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Should the State Tighten Regulations on Local Economic Development?

In the early 1990s, as California experienced its most severe economic decline since the Great Depression, Governor Pete Wilson proposed a host of measures to streamline, reform, and end policies that allegedly placed the state and its communities at a competitive disadvantage. While the state lost 720,000 jobs and its cities and counties scrambled to attract and retain businesses, a few communities lavished public resources on private projects that showed little promise of benefiting those communities as a whole. After several such "give-aways" received significant media attention, the state legislature began to consider measures to curb abuses associated with this approach to local economic development. In 1999, Governor Davis signed AB 178, which limited competition among localities for so-called "big box" retailers and auto malls.

Despite the media attention and subsequent legislative action, there has been little research on competition among localities for economic development. In *Local Economic Development in Southern California's Suburbs: 1990–1997*, Max Neiman, Gregory Andranovich, and Kenneth Fernandez address this lack by analyzing local economic development policy in Southern California. In particular, the authors:

- Trace the recent history of economic development in the United States,
- Use detailed surveys to characterize local economic development policy in a seven-county region,
- Describe what communities do to attract and retain development, and
- Assess explanations of why communities adopt these policies.

Finally, the authors address apprehensions over local competition for economic development and reframe the regulation debate in terms of the state-local power balance.

The Origins of Local Development Policy

By the 1990s, economic development was a decidedly local affair. Federal aid, a critical feature of local economic development since the 1930s, was curtailed or eliminated after 1980, when the Reagan and Bush Administrations oversaw a 35 percent reduction in national grants to cities. This reduction had important consequences for California's cities: In Los Angeles, for example, the federal contribution to the city's budget dropped from 19 percent in 1977 to 2 percent in 1985. At the state level, economic development policy stressed two broad themes: building on California's natural strengths and fostering competition. The first theme emphasized the state's role in providing infrastructure for economic development, but the second encouraged local governments to fashion their own economic development strategies.

During the early 1990s, however, the state withdrew resources for municipal purposes and the recession dissipated what local revenues remained. In general, California's cities responded by exploring corporate-centered economic development, focusing on local "growth machines" rather than grass-roots participation. The authors note that this response may be due in part to generally low levels of public concern for local economic development policy. The public typically pays attention only when business or residential development conflicts with the lifestyle and amenity concerns of local residents.

How Do Cities Approach Economic Development Policy?

As their awareness of policy options increased during the 1990s, California's localities implemented more—and more focused—economic development efforts. By 1997, most local economic development policies clustered into three broad groupings:

- Streamlining, such as one-stop permit processing,

- Classic redevelopment policy, including land assembly and tax increment financing, through which localities acquire properties for resale or use by private parties and finance these acquisitions with bond sales, which are paid for with the revenue generated by the increased value of these "redeveloped" properties, and
- Intergovernmental grants and subsidies (for example, enterprise zones and training grants).

Although redevelopment and tax increment financing often are criticized as unwarranted or wasteful expenditures of public resources, most of the other measures taken by local governments in the name of economic development are relatively uncontroversial.

In addition to identifying and describing these policy categories, the authors found that the cities' perceptions of competitiveness did not predict the level of their development policy efforts. Although 65 percent of respondents reported that they had examined the development policies of other cities, only 38 percent said that they had adopted specific policies as a result of competition from other cities. About 34 percent said that such competition influenced the number of incentives their localities offered to businesses. The survey also indicated that such competition is usually local: When asked to list their competitors, the majority of respondents named nearby cities in the same county.

The authors also tested models that purport to explain economic development activity. Although some models emphasize either the level of competitiveness in a region or the political and institutional characteristics of the locality, the findings indicate that the best predictor of economic development activity is sheer economic need. Family income is negatively correlated with such activity, and high unemployment and community size are positively correlated. In general, the findings offer little evidence that prosperous localities pursue economic development more actively than less affluent communities.

The findings regarding political and institutional factors are also suggestive in this regard. Cities with a mayor-city council form of governance tend to have higher levels of overall development activity than do those with a city council-city manager form. Surprisingly, there was no relationship between any particular policy measure and either the size of the local economic development staff or the level of electoral conflict related to economic development. The three most significant factors in local development policy are population size, the perceived importance of the local economic development staff, and the importance of local business people. That is, larger communities with important local agencies and private sector actors tend to have higher levels of policy activity.

Perhaps the most significant finding concerns the effects of perceived competition among localities. Initially, the analysis indicated that the more competitive a city was seen to be, the more effort it expended on behalf of local economic development. But after controlling for other factors, the authors found that competitiveness as such did not have an independent effect on policy. This finding calls into question the need to curb such competition through legislative action at this time.

Economic Development and the State-Local Relationship

These findings strongly suggest an alternative view of competition among local governments and the need for state regulation. Eliminating interjurisdictional competition for local development is probably not a realistic goal. Localities will continue to compete for economic activity so long as local residents, property owners, or public treasuries benefit from having more development of some kinds and less of others. This competition is especially likely for established communities in densely populated areas, which tend to be more sensitive to the policies of nearby communities.

If eliminating local competition for economic development is not a realistic policy goal, neither is it an obviously worthy one. At a time when local fiscal authority is already weak, further constraints on competition for local economic development may be unhelpful, especially if the evidence suggests that this competition is not disabling in the first place. The authors conclude that such restrictions may very well exacerbate the problem of weak local authority in an effort to "solve" the less urgent problem of costly give-aways.

This research brief summarizes a report by Max Neiman, Gregory Andranovich, and Kenneth Fernandez, Local Economic Development in Southern California's Suburbs: 1990–1997 *(2000, 106 pp., $12.00, ISBN: 1-58213-025-6). The report may be ordered by phone at (800) 232-5343 [mainland U.S.] or (415) 291-4415 [Canada, Hawaii, overseas]. A copy of the full text is also available on the Internet (www.ppic.org). The Public Policy Institute of California is a private, nonprofit organization dedicated to independent, objective, nonpartisan research on economic, social, and political issues affecting California.*

PUBLIC POLICY INSTITUTE OF CALIFORNIA
500 Washington Street, Suite 800 • San Francisco, California 94111
Telephone: (415) 291-4400 • Fax: (415) 291-4401
info@ppic.org • www.ppic.org