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PERSPECTIVE

What Americans Demand From State Governments

W. MICHAEL COX AND RICHARD ALM

The Great Recession's aftermath roiled state budgets and gave new urgency to questions about the size and scope of government — how much to tax, how much to spend and how much power to cede to unions. The answers lie in the movement of people across state lines — Americans voting with their feet.

Internal Revenue Service data for 2004 to 2008 show Texas was the hands-down winner in net migration, with a gain of 500,000 people. Florida came next, adding 350,000 migrants, followed by North Carolina, Georgia and Arizona.

California still added newcomers from overseas, but it nevertheless led all states with a net loss of more than 700,000 residents — enough to nearly empty San Francisco. New York saw a net outflow of 550,000 people. Michigan, New Jersey and Illinois also had big population losses over the four-year period.

Is there any message in all these comings and goings? To find out, we used the powerful tool that made "Freakonomics" a runaway best-seller — regression analysis.

We examined 16 measurable differences among states — for example, the jobless rate, average earnings, the environment for small business, income taxes and public spending growth. Six of the 16 prove to be significant drivers of net migration, and taken together they account for two-thirds of annual interstate population flows.

Weather matters — but nobody can do much about it. State and local policy-makers, on the other hand, can influence the five other factors driving net migration — income tax rates, union power, spending growth, public schools and home prices.

Income taxes burden citizens when a dollar going to public services delivers less benefit than a dollar spent on private consumption and savings. The highest marginal income tax rates are 12% in Massachusetts, 11% in Oregon and Hawaii and 10.8% in New Jersey. By contrast, Texas and six other states don't impose any income taxes at all.

Our analysis reveals the impact of the gap between high- and low-tax states. A 10-percentage-point cut in the highest marginal rate would prompt the net in-migration of 444,808 people over a decade.

Strong unions deter migrants in two ways. First, they restrict their benefits to existing members, who don't necessarily want competition from new workers. Second, they inhibit job creation by raising the costs of doing business.

As a result, employers and workers will be attracted to less unionized states, where markets set pay and companies have greater leeway in hiring new workers, firing redundant ones and adjusting their operations.

State labor laws influence the strength and spread of unions. All but two of the 25 states with the highest membership rates allow contracts that require workers to join unions and pay dues. Right-to-work laws that prohibit mandatory union membership hold sway in all but one of the 20 states with the lowest unionization rates.

Education Magnet

Private-sector union membership varies from a high of 27.5% of the workforce in New York to a low of 3.3% in South Carolina. A 10-percentage-point decrease in a state's private-sector unionization rate would lead to net in-migration of 394,832 people a decade.

Like big unions, big government puts a damper on economic activity, especially if it means higher taxes. In our analysis, several measures of government size didn't meet accepted standards for significance. But one did — the five-year rise in per capita state and local spending, measured relative to the average of all states.

Most likely, big spending increases create fears that future tax hikes will be necessary to sustain the growing public sector.

Before the Great Recession led to budget-cutting in many states, government spending had been rising fastest in Wyoming, Rhode Island and Florida. The slowest growth had been in Alaska and Oregon. Five-tenths of a percentage-point decrease in the relative growth of state and local spending would attract 23,189 newcomers in a decade.

For generations, education has been the most reliable path to higher-paying jobs and better living standards — so potential migrants with children are likely to seek states with superior schools. Students in Massachusetts, Minnesota and Vermont perform the best on proficiency tests. At the other end of the rankings are Missis-

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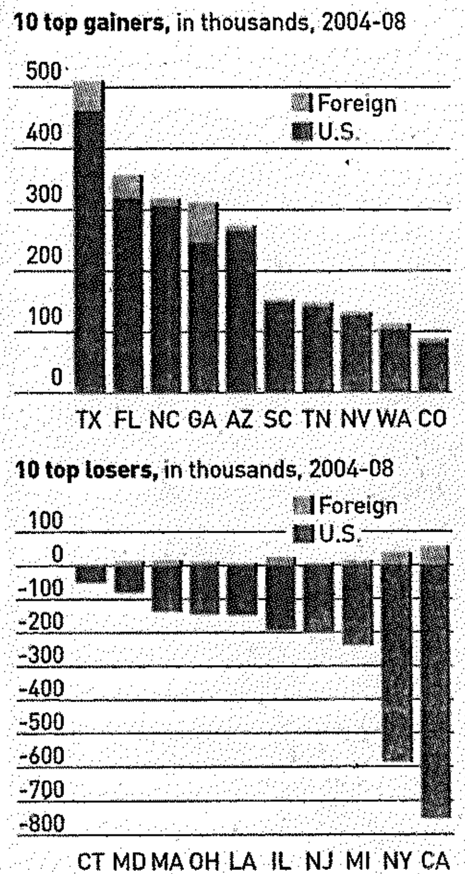
Hola Texas, Adios California

From 2004 to 2008, net migration added more people to Texas than any other state. California and New York suffered the greatest losses.



Source: Center for Global Markets and Freedom, SMU Cox School of Business

sippi and New Mexico.

Among the many measures of educational quality, scores on public schools' eighth grade proficiency tests in reading and math provide the best fit for net migration. Our analysis shows that a 10-percentage-point increase would bring in 272,181 people a decade.

Net migration finds a preference for lower taxes and skepticism about rising spending — so education's importance to net migration doesn't amount to a blank check for increasing school budgets. The most promising cost-effective strategies for improving education include healthy doses of competition and consumer choice, an approach championed by Nobel laureate Milton Friedman.

Reason To Leave

The housing bubble erupted mainly on the East and West Coasts, suggesting that local policies have a lot to do with housing prices. After California began enacting various land-use restrictions in the 1970s, real estate prices went into an upward spiral that left the rest of the nation far behind. By contrast, Dallas and Houston had faster income and population growth than California, but the Texas cities saw only modest housing price inflation because they imposed fewer restrictions on land use.

Keeping a roof overhead takes a big chunk of a typical family's budget, creating incentives to leave states with high home prices for places with more affordable housing. The regression analysis shows that a $50,000 decrease in a state's median housing price would yield net in-migration of 111,588 more people a decade.

By voting with their feet, Americans are sending a strong message to policymakers. States can make themselves more attractive to domestic migrants by lowering taxes, enacting right-to-work laws, reining in spending growth, improving education without spending a lot of money and limiting the land-use restrictions that raise housing prices.

Other policies could affect net migration. Indeed, we suspect tort laws and transfer payments may induce people to move, but we've not been able to prove it.

Americans aren't likely to favor one sort of government in their state capitals and communities while tolerating a wholly different type of government in Washington. Good state policy ought to be a guide for the nation as a whole.

Migration within the U.S. tells us that Americans prefer lower taxes — even if it means sacrificing some public services. Heeding this message should prompt the national government to cut spending and reduce the nation's mammoth budget deficits.

Cox is director of the Center for Global Markets and Freedom at Southern Methodist University. **Alm** is writer in residence at the center.