Wait for us

Like everywhere else, it seems, debt among state and local governments is rising

By RONALD A. WIRTZ
Editor

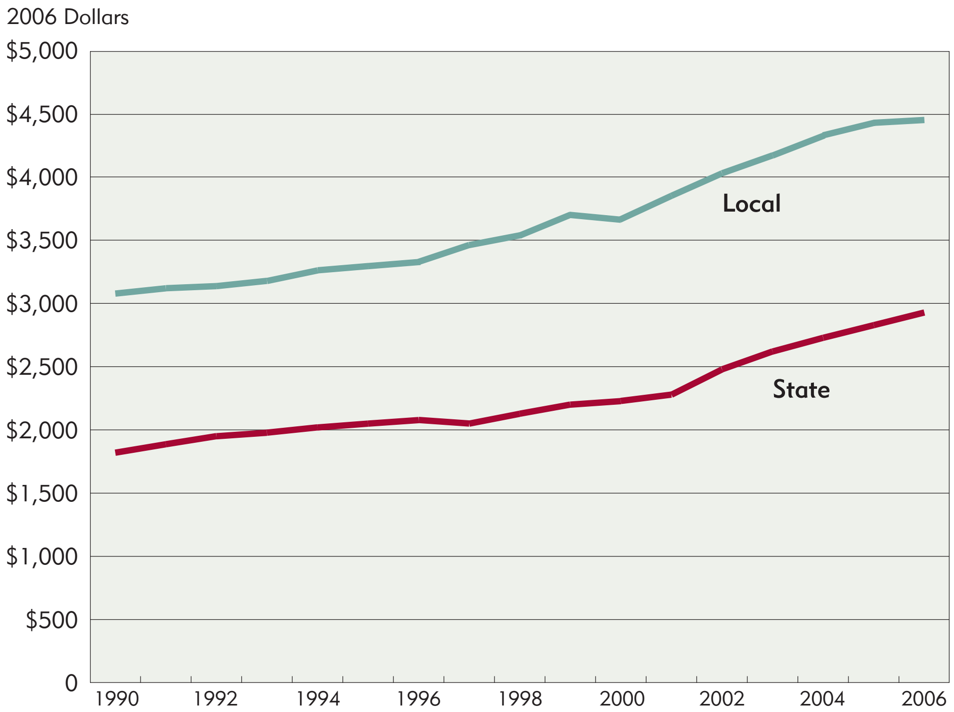
You've heard plenty of late about sky-high home foreclosures, rising credit defaults and unsustainable debt loads. Various federal bailouts and stimulus packages have also turned the spotlight on corporate and federal government debt.

What you haven't heard much about—at least not yet—is the rising debt of state and local governments. It's difficult to generalize public debt trends among Ninth District states and their many local governments, save to say that debt is rising almost across the board. But the trajectory of debt is rising at a different grade in different states, and among different levels of government.

There also seems to be a balancing act between debt at state and local levels, where high debt at one level is balanced by (comparatively) lower debt elsewhere.

Chart 1

Per Capita State and Local Government Debt in the United States



Source: U.S. Census, State and Local Government Finances

The fine print on public debt

The debt pie can be cut in many ways. Across the United States, for example, public debt has gone up steadily. Adjusted for inflation, it increased by 80 percent from 1990 to 2006 and by 32 percent from 2001 to 2006, according to the U.S. Census Bureau. The population has also grown considerably over this period, which matters when it comes to sustainable debt. On a per capita basis, growth of state and local debt was about 50 percent from 1990 to 2006 (see chart 1). Combined, state and local debt totaled $2.2 trillion. That might sound like a lot, but it is a fraction of federal debt, now more than $10 trillion.

Unfortunately, data on government debt are not as straightforward as one might hope. For example, Census figures often don't match the debt figures that states themselves publish in their comprehensive annual financial reports (CAFRs). (See Charts 2–4. Additional charts are available online at minneapolisfed.org.) Sometimes the figures can be wildly different. In Wisconsin, for example, Census figures show state-level debt at $21 billion in 2007, while the state lists outstanding debt at $11 billion. For Montana, Census figures show state-level debt at $4.6 billion in 2007, but the state declared it owed just $395 million. For North Dakota, however, Census and state figures are a close match.

The divergence stems from what is counted, and by whom. Census figures, for example, include bonded debt of any kind, whether general obligation, revenue or other forms. But many states don't recognize debt in a similar fashion. That's because state governments (local ones too) give bonding authority to various agencies and quasi-public authorities (also called "component units") to help finance things like health care facilities, housing programs, utilities, and higher education facilities and student loans.

But responsibility for repaying that debt technically lies outside the primary functions of state government. Payments for bonds issued by a health care facilities authority, for example, are made by the private health care organizations that benefit from the state-assisted financing. Because the bonds were issued by a state-based entity, the Census counts such debt. From a state's perspective, it bears no direct responsibility for repaying that debt, so states often don't count it (though some do), and there doesn't appear to be a standard formula for tracking debt among states.

The statistical pablum is important because state debt trends can look very different depending on the figures you look at. Montana's state debt has exploded according to Census figures. By the state's own record-keeping, it's a fiscal tightwad.

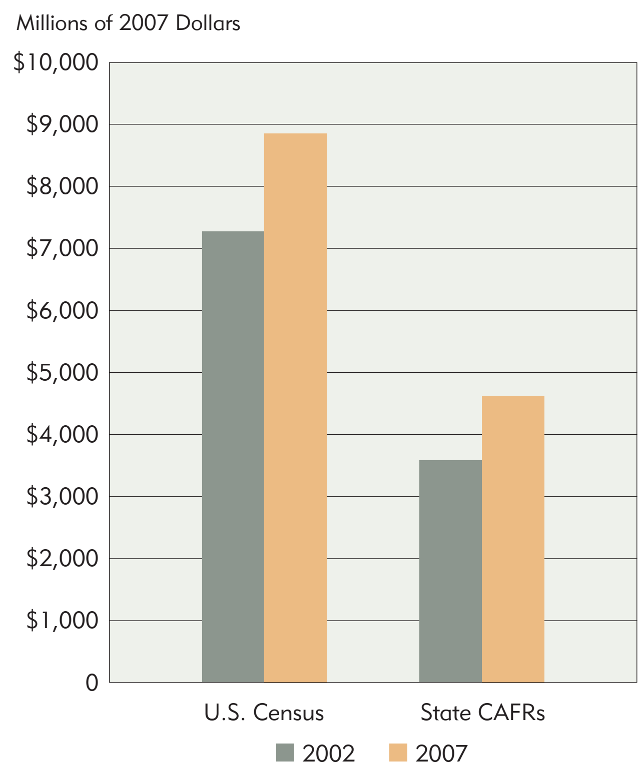
Balloon debt

Before any particular state starts to feel really good or bad about its fiscal condition, it should examine debt among its local governments: Counties, cities and school districts hold an enormous amount of debt.

Data on local government debt are typically not as current as state-level data and tend to be spottier. The Census also offers no comparable figures for local government in a particular state. Most such data come from states (often only on request), and it's difficult to know the accounting methods in each case. Indeed, not all states track local government debt. North Dakota, for example, collects no debt data at the municipal or county level, and Minnesota similarly has no annual data on debt among its hundreds of school districts.

The data that are available suggest that government debt is like a balloon: Squeeze or control it at one level of government, and it's likely to bulge out

Chart 2 **Two Measures of Minnesota State Debt***



*At end of fiscal year

Sources: U.S. Census, State and Local Government Finances; Minnesota comprehensive annual financial reports

Chart 3

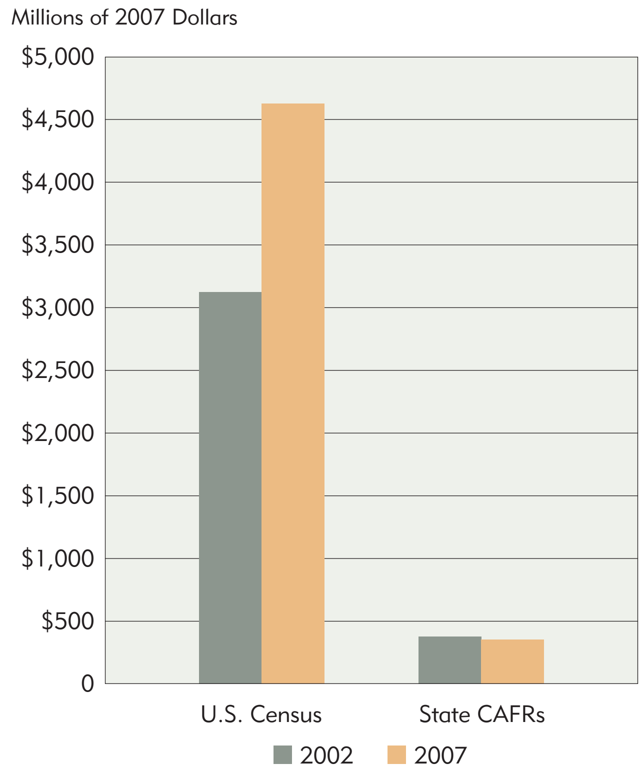
Two Measures of North Dakota State Debt*

*At end of fiscal year

Sources: U.S. Census, State and Local Government Finances; North Dakota comprehensive annual financial reports

Chart 4

Two Measures of Montana State Debt*



*At end of fiscal year

Sources: U.S. Census, State and Local Government Finances; Montana comprehensive annual financial reports

elsewhere. Debt exploded at the state level for Wisconsin from 2002 to 2007, for example, but debt growth at the school district, county and city levels was subdued more than in any other district state. It was the opposite for Montana, and particularly South Dakota: Modest levels of state debt were belied by much higher debt growth among different levels of local government (see Chart 5).

In some district states, total outstanding debt is also considerably higher among local governments. In Minnesota, the state's debt of $4.7 billion (as measured by the state, not the Census) is dwarfed by the $8.3 billion owed by its cities, according to data from the Office of the State Auditor. Data from the Minnesota Department of Education suggest that cumulative debt for school districts ranges upward of $7 billion or $8 billion. In Montana and South Dakota, city and school district debt are similarly as high as or higher than state debt. Though growth rates of county-level debt were high in a couple of instances, nominal county debt was comparatively low across the board.

If there is good news regarding debt, it's that governments at all levels have benefited from unrivaled low borrowing costs through much of this decade, reducing the cost of recent borrowing and offering the opportunity to refinance more expensive legacy debt.

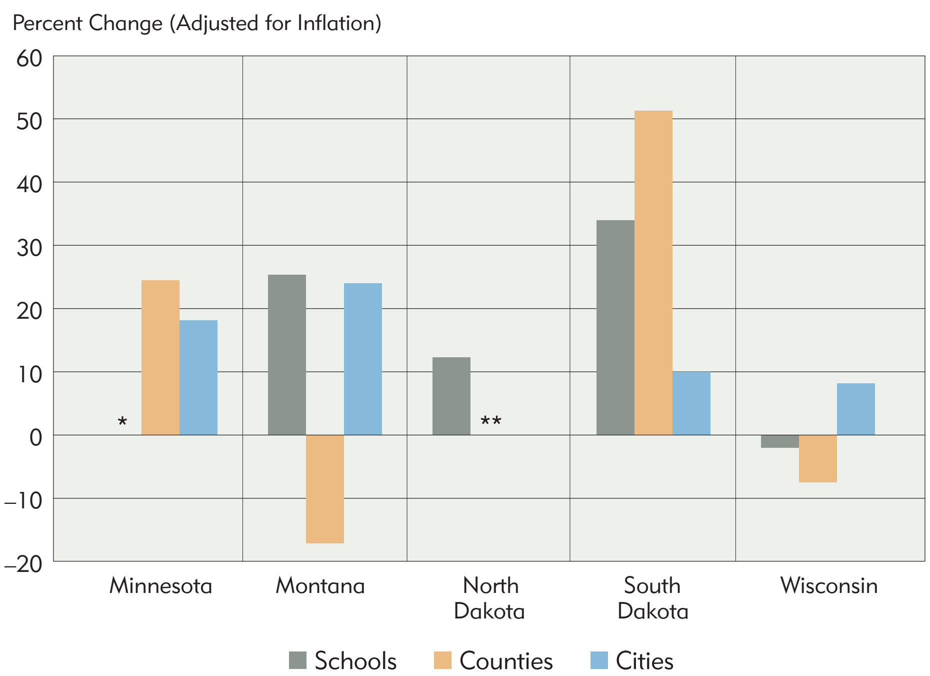
The velocity of debt accrual appears to be abating as well. Though bond issues are not the only way for governments to accrue debt, they are a major source, and since 2002 state and local governments in the district have scaled back on the annual number and size of issues they have taken to the bond market.

Borrowing for capital projects is also likely to remain modest in the near term, given tightness in the municipal bond market and red ink gushing from state budgets, particularly in Minnesota and Wisconsin. The federal stimulus package will also help state and local governments tackle some of their infrastructure priorities that might have otherwise required borrowing. f

Chart 5

Debt Growth Among Local Government Jurisdictions

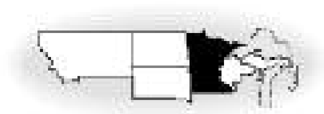
2002 to 2007



*School debt not available; county debt through 2006 only.
**City and county debt not available.

Sources: Minnesota Office of the State Auditor; Montana Local Government Services Bureau; North Dakota Department of Instruction; South Dakota Department of Legislative Audit, South Dakota Department of Education; Wisconsin Department of Revenue, Wisconsin Department of Public Instruction

MINNESOTA



Mother Teresa takes a hit from stock decline

Recessions take no prisoners. That includes foundation and other grant makers, who said support to nonprofits will likely be flat or decline this year.

The Minnesota Council of Nonprofits surveyed 107 grant-making organizations late last year, including private, corporate and community foundations, and found that a majority of them are expecting to reduce their giving this year, some by as much as 4 percent, because of the decline in the stock market and related asset bases. The worse news is that grant makers foresee further asset losses in 2009.

Consequently, grant makers anticipated the number of awards to decrease; more than four times as many expected to decrease awards (36 percent) as expected to increase awards, though a fair portion reported being uncertain about 2009 grant making. The largest foundations, which award $10 million or more annually, expected their giving to decline only 1 to 2 percent. That might seem manageable, but it is compounded by nonprofits' expectations of much higher demand for services this year.

And you thought housing was bad

While most of the attention this recession has been on housing, trends in commercial property in some markets have been just as deflating.

For example, the combined dollar value of office property sales in the downtowns of St. Paul and Minneapolis crashed by two-thirds last year compared with 2007, on par with the trend nationwide, according to the research firm Real Capital Analytics. Some of the drop is due to lower square-foot prices, but a majority was due to a lack of interested buyers. A report by Colliers International noted that larger sales were "noticeably absent."

The value of retail space sold was also down by two-thirds. Sales of industrial property looked comparatively bright, falling "just" 19 percent, compared to 46 percent nationwide; the average price per square foot sold reportedly even rose slightly. Most of the sales, however, occurred in the first half of 2008, according to Colliers.

A separate survey by Colliers' investment business found that more than three-quarters of investors in these markets expected to stay on the sidelines until the second half of 2009.

—Ronald A. Wirtz