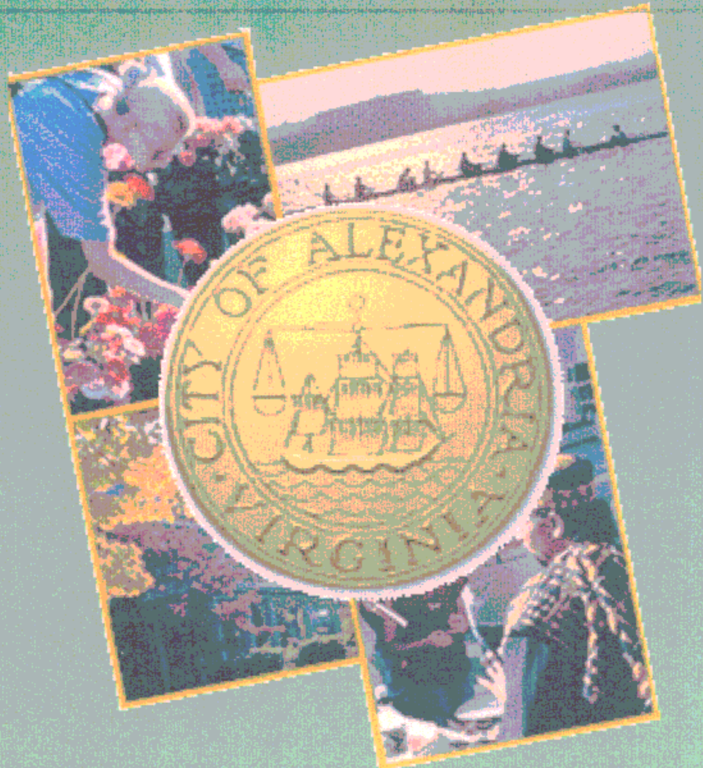
City of Alexandria

Financial Issues

City Council Retreat

October 26, 2002

Economic and Revenue Outlook



City Council Retreat

October 26, 2002

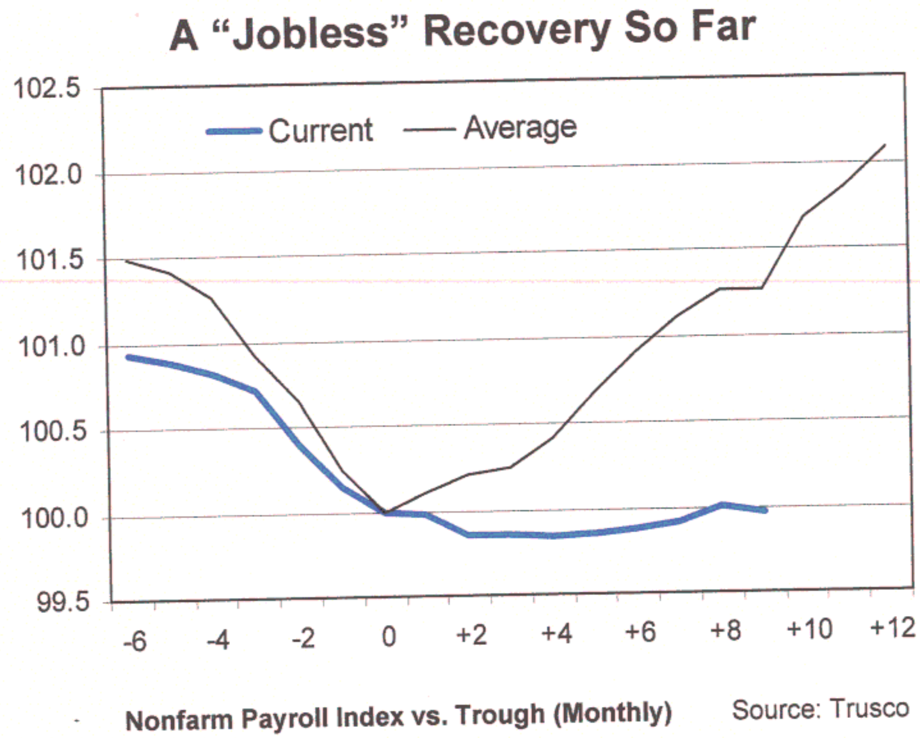
Economy - National

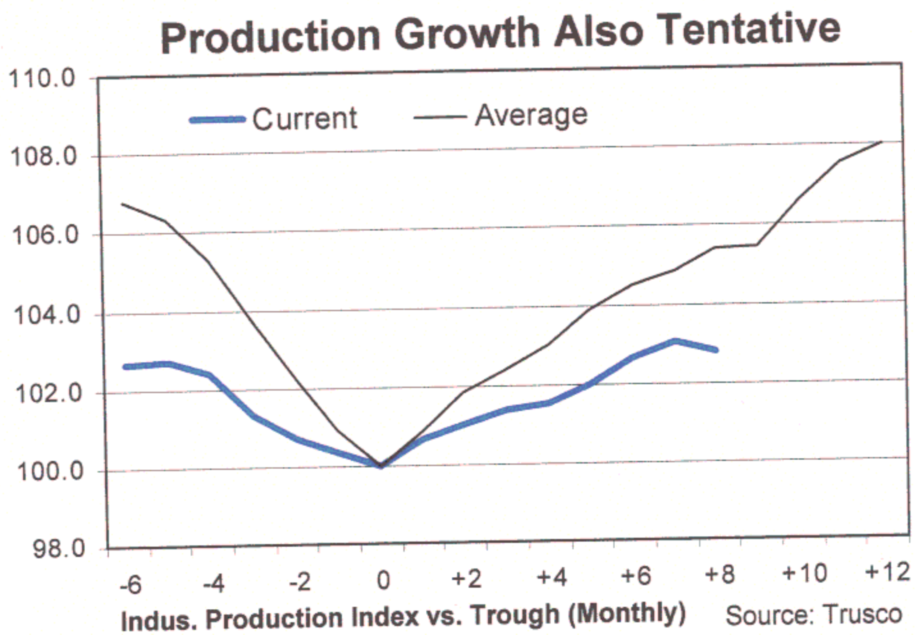
- Deflation/stagnation/recovery?
- Unfinished double dip recession?
- Prior consensus prediction of recovery in summer of 2002 incorrect
- Disagreement on economy's direction

Economy - National

- Uncertainty related to war concerns
- Consumer confidence down
- Retail spending dropped in September
- Impact of $7 trillion in stock market losses
- Discretionary spending impact (tourism, consumer goods, vehicles)

Recovery Monitor: A Slower Than Average Pace

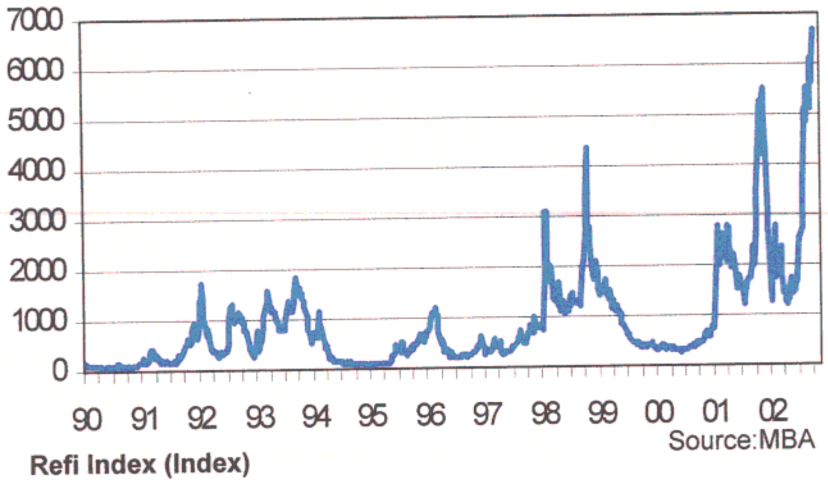




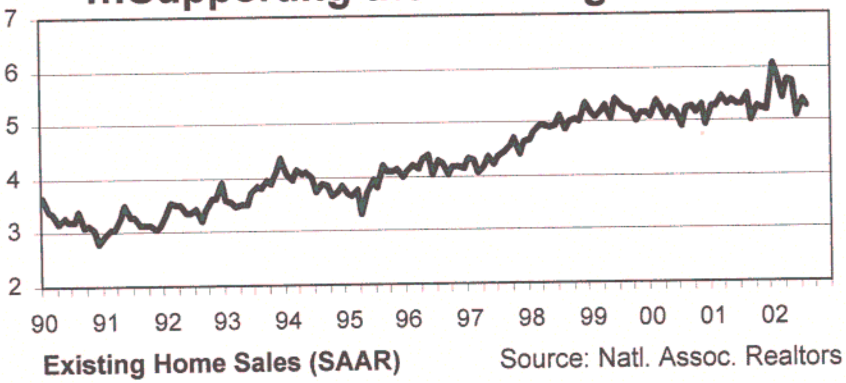
- Though not yet "official", the current recovery started near the beginning of the year. These charts compare the pace of the current recovery with that of the past 5 recoveries, using "0" and "100" as the end of the recession. The chart at left shows that businesses have been much more reluctant to hire in the current recovery, which tends to restrain income growth and confidence.

- The current recovery has also seen slower-than-average growth in industrial production. Some of the blame can be traced to caution and a lack of pricing power for many companies. Another reason may be that auto output, the largest piece of consumer durable goods production, did not experience a typical recession downturn.

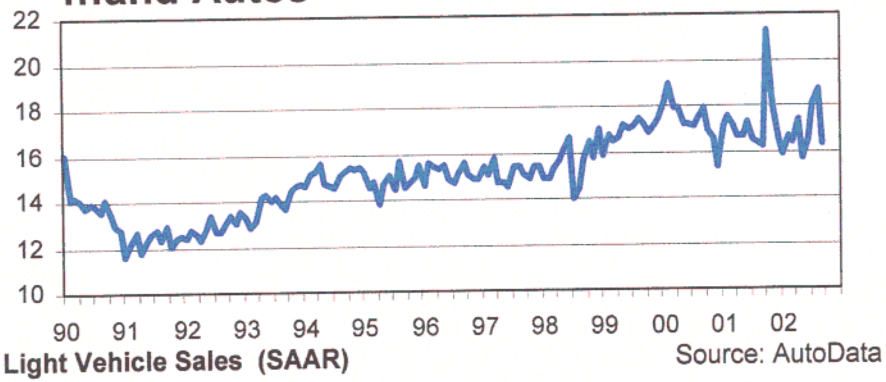
Low Rates Prompted Surge in Refinancing...



...Supporting the Housing Market...



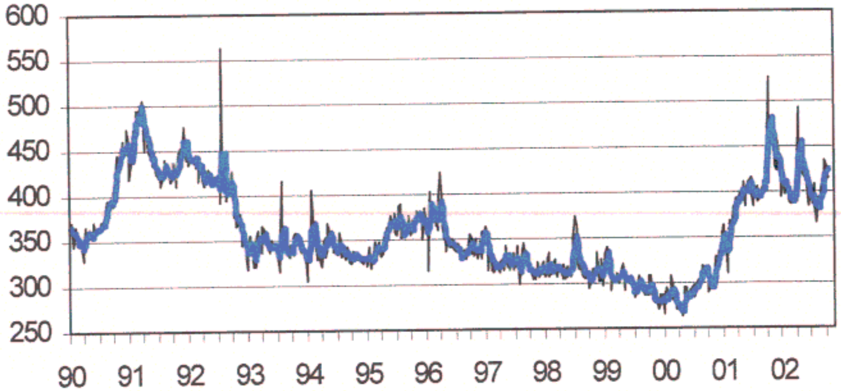
...and Autos



Stimulus to Consumers Supports Growth...

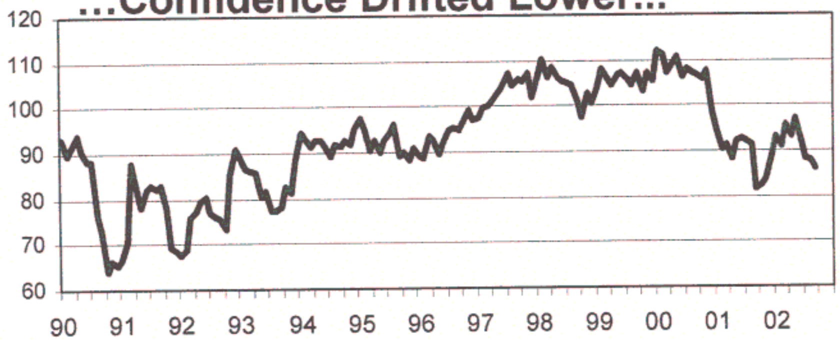
- Historically low mortgage rates have spurred a record level of home mortgage refinancing. This has allowed many consumers to either lower monthly payments, extract the equity in their homes, or both.
- The low mortgage rates have also supported the housing market since 1999 and throughout the recession last year. While this high level of home sales can be maintained by falling rates, the housing market is unlikely to experience a typical cyclical surge in the months ahead.
- Another beneficiary of lower rates and refinancing has been auto sales, which additionally have been spurred by attractive financing offers. Like housing, however, autos did not experience a recession, and may have limited upside.

Initial Jobless Claims Increased...



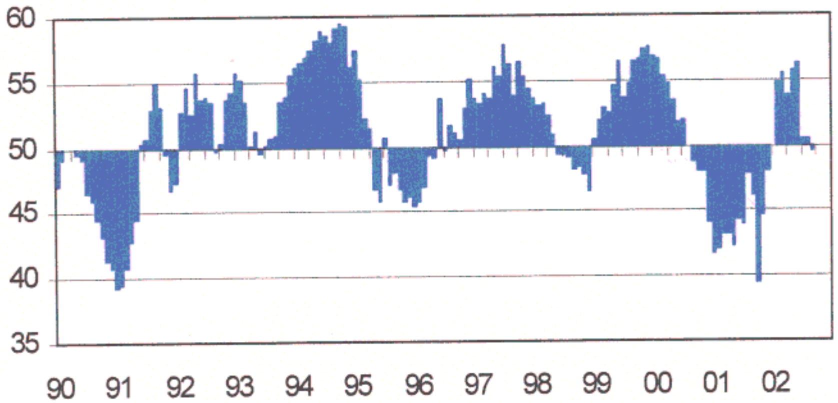
Initial Claims (Weekly w/ 4-Wk Avg.) Source:BLS

...Confidence Drifted Lower...



Consumer Sentiment (Level) Source:U of Michigan

...and Manufacturing Growth Eased



Inst. Purchasing Managers Index Source: ISM

...but Recent Weakness Fuels Doubt of Sustainability

- With only modest job growth so far in this recovery, the recent rise in jobless claims has raised fears of another round of corporate layoffs. However the increase is well below the peak of a year ago.
- Sluggish job growth, the threat of war and a continued weak stock market diminished consumer confidence, though it remains above the recession low from last year.
- Manufacturing momentum has also slowed recently following seven monthly increases. However, this slowing may be more of a reaction to the second quarter slowdown in consumer spending rather than anticipation of future weakness.

Economy - Regional

- Washington, D.C. area job losses
- Unemployment increased
- Office vacancies increased
  - D.C. area = 7.3% to 12.2%
  - Northern VA = 8.8% to 15.9%
  - Tysons to Loudoun = 18.8% to 22.3%

Economy - Regional

- Dot.com and telecom economic fuel of consumer and business spending gone
- Federal security and defense spending increasing
- 4.1% federal pay adjustment for civilian and military proposed
- Area diversified, but no real growth

Economy - Regional

- Tourism and business travel decreased
- Regional net loss in jobs
- New construction starts lower
- Housing supply/demand closer
- Commercial and residential real estate values peaking as an investment class

The Wall Street Journal

THURSDAY, OCTOBER 10, 2002 D1

Time to Cash Out Of Real Estate, Too?

Pros Start to Shed Property Holdings, Fearing A Correction; Timing When to Sell the House

By Ray A. Smith

SOME OF THE smart money is moving out of real estate.

With stocks plunging, investors have poured billions of dollars into properties over the past year, gobbling up real-estate stocks and mutual funds or buying rental units. So far this year, some $3.46 billion have flowed into real-estate mutual funds, up from $302 million in the year-earlier period, according to AMG Data Services.

Now, however, there are signs that the run might be over. Rents are dropping for office space, and building prices are likely to begin sliding soon. After two years of increases, returns on real-estate investment trusts fell 9% in the third quarter, according to Morgan Stanley.

Some money managers and pension plans have seen enough. They are lowering their exposure to real estate. For individuals, financial planners are recommending cutting holdings to about 5% to 10% of your total assets, not including your house. That's down from recommended holdings of as much as 15% earlier in the year.

Armada Small-Cap Value Fund in Cleveland, which has some $800 million under management, has trimmed its REIT allocation to 9% from 15%, says portfolio manager Dan Bandi. Instead, the fund is buying stocks of basic material makers, such as paper or chemical companies—that tend to benefit first in an economic cycle. "We looked at relative valuations and who would benefit from a strengthening economy, and we thought that would be cyclicals as opposed to the REITs," he says.

Peter Doyle, chief investment strategist of Kinetics Mutual Funds, in White Plains, N.Y., says he recently sold some of his office REIT holdings such as **Vornado Realty Trust** and **SL Green Realty** over concerns about the office market in the New York area. His rationale: Financial-services companies that occupy much of the office space in New York are laying off employees, and "ultimately, that will have ramifications for the REITs that are the landlords."

The widely held Teachers Insurance and Annuity Association-College Retirement Equities Fund, or TIAA-CREF, also recently trimmed its pension system's holdings in real-estate securities to $900 million from $1.05 billion at the beginning of the year.

Real estate generally tracks the performance of the economy, and the broad, continuing weakness is undercutting demand for space. A case in point is the office market, where the vacancy rate hit 15.7% recently, its highest level since 1993, according to Reis, a research firm.

On top of that, demand for real estate has been pumped up by temporary factors such as histori-

Please Turn to Page D6, Column 4

What to Do

Concerned you have too much riding on real estate? Here are some guidelines.

- The current recommended allocation for people who hold real-estate investments in their portfolios is 5% to 10% vs. 10% to 15% earlier in the year (excluding your home).
- Investment managers are selling apartment and office REITs, but holding mall REITs.
- If you are thinking of selling a home, it may be a good time. Price increases have put homes out of reach for many, which could weaken demand.

Economy - City

- City economy stable for now, but future uncertain
- Not back to pre 9/11 economic status
- Rates of growth or decline in question

Economy - City

- Key economic statistics (CY)

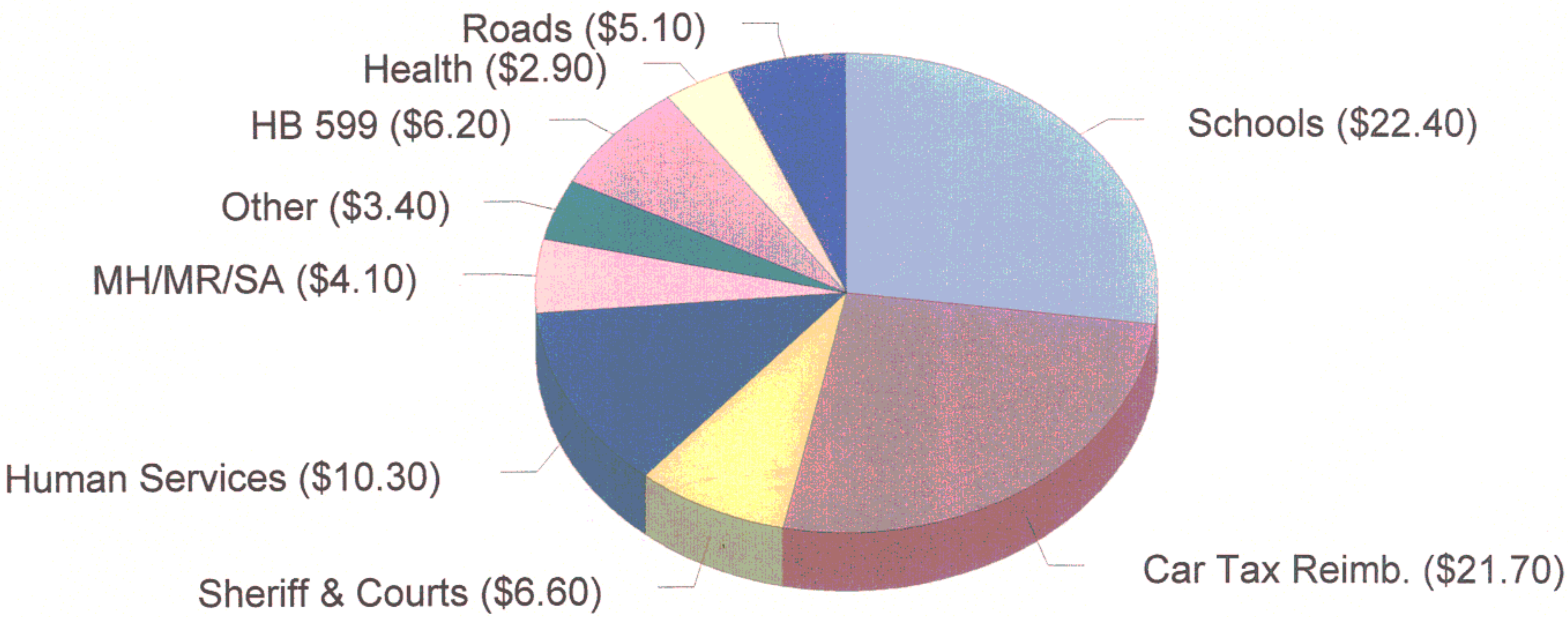
	2nd Qtr 01	1st Qtr 02	2nd Qtr 02
Office Vacancy	7.6%	12.1%	11.0%
Unemployment	2.3%	3.9%	3.6%
Hotel Occupancy	83.5%	48.4%	78.3%
Residential Construction	1,546 (4th Qtr)	294	223

Economy - City

- Home sales down 10% in 2002
- Unsold homes increasing
- Apartment vacancies increasing
- Drop in discretionary spending likely
- Commercial construction starts low

City of Alexandria: State Budget

FY 2003 All Funds: $82.7 Million



State Revenue Changes FY 2003

Program	Existing State Appropriation	Estimated Reduction
1. HB 599	$6,129,000	$275,805
2. CSB	$3,838,685	$383,868
3. Commonwealth's Attorney	$848,000	$59,360
4. Finance	$559,000	$61,490
5. Clerk of Courts	$839,000	$92,290
6. Social Services	$4,081,700	$40,817
7. Voter Registration	$66,000	$4,800
8. Aging	$171,900	$18,910
9. Arlandria Clinic	$112,500	$16,875
10. Library	$240,000	$37,000
11. NVDH (Detention) State Block Grant	$1,561,950	$234,293
12. Project Discovery	$70,000	$10,500
13. SBDC State funds	$23,000	$23,000
14. Rental Vehicle Taxes	$26,000	$2,600
15. Lloyd House	$28,371	$4,256
16. Fort Ward	$28,371	$4,256
17. Hydrilla	$14,185	$2,128
Estimated Total Reduction	**(as of 10/23/02)**	**$1,272,248**

State Revenues

- Options to manage losses:

  1. Backfill 100% or less
     - from contingent reserve?
     - from FY03 expenditure reductions?
     - combination of above?
     - prioritization of backfill

  2. No backfill of losses with local funds

Revenue Budget

- FY 2003 and FY 2004 revenue uncertain
- Personal property
  Actual = +6% vehicles, -3% business equipment
  Budget = +4% vehicles, +2% business equipment

The Wall Street Journal

How Detroit Is Ruining Your Car's Value

Zero-Percent Deals Wreak Havoc on Resale Prices; The Good News: $8,300 for a 2000 Ford Taurus

By KAREN LUNDEGAARD

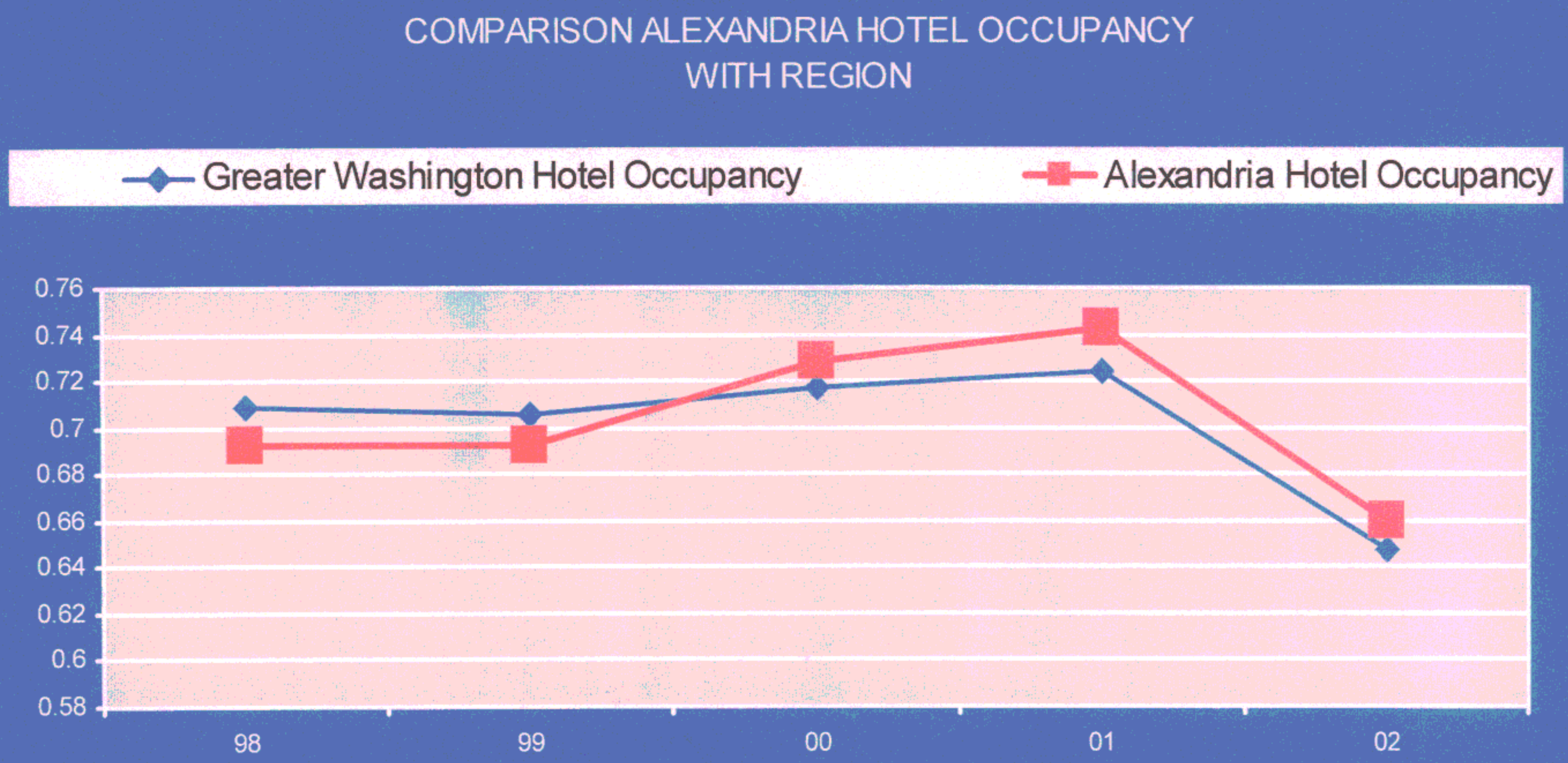
THERE'S A LITTLE-NOTED downside to the slew of financing incentives that Detroit is using to keep car sales humming: The enticing deals are triggering sharp declines in the value of cars the minute they drive off the lot.

One reason: Millions of Americans are snapping up new cars, which is increasing the glut of used cars on the market and driving their values down. In addition, the incentives themselves are effectively slashing the prices on new cars, which are a key factor in determining resale values. That also shrinks the value of earlier models already on the road.

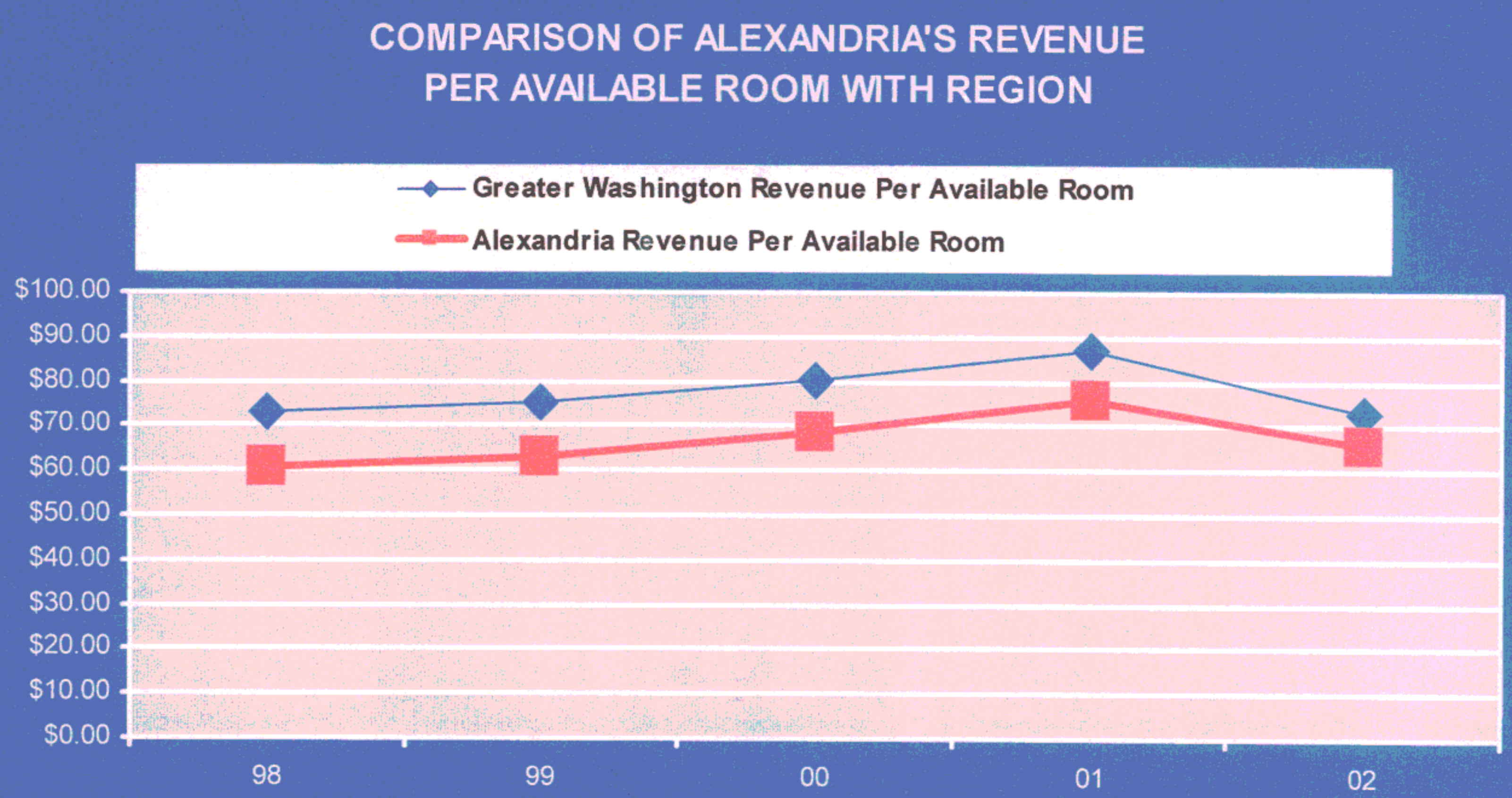
One case in point is the 2000 Ford Taurus SE, which had a sticker price of $19,440 but now is worth only about $8,300.

For shoppers, it's a very good time to buy many kinds of used cars. Many of the best used-car deals are on larger SUVs and smaller cars because they have been so heavily discounted. The typical two-year-old Chevy Suburban C1500, with a $26,421 sticker price, now fetches only $15,404 at trade-in, estimates Edmunds.com, a Santa Monica, Calif., auto-information company. That's $1,400 less than the resale value of the 1998 model at the end of 2000.

Hotel Occupancy



Hotel Rev PAR



Revenue Budget

- FY 2003 revenue assumptions too high?
- Retail Sales up 3%?
- Restaurant Meals up 4%?
- Transient Occupancy up 12%?
- Short Term Investment Rate not at 2.6%

Real Estate Tax Base: CY 2002

- + 11.2% overall increase
- + 9.0% reassessment
- + 2.2% new growth
- + 15.3% single family
- + 17.2% condominium
- + 1.6% commercial

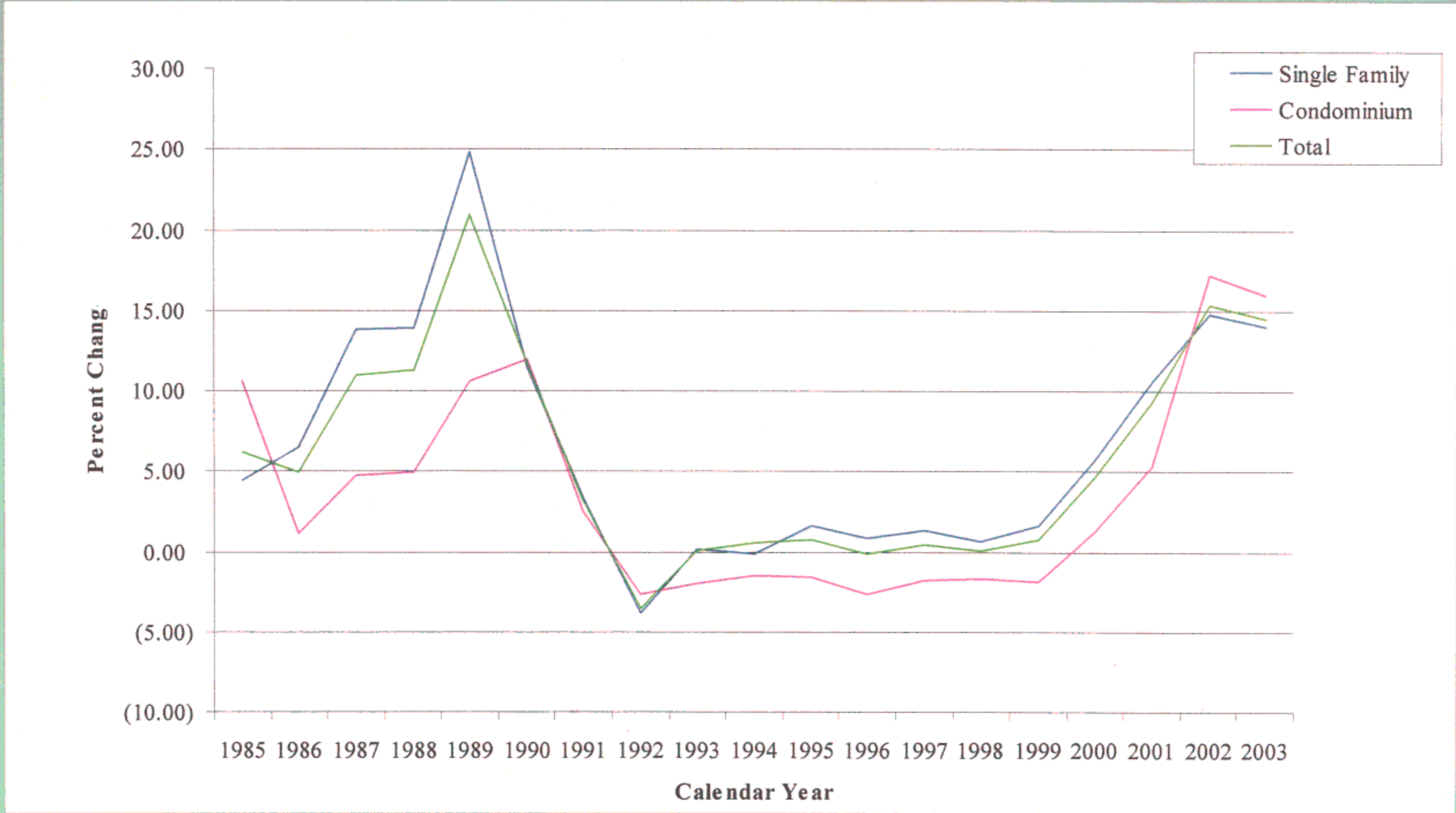
Real Estate Estimates: CY 2003

- + 11.5% overall increase
- + 9.0% reassessment
- + 2.5% new growth (primarily PTO)
- + 14% single family
- + 16% condominium
- + 5% commercial

Real Estate Trends

- Average residential sales prices up 11.6% to $276,798, for first nine months
- Low mortgage interest rates
- Residential sales volume down 10%
- City market share down 11.6%
- Inventory up 50% in Northern Virginia

Residential Home Value Changes from 1985 to 2003



Expenditure Challenges In FY 2004 and Beyond

Operating Expenditures
And
Capital Improvement Program

City Council Retreat, October 26, 2002

FY 2004 Budget Issues

- City step increase: $ 3.0 million
- Local CPI-U at 2.3%
- City COLA: @ 2.3% = $3.7 million
- Health Insurance increase to $1.5 to $2.0 million
- VRS: prior promise of no rate increase
- City operating budget increase could total over $9 million
- Debt Service (now $17.7 million) increases $1 to $3 million depending on CIP projects and timing
- Significant debt service increase in FY 2005 and beyond

FY 2004 Budget Issues

- Guideline to Departments funds merits only
- Non-Personnel at 0% results in up to $2 million savings
- Possible demands beyond guidelines
  - Backfill state cuts
  - Police staffing
  - Recreation needs as result of study
  - Affordable housing
  - School compensation
  - New capital projects

FY 2003 School Operating Budget

- School step increase = $1.9 million
- School COLA @ 2.3% = $2.8 million
- Restructured Compensation Discussions
  - Increase to 190 school days
  - New pay scales/benefits (+ $2.9 million)
- Health Insurance (+ $1.2 million)
- Performance Evaluation Program
- State Aid reductions?
- School budget increase could total $10.0 million

School Enrollment

- 11,167 = FY 2001
- 11,104 = FY 2002
- 11,311 = budgeted in FY 2003
- 10,979 = actual (9/30/02)

Conclusion

Major budget challenge ($ in millions)

City operating	$9
City initiatives	TBD
WMATA	2
School operating	10
Debt service	3
Cash capital	TBD
Total:	$24 million

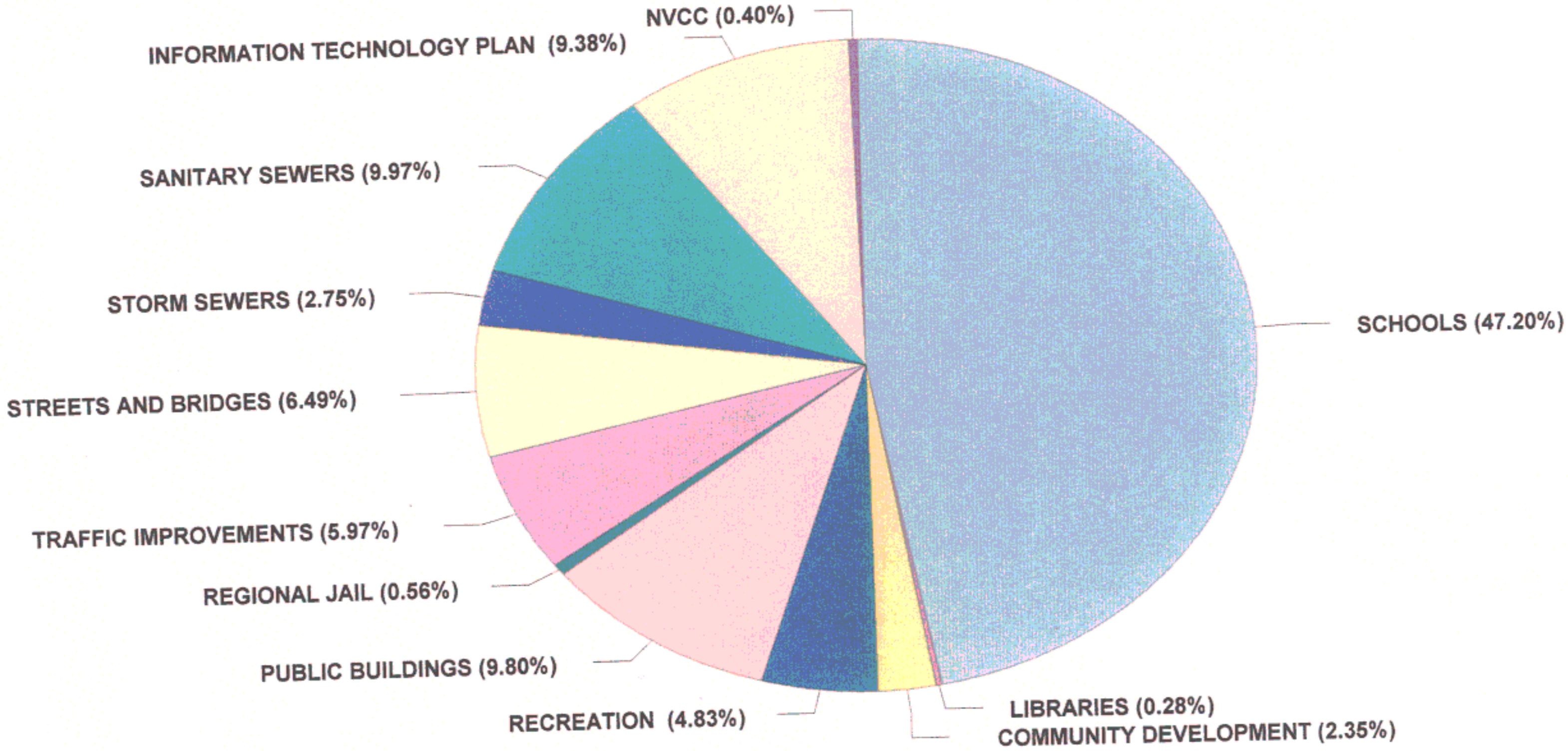
Conclusion

- $24 million represents need for more than a 7% revenue increase
- Revenue increase of about 4% likely
  - Leaves a 3% or $10 million gap
- Assumes no change in real estate tax rate
- State aid reductions will widen gap
- Fees for refuse and sewer service being studied in relation to cost recovery
- Prioritization to fund essential services, deferring many initiatives necessary
- Some services or program areas will be cut back

Current Capital Improvement Program (FY 03-FY 08)

- Totals $183.8 million in local funding
- $15 million in cash capital in FY 04
- Increasing cash capital
- $55 million in bond issuance

Current Capital Improvement Program FY 2003 – 2008



Updated CIP projects for consideration

- School Capital ($ in millions)
  - Funding for six years now at $86.7
  - Minnie Howard: $13.2 (increase of $6.3)
  - T.C. Williams: $74.5 (increase of $45.7)
  - Elementary expansion assumed dropped: $20.9
  - Funding for all projects estimated at $122.9 through FY 2008
  - This represents a $<u>36.2</u> increase
  - FY 2009 projects to be identified

Project Overview

City of Alexandria

Public Safety Center and

New Police Department Facility

Project Goals

- Alleviate overcrowded space conditions at the current Public Safety Center for Police, Sheriff and Magistrate
- Address and correct slab settlement conditions
- Plan for and address future space needs of the Police Department, Office of Sheriff and Magistrate

Existing Public Safety Center

- 1987 – Public Safety Center opens

Police Department

	1987	2002 Current	2014 Projected
Required Space (Useable Square Feet)	39,636	87,172	99,770
Employees (not including volunteers)	335	430	560

Sheriff

	1987	2002	2014
Required Space (Useable Square Feet)	14,453	30,936	N/A
Employees (not including volunteers)	155	196	N/A

Magistrate

	1987	2002	2014
Required Space (Useable Square Feet)	857	921	N/A
Employees (not including volunteers)	7	7	N/A

External Impacts to PSC Location

- Wilson Bridge Ramp Construction
  - Extreme Negative/Disruptive Impact
    - Parking Space Losses
    - Access During Business Day
- Eisenhower Valley Development
  - Increased Access Difficulty
    - New Office Development Traffic
    - Impact on Mill Road Parking

Public Safety Center
Interim Plan

- Acquire leased space for Police Department to temporarily address the space shortfall (12 to 14 month process)
- Begin slab settlement correction work after temporary leased space for Police Department is occupied

Planning for Future Police Department Space Needs for 2014

Planning Year – 2014

- Space Analysis reveals a need for:
  - 99,770 square feet of useable space. This represents a shortfall of 60,134 square feet in relation to the current space of 39,636 square feet
- Parking Analysis reveals a need for:
  - 782 spaces for fleet and employees and 50 spaces for visitors totaling 831 spaces—a shortfall of 449 in relation to the current parking of 382

Project Assumptions

Proposed New Facility

- People
  - Current staffing level – 466 total (430 employees + 36 volunteers)
  - Projected staffing level – 606 total (560 employees + 46 volunteers)
- Building
  - Four Story Masonry Structure
  - Gross Area - 108,445 square feet (Useable Area – 99,770 square feet)
- Parking
  - Parking on Lower Level of Building (82 vehicles)
  - Four story parking structure (700 vehicles)
  - 50 vehicles on the surface for visitors
- Site
  - Total Site Area – 6 Acres
    - Building, Garage & Parking Area – 117,689
    - 200 foot Security Zone – 76,148 sf
    - Access Roads & Green Space – 39,422 sf

Project Budget – Option 1

All figures are in millions

Activity	FY03	FY04	FY05	FY06	FY07	FY08	Total
New Facility							
Site Selection/Acquisition	$0.09	$16.61					
Design		$2.05	$2.10	$.05			
Construction			$.50	$41.45	$.25	$.20	
Move					$.10	$.20	
Subtotal	**$.09**	**$18.66**	**$2.6**	**$41.50**	**$.35**	**$.40**	**$63.6**
Temporary Relocation							
Design	$0.05	$0.05					
Construction		$0.80					
Move		$.050					
Subtotal	**$.05**	**$0.90**					**$.95**
Slab Settlement & Repair							
Design			$0.10	$0.25	$0.23		
Construction					$0.03	$6.59	
Subtotal			**$0.10**	**$0.25**	**$0.26**	**$6.59**	**$7.2**
Total	**$0.14**	**$19.56**	**$2.70**	**$41.75**	**$0.61**	**$6.99**	**$71.75**

Grand Total **$71.75**

Project Budget – Option 2

All figures are millions

Activity	FY03	FY04	FY05	FY06	FY07	FY08	FY09	FY10	Total
New Facility									
Site Selection/Acquisition	$0.09	$16.61							
Design				$2.13	$2.19	$.05			
Construction					$.52	$43.12	$0.26	$0.21	
Move							$.11	$.21	
Subtotal	**$.09**	**$16.61**		**$2.13**	**$2.71**	**$43.17**	**$0.37**	**$0.42**	**$65.5**
Temporary Relocation									
Design	$0.05	$0.05							
Construction		$0.80							
Move		$.050							
Subtotal	**$.05**	**$0.90**							**$.95**
Slab Settlement & Repair									
Design		$0.34	$0.22						
Construction			$6.24						
Subtotal		**$0.34**	**$6.46**						**$6.80**
Total	**$0.14**	**$17.85**	**$6.46**	**$2.13**	**$2.71**	**$43.17**	**$0.37**	**$0.42**	**$73.25**

Grand Total $73.25

CIP Funding Challenges

($ in millions)

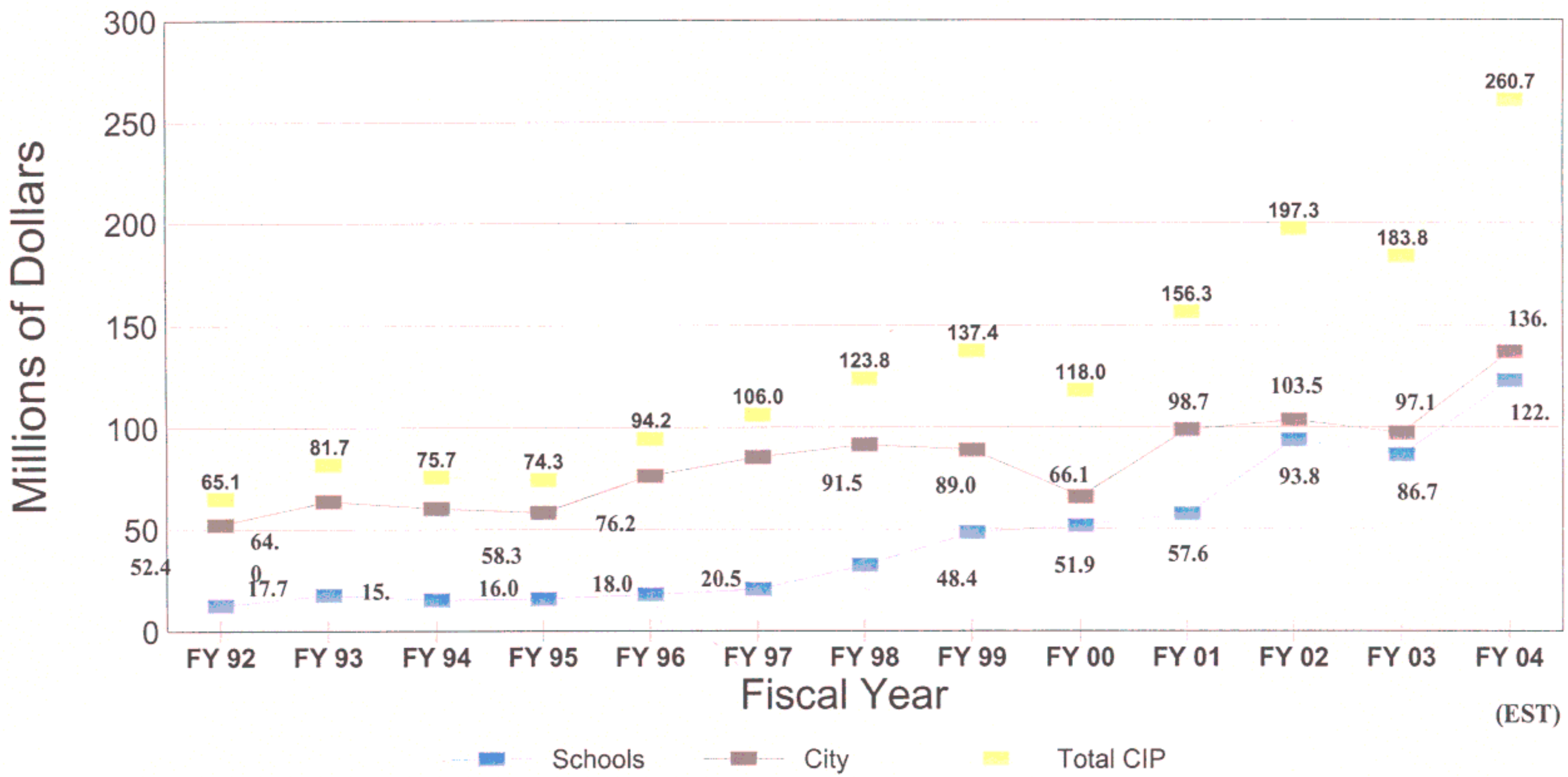
	FY 04	FY 05	FY 06	FY 07	FY 08	FY 09	Total
City-Current	**$22.5**	**$11.9**	**$10.5**	**$9.3**	**$7.5**	TBD	**$61.7**
Schools-Current	**20.8**	**25.0**	**13.6**	**4.4**	**3.3**	TBD	**67.1**
Schools-New	**18.4**	**14.1**	**19.5**	**3.8**	-	TBD	**55.8**
Public Safety Ctr- Reloc, New	**15.0***	**2.6**	**41.6**	**0.4**	**0.4**	-	**60.0**
Public Safety Ctr- Slab repair	-	**0.1**	**0.2**	**0.3**	**6.6**	-	**7.2**
City-New	TBD	TBD	TBD	TBD	TBD	TBD	TBD
WMATA-IRP	**0.3**	**0.6**	**1.3**	**0.6**	**(2.2)**	**8.3**	**8.9**
WMATA-SAP, SEP	TBD	TBD	TBD	TBD	TBD	TBD	TBD
Total:	**$77.0**	**$54.3**	**$86.7**	**$18.8**	**$15.6**	**$8.3**	**$260.7**

*** Reflects reallocation of $4.6 million previously funded for slab repair**

Historical CIP Funding

Total Local Funding – Approved Six-Year CIPs

Schools Compared to All Other Projects



Preparing the FY 04 to FY 09 CIP

- Project prioritization vital
- Deferral of some current and new projects may be necessary
- Capital funding limitations
- Impact of debt service on operating budget
- Impact on City financial policies