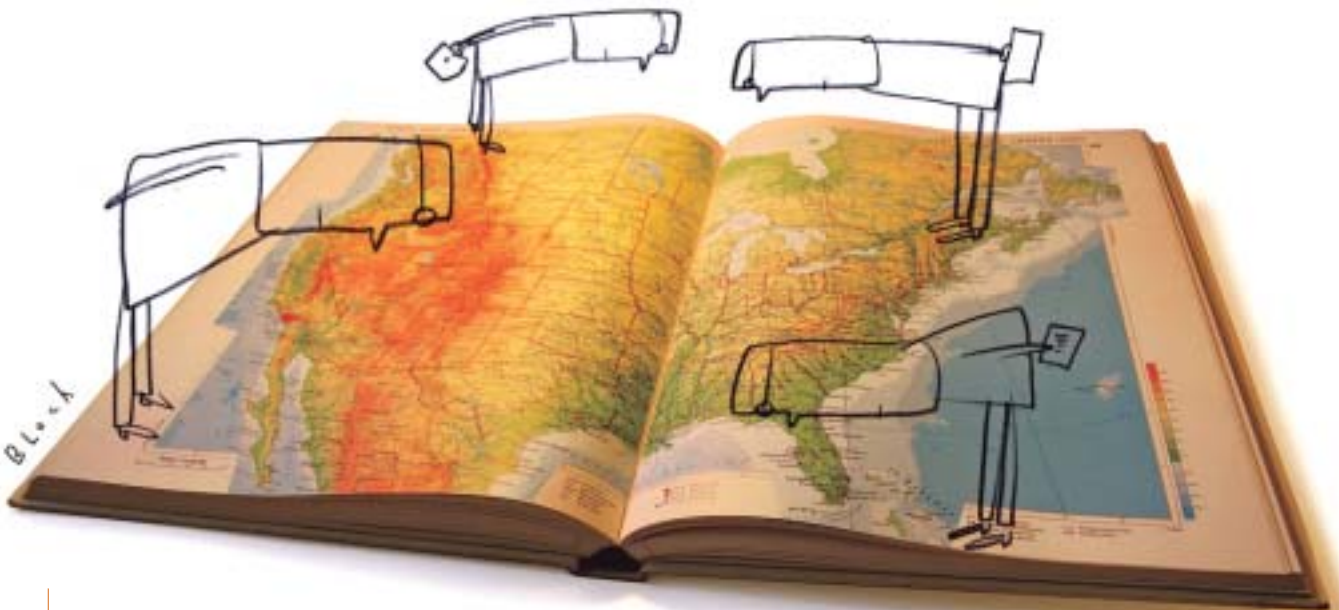


The Best Places

For Doing Business in America
2005



We examined
274 population centers,
looking for job creation
and other signs that
businesses are thriving.
Here's what we found:

BY JOEL KOTKIN
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The economies
of most big cities
are idling.
The real
entrepreneurial
hotbeds are
now on
the periphery—
where low costs
make it possible to
thrive in a tough
global economy.

the new economy didn't disappear. It changed addresses.

The dynamic, job-generating information-technology and service companies that characterized the boom of the 1990s are still around. But it's getting harder to find them in the usual high-tech clusters like Silicon Valley, Boston, and Austin. Instead, five years after the bubble burst and a year or so into an economic recovery, those same kinds of companies are thriving in places like Reno, Nev., Boise, Idaho, and Naples, Fla.—cities that were once mere specks on the new-economy map.

Thanks to lower housing and labor costs, more favorable regulatory environments, and, in some cases, lower taxes, these smaller cities are proving ideal places for doing business—especially in a globalized economy in which companies operate under relentless pressure to keep costs low and quality high. In many cases, it is precisely these low costs that allow U.S. companies to

successfully compete in industries that often seem all but ready to concede to India and other countries. Rather than sending business overseas, many companies are instead opting to contract with lower-cost domestic suppliers—a new wrinkle in the outsourcing trend known as home-shoring.

Take Boise. Nestled at the base of the Rocky Mountains, the city has long been known for its astonishing scenery and outdoor recreational opportunities. But in recent years, Boise has undergone a transformation. Since 2001, the number of information jobs in the area has jumped 5.9%. Professional business services jobs have grown 9.1%, and the financial services sector has grown more than 11.3%. By contrast, San Jose, in the heart of Silicon Valley, has experienced a 23% drop in information jobs, a 21.5% loss in business services jobs, and a 2.2% loss in financial services positions over the same period.

Boise's surge is being fueled by com-



Weighing the Odds
Aki Korhonen was ready to move on. Would his staff cross the border with him?



#1

[REPORT FROM RENO]

A Californian Rolls the Dice

FIFTEEN YEARS AGO, Aki Korhonen moved from Finland to California, where the wide-open entrepreneurial climate was suitable for a man with dreams. He founded a successful company in the Bay area, a diagnostic software maker called PC-Doctor.

Soon enough Korhonen was dreaming again—of a place where everything didn't cost so damn much. So in 2003 he left, taking PC-Doctor 231 miles northeast on I-80 to a new entrepreneurial home in Reno, Nev.

Korhonen started PC-Doctor in 1993, and by 1999 the company's 40 employees occupied a 7,000-square-foot office in Emeryville, looking out onto San Francisco Bay. But Korhonen was already itching to get out. He added up the pluses: Nevada's lack of personal and corporate income tax, its lower utility and workers' comp costs, the ability to make PC-Doctor a high-paying local company by simply maintaining the salaries he'd been paying. "There wasn't one main reason," Korhonen says, "but adding up all the little ones together, Reno was the hands-down obvious choice for us."

At the same time, asking a diverse, multicultural work force to up and move could have gutted PC-Doctor, and Korhonen was determined to retain as many employees as possible. Enter the Economic Development Authority of Western Nevada, or EDAWN, an aggressive nonprofit business recruitment group. EDAWN surveyed the needs of PC-Doctor's employees and then brought in six community leaders to answer their questions. General issues of real estate, education, recreation, and job opportunities for spouses were raised, and so were more specific concerns, including those of the gay parents who were concerned about tolerance for their child. "It was a tough sell," says Chuck Alvey, president of EDAWN, "but you could hear the group's collective sigh of relief when we explained the influence of the creative class in our school system."

More than half of the PC-Doctor work force moved to Reno. The company has since added 40 new employees, bringing the head count to 64, and workers of all vintages are putting down roots. "Every month we have an employee buying a house," says Korhonen.

Granted, his is the enthusiasm of the transplant—the average cost of a new three-bedroom house in Reno is still \$307,000, almost 15% above the national average. But in San Francisco that house would cost \$869,000. "To be honest, I didn't expect the relocation to be this positive," Korhonen says. "People are rushed and stressed in California. Reno has a much better atmosphere."

—Patrick J. Sauer

panies like Treetop Technologies, a software services firm that has added 83 jobs over the past two years and now has 110 employees and offices in nine states, Calgary, and Singapore. Clients such as Hewlett-Packard, Agilent, and the state of Idaho rely on Treetop to provide application support, development, and administration—the very services that many fret are destined to leave the U.S. for India. Treetop's revenue hit \$10 million in 2004.

Founder and CEO Jason Crawforth, a 35-year-old Boise native, says he couldn't have done it anywhere else. Housing prices in Boise can be as much as 75% lower than in the San Francisco Bay area, according to the National Association of Realtors. That makes it easier to attract talented employees while paying some 30% less than in Silicon Valley. A software-testing engineer earning \$65,000 a year at Treetop, for example, would command a salary of at least \$85,000 in the Bay area, according to Crawforth. "People here are competent, speak well, tend to be patient, and have a good attitude," Crawforth says. "I have almost no turnover and people love the opportunity to be here. That's what makes this such a great place to do home-shoring."

Entrepreneurs like Crawforth helped propel Boise to the No. 2 spot in *Inc.*'s annual ranking of the best places for doing business in America. And it's not just Boise. Nearly all of the areas ranking high on our list are making use of the same formula. They're using their lower business and housing costs to attract entrepreneurs and stimulate strong growth in IT, business services, and finance—creating a new new economy in the shadow of the old one.

How did *Inc.* arrive at the 2005 rankings? We didn't try to quantify subjective criteria such as good weather and proximity to research universities. Our assumption is that job growth is the best measure of a region's economic vitality—especially as it applies to entrepre-

neurs. So we looked for jobs. If, as in the classic Small Business Administration formulation, small businesses produce up to 80% of the new jobs in this country, a region showing strong job growth is bound to be a hotbed of entrepreneurial activity. What's more, strong job growth suggests that a region's economy is expanding. That means new demand and new opportunities.

Inc. measured current-year employ-

ment growth in 274 metropolitan statistical areas, as defined by the Bureau of Labor Statistics. (Most of the MSAs bear the name of a single city, but all MSAs include areas surrounding the namesake city.) We also looked at average annual job growth over the past three years and compared job growth in the first and second halves of a period comprising the past 10 years. Job-growth factors account for about two-



Say Uncle Increasingly, defense spending stays close to the capital. And so Pete Howton does the same.



[REPORT FROM VIRGINIA]

This Sector Is Secured

GEORGE BUSH RECEIVED less than one out of every 10 votes in the nation's capital, and also lost most of the surrounding suburban counties, but he has proved very, very good for the Washington region. At a time when other

big East Coast cities have been idling, the D.C. region has been racking up some of the most impressive growth numbers in the country.

Led by northern Virginia, No. 11 on our list, the region's economy has become so strong that even long-troubled Washington, D.C., has a respectable No. 28 ranking, far above almost all other major eastern cities. The key to this rise, suggests George Mason University economist Stephen Fuller, lies in the remarkable ramp-up of spending for both defense and homeland security.

Between 2001 and 2003, federal procurement in the region jumped to more than \$42 billion from \$31 billion. Nearly all the increase, Fuller says, is attributable to defense and homeland security spending. Today the Washington area receives more procurement dollars than the entire state of California. This massive transfusion of debt-financed money helped the local economy recover from the aftermath of the dot-com collapse. The IT sectors of San Jose, Boston, and San Francisco are still in a deep swoon, but the Washington area has recovered virtually all its industry employment.

The rise of government spending has done much to stimulate entrepreneurial development. As Fuller points out, much of the expansion in government programs takes place among the so-called "Beltway bandits," companies that contract out with the federal leviathan. The expansion of defense and homeland security spending has been a godsend for these firms. Many of them are headed by and staffed with people coming directly from the armed forces, the CIA, and the FBI, and they come complete with the security clearances that are required for so much of the work.

Harry "Pete" Howton, a Naval Academy grad and founder of Virginia's Gray Hawk Systems, which stood 184 on last year's Inc. 500 list, doubts he could staff his 500-person firm, now growing by 15 to 20 people per month, in any other part of the country. Ninety-five percent of Gray Hawk employees have security clearances. "You have a labor force here you can't get anywhere else," Howton says. "You are working with a lot of guys from the service who know each other and like each other. You draw on people's friends."

Some of those friends, Howton adds, are still inside the bureaucracies that hand out the big contracts—another advantage to staying in the D.C. area. Proximity still matters in the procurement world. Alexandria, where Gray Hawk is based, is a quick hop from the Pentagon, just across the river from the Capitol, and a 30-minute drive from CIA headquarters in Langley, Va. —J.K.

#11

thirds of each city's final score; the balance among industries accounts for the remainder. (For a more detailed explanation of our methodology, see "How the Rankings Were Calculated," page 104. The rankings themselves begin on page 107.)

Scanning the list, it's hard not to conclude that the dominance of the nation's coastal urban centers is a thing of the past. San Francisco comes in at No. 188,

Boston at No. 203, and San Jose at No. 254. But that's not exactly fair. For one thing, many of the smaller regions at the top of the list have correspondingly smaller economies. Just as it's easier for fast-growing start-ups to post bigger percentage jumps in revenue than larger, more established corporations, smaller cities also have an easier time racking up impressive increases in employment growth rates. And not all big cities are

suffering. San Diego (No. 22) and Milwaukee (No. 66), for example, are making impressive strides. In one of the list's biggest surprises, Washington, D.C., and its surrounding suburbs have emerged as a veritable hot spot—though that's largely the result of record deficit spending and the strong tendency for government agencies in defense and homeland security to procure domestically. (See "This Sector Is Secured," above.)



True North Keep your hip kids, says Randy Rose, and send him workers who want to work.

[REPORT FROM GREEN BAY]

Everyone's a Knowledge Worker

IT'S CONVENTIONAL WISDOM that economic dynamism follows (and further attracts) the hip, the creative, the exceptional. But Randy Rose, CEO and president of Enzymatic Therapy, a 300-person manufacturer of dietary supplements,

says the key to success is a much humbler thing: drawing good local workers.

Rose, whose firm is based in Green Bay, Wis. (No. 4), credits his company's growth to the high caliber of the managers and rank-and-file workers he hires locally. "These are not only people who have a strong work ethic but they want to develop their careers," he says. "We try to have a learning organization here, and people here want to learn and grow. It makes all the difference in the world."

For some time Wisconsin has had the premier entrepreneurial economy in the Midwest. In addition to Green Bay, the No. 1 midsize city on last year's list, the state's standouts include La Crosse (No. 15) and Madison (No. 38). Even Milwaukee, the big city in the state, is a respectable No. 66. What's behind this success? In large part it's the quality of Wisconsin's public education system. Rose says the local workers he hires are well educated and well trained, at whatever level they are employed. Other Wisconsin business owners say the same. From the assembly line to the laboratory, Wisconsin employers seem particularly pleased with the level of skill and commitment shown by their workers.

Wisconsin also has avoided the problems associated with overconcentration in one industry—in particular the sensitivity to fluctuations in various marketplaces. This can be seen in the poor ranks for places tightly linked to particular industries—such as Detroit (No. 213) and Flint, Mich. (No. 271), both of which rely on the auto, and Columbia, S.C. (No. 266), which depends on textiles.

In addition, Wisconsin excels in highly specialized firms in areas such as machine tools, measurement controls, and machinery for making paper products. Many of these smaller manufacturing companies have actually benefited from the explosive growth in China. Between 1999 and 2003, the state's exports to China rose 265%, more than twice the Midwest average and almost three times that for the rest of the country.

Meanwhile, Wisconsin has a low cost of living and exceptional recreational opportunities. And the word is getting out, meaning it's becoming easier to add imported talent. Rose recently hired top managers from Oakland and Chicago. "When I first got here in 2002," he says, "our equity partners said it would be hard to get people here because of the location. What we found was quite the opposite." —J.K.

But the hottest areas continue to be the emerging economies of the South and West—such as Reno, this year's No. 1 city. Plenty of people may still head to "The Biggest Little City in the World" for gambling and easy divorces. But plenty more, many of them refugees from the San Francisco Bay area, are drawn by low housing prices and the friendly business environment. That steady migration has resulted in a 14.1% increase in business services jobs and a 6.1% increase in financial services jobs since 2001. PC-Doc-

tor, for example, a maker of software to test the components of personal computers, used to have offices overlooking San Francisco Bay. (See "A Californian Rolls the Dice," page 95.) But by 2003, the company decided California's high costs were too much of a strain on the bottom line and moved to Reno, setting up shop in a complex near offices of Microsoft and Intuit. With competitors in India offering similar services for one-quarter of the price, the move was a matter of survival, says Aki Korhonen, the

firm's founder and president. "You can't make the argument for operations in the Bay area versus India," he says.

But you can make the argument for Nevada, Korhonen learned. By moving to Reno, PC-Doctor has been able to cut basic operating expenses nearly 20%. That's helped the company keep blue-chip clients like Dell, IBM, and Fujitsu. And adjusting to doing business in Reno has been easy, Korhonen adds. Most computer manufacturers have consolidated in Asia, so it doesn't much matter where PC-Doctor is based. Nor has it been hard to attract talented employees. "A lot of our people are in their early 30s, and they benefited from the move," Korhonen says. "They can buy a home and, if they want, have a family on a single income."

Such factors have produced one of the most important shifts in the new new economy—the movement of young, educated workers, the raw material of growth, away from high-cost urban centers like Boston, the Bay area, and New York. "The knowledge migration—the bright flight—is going to smaller places that are not usually the prime suspects," says William Frey, a demographer at the Brookings Institution. "These places now have more to offer. The Starbucks culture is now coast-to-coast. You can get satellite TV, read good books, and go to good restaurants in all kinds of places."

Of course, not all lower-cost locales are doing well. No one complains about housing prices in, say, Sharon, Pa. (No. 272), Lansing, Mich. (No. 273), or Muncie, Ind. (No. 274). But those areas, beaten down by manufacturing's long decline, continue to suffer. On the other hand, communities that can attract skilled workers and nurture knowledge-based or service-industry businesses are thriving. Fort Myers, Fla. (No. 9), once was known as little more than a retirement haven. Now Fort Myers, as well as much of the rest of the southwestern Florida coast, is brimming with newly minted information, business services,

and financial services firms, many of them staffed with migrants to the area. “There’s a great and growing availability of talent in the area,” says Craig Pizaris-Henderson, whose search-engine marketing firm, FindWhat.com, is based in Fort Myers. The company has revenue of \$169 million and employs 195 in an office a stone’s throw from the Gulf. “We can fill most positions here within 24 hours,” Pizaris-Henderson says.

FindWhat.com is cashing in on a little-noticed trend that has been building for well over a decade. Even in the late 1990s, when the dot-com boom was in full flower and all the world’s attention was focused on Silicon Valley and Boston’s Route 128, some of the biggest job gains among educated workers were

each added 130,000 people over the same period.

These shifts in migration have had a profound effect on the relative health of the nation’s largest and most celebrated economies. Since 2001, for example, once red-hot Austin (No. 152) lost 12.9% of its information and 7.3% of its business services positions. Over the same period, Boston, one of the new economy’s first hotbeds, shed 22.3% of its information jobs, 11% of its business services positions, and 6.8% of its financial services jobs. San Francisco, another former new-economy darling, has suffered similar losses. New York City finally appears to be emerging from its post-September 11 slump, rising 41 places to No. 184, thanks to strong

to No. 66, this year—one of several Wisconsin areas that are making the state an anomaly in the Midwest. (See “Everyone’s a Knowledge Worker,” page 99.) Another surprise is St. Louis (No. 44). The city’s core continues to struggle, but its western suburbs are in the St. Louis MSA, and they boast a growing array of technology and business services firms. Day Veerlapati, president and CEO of S2Tech, a 75-person systems-development firm in the St. Louis suburb of Chesterfield, says lower costs, particularly lower housing costs, have helped him recruit software writers. “When I tell my friends in California that they can buy a four-bedroom house for \$150,000, they start to salivate,” Veerlapati says.

Declustering patterns can be seen in big cities. Philadelphia and its suburbs seem to exist on different planets.

taking place in Sunbelt cities like Orlando, Phoenix, Charlotte, N.C., Atlanta, and Las Vegas. Between 1995 and 2000, for example, Naples, Fla., ranked first in terms of net migration of young, single, college-educated people, according to the U.S. Census.

The process has only accelerated since then. Cities like New York, Boston, and San Francisco still attract many of the best and the brightest when they are in their 20s and early 30s. But as these people get older and start families, they tend to move to nearby suburbs or out of the region entirely. That’s one of the reasons, according to William Frey, that there has been large-scale out-migration among native-born Americans from major urban centers and a corresponding movement of people into places like Riverside-San Bernardino, Calif. (No. 6), Las Vegas (No. 14), and Phoenix (No. 16). Between 2000 and 2003, for example, New York experienced a net out-migration of some 469,000 native-born citizens. In San Francisco, the number was 118,000. Las Vegas and greater Phoenix, by contrast,

growth in health care and business and financial services. Yet New York’s overall performance pales compared with that of the region’s suburban economies, including Monmouth-Ocean, N.J. (No. 39), and Putnam County (No. 36) in New York’s Hudson Valley.

Similar declustering patterns can be seen in other big northeastern cities. The economies of Philadelphia (No. 265) and its southern New Jersey suburbs (No. 24), for example, seem to exist on different planets. A similar divergence can be seen between fast-growing Manchester, N.H. (No. 21), and the Boston region, from which it draws both workers and entrepreneurs. “Our address in southern New Hampshire was a big draw for engineers from down there,” says John McLaughlin, president and CEO of CoreMedical, a medical-industry job-placement firm in Windham, about 20 miles north of Manchester. “It’s the taxes, the housing costs, and the business climate that make the difference.”

Of course, not all metropolitan economies are hurting. Greater Milwaukee jumped more than 100 places,

Many big cities are struggling to catch up. Michigan Gov. Jennifer Granholm, for example, has launched a much-ballyhooed “cool cities” initiative, which stresses cultural and artistic development aimed at attracting young knowledge workers and new-economy companies to suffering Michigan cities like Detroit (No. 213) and Grand Rapids (No. 259). Mayor Martin O’Malley of Baltimore (No. 258) is considered an emerging Democratic Party superstar for similar efforts to target the hipster crowd. Sadly, neither the demographic data nor our own economic analysis reveals any substantial improvements in those cities.

The problem lies not in a dearth of hipness, but in a failure among many large cities to address longstanding problems rooted in the industrial age, says Joe Gyourko, a professor of real estate and finance at the University of Pennsylvania’s Wharton School. Many of America’s older cities remain saddled with large bureaucracies designed for a larger population and a broader tax base. Even as that tax base has shrunk,

few have managed to trim public payrolls or even boost productivity.

Philadelphia, for example, has succeeded in giving its center city an impressive face-lift—attracting tourists, as well as a growing community of singles,

don't really create jobs, we create companies. Route 128, Austin, and Silicon Valley are not where jobs are being created in America.”

Meanwhile, new venture capital networks are sprouting in places like Utah

vestors from the Bay area.

Treetop Technologies' Jason Crawford built his company without venture capital. But he welcomes these developments. More investment capital means that more entrepreneurs and

Venture capital networks are sprouting in Utah and Nevada—areas that have traditionally looked to the coasts.

gays, and childless couples. One result is that real estate values have risen dramatically. But the city's high business taxes, poor level of public services, crummy public schools, and reputation for political corruption continue to chase businesses to the neighboring suburbs (which, because of the population density of the East Coast, have their own MSA). “Philadelphia can't adjust to a high-mobility world where people can simply go somewhere else,” says Gyorko, who has studied the city's long-term decline. “To business and to the middle class, it seems very hard to reform. It's simply easier to exit.”

Are all established centers of high-wage employment destined to decline? Not necessarily. The existing concentrations of skilled workers and capital in a big city still can propel job growth. Seattle, for example, shot 91 spots up our list this year, to No. 72, thanks in part to Microsoft and its myriad spin-offs. New York and even hard-pressed San Francisco also are picking up steam.

Such growth may well continue into the decade's second half. Of course, so will competition—not only from abroad, but from the increasingly competitive regions that top this year's survey. These are areas that appear poised to provide the next generation of entrepreneurs the best fields of opportunity. Places such as Boston, San Francisco, and Silicon Valley will probably remain prime places to launch new concepts or companies, but they no longer may be the places to build them. “We've lost the hunger,” says John Butler, director of the Ic2 Institute in Austin, which studies economic and technology trends. “We

and Nevada—areas that have traditionally been forced to look to the coasts for investment capital. In 2000, there was only \$100 million in early-stage funds in Utah, notes Greg Warnock, managing director of VSpring Capital in Salt Lake City. Today, he estimates, that total is more than \$650 million.

It's no coincidence that Salt Lake City jumped 73 spots on this year's list, to No. 31. Says Warnock: “We are positioned to become a center of innovation.” You don't have to look too hard to encounter similar sentiments in other centers of the new new economy. These areas not only are developing their own investor networks, they are becoming increasingly attractive for in-

skilled workers will begin taking a second—or, indeed, even a first—look at his hometown. Once they do, Crawford predicts, they'll be hooked by Boise's low costs and high quality of life. More than that, he believes Boise's human values, its sense of community and cooperation, will accelerate its evolution into a major technology center. “Boise is all about intimacy, about people knowing each other,” Crawford says. “People here are determined to work together to create a community that can compete with anyone.”

Contributing editor Joel Kotkin is an Irvine Senior Fellow with the New America Foundation and the author of The City: A Global History (Modern Library, 2005).

HOW THE RANKINGS WERE CALCULATED

Our rankings are derived from three-month rolling averages of U.S. Bureau of Labor Statistics unadjusted employment data reported from September 1994 to September 2004. The data reflects the North American Industry Classification System categories, including total nonfarm employment and jobs in manufacturing, financial services, business and professional services, educational and health services, information, retail and wholesale trade, transportation and utilities, leisure and hospitality, and government. This allowed us to focus not only on job growth, but on high-wage sectors as well.

All areas for which full data sets and uniform area definitions were available from the past 10 years—274 regions in total—were included in this analysis. This approach excluded the construction sector, for which data was not reported for many of the regions in the BLS database. And it excluded the Denver and Boulder areas, which were redefined in January 2003. Preliminary reviews of the data do not show either of these two regions near the top of the rankings. Two additional regions—Hackensack and Patterson-Clifton-Pasaic, N.J.—were not included because they were not included in the latest BLS data. In instances where estimates were revised for 2003, the new values were used.

The growth index is calculated from a normalized, weighted summary of: 1) the current and prior year's employment growth rates, with the current year emphasized (two points); 2) the sum of the 1999–2004 and 1994–1999 employment growth rates multiplied by the ratio of the 1994–1999 growth rate over the 1999–2004 growth rate (two points); and 3) the difference between the current year's growth rate and the average 2001–2004 growth rate (half a point).

The balance index is calculated from a normalized, weighted summary of: 1) the standard deviation of each area's current percentage mix of major employment sectors (one point); the standard deviation of each area's percentage of total 1999–2004 growth generated by each sector (one point); and 3) the standard deviation of each sector's 2001–2004 growth rate (half a point).

To compute the final rankings, the growth index was weighted by 4.5 of a total of seven points and the balance index by 2.5 of seven points. Full growth and balance index data for all 274 regions can be found on Inc.com. —**Michael A. Shires**

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