ECONOMIC DEVELOPMENT 101 FOR GOVERNMENT OFFICIALS

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The purpose of economic development is twofold:

1. To give greater and greater numbers of people greater access to wealth
2. To increase the tax base of communities in order to provide higher quality public services to citizens

The focus of economic development is to diversify the economic base, thereby increasingly cushioning the community against economic shocks. We achieve the purpose and focus of economic development by assisting in the creation and retention of primary jobs and/or increasing the amount of income coming into the community from outside its market area.

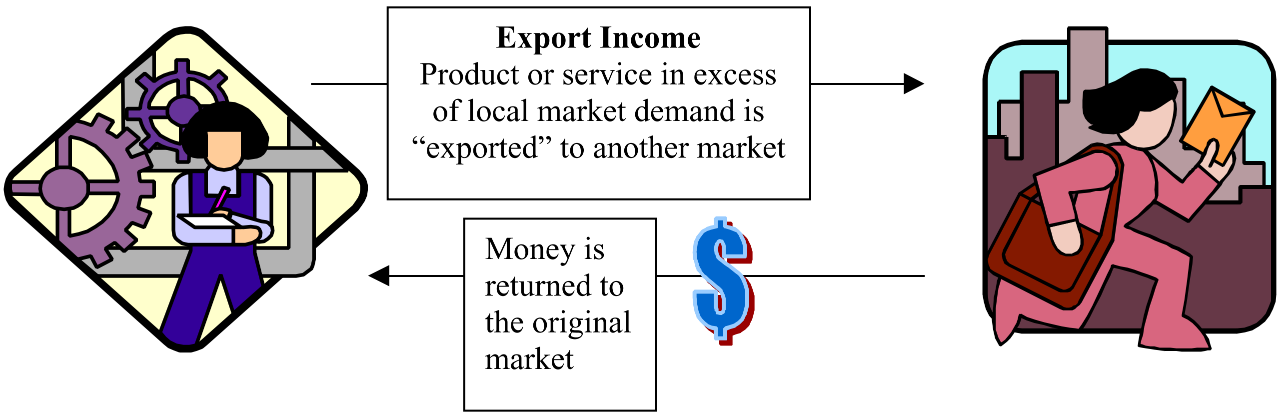
"Primary" or, as they are sometimes called, "export income" jobs are defined as jobs which produce goods and services in excess of what can be consumed in the local marketplace. For example, Jefferson County produces more guided missiles than can be "consumed" by Jefferson County residents. The missiles are "exported" to another market (e.g. Cape Canaveral) and money is returned to Jefferson County for the product.

There are only two types of income that economic developers attempt to increase into their communities:

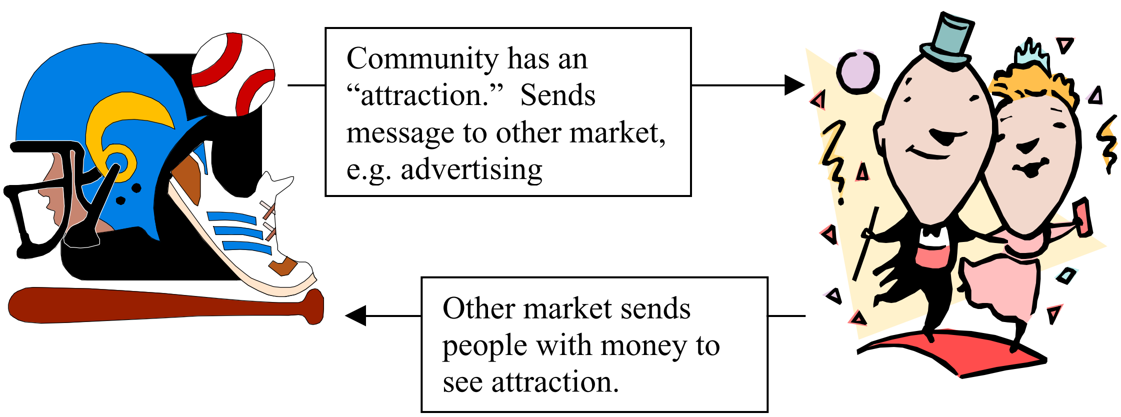
1. *Export income*: Income derived from the production of goods and services in excess of the consumption capacity of the local market. See guided missile example above.

2. *Primary income*: Income derived when the local market has an "attraction" (convention center, etc.) which draws visitors who spend money in the local marketplace. We call these people "Shriners."

EXPORT INCOME



PRIMARY INCOME



Marketplace defined in relation to primary employment

Primary employment is further defined by how the “local market” is defined. For example, retail centers are not typically defined as primary employers by a state. Why? Because the shopping centers located within a state are typically spending money that has already been “created” by primary employers in the state. It is not “new money.” However, a state such as Colorado would define a shopping center located on its border as a primary income generator because much of its income will be generated outside the state’s boundaries or its “defined market.” The local 7-11 is not a primary employer in a city, but if the market is defined as the local neighborhood where the 7-11 is located, then it becomes the neighborhood’s primary employer. In other words, the definition of “primary or export income” employment changes depending on your definition of the market.

In Jefferson County, for example, a local copying company may derive 30 percent of its income from Denver. That portion of its income is “primary.” But on a metropolitan scale, since all of its product is “consumed” in the six-county area, the copying company is not a primary employer for the region.

“Support/service” or “spin-off” jobs

Jobs that are created as the result of the demands for goods and services generated by the primary employer are called “support/service” or “spin-off” jobs. These jobs do not create wealth. They are the product of “wealth” created by primary employment. Generally they are jobs like retailing, lawyers, doctors, government workers, chamber of commerce executives, non-profit employment, etc. These jobs provide services to primary jobs. They may also include jobs that meet the required “input” needs of primary jobs. For example, a beverage company may export 100 percent of its product outside the local market. But to do so the beverage manufacturer needs other “inputs” such as aluminum cans, glass bottles, labels, cartons, etc. While the companies producing these inputs may be manufacturers, they are not "primary jobs" if all their products are consumed by the local beverage manufacturer. If, however, they sell their inputs to other companies outside the local market, they become "export income" employers to the extent they sell outside the local area.

Spin-off or support/service jobs are typically associated with the term "multiplier." The oft-maligned term "multiplier" comes from a series of economic calculations that estimates the number of jobs required to meet the needs of one primary job. The larger the multiplier, the greater the economic impact of the primary job. The size of the multiplier is determined by two things: average wage paid to the primary employee; and the amount and cost of "inputs" required for the primary employee to accomplish his work.

For example, the multiplier for an automobile manufacturer is higher than the multiplier for a software developer even if both the workers are paid the same wage. Why? Because the auto worker requires a multitude of inputs not required by the software developer. The auto worker needs tires, wiper blades, glass, steel, electronics, seats, mirrors, lights, etc to accomplish his task. This requires a host of other companies supplying him, which, in turn, creates many spin-off jobs. The software person on the other hand needs computer chips, a screen, storage media, keyboard and printer. These inputs are significantly less than the auto worker. Hence, the "multiplier" for a software engineer making the same amount of salary as the auto worker is less.

A "typical" multiplier in the Metro Denver area is in the 2.1 to 2.6 range. Translated, this means, that the primary job needs between 2.1 and 2.6 support/service or spin-off jobs to accomplish his work and to meet his living needs. Retail employment, because of its low wages and limited "primary income generating capacity" will have multipliers in the .3 to .6 range. This is not a good investment of time for an economic development professional. Retail is seldom a good primary employer because of the old adage, “Retail follows rooftops.” In other words, retail must follow customers and those customers are created through primary employment’s wealth-generating ability.

A mature regional economy that offers a wide array of goods and services for purchase by the primary job will also have a larger multiplier than a smaller market. In other words, a diverse economy “holds on” to the primary worker’s income longer. In an immature market, lacking many of the goods and services demanded by the primary job, the dollar exits more quickly, thereby reducing the multiplier.

Strategies to increase primary employment

Communities seeking to improve their economic position engage in two principle activities to achieve their desired result:

1. Attraction of primary employers
2. Retention and expansion of primary employers

Attraction

Attraction activities usually start with a ***“targeted industries” study***. This process analyzes the growing industrial segments of the national economy and compares these growth sectors with the local community’s industrial base. It examines why these sectors are growing or not growing in the local community. It determines reasons why some segments are not suited for the local economy (too distant from markets, workforce shortages, too smelly, etc.) and what gaps might be filled to make the local community more desirable to these companies. It looks at companies that are a “good fit” for the community and that can diversify the local economic base.

In Metro Denver, the Metro Denver Network commissioned such a study in 1986. Using a nationally recognized accounting firm, the region determined that:

1. Growing sectors in the national economy included: insurance, medical products/services, computer-aided manufacturing, biotechnology, computer storage devices and financial services
2. Metro Denver had a glut of office space suitable for many of these types of jobs to locate
3. A highly trained workforce in Metro Denver that could fill these jobs was, at the time, underemployed or unemployed

This plan sparked what many believe is the economic turnaround of the late 80s and early 90s. This process was repeated in 1998 when the Metro Denver Network published “Tech Vision,” the next strategic plan for the decade of the year 2000.

Following the completion of a targeted-industries study, the local community embarks on a **program to fill the “gaps”** identified in the study. This may include such things as: increasing air service, building different kinds of buildings, adding new courses at the local college or changing regulations which discourage location of desired companies.

Coincident with the efforts to fill gaps in local services, the community embarks on some type of advertising and marketing effort. Most communities will engage in one or all of the following:

1. Print advertising – placing ads in development magazines, newspapers in targeted geographic areas, etc.
2. Recruitment trips – traveling to other areas in efforts to lure companies from one community to another
3. Video production – creating a video extolling the virtues of the local community
4. Economic briefing – designing a multi-media briefing for prospective employers who come to visit the local community

5. Site selection conferences – bringing executives in targeted sectors to the local community for wining, dining and indoctrination
6. Trade shows – attending and exhibiting at trade shows or conferences where targeted industries congregate, i.e. electronics, biotech symposiums, facilities management seminars and conferences, etc.
7. Cold calling – telephone or direct visits on unsuspecting, potential employers
8. Public relations – hiring p.r. firms to tout the “wonderful quality of life” in “YOUR COMMUNITY’S NAME HERE”

Of the foregoing, only #4, #5, #6, and #8 work well alone. Print advertising is only effective if it serves to reaffirm the purchase decision of a company. It will NOT generate new leads. Videos are a complete waste of money. They consume large dollars and are obsolete when the editing is finished. Cold calling is good practice for your sales staff but a complete waste of time. One year we called over 20,000 companies. Not one prospect was generated by the effort.

Retention and Expansion

Over 80 percent of all jobs created in a local economy come from existing employers. Any good economic development program has a retention and expansion component. Unfortunately, virtually every retention and expansion program is no good. The typical program consists of staff and volunteers making calls on local employers. The company representative typically recounts a series of ills, horror stories and problems with local governments. The economic development representatives listen attentively, take notes and follow up on some of the simpler problems outlined. Everyone feels good and virtually nothing is accomplished.

For a retention and expansion program to accomplish its goals, it must have two components:

1. A strategic element that focuses on public infrastructure improvements

2. Value-added services that are meaningful to the local company

The same things that attract new employers will keep existing firms

Communities with good capital investment programs, attentive training institutions, moderate tax and regulatory environments and affordable housing are always desirable locations. These elements can be achieved with a strong vision from elected officials, government employees and the private sector working jointly. Communities without vision fail.

The second element requires direct assistance from the local economic development organization. If the local group sees itself as a business partner with local companies, retention is high. Providing such things as regulatory and training assistance, new business leads, competitor analysis, technology advances, marketing assistance, etc. provide a needed "value added" service to local employers. A full understanding of "who" are primary employers, their strategic directions and the components of their success should dictate the types of services provided. Unfortunately, few economic development organizations possess this type of skill and expertise. Too often the economic development professional becomes a glorified real estate broker, hustling sites to new employers while ignoring the riches in his own backyard.

Incentives

Nobody wants to pay retail prices. A solid incentive program is based on the principles of good economic theory. Here are some general rules on the topic:

1. Incentives should only go to primary employers who pay wages in excess of the average local wage
2. Companies in targeted sectors (either new or existing) should receive preference as well as an existing, non-targeted firm experiencing rapid growth in a stable or even declining industry. "There is no such thing as a 'growth industry', only growth companies." John Welch, Jr., General Electric

3. Tax incentive packages should never total more than one-half of the entire, direct tax revenue expected to be paid by the new firm
4. Training funds are the best incentive; if the company fails, a better-trained workforce remains and serves as an inducement for a new, replacement firm
5. Non-cash incentives are sometimes just as good as cash. A malt beverage manufacturer might be more interested in using the excess sewage treatment capacity of the municipality than getting cash to construct a new one
6. Every community offering incentives should have an economic analysis model that calculates the tax revenue vs. costs of a new employer. Highly sophisticated communities will have the capacity to determine "marginal cost" impacts. For example, the local sewer plant is at capacity. A new employer with heavy treatment demands will require a new plant to be built. If the cost is not borne directly by the prospective employer, a new plant will actually result in increased costs for all the treatment plant customers
7. More than anything, incentives are Oriental. They are a "show of face." Many times it will not matter if the local group has the most money on the table. What will matter is that they gave more of what they had than their competitors
8. Most companies will not use all the incentives offered. They will be content that the local community <u>made</u> the offer. When John Welch Jr. of GE was offered a tax abatement from the local school district, he asked, "Why would I take money from the company that produces my workforce? Isn't that cutting off my nose to spite my face?"

Basic information elements of an economic development program

Every economic development program has some basic products and services it provides to prospective companies. Remember…economic development organizations do not create new jobs. They provide information and assistance to companies who create new jobs. A good economic development program will strive to have the most comprehensive and current information available. The program's goal is to have information that is so good, it will be used to compare against all other competitors.

1. Demographic information: Most commonly requested information from companies–includes population, educational institutions and achievement, race and ethnicity breakdowns, income levels, wage and salary schedules, housing costs, etc.
2. Public infrastructure and costs: Transportation corridors, traffic counts, distance to national and international air service, major public construction projects recently completed or planned, sewer, water and telecommunication infrastructure availability and age, public facilities such as convention centers, schools, higher education institutions, courses taught at local colleges and universities, etc.
3. Taxes, fees and regulations: Income, sales and property tax information–development fees, regulatory processes and timelines, unusual requirements such as land donations, impact fees, etc., off site improvement requirements, tap fees, electrical hook-ups and telecommunication taxes or fees
4. Quality of life: Parks, trails, open space, attractions, sports, school athletics, music, performing arts, museums, etc.

This information is usually contained in two documents: a "Factbook" and a "Community Profile." The Community Profile contains a quick synopsis of the above. The Factbook is a substantial document providing comparative, in-depth data on the above topics and others.

Measuring the effectiveness of your economic development program

To the economic developer, success is measured in the number and quality of new jobs created and retained. Smaller numbers of new jobs with high wages are preferable to many jobs with low wages.

To the local government, the success may be measured in increased tax revenues. Do sales and property taxes in your city/county exceed the regional average? Are tax receipts growing faster than competitors revenues?

There are complex means to determine whether the growth your community is experiencing is a function of “normal” market activity or your economic development program. Called “shift-share analysis,” this process permits the economic development organization to measure, to a stronger degree, the effectiveness of its programs. It also permits decision makers the capacity to determine whether one type of activity versus another is more effective in job creation. These types of analyses take several years to measure, but can provide valuable input into a quality evaluation of your program.

Selecting a quality staff

A strong economic development staff will be comprised of professionals with backgrounds in real estate, taxation, marketing, transportation and environmental issues. The American Economic Development Council (AEDC) offers a certification program called the “Certified Economic Developer” or CED. To obtain a CED, the professional must have several years of experience and successfully complete a rigorous testing program. For young professionals, this certification provides additional testament to their suitability for jobs with greater responsibility. For more seasoned economic developers, the certification program has less meaning.

The best test of a staff is the experiences they have gained during their tenure. The professional whose experience includes highly complex projects of some magnitude, work at the state or regional level, and who has faced the challenges of contentious annexation or “no growth” elections is usually a strong candidate for any job in your organization.

Reasons companies locate to your community

If you read the newspaper, you are quickly convinced that a company locates only to those communities who cough up the big bucks. Not true. There are a host of reasons for the final location decision with incentives ranking near the bottom of their top ten. “Location” is still the major determining factor, but its definition has changed over the years. With technological advances in telecommunications, “location” may mean the CEO likes to live in a certain area where he/she can still operate his company through modern telecommunication services. Here are the main reasons companies locate. They change from year to year based on changes in market conditions.

1. Within 60 minutes of an international airport
2. Proximity to markets
3. Labor skills and availability
4. Tax and regulatory environment
5. Close to major universities
6. Quality of life issues
7. Cost of doing business, i.e. labor rates, taxes, transportation costs, etc.
8. Strong and stable political leadership
9. Incentives
10. New or planned public infrastructure

Remember...you are not judged by where you are today. You are judged by where your community is going. In the 1980s Denver was not on any company’s Top Five list for relocation. As the region began to make important infrastructure investments, such as DIA and the convention center, companies began to notice. The region moved from #25 as the most desirable location for office and manufacturing in 1987 to #2 and #3 respectively by 1991. DIA was not completed until 1992. It was the community’s forward momentum that drove international interest, not the position it found itself in 1987.