

**Testimony of Daniel J. Ikenson
Associate Director, Center for Trade Policy Studies,
Cato Institute, Washington, DC**

before the

**Subcommittee on Commerce, Manufacturing, and Trade
Committee on Energy and Commerce
United States House of Representatives**

**Made in America: Increasing Jobs through Exports and Trade
March 16, 2011**

Summary of Testimony

Increasing the number of jobs in the economy by expanding trade—both exports and imports—is a good bet. Historically, there has been a strong relationship between economic growth, trade (both exports and imports, individually and combined), and job creation in the United States.

Despite the “Made in America” orientation of today’s hearing, it is important to note that trade in products that are made in America, or partially-made in America, or designed in America but produced abroad, or entirely designed and produced abroad from components manufactured abroad supports U.S. jobs up and down the supply chain through various channels. Both exports *and imports* support U.S. jobs.

But many Americans believe that exports are good, imports are bad, the trade account is the scoreboard, the trade deficit means the United States is losing at trade, and it is losing because our trade partners cheat. Many point to the trade deficit as the obvious explanation for the much exaggerated death of U.S. manufacturing. According to polling data, Americans are generally skeptical about trade and its impact on jobs, manufacturing, and the U.S. economy. And why shouldn’t they be? After all, the public is barraged routinely with misleading or simplistic coverage of trade issues by a media that is too often heavy on cliché, innuendo, and regurgitated conventional wisdom, and lacking in substance and analysis.

President Obama has already offered his answer to the question implicit in this hearing. His National Export Initiative aims to double U.S. exports in five years by reducing and eliminating various administrative, regulatory, and financial obstacles faced by U.S. exporters. Although the plan features some laudable components, it includes several errors of omission and commission that are likely to limit or undermine the NEI’s success.

Any serious plan to boost U.S. economic growth and hiring should start by identifying all policies, regulations, practices, and conditions that impede U.S. competitiveness, not just those obstacles that confront U.S. companies as exporters.

**Testimony of Daniel J. Ikenson
Associate Director, Center for Trade Policy Studies,
Cato Institute, Washington, DC**

before the

**Subcommittee on Commerce, Manufacturing, and Trade
Committee on Energy and Commerce
United States House of Representatives**

**Made in America: Increasing Jobs through Exports and Trade
March 16, 2011**

Good morning, Chairman Bono-Mack, Ranking Member Butterfield and members of the subcommittee. I am Daniel Ikenson, associate director of the Center for Trade Policy Studies at the Cato Institute. Today, I am very pleased to be able to share my views on the topic of manufacturing, trade, jobs, and other economic issues related to the subject of today's hearing. The views I express are my own and should not be construed as representing any official positions of the Cato Institute.

Introduction

Increasing the number of jobs in the economy by expanding trade—both exports and imports—is a good bet. Historically, there has been a strong relationship between economic growth, trade (both exports and imports, individually and combined), and job creation in the United States. In the quarter century between 1983 and 2007, as real GDP more than doubled and the real value of U.S. trade increased five-fold, the U.S. economy created 46 million net new jobs, or 1.84 million net new jobs per year.¹ In 22 of those 25 years, the annual changes in GDP, trade, and job creation all moved in the same direction—either all positive or all negative. And as economic growth came to a halt and then turned negative in 2008 and 2009, respectively, trade contracted by 12 percent and the economy shed over six million jobs.

Despite the “Made in America” orientation of today's hearing, it is important to note that trade in products that are made in America, or partially-made in America, or designed in America but produced abroad, or entirely designed and produced abroad from components manufactured abroad supports U.S. jobs up and down the supply chain through various channels. Both exports *and imports* support U.S. jobs.

But many Americans believe that exports are good, imports are bad, the trade account is the scoreboard, the trade deficit means the United States is losing at trade, and it is losing because our trade partners cheat. Many point to the trade deficit as the obvious explanation for the much exaggerated death of U.S. manufacturing. According to polling data, Americans are generally skeptical about trade and its impact on jobs, manufacturing, and the U.S. economy. And why

¹ 2011 Economic Report of the President.

shouldn't they be? After all, the public is barraged routinely with misleading or simplistic coverage of trade issues by a media that is too often heavy on cliché, innuendo, and regurgitated conventional wisdom, and lacking in substance and analysis.

President Obama has already offered his answer to the question implicit in this hearing. His National Export Initiative aims to double U.S. exports in five years by reducing and eliminating various administrative, regulatory, and financial obstacles faced by U.S. exporters. Although the plan features some laudable components, it includes several errors of omission and commission that are likely to limit or undermine the NEI's success.

In the pages to follow, this testimony will address and attempt to correct lingering misperceptions about trade and manufacturing, describe some of the shortcomings of the NEI, and offer some alternatives for increasing economic growth and creating jobs through trade.

The Myth of Manufacturing Decline

Americans often hear that some nefarious foreign trade practices are to blame for the decline of U.S. manufacturing. But the problem with that presumption of causation is that U.S. manufacturing is not in decline in the first place. Until the onset of the recent recession (when virtually every sector in the economy contracted), U.S. manufacturing was setting new performance records almost year after year in nearly all relevant statistical categories: profits, revenues, investment returns, output, value added, exports, imports, and others. After contracting during the recession of 2008 and 2009, the manufacturing sector has come roaring back. According to the Institute for Supply Management, economic activity expanded in the manufacturing sector for the 19th consecutive month in February 2011, reaching its highest level since May 2004.²

In absolute terms, the value of U.S. manufacturing has been growing continuously, with brief hiccups experienced during recessions over the past several decades. As a percentage of our total economy, the value of manufacturing peaked in 1953 and has been declining since, but that is the product of rapid growth in the services sectors and not—as evidenced by manufacturing's absolute growth—an indication of manufacturing decline.³

The preponderance of Chinese and other imported goods on retail store shelves may give the impression that America does not make anything anymore—a fallacy sensationally exploited by ABC News in its recent series, “Made in America.” But U.S. factories make lots of things—in particular, high-value products that are less likely to be found in retail stores—like airplanes,

² Institute for Supply Management, February 2011 Manufacturing ISM *Report On Business*, <http://www.ism.ws/ismreport/mfgrob.cfm>.

³ For more comprehensive treatments refuting the myth of manufacturing decline in the United States, see Daniel Ikenson, “Thriving in a Global Economy: The Truth about Manufacturing and Trade,” Cato Institute Trade Policy Analysis no. 35, August 28, 2007; Daniel Ikenson and Scott Lincicome, “Audaciously Hopeful: How President Obama Can Help Restore the Pro-Trade Consensus,” Cato Institute Trade Policy Analysis no. 39, April 28, 2009, pp. 12–16; and Daniel Griswold, “Trading Up: How Expanding Trade Has Delivered Better Jobs and Higher Living Standards for American Workers,” Cato Institute Trade Policy Analysis no. 36, October 25, 2007.

advanced medical devices, sophisticated machinery, chemicals, pharmaceuticals, and biotechnology products. American manufacturers are no longer heavily in the business of making sporting goods, tools, clothing, footwear, housewares, and furniture, but their factories are still the world's most prolific, accounting for 21.4 percent of global manufacturing value-added in 2008, while China accounted for 13.4 percent.⁴

America has maintained its industrial preeminence by transitioning away from high-volume, low-value industries into higher value-added production. In the process, the number of jobs in the manufacturing sector—perhaps the most important metric from a political standpoint—has declined. U.S. manufacturing employment reached its peak of 19.4 million jobs in 1979—**fourteen years before the implementation of the North American Free Trade Agreements and 22 years before China joined the World Trade Organization.** So the downward trend in manufacturing employment, along roughly the same trajectory for 30 years, began long before the common scapegoats for manufacturing job loss even existed.

Manufacturing job loss has very little to do with trade and a lot to do with changes in technology that lead to productivity gains and changes in consumer tastes. China has also experienced a decline in manufacturing jobs—in fact, many more jobs have been lost in China's manufacturing sector—for the same reasons. According to a 2004 study published by the Conference Board, China lost 15 million manufacturing jobs between 1995 and 2002, a period during which 2 million U.S. manufacturing jobs were lost.⁵

The fact of the matter is that, with the exception of cyclical contractions during noted economic recessions, the U.S. manufacturing has been thriving in the global economy. Whether U.S. manufacturing will continue to thrive and even become a reliable job creator in the years ahead depends to some extent on the public policies adopted and eschewed.

No Longer “Us” vs. “Them”

During the past few decades, a truly global division of labor has emerged, presenting opportunities for specialization, collaboration, and exchange on scales once unimaginable. The confluence of falling trade and investment barriers, revolutions in communications and transportation, the opening of China to the West, the collapse of communism, and the disintegration of Cold War political barriers has spawned a highly integrated global economy with vast potential to produce greater wealth and higher living standards.

The dramatic reduction in transportation and communication costs combined with widespread liberalization of trade, finance, and political barriers are all accomplices in what has been called “the death of distance.” Under the new paradigm, the factory floor is no longer contained within four walls and one roof. Instead, the factory floor spans the globe through a continuum of

⁴ United Nations Industrial Development Organization, “National Accounts Main Aggregates Database, Value Added by Economic Activity,” <http://unstats.un.org/unsd/snaama/resQuery.asp>.

⁵ Yuan Jiang et al., “China's Experience with Productivity and Jobs,” Conference Board Report Number R-1352-04-RR, June 2004.

production and supply chains, allowing lead firms to optimize investment and output decisions by matching production, assembly, and other functions to the locations best suited for those activities.

In the 21st century, it is inaccurate to characterize international trade as a competition between “us” and “them.” Because of foreign direct investment, joint ventures, and other equity-sharing arrangements, quite often “we” are “they” and “they” are “we.” Even the U.S. automobile and steel industries attest to this new reality. And as a result of the proliferation of disaggregated, transnational production and supply chains, “we” and “they” often collaborate in the same endeavor. Under the new paradigm, workers in developed and emerging countries are more likely to be coworkers than competitors. Today’s global economic competition is less likely to feature “our” producers against “their” producers and more likely to feature entities that defy national identification because they are truly international in their operations, creating products and services from value-added activities in multiple countries. There is competition between supply chains, but success first demands cooperation and collaboration within supply chains (i.e., cooperation and collaboration between some of “us” and some of “them”). This new commercial reality demands policies that are welcoming of imports and foreign investment, and that minimize regulations or administrative frictions that are based on misconceptions about some vague or ill-defined “national interest.”

A recent analysis from the Asian Development Bank Institute of the complex production-supply chain surrounding production of Apple’s iPhone is both testament to the benefits of globalization and the latest indictment of a decrepit international trade flow accounting system that nourishes misleading trade skeptics and misinforms policy.

Following in the footsteps of a groundbreaking and widely-cited 2007 University of California-Irvine study, which disaggregated the components of a Chinese-assembled Apple iPod and assigned its constituent value to the companies and countries responsible for their production, two researchers at the Asian Development Bank Institute applied a similar analysis to the Apple iPhone. Like the UC-Irvine iPod study before it, the ADBI analysis found that just a tiny fraction of the cost of producing the iPhone is Chinese value-added. The only Chinese input is labor, which is used to assemble the components manufactured in other countries. The value of that labor accounts for \$6.50 or 3.6 percent of the total cost of \$178.96 to produce an iPhone (about the same percentage as the iPod). The other 96.4 percent of that total is the cost of components produced (and the labor and overhead employed to produce those components) in Japan, Germany, South Korea, the United States, and several other countries. This breakdown is very similar to that found for the iPod in 2007, and the punch lines are identical.

While firms in Japan and Germany account for the most expensive parts (and quite obviously benefit from the advent of the iPhone), most of the value of the iPhone (like the iPod) accrues to Apple, which reaps the lion’s share of the approximately 100 percent markup. When iPhones sell for \$399 in the United States, the difference between that retail price and the \$178.96 cost of production goes to retailers, distributors, marketers, other firms in the supply chain, and to Apple, which distributes some earnings to its shareholders and retains some for research and development, supporting engineering and design jobs higher up the value chain so that the virtuous circle can continue.

Rather than appreciate how this complementary process harnesses the benefits of our globalized division of labor, some begrudge iPod and iPhone sales in the United States for adding to the bilateral trade deficit. Technically, for every \$399 iPhone sold in the United States, the U.S. bilateral trade deficit with China increases by \$178.96 (its full cost of production). Even though only \$6.50 of that iPhone is Chinese value, under our antiquated, pre-globalization, method of tallying a nation's imports and exports, the entire \$178.96 is chalked up as an import from China because that was the product's final point of assembly. According to the authors of the ADBI study, iPhones added \$1.9 billion to the politically volatile U.S. trade deficit with China in 2009. Alas, this is the basis of the claim—popular among the most shameless trade critics—that America has a "high-tech" trade deficit with China.

Should we lament a trade deficit in iPhones or any other products assembled abroad, particularly when those products comprise U.S. value-added and support high-paying U.S. jobs?

U.S. factories and workers are more likely to be collaborating with Chinese factories and workers in production of the same goods than they are to be competing directly. The proliferation of vertical integration (whereby the production process is carved up and each function performed where it is most efficient to perform that function) and transnational supply chains has joined higher value-added U.S. manufacturing, design, and R&D activities with lower-value manufacturing and assembly operations in China. Though the focus is typically on American workers who are displaced by competition from China, legions of American workers and their factories, offices, and laboratories would be idled without access to complementary Chinese workers in Chinese factories. Without access to lower-cost labor in places like Shenzhen, countless ideas hatched in U.S. laboratories—which became viable commercial products that support hundreds of thousands of jobs in engineering, design, marketing, logistics, retailing, finance, accounting, and manufacturing—might never have made it beyond conception because the costs of production would have been deemed prohibitive for mass consumption. Just imagine if all of the components in the Apple iPhone had to be manufactured and assembled in the United States. Instead of \$178.96 per unit, the cost of production might be multiple times that amount, and quite possibly prohibitive.

Consider how many fewer iPhones Apple would have sold; how many fewer jobs iPhone production, distribution, and sales would have supported; how many fewer young programmers would be employed designing "apps"; how much lower Apple's profits (and those of the entities in its supply chains) would have been; how much lower Apple's research and development expenditures would have been; how much smaller the markets for music and video downloads, car accessories, jogging accessories, and docking stations would be; how many fewer jobs those industries would support; and the lower profits those industries would generate. Now multiply that process by the hundreds of other similarly ubiquitous devices and gadgets: computers, handheld video game players, Blu-Ray devices, and every other product that is designed in the United States and assembled in China from components made in the United States and elsewhere.

It is beyond question that countless U.S. jobs depend on imports from China.

The Atlantic's James Fallows characterizes the complementarity of U.S. and Chinese production sharing as following the shape of a "Smiley Curve" plotted on a chart where the production process from start to finish is measured along the horizontal axis and the value of each stage of production is measured on the vertical axis. U.S. value-added comes at the early stages—in branding, product conception, engineering, and design. Chinese value-added operations occupy the middle stages—some engineering, some manufacturing and assembly, primarily. And more U.S. value-added occurs at the end stages in logistics, retailing, and after-market servicing. Under this typical production arrangement, collaboration, not competition, is what links U.S. and Chinese workers.

Over the past couple of centuries, economists have spoken of comparative advantage in the context of industries. In David Ricardo's telling, Portugal had a comparative advantage in wine-making and England had a comparative advantage in cloth-making. So each country would focus its productive efforts where they were most efficient, and exchange surpluses, to attain the highest level of output and consumption. Today comparative advantage can apply to functions in the supply chain. China may have a comparative advantage in electronic assembly operations vis-à-vis the United States today, the United States may have a comparative advantage in product design vis-à-vis Japan, and Japan may have a comparative advantage in component production. Instead of trading wine for cloth, the modern set-up implies a collaboration between U.S. engineers, Japanese manufacturers, and Chinese assemblers—that is, collaboration in the production of Apple iPods and similar products. But as a country's skill sets change—partly as a function of its policies—the people will become relatively more efficient in some endeavors and relatively less efficient in others.

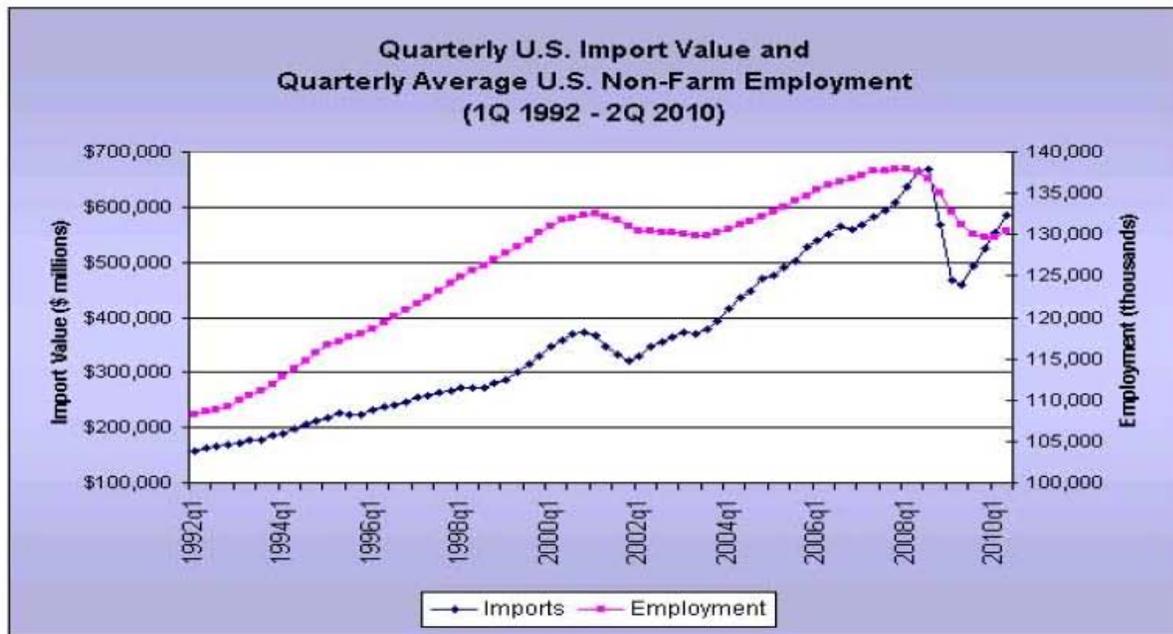
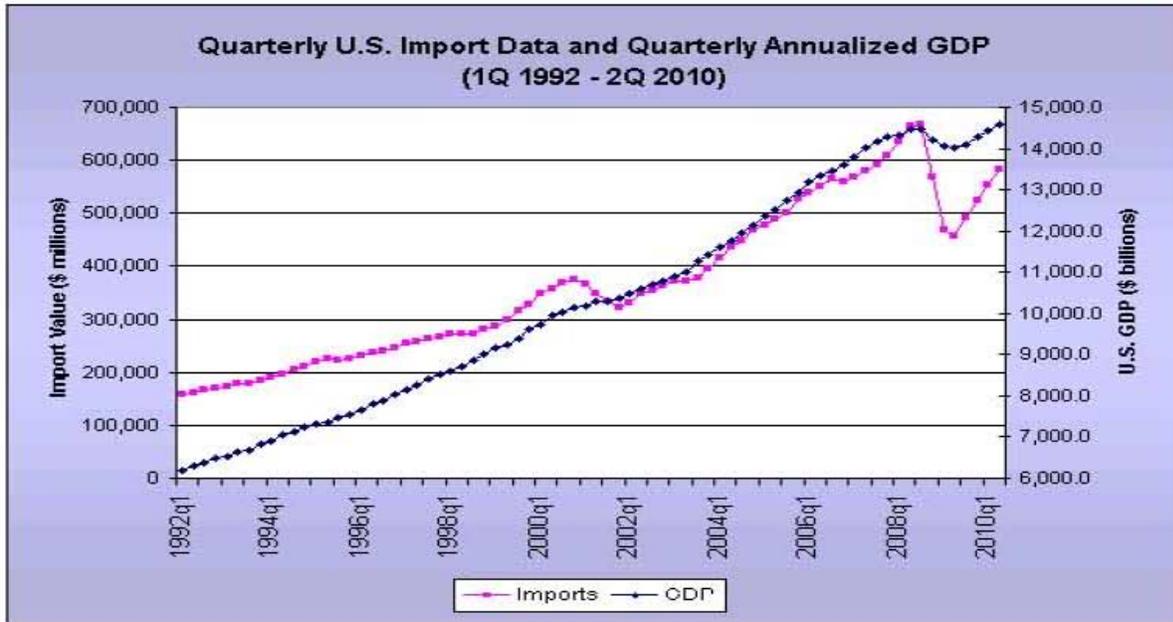
That countries are not destined to remain in their current supply chain rungs, but can ascend or descend the value-chain, as the case may be, should be motivation enough for governments, both rich and poor, and at all stages of development, to adopt the policies that are most likely to provide the greatest and highest valued-added opportunities for their people.

Imports Get an Undeservedly Bad Rap

People generally understand that exports contribute to economic growth, which is essential to job creation. But many then make the mistake of reasoning: if exports help grow the economy and create jobs, then imports must shrink the economy and cost jobs. That is the central misconception perpetrated by media every month when the Census Bureau releases the monthly trade figures. Emblematic of this kind of bad reporting is last week's story by AP Economics Writer Martin Crutsinger, who wrote: "A widening trade deficit hurts the U.S. economy. When imports outpace exports, more jobs go to foreign workers than to U.S. workers." Well, that outcome is possible, but as an ironclad law, it is an indefensible statement.

The description of global production and supply chains above is a fairly strong argument for the benefits of imports and strong evidence that imports support U.S. jobs. But imports support U.S. employment through many other channels, as well. According to the Bureau of Economic Analysis, "intermediate goods" and "capital equipment"—items purchased by producers, not consumers—accounted for more than 55 percent of the value of all U.S. imports last year. So, imports that are too often assumed to be consumer goods that come at the expense of domestic

production are more often than not used as inputs for domestic production. Better and more affordable access to those imports helps reduce the costs of production, enabling producers to better compete and support U.S. jobs and wages. The 45 percent of imports that are consumer goods support U.S. jobs in logistics, transportation, wholesaling, retailing, and after-market service industries. The nearby charts show how imports move in tandem with GDP and employment.

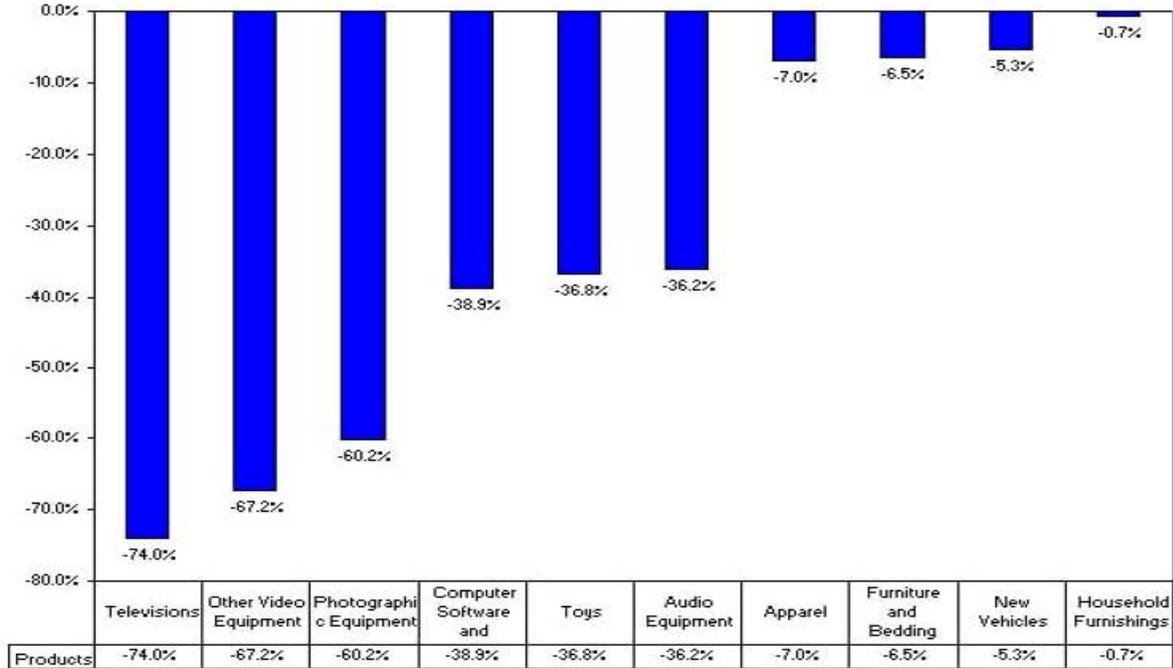


And by helping to keep prices lower and quality higher, imports allow consumers to have more resources with which to purchase other products and services or to save, both of which support

more U.S. jobs. The next set of charts compares price changes over time of products that tend to be heavily traded and products and services that are generally not traded.

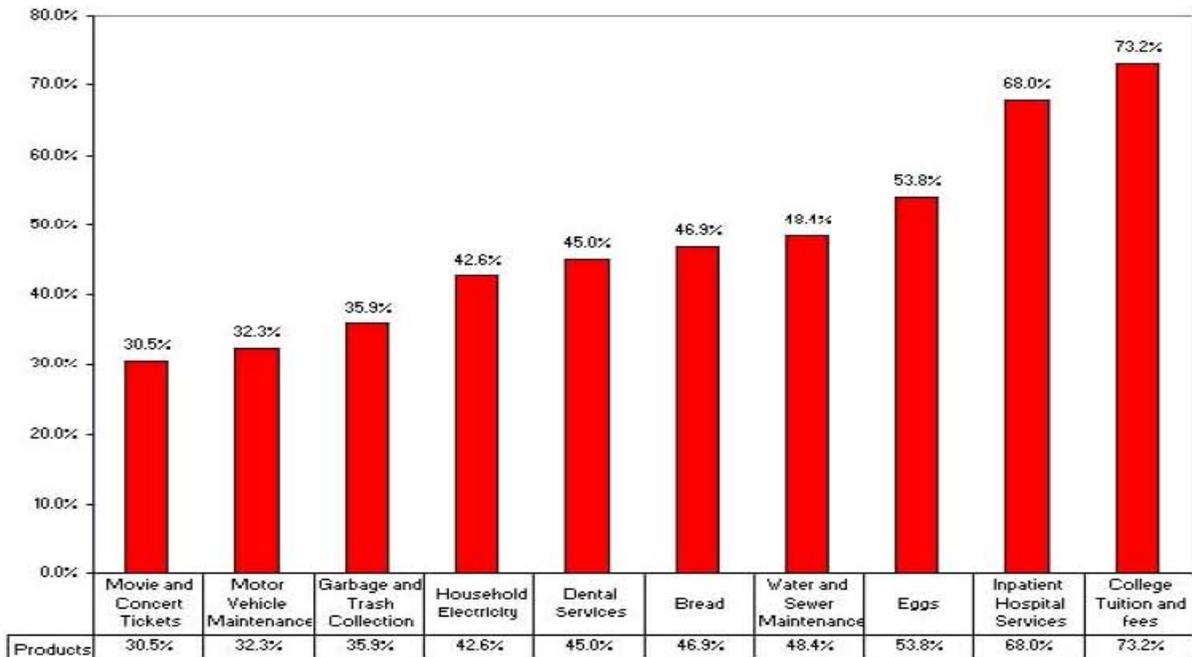
**Price Changes of Highly-Traded Products (CPI-U)
2000-2009**

Source: U.S. Bureau of Labor Statistics



**Price Changes of Products and Services Less Likely to be Imported (CPI-U)
2000-2009**

Source: U.S. Bureau of Labor Statistics



Moreover, when U.S. consumers and producers purchase imports, foreigners obtain dollars with which they can support U.S. jobs through their own purchase of U.S. exports or through investment in U.S. businesses.

Some of the misunderstanding can be traced to the famous National Income Identity, which expresses gross domestic product, as: $Y = C + G + I + (X-M)$. That is, national output (Y) equals personal consumption (C) plus government spending (G) plus investment (I) plus exports (X) minus imports (M).

The expression clearly lends itself to the wrong interpretation. The minus sign preceding imports suggests a negative relationship with output. It is the reason for the oft-repeated fallacy that imports are a drag on growth. But that is the wrong conclusion.

The expression is an accounting identity, which "accounts" for all of the possible channels for disposing of our national output. That output is either consumed in the private sector (C), consumed by government (G), invested by business (I), or exported (X). The identity requires subtraction of aggregate imports because consumption, government spending, business investment, and exports all contain, in various amounts, import value. Americans consume domestic and imported products and services, the aggregate of which shows up in consumption. Likewise, government purchases include domestic and imported products and services; businesses invest in domestic and imported machines and inventory; and, exports often contain some imported intermediate components. Thus, the identity would overstate national output if it didn't make that adjustment for imports. After all, imports are not made on U.S. soil with U.S. factors of production, so they shouldn't be included in an expression of our national output.

To reiterate, it is a simple matter of accounting: as an expression of national output, the National Income Identity subtracts imports only because imports are that portion of consumption, government spending, investment, and exports that are not produced on U.S. soil with U.S. factors of production. If we did not subtract an aggregate import value, then national output would be overstated.

But this is unnecessarily confusing. Why has it not been commonplace to use notation that conveys in no uncertain terms that C and G and I and X include some amount of imports? Maybe something like this:

$$Y=C(d)+C(m)+G(d)+G(m)+I(d)+I(m)+X(d)+X(m)-M,$$

where (d) connotes domestic; (m) connotes imported; and $M=C(m)+G(m)+I(m)+X(m)$.

Again, imports are subtracted, not because they are a drag on output, but because imports are included in the other constituent elements of the identity. I've always found it misleading that the parentheses go around X-M – which isolates the expression "net exports," but in the process can obscure the fact that imports are subtracted from the whole expression.

The National Export Initiative

In his February 2010 State of the Union address President Obama announced a goal of doubling U.S. exports in five years. That goal was soon enshrined as the “National Export Initiative,” which has since become the centerpiece of the administration’s trade policy agenda.

Some of the components of the NEI are eminently sensible as standalone policies. For example, efforts to clarify, simplify, and streamline U.S. export control procedures—should they succeed—are likely to reduce regulatory obstacles and spur meaningful export growth without imposing new burdens or diverting resources from elsewhere in the economy. Likewise, passage of the long-pending bilateral trade agreements with South Korea, Colombia, and Panama, and conclusion of the decade-long Doha Round of multilateral trade negotiations and the ongoing Trans-Pacific Partnership negotiations would reduce or eliminate barriers to U.S. exports in a variety of sectors. And, it would not be unreasonable to expect that the resulting increase in trade would lead to job growth—despite the anomaly of 2010 (i.e., positive economic growth, strong trade growth, but negative job growth).

But other aspects of the National Export Initiative—call them errors of omission and commission—are more troubling. The NEI presumes that the only obstacles confronting U.S. exporters are those that exclusively concern their activities as exporters. But, in fact, before they are exporters these companies are producers, and as producers they have production costs that are often inflated by dint of policy—import duties, a weak dollar, regulatory compliance costs. The NEI is silent on these significant obstacles to U.S. competitiveness at home and abroad.

According to the Bureau of Economic Analysis, “intermediate goods” and “capital equipment”—items purchased by producers, not consumers—accounted for more than 55 percent of the value of all U.S. imports last year. That fact alone makes clear that imports are crucial determinants of the profitability of U.S. producers and their capacity to compete at home and abroad. Yet the NEI commits not a word to the task of eliminating or reducing the burdens of government policies that inflate import prices and production costs.

During the decade between 2000 and 2009, the United States imposed 164 antidumping measures on a variety of products from dozens of countries. A total of 131 of those 164 measures restricted (and in most cases, still restrict) imports of intermediate goods and raw materials used by downstream U.S. producers in the production of their final products. The cases were filed and the duties imposed without any of these downstream companies having had the opportunity to make their case before the International Trade Commission that the duties would adversely affect them. Under the present antidumping statute, the administering authorities are forbidden from considering the impact on consuming industries—or the impact on the economy more broadly—when deciding whether or not to levy the duties. That is a major oversight that should have been identified as an obstacle to U.S. export competitiveness by the administration in its development of the NEI.

In January, a *Wall Street Journal* editorial featured the story of what was recently a profitable and expanding magnesium die-cast auto parts industry in the United States. The U.S. and foreign markets for these engine parts (which are lighter but stronger than the more common aluminum parts, so in high demand from auto producers looking to improve fuel efficiency) were growing. But then the sole U.S. producer of magnesium—a monopolist in Utah—brought an

antidumping case against imports from China and Russia. The resulting duties drove the cost of magnesium in the United States well above the world price, and slowly but surely, the U.S. firms started to die off.⁶ That an industry comprised of a single producer with 370 employees can snuff out downstream industries—particularly up-and-coming industries—is costly economic policy that the NEI should be addressing.

Another concern about the NEI is that it may tempt the administration further down the slippery slope of industrial policy. Although doubling exports to \$3.14 trillion by the end of 2014 would be a laudable achievement, enshrining that goal as a national imperative presents risks. “Five-Year Plans” have a way of breeding zealous devotion to goals for the sake of goals, sometimes at the expense of the process that would otherwise lay the foundation for greater and enduring success. By exhorting U.S. exporters to “win the future” and describing the imperative of “making sure we’re not ceding markets, exports, and the jobs they support to other nations,” the president is reinforcing an image of trade as an adversarial, zero-sum endeavor.

With over \$100 billion in direct subsidies and tax credits already devoted to green technology, it is no secret that President Obama has been promoting investment in solar panel, wind harnessing, lithium ion battery, and other industries he deems crucial. Concerning those industries, the president said: “Countries like China are moving even faster...I’m not going to settle for a situation where the United States comes in second place or third place or fourth place in what will be the most important economic engine of the future.”

With all due respect, how does the president know that those will be the most important economic engines of the future? By placing bets on particular industries, the administration is overriding a selective, evolutionary process that has undergirded the world’s most successful innovation machine, while reducing the chances of worthy ideas, firms, and industries leading the next commercial wave. Did President Obama’s predecessors anticipate the arrival of Steve Jobs, Bill Gates, or Marc Zuckerberg and the revolutionary products and services they delivered? Did Washington bureaucrats foresee the advent of specific life-extending medicines and devices, like digestible, pill-sized cameras? Had those proposing industrial policy in response to a rising Japan in the 1980s and early 1990s prevailed, much of the technology and medical advances taken for granted today never would have come to fruition.

Despite the risks and uncertainty of industrial policy, the administration seems to be getting a lot of encouragement in that direction from a wide swath of captains of industry, economics writers, and media pundits.

Policy Solutions

A serious plan to boost U.S. economic growth and hiring should start by identifying all policies, regulations, practices, and conditions that impede U.S. competitiveness, not just those obstacles that confront U.S. companies as exporters.

⁶ For more in-depth coverage of this story, see <http://www.cato-at-liberty.org/death-by-antidumping/>

Although trade's critics speak of a "race to the bottom," where governments compete for investment by lowering their standards—a concern unsupported by trade and investment flows—it is really more appropriate to speak of a race to the top. Governments are competing for business investment and talent, which both tend to flow to jurisdictions where the rule of law is clear and abided; where there is greater certainty to the business and political climate; where the specter of asset expropriation is negligible; where physical and administrative infrastructure is in good shape; where the local work force is productive; where there are limited physical, political, and administrative frictions; and so on. Those once-clear American advantages have atrophied.

This global competition in policy is a positive development, but we are kidding ourselves if we think that we don't have to compete and earn our share with good policies. The decisions we make now with respect to policies on immigration, education, energy, trade, entitlements, taxes, and the role of government in managing the economy will determine the number and kinds of jobs created, as well as the health, competitiveness, and relative significance of the U.S. economy in the decades ahead.

According to a survey of 13,000 business executives worldwide, conducted by the World Economic Forum, 52 countries have less burdensome regulations than the United States. Add to the fact that the United States has the highest corporate tax rate among all OECD countries, the sense that the rule of law is no longer bedrock, the business and political climates remain uncertain, asset expropriation (through torts, bankruptcy, antitrust and other mechanisms) is a real threat, the workforce doesn't have the skills required by producers in an economy at the technological fore, the regulatory environment is stifling, compliance costs are eating into the bottom lines of more and more companies, the government treats our innovators as adversaries, physical infrastructure is in disrepair, and it becomes less mysterious why U.S. businesses aren't investing and hiring in droves. Meanwhile, forward-looking governments around the world are wooing investment in R&D facilities, high-end manufacturing plants, and educated human beings with proper incentives, as U.S. policies treat those investors and skilled immigrants with contempt or indifference.

President Obama visited recently with the Chamber of Commerce and argued that he had made concessions to business by moving toward the center on tax and trade policy, and that now was the time for business to reciprocate by investing and hiring. But the president's small steps toward the center come after two years of sprinting to the left on economic policy. After ObamaCare, Dodd-Frank, taxpayer bailouts, unorthodox and legally-questionable bankruptcy procedures, subsidies for select industries, Buy American and other regulations governing how and with whom "stimulus" dollars could be spent, and the administration's tightening embrace of industrial policy, businesses want a more quiet, less intrusive, less antagonistic, predictable policy environment before they will feel comfortable investing and hiring.

In the meantime, a policy that would likely produce quick dividends would be one that reduces the administrative costs of importing. After all, most U.S. exporters—before they are exporters—are producers. And as producers they consume raw materials and other industrial inputs and components. Many of those inputs are imported or their costs are affected by the availability and prices of imports.

The president understands this. On August 11, 2010 at a White House signing ceremony, he offered the following rationale for a bill he was about to sign into law:

The Manufacturing Enhancement Act of 2010 will create jobs, help American companies compete, and strengthen manufacturing as a key driver of our economic recovery. And here's how it works. To make their products, manufacturers – some of whom are represented here today – often have to import certain materials from other countries and pay tariffs on those materials. This legislation will reduce or eliminate some of those tariffs, which will significantly lower costs for American companies across the manufacturing landscape – from cars to chemicals; medical devices to sporting goods. And that will boost output, support good jobs here at home, and lower prices for American consumers.⁷

It's tough to argue with that rationale. After all, “intermediate goods” and “capital equipment” accounted for 55 percent of U.S. import value last year, which amounted to over \$1 trillion in costs. U.S. tariffs and other import barriers increase the costs of production for U.S. companies, putting them at a disadvantage vis-à-vis foreign firms in the U.S. market and abroad.

But America's competitors aren't sitting still. Over the past two years, the Canadian and Mexican governments unilaterally slashed tariffs on a host of industrial inputs to reduce production cost and boost the competitiveness of their producers. Small and mid-sized businesses were reported to be enthusiastic about the tariff cuts, which will cut costs and paperwork. By 2015, the only goods subject to import duties in Canada will be supply-managed goods in the agricultural sector and some consumer products.

And in Mexico, in an effort to “reduce business operating costs, attract and retain foreign investment, raise business productivity, and provide consumers a greater variety and better quality of goods and services at competitive prices,” the Mexican government initiated a plan in 2007 to unilaterally reduce tariffs on 70 percent of the items on its tariff schedule. Those 8,000 items, comprising 20 different industrial sectors, accounted for about half of all Mexican import value in 2007. When the final phase of the plan is implemented on January 1, 2013, the average industrial tariff rate in Mexico will have fallen from 10.4 percent to 4.3 percent.

Among the major differences between the U.S. tariff liberalization and those in Canada and Mexico is that the U.S. action is temporary and only applicable to industrial inputs if there is no producer interest that objects. Our bolder North American neighbors have instituted permanent liberalization across the spectrum so as to afford their producers lower costs and an operational environment of greater business certainty.

On tariffs and other reforms that could encourage business investment and hiring, U.S. policymakers have a lot to learn from the actions of our trade partners.

⁷ President Barack Obama, The White House, Office of the Press Secretary, “Remarks by the President at the Signing of the Manufacturing Enhancement Act of 2010,” August 11, 2010.