CHAPTER 1

HAWAII'S COMPETITIVENESS

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"What can Hawaii do to stay competitive in the world market and keep its economy strong?"

In today's global economy, every state is asking this question with more and more urgency. To their credit, Hawaii state and local officials have been concerned with economic development and Hawaii's competitiveness for a long time. Their main theme has been the idea of diversifying the economy away from its tourism base—natural enough, given our substantial dependence on this industry.

High-tech industries have been a particular target, but success has been elusive. While no one can deny the attractiveness of these high-wage, environmentally-friendly industries, every other state is trying the same thing. Hawaii faces tough competition, particularly from the more established areas such as Silicon Valley, Route 128 near Boston, the North Carolina Research Triangle, and Austin, Texas.

Moreover, this diversification approach, viewed as part of the state's economic development strategy, increasingly is out of step with the strategies followed by successful global corporations and developing countries today. While Hawaii is neither a company nor a country, state officials should learn what they can from others' experiences.

An outdated notion. In corporate strategy, diversification for its own sake is an outdated concept. The wave of corporate diversification so much in vogue in the late 1960s and early 1970s produced very few results. Managing businesses with unrelated component parts simply proved too hard and too unrewarding for shareholders.

The only corporate diversification still recommended is into a field related to the core business. A local example of this is PRI's decision to sell gasoline at retail through its Gas Express outlets. Such a strategic thrust, if carried off artfully, can indeed add value because management brings something to the party (its core-business acumen) and because the potential for *synergy* between the core business and a related business is high.

A similar change in thinking about diversification has taken place in many countries. During the 1960s and 1970s, every nation with a dominant single export product (for example, Chile and copper) wanted to diversify so as to buffer its economy from wide swings in prices and demand. Usually, these efforts failed. Some simply weren't attractive places to do business. They tended to have a large public sector—that is, government involvement in business. Perhaps this public sector had grown initially to help absorb the risk in promoting the special export. Subsequently, through bureaucratic dynamics, it had become a "black hole," draining the country's economy of its entrepreneurial energy.

Indeed, in many developing nations an unhealthy symbiosis occurred in which entrenched elites used the public sector to reinforce their political and economic power. Under such circumstances, diversification couldn't possibly succeed. What business would be attracted by such a "statist" economic climate?

During the debt crises of the 1980s, many countries realized that they had to shift their focus to doing better what they already were doing well, and creating a fertile environment in which new businesses could grow.

In a fertile economic environment, industries feed on and reinforc each other *synergistically* (there's that word again!), to produce wha Michael Porter of the Harvard Business School calls sustainable competitive advantage. Porter suggests that four interdependent forces— diamond—influence a nation's (or a state's) international competitiveness and its economic fertility. I like to extend the diamond imag to baseball:

- At first base are the end market, or demand, conditions—th market size and the sophistication and preferences of consumers.
- At second base are the sophistication and the degree of rivalr in the domestic market. Firms that have had to live by their wits in domestic market will do better in foreign markets.
- At third base are production factors—the supply of land, skille labor, capital and the like.
- Finally, at home plate is the constellation of related an supporting industries. In today's global economy, production is s complex and specialized that a country or state needs a "critical mass of related industries to support competitiveness.

Porter adds two "outside" influences: government (the umpire, t stick with our baseball analogy) and "chance." Either can affect any o the points of the diamond, for good or ill.

Hawaii's two diamonds. Hawaii really has two diamonds—one fo the travel industry and one for the rest of the economy. Hawaii' tourism diamond is competitive, vibrant and mutually reinforcing. O the demand side, the customers are sophisticated and world class, th potential market is large, and Hawaii enjoys the benefits of a diversifie clientele in Asia and in America.

As for supply, Hawaii's unique environment is a precious asset an America's political stability means that capital can flow into the island freely. Related and supporting industries include the University c Hawaii's School of Travel Industry Management and its College c Languages, Linguistics and Literature (one of only three U.S. Nationa Resource Centers for the Study of Foreign Language), as well as a entire nexus of travel-related firms, including the airlines and a excellent telecommunications network.

Competition in the travel and tourism industry in Hawaii i vigorous; government, through the Hawaii Visitors' Bureau and other means, plays a supporting role.

This is not to say the travel and tourism industry is immune from business cycles in America or Japan, or from overbuilding, as has occurred on the neighbor islands. But the travel and tourism diamond, most would agree, is relatively healthy.

The rest of Hawaii's economy is another matter. Land is scarce and skilled labor is in short supply. The local market of 1.1 million people is not as sophisticated as those in major cities of Asia or the West, and those markets, in turn, are a long way away. Related and supporting industries for anything but travel and tourism are not world class, nor is competition at the same level of intensity as it is at other points around the Pacific Rim.

Because the state's natural beauty is such a remarkable asset, government has a special role in Hawaii. One would expect regulation's hand to be a bit heavier here. In fact, however, it goes well beyond the reasonable. There is really no excuse for the bureaucratic impediments that have pushed our housing prices and business costs so high. Cooper and Daws' *Land and Power in Hawaii* is among studies reporting that those in government have not always succeeded in separating private from public interest. The elite from our former plantation-based economy has been replaced by a new elite based in politics and real estate.

Competition is not encouraged. Government has done little to encourage competition. When the prospect for more competition in the local air market came up in 1991, in the form of interisland service by United Airlines, the immediate reaction of elected officials was to warn the prospective intruder away. But protection of local companies, in the name of protecting local consumers, could in fact be a smoke screen to help insiders hold their economic and political power.

In fact, the one-export-commodity developing country model, with an overdeveloped public sector that adversely affects entrepreneurial activity and an entrenched elite trying to maintain its privileges, has uncomfortable echoes in what we find in Hawaii today—and is one of the reasons Hawaii's competitive diamond (except for tourism) is so weak.

"So what should we do instead to insure appropriate development of Hawaii's economy?"

We need a strategy as sophisticated as the times in which we live That means diversification, but in areas that build on our strength, tha take advantage of the vibrant competitive diamond in our core busines of tourism, and of its related and supporting industries. In essence, we'r talking about "dancing with the one that brung you," instead o searching for a new partner.

It also means that we open our arms to outsiders who hav something to share, and get rid of the mentality that puts "who yo know" ahead of "what you know." Finally, it means convincin government that its proper role is umpiring business development rather than trying to hit home runs as a player itself.

These basic principles have a couple of operational consequences Hawaii should have—should have had five years ago—a conventio center. Business travel is a natural adjunct to pleasure travel. Th experiences of business travelers will do more to create Hawaii's image as "Geneva of the Pacific" or "Capital of the Pacific" (with thanks for both c these to Bud Smyser) than all the advertising that money can buy.

Hawaii should shed its provincial outlook and build on it multicultural population. This includes promoting the state's educa tional institutions in Mainland and Asian markets and eliminatin enrollment "caps" on outsiders.

Sensible diversification. Several other areas that build on Hawaii' strengths also make for sensible diversification. Health and sports related industries fit well with the state's image as a universal healt provider and a fitness mecca. For many reasons, golf courses are a almost ideal replacement for sugar, an industry that would have die here years ago had it not been for expensive federal "life support."

Certain types of scientific research and research-based activitie particularly those related to the oceans, the heavens, geology, biotech nology and tropical agriculture, fit naturally with the University c Hawaii's own distinctive competencies.

In both of these categories, Hawaii would be cooperating with tw "chance" factors—demographic trends toward older, more health conscious populations in industrial countries and a growing global concern about the environment.

As we focus on our core strengths, we must also take care to repair our weaknesses. Housing and education, the most prominent, receive plenty of attention in this book and elsewhere. I would only add that the industries mentioned above as good candidates for state promotional efforts generally require well-educated managers and workers. To attract these from the Mainland and Asia and to convince Hawaii's own sons and daughters to remain here, the quality of the state's education system and the affordability of its housing simply must improve. These two factors have become genuine bottlenecks to state economic expansion and growth.

Two other areas of weakness that need special attention are politics and the media.

Our political process is far too complacent. The state badly needs a genuine two-party system. Massachusetts was a one-party state. As a registered Democrat, I rather liked being a member of the party in power. But I have to admit that in 1988, when the recession hit Massachusetts with such vengeance, the state simply had not known the kind of healthy political debate that would have enabled it to cope with massive economic adversity.

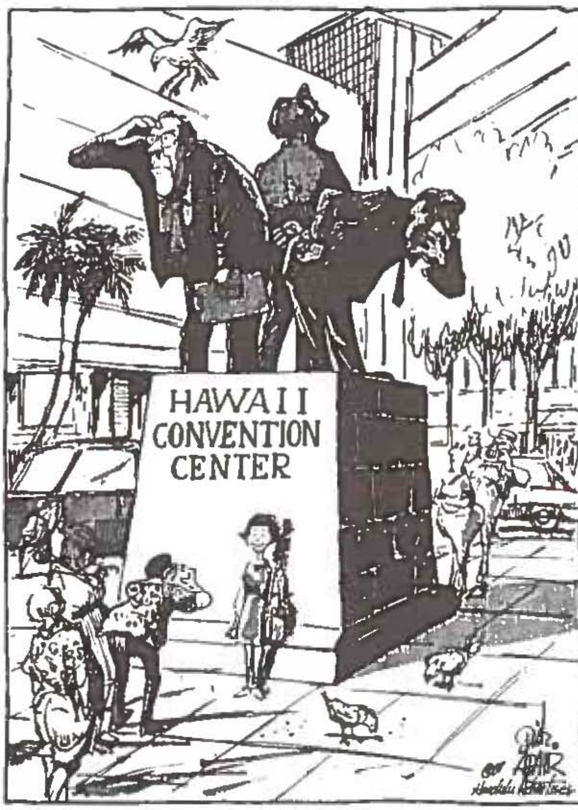
Indeed, in the 1990 gubernatorial campaign the atmosphere was one of civic desperation, with a whiff of what Germany must have been like in the early 1930s. Candidates whose electability in normal times would have been questionable became their parties' nominees. In the end, the state turned to a wealthy Republican whose major theme was that he and his party weren't responsible for what had gone before.

Deja vu. As we see Hawaii's economy softening, I have a vague feeling of *deja vu*. I hope I'm wrong. And I hope we don't need a recession to revitalize the Republican Party. But I'm certain that a second vigorous and organized voice would improve the quality of our political decisions.

My second area of special concern is the media. With the exception of The *Honolulu Advertiser*'s James Dooley and *Hawaii Monitor*'s Ian Lind, the tradition of investigative journalism is underdeveloped in Hawaii, to put it kindly.

Journalists tell me that their local news is targeted at a mythical "Minnie Fukuda" who lives in Kalihi, is in her mid-50s, and worries mostly about the price of rice. But journalists need to keep Minnie's long-run interests in mind, too. Minnie and her descendants will be better served by a media that, by the energy of its reporting, forces consumers, businesses and government to compete more effectively in the marketplace of ideas. Such a setting will certainly produce government policies and laws more responsive to the state's needs.

In summary, we must build on our strengths. We must diversify, but in related, not unrelated areas. We also must adopt market-oriented reforms to create a more fertile field. Hawaii has fared well for a long time, but in many ways this has been despite governmental efforts rather than because of them. And the parochialism of an "old boys club" simply has to give way to a more enlightened global perspective if Hawaii is to compete effectively in an increasingly sophisticated world.



"BOY, PARKING IN SHOPPING CENTERS IS REALLY GETTING TO BE A PROBLEM..."