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- ***Globalization has caused significant changes in the American economy, including job losses and an influx of new technologies and products that have strengthened local businesses.***
- ***More than 50% of Chicago's economic growth is driven by the global economy.***
- ***The rapid pace at which the global economy is developing means that few places will stay competitive without developing new strategies for managing globalization in the future.***
- ***The Chicago region must boost its rates of innovation and technology to stay competitive in this new era of globalization.***

issue: *Globalizing Local Economies: The Chicago Region's Record To Date*

by Rebecca Steffenson and James M. Banovetz

Editor's Note: The first of a three part series, this Policy Profile and the next two in this series are taken from a study entitled "Assessing Global Competitiveness: A Look at Chicago" undertaken by the Northern Illinois University's Center for Governmental Studies. This first in the series will focus on the Chicago region's response to the forces of globalization; the second will discuss how local economies, and especially the Chicago region, can best position themselves to optimize their benefits from globalization; the third will discuss the role of engaged universities in building regional capacity for competing in the global economy.

Globalization is a catchphrase broadly used to describe the increased connectivity of people and places across the globe. In a nutshell, globalization describes a process by which advances in communications and transportation increase the flow of people, goods, services, and capital across traditional national boundaries. Globalization has made the world a smaller, more accessible, and increasingly interdependent place.

A sense of globalization's impact can be seen from an examination of the 2008 presidential election in the U.S. Nearly every substantive issue in the campaign, including the economy (the credit crisis), immigration (illegal immigration), international trade (North American Free Trade Act), tax increases (on investment earnings), employment (skilled jobs moving overseas), the war (international movement of terrorists), energy and the environment (dependence on petroleum imports) was linked to the forces or consequences of globalization.

On the local level, too, globalization affects communities (see Figure 1 on the next page). A new global culture is emerging, and mobile talent pools and knowledge based firms are increasingly judging communities on how involved and responsive they are to globalization opportunities, needs, and concepts.

What problems result from globalization?

Globalization has caused some very significant changes in the American economy. These are summarized in Figure 2 on the next page. Most importantly, globalization has prompted major shrinkages of manufacturing industries across the United States.

Illinois, like other places all over the world, was forced by globalization to restructure its economy in the face of intensifying global competition. The State of Working Illinois Report has documented steady job losses in manufacturing industries across the state.[1] Over half of those loses were in industries producing durable goods.

figure*one* **Globalization's Effects on Communities**

- Makes it easier and more cost effective to trade goods across much further distances. This means that new offices and factories can now be located even in rural areas.
- Allows providers to deliver services from almost anywhere in the world.
- Opens lucrative new foreign markets for goods even into less developed areas of the world as consumer purchasing power increases. This process has been accompanied by the elimination of tariffs and other barriers to trade, and that elimination has, in turn, led to higher living standards in the communities whose nations have reduced such barriers.
- Increases flows of people across international boundaries and brings people from many different cultures into communities. Such movement of people to new communities also increases the flow of knowledge and ideas, creating new opportunities for cultural exchange.

Globalization has also created new jobs in service sectors, but these new jobs on average pay, or have tended to pay, less than the jobs they replaced. Fifty-six per cent of the new jobs projected to be created through 2012 will pay less than the current annual average wage in Illinois.[2] Thus, another downside of globalization has been the potential to increase the wage differential between higher and lower-skilled workers and thereby increase income inequality in the short term.[3]

More recently, globalization has created competition in service sectors of the economy as well. Rapid advances in telecommunications technology and improved education in other countries has made it cost effective for many firms to move jobs in such fields as technical support and creative design to more nations, such as China and India. A 2002 study projected that 3.3 million U.S. service jobs and $136.4 billion in U.S. wages will move overseas by 2015.[4] A Brookings study of the movement of U.S. jobs overseas has forecast higher than average job losses in 28 major U.S. metropolitan areas between 2004 and 2015 in both high and low wage occupations.[5] Nine per cent of management jobs and 10 per cent of business and financial operations jobs are expected to move offshore by 2015.[6]

Immigration from developing to developed countries around the world is a very controversial effect of globalization. Immigrants change the social and economic climate of the communities to which they migrate, but they also create closer economic and social ties between their home regions and the communities to which they migrated. Some people fear the impact of migrants upon the communities to which they come, but others believe that migrants help to expand cultural opportunities for all residents. The economic impact of the estimated 11.6 million illegal immigrants in the U.S. has raised concerns that they will drive down wages and overburden government support services.

What are the benefits of globalization?

While there is no doubt that globalization causes problems for those businesses and workers adversely affected by it, globalization is also an agent of opportunity. Some of these are summarized in Figure 3 on the next page.

Recent globalization pressures have created a global economy where competition is driven more by the value added by technical knowledge and less by lower cost. It is an economy in which growth, productivity, and higher wages are tied directly to the capacity of industries to maximize efficiencies through creative and customized business solutions. In order to be competitive, manufacturing industries must harness the creative energies of educated workers to make products improved through innovative research and design. Service sectors are forced to become increasingly creative and knowledge intensive. Competitive advantage is no longer a function of lowest

figure*two* **Disadvantages of Globalization**

- Local manufacturers must compete with goods produced abroad where wages and production costs are less.
- Local industries have moved production overseas.
- Well-paying factory jobs have disappeared, leaving many workers unemployed and some local economies devastated.
- Jobs in the service sector created by globalization have paid lower wages than the manufacturing jobs that were lost.
- Many service sector jobs have also moved overseas where wages are lower.
- Mass flows of new immigrants from less developed nations to developed nations has led to many community-based problems and challenges.

figure*three* **Advantages of Globalization**

- Creates opportunities for growth, more efficient production, and higher wages.
- Changes the basis of economic competition from lowest cost to quality of equipment, skill of workers, and business friendly regulatory environments.
- Increases the profitability of firms that adapt to the pressures of global competition.
- Increases labor productivity, creates new jobs, and increases incomes.
- Lowers unemployment rates, raises property values, and results in strong income growth in the communities with the greatest numbers of immigrants.

cost, but rather of the quality of equipment, skill of workers, and limited amount of government regulation.[7]

Globalization, in short, gives U.S. firms new access to capital while direct foreign investment in the U.S. gives domestic firms an influx of new technologies, innovative processes, products, ideas, and management skills, all of which help strengthen local industries. Figure 4 sets forth a specific listing of the economic advantages of globalization to the U.S. economy.

Within the United States, globalization can help or hurt a region. *To reap the full benefits of globalization, a region like Chicago must structure its environment so that: (1) local economies and communities can be flexible enough to diversify under the pressures of global competition; and (2) local governments can assure industries full access to the tools they need to compete in the competitive global environment.* The rapid pace at which the global economy is adapting and developing, however, means that few places will stay competitive without developing strategies for managing globalization in the future.

How Does Globalization Affect the Chicago Region?

The Chicago metropolitan region has the potential to be a major player in the global economy because it has the physical and digital infrastructure required to connect firms to global markets. Besides being home to one of the busiest international and inter-modal transportation hubs for cargo in the world, Chicago also has one of the world's most advanced telecom systems and is home to the Chicago Network Access Point (NAP), which is the world's largest internet exchange point by volume. This infrastructure has helped Chicago based companies trade around the country and the world, and kept the entire region active in the global economy.

Estimates based on national trade data suggest that Chicago is now one of only four metro areas in North America[15] where more than fifty percent of the economic growth is driven by foreign demand. This means that Chicago is one of only four cities in North America where economic growth is more tied to the global economy than to the national domestic economy. The statistics in Figure 5 on the next page demonstrate the economic impact of this reality on the region.

Foreign direct investment is another testament to the global position of the Chicago region. The state of Illinois now ranks number one in the Midwest and number

figure*four* **Globalization's Economic Advantages for the U.S.**

- Ninety-five percent of the world's consumers live outside the U.S.[8]
- Firms which export (sell) their products abroad have been found to be more productive, more technology and capital intensive, and pay wages up to 18% higher than firms that do not export their products.[9]
- Companies that optimize their global networks reduce their supply costs and earn profits up to 73% higher than competitors that do not.[10]
- Manufacturing processes relocated abroad accounted for 20% of the average growth in labor productivity between 1992 and 2002.[11]
- The worldwide outsourcing of technology is predicted to create 337,625 net new U.S. jobs by 2010 and increase real hourly wages in the U.S. from six to twelve cents per hour between 2005 and 2010.[12]
- For every dollar the U.S. sends abroad in relocated business operations, it gets back roughly $1.12.[13]
- On average, foreign-owned establishments in the U.S. pay higher wages than locally owned ones and such direct foreign investment creates new employment opportunities.[14]

figure*five* Chicago's Global Economy

- Chicago's total exports rose from $26 billion in 2005 to $29 billion in 2006. A total of 13,891 firms exported $42 billion in goods from Illinois in 2005. Illinois companies exported to 209 foreign destinations in 2006.
- Exports supported 448,400 jobs in Illinois in 2003. Between 2002 and 2006, Illinois exports increased 64%.
- Small and medium sized firms with fewer than 500 employees constituted 89% of Illinois' exporting firms and generated 23% of the total merchandise exported in 2005. But there is room for improvement: it is estimated that only 10% of small businesses in Illinois are active in the export market, yet an estimated 60% of such firms could be viable international players.

five in the U.S. as a destination for foreign investment. Relevant statistics are presented in Figure 6.

These statistics point to a resurgence in Chicago's reputation as a global business center. At the start of the millennium, *Business Week* warned that Chicago was "slipping as a business center" and "still struggling to find the spark that will ignite it as a 21st century city."[16] More recently, however, Chicago's status as a global city has been acclaimed by a host of business and financial commentators. For example, Chicago has repeatedly gained *Site Selection Magazine's* top spot as a center for business attraction (March, 2007), *The Economist* hailed Chicago as a "success story" for "emerging from the process of deindustrialization" (March 16, 2006); and the Financial Times' *FDI Magazine* labeled Chicago a "City of the Future" based on its strong economic indicators and high levels of public and private investment (April 25, 2007).

Finally, just as the region's economy has responded to globalization by diversifying, so, too, has its population. According to the American Community Survey (2006), Illinois' nearly 1.8 million immigrants make up 13.8% of its population; foreign born workers account for as much as 55 per cent of the population growth in Illinois. In Chicago, immigrants make up as much as 20 per cent of the metropolitan area's workforce. Nearly 45 per cent of all of the region's immigrants arrived within the past ten years.

Immigration is no longer primarily an urban phenomenon: more than half of these new arrivals have chosen to bypass the city and move directly into suburban neighborhoods.[17] This demonstrates a remarkable shift from 1990 when only three suburban communities were considered new ports of entry.[18]

How well is Chicago actually competing in the global marketplace?

Measuring employment concentration in knowledge intensive professional occupations – occupations key to the new global economy – is one way to answer this question. In the late 1990's, analysts at the Chicago Federal Reserve Bank argued that Chicago had broken away from the rest of the nation's rust belt by demonstrating strong employment growth in knowledge intensive and business and professional sectors, but significant declines in employment growth in these sectors between 2002 and 2004 raised some questions about the region's future.[19]

In 2001, the Metropolitan New Economy Index found that Chicago underperformed in comparison to other metro areas across the country in the knowledge economy. Chicago ranked 19th overall behind cities like San Francisco, Seattle, Raleigh-Durham, Houston, and Denver, scoring particularly low (35th) for aggregated knowledge jobs. In 2007, The State of the New Economy Index ranked Illinois 16th in the U.S., but reported that the state scored relatively high in knowledge jobs measured by employment in knowledge occupations (9th) and high wage traded services (8th).[20]

The same index also highlighted other trends which raise questions about the overall competitiveness of Illinois' knowledge economy. And although Chicago is one of the busiest cargo centers in the world, the value of exports from Chicago is lower than many rival regions. Even worse from a global economic perspective, although the

figure*six* Foreign Investment in Chicago and Illinois

- An estimated 1,600 foreign-owned businesses from 56 countries are located in the Chicago metropolitan area.
- In 2004, Illinois had 5,602 foreign-owned businesses supporting 235,600 jobs. These businesses supplied over 10% of the state's jobs in manufacturing employment.
- In 2004, foreign-owned businesses had investments valuing $40 billion in property and plant infrastructure in Illinois' manufacturing sector and another $10 billion in service facilities.

figure*seven* **Employment by Foreign Owned Establishments: Chicago: 2002**

Industry	Employment
Manufacturing	83,220
Wholesale Trade	34,517
Finance and Insurance	27,094
Professional, Scientific, Technical	22,422

service economy in Illinois represents 73 per cent of business sales, the region's service providers' exports remain significantly lower than manufacturing exports.[21]

How does the Chicago region compare in terms of foreign investment?

Without doubt, foreign direct investment (FDI) is flowing into the Chicago region, but it is unclear what real impact this investment has beyond the percentage of overall state employment. FDI data does not indicate whether the investment creates new employment or simply shifts employment from domestic to foreign owned employers.

A 2005 study by The Brookings Institution found that FDI in the Chicago region promoted more employment in manufacturing and wholesale trade than in robust higher wage sectors such as finance, insurance, and professional and scientific services. (See Figure 7.) The study also ranked global metropolitan areas based on their connectivity to international service networks in accounting, advertising, banking/finance, insurance, law, and management consulting. Chicago scored relatively high relative to other U.S. cities, second only to New York, but as a globally connected place, Chicago ranked 7th behind London, New York, Hong Kong, Paris, Tokyo, and Singapore.

Does local government affect global rankings?

In the 2007 Master Card Worldwide Center of Commerce ranking of 50 top global commerce centers, in which Chicago placed 4th over-all, Chicago scored particularly high relative to other international cities based on its legal and political frameworks and the role the city government plays facilitating the flow of goods, services, finances, and information. It was noted, for example, that it takes only 12 days on average to register property in Chicago versus 21 days in London and 183 days in Paris.

The support local governments give to the local business climate can have a major impact on global economic participation. This is particularly true in the U.S. where the regulatory system is highly decentralized to state and local governments, and even more true in Illinois where the number of local governments is not only the highest in the nation, but 50 per cent higher than Pennsylvania, the state with the second highest number of local governments. The multiplicity of levels of government and the number of local governments can create both uncertainty and the perception of higher business costs in the minds of investors, especially foreign investors.[22]

Divergence in governmental regulation of professional services can also pose barriers to the flow of highly talented professionals. Governments elsewhere have taken steps to pursue regulatory cooperation in order to facilitate freer flows of services and service providers.[23]

Tax policy can also be a competitive advantage or disadvantage in the global economy, and a 2006 Illinois State and Local Business Tax Burden Study found that Illinois has higher tax burdens than its neighbors with which it competes for business investment.[24]

Finally, Chicago is not a global banking leader, and the legacy of Illinois financial regulatory policy is one of the factors blamed for the city's low impact on the decisions which shape the international banking climate.[25]

What limits the Chicago region's ability to compete globally?

The weakest link in the Chicago region's economic performance, and the one that stands to most hinder its future competitiveness, is the state of innovation. Despite a high concentration of world class research universities in both the Chicago metropolitan area and in the state of Illinois, neither the region nor the state is recognized to be on a par with other centers of innovation found across the nation. Consider:

- The New State of the Economy Index, 2007, gave Illinois an innovation ranking of 24th in the country as measured by comparative levels of high-tech and science engineering jobs, venture capital, patents per worker, and industry investment in research and development.
- On the Index, Chicago not only fell well behind the national innovation leaders such as Silicon Valley, Boston,

figure*eight* **An Example of Global Collaboration Networks**

The creation of the new Boeing 787 Dreamliner aircraft was developed by an international collaborative process that involved over 50 partners from 130 different locations working together for more than four years.

and Seattle, but it was also outranked on innovation scores by other Midwestern cities including Minneapolis, Pittsburgh, St. Louis, and Detroit.

- Similar findings have been echoed by the World Knowledge Competitiveness Index, which compares regions using 17 measures of knowledge capital, regional economy outputs, and knowledge sustainability.[26]

- Chicago does not even register as a "spike" on the world map of the most successful technology centers in the world.[27]

Why is the Chicago region so far behind other cities?

While more research on the state of innovation in the Chicago region is needed to answer this question definitively, some reasons that have been advanced are:

- The region's lack of success in securing federal research and development money.

- A lack of internal organization and clear leadership at the regional or state level.

- Competition between universities.[28]

What is clear is that the Chicago region and the state of Illinois will need to start leveraging its assets and boost rates of innovation and technology commercialization to stay competitive in this new era of globalization.

Globalization is changing the whole process of research and development as the most competitive firms have begun increasingly to rely on decentralized global networks of research and development teams rather than large central and vertically integrated research departments. (See Figure 8.) These global collaboration networks invest fewer resources in training and developing internal talent. Instead, they seek partners with contextual knowledge possessed by virtue of the talent's position in a particular local place. In addition to technical expertise, they seek partners skilled in critical thinking, coordination, and advanced communication skills – knowledge and abilities not inherently produced by most traditional educational curriculum programs. This reality, in turn, creates new challenges for workforce development in local regions that wish to be more globally competitive.

One of those challenges is to achieve the ability to produce, attract, and retain the best available knowledge talent. In addition to state-of-the-art universities, regions like Chicago must also be places where Richard Florida's "creative class" want to live and work. In the global economy, such places must have cultural amenities which appeal to highly skilled workers recruited from an international economy – amenities such as foreign curriculum schools, ethnic media outlets, and success at integrating such migrants into the economic, political, and social life of the region.

What does this mean for the Chicago region?

As one of the world's major cities and transportation hubs, Chicago is well positioned to compete in the global economy. Despite a relatively successful transition to the global economy, neither the Chicago metropolitan area nor the state of Illinois rank among the nation's most competitive knowledge economies. As a result, and as the State of the Economy Index and the World Knowledge Competitiveness Index indicate, Chicago is not now competing in the global economy as well as it could and should be.

The Chicago region must confront a number of problems. The second Policy Profile in this series will provide details on how regions generally, and Chicago specifically, can become more competitive participants in the new global economy.

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28. Editor's note: The University of Illinois, the natural institution to serve as a leader among universities in the state, has historically pursued a policy of severe competition with other universities in the state, and sometimes even between campuses within the University's own system.

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Rebecca Steffenson, a specialist in global governance, international institutions, and regional economic integration, holds a Ph.D. from the University of Glasgow; United Kingdom, and an M.A. from University College, Dublin, Ireland. She has held research and teaching positions at DePaul University, Chicago; Queen's University, Belfast; the University of Glasgow; and the European University Institute in San Domenico di Firenze, Italy. She is currently at Northern Illinois University working with the Center for Governmental Studies and the Department of Political Science.

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