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THE RECALL CAMPAIGN

A Variable Climate

■ To one company, California remains the place to be. To another, the cost of doing business has become too much.

By Marla Dickerson, Times Staff Writer

Some of the busiest workers at **Spirit Apparel Inc.** these days are washing down equipment that's being stripped from the factory.

Slammed by burgeoning costs, the Orange County silk-screening company is laying off most of its 200 employees this month, when it will shift production to a new facility in Mexico.

"We cut everything we could think of, but it just wasn't enough," said President Al Rowland, watching employees folding some of the last sweat shirts to be printed at the Irvine plant. "Financially, California just doesn't pencil any- more."

The state's high business costs also are a major concern for Pulmuone USA Inc. Yet the subsidiary of South Korean food giant **Pulmuone Co.** has pinpointed Southern California as its beachhead for conquering the U.S. market for soy-based products. In August the company cut the ribbon on a \$14-million tofu plant in Fullerton, its second major facility to open in the region in the last eight years.

"California is critical to our growth strategy," sales director John Sim said. "I'm not sure there is anything that could drive us out."

How two manufacturers of inexpensive, low-margin products could come to such opposite conclusions underscores the schizophrenic nature of California's economy: By many measures, the state is one of the worst places to do business. Yet at the same time, it remains one of the world's entrepreneurial hotbeds.

With its spiraling costs for everything from labor to insurance, overall business expenses in California are 32% above the national average, according to a recent study by the Milken Institute, a Santa



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Monica think tank. Electricity bills typically run twice those elsewhere, and companies in the state pay the country's highest workers' compensation premiums.

Such comparisons have made California's business climate a top issue in the gubernatorial recall race and have brought business recruiters from as far away as New Hampshire. They're urging revolt as part of their "Live Free or Die Tour."

"If you are looking at the pack of states with which we compete, we are not in the running," said Steve Spears, principal with SAER Group, which just gave California an F on an economic development score card. "When you get down to the core items that a businessperson has to look at to make it economically, we just totally flunk."

Yet for all that, California's \$1.4-trillion economy remains one of the most vast and dynamic anywhere.

New business incorporations in the state have surged this year to levels unseen since the height of the last economic boom. California continues to outpace the rest of the country in population growth and personal income. And by 2005, UCLA forecasters predict, the state once again will be a leader in job creation, just as it has for much of the last half-century.

California's economic advantages are substantial. With its large and diverse population, the state is one of the world's most desirable consumer markets. Strategically perched on the Pacific Rim with the West Coast's largest port, it is the nation's prime gateway for booming trade with Asia. And being in California means having access to the leading centers in industries such as entertainment, technology and biomedical sciences.

Even though some companies and residents have fled California — fueling sound bites on the campaign trail and soul-searching over whether the Golden State's dream has lost its promise — that's only half the story in the eyes of UCLA economist Tom Lieser.

"There's a tendency by natives to think it's all gone to heck in a handbasket," he said. "But there's always a new bunch of migrants who don't view it the same way. To the new arrivals, it's still a wonderland."

Trouble in Paradise

For Spirit Apparel's Rowland, it is indeed paradise to live in California. He just can't afford to do business here.

The move to Toluca, Mexico, outside Mexico City, is one he didn't want and couldn't have imagined when he started the venture in 1983 with a partner and then-wife Kim Herbert to print T-shirts for the nearby surf wear industry. One small order from **Quiksilver** Inc. multiplied into a business that eventually employed 300 people at its peak in 2000.

"It just kind of blossomed," Rowland said.

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The partners were riding a wave of California garment production that for years managed to defy the global forces that were pulling under Southeastern textile factories. By focusing on quick-turnaround, up-to-the-minute fashion items and specialty niches such as surf wear and swimwear — and aided by Latino and Asian immigrants willing to work cheap — the state's apparel manufacturers added jobs well into the late 1990s. This happened even as employment in the industry was plunging nationwide.

No longer. The state's garment industry has been brutalized over the last three years, shedding nearly 28,000 net jobs — a whopping 23% of its employment base — compared with about 15% for California's manufacturing sector as a whole.

Much of the blame lies with low-wage foreign competition and demands for ever-lower prices from U.S. retailers. Rowland says the amount he is paid to print logos and designs on garments hasn't changed in a decade.

Yet his operating costs have soared. His power bill tripled after California's botched energy deregulation plan. Workers' compensation costs more than quintupled, from \$96,000 in 1999 to \$540,000 currently. Meanwhile, minimum-wage increases in 2001 and 2002 — which bumped up California's minimum hourly rate to \$6.75, compared with the \$5.15 federal standard — only added to Spirit Apparel's labor costs.

Rowland, who has been running on a profit margin as low as 2 cents a garment on some items, said there was no way to make all that up. He said he lost money the last two years, hoping for a turnaround that isn't coming.

"We didn't want to close the doors, so we decided to move our doors instead," he said. "We had a good run here. But continuing in California wasn't an option."

Spirit Apparel's Mexican plant is up and running with 75 workers and is expected to employ 300 within a year. Rowland and Herbert will remain in Orange County, along with a small customer service and product development staff. Longtime employees such as Cilvia de la Cruz must find employment elsewhere.

"I'm scared," said De la Cruz, who started out laundering T-shirts and worked her way up to management assistant. Now 36, she has been with Spirit Apparel half her life. "I've never worked anyplace else. This is my family."

To business leaders, the loss of manufacturing jobs is particularly worrisome because they tend to pay above-average wages, create spinoff jobs in other parts of the economy, generate exports and provide less-educated workers such as De la Cruz a ladder to the middle class. Some production workers at Spirit Apparel earn as much as \$16 an hour. But manufacturers also are more exposed to global competition than are other sectors such as services or government, and thus are hypersensitive to business costs.

Los Angeles consultant Larry Kosmont, who conducts an annual survey on regional business costs, said it was unlikely that the industrial sector would rebound even when the economy picked up. He said that although some

manufacturers would undoubtedly continue to thrive in California's giant consumer market, many others would be forced to go elsewhere.

"It's what I call the showroom economy," Kosmont said. "We sell the Mercedes here, but we don't make it here. We get the well-dressed salesperson on the showroom floor, but all the folks who made the product are somewhere else."

Turning Tofu to Gold

Executives at Pulmuone Co., South Korea's largest maker of tofu with \$400 million in sales last year, were undeterred by the Golden State's business barriers when they chose it to anchor their U.S. operations.

Although plenty of other places offered lower costs, the company was more interested in tapping into California's huge base of Asian immigrants, particularly Koreans, who already knew the brand.

The company's beginnings in 1991 in Los Angeles were humble: Four employees took turns driving a delivery van, peddling imported noodles and chili paste to ethnic markets around Los Angeles, which boasts the country's largest Asian population at 1.3 million.

Business proved so brisk that Pulmuone (pronounced pull-moo-WON) opened its first tofu plant in South Gate in 1995. In the midst of Southern California's deep recession, it was soon cranking out jiggly blocks of soybean curd at full capacity.

Scott Jung, purchasing manager for a small group of Los Angeles-area supermarkets, said Pulmuone swiftly became the favored brand among his mostly Korean immigrant customers.

"It was a sensation," said Jung, whose company's holdings include three H.K. Super Market stores and the Galleria Market in Koreatown. "Customers knew that Pulmuone was a good company. They liked the high quality."

Although some food processors have fled to neighboring states or even south of the border to serve the big Southern California market, Pulmuone's Sim said that has never been a consideration for his company.

"Our emphasis is on fresh, safe, natural products," he said. "We had to be close to the market."

Tofu is a price-sensitive commodity in Los Angeles, with two 18-ounce trays selling for as little as 99 cents at some Asian grocery stores. To compete, Sim said, Pulmuone has relied heavily on automation to wring labor out of the process. The gleaming tofu line in the Fullerton plant can run full tilt with only three workers, compared with 10 at the South Gate facility.

On a recent day, the factory floor in Fullerton was virtually deserted as Sim explained to a visitor how soybeans are soaked, mashed, cooked and filtered to extract protein-rich milk, which then is coagulated, pressed, sliced, packaged and pasteurized. Human hands never touch the product until it

rolls off the assembly line, where it is transported to a giant cooler to chill before being shipped to customers.

"We'd like to employ more people, but in this environment we have to be extremely cost efficient," Sim said. "California's business climate is tough. But instead of fighting it or leaving, we built a state-of-the-art factory."

Such productivity gains have been the key to many California companies' succeeding and creating wealth despite the state's well-deserved rap as a high-cost place to do business.

In fact, California has for many years exceeded the national average for productivity across many industries, and in 2000 the state ranked sixth in real output of goods and services per hour of work, according to the Federal Reserve Bank of San Francisco.

Low-cost tofu is fine. But Sim says his firm's future rests in creating higher-margin products for the mainstream market.

The company recently developed a line of soy-based smoothies and soon will introduce its grilled, diced and marinated "gourmet" tofu, in flavors such as chili lime and Sicilian tomato basil.

To Sim, freewheeling, health-conscious California has proved to be the perfect location for his company's product development. With 55 employees and \$13 million in U.S. sales, Pulmuone is shooting for \$100 million in U.S. revenue within four years.

"This market is incredibly dynamic," Sim said. "We're very confident about our future here."

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