

AUGUST 3, 2022

Budget Reserves

PRESENTED TO:

Assembly Budget Subcommittee No. 6 on
Process, Oversight and Program Evaluation
Hon. Philip Y. Ting, Chair



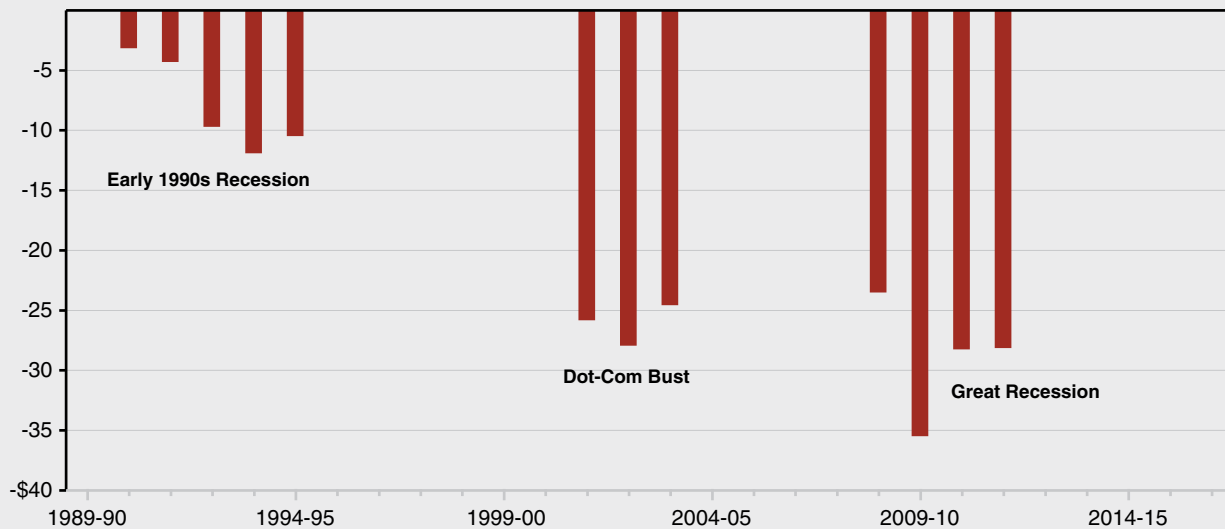
LEGISLATIVE ANALYST'S OFFICE

How Do Budget Problems Happen?

- Budget Problems Most Commonly Occur as a Result of Recessions
- Recession Risk Heightened
- Budget Problems From Most Recessions Are Sizeable

Annual Estimated Tax Revenue Losses by Recession

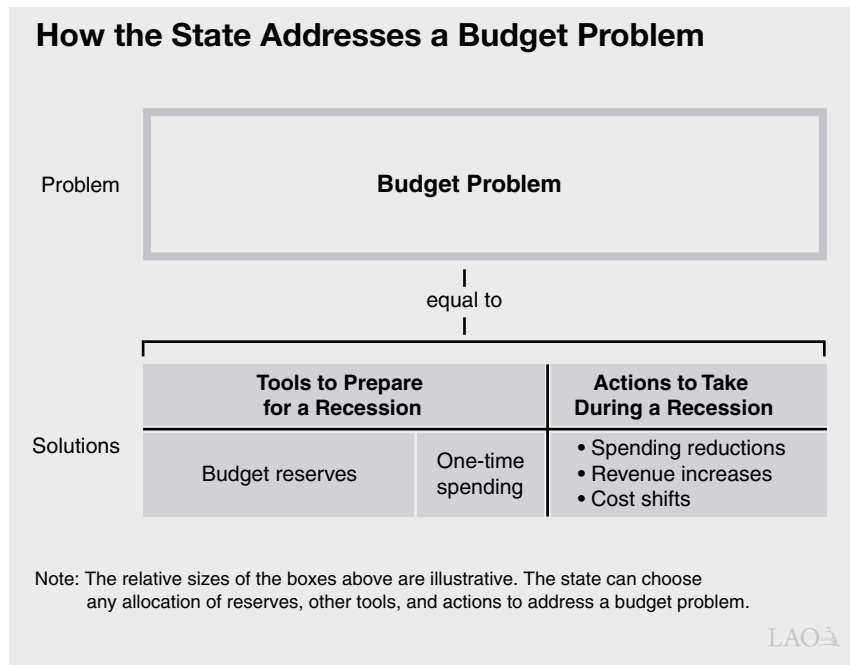
Inflation Adjusted, in 2017-18 Dollars (In Billions)



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How Does the State Address a Budget Problem?



Tools to Prepare

- Deposit funds into reserves.
- Pay down debt.
- Plan for multiyear structural balance.
- Spend funds on a one-time, rather than ongoing, basis.

Actions to Take During a Recession

- Reduce spending.
- Increase revenues.
- Shift costs.



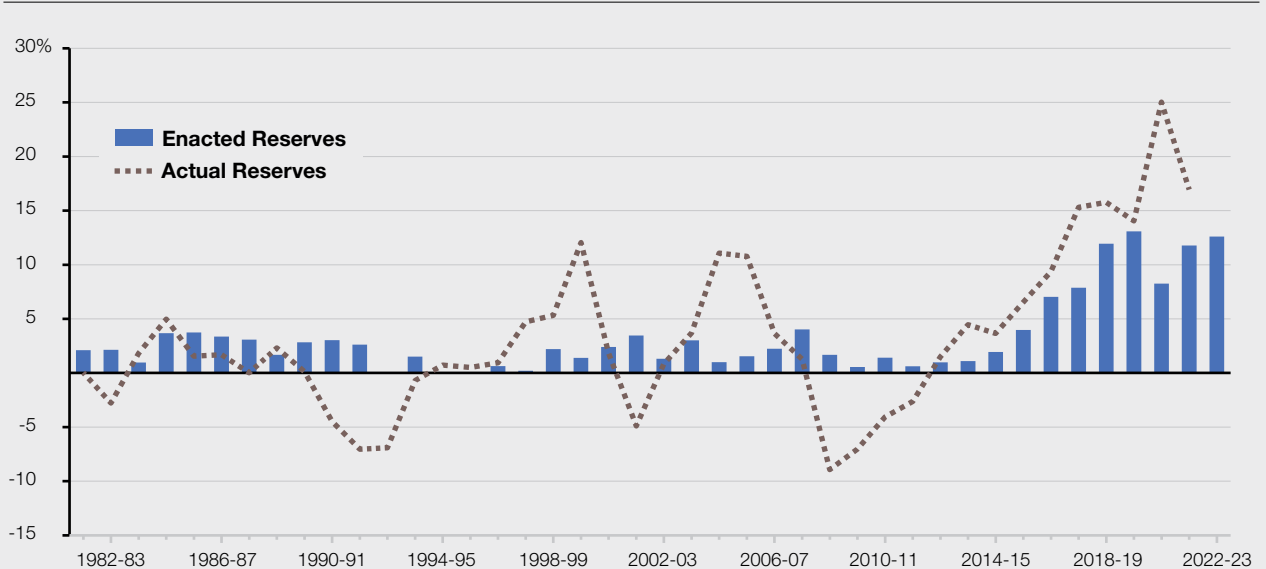
How Much Should the State Save in Reserves?

The optimal size of the reserves is ultimately a legislative policy decision. That is because it involves a trade-off between current expenditures for the support of state programs and potential adverse consequences for these same programs if reserves do not adequately cover revenue losses (and possibly increased costs).

Recent Budgets Have Significantly More Reserves Than Previous Decades

Reserves Today at Historically High Levels

Reserves as a Share of Revenues and Transfers



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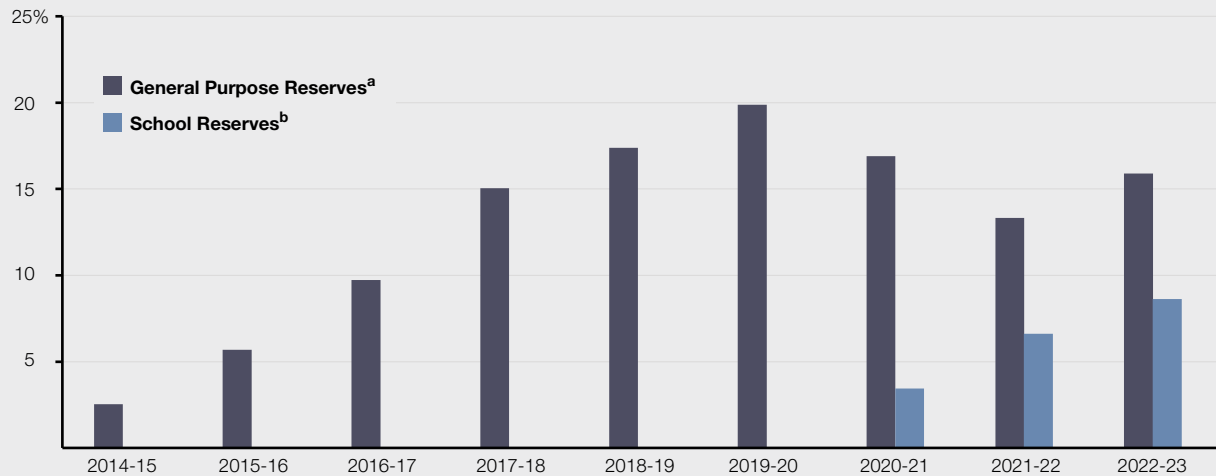


How Much Should the State Save in Reserves?

(Continued)

General Purpose Reserves Have Not Quite Reached Pre-Pandemic Share of Budget

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^a General purpose reserves (including BSA and Safety Net Reserve) as a share of the non-school budget. Excludes Special Fund for Economic Uncertainties because the graphic shows actual, rather than enacted, levels. Actual SFEU balances vary widely depending on fluctuations in revenues.

^b Proposition 98 (school) reserves as a share of overall school budget.

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Comments

- **Recession Risk Heightened.**
- **State Much Better Prepared for a Recession Now Compared to Situation Before Great Recession and Dot-Com Bust...**
- **...However, Despite Historic Revenue Growth, Reserves Have Not Quite Reached Pre-Pandemic Shares of Budget.**
- **Optimal Level of Reserve Is Ultimately a Legislative Policy Decision.**

