



MICHIGAN  
CHAMBER

Foundation

2012 Michigan Economic

# COMPETITIVENESS STUDY



*An analysis of issues to advance Michigan in a complex global economy*

# 2012 Michigan Economic Competitiveness Study:

An analysis of issues to  
advance Michigan in a complex  
global economy

Executive Brief

## About the Michigan Chamber Foundation

The Michigan Chamber Foundation was established as a non-profit supporting organization to the Michigan Chamber of Commerce in 1985 for the following purposes:

- To plan and conduct nonpartisan public education programs regarding free enterprise, productivity and basic economic issues affecting the state of Michigan;
- To establish and operate a leadership institute designed to provide promising future leaders assessment of Michigan's assets, challenges and opportunities to give participants the background and network of contacts necessary to make a positive impact on Michigan's future;
- To conduct nonpartisan research and distribute policy studies on issues facing Michigan including, but not limited to taxation, government regulation, government spending, health care and transportation.

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## Introduction

The purpose of the study was to conduct a comprehensive analysis of the Michigan economy and evaluate its rank and performance across a number of metrics including, but not limited to, Gross State Product (GSP) growth, tax policy, regulatory policy, and cost of doing business. Accordingly, the focus was primarily on the Michigan economy and its outlook for the future. It accomplishes that objective by focusing on different aspects of the Michigan economy and compares it with all other states within the United States. The study briefly outlines the current state of U.S. competitiveness in the global economy and then focuses on Michigan's economic performance relative to national averages and the other 49 U.S. states. It is important to note that the Michigan economy moved in tandem with the U.S. economy in the sense that both experienced a decline in competitiveness relative to its competitors. In order to find answers for what contributed to this decline, the study's authors conducted a comprehensive survey of the literature regarding sources of economic growth to determine what was absent from or hindering the Michigan economy. The authors focused on productivity in Michigan and the factors that impact productivity. Specifically, the study focused on tax structures, the regulatory framework governing businesses, education and other components reflected of the general business environment. With a focus on productivity, this study also analyzed the issue of Right To Work legislation both at a theoretical and an empirical level. The results are interesting to say the least. Although the topic is controversial in some quarters, the results deserve serious attention and discussion at all levels of the public policy decision making process in Michigan.

To begin, there is fundamental agreement among economists as to the sources that drive economic growth. There are definite reasons why some nations grow and others don't. Robert Barro (1991) in his seminal paper, "Economic Growth in a Cross Section of Countries," tried to answer that question. He studied the key economic and political factors that determined 98 countries' competitiveness that led to economic growth and standards of living. It is clear from his study and others that economic growth is helped by investments in human capital, lower tax

rates, a lower regulatory burden on businesses and emphasis on the overall human development matrix. It is also clear that the U.S. has been steadily falling behind in these critical investment areas, or at least unable to keep up with the investments vis-à-vis its competitors. Also, government is becoming increasingly more important in the overall scheme of things as compared to the private sector. In addition, the federal government budget deficit and national debt is growing alarmingly high and the financing of the deficit has been instrumental in increasing the cost of capital, making it difficult for private businesses to invest in critical areas. Many economists would argue that this unprecedented increase in government spending has been the primary reason behind the relative decline in American competitiveness. In the appendix of the study, numerous tables and charts are provided that highlight this decline in U.S. competitiveness.

The 20th century clearly was the “American Century.” The 1900’s saw the United States become the world’s largest, most productive and most competitive economy while also becoming the world leader in invention and innovation. However, towards the end of the 20th century, grave concerns began to be voiced as to whether or not the U.S. could maintain its standing in the global economy. Income growth and job growth began to slow toward the end of the 20th century and has continued to slow into the 21st century. While this was happening, it is also true that government was becoming more and more significant in the U.S. economy. According to the Congressional Budget Office and the Heritage Foundation, government at all levels in the United States consumed less than eight percent of GDP by expenditures in 1902 and today consumes more than 42 percent. The U.S. now has the highest corporate income tax rate in the industrialized world at 39.2% (the industrialized world average is 24%) according to the Tax Foundation, not because the U.S. has raised taxes, but rather because many of its competitors have lowered their rates over the last decade. Based on 2010 data, the U.S. also has among the highest long-term and integrated capital gains tax rates in the industrialized world at 19% and 51.5% respectively. The U.S. tax system has become more and more burdensome and has contributed to decline in U.S. competitiveness.

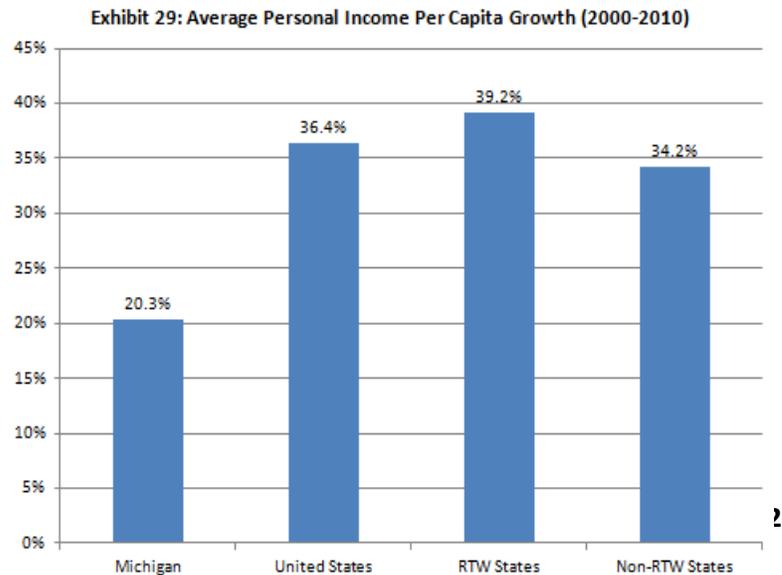
The 2012 Heritage Foundation/Wall Street Journal's *Index of Economic Freedom* measures political freedom, prosperity, and economic freedom across 10 metrics to gauge the economic success of 184 countries around the world. In 1995, the U.S. was ranked fourth in the world on the index and in 2012 the U.S. has dropped to tenth.

Over the last one hundred years, the United States as a country lost sight of what made it great. The case is similar for Michigan. The U.S. economy's pace for invention, innovation and new business formation was staggering in the 1900's, with Michigan at the epicenter of much of that growth. Michigan-based companies like Amway, Chrysler, The Dow Chemical Company, The Ford Motor Company, General Motors, Kellogg, Upjohn and Whirlpool were complemented and supplemented by thousands of small and medium-sized entrepreneurial organizations making Michigan a center for business excellence for much of the 20th century (U.S. Department of Commerce Report, 2012). However, Michigan began to lose its competitive edge to lower-cost U.S. states and foreign countries starting in the 1970's and continuing into the twenty-first century. Today, the Michigan economy is heavily dominated by the automobile industry and has not attracted sufficient new businesses or developed home-grown entrepreneurs to ensure strong economic growth and wide scale economic diversification.

The following are examples of the many factors used in this study to evaluate the competitiveness of the Michigan economy relative to the U.S. as a whole, as well as Right To Work (RTW) states and Non-Right-To-Work (NRTW) states:

### 1. Growth in Personal Income

Personal income per capita growth in Michigan grew 20.3% from 2000-2010 while the U.S. average income grew at 36.4% over the same period. Personal income growth over the period grew at just under 40% in RTW



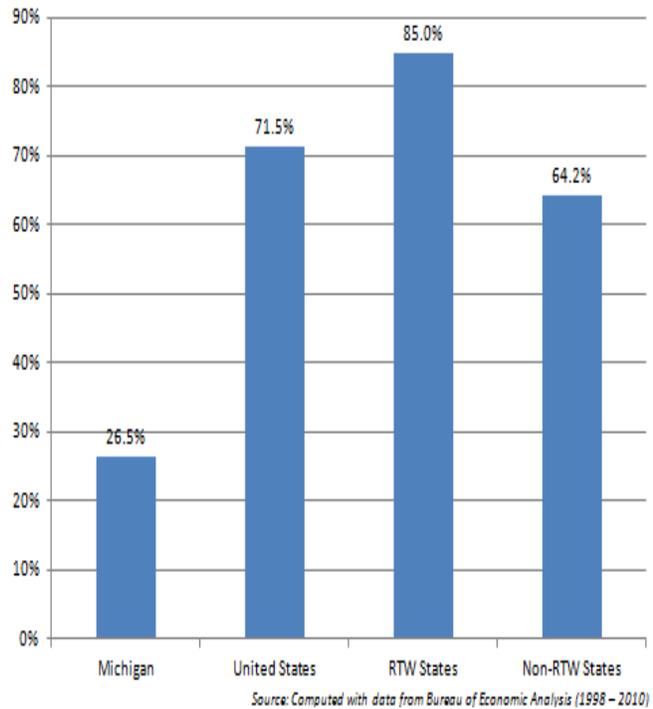
Source: Computed with data from Bureau of Economic Analysis (2000 - 2010)

states and at 34.2% in NRTW states (see Exhibit 29).

## 2. Real Gross State Product (GSP) Growth

From 1998-2011 Michigan Real Gross State Product (GSP) lagged the national average significantly. While the U.S. economy grew from an overall Gross Domestic Product (GDP) level of more than \$8 trillion in 1998 to just under \$15 trillion in 2011 or 71.5%, the Michigan economy grew by only 26.5% over the same period. Gross State Product grew at an average rate of 85% over the same period in RTW states while realizing a slower growth rate in NRTW states of 64.2% (see Exhibit 17).

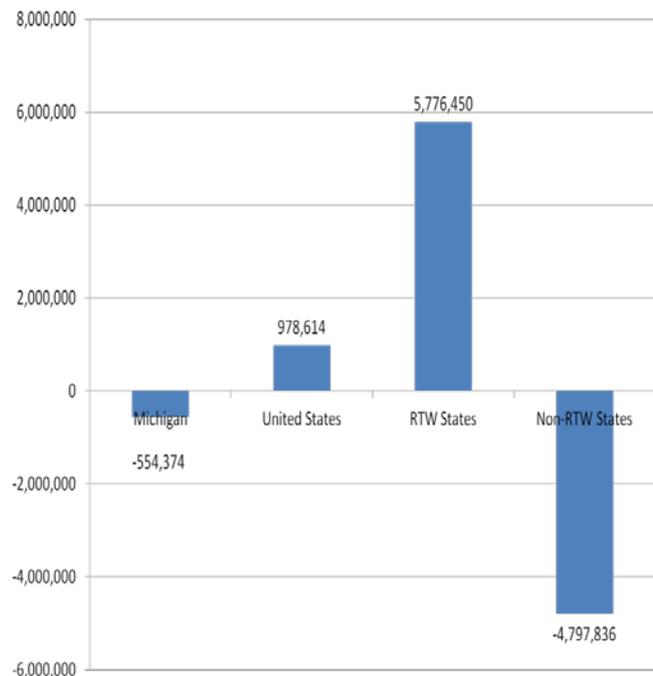
Exhibit 17: Gross State Product Growth (1998-2011)



## 3. Net Population Migration

Michigan's population net migration from 2000-2010 was among the worst in the United States with a loss of 554,374 people. Net migration is defined by the difference in people leaving a state relative to people migrating to a state over a given period of time. The overall U.S. population net migration for the same period was just under 1,000,000 people net positive with RTW states experiencing a positive net migration total of just under 6,000,000 and

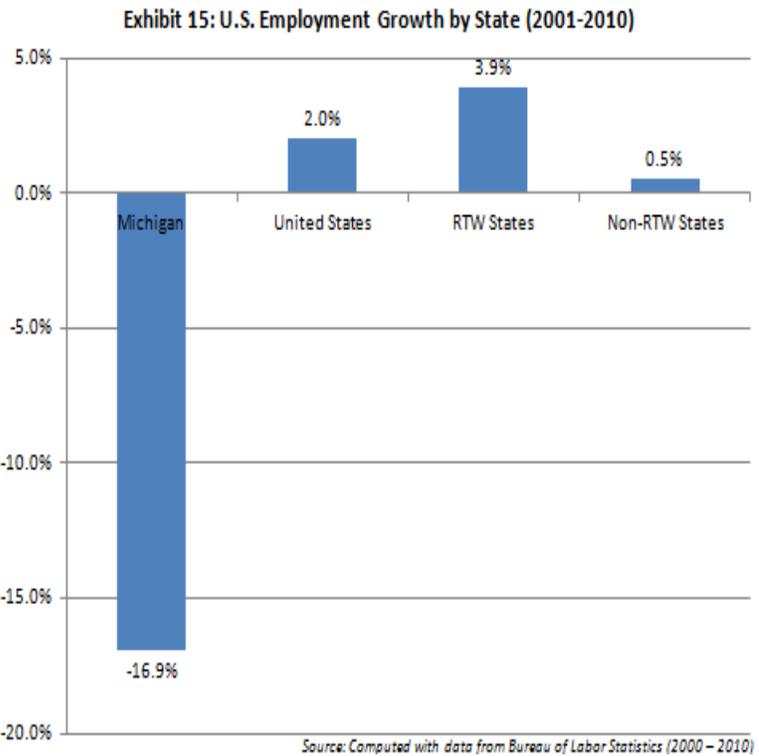
Exhibit 13: U.S. Population Net Migration by State (2001-2010)



NRTW states suffering a net migration loss of just under 5,000,000 (see Exhibit 13).

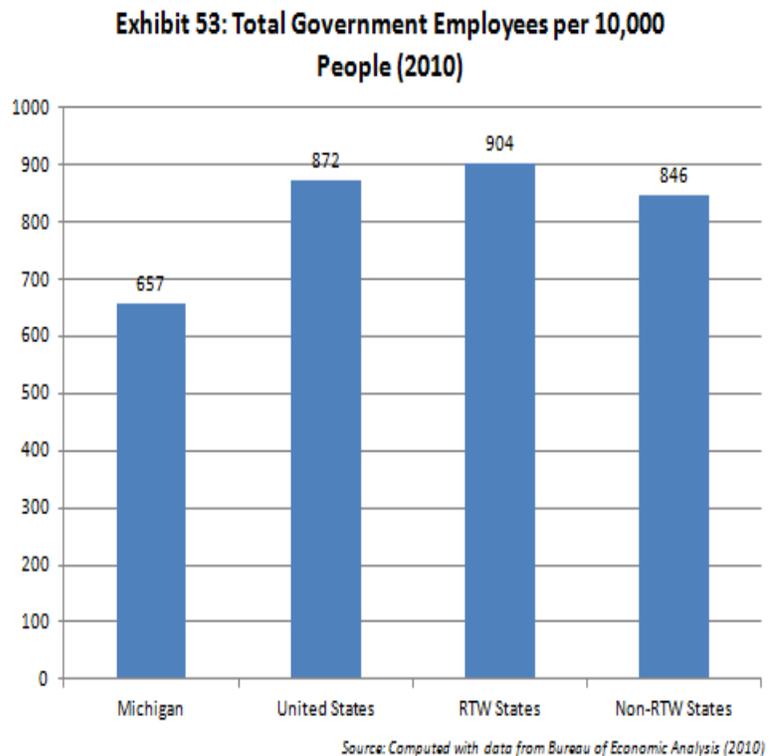
#### 4. State Job Growth

During the same period, Michigan Non-Farm Employment growth declined 16.9% while U.S. overall growth was just 2.0%. RTW states saw employment growth at just under 4.0% while NRTW states job growth was .5% (see Exhibit 15).



#### 5. Total Government Employees Per 10,000 People

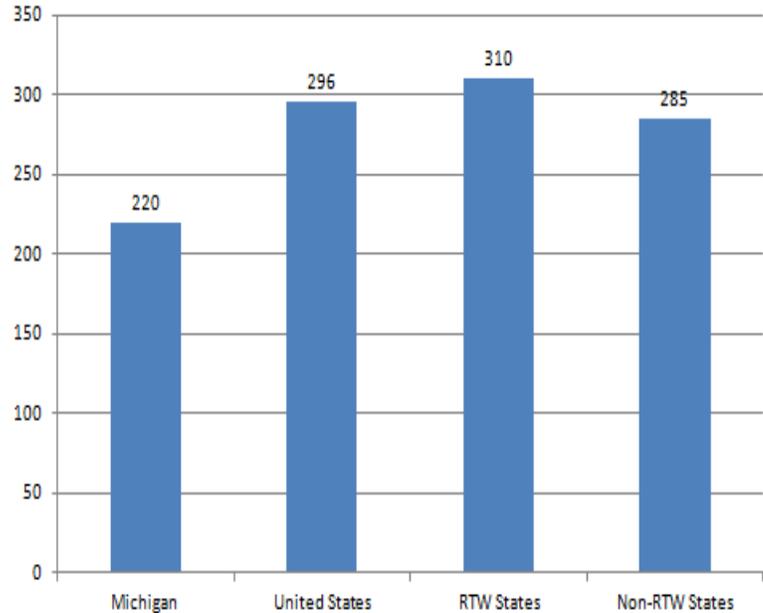
Michigan, as of 2010, has 657 government employees per 10,000 people, ranking it fourth best in the country (see Exhibit 53).



### 6. Monthly New Business Starts Per 100,000 People

The Kauffman Foundation ranked new business start-ups per 100,000 people per month per state in 2011 with the national average being 296 and the Michigan average at just 220. The RTW state average was 310 and the NRTW state average was 285 (see Exhibit 79).

Exhibit 79: The Kauffman Foundation's Number of Business Start Ups (2011)

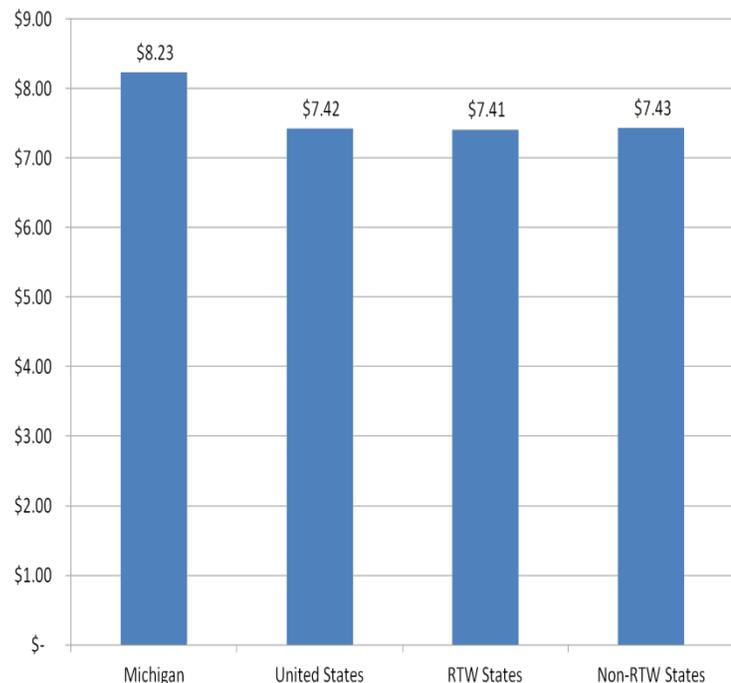


Source: Computed with data from The Kauffman Foundation (2011)

### 7. Industrial Cost of Natural Gas

Michigan seems to be very competitive in the area of average cost of electricity, but not natural gas per unit. It was below the national average for electricity as well as below the RTW average price for electricity per unit in 2010. However, the RTW average for natural gas was below the national, NRTW, and Michigan averages in all

Exhibit 71: Industrial Natural Gas Prices (2010)

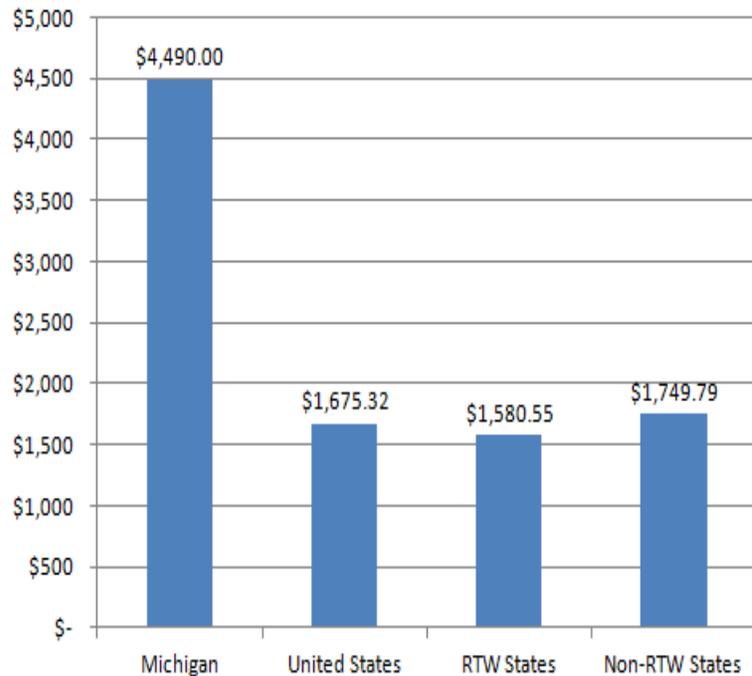


three natural gas categories we studied for 2010 (see Exhibit 71).

### 8. Automobile Insurance Cost

The cost of doing business in Michigan is high by a number of key metrics. The median price for an automobile insurance policy in Michigan is the highest in the country, according to a recent study released by CarInsuranceQuotes.com. The median average in Michigan is \$4,490 while the national average is just under \$1,700. The RTW average is \$1,580 while the NRTW average is just under

Exhibit 59: Median Price of Annual Car Insurance Policy (2012)



Source: Computed with data from Bureau of Economic Analysis (2012)

\$1,750. Because Michigan requires long-term catastrophic care as a part of its no fault coverage, the cost figures out to be 8% of household family income to purchase insurance. Massachusetts is the best bargain at 1.43% of household family income (see Exhibit 59).

### 9. The Northwood University Competitiveness Index

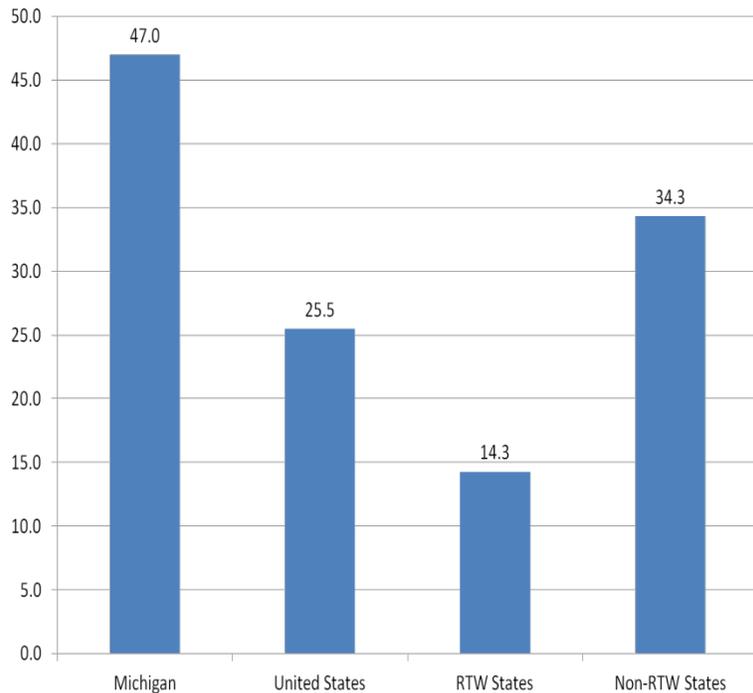
*The Northwood University*

*Competitiveness Index* was developed for this study and is comprised of five factor categories measuring various areas of economic performance for all 50 states (1 is the most favorable and 50 is the least favorable). Unlike many other indices

Exhibit 98: Northwood's State Competitiveness Index			
Alabama	30	Montana	18
Alaska	42	Nebraska	2
Arizona	14	Nevada	17
Arkansas	9	New Hampshire	27
California	49	New Jersey	43
Colorado	19	New Mexico	16
Connecticut	41	New York	39
Delaware	29	North Carolina	24
Florida	22	North Dakota	1
Georgia	13	Ohio	45
Hawaii	31	Oklahoma	7
Idaho	12	Oregon	44
Illinois	46	Pennsylvania	25
Indiana	32	Rhode Island	50
Iowa	15	South Carolina	34
Kansas	10	South Dakota	4
Kentucky	38	Tennessee	21
Louisiana	20	Texas	3
Maine	36	Utah	4
Maryland	11	Vermont	33
Massachusetts	48	Virginia	6
Michigan	47	Washington	35
Minnesota	26	West Virginia	23
Mississippi	37	Wisconsin	40
Missouri	28	Wyoming	8

where the data and/or categories are assigned weights by the researchers, the Northwood Index assigns weights based on factor analysis which initially involved 200 variables. The weights are market sensitive since these weights are susceptible to change with changes in the economic conditions, so the indices based on these weights are snapshots of current market conditions. Thus, the model delivers an overall ranking for a state, provides evidence of strengths and

Exhibit 99: Northwood's State Competitiveness Index



weaknesses relative to other states by category, and the weights assigned in each category by the model may be useful in prioritizing efforts to improve a state's relative competitiveness (See Exhibits 98 - 99).

Below are the Factor Categories and the key variables that influenced each factor:

**Factor 1 (General Macroeconomic Environment)** - considers general measures of state-wide economic health such as unemployment rates, labor for participation rates, per-capita income, and life-satisfaction (another measure of well-being in addition to per-capita income).

**Factor 2 (State Debt and Taxation)** - considers state debt per capita, cost of living, and tax burden per capita (tax burden considers state sales taxes, selective taxes, license taxes, corporate income taxes, and state income taxes).

**Factor 3 (Workforce Composition and Cost)** - percentage of the working population that is part of a union, percentage of the private working population that is a member of a union, the percentage of the public working population that is a member of a union, and cash payments to beneficiaries (including withdrawals of retirement contributions) of employee retirement, unemployment compensation, workers' compensation, and disability benefit social insurance programs.

**Factor 4 (Labor and Capital Formation)** - considers employment growth, population growth, migration, and organizational birth and death data.

**Factor 5 (Regulatory Environment)** - is a composite of other indices that consider the business friendliness of a state's regulatory framework/environment.

Based on the most current available data, Michigan’s economic performance in the five categories is:

1. General Macroeconomic Environment - 48th
2. Debt and Taxation - 10th
3. Workforce Composition and Costs - 45th
4. Labor and Capital Formation - 45th
5. Regulatory Environment - 24th

Overall, Michigan ranks 47<sup>th</sup> out of the 50 states in the Index. Consequently, the state’s relatively strong performance in terms of Debt and Taxation and Regulatory Environment are outweighed by its relatively weak performance in the factor categories of the General Macroeconomic Environment, Workforce Composition and Costs, and Labor and Capital Formation. A careful analysis of factors 1, 3 and 4 coupled with sound public policies designed to address said issues will enhance Michigan competitiveness in the future.

### **Conclusion**

It is important that the reader understands how large and important the Michigan economy still is within the U.S. and global economy. Michigan’s GSP is roughly equivalent to the GDP of the country of Austria which would make Michigan one of the 30 largest economies in the world if it were a country. However, this study does not paint a rosy picture of Michigan’s competitive position relative to most other U.S. states. Michigan’s ranking on *The Northwood University Competitiveness Index* of 47 indicates Michigan has tremendous room for improvement but also reasons for optimism. This study’s regression analysis indicates that RTW states have a strong statistically significant relationship on productivity growth. However, effect of RTW legislation is often hard to isolate since most RTW states are business friendly. Since RTW states are generally business friendly, capital formation is higher resulting in higher productivity growth. This study indicates further consideration is needed to better determine the causal relationship between RTW legislation and competitiveness. The research contained in this study should serve as a guidepost and tool for benchmarking for Michigan public policy leaders. For many years Michigan was the economic catalyst for much of the U.S. economy; Detroit put America and much of the world on wheels, and Michigan was the “Arsenal of Democracy” in World War II. Can Michigan return to the position of greatness it once occupied in the U.S. business structure? The answer is unequivocally yes, but only if we confront the economic reality facing this great state. Michigan must set its sights high and benchmark to best economic and political practices of this country’s top performing states. Finally, this study references reasons for optimism found by studying the countries of Canada and New Zealand, which have recently experienced reform in their business climates.



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