Cautionary Notes for Competitive Cities

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Introduction

Leaders of American cities seeking to foster economic growth often look to success stories from other places to provide models and strategies they can adopt. Unfortunately, many of the popular success stories tout benefits that are at best exaggerated and at worst apocryphal. Moreover, context matters, and a strategy that is successful in one city may not prove effective in another. This paper reviews some of the policies that city planners, mayors, and civic groups consider promising for fueling economic growth. Although each of them may have worked in particular circumstances, we explain why they are typically not successful and why policymakers should be cautious in adopting them.

Conceptual Framework

While the term 'economic development' refers broadly to the "process of improving the standard of living and well being of the population," policymakers and the public tend to use the word to refer more narrowly to increasing the number of jobs, the number of businesses, and/or incomes in the city.[1] This distinction is important and to some extent, the narrower focus excludes important benefits (or costs) of economic development policies. Consider for example, the renovation of Pike's Place Marketplace in Seattle. Regardless of any economic development benefits per se, there are many

[1] The MIT dictionary of Modern Economics, fourth edition, edited by David Pearce, page 119.

residents in Seattle who were pleased to see this piece of the city's history restored (Frieden and Sagalyn 1989).

In this paper, we focus on the narrower definition of economic development and look specifically at the impacts of public policies and investments on growth in jobs, firms and incomes. Throughout, however, we will keep these 'consumption benefits' in mind – benefits that may well justify the investment, despite disappointing effects on economic growth.

We consider seven strategies: infrastructure investment; three types of tax policy (lowering overall taxes; offering special tax deals to specific firms and enterprise zones); government efforts to draw high-tech industry; and two forms of promoting tourism (building stadiums and legalizing casino gambling).

Investing in Infrastructure

The role of public investment in the economy captivated national attention in the early 1990s. Amid claims from engineers that the nation's infrastructure was crumbling and assertions from economists that insufficient investment in infrastructure was slowing the economy, government officials argued for substantial increases in public spending. Early in his first term, for example, President Clinton proposed that an additional $20 billion be spent on a national infrastructure initiative.

While we will focus our discussion on highway infrastructure (including roads, interstates, and streets), the term infrastructure is often used to include a broad range of 'public capital' such as mass transit, water resources and supply, waste water treatment facilities, and even the stock of school and municipal buildings. Much of our discussion about roads can be generalized to other categories of infrastructure, which have, in fact,

been found to be even less effective at spurring economic growth.

Building roads has long been considered an effective strategy for fueling economic growth. First, such public roads may contribute to firm output in the same way that private capital or equipment might -- public roads are, in part, that is, just 'unpriced' or 'free' inputs to production. Second, they may make transportation of goods and services cheaper, which in turn lower the cost of purchased inputs. Third, they may reduce commuting times and expand the geographic area over which cities will be able to draw labor, meaning labor costs should decline and supply will be more readily available. Such reductions in transportation costs, inputs, and wages then fuel economic growth by luring businesses into the city and spurring production by those already there. Finally, the actual construction of roads involves the employment of workers, consumption of supplies, and so on.

What evidence fueled the 'infrastructure scare'? To begin with, engineering needs assessments indicated that many bridges and roads had declined in quality and continued to be neglected.[2] [3] Then, there was the exciting econometric work of David Aschauer. In a series of studies, he argued that the decline in infrastructure investment was a key factor in the poor performance of the US economy in the 70's and 80's and that increasing infrastructure investment could lead to substantial economic gains studies

[2] See, for example, *Fragile Foundations: A Report on America's Public Works*, National Council on Public Works Improvement, 1988

[3] In 1992, for example, the Federal Highway Administration estimated that $46.2 billion was required to keep highway and bridge performance at 1991 levels, yet only 35.9 billion was budgeted. This is not, by itself, evidence that spending is insufficient – the public may be willing to forgo high performance on highways and bridges in favor of some other public priority, say education or policing or in favor of holding on to more money for private uses. More generally, the public may merely have decided not to keep the roads in tip-top condition. Also, notice that some of the decline in spending may be traced to the completion of the interstate highway system which many regard as substantially a one-time investment.

(Aschauer 1988, 1989). For example, his work implied that the slow rate of infrastructure investment could explain more than half of the slowdown in productivity in these decades. Even more startling, perhaps was his claim that the rate of return to infrastructure investment was almost 70 percent.

Aschauer's results should be viewed with caution, however. While his work indicates a strong correlation between infrastructure investment and income, it does not clarify the direction of causality. Does higher infrastructure investment lead to economic growth? Or do higher incomes lead to greater infrastructure investment?

The flurry of research spurred by Aschauer's provocative results attempted to disentangle the direction of causality and get clearer estimates of impact of investment on economic growth. Turning to state and regional data, these analyses found that the impact was far more modest than Aschauer had claimed, and in some cases non-existent.[4] Few studies, however, have investigated the impact of investment on economic growth of cities per se. Dalenberg and Partridge (1995), a recent exception, looked at metropolitan areas and found a *negative* impact of highway spending on employment.

Taken together, these papers provide fairly persuasive evidence that infrastructure investment is not likely to be the wholesale solution to languishing cities across America – at least in part because of the already large stock of public capital in the United States. In fact, several cities across the country, including Boston, Fort Worth, Hartford, New York, Oakland, Pittsburgh, Providence and San Francisco, are now dismantling the

[4] Most of these focused on states' economies (rather than the national economy as had Aschauer) and, in so doing, were able to make use of "fixed effects" estimators which statistically account for many of the unchanging attributes of states – such as climate, topography, etc – that may influence economic growth. Fisher (1997) provides a nice introduction to this literature, summarizing some of the highlights of the literature on economic development and public services more broadly.

freeways and highways that were once considered essential for a thriving economy (Lockwood 2000).

Still, there may be local areas in which infrastructure investment would be effective. Econometric studies essentially measure the 'average effect' of additional infrastructure across the country, and since most areas have adequate infrastructure, the estimated impact is small.[5] But infrastructure investment may be effective in areas where the stock is aging or in growing areas, such as Phoenix, Arizona, where the stock is small relative to growing needs.

Certainly, this is a subject on which research is needed – research that examines the impact of infrastructure investment on cities, and distinguishes the impacts on 'infrastructure poor' cities from the impact on cities with relatively adequate facilities. Certainly, the results of the existing research suggest that careful cost-benefit analyses should precede public investment in roads as a tool for economic growth. Finally, cities might consider using tolls in a system of congestion pricing to make better use of their existing infrastructure instead of looking to additional investment. Put simply, higher prices during periods of peak utilization can be used to shift some demand to off-peak periods, smoothing traffic flows and reducing travel times, without costing significant amounts of money. While it seems unlikely that congestion pricing by itself would yield significant improvements in economic growth, that is a matter for future research.

Lowering Taxes

[5] Poor quality roads appear to be concentrated in a small number of areas. Sanders (1993) shows that 40% of all bridges that have been classified as deficient are located in just 6 states. More than half of all bridges in New York State fall into this category as compared to just 2% of Florida bridges and 6% of Oregon bridges. There is a similar pattern to pavement quality. While in 1989, it was estimated that 11% of all

Governors and mayors recognize that businesses consider taxes when making location decisions. All else equal, lower taxes mean lower costs for firms, which suggests that by reducing taxes, a city may attract new firms and new jobs. Similarly, lower sales taxes may attract shoppers to the city, or induce existing city shoppers to buy more. Yet it is far from certain that such reductions are an effective strategy to spur economic growth. For one thing, low taxes are often accompanied by low levels of public services. For another, business taxes represent a relatively small part of the cost of doing business for the typical firm compared, say, to wages and other expenses. Firm location decisions depend critically upon such factors as the characteristics and availability of the local workforce, proximity to markets, and the mix of public services, in addition to tax burden.

While there is abundant economic research on the role of taxes in economic growth, consensus about the magnitude and significance of the impacts remains elusive, due, in large part, to stubborn empirical and conceptual difficulties.[6] Precise estimates, for example, require disentangling the impact of taxation from the impact of public services and other city characteristics and to measuring the real tax burdens of firms, both of which are difficult to do in practice.

Most empirical studies of tax policy and economic growth attempt to estimate the impact of the level (or mix) of taxes on a measure of economic activity – typically

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roads are of poor quality, in most states the problem is relatively small – i.e., only 4% of the roads in Connecticut are of poor quality.

[6] Wasylenko [1997], Bartik [1991, 1994a and 1994b] provide a valuable overview of the economic literature on the relationship between taxation and economic development as well as drawing out the policy implications of this research.

income, employment, investment, plant relocations, expansions or births.[7] These analyses typically consider overall tax burdens (averaged over income or population), and yield estimates of impact of changes in the overall level of taxation, rather than of a particular tax. An alternative methodology is based upon simulating the tax burden of a set of hypothetical firms in different jurisdictions[8]. These typically involve the estimation of the value of the 'standing offer' to a set of hypothetical firms with different characteristics, and don't include special deals, discussed below. The importance of this research is that it reveals 'what matters' to firms, thereby helping to focus policy attention on those policies and tax provisions that may prove effective.

Despite the empirical difficulties, the economic research does suggest some conclusions. First, the overall lesson is that taxes are likely to have a small, albeit statistically significant effect on business locations and economic growth.[9] Second, effects tend to be larger in smaller areas, which is consistent with intuition. The smaller the area over which firms are choosing locations (the closer the 'competitor' locations to the city), the more similar locations are likely to be in terms of the non-tax characteristics and amenities, and, hence, the more important taxes are to their location decision. These results suggest that mayors should consider tax policy in luring businesses from their neighbors, but not as a strategy to lure firms from more distant locations. (Of course,

[7]These studies differ importantly in their treatment of tax and fiscal variables. Some measure tax revenues, for instance, as a fraction of income or population, essentially measuring the average tax burden. Others specify a list of nominal tax rates in different categories. The first method essentially ignores the differences in the mix of taxes – say, between sales and income taxes, taxes on firms versus taxes on individuals - and differences in tax rates versus tax bases. The second method includes no consideration for the tax base and so is generally inferior to the first.

[8] Fisher and Peters [1998] provide a careful and comprehensive discussion of this methodology and the results of their exciting work in this area.

[9] Bartik [1994 a, b] suggests the elasticity of business location and economic growth with respect to taxes lies somewhere between -0.1and –0.6 for states and regions, with an average somewhere around -.3. Studies that focus on intraregional tax competition yield estimates of tax elasticities that are considerably higher.

aggressively trying to lure business from your close neighbors might not be a wise policy.)

Note, however, that even in the 'best case' estimates, lowering the overall level of taxation is not a very effective way to spur economic growth. Further, given the difficulty of enacting tax reductions and the political 'capital' that has to be spent to do so, the case for turning to tax policy to fuel economic growth is even less clear – since tax reductions may crowd other interventions out of the policy debate. Of course, there may be cities where taxes are so high, relative to their suburbs and other cities, that reducing overall taxes may be an important first step in an economic development plan. But these will be the exception to the rule.

One interesting and more promising alternative to reducing overall taxes is to alter the mix of taxation. As an example, there is some evidence that moving toward a mix of land value taxation and property value taxation from a system of pure property value taxation may serve to increase economic growth.[10] Similarly, cities might increase reliance on user fees and charges, which are paid only by those using a particular public service, and congestion pricing to increase the efficiency of revenue raising.

Lowering Taxes: Special Tax Deals for Specific Firms

Rather than trying to attract firms by changing the overall tax structure, cities sometimes turn to offering specialized tax 'deals' to particular firms either in an effort to lure these firms to locate in the city or to keep them from leaving.[11] Hard data on the

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[10] Oates and Schwab 1997.

[11] See Fisher and Peters (1997) for a longer discussion of the various forms of tax incentives and research in this area.

prevalence and magnitudes of these deals is scanty, however, data on economic development tax expenditures available for Michigan, New York, and Louisiana, suggest that these three states lost some $25-$60 per capita in annual tax revenues in the early 1990's (Bartik 1994). Further, anecdotal evidence suggests that cities may be foregoing significant amounts of tax revenues in 'sweetheart deals' with particular firms.

Consider the recent negotiations with the New York Stock Exchange. New York State and City officials have offered $160 million in tax breaks and electricity subsidies to keep the Stock Exchange in Lower Manhattan (Bagli 2000).[12] Similarly, New York City offered CBS an additional $10 million in subsidies in 1999, just six years after it gave the company $50 million in tax breaks to stay in Manhattan for 15 years (Bagli 1999).

Whether or not these sorts of deals make sense depends first on what firms would have done in the absence of any special incentive. Special deals can only yield positive growth effects if they truly change firm location decisions. Some cities have no doubt offered special deals to firms that would have chosen to locate there in any case. What is more, firms that remain in the city after receiving a favorable tax deal may have decided to stay even without any particular tax preference. Many observers, for instance, thought CBS was bluffing when it told New York City officials in 1999 that it was once again considering a move to Jersey City (Bagli 1999). Naturally, policymakers should try to distinguish between firms that really need special treatment and those whose threats are empty, but unfortunately, it is not easy to do so.

[12] The City and State have also agreed to provide up to $480 million toward the cost of building a new trading complex (Bagli 2000).

Even where incentives are in fact necessary to draw firms, they may not be advisable. The amount of foregone revenue needs to be carefully compared to jobs, or income, that are likely to be generated and, as always, compared to the jobs or income that would be generated by alternatives, including the possibility of lowering the overall level of taxes.

Note that estimating the impact of special tax incentives on economic growth is even more difficult than estimating the impact of the overall tax burden. There is a dearth of data on the actual packages that are offered and accepted. And, while some states report data on tax expenditures, special deals are often not identified in these reports. Further, distinguishing between one city's 'special deal' and another city's 'tax reform' is difficult.

While there is relatively little econometric research in this more specific area, special tax deals should be viewed with caution. Given the finding that the impact of taxation on firm location is relatively modest, special tax incentives are only likely to affect firm decisions if they are fairly substantial. In that case, the additional jobs and income created would have to be similarly large to justify the expense.

The political pressure to avoid the 'loss' of jobs to other cities and suburbs is intense and it is tempting to offer incentives to keep firms from leaving. Similarly, the political rewards for bringing in 'new businesses' may tempt mayors to offer incentives to likely prospects. These should both be viewed with caution, as the public rarely appreciates the full cost of these tax incentives that must be paid for over a number of years, and city leaders should balance the political benefits with a concern for the longer term costs.

Lowering Taxes: Special Deals for Particular Neighborhoods (Enterprise zones)

During the 1980s and 1990s, enterprise zones were debated in this country and many states adopted them. As of 1995, 37 states had some form of enterprise zone program, and nearly 3,000 zones had been created within them (Boarnet and Bogart 1996; Wilder and Rubin 1996). At the federal level, the Clinton Administration launched an enterprise zone program in 1993, and there are now 23 urban empowerment zones and 64 urban enterprise communities.[13] These programs differ in specifics, but they all provide geographically targeted tax preferences and other incentives in an attempt to induce firms to locate or expand in the area.[14]

Enterprise zones were first proposed by British geographer Peter Hall. Looking to the success of Hong Kong, where a policy of no taxes and minimal regulation appeared to have produced dramatic economic growth and ample new job opportunities, Hall proposed trying the same strategy in England's declining urban neighborhoods (Moss 1995). And recall the lesson from above that the smaller the area, the more effective the tax incentive.

Despite great promise and enthusiasm, enterprise zones have yielded disappointing results. Most studies of Great Britain's original program in 1981 suggest it was a failure. Employment grew more slowly within the zones than outside, and the incentives appeared to have little effect on firm location or expansion (Ladd 1993). The

[13] The enterprise communities are eligible for a far more modest set of Federal benefits. Employers in enterprise communities are not eligible for wage tax credits, for instance. They are, however, eligible to receive tax-exempt bond financing.

studies in this country have generally been pessimistic as well (Ladd 1993). So why is it that enterprise zones have not lived up to their promise?

First, even in small areas, the subsidies offered tend not to be large enough to dramatically alter business location decisions. Interviews of firms in enterprise zones suggest that incentives are only a small part of reason they decided to locate there (Fisher and Peters 1997). Indeed, one study found that nearly half of firms in enterprise zones do not even take advantage of the available incentives (Dowall 1996).

Second, to the extent that subsidies are effective, they are most likely to draw firms who would have located nearby in any case. Indeed, many charge that enterprise zones succeed only in relocating business activity from neighboring locations. The evidence is somewhat mixed here, and ultimately, it may be impossible to satisfactorily distinguish between "new" jobs and jobs that would have arisen elsewhere if the zone did not exist. In any event, the distinction might not be that important - is such relocation really so damaging in the case of enterprise zones? Isn't the very point of enterprise zones to redirect investment in this way – that is, towards distressed, high unemployment areas – even if the investment comes from adjacent areas?

A third potential concern is that even if a zone succeeds in generating new investment, it may not produce new jobs. If subsidies are targeted to capital, for instance, firms may shift to more capital-intensive production and even perhaps, reduce employment (Papke 1993). Similarly, if there is not a ready supply of workers to meet the increased demand, the end result may simply be an increase in wages. Finally, even if new jobs are created in a zone, they may not go to residents. The most sophisticated

[14] Ladd (1993), Papke (1993), and Fisher and Peters (1997) all provide good overviews of the research on enterprise zones.

studies, in fact, have found that zones have no effect on the income and employment of zone residents (Papke 1994; Boarnet and Bogart 1996). Indeed, residents may even be hurt as local land rents increase.

It is worth emphasizing again how difficult it is to identify the unique contribution of zone designation on subsequent economic growth. Furthermore, the package of incentives differs quite radically across enterprise zones, making generalizations difficult. With this said, we can take away a few lessons. First, enterprise zone designation is unlikely to radically change the rate of economic growth in a local area. Second, policymakers should understand that zones are likely to redirect economic activity from areas outside the zone. This may in certain cases be desirable, but policymakers need to be cognizant of this basic rule. Third, policymakers should pay close attention to the particular mix of subsidies and structure them in a way that will encourage employment, especially among zone residents. Finally, it should be said that enterprise zones might have political benefits in mobilizing local leaders to develop new initiatives and in fostering a broader community dialogue.

Picking Winners –The High-Tech Strategy

Silicon Valley has become a symbol of the extraordinary benefits that high technology industries can bring to regional economies. In just a few decades, the birth and expansion of microelectronics firms transformed the Valley from an agricultural community into one of the fastest growing and most affluent regions in the country (Saxenian 1985). Not surprisingly, then, many policymakers see the Valley as the model to replicate. Oklahoma's "High-Tech Triangle," Tennessee's "Technological Corridor,"

New Mexico's "Rio Grande Research Corridor," and New York City's "Silicon Alley," are just a few of the slogans that are now sprouting up as local areas attempt to transform themselves into the next high-tech hot-spot (Malecki 1985). The latest version is to attract the rapidly expanding number of Internet start-ups.

Certainly, these cities and regions are correct that high tech firms often drive growth. One recent study, for instance, finds that 65 percent of the difference in total output growth across metropolitan areas can be explained by the rate of high-tech growth and the initial high-tech density (DeVol 1999). And high-tech industries are only growing in importance. The problem, however, is that the conditions that led to the rise of Silicon Valley, as well as that of the other high-tech regions (e.g., Route 128 in Massachusetts, Research Triangle in North Carolina, Austin, Texas), are quite exceptional and difficult to replicate. Ironically, while Internet entrepreneurs can ultimately deliver their products from anywhere, these firms may be even more constrained in their locational choices than more traditional industry.

Consider, for instance, the case of Willimantic, Connecticut, a nineteenth century mill town which is pinning its hopes on a $28 million makeover of a 300,000 square foot thread mill designed to attract a cluster of high-tech start-ups. "Wiring the mill with high capacity computer lines will attract e-businesses like moths to a light," said one optimistic local businessman (Zielbauer 2000). Yet the town hardly seems positioned to capture such a niche. Why would an Internet entrepreneur choose to launch operations from a town where only 18.7% percent of residents have college degrees (U.S. Census, 1990)? Moreover, the town's location is far from ideal. Twenty six miles east of Hartford, the town is beyond commuting range of Boston and New York City and lacks

the natural amenities of small towns further north in New England that might attract young professionals.

While Willimantic might score a modest success with its high-tech mill, a high technology renaissance is likely to require more than high-speed access. One critical ingredient for high-tech firms is a skilled workforce. Thus, many high-tech firms locate in areas with amenities that are likely to attract professional workers. Surveys of scientists and engineers suggest that they prefer relatively large urban areas (or small areas with attractive amenities), with universities, good schools, and well-maintained public facilities (Malecki 1984). And the locational choices of high-tech firms bear this out. Nearly all the headquarters and research facilities of high-tech firms are located in metropolitan areas, and most are located near major universities or research centers (Malecki 1980; DeVol 1999).[15] This is again a natural way to find skilled workers, as well as a way to work with and gain help from academic researchers.

High-tech firms also gravitate towards other firms in similar or related industries. High-tech capital goods industries are the most concentrated of any in the United States, and births of new high-tech firms are most likely to occur in metropolitan areas that have larger numbers of existing firms in the industry (Schoonhoven and Eisenhardt 1992; Black and Henderson 1999).

There is growing evidence that such clustering is beneficial to firms, especially in information-intensive industries where potential "knowledge spillovers" are likely to be large (Rauch 1993; Glaeser et al. 1992; Jaffe et al. 1993). Firms near to one another are more likely to learn from one another about new products and techniques. Moreover,

[15] More fundamentally, all of the areas that have attracted high-tech have a large percentage of college graduates in the labor force (DeVol 1999).

clustering allows firms to draw from a shared pool of workers who have industry-specific skills. In particular, since workers can more easily find out about other opportunities and moving costs are low, clustering facilitates the transfer of workers from one firm to another. Thus, we end up with something of a virtuous cycle. It is the cities and regions that are fortunate enough to have had high-tech firms in the past that are the ones likely to attract more in the future (Krugman 1997).[16]

Because of the strength of these fundamental forces underlying location decisions, the conventional tools used to attract industry (low taxes, subsidies, and low-wage labor) may be especially weak in influencing the location decisions of high-tech firms. One study, for instance, found that variation in taxes and subsidies across metropolitan areas were completely unrelated to the location of high-technology manufacturing and services (O-hUallachain and Satterthwaite 1992).

In the short-term then, while high technology appears central to economic growth, it is not clear that cities – especially small cities -- can do much to promote it.[17] Much of what seems to be important to high tech industry, such as proximity to other firms and the characteristics of the labor force, is determined regionally, rather than inside the city limits. Thus, investing heavily in telecommunications infrastructure and subsidies seems

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[16] There are metropolitan areas that have recently gained a foothold in the high-tech industry without obvious natural advantages. Boise, Idaho and Sioux Falls, South Dakota, for instance, have managed to attract a number of high-tech manufacturers. But the firms that have moved there are largely branch plants that undertake more standardized forms of high-tech manufacturing, such as personal computer and accessory manufacturing (DeVol 1999). These metropolitan areas remain cost-effective production centers; they are not the dynamic, high-tech research and development centers that appear to generate such innovation and rapid growth.

[17] Certainly, federal government investment in research and development (and military spending in particular) had a great deal to do with the growth of Silicon Valley (Saxenian 1994). But Silicon Valley also had many natural advantages, including proximity to Stanford, proximity to San Francisco, and climate.

unwise. Moreover, cities should understand that high-tech growth and concentration comes with some costs. Offering few jobs for the middle-class, high technology growth is blamed by many for widening income disparities, inflating housing prices, and exacerbating other costs of growth (Saxenian 1994). Moreover, life cycles in technology products are short and are getting shorter, making this industry inherently volatile. Still, long-term prospects in this arena are critical, and clearly additional research is warranted to help us learn what local governments can do. Can cities attract high tech industry by investing in colleges and universities? And if so, what types of educational institutions make a difference? How important is the quality of secondary education? What is effectiveness of workforce development programs, of community colleges, of industry-college partnerships?

Promoting Tourism

City leaders spend considerable public resources on projects such as stadiums, convention centers, entertainment districts, and festival malls in an effort to attract tourists (Eisinger 2000; Judd and Fainstein1999). Ribbon ceremonies mean political capital for elected officials. And local leaders expect economic rejuvenation from increased tourists and middle class visitors. But a growing literature suggests expectations for these projects should be tempered considerably (Swindell and Rosentraub, 1998). Leaders must attend to the significant construction costs, public subsidies for operations and debt service, job creation projections, and increases in total regional entertainment spending that can be reasonably expected. We consider the case

of stadiums and casinos, but the lessons gleaned here can also be applied to the case of other projects, such as convention centers and festival marketplaces.

Promoting Tourism: Stadiums

One of the most popular strategies for fostering economic growth in cities is the construction of new sports stadiums and arenas. There are, after all, lots of sports fans and the notion of attracting droves of them into your city has considerable appeal. By investing in a new stadium, the argument goes, a city can generate economic activity – more jobs and more income due to purchases and employment both in the stadium itself and in the surrounding businesses that will thrive with increased activity. This additional economic activity will, in turn, generate increases in tax revenues sufficient to "pay for" the public investment in the stadium. Unfortunately, these rosy predictions are rarely borne out. First, a new stadium is expensive. Sports facilities now cost cities over $200 million on average (Noll and Zimbalist 1997). Two proposed stadiums along the Ohio River shore in Cincinnati are projected to cost more than $1.4 billion ("Interest…" 2000). Even minor league stadiums are costly. New York City, for instance, recently agreed to build a new minor league stadium in Staten Island at an expected cost of $76 million.[18]

Second, while attendance at sports events and revenues from tickets and related sales may, in fact, rise, they are likely to do so at the expense of businesses elsewhere in the area, such as movie theaters, bowling alleys, and restaurants. In principle, the increase

[18] Although the Staten Island proposal is unusually costly, other recent minor league stadiums have had hefty price tags as well. Consider that a recent stadium for a Triple A team in Lakewood, New Jersey cost $20 million, while a stadium for a Double A team in Round Rock, Texas cost $18.7 million. Class A parks

in economic activity at (or related to) the stadium could be sufficient to outweigh the loss in economic activity elsewhere. But the evidence suggests otherwise. Indeed, the finding that stadiums yield little or no economic growth is one of the few points on which there is almost unanimous agreement among economic researchers. The multiple analyses presented in Noll and Zimbalist (1997) find no significant impact of sports stadiums on either cities or metropolitan areas. Coates and Humphrey (1999), in fact, report that stadiums have *negative* effects on income. Further, the money paid to players in salaries rarely contributes to the city economy, since these athletes rarely live in the city where they play.

Of course, the location of a stadium within a metropolitan area may matter -- a basketball arena in downtown Washington, DC yields a different pattern of economic activity than an arena in suburban Maryland. Specifically, a stadium in downtown Washington means more of the benefits of the stadium would accrue to the District of Columbia itself, even assuming that the benefits to the metropolitan area as a whole are the same in both locations. Put simply, locating a stadium inside city limits may well be better for the city itself than a stadium located just outside its borders. With this said, the evidence suggests that stadiums are unlikely to have any significant impact even in their immediate neighborhood. (Rosentraub (1997))

Note that there is an alternative justification for public financing of stadiums and it could be a good one. One could argue that a stadium generates significant externalities that warrant public subsidy. That is, major league baseball may create a benefit accruing to people who are neither buyers nor sellers of the production of the game. There may be

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in Binghamton, New York, Norwich, Connecticut, and Dayton, Ohio, cost $4.8 million, $10 million, $20 million, respectively (Dwyer 1999).

taxpayers *who never attend a game or buy anything associated with the game* who nevertheless are willing to pay to prevent the team from relocating, or to have a team locate in their city. The presence of such an externality may cause the direct demand for games that is experienced by sports teams to understate the total value of sports to local consumers. It is difficult to quantify these consumption benefits, but one way to get some idea of their magnitude is to bring the issue to the ballot box. A referendum would give voters the opportunity to consider their personal preferences and express their willingness to pay for a stadium.

Promoting Tourism – The Casino Gamble

More and more cities are considering casino gambling as a winning economic development strategy. The continuing economic boom in the city of Las Vegas as well as the success of tribal casinos elsewhere fuels this enthusiasm.[19] City leaders in Detroit, for example, hope the new $225 MGM Grand Casino, which opened in August 1999, will jump-start its economic development - promising thousands of new jobs and $250 million in tax revenues over the next four years (Claiborne 1999). Joliet, Illinois and Buffalo, New York are also considering casinos for economic development (Ziemba 2000).

Certainly, Las Vegas has been a remarkable success. The gambling/hospitality industry created gross statewide revenues of almost $8 billion in 1997, and generated about $36.5 million in county-level revenues in fiscal year 1997 (NGISC 1999). As Las

[19] Casinos, and gambling more generally, are a revenue- and growth-generating strategy common to urban and non-urban localities; however, this discussion will consider the relevance of casinos as an economic development strategy for cities in particular. While the successes of Foxwoods gambling complex in southeastern Connecticut, for example, is important, its more remote location, outside of a major metropolitan area, limit its relevance for urban leaders considering casinos for economic development.

Vegas casinos profit and generate revenues, they have also been credited with the development of what is now the fastest growing city in the country. The population in metropolitan Las Vegas grew from 562,280 in 1985 to 1,036,290 in 1995 to over 1.25 million today.[20] And employment is rising at a similar pace. The unemployment rate in the metropolitan area was just 2.8% at the end of 1998 (NGISC 1999).

But policymakers considering casino gambling as economic development should be cautious before trying to recreate the Vegas success. Consider Atlantic City, New Jersey. The casino boardwalk there abuts on continued urban blight. In 1998, despite billions in private investment, the unemployment rate in Atlantic City stood at 12.7% - well above both the national rate and the rate for the rest of the state (NGISC, 7-11). The casinos employ largely outside workers, and little non-casino employment has been generated (Gross 1998; Sternlieb and Hughes 1983). Non-casino business has also continued to decline such that there is little within a few blocks of the Atlantic City boardwalk. And those remaining are mostly pawnshops, cash-for-gold stores and discount outlets.[21]

Unfortunately, there is little in the way of systematic research to determine why and when casinos succeed.[22] Legalized gambling is a relatively new phenomenon in the U.S.; therefore, research of its economic impacts is in its infancy. Further, much of the existing research is methodologically limited. It is, as always, extremely difficult to

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[20] Center for Business and Economic Research at the University of Nevada, Las Vegas website www.unlv.edu/research_centers/cber.

[21] This discussion has focused on the benefits in Las Vegas and Atlantic City. The concomitant costs of casinos, while difficult to quantify, are not minimal. Economic costs include the drain on public services such as roads, sewer systems, and water supply as well as the cost of increased crime and crime prevention.

[22] Gambling interests commissioned much of the research conducted to date, which raises serious questions about its objectivity. Eadington (1999) provides a very good introduction to the economics of casino gambling.

identify the independent impact of casino gambling on economic growth, because of the difficulty of determining what growth would have occurred in the absence of this policy change. In addition, fully accounting for the social costs of casino gambling – due to increased crime, compulsive gambling, and so on – presents a host of practical and conceptual problems that researchers are working to resolve.

Considering these two cases and the available economic literature, a few lessons emerge. First, casinos that draw revenues from outside of the local economy are more likely to spur economic growth. These casinos are not merely shifting around intra-jurisdictional entertainment spending but introducing new dollars.

Second, casinos that can draw such tourists for longer periods of time are more likely to fuel growth. Tourist gamblers, visiting for days at a time, spend considerably in the local economy during their stay. Destination casinos, offering restaurants, retail, recreation, and convention space along with a wide variety of gaming opportunities, are best able to compete (Rose Associates).

Further, the competitive structure of the casino market may be important in determining the impact of casinos on the local economy. Gazel (1998) argues that the local benefit will depend upon the extent to which the profits from the casinos are locally re-invested. If casinos have monopoly power, and their corporate owners are located elsewhere, as is true for most of the new casinos outside of Nevada and New Jersey, the economic development effects are especially likely to be small.

Consider again the cases of Las Vegas and Atlantic City. Located essentially in the middle of the desert, Las Vegas has always been a destination resort. By contrast, Atlantic City is within a few hour-drive of millions of residents. Therefore, most of its

gamblers are day-trippers spending little in the local economy. Certainly, casinos are generating profits and revenues, but money is not flowing into the local economy more broadly.

Las Vegas' success with casino-driven economic development is undeniable. But the conditions that created this mecca for gambling are rather exceptional and hard to replicate – as evidenced by the more limited success in Atlantic City. Indeed, much of the success of Las Vegas is no doubt due to simple fact that for years, Nevada was the only state in the country that permitted casino gambling. For decades, it was thus protected from competition. By the end of the 1990's, 27 states had permitted at least some form of casino gambling (Eadington 1999). The point is, policymakers must examine the nature of their city in particular – the location of potential competition, the prospects for attracting visitors -- when weighing the potential benefits and costs of promoting casinos.

Lessons

The first lesson is that the potential benefits of these strategies tend to be exaggerated in the popular press. These policies may be intuitively appealing, but in practice they are unlikely to be successful strategies for spurring economic growth in most cities. Consider infrastructure. While few would argue that adequate roads and highways are not critical to urban economic development, the stock of roads and highways in the US today is extensive, and it isn't clear that adding more at this point

will be beneficial. There are some cities constrained by inadequate infrastructure, but these are the exception, rather than the rule. Similarly, while excessive taxation may well serve to hamper growth, it is unlikely current tax levels are high enough that reducing taxes from existing levels will spur growth. Again, there may be some cities suffering from prohibitive taxes, but altering the *mix* of taxes, say, toward land value rather than property value taxes or toward user fees and congestion pricing, is likely to be more fruitful for the majority of cities.

Second, the conditions that make economic development strategies successful are complex. A whole confluence of factors (human capital; local institutions; federal government support; timing; proximity to other cities) may ultimately determine the success of a particular policy within a city. Unfortunately, it is very difficult to identify which the precise conditions critical to making a strategy a success in a particular place. Moreover, even if accurately identified, the conditions may be difficult or impossible to replicate.

Nonetheless, city leaders should do their best to understand their city's particular situation and to carefully evaluate the applicability of different strategies to the local environment. As an example, while creating casinos may successfully draw economic activity to isolated Native American reservations, the impact of casino gambling on cities is likely to be more modest.

Finally, policymakers should look beyond potential impacts on economic growth to consider the benefits of economic development policies and projects on the broader well being of their citizenry. Some economic development projects provide significant amenities that citizens value, and those should be factored into evaluations as well. Even

if a project fails to deliver the number of new jobs that had been hoped for, the city will be left with something of value to the community, i.e., a new school, new roads, or a sports arena that residents can enjoy.

Future Research

Perhaps the most important lesson that we hope to communicate is that there is still a great need for careful research. Significantly, for instance, most of the studies investigating the efficacy of these economic development strategies has focused on estimating impacts on states, metropolitan areas, and local jurisdictions (which include a broad range of localities including suburban and rural areas in addition to urban areas). There has, in contrast, been relatively little work investigating the policies and programs that serve to increase the economic growth and development of cities per se. Systematic research is needed to assist planners and policymakers who share the responsibility for urban economic development.

To be specific, we need additional research considering the efficacy of policies aimed at improving elementary and secondary education, reducing crime, improving colleges and universities, lowering or reforming taxes, that focus specifically on the impact of these policies on cities, per se.

Conclusion

This evidence catalogued in this paper suggests strongly that there are no 'magic bullets'. Changing the direction of a city's economy is difficult, and the factors that drive economic growth are frequently outside the scope of a mayor's ability to affect them.

Even policies that seem to work do so in small measure, creating marginal improvements that are never fully satisfying to a public looking for dramatic change. Still, this does not mean that local leaders should give up. It means that they need to work hard to design a strategy that is appropriate for their environment, and it means they should look beyond the strategies that we have discussed here. Appealing as they may be, these conventional policies typically yield disappointing results. Finally, we suggest a few alternative policies that may be more promising, though these too need to be carefully scrutinized and researched as they are adopted by cities in the future.

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