

State Competitiveness: Creating an Economic Strategy in a Time of Austerity

*National Governors Association Winter Meeting
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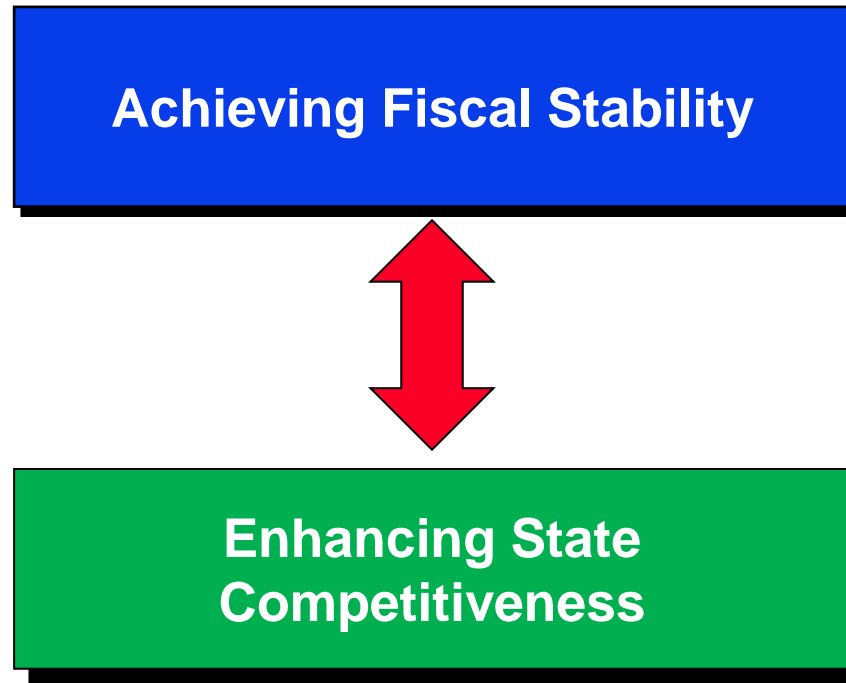


**Professor Michael E. Porter
Harvard Business School**

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

For state economic profiles: www.isc.hbs.edu/stateprofiles.htm

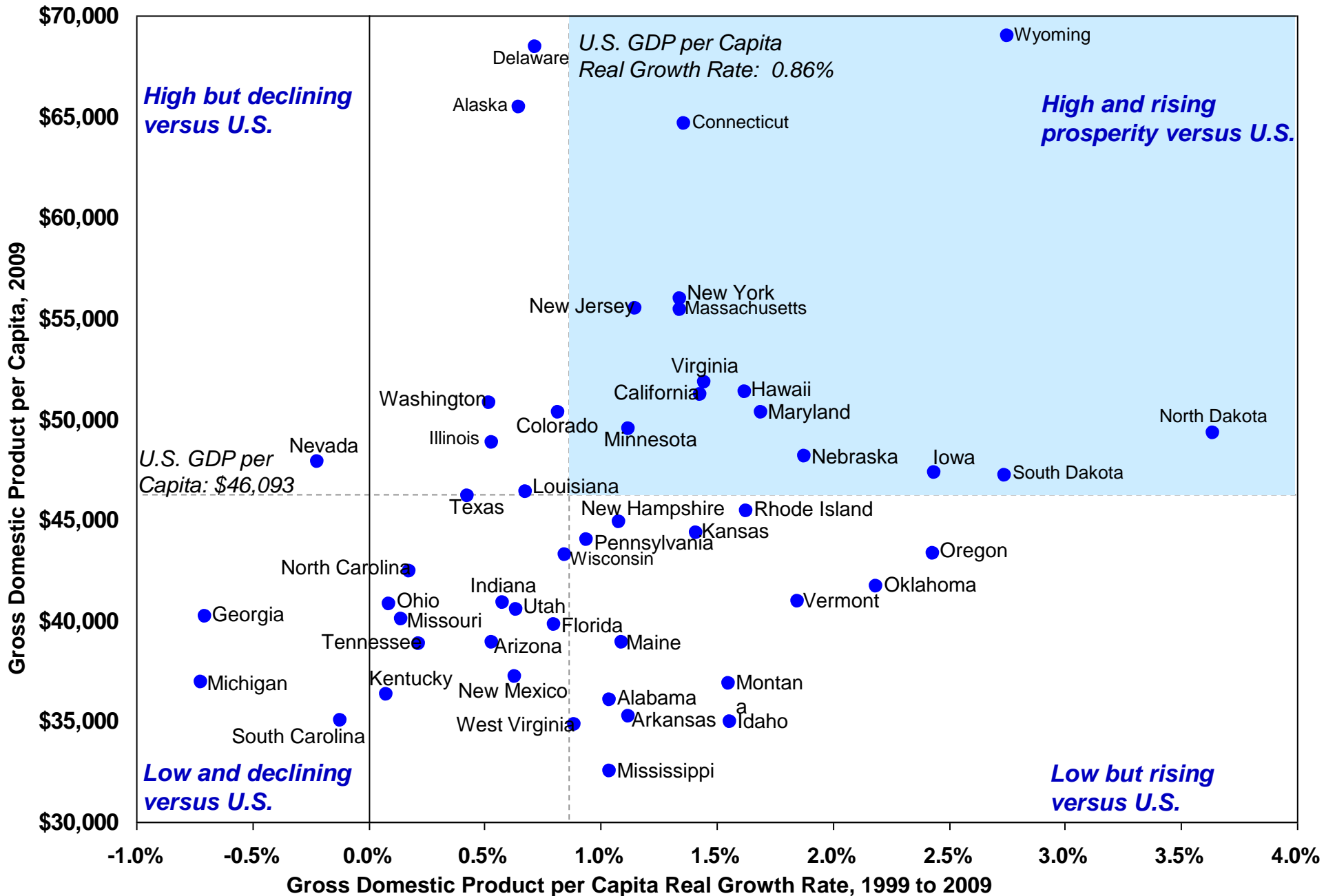
The Economic Challenge for Governors in 2011



- **Competitiveness** is the only way to achieve sustainable job growth, improving wages, and stable public finances
- Creating a **clear economic strategy** for the state, that engages all stakeholders, is **even more important** in times of budget cutting and austerity

Understanding State Economic Performance

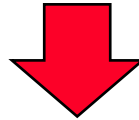
1999 - 2009



Notes: Real GDP figures in 2005 chained US dollars from the Bureau of Economic Analysis. Growth rate is calculated as compound annual growth rate. D.C. excluded
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What is Competitiveness?

- Competitiveness is the **productivity** with which a state utilizes its human, capital, and natural resources
- Productivity determines **wages** and the **standard of living**
 - Productivity growth determines sustainable **economic growth**
- Productivity depends on **how** a state competes, not what industries it competes in
- **Innovation** in products and processes is necessary to drive productivity growth



- Only **productive businesses** can create wealth and jobs
- States compete to offer the **most productive environment** for business
- The public and private sectors play **different but interrelated roles** in creating a productive economy

New Jersey Competitive Performance

Prosperity

Gross State Product per capita, 2009

• In New Jersey:	\$55,464	Rank: 7
• In the US:	\$46,093	
• State difference to US:	20.3%	

Growth in Gross State Product per capita, real annual rate, 1999-2009

• In New Jersey:	1.15%	Rank: 21
• In the US:	0.86%	

Productivity

Gross State Product per labor force participant, 2009

• In New Jersey:	\$106,667	Rank: 7
• In the US:	\$92,382	
• State difference to US:	15.5%	

Growth in Gross State Product per labor force participant*, 1999-2009

• In New Jersey:	1.06%	Rank: 31
• In the US:	1.09%	

Average private wage, 2008

• In New Jersey:	\$50,923	Rank: 5
• In the US:	\$42,435	
• State difference to US:	20.0%	

Private wage Growth, annual rate, 1998-2008

• In New Jersey:	3.15%	Rank: 35
• In the US:	3.32%	

Innovation Output

Patents Per 10,000 Employees, 2009

• In New Jersey:	7.80	Rank: 13
• In the US:	6.83	

Growth in total patents, annual rate, 1998-2009

• In New Jersey:	-2.54%	Rank: 44
• In the US:	0.23%	

Traded establishment formation, annual growth rate, 1998-2008

• In New Jersey:	0.47%	Rank: 47
• In the US:	1.79%	

Cluster

Share of State Traded Employment in Strong Clusters, 2008

• In New Jersey:	68.5%	Rank: 2
• In the US:	41.8%	

Change in Share of National Employment in Strong Clusters, 1998-2008

• In New Jersey:	-0.23%	Rank: 37
• In the US:	-0.06%	

Labor Mobilization

Labor Force Participation, 2009

• In New Jersey:	67.2	Rank: 21
• In the US:	65.4	

Employment, 2010 (December)

• In New Jersey:	4,079,180	Rank: 10
• % of US:	2.93%	

Employment growth, annual rate, 2000-2010 (December)

• In New Jersey:	-0.12%	Rank: 38
• In the US:	0.11%	

Unemployment, 2010 (December)

• In New Jersey:	9.1%	Rank: 29
• In the US:	9.4%	

Change in Unemployment, 2000-2010 (December)

• In New Jersey:	5.4%	Rank: 35
• In the US:	5.5%	

Population

Population, 2009

• In New Jersey:	8,707,707	Rank: 11
• % of US:	2.84%	

Population growth, annual rate, 1999-2009

• In New Jersey:	0.41%	Rank: 39
• In the US:	0.96%	

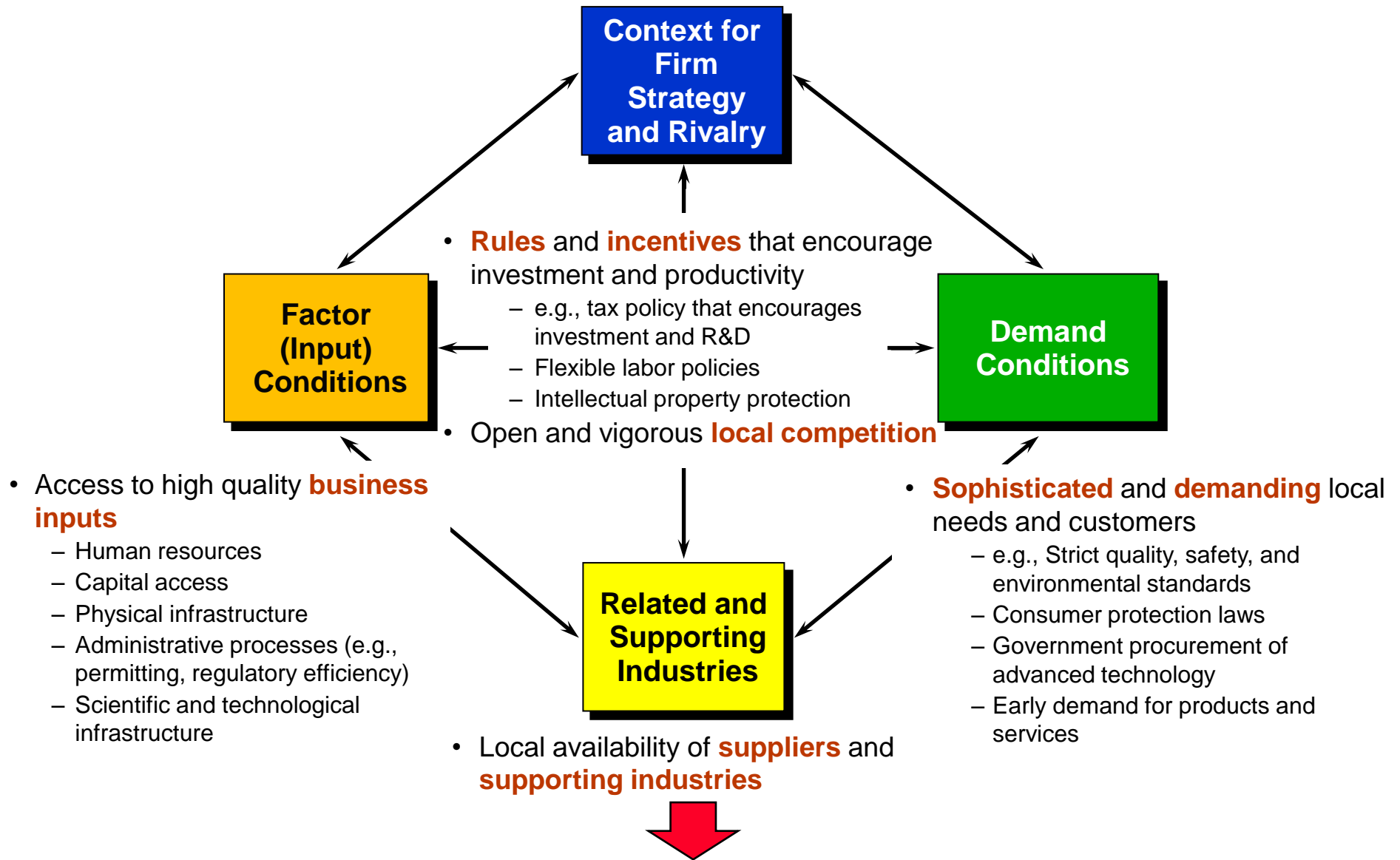
What Drives State Productivity?

**Quality of the
Overall
Business
Environment**

**State of Cluster
Development**

**Policy
Coordination
among Multiple
Geographic
Levels**

Quality of the Business Environment



- **Many things matter** for competitiveness
- Successful economic development is a process of improving the business environment to enable **increasingly sophisticated ways of competing**

Improving Productivity in the Business Environment

Key Issues for States

- Simplify and speed up **regulation** and **permitting**
- Reduce unnecessary **costs of doing business**
- Establish **training programs** that are aligned with the needs of the state's businesses
- Focus **infrastructure investments** on the most leveraged areas for productivity and economic growth
- Design all policies to support **small growth businesses**
- Protect and enhance the state's **higher education** and **research** institutions
- Relentlessly improve of the **public education** system, the essential foundation

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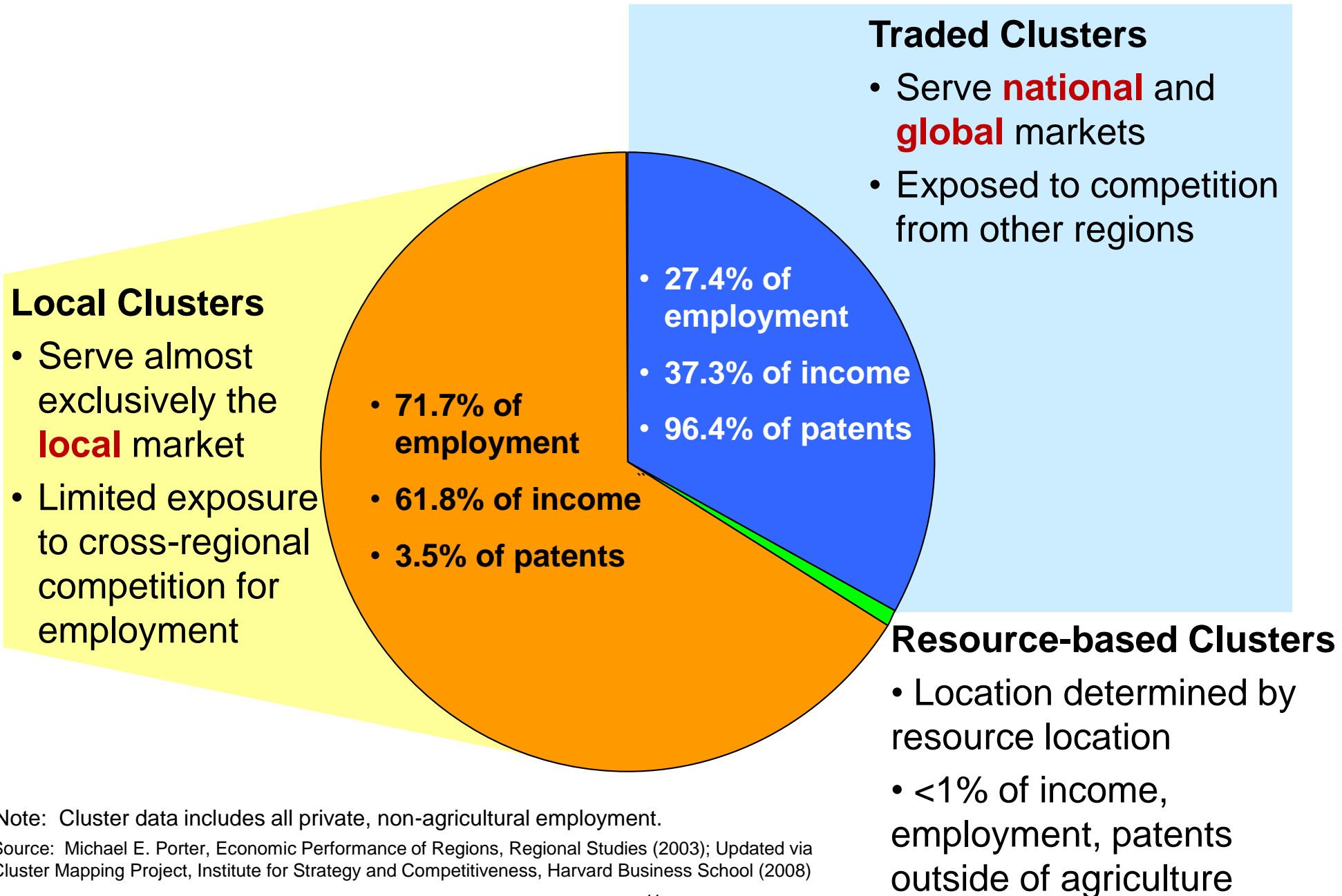
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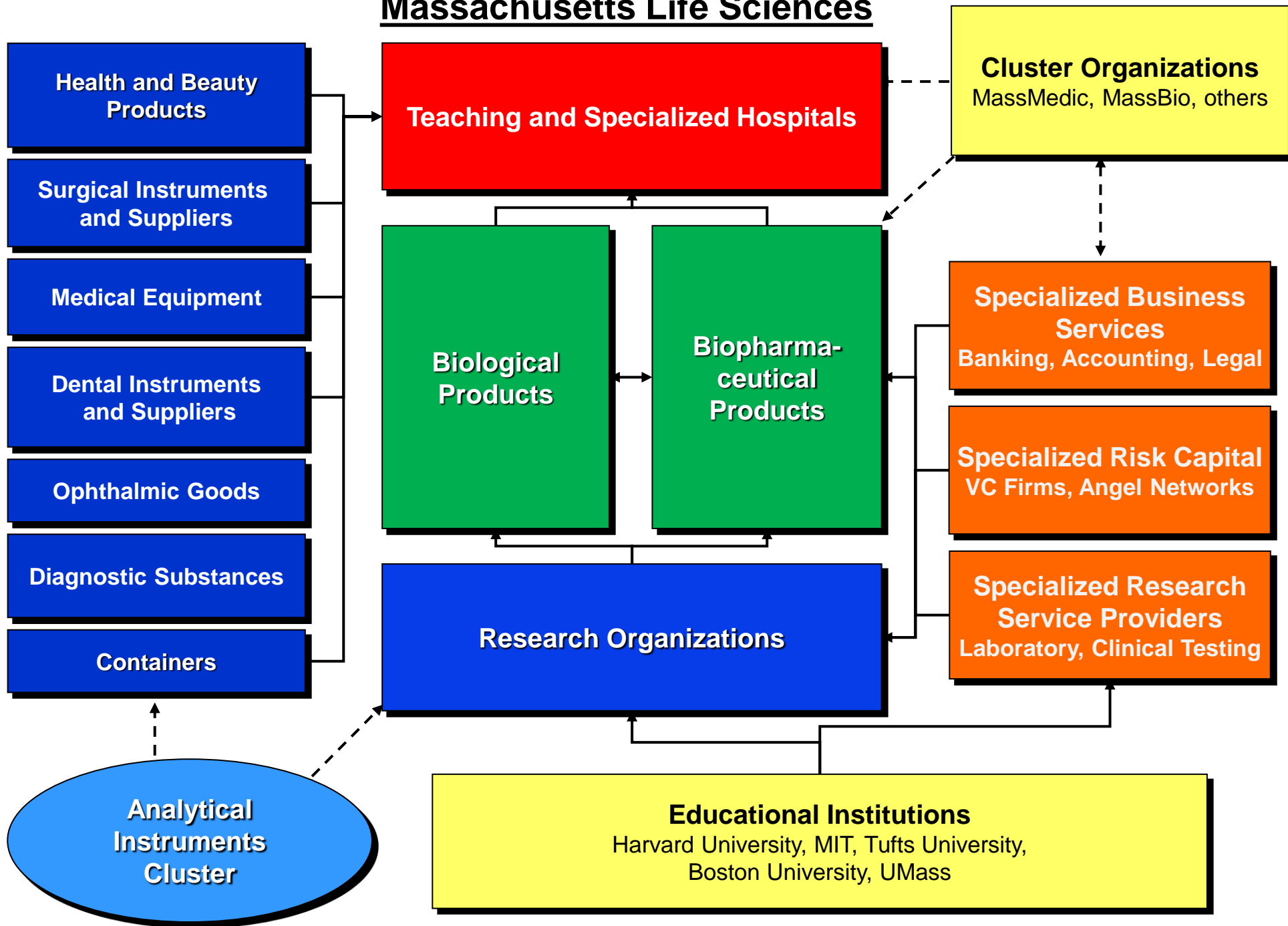
Composition of Regional Economies, U.S. 2008



Note: Cluster data includes all private, non-agricultural employment.

Source: Michael E. Porter, Economic Performance of Regions, Regional Studies (2003); Updated via Cluster Mapping Project, Institute for Strategy and Competitiveness, Harvard Business School (2008)

State of Cluster Development Massachusetts Life Sciences

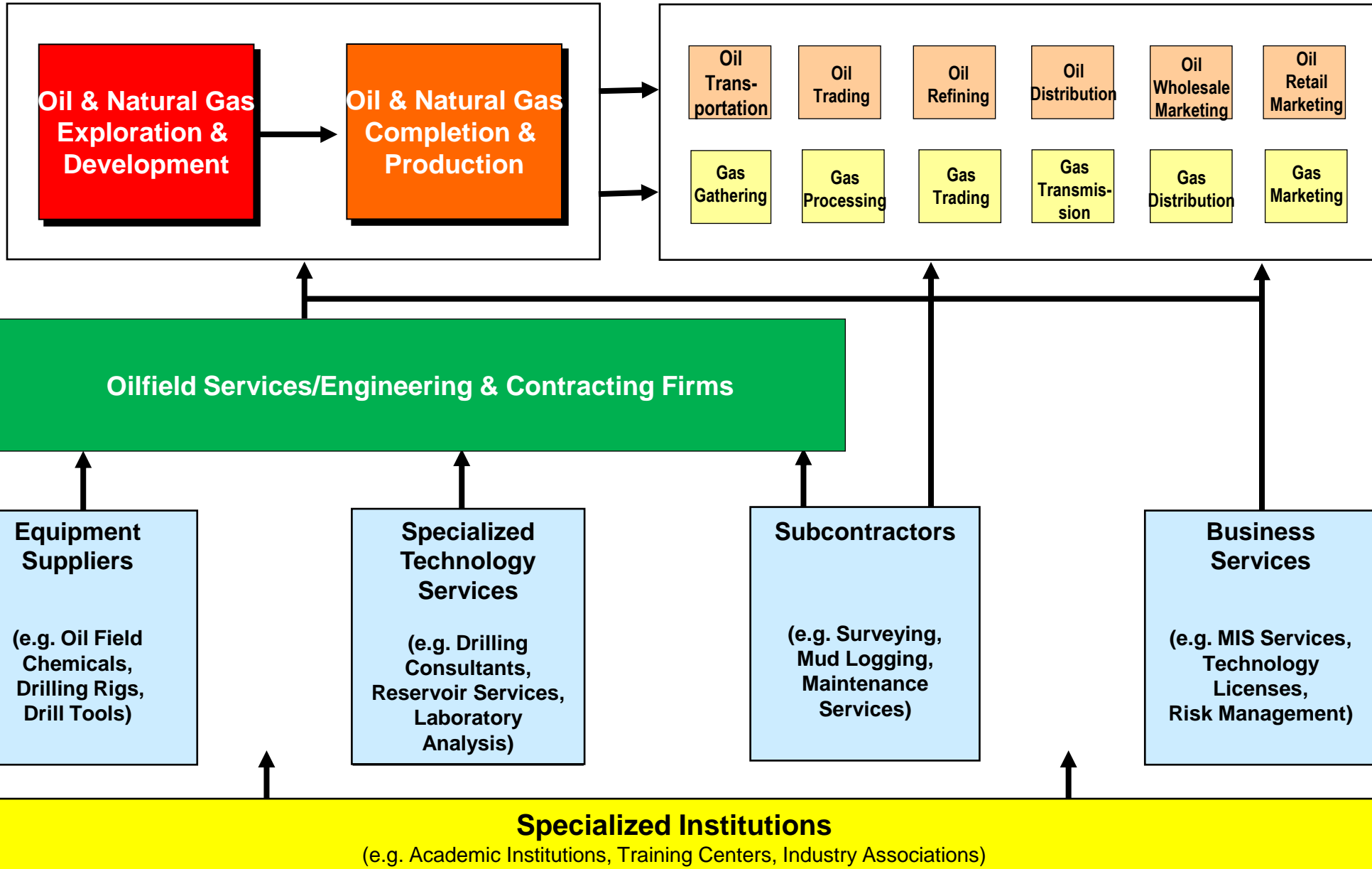


State of Cluster Development

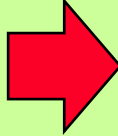
Houston Oil and Gas

Upstream

Downstream

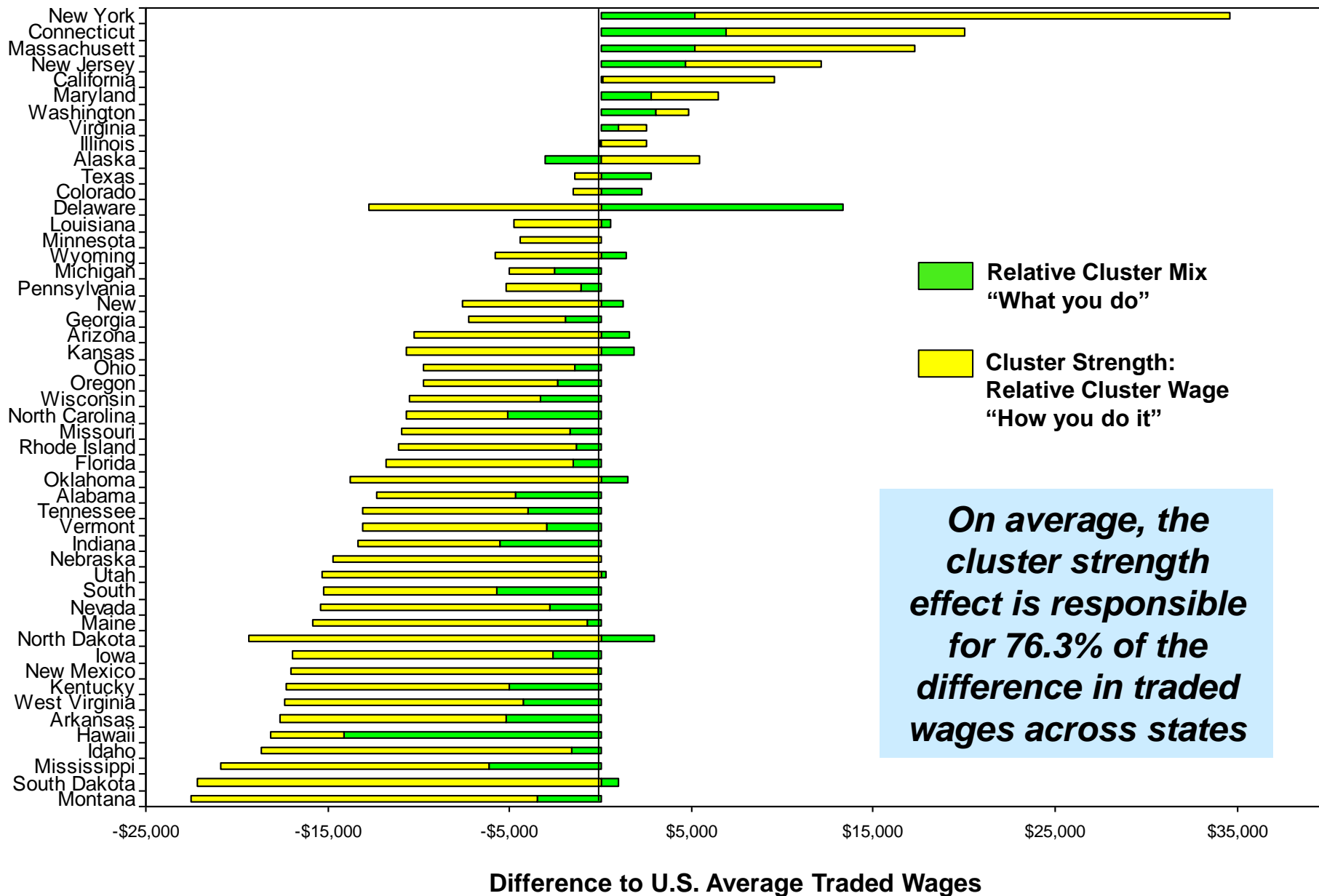


Strong Clusters Drive Regional Performance

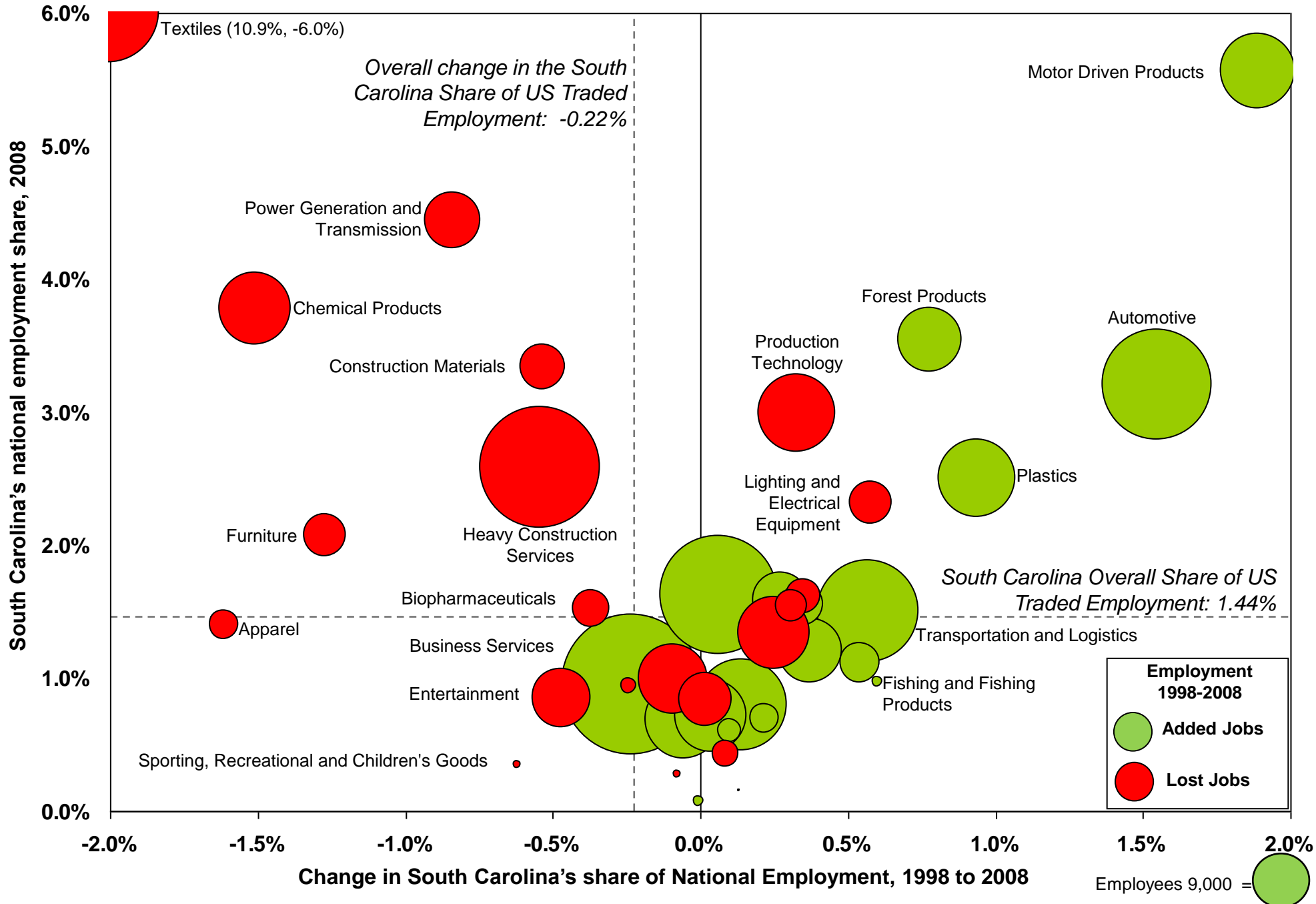
- Specialization in **strong clusters**
 - **Breadth** of industries within each cluster
 - Strength in **related clusters**
 - Presence of a region's clusters in **neighboring regions**
- 
- **Job** growth
 - Higher **wages**
 - Higher **patenting** rates
 - Greater **new business** formation, growth and survival

Impact of Cluster Mix and Cluster Strength on Average Traded Wages

U.S. States, 2008

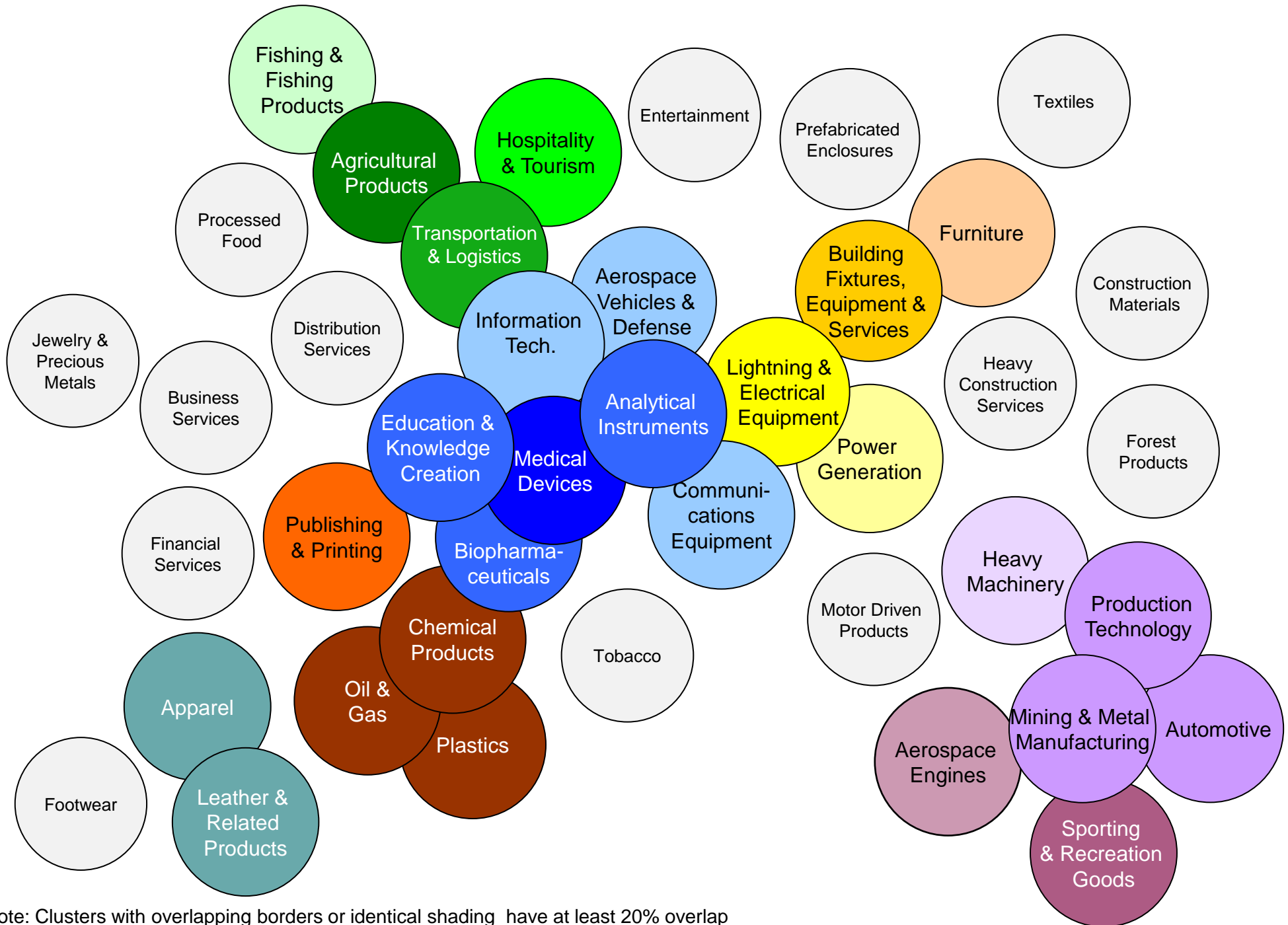


Composition of the South Carolina Economy Specialization by Traded Cluster, 1998 to 2008



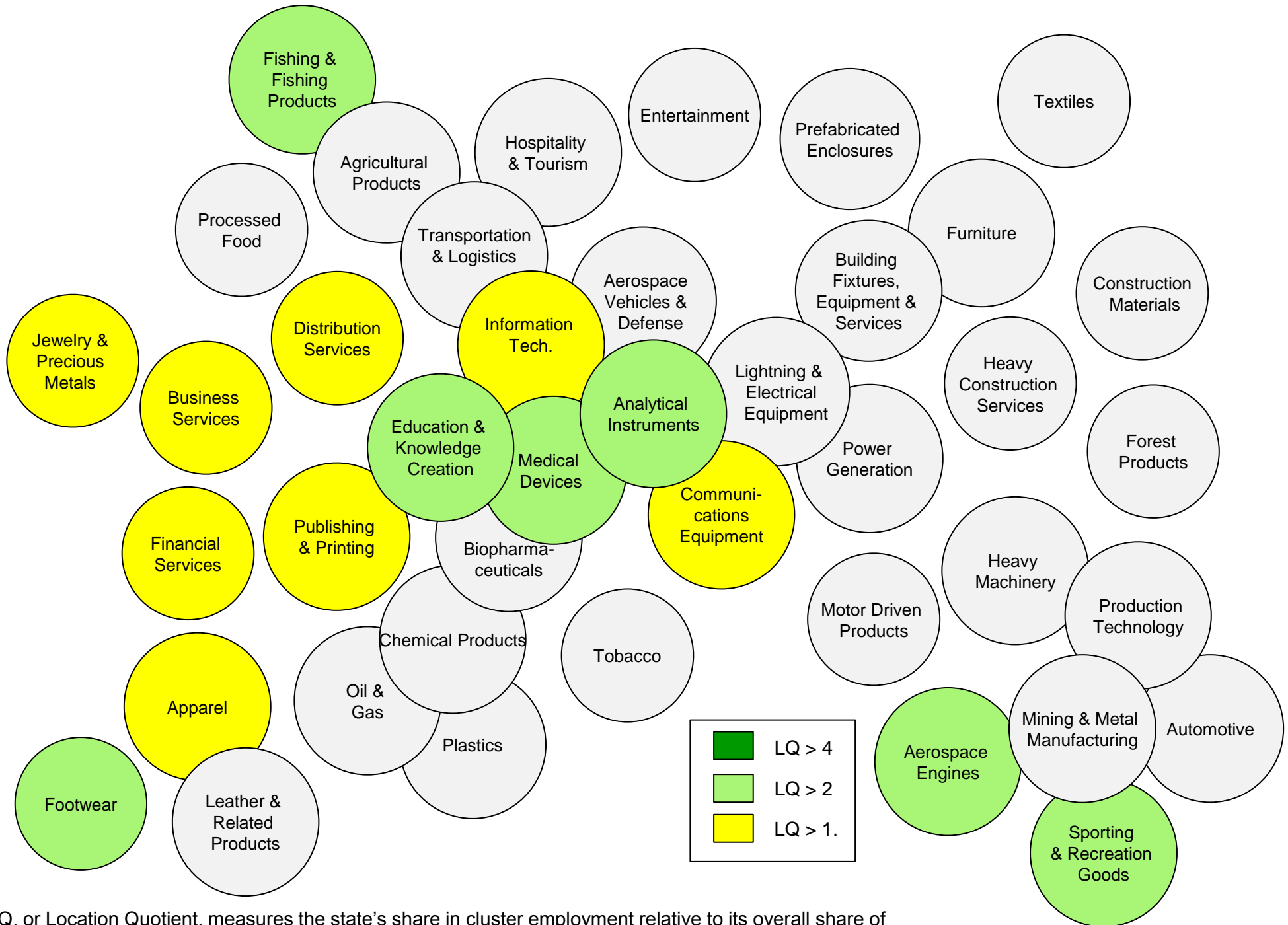
Source: Prof. Michael E. Porter, Cluster Mapping Project, Institute for Strategy and Competitiveness, Harvard Business School; Richard Bryden, Project Director.

Related Clusters and Economic Diversification



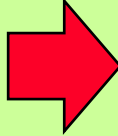
Note: Clusters with overlapping borders or identical shading have at least 20% overlap (by number of industries) in both directions.

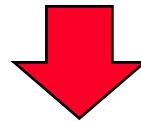
Massachusetts Cluster Portfolio, 2008



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.

Strong Clusters Drive Regional Performance

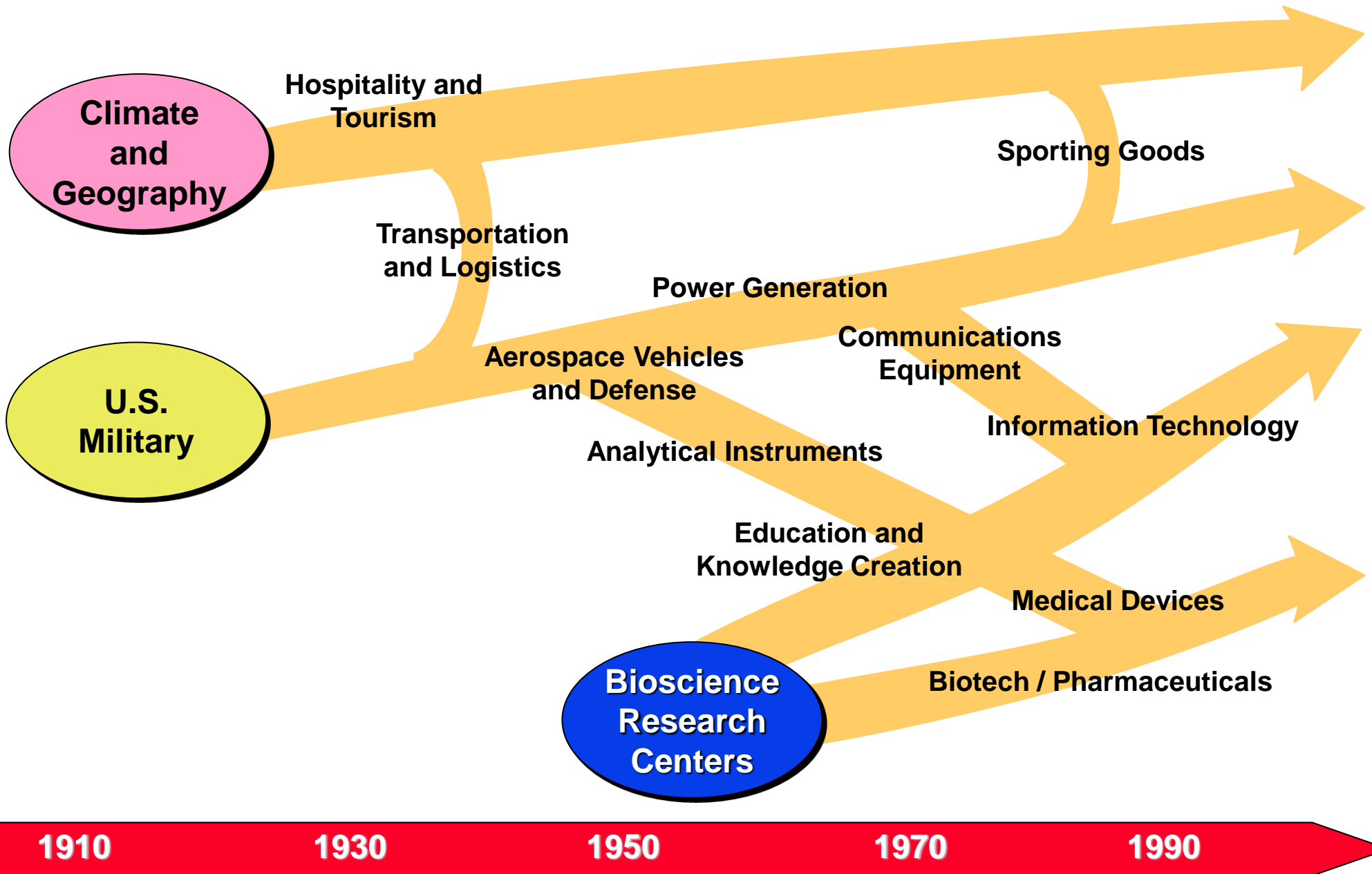
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- Build on the state's **existing and emerging** clusters in the state rather than chase hot fields
- Economic diversification usually occurs **within clusters** and **across related clusters**

The Evolution of Regional Economies

San Diego



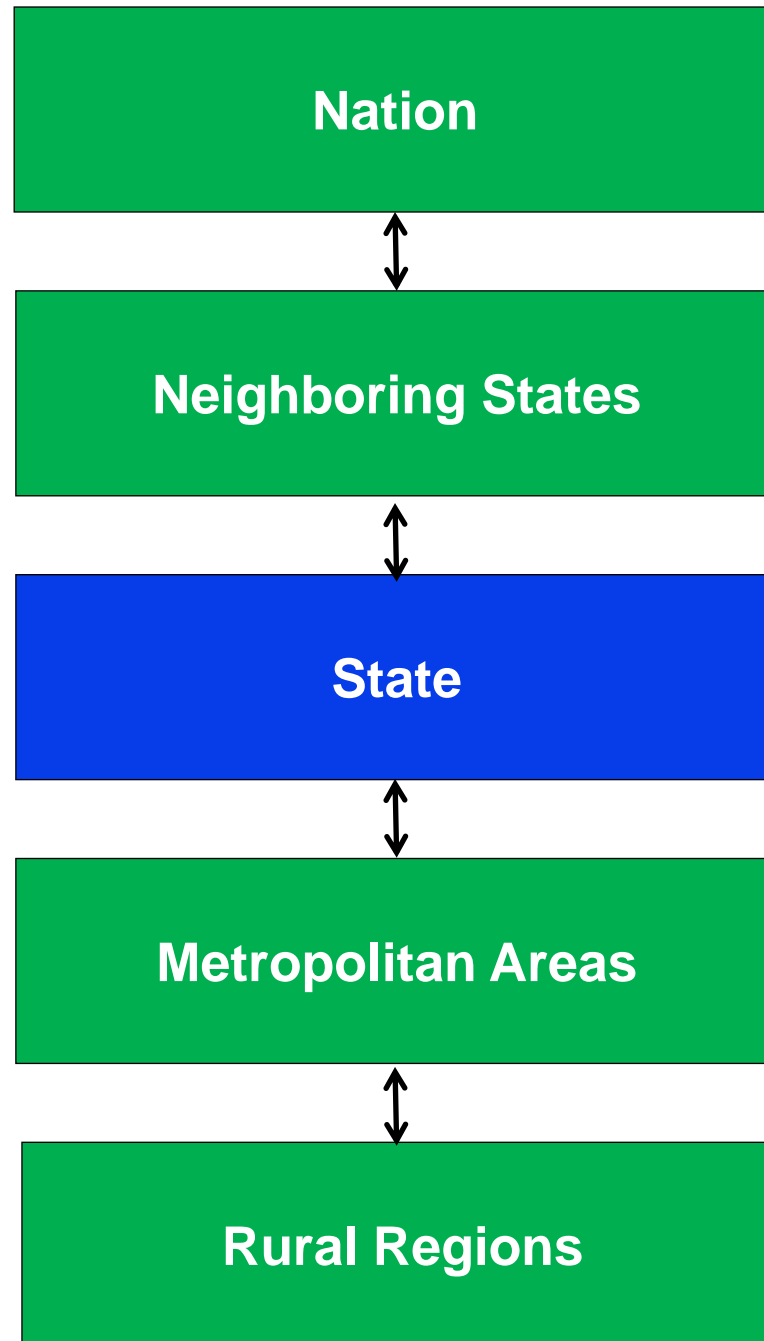
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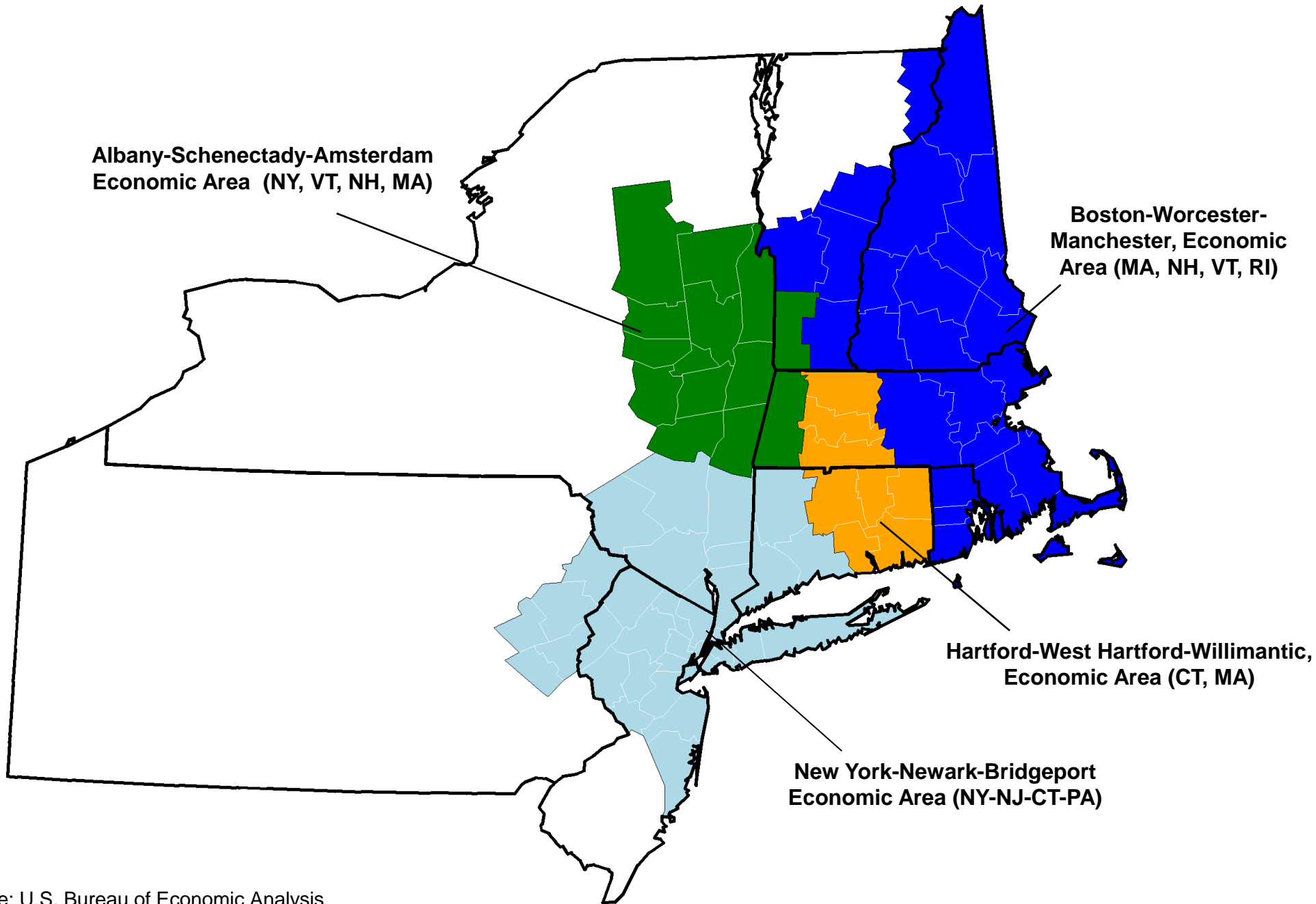
**Policy
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Geographic Influences on Competitiveness

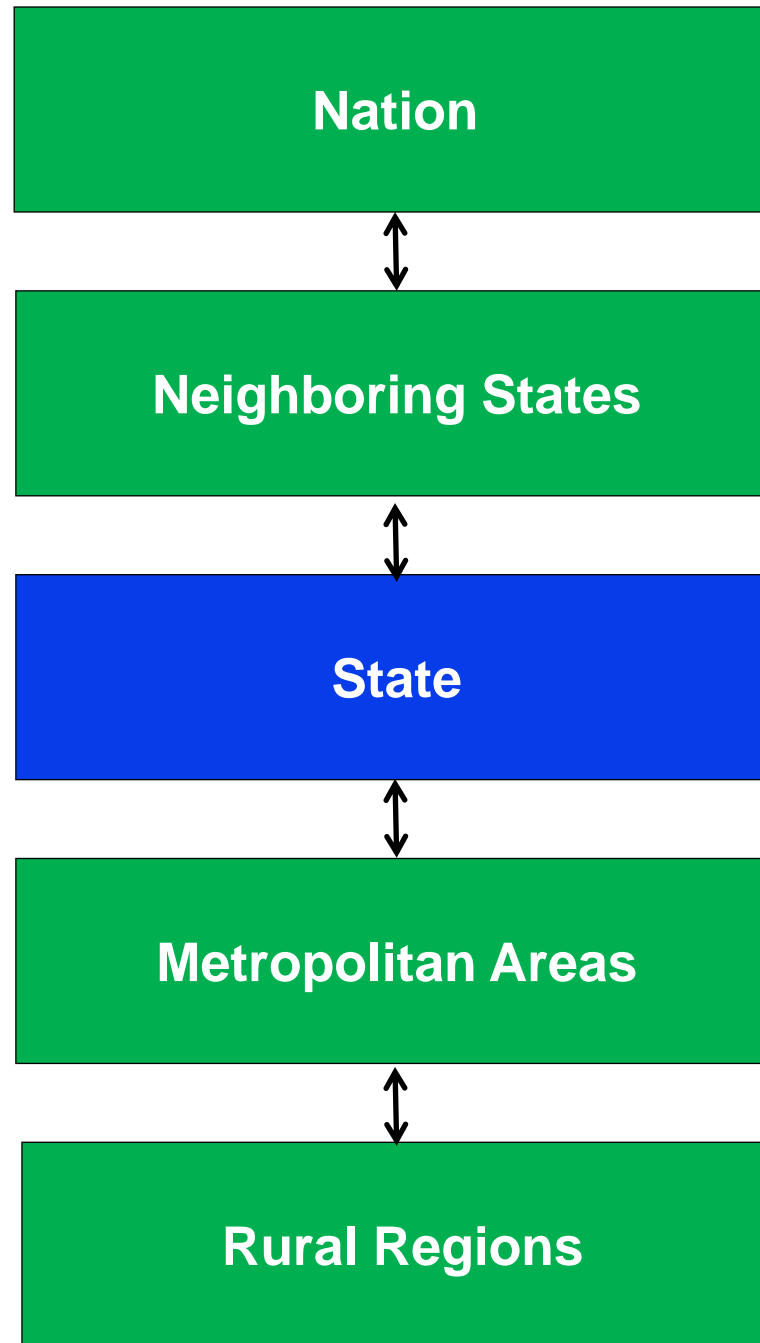


Defining the State's Economic Regions

Massachusetts in BEA Economic Areas



Geographic Influences on Competitiveness



- **Influence** and **access** federal policies and programs

- Integrate policies and infrastructure with neighbors

- Assist each metro area in developing its own strategy

- Connect rural regions with urban areas

Creating a State Economic Strategy

State Value Proposition

- What can be the **distinctive competitive position** of the state given its assets, location and potential strengths?

Developing Unique Strengths

- What elements of the business environment can be **distinctive strengths** relative to peers?
- What **strong** or **emerging clusters** can be built upon?

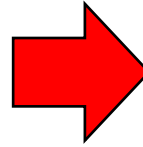
Achieving and Maintaining Parity with Peers

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

- 
- State economic strategy requires **setting priorities** and **moving beyond** long lists of discrete recommendations

How Should States Compete with Each Other?

Tactical (Zero Sum Competition)



Strategic (Positive Sum Competition)

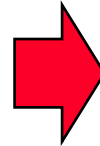
- Focus on attracting **new** investments
- Compete for **every** plant
- Offer **generalized** tax breaks
- Provide subsidies to **lower / offset** business costs
- Every city and sub-region **for itself**
- **Government** drives investment attraction

- 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**
- Government and the private sector **collaborate** to build cluster strength

The Shifting Process of Economic Development

Old Model

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

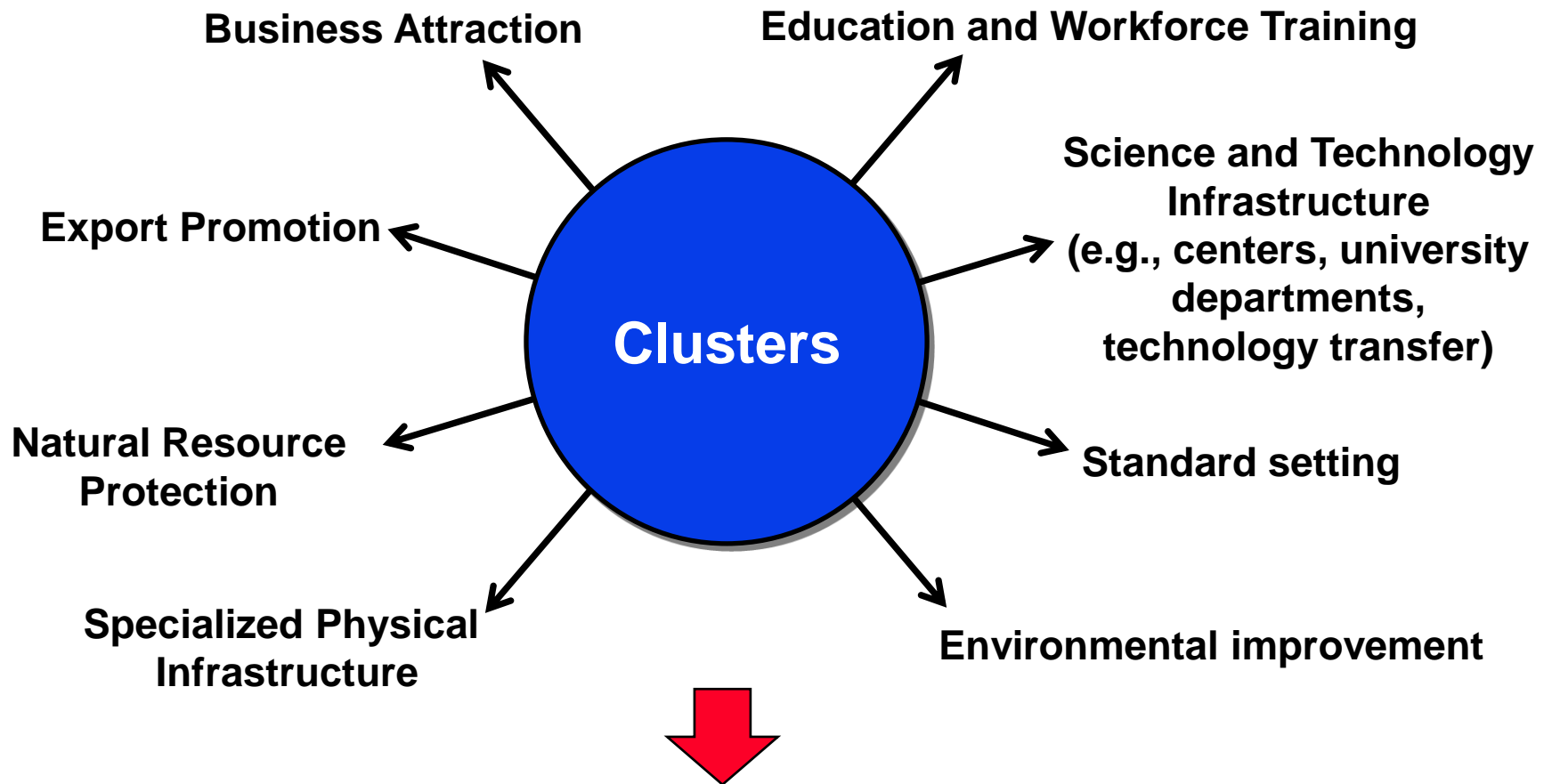


New Model

- Economic development is a **collaborative process** involving government at multiple levels, companies, teaching and research institutions, and private sector organizations

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

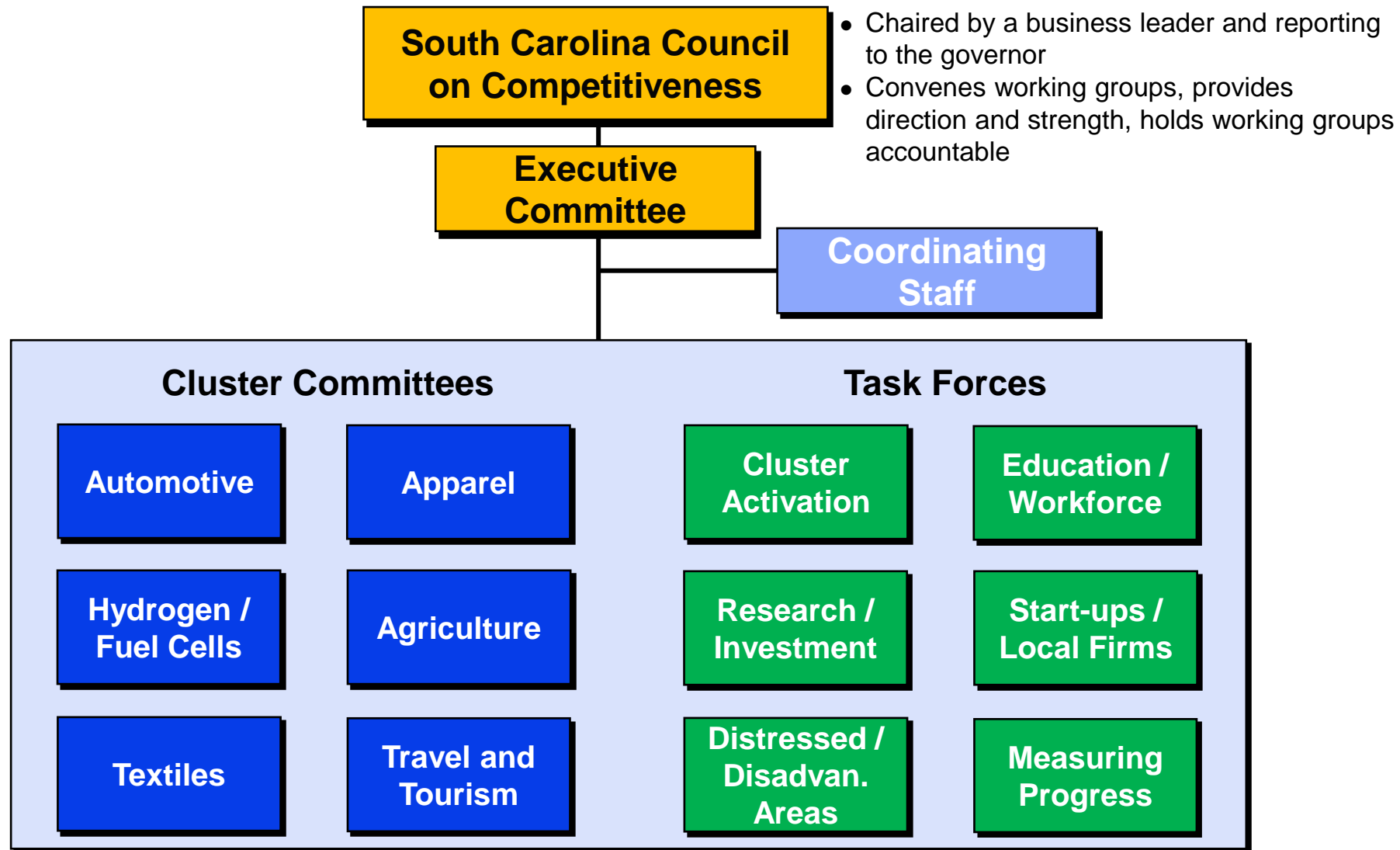
Aligning Economic Policy and Clusters



- Clusters provide a framework for **organizing the implementation** of many public policies and public investments directed at economic development to achieve greater effectiveness

Organizing for Economic Development

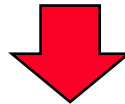
South Carolina Council on Competitiveness



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

Concluding Remarks

- The goal of economic strategy is to enhance productivity and thus fundamental **competitiveness**. This is the only way to create jobs in the long run
- Improving **productivity** and **innovation** must be the guiding principles for every state policy choice
- Improving competitiveness does not require new resources, but **using existing resources better**
- Improving state competitiveness will require governors to **mobilize the private sector**, not rely on government alone
- Economic strategy is not about ideology, but getting **results**



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