



Mapping the Risk from State and Local Government Employment

October 2010

Economists since Keynes have recommended countercyclical fiscal policies to moderate the impact of the business cycle and encourage steady growth. However, the weak current status of State and local budgets has necessitated job cuts that have overwhelmed the uptick in private sector hiring. The October 8 New York Times reported:

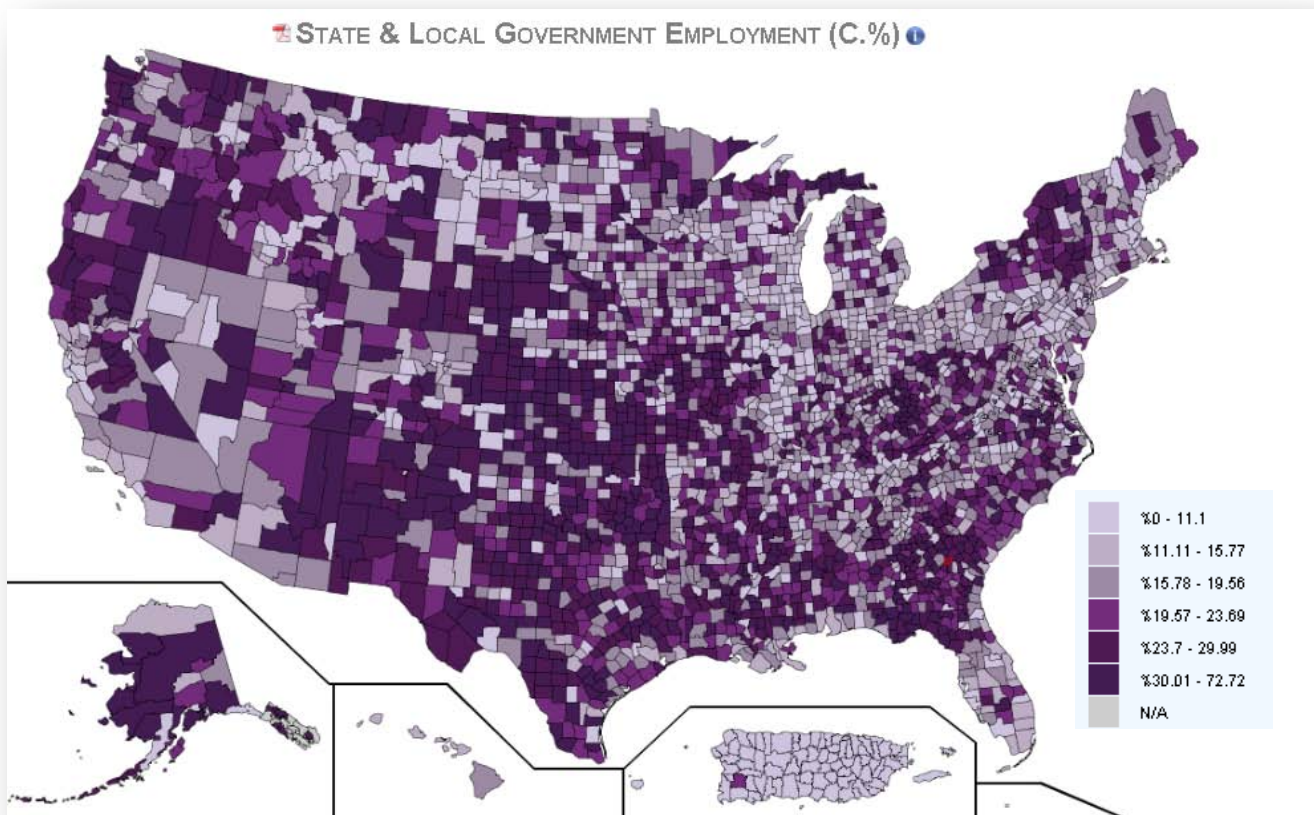
“[O]ver all, the economy lost 95,000 nonfarm jobs in September, the result of a 159,000 decline in government jobs at all levels. Local governments in particular cut workers at the fastest rate in almost 30 years...President Obama has repeatedly called for additional measures like infrastructure projects and tax incentives, which have been met with opposition from Republicans over deficit concerns. The word “stimulus” itself seems to have become politically toxic in the lead-up to the midterm Congressional elections next month.”

In fact, this is the fourth consecutive month that cuts in government jobs have completely wiped out gains in private sector employment. Falling levels of local government employment are a double-edged sword for municipal investors. On one hand, they indicate fiscal discipline. Localities that reduce headcount in order to balance their budgets indicate that they are willing to take painful measures to meet their obligations.

On the other hand, deep cuts in services can have severe impacts on the economy and the community at large, potentially doing more harm than good for long-term solvency. The immediate impacts of reducing the wages paid into a community can include a decrease in employment and population and an increase in demand for certain local services, all of which will reduce local revenue. But the long term damage to the community can be much larger. The perception that cuts to school programs may lower the test scores of local schools, or that cuts to public safety may increase crime rates, can have a severe impact on real estate values and population growth.

Lumesis believes that areas with a high percentage of their employment in government jobs should be considered to be likely to underperform, regardless of how the economic recovery progresses. Should the rebound in private sector employment continue, these areas will be less likely to fully benefit due to the lower importance of the private sector. And should the economy continue to weaken, these local governments are likely to have higher labor expenses and more difficulty reducing headcount due to the political strength and influence of local labor. According to the Bureau of Labor Statistics, in 2009 41% of government workers were unionized, including almost 47% of local government workers. The number in the private sector was 8%.

For those who work in the private sector or in urban areas, it can be difficult to conceive of how important State and local employment is in some areas of the country. On the following page is a map of employment by State and local governments as a percentage of total employment in each county. The data is taken from the Bureau of Labor Statistics QCEW program and does not include federal employees. The counties colored in the deepest shade of purple depend on State and local governments to employ more than 30% of their workers!



In analyzing this map for potential trouble spots, it is important to consider the overall economic and budgetary condition of the areas with a high percentage of government employment. States that have been able to weather the last three years with relatively little impact to their balance sheets are generally well positioned to continue providing consistent services to their communities. States that are already experiencing strain in the budgeting, on the other hand, are likely to need to spread the impact across stakeholders, including constituents, unions, and potentially bondholders.

Northern California and upstate New York stand out as particularly vulnerable on this map, as both States face difficulties in balancing their budgets. Other areas of concern include much of Georgia and the Florida panhandle. While strain continues to be felt nationwide, investors should be particularly aware of issuers that will be exposed to continued cuts in the public sphere. The potential “anti-stimulus” from State and local governments will eventually impact private sector growth, as essential services are cut. Already, there is anecdotal evidence that cuts in fire department budgets in Northern California are resulting in more fires growing out of hand, and that cuts in police forces are leading to higher crime rates: factors which can lower taxable land values and trigger a downward cycle for local budgets.

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