

# California Fiscal Focus

A Monthly Report from State Controller Betty T. Yee

May 2018

## With May Budget Revision Imminent, CA Controller Reports State Revenues Exceeding Projections

State Controller Betty T. Yee reported California collected more tax revenue during the month of April than in any previous month of the 2017-18 fiscal year so far. Moreover, total April revenues of \$18.03 billion were higher than estimates in the governor's FY 2018-19 proposed budget by 5.3 percent.

For the first 10 months of the 2017-18 fiscal year that began in July, total revenues of \$107.13 billion are \$4.72 billion above estimates in the enacted budget and \$3.82 billion higher than January's revised fiscal year-to-date predictions. Total fiscal year-to-date revenues are \$10.25 billion higher than for the same period in FY 2016-17.

For April, personal income tax (PIT) receipts of \$14.17 billion were \$715.9 million, or 5.3 percent, higher than estimated in January. For the fiscal year, PIT receipts are \$2.58 billion higher than anticipated in the proposed budget. Traditionally, April is the state's peak month of PIT collection.

April corporation taxes of \$2.40 billion were \$78.4 million higher than forecasted in the governor's proposed budget. For the fiscal year to date, total corporation tax receipts are 13.5 percent above assumptions released in January.

Sales tax receipts of \$946.1 million for April were \$139.1 million, or 17.2 percent, higher than anticipated in the governor's FY 2018-19 budget proposal. For the fiscal year, sales tax receipts are in line with the proposed budget's expectations.

Unused borrowable resources through April exceeded January projections by 36.9 percent. Outstanding loans of \$4.52 billion were \$6.35 billion less than the governor's proposed budget expected the state would need by the end of April. The loans were financed entirely by borrowing from internal state funds. For more details, [read the monthly cash report](#).



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## Perspectives on Demand, Supply, and Affordability Amid California Housing Shortage

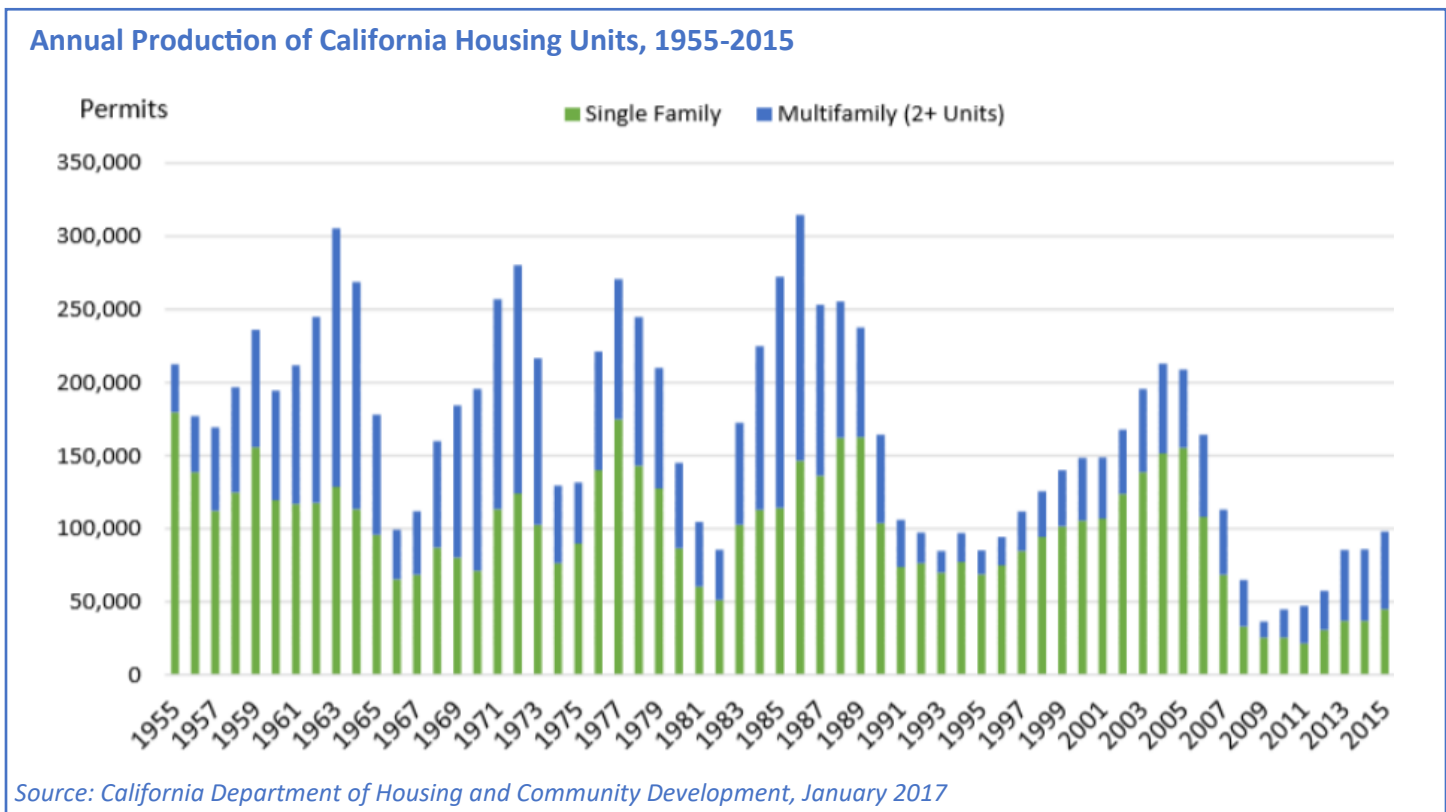
California has a severe housing shortage that is damaging our economy. The state’s Housing and Community Development Department (HCD) estimates California needs to build a minimum 180,000 units per year statewide to meet existing demand, yet only 80,000 new units per year were added to the state’s housing stock over the last decade. Except during four recessions, California’s housing construction exceeded 200,000 units per year from the mid-1950s to 1990. Since then, housing construction only exceeded this benchmark in the boom years of 2004 and 2005. Moreover, much of the construction during the latter half of the 20<sup>th</sup> Century was multifamily rental units.

The McKinsey Global Institute offered even more dire estimates in 2016, noting California’s housing stock ranked 49<sup>th</sup> nationwide and concluding the state needs to build upward of 250,000 to 400,000 units per year in the next 10 years to meet demand and catch up to other states. McKinsey estimated the housing shortage cost

California’s economy \$140 billion per year, or six percent of gross domestic product. Using another method in 2017, [economists from the University of Chicago and UC Berkeley demonstrated](#) the negative impact of housing constraints on economic growth from diminished labor mobility in major U.S. cities.

These studies also underscore the negative impact of the housing shortage on the state’s most vulnerable workers and families. McKinsey points to a \$50 billion annual housing affordability gap, with six billion California households unable to afford housing, with the largest concentration in the greater Los Angeles area and the San Francisco Bay Area. According to HCD, three million California renter households pay more than 30 percent of their income for rent, while another 1.5 million pay more than 50 percent. Twenty-two percent of the nation’s homeless population lives in California.

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The state's nonpartisan [Legislative Analyst's Office](#) (LAO) and UC Berkeley's [Institute of Governmental Studies](#) (IGS) say an increase in housing supply would benefit Californians across the economic spectrum. Alleviating the housing supply shortage would benefit both employers and workers. Employers are concerned about the cost of housing and attracting employees to fill positions needed to maintain growth, while workers struggle to manage expenses as the relative cost of housing to wages continues to grow.

Moreover, several studies from the National Bureau of Economic Research (NBER) indicate the cost of building new housing hurts workers at the macroeconomic level. Two recent papers by the [American Economic Association](#) and [NBER](#) discuss how the price of housing regulations can exceed the cost of building new housing, particularly in economically productive urban regions such as the Bay Area and greater Los Angeles. [Another NBER paper](#) relates how cost barriers to building new housing in economically productive areas limits the opportunity of less-skilled workers to move to higher-income areas. The result is a dual loss, both of potential additional income to individuals and of growth to the economy.

As policymakers struggle with new measures to positively influence housing affordability, some of the strongest resistance comes from individuals with deep ties to existing communities. These include homeowners in more affluent neighborhoods, as well as renters and small businesses struggling with the impact of gentrification on less-affluent areas that have suffered disinvestment and neglect in the past.

Much of the analysis of the impact of supply and demand on housing and worker mobility is less consequential at an individual level. For example, mobility in the housing market also relates to concerns about gentrification and displacement [as discussed by Lance Freeman](#) of Columbia University, who focuses on moderate-income household migration into gentrifying neighborhoods to examine the net effect of gentrification. Freeman and other economists argue housing market mobility can overstate the impact of gentrification on displacement in some

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areas, but he acknowledges that rising prices leave lower-income residents with few choices as they move.

While IGS and LAO agree on the need for additional housing supply to address costs, they disagree on the extent to which subsidies are needed to meet the needs of lower-income residents in a constrained market. IGS suggests that much of the new market-rate housing built since 2000 is unlikely to become more affordable through filtering – a process where housing stock ages and becomes more affordable – for generations.

IGS suggests investments in subsidized housing for lower-income residents are twice as effective at alleviating displacement of lower-income households, but the relative impact of subsidized versus market-rate housing on displacement differs substantially from place to place. For example, IGS closely examined two parts of one census tract south of San Francisco's Market Street, both of which experienced significant market-rate and subsidized housing production since 2000. One area showed signs of displacement and rising rents, while the other did not. IGS did not find a conclusive reason.

[Stanford University research](#) on the positive economic impact of inclusionary housing policies and low-income housing tax credits (LIHTCs) shows significant sensitivity to neighborhood-level variables, including an area's history of segregation. This research relies on the necessity of building new housing supply to meet growing housing needs at all income levels and to address historic disinvestment. From the high cost of regulatory interventions to the overall cost of shelter, many acknowledge the need to better target scarce resources.

## California Population Changing with High Housing Costs

For the last quarter-century, domestic migration has shown greater numbers of Californians migrating to other states than residents of other states migrating to California. The state's nonpartisan Legislative Analyst's Office (LAO) recently reported California experienced net negative domestic migration by one million residents over the last 10 years. Notably, the difference between residents moving in and out of California narrowed more during the last decade than the prior 15 years.

LAO data also indicate that – notwithstanding overall net-negative migration – California has gained more people with higher incomes and higher levels of education. The LAO report does not offer reasons for the relative gains in more affluent or educated migrants from other states. [Next10 issued a report](#) prepared by Beacon Economics juxtaposing population, housing, and employment data and using the same population data source as LAO.

The additional data used by Beacon Economics show migration of more highly educated people into the Bay Area, which has the most robust growth in higher-wage jobs. High- and middle-wage jobs in southern California also attract interstate migrants, but any influx is offset by a greater proportion of lower-wage jobs and net-negative migration consistent with their job mix. Wage levels in rural California also are consistent with patterns of net-negative migration.

Next10 and Beacon Economics attribute these migration trends to higher housing costs. The report relates some of the most severe housing shortages in rural California to these population trends. Inexplicably, however, housing has been constructed in California at lower rates during the last 10 years than the previous 15-year period.

Notwithstanding net-negative domestic migrations, California's population has continued to grow from international migration. California is home to more than a quarter of immigrants to the United States, according to the [Public Policy Institute of California](#) (PPIC). PPIC data suggest overall immigrant incomes are lower, but immigrants work at similar rates as U.S.-born residents. Data from Next10 and Beacon suggest international immigration trends show an increase in educated migrants seeking high-wage employment, although at different levels.

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