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The Covid-19 Crisis of 2020 vividly demonstrates the consequences of four decades of the decline of US manufacturing. A combination of tax policies that favor financial services, trade policies that lead to deficits, corporate policy that drives outsourcing, technology policy that under invests in advanced manufacturing, and talent policy that undervalues STEM education, led to a lack of resilience, surge capacity, and redundancy in our supply base. These trends have undermined our productivity capacity, imperiled our defense industry base, and caused millions of people to lose their jobs. Now our very lives are threatened.

The dramatic impact of the Covid-19 crisis, and the unprecedented national public and private response it evoked, provides an opportunity for a fundamental re-thinking of the strategy to restore our productive capabilities.

Three major themes emerge:

First, in the US federal system, States play a necessary and critical role in policy development, program implementation, and political sustainability. Governors have clearly demonstrated the leadership role of the States in facing the Covid crisis. This is nothing new: over the decades, States have demonstrated their essential role administering federal funded programs, such as the interstate highway system, Medicaid, unemployment insurance, workforce training, and K-12 education.

David Osborne's Laboratories of Democracy (1988) describes the singular role of States in a variety of programmatic areas, reflecting the nation's diversity, State governments' granular knowledge of local conditions, and their greater agility in administration than the federal government. (Local governments can carry out important responsibilities, but only through State legislative delegations of authority – "Dillon's Rule".)

Second, States are a necessary component of a robust federal system, but not sufficient. The country needs leadership at the national level. Existing federal agencies do have the authority and flexibility to respond to unexpected challenges – if they are led by experienced administrators, have adequate resources, and value professional expertise, and have top level political support. (By contrast, see "Testing Blunders Cost Vital Month in U.S. Virus Fight" (NYTimes, March 29, 2020).

Third, large corporations – by themselves –have generally not been able to quickly pivot to repurpose their facilities, retrain the workforces, or reprogram their robots to respond to the immediate needs for crucial medical supplies. The decline of vertically integrated industrial systems through the Wall Street driven “asset lite” and “shareholder value” strategies, has created a highly efficient, just-in-time, global supply chain, which unfortunately lacks redundancy, resilience, and is blind to single source dependency in its lower tiers.

Yesterday, Rob Atkinson issued a brief white paper “Time for a Federal-State National Economic Development Partnership” – this is precisely what is needed to restore our domestic supply chains and it builds upon Stephen Ezell’s longer paper from the Spring – “Policy Recommendations to Stimulate US Manufacturing Innovation”

It is important to remember that small manufacturing firms are the base of our domestic supply chain. There are nearly 300,000 manufacturing establishments, 99% with fewer than 500 employees, employing about 50% of all manufacturing workers, and the majority of these firms have fewer than 50.

On this panel you will hear about leading examples of State and regional efforts to address supply chain issues helping small firms become more productive and competitive.

These programs are managed by non-profits organizations, academic institutions, state governments, but funded by federal agencies. They are effective and efficient, but sub-optimally funded and often bureaucratically constrained.

There are other good programs that operate in this space – EDA's Regional Innovation Strategies program and OEA's Defense Manufacturing Community Support Program provide assistance for regional strategies.

These programs primarily work on the "supply side" of the equation; but much more challenging is encouraging the use of domestic firms by OEM's - the "demand side."

President Elect Biden's BuildBackBetter -Buy America provisions is a good start – but needs to be strictly enforced through a rigorous waiver process coupled with robust supplier scouting outreach. This approach was proven during the ARRA response to the First Great Recession, in those sectors, such as Transportation, where federal agencies had a direct role. MEP developed an effective mechanism for identifying domestic firms that could deliver goods or had the capability to do so. Its efficacy was demonstrated again by the large number of grass roots local, state and regional efforts to identify suppliers of personal protective equipment during the Great Pandemic.

However, the relationship between private sector OEM's and their suppliers is more difficult to affect because it reflects a classic "market failure" – there is no incentive for OEM's to invest in long term relationships with their suppliers because they can appropriate the full value of such investments . This is driven by the financial markets focus on stock prices, shareholder value as the goal of a corporation, and the consequent outsourcing of functions, the offshoring of supply chains, resulting in the creation of asset lite firms. The result is that purchasing decisions are transactional, purchasing offices are generally evaluated on the basis of cost savings.

Sue Helper and colleagues such as John Gray at Ohio State have examined this challenge; Harry Moser of the Reshoring Initiative has analyzed the Total Cost of Ownership in an attempt to persuade private firms that utilizing domestic suppliers, and reshoring in particular, is financially beneficially, when all risk factors are taken into account.

Although the private sector dis-incentives to invest in domestic suppliers cannot be re-balanced by State and regional programs – it is primarily a federal responsibility – States and localities can adopt some programs to influence private sector purchasing decisions.

What are some of the concepts that can drive this forward?

First, federally funded and managed national systems, like MEP, SBDC, and NNMI, generate "network effects." As Rob Atkinson writes – "A Federal-State Paretnership would be greater than the sum of its parts."

Second, all relevant federal policies should have an explicit "reshoring" criteria – analogous to OMB's assessment of the impact of new regulations, or CBO's scoring of legislation.

Third, States have effectively demonstrated their ability, in key areas where they have regulatory and purchasing power, to change private behavior. California's environmental standards have affected auto emission controls. Of course, few States have California's impact, but the use of inter-state compacts could leverage individual assets. The Regional Greenhouse Gas Initiatives is just one example.

Fourth, federal grants in aid should be aggregated to provide incentive to change local behavior. Any funding for economic development should have an explicit, and rigorously enforced non-poaching agreement. The wasteful, counter-productive, relocation and attractive exercises (think Amazon's HQ2) squander resources and distort investments. (See Greg Leroy, Good Jobs Now) A better model is the Obama era DEd Race to the Top, which required local educational reform as a condition of receiving funding.