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# Michigan Supply Management: Why Companies are Moving to West Michigan

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## Industrial Market

The year 2014 will long be remembered as a year of “doing it right” in West Michigan. A glance at the local unemployment numbers show that many West Michigan counties have some of the lowest unemployment rates in the state, and most counties are **well under** state and national unemployment percentages. Needless to say, the local economic development offices in West Michigan have been humming. Our existing companies are expanding, and new companies are taking a look at West Michigan for the first time ever. The local development offices have identified the possibility of SEVERAL THOUSAND new jobs coming to our area over the next year or so.

Why are companies coming to West Michigan? In a similar light, why are our existing companies expanding in West Michigan and not fleeing to other states that, say, offer no taxes for ten years? With a few exceptions, these firms are not charities. They are coming to West Michigan because they can make a long term investment in plant, equipment, and jobs, AND as a result, **make money**. Why West Michigan? In the simplest form, the decision to come to our side of the state is based on a simple formula: West Michigan offers the lowest **total cost of doing business**.

In recent years, the computer has made a huge difference in assessing various locations around the world. A book written a few years ago entitled, “The World is Flat,” notes that almost all of the major corporations of the world, and some of the smaller firms as well, are now operating on “enterprise” software such as Oracle and SAP. Hence, even without any sort of an international treaty, the accounting rules and the accounting systems for the **world** have become unified. It is important to note that profitability, or lack thereof, around the world is the same metric. Unlike the paradigm of the 1970s, central management can track **real-time** performance of as many as 300 locations around the world—and assess their profitability—or lack thereof.

When considering a new location, it isn't a quantum leap to figure out that this same “enterprise” software is used to calculate the cost of doing business at any potential location worldwide. Obviously, factors that are plugged into the model include the projected cost of labor, local taxes, federal taxes, state taxes, and cost of insurance, especially including worker's comp. Other local input factors that may be deal-breakers include the cost of electricity, cost of transportation, cost of water, and the cost of waste disposal. Overall, the location must have a significant degree of “viability,” meaning that the new firm would be easily and

quickly integrated into the local area. This is the reason that a rural county could offer free taxes, free utilities, and even free land only to find that the local workforce was so small that potential new workers would have to drive many miles to get to work.

Unfortunately, thanks to new accounting software, unprofitable locations now tend to stand out **like a sore thumb**. For instance, a Fortune 500 auto parts supplier recently observed that a small plant located in West Michigan was only marginally profitable compared to other locations. Management initially tried to work with the cost structure of the plant, but after several years of minimal improvement, the decision was made to abandon the West Michigan location and move the production to South Carolina. Fortunately, this incident is the exception and not the rule.

Another major consideration is infrastructure. Traditionally, infrastructure has included things like access to rail line sidings, good roads, water, and sewer. But every business is different. For instance, some firms that do business worldwide find it best to be near a major airport so that potential clients and customers can visit, and that the firm's salesforce can easily spread out to the world. For others, such as a plating company, access to sufficient electric power at a reasonable rate may be essential.

And then there is the geographical cost itself. Specifically, where are the firm's customers, and what is the cost of shipping to their locations? Obviously, if the product is light, in the age of, “If it fits, it ships,” this may not be a problem. For heavier products, the cost of freight becomes a major consideration. The same is, of course, true of **INBOUND** freight, which can add considerably to the cost.

Clustering. For at least the last 150 years, competing firms have tended to co-locate or “cluster” near a common location. Steel firms located in Pittsburgh. Auto firms located in Michigan. Furniture firms located in Grand Rapids. Although shipping considerations may be a part of the reason for co-location, the bigger consideration is the local support structure, such as the right industrial distributors, the right equipment repair facilities, and perhaps most importantly, a pool of labor familiar with the industry that doesn't have to be trained from scratch.

Then comes the essential analysis of the soft factors. The classic case comes from Texas Instruments, which negotiated a seemingly remarkable deal for lower taxes and virtually free land in order to build a semiconductor research center

in Lubbock, Texas. Hiring a few local clerical workers was not a problem, but getting middle level engineers and other experienced management to uproot from culturally diverse Dallas and move to Lubbock resulted in a major problem. Some employees literally left the company rather than move. Of course, the local “work ethic” cultural factor can also come into play. Some local firms that have recently located facilities on the eastern side of the Michigan have been stymied by the “us versus them” mentality in some locations, as well as the blatant lack of company loyalty.

Local attitudes toward the potential new business can also make a difference. If the potential business operates inside four closed walls with no smokestacks in the air, chances are that it may raise little discussion. However, even if the plant is baking bread, someone will probably object to the smell of freshly baked bread wafting through the air at all hours of the night. If the plant will employ a large number of people, others may object to the increase in street traffic near the plant, and demand that the plant be located on the other side of town. The boards of many of Michigan’s rural incorporated townships want developers to locate in adjoining townships in order to keep their township rural. This is often referred to with the generality of “not in my back yard.” Of course, the attitudes of some locations are just anti-business, and building the plant would result in local resentment of the firm and its employees. If a firm senses that local inspectors or local assessors have an anti-business attitude, they will look elsewhere.

### **Where West Michigan Shines**

The latest report from the Michigan Department of Technology, Management, and Budget notes that Kent County has the lowest unemployment rate (4.0%) among the 83 counties in Michigan. Kalamazoo County is not far behind at 4.7%, and Calhoun County at 5.1%. This compares very favorably with the state’s official rate of 7.1%, and the national rate of 5.8%. The average GDP growth for all “Metropolitan Statistical Areas” (MSAs) in the nation grew at a rate of 1.7% in 2013. In the Grand Rapids MSA, the growth rate was 3.9% followed by 2.4% in Kalamazoo-Portage, and 1.4% for the Battle Creek MSA.

### **Why are we doing so well? Several factors come to mind.**

1. *Productivity.* If you ask the management of any company that has locations throughout the state, they will most often tell you that the West Michigan work force is more productive than other locations in the Midwest. Along those same lines, the work ethic of MOST West Michigan workers compares favorably with that of other locations around the nation.

2. *Schools.* Convincing high-powered employees to move to a new city in a new state requires evidence that good education is available. I know, we all think our schools can do better, and they can. However, compared to many other cities and many other states, our schools are well ahead of the averages. Furthermore, we have a wide selection of charter, religious,

and private schools for those that are inclined to send their children to those types of schools.

In another educational perspective, many firms are looking for an endless stream of educated job-seekers to fill positions. Although there is always room for improvement, West Michigan does have a well-trained workforce to choose from when new jobs are posted.

3. *University Support.* Particularly in high tech and biotechnology, many firms are looking for partnerships with local universities for internships, research support, and qualified job-seekers to fill positions. Through Grand Valley State University, Western Michigan University, Michigan State University, and a host of private colleges, West Michigan offers plenty of support in this category. For technology jobs, we have numerous junior colleges that do an excellent job training electricians, mechanics, computer operators, and the like.

4. *Simpler Taxation.* Only a few years ago, NUMEROUS development opportunities were lost because of the complications of the old Michigan Business Tax. Although some states levy no significant corporate income tax, the replacement of the Michigan Business Tax with the new, flat rate 6% tax has at least made computation and reporting much simpler. Just a few years ago, it was typical for a small or medium-sized firm to file a 250-page Michigan Business Tax return. With the new system, the same tax return may now be only six pages. When assessing the all-important total cost factor, an **accurate** estimate is essential. Under the old system, it was very difficult. When one out-of-state firm asked for an accurate estimate of the Michigan Business Tax, one frustrated state official was quoted as saying, “Why don’t you just build your plant here, and we will tell you what the tax is at the end of the year.”

Although the repeal of the hated “Personal Property Tax” is still too new to have much of a current impact, the future upshot from an economic development standpoint is very significant. Michigan was one of the few remaining states to get rid of this arcane system of taxing, and some analysts suggest that the most immediate impact may be an increase in capital investment among Michigan’s existing firms now that new investment is no longer discouraged.

Another future tax issue that is now on the radar relates to unfunded pension liabilities for any potential location and what the situation will look like in, say, twenty or thirty years. If no plan is in place to balance these liabilities, the unfortunate local businesses will probably be stuck with the bill when the credit runs out. Or like Detroit, they may just flee in advance. Coleman Young, the former mayor of Detroit once commented about a firm leaving the city, “Good riddance. We didn’t need them anyway.”

5. *Capital Availability.* Believe it or not, West Michigan has plenty of venture capital available to invest when the right opportunities come along. Venture capitalists are sometimes

called “angel investors” because they provide opportunities for startups that look promising. If you Google “Angel Investors Michigan,” you will find organizations like Great Lakes Angels, Grand Angels, Capital Angels, Muskegon Angels, and the Michigan Angel Fund all of which are just some of the organizations ready to connect investors with good opportunities.

6. *Right to Work.* Granted, this is very controversial issue. However, the FACT remains that about 60% of the major firms would not seriously consider Michigan for expansion until after the Right-to-Work law was recently passed. Organized labor remains vehemently opposed to Right-to-Work, but this change has resulted in numerous new employment opportunities in Michigan, and will continue to result in economic gains in the future.

7. *Clustering.* As previously noted, some firms choose West Michigan to locate because of the proximity to other similar companies. The support structure in terms of suppliers, distributors, repair facilities, and the like are already in place. Furthermore, there are trained employees from which to draw.

8. *Cost of Living.* The Consumer Price Index (CPI) for West Michigan consistently runs at about 90% of the national average. Needless to say, a lower CPI at least partially translates to a lower cost of doing business.

9. *MEDC.* Simply stated, the role of the Michigan Economic Development Corporation is to “assist local development organizations to secure new jobs for Michigan.” And yes, they also provide financial and tax incentives that are sometimes essential to “seal the deal.” About five years back, the organization was roundly criticized for awarding incentives based on political, rather than economic, considerations. There were calls for the termination of the organization altogether, given the amount of political cronyism money they were throwing down the proverbial rat hole. Although some segments of the electorate still feel that MEDC constitutes a form of corporate welfare, the fact remains that most major states have competing organizations that also provide lucrative incentives. Some don’t like it, but that’s just the way business development is done in 2014. On the balance, the new leadership in the past few years has done an excellent job in helping to expand economic opportunities in Michigan and eliminating the cronyism of the past.

10. *Active Development Agencies.* A huge portion of our local success in economic development must be attributed to the prowess of our local development offices, the largest of which are “The Right Place” and “Southwest Michigan First.” Granted, our development people are also well-trained in the old-fashioned art of “schmoozing,” but just showing potential companies our beautiful parks, our sandy beaches, and our positive attitude is not enough in today’s world. In fact, not even close. Again, firms choose to locate or expand in West Michigan because it is **profitable** to do so. And given a

chance, we have the people in our development offices who can show why West Michigan is the place to be. Believe it or not, some economic development offices around the country consist of one director and one secretary, and they spend most of their time simply placing ads in magazines and answering the phone. Not so in West Michigan.

11. *Good Publicity.* On the people side, Kalamazoo, Grand Rapids, South Haven, and other local cities frequently pop up on various lists of “best places to live.” Fine, but deciding to locate in West Michigan is still a **business** decision. All corporate and local development offices subscribe to a magazine entitled “Site Selection.” For 2014, Michigan came in at 6th place in the nation, up from 16th place in 2013. Among the Great Lakes states, Michigan is **Number One**. Just a few years ago, Michigan regularly ranked in the bottom quartile. In short, Michigan wasn’t even on the radar for consideration by most out-of-state firms. What a difference a few years make!!

### **Problems**

Adding all of this together says that the “bottom line” or the lowest “total cost” for doing business for many firms **around the world** may well be here in West Michigan. Granted, if we had a perfect environment for jobs, we wouldn’t have to worry. But the fact remains that we still have a few stumbling blocks that result in West Michigan losing out to other states.

One of the main reasons for firms not coming to West Michigan is obvious and expected. Locating in West Michigan doesn’t fit their business model, i.e., we are too far away from their primary customers; we are too far away from their main sources of supply; the weather is not conducive to their type of business, or other locations simply offer a lower cost of doing business. Of course, the soft factors such as where the founders like to be located play a role as well. We can’t expect to win all new business, and there are factors over which the development advocates and the politicians have little control. However, there are a few areas that **CAN** be improved.

*Tax Consistency.* Granted, lower taxes are always popular with businesses, but most of these businesses also know that there is a point at which taxes are cut so low that the firm can be driven out of business because of the underfunding of essential government services. Adequate police, fire protection, and sanitation are obvious, but so are the aforementioned school systems for providing a stream of qualified workers. Ten year tax breaks are often tendered to attract an initial investment, but what happens after the grace period is over? Chrysler in good faith once located a plant in Wisconsin only to have the local officials crank up the tax bill to four times the initial estimate in less than ten years.

Again, consistency and predictability of taxes and tax policy are paramount. Unfortunately, elected official, especially at the local level, turn over. New officials and assessors may

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come to power who take a negative attitude toward the business, and tax fights may ensue. This poisons the water for further development.

*Electric Power.* Many people are unaware that Michigan commercial electric power rates are higher than most of the rest of the United States. They are 15% higher than Ohio, 16% higher than Indiana, and a whopping 31% higher than Illinois. Part of the reason for these higher rates comes from the lack of a competitive rate structure, and part is the result of the on-going push for more green energy. Whereas wind turbines are now profitable investments for DTE and Consumers Power given the high level of the current rate structure, other states have taken advantage of the lower cost of natural gas for their expansions in generating capacity. Hence, industries that require large amounts of electricity go to those states. It's a trade-off that most people feel is worth the additional cost, although the resulting higher cost of electricity results in forcing most firms that require large amounts of electricity to look elsewhere. The exception is that electric power for the far southwest corner of Michigan comes from AEP (American Electric Power), and the rates are less.

*Untrained Regulators.* One of the classic cases from a few years ago involved a stiff fine levied against a farmer/landowner in Roscommon County. The DNR inspector found that the farmer had apparently dammed up a small creek near the back of his property for some unknown reason. The DNR regulator issued a fine and demanded that the dam be torn down immediately. To make a long story short, the landowner wrote the DNR a long letter in an attempt to educate the inspector about the nature and habits of the Michigan beaver.

The overwhelming majority of regulators do not operate this way. They know the law, they know the rules, and most importantly, they know the industry they are regulating. However, stories abound about inspectors who have a personal agenda or an ax to grind with the industry they are regulating.

*Overregulation.* In the past four years, the Michigan Legislature has methodically eliminated numerous outdated regulations. Work is now proceeding to eliminate overlapping regulators, i.e., multiple agencies calling on the same businesses to inspect similar factors. However, as a catch-all, the concept of government overregulation continues to stand in the way of business expansion.

Granted, SOME degree of red tape is definitely needed in order to keep the environment safe and to maintain property values in the surrounding area. Again, there is a question of balance. Firms expect government regulation, but they do not expect overregulation.

It would be possible to write a book about economic development in West Michigan and still not cover everything. But in today's world, it is essential that that our state, county, township, and city officials understand how we got to where we are now as well as where we need to go in the future. With a few wrong turns, **all or most of these gains can be reversed.** We must recognize that the successful economic growth we have experienced in recent years is the result of a lot of hard work, not just blind luck. Furthermore, we cannot rest on success. Innovation and creativity will drive the future, and for the sake of our posterity, it is our job as a society to make sure that the right people and policies are in place to make it happen. ■