RESEARCH PROJECT:

Minnesota Regional Manufacturing/Technology Opportunity Assessment:
Southwest Region

Round Table Discussion/Executive Summary

DATE:
June 1996

Bureau of Business and Economic Research

University of Minnesota Duluth
Center for Economic Development
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This report was sponsored by and written with the editorial assistance of Minnesota Technology, Inc.

Prepared for:
Minnesota Technology, Inc.
I. INTRODUCTION

The purpose of this paper and five others like it is to describe the economic base of six regions in the state of Minnesota, and to identify possible future niches for development. The relative health of Minnesota’s economy today, and nearly full employment allows us an opportunity to plan strategically for the long term health of our state’s economy. For this reason, our philosophy in formulating this paper and our recommendations has been that economic development efforts should focus on industries providing high wage/high value jobs which lead to an improved quality of life for Minnesota’s citizens.

The economic base of Southwest Minnesota is still defined today by non-technological, agriculture-related industry. This economic base is described in the first section of this paper under the heading of Strongest Industries.

Our recommendations begin with a look at the top technology manufacturing performers in the region, identified by analyses of secondary data, focus group discussion, and individual interviews with knowledgeable people in the region. In the same way, we have identified candidates for business retention and development efforts that are important suppliers to the industries which comprise the economic base of the region.

Readers who are interested in further information are invited to look at reports 1 and 2 for the Southwest region.

Report #1: SUPPORTING DATA, including the Notion of Economic Base, Measuring Economic Base, Employment in Southwest Minnesota, Location Quotient Values for Southwest Minnesota, Shift-share Analysis for Southwest Minnesota, Input-output: Industry Ranking by Output Levels, Manufacturing - Technology Rankings, and appendix material with complete data.

Report #2: PRELIMINARY DATA, including Discussion of Data Sources, Data Organization, Industry Leaders, General Information and Analysis of Regional Structure for Key Industries, and tables of top performers.

The data for these reports are taken from secondary sources, including:

# **Regional Economic Information System** (REIS), United States Department of Commerce.

# **County Business Patterns** (CBP), United States Department of Commerce.

# **NU OnRamp**, University of Nebraska Bureau of Business Research computer based retrieval system (NUOR).

# **IMPLAN 1993**, MIG, Inc. Stillwater, MN.

# **Standard Industrial Classification Manual**, Executive Office of the President, Office of Management and Budget.
II. ECONOMIC BASE OF SOUTHWEST MINNESOTA

STRONGEST INDUSTRIES

The industries that make up the economic base of a region can be identified by their performance in five categories: employees (or level of employment), value added to the region, exports from the region either to the rest of the United States or to foreign countries, interaction with other industries in the economy leading to a ripple effect among industries, and prospects for future economic growth. A region depends upon the industries which dominate these categories in a very real way. Their strengths and weaknesses should be of major concern to those with an interest in the growth and development of the regional economy.

The following list of industries represent those in the Southeast region that are dominant in the above categories of performance. To be included in the following list requires that the industry be in the top thirty industries (out of over 500 industries) in at least four of these five categories of performance.

Economic base, in a technical sense, consists of industries that bring money in from outside the region through export activity. This money is then used to buy local goods and services either as semi-finished goods or professional services contributing to basic production. The secondary or local supplying industries are part of the infrastructure that makes a basic industry competitive in the global market place. Thus construction, local retail trade, business services, and other industries such as these both depend on the basic industry and nurture it.

Key Facts about Southwest Minnesota’s Economic Base: Top Industries from Analysis of Data Sources

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Key identified both by data sources and focus groups/interviews
Agriculture Production

The importance of Agriculture Production in the region is obvious to most observers. Not to list it here would be to overlook the dominant industry in the region. For the purposes of this report Agriculture Production includes the sectors of Hogs, Pigs and Swine; Cattle Feedlots; and Oil Bering Crops. Major changes are taking place nationally regarding the federal government’s role in regulating or encouraging agricultural production. Farm subsidies will be phased out over time and less regulation is in the future. NAFTA and other trade agreements will change the competitive picture for agriculture in both the near term and far into the future. Continued monitoring of these events and of the ability of local agriculture to compete in these changing markets would be in the region’s and in the state’s interest.

As is true for many other industries operating in an increasingly competitive environment, efficiencies provided by the regional economy through infrastructure development, workforce productivity, and the cost/provision of local government services will influence the agriculture industry’s ability to compete and grow. To take such influences for granted could be to invite significant economic dislocations in the future.

Meat Packing Plants

This industry was identified as being basic to the region through various analyses of data provided by the U.S. government and by the IMPLAN data base. Value-added agriculture production was also identified through individual interviews and focus group sessions.

Meat Packing plants are major exporters from the region, bringing in money which is re-spent locally, and which contributes to a ripple effect through the economy.

They are major employers and account for significant compensation levels in the region, paying close to $30 million in 1993. They also represent a major growth sector in the economy, adding 200 employees to the region between 1990 and 1993. Most of this additional employment is identified as being due to the competitive advantage of the region due to the presence of a large agricultural sector in the region.

Of concern (in addition to the general concerns listed above) is the indication that the industry is a slower than average growth industry nationally. The focus groups and individual interviews reported that the jobs in this industry are not particularly well paid, that the employees tend to be transient, and that the lack of affordable housing for individuals earning these levels of pay is a potential impediment to attracting and maintaining an adequate workforce.

Despite the lower paid nature of the jobs provided by this industry it has many other positive effects on the economy. Not the least of these is the inter-industry economic impact on many other industries in the region.

Poultry Processing

Poultry Processing is another agricultural value-added component of major importance to the region. This industry was identified as important by the data analysis as well as through the focus group and interviews.

As with Meat Packing Plants, Poultry Processing is high in most performance categories (compensation, export levels, total output, value-added, and multiplier values). While employment in the industry was seen to be declining between 1990 and 1993, the decline is partially a function of the switch to a frozen turkey product in the region. This particular sector was talked about again and again by those being interviewed and participating in the focus groups. The conversations were generally quite positive in terms of the potential for this industry to grow and be a significant future contributor to the region’s economy.

As was true for the Meat Packing industry, pay levels and potential workforce concerns were cautions to the otherwise rosy picture for Poultry Processing. However, both the Meat Packing and the Poultry Processing industries were identified, with some pride,
as industries that are locally grown, which is
the central point of the first recommendation.
Maintaining an atmosphere that allows for
such local entrepreneurship and industrial
development should be a high priority for the
region.

# Dairy and Sugar Processing

Concerns in Dairy and Sugar Processing are
essentially the same as for Meat Packing and
Poultry Processing. These remain major
exporters, and coupled with agriculture itself
they represent the economic base of the
region.

# Farm Machinery

Interest in the Farm Machinery industry came
out of the focus group and individual
interviews. While the government and
IMPLAN data can’t be broken down below
the four-digit SIC designation of Farm
Machinery, the focus group concentrated on
one particular aspect of this industry:
Precision Fertilizer Application Equipment.

This industry was perceived as a bright spot
within the economy. It was identified in the
interview process as having a diversified
market with global potential. The industry is
growing because of environmental concerns
over the older methods of applying fertilizer,
and because of major technological changes
in the industry.

While Farm Machinery manufacturing is not
generally considered a high tech industry,
this sub-component of the industry is
certainly high tech, at least in this region.
The interview respondents indicated that the
need to stay on the cutting edge in
manufacturing processes for this industry is
already spinning off the development of
unrelated products. The industry was also
identified as a heavy user of computers, all of
which are imported at the present time.

They identified this as a possibility for import
substitution—the provision or manufacture of
specialized computer equipment for regional
users such as Farm Machinery
manufacturing.

# Medical Industry (Hospitals,
Specialized Nursing Care, etc.)

An interesting outcome from the analysis of
secondary data and from the interview/focus
group process is that, in every region of the
state, the medical industry came out as a
leader. This leadership was in terms of total
employment, but it was also a relative leader
in every employment category in which the
region was compared to the rest of the
nation. We generally think of the Twin Cities
and Rochester when we think of Minnesota
medicine. We found out that Minnesota is a
medical state, in rural areas as well as in
urban areas.

Few industries depend more on policy
changes and changes in insurance practices.
Few industries are also in such a state of
flux. There is talk of consolidation, there is the possibility of changes in ownership and control of local hospitals, there is the probability that outside forces will play a larger role than in the past, and there is a likelihood that many hospitals will move from non-profit to for-profit in the near future. There is also the possibility of the loss of many rural hospitals in the not too distant future.

All of these possibilities spell major potential changes in the medical industry in Southwest Minnesota as well as for other regions in the state. It may be that this is not an industry for which industrial prospecting makes sense. But it is an industry towards which attention should be paid and plans made for a changing future.

III. RECOMMENDATIONS

RECOMMENDATION I:  A focus of economic development efforts should be on helping those existing industries which provide higher wage/value jobs to grow and survive, as opposed to emphasizing the recruitment of new businesses.

While this recommendation stems from conversations during focus group interviews in the region, it is a recommendation that requires discussion on its own merits, perhaps throughout the state. There is an increasing awareness in economic development circles that regional economic development, especially in rural regions, stems from internal sources. Small-to-medium sized enterprises, begun and nourished by local residents, often define the economic future of a rural region or even urban neighborhoods. Competitive industrial prospecting, combined with strong locational financial incentives, too often amounts to a zero sum game in which one region in the state simply attracts firms from other regions in the state.

Further, it is not unusual to find industries offered incentives at a location they would have chosen in any case. Locating firms simply take advantage of significant concessions from competing regions in the process. There is a question as to whether benefits and costs of industrial prospecting, coupled with tax and financial give-a-ways, add up to positive outcomes in many instances. And once industries are located in a region, they are often ignored and taken for granted.

TOP TECHNOLOGY MANUFACTURING PERFORMERS

Here we have identified the top performing technology industries with a strong local base. These are industries which typically provide higher wages, and may be worthy of additional economic development attention. Individuals in the focus group/interviews did confirm that these industries existed in the region, but other than ethanol production, none of the industries were specifically mentioned by the respondents as their choices for niches in the future.

# Computer Storage Devices

This industry produces storage devices such
as disk drives, magnetic storage devices, tape storage units, etc. It was identified as a fast-growth industry for the region in terms of employment. It was also identified as an industry with high compensation levels in this study. Further encouragement of this industry’s competitive position in the global economy might well pay dividends for the Southwest Region.

**# Biological Products Except Diagnostic**

These are firms that produce bacterial and virus vaccines, toxoids, serums, and related products. It showed an increase of 53 employees between 1990 and 1993 to a total of 137 employees. It is a sector that is growing due to competitive advantages in the region, although our research can’t show what those advantages might be at this point in time. It also shows an increase in relative importance when compared to its national counterpart.

**# Surgical Appliances and Supplies**

This is another industry the focus groups and interviewees could identify but could not say much more about. Like the previous industries, it is a growth sector in the region, both in absolute and in relative terms. Its total employment of 408 does not make it the largest by any stretch of the imagination. However, it is identified as being one of the better industries from an employee compensation point of view.

**# Ethanol Production**

Although not supported by analysis of government data, both individuals in the focus groups and individuals interviewed were quite positive regarding the future for Ethanol Production. There is one existing plant and another on the way.

Employment is increasing, wages are better than for some other manufacturing plants in the region, and the future looks bright because of ethanol’s ability to burn cleaner than petroleum based products alone. Two cautions that have some people worried is the possibility of rising corn prices and the oil lobby’s work against any government imposed requirement to use ethanol as an environmental program.

This industry is a niche. Local and state efforts at making and keeping this industry competitive will undoubtedly lead to benefits for Southwest Minnesota in the future.

**# Electronic Coils and Transformers**

This is another major growth sector in the region, posting an increase in employment of 120 employees between 1990 and 1993. Two other electrical sectors were also identified by the analysis of employment: Electrical Industrial Apparatuses, and Lighting Equipment.

Taken as a group, there seems to be an argument for emphasizing electrical unit manufacturing as a possible growth sector for the region. We were not able to determine whether or not this was limited to routine manufacturing processes with accompanying lower wages, but we suspect this to be the case. Further investigation may be worthwhile along these lines.
We found a number of industries in the Southwest Region which are contributing significantly to the region’s economy but that are displaying signs of difficulty or that are declining in importance. (Our next several observations are in terms of employment.) These industries should be the focus of retention efforts on the part of local governments and development agencies. A successful retention effort is likely to pay dividends at least as large as high risk efforts to attract new industry into the region.

Technology industries either disappearing from the region or declining in competitive advantage include: Construction Machinery manufacturing, and Household Audio and Video Equipment manufacturing (which apparently has left the region).

# Prefabricated Metal Buildings and Components.

This is a manufacturing industry that produces portable and prefabricated metal buildings. It also produces parts and prefabricated metal panels associated with such buildings.

The local industry Prefabricated Metal Building and Components lost 207 employees between 1990 and 1993.

Relative to the nation, the Prefabricated Metal Buildings and Components industry was concentrated in this region in 1990. While its presence was more significant in the region than for the nation as a whole in 1993, the level of concentration was much less.

This industry is not a fast-growth industry nationally. However, slow-growth is not the biggest explanation for this industry’s performance. Data from another part of our analysis shows that a competitive component accounts for most of the difference. The region is losing out relative to the rest of the nation due to some competitive disadvantage in attracting employers in prefabricated metal buildings manufacturing.

# Meats and Meat Products Wholesaling

Nationally, this is not a fast-growth industry. It is an industry that has been subject to the downsizing trend in manufacturing.

What is more, the industry was less concentrated in the region in 1993 as against its position in 1990.

Despite these trends, the Meats and Meat Products Wholesaling industry is still basic to the region as an important exporting industry. It is supportive to the meat processing industry which was identified by the focus group as a potential growth industry in the future. It still employs over 130 individuals and it may very well be a strong candidate for retention efforts by local developers.

# Boat Building and Repairing

Another concern is the Boat Building and Repairing industry in the manufacturing category. This industry lost 167 employees over the three-year period according to our data sources, once again for the most part due to the competitive component in the shift-share analysis. However, this industry is also identified as a slow-growth industry nationally out of the shift-share analysis.

There was a 43% drop in the location quotient values for this industry. It is still basic to the region, but its level of concentration relative to the nation has declined. Again this tends to confirm that the region is losing competitively in this industry as well as experiencing the downsizing characteristic of manufacturing. Boat Building and Repairing could represent another candidate for retention effort explorations.

# Others

A topic of some concern in the region during both the focus group and the individual interview sessions was the decline of Miscellaneous General Merchandise Stores, and a number of other retail categories. There is a general decline in retail employment as we move towards fewer
labor-intensive processes in everything from general merchandise to grocery stores.

An apparent trend towards concentration in larger establishments is affecting both the number and diversity of establishments in the retail sector.

There is an apparent desire on the part of those interviewed to retain a diverse retail sector in downtown areas of the region. It could be that special retention oriented actions will need be taken if this retention is to be realized.

**RECOMMENDATION II: Because basic industries buy many of their inputs to production from other local firms, attention to these local suppliers’ needs helps to make the basic industries more competitive.**

A region’s economic future requires that the region be efficient. Efficiency lowers the cost of production, making the region more competitive. Efficiency can be associated with those industries supplying the basic sector, the provision of government services, the character of the region’s infrastructure regarding roads and communications, and the efficiency of local resources, such as the productivity of its workforce. So much attention is often paid to a region’s exporting industries that those local industries supporting the base are often ignored and forgotten. This section looks at a few of those local industries that supply the economic base.

**# Construction**

One sector identified as the leading local supplier time and time again was that of Construction. Three basic industries are especially dependent on Construction: Electronic Equipment, Non-Electrical Machinery, and the Medical industry.

Because the industry is competitive, little government encouragement or interference is necessary. However, making sure the industry has what it needs in the way of skilled workers could be viewed as a responsibility of the local education structure. Monitoring the finance picture in the region to make sure funds for construction are there when needed could be the responsibility of government, and the business community itself. Quality assurance is the responsibility of everyone associated with construction in the region. These would be the recommendations associated with this apparently critical regional local supply industry.

**# Utilities**

Suffice it to say that local utilities play a major role as a supplier to regional basic industries. We highlight this industry at this point for many of the same reasons we highlighted the Medical industry earlier--there is much going on that could change the efficiency and nature of this industry in the very near future. The possibility of de-regulation at the federal level, the existing fact of de-regulation in the interstate wholesale transmission of electricity, the ever present concerns over the environment as it relates to this industry, and the already occurring consolidation of the industry through multiple mergers and acquisitions, make this industry one of concern to this and to many other regions in the nation.

**# Motor Freight Transportation and Warehousing**

This IMPLAN industry is really a composite of several industries identified by the government through the Standard Industrial
Classification code. Therefore, it is somewhat difficult to tell whether this is an industry that would also be a possible candidate for import substitution. We can say that it was a major local supplier to various manufacturing industries in the region. We will point out later that transportation was also identified by the focus groups/interviewees as a potential impediment to the future development of the region.

# Suppliers Elsewhere Discussed

The industries listed below are also important suppliers to the basic industries of the region, and are discussed in greater detail later in this presentation.

- Printing and publishing
- Chemicals and allied products
- Communications
- Business and Consulting services

RECOMMENDATION III: Substituting locally produced goods and services for those previously imported defines a niche for future development. We recommend this option be explored.

The substitution of local goods and services for imported goods and services, or import substitution, is a particularly strong economic growth strategy when it works because it not only provides the direct employment associated with the new facility, but it increases the interaction between local industries. As discussed earlier in this report, local supplying industries are part of the infrastructure that makes a basic industry competitive.

# Printing and Publishing

Printing and Publishing appeared as a top supplier for every basic industry we investigated. While this industry is dependent on basic activity for its own survival, it can also be said that the basic industries in the region depend on this industry for their own levels of competitiveness. Looking at the location quotients reveals that this industry is under represented in the region, relative to the rest of the nation. The IMPLAN system also identifies many of the services and products of Printing and Publishing as being major imports into the region. In other words, this industry is an important local supplier and a good candidate for import substitution.

# Chemicals and Allied Products

This has always been a fascinating industry in Minnesota. It appears again and again as a major local supplier to local industries, particularly in the manufacturing sectors. Yet, when looking at individual components of this IMPLAN identified industry, we find that the industry is under represented in the region and in the state. It is consistently identified as a major import as well as a local supplier.

This may be due to the locational aspects of Chemicals and Allied Products, where plants locate near some kind of supply materials. Or the industry may need to locate in clusters due to agglomeration economies from
proximity. This project was not funded to do specific industry studies, but this might be an interesting one to investigate for future import substitution possibilities.

# Business and Consulting Services

This is a particularly interesting local supplier. It is one of the fastest growing industries in the nation and is a particularly “footloose” industry in terms of location. Yet, when looking at this important supplier, we find the industry to be generally under represented in the region relative to the nation, we also find the region not participating in the national trend of high growth (at least in terms of employment), and we find a relatively large level of imports of these services from other regions.

Consultants are working out of their homes to a greater and greater extent. There is some evidence that they either locate near the amenities and “action” found in large cities or they locate in rural areas where amenities are high. Industry is looking towards consultants to a greater extent than was true in the past because of the outsourcing trend in research and marketing analyses. Right now, the compensation levels in this industry are quite high because of the high level education and training associated with consulting services. This is an important local supplier to industry and might very well be a strong candidate for import substitution.

# Additional Candidates for Import Substitution

We have already mentioned several candidates for import substitution. Mentioned above are probably the most important of the possible cases. However, we can also identify industries that are under represented in the region relative to the nation, meaning that the percentage of employment in the regional industry of concern is lower than the percentage of employment for the same industry nationally.

While this could be interpreted as an industry from whom imports are being secured, it could also mean that a given level of output is being produced in the region with fewer inputs which would constitute a desirable efficiency outcome.
Since we did not analyze these industries beyond the location quotient possibility, a simple list of some possibilities is provided below.

- Advertising Agencies
- General Warehousing and Storage
  Hospital and Medical Service Plans
- Prepackaged Software
- Help Supply Services
- Private Schools and Educational Services, not elsewhere classified (n.e.c.)
- Advertising, n.e.c.
- Computer Programming Services
- Metal Stampings, n.e.c.
- Wood Pallets and Skids
- Data Processing and Preparation
- Computer and Software Stores
- Direct Mail Advertising Services
- Employment Agencies
- Fabricated Metals, n.e.c.
- Agricultural Chemicals, n.e.c.
- Landscape and Horticultural Services
- Commercial Printing, Lithographic
- Direct Selling Establishments
- Retail and Local Service Providers

### IV. POTENTIAL IMPEDIMENTS TO FUTURE ECONOMIC GROWTH

This last section draws primarily on the information provided by focus groups and individual interviews. We asked the focus groups and those interviewed individually what might be their concerns and recommendations for future development. We also asked what government, local development agencies, and the business community itself might do to aid meaningful economic development. What follows is our interpretation of the interview responses categorized by topic.

#### # Infrastructure: Communications, Highways, Housing

There were very strong feelings on the part of the respondents that the region needed significant upgrading of communications technologies. High-speed phone lines, perhaps fiber optic technologies, and related capabilities were mentioned frequently and with a great deal of enthusiasm. There was wide-spread agreement that the current phone system was inadequate to the point of being problematic and a hindrance to future development efforts. There was also wide-spread agreement that the regional phone company was unresponsive to the region's needs.

Needs were discussed in terms of what was needed for the region to keep up with the rest of the world. High speed access to networks, the Internet, and other communications possibilities were clearly in the forefront of concerns expressed in the interviews/focus groups.

If technology industries are to locate in the region, the communications technology must be there to support them. A serious evaluation of where the region is in this regard and what must be done to provide the needed communications infrastructure would
be a wise use of regional and state resources.

One area that could be improved with respect to infrastructure is the highway system between communities in Southwest Minnesota and the Cities. The respondents were not necessarily calling for four-lane highways, although the highway linking Rochester to the Twin Cities was mentioned enviously on more than one occasion. But widening the highways linking the region to the Cities, along with keeping maintenance high, was listed as a priority.

Housing shortages were also identified as impediments to economic development in the area.

# Government Regulation

It is true in most of Greater Minnesota that relations with the population center of the state is of concern. This state is somewhat unusual in that the population, government, research, and growth centers all reside in one set of communities. In some instances, this creates jealousies that are not justified. But in other instances, the potential arrogance that comes with power can create very real problems for the rest of the state.

The primary complaint coming out of the interviews/focus groups was that of excessive government regulation. Coupled with this regulation was a perceived indifference on the part of state agencies--indifference stemming from a lack of appreciation and interest in what is happening outside of St. Paul.

The regulation category most often cited as problematic was the environmental area. However, general rules, regulations, and of course, taxes were also cited.

# Business Sector

A very good conversation came out of the question, “What can the business sector do to help the region develop?” The answer was clearly one of coordination. The interviewees and focus group argued that the business sector must do a better job of articulating their needs to government, to the educational institutions, to development agencies, and even to each other so that policies and programs aimed at helping them remain competitive can be developed. Discussion also identified the potential problem of local firms being so caught up in their own problems and prospects that they miss opportunities to be a bigger part of the community.

One business individual in the focus group took it upon himself to visit local schools with a clearly defined list of what future graduates would need to have in the way of personal and professional skills to work in his company. The list was exhaustive, clear, and to the point. More of this type of activity, on a coordinated basis, was seen as a possible solution to workforce problems in the region. Perhaps development agencies should take on a role that would lead to more discussions between owners and managers of local firms towards the goal of identifying areas where their competitive positions would be improved through community based actions.

# Collaboration

There was discussion on the need to look beyond the community for which any one official had responsibilities and think in regional terms. This type of activity could parallel the business associations suggested above and may even be formally linked in some manner.

There was concern about the links between the region and the Twin Cities. Even though there were concerns about the Twin Cities’ attitudes towards Greater Minnesota, there was also a recognition that the Twin Cities represents the driver of economic development in the state and that what happens in the Twin Cities will frame many of the development potentials for Southwest Minnesota.

The call for collaboration follows from a growing belief that true development can rarely be imposed from the outside, but that it is endogenous to the community. Civic responsibility, associational development, and common works to solve common problems is a big part of this new way of
thinking. The Southwest Region seemed to sense this in their responses to the question of what can be done locally. We would encourage many more discussions along these lines.