Controller John Chiang
California State Controller's Office
November 2009 Summary Analysis | Volume 3, Issue 11

Statement of General Fund Cash Receipts and Disbursements

State Finances in October 2009

⇒ The State's General Fund revenues beat estimates for the month of October. Compared to the estimates in the amended 2009-10 Budget Act enacted on July 28, 2009, total General Fund revenues were up $285 million (7.1%). This was driven by corporate taxes that were $248 million higher (151.3%) than the estimates, and personal income tax revenues that were $10.5 million above (0.4%) the estimates. Sales taxes were $102 million below (-8.9%) the estimate. The total for the three largest taxes was above the estimates by $157 million (4.0%).

⇒ Compared to October 2008, General Fund revenue in October 2009 was down $212 million (-4.7%). The total for the three largest taxes was below 2008 levels by $200 million (-4.7%). Personal income taxes came in $488 million below (-15.8%) last October. However, corporate taxes were up $121 million (41.7%) from last October, and sales taxes were up $168 million (19.1%).

(Continued on page 2)

Budget vs. Cash

The State's budget is a financial plan based on estimated revenues and expenditures for the State's fiscal year, which runs from July 1 through June 30.

Cash refers to what is actually in the State Treasury on a day-to-day and month-to-month basis.

Monitoring the amount of cash available to meet California's financial obligations is the core responsibility of the State Controller's office. On average, the Controller's office issues 182,000 payments every day.

The State Controller's Office is responsible for accounting for all State revenues and receipts and for making disbursements from the State's General Fund. The Controller also is required to issue a report on the State's actual cash balance by the 10th of each month.

As a supplement to the monthly Statement of General Fund Cash Receipts and Disbursements, the Controller issues this Summary Analysis for California policymakers and taxpayers to provide context for viewing the most current financial information on the State's fiscal condition.

This Summary Analysis covers actual receipts and disbursements for October 2009 and year to date for the first four months of Fiscal Year 2009-10. Data are shown for total cash receipts and disbursements, the three largest categories of revenues, and the two largest categories of expenditures.

This report compares actual receipts against historical figures from 2008. A statement of estimated cash flows for the Amended 2009-10 Budget Act enacted on July 28, 2009, are used as estimates for a basis of comparison.

(Continued from page 1)

Tax Revenue Fiscal Year to Date

⇒ Compared to the amended 2009-10 Budget Act, General Fund revenues are below the year-to-date estimate by $794 million (-3.2%). The three largest sources of revenue were lower than estimates by $1.47 billion (-6.3%).

⇒ Sales tax collections year to date were down by $387 million (-4.9%) from the amended 2009-10 Budget Act estimates. Income taxes were $1.17 billion lower (-8.8%) than expected. Corporate taxes came in higher than expected by $92.8 million (4.1%). Because the amended 2009-10 Budget Act estimates contained actual revenue through its late passage, this revenue deterioration occurred primarily between August and October.

⇒ Compared to this date in October 2008, revenue receipts are down by $2.29 billion (-8.8%). This was driven by personal income taxes, which came in $2.2 billion (-16%) below last year at this time.

⇒ Year-to-date collections for the three major taxes were down $2.2 billion (-9%) from last year at this time and corporate taxes were $176 million lower (-7.0%). However, retail sales taxes were up $316 million (4.4%) from last year's total at the end of October.

(Continued on page 3)

What The Numbers Tell Us

Signs of Light...

October's numbers may contain some signs that California's economy is gradually beginning to heal. Both personal income and corporate taxes beat monthly estimates, while corporate and sales taxes also came in higher than October 2008.

The rise in sales tax indicates that consumer activity has begun to stabilize. Several federal programs such as the "Cash for Clunkers" generated significant consumer spending on new cars in the third quarter. The first-time homebuyer tax credit coupled with low home prices has spurred existing home sales over the past two quarters, as well. This also has contributed to increased consumer spending on both durables and nondurables needed for home repairs and alterations. Indeed, the rise in consumption nationally contributed to nearly all of the third quarter increase in the real gross domestic product (GDP).

The State's expenditures also came in below the 2009-10 amended Budget Act estimates by a healthy 3.4%. Both the California State Universities and the Universities of California received ARRA (American Recovery and Reinvestment Act) funds, which were not included in the estimates that contributed to that variance. However, there were other savings at the state and local levels that also added to the overall reduction in October's disbursements.

It is important to note the good news along with the bad. Total receipts for the fiscal year are still below both year-to-date comparisons over 2008-09 and the amended 2009-10 Budget Act. California's unemployment rate was at 12.2% in September, though down 0.1% from August, and the State shed another 38,000 jobs from its nonfarm payrolls since then. New construction is still waning as evidenced by the lack of newly permitted residential units, which were 35% lower on an annualized basis in September 2009 than they were in September 2008.

There is evidence that the State has begun the healing process, but the road to recovery likely will be rocky.

(Continued from page 2)

Summary of Net Cash Position as of October 31, 2009

⇒ Through October, the State had total receipts of $24.1 billion (Table 1) and disbursements of $35.2 billion (Table 2).

⇒ The State ended the last fiscal year with a deficit of $11.9 billion, and the combined current year deficit stands at $23 billion (Table 3). Those deficits are being covered with $14.2 billion of internal borrowing and $8.8 billion in external borrowing.

⇒ Of the largest expenditures, $26.6 billion went

(Continued on page 4)

Borrowable Resources

State law authorizes the General Fund to internally borrow on a short-term basis from specific funds, as needed.

Payroll Withholding Taxes

"Payroll Withholdings" are income taxes that employers send directly to the State on their employees' behalf. Those amounts are withheld from paychecks during every pay period throughout the calendar year.

Revenue Anticipation Notes

Traditionally, the State bridges cash gaps by borrowing money in the private market through Revenue Anticipation Notes (RANs). RANs are repaid by the end of the fiscal year.

Non-Revenue Receipts

Non-revenue receipts typically are transfers to the General Fund from other state funds.

Table 1: General Fund Receipts, July 1, 2009 - October 31, 2009 (in Millions)*

Revenue Source	Actual Receipts to Date	Amended 2009-2010 Budget Act Estimate	Actual Over (Under) Estimate
Corporation Tax	$2,353	$2,261	$93
Personal Income Tax	$12,174	$13,345	($1,171)
Retail Sales and Use Tax	$7,439	$7,826	($387)
Other Revenues	$1,750	$1,079	$672
Total General Fund Revenue	$23,717	$24,510	($794)
Non-Revenue	$403	$463	($60)
Total General Fund Receipts	$24,120	$24,973	($854)

****Note:*** *Some totals on charts may not add, due to rounding*

Table 2: General Fund Disbursements, July 1, 2009-October 31, 2009 (in Millions)

Recipient	Actual Disburse-ments	Amended 2009-10 Budget Act Estimate	Actual Over (Under) Estimate
Local Assistance	$26,638	$26,991	($353)
State Operations	$7,677	$8,687	($1,010)
Other	$887	$776	$111
Total Disbursements	$35,202	$36,454	($1,252)

(Continued from page 3)

to local assistance and $7.7 billion went to State operations (See Table 2).

⇒ Local assistance payments were $353 million lower (-1.3%) than the amended 2009-10 Budget Act and State operations were $1 billion below (-11.6%) these estimates.

Table 3: General Fund Cash Balance As of October 31, 2009 (in Millions)

	Actual Cash Balance	Amended 2009-2010 Budget Act Estimate	Actual Over (Under) Estimate
Beginning Cash Balance July 1, 2009	($11,908)	($11,908)	$0
Receipts Over (Under) Disbursements to Date	($11,082)	($11,481)	$399
Cash Balance October 31, 2009	($22,991)	($23,389)	$399

How to Subscribe to this Publication

This Statement of General Fund Cash Receipts and Disbursements for October 2009 is available on the State Controller's Web site at www.sco.ca.gov.

To have the monthly financial statement and summary analysis e-mailed to you directly, sign up at: http://www.sco.ca.gov/ard_monthly_cash_email.html

Any questions concerning this Summary Analysis may be directed to Hallye Jordan, Deputy Controller for Communications, at (916) 445-2636.

California State Controller John Chiang:

300 Capitol Mall, Suite 1850
Sacramento, CA 95814

P.O. Box 942850
Sacramento, CA 94250

777 S. Figueroa Street, Suite 4800
Los Angeles, CA 90017

Telephone (213) 833-6010
Fax: (213) 833-6011

Telephone: (916) 445-2636 **Fax: (916) 445-6379** **Web: *www.sco.ca.gov***

California Economic Snapshot		
New Auto Registrations (Fiscal Year to Date)	**230,734** Through August 2008	**166,567** Through August 2009
Median Home Price (for Single Family Homes)	**$283,000** In September 2008	**$251,000** In September 2009
Single Family Home Sales	**40,317** In September 2008	**40,216** In September 2009
Foreclosures Initiated (Notices of Default)	**94,240** In 3rd Quarter 2008	**111,689** In 3rd Quarter 2009
Total State Employment (Seasonally Adjusted)	**14,930,947** In September 2008	**14,199,856** In September 2009
Newly Permitted Residential Units (Seasonally Adjusted Annual Rate)	**57,976** In September 2008	**37,468** In September 2009
Data Sources: DataQuick, California Employment Development Department, Construction Industry Research Board, State Department of Finance		

Featured Articles on California's Economy

The opinions in these articles are presented in the spirit of spurring discussion and reflect those of the authors and not necessarily the Controller or his office. This month's report includes an article by Dr. Randall Zisler, President and Chief Executive Officer, and Matthew Zisler, Managing Director, Zisler Capital Partners, Marina del Rey, California.

Overview of the Commercial Property and Capital Markets with Implications for the State of California

By Dr. Randall Zisler, President and Chief Executive Officer
and Matthew Zisler, Managing Director
Zisler Capital Partners, Marina del Rey, California

Overview

⇒ Property values have declined rapidly and should bottom in 2010.

⇒ Capital markets are impaired; an avalanche of maturing debt will present considerable challenges to borrowers, the State and the nation as a whole.

⇒ Vacancy rates in commercial property are approaching their peak, but rental growth will likely turn positive only in 2011 and beyond.

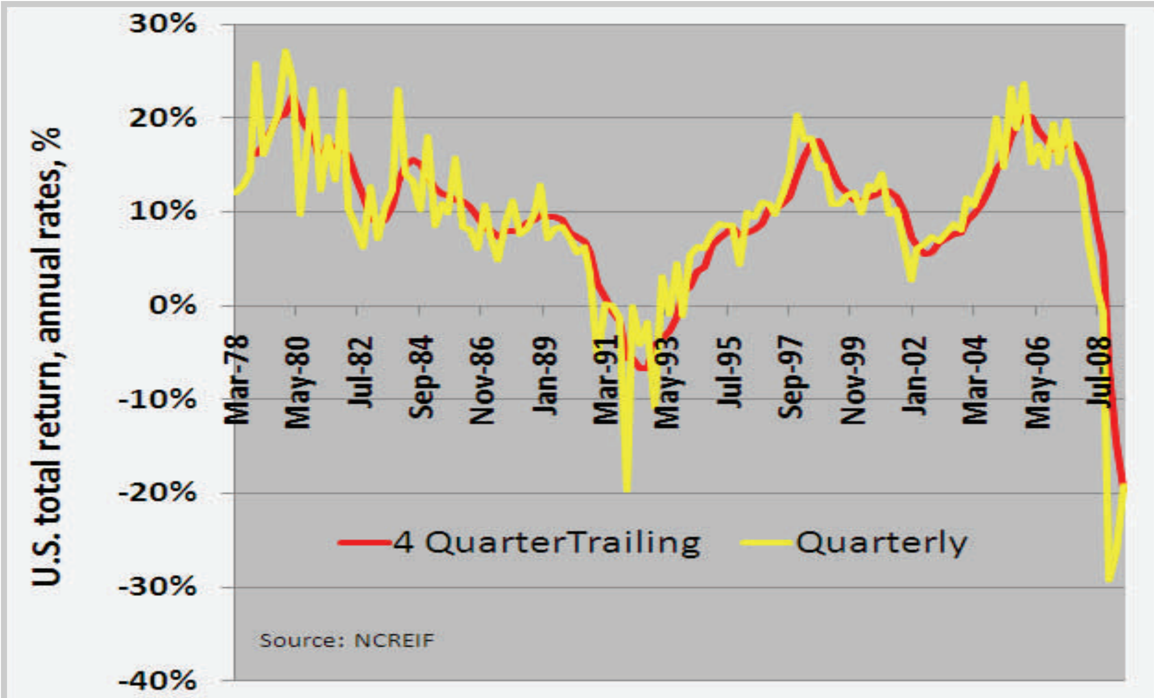
⇒ The dire state of the still-worsening commercial property markets is already adding to California's fiscal woes.

Capital Markets and Valuation

Whereas excessive and imprudent leverage fed the bubble, deleveraging not only popped the bubble, but, in the process, destroyed record amounts of equity and debt. Most deals financed with high leverage from 2005 to the present are under water. The equity is gone and the debt, if it trades at all, trades at a deep discount to face value. Most leveraged equity invested in real estate has

(Continued on page 7)

Chart 1: Total property returns have hit historic lows



(Continued from page 6)

evaporated since property prices, if marked to market, have fallen 30% to 50%.

The chart above shows overall U.S. property total returns, quarterly (at annual rates) and lagging four quarters. This appraisal-based, lagging index shows sharp negative returns exceeding the deterioration of the RTC (Resolution Trust Corp.) period of the early 1990s. (See Chart 1.) Second quarter 2009 returns indicate the possibility that total returns, while still negative, may have hit a point of inflection. We expect that property values in many sectors, especially office, retail, and industrial, will likely deteriorate further in 2010 with improvement beginning sometime in 2011.

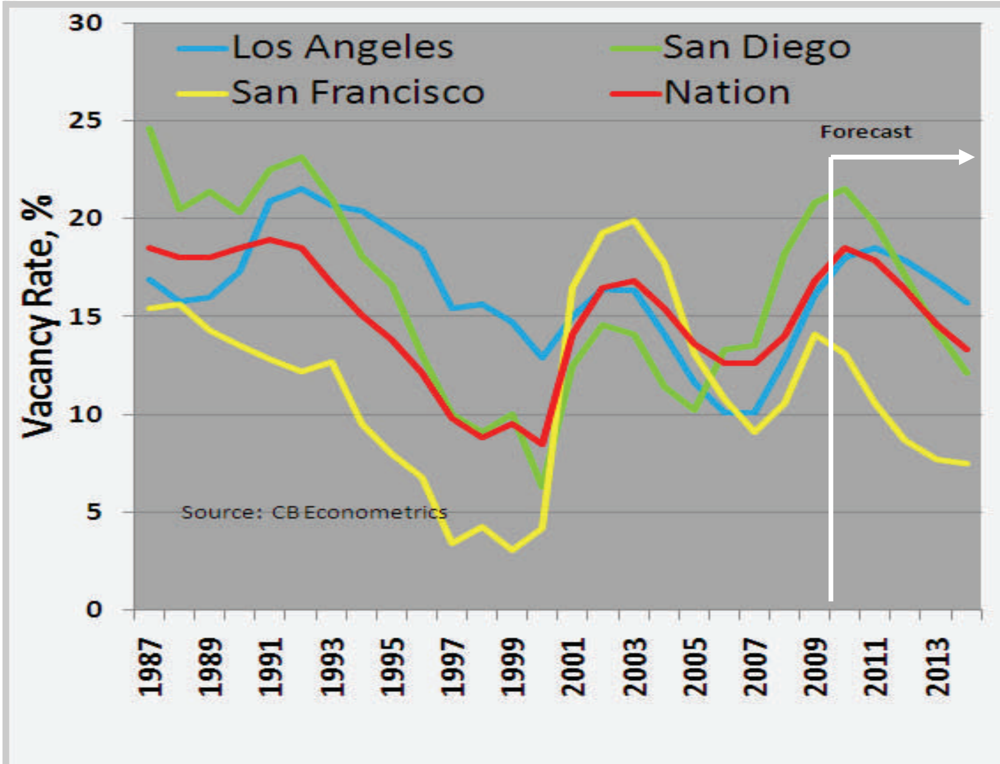
The deflationary spiral is ongoing and likely to proceed much further. The economy is deleveraging, a painful process that spares few sectors, least of all real estate. At present there is a historic capital markets imbalance, the resolution of which awaits the massive in-process repricing of all commercial real estate. We believe that, despite the availability of few sales comparables, the bottom of the cycle is at hand.

A crisis of unprecedented proportions is approaching. Of the $3 trillion of outstanding mortgage debt, $1.4 trillion is scheduled to mature in four years. We estimate another $500 billion to $750 billion of unscheduled maturities (i.e., defaults). Unfortunately, traditional lenders of consequence are practically out of the market and massive amounts of maturing debt will not easily find refinancing. Marking-to-market outstanding debt will render many banks, especially regional and community banks, insolvent, especially as much of the debt is likely worth about 50% of par, or less.

The inability of many banks and other capital sources to lend not just to real estate firms but to other businesses in the State as well presents a

(Continued on page 8)

Chart 2: California and national vacancy rates are peaking



(Continued from page 7)

real challenge to the private sector and state and local governments.

Property—National and California Perspectives

Commercial property operations — occupancy and rental growth — remain weak. The good news is that vacancy rates are peaking in most commercial property categories in California and elsewhere across the nation. The recent trend and outlook for vacancy rates in Los Angeles, San Diego, and San Francisco mirror the nation, as shown in the chart above.

San Francisco, of the three profiled California cities, has the lowest vacancy rate. Since the city's vacancy rate will reach equilibrium sooner, rental growth will turn positive as early as 2010. However, Los Angeles and San Diego will likely lag by as much as two years.

Implications for California

The economic crash and its aftermath are affecting all sectors of the economy, real estate being no exception. Real estate, especially in the transactional sub-sectors (e.g., brokers, etc.), accounts for a significant share of the California labor force. The downturn has created a vicious negative feedback, a symptom of which is still ongoing property deflation and tenant defaults. Attendant symptoms are reduced property tax revenues, failing businesses, decimated transactions volume, and reduced income and sales tax revenues. The extent to which the recovery is delayed will depend on a number of factors, not least of which is the extent and timing of loss recognition by owners and financial institutions.