

FEDERAL GOVERNMENT SHUTDOWN: IMPACTS ON WISCONSIN

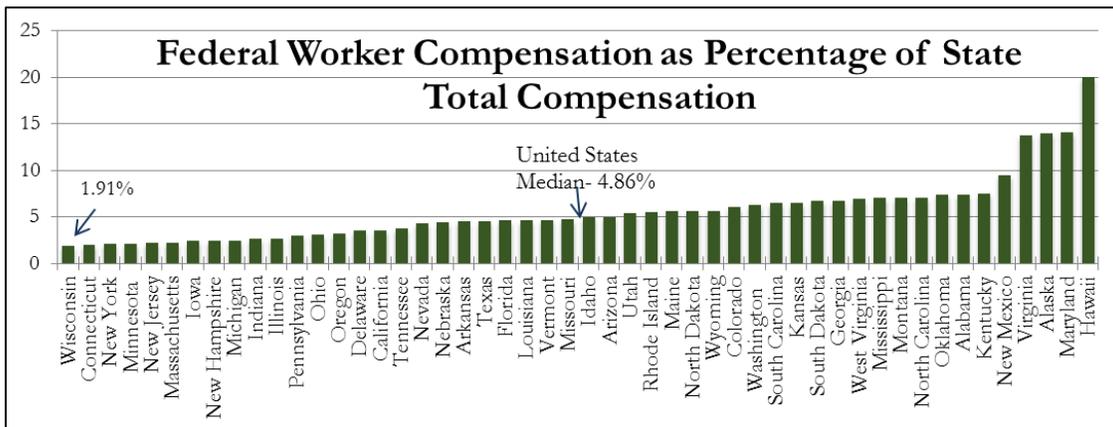
By Bradley Lichtfuss, CBEA Research Analyst

It has been two years since the 2013 government shutdown, and although it appears as if the government has avoided another at the start of this fiscal year, the possibility of the same events unfolding has brought this issue to the forefront of our nation's conscious. The economic impact of the shutdown has been examined at the national level to a great extent, but this essay intends to briefly examine how Wisconsin was impacted by the shutdown and what future shutdowns could mean for the economic welfare of the state. What was found is that Wisconsin is uniquely positioned to weather a shutdown well, but also to have the overall health of its economy damaged if the Federal Government were to close up shop again in the future.

The government shutdown that

occurred in 2013 was the second longest since 1980, at 16 days, and has been considered the most significant on record when looking at the number of days federal employees were furloughed. The Office of Management and Budget provided an extensive report detailing the economic, budgetary, and programmatic costs of the shutdown. The report estimated that 4th quarter Gross Domestic Product was .2-6 percentage points lower than expected due to the shutdown and that 120,000 private sector jobs were not created in the first two weeks of October.¹ Wisconsin shared in this burden along with the rest of the nation, but to a lesser degree than other states. This is due to the fact that Wisconsin has the lowest percentage of federal worker compensation as a percentage of total

Figure 1



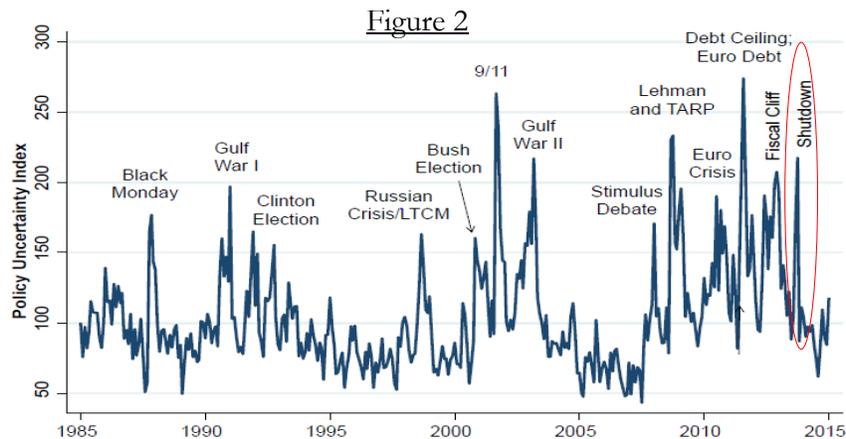
compensation in the state at 1.91%; the least of all 50 states and well below the national average of 4.86% as displayed in Figure 1.

This data was found utilizing the Bureau of Economic Analysis' records on employee compensation by industry by state, and by taking the sum of the total income of civilian employees at the federal level and the military and dividing it by the total compensation of all employees in the state. Wisconsin is thus relatively insulated from the direct impacts of a government shutdown, but they are also fairly vulnerable when examining more far reaching potential impacts of a shutdown.

The Office of Management and Budget's estimates on the negative economic impact of the government shutdown did not incorporate or capture, "any of the additional costs imposed through the impact of the shutdown on consumer and business confidence".² This is an important omission due to the fact that approximately two-thirds of our nation's GDP comes from consumption expenditures. This problem is highlighted by the results from a relatively new measure of consumer and business confidence called the economic policy uncertainty (EPU) index developed by Baker, Bloom, and Davis. This measure is comprised of four sub-indices which are: News-Based Policy

Uncertainty Index (.5), Tax Expirations Index (.167), CPI Forecast Disagreement Measure (.167), and the Federal/State/Local purchases disagreement measure (1.67).³ The largest portion of the index, the News-Based Policy Uncertainty component, examined 10 nationally known newspapers for the combination of the words economic (economy), uncertain (uncertainty), and policy (based on several key words) to create a measure of uncertainty based on governmental action and events in the United States. As figure 2 (below) displays, the 2013 government shutdown ranked in the top five events in terms of the level of uncertainty in the last three decades in the United States.

This level of uncertainty has been shown to foreshadow increases in stock volatility and also a decline in investment, output, and employment at the national level.⁴ In addition to this, research by members of the Federal Reserve Bank of St. Louis have shown that, "there is a significant relationship between sentiment measures and retail sales growth in several states" and that there is an average correlation of .43 between personal consumption expenditures and both major sentiment indices (University of Michigan's Index on



Consumer Sentiment and the Conference Board's Consumer Confidence Index).⁵ As to be expected, there is also a strong inverse relationship between the University of Michigan's Index on Consumer Sentiment and the Economic Policy Uncertainty Index discussed above as displayed in Figure 3.⁶ The paper qualifies its results by stating that consumer sentiment has limited

predictive power to forecast future consumption alone, but if we acknowledge its contributions combined with that of other variables that share in explaining the rise and fall of personal consumption expenditures in individual states it becomes a useful tool to obtain a snapshot of the current state of the economy. This is significant for the

Figure 3

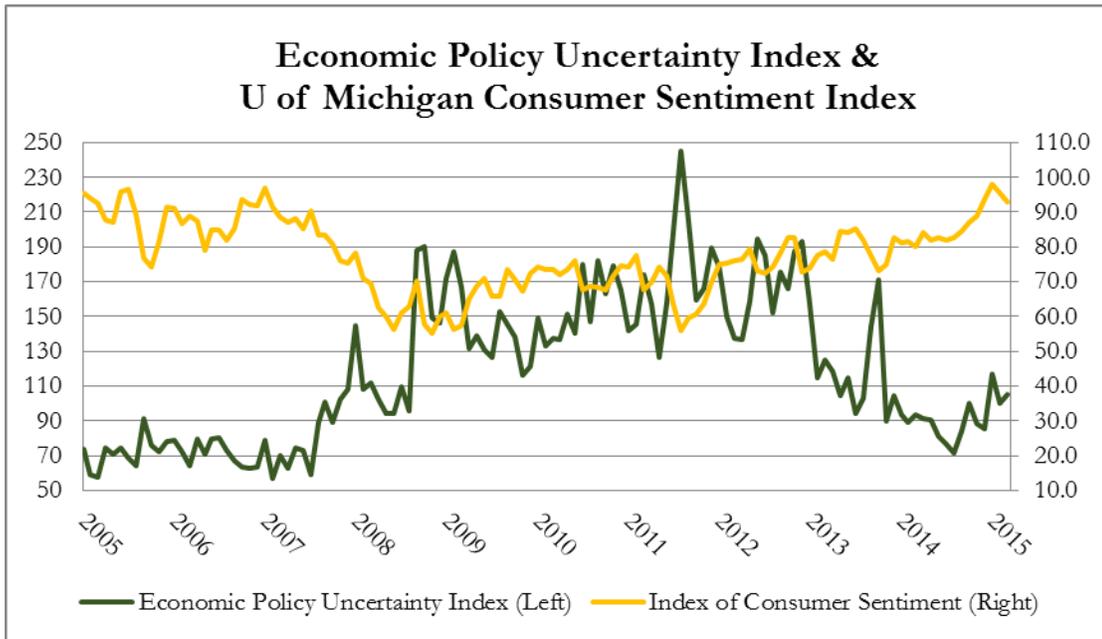
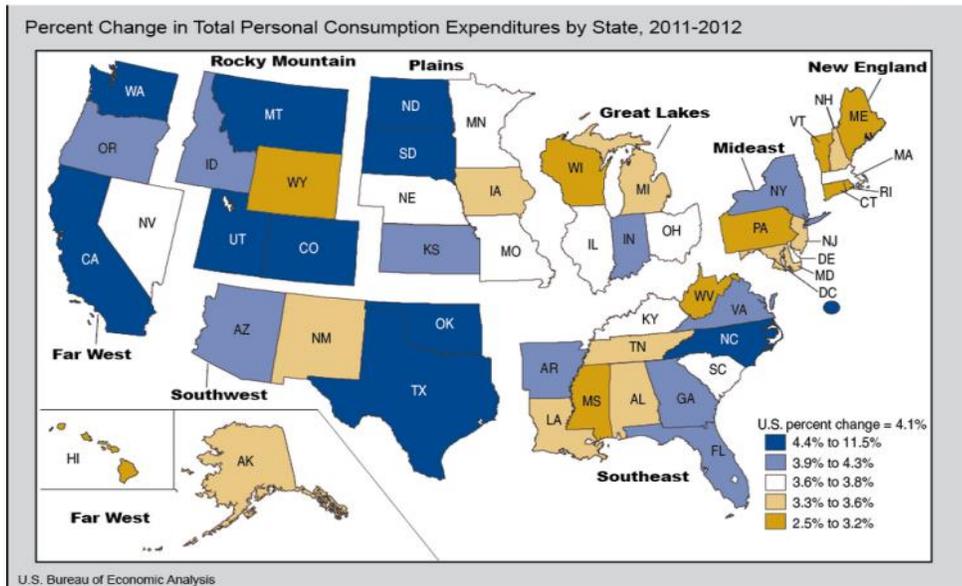


Figure 4



state of Wisconsin because of its already slow rate of growth in Personal Consumption Expenditures (PCE). Wisconsin was one of the ten slowest states to grow in this area from 2011-12 having a rate of 2.5-3.2% growth, as shown in figure 4.⁷ This slow recovery displays a reluctance to spend, which is only made worse when consumer and business confidence is down, which government shutdowns have a great capacity to induce. Wisconsin needs businesses to expand and for new endeavors to be attempted within the state to experience a full economic recovery which is not likely to occur when PCE growth rates are slow and when the possibility of government shutdowns compound the problem.

In summary, the overall economic impact of the 2013 government

shutdown was the largest over the past three decades of our nation and it is difficult to assess the overall cost of the event to our nation. Wisconsin has been shown to be both simultaneously insulated from the direct effects and vulnerable to the ramifications of another government shutdown indirectly via uncertainty and consumption. Governmental actions and events have been shown to play a significant role in determining our level of economic wellbeing over the years, and hopefully those in Washington consider the full weight of the costs a government shutdown can have on the national economy, as well as Wisconsin's economy before heading down that path again.

^{1,2} "Impact and Costs of the October 2013 Federal Government Shutdown." (November 2013) Office of Management and Budget..

^{3,4} Baker, Scott, Nicholas Bloom, and Steven Davis. "Measuring Economic Policy Uncertainty." Economic Policy Uncertainty. 2013. http://www.policyuncertainty.com/us_monthly.html

⁵ Garrett, T., Hernandez-Murillo, R., and Owyang, M. (September 2004) "Does Consumer Sentiment Predict Regional Consumption?" *Federal Reserve Bank of St. Louis*. <https://www.google.com/webhp?sourceid=chrome-instant&ion=1&espv=2&ie=UTF-8#>

⁶ Economic Policy Uncertainty data and University of Michigan's Index on Consumer Sentiment- contact CBEA for more source information.

⁷ "Personal Consumption Expenditures by State, 1997-2012." (August 2014) Bureau of Economic Analysis- Press Release. http://www.bea.gov/newsreleases/regional/pce/pce_newsrelease.htm.

Bradley Lichtfuss '16 is a research analyst with the Center for Business and Economic Analysis. His most recent project examined the impact of financial incentives on future educators' willingness to teach in a high-need urban environment (Called to Serve: A Choice to Teach in a High-Need School). Bradley is a senior pursuing a double major in economics and political science.

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