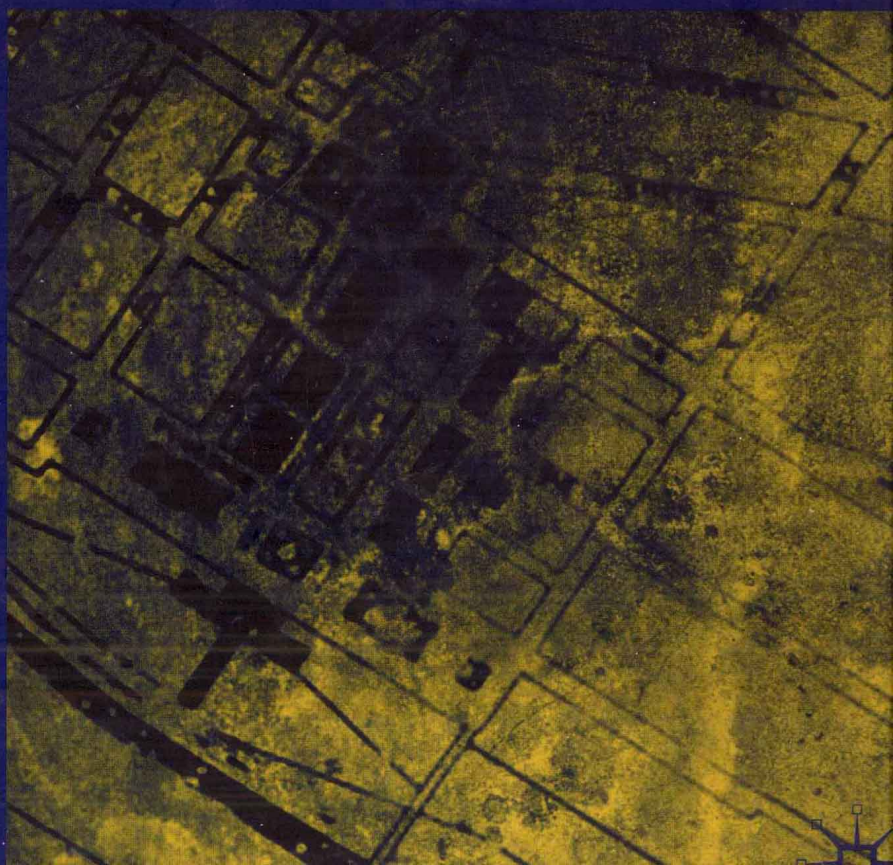


INCENTIVES FOR REGIONAL DEVELOPMENT

Competition Among Sub-National Government

Kala Seetharam Sridhar

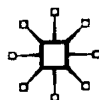


Incentives for Regional Development

**Competition Among Sub-National
Governments**

Kala Seetharam Sridhar

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First published in 2005 by

PALGRAVE MACMILLAN

Houndmills, Basingstoke, Hampshire RG21 6XS and

175 Fifth Avenue, New York, N.Y. 10010

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ISBN-13: 978-1-4039-4788-8

ISBN-10: 1-4039-4788-0

This book is printed on paper suitable for recycling and made from fully managed and sustained forest sources.

A catalogue record for this book is available from the British Library.

Library of Congress Cataloging-in-Publication Data

Sridhar, Kala Seetharam, 1966–

Incentives for regional development : competition among
sub-national governments / Kala Seetharam Sridhar.
p. cm.

Includes bibliographical references and index.

ISBN 1-4039-4788-0 (cloth)

1. Economic development – Government policy. 2. Regional planning –
Government policy. 3. Tax incentives. 4. Industrial policy. 5. Industrial
promotion. I. Title.

HD75.S77 2005

338.9—dc22

2005042144

10 9 8 7 6 5 4 3 2 1

14 13 12 11 10 09 08 07 06 05

Printed and bound in Great Britain by

Antony Rowe Ltd, Chippenham and Eastbourne

Acknowledgements

This book, as in all cases, is the result of cooperation from several people, without which it would not have been possible. First of all, I would like to thank the National Institute of Public Finance and Policy for facilitating the time to work on this book. I would like to thank the United States Department of Housing and Urban Development which funded the research in Chapters 2, 4, and 5, through its 1997 Doctoral Dissertation Research Grant H-21090SG. For work in these chapters, I am very thankful to Professors Chuck Adams, Don Haurin, late Professor G.S. Maddala, Anand Desai, and Mary Marvel, all at the Ohio State University, for their guidance. For work in Chapter 3 pertaining to Illinois' enterprise zones, I am indebted to Professors Peter Fisher and Alan Peters at the University of Iowa, for their guidance and comments. I thank the Ohio Department of Development for providing data necessary for the evaluation of Ohio's enterprise zone programme in Chapters 4 and 5. Further, I am very thankful to the various enterprise zone administrators in Ohio for patiently filling out my survey pertaining to infrastructure costs and several CRA administrators in Ohio for their discussions over the phone. Finally, I thank the erstwhile Illinois Department of Commerce and Community Affairs, and the current enterprise zone administrators in Illinois, Mr Thomas Henderson and Mr Mickey Harris, with the Illinois Department of Commerce and Economic Opportunity, for sending me current information about Illinois enterprise zones.

For work in Chapters 5 and 6, I am indebted to the Indian Institute of Management in Lucknow, India for providing seed money to facilitate the research. I am very thankful to Mr Onkara Murthy at the Karnataka Industrial Areas Development Board (KIADB) for taking me around the various firms in the Hassan growth centre. Further, I am thankful to Mr K.C. Sharma with the Haryana State Industrial Development Corporation (HSIDC) for taking the time to visit several firms in the Bawal growth centre along with me. I thank Mr Alok Kumar, Joint Managing Director of the UP State Industrial Development Corporation (UPSIDC), and his colleagues, for taking the time to answer my questions relating to growth centres in UP during my visit to Kanpur. Further, I am grateful to Mr K.C. Mishra and his colleagues with the Gorakhpur Industrial Development Authority for introducing me to various firms and answering my detailed questions. I thank Mr N.P. Singh of the Satharia Industrial Development Authority for facilitating my visits to various firms in the Satharia growth centre, to enable the assessment. In all of the growth centres that I visited, I wish to thank heartily the representatives of various firms that made themselves available to answer

the various questions I had about their location decision and other aspects of their operation. Finally, I would like to thank Mr S. Jagadeeshan, Joint Secretary in the Department of Industrial Policy and Promotion, Ministry of Commerce and Industry, Government of India, for arranging to send me secondary data regarding growth centres in the country.

I thank Dr Amaresh Bagchi at NIPFP, Mr R.K. Bajaj, Commissioner of Income Taxes, and Ms Ann Martin of Palgrave, for heartily offering to help with Palgrave's tax form. I am very thankful to Ms Amanda Hamilton of Palgrave, the commissioning editor for this book, who patiently and promptly answered all of my questions relating to all aspects of the book. Thanks are due to Mr Keith Povey for his patience with copy-editing and proof-reading the book. I thank Ms Amita Padhwal for her assistance in formatting the book.

Further, I would like to thank Sage Publications for permitting me to reprint substantial parts of my work that had been published previously in the *Economic Development Quarterly*, 10 (1), 69–90 in Chapter 3. I wish to thank the University of Delaware's College of Business and Economics for providing copyright permission to reprint substantial parts of my paper published in the *Review of Regional Studies*, 30 (3), Winter 2000, 275–98 in Chapter 4. Further, I would like to acknowledge with thanks the copyright permission granted by the Centre for Community Economic Development at the University of Wisconsin, Madison, for allowing me to reprint substantial parts in Chapter 5, from my paper published in the *Journal of Regional Analysis and Policy*, 31 (2), 2001, 1–32. Thanks are due to the editorial office of the *Economic and Political Weekly* for permitting me to reprint parts of my paper 38 (39), 2003, 4121–30 in Chapter 7.

Last but not least, I thank the incredible support and encouragement of my husband from the time of the proposal formulation to the fruition stage to writing and formatting. My little daughter, Vindhya, supported efforts of the book in her own way, without being aware of how much she was contributing. Finally, my parents and family played a big role in providing the moral support necessary for completing this work.

KALA SEETHARAM SRIDHAR

List of Abbreviations

2SLS	Two-Stage Least Squares
AFDC	Aid to Families with Dependent Children
A&N Islands	Andaman and Nicobar Islands
ARV	Annual Rental Value
B-C	Benefit-Cost
BEA	Bureau of Economic Analysis
CAGR	Compounded Annual Growth Rate
CETA	Comprehensive Employment Training Act
CPI-U	Consumer Price Index-Urban
CPS	Current Population Survey
CRAs	Community Reinvestment Areas
CRTS	Constant Returns to Scale
CSR	Corporate Social Responsibility
CT	Connecticut
DCCA	Department of Commerce and Community Affairs
DCEO	Department of Economic Opportunity
DIPP	Department of Industrial Policy and Promotion
EC	Enterprise Communities
EZs	Enterprise Zones
FL	Florida
FY	Fiscal Year
GCs	Growth Centres
GDP	Gross Domestic Product
GIDA	Gorakhpur Industrial Development Authority
GIS	Geographic Information Systems
GLS	Generalized Least Squares
GPO	Government Printing Office
HSIDC	Haryana State Industrial Development Corporation
IL	Illinois
IN	Indiana
INR	Indian Rupees
I-O Analysis	Input-Output Analysis
IRBs	Industrial Revenue Bonds
IT	Information Technology
KIADB	Karnataka Industrial Areas Development Board
LHS	Left hand side
MAX	Maximum
MIN	Minimum
MNCs	Multinational Corporations

MO	Missouri
MW	Megawatts
N/A	Not Applicable
NCR	National Capital Region
NIUA	National Institute of Urban Affairs
NLS	National Longitudinal Survey
OBES	Ohio Bureau of Employment Services
OH	Ohio
OLS	Ordinary Least Squares
PDS	Public Distribution System
PSID	Panel Study of Income Dynamics
PPPs	Public-private Partnerships
RCs	Renewal Communities
RHS	Right hand side
SC	Scheduled Castes
SEZs	Special Economic Zones
SIC	Standard Industrial Classification
SIDA	Satharia Industrial Development Authority
ST	Scheduled Tribes
TIRC	Tax Incentive Review Council
UA	Urban Agglomeration
UEZ	Urban Enterprize Zone
UP	Uttar Pradesh
UPA	United Progressive Alliance
UPSIDC	UP State Industrial Development Corporation
US Department of HUD	United States Department of Housing and Urban Development
US	United States
VAT	Value Added Tax

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Part I

Introduction

1

Regional Development Incentives in the United States and India

1.1 Introduction and background

In this book, I study the effectiveness of policies to promote regional development and competition among sub-national levels of government. I study competition among sub-national governments in the United States and India to attract private investment, respectively with the use of tax and infrastructure incentives.

I examine empirical evidence regarding incentives offered by state and local governments in the United States and contrast this evidence with that from incentives offered by state governments in India. Note that although the title speaks of 'incentives for regional development' I will only discuss financial/tax incentives and infrastructure incentives in the book. The reader should be aware that the regional development literature includes non-financial incentives also. There is a stream of literature on regional development (that is, learning regions, milieu of innovation, industrial districts),¹ which is widely discussed throughout the world. Such policies have been characterized as 'new wave' policies (Bartik, 1991) or demand-side policies (Eisinger, 1988). They are all programmes targeted at existing firms. Those policies include services such as providing information regarding the existence of markets, export promotion assistance, assistance to small firms in the form of business incubators, hosting of trade fairs, support of high-technology, e-learning programmes, and other services which boost firm productivity and the development of the region as a whole. While the reader must be aware that there is a stream of literature in each of these areas, the focus of this book is supply-side policies that target branch plant recruitment.

1.2 Motivation for the book

The motivation for this book comes from the extensive use of financial incentives to attract firms and jobs in the United States (especially through the use of enterprise zones (EZs)) that continues to be hotly debated and

aggressively pursued by states. For instance, the conventional state of Iowa in the Midwestern United States recently passed enterprise zone legislation, and as of September 2002, 332 EZs were certified in this state, with the programme's popularity having steadily grown since 1997 (McDermott, 2002). In November 2003, I met the Mayor of the City of Chicago. He expressed the firm view that if Chicago does not offer financial incentives, it will lose out in the war for jobs. So while many sub-national governments in the United States realize the futility of such financial incentives in general, no state or local government wants to lose out in the 'race to the bottom'. For this reason, they continue to offer such incentives.

The motivation for the book also comes from the poor state of infrastructure in India's various states, where the use of programmes such as growth centres (GCs) that provide infrastructure incentives to firms can trigger huge infrastructure reforms throughout the country.

Florida (2002) showed that those US cities and regions that use tax incentives, in fact, attract manufacturing industries, and it may appear that these firms are contributing little to regional development in the present knowledge-based economy. It may be misconstrued that in the present knowledge-based economy, regional development comes from innovation, which calls for incentives other than taxes and infrastructure. Boekema *et al.* (2000) argue that successful firms, as well as governments, are those which have control over and access to flows of information and knowledge of technologies, markets, and organizational and managerial practices. Note, however, that infrastructure (including good roads, uninterrupted power, reliable telecom, banking and related services) is quite critical to the success of all firms – whether they are primarily manufacturing, services or knowledge-based.

In the case of India, although it has emerged recently as a knowledge-intensive economy dependent on IT and IT-enabled services, it continues to be a developing economy with an underdeveloped infrastructure and is not yet a full fledged knowledge-based economy in the sense that the USA and Europe are. Because of this, what is good for the industrial economy is good for the Indian economy. Further, all the leading thinkers of the world, including economists and corporate leaders, agree that a large and sound manufacturing base is necessary to compete in the globalized market. So as Eisinger (1995) points out, there is a return to industrial recruitment among the American states. This is also true in relation to the Indian states which are pursuing entrepreneurial and knowledge-based strategies targeted at existing firms, along with financial incentives to attract new ones.

1.3 What is the black box that converts incentives to regional development?

Throughout the book, regional development refers to improvement in the areas' infrastructure, amenities, job opportunities, and, more generally, its