

Economic Outlook and Proposition 30

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2015-16 Developments

- The near-term outlook for Local Control Funding Formula (LCFF) funding increases is positive
 - The economic recovery from the Great Recession continues
 - State revenue growth for 2014-15 is tracking the Budget forecast
 - ◆ As of September 2014, revenues are up 1.5%, or \$324 million
 - ◆ The Legislative Analyst's Office (LAO) forecasts \$2.1 billion more than the Budget forecast for the fiscal year
 - State revenues exceeding the forecast would be available for one-time purposes, including paying the remaining \$1 billion in apportionment deferrals
- The Department of Finance (DOF) projects LCFF gap closure for 2015-16 to be 20.68%, which we estimate will require approximately \$2.6 billion

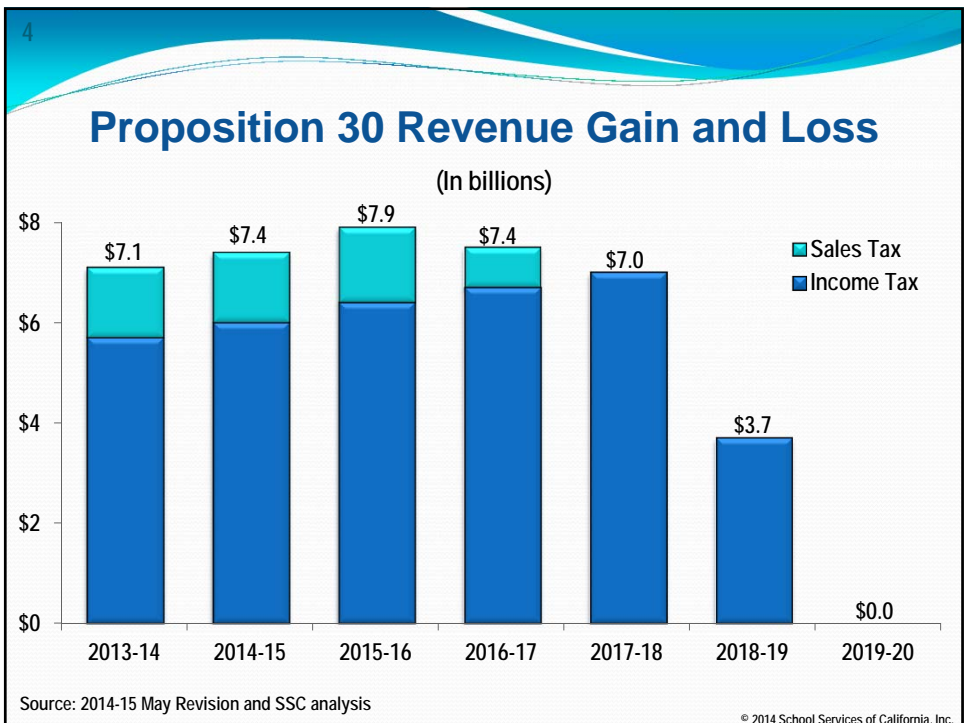
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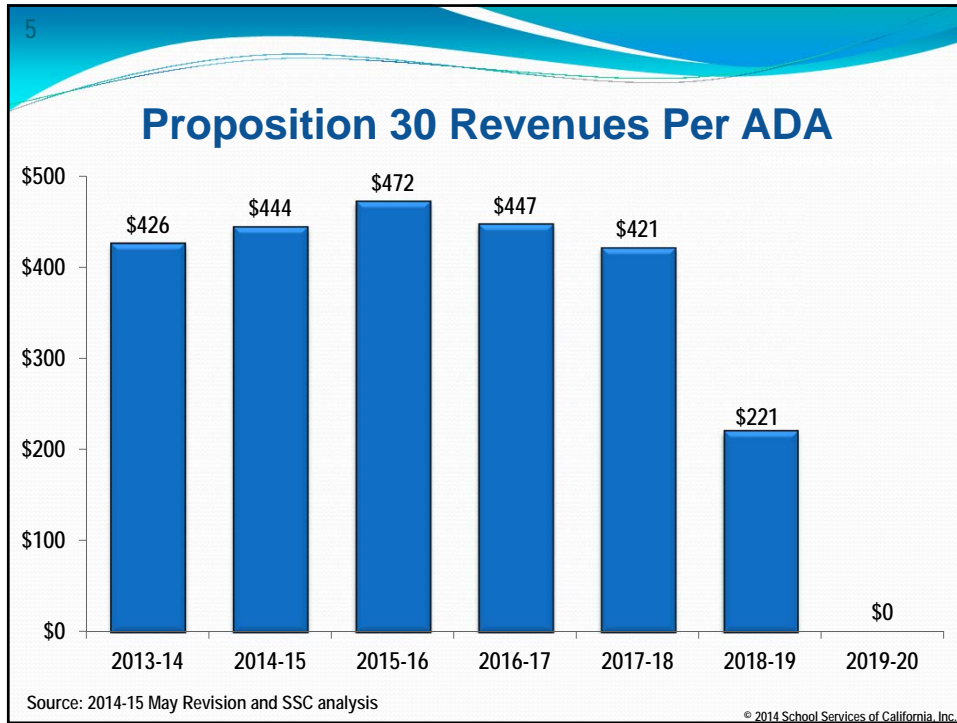
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Proposition 30 Taxes Are Temporary

- Proposition 30, approved by voters in November 2012, temporarily increased the state sales tax and income tax rates for high-income earners to address state revenue shortfalls stemming from the Great Recession
- The higher rates boosted revenues \$7.1 billion in 2013-14 and are forecast to provide \$7.4 billion in 2014-15
- Unless extended by the voters, these higher taxes will expire as follows:
 - The 0.25% sales tax increase expires in 2016 (i.e., the 2016-17 fiscal year)
 - The personal income tax increase expires in 2018 (i.e., the 2018-19 fiscal year)

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The Next Recession?

- Neither the DOF nor the LAO forecast when a recession might occur
 - Their models generally provide a standard forecast based on prior year economic activity
- Some economists analyze business cycles to forecast when recessions will occur
 - These models examine trends in population, interest rates, prices, inventories, raw materials prices, etc.
- IRT Economics, a firm focusing on business clients, forecasts a recession in 2019, based on rising interest rates and health care costs
 - If this forecast is correct, the current recovery will be the longest since the Civil War, according to the LAO
- Any downturn in the latter half of this decade will have profound effects on state revenues because the Proposition 30 taxes expire during this period

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Closing Thoughts: The Governor's Budget for 2015-16

- Release of the Governor's Budget for 2015-16 is fewer than three months away – what can we expect?
- Proposition 98 Growth
 - Revenues exceeding the current-year budget forecast; expect the remaining apportionment deferral to be bought out this year
 - Sufficient revenue growth to achieve the DOF's projection of 20% gap funding in 2015-16, about \$2.6 billion or \$430/ADA
- Rumors around the Capitol
 - Reform of State School Facilities Program
 - ◆ Need-based state assistance: LCFF factors, assessed value per ADA?
 - Categorical funding for Adult Education
 - Accelerated funding for CTE in LCFF
- Legislative initiatives to address CalSTRS/CalPERS funding squeeze

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Thank You!



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