TRADE AND MANUFACTURING

BY HAROLD KING

What's the Deal?

Trade, Trade Agreements and Hudson Valley Manufacturers

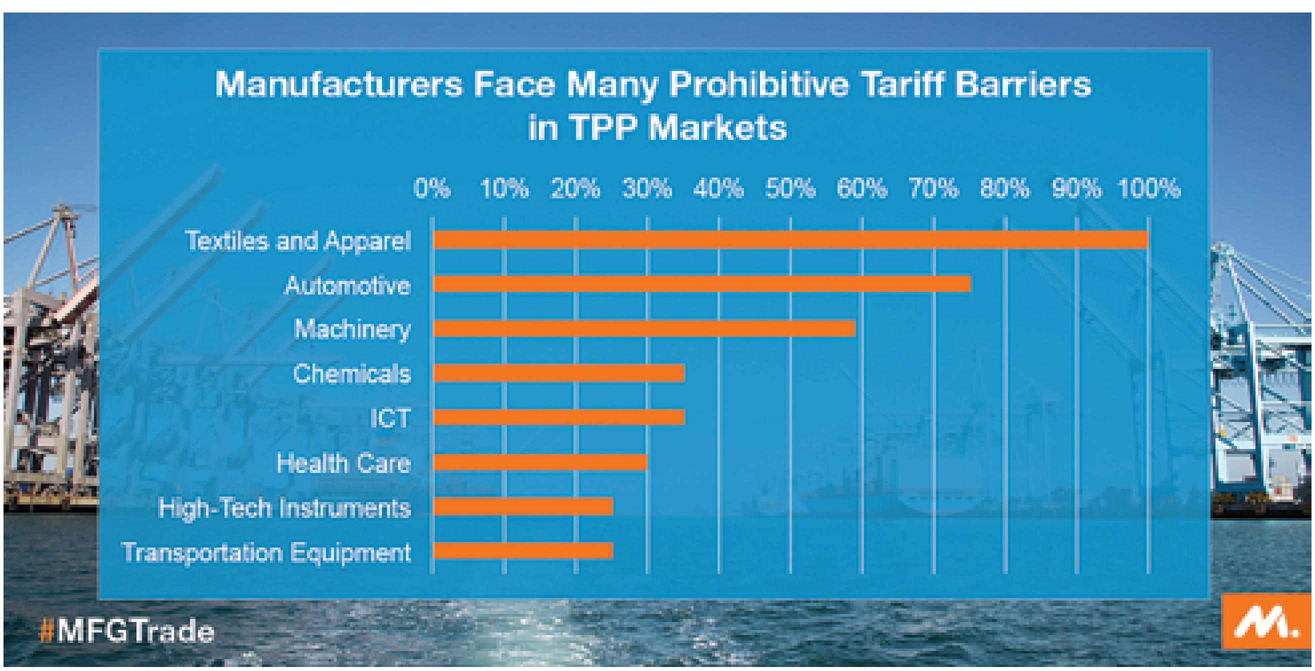
With all the negative talk this election season about the impact of globalization and trade on our economy we look at the pros and cons of trade and trade agreements and their effects on Hudson Valley Manufacturers.

International trade and the rules that govern it are front and center in this year's national election campaigns. Both major party candidates, as well as the Green and Libertarian candidates, have to one degree or another, taken the position that trade deals have killed U.S. jobs and weakened the economy. This position surely taps into the angst felt by many voters, but is it accurate? Does free trade hurt the economy or does it help? As is usually the case the answer is complicated and depends on a variety of factors and since our interests at HV Mfg are specific to one industry in one region we will attempt to answer the question: "Are trade agreements a net positive or negative for Hudson Valley Manufacturers and their employees?

One variable that makes even this narrow question difficult to answer is the simple fact that when we say "Hudson Valley manufacturers" we are using a geographical moniker that describes only one aspect of what are really many different types of companies. Some are small firms with a single location here in the Valley whose customers are largely other local companies. Others have a single location in the region but sell to customers around the world. Many are part of larger companies with multiple location throughout the nation and the world, while still others are foreign owned companies producing locally. Obviously trade agreements will effect these firms in different ways.

This is Not a New Debate

The role trade should play in our economy has been a subject of debate since the nation's founding. Tariff receipts were the major source of revenue for the federal government for the nation's first 50 years or so, accounting for fully 90% of annual revenues. Trade policy became contentious numerous times in the 19th century including during the Civil War, but one of the fiercest debates occurred at the turn of the 20th century. At that time the early progressives fought to tear down trade barriers which, they argued, protected cartels and made goods more expensive for the average citizen. President Teddy Roosevelt famously bucked his Republican Party to lower tariffs on many goods in 1909 while his successor Democrat Woodrow Wilson was elected largely on a tariff reduction



platform and accelerated the lowering of tariffs throughout his first term. That policy was reversed in what is perhaps the most well known tariff legislation – Smoot-Hawley – which dramatically raised them in 1930 forcing retaliation from other nations and the deepening of the great depression.

Since the end of the Second World War and the establishment of the General Agreement on Tariffs and Trade (GATT) in 1947 trade policy has been liberalizing steadily amongst capitalist nations with tariffs and other barriers steadily being reduced.

Alphabet Soup - Free Trade Agreements

During this liberalization there have been numerous multi-lateral and bilateral agreements to promote trade. In addition to the aforementioned GATT the most significant multi-lateral agreement the United States is a party to is the North American Free Trade Agreement (NAFTA) between the U.S., Canada and Mexico. As for bilateral agreements we are party to more than 20 with nations that include Australia, South Korea, Columbia, Israel and Singapore. The U.S. is also a member, along with 122 other nations, of the World Trade Organization (WTO) an intergovernmental organization which regulates international trade amongst its members.

It is a proposed new multi-lateral agreement that has thrust international trade back into the forefront of political debate: the Trans Pacific Partnership (TTP) involves 12 countries: the US, Japan, Malaysia, Vietnam, Singapore, Brunei, Australia, New Zealand, Canada, Mexico, Chile and Peru. The pact aims to deepen economic ties between these nations, slashing tariffs and fostering trade to boost growth. The agreement would create a new single market something like that of the European Union (EU). TPP was negotiated by the current administration under Trade Promotion Authority (TPA) where Congress gives the President of the United States the authority to negotiate international agreements that Congress can approve or deny but cannot amend or filibuster.

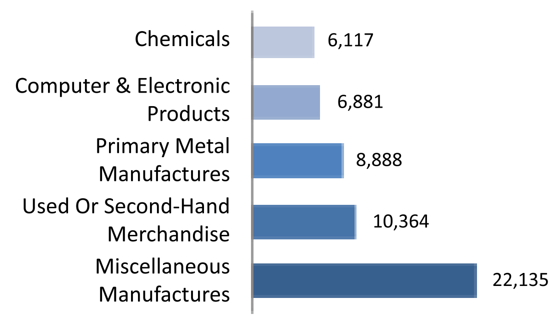
The Case For TPP

Supporters of TPP argue that the benefits of removing tariff and non-tariff barriers that restrict global trade and investment of goods and services are significant. First, the sheer volume of trade that exists between these nations is huge and reducing barriers will improve efficiencies. Second, the TPP – which seeks to govern exchange of not only traditional goods and services, but also intellectual property and foreign investment – would promote trade in knowledge-intensive services in which U.S. companies exert a strong comparative advantage. Third, killing the TPP would do little to bring factory work back to the U.S. or other countries involved, while the potential gains of the TPP for manufacturers of high value goods are significant. Finally, it is argued that although China is not part of the TPP, enacting the agreement would raise regulatory rules and standards for several of China's key trading partners which would, in turn, pressure China to meet some of those standards and cease its attempts to game global trade to impede foreign multinational companies.

The Case Against TPP

There are several arguments pointing at the risks to implementing TPP: First, given that many of the participating nations feature less expensive labor markets, it is feared the agreement would lead to an accelerated loss of good paying factory jobs. There are fears about the impact such a wide-ranging agreement might have on intellectual property laws and patent enforcement – there is concern for example that the deal may extend the scope of patents in sectors such a medicine and prevent the distribution of generic drugs. More concerning to many is the suspicion that the deal would enable foreign corporations to skirt domestic courts and directly challenge our health, environmental and other public interest policies before extrajudicial foreign arbitration boards. Finally, a major criticism is that TPP was negotiated behind closed doors and the complete agreement has been seen by few outside of Congress and the administration. That lack of transparency and accountability in this highly important agreement is a major concern.

New York's Top 5 Export Industries
(Value in Millions of US dollars)



**Indicates that portions of the MSA are shared with one or more other states.*
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Department of Commerce, International Trade Administration

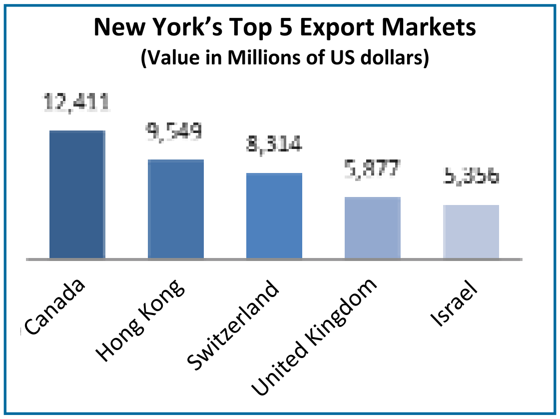
Free Does Not Necessarily Mean Fair

Nearly all manufactures in the United States are for trade deals that are both free and fair, but free trade does not always mean the playing field is level. Critics point to 2 significant issues that make American goods and services less competitive with their overseas rivals – even where free trade deals are in place. The first is the Value Added Tax (VAT). Many nations – particularly in Europe employ this tax on all goods and services sold in their countries. VAT taxes goods – as the name implies – at each stage where value is added. Exports from VAT countries enjoy rebates of VAT taxes which goods sold domestically in those same countries would be subject to. U.S. exports to those countries receive no such rebate of federal taxes and much smaller relief from state sales taxes. This problem is compounded because imports into VAT countries are subjected to VAT at the border, while imports into the U.S. are not taxed at our border. As a result, U.S. exports are taxed twice, while exports from VAT countries are traded free of certain types of taxes.

When a U.S. made good – say a car – is exported to, Germany for example, a VAT is added to the cost of that car. Conversely, however, since the United States has no VAT when a German company exports its car to the United States, no such tax applies.

Currency manipulation is the second major concern of "Fair Traders." Currency manipulation is a policy used by governments and central banks of some of America's largest trading partners to artificially lower the value of their currency (in turn lowering the cost of their exports) to gain an unfair competitive advantage. Simply explained, in order to weaken its currency, a country sells its own currency and buys foreign currency – usually U.S. dollars. Following the laws of supply and demand, the result is that the manipulating country reduces the demand for its own currency while increasing the demand for foreign currencies. With its own currency weaker the cost of U.S. exports to that county increase, making them less attractive to consumers. The converse is also true making their exports to the United States more attractive to consumers.

Any trade deals that do not address these issues, critics argue, are not creating a level playing field for competition.



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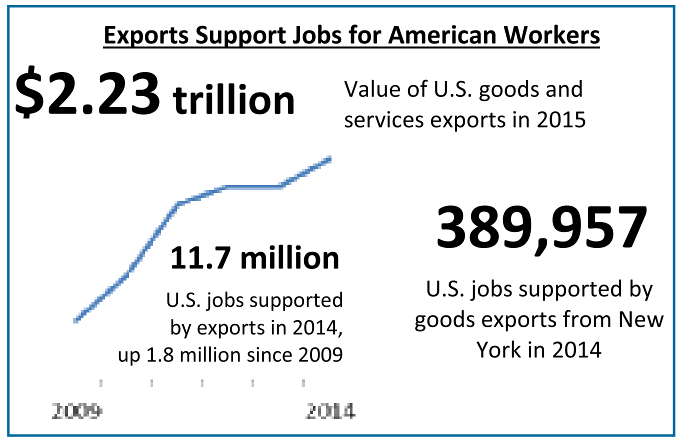
The Question at Hand

With all that said the question remains, is free trade or more particularly free trade agreements, good or bad for Hudson Valley manufacturers and their employees? Given what we know the answer is –for the most part – good.

For all their diversity in terms of products, ownership and customer base, Hudson Valley manufactures tend to have a few important things in common, they produce innovative, high quality, high value added goods efficiently and effectively - and they export. The relatively high cost of producing goods in New York has meant that high volume, labor intensive lower cost goods have long since gone from our region. What remains are innovative companies with high quality products that are in demand around the world. (MPI and Ertel Alsop featured in this publication are good examples) Any agreements that reduce tariffs and other barriers to trade make these Hudson Valley products more attractive. What's more most of what is manufactured in the Hudson Valley are goods and equipment used in the production of other goods. Semi-conductors for computers, food processing equipment and building materials for instance. High value products that are bought by firms overseas which in turn use them to make consumer goods that may eventually find their way back to the United States.

This is not to say that all firms benefit. Far from it in fact. Many firms, particularly some in the metal and plastic machining industry, face stiff competition from abroad. This is in spite of the fact that many have invested heavily in advanced equipment and technology. Reduced trade barriers have invited competition in these and other industries to compete for customers. It is also not to say that trade agreements cannot be improved, or that future agreements should not include provisions on VAT and currency manipulation.



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What About the Workers?

Research from the Bureau of Labor Statistics found that the total number of manufacturing jobs peaked in the United States in 1979, 15 years before North American Free Trade Agreement (NAFTA) and more than 20 years before China became a member of the World Trade Organization in 2001, which opened that market more fully.

Far more damaging to employment numbers in manufacturing has been the revolution in technology and automation. As mentioned earlier the high cost of doing business in New York forced Hudson Valley firms to invest in technology and automation. The result is fewer workers producing more, however these workers have more skills and higher earnings. Trade liberalization has – again on balance – opened markets to Hudson Valley products enabling them to grow and prosper. According to the Commerce Department New York state exported $68.12 billion in manufactured goods in 2014 with $22.21 billion of that with our free trade agreement (FTA) partners. What's more 24.20% percent of employment in the New York State stemmed from exporting in 2011.

It's a close call – but for the most part more free global trade benefits Hudson Valley manufactures.