KEYBRIDGE RESEARCH

KEY INSIGHTS

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# U.S. Public Sector Employment Now At Turning Point

## Key Insights

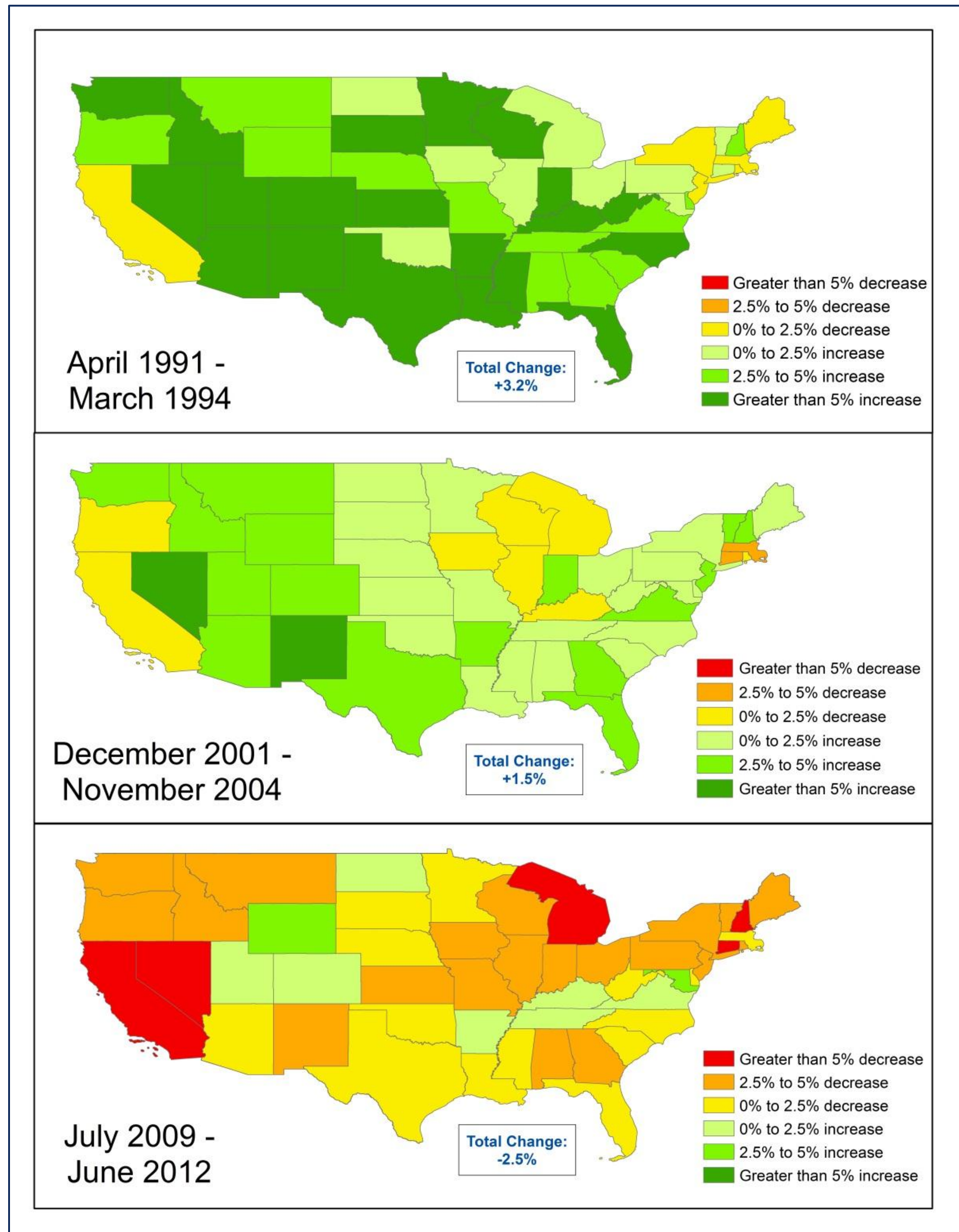
- Since the end of the Great Recession, employment in the public sector has declined significantly. This result is atypical; following the last two recessions, the public sector grew by 3.2 percent and 1.5 percent (respectively) during the first three years of economic recovery.
- The decline in government employment is largely a byproduct of state budgetary pressures caused by the recession.
- Recent data suggest that public sector employment may have turned a corner. Nationally, the decline in government jobs slowed significantly in 2012, and public sector payrolls increased in three of the last four months. This trend is particularly prevalent in states that no longer face projected budget shortfalls.
- Rebounding housing markets, resurgence in the automobile and manufacturing industries, and large increases in domestic energy production are among the likely factors contributing to the improvement in state budgets. As fiscal pressures on state and local governments ease, states are better able to balance their books while also maintaining and growing the public sector workforce.

*The public sector has steadily declined in the years after the Great Recession, dragging down the pace of overall job growth.*

The recent recession was the deepest and lengthiest experienced in the United States since the Great Depression in the 1930s. Roughly 7.5 million American jobs were lost from December 2007 to June 2009 during the recession itself (representing 5.4 percent of U.S. workers), and an additional 1.2 million jobs disappeared before the labor market finally bottomed out in February 2010. Indeed, more than twice as many jobs were lost during the recession than were lost during the previous two recessions combined.

One of several factors contributing to the tepid and uneven nature of job growth since the end of the recession has been the persistent decline of government payrolls. This decline significantly differs from the last two economic recoveries. As shown in the bottom map of Figure 1, public sector payrolls fell by 2.5 percent during the three years following the recession, representing a loss of more than 570,000 jobs. Conversely, government payrolls *increased* by 3.2 percent and 1.5 percent in the 36 months following the 1991 and 2001 recessions (respectively), as illustrated in the top two maps of Figure 1.

**Figure 1: Change in Government Employment Following Last Three Recessions**




*The widespread loss of government jobs during the current economic recovery is atypical relative to the last two recoveries.*

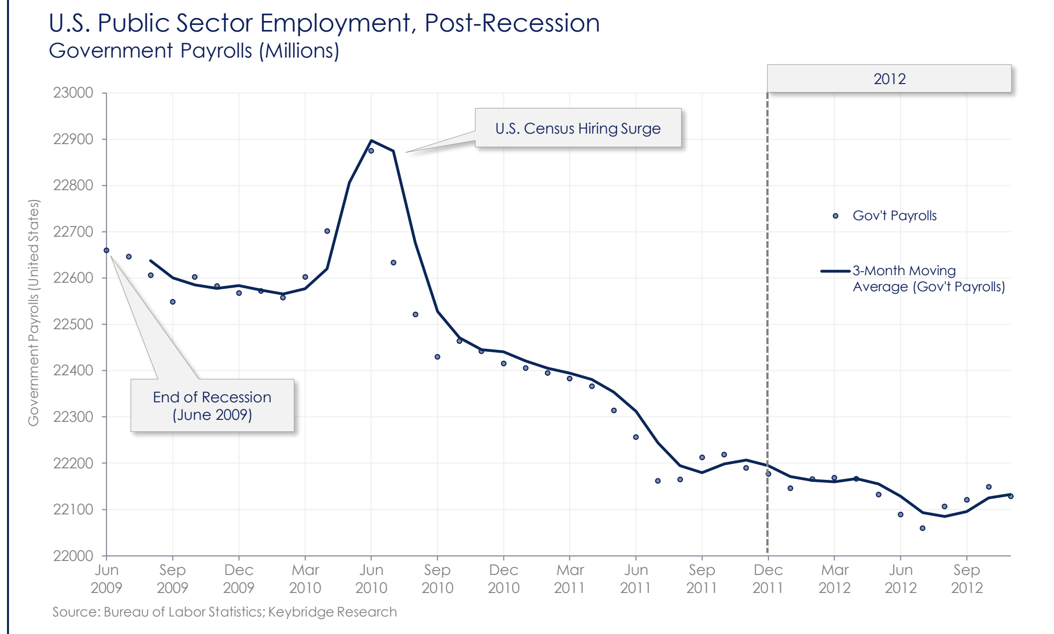
*The decline in public sector employment was largely the result of state budgetary pressures.*

The decline in public sector employment since the Great Recession ended has been driven largely by historically unprecedented state budget deficits. States faced shortfalls totaling $540 billion from 2009 to 2012 — more than double the cumulative shortfalls that occurred over a similar length of time following the 2001 recession — and in most states these shortfalls necessitated severe spending cuts and layoffs and restricted new hiring.[1]

While the decline in government payrolls in the three years following the recession was severe, this trend has slowed in 2012, and recent data suggest that public sector job losses may have finally "bottomed out." As shown in Figure 2, with the exception of a temporary hiring surge related to the 2010 Census in the spring/summer of that year, public sector employment generally fared better in 2012 than at any other point during the recovery. Specifically, while government payrolls declined by a 2.6 percent annualized rate nationally from May 2010 – December 2011, in 2012 the annualized decline has been only 0.2 percent, and since August the public sector has *expanded* by a 0.4 percent annualized rate.

*Recent data suggest that the public sector may have finally "bottomed out."*

## Figure 2: Change in Government Employment Following 2009 Recession

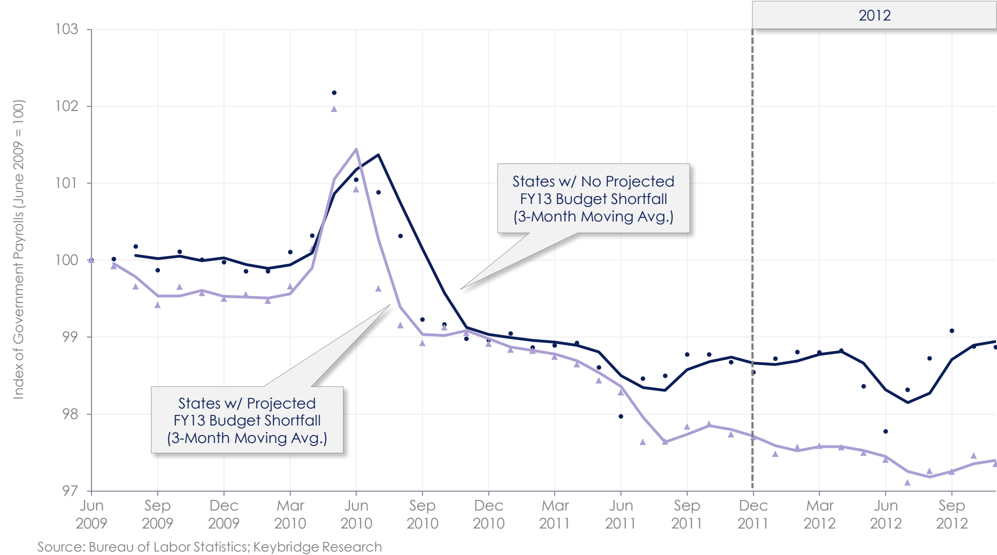


Source: Bureau of Labor Statistics; Keybridge Research

Not surprisingly, the rebound in public sector employment is most apparent in the 20 states that are projected to have no budget shortfall in 2013, as shown in Figure 3.[2] In these states, government payrolls have increased in 2012 at a 0.4 percent annualized rate, while states with persisting budget gaps have seen a decline in public sector jobs of 0.4 percent (annualized) over the same period.

*States with no projected FY13 budget shortfall are experiencing faster growth in public sector employment.*

Figure 3: Change in Government Employment Following 2009 Recession in States with Projected Budgetary Shortfalls



Source: Bureau of Labor Statistics; Keybridge Research

Several factors are likely contributing to the improvement in state budgets and the resurgence of the public sector:

*An improved housing market — coupled with growth in the manufacturing and energy production sectors — is helping many states generate more tax revenue, balance their budgets, and resume public sector hiring.*

- First, there is growing evidence that the U.S. housing sector has finally turned a corner. According to the most recent Federal Housing Finance Agency monthly report, U.S. home prices have increased in 2012 by 5.4 percent (annualized).[3] Increasing home prices lead to greater tax revenues for state and local governments, which eases budgetary pressures and facilitates public sector employment growth.

- Second, the resurgence of the U.S. automobile and manufacturing sectors is partially responsible for improving state budgets, particularly in states where these are major industries. Through November, U.S. auto sales in 2012 have increased by 13.7 percent (+15.1 percent annualized rate),[4] boosting industry profits and spurring economic activity in auto-producing states. This growth, in turn, has generated additional tax revenue for state and local governments and led to increased public sector hiring flexibility. In addition, historically low domestic natural gas prices and rising overseas labor costs are causing some manufacturing companies to relocate back to the United States after decades of industry decline, which is also a likely factor contributing to the improving economies of these states.

- Third, large increases in domestic energy production made possible by new extraction technologies have improved local economies and provided a financial windfall to state governments. From 2009 – 2012, domestic crude oil production increased by 17 percent and domestic natural gas production

increased by 12 percent; these trends are expected to continue.[5] A ramp-up in "unconventional" oil and natural gas extraction through horizontal drilling and hydraulic fracturing has generated additional state and local tax revenue, affording these states more flexibility in balancing their budgets without laying off public workers. As shown in Figure 4, in the eight states in which oil and gas extraction comprises at least two percent of the state economy,[6] the public sector has increased by 0.6 percent (annualized) in 2012 — substantially better than the 0.4 percent annualized decline that has occurred in all other states.

*The recent boom in oil and natural gas extraction has provided additional tax revenue for energy-rich states and allowed the public sector in these states to recover more quickly.*

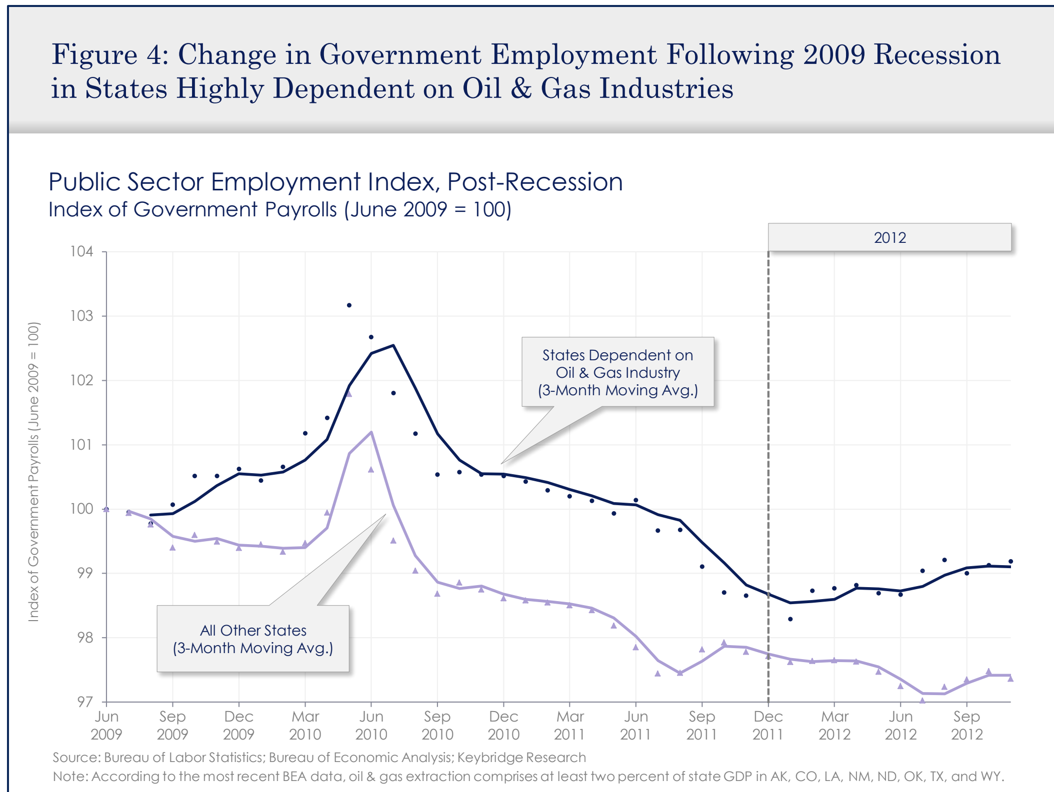



Figure 4: Change in Government Employment Following 2009 Recession in States Highly Dependent on Oil & Gas Industries

Source: Bureau of Labor Statistics; Bureau of Economic Analysis; Keybridge Research
Note: According to the most recent BEA data, oil & gas extraction comprises at least two percent of state GDP in AK, CO, LA, NM, ND, OK, TX, and WY.

*Moving forward, public sector job growth could provide an added boost to U.S. employment and the economy.*

Public sector employment faces significant challenges due to ongoing efforts to curb federal government spending through "fiscal cliff" and debt ceiling negotiations, as well as continued budget shortfalls at the state and local level in many jurisdictions. However, despite these headwinds, recent data suggest that the trend of public payroll reductions may be reversing. Improvements to government payroll data will provide additional downward pressure on the unemployment rate. Moreover, even if public sector employment growth is flat in the coming months, it would represent a marked improvement given the perpetual declines that have occurred since mid-2010.

[1] Center on Budget and Policy Priorities (CBBP) (2012). "States Continue to Feel Recession's Impact." June 27, 2012. Available at http://www.cbpp.org/files/2-8-08sfp.pdf.

[2] CBBP (2012). The 20 states are Alaska, Arizona, Arkansas, Delaware, Idaho, Indiana, Iowa, Kansas, Michigan, Montana, New Mexico, North Dakota, Oklahoma, Rhode Island, South Carolina, South Dakota, Tennessee, Utah, West Virginia, and Wyoming.

[3] Federal Housing Finance Agency (2012). "FHFA House Price Index Up 0.5 Percent in October." Monthly Index Values for Latest 18 Months: U.S. and Census Divisions. Available at http://www.fhfa.gov/webfiles/24839/OctoberMonthlyHPIF122012.pdf.

[4] Haver Analytics (2012). Data sourced from the Department of Commerce, Bureau of Economic Analysis.

[5] Energy Information Administration (2012). "Annual Energy Outlook 2013 Early Release." Data tables available at http://www.eia.gov/forecasts/aeo/er/.

[6] According to the most recent data from the Bureau of Economic Analysis, the eight states in which oil and natural gas extraction comprise at least 2 percent of the state economy are Alaska (16 percent), Wyoming (14 percent), Louisiana (7 percent), Oklahoma (7 percent), Texas (6 percent), New Mexico (5 percent), Colorado (2 percent), and North Dakota (2 percent).