Kansas 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

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
<table>
<thead>
<tr>
<th>Category</th>
<th>Start Position</th>
<th>Trend</th>
<th>Current Position</th>
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</thead>
<tbody>
<tr>
<td><strong>Prosperity</strong> - GDP per Capita, 2000-2010</td>
<td>30</td>
<td>19</td>
<td>26 +4</td>
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<td><strong>Wages</strong> - Average Private Wage, 1998-2009</td>
<td>30</td>
<td>28</td>
<td>31 -1</td>
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<td><strong>Labor Mobilization</strong> - Proportion of Working Age Population in the Workforce, 2000-2010</td>
<td>14</td>
<td>5</td>
<td>7 +7</td>
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<tr>
<td><strong>Labor Productivity</strong> - GDP per Workforce Participant, 2000-2010</td>
<td>30</td>
<td>27</td>
<td>31 -1</td>
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<tr>
<td><strong>Innovation</strong> - Patents per Employee, 2000-2010</td>
<td>33</td>
<td>7</td>
<td>30 +3</td>
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<td><strong>Cluster Strength</strong> - Employment in Strong Clusters, 1998-2009</td>
<td>33</td>
<td>18</td>
<td>27 +6</td>
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<tr>
<td><strong>Leading Clusters</strong> by employment size, 2009 (national rank)</td>
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<td>- Processed Food (15)</td>
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<td>- Heavy Machinery (10)</td>
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</table>
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.

U.S. Labor Force Participation Rate: 64.7%

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

Highly productive and productivity rising versus U.S.

High but declining 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

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

Gross Domestic Product per Employed Worker, 2010

U.S. GDP per Employed Worker: $94,315

$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

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

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

High and declining innovation

High and improving innovation rate versus U.S.

Low and declining innovation

Low and improving innovation

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

- Health and Beauty Products
- Surgical Instruments and Suppliers
- Medical Equipment
- Dental Instruments and Suppliers
- Ophthalmic Goods
- Diagnostic Substances
- Containers

Teaching and Specialized Hospitals

Biological Products

Biopharmaceutical Products

Research Organizations

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

Educational Institutions: Harvard, MIT, Tufts, Boston University, UMass

Analytical Instruments Cluster
Example: Houston Oil and Gas Cluster

Upstream

Oil & Natural Gas Exploration & Development

Equipment Suppliers
(e.g., Oil Field Chemicals, Drilling Rigs, Drill Tools)

Specialized Technology Services
(e.g., Drilling Consultants, Reservoir Services, Laboratory Analysis)

Subcontractors
(e.g., Surveying, Mud Logging, Maintenance Services)

Oil & Natural Gas Completion & Production

Specialized Institutions
(e.g., Academic Institutions, Training Centers, Industry Associations)

Specialized Technology Services
(e.g., Drilling Consultants, Reservoir Services, Laboratory Analysis)

Subcontractors
(e.g., Surveying, Mud Logging, Maintenance Services)

Downstream

Oil Transportation

Gas Gathering

Oil Trading

Gas Processing

Oil Refining

Gas Transmission

Oil Distribution

Gas Trading

Gas Distribution

Gas Marketing

Oil Wholesale Marketing

Gas Marketing

Oil Retail Marketing

Business Services
(e.g., MIS Services, Technology Licenses, Risk Management)

Oilfield Services/Engineering & Contracting Firms
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

Bioscience Research Centers

Hospitality and Tourism
Transportation and Logistics
Power Generation
Communications Equipment
Analytical Instruments
Education and Knowledge Creation
Medical Devices
Information Technology
Biotech / Pharmaceuticals

Aerospace Vehicles and Defense

Sporting Equipment

Traded Cluster Composition of the Kansas Economy

Overall change in the Kansas Share of US Traded Employment: 0.06%

Aerospace Vehicles and Defense
(10.0%, +0.8%)

Processed Food

Heavy Machinery

Oil and Gas Products and Services

Publishing and Printing

Production Technology

Chemical Plastics

Metal Manufacturing

Power Generation and Transmission

Construction Materials

Agricultural Products

Textiles

Apparel

Sporting, Recreational and Children’s Goods

Motor Driven Products

Information Technology

(2.0%, 1.6%)

Aerospace Engines

Analytical Instruments

Aerospace Engines

Communication Equipment

Building Fixtures, Equipment and Services

Motor Driven Products

Analytical Instruments

Chemical Products

Motor Driven Products

Analytical Instruments

Metal Manufacturing

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2012 – State Competitiveness – Rich Bryden

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Traded Cluster Composition of the Kansas Economy (continued)

Overall change in the Kansas Share of US Traded Employment: 1.09%

Kansas Overall Share of US Traded Employment: 0.06%

Kansas Job Creation in Traded Clusters
1998 to 2009

Net traded job creation, 1998 to 2009: +8,149

* Percent change in national benchmark times starting regional employment. Overall traded job creation in the state, if it matched national benchmarks, would be −18,042.


Indicates expected job creation given national cluster growth.*
Kansas Wages in Traded Clusters vs. National Benchmarks

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>
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<tr>
<td>New York</td>
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</tbody>
</table>

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.
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<td>New Business Formation</td>
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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

Neighboring State <-> State <-> Neighboring State

Metropolitan Areas

Rural Regions
Defining the Appropriate Economic Regions

The economies of states are often an aggregation of distinct economic areas with differing circumstances.

Wage Performance in Kansas Metropolitan Areas

Growth Rate of Private Wages, 1998-2009

Kansas Growth Rate of Wages: 3.00%

U.S. Growth Rate of Wages: 3.01%

Kansas City MSA*

U.S. Average Private Wage: $42,403

Kansas Average Private Wage: $36,769

Average Private Wage, 2009

$46,000

$42,000

$38,000

$34,000

$30,000

$26,000

2.2%

2.4%

2.6%

2.8%

3.0%

3.2%

3.4%

*St. Joseph MSA*

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

Average Private Wage, 2009

- $24,000
- $28,000
- $32,000
- $36,000
- $40,000
- $44,000
- $48,000

Growth Rate of Private Employment, 1998-2009

-6.0% -5.0% -4.0% -3.0% -2.0% -1.0% 0.0% 1.0% 2.0% 3.0%

U.S. Average Private Wage: $42,403

Kansas Average Private Wage: $41,596

*St. Joseph MSA*

*Kansas portion only

Source: Census CBP, authors’ analysis. Note: “Bubble” size in chart is proportional to employment in 2009.
Geographic and Governmental Influences on Productivity

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

- Nation
- State
- Metropolitan Areas
- Rural Regions
- Neighboring State
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

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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

- 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.