



# THE WEALTH OF CITIES

Pursuing Economic Freedom  
Closer to Home





Asked to name mankind's greatest invention, some might point to early innovations like the wheel or the plow. Others might make the case for more modern technologies, such as electricity, the internal combustion engine or computers and the Internet. An intriguing answer comes from Edward Glaeser—the city. Hear him out. Cities are our greatest invention, the Harvard professor says, because proximity, density and closeness produce an environment where human creativity and cooperation flourish. New ideas emerge, percolate, mutate and spread. Old ideas fall into the dustbin of history. Most of humanity's progress has sprung from the perpetual churning of ideas and enterprises that takes place in the urban milieu. On a day-to-day basis, city life at street level can be noisy, crowded, frustrating and at times downright intimidating. It makes Glaeser's celebration of cities seem idealistic. Yet, the grand sweep of history reveals an inexorable migration to cities, accompanied by advancements in technology, culture and living standards—a progression that has been speeding up in recent decades. Today's cities share a lineage that goes back to ancient times, when our ancestors massed and intermingled in such places as Babylon in the Mideast, Athens and Rome in the Mediterranean, Teotihuacán in Mexico, Delhi in India, Xian in China. London, Amsterdam and Venice arose as key centers of commerce in medieval Europe. These cities were the glory of their times, but urbanization didn't really pick up steam until the Industrial

Revolution provided greater rewards for leaving farms to take jobs in factories. As wave after wave of people arrived, cities and the nations that surrounded them became wealthier.

The United States industrialized ahead of the rest of the world, giving Americans an early start on the march from the countryside to cities. The sun set on the U.S. industrial era decades ago, but urbanization has continued apace as the economy shifted toward knowledge-based industries and services. Now, nearly 80 percent of Americans live in cities, and they're increasingly concentrated in the biggest metropolitan areas (*see Exhibit 1, page 4*).

Taken together, the country's city-dwellers are very productive. The 25 largest U.S. metropolitan areas, home to 40 percent of the population, account for more than half of U.S. economic activity. Urban areas' contribution rises to nearly 65 percent for the top 50 cities and almost 75 percent for the top 100. On a per-person basis, city workers churn out significantly more goods and services than rural residents (*see Exhibit 2, page 5*). The implication is clear: cities are the engine of America's

economy, and the nation's prosperity will depend on cities as dynamic centers of economic growth.

Looking around the country, we see huge gaps in major metropolitan areas' economic fortunes—every booming Dallas-Fort Worth is offset by a sclerotic Detroit. In *The Wealth of Nations*, published in 1776, Scottish economist Adam Smith

Metropolitan Statistical Area (MSA) on a spectrum between 0 for lowest economic freedom and 10 for highest economic freedom (*see Box 1, page 6*).

MSAs that score highly on the index will tend to have relatively low taxes, smaller government spending and public employment, less dependence on government transfers, pay rates largely driven by market forces, and below-average union membership. In short, these cities give markets more breathing space, letting businesses and individuals make the decisions that shape local economic activity. MSAs with low economic freedom scores will generally have higher taxes and greater government meddling in local economic affairs.

Stansel's scores reveal the large gaps in economic freedom among U.S. metropolitan areas—from a high of 8.52 in Naples, Fla., to a low of 3.32 in El Centro, Calif. Wide disparities exist even within states—proof that local policies do matter. For example, Tyler in northeast Texas ranks as the nation's 13<sup>th</sup> most economically free city, while Laredo in South Texas comes in at No. 299.

Seventeen of the 20 most free MSAs are in states with no income tax—Florida, New Hampshire, South Dakota, Tennessee and Texas. Fifteen of the least-free MSAs are in California

Among the 30 largest MSAs, the top five places for economic freedom are in Texas and Florida, two states celebrated for keeping taxes low (*see Exhibit 3, page 7*). The Tampa-St. Petersburg area on Florida's Gulf Coast ranks first in economic freedom, joined by Miami at No. 4 and Orlando at No. 5.

The two other Top 5 MSAs are in Texas, with Houston ranking second and the Dallas-Fort Worth area following right behind at No. 3. San Antonio comes in just a few notches later at No. 8. The strong showing isn't all that surprising because Texas leads in state-level economic freedom in the latest









to variances of living costs. MSAs with greater economic freedom impose fewer impediments to new housing, so supply increases blunt upward pressure on prices. The same applies to other markets—less government meddling and greater competition help keep prices low.

The combination of low taxes and living costs makes paychecks go further. Wage rates are often quite high in places with low economic freedom, such as New York and Los Angeles. After adjusting for differences in taxes and living costs, however, average hourly wages are nearly \$16 in the 40 percent of MSAs with the highest economic freedom (*chart 5*). Adjusted pay in the least-free group falls to \$12.40.

The less-constrained capitalism of the freest cities doesn't widen the gap between rich and poor. Income inequality, measured by wage dispersion, is lowest for the middle 20 percent, but the most-free group exhibits significantly less inequality than the least-free one (*chart 6*).

What's going on? Equality may increase as lower living costs attract middle-class families to MSAs with high

economic freedom. In the least-free MSAs, inequality may increase as the middle class leaves, poor households stay put because of generous public assistance, and wealthy families hang on because they think the good life in their city is worth the high taxes and other burdens.

Pursuing economic freedom closer to home, Americans stand to gain faster economic growth, rapid job creation,

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to 2011, we find that Atlanta, one of the Top 10 freest MSAs, led all major metropolitan areas with cumulative net in-migration totaling nearly 1.7 million—a gain equivalent to hauling the entire Nashville metropolitan area down into North Georgia over two decades (see Exhibit 5).

Other big MSAs with Top 10 economic freedom scores had high levels of net in-migration. Phoenix added 1.4 million newcomers. The Dallas-Fort Worth area welcomed more than 1.1 million. Tampa, Houston and Orlando had healthy gains. Relatively unfree Riverside

confounds as the only anomaly, but many of its newcomers probably arrived from nearby Los Angeles.

Turning to out-migration, two economic freedom-challenged MSAs stand out—Los Angeles and New York. Between 1992 and 2011, both endured cumulative net losses of around 4.1 million residents—more than enough people to fill the Seattle metropolitan area. Chicago had net out-migration of nearly 1.3 million.

The correlation between economic freedom and net migration becomes clearer when we broaden the inquiry to the 100 largest MSAs. The most-free

20 percent attracted nearly 9 million new residents, while the loss for the least-free group totaled more than 7.1 million (The correlation

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*Box 2, pages 12-13*). The most logical answer—the toll of high taxes and other interventions—has important implications for economic freedom in America’s MSAs.

The migration data suggest that Americans are moving toward economic freedom and its benefits—the direct ones like lower taxes and the indirect ones like faster job growth. These findings should alert us to the folly of traditional dogmas that have saddled so many cities with high taxes and kept their citizens under the thumb of City Halls that think they know best.

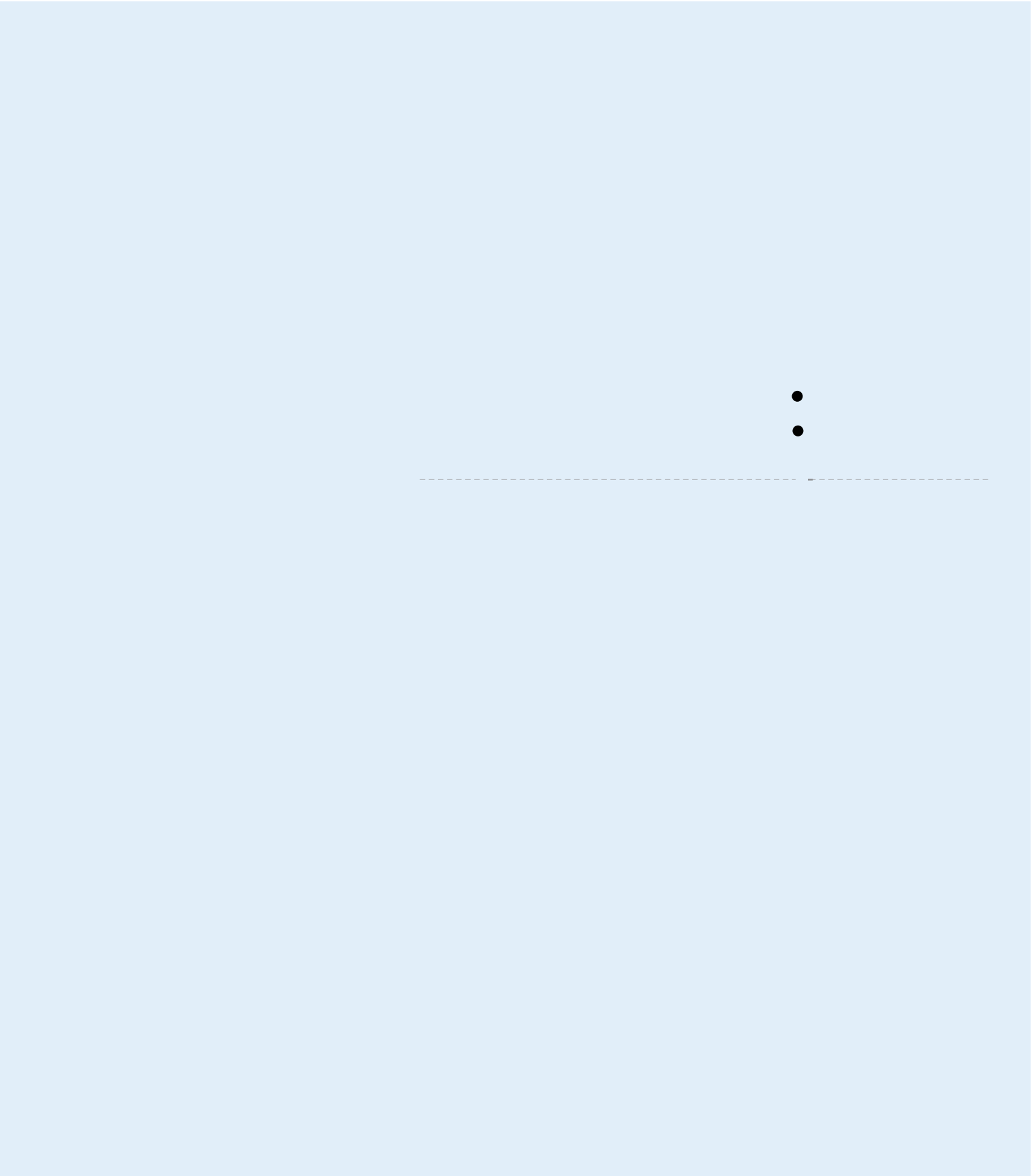
Stansel developed the MSA index only a few years ago, and it doesn’t have enough data to assess whether economic freedom has been gaining or losing ground in America’s cities. A look at policies around the country, however, suggests that local governments routinely use their powers to abrogate their citizens’ economic freedom.

Taxes are probably the most common way cities erode economic freedom. Local authorities tax property, retail sales, utility payments and, in some jurisdictions, income. According to the Tax Foundation, local tax burdens have been rising—from 4 percent in the 1950s to nearly 7 percent today. Taxes beget spending—as sure as night follows day. The Tax Foundation reports that local governments’ per capita spending rose from 6 percent of GDP in the 1950s to more than 10 percent in this decade.

Higher government spending means that more resources will be allocated by political rather than market processes.

New York, NY  
Los Angeles, CA  
Chicago, IL  
Boston, MA  
Miami, FL  
San Francisco, CA  
Philadelphia, PA  
Dallas, TX  
Seattle, WA  
Washington, DC  
Pittsburgh, PA  
Houston, TX  
Minneapolis, MN

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permits and inspections. At its worst, food—no trans fats! this regulatory activism raises costs, Most cities dictate who can drive subverts real estate values and sti esa cab or operate a hotel. These development. restrictions are common, and few

Local governments trifle with people paid much attention to them property rights, invoking the power until new technologies upset the of eminent domain to seize private status quo. Uber, which turns private property, sometimes for legitimate cars into taxis, and Airbnb, which public purposes and sometimes for the turns private homes into hotels, used bene t of real-estate developers and the the Internet to create new markets owners of professional sports teams. where buyers and sellers could nd

Economic freedom rests on businesses each other and set prices outside the and their customers deciding the prices, existing regulatory structure. Some products and service quality that suits cities welcomed the new businesses; them. In many parts of the country, others responded by trying to regulate cities haven't been shy about replacing or even outlaw them.

the diversity of the marketplace with A growing number of city the conformity of government control. governments refuse to let market Rent controls prescribe how much forces determine pay scales for low- landlords can charge their tenants for skilled workers, moving the forefront apartments. In recent years, hundreds of efforts to raise minimum wages of cities decided shoppers shouldn't be above the federally mandated \$7.25 able to carry their groceries home in an hour. Over the next few years, free plastic bags. New York City tells minimums will rise to \$15 an hour in its restaurants how to prepare their San Francisco, Los Angeles and Seattle,



Many Americans fuss about government's burden on the economy, but many other parts of the world suffer far worse afflictions from taxes, regulation, corruption, insecurity and poor governance. For some countries in Asia, the Middle East, Latin America and Africa, the

# News and Data Science

Page 2:

Edward Glaeser, Triumph of the City:

How Our Greatest Invention Made

Us Rich,

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# 2014-15: Year in Review

*Editor's note: The O'Neil Center is switching its annual report from a calendar year to the SMU academic year, which runs from June 1 through May 31. To avoid a gap, this report also reviews events from January to May of 2014.*

As the 2014-15 academic year came to a close, SMU Cox Dean Al Niemi announced that Robert Lawson would become the new director of the William J. O'Neil Center for Global Markets and Freedom. Lawson, who joined the O'Neil Center in 2012, replaced founding director W. Michael Cox, who will continue as an integral part of the O'Neil Center as he returns to his research and teaching.

"The O'Neil Center's mission will not change," Lawson said. "Our programs will evolve, and we'll be doing some new things, but our focus will remain on research and teaching, looking at why some economies prosper and others don't." (*For more, see the conversation on Page 18.*)

The 18 months covered in this review saw several highlights—an annual report essay looking at economic freedom as a form of capital, a conference focused on migration as a path to a better life, an update on the *Economic Freedom of the World (EFW)* report and a PBS documentary built of the EFW work of Lawson and his colleagues (*For more on the movie, see inside back cover.*)

The center received a vote of confidence in the form of significant new financial support from a number of donors—the O'Neil family, the Charles G. Koch Charitable Foundation, the Dallas-based William E. Armentrout

Foundation and Fort Worth businessman W. Grady Rosier.

In January 2014, the center added research associate Ryan Murphy, who earned his doctorate in economics at Boston's Suffolk University in 2013. Murphy will work with Lawson on measuring economic freedom. In addition to Lawson, Cox and Murphy, the O'Neil Center staff at the end of the 2014-15 academic year included Dean Niemi, professor Michael Davis and writer in residence Richard Alm.

After four decades as a leading free-market scholar, Dwight R. Lee retired in May 2014. In another departure, Youth Initiative manager Kathryn Shelton gave birth to her first child, a girl, in July 2014 and left the center.

Lee was the center's first hire in 2008. In retirement, he will continue his affiliation with the O'Neil Center as scholar in residence. He will use his O'Neil Center affiliation in his writings and other professional activities.

About three dozen colleagues and collaborators from across the country gathered at SMU to honor Lee's contributions to the profession. Richard McKenzie, a long-time collaborator, compiled a booklet of Dwightisms—Lee's oddly logical and self-deprecating pronouncements. One example: "Speaking of opportunity cost, mine is so low that my economic rent from my job is greater than my salary."

In early 2014, the O'Neil Center published its fifth annual report,

highlighted by the essay "Living Above Our Means," written by Cox and Alm. It takes an innovative look at economic freedom, seeing it as a form of capital stock that takes a long time to build and depreciates if not properly maintained.

The essay finds economic freedom essential to building each nation's capital stock, which in turn becomes a key factor in the gap between rich and poor countries. About 90 countries are living below their means and can look forward to rising consumption in the future. With its recent declines in economic freedom, the United States is one of just four countries living above their means. They can expect to face difficulties in maintaining current levels of consumption.

In September 2014, Lawson and his co-authors released the latest



With a grant from Capital One,  
the O'Neil Center started a reading

skew immigration toward highly productive workers. The visa price would vary with economic conditions, rising in good times when a lot of foreigners see opportunity and falling in hard times. Add in a humanitarian and refugee allotment, and the system would admit 1.5 million immigrants a year, considerably higher than existing limits.

“The U.S. Treasury would receive \$20 billion in new revenue,” Vedder said. “An idea that would make expanding immigration more popular with the American people would be to dedicate these revenues to reducing individual income taxes.”

in 2013, which died in the House of Representatives under the intense heat of populist pressures.

Nowrasteh urged positive messages that support greater immigration—inspiring stories of newcomers’ achievements, appeals to traditional American values. “When immigration is in the news, it’s almost always for bad reasons. It’s always when it’s a crisis, when it’s a problem,” he said. “It’s almost never in the news when it’s a good thing.”

Immigration brings great benefits to the economy, Vedder said, but current policies keep hundreds of thousands, maybe even millions, of potential newcomers out of the country. As an alternative to the status quo, he proposed using market forces to determine which foreigners get a legal right to live in this country.

The centerpiece of the proposal would be a daily on-line auction of 5,000 visas for work in the United States, with a hefty price that would

Within the United States, Ashby’s research identified several key aspects of economic freedom that attract migrants—lower top marginal tax rates, less restrictive minimum wages, relatively low government employment and less union power. For migration among countries, Ashby found a 1 percent gain in economic freedom associated with a 0.41 to 0.53 percent increase in immigration rates. “Economic freedom matters, and it matters considerably, even when I controlled for income,”

Ashby said. “People cared about economic freedom. Suburban people care about it—middle class people care about it—people who are not rich care about it.”

low-skill jobs that entail manual labor on days with temperatures as high as 110 degrees.

Landmark Nurseries draws mostly from a pool of workers from Mexico and El Salvador, and complying with the immigration laws is a burden. "I go to great extremes to make sure we have legal employees, and I have to look at all kinds of documents," Prewitt said.

Sponsors contributed nearly \$50,000 to the conference, led by AdvoCare, the presenting sponsor, and Richard Weekley, Cary Maguire and Harriet and Warren Stephens. To allow continued access to the conference presentations, the O'Neil Center posted videos of all the speakers on its website.

In addition to the conference, the O'Neil Center enhanced intellectual diversity on the SMU campus by sponsoring speakers with iconoclastic points of view.

In February 2014, the O'Neil Center hosted Ladar Levison (SMU '03) founder of Lavabit LLC, the encrypted

email service company that Edward Snowden used after his disclosure of classified National Security Agency documents. Once Snowden's identity became public, a federal search warrant demanded that Lavabit disclose the private keys for all its users. Levison shut down operations shortly afterward to avoid compromising its users' privacy. Levison's talk directly confronted government overreach and privacy in the digital age.

In November, about 150 students and guests attended an O'Neil Center-sponsored debate on sweatshops. Benjamin Powell, director of Texas Tech's Free Market Institute, contended that low-

SMU presentations—one on how the Internet squeezes traditional middlemen by reducing transaction costs, and the other, titled “The Thing Itself: Riding the Unicorn Over a Cliff,” an analysis of the follies of leftist intellectuals and the government policies they advocate.

David Boaz, executive vice president at the Cato Institute, gave an invitation-only lunch speech for O’Neil Center supporters on libertarian principles, based on his book *The Libertarian Mind*, and a public talk about the failures and foibles of America’s long-running war on drugs.



As in years past, O’Neil Center scholars put their ideas on paper, charging into academic and public debates on a range of topics of import to economic freedom.

In early 2014, Cox and Alm were invited to join five other commentators to form *Investor’s Business Daily’s* Brain Trust. Each will write about six articles a year, which will receive premium front-page display in O’Neil Center founder Bill O’Neil’s newspaper.

The first Cox and Alm venture was “Money Won’t Revive Flat-Lining

Schools,” published in March. They followed up with a two-part op-ed that took on the nation’s income inequality by discussing what the rich do to benefit all Americans and the importance of incentives and education in lifting up the bottom of the income distribution. In September, Cox and Alm laid out the case for cutting U.S. corporate tax rates.

In 2014, Dallas-based *D CEO* magazine published four Cox and Alm chart-and-text articles focusing on the Texas economy. One showed that Dallas-Fort Worth and Houston had the strongest job growth among the 15 largest U.S. metropolitan areas. The others highlighted the low volatility in the Dallas housing market, the relatively high buying power of Texas wages and the Dallas area’s surprisingly low income inequality.

Cox and Alm started out 2015 with a one-pager in *D CEO* looking at Texas’ economic freedom as capital stock—a localized version of the annual report essay.

The magazine then gave Cox and Alm a battle-eld promotion of sorts, increasing their column to two pages. Their first expanded essay was titled “The Energy Enigma,” which debunked the idea that Texas’ prosperity requires

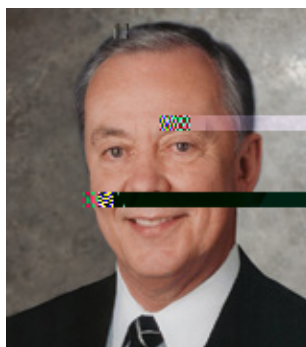
high oil prices. The state grew most rapidly in the 1990s, when oil prices were at a low ebb. Their second two-pager focused on the secret of Dallas-Fort Worth’s rapid job creation—labor market freedom.

In addition to co-authoring the 2014 edition of the *EFW* report, Lawson published two academic-journal articles: “Can Two Observations Confirm a Theory? A Comment on Max U versus Humanomics” in the *Journal of Institutional Economics* and “Does Immigration Impact Institutions?” in *Public Choice* (with J.R. Clark, Ryan Murphy, Alex Nowrasteh and Benjamin Powell).

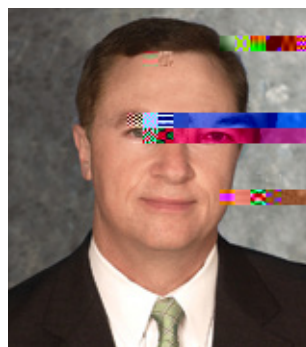
Early 2014 saw release of Lawson’s book (with Larisa Burakova) on the triumph of economic freedom in a former Soviet republic—



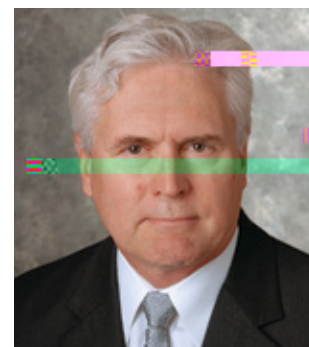
Robert Lawson, Director and Fullinwider Endowed Centennial Chair in Economic Freedom



Albert W. Niemi, Jr., Dean, SMU Cox School of Business



W. Michael Cox, Founding Director, William J. O’Neil Center for Global Markets and Freedom



Michael Davis, Senior Lecturer, SMU Cox School of Business



and *Entrepreneurship*.

In the 2014-15 academic year, Murphy wrote eight articles for scholarly publications. In addition to joining Lawson et. al. on “Does Immigration Impact Institutions?,” Murphy had “The Plucking Model, the Great Recession, and Austrian Business Cycle Theory” in the *Quarterly Journal of Austrian Economics* and “Nutritional Efficiency Wages and Unemployment: Where’s the Beef?” (with Benjamin Powell) in the *American Journal of Agricultural Economics*.

The rest of Murphy’s output: “Heterogeneous Moral Views in the Stateless Society” in *Libertarian Papers*, “The Impact of Economic Inequality on Economic Freedom” in the *Cato Journal*, “What Do Recent Trends in *Economic Freedom of the World* Really Tell Us?” in *Economic Affairs*, “Unconventional Con dence Bands in the Literature on the Government Spending Multiplier” in *Econ Journal Watch*, and “The Unconstrained Vision of Nassim Taleb” in *The Independent Review*.

Murphy’s non-academic publications included “Benefits to the Poor of Texas Franchise Tax Repeal,” published as a *National Center for Policy Analysis Policy Report* in June 2014, and “A

Rent-Seekers Tax?” in the summer 2014 issue of *Regulation* magazine.

Murphy also had an op-ed in the July 15, 2014, issue of the *Austin American-Statesman*, titled “Repealing Texas’ Franchise Tax.”

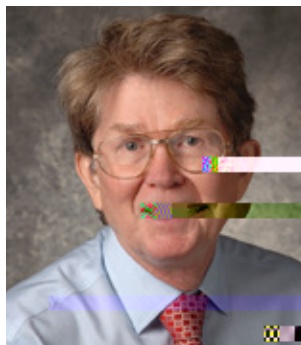
Lee wrote “The Two Moralities of Price Gouging” for *Regulation* magazine in spring 2014. Transitioning to scholar in residence, Lee remained productive. He published “Buchanan and Tullock Ignore their Own



Richard Alm, *Writer in Residence*,  
William J. O’Neil Center for  
Global Markets and Freedom



Ryan Murphy, *Research Associate*,  
William J. O’Neil Center for  
Global Markets and Freedom



Dwight R. Lee, *Scholar in Residence*,  
William J. O’Neil Center for  
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# Economic Freedom in Action: Changing Lives

The Economic Freedom of the World report, co-authored by the O'Neil Center's Robert Lawson, provided the intellectual basis for a PBS documentary that shows the benefits of economic freedom in human terms.

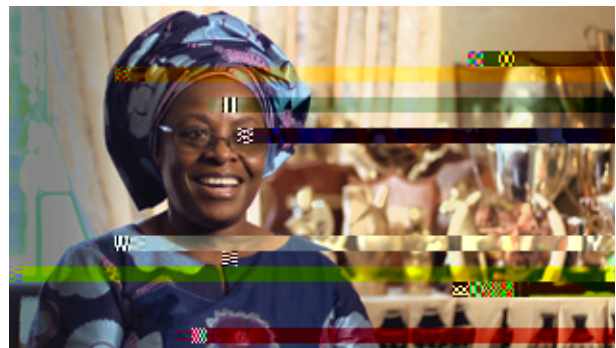
Produced by the Free to Choose Network, Economic Freedom in Action: Changing Lives tells the stories of entrepreneurs who are prospering in countries that made significant gains in economic freedom. The film, which aired on public television stations across the country in 2014-15, included on-camera interviews at the Fraser Institute in Canada with Lawson and Economic Freedom of the World co-authors James Gwartney and Josh Hall.

The O'Neil Center hosted showings of Economic Freedom in Action at SMU. In addition, we sponsored watch parties at more than 80 universities around the country, using a grant from the Charles G. Koch Charitable Foundation to provide copies of the film, posters, flyers, and food and beverage stipends.

Complete information on the documentary can be found at <http://www.changinglivesfilm.com>.



South Korea: Daesung Kim, refugee to venture capitalist



Zambia: Sylvia Banda, food services company founder



Slovakia: Katarina Rybarikova, Paul Frank-brand retailer



Chile: John Hernandez, building a bee-keeping business



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