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Sparking demand:

Industry, destination determine region's export opportunities



Wilco Machine & Fab may be based in tiny Marlow, Okla. (population 4,500), but the company has quickly established a global presence.

Founded 30 years ago, Wilco has developed a solid reputation as a manufacturer of bulk transport and storage equipment for the energy industry. But, in 2007, the company's leaders knew they needed to find new ways to keep the business growing and began work on developing the firm's first export plan.

Since then, the firm has embarked on an aggressive strategy of expanding its export market, targeting countries in Latin America and the Middle East where demand for its products is expected to grow significantly.

"The decision to pursue an export growth strategy was almost a no-brainer," says Anthony Chandler (pictured above), Wilco's vice president of administration. "Seventy percent of the world market is outside the U.S., and any growth will come from other countries."

Wilco hired more engineers to ensure its equipment would meet the needs of global customers. Following trade missions to Brazil and the Middle East, the company struck business agreements with firms in both regions. Currently, Wilco is looking into ways to expand into Russia and southeast Asia.

"You've got to be a solution provider," Chandler says. "Everything has to be customizable to fit a client's needs. You just can't sell a widget anymore."

Wilco is one of many companies looking for—and finding—opportunities overseas. United States exports were dealt a heavy blow during the financial crisis, but as the economy recovers from the recent recession, many economic forecasts call for continued growth in export markets.

In the Tenth Federal Reserve District—an area that includes Oklahoma, along with Kansas, Colorado, Nebraska, Wyoming, western Missouri and northern New Mexico—the prospects for export growth are also strong, say Chad Wilkerson and Megan Williams of the Federal Reserve Bank of Kansas City. However, the effect of export growth on the economies of individual states will vary based on factors such as industry mix and export destinations, they explain.

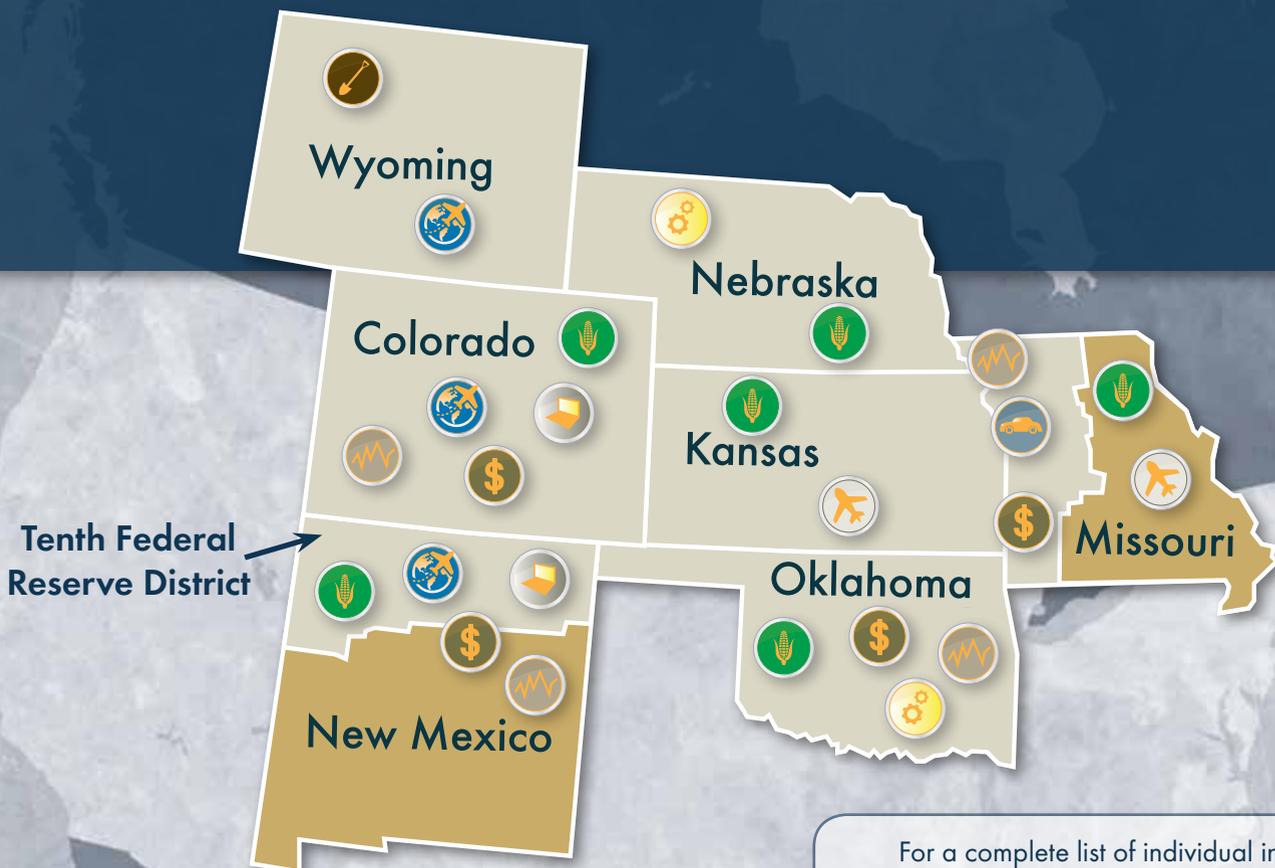
"Most states in the District are likely to see fewer benefits from exports than the rest of the nation, largely due to smaller export sectors and less-favorable industry mixes," says Wilkerson, who is the Kansas City Fed's Branch executive at its Oklahoma City office. "Of course, there are exceptions."

"In general, states in the District have

Regional Exports

One way to explain variations in export growth across the Tenth Federal Reserve District is to look at each state's industry mix. Throughout the District, several industries are responsible for a larger share of exports than the nation as a whole. This map shows the industries in each state that export more than their national averages.

- Materials and supplies
- Agriculture and food
- Computers and software
- Travel
- Aircraft and parts
- Royalties and other services
- Automotive parts
- Machinery and equipment
- Business and financial services



For a complete list of individual industries and export destinations, see Chad Wilkerson and Megan Williams' *Economic Review* article "The Export Potential of Tenth District States" at KansasCityFed.org/publications.

an adequate mix of trading partners,” adds Williams, an associate economist at the Oklahoma City Branch. “But other factors play a role in determining the District’s export potential.”

Recent export trends

During the height of the financial crisis, world trade essentially collapsed as credit became harder to get and firms pulled back on expansion plans, Wilkerson says. From the second quarter of 2008 to the same period in 2009, U.S. exports fell more than 20 percent, the largest decline in a half-century.

However, exports soon bounced back. By the second half of 2009, the sector began to recover, and by the first quarter of 2010, exports were up 16 percent from year-ago levels.

Among the industries benefitting from the recent rise are those producing manufactured goods such as automobiles, auto parts, materials and supplies.

“These industries suffered the biggest hit during the financial crisis, so logically, they had the most room to rebound,” Williams says.

U.S. exports have also rebounded in terms of destination, the economists say. By early 2010, exports to Asia were up about 30 percent from a year earlier, and exports to Canada and Mexico also experienced solid gains.

In the District, the decline in exports affected the regional economy less than the nation as a whole. This is largely because the District has a smaller export sector, accounting for just 9.5 percent of District gross domestic product (GDP), compared to 13 percent for the nation, the economists say.

Wilkerson and Williams add that as a result of the smaller export sector, the impact of the export decline on the District’s overall GDP was likely about two-thirds of that experienced by the nation. And, as global trade has rebounded, the export boost to the District has also been smaller proportionally when compared to the nation.

Explaining differences

When Wilkerson and Williams looked at the export activity throughout the District, they noticed wide differences among individual states. For example, New Mexico saw a 50 percent decline in manufacturing exports during the recent downturn, while Nebraska and Oklahoma saw declines of less than 15 percent. Likewise, during the national export boom of 2003-08, total exports from Kansas grew 40 percent faster than the national rate, while exports from Colorado and New Mexico grew about 30 percent less.

What accounts for the large variations?

“Several District states have unique export sectors,” Wilkerson says. “What and where a state exports can account for much of the difference in export trends.”

For District states, Wilkerson and Williams identified three important factors that help explain the differences:

- **Industry mix:** “Foreign demand for certain goods and services changes over time,” Wilkerson says. “Because different areas of the country produce different types of products, export activity can vary from state to state.” As a share of total exports, the District has a higher concentration than the United States in agriculture and food, aircraft and parts, travel, business and financial services, and royalties and other services.

- **Destination:** The District’s destination mix is similar to the nation’s in that the two biggest export destinations are western Europe and Canada. However, some District states, including Kansas and Nebraska, have a higher share of exports headed to Japan and eastern Europe. States that export to fast-growing countries or countries with favorable exchange rates can also have an advantage.

- **Local factors:** These factors include such things as attraction or loss of exporting firms, higher or lower exporting levels from current firms, the proximity of new trading partners, changes in the long-term costs of transportation

and communication, local policy differences, and changes in human and physical capital.

Wilkerson and Williams analyzed the relative contributions of these factors in determining the export growth trends for the District and each state.

The economists found that from 2003 to 2008, the District's export sector grew slightly faster than the rest of the nation due to a favorable industry mix, which, along with local factors, helped offset a slightly less favorable mix of export destinations. The District's large presence in agriculture and aircraft exports helped fuel this export boost, Wilkerson and Williams say.

Kansas' export sector, in particular, benefited from its heavy concentration of aircraft suppliers. Wichita, which has aircraft

facilities operated by Boeing, Cessna, Hawker Beechcraft and others, was recently named the top metro area in terms of export growth in a report from the Brookings Institution. The report said Wichita was one of four metros that doubled its exports during the last five years.

"The experience of Kansas shows how local factors, such as the concentration of large exporting firms, can provide a sizable boost to a state's total export sector," Wilkerson says.

For other states, such as Oklahoma, the mix of trading partners played a more important role. Oklahoma sends more exports than the national average to fast-growing Africa and the Middle East. The higher concentration of exports to those regions helped Oklahoma post faster-than-average export growth from 2003 to 2008.

WICHITA-BASED AIRCRAFT MANUFACTURER HAWKER BEECHCRAFT is a major exporter and a key part of the region's aircraft cluster. The presence of major exporters such as Hawker Beechcraft helped make Kansas the top exporting state in the Tenth District in 2008. However, the state's mix of industries and export destinations are not expected to be as favorable as the rest of the nation in the coming years, say economists Chad Wilkerson and Megan Williams of the Kansas City Fed.

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The outlook

Most economic forecasts predict strong U.S. export growth in the near future, with estimates of 10.5 percent annual growth through 2014. World economic growth, especially in emerging countries, is also expected to rise strongly. An estimate from the International Monetary Fund found global GDP could grow 4.8 percent in 2010 and 4.2 percent in 2011, with even stronger growth in developing Asian countries.

In addition, exporters are gaining support from policymakers, with the White House announcing a goal earlier this year of doubling exports within the next five years. Another positive factor for U.S. exporters is the dollar's comparatively weaker position against several currencies, making U.S. exports cheaper for overseas consumers.

Of course, how much the District will benefit from this expected export sector growth remains to be seen. Similar to the export boom from earlier this decade, much will depend on individual industries and destinations, Williams and Wilkerson say.

For example, automobiles and parts, along with machinery and equipment, could experience the fastest export growth among U.S. industries during the next few years. However, agriculture—a major District export—could grow much more slowly, but still at a 6 percent annual pace, according to some estimates.

In terms of destinations, China, Asia (excluding Japan), and Mexico appear to hold the most promising potential for U.S. exporters. Meanwhile, exports to Canada, Latin America and western Europe will grow much more slowly—but still likely more than 7 percent annually.

When this forecast is applied to the District, it appears the District's exports will grow more slowly than the nation, Wilkerson and Williams say. The District's higher concentration in agricultural exports and low concentration in automobile production

translate into lower export growth potential.

“But, the District is still likely to see strong export growth,” Williams says. “If the District's export industries grow as forecast, District exports would rise by about 9 percent annually through 2014. That's a strong increase, but about 12 percent slower than the nation.”

However, if the District's exports grew as their destination mix suggested, the District's export growth would more closely resemble the nation's, Williams and Wilkerson say.

“The trading partners of most District states are expected to experience solid growth in the near-term,” Wilkerson says. “Also, other factors, such as policies developed by local leaders and efforts to improve worker skills, will play important roles for individual states. The most successful regions could be those that develop their local resources to take advantage of the emerging global market.”

That solid growth could mean more opportunities for companies such as Wilco Machine & Fab, where executives clearly see potential for expanding markets.

“There's an enormous amount of growth opportunity,” Wilco's Chandler says. “We're having a lot of success, and companies not looking for export opportunities are really selling themselves short.”



BY BILL MEDLEY, TEN CONTRIBUTING WRITER

FURTHER RESOURCES

“THE EXPORT POTENTIAL OF TENTH DISTRICT STATES”

By Chad Wilkerson and Megan D. Williams
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COMMENTS/QUESTIONS are welcome and should be sent to teneditors@kc.frb.org.