal Outlook: Office Vacancies Remain Elevated

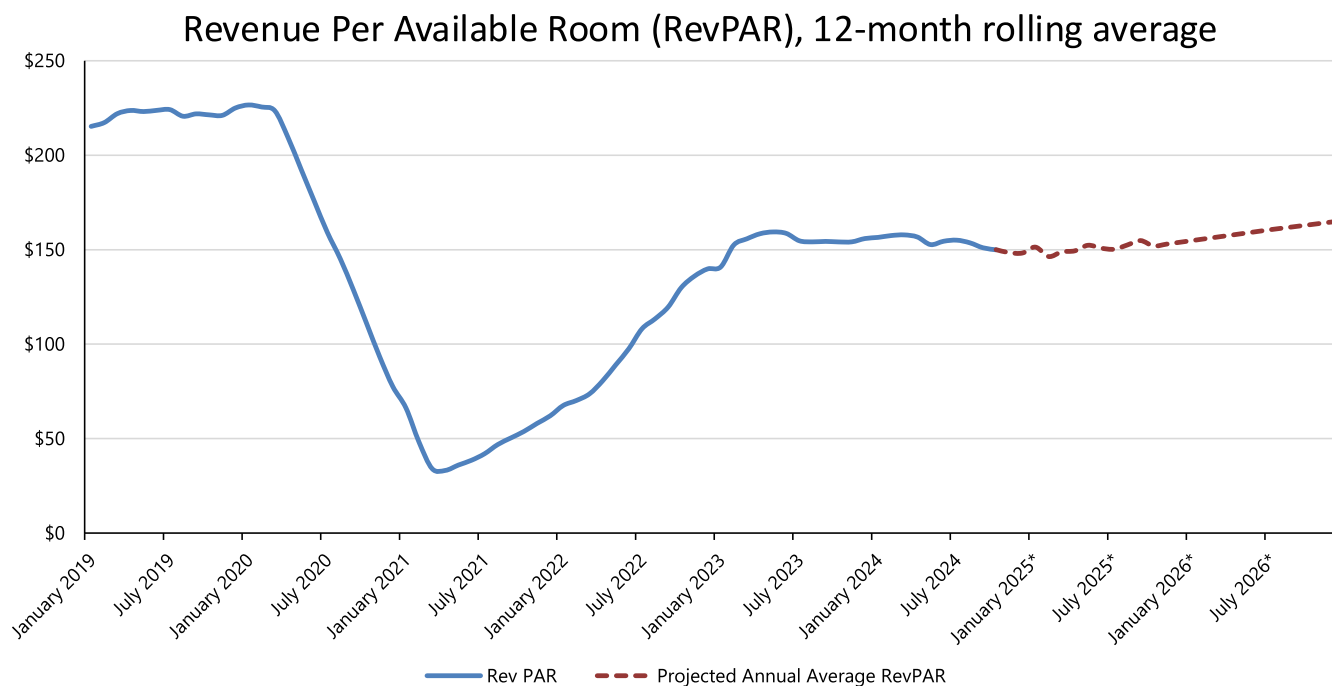
Remote work trends continue to affect the city's economy, as office vacancy rates impact sales tax revenue, hotel activity and convention activity

Physical Attendance in Offices vs. 2019: San Francisco and Comparable Metros (12-week Moving Average)





# Fiscal Outlook: Hospitality Industry Recovery is Slowing



Source: FY 2017-18 to FY 2023-24: STR and SF Travel. FY 2025-2026 to FY 2029-2030: Controller's Office





# Mayor's Priorities & Department Budget Instructions



## Mayor's Priorities

- Maintaining core city services, including public safety and clean streets
- Continue significant progress decreasing unsheltered homelessness; ensuring effective mental health treatment
- Propose opportunities to improve operational efficiency in service delivery and reporting across all areas of City services



## Budget Instructions: For Departments

Overall:

- **Permanently reduce General Fund spending by 15% beginning in FY 25-26**
- **Assess CBO grant allocations for efficiency.** Only fund community-based organizations that demonstrate strong outcomes and cost-effectiveness, focused on direct service to clients
- **Re-examine all contractual services and non-personnel** expenditures
- **Eliminate vacancies, do not add new FTEs.** Hire only for core department functions
- **Consider hiring freezes.** Layoffs are not preferred, but if necessary to meet target, please identify specifics in budget submission



## Budget Instructions: For Departments (continued)

Year Two only:

- **Reorganize to eliminate redundancy.** MBO will work with departments to identify programs for Year Two consolidation
- **Update nonprofit COLA (CODB) from Base to reflect CPI** (revise from 3% down to 2.4%) in Year Two



## Budget Instructions: For Departments (continued)

Other:

- **Do not book travel.** Effective 12/15/24, City-funded overnight and/or air travel is prohibited unless required by an outside funder or third-party agreement. MBO will be monitoring all travel expenditures monthly
- **Prepare grant performance data.** During Mayor phase, MBO may request detailed program- and grant-level performance data for all existing grants to CBOs



## Budget Instructions: Reminders

- Non-General Fund departments must balance their own budgets
- Budget transparency legislation requires 1-2 public meetings before February 14



## Budget Instructions: Calendar

|                          |  |
|--------------------------|--|
| December 2024            | Five Year Financial Plan Update (Joint Report)               |
| January 17, 2025         | Capital and COIT budget requests due                         |
| February 2025            | Controller's 6-Month Report                                  |
| <b>February 21, 2025</b> | <b>Department budget submissions due</b>                     |
| March 2025               | March Update to the Joint Report                             |
| May 2025                 | Controller's 9-Month Report; Governor's May Revise           |
| June 1, 2025             | Mayor proposes a balanced budget to the Board of Supervisors |
| June 2025                | Budget and Appropriations Committee hearings                 |



# Thank you