Outline

- Update on economic conditions
- Economic recovery, the budget, and long-term goals
- Framework for setting recovery priorities
Where California Stands

- So far, employment and growth no worse than recent slowdowns
- California’s economic indicators look broadly like U.S.
- Housing in California much worse
- Hardest hit
  - Southern California
  - Construction and finance
Job Growth

Annual employment growth, October to October
Bureau of Labor Statistics

California
U.S.
Unemployment Rate

Monthly unemployment rate (seasonally adjusted)
Bureau of Labor Statistics
How This Recession Differs

■ Housing price declines and financial effects preceded employment slowdown
  – Early 2000s and early 1990s started with employment contraction

■ Another Great Depression?
  – Financial markets triggered both crises, but today...
    ■ Much faster and better policy response
    ■ Different magnitude
National Forecast Continues to Deteriorate

Economic predictions for 2009, by month of prediction

*Wall Street Journal* economic forecasting site, 12/11/08

Predicted 2009 GDP growth (left axis)

Predicted Dec 2009 unemployment (right axis)

Unemployment rate, December 2009

2009 GDP growth

May | Jun | Jul | Aug | Sep | Oct | Nov | Dec
---|---|---|---|---|---|---|---
0.0% | 0.5% | 1.0% | 1.5% | 2.0% | 2.5% | 3.0% | 3.5%

7.0% | 7.5% | 8.0% | 8.5%
How Long a Recession?

Share of economists predicting when national recession will end

Wall Street Journal economic forecasting site, 12/11/08
Timeline to Recovery

- Mid-2009: GDP growth turns positive, recession officially ends
- Late 2009 or early 2010: Job growth turns positive
- Early to mid-2010: Unemployment rate peaks
- 2010 (but who knows): Housing prices rise
  - *WSJ* poll: -4.9% in 2009
  - California predictions vary wildly
  - Does economic recovery depend on housing?
California Forecast: Job Growth

Graphs show high, low, and average forecasts:
LAO, UCSB, UCLA, Milken, DoF, and Chapman

<table>
<thead>
<tr>
<th>Year</th>
<th>Forecast</th>
</tr>
</thead>
<tbody>
<tr>
<td>2009</td>
<td>-4.1%</td>
</tr>
<tr>
<td>2010</td>
<td>-2.4%</td>
</tr>
<tr>
<td>1980–2007 average</td>
<td>1.6%</td>
</tr>
<tr>
<td>1982 recession</td>
<td>-2.5%</td>
</tr>
<tr>
<td>1992 recession</td>
<td>-1.8%</td>
</tr>
</tbody>
</table>
California Forecast: Unemployment

Graphs show high, low, and average forecasts: LAO, UCSB, UCLA, Milken, DoF, and Chapman

- 1982 recession: 11.0%
- 1992 recession: 9.9%
- 1980–2007 average: 6.9%

Peak unemployment

- 2010 Q1: 8.9%
Outline

- Update on economic conditions
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Economic Recovery Overlaps with Other Goals

- Balanced budget
- Long-term sustainable growth

Economic recovery

Minimize the conflict
Maximize the overlap
Governor’s Budget Forecast*

<table>
<thead>
<tr>
<th></th>
<th>2008–09</th>
<th>2009–10</th>
</tr>
</thead>
<tbody>
<tr>
<td>Expenditure change vs. 2007–08</td>
<td>+1.2%</td>
<td>+7.7%</td>
</tr>
<tr>
<td>Revenue change vs. 2007–08</td>
<td>-14.7%</td>
<td>-15.9%</td>
</tr>
<tr>
<td>Budget gap</td>
<td>-$14.8 billion</td>
<td>-$41.8 billion</td>
</tr>
</tbody>
</table>

- Personal income and corporation tax revenues much lower than planned
- LAO forecast: $27.8B budget gap in 2009–10 (November 2008)

* As of 12/11/08
The Budget Crisis and Economic Recovery

- The budget crisis means
  - Need to take $40B out of the economy
  - Hard to sell bonds
  - Projects underway may be halted

- Recovery-friendly budget balancing
  - Roll over deficit
  - Get federal assistance
  - Choose less harmful tax increases and spending cuts
## California’s Options for Raising Revenue

<table>
<thead>
<tr>
<th>Revenue source</th>
<th>DoF 2008–09 forecast*</th>
<th>How to raise several billion</th>
</tr>
</thead>
<tbody>
<tr>
<td>Personal income tax</td>
<td>$47B</td>
<td>10% surcharge = $4.7B</td>
</tr>
<tr>
<td>Sales and use tax</td>
<td>$25B</td>
<td>1-cent increase = $5B</td>
</tr>
<tr>
<td>Corporation tax</td>
<td>$10B</td>
<td></td>
</tr>
<tr>
<td>Other revenues and transfers</td>
<td>$5B</td>
<td>Restore 2% vehicle license fee = $6B</td>
</tr>
</tbody>
</table>

*As of 12/11/08*
Federal Recovery Blueprint from Center for American Progress

- $55B to spur demand
  - Social services and neighborhoods
- $70B to states directly
  - FMAP (Medicaid) and general block grants
- $175B on infrastructure
  - $100B for “green” projects
- $50B in tax cuts

California’s share = 10%?
California’s Current Approaches to Recovery

- **Democrats**
  - Accelerate bond funds
  - Support “green” industries
  - Push for federal funds

- **Republicans**
  - Reform employment, procurement, and construction rules
  - Loosen environmental requirements
  - Tax credits (e.g., for new hires and investment)
  - Avoid tax increases

- **Governor**
  - Accelerate bond funds
  - Reform employment rules
  - Reform construction rules (e.g., design-build and hospital review)
Outline

- Update on economic conditions
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Tentative Agreements from Our Initial Conversations

- The budget crisis severely constrains recovery options
  - Fundamental budget reform needed
- Must balance immediate recovery needs and long-term goals
  - Infrastructure spending
  - Regulatory reform
- California needs a plan for spending federal funds
The Three Big Questions

- How can the state balance the budget while minimizing economic harm?
- How should the state select infrastructure projects?
- What can the state do on its own?
Notes on the use of these slides

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Questions? Contact Jed Kolko: 415-291-4483, kolko@ppic.org

Thank you for your interest in this work.