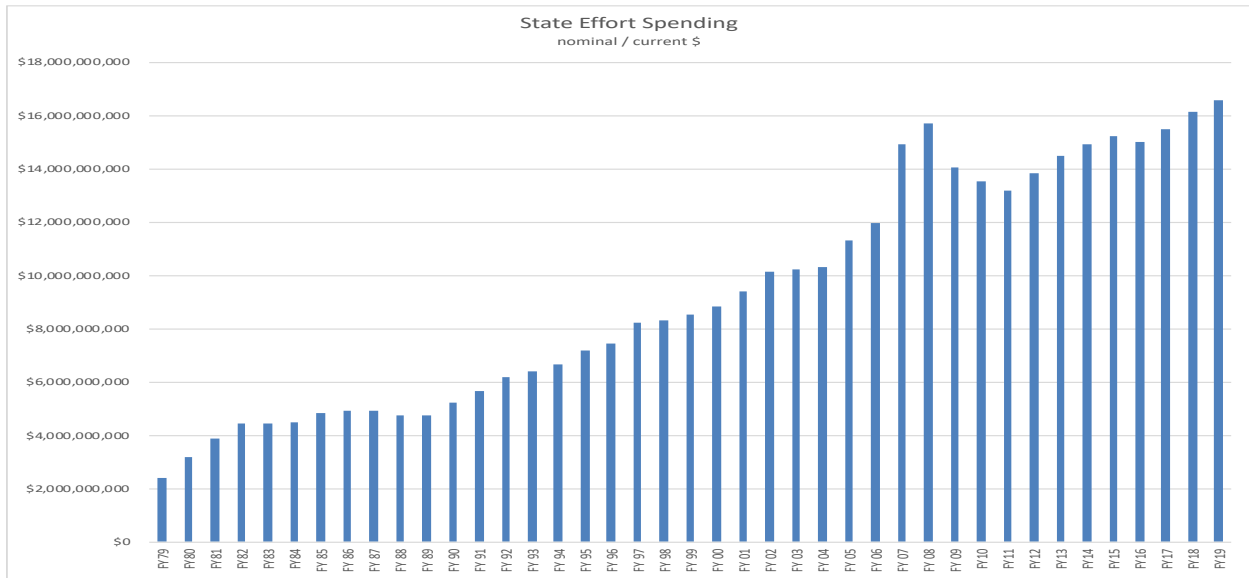


# How Large Is State Government?

The question of the size of state government has become a component of the overall budget debate. The following discussion and accompanying charts are meant to inform this question. The chart below is the history of total state effort spending since FY79 through FY19.<sup>1</sup>



The growth in state effort spending over time is obvious, but not very interesting. Virtually all economic and fiscal aggregates increase over time, reflecting the increasing size of populations, incomes, and the economy in general. Absolutely increasing expenditures doesn't say much meaningful about the size of government.

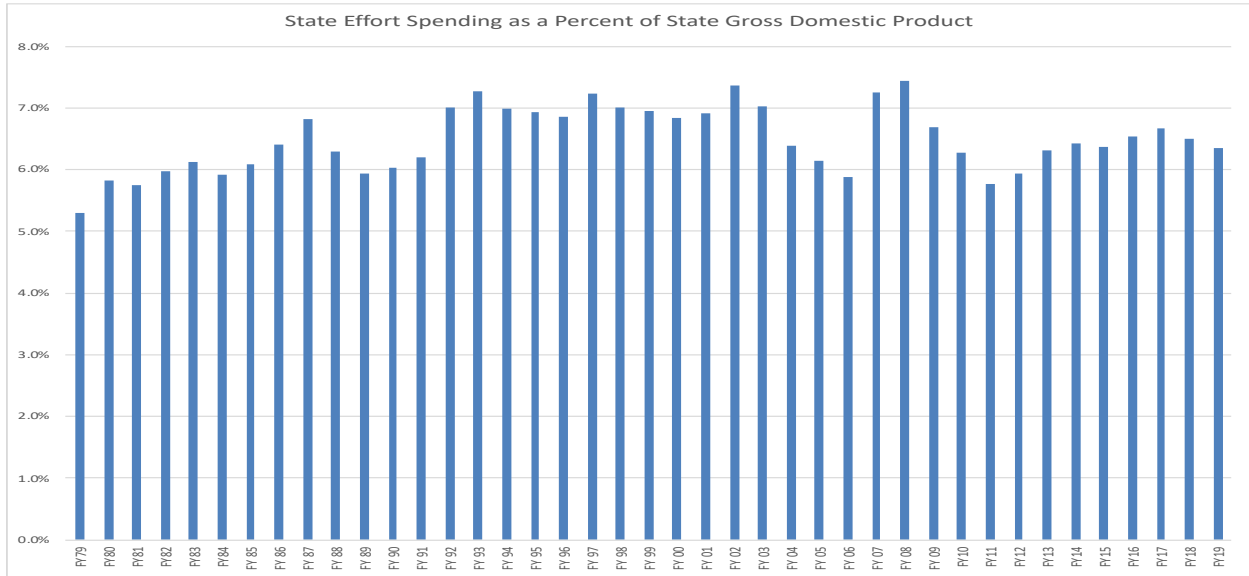
In addition, the use of state budget means-of-finance concepts overstates the true state effort level of spending because substantial federal funding is appropriated through state statutory dedications and self-generated revenue means-of-finance. For example, in FY19 \$1.118 billion of federal funds were appropriated through state effort means-of-finance statutory dedications and self-generated revenue (Transportation Trust Fund, Clean Water State Revolving fund etc). Thus, state effort levels were overstated by approximately 7% and consequently, state effort as a percentage of the state economy was overstated by about four-tenths percentage points for that year, the measure of the size of state government examined by this brief. The effect of this overstatement of state effort occurs in all years to varying degrees.

Since true state effort expenditures are financed by extracting revenue from the state economy, the more interesting metric is the ratio of state effort expenditures to the state's economy. This reflects how large state effort expenditures are relative to all expenditures in the economy, and

<sup>1</sup> The concept of "state effort" encompasses all state government expenditures other than those designated as federal means-of-finance in state budgeting; namely, the budgeting means-of-finance categories of state general fund-direct, fees & self-generated revenue, and statutory dedications. All figures are reported in the Executive Budgets of the state government, reflecting actual expenditures of the completed prior year. The fiscal years depicted are the earliest year of data available to the Legislative Fiscal Office through the last fiscal year available.

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is commonly considered a measure of the size of government in a meaningful sense. The size of the economy is measured by state gross domestic product.<sup>2</sup> The chart below depicts that ratio over the historical period FY79 through FY19.



Since the height of each bar is a ratio, the change in the height of each bar from year-to-year reflects the relative change in state effort expenditures to total expenditures in the economy. From the perspective of generally rising expenditures, an increase in the height of the bars means state effort spending increased more than total spending in the economy increased. A decrease in the height of the bars means state effort spending increased less than total spending in the economy increased.

The fairly steady upward trend in the level of nominal state effort expenditures indicates that much of the variation in this ratio results from the various forces that influence the state economy. National and international economic conditions, and particularly energy markets with regard to the relatively large energy producing and consuming industries of Louisiana, have outsize influence on the annual and short-run size of state government as reflected in this metric. The multi-year disturbance of hurricanes Katrina and Rita at the beginning of FY06 is also evident in both charts above.

However, the most remarkable aspect of the ratio is the long-run stability within the 6% - 7% range. If the size of government were getting continually larger, we would expect the ratio to be getting continually larger as state effort spending comprised a larger and larger share of total

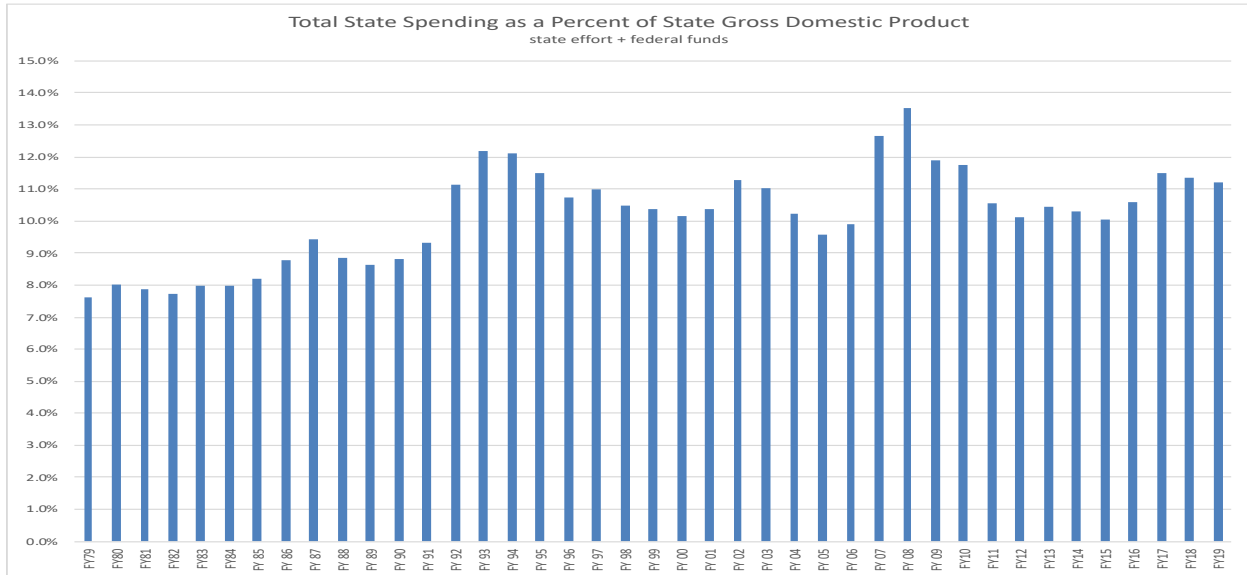
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<sup>2</sup> State gross domestic product is analogous to the national gross domestic product concept, and is estimated by the same federal agency, the Bureau of Economic Analysis of the U.S. Department of Commerce. Values reflect total expenditures on current production in the economy and are estimated for each quarter of the year on an annualized basis. The quarterly observations that comprise state fiscal years are averaged into a single annual value reflecting the July – June fiscal year of state government expenditures to provide the denominator of the ratio.

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spending in the economy, reflected in continually higher and higher bars in the chart. Over the long run, this has not happened. The relatively stable ratio reflects the fact that, over the long-run, state effort spending has increased at a pace roughly equivalent to the pace of total spending in the economy.<sup>3</sup> State government has not been getting larger relative to the economy.

The relative stability of the long-run size of state government is also evident when federal means-of-finance is added to state effort expenditures. The chart below depicts the ratio of total state government expenditures to the total of expenditures in the state economy.



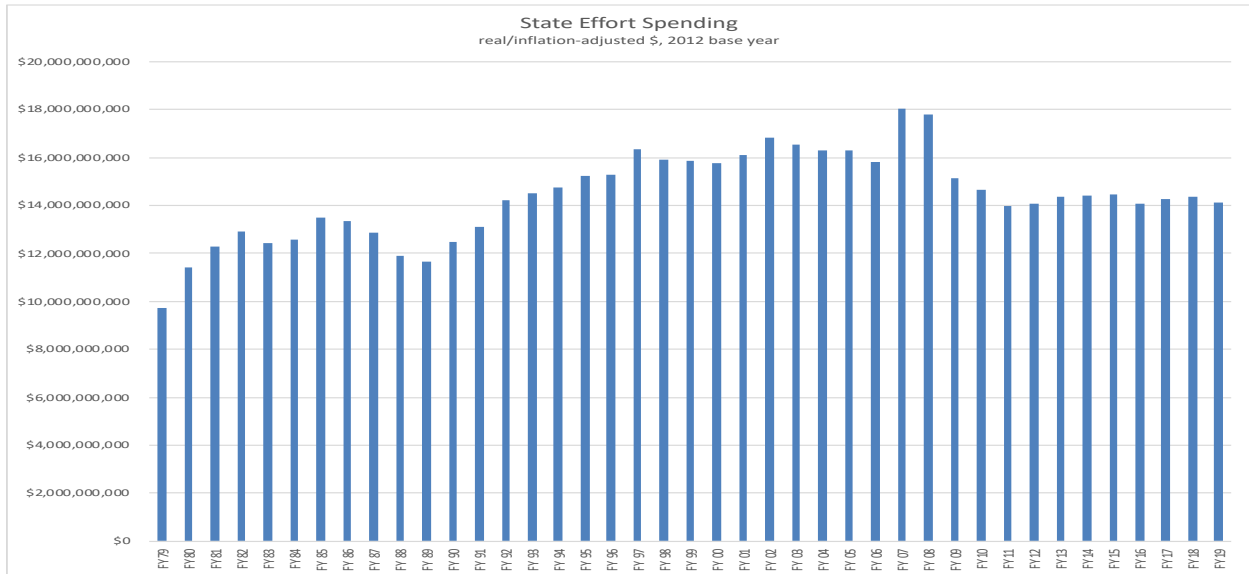
With the inclusion of all federal funds, the expenditure numerator of the ratio is higher for the same economy size denominator, resulting in all the bars being higher than when only state effort expenditures are included.<sup>4</sup> However, over the long-run, the total spending result is similar to the state effort spending result. Even with federal means-of-finance included, the long-run size of state government has been fairly stable in the range of 10% - 12% of the total state economy, and mostly in the 10% - 11% range since the early-1990s.

<sup>3</sup> State effort spending is financed by extracting taxes and fees from the state economy. Since State government has to run a balanced budget from year-to-year, it is not possible for the State share of total spending in the economy to continuously grow unless tax rates and/or bases are continuously increased by statutory and/or administrative action. The relatively stable share of state effort spending evidences the fact that this does not occur. Another way for the State share to rise continuously would be a growing value of natural resource extraction. This may be an explanation for a rising State share in the 1970s and early 1980s, but has not been much of a factor since then.

<sup>4</sup> Since the numerator includes federal means-of-finance expenditures, it might be appropriate to include in the denominator some amount of additional total-economy expenditures. However, it is difficult to make sense of this adjustment since the total state economy utilized in the denominator is already, in part, attributable to federally financed expenditures. The more appropriate adjustment might be to reduce the denominator for use in the state effort ratio to reflect total-economy expenditures attributable to only state financed spending. These considerations seem trivial in light of the fact that Louisiana comprises only a very small share of national economic aggregates, typically around a 1.4% share.

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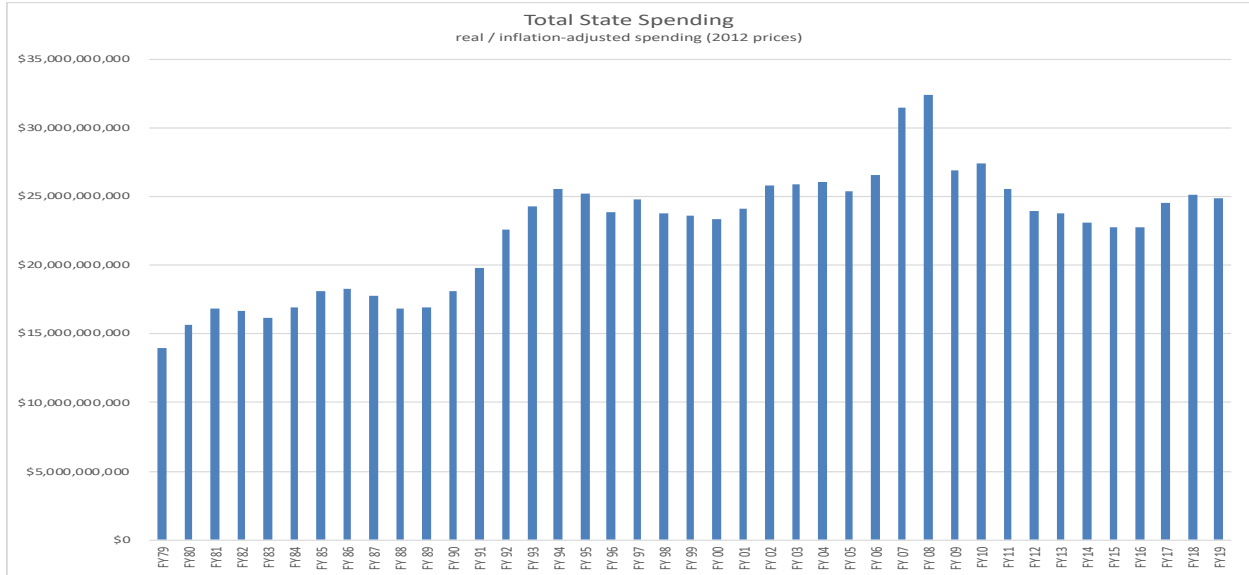
Another check on this long-run stability observation is to look at spending after adjusting for inflation. The chart below depicts state effort expenditures adjusted for inflation<sup>5</sup>. This puts the expenditures in a buying power context. As seen in the chart below, variation and cycling over the years occurs, but the longer-run phenomenon of governmental stability, especially since the late-1990s, is exhibited in real inflation-adjusted spending, as well.



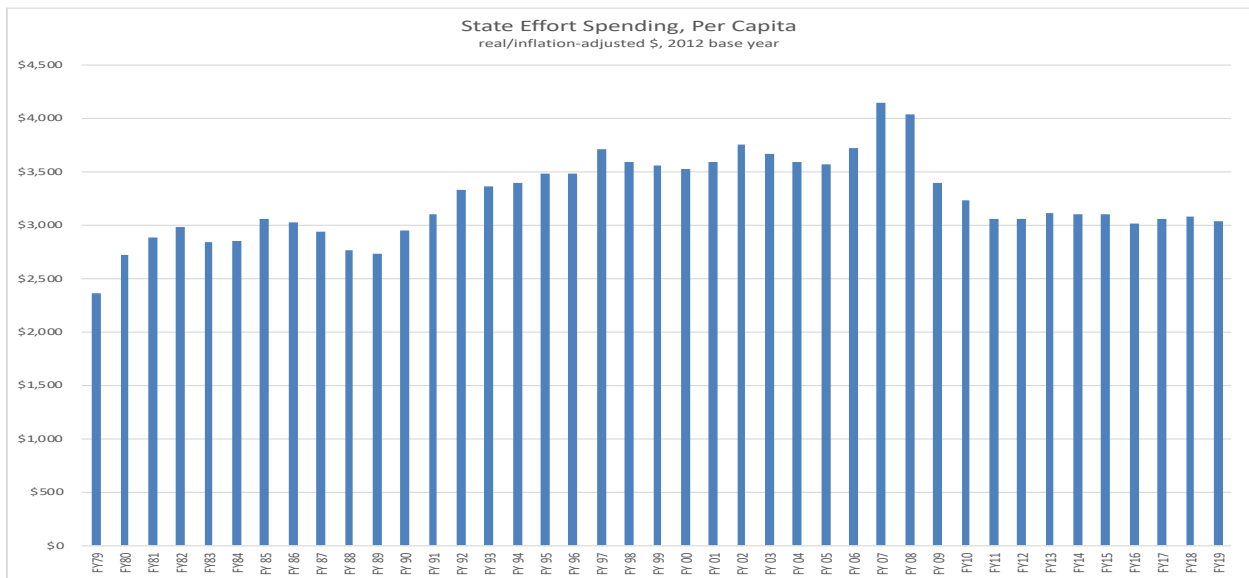
When federal means-of-finance is added, the inflation-adjusted level of spending still exhibits cycling, and more of an upward trend over the course of the total history. The chart below depicts total state expenditures, including federal means-of-finance, adjusted for inflation. Thus, if there has been an increase in the size of state government, as reflected in this particular metric, it has been largely attributable to federal financing. However, even this metric has exhibited relative stability since the mid-2000s.

<sup>5</sup> Annual nominal state effort expenditures were adjusted to a 2012 base year buying power utilizing the state & local government total consumption chained price index generated by the U.S. Dept. of Commerce, Bureau of Economic Analysis. Thus, expenditures prior to 2012 are inflated to a 2012 dollar equivalent, while expenditures after 2012 are deflated to a 2012 dollar equivalent.

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A final exhibit of the stability of the size and effort of state government is reflected in the two charts below, depicting inflation-adjusted state effort expenditures and total expenditures, including federal means-of-finance spending, both on a per capita basis. The first chart below depicts inflation-adjusted state effort expenditures per capita, and exhibits remarkable stability over the course of the entire history. While the population, the economy, and nominal expenditures have grown over time, state effort financed purchases of real services for residents on average have been largely flat<sup>6</sup>.



<sup>6</sup> Over this history, the state population has grown by 13.2% or over 543,000 residents, and the state economy has grown by 21.3% in real inflation-adjusted gross domestic product.

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The chart below depicts per capita inflation-adjusted total state expenditures, including federal means-of-finance. More cycling and modest upward trending occurs with federal financing included, but still relative stability from the mid-1990s. Again, any increase in the size of state government spending over this forty year history has been largely attributable to federal means-of-finance.

