Understanding Community Economic Impacts

Public policymakers play a major role in economic growth by offering incentives (both financial and nonfinancial) to firms to locate in the community. Depending on the investments and incentives, the economic impact of a new industry can be significant. For officials, any new employment will boost total employment and income in the local economy. In the long run, the primary concern of officials is improving the economy. This information sheet is a guide to help policymakers understand economic impact analysis.

What Is Economic Impact

Public policymakers often want to know the impact of community economic development projects on the local area.

Analysis?

Economic analysis shows how a potential development may impact key sectors of the local economy. It usually focuses on four key areas: 1) employment, 2) labor income, 3) output, and 4) government finances or taxes.

Methods

Analysts typically measure economic impact by using primary and secondary data and some type of economic model of the local economy. Information about the new firm's local investment, payroll, employment, output, and sectors relevant to plant operations let them estimate the economic impact of such development in two phases: construction and operation.

Specific Impact Questions

Following are key questions[1] about economic impact analysis that policymakers should address. The answer to these questions should also help them understand their roles and responses to an industry's desire to locate in the community. [2]

1. What Are Economic Impacts?

Economic impacts are effects on the level of economic activity in an area. They are usually viewed as the expansion or contraction of an area's economy, resulting from changes in (such as opening, closing, expansion, or contraction of) a facility, project, or program.

2. How Do You Define Economic Impacts?

They are usually defined as (1) business output (or sales volume), (2) value added (or gross regional product), (3) wealth (including property values), (4) personal income (including wages), and (5) jobs. Any of these measures can indicate improvement in the economic well-being of area residents, which is usually the major goal of economic development efforts.

3. How Do Economic Impacts Occur?

They typically occur in two phases:
(1) **direct economic effects** are the changes in local business activity occurring as a direct consequence of public or private business decisions or public policies and programs; and

[1] Several of these questions are drawn from the primer: *Measuring Economic Impacts of Projects and Programs* by Glen Weisbrod.

[2] Further explanations on the role and response to industrial prospects are found in Extension Publication M1433, *Understanding Local Government's Role and Response to Economic Development.*

(2) the **"indirect" and "induced"** impacts of a project are the "multiplier effects," since they can make the overall economic impacts substantially larger than the direct effects.

4. What Are Economic Multipliers?

Multipliers arise as a result of local businesses, households, and governmental agencies purchasing goods and services from one another. Such interaction within the local economy creates additional or multiplier effects.

Three common multipliers used in economic impact analysis include employment, income, and output. They measure the additional change given a one-unit change in economic activity. For employment, the multiplier would be interpreted as the total change in employment due to a one-unit change in employment. In other words, how much does total employment change in the community when it adds one new job? Similar interpretations could be made for the income and output multipliers in the paper.

Three common multipliers used in economic impact analysis include employment, income, and output. They measure the additional change given a one-unit change in economic activity.

5. How Do You Use Multipliers?

Multipliers are often used to measure economic growth and change in an area because of an opening, closing, expansion, or reduction.

6. What Factors Could Affect the Multipliers?

Multipliers are affected by geographic and economic surroundings. A large area generally has a large multiplier; thus, a dollar is able to circulate more often before leaking out than would be the case in smaller areas. WHY? Small, rural isolated areas tend to have limited goods and services, so consumers have to travel outside the immediate area to shop, reducing the potential for spin-off effects. So, not all multipliers are created equally.

Other factors that determine the multiplier impacts include type of new industry, wage rates at the new plant, availability of local labor, availability of local shopping facilities, support services demanded by the new plant, and the local transportation network.

Multipliers are affected by geographic and economic surroundings; thus, not all multipliers are created equally.

7. Are There Other Impacts?

Economic impacts may also lead to fiscal impacts, which are changes in government revenues (income, sales, and property taxes) and expenditures (on water, sewer, roads, and such). While they are related, fiscal impacts are not the same as economic impacts.

Conclusion

The immediate economic impact of a new firm can be significant, depending on the level of investments and tax abatements given to attract the plant to a community. Local officials' decision to develop the local economy depends on the direct and secondary benefits for the area. Direct spending can create more jobs and income for local residents. Investments in equipment, supplies, and other goods and services by the new firm will create more secondary spending, causing total investments to rise in the local economy.

For More Information

Myles, Albert E. 2005. *Understanding Local Governments' Role and Response to Economic Development*. Mississippi State University Extension Service. Publication M1438.

Myles, Albert E. and Garen Evans 2005. *Measuring the Impact of New Industry in Town*. Mississippi State University Extension Service. Publication M1372.

Weisbrod, Glen. 1997. *Measuring Economic Impacts of Projects and Programs*. Economic Development Research Group, Northwestern University. Website.
http://www.edrgroup.com/pages/pdf/Econ-Impact

Mississippi State University Extension Service

MSUcares.com

By **Dr. Al Myles**, Extension Professor, Agricultural Economics

Information Sheet 1836
Extension Service of Mississippi State University, cooperating with U.S. Department of Agriculture. Published in furtherance of Acts of Congress, May 8 and June 30, 1914. VANCE H. WATSON, Director
(POD 03-08)