INCENTIVIZING THE MISSING MIDDLE: THE ROLE OF ECONOMIC DEVELOPMENT POLICY

HEATHER M. STEPHENS, WEST VIRGINIA UNIVERSITY

Co-authored with CARLIANNE PATRICK, GEORGIA STATE UNIVERSITY
A wealth of research has documented the decline of the middle class and the increase in inequality in the United States (Pew Research Center 2015; 2016; Chetty et al. 2014; and Piketty 2013; among others).

While some inequality can help drive growth,
  • Recent research suggests that the current levels of inequality in the U.S. may be suppressing economic growth (e.g. Partridge and Weinstein 2013; Atems 2013).

At the same time, inequality and poverty are more pronounced in some areas than others
  • This may be due to the industrial composition (Florida, 2017).
  • However, the mechanisms for increased inequality at the local level are not well understood.
ECONOMIC DEVELOPMENT INCENTIVES

• Economic development incentives are the primary policy tool for promoting local economic and employment growth.

• Previous research suggests that incentives have varied effects.
  • Harger et al. (2019) find that targeted incentives may help some industries, while hurting others.
  • Patrick (2016) demonstrates that capital subsidies result in changes in firm behaviors and local industry composition that limit job creation.
RESEARCH QUESTION

• Are economic development incentives contributing to the decline of the middle class and increasing inequality?

• We consider the impact of economic development incentives on employment changes in “middle class” industries.

• We define industries in two ways:
  1. Based on the average wages in that industry
     - Middle wage is “middle class”
  2. Based on the occupations in that industry
     - Working class is “middle class”
• Classifying middle class industries is based on the average wage income in that industry using data from EMSI, Inc.

• Following guidance by the Pew Research Center (2015;2016)
  • We adjust American Community Survey (ACS) data based on average household sizes and number of earners.
  • Middle class industries include those with incomes between two-thirds to double the median income or within a middle class wage range from $20,485 to $61,455 (in 2016 dollars).
DATA – CLASSIFYING INDUSTRIES BASED ON OCCUPATIONS

• Using data from the Martin Prosperity Institute (MPI)
  • Industries’ occupations are classified into four major categories:
    • Creative Class
    • Working Class
    • Service Class
    • Agriculture (not included in our analysis)

• We classify industries as in a category if the highest percentage of jobs is in that category.
DATA – COMPARING INDUSTRY CLASSIFICATIONS

• Middle-wage and working-class industries are not the same.
  • Only about 37% of industries that are working class are also middle wage.

• Some differences include:
  • Administrative and support industries classified as middle wage and service class (e.g., skilled nursing facility industry)
  • Industries requiring specialized manual labor classified as working class but high wage (e.g., oil and natural gas pipeline industries)
  • High cognitive skill service industries classified as middle wage and creative class (e.g., architecture industry and performing arts)
OTHER DATA

• Detailed employment data by Metropolitan Statistical Area (MSA)

• W.E. Upjohn Institute Panel Data on Incentives (PDIT)
  • 45 industries in 47 cities in 33 states (92% of 2013 private sector GDP)
  • Use annual 12% discounted net taxes by city and industry
  • We assume that city net taxes are representative of MSA net taxes
  • Does not include all industries
• The share of employment in middle-wage industries is declining.
• The share of jobs in low-wage industries is increasing.
TRENDS IN EMPLOYMENT BY MPI CLASS

- The share of employment in working-class industries is declining.
- The share of jobs in service-class industries is increasing.
- Some evidence of increasing share of jobs in creative-class industries.
“TARGET” WAGE CLASS BY CBSA

2000

2015
“TARGET” MPI CLASS BY CBSA

2000

2015
CHALLENGE WITH OUR RESEARCH

• Are we actually able to get at whether incentives are causing changes in employment or is something else going on?

• We use special statistical techniques to control for this.
OUR FINDINGS

• Our analysis suggests that economic development incentives are having an effect on the distribution of employment across wage and industry classes.

• Incentivizing working-class and middle-wage industries has positive employment effects for those industries.
  • For working-class industries, these incentives also increase employment in other industries.

• There is no evidence that reducing incentives (or raising taxes) on creative-class and high-wage industries has negative employment effects for any industry type.
  • It may even increase employment in working-class and middle-wage industries.
POLICY IMPLICATIONS AND NEXT STEPS

• The most incentivized classes of industries tend to be those classified as “high-wage” or “creative-class”
  • However, we find evidence that these incentives are NOT increasing employment in these industries and are contributing to the hollowing out of the middle class.

• Economic development professionals and other policymakers may want to consider this when making future decisions about incentives.

• In our future research, we will further explore the impact of these incentives on the relative wages and employment in targeted industries
  • Compared to non-targeted industries in that location.
  • Compared to those industries in other locations.
THANK YOU!

Heather Stephens
Assistant Professor
Resource Economics and Management
West Virginia University

✉️ heather.stephens@mail.wvu.edu