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The Biggest Loser From Full Employment? Government.

Unemployment is low. State and local budgets are tight. Expect shortages of public servants.

There's room to quibble about whether the U.S. has reached "full employment." Yes, the unemployment rate is and has been low. But labor-force participation remains subdued, and some measures of wage growth are stunted.

If the U.S. is not at full employment, it's certainly getting closer. That's worse and worse news for government, as it will struggle to hire and retain workers.

For a variety of reasons, the government employment cycle lags behind the overall cycle. Partly that's because government revenue rises after the private sector heats up, not simultaneously. Income taxes are paid only after companies have hired workers. Before corporate profits can be taxed, they have to be earned. Tax revenue from capital gains can flow into the public coffers many months after assets have been sold.

Tax revenue from ordinary economic activity is volatile as is, but the unusual nature of the nationwide housing downturn in the 2008 recession had a profound impact on local tax streams. The run-up in housing prices during the boom years led to higher appraised values and increased property tax revenue for municipalities to spend. The bust led to lower appraised values and budget deficits that had to be closed, in many cases via spending cuts and layoffs, as the private sector was going through the worst recession in 80 years. While home prices have recovered to varying degrees around the country, appraisals often occur with a multiyear lag, which has constrained local budgets during the economic recovery.

The financial accounting of when tax revenue is earned and can be spent is one thing, but the governing philosophies of politicians during this economic cycle are another. Elected officials who came into office in the aftermath of the great recession were mostly focused on shoring up budgets. In part this was because the electoral wave in 2010 following the recession was dominated by austerity-focused Republicans, but it affected Democrats as well. Big city mayors, who tend to be Democrats, had to balance their budgets, and it's hard to get people to agree to tax hikes to fund services when unemployment is high. Rainy day funds needed to be built up, and in some cases, pension costs needed to be addressed.

Even though that 2010 electoral wave was seven years ago, it continues to be a powerful movement. Eighteen governors currently in office were elected in 2010. Most of them are term-limited in 2018, but until then … it's difficult to get people who came into office promising to cut spending to then turn into stimulus mavens late in their tenures.

In the same way that overhiring during the boom years came back to bite governments, underhiring now is going to increasingly lead to pain when governments are inevitably forced to catch up. Government payrolls didn't hit bottom until January 2014, nearly five years after the technical end of the recession. They are back to their level from December 2007, when the recession began. By comparison, over that same time frame, private sector payrolls have increased by 8 million workers.

While it would be nice to think that government has gotten dramatically more efficient over the past decade, the combination of tight budgets and recession-scarred governing mentalities means that public sector employment is short of where it needs to be to return to pre-recession levels of service. To get North Carolina back to prerecession student-to-teacher ratios, the state would need to hire more than 5,000 teachers.

Funding isn't the only obstacle to a recovery in government services. The labor market is also newly tight. Atlanta Mayor Kasim Reed noted it was much easier hiring police officers when the local unemployment rate was 10.5 percent.

For the country as a whole, to get the ratio of private sector to public sector workers back to its December 2007 level, we would need to hire an additional 1.6 million public sector workers. That won't be quick; to increase government employment by 1.6 million in the 1990s took eight years.

Every month that passes in which government doesn't start to address its hiring shortfall means that more teachers and police officers retire and aren't replaced. It means quality government workers who are desired by the private sector become more tempted to leave their government jobs for higher pay elsewhere in a tight labor market. And it means fewer people bother to apply for government jobs during a period with lingering hiring freezes and compensation packages that haven't caught up with where we are in the economic cycle. If politicians think voters are upset by debt and deficits, wait until we have widespread shortages of police officers and teachers.

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