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Are Regional Incomes Diverging?

by

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ARE REGIONAL INCOMES DIVERGING?[1]

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After five decades of narrowing regional income differences in per capita personal income (PCPI), regional income differences appear to have widened during the 1980s. From 1929 to 1979, PCPI increased from 64 to 90 percent of the national average for low income regions of the U.S. (Southeast, Southwest, Plains and Rocky Mountain) and declined from 127 to 107 percent in the high income regions (New England, Mideast, Great Lakes and Far West). The reduction was so great that by 1979 state PCPI inequality was less than one-third of its 1929 levels.

This strong empirical evidence has been used to support the notion that as a nation develops economically, regional differences disappear, or regions will converge to some national average. If the data are reflective of actual economic development and growth, the implications on federal, state and local development efforts are pronounced. Proponents of the free market economy maintained that the national economy is efficient in development and growth, hence there is no need for government intervention. In other words, as the nation's economy grows and develops, inequalities in income across regions will gradually diminish in a naturally occurring process.

However, more recent empirical evidence suggests a disturbing reversal of these earlier trends. Starting in the late 1970s, low income regions began to loose some of the progress they had made during the previous fifty years. From 1979 to the late 1980s, the low income regions slipped back to 88 percent of the national average, and the high income regions rose to 109 percent (see top chart). Only three smaller regions resisted the national trend. The Southeast region continued to show upward movement toward the U.S. average, while the Great Lakes and the Far West showed continued downward movement to the U.S. average. The Great Lakes states, in which Wisconsin is a member, actually fell below the U.S. average.

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[1] For additional readings see D.H. Garnick, "Accounting for Regional Differences in Per Capita Personal Income Growth: An Update and Extension," *Survey of Current Business*, January, 1990. T.D. Rowley, J.M. Redman, and J. Angle, *The Rapid Rise in State Per Capita Inequality in the 1980s: Sources and Prospects.* Economic Research Service, U.S. Department of Agriculture. Staff Report AGES 9104 (January 1991).

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More recent and detailed information on the performance of regional economies—and in particular Wisconsin—can be gained by examining the coefficient of equality (CoE) in regional PCPI. A high CoE value suggests a high degree of inequality, low values of CoE suggest a low degree of inequality. By plotting the CoE over time, insights into regional income convergence or divergence can be gained. Earlier studies of the CoE for the U.S. concurred with the analysis discussed above; regional differences are becoming smaller, or regions are converging. This is evident by the downward movement in the CoE plotted in the second chart. However, from about 1979 the CoE increased for the nation and Wisconsin counties. This latter trend in the CoE suggests a widening gap between higher- and lower-income regions across the U.S. and within Wisconsin.

Several reasons have been advanced for the apparent reversal of the regional convergence trends at the national level. For example, the boom-bust of the energy industry in the Rocky Mountain states and Alaska, the massive military buildup that occurred in New England and California, and significant retirement migration to the Southeast. For Wisconsin, it appears that the growth in incomes in the northern and western parts of the state did not keep pace with growth in the southern and eastern parts of the state. The strong performance of Wisconsin's manufacturing belt appears to be bucking the national downward trend in manufacturing industries. Unfortunately, our current models of regional economic growth and development have not done an adequate job in helping explain or predict the reversal evident in the 1980s: we know less about regional economic performance than we had previously thought.

Perhaps the most important ramification of these trends is the role of federal, state and local economic development policies. Prior to the late 1970s a strong case could be made for limited government intervention, today the evidence of regional divergence strongly suggests a more active role for federal, state, and local governments in formulating effective economic development and growth policies.

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