Hawaii Competitiveness:
Creating a State Economic Strategy

For further material on regional competitiveness and clusters: www.isc.hbs.edu/econ-clusters.htm
For state economic profiles: www.isc.hbs.edu/econ-statesregions.htm

Professor Michael E. Porter
Harvard Business School

March 20, 2012
The Economic Challenge for Governors in 2012

Achieving Fiscal Stability

Enhancing State Competitiveness
What is Competitiveness?

- Competitiveness is the **productivity** with which a state utilizes its human, capital, and natural endowments to create value.

- Productivity determines **wages**, **jobs**, and the **standard of living**.

- It is not **what** fields a state competes in that determines its prosperity, but **how productively** it competes.
Where Does Productivity Come From?

Businesses and government play **different but interrelated roles** in creating a productive economy

- Only **businesses** can create **jobs** and **wealth**
- **States** compete to offer the **most productive environment** for business
Agenda

1. How is your state doing? State Performance Scorecard
2. Why? Explaining your state’s performance, strengths, and weaknesses
3. Where to go from here? Action Steps
### Hawaii Performance Scorecard

#### Prosperity
*GDP per Capita, 2000-2010*

<table>
<thead>
<tr>
<th>Start Position</th>
<th>Trend</th>
<th>Current Position</th>
</tr>
</thead>
<tbody>
<tr>
<td>16</td>
<td>23</td>
<td>19 (-3)</td>
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</table>

#### Wages
*Average Private Wage, 1998-2009*

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<tr>
<td>28</td>
<td>45</td>
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#### Job Creation

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<td>36 (-8)</td>
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#### Labor Mobilization
*Proportion of Working Age Population in the Workforce, 2000-2010*

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#### Labor Productivity
*GDP per Workforce Participant, 2000-2010*

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#### New Business Formation

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#### Innovation
*Patents per Employee, 2000-2010*

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#### Cluster Strength
*Employment in Strong Clusters, 1998-2009*

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#### Leading Clusters
*by employment size, 2009* (national rank)

- Hospitality and Tourism (12)
- Transportation and Logistics (33)
- Jewelry and Precious Metals (19)
- #NA
- #NA
Comparative State Prosperity Performance
2000 - 2010

Source: BEA. Notes: GDP in real 2005 dollars. Growth rate is calculated as compound annual growth rate.
Comparative State Labor Mobilization Performance
1999-2010

High Labor Force Participation and Participation rising versus U.S.

High but declining versus U.S.

Low and declining versus U.S.

Low but rising versus U.S.

Notes: Source BLS.
Comparative State Labor Force Productivity Performance
2000-2010

Real Growth in Gross Domestic Product per Labor Force Participant, 2000-2010

Sources: BEA, BLS. Notes: GDP in real 2005 dollars. Growth rate is calculated as compound annual growth rate.
Comparative State Employee Productivity Performance
2000-2010

Gross Domestic Product per Employed Worker, 2010

Sources: BEA, BLS. Notes: GDP in real 2005 dollars. Growth rate is calculated as compound annual growth rate.

High but declining versus U.S.

Highly productive and productivity rising versus U.S.

U.S. GDP per Employed Worker
Real Growth: 1.42%

Low and declining versus U.S.

Low but rising versus U.S.

Real Growth in Gross Domestic Product per Employed Worker, 2000-2010

$60,000
$70,000
$80,000
$90,000
$100,000
$110,000
$120,000
$130,000
$140,000
$150,000

0.0% 0.5% 1.0% 1.5% 2.0% 2.5% 3.0% 3.5%
Comparative State Innovation Performance
2000 - 2010

High and declining innovation

U.S. average Patents per 10,000 Employees: 7.77

High and improving innovation rate versus U.S.

Low and improving innovation

Growth Rate of Patents per 10,000 Workers, 2000 to 2010


2012 State Competitiveness – Rich Bryden
Why?
What Drives State Productivity?

1. Quality of the Overall Business Environment

2. Cluster Development

3. Policy Coordination among Multiple Levels of Geography/Government
Why?
What Drives State Productivity?

1. Quality of the Overall Business Environment

2. Cluster Development

3. Policy Coordination among Multiple Levels of Geography/Government
Quality of the Overall Business Environment

Context for Firm Strategy and Rivalry

Rules and incentives that encourage local competition, investment and productivity
- e.g., tax policy that encourages investment and R&D
- Flexible labor policies
- Intellectual property protection
- Antitrust enforcement

Factor (Input) Conditions

Access to high quality business inputs
- Human resources
- Capital access
- Physical infrastructure
- Administrative processes (e.g., permitting, regulatory efficiency)
- Scientific and technological infrastructure

Demand Conditions

Sophisticated and demanding local needs and customers
- e.g., Strict quality, safety, and environmental standards
- Consumer protection laws
- Government procurement of advanced technology
- Early demand for products and services

Related and Supporting Industries

Local availability of suppliers and supporting industries

• Many things matter for competitiveness
• Economic development is the process of improving the business environment to enable companies to compete in increasingly sophisticated ways
Improving the Business Environment
Common Action Items

1. Simplify and speed up regulation and permitting

2. Reduce unnecessary costs of doing business

3. Establish training programs that are aligned with the needs of the state’s businesses

4. Focus infrastructure investments on the most leveraged areas for productivity and economic growth

5. Design all policies to support emerging growth companies

6. Protect and enhance the state’s higher education and research institutions

7. Relentlessly improve the public education system, the essential foundation for productivity in the long run
Why?
What Drives State Productivity?

1. Quality of the Overall Business Environment
2. Cluster Development
3. Policy Coordination among Multiple Levels of Geography/Government
What is a Cluster?

A geographically concentrated group of interconnected companies and associated institutions in a particular field.

**Traded Clusters**
- Compete to serve **national** and **international** markets
- Can locate anywhere
- 30% of employment

**Local Clusters**
- Serve almost exclusively the **local** market
- Not directly exposed to cross-regional competition
- 70% of employment
Example: Massachusetts Life Sciences Cluster

1. Health and Beauty Products
2. Surgical Instruments and Suppliers
3. Medical Equipment
4. Dental Instruments and Suppliers
5. Ophthalmic Goods
6. Diagnostic Substances
7. Containers

Primary Nodes:
- Biological Products
- Biopharmaceutical Products
- Teaching and Specialized Hospitals
- Research Organizations
- Educational Institutions

Cluster Organizations:
- MassMedic, MassBio, others
- Specialized Business Services
- Banking, Accounting, Legal
- Specialized Risk Capital
- VC Firms, Angel Networks
- Specialized Research Service Providers
- Laboratory, Clinical Testing

Specialized Areas:
- Analytical Instruments Cluster
- Educational Institutions
  Harvard, MIT, Tufts, Boston University, UMass
Example: Houston Oil and Gas Cluster

**Upstream**

- **Oil & Natural Gas Exploration & Development**
  - (e.g., Oil Field Chemicals, Drilling Rigs, Drill Tools)
- **Oil & Natural Gas Completion & Production**
  - (e.g., Drilling Consultants, Reservoir Services, Laboratory Analysis)
- **Equipment Suppliers**
  - (e.g., Oil Field Chemicals, Drilling Rigs, Drill Tools)
- **Specialized Technology Services**
  - (e.g., Surveying, Mud Logging, Maintenance Services)
- **Subcontractors**
  - (e.g., Surveying, Mud Logging, Maintenance Services)
- **Specialized Institutions**
  - (e.g., Academic Institutions, Training Centers, Industry Associations)

**Downstream**

- **Oil Transportation**
- **Oil Trading**
- **Oil Refining**
- **Oil Distribution**
- **Oil Wholesale Marketing**
- **Oil Retail Marketing**
- **Gas Gathering**
- **Gas Processing**
- **Gas Trading**
- **Gas Transmission**
- **Gas Distribution**
- **Gas Marketing**
- **Oilfield Services/Engineering & Contracting Firms**
- **Business Services**
  - (e.g., MIS Services, Technology Licenses, Risk Management)
Strong Clusters Drive Regional Performance

- Specialization in **strong clusters**
- **Breadth** of industries within each cluster
- Strength in **related clusters**
- Presence of a region’s clusters in **neighboring regions**

- **Job** growth
- Higher **wages**
- Higher **patenting** rates
- Greater **new business** formation, growth and survival

*On average, cluster strength is much more important (78.1%) than cluster mix (21.9%) in driving regional performance in the U.S.*

Clusters and Economic Diversification

Note: Clusters with overlapping borders or identical shading have at least 20% overlap (by number of industries) in both directions.
The Evolution of Regional Economies
San Diego

- Climate and Geography
- U.S. Military
- Hospitality and Tourism
- Transportation and Logistics
- Power Generation
- Aerospace Vehicles and Defense
- Communications Equipment
- Analytical Instruments
- Education and Knowledge Creation
- Information Technology
- Medical Devices
- Biotech / Pharmaceuticals
- Bioscience Research Centers

Traded Cluster Composition of the Hawaii Economy

Overall change in the Hawaii Share of US Traded Employment: 0.02%

Hawaii national employment share, 2009

Change in Hawaii share of National Employment, 1998 to 2009

Hawaii Overall Share of US Traded Employment: 0.38%


Employees 10,500 = 0.4%

Footnote:

- Employees
- 0.0%
- 0.5%
- 1.0%
- 1.5%
- 2.0%
- 2.5%
Traded Cluster Composition of the Hawaii Economy (continued)

Hawaii national employment share, 2009


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Hawaii Job Creation in Traded Clusters
1998 to 2009

Job Creation, 1998 to 2009:
-2,000
-1,000
0
1,000
2,000
3,000
4,000
5,000
6,000
7,000

Business Services
Education and Knowledge Creation
Information Technology
Distribution Services
Processed Food
Plastics
Entertainment
Forest Products
Publishing and Printing
Medical Devices
Textiles
Oil and Gas Products and Services
Renewable Energy
Biopharmaceuticals
Lighting and Electrical Equipment
Construction Materials
Power Generation and Transmission
Motor Driven Products
Prefabricated Enclosures
Production Technology
Medical Devices
Biopharmaceuticals
Lighting and Electrical Equipment
Construction Materials
Power Generation and Transmission
Motor Driven Products
Prefabricated Enclosures
Production Technology

Net traded job creation, 1998 to 2009:
+2,565

Indicates expected job creation given national cluster growth.*

* Percent change in national benchmark times starting regional employment. Overall traded job creation in the state, if it matched national benchmarks, would be 13,285.
Hawaii Wages in Traded Clusters vs. National Benchmarks

Hawaii average traded wage: $39,052

U.S. average traded wage: $56,906

Productivity Depends on How a State Competes, Not What Industries It Competes In

<table>
<thead>
<tr>
<th>State</th>
<th>State Traded Wage versus National Average</th>
<th>Cluster Mix Effect</th>
<th>Relative Cluster Wage Effect</th>
</tr>
</thead>
<tbody>
<tr>
<td>Connecticut</td>
<td>+27,171</td>
<td>7,028</td>
<td>20,142</td>
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<tr>
<td>New York</td>
<td>+24,102</td>
<td>3,628</td>
<td>20,474</td>
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<td>Massachusetts</td>
<td>+16,169</td>
<td>4,391</td>
<td>11,778</td>
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<tr>
<td>New Jersey</td>
<td>+13,535</td>
<td>3,761</td>
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<td>California</td>
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<td>Rhode Island</td>
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<td>Missouri</td>
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<td>Alabama</td>
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<td>Florida</td>
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<td>Wisconsin</td>
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<td>Nebraska</td>
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<td>Utah</td>
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<tr>
<td>Tennessee</td>
<td>-12,172</td>
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<tr>
<td>Indiana</td>
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<tr>
<td>Vermont</td>
<td>-13,368</td>
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<tr>
<td>Nevada</td>
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<td>North Dakota</td>
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<td>1,004</td>
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<td>South Carolina</td>
<td>-15,276</td>
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<tr>
<td>Arkansas</td>
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<td>-4,560</td>
<td>-10,818</td>
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<td>-12,555</td>
<td>-3,487</td>
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<tr>
<td>New Mexico</td>
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<td>-288</td>
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<tr>
<td>Kentucky</td>
<td>-16,215</td>
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<tr>
<td>Maine</td>
<td>-16,379</td>
<td>-968</td>
<td>-15,412</td>
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<tr>
<td>Iowa</td>
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<td>Idaho</td>
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On average, cluster strength is much more important (78.1%) than cluster mix (21.9%) in driving regional performance in the U.S.

LQ, or Location Quotient, measures the state’s share in cluster employment relative to its overall share of U.S. employment. An LQ > 1 indicates an above average employment share in a cluster.
## Hawaii Performance Scorecard

### Prosperity

**GDP per Capita, 2000-2010**

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### Labor Productivity

**GDP per Workforce Participant, 2000-2010**

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**Patents per Employee, 2000-2010**

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### Leading Clusters

**by employment size, 2009 (national rank)**

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- Transportation and Logistics (33)
- Jewelry and Precious Metals (19)
- #NA
- #NA

### State Rank

- 1-10: 21-30
- 31-40
- 11-20
- 41-50

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Cluster Development
Common Action Items

1. Build on the state’s **existing and emerging clusters** rather than chase “hot” fields

2. Pursue economic diversification **within clusters** and **across related clusters**

3. Create a private sector-led **cluster upgrading program** with matching support for participating private sector cluster organizations
   - Government should **listen** and **remove obstacles** to cluster improvement

4. **Align** other state economic policies and programs with clusters

Clusters provide a framework for organizing the implementation of many public policies and public investments to achieve greater effectiveness.
Why?
What Drives State Productivity?

1. Quality of the Overall Business Environment
2. Cluster Development
3. Policy Coordination among Multiple Levels of Geography/Government
Geographic and Governmental Influences on Productivity

- Nation
- State
- Metropolitan Areas
- Rural Regions
- Neighboring State
- Neighboring State
The economies of states are often an aggregation of distinct economic areas with differing circumstances.

**Wage Performance in Hawaii Metropolitan Areas**

Source: Census CBP, authors' analysis. Note: “Bubble” size in chart is proportional to employment in 2009.
Employment Performance in Hawaii Metropolitan Areas

U.S. Growth Rate of Employment: 0.52%

Hawaii Growth Rate of Employment: 1.46%

U.S. Average Private Wage: $42,403
Hawaii Average Private Wage: $36,328

Honolulu MSA
Rest of State

Source: Census CBP, authors' analysis. Note: “Bubble” size in chart is proportional to employment in 2009.
1. **Influence** and **access** federal policies and programs

2. Work with each metro area to develop a **prioritized strategic agenda**

3. **Connect** rural regions with proximate urban areas

4. **Integrate** policies and infrastructure planning with neighbors
Agenda

1. How is your state doing?  State Performance Scorecard
2. Why?  Explaining your state’s performance, strengths, and weaknesses
3. Where to go from here?  Action Steps
Agenda

1. How is your state doing?  
State Performance Scorecard

2. Why?  
Explaining your state’s performance, strengths, and weaknesses

3. Where to go from here?  
Action Steps

Biggest Action Item of All
Create an Economic Strategy

• What is the **distinctive competitive position** of the state or region given its location, legacy, existing strengths, and potential strengths?
  – What unique value as a business location?
  – For what types of activities and clusters?

**Define the Value Proposition**

**Develop Unique Strengths**

• What **elements of the business environment** can be unique strengths relative to peers/neighbors?
• What **existing and emerging clusters** represent local strengths?

**Achieve and Maintain Parity with Peers**

• What **weaknesses** must be addressed to remove key constraints and achieve parity with peer locations?

• Economic strategy requires **setting priorities** and **moving beyond** long lists of separate recommendations.
How Should States Compete for Investment?

Tactical (Zero Sum Competition)

- Focus on attracting **new** investments
- Compete for **every** plant
- Offer **generalized** tax breaks
- Provide **subsidies** to lower / offset business costs
- Every city and sub-region **for itself**
- **Government** drives investment attraction

Strategic (Positive Sum Competition)

- Also support greater local investment by **existing** companies
- Reinforce areas of **specialization** and emerging cluster strength
- Provide state support for training, infrastructure, and institutions with **enduring benefits**
- Improve the **efficiency of doing business**
- Harness efficiencies and coordination **across jurisdictions**, especially with neighbors
- **Government** and the private sector **collaborate** to build cluster strength
Harnessing the New Process of Economic Development

Competitiveness is the result of both **top-down** and **bottom-up processes** in which many companies and institutions take responsibility.

**Old Model**
- **Government** drives economic development through policy decisions and incentives

**New Model**
- Economic development is a **collaborative process** involving government at multiple levels, companies, teaching and research institutions, and private sector organizations
Example: Organizing for Economic Development

South Carolina Council on Competitiveness

Executive Committee

Coordinating Staff

Cluster Committees

- Automotive
- Hydrogen / Fuel Cells
- Textiles
- Apparel
- Agriculture
- Travel and Tourism

Task Forces

- Cluster Activation
- Research / Investment
- Distressed / Disadvan. Areas
- Measuring Progress
- Education / Workforce
- Start-ups / Local Firms

Chaired by a business leader and reporting to the governor
Convenes working groups, provides direction and strength, holds working groups accountable

Effective economic policy also requires **coordination within government**
Summary

• The goal of economic strategy is to enhance **productivity**. This is the only way to create jobs, high income, and wealth in the long run

• Improving **productivity** and **innovation** must be the guiding principles for every state policy choice

• Improving productivity does not require new public resources, but using existing resources better

• Improving productivity demands that governors **mobilize the private sector**, not rely on government alone

• Economic strategy is non-partisan and about getting **results**
Next Steps

1. Reach out to your team

2. Reach out to the business community


The prosperity of the U.S. economy will depend more on the success of states in improving competitiveness than what happens in Washington.