State Budget 2009-10

Closing the $60 Billion Budget Gap

The amendments to the 2009-10 Budget are the culmination of California's effort to restore balance to a state budget that has been decimated by the worst budget crisis in the state's history.

In February, the state enacted $36 billion in solutions to what was then estimated to be a $42 billion General Fund budget gap (the additional $6 billion in solutions failed to pass at the special election in May). The amendments to the 2009-10 budget include another $24 billion in solutions to address the further deterioration of the state's fiscal situation identified in the May Revision. The $60 billion in budget solutions adopted this year addresses the largest budget gap the state has ever faced, both in dollar amount and in the percent of General Fund revenues it represents.

Components of the $60 Billion Budget Gap

Figure INT-01 displays the components of the $60 billion budget gap the state has faced in developing the budget for 2009-10. As the figure shows, the largest contributor to the budget gap is the reduction in the baseline revenue forecast for 2008-09 and 2009-10. This reduction is due almost entirely to the economic recession. In May 2008, the Department of Finance forecast the output of the state's economy (as measured by personal income) to be $1.589 trillion in 2008, $1.655 trillion in 2009 and $1.739 trillion in 2010. In the May 2009 forecast, the equivalent values were $1.559 trillion, $1.543 trillion and $1.564 trillion, reflecting reductions of 1.9 percent, 6.8 percent and 10.1 percent, respectively. General Fund revenues are very sensitive to changes in the economy, so these reductions in economic output translated into massive reductions in the baseline revenue forecasts between May of 2008 and May of 2009 of 20.4 percent for 2008-09 and 22.7 percent in 2009-10. Figure INT-02 shows General Fund revenues over the last decade and demonstrates how severely the recession has affected revenues in the last two years.

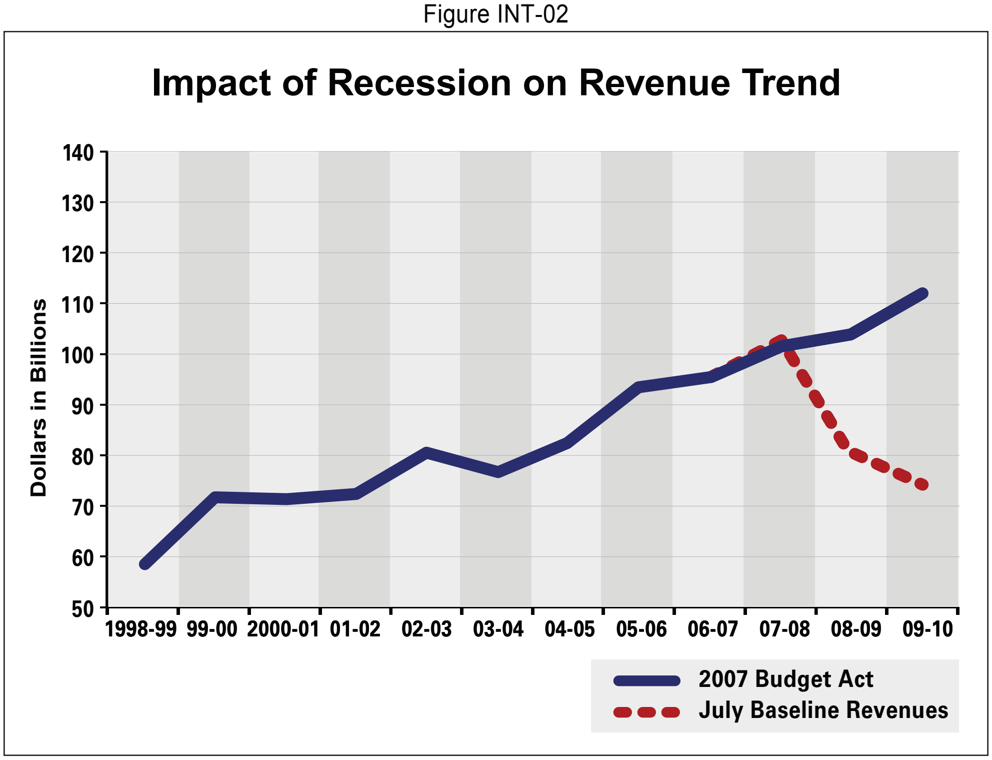
Figure INT-01

Development of the $60 Billion Budget Gap

(Dollars in Billions)

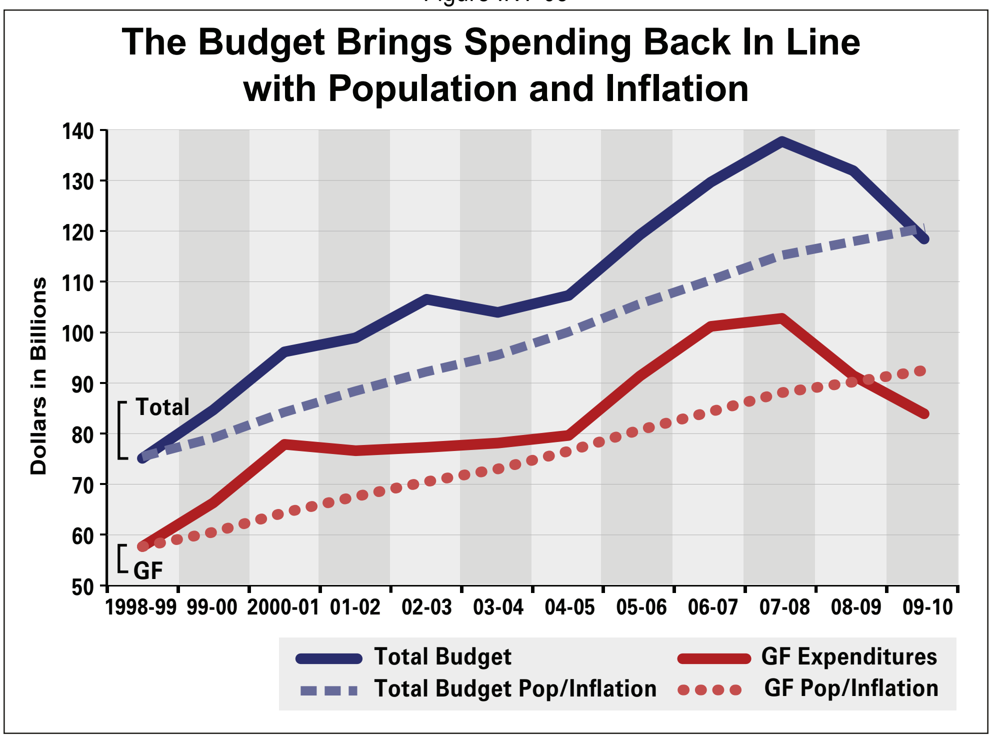
June 30, 2010 Reserve forecast in September 2008	-$1.0
Changes to Reserve:	
Two-year Reduction in Baseline Revenues	-47.3
Two-year Change in Workload Spending	-10.8
Target Reserve at Budget Agreement	-0.9
Budget Gap	-$60.0

Figure INT-02



Spending growth also contributed to the budget gap. For much of the last decade, state spending grew faster than population and inflation. As Figure INT-03 shows the budget reduces spending below the population and inflation trends. While the figure shows that spending grew sharply in 2004-05 and 2006-07, it is important to note that about half of the increase was due to repayment of debts incurred during the last state budget crisis and to the loss of one-time solutions adopted during that crisis.

Figure INT-03



Solutions to Close the $60 Billion Budget Gap

Figure INT-04 displays the $60 billion in budget solutions enacted this year. The solutions are wide-ranging, touching all three of the state's major revenue sources and cutting spending in virtually every state program that receives General Fund support.

Figure INT-04

How the $60 Billion Budget Gap Was Closed

(Dollars in Millions)

	2009 Budget Act - enacted in February	Amendments to the Budget Act of 2009	Total Solutions
Cuts	$14,893	$16,125	$31,018
Taxes	12,513	-	12,513
Federal Stimulus	8,016	-	8,016
Other	402	8,034	8,436
Total	$35,824	$24,159	$59,983

Outlook for the Future

California's budget situation is likely to remain challenging for some time for two reasons. First, while the economic forecast projects a recovery from the recession will begin next year, the recovery is not expected to be as robust as in past years. Second, some of the solutions to the budget crisis are one-time, or of limited duration. This is to be expected in the face of such a severe fiscal crisis. It would simply not have been possible to have balanced the budget entirely with permanent tax increases and ongoing spending cuts, given federal, constitutional and other limitations. Further, as much of the current budget shortfall is associated with a temporary economic downturn, the inclusion of some temporary solutions is appropriate. Preliminary projections for the coming fiscal year suggest that the state will face a significant budget shortfall; perhaps in the $7 to 8 billion range, with even larger shortfalls projected in out-years. However, the state's ability to manage its way through the nadir of this economic cycle demonstrates a determination and ability to overcome future budget challenges. Moreover, the budget contains a wide range of reforms that will significantly reduce spending growth in the future.