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*Commentary on the rural economy*

CENTER *for* THE STUDY OF RURAL AMERICA

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# *New Issues*

ON THE RURAL HORIZON



# Peering

## ON TO THE RURAL HORIZON

by MARK DRABENSTOTT

*The past year was generally upbeat for the rural economy, with most of the countryside enjoying solid economic gains.*

Agriculture led the way, with big crops and solid livestock profits. While farm income fell from the previous year, it was second only to the record level of 2004. The continuing boom in farmland values underscored the positive tone in farm country. The rural service sector also scored impressive growth, breathing new life into the hopes of many rural places that they can be competitive locales for service companies. Rural service jobs grew more than 2% through the first three quarters of 2005. The growth in producer services, a high-wage portion of the sector, fueled new optimism about the future. Finally, rural America's abundant natural resources also contributed to the healthy economy. Booming energy prices fueled a surge in energy production. And scenic rural areas continued to enjoy job growth through recreational services. The manufacturing sector remained a soft spot in the rural economy. Even so, continued reports of successful shifts to advanced manufacturing suggest that factories will remain an important economic engine throughout the countryside.

The solid economy should continue in 2006. The national economy is expected to grow moderately, with solid consumers and businesses spending even as the housing sector slows down. Coupled with continued growth in the global economy, demand for many of the products that rural America sells should continue to expand. Agricultural prices may be weighed down by bins bulging from a big harvest in 2005, but farmers should still post solid income. The rural service sector may be the bright spot in the year ahead, as more firms discover the advantages of skilled rural workers at comparatively low cost. A slowing national housing market may take some of the wind from the sails of the rural land boom, but most analysts expect land values to keep rising, though perhaps at a slower pace.

A quick glance at the economy, therefore, suggests another good year for rural America in 2006. Still, there are some significant clouds on the horizon that bear watching. As in recent years, we will continue to monitor the rural economy

for the effects of globalizing markets. A particularly important issue as 2005 drew to a close was the current Doha Round of World Trade Organization talks. The WTO acts as an important referee in global trade, and there are concerns whether a global stalemate on the future of agricultural subsidies will halt progress in the Round overall. The Doha Round is focused on ensuring trade expansion that will benefit developing countries, some of rural America's most important trading partners. For instance, nearly three-fourths of all U.S. agricultural exports now go to developing countries. Therefore, a positive outcome to the Round holds huge promise for the rural economy.

For us at the Center, a core portion of our work in 2006 will continue to be tracking how rural regions build competitive economic engines amid globalizing markets. Three other issues that are somewhat newer on the horizon also bear watching.

*Energy prices* have moved significantly higher over the past year. The higher prices eat into many rural wallets, especially since most rural workers commute greater distances to and from their jobs. At the same time, though, the higher prices

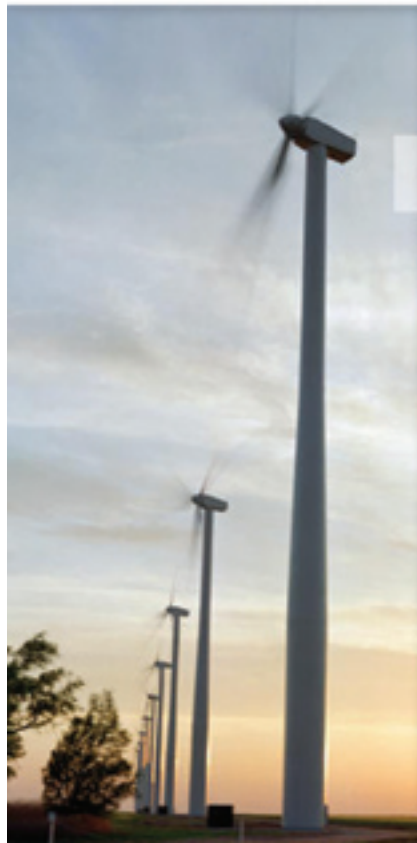
may spawn whole new industries aimed at offsetting the impact of higher prices—from bio-fuels to new products designed to replace those derived from petroleum, such as bio-plastics. Many of these industries will be located mainly in rural areas.

The *budget climate* poses a big paradox for rural areas. The federal budget has moved into significant deficit over the past couple years, even as more federal mandates have been pushed down to state and local governments. Many rural places have limited capacity to fund the new mandates. Moreover, rural areas already claim a smaller share of the federal budget on a per capita basis. As this story unfolds, fiscal necessity may become the mother of useful innovation. Rural areas may find new ways to partner and achieve fiscal efficiencies—and partnering may also improve the ability of rural communities to tap federal grants that can spur economic growth.

Finally, *sprawl* is becoming a contentious issue for rural and metro areas alike. The housing boom of the past decade has pushed the nation's metro areas out into many rural areas, creating a host of development and land management issues. Some rural areas welcome the development, while others scorn the loss of land and control. Regardless of which side of the issue they fall, however, all rural areas have a new opportunity to think regionally about a stronger future.

# 2005

At this point, the outcome of these three new issues is anything but certain. Given the potential size of the impact, however, they will have an important bearing on how rural areas grow. Accordingly, this year's annual report reviews the rural economic outlook and then takes a closer look at the three issues—ones we will be watching in the period ahead. In each case, we discuss the pluses and minuses involved and identify the factors likely to determine the outcome.



# THE 2005 Rural Economy

AT A GLANCE

by SEAN MOORE

*The rural economy continued to brighten in 2005, with both the farm and the nonfarm sectors showing major strength.*

Net farm income is expected to be \$71.8 billion, marking yet another year of exceptional returns for the farm sector. Meanwhile, nonfarm jobs continued to grow at a healthy rate, led by renewed strength in the service sector. Manufacturing showed slight improvement, but the bulk of nonfarm job gains came from the service industries.

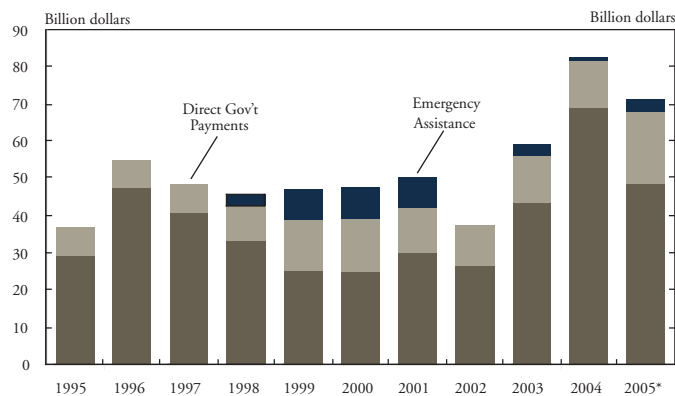
## AGRICULTURE SHINES ONCE AGAIN

Farm operators, both crop and livestock, had another excellent year in 2005 despite challenges from hurricanes and drought. USDA projects net farm income to be \$71.8 billion, well above the ten-year average and the second-highest on record (CHART 1). Underpinning the record incomes were higher cattle prices, a bumper corn harvest, and increased government payments.

Livestock producers enjoyed across-the-board strength. Dairy prices were favorable, while strong consumer demand for protein supported higher beef and pork prices.

Hog producers were especially profitable as prices held well above breakeven levels throughout the year. The profit picture for cattle producers was somewhat mixed, however, as higher feeder cattle prices led to profits for ranchers but dampened opportunities for feedlot operators.

CHART 1  
NET FARM INCOME



\*Forecast, November estimate  
Source: USDA

Despite some localized challenges by hurricanes and drought, 2005 turned out to be an exceptional year for the nation's crop producers. USDA estimates 2005 gross receipts at \$113 billion, down \$11 billion from the previous year but still well above the historical average.

Crop producers did well in part because the effects of hurricanes and drought were mostly localized. The devastation of hurricanes Katrina and Rita, while severe for Gulf Coast agricultural producers, had little impact on producers in other parts of the country. Similarly, drought substantially lowered yields in parts of the Corn Belt, but as a whole, U.S.

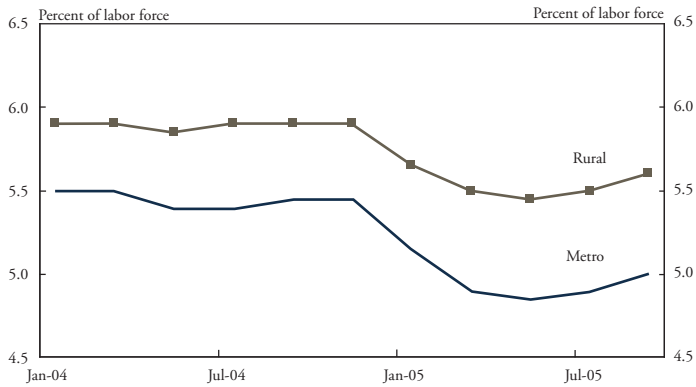
corn producers harvested the second-largest corn crop on record. The abundant harvest, however, pushed prices lower. The lower prices for corn contributed heavily to a sharp jump in direct government payments, which climbed almost \$10 billion over a year ago, at \$22.7 billion. At least \$3.7 billion came as ad hoc and emergency payments to producers hit by drought and other disasters. A great deal of the increase will result from counter-cyclical payments

designed to kick in when prices are low.

## SOLID GROWTH IN THE NONFARM SECTOR

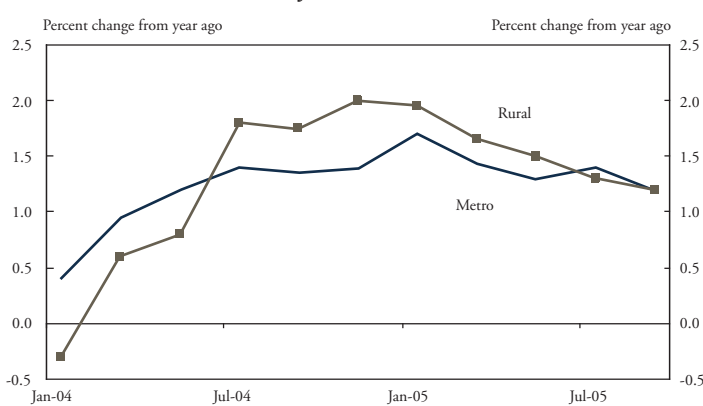
The rural nonfarm economy stayed on its path of expansion through 2005. Wages for the average rural worker climbed almost 2% during the first three quarters of the year, as the unemployment rate trended slightly lower (CHART 2). Payrolls grew robustly, with year-over-year job gains holding near 1.5% throughout the year (CHART 3). Thanks to this consistent growth, rural firms added 291,000 jobs by the end of the third quarter, reaching their highest mark in over four years.

**CHART 2**  
RURAL AND METRO UNEMPLOYMENT RATES



Source: BLS, payroll survey, seasonally adjusted

**CHART 3**  
RURAL AND METRO BUSINESS JOB GROWTH



Source: BLS, payroll survey, seasonally adjusted

## MANUFACTURING REBOUNDS BUT CHALLENGES REMAIN

Manufacturing jobs grew modestly but consistently in 2005, following sharp contractions in payrolls from 2000 to early 2004. Early in the year, payrolls edged up nearly half a percent and held steady. Mass layoffs and plant closures eased and fell to their lowest levels in several years (CHART 4).

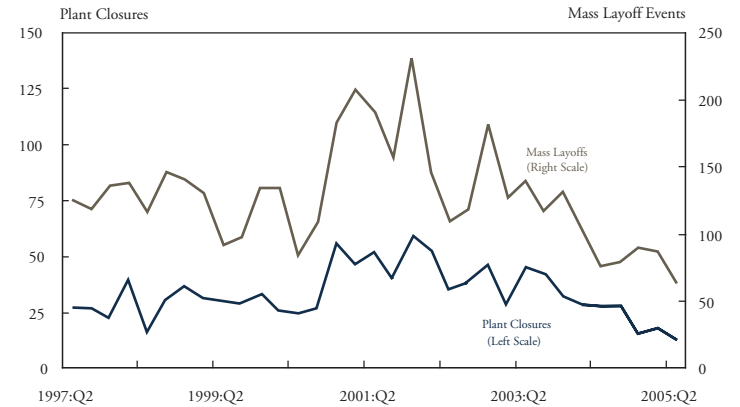
Despite recent improvements in manufacturing, the sector continues to suffer from the longer-term trends of consolidation and restructuring. Manu-

facturing's share of rural employment has fallen from nearly 25% in 1970 to roughly 16% in 2004. This fall is due partly to the rise of other sectors of the rural economy but primarily to outright job losses.

While manufacturing as a whole has lost jobs over the last two decades, the composition of the *national* manufacturing workforce has simultaneously shifted in favor of high-skill occupations—an area where the U.S. holds a competitive advantage. High-skill workers have become a much larger share of the manufacturing workforce. In 1983, high-skill workers represented 16% of all manufacturing jobs. By 2002, this share had climbed to 25%. During this time, manufacturing jobs in medium and low-skill occupations fell 8.2% and 25%, respectively. In contrast, jobs for high-skill workers soared 36.6%.

Similar data is currently unavailable for rural manufacturing, although rural America has responded to

**CHART 4**  
RURAL PLANT CLOSURES AND MASS LAYOFFS



Source: Bureau of Labor Statistics

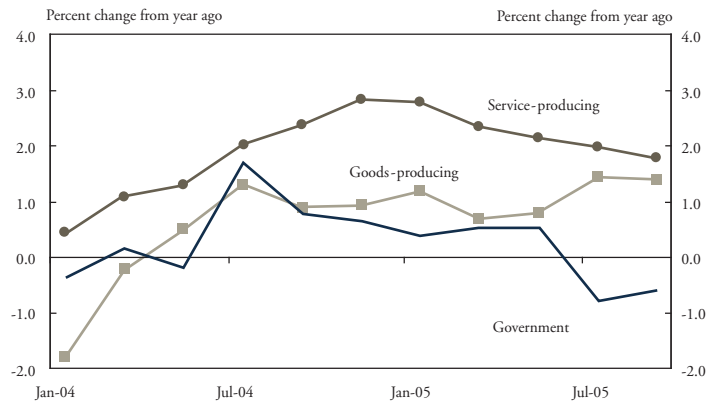
the nationwide shifts in the manufacturing workforce by providing more and more high-skill workers. Over the last three decades, the high school completion rate among rural workers increased from 35% in 1970 to 77% in 2000. Even more important, completion rates for community colleges and four-year institutions are up significantly. As long as the rural workforce has skilled workers, high-skill manufacturing firms should continue to call rural America home.



### A RENAISSANCE FOR THE RURAL SERVICE SECTOR

Across rural America, new opportunities for high-skill workers are emerging in services. The sector had a renaissance year in 2005, bouncing back mightily from the losses of the last recession and emerging as the leading source of job creation across rural America. Service payrolls increased well over 2% during much of the year, while traditional rural heavy-weights, government and manufacturing, mustered gains of less than 1% (CHART 5).

**CHART 5**  
**RURAL BUSINESS JOB GROWTH**



Source: BLS, payroll survey, seasonally adjusted

Within the service sector, the best performing groups in 2005 included producer services and consumer services. Producer services, largely made up of high-skill industries like professional and business services, made an impressive run, with year-over-year job growth at 3.3%. More important, the group accounted for the largest share of job creation in rural America, with 27% of the 291,000 jobs added during the year (CHARTS 6 AND 7).

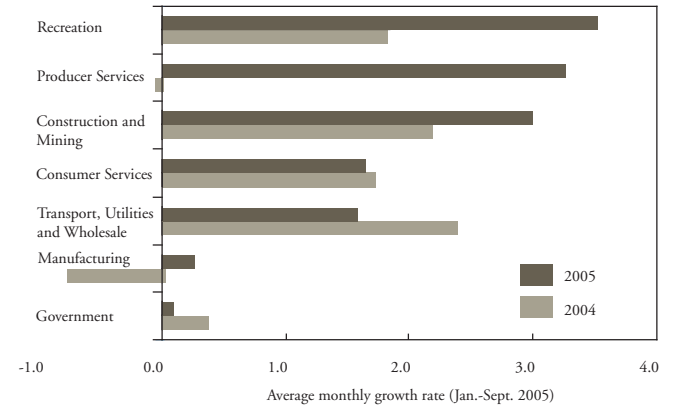
The much larger consumer services group (retail trade, education and health services) followed producer services,

accounting for 26% of the rural jobs created. Retail trade added a few jobs during the year. Education and health services recently passed retail trade as the third-largest area of the rural economy, behind manufacturing and government. The performance of these sectors shows that rural America can compete in high-skill services. One way high-skill rural workers are succeeding is through “rural sourcing.” Rural sourcing refers to the practice of relocating certain business operations, not in India or Mexico, but in rural areas, so that firms can take advantage of cost savings.

The practice has its roots in the outsourcing, or offshoring, of call centers and other IT operations to foreign countries. However, many among the recent wave of firms engaging in the practice are discovering that the benefits of locating operations in a foreign country do not always outweigh the problems.

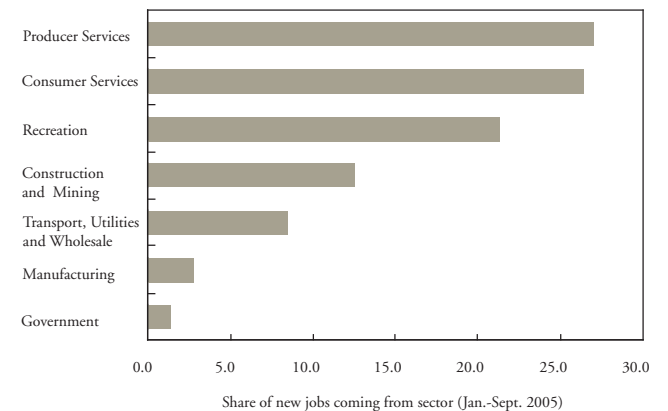
Increasingly, rural sourcing is seen as a way around these hurdles, enabling companies to reap the benefits of outsourcing while reducing their risk exposure. In the field of information technology, innovative firms such as Rural Sourcing Inc. are helping companies reach rural service workers. They operate as the link between companies seeking reduced costs and risks and rural America’s untapped high-skill workers. The arrangement has implications for the economic development of rural regions as well. Not only does rural sourcing provide cost savings to firms, but it also provides jobs to skilled rural workers who, because of geography, would not have access to such opportunities.

**CHART 6**  
**SECTOR JOB GROWTH**



Source: BLS, payroll survey

**CHART 7**  
**JOB CREATION LEADERS**



Source: BLS, payroll survey

# the rural economy

## ALL THINGS NATURAL BOOMING

Natural amenities and natural resources were booming areas for rural America during 2005. Recreational services contributed to the strength of rural labor markets in the first three quarters with strong growth at 3% (CHART 6). Growth was especially strong for regions with abundant natural amenities. These regions saw total employment growing nearly 4% in 2005. Land values across the country were also on the rise, with double-digit appreciation in many areas. Much of the buying interest for farmland came from recreational demand, which in turn helped fuel growth in recreational services.

Higher prices for oil, natural gas, coal, and other basic commodities helped spur profits for mining companies and increase the value of mineral rights. These higher prices also helped boost state and local government revenues through higher severance tax collections on mineral rights.

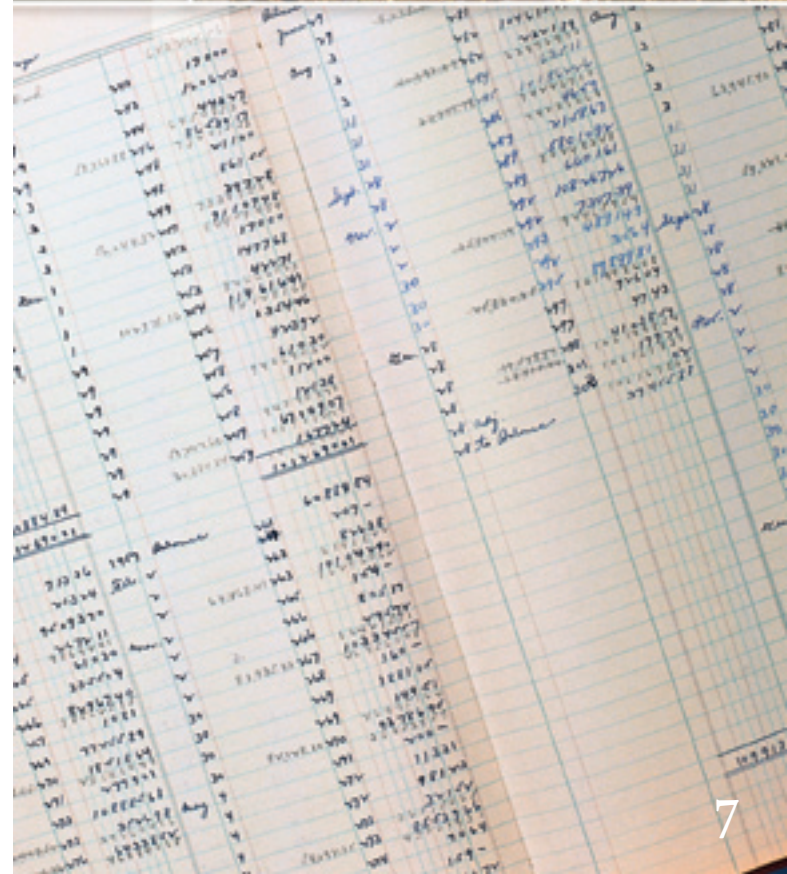
The boom in natural resources, particularly oil and gas exploration, has led to shortages of skilled workers. In some areas, demand for skilled oil and gas workers is currently so high that drillers must consider other options to cope with the shortage. In at least a few cases, drillers have imported

from China entire rigs, complete with crew, due to the domestic shortage of skilled workers and equipment. Companies and even states such as Colorado are addressing the skill shortages by funding training programs to develop an even larger trained workforce.

## A STRONG OUTLOOK FOR THE RURAL ECONOMY

The rural economy continued to shine in 2005 thanks to dual successes in agriculture and the nonfarm sector. Strength in agriculture was broad-based, fueling near-record returns. Natural amenities and natural resources should continue to boost the rural economy, although a possible slowing in the national housing market may cool the rural land boom somewhat.

Farm prospects continue to look bright for 2006. The outlook for traditional commodity-based rural manufacturing is less clear, although restructuring in the industry bodes well for high-skill workers. Meanwhile, rural America has seen the service sector reassert itself, becoming the leading creator of jobs in the nonfarm sector in 2005 and likely in the future as well.





# High Energy Prices

by JASON HENDERSON

BOON OR BANE?

## *The U.S. economy confronted soaring energy prices in 2005.*

The high prices were often a tougher challenge to rural economies due to their intense dependence on the automobile and their heavy reliance on energy-intensive industries. Still, high energy prices are a potential boon for rural places rich in traditional and alternative energy resources. Thus, despite the rising costs, higher energy prices might be the catalyst rural America needs to spark new economic opportunity.

### **HIGH PRICES: BANE FOR THE RURAL ECONOMY**

Prices for most major energy products (gasoline, natural gas, diesel fuel, coal) soared as much as 50% in 2005. Higher gasoline prices have a huge impact on rural households, due to their heavy dependence on cars and trucks for transportation. Rural businesses also appear to be especially sensitive to rising energy prices as they tend to be more energy intensive than urban businesses.

Prices at the gas pump remained roughly 25% above year-ago levels, despite falling from September's record levels. With rural America's long commutes, higher gasoline prices can be

painful to rural drivers.<sup>1</sup> According to the Consumer Federation of America, rural households spent \$2,087 for gasoline in 2005, compared to \$1,705 spent by their urban neighbors.<sup>2</sup> Accordingly, coupled with their lower income levels, rural households spend a greater share of their income on gasoline than urban households.

In addition to bearing higher commuting costs, rural households also pay higher bills for heating and electricity. Fuel oil and natural gas prices have posted the biggest gains over the past year, rising almost 50%. As a result, winter heating bills are surging, and analysts expect home heating expenditures to rise 48% in the 2005-06 winter heating season.<sup>3</sup> Heating bills may be especially high in rural areas, where local competition among fuel suppliers is less fierce.<sup>4</sup>

Rural businesses are also facing higher costs due to surging energy prices. In the farm sector, higher energy prices have led to substantially higher input prices. Compared to 2004, farmers paid 40% to 50% more for fuel in 2005. Higher natural gas

prices translated into higher fertilizer prices, with more sizable gains expected in 2006. Crop producers, especially corn and wheat producers that use more fuel and fertilizer, face perhaps the toughest challenge in dealing with higher energy costs.

Input costs are also on the rise for nonfarm businesses. Rural manufacturers are often more concentrated in energy-intensive industries. For example, in rural America, more than a third of manufacturing's earnings come from industries with above-average energy costs per value-added, compared to a quarter in urban areas.<sup>5</sup> Thus, higher energy prices are likely to take a bigger toll on rural business than urban business.

### **HIGH PRICES: BOON FOR THE RURAL ECONOMY**

While many rural businesses, workers, and residents feel the pinch of higher energy prices, the higher prices also present significant economic opportunities for rural America. Most of the nation's mineral extraction and energy production occurs in rural places. Higher energy prices also boost prospects for alternative fuels and other bio-based products, an opportunity in rural America that now burns brighter.

energy



Higher energy prices have boosted returns in the energy business—and in the process, have improved balance sheets for rural governments. Along with oil and gas companies, state and local coffers are seeing higher tax revenues. The higher oil and gas prices are boosting severance taxes, taxes paid on nonrenewable resources removed from the earth. The biggest gains happen in predominantly rural states, such as Wyoming and Oklahoma. Wyoming expected a \$10 million increase in severance tax collections when 2005 began, but collections were up more than \$40 million.<sup>6</sup> In addition, Wyoming now expects a \$220 million increase in mineral royalty payments.

Higher energy prices also provide new market support for bio-fuels as the costs of these alternative fuels become more attractive with higher petroleum prices. Ethanol use has exploded in the past two years. Ethanol is a bio-based oxygenate for gasoline and is the primary blending alternative for gasoline in regions that have banned the use of MTBE, a petroleum-based oxygenate that is added to fuel. In 2005, more than 4 billion gallons of ethanol were produced in the United States, up from 1.7 billion in 2001.<sup>7</sup> The new energy bill established a new renewable fuels standard that is expected to drive up ethanol use to 7.5 billion gallons by 2012. The number of ethanol plants has surged, and higher oil prices are making ethanol production more profitable (MAP 1).

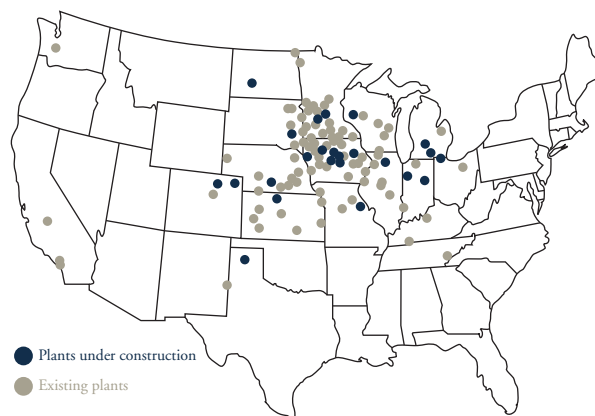
Bio-diesel is also expanding at a rapid pace. Environmental policy was already underpinning a surge in bio-diesel. The Clean Air Act mandates the reduction of sulfur from diesel to reduce particulates in the air. However, diesel fuel with low sulfur content has a greater corrosive effect on diesel engines due to loss of lubricity.

Soy diesel is a bio-diesel product that overcomes this dilemma because it has inherent lubricating benefits that make diesel fuel less corrosive. Higher fuel prices now make bio-diesel more competitive. Thus, investments in soy and other bio-diesel plants are increasing sharply with production capacity expected to increase over 50% in 2006.<sup>8</sup>

Higher energy prices not only support alternative fuels, they also make alternative sources of electricity generation more attractive. Across the country, substantial investments are made in wind turbines. In the Pacific Northwest, the amount of wind power capacity under development will power a million homes.<sup>9</sup> Nontraditional energy companies, like John Deere, are making investments in wind generation. Wind turbines provide another rural revenue source as farmers receive additional lease revenue to host wind turbines.

Surging fuel and oil prices are also underpinning new economic opportunities in products that can replace those made from petroleum. Bio-based alternatives are emerging in a wide range of products from paints to plastics to lubricants.

MAP 1  
CURRENT AND PROPOSED ETHANOL PLANTS



Many of these products are derived from oil seeds, such as soybeans. Others involve corn. In Blair, Nebraska, for instance, Cargill-Dow is deriving polymers for plastic containers from corn. The original driver for bio-based products was producing environmentally friendly products. With the surge in petroleum prices, however, some bio-based products are now actually cheaper than petroleum-based products.

Rural businesses, workers, and households are naturally concerned about the impact of higher energy prices. They must budget more for materials, gasoline, and home heating. Without doubt, high energy prices will be a drag on the rural economy and a challenge for rural America. But such challenges can become opportunities. Today's higher energy prices may indeed become the catalyst for a new generation of economic activity—right in rural America's backyard.

<sup>1</sup> Calculations are based on Department of Commerce data on U.S.A. Counties, CD.

<sup>2</sup> Cooper, Michael. 2005. "The Impact of Rising Prices on Household Gasoline Expenditures," Consumer Federation of America manuscript, September.

<sup>3</sup> Department of Energy, Energy Information Administration.

<sup>4</sup> Department of Energy, 2004. "Residential Heating Oil Prices: What Consumers Should Know," DOE/EIA-X048, September.

<sup>5</sup> Calculations are based on REIS data from the Bureau of Economic Analysis and Census of Manufacturers data.

<sup>6</sup> Congressional Revenue Estimating Group, Economic Analysis Division, Wyoming State Government. 2005. *CREG Monthly Report*, September.

<sup>7</sup> American Ethanol Coalition, [www.ethanol.org](http://www.ethanol.org).

<sup>8</sup> Calculations are based on expectations from National Biodiesel Board, [www.biodiesel.org](http://www.biodiesel.org).

<sup>9</sup> Harvesting Clean Energy, [www.harvestingcleanenergy.com](http://www.harvestingcleanenergy.com).

# New Federalism—

## PROBLEMS OR OPPORTUNITIES for RURAL AMERICA?

by SARAH A. LOW

*The federal budget deficit remained high in 2005.*

One way Washington has responded to this problem in the past is by shifting more responsibility for social programs to state and local governments, a process called *New Federalism*. This process has been under way for more than four decades and has resulted in more local control over spending programs, something rural communities underuse. Federal grant money helps states pay for these programs—but the grants often come with a price. Many grants have mandates that are not fully funded and require the states to contribute funds.

This shift in authority and heavier burden on spending touches all state and local governments, but evidence suggests it puts particular strain on rural regions. Smaller, more remote communities are less able to marshal necessary financial resources. They already receive less federal funding per capita than urban places. And their limited staffing often makes it difficult to compete with urban areas for federal funds.

But New Federalism also offers rural America new opportunities. The transfer of authority to local leadership gives

communities more discretion over the use of federal monies. New Federalism can also spur the formation of partnerships that can help rural regions tap federal funds and provide public services more economically.

### THE ROOTS OF NEW FEDERALISM

Before New Federalism was conceived, the states and the national government shared power for spending federal funds. New Federalism changed this relationship, transferring more federal power down to states and localities. This shift was intended to decentralize control of federal funds and to make federally funded programs more responsive to local needs. Rural areas, like their urban counterparts, welcomed this shift in authority.

President Richard Nixon coined the term “New Federalism” at a time when the economy was struggling with energy shortages, rising unemployment, inflation, and recession. His intent was to shift responsibility for federal programs to state and local government through block grants, large

sums of money granted to states and localities with much latitude on how the money was spent.

The Community Development Block Grant (CDBG) program gave states more discretion over spending federal monies and remains to this day one of the federal government’s primary development programs. The CDBG program, however, has one important caveat: Certain federal conditions must be met, or else block grant funds are reduced or eliminated altogether.

Attempts were made throughout the 1980s and 1990s to reduce federal authority on local spending. During the Reagan administration, a number of social programs were consolidated into nine block grants, strengthening local control and increasing spending flexibility. During the Clinton administration, Congress compelled the federal government to pay states for the enforcement of new federal policies and mandates—although some analysts debate the effectiveness of this legislation.<sup>10</sup>

Thus, New Federalism and the resulting shift to more local leadership can have a significant impact on poverty, education,

and environmental and emergency preparedness programs:<sup>11</sup>

- In 1996, welfare reform gave states new authority to run their welfare programs with federal block grants.
- In 2000, the Educate America Act reduced national education regulations and gave the states more money to meet education goals. The No Child Left Behind legislation recently reversed this trend, increasing the federal regulations of public education—a power that has traditionally rested with local school boards.
- Recent calls for reducing federal environmental regulations favor a prominent role for regional government and grassroots organizations.
- The terrorist attacks of 2001 were the impetus behind changes in grant programs for state and local emergency preparedness.

Policymakers at all levels of government tend to agree that local control is essential to the success of these programs. In short, New Federalism empowers states and localities to address such social issues on their own terms, rather than following a one-size-fits-all national policy. Still, as federal funds do not fully fund all federal mandates, the transfer of federal government roles to state and local governments often creates a fiscal and resource squeeze for many regions.

### NEW FEDERALISM—PLACING RURAL AMERICA AT A DISADVANTAGE?

New Federalism can be a disadvantage when federal responsibilities are pushed down to regions where a limited tax base or taxation authority makes meeting fiscal obligations difficult. The National Conference of State Legislatures estimates the unfunded cost imposed on states will reach \$30 billion in fiscal year 2006.<sup>12</sup>

The cost of New Federalism hits rural regions especially hard. Rural areas often have a small tax base and receive fewer federal funds per capita than urban areas. Additionally, many rural regions lack the technical resources to win competitive federal grants, a funding mechanism that is gaining wider acceptance in Washington.

### Rural Areas are Harder Hit by Federal Spending Requirements

To receive federal block grants, states are required to contribute funds of their own and meet the federal standards attached to the grant. Many analysts feel these standards often have the effect of imposing unfunded mandates on state and local governments. As a result, these governments sometimes must cut local priorities to meet federal requirements.

Covering the cost of unfunded mandates is typically more difficult for rural states than urban states. In rural states, unfunded mandates are estimated to account for 4.7 to 8.2% of state budgets—6.3% on average.<sup>13</sup> By contrast, unfunded mandates cost the average urban state 4.5% of its budget. In fiscal year 2004, South Dakota, a rural state, spent approximately 7.3% of its general fund appropriations covering the costs of such programs. Meanwhile, the predominantly urban state of Connecticut spent 2.5% of its general fund on cost shifts from the federal government (MAP 1).

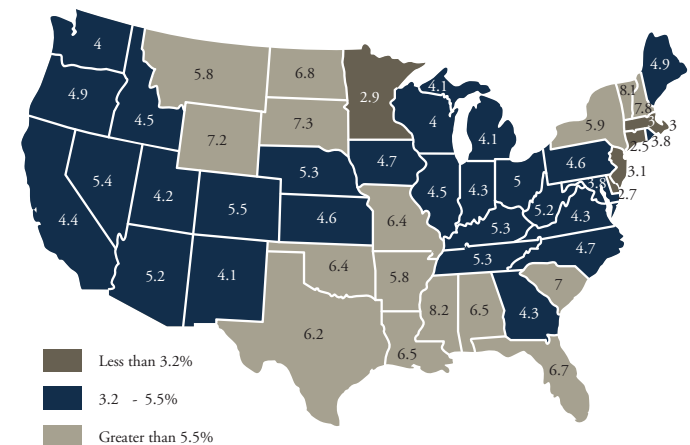
### Rural America Receives Less Federal Funding

The problem of unfunded mandates is compounded because rural states already receive a comparatively smaller portion of the federal spending pie. Over the past five years, average annual federal spending per

person was \$328 higher in metro areas than in nonmetro areas.<sup>14</sup> In some categories of federal spending, the gap is even wider. For instance, in 2001, the federal government spent three times as much on metropolitan community development (\$20 per capita) than on rural community development (\$6 per capita). Agricultural and natural resource spending accounts for the majority of federal funding going to rural areas (\$564 vs. \$46 per capita in metro areas), other than income security.

Further, many rural communities are at a disadvantage in receiving federal funds because Community Development Block Grants are more difficult for rural communities to obtain. Metro counties of greater than 50,000 people receive guaranteed CDBGs each year, while rural areas must compete against one another for smaller, one-time, state-administered CDBGs.<sup>15</sup>

MAP 1  
PERCENT OF STATE APPROPRIATIONS SPENT  
ON UNFUNDED FEDERAL MANDATES





### *The Competitive Funding Disadvantage*

Competitive federal funding grants are gaining popularity as a vehicle for delivering federal funds to localities. A recent report of the Strengthening America's Communities Advisory Committee concluded that competitive grants are the best federal funding mechanism for regions because they achieve results and ensure accountability.<sup>16</sup> However, the report notes that distressed communities, including many rural communities, may need technical assistance to compete for these

grants. Rural governments find it harder to compete for grants due to their small scale and limited resources. Rural government leaders are often part-time or volunteer public servants with relatively few or no paid staff. In comparison, urban jurisdictions often have full-time economic analysts, grant writers, and program coordinators. Rural regions may be better able to access federal funding if they put aside previous competition between communities and work together as a larger economic region.<sup>17</sup>

### **NEW FEDERALISM—PROBLEMS OR OPPORTUNITIES FOR RURAL AMERICA?**

New Federalism can result in spending increases that strain rural finances as rural regions face a funding gap, partly due to their smaller tax base. Starting out with fewer federal funds per capita exacerbates the problem. A future shift to competitive federal funding mechanisms may widen the metro/rural funding gap unless rural regions obtain more grant-writing resources and boost their technical skills.

New Federalism essentially puts rural governments at a fork in the road. One pathway leads to acceptance of the widening funding gap. Another pathway may lead to a stronger fiscal balance. By partnering with other communities, and pooling resources, rural governments can work to become more efficient in providing public services—and more competitive in winning federal grants. Going it alone has always been a natural course for rural communities. Competition and independence have defined rural culture for generations. Just as small towns have battled one another on high school football fields, they have also battled each other for new industries and economic development.

# new

Forming regional partnerships is the more difficult path, but two key benefits arise from rural regions working together. Previously fragmented communities can reduce the costs of providing public services by pooling resources and working together. Regional cooperation can bolster communities' ability to provide a variety of services, such as small business assistance and education programs. In addition, by partnering, rural communities can hire economic analysts, grant writers, and program consultants to help win competitive federal grants—competitive edges that rural communities by themselves could never afford.



# federalism

One success story in rural partnering comes from Missouri, where rural counties partnered with the city of Columbia to provide support for the Mid-Missouri Technology Business Incubator. Local leaders formed the partnership to benefit a number of surrounding rural communities. This broad regional involvement significantly influenced the federal government's decision to support the Incubator. By itself, the city would not have been eligible for federal support. But making the project regional in scope—by embracing distressed neighboring communities—was a critical factor in the partnership receiving federal funds.

The Missouri example, and others like it, shows that regional partnering can be an essential step in accessing federal funding and meeting the fiscal challenges of New Federalism. New Federalism clearly poses problems for both rural and urban places. But at the same time, it gives rural governments a new choice that in the end may hold strong benefits.

<sup>10</sup> Boyd, Eugene. 1997. American National Government, Government Division. U.S. Department of State.

<sup>11</sup> Close Up Foundation Civics Education. 2005. "The New Federalism." [www.closeup.org/federal.htm](http://www.closeup.org/federal.htm).

<sup>12</sup> Congressional testimony of Delegate John Hurson, President, National Conference of State Legislators, regarding the Unfunded Mandates Reform Act of 1995, April 14, 2005.

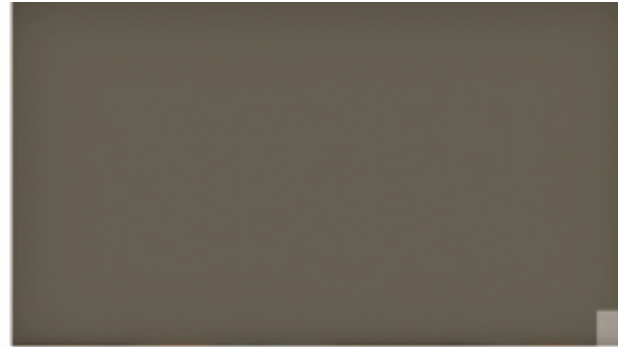
<sup>13</sup> The smallest unit of analysis is U.S. states. We define rural states as having 35% of the population living in rural counties. Appropriation and unfunded data from the National Conference of State Legislatures, May 12, 2004.

<sup>14</sup> Information was summarized from "Federal Investment in Rural America Falls Behind," W.K. Kellogg Foundation. 2004.

<sup>15</sup> Fluharty, Charles. "Assessing the State of Rural Governance in the United States." Proceedings, New Governance for a New Rural Economy. Federal Reserve Bank of Kansas City. 2004.

<sup>16</sup> Report of the Strengthening America's Communities Advisory Committee, July 2005.

<sup>17</sup> Fluharty.





# Sprawl:

by STEPHAN WEILER

## FRIEND OR FOE TO RURAL PLACES?

*The expansion of cities has been perhaps the most distinct geographic evolution of the American landscape over the last few decades.*

Metropolitan counties grew 12.3% per decade between 1970 and 2000, adding roughly 70 million new residents. As the demand for housing has risen, growth has naturally occurred at the suburban edges of these cities.

While there is no exact definition of “sprawl,” the term connotes the increasingly low-density residential development that occurs at the edges of urban cores. Such development implies that an urban core of a given population will occupy more land, thereby encroaching on previously less-developed rural landscapes.

Sprawl has been both a friend and foe to rural communities. Such growth reflects the dynamic job market of metro areas, which has been considerably stronger than in rural areas and has often literally carried rural communities in their wake. Yet development pressures are rapidly reshaping traditional land uses, leading to a sense of a loss of control in these communities. Further, evidence shows that new residents don't always

bear all the costs of new development, leading to spillovers onto the economies and ecologies of neighboring rural areas. In short, sprawl creates a dilemma for many rural communities in the push of development. Partnering across traditional jurisdictional boundaries can help mitigate these problems, but such partnering is slow to emerge.

### SPRAWL'S PACE

The growth at the periphery of many urban areas has been remarkable. The suburbs of Los Angeles, often seen as the epitome of sprawl, added over 15% to their population each decade from 1970 to 2000. The suburbs of Phoenix sprawled four times as fast.<sup>18</sup> In the mid-1990s, the edge of the Phoenix metro development swelled over seven feet per day.<sup>19</sup> Similarly, Denver's suburban ring grew more than 35% on average in each decade from 1970 to 2000.

Metro areas dominate population growth and associated land use patterns for the country as a whole. In the 1990s, metro

counties in general grew more than 55% faster than rural counties. Their suburban fringes absorbed 83% of the largest metro areas' new residents. Land consumption rates doubled population growth rates, underscoring the voraciousness of development patterns.<sup>20</sup>

Economists tend to view these growth patterns as natural. Some locations simply have an advantage over others in their ability to grow. The most central locations specialize in activities that require a lot of face-to-face interaction or offer different business clusters that can exploit synergies with one another. In contrast, when large amounts of space are plentiful and tight-knit interactions with other neighbors are not necessary, single-family housing on larger parcels of land often develop.<sup>21</sup>

### FRIEND OR FOE?

Interestingly, this rapidly evolving rural/urban interface has in many ways been a friend to rural areas that have otherwise faced economic stagnation. Rural counties closest to metro areas have directly benefited from the job and income spillovers emanating from the urban core. Over the 1990s, nonmetro counties adjacent to metro areas had 25% faster

job growth than their more isolated counterparts. The income and population growth of Denver's burgeoning Douglas and Elbert counties in the latter part of that decade were directly attributable to the growth of high-wage technology positions in southern Denver's technology parks.

Even hinterland rural areas have found ways to create opportunities from long-distance relationships with urban centers. Nearby farming communities often provide high-value food products to urban gourmets and restaurants. Rural areas also supply services to metro areas, such as the back office facilities in California's Central Valley that support high-tech Bay Area companies.

New challenges, however, are emerging. The growth of cities has led to an increasing demand for lower-density perimeter sites, effectively extending urban areas into "exurban," previously rural areas. Given that residents' willingness to pay for an acre of residential land is much higher than virtually any other traditional rural use of the land, such as production agriculture, the value of land near these urban areas is increasing rapidly.<sup>22</sup>

The surge in exurban land values is even greater near cities that have recently experienced a housing price boom, such as in California and along the Rocky Mountain urban corridor. Rural residents in these areas feel like they are losing control over their communities' shape and direction in the face of these market forces.

The costs of such new fringe developments are often high and not always borne by the developers or the new residents.

Infrastructure, such as roads and utilities, is often underpriced relative to its actual costs in these settings, implying that residents in more central areas are effectively subsidizing fringe developments.<sup>23</sup> Such underpricing can make larger parcels and more extensive sprawl more attractive than would be the case if developers and homeowners faced the true cost of needed infrastructure.<sup>24</sup>

In addition to existing fiscal consequences, sprawl can also create new foes for previously distinct rural areas, particularly in terms of environmental impacts. For example, the increasing number and severity of wildfires in the West is one result of such new types of development. Protecting far flung residences from wildfires can be costly, consuming a disproportionate amount of public resources. Further, the encroachment of such residential development into more sensitive landscapes also increases the likelihood of such wildfires in the first place. This type of "cumulative causation" only exacerbates the implicit subsidy created by infrastructure's average cost pricing in sprawling residential development.<sup>25</sup>

Regional collaboration is the key to turning these challenges into opportunities. Partnerships involving government, institutions, and the private sector will help determine whether rural areas ultimately gain more than they lose from sprawl. Urban areas and rural peripheries both benefit from the economic growth that urban cores generate, and thus both have a stake in productive partnering that mitigates sprawl's fiscal and environmental problems. Proper

pricing of infrastructure and agreements on parcel sizes and open spaces are critical to raising everyone's well-being.

First steps are being taken on just such cross-jurisdictional challenges. According to the American Planning Association, 12 states had developed state-wide growth management guidelines at the turn of the millennium, although only a handful have yet imposed any coordination of management plans at lower levels of government. The various jurisdictions within the Phoenix area all use growth management tools, but there is not yet much coordination among them.<sup>26</sup> Various regional mechanisms thus appear to recognize a need for cooperation. Further coordination could help growth and sprawl move from foes to friends as rural and urban areas continue to evolve together in the new millennium.

<sup>18</sup> Rappaport, Jordan. 2005. "The Shared Fortunes of Cities and Suburbs," Federal Reserve Bank of Kansas City *Economic Review*, Third Quarter, pp. 33-60.

<sup>19</sup> Morrison Institute for Public Policy. 2000. *Hits and Misses: Fast Growth in Metropolitan Phoenix*. Phoenix: Arizona State University Press.

<sup>20</sup> U.S. Department of Housing and Urban Development. 2000. *The State of the Cities*. Washington, DC: Government Printing Office.

<sup>21</sup> Alonso, William. 1964. *Location and Land Use*. Cambridge, Mass. Harvard University Press.

<sup>22</sup> Novack, Nancy. 2005. "Agricultural Credit Conditions: Booming Farmland Values," *Main Street Economist*, June.

<sup>23</sup> Brueckner, Jan. 2000. "Urban Sprawl: Diagnosis and Remedies," *International Regional Science Review*, 23(2) 160-71.

<sup>24</sup> Dispersed rural residential development in Colorado costs county governments and schools \$1.65 for every dollar of new revenue produced (Coupal, Roger, and Andrew Seidl. 2003. "Rural Land Use and Your Taxes: The Fiscal Impact of Rural Residential Development in Colorado," Agricultural and Resource Policy Report 03-03. Colorado State University: Fort Collins).

<sup>25</sup> Weiler, Stephan and David Theobald. 2004. "Pioneers of Rural Sprawl in the Rocky Mountain West." *Review of Regional Studies*, 33(3): 264-83.

<sup>26</sup> Morrison Institute for Public Policy. 2000. *Hits and Misses: Fast Growth in Metropolitan Phoenix*. Phoenix: Arizona State University Press.

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