How We Lost the California Dream, and How to Get It Back

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Presentation Theme

• Compare CA economic outcomes with quality of governance over two periods of time
• (1) 1950s – 1970s, rapid growth, small government budgets
• (2) Post-1970s, slower growth, large government budgets
• We will see large differences in efficiency, priorities, and accountability of government between these 2 periods
Presentation Theme

• Today, we have:
• Large inefficiencies
• Organization failures within gov’t
• Costly regulations protecting politically important groups
• Government prioritizing spending of pet projects over highly valued, priority items
• Failed governance ended CA Dream
Presentation Theme

- Why has quality of governance declined?
- (1) Lack of accountability, reflecting a sea change in culture within gov’t
- (2) Lack of incentives within government
- (3) Public-private partnership became adversarial
- Nonpartisan ideas to help restore the dream
The Birth of the California Dream

• In 1900, CA just 2 million people, 2.5 percent of U.S.
• Mississippi was larger, Ohio 4 times larger,
• Chicago nearly as large
• 1970, 20 million: nearly 10 percent of U.S. population
• Just 5.1 million by 1970 if California had grown at the national average.
How Did We Manage California’s Enormous Growth?

• Young population – 50% under 24 years
• Meant relatively few taxpayers, but big budget demands, including:
  • *Schools, hospitals, water, roads, utilities...*
• Financed with a per-person state budget just 13% of today’s budget!
• *But we found a way to make these investments, & CA flourished*
How Did We Pull This Off? A Successful Vision of State Governance

• (1) Spending focused on priorities
• (2) Very efficient, low cost
• Capital spending was 25% of budget!
• Top-rated schools & universities, major water, road, & utilities investments, creation of new towns and cities
• Gov’t facilitated creation of the dream – highly effective public/private partnership
Shared Bipartisan Vision of Focused, Efficient Government

• Governor Pat Brown’s budget statements:
• “We must invest to accommodate our magnificent growth. Our priority is to protect & invest”
• “We can’t abuse taxpayers. We must use their precious tax dollars wisely.”
• “Return on our public investments must be at least as high as on private investments.”
• California flourished – We realized CA dream
The California Dream Was Realized

- Population grew from 7 million to 20 million
- Broad economic base (finance, aerospace, entertainment, energy, tourism services)
- Top-rated schools and public universities
- Top-rated water systems, roads, highways, electrical infrastructure
- Housing much more affordable than now (35% premium, compared to 118% premium today)
California Today: Lots of Spending, But Not Much to Show For It

- Population declining (500,000 drop since 2020)
- 2020 population projection (made in 2020) was off by 1 million
- Per-person (inflation-adjusted) spending is 7.5 times higher today than 1960s, but...
- Basic gov’t functions not getting done
- What’s not getting done? Public investments
- Capital spending only 4% of state budget
- This doesn’t even cover depreciation
Consequences of Our Failure to Adequately Invest

• California infrastructure graded D+ by Society of Civil Engineers
• 1,680 Dams in Risky Condition
• 70% of our dams over 50 years old
• 1 out of 18 bridges structurally deficient
• 50% of bridges have exceeded lifespan, including high traffic routes (I-5, I-80, 101)
Consequences of Our Failure to Adequately Invest

- Deficient CA roads cost drivers $61 billion per year
- Fewer usable miles of roadway today than in 1990
- Commuters burn additional 296 million gallons of gasoline annually, stuck in traffic
- CA road quality is 49th in country, despite 2nd highest state gasoline taxes in country
- Recall Gov. Pat Brown: “Government’s priority is to invest; we can’t abuse taxpayers. We must use their precious tax dollars wisely.”
California Today:
Consequences of Not Investing

• Oroville Dam 2017 failure (built in 1968)
• 188,000 were evacuated
• Identified for retrofitting in 2005
• Cracks in Dam reported in 2013-15...
• $1.1 billion to fix failed dam
• Compared to estimated $60 million retrofit
• Why wasn’t this investment made?
California Today:
Consequences of Not Investing

• 2018 Santa Barbara Mudslides
• 23 dead, over $500 million in damages
• Debris flow basins not cleared for decades; capture capacity declined 60% - noted in 2005
• Insufficient budget, environmental lawsuits
• Army Corps of Engineers warned “Danger of loss of life is great”, “Lack of Adequate Maintenance” of debris basins
California Today: Consequences of Not Investing

• 2023 California Storms
• 17 dead, $30-$34 billion in damages from flooding
• Much of California’s storm drainage system was built in 1940s or earlier (LA system built in 1915)
• California’s storm drainage graded D+ by Society of Civil Engineers
California Today: Consequences of Not Investing

• Many water pipes 60 years or older
• 228 billion gallons of water lost each year due to pipe failures
• No new major water investments since California Water Project (1973)
• Since 1996, voters have approved $27 billion in bonds for new water projects
• Most of the funding is yet to be spent...
California Today: Consequences of Not Investing

- Senator Feinstein: “We have same water infrastructure as when population was 16 million”
- *Semi-regular drought brings water rationing, damages state agriculture, creates uncertainty*
- *California suffers damages when it rains, and when it doesn’t rain…*
- *Why haven’t we made investments?*
California Today: Consequences of Not Investing

- 9 of 10 biggest CA fires since 2012
- $422 billion losses from 2022 Camp Fire alone
- Over 2,000,000 properties now at risk
- *Since 2005, California’s greenhouse gas reductions offset by wildfire emissions*
- Doesn’t include particulate emissions and their impact on health and mortality
- **High value priorities are not being addressed**
California Today - Failed to Invest in Infrastructure

• 4,600 miles (46%) of LA sidewalks are broken & identified as an injury risk
• Inadequate repair budget, LA faces 400 personal injury litigations annually from those injured on sidewalks
• Pat Brown (1961) – “Government’s priority is to protect and invest” - basics aren’t getting done
California Today - Failed to Invest in Public Services

- Employment Department’s 40-year old IT system crashed in 2020, 1.5 million unemployment claims backlogged for months...
- ...While $32 billion paid in fraudulent claims
- As many as 60 different claims sent to 1 address
- In private sector, IT system wouldn’t be obsolete
- Because competition incentivizes efficiency
- We need to improve incentives & accountability in government
California Today - Failed to Invest in Housing

• California is 49th in construction & affordability
• San Francisco & Silicon Valley highest income...
• But only 18 percent of SF & Silicon Valley households can afford median-priced home
• 2/3 of households can afford median-priced home in rest of country
• Why aren’t we building enough housing?
California Today - Extremely Expensive for Many

- CA living costs 45% higher than national average
- 4th highest electric costs, 2nd highest gas prices
- 34% live in poverty or near poverty
- At least 25% of country’s homeless in CA
- 13 million Californians on Medicaid – would be 5th largest state in U.S.
- Qualify for Medicaid if income under $41,000 (family of 3)
- California Dream unattainable for most
How Did We Lose Our Way?

- **Shared principles of governance changed**
- Began late 60s/early 70s, reflecting political & cultural changes, and birth of *Environmental Movement*
- We made the mistake of not addressing environmental damages
- But Environmental Movement became highly politicized
- It now dominates much of what can – and can’t – be done in the state
Environmental Policy Not Adequately Disciplined by Economic Principles

- California Environmental Quality Act (1970)
- “…Adopt all feasible measures to mitigate environmental impacts of development”
- Feasible doesn’t mean practical. Or in the best interests of society.
- CEQA inconsistent with central principle of economics – we face tradeoffs.
- Over time, we gradually abandoned fiscal responsibility and an efficient public sector
CEQA & California Housing

- CEQA reduced housing supply, increased construction costs
- CEQA “weaponized to fight development”
- *Between 1940 & 1970, California housing cost 35 percent more than rest of country*
- Because supply grew with demand
- *After 1970, construction dropped & house price premium rose to 80 percent by 1980*
Housing Prices Rise -
Supply is Constrained by Regulations

• Today, CA home to 10 of 11 most expensive housing metro areas in country
• 10 of 12 most expensive rental
• CEQA and other regulations are major factor in reducing supply and increasing construction costs
Today’s California Housing Crisis

- **Median CA Single-Family Home:** $716,000
- **Median CA Condo:** $500,000
- Rest of country single-family home: $328,000
- CA price premium increased to 118%
- If premium remained 35%, then median CA home price would be $443,000 today
CEQA Creates Enormous Inefficiencies

• Newhall Ranch – 60,000 population planned community near Valencia
• Plans submitted in 1994
• 25 years to resolve CEQA-related lawsuits
• Community size scaled back significantly.
• First homes might be available in 2023
• Enormously inefficient and socially costly
• There have been calls for CEQA reform for decades. Why hasn’t CEQA been modified?
Loss of Fiscal Discipline & Efficiency – Building Costs Skyrocket

• Santa Clara County bought “extended-stay” motel for $14 million, converting to apartments
• This is a “property flip” – adds just communal kitchen, laundry facilities, & some recreation
• At a cost of $15 million...something is wrong.
• And no one seems to be questioning this.
• Why?
Loss of Fiscal Discipline & Efficiency – Budget Skyrockets

• Palo Alto is preserving a mobile home park at a cost of over $700,000 per space
• LA affordable housing is costing $837,000 per unit to build
• SF renovating apartment buildings at cost of $1 million per apartment
• This is not “affordable housing”

• Where is the accountability? Where is the respect for taxpayers?
Loss of Fiscal Discipline & Efficiency

- $300 billion state budget – over $20,000 per household
- 7.5 times larger than in the days of Pat Brown
- 5th highest personal tax burden
- 3rd highest business tax burden
- Per-capita budget 70 percent higher than 2013-14 state budget – have services improved?
- Where is the accountability to taxpayers?
California Loses Major Businesses as Regulations, Taxes & Costs Rise

• Hewlett-Packard, Toyota, Nissan, Nestles, Occidental Petroleum, Schwab, Tesla, Oracle, CB Richard Ellis

• Number of business relocations doubled in 2022
• Relocating to low-cost states (TX, FL, NV, Tenn)
• CA 49th in business-friendly policies
• CA 48th tax rates
• CA 49th in economic freedom rankings
• Why aren’t policy makers addressing these issues?
Investments Gone Sideways

• **California High-Speed Rail**
  - $33 billion budget to link the state, north to south, central valley to the coasts, 2018 completion, with 220 mph train travel
  - Sounded like a winner, but no one was watching the hen house...
  - State delegated most aspects of project to consultants, who were large contributors to 2008 state bond issue
**Investments Gone Sideways**

- **Today** - $105 billion estimate to build LA to SF leg, but this based on 2019 estimates
- **There is no chance** the full system – the one that was sold to voters in 2008 – will be built
- **One of the major benefits from project** was **reduced carbon emissions**, but state is **banning gasoline-powered vehicles by 2035**...
Investments Gone Sideways

• Bakersfield to Merced route is planned for completion.
• When? 2033 (maybe) at a cost of $33 billion (maybe).
• Imagine voters being asked in 2008 “Would you approve $33 billion for high-speed rail between Bakersfield and Merced, and it won’t be operative for 25 years.”
• “Respect the taxpayer.” Where is the accountability?
Restoring the Dream

• No magic wand is needed...
• Application of standard economic principles & focused leadership
• Incentivize efficiency, increase accountability
• Restore principle that budgets are sacred
• We can make investments, support growth and do a better job of protecting the environment
Restoring the Dream - Housing

• Remove constraints to building. And build at a lower cost.

• Need CEQA reforms, including eliminating duplicative lawsuits, procedural reforms to eliminate delays, full disclosure of identities of parties.
Restoring the Dream - Housing

• Urban growth boundaries (UGB) and Local Area Formation Commissions (LAFCO) stand in the way of creating new communities.
• These restrict footprint of cities and create boundaries between urban/residential land and greenbelt and agricultural land.
• And new communities (think new suburbs) have substantial advantages in creating new housing
Restoring Efficiency & Accountability in State and Local Government

- 2/3 of state budget just for K-12, health and human services, prison system
- All should perform much better – incentivize efficiency & require accountability
- Review compensation standards
- Reward high performance and hold leaders accountable for organizational outcomes
- State worker compensation twice as high as private sector $143,000 (2019)
Restoring Efficiency & Accountability - Prison System

• CA prisons cost $90,000 per inmate - twice as much as rest of country
• Politically powerful union
• Compensation twice as high as national average
• Resists reforms that would reduce recidivism
• Only 3 percent of budget spent on education, job training, & behavioral therapy, combined
• Repurpose budget, focus on improving post-prison outcomes, create incentives to do this
Restoring Efficiency & Accountability - Medicaid (Medi-Cal)

• Medicaid - Inefficient, inadequate accountability
• $4 billion paid in ineligible claims
• 2016 review:
  • “Integrity & compliance remain problematic”
  • This was same statement as the 2012 review
• Poor patient satisfaction – patients increasingly use ER & urgent care for basic health services
• Health outcomes about same for Medicaid patients and patients with no insurance
Restoring Efficiency & Accountability - Medicaid (Medi-Cal)

- 2019 State Auditor Report: Medi-Cal ranks 40\textsuperscript{th} among U.S. states for pediatric care
- System suffers from “deficient oversight”
- Hold leaders accountable for system performance – we see poor performance, year after year, including chronic problems that are never resolved
- Increase competition among providers
Restoring Incentives & Accountability—K-12 Education

• CA schools were once top-ranked.
• K-12 today ranked 44th in math, 38th in reading
• Just 1 out of 3 kids at grade level in math and English language skills
• We need competitive merit & specialist-based pay
• Sensible teacher tenure reform
• Create a mindset of innovation
• This was platform of Marshall Tuck (D), who narrowly lost 2018 Superintendent race
Conclusions

• *There is a better way*

• Return to what Governor Pat Brown emphasized 60 years ago

• Efficiency. Respect the Taxpayer. Prioritize what citizens really want

• To do this, we need accountability and appropriate incentives within government organizations

• *This will help restore the California Dream*
Thank You!

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