V. Conclusions: The End of the Beginning

Review and Outlook

The Midwest economy is now firing on all cylinders. Almost all subregions and industrial sectors are growing and the geography of prosperity is widespread. Nonetheless, we recommend that the region continue to assess those challenges and chronic problems that good economic times tend to disguise. Even in its success, the region remains challenged to produce high-paying job opportunities and the skilled workers to fill them. Current data suggest that the region's success is somewhat skewed toward higher labor force participation, while income growth (most of which arises from work force earnings) still has room for improvement and has not recovered to previous heights in relation to other regions.

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How do we go about keeping the Midwest on the track of prosperity? Because the region now has some financial respite and because we have some knowledge of the way that the global economy is changing, this is an opportune time to ask, what are the key challenges ahead?

The underlying causes of the Midwest's economic revival suggest reasons for cautious optimism about the future, but also recommend vigilance and a recommitment to economic renewal by the region's decisionmakers. A common theme that runs through this entire report is the critical restructuring of the region's industrial base during the past ten to 15 years. Midwest industry's achievement of a position of competitiveness in international markets has been strongly linked to the competitive stimulus of imports from abroad, the technology transfers associated with and competition derived from foreign direct investment in major Midwest industries, and increased interregional competition within U.S. borders. During this time of adjustment, the region has done much to bring about its own success. Still, the Midwest should be focused on continual improvement, because changes in external forces over which it has little control may turn against it in the future. If external forces do turn against the region, there will be a much appreciated dividend that the region can achieve through its own devices, in terms of productively employing people and resources.

Are there currently signs of external reversal? External forces such as export demand and federal spending patterns continue to be favorable, though, as always, there are concerns on the horizon. The regional growth effects of defense cutbacks over the past ten years are leveling off as the defense budget stabilizes. The terms of trade versus one competitor, Japan, have recently been moving in Japan's favor, which may pressure domestic automotive production. In addition, the downward trend in real energy prices, which has steadily assisted heavy manufacturing in recent years, was disrupted, at least temporarily, during 1996.

The Midwest should also recognize that it remains steeped in industries that perform erratically over time—durable goods manufacturing and production agriculture. The recovery of these industries has indeed provided a boost to the region. However, the Midwest's volatility relative to other regions owing to these industries has probably not been altogether repealed. Consequently, its progress in growth, investment, and innovative public programs will likely be tested during the nation's next recession. At the same time, these key individual industries and areas continue to undergo profound secular restructuring. In addition, the region's legacy from its previous economic development continues to present challenges.

Optimism for the future is based on the observation that, with regard to changed behavior, success often builds on itself. The Midwest owes much of its success to its own hard-fought efforts. Some firms have closed, some industries have downsized, and still others have begun anew or made difficult transitions to new technologies and modes of operation. The region's industries are now keeping a vigilant eye on their global competition, and are attempting to stay on the vanguard of technological changes. While the region cannot as yet be singled out as a leader in entrepreneurial business climate, culture, and support, it has moved forward significantly in this regard. Similarly, much of the region's work force has learned well the lesson that well-paying jobs cannot be taken for granted—life-long learning must be adopted as a model for continued success. The public sector's conservatism in public spending continues to serve the region well, even as it has gained renown as an innovator in restructuring public responsibilities such as education and welfare. So too, the region's long period of prosperity has helped to build institutional capital—private sector networks, foundations, and nonprofit organizations—which continue to chip away at social and economic challenges.

All of this suggests that Midwest policymakers should neither be congratulatory nor complacent in their views of the region's current success. Much remains to be accomplished and, over the longer term, there do not appear to be any discernible natural advantages or reliable external trends that will sustain the region. For the region to continue to prosper, public and private decisionmakers should work very hard to maintain its competitiveness.

Blueprint for Action

The wealth of material presented in this report has made it clear that there is little room for one-size-fits-all policies to support regional growth. The following blueprint for further analysis and action is therefore described in three broad themes:

- An increased emphasis on education and work force training;
- A heightened attention to and evaluation of region-specific public policies; and
- Understanding and adapting to changing industry restructuring, location, and technologies.

On the surface, these themes appear simple, but designing policy to enhance the region's economy requires a careful understanding of the interconnections between these areas. In many ways, all of these themes reflect the importance of regional adaptation to globalization. Ironically, as the world economy becomes more integrated, regional differences and policies become more important.

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Education and Work Force Training

In today's globally competitive environment, a human capital advantage has come to mean more to relative prosperity and income, as natural resource and location advantages have come to mean less. These are compelling reasons to fashion efforts to enhance the region's human capital stock.

Technology and information now add more value to goods, products, and services in general, so that economic returns to factors having these features have heightened. At the same time, there are now increased global trade and capital flows; manufactured goods have generally become smaller and lighter; services have become increasingly portable (and tradable); barriers to trade have fallen; and both financial and physical capital mobility have increased. These trends have allowed a sharper specialization along the lines of each nation's and region's comparative advantage, and the U.S. specialization has shifted towards technology- and information-intensive goods and services. The upshot is that, for U.S. regions, the human capital stock of their (still mostly immobile) work force may be the only sustainable advantage in growth and relative income.

This presents both opportunities and challenges for regions. One implication is that, where appropriate, public sector and private sector actions to enhance human capital and employability will do much to improve a region's well-being and growth path. Now especially, with much of the nation's economy at full capacity and with the economic structure coming to favor skills and knowledge, regional growth opportunities are being determined by available supplies of skilled labor. The quality and pervasiveness of a region's private and public educational institutions and labor training programs encourage expansion of existing companies and provide a basis for luring new firms and establishments.[97]

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The Midwest appears to have some catching up to do in work-based learning and school-to-work transition programs. A recent study suggests that the Big Three auto makers will lose over 200,000 workers to attrition and retirement between now and 2003.[98] It is not surprising that the region's infrastructure to teach students in technical trades fell into disrepair following the early 1980s, when the region saw 20% of its existing manufacturing jobs disappear and few new industrial workers were needed. However, the industrial renaissance has now caught up with the labor force.

The heightened importance of skills, along with greater turnover of both jobs and skill needs, also suggests that efforts to provide and certify skills for workers (perhaps continually over their lifetime) will serve both workers and the firms who must recruit them. One such example is the project being led by the Council of Great Lakes Governors and the National Tooling and Machining Association to develop Metalworking Skill Standards. This project is moving along several fronts to identify, train, and certify those skills used by metalworking industries.

Problem areas continue to be central cities and low-income urban neighborhoods. New job openings there typically require skills that do not match the skills of the unemployed. Central city–suburban job networks and programs may be part of the answer. These efforts attempt to provide transportation to remote jobs, find affordable housing closer to job sites, or enhance the information network that is needed for semi-isolated workers to learn of job openings. More general efforts to ensure effective schools at the elementary and secondary level will continue to pay off for the region, but the political obstacles may be high and innovations in education delivery, though numerous, remain small in proportion to the school age population.[99]

Regional Policy Importance

In a globally competitive environment, decisions on investment are more sensitive than ever to cost and amenity differences and, therefore, more likely to be influenced by regional policy. So too, much of today's current federal legislative momentum favors a return of regional authority to the local level. Among issues under discussion are work force policy and training, welfare design, elementary and secondary education, and region-specific (ecosystem-specific, region-wide) environmental policies.[100] For example, in the area of labor force training and income assistance, the recent transfer of welfare responsibility will effectively penalize states that are unable to bring their welfare-receiving families into the work force. Successful regions will have an advantage in terms of both federal funds and economic growth in the years ahead.

One less-obvious application of the importance of regional policy decisions arises from the observation that wealth creation in the region continues to rise because its borders have been open to commerce both internationally and across state lines. Some observers have pointed out that Europe is struggling to establish what the U.S. has already achieved—a common currency area with minimal cross-border barriers to trade, investment, and migration. Evidence was brought forward that the preponderance of trade for any given Midwest state continues to be internal to neighboring states in relation to trade abroad. The question then arises whether the Midwest should strive to stay ahead of the curve in this apparent advantage. Further research and public policy analysis along these lines should investigate remaining interstate barriers in the Midwest such as unnecessary occupational licensing, cross-standards for freight hauling, and lack of tax harmonization.

Midwest states should reexamine the principles and practices of how they tax business activities and business entities.

Some have suggested that the common practice of selective tax incentives is just this sort of interstate trade distortion and that the federal government, or cooperative state agreements, should prohibit or circumscribe the practice. Others believe that states should continue to hold such prerogatives, but that more informed and rational policies on the part of states are called for. While this issue will continue to be debated, it is clear that regional tax and spending policies are likely to be more decisive than before. As global competition has worked to heighten the effects of tax differences on the location of capital and labor, Midwest states should reexamine the principles and practices of how they tax business activities and business entities. Shifts toward taxing business in alignment with the costs of services businesses receive from state–local government would be a direction for improvement.

Changing Industry Structure, Location, and Technology

A final broad area of challenge to the Midwest is the necessity to adapt to ongoing and unfolding technological and industrial restructuring. The heightened degree and pace of global competition is hastening the geographic division of labor, compelling regions to readily respond and adapt to changing work force and infrastructure needs of business. Because distinctly different trends for urban and rural areas were identified, we present these changes separately.

Urban Cores and Metropolitan Areas

In metro areas, core counties continue to shed manufacturing jobs which, in the past, have provided one avenue to the middle class for central city households. Financial, travel, and business service industries are successfully replacing manufacturing in urban cores and metropolitan areas. While many of these industries offer high-paying jobs, the required skills do not always match up well with urban populations. Accordingly, a higher premium is placed on educational and training programs even though many inner-city public schools are perceived to be failing in their efforts to educate a rapidly growing young population.

A second concern relates to the pace of job growth in urban core areas. Many central cities will continue to face the many problems of transforming to a lower density of living and working as the tendency has been for jobs and the most mobile population segments to disperse to the periphery of metropolitan areas. It is an unsettled question as to whether this dispersal arises from natural, underlying economic forces, or changes in technology, or whether government policies and incentives encourage lower density. Much more needs to be understood about why firms and people continue to spread out within metro areas, whether these trends will continue or stabilize, and whether public policies are needed either to ease the transition or to stem the dispersal.

Third, a high degree of proliferation and fragmentation of government may pose no less a challenge for suburban governments than for the central cities of large urban areas in the Midwest. In some regards, central city governments may benefit from there being many adjacent governments which can work to keep costs down and quality up through competition among suburbs for residents and firms. On the other hand, some observers believe that, as economies have outgrown their cohesive city government boundaries, metro area decisionmaking has become overly fragmented. Related to the fragmentation of suburban government is the fact that land use and development decisions are being made by many small (mostly municipal) entities. Insofar as small local governments exercise land use controls in their own interests, the larger interests of surrounding communities may be neglected or harmed.[101]

Rural Communities

Despite the sharp rebound in nonmetro counties, rural population growth still lags that of urban areas.

Rural communities face many challenges if the gap between rural and urban population growth is to be narrowed. Despite the sharp rebound in nonmetro counties, rural population growth still lags that of urban areas. Declining population threatens the viability of many rural communities, where some minimum population scale is needed to maintain schools and other public services and retail accessibility.

Much of the downward population pressure facing the rural Midwest derives from the continuing productivity gains in both agriculture and rural manufacturing. Those gains are prerequisites for maintaining a competitive edge in an increasingly global marketplace. They also can translate into fewer jobs, despite expanding output. Looking to the future, the mega farms that characterize the latest wave of agricultural restructuring foreshadow continued declines in the number of farms and farm families. Perhaps more critically, the issues surrounding mega farms raise concerns about whether the Midwest will retain its dominance in pork and milk production and related food processing activities.[102] Moreover, in the case of hog operations, midwestern states may face a difficult choice—to accommodate the environmentally noxious demands of new hog operations or to risk losing this industry to other regions.

Despite increasing location of manufacturing in rural counties, the relative wage gap in manufacturing between urban and rural areas has actually widened. This echoes a similar trend in business service industries. While in some instances, lower wages may indicate an improved competitive position for a region, this is probably not the case in this instance. Throughout much of the past ten to 15 years, urban areas have been specializing in the high-paying skilled segments of business services, finance, and corporate administration of goods-producing industries, while manufacturing production activity has been shifting to rural areas. The productive edge which has come about through enhanced communication and air travel has, so far, favored large urban areas in this regard. This presents a challenge to rural areas in providing not only jobs, but high-paying, high-skilled jobs.

A Future that Requires Better Regional Information

A common finding throughout this project has been unrelenting globalization, leaving behind industrial restructuring and a scramble to reshape public policies that can ease the needed adjustments. As the world integrates economically, decisions at the regional and local level become increasingly important. One-size-fits-all policy options will therefore be less relevant as region-specific conditions and behaviors increasingly need to be taken into account in policy formation. However, innovative regional policies can only be fashioned with better information and data on local places, along with widely communicated analysis of how policies are performing elsewhere, and why.

The domicile of such analysis and information is not as important as the necessity for it to be available and communicated to those who must fashion policy in multistate regions, states, and local areas. The project *Assessing the Midwest Economy* represents a first step in that direction, a step which will lead to others, both by us and by you.