Economic development in US alters course because of recession

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Abstract

States in the USA have been reacting to increased budgetary pressures by reducing discretionary budgets, including economic development. As a result, state economic development organizations are adopting new strategies such as innovation, clusters, entrepreneurship and economic gardening. They are increasingly partnering with regional organizations and the private sector, including in some instances moving entirely to a public-private partnership in lieu of a state agency. Calls for increase efficiency and effectiveness of economic development investments have not to date been met by increased evaluation or accountability.

Keywords

Economic development strategies, entrepreneurship, innovation, clusters, economic gardening, regionalism, private-public partnerships

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For the past three years, states have faced increasingly challenging budget shortfalls, the result of declining revenues due to the recession, and resistance to the use of tax increases to balance the budgets. Increasing portions of states' budgets are nondiscretionary, including health care costs, pensions and education, leaving budget cutters focused on discretionary items, including economic development. These same dynamics are also impacting the federal budget, and so to the extent that the states the laboratory for

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enhancing economic development and job creation, the strategies being employed by the states to cope with reduced budgets are instructive.

In the past three years, seven trends have emerged in economic development in the US, replacing the traditional recruitment model prevalent for the preceding decades. Instead of using incentives to lure companies from one locale to another, a zero-sum game at best, states are now using seven other strategies to compete for economic sustainability. These strategies are generally less expensive to implement than recruitment, and, in some cases, involve pushing activities into the private sector or to local governments, lowering the state contribution and budget.

The first strategy is regionalism. Some states are reducing their statewide focus and instead planning and acting in sub-state regions. This approach reflects the varied geographic, demographic and economic realities of the regions, and allows a great deal of self-determination at the local level. A popular methodology that supports regionalism is "asset-mapping" where regions are encouraged to catalogue their physical, social, intellectual and human assets. These maps are then used to build strategies that capitalize on a region's strengths, and identify ways to strengthen areas that are weaker.

For instance, the Mobilize Maine project was implemented in three regions of the state, Northern Maine, Eastern Maine and Androscoggin Valley (Western Maine). In each region, an extensive asset mapping effort was undertaken in 2010, resulting in a new appreciation of the positive attributes of each area. In Androscoggin Valley, they found a 10 of Maine's 14 highest mountains, a vibrant Nordic and Alpine ski industry, arts and cultural performance venues, and a substantial transportation and logistics opportunity. The Northern Maine Development Corporation used the asset-mapping analysis to focus in on two industry clusters, information technology and energy, as focal points for future economic growth. One leader noted that asset mapping allowed local business leaders to be engaged in shaping economic development strategy. These efforts were funded entirely by local economic development agencies, federal funds and private corporate contributions. No state funds were used at all, reflecting an explicit strategy to drive economic development activity to the regions.

A related strategy that is emerging nationally is the focus on innovation and clusters. Once the purview of technology-based economic development organizations and separate from local, regional or state economic development infrastructure, innovation and clusters have become a buzzword in the states. As traditional industries continue to decline and go offshore, more and more states and regions are looking at their intellectual assets such as local universities and other research organizations, and thinking about how to leverage them for job creation. A related development is the focus on clusters, where analysis of strengths in particular sectors or intersection of industries, leads to a sustained investment in a cluster, either through a cluster development organization, or through projects that strengthen a targeted area.

Again, much of the initiative for these new efforts has been regional and costs have been largely borne by large companies in those regions. A notable exception is in Ohio where $2.3 Billion in bonds were issued to fund the Third Frontier Initiative. The Initiative in turn funded a number of programs including NorTech in northeast Ohio, a regional innovation organization serving 21 counties surrounding Cleveland, Ohio. This is an area that is in the heart of the Rust Belt, a region that has seen declining manufacturing for over three decades. NorTech has used roadmapping to assess its opportunities, and is now focusing on two clusters, advanced energy and flexible electronics.

Like other midwestern states, policymakers in Ohio are trying to retool their economies by focusing on policies that develop the innovation economy. Minnesota has recently created an 18-member Science and Technology Advisory Commission, while Nebraska's Innovation and Entrepreneurship Task Force offered policy advice to the Governor in December, calling for increased entrepreneurship support. The Iowa Innovation Council was just formed for a similar purpose. All are private sector driven, although the recommendations will have fiscal implications for the states. For instance, Minnesota and Michigan each have new angel capital tax credit programs that generally support innovation-based companies, but have a direct negative impact on revenues in the short term.

Another example is the Oregon Nanoscience and Microelectronics Institute, (ONAMI) a cluster development organization dedicated to increasing research and accelerating commercialization of technology developed at its members institutions. A collaborative organization, ONAMI is taking technology-based economic development practices across three member institutions to create critical mass in a less-populous state.

A third strategy, practiced by all of the examples mentioned so far, is support for entrepreneurship. For thirty years or more, the US has been supportive of small business, but as an afterthought to the attraction and retention of large employers. Now, new research enabled by the release of a longitudinal database of US enterprise has led to published reports by the US Small Business Administration and the Kauffman Foundation that separate out small businesses from start-ups and rapidly growing young businesses. According to this research,[2] young businesses less than five years old have created the majority of net new jobs.

A number of new initiatives to support entrepreneurs have emerged in the last few years, joining the existing incubators and small business support programs that have been in existence in all states since the 1980s. Venture support organizations such as JumpStart in Cleveland, Ohio, MassChallenge in Boston, Massachusetts, and i2E in Oklahoma all

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[2] Acs ZJ, Parsons W and Tracy S (2008) High-impact firms: gazelles revisited. Washington DC: Small Business Administration, contract SBAHQ-06-Q-0011. Stangler D and Litan RE (2009) Where will the jobs come from. Kansas City, KS: Kauffman Foundation.

combine mentorship, funding and network development to fast track young and promising enterprises.

This strategy exists alongside a more traditional economic development strategy gaining currency – economic gardening. Simply stated, economic gardening means working with local businesses, usually existing companies with 10-99 employees, to create jobs. This is a huge transition for many state and regional economic development organizations, which previously used significant budgets to recruit large companies from other cities, states and countries. Now, with greatly reduced budgets, economic developers are finding that they can support local companies by helping make connections, providing financing and expertise, and creating markets (e.g., energy efficiency standards that support local construction and energy companies by creating demand). This effort is seen as less expensive that recruiting and more effective than supporting start-ups.

GrowFL, for instance, is the official Economic Gardening Technical Assistance Program for the State of Florida, created in 2009 to stimulate investment in Florida's economy by providing technical assistance for expanding businesses in the state. The program provides technical assistance for "second-stage" companies, and helps them grow.

One strategy for which there was new funding during the recession, primarily from the federal government, was green jobs. The policy window formed by the convergence of interest in and concern about climate change, the oil price spike in the summer of 2009, and US consumer's increasing support of environmental issues, led to a surge of strategies focused on developing a green economy. This proved to be a very large tent, including alternative and renewable energy, local agriculture and food production, bio-based industrial products and energy efficiency. Almost $4 billion in funding from the American Reinvestment and Recovery Act (ARRA) was available for research for new renewable energy technologies as well as retrofitting of homes and industrial sites for energy efficiency.

Projects supported included the 845 MW Caithness Shepherds Flat wind farm in eastern Oregon, the new Massachusetts Clean Energy Center test facility for large wind blades, a solar energy system in Nelsonville, Ohio, and a compressed natural gas facility for Idaho's Treasure Valley Clean Cities Coalition. For states and regions with projects that were "shovel-ready," this funding was a great help, but otherwise did little to offset ongoing budget shortfalls.

Another approach to surviving the recession and budget cuts is not confined to economic development alone, but has been highlighted in this community. As governors and legislators struggle to make cuts, they often ask, "Which economic development programs are making the biggest difference? Which are the most efficient? Which are the most effective? Unfortunately, most state and regional economic development organizations cannot answer this question well, if at all. Some organizations make an attempt to collect job impact data, but the quality of this data vary widely and are generally discounted by legislative bodies. Most organizations do not have the data systems in place to track the companies that take advantage of their programs, nor do they regularly assess the progress of their clients. And, most critically, the organizations lack the analytic ability to determine what would have happened without the assistance offered by the economic development agency, the causality question.

Tax incentives are among the least studied economic development programs, and also one of the most expensive. Generally, these are under the oversight of the state's revenue (tax collection) agency, not economic development, and, once enacted, are rarely reviewed.

One counter example is the William S. Lee Act tax incentives in North Carolina. These incentives were designed to encourage industry to invest in the most rural and poor regions of the state. After several years of analysis by economists at the University of North Carolina-Chapel Hill found that the Lee Act incentives were not effective, they were replaced and restructured in 2006.

One last trend that has been accelerating in the past three years relates not to strategy per se, but is a reaction to budget pressures. Thirteen states have proposed or have already transitioned from a state agency for economic development to a private-public partnership. The advantages of this change are thought to include increased private corporate leadership, accountability, less bureaucracy and therefore more flexibility and responsiveness. Many who propose these changes also hope that a private-public partnership will mean decreased public budget inputs, although this rarely happens in practice.

States as diverse as Arizona, Iowa, Ohio and Wisconsin are in the process of changing from a fully public model to a partnership model. They will join Michigan (Michigan Economic Development Corporation, Rhode Island (Rhode Island Economic Development Corporation) and Florida (Enterprise Florida) among others. It remains to be seen if these organizational structures are anymore efficient or effective at economic development than their predecessors, or if this strategy is merely moving the chess pieces around.

2012 continues a multi-year trend of decreasing revenues and increasing pressures on state budgets. The easy cuts have been made, and federal funds that propped up many state budgets in 2009 and 2010 are no longer available. Ironically, economic development budgets are targeted for cuts, even as calls for job creation get louder and louder as the recovery proceeds very slowly. States are responding with new strategies and shared responsibility with the private sector and their regions.