The Ascension of DFW

How to Keep a Good Thing Going

2009 Annual Report
O'Neil Center for Global Markets and Freedom
SMU Cox School of Business

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The O'Neil Center for Global Markets and Freedom was established at SMU in 2008 by William J. "Bill" O'Neil (BBA, '55) and his wife Fay C. O'Neil to study the impact of competitive market forces on freedom and prosperity in the global economy.

The center offers education and training for today's forward-looking individuals who recognize the importance of globalization in changing the business environment in which we are all operating.

A Message from the Dean

The ebbs and flows of regional economies have intrigued me for as long as I can remember. It may go back to my childhood in New England, where I saw boarded up factories in once-thriving Massachusetts cities, such as New Bedford, Lowell and Fall River. The textile and apparel industry, once the region's bread and butter, had moved to the Southern states.

Years later, my dissertation and a book I wrote explored the industry's post-World War II southward migration, identifying the decisive factors as lower taxes and wages and cheaper energy and land. In short, textile and apparel companies went looking for a better place to do business—and they found it.

W. Michael Cox and Richard Alm tell a 21st Century version of the same story in "The Ascension of DFW," the essay in the first annual report from the O'Neil Center for Global Markets and Freedom. They portray the Dallas-Fort Worth area as today's better place to do business, benefitting from Texas' low taxes and limited government.

The textile and apparel industry that left New England for the South a few generations ago has now moved off shore, evidence that the great forces determining regional fortunes are now global rather than national in scope. Cox and Alm recognize globalization's vital role in DFW's prosperity. They identify DFW companies that are prospering in the global marketplace and make a strong case for the region emerging as a leader in services exports.

This essay is important work. It should generate great interest in California and other places, where companies burdened by taxes and regulations are looking for a better place to do business. It should also be read by DFW business leaders—not so they can gloat but so they can recognize what they must do to keep a good thing going.

As dean of the SMU Cox School of Business, I can't overemphasize this essay's value for our students—those already on campus and those who will enroll in the future. Choosing to study at SMU puts them at the heart of a vibrant, globalizing regional economy that will offer untold opportunity in the decades ahead.

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

The Ascension of DFW

How to Keep a Good Thing Going

By W. Michael Cox and Richard Alm

Economic freedom, globalization and exportable services give a lift to the DFW economy.

The Dallas-Fort Worth metropolitan area rises out of North Texas' pancake-flat prairies as a concrete, steel and glass monument to sheer determination and entrepreneurial drive. More than 6.3 million people sprawl across almost 9,300 square miles, among them 3 million workers who produce $400 billion a year in output.

Looking at today's DFW, the nation's fourth-largest urban economy, it's easy to forget that just 140 years ago Dallas was an isolated hamlet of 2,967 hardy souls, clinging precariously to the banks of the Trinity River. Atop Texas' population ranking in 1870 were Galveston at 13,818, San Antonio at 12,256, Brenham at 9,716 and Houston at 9,382. Dallas was far down the list at No. 17.

The city might have remained Prairie backwater if not for the railroads. The Houston and Texas Central came up from the south in 1872. A year later, the Texas and Pacific steamed into town with an east-west route, making Dallas a commercial crossroads and giving it an edge over other North Texas cities *(see box, page 4)*.

Rail connections made Dallas a shipping and supply center for North Texas, stimulating the city's first boom, a growth spurt that increased the population 50-fold in five decades. With nearly 160,000 people, Dallas ranked as the nation's 42nd largest city in 1920.

Even as Dallas grew in the first half of the 20th century, its livelihood depended on the land. In a Texas economy fueled by cotton, cattle and oil, the Dallas area didn't grow it, raise it or pump it. The city profited through financing, marketing, trading and merchandising what the land produced. By 1960, Dallas' population had risen to 680,000, ranking 16th in the nation.

At the top of the heap were the great manufacturing centers in the East and Midwest, which had grown up around water transport and railroad hubs. New York, Buffalo, Boston, Chicago, Cleveland, Detroit, Pittsburgh and St. Louis dominated the U.S. economy from the late 19th century to the mid-20th century. They had become the nation's chief producers of household

appliances, automobiles, consumer goods, machinery and steel.

In the second half of the 20th century, American manufacturing began its slow and inexorable decline as the nation's economic base shifted to services. New York, Chicago, Boston and a few other big cities adapted to the new economic reality by replacing factory jobs with services work.

Other industrial cities lost their manufacturing jobs and went into long-term decline. Cleveland, St. Louis, Pittsburgh and Buffalo, all once among the 10 largest U.S. cities, have now fallen out of the Top 40. Along with Detroit, they have become sad symbols of urban decline and neglect, struggling with falling property values, crime and unemployment.

Tied to agriculture, ranching and oil, Dallas and its surrounding cities didn't play a large role in America's Industrial Age. DFW emerged as an economic powerhouse only in the second half of the 20th Century—after air-conditioning eased the misery of North Texas' hot summers.

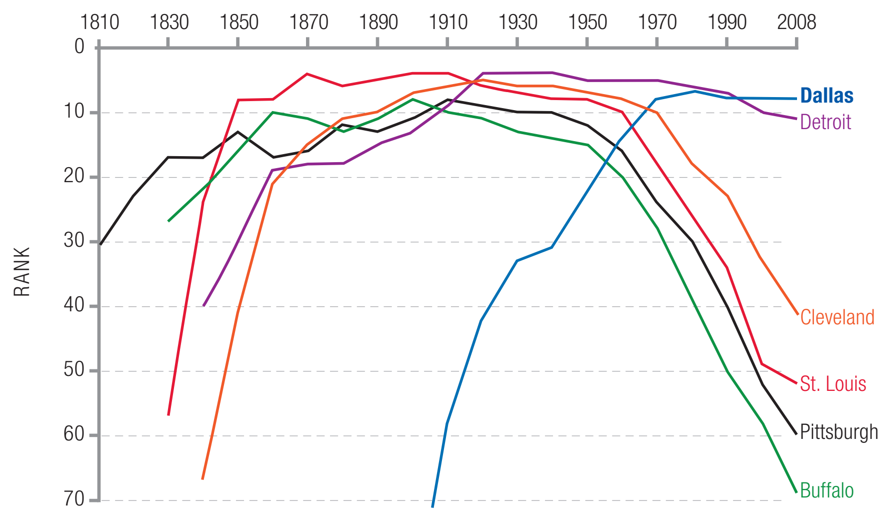
Building a vibrant economy based on white-collar employment, Dallas rocketed up the ranks of U.S. cities, bypassing the fading urban centers of yesteryear. By the late 1960s, it had become one of America's 10 largest cities *(Exhibit 1)*.

And growth has been accelerating.

EXHIBIT 1

Rising Toward the Top

Dallas' strong post-Industrial Age economy has been the key factor in its climb in the population ranking of U.S.cities. Once-dominant Rust Belt cities have fallen in the rankings.



From 1998 to 2008, DFW added an average of 150,000 new residents a year, an annual gain that rose to 165,000 in the past three years. At this rate, DFW adds nearly 1 million people every six years.

The main attraction has been jobs. Over the past 15 years, a period that includes two recessions, DFW employment has climbed from 2.3 million to 2.9 million, ranking second only to the New York area in net job creation. DFW is one of just seven Top 20 cities to add jobs since 2004.

DFW's population growth is on pace to add almost 1 million new residents every six years.

Railroads: A Catalyst for Economic Change

After the Civil War, America laid railroad tracks at a furious pace. Total mileage increased from 52,922 in 1870 to 166,703 in 1890 as the railroads pushed west and south.

Early in this period, locomotives started chugging into North Texas, creating a transportation revolution that reordered the fortunes of the region's cities. Before the railroad arrived in Texas, passengers and goods moved overland to the nearest river or seaport in wagons pulled by horses, mules or oxen. Epic cattle drives took beef on the hoof to railheads in Kansas.

Texas' Biggest Cities, 1870

1. Galveston	13,818
2. San Antonio	12,256
3. Brenham	9,716
4. Houston	9,382
5. Sherman	6,348
6. Brownsville	4,905
7. Jefferson	4,190
8. Austin	3,907

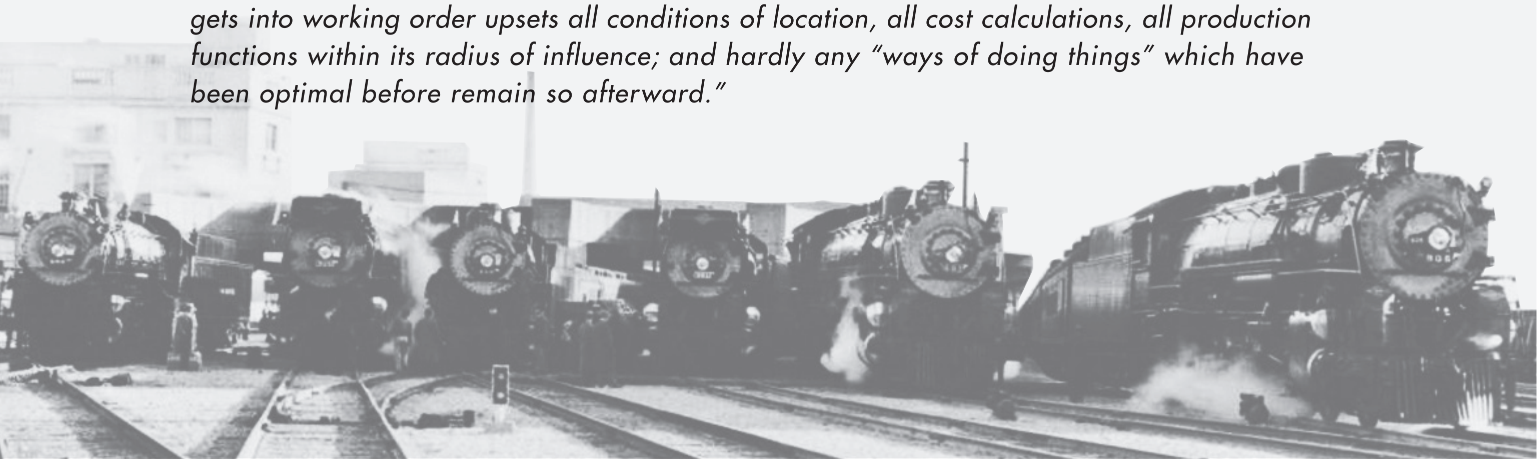
Down on the Gulf Coast, Galveston was Texas' biggest city in 1870. In the northern part of the state, Jefferson rose to prominence because of its location on the banks of Big Cypress Bayou, then a navigable branch of the Red River. Steamboats docked in Jefferson, bringing new residents to Texas and taking the state's farm products to market—especially cotton. The city boomed. It was the first in Texas to install natural gas for lighting and manufacture ice for commercial sale.

Between 1867 and 1870, Jefferson's trade jumped from $3 million to $8 million, putting it behind only Galveston as a commercial center. A few years later, the bottom fell out. In 1873, the Corps of Engineers blew up a log raft on the Red River near Shreveport, La., lowering the water level in Big Cypress Bayou and impeding steamboat traffic. At about the same time, the railroads came to North Texas, arriving in Dallas before Jefferson.

Dallas began its rise, Jefferson its decline.

More than six decades later, economist Joseph Schumpeter seized on railroads as a prime example of the kind of world-shaking technological change that would send great waves of progress through a capitalist economy. He put it this way:

"A railroad through new country, i.e., country not yet served by railroads, as soon as it gets into working order upsets all conditions of location, all cost calculations, all production functions within its radius of influence; and hardly any "ways of doing things" which have been optimal before remain so afterward."



Like the rest of the country, DFW lost jobs in the severe downturn. However, it remained relatively healthy in hard times. During 2009, the only large metropolitan area with a lower unemployment rate was Washington, D.C., where the economy relies largely on public spending.

DFW owes its economic success to a variety of factors. The area offers a skilled labor force, modern infrastructure, relatively low costs of doing business and a central location tied to air, rail and road networks.

DFW's diverse economy is home to major players—some home grown, some transplants—in communications, consumer products, chemicals, energy, entertainment, financial services, information processing, high technology, health care, home building, retailing and transportation.

In 2008, the area had 116 public and 63 private companies with revenues exceeding $100 million. It has more corporate headquarters than any other U.S. metropolitan area, including 24 companies in the Fortune 500.

These advantages often show up in business climate surveys, but they don't completely explain DFW's economic success. The ascension of DFW—and the region's prospects for the future—owes even more to three fundamental factors that the studies often overlook.

First, DFW benefits from its location in Texas, a state that maintains one of the world's freest economies. Second, DFW has embraced globalization, emerging as a leader in profiting from opportunities outside the United States. Third, DFW brings together businesses and workers well-suited for success in the up-and–coming services economy, both at home and overseas. For DFW, nurturing these advantages is the best way to keep a good thing going.

DFW has more corporate headquarters than any other U.S. metropolitan area.

Thousands of DFW companies are engaged in global business—among them GameStop, Kimberly-Clark and Cinemark.

Economic Freedom

Adam Smith and Milton Friedman taught us the path to prosperity lies in economic freedom. Empirical proof for their eloquent arguments comes from the Fraser Institute, which finds that the nations with top scores on its Economic Freedom of the World measures have the highest per capita incomes.

Fraser ranks the U.S. economy as one of the freest in the world. A related Fraser study ranks Texas the second freest state, behind only Delaware *(Exhibit 2)*. Other large states are far down the rankings—Florida at No. 22, California at No. 29 and New York at No. 41.

What is Texas doing right? The answer lies in the metrics that gauge economic freedom at the state level *(Exhibit 3)*. For starters, Texas keeps taxes low. It's one of seven states with no individual income tax and one of five states with no corporate income tax. Texas levies a general business tax—but at a relatively light effective marginal rate of less than 1 percent.

Other states penalize work and enterprise more heavily—for example, the highest marginal tax rates are 12 percent on individual income in Massachusetts and 12 percent on corporate profits in Iowa. California's top rates are 10.6 percent for wages and 10.8 percent for corporate profits.

With no income taxes, Texas relies primarily on sales taxes to finance its government operations. But that doesn't mean the state socks it to consumers. Texas lies back in the pack at 19th in sales tax collections as a share of gross state product (GSP), tied with California, a state that puts a heavy income tax burden on its workers and companies. However, Texas is only a few tenths of a percentage point out of the bottom third. Among states with no individual income taxes, only Alaska has a lower ratio of sales taxes to GSP.

When it comes to the size of state government, Texas fares quite well. It's near the bottom in spending as a share of GSP. Government transfers as a share of state economic activity are low, too. Texas finds itself in the middle of the pack in the government's share of the state workforce.

Texas' labor market is relatively free of impediments that discourage job creation. Partly because its right-to-work laws forbid forcing workers to join unions, Texas ranks low in union membership—at 6.2 percent of private sector workers, well below New York's 27.5 percent and California's 17.8 percent. The gap widens considerably among government workers. Texas' public sector unionization rate is 14 percent, compared with New York's 73 percent and California's 58 percent.

Unlike California and 13 other states, Texas doesn't mandate a minimum wage above the federal standard. Texas' minimum wage is relatively low compared with the average wage, suggesting that employers and workers freely negotiate a relatively large share of the state's wage contracts.

Texas' high degree of economic freedom gives home-grown businesses room to grow. It also acts like a magnet for newcomers—job seekers and companies from other states and countries. Texas ranks third among states in "insourced" jobs, or employment generated by foreign investment.

The result is a private-sector dynamism that put five Texas metropolitan areas among the top 12 on *Inc.* magazine's Top Cities for Doing Business. *Chief Executive* magazine named Texas the

Texas is one of the few states with no individual income tax and no corporate income tax.

EXHIBIT 2

Texas Stands Tall in Economic Freedom

The Fraser Institute uses a range of data to determine how states compare in policies favorable to free enterprise.

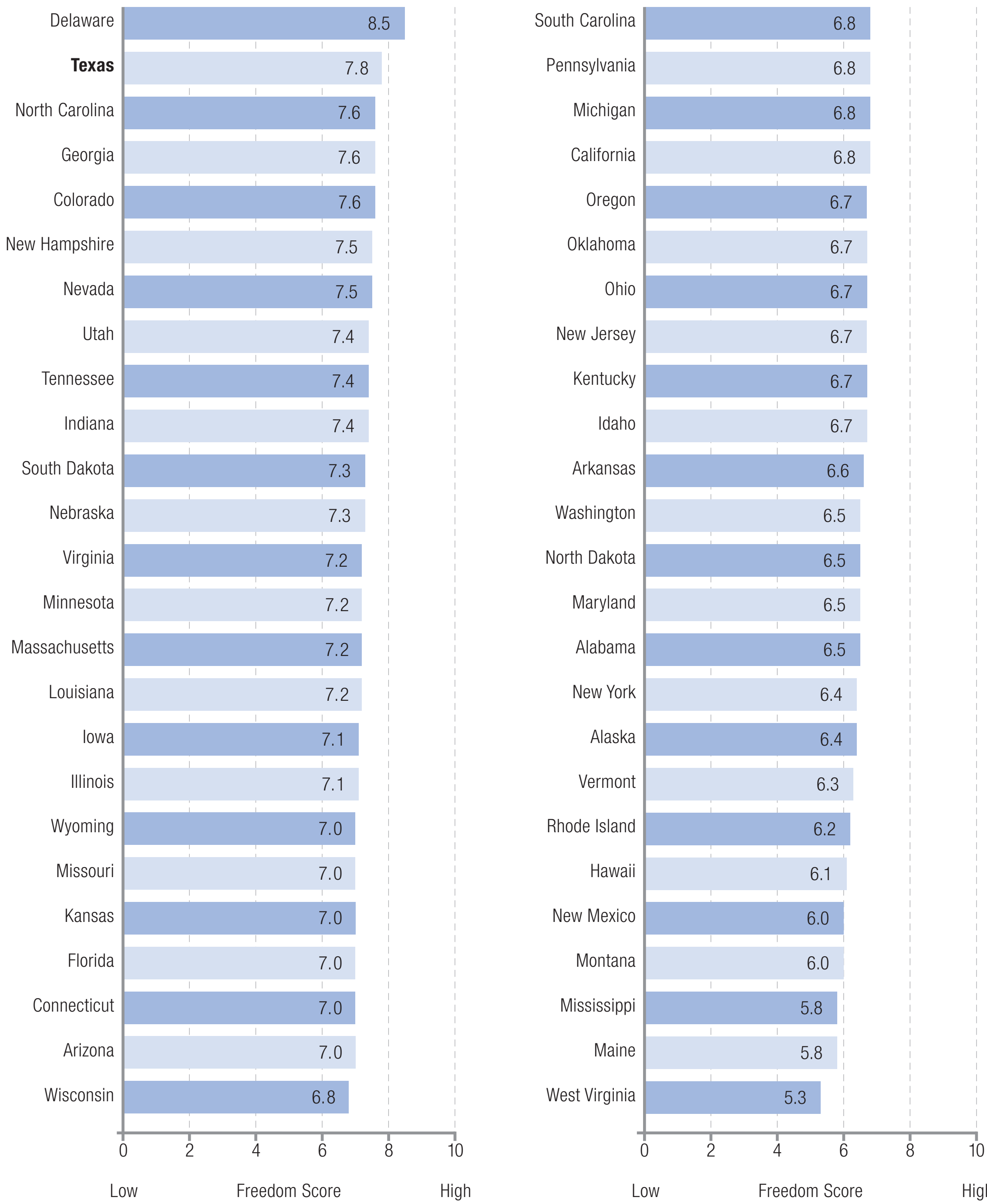
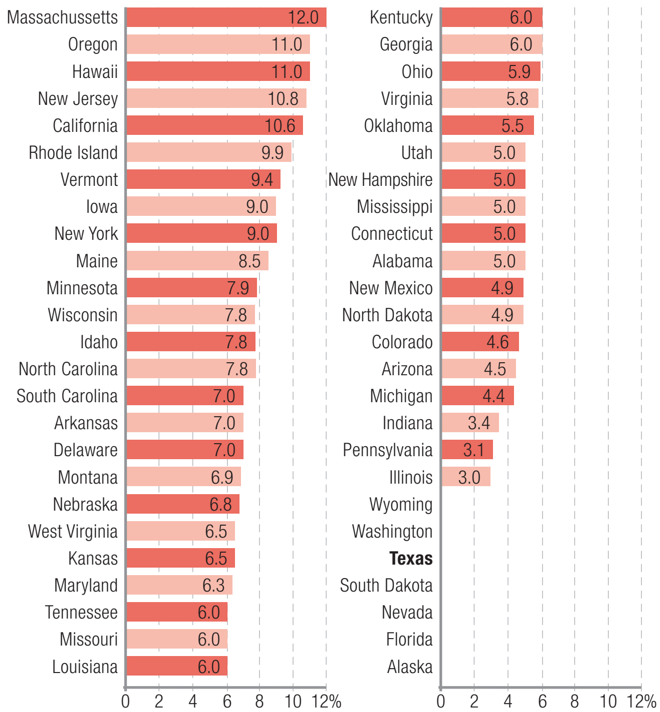


EXHIBIT 3

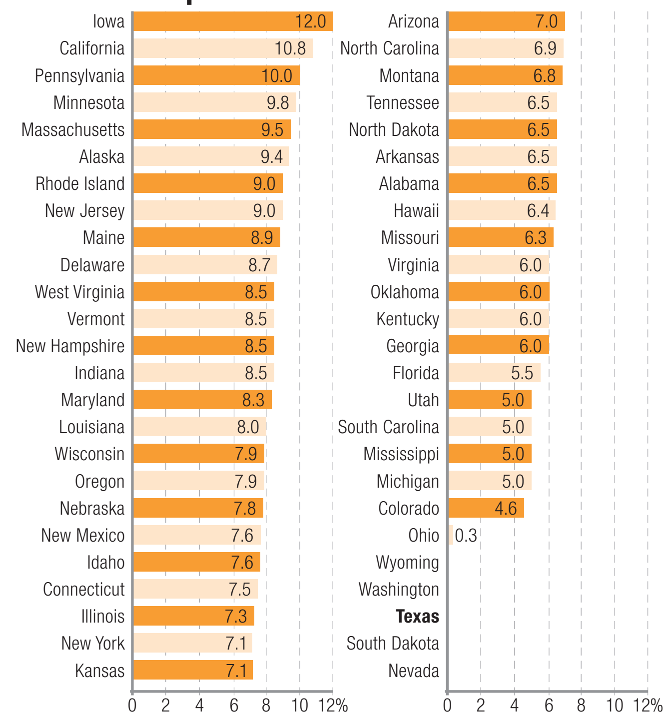
Texas' Economic Freedom: A Closer Look

Various measures show how Texas ranks relative to other states in tax burden and other factors that contribute to a market economy's success.

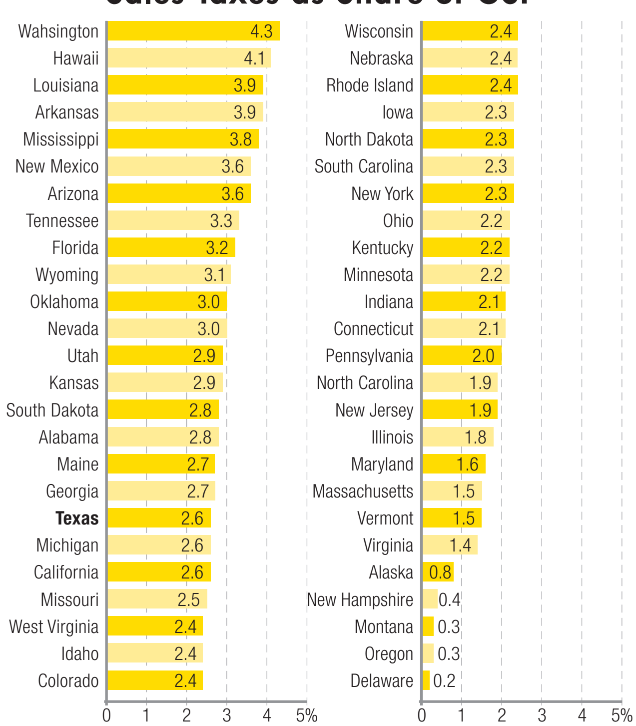
Individual Income Tax Rates



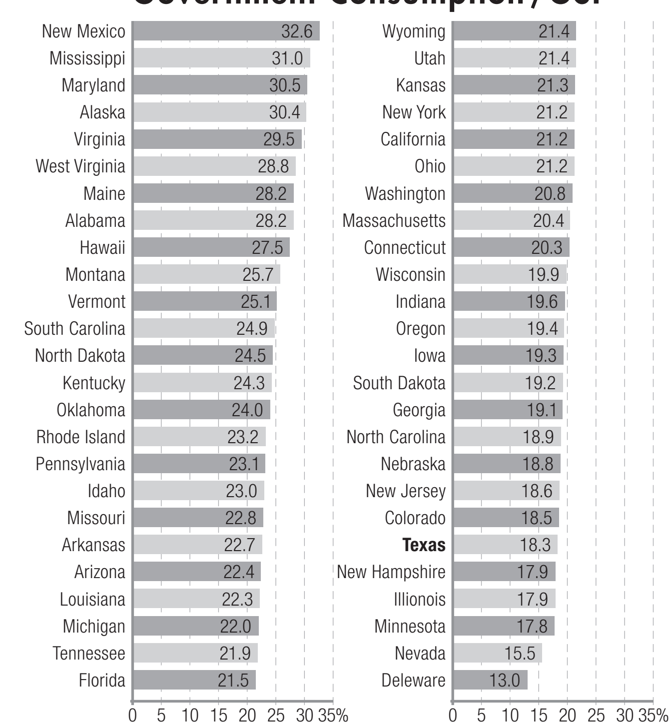
Corporate Income Tax Rates



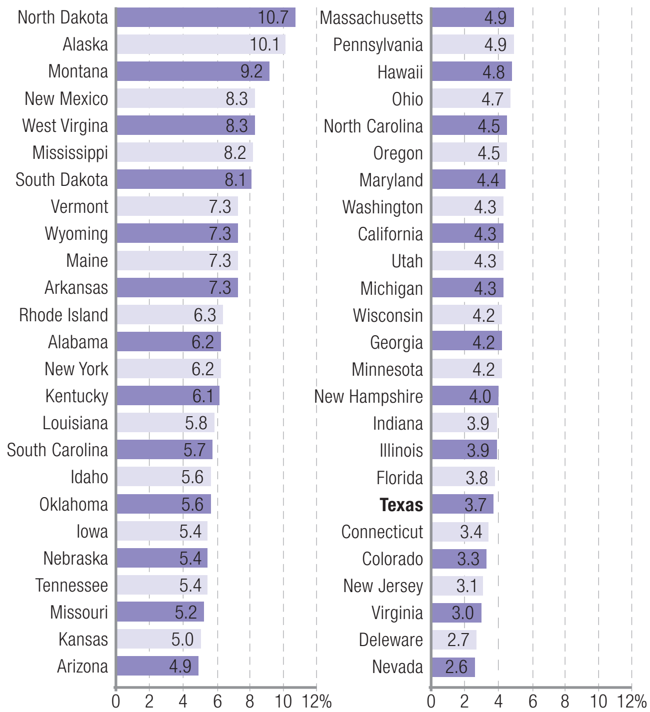
Sales Taxes as Share of GSP



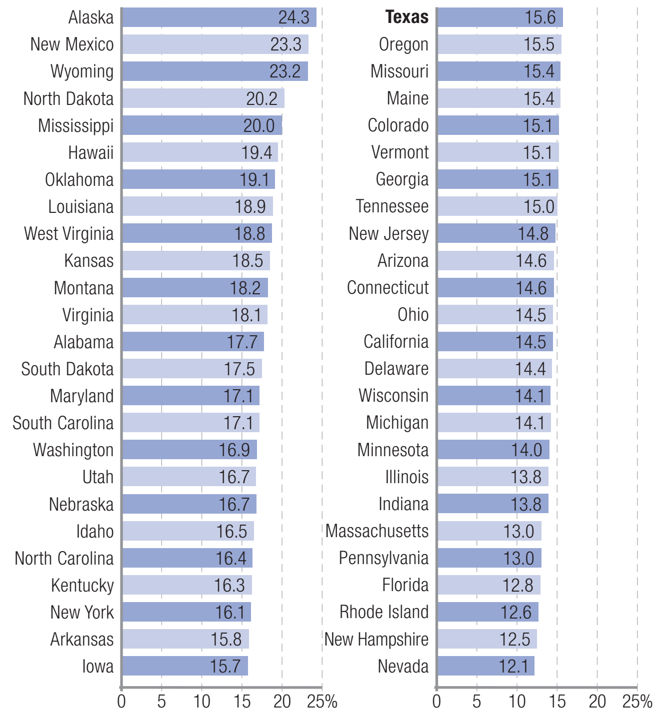
Government Consumption/GSP



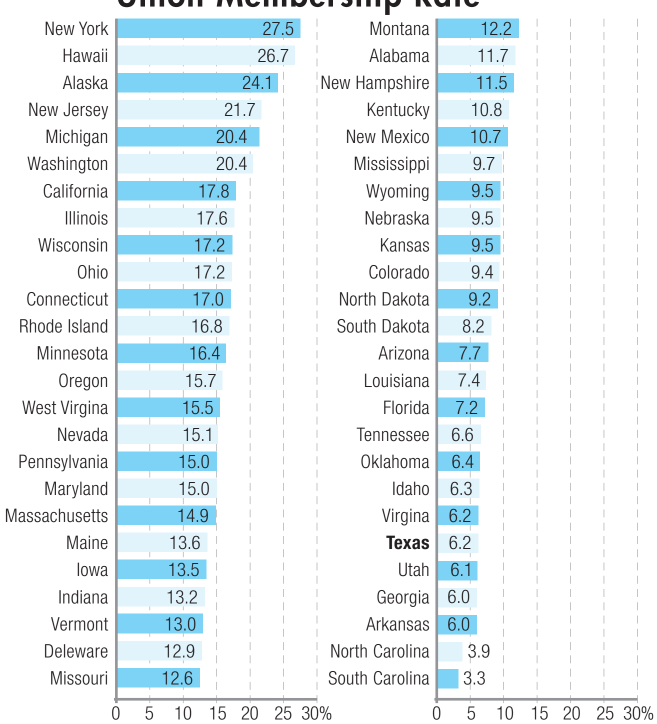
Government Transfers / GSP



Government Share of Labor Force



Union Membership Rate



Minimum/Average Wage

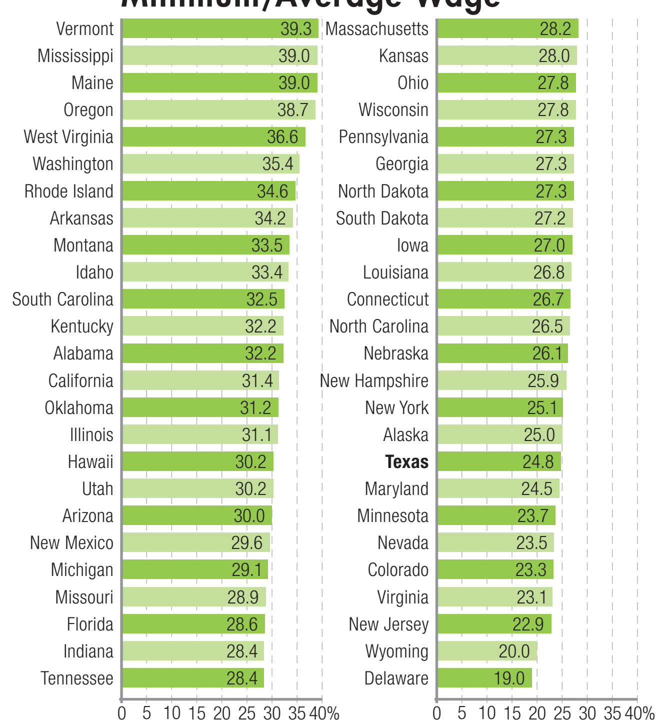
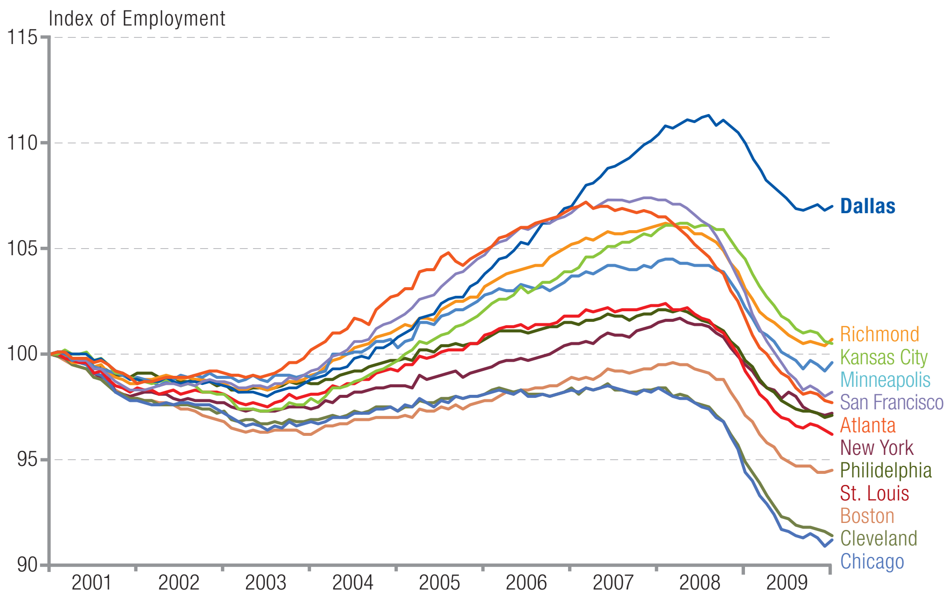


EXHIBIT 4

Job Growth Fastest in Dallas Fed District

Greater economic freedom has been a key factor in stimulating employment gains in a region that includes Texas and parts of Louisiana and New Mexico.



best place for job growth and business in 2009—and California the worst.

Employment growth in the 12 Federal Reserve districts confirms that Texas' economy has been doing particularly well in the past few years. At mid-decade, with recovery from the relatively mild 2001 recession under way, the Dallas Fed's area was among the top three districts in job growth. Since then, it has rocketed to the top, faring better even after the nation fell into a deep recession at the end of 2007 *(Exhibit 4)*.

Legally speaking, Texas' economic freedom doesn't extend beyond the state borders. As a practical matter, however, the state's companies can take advantage of that freedom to prosper nationally and even globally.

World of Opportunity

Globalization is a straightforward concept—the breakdown of barriers to the movement of goods, services, money, people and ideas across national boundaries. Integrating the world economy increases competition for workers and companies, and it unleashes forces that forge more efficient international distribution of production. Low-wage nations gain routine manufacturing and services, and high-wage nations specialize in more sophisticated economic activity.

Globalization's competition and efficiency often come at the cost of wrenching changes in the labor market, and many Americans want to retreat in vain hopes of maintaining the status quo. That's a mistake for two reasons. First, hiding from globalization leads to economic decline. Second, globalization creates opportunities for many U.S. companies and workers.

Simple math provides a rough idea of what's out there. With 306 million people, the U.S. makes up only a small share of the world's population of 6.5 billion. So 21 of 22 potential customers are beyond our borders. Just a small percentage of the world's business will add significantly to the sales and employment of companies in DFW and the rest of the United States.

Big overseas markets too poor to buy or hunkered down behind protectionist walls would mean little to U.S. companies. In the past two decades, however, China, India and many other countries have freed their markets and opened their economies—joining the global capitalist system. These remarkable revolutions of ideology and policy created 3 billion new capitalists, igniting growth spurts that have lifted millions of people out of poverty.

Consider just China and India, with a combined population of 2.5 billion. From 1998 to 2008, China's economy expanded an average 9.5 percent a year and India's grew by 7 percent a year *(Exhibit 5)*. The growth means workers who are eager to buy consumer goods and companies that are ready to purchase intermediate inputs.

We hear about these Asian giants' huge exports, but economic revival has also whetted these nations' appetites for the world's goods and services. China exports 35 percent of its GDP—but it imports 28 percent. India exports 24 percent and imports 30 percent.

Globalized countries, regions, industries and companies stand the best chance of profiting from the growing demand from China, India and other countries. When we look at DFW, we see a corporate makeup and talent pool tailor made for the global marketplace.

Measuring globalization isn't easy for nations. It's even trickier for states and cities, whose international connections aren't always well documented. For North Texas, signs of increased globalization include an expanding roster of foreign-owned companies, more foreign-born residents and healthy international traffic at DFW International Airport.

Evidence of DFW's globalization is particularly strong at the company level. Many local firms have made strides in foreign markets, with international operations accounting for a greater share of their overall revenues *(Exhibit 6)*.

Dallas-based Texas Instruments has had an eye on global markets for decades. The company opened its first foreign plant in 1957 and expanded overseas operations as it became one of the world's leading suppliers of semiconductors for cell phones and other products.

By 1998, TI was well-established globally, earning two-thirds of its revenues outside the United States. Foreign sales fluctuated over the next decade but hit 88 percent of total revenues in 2008. Meanwhile, domestic sales shrank—both in relative and absolute terms.

Like TI, Fort Worth-based American Airlines has a decades-long heritage of doing business internationally. From 1998 to 2008, its foreign operations grew from 30 percent to 41 percent of revenues, providing the only source of growth in a tough decade for the airline industry.

Farmers Branch-based Celanese, a major chemical producer, logged 75 percent of its sales overseas in 2008, up from 61 percent six years earlier. Kimberly-Clark, an Irving-based maker of Kleenex tissues, Huggies diapers and other paper products, saw its foreign sales rise from 40 percent of revenues in 1998 to 48 percent in 2008.

At Fluor, an engineering and construction firm based in Irving, the overseas share of revenues went from 38 percent to 49 percent over the decade. The 10-year increase in share of overseas sales for Ensco, a Dallas-based provider of offshore drilling services, was 45 percent to 79 percent. Commercial Metals, an Irving-based company that manufactures, recycles and markets steel and other metals, went from 14 percent to 41 percent.

Some companies are relative newcomers to the global market. Grapevine-based GameStop, the world's largest video game retailer, had

When we look at DFW, we see a corporate makeup and talent pool tailor made for the global marketplace.

EXHIBIT 5

Big Overseas Markets Growing Rapidly

DFW companies can find export opportunities in emerging economies that are growing rapidly. When combined, China and India make up a market eight times larger than the United States, growing three times as fast.

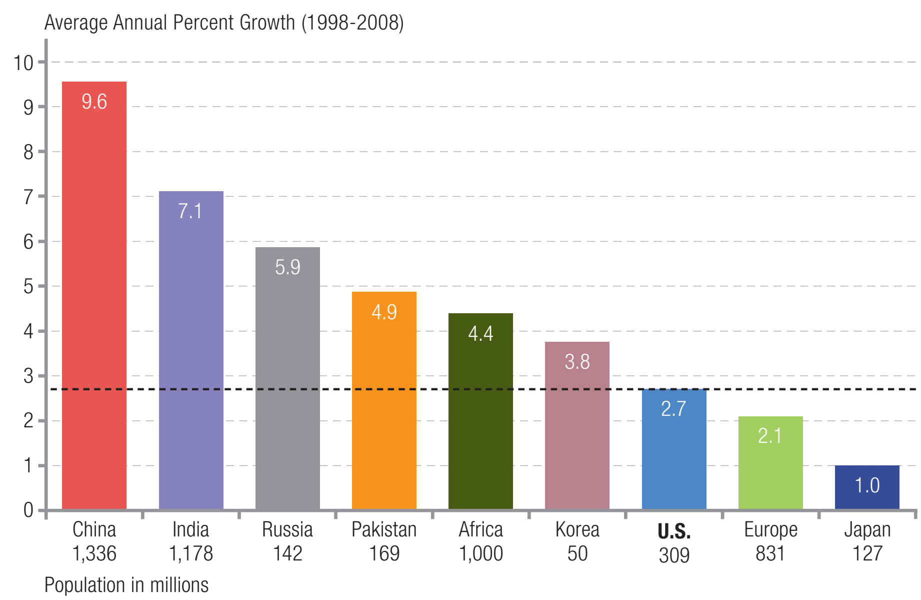
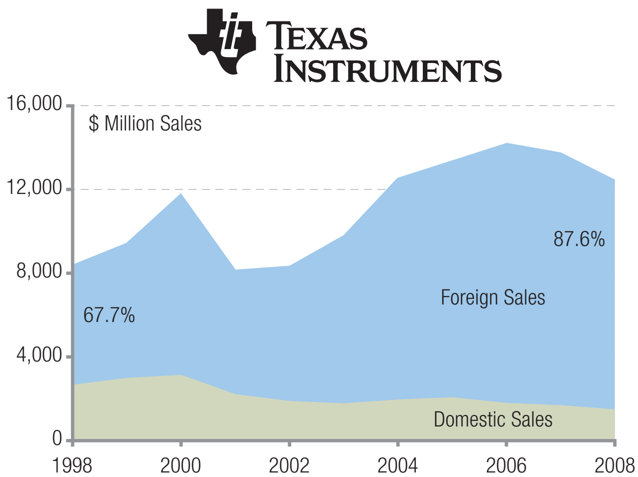
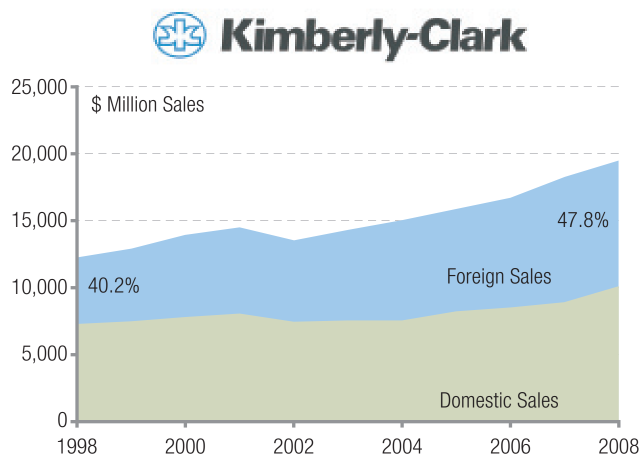


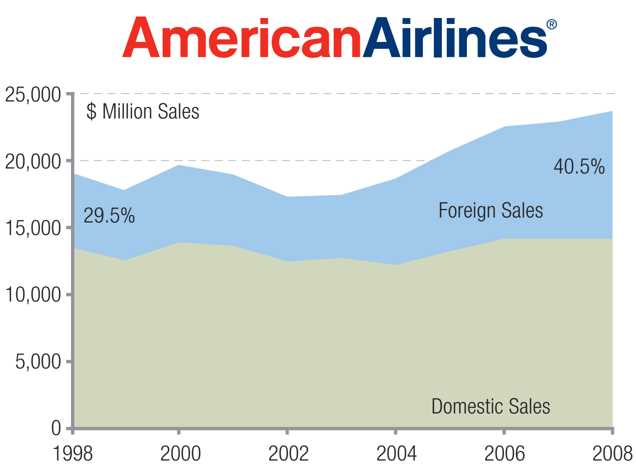
EXHIBIT 6

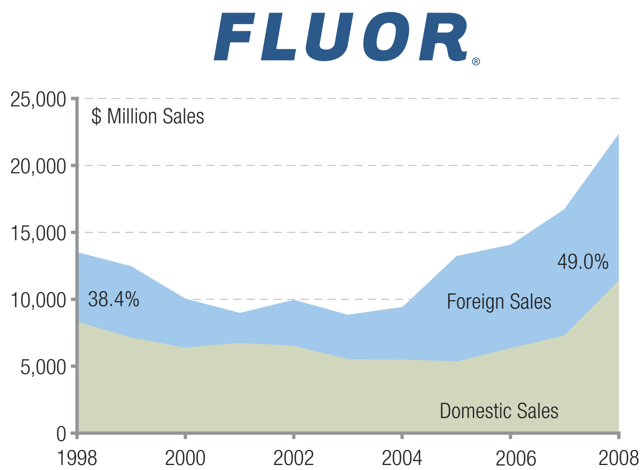
DFW Companies Venture Abroad

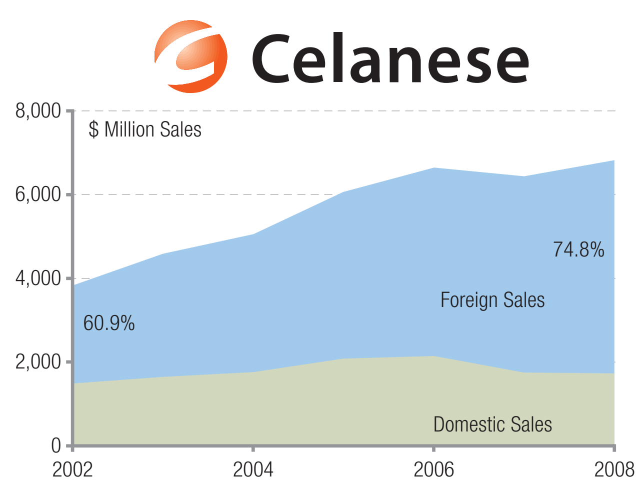
Taking advantage of globalization, many North Texas-based companies are finding that foreign countries offer the best prospects for sales growth.

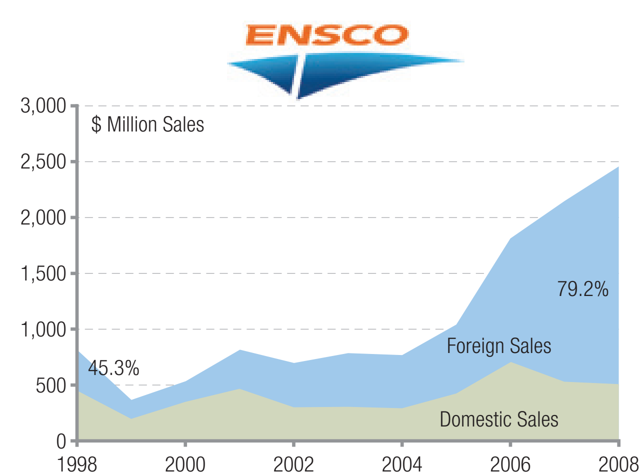




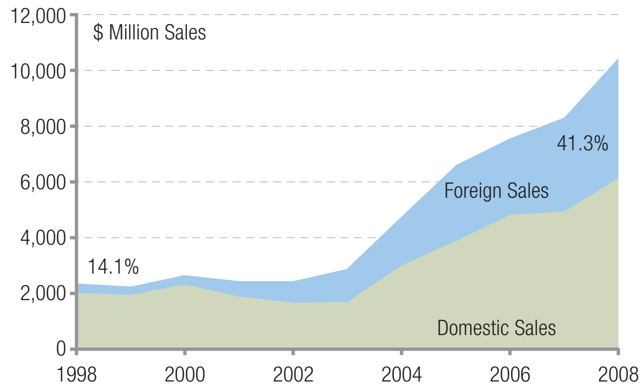




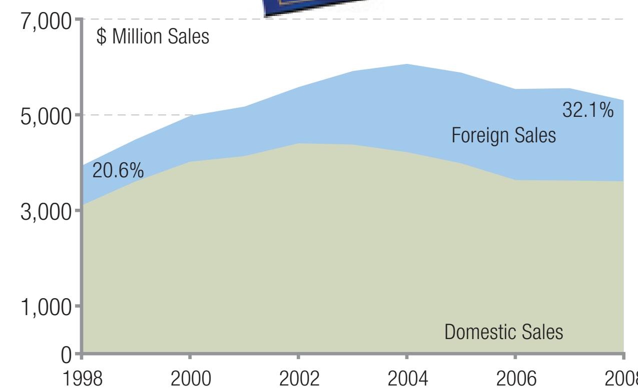




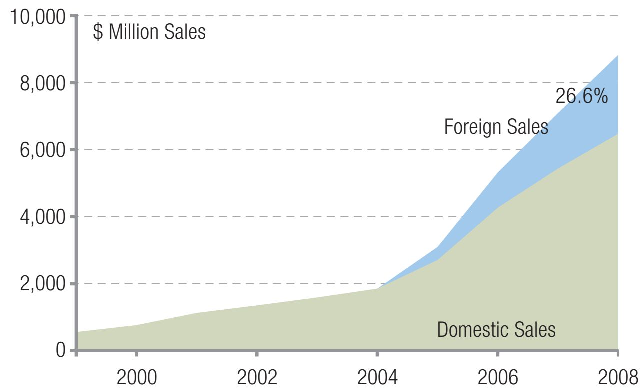
Commercial Metals Company



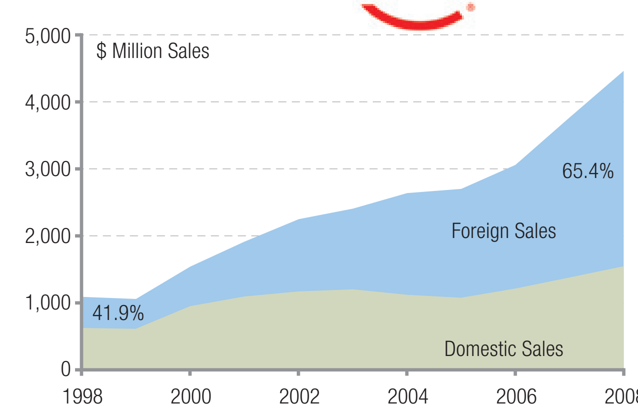
BLOCKBUSTER



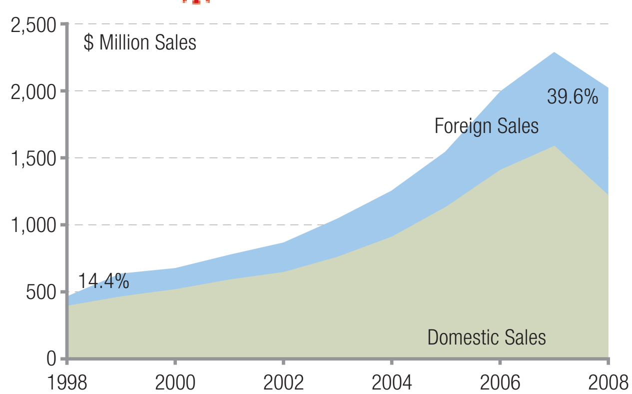
GameStop



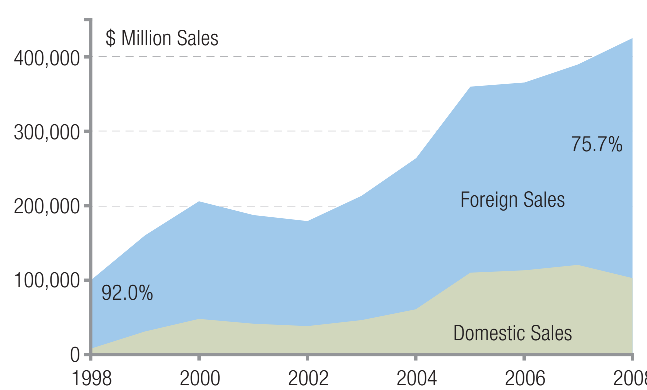
FLOWSERVE



AllianceData



ExxonMobil



no overseas sales until 2005; since then, the company has spread to 16 countries and its foreign operations rose to 27 percent of revenues in 2008.

Alliance Data Systems, a Dallas-based company that sells data and electronic marketing services, expanded its overseas business from 14 percent to 40 percent of revenues. Dallas' Blockbuster, the movie and video rental company, rose from 21 percent to 32 percent.

Foreign customers accounted for nearly two-thirds of revenues at Flowserve Corp., an Irving-based industrial pump and valve supplier for energy, power, chemical and water. For Irving-based ExxonMobil, the foreign share has slipped over the past decade, but the oil giant's overseas revenues have risen sharply and still account for three-quarters of the total.

Many other DFW Fortune 1000 companies are doing well in the global marketplace—among them, semiconductor manufacturer Diodes, chemical-maker Kronos Worldwide, and watchmaker Fossil *(Exhibit 7)*. As Southwestern Bell, AT&T was once the local phone company; now, it earns more than a quarter of its revenues from global operations.

In addition, internationally successful companies based elsewhere have major operations in DFW—for example, Hewlett-Packard added to its North Texas presence in buying EDS, a Plano-based information processing company, in 2008. PepsiCo operates its global snack-food division from Frito-Lay's Plano headquarters.

Yum! Brands has been going global with KFC fried chicken, Pizza Hut and Taco Bell, and its Dallas-based subsidiary Yum! Restaurants International oversees more than 13,000 restaurants in 110 countries. DFW also hosts significant operations for building systems and auto parts maker Johnson Controls, computer services icon IBM and consumer products giant Procter & Gamble.

Among privately held companies, many DFW stalwarts have been globalizing. For example, Mary Kay sells cosmetics in 35 countries. Hunt Oil operates in Canada, Yemen, Peru and other countries. Beck Group, a Dallas-based construction firm, has established a foothold in Mexico City.

For nearly two decades, SMU's Caruth Institute for Entrepreneurship has identified DFW's fastest-growing emerging companies. More than half the Dallas 100's class of 2009 already had ties to foreign markets, suggesting the up-and-coming generation of business leaders is focused on globalization's opportunities.

International business runs two ways—imports as well as exports. DFW companies selling abroad are joined by others with business models that rely on international supply chains. Plano-based J.C. Penney and Michaels Stores, an Irving-based national arts and crafts chain, stock their shelves with foreign-made goods—so they can hold down costs and survive in the highly competitive U.S. retail sector.

EXHIBIT 7

Globalizing North Texas

In addition to the companies featured in Exhibit 6, DFW's international reach extends to other locally significant Fortune 2000 firms (foreign revenues as shares of total).

DFW Based	Pct.	DFW Operations	Pct.
Diodes	80.0	Hewlett Packard	68.8
Kronos Worldwide	62.1	Johnson Controls	64.9
Fossil	56.4	IBM	64.6
AT&T	27.0	Procter & Gamble	60.5
Pfsweb	22.1	Yum! Brands (photo)	54.6
Cinemark Holdings	21.9	General Motors	49.4
Lennox International	18.6	Pepsico	48.0
Sally Beauty Holdings	18.0	Microsoft	40.5
Zales	15.2	FedEx	28.1
Perot Systems	12.8	Raytheon	19.8

Among the DFW companies selling services abroad is Laguarda.Low, an architectural firm whose project include the Avenida 8 shopping center in Sao Joao da Madiera, Portugal.

Selling Our Services

For millennia, coastal cities have been at the forefront of globalization—not surprising because they were the portals through which people and goods entered and left most countries. Cities like DFW could only connect to the world through these seaports. Now, information and communications technologies are eroding coastal cities' edge and giving hinterland cities direct access to the global markets.

These advances are familiar by now—computers, cell phones, sophisticated software, fiber-optic transmission lines and, most important, the Internet. In the past decade or so, this global communications network has reached critical mass in two key areas. First, data-transmission capacity has become large enough to move vast amounts of information at trivial cost. Second, connectivity has reached nearly every corner of the world, greatly expanding the potential for making business contacts.

In the 21st century, the Internet is to services what the train was to goods in the 19th century—a revolutionary delivery vehicle. The Internet breaks down the physical obstacles that once stifled international trade in services. The result is a fusion of national services markets into global ones. Companies can now court far-flung customers and deliver services nearly anywhere in the world cheaply and quickly.

The impossible becomes possible, then routine. Bandwidth is wide enough to manipulate tiny computerized surgical tools at vast distances, allowing doctors to operate on patients in other counties. Using TutorVista.com, American students can sit at their home computers and tap into on-line tutoring from PhD.s in India and other far-off places.

New technologies, combined with a worldwide lowering of trade barriers, have fueled a global surge in selling services across international borders. The United States has been a big winner, ranking No. 1 in services exports by a wide margin. U.S. companies sold $526 billion in services abroad in 2008, a gain of 84 percent since 2000, surpassing the 66 percent growth rate for goods.

U.S. trade deficits in goods have been massive; meanwhile, the country runs a large and growing surplus in services. The United States ran a services surplus of $144 billion in 2008, up from $75 billion in 2000 and $58 billion in 1992. For U.S. companies, winning in the global services marketplace owes to the excellence of their products, not subsidies or protectionism.

Digging down into Commerce Department data shows the United States has been a top-notch competitor in many of the high-value-added services that support well-paying jobs. In 2008, our exports exceeded imports by nearly nine to one in operational leasing, a segment of the industry that handles short-term deals on airplanes, vehicles and other equipment *(Exhibit 8)*.

Our edge was six to one in distributing movies and television shows and nearly four to one in mining and architectural, construction and engineering services. Royalties and license fees, one of the largest categories in dollar terms, came out better than three to one, as did law, education, finance, medicine and advertising.

All told, the U.S. did well in 21 of 22 services trade categories. It recorded striking surpluses in 12 of them. We held our own in nine others, where exports and imports were fairly well balanced. Only in insurance did the United States run a significant deficit, an outcome that reflects a rich country's need to spread risk through global reinsurance markets.

Dallas' services prowess has deep historical roots. Becoming a railroad crossroads in the 19th Century created wealth and a thriving services economy–with Dallas as a broker for Texas' cotton and a financier for the state's oil industry. Over the decades, the skills and infrastructure that served local industries grew to meet the needs of national customers. Now, DFW services companies are taking the next step—the global arena.

Data aren't available to directly measure major cities' services trade. However, employment counts show that services make up a large and growing share of DFW's economy. At the end of 2009, service-producing industries accounted for 83.2 percent of the metropolitan area's private-sector employment, up from 76.8 percent at the decade's start. Meanwhile, the share of workers in goods-producing industries has been declining steadily.

Most U.S. cities have seen similar employment-base shifts, but DFW has also been rapidly enhancing its capacity as a global services provider. It has built up its workforce in information, finance, and professional and business services—the categories most likely to reach customers outside the metropolitan area. By contrast, education, health care, leisure and hospitality are services that cater largely to local and regional markets.

The three highly tradable services

EXHIBIT 8

A U.S. Success Story: Services Trade

Comparing exports and imports shows that U.S. companies are competitive in an overwhelming majority of services categories.

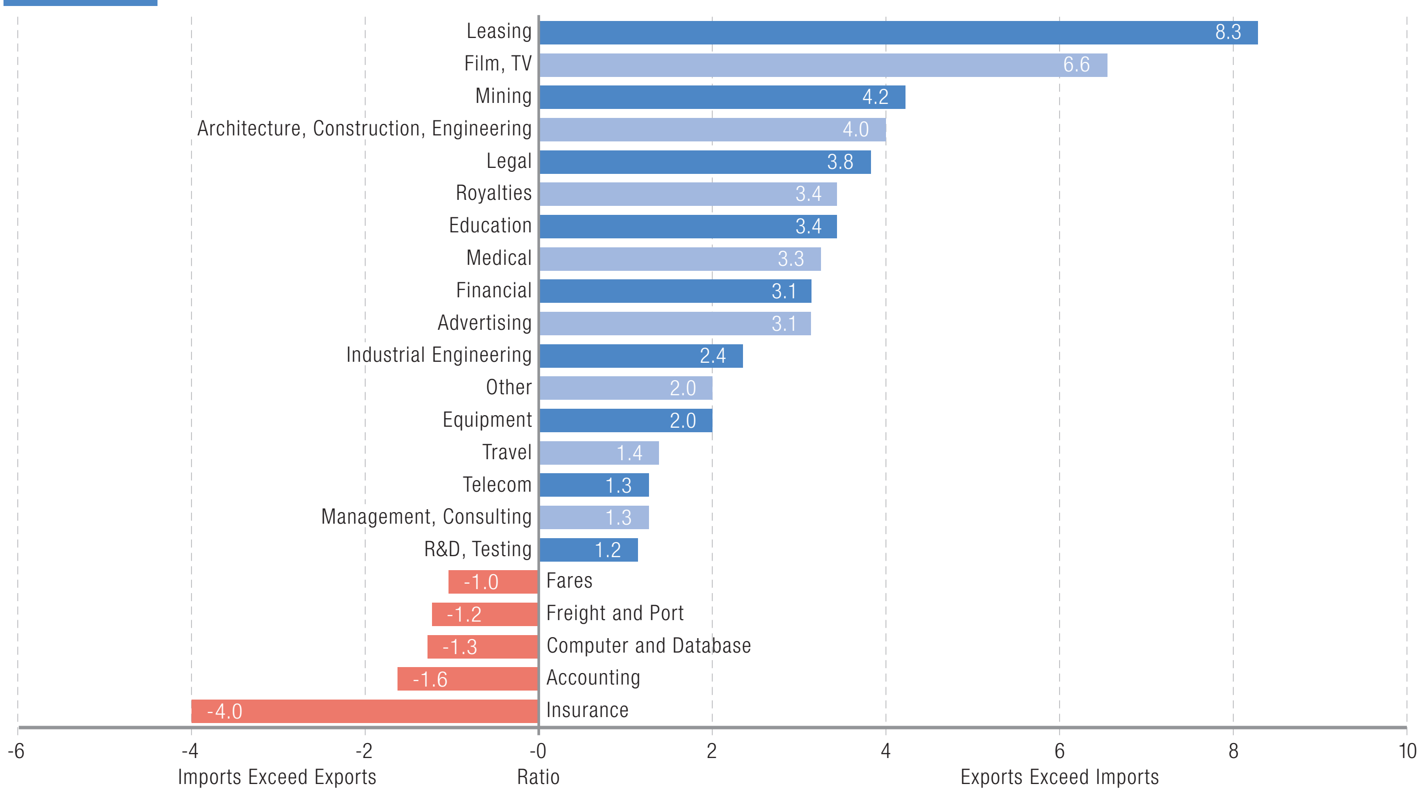
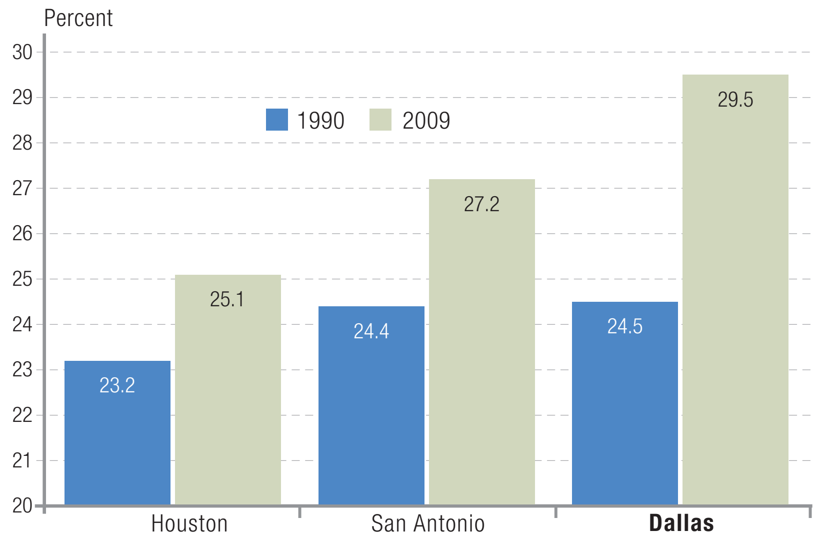


EXHIBIT 9

Primed for Globalization

The Dallas area has an edge in the share of private-sector employment in the three types of services that are easily exported—information, finance, and professional and business services.



Now, DFW services companies are taking the next step—the global arena.

industries highlight a key difference among DFW, Houston and San Antonio. In 1990, the three cities all had slightly less than a quarter of their private employment in information, finance, and professional and business services. Since then, DFW has added 5 percentage points, well above San Antonio's gain of 2.8 points and Houston's 1.9 points *(Exhibit 9)*.

What's more, the Dallas side of the metropolitan area, which includes Plano and Irving, exceeds the national norm in employment in a half-dozen key service industries. According to location quotients calculated by the Dallas Fed, Dallas' concentration of jobs is 60 percent higher than the U.S. in both information and finance and insurance. The area also shows strength in professional and business services.

By and large, these match the kinds of services that show up in national export statistics, suggesting the Dallas-side cities have the necessary skills to exploit the boom in services trade. The same strengths don't show up on the Fort Worth–Arlington side of the Metroplex.

DFW companies are finding their niche in global services—for example, American Airlines, Alliance Data and Blockbuster among the big companies. Law firms have stretched overseas with their clients, opening offices in Dubai, Moscow and dozens of other cities.

Smaller DFW companies are also going global. In the last 10 years Laguarda.Low, a Dallas firm, has worked on more than 300 projects in 25 countries, ranging from Portugal and Poland to India and China. Six-person Burada Inc. is a top-ranked software developer with projects in Spain and the United Kingdom, employing workers in Russia and Canada—all run out of a home office in Wiley, just east of Plano.

How to Keep It Going

The Dallas-Fort Worth area doesn't face the daunting burdens of a St. Louis or a Cleveland. Those cities' challenge lies in reversing long-term economic declines. Now at the top of its game, DFW needs to make sure it retains—and, if possible, enhances—the advantages that attract new residents, new jobs and new employers.

We already know how to keep a good thing going. It starts with embracing economic freedom. Keep taxes low and government small. Shun unions. Let new jobs and industries rise to replace those heading into decline.

Key elements of economic freedom lie beyond DFW's direct control. Tax, labor and trade policies are decided in Austin and Washington, D.C. These policies have a direct bearing on economic freedom, and it's incumbent on DFW business and political leaders

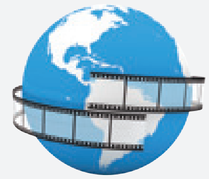
Seven Rules for Exporting Services

Many companies in DFW and elsewhere are already doing well selling services overseas. What makes them so successful?

1 They didn't assume their services couldn't be exported. Today's technologies allow us to do things that were unthinkable just a decade ago.

2 They looked for foreign growth. China and India have been America's fastest growing services markets. Their economies have been expanding rapidly in this decade, even during recession in America.

3 They didn't buy into the myth of anti-Americanism. Foreign consumers are fascinated by U.S.products and consumerism. The United States took eight of the top 10 spots in the Interbrand survey of best global brands in 2009. Look at the 10 biggest budget Hollywood movies: Foreign box office receipts nearly doubled domestic revenues.



U.S. Movies Cash in Overseas

	Movie	Budget	US Gross	Foreign Gross
1	Pirates of the Caribbean: At World's End (2007)	$300,000,000	$309,420,425	$651,576,067
2	Spider-Man 3 (2007)	$258,000,000	$336,530,303	$554,341,323
3	Harry Potter and the Half-Blood Prince (2009)	$250,000,000	$301,959,197	$635,540,708
4	Avatar (2009)	$237,000,000	$742,844,322	$1,950,000,000
5	Superman Returns (2006)	$232,000,000	$200,120,000	$191,000,000
6	Quantum of Solace (2008)	$230,000,000	$169,368,427	$407,000,000
7	Pirates of the Caribbean: Dead Man's Chest (2006)	$225,000,000	$423,315,812	$642,344,000
8	The Chronicles of Narnia: Prince Caspian (2008)	$225,000,000	$141,621,490	$277,868,796
9	Transformers: Revenge of the Fallen (2009)	$210,000,000	$402,111,870	$434,185,358
10	King Kong (2005)	$207,000,000	$218,080,025	$332,437,332
	Total		$3,245,371,871	$6,076,293,584

4 They adapted services to the local market. Delivering Americana can only go so far. Every country has its own customs and tastes, and successful services exporters get to know what the customers want. Yum Brands! took localization to its ultimate—selling Chinese food to the Chinese.

5 They developed multinational labor resources. Local workers and expats can both be effective, but they can't replace a cadre of true globalists, steeped in the firm's corporate culture but flexible and worldly enough to do business in nearly any country.

6 They entered markets that don't yet have a home-grown infrastructure of sophisticated services. Texas law firms have been negotiating global energy deals for generations, so they're in great demand in the Middle East, ex-Soviet republics and elsewhere.

7 They didn't see services exports as a game only for big business. Among the Fortune 2000, the percentage of sales coming from abroad shows no correlation to company size. Many small businesses are going global right out of the chute.

to fight against bad policies in the state and national arenas.

Local policies matter, too. Economic freedom provides a great advantage to Dallas, but we should never forget that we compete within the state with Houston, Austin, San Antonio and other metropolitan areas that offer the same advantages.

Keeping a good thing going also entails committing to globalization by actively pursuing foreign business *(see box, page 18)*.

Back in the 1870s, Dallas got it right by hopping aboard the era's growth engine—the railroads. With each generation, DFW business leaders and workers have chased opportunity wherever it arose. This is no time to stop. The 21st century's engine of growth will be globalization.

Local, in-state and national business may be more convenient and less risky, but some of the best opportunities in upcoming decades will come from the emerging nations with a need for the kind of sophisticated services DFW can offer.

America's edge lies in the specialized services, which create jobs for well-educated workers. DFW's dynamic economy has attracted brainpower from the rest of the state, the nation and other parts of the world. However, North Texas could do more to develop home-grown talent, the graduates of North Texas colleges and universities going to work in offices just a short drive from their campuses.

Embracing economic freedom, committing to globalization and deepening our talent pool won't be easy. These actions require great effort and unleash forces that bring competition and constant change. But facing up to globalization makes us stronger and change revitalizes us. We mustn't shrink from the challenge. If we get it right on economic freedom, globalization and services, the ascension of DFW will continue for many generations.

W. Michael Cox is director of the William J. O'Neil Center for Global Markets and Freedom. Richard Alm is writer in residence at the Center.

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Notes and Data Sources

EXHIBIT 1

U.S. Census Bureau, various publications, notably Table 1. Rank by Population of the 100 Largest Urban Places, Listed Alphabetically by State: 1790-1990.

BOX, PAGE 3

Ninth Census of the United States, June 1, 1870, Volume 1, Table 3: Population of Civil Divisions Less Than Counties, pages 270-75.

PAGE 6

For more on Texas' business tax, see Jason L. Saving, "Will New Business Tax Dull Texas' Competitive Edge," Federal Reserve Bank of Dallas, *Southwest Economy*, March/April 2008.

EXHIBIT 2

The Fraser Institute. Economic Freedom of North America 2008 Annual Report, by Amela Karabegovic and Fred McMahon. The Fraser report documents the link between the economic freedom and higher incomes. Countries in the top 25 percent of the rankings had an average per capita income of $34,461 in 2007, compared to $15,416 for the second quartile, $7,205 for the third quartile and $4,039 for the bottom quartile. The United States ranks sixth in economic freedom. Its per capita income was well above the top-quintile average at $45,592.

EXHIBIT 3

Highest marginal income tax rate and highest corporate income tax rate: The Tax Foundation. Sales tax collected as a percent of gross state product (GSP), government consumption as a percentage of GSP, transfers and subsidies as a percent of GSP, government employment as a percent of total employment, union membership rate, and minimum relative to average wage: The Fraser Institute. Economic Freedom of North America 2008 Annual Report.

EXHIBIT 4

Federal Reserve Bank of Dallas. For the boundaries in each Federal Reserve District, see the Federal Reserve System map at http://www.federalreserve.gov/otherfrb.htm.

EXHIBIT 5

World Bank, World Development Indicators and United Nations Department of Economic and Social Affairs, World Population Prospects, Table A.1.

EXHIBITS 6 and 7

Thomson One Banker and company annual reports. The logos are registered trademarks of the companies and used by permission.

EXHIBIT 8

U.S. Department of Commerce, Bureau of Economic Analysis.

EXHIBIT 9

U.S. Department of Labor, Bureau of Labor Statistics.

BOX, PAGE 18

Nash Information Services, www.the-numbers.com, movie budget records.

2009 O'Neil Center Annual Report

design by wiswallmclaindesign

2009: The Year in Review

The O'Neil Center made significant strides in just its second year. W. Michael Cox became full-time director in May after ending a 25-year career at the Federal Reserve Bank of Dallas. Cox joined four holdovers on the center's faculty—SMU Cox dean Albert W. Niemi Jr., Michael Davis, Dwight R. Lee and Maria Minniti.

Collectively, they taught more than 700 students in 21 classes. They published more than 20 articles and gave more than 50 speeches, seminars and outside presentations. The news media turned to O'Neil faculty members' expertise on at least 110 occasions.

Cox wrote "From Teflon to Tarzan, the '30s Proved Capitalism Never Sleeps" for *Investor's Business Daily*," arguing that capitalism generates progress even in the worst of times. In a Federal Reserve Bank of Dallas *Economic Letter* titled "Labor Market Globalization in the Recession and Beyond," he and two co-authors found that virtual immigration held up better than physical immigration in the recent recession.

Television, radio and print reporters called on Davis for commentary on a range of topics—among them, DFW and national economic conditions, the car industry under duress, the Dallas Cowboys' business empire and health-care issues.

For the *Intercollegiate Review*, Lee wrote about how capitalism's benefits are often miscast as problems in "Nothing Fails Like the Success of Private Enterprise and Freedom." He presented a paper titled "Solving Problems in the Information Age by Destroying Vital Information" at the Association for Private Enterprise Education meeting in Guatemala City, Guatemala.

Minniti held a PhD workshop on entrepreneurship research that attracted 25 participants from 15 countries. She and a co-author analyzed data from 16 countries and published their findings in an *Economic Letters* article titled "Unemployment Benefits Crowd Out Nascent Entrepreneurial Activity." Minniti received an award for Outstanding Teaching in the MBA Program at SMU's Cox School of Business.

In October, the Center hosted its first conference. More than 300 executives and students gathered at SMU's Collins Center to explore "What Do Businesses Need to Succeed in Today's Competitive Global Economy?"

Cox presented his research on Dallas-Fort Worth's global opportunities, expanded into the essay in this annual report. Here are highlights from other presentations:

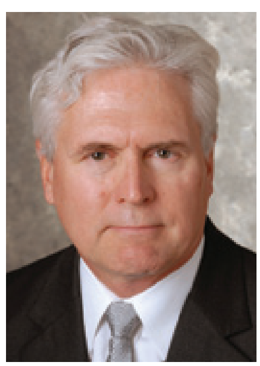
Richard Fisher, *president and CEO, The Federal Reserve Bank of Dallas.* Recent decades have been marked by rapid integration of the world economy, but some analysts see the sharp trade contraction in 2008 and 2009 as a signal of globalization's reversal. Fisher refuted this deglobalization thesis.

According to Fisher, there's no evidence of reversal in globalization's signature feature—the whittling away of gaps between home-market and world prices. He concluded that trade's decline came not from deglobalization but from plunging consumer demand, exacerbated by the drying up of trade credit in the wake of financial market turmoil.

Thomas J. Falk, chairman and CEO of Irving-based Kimberly-Clark, joined by two of the company's global executives— Stephen Shao, who runs the China operations, and Gustavo

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

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



Michael Davis, SMU Cox School of Business

Dwight R. Lee, William J. O'Neil Endowed Chair in Global Markets and Freedom

Maria Minniti, Professor and Bobby B. Lyle Chair in Entrepreneurship

Calvo Paz, the top manager in Russia and Eastern Europe: The Irving-based paper and consumer products producer operates more than 100 manufacturing facilities in 45 countries. Recruiting talented people remains one of the key challenges for global businesses—especially in fast-growing markets like China and Russia, Falk said.

Shao, a Chinese-born MIT graduate, said that offering opportunities was the best way to recruit China's young, ambitious college graduates. Calvo Paz, a native of Argentina, said the challenge in Russia was finding entrepreneurial gems among a population used to being told what to do.

"The consumer is at the center of everything we do," Falk said. In Russia, mothers tend to be young and fashionable, snapping up blue jean-themed Huggies diapers, Calvo Paz said. In China, mothers are older and willing to spend to buy the best for their one child, Shao said.

William J. O'Neil, ***publisher of Investor's Business Daily:*** The legendary investor and author said young companies drive American capitalism. Every one of the 27 cycles since 1880 was led by entrepreneurs or innovators who created something newer, faster, better or cheaper.

In this competitive society, O'Neil said, the new will rise to eclipse the old, so investors can't merely buy and hold. They will do much better looking for innovative companies about to break out.

O'Neil verified this proposition through a dozen or so historical examples, starting with Richmond & Danville railroad in 1885. He pointed to General Motors in 1915, IBM in 1926, RCA in 1927, Texas Instruments and Xerox in 1958, McDonald's in 1970, Microsoft in 1989, America Online in 1994, Qualcomm in 1999 and Google in 2004. O'Neil said it's just as important to watch for early warnings of distress—as with Enron in 2001.

Robert A. Lawson, ***co-author of the Economic Freedom of the World report:*** The Auburn University professor reviewed the latest results from the Fraser Institute's annual report that tracks economic freedom in 141 countries around the world. The United States ranked sixth in the world in economic freedom, trailing Hong Kong, Singapore, New Zealand, Switzerland and Chile.

Lawson said U.S. economic freedom rose for two decades but ebbed since 2000. Two factors are at work—growing government spending and weakening protection for property rights. He expects the country's scores to slip further when data for the past two years become available.

Scott Smith, ***vice president of staffing, AT&T Corp.; talent coach*** **Tina Sivinski,** ***founder,*** **Viveza;** ***and executive recruiter*** **Nancy Keene,** ***director, Stanton Chase:*** According to Scott, AT&T hires 25,000 to 30,000 workers a year. Over the next few years, he said, the biggest challenge will be filling the ranks of the "knowledge workers," loosely defined as college graduates. In 2012, the number of jobs that require a degree will exceed supply by 25 million.

Sivinski described talent as "the single biggest competitive advantage that we have"—a statement true for firms as well as individuals. She urged business leaders to adopt programs to identify and develop it.

In helping companies find the talent they need to prosper, Keene has seen a growing need for international expertise. Some companies want to bring international experience into their U.S. headquarters and others seek to beef up their capacity for rapid expansion overseas.

Richard K. Templeton, ***chairman, president and CEO of Texas Instruments Inc.:*** The electronics company's top executive ended the conference with a succinct message for companies, workers, cities, states and even universities: "The winners in the world will be those who embrace the global marketplace as an opportunity not as a threat."

TI serves as a model of the global company—88 percent of its revenue from foreign sales, 60 percent of its 25,000 employees overseas, manufacturing and sales in 30 countries. As a global company, TI benefits from being able to hire the best and brightest no matter their nationality and seize opportunities almost anywhere.

Being close to customers pays off, Templeton said. In the 1980s, TI's operation in Nice, France, helped an obscure lumber company from Norway develop a digital signal processor. Working with Nokia, TI got a start in a business where it now has 50 percent of the global market.

A decade ago, TI Japan took on the challenge of putting the power of a Sony Playstation into a cell phone, creating a toehold in the smart-phone market. Now, TI engineers are working on battery powered bicycles in Taiwan and solar-powered LED lighting in India. "When you're global, you get access to the best ideas," Templeton concluded.

To view conference videos or find more information about the O'Neil Center, go to: www.oneilcenter.org.

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