Rhode Island Policy Reporter

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Where has the money gone?

BECAUSE a fair amount of my time is spent detailing misconceptions about government spending, I hear this question fairly often: "Where has the money gone?" This frequently happens after people have been informed that welfare spending consitutes around 1/2 of 1% of the state's general revenue budget, or that Medicaid for the poor constitutes only around 7%. If these items that they've heard so much about aren't really the problem with government spending, then what is?

This past winter, a friend called my attention to a fascinating set of numbers compiled by a professor at URI (see Figure 1 below). The chart showed the growth of the state budget since 1950. My friend ran across the numbers on the "Ocean State Republican" web site, where sneering comments ran like this:

> What this data shows us is that in real terms the Democrat General Assembly has increased the State budget over NINE-FOLD since 1950! Recall that the overall population of the state hasn't changed all that much over the same exact period…Recall too that in the 1950s we already had all of the essential government services—roads, bridges, schools, water, police and fire protection—so this nine-fold increase is not attributable to "essential government services." [1]

This, of course, is deeply uninformed. But let's count the ways, because they tell a good story. To begin with, inflation. The writer used the CPI (Consumer Price Index) to correct for inflation. The CPI measures some services, like college tuitions and haircuts, but mostly it's a measure of the price of goods a household buys. Households don't buy asphalt for roads, or classroom desks or judicial pensions, so already we're wondering whether this is the right index. Maybe we should use the Employment Cost Index or the Producer Price Index instead? These are all indexes of inflation, but they are all different, because inflation isn't a simple thing.

But maybe, since the whole point of the original post was to compare the cost of government to our ability to pay for it, we should look at the state's personal income. Personal income measures the size of the state's economy by how much money we all earn. In Figure 2, I've scaled the personal income data down and overlaid it on the general revenue spending and they track very well.

But this isn't the end of the story. You can see that in 1950, the spending line is a tiny bit below the personal income data, a difference that has disappeared by 2005. This shows that general revenue has, in fact grown faster than the state's economy. Figure 3 (next page) shows the ratio of general revenue and personal income, which makes the change much clearer. In 1950, the government spent a tiny bit more than 3% of total personal income, while these days it's more like 7.5%.

In the web site's presentation of these numbers, they point out that in 1966, public employee unions were recognized, and in 1971 the income tax was established, and blame the acceleration on that. But that's not what this graph shows. What you see there might say that the cost rise accelerated in 1966 but whatever was going on began by 1950, or before. Public employee unions weren't around until long after this trend began. There are new state departments since then, but most of those are small ones.

[1] *http://oceanstaterepublican.com/2008/03/27/rhode-island-citizens-one-million-boiling-frogs/*

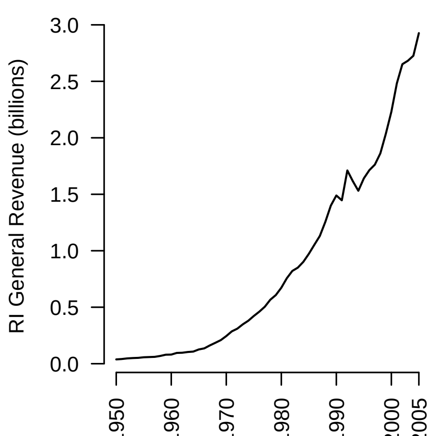

Figure 1: Growth of RI general revenue spending. This is dramatic growth, but it's not the only thing that's grown like this. (Source: state budget documents, many thanks to Pat Logan at URI.)

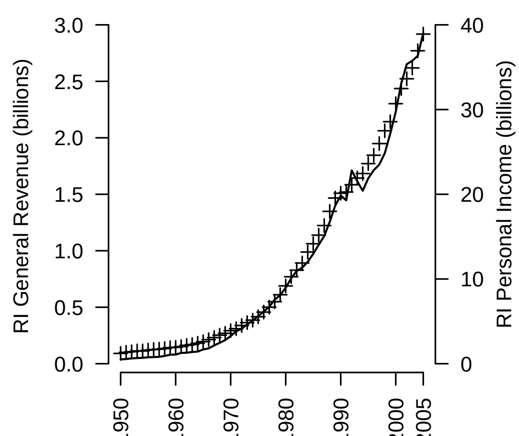

Figure 2: The same graph with estimates of total state personal income plotted on top. The personal income scale is to the right. (Income estimates from Bureau of Economic Analysis.)

So what happened? Well, how about the biggest demographic shift in our nation's history?

Fish don't notice the water Like those clueless fish, most of us don't recognize that the world we've built around us is a very expensive one to run. Our state is filled with people ready to tell you about the positive impact of consolidating school districts and even towns. They attend school committee meetings all over the state, chanting "economies of scale" and "consolidation" and similar mantras. In my experience, though, most remain utterly oblivious to the the best way to get economies of scale: live in a city.

The truth is that moving everyone to the suburbs was a very expensive thing to do, and has cost us billions of dollars in infrastructure and operating costs, but these are costs that no one ever tots up for examination.

Here's an example: The Providence Water Supply Board provides water not only to its retail customers, who are clustered in the urban centers of Providence, Cranston and Johnston, but also to satellite water systems, which tend to be less urban, like Kent County, Warwick, Smithfield and Bristol County. In 1958, the PWSB delivered 35.7 million gallons of Scituate water each day to its retail customers.[2] In 2007, the retail customers only needed 40.3 million gallons. But the suburban systems' demand went from 4.7 million gallons in 1958 to 9 million in 1969 to 30.3 million today. All that new demand came with new miles of pipe to service, new employees to manage and new facilities to maintain. The growth was where their pipes weren't.

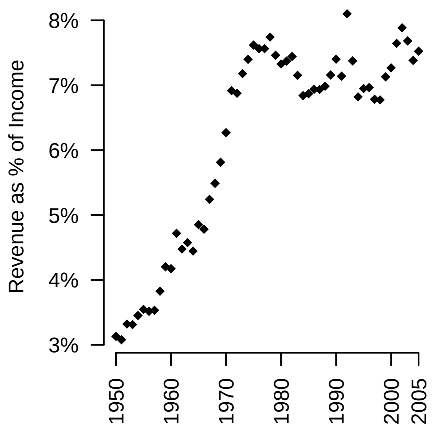

Figure 3: General revenue expressed as a percentage of personal income. You can see from this that we are currently spending a little more than twice what we spent in 1950. But you can also see that whatever it was that pushed us from that low level to where we are now was already underway by 1950.

And it's not just that we've had to build new infrastructure. It's usually more expensive, too. In West Warwick, there is a sewer system, built more than a hundred years ago. It currently has a capacity of 10.5 million gallons per day, and usually operates at a bit more than half that. It uses 100 miles of sewer pipes, most of which are gravity-fed, so needs only four pumps to serve 32,000 residential customers who produce about half the sewage, and a few big industrial users like Amgen who provide the other half. Running the system costs about $9 million each year.

Most public services are more expensive to provide in the suburbs.

In 1913, when West Warwick and Warwick parted, they were two very different places. West Warwick was urban and industrial and the other rural and agrarian. Fifty years later, though, Warwick was fast losing its rural character, and in 1962, it began construction of a new sewer system. Today, the system serves around 60,000 people with 250 miles of pipe. Its total capacity is 7.7 million gallons per day, and it usually runs at around 4.5 million. Warwick is pretty flat, though, so the system has 45 pumps to move its sewage down the pipes, and it costs about $17 million each year to run it.

So look: Warwick has a system that costs twice as much money per residential customer to run. The reasons aren't hard to see: they have 2.5 times as much pipe and ten times as many pumps. All told, they have to spend about twice as much money each year to process *less* sewage. Meanwhile, there is enough unused capacity in the West Warwick system to service almost all the sewage Warwick produces. To put it a different way: the luxury of occupying Warwick—with its expansive 2-acre house lots and other signs of low density—costs $17 million a year in sewage processing.

The same is true of virtually any other service you can name, including gas lines, electric lines, cable TV and telephones. The cost per customer of these services in the compact urban cores is much less than the cost of providing them to customers hundreds of yards from each other. The cost of these services is borne by the ratepayers, but they have an impact on other taxes, too, not merely because governments are typically the largest ratepayers for

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[2] 1958 data from state Water Resources Board, current data from the Providence Water Supply Board, and 1969 data from a history of the Water Supply Board written in 1969 by Wayland Ingram, an engineer who worked there.

water and sewer services. We have state offices whose job it is to inspect and set standards for the water and sewer systems, and only a few of the larger systems are effectively divorced from the management of the towns they serve. On the contrary, most share offices, vehicles, employees and bond ratings with their town governments.

Turning more directly to tax-supported expenses, how about miles of road? I found a delightful 1958 report in the state library called "Rhode Island Roads." In it, I learned that in 1958, we maintained 4,069 miles of streets and roads. By 1995, we were up to 5,893 miles, and by 2006, the mileage was at 6,528.[3] The construction of the interstate highway system in the 1960's and 1970's obviously added miles to that sum. Because those are expensive roads to maintain and police, they added an outsize share of expense, but tremendous growth in smaller state highways and local roads are expensive, too. In 1958, we had 3,020 miles of local roads while in 2006, FHWA statistics show 5,538 miles. According to DOT a two-lane road costs upward of $400,000 per mile to resurface.

Other expenses? According to FBI crime reports, our state has approximately 300 more police employees (officers and civilians) now than ten years ago. But these new police are concentrated in the low-crime towns that can afford them, not the high-crime places that may need them. (See **RIPR** issue 28.) Firefighters? Providence has roughly the same number today as fifty years ago, with a third fewer people to support them, but no fewer houses to burn. Meanwhile, new fire stations have sprung up in the suburbs like dandelions on their lawns.

Schools? The story there is more complicated, and the effect of a decamping population is masked by the baby boom, changing demographics, curricula and educational norms. Despite some significant dips in the '70s and '80s, over the long term, school populations have not declined significantly in the cities, even as the overall population has. Providence, for example, now educates 24,000 children, down from around 26,000 in the 1950's. Other cities show the same: Pawtucket 8781 (9000 in 1955); Woonsocket 6250 (4200); Central Falls 3350 (1600). In the suburbs, the story is different: Portsmouth 2900 (1100); North Kingstown 4500 (2200); East Greenwich 2400 (950), Narragansett 1470 (490).

We've invested hundreds of millions of dollars in new schools since 1950. Quite a lot of that would have happened anyway, as old school buildings were improved and replaced. But the question of schools provides a fulcrum around which to turn this article from a discussion of why suburbs are more expensive to run than cities to a discussion of why, despite that, taxes are lower there.

[3]The modern data is from Federal Highway Administration reports. In the late 1980's, as GIS systems became widely used, the method of counting road miles changed. The earlier number, derived from compilation of reports from public works departments is likely not as accurate. But the purpose here is to show the scale of growth, not to calibrate it.

	1950		1993
47.5	Narragansett	2823	New Shoreham
24.9	Providence	902	Little Compton
22.8	Pawtucket	800	Jamestown
22.7	Woonsocket	632	Narragansett
21.4	Central Falls	505	East Greenwich
19.5	Newport	480	Barrington
17.8	South Kingstown	419	Westerly
17.7	**RI**	419	Newport
17.2	Little Compton	363	Portsmouth
16.4	Barrington	357	Scituate
16.1	Scituate	329	Smithfield
15.8	Portsmouth	325	North Kingstown
15.7	West Warwick	325	Lincoln
15.4	East Providence	320	South Kingstown
13.9	Jamestown	318	Warwick
13.7	Tiverton	314	Tiverton
13.6	Westerly	304	Johnston
13.5	Cranston	299	Cranston
13.3	Lincoln	297	North Smithfield
12.7	North Providence	280	East Providence
12.4	Charlestown	277	Middletown
11.7	Cumberland	275	Cumberland
11.6	North Kingstown	274	Bristol/Warren
11.6	Warren	273	North Providence
11.3	North Smithfield	260	**RI**
11.1	Middletown	247	Foster
10.8	New Shoreham	225	Exeter/WG
10.7	Foster	206	West Warwick
10.7	Bristol	200	Glocester
10.6	East Greenwich	192	Coventry
10.5	Richmond	176	Pawtucket
10.3	Smithfield	159	Burrillville
10.1	Coventry	135	Providence
9.4	Warwick	122	Woonsocket
8.7	Burrillville	55	Central Falls
8.2	Glocester		
7.9	Exeter		
7.1	Johnston		
6.6	West Greenwich		
5.8	Hopkinton		

Table 1: Thousand dollars of assessed value per student, 1951 vs. 1993. The drop in the rank of the average tells you about the plight of the majority of students. (Source: RI Department of Education. The lists are different lengths because of district consolidations and because property tax data wasn't published for Chariho.)

Expensive services, low taxes Back in the early postwar years, Providence was rich. Not just the East Side, either. There were poor neighborhoods, of course, but there was more than one rich neighborhood, as the decrepit mansions of Elmwood now testify.

A decent measure of a town's ability to pay for its services is the taxable wealth behind each student in the schools. In 1950, only Narragansett, with its seaside mansions and few students, was ahead of Providence in wealth per student in its schools (see Table 1). Rhode Island's other cities were right behind Providence on the list: Pawtucket, Woonsocket and Central Falls were 3,4 and 5, respectively. East Greenwich was at 29, Warwick was 33 and Hopkinton at the very bottom. The school tax rates were pretty much the exact opposite, with Hopkinton's by far the highest in the state, Warwick at number 3, East Greenwich at 11, and the top four cities and Narragansett holding down the bottom end of the list.

But then people started selling houses in the cities and buying them out of town, and property values began to shift. As early as 1959, the picture was changing. Woonsocket, Central Falls and Newport had all slid down the list. Providence and Pawtucket were still at 3 and 4, but East Greenwich had moved up to 7.

Runaway growth in the suburbs masked how costly they are to run.

As the cities absorbed one hit after another to their tax rolls, they weren't losing students in the schools,[4] or houses to protect or streets to keep clean. They were only losing people—older people and prosperous people—and money. Meanwhile, on the other side of the coin, suburbs were gaining people whose new taxes didn't quite pay for the cost of the schools, roads and fire departments they demanded. But that was largely not a problem, because more people were coming next year, and property values were increasing, too.

During the 1960's, suburban growth rates of 4 to 5% per year were not at all uncommon (North Kingstown, Coventry, East Greenwich, among others), and they were even higher in the 1950's. When revenues are growing at more than 5% a year, anyone can balance a budget, and many did so while clucking sanctimoniously at the cities. The places that rose on the list on page 3 could finance their growth with new revenue that came in the mail, while the places that tumbled down the rankings could only moan about their lost revenue (and petition for state aid, which was only grudgingly awarded).

As late as 1977, Providence was still number 6 on this list, but the other cities had slid way down, and Providence was soon to follow. After the 1989 slump in real estate values, the list assumed its modern shape, with the cities in the basement and the rich suburbs elbowing into the company of the beach communities.

The short version of all this is that the flight to the suburbs devastated our urban centers and their ability to support government services. The inexpensive government of the suburbs was only a fiction produced by astonishing growth rates and a certain lag in providing the necessary services. (The need for sewers in Warwick predated their construction by several years.) The flight itself happened in part because of social pressures (race, poverty, desire for that little house on the 2-acre lot in the country), and in part because of consciously-chosen government policies (2-acre zoning, state support for new infrastructure, the interstate highways, "urban renewal," and much more).

So where has the money gone? Most of it went to build what amounts to an entire second state's worth of sewer lines, police stations and roads. Union contracts, care for the poor, and increased government services are obviously part of the story of the cost of government, but the effects described here are not minor details. The expensive choices we've made have been masked by the fiscal effect of the flight to the suburbs, but that masking effect only lasts as long as the growth does. When the growth slows, that's when the piper comes for his due, and taxes rise to pay for the expenses no longer covered by growth.

Since the 1950's, we've build a whole second state's worth of infrastructure.

The point of this observation isn't to mourn what might have been, but to make the correct diagnosis. A malignant tumor in your head may give you a headache, but you're not going to cure it with aspirin (or decapitation). Getting the diagnosis right isn't about exonerating anyone or blaming anyone, but about *fixing our problems*. If you don't get it right, the problems don't get fixed. You spend your time addressing the wrong issues and wonder why things don't get better—not a bad description of what goes on in our statehouse every year. ■

[4] Well, they were losing *some*, but not fast enough to make a difference, and they have gained them all back.

BOOK REVIEW

Reading the Tea Leaves

Bad Money
Kevin Phillips, HarperCollins, 2008, 240 pages

In 1974, the US and Saudi Arabia made a deal: the Saudis agreed to keep pricing their oil in dollars, and the US agreed… well no one's quite sure what we agreed to, but since then, Saudi Arabia has been one of our best customers for advanced weaponry, we have defended them against Saddam Hussein and others and have generally been the best friend a fundamentalist Islamic feudal kingdom could hope for.

Whatever the details, the fact remains that for the past few decades, the most important commodity in the world has been priced in our nation's currency. This has created an extraordinary demand for dollars, making it easy to finance our budget and trade deficits while still keeping our interest rates low and our economy churning. The consequences have been astonishing. Freed from having to worry about the balance of trade, we have recklessly pursued what would have been disastrous consequences in any other country on the planet. We have willingly disassembled what was once the strongest manufacturing sector in the world and constructed in its place the tallest and most precarious pile of financial services any nation has ever dared try.

In any other country, the authors of this insanity might be vilified, but here they are lionized as the captains of the "new economy." Business writers among the camp followers have rushed in to offer justifications. Not for us the "old" economy of smokestacks and the grubby making of mere things; we have progressed to a higher plane. We now deal in clean "post-industrial" commodities like services and the abstractions of derivative investments. Occasionally they will mourn the "displacement" and "structural adjustment" necessary to the shift, but go ahead to assure us that this is nothing more than Schumpeter's "creative destruction" and that all is for the best in this best of all possible worlds. Dr. Pangloss had nothing on George Gilder or Thomas Friedman.

The people who have destroyed our economy are instead celebrated as business heroes.

To his vast credit, Kevin Phillips is having none of this. In his new book *Bad Money*, he not only describes the situation, but points out that over the course of the Bush administration, our nation's reckless financial and military policies have tested the limits of this already indulgent arrangement. Our trade and budget deficits have ballooned beyond most people's imaginations, and we have fairly thoroughly offended the nations whose forbearance we most need. Thus we have nations all over the world actively seeking to undermine the dollar, like OPEC members Venezuela and Iran. Even China, who owes so much

Elevating the trivia

Our press corp's dishonest fascination with inane trivia is one of its most maddening features. Take one example: in May, towards the end of her campaign, Hillary Clinton was pilloried in articles and on television for mentioning that Bobby Kennedy was killed in June. But what did she say? It was a clumsy way to say that yes, campaigns have gone into June before, but that's all she appeared to be saying. And in fact, she said the exact same thing in March when it went without notice. But this time (apparently provoked by emails from the Obama campaign), the press went into convulsions, with reporters tumbling all over each other to denounce this terrible remark. MSNBC's Keith Olbermann even made a special comment—several minutes of valuable air time—about how terrible it was.

This was nothing but one more in a long and aggravating line of fake scandals: little bits of nothing ginned up into something for lazy reporters and pundits to yammer about. Over the last 20 years, we've suffered an endless series of them: from Michael Dukakis and the pledge of allegiance to Whitewater to Al Gore and *Love Story* and more. It's not that this kind of thing isn't understandable. Put yourself in a reporter's shoes: you've just sat through the five hundredth candidate "town hall" meeting where people have asked about Social Security and universal health care. Maybe someone asked a question about water rights. So afterward, dreading the research you'll need to write about that, you have a bright idea—or a canny campaign operative has the bright idea for you—and you ask Hillary about the long campaign because that's something you can write about quickly. Not needing to do any research means you can write your story in time to join that cute CNN producer at the hotel bar's happy hour. And *that's* where so much of our campaign coverage comes from.

This time, the performance was so shameful that two prominent journalists pointed out how silly it was. Richard Cohen, of the Washington Post, wrote that "I hate that Clinton's observation that Robert F. Kennedy was assassinated in June ran on and on when everyone save some indigenous people in the Brazilian rain forest knew what she meant." Michael Kinsley seconded the point in the New York Times.[a] Essentially what these two members of the press said is that their colleagues were guilty of creating a storm out of nothing. They had become the news instead of reporting it. But they both also showed they could be as dense as Phillips on the point, and neither seemed to understand what a disgrace this kind of behavior constitutes. –TS

[a] These quotations are owed to *dailyhowler.com*, an invaluable source for informed criticism of political coverage.

of its prosperity to our market, is quietly trying to wean itself from dollars.

Even apart from annoying the rest of the world, we may have carried things a shade too far. The ills of the subprime mortgage market did not themselves constitute a global economic crisis. Some Americans—even a few million—defaulting on their mortgages is not necessarily tragic to residents of Mumbai. It's the structure of Wall Street's insurance and reinsurance schemes, and the related chicanery, that turned what might have been a serious but containable problem for our nation into the cataclysm we're watching unfold today. And the hollowing out of our manufacturing economy has had devastating consequences for the middle class, the engine of consumer demand.

Phillips draws fascinating parallels between our circumstances and the declines of Hapsburg Spain, the Dutch Empire and Great Britain between 1900 and 1950. Among other common threads, he points out that in each of these, the lords of finance gained ascendancy over the explorers, engineers, miners and manufacturers who created the wealth that powered these empires. Compare this to our situation, where the financial service sector now contributes more to our GDP than manufacturing. The hedge fund managers control (and have) extraordinary wealth, even compared to the princely CEOs who are chauffeured among us. The top ten American hedge fund managers collectively earned $16.1 billion last year, while the top ten American CEOs earned a measly $436 million.[5] It almost makes you feel sorry for the CEOs.[6]

Phillips paints this picture well, connecting the necessary dots and providing depth enough to make the problems clear, but not so much as to overwhelm. But he doesn't stop there, and moves on to a look at the capacity of our political system to deal with these immense problems. His diagnosis is pretty simple: in our strictly bipolar political system, nothing can happen without at least one party getting behind a solution, and both are deeply invested in the "new economy" claptrap. The leading lights of neither party see the increased financialization of our economy as a problem, though to their credit, there is at least some polite dissension on the Democratic side.

But unfortunately, it's in his analysis of our politics that Phillips doesn't quite close the deal. One reaches the end of this cool little book and reflects that it is indeed possible to write a 240-page book excoriating the state of our politics and not spare a single word for the failings of the press. But with so few reporters willing or able to write about the very subjects at the heart of this book, it hardly seems a minor omission. One might be forgiven for suspecting that Phillips, a widely-published newspaper columnist, is blinded by his own participation.

Can we understand our politics without understanding the press?

The failings of the press are complicated and resist generalization. There is the love of narrative, the lack of reporters willing to take on technical issues (*pace* Phillips himself), the fascination with inane trivia and "character" issues (see box), the willingness to read minds, and much more. It's a complicated story, but to try to understand the defects of our politics without understanding the defects of the press is a fool's errand.

Read this book. Its descriptions of our economy and the real problems that face us are invaluable and dead-on. But realize as you're reading it that most of us learn about these things through the 21st century American press, an imperfect lens if there ever was one. To address the subject and not the lens guarantees that you're not seeing the whole picture. ■

[5]Sources are detailed at *whatcheer.net*. Incidentally, thanks to the efforts of NY Senator Chuck Schumer, the hedge fund managers are taxed at a lower rate, too, but that's a different story.

[6]Almost.

stamp

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