Analytics

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Economic growth starts at home

In his recent State of the State address the Governor asserted that the legislated expiration of both his earlier 17% increase in Delaware's top personal income tax rate and the 34% increase in the average gross receipts tax rates were "unaffordable tax cuts today."

How has Delaware fared since Governor Markell's first State of the State speech and proposed budget? Between January of 2009 and today Delaware has lost almost 7,000 jobs, the unemployment rate is unchanged at 6.9%, the labor force has fallen by more than 3,000, and per capita income remains below the U.S. average.

Governor Markell says he does not support "turning our backs on our most vulnerable citizens" or "compromising public safety" by imposing significant cuts to the budget. That said, are there easy examples of spending cuts which are needed?

Take, for example, the Delaware Department of Education (DDOE), the top spending department in the state.

This fiscal year DOE will spend $604,000 on on-line periodicals, even though these are available through the University of Delaware's Morris Library. A report issued in 2008 recommended consolidation of school districts to save administrative overhead, but no action has been taken and Delaware ranks 8th among the states in administrative spending per pupil. Delaware spends over $81 million a year on student transportation, which is more than 47 other states.

And what is the opportunity cost to Delaware's economy of keeping taxes higher and not cutting any state spending?

Growth in jobs within a state is a result of the net migration of firms, the birth and death of firms, and the expansion and contraction of firms. Recent analysis of the National Establishment Time-Series by the Illinois Policy Institutes (IPI) provides important insights for Delaware.

IPI examined job data spanning 1995 through 2009. Over that period employment in Delaware rose just 1.6%, ranking Delaware 41st among the states and well below the national increase of 11.6%.

The lack of job growth wasn't due to the net out-migration of companies from Delaware. Over the study period net-migration added 2.3% to the total jobs in the state, ranking Delaware second among all states. Certainly Delaware's economic development community's business recruiting efforts paid off.

Delaware did not fare as well with respect to net start-ups. The jobs created by business start-ups in Delaware fell short of the jobs lost through the closure of businesses. This placed Delaware in the bottom fifth of the states in job change from the birth and death of firms.

Finally, and most significantly, Delaware ranked dead last among the states in the net jobs gained through the expansion and contraction of existing firms. Over the study period Delaware had a net gain of 8% from the process of expansion and contraction, which is half of the U.S. average across the U.S and less than a third of the net gains in the leading states of Arizona and Florida. Delaware ranked fourth to last in rate of expansion of existing firms.

The lackluster performance of Delaware's existing firms is a major factor behind the state's poor job growth. It is a reflection of higher taxes, regulations, relative energy costs, and poor quality public schools. The state doesn't need to do a better job recruiting; it needs to create the conditions that encourage investment and expansion of its existing businesses over the long haul.

Allowing households to keep and spend more of their income, and allowing businesses to reinvest their gross receipts rather than turning them over to the state, requires belt tightening by state government in the short-run, but will restore economic growth to Delaware over the long-run.

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