

Self-Employment in Rural America: The New Economic Reality

By Stephan J. Goetz

In Brief...

The Situation:

- Since 1969, the number of self-employed rural workers has expanded by over 160 percent to 5.6 million. In comparison, there was only a 64 percent growth in rural wage and salary workers over the same time period.
- If current trends continue, one rural worker will be self-employed for every three wage-and-salary workers by 2015.
- In the last four years, self-employment earnings relative to earnings of traditional workers have reached historic lows. In 2005, the average self-employed worker earned only one-half of what wage-and-salary employees captured (\$16,851 versus \$31,596).
- There are several factors that have bearing on both the rates and earnings associated with self-employment. These factors can be classified into two major categories: (1) characteristics of the population pool from which the self-employed are drawn; and (2) community-level attributes that help assist, or serve as barriers, to the self-employed.

Policy Options:

- Individual entrepreneurs and the self-employed must rely on the availability of auxiliary supporting businesses to operate efficiently and profitably. Often, these supportive services are not available. Strategic temporary public investments may be needed and justified to help facilitate the development of these key services in some rural areas (such as temporary help, daycare, courier/messenger, legal and accounting services, and office supply businesses).
- Self-employed persons need better access to higher-education institutions (i.e., business schools, community colleges, land-grant institutions) that offer specialized entrepreneurship and business training. New ways to deliver programs and technical assistance to current and potential entrepreneurs/self-employed must be encouraged.
- State and local governments should explicitly recognize the growing importance of self-employed workers, especially in rural areas. Since state governments only keep track of workers who are covered by unemployment insurance (the so called ES-202 information), they have little knowledge of how their policies affect a growing segment of the labor force. As such, state governments are urged to take an important first step in collecting and reporting basic economic data on this expanding sector of their economies.

Self-employment is the new reality for a growing segment of the U.S. labor force, and more so in rural than in urban areas. Although self-employment potentially holds many opportunities for rural economies, earnings of the rural self-employed lag significantly and increasingly behind those of traditional workers. Without more coordinated supports and policy intervention, an economy built on self-employment may threaten a middle-class way of life.

In the mostly rural, natural resource-based industries, labor-saving technology – coupled with globalization in a flattened world – are causing tremendous upheaval. At the forefront of this new international economy, corporations such as Wal-Mart are squeezing labor resources and inefficiencies out of the global value chain, causing rural factories to close and relocate, while delivering goods at the lowest possible cost to consumers. On the up side, these same forces are creating incredible opportunities for small, footloose firms and individual entrepreneurs. As partial evidence of this, the number of self-employed in rural areas has doubled since the 1980s. In addition, the presence of self-employed workers and small businesses can help to raise wage-and-salary

employment; thus, the self-employed are important engines of economic growth in their own right.¹

This remarkable spread of self-employment has important implications for elected leaders, ranging from immigration policy to health insurance, education, broadband, and technology policy to welfare reform. Because self-employment earnings lag significantly behind earnings in wage and salary jobs, public policymakers face a critical opportunity to raise the productivity of the self-employed. This article offers a snapshot of how self-employment is playing out in different locales across the country, with particular focus on rural areas. It documents the numbers of self-employed and their wages relative to standard wage and salary workers. The results underscore the importance of regional and local distinctions that create or inhibit self-employment and related returns to that employment. The brief concludes with key directions for policymakers in supporting and advancing local self-employment.

Rural Self-Employment is Booming . . .

The number of rural residents who are self-employed has doubled in the last three decades.

Self-Employment Defined

The terms entrepreneurship and self-employment are often used interchangeably, even though they are not necessarily identical phenomena. The reason for this is that we do not have better data on entrepreneurs. Entrepreneurs in this article are those who file their income taxes as proprietors or independent business owners. This can include anyone from insurance agents to loggers, hair-dressers, construction workers, financial and legal advisers and small independent “mom-and-pop” store retailers.

The analysis is based on IRS Schedule C, Form 1024 income tax filings by non-farm proprietors or self-employed workers, compiled for each county by the Bureau of Economic Analysis (Regional Economic Information System). These self-employment data do not allow us to distinguish between more highly-skilled workers (such as lawyers or “lone-eagle” technology workers) and less-skilled workers such as those providing hair dressing and lawn mowing or snow removal services.

Today, 5.66 million rural workers are self-employed full- or part-time (this number includes only non-farm self-employed), a 160 percent increase since 1969. In comparison, the number of full- and part-time rural wage-and-salary workers overall grew by only 64 percent, to 19.8 million workers in 2006 (see Figure 1).²

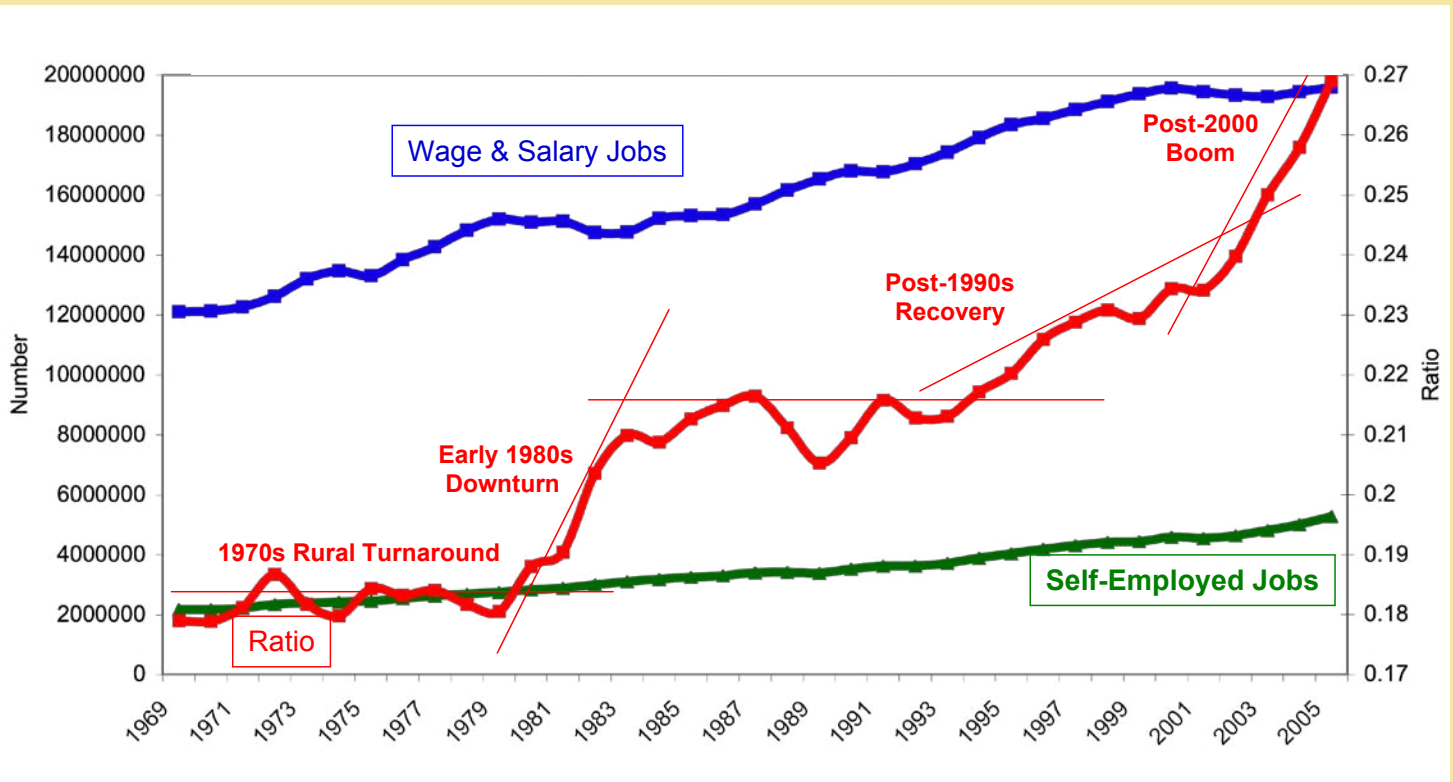
While the wage-and-salary job numbers by definition closely track the national business cycle, declining or stagnating during recessions, the number of self-employed workers has shrunk in only two of the 36 years shown in Figure 1: in 1989 and in 2001. On average, 81,500 new rural self-employment jobs were created each year over this period, with a higher number in more recent history. In comparison, rural wage-and-salary jobs on average increased by 210,000 net new jobs each year over this period.

As a result of these trends, the ratio of rural self-employed to wage-and-salary workers has increased sharply, from 18 to 27 percent between 1969 and 2005. The relative rise in

self-employment is especially pronounced since 2000, but similar surges occurred in the early 1980s. These trends explain the popularity of books such as Paul and Sarah Edwards' *Secrets of Self-Employment* (Tarcher Press, 1996); Daniel Pink's *Free Agent Nation* (Warner Business Books, 2001), and Louis Uchitelle's *The Disposable American* (Knopf, 2006). If recent trends continue, one rural worker will be self-employed for every three wage-and-salary workers by 2015.

During the most recent economic upturn, proportionately more workers were seeking self-employment than wage and salary jobs. We do not know to what extent this reflects a lack of wage-and-salary employment opportunities or the pursuit of new opportunities in self-employment because the data are not strong enough to make this assessment. The fact that returns to self-employment continue to fall relative to those in wage-and-salary employment (see below), suggests that more people are being forced into self-employment rather than doing so voluntarily.

Figure 1: Trends in Rural Wage-and-Salary vs. Self-Employment Jobs, and Ratio of Self-Employed to Wage-and-Salary Workers, 1969-2005.

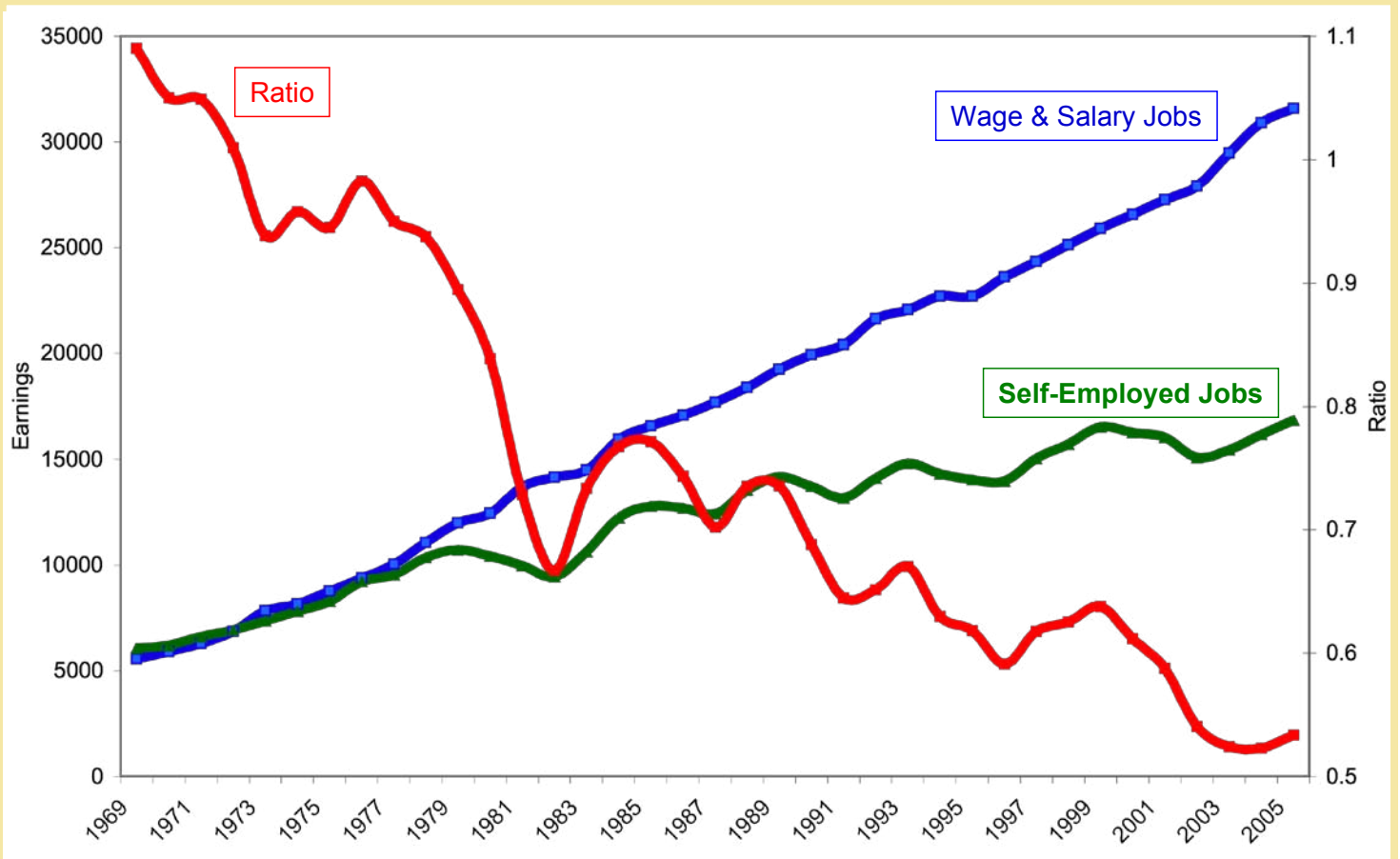


During the 1970s “rural renaissance” (when rural areas saw a remarkable influx of residents, including many return-migrants who had left earlier when rural economic opportunities were scarce), self-employment and wage-and-salary jobs expanded at about the same rate, and the ratio of these two employment types remained the same (Figure 1). During the 1980s downturn, wage-and-salary jobs declined more rapidly (or grew less rapidly) than the number of self-employed, sharply increasing the ratio of the self-employed to traditional workers. Likewise, in the post-2000 boom, self-employment accelerated more rapidly than wage-and-salary jobs. This could reflect more self-employment possibilities or fewer wage-and-salary opportunities, or both, whereas in the earlier expansions wage-and-salary employment growth tended to go hand in hand with self-employment growth.

... But Wages are Lagging

Although more people are turning to self-employment in rural areas, their wages are not keeping up with those of wage and salary workers. Bureau of Economic Analysis data show that the returns to rural self-employment, or earnings per proprietor, lag far behind the returns to rural wage-and-salary employment (Figure 2). These earnings data are nominal, which means they have not been adjusted for inflation. In 1969, the average self-employed worker earned \$6,071, whereas the average wage-and-salary job paid \$5,569 (a ratio of 109 percent). By 2005, the average self-employed worker earned about one-half that of the average wage-and salary worker: \$16,851 versus \$31,596.

Figure 2: Trends in Rural Nominal Earnings per Job: Wage-and-Salary vs. Self-Employment, and Ratio, 1969-2005.

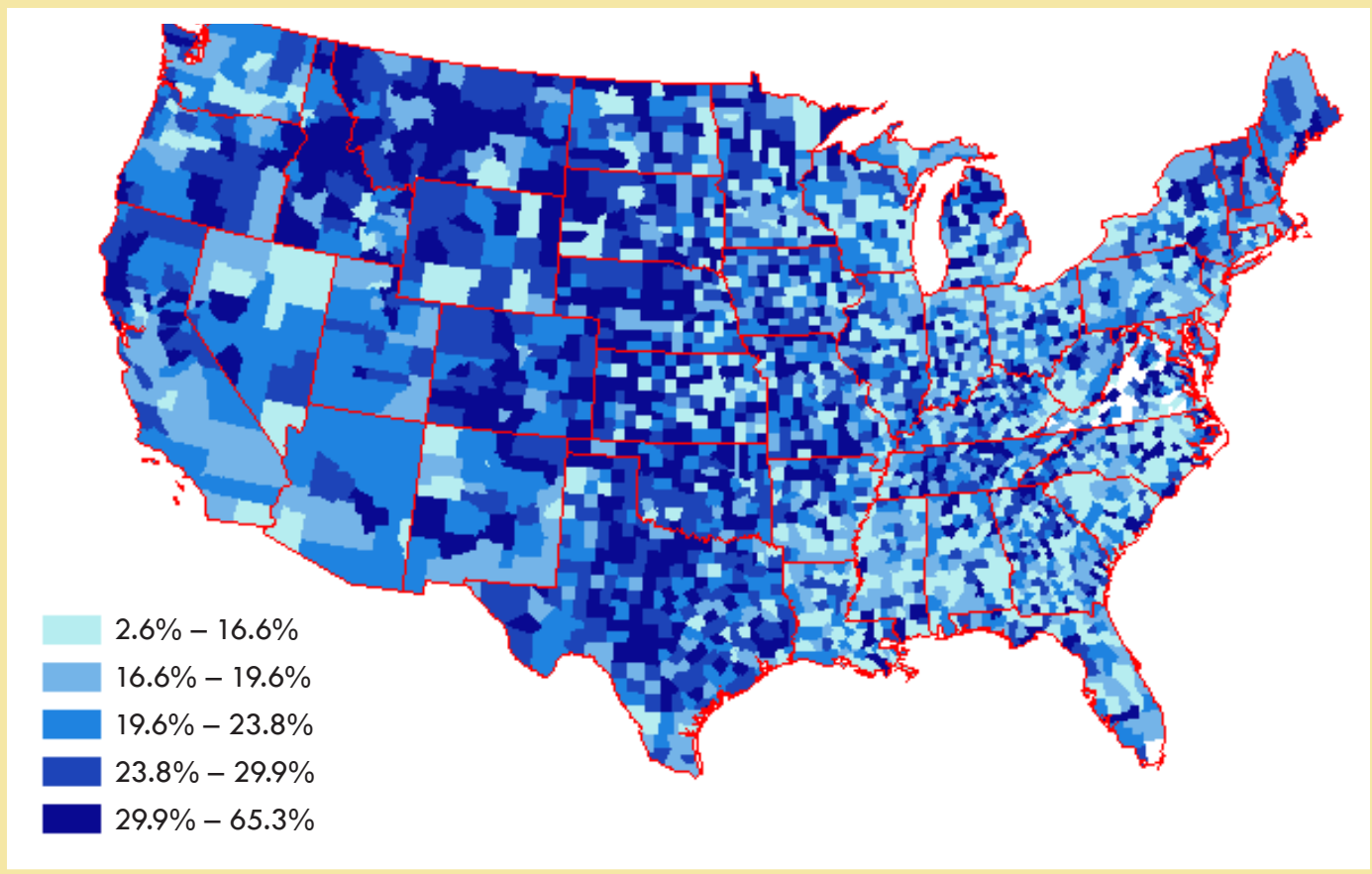


The ratio of returns to self-employment first started to lag significantly behind wage-and-salary earnings in 1978, just as self-employment made its first surge against wage-and-salary work (the red line in Figure 2 represents the ratio of earnings per self-employed to earnings per wage-and-salary worker). The ratio of the two series is not affected by inflation: it shows the “real” value of a self-employed worker versus a wage-and-salary worker. In the last four years, self-employment earnings relative to earnings of traditional workers have reached historic lows. Better data than those currently available are needed to examine whether these differences are due to part-time vs. full-time employment differences or linked to underreporting of self-employment income.

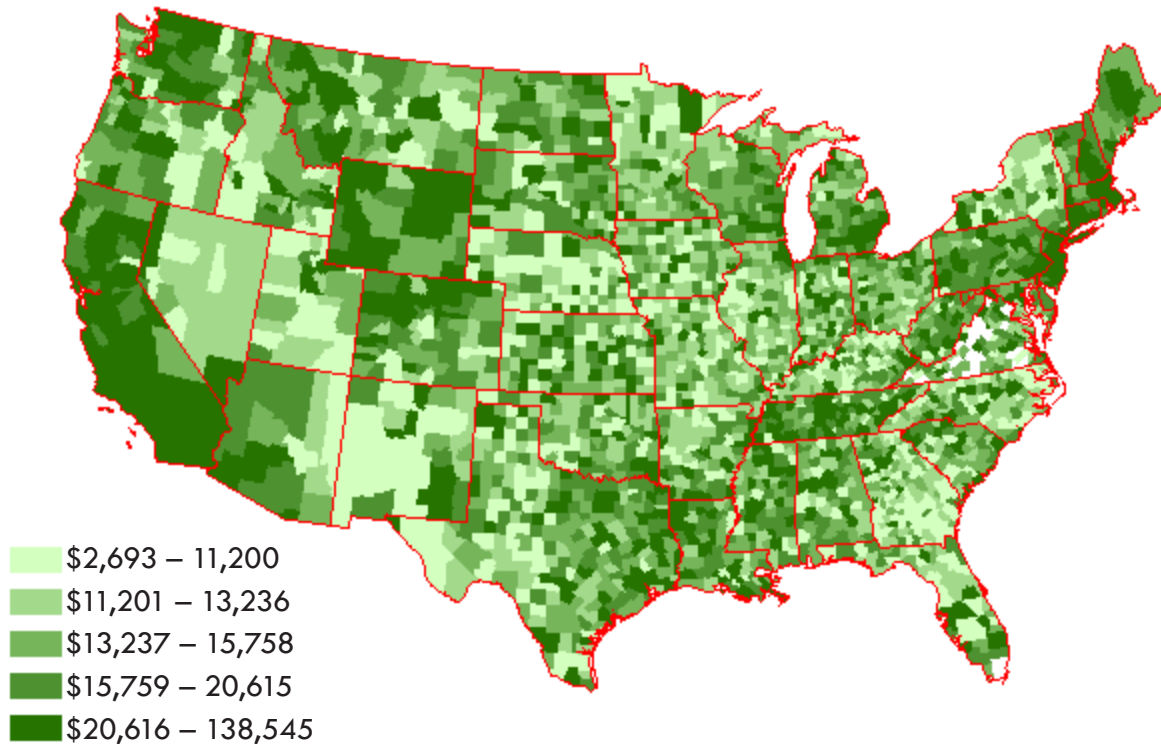
The Country’s Midsection Relies More on Self-Employment, But Higher Pay is on the Coasts

Maps 1 and 2 show the shares of self-employed workers in 2004 and the average returns to self-employment in 2004. Each color category contains 20 percent of the observations. For example, between 29.9 and 65.3 percent of all workers are self-employed in the counties shaded in the darkest blue. The nation’s midsection clearly relies more on (non-farm) self-employment than do other areas of the nation. This may reflect a culture of self-made individuals working for themselves, and it also shows that those who want to work for themselves can do so in remote, nonmetro areas. Furthermore, it is noteworthy that these counties tend not to occur in isolation but are “clustered” together.

Map 1: Self-Employment Shares, Non-Farm Workers, 2004 [Quintiles].



Map 2: Self-Employment Returns, Non-Farm Workers, 2004 [Quintiles].



Higher earnings, however, go to those on the coasts, parts of southern Michigan, and much of the South (except in Georgia and Florida) (see Map 2). Although not universally true, the higher returns are in metro counties. Low returns are clustered in Georgia and Nebraska as well as portions of the Intermountain West (see Maps 3 and 4). These areas offer higher incomes because of agglomeration economies (which produce economies of scale and strong networks) but also higher costs of living. To some extent, these higher costs of living will offset the higher earnings in “real” terms, but it is very likely that the greater population densities in metro areas also allow the self-employed to enjoy greater productivity and, therefore, higher earnings even after factoring in the higher costs of living.

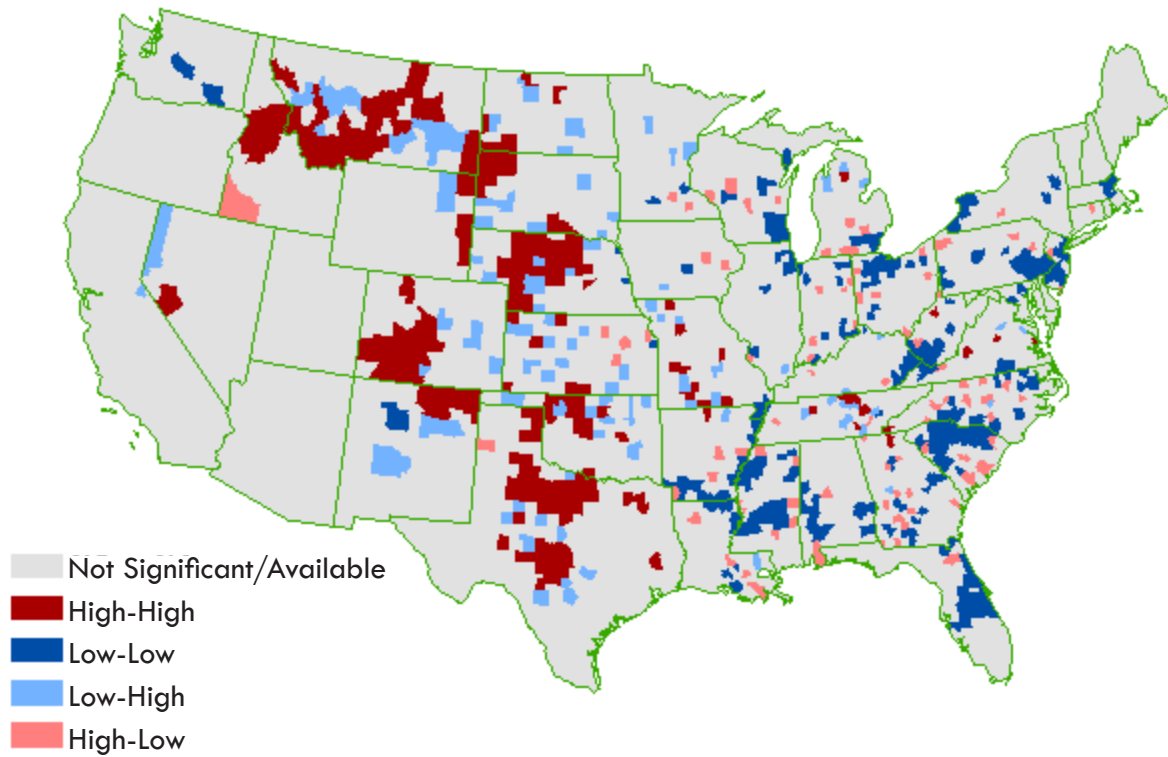
Meigs County, Tennessee, led all other U.S. counties in 2004 with 185 self-employed workers for every 100 wage-and-salary workers (a ratio of 1.85). That is, there are nearly twice as many self-employed as wage and salary workers in the county. According to Professor Fisseha Tegegne of Tennessee State University, self-employment in this county

includes wood working, trucking, pottery, carpentry, brickwork and in-house auto repair, in addition to tourism-related businesses. These workers may also include self-employed individuals in the music industry. Meigs County has lost its garment manufacturing base, has few public sector jobs, and has experienced considerable population exodus.

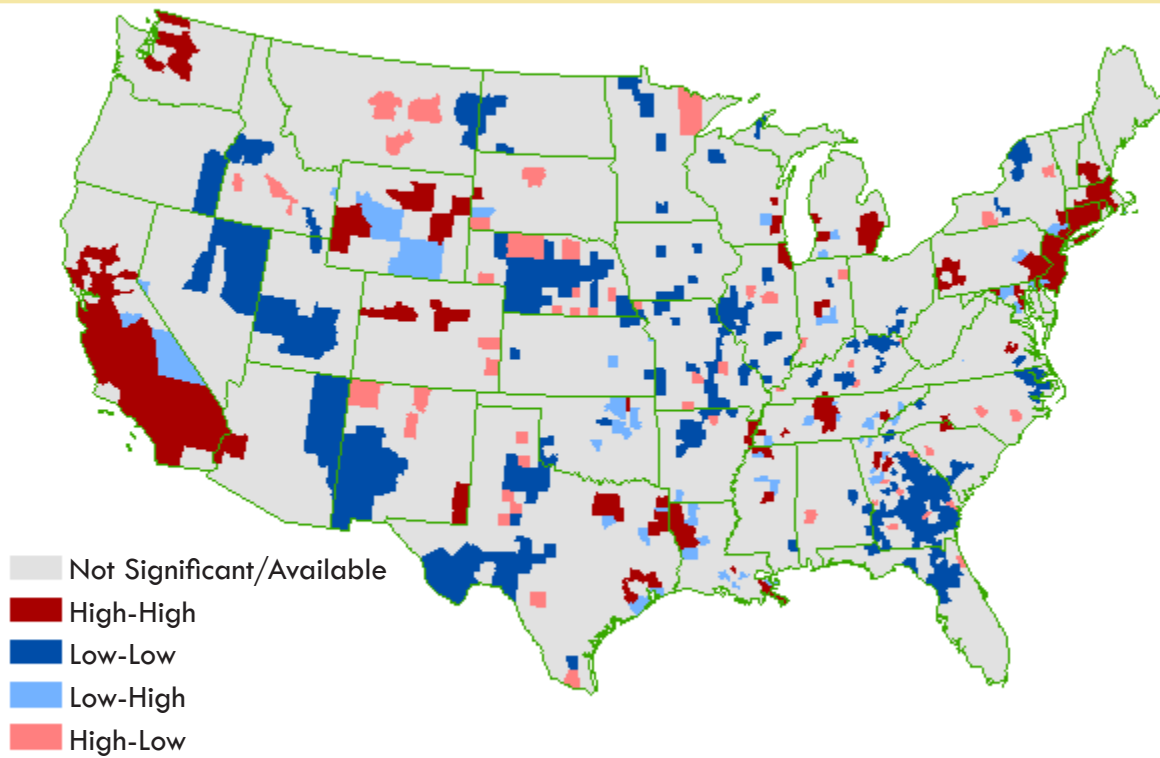
The county with the fewest self-employed is Tunica County, Mississippi, with only 2.5 self-employed workers for every 100 wage-and-salary employees. Tunica County saw the largest drops in poverty of all nonmetro counties in the 1990s, largely because of a booming gaming industry. The fact that a drop in poverty rates coincided with low ratios of self-employed is consistent with the low returns to self-employed as noted above.

The highest average earnings per self-employed worker in 2004 were in New York County, New York, at \$138,545, followed by \$87,491 in Harris County, Texas, and \$85,119 in Denver County, Colorado. The lowest earnings were in Flagler County, Florida, with \$2,693 (down

Map 3: Hot and Cold Spots for Clusters of Self-Employment Shares, 2004.^{6*}



Map 4: Hot and Cold Spots for Clusters of Self-Employment Earnings, 2004.^{6*}



*See Endnote 6 for more information on Maps 3 and 4.

from one of the highest returns in 1969, with \$11,169); Twiggs County, Georgia, with \$2,918; and McPherson County, Nebraska, with \$3,100.

Self-Employment Rates and Returns Vary for Different Reasons

There are a variety of items that have important bearing on both the rates and earnings associated with self-employment. Those factors that we found to be most significant – either in a positive or negative way – are outlined in Table 1.³ We find, not surprisingly, that higher risks deter self-employment while higher self-employment pay relative to wage-and-salary employment tends to promote the growth of self-employed persons.

It is useful to separate the factors into two categories: (1) characteristics of the population pool from which the self-employed are drawn; and (2) community-level factors or resources that are available to assist the self-employed. Here is a snapshot of some of our key findings:

- **Age:** Greater life and work experience of the population, as measured by age, is important. In preliminary research, we found that the returns (in earnings) to self-employment are higher in communities with an older or more experienced population (up to 37 years of age on average).
- **Education:** Shares of college graduates in a community are less important than shares of high school graduates in stimulating self-employment growth.
- **Foreign-Born Population Shares:** Counties with larger foreign-born populations and greater ethnic diversity have higher rates of self-employment, but higher foreign-born shares are associated with lower earnings from self-employment.
- **Access to Credit or Collateral:** Such access is critical if self-employment rates are to increase. Access to credit does not appear to affect the returns to self-employment, however.

- **Unemployment Rates:** The effect of the local unemployment rate is noteworthy in that a rising unemployment rate initially increases the number of self-employed, as might be expected, but eventually has the opposite effect as local economic conditions deteriorate to such an extent that self-employment disappears.
- **Temporary Help and Daycare Services:** In communities with more temporary help and daycare services workers, both the returns to self-employment and shares of self-employed workers are greater.⁴
- **Couriers and Messenger Services, and Office Supply and Stationary Stores:** These kinds of business support services help to raise the earnings of the self-employed, but they do not affect the rates or shares of self-employment.
- **Junior Colleges, Business Schools and Computer and Management Training establishments, and Technical and Trade Schools** are associated with higher returns to self-employment, presumably because they increase the skill sets of these workers. However, only technical and trade schools are also associated with higher self-employment rates.
- **State Policies:** The smaller the degree of state intervention in the economy, in terms of labor market and other regulations, and tax policy, the greater is the share of individuals who are self-employed.
- **Big-Box Stores:** These kinds of stores tend to reduce self-employment rates but they also are associated with higher returns to self-employment, as predicted by economist Joseph Schumpeter.
- **The Presence of Broadband Services** (or ISPs) tends to be associated with higher returns to self-employment, but does not affect the rate at which individuals are self-employed.

Clearly, both the characteristics of individuals and the features of the communities in which they live

Table 1: Key Factors Impacting Self-Employment Rates and Earnings in Rural Areas.

Variable	Shares or Rates	Earnings
Age or experience	+	+
Foreign-born population	+	-
Access to credit	+	
Temporary help services	+	+
Couriers and messenger services		+
Office supply and stationary stores		+
Daycare services	+	+
Junior colleges, business schools, computer and management training		+
Technical and trade schools	+	+
Pro-business state policies	+	<i>nd</i>
<i>nd = Not Determined</i>		

make a difference in terms of self-employment rates and success – as measured by the earnings of the self-employed. Given our findings on age – that communities with more workers in their later twenties and thirties have larger returns to self-employment – a graying rural population does not bode well for future growth in rural self-employment.

The results also suggest that the ability to outsource certain business functions through temporary help agencies may be critical to raising the returns to self-employment because it allows the self-employed to focus on their core activities. This may cause problems for rural areas since it highlights a basic chicken-and-egg situation; no one provides (supplies) to these business services because the demand for the services is not articulated or perceived to be present, and the demand for these services is not there because no one is supplying the services. For example, an entrepreneur with a good idea may fail to start a new business because there is no small business tax accountant in a community. But, there is no such tax accountant in the community because there are no small businesses seeking these services. This represents a basic coordination or market failure

Temporary help and child day care services are associated with both higher rates of self-employment and greater returns. Lack of child care is not typically viewed as a limitation to expanding

entrepreneurship, but it may warrant greater attention both as a constraint to and opportunity for self-employment.⁵ An opportunity exists for expanding the roles of colleges, universities and professional schools in stimulating local rates of and returns to entrepreneurship or self-employment. More specifically, we find that the self-employed respond positively to higher earnings opportunities, and educational institutions are positioned to help improve the skills and business savvy of individuals who find themselves laid off from regular wage-and-salary employment.

Of particular interest for rural areas, our results reveal that rural areas and places with more natural resource amenities have significantly higher rates of self-employment growth over time than do metro areas or areas with fewer such amenities. To the extent that self-employment is the new workforce reality, this may be a positive development. Our research also shows that state-level public policy exerts a significant influence on self-employment growth rates over time. In particular, in states with less heavy-handed government involvement and intervention in the economy in terms of taxation and regulations, self-employment rates are rising more rapidly over time. Even so, state government has a potentially important role of removing barriers to entry into self-employment, for example, by addressing constraints to the

growth of the various businesses and educational institutions mentioned above, so long as such intervention leads to the creation of public goods.

Policy Implications

Human beings do not live by their economic relationships alone and there is growing recognition of the profound value of trust, social networks and interpersonal relations to individuals' success in the economic sphere. The 2007 Kauffman Prize Medal for Distinguished Research in Entrepreneurship was awarded to Professor Toby Stuart for his seminal research on the productivity-enhancing effects of successful social networking on entrepreneurship. It is less clear, however, what role the government or public sector can and should play in fostering such social networking.

As illustrated by Table 1 above, individual entrepreneurs and the self-employed must rely on auxiliary local supporting businesses to operate efficiently and profitably. These businesses may range from photocopying and legal advice to day care providers or temporary help service agencies. The emergence of such supporting firms, or a lack thereof, can pose a fundamental chicken-and-egg problem especially in rural communities: there is a dearth of such businesses because there are no entrepreneurs or self-employed workers who demand these services, and there are no self-employed workers because no supporting businesses are available locally to allow them to operate profitably.

Helping communities to break out of this vicious circle may be a challenge, but success in doing so could create public benefits that justify short-term public intervention (subsidies). Of course, many of the individuals who operate these kinds of supporting services may also be self-employed. Raising their productivity is an important opportunity.

To a large extent, communities and regions control their own destinies. For example, leaders of some rural communities aggressively provide broadband services to their local firms and

residents. During recent holiday seasons, an estimated 50 percent of all online retail sales were completed by small retailers rather than big chains, and many of these small firms are owned by self-employed individuals as sole proprietorships.

Institutional factors such as rules, regulations and income tax levels also matter. For example, right-to-work laws, which basically enable workers to engage in labor activities without having to join labor unions or pay membership dues, are associated with higher self-employment growth rates over time. Similarly, some communities contain business schools and community colleges that specialize in basic entrepreneurship or business training. These institutions may increase local self-employment rates by providing basic business knowledge and start-up advice, and new ways of delivering this training into more counties should be explored. USDA's Cooperative Research, Education, and Extension Service (CSREES), in partnership with its state land-grant university partners, have a potentially important new role to play in this context. Already a major web-based entrepreneurship initiative is underway in the form of an eXtension Community of Practice, designed to bring entrepreneurship training and skills-building into more rural communities. This new website can be found at www.extension.org/entrepreneurship.

Finally, it is important for state government leaders to explicitly recognize the growing importance of these self-employed workers, especially in their rural areas. At present, state governments keep track only of workers who are covered by unemployment insurance (the so-called ES-202 or Employment Security series). This means that they have virtually no knowledge of how their policies affect a growing segment of the labor market. Just drawing attention to this group, by collecting and reporting basic economic data on them, is an important first step.

Conclusion

It is clear that self-employment is important to rural areas and that it will likely become even more so in the future. It is also clear that policy can

make a difference in terms of self-employment success, and that self-employment itself stimulates wage-and-salary employment. Even so, state policy makers must walk a very fine line between not regulating excessively on the one hand, and strategically identifying key sectors where barriers to entry may be preventing expansion. In other words, intervention can be justified economically only if doing so is associated with the creation of a public good (or removal of a public bad). To further fine-tune policies, however, it is imperative that we invest in better data collection on entrepreneurs.

The role of research universities and their local spillover effects also need to be better understood, along with the types of institutional environment within universities that are most effective in moving the results of pure research and discovery into innovation that leads to new business formation. Universities, colleges, and professional schools are not yet playing the role of comprehensive local and regional engines of growth that they could play. In fact, there is substantial opportunity in many university and college towns to help increase the productivity of the self-employed.

This article shows the merits – and importance – of examining entrepreneurial and self-employment activity within the broader context of the local communities and economies. Even as the Internet is widely believed to reduce, if not eliminate, the importance of space and distance, the locally-varying factors that distinguish one place from another are becoming increasingly critical. Perhaps most significantly, locally-varying factors clearly account for differences in returns to self-employment in different locales.

About the Author

Dr. Stephan J. Goetz is a professor of agricultural and regional economics at The Pennsylvania State University, where he also serves as director of The Northeast Regional Center for Rural Development. His current research, which has been supported by the Kauffman Foundation of Entrepreneurship, focuses on the causes and impacts of self-employ-

ment and entrepreneurship in rural economic development, as well as on industry clusters. He is a co-editor of the forthcoming book *Targeted Regional Economic Development* (Routledge Publ., 2008) and has been a member of the Board of Directors of the Center for Rural Pennsylvania since 1999.

Further Reading

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Endnotes

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1. Sundar S. Shrestha,, Stephan J. Goetz, and Anil Rupasingha, "Proprietorship Formations and U.S. Job Growth," *Review of Regional Studies* (forthcoming); Steven Deller and James McConnon, "Microenterprises and Economic Growth: A Panel Study of the U.S. States 1977 to 1997," *Applied Economic Letters*, March 13, 2007; Scott Loveridge and Denys Nizalov, "Operationalizing the Entrepreneurial Pipeline Theory: An Empirical Assessment of the Optimal Size Distribution of Local Firms," *Economic Development Quarterly* 21, 203-222.

2. By 2005, the number of wage-and-salary workers had not yet recovered to pre-recession levels (19.6 million in 2000), although their number had increased from the trough of 19.3 million in 2003. This reflects the so-called "jobless recovery" during which far fewer jobs were created than historically in post-recession recovery periods.

3. We examined the independent effects of various factors that likely influence the returns to and rates of self-employment. That is, using statistical methods, we isolated and focused on the effect of any given variable holding constant other (rival) causes. It is as if all counties are put on a level playing field, and then the effect of a given variable on changes over time in self-employment rates is isolated. See Stephan J. Goetz and Anil Rupasingha, "Determinants and Implications of Growth in Non-Farm Proprietorship Densities: 1990-2000," forthcoming, *Small Business Economics*.

4. Stephan J. Goetz, "The Place-Based Structural Determinants and Effects of Self-Employment: Final Report to the Kauffman Foundation," Rural Development Paper no. 33. University Park, PA: Northeast Regional Center for Rural Development, September 2006. Available at <http://nercrd.psu.edu/Publications/rdppapers/rdp33.pdf>

5. Mildred Warner, "Articulating the Economic Importance of Child Care for Community Development" Special Issue: Community Development: *Journal of the Community Development Society*, Volume 37 No 2, June 2006. <http://government.cce.cornell.edu/doc/reports/childcare/cds.asp>

6. Maps 3 and 4 show concentrations or clusters of counties with unusually high (dark red) and low (dark blue) levels of the variables plotted, i.e., very high or low shares of self-employed workers and high and low shares of self-employment earnings. Also shown are cases where counties with very high levels of the variables are adjacent to counties with very low levels of variables. This statistical tool is especially helpful for identifying regions of the country, or county clusters, where self-employment shares and earnings are unexpectedly high or low. These counties may warrant further investigation to help understand how self-employment arises or fails to arise.

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