Triad Should No Longer Play the Low-Wage Game

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Last week, WUNC-TV aired the "Triad CEO Forum," a live broadcast from UNCG's campus that featured business leaders from the Triad in a panel discussion about the local economy and its future.

The panel members touched upon many familiar issues: the decline of traditional manufacturing industries, the need to be competitive in foreign markets, and the changing nature of the workplace. All talked about the importance of business leadership and of the role of education in training the workforce of tomorrow.

But as I listened to the CEOs, I began to think about a subtext of their discussion: the degree of differentiation of the Triad economy from other regional economies.

In the language of economists, this has to do with the *elasticity* of the demand for the goods and services the Triad produces. Demand elasticity is a topic that has frustrated generations of economics students, and if you ever took an economics class, you may have gotten a sick feeling in the pit of your stomach upon reading this paragraph. But the concept is actually pretty simple.

The more good substitutes a product has, the more elastic its demand is. And the more elastic its demand is, the more sensitive buyers are to changes in the product's price. Naturally, if a buyer can easily and conveniently go down the street and buy virtually the same product as the one she's considering, then a small difference in price will matter a lot. Sellers of highly elastic products have to compete primarily on the basis of price, and that kind of competition is brutal.

On the other hand, if the product in question is distinctive in some way, then small price changes matter less. To an economist, distinctiveness means that the product's demand is relatively *inelastic*. It has relatively few good substitutes, and so a price increase will drive fewer buyers away. The seller has more latitude to cultivate its position in the marketplace, and its profits tend to be higher.

Inelastic demand can arise for a number of reasons. The extreme case is monopoly, in which a single seller provides the product. True monopolies are rare, and even those that are mandated by the government, such as local cable-television franchises, are susceptible to competition from new technologies. Inelastic demand can result in varying degrees from reputation and brand image, convenience of purchase, and innovation.

In the business world, the few big winners of the high-elasticity game generally have a superior process that allows them to maintain low prices. The superior process partially immunizes the company from the vagaries of market price, and in a way it allows the company to act as though its product's demand is less elastic than it really is. But this is a fast-moving game, and it's not for the faint of heart.

In the world of regional economics, winning the high-elasticity game usually implies the existence of some particular geographical advantage, such as proximity to a mineral resource. Without such natural advantages, the high-elasticity game forces a regional economy to compete on the basis of low wages. That has been the

Triad's approach for decades, and for decades it worked well as the economy was focused on commodity manufacturing. But it's become apparent that such an approach no longer works.

I was thinking about inelastic demand and regional economics last month when I happened upon news stories about the labor disputes in Las Vegas. Restaurant and hotel workers have been threatening a work stoppage for some time now, and negotiations over wages and work rules have been on-going.

My initial reaction to the news was to predict a quick settlement, because entertainment is Las Vegas's dominant industry and it's a distinctive product. To be sure, opportunities to gamble seem to be everywhere these days, and there are plenty of other convention and vacation destinations around the country. But Las Vegas is different. New York may be the city that's so great they had to name it twice, but Vegas shares one-name-only cultural status with Madonna and Shaq.

So entertainment in Las Vegas has a fairly inelastic demand. Not only would slightly higher labor costs fail to change that, but the industry's fundamental profitability would make the lack of a labor agreement much more costly than the agreement itself.

I wish I could predict stock-market moves this well. Over the last couple of weeks, resorts and casinos along the famous Las Vegas Strip have agreed to a package of wage increases. Union officials are "extremely pleased" with the agreements so far. "We got what we asked for," said one union negotiator. As of this writing, there is still some uncertainty about how talks with downtown casinos will go, but the mood appears to be upbeat.

In these parts, the mention of Las Vegas often conjures up the oft-discussed threat that that city will whittle away at the success of the biannual International Home Furnishings Market in High Point. But the High Point market is in a strong position to resist Las Vegas's challenge, and for the same basic reason that Las Vegas is settling its labor disputes now.

The growth of off-shore production may be eating away at this area's standing as the capital of furniture manufacturing, but High Point remains the capital of furniture marketing and design. As long as Market officials focus on this dimension, High Point will be able to maintain its distinctive position in the furniture world. It's really about intellectual capital, not parking and hotel rooms.

And that provides a lesson for the rest of the Triad. Sometimes getting at the important issues requires a change of perspective. For example, we need to free ourselves from our historical low-wage mentality. We don't want to have a low-wage economy; we want high wages. But the idea that low wages are good persists, a vestige of the high-elasticity game the Triad has played for decades. And remember, that's a game we don't want to play any more. Yet even the authors of the McKinsey Report, the founding document of Action Greensboro, fell prey to that misconception when they used "low wages" as a positive factor in ranking city economies.

Because the Triad doesn't possess that singular geographical advantage, our ability to generate economic distinctiveness will depend on our cultivation of intellectual capital, through innovation and the fostering of our most promising industrial clusters. UNCG Chancellor Patricia Sullivan noted during the "Triad CEO Forum" that the university "doesn't make widgets; it develops human capital." Competing successfully with other regional economies will mean that in a sense, the same will have to be true for Triad industry as a whole.

The panelists on the "Triad CEO Forum," ended on a positive note. Mackey McDonald of VF Corporation noted that problems tend to create opportunities, and therefore the Triad economy has a lot of opportunities right now. And Bud Baker of Wachovia Corporation claimed that "the pessimists are always wrong in America." They'll be wrong here as well, but only if the Triad economy manages to become distinctive in some significant way.