



Summary of Discussion with Dan McElroy

8301 Creekside Circle #920, Bloomington, MN 55437

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Present : Verne Johnson (Chair); David Broden, Janis Clay, Marianne Curry, Paul Gilje, Jim Hetland, Ted Kolderie, Dan Loritz, Tim McDonald, John Mooty, Jim Olson, Wayne Popham, Paul Taylor, Bob White

Key Points: *Despite the economic downturn, Minnesota's economy is sound and strong; although not growing quickly enough. The economy is diversified and clusters of like business teamed with a strong workforce make the state attractive to business. But this message is not being heard as it could be; in the media and with the consultants that make recommendations to large companies on where to open operations. There is promise for growth in new industries and reason to be optimistic.*

A. Context of the meeting - Minnesota will need a prolonged period of economic growth to create jobs and begin generating revenue again during this time of contraction. Mr. McElroy is in a position to understand the state's assets and outlook.

B. Introduction

Dan McElroy is Commissioner of the Minnesota Department of Employment and Economic Development, appointed by governor Pawlenty in January 2007. He formerly served as the governor's senior advisor on innovation, after serving almost two years as chief of staff. McElroy served as commissioner of the Minnesota Department of Finance from January 2003 until February 2004.

McElroy served in the Minnesota House of Representatives from 1995 to 2003. During that time, he was an assistant majority leader, chair of the Committee on Jobs and Economic Development Finance and chair of the Legislative Audit Commission. McElroy served as mayor of Burnsville from 1987 to 1994 and as a member of the Burnsville City Council.

In the private sector, McElroy was active in the travel agency business from 1979 to 1994 and in the travel agency software and consulting business from 1994 until 2003.

C. Comments and discussion - During comments and discussion, the following points were raised.

1. Introduction to Minnesota Department of Employment and Economic Development —

"Despite all my background of government service," McElroy said, "for most of the last 40 years I've been running businesses. A serial entrepreneur-I didn't sell the last one until being tapped by Pawlenty."

He said that he thinks of himself as a policy wonk, not as an economist. "Which is good because sometimes I ask people questions they don't anticipate."

Employment and Economic Development are encompassed in a single agency McElroy said, because they are so closely linked. Through automation of various services, staffing was reduced from 1,900 to 1,600 people. The agency runs workforce development and adult job training, operates the state's unemployment insurance system, assists local economic and community development efforts, and operates the Minnesota trade offices. The agency also has an information role; publishing two magazines and information about the state online at <http://www.positivelyminnesota.com/> . Almost everything they do is through partners.

2. Minnesota's economy is sound and diversified, but not growing — John Adams (University of Minnesota) describes an economy as a mosaic with different layers. Minnesota is the sum of different sectors and regions. McElroy said his office spends an enormous amount of time bringing different resources together. "Economic development is an umbrella thought process on how, over time, to make a state more effective."

The government can play a role bringing people together. Some talk about silos McElroy said, but he calls them policy systems. These systems form the foundation of economic strength and are the fundamentals to a strong society: families, non-profits, early childhood education, K-12 and higher education, affordable housing, mental health, and transit.

In three months during 2007-2008 unemployment in Minnesota was slightly higher than national average. This was due in part to the hit taken by particular industries during the downturn; including housing and building components, primary construction materials and mortgage finance.

"We're back now to being below the national average of unemployment." It varies by region. Fargo-Moorhead is at 5 percent; Brainerd 19 percent. "The people who have been hammered in this recession are those who have little education."

McElroy said that he is cautiously optimistic. The number of people making new claims for unemployment have been dropping and has been below 4,000 for two weeks in a row-something not seen since 2007. The number of jobs on the state jobs board has doubled.

3. There is no button that government can push to jump-start the economy — "Recessions are cycles," McElroy said, and he is comfortable that we will come out of this. Art Rolnick said to him, "You know, there is no button government can push." It is a combination of liquidity, confidence and time. Liquidity started this mess with the credit crunch and high oil prices. Consumer confidence is key to keeping the economy churning.

Clustering of like-industries is important to the state. "A key is the size and willingness of the workforce to work." A member commented that the core economy of Minnesota has been said to run

from St. Cloud down through the Twin Cities, to Rochester? "Some of the new projects have been outside of that area," he responded. Part of the reason why Faribault has done so well is that it has had good partnerships with local government; it's rural enough that land is cheap but metro enough that there are a lot of workers.

The legislature is making efforts: The jobs bill passed this session included an angel tax credit and there was an increase in R&D tax credit from 5% to 10%.

He said that he is a *realist* on the economy. "Over the long term I'm optimistic. The unit of geography is the Midwest; we have the strength of a very strong workforce from educational and cultural points of view; strong wind and water; strong position in the middle of the continent."

A member commented that it seems to him to be inconsistent to be optimistic—that Minnesota has been dropping relative to other states.

4. Is Minnesota's economic position dropping?— "No, the data doesn't support that," McElroy responded. "It is not as bad as people say it is." He alluded to the role of the media in pushing this message and commented that "The Star Tribune is way off."

Minnesota has gone from 18 to 21 Fortune 500 companies, "the greatest number per capita, by a lot." Students continue to be at the top in ACT and SAT scores. The state will need to pay attention that it remains a place of innovation.

"The one I worry most about is growth in personal income—the energy states have blown us away; smaller states with large energy resources.

Responding to the public perception that Minnesota is not competitive, McElroy said that there are ways to improve competitiveness—comparative tax rates between C-corps, for example. "We've done some smart things about the R&D tax credit; foreign investment credit. Ernst & Young says we're around 18th in smartness of our tax structure."

5. Minnesota's economic appeal is weaker than it should be — Minnesota does not make the finals with the location consultants used by major companies when they are considering a re-location or development. Those consultants do not have Minnesota on the top of their list.

He told a story that after one conservation technology company located a 160,000 square foot facility here, Deloitte remarked, "We're just shocked. Minnesota's not an attractive state. Minnesota's not a right to work state (<http://tinyurl.com/yc59dx>) and utility costs are high. But this company wanted to come "because of the strength of the glass cluster."

The time frame on the environmental review process is too long and utility costs are going to be an issue. "The decision to be early into renewables was a good decision over the long term, but will cost more now."

Minnesota's workers comp rates are higher than Western states, but this may not be all bad, McElroy said. "We provide better benefits and we have more generous unemployment pay. Culturally I don't think we're ready to (or want to) change them."

6. How well is Minnesota being marketed?— "You've read a lot of good news that I haven't seen before," a member commented. "Consumer confidence depends on information. What are you doing to publicize the state's strong points?"

McElroy said that he gives 150 or more speeches per year-spends a lot of time with the media. "It's hard to get good news on the front page." Minnesota won a competition for a plant, and he called their HR executive to ask what it was that closed the deal. "She said it is our workforce-hard working, honest, innovative." It's hard to make that a news story.

7. There is both a need and an opportunity to save money in state services — As you listen to the candidates for governor, a member asked, do any of the discussions alarm you to the future of the state?

"I don't get alarmed easily; I get excited. The two critical questions are whether we can slow the growth in the cost of health care and can we continue to engage people, non-governmental organizations and others to take services off government. I think the strategy Ted Kolderie, Joe Graba and Clayton Christensen are working on in education is on the track here."

He continued: "I get horribly frustrated with Tom Dooher and his office who are good people, but change averse. Joe Graba (a former union leader) said it best when he said everyone wants our schools to be better but nobody wants them to be different. I think there is a consensus now nationally that schools will have to change."

8. Concern over growth in medical expenses— What is going on with medical costs? "A state employee group insurance program targeted six disease clusters for intensive monitoring and oversight." He is convinced about the power of incentives. "A co-pay mechanism in my insurance plan was a significant part of why I lost weight-100 pounds and kept 85 off. I became convinced it was a health investment."

9. Minnesota's future economy— We cannot rest on our laurels, he followed. We are competing now on labor with countries in the developmental stage of their economies. We have got to lead by staying ahead on innovation.

10. State's main economic producers identified — A member asked where Minnesota makes its living-doing what, selling to whom-and what are the major movements in those areas?

McElroy responded that the big industry clusters continue to be manufacturing (high-tech, glass, building components); health care and medical device; two heritage industries-agriculture and food processing, retail and distribution is enormous; transportation including the port of Duluth and railroads.

Financial services continues to be healthy as well: "US Bank, Wells Fargo, TCF didn't do a lot of stupid things" leading up to the crash.

11. Possible change in the economy in the future — Where is the change going to be?

There may be pickup in alternative energies. "Offshore wind potential in Lake Superior is amazing." Visual impact and ice issues are going to be challenges, but he emphasized that the potential in the

water far surpasses anything on land. This can be a new sector for growth. And, biofuels: Liquid biofuels will also benefit from Minnesota's high tech and agricultural cluster.

"Companies and entrepreneurs come to Minnesota for the cluster strength. We don't have the financial incentives others have, but we do have diverse industries and a strong labor market."

12. Strategies for economic development — McElroy's office has four strategies for economic development:

1. Help Minnesota businesses stay and grow
2. Help entrepreneurs develop businesses here
3. Help existing businesses become more productive and competitive here
4. Help business relocate here

"Think of economy in terms of layers." The industrial revolution affected the foundational manufacturing layer. As layers get more productive it makes room for more layers; others build on top. Minnesota has got to recognize that more and more, other economies may be doing the first layers. We can stay ahead by being the highly productive and innovative in both existing and in new industries.

D. Closing

1. Essential steps for the future— The chair asked Mr. McElroy whether he had any messages he'd like to leave with. "That Minnesota continues to be a strong state and that we cannot rest on our laurels.

"Minnesota needs to make investments in infrastructure and the workforce without creating disincentives. We don't have to be the lowest tax state, but we need to be wary of where the hindrances are to business." He agreed with a remark made by Governor Pawlenty that the state needs to improve the value of services, improving on the line of cost per unit.

Thanks to Mr. McElroy for the visit today.