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# Hawaii: Priced Out of Paradise

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## Abstract

Hawaii adopted a state budget that authorizes $14.3 billion in spending for FY2019. The Aloha State's economy continues to benefit from record-breaking tourist numbers and robust federal military spending. Although the state's unemployment rate is among the lowest ever recorded for any state in the nation, the cost of housing has made it increasingly difficult for working families to purchase a home. Tax revenues are strong, but they remain very dependent on the tourism industry. Hawaii also faces huge liabilities for pension and health care payments that are promised to retired state employees.

"I have to confess that I don't know my Twitter account log-ons and the passwords."

—Governor David Y. Ige, January 22, 2018

At 8:10 a.m. on the morning of January 13, Hawaii residents were greeted with an alarming message that flashed across phones throughout the state: "BALLISTIC MISSILE THREAT INBOUND TO HAWAII. SEEK IMMEDIATE SHELTER. THIS IS NOT A DRILL." After months of following news reports detailing the rising hostilities between North Korea and the United States, locals and tourists alike reacted with confusion and panic. Then, 38 minutes after the alarm with issued, the Hawaii Emergency Management Agency sent another message declaring it to be a false alarm (Nagourney 2018). Governor David Ige, who later admitted that he did not know his Twitter password, was excoriated in the local press for his lack of leadership during the crisis. Although the governor faced a tough reelection challenge from popular Democratic Congresswoman Colleen Hanabusa, he emerged victorious in the primary and the November general election.

The governor won his reelection battle in large part because the Aloha State's economy continues to boom. More tourists are arriving than ever before, construction of new condominium towers continues apace, and nearly everyone who wants a job has one. In December of 2017, Hawaii registered an unemployment rate of just 2%, the lowest ever recorded in any U.S. state since records were first kept over forty years ago (UHERO 2018). Despite the healthy economy, the state's crushing cost of living has forced many longtime residents to flee to cheaper metropolitan areas on the mainland. In 2017, Hawaii was one of a handful of states that saw a decline in its population (U.S. Census Bureau 2017). According to an analysis by the Economic Policy Institute, a family of four needs to earn at least $115,000 to achieve a modest middle-class lifestyle (Economic Policy Institute 2018). Although food, fuel, and other necessities are expensive in this island state, the cost of housing – the highest in the nation – is the main cause (Van Dam 2018).

The state legislature, which continues to be overwhelmingly Democratic, has seen new leadership. Longtime Speaker of the House, Joe Souki, was forced to resign after an investigation by the State Ethics Commission found that he had sexually harassed multiple women. The looming costs of healthcare and pension benefits for retired workers continue to threaten the state's bond rating. Other issues include a rapidly aging population, the massively over budget Honolulu Rapid Transit system, and efforts to regulate online visitor accommodation websites like Airbnb.

## Population and Demographics

Hawaii's racial and ethnic diversity is unique in the United States. Over 74 percent of the state's residents identify as nonwhite, a vastly higher number than the 23 percent in the nation as a whole (See Table 1). Extensive immigration from the Asia-Pacific region continues to contribute to Hawaii's high number of foreign-born residents. Nevertheless, the high cost of living means that local working families are more likely to leave Hawaii for the mainland than ever before. Hawaii now has one of the highest proportions of residents age 65 and older in the nation (Kaiser Family Foundation 2017). This factor, combined with the state's rapidly aging population, has put pressure on the state's underfunded pension system.

The high cost of living has also contributed to a rise in economic inequality. Indeed, despite Hawaii's reputation as a state with harmonious race relations, deep inequalities persist. In fact, Native Hawaiians and other Pacific Islanders are far more likely to live in poverty than Hawaii's white and Japanese residents (Hofschneider 2018a).

**Table 1. Demographic Comparisons in 2016: Hawaii v. U.S. (Percentages)**

| | *Hawaii* | *U.S.* |
|---|---|---|
| White | 26.7 | 77.1 |
| High School Graduate | 91.0 | 86.7 |
| Bachelor's Degree or Higher | 30.8 | 29.8 |
| Born in US | 17.7 | 13.2 |
| Persons in poverty | 10.6 | 13.5 |
| Persons without Insurance (< 65 yr) | 4.7 | 10.5 |
| Civilian labor force (> 16 yr) | 61.5 | 63.3 |
| Population per square mile | 211.8 | 87.4 |
| Median household income | $69,515 | $53,889 |

Source: U.S. Bureau of the Census

**Table 2. Demographic Comparisons in 2016: Hawaii Counties**

| | *Hawaii* | *Honolulu* | *Maui* | *Kauai* |
|---|---|---|---|---|
| Population Disbursement | 13.8 | 69.4 | 11.6 | 5.0 |
| Bachelor's Degree or Higher | 26.8 | 32.7 | 26.1 | 28.0 |
| Foreign Born Persons | 11.2 | 19.1 | 17.9 | 16.5 |
| Population in Civilian Labor Force | 58.3 | 60.9 | 68.6 | 64.4 |
| Race: White Alone | 34.3 | 23.3 | 35.8 | 33.8 |
| Persons in poverty | 18.3 | 9.2 | 10.7 | 11.2 |
| Persons without Insurance (< 65 yr) | 5.9 | 4.4 | 5.4 | 5.2 |

Source: American Community Survey, U.S. Bureau of the Census

**State of the Economy in Hawaii**

Business in Hawaii is booming, but after several years of rapid growth, the economy will likely cool off in the coming years. The University of Hawaii's Economic Research Organization (UHERO) predicts a 1.3 percent increase in real GDP during 2017 (see Table 3). Although this growth is expected to slow, it should continue through 2020. Unemployment has averaged just 2.7 percent for 2017, one of the lowest rates ever recorded (see Figure 1). Now that the economic recovery is largely complete, UHERO economists expect that job growth will slow to 1% in 2018 (UHERO 2017a).

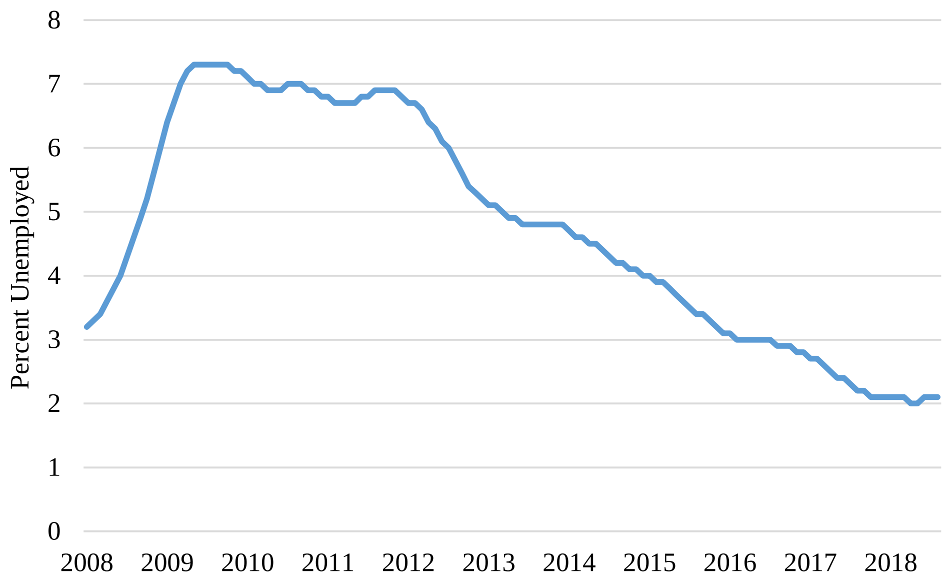
The out-migration of many residents who have been priced out of the islands has contributed to this labor shortage. Unfortunately, the tight labor market has not led to meaningful wage increases for most workers (UHERO 2017a). In real terms, wages have declined a bit since 2017, in part because the many of the industries that have seen the strongest job growth are in low-wage sectors like the service industry (UHERO 2018).

Hawaii's economy depends upon three major industries: tourism, construction, and the military. Between 2014 and 2016, the construction industry created roughly one-third of all new jobs in Hawaii. New glass and steel condominium towers have transformed once-sleepy districts in Honolulu into vibrant nightlife destinations. Military spending continues to be robust, and Hawaii should benefit from the Trump Administration's request for more defense spending, particular for the U.S. Navy. The National Conference of State Legislature ranks Hawaii as second in the nation in the percentage of GDP contributed by military spending (NCLB 2017, Governing 2017). In total about 12.4 percent of the state's gross domestic product comes from federal spending.

Tourism has always been the backbone of modern Hawaii's economy, and it has seen enormous success in recent years. In 2017, 9.38 million people visited the islands. The tourism industry generated an astonishing $16.78 billion in visitor spending, which contributed to $1.96 billion in tax revenue (Hawaii Tourism Authority 2017, Table 3). Although hotels have reported full occupancy since 2012, the number of visitors is 20% higher today than in 2008 (See Figure 2). Visitor spending has also grown, although it has not matched the levels achieved during the 1980s.

At this point, it is not clear how many more visitors Hawaii can accommodate. Economists predict that this may result in a slower rate of growth of arrivals to 1.5% in 2019 and 1% in 2020. Some of this will depend upon whether several new resort projects are approved on Oahu, and the future regulation of transient vacation rentals (UHERO 2017b). There is also more resistance to the expansion of tourism from Hawaii's year-round residents. For the first time in decades, the legislature has started to question state money spent to increase tourism, and it recently attempted to reduce appropriations for the Hawaii Tourism Authority (HTA). During the last legislative session, Senate Ways and Means Chair Donovan Dela Cruz questioned why the HTA should continue to have a "budget of $80-plus million when we've already reached what people feel is a heightened capacity" (Daysog 2018).

**Figure 1. Hawaii Unemployment Rate, 2008 - 2018**



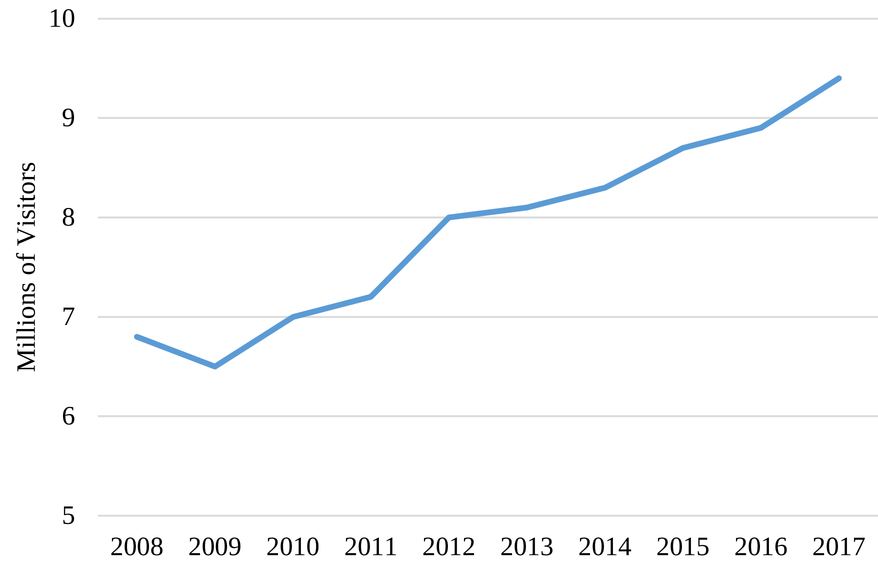

Source: U.S. Bureau of Labor Statistics

**Table 3.**
**Hawaii Economic Indicators: Year-Over-Year Percentage Change**

| | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 |
|---|---|---|---|---|---|---|
| **Visitor Arrivals** | 4.5 | 3.1 | 4.1 | 1.5 | 1.1 | 0.8 |
| U.S. Visitor Arrivals | 6.9 | 4.1 | 4.4 | 1.4 | 1.1 | 0.8 |
| Japan Visitor Arrivals | -1.9 | 0.4 | 7.1 | 2.3 | 1.5 | 0.4 |
| Other Visitor Arrivals | 3.1 | 2.6 | 0.5 | 0.9 | 0.9 | 1.1 |
| **Non-farm Payrolls** | 1.8 | 1.6 | 0.9 | 0.7 | 0.6 | 0.6 |
| **Unemployment Rate (%)** | 3.6 | 3.0 | 2.7 | 2.8 | 2.9 | 3.3 |
| **Inflation Rate, Honolulu** | 1.0 | 2.0 | 2.8 | 3.2 | 3.1 | 2.6 |
| **Real Personal Income** | 3.7 | 2.4 | 0.8 | 1.3 | 1.3 | 1.3 |
| **Real GDP** | 3.9 | 2.1 | 0.6 | 1.3 | 1.1 | 1.4 |

Note: Figures for 2018 – 2029 are forecasts.
Source: UHERO 2017a

**Figure 2. Visitor Arrivals by Year, 2008 - 2017**




Source: Department of Business, Economic Development and Tourism, State of Hawaii

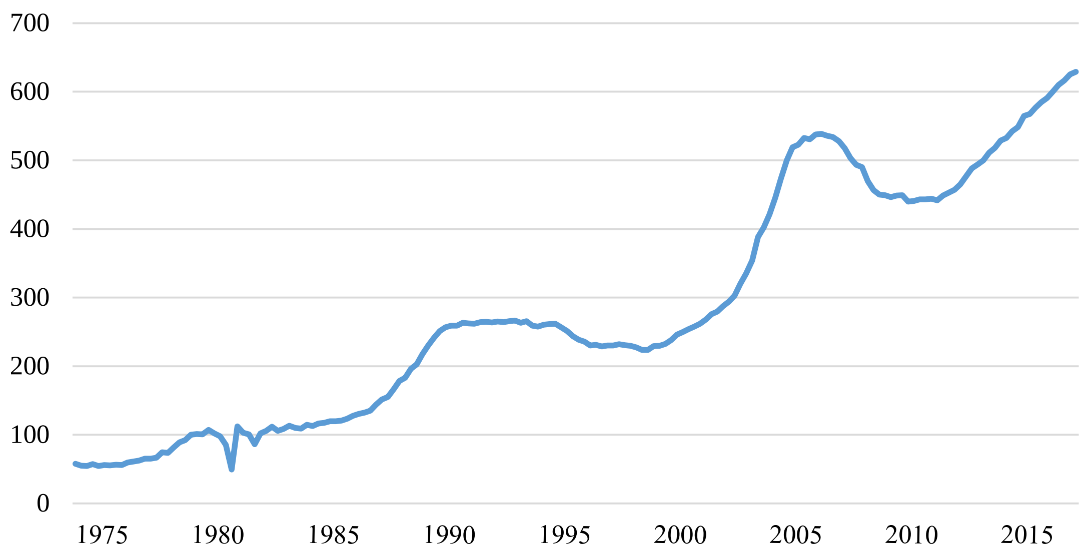
The federal tax cuts passed by Congress in December 2017 are not predicted to provide much of a boost to Hawaii's soaring economy. More concerning is the potential for new restrictions on trade and immigration that would almost certainly negatively affect business in Hawaii (UHERO 2017c). On a more positive note, the new federal budget that will fund the federal government through September 30, will funnel millions of dollars to Hawaii. Given the state's dependence on military spending, the additional $80 billion approved for new defense spending will almost certainly benefit Hawaii, including $60 million for an improved radar defense system (Grube 2018). Hawaii's senior U.S. senator, Brian Schatz, called it "the best appropriations bill that we've seen for our state since I got here" (Schatz 2017).

Hawaii's high cost of living continues to make it a challenge for all but the wealthiest residents to remain in the state. In 2017, Hawaii was ranked as the most expensive place to live in the United States (Van Dam 2017). Indeed, as the nonpartisan Institute on Taxation and

Policy concluded after taking the cost of living into account, Hawaii has the lowest wages in the nation (Institute on Taxation and Policy 2018).

Although the higher prices for food and transportation certainly contribute to the cost of living, the price of housing is the major culprit. The median price for a single-family home increased only modestly during 2017, but housing prices overall are up by 30% since 2011 (Figure 4). Today, the median price in Honolulu for a single-family home is $752,000 and the price for a condominium is nearly $400,000 (Gomes 2017). To be sure, the median income in Honolulu increased almost 11 percent from 2017 to 2018 to $96,000, but this has done little to help working families who still find themselves priced out of the real estate market. According to federal guidelines, an income of up to $93,000 now counts as "low-income" for a family of four in Honolulu (Hofschneider 2018b). It is no wonder, then, that many young people have decamped for more affordable metropolitan areas like Las Vegas.

Figure 3. Hawaii House Price Index, 1975 - 2018




**Source:** St. Louis Federal Reserve and U.S. Federal Housing Finance Agency.
Index 1980: Q1 = 100.

**Hawaii's Taxation System and Revenue**

More than most states, Hawaii relies on consumption and income taxes to fund most of its operations. Most services, including public education, that are managed at the local or municipal level in other states are run by the state in Hawaii. Three major taxes provide Hawaii most of its general revenue. Hawaii's unique general excise and use tax (GET) imposes a 4.5 percent levy on all business activity, including rental property, in the state. The personal income tax is relatively high and ranges from 1.4 percent and increases to a rate of 11 percent, giving Hawaii the second-highest state tax bracket in the nation (Hawaii Budget and Policy Center 2018b). The transient accommodation tax (TAT) – popularly known as the hotel tax – is a special state tax applied to hotel rooms and apartments that are occupied for fewer than 180 consecutive days (Department of Budget and Finance 2017b).

Hawaii has the third highest rate of per capita state tax collections at $4,530, although a percentage of these are paid by tourists. (Hawaii Budget and Policy Center 2018b). In the last fiscal year, Hawaii's total tax collection amounted to $7.3 billion. The GET provides 44% of total revenue ($3.2 billion), which is lower than the 31.6% on average for all fifty states. Hawaii receives 30.6% of its revenue ($2.2 billion) from its income taxes, which is slightly lower than the average of 37.2% of all states. Other state taxes, including the TAT and fuel tax generated another $1.9 billion in revenue (Pew 2017, Hawaii Budget and Policy Center 2018b).

Counties retain the sole authority to tax property in Hawaii, which means that this important source of revenue is not available to the State of Hawaii. Nor does it appear that this will change at any point in the near future. In November, a constitutional amendment was on the ballot that asked voters to give the state the power to tax property. Although the state Supreme

Court invalidated the measure because the language was judged to be confusing, polling showed that it would have been soundly defeated (Blair 2018).

Hawaii's GET tax is different than the more familiar system of state sales taxes that are only applied to the end user of a good or service. The GET taxes *all* services and goods even when that service or good is later sold to someone else. Although the rate is only 4.5%, it generates a much higher rate of tax revenue, since it can be applied many times to the same good or service. Like a sales tax, vendors often add this as a separate item to the cost of their goods or services. It is difficult to compare the GET to most state sales taxes, but one study estimated that it generates revenue similar to a 10-percent sales tax rate. This makes Hawaii's rate similar to the sales tax rate of Louisiana, which currently has the nation's highest sales tax rate of 9.98 percent (Hawaii Budget and Policy Center 2018b). Furthermore, unlike many states that have high rates of sales tax, Hawaii's GET applies to nearly everything, including food and rental income.

The last major tax is the TAT. It contributed $508 million to state coffers in FY2017. Although the TAT accounts for only 7 percent of state revenue, the state has raised it several times over the past several years, a further indication of how reliant state tax revenues are on the tourism industry (Hawaii Tax Review Commission 2017). Prior to 2009, for example, the TAT rate was only 7.25 percent. It was raised to 9.25 percent during the Great Recession to make up for declines in state income taxes (Hawaii Tax Review Commission 2017). In 2017, the TAT was increased again by one percentage point to provide revenue for Honolulu's over-budget rapid transit rail project (Hawaii Budget and Policy Center 2018b). This most recent increase was passed over the fierce objections of hotels and other major players in the state's tourism industry, making it unlikely to go up again in the near future.

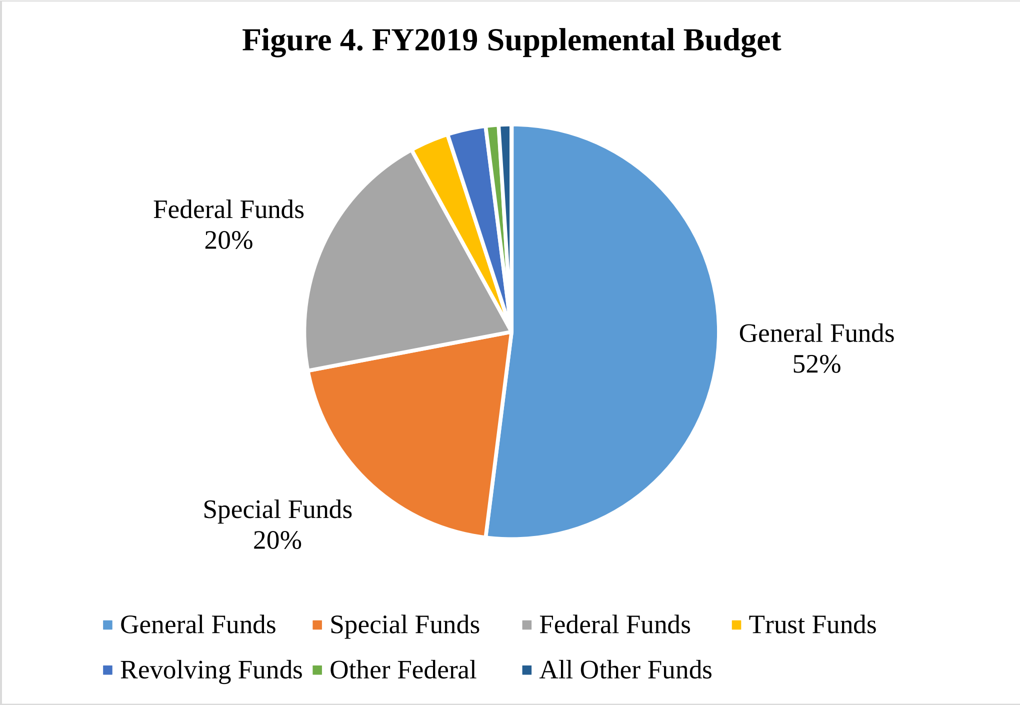
The proper way to regulate and tax transient vacation rentals continues to vex the legislature. Although the rise of Airbnb and other online home-sharing services has expanded the number of tourists the state can accommodate beyond the approximately 80,000 hotel and timeshare units, it has also put upward pressure on rental prices for longtime residents. The University of Hawaii Economic Research Organization estimates that there are 14,000 rooms that were on the vacation-rental market on 2016, a number that has probably increased in the past year (UHERO 2018).

Although Hawaii's taxes may appear to be burdensome, they are structured to take advantage of the state's tourism economy. Both the TAT and the GET are designed to push some of the tax burden to the more than 9 million tourists who visit the islands every year. Most studies estimate that tourists and nonresident property owners pay about one-quarter to one-third of all state and local taxes (Hawaii Tax Review Commission 2017). The model of taxation also means that the state's revenues can drop dramatically during recessions when the tourism industry is in decline. They can also be affected when visitors spend less money than anticipated. For example, although tax collections have increased over the last two fiscal years, they increased by much less than expected, forcing Gov. Ige to cut 10% of the state's discretionary spending (UHERO 2017c).

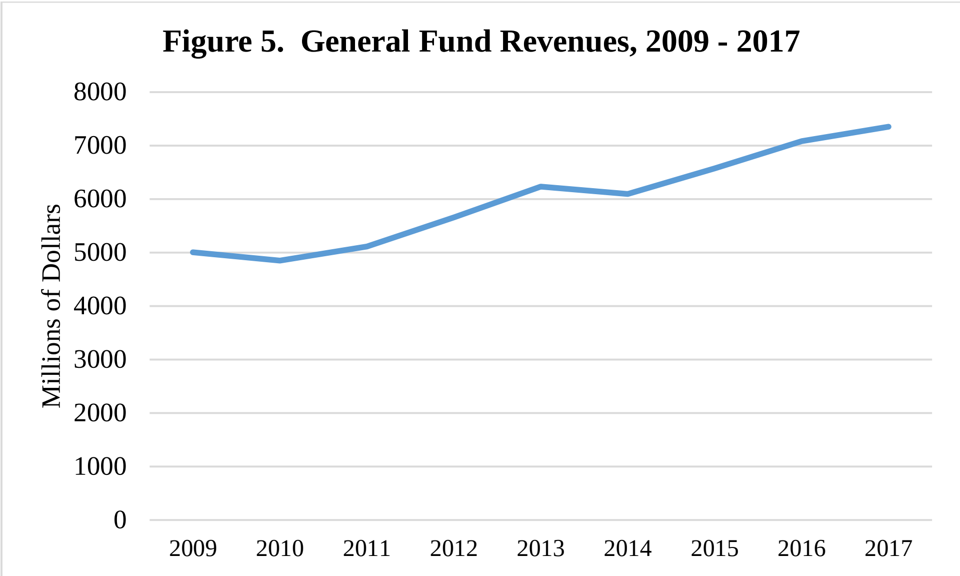
Hawaii's heavy reliance on consumption taxes has led it to develop one of the least equitable tax systems in the United States. Indeed, the top 1% of families in Hawaii spend only one percent of their income on excise taxes, while poor families pay up to 11%. In 2015, the Institute for Taxation and Economic Policy ranked Hawaii as second only to Washington State for the percent of taxes paid by the poorest 20% of families (Institute on Taxation and Economic Policy 2015). A follow-up report in 2018 found that Hawaii had the 15$^{th}$ most unequal system of taxation among all fifty states (Institute on Taxation and Economic Policy 2018). During the last legislative session, Hawaii did adopt a state-level earned income tax credit, which should provide some relief for the working poor.

**Structure of the State Budget**

Hawaii's state budget is divided into an executive budget for state agencies that comprises 99 percent of all spending. Smaller budgets are appropriated for the state's legislative and judicial branches, as well as the state's unique agency to serve Native Hawaiians: The Office of Hawaiian Affairs. The current executive budget is made up of the state's general fund revenues of $7.5 billion, special funds of $2.9 billion, federal funds of $3 billion, and other funds, including trust funds for the state's pension and health care for retired employees that amounts to nearly $1 billion. As Figure 4 shows, the state's general fund makes up a little over half of Hawaii's total budget. Capital Improvement Projects (CIP) are funded by general obligation bonds and are not included in the overall state budget.




Source: State of Hawaii, FY2019 Executive Supplemental Budget in Brief




Source: State of Hawaii, FY2019 Executive Supplemental Budget in Brief

Hawaii's economy has long benefited from federal military spending, but it receives fewer direct federal grants than many states. As Figure 4 shows, federal funds contribute about 20% to Hawaii's total budget. The Center on Budget and Policy Priorities, reviewing data from

FY2017, found that Hawaii received the least amount of revenue from direct federal grants at about 17.5 percent. This was significantly lower than the national average of 31.3 percent (Hawaii Budget and Policy Center 2018b). Most of these federal dollars go to support programs such as the Supplemental Nutrition Assistance Program (SNAP), Temporary Assistance for Needy Families (TANF), the Children's Health Insurance Program (CHIP), and Medicaid. A much smaller percentage of these funds – less than 9 percent – go to support educational programs.

This troubling trend is not new to Hawaii. Over the last decade, federal funds have made up a smaller part of the overall state budget. If federal matching funds for Medicaid are excluded, federal funds only grew by 16% over the past decade even as executive budget spending increased by 22% (Hawaii Budget and Policy Center 2018a). The reduction in funds has led Gov. Ige and his predecessor Gov. Neil Abercrombie to push state agencies to find ways to increase the amount of federal money in support of state programs.

Despite Hawaii's inability to increase its share of federal money, the state's robust tourism and construction industries have contributed to a healthy growth in tax revenues. As Figure 5 shows, Hawaii's general fund revenues have increased steadily since the Great Recession, growing by 31 percent between fiscal years 2009 and 2018. Nevertheless, as previously discussed, this model of taxation is highly dependent on the continued success of tourism. When visitor arrivals decline, as they did during the last recession, the state is forced to raise income taxes or to dip into its emergency funds.

Hawaii's reserve fund, the Emergency and Budget Reserve Fund (EBR), which was created from tobacco settlement money and direct legislative appropriations, is relatively low compared to other states. After being drawn down to nearly nothing during the Great Recession, it is in a more stable position today. In FY2016, the state had a one-time surplus of $1 billion that allowed it to make significant contributions to the EBR (Hawaii Budget and Policy Center 2018b). Today, the EBR has approximately 4.2 percent of general fund expenditures, which places Hawaii slightly below the national average of 5.4 percent (Hawaii Budget and Policy Center 2018b). In fiscal year 2018 the legislature appropriated $125 million, and it is likely that a similar amount will be appropriated during FY2019.

**The Budget Process**

The Hawaii State Legislature is a part-time legislature that meets from January to May every year. The governor is mandated to present a budget request that is prepared by the Department of Budget and Finance in consultation with executive departments. This budget is a biennial request in budget years, and a supplemental request in off-years. FY2019 is a supplemental year. The governor is also required to submit a six-year financial plan for the state.

The governor sends his budget 30 days before the legislative session convenes. The governor's budgetary request reflects the needs of 17 departments, his office, the office of the lieutenant governor, and the University of Hawaii System. State departments submit their budget requests to the state's Department of Budget and Finance, which crafts the budget. By January 10, the state's Council of Revenues is required to share its forecast of the state's general fund for the current fiscal year and the next six fiscal years.

The Senate Ways and Means Committee and House Finance Committees must consider all financial bills. The budget is broken into two proposals. The first is for general departmental spending, and the second is for CIP appropriations that include state infrastructure investments and upgrades. "First decking" is the date by which the budget must be passed out of the House

Finance Committee so it can be voted upon by the full House. The date on which bills are passed from one chamber to the other is called "crossover," which occurs earlier than other bills.

When the budget reaches the Senate, it is referred to the Ways and Means Committee. Second crossover occurs when the budget proceeds out of the Senate and to a conference committee. Final decking is when the budget proceeds out of conference and back to both chambers for a final vote. All members of the legislature will vote three times on the state's budget. The Hawaii Constitution requires that the budget be balanced every year, and this often requires the legislature to make off-year amendments to adjust spending. Although the legislature is not required to amend the budget during the second year of the biennium (even-numbered years), it nearly always does so (Hawaii Budget and Policy Center 2018b).

**Executive Budget and Legislative Response**

Gov. Ige's supplemental budget request for FY2019 asked for major investments in transportation infrastructure, schools, and harbors, along with significant funding for more affordable housing. The governor's supplemental budget called for $15 billion more in capital improvement projects, which represented a 215 percent increase from the original biennium budget submitted last year. Under the current six-year financial plan, spending will continue to outstrip projected revenues until 2023, which will draw down the state's $1 billion surplus (Eagle 2017). In his supplemental budget request, the governor requested only modest general spending increases of $85.5 million. Much of this increased funding was designed to provide money for school health services, more funds for the state's long-term care assistance programs, and an additional $800,000 for homeless outreach programs (Eagle 2017).

The governor's supplemental budget request did not receive a warm response in the legislature. House Finance Chair, Sylvia Luke, is known for being cautions and methodical, and her counterpart in the Senate, Donovan Dela Cruz, is similarly conservative in fiscal matters. Cruz has been a critic of Ige for being too free with state dollars and told the press that the state was "not living within its means" (Dayton 2018). Cruz was also a supporter of Ige's opponent, Congresswoman Colleen Hanabusa, who challenged the governor in the Democratic primary. In the end, the House Finance Committee cut $35 million from the governor's budget. Under Gov. Ige's six-year financial plan the state would achieve a negative budget balance of $95 million in 2022. The House proposed a more conservative budget that left it with a $108 million surplus (Eagle 2018a).

Despite the relatively modest cuts to the proposed budget, the Ige Administration criticized the changes made by Luke and her colleagues in the House. During the tense budget negotiations in the spring of 2018, a parade of top administration officials appealed to Sen. Cruz, the Chair of the Senate Ways and Means Committee, to restore funding for their budget priorities. The State Department of Health registered particular concerns about the House's plan to eliminate nurse and psychiatric positions from the budget. The University of Hawaii system was also hit especially hard. Out of the $6.7 in additional funding quested by the governor, only $1.8 million was approved.

As is often the case, many of the governor's requests were restored during the final budget negotiations. The governor also received some support when the State's Council of Revenues, which determines the state's projected revenues for the coming year, adjusted its estimates up slightly from 4.5 percent growth to 5.3 percent growth for the general fund. This authorized the legislature to spend about $50 million more than in FY2018 (Eagle 2018).

**The Approved Budget for Fiscal Year 2019**

Hawaii's total budget when all federal grants, operating appropriations, and capital projects are totaled amounts to $17.5 billion. Nearly all of that budget goes to support executive branch spending that amounts to $16.8 billion. As Table 4 shows, during FY2019, the judiciary received $185 million, while the legislature and the Office of Hawaiian Affairs operated with much smaller budgets of $185 million and $9 million respectively. Hawaii is fourth among all fifty states in per capita spending of state-generated revenues with $9,685, compared to a national average of $5,858 (Kaiser Family Foundation 2018)

**Table 4. Total General and Capital Expenditures**

| | |
|---|---|
| Executive | $16.8 billion |
| Judiciary | $185 million |
| Legislative | $42 million |
| Office of Hawaiian Affairs | $9 million |
| Grants in Aid: | $30 million |
| Appropriations Bills: | $481 million |
| TOTAL | $17.5 billion |

Source: State of Hawaii, FY2019 Executive Supplemental Budget in Brief

The legislature authorized $129 million in general spending beyond Governor Ige's request, but it slashed his requests for more than $4 billion in capital improvement projects. Capital improvement projects, which are mostly financed through the state's general obligation bonds, totaled $2.1 billion in fiscal year 2019. The state also provided one-time appropriations to homeless programs ($15 million) and an innovative elderly care program for seniors ($5 million). The islands of Kauai and Oahu received a total of $100 million to help them recover from two major flooding disasters, and Hawaii Island received millions in assistance to help manage the eruption of the Kilauea volcano (Eagle 2018c).

Table 5 details the authorized spending for all of Hawaii's executive agencies. Most of these appropriations go to the salaries of the state's 48,222 permanent employees and 4,067 temporary employees. The department of Human Services' massive $3.6 billion budget goes to pay the state's share of Medicaid and other social programs. The Department of Budget and Finance's budget of $2.8 billion is particularly large because "fringe" benefits for state employees, such as health insurance and pension contributions, are paid out of its budget rather than directly by the employing agency. The Department of Education is the state's largest employer with almost 23,000 positions (Hawaii Budget and Policy Center 2018b). This year the legislature made only minor adjustments to each executive department's appropriations in the supplemental budget for the second year of the biennium.

| **Table 5. Executive Budget 2019** | ($ millions) |
|---|---|
| Accounting and General Serv. | 203.7 |
| Agriculture | 51.9 |
| Attorney General | 98.0 |
| Business, Ec. Dev., & Tourism | 270.3 |
| Budget and Finance | 2,858.5 |
| Commerce & Consumer Aff. | 81.7 |
| Defense | 131.2 |
| Education | 1,975.1 |
| Governor | 3.5 |
| Hawaiian Home Lands | 57.0 |
| Health | 1,046.7 |
| Health – HHSC | 693.5 |
| Human Resource Develop. | 25.4 |
| Human Services | 3,586.9 |
| Labor & Industrial Relations | 473.4 |
| Land & Natural Resources | 150.5 |
| Lt. Governor | 1.1 |
| Public Safety | 275.5 |
| Taxation | 28.2 |
| Transportation | 994.8 |
| University of Hawaii | 1,170.7 |

Source: State of Hawaii, FY2019 Executive Supplemental Budget in Brief

Along with general appropriations for salaries and operating budgets, the legislature also approved $481 million in separate one-time appropriations bills. Among the winners was the Department of Business, Economic Development, and Tourism which received $1.5 billion to simulate its Accelerator Program to aid innovation among small businesses.

The Department of Human Services received an additional $15 million to fund homelessness programs and services throughout the state, an appropriation that shows just how acute the homeless crisis has become in Hawaii. A Department of Housing and Urban Development study found that in January 2017, 51 in 10,000 people in Hawaii were homeless –

the highest rate in the nation.  Hawaii is also one of four states where more than half of all homeless people were living in unsheltered locations (USHUD 2017).  The situation has become so dire that the legislature appropriated $30 million for the development of so-called "ohana zones" [the Hawaiian word for family] on Oahu, Kauai, Maui, and Hawaii islands (SB2401). Although it is not yet clear how these sites will be managed, they are designed to offer homeless individuals a safe and legal place to camp on state-owned lands (Blair 2018).  In a separate appropriation, the legislature also committed $200 million to accelerate the development of affordable rental units (HB 2748).  The money will allow the Hawaii Housing Finance and Development Corporation to create an additional 1,600 affordable units for rent (Office of the Governor 2018).

The Department of Health (DOH) received an additional $28 million in subsidies for the Maui Health System, an appropriation that primarily goes to support Maui Memorial Medical Center, which has been operating at a loss for years, but is the only major hospital on the island of Maui.   The DOH also received nearly $5 million in support of Hawaii's innovative Kupuna Care network [the Hawaiian word for the elderly], a program designed to provide seniors with small cash grants to hire part-time aid workers to perform simple household tasks.  This program has enjoyed great popularity among the public and in the legislature.  It is so popular, in fact, that the legislature took the rare step of doubling the governor's requested appropriation this year (Eagle 2018c).  The Department of Transportation received over $50 million to upgrade car rental facilities and for other minor improvements at the international airports in Honolulu and on Maui.  The state legislature also provided $30 million in grants-in-aid to nonprofit organizations during FY2019 (Hawaii Budget and Policy Center 2018a).

The state's capital improvement budget for FY2019 totaled $2.4 billion. These funds go to departments to pay for large infrastructure projects and other one-time improvement expenditures, often for roads, schools, airports, and other major infrastructure investments. The state's CIP budget included $800 million in new school construction and more than $100 million in improvements to University of Hawaii facilities. It also included $40 million in funding to complete a new women's prison that should reduce overcrowding in existing facilities and $21.5 million for upgrades to the state's public housing stock (HB 1900).

**Trends in State Spending and Obligated Spending**

The nonpartisan Hawaii Budget and Policy Center compared the budgets between the recession of FY2009 and FY 2019 and concluded that there was a 31% overall increase in spending. Much of that can be attributed to an 84% increase in the budget of the Department of Human Services to support the state's Medicaid system Med-QUEST. As in all states, the costs of health care have increased in Hawaii. The state's Medicaid costs went up as more people enrolled in Medicaid under the Affordable Care Act. All state departments have seen their budgets increase, except those for the office of the governor and the lieutenant governor, which have declined by approximately $1 million since 2009 (Hawaii Budget and Policy Center 2018a).

Over the past several years, a larger share of the budget has been taken by obligated spending in the service of Medicaid, the state's debt, and health and pension benefits for retired state employees. On the positive side, the state's level of indebtedness is relatively stable. As of

July 1, 2018, Hawaii held $7.2 billion in general obligation bonds, $3 billion in revenue bonds, and about $1.3 billion special purpose revenue bonds (Department of Budget and Finance 2018). In recent years, the governor and the legislature have made considerable efforts to improve Hawaii's credit rating. The Ige administration has created a "rainy day" fund of $354 million, which led Moody's Analytics to determine that Hawaii was one of just 16 states that could weather the stress test of a new recession (Office of the Governor 2017).

The more concerning obligation is the state's huge liability for pension payments and health care for state workers, which amount to $25 billion in unfunded liabilities for Hawaii. Pension payments and other post-employment benefits took up 47% of all Hawaii's general revenue. To be sure, Hawaii has increased its payments to the state's public pension system, the Employee Retirement System (ERS). Yet the unfunded liability for the ERS is $12.9 billion, and an additional $12.5 billion is owed to the state employee health care trust fund (Hawaii Budget and Policy Center 2018b). After years of raiding the pension system to pay for other projects, fiscal year 2019 marks the first time Hawaii will begin pre-funding 100 percent of public workers' retirement benefits. Gov. Ige expects that this will save Hawaii $1.6 billion over the next two decades (Eagle 2017).

**Conclusion**

Increases in military spending and Hawaii's historically strong tourist industry should leave the state in a strong financial position over the next several years. Yet the state's spending may become unsustainable if tax revenues do not continue to increase. Despite predictions that the state would end FY2018 with a budget surplus of $1 billion, it will only have a $750 million cushion in FY2019. The leadership in the state Legislature has become increasingly concerned about these developments. As Sen. Dela Cruz, the chairman of the Senate Ways and Means

Committee recently remarked, "If the administration doesn't figure out a way to increase revenues other than raising taxes and doesn't limit its expenditures, or at least do things in public-private partnerships to provide services (and) limit expenditures, then we're going to be continually spending more than we bring in" (Dayton November 2018).

Hawaii's unsheltered homeless population continues to be among the highest in the nation, it has stabilized, and this progress is almost certainly due to aggressive action by Gov. Ige and the legislature. More troubling is the lack of affordable housing that continues to force longtime residents to move out of the state despite its booming economy. Although there were a number of new programs enacted to address this daunting policy challenge, it seems unlikely that any bills will provide long-term solutions to Hawaii's affordable housing crisis.

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