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Timothy J. Bartik
W.E. Upjohn Institute, bartik@upjohn.org

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POLICY BRIEF

Should We Target Jobs at Distressed Places, and If So, How?

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BRIEF HIGHLIGHTS

- *Even in a booming U.S. economy, some distressed places struggle with job availability, as prime-age employment rates are over 8 percentage points lower than in booming places.*
- *"Moving people to jobs" cannot solve the problem of distressed places: encouraging out-migration leads to a loss of jobs in that place of roughly equal percentage size to the loss of population.*
- *"Moving jobs to people" increases local employment rates by three-fourths more in distressed places than in other places, and these increases persist for decades.*
- *Current "place policies" are dominated by state business tax incentives, but these incentives are often costly per job created, and booming states frequently offer higher incentives than distressed states.*
- *Federal and state "place policies" should target distressed places; focus tax incentives on high-multiplier businesses; and invest in customized small-business advising, public infrastructure, land development, and job skills.*

For additional details, see the working paper at https://research.upjohn.org/workingpapers/308/.

Even when the U.S. economy is booming, some places lack sufficient jobs.

Consider "prime-age" workers, ages 25 to 54. The employment-to-population ratio (employment rate) for such workers varies greatly between booming and distressed places. Ten percent of the U.S. population lives in booming places, where the prime-age employment rate exceeds 83 percent. Another 10 percent, however, lives in distressed places, where the prime-age employment rate falls below 75 percent.

Lower employment in distressed places is associated with poorer mental health, substance abuse, crime, family breakdowns, and local fiscal problems. Children from distressed places end up with lower earnings as adults.

What can policymakers do? One solution is to bring people to jobs, by subsidizing moves to places with growing employment. An alternative solution is to bring jobs to people, by creating more employment opportunities in distressed places. Currently, the typical "place-oriented" policy is a "jobs-to-people" strategy run by state and local governments, which offer tax incentives to businesses that promise to create jobs.

Mounting evidence suggests that "people-to-jobs" strategies have limited potential to solve the problems of distressed places. Although "jobs-to-people" strategies have greater potential, the current regime of tax incentive competition is often wasteful and needs reforms. To summarize:

- Because most individuals have strong ties to home, subsidizing out-migration induces only a small share to move.
- Out-migration reduces both population and jobs in equal proportion. A lower population depresses local demand, housing prices, and construction. Encouraging people to leave a distressed place thus does not make it easier for those staying behind to find jobs.
- On average, one-fifth of new local jobs created by incentives end up going to residents (rather than in-migrants).
- But this share rises to over one-third in distressed places, as new jobs in distressed places are more likely to help the local nonemployed.
- Nonetheless, the current state and local competition to lure businesses does not help distressed places, as booming areas offer tax incentives at least as large as those offered by distressed places.
- Moreover, current incentives favor large corporations, rather than the companies that are more likely to create downstream jobs. Current incentives are excessively long-term, which is ineffective because most businesses are focused on the short-term.
- Effective local job-creation strategies make the inputs businesses need to produce goods and services more readily available, something the private market does not always adequately do. These strategies include offering smaller businesses high-quality advice on new technologies and new markets, upgrading local roads and

Encouraging out-migration from distressed places does not help those left behind, as it reduces jobs in distressed places.

other infrastructure, providing land zoned and prepped for industry, and educating workers for the skills businesses need.

Encouraging Out-Migration from Distressed Places is a Bad Idea

Why focus on places? Shouldn't helping people be our goal? And if people are best helped by moving out of distressed places, shouldn't we encourage that out-migration?

We should focus on places because people care about them. Most people have strong ties to family, friends, and organizations in their hometowns. These ties are valued for their own sake, even if they may also be useful for other goals. If someone suffers a job loss or other crisis, one's social network can often help.

A good job in one's home community therefore can be more valuable than a good job somewhere else. The costs of migration can involve sacrificing some of the value of home and community ties. Additionally, a community with fewer long-term residents can have lower "social capital"—weaker local organizations and civic participation.

Furthermore, encouraging out-migration may not only be a bad goal, it is often ineffective. Even sizable moving subsidies, of $10,000 or more, lead only a tiny fraction of residents to relocate.

As Adam Smith said in *The Wealth of Nations* back in 1776, "A man is of all sorts of luggage the most difficult to be transported."

If a distressed place has too few jobs, relative to population, encouraging out-migration might seem a good strategy to re-equilibrate the local labor market, reducing population to fit the available jobs. But this overlooks that out-migration also destroys jobs. The out-migrants take away some spending that otherwise would have occurred, reducing local demand. Out-migration also reduces local housing construction and housing prices, and since spending is related to housing wealth, this can further reduce local demand.

Consequently, when a local labor market's population falls, evidence indicates that local jobs fall by a similar proportion. Out-migration thus does little to improve the employment rate.

Job Growth in Distressed Places Helps Both Locally and Nationally

Will adding jobs in distressed areas help the nonemployed? One could hypothesize that people moving in, attracted by new jobs, would quickly offset any short-term benefits for residents from more jobs. In this case, the new jobs simply encourage higher housing prices and gentrification.

This pessimistic theory, however, is not borne out by empirical estimates. Even 10 years after new jobs are added to a local labor market, employment rates there are higher. For every 100 new jobs created, 20 to 30 residents are employed who otherwise would not be. These long-run effects seem to persist even after two or three decades.

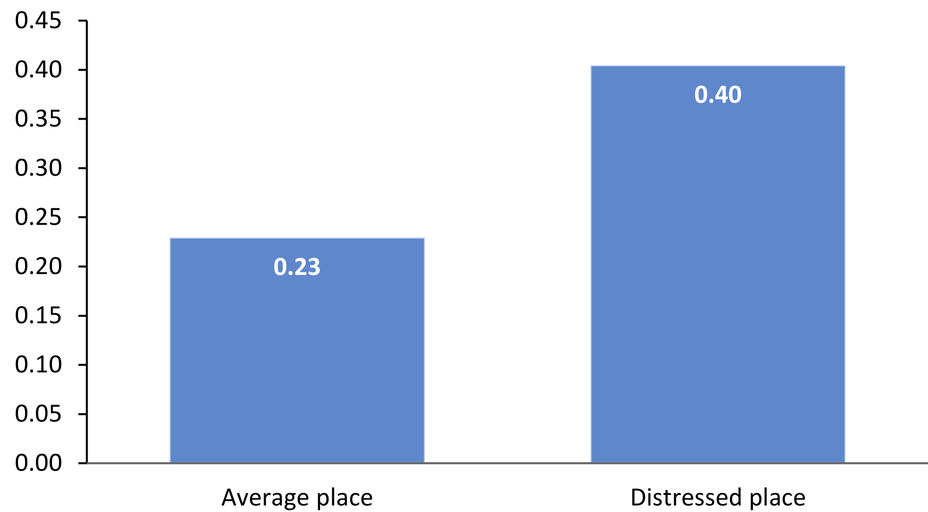
Why can these long-term effects on employment rates persist, even after full migration adjustment? Because more jobs in a local labor market allow some residents, who otherwise would not be employed, to gain labor market experience. This extra job experience increases these residents' job skills and self-confidence. As a result, these residents become more competitive in the job market: they are better able to get and keep jobs of higher quality. The extra labor market experience may even help the next generation be more successful.

Moreover, these benefits of job growth are asymmetric: local job growth effects are 60–90 percent higher in a distressed place than in an average place. For every 100 new jobs, about 23 contribute to raising the employment rate in an average place, but 40 do so in a distressed place (Figure 1).

Because of this asymmetry, creating jobs in distressed places raises national employment and output. The additional jobs created in distressed places draw people into productive employment, raising the overall effective national labor supply and economic output.

Redistributing jobs to distressed places can raise national employment.

Figure 1 Share of Added Jobs That Raise LR Employment Rate in:



These benefits are also modestly progressive in that the largest boost to income occurs among lower-income groups, who are less likely to be employed and stand to gain the most from greater job opportunities.

Our Current State Competition for Jobs Is Not an Effective Way to Help Distressed Places

Governors and mayors currently try to attract jobs by granting tax incentives to businesses, to the tune of almost $50 billion annually.

While these incentives may help attract jobs, they are not the best policy solution to help distressed places, for at least three reasons:

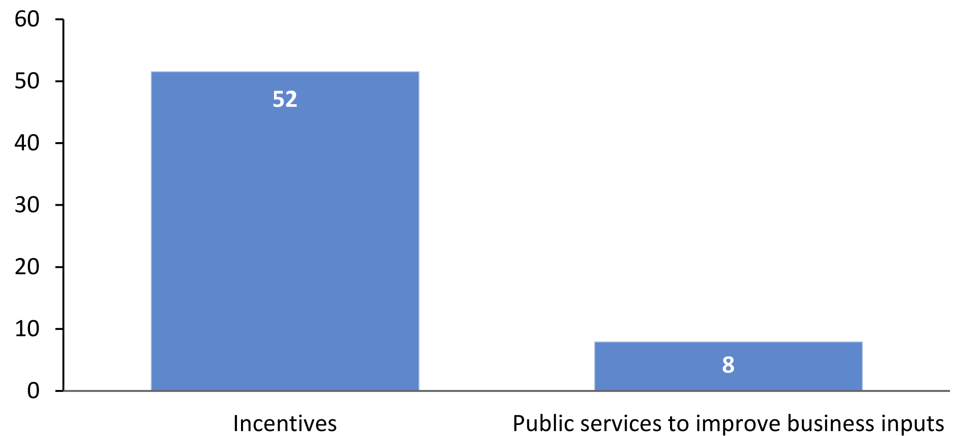
1) **Incentives are not targeted at distressed places.** The incentives that states offer generally are not related to underlying economic conditions. For example, Indiana's incentives are twice as high as Illinois's, even though these neighboring states have similar employment rates. Even within states, incentives are generally available to communities regardless of whether they are booming suburbs or distressed central cities or struggling rural areas.

2) **Incentives are poorly designed.** Incentives often last for 10 to 15 years, much longer than the salient period over which many business owners make location and expansion decisions. Incentives also go to all kinds of firms, with little concentration toward high-tech industries, which have been found to create greater numbers of jobs in related and downstream industries. To the extent that some firms are favored in being granted incentives, those favored tend to be large corporations. Governors and mayors appear to be tempted by the political benefits of current incentive policies: providing incentives to high-profile large corporations generates favorable public relations, and making incentives long-lasting defers the costs onto the next governor or mayor. Unfortunately, these features also do less to promote job growth.

3) **Few resources go to job-creation policies that seek to improve business inputs and have proven to be relatively more cost effective.** Customized business advice to small businesses, such as manufacturing extension services, has been shown to offer a return on investment of over five to one. Updating roads and other public infrastructure can effectively spur local job creation, as can providing industrial parks with land zoned and permitted for new business activity. Job-skills programs that are oriented to business needs, such as customized training programs designed around a specific business's skill needs, also can be a cost-effective way of promoting local job growth. Despite these advantages, current place-oriented policies spend $6.50 on incentives for every $1.00 spent on targeting local business inputs (Figure 2).

Federal policy should tax excessive incentives to large corporations, and it should help distressed places by subsidizing local business inputs.

Figure 2 Annual Resources, in Billions of Dollars, for Place Policies to Create Jobs: Incentives vs. Business Input Services



Needed Reforms: Cut Back Wasteful Incentives, Enhance Local Business Inputs in Distressed Places

Reforms to current place-oriented policies are needed. Such reforms could come from state governments acting in their own residents' interests. States could greatly increase the effectiveness of place-oriented policies through greater targeting of distressed places, cutting excessively long-term incentives, and placing more emphasis on public services to enhance business inputs.

However, handing out long-term tax incentives to large corporations can bring large political benefits to elected officials, with costs paid by their successors, and this makes reform a challenge. In the absence of state policy changes, federal intervention should be considered.

The federal government could consider levying a tax, maybe even as great as 100 percent, on large tax incentives or cash grants that states make available to individual large corporations but not similarly situated smaller businesses.

Such a tax would be consistent with a federal concern over the largest corporations having excessive power, yet it would still give considerable freedom to states to set their own tax policies. States could hand out investment tax credits or job creation tax credits, as long as businesses of all sizes were equally eligible. Moreover, this federal "incentive tax" could be administratively feasible, affecting only a manageable number of large corporations. For example, fewer than 1,500 firms have over 10,000 employees nationwide.

Federal policy could also provide a cash block grant to help enhance business services in distressed places. This grant could be used flexibly by state and local governments to bolster business services to smaller businesses, local infrastructure and land development, and job training.

If the federal block grant program required that distressed places be targeted based on quantifiable criteria, then the program's effectiveness could be rigorously evaluated. Targeted places could be compared with similar places that just missed the cutoff for being targeted.

A federal block grant program with an annual cost of $20 billion could eventually create millions of jobs in distressed places. This job creation in distressed places would reduce the number of persons left behind by the economy, while enhancing overall national growth.

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