



HdL[®] Companies
TEXAS FORECAST
SALES TAX TRENDS AND
ECONOMIC DRIVERS

APRIL 2020

HdL provides relevant information and analyses on the economic forces affecting Texas' local government agencies. In addition, HdL's Revenue Enhancement and Economic Development Services help clients to maximize revenues.

HdL serves over 500 cities, counties and special districts in Texas and across the nation.



*Delivering Revenue, Insight and Efficiency
to Local Government Since 1983*

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2020 FORECAST

Summary

Swift reaction to the COVID-19 pandemic by government leaders, consumers, and businesses has caused a sudden and substantial decrease in spending on certain taxable goods and services. National and state responses to COVID-19, combined with uncertainty as to the duration and scope of related economic disruption, make revenue projections during this unprecedented time especially challenging. The Texas Comptroller does not expect to release updated tax revenue projections until mid-summer. Nonetheless, HdL understands assessing the potential impact on your jurisdiction's sales and use tax is vitally important and a priority consideration. HdL prepared the attached forecast that incorporates insights from respected publications, numerous industry-specific analysts, and HdL sales and use tax specialists. HdL will make available a sales and use tax assessment tool to allow you to combine insights from this consensus forecast, your jurisdiction's sales and use tax data, and input from those that know your community best --- you and your team, to project sales and use tax revenue for future reporting periods.

HdL Consensus Forecast

HdL's Consensus Forecast considers impacts of previous historic downturns, reports and projections from industry-specific analysts, economic studies, and updates from federal, state, and local leaders. As the COVID-19 pandemic is an unfolding, fluid event, HdL anticipates updating its Consensus Forecast over time as circumstances evolve and more definitive information becomes available.

This initial forecast assumes current social distancing strategies to flatten the curve of virus spread remain in place, site-specific containment strategies to reopen the Texas economy are implemented slowly, business and industry leaders work cooperatively to minimize supply chain disruptions, and federal, state, and local economic stimulus actions successfully deter deep recession. It considers marginal or overly-leveraged businesses will not survive a lengthy shutdown, businesses will be cautious with capital investment and hiring, business travel may be curtailed long-term in deference to teleconferencing, the return to previous consumer spending patterns will not be immediate, and a shift to online retail will continue.

For purposes of this forecast, HdL segmented sales and use tax data into eight unique business groups defined by HdL.

- Construction and Manufacturing
- General Retail
- Internet Retail
- Grocery and Pharmacy
- Restaurants and Entertainment
- Professional and Financial Services
- Telecom, Utilities, Waste, and Other Provider Services
- Other

HdL Companies

2020 FORECAST

These business groups were developed after careful review of historical sales and use tax data to identify common economic trends among specific business types. Acknowledging inaccuracies associated with NAICS codes reported by taxpayers, balanced with the need for timely development of this forecast, HdL reviewed and where appropriate, reclassified taxpayer-specific data to the appropriate business category. The context of the trends for each of the eight categories is provided within the forecast.

Currently, actual net sales and use tax payments are known for January, February, March, and April 2020 (reflecting consumer activity for the 4-month period November 2019 – February 2020). The first month forecasted is May 2020, reflecting consumer activity for the month and quarter ending March 2020, the first sales and use tax allocation period directly impacted, at least in part, by the COVID-19 outbreak. A forecast is also provided for the month of June 2020, reflecting consumer activity for April 2020, and for each quarter thereafter through December 2020 (consumer activity through October 2020). For all forecasted periods, the percent change reflects the forecasted percent change over the same period in the prior year.

Projecting sales and use tax is always a challenge; projecting sales and use tax during unprecedented, turbulent times is far more difficult. It must be recognized that events yet unknown and unpredictable will impact future sales and use tax performance. We encourage you to consider this information in combination with other valued information to which you and your team have access. HdL will continue to monitor related developments and will release future updates to the forecast as circumstances warrant.

Client Action

The following items are included for your consideration:

- HdL Consensus Forecast, April 2020, Statewide Sales and Use Tax Trends (with industry-specific context for statewide sales tax trends within eight business categories).
- Sales and Use Tax Allocation Data by Business Category for Allocation Periods May 2018 through April 2020.

As a reminder, you can run and review the standard sales and use tax reports we make routinely available to you and your team by visiting hdlcompanies.com. Hover over the **Login** tab at the upper right-hand corner and click on Texas Sales Tax. You will be automatically directed to our client portal log in page.

The health and safety of our teams, along with the quality and continuity of our services continue to be our top priority. Our client service team members remain available to assist you by calling 512-906-0429 or by email:

- Amy Flanigan, Client Services Manager, aflanigan@hdlcompanies.com
- Robin Humphrey, Client Services Manager, rhumphrey@hdlcompanies.com
- Paula Barr, Director, Client Services, pbarr@hdlcompanies.com

HDL CONSENSUS FORECAST – APRIL 2020

STATEWIDE SALES TAX TRENDS

 **TOTAL MAY '20 -12.8% | JUNE '20 -18.4% | 3Q20 -21.9% | 4Q20 -18.6%**

(Based on Sales Tax Allocation Month)



Construction & Manufacturing

MAY '20 -10% | JUNE '20 -15%

3Q20 -20% | 4Q20 -25%

This business category includes the oil and gas sector and is impacted by the recent price collapse and the reduction in demand for petroleum products as travel is curtailed. Reports suggest construction projects will continue but at a much slower pace with outdoor environmental factors and the ability to isolate workers from one another working in the favor of this business category. Current project halts and cancellation of projects not yet started are being reported by an increasing number of contractors, with shortages of equipment and materials a contributing factor. As individuals and families shelter in place, home improvement projects are a focus, lifting the near-term performance of home improvement centers such as Lowe's and Home Depot. Nonetheless, reduced overall spending compared to last year is expected. Economic uncertainties are also expected to put pressure on home sales thus hurting contractor-driven sales. US industrial production plunged in March 2020 as factories in a variety of sectors halted work to protect workers from the outbreak. Manufacturing activity is expected to continue to slow due to supply chain constraints, weaker demand, and social distancing in the workplace.



General Retail

MAY '20 -35% | JUNE '20 -40%

3Q20 -33.3% | 4Q20 -15%

A significant drop in core retail sales is expected as communities implement social distancing measures to flatten the curve of virus spread at the recommendation of health professionals and government leaders. Large shopping centers and popular retailers are experiencing periods of closure in conjunction with shelter in place orders. Brick and mortar retail sales are expected to be bleak through May and June. As consumer confidence drops and unemployment woes set in, it is expected discretionary spending will be curtailed and negatively impact this category throughout the remainder of 2020. Target and Walmart, while incorporating general retail, grocery, and pharmacy components, are included in this category as data suggests these businesses respond economically like other general retail businesses rather than as grocery and pharmacy entities.



Internet Retail

MAY '20 +75% | JUNE '20 +75%

3Q20 +75% | 4Q20 +65%

Substantial growth is projected in this category, fueled by the implementation of the Wayfair Supreme Court ruling beginning in October 2019 (and first reflected in sales tax allocations in December 2019) combined with an increase in online retail transactions. Remote sellers with no physical presence in Texas but marketing taxable products and services in the state are now required to collect and remit sales and use tax, and marketplace providers such as Amazon, Etsy, eBay, and Wal-Mart.com Marketplace must now report sales and use tax on behalf of third-party vendors that utilize their marketplace platforms. The shift from brick-and-mortar shopping to online retail will intensify in response to social distancing.



Grocery Stores & Pharmacy

MAY '20 +15% | JUNE '20 +7.5%

3Q20 +3.3% | 4Q20 +2.5%

Continued growth in this category is expected with consumers stocking up for quarantine and prolonged school closures. With most dining out options curtailed entirely or limited to take-out/curb-side pick-up/delivery, consumer spending in this category is expected to increase to support eating at home due to social distancing. In addition to major grocery store chains, such as HEB, Kroger, Randall's and Tom Thumb affiliates, this category also includes CVS and Walgreens pharmacies, convenience stores and smaller food marts. Warehouse clubs such as Sam's Club and Costco are also included as data sources suggest these entities respond economically more like grocery stores than general retail establishments.

STATEWIDE SALES TAX TRENDS

 **TOTAL** MAY '20 -12.8% | JUNE '20 -18.4% | 3Q20 -21.9% | 4Q20 -18.6%

(Based on Sales Tax Allocation Month)



Restaurants & Entertainment

MAY '20 -30% | JUNE '20 -45%

3Q20 -63.3% | 4Q20 -60%

Consistent with the outlook for the General Retail business category, the Restaurant and Entertainment sectors, which include hotels, are expected to experience major impacts due to travel restrictions, and cancellation of festivals, sporting events, concerts, and closures of theme parks, cinemas, museums and historical sites due to social distancing and gathering limitations. Restaurants and other facilities that prepare and serve food are largely restricted to take-out/curb-side pick-up/delivery modes. Consumer spending for food has shifted to grocery store spending in response to shelter-in-place orders. Prolonged shelter-in-place restrictions may impact the long-term outlook for this category as dining habits may change. Even as efforts shift to loosening shelter-in-place restrictions, restaurant seating capacities will be limited in response to social distancing requirements. This industry is most vulnerable to permanent closures as tight operating margins existed prior to the pandemic.



Professional & Financial Services

MAY '20 -3.0% | JUNE '20 -5.0%

3Q20 -13.3% | 4Q20 -15%

This category encompasses services delivered by professionals or other specially-trained personnel across a variety of sectors including healthcare, medical supplies information technology, property management, education, banking, insurance, credit services, and engineering and consulting services not related to the construction industry. A review of historical data suggests these services are not, individually, significant drivers of sales and use tax. As a group, however, they are worthy of note as they tend to react similarly in times of economic uncertainty. Activity across this category is expected to contract at levels consistent with the overall economy.



Telecom, Utilities & Other Service Providers

MAY '20 +3% | JUNE '20 +3%

3Q20 +3% | 4Q20 +3%

Continued modest growth comparable to pre-COVID-19 levels is expected in this category encompassing telephone, cellular, cable, internet, data and software services, commercial and residential utilities, and waste removal services. The outlook considers an increase in demand for internet, data, and software services prompted by shelter-in-place orders and the deployment of staff and students working and learning from home.



Other

MAY '20 -10% | JUNE '20 -16%

3Q20 -20% | 4Q20 -20%

This is a “catch all” category of businesses not better classified in other categories. HdL has made a concerted effort to review and re-classify businesses to other categories to reduce the significance of this category for forecast purposes. Activity across this category is expected to contract at levels consistent with the overall economy.

HdL Companies

AUSTIN

8700 Manchaca Road
Austin, TX 78748
Telephone: 512.906.0429

HOUSTON

9821 Katy Freeway #440
Houston, TX 77024
Telephone: 713.481.6975



HdL Companies

888.861.0220 | hdlcompanies.com