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Recent Trends and Historical Contexts in the Rise and Fall of Economic Regions

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A significant development that sooner or later will be placed on the research agenda of economic and business historians is the convergence of regional per capita incomes in the United States that has taken place during the last half century. For example, in 1929 per capita incomes in the Southeast and Southwest were 50 and 60 percent of the national average, respectively. By 1980 per capita incomes in these regions had moved to within 90 and 95 percent of the national average. By way of contrast per capita income in the Mideast moved from 140 to just over 110 percent of the national average over the same period, while New England's percentage went from 125 to just under 110 in that fifty-year traverse. Other statistics on trends in capital formation, population growth, employment, and so on would all reveal a similar "gaining" of the southern and western regions on those of the Northeast and Midwest. This imbalance in the economic performance of regions within the United States has even accelerated within the past decade or two, which in turn has sparked intense debates on development policy at the national level and feverish activity at state and local levels seeking to lure industry and jobs. To be sure, popular perceptions of this decline or slippage in the economic performance of the older regions is based on relative or comparative analysis like the above rather than absolute decline or backwardation. Yet my own home state of Illinois has lost almost 300,000 jobs since 1980 due to the outmigration and relocation of industrial establishments. Our sister state, Michigan, has fared even worse; and a similar tale could be told for many of the older, industrial areas.

The contemporary business press and modern scholarship has offered a variety of explanations of this phenomenon ranging from the differential effects of international economic competition, wage structures, labor force composition, unionization, and climate to unexplained spatial clusterings of high-growth industries around major research universities and industrial park complexes. New words like re-industrialization and de-industrialization have been coined in the search for a deeper understanding of the phenomenon of differential regional growth, and an increasing number of academics and businessmen are calling for the formation of an industrial policy. The proliferation of ideas and proferred solutions signals the need for perspective. Perspective is the province of the historian, but can we contribute anything? My answer would be a qualified "yes".

The qualification arises because the principal focus of business and economic historians has been on economic growth and performance in the nineteenth and early twentieth centuries. Relatively less emphasis has been placed on the phenomenon of economic decline. Economic decline has, for the most part, been treated as a pathological phenomenon confined to particular regions, like the postbellum South, or particular industries, like New England's textiles or the charcoal segment of the iron industry. The _explicans_ for growth has been the playing out of natural market forces with a subsidiary litany of abundant factor supplies harnessed by improving technologies, undergirded by an expanding scientific capability within the framework of permissive and enabling, albeit weak, legal and governmental institutions. That which has explained growth does not explain decline and conversely, so that they have never been seen as inseparable parts of the same conceptual whole. All of this has formed a major intellectual enterprise, and it would be rash to condemn it as wrong or misguided in an absolute sense.

One cannot escape the conclusion, however, that our approach to the subject of growth and decline has been _ad hoc_, but, more important, incomplete. It has been incomplete for two reasons. First, the role of government has never been satisfactorily integrated into our analyses. Second, the watershed in the relationship of the federal government to the economy that occurred in the post-World War II period has been treated more as a stylized fact than as an object for deeper analysis and explanation. The consequence of this disjuncture has been that the relatively recent experience of industrial restructuring and regional reorientation around different economic bases, which appears somewhat mystical to those who look at these developments through a stylized public/private relationship. Quite obviously something has changed. But what is it that is new in that which is older and more familiar?

That government affected the historical economy prior to World War I has become not only an increasingly accepted proposition, but has inspired quite a few inquiries in recent years. In general this work has focused on regulation and legislation aimed at particular industries, on the one hand, and has chronicled specific events aimed at specific sectors, on the other. On the latter view, the policy since the founding of the United States has been to encourage economic development and growth through improved transportation — canals, then railroads, highways, harbor development, river improvement, and the like. Other programs in the historical economy have involved more direct incentives via homesteading acts, provision of water control services and facilities, and rural electrification. By these means the government facilitated the private economy, but the weight of historical scholarship has left no doubt that the impetus to growth primarily came from market forces. Government was, at best, the handmaiden. Government policy had a programmatic character. The objects of such policies were national in scope, although in various subperiods their effects impinged differently on different regions.

It is also well to bear in mind that by government in the historical economy we mean state and local as well as federal; and that the purely fiscal effects of state and local government exceeded those emanating from the federal level. For more than 100 years from 1789 to 1893 tariffs and customs duties provided the preponderance of revenues for the national government. In the 1890s more than half of federal revenue came from tariffs. After the major role personal and corporate income taxes played in World War I, they remained a latent force until World War II. From the early 1920s until the early 1940s, they accounted for less than half of total net revenues. In the three decades from the mid-1950s to the present there were significant changes in tax structure. Personal income tax revenue remained steady at about 45 percent of federal revenues, while corporate taxes declined from about 30 percent to 8 percent over the same period. The slack had been taken up by payroll taxes, increasing from 11 to 37 percent of the annual federal total. The point of this recitation is not to outline in detail the changing sources of federal revenues, but merely to indicate that federal finance was becoming more broadly based, hence powerful _vis a vis_ state and local government in the twentieth century.

In fiscal year 1929, revenues raised by state and local governments amounted to 65 percent of the total of government at all levels. By fiscal year 1950 the ratio had reversed, with the federal government taking 65 percent of all tax revenue. Some measure of the magnitude of the fiscal effects of federal expenditure over this period may be gained from the knowledge that tax receipts at all levels combined totaled $11.2 billion in 1929 and $940 billion in 1980.

This growth of federal fiscal power is well known, but much less well understood. It has become a commonplace to observe that the taxing and expenditure, that is fiscal activities of the federal government affect the rate of growth as well as level of _national_ income. Another way of phrasing this bit of conventional wisdom is to assert that _aggregate_ fiscal policy affects the _aggregate_ level of national income. But the aggregate is nothing more than the sum of the parts, in the case at hand we may view the national economy as the outcome of a collection of regional economic experiences and episodes. More especially, we might ask: "Does national economic policy have regional impacts?" and, if so, "How have these effects contributed to contemporary economic and industrial performance by region?"

A simple concept, the federal balance of payments to the individual states, reveals something of the problem. The federal balance of payments or federal flow of funds, as it is also known, is simply the ratio of estimated federal government expenditures in each state to the estimated federal revenues from residents (personal and corporate) of the state. If the ratio equals one, it means that tax payments from the state to the federal government exactly equal the expenditure of federal funds within the state. If less than one, it means state taxpayers are sending more money to Washington than Washington is returning — and greater than one, conversely.

In the early 1950s, midwestern states had ratios well below one on average. A similar pattern was found in the northwest. Southern states ranging in a belt from South Carolina to New Mexico were almost all above two. The state-by-state pattern might vary within regions, but the interregional pattern was clear enough. Southeastern and southwestern states were receiving over $2 of federal spending within their borders for every $1 sent to Washington, while the midwestern and northeastern states were getting something like 75 cents return on the federal balance of payments; but a clear margin of advantage remained for the South, broadly defined. For example a study of the federal balance of payments for the period 1975-1979 shows that the states of the Midwest and Northeast sent $165 billion more in taxes to Washington than they got back in federal spending.

While federal defense spending does not tell the whole story, its patterns and politics does reveal something of how the convergence in regional per capita incomes was brought about. As early as 1952 the potential of the federal government's procurement power to stimulate economic development in distressed areas was recognized with the issuance of Defense Manpower Policy No. 4 (DMP-4) by President Truman. The purpose of this policy was to direct a portion of federal procurement contracts to firms in areas of high unemployment.

Total defense spending in fiscal year 1983 was $245 billion, of which $71 billion was spent in the Northeast and Midwest and $174 billion was spent in the South and West. It has been estimated that each $1 billion of defense spending generates about 40,000 jobs per year. From this it can be readily seen that the difference in defense spending patterns (military pay plus procurement) across regions accounts for roughly 4.0 million more jobs (4 percent of the national labor force) in the South and West than in the Northeast and Midwest. Two caveats apply. First, this kind of measure is very crude; and second, only the employment effects of defense spending are portrayed, not the employment benefits of <u>all</u> federal spending. All federal expenditure in 1983 was $900 billion so that the regional employment effect of defense spending tells only a portion, approximately 25 percent, of the tale of the imbalance in regional growth.

Since the 1930s, the federal government has invested billions of dollars in laying the foundation for economic revival in the South and development of the West. Massive federal outlays for the Tennessee Valley Authority, interstate highways, water and energy projects, rural electrification, port construction, the space program, in addition to military bases, plus defense and other procurement, established the basis for rapid economic growth in these regions. Without putting too fine point on the threads of this argument, the enormous fiscal stimulus applied to the South and West was, in good part, financed by the adverse federal balance of payments, that is the ratio of federal expenditures to tax receipts, in the Midwest and Northeast. Even today as relative, and in some cases, absolute, economic decline continues in the older regions, federal policy remains tilted toward the development interests of the South and West.

What remains is to investigate the underlying forces and factors that account for the regional tilt in federal spending. Quite naturally we are led to the political process. Two committees of the legislative branch dominate federal finance. The House Ways and Means Committee, which pre-dates even the formation of the Treasury, and the Senate Finance Committee, which became a standing committee in 1816, now wield enormous power over the budget and the economy. They have jurisdiction over all the revenues in the budget and roughly half of the spending.

This gives them more power over the budget than either the Budget or Appropriations committees.

The sources of government revenue from 1789 to the end of the nineteenth century were the subject of the most heated partisan and regional politics. Tariff debates separated Whigs from Federalists, Democrats from Republicans, North from South, industry from agriculture, protectionists from free traders, Presidents from Congresses, House from Senate and Committees on taxes from Committees with jurisdiction over commerce and manufacturing. In the early decades of the twentieth century, however, even after the tariff declined as a major source of revenue, the battles continued. While financial and economic historians have written extensively on the politics of tariffs, other aspects of the federal fiscal process have received scant attention.

While my own reading of legislative history is incomplete, I am tempted to speculate that, in this century, both the House Ways and Means and Senate Finance committees were controlled in more years than not by members from the border states and the South, that southern senators and congressmen achieved more seniority and key committee assignments that legislators from other regions, and finally that southerners recognized a distinct regional interest and acted accordingly. To prove all that would be a tall order, but these conclusions do have the virtue of being consistent with the facts of comparative regional development.

The tale I have outlined links relative economic performance by region to the effects of the ratio of federal expenditure to tax receipts by state or region. The distributional rules, or allocative decisions, derive from committees and caucuses in the House and Senate whose dominant members recognize a regional economic interest and act accordingly. It has also been indicated that this imbalance in regional fiscal stimulus is sufficiently powerful to account for the differential economic performance between the Midwest and Northeast and the South and West over the last half century.

I believe this view provides a useful perspective on the contemporary concern over the restructuring of American industry in that the fiscal process outlined above embraces and accounts for both growth and decline. Contemporary handwringing over international competitiveness, de-industrialization, re-industrialization, and the panacea of economic salvation through high-tech all suffer from misplaced emphasis. Hopefully these remarks have once again demonstrated the utility and importance of the historian's craft.

MANAGEMENT AND TECHNOLOGY