

Economist.com

Friday July 10th 2009

[Home](#)[This week's print edition](#)[Daily news analysis](#)[Opinion](#)[All opinion](#)[Leaders](#)[Letters to the Editor](#)[Blogs](#)[Columns](#)[KAL's cartoons](#)[Correspondent's diary](#)[Economist debates](#)[World politics](#)[All world politics](#)[Politics this week](#)[International](#)[United States](#)[The Americas](#)[Asia](#)[Middle East and Africa](#)[Europe](#)[Britain](#)[Special reports](#)[Business and finance](#)[About our new page](#)[All business and finance](#)[Business this week](#)[Economics focus](#)[Management](#)[Business education](#)[Economics A-Z](#)[Markets and data](#)[All markets and data](#)[Daily chart](#)[Weekly indicators](#)[World markets](#)[Currencies](#)[Rankings](#)[Big Mac index](#)[Science and technology](#)[About our new page](#)[All science and technology](#)[Technology Quarterly](#)[Technology Monitor](#)[Books and arts](#)[All books and arts](#)[Style guide](#)[People](#)[People](#)[Obituaries](#)[Diversions](#)[Audio and video](#)[Audio and video library](#)[Audio edition](#)[The World In](#)[The World in 2009](#)[The World in 2008](#)[The World in 2007](#)[The World in 2006](#)[The World in 2005](#)[The World in 2004](#)[Research tools](#)[All research tools](#)[Articles by subject](#)[Backgrounders](#)[Economics A-Z](#)[Special reports](#)[Style guide](#)[Country briefings](#)[All country briefings](#)[China](#)[India](#)[Brazil](#)[United States](#)[Russia](#)[My account home](#)[Newsletters and alerts](#)[Manage my newsletters](#)

Search

Economist.com

Go

Log in: e-mail

Password

Go

[E!](#) Requires subscription Remember me[Register](#)**Get 4 FREE trial issues >>**[Subscribe](#)[Student offers](#)[Site feedback](#)

The Economist Debate Series

Sustainable developmentCan chemistry create truly sustainable development?
July 3rd-15th

IN ASSOCIATION WITH



JOIN THIS LIVE DEBATE >

Economist.com**Special report****A special report on Texas****Tex-mix**

Jul 9th 2009

From *The Economist* print edition**The state's best and worst sides**

THOUGH the Texas model has many critics, its admirers tend to list the same advantages. The low tax burden (second-lowest in America) invariably comes top of the list. Arthur Laffer, inventor of the famous curve, reckons that one of the most important determinants of whether a state does well or badly is not just the overall level of taxes but their structure too. A high, progressive personal income tax, he says, is about the worst incentive-killer you could devise. Americans are highly mobile, so the most able will simply leave for another state. Mr Laffer himself left California for low-tax Tennessee three years ago because he felt that bad taxes were destroying the state's economy.

Progressive taxes are considered fairer, but better to leave it to the federal authorities to impose a progressive income tax, the same for every state. The nine states with a personal-income-tax rate of zero, Mr Laffer finds, had net domestic immigration of 4.5% of their population in the ten years to 2007; the nine with the highest marginal tax rates saw outflows averaging 2.2%. A high state tax on capital gains is also bad because it tends to be volatile, causing big budgetary problems. Texas does not have one of those either.



Next on its list of advantages usually comes the feeble state of its unions. Texas, like 21 others, mostly in the South, is a "right to work" state, so no one can be compelled to join a trade union. Only 4.5% of its workforce is unionised, against 12.4% nationally. Even where unions are well represented, as at the port of Houston, the management says they behave sensibly.

Then there is tort reform. Texas used to be a plaintiff's dream, with few restrictions on who could sue for what and where. Class-action suits against big corporations used to be heard by juries who made free with the defendants' money. George Bush (who was governor of Texas from 1995 until he headed off to greater things in 2000) partially reformed the system in 1995. Rick Perry, his successor, oversaw a second reform in 2003, concentrating on medical awards that were driving doctors away. Since then malpractice-insurance rates have fallen and the doctors have returned.

The state's sound public finances are often noted too: in the landmark legislative session of 2003 (Texas's legislature meets only every other year, for 140 days) Texas eliminated a budget deficit of close to \$10 billion and has not looked back. It is still in surplus, though only thanks to a large dollop of cash from the federal government. Since 1988 the state has maintained a "rainy-day fund", paid for by taxes on oil and gas companies, which is now worth \$6.7 billion; it can be raided only if two-thirds of both houses of the state legislature agree, and Mr Perry vows not to touch it in the current, arguably rainy, downturn.

[Comment \(2\)](#)[Recommend \(2\)](#)[E-mail](#)[Share](#)[Print](#)[Buy PDF](#)[Reprints & permissions](#)**Related Items****In this special report**[Lone Star rising](#)[The best and worst of Texas](#)[Schools for the poor](#)[Texas's diversifying economy](#)[The red and the blue](#)[The new face of America](#)[Sources and acknowledgments](#)[Offer to readers](#)**From *The Economist***[Texas faces the downturn](#)[Mar 19th 2009](#)[Race and university admissions](#)[Feb 26th 2009](#)**Audio**[An interview with Christopher Lockwood, author of this special report.](#)**Country briefing**[United States](#)**More articles about...**[America's economy](#)[Higher education](#)[Schools](#)**Websites**[The Office of the Governor outlines the Texas Enterprise Fund. The state also has an Emerging Technology Fund. Two think-tanks are the Centre for Public Policy Priorities, for a left-of-centre take and the Texas Public Policy Foundation, for a more market-oriented view. Houston is the birthplace of the Knowledge Is Power Programme and Youth Engaged in Service.](#)

Advertisement

- Manage my RSS feeds
- Manage special-offer alerts
- More »
- Renew my subscription
- Change my print subscription delivery, billing or e-mail address
- Pay my bill
- Activate premium online access
- Report a missing copy
- Suspend my subscription
- More »

- Digital subscriptions
- Subscribe to Economist.com
- Manage my subscription
- Mobile edition
- Audio edition
- Download screensaver
- More »

Classifieds and jobs

- The Economist Group
- About the Economist Group
- Economist Intelligence Unit
- Economist Conferences
- Intelligent Life
- CFO
- Roll Call
- European Voice
- EuroFinance
- Reprints and permissions

EIU online store

Economist shop

Advertisement

Your opinion could give you a chance to win **\$1000!**

Survey and chance to win provided by Safecount.net and Dynamic Logic.

TAKE A SURVEY

Start »



A fourth factor is the amount of help that state and local government offers to business. Here purists on the right find common ground with those on the left who complain that companies are given generous tax breaks but education and health are underfunded. All states these days compete to get businesses to move in; Scott McCown of the Centre for Public Policy Priorities (CPPPP) in Austin calls this “buying dates”. Such incentives distort the market and benefit newcomers at the expense of established companies.

Texas’s package of benefits is handsome. In 2003 its legislature voted in a Texas Enterprise Fund, with \$295m, since topped up, to spend on luring companies to Texas; that was followed two years later by a \$235m Emerging Technology Fund. These are among the biggest such funds anywhere in America.

The legislature also allows Texas city governments great latitude in designing their own inducements for business. Free land, cheap electricity, subsidies towards the wages of higher-paid workers, funds for training and long tax holidays are now essential weapons in municipal armouries. Most controversial are the “abatements” offered to big investors that exempt them from paying property taxes to the local school districts; in Texas, as in most states, these taxes are the schools’ main source of funding.

Sprats and mackerels

Such inducements are helpful for the companies, but they also make business sense for the cities that offer them. Gary Lawrence, who heads the Economic Development Alliance of the city of Lubbock, in the Texas panhandle, explains that one electronics investment he backed cost the city \$4.7m in revenue forgone over ten years. But in return the company undertook to create 165 well-paid jobs, creating a demand for houses that is increasing income from property taxes as well as sales taxes. The \$4.7m should be written off in as little as three years. This kind of deal has put Lubbock on the map.

Advertisement

Mr Perry and the Republicans who have dominated both chambers of the legislature since 2003 can claim some credit for all those boosts to business. But they get none for Texas’s biggest advantage: its sheer size. Larger in area than any country in the European Union and than any American state bar Alaska, Texas has huge amounts of space into which its cities can expand. This has allowed Houston to sprawl over some 600 square miles; it is probably the most spread-out big city in America and has no zoning restrictions, allowing the market to determine the best balance between retail, commercial and residential uses.

California is constrained by its mountains and the ocean, to say nothing of the demands of environmentalists keen to preserve its remarkable natural beauty. Texas, says Michael Lind, a fifth-generation Texan who writes about demography, identity, history and much else, “is flat and ugly. The Sierra Club is not going to kick up a fuss if Houston or Dallas keeps on growing.” He is being a little harsh; most of central Texas is perfectly nice-looking grassland. But there certainly is a lot of it.

Limitless space translates into low property prices; you can buy a 1,500 square foot (140 square metre) starter home for as little as \$100,000 in a decent part of Houston or Dallas; small rented homes in the grimmer parts of south-east Houston are advertised for as little as \$99 a week. With taxes and prices also lower, an incomer from California might easily save 30% or more of his salary by moving from Silicon Valley to the “Silicon Hills” of Austin.

Learning difficulties

Red McCombs is no bleeding-heart liberal. A lumbering giant of a man and one of Texas’s crop of a couple of dozen billionaires, he built his fortune by buying and selling everything from car dealerships to football teams. But he gets distinctly emotional about the poor performance of Texas’s educational system. “The biggest blight on our state”, he thunders, “is the terrible graduation rate from our high schools. Shame on us! It’s been that way for 30 years, and it’s getting worse. Have we been greedy, ignorant, uncaring? Maybe all of those things.”

Mr McCombs is not alone. Almost everyone interviewed for this report expressed concern about the poor state of Texas’s public schools and the mediocre record of its universities. Stephen Klineberg, professor of sociology at Rice University in Houston, puts it bleakly: “If we fail to turn our education system around, we will find that a whole generation has been locked out of the jobs market.” The drop-out rate from

Texas' Hispanic

According to a state and he

then, we will lose a generation getting there." Texas ranks 34th in terms of expenditure per pupil, but Mr McCown reckons that it needs to spend more than the average, not less, because of the high proportion of its students that do not speak English at home, or at all.

Others disagree. If money were everything, California's children would have much better test scores than Texas's, but a recent study by McKinsey, a consultancy, shows the opposite. As it happens, Houston is the birthplace of two independent or "charter" school movements that are now taking America by storm: KIPP (the Knowledge Is Power Programme—see box, previous page) and YES (Youth Engaged in Service).

Neither requires increased spending; in fact, their costs per pupil are generally lower than those of the school districts in which they operate and compete. Their results have been phenomenal, with typical drop-out rates of less than 5%. But the number of charter schools in Texas is currently capped at 215, and a mere eight new ones were authorised last year. And only well-motivated parents tend to send their children there. However, there is some evidence that their presence is encouraging the school districts to up their game.

For Texas's universities, there is probably no substitute for digging deep and spending more money, and the state government is trying to do just that. Embarrassingly, Texas has only three "tier-one" universities (generally defined as meaning that a university undertakes at least \$100m-worth of research a year). California has nine tier-one universities and New York state seven.

Buying brainpower

Texas's three are the University of Texas at Austin; A&M at the small town of College Station; and the tiny (and private, hence expensive) Rice at Houston. So none of Texas's three largest cities has a big tier-one university to its name. A bill passed by this year's legislative session commits the state to help no fewer than seven tier-two universities reach tier-one status. If voters agree in a referendum, up to \$680m could be available. Texas should also be saving money by cutting administrative costs at the universities, which are way too high.

Other efforts are under way. Francisco Cigarroa, the chancellor of the University of Texas system and the first Hispanic ever to hold this prestigious job, says his board has authorised a \$150m fund to bring leading academics to Texas. The system, made up of 15 centres of learning, now has a \$3 billion fund (approved in a 2007 referendum that would surely have failed in just about any other state) to establish a world-class cancer foundation. It has just recruited a Nobel laureate as its chief scientist.

David Dewhurst, Texas's lieutenant-governor and president of the Senate (jobs that arguably make him the most powerful person in the state), says that Texas is still adding to its university enrolment whereas California's is contracting. "If you aren't making money, you can't expand," he says. That, in a nutshell, is the philosophy of Texas today. But allowing the state's schools and universities to improve enough to meet its future needs, while keeping the low taxes that businesses find so attractive, will be a tricky balancing act.

Readers' comments

The Economist welcomes your views.

[View all comments \(2\)](#)

[Add your comment](#)

[Next article »](#)



Want more? Subscribe to [The Economist](#) and get the week's most relevant news and analysis.

Maximise potential in international trade with RBS - [Read our FREE report](#)

Full-time faculty position

Top graduate school in Lima, Peru searches for Ph.D / DBA graduates from recognized universities.

For more information, [click here](#).

Manufacturing Excellence Awards 2009

On Thursday we will be celebrating the best that British business has to offer.

[Read more](#) about the UK's premier manufacturing benchmarking scheme and its top 20 firms that have reached the prestigious final.

FSA — PRUDENTIAL POLICY

Associates, Senior Associates & Technical Specialists — Wholesale and Prudential Policy Division

[click here](#) to apply

Sponsor's feature

[About sponsorship](#)

[Staff books](#) [Career opportunities](#) [Contact us](#) [Subscribe](#)

[Site feedback](#)

Copyright © The Economist Newspaper Limited 2009. All rights reserved. [Advertising info](#) [Legal disclaimer](#) [Accessibility](#) [Privacy policy](#) [Terms & Conditions](#)

[Help](#)