New Hampshire Competitiveness: Creating a State Economic Strategy

Professor Michael E. Porter
Harvard Business School

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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
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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<tr>
<td><strong>Prosperity</strong></td>
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<td>GDP per Capita, 2000-2010</td>
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<td><strong>Wages</strong></td>
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<td>Average Private Wage, 1998-2009</td>
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<td><strong>Job Creation</strong></td>
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<td><strong>Labor Mobilization</strong></td>
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<td>Proportion of Working Age Population in the Workforce, 2000-2010</td>
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<td><strong>Labor Productivity</strong></td>
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<td>GDP per Workforce Participant, 2000-2010</td>
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<td><strong>New Business Formation</strong></td>
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<td><strong>Innovation</strong></td>
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<td>Patents per Employee, 2000-2010</td>
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<td><strong>Cluster Strength</strong></td>
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<td><strong>Leading Clusters</strong></td>
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<td>by employment size, 2009 (national rank)</td>
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<tr>
<td>Information Technology (28)</td>
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State Rank: 1-10, 11-20, 31-40, 41-50
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 but declining versus U.S.

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

Change in Labor Force Participation Rate: 64.7%

Low and declining versus U.S.

Low but rising versus U.S.

Change in Proportion of Working Age Population in the Workforce, 1999-2010

Notes: Source BLS.

50% 55% 60% 65% 70% 75%

-7% -6% -5% -4% -3% -2% -1% 0% 1% 2%


50% 55% 60% 65% 70% 75%

-7% -6% -5% -4% -3% -2% -1% 0% 1% 2%

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.

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

High but declining versus U.S.

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.
Comparative State Innovation Performance
2000 - 2010

High and declining innovation

High and improving innovation rate versus U.S.

Low and improving innovation

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

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


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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

Factors (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

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

Context for Firm Strategy and Rivalry

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**

- **Analytical Instruments Cluster**

- **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
Example: Houston Oil and Gas Cluster

Upstream

- Oil & Natural Gas Exploration & Development
- Oil & Natural Gas Completion & Production

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

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

Specialized Institutions
(e.g., Academic Institutions, Training Centers, Industry Associations)
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
  - Hospitality and Tourism
- U.S. Military
  - Aerospace Vehicles and Defense
  - Transportation and Logistics
  - Power Generation
  - Communications Equipment
  - Information Technology
  - Education and Knowledge Creation
  - Medical Devices
  - Biotech / Pharmaceuticals

Bioscience Research Centers

Traded Cluster Composition of the New Hampshire Economy

Change in New Hampshire share of National Employment, 1998 to 2009

Overall change in the New Hampshire Share of US Traded Employment: -0.02%

New Hampshire national employment share, 2009

Traded Cluster Composition of the New Hampshire Economy (continued)

Overall change in the New Hampshire Share of US Traded Employment: -0.02%

New Hampshire Overall Share of US Traded Employment: 0.55%

Change in New Hampshire share of National Employment, 1998 to 2009

-0.10% -0.05% 0.00% 0.05% 0.10%

Employees 4,000 =

New Hampshire Job Creation in Traded Clusters
1998 to 2009

Net traded job creation, 1998 to 2009: -11,414

* Percent change in national benchmark times starting regional employment. Overall traded job creation in the state, if it matched national benchmarks, would be -15,395.

New Hampshire Wages in Traded Clusters vs. National Benchmarks

Power Generation and Transmission
Financial Services
Information Technology
Distribution Services
Business Services
Analytical Instruments
Medical Devices
Aerospace Engines
Motor Driven Products
Heavy Construction Services
Leather and Related Products
Production Technology
Communications Equipment
Publishing and Printing
Automotive
Lighting and Electrical Equipment
Building Fixtures, Equipment and Services
Forest Products
Sporting, Recreational and Children's Goods
Plastics
Metal Manufacturing
Jewelry and Precious Metals
Biopharmaceuticals
Chemical Products
Transportation and Logistics
Heavy Machinery
Apparel
Textiles
Construction Materials
Education and Knowledge Creation
Processed Food
Furniture
Hospitality and Tourism
Entertainment
Agricultural Products
Oil and Gas Products and Services
Aerospace Vehicles and Defense
Tobacco
Prefabricated Enclosures
Fishing and Fishing Products
Footwear

Wages, 2009


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### 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>
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<td>+27,171</td>
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<td>20,142</td>
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<tr>
<td>New York</td>
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<td>3,628</td>
<td>20,474</td>
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<td>Massachusetts</td>
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<td>California</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.
### New Hampshire Performance Scorecard

#### Prosperity
**GDP per Capita, 2000-2010**
- Start: 19
- Trend: 31
- Current: 24 (-5)

#### Wages
**Average Private Wage, 1998-2009**
- Start: 20
- Trend: 8
- Current: 15 (+5)

#### Job Creation
- Start: 13
- Trend: 28
- Current: 20 (-7)

#### Labor Mobilization
**Proportion of Working Age Population in the Workforce, 2000-2010**
- Start: 4
- Trend: 30
- Current: 7 (-3)

#### Labor Productivity
**GDP per Workforce Participant, 2000-2010**
- Start: 27
- Trend: 42
- Current: 34 (-7)

#### New Business Formation
- Start: 30
- Trend: 14
- Current: 13 (+17)

#### Innovation
**Patents per Employee, 2000-2010**
- Start: 9
- Trend: 27
- Current: 9 (+0)

#### Cluster Strength
**Employment in Strong Clusters, 1998-2009**
- Start: 25
- Trend: 10
- Current: 14 (+10)

#### Leading Clusters
- Education and Knowledge Creation (28)
- Analytical Instruments (12)
- Distribution Services (33)
- Production Technology (17)
- Information Technology (28)
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
Defining the Appropriate Economic Regions

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

Wage Performance in New Hampshire Metropolitan Areas

Average Private Wage, 2009

Growth Rate of Private Wages, 1998-2009

U.S. Growth Rate of Wages: 3.01%

New Hampshire Growth Rate of Wages: 3.44%

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

New Hampshire Average Private Wage: $41,596

Manchester MSA

Boston MSA*

Rest of State

*New Hampshire portion only

Source: Census CBP, authors' analysis. Note: "Bubble" size in chart is proportional to employment in 2009.
Employment Performance in New Hampshire Metropolitan Areas

**U.S. Growth Rate of Employment:** 0.52%

**New Hampshire Growth Rate of Employment:** 0.83%

**Average Private Wage, 2009**

- **U.S. Average Private Wage:** $42,403
- **New Hampshire Average Private Wage:** $41,596

**Growth Rate of Private Employment, 1998-2009**

- **Manchester MSA**
- **Boston MSA**
- **Rest of State

Note: “Bubble” size in chart is proportional to employment in 2009.

*New Hampshire 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
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

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**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

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

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

- Education / Workforce
- Start-ups / Local Firms
- Measuring Progress

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.