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BUSINESS ENVIRONMENT REPORT B220

Local and state government investment

September 2021

Key Statistics

Estimated value in 2022: $349.74 billion

2017-2022 Compound Growth: -0.51%

Forecast value in 2027: $373.15 billion

2022-2027 Compound Growth: 1.30%

Current Performance

Unlike the federal government, state and local governments must balance their annual budgets. Any existing deficit must be covered with bond issuances. However, because state and local governments cannot buy back their issued bonds and experience actual default risk, they generally experience a tougher and more expensive credit market than the federal government. As a result, when new expenses appear or revenue drops, state and local governments often have to cut spending from somewhere else. Over the past decade, spending on social benefits increased significantly for state and local governments due to the aging population. Older citizens require more medical care and the aging population of the United States has caused state governments to allocate larger portions of their budgets to Medicare and other programs for the elderly. As a result, governments often cut investment programs, leading to periods of stagnant or receding investment totals.

The recession in 2008 and 2009 severely damaged nonfederal investment. This economic downturn caused sweeping job losses and wage declines, drastically reducing tax revenues for state and local governments. Many states and municipalities then experienced budget crises due to this severely restricted revenue. Though the federal government provided funding through the American Recovery and Reinvestment Act of 2009 stimulus plan, state and local investment fell 1.0% in 2009 and 3.8% in 2010. While the overall US economy improved over 2011, federal aid began to dry up and the unemployment rate remained largely unchanged, causing local and state government investment to decline 4.5% in 2011.

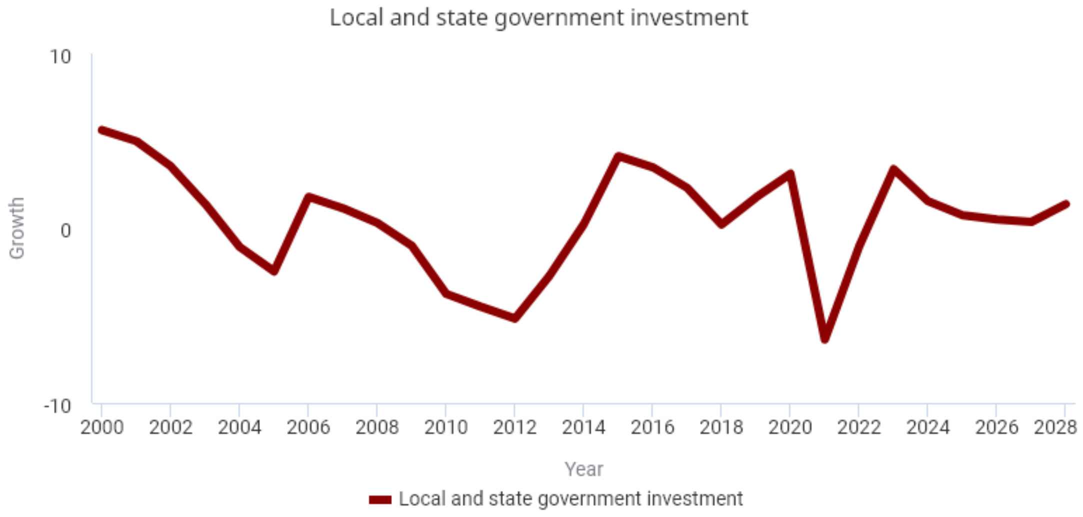
While state tax revenue has gradually recovered as economic growth picked up, state governments must also cope with declining federal government assistance, in particular, the end of stimulus funding from the American Recovery and Reinvestment of Act of 2009. As federal funding dries up, state governments cut back expenditures to balance their books. As a result, state and local government investments fell a record 5.2% in 2012, followed by a decline of 2.7% in 2013. The value of state and local government investments remained stagnant in 2014 and then increased 4.1% in 2015, as municipalities attempted to revamp investment to boost low productivity gains. However, ongoing budget shortfalls caused the value of these investments to slow in 2017. This has changed once more in 2021, declining 6.4% amid the COVID-19 (coronavirus) pandemic and economic downturn as budgets are constricted after 2020. Overall, this metric is estimated to decrease at an annualized rate of 0.5% over the five years to 2022.

Local and state government investment represents the total value of funds allocated by local and state governments for fixed assets such as structures, equipment and software. Data is sourced from the Federal Reserve Bank of St. Louis and is measured in chained 2012 dollars.

Outlook

Local and state government investment is projected to rise at an annualized rate of 1.3% over the five years to 2027. While a sustained level of low unemployment and gradually rising wages will likely bolster government investment activity over the coming years, various demographic and political trends will significantly constrain the value of these investments. In particular, the aging US population will continue to restrict the amount of funding that can be used for investment. The retired proportion of the US population will continue to expand during the forecast period, putting further strain on government social programs. In turn, the mounting financial liability of these programs will force governments to divert funds away from the growth of other areas, such as investment programs.

Data Volatility



Year	$ billion	% Change	Year	$ billion	% Change
1999	333.33	N/A	2014	325.47	0.2
2000	352.08	5.6	2015	338.90	4.1
2001	369.62	5.0	2016	350.74	3.5
2002	382.73	3.5	2017	358.84	2.3
2003	388.07	1.4	2018	359.63	0.2
2004	383.92	-1.1	2019	365.98	1.8
2005	374.45	-2.5	2020	377.36	3.1
2006	381.17	1.8	2021	353.36	-6.4
2007	385.53	1.1	2022	349.74	-1.0
2008	386.75	0.3	2023	361.56	3.4
2009	382.85	-1.0	2024	367.14	1.5
2010	368.47	-3.8	2025	369.90	0.8
2011	351.94	-4.5	2026	371.77	0.5
2012	333.74	-5.2	2027	373.15	0.4
2013	324.67	-2.7	2028	378.32	1.4