

1. Stephen R. Byers (Prof. Thomas D. Hopkins) Economics

Kearse Award honoree Stephen R. Byers regrets that he cannot be here today, but I nonetheless am pleased to introduce this author and his paper, entitled "Keeping Pace in a Global Economy: Pennsylvania's Perspective." Stephen now is in Pennsylvania completing his thesis for RIT's BS/MS Computer Engineering program. He has accepted a government position to start June 2008 and later plans to pursue an MBA. Stephen completed several RIT economics courses before writing this insightful and timely paper for a Fall 2007 Public Finance course. "Keeping Pace" clearly addresses the acute problem of economic distress afflicting much of the State of Pennsylvania. It then contrasts that somber story with the far more encouraging experience of one thriving western Pennsylvania county. Byers concludes: "Whether a state or county government can steer its own destiny or is just an unwitting victim or benefactor of external circumstances is uncertain, but where good planning meets opportunity, something is bound to happen." The author points out that, given our system of federalism, Butler County Pennsylvania's success in overcoming its economic challenges constitutes a case that much of the nation profitably could study. The paper is analytically sound, balanced, and well-crafted, amply deserving Kearse Award recognition.

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Keeping Pace in a Global Economy: Pennsylvania's Perspective

The confluence of the modern technological era and the enactment of national free trade policies, exposing domestic firms to direct foreign competition, has deleteriously compounded the challenges faced by America's older cities, small steel towns, and rural communities as they struggle to find their niche in the emerging global economy. The cascade effect of economic downturn is pronounced in western Pennsylvania, as a new generation of educated young adults moves away from family farms, small towns, and even larger cities in search of high-tech jobs and better opportunities. This paper will examine the policies and progress at the state and local levels in Pennsylvania designed to revitalize and retool, including taxation, incentives, education, and new corporate investment.

The dot-com bubble of the 1990s and early 2000 ushered in a dramatic expansion of digital connectivity in the United States. Telecommunications companies, relying on overly optimistic sales projections, laid expansive fiber optic networks with zeal, while high-tech startups run by a new generation of entrepreneurs challenged the brick and mortar establishment as they raked in the venture capital. Although the initial expansion collapsed, purchase of the resulting infrastructure and dark fiber at costs well below the original investment enabled the continuing exponential growth in internet bandwidth, the lifeblood of modern corporations. At the height of this activity in the years 1999 to 2000, however, the U.S. Census Bureau and Bureau of Labor Statistics ranked Pennsylvania first among the fifty states for absolute number of young workers

lost, and gave an equally gloomy assessment of business starts and economic growth, ranking Pennsylvania in the bottom ten [1]. In 2003, a study by the Metropolitan Policy Program at the Brookings Institution posits that Pennsylvania's population is also aging, ranked second for its share of citizens over the age of 65 [1]. The Keystone State, a once formidable producer of steel with a robust manufacturing and industrial presence, is losing the young talent, many graduating from its own world class Universities, sought after by high-tech firms in neighboring states.

In March 2007, Brookings released a follow-up to the alarming 2003 study and reiterated its recommendations, noting that while the state is still barely growing, a spirit of reform is spreading from Harrisburg to local communities [2]. Governor Rendell's "New PA" initiative, Keystone Principles for Growth, Investment, and Resource Conservation, and associated assimilation of plans by prior governors, seeks to spur investment and empowerment of local governments, and includes an online presence where businesses and citizens can "find everything you need to succeed in Pennsylvania" [3]. Progress on the economic competitiveness front includes the old staple of economic stimulus packages and tax breaks for new businesses, but addressing systemic problems takes a strong and sustained commitment to change, requiring broad public support, once thought difficult to forge across the multifaceted landscape of Pennsylvania.

Economic development and population growth within Pennsylvania over the last decade appears biased toward the southeast quadrant of the state. Figure 1 shows counties with a net population growth from 2000 to 2005 in blue, and those with a net population loss in red. A causal relationship between population shifts and job

creation, in effect, citizens moving across the state seeking employment, implying that one region's economic growth occurred at the expense of another, has not been explicitly proven in this case. However, overall unemployment in the state did fall by 2006 to levels on par with the national average [4] and the state's job growth ranking improved from 45th in the 1990s to 37th [5]. The Pennsylvania Economy League has shown that counties in the southeast have experienced a corresponding increase in fiscal health, although several counties in south central PA, which also experienced population growth, experienced declines in fiscal health comparable to northwest counties [2]. Although there appears to be a trend, there are always anomalous circumstances to consider, such as Butler County.

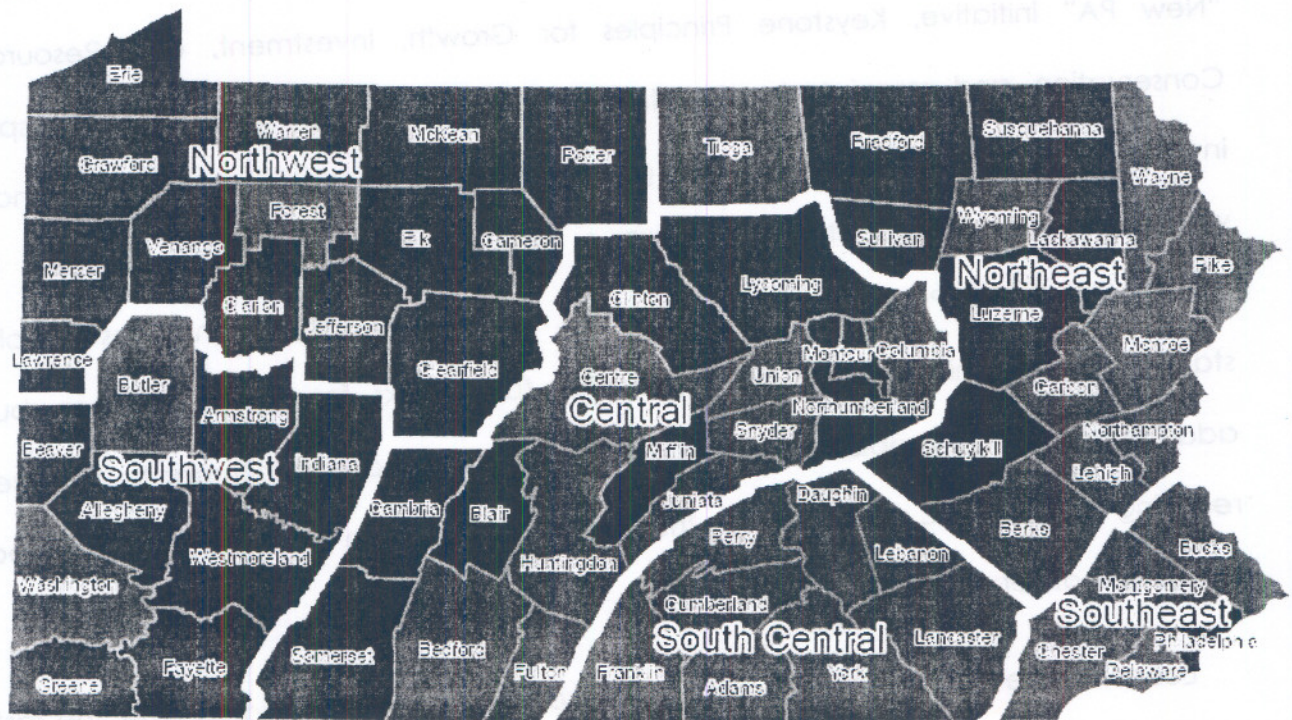


Figure 1 – U.S. Census Bureau, Population Change By County, 2000-2005

Once again, people continued to move out of Pennsylvania at a faster rate than they moved in, however the recent trend is small compared to the relative mass exodus of the 1990s (Figure 2).

The latest Brookings study points out that the trend of population spreading that saw cities lose nearly 5% of their population and second-class townships grow by nearly 12% in the 1990s has continued through 2000 to 2005, with cities losing another 3.3% of their population and rural areas hollowing out, losing 2.6% of their respective population [2]. The growth of second-class townships has had a corresponding boom on issuance of building permits in those areas, and housing developments continue swallowing up farmland at an alarming rate, even in areas not experiencing net population increases. Pittsburgh, a city in the southwestern quadrant, has only about half the population today as it did during its peak in the 1950s. With an unbalanced budget, more than a trillion dollars in debt, pressure to maintain city services, and an aging infrastructure, not to mention aging population, the city faces appreciable challenges.

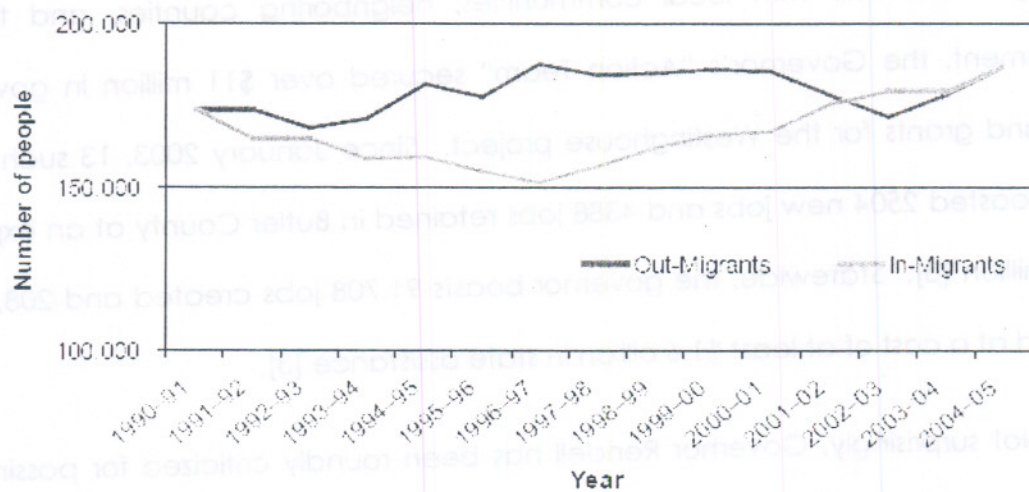


Figure 2 – Internal Revenue Service, County-County Migration Data

On the northern outskirts of Pittsburgh, however, is the bustling township of Cranberry, in Butler County. Classified as a second-class township, Cranberry has experienced significant population growth, 14.8 thousand to approximately 28 thousand people in the years 1990 to 2000 [9], and continues to expand. Westinghouse Electric Company recently announced plans to locate its headquarters and new engineering facilities in the area, creating over 900 new jobs and bringing the Westinghouse total to almost 4,500 employees in the western PA region [3]. Westinghouse Nuclear will have a strong presence and is poised to engineer and build the next generation of nuclear power plants in the United States and around the world. Governor Rendell used the groundbreaking as an opportunity to tout his "New PA" initiative as an instrumental factor in this economic development [3]:

"Without the strategic development areas legislation I signed into law last November, Westinghouse might have relocated out of Pennsylvania," Governor Rendell said. "This project serves as a clear example of how SDAs are already working to help companies not only stay in the commonwealth, but also to expand, encourage capital investment, and promote job creation and retention.

Working in concert with local communities, neighboring counties, and the state government, the Governor's "Action Team" secured over \$11 million in government loans and grants for the Westinghouse project. Since January 2003, 13 such projects have boasted 2504 new jobs and 4388 jobs retained in Butler County at an expense of \$46.6 million [3]. Statewide, the governor boasts 91,708 jobs created and 208,550 jobs retained at a cost of at least \$1.6 billion in state assistance [3].

Not surprisingly, Governor Rendell has been roundly criticized for passing large budgets in recent years. The 2006-2007 budget weighed in at \$55 billion, with a new

\$19.4 million line item for "regional development initiatives." Commentator Steven Voigt says with regard to this regional development initiative [8]:

"My friends who are close to the budget process characterize this fund as more duplicitous than obscure. With voters increasingly dissatisfied with business-as-usual politics and politicians who seem more interested in lobbying for legislative pay raises than finding creative solutions to improve Pennsylvania's economy, my friends tell me that this fund is nothing more than a bonanza give-away to try to please the districts and constituents of General Assembly members who march in step to the tune of present leadership."

"They tell me that reform-minded candidates on both sides of the aisle who place a higher priority on making the tough decisions required for economic progress than securing legislative pay raises and striving to be lifers in political office stand little chance of receiving grants for their districts from this \$19.4 million leadership-controlled fund."

Is Pennsylvania trying to spend its way to prosperity? Are these initiatives thinly veiled pork barrel spending? Steven's comments resonate with some in the state who harbor an intrinsic distrust of Harrisburg politicians following a history of sordid political scandals and charges of corruption. Of course, fiscal conservatives also keep a wary eye out for tax increases stemming from these large budgets that might threaten to derail future economic progress. The western half of the state is otherwise economically depressed, so do the residents of Cranberry owe the prosperity of the Butler area to the result of these focused initiatives, government grants, etc., or is there more to the story?

Certainly, tax breaks are attractive to any business, but one finds the ingredients of Cranberry's success mixed and coming to fruition well in advance of Governor Rendell's tenure. With cheap farmland and proximity to Pittsburgh and a major intersection of the Pennsylvania Turnpike, people and businesses chose to flock to the area, cyclically evolving the rural farming community into a modern regional powerhouse. The township decided rather early in 1989 to adopt a "Pay Your Own Way" philosophy, not entertaining abatements, subsidized public utility extensions, or other incentives that that might encourage sprawl [9]. The philosophy may have put

them at odds with other western PA municipalities eager for new development, however it was felt that these schemes were in effect, "buying development – and the hope for future tax revenues – by transferring large sums of taxpayer money into the private sector, frequently at the long-term expense ... of community welfare" [9]. Was the township relying on the state government to fund what it would not, or was the state spending its economic incentive money on an area and projects that already had momentum and would succeed regardless of external influences? No one knows if Westinghouse would have chosen to relocate elsewhere in the absence of government aid, but like any good business, Westinghouse knew they had leverage and skillfully used it against Governor Rendell's economic rejuvenation rhetoric to negotiate a better deal. In terms of fairness, Cranberry had it right when they prominently added, "maintain low taxes" to their revised strategic plan back in 1995, and not, as some might say, "maintain higher taxes, but give out lots of grants and tax deferrals to those businesses we deem arbitrarily acceptable or as payback for political favors."

According to the Bureau for Economic Analysis, the economic sectors in Pennsylvania that saw the biggest employment gains, education and health services, had lower average compensation compared to manufacturing jobs, which experienced steep declines [7]. The transition to non-manufacturing jobs will be difficult for many who grew up in an era where a high school diploma was sufficient and one expected to work in the steel mill or factory as long as they were able. For those families whose sons and daughters transition away from farming or whose farm turns insolvent, they at least have the equity of their land, machinery, and cattle with which to provide for retirement or pay for school.

Pennsylvania is indeed blessed with many excellent public schools and boasts a high school graduation rate of 86.7%, compared to a national rate of 84.2% [2]. While the state lags behind in percentage of adults who attained college degrees nationally, the trend shows yearly improvement and the state is home to several distinguished universities and colleges, such as The University of Pennsylvania. Salary tends to correlate with education, and average compensation in the state was slightly lower than the national average of \$49,777 in 2005, although neighboring New York and Maryland had significantly higher averages at \$62,100 and 54,700, respectively, leading to a regional disparity of concern to some commentators [2].

There is more to the story than nominal salaries; relative cost of living differences between two areas has a tremendous impact on real spending power. According to the latest data available, a \$48,000 per year salary in Pittsburgh, PA, the state average, is equivalent to a \$60,000 per year salary in Baltimore, MD, with housing at least 60% more expensive [6]. Philadelphia has a similar cost of living compared to Baltimore, but both are dwarfed in comparison to bigger cities such as Los Angeles, CA or New York, NY, where the equivalent cost of living in Manhattan is a staggering \$103,600 per year [6]. Perhaps Pennsylvanians enjoy country living for more than the peace and quiet.

The problem of fiscal distress remains, however, in those municipalities who are not one of the Cranberry's of PA. According to a report by the Pennsylvania Economy League, the majority of cities, boroughs, and first-class townships have seen a general trend of declining fiscal health since the 1970s, although second-class townships usually fared better [10]. If the economic competitiveness of the larger state is tied to the quality of services and competitiveness of the individual local municipalities, promoting

sound economic development and governance at the local level is as important to overall economic growth as statewide policies and initiatives. One thing is clear, current state gambling initiatives to fund public education or casinos authorized and built with the promise of solving citywide budget deficits are not living up to the promises made by Harrisburg when convincing the public to vote for such schemes. Band-aid solutions are not what the doctor ordered.

In summary, the Agenda to Renew Pennsylvania, as presented by Brookings, reiterates the following priorities for reform [2]:

1. Empower local governments
2. Continue making reinvestment a priority
3. Continue strategic investment in key industries

The revival of the State Planning Board in late 2003 was seen as a critical step toward coordinated economic planning and suggested several reforms for passage by the General Assembly in support of the Agenda to Renew Pennsylvania priorities. One promising recommendation involves changes in the law, making it easier for local municipalities to consolidate and/or share services, such as police departments or water treatment. Economies of scale could be leveraged to provide key government services across local governance boundaries at an overall reduced cost. While reducing layers of redundant bureaucracy and inefficiency is laudable, local communities take pride in their schools and control they have over public services. Other recommendations carry a similar theme, consolidation of local governments, allowing for easier redrawing of district lines, implementing a streamlined tax collection system, and consolidation of municipal pensions at the state level [2]. Even the

Pennsylvania Department of Transportation has re-evaluated its priorities and shifted funding from new highway projects toward strategic investments and better maintenance of existing infrastructure. Whether a state or government can steer its own destiny or is just an unwitting victim or benefactor of external circumstances is uncertain, but where good planning meets opportunity, something is bound to happen. Federalism indeed offers the best case study and one would be wise to study those states and counties who have successfully capitalized on the twenty first century.

References

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