Forecasting the Financial Future for Virginia's Localities

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“Bear” Case for Economy

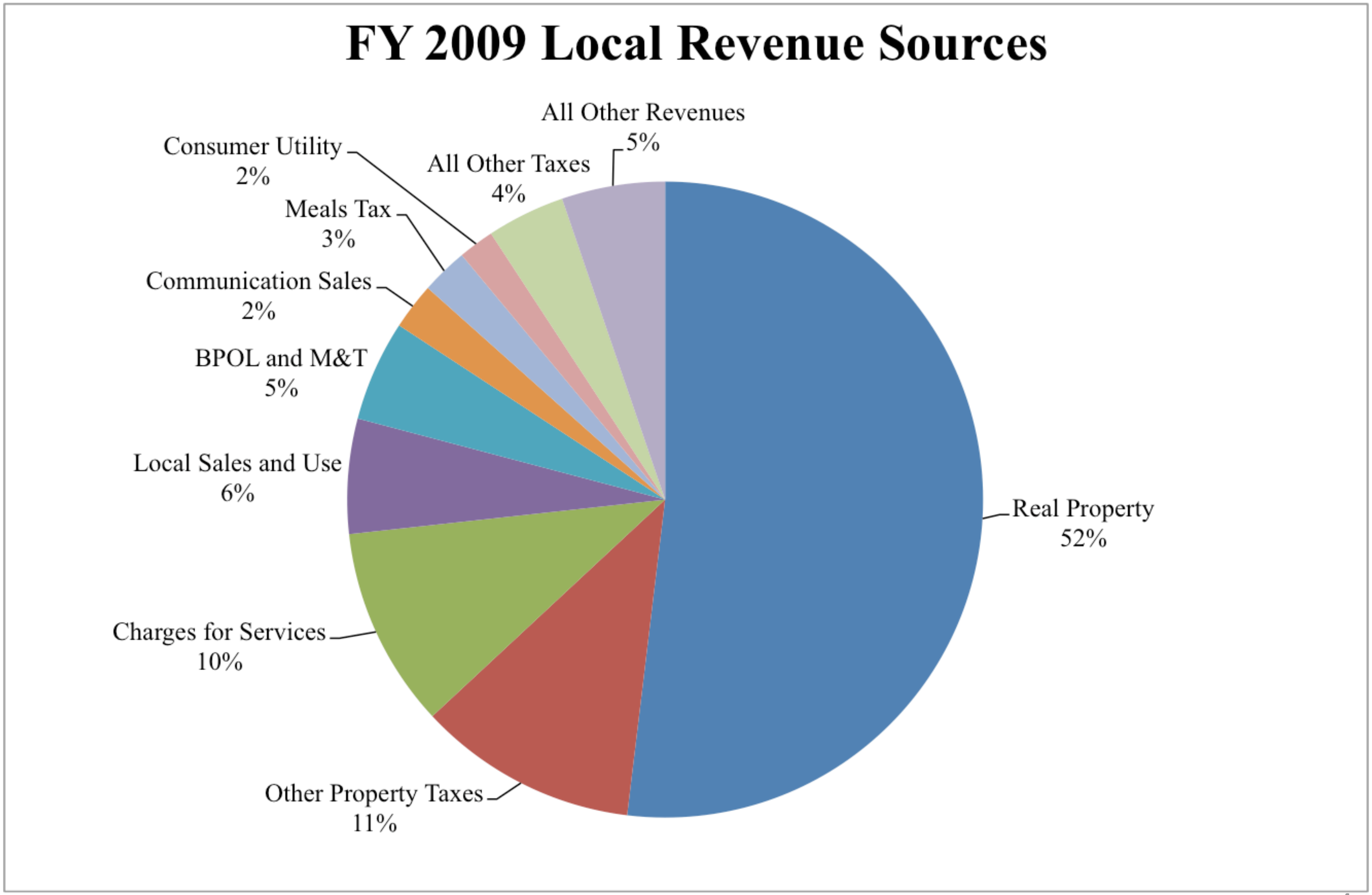
- Debt bubble has shifted from private to public sector.
- Waning federal stimulus, potentially rising federal taxes, increasing protectionism & regulation
- Anemic job growth
- Deflation risk
- Faltering real estate recovery
- Leading indicators may have peaked
- Confidence crisis

“Bull” Case for Economy

- Strong growth in emerging economies
- Low borrowing costs
- Pent-up demand?
- Credit markets on the mend
- Steep yield curve predicts no double-dip
- Healthy corporate profits, high productivity, and record high corporate cash
- Tame inflation

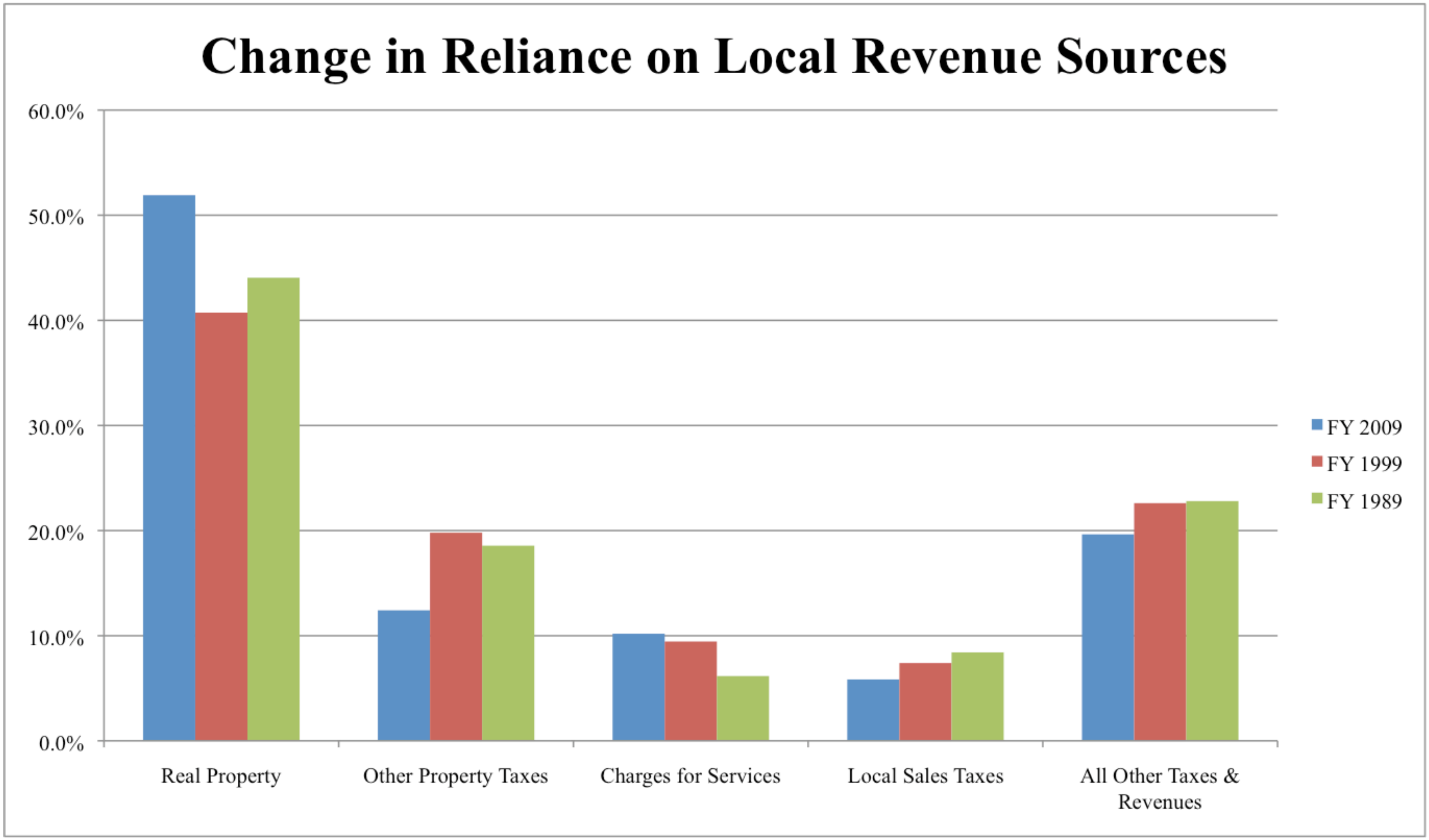
Local Revenue Sources

Locals depend heavily on real property taxes



Source: Auditor of Public Accounts Comparative Report of Revenues and Expenditures

Reliance on Real Property Revenues Has Grown Significantly



While Virginia Existing Home Prices *May* Have Bottomed in 2010.1Q …

Median Sales Price of Existing Single-Family Homes for Metropolitan Areas

(Thousands $)

Metropolitan Area	2007	2008	2009	2010.I	2010.II p
U.S.	$217.9	$196.6	$172.1	$166.4	$176.9
South	178.8	169.4	155.0	142.6	155.5
Richmond, VA	233.7	223.5	N/A	N/A	199.6
Hampton Roads Metro	226.8	220.0	210.0	195.0	210.0
Washington D.C. Metro	430.8	343.4	308.6	292.6	331.6

*All areas are metropolitan statistical areas (MSA) as defined by the US Office of Management and Budget as of 2004.

They include the named central city and surrounding areas. N/A Not Available p Preliminary

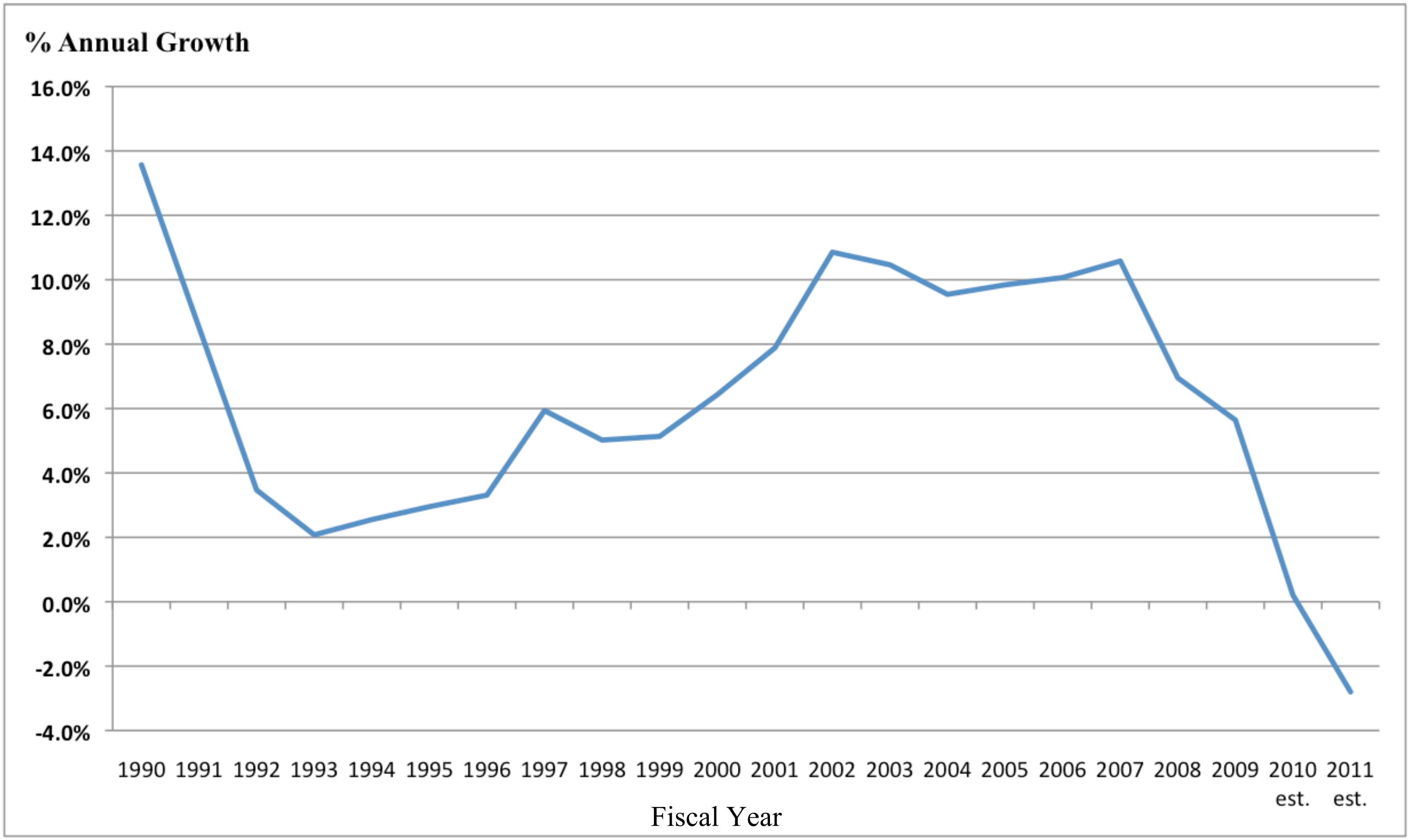
...Commercial Real Estate Still Soft

Virginia Commercial Real Estate Activity 1st Q 2010

Sales Volume Compared with Previous Quarter	-10%
Sales Volume Compared with Previous Year	-12%
Sales Prices Compared with Previous Quarter	-1%
Sales Prices Compared with Previous Year	-12%
Volume of New Construction Compared with Previous Quarter	-10%
Leasing Activity Compared with Previous Quarter	-1%
Rental Rates Compared with Previous Quarter	-7%

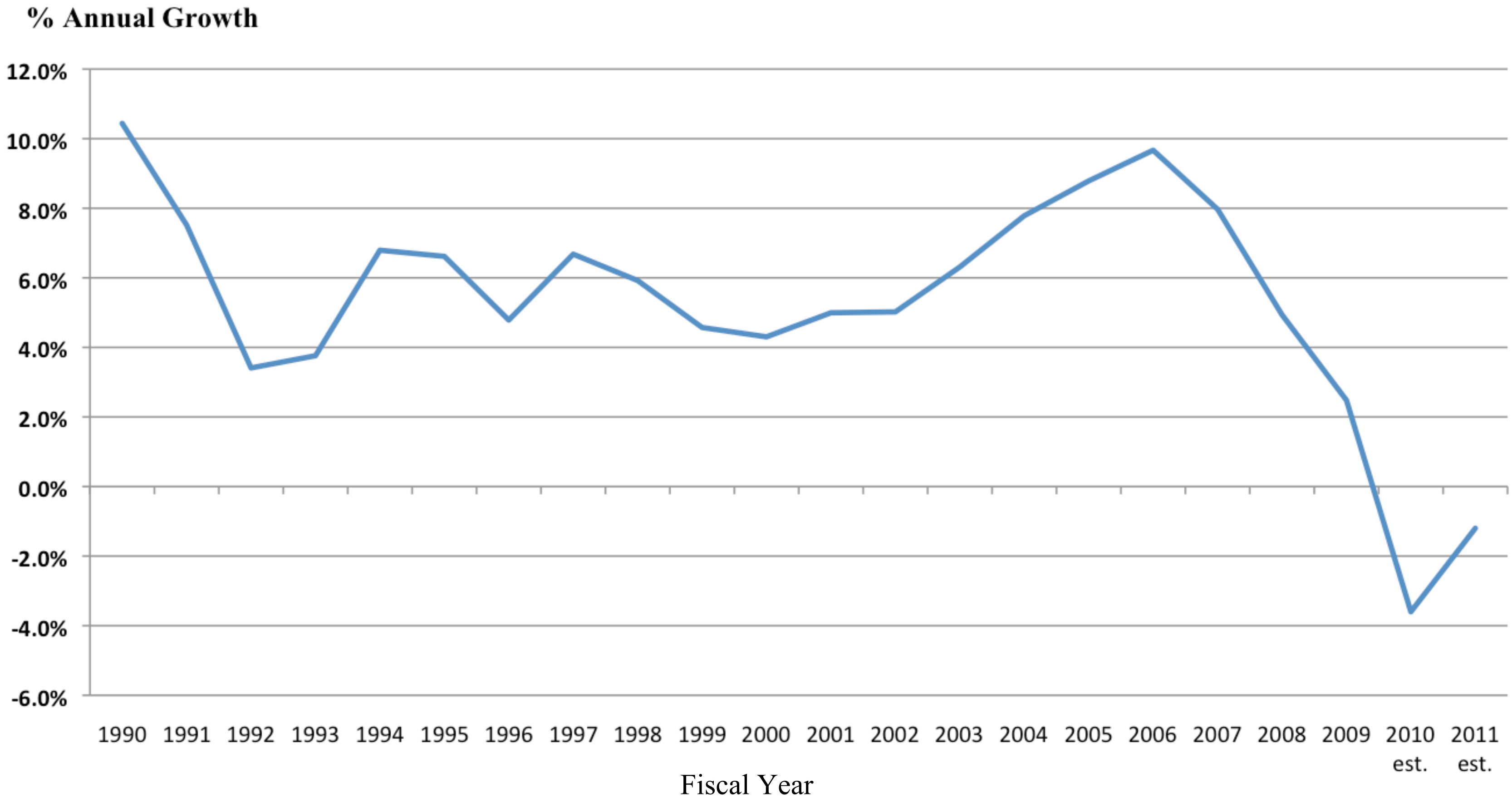
Commercial Real Estate QUARTERLY MARKET SURVEY, June 2010

Property Tax Revenues Expected to Decline At Least Through FY 2011



Growth in Total RE Assessed Values (106 localities surveyed):			**Growth in Total RE Revenues (109 localities surveyed):**	
2009 to 2010:	**-5.0%**		**FY2009 to FY2010:**	**0.2%**
			FY2010 to budgeted FY2011:	**-2.8%**

…Growth in Total Local Revenues Still Declining as Well

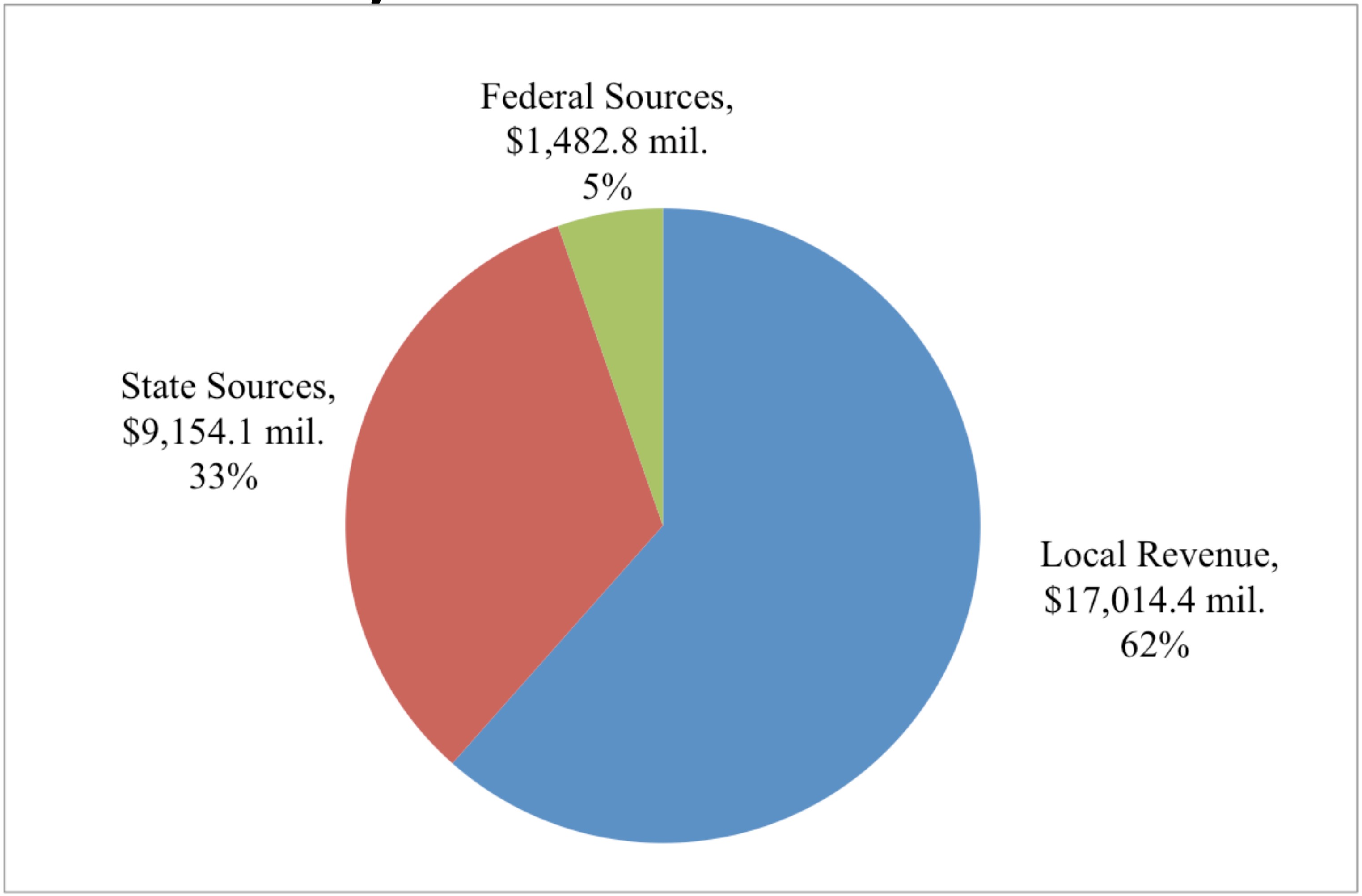


107 localities responding to VML/VACO survey:

FY2009 to FY2010: -3.6%

FY2010 to budgeted FY2011: -1.2%

State Sources Provided One-Third of Locality Revenues in FY 2009



Source: Auditor of Public Accounts Comparative Report

GF State Aid to Localities Has Decreased by $900 Mil. Since FY 2009

	FY 2009	FY 2010	FY 2011	FY 2012
Direct Aid to K-12 (1)	**$5,607.6**	**$5,354.0**	**$4,865.7**	**$4,903.1**
Health and Human Services	**$888.4**	**$878.7**	**$823.3**	**$813.7**
CSA	*$299.7*	*$279.2*	*$272.2*	*$274.0*
Community MH/MR Services	*$249.4*	*$256.5*	*$230.1*	*$230.1*
Local Social Services Staff	*$117.4*	*$117.4*	*$114.4*	*$111.4*
Community Health Programs	*$117.6*	*$116.9*	*$106.1*	*$105.0*
Welfare Services and Programs	*$104.3*	*$108.7*	*$100.5*	*$93.2*
Public Safety	**$734.3**	**$666.3**	**$671.6**	**$642.7**
Local Sheriffs Offices (2)	*$406.1*	*$366.6*	*$399.9*	*$387.4*
Local Police Depts HB 599	*$197.3*	*$180.8*	*$178.7*	*$160.0*
Local Jail Per diem	*$80.1*	*$68.1*	*$47.6*	*$49.9*
Financial Assistance for Juvenile Justice	*$50.8*	*$50.8*	*$45.4*	*$45.4*
Car Tax	**$950.0**	**$950.0**	**$950.0**	**$950.0**
Constitutional Officers	**$155.3**	**$142.2**	**$144.2**	**$144.2**
Local Government RCA	**($50.0)**	**($50.0)**	**($60.0)**	**($60.0)**
Total Local Aid	**$8,285.6**	**$7,941.2**	**$7,394.8**	**$7,393.7**

(1) includes $584.2 mil. for FY 10 and $126.4 for FY 11 in appropriated federal stimulus funding

(2) includes $109.5 mil. in appropriated federal stimulus funding for FY 10

Existing Spending Pressures Will Limit State Aid to Localities for Foreseeable Future

- Constitutional requirement to fill Rainy Day Fund.
  - Requires deposit of half of growth above previous six-year average GF revenue growth. Expect $200-300 million/year in deposits in FY 2014-2017 to restore fund.
- Continued 10% Medicaid growth rates (costs + utilization), plus new health care bill requirements in 2014 (additional Medicaid eligibility costs state $100's of millions /yr).
- VRS contributions for both teachers and state employees will have to be restored to actuarially sound levels. Plus, adopted budget calls for 10 year payback of prior cuts. Employer rates will significantly increase.
- Continued growth in future biennia debt service requirements.
- Other numerous pent-up demands for additional state agency funding.
- No appetite for general fund tax increases and additional revenue pressures for transportation first.

There Have Been Large Shifts in Virginia Employment Over the Last 10 Years

	June 2000 Employment	June 2010 Employment	Change	% Change
Total Nonfarm	3,557,400	3,674,400	117,000	3.3%
Natural Resources and Mining	11,500	9,700	(1,800)	-15.7%
Construction	214,600	182,600	(32,000)	-14.9%
Manufacturing	364,900	231,800	(133,100)	-36.5%
Trade, Transportation, and Utilities	648,100	623,300	(24,800)	-3.8%
Information	120,000	74,700	(45,300)	-37.8%
Finance	180,700	178,300	(2,400)	-1.3%
Professional and Business Services	575,200	643,400	68,200	11.9%
Educational and Health Services	330,700	460,000	129,300	39.1%
Leisure and Hospitality	317,700	366,900	49,200	15.5%
Other Services	162,200	197,700	35,500	21.9%
Government	632,000	706,000	74,000	11.7%
Federal	*158,700*	*180,600*	*21,900*	*13.8%*
State	*139,400*	*149,500*	*10,100*	*7.2%*
Local	*333,900*	*375,900*	*42,000*	*12.6%*

Source: Virginia Employment Commission

Where Are Jobs Coming Back?

	June 2009 Employment	June 2010 Employment	Change	1 Year % Change
Total Nonfarm	3,678,000	3,674,400	(3,600)	-0.1%
Natural Resources and Mining	10,100	9,700	(400)	-4.0%
Construction	192,100	182,600	(9,500)	-4.9%
Manufacturing	238,300	231,800	(6,500)	-2.7%
Trade, Transportation, Utilities	625,200	623,300	(1,900)	-0.3%
Information	81,800	74,700	(7,100)	-8.7%
Finance	181,800	178,300	(3,500)	-1.9%
Professional and Business Services	639,300	643,400	4,100	0.6%
Educational and Health Services	450,700	460,000	9,300	2.1%
Leisure and Hospitality	364,000	366,900	2,900	0.8%
Other Services	188,400	197,700	9,300	4.9%
Government	706,300	706,000	(300)	0.0%
Federal	166,200	180,600	14,400	8.7%
State	148,600	149,500	900	0.6%
Local	391,500	375,900	(15,600)	-4.0%

Localities Should Plan On Tough Budgets for Foreseeable Future

- Federal relief is waning.
- Do not expect meaningful increases in state aid for several biennia.
- While a double-dip recession is not likely, job growth and real estate recovery will likely be slow, therefore:
  - Slow increases in real estate assessments;
  - And slow growth in most other local taxes.