CALIFORNIA FOUNDATION ON THE ENVIRONMENT AND THE ECONOMY

CFEE SEMINAR

"Even the Longest Journey Begins With a Single Step..."
- The Road to Recovery

Tuesday, May 19 | 11:00am

Public Debt-Financing in California

With the 2020-21 state budget deficit estimated to range between $18 and 31 billion[1] or as high as $54 billion,[2] California will have to look to additional funding sources to stimulate economic activity on the scale needed to prevent further economic contraction and invigorate recovery efforts. The same holds true for local governments, which the League of California Cities project to collectively suffer $7 billion in lost revenues over the next two years.[3] [4]

One instrument for helping to launch an economic recovery is debt-financing. In broad terms, there are two ways that debt can play a crucial role in California's economic recovery.

1. Unspent Voter-Approved Debt

Prior to the COVID-19 pandemic, California voters and the Legislature approved General Fund-supported bonds to be spent on projects ranging from transportation and water infrastructure to public facilities like schools, hospitals, and more. While much of this money has already been disbursed, there remains up to **$42 billion** in authorized bond funds that have not been sold.[5] [6]

In addition to unissued state debt, local governments too have authorized indebtedness that has not yet been expended. For instance, California school and community college districts have yet to access **$52.4 billion** in voter-approved general obligation bonds.[7] Cities, counties, special districts, and other local agencies also possess the ability to issue bonds for debts, some approved by voters and others only requiring board approval.

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[1] The 2020-21 Budget: California's Spring Fiscal Outlook. *Legislative Analyst Office*. May 8, 2020 https://lao.ca.gov/Publications/Report/4228
[2] Revised Budget Summary. *The Department of Finance.* May 15, 2020. http://www.ebudget.ca.gov/home.php
[3] Support Local Recovery Coalition. *League of California Cities*. April 2020. https://www.cacities.org/Policy-Advocacy/Hot-Issues/Support-Local-Recovery
[4] Municipal revenue shortfalls are based off a June 1, 2020 reopening of the economy. The projected deficit will increase as "Stay at Home" orders are extended or re-instituted.
[5] "Overview of State Bond Debt". *California Secretary of State.* March 2020 https://voterguide.sos.ca.gov/voter-info/overview-state-bond-debt.htm
[6] There are also other types of state-supported debt that have not been issued
[7] "K-14 Voter Approved General Obligation Bonds: Authorized, But Unissued – 2020 Update" *California Debt and Investment Advisory Commission (CDIAC)* https://www.treasurer.ca.gov/cdiac/publications/k14update-2020.pdf

As state leaders grapple with dramatic reductions in the General Fund, uncertainty about federal stimulus packages, and the political and economic pain to increase taxes, this previously approved financing represents "low-hanging financial fruit" that could help seed recovery efforts. And while these funds are often obligated to specified projects and programs, there are key questions worth exploring regarding their disbursal:

- How quickly can such monies be expended?
- Can their disbursal be coordinated in ways that support a broader statewide recovery strategy?
- Is it prudent to proceed with debt issuance – either expedited or business-as-usual – while public revenues are experiencing an acute decline?
- Can these projects be part of the "greening" of the state's infrastructure?

2. Excess Debt Capacity

Beyond the issuance of previously approved debt, a potentially even larger pool of funding exists if state and local agencies were to activate their "excess debt capacity." Simply put, the excess debt capacity is the additional amount of money that an agency can borrow, *but is not already borrowing*, while remaining in a financially sustainable position.

Each public agency has its own unique revenue streams, asset holdings, expenses, and thus, its own unique capacity to take on new debt.[8] Although the total statewide debt capacity is difficult to determine due to the diversity of public entities throughout California, it is conceivable that there are **tens of billions of dollars** of excess borrowing capacity.

To better understand this untapped resource, state leaders may think through the following questions as they develop comprehensive strategies to spur an economic recovery:

- What is the total debt capacity of all public agencies in California?
- How can the state incentivize agencies to swiftly leverage their own debt capacity to support recovery efforts?
- How much additional funding – from private investors and/or federal stimulus – may be attracted on the basis of having debt-financing already in place and specific projects lined up?
- During the Great Recession, how did agencies debt-finance their projects without overleveraging themselves during a similar period of declining revenues?

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[8] Capital Financing and Debt Management. *Institute for Local Government.* January 2013. https://www.ca-ilg.org/sites/main/files/file-attachments/capital_financing_and_debt_management.pdf?1401990866