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Urban fiscal stress: Is it inevitable?

Charles F. Stamm

That younger cities also have lower private investment may be due to the fact that such investment is just building up. Therefore, to establish the relative industrial age, each city was classified on the chart according to both its recent population growth or decline and the change in manufacturing employment.

Then, for each grouping of cities in the chart, the mean values for each financial variable were arrayed against the social, economic, and structural groupings. Analyzing the chart on page 16 enables the reader to determine:

—What economic, social, and structural conditions are associated with cities showing fiscal strength or stress?
—What cause and effect relationships might exist between variables?

The chart provides a statistical base for the different financial conditions that occur under different social, economic, and structural conditions.

For example, as population ceases to grow, or even declines, the demand for social services increases. Note the difference in current operating expenses between mature and young cities: the group containing Hartford and Buffalo—both mature cities—has mean expenses of $618.21, while the group containing Topeka and Little Rock—both young cities—has a mean of $416.89.

As services increase, so does the municipal workforce—sometimes growing three or more times the size of that in younger cities. For example, in an older city such as New Haven, the municipal employment rate is 7 percent of the city's total employment, while that of Omaha and Grand Rapids is but 2.5 percent.

To support these services, greater demands are placed on the city's financial resource base. Thus, the rise in federal and state aid. Note also the higher taxes as a percent of personal income, up to 8.5 percent for the likes of Trenton and Buffalo, compared to 3.8 percent for such younger cities as Jacksonville and Indianapolis. Moreover, as cities reach maturity in the aging process, growth in state and federal aid does not keep up with cost growth rates. Therefore, the local tax base is often raised at a rapidly increasing rate to meet rising costs.

One problem in analyzing city financial status is the lack of generally accepted financial performance standards.

In the private sector, there are accepted financial ratios and levels for debt, liquidity, and the like. Such standards are generally set as the normal performance for each industry. A given company can easily be measured against these norms to determine its relative strength. No such measures, however, have been established for the public sector.

Therefore, the research team compiled both the average values and the highest values for the financial variables shown in the chart on page 16. These upper values provided a benchmark against which each city could be evaluated. Of course, these upper values are not static. Such factors as public attitudes and national economic conditions continually change.

By analyzing the information on the chart, along with numerous other tests, researchers were able to link financial performance to changes in non-financial (social, eco-

THE FOUR VARIABLES

FINANCIAL VARIABLES	Low value	High value
Revenue:		
Local tax effort	3.83%	8.55%
Local taxes per capita	$181.41	$360.00
Percent of intergovernmental revenue	30.00%	43.00%
Debt:		
Total debt per capita	$341.02	$690.38
Interest per capita	$15.10	$33.88
Municipal capital spending per capita five-year average, 1971-75	$40.88	$120.09
Expense:		
Fire expenses per capita	$17.17	$46.50
Education expenses per capita	$196.79	$281.73
Health expenses per capita	$3.57	$15.82
Welfare expenses per capita	$60.00	$24.58
City full-time-equivalent employment/total city employment	2.27%	6.96%
Average city wages	$6,694.00	$9,292.00
Net operating expenses per capita	$416.89	$618.21

ECONOMIC VARIABLES:

Change in population
Percent change in single family housing starts
Manufacturing capital spending
Change in manufacturing employment ratio
Percent change in manufacturing capital spending
Median family income

SOCIAL VARIABLES:

Percent minority population
Percent families below low income level
Unemployment rate
Percent pre-1939 housing stock

STRUCTURAL VARIABLE:

Population density

nomic, and structural) conditions. Thus, they explored a variety of questions. For example, what happens to taxes, debt, and expenses under different non-financial conditions? What financial patterns exist?

The Conclusions

Is fiscal stress widespread? Our data for 1975 indicates not. Few of the 66 cities reached any of the 13 upper financial values. No city reached more than four. Few were generally above their cluster averages. Thus, even while debt load in one city might be high, its tax level might be low, leaving room for policy change and creative management. Since so few cities had approached even a small number of higher variables, it appears that even the cities that were most pressed still had leeway before a stress situation occurred. In short, from a purely financial perspective, cities in 1975 appear to have been better off than many people might have believed.

We emphasize that our data is over three years old. Since 1975, financial pressures on many cities have grown. Taxpayer revolt, the slowing growth rate of federal aid, the elimination of some state and federal programs, plus many other factors, have combined to create new fiscal problems for cities.

The important point, however, is not the standing of any individual city. Rather, it is the *variation* in spending patterns among cities. Clearly, cities do not respond uniformly to the industrial aging process. Apparently, therefore, city policy makers can choose from many more financial options than might have been supposed.

Do poor social, economic, and structural conditions cause fiscal stress? Surprisingly, no. Contrary to what might be expected, cities with comparatively poor social, economic and structural conditions showed varying degrees of financial strength. Those cities with poorer non-financial conditions tended to have high per capita taxes, debt, and expenditure ratios. However, there were notable exceptions, such as Pittsburgh and Trenton, where these financial ratios were substantially better. The exceptions indicate that poor conditions impact but do not, by themselves, cause fiscal stress.

Is fiscal stress an inevitable result of the aging process? No, nor does economic growth ensure fiscal strength. It is commonly assumed that the older cities now suffering growing social, economic, and structural problems must necessarily be financially stressed. This is true in many cases, but some cities clearly "buck the trend." How have they done so? Basically, while most cities tend to expand services as the city ages economically, these other cities have held the growth of service expenditures in check.

At the other end of the spectrum, the chart shows that good social, economic, and structural conditions—characteristics of younger cities—do not always go hand in hand with good financial conditions. Indeed, some cities with good non-financial characteristics, such as Denver, rank towards the stressed end of the financial scale.

Is federal/state aid directed at economic and financial problems? Not necessarily. Government assistance tends to favor cities with poor social and structural characteristics. As a result, some cities with these poor characteristics receive somewhat more state and federal aid, even though they may be economically and financially better off than other cities receiving less aid. This social/structural bias has held even for those programs designed to relieve fiscal stress, such as the Anti-Recessionary Fiscal Assistance Program which expired in 1978. Some cities receiving substantial sums under this program—e.g., New Orleans and Jacksonville—were financially better off than other cities of similar size receiving little, if any, funding.

The Implications

What do these findings mean? Can a given city's condition be directly measured? Are there clear answers to relieving our cities' "financial" problems? Surely, no. The problems are too complex. However, the analysis does suggest that the finances of our cities can be better understood. Also, the study does provide a foundation for a number of important initiatives that could be undertaken in both the public and private sectors.

Federal and State Actions.
State and federal aid to cities has often been allocated on the basis of economic, social and structural variables, even when the express purpose of the aid has been to alleviate fiscal stress rather than to remedy economic, social, or structural ills. However, this study shows that fiscal stress does not always accompany such ills. Therefore, the use of these non-financial measures as surrogates to indicate financial condition could result in classifying some cities as stressed when, in fact, they are not. Therefore:

State and federal agencies must define the purposes of each program and then develop funding criteria appropriate, including financial measures.

SIXTEEN CASES OF ECONOMIC BASIC CHARACTERISTICS LINKING MUNICIPAL FINANCIAL PERFORMANCE THE STATISTICAL MEANS AND ANALYTICAL RATIOS

	SMALL DEPENDENT POPULATION				LARGE DEPENDENT POPULATION		
	High private investment and income	Above-average private investment and income	Average private investment and income	Below-average private investment and income	High private investment and income	Above-average private investment and income	Average private investment and income
Revenue:							
Local tax effort	5.11%	5.65%	5.45%	4.48%	3.83%	5.40%	6.13%
Local taxes per capita	$261.43	$311.74	$264.35	$206.67	$181.41	$277.11	$266.70
Percent of intergovernmental revenue	30.20%	32.20%	31.10%	33.30%	43.00%	35.20%	37.40%
Debt:							
Total debt per capita	$690.38	$520.60	$491.32	$434.73	$475.70	$371.50	$478.90
Interest per capita	$32.25	$29.42	$17.79	$20.03	$22.30	$18.34	$21.94
Municipal capital spending per capita five-year average, 1971-75	$67.57	$99.09	$74.97	$71.23	$68.44	$53.16	$97.53
Expense:							
Fire expenses per capita	$19.40	$30.79	$28.51	$25.36	$20.04	$24.58	$34.65
Education expenses per capita	$254.22	$281.73	$231.53	$208.73	$196.79	$251.22	$216.60
Health expenses per capita	$8.45	$8.63	$7.30	$3.85	$14.47	$6.41	$8.01
Welfare expenses per capita	$5.40	$4.12	$1.77	-	$10.60	$.79	$5.15
City full-time-equivalent employment/total city employment	2.50%	3.75%	3.50%	3.07%	2.56%	2.27%	5.30%
Average city wages	$7,904.00	$9,103.00	$7,059.00	$7,658.00	$8,335.00	$8,492.00	$7,724.00
Net operating expenses per capita	$466.74	$515.10	$470.70	$445.56	$419.29	$466.88	$482.93
Mean population (thousands)	230.12	221.24	151.11	285.60	636.71	323.31	290.86
Ratio current expenses to taxes	178.50	154.60	164.80	215.60	231.10	168.50	194.20
Ratio total debt to taxes	260.05	159.02	174.15	210.34	262.22	134.06	179.56
Ratio interest to debt	4.70	5.80	3.60	4.60	4.70	4.90	4.60
Ratio capital to current expenses	0.72	1.02	0.81	0.80	0.82	0.57	0.94
Number of cities in cluster	7	6	13	5	2	6	13
Aging Process Code	Baton Rouge +	Daly City +	Amarillo +	Albuquerque +	Indianapolis +	Decatur +	Baltimore −
(−) Mature cities: manufacturing employment declined in two consecutive periods (1954-67 and 1967-72), the rate of decline accelerated in the second period, and population declined in two periods (1950-60 and 1960-70). (9 cities)	Bloomington +	Fort Worth +	Cambridge −	Austin +	Jacksonville +	Evanston +	Boston −
	Denver +	Madison +	Duluth 0	Long Beach +		Grand Rapids +	Bridgeport −
	Hollywood +	Rochester +	Eugene +	Salt Lake City +		Kansas City +	Dayton 0
	Irving +	Seattle 0	Greensboro +	Tucson +		Milwaukee 0	Louisville 0
	Phoenix +	Stamford +	Lincoln +			Omaha +	Mobile 0
	Tempe +		Little Rock +				Montgomery +
(0) Growing cities: manufacturing employment declined in the first and second periods or second period alone, and population declined from 1960-70. (No acceleration in the rate of decline in manufacturing employment.) (13 cities)			Minneapolis 0				Pasadena 0
			San Angelo +				Pittsburgh 0
			Topeka +				Port Arthur +
			West Palm Beach +				Pueblo +
			Wichita +				Springfield 0
(+) Young cities: both manufacturing employment and population expanded in all applicable periods. (44 cities)			Worcester −				Syracuse 0

Thus, in both the short and long term, federal and state programs aimed at fiscal stress should concentrate on the factors shown to contribute most heavily to financial problems, namely such poor economic conditions as declining private investment and a shrinking job base.

State and federal aid designed to combat fiscal stress in both the short and long term should be directed at improving the economic base of cities, notably through support of private sector job creation.

State and federal agencies need to maximize the effectiveness of whatever aid they target to relieve *current* fiscal stress—while, for the long term, relieving such stress among younger cities can be still another objective. Of course, such aid must support—not dictate—local plans and objectives. But obviously such aid should foster improved planning and economic growth/stabilization, so that younger cities can avert the painful retrenchment that many older cities must now face.

	HIGH POPULATION DENSITY				LOW POPULATION DENSITY				
Below-average private investment and income	**High private investment and income**	**Above-average private investment and income**	**Average private investment and income**	**Below-average private investment and income**	**High private investment and income**	**Above-average private investment and income**	**Average private investment and income**	**Below-average private investment and income**	**Sixty-six cities mean**
6.43%	5.60%	5.58%	7.18%	8.55%	4.44%	5.46%	4.77%	4.97%	5.65%
$273.49	$283.44	$298.86	$327.95	$360.00	$223.76	$289.99	$220.22	$218.73	$265.02
37.50%	38.30%	37.60%	39.80%	37.60%	30.40%	29.90%	30.10%	35.90%	34.60%
$585.83	$430.78	$341.02	$515.95	$661.59	$748.55	$551.07	$462.48	$504.01	$516.86
$25.56	$22.36	$15.10	$24.22	$27.24	$33.88	$32.65	$16.67	$22.91	$23.19
$95.59	$73.43	$49.88	$111.57	$120.09	$64.93	$102.37	$67.68	$78.14	$82.73
$35.30	$24.29	$26.89	$38.34	$46.50	$17.17	$28.56	$26.62	$27.75	$29.55
$242.71	$249.22	$266.35	$240.03	$251.23	$237.58	$266.60	$212.36	$227.53	$236.94
$7.31	$15.82	$7.67	$10.44	$14.33	$6.77	$7.37	$5.63	$3.57	$7.56
$13.29	$12.52	$.60	$5.66	$24.58	$3.57	$4.32	$1.84	$4.80	$5.52
5.28%	2.73%	2.53%	5.93%	6.96%	2.40%	3.48%	3.28%	3.90%	3.98%
$7,375.00	$7,587.00	$9,292.00	$8,342.00	$8,546.00	$8,206.00	$8,303.00	$6,694.00	$7,057.00	$7,746.00
$531.25	$483.72	$486.93	$551.66	$618.21	$442.43	$495.04	$416.89	$469.79	$484.61
240.55	386.39	323.34	348.87	244.35	287.61	221.21	127.20	245.63	250.88
181.10	170.70	162.90	163.10	171.70	198.30	161.00	189.70	214.70	182.90
214.20	151.98	114.11	157.32	183.78	286.74	184.46	210.48	230.42	201.90
4.30	5.20	3.90	4.70	4.10	5.30	6.20	3.60	4.50	4.50
0.90	0.76	0.51	1.04	0.97	0.73	1.11	0.64	0.83	0.85
14	3	6	11	5	6	6	15	14	66
Atlanta +	Denver +	Daly City –	Baltimore –	Buffalo –	Baton Rouge +	Decatur +	Amarillo +	Albuquerque +	
Buffalo –	Phoenix +	Evanston –	Boston –	Hartford –	Bloomington +	Fort Worth +	Duluth 0	Atlanta +	
Fresno +	Tempe –	Grand Rapids –	Bridgeport –	Long Beach +	Hollywood +	Kansas City +	Eugene +	Austin +	
Galveston +		Milwaukee 0	Cambridge –	New Haven –	Indianapolis +	Madison +	Greensboro +	Fresno +	
Hartford –		Omaha –	Dayton 0	Trenton –	Irving +	Rochester +	Lincoln +	Galveston +	
Jackson +		Seattle 0	Louisville 0		Jacksonville +	Stamford +	Little Rock +	Jackson +	
New Haven –			Minneapolis 0				Mobile 0	New Orleans 0	
New Orleans 0			Pasadena 0				Montgomery +	Richmond +	
Richmond +			Pittsburgh 0				Port Arthur +	St. Petersburg +	
St. Petersburg +			Springfield 0				Pueblo +	Salt Lake City +	
Savannah –			Syracuse 0				San Angelo +	Savannah +	
Spokane 0							Topeka +	Spokane 0	
Tampa +							West Palm Beach +	Tampa +	
Trenton –							Wichita +	Tucson +	
							Worcester –		

Obviously, state and federal aid programs must not encourage inefficiency. Aid should be targetted to clearly defined objectives, and may be accompanied by performance requirements and management incentives. These are important to ensure that federal and state grants contribute to solving, not compounding city problems.

Municipal Actions

The study shows that cities respond to the pressures of economic aging in widely differing ways. Some cities even maintain financial equilibrium in the face of serious economic, social, and structural problems. Thus, the study highlights the importance of management and political decision in avoiding fiscal stress.

However, some important management requirements are in order if decision-making is to be effective:

City officials must gain a better understanding of their city's current and future needs/resources. This requires a vastly improved data base.

Cities should use their resources to encourage developing an economic

resource base for the long term.

The study shows that older cities appear less able to use their capital investment to maintain a proportionate level of private investment, which is essential in supporting the city's economic base. Clearly, there are difficult trade-offs between immediate services versus long-term job opportunities and tax base growth. This, however, is a matter of establishing priorities that only local citizens and officials can determine.

Cities must also strive to improve their structural conditions.

Those cities in the study that were able to increase their geographical boundaries or revenue base, through such measures as annexation and tax base sharing, have prolonged the period of fiscal stability and been better able to moderate debt and taxes. Existing legal and regulatory barriers to such measures should be reviewed for their impact.

Citizens and public officials must be willing to adjust spending to match available resources.

Some relief for fiscal problems can come through improved efficiency and productivity of operations, as many cities are now demonstrating. Beyond that, however, cities may face painful budget decisions.

Public and Private Sector Actions

Accurate, comprehensive information is needed by (1) city officials to manage their operations, (2) federal and state officials to develop programs and allocate funds, and (3) investors to make wise decisions. Yet municipal financial data is inadequate to support any of these needs in most cities. The enormity of the data problem is demonstrated by the fact that fully one-half the cities originally to be studied had to be excluded because too much data was missing. And while data for the 66 cities that were included provided a sound basis for the analysis, some key items, such as pension fund liabilities, were lacking for even these cities. Other major problems included inconsistency of data and lack of detail. To remedy this:

> "Population declines in many large cities are part of a long-range decentralization process that is improving the housing, work places, and neighborhood environments of millions of Americans. . . . Therefore, public policy should not aim at stopping or reversing this process."
>
> Anthony Downs, Brookings Institute

Uniform standards of municipal accounting and reporting must be developed and adopted nationally.

Upgrading municipal accounting and reporting systems will surely be time-consuming and costly at the outset. However, the potential benefits outweigh these considerations in the long run. Such benefits include improved management of cities, increased investor confidence, more accurate bond ratings, more equitable and productive distribution of state and federal aid, and greater citizen awareness.

Additional research should be undertaken, targetted to improving city financial management.

The purposes of such research could include: (1) discovering cause and effect links between public and private capital spending, which could enable cities to allocate their funds in ways that would attract more private investment; (2) identifying actions that can help cities avert major financial problems during local or national economic downturns; and (3) pinpointing problems unique to small cities and, hopefully, identifying the solutions.

Summation

First, industrial aging is a major factor in municipal fiscal performance. Moreover, the process is inevitable. Yet it appears that fiscal stress can be avoided, even by those cities facing adverse social, economic, and structural conditions. What is required is a willingness by the community to forego lower priority services—however desirable—in order to balance resources and expenditures. Nevertheless, the outcome is clearly a function of choice, not predetermination.

Second, the political and management decision-making processes have central roles in realizing the potential for older cities to renew their economic base. Is there a cause and effect relationship between private investment on the one hand and economic, social, structural, and financial conditions on the other? Further research will be necessary to learn the answers. However, if such links are established, it will still be up to local citizens and public officials to determine how to balance current needs and the long term necessity to encourage investment. It comes down to choice, and to whether or not the political reality in each community will change to emphasize long-term results.

We believe that it must. △