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Welcome to the Amazon Games

Hear an echo? That's the world's largest e-commerce company doing to economic development what it did to shopping malls.



by RON STARNER & ADAM JONES-KELLEY

funny thing happened on the way to the e-store. Amazon launched a “search” for a second headquarters home, and upended another industry in the process. The established rules of site selection and economic development went the way of the suburban shopping mall. Forget the comfy confines of the confidential site search; Amazon decided it would pit every state and community against each other in a dramatic public competition akin to American Idol or the Amazing Race, though talent alone will get you nowhere in this contest.

If this is real — if it's exactly as stated and billionaire entrepreneur Jeff Bezos has his way — Seattle-based Amazon will bring tens of thousands of high-wage jobs to the North American community willing to pony up the most cash — er, “incentives package” — to lure the Washington giant to its new home. This is a first in the history of corporate site selection.

How'd we get here?

This magazine's reporting of US-based Amazon capital investment projects over the past five years shows that the e-commerce firm, on average, nets between \$10,000 and \$15,000 per job in incentives.

The Amazon RFP issued on September 7 for the competitive HQ2 project promises to deliver up to 50,000 jobs and \$5 billion in capital investment to the lucky winner over 15 years — provided the winning bid includes enough “special incentives” to sway Bezos to sign on the dotted line.

The public auction was barely two weeks old before New Jersey Gov. Chris Christie and the New Jersey legislature offered to put together an incentives package valued at \$5 billion. Intrepid readers proficient in the dying art of math will note that works out to about \$100,000 in incentives per job, a slight tick up from the norm.

May the Odds Be Ever in Your Favor

This unprecedented nationwide competition has become the Hunger Games of economic development, inciting breathless excitement in far-flung communities and near daily handicapping by the news media. But how many communities have a realistic shot at being the victor, and what are they likely to win when they are?

These are questions largely ignored in the frenzied coverage this announcement has produced. And there are none more critical, as this process, the ultimate cost of winning the penultimate prize and the precedent this will set will offer lessons for business executives, site consultants, community leaders and everyone interested in improving the practice of economic development.

If ensuring an equitable return on investment for all parties involved is truly the object of the game, then it's worth heeding words of caution from economists studying this deal.

The bottom line, they say, is this: It won't be easy to quantify the benefits of Amazon HQ2 to any community because complex deals like this tend to evolve over many years. Measuring ROI in economic development isn't an exact science. And if Amazon is really as interested in helping a community grow in a healthy way as it is in steamrolling the best deal for the company, then it won't ask for more than the deal is worth.

We wouldn't bet your discounted Whole Foods organic kale on that happening. If this is real, they'll chase the dollars. And the winning community may wind up regretting they volunteered as tribute.

Experts like Jim Rounds, president of Rounds Consulting Group in Arizona, doubt the deal will ever materialize as presented.

“I don’t think the scale is legitimate. I am confident there won’t be 50,000 workers making \$100K a year. You don’t expand a headquarters that way. My best guess is that maybe half the numbers are real — wages half of what’s been touted and half the capital investment.”

What Amazon Wants in its Shopping Cart

This is the easy part. Amazon has been unambiguous in its desire to maximize the incentives in this deal. After laying out the basic location prerequisites — a metro area of at least 1 million people (which many smaller communities gleefully ignore); a stable and business-friendly environment; ability to attract and retain strong technical talent; and a location within 45 minutes of an international airport — the RFP lists Amazon’s “key preferences and decision drivers.” This is a colorful euphemism for “Show me the money!”

Unsurprisingly, two of the top three decision drivers center on incentives. “Incentives offered by the state/province and local communities to offset initial capital outlay and ongoing operational costs will be significant factors in the decision-making process,” the RFP states. Amazon then lists the incentives it wants: “land, site preparation, tax credits/exemptions, relocation grants, workforce grants, utility incentives/grants, permitting, and fee reductions.” In short, they’ll take everything, and probably ask for an option on your first born.

Amazon — which has built more than 140 million sq. ft. of warehouse and data center space around the country -- is accustomed to getting what it wants from state and local governments. An analysis by Good Jobs First, a pro-labor think tank in Washington, D.C., reports that Amazon collected more than \$750 million in government subsidies for its projects over the past decade. Oregon alone has committed more than \$213 in incentives for Amazon during that time, the most of any state, according to The Business Journals, which estimates that the total value of government subsidies for Amazon now tops \$1.24 billion nationwide.

Greg LeRoy, executive director of Good Jobs First, says Amazon has amassed an expert team of site selectors and incentives negotiators and they’re sharpening their swords for the battle ahead.

“I suspect that Amazon already knows where it is going or has a very short list,” LeRoy says. “They have been hiring more lawyers and CPA-level people for that department. They have a very sophisticated internal path.”

That means that much of this is for show, an act they will play out to extract maximum payout from their intended target(s).

LeRoy also points out that “a deal this size will automatically qualify for massive corporate income tax credits which will obliterate the company’s income taxes for many years. They will also get

exempted from paying sales taxes on building materials and equipment. More than likely, local government will abate property taxes for a long time. What else is there?"

Is this a good thing for the local economy? Measuring whether all these abatements and credits are a good deal is a complicated matter, say the experts who study ROI on such deals.

Dr. Peter Evangelakis, economist at Regional Economic Models Inc. (REMI) in Amherst, Massachusetts, says a change in a few thousand jobs can adjust ROI by hundreds of millions of dollars for state and local governments.

"If Amazon builds employment slowly or does not hit its 50,000-employee target, revenue gains can shrink significantly for state and local governments," he says. "Governments need to consider these scenarios when deciding what incentives are worth offering."

One thing those governments can count on: Amazon will have calculated all possible scenarios. It isn't just hiring lawyers and CPAs, after all. It's also hiring elite economists of its own.

"Amazon has been hiring economics Ph.D.s and professors quite heavily in the last five years," says Duke University economist Allan Collard-Wexler, a co-author of a new report on the effects of cartels who works in the field of industrial organization. "The chief economist at Amazon used to teach the same classes I teach at Duke right now. Academia is open — you see papers. Amazon is closed — you just get hints of what they're doing. So a lot of research in our field has essentially gone dark, because it's happening inside Amazon."

Boon or Bust?

Evangelakis notes that if 50,000 good-paying jobs are truly added over 10 years, it could add up to \$12.9 billion to state revenues over 15 years. But if Amazon — which employs 382,000 people worldwide — adds only 2,500 new employees over five years, he says, the increase over that same period would be just \$869 million.

"No one should be under the illusion that Amazon does not already know the top five places where this will be successful."

—Mike Bennett, Founding Partner, Avenue Advisory Group, Chicago

"That's why it's important that government works with Amazon to ensure mutual benefit," Evangelakis says. "My advice to government leaders is to negotiate with Amazon and get them to buy into state and local economies so that it's a win-win package. These economic and fiscal impacts are crucial to inform policy decisions."

The fiscal impacts of Amazon could well be enormous. Among other benefits to a community, Amazon can raise the property tax base for local government, increase collections of personal income taxes, increase sales tax revenues, and increase corporate income tax collections, says Evangelakis.

The downside, he says, would include upward pressure on wages, increasing production costs across the economy and downward pressure on regional competitiveness. “Population and wage increases will drive up housing prices and your community will become a more expensive area to live in,” the economist adds.

It’s a risk. These trade-offs must be considered carefully before state and local governments empty the coffers to lure Amazon, as Jim Rounds cautions. “If this deal is dominated by the economic incentives, then everything falls apart for the community. My advice — if they don’t meet the economic fundamentals, the only way to win the project is through incentives, and that’s not good for you.”

Not everyone is so hesitant. John Boyd, principal of The Boyd Company Inc., a prominent headquarters site consulting firm in Princeton, New Jersey, says that despite the hefty asking price, states and communities should do their due diligence and put forth their strongest bid.

“The Amazon search is playing out very publicly and contrary to most site selection projects,” Boyd says. “Very few companies have the swagger and wherewithal to pull this very public site search strategy off. It is something we would generally not recommend to our clients.”

On incentives, Boyd says, “My message to the public weary on incentives today is to encourage your lawmakers to do the heavy lifting first — pension reform, consolidating municipal services, cutting taxes and making government less expensive. Then we can have a discussion on the propriety of incentives. Until then, incentives are a necessary evil, especially for high-cost states like New Jersey, Connecticut, Massachusetts, New York, Illinois and California.”

REMI conducted its own analysis and concluded that these 10 cities make the most sense as the right destination for Amazon HQ2: Atlanta, Austin, Baltimore, Boston, Chicago, Denver, Detroit, Minneapolis-St. Paul, Pittsburgh and Tulsa. Site Selection magazine suspects New York and Washington, D.C., would also be in the mix, as would Toronto — after all, the company was careful to state in its announcement that it would be a second HQ in North America, not necessarily in the United States.

“I think Amazon made a mistake, frankly. Here is a big, very successful company looking to extract incentives from hard-pressed communities. When there are 50-plus losers and one winner who has to cough up big bucks, this won’t look good for Amazon.”

— Richard Florida, Economic Development Adviser and Author of *The New Urban Crisis*

Mike Bennett, founding partner and site consultant at Avenue Advisory Group in Chicago, conducted his own analysis.

“Amazon is in the business of disruption. The normal rules don’t apply to them,” Bennett says. “Amazon is very smart and innovative. No one should be under the illusion that Amazon does not already know the top five places where this will be successful. There are only a handful of communities that can meet this need.”

Flying in the face of the majority opinion, Bennett believes that incentives won't, in fact, be the deciding factor. "I don't think that a company like Amazon will make a 30-year decision based on incentives," he says. "Amazon is a cutthroat business that wants to maximize shareholder value, but they also know that short-term benefits will not outweigh long-term investments that they will need to be successful."

Disruptor? 'Don't Give Them a Penny'

Richard Florida, an economic development adviser who wrote *The Rise of the Creative Class* and *The New Urban Crisis*, isn't so sanguine about the economic risk in offering a massive incentive package. Florida urges government leaders to "use this as an opportunity to bring your community closer together, to highlight your strengths and understand and begin to deal with your weaknesses." He also advises locations to respond directly to the RFP and "not to your own internal political issues."

On incentives, Florida is blunt about the \$136-billion company that currently has about \$26 billion in cash on hand: "Do not give them a penny in incentives."

Florida says he hopes that Amazon's highly publicized site search exposes much-needed improvements in the practices of corporate site selection and economic development.

"I think Amazon made a mistake, frankly," he says. "They should have done this quietly. It's already causing a backlash. Tech companies' brands are taking a hit. Here's a big, very successful company looking to extract incentives from hard-pressed communities. When there are 50-plus losers and one winner who has to cough up big bucks, this won't look good for Amazon."

Jeff Finkle, president of the International Economic Development Council, says that Amazon's highly public site search isn't without benefit. "I think the process that Amazon is asking communities to engage in is going to be eye-opening," he says. "We'll see more transparency in this than we will see in almost any site selection process anywhere. There is some good education in this for the public and the media."

Still, Finkle harbors concerns. "I worry that communities will throw too many incentives at them and that Amazon will take too much," he notes. "Will the winning community have buyer's remorse? Amazon is asking questions about clawback provisions. They may be trying to downgrade communities that are trying to protect their public tax dollars."

Finkle cites the example of Under Armour in Baltimore as a model of headquarters development, a model he hopes Amazon will follow.

"I think Amazon could make a huge statement if they pick a large urban area that meets their criteria and they don't take too much in incentives," says Finkle. "If they help rebuild that community, that would be a real benefit. Under Armour is taking that approach in Baltimore. Wouldn't it be cool if Amazon adopted the same strategy?"

'No Comparison for a Project Like This'

Multiple interview requests to Amazon for this piece were turned down, but the company has been very specific about how this search will be conducted.

"We expect HQ2 to be a full equal to our Seattle headquarters," said Jeff Bezos, founder and CEO of Amazon and one of the five richest people on earth with a net worth of \$83.5 billion. "Amazon HQ2 will bring billions of dollars in up-front and ongoing investments, and tens of thousands of high-paying jobs. We're excited to find a second home."



Jeff Bezos, founder and CEO of Amazon and one of the five richest people on earth with a net worth of \$83.5 billion.

But why? What's the endgame? Can Amazon actually deliver on its HQ2 plans? "Yes," says Bennett. "Amazon could add 50,000 jobs over 20 years, but keep in mind that Amazon is not just one company. It now has dozens and dozens of arms, including a grocery store chain in Whole Foods.

"What they're doing with this HQ2 site search is like a stress test for states and communities," he adds. "They want to look at labor markets and determine their breaking point, and then see how

that aligns with their own growth plans. There is no comparison for a project like this, because we have never seen it done before.”

Noted site consultant Steve Weitzner of Silverlode Consulting in Cleveland agrees.

“A community’s biggest mistake could be just pitching a greenfield location. Companies don’t make decisions. Human beings at companies make decisions, and they remember cool flashy ideas. You must connect at a human level. Check all the boxes, but also be a place that cannot be ignored. Present your place in a way that Jeff Bezos will think is pretty cool.”

Disruptor, indeed. Sometimes disruption is good, forcing markets to adapt, evolve, grow stronger. Sometimes disruption is just ... disruptive. Whether this deal is real, whether it will ever be the windfall communities are clamoring after, remains to be seen. But the notes of caution cited by the experts interviewed for this piece should be part of the equation.

Remember, Tributes: No one really wins the Hunger Games. You just hope not to lose.