Observations from Economists
Municipal Finance Institute 2020

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The 2021-22 Budget: California’s Fiscal Outlook

Presented to:
League of California Cities

Carolyn Chu
Legislative Analyst’s Office

What Has Changed Since the Budget Passed?

- Rapid Rebound Results in Incomplete, Uneven Recovery
- Spike in Unemployment Was Historic, but Less Than Feared
- Drop in Consumer Spending Was Very Large, but Short-Lived
- Stock Market and Technology Sector Doing Particularly Well
- Safety Net Program Caseloads Have Not Materialized as Anticipated
What Has Changed Since the Budget Passed?

(Continued)

Economic Uncertainty Clouds Outlook

Main Forecast Is Our Best Assessment
Likely Significant Windfall in Upcoming Year

**General Fund Condition Under Fiscal Outlook**
*(In Millions)*

<table>
<thead>
<tr>
<th></th>
<th>2019-20</th>
<th>2020-21</th>
<th>2021-22</th>
</tr>
</thead>
<tbody>
<tr>
<td>Prior-year fund balances</td>
<td>$11,280</td>
<td>$5,550</td>
<td>$32,159</td>
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<tr>
<td>Revenues and transfers</td>
<td>141,851</td>
<td>173,464</td>
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<td>Expenditures</td>
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</tr>
<tr>
<td><strong>SFEU Balances</strong></td>
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<td>Reserves</td>
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<td></td>
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<tr>
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<td><strong>Total Reserves</strong></td>
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SFEU = Special Fund for Economic Uncertainty and BSA = Budget Stabilization Account.

Despite Windfall, Budget Faces Operating Deficit in 2021-22...

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...Which Grows in Future Years

Under Main Forecast, Operating Deficits Grow Over Multiyear Period (in Billions)

- General Fund "Windfall"
- General Fund Operating Deficit

Could the Economy Grow Fast Enough to Overcome Operating Deficits?

How Likely is the Budget to Break Even? General Fund Revenues (in Billions)

The shaded region on the graph shows our estimates of how much revenue might differ from our main forecast. Our estimates suggest revenues are more likely than not to be in the inner shaded area. Revenues in the outer shaded area are less likely. Revenues beyond that are very unlikely. The horizontal point shows the amount of revenue needed for the budget to stay balanced without further reductions.

2009-10
LAO Main $842 $814 $864

2010-11 Break-even Point $190 $182 $185

2011-12 $139 $151 $179

2012-13 $129 $153 $172

2013-14 $139 $153 $172

2014-15 $139 $153 $182

Most of the estimates are below the breakeven point, suggesting the budget is likely to face an operating deficit, even if revenues grow diffusely according to our estimates.
Comments and Recommendations

➢ Recommend Restoring Budget Resilience
➢ Recommend Using Remainder of Windfall for One-Time, Pandemic-Related Needs
➢ Some Early Actions Would Be Reasonable
➢ Recommend Legislature Begin Multiyear Process to Address Operating Deficit Now

Sources of Expenditure Growth

* Excludes CDCR employees.

[Bar chart showing major drivers of cost growth from 2020-21 to 2024-25: Mid-23+1.1%, PSS 16.9%, Employee Compensation -10.4%, Core 2.6%, SS 19.3%, Other 4.2%]
In Contrast to the Rest of the Budget, Funding for Schools Grows

Funding for New Commitments Grows Over Time (In Billions)

- Supplemental payments
- Amount by which guarantee exceeds program cost

Assumes existing programs are adjusted for the statutory cost-of-living adjustment and attendance changes.
10 Year of GDP Growth: San Francisco & the State

Real GDP in San Francisco and California, 2008-18 (2008=100)

Source: BEA
SF Area Down 93K Jobs, Despite Good October

Source: EDD

Tourism Hit Hardest – Private Office the Least

Percentage Change in Employment by Industry, San Francisco Metro Division, March-October 2020

Source: EDD
SF Small Business Closures Higher than Others

Year-over-Year Percentage Change in Number of Small Businesses Open, Select California Cities

Q2: 43% Annual Drop in Sales Tax: Worst in State

Source: HDL
Large Brick & Mortar Losses– No Online Sales Gain

<table>
<thead>
<tr>
<th>Major Industry Group</th>
<th>Count</th>
<th>2020</th>
<th>2019</th>
<th>$ Change</th>
<th>% Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>State and County Pools</td>
<td>8,653</td>
<td>8,146,718</td>
<td>14,827,628</td>
<td>(6,680,910)</td>
<td>-44.8%</td>
</tr>
<tr>
<td>Restaurants and Hotels</td>
<td>10,217</td>
<td>10,714,852</td>
<td>9,079,016</td>
<td>(1,635,836)</td>
<td>-17.9%</td>
</tr>
<tr>
<td>General Government Offices</td>
<td>3,043</td>
<td>3,655,804</td>
<td>3,927,721</td>
<td>(271,917)</td>
<td>-7.0%</td>
</tr>
<tr>
<td>Business and Industry</td>
<td>1,541</td>
<td>2,881,779</td>
<td>3,141,360</td>
<td>(260,587)</td>
<td>-8.3%</td>
</tr>
<tr>
<td>Food and Drugs</td>
<td>833</td>
<td>1,632,742</td>
<td>2,485,040</td>
<td>(852,308)</td>
<td>-34.3%</td>
</tr>
<tr>
<td>Building and Construction</td>
<td>130</td>
<td>624,689</td>
<td>2,445,216</td>
<td>(1,820,527)</td>
<td>-74.4%</td>
</tr>
<tr>
<td>Autos and Transportation</td>
<td>818</td>
<td>52,920</td>
<td>144,347</td>
<td>(91,427)</td>
<td>-63.9%</td>
</tr>
<tr>
<td>Fuel and Service Stations</td>
<td>818</td>
<td>52,920</td>
<td>144,347</td>
<td>(91,427)</td>
<td>-63.9%</td>
</tr>
<tr>
<td>Transfers &amp; Unidentified</td>
<td>130</td>
<td>624,689</td>
<td>2,445,216</td>
<td>(1,820,527)</td>
<td>-74.4%</td>
</tr>
<tr>
<td>Total</td>
<td>51,657</td>
<td>30,790,957</td>
<td>53,790,470</td>
<td>(23,000,113)</td>
<td>-42.8%</td>
</tr>
</tbody>
</table>

Source: HDL

Change in Sales Tax by Zipcode, through June

![Map showing annual change in sales tax by zipcode, 2019Q2 to 2020Q2](image_url)

Source: HDL / San Francisco Controller's Office
SF Total Job Listings Also Lag Other Cities

Year-Over-Year Percentage Change in Total Job Listings, Major California Cities, January-October 2020

Source: Burning Glass / Opportunity Insights

SF Job Listings of Nine Large Tech Companies

Total SF Job Postings for Nine Large SF Tech Companies:
January 2019 - October 2020

Source: Burning Glass / EDD: Companies are Airbnb, Amazon, Apple, Facebook, Google, Salesforce, Square, Twitter, and Yelp.
Mobility Data: SF Residents Stay at Home the Most

Year-over-Year Percentage Change in Time Spent Outside Home in Different Places, San Francisco, February-November 2020

Source: Google / Opportunity Insights

SF’s Drop in Asking Rents is Sharpest in the U.S.

Year-over-Year Changes in San Francisco Residential Apartment Asking Rents

Source: ApartmentList
San Francisco’s economy has been relatively weak during the pandemic, compared to large California and U.S. cities. Clearly, one reason for this has been the relatively high compliance with public health requirements, as evidenced by the Google Mobility data.

The unusual drop in sales tax, the lack of growth in online retail, and the unusually steep decline in the rental housing market all point to increased out-migration, at least temporarily.

If this is true, San Francisco’s economic recovery does not merely hinge on virus abatement, a recovery in consumer spending, and renewed confidence in travel, taking transit, and congregating in large groups. These are challenges that face every city, to various degrees.

The pace of the city’s recovery will also depend on decisions by workers and businesses about the cost and value of San Francisco office space, and Bay Area housing, compared to alternative cities.

One positive factor is the rebound in hiring by large tech companies in the city, which has – at least tentatively – returned to pre-pandemic levels.