

THE PEW CHARITABLE TRUSTS

Preparing for the Next Economic Downturn

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About The Pew Charitable Trusts

- Conducts research and analysis to improve policy, inform the public, and invigorate civic life.
- Established expertise on fiscal management of states, supported by research and experience providing hands-on assistance.
- Committed to identifying fiscal best practices and focused on non-partisan, data-driven solutions.

An Overview

- A multiyear perspective on revenue and expenditures can help policymakers avoid crisis-driven decisions and unsustainable budget practices.
- States can use a variety of fiscal management tools to attain this longer-term view of their budgets and to manage uncertainty, including multiyear revenue and expenditure projections and budget stress tests.
- These tools help states evaluate their fiscal outlook over the long run, assess how much they should set aside in their rainy day funds to weather economic downturns, and sustainably fund vital programs and services, among other things.

Long-Term Budget Projections

- Long-term budget projections are forecasts of revenue and expenditures that look at least three years into the future.
- These projections can help inform key decisions, including whether the state can afford new costs (from increased spending or tax cuts), or whether it needs to adjust to maintain a balanced budget (by cutting spending or increasing revenue).

Long-Term Budget Projections

The Six Fiscal Principles of Constructing Long-Term Budget Projections

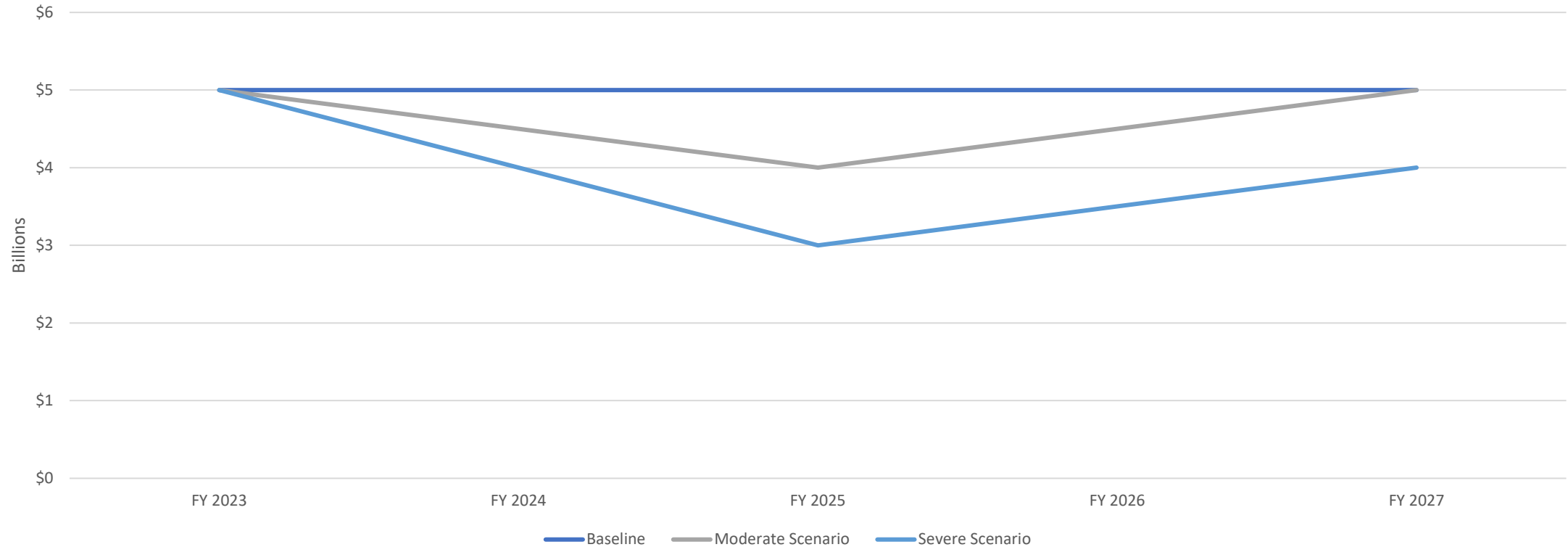
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| 1. Analyzing major revenue sources and spending categories. | 4. Accounting for the effects of potential policy changes. |
| 2. Looking ahead at least three years. | 5. Distinguishing between one-time and ongoing revenue and expenditures to estimate structural balance. |
| 3. Estimating baseline revenue and spending, using a “current services” approach to anticipate the amount of funding needed to maintain consistent service levels for programs in future years. | 6. Identifying the key factors driving the state’s structural position. |

Budget Stress Testing

- Budget stress tests help states estimate the potential budget shortfalls that could result from adverse events such as a possible economic downturn or a pandemic-induced recession.
- Incorporating a budget stress test into routine planning allows the state to account for economic downturns and manage business cycles. This can help policymakers make sound long-term plans.

What is a budget stress test?

Example: Predicted Revenue Shortfalls



Considerations for budget stress testing

1. Does it analyze revenues? Expenditures?
2. Does it include multiple scenarios or ranges?
3. Does it compare results to available contingencies?
4. Is it publicly available?
5. Is it performed on a regular interval?

Discussion Questions

- Would these fiscal management tools be helpful for your state ahead of the next economic downturn?
- Has your state considered doing long-term budget projections or a budget stress test?
- What resources would your state need in order to implement these practices?

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