

Cluster-Based Economic Development in Mendocino County

*Developing Industry Clusters
Economic Growth Opportunities of Manufacturing in Mendocino County*

December 2006

Business Services Network:

Economic Development & Financing Corporation
Mendocino Private Industry Council, Inc.
West Company
Mendocino County Executive Office
Mendocino County Workforce Investment Board
Mendocino County Promotional Alliance
631 South Orchard Avenue
Ukiah, CA 95482-5011

Study conducted by the Northeastern California SBDC
California State University, Chico
Chico, California 95929-0765
Phone: 530-898-4598
Fax: 530-898-4734
www.csuchico.edu/cedp/



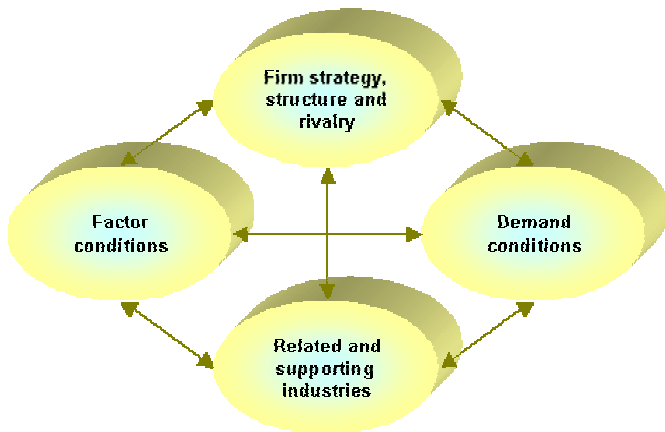
Introduction

Cluster-based economic development is a complex strategy, but successful implementation has proven to greatly benefit local economies in America.

The 21st Century concept of clusters started with Harvard Business School's Michael Porter, who defines clusters as "groups of similar and related firms concentrated in a small geographic area."¹ A cluster can be vertical (businesses in a particular supply chain in the same community) or horizontal (a group of businesses in the same industry).

A cluster often develops around a unique good supplied in the community (such as wine grapes) or an industry leader in the community (such as Microsoft). Both vertical and horizontal clusters may develop around both of these situations.

Porter's diamond of advantage concept is as follows:



Firm strategy and rivalry: the degree to which a community's firms compete and innovate

Demand conditions: the degree to which a firm's product is demanded in the community

Related and supporting industries: the degree to which a firm's suppliers exist in the community

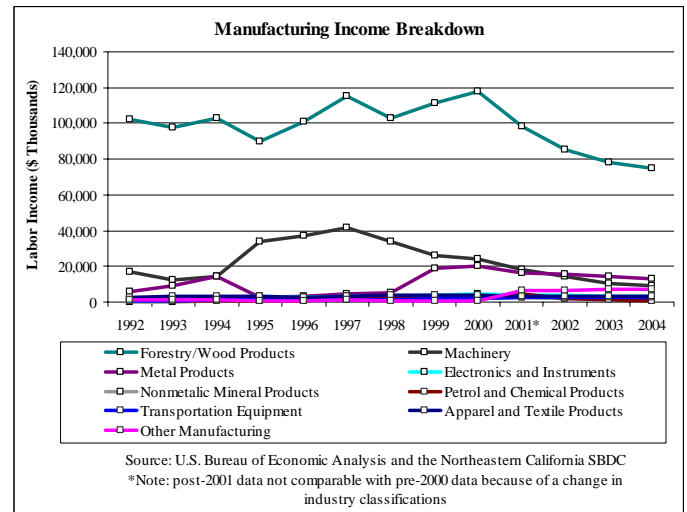
Factor conditions: the degree to which infrastructure and support necessary to the firm exists in the community

While most clusters in America developed without government influence, governmental agencies can encourage a cluster to develop by building the means by which local businesses interact and buy goods and services from each other.

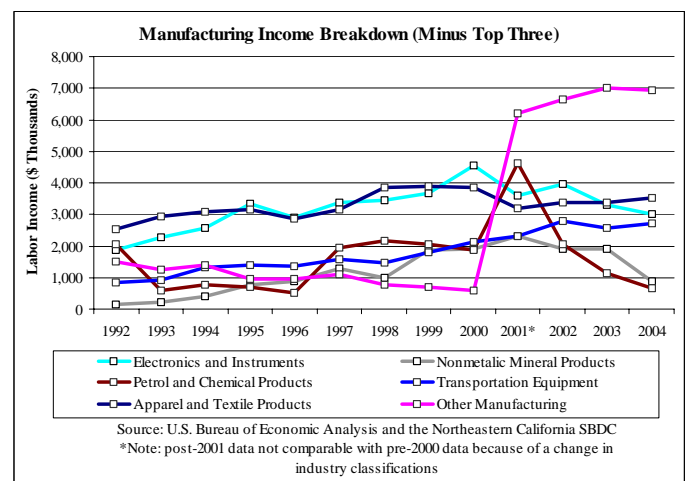
¹ Porter, Michael E. The Competitive Advantage of Nations. Simon & Schuster. 1990.
Revised 2/12/07

Mendocino Manufacturing Trends

Looking at manufacturing income data through 2004, all major manufacturing sectors had been in decline since about 2000. Despite deep cuts in production, forestry and wood products, including logging, continues to dominate Mendocino manufacturing. Machinery and metal products, the two largest groups after forestry, are both in decline.



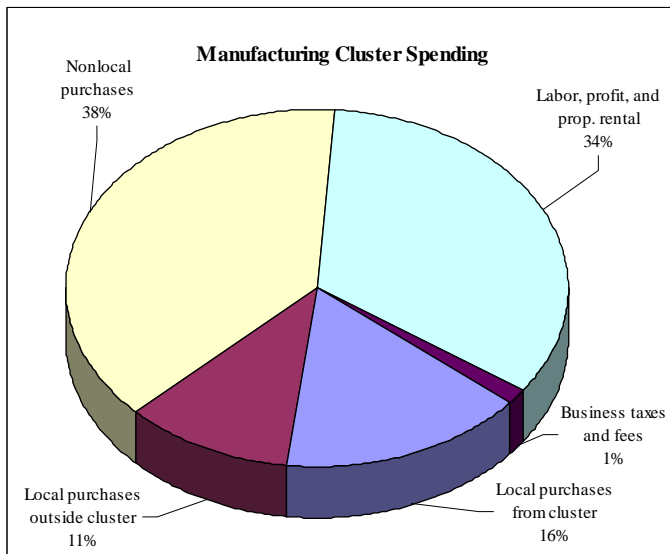
Zooming in on the bottom six industry groups by excluding the top four, we see that there may be some bright spots in apparel, transportation equipment, and other small-industry manufacturing, but there is no rapidly-developing manufacturing industry cluster through 2004.



Note: Food and beverage manufacturing is not included here because $\frac{3}{4}$ of all production in this sector is wine, which will be covered in another cluster brief.

State of the Existing Manufacturing Cluster

A strong cluster is indicated by local purchases from the cluster exceeding all nonlocal purchases. In Mendocino County's manufacturing sector, nonlocal purchases (yellow in the chart below) is more than double local purchases from the cluster (blue). Therefore, much needs to be done to develop the manufacturing cluster in Mendocino County into a significant economic engine.



Source: IMPLAN Economic Impact Analysis System

The first step is to examine what Mendocino manufacturers are buying outside of the county. Utilizing the IMPLAN economic impact analysis system, the Northeastern California SBDC is able to calculate imports by industry. The top ten nonlocal suppliers of Mendocino County manufacturers are listed below with primary products made in Mendocino County with those supplies in parentheses. These imports were valued between \$32 and \$6 million in 2003.

1. **Wholesale trade** (wood products, food, lumber, beverages, carpet, structural metal, transportation parts)
2. **Forest nurseries and timber tracts** (lumber, wood products)
3. **Imported labor** (forestry services, food, carpet, beverages, transportation parts)
4. **Profits to nonlocal owners** (food and beverages)
5. **Logging** (lumber, wood products)
6. **Fiber, yarn, and thread** (carpets)
7. **Organic fiber** (carpets)
8. **Specialized prof. & tech. services** (wood products)
9. **Metal containers** (beverages)
10. **Iron and steel** (beverages)

What Manufacturers Need

The following are a list of documented needs and requirements sought by growing manufacturers.

Access to Resources: Manufacturers need access to the goods they use in their processes. Mendocino County has ready access to lumber and can easily develop production of wood products needed by other manufacturers

- Input products (varies widely by subsector, i.e., wood, rock, and other manufactured products)
- Business services

Access to Markets: Manufacturers mostly sell to other manufacturers or to wholesale trading companies, either local or places with relatively inexpensive transportation

- Wholesale trade
- Retail trade
- Sales directly to mass-market customers
- Internet sales
- Assistance with advertising/promotions (i.e. economic gardening and regional branding)

Access to General Labor: Manufacturers need access to honest and trainable blue-collar labor to handle directed, repetitive tasks

- K-12 education
- Vocational training/ROP programs

Access to Skilled Labor: Manufacturers need specialists in their field to provide innovation that allows the manufacturer to continue to be competitive

- Colleges and universities

Inexpensive Land and Buildings: Manufacturers need low-cost inputs to compete with other low-cost places to do business domestically and abroad.

- Real estate
- Construction
- Special incentive districts (RDA, EZ, etc.)

Investment Capital: Manufacturers typically invest in expensive equipment to produce their products.

- Finance
- Entrepreneurs
- Investors

As more of these resources become available in Mendocino County, and as more local manufacturers use them, the manufacturing cluster in the county will strengthen and produce increased jobs and wealth for its residents.

Manufacturing Customers

The top ten nonlocal customers of Mendocino County manufacturers are listed below with products purchased in parentheses. The value of exports to each sector ranged from \$124 to \$10 million in 2003

1. **Households** (food, beverages, carpets, transportation parts, tires, wooden art)
2. **Paper mills** (lumber, wood byproducts)
3. **Single-family housing** (wood products, carpets)
4. **Restaurants** (food, beverages)
5. **Sawmills** (lumber, forest products)
6. **Commercial construction** (wood products, structural metal)
7. **Processed wood manufacturing** (lumber)
8. **Logging** (lumber, forest products)
9. **Home maintenance** (wood products)
10. **Commercial maintenance** (wood products, structural metal)

The existence of households at the top of this list is significant, not only because households purchase manufacturing goods valued at three times that of the second industry, paper mills (\$44 million), but underscores the link between local manufacturing and tourism. In this way, manufacturing can be seen not only as a cluster, but may be more appropriately analyzed as a sector in a cluster involving tourism.

Lumber and wood products is prominent on both the list of imported and exported products in Mendocino County. Because of this, there may be opportunities to strengthen this sector of the manufacturing cluster without cutting down more trees. If local economic development can find products produced in the county that are exported, while other local businesses are importing the same commodity, then a new intra-county sales link may be established that would strengthen the cluster by reducing imports and increasing local sales. There are \$95 million per year in unprocessed forest products exported outside of Mendocino County every year. That is a lot of product that could be used to produce finished goods in Mendocino County if transport costs for those goods were low enough.

Food and beverages are also prominent exports in Mendocino County. A shared branding effort in the county or for the North Coast in general can increase the prestige and demand of Mendocino County food and beverage products, increasing sales for local manufacturers if they wish to expand their operations.

Capturing Economic Impact

Capturing the economic impact of manufacturing as a whole is more difficult than in most clusters, although increasing the economic impact can be done. Manufacturing is a diverse industry in terms of products used. The most common inputs are various farm products, wood, metal, rock, chemicals, and other manufactured products. Therefore, it is difficult to encourage the development of supplies that aren't already found in Mendocino County, like petroleum, gold, etc. Even for resources available in the county, like wood and rock, increasing extraction could decrease the economic and noneconomic value of the county. Still, there are three things the county can encourage to increase the economic impact of manufacturing.

1. Provide Services Manufacturers Need

Although they often work with different products, many manufacturers require the same types of services regardless of product, such as accounting, janitorial, business consulting, and more. Supporting the development of businesses that provide services to manufacturers and encouraging local manufacturers to utilize these services increases the economic impact of manufacturing growth.

2. Provide Products and Services Needed by Workers and their Families

Most households with manufacturing workers fit into several lifestyle categories with common spending patterns. Manufacturing workers are more likely to shop at home improvement, auto parts, pet, sporting goods, and warehouse food stores. Ensuring that the variety and price of these products is such that residents do not have to leave the county to do their shopping will ensure that the county can capture a greater share of a growing manufacturing industry.

3. Provide Housing for Households Earning a Manufacturing Income

Mendocino manufacturers import about \$25 million worth of labor every year, mostly from workers living in less expensive housing in Lake County. Mendocino County competes with Lake for spending from these workers. More affordable housing options in Mendocino County will ensure that a growing manufacturing workforce could live and spend more money locally.

Developing Manufacturing

Developing and retaining manufacturing in California has been difficult given the state's business and employment tax and legal structure. Highly cost-competitive manufacturers have left for other states and sometimes, other countries in an attempt to compete. However, not all manufactured products compete primarily on cost. Sometimes product quality, product origin, or the production process are more competitive factors than costs. This is true among organic products, for example. These are the types of products that are likely to be manufactured in Mendocino County.

The four ways by which local industries grow are as follows:

Creation: Business creation is sparked by entrepreneurial people within a community.

Unfortunately, most businesses do not last more than five years and those that are failing produce very little income and employment. Business counseling, for business owners choosing to accept it, has proven to increase the change of business success. It is important to demonstrate to Mendocino County's rural businesses early in development that business counseling is not for people who fail, it is for people who succeed.

Expansion: Business expansion can happen either when the market demand for a product grows beyond the producer's capacity, or a producer actively expands their product line or seeks new markets for their existing products. Either way, business expansion is responsible for the majority of new employment in a community and a multitude of expanding businesses in a sector typically lead to the development of a strong industry cluster as they purchase each other's products.

Attraction: Business attraction is the traditional way to develop manufacturing in a rural community. Rural areas are usually able to market low-cost land and high unemployment to lure new businesses. However, land prices in Mendocino County and its relatively low unemployment rate would make manufacturing attraction less cost-effective unless it is utilizing a vacant facility where manufacturing had taken place frequently and there are other benefits for the inquiring company to move to Mendocino County (such as customers, suppliers, and labor that can be tapped locally).

Retention: Retaining manufacturers in the county is critical. Existing businesses are more likely to have set up local supply chains than newer ones, so their economic loss is usually greater than the addition of a similar-sized company.

Policy Recommendations

Mendocino County has a few resources than can attract and grow certain types of manufacturers, but lacks some of the important resources that would allow manufacturing to grow and become a significant cluster. Policy recommendations focus on developing these resources

1. Support revival of the Northwestern Pacific Railroad between Suisun and Willits

Small manufacturing provides jobs to one or a few people, but before these firms could grow into substantial economic drivers for the county, regaining railroad service along the old Northwestern Pacific tracks to the national railroad network at Suisun is critical. Manufacturing can survive without the railroad, but it is unlikely to become a cluster in Mendocino County without the railroad that would allow inexpensive transport of large volumes of goods.

2. Identify and assist local manufacturers wanting to start a business or expand

Support organizations that provide services to small businesses such as the Redwood Empire Small Business Development Center (SBDC). The Northeastern California SBDC provides economic gardening data services to businesses looking for new customers. The West Company is the local outreach organization providing small business development services. They have offices in Fort Bragg and Ukiah.

3. Encourage manufacturers to purchase locally

The Northeastern California SBDC could not identify any specific product or service that manufacturers purchase outside Mendocino County that could be purchased locally, although local economic development should seek out such opportunities to increase sales and reduce imports whenever feasible.

4. Link manufacturers to governmental and nongovernmental resources available to Mendocino County businesses

Communicate the existence of assistance programs, such as the Economic Development Financing Corporation, economic gardening, and the redevelopment district to help manufacturers start up and expand in Mendocino County.