



Kavet, Rockler & Associates, LLC

985 Grandview Road
Williamstown, Vermont 05679-9003 U.S.A.
Telephone: 802-433-1360
Cellular: 802-272-8385
Facsimile: 802-613-1014
E-Mail: Kavet@aol.com

Review of Act 250 Economic and Fiscal Analysis Associated with Proposed St Albans Wal-Mart Development

Prepared for the
City of St Albans, Vermont

May 12, 2006

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Background Information

Report Scope and Purpose

This report was commissioned by the City of St Albans. It reviews the economic and fiscal impact study associated with Act 250 Project No. 6F0585 for the development of a 160,000 square foot Wal-Mart retail store in the adjacent Town of St Albans, prepared in October of 2005 by Economic and Policy Resources, Inc.¹, hereafter referred to as “EPR.” This report specifically reviews economic and fiscal impacts that may be relevant to the City of St Albans.

Qualifications

This report has been prepared by Thomas E. Kavet and Nicolas O. Rockler, principals with Kavet, Rockler and Associates, hereafter, “KRA.” Together, the two KRA principals have more than 50 years of combined regional economic modeling, economic impact analysis, econometric, economic and demographic forecasting, database development, strategic planning and economic information systems expertise. We have extensive experience with REMI, IMPLAN, REDYN, BEA and other regional economic modeling systems and source data that may be used in regional economic and fiscal impact analyses, such as the subject analysis. We also have knowledge of and economic modeling experience with the geographic region that is focus of the subject analysis.

As Consulting Economist to the Vermont State Legislature since 1996, Thomas E. Kavet has provided expert testimony on a wide range of economic and public policy issues. He has conducted numerous regional economic impact analyses

¹ As rendered available on the Vermont Agency of Natural Resources website at:
<http://www.anr.state.vt.us/Imaging/Planning/6F0583/Economic%20Study.pdf>

and provides ongoing economic and revenue forecasting services and specific economic analyses in support of topical issues of relevance to the Legislature. Many of the semi-annual economic and revenue forecasts prepared by Mr. Kavet are currently posted on the JFO website at www.leg.state.vt.us/jfo/outlook.htm. Other legislative special studies in the areas of education financing, grand list growth, tax increment financing, tobacco and cigarette taxation, economic development, minimum wage and livable income analysis, diesel fuel taxation, energy policies, the New England Dairy Compact, related agricultural policies, numerous proposed tax changes, public school enrollments and detailed State demographic analyses are available upon request. Mr. Kavet also manages the Vermont REMI, REDYN and IMPLAN econometric models for the State of Vermont, Legislative Joint Fiscal Office and has worked as a consultant for REMI (Regional Economic Models, Inc. of Amherst, MA), the economic model system employed in the subject analysis .

Mr. Kavet has been an independent economic consultant based in Vermont for more than 15 years. Prior to that, he was a Vice President at McGraw-Hill/Data Resources, Inc. (DRI), now Global Insight, Inc., the nation's largest economic consulting and forecasting firm. At DRI, Mr. Kavet created and led the Construction and Real Estate Information Service, with responsibility for economic forecasting, econometric modeling, database and information systems development and management of more than 150 employees.

Nicolas O. Rockler recently completed a post-doctoral fellowship at the Massachusetts Institute of Technology where he worked extensively with county and regional economic issues. Dr. Rockler also has extensive prior experience with regional economic data and forecasting as an independent economic consultant and Director of Economic Products at McGraw-Hill/Data Resources, Inc. (DRI). While at DRI, Dr. Rockler managed macro-economic models and forecasts for many U.S. states and led the development of the first nation-wide metropolitan area forecasting service.

Over the past 25 years, Dr. Rockler and Mr. Kavet have collaborated on a wide range of public and private sector economic projects, including the first comprehensive regional estimates of the stock of U.S. buildings; state, city and county-level macro-economic and demographic models; county-level market demand systems; the largest construction and real estate database in the world, and currently, regional economic impact modeling associated with business development subsidies, housing, major hospital and health care policy issues, port and infrastructure development and environmental issues.

KRA is familiar with, and utilizes in its work, the latest in econometric modeling software and computer systems and has access to both human and data resources in federal and state government, among professional peers and with private sector contacts in a variety of relevant disciplines.

Primary Findings

Overview and Summary

We find the subject report to be an exceptionally detailed analysis of potential economic and fiscal impacts and of considerably greater depth than many Act 250 economic impact reports, however, ***there are critical methodological and modeling assumptions, along with data quality issues, underlying the analysis that we believe bias the results in a direction that significantly underestimates potential negative economic and fiscal impacts on the City of St Albans.***

While many of the subject report estimates and conclusions are not outside the plausible impact range, they do not, in our opinion, represent either “conservative,” as characterized in the EPR report², “likely” or “worst case” economic and fiscal impacts with regard to the City of St Albans. Instead, the impact estimates for St Albans could more appropriately be characterized as close to “best possible case” impacts.

Findings

Based on the data reviewed and information available to date, there are four major findings that render the impacts affecting the City of St Albans as both unlikely and unreasonable:

1) *The subject report did not utilize extant research and empirical analysis specific to Wal-Mart developments in modifying and specifying inputs to the core REMI model used to generate aggregate economic and fiscal impacts.* By using default model values for retail employment, payroll and related inputs, net retail employment and other aggregate economic gains are overstated, thereby understating likely competitive retail and other employment losses. We believe this misspecification could result in retail employment losses in the City of St Albans that are at least four to five times those presented in the subject report.

Nowhere in the 149 page subject report and summary is there a literature review of studies addressing potential economic issues that are specific to Wal-Mart developments. Although a preponderance of the literature on job, wage and other economic impacts associated with Wal-Mart developments have been prepared by advocates for one side or the other of a Wal-Mart development and suffer from methodological flaws, biased assumptions and/or poor quality or unavailable source data, there are many valid studies that could have been used to inform and adjust model

² See, for one of several instances, page 13, paragraph 3, of subject report.

inputs.³ The findings of many of these studies call into question the use of critical default model “averages,” and should have been considered in preparing model inputs and related assumptions.

The most understandable omission, and most relevant independent study, was released by the highly respected National Bureau of Economic Research (NBER) in November of 2005, one month *after* the EPR Act 250 report was issued, entitled, *“The Effects of Wal-Mart on Local Labor Markets.”* This study, by Neumark, Zhang and Ciccarella,⁴ is probably the most extensive impartial analysis of the economic and employment impacts associated with the introduction of Wal-Mart stores in the U.S. performed to date.

The study focuses primarily on county-level employment and earnings impacts associated with Wal-Mart developments throughout the U.S. It uses an extraordinarily rich dataset, provided in large part by Wal-Mart, and viewed impacts over a long time horizon. The study found that:

“In the retail sector, the representative Wal-Mart presence (about 8 years) reduces employment by two to four percent. There is some evidence that payrolls per worker also decline, by about 3.5 percent, but this conclusion is less robust. Either way, though, retail earnings fall. Looking at total employment, some of the evidence points to employment increases, although the regional evidence for the South and perhaps the Midwest points to employment declines. At the same time, there is stronger evidence that total payrolls per worker and per person decline, by about two and five percent respectively, implying that residents of a local labor market do indeed earn less following the opening of Wal-Mart stores. Finally, we find clear evidence of adverse effects of Wal-Mart stores on retail employment, total employment and total payrolls per person in the South, where Wal-Mart stores are most numerous on a total and per capita basis, and where they have been open the longest.”

The reasons that Wal-Mart-specific analyses, such as the above, differ from “average” model output from sources such as REMI, is that Wal-Mart is anything but an “average” retail operation. Wal-Mart wages and benefits are lower than “average,” the economic multipliers for retail trade are significantly lower than “average,” and the prices offered to consumers are much lower than “average.” These differences should be accounted for in any model used to measure impacts. In the model used for this Act 250 analysis, there was no such adjustment or model calibration.

³ See, for examples, Emek Basker, 2003, *Job Creation or Destruction? Labor-Market Effects of Wal-Mart Expansion*, University of Missouri; Stephan Goetz and Hema Swaminathan, 2004, *Wal-Mart and County-Wide Poverty*, Department of Agricultural Economics and Rural Sociology, Pennsylvania State University; and Kenneth Stone, 1995, *Impact of Wal-Mart Stores on Iowa Communities, 1983-93*, (and subsequent update in 1997), *Economic Development Review*, 13(2), 60-9.

⁴ David Neumark is a Senior Fellow at the Public Policy Institute of California (PPIC) and Professor of Economics at the University of California, a Research Associate at the NBER. Junfu Zhang is a Research Fellow at PPIC. Stephen Ciccarella is a Research Associate at PPIC.

Net regional employment declines are consistent with Wal-Mart developments because Wal-Mart is a much more efficient retailer than smaller local retailers. This is one of the reasons Wal-Mart prices are lower than most competitors and one of the reasons Wal-Mart routinely drives small local retailers out of business. As local retailers are displaced by Wal-Mart, sales per employee in the region will rise. Because regional retail sales are not significantly expanded by the presence of a Wal-Mart, total employment and retail employment, in particular, can decline.

Another reason some net regional economic effects from a Wal-Mart development can be negative, is that the economic multipliers associated with local retail trade are much greater than those associated with national chains and Wal-Mart, in particular. The multiplier effect of local retail business expenditures on accounting, distribution, wholesaling and legal expenses, for example, are virtually all captured within the State, if not the immediate town or region, whereas these same expenditures for Wal-Mart are virtually all out-of-region and out-of-State. Proprietor income and profits are also largely captured in-State and in-region for local retailers, while most of this is exported out-of-State in the case of Wal-Mart and other national chain stores.

Lower consumer prices and increased purchasing power are the primary economic benefits from Wal-Mart, but may not offset regional earnings and employment declines, or increased public taxpayer burdens. There can be no question, however, that the net economic and fiscal impacts of the proposed Wal-Mart will be decidedly negative to the City of St Albans.

If model inputs specific to Wal-Mart were developed and used in the subject report, it is likely there would be:

- No net employment gain in the region, instead of the estimated increase of 66 net new jobs,
- A small net decline in retail employment in Franklin County, instead of a net gain of 137 jobs,
- Correspondingly greater competitive retail employment losses in nearby retailing centers within Franklin County, especially St Albans City, possibly in the range of 200 to 400 jobs or more, if secondary impacts were completely included,
- Significantly greater negative fiscal impacts on municipalities affected by competitive job loss, especially St Albans City,
- Lower net personal income, gross regional product, and related economic effects in the region,
- Higher State transfer payments and public assistance expenditures, due to lower per capita payrolls and reduced private sector benefits, and,

- Lower or no significant net population impacts within the County or region.

Because the core model output is seriously biased, all downstream analysis based on this output suffers from the same bias. In some cases, it will not affect the conclusions drawn – particularly those concerned with excessive net growth - however, for those impacted by job losses and related competitive economic impacts, the study conclusions cannot be considered a reasonable or valid estimate of likely economic and fiscal impacts.

2) *The use of an aggregate six county model, especially given the counties involved, is not optimal and places undue reliance on distribution algorithms for country level impacts.* It would have been preferable and consistent with “best practices” to use either a model with six individual counties, or a four county model consisting of the highest impact counties, with individual county and “balance of state” detail available. Even a one county model consisting of Franklin County and a balance of state region would have been preferable. Any of the above configurations would have enabled more accurate placement of investment and trade flows between the primary impact county (Franklin) and surrounding counties.

The many distribution algorithms used in the subject report to allocate the regional impacts are also lacking in transparency and require further disclosure in order to fully evaluate their reasonableness. In many instances the final report output does not meet this standard.

3) *The definition of secondary impacts is excessively narrow, and the methodology used to estimate these impacts minimizes the potential negative effects of such additional competitive retail development on the City of St Albans.*

While it can be difficult to conclusively identify related secondary development activity, the standard used in the subject report excludes a great deal of the likely development that will occur as a result of and in close proximity to the proposed Wal-Mart development. For example, we understand that a substantial Lowes building materials store, a smaller (50,000 square foot) farm and tractor store and at least one restaurant have already been proposed in the vicinity as a result of the planned Wal-Mart opening, but most of these have been excluded from the EPR analysis.

Secondary impacts such as these are a regular feature of Wal-Mart developments and are stimulated by, and reliant upon, the huge traffic flows that Wal-Mart creates. The presence of such planned and future tangential development will further negatively impact competitive local retailers, especially in the City of St Albans, expanding the range of affected merchandise, automotive, food and professional service

establishments. The secondary growth impacts could eventually even exceed those directly connected with direct competition to Wal-Mart.

4) *The retail trade model used to estimate retail “demand,” “supply” and “leakage” appears to be fraught with theoretical and data errors and cannot be considered a reliable basis for estimating likely retail trade flows within the region or County, or potential economic and fiscal losses within the City of St Albans as a result of the development of the proposed Wal-Mart store.* Additional data disclosure showing all data inputs used to derive and distribute the basic demand and supply concepts is necessary to fully evaluate this approach, but the net effects presented in the report are not consistent with either economic theory or likely county or sub-county impacts based on a review of the effects of other Wal-Mart retail developments.

For example, the methodology assumes that imbalances in estimated demand and sales (and we question the extent to which demand or supply can be accurately measured within the tolerances of the stated output at this level of geographic detail) represent an opportunity for additional retail sales in a region that will not cannibalize existing retail stores. This assumes that Wal-Mart and related secondary developments have some fixed upper limit on their sales capacities. If they are truly competitive with another retailer, they will not just absorb the demand that is considered “excess,” they will absorb all the demand that may be competitively vulnerable in a locale. This has been the empirically observed pattern in other Wal-Mart developments and is likely in Franklin County.

As an example of a potentially critical data and conceptual omission, Journey to Work data from the Census Bureau show that nearly a third of all Franklin County residents commute to jobs in Chittenden County⁵ versus about 1% of Chittenden County residents commuting to Franklin County. Although it is likely that some sales loss will occur at Chittenden County retailing operations as a result of the proposed St Albans Town Wal-Mart, it is also likely that Franklin County residents who commute to Chittenden County for work will continue to shop in Chittenden County, at the Wal-Mart in Williston and elsewhere.

Given the vast shopping opportunities in Chittenden County, we believe the stated result that almost 25% of all sales from the proposed St Albans Town Wal-Mart will come from Chittenden County⁶ is unlikely. This calls into question the methodological basis of these calculations and requires more complete disclosure and review of additional source data detail to confirm the reasonableness of this approach.

Based on case studies of other Wal-Mart stores, we believe the vast majority of the sales in the proposed store will be drawn from Franklin

⁵ See: <http://www.census.gov/population/www/cen2000/commuting.html#VT>

⁶ See subject report, page 34, Table 10

County and most will be competitive with existing retailers in Franklin County - and especially St Albans City.

Detailed studies in the State of Iowa (Stone, 1988, 1993 and 1997) have shown that "some small towns lose up to 47% of their retail trade after 10 years of Wal-Mart stores nearby."⁷ The most recent of these studies show that competitive sales losses in nearby retail centers persist and increase over the entire 10 year time horizon of the study for many merchandise categories and that sales declines are most severe in small rural areas, exceeding 60%.

A compilation of potentially affected businesses in St Albans City, prepared by Town officials and attached as Appendix A, shows more than 45 downtown businesses with municipal tax revenues totaling nearly \$300,000 that could be seriously affected by a competitive Wal-Mart presence. An additional 21 stores representing City tax revenues of about \$84,000 will also be vulnerable to secondary development and any expansion of stated Wal-Mart departments in the proposed store (such as beauty and hairdressing services). These businesses represent about 20%-30% of the total St Albans downtown district tax base.

If all or some of the high impact businesses were to close, and we regard this as likely, there could be reverberations that affect virtually all downtown businesses, as traffic decreases, vacancies rise, rents decline and real estate values slow or decline. The same economic multiplier effects that work to magnify the positive effects of economic growth also work in reverse during a regional decline such as this. Although there are important offsets in St Albans City that may mitigate the negative effects to some extent (primarily steady and growing office employment in the downtown area), the competitive effects from the proposed Wal-Mart could be a significant blow to the City's efforts to create and expand a revitalized historic downtown district.

In addition to private sector losses and reduced municipal tax revenues, the return on recent public sector investment in downtown St Albans is also at risk. As illustrated in Appendix B, more than \$7 million in federal, state, and local government investments have been made in support of preserving and expanding this unique downtown district. The public interest in this investment is substantial and could be largely negated by shuttered businesses and competitive loss resulting from the proposed Wal-Mart development and related secondary impacts.

Critical data discrepancies, such as the Grand List values presented for St Albans City (and other jurisdictions) also need to be reconciled before the subject analysis can be considered reliable. The data presented on page 99, Table 34, of the EPR report, for example, do not comport with either State Tax Department or City of St Albans data.

⁷ Kenneth Stone, 1997, *Impact of the Wal-Mart Phenomenon on Rural Communities*, Published in Farm Foundation Proceedings, *Increasing Understanding of Public Problems and Policies - 1997*, University of Iowa

Summary and Observations

Given the emergence of new empirical data relevant to the subject analysis that was not available at the time of the initial analysis, we recommend the District Commission request a revised analysis be performed using this information to calibrate model inputs and define “likely” or (preferably) “conservative” estimates of economic and fiscal impacts. Given the complexity of the subject report, we would also recommend a more extensive technical exchange of data and methodologies with economists from other interested parties so as to fully understand and test all distribution algorithms, non-confidential data sources and assumption sensitivity ranges.

It is clear that the proposed Wal-Mart development will have a major impact on retailers in the City of St Albans. The initial 160,000 square foot store and likely secondary development – some of which is already in the planning stage – will create a new regional retailing center that will rival any in the County. It will draw significant sales, profits and retail traffic from the downtown district to the new area, affecting downtown real estate values and municipal tax revenues.

Wal-Mart is not “just another big box retailer.” As the second largest company in the world⁸ and a competitor without rival in its field, it has clearly demonstrated the devastating impacts it can have on local retailers in neighboring communities. The City of St Albans has worked hard and invested millions of dollars in public funds to create a vibrant and extraordinary downtown district. The economic threat to viability this district from the proposed development should not be underestimated.

⁸ Only eclipsed this year by Exxon/Mobil, due to extraordinary oil revenue increases. In 2005, Wal-Mart was the world's largest private sector company.