PPIC was founded in 1994 in the midst of the state’s most severe economic downturn since the Great Depression. The decade that followed was in many ways the best and worst of times for the Golden State. The recession was followed by an upturn that many saw as the dazzling dawn of a new economy, an economy impervious to forces that periodically and, it seemed, inevitably brought the old one to its knees. The state government suddenly found itself awash in revenues and optimism about programs that seemed infeasible just a few short years before. Yet, in the midst of all the exuberance, there were forces at work and trends building that would, by the end of the decade, seriously wound this brave new economy and plunge the state into unprecedented fiscal and governmental crisis.

It was to study those forces and trends that William Hewlett, Roger Heyns, and Arjay Miller founded PPIC. It may seem that in this decade, the state of the state has come full circle—and then some. Income inequality remains higher here than in the rest of the nation, the structure of government is under constant stress, the public has little respect for its elected representatives, and the fiscal future seems perilously uncertain. Programs that were put in place to make things better, such as deregulation of the power grid, seem to have made things worse. In sum, it was a dramatic and challenging time to launch a new think tank, but these are exactly the kind of events that PPIC was intended to study in order to provide an understanding of both the problems and the solutions.

To help us document PPIC’s contributions, we asked David Lesher, a highly regarded California journalist, to review the state’s key public policy challenges over these tumultuous ten years and then consider how PPIC’s work informed the public debates. Combined with a timeline of important events, his ten brief essays provide a compelling summary of how California public policy issues were evolving as the world entered a new millennium, the nation endured a challenge to its national security, and the state experienced one of the most dramatic transitions of gubernatorial leadership in American history.
When PPIC opened its doors in the summer of 1994, California was in the midst of a profound economic transformation. The Berlin Wall had fallen five years earlier, and the state’s Cold War industries all but collapsed soon afterward. Major defense manufacturers eliminated more than 300,000 jobs in California, and the federal government closed more than two dozen military bases. California’s recession lasted about three years—a bit longer than elsewhere in the nation—and produced record deficits in the state budget.

The economic hardships also contributed to a year of political upheaval. In Washington, Republicans gained control of the House and Senate. In California, Governor Pete Wilson was reelected, while Speaker Willie Brown’s Democrats lost control of the state assembly. Voters also passed Proposition 187, the landmark measure against public benefits for illegal immigrants.

Politically, economically, and demographically, California’s population was changing rapidly and dramatically. With its first report, PPIC launched a multiyear study about an increasing gap between rich and poor that posed important questions for the state’s future. Deborah Reed, an economist and poverty expert recruited from the University of Michigan, found that the income gap in California was similar to the nation’s income gap until the late 1980s, but during the recession years it became much larger.

Reed’s study was the most comprehensive on the topic to date. Analyzing 26 measures of income, she found that the gap grew faster in California not because the rich were getting richer here but because the poor were getting poorer. In 1969, 20 states had a wider income gap than California. By 1989, California’s gap was the sixth largest. As the state struggled to emerge from its economic slump, the report offered key insight for the future of government poverty programs and for businesses assessing the California workforce.

The state’s recession began to ebb in early 1994, lagging a bit behind the U.S recovery. Amid the rubble of major industries, it wasn’t clear just how economically fertile California remained. The state lost more than 800,000 jobs in the first half of the decade. But in
remarkable growth tracked by PPIC researchers, more than two million jobs were created in the second half of the 1990s.

California emerged from recession a different state. Its entertainment industry was the first to roar out of the slump, followed closely by the historic explosion in technology companies. California has always been one of America’s best incubators for start-up businesses, so it was well positioned to seize on new trends. Geographically and demographically, it was also poised for gains from globalization.

PPIC’s ongoing study of income inequality found that the income gap between rich and poor shrank slightly and then stabilized during the economic growth in the late 1990s. At first, the poor outpaced the rich in income growth, narrowing the gap. Then, both groups grew at a similar rate. Still, Reed reported that California’s gap had grown by 50 percent over the previous 30 years compared to 25 percent nationally and that education was to be a primary factor in the state’s wage gap. Thirty years ago, a high school graduate earned just 9 percent more than a dropout.

An increasing gap between rich and poor posed important questions for the state’s future

By 1997, the wage gap between a high school graduate and a dropout had grown to more than 35 percent.

“Given the trends and the causes we identified, it seems reasonable to anticipate continuing high income inequality in the state’s future,” Reed warned.

The PPIC Statewide Survey, directed by Mark Baldassare, found that Californians were well aware of the income gap: 56 percent said the state is divided between haves and have-nots, compared to about 40 percent of U.S. residents who drew that conclusion about the nation at large.
On December 6, 1994, Orange County became the largest municipality in U.S. history to declare bankruptcy. It was a shocking crisis. Here was a large and growing suburban area, with a reputation for affluence and conservatism, amassing a huge public debt through risky speculation in the financial markets—and then refusing to pay its bills.

On Wall Street, most analysts wrote this off as a fluke, caused by an underqualified county treasurer. But in the first comprehensive look at the topic, PPIC Senior Fellow Mark Baldassare warned that conditions leading to Orange County’s bankruptcy continued to exist in local governments throughout California. In his book, *When Government Fails: The Orange County Bankruptcy*, Baldassare traced the roots of the crisis back to Proposition 13. The 1978 landmark ballot initiative to cut property taxes severely limited the ability of local government to raise revenue and respond to changing local conditions.

Subsequent initiatives and shifting budget responsibilities have contributed to an increasingly dysfunctional system of state and local governance in California. Today, it is a top priority for reformers. The current inequities led cities and counties to cut back on police, firefighters, libraries, and pothole repairs even while state government reported record budget surpluses in the late 1990s. They also forced local governments to seek additional money through risky ventures such as the investment policies of Orange County or through development plans that sometimes run counter to balanced growth.

With an extensive portfolio of research on state and local governance, PPIC has documented many of the profound changes that have resulted from policy decisions struggling to balance local needs and resources under these conditions.

PPIC researchers Paul Lewis and Elisa Barbour surveyed local officials in 330 California cities to prepare their study on the intense competition for retail developments that generate sales tax revenue. They found a dramatic range in the amount of local sales tax per resident in Orange County.

**Who lost and how much in the Orange County bankruptcy?**

![Bar chart showing losses](chart.png)

Source: *When Government Fails: The Orange County Bankruptcy.*
California, with some cities getting just over $2 and others exceeding $56,000. The study also revealed that instead of increasing local revenues statewide, the concessions cities made to lure retail businesses appeared to have little overall effect on retail location decisions and sales tax revenues.

“It appears that the primary effect of cities’ actions in favor of retail is simply a transfer of resources from local government to retailers, developers, and landowners,” said Lewis.

In another study, Marla Dresch and Steven Sheffrin found that cash-strapped local governments were assessing the highest developer fees in the nation on new home builders. In rapidly growing Contra Costa County, where the researchers studied four years of real estate sales, developer fees accounted for up to $30,000 in the price of a new home.

Another popular tool used by local governments to raise revenue since Proposition 13 is the redevelopment project. As an incentive to improve blighted areas, state law entitles redevelopment agencies to a proportion of the increase in property taxes generated by redeveloped property. Taking a close look at the link between redevelopment and the increase in property values, Michael Dardia challenged the rationale behind that arrangement. His study, the first of its kind, found that three-quarters of the redevelopment projects studied failed to generate more in increased value than redevelopment agencies took away in property taxes. He estimated that California redevelopment agencies divert more than $170 million in property taxes each year that would otherwise go to counties, special districts, and the state.

For all of the trauma blamed on Proposition 13, however, the PPIC Statewide Survey found that the measure remains popular. Thirty-eight percent of Californians said the property tax limit has had a good effect on local government services compared to 23 percent who believe it has had a bad effect.
class size reduction

As the economy improved, it was replaced by education as the state’s top priority. An excellent public education was once the hallmark of California’s famed quality of life. By the mid-1990s, K–12 education in California ranked among the lowest in America for student spending and performance.

There was plenty of finger-pointing. During the recession, state lawmakers shifted more responsibility for education funding to cash-strapped cities. The powerful teachers unions were blamed for being greedy at the expense of students. And educators debated the merits of testing standards and curriculum strategies.

In 1996, state lawmakers responded by dedicating the first budget surplus of an improving economy to a landmark plan for reducing class sizes. At a cost of nearly $1 billion, the state sought to limit class size in the first four years of elementary school to a maximum of 20 students—a one-third reduction from the average at the time. In the glowing media coverage that followed, one educator said it was “clearly a watershed” and another called it “the start of a renaissance” for public education.

Many more education reforms followed. But years later, California public schools still struggled financially and academically. The reasons are complex, but an ongoing research effort by PPIC has challenged earlier assumptions and illuminated many of the root difficulties.

One study, looking directly at class size reduction in the state’s elementary schools, uncovered a wide range of experiences. Overall, the study found a positive effect on low-income student performance. But in Los Angeles, test scores in low-income schools actually dropped when classes were made smaller. Elsewhere, scores increased as much as 15 percent. These differences underscore the importance of other conditions besides class size for quality education. Because of the huge jump in demand for teachers created by class size reduction, many...
low-income schools found themselves with many inexperienced, uncredentialed teachers. When Governor Gray Davis focused considerable funding and political attention on the quality of school teachers, PPIC researchers responded with a series of studies on the topic. They found that teacher quality is a critical element of student performance, but poverty and peer groups have a much greater influence. One study found that if a student were to switch from a low-performing peer group to a high one, his or her math score would be 9 percent higher than it otherwise would have been.

In Sacramento’s rush to reform education during the 1990s, lawmakers increased the standards and accountability for public schools. But despite the budget surpluses, spending on schools did not increase as rapidly.

The contrast between standards and spending changes from Sacramento was captured in a PPIC study that found California had adopted some of the highest academic expectations in the country, but it continued to lag in funding. Under the state’s Academic Performance Index, state educators are expected to bring California students up to a level that would place them higher than 70 percent of their peers nationally. However, the study reported that at the same time, California has 25 percent fewer teachers per student than schools nationally, due partly to the state’s high teacher salaries.

PPIC has focused special research effort on school finance, suggesting the need for new policies that would allocate education money based on a school’s teaching challenge, not just on its number of students. A quarter of California’s 6 million public school students have limited English skills, one study found. PPIC research pointed to poverty, even more than language, as the greatest challenge for improving academic performance.

Yet, a comprehensive look at California school finance also found more resources are still directed to affluent students than to those who are poor. More than 20 percent of the teachers in schools with low-income students were not credentialed, compared to 2 percent in higher-income populations. Thirty years after the U.S. Supreme Court’s landmark Serrano decision ordered equitable school funding in California, the study found striking differences in spending on students even within the same region or district.

“This raises questions about the state’s decades-long effort to equalize resources,” said Julian Betts, one of the study’s three authors.
In California’s rapidly changing demographic, the passage of Proposition 187 in 1994 was a political watershed. The measure sought to block undocumented immigrants from access to public benefits such as education, welfare, and health care. The issue was brought to the surface by the recent recession and then fought out in a divisive campaign. For California, it was the first prominent display of the resentment over illegal immigration that had been simmering for several years.

After its passage by nearly 60 percent of California voters, the measure was partially dismantled. Parts of the proposition regarding health and welfare benefits were later adopted in federal law, and court challenges blocked the measure’s ban on education for undocumented youth. But Proposition 187’s greatest impact was as a catalyst in California’s growing awareness of its own new identity.

Eventually, the forces put into motion by Proposition 187 would reshape the political landscape of America’s largest state. Latino political participation surged and was partly responsible for several years of solidly Democratic rule in California. The Latino caucus in Sacramento grew to near parity with its share of the state’s population. As both of the major parties stepped up their outreach to Latino voters, the mainstream political dialogue grew less divisive and began to reflect the vision of a more inclusive state.

Yet, as PPIC reported in a range of studies on California’s changing government and political structure, the landscape remained unsettled. Despite the improvement, Latino political participation continued to lag significantly behind other groups. And voter distrust toward government institutions and political leaders was growing rapidly.

PPIC Director of Research Mark Baldassare captured the major trends under way in his 2000 book, California in the New Millennium: The Changing Social and Political Landscape. Drawing on a dozen focus groups and five statewide opinion surveys, Baldassare foresaw a significantly different state in the mid-21st century, given its changing demographics, increasing regional diversity, and voter distrust.
attitudes. The book identified a critical juncture for California, “with its social and political landscape changing at the same time that a rapidly growing population is beginning to put incredible pressure on the state’s resources.”

One of the most prominent questions about California’s future is whether its electorate will be representative of its population

The challenges are a test for democracy in California and the ability of a diverse population to reach consensus on the changing nature of the state. A number of PPIC studies looked at the political participation essential to consensus from different angles: PPIC researcher Claudine Gay looked at congressional districts and found that Latino voter turnout increased significantly when the ethnic population was concentrated. Another report, by Zoltan Hajnal and Hugh Louch, found encouraging agreement among ethnic groups on most ballot measures as well as troubling differences on racially based issues.

One of the most prominent questions about California’s future is whether its electorate will be representative of its population. In a study for PPIC, university researchers Jack Citrin and Benjamin Highton looked at a decade of political participation records to forecast the makeup of the state’s electorate in 2040. One significant finding was that white voters might continue to be a majority of the electorate even at a time when whites would represent just more than a third of the state’s population. The study indicated that the ethnic participation gap would narrow significantly for Latino and African American voters as education and income differences were reduced. The prediction was different for the gap for Asian voters, whose participation is more commonly traced to cultural differences.
welfare reform

On August 23, 1996, President Clinton signed a sweeping overhaul of the nation’s 61-year-old guarantee to help the nation’s poorest children. His bill eliminated the open-ended program of federal cash grants known as Aid to Families with Dependent Children. In its place, the bill gave states far more control and responsibility for poverty programs and limited the amount of time that indigent adults could receive assistance.

Supporters of the idea said it was needed to end the ongoing cycle of dependency in which too many teenagers saw early parenthood and a welfare income as a way of life. But the plan was highly controversial among advocates for the poor, who worried that too many welfare recipients would not find work and could be left on the streets without help.

Over the next several years, PPIC closely tracked the issue, providing California with a comprehensive and detailed look at the evolving nature of its massive welfare population.

In early 1997, when the California legislature opened debate about its own version of the new welfare program, PPIC provided lawmakers and other interested parties with a detailed profile of the state’s poor population that challenged traditional assumptions. The study by Stanford economists Margaret O’Brien-Strain and Thomas MaCurdy found that welfare was not a way of life for the vast majority of the state’s recipients, who had work income as well as cash assistance. It also revealed that the largest racial category was non-Hispanic white women and that most recipients had high school degrees.

The study offered encouraging news about the prospects of moving a large portion of the welfare population into the workforce. But it also warned that about 432,000 recipients were “highly dependent” on their welfare income. Two years later, PPIC researchers Hans Johnson and Sonya Tafoya looked at the barriers for moving welfare recipients into the workforce and found that 80 percent of the population had low or very low basic skills in such things as reading a bus schedule or completing an employment application. The study also warned that the problem was greater in California than elsewhere.
At the time, welfare reform was receiving widespread credit for helping reduce the population dependent on financial aid. At the end of the decade, California’s total caseload had dropped by more than a third since President Clinton signed the landmark overhaul. Still, a slowing economy and the approaching time limits pointed to significant hurdles ahead.

While California’s welfare caseload had dropped, every other large state except New York had seen larger reductions. A PPIC study revealed some causes: California’s version of welfare reform was more generous than elsewhere. Unlike the other large states, California continued cash assistance for indigent children even after their parents exceeded their time limit or were sanctioned for not complying with program rules. The state’s monthly cash grants were also among the largest, and recipients were allowed to earn more income from work without a cut in their public benefits.

In January 2003, five years after the effective date of California’s welfare reform plan, the first recipients reached their lifetime limit for cash assistance. Already, more than 1.4 million people had moved off California’s welfare rolls. In an extensive survey that interviewed former welfare recipients over a period of months, PPIC found more encouraging news, reporting that 90 percent of California families that leave public assistance continued to have a working adult one year later. Also, in nearly 70 percent of the single-parent households that left welfare, the working income was enough to raise the family above the poverty line.

The study also found that many of California’s indigent aren’t aware of the benefits available to them. Inexplicably, some leave welfare and don’t return even when they are eligible. Instead, they sometimes live in crowded or substandard housing. “One of the questions raised by our findings is how to help needy families who have made a break from the welfare system—and who don’t want to go back,” said co-author Margaret O’Brien-Strain.

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**California has experienced rapid population growth**

Sources: Census Bureau estimates and PPIC projections.
high-tech boom and bust

When PPIC opened its doors ten years ago, dot.com was still a meaningless phrase to most Americans, and the landmark release of Windows 95 was still on the drawing boards. Just a decade later, technology has gone through generations of change, and it has transformed almost every aspect of daily life.

California’s integral role in spawning the technology revolution reaffirmed its heritage as a place for futurists and innovators. The surging growth born in Silicon Valley and elsewhere yanked the state from its economic troubles and flung it toward unprecedented levels of growth and revenue. The state’s General Fund, brimming with billions of dollars in surplus, doubled its spending in barely six years. Education and health care programs expanded, environmentally sensitive land was protected, and taxes were cut.

When the technology bubble burst, its negative impact was equally great. Within five years, California’s credit rating was the worst in America, and its astounding budget deficit will be felt for generations.

With such a critical and volatile role in the quality of life for Californians, the technology industry is an important topic for public policy researchers and decisionmakers. The state’s ability to resolve many of the pending issues regarding growth and public services may depend on the fortunes of the technology industry.

At PPIC, high-tech expert Junfu Zhang was recruited from Brookings, where he was a dissertation fellow, to explore the dynamics of Silicon Valley and assess its ability to grow the California economy once again. His report described Silicon Valley as a powerful incubator for start-up businesses, nourished by a unique environment for creativity and risk-taking. The area’s success wasn’t due to big or old companies. Nearly all of the jobs created during the 1990s were in companies that didn’t exist before the decade began. Compared to entrepreneurs in other tech centers, Silicon Valley’s entrepreneurs had much quicker access to venture financing, and their employees were more likely to leave and start new firms.

Zhang’s report was encouraging for policymakers looking to technology companies for continued growth. “Silicon Valley’s greatest asset is its ability to reinvent itself,” he said in his report.

Another PPIC report, by Berkeley professor AnnaLee Saxenian, explored the timely issue
of high-skilled immigrants in technology companies. Saxenian found that, in 1998, Chinese and Indian engineers were running one-quarter of Silicon Valley’s high-technology businesses. In that year, their 2,775 companies collectively accounted for more than $16.8 billion in sales and over 58,000 jobs.

Silicon Valley’s greatest asset is its ability to reinvent itself

The findings were helpful for Washington lawmakers considering the number of H1B visas to allow for high-skilled immigrants. The study suggested that immigrant entrepreneurs, instead of displacing U.S. workers, are important creators of jobs.

California’s treatment of its job-creators has been one of the most critical topics for lawmakers during the last decade. The state was slower than the rest of the nation in climbing out of recession during the mid-1990s, prompting Governor Pete Wilson to describe California as a “bad product.” Today, as the state struggles with financial hardship once again, Governor Arnold Schwarzenegger considers it “the worst business climate in the nation.”

Measures of the business climate are popular communication tools for media and lawmakers. But a PPIC study by Michael Dardia and Sherman Luk also found that analyzing that climate is exceedingly complex in a state as diverse as California.

Their report challenges the common wisdom that California was hemorrhaging jobs during the recession, because some industrial sectors were doing well. The study looked closely at years of employment data from the state’s eight largest metropolitan areas and concluded that there are so many differences that it would be misleading to generalize about a California-wide business experience. “The large variation in industrial and regional characteristics presented in this study show that California is simply too large and heterogeneous for the notion of a uniform climate to be very helpful in setting policy.”
On March 29, 2001, the U.S. Census Bureau officially logged California as a state without an ethnic majority population. Just a decade earlier, non-Hispanic whites made up nearly three-quarters of the state’s residents. In the latest count, their share was less than half.

No other region in the modern world has undergone the tremendous and rapid population change that California has experienced in recent decades. As PPIC demographer Hans Johnson told a state oversight panel, the population of California is among the most diverse and complex in the world. It more than tripled in size during the past two generations, and today it contains nearly one out of every eight U.S. residents. By 2030, it is expected to grow to 50 million people; by 2025, Latinos are projected to be the largest ethnic group.

“The substantial population of immigrants in California means that the future of immigrants and their descendants will largely determine the future of California,” Johnson told the panel.

Accommodating the needs of a rapidly growing and diverse population is the primary focus of public policy in California today. It is driving key decisions about the growth of housing, jobs, and transportation systems. It is reshaping the health care system to address a younger and poorer population. And it is the greatest challenge in meeting education goals for access and performance.

PPIC research has helped decisionmakers understand the magnitude and the dynamics of the dramatic population change under way.

In one study, Johnson described how experiences vary significantly between regions: Two of the state’s fastest growing areas—the Inland Empire and the San Joaquin Valley—are also two of its poorest. Also, the income gap between regions grew dramatically in the last decade, with the Bay Area jumping more than 20 percent and the San Joaquin Valley reporting a drop.

Such regional contrasts and the political clashes over racial issues have sparked concern about volatility in California’s melting pot. But PPIC Director of Research Mark Baldassare and Research Fellow Zoltan Hajnal
found signs of encouragement when they looked at opinion surveys of more than 20,000 adults over a two-year period. More than 80 percent of Californians in each ethnic category expressed satisfaction with race relations in their area, and solid majorities in each group expected conditions to improve.

“In many important respects, this diverse population also shares a common vision of the future and of the state’s policy needs,” Baldassare said.

Several studies at PPIC examined the nature of the immigration boom that continues to drive California’s population changes, sometimes raising important questions about the assumptions behind major policy. For example, almost half of all births in California during the last decade were to foreign-born mothers. But PPIC research indicated that the children of immigrants will likely have substantially lower birth rates than their parents. If so, the study suggested, population projections for the state could be significantly lowered.

PPIC also documented the growing inability of California’s population to be segmented into ethnic categories, with a report that found over 14 percent of all births were to mixed-race parents. More than half of the state’s multirace babies had a white and a Hispanic parent.

Understanding the nature of these population changes is important for effective policy. PPIC has also focused significant attention on undocumented immigration to help foster a common understanding about an important topic.

For example, PPIC studies have documented that unauthorized immigration is responsive to economic conditions in California and that much of the cross-border traffic is from immigrants who do not settle permanently on either side.
It was about 10:30 on a Monday morning when the elevator at 2001 Embarcadero North clanked to a stop between floors. Elsewhere, traffic snarled when street lights shut down, an ice cream store gave away its melting product, and an anxious mother worried when her invalid, four-year-old daughter’s ventilator stopped working.

The blackout on March 19, 2001, left more than one million people in the dark and it lasted for several hours. It wasn’t the first time California electricity regulators had been forced to shut down portions of the power grid because there wasn’t enough energy to go around. But the blackouts were becoming longer and more frequent, turning months of consumer anger over prices into widespread fear about a dangerous crisis that was spiraling out of control.

In a state that is well acquainted with such natural disasters as earthquakes, fires, and floods, the most frustrating element of the electricity crisis was that it was largely self-inflicted by faulty government policies. Californians were already unhappy about the performance of their state government. But the electricity crisis was a threshold experience, demonstrating to voters that government problems went beyond the deteriorating quality of public services. Now, the public was forced to worry about basic services that it had previously taken for granted. Eventually, fallout from the energy crisis would help convince Californians that it was time for a radical and unprecedented recall of the governor.

PPIC recruited Christopher Weare, a former USC professor with a background in California utilities and politics, to provide a comprehensive overview of the state’s energy condition. His report helped illuminate an exceedingly complex and little understood topic. It also raised warnings that California risks a repeat of the crisis if it does not take steps to restore a stable energy market.

The most frustrating element of the electricity crisis was that it was largely self-inflicted by faulty government policies.

None of that concern was evident when state lawmakers voted unanimously in 1996 to pass the energy deregulation bill that triggered the state’s crisis less than five years later. California had the highest electricity prices in the country, nearly 50 percent above the national average. This bill was supposed to solve everyone’s problems. Consumer groups supported it because household rates were scheduled to drop 20 percent by 2003. Environmentalists won $500 million in assistance for renewable energy programs. Utilities were allowed to recover $30 billion in bad investments on
nuclear plants. And small-government advocates hailed a national model for injecting competition into a lethargic industry.

While California debated its energy overhaul, however, investment in new power generation plants came to a halt. And when the bill passed, California utilities sold many of their generating plants to out-of-state companies. Within a few years, California’s power supply was inadequate to meet demand. In a newly unregulated market, prices soared immediately.

California’s energy market remains a patchwork of the solutions that government leaders implemented to escape the crisis. The state’s two largest utilities went bankrupt and government agencies took responsibility for the sale and supply of the state’s power. Federal policy zig-zagged from distant monitoring to market regulation and then criminal investigation. Finally, corruption scandals related to California’s crisis caused the bankruptcy of a giant energy company and its prestigious accounting firm.

Weare’s study takes apart the elements that led to California’s crisis and the temporary solutions that remain in place. He concluded that adequate power supply and long-term energy contracts are essential elements in a stable market. And he identified natural gas price increases, unrelated to California’s deregulation, as a prime contributor to the volatile electricity market and an important issue for long-term stability.

Weare recommended a series of policy changes including an increase in demand management programs to discourage consumption at peak times. He also warned government that “continued ambiguity and conflict may lead to market uncertainty, stifle investment in critical infrastructure, and risk the same errors that precipitated the crisis.”
Many states had budget shortfalls in 2003, but California’s record-shattering deficit was far beyond the experience elsewhere. And it wasn’t a surprise. In recent years, lawmakers often used temporary fund-shifts and other one-time solutions to delay the problems, not solve them.

In a non-election year, there was early and cautious optimism that lawmakers might finally reach a meaningful compromise agreement. But there aren’t many moderates in the California legislature any more, and talks soon broke down over a plan to increase taxes. By spring, California had the worst state credit rating in America.

That summer, the depths of the state’s financial and leadership crisis became clear. In an increasingly partisan environment, lawmakers were unable to reach agreement even in the face of a major crisis. Government watchers had warned for decades that the financial structure for state and local government is a precarious patchwork of ad hoc policies, some from voters and some from lawmakers. It looked as though the problems were finally coming home to roost. When a budget finally passed, much of the deficit was covered by borrowing. Once again, it appeared lawmakers had temporarily skirted a problem, not solved it.

The public’s concern was revealed in a series of opinion polls conducted by PPIC’s Statewide Survey. In his years as a California pollster, Survey Director Mark Baldassare had never seen measurements like those he detected in 2003. Barely two years earlier, 78 percent of Californians said they saw good times ahead. Now, almost as many predicted bad times were coming. The economy and jobs leaped to the top of the list of voter concerns, followed by the budget deficit and, finally, education, which had been the number-one issue during the years of prosperity. Ominously, the survey also found that barely a third of adults trusted government “most of the time” and just a quarter approved of the way Governor Gray Davis handled the budget.

In barely five years, California reported both its highest budget surplus and its deepest budget deficit in history
“These are dismal numbers for consumer confidence by historical standards, and certain to have both political and economic consequences,” Baldassare testified to a state assembly committee in March 2003. “We find that Californians are focused on the troubling events of current times—the economic slowdown, the state’s budget deficit, and the possibilities of war abroad and terrorism at home.”

One of the most serious problems lawmakers hope to resolve in the future is the volatility in California’s budget. Revenue growth in the late 1990s caused spending from the state General Fund to double. The money paid for landmark reforms such as class size reduction and expanded health coverage. But in barely five years, California reported both its highest budget surplus and its deepest budget deficit in history. When the money disappeared, lawmakers still protected the programs they bought with a budget surplus.

Californians didn’t want to cut the new programs either. In June 2003, the PPIC survey found that over 70 percent of adults were opposed to cuts in education or health care, even though those two categories represent more than 80 percent of state spending from the General Fund. Californians also didn’t like many of the tax or fee increases that lawmakers were considering on wealthy incomes, sales, or vehicles. But the survey did find signs of support for other solutions—such as Internet taxes, cigarette taxes, and reforms to Proposition 13.

Before another committee, Baldassare testified that “Policymakers would be well advised to take advantage of the public’s desire for change and consider bold, new ideas for tax and spending reforms that aim to provide Californians with a better-functioning fiscal system in the future.”

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California’s state budget relies on volatile revenue sources

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<tr>
<td>1998</td>
<td>$7.5 billion</td>
<td>$12.7 billion</td>
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<td>1999</td>
<td>$12.7 billion</td>
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<td>2001</td>
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<td>2004</td>
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It’s been nearly a century since Governor Hiram Johnson promised on the eve of his election that “the recall will be a pistol in the hands of the people.” Until now, voters have experienced wars, riots, depression, and corruption without ever drawing the weapon Johnson provided them in 1911. The fact that they used it so swiftly and decisively against Governor Gray Davis is strong indication of the unprecedented conditions in California today.

The roots of the recall go far beyond the governor’s office. Political seismologists have detected signs of such an uprising for several years, even when California was experiencing the good times of the late 1990s.

As PPIC’s Mark Baldassare described in his book, A California State of Mind: The Conflicted Voter in a Changing World, the prosperity near the turn of this century suggested a golden era was ahead. Confidence in the economy was the highest it had been in decades. Even then, however, there was a foreboding trend under way in public attitudes. Californians still distrusted government and lacked confidence in the ability of lawmakers to cope with the formidable challenges facing the state—rapid population growth, increasing racial and ethnic diversity, a crumbling infrastructure, congestion, pollution, energy shortages, and a host of other problems. In A California State of Mind, Baldassare saw the hope for a golden era ending with the terrorist attacks on New York and Washington in September 2001. As surveys showed, the high spirits recorded during America’s brief period of peace, prosperity, and security soon began to deteriorate.
Baldassare’s research involved 14 focus groups and a series of 11 public opinion polls that reached over 22,000 adults between 1999 and 2001. The primary theme of the research is the lack of trust toward elected officials. It is a prophetic account of the California electorate and many of the raw and early emotions that would eventually lead to the governor’s recall.

Despite their unhappiness about government performance and frustration over the energy crisis, voters reelected Davis in 2002. But the campaign was also one of the most negative in California memory. Davis, who worried publicly about facing millionaire candidates, fueled public cynicism by raising an unprecedented $70 million in campaign funds. Even after outspending his opponent, Davis barely won an election that saw the lowest general election turnout in state history.

By the summer of 2003, when lawmakers were well past their deadline to resolve the state’s soaring budget deficit, the petition to recall Davis qualified for the ballot with nearly twice the required signatures. In October, more than 55 percent of voters supported the recall, and Arnold Schwarzenegger, the winning replacement candidate, outpolled Davis.

The history of the 2003 recall is still being written. Now that they’ve used it, will voters be more likely to use it again? Many of the systemic problems that increased partisanship and discouraged compromise are still present in Sacramento. But the radical nature of an unprecedented recall also tempted government watchers to predict a new era in which the relationship between the people and their representatives will be forever changed.
With a growing budget deficit, continuing waves of immigrants, a troubled health care system, a growing population of low-income families, and an electorate embracing more and more mechanisms of direct democracy, outsiders are now asking, “Is California for real? Can all this be happening at once?”

The answer is that California is dealing with the present just as it has dealt with its tumultuous past: with a large dose of hard work and creativity—and a dash of the dramatic.

Still, the challenges we face are formidable: provide more education resources for the rapidly growing population of youth; structure a health care system that offers care to those without health insurance coverage; build the infrastructure sufficient to accommodate another 10–15 million people in the next 20 years; implement a water allocation program that moves this precious natural resource to its highest and best use; revisit the design of the electric power industry to reflect the interdependency of private supply and public interest; and redesign our system of public finance to provide some fiscal muscle and autonomy at the level of local government. The multiplicity of these challenges will test state and local governments as never before.

To those who might choose to criticize California, remember that it still embodies the golden dream for hundreds of thousands of immigrants who come here every year.
Yet, to those who might choose to criticize California, remember that it still embodies the golden dream for hundreds of thousands of immigrants who come here every year. It is both a laboratory of change and a safe harbor for those ready to settle down.

Pragmatism is a recurring theme in all of PPIC’s first decade of work—whatever the problem, Californians and their representatives have found a way to work a solution. The solutions have not always been elegant or easy to implement, but they keep California moving along as we seek ever better options. As PPIC works to learn more about the state and to offer up its own version of those pragmatic solutions, our goal will be to help decisionmakers preserve the golden dream for those here today and for the generations yet to come. We are deeply grateful to our founders for having the vision and providing us with the opportunity and the resources to serve the state in this way.

David W. Lyon
President and CEO
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■ PPIC Statewide Survey, June 2003 (Mark Baldassare)

the recall
■ A California State of Mind: The Conflicted Voter in a Changing World (Mark Baldassare)
■ PPIC Statewide Survey, October 2003 (Mark Baldassare)

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