(Elizabeth Hill's Webcast Describing the Fiscal Outlook)

November 14, 2007

California's Fiscal Outlook: LAO Projections 2007-08 Through 2012-13

Summary

Deterioration of the 2007–08 Budget

At the time the *2007–08 Budget Act* was enacted in August 2007, the budget plan focused on closing the gap between General Fund revenues and expenditures for the fiscal year and maintaining a $4.1 billion reserve. Since that time, the 2007-08 budget situation has deteriorated by almost $6 billion. Under our forecast, absent corrective action, the state would end the current fiscal year with a $1.9 billion deficit. The state's dimming fiscal outlook is due to:

- Continued softness in the state's economy lowering the forecast of revenues.
- Lower property taxes, driving state General Fund spending on K–14 education upwards.
- A likely delay in the sale of EdFund and a reduction in anticipated revenues.
- Delayed implementation of new tribal gambling compacts.
- A court-ordered payment to the state's teacher retirement system.

State Also Faces $8 Billion Shortfall in 2008–09

In addition to a negative carry-in balance from 2007–08, we project the state will face an $8 billion operating shortfall in 2008–09. Revenues are projected to grow by 4.6 percent, hampered by the ongoing effects of the weakened economy. On the expenditure side, spending is projected to grow by 7 percent—reflecting both cost increases in most state programs and the end of many 2007–08 one-time budget solutions.

Multibillion Dollar Shortfalls Through 2012–13

Like in 2008–09, we project state costs will exceed revenues by $8 billion in 2009–10. After that, the shortfall will drop to the range of $3 billion each year. The primary factor responsible for this drop between 2009–10 and 2010–11 is that $11.3 billion in previously issued deficit-financing borrowing would be fully paid off in the spring of 2010. This will free up over $3 billion in annual debt service payments beginning in 2010–11.

LAO Bottom Line

In order to balance the 2008–09 budget, the state will have to adopt nearly $10 billion in solutions. Addressing the state's current budget problem is even more urgent because we forecast a *continuing* gap between revenues and expenditures. A plan to permanently address the state's fiscal troubles must involve a substantial portion of ongoing solutions. This is not only because of the persistent operating deficits projected throughout the forecast, but also because of the downside risks inherent with the economy, General Fund revenue volatility, and a wide range of budgetary uncertainties. Making tough choices now will allow the state to move closer to putting its fiscal woes in the past.
