



BEYOND -the- RECESSION

Are better times ahead for
public education?

By Julie Phillips Randles

Imagine the national economy as a hospital trauma unit patient. At the end of 2009, the patient was in the recovery room and out of imminent danger. The bleeding had stopped, but the patient remained anemic and was listed in serious condition.

Such is the assessment of economic experts who say the patient, known as The Great Recession, is out of the woods and has begun a fragile recovery. The economy is growing (sparsely), layoffs have slowed, wage growth is slight and credit is tight.

But if all agree the patient is improving, when will the patient be on his feet again working hard enough to provide a payday for California's public school system?

That's where the prognosis gets iffy. But a look at the national economy, California's place in the recovery and what's expected in the coming year begins to yield a clearer picture of the patient's overall health.

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Evidence of improvement

The Great Recession officially began in December 2007 and was the deepest economic downturn since the recession of 1981-82, according to Nancy D. Sidhu, chief economist at the Kyser Center for Economic Research and a frequent speaker at CASBO's CBO Symposium. "It looks for the moment that the economy has stopped falling. We're still near the bottom in terms of the level of activity, but we're moving in the right direction," Sidhu said.

What's not clear is whether this will be anything more than a slow recovery "largely because there won't be money to borrow, and that could take some time," she added.

Sidhu is also keeping her eye on consumer spending, especially such key products as vehicles, furniture, appliances and building materials, all of which have been in decline in the past year. Having said that, U.S. data shows retail sales were at their worst at the end of 2008, were flat until the summer of 2009 and have since been slowly rising. "So that's promising," said Sidhu.

Richard C. O'Sullivan, principal at Change Management Solutions in Maryland and a speaker at ASBO International's 2008 economic summit, agrees that the economy is in recovery mode and said "the evidence of that is the turnaround in employment and household savings."

As to the show-me indicators: "My rejoinder to those who say 'look at indicators we've always looked at – those haven't turned yet' I say you've missed the point. This recovery is going to be different.

"The national economy today is in transition from an economy driven by short-term consumer demand to (one driven by) long-term investment both by retiring baby boomers and businesses," O'Sullivan summed up.

Overall, the experts say the country's in for modest economic growth in 2010. Sidhu referred to the current economy as "freshly off the bottom," adding "there are always glimmers of hope, but that's about all there are."

The case in California

A report from the Pew Center on the States, an independent nonprofit group that identifies and advances state policy solutions, calls California "a case study in financial mismanagement." Quotes like that – and the added assessment by Pew that that state is on the path to virtual insolvency – begs the question, where does California stand in the case for recovery?

O'Sullivan says California is "pretty far behind" the rest of the nation in terms of feeling an economic uptick.

"It looks to me as if the recovery which begins in 2010 in economic activity suggests that revenue into the state won't start growing until fiscal 2010-11, and that's making some heroic assumptions," Sidhu said.

The state's non-partisan Legislative Analyst's Office has said the state was down \$6.3 billion in 2009 and predicted a \$14.4 billion budget gap in fiscal 2010-11. Translation – the state will be strapped for several years, even after the economy recovers.

On paper, Gov. Arnold Schwarzenegger's budget plan released in January funds schools at about the same level this year and the following year. However, the proposal includes

Revenue into the state won't start growing until fiscal 2010-11, and that's making some heroic assumptions.

\$1.7 billion in cuts to revenue limits, about \$283 per ADA and a \$45 million cut to county offices of education. The governor also plans to delay about \$100 million in payments owed to schools in 2010-11. Previous areas of flexibility granted last year will continue through 2012-13.

Dennis Meyers, principal economist at the California Department of Finance, predicted a drawn-out recovery in the state. "For schools, in the next two years, we're looking forward to a modest recovery and getting back to what you might call 'normal growth' in mid to late 2011-12. For California, you have the unemployment rate being somewhat elevated through 2012. It's going to be a while before we get back to what we were seeing four or five years ago. It's not going to be a quick turnaround like 2001-02."

Joel Montero, chief executive officer for the Fiscal Crisis & Management Assistance Team (FCMAT), points to the LAO report which predicts "positive movement" for the state's economy in the third quarter of 2010. "Watch the sales and use tax as an indicator for the state. When it gets positive, that's an indication that people are putting money back in the economy," Montero noted.

But with talk of a recovery underway, some question whether schools' stakeholders understand the depth of recent cuts and the lag that's inherent in improved funding to schools.

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“My concern is that the general public doesn’t realize how bad it is,” explained Renee Hendrick, director, business services, for the Orange County Department of Education and president-elect of CASBO. “Education was cut 20 percent in one year and because we tried to keep it away from the classroom, I don’t think parents noticed.”

Fueling the recovery

While experts are on the same page, most predicting a sluggish recovery, they offer various indicators that prove a recovery is underway.

Sidhu refers to her “two-minute drill” of indicators for proof that the freefall has stopped and recovery is at hand. The stock market thinks the recovery is at hand, and the market always leads an upturn. Segments of the housing market have also turned up, Sidhu noted, but those improvements “could stop on a dime.” Sales of existing homes have been pretty strong for nearly a year and the supply of foreclosed homes entering the marketplace appears to have slowed. Median home prices are edging up and consumer spending is beginning a slow ascent.

Our concern is that even if the economy is better, we’re not going to see the effects fast enough.

O’Sullivan couches his evidence for improvement in terms of economic drivers. “This isn’t the type of recession where you were knocked down and you stand up and dust yourself off. There’s been a shift in the fundamental drivers of the economy,” O’Sullivan said.

He indicated that the drivers that have been in place – retail sales, housing and financial services – slowed faster than the new drivers could ramp up. The new drivers – which he identifies as health care, green technologies and adult education – are more capital intensive and less labor intensive, but they are driving a recovery nonetheless. While they create fewer jobs



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than the sectors that are laying off, the jobs that are created are higher paying.

Proof positive that the economy is getting better, according to O'Sullivan, will be an increase in business investment, growth from exports and government spending.

Silver linings

Finding a silver lining in an economy that decimated school district budgets may be a long shot, but our experts gave it a try, identifying a few ways that the school industry may have benefited – at least a little – from the recession.

Sidhu likened the crisis to a good rain shower that leaves the streets clean and washes away the grunge, but conceded there is not much of an upside for schools.

“On the purchasing side there are some opportunities because vendors are struggling and might be willing to cut prices,” Sidhu said. And competition for the handful of school construction projects planned might also benefit districts by way of tight bidding. “This is a period in the cycle when they can do a little judicious spending and prices will be lower.”



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Experts predict when schools will benefit from current recovery

CASBO asked a number of experts in education funding to weigh in on when the apparent national economic recovery would begin to benefit public school funding in California. Here are their predictions:

Prediction: 2012-13

Ken Hall, founder, School Services of California, executive in residence at the University of Southern California

“California is beginning to turn around. I think economically we have encountered the bottom, but unfortunately, we have a long way to go before it impacts public education. There are a couple of indicators educators can look for. One is housing starts and housing prices. That indicator, if it begins to turn around more substantially, means more property tax revenues – so watch for property tax assessment increases. If you see a substantive increase, you can figure education increases are around the corner. The 2010 budget hopefully will be a constant to the current dollar levels and 2011 would have a slight growth to it. It will be the 2012-13 budget before it's to the pre-recession levels.”

Prediction: 2012-13

Joel Montero, chief executive officer, Fiscal Crisis & Management Assistance Team (FCMAT)

“If the state as a whole were to improve starting today, the translation to education will lag by 12 to 18 months. Watch sales and use tax as an indicator. When it gets positive, that's indication that people are putting money back in the economy. The earliest we would ever see a funded COLA would be 2011-12, more likely is 2012-13, and even then it will be small and will not cover the loss that will have occurred in the previous two or three years.”

Prediction: 2014-15

John Mockler, president, John B. Mockler and Associates, a consulting firm specializing in education policy and finance

“The only thing that will hold us up will be the Maintenance of Effort (MOE). In general, revenue is a problem when we lower taxes the year after next. We have reduced the percent of our income that we pay in taxes each of the last four years. Recall that in order to get the budget passed one year, they reduced business taxes, and that kicks in next year. There are a lot of time bombs that kick in.”

Prediction: 2012-13

Don Zimring, superintendent, Las Virgenes Unified School District

“I think the economic recovery has clearly begun and we'll start seeing some additional revenues to the state. The state will be under incredible pressure to give something back; to start rebuilding what they have dismantled. We'll start to see some basic payback in three years.”

– J.P.R.

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Montero noted the difficulty in finding an upside due to the fact that in an 18-month period, nearly \$1,700 per student was lost.

The potential bright spots he has heard suggested are that “education fared better than other industries,” and that the funding crisis forced efficiencies.

“The angle I’ve heard is that one of the things this has done is created the requirement for every single district to look at every single expenditure and operate more efficiently,” Montero said. “You could argue that 50 percent (of districts) aren’t in trouble in that they prepared themselves better or made themselves more efficient, and you could argue that’s a collateral advantage.”

CASBO’s Hendrick addressed the silver lining concept by noting that the national recession and California’s ongoing budget crisis may have pushed the state’s education system closer to reform. “There is talk about redoing the finance formulas for schools to make it more stable. I know there’s been talk about it for years, but maybe now is the time to really talk about that,” Hendrick said.

A sense of “unified concern” also has emerged among groups that are often at odds, even those who meet at the bargaining table. “The unions are being more cooperative than in

School leaders certainly have their work — make that more work — cut out for them.

the past,” noted Hendrick, adding that some unions are coming to the table seeking multiyear agreements, in some cases with no salary increase.

When will schools benefit?

So just when will the alleged uptick trickle down to schools in the way of improved funding?

“I’m suggesting that if money from property taxes is going to be down and stay down for a long time, given the low level of household formations that drives housing, we aren’t going to see a return to pre-2008 housing levels for five years nationwide,” O’Sullivan said.

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By that time, baby boomers will have begun retiring in larger numbers, which causes O'Sullivan to question whether the 40 percent funding level inherent in Proposition 98 can be supported.

"If I were in California schools I would say, 'Is that number defensible and where else are we going to get the money?' I would say that would be public-private partnerships and school business officials becoming more entrepreneurial."

Sidhu relies on basic economic principles to make her prediction for improved funding for schools. "Until banks get fixed and homes start selling and are filled again, it will not get better for school districts," Sidhu said.

Montero's estimate for improvement is 2012-13, after an even tougher 2010-11 budget year due to the loss of federal stabilization money.

CASBO's Hendrick noted that the state's schools won't benefit from the recovery until months after it's in full swing – likely 18 to 24 months after the significant improvement anticipated for late 2010.

Add to that the impending end of a temporary sales tax increase set to expire this spring and the potential for deferrals that

were one-time fixes to also disappear, and the lag in improved funding is extended.

"Our concern is that even if the economy is better, we're not going to see the effects fast enough," Hendrick said.

In the meantime

Given the expected slow pace of the economic uptick, improvements to the economy won't translate into improved school funding any time soon, meaning school leaders certainly have their work – make that *more* work – cut out for them.

That's where O'Sullivan's suggestion for entrepreneurship and partnering comes in. "Money will not come from local tax sources but from state, federal or private sector economic development," he predicts.

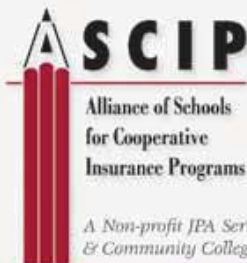
Schools should consider tapping new funding sources by watching the direction in which the economy is moving and beginning to serve those needs. "What we're talking about is public education going back to its roots," he said. That includes getting businesses more engaged and ensuring that schools are responsive to business needs.



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Schools should consider tapping new funding sources by watching the direction in which the economy is moving and beginning to serve those needs.

This type of partnering – essentially schools being responsive to the labor market – might emerge as a key, yet currently untapped, new funding source for schools.

Other opportunities some districts have begun to consider, according to Montero, are additional general obligation bonds to fund facilities locally and, on the program side, studies of parcel taxes.

He questions the real capacity for local communities and businesses to make up the shortfalls schools are experiencing,

which would essentially mean either asking taxpayers to carry a larger part of the burden or convincing corporations to do so.

But O’Sullivan contends there are opportunities. “It might be 5 percent of your budget now, but in the short run, it may be 100 percent of your growth,” he noted. ■■■

Julie Phillips Randles is a freelance writer based in Roseville, Calif.

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