EMPOWERING AMERICAN CITIES

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The Secret Sauce in Local Economies: Why Some Cities Grow Faster Than Others

September 2024

With so much of the news focused on the national economy, it is easy to forget that the country's economic picture is a mosaic of snapshots that reflects America's diverse local communities. These microeconomies are the places where we live and work—the neighborhoods where we shop for groceries, raise our families, spend our leisure time, and retire. When our communities are economically healthy, consumer power grows and standards of living rise. In turn, businesses can invest, innovate and expand in a virtuous cycle.

Not every microeconomy enjoys good economic health all the time. Periods of stagnation halt the virtuous cycle or recession sends it in reverse, when businesses close and people leave. Downturns inflict real pain on communities, companies and households, underscoring the imperative for policymakers and business leaders to understand the characteristics that drive or limit local economic growth.

Meeting this priority, the Empowering American Cities initiative aims to help community members develop an understanding of the drivers of growth. This research collaboration between Fifth Third Bank and the Kenan Institute of Private Enterprise examines extended metropolitan areas (EMAs) across the US, teasing out the factors that indicate each area's economic well-being. We analyze key metrics of economic health, including an EMA's productivity, gross domestic product and a structural measure we call Embedded Local Growth Characteristics, or ELGC.

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Empowering American Cities is a collaboration between one of the nation's largest regional banks and a university-based think tank renowned for its economic research. The Kenan Institute of Private Enterprise at the University of North Carolina at Chapel Hill uses proprietary statistical techniques to analyze data for microeconomies representing 88% of U.S. economic activity, while Fifth Third Bank provides in-depth local knowledge that comes from 165 years of serving communities. Together, they generate insights supporting sustained business growth and healthy communities that extend beyond traditional banking solutions.

PRODUCTIVITY

In its simplest terms, productivity is the level of economic output generated by each worker.

Human labor produces the goods and services we consume, yet some work yields more than others. A country's total output, or GDP, is not merely equal to its working population but is a product of labor and capital—the tools, skills and money that people use in their work to boost production. Productivity is a measure of this multiplier effect, indicating how much economic activity is generated with a given amount of work.

Productivity gains are achieved in many ways—for instance, by investing in new technologies, learning new skills or enhancing business processes. When a farmer switches to better fertilizer, a company streamlines its workflows or a chef attends culinary school, productivity is improved. And when workforces, industries and economies become more productive, they can provide more (and better) goods and services for the same amount of work. This progress helps to create wealth and promote higher standards of living, which is why economists, business leaders and policymakers are all concerned with increasing productivity.

When we say *Embedded Local Growth Characteristics*, what do we mean?

The ELGC indicator is a statistical measure that suggests the relative size of an economy's potential growth engine. Broader than productivity, ELGC measures the factors that drive productivity, industry and demographic shifts. An economy that has favorable growth characteristics is like a car's engine that has a lot of cylinders: It can generate more power with the same amount of fuel. The "embedded" aspect speaks to this metric's structural components, which are independent of cyclical economic dynamics and supply side factors, such as labor and financial market conditions. These structural components include an economy's industry mix, demographics, workforce skill level and net migration. A city with large shares of its skilled workforce employed in highly productive sectors, with a large proportion of its population of working age, and with a healthy amount of people moving there from elsewhere would have excellent Embedded Local Growth Characteristics. These attributes indicate a powerful engine of economic growth.

THE COMPONENTS OF ELGC:

Industry Mix

Population Growth and Demographic Trends

Workforce Skill Level

ELGC RANK	LARGEST 50 EMAS	ELGC RANK	MIDSIZE 100 EMAS
1	Austin, TX	1	Fayetteville and Springdale, AR
2	San Francisco Bay Area, CA	2	Boise, ID
3	Seattle, WA	3	Palm Bay, FL
4	Nashville, TN	4	Des Moines, IA
5	Raleigh and Durham, NC	5	Fort Collins, CO
6	Salt Lake City, UT	6	Charleston, SC
7	Dallas and Fort Worth, TX	7	Destin, FL
8	Portland, OR	8	Visalia, CA
9	San Antonio, TX	9	Huntsville, AL
10	Charlotte, NC	10	Omaha, NE

Who are the top performers?

EMAs with the most favorable ELGC tend to have highly productive economies and exhibit the strongest historical and projected economic growth. Our data show that ELGC, productivity and GDP growth, while not equivalent, are closely related metrics and fundamental indicators of economic well-being. ELGC is an especially interesting unit of analysis because we can separate this indicator into its distinct components, factors that influence a local economy's economic potential. As with all the economic metrics we analyze, for ELGC rankings we divide EMAs by size into two distributions: the largest 50 by population and the next 100 cities. We find that splitting our sample of 150 EMAs into these two groups allows for more useful comparisons, particularly when analyzing ELGC, as we find large and midsize cities exhibit different economic dynamics.

Industry mix

Industry mix is a key constituent of an economy's ELGC—having large shares of its workforce employed in high-productivity sectors boosts an EMA's potential growth engine. A high-productivity sector is one that produces high output per worker relative to other sectors. Of the Bureau of Labor Statistics' 10 "Supersectors," Finance and Real Estate is currently the most productive, as it generates more than 20% of US GDP while accounting for only 6% of the country's workforce. The Information sector is second, producing 5% of the nation's output from a mere 2% of its employment.

Ranking No. 2 overall in ELGC strength and projected GDP growth, the San Francisco Bay Area EMA boasts an enviable engine of economic growth, thanks in part to its favorable industry mix. The Bay Area's Information and Manufacturing sectors are especially large and productive relative to national averages. These two sectors together account for 15% of the EMA's employment and nearly a third of its GDP while the same sectors' shares add up to 10% and 15%, respectively, for the nation. A strong Information sector tends to create structural synergies and build resiliency to cyclical downturns across industries. Computing and information-driven technologies are central components of modern, advanced economies, and these technologies' importance is only growing. With its large and exceptionally productive Information sector tied to high-tech Manufacturing, the San Francisco EMA's strong ELGC points to the economy's foundational strengths, meaning an economy that produces more (and more desirable) goods and services for less input.

BUT ISN'T SAN FRANCISCO'S DOWNTOWN DYING?

News reports have detailed San Francisco's attempts to lure businesses back to downtown after the pandemic and the resulting shift to remote work left many storefronts vacant. The San Francisco Bay Area EMA extends far beyond downtown (and San Francisco's city limits), so economic activity that has migrated to San Jose, Silicon Valley or other locations within the city's economic orbit continue to make the Bay Area a GDP powerhouse.

Large EMAs tend to have many economic advantages over midsize cities, and the benefit of scale holds true for ELGC. That's because the largest and most lucrative players in the Finance and Real Estate, Information, and Manufacturing sectors are generally in or around the country's largest cities. Some midsize EMAs, however, buck this trend and boast large shares of their workforce employed in the most productive industries.

Omaha, NE, for one, is a midsize EMA yet is home to four Fortune 500 companies and deeply rooted finance and insurance industries that consistently outperform national averages. Its Finance and Real Estate sector employs 8% of its workforce and produces 27% of its GDP—each share about 33% greater than the national average. This beneficial industry composition helps Omaha to break into the top 10 in our ELGC rankings of the 100 midsize EMAs.

Migration and population growth

The trope "demographics is destiny" is commonly heard among political strategists, and yet an area's demographic composition is an even more potent indicator of its economic fortunes than it is any election outcome. For an economy to grow, it is helpful that its population grow and that its working age population remain at a healthy level. ELGC captures population's central importance to an EMA's economic expansion, as many metro areas that have some of the healthiest demographic trends tend to exhibit the strongest ELGC and largest engines of growth.

Nashville's strong ELGC ranks fourth among the 50 largest EMAs, in part because of the robust population growth it has sustained for decades. In 2023, the Nashville area grew by 26,582 people, or about 73 newcomers every day. The city ranks 11th in the nation in the average number of migrants (international and domestic) per 1,000 residents over the past decade, and it ranks fifth in population growth over the same period.

A national beacon for the music and entertainment industries, Nashville offers attractive amenities for newcomers of all ages. The droves of people moving to town are both leading and lagging indicators of a robust labor market: In a virtuous economic cycle, people come for the job opportunities while new entrants help to create jobs for others through the economic activity they generate. Middle Tennessee exhibited healthy job growth in 2023, with more than 17,000 new jobs.

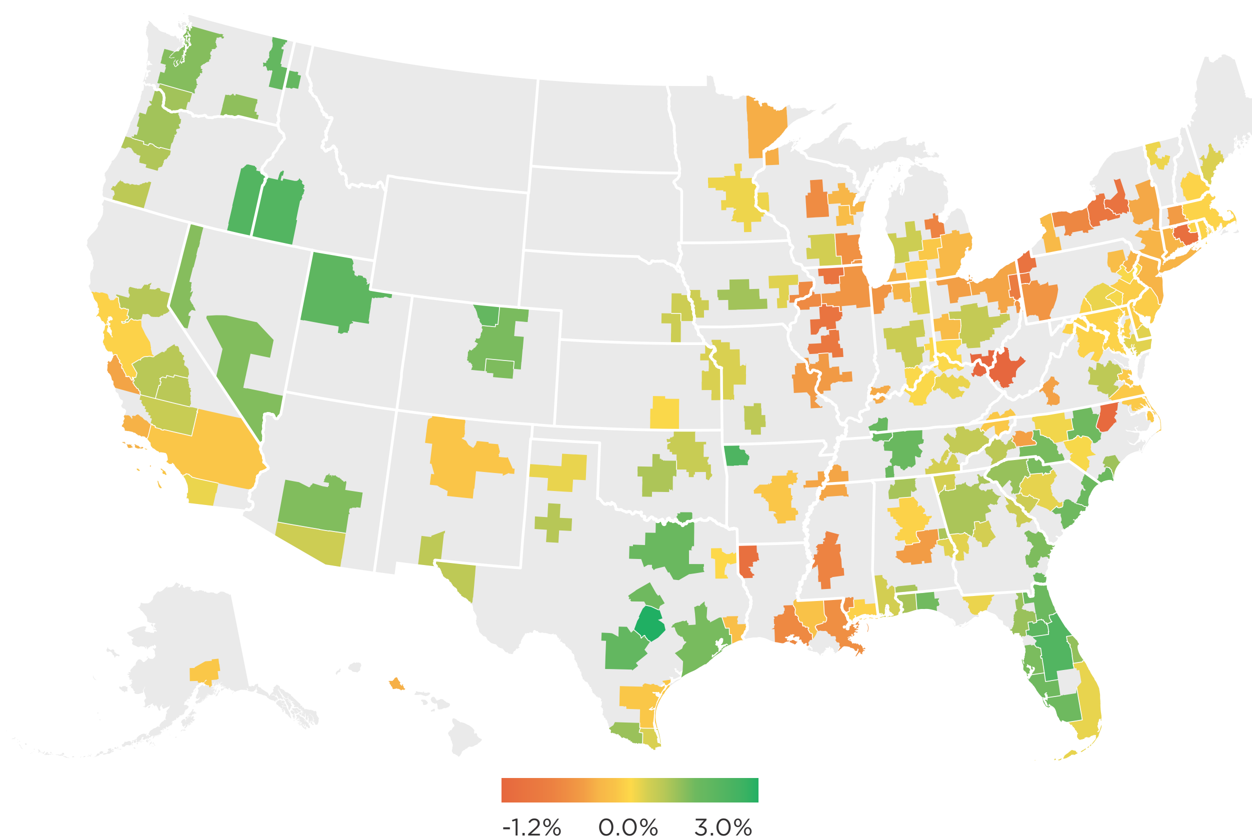
While the Nashville EMA offers a cheaper cost of living than many major economic hubs, like New York City or San Francisco, new arrivals are contributing to a recent rise in prices. This notably less virtuous cycle stems from the increased demand for housing and other goods and services brought about by the newcomers. While a growing base of human capital leads to strong ELGC and a robust engine of economic growth, an EMA's housing, transportation and other infrastructure must keep pace with the increasing population.

Skills

People are an economic engine's central components, yet not all human capital is equally valuable. A growing population will not translate to economic growth if that population is unable to perform productive work, and a workforce's productivity is commensurate with its skill level. These factors mean that workers must have the appropriate and necessary skills to be productive in a specific economy and sustain robust growth. Using educational attainment as a proxy for skill level, we observe how having a skilled workforce boosts an area's growth potential: EMAs with greater shares of highly educated workers tend to have strong ELGC.

Raleigh and Durham's robust ELGC ranks it fifth among the 50 largest EMAs, thanks in part to its skilled workforce, many of whom are prime age workers, and its rapid population growth. The region ranks 11th in the nation for share of workers with a bachelor's degree or higher and

10-Year (2013-2023) Growth of Prime Working-age Population



seventh in prime working age population growth over the past decade. These statistics mean that Raleigh and Durham has a large share of workers between the ages of 25 and 54 and that many of these workers are highly educated.

Essential to Raleigh and Durham's success is the area's ability to retain and attract highly skilled people. The area's four universities – North Carolina State University, Duke University, the University of North Carolina at Chapel Hill and North Carolina Central University – every year graduate thousands of skilled young people, creating a spring-fed pool of talent ready to begin careers in the Research Triangle's highly productive industries. This homegrown talent pipeline, combined with the EMA's affordable land, low corporate taxes and reliable infrastructure, attracts businesses to the area. Reflecting the area's strong ELGC, Raleigh and Durham's nurturing environment shows how the structural elements that contribute to a robust growth engine tend to build on themselves. As firms arrive, job opportunities grow and more skilled workers relocate to the Triangle, reinforcing the area's appeal for other corporations to commit to building campuses in the region.

What can be learned? What is replicable?

These cases of strong ELGC bode well for Nashville, Raleigh and Durham, Omaha and San Francisco, but are their success stories replicable? What can other cities learn from their examples? From Omaha and San Francisco, we glean that to nurture productive, resilient industries requires smart investment and long-term planning. ELGC pertains to structural economic factors, and changing an economy's structural elements does not happen overnight. Business and policy leaders aiming to optimize their economic productivity should invest in the most productive, forward-facing industries. Information is a prime example of a sector that produces a lot of output for a relatively small amount of input, one that creates synergies across sectors, and a group of industries primed for growth this century.

From Nashville as well as Raleigh and Durham, we can distill a message to cities everywhere: Be attractive, particularly to skilled young people. Keeping the cost of living down and providing amenities that appeal to the rising cohort of workers are fundamental ways to enhance an area's attractiveness. Housing constitutes a major expense for individuals and families, meaning that communities should prioritize policies that control housing costs. To

enhance their appeal, cities could also invest in attractive urban amenities, including cultural institutions (e.g., theaters and museums), dining and retail establishments, green spaces and transportation.

Who are the bottom performers?

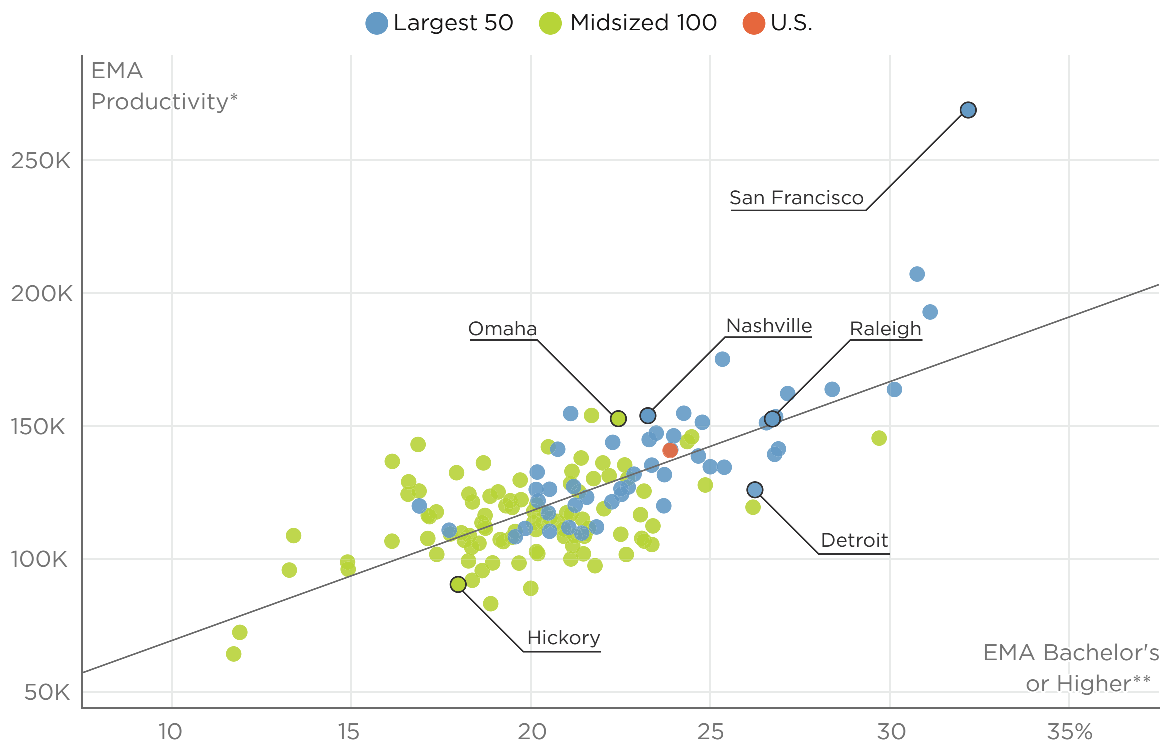
The EMAs with the weakest ELGC among their size cohort offer instructive cases that point to proposals for improving an area's long-term growth prospects. The EMAs with the least favorable ELGC often have employment shares weighted toward relatively low-output sectors, such as Leisure and Hospitality – industries that produce less than those in higher productivity sectors, even in times of full employment. Additionally, many of the weak ELGC EMAs are over reliant on a single industry, such as outdated modes of Manufacturing, which reduces their resiliency to cyclical downturns and macroeconomic headwinds. Low ELGC may also indicate problematic demographic compositions characterized by shrinking populations, low shares of working age adults, or a low-skilled workforce.

Ranked 96th in ELGC among the midsize 100 EMAs, Hickory, NC, shows how an aging population and a dearth of highly educated workers hinders an area's growth potential. Hickory's population has grown at a mere 0.1% annually over the past decade, which means that its population has aged faster than 88% of the EMAs in our sample. Over the same period, its prime working age population—those between the ages of 25 and 54—has shrunk by 0.5% annually. A compounding structural problem is that an outmoded Manufacturing sector dominates the area economy, employing 26% of its workers and accounting for nearly a quarter of its GDP in 2023. The area's Manufacturing productivity has declined by 1.2% annually over the past decade, and because the EMA's economy is so heavily reliant on Manufacturing, this weakening has dragged down the region's overall productivity growth, which ranks 78th out of the midsize 100 EMAs. Lack of educational attainment is another compounding issue for Hickory, as it ranks 84th out of 100 midsize EMAs in the share of its workforce with bachelor's degrees or higher.

An aging workforce that is lagging in educational attainment makes it difficult for Hickory to attract the high-productivity industry jobs that drive growth in other areas. The good news is that, with these structural ills diagnosed,

ELGC RANK	LARGEST 50 EMAS	ELGC RANK	MIDSIZE 100 EMAS
50	New Orleans, LA	100	Allentown, PA
49	Greensboro, NC	99	Rocky Mount, NC
48	Memphis, TN	98	McAllen, TX
47	Detroit, MI	97	Youngstown, OH
46	Virginia Beach, VA	96	Hickory, NC
45	Milwaukee, WI	95	Lafayette, LA
44	Cleveland, OH	94	Charleston, WV
43	St. Louis, MO	93	Corpus Christi, TX
42	Chicago, IL	92	Erie, PA
41	Birmingham, AL	91	Beaumont, TX

EMA Employment Share Of Bachelor's Degree Or Higher

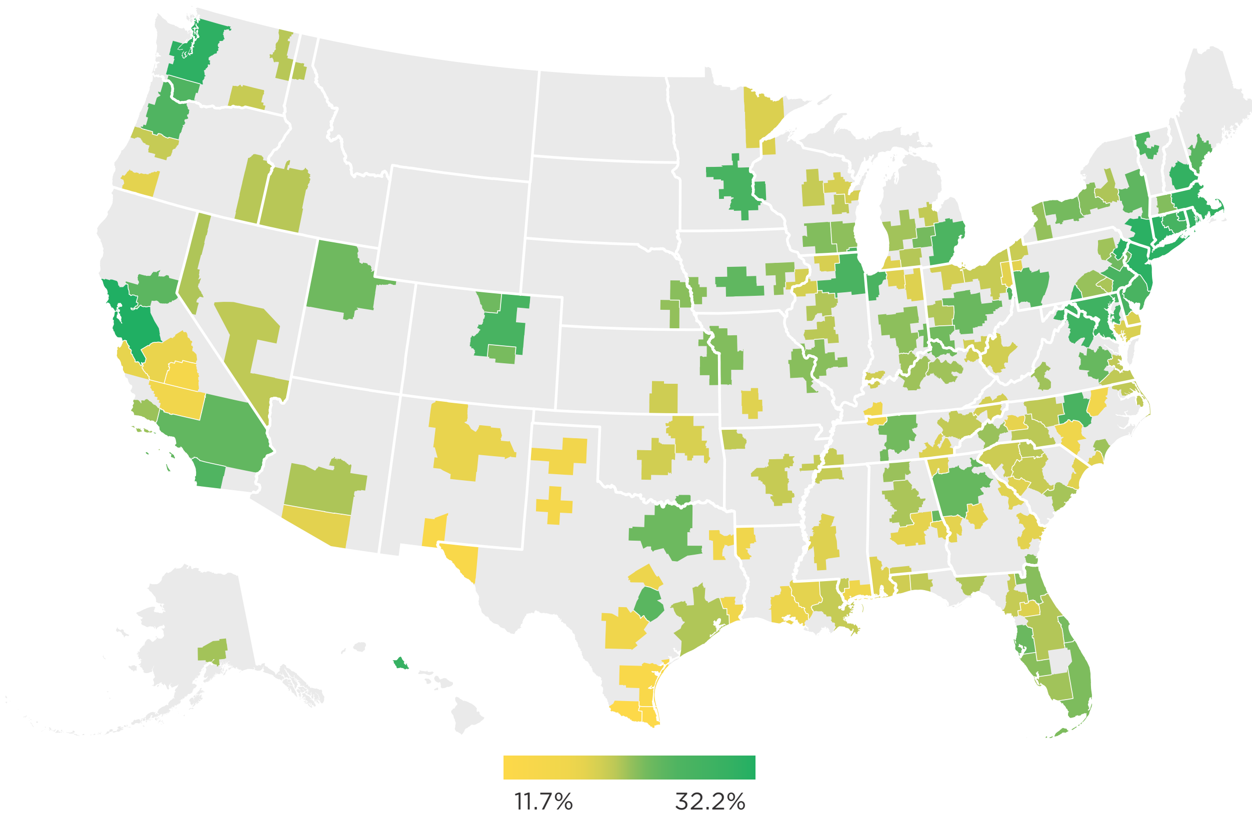


*Real GDP per employee **EMA employment share of bachelor's degree or higher

solutions can be prescribed. Investing in education and training programs would enhance workforce skill levels, and the rise of remote and hybrid work could help Hickory attract families looking to put down roots in a beautiful area that boasts a low cost of living. This sort of rebranding is a necessary step to improve the structural factors that contribute to long-term growth.

Like Hickory, the Detroit EMA's demographic woes over the past decade have weakened its ELGC, which ranks in the bottom five of the largest 50 EMAs. In this period, Detroit's population has remained flat, its pool of prime working age residents has shrunk, and the number of residents 65 or older has increased by over 200,000. Meanwhile, the area has experienced net negative domestic migration, losing annually about 4.5 people per 1,000, on average. Detroit's most important industry, the manufacturing of transportation equipment (cars and car parts), is responsible for three-quarters of the 26,000 new manufacturing jobs since 2014. Yet Manufacturing GDP has declined by $1.3 billion over the same period. This means that the EMA's Manufacturing sector productivity has dropped by almost 2% annually in the past decade. The productivity decline may result from retooling and the learning curve of moving toward manufacturing electric vehicles, which implies future productivity growth. Many of the high-productivity EV manufacturing jobs, however, have moved south as Detroit and the rest of Michigan have faced fierce competition with other Midwestern and Southern states to land new factories. Despite the domestic

Share of Employment with Bachelor's Degree or Higher



automobile industry's past struggles, Detroit's diversifying agglomeration of advanced manufacturers, its advantageous position as a primary gateway to Canada, and its collection of high-value capital all point to strengthening structural factors. These elements that portend a brighter future may not be reflected in ELGC, however, which is an empirical indicator based on data from years past.

In Detroit's case, we observe how demographic problems and an overreliance on one sector create structural issues that limit potential growth. Industry diversification is a key solution, yet building a diverse mix of advanced, future-focused industries is a slow and capital-intensive process, easier said than done. Structurally sound investments are those that anticipate industry trends, so that local businesses remain flexible and can meet market demands in the near and medium term. Structural problems, like an aging workforce and antiquated industry mix, can only be remedied stepwise with long-term planning and investment – local leaders must think generationally and at a human scale. What economy do we want 10, 20 or 30 years from now? What sort of community do young professionals want to make their home? This project aims to help answer these sorts of questions, and ELGC is a useful tool in this process.

To learn more about Embedded Local Growth Characteristics and discover the power of our regional economic indicators for 150 US EMAs, visit empoweringamericancities.com.

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