

Trends Magazine

America's Future? California vs. Texas
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In the 1950s and '60s, California was the embodiment of the American Dream, offering great schools, roads, jobs, and communities with all the latest amenities, not to mention good weather, beaches, and quick access to the mountains and wilderness for recreation. As home to Disneyland and the movie industry, the state represented all that was glamorous and new.



Cut to the present day. California is \$26 billion in the hole and has recently been paying its bills with IOUs. It takes on new debt at a rate of \$25 million a day. Its once-proud schools are suffering and the prison system is releasing criminals early because the state can't afford to keep them. Social services are being cut right and left. Infrastructure is aging and falling apart. Unemployment is nearing 12 percent. State employees are forced to take unpaid furlough days and many California cities are worse off than Detroit. Its state income tax is the second highest in the U.S., and government regulations seem perversely aligned to discourage people from doing business there.

Texas, on the other hand, was considered something of a backwater in the 1950s and '60s, and certainly not a glamorous destination for the upwardly mobile masses. How things change.

The Lone Star State has more Fortune 500 headquarters than any other place in the union: California has 51, New York has 56, and Texas has 64. AT&T, Dell, Texas Instruments, ExxonMobil, ConocoPhillips, American Airlines, Continental Airlines, Southwest Airlines, J.C. Penny, and Halliburton are all located in Texas.

Texas also has a geographic advantage over California. California has mountains that limit growth. Texas is largely flat. California is big. Texas is bigger. If you drive from Houston to El Paso, you're halfway to Los Angeles – without leaving Texas.

Texas created 70 percent of all the new jobs in the United States in 2008, and it has a budget surplus. Unemployment in that state is two percentage points below the national average. It has one of the lowest rates of repossession for housing. There is no state income tax, nor is there a tax on capital gains in Texas. No wonder it's the fastest-growing state in America, with 150,000 new residents arriving each year. **Houston promises to become the nation's third-largest city in the near future, edging out Chicago for that spot.** And 3 of the 10 largest cities in the United States are already in Texas – Houston, Dallas, and San Antonio.

Both the *Brookings Institution* and *Forbes Magazine* studied America's cities and rated them for how well they create new jobs. **All of America's top five job-creating cities were in Texas.** It's more than purely economics and regulation can explain, though. Texas – and Houston in particular – has a broad mix of Hispanics, whites, Asians, and blacks. **When Hurricane Katrina hit, Houston took in 100,000 people. Many stayed and are now grateful workers.** Not surprisingly, Houston has more foreign consulates than any American city other than New York and Los Angeles.

And while Texas is creating jobs and new business, the *Financial Times* recently observed that the failure of a state as large and important as California is serving as a drag on the entire U.S. economy. Much of what we perceive as a national housing crisis, for example, is really concentrated in a few of the hardest-hit regions – California and Florida chief among them. Meanwhile, areas such as Texas have experienced a much milder downturn. In short, the catastrophes in Florida, Nevada, and especially California make the national market look really bad.

California is home to almost 12 percent of the population of the United States, with some 37 million residents. As jobs are lost there, purchasing power goes down, and pay cuts on existing jobs make it worse. The overall effect is to slow the recovery from recession for the whole nation.

But, how did this happen? What's *wrong* with California, and what's *right* with Texas? It really comes down to four fundamental differences in the value systems embodied in these states:

- **First**, Texans on average believe in laissez-faire markets with an emphasis on individual responsibility. Since the '80s, California's policy-makers have favored central planning solutions and a reliance on a government social safety net. This unrelenting commitment to big government has led to a huge tax burden.
- **Second**, Californians have largely treated environmentalism as a "religious sacrament" rather than as one component among many in maximizing people's quality of life.
- **Third**, California has placed "ethnic diversity" above "assimilation," while Texas has done the opposite. "Identity politics" has created psychological ghettos that have prevented many of California's diverse ethnic groups and subcultures from integrating fully into the mainstream. Texas, on the other hand, has proactively encouraged all the state's residents to join the mainstream.
- **Fourth**, beyond taxes, diversity, and the environment, Texas has focused on streamlining the regulatory and litigation burden on its residents. Meanwhile, California's government has attempted to use regulation and litigation to transfer wealth from its creators to various special-interest constituencies.

In the wake of California's meltdown and Texas' ascendancy, what's ahead? And what will it mean for the country as a whole? Consider the following six forecasts:

- **First, as the recovery accelerates, expect to see California's loss of jobs to Nevada accelerate.** It's difficult for most employers to make a solid business case for starting up or expanding a business in California, when nearby Nevada offers so many advantages. Over the longer term, this high-profile debacle will serve as a wake-up call not just to California, but to states across the country.
- **Second, expect to see a backlash in California and across the country against regulations, especially green initiatives that can't clearly demonstrate a positive ROI.**

Everyone agrees that doing more with less and cleaning up the environment are desirable objectives. But they're not so desirable when they take away jobs or take down whole industries. Toyota, for example, recently announced the closing of its NUMMI manufacturing facility at Fremont, California. This operation has turned out more than five million cars since it opened in 1982 and it employed 5,500 people at an average salary of \$65,000 a year. A joint venture between Toyota and General Motors, the facility received 42 awards for environmental achievements. And, it was one of the greenest factories in the world, according to *Investor's Business Daily*. However, it was closed because California's regulatory environment is discouraging enough to drive out the best of businesses. The plant was able to chug along through a good economy, but in a recession, the burden was untenable. Notably, **Toyota is not going to stop making these cars**. It's simply moving the operations to Japan, Canada, and – you guessed it – Texas. A steady stream of developments like this one will force voters -- and workers are voters – to make sure that California laws don't end up shipping *their* jobs to Texas.

- **Third, watch for the smart money, including venture capital, to begin migrating to Texas for start-ups in many areas, including energy, info-tech, manufacturing, and biotech.** Just as Delaware's tax laws once encouraged numerous businesses to incorporate there, even when they had no connection to the state, Texas will become a magnet for new businesses by offering cheap land, a favorable regulatory environment, a business-friendly culture, and a large supply of skilled labor. Unless California revamps dramatically, expect to see its economy languish, even as the recovery takes off.
- **Fourth, to make its business climate even more business-friendly, Texas will invest heavily in secondary education and work hard to attract the best talent to its research universities.** Keep an eye especially on the University of Texas, which already has a first-rate campus and faculty. **Within 10 years, UT, as the locals call it, may well rival Stanford or Berkeley.**
- **Fifth, other states will adopt tort reform measures pioneered in Texas.** Unlike California and most other states, Texas has been aggressive in minimizing the enormous burden of frivolous lawsuits. While rabid plaintiff counsel, like Milberg Weiss and others, were allowed to “run amok” in California, Texas has seriously constrained their opportunities.
- **Sixth, look to Texas to become a cutting-edge cultural mecca.** Houston has always offered a vibrant cultural scene, ever since the Alley theater company was founded there in 1947 by Nina Eloise Whittington Vance. In the coming years, this trend will spread to the major cities of Texas, attracting the best talent and money and shifting the cultural balance of the nation away from New York and San Francisco.

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