

# **The Impact of Taxes and Incentives on the Inward Investment Performance of US States**

**Results of a study by Dr. Henry Loewendahl**

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- **ICA Incentives** database of over 7,000 foreign and domestic incentives deals in the USA with a total incentives value of \$50 billion from 2010-Sept. 2013. After removing outliers and small sample sizes, the average incentive per job created in US states was \$20,000 over the period
- **fDi Markets** database of over 27,000 FDI and inter-state greenfield investment projects tracked in the USA from 2003-July 2013. These projects have created an estimated 1.2 million new jobs and 5,600+ investment motives have been recorded for these projects
- The **2013 State Business Tax Climate Index** from the Tax Foundation

# **How important are taxes & incentives in location decision making?**

**EVIDENCE FROM OVER 3,000 COMPANIES  
INVESTING IN THE USA**

## Motives for FDI and inter-state investments in USA

Motive	Projects	% of Projects
Skilled workforce availability	438	33.2%
Proximity to markets or customers	387	29.3%
Regulations or business climate	276	20.9%
IPA or Govt support	273	20.7%
Domestic Market Growth Potential	228	17.3%
Infrastructure and logistics	208	15.8%
Finance Incentives or Taxes or Funding	157	11.9%
Lower Costs	112	8.5%
Attractiveness / Quality of Life	68	5.2%
Industry Cluster / Critical Mass	67	5.1%
Other Motive	208	15.8%

## Motives for FDI and inter-state investments in USA

Motive	Projects	% of Projects
Proximity to markets or customers	203	34.3%
Skilled workforce availability	189	32%
Regulations or business climate	107	18.1%
Domestic Market Growth Potential	103	17.4%
Infrastructure and logistics	99	16.8%
Industry Cluster / Critical Mass	94	15.9%
Attractiveness / Quality of Life	70	11.8%
IPA or Govt support	63	10.7%
Lower Costs	46	7.8%
Finance Incentives or Taxes or Funding	45	7.6%
Other Motive	121	20.5%

## Motives for FDI and inter-state investments in USA

Motive	Projects	% of Projects
Skilled workforce availability	175	79.5%
IPA or Govt support	42	19.1%
Attractiveness / Quality of Life	37	16.8%
Regulations or business climate	37	16.8%
Proximity to markets or customers	20	9.1%
Facilities Site or Real Estate	19	8.6%
Domestic Market Growth Potential	17	7.7%
Infrastructure and logistics	16	7.3%
Finance Incentives or Taxes or Funding	14	6.4%
Lower Costs	14	6.4%
Other Motive	34	15.4%

## Motives for FDI and inter-state investments in USA

Motive	Projects	% of Projects
Skilled workforce availability	159	50.1%
Proximity to markets or customers	74	23.3%
Industry Cluster / Critical Mass	58	18.3%
Universities or researchers	49	15.4%
Technology or Innovation	35	11%
Regulations or business climate	29	9.1%
Domestic Market Growth Potential	27	8.5%
Attractiveness / Quality of Life	26	8.2%
Presence of Suppliers or JV Partners	21	6.6%
IPA or Govt support	21	6.6%
Other Motive	57	18%

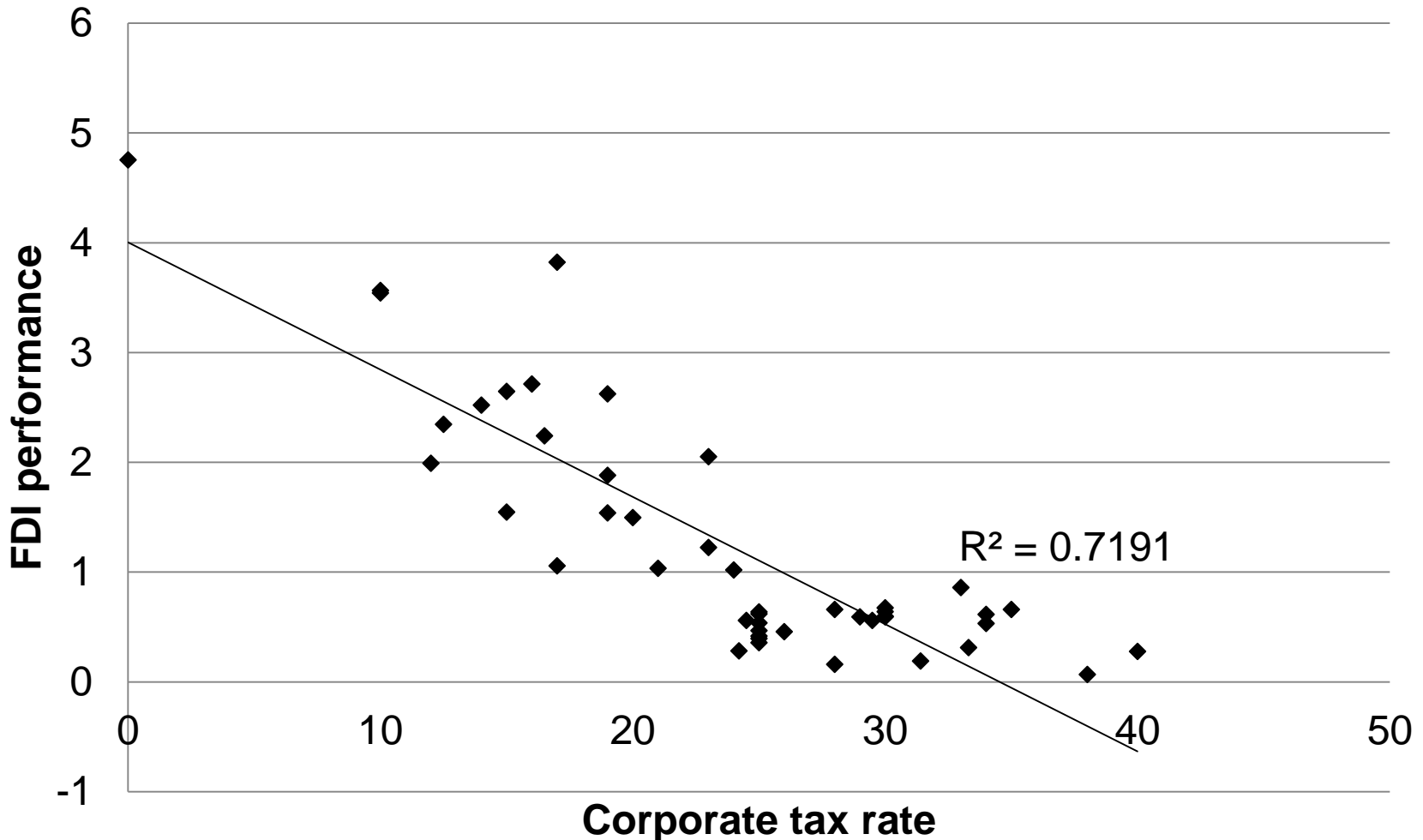
- Overall, taxes & incentives rank the 8<sup>th</sup> most important location determinant for FDI and inter-state investment in the USA
- Taxes and incentives are most important for Manufacturing projects and least important for R&D projects
- Markets and skills dominate as the most important location determinants
- Over time, incentives have become less important
- Since 2012, Technology & Innovation and Universities/Researchers have become more important than Taxes and Incentives
- Incentives are slightly more important for foreign investment than for domestic investors



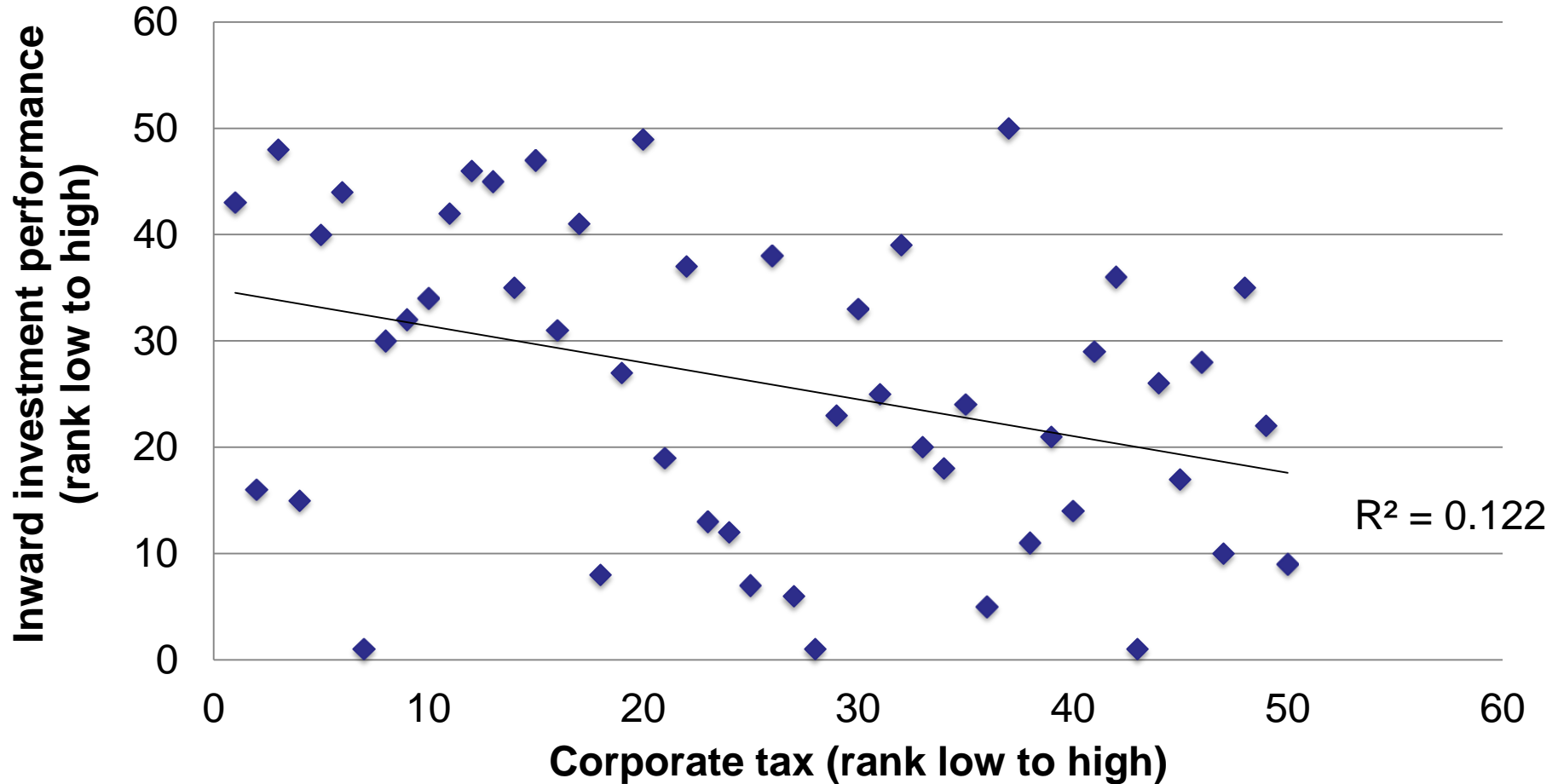
# **Impact of taxes and incentives on inward investment performance**

**statistical evidence**

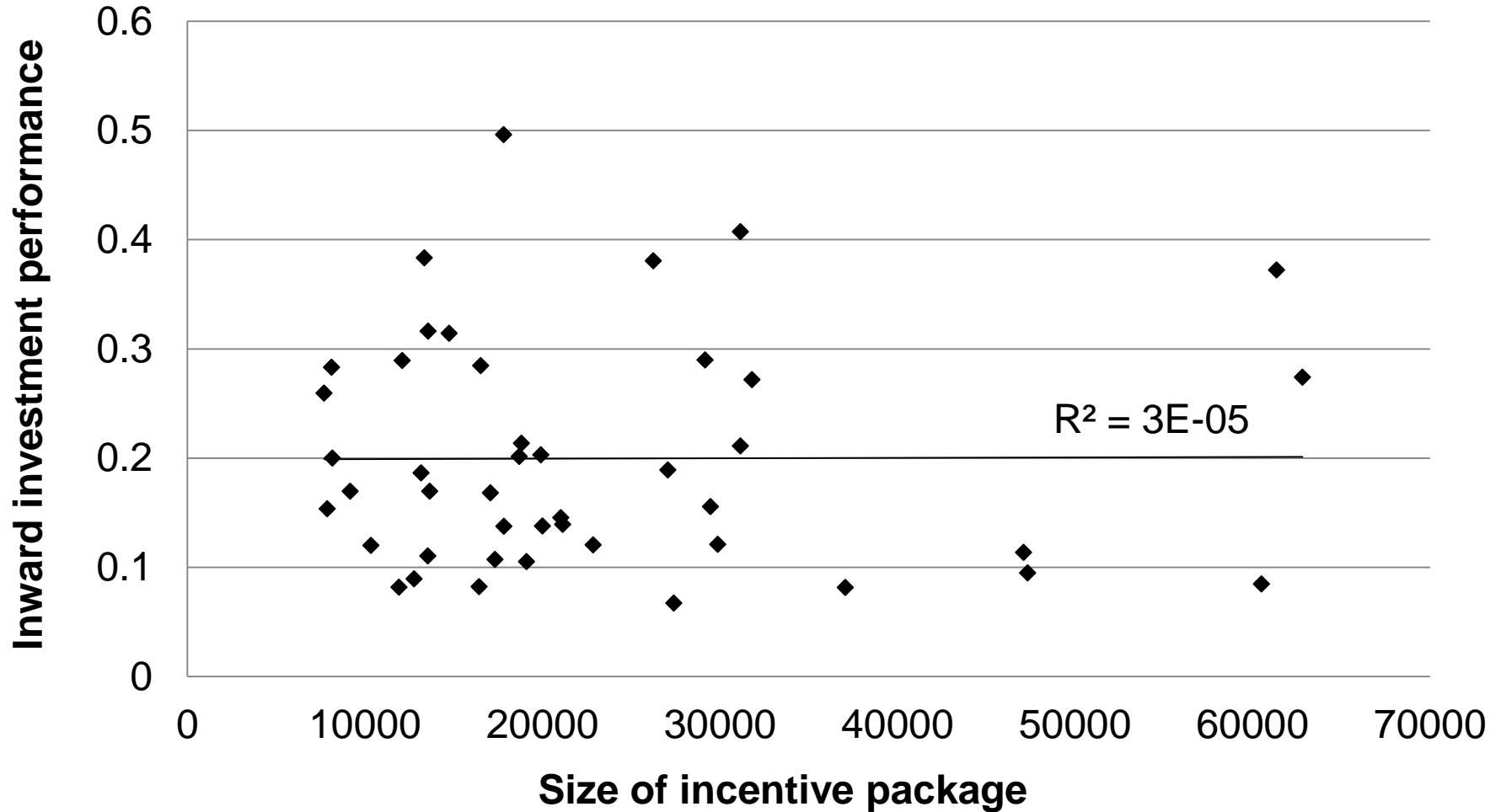
## Corporate tax and FDI performance at the country level



## Corporate tax and inward investment performance of US states

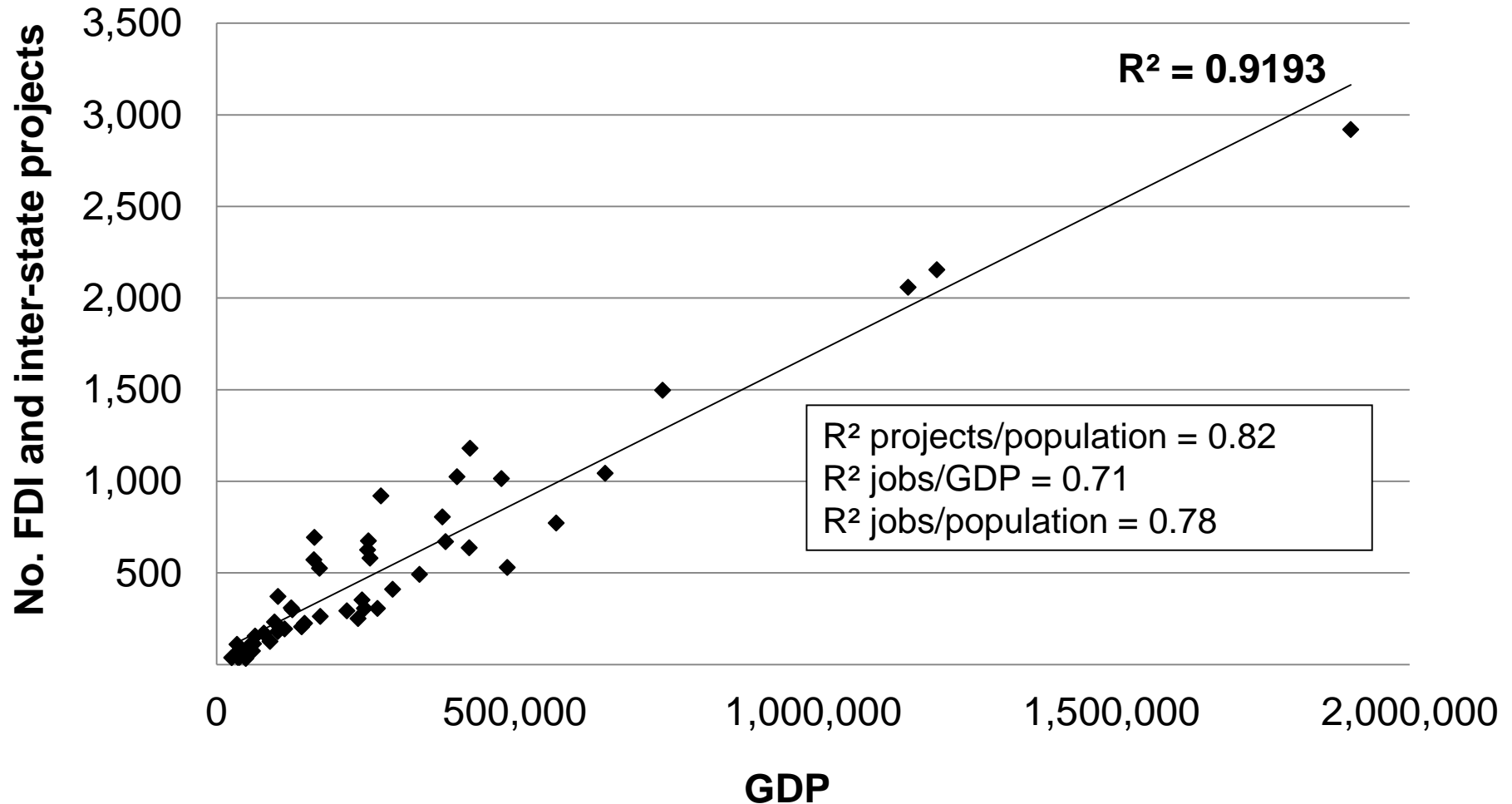


## Incentives and inward investment performance

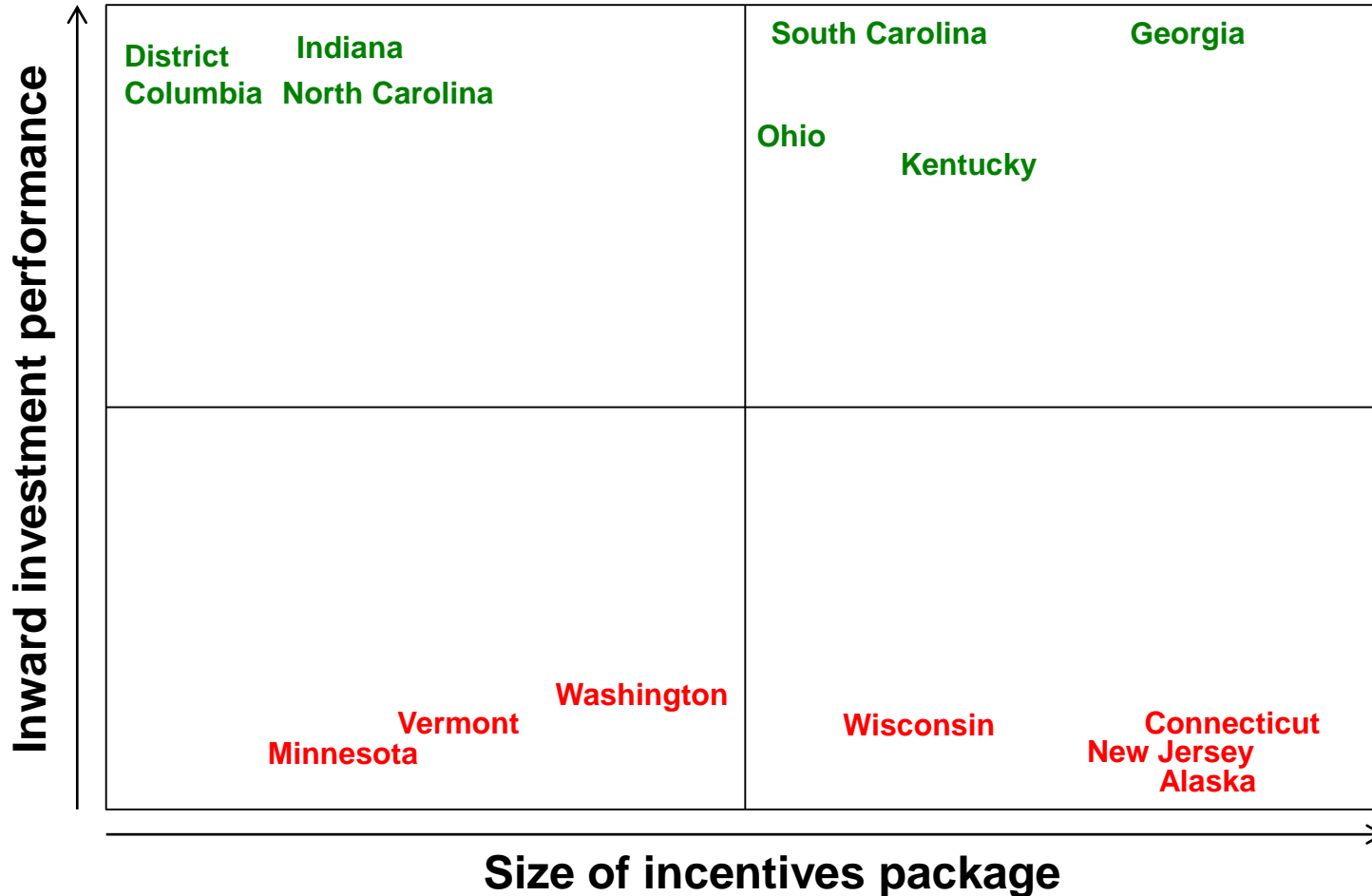


Source: ICA Incentives and fDi Markets. Inward investment performance shows no. of jobs from FDI + Inter-state projects relative to size of GDP (per \$m GDP). Size of incentive package is \$ incentives per job created

## Inward investment Projects and GDP of US States



**Incentive levels in top 7 best performing inward investment states and 7 worst performing states**



Source: ICA Incentives and fDi Markets. Inward investment performance is no. projects attracted relative to size of population and GDP. Size of incentives package is \$ incentives per job created

# Conclusions and implications



- The evidence presented shows that taxes and incentives are important for investors, but are certainly not the critical drivers
- Inward investment is driven by access to markets, labor skills and increasingly to access technology/innovation rather than incentives. Indeed, quality of life is often higher ranked than incentives by investors
- The country level evidence clearly shows that FDI performance is influenced by corporate tax – which is one key explanation why the FDI performance of the USA is weak; the US has the highest corporate tax in the developed world
- But at the state level there appears to be no statistical link between corporate tax and size of incentives package and inward investment performance
- This maybe because so many states offer tax and other financial incentives that they do not significantly influence location but in their absence investors may, in some cases, invest elsewhere





- Examining the best and worst performing states shows that some of the best performing states also offer large incentives packages, indicating that incentives can be very effective
- On the other hand, some of worst performing states also offer amongst the largest incentives packages, suggesting that incentives are not effective in compensating for underlying weakness in attracting inward investment
- This study adopted unique data available on FDI performance and investment motives from fDi Intelligence and incentives packages from ICA Incentives
- More concrete research is needed to examine:
  - Incentives at a sector level and how this impacts performance
  - The impact over time of a new incentives regime on performance
  - Empirical models for location determinants using data now available
  - Concrete case study research on specific locations which are over and under performing and the role of incentives in their performance

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