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## Broadband won't drive regional business growth

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*Broadband won't drive regional business growth, despite claims to the contrary, writes **John Daley**.*

Expectations for the NBN are high. But will it drive a boom in regional employment? Or are better coffee shops more important?

There is a widespread belief that better broadband will drive regional growth. But the evidence suggests that, if anything, broadband will increase the incentives for businesses to set up in large cities rather than in the regions.

If we are going to spend \$43bn because it will promote regional employment growth, we should understand why cities attract businesses, and why the NBN will make a difference.

Why would businesses ever set up in cities where the rents are higher and it takes longer to get to work?

By locating many people together, it is easier for companies to find specialised workers. If this were the key advantage of cities, businesses might be able to locate anywhere and construct a "virtual" workforce of specialists located around the country, given good enough communications technology.

But cities have wider economic appeal than a mass of willing workers. The economics literature suggests that businesses are attracted to cities mainly to be near many other specialised companies they can cooperate with as suppliers, customers or partners.<sup>1</sup>

Does this business-to-business cooperation depend on face-to-face communication, or could high-quality video interaction through broadband make a difference?

The earliest adopters of broadband – those in the IT industry itself – show no sign that better communications technology allows businesses to disperse. IT-dependent businesses are in fact *more* likely to locate near each other than businesses in other industries.<sup>2</sup>

One of the best studies about how people actually interact surveyed 6,000 workers in France.<sup>3</sup> It found that workers spend the same amount of time communicating with co-workers, whether they work in large cities or in regional areas.<sup>4</sup> However businesses in cities, rather than regions, communicate with a greater number of *other* businesses, more often.<sup>5</sup> This is true even for workers with similar levels of education, in similar industries, and in similar sized businesses.<sup>6</sup> This fits with the economic theory that businesses are prepared to pay high city prices in return for the opportunity to identify and work with many other specialised businesses.

Perhaps companies could work with other specialised businesses remotely if they had better communications. If this were so, one would expect regional and small city firms to use telephone and email more, as a substitute for not seeing customers and suppliers in person. But the evidence suggests that *city* workers use phone and email more. Workers in cities with over 2 million people are almost twice as likely to use phone and email as workers in cities with less than 100,000 people.<sup>7</sup> Again, these results are true even for workers with similar levels of education, in similar industries, and in similar sized businesses.<sup>8</sup> Even small businesses are more likely to have more extensive contacts with other businesses if they locate in cities rather than regions.

A likely interpretation is that city firms establish contact with other businesses more often – usually in person – and then follow up on the greater number of contacts through phone and email. This fits with the evidence that workers who meet more often face-to-face *also* tend to use telephones more.<sup>9</sup>

It is unlikely that broadband is going to change this pattern radically. How confident would you be about taking on a new supplier for a complex service if you had never met them in person? And if you provide a niche service to many customers, would you be prepared to give up the opportunity to meet potential customers at casual functions in person?

If anything, broadband may increase the advantage of large cities as it becomes even more efficient to make the most of relationships that have been formed in person.

High quality broadband has other advantages. It allows the relocation to regional areas of business operations that depend on high quality broadband, but not on interactions with many other businesses – a call centre, for example. However, this is likely to be a minority – most businesses shell out city prices to be near other businesses, not just a 10Mb connection.

The NBN may have other justifications. In today's society broadband is increasingly a basic service essential to social inclusion. Particularly in regional areas it may provide home-based educational and health services that are not otherwise accessible. Reasonable broadband should be seen as a utility like electricity, with governments responsible for ensuring that a service is available. But just as electricity supply is interrupted more often in regional areas, regional broadband is likely to be lower quality, reflecting that it is more expensive to deliver.

Proponents of the NBN will need to argue that its cost is justified in these other ways. Given the evidence, they cannot claim that it is likely to spur a large number of businesses to set up in regional areas. Beyond the internet – even beyond coffee shops – cities offer some advantages to businesses that regions struggle to match.

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<sup>1</sup> See Glaeser E, "Cities Do it Better" *New York Times* (27 April 2010); <http://economix.blogs.nytimes.com/2010/04/27/cities-do-it-better/>; Glaeser E (ed), *Agglomeration Economics*, NBER (2010).

<sup>2</sup> Kolko J, "Agglomeration and Co-Agglomeration of Services Industries" *Public Policy Institute of California* (2007) [http://mpr.ub.uni-muenchen.de/3362/1/MPRA\\_paper\\_3362.pdf](http://mpr.ub.uni-muenchen.de/3362/1/MPRA_paper_3362.pdf) 24

<sup>3</sup> Charlot S and Duranton G, "Cities and Workplace Communication: Some Quantitative French Evidence" *Urban Studies* Vol 43 (2006) 1365

<sup>4</sup> Charlot & Duranton (2006) 1374

<sup>5</sup> Charlot & Duranton (2006) 1374-5

<sup>6</sup> Charlot & Duranton (2006) 1377-9

<sup>7</sup> Charlot & Duranton (2006) 1376

<sup>8</sup> Charlot & Duranton (2006) 1380

<sup>9</sup> Charlot & Duranton (2006) 1385