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The Efficiency of Local Government: The Role of Privatization and Public Sector Unions¹

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Abstract

Local governments spend roughly \$1.6 trillion per year to provide a variety of public services ranging from police and fire protection to public schools and public transit. However, we know little about public sector's productivity in delivering key services. Public bus service represents a standardized output for benchmarking the cost of local government service provision. Among the top twenty largest cities, there exists significant dispersion in the operating cost per bus mile with the highest being more than three times as high as the lowest. Using a regression discontinuity design, we estimate the cost savings from privatization and explore the political economy of why privatization rates are *lower* in high cost unionized areas. Our analysis suggests that fully privatizing all bus transit would generate cost savings of approximately \$5.7 billion, or 30% of total U.S. bus transit operating expenses. The corresponding increased use of public transit from this cost reduction would lead to a gain in social welfare of \$524 million, at minimum, and at least 26,000 additional transit jobs.

Keywords: Government Service, Efficiency, Privatization, Union

JEL classification: D7, H7, J4

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