EVALUATING THE FISCAL POLICY OF STATES:

WHO ARE THE SINNERS, WHO ARE THE SAINTS?

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What is the Role of State Governments in Our Fiscal System?

RESPONSIBILITY NO. 1: Provide Services:

TOTAL = ED. + WELFARE + HEALTH/HOSP + HIGHWAYS + PRISONS

$5000 = $1800 + $1350 + $372 + $350 + $165

(36%) (27%) (8%) (7%) (3%)

At a Tax Rate on Personal Income of:

τ = .09

RESPONSIBILITY NO. 2: Managing Our Public Wealth:

W = [K + CASH] - [DEBT + UFL]
OUR FOCUS IS ON WEALTH MANAGEMENT

FIGURE 1: ALL STATES, ASSETS AND LIABILITIES

\[ W = [K + \text{CASH}] - [\text{DEBT} + \text{UFL}] \]

\[ W = [$7,600 + $2900] - [$2900 + ?????] = $7,600 + ?????? \]

\[ \text{K = REPLACEMENT COSTS OF EXISTING INFRASTRUCTURE} \]

\[ \text{CASH = MARKET VALUE OF NON-TRUST CASH AND SECURITIES} \]

\[ \text{DEBT = MARKET VALUE OF OUTSTANDING DEBT} \]

\[ \text{UFL = UNFUNDED PENSION LIABILITIES} \]
Figure 1

Assets & Liabilities
(2005 Dollars)

$ - Per capita (1000s)

PUBLIC CAPITAL
NON INS C&S
LTD OUT

ESTIMATES OF UFL: STATE & STATE MANAGED PLANS

1972: $3,500/PERSON

1982: $4,800/PERSON

1990: $4,200/PERSON

2008: $6,625/PERSON


INSERT TABLE: STATE UFL (TERMINATION VALUES)

FIGURE 2: ARE WE CLOSING THE GAP?
# STATE PENSION UNDERFUNDINGS

## [TERMINATION VALUES]

<table>
<thead>
<tr>
<th>State</th>
<th>ABO Liability Treasury Rate (L)</th>
<th>Pension Assets (A)</th>
<th>*State Population (N)</th>
<th>(L - A)*10^9/N</th>
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<tbody>
<tr>
<td>Alabama</td>
<td>61.8</td>
<td>21.4</td>
<td>4,708,708</td>
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<td>15.5</td>
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<td>75.2</td>
<td>33.1</td>
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<td>5.3</td>
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<td>64.3</td>
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<td>26.4</td>
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<td>Utah</td>
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<td>Wisconsin</td>
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<td>Wyoming</td>
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<td>4.4</td>
<td>544,270</td>
<td>$9,921.55</td>
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</tbody>
</table>

* State populations are from the 2009 Statistical Abstract (July 2009)
Figure 2
Annual Pension Underfunding
(2005 Dollars)

$ - Per capita


-10 -5 0 5 10 15 20 25 30 35 40

- UFL03
MANAGING OUR PUBLIC WEALTH

1. WHAT STATES DO:

SUR/REVENUES =

TAXES/FEES + AID + INTEREST/WDRAW + PROFITS + ASSET/SALES

SUR/EXPENDITURES =

WAGES/BEN + PENCONT + MAINTENANCE + GRANTS + INTEREST

SUR/REVENUES - SUR/EXPENDITURES = SUR

SUR > 0, Funding for Next Year, or Savings

SUR < 0, Need to Borrow Against Next Year
2. FOR WEALTH MANAGEMENT, WHAT STATES *SHOULD DO*:

\[
\text{PPWSUR/REVENUES} = \text{TAXES/FEES + AID + INTEREST/WDRAW + PROFITS + ASSET/SALES}
\]

\[
\text{PPWSUR/EXPENDITURES} = \text{WAGES/BEN + “NORMALCOST” + MAINTENANCE + GRANTS + INTEREST + “DEPRECIATION”}
\]

\[
\text{PPWSUR/REVENUES - PPWSUR/EXPENDITURES} = \text{PPWSUR}
\]

PPWSUR > 0, Funding for Next Year, Savings

PPWSUR < 0, Need to Borrow Against Next Year

3. SUR > PPWSUR
“FLOWS” = “CHANGES IN STOCKS”

$$PPWSUR = (p - \rho)\ell + [k - \delta(K_0 - A) - vA] + [s - c] + [-d]$$

$$(p - \rho)\ell = \text{Overfunding of Normal Cost, Supplemental Cost Contribution}$$

$$[k - \delta(K_0 - A) - vA] = \text{Net Investment - Market Value of Sold Assets}$$

$$[s - c] = \text{Net Contributions to Cash, “Rainy Day” Fund Build-Up}$$

$$[-d] = -[\text{New Borrowing - Repayment}], \text{Changes in Stock of Debt Outstanding}$$

LET’ S SEE HOW STATES ARE DOING

FIGURE 3: State Fiscal Surpluses

FIGURE 4: SUR/Revenues & SUR/Expenditures
Figure 3
State Fiscal Surpluses
(2005 Dollars)

$ - Per capita


-300 -200 -100 0 100 200 300 400 500 600 700

SUR

PPWSUR
Figure 4
State Revenues and Expenditures
(2005 Dollars)

$ - Per capita


REV EXP

1000 1500 2000 2500 3000 3500 4000 4500

Per capita

THE AGGREGATES, MAY HIDE THE PROBLEMS:
Looking at Individual States

FIGURES 5a-e: The “Headline States”

FIGURES 5f-5h: District 3 States

FIGURES 5i-5k: Have the Candidates “Walked the Walk”
Figure 5a
PPWSUR: California
(2005 Dollars)

$ - Per capita


-900 -800 -700 -600 -500 -400 -300 -200 -100 0 100 200 300 400 500 600 700 800 900

-PPW
Figure 5b
PPWSUR: Illinois
(2005 Dollars)

$ - Per capita

-300 -200 -100 0 100 200 300


PPW
Figure 5c
PPWSUR: Michigan
(2005 Dollars)

$ - Per capita

Figure 5d
PPWSUR: New York
(2005 Dollars)
$ - Per capita
PPW
(2005 Dollars)$
Figure 5e
PPWSUR: Ohio (2005 Dollars)

$ - Per capita


-200 -150 -100 -50 0 50 100 150 200
Figure 5f
PPWSUR: Pennsylvania
(2005 Dollars)

$ - Per capita


PPW
Figure 5g
PPWSUR: New Jersey
(2005 Dollars)

$ - Per capita
Figure 5h
PPWSUR: Delaware
(2005 Dollars)
Figure 5i
PPWSUR: Massachusetts
(2005 Dollars)

$ - Per capita

Figure 5j
PPWSUR: Texas
(2005 Dollars)

$ - Per capita

-100 0 100 200 300 400 500 600


- PPW
Figure 5k
PPWSUR: Utah
(2005 Dollars)

$ - Per capita


PPW
LOOKING FOR CAUSES: Who Saves, Who Doesn’t

FIGURE 6: Big States vs. Small States

FIGURE 7: “Mineral” States vs. the “Rest”

FIGURE 8: “Rust Belt” vs. “Wheat Belt” vs. “Sun Belt”

FIGURE 9: “Red” States vs. “Blue” States
Figure 6
PPWSUR: Big vs Small States
(2005 Dollars)

$ - Per capita

BIG10PPW
SML10PPW
Figure 7
PPWSUR: Mineral States vs Non-Mineral States
(2005 Dollars)

$ - Per capita

MINPPW

OTHPPW
Figure 8
PPWSUR: Rust vs Wheat vs Sun
(2005 Dollars)

$ - Per capita


RUSTBELT
WHEATBELT
SUNBELT
Figure 9
PPWSUR: Red States vs Blue States
(2005 Dollars)

$ - Per capita


REDPPW
BLUEPPW
DISCUSSION

QUESTION NO. 1: Is This a Problem?

In the Short-Run: Sure, but that’s why we save.

In the Aggregate: Not Really, Except for Pensions

For Some States: Absolutely, but So What?

Will There be a Contagion ala Italy and Greece?

Perverse Fiscal Incentives
QUESTION NO. 2: If There is Problem, What to Do?

SOLUTION NO. 1: Federal Bailouts?

ARRA was arguably a bailout.


SOLUTION NO. 2: Regulation via Balanced Budget Rules?

Ex Post, No Override, Independent Enforcer

FIGURE 10: “Strong” vs. “Weak” BBR States

FIGURE 11: “Elected” vs. “Appointed” Supreme Court Enforcement
Figure 10
PPWSUR: Strong BBR States vs Weak BBR States
(2005 Dollars)

$ - Per capita

Figure 11
PPWSUR: (Strong BBR Enforced by) Elected vs Appointed Supreme Court
(2005 Dollars)

$ - Per capita

SOLUTION NO. 3: Market Discipline?

No Federal Bailouts, Transparency

THE FRB “TRANSPARENCY PROJECT”