

## PART I: PUGET SOUND'S ECONOMIC CHALLENGE

### A. A New Global Context—The Starting Point

Regardless of whether one is in business, from government, an educator, from the non-profit sector or simply a citizen of the world, no one can argue with a fundamental challenge of our times—the pace of change is quickening and the world is becoming a more competitive place. Even particularly informed leaders cannot recall when the world economy grew as fast as it is growing today; or when technological change was as rampant; or when the growth of competitor nations and new trading arrangements was as intense; or when the patterns of commerce like offshoring was so visible; or when social change like the rise of the “creative class” was seen as so important as is the case today.

*“...the fact remains that we have not yet, as a society, come to terms with just how competitive the world has become.”*

*The U.S. Council on Competitiveness, 2004*

How is the global economy doing? The International Monetary Fund (IMF) recently reported that global GDP is likely to increase by 5% this year, a rate not seen for a quarter century. Many emerging economies are seeing their fastest growth in 25 years. China, of course, leads in this story, but other countries in nearly every continent are also doing well. Japan, on hard times only a couple of years ago, is recovering faster than expected. Brazil and Chile are leading the growth in South America. South Africa, overcoming the challenges of apartheid, is also coming into its own. After a troubling start, the Euro is strengthening beyond the expectations of many experts (even while economic growth in the 12 Euro countries remains sluggish).

Robust consumer spending in the U.S. has kept our nation's economy strong, even in the wake of the economic perfect storm—the dot.com bust, a stock market collapse more serious than that seen since the Great Depression, and the terrorist attacks of September 11, 2001. Most forecasters predict weak growth in the U.S. in the foreseeable future.

While respected experts from the IMF, the Organization for Economic Cooperation and Development (OECD), the European Central Bank, and our own Federal Reserve are generally optimistic about the global economy, at least in the near term, there are a few mega-threats on the horizon. Oil, currently priced at slightly more than \$60 per barrel and seemingly stuck at prices substantially above a 10-year rolling average, worries many experts. Persistently high oil prices would seriously constrain the world's economy for decades. Concerns that China's economy could overheat and crash, and bring the global economy down with it, are of concern. A pressing need for baby boomers in the West to finally begin saving for their retirement is another major concern among many experts. Savings for retirement cut into consumer spending, the major engine for growth throughout the West for many years.

The Puget Sound region is profoundly affected by, and has an effect on, not only the global context but other layers of economic activity that surround it in what can be seen as concentric circles. These circles begin with links to the rest of the state of Washington, then with Alaska and the Western Canadian provinces of British Columbia, Alberta, and the Yukon Territory, radiating northward, and then outward to include the U.S. states of Idaho, Montana, Oregon, and Wyoming. These states are organized into a group composing the Pacific Northwest Economic Region (PNWER), of which the Puget Sound region is an important part.

Increasingly, this group has identified areas of collaboration and improved competition on issues including: cross-border issues related to U.S. homeland security, energy production and transmission—including the citing of a new gas pipeline, the changing dynamics and infrastructure needs of the

telecommunications industry, healthcare and the importation of prescription drugs from Canada, as well as preparation for the Winter Olympics in Vancouver in 2010.

The West Coast Corridor Coalition, another collaborative effort between the California, Oregon, Washington and Alaska state departments of transportation and representatives from local governments, ports, and businesses, is focused on improving the movement of freight and goods through, from, and within the West Coast to support the regional and national economies. As this coalition begins to identify key issues and take action, the Puget Sound region will be positioned to play a central role in these issues and must help set the tone of these collaborative efforts.

## B. Technological Change—The Imperative to Keep Pace

How fast has technology acted to change the way we live and work? Since the global depression of the 1930s, we have seen the emergence of health technologies including antibiotics, major surgeries as outpatient procedures and a map of the human genome. Many such breakthroughs have occurred in the Puget Sound region. Information technologies have exploded to include wide-ranging computer hardware and software products, so much so that growth in the future, say many experts, may be constrained by the fact that we have more computing power and software than we need. Communication technologies have also exploded on the scene, now providing cellular service within almost any urban center in the world. Space exploration and less expensive jet air travel has recently led to non-government travel into space. Can space tourism be far behind? Finally, the world's Green Revolution has helped developing countries feed themselves and export surpluses to other countries.

No one would argue that technological innovation has dramatically changed the way we live, work and produce. Output per worker during this period in the U.S. jumped five times, which translates into sustained 5% annual increases. Overall, a picture emerges of large global productivity increases; even once very undeveloped countries are now playing in the global economy by taking advantage of vast networks of almost instantaneous communications and low cost air travel. *BusinessWeek* magazine reports that a new global commitment to technology may be signaling a wave of technological advances at least as profound as those of the past six or seven decades.<sup>1</sup>

While the U.S. remains the strongest source of innovation in the world, much of the rest of the developed and developing world is advancing as well, notably China and India, who are now the leading producers of college graduates. The European Union countries are now tied with the U.S. in numbers of graduates each year. A growing number of observers of university spending and research and development trends in the U.S. are concerned about the U.S. falling behind its competitors. Shirley Ann Jackson, president of the American Association for the Advancement of Science, calls the issue a “quiet crisis.” But Jackson also notes, “We still truly have the best graduate programs in science and engineering...and the kind of economic system and capital markets that support the exploitation of technological innovation.”

The U.S. innovation challenge is to strengthen the climate that supports basic research while keeping discipline in the economic system so that market forces screen innovation for products with commercial potential. Joel Mokyr, president of the Economic History Association and an expert in the history of technology says, “There is nothing preordained about innovation...there are a hundred ways that this process (of the U.S.'s) could go wrong.” In this context, loss of technological leadership would be disastrous to the nation.

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<sup>1</sup> \_\_\_\_\_ . *BusinessWeek*. October 11, 2004.

## C. Globalization, Offshoring and Lean Manufacturing

How fast has the truly global economy developed? While U.S. foreign investment has been an economic feature for decades, the major global trading agreements, NAFTA being the prime example, are but a decade old. Today the European Union has 25 member states without trade barriers. In South America, MERCOSUR is linking together several former national economic rivals on that continent. Other trade agreements are also emerging, each further turning what was once a global economy of hundreds of national players into one of a handful of integrated trading blocs. And, to set the rules of the global economy, the World Trade Organization has gained strength, albeit in the context of growing controversy over its role in globalization.

Offshoring of jobs is arguably the most talked about trend in international business. For decades, business leaders have sought cost advantages by building wholly owned plants off shore. For the most part it was the less skilled, blue-collar jobs that disappeared. But today, even highly skilled jobs are going away, not to foreign corporate divisions or companies in strategic partnerships, but to firms who provide contract labor from thousands of miles away as though it was in the next room.

Near instantaneous communications makes it all possible. Doomsayers see a wave of job losses stemming the interest of young people to learn skills that might be sourced from low cost environments. Over the past few years, local community colleges reported fewer students seeking to learn basic machining and programming skills (although there is renewed interest in machining as the opportunities at The Boeing Company grow).

Optimists see the process as the latest productivity miracle of the Internet and other communication technologies. But there is little doubt that the trend is troubling, especially to young people trying to figure out the skills to learn that will be least likely to be replicated by young people living in lower cost environments.

The case of software programmers is instructive (and relevant to the region). While job losses to places like Bangalore, India's Silicon Valley, are troubling, some experts see no national crisis yet. Unemployment among software programmers is about 7%—not too far beyond the national unemployment rate. And the job losses are most acute among less creative skills such as bug fixing, updating code and other routine tasks, not more skilled programming. However, some experts say that time is running short. John Parkinson, chief technologist at Cap Gemini Ernst & Young, says that “scenarios (of skilled jobs disappearing) start to look wild and wacky after 2010” and that within a decade “the new consumer base in India and China will be moving the world.” The impacts will surely go far beyond the information industries.

Lean manufacturing is another trend in advanced countries. Some firms, including Boeing, are finding ways to take out layers of employment through automation and other productivity enhancements. Boeing has launched a far-reaching lean manufacturing initiative that includes fabrication of major sub-assemblies offshore, transporting them in large bodied planes to assembly sites in the region and other places both in the U.S. and elsewhere. Looking into the future, it is hard to envision Boeing not accelerating these trends in some ways, no doubt affecting operations in the Puget Sound area.

## D. Social Development—The Rise of the Creative Class

In his book, *The Rise of the Creative Class*, Richard Florida argues that “a key fact of our age is that more of us are doing creative work for a living...30 percent of all employed people belong to this new class.” Florida's observations are expansive and resonate with many. “What we are witnessing in America and across the world extends far beyond high-tech industry or any so-called New Economy: It is the

emergence of a new society and a new culture—indeed a whole new way of life. It is these shifts that will prove to be the most enduring development of our time.”

The challenge for a region like Puget Sound and its employers is to recognize the importance of these shifts, making the community and places of work attractive to a growing number of people who prize a certain lifestyle over accumulating wealth. A particular challenge is that old forms of social capital found in most any region—rotary clubs, fraternal orders, chambers of commerce—may not meet the needs of the creative class. A trend is already visible in regions such as Austin, San Diego and Silicon Valley of new kinds of leadership groups forming. Most of these new alliances involve collaboration among partners that typically have not partnered before. The Itasca Project of the Minneapolis-St. Paul region, San Diego CONNECT, and Joint Venture: Silicon Valley Network each represent new organizational models of community and economic development leadership and foreshadow in important ways the array of new challenges faced by regions across the county and around the world.