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Op-Ed

California, a bad bet for business

Why would new enterprises come to a state like this?

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In its most recent annual ranking of "business friendly" states, Forbes magazine had some blunt advice for investors: "Utah and Colorado have maintained strong business climates. Forget about California."

Californians like to dismiss such assessments of the Golden State and instead point to its natural beauty and quality of life. They tend not to worry what people in other states think. But they should. California is no longer the economic miracle it once was. Silicon Valley no longer has a monopoly on high-tech talent and innovation. Hollywood has to compete for movie locations with Utah and Morocco. Real estate investors see better development prospects in states with fewer foreclosed and abandoned homes. And SoCal porn producers know they don't need huge wardrobe containers to move to Nevada.

Californians tend to be complacent about these competitive risks. On the surface, things don't look too bad. Sure, the state's finances are in shambles and the Legislature in disarray. But median personal income ($42,578) is well above the national average ($39,945).

These things can't compensate for some disturbing recent trends. The growth of the state's $2-trillion economy has slowed dramatically. Since 2000, the state's economy has grown significantly more slowly than the rest of the nation. Last year, California ranked 34th in real GDP growth. That sluggish growth has burdened it with among the highest unemployment rates (10.9%) in the nation. If businesses heed Forbes' advice to avoid the state, the situation will only worsen.

So what is it that makes California unfriendly to business? For starters, it's very expensive to do business in the state. Corporate taxes are high, as are energy and labor costs, according toMoody'sAnalytics and the Tax Foundation. In the Forbes rankings, the state also comes in at No. 40 in the category of regulatory environment. To compute the state's regulatory score, Forbes looks at the Pollina Corporate Real Estate Index, Pacific Research Foundation's Tort Liability Index, PRI's Economic Freedom Index,Moody'sbond ratings, transportation infrastructure and right-to-work laws. Thank goodness it didn't also look at the Los Angeles City Council's proposed new regulation of the porn industry's safe-sex practices — a proposal that increases both regulation and costs in an economically important industry in the state. California also ranks a disappointing No. 32 in the "labor supply" category, based largely on its low high school and college graduation rates. This ranking represents a precipitous decline from the days when California's colleges were ranked among the best in the world.

Forbes is not the only naysayer about California's business climate. The Canadian-based Fraser Institute compiles a similar ranking for the 50 states and the 10 Canadian provinces. Fraser's ranking is based on 10 statistical indicators that more narrowly focus on business concerns (tax rates, minimum-wage levels, unionization rates, public-sector employment and the like). The Fraser rankings came out in January. In that ranking, California scores even worse — a dismal No. 44 among the 50 U.S. states. South Dakota, Delaware and Texas top the Fraser list, while Vermont, New York and Alaska reside at the bottom.

California's dismal showing in the Fraser rankings of business climate stem primarily from the state's relatively high income tax rates, high minimum-wage thresholds at both the state and local levels, and a high rate of unionization among public-sector employees. The state also scores poorly on its high ratios of public-sector spending and income transfers because of such things as its workers' compensation system, unemployment insurance costs and fat public pensions.

Although many Californians take pride in some of these wage and spending policies, Fraser emphasizes the effect they have on business decisions — especially decisions about locating new businesses in the state or expanding existing enterprises. According to Fraser, these rankings are crucial to economic growth. States that have improved their rankings have grown per capita incomes faster than other states. States whose rankings have declined have experienced more sluggish growth. The Fraser survey found government growth, higher taxes, minimum-wage hikes and increased unionization to be significant impediments to economic growth.

By those measures, it's no wonder California is declining. L.A.'s intrusions into the porn industry, San Francisco's new highest-in-the-nation minimum wage ($10.24 an hour) and Gov. Jerry Brown's relentless push for higher taxes, more regulation, increased public spending and a $100-billion railroad augur poorly for future rankings.

It's tempting to dismiss these rankings as biased or inconsequential. But that would be a mistake. If California is to prosper again, it's got to attract new business. And having a business-unfriendly reputation works against its ability to do that.

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