7. Issues and Recommendations for Program Improvement

The core of this report is in the assessment of ARC investments relative to project outcomes. That investigation, including subjective discussions with stakeholders, also suggested a modest list of recommendations as a reflection on issues that arose from the evaluation of the 104 projects. These observations are not meant as a total assessment of the program, its priorities, or its delivery system.

The Commission's investments and priorities have—and will continue to be—fundamentally driven by three factors:

- Internal policy objectives such as investment focus on distressed and at-risk areas, and stimulation of entrepreneurship,

- Identification of objectives and opportunities by local and district-level development entities within the Region; and

- State priorities and fiscal constraints.

Recognizing these overarching factors, the comments that follow are offered to inform the program and its investment process.

* Measured Outcomes Indicate Reasonable Investment Strategy

All project classifications appeared to us to fall within reasonable and accepted job cost parameters using the ARC share calculation method (and certainly by the full credit method). In general, there is a clear efficiency to utilizing projects that serve multiple firms, as most except industrial site project are likely to do.

Costs associated with the development of incubators, whose primary service purpose is to nurture enterprises early in their formation, are undertaken with the understanding that the most meaningful job creation will come in later stages. For that reason, and because of the stark problems of entrepreneurship faced by large segment of the Region (below), the solid new job return on investment of incubators is specifically noted.

While the telecommunications projects in the sample pool appeared to be highly effective and popular among stakeholders (including among those who have not yet applied for any) the nature of these projects call for attention to meaningful ways to project and measure outcomes. This is a difficult process which would benefit from some intensive thought.

While the housing projects reviewed generally fulfilled their projections and, in several cases, triggered community revitalization beyond expectations, there are no historic guidelines to assess housing costs (as there are for job creating economic development efforts, for example). The ARC appears not to have developed any guideline in-house, either. The classification would benefit from a housing cost policy which addresses issues such as per unit dollar guidelines, and inclusion and assessment of indirect (e.g., area business) impacts.

Projects Made Progress On Strategic Objectives

While statistical measures are important, progress on strategic objectives which address the weaknesses of the Region are at least as critical to the investment process. As Chapter 5 suggests, projects in the sample pool had real impact on their host communities, often far beyond (and sometimes in different directions) than originally anticipated. Specific job projections aside, the effect of the project pool overall on a range of strategic objectives important to the Region's future should not be minimized, including:

- Economic diversification stabilizing local economic conditions;
- Reuse of vacant or underutilized sites and consequent revitalization of surrounding neighborhoods;
- Support for traditional industries that continue to be the backbone of many project counties;
- Successful speculative development efforts;
- Enhancement of local work force development;
- Significant non-economic community revitalization impacts;
- Tangible progress in distressed counties.

Highly Favorable Perception of the ARC Program

The Region's administrative approach to the Program consciously streamlines the development process by making commitments and following through without adding administrative burdens to either the Commission or its grantees. The current system is highly regarded by local development professionals and should be maintained. Project stakeholders consistently commented on the ease of working with the ARC, and several noted with approval the ARC's ability to invest in planning and feasibility studies necessary to subsequent projects. However, as discussed in more detail below, a disturbing number of project areas appeared to retain only partial information regarding project development or outcomes, a situation which will weaken the program if not remedied.

The Infrastructure Program's ability to fund limited residential-only and speculative development projects is also highly valued. The Program's ability to provide flexible economic development investments without demanding a bird-in-hand is prized among economic development professionals. Looking at the projected and actual impact results, investments targeted for residential and speculative economic development (though less convincingly in this evaluation round) appear to have generally paid off.

Importantly, representatives of almost three-quarters of all projects in the sample pool (and 76% of all economic development projects) expressed the opinion that their specific projects would not have been undertaken or completed without ARC participation. This widespread assessment indicates a valued and discerning eye for critical project investments by ARC staff.

File-Keeping Protocols Would Benefit From Attention

Through the interview process, there were indications that project files in several areas had not received the preliminary or follow-up attention required to help ARC fully understand results of its investments. In most cases, these deficiencies were partial, although in several cases significant. Interviewees (who were identified as key regional or local project contacts) were sometimes bereft of information on projects or unable to locate files.

In all, we noted information deficiencies of varying levels in 35 projects (34%), including:

- 6 projects with limited or no original impact projections;
- 13 which could not confirm key budget information;
- 14 could not confirm the existence or volume of private investment resulting from the project;
- 9 which could not confirm job impacts; and
- Many which could not confirm wages or other job quality indicators resulting from the projects.

While one state (MS) appeared to have limited information on as many as five projects and several were unable to respond completely for three or four, there was no discernible geographic pattern among areas with deficient projects. There were three information-deficient projects in two different LDDs, but that is not to say that the LDDs themselves were the responsible record-keeping entity.

This is a complex situation: On the one hand, ARC is lauded by development professionals because it ties a minimum of administrative burden to its investments. On the other hand, it is clear that projection and outcome files must be kept if the ARC is to learn from its successes and disappointments. We strongly suggest that a file-keeping protocol which aligns with, and does not add to the requirements of, ARC's common funding partners, be developed and strictly applied.

It's also worth noting that the 2000 evaluation round made some related findings:

Data collection might be refined to include closeout information on actual private investment related to ARC-funded projects. In addition, ARC could explore with other federal, state, and local agencies how to devise better data collection methods for assessing the quality of jobs, the associated wage rates, and even the extent of part-time vs. full-time hours associated with these jobs.

In the meantime, the ARC has also identified this issue and has entered into discussions with other basic funding agencies to address it (through the venue of OMB and an interagency coordinating council). In light of limited resources and the unlikelihood of added incentives to grant recipients in the field, the simplest effective solution might simply involve follow-up from the ARC at project close-out in order to ascertain impacts to date.

Project Classification System Should Be Reviewed

At several points in the evaluation process, it became clear that project classifications were often ambiguous, to the extent that the designations themselves should be revisited.

Most common was the overlap between industrial site, industrial park and development-related water-sewer projects, which could themselves take place in the service of an industrial park or site (and were in some cases specific to them). In other situations, it was difficult to understand the decision to designate a project as an industrial park versus site; both appeared suitable, and the classifications appeared to be without apparent difference. One telecommunications project took place in an incubator, serving incubator clients, and could have been classified as either. Access road projects are, almost by definition, specifically related to large industrial site or park development efforts, and access road costs are often folded into projects that adopt those classifications.

In short, the categories without a difference might be merged, and differences in function that most likely affects outcomes (for example, re-use projects where costs might be higher and job development lower, but in the service of the additional virtue of blight reduction) might be considered as new designations.

Consider Expanding Telecommunications Investments and Focus on Traded Services

As noted in Chapter 6 of the report, 64% of all project areas report communications sector sales concentrations (area based firms) that are less than 50% of the US average. This sector is apparently struggling and, in view of its national growth numbers, provides an opportunity for ARC districts.

While Chapter 6 also notes progress in the broad (often lower-value) services sector in project areas, the communications data suggest that traded services continue to lag significantly throughout the region, as we originally pointed out in the 2000 evaluation round:

> In the same (1990-2000) period, service concentrations increased in only 43 of 76 project areas despite the national explosion of firms and jobs in this sector. These findings suggest (the desirability of) increased attention to development of traded services and projects targeting their development.

This is an important area for strategic focus; as manufacturing declines across the economy, value-added traded services (that is, services which are likely to bring in dollars from outside the area in which a company is located) become critical value-added generators for the local economy. And it is in these services, in particular, that project areas and, we project, the Region, is weak.

In support of this notion, we found that 75% of all project areas reported sales concentrations of area-based Financial Services and related firms at least 20% below national levels. The jointly lagging communications and financial services industries suggest that the regional lag in traded services has, if anything, deepened.

That prelude underscores the need expressed by a variety of stakeholders for rural broadband access and additional telecommunications investment by the ARC. This envisioned future project focus was at least a pervasive as expressions of interest regarding more traditional infrastructure needs. It is particularly noteworthy that in one telecommunications project area, the ARC investment was credited with the success of a local incubator, including the repatriation of a local business which had previously relocated to an urban area with broadband access.

In addition, investments targeted toward area-based firms in these sectors would help balance local economies and strengthen the region in the country’s two highest growth sectors.

Consider Simultaneous Telecommunications and Bricks-and-Mortar Investments in Single Sites

The frequent emphasis placed by project stakeholders on the impact of telecommunications enhancements for businesses in rural areas suggests that ARC consider simultaneous investments (bricks-and-mortar and telecommunications) at single sites. From urban locations with routine broadband and cable access, it's easy to forget the relative advantage of businesses in connected areas over those which are not so favored. The attraction of rural sites, and the added likelihood of success for businesses at those sites, is greatly enhanced by state-of the art telecommunication infrastructure. Investment in sites without that access will be increasingly hindered by the lack of high speed connections. On a case by case basis, ARC should consider enhancing the competitive advantage of its bricks and mortar investments with corollary telecommunications project investments as well.

This added focus would aid in general business development efforts, but in particular with new traded services initiatives, due to the disproportionately heavy reliance of traded services firms on cutting edge connections.

Consider Retention Growth Investments

Because we think what we have to say about the growth problems of mature firms could be significant, we've decided to briefly review that Chapter 6 discussion here.

Here's what we did: We took the universe in each project area in 1998, and tracked those firms (and only those firms for this analysis) through 2004. We did the same thing for all identified firms doing business throughout the US in 1998. The firms that we began tracking in 1998 and that were still in business in 2004 we refer to here as "mature" or "survivor" firms.

Then we looked at the growth patterns of the groups of mature firms. We found that the mature firms in Appalachian areas we reviewed grew less than the national rate of that peer group (using annual reported sales as a benchmark). We also found that, in an uncomfortable number of cases, the proportion of mature firms in Appalachian areas which fell into very small sales classes actually increased over time. Moreover, we saw (from the separate entrepreneurial activity analysis) that many Appalachian areas coupled the "mature firm growth" problems with sluggish entrepreneurial activity.

Here are the details:

Nineteen of 70 project areas reported very small sales category survivor (mature) firm concentrations that were at least 120% of the US average. This means that higher proportions of mature firms in project areas have fallen behind relative to their peers at the national level. This stark concern suggests added project focus on retention and growth assistance to existing firms, with the awareness that assistance should be reviewed for viability of the candidate firms, especially given some of the ARC's recent experience with traditional firm projects (e.g., Mountain City Sewer, Hammondsport Access Road).

Areas reporting both low entrepreneurship indices and disproportionately high concentrations of low sales firms among the more mature business population (survivors) should be the focus of some particular concern. Twenty-seven project areas indicate both a survivor sales class index of the lowest sales-level firms that is at least 10% above US norms and startup activity indices below the project area average of 0.81 (19% below US levels).

At least 30% of all project areas showed small sales survivor concentrations at least 110% of the US level and startup activity indices 20% below US levels. That finding calls for a review of concerns in such areas and the development of the programmatic efforts aimed at the growth of mature regional firms.

Consider Expanding Investments in Entrepreneurship

As detailed in the Section 6 Economic Vitality Analysis, entrepreneurship lags extensively throughout the sample pool. This is the case in the current evaluation round as it was in the last. Some progress has been made in some locations, there are further declines in others, but the conclusion is inescapable; the Region's distressed, at-risk and transitional areas appear to bear the burden of sluggish long-term entrepreneurial activity.

Second -- the good news -- is that focused efforts to address this problem work. Incubators were among the most successful projects in this evaluation, as they were in the 2000 evaluation round. Incubators sustain new businesses, help create jobs -- and appear to retain the firms and jobs they create in the areas served.

Once again, ARC dollars targeted at incubators (new and expansions) paid off. Once again, representatives of incubator projects expressed the need for ongoing operational and technical assistance.

Additional investment with entrepreneurial targets -- incubator and technical assistance -- is highly recommended for consideration.

In the 2000 evaluation round, we noted the value of follow-up technical and operational assistance to various projects, but especially incubators:

> Certain valuable projects, often in remote and distressed counties, are unlikely to be self-sufficient for several years. Follow-up operational support should be selectively considered, particularly in areas not poised for high growth. It is important to condition this support with an evaluation of the project sponsor's plan to develop self-sufficient operations. In general, this costly assistance would be best used for critical strategic efforts--such as the development of much-needed "full-service" incubators.

While we found incubators that were on sure economic footing this time around, there were others that --despite strong tenancy records -- had been forced to cut staff and/or services. In addition to broader incubator efforts, we continue to believe that follow-up assistance -- whether emanated by the ARC or state entities -- is a critical piece of the ongoing struggle to enhance entrepreneurial activity and success in Appalachia.

Other Prior Concerns

At least three other recommendations that were noted in the earlier (2000) evaluation round did not surface in any of the project sample reviews this time, which is in itself worth noting:

- In 2000 we noted that:

> A number of counties will likely have "developed themselves" out of future grants because of a higher economic status by the 2000 census. The Commission should consider promoting the "pocket of distress" concept to permit applications from distressed portions of those counties which have progressed from distress status as a whole, but retain significant distressed portions.

ARC has since developed a "pocket of distress" policy which was implemented in 2002. The fact that the abandonment of distressed pockets in otherwise thriving counties was not raised by a single stakeholder this time around is in itself an indicator of some success.

- We also suggested in 2000 that "project buy-in should probably include commitments from non-recipient agencies (e.g., area zoning commissions) in a position to influence project outcomes", largely in an effort to avoid sprawl consequences from projects. With the exception of traffic issues in a competitive county with a large and hugely successful technology park (Huntsville, AL), sprawl did not arise as an issue in our discussions with stakeholders this time. We are informed by ARC staff, however, that it remains a concern in areas that are close to competitive or attainment counties (e.g. North GA, eastern panhandle of WV).

- Finally, as the result of repeated concerns expressed by stakeholders, we asked this question at the end of the 2000 evaluation round:

> Should an economic project that will primarily create a competitive advantage to a community or county near a state border because of tax benefits be encouraged? Such a question is difficult to answer in the abstract--but efforts should be made to identify and grasp these and other likely indirect impacts before the investment is implemented, not after the fact.

Again, despite the border proximity of some projects, this issue arose in only one discussion this time -- and that was from a stakeholder eyeing commerce from across state lines that could be captured as a result of the project under review. ARC staff suggests that the pirating issue still exists, but may simply not have been prominent in the sample pool. We bow to the Commission's expertise and experience.