

Michigan's Manufacturing Initiative: From Concern to Action

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Politics is about taking extreme, original ideas and misrepresenting them as already being solidly in the mainstream. – Richard Viguerie

It's the economy, stupid. – James Carville

Manufacturing Michigan

The scope of the manufacturing crisis in the U.S. and Michigan is by now well established. The U.S. has lost more than 16%, and Michigan nearly 21%, of their manufacturing jobs since mid-2000. Since early 2001, not only employment but also output has been falling. For whatever reasons, we are “deindustrializing.” (This paper is accompanied by 20 Powerpoint slides, which provide additional data and argument.) As we will see, while some parts of the U.S. may dare not worry, in Michigan we have no such luxury.

Political & Cycle Peaks & Troughs	Date	United States		Michigan	
Clinton-Gore Take Office	Jan-93	16,661,000		798,900	
Pre-Asian Financial Crisis Peak	Jun-98	17,708,000		894,900	
Pre-Recession Peak	Jun-00	17,403,000		912,000	
Bush-Cheney Take Office	Jan-01	16,993,000		842,800	
Latest Available Data (<i>preliminary</i>)	Sep-03	14,556,000		723,000	
	Mfg Output				
Changes:					
Jan-93 - Jun-98	rising	1,047,000	6.3%	96,000	12.0%
Jun-98 - Jan-01		-715,000	-4.0%	-52,100	-5.8%
Jan-01 - Jul-03	falling	-2,437,000	-14.3%	-119,800	-14.2%
Jun-00 - Sep-03		-2,847,000	-16.4%	-189,000	-20.7%

In Michigan, manufacturing is the economy. There is more in Michigan than manufacturing, of course, but any prolonged pain in the factory sector quickly translates into fiscal crisis in Michigan. This is, in fact, *more true in Michigan than in states, such as North Carolina, which have a significantly larger proportion of their jobs in the manufacturing sector*. What makes manufacturing matter so much in Michigan is that so much – both within and beyond the sector – is tied to it. Some obvious examples include production parts suppliers tied to the Big Three, machine-tool and tooling suppliers tied to Big Three and Tier One engineering, engineering

¹ Views expressed are those of the authors alone. The authors acknowledge the essential role of Sean McAlinden of CAR, Joel Rogers of the Center on Wisconsin Strategy (who is advising the Doyle administration in Wisconsin on its parallel manufacturing initiative), and manufacturing extension consultant and former Michigan Modernization Service director Jack Russell. None of these three colleagues should be held responsible for any errors of analysis or political judgment.

service firms linked to new vehicle and component design and prototyping, and business services linked to all of these.

Governor Granholm's manufacturing initiative is thus most welcome. The state has already lost 189,000 manufacturing jobs in the past 3-1/4 years. New UAW-Big Three contracts permit many plant closings and/or asset sales, including quite a number in Michigan. A smaller proportion of Michigan's manufacturing workforce will be covered, in the years ahead, by income security arrangements that buffered State tax receipts over the business cycle. This will be true even if many Michigan plants of Tier One suppliers are organized in the years ahead.

A clear principle emerges from this sober facing of reality: **a high proportion of State subsidies, incentives, and training funds should be reserved explicitly for manufacturers.** Since many of these resources are already directed by the MEDC, which to its credit already has a clear focus on manufacturing, this should not be a hard principle to implement in Michigan.

[Big, Federal, Unlikely, Beyond Our Control](#)

So far, we are stating the obvious, merely recognizing that applying Carville's dictum here means to worry when manufacturing output and employment lag. Much of what can and should be done for manufacturing is, of course, federal, where the pressure points for trade, currency valuation, pension funding, cost of capital, and health care financing all require Congressional action and Presidential consent. It is thus entirely proper that Michigan understand its manufacturing sector, and assess the impact on its future of various federal initiatives under discussion.

But these federal initiatives are uncertain in political feasibility and, even if enacted, in their impact on manufacturing, nationally and here in Michigan. Encouraging domestic investment does not cause that investment to occur in Michigan. Reducing health care or pension financing costs may improve some major Michigan manufacturers' earnings and balance sheets, but these improvements do not necessarily redound to Michigan's benefit. Worst of all, Michigan has very little say in whether and how such federal initiatives move forward.

To Mr. Viguerie's point, then, we need some ideas that are, if not extreme and original, at least bold and local, or – as we will soon see – bold and *regional*. We have been working on these ideas, and we offer them for comment, critique, and maybe just a little concurrence. If many of them do not strike our limited intended readership as controversial, then we have failed.

[Bang on the Congress and the Regulators](#)

The best of the several federal initiatives are probably those contained in the Michigan Democratic caucus letter to Bush, thanks to the knowledge and hard work of Sandy Levin's staff. But even these initiatives are almost completely national in character, with the exception of the call for increased R&D for advanced motor vehicles. In our view, Michigan should have its own program for future vehicles, which is clear-eyed about what is, and isn't, real. We will return to this point shortly.

There are two things not in the “Levin Package” that Michigan needs the fed to look at. Both have regulatory as well as legislative aspects, and both may have “deregulatory” appeal on both sides of the aisle in Congress:

1. **Seek more relaxed anti-trust rules for collaboration among small (sub-500-employee) manufacturing firms.** Currently, pre-competitive collaboration is permitted in some areas. But small companies in such key Michigan industries as tool & die need to be able to collaborate in precisely the areas in which they compete, to be able to join together to quote business consortially and collaboratively. This new business model is effectively limited by anti-trust law and its enforcement. MEDC is funding an MMTC-centered collaborative EDJT project in this area already, and needs to do more. This will be easier and more effective with the feds’ nod.
2. **Seek more effective DOD “Buy American” purchasing policy and behavior** in key Michigan industries, including again tooling. This is good national policy, and not “pork” for Michigan, and should therefore be at the top of Senator Levin’s agenda.

On these two, there should also be ready allies in the delegations of the Upper Midwest states. Such a regional coalition is a better bet today than at any time in memory. The Michigan-Indiana business climate war is over; Illinois and Iowa have manufacturing-focused Democratic governors; and Governor Doyle in Wisconsin is mounting a manufacturing initiative in his state that is uncannily like our own.

Define and Convene Our Region

There are many manufacturing-intensive states, located in many regions. Many of those states and their regions are Michigan’s competitors. Some of the policies that are “good for manufacturing” are better for those regions than for us. But, while we will need a Michigan-only strategy, we will do better if our region succeeds as well. And just what is our region? The answer is more than a matter of map-reading, or even of seeing whose shores the Great Lakes wash up on. Common sense and input-output analysis both confirm that **our region is Michigan, Indiana, Ohio, Illinois, Wisconsin, and perhaps Iowa**, at least from Greater Des Moines east. *These states, and only these states², share what is, viewed from a high enough altitude, a single, complex supply chain of complex mechanical assemblies, and their constituent parts, that feed the region’s dominant export industries: automotive, heavy truck, construction equipment, and manufacturing tools and machinery.* These industries (though not them alone), and their supply bases, are what defines every economy in the world that seeks to apply science, engineering, and technology to producing the goods whose use raises global living standards. With the possible exception of Britain, no developed economy in the EU (and certainly not Japan) allows these industries to languish.

Because these industries, despite their current stress, are the world’s envy, other US regions desperately want them. Michigan’s manufacturing policies need to support our region in its life-or-death competition not just with “China,” but with our biggest competitor, the upper south. This region, which extends north and south from northern Kentucky to central Alabama and east

² From a regional trade perspective, southeastern Minnesota, extreme northwest Pennsylvania, and New York from Syracuse west also function as part of the region.

to the Carolinas, has targeted our region's industries – first their assemblers, and then their suppliers – just as surely as Japan's Ministry of International Trade & Investment (MITI) targeted them in the 1960s and 1970s. Michigan needs to go to school with Indiana, Ohio, Illinois, Wisconsin, and Iowa (hereafter, MOWI³) rather than going to Washington, DC with the governors of North Carolina or California, however “manufacturing”-intensive their states may be.

We recommend, and hereby offer to help, the Governor work to convene a **Regional Governors' Conference on Manufacturing Renewal** in the near future. The content and the roster both should be informed by the arguments of this paper. Like the Governor's upcoming Michigan manufacturing summit, the emphasis should be on gaining broad support for a well-thought-out agenda that favors better-performing (sometimes called “high road”) manufacturers, and care should be taken not to allow large multinational companies to stifle the voices, and interests, of better small companies. We believe we could corral foundation funding and follow-on interest in such a conference; Dan Luria and Joel Rogers (see footnote 1, page 1) are already in discussions with several foundations about this pre-step to a “high-road onshore manufacturing association” that would move beyond least-common-denominator policy fixes that amount to little more than aids to “a race to the bottom.”

We also recommend bold thinking about **cross-state subsidies**. For example, providing a training grant to a northern Indiana manufacturer that supplies a critical part to a component made in Michigan and shipped to a Tennessee customer might be a political nightmare, but it makes a lot more sense than helping a company that sells its wares to Michigan wholesalers or retailers. Indiana is said to be doing some of this already. The logical extension of this is to have a rationalized system of “export incentives” for the MOWI³ region.

Financing Manufacturing Renewal

It is widely believed that Michigan has no money with which to move its economy forward. But we now present three “extreme, original ideas” that suggest that this is not the case:

1. **Stop placing long-odds bets on glitzy flavors-of-the-decade.** Fuel cells as anything but replacements for diesel backup generators are not around the corner. The Big Three, despite what they might say, are neither sanguine nor inclined to devote serious resources. In the near-term, they are going for 5-15% increases in fuel economy by tweaking transmissions and selling some low- and mid-volume gas-electric hybrids. Medium-term, their plans are for diesels, on which all are working closely with their European and Japanese partner OEMs. Nanotechnology could make small things big, but State investment won't play much of a role, and having world-class universities will hold the techies here far more effectively than a few tens of millions. In “life sciences,” it's the same story: maybe a big payoff somewhere, someday, on something; but again big state spending here amounts to gambling with the milk money. And what does any of this have to do with the world-envied supply chain underlying automotive, heavy truck, construction equipment, and manufacturing tools and machinery? Michigan, along with most other states, is buying incredibly expensive “lottery tickets.” Gambling is not the way a revenue-strapped state maximizes the return on its spending. We recognize that some low-cost, high-visibility initiatives may need to be retained as cover. We

acknowledge that there have already been substantial cuts in some of these initiatives; keep it up. The simple point is that there is plenty of money available to do “economic development” right. This will be even more true if we ...

2. **Stop giving taxpayers’ money to companies**, including manufacturers, **that don’t provide good jobs**, don’t “export” their output and thereby bring in income from beyond the state or region, and don’t buy their inputs in the state or region. We will explore this point in much more detail below, but suffice it to say that today Michigan showers much of its limited, but still substantial, largesse on companies that do not meet these criteria. (We strongly recommend the organization Good Jobs First, which has an excellent website, for the argument and tools about “targeting” assistance to the companies that really contribute to the economy.)

3. **Start really focusing on return on investment (ROI)** . We’ve already talked about the low ROI on big “high-tech” bets, including the recent proposal to get former corporate technology “experts” to assess the patent potential of in-state R&D. Focusing on ROI also includes getting something in return from companies we support. Over the past 12 years, State government tried hard to indulge local economic developers’ desire to remove what few strings there were on tax abatements and other subsidy packages. This needs to be reevaluated, and thought is needed on the most effective conditionalities for State aid. It also means preferring to provide aid in forms that guarantee the results rather than hoping for them. Tax credits are generally a bad idea: they attract opportunists and free riders, and have a revenue cost that cannot be predicted. Direct service to companies for technical upgrading and direct grants to pay for worker training are better. And they’re better still if they are reserved only for firms making real income contributions to the state (good jobs, “exports,” local purchasing), and for technical assistance and/or training that is (1) consistent across the state and (2) portable – both so the trainee has mobility from less good to better employers anywhere in the state, (3) modular, so that money is not wasted on “development” and hence more people can be trained per dollar.

Healthier & Cheaper

Health care financing is ruinously expensive for the majority of Michigan manufacturers that provide decent coverage for their employees. The big fixes, if they ever come, will have to be federal in policy and single-payer in content. There are some revenue-sapping federal ideas on the table, notably the Gephardt credit and some of its variants. We’re not holding our breath, nor are we waiting to exhale.

Large state purchasing pools can be a step toward lower costs, toward taking health insurance out of competition among firms in the state, and toward reducing Ontario’s advantage relative to Michigan. The basic design specs are: everybody in, public health investment, severe cutbacks in redundant equipment and advertising, and the application of zero-defect quality and “lean manufacturing” techniques in the health care sector. California has an all-in, pay-or-play model that’s worth study and, perhaps, imitation. Illinois and Maine have innovative initiatives on

prescription drug purchasing from Canada. (Don't sweat the Big Pharma campaign against it: Canada's FDA is better than ours, and NAFTA probably backs up buying our drugs there.³)

Cleaner & Faster

On the environment-manufacturing interface, Governor Doyle in Wisconsin has this right. We should seek **the highest environmental standards, but the quickest permitting**. *The Michigan Automotive Partnership has identified nine steps* to take time out of the permitting process without sacrificing environmental quality. These already have MEDC blessing, and the State should move on them.

This approach should be part of the regional approach outlined above as well. With Wisconsin already fully on this wavelength, the job is already partly done.

Michigan continues to have higher **electric rates for industrial users** than most other states. This is particularly true for DTE customers. Some effort is warranted to negotiate lower rates for these users. The impact of resulting higher rates for low-income residential consumers can and should be offset by increased energy assistance. Finally, the State's major utilities need to be jawboned into higher efficiency, much as the Governor has done in her dealings with the Detroit Medical Center. Modest State investment in energy efficiency makes sense on its own terms, and would help to offset higher residential and commercial rates.

Enhancing the Regional Supply Chain

First, a little manufacturing history. In 1978, Michigan had well over twice the number of hourly Big Three jobs it has today. Yet nationally, employment in the automotive sector is almost identical to its peak of 25 years ago. What's changed is that much of what used to be done in the Big Three has either started to be done by the North American facilities of Toyota, Honda, Nissan, and others, or by large Tier One suppliers. While Michigan has most of these suppliers' technical and sales centers, it hosts a relatively small share of their manufacturing facilities.

That needs to change. Tier One suppliers are the state's single largest opportunity to get its workforce connected to the transplants rather than only to the Big Three. With the new UAW-Big Three deal, these companies will be offering good jobs, whether under UAW contracts or as a means to avoid them. As we will see, training grants are our largest point of leverage for both attraction and expansion of this critical slice of manufacturing.

An emphasis on supporting **local purchasing should inform the conditions for helping these and other manufacturers**. Tax breaks (less preferred) and training subsidies (more preferred), whether for a GM plant the State seeks to save and grow, or for a Bosch or Denso plant the State seeks to attract⁴, should come with realistic floors on in-state and/or in-region purchasing. A GM assembly plant that buys stampings from an Ohio stamping plant that buys steel from a

³ As to Pfizer's objection, why not simply ask that company to contribute its projects to the buying pool at or below the Canadian price? This seems a reasonable *quid pro quo* for generous, on-going State aid.

⁴ These examples are not chosen at random. Facilities of these important, technology-rich global suppliers are available to Michigan, particularly if the right training package can be assembled.

Michigan mill is a far larger economic contributor than a Michigan stamping plant that buys steel from a mill in Georgia. And since companies can change their sourcing, Michigan needs to be clear with the firms it aids what it expects from them, and over what period of time.

The Governor should use the back-room version of her bully pulpit to **jawbone the Big Three, the transplants, and major Tier Ones to buy more of their manufactured inputs in Michigan** or, at the least, in the region. Both the Big Three and the transplants should be leaned on, in particular, to do more of their tooling buy here. The message should be: “We can and will do more for you than we have, but only if you behave in a way that helps all of Michigan manufacturing succeed.”

Exporting beyond the US is also important. With the US dollar likely to fall further in the quarters ahead, more **offshore sales** by Michigan manufacturers are a real possibility. The largest of these will be to other developed countries, primarily in the EU. Yet the State’s only two export-promotion offices are in Beijing and Mexico City.

[Taxing Manufacturing](#)

Michigan recently enacted a lien law for its moldmakers. The point of this law was to ensure that these shops get paid on a timely basis. It’s been effective for mold sales to in-state customers, but less so out-of-state. A regional effort is needed. Moreover, other industry sectors – including die-making, special machine-building, and prototyping – badly need this protection as well. Several states in our region have such laws, as we understand it, for their entire manufacturing sector. We think Michigan should **extend the mold lien laws to all of manufacturing, and to customers in our in-region neighbor states**, as well. Large customer firms will oppose this, as it opens them up to liability when they don’t honor agreements. (They will cave, however: It’s never good PR to object to honoring your contracts.)

We do not see significant inequities for manufacturers via-a-vis other sectors in Michigan as a result of the **Single Business Tax**. Longer term, if and as the Granholm Administration considers how to amend or replace the SBT, several important principles should be considered. The first is that good jobs in manufacturing are very often associated with high capital-intensity; firms that use a lot of capital equipment should get tax benefits that labor-intensive firms do not. (On this count, the SBT has a lot to recommend it, by the way.) Revising State tax law to assist capital-intensive manufacturers, and manufacturing as a whole, won’t be revenue-neutral, obviously, unless some sectors pay more taxes than they do today. We think **a prime target for higher business taxes should be large commercial developments, aka malls and office parks**. Such a tax policy tilt is fully consistent with the Governor’s stated desire to reduce sprawl and its attendant costs.

[The Right Upgrading for the Right Manufacturers](#)

The authors work for the MMTC, which gets \$1.5 million from the MEDC’s “corporate” funds, which currently come from casino gaming. Until two years ago, MMTC got \$2.3 million. These funds “match” a grant of \$2.25 million from the NIST MEP program in the US Commerce Department. MMTC also does \$500,000 or more in EDJT-funded training each year. Manufacturers are happy with the service, and report large sales, investment, and cost-savings

impacts. MMTC is thus an example of an efficient direct service investment: it serves the key sector, it only provides what firms in the sector want, it leverages federal dollars, and it connects properly to the State's main manufacturing training program (EDJT). The only reputable study of the state revenue impact of an MMTC-like program, which looked at the Industrial Resource Centers in Pennsylvania, concluded that each \$1 of State support resulted in \$1.24 of State revenue.

MMTC also provides informal support to nearly every manufacturing-related initiative in the state. This paper, and the research behind it, is one example.

We believe that **MMTC should have more support from the State**. This support should be tied to the objectives laid out above, i.e., *the incremental effort should be with firms that provide good jobs, export from the state and region, and buy inputs within the region* and preferably the state. An early priority is to come up with a clear, transparent, and consistent measurement system to assess how manufacturers seeking State-supported technical assistance and/or training stack up against these criteria. Those that stack up well should get more help than they have in the past; the rest should get less, or none.

MMTC service, as well as the State's other types of support for manufacturers, should be conditioned on an **objective assessment, or benchmarking, of companies seeking service**: the services should match the needs, and be tied to performance improvement objectives. Happily, MMTC already is arguably the nation's leader in benchmarking the performance of small and medium-sized manufacturing companies. The State needs to take much more advantage of its investment in this resource, using it for MEGA applications, EDJT applications, and more – anything in which the content of training or direct assistance depends on performance. As training becomes more modular (see below), benchmarking can be an important input into deciding which modules need to be implemented.

In addition, service should be constructed to be efficient, and that will often mean serving **groups of companies**. While our work finds the concept of industry, regional, and industry-regional clusters somewhat unconvincing, there is no question that group projects work at least as well as individual-firm projects and do so for less money per firm. This group concept will be particularly important when it comes to spending training money for smaller companies (see below), as opposed to for OEMs and large Tier Ones. Again, the emphasis should be on firms that are in the region's key supply chains, even if they are in subsectors that are not large. Thus a group of small stampers and molders trying to integrate their processes into a common assembly are a better bet than a group of printers or food processors.

The State may have other objectives to which it seeks to tie increased support for technical assistance providers, e.g., **more service to companies in Detroit and other distressed "core cities."** However, in doing so, it is important not to let geography trump the larger objectives of good jobs, exports, and local purchasing.⁵

⁵ A good approach might be to condition increased assistance to a requirement to try to visit and assess every core cities manufacturing plant with, say, 50 or more employees. The assessment requirement would be one way to build a census of all of the "good" urban plants. Such plants, and others with a potential to look like them with a little push, could then become the focus of intensive, coordinated service delivery. The same can be said of statewide

The Right Training for the Right Investors

Training is an essential complement to the investments we want manufacturers to make in Michigan to produce products they export from our region. The previous administration properly focused much of the work of its lead economic development agency, the MEDC, on manufacturing retention and expansion, but at the same time cut the training resources available to help with the job from nearly \$70 to barely \$10 million. Despite the collapse of the accounting-polluted dot-com boom, and the decline in manufacturing jobs that began in mid-1998, the State continued its unaffordable, high-stakes high-tech gambling strategy. The State's portfolio should move away from these long-shot bets and put **more money into spent on high-quality, modular, portable training for manufacturers** that better express the risk tolerance of a state with limited resources and a firm knowledge of what drives its economy.

A recent CAR study of incentives to automotive OEMs and Tier Ones found that, while Michigan is "competitive" (apologies for this use of the term) in most areas, we spend much less than our competitor region, the southeast, on training and the wages of those in training. The CAR study found that new upper Midwest auto plants got "recruitment and training" subsidies averaging about \$1,000 (3% of \$38,100 per job), versus almost \$16,000 for new southern auto plants (18% of \$87,300 per job). Training is the most defensible part of these dubious packages: the workers get skills. The more such training fits the consistent-modular-portable spec, the more those skills are likely to hold that Michigan worker in good stead, even if the particular employer goes away or the worker switches to a different one.

Much of the content for these modules already exists, some of it in excellent Big Three training materials. The development of much of it was paid for, in whole or in part, by the State, which may well have no official memory of it. Meanwhile, WIA money flows to local WIBs that spend much of it developing training content that may already exist. Two different WIBs may be paying for the development of nearly the same curriculum content. **The Governor needs to assert content control over the statewide WIB**, which must in turn discipline local WIBs to focus on the right training content. Note that a WIB that, beyond its TANF role, shared the Administration's focus on manufacturing could aggressively accumulate federal resources beyond the \$12-15 million that flows through it today, notably from the US Labor Department's H1B program, to which employers hiring non-citizen technical personnel must pay fees. This is crucial, since Michigan's Congressional delegation is, sad to say, in a comparatively weak position to secure Labor/HHS, Defense, or CJS federal earmarks.

WIA funds, EDJTs, H1B's and the rest of the alphabet soup should be thought of as **a single training "budget."** **At least 75%** of that budget, as in Gov. Doyle's Wisconsin plan, **should be reserved for manufacturing.** As noted above for technical assistance, training should be preferred if it is for workers from a group of firms learning together. Consortial learning among smaller firms, especially if it includes a component that helps grow these firms markets, is the highest and best use of training money.

technical assistance: **the State needs to know which companies have distinctive competencies that position them to succeed and to export profitably from our region** to the rest of the US and the rest of the world. Under new Governor Ed Rendell, Pennsylvania has already issued an RFP to determine which manufacturing subsectors and companies in that state can compete on this basis.

And if Michigan is to spend more on training for manufacturers, and spend it more efficiently, what should it ask from OEMs and Tier Ones, and what should it ask from smaller manufacturers? In all cases, it should **focus training support on plants and workers that get paid at least \$14 an hour**, the amount that recent budget studies conclude is required to support a family without overtime work. (Because the state does need to address school-to-work and welfare-to-work populations, of course, some portion – not to exceed 10-15% -- of the training budget should be reserved for these purposes.) In all cases, it should **build the queue so that the front of the line is clogged with firms that are part of the region’s core supply chain**, i.e., making parts or components for automotive, heavy truck, or construction equipment, and not, for example, for screen doors.

Implementation

We are not politically savvy enough to know how to move many of these proposals. At the extreme, there are two models, neither of which may be right. One would be for the Governor to **name a “czar”** of the manufacturing initiative. On the plus side, every good idea needs an effective, ruthless tyrant. On the other hand, the opposition in the legislature could easily personalize the initiative to bad effect. At the other end of the spectrum would be the “final year of Clinton” approach of **many quiet, small initiatives that add up** to something larger (*aka* the Kennedy-Specter approach to kids’ health care). This has much to recommend it, but intrinsically lacks any energizing character. No doubt, there are some good hybrids, e.g., loud and public on a Governors’ Conference, quicker permitting, and a health care cost fix; but quieter and subtler on the training, technical assistance, and partial de-funding of expensive, risky bets.

We welcome your criticisms and questions, and are at your disposal.