

# What Works in State Economic Development Policy?

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# Outline of Talk

1. What is economic development?
2. What works in economic development?
3. Observations on Wisconsin's programs

# What is state economic development policy?

**Common view:** Policies to increase job growth

**My view:** Policies to increase earnings per capita of state residents

**Why it matters:** **Wage rates** and **who gets the jobs** have large effects on social benefits

# State economic development policy = labor market policy

Earnings per capita of state residents can be increased by:

- **Labor demand policies:** Policies to increase quantity and quality of jobs available to state residents
- **Labor supply policies:** Policies to increase quantity and quality of labor supply of state residents

My talk today focuses on labor demand policies

# What Works?

## Labor Demand

- Financial/tax incentives
- Customized job training
- Manufacturing/business extension
- Entrepreneurship training/small business development
- Information/ombudsmen
- Capital assistance
- High tech

## Labor Supply

- Preschool

# 1. Financial/tax incentives

**Description:** Tax credits or grants to individual businesses to encourage location, expansion, or retention.

**Evidence:**

- Typical incentive can be offset by wage change of \$0.79/hour
- Typical incentive decisive in 4% of cases
- Cost per job: \$200,000 in present value
- Incentives more effective if targeted at quality job creation for unemployed in existing small businesses (e.g., MEED program, Minnesota, 1980s)

## 2. Customized job training

**Description:** Provide a business that is locating or expanding, or considering leaving or downsizing, with job training for current or new workers customized to business's needs

**Evidence:**

- 10 to 16 times as effective as financial incentives
- Effective because: upfront; skills hard to find; subsidy recovered if business leaves
- Can be tied to “first-source” programs to encourage hiring of local unemployed

# 3. Manufacturing/business extension

**Description:** Free or low-cost advice to businesses to improve business productivity and sales.

**Evidence:**

- Lowers costs by \$3 per dollar spent
- Average assisted business gets sales increase of \$143K, cost reduction of \$50K
- Some states (PA, TN) run broader business extension that pays for short-term consulting from state university faculty



## 4. Entrepreneurship training/small business development

**Description:** Provide potential or actual small businesses with advice or training in business planning or operations.

**Evidence:**

- Entrepreneurship training increases successful start-ups by one-third
- Small business development centers and incubators also have evidence of success

# 5. Information/ombudsmen

**Description:** Provide existing state businesses, or business prospects, with information and connections to help overcome barriers to business location or expansion.

**Evidence:**

- Highly successful per dollar spent
- Particularly important for small and medium-sized businesses
- Help with regulations, permits, and program requirements is especially effective
- Business visitation also useful source of feedback on state issues

## 6. Capital Market Assistance

**Description:** Provide direct government loans/grants/ investment to businesses, or indirectly encourage private sector financing.

**Evidence:**

- Most programs not evaluated
- Favorable evidence on Capital Access Programs (subsidize bank lending to risky businesses)
- Favorable evidence on SBA loan guarantees; revolving loan funds; “business development financial institutions” in distressed areas

## 7. High tech

**Description:** Includes all of previous 6 programs, but targeted at high-tech. Also includes technology transfer from universities to local businesses.

**Evidence:**

- Coordinated strategies more successful
- Some favorable evidence for PA's Ben Franklin Technology Partners program (regional centers, coordinated programs)
- San Diego also useful model
- University role in providing consulting and workers more important than research spinoffs

# Common principles of successful labor demand programs:

- **Information and training** is often cheap and effective
- **Small and medium-sized businesses already in state** are often easier to influence than large out-of-state businesses

## 8. High-quality universal preschool

**Description:** Preschool programs with small class sizes and quality teachers, operating half-day during the school year, with universal availability for all 4-year-olds.

**Evidence:**

- Strong evidence of long-term effects in improving adult employment, wages, and education, and lowering crime
- In long-run, increases state jobs by about twice as much per dollar as financial incentives to business
- Economic impact is delayed
- Similar analysis can be done of other labor supply or job skills programs

# Observations on Wisconsin's Programs

- Wisconsin places less emphasis on costly financial incentives than other states
- Wisconsin does all the labor demand programs discussed in this talk
- Are the programs large enough and linked together well enough to have the desired impact?
- Do programs have a good feedback system?