U.S. Senate Committee on Banking, Housing, and Urban Affairs
Subcommittee on Economic Policy
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"Steps to a Stronger U.S. Manufacturing Sector"
By Leo Hindery, Jr.
(Written Testimony)

The Manufacturing Imperative
The importance of the manufacturing sector to America and the American economy is, to most policy makers and economists, hard to dispute, yet over just the past 12 years U.S. manufacturers have cut 30-plus percent of their workforce, or more than 6 million workers. The manufacturing sector's contribution to GDP has fallen to around 12 percent from nearly 23 percent in 1970.[1] [2]

In a compelling statement in defense of the importance of manufacturing to domestic job creation and maintaining America's competitiveness and national security, Rich Harshman, President and CEO of Allegheny Technologies Inc., wrote: "*You can't just have a service sector as the underpinning of a successful, diverse and globally competitive economy. The type of economic diversification that can support a middle class and meet our international obligations mandates that the U.S. be a successful manufacturer*."[3]

The attributes and implications of the manufacturing sector are compelling:

1. *Largest multiplier effect*. Manufacturing has by far the largest employment multiplier of all sectors of the economy, at least three times that of any service sector, including the hallowed financial services sector.
2. *Productivity powerhouse*. Manufacturing productivity growth is consistently 60 percent greater than in the private, non-farm economy as a whole.
3. *Better wages and benefits*. Manufacturing employees earn, on average, 23 percent more than workers in other parts of the economy.
4. *Source of innovation.* Manufacturers are responsible for more than 70 percent of all business R&D.

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[1] "A Reality Check on American Manufacturing," Bloomberg Businessweek, September 10-16, 2012.
[2] Table B-1 et al. of the August 2012 BLS Employment News Release, http://www.bls.gov/news.release/pdf/empsit.pdf .
[3] "Made in America" special advertising section, Bloomberg Businessweek, September 10-16, 2012.

5. *Diversified employment*. And ethically, manufacturing employs workers at all skill and educational levels and reduces income inequality.

Yet even as we meet here today, the meager real economic recovery which we are experiencing has, in relative terms, substantially further disadvantaged production and non-supervisory workers.[4]

Size of the Manufacturing Sector

What we have consistently failed to do in America since about 1980 is appropriately 'size', so to speak, the sector.

Right now, the U.S. manufacturing sector employs about 12 million workers, or just 8 percent of the U.S. civilian labor force. However, work we've done shows that the sector needs to represent more on the order of 20 percent of total U.S. employment, otherwise periodic consumer-credit driven bubbles will continue to plague our economy while concurrently we will never bring to bay our several hundred billion dollar a year trade deficit in manufactured goods.

It's actually far more important that policy makers focus on our manufactured goods trade deficit, with its myriad adverse economic, social and defense implications, than on the more nuanced federal budget deficit. In fact, it's almost impossible to fix the budget debt without fixing the trade deficit.[5] Because, when you try to do that as we have for the last three years, the results of the austerity on jobs and the economy, especially for hard working lower-income Americans, has been devastating.[6] And we know, verifiably, that eliminating the trade gap in manufactured goods can be achieved without materially reducing Americans' standard of living.[7]

A National Manufacturing Policy

Perhaps the primary reason for America's dramatic decline in manufacturing is that unlike every one of its large trade competitors, the U.S. does not have an articulated all-of-government national manufacturing policy. U.S. Government policies related to access to financing, R&D and investment tax credits, taxes, foreign subsidies and domestic procurement must be integrated into a dynamic

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[4] Ben Casselman, "Job Gap Widens in Uneven Recovery," *Wall Street Journal*, November 11, 2013.
[5] Joseph Stiglitz, *Making Globalization Work*, 2006, pp. 245-68.
[6] Paul Krugman, "The Mutilated Economy," *New York Times*, November 7, 2013.
[7] Michael Mandel and Diana G. Carew, "Manufacturing in the App Economy: How Many Jobs Should We Aim For?" Progressive Policy Institute, May 2012.

cohesive strategy. Mandating the U.S. government develop a coherent strategy is an idea that has been proposed by a number of members of Congress and the Senate, and it's something that is long overdue.[8]

In considering a national manufacturing strategy, it is not simply enough to identify what the U.S. should be doing. Countries like Singapore, China, and others already prepare their own national economic strategies, where they indicate certain preferred sectors into which they deploy significant subsidies to build at home and attract companies from abroad. The U.S. should not turn a blind eye to foreign country's economic strategies, and rather should make a *defensive* economic strategy a key part of any national manufacturing strategy. This defensive strategy should focus on identifying key subsidies and unfair trade practices, like discriminatory technology standards, being used to build up local industries to the detriment of U.S. businesses and workers. And our trade enforcement agencies should get serious about forcing the disclosure of the subsidies and unfair trade practices and bring cases to stop them.[9]

Access to Financing

While commercial bank lending to the nation's large multinational manufacturers is fairly robust, more than a quarter of the small and medium-sized manufacturers (or SMEs) still cite "*lack of capital to grow*" as their biggest challenge, precisely at the time they need loans to hire more workers, buy new equipment and aggressively market themselves.

The banks' expressed reservation, as if out of the movie "Casablanca," is that these SMEs are "too dependent on short-term contract work"[10], which of course is what largely defines most manufacturing SMEs.

Part of the problem is our largest national banks' focus on *short-term financialism* and the attractiveness to them of generating revenues through secondary-market trading rather than from primary market capital raising and on-the-ground lending. The Dodd-Frank Act's reforms to ban proprietary trading, if meaningfully implemented, should help reorient the major banks away from betting on the ups

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[8] See S. 1709 Coons-Kirk bill on the subject, co-sponsored by Sherrod Brown, at http://www.coons.senate.gov/newsroom/releases/release/senators-coons-kirk-introduce-bipartisan-bill-to-create-a-national-manufacturing-strategy.

[9] See S. 355, Merkley-Enzi bill to require USTR to do a counter-notification of subsidies for any country two years in a row that does not meet its WTO requirements to notify on subsidies.

[10] Parija Kavilanz, "Manufacturers to banks: We need money now," CNNMoney.

and down on markets, and instead focus on raising capital for customers. More should be done as well.

Programs such as the State Small Business Credit Initiative, passed in the 2010 Small Business Jobs Act, also appear to offer a successful, flexible model that the Congress may wish to revisit and expand. States like Michigan have used the 2010 Act to fund collateral support programs, while others have used it to support loan losses by banks, allowing them to make loans that would otherwise not get made.

The U.S. also needs to be more realistic in its approach to public development banks. All of the world's leading industrial nations – *except the United States* – have important public development banks, which in the aggregate account for 25 percent of the assets of the world's banking system and 30 percent of the financial assets in the banking system of the European Union.[11]

Specifically to this point, all of the world's leading industrial nations, except the U.S., have important public development banks: Japan relies on Japan Development Bank; Germany on Kreditanstalt fuer Wiederaufbau (KfW); South Korea on Korea Development Bank; Brazil on Brazil Development Bank (BNDES); Canada on Business Development Bank of Canada; and of course China on China Development Bank. And by not deploying public capital to support manufacturing, the U.S. is putting our businesses at a competitive disadvantage and allowing foreign countries to pull jobs overseas, which is especially the case if the U.S. does not aggressively enforce illegal subsidy cases through WTO and U.S. domestic trade remedy law.

These countries also use their export-import banks far more aggressively than the United States uses its, often notably to make 'matching loans' to help offset foreign competition.

Another way to provide this funding is through a "Made in America Bonds (MABs)" program modeled on the Build America Bonds program that was created by the American Recovery and Reinvestment Act of 2009.[12] As proposed by Michael Lind and Daniel Mandel of the New America Foundation, Made in America Bonds would be a new class of tax credit bonds issued by states, local

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[11] Jose de Luna-Martinez and Carlos Leonardo Vicente, "Global Survey of Development Banks," The World Bank – Policy Research Working Paper 5969, February 2012.
[12] Michael Lind and Daniel Mandel, "Made in America Bonds," New America Foundation, March 22, 2010.

governments and other authorized entities, especially municipalities, to encourage the establishment and expansion of manufacturing in the United States.

Important aspects of the MAB program should be (a) "employment impact statements" to determine which proposed new manufacturing initiatives are most likely to create and support U.S. jobs and (b) "Made in America" requirements, since no single measure would do more to help resuscitate U.S. manufacturing employment than an all-of-government buy-domestic procurement requirement.

Another aspect of maintaining a level playing field with respect to access to capital relates to state-owned and state-invested enterprises (broadly defined as SOEs) operating on other than commercial considerations. The U.S. needs to establish a legal structure to prevent anticompetitive practices, and to then ensure that when they occur, there are specific legal remedies available.

We of course have laws against unfair trade – most notably the Sherman Antitrust Act passed almost 125 years ago and the Clayton Antitrust Act passed roughly 25 years later. But vis-à-vis the new world of foreign investment by SOEs, especially given China's "*go out*" strategy designed to promote its SOEs' foreign investments and activities, there is in reality little in current law to adequately ensure that U.S. workers, businesses and investors have a level playing field to compete for the ownership and control of important national economic resources. Compare this to Canada, which recently passed a foreign investment law that allows the government to review foreign investments in light of their impacts on Canada's national economic strategy.

Should a major Chinese or Vietnamese SOE seek to establish operations in the U.S. market directly or through takeovers of U.S. firms, there is now the real risk that such SOE could, given its below-market state-supported cost-of-capital and other behavior, unfairly compete with U.S. businesses, workers and investors, all without running afoul of our current antitrust laws. It's past time to update our foreign investment laws to ensure a level playing field, and the United Steelworkers have proposed some interesting ideas in their important position paper "Ensuring Competitive Markets."[13]

The 2012 Task Force on Jobs, which I co-chaired with USW President, Leo Gerard, also identified three investment incentives that should be made part of any overall access-to-capital initiative, including:

[13] United Steelworkers Union, Position Paper: "Ensuring Competitive Markets," June 2013.

- First, extend and expand Treasury's 1603 Cash Grant Program for manufacturing-centric renewable energy production.
- Second, extend the Advanced Manufacturing Tax Credit (Section 48c) of The American Recovery and Reinvestment Act (ARRA) in order to prompt further investments in qualified advanced energy projects at manufacturing facilities.
- Third, expand the Loan Guarantee Program of Title 17 of the Energy Policy Act of 2005 to include "energy-efficiency" investments.

Permanent R&D and investment tax credits *directly linked to job creation* would also play an important role in industrial revitalization. Such tax credits would help rehabilitate and renovate existing manufacturing facilities, provide incentives for purchasing new equipment, and jump-start new technologies and process-development.

Tax Reform

President Obama has said many times that, "It's time to stop rewarding businesses that ship jobs overseas, and start rewarding companies that create jobs right here in America."[14]

Two actions would significantly improve the financing prospects and the global competitiveness of the manufacturing sector:

- First, reduce the corporate tax rate from 35 percent to between 25 and 28 percent while getting rid of the corporate "tax expenditures" that have nothing to do with retaining existing jobs and creating new ones.
- Second, enact a value-added-tax (VAT) to offset the significant tax disadvantages now faced by American corporations on account of the VATs used by most trading partners, but not by the U.S. Right now, in order to attract overseas investment and retain domestic production, our major foreign competitors without exception use a lower corporate income tax combined with a VAT, the result of which is net higher taxes on U.S.-made products sold both at home and abroad.[15]

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[14] http://www.whitehouse.gov/the-press-office/2012/01/24/remarks-president-state-union-address

[15] Leo Hindery, Jr. and Michael Lind, "America needs a VAT," *Los Angeles Times*, May 24, 2010.

Building Our Physical Infrastructure

A key foundation of the manufacturing sector – and a widely recognized public responsibility – is infrastructure. Moving materials and goods – and workers – around the country and to market requires roads, rapid transit, bridges, ports and airports that serve 21st century needs. Right now, however, the U.S. is sorely underinvesting in infrastructure, and what's especially needed, for manufacturers of all sizes and for the nation, is a new large National Infrastructure Bank, ideally with the following principle characteristics:

- The Bank should be an independent financial institution owned by the federal government with overall capitalization of at least $1 trillion and with its primary source of leverage being the large state and municipal pension plans.
- As its equity-capital base the Bank should have a soft federal guarantee equal to about one-tenth of its total capitalization, which, if thoughtfully designed, will *not* need to be "scored" and thus added to the federal deficit.
- Using its authorization to make and guarantee loans, leverage private capital, and issue general-purpose bonds, the NIB should be allowed to fund a broad range of infrastructure projects beyond traditional roads, rails and runways.
- Governance should be by an independent, non-partisan board of (i) executives who are expert in infrastructure, (ii) labor leaders and (iii) public policy experts.
- Projects in the states and for the local governments whose pension plans participate in capitalizing the Bank should have preference over those of states and local governments which elect not to participate.
- Finally, the Bank should only fund projects which adhere to "buy domestic" (Made in America) requirements that are consistent with the United States' international trade agreements.

The Defense Production Act, which is up for reauthorization next year, might, if DOD's understandable concern about quick delivery of time-sensitive goods can be addressed, might serve as a meaningful complement to an all-of-government National Infrastructure Bank.

One further comment I must add is that maintaining mostly local, public control of our infrastructure is critical. Resuscitating America's infrastructure cannot become a mechanism for outsourcing control over some of our major rehabilitated roads and bridges and, especially, some of our vital seaports and airports to private investors, whether they're from Wall Street, Beijing or Abu Dhabi. Of particular concern, at least to me, is the proposal, yet again being advanced by former Treasury Secretary Bob Rubin, that China's big banks be given a major role in upgrading our important infrastructure.

Building Our Human Infrastructure

Abundant, pertinent skills are integral to the robustness of a nation's manufacturing sector, and skill setting must be part of any national manufacturing policy. Currently, far too many young Americans are growing up without the opportunity to obtain the skills and the interest at young enough ages to develop promising careers in manufacturing.

By the time students get out of middle school, if they've not developed sufficient science, technology, engineering and math skills – i.e., so-called "STEM" skills – it may well be too late for them in the increasingly highly automated world of advanced manufacturing. Yet we know that working with your hands at almost any level is a great way to establish living wage careers in the manufacturing sector.

Many countries use the promise of free education and training for local workforces – and apprenticeship programs[16] – to attract investors to move factories and associated jobs abroad. The U.S. can't sit idly by without further eroding our global competitiveness.

Expanding STEM education as well as career and technical education – and providing professional development and support for teachers and school leaders to promote high-quality instruction – is critical to restoring the human infrastructure of the U.S.[17] As we are hopefully winding down our involvement with foreign wars, we need to redouble our training efforts here at home as we did in the immediacy of the end of the Second World War.

Trade Enforcement

Any effort aimed at revitalizing manufacturing in America must include fundamental reform of our trading relationships. For example, our annual trade deficit in manufactured goods just with China costs us about $40 billion in lost wages.[18]

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[16] Nelson D. Schwartz, "Where Factory Apprenticeship Is Latest Model From Germany," *New York Times*, November 30, 2013.

[17] S. 1675, "Preparing Students for Success in the Global Economy Act," Senator Jeff Merkley et al.

[18] Economic Policy Institute, September 30, 2013.

Much has been written about how China has unfairly gained trade advantages through its abysmally low direct-labor costs, low-grade environmental and labor standards and currency manipulation. These same conditions are now drawing American manufacturing jobs to even less developed countries, like Vietnam and Bangladesh. As trade scholars such as Hastings trade law professor Joel Paul have argued for and policy leaders like Subcommittee Chairman Merkley have endorsed, it should be easy to include the cost of both adequate wages and sustainable production methods within the calculation of the cost of production in anti-dumping duties which should incentivize foreign companies to raise wages, workplace safety, and environmental compliance proactively.[19]

Less appreciated, however, are the variety and magnitude of the other measures China, for example, uses to game the system. Since some of these unfair practices are already being adopted by countries such as Brazil and Vietnam, getting right America's trade relationship with China is particularly critical. These so-called "trade advantages" include: China's regulations to block foreign firms from selling their products to government agencies; technical standards that prevent or hinder the government and local businesses from buying U.S. goods; and rules that force Western companies to give up technological secrets in exchange for market access.

Of the many possible responses to the persistent trade abuses that are happening in China and elsewhere, six that particularly stand out are as follows:

1. The administration's focus should not be, as it states, growing gross exports.[20] All that matters is our *net exports* position, which currently remains massively negative.[21]
2. The next required Semiannual Report on International Economic and Exchange Rate Policies from the Treasury Department must be objective and designate any country as a currency manipulator that meets the standard. Thereafter, the USG needs to go after *all* of that country's illegal subsidies.
3. The USG should not enter into new investment treaties with countries like China until those countries are fully WTO-compliant. For example, there are still serious questions about China's Indigenous Innovation Production

[19] Joel Paul, "Fair Wages for Free Trade," *Huffington Post*, October 10, 2012, http://www.huffingtonpost.com/joel-richard-paul/fair-wages-for-fair-trade_b_1944379.html.
[20] August 4, 2010 letter to President Barack Obama by Senators Sherrod Brown (D-Ohio), Olympia J. Snowe (R-Maine), Charles E. Schumer (D-N.Y.), Debbie Stabenow (D-Mich.), Jim Bunning (R-Ky.), Arlen Specter (D-Pa.), Susan M. Collins (R-Maine), Ron Wyden (D-Ore.), Benjamin L. Cardin (D-Md.), Robert P. Casey, Jr. (D-Pa.) and Carl Levin (D-Mich.).
[21] Leo Hindery, Jr., "U.S. – China: How Long China's Doormat?" Huffington Post, August 24, 2010.

Accreditation (IIPA) Program. In the interim, the USTR should bring a Section 301 case against the IIPA Program.[22]

4. The "one size fits all" premise behind the proposed Trans-Pacific Partnership FTA negotiations – which would include Brunei and New Zealand equally alongside China and Japan – is deeply flawed, both intellectually and economically, and should be revisited.
5. Congress needs to pass a bill similar to the Reciprocal Market Access Act of 2011 (H.R. 1749) and its Senate counterpart (S. 1766) which would eliminate the distinction that exists between traditional tariff barriers and the much-larger non-tariff barriers that prevent fair market access by American suppliers.[23]
6. Finally, "trade agreement enforcement" should be moved from the U.S. Trade Representative's office to a fully enabled and funded office in the Justice Department. At a minimum, the new Assistant Secretary of Commerce for Enforcement and Compliance should be named the head of the Interagency Trade Enforcement Committee and made independently accountable to Congress for the ITEC's trade enforcement agenda. A top-to-bottom review of the USG's trade enforcement capabilities, including budgetary, should be initiated.

Conclusion

Getting our manufacturing policy right means taking actions both here and abroad. We have to adopt a national manufacturing policy, build our physical and human infrastructure, close tax loopholes that drive manufacturing abroad, and fight for a level playing field in international trade. Although the Obama administration has made some progress, the United States is still tolerating far too many selfish, short-sighted behaviors that are hurting the middle class and its workers, creating a large and unsustainable trade imbalance in manufactured goods, and crippling our economic vitality and national security.

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[22] Leo Hindery, Jr., "China Trade: A 'Target Rich Environment,'" Huffington Post, March 20, 2012.

[23] Ibid.