ALLEGHENY INSTITUTE
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Pennsylvania's Ever-Expanding Economic Development Industry

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Key Findings

- The Governor's stimulus plan involves $2.3 billion in grants, loans, and guarantees in order to generate $5 billion in private sector investment. In other words, the stimulus would rely on $1 in public money for every $2.50 in private dollars.

- Also looked at another way, the state is planning to "invest" about $185 for every Pennsylvanian over the three-year time frame in order to once again attempt to jump start the state's economic performance.

- From 2003 through the end of 2005, $1.24 billion has been spent on economic development functions.

- The seven-county Pittsburgh metro area received $283 million--$118 per capita--in economic development funding from 2003 through 2005. Of this total, $171 million, which represents 60 percent of the metro area total and 14 percent of the state total of $1.24 billion, was awarded in Allegheny County.

- It is nearly impossible to determine whether the state's efforts actually cause jobs to be created or retained, to take punitive measures if the projections of the recipients come to pass, or to claim that the state's overall performance is related to economic development spending. Despite these facts, spending persists.

- Despite the efforts of the administration to claim their job creating programs have produced the meager increase in jobs since 2003, the evidence does not support this claim.

Introduction

Pennsylvania is no stranger to handing out public money in its pursuit to build communities, develop infrastructure, and help companies create and retain jobs in the state. In fact, one could say that the state has quite a deep affection for economic development. This is certainly shown in the "alphabet soup" of programs available to stimulate the private sector.

For all of the questions surrounding its effectiveness, job creation programs have tremendous staying power. Regardless of party affiliation, regardless of the number of legislators and governors that come and go, economic development remains. In fact, it often expands. The current administration's efforts have been bolstered by the passage of new programs in 2004 that aim to help promote site development, venture capital firms, tourism, agriculture, and water supply to chase down private dollars.

Though dubious, the administration has made, and continues to make, claims that its stimulus program is directly responsible for pushing Pennsylvania to an all time high in job totals and for depressing the unemployment rate. [1] Even if all of the job growth were solely attributable to the economic development spending, its dollars spent per job created ratio would be far from cost-effective.

Much like other states, Pennsylvania is using the economic development programs at its disposal to reward favored companies and to compensate for the issues that are really the root causes of slow growth: taxes, regulations, and bad labor climate.[2] Don't look for these core issues to be addressed anytime soon. But do expect the state to continue its practice of doling out dollars as it tries to spur economic growth. The ultimate irony is that for all of the spending on economic development, Pennsylvania's employment creation continues to languish.

This report examines the state's economic development spending patterns from 2003 through the end of 2005. By using the press releases of actual economic development award announcements[3], it chronicles the spending by metro areas, with detail on awards in the Pittsburgh metropolitan area, and, specifically, Allegheny County. It also presents some background on the sources of the money, when those sources were created, and the purpose for which the money is awarded.

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[1] Office of the Governor of Pennsylvania (www.governor.state.pa.us)

[2] For instance, Ohio voters approved Issue 1 in November of 2005 to spend $2 billion on traditional infrastructure ($1.35 billion), the expansion of a program called the Third Frontier that involves investing in new start up enterprises ($500 million) and the development of business sites that will be ready for companies to occupy ($150 million). See David Hansen "Ohio Voters Approve $2 Billion Jobs for Ohio Plan" in Budget and Tax News (www.heartland.org)

[3] News releases archived on (www.governor.state.pa.us). All data on location, dollar amount, source(s) of money and date contained in this report came from the releases.

How Much Money?

After being elected and taking office, the Governor's stimulus plan began to take shape: $2.3 billion in grants, loans, and guarantees in order to generate $5 billion in private sector investment. In other words, the stimulus would rely on $1 in public money for every $2.50 in private dollars. Also looked at another way, the state is planning to "invest" about $185 for every Pennsylvanian over the three-year time frame in order to once again attempt to jump start the state's economic performance.

From 2003 through the end of 2005, about half of that amount has been spent. The $1.24 billion expended has gone to companies for a variety of purposes and in a variety of places around the state. It has come through programs created decades ago as well as newly established ones.

Where Has the Money Gone?

By Metro Area

There are 13 "Pennsylvania based" metropolitan areas that consist of over 10 million people. The remainder of the state--just about 2.5 million people--resides in counties not attached to one of those metros. The table on the next page shows these areas, the counties that comprise each area, and the total amounts for each. The table is ranked in descending order based on per-capita amounts.[4]

As is evident from the table, the Johnstown metro area has been by far the biggest beneficiary of the state's recent years of economic development spending, netting $195 on a per person basis. This is four times as many dollars as the per capita amount from the York metro area. On average, the per capita amount spent in these 13 metro areas and the 33 non-metro counties was $111. The Pittsburgh metro received slightly above the average, with Johnstown, Erie, and Lebanon taking in amounts well above average.

Pittsburgh Metro Area and Allegheny County

The seven-county Pittsburgh metro area received $283 million--$118 per capita--in economic development funding from 2003 through 2005. Of this total, $171 million, which represents 60 percent of the metro area total and 14 percent of the state total of $1.24 billion, was awarded in Allegheny County.

[4] List of metro areas from the U.S. Census State and Metropolitan Data Book (www.census.gov) and the Pennsylvania State Data Center (www.pasdc.hbg.psu.edu). For the Philadelphia metro area, only the Pennsylvania portion of its population was counted in order to get per-capita amounts. And though there are metro areas from other states that contain Pennsylvania counties, those counties are treated as not belonging to a metro area in this analysis.

Economic Development Spending By Metro Area

Metro	Counties in Metro	$ Amount (000s)	Population (000s)	Per Capita
Johnstown	Cambria	$ 29,000	149	$ 195
Erie	Erie	$ 40,400	280	$ 144
Lebanon	Lebanon	$ 16,800	123	$ 137
Williamsport	Lycoming	$ 14,700	118	$ 125
State College	Centre	$ 17,100	142	$ 120
Pittsburgh	Allegheny, Armstrong, Beaver, Butler, Fayette, Washington, Westmoreland	$ 283,600	2410	$ 118
None	33 Counties not assigned to a PA metro	$ 228,000	2041	$ 112
Altoona	Blair	$ 13,200	127	$ 104
Lancaster	Lancaster	$ 49,300	483	$ 102
Scranton-Wilkes Barre	Lackawanna, Luzerne, Wyoming	$ 51,900	552	$ 94
Allentown-Bethlehem-Easton	Carbon, Lehigh, Northhampton	$ 69,700	768	$ 91
Philadelphia	Bucks, Chester, Delaware, Montgomery, Philadelphia	$ 322,600	3875	$ 83
Harrisburg	Cumberland, Dauphin, Perry	$ 42,900	517	$ 83
York	York	$ 18,200	395	$ 46

The largest award announcements (ranked by total dollar amount per announcement) in Allegheny County were:

- August of 2004--$73 million from Redevelopment Assistance Capital Program for various redevelopment projects in the city of Pittsburgh and in the remainder of Allegheny County. These projects included dollars for Nine Mile Run, South Side Works, Children's Hospital, brownfield redevelopment in McKeesport and other Mon Valley sites
- November of 2005--$12.2 million from a combined package of PennWorks, TIF Guarantee, and Base Retention grant for Pittsburgh International Airport
- July of 2005--$10.8 million in a combined package from Infrastructure Development Program, Opportunity Grant, Job Creation Tax Credits, and Customized Job Training for Dick's Sporting Goods
- November of 2005--$8 million from the Business in Our Sites Program for East Liberty site development
- April of 2005--$6.9 million from PennWorks to Pittsburgh International Airport
- October of 2005--$6.4 million in a combined package from Pennsylvania Industrial Development Authority, Opportunity Grant, Customized Job Training, and Job Creation Tax Credit for American Eagle Outfitters new headquarters in

the South Side Works development--a development that has already received an infusion of public money

- January of 2005--$6 million from Business in Our Sites for Airport Business Park
- April of 2004--$5 million from the Redevelopment Assistance Capital Program for Schenley Park redevelopment
- November of 2005--$5 million from the Venture Capital Investment Fund for Draper Triangle
- November of 2005--$4.6 million from PennVest for sewer improvements in Sewickley

This goes without counting what promises to be a significant, $30 million gift from the state for the PNC Three Plaza that is to be developed in downtown Pittsburgh. Though there has been a general statement of commitment of state money, there is no clear word of the exact source of the money.[5] Past awards for the stadiums and convention center construction also push up the dollar total for the county.

The Sources of the Spending

As stated in the outset of the report, the state has quite an arsenal of economic development programs at its disposal. Most are under the auspices of the Department of Community and Economic Development. The Redevelopment Assistance Capital Program is administered by the Office of the Budget. Some of the programs have been around for quite some time: the Pennsylvania Industrial Development Authority (PIDA) goes back to Act 537 of 1955. The late 1980s and the 1990s saw the enactment of the Machinery and Equipment Loan Fund, the Opportunity Grant, Job Creation Tax Credits, and Customized Job Credits.[6]

The most recent ramping up of economic development came in 2004 with the passage of Act 22 and the approval of a statewide referendum on water and wastewater infrastructure. The major programs created in Act 22[7] were:

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[5] Mark Belko "PNC to Build Skyscraper on Fifth Avenue, May Trigger Downtown Revival" Pittsburgh Post-Gazette, December 20, 2005. Article notes "Governor Ed Rendell has pledged $30 million through various state funding streams."

[6] Legislative Budget and Finance Committee Report "Department of Community and Economic Development: Economic Development Programs" October, 2000. Customized Job Training Program created by Act 116, 1985; Infrastructure Development Program, Act 116 of 1996; Job Creation Tax Credits, Act 100 of 1998; Machinery and Equipment Loan Fund, Act 120 of 1988; Opportunity Grant, Act 67 of 1996; Pennsylvania Industrial Development Authority, Act 537 of 1955; Pennsylvania Infrastructure Investment Authority (PennVEST), Act 16 of 1988; Small Business First, Act 100 of 1998.

[7] Pennsylvania General Assembly, Act 22 of 2004. There are other programs listed in the Governor's stimulus program, including Building PA, Base Development, Core Industries, and others. Most of the expansion was done as a way to "make up" for forgetting certain aspects of the economy or developments. For instance, the DCED description of the First Industries Fund notes that "agriculture and tourism are Pennsylvania's two largest industry segments. Yet, historically, the Commonwealth has provided little in the way of financial incentives to help them with the purchase of assets or capitalization needs". One must wonder if anyone at the state realized that perhaps part of the reason agriculture and tourism grew to the point of being large industries was because there was little or no intervention.

- Business in Our Sites--Empowers communities to attract growing and expanding businesses by helping them build an inventory of ready sites
- First Industries Fund--A program aimed at strengthening Pennsylvania's agriculture and tourism industries
- Housing and Redevelopment Assistance--Program assisting communities in becoming competitive for business retention, expansion, and attraction
- Venture Capital Investment Program--Loans to venture capital fund managers to invest in young Pennsylvania research and development companies
- Venture Guarantee Program--Loan guarantees to venture companies for investments in entrepreneurs and young companies
- Second Stage Loan Program--Loan guarantees for working capital for two to eight year old manufacturing, biotech, and technology-oriented companies

The state is also expanding its reach into being a guarantor for tax increment finance projects by pledging its credit (up to $5 million per project) as a way to lower risks on redevelopment projects, and with other non-TIF projects through the Infrastructure and Facilities Improvement Program. The Water Supply and Wastewater Infrastructure Program (PennWorks) was put into place after approval on a statewide referendum question in April of 2004.[8]

Most important, perhaps, was that Act 22 also created the Commonwealth Financing Authority, a seven-member board that is described as an "independent agency of the Commonwealth to administer Pennsylvania's economic stimulus packages. The authority holds fiduciary responsibility over the funding of programs and investments in Pennsylvania's growth".[9] Three of the members are the Secretaries of the Departments of Banking, Budget, and Community and Economic Development, the four others being legislative appointees.

Dividing the $1.2 billion up among the sources from which the money was derived gives an idea of what the state places value on: specific sources of money are tied to specific uses.

Here are the sources from where the bulk of the money came:

- $415 million, 33% of total, awarded solely from the Redevelopment Assistance Capital Program, which is used for economic development and the prevention of

[8] Department of Community and Economic Development (www.newpa.com). It is of interest to note that there appears to be a discrepancy between the language of the referendum question and the terms and uses of Penn Works funds in the DCED guidelines. The question--which passed with 63 percent of the vote in 2004--asked "Do you favor the incurring of indebtedness by the Commonwealth in the amount of $250,000,000 for use as grants and loans for construction, expansion, and improvement of water and wastewater infrastructure including water supply and sewage treatment systems?" The DCED guidelines note that Penn Works funds can be used for "water and sewer projects not used solely for residential purposes" and its terms state "the project must serve a site or sites being prepared for economic development activities which involve the investment of capital in Pennsylvania enterprises and communities or which results in the creation of new or the preservation of existing jobs".
[9] Ibid

blight. As mentioned above, this program is administered by the Office of the Budget and does not appear to have any limit on the amount of the award. Our 2003 report documented the allocations made under this program in the Pittsburgh metro area, with the majority dedicated to funding the professional sports stadiums in Pittsburgh.[10]

- $217 million, 21% of total, was from what is termed multiple sources, meaning projects that received an award split up among various sources. The most common combination of awards was between the state's Opportunity Grant, Job Creation Tax Credits, Customized Job Training, and Machinery and Equipment Loan Fund, but in some cases also included PIDA loans, RACP funds, or Small Business First funds
- $146 million, 12% of total, awarded solely through the Business in Our Sites program, which is dedicated to creating shovel ready sites throughout the Commonwealth
- $87 million, or 7%, awarded solely through the Pennsylvania Industrial Development Authority, commonly known as PIDA.
- $60 million, or 5%, awarded solely through the Pennsylvania Water and Wastewater Infrastructure Program (PennWorks)

It is interesting to note that the five categories above represented nearly 80 percent of all the money given out and that the money funneled through Business in Our Sites and Penn Works are newly created programs with the money only being handed out in 2005.

The remainder of the awards came through various funding streams. Here are the smaller amounts handed out from the programs created in 2004:

- $29.5 million, or 2% of the total spent, awarded solely through the Venture Capital Investment Program
- Infrastructure and Facilities Improvement Program ($13.8 million, 1% of total),
- First Industries Fund ($10.9 million, 0.8% of total),
- Housing and Redevelopment Assistance ($2.9 million, 0.2% of total),
- Second Stage Loan Program ($125,000, 0.01% of total)

What Effects?

We have pointed out that spending on economic development often yields negligible results: sometimes the promised jobs never materialize, it is hard to assess the real effect if they do, and it is difficult to connect economic development as a causal factor of economic growth.

What Happens if Jobs aren't Produced?

The problem here is that there is little, if any, clawback provisions that make the company receiving the award give it back. Awarding economic development dollars is

[10] Allegheny Institute for Public Policy Report # 03-04 "Hoping for Growth: An Analysis of Government Development Expenditures"

often done on the basis of the jobs anticipated, and not on what is actually created. For instance, take the summation of the activities of the Governor's Action Team, a group of economic development professionals that report directly to the chief executive. "In 2005, the Governor's Action Team completed 206 projects that resulted *in commitments* for 20,257 new jobs and the retention of 40,556 existing jobs"(emphasis added). What can be done if those commitments fail to come to pass is anyone's guess.

There is also the issue of how much it costs the state to produce those committed jobs--the same note about the Governor's Action Team says that $421 million in assistance was leveraged (this number likely does not count programs like the RACP, PennVEST, or others not overseen by GAT) to get those 60 thousand jobs created or retained. On a per job basis, that amounts to $6,922.

How Will We Know if the Efforts are Having an Impact?

Unless each and every economic development project is tracked and then dissected to see whether the promises come to pass, there is really no way to know if the jobs were created. But one would think that if the state truly believed in their efforts to stimulate the economy, they would do more to assess and publicize the fruits of their labor. But they really do not. It bears repeating the findings of the 2000 LBFC study:

> "Assessing the impact of an economic development program is difficult, and the procedures for collecting performance information for DCED's economic development programs currently range from rigorous to none. DCED often reports information on jobs created and retained by the various programs, but this information frequently only represents what the applicant anticipates being created or retained at the time the application is submitted. DCED often subsequently reports information based on reports submitted by company officials after the project is completed, but does not routinely verify the accuracy of the reported jobs data".[11]

So it is an almost impossible task to determine whether jobs were really created or retained, if the state money was used to create or retain those specific jobs, or whether beneficiaries are even telling the truth.

"Growth" In PA: A Result of the Stimulus?

Has the economic development juggernaut in Pennsylvania turned the state around? The administration certainly believes so. According to the Governor's accomplishments on the state's website:

> "[The] stimulus plan works. In May of 2005, the number of employed Pennsylvanians reached an all time high of 6,045,000--an increase of 28,000 over the record set in April and 200,000 more than when Governor Rendell took office in 2003. Additionally, the statewide unemployment rate dropped below 5 percent

[11] Legislative Budget and Finance Committee report

> for the first time since April of 2001 and the state gained jobs in the good producing and service providing sectors in three consecutive months for the first time in a decade. Largest gains were in the construction sector, which added 2,700 new workers in May, reaching an all time record high of 256,300. While we might see some fluctuation in the unemployment rate in the coming months, May employment numbers provided proof of our economic development successes, and evidence that these encouraging trends will continue."

The fact that the nation has enjoyed a long period of low interest rates and very stimulative tax rate cuts is undoubtedly responsible for a significant portion of the state's relatively meager job gain. Most of the industry sectors showing the biggest job increases were not the beneficiaries of government largesse and grew for other reasons as dictated by market forces. For instance, a press release noted that three service providing industries set or matched record high job counts. These industries--professional and business services, education and health services, and leisure and hospitality services--are not areas that are recipients of much of the state's development dollars.

It would not be at all surprising to see an increase in construction jobs--after all, much of the economic development award money is based on building new structures in the pursuit of eradicating blight and stimulating development. Officials always connect building and construction as progress: instead, what they are really doing is confusing activity with growth. Instead of real and positive economic growth, state spending often leads to glitzy new structures that have negligible long-term impacts on economic activity.

But the track of the administration is not to say whether a certain subsidy released in a certain month to a certain company created or retained the jobs they were supposed to, but rather on the anticipated jobs or the performance of the state economy as a whole, not taking into account other possible causes for growth. In this way, economic development spending is truly a no lose situation, at least politically.

It is also instructive to examine the jobs creation issue at the regional level. There seems to be no real pattern between the state spending and changes in non-farm employment levels. Despite the huge sums of money pumped into the Pittsburgh and Philadelphia metro areas, both lost jobs over the three-year time frame ending in November of 2005. York--despite having the lowest per-capita spending on economic development, grew 5.8 percent. The third highest metro in level of spending (Lebanon metro) had the highest percentage change in non-farm employment (8.05%). The highest metro in spending, Johnstown, experienced a growth rate that is virtually indistinguishable from the Allentown-Bethlehem metro (3.2% vs. 3.5%), yet the latter received nearly $100 less per-capita in economic development money.

Conclusion

All told, the evidence is pretty clear. Pouring huge sums of state taxpayer money into selected projects has had little, if any, positive impact on Pennsylvania's job totals. And little wonder. Pennsylvania's business climate does not compare favorably with other states and parts of the world in terms of being attractive to capital spending. High tax rates, overly restrictive regulations, unions and unfavorable labor laws all raise the cost of doing business in Pennsylvania, which lowers the return on investment. Plans to raise the minimum wage in the state above Federal levels also put Pennsylvania at a competitive disadvantage. Lower returns lead to weaker private investment and slow employment growth.

The strategy of picking projects to pour taxpayer money into does nothing to address the business climate problem. Indeed, it makes it worse. First, if tax dollars are being handed out to some businesses, non-subsidized businesses are being forced to contribute through the taxes they pay. Second, these handouts to selected firms put unsubsidized firms at a competitive disadvantage and could lead to lower investment and job formation at those firms than would have otherwise been the case. There is no free lunch.

Third, to the degree that the state subsidies lead to private investment in projects that would not have happened without the taxpayer money because the return on investment would have been too low, then the subsidy is producing a misallocation of capital resources. Fourth, the program of handouts weakens the private sector by creating a group of businesses that believe they are entitled to special treatment by government--a group that will grow inexorably larger over time to the state's great detriment. Finally, it must be recognized once and for all that the government can never be a substitute for the market when in it comes to efficient allocation of resources.

Among the states, Pennsylvania has long ranked as one of the top per capita spenders on jobs creation programs and yet it has continued to languish as one of the weaker performers in terms of employment gains. Doesn't common sense suggest it's time to try something else? In this case, a tried and true method of encouraging the private sector is to make significant business tax cuts.