Community Development, Economic Development, or Community Economic Development?

Concepts, Tools and Practices

Location Theory: Business Climate

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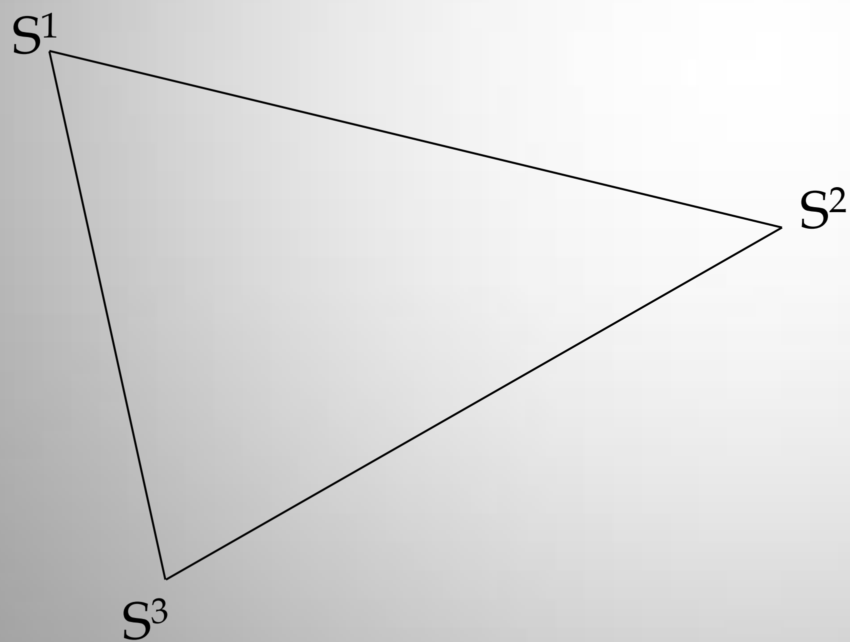
Location Theory:
Business Climate

In neoclassical location theory we found that firms often go through a two step process. The first step is to select a general region somewhere between input suppliers and output markets.

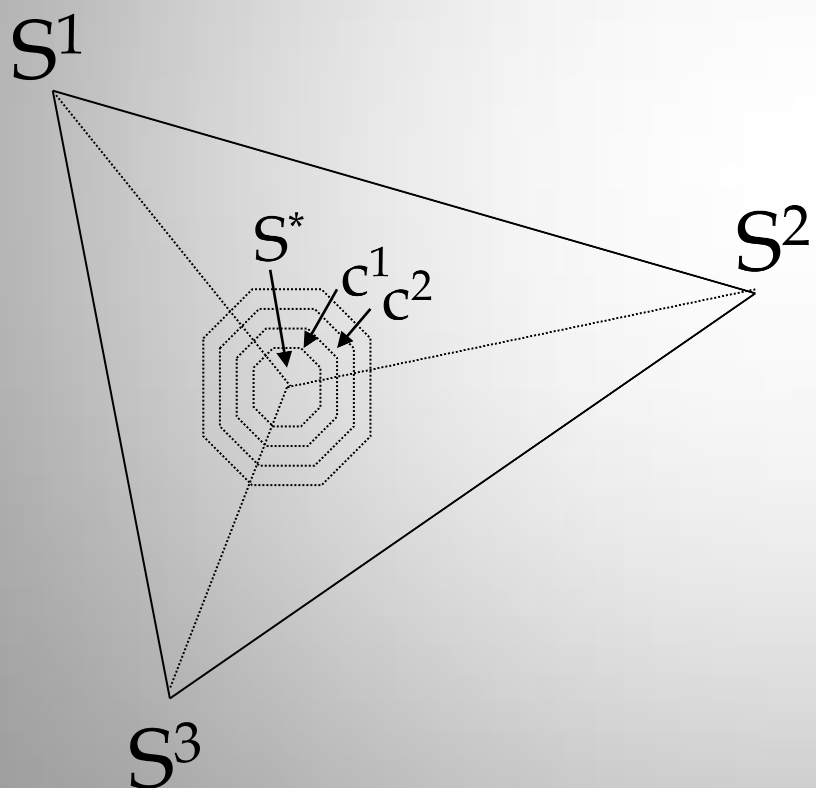


In this example the firm must pick a location somewhere between markets S^1, S^2 and S^3. This could be Chicago, St. Louis and the Twin Cities.

The community has little if any influence on their geographic location.

Location Theory:
Business Climate

In the <u>second step</u> the firm must pick a specific location. Here the firm will be looking at things like real estate costs, labor costs and taxes.



Within this framework firms are looking to minimize costs in order to maximize profits. So while the location S^* may be the transportation cost minimizing location, but lower costs at C^2 may more than compensate for slightly higher transportation costs.

Location Theory:
Business Climate

<u>It is in this second stage of the location decision-making process that communities often have some influence on firm location decisions.</u>

In a “cost minimization” (in order to maximize profits) world, what are the policy options?   Think in terms of “business climate”.

- **Cheap labor**
- **Low taxes**
- **Limited regulation**

Business Climate?

Location Theory:
Business Climate

The International Economic Development Council:

Business climate indicates how states state, regional and local policies, relationships and local communities support business development. Ultimately, a good business climate allows businesses to conduct their affairs with *minimal interference* while accessing quality high inputs and customers at *low costs*.

Location Theory:
Business Climate

This way of thinking dominated the "First Wave" of economic development thinking……..the Mississippi Balance Agriculture with Industry Act (BAWI) policies of the Great Depression era laid the foundation for the "new war between the states".

Strategies ➔ Focus on business recruitment
(aka smoke stack chasing)
Low land and labor costs, low taxes, and limited regulations.

Tax incentives and give-aways like free land/buildings.

Location Theory: Business Climate

Countless number of companies-consultants have developed measures or indices of business climate:

- Fantus Company
- Grant Thornton
- Small Business and Entrepreneurship Council
- Beacon Hill Institute
- Progressive Policy Institute
- Fraser Institute and the National Center for Policy Analysis
- Corporation for Enterprise Development
- And many many others

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Location Theory:
Business Climate

Countless number of companies-consultants that have developed measures or indices of business climate:

There are problems with these different measures:

1. **There is little consistency across the different measures.**

2. **None are satisfactory predictors of economic growth.**

We have really had to rethink what we mean by business climate.

Location Theory:
Business Climate

Since the introduction of the Mississippi Balance Agriculture with Industry Act (BAWI) and the narrowly focused view of Business Climate narrowly as the cost of doing business two things have happened:

1. The structure of the economy has changed from being dominated by large manufacturing firms to a service based economy with most job growth coming from smaller firms.

2. Our theoretical understanding of what drives firm location decisions has become more refined which in turn leads to more refined thinking about policies communities can pursue.

Location Theory:
Business Climate

Increasingly, firms are looking for:

- **High quality infrastructure (broadband)**
- **Quality public services such as police/fire protection**
- **Skilled labor**
- **Consistency in rules-regulations**
- **Generally high quality of life characteristics**

and not only offer low cost alternatives for the firm but, more importantly, offer a viable comparative advantage over other locations.

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Location Theory:
Business Climate

<u>The balance between taxes and services</u>:

Research has suggested two things: (1) taxes are "bad" for firm location but (2) public services are "good" for firm location.

The "trick" is the proper balance between taxes and services. Unfortunately the proper balance varies across different types of industries and businesses.

Research also suggests that (1) if people/businesses believe that they are <u>not</u> getting the services they are paying for, then a problem is present and (2) as the economy grows the demand for public services grows, but the growth in the public sector should be slower than the overall economy.

Location Theory:
Business Climate

The "truth" about firm location and regulations:

The traditional view is that businesses incur costs to meet regulations, and as a result will avoid places with regulations.

The "behavioral approach" to firm location tells us that some *regulations can remove risk and uncertainty* (firms know what they can and cannot do).

But, inconsistent regulations or what appears to be randomly changing regulations not only causes uncertainty but can increase the costs (costs to comply with random changes in regulations).

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Business Climate

- **What complicates the problem is that firms in different industries look at different factors.**
- **No two industries are exactly alike and as such they look at different factors in the second stage.**
- **For example, firms that are seeking high skilled professionals (e.g., engineers, computer scientists, etc.) will look at things like quality of life while other firms, such as food processors, are more concerned with access to input supplies and labor costs.**

One must avoid blanket generalizations!

Location Theory:
Business Climate

Business Climate has more to do with the "attitude of the community";

- **Willingness to work together**
- **Willingness to experiment**
- **Willingness to learn from mistakes**
- **Willingness to look within**

Is the community entrepreneurial?

Location Theory: Business Climate

"Community entrepreneurs" can essentially be viewed as mobilizers of networks. They can mobilize internal networks within the community as well as external networks. Networks help individuals to know what, how, when, who, and why. This includes the ability to tap into the "right people" to help solve a community problem. These people can be inside or outside the community itself.

Location Theory:
Business Climate

An "entrepreneurial community" probably has a greater capacity to adjust to constantly changing economic conditions surrounding it. They learn from their own and other's mistakes. They rely on successful colleagues/communities as role models. They recognize that there is no cookbook because of the uniqueness of each and every community and situation. They also realize that the community economic development process is the long-term envelope of short-term projects and is in need of constant reevaluation.

Location Theory:
Business Climate

"Community entrepreneurs" create an acceptance of rebirth. They help create the visions and convincingly communicate that vision to local and non-local networks. These are visions of new comparative advantages. Finally, they integrate community resources, people, and networks. Community entrepreneurs are engaged in managing turbulent organizational change and deciphering complexity.

Location Theory:
Business Climate

The "successful" community will think of business climate not as the *low road* via low taxes, cheap labor and land and no regulations, but rather through the "high road" of the entrepreneurial spirit of experimentation, learning, networking, and adjusting to unique situations.

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