

CROSS COUNTRY

Blame Taxes for Baltimore's Rot

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Baltimore

If you've seen HBO's "The Wire," you know why those of us who live in Baltimore are often asked whether our city really is the hellhole it is portrayed to be on TV.

Our answer is, well, yes. Baltimore deserves the Third-World profile it has developed because it has expanses of crumbling, crime-riddled neighborhoods populated by low-income renters, an absent middle class, and just a few enclaves of high-income gentry near the Inner Harbor or in suburbs.

This wasn't what Baltimore looked like in the 1950s. Then it was a prosperous, blue-collar city of about 950,000 with a median family income 6.6% above the national average. Back in the good old days, Baltimore had a smaller percentage of residents living in poverty (22.7%) than the nation as a whole (27.8%), and a greater percentage of families (23.1%) earning a middle-class income of at least \$44,600 in today's dollars than the rest of the country (19.1%).

Today, the city has a population that is almost 50% smaller, and about 40% of families with children live at or near the federal poverty line. Among the country's 100 most populous cities, Baltimore ranks a shameful 87th on median household income.

How did this happen?

Most people think of cities as dense concentrations of people. They are that, of course. But they are also dense concentrations of capital – homes, offices, factories, theaters and roads. All of these assets are attractive to people because, when they are in close proximity to each other, they offer the chance of a more prosperous life.

The problem is that once capital is built, it can become a target for tax-and-spend politicians who bank on the fact that physical capital will continue to draw people, even as it is taxed more heavily. This is what has happened in Baltimore. The city has waged a war on capital for more than 50 years, raising property taxes an astonishing 21 times from 1950 to 1985.

But what politicians don't seem to understand is that the target may be degraded or destroyed in the process. There are now at least 30,000 housing units in Baltimore that are abandoned and waiting to be demolished, while even old, upper-crust neighborhoods now have a seedy look. Property taxes are so high – as well as the strong likelihood they will soar even higher in the future – that even maintenance, no less capital improvements, are a losing proposition. Renovations or upgrades may add less value to a house than it will cost in taxes on that house with a higher assessed value.

Politicians, in short, reason that because physical capital cannot typically be picked up and moved, it is immutable. Wrong. It depreciates. Fail to replenish or improve it, and it decays to uselessness.

Moreover, while physical capital may not be mobile, financial and human capital are. Property tax rates in Baltimore County (outside the city) are less than half of those inside the city (1.1% versus 2.268%). The suburbs are thriving even with the center city decaying.

In the 1990s, private-sector employment shrank 12.7% (a loss of 46,800 jobs) in Baltimore. From 2000 to 2007 it shrank again, this time by 10.4% (33,600 jobs). By contrast, employment in the rest of the metro area grew by 25.1% in the 1990s, and by another 13.9% since 2000.

To the extent that city officials recognize the problem, they seem to confuse symptoms with the root cause of the economy's disease. For them, poverty, street crime or bad schools are the problem. Their solution is always more social spending and still-higher taxes, together with targeted tax breaks and subsidies aimed at bringing "big footprint" development projects downtown. And because the city has managed to entice developers to build a few large projects (the National Aquarium, two stadiums, several office towers, upscale hotels and pricey waterfront condos), the champions of public redevelopment argue that the city is on the right track.

True enough, the ability to hand out subsidies gives officials great power. But it also gives them a reason, and incentive, to dismiss the common sense that if tax breaks for the well-connected are a good idea, lower tax rates across the board would lead to broad-based redevelopment.

The person best positioned to put an end to the city's war on capital is Democratic Mayor Sheila Dixon. Over the past year she even hinted at making tax reform a priority.

In December, a commission appointed by Ms. Dixon concluded that the city should immediately cut its property tax rate to 2.02% and, within a few years, reduce it further to 1.614%. That isn't going to happen, however. Her budget, approved last month, raised spending 11% and reneged on a promise made by Gov. Martin O'Malley when he was still mayor in 2006 to cut property taxes by 0.02% to 2.248%.

But the issue of property taxes and development is not yet over. The state prosecutor is currently looking into allegations that Ms. Dixon took gifts from property developers while giving special tax breaks.

The evergreen rationale for high property-tax rates is that a city can't afford low ones. When she announced her spending plan for the year, Ms. Dixon insisted that "people think there's fat within the budget, [but] it's very lean."

Left unsaid: The city spends 61% more per person than the surrounding county. And in reality, cutting property taxes would only temporarily cut property tax receipts. Making Baltimore friendly to capital investment would unlock a flood of new (unsubsidized) investment that would restore revenues and facilitate an organic, widespread renewal of the city.

What's needed is the political will to tighten the bureaucracy's belt in the near term, and the ingenuity to create a fiscal bridge to a recapitalized, healthier city. So far, Baltimore is sticking with its "capital punishment" policies and it's killing the city.

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