"WILL WE HAVE AN ECONOMIC RECOVERY WITHOUT A STRONG U.S. MANUFACTURING BASE?"

HEARING

BEFORE THE

COMMITTEE ON SMALL BUSINESS
HOUSE OF REPRESENTATIVES

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HEARING ON "WILL WE HAVE AN ECONOMIC RECOVERY WITHOUT A STRONG U.S. MANUFACTURING BASE?"

WEDNESDAY, APRIL 9, 2003

HOUSE OF REPRESENTATIVES,
COMMITTEE ON SMALL BUSINESS
Washington, D.C.

The committee met, pursuant to call, at 2:08 p.m. in Room 2360, Rayburn House Office Building, Hon. Donald Manzullo presiding.

Present: Representatives Velazquez, Graves, Gerlach, Chocola, King, Udall, Ballance, Christian-Christensen, Napolitano, Acevedo-Vila, Majette, Marshall

Chairman MANZULLO. Good afternoon and welcome to this hearing of the Committee on Small Business. We have been advised that at 2:30 there is going to be a series of three votes, which will give us about a half an hour of exciting time on the floor, and you guys will not have anything to do here for a while. Obviously, we will try to get in as much testimony as possible before then.

I especially welcome those who have come some distance to participate. Today, we are going to talk about manufacturing. Most Americans do not fully realize the importance of manufacturing in America. The message I want to get across today is that manufacturing matters to everyone in a big, big way.

Let me be blunt about why we are having this hearing and why we will have a series of hearings to follow. Our domestic manufacturing base is being hollowed out right before our own eyes, and it is other American companies that are doing it. We are fast becoming a nation of assemblers, and even that may disappear soon. Most Americans, including many in Congress, brush off manufacturing as being passé.

It is happening also in the service sector. The February 3rd edition of Business Week had on it this cover: "Is Your Job Next? A new round of globalization is sending upscale jobs offshore. They include chip design, engineering, basic research, even financial analysis. Can America lose these jobs and still prosper?" That is Business Week.

At the rate we are going, 3.3 million jobs will move overseas by 2015. The title in today's Washington Times editorial says: "More Troubling Jobless News." We have lost over 1.4 million, mostly manufacturing, jobs just since September 11th. Even the service industry is short 200,000 jobs since 9/11. It is time to wake up. If we keep losing our manufacturing jobs, we will not have much of a service sector to worry about. Once our manufacturing base disappears, so do other economic sectors.

Engineers, your typical high-paid, white-collar jobs, are moving overseas. Boeing laid off 5,000 engineers in favor of lower-cost, Russian engineers, and you wonder what is going to be the next shoe to drop in the loss of our engineers in this country. GM and Ford are forcing their suppliers to move overseas to keep contracts. Those businesses will be hiring their engineers from overseas. Guess what? Many engineering jobs exist because of manufacturing.

Here are some facts, and they are not good. Two-thirds of reemployed manufacturing workers earn an average of 12 percent less in their new job. One-quarter earn less than 30 percent or more. Foreclosures hit a record high last quarter in places hardest hit by the manufacturing downturn, especially the Midwest and the Southeast, in part because the manufacturing sector has lost more jobs during the last economic downturn than any other sector. On March 31, Fortune reported that 10 percent of all U.S. spending is consumed on cars and related services. How many cars and other related services can two million unemployed people buy?

These are just two examples of how our economy is integrated and rests on the health of the manufacturing sector. From July 2000 through March of 2003, we have lost over 2.2 million manufacturing jobs, or nearly 12 percent. Manufacturing employment has now contracted for 32 straight months.

On April 1, 2003, the purchase manager's index, PMI, was set at 46.2 percent, its lowest reading since November of 2001. Analysts had predicted the index would fall to 49. Any number below 50 suggests that manufacturing is failing to grow. Orders to U.S. factories fell 1.5 percent in February, the worst showing in five months. According to an April 2nd Census report on manufacturer shipments for February, new orders declined 4.9 billion, shipments were down 5 billion, and unfilled orders decreased 1.1 billion, down for six consecutive months. On top of that, GM and Ford announced double-digit cutbacks in production. That means less work and even more layoffs for those supporting the auto industry. The tool-and-die industry is heavily dependent on new product introduction with the automotive industry absorbing nearly 50 percent of the tooling.

One of the issues driving this train is the tremendous pressure Wall Street puts on corporate America. I think if we look behind the layers, we will find companies forced to drive up stock values to make their quarterly estimates doing whatever they have to do to drive down the costs and increase margins. Do not get me wrong. That is the essence of capitalism. The problem is that this is short-term planning. It is tunnel vision, and these decisions made in a vacuum have a monstrous effect on everyday America.

The second problem we face is having no statistics on how much domestic content is actually in support of U.S. manufacturing goods, and no one is being held accountable for it. Today, "manufactured" does not necessarily mean made in the USA. All it has to be is assembled here, and that is what is becoming of our industrial base, with the exception of bonded goods going to Mexico through NAFTA and NAFTA content in automobiles. We just do not know how much of a product exported from the United States represents foreign material.

Our office has put together a presentation that outlines 10 major factors working against small manufacturers, who are the core of our industrial base. You will see they are fighting against high regulatory and tax burdens, overvaluation of the dollar, and low-cost labor, among others. For example, Chinese hourly compensation costs for tool makers and tool designers are 1⁄12 of those in the U.S., and those in Taiwan are 1⁄3. Sixty percent of this nation's 43 million uninsured are small business owners, their employees, and families.

The district that I represent, Rockford, Illinois, is home to the heaviest per capita concentration of machine tool-and-die companies in the nation. The Washington Post calls Rockford "a barometer in the heartland." That was the headline of a three-page story in the Post, March 25, 2001 edition. The subheadline says: "Rockford Holds Clues to Shifts in the U.S. Economic Climate."

Rockford was a national predictor in the early 1980s when its unemployment led the nation, at 24.9 percent. It remains a predictor today, still with one of the highest unemployment rates in the nation, at 10.9 percent. In February of this year, the national average is 5.8 percent. Overall, our district is experiencing the highest unemployment since the recession of 1992 and 1993. Since February of 2000, Rockford area factories have shed 9,400 manufacturing jobs, nearly 19 percent of the manufacturing workforce.

This is not just a problem facing Rockford-based manufacturers. The problems of Rockford, Illinois, are representative of the crisis in manufacturing across the nation, and it is something that we must fix.

[Mr. Manzullo's statement may be found in the appendix.]

Chairman MANZULLO. I look forward to the opening statement of my colleague, Ms. Velazquez.

Ms. VELAZQUEZ. Thank you, Mr. Chairman. Today, our nation continues to struggle. The economy is losing jobs faster than it can create them, which is bad news for the 8.4 million unemployed Americans, many of whom have been out of work for more than six months.

The manufacturing sector has always been one of the most vibrant and innovative in the American economy, made up largely of small- and medium-sized firms. U.S. manufacturing accounts for about two-thirds of private research and development expenditures and almost 20 percent of our GDP. It is a major source of good jobs for three-fourths of American workers, and it is the largest sector in 13 states.

It is unfortunate that the manufacturing sector, like the American economy as a whole, is suffering. As the economy slipped into recession in 2001, business investment on exports dropped significantly. This plunge directly affected the manufacturing industry. There have been 31 consecutive months of employment losses in manufacturing, for a total of about 2.4 million jobs, bringing this critical sector to its lowest level in 40 years. But it is not just one issue plaguing this important sector; there are many.

First, the business climate is wracked by uncertainty. The war in Iraq and its effect on world oil suppliers, combined with consumer apprehension and the inconsistent stock market, have caused uneasiness about the future. The manufacturing sector is certainly feeling this trepidation. Perhaps more importantly, though, the manufacturing sector is so weak because of a series of faulty policies put forth by the current administration, which has done nothing to ease this situation. In fact, these policies have only made things worse.

Health care is a problem for many Americans, especially those who work for a small business. Rising health care costs have taken a special toll on manufacturers. Health care is a major factor in undermining the competitiveness of manufacturers in the global marketplace. The Bush administration's trade policies have done little to help manufacturers gain back their competitive edge. The liberalizing of trade agreements and policies such as Fast Track have caused domestic producers to lose market share to foreign competitors.

In addition, the large, U.S. trade deficit in manufactured goods, driven in part by an overvalued dollar, has been responsible for massive job dislocation and plant closings across the country. The strong dollar is pricing small domestic producers out of international markets while creating windfalls for companies that can move overseas and produce goods for sales in the United States, and that is exactly what is happening. Many American firms are moving their factories and their jobs overseas because they reap the benefits under U.S. tax policy. The current tax code also gives billions in subsidies to companies that transplant their factories, outsource production, and then hide profits in offshore tax shelters.

Once again, the administration's policy helped big business at the expense of small business. The Bush administration's energy policy, or lack of one, is another example of this. The constant energy price hikes are hitting manufacturers especially hard. It has been forecasted that until energy supplies increase and prices stabilize, economic growth will be elusive.

Not only are we dealing with bad policies; we are also dealing with bad priorities. In the latest, FY 2004, President Bush slashed many small business programs, including those to help manufacturers. The manufacturing extension program, a $100 million program, will be closed out next year. The Small Business Administration, which provides the only real source of trade assistance for small business, has seen its funding continue to shrink. The SBA's export working-capital program is facing cuts in the FY 2004 budget.

Given the dismal economic outlook, how can we expect manufacturers to bounce back without giving them the right tools? That is why we are here today. Manufacturers are the cornerstone of the American economy. They have, in large part, made the U.S. a world leader and economic powerhouse, but the current climate, both at home and overseas, puts a damper on any kind of recovery for this sector. In addition, the trade, tax, budget, and energy policies of this administration have only compounded the problems of the manufacturing industry.

What we need is change. Without change in these policies and the recognition that manufacturing can be a big player in our economic recovery, we will see this downturn go on, but if we design new policies and give manufacturers the assistance they need, this nation's economic recovery will no longer be so far out of reach. Thank you, Mr. Chairman.

[Ms. Velazquez's statement may be found in the appendix.]

Chairman MANZULLO. Thank you. We are going to start with the Under Secretary for International Trade, Department of Commerce, Grant Aldonas, and as soon as he completes his opening statements, I am going to open it up for questions so that he can get back to the Department of Commerce and help create more jobs for us in the manufacturing sector. I want to do that so you do not become a victim of the tyranny of the bells; the rest of us will. Mr. Aldonas, we look forward to your testimony.

Mr. ALDONAS. I appreciate it.

Ms. VELAZQUEZ. Mr. Chairman, may I ask a question, please?

Chairman MANZULLO. Yes.

Ms. VELAZQUEZ. Did you get any testimony coming from the administration? Because we have not. Do we have it?

Chairman MANZULLO. It is on its way.

Ms. VELAZQUEZ. It is on its way. That is appropriate?

Chairman MANZULLO. All right. Let us just move on. Okay? Every once in a while that happens.

Ms. VELAZQUEZ. Well, Mr. Chairman, it is not fair. How could we be prepared if we do not receive the administration's position? That is unfair.

Chairman MANZULLO. I do not have it either, but I would like to proceed. Mr. Aldonas——.

Ms. VELAZQUEZ. That is what we expect that the groups deserve because they all submitted their testimony, and I want to be on record on that.

Chairman MANZULLO. Your objection will be noted. Mr. Aldonas, we look forward to your testimony.

STATEMENT OF THE HONORABLE GRANT ALDONAS, UNDER SECRETARY FOR INTERNATIONAL TRADE, DEPARTMENT OF COMMERCE

Mr. ALDONAS. Thank you, Mr. Chairman. Just by way of explanation, yesterday I was in Jackson, Mississippi, and I was handing out an export achievement certificate to a small manufacturer called Duropatch, and as we think about some of the larger issues that affect American manufacturing, one of the things that I want to talk about are some of the very significant success stories we have. And as we go through this, you will find that every one of them is really based on the initiative from American manufacturers, their innovation, and policies that are designed to create the environment where they can succeed.

In particular, this manufacturer has made great inroads into the Mexican market as a result of the North American Free Trade Agreement by virtue of being able to sell into markets where the Mexican government is trying to improve their infrastructure. What Duropatch produces is something that fixes roads, which means there is a huge market in Mexico for what this person manufactures, and through the Gold Key program at the Commerce Department, we were able to help him find a series of contracts throughout Mexico.

It is that sort of success story really that reflects not only what we do at the Commerce Department but the commitment the Committee has and has voiced many times over for the efforts of our trade-promotion program and for our trade policies, and that is a good point of departure, Mr. Chairman. I want to thank you for holding the hearing.

Number one, we share the concerns about the American manufacturing sector, and I have very much appreciated your leadership and your counsel and advice about the challenges facing the sector. I am familiar with the circumstances of Rockford. Rockford was much on our mind, I know, when I served in the government in the past because it has always been a leading indicator, and certainly the industries that are part of Rockford are the bedrock of American manufacturing. You cannot look at the machine tool industry and start to think about the rest of the economy.

That is a point that I think is worth reinforcing. What we have, frankly, going on, you described as hollowing out, Mr. Chairman. I really want to underscore that as well as challenges. We have some real strengths. If you look at the World Economic Forum's most recent report on competitiveness, the United States economy was listed number one, and if you go through the factors that the World Economic Forum listed in terms of our competitiveness, what you will find are exactly those things that are at the heart of American manufacturing, those things that continue to lead us in shaping the world.

I also wanted to point to an example, when we think about hollowing out, to make sure that we put it in the proper context. It is an example from my own experience. When I was in private practice, I had the opportunity to advise many of America's foremost high-tech manufacturers, and in the process what I found was, over a 15 to 20 year period, was a fairly interesting phenomenon.

A good example would be folks in the semiconductor industry and firms that operate in the aerospace sector. For years, they had operated in house their own logistical services, their own transportation services. What they found was that they could outsource those services to leading service providers like UPS in the United States, lower their costs, take advantage of the scales that UPS could offer, and what that did was really create not only a more competitive manufacturing sector but also a more competitive service sector by virtue of the scale that UPS could introduce.

Now, the reason I raise it here is what it also meant is that we do have to deal with some of the accounting realities. Jobs that used to be identified as manufacturing jobs often are taking place in what is now the service sector because of this reengineering and restructuring that is going on in our economy. So one of the things that I want to reinforce is how these two things work together, and rather than saying that this undercuts the critical nature of what is going on in manufacturing and the hollowing out we face, I like to think of it more as we should always remember who our service sector actually serves. We have got a manufacturing base in this country which, in fact, is instrumental as a consumer of a lot of what our service industry provides, and absent a strong manufacturing base, we will not have a strong service sector as well.

Mr. Chairman, you noted the statistics, and I do not think it is any coincidence that when we saw the most recent statistics in terms of a downturn in manufacturing, we saw a sharp downturn in services as well, and it underscores the point that as goes manufacturing, so goes the U.S. economy, and I think that is the thing we always have to keep in focus so when there is a debate about us becoming a service economy, we should not lose sight of the fact that manufacturing is right at the heart of the American economy and always will be.

Now, if I could, I wanted to talk a little bit about some of the challenges facing our manufacturing industry and just underscore that we are completely on the same page with you, Mr. Chairman, in terms of the challenges. First of all, manufacturing preceded the rest of the economy into recession by at least 18 months, and most economists would say longer. The Asian financial crisis in 1997 led to a sharp drop in demand for capital goods, the sorts of things that your tool-and-die manufacturers produce components for and then are exported abroad. In addition, the financial crisis, as it spread, led to a 40 percent appreciation in the value of the dollar from 1997 to 2001, in large part because the United States economy remained the only appreciable engine of economic growth in the world economy.

Furthermore, Europe and Japan trailed us into the recession and still have not recovered. While I think a lot of attention gets focused on the Japanese economy, it is interesting that if you take Great Britain out of the European economy, Europe's growth was 0.3 percent last year; in other words, they have not recovered. So the traditional sort of balance you would see in the world economy, with other economies growing and adjustment in the value of the dollar and us finding some export-led growth that would encourage the manufacturing sector, is not happening at this point.

Finally, as you noted the statistics, I will not repeat them in terms of what has happened more recently, but it does underscore the point about the need for action. I think it is fair to say to the Ranking Member that I disagree strenuously with the comments about the administration's policies. I would have to say that if you dissect what is going on in our economy and look deeply into it, what you are going to find is two-thirds of our economy is consumer spending, and one-third of it is business investment. Consumers have really maintained the economy throughout a recession that started in the last administration.

What we have done, both with the tax cuts in 2001 and with the President's most recent program, is try and tailor it so what it actually does is encourage business investment by dropping the cost of capital. If you talk with manufacturing firms in this country, one of the first things that comes up is that, with respect to the cost of capital and corporate income, we tax it at a 70 percent rate essentially as a result of the double taxation of corporate income. And while I know it is popular for many people to talk about this as a tax cut, the largest tax cut ever solely directed at business, what it is is tax reform, and it is tax reform designed to lower the cost of capital that means everything to American manufacturers.

As a practical matter, the only way we are going to compete going forward is by making sure that we add to our productivity.

That means heavy investment in capital to try and make us competitive. What that means is the most fundamental things we can consistently do for American manufacturers is keep interest rates low and try and reduce their cost of capital by making sure that the income is taxed only once. The upshot of it is I think the President has got a strong program that he has put forward that really does address many of the needs of manufacturers.

I also take issue with the idea that it is solely structured around manufacturing and is solely structured around business. As a practical matter, what we have got in front of us is a strong savings program that is directed exclusively at straightening out many of the things that Congress has introduced over time in terms of our savings programs. What the President has opted for is something that is a very clear-cut savings plan which was a part of the President's budget and, if enacted, would mean an awful lot to small manufacturers and, frankly, to consumers all across the country.

Now, we are not content really to rest solely on the President's program. What Secretary Evans announced during Manufacturing Week in Chicago was that the administration and the Commerce Department, in particular, would lead an effort to look at the challenges that are facing American manufacturing, and we have partnered with many of the organizations represented at the table in terms of trying to launch that investigation. Secretary Evans has asked me to lead that. Our intent is to hold a series of field hearings across the country so that we encourage as many industries in the manufacturing sector to come forward and talk to us about the challenges they are facing to see what part of that is something that government can tackle, and here I really want to come full circle to where I started out.

When I look at the many manufacturers like Duropatch in Jackson, Mississippi, that succeed in the marketplace, what you always find is governments can create the environment, but ultimately we are going to have to rely on the innovation and the energy that our own small business sector provides. Ultimately, that is where the answer lies. Our job is to create that environment. We are committed to doing it, Mr. Chairman. Thank you.

[Mr. Aldonas' statement may be found in the appendix.]

Chairman MANZULLO. We have the tyranny of the bells starting in. Mr. Aldonas, can you stick around until we get back for questions?

Mr. ALDONAS. Sure.

Chairman MANZULLO. Are you sure?

Mr. ALDONAS. Yes.

Chairman MANZULLO. Okay. And then, Congressman Ryan, as soon as we get back from voting, then we can get your testimony also. Okay. We are adjourned until about 3 o'clock, unless the votes end earlier.

[Whereupon, at 2:31 p.m., a recess was taken.]

Chairman MANZULLO. The Committee will be called back to order, and sorry for the inconvenience.

I have just one or two questions to ask of Under Secretary Aldonas, and that would be really an embellishment of where you started on your main testimony, and that is the President tasked the Secretary of Commerce to come up with a comprehensive plan for restarting or resurrecting manufacturing, whatever it is called, and that would be my question to you, Mr. Aldonas, to give us more of the meat of what that proposal is and how you plan to bring it to fruition.

Mr. ALDONAS. I could not describe the meat right now because we need to spend some time talking with our manufacturers. What we need to do is shorten that time as much as possible, which is why, even during the break, we were talking amongst ourselves about what I have drafted as an outline that outlines the process so that we have a deliverable by mid-summer which has both recommendations for action as well as points that we need to look further into with specific industries.

The next step in that process, after we have gotten that done inside the Commerce Department, which I expect to conclude tomorrow morning, is to get it to our friends with labor and with business so that they get a chance to take a look at it and make sure they feel comfortable with it and then help us identify the places where we ought to be going as a part of the outreach. We have already launched a literature study. There is a real rich body of literature out there about a number of things that are affecting manufacturing. We are going through that material now inside the Commerce Department, so we have got that base in place before we head out on the field hearings.

But my expectation is we will do really three things. We will gather and analyze the material that is available as a part of the literature search. We will certainly rely on things like the national academy, which you may know has launched a recent investigation of its own with respect to high-performance manufacturing. So we will try and piggy-back as much on those resources as we can where they are tapping into certain industries and move our focus elsewhere so that we try and do as good a job as we can coordinating within the Executive Branch about how to approach the issue.

I hope that we will be through the field hearings by the end of May and that we will be developing a series of recommendations, as I said, both for action as well as what we ought to be doing in terms of further study on individual industrial sectors. So our goal is really to have something in an interim report to the Secretary really at the start of July, and that is a point where I would hope what we can do is come up, maybe in an executive session, and sit down with everybody and start to talk that through here with the Small Business Committee because it is going to be important for us to be hearing from members as well, so that as we start thinking about developing an agenda—I understand this is a bipartisan issue, and it is something where both sides have to come together because that is the thing that is really going to drive any sort of agenda to the extent that we need legislative action and, frankly, to the extent that we need support from the Congress for what we could do on the administrative side of the house as well.

Chairman MANZULLO. Ms. Velazquez?

Ms. VELAZQUEZ. Thank you. Mr. Aldonas, you said that the Bush administration has reduced the cost of capital. Do you know where the bulk of capital to small businesses, including small manufacturing, comes from?

Mr. ALDONAS. Most of it comes from lending, and what you want to do is try and do two things. One is not only reduce the interest rate that gets charged, but you also want to try and make sure that you deepen and broaden the pool of capital that is available so that investors with a broader risk profile, venture company, essentially, can come and assist. And why that is important is you do not want to leave small business manufacturers solely at the behest of lending institutions. If they can find someone who is willing to invest in them, provide the private equity so there is not an interest payment attached to it, you oftentimes have somebody who is more committed to the growth of the enterprise.

Ms. VELAZQUEZ. Okay. I agree with you, it is lending, but do you know what type of lending, from where?

Mr. ALDONAS. Well, sure. It is local banks, oftentimes with guarantees from small business——

Ms. VELAZQUEZ. No. I am going to help you.

Mr. ALDONAS [continuing]. And with the Small Business Administration.

Ms. VELAZQUEZ. Yes. Most of the lending to small businesses comes from the loan business programs within the Small Business Administration. In fact, 40 percent of long-term capital to small businesses comes through the 7(a) loan program, 504, all of those loan business programs. So when you said that the administration reduced the cost of capital, I want for you to explain to me how can you say that when the administration capped last year all of the SBA business loan, taking billions of dollars out of the economy; and, two, the administration has not ended yet taxing small businesses by overcharging by $1.5 billion in excessive fees that small businesses have to pay when they access one of these loan programs. And then, on top of that, the FY 2004 budget for the Small Business Administration is $3 billion below last year's request, and this is just the $3 billion just for the 7(a) loan program.

So I need for you to help me understand how the administration reduced the cost of capital for small businesses, including small manufacturers.

Mr. ALDONAS. Let me give you an example because I think we are talking about two different things. The fact that you reduced the amount of funds, the amount, the quantity, of funds, flowing through the SBA does not necessarily mean that you are raising the cost of capital. For example, in the President's proposal, which has passed the House and which I hope will certainly become law, there are things that allow small businesses to expense the cost of capital rather than having to amortize it over the useful life of the equipment. What that does is reduce the cost of capital from the perspective of them going to the markets. They can see a lower tax burden on small businesses, and it gives them more of a reason to invest, and ultimately what we want to do is encourage equity investment to the maximum extent possible.

Ms. VELAZQUEZ. Okay. Mr. Aldonas, in the manufacturing industry, many businesses are currently managing extraordinary amounts of debt. The President's tax plan, if it passes, will drastically increase the budget deficit, driving up long-term interest rates and only exacerbates these manufacturers' problems by increasing borrowing costs. So, once again, how do these actions reduce the cost of capital? Would you please help me understand that?

Mr. ALDONAS. Sure. If what you are doing is you are trying to turn to the private equity market, and you are trying to encourage people to invest, what you want to do is show that there will be a higher cash flow coming through the company, and what you do with the President's tax plan is ensure that there is a higher cash flow coming through the company so it is more attractive to an investor, and, overall, we are better off, frankly, if small manufacturers have a deeper pool of equity capital to turn to, and the reason fundamentally is that they are not stuck with an interest rate charge that is driven by a lot of forces, not just the budget.

Ms. VELAZQUEZ. Okay. Let us move to my next question.

Mr. ALDONAS. Sure.

Ms. VELAZQUEZ. At a time when the manufacturing industry is facing a crisis, the administration has decided to terminate programs such as the Manufacturing Extension Partnership program, a program especially tailored to assist small and medium manufacturing firms. Can you please tell this Committee why the administration is cutting this program from its budget at a time when it is most needed?

Mr. ALDONAS. Absolutely. It is a very, very good program. We are facing budgetary constraints, and the question is where are you going to invest your limited amounts of resources, and under these circumstances, the decision that was made is that there are other tools that we can try to use to lower the cost of capital and improve the prospects for investment, including in the small business sector, and so the goal has to be to look at as many tools as you possibly have. But this is one which nobody thinks there is a problem with the program. Having said that, it is one of those things where, given the constraints, we decided this was one that we were going to have to cut.

Ms. VELAZQUEZ. So this is the way you are going to help the manufacturing industry that has been in a crisis for so long, by eliminating a program that is tailored just to assist them, but the dividend tax cut that only is going to benefit three percent of small businesses, that is in place. Thank you.

Mr. ALDONAS. Well, you have to be very clear. The figure you cite about helping only three percent of the businesses in the United States, I have real trouble with because being enough a student of the tax laws, these are generally applicable provisions, and, indeed, there are additions on top of the elimination of the double taxation of corporate income that are generated specifically for small business, particularly with respect to their capital investments.

So if what you are thinking is what you are trying to do is create a small business environment where they have an opportunity to invest in those things that will make them productive and lower their overall cost of production, it means things like expensing of their capital costs, and that is why that is built into the President's plan.

Ms. VELAZQUEZ. Expensing; that is the only thing that small businesses are going to get.

Mr. ALDONAS. No, no, no. That is not true. It is on top of everything else in the proposal. Everything else that is built into that proposal is designed to help businesses across the board.

Chairman MANZULLO. This is good, but let us stick to manufacturing.

Mr. ALDONAS. Okay.

Chairman MANZULLO. Mr. Chocola?

Mr. CHOCOLA. Mr. Aldonas, I am sorry I was not here for your testimony. If this was covered, I apologize, but I come to Congress from a manufacturing background. I have spent my entire adult life in the manufacturing business. We had about 1,300 employees. We made agricultural equipment. Just as a statement, if we had had the opportunity to not have double taxation on the dividends of operating companies, both in the private and the public sector, it would have been a great opportunity to create more jobs. So certainly, some, real-life experience, would love to have that opportunity to grow our economy and grow job opportunities.

A quick question: About 45 percent of our business was outside the United States. We were basic manufacturing, metal bending, injection molding. We did not do anything high tech, but we were able to take advantage of the opportunities of the global economy. A lot of times you hear about direct-labor costs, and we move jobs to Mexico or China because of direct-labor costs. We probably never would have moved our business because of that. What we were more concerned with was the excess taxation, regulation, litigation that I, as CEO, had to spend an inordinate amount of my time rather than serving our customers and building our business. Are you aware of any studies or research that really shows why companies move their business or why jobs are lost in manufacturing, especially small businesses?

Mr. ALDONAS. Actually, if I could provide a written response to that because we are going through that process right now with developing the literature search so that we are informing ourselves, and what I ought to do is make the bibliography available to you because there is a wealth of information out there. We have touched base with the folks that do the World Economic Forum's competitiveness study to sort of tease through all of their research materials. That is a great starting point because they look at economies all across the world, not just the U.S. economy. But we will make sure we provide that to you.

Mr. CHOCOLA. Thank you very much.

Mr. ALDONAS. Surely.

Mr. CHOCOLA. Mr. Chairman, I yield back my time.

Chairman MANZULLO. Okay. Ms. Napolitano?

Ms. NAPOLITANO. Thank you, Mr. Chair. Mr. Aldonas, there is a question here that begs a little bit of an answer. Under the President's dividend tax cut, only those companies with a profit will see any change with regard to their treatment of their dividends. The companies without a profit will have their dividends taxed at the individual level. The reason is the plan is designed to prevent double taxation of the dividends; thus, the companies without a profit have not been taxed at the corporate level, so it is not double taxation if you continue to tax individuals. Additionally, companies that cannot pay dividends may see a shift of investment away from their businesses towards companies that can.

The question is, most manufacturers either do not have a profit or cannot afford to issue dividends to their shareholders because of the economy. The President's dividend tax cut only impacts those dividends which are paid by companies who have a profit. These companies with a profit will still have their dividends taxed at the individual level. Is there a concern that the dividend tax cut will shift further investment dollars away from manufacturing to businesses that can take advantage of the President's tax proposal?

Mr. ALDONAS. It is a very good question, and it requires really a chance to unpack some of this. When an investor is looking at a company, looking at their cash flow, they look at the potential tax burden. They are trying to look at the cash flow and what profits may eventually come from that as they try to decide to invest, and to the extent that what you are doing with the tax laws is lowering the potential burden in the future should they generate income, it makes it a more attractive investment for somebody who is looking at it from the outside.

So even to the extent that what you find with American manufacturers who may not be generating a profit now, things that reduce their potential tax burden in the future are attractive to an investor if you are trying to pull that investment in, so that is number one. I am sorry.

Ms. NAPOLITANO. Yes, but let me just step in and say that manufacturers need the help now. They are in dire straits. They have been for a number of years, and they cannot afford to wait. A lot of them are in really the throes of bankruptcy.

I would like to yield time to the Ranking Member.

Mr. ALDONAS. If I could, though, I wanted to finish my response, Congresswoman. The other thing that is, I think, important to realize about the changes here is that we right now in the tax code have a significant discrimination in favor of debt, and what that leads American companies to do is draw on lending rather than go into the equity markets, and the effect of that is to impose a very high cost on our companies. We make it more attractive for them to bring on a debt burden. And one of the real benefits of the President's proposal is that it eliminates as much as possible of that preference for debt in the system, and, as a consequence, what it does is make more money available through private equity for investment, small and large businesses. And the importance of expanding that pool is, overall, it lowers the potential cost of doing business in the United States.

Ms. VELAZQUEZ. Mr. Aldonas, I guess that you are arguing against what you were just saying because you say that profits in the future for small manufacturing, but my question to you is, if an investor is going to invest, he is going to look at whether or not a small manufacturer is going to have profits. If they do not, they will not invest in that manufacturer. They will invest in someplace else where they then can benefit from the dividend tax cut.

Mr. ALDONAS. But then I think, I mean, with all due respect, the question is what other tools do you have under those circumstances to lower the cost of capital, and the question really is whether you are going to do something that creates the environment where individual companies can succeed or whether you have decided that we are going to get into the business of wholesale subsidies. And, frankly, from the perspective of an administration that believes in the market, I think our goal is to try and create the environment where companies can succeed, not getting into the business of favoring certain companies over others.

In fact, to be honest with you, the more you encourage the Executive Branch to divide the economic grants that are available in any marketplace, that is not a power you want to give to the Executive Branch because that leads to preferences for individual companies, which, frankly, from our perspective, is something that ought to be sorted out in the marketplace, not based on the decision of anybody in the government.

Ms. NAPOLITANO. Mr. Chairman, I yield back the balance of my time.

Chairman MANZULLO. Thank you. Mr. Ballance?

Mr. BALLANCE. Thank you, Mr. Chairman. Just a brief followup, Mr. Aldonas. In response to Ms. Velazquez, you mentioned short capital. I take it that when the administration was putting together this budget, it realized the dire strait that manufacturing was in and chose to make these cuts in any event.

Mr. ALDONAS. Absolutely. What we are trying to do is create an environment where you are lowering the cost of capital and trying to encourage investment. Ultimately, we want to make sure that the United States is the most attractive place to invest possible so that that drives our economic growth, and lowering taxes is a part of that. Certainly, lifting what happens to be the highest-rated taxation on corporate income in the world, 70 percent, is a smart thing to do under those circumstances if we are trying to encourage a broader pool of private equity capital that funds a lot of what our companies have to do.

I think the other point is that there is nothing about maintaining existing taxes on corporate America, particularly on small- and medium-sized businesses, that any economist will tell me, at least, is a good idea, given the straits that our manufacturers are in. I cannot find that. I honestly cannot find somebody who says to me that leaving in place a 70 percent tax burden on corporate income is wise if what we are trying to do is encourage investing in manufacturing. I cannot find them.

Mr. BALLANCE. Just one more follow-up. That is philosophy, and I guess we could debate that, but in my district, in Vance County and Halifax County, we have a lot of businesses going out of business and a lot of people without jobs, and, of course, the tax cut is not going to help them, but having a job would.

Mr. ALDONAS. Well, if I could respond to that, though, I mean, these two things are two halves of the same walnut. If you want small businesses to be able to produce jobs, which is the greatest gift anybody can extend—certainly, I know, growing up, whether it was me starting out or whether it is my daughter, who is graduating right now—she is coming into a tough economy—I understand that, but for our small businesses to provide those jobs, the things we have to do is create the environment where they can succeed, and, frankly, taxing their income at twice the rate, frankly, is not the ideal way to give them the power to create the jobs for your constituents and my daughter.

Chairman MANZULLO. Thank you, Mr. Aldonas. You have to run back to the Department of Commerce. We want to thank you for—do you want to stick around, or what would you like to do?

Mr. ALDONAS. Actually, I still have some lumber negotiations going on that I have got to go back to,——.

Chairman MANZULLO. All right. Okay.

Mr. ALDONAS.—but what I would like to do at some point, Mr. Chairman, if I could, is, as we go through this process with our colleagues, and I know I was talking with both Rich and certainly Jerry about how we need to get together to sort through our outline and identify areas we need to be looking at, I want to come back to the Committee——

Chairman MANZULLO. Absolutely.

Mr. ALDONAS [continuing]. So that what I am doing is figuring out if Mr. Ballance has a constituency we need to be visiting to understand the dynamic of the problems they are facing, I want to be there.

Chairman MANZULLO. The door is open. Ms. Napolitano, a short question.

Ms. NAPOLITANO. A very quick question, Mr. Aldonas, and that has to do with the administration's effort to assist small businesses to establish a business presence in a host country. Can you tell me what is happening? And understand, I have been in international trade for a while.

Mr. ALDONAS. A long time, yes.

Ms. NAPOLITANO. You remember that. I find that the large companies have the ability to do their own. Small companies need the assistance. When I took a group of my business people over to the Department of Commerce and the California trade and commerce agencies, they have very limited personnel to be able to do the outreach. What are we doing to be able to assist penetration? It begs the question.

Mr. ALDONAS. No, no, and you could help me there, Congresswoman, because traditionally I think people have looked to the Commerce Department to promote our exports, and, of course, what you are finding is exactly what everybody else is finding: Oftentimes, to be able to export, you may have to create a representative office overseas. Well, that is investment, and I think there has been an argument for a very long time that the Commerce Department should not be in the business of encouraging foreign investment with the idea that jobs would go with that investment. And, of course, what I think we need to do is make sure that the Commerce Department is in a position so our foreign commercial service officers really are empowered to help that constituent.

The other thing I think we have to do is look at the overseas private investment corporations, which I do not know that they are here or part of the discussions, but traditionally they have facilities that are not used by small businesses, and I think they are only now becoming alive to the fact that small businesses, to be able to export, are going to have to invest for precisely the reasons you cite.

Ms. NAPOLITANO. And a follow-up to that is that in speaking to the AMCHAMs in several of the foreign countries that I have been privileged to visit, I have consistently asked the question of the AMCHAMs if they have an arm of the chamber to assist American business penetration in those countries. Only two, Brazil and Hong Kong, have that ability. Is there any way that the administration will work with these AMCHAMs to be able to help them do that outreach? Hong Kong already does workshops in the U.S. Why are we not dovetailing efforts with them to be able to promote those companies that need help or that want to be able to assist penetration?

Mr. ALDONAS. It is a good point. I would like to hear more about it because I think we have got a wonderful network, as you know, in terms of both the Commerce offices in the United States as well as our offices abroad, and it is underutilized. It really could be a powerful tool to help in those instances.

Ms. NAPOLITANO. Not many people know where to go, what Web site to hit, where the information is concise enough for them to understand while they are tending to business, trying to stay alive and make a dollar.

Mr. ALDONAS. You are absolutely right.

Chairman MANZULLO. Okay. The Commerce Department, pursuant to a conversation we had with their working group on small- to medium-sized exports, has come up with a personal export officer program. Professor Czinkota had a hand in that also, and Gerry Jensen Moran is the head of the TPCC.

Mr. ALDONAS. Which she is unbelievably good, I have to say. She really is the best.

Chairman MANZULLO. She would be the person to answer the question. Congress is now cross-training 10 agencies from the same manual so the small business person could get in there and get the job done.

Mr. Aldonas, thank you for being with us today.

Mr. ALDONAS. Thank you very much. I appreciate it.

Chairman MANZULLO. Our next witness is Congressman Tim Ryan, who probably has the reputation of being the shortest member in terms of longevity on the Small Business Committee. He was here and asked a burning question on an issue to which he is going to testify, and then he got appointed to the Armed Services Committee, and then he left us.

Mr. RYAN. I miss you already, Mr. Chairman.

Chairman MANZULLO. There we are. We look forward to your testimony, Congressman Ryan.

STATEMENT OF THE HONORABLE TIMOTHY J. RYAN, U.S. REPRESENTATIVE, OHIO

Mr. RYAN. Mr. Chairman, that would make four committees for me, and as much as I do love you. Thank you very much for being here, and I appreciate all of the work that you have done, Mr. Chairman, on the Berry Amendment, which is the topic today. Madam Ranking Member as well, I want to thank you for allowing me to testify today.

U.S. manufacturers and their skilled employees are at grave risk as American companies continue to lose market share. The problem is serious, and I commend the Committee for looking at this issue and working to help our nation's manufacturing industry. For the first two months of 2003, employers initiated 3,597 mass-layoff actions, according to the U.S. Department of Labor, Bureau of Labor Statistics. In total, 340,000 workers were affected. Manufacturing industries accounted for 35 percent of all mass-layoff events and 40 percent of all initial claims filed in January and February.

These statistics show me one thing, Mr. Chairman: The United States is continuing to lose its domestic manufacturing base. Our colleague and friend, Ranking Member Ike Skelton, has often said that the U.S. armed services serve, in peacetime as well as war, as insurance for our great nation. Well, Mr. Chairman, I believe that the U.S. manufacturers are the insurance for our armed services. We cannot be relying on foreign supplies for the products that are vital to our national security. Today, there is only one U.S. company that makes track for the United States Army tank systems. Likewise, there are only three U.S. manufacturers of titanium, a specialty metal that is an essential component in military aircraft and engines. These domestic manufacturing operations and the skilled workforce that produced the products for our armed services are critical.

Recently, I was informed by the Employment and Training Administration of the Department of Labor that workers in my district lost their jobs because of foreign imports. RMI Titanium, which is located in Niles, Ohio, was forced to lay off workers because Boeing Commercial Air Group decided that it was a better idea to import its titanium from Russia. RMI's employment declined, and American men and women lost their jobs because Boeing is increasing its titanium imports and not purchasing it domestically. Therefore, the unemployed workers qualified as adversely affected, secondary workers under Section 222 of the Trade Act of 1974.

Mr. Chairman, how many other workers, how many small businesses will this have to happen to until we watch our industrial base continue to decline? Today, government and business need to come together to secure our nation's industrial base, and the foundation for doing so is already in place. Mr. Chairman, as you know, it is the Berry Amendment, and that is why I am here today, because the Berry Amendment protects U.S. textile companies, food producers, and manufacturers by requiring the U.S. military to purchase products that are 100 percent made in the United States.

The Berry Amendment and the Buy American Act are critical to homeland and national security. They were enacted to ensure that the United States preserves its domestic capability to produce the full range of products that are essential to our armed forces and, in turn, our national security.

Mr. Chairman, let me just wrap up, and I would be happy to take any questions, but the bottom line here is that we have a responsibility, as members of Congress, not to any one corporation, not to the business community. We have a general sense to provide a good atmosphere for the business community to thrive and to prosper, but when it comes to the national security of this country, we have an obligation to make sure that in a time of war, like we are in right now, we can procure everything that we need right here in this country, and, unfortunately, the waivers to the Berry Amendment over the past two years have weakened our ability to do that.

I know, for example, in my district, as I mentioned, we are losing the titanium industry. There are three titanium manufacturers left in this country, and there is a massive supplier in Russia, which American companies are buying from. And as we understand the pressures and the economic downturn, we have to remember that our first obligation is to protect our own country and be able to do that from the products that we can buy from this country.

And so I urge this Committee and you as well, Mr. Chairman, to keep the pursuit of the Berry Amendment and keep being such a vigorous advocate of closing the loopholes in the Berry Amendment and really just enforcing it the way it is right now. So with that, Mr. Chairman, I would be happy to continue this discussion or take any questions.

Chairman MANZULLO. Well, we have got a vote on the floor now.

Mr. RYAN. This is more important, Mr. Chairman.

Chairman MANZULLO. It probably is. There is a food fight going on down there. How many votes are there? Does anybody know? Three votes? Wonderful. It is going to be at least a half an hour. We will be back in about a half an hour. That is all I can tell you at this point. Thank you.

[Whereupon, at 3:32 p.m., a recess was taken.]

Chairman MANZULLO. The Small Business Committee will come to order. Those are not more votes. We are supposed to have three more votes at 5 o'clock, and I am sorry for the tyranny of the bells.

I have been advised that Mr. Harbour has to catch a five-thirty plane, so I am going to start with you. Is that correct?

Mr. HARBOUR. Yes, sir.

Chairman MANZULLO. And we have the five-minute clock here, and we look forward to your testimony, please.

Mr. HARBOUR. Okay. I apologize for any inconvenience.

Chairman MANZULLO. No inconvenience. Go ahead, please.

STATEMENT OF RON HARBOUR, PRESIDENT, HARBOUR AND ASSOCIATES, INC., TROY, MICHIGAN

Mr. HARBOUR. Thank you, Mr. Chairman, for the invitation to speak with you at this hearing. Today's subject matter is near and dear to my heart, as it relates directly to the environment in which I work and live in every day.

I am an owner of a consulting firm called Harbour and Associates in Detroit. We work with many manufacturing companies in helping improve their costs, quality, and productivity, with particular emphasis on the manufacturing side. Being in Detroit, most of our work is with the automotive companies, both domestic and foreign owned, as well as many of their suppliers. Nonetheless, we have worked with many non-automotive companies as well.

In addition, our firm publishes an annual study called the Harbour Report, which I have here in my hand. It is a document that analyzes and ranks the performance of all of the North American automakers, including discussions on what drives their results. In support of our work, we have had the privilege to walk the floors of almost every automotive plant in North America, Japan, and Europe and many of their suppliers. I believe this experience gives me a unique insight into what has evolved in the recent history of U.S. manufacturing, certainly in one of its largest segments, the automotive industry. However, the lessons learned are analogous across many industries.

Like many industries, the automotive industry was broadsided by an unanticipated foreign competition 20 years ago and has never fully recovered. Initial responses were protectionist, with import quotas and tariffs in response to cries of dumping and unfair competition. Our early research in 1980 and 1981 for the Department of Commerce told a very different story from what everyone assumed was the problem. Our tours of Japanese plants revealed operations that attained much higher levels of quality and productivity than U.S.-based operations through very strong design, engineering, and training. Although differences did exist at that time in labor rates and currency exchange, the companies were simply better manufacturers.

Protectionism only bred complacency in the 1980s, but once the foreign competitors began manufacturing directly in North America, Detroit was forced to compete. Competition has saved what is left of the domestic auto industry, as many domestic plants and their suppliers have reached world-class levels of performance. The American consumer is the one that has won because cars and trucks are far better quality and dramatically less cost, adjusted for inflation, than they were ever in history.

A manufacturing base is vital to a strong and modern economy. This is well known in Japan, Germany, Korea, as well as emerging economies such as China. I wonder how we would be supplying our troops in Iraq with planes, ships, guns, and missiles if we could not produce them in the U.S. What would we do, import them?

Those who claim a modern economy can be primarily service based and blind to the fact that those same service-based companies need a consumer for their services. Manufacturing-based companies provide a large customer base for those companies. In other words, a balance between service and manufacturing is key to a vital economy.

Recent studies have demonstrated the far-reaching effects well-compensated manufacturing jobs have on nearby businesses, both other manufacturers and service providers. These include the corner grocery store, the local Wal-Mart, banks, barber shops, electronics, recreational vehicles, furniture. Little wonder states throw hundreds of millions of dollars at foreign auto companies looking for a home for their new plant. Unfortunately, most domestic companies have not been able to secure the same kind of financial support.

I am greatly concerned about the decline of our manufacturing base in this country, and I believe it will have long-term ramifications to our economy. Many factors have driven the shrinking of employment levels in manufacturing, some purely from healthy gains in productivity. Other jobs have left due to our lack of competitiveness. But many are gone due to the lack of any kind of business/government alliance to cultivate the growth of manufacturing in the U.S.

I hope that our discussion this afternoon can constructively lead to solutions to this American dilemma, and I promise to do all I can to contribute. Thank you, Mr. Chairman.

[Mr. Harbour's statement may be found in the appendix.]

Chairman MANZULLO. Thank you very much. I trust that you will have an extra copy of the Harbour Report for our convenience.

Mr. HARBOUR. Yes. I can leave it.

Chairman MANZULLO. Thank you. Our next witness is Jerry Jasinowski, president of the National Association of Manufacturers.

STATEMENT OF JERRY JASINOWSKI, CHAIRMAN, NATIONAL ASSOCIATION OF MANUFACTURERS

Mr. JASINOWSKI. Thank you very much, Mr. Chairman, and let me congratulate you for your leadership on manufacturing on this Committee and generally. I wish to make five points and ask that my statement be included in the record.

Chairman MANZULLO. All of the statements will be included in their entirety without objection.

Mr. JASINOWSKI. I represent the National Association of Manufacturers, with roughly 14,000 companies, almost 17 million workers, and they are both large and small, and although there are some differences between the two, for the most part what I am going to say reflects both large and small manufacturers.

The five points I would make are these. We have had you say, myself say, and Rich Trumka say that manufacturing is in crisis. Many others have said the same. Grant Aldonas did not differ from that view. Most of the Democratic and Republican members of your Committee agree. I think we now are over the hump with respect to recognizing the serious crisis we are in, and we need to, therefore, move for bipartisan, executive, congressional, labor, and management cooperation to build a big, strong coalition to ensure that we have the policies to achieve over a number of years, not a quick fix, the renewal of manufacturing and its employment.

Item Number 2: Why is there this agreement about a crisis? It is because there is a disconnect between the huge benefits of manufacturing, on the one hand, and the reality of where we are now. The benefits range from the fact that we are the engine of growth, we have the technology, the highest rates of productivity, we provide for the national defense and security, as you see in Iraq, we have the best jobs, we are the heart of trade, and all of these things are the things that drive the economy and the service sector.

So if we are such a jewel, how is it that we could have the following set of negative situations? We have the slowest economic recovery in modern history. We have a two percent increase in output in the first year for manufacturing, compared to a usual 10 percent increase in output that we get in most recoveries, and currently, in March, manufacturing is dead in the water.

We have lost over two million jobs. These are among the best jobs in the world, paying 20 percent more than the other jobs in this country, and that is the state of play today, and it is this gap, I suggest, between the extraordinary factors that show that manufacturing matters, on the one hand, and the fact that we are dead in the water currently with respect to output growth and employment.

What do we do in these situations? The NAM passed a resolution, which is a part of my testimony and I would like included in the record. It is a very large board of large and small members of manufacturing firms, and they said that we needed to do a whole range of things on both the policy and on the infrastructure front.

Let me talk about the three key policy areas. One, we have got to have growth. The economy is dead in the water. If you do not get growth, you do not improve manufacturing, demand, you do not provide employment, and you do not provide anything. There was a lot of debate about the President's tax package. I would point out that if people do not like the composition, then let us get some compromise and change. We support the composition as it is, but I understand there are different points of view.

The fact is it is critical to get a package to stimulate growth now, not later, now. And the other thing I would say is although you can debate the dividend part of this as you wish, I would point out that the individual rate cuts are extremely important for small manufacturing and small enterprise because they are in many cases Schedule C. But my main point is let us get agreement that we should have a stimulus to occur there.

The second area of crucial policy concern is trade and China. We have an uncompetitive playing field in many trade areas today, while the United States has been the most open trading country in the world. We should not move to protectionism. What we should do is, in fact, force that everybody play by the rules and, in particular, that China play by the rules. The Chinese government and the Chinese economy has exchange rates that are 40 percent undervalued. They have subsidies, unfair trade, and counterfeiting. They have a situation where they do not have protection of intellectual property rights, nor do they have proper allowance for exports. We have the largest trade deficit now of anyone with respect to the Chinese, and that must stop. If it does not stop, we will have protectionism.

Chairman MANZULLO. How are you doing on time? I want to make sure everybody gets in before the bells go off at five.

Mr. JASINOWSKI. The only last point is that we have got a cost escalation in this country which is shifting manufacturing abroad, and that is the third policy we must address, Mr. Chairman. Thank you.

[Mr. Jasinowski's statement may be found in the appendix.]

Chairman MANZULLO. Thank you. Mr. Trumka.

STATEMENT OF RICHARD TRUMKA, SECRETARY/TREASURER, AFL–CIO

Mr. TRUMKA. Thank you, Mr. Chairman and Representative Velazquez. I am pleased to have the opportunity to appear before the Committee on behalf of the unions of the Industrial Union Council and the 13 million working men and women of the AFL–CIO.

The industrial unions of the AFL–CIO have banded together to respond to the deep crisis in manufacturing. We are dedicated to finding solutions to the serious challenges that face U.S. manufacturing and threaten the livelihood of millions of American working families. It is important to note that about two-thirds of all workers and manufacturers represented by unions are employed by small- to mid-sized businesses. That is 200 workers or less.

For 32 straight months, manufacturing has lost jobs. That is the longest stretch, Mr. Chairman, since the Great Depression. Since April of '98, we have lost 2.5 million manufacturing jobs, nearly 13 percent of our total.

Among the disturbing trends that many economists have noticed, capacity utilization in U.S. manufacturing, a measure of production activity, dropped to 74 percent late last year, its lowest level since 1983, and our trade deficit in goods is now growing by $1.3 billion each day. Nearly every state in the nation has suffered manufacturing job losses, as the chart enclosed in my testimony shows.

Unless these trends are reversed, serious damage will be done to the livelihoods of American working families and to the nation's economy. Manufacturing historically has been a major generator of good, high-skilled, well-paid jobs, including in non-manufacturing sectors, and remains a mainstay of local and state economies throughout the nation. Manufacturing's decline not only undermines the quality of manufacturing jobs but also contributes to the stagnation of all workers' wages. Moreover, the massive scale of manufacturing plant closings and job layoffs is contributing directly to the serious financial crisis afflicting every state in the nation.

America's manufacturing workers are the most productive in the world, but they operate under enormous competitive disadvantages resulting from several factors, such as unfair trade and tax policies, an overvalued dollar, inadequate investment incentives, health care costs not borne by overseas producers, and foreign government subsidies. Unless these problems are addressed soon, American manufacturing capacity and jobs may end up permanently lagging, and our economic strength may be permanently weakened. U.S. productivity and wage gains have been largely driven by the performance of the manufacturing sector. It is unlikely that another sector can step in to offer comparable wages, benefits, or productivity gains on as large a scale.

Mr. Chairman, I will say that we will not have a stable, broad-based economic recovery without a strong manufacturing base.

There are a few issues I would just like to mention today very briefly. They are enclosed and handled more adequately in my written testimony. When it comes to investing in manufacturing, we recommend restoring funding for the MEP. We encourage Congress to replace the FSC with a broad-based, manufacturing tax credit that rewards companies for keeping good jobs here and creating new ones.

Trade; put simply, America's trade policy has failed. That is not a partisan criticism, as unfettered trade liberalization has been an imperative for all administrations recently. Congress can do two things: First, oppose new trade agreements, such as the Free Trade Agreement of the Americas, based on the failed NAFTA model, which has produced an $87 billion trade deficit, and FTA will be NAFTA times 10. Also, Congress should aggressively challenge non-tariff barriers to trade and ensure that our trade laws our enforced.

Mr. Chairman, we ask Congress to take these steps immediately. First, Congress should pass the manufacturing tax credit to replace

FSC. Second, Congress should pass a prescription drug benefit to help deal with the most expensive aspect of retiree health care and work on broader health care solutions. Third, Congress should not pass any more trade agreements like FTAA that would expand our trade deficit, based on the failed NAFTA model.

Fourth, Congress should initiate trade cases to enforce U.S. trade laws and take aim at non-tariff barriers to trade in China, Japan, the EU, and elsewhere. Fifth, Congress should stop companies from reincorporating overseas to avoid paying their fair share of taxes. Sixth, Congress should strengthen the Buy American provisions for the Department of Defense. Our defense budget is extraordinarily large, but defense manufacturing jobs are disappearing. There has not been a national strategic inventory by the DoD since 1996. And, finally, Mr. Chairman, Congress should recognize this for what it really is: a crisis that imperils our economy. Thank you, Mr. Chairman.

[Mr. Trumka's statement may be found in the appendix.]

Chairman MANZULLO. Thank you very much. The next witness is Paul Freedenberg, vice president of the Association for Manufacturing Technology. Mr. Freedenberg?

STATEMENT OF PAUL FREEDENBERG, PH.D., VICE PRESIDENT FOR GOVERNMENT RELATIONS, THE ASSOCIATION FOR MANUFACTURING TECHNOLOGY

Mr. FREEDENBERG. Good afternoon. My name is Paul Freedenberg. I am vice president for government relations at AMT.

A.M.T. is a hundred-year-old, trade association that represents approximately 360 machine tool builders and related product firms located throughout the United States. I am pleased to testify before you today on the importance of America's manufacturing sector to our economic strength and stability. I will also discuss the uphill battle my industry, America's machine tool industry, faces to survive in these tough times.

Mr. Chairman, I would like to begin by thanking you for your strong leadership, along with Congressman Neal of Massachusetts, of the House Machine Tool Caucus, which has provided invaluable support and encouragement to our industry. Mr. Chairman, I would also like to thank you and members of your Committee who supported the economic-stimulus package enacted into law last year. The 30 percent expensing provision included in the package was AMT's top legislative priority for the 107th Congress. Improving and extending it, making it permanent, is AMT's top legislative priority for the 108th Congress.

Manufacturing has contributed to the overall economic growth, disproportionately to its actual share of the GDP. Over the past 30 years, manufacturing's share of GDP has been falling, while at the same time finance, insurance, and real estate, and services' share of GDP have been rising. Manufacturing's share has fallen by almost 50 percent during that period. Nevertheless, during the last major economic growth period, which was 1992 to '98, manufacturing accounted for more than half the rate of growth of the GDP, far more than any other sector.

The machine tool industry is a very small segment of our nation's manufacturing infrastructure relative to its critical importance.

Significantly, machine tools should be understood as the basic building blocks for all other industries, whether those industries are automotive, defense, aerospace, electronics, or appliances. Everything made in a factory is either made on a machine tool or on a machine made by a machine tool. Approximately 30 percent of the machine tool industry's output is exported, and both at home and abroad our industry competes with machine tool companies from around the industrialized world.

In my written testimony, I discuss our nation's remarkable productivity boom during the last decade. Well, that boom would not have been possible without a strong machine tool industry. That means that the key to reversing the economic downturn that we are currently experiencing and returning our nation to economic prosperity is also dependent on the maintenance of a strong and healthy machine tool industry, which is the key component of this nation's manufacturing infrastructure.

Machine tools translate the dizzying advances in information technology into the design of new manufactured products and the factory floor automation that more efficiently produces those products. It ought to be, therefore, cause for grave concern that this critical industry is experiencing the worst conditions in its domestic market in a half a century. Orders are off by more than 55 percent since their peak in 1997. Import penetration has increased more than 40 percent in the past four years, due, in large part, to an overvalued U.S. dollar combined with our trade competitors' anti-competitive subsidies and currency distortions.

To add to our industry's problems, we have seen increased outsourcing by our largest U.S. customers. We have also seen lost sales as a result of unfair offset conditions that force companies to manufacture large portions of products, such as aircraft, in the purchasing country.

Leading analysts for the machine tool industry are projecting a 7 to 18 percent rebound in orders this year, but even if this projection is accurate, 2003 orders, in real terms, will still be weaker than they have been for 50 years.

Let me focus on one leading problem that all U.S. industry confronts. There is great concern across a wide variety of industries regarding the Chinese government's strategy of undervaluing their currency in order to garner exports and foreign investment. Last year, our bilateral trade deficit with China exceeded $103 billion. Indeed, China is accumulating foreign reserves at a rate of more than $6 billion per month. This is an uneven trade arrangement, and it is directly related to the distortion of the value of the two nations' currencies.

I will move ahead. What we call for is discussions with the Chinese to get them to remove the peg, which is now at an artificial rate of 8.2 to 1.

In spite of the hard times that we are facing, the United States is still the undisputed leader in developing new manufacturing technologies. Our products remain globally competitive in an increasingly hostile marketplace. However, as the struggle for survival continues, it is getting more and more difficult to maintain our lead. I call for a number of legislative improvements, such as enhancing and extending the 30 percent expensing allowance, as part of the President's economic-growth and jobs package. We also need a sound export policy with a replacement for the FSC, as has been mentioned by a number of the other——.

Chairman MANZULLO. How are you doing on time, Paul?

Mr. FREEDENBERG. I will be done in one more paragraph.

We also need export-control reform, which I know you are very familiar with, and I have seen Chinese factories stocked with European and Japanese machine tools doing what American machine tools could do if export controls were not so archaic and counterproductive. We also need fixing of the visa process. With these sensible reforms, we think our industry can continue to be a critical building block of America's continued prosperity and security, and with that, I will stop.

[Mr. Freedenberg's statement may be found in the appendix.]

Chairman MANZULLO. Thank you. Professor Czinkota? Okay. Go ahead.

STATEMENT OF MICHAEL R. CZINKOTA, PH.D., PROFESSOR OF INTERNATIONAL BUSINESS, GEORGETOWN UNIVERSITY, McDONOUGH SCHOOL OF BUSINESS

Mr. CZINKOTA. Thank you, Mr. Chairman, Representative Velazquez. Let me introduce my research assistant, Ms. Allison Haggar, who will show the different exhibits I am referring to.

Since 1975, the U.S. has been importing more than exporting, which led to a current account deficit. This exhibit shows you that there were always ups and downs, but since the early 1990s the growth of the deficit has been rapid and major.

Exhibit 2 shows the current account components. Merchandise trade is the largest component and contributes the most to the deficit.

Exhibit 3 shows that U.S. merchandise exports have been rising. However, since the mid-nineties these increases have been far below the growth in imports, and the gap has been widening rapidly.

Exhibit 4 breaks our merchandise trade down into its key components, which are manufactured goods, mineral fuels, and agricultural goods, and you can see that 81 percent of our merchandise exports are manufactured goods, and 84 percent of our imports are manufactured goods.

Exhibit 5 shows that since 1992 the growth of imports and manufactured goods has been much steeper than the growth in exports, leading to a widening manufactures trade deficit.

In Exhibit 6, you can see the top surplus and deficit countries in U.S. manufactures trade. We have some surpluses with the Netherlands, Australia, and Belgium, but they are dwarfed by the deficits with Mexico, Germany, Japan, and China. The 2002 bilateral trade deficit with China alone was $103 billion.

On a commodity basis, Exhibit 7 shows that in 2002 there were large U.S. surpluses in airplanes and parts manufactures, wooden manufactures, and chemicals, but they were far outweighed by deficits in furniture, toys, television, apparel. The largest deficit was in motor vehicles, with an imbalance of $111 billion.

Let me now provide a domestic and global historical context. In the mid–1800s, about 68 percent of U.S. employment was in the agricultural sector. Manufacturing accounted for 17 percent. By 2001, agriculture had declined to 1.5 percent of employment, and manufacturing, after some strong growth, had declined to 14.8 percent, below the levels of when it was first measured in the 1800s.

Exhibit 8 compares manufacturing employment in the United States, Germany, and Japan. German manufacturing declined by more than 13 percentage points during the past 30 years. In Japan, the decline was 6.5 percentage points. This sharply contrasts with U.S. employment changes. U.S. and Japanese manufacturing employment were almost equal in 1970 as a proportion of the economy. Since then, U.S. proportionate employment has been cut almost in half and is now more than five percentage points below Japan and almost 10 percentage points below Germany.

Manufacturing has been transferred to emerging economies. Exhibit 9 shows the proportion of manufacturing has typically doubled in countries like Malaysia, South Korea, Thailand, and Indonesia. That is it for the charts. Thank you.

Now, briefly, some key causes. The shifts have been greatly enhanced when manufacturers underexport. We only export 11 percent of GDP, compared to 34 percent of the European Union and 26 percent for China. Many U.S. firms have subsidiaries abroad to benefit from low labor costs or to comply with offset requirements.

In 2000, such import shipments from foreign affiliates were about 14 percent of our imports. Long-term supplier relationships lead to additional captive imports, and, of course, the subsidiaries of foreign firms in the U.S. account for another 20 percent of imports. What that all means is more than half of U.S. imports are done by U.S. corporations who prefer to source abroad rather than produce at home.

What are some of the practical implications? Long-term adjustment does little for the unemployed, who are overwhelmed at this time. We need U.S. manufacturers to export more and compete better with imports.

During trade negotiations, we always hear that other countries worry about any U.S. desire for more market share. However, I believe we have the right to argue for a special case. The United States continues to offer its consumptive power as an economic locomotive to the world. Our manufacturers have suffered the most drastic declines among all of the industrialized nations. When it comes to concessions, we already gave at the office.

When a manufacturing concern disappears, effects go beyond jobs. Replacement parts are more difficult to get or more expensive. For industries especially critical to the national welfare, this can be devastating in an emergency. How many of us would like to rely today on old friends abroad for the rapid resupply of crucial manufactures? Manufacturing migration also affects innovation and market responsiveness. When companies stay close to their market, they gain experience and boost performance. When production is removed from its primary market, such rapid response to market demands may be dulled, which leads to a decline in manufacturing competitiveness.

Chairman MANZULLO. How are you doing on time?

Mr. CZINKOTA. I will take less than a minute.

Important is also the consideration of what it does to clusters. Few companies can get together and form successful clusters, but it also works in reverse. If a few companies leave the cluster, then the entire industry can fall behind.

What can be done about all of this? Protectionism may sound like the easy answer, but it is not because it substitutes government judgment for market direction. Better to encourage existing market activities—trade promotion, for example, with a personal export officer—to make companies more successful.

There also needs to be more fusion of products, services, and financing with global networks. Just consider one example from the automotive industry. Air bags, the global positioning system, and the telephone in a car are no longer anything special, yet by bringing all of these components together, car manufacturers have developed an entire new level of passenger assistance which can independently notify emergency services. Such fusion of available products and networks is crucial to our competitiveness.

Finally, for too long there has been no linkage between governmental market-opening efforts and the benefits obtained by industry. Trade negotiations result in winners and losers, but there is no incentive for the winners to share their bounty. We need a program where private sector winners help pay for the cost of adjustment, a program that is an essential engine for further trade policy liberalization. After all, even free trade carries a price. Thank you, Mr. Chairman.

[Mr. Czinkota's statement may be found in the appendix.]

Chairman MANZULLO. Thank you, Professor. I saved the last witnesses who are actually involved in manufacturing for the last because I wanted them to hear everything that came before because I know they want to do a lot of comment on that.

David Sandy is vice president of MS Willett, Inc., in Cockeysville, Maryland. Is that Mr. Bartlett's district?

Mr. SANDY. That is correct.

Chairman MANZULLO. Okay. I look forward to your testimony. You might want to pull the mike up a little bit closer.

STATEMENT OF DAVID SANDY, VICE PRESIDENT, MS WILLETT, INC., COCKEYSVILLE, MARYLAND

Mr. SANDY. A little closer. Thank you. Good afternoon, Mr. Chairman, Ranking Member, and members of the Committee. Thank you for the opportunity to testify on behalf of my coworkers and the 2,000 member companies of the National Tool and Machining Association regarding the state of the U.S. manufacturing and tooling and machining industry.

First, I would like to thank you, Mr. Manzullo and Ms. Velazquez, for your enduring support of our industry. You have been strong proponents for NTMA, and you should be commended for it.

I work for MS Willett. We are a metal-working company that offers a unique blend of development, engineering, tooling and automation, and production services. Willett is family owned and is a tool-and-die, metal-stamping production company. We have two main focuses of business: production metal stampings and automated metal-stamping systems. The company designs and builds quality tools, dies, metal stampings, and assemblies. We are located in Cockeysville, Maryland, where we employ 120, and we do business all over the world.

Let me tell you a little bit about the National Tooling and Machining Association and the member companies. This will serve as a review for you, Mr. Chairman, but for the rest of us, nearly every manufacturing company in the country and in the world does business with our industry. The U.S. tooling and machining industry employs close to 450,000 people nationwide and has accounted for shipments in excess of $43 billion annually. The metal-working industry includes precision machinists, die makers, and mold makers, as well as tool-and-die designers. Without them, the mass production of manufactured goods would not be possible.

As we have heard today, the demise of U.S. manufacturing and, therefore, the tooling and machining industry is accelerating at an alarming rate. I will not expand on that; you can read about it in my written testimony.

One of the factors that is contributing to the problems of our industry is the exodus of American companies to other countries. For example, Black & Decker was once a $4 million-per-year account for Willett. Today, it is a fraction of that, due, in part, to their business movement to China, Eastern Europe, and Mexico. Black & Decker executives have recently told us that, in addition to closing their plant in Easton, Maryland, that their plant in Fayetteville, North Carolina, will also be closing its doors in the very near future. All of the production-stamping work which we did for Black & Decker will be gone within the next few months. We had a mutually successful relationship with Black & Decker for over 30 years. This is coming to an end because the work is going to be done in other countries, and, ironically, our plant is within five miles of their headquarters in Towson, Maryland.

I will give you another story of an account we lost to overseas competition. This was Fedders Rotorex. They were a good account for us. They manufactured compressors for air conditioners. We did about a million dollars a year in business with them, and they moved it all overseas.

A few of the things that are making it difficult for us to do business include the rising cost of health insurance. In 1999, our premiums were about $200,000 per year, and now they are over $350,000 per year in just a few years. The cost of capital equipment is high. In the last year, we have been able to invest $2 million. Overall economic conditions do not help. I do not know if it has been mentioned, but we have suffered miserably due to the steel tariffs.

Chairman MANZULLO. Mr. Sandy, could you move to the national defense portion of your testimony?

Mr. SANDY. Yes. As important as this industry is to the economic well being of the country, it is even more important to our national security. A healthy industry is an important component of defense-production capabilities. We are the companies that produce the plastic-injection molds that are used to build nuclear submarines, the ones that provide parts for our missile defense system, and the wheels and joints on airplanes, the parts used to make rifles for our infantry.

Increasingly, defense prime contractors are subcontracting parts and tooling for defense systems to Asia. This practice is not being monitored by the Department of Defense, and as a result, the military is becoming increasingly dependent on foreign sources to supply critical parts and systems for weapons. I applaud the Chairman and Ranking Member for recognizing this as a problem. Your request for an investigation by the General Accounting Office into this would prove to be an invaluable tool in fixing this situation.

We are aware of defense contractors subcontracting to foreign companies for precision machining jobs. Take, for example, the recent West Coast longshoremen's strike. Suppose a part was needed in a critical military weapon. The needed part would have been delayed somewhere off the coast of California. In this day and age, can we allow our country to be dependent on foreign nations to provide us with the parts we need to keep our weapons that protect our nation operational?

Another point I want to make is that the average age of our workers in the tooling and machining industry is over 50 years. As the current workforce grows older and fewer people are trained, America stands to lose an industry that is the bedrock of economic stability and wealth creation.

Chairman MANZULLO. Let me stop you right there.

Mr. SANDY. Yes.

[Mr. Sandy's statement may be found in the appendix.]

Chairman MANZULLO. I want to get in Mr. Anderberg because I do not want to have those bells ring on his time, or he will ring my bells. Okay? We can come back to you on some questions.

Our last witness is Eric Anderberg, who is my constituent from Rockford, Illinois. Eric, we look forward to your testimony.

STATEMENT OF ERIC ANDERBERG, GENERAL MANAGER, DIAL MACHINE, INC., ROCKFORD, ILLINOIS

Mr. ANDERBERG. Thank you, Mr. Chairman, and thank you, Ms. Velazquez, for the opportunity to be here today. It is truly an honor.

My name is Eric Anderberg. I am from Dial Machine, Rockford, Illinois. It is our family business. My father founded it 37 years ago. We are a contract machine shop. We make components for large, capital-equipment manufacturers in the United States. We rely on their success for our business. We supply construction and machine tool, aerospace, nuclear, and even, directly or indirectly, the military.

Business for Dial Machine has been terrible for the last four and a half years, from the beginning of the recession at the end of '98, and I believe that is when the machine tool industry started to go down. Currently, we employ around 40 people. That is 50 percent of what we used to employ back in 1998. The drop in sales that we have had corresponds with that.

As you know, the Department of Labor issued that there were 36,000 jobs lost in March in manufacturing, 2.2 million in three years. This has been very hard on Rockford, since nearly 30 percent of the employment in Rockford can be tied to manufacturing. In a community of 150,000 people, Rockford has lost over 5,000 manufacturing jobs in the last 18 months alone.

It has hit the community hard, and I would like to give a micro example of how I think the American economy will not fully recover without a manufacturing base. It has to do with a former employee that we used to have that we had to lay off two years ago because of lack of work.

Today, he works at a national, home-improvement box store in Rockford. He is in the service economy now. He makes $7 an hour versus the $15 an hour he used to make as a tool maker at Dial Machine. It is also part-time employment, so he has no benefits, and he works less than a 40-hour week. At Dial Machine, he had full benefits, health coverage, a 401(k), and full-time employment. I know that he and his wife purchased a house five years ago, and his wife is in the service industry as well. Both are struggling to make their ends meet and to make their payments.

So what is really the effect to the economy of these two people? My question is, how many vacations will they take? How many airline tickets will they buy? What hotels will they stay in? What type of insurance premiums can they afford? What about their retirement? What type of automobiles can they afford at these wages? What type of restaurants will they stay in? And what taxes, federal or state, if any, will they pay at these wages?

The trickle-down effect is clear, not only for the manufacturing industry but for the service economy as well, to the American economy. Take this one example and multiply it by the 2.2 million job losses we have had in manufacturing, and it is clear to see what the effect on our economy is, in aggregate, of the loss of our manufacturing base.

How did our manufacturing base get to this point? In the views of most small manufacturers, there are many to argue, but the main reason is the burden of government. This institution legislated the rules, the taxes, the regulations, the agencies, tort law, and the many other burdens that we, as manufacturers, live with in America. Government created a huge, fixed cost, a burden, that has been placed upon us, the small manufacturers, and that puts us at a disadvantage to compete globally at the offset, to be a manufacturer in the United States with a cost so high.

With that said, our government opened the door to unfettered, free international trade, but it has not been very free for small American manufacturers. Auction sheets come in weekly to our business of closed companies that just cannot make it anymore. Over the last five years, we have accumulated thousands of these fliers, and, talking to my father yesterday, three more came in the morning mail. If you walked in our office, you would see stacks of them in our storeroom from five years' accumulation.

Free trade has also allowed the multinationals to pull up their manufacturing facilities and leave and go to other countries like China. They have abandoned their suppliers and employees in our country for cheap production costs in countries like China that have no standards or high costs imposed upon their manufacturing base. Then they ship those products back to the United States under the guise of free trade. But can you really blame the multinationals for doing this? They are escaping the high fixed costs that our government has put upon them.

The multinationals, they have the resources to move their production overseas, but, unfortunately, small manufacturers do not, which brings me—I would like to talk about China. As you know, Mr. Chairman, I was on a trade mission to China, and I got back about a month ago. The purpose of the trade mission was to procure business for small manufacturers. I was very pessimistic. I still, after our visit, China being the largest threat to American manufacturing. But then I also see China as a huge opportunity.

What we learned over there is that China is going to spend $270 billion, American dollars, this year on infrastructure and capital improvements. A lot of that money is going to be spent outside Chinese borders for products from other countries. They will spend one and a half trillion in the next five years on capital infrastructure improvements. American business needs to get a piece of that action.

China is ready to buy. The Chinese government fully understands, better than our own government, the position that our economy is in. They are concerned mainly with two points, that either the door is going to close on the unfettered trade going from China to the United States or that their market is going to disappear for their products in the United States because nobody can afford their products anymore with our struggling economy. What we need to do is take advantage of this situation and have our government use its political leverage to force not only China but the other nations that have trade imbalances with us to trade with small manufacturers and the manufacturing base of this country.

I have many other points to talk about, but I will take your questions right now.

[Mr. Anderberg's statement may be found in the appendix.]

Chairman MANZULLO. Thank you very much for the testimony of everybody. There are two things that can be done immediately to help spur American manufacturing, and they are very easy. One is to have American manufacturers and the heads of the various service agencies and other agencies within the U.S. government follow the Berry Amendment and the Buy American Amendment.

We are embroiled now in a deep controversy with the Secretary of the Air Force, who signed a Berry waiver to allow Russian titanium to be placed in the engines and the bodies of our fighting machines, of our airplanes. Russia is exporting so much titanium to this country that they requested, and they received, an exemption under the GSP rules so that they do not have to pay the 15 percent tariff, which means Russia is sending more than 50 percent of the imported titanium into this country.

In addition, titanium, as you know, comes in what is called a "sponge". It is a chemical wash, and the sponge that comes into the United States, because there is not enough sponge manufactured domestically, is subject to a 15 percent tariff, which the three remaining titanium manufacturers have to pay. And then the Air Force tells us it is cheaper to buy from Russia. Of course, it is. They created it all. It is very cozy. The domestic guys have to pay a 15 percent tariff on the imported sponge for the basis of their titanium production, whereas the titanium ingots come completed from Russia, subject to no tariff whatsoever.

This has got to stop. We did it with the berets, a very hot hearing that lasted 4½ hours. I had to subpoena three generals to come in for that.

There is enough titanium in this country available at market prices to fulfill all of the needs. It has got to stop, and it has got to stop now. No more compromises. Just enforce the laws that are on the books. It is just that simple, and yet people do not want to do that. We have got to reform the Berry Amendment to give notice to affected parties, perhaps impose the Regulatory Flexibility Act, and to do away with these blanket waivers of the Berry Amendment. We can restart hundreds of jobs, thousands, by following existing law.

The second thing we can do is this. We have been working on this very hard. It is called "America's Jobs First." We have been trying to encourage American companies that set up manufacturing overseas to follow this very closely. Eric was over there. Don Metz was over there. All that the American companies have to do that are manufacturing overseas is simply buy their tools and dies and molds from American manufacturers. They can be almost competitive in price. The molds and tools and dies last a lot longer.

It is so simple. This is so simple, and we have been begging American companies overseas, begging them, please do not forget the guys you left behind, the same companies that come to us and ask us for free trade votes, and we say, "Just a second." This is so simple. But there are about five rings that separate the CEO of a company and the person in charge of purchasing. The latter is charged by the former to buy the best product at the cheapest possible price.

It would be so simple for General Electric in Shanghai, for Boeing doing business in China, for Caterpillar doing business in Japan and Mexico. All they have to do is buy the tools and dies and molds from the guys back here in the United States. Do you have any idea what that would do to restart manufacturing? It would be phenomenal. You would not have to change one trade law. You would not have to have one more program. You would not have to have anymore congressional hearings on this. But it is just some common sense that is lacking in corporate America, and we have begged and begged and begged the American companies.

So you know what we had to do with Eric? Tell them, Eric. On the trade mission, tell them who you had to go to.

Mr. ANDERBERG. We had to go to an outside help to—we were in touch with an American developer, who helped us set up this trade mission.

Chairman MANZULLO. With Chinese companies.

Mr. ANDERBERG. With Chinese companies.

Chairman MANZULLO. So what Eric has had to do is because the American manufacturers overseas would not give the guys any contracts for tools and dies and molds, the Chinese, as Eric said, recognize that, long-term, the manufacturing base in America being destroyed means they will not have a market for their products, and, as Eric said, the Chinese are thinking long term, and the Americans are not. So Eric has had to do it. He had to go the Chinese to get contracts from them because the American guys overseas said they are not interested in working with us.

Mr. ANDERBERG. And they are eager to do it.

Chairman MANZULLO. And the Chinese are eager to do this. This is really, if you look in the handout on manufacturing called "America's Jobs First," Mr. Aldonas is very much interested in this, and I just do not know how much more to get out the word. Jerry, you work with the manufacturers every day.

You know, the bottom line is not saving money. The bottom line is producing a product at a reasonable cost and having somebody around to buy it.

Anyway, those are two things that we can do right away. Ms. Velazquez.

Ms. VELAZQUEZ. I just would like to ask each one of you to tell me, beyond the titanium issue that I do not know how many small manufacturers would be impacted by, if you can point out to us one or two issues where the federal government has a role to play immediately to help the small manufacturing base. Mr. Anderberg?

Mr. ANDERBERG. Well, as I talked, the cost of government, the burdens; it is not going to be immediate. What we learned in China was that they fully understand the situation, and when we were in the city of Harbin, we met with provincial trading groups. Everything is government-owned in China.

Ms. VELAZQUEZ. So do you think that the trade policies that we adopted benefit you?

Mr. ANDERBERG. Well, there are export trade policies, and I am sure Mr. Freedenberg can attest to, that make it difficult for us to sell to China. For example, in Rockford, Ingersoll, we need to get visas for their engineers and their people to come to Rockford to okay millions of dollars worth of equipment sitting in their plant to ship to China, and our visas are not being issued. You know, what is the sense?

As for small manufacturers and small business, when I go back to Harbin, we signed a letter of intent with their trading group for $40 million that they intend to purchase from small manufacturing over the next year.

Ms. VELAZQUEZ. Thank you.

Mr. ANDERBERG. We need help. We need political pressure to make that happen.

Mr. SANDY. I think Congress needs to address the practices of the banking industry as it relates to withdrawing working-capital loans when asset-backed loans' value declines. I have heard more and more instances where this is happening to member companies in the NTMA.

In our own case, our lender has requested that we find another bank. They are in the process of upgrading their portfolio with less-risky loans. Banks are reluctant to extend working-capital loans to manufacturing companies such as ours. Asset-backed loans are the norm and increasingly more difficult to obtain due to the devalued market for used equipment, which is our principal asset. Thank you.

Ms. VELAZQUEZ. Thank you. Mister——.

Mr. FREEDENBERG. We talked about export controls. We talked about the visa problem, which is a major problem and is a deterrent to the Chinese doing business with us.

Chairman MANZULLO. Pull the mike closer to you, Paul.

Mr. FREEDENBERG. We also talked about what I discussed was the Chinese practice of undervaluing their currency. We are talking about the Chinese having wage advantages of 12-to-1 against us, and then they have a currency that is undervalued by 40 percent by some estimates. The U.S. Treasury entered into those types of discussions with the Japanese in the 1980s. It was highly successful. They could do the same sort of thing with the Chinese. The Chinese are pegging their currency. They can peg it wherever they want, although right now they are pegging it at an unreasonable level.

So those are the sorts of things, that plus expanding and extending the expensing provision, which is in the tax bill, would help.

Ms. VELAZQUEZ. Sir?

Mr. HARBOUR. Just briefly, my comment echoes the earlier comment about the availability of capital. There are a couple of companies that I am working with now—in fact, one that I have an equity interest in—and although they have solid balance sheets, they still are basically blacklisted by the banks in Detroit. This is a very common thing in the city of Detroit as certain manufacturing businesses have gone belly up, and the greater that list grows, the more they get blacklisted by the traditional lenders that the Department of Commerce spoke about earlier today.

So it is this death spiral that continues. The more of them that go out of business, the less likely it is that they can get any available capital to either grow or to recover from the situation that they are in. That is a very dire circumstance, I know, in our town, and it sounds like it is shared in other places.

Ms. VELAZQUEZ. Mr. Trumka?

Mr. TRUMKA. Yes. I agree with much of what has been said. We also think that Congress should pass a manufacturing tax credit to replace FSC immediately. We need help with health care, particularly prescription drugs. We think that no more trade laws patterned after NAFTA should be passed. We think that Congress can become very, very much more aggressive. They can initiate trade cases to enforce U.S. trade laws and to take aim at non-tariff barriers in trade with China, Japan, the EU, and elsewhere, and we think that you should strengthen the Buy American provisions for the Department of Defense and move aggressively in that direction.

Ms. VELAZQUEZ. Thank you.

Mr. JASINOWSKI. Agreeing with much of what has been said, I have tried to make up the items I would suggest, Congresswoman, that do not require in many cases legislation, although a few do. In the trade area, I would agree with Richard that we ought to focus on non-tariff barriers. That can be done right away. We can focus on reducing exchange export controls. Exchange rates with respect to China can be done without any legislation by the administration bringing sufficient attention, and, finally, an export promotion. All of those things can be done without legislation and can be done immediately.

On the growth front, I agree with the bank lending. We have been arguing with the Federal Reserve, you have got to reduce the regulatory pressure you are now putting on banks that keeps them from making loans to small companies. Expensing, extended, as Paul suggested. The current pension rate for calculating pensions can be done by executive fiat by the Department of Treasury. It now is much too high relative to what are the realistic rates, and that would cause a huge inflow of capital into business, and a tax credit or some kind of thing that would deal with FSC, as Richard suggested.

On the cost side, a number of regulatory measures could be streamlined and not done. Asbestos legislation ought to be passed quickly, and I think that a prescription drug benefit on health care.

And, finally, since you asked the question, Congresswoman, I would say that we would support organizing the budget priorities a bit differently than the administration to maintain some MEP and certainly to put additional expenditures into export promotion.

Ms. VELAZQUEZ. Thank you.

Mr. CZINKOTA. In addition to some of the items mentioned, I would have three watch words: communication, streamlining, and linkage. Communication of long-term issues, such as in a new world of uncertainty, how does that affect transnational border flows? Isn't it better if we have things at home? What is the effect of migration of manufacturing on innovation in processes, which is quite negative, in the long term? So communicating that.

Secondly, streamlining processes, such as export promotion, export controls. There are lots of things which can be done there with limited funds.

And, finally, link negotiation benefits with support for trade adjustment. They should not be separate. If somebody gains very much through such negotiations, then they should be able to help out with some of the adjustment costs.

Ms. VELAZQUEZ. Thank you. Thank you, Mr. Chairman.

Chairman MANZULLO. You might be interested, Mr. Trumka. There is a bill called the Crane-Rangel-Manzullo Bill that deals with FSC, that encourages manufacturing to stay at home in order to get that credit, and we would be delighted to work with you. Jerry mentioned about a half a dozen items. I mentioned a couple. There are probably 10 action items that we could put together just as a result of this hearing that could be implemented almost immediately through the folks that are here. Go ahead.

Mr. JASINOWSKI. Mr. Chairman, I just wanted to respond to your initiatives and say, although we do not have an active program in support of the Berry Amendment, the way you described it with respect to the unfair trade practices that allowed the Russians to use the titanium is something we would like to look at and look at any situation where there is an unfair playing field with respect to American products that are associated with national security.

Chairman MANZULLO. I really appreciate that. Thank you. That is great. Mr. Trumka?

Mr. TRUMKA. I would just like to say, Mr. Chairman, that we look forward to working with this Committee and all of the members of it to try to reinvigorate American manufacturing.

If I could, could I just make one correction for the record? One of your witnesses said there was a longshore strike. It was not a strike; it was an employer lockout. I want to make sure that the record is accurate.

Chairman MANZULLO. Okay, okay. I appreciate that. Any other comments on that?

Mr. JASINOWSKI. One other comment, Mr. Chairman, which I would just ask for the record. We have a breakdown that shows that there are 71,000 manufacturing plants associated with this Committee and how many plants are in each state, and we have broken out the unemployment loss by state of manufacturing jobs. In the case of your state, unfortunately, it is 80,000. I would like that for the record, and maybe your staff might consider sharing it with the Committee. I do think it brings it down to the district level in a very useful way.

Chairman MANZULLO. Let me reserve my ruling on placing the whole thing in the record because of the size of it.

Mr. JASINOWSKI. I agree, Mr. Chairman. I am more interested in the Committee members seeing the specific——.

Chairman MANZULLO. I will make sure that every member personally gets a copy of it.

Professor Czinkota, I have a question to ask you. Back to the charts, it would be chart number—I feel like this guy on "Johnny Carson." Do you remember with the charts, how to get to the used car lot? Exhibit 7. It does not make much difference which sector you have there. Can you see that?

Mr. CZINKOTA. Yes, sir. I am unclear on the question, sir.

Chairman MANZULLO. I have not asked it yet.

[Laughter.]

Chairman MANZULLO. You can always tell the professors. You know, they are always waiting on the students.

Professor, do you know of any available economic tools in the private sector or in the public sector whereby you can evaluate how much of a particular export by the United States represents foreign products?

Mr. CZINKOTA. In terms of content?

Chairman MANZULLO. In terms of content.

Mr. CZINKOTA. Foreign content?

Chairman MANZULLO. Right.

Mr. CZINKOTA. Well, the Bureau of Economic Analysis does some data collection but very, very limited.

Chairman MANZULLO. Okay. It is not there.

Mr. CZINKOTA. There is really no tool that I am aware of, apart from the anecdotal evidence which is supplied by some individual manufacturers. For example, Boeing has done that in the past on occasion to talk about local content, foreign content. But we do not have an organized data-collection presence in that area that I am aware of.

Chairman MANZULLO. Okay. It would be interesting to see that because the trade deficit may even be greater than what it is because this is what I call the hollowing out of manufacturing. What I am seeing is there is more and more assembling going on with all of these foreign parts coming in, put together in America, placed on a product, and then the product is exported, and you have to ask yourself how much of that is in there.

The other question I wanted to ask is, in terms of procurement, many people think, and I have a tendency to agree with it, that the 200 to 250 billion dollars in U.S. procurement that we have in the United States, what we pay for out of taxpayer funds for use by the government should serve as a hedge or a way to level the playing field with regard to cheap imports. Imports are cheap. I am not demeaning them; it is just that they are cheaper in price on it. Do you know of any tool, public or private, that can measure the amount of foreign procurement that is purchased by American companies and the amount of American procurement that is purchased by foreign companies?

Mr. CZINKOTA. There are some data on that collected by the OECD in connection with the Government Procurement Code, especially by those who are unhappy about procurement levels, and they then collect certain data to point out shortcomings of the procurement code. To your first question, there are requirements, for example, if a firm seeks Ex-Im Bank funding, to have a certain degree of domestic content, and if the foreign content exceeds the limits, then there will be no such funding. So in that sense, companies have to self-declare what the proportion is. But, again, in terms of a data base where we could just seek recourse to and print out the numbers, no, we do not have that.

Chairman MANZULLO. I raised this issue with the USTR's office because there is a movement to open up U.S. procurement to other countries via the new, proposed free trade agreements. Lacking quantitative data as to who is actually winning under these circumstances, we have got to sit back and take a look, is that what we really want to do? Obviously, we can contract with China or Mexico to build 100 percent of our defense a lot cheaper than what we could do in America. Is that really what we want to do?

So that is critical data, and the reason it is done in the free trade agreements—I voted for every free trade agreement. I really believe in that. The opposite of that is the ugly head of protectionism. But every free trade agreement should be based upon data that can be substantiated, and I am extremely concerned that any new free trade agreement open the doors of more procurement from the United States than what we have now.

If you take a look, for example, at the Buy American Act, that only requires, with the exception of the application of the Berry Amendment regarding strategic metals, that only requires that the Defense Department can buy something, but it only has to have 50.1 percent American content. I think we should consider raising that to 75 percent. It is not protectionism. What it does, it ensures the domestic industrial base that we have in this country.

The Berry Amendment itself, as you take a look at it and look at the purpose of it, we see, again, on those engines that have Russian titanium, they have Japanese nickel drive shafts. And then the more we continue this inquiry with regard to the waiver granted by the Department of Air Force, then we see this tremendous amount of hollowing out that is going on in manufacturing. So we need somehow to find out the data, and if that data were there on how much of foreign materials are going in, it might be even more shocking than what it is.

We have a little bit of time here, and I know we have been pressed, but I would like to leave this open, if any of you have any questions you want to ask of each other or make any concluding statements.

Okay. Thank you very much for your testimony. Jerry would like to talk to you—maybe we can come back in a couple of weeks—

about that Barry Amendment, bring you up to date on what is going on there.

Mr. JASINOWSKI. We would like to be informed. Thank you very much.

Chairman MANZULLO. And, again, thank you all for coming, especially those that traveled great distances to come here. I appreciate it very much. Thank you.

[Whereupon, at 5:15 p.m., the Committee was adjourned.]

House Committee on Small Business

"Will We Have An Economic Recovery Without A Strong U.S. Manufacturing Base?"

April 9, 2003

Opening Statement of Committee Chairman Don Manzullo

Good afternoon and welcome to this hearing of the Committee on Small Business. I especially welcome those who have come some distance to participate. Today, we're going to talk about manufacturing. Most Americans don't fully realize the importance of manufacturing. The message I want to get across today is that manufacturing matters to everyone in a big, big way.

Let me be blunt about why we're having this hearing and why we will have more to follow. Our domestic manufacturing base is being hollowed out right before our very eyes. And it's other American companies that are doing it. We are fast becoming a nation of assemblers and even that may disappear soon.

Most Americans, including many in Congress, brush off manufacturing as being passé. Take a look around you. It's happening in the service sector, too. The February 3rd edition of BusinessWeek had this on the cover: "Is Your JOB Next? A new round of globalization is sending upscale jobs offshore. They include chip design, engineering, basic research – even financial analysis. Can America lose these jobs and still prosper?" At the rate we're going, 3.3 million jobs will move overseas by 2015.

The title in today's Washington Times editorial says, "More troubling jobless news." We've lost over 1.4 million mostly-manufacturing jobs since 9/11. Even the service industry is short 200,000 jobs since 9/11. Wake up, folks! If we keep losing our manufacturing jobs, we won't have much of a service sector to worry about.

Once our manufacturing base disappears so do other economic sectors. Engineers, your typical, high-paying, white-collar job, are moving overseas. Boeing laid off 5,000 engineers in favor of lower cost Russian engineers. GM and Ford are forcing their suppliers to move overseas to keep contracts. Those businesses will be hiring their engineers from overseas. Guess what? Many engineering jobs exist because of manufacturing.

Here are some facts and they are not good:

Two-thirds of reemployed manufacturing workers earn an average of 12% less on their new job. One-quarter of those earn less than 30% or more.

Foreclosures hit a record high last quarter in places hardest hit by the manufacturing downturn, especially the Midwest and Southeast, in part because the manufacturing sector has lost more jobs during the latest economic downturn than any other sector."

On March 31st, Fortune reported that 10% of all US spending is consumed on cars and related services. How many cars and other related services can 2 million unemployed people buy?

These are just two examples of how our economy is integrated and rests on the health of the manufacturing industry.

From July 2000 through March 2003, we have lost over 2.2 million manufacturing jobs, or nearly 12 percent. Manufacturing employment has now contracted for 32 straight months.

On April 1, 2003, the Purchase Managers Index (PMI) was set at 46.2 percent, its lowest reading since November 2001. Analysts had predicted the index would fall to 49. Any number below 50 suggests that manufacturing is failing to grow.

Orders to U.S. factories fell 1.5 percent in February, the worst showing in five months.

According to an April 2nd Census report on Manufacturers' Shipments for February, new orders declined $4.9 billion, shipments were down $5.0 billion, and unfilled orders decreased $1.1 billion, down six consecutive months.

On top of that, GM and Ford announced double-digit cutbacks in production that means less work and even more layoffs for those supporting the auto industry. The tool and die industry is heavily dependent on new product introduction in the automotive industry, absorbing nearly 50 percent of tooling.

One of the silent issues driving this train is the tremendous pressure Wall Street puts on Corporate America. I think if we look behind the layers we will find companies, forced to drive up stock values to make their quarterly estimates, doing whatever they have to do to drive down costs and increase margins. Don't get me wrong – that is the essence of capitalism. The problem comes when they do this with tunnel vision thinking that such decisions are made in a vacuum without having monstrous effects on everyday America.

A second problem we face is having no statistics on how much domestic content is actually in supposedly US-manufactured goods. And no one is being held accountable for it. Today, manufactured doesn't necessarily mean made in the US. All it has to be is assembled here. If that's what's becoming of our industrial base, we're in big trouble.

My office has put together a presentation that outlines ten major factors working against small manufacturers, who are the core of our industrial base. You will see that they are fighting against high regulatory and tax burdens, overvaluation of the dollar, , and low-cost labor, among other things. For example, Chinese hourly compensation costs for toolmakers and tool designers are one-twelfth of those in the US, and those in Taiwan are one-third.

Did you know that 60% of this nation's 43 million uninsured are small business owners, their employees and families?

In my district, Rockford is home to the heaviest per capita concentration of machine tool and die companies in the nation. The Washington Post calls Rockford "a barometer in the heartland." That was the headline of a three-page story in the Post's March 25, 2001 edition. The sub-headline says Rockford holds "clues to shifts in the U.S. economic climate." Rockford was a national predictor in the early 1980s, when its unemployment led the nation at 25 percent. It remains a predictor today, still with one of the highest unemployment rates in the nation at 10.9 percent in February 2003 (the national average is 5.8 percent). Overall, my district is experiencing the highest unemployment since the recession of 1992 and 1993. Since February 2000, Rockford-area factories have shed 9,400 jobs, nearly 19 percent of the manufacturing work force.

This is not just a problem facing Rockford-based manufacturers. The problems of Rockford are representative of the crises in manufacturing across this nation. We must fix it.

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House Committee on Small Business

"Will We Have An Economic Recovery Without A Strong U.S. Manufacturing Base?"

April 9, 2003

Opening Statement of Committee Ranking Member Nydia Velazquez

Thank you, Mr. Chairman.

Today, our nation continues to struggle. The economy is losing jobs faster than it can create them, which is bad news for the 8.4 million unemployed Americans, many who have been out of work for more than 6 months.

The manufacturing sector has always been one of the most vibrant and innovative in the American economy. Made up largely of small and medium-sized firms, U.S. manufacturing accounts for about two-thirds of private research and development expenditures and almost 20 percent of our GDP. It is a major source of good jobs for three-quarters of American workers, and is the largest sector in 13 states.

It is unfortunate that the manufacturing sector – like the American economy as a whole – is suffering. As the economy slipped into recession in 2001, business investment and exports dropped significantly. This plunge directly affected the manufacturing industry. There have been 31 consecutive months of employment losses in manufacturing – for a total of about 2.4 million jobs – bringing this critical sector to its lowest level in 40 years.

But it is not just one issue plaguing this important sector – there are many. First, the business climate is racked by uncertainty. The war in Iraq and its effect on world oil suppliers, combined with consumer apprehension and a volatile stock market have caused uneasiness about the future. The manufacturing sector is certainly feeling this trepidation.

Perhaps more importantly, though, the manufacturing sector is so weak because of a series of faulty policies put forth by the current administration, which has done nothing to ease the situation. In fact, these policies have only made things worse.

Health care is a problem for many Americans, especially those who work for a small business. Rising health care costs have taken a special toll on manufacturers. Health care is a major factor in undermining the competitiveness of manufacturers in the global marketplace.

The Bush administration's trade policies have done little to help manufacturers gain back their competitive edge. The liberalizing of trade agreements and policies such as Fast Track have caused domestic producers to lose market share to foreign competitors. In addition, the large U.S. trade deficit in manufactured goods – driven, in part, by an overvalued dollar – has been responsible for massive job dislocation and plant closings across the country.

The strong dollar is pricing small domestic producers out of international markets while creating windfalls for companies that can move overseas and produce goods for sales in the United States.

And that is exactly what is happening. Many American firms are moving their factories – and their jobs – overseas because they reap the benefits under U.S. tax policy. The current tax code also gives billions in subsidies to companies that transplant their factories, outsource production, and then hide profits in offshore tax shelters.

Once again, the administration's policies help big business at the expense of small business. The Bush administration's energy policy – or lack of one – is another example of this. The constant energy price hikes are hitting manufacturers especially hard. It has been forecasted that until energy supplies increase and prices stabilize, economic growth will be elusive.

Not only are we dealing with bad policies, we are also dealing with bad priorities. In the latest FY 2004 budget, President Bush slashed many small business programs, including those to help manufacturers. The Manufacturing Extension Program (MEP) – a $100 million program – will be closed out next year.

The Small Business Administration, which provides the only real source of trade assistance for small business, has seen its funding continue to shrink. The SBA's Export Working Capital Program, is facing cuts in the FY 2004 budget. Given the dismal economic outlook, how can we expect manufacturers to bounce back without giving them the right tools?

That is why we are here today. Manufacturers are the cornerstone of the American economy – they have, in large part, made the U.S. a world leader and economic powerhouse. But the current climate – both at home and overseas – puts a damper on any kind of recovery for this sector. In addition, the trade, tax, budget and energy policies of this administration has only compounded the problems of the manufacturing industry.

What we need is change. Without change in these policies and the recognition that manufacturing can be a big player in our economic recovery, we will see this downturn go on. But if we design new policies and give manufacturers the assistance they need, this nation's economic recovery will no longer be so far out of reach.

Thank you.

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Statement by Representative Steve King
Before the House Committee on Small Business
April 9, 2003

I wish to thank Chairman Manzullo and Ranking Member Velazquez for holding this important hearing to explore the problems facing U.S. manufacturers and ways that Congress can assist economic recovery.

My personal business experience of 28 years mirrors that of many in our nation. When I was first starting my business, I naively thought that producing a quality product at a competitive price was all that I needed to succeed. I borrowed 100 percent and bought an old bulldozer and went to work. I quickly learned that I'd rather be lucky than good. There was always a bureaucrat standing there with his hand out looking for his share of the profits. I came to realize that 43 separate agencies regulated my business. There was absolutely no way anyone could operate in compliance with all of their regulations at any given time. Our government has produced a punishing series of roadblocks to entrepreneurship. I favor reforms that will permanently improve the legal, regulatory, health care and retirement systems, while lowering the anti-growth and costly job-destroying burdens the government currently imposes.

I am concerned that since the economic slow-down began in July of 2000, Iowa has dropped from 261,700 manufacturing jobs to 244,700 in December of 2003, a decrease of 17,000 jobs or 6 percent. According to the National Association of Manufacturers, nationwide manufacturing has shed 2 million jobs in 2 years. By far, the largest job losses in the economic slow-down have been in the manufacturing sector. There have been 32 consecutive months of job loss in manufacturing, including 16,000 in January. In contrast, the non-manufacturing sector has witnessed signs of recovery and has since added nearly a million within the past year. There were 18.5 million people working in manufacturing before the recession; today there are 16.5 million.

Small and large manufacturing is challenged in one the most intense global competition markets in history which makes it virtually impossible to raise prices even as costs continue to rise for many reasons including actions by government or its failure to act. On the domestic front cost obstacles of health care inflation, and regulatory and legal burdens to volatile energy prices have combined with slow economic growth domestically and around the world, a persistently overvalued dollar, terrorism and geopolitical uncertainty.

Even as the nation has been focused on the war with Iraq, the economy is of central importance right now and actions must be taken to steer our course back on track. There are several initiatives that would assist in rejuvenating manufacturing, such as a tax policy that enhances economic growth and encourages productivity through technology and investment incentives. Additionally, trade policy that levels the global playing field for American manufacturers by opening markets, lowering tariffs, modernizing export controls and sanctions policies, enforcing trade laws and achieving market driven currency valuations. To this end, I commend Chairman Manzullo for authoring a letter to U.S. Trade Representative Zoellick asking for careful consideration of proposals that assist domestic manufacturers. As we consider the Energy Policy Act of 2003 (H.R. 6), it is my hope that a national energy policy will bring sustainable economic growth in manufacturing, with emphasis on reliable supply at affordable prices, conservation, increased efficiency, strengthened infrastructure, and investments in new technologies.

Again, I thank the Chairman and Ranking member for holding this hearing . As we all agree that manufacturing has been and will continue to be vital to our economy and nation, I look forward to working with the Committee on future initiatives to revitalize and promote growth.

Prepared Testimony of
Under Secretary of Commerce for International Trade
Grant D. Aldonas
Before the House Committee on Small Business

April 9, 2003

Thank you, Chairman Manzullo, Congresswoman Velazquez, and Members of the Committee for the opportunity to join you in a discussion of the challenges facing American manufacturers. Mr. Chairman, under your leadership, the Committee has proved a consistent advocate for American small businesses, particularly the many small and medium-sized firms that represent the heart of American manufacturing.

President Bush, Secretary Evans, and I believe in the importance of America's small and medium sized enterprises to the health of the American economy and to our future. Our mandate at the Department of Commerce and the International Trade Administration (ITA), which I lead, is to create an environment in which all enterprises, including small businesses and entrepreneurs, can flourish. In order to achieve that, one hundred percent of our resources are directed toward ensuring that America's small and mid-sized manufacturers can compete and win in the global economy.

Competitiveness of American Manufacturing

Mr. Chairman, let me begin with a point on which I know this Administration and members of the Small Business Committee agree – that the manufacturing sector in America is the foundation on which much of the rest of our economy is built. Census Bureau statistics reflect that fact. Manufacturing generates 16 percent of the national gross domestic product and directly employs 18 million Americans, 14 percent of all workers.

What those statistics do not capture, however, is the extent to which manufacturing drives much of the rest of the economy. Much is made of the rise of the service sector over the last twenty years. It is an area of undeniable strength and competitive advantage in the U.S. economy. But, we should not overlook the fact that much of the growth in the service sector has come from outsourcing functions that American manufacturers used to perform for themselves.

Let me give you a concrete example from my own experience. While in private practice, I had the privilege of advising a number of the major American high-tech manufacturers. In the mid- to late- 1980s, virtually every one of those enterprises handled all of their own shipping and customs brokerage. With that went a variety of administrative and compliance costs. Today, we see major firms like UPS provide those services at a much lower cost. The ability of a UPS to offer those logistical services on a scale no manufacturing firm could match helped U.S. manufacturers and exporters to reduce their costs significantly.

What it also meant was that jobs and statistics that used to show up in the manufacturing column in our national income accounts now show up under the heading of services. For our present discussion, we should draw two practical points from that restructuring of the U.S. economy over the past two decades. The first is that the process of restructuring has strengthened our ability to compete worldwide in both manufacturing and services. The efficiencies gained through that restructuring represent hard won results that continue to drive increases in productivity, which ultimately drives our rising standard of living.

The second point we should understand is who our service industries serve – they serve our manufacturing base, as well as other sectors of our economy, and in the absence of a strong manufacturing sector, our service industries would suffer as well. The fact that recent slowdowns in the services sector mirrored similar slowdowns in manufacturing activity is no coincidence. In short, manufacturing activity drives economic growth beyond the 16 percent of GDP reflected in Census Bureau statistics, which underscores the importance of understanding the competitive challenges our manufacturing sector faces today in global markets.

Now, what is undeniable and what brings us together today is the fact that American manufacturing is facing one of the most significant competitive challenges it has faced. The recession in manufacturing that President Bush inherited began at least 18 months before the recession overtook the economy as a whole. The sharp decline in economic growth in Asia following the Asian financial crisis meant a sharp fall in demand for the capital goods that represent areas of U.S. manufacturing excellence. The 40 percent appreciation in the dollar from 1997 to 2001 reflected the underlying strength of the U.S. economy, but also put American manufacturers under increasing pressure both in terms of the competitiveness of their exports and in terms of the competition they faced here at home. Indeed, the fact that Europe and Japan trailed us into the recession and still have yet to recover (e.g., European economic growth in 2002, without the contribution of a growing British economy, was 0.3 percent) has meant a stiff challenge for American manufacturers that relied on those markets for a share of their own growth.

Does the fact that our manufacturing sector faces those challenges mean that this important sector of the economy is unable to compete in world markets? In my view, the World Economic Forum's 2002 *Global Competitiveness Report* answers that question directly. The report named the United States as the most competitive economy in the world. The report highlighted America's significant levels of research and development, innovative business community, strong venture capital markets, and commitment to innovation and technological advancement.

Each and every one of the factors cited by the World Economic Forum's report underscores the basic strength of our manufacturing sector. Throughout our history, the manufacturing sector has seized opportunity and pursued the latest science. In fact, manufacturing accounts for approximately two-thirds of private research and development expenditures. This has resulted in sustained technological innovations and tremendous productivity gains, which in turn have fueled higher wages, living standards, and economic growth.

That record of innovation, both in products and manufacturing processes, and in business and financial management, has yielded continuing gains in productivity. With rising productivity, the business pages of our newspapers generally focus on jobs lost and take that as a weakness in American manufacturing. What that overlooks is that productivity gains are the most fundamental indicator of a nation's economic health.

Let's take steel, for example, which is an industry that has received a great deal of attention as a result of the President's efforts to ensure that we eliminate a 50-year legacy of government distortion in the marketplace that propped up an enormous amount of excess steelmaking capacity worldwide. There is no doubt that the steel industry has undergone considerable change over the last 20 years, as much due to domestic competition from innovative mini-mills domestically as from subsidized competition from abroad. That restructuring in response to competition is ongoing today.

Again, much of the focus is on the loss of jobs in the industry. Employment in the steel industry in 1972 was 568, 000. By 2002, this past year, employment in the industry had fallen to 188,000 or about one-third of the number employed 30 years ago. The President has shown leadership in encouraging restructuring within our industry, while at the same time, addressing those foreign government practices that precipitated much of the crisis in the U.S. steel industry. This Administration has also worked in concert with Congress to reinforce the worker adjustment programs that benefit those employed in the steel industry and those whose pensions continue to depend on the industry's health.

There is one fact, however, that we should not overlook -- and it is a fact that foreshadows the revival in American steel and American manufacturing generally. Today, with less than one-third of the personnel it employed 20 years ago, the American steel industry produces more steel than it ever has in the past. What the American steel industry has done, despite all of the criticism to the contrary, is increase its productivity by 132 percent over the past 30 years, which is exactly on par with the increase in productivity (134 percent) in the rest of American manufacturing. That fact alone rebuts much of the criticism leveled at the U.S. steel industry on the ground that it has not responded to the challenges it faces in global markets.

It also rebuts those who have written off the American steel industry as an industry of the past. Frankly, based on my understanding of the ongoing changes in the industry and the continuing drive to lower costs, the American steel industry is meeting the commercial challenges it faces. The steel industry that comes out of this current period will be stronger, healthier, and very much a part of America's economic future.

The reason I focus on steel is not because it has drawn so much attention over the past two years, and I know this is a particular focus of yours, Mr. Chairman. I focus on steel to underscore the fundamental point that steel is very much a part of the American manufacturing sector. Indeed, steel lies at the heart of American manufacturing.

I say that to emphasize that the challenges facing the steel industry are precisely the challenges facing the rest of the manufacturing sector in America. My impression is that whatever disagreements you may find within the manufacturing sector regarding the relief the President granted under section 201, those differences are small in comparison to the near unanimity among all U.S. manufacturers about the common challenges they face in today's global markets.

It is those common concerns that I intend to address with the remainder of my testimony. Before I do, however, I want to add one further point that adds to the urgency of addressing the competitive challenges our manufacturers face. The President's and Secretary Evans' interest in manufacturing is not based on economics alone.

Today, as we meet, you can turn on any television and watch the men and women of our armed forces liberate the Iraqi people. Watching our forces topple (literally, based on the latest press reports of U.S. soldiers helping Iraqi citizens tear down statutes of Saddam Hussein) the horrible regime in Baghdad should drive home the point that our safety and security - and in many instances the safety and security of people half a world away - depend on the ingenuity, innovation, and success of America's manufacturers. That is true of military hardware and advances in technology on display in Iraq. It is also true of the less immediately visible advances in biotechnology that help combat bioterrorism or the diagnostic and surveillance equipment that will help ensure both our safety here at home while allowing us to maintain an open economy on which our strength depends.

For President Bush, Manufacturing Matters

With that as context, let me assure you that President Bush and the Secretary know, as you do, that manufacturing matters. It matters to our economic health, job creation, continued growth, and our security. That is why the President's economic and growth program focuses on issues of particular importance to American manufacturers.

First and foremost, the President directly confronted the recession he inherited upon taking office. Beginning in the spring of 2000, we experienced several economic setbacks. The equity markets collapsed, and an energy crisis gripped the west. Business investment dropped off sharply in response to an excess capacity bubble, unemployment rose, and corporate scandals began to cast a dark shadow over the financial sector. And of course, there were the events of September 11th, from which we are continuing to recover.

In the face of these challenges, the President made economic growth his highest domestic priority. In 2001, President Bush successfully pressed for and passed the largest tax cut in more than two decades, which resulted in sustained spending by American consumers. In addition, our nation's manufacturers asked that we lower the cost of reinvesting in their businesses and conducting research and development. The President delivered on that request. He produced a sharp cut in tax rates, and asked Congress to accelerate the remainder of those cuts to stimulate business investment.

Because of this swift action, the economy grew by a rate of almost three percent last year and, nationwide, incomes are rising faster than inflation. Interest rates are lower than they have been in 37 years, allowing Americans to refinance their homes and adding billions to their pocketbooks and to the economy. Home ownership - a central part of the American dream - rose to 68 percent. In addition, productivity rose 4.8 percent in 2002, the largest increase since 1950.

Now, the President is intent on fostering increasing levels of growth in the business community. He has asked Congress to accelerate the remainder of his 2001 tax cuts to stimulate business investment. He has asked Congress to eliminate the double-taxation of corporate income, which will free an estimated $20 billion for our economy and make business investment a far more attractive proposition. And he has asked Congress to increase expensing limits for small businesses. Mr. Chairman, as both you and the President know, small businesses serve as the backbone of our economy. They need an increase in the expensing allowance from $25,000 to $75,000.

Critics of the President's plan have fostered the view that it focuses solely on business interests. That, of course, is completely false. You do not have to look any further than the innovative savings proposals presented with the President's budget to know that the President has focused on tax reforms and tax simplification that would directly benefit individuals at all levels of the U.S. economy.

That said, to the extent that a number of reforms proposed by the President directly address concerns registered by American manufacturers, you have to ask why the critics object. For example, the American economy is made up of approximately two-thirds consumer spending and one-third business investment. While consumer spending has remained strong over the last two years, business investment has lagged. It has become increasingly difficult for American manufacturers to obtain capital for expansion and productivity enhancing investments that will allow them to compete globally. Frankly, that should come as no surprise to this committee, which I am sure, understands that taxing business income at an effective rate of 70 percent, due to taxation of such income once when it is earned and again when it is distributed to shareholders, is a huge disincentive to invest in American manufacturing.

In short the President's economic and growth proposals focus on that sector of the economy that most needs a push at this point - business investment. And it does so in ways that addresses many of the chief complaints of American manufacturers regarding their cost of capital, which directly influences their ability to raise their productivity and their ability to compete globally.

I know that the House passed the President's economic package in its entirety. For the benefit of American manufacturers, America needs you to press forward with these important reforms in the final package. For America's countless small businesses and manufacturers, it will provide much needed incentive for capital formation and investment, while also empowering businesses to make decisions based in economics and not the tax code.

We also need your continued support for the other strand of the President's economic program – expanding trade. President Bush has fostered a two-pronged approach to trade that serves our manufacturer's best interests. The first prong involved obtaining Trade Promotion Authority so that the President could reassert America's leadership in international trade negotiations.

The President has acted on his promises in that regard. In the first two years of his Administration, the President has seen the successful launch of a new round of global trade talks in the World Trade Organization. To further the interests of our manufacturers, the President has tabled a proposai for lowering tariffs on industrial goods that would end the inequities in the current trade regime by ensuring that all WTO members eliminate tariffs on all manufactured goods. Currently, the average U.S. tariff on such products is less than 2 percent, while the average tariffs in most of the rest of the world are in double digits, many times the U.S. rate. The President's proposal would eliminate that imbalance and open new markets for American manufactures.

The President has completed long-delayed free trade agreements with Chile and Singapore. He has reinvigorated talks designed to complete a hemisphere-wide Free Trade Agreement of the Americas. And, he has launched new talks with our Central American trading partners, Morocco, Australia, and the members of the South African Customs Union. These last three can serve as particularly important models of how trade and economic development policies can work together to produce a higher standard of living for the developing world, as well as new markets for our manufacturers.

The second prong of the President's strategy is one I am particularly proud of because it involves the many fine colleagues I have the pleasure to work with at the Commerce Department and other trade promotion agencies, such as the Export-Import Bank, the Overseas Private Investment Corporation, the Trade and Development Agency, and the international office of the Small Business Administration.

At the outset of the Administration, we launched a benchmarking study of how to improve our trade promotion. That led to the publication of a National Export Strategy in 2002, with 65 separate recommendations for improvement in our processes. I am pleased to report that we are providing the Committee with our first follow-up report on implementation of the recommendations and to allow you to measure that progress on behalf of America's manufacturers.

This effort has involved the dedication of much of the 2400 employees of the International Trade Administration, as well as a large number of colleagues in other trade promotion agencies. None of that would have been possible without the consistent focus of the President and Secretary Evans. And, none of that would have been possible without the consistent support of the Small Business Committee throughout the process.

Many of those efforts have paid off in particular for small and medium-sized exporters. For example, the President's e-government program included an "International Trade Process

Streamlining Initiative." Under that initiative, we will work to enhance Export.gov, the government's existing online portal for small business export assistance information. We intend to create a seamless environment for small and medium-sized enterprises to research markets, gather trade leads, and conduct a majority of their export transactions online. That electronic backbone for our exporters in the manufacturing sector will provide more timely and accurate export information and result in cost savings for U.S. businesses by reducing the amount of time they spend trying to get information and filling out applications and forms.

The President's Manufacturing Agenda - Addressing the Competitive Challenges Facing American Manufacturing

While I believe that the President's economic plan and our ongoing initiatives at the Department will address many of the immediate needs of our nation's manufacturers, I also know that President Bush and Secretary Evans are not satisfied even with the strong record of economic growth the economy has registered despite the multiple challenges it has faced in the last two years. I know that President Bush and Secretary Evans will not be satisfied until we have done everything we can to create conditions that will allow manufacturers to maximize their competitiveness and spur economic growth.

One thing both the President and the Secretary have consistently emphasized is that the government cannot create jobs. It is the private sector that creates jobs. Government's role is simply to create the environment in which individual initiative, innovation and effort are rewarded. In other words, it is our responsibility to ensure an environment in which the private sector can succeed in creating jobs and economic growth that raises the standard of living for all Americans.

One need not look further than the most recent Census Bureau statistics to see the need for us to mobilize on behalf of the manufacturing sector to create that environment. Manufacturing has yet to recover fully from the recession. According to the Census Bureau, shipments of manufactured products decreased 1.5 percent in March 2003, the largest decrease since February 2002, and investment by these firms into new manufacturing equipment declined by 7 percent in 2001. Machine tool consumption dropped 24.9 percent in January 2003, compared to the previous month. Just last week, the Commerce Department announced that new orders for manufactured goods dropped 1.5 percent, which is the largest drop since September 2002.

In addition, we are all aware of the significant job losses in manufacturing. I am particularly concerned by the loss of engineering talent and experience. Our nation's manufacturers employ some of the best and brightest scientific minds, and their work has contributed to our national prosperity and economic growth. The loss of their technology expertise and innovation could produce a ripple effect in our economy.

Given the critical importance of our manufacturing base, the President and Secretary Evans are committed to ensuring that our manufacturers have what they need in the way of economic policy that will allow them to drive growth, innovation, and ultimately success.

Toward that end, Secretary Evans, in a speech during Manufacturing Week in March in Chicago, outlined an aggressive Administration agenda that will cement the role of manufacturing as a driving force in increasing productivity, economic growth, and living standards.

First, Secretary Evans has asked me to lead a comprehensive look at both the challenges and opportunities facing American manufacturing. I will rely on many of the bureaus within the Commerce Department whose activities are immediately relevant to American manufacturing for much of the legwork, including representatives from the Economic and Statistics Administration, National Institute of Standards and Technology, Patent and Trademark Office, Minority Business Development Agency, and others. We intend to reach out to the manufacturing sector across the country through a series of field hearings designed to ensure that we gain a broad cross-section of views from all industries within the manufacturing sector. I intend to ensure a particular focus on the needs of small and medium-sized enterprises as a part of that outreach.

We will work in close consultation, as well, with our manufacturers' customers, the financial community, academia, states and local communities both to discern the challenges we face and to identify the best practices within both the private sector and government to encourage a vital manufacturing sectors. We will coordinate efforts with the White House and the President's Council of Advisors on Science and Technology. We will also utilize the expertise of other agencies on their particular issues, consulting with the Treasury Department on tax matters, for instance, and the Labor Department on developing a flexible, well-trained workforce equal to the manufacturing sector's needs.

Gathering information from all these sources, we expect to develop recommendations for private sector action, government initiatives, and further work. Working together with organizations such as the National Association of Manufacturers that represent a broad cross-section of the manufacturing industry, we aim to have an interim report on the state of manufacturing by summer and a final report in the fall. I also anticipate working with this committee, and others in Congress, to discuss our findings.

Needless to say, we will have a very full plate. For instance, we have heard from countless American manufacturers that rising health care costs are affecting their competitiveness. The President heard those concerns and responded. He has proposed to expand the number of community health care centers, extend prescription drug benefits to retirees at lower cost, and reform medical malpractice laws so that awards compensate victims rather than trial lawyers. Yet, we're not finished. We will continue to examine what we can do to stabilize the cost of health care for employers.

America's manufacturers have asked this Administration for stronger intellectual property protection and funding for federal science programs. Again, the President heard those concerns and responded. We redoubled our efforts at the Department of Commerce to eliminate piracy of intellectual property abroad, and we are improving the speed and quality of patent and trademark processes at home. The President also proposed increasing federal research and development funding by more than 25 percent to $123 billion for 2004. But again, the President is not satisfied. Secretary Evans has asked us to determine whether these proposals will be sufficient to meet the needs of our manufacturers.

As a final example, I would like to highlight what the President has done in response to manufacturers' requests that he encourage a reliable supply of low cost energy, reform the New Source Review program on power plant emissions, and ensure science-based air quality standards. The President offered a National Energy Policy, an assessment of the New Source Review program, and an aggressive strategy to cut greenhouse gases over the next ten years based on sound science. Nonetheless, the President still believes that we can do more, and Secretary Evans has asked us to look at these issues along with the others.

I think it is also important to stress that when we find issues that need to be addressed, we do not intend to wait until there is a final report to begin our efforts to address those challenges. That process has, in fact, already begun. Let me give you just one example.

As we started the process of examining the challenges facing our manufacturers, one issue that they identified for immediate action was the issue of product standards. Foreign product standards – the process of their development and the effect of their technical regulations – have become an increasingly important barrier for U.S. exports. Some nations use divergent standards peculiar to their nation or region, redundant testing and compliance procedures, unilateral and non-transparent standard setting exercises, and a confusing thicket of other standards-related problems that can result in artificial impediments to trade.

To address this concern, one month ago, I was pleased to join Secretary Evans and Deputy Secretary Bodman to announce a new Department of Commerce Standards Initiative. The eight-point initiative will ensure that standards do not unfairly inhibit American companies from entering new markets. While assessing the situation, we will work to develop training programs so that staff in foreign markets can recognize and respond to standards issues; expand our early warning system to disseminate market intelligence and information on standards developments in key foreign markets; partner with the proposed President's Export Council subcommittee on technology and competitiveness; and, host a series of industry-specific roundtables to gather input from U.S. industry on the most pressing standards issues and priority foreign markets.

Given that standards and standards-related technical regulations are pervasive features of global commerce, affecting an estimated 80 percent of world commodity trade, this effort is significant. And in confronting this issue head-on, the President has charged his Administration with reducing the barriers to trade caused by foreign governments' policies on standards and technical regulations.

The Manufacturing Agenda is the President's Agenda

What I hope my testimony has underscored for the Committee is that, from product standards to tax and health care reform to energy policy and to trade negotiations, the American manufacturing agenda is our agenda. This Administration understands that for generations, American companies have been able to produce the highest quality goods, efficiently and economically. In the process, manufacturers have provided good jobs for millions of skilled American workers, raised our standard of living and standards of living throughout the world, and played a central role in securing our safety and liberty.

Given that history, it's not surprising that both the Administration and the Committee, under your able leadership, Mr. Chairman, are both committed to the health and vitality of American manufacturing. Bluntly, to be America, and to do what America has always done, our manufacturers must not only compete in global markets, but succeed. Our job is to create the conditions that will allow that to happen.

Once again, Mr. Chairman, I want to thank you for the opportunity to appear before the Committee and for your foresight in holding this hearing. I appreciate frequent advice and consultation we at the Commerce Department have had with you and all members of the Committee and their staffs. Working together, I have no doubt that we can affect real change and enable America's manufacturers and workers to compete in the global marketplace.

I look forward to your questions.

4/9/03 Congressional Committee Hearing

Thank you, Mr. Chairman, for the invitation to speak with you at this hearing. Today's subject matter is near and dear to me as it relates directly to the environment in which I live and work every day.

I am the owner of a consulting firm, based in Detroit. We work with manufacturing companies in helping them improve their cost, quality and productivity performance, with particular emphasis on the manufacturing side. Being in Detroit, much of our work is with the automotive companies both domestic and foreign owned, as well as their many suppliers. Nonetheless, we have worked with many non-automotive companies as well.

In addition, our firm publishes annually a study called the Harbour Report, a document that analyzes and ranks the performance of all the North American automakers, including discussions on what drives their results. In support of our work, we have had the privilege to walk the floors of most every automotive plant in North America, Japan and Europe and many of their suppliers. I believe this experience gives us unique insight into what has evolved in the recent history of U.S. manufacturing, certainly in one of its largest segments, the automotive industry. However, the lessons learned are analogous across many industries.

Like many industries, the automotive industry was broad-sided by unanticipated foreign competition over twenty years ago and has never fully recovered. Initial responses were protectionist, with import quotas and tariffs in response to cries of dumping and unfair competition. Our early research in 1980 and 1981 for the Department of Commerce told a very different story that what everyone assumed was the problem.

Our tours of Japanese plants revealed operations that attained much higher levels of quality and productivity then U.S. based operations through very strong design, engineering and training. Although differences existed in labor rates and currency exchange, the companies were simply better manufacturers.

Protectionism only bred complacency in the 1980's, but once the foreign competitors began manufacturing directly in North America, Detroit was forced to compete. Competition has saved what is left of the domestic auto industry, as many domestic plants and their suppliers have reached world class levels of performance. The American consumer has won because cars and trucks are better quality and less cost than ever in history.

A manufacturing base is vital to a strong and modern economy. This is well known in Japan, Germany, Korea and as well as in emerging economies such as China. I wonder how we would be supplying our troops in Iraq with planes, ships, guns and missiles if we couldn't produce them in the U.S. What would we do, import them?

Those who claim a modern economy can be primarily service-based are blind to the fact that those same service-based companies need a consumer for their services. Manufacturing-based companies provide a large customer base for those companies. In other words, a balance between service and manufacturing is key to a vital economy.

Recent studies have demonstrated the far reaching effects well compensated manufacturing jobs have on nearby businesses, both other manufacturing or service providers. These include the corner grocery store, the local WalMart, banks, barber shops, electronics, recreational vehicles, furniture, etc. Little wonder states throw hundreds of millions of dollars at foreign auto companies looking for a home for their new plant. Unfortunately, most domestic companies have not been able to secure the same financial support.

I am greatly concerned about the decline of our manufacturing base in this country and I believe it will have long term ramifications to our economy. Many factors have driven the shrinking of the employment levels in manufacturing, some purely from healthy gains in productivity. Other jobs have left due to our lack of competitiveness. But many are gone due to the total lack of any kind of business/government alliance to cultivate the growth of manufacturing in the U.S.

I hope our discussion this afternoon can constructively lead to solutions to this American dilemma. I promise to do all I can to contribute. Thank you.

Jerry Jasinowski
President
National Association of Manufacturers
House Small Business Committee
Washington, D.C.
April 9, 2003

Thank you, Mr. Chairman. I am Jerry Jasinowski, President of the National Association of Manufacturers. We are the nation's oldest and largest industrial trade association representing 14,000 member companies and 350 member associations serving manufacturers and employees in every industrial sector in all 50 states. Approximately 10,000 of our members are small and medium-sized manufacturers.

On behalf of the NAM, I thank the Committee for this opportunity to discuss the importance of manufacturing to our country, and the unprecedented challenges that today threaten our competitive leadership in manufacturing.

I am especially pleased to share this spotlight with my friend Rich Trumka of the AFL-CIO. It is not often that Rich and I have the opportunity to appear together, and I believe it is fair to say that this joint appearance underscores the gravity of the issue we are here to discuss. The NAM and the AFL-CIO have many differences, but when it comes to sounding the alarm bell about what is going on in American manufacturing, we speak with one voice.

I am especially pleased that Grant Aldonas, Underecretary of Commerce for International Trade, could join us today. Grant's presence underscores the Bush Administration's concern about manufacturing. In an address to National Manufacturing Week last month, Commerce Secretary Don Evans made it clear that the Bush Administration is cognizant of what is going on, and eager to help turn it around. In that address, he announced that Grant would head up an inter-agency task force to review the challenges facing manufacturing, and recommend policies to strengthen manufacturing.

This review is critically needed because manufacturing and its workers are in crisis. The recent economic downturn was no ordinary recession but rather centered on manufacturing. Manufacturing has lost jobs for 32 consecutive months, more than 2.1 million. In your home state of Illinois, Mr. Chairman, you lost almost 80,000 manufacturing jobs between July 2000 and December 2002. In fact, in that time period manufacturing has lost jobs in 49 of the 50 states.

Over the past year and two months, we have seen the weakest manufacturing recovery from recession since the Federal Reserve started keeping tabs on such things back in 1919. The data show that since December 2001, manufacturing production has edged up only 1.6 percent, drastically slower than the first 14 months of the previous six recoveries when growth in manufacturing averaged 10.8 percent.

Any review of manufacturing by the Department of Commerce or this Committee must be comprehensive and take into account the fundamental economic changes taking place because of technological change and globalization. A major focus must surely be the information and grassroots infrastructure needed to strengthen manufacturing and empower manufacturing workers for the long term.

In a resolution adopted in February, the NAM Board of Directors articulated an outline of the things we believe should be done to address these challenges. With your permission I would like to submit this Resolution to the Committee for the record.

In brief, we believe a review of manufacturing should focus on four primary areas:

- the strengths and successes of modern U.S. manufacturing;
- the unique challenges confronting manufacturing today; and
- the new public and corporate policies needed to address these challenges.

Turning to more of the strengths, manufacturing is essential to economic growth and employment opportunities. During the prosperity of the 90s, manufacturing was the largest contributor to economic growth. Manufacturing accounts for a quarter of U.S. economic output, 64 percent of exports, 62 percent of R&D, and 27 percent of growth. It is the driving force of technological progress and productivity growth. Indeed, during the late half of the 1990s, when the overall economy recorded respectable productivity gains of 2.5 percent a year, manufacturing roared ahead at 4.5 percent a year, or almost double that of the rest of the economy.

The loss of manufacturing jobs is particularly critical because they are some of our best jobs and have a major ripple effect throughout the economy. Manufacturing workers are among the best paid in our country earning 20 percent more than the average wage and more than 80 percent of them receive health insurance. In addition, manufacturing jobs tend to create and support more employment in other sectors than do service jobs. Our most conservative estimates suggest that the 16.5 million manufacturing jobs support at least nine million more jobs in other sectors of the economy.

It is also essential to emphasize the contribution manufacturing makes to national security – a contribution that has been dramatically visible to all of us in recent weeks. Our ability to deal with the regime of Saddam Hussein with minimal loss of civilian life among Iraqis, and relatively few casualties among our own troops, is based upon the advanced digital, laser and communications technology of industry. From the advanced fighter planes to the high tech ordnance guidance systems to night vision goggles – it is all a story of manufacturing genius at work.

Manufacturing is our nation's laboratory of innovation where our most creative people experiment with breakthroughs in technology in quest of the breakthrough products and more efficient processes that are the heart of productivity. In my book, "Making It In America," I told the stories of 50 companies that have paved the way for thousands of others through innovation. Manufacturing is the driving force of progress.

But hundreds of shuttered factories and more than two million lost jobs are a shot across our bow. We have a problem and we have to deal with it. In my view, we face three fundamental policy challenges if we are to preserve our global leadership in manufacturing competitiveness:

- One - the economy remains listless and uninspiring. Our first step to getting manufacturing back in high gear is to increase demand for manufactured products. The tax reductions proposed by the Bush Administration, or some reasonable variation thereof, offer the best hope for restoring confidence among consumers, investors and business. We have to get our economy growing again.
- Two - rapidly-rising business costs stemming from a general indifference to the burden of government rules and requirements on business are becoming an economic burden on our companies and workers. For some companies, the cost is simply too much. They must either lay off employees or outsource work to foreign countries.

A major issue for manufacturers is health care. As you know, most Americans obtain health insurance through their employers. Our industry is staggering under the weight of rising health insurance costs. Many of our members report double digit annual cost increases for health insurance. One of our top priorities is to persuade Congress to abandon the benefit mandate and health care liability agenda of its recent past in favor of proposals to help extend health insurance to more people, and to help keep costs under control. We are pursuing an agenda of health insurance affordability featuring health insurance access, a prescription drug benefit only in the context of comprehensive Medicare reform, and medical liability reform.

The asbestos crisis is a classic example of how ill-conceived public policy undermines our industrial strength. Asbestos litigants often can offer no evidence of harm or injury, yet awards are routinely in the tens of millions. At least $54 billion has been paid on more than 600,000 claims. More than 60 companies have been forced into bankruptcy and many more are threatened with extinction if a remedy isn't found soon. There are estimates that tthe total cost of asbestos litigation will exceed $250 billion if something isn't done. I should add that 38 of the nation's top 100 defense contractors are now asbestos defendants. This situation is literally insane and cries out for a legislative solution. The Supreme Court has repeatedly said that the asbestos crisis demands Congressional action. Every day of delay brings more economic damage to our country.

- While manufacturers must contend with steadily rising costs of doing business, unprecedented foreign competition makes it impossible for them to keep pace. Many of our trading partners routinely exacerbate their natural advantages with unfair trade barriers, including manipulation of currency values. China is the most conspicuous offender in this regard, and is emerging as the primary threat to many of our core industries. By some estimates, China's currency is undervalued by as much as 40 percent giving them a tremendous unfair advantage over U.S. companies – which means that China's exports to the U.S. cost 40 percent less than they should and that U.S. exports to China cost 40 percent more than they should..

Manufacturers are particularly worried because China's production is quickly moving beyond the traditional areas of textiles, toys and footwear – and into higher value-added production. Machinery imports from China are up nearly 50 percent in the last 12 months, furniture imports are up over 40 percent and organic chemicals are also up 40 percent. The list goes on. Last year, our trade imbalance with China passed the $100 billion mark and the deficit is growing by $20 billion a year. We cannot afford to keep hiding our heads in the sand to avoid facing up to this challenge.

In sum, manufacturing is the heart of our economic strength and national security. We cannot long maintain our position among the family of nations without a strong and viable manufacturing sector. That is why the NAM Board of Directors authorized the Campaign for Growth and Manufacturing Renewal that I mentioned earlier to raise awareness of how vital manufacturing is to our economy, identify the impediments to our competitiveness and rally support for pro-manufacturing policies and legislation.

Our basic policy objectives are:

- Tax policy that enhances economic growth and encourages productivity through technology and investment incentives, such as the expensing proposal in the President's tax plan;
- Trade policy that levels the global playing field for American manufacturers by opening markets, lowering tariffs, modernizing export controls and sanctions policies, enforcing trade laws and achieving market driven currency values;
- Cost-cutting reforms that will permanent improve the legal, regulatory, health care and retirement systems while lowering anti-growth and costly job-destroying burdens they impose;
- A national energy policy to ensure sustainable economic growth in manufacturing with emphasis on reliable supply at affordable prices, conservation, increased efficiency, strengthened infrastructure and investments in new technologies;
- Asbestos litigation and legal system reforms to reduce unwarranted burdens on the private sector;
- Technology policy that will preserve and enhance the U.S. lead in R&D and innovation and assure protection of intellectual property and strengthen our engineering and advanced skills; and
- Worker and skills enhancing efforts to put people back to work and to empower today's workers to meet the challenges of tomorrow.

In closing, permit me to state what I believe to be our most fundamental task – to increase visibility and awareness of the importance of manufacturing to our society, and the compelling need to preserve and enhance our manufacturing capability, and to do this at both the national and grassroots level. In our Resolution, we call for a Blue Ribbon Commission to take the lead in this effort. We see this commission as a forum to provide the research and initial direction for manufacturing renewal. Perhaps the Department of Commerce review can accomplish this objective.

In addition, we intend for forge a public-private coalition of business, labor unions, universities, public schools, government agencies and private think tanks that will work together to conduct further research and tell the manufacturing story and foster a new generation of young Americans committed to preserve our manufacturing legacy.

To meet this challenge, the coalition must rely upon the same capacity for innovation that has characterized manufacturing these many years, and made possible our world leadership. The challenges of a weak economy, changing technology, rising costs, and global competition will not yield to worn out phrases or yesterday's policies. We must bring to this challenge that same creative capacity that characterizes the people in the plants and factories who make things in America. The policies that would enhance and sustain our world leadership in manufacturing must be as innovative as manufacturing itself.

I thank the committee for affording us this opportunity to discuss the challenges facing manufacturing – and the timeless importance of innovation.

TESTIMONY OF RICHARD L. TRUMKA
SECRETARY-TREASURER
AMERICAN FEDERATION OF LABOR AND CONGRESS OF INDUSTRIAL ORGANIZATIONS
BEFORE THE HOUSE COMMITTEE ON SMALL BUSINESS
"Will We Have An Economic Recovery Without A Strong U.S. Manufacturing Base?"
April 9, 2003

Thank you, Mr. Chairman, Ms. Velazquez, and members of the committee. I'm pleased to have the opportunity to appear before the committee on behalf of the unions of the Industrial Union Council and the 13 million working men and women of the AFL-CIO.

The industrial unions of the AFL-CIO have banded together to respond to the deep crisis in manufacturing. We are dedicated to finding solutions to the serious challenges that face U.S. manufacturing and threaten the livelihood of millions of America's working families. It's important to note that about two-thirds of all workers in manufacturing represented by unions are employed by small to mid-size businesses.

For 32 straight months, manufacturing has lost jobs, the longest such stretch since the Great Depression. Since April 1998, the United States has lost 2.5 million manufacturing jobs, nearly 13 percent of the total manufacturing workforce.

Among the disturbing trends that many economists have noticed: capacity utilization in U.S. manufacturing, a measure of production activity, dropped to 74 percent late last year, its lowest level since 1983. Also, our trade deficit in goods is now $1.3 billion each day. Nearly every state in the nation has suffered manufacturing job loss, as the chart I've included with my testimony shows.

Unless these trends are reversed, serious damage will be done to the livelihoods of America's working families—and to the nation's economy. Manufacturing historically has been a major generator of good, high-skilled, well-paid jobs, including in nonmanufacturing sectors, and remains a mainstay of local and state economies throughout the nation. Manufacturing's decline not only undermines the quality of manufacturing jobs, but also contributes to the stagnation in all workers' wages. Moreover, the massive scale of manufacturing plant closings and job layoffs is contributing directly to the serious fiscal crises afflicting virtually every state in the nation.

America's manufacturing workers are the most productive in the world. But they operate under enormous competitive disadvantages resulting from several factors, such as unfair trade and tax policies, an overvalued dollar, inadequate investment incentives, health care costs not borne by overseas producers, and foreign government subsidies. Unless these problems are addressed soon, American manufacturing capacity and jobs may end up permanently lagging. And our economic strength may be permanently weakened: U.S. productivity and wage gains have been largely driven by the performance of the manufacturing sector. It's unlikely that another sector can step in to offer comparable wages, benefits, or productivity gains on as large a scale. Mr. Chairman, I will say that we won't have a stable, broad-based economic recovery without a strong manufacturing base.

There are a few issues I'd like to focus on today: investment in manufacturing and workers, a manufacturing tax credit, trade policy, currency valuation, and health care. In addition, I want to note that I believe there are many issues on which we can work cooperatively with employers and the Congress, despite differences we may have on other policies.

INVESTING IN MANUFACTURING

To encourage "high-road" strategies for industrial development, we recommend increased incentives, assistance and access to capital for small- and medium-sized manufacturers, as well as increased funding and incentives to employers for workforce training, emphasizing joint labor-management initiatives and industry skill standards. We recommend restoring funding for the MEP (manufacturing extension partnership) program to help manufacturers with training and performance needs.

REPLACING THE FSC

As a result of a World Trade Organization (WTO) ruling against the United States, this year the Congress is likely to consider changes to a provision of our tax law called the Foreign Sales Corporation (FSC) that had served as an incentive for U.S. exporters. We encourage Congress to replace the FSC with a broad-based manufacturing tax credit that rewards companies for keeping good jobs here and creating new ones. It's about time our tax code included incentives to retain jobs—and not ship them abroad.

Some in the Congress and the multinational business community are proposing to replace the FSC with nearly $90 billion in tax breaks for multinational corporations that will reward companies for sending American jobs overseas. This approach appears to define "enhancing American competitiveness" as boosting the profitability of multinational corporations to produce anywhere they choose, so long as they keep an American mailbox.

America's working families strongly oppose the offshore tax incentive plan to replace the FSC and support bipartisan efforts to craft an alternative that will grow manufacturing jobs in the United States. We are very interested in the idea of a manufacturing tax credit, which some businesses and Members of Congress have proposed.

TRADE

Put simply, America's trade policy has failed. That's not a partisan criticism, as unfettered trade liberalization has been an imperative for all recent administrations. But a look at the results shows that something must be done on trade—and soon. Last year, the U.S. trade deficit in goods hit a record-breaking high of $485 billion. U.S. exports actually fell for the second year in a row. Our 2001 $4.5 billion trade surplus in advanced technology products turned into a $17.5 billion deficit in 2002. It is hard to see where U.S. comparative advantage lies in the new global economy that current U.S. trade policy has helped to shape.

In the last decade or so, we have signed bilateral free trade agreements with four countries: Israel, Canada, Mexico, and Jordan. In each case, these agreements were sold to the Congress and the American public as "market-opening agreements," and in each case, our bilateral trade balance deteriorated after the implementation of the agreement.

The most dramatic instance is, of course, NAFTA, where a deficit with Mexico and Canada of $9 billion in 1993—before the implementation of NAFTA—has ballooned almost tenfold, to $87 billion in 2002. The U.S. has even managed to rack up a small trade deficit with tiny Jordan, with whom we had a surplus when we entered into a free trade agreement in 2001. Of course our largest trade deficit is with China. Since granting China Permanent Normal Trade Relations in 2000, which we were told would help us sell American goods in China, the U.S. trade deficit with China increased by almost 25 percent, hitting a staggering $103 billion last year – our single largest bilateral deficit.

Our trade policy must first seek to do no further harm. That's why we are distressed that at least half a dozen sets of trade negotiations are underway on agreements styled largely after NAFTA. We must refocus our policy to reduce the unsustainable U.S. trade deficit, protect U.S. trade laws that promote fair trade, and require the inclusion of enforceable workers' rights and environmental standards—far beyond what is envisioned in the current Fast Track authority.

CURRENCY

The overvalued dollar also has been a key factor diminishing U.S. manufacturing competitiveness and driving up the trade deficit. From January 1995 to January 2003, the dollar appreciated by 33 percent. A rise in the dollar increases the price of U.S.-produced goods relative to foreign goods, making them less attractive in domestic and world markets. This bias favors U.S. investment abroad over U.S. producers. The high dollar has discouraged investment in domestic manufacturing, reducing manufacturing investment by $37 billion in 2001.

Large manufacturers have often relocated overseas, where they could pay for inputs to production with undervalued foreign currencies while earning overvalued dollar revenues on sales to American domestic markets. At the same time, many small manufacturers, lacking the means to move overseas, have been forced to cut profits, incur losses, or close their doors. Congress should take a more active role in addressing the overvalued dollar, as well as examining foreign currency manipulation, such as that in China which pegs its currency to the dollar, but at an undervalued rate.

HEALTH CARE

The manufacturing sector is being especially hurt by the national health care crisis and exploding health care costs, which are rising up to 13 percent yearly. Companies that do the right thing and offer health benefits are harmed by competition with U.S. companies that don't provide benefits, as well as with overseas producers who are subsidized or don't provide benefits. Health care is the number one issue in contract negotiations today.

Manufacturing firms tend to have disproportionately more retirees whose costs are shared with a shrinking active workforce. For instance, up to $830 of the cost of each car produced by the Big Three automakers goes towards health care costs. Unless the Congress addresses health care, including retiree health care and prescription drugs, the competitive pressures will only grow stronger. This is not just about our people's health—although that should be reason enough—it's about the health of our economy. American manufacturers cannot compete well with countries where health care is a government service and not up to the individual company to provide it.

CONCLUSION

The extent to which we successfully revive our manufacturing base may determine the depth of the nation's economic recovery and shape its future economic prosperity. It is therefore vital for Congress to acknowledge the severity of this crisis and take the necessary steps to reform the policies that are at its root.

Thank you.

TESTIMONY OF DR. PAUL FREEDENBERG
VICE PRESIDENT FOR GOVERNMENT RELATIONS
AMT — THE ASSOCIATION FOR MANUFACTURING TECHNOLOGY
BEFORE THE
COMMITTEE ON SMALL BUSINESS
U.S. HOUSE OF REPRESENTATIVES
APRIL 9, 2003

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I. INTRODUCTION

Good afternoon. My name is Paul Freedenberg, Vice President for Government Relations at AMT – The Association For Manufacturing Technology.

Pursuant to House Rule XI, clause 2(g)(4), I am obligated to report to you that AMT has received $219,000 in fiscal years 1997-2000 and $84,200 in fiscal year 2002 from the Commerce Department's Market Co-operator Development Program to help pay for a service and training center in China.

AMT is a 100-year-old trade association that represents approximately 360 machine tool builders and related product firms located throughout the United States. I am pleased to testify before you today on the importance of America's manufacturing sector to our economic strength and stability. I will also discuss the uphill battle my industry, America's machine tool industry, faces to survive these tough times.

Mr. Chairman, I'd like to begin by thanking you for your strong leadership – along with Cong. Neal of Massachusetts – of the House Machine Tool Caucus, which has provided invaluable support and encouragement for our industry. Mr. Chairman, I'd also like to thank you and the members of your Committee who supported the economic stimulus package, enacted into law last year. The 30 percent expensing provision included in the package was AMT's top legislative priority for the 107th Congress. Improving and extending it permanent is AMT's top legislative priority for the 108th Congress.

II. THE IMPORTANCE OF AMERICA'S MANUFACTURING SECTOR

There is no refuting the importance of America's manufacturing sector to our economic growth and strength. For every dollar of final output in manufacturing, $2.26 is created through its backward linkages to other parts of the economy. This compares to $1.91 for transportation, communication, and utilities, $1.53 for finance, insurance, and real estate, and $1.70 for services.[1]

Productivity was the key to the economic boom of the 1990s, and it is important to remember that productivity gains in manufacturing outpaced those for the rest of the economy by a significant amount. Indeed, over the past 15 years manufacturing productivity has grown by an average of 1.4 percent per year while overall productivity averaged a mere 0.8 percent increase over the same time period. Moreover, productivity in the durable goods sector has grown by an average of 2.3 percent per year during the previous 25 years.

One of the benefits of these gains in productivity has been significant decreases in unit labor costs. These decreasing or contained unit labor costs translate into lower inflation and enable higher wages to workers, helping to elevate the overall standard of living. Manufacturing wages outpaced those of other sectors two to one. Over the past 10 years, manufacturing wage increases have averaged 3.4 percent per year while price increases for manufactured goods have averaged 1.5 percent per year over the same period. It is productivity gains in manufacturing that have enabled that advantageous gap to continue.

Another benefit of these productivity gains is an estimated $618 billion gain in Gross Domestic Product ("GDP") from 1992-1998 that came as a direct result of a surge in the productivity of durable manufacturing. This figure comes from a study titled *Producing Prosperity – Manufacturing Technology's Unmeasured Role in Economic Expansion* by Dr. Joel Popkin. By 1998, GDP was $238 billion greater than it would have been had it not been for that surge in productivity. Additionally, thanks in part to improvements, in large part, to

[1] Includes lodging, restaurants, health care, education, auto repair and other services.

manufacturing technology, American households saved $21 billion in 1998 alone in automotive maintenance and repair costs resulting from quality improvements in automobiles from 1985-1998.

The spread between overall inflation and the annual price increases from what consumers pay for manufactured goods has been widening. The difference in the inflation rates between goods and services has averaged 2.5 percentage points over the last 10 years. In the previous decade that gap was only 1.4 percentage points. The reason for the change has come from a significant slowdown in price increases for goods relative to services.

Manufacturing has contributed to overall economic growth disproportionately to its actual share of the GDP. Over the past 30 years, manufacturing's share of GDP has been falling while at the same time finance, insurance, and real estate and services' share of GDP have been rising. Manufacturing's share has fallen by almost 50 percent during that period, while service's share has doubled and finance, insurance, and real estate's share has risen by 50 percent. Nevertheless, during the last major economic growth period (1992-1998) manufacturing accounted for more than half the rate of growth of the GDP -- far more than any other sector.

In 1999 manufacturing's share of investment in new equipment dropped below 20 percent for the first time in 70 years. It now stands at 17.4 percent. That is a very bad sign if we want continued productivity growth and a continued increase in our standard of living.

Manufacturers accounted for 62 percent of industrial research and development in 2000. That is a drop of 18 percentage points from the 80 percent it accounted for 10 years ago.

The recent investment surge and resulting overhang has primarily occurred in the high-tech telecommunications and information processing sectors of the economy. A large part of this surge in information and telecommunications technology was a result of the "Y2K" scare of the late 1990s, which led many companies to divert investment from new productive equipment to fixing the "Y2K" problem. The machine tool industry was one of the sectors that suffered from that diversion of capital purchases. To the extent that there is over-capacity in machine tools and other types of productive capital equipment, it is overcapacity in over-age, antiquated equipment. Over 60 percent of the machine tools in American factories today are over 10 years old. This compares with a very high percentage of newer more productive machines in the factories of our customers' European and Asian competitors.

III. THE STATE OF THE U.S. MACHINE TOOL INDUSTRY

The machine tool industry is a very small segment of our nation's manufacturing infrastructure relative to its critical importance. Significantly, machine tools should be understood as the basic building blocks for all other industries, whether those industries are automotive, defense and aerospace, electronics, or appliances. Everything made in a factory is either made on a machine tool or on a machine made by a machine tool. In fact, everything that is produced or sold by every business in America – is either made by a machine tool or by a machine that was made by a machine tool. Examples of machine tools include: cutting, grinding, forming and assembly machines; inspection and measuring machines; plus all automated manufacturing systems. Approximately 30 percent of the machine tool industry's output is exported, and, both at home and abroad, our industry competes with machine tool companies from around the industrialized world.

I began this testimony by discussing our nation's remarkable productivity boom during the past decade. Well, that boom would not have been possible without a strong machine tool industry. That means that the key to reversing the economic downtown we are currently experiencing and returning our nation to economic prosperity is also dependent on the maintenance of a strong and healthy machine tool industry, which is the key component of this nation's manufacturing infrastructure. Machine tools translate the dizzying advances in information technology into the design of new manufactured products and the factory floor automation that more efficiently produces those products.

It ought to be, therefore, cause for grave concern that this critical industry is experiencing the worst conditions in its domestic market in a half a century. Orders are off more than 55 percent since their peak in 1997. Import penetration has increased more than 40 percent in the past four years, due, in large part, to an overvalued U.S. dollar combined with our trade competitors' anti-competitive subsidies and currency distortions. To add to our industry's problems, we have seen increased outsourcing by some of our largest U.S. customers. We have also seen lost sales as a result of unfair offset conditions that force companies to manufacture large portions of products such as aircraft in the purchasing country.

This, in turn, has caused further industry distress and caused banks to be quicker to foreclose on their manufacturing clients with hard assets, while allowing their service industry clients with similar balance sheets to continue to operate. These banking decisions have not been based on the long-term viability of the individual companies but rather on the value of their assets and what they could bring in at auction. This thinking has affected all manufacturers, machine tool builders as well as their customers.

More than 30 machine tool companies have closed their doors in the past 18 months. This represents nearly 10 percent of the companies in the entire industry and a much greater percentage of the industry's employment and assets. You may recall that one year ago this month, Edward W. Fedor, President of Masco Machine, Inc. located in Cleveland, Ohio, testified before your Committee on the crisis facing U.S. manufacturers. Months later, Masco became a victim of the crisis about which Mr. Fedor was speaking, when the company was forced to close its doors at the end of 2002. Masco had been a member of our trade association since its creation more than twenty years ago.

IV. CURRENCY PROBLEM

Leading analysts for the machine tool industry are projecting a seven to 18 percent rebound in orders this year. But, even if this projection is accurate, 2003 orders, in real terms, will still be weaker than they have been in more than 50 years. Let me focus on one leading problem that all of U.S. industry confronts. There is great concern across a wide variety of industries regarding the Chinese Government's strategy of undervaluing their currency in order to garner exports and foreign investment. Last year our bilateral trade deficit with China exceeded $103 billion. Indeed, China is accumulating foreign reserves at a rate of more than $6 billion per month. This is an uneven trading arrangement, and it is directly related to a distortion in the value of the two nations' currencies.

China's strategy over the past decade has been to keep the value of its currency low, boosting its exports and holding down imports. Chinese intervention, through massive purchases of U.S. dollars, has kept the Chinese yuan from appreciating despite large trade surpluses and investment inflows. By some estimates, the yuan (also called the renminbi) is as much as 40% below the value that would be set by the marketplace. That means that U.S. exports to China may be overpriced by as much as 40 percent and that Chinese goods in the U.S. would be under priced by that much. This is a critical factor in the huge U.S. trade deficit with China and in the relocation of so many companies to China, where they can benefit from what is, in effect, a currency subsidy.

It is indisputable that there is no free market for the yuan. Despite rapid economic growth, rapidly rising productivity, soaring exports, and huge foreign investment inflows – all factors that would normally cause a currency to appreciate – China has kept its currency pegged at 8.2 yuan to the dollar since 1994. The Chinese central bank sets the exchange rate by requiring companies and individuals to turn over their foreign currency earnings at the rate set by the bank. The central bank, in turn, has made massive purchases of U.S. dollars, adding these to China's foreign currency reserve accounts. China's foreign currency reserves, almost entirely in dollars, now stand at $286 billion. China's dollar holdings have doubled in four years.

The U.S. trade deficit with China was $103 billion last year, the largest bilateral trade deficit in the world! United States *imports from* China have been growing at more than twice the rate of U.S. *exports to* China. Of greater importance, however, is the currency imbalance. China's import tariffs have averaged about 15 percent. If analysts are correct and the currency is 40 percent undervalued, the **effect of a free currency market would be more than twice as large as the effect of eliminating all tariffs.**

The global U.S. trade deficit last year was $470 billion – up $300 billion in the last five years and now nearly five percent of the United States' GDP. The major reason is that for those five years the U.S. dollar has been significantly overvalued relative to foreign currencies. The dollar peaked in February 2002 at 30 percent above its normal level for the previous decade. Since then it has been returning to more normal levels, and in February 2003 stood at 15 percent over normal levels. Most of the adjustment has been against the euro. None could occur against the yuan, **because it is pegged to the dollar at the artificial rate of 8.2 to one.**

As two of the great trading nations of the world, the United States and China must have a healthy trade relationship. Trade barriers and distortions should not be tolerated. China's World Trade Organization ("WTO") entry is reducing its formidable trade obstacles. But the currency-related trade distortions must also be ended. This issue is the responsibility of the Secretary of the Treasury, and it is AMT's hope that Secretary John Snow will enter into discussions with his Chinese counterparts at the earliest possible opportunity with the objective of achieving a more reasonably priced yuan. This trade distortion must be eliminated or we may see whole industries either lose their markets entirely or be forced to relocate to China in order to survive.

V. TAX POLICY

Beyond entering into discussions with the Chinese Government, there are many other ways Congress can help. One way to offset the production cost disadvantages that currently exist would be to stimulate the capital investment necessary to modernize plants and equipment, thereby increasing not only production but most importantly productivity. The obvious way to accomplish this goal would be by **substantially enhancing and extending the thirty percent expensing allowance** during consideration of the economic growth and jobs package that will be occurring shortly. The current additional expensing allowance is due to expire in September 2004, just at the time when it should really begin to influence buying decisions on a large scale. It has already been shown to have an impact even under the worst conditions, so the size of the allowance should be expanded and its expiration date extended to ensure that U.S. machine tool builders and their customers are able to fully realize the benefits when the economy does begin to recover. This can be done with a relatively low 10-year revenue loss. For approximately $15 billion over 10 years, you could increase the 30 percent expensing allowance to 50 percent and extend it through 2005; or you could increase it to 70 percent or even 80 percent and allow it to expire at the end of 2004. Either decision would have a huge simulative effect on business investment and on the productivity and competitiveness of U.S. companies who are struggling to survive in an increasingly hostile international competitive market. We commend Congressmen Jerry Weller and Phil English for their leadership on this issue, as well as the over 100 other members of Congress who have signed on as cosponsors of one or both of their bills.

We also strongly support the Section 179 small business expensing increase contained in the President's economic growth and jobs package, along with the ending of double taxation of dividends and the escalation of the effective dates of individual rate reductions. The President's program is a good one. It will bring about short and long term economic growth. The adoption by Congress of an enhanced expensing allowance for all businesses would make the President's proposals even better.

VI. HEALTH CARE

Health care remains a key area of concern for our members. Like most businesses, they face ever-increasing difficulties as they attempt to offer their employees quality and choice in health care coverage. Double-digit annual rate increases for health insurance have become the all-too-painful reality.

We believe that Association Health Plans offer one promising solution. As you know, Mr. Chairman, associations wishing to sponsor health care plans for their members currently face a state-by-state patchwork of differing mandates and regulatory regimes. For organizations such as AMT, this situation has made offering such services a practical impossibility.

H.R. 660, which was introduced earlier this year by Congressman Fletcher, would free associations to sponsor health care plans on a nationwide basis. We are grateful that so many members of this committee were original cosponsors of this legislation. In particular, we applaud Chairman Manzullo and Ranking Member Velázquez for joining together as original cosponsors. In the two months since introduction of the bill, over 100 members of the House have signed on as cosponsors.

Though not a panacea for all of the challenges that confront small businesses struggling to offer quality health care, this proposal would help harness the purchasing power that small businesses have when they band together.

AMT actively supports this legislative proposal.

VII. <u>EXPORT CONTROL REFORM</u>

Another way to help strengthen manufacturing is through reform of our nation's export control policy. When machine tool companies finally do get orders, many times they are unable to fill them because of unilateral and sometimes irrational export control regulations. United States export control policy, particularly with regard to China, puts U.S. companies at a significant disadvantage in obtaining sales to what is likely to be the fastest growing and largest market for capital goods over the coming decade. Statistics we have gathered from official U.S. Commerce Department sources demonstrate that export license applications to China are likely to take from four months to as long as a year to review. Moreover, export license applications for Chinese end-users during many of the past several years have been rejected at an almost 50 percent rate by the U.S. government. By contrast, our allies obtain licenses for these very same products to these very same end-users in days, or at most a few weeks. Repeatedly over the past decade, the United States government has taken a negative approach toward machine tool sales to China while our allies have not. The result has been that the Chinese have been denied nothing in terms of high technology, while U.S. firms have lost out in a crucial market. This serves neither our commercial nor our strategic interests. Indeed, the Chinese have begun to warn U.S. machine tool builders to not even bid for new Chinese projects, since many Chinese factory managers' experience with our export control system has been so negative.

When I traveled through aircraft factories on a November 2002 export control trip through China, I witnessed facility after facility producing Boeing and Airbus parts and components on European and Japanese five-axis machines. Surprisingly, the factory managers with whom I spoke voiced their preference for U.S. machine tools and some were being employed on their factory floors. But they also made it clear that they would not hesitate to order from U.S. competitors if the U.S. licensing system continued to subject them to long delays and uncertainties. We are at the outer limits of Chinese factory managers' good will, and yet we continue to make U.S. machine tools difficult to acquire by subjecting Chinese buyers to an export control process that seems to be operating on unfounded assumptions, accomplishing little of national security value in the process.

VIII. DIFFICULTIES IN OBTAINING VISAS

Another obstacle our industry faces is the difficulty in obtaining visas for our customers. There have been numerous promises by State Department officials to fix the current bureaucratic foul-up in which anyone attempting to bring customers, or other visitors, into the United States from China (and other Asian countries) has been met with delays and confusion regarding the procedure and the time frames for obtaining visas. Machine tool companies (most notably, including a major company in your hometown, Mr. Chairman) have been unable to get their customers into the country in order to witness demonstrations of machines that they have already purchased. Boeing has been unable to bring in pilots to qualify on their planes, or prospective customers to watch demonstrations of Boeing products. United States resorts are unable to get their summer workers into the country, and even desperately ill patients have died while awaiting visas for medical care at U.S. hospitals.

Despite State Department promises, the visa situation has actually deteriorated, with delays of four months or more not uncommon. Some Chinese visitors have not even been able to arrange the initial interviews with the U.S. consulate, which is, of course, the pre-condition for obtaining a visa. Based on calls that I receive every day, I can tell you that AMT members have millions of dollars in machines tied up on their floors (waiting for their Chinese customers to participate in final run-off inspections), or (in the case of potential customers visiting their U.S. plants) have lost similar amounts to foreign competitors able to take advantage of the glacial pace of the U.S. visa bureaucracy.

IX. CONCLUSION

In spite of the hard times we are facing, the United States is still the undisputed leader in developing new manufacturing technologies, and foreign customers recognize the value of American quality and technology. Our products remain globally competitive in an increasingly hostile marketplace. However, as the struggle for survival continues, it is getting more and more difficult to maintain our leading edge.

I urge members of the Committee to support legislation and public policy initiatives aimed at strengthening America's manufacturing infrastucture, such as enhancing and extending the 30 percent expensing allowance as part of the President's economic growth and jobs package.

America also needs a sound export policy, including strong support for export financing and promotion. That means that we need appropriate funding levels for these functions. We need a sound manufacturing technology policy, with sufficient funding for government research and development programs, in order to stimulate the movement of research into products. The Foreign Sales Corporation ("FSC") must be replaced with a WTO-consistent lower effective tax rate for manufacturing activities conducted in the United States. We need to fix our process for granting visas so that our customers can visit and see the machines they have already purchased and are not alienated in the process of purchasing U.S. machinery. Finally, our legal system is in need of reform (such as a statute-of-repose for machine tools and other workplace equipment).

Without those sensible reforms, the U.S. machine tool industry, which is a critical building block of America's continued prosperity and security, could very well disappear. Mr. Chairman, our industry applauds your efforts and hopes to continue to work with you in your efforts to build a stronger America. Thank you, Mr. Chairman. I will be pleased to respond to your questions.

U.S. MANUFACTURERS IN THE GLOBAL MARKETPLACE: MARKET SHARE CHANGES, VULNERABILITIES, AND POLICY CHALLENGES

Testimony of
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CONGRESS OF THE UNITED STATES
House of Representatives
108[TH] Congress
Committee on Small Business
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U.S. Manufacturers in the Global Market Place: Market Share Changes, Vulnerabilities, and Policy Challenges

Professor Michael R. Czinkota

Chairman Manzullo, distinguished members of the Committee, thank you for inviting me to testify here before you today. At Georgetown University's McDonough School of Business, where I teach, our international marketing team has systematically tracked the international activities of U.S. manufacturing firms for more than two decades. One key focus rests with small and mid-sized U.S. exporters, where we track concerns and forecast changes in international business practices. I will provide you today with an overview of the changing export and import flows of U.S. manufactured goods in the global economy, offer some thoughts on the possible repercussions of these changes, and make suggestions for policy consideration.

A VULNERABLE TRADE POSITION

As you requested, I first offer some background on the U.S. international trade position and draw a link to manufacturing. Since 1975 the United States has been importing more than exporting, therefore running a continuous current account deficit.

Exhibit 1 shows the U.S. current account balance over the past 32 years. While there have always been ups and downs, since the early 1990's the growth of the deficit has been rapid and major. On a global level, U.S. imports are necessarily some other country's exports. Our current account deficit is matched by bilateral current account surpluses of other nations. At $ 103 billion China had the largest current account surplus with the United States in 2002, followed by Japan with $70 billion, Canada with $50 billion, and Germany with $36 billion.

Exhibit 2 breaks the current account down into its components: merchandise trade, services trade, investment income, and net unilateral transfers. Merchandise trade is not only the largest factor, but it also contributes the most to the deficit. In 2002, services trade was substantial and had a surplus of over $49 billion but was overwhelmed by merchandise flows. Investment income produced a deficit of $5 billion, while net unilateral transfers resulted in a deficit of $56 billion.

Virtually without exception, the size of the deficits in merchandise trade has driven the size of current account deficits. Exhibit 3 shows that U.S. merchandise exports have been constantly rising. However, since the mid-1990's, these increases have remained far below the increases in merchandise imports. Therefore, the gap between imports and exports has been widening and merchandise trade deficits have been growing rapidly.

Exhibit 4 breaks overall merchandise trade down into its components: manufactured goods, mineral fuels, agricultural goods, and the catchall category of "other". For both U.S. exports and imports manufactured goods play a key role. 81 percent of our merchandise exports are manufactured goods, as are almost 84 percent of our imports. In comparison, proportionately, we export much more in agricultural goods and much less in fuels than we import.

Exhibit 5 highlights the deficit development in manufactures trade. While there have been deficits over the decades, these were quite stable in their size during the 1980's and into the early 1990's. However, from 1992 on, the growth of imports in manufactured goods has been much steeper than the growth in exports, leading to a widening manufactures trade deficit.

Exhibit 6 indicates the top surplus and deficit countries in U.S. manufactures trade. While we run substantial manufactures surpluses with the Netherlands, Australia, and Belgium, these are dwarfed by our manufactures deficits with Mexico, Germany, Japan and China. In 2002 U.S. bilateral manufactures trade with China alone was $103 billion in deficit.

Looking at the key manufactures trade imbalances by type of commodity, exhibit 7 shows that in 2002, there were large U.S. surpluses in airplanes and parts, wood manufactures, scientific instruments and chemicals. Yet, these surpluses were far outweighed by deficits in industries such as furniture, toys and games, televisions and VCR's, and apparel. The largest deficit category in the manufacturing sector is motor vehicles, with an imbalance of $111 billion.

PROVIDING AN OVERALL CONTEXT

Let me now provide a domestic and global historical context. In the mid-1800's, about 68 percent of U.S. employment was in the agricultural sector. Manufacturing accounted for only 17 percent of employment. Since then, the employment absorbed by these sectors has shifted dramatically. By 2001, agriculture, for example, accounted only for 1.5 percent of employment. But we do not have 66 percent of the work-eligible population consisting of unemployed farmers. Rather, there have been dramatic increases of employment in the services sector, where employment has risen from 22 percent to almost 80 percent of the overall economy. The manufacturing sector, in turn, grew to an employment proportion of almost 30 percent in 1960. In the last 20 years, however, employment levels have decreased at a rising rate. At the turn of the new millennium, U.S. manufacturing employment, at 14.8 percent, had decreased below the levels of when it was first officially measured.

For a global context, exhibit 8 compares employment developments in manufacturing in the United States, Germany and Japan. German manufacturing employment dropped by more than 13 percentage points during the past 31 years, and its shift as a proportion of GDP, was from 36 percent to 23 percent. The steepest decline came in the 1990's when, within one decade, employment dropped by almost 7 percentage points. In Japan, manufacturing employment dropped by 6.5 percent from 1970 to 2001. As a percent of GDP, the shift was from 33.5 to 21 percent. There, the steepest decline also occurred in the 1990's; yet, it was a much milder reduction in which manufacturing as a percent of total employment fell by 3.5 percentage points. This is in sharp contrast with U.S. employment changes. U.S. and Japanese manufacturing employment were almost the same in 1970. Since then, U.S. proportionate employment has been cut almost in half – and is now more than five percentage points lower than the Japanese manufacturing employment and almost 10 percentage points below German levels. U.S. manufacturers and their workers have, therefore, undergone the most drastic changes among the three countries when it comes to employment. While other countries have taken protective measures to soften the blow against their manufacturers, U.S. firms have experienced the full power of market forces.

All these shifts in employment reflected a transfer of manufacturing away from the industrialized nations towards the emerging economies. Exhibit 9 shows how the proportion of manufacturing has rapidly grown in nations such as Malaysia, South Korea, Thailand, and Indonesia.

THE PRODUCT CYCLE

These developments are consistent with the theory of the product cycle, which was developed by Professor Raymond Vernon of Harvard University in the 1960's. He postulated that a product and the methods for its manufacture goes through three stages of maturation, and as the manufacturing process becomes more standardized and low-skill labor intensive, comparative advantage in its production and export shifts across countries.

Initially, a product will be most effectively designed and manufactured near the parent firm in a highly industrialized market due to the need for proximity to information and the need for communication among the different skilled-labor components required. As production expands, its process becomes increasingly standardized. The need for flexibility in design and manufacturing declines with the demand for highly skilled labor declining as well. Competition increases, putting downward pressure on prices and profit margins and making production costs an increasing concern. The firm faces a crucial decision at this stage: Either lose market share to foreign-based manufacturers using lower-cost labor or invest abroad to maintain its market share. In the final stage, the manufacturing process is completely standardized, and the country of production is simply the one with the cheapest unskilled labor. Therefore, manufacturing capabilities and costs together with investment preferences cause the shift of manufacturing plants between countries.

SOME KEY CAUSES

Such a shift is greatly hastened when manufacturers under-export. When entering international markets, firms are faced with new risks, new cultures, new processes, and new conditions such as changing exchange rates and divergent government regulations. There are difficulties in obtaining financing for export ventures, and the regulatory rules for exporters can be complex. For many U.S. firms, the size of their home market seems to provide ample opportunity, obviating the need to learn about international prospects. As a result, U.S. firms do not take sufficient advantage of international market opportunities and under-export relative to other nations. U.S. merchandise exports comprise only 11 percent of GDP, compared to almost 34 percent for the European Union (excluding intra-EU trade) and 26 percent for China. On a per capita basis, in 2002 the European Union exported $7,434 for every man, woman and child, while for the United States it was only $3,794.[1]

U.S. manufacturers also contribute to the migration of plants. In order to maintain their price competitiveness many of them have established subsidiaries abroad to take advantage of lower labor costs. They specify the products to be produced by these subsidiaries, decide on the quantities to be turned out, and determine the volume of shipments back to the United States. In 2000, the latest year for which data are available, such import shipments from foreign affiliates of U.S. companies amounted to 14 percent of U.S. imports. In addition, many firms have developed long term supplier relationships with firms abroad, which lead to another large set of "captive" imports.

Subsidiaries of foreign firms in the United States also import from affiliated plants of their home countries. The share of U.S. imports accounted for by these foreign parents of U.S. affiliates was 20 percent in 2000.[2] Therefore, at least one half of U.S. imports are initiated and encouraged by U.S. corporate entities who consider it good business strategy to source from abroad rather than producing in the United States.

PRACTICAL IMPLICATIONS

The fulfillment of theoretical expectations does not mitigate the very real problems of daily life. While it is comforting to point towards the gradual adjustment of employment sectors over time, individuals currently experiencing the economic shifts through their personal unemployment will see this explanation as providing little solace. The economy appears to be working quite efficiently from a long-term perspective. But the need to adjust lifestyles, obtain a new set of skills, and change location may be overwhelming to many. Similarly, such shifts have an impact on the firm's stakeholders. Companies are one piece of a mosaic that affects the appearance and stability of the other pieces. For example, the disappearance of a firm will affect the local community and government, shape the fate of local suppliers, educational opportunities, health care, and may even determine whether a community can survive.

There also has to be a holistic perspective which looks beyond the immediate surroundings. When important shifts occur in the economy, we need to think beyond the static effects and consider the repercussions down the road. Otherwise it would be the rare exception to see investments for the long term common good. There would be few trees planted, lighthouses built or basic research projects conducted.

Finally, we realize that while important, the economic dimension cannot be the only criterion driving our nation. Issues such as national security, public safety, our overall standard of living must be considered when analyzing the importance of specific changes.

REPERCUSSIONS AND CONCERNS

The shift in our manufactures trade and the continued accumulation of growing trade deficits gives rise to concerns on a macro- and microeconomic level. Nations need to have a sound footing in order to be strong in their offense against terrorism, capable in their maintenance of a standard of living, and kind in their support of the poor and the ill.

We know that on the macroeconomic level trade deficits of the current magnitude are unsustainable in the long run. At about five percent of GDP, these trade deficits add to the U.S. international debt burden, which must be serviced through interest payments and eventually perhaps even repaid. Therefore, an improved global performance by U.S. manufacturing firms which results in an increase in their exports and an improved competitiveness with imports will be crucial for the nation.

There will be concern by the international trade community about any U.S. desire to gain more market share for its exports and to stem the rapid increase of imports. However, the U.S. has the right to argue for a special case. After all, as the trade figures have shown, over the decades the U.S. market has remained wide open to imports. Even today, when faced with many international machinations, the United States continues to offer its own market and consumptive power as an economic locomotive to the world. Many nations would have fallen into the abyss of economic disaster had their exports not had virtually unfettered U.S. market access as a recourse. And as we have seen, U.S. manufacturing has already paid the price by suffering the most drastic declines among all the industrialized nations.

We should also consider our manufacturing capability in the context of our lifestyle and national needs. When a manufacturing sector disappears domestically, it leaves behind a void which goes beyond lost jobs. Replacement parts suddenly become unavailable or much more expensive. Product re-orders, now filled abroad, take weeks rather than days. Some crucial input components to other manufacturing processes may be lost or delayed, slowing down the production of related products. Particularly for industries critical to the national welfare and national security, such effects can be devastating in case of an emergency. Even if there is a good relationship with the governments of the countries to which sensitive manufacturing industries migrate, one has to take the long term developments under consideration. For example, how many of us would wish, in today's fog of war, to rely on old friends abroad for the rapid re-supply of crucial manufactures? We must recognize that the much praised interdependence of globalization of manufacturing has increased our national dependence.

Then there are the effects of manufacturing migration on innovation and market responsiveness. Together with my colleague Masaaki Kotabe of Temple University, I have analyzed the use of emerging technologies in existing products. We found that the closer companies are to their market, the more they can use such technologies in new products. Japanese companies systematically incorporate new technologies in existing products. This enables them to gain experience, debug technological glitches, reduce costs, boost performance, and adapt designs for worldwide customer benefit. As a result, they have been able to increase the speed of new product introductions, meet the competitive demands of a rapidly changing marketplace, and capture market share. The continual introduction of newer and better designed products brings a greater likelihood of market success. However, when production is removed from its primary market, such rapid response to market demands may well be dulled, which can lead to a decline in manufacturing competitiveness.[3]

Sourcing from abroad through independent suppliers on a contractual basis may also have long-term consequences on the processes, competence, and capabilities of firms. In a comparison between the outsourcing networks of Japanese and U.S. companies, Professor Kotabe finds that U.S. companies gradually severed their value chain and, in search of cost efficiency, have willingly increased their dependence on foreign suppliers for components and finished products that have become technologically more sophisticated. The creation of new technology is a gradual and painstaking learning process of continual adjustment and refinement, as new productive methods are tested and adapted in the light of a company's accumulated experience. Thus, over-reliance on acquisitions and new technologies from other firms may not result in the same sustainable competitive advantage available through internal development. The manufacturing shift abroad may, therefore, eradicate current technology, design and process advantages possessed by U.S. firms, placing them and the country at further, future disadvantage.[4]

There are also effects of manufacturing migration on cluster formation. Over the past decades we have learned and observed that many industries tend to gradually emerge in a cluster formation – where a diverse set of firms eventually shapes regions or centers of excellence. Such centers are characterized by strong competition from a wide variety of firms, demanding customers, and a multitude of creative and innovative suppliers. They tend to be attractive to job seekers in that particular industry, generate specific expertise, and bring in even more firms wanting to be in close proximity to industrial capability either for production or buying purposes. Silicon Valley in California or the Diamond District in New York can serve as examples.

Typically only a few firms were the originators of such a cluster of excellence. It is therefore reasonable to expect that similar developments are true in reverse. For example, the migration of a few key firms can result in the decomposition of such clusters and their relocation to other regions. Such a phenomenon may occur particularly in industries where changes in technology make skill levels less important. As the shoe and optical equipment industries have demonstrated, a decline in the skills required can lead to movement of an entire industry. Such a lumpy migration of manufacturing can then result in a greatly magnified effect on individuals and communities. Therefore, the shift of any one manufacturing firm must be seen in the context of the overall stability of existing clusters.

SOME POSSIBLE POLICY REMEDIES

The concerns raised can be addressed by various actions. One major temptation may be to press legislation against those countries and foreign industries which account for substantial imbalances in manufactures trade. Doing so, however, runs the grave risk of substituting government judgment for market direction, a replacement which has not distinguished itself by past success. Prices might rise disproportionately, consumers might be deprived of desirable goods, and firms might find their ability to export undermined.

More positive change might be achieved by encouraging existing market activities through better processes, more support and more information. For example, export promotion can persuade U.S. manufacturers to take more advantage of international opportunities. This will require coordinated and streamlined services by government. They must include more information, a greater availability and ease of export financing, more streamlining of the logistics of international shipments, better tools for risk analysis, and better targeting for the delivery of this support. For example, there need to be more systematic efforts to introduce customer relations management (CRM) activities and benchmarks into government export promotion work. When a firm seeks governmental help with financing, communication, or its shipments, such assistance ought to be provided through one "personal export officer", regardless of which agency handles the details.

There also needs to be more emphasis on and opportunities for the bundling of products, services, financing and the creation of global networks when it comes to the international effort. It is through such bundling that U.S. manufacturers can gain specific advantages not available to their competitors abroad. Consider one example from the automotive industry: Airbags, the global positioning system, and a telephone in a car are no longer anything special. Yet, by bundling all these components together, car manufacturers have been able to develop an entire new set of passenger assistance services which can even independently notify emergency services in case of an accident.

Such combinations of available products, technology and networks can lead to an entirely new plateau of customer satisfaction.

On the regulatory side, a stable and safe international environment is, in itself, an important support for U.S. firms. But regulations also need to incorporate more of an international dimension by considering the global implications and effects of regulatory actions. For example, U.S. export control rules need to be revisited in order to ensure that they are precise and targeted, while not needlessly inhibiting to firms. For example, the foreign availability of products needs to be taken into consideration before denying a firm the opportunity to export. If similar products are available from abroad (even though perhaps at different prices and in different quantities), the regulatory community must face a particularly high hurdle of proof of effectiveness before denying a license application. Likewise, if a U.S. firm receives an export order which requires the production inspection of the foreign buyers, our visa regulations should be able to quickly accommodate the need for a brief visit by foreign customers. By delaying such visits for months, current and future manufacturing export contracts may well be in jeopardy. In revising the structure of our critical industries list it would also make sense to add the survival of manufacturing industries as a specific evaluative dimension.

There should be a systematic effort to alert customers and consumers to the long term consequences of their purchasing decisions. Their knowledge level should be addressed before the final consequences of their decisions are reached. Perhaps we can learn from the motto of a national clothing chain: "An informed consumer is our best customer." More available domestic information on manufacturing and its future may well affect have some decision processes. The White House Office of Global

Communication has been created to let the world know more about the U.S. and its intentions abroad. Perhaps a similar outreach effort should communicate the condition of manufacturing to a domestic audience.

As a caveat, it is worth noting that services are, at 79 percent of the workforce, the largest employing economic sector in the United States. Increasingly U.S. services industries are becoming footloose and are beginning to go global. We have all heard the stories about the back office operations in Ireland and India. These services are growing progressively sophisticated. For example, many x-ray and CT scan frames are read by radiology experts abroad. We should therefore also consider how to ensure that U.S. services firms and employees retain their international competitiveness.

There is always the question of who pays for such efforts. For the past half century, various U.S. administrations have been instrumental in opening up world markets. Congress has been supportive by ratifying the resulting agreements with the expectation of beneficial economic effects. However, the positive effects caused by free trade are not self-evident; they must be explained, defined, and provided by industry in a highly visible fashion on a regular basis, particularly when it comes to jobs. The public understanding of free trade and its resulting reverberation is often insufficiently addressed. In listening to some of the arguments brought forth by activists against free trade, one might gain the impression that there are no benefits at all. It is up to the beneficiaries to step up to the plate and provide positive evidence both to legislators and the public at large.

For too long, there has been little, if any, linkage between the governmental efforts which open markets and the industry response to the benefits obtained from such openings. For example, even though most trade negotiations result in both winners and losers, there are no current incentives for winners to let others share in their bounty. Similarly, there are few if any requirements placed on the beneficiaries of protective measures to convincingly demonstrate how they have used their enhanced revenues to help the transition of workers and communities. Perhaps the times should be over during which industries reap the benefits from government actions and negotiations, without having to deal with any of the negative reverberations.

The free riders, of which we have more than a bus full, need to become part of a national dialogue that addresses temporary dislocations and finds acceptable solutions for those affected by transitions. We need a program where we learn to appreciate the requirements for adjustment by all stake holders, including workers and their communities and where winners chip in to pay for the cost of such adjustment. In an era of renewed budget restraint, such a program can become an essential engine for further trade liberalization. If there are trade enhancing measures for which there is not sufficient public sector funding, perhaps the private sector can pay for further trade policy aims. After all, even free trade carries a price.

Chairman Manzullo, distinguished members of the Committee, thank you very much for the opportunity to share my thoughts with you and for your attention. I will now be glad to answer any questions you might have.

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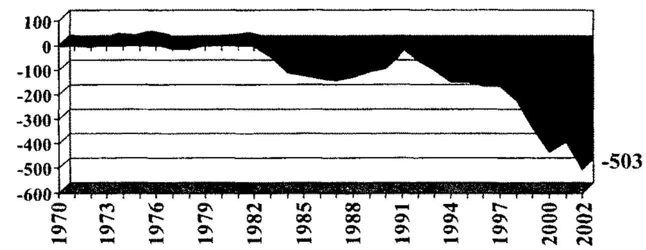
3. Michael R. Czinkota and Masaaki Kotabe, "Product Development the Japanese Way," Journal of Business Strategy, 11, November/December 1990: 31-36
4. Masaaki Kotabe, "Efficiency vs. effectiveness orientation of global sourcing strategy: A comparison of U.S. and Japanese multinational companies," Academy of Management Executive, 1999, 12,4, 107-119

Professor Michael R. Czinkota, Georgetown University

Exhibit 1

U.S. Current Account Balance, 1970-2002

$U.S. Billions



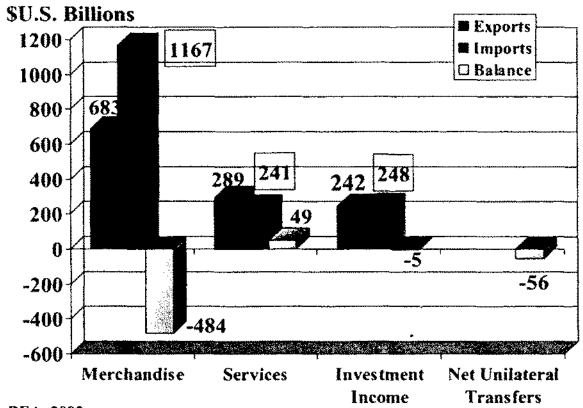
Bureau of Economic Analysis (BEA), 2003

Professor Michael R. Czinkota, Georgetown University

Exhibit 2

U.S. Current Account Components, 2002

$U.S. Billions



BEA, 2003

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Exhibit 3

U.S. Merchandise Exports, Imports, and Deficits 1978-2002

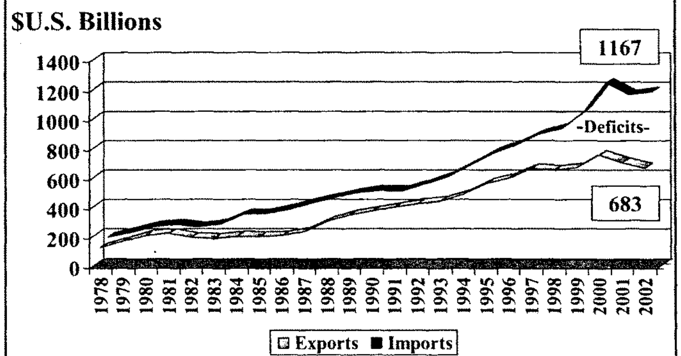

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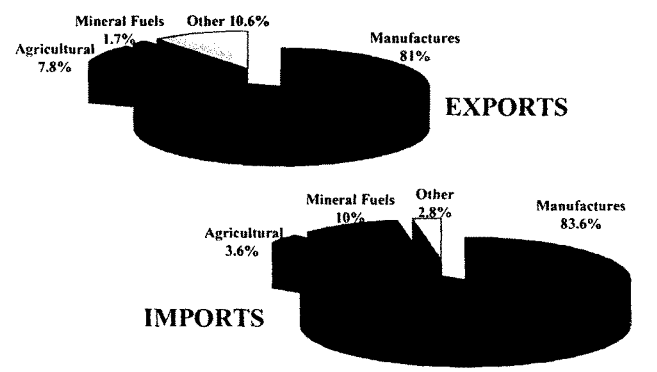
Exhibit 4

Composition of U.S. Merchandise Trade, 2002



Census, 2003

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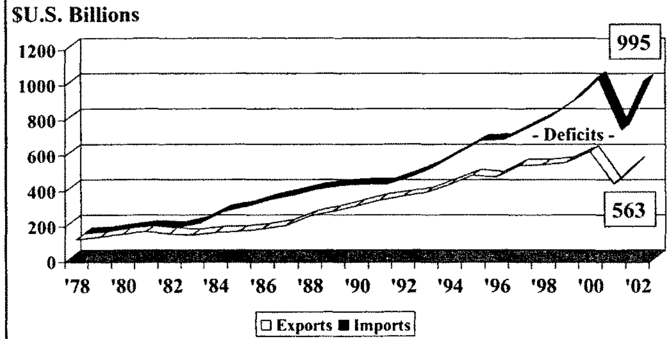
Exhibit 5

U.S. Manufactures Exports, Imports, and Deficits 1978-2002



Census, 2003

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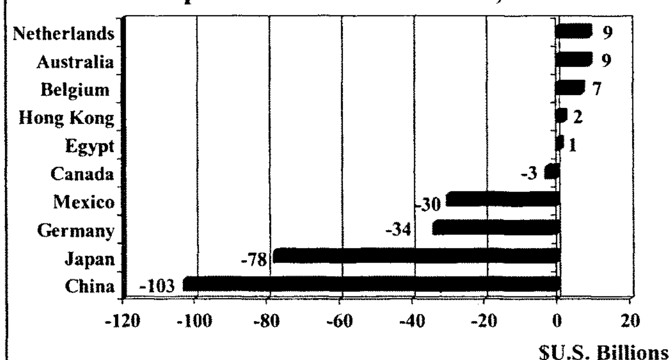
Exhibit 6

Key Manufactures Trade Imbalances for Top Surplus & Deficit Countries, 2002



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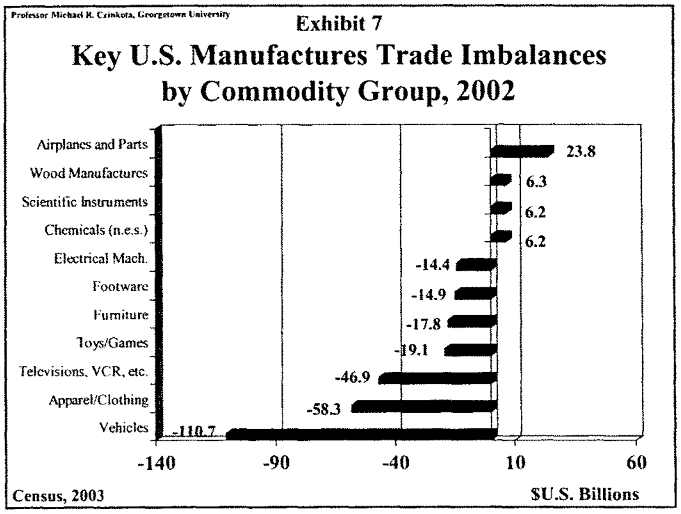
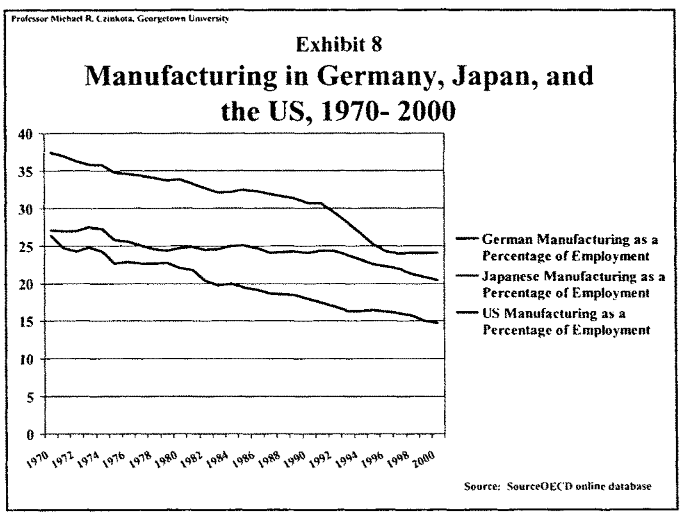
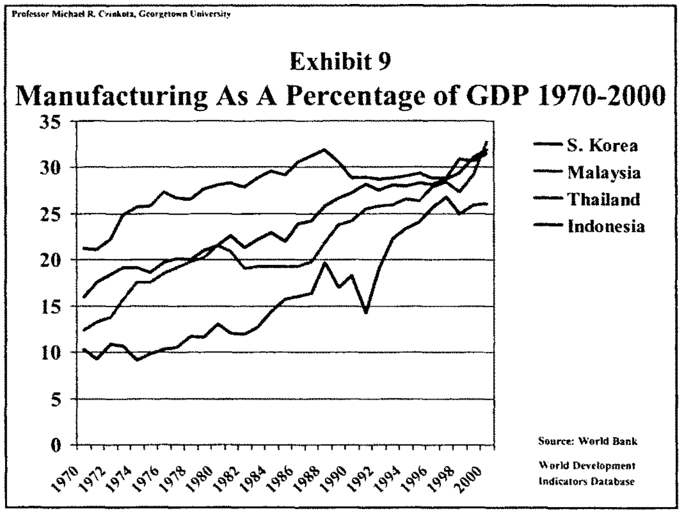

Professor Michael R. Czinkota, Georgetown University
Exhibit 7
Key U.S. Manufactures Trade Imbalances
by Commodity Group, 2002
Airplanes and Parts
Wood Manufactures
Scientific Instruments
Chemicals (n.e.s.)
Electrical Mach.
Footware
Furniture
Toys/Games
Televisions, VCR, etc.
Apparel/Clothing
Vehicles
23.8
6.3
6.2
6.2
-14.4
-14.9
-17.8
-19.1
-46.9
-58.3
-110.7
-140
-90
-40
10
60
Census, 2003
$U.S. Billions


Professor Michael R. Czinkota, Georgetown University
Exhibit 8
Manufacturing in Germany, Japan, and
the US, 1970- 2000
40
35
30
25
20
15
10
5
0
1970
1972
1974
1976
1978
1980
1982
1984
1986
1988
1990
1992
1994
1996
1998
2000
German Manufacturing as a Percentage of Employment
Japanese Manufacturing as a Percentage of Employment
US Manufacturing as a Percentage of Employment
Source: SourceOECD online database


Professor Michael R. Czinkota, Georgetown University
Exhibit 9
Manufacturing As A Percentage of GDP 1970-2000
35
30
25
20
15
10
5
0
1970
1972
1974
1976
1978
1980
1982
1984
1986
1988
1990
1992
1994
1996
1998
2000
S. Korea
Malaysia
Thailand
Indonesia
Source: World Bank
World Development
Indicators Database

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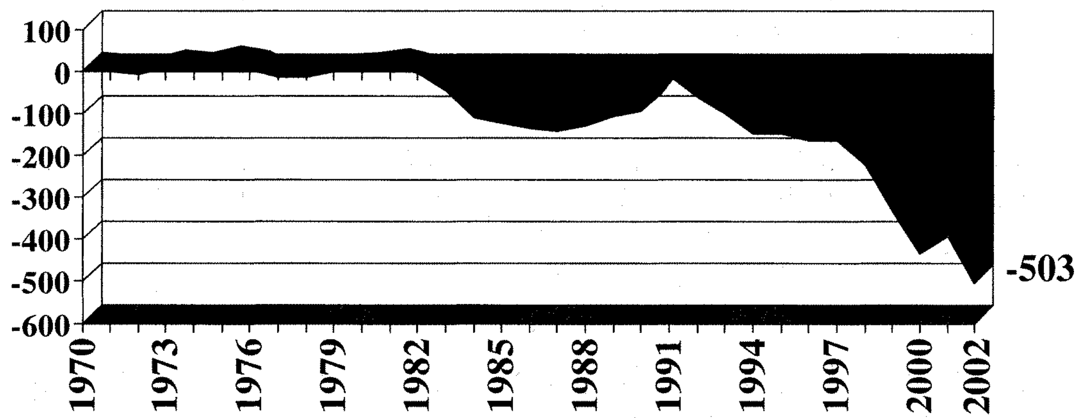

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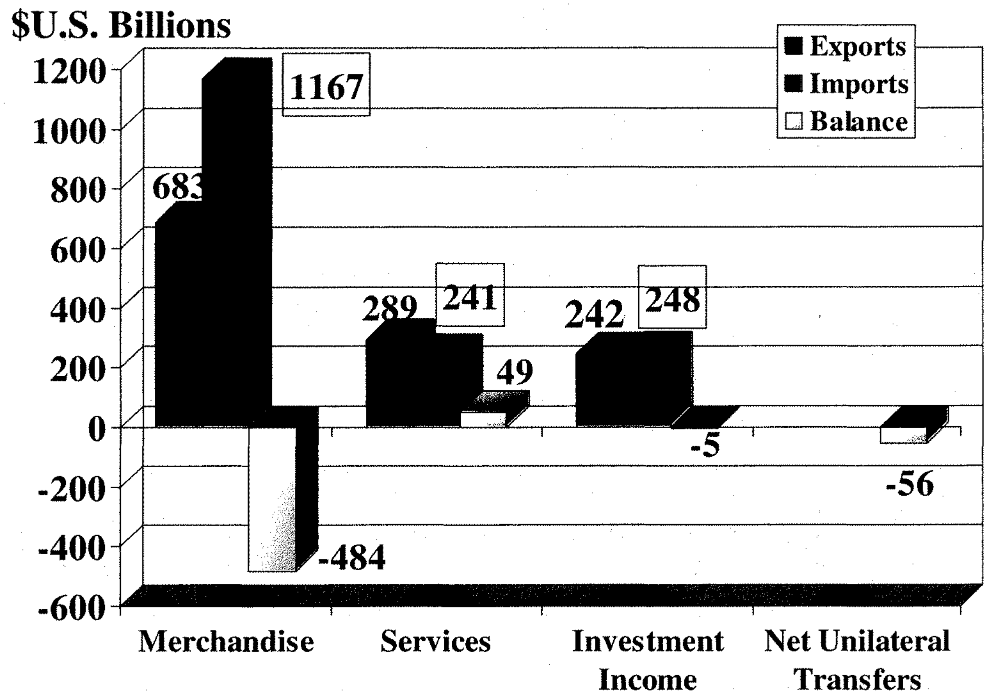

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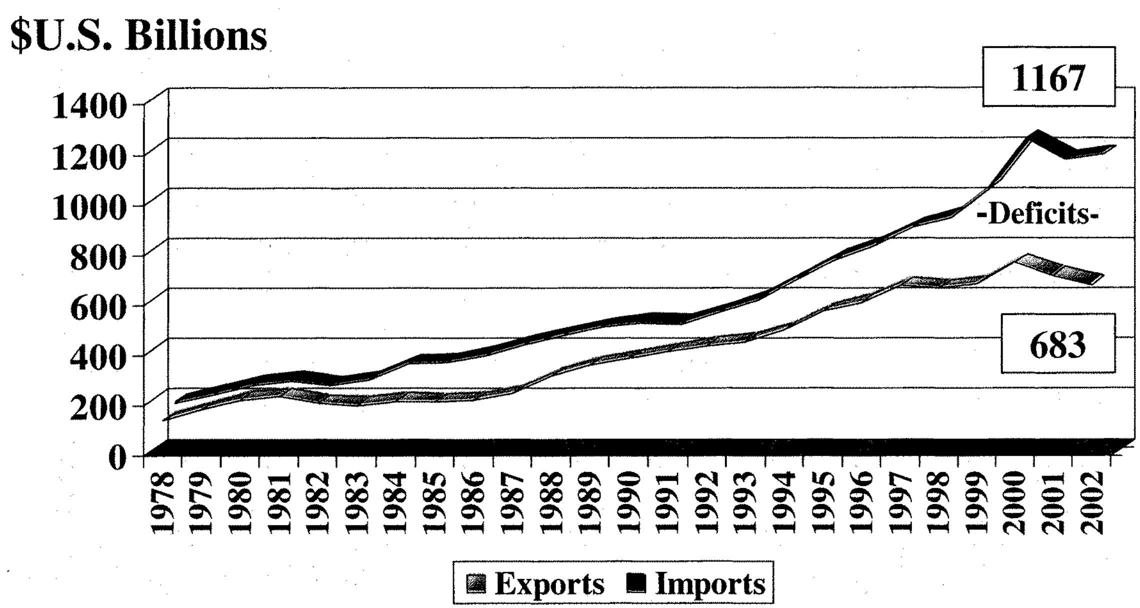

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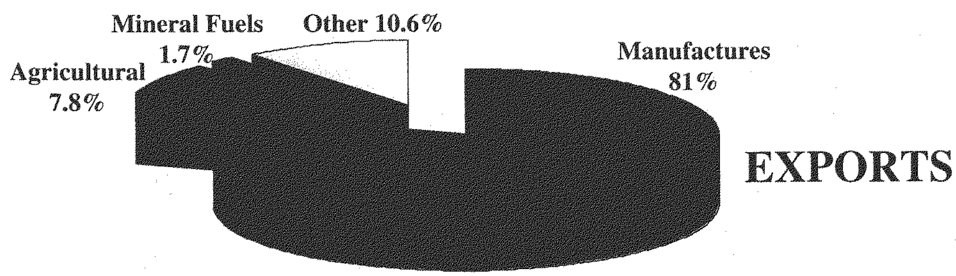

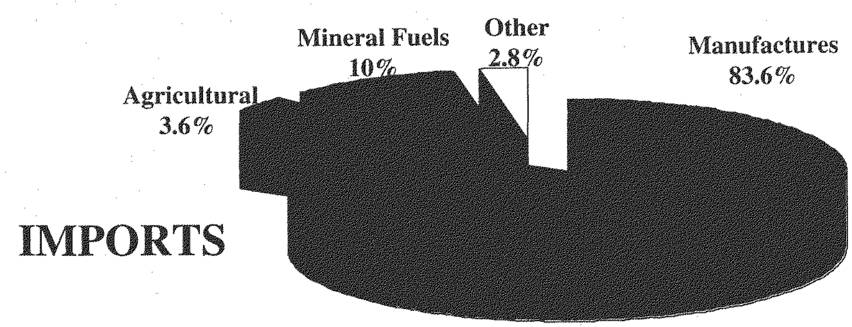

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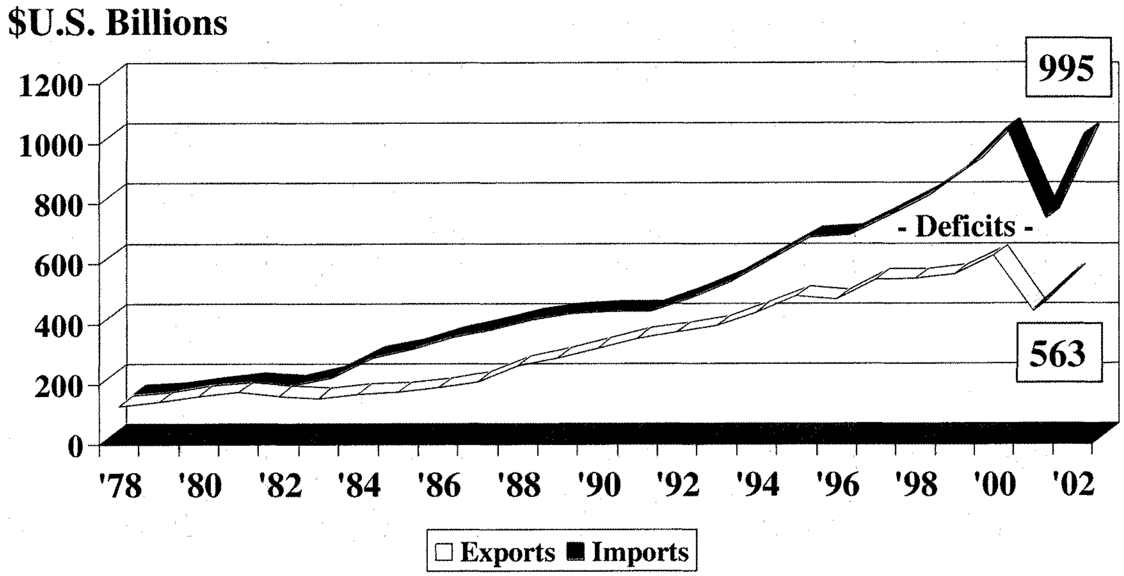
Exhibit 5

U.S. Manufactures Exports, Imports, and Deficits 1978-2002



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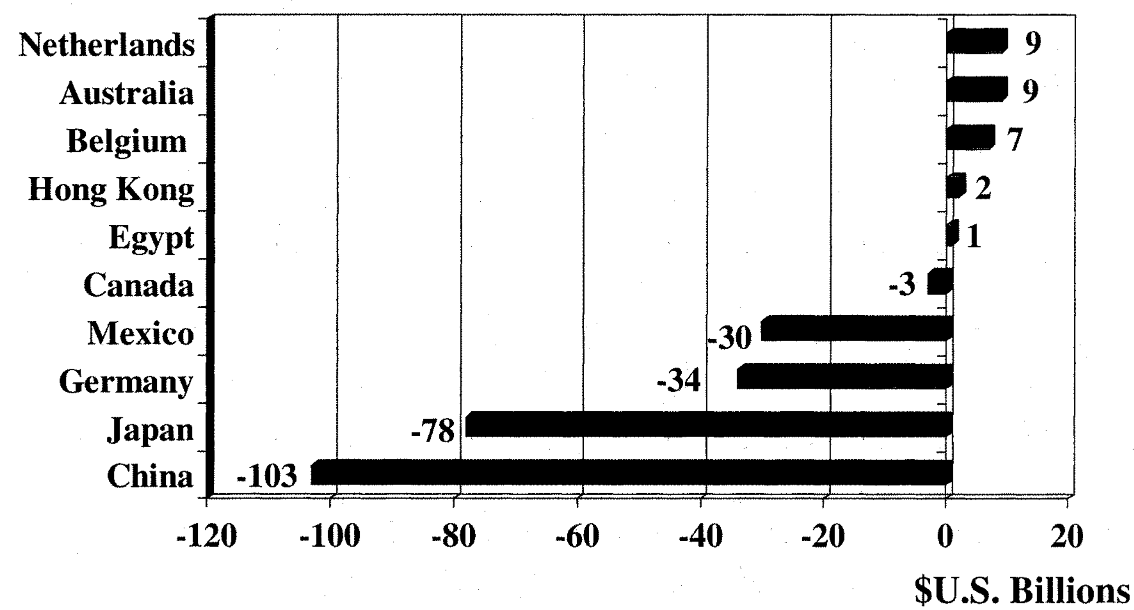

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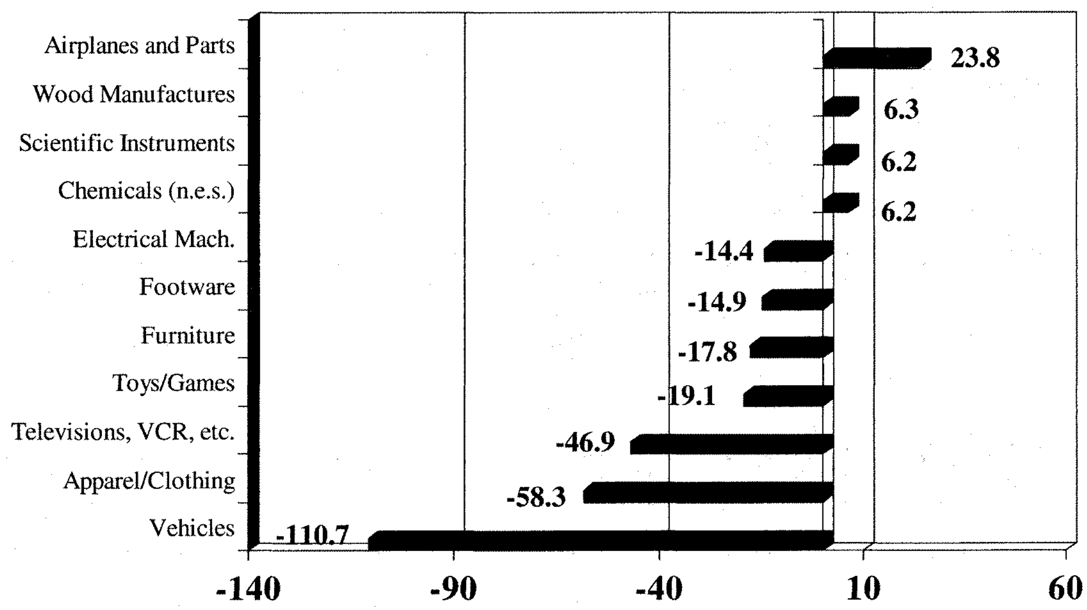
Exhibit 7

Key U.S. Manufactures Trade Imbalances by Commodity Group, 2002



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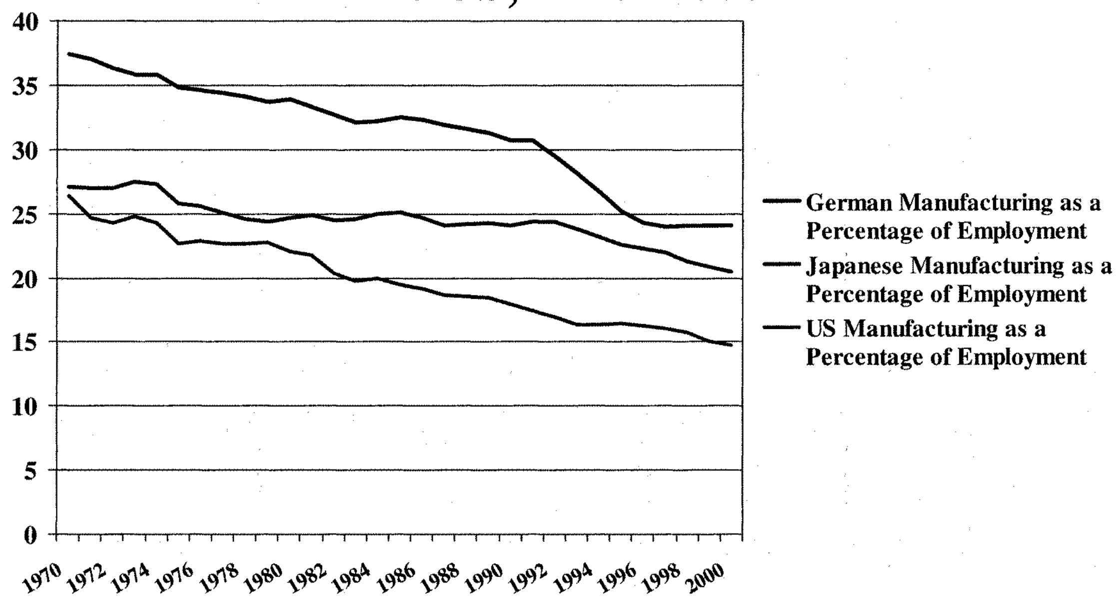

Source: SourceOECD online database

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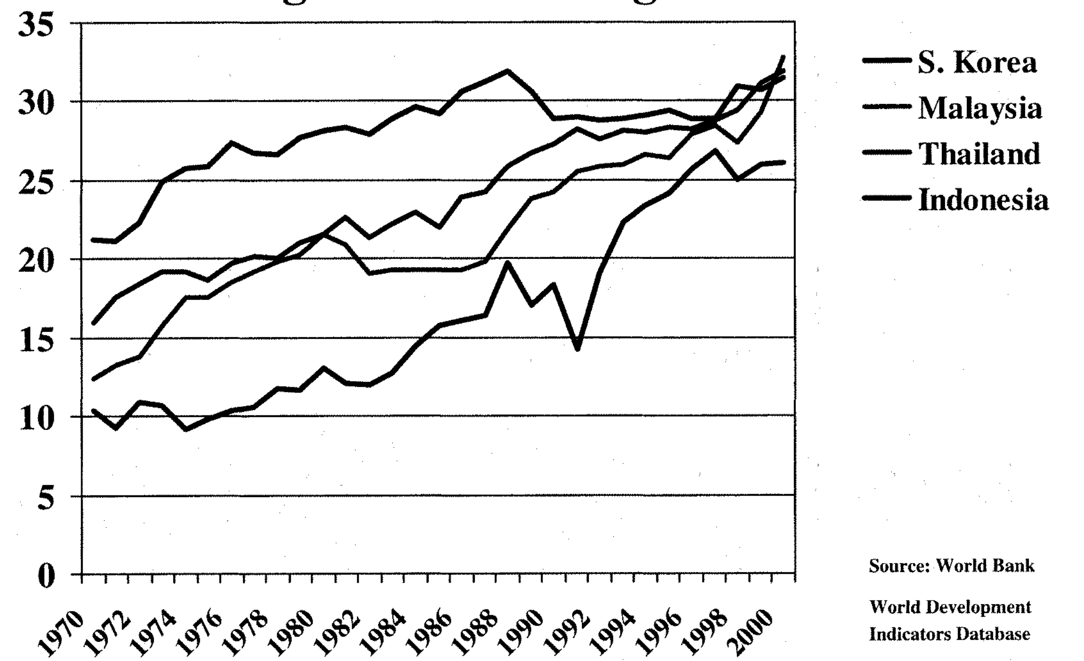

STATEMENT

BEFORE THE
U.S. HOUSE SMALL BUSINESS COMMITTEE

April 9, 2003

BY
Mr. DAVID SANDY
VICE PRESIDENT
M S WILLETT, INC.
COCKEYSVILLE, MARYLAND
On behalf of the
NATIONAL TOOLING & MACHINING ASSOCIATION
9300 LIVINGSTON ROAD
FT. WASHINGTON, MD 20744

Good morning. Mr Chairman, Ranking Member and Members of the Committee, I am David Sandy from Towson, Maryland. Thank you for the opportunity to testify on behalf my coworkers and the 2,000 member companies of the National Tooling & Machining Association regarding the state of the U. S. manufacturing and the tooling and machining industry.

But first I want to thank you Mr Manzullo and Ms Velazquez for your enduring support of our Industry. You have both been strong proponents for NTMA and you should be commended for it.

I'm Vice President of M.S. Willett, Inc. a metal working company that offers a unique blend of development, engineering, tooling and automation and production services. Willett is a family owned tool, die and metal stamping production company. Willett has two main focuses in its business, Production Metal Stampings and Automated Metal Stamping Systems. The company designs and builds quality tools, dies, metal stampings and assemblies. We're located in Cockeysville, Maryland, where we employ 120, and we do business all over the world.

What is tooling and machining industry? Tooling is, in its simplest sense, the means of production. "Special" tooling, such as dies and molds, is custom designed and made to manufacture specific products, generally in quantity, and to the desired levels of uniformity, accuracy, interchangeability, and quality. Machining involves the use of a wide variety of machine tools to cut or form material, usually metal to precise shapes and dimensions.

Why is tooling and machining important for to the United States? The broad industrial group known as tool and die includes stamping and trim dies (tools that stamp parts out of metal sheets), mold making (molds produce plastic parts), die cast dies (die casting means forming aluminum parts), forging dies (used to form hot iron and other metal pieces), tools and fixtures (used to hold pieces in place to perform additional manufacturing steps), precision machining (forming objects by cutting to specifications within .001") and many other manufacturing specialties. **These industries build the tools that are used as the building blocks of manufacturing. All mass manufactured objects begin at the hands of a tool and die maker.**

Nearly every manufacturing company in the country, in the world, does business with our industry. The U.S. tooling and machining industry employs close to 450,000 people nationwide and accounted for shipments in excess of $43 billion. The metalworking industry includes precision machinists, die makers, and mold makers, as well as tool and die designers. Without them, the mass production of manufactured goods would not be possible.

As we have heard today, the demise of US manufacturing and therefore the tooling and machining industry is accelerating at an alarming rate. Unlike typical business downturns of the past when manufacturers simply cut back and waited for recovery, in the current downturn manufacturers are rapidly relocating outside the US and large numbers of small and mid-sized US manufacturers are closing down permanently due to foreign competition. The resulting loss of family sustaining blue-collar jobs is undermining the US middleclass and devastating rural communities where manufacturing is essential to the local economy.

The International Trade Commission (ITC) has recently completed its (332-435) investigation on the conditions in the U.S. tooling industry and submitted their report to the House Ways and Means committee. The study paints a very bleak picture of the industry and the future of the US economy. The market is currently facing a problem with overcapacity. The overcapacity has been created in part because American companies are closing their U.S. manufacturing plants and moving offshore in search of fewer government regulations, lower taxes and cheaper labor. At the same time foreign companies are becoming more technologically advanced and are able to offer significantly lower prices, sometimes as much as 60% cheaper. The industry could see as many as 50% of the shops close their doors in the next couple of years.

As I testified at the ITC hearing Prior to January 2001, the average backlog in weeks was 48. Since January 2001, our average backlog has been 10, with occasional periods as low as three weeks. As a result, an average workweek before 2001 was 60 hours, and this has fallen to 42. Prior to January 2001, we used to quote jobs on an average of 20 per month, which usually netted us 30 percent of those quoted. This past year, we've quoted on 211. Now, we estimate we've lost at least four jobs to foreign competition in the last two years. Now, we're not sure, but we believe these went to China. Now, these jobs lost have cost us approximately a half-a-million dollars. This is money we could have used to invest on new equipment, training of personnel, improvement of our business in other ways, or paid to our employees in wages and benefits.

Another factor contributing to the problems of our industry is the exodus of American companies to other countries. For example, Black & Decker was once a four million dollar per year account for Willett. Today, it's a fraction of that, due, in part, to their business movement to China, Eastern Europe, and Mexico. Black and Decker executives have recently told us that in addition to closing their plant in Easton, Maryland that their plant is Fayetteville, NC will also be closing its doors in the very near future. All of the production stamping work which we did for Black and Decker will be gone within the next few months. We had a mutually successful relationship with Black and Decker for over 30 years. This is coming to an end because the work is going to be done in other countries. Ironically our plant is 5 miles from the corporate headquarters of Black and Decker in Towson, Maryland.

We had another account, Fedders Rotorex. This was a million dollar a year account, which we lost entirely to movement overseas. Now, the loss of just these two accounts has cost Willett tens of millions of dollars in business, and in March of 2001, we laid off 15 people.

I'll tell you about -- just a few other things that I know are hurting our company. First, there's the high cost of healthcare. Our cost today is over $350,000 annually, compared to 200,000 in 1999. The high cost of capital equipment. In the last three years, we've invested two million dollars. Overall economic conditions don't help. And just so you know it, we have suffered miserably as a result of the tariffs on foreign steel.

Congress needs to address the practices of the banking community as it relates to withdrawing working capital when asset-backed loans' value declines. I have heard more and more stories from members who have had their lines of working capital diminished or cancelled by their bank.

In our case, our lender has requested that we find another bank. They are in the process of upgrading their portfolio with less risky loans. Banks are reluctant to extend working capital loans to manufacturing companies such as ours. Asset backed loans are the norm and increasingly more difficult to obtain due to the devalued market for used equipment which is our principle asset.

Overall, I believe there has been a concerted effort by banks, both national, regional and local, to no longer maintain a loan portfolio in this industry, because of the decreased margins due to the Southeast Asian competition.

ECONOMY

The tooling and machining industry is critical to our country's economic health as it makes possible the existence of virtually every other manufacturing industry. The U.S.'s economic strength has been based on its manufacturing capability. In order for these companies to continue to improve and grow they have relied on innovations in manufacturing that are brought on by the tooling and machining industry. If we are to continue to grow economically we need innovative American companies. However, as the market continues to falter for the industry, fewer companies are open and thus a large percentage of the creativity and innovations are lost

The broader U.S. economy is suffering as well because manufacturing does more than any other sector to stimulate the economy. The average income of $44,700 for an employee and the consequent spending power of manufacturing workers is higher than that of any other sector and, due to its high multiplier effect, manufacturing directly or indirectly generates more jobs than any other sector. The manufacturing sector and the non-manufacturing industries that are directly linked to manufacturing, account for 45 percent of U.S. GDP and 41 percent of national employment. But as we see the closure of business, many of the new jobs created by small manufacturers in recent years are being permanently lost.

NATIONAL DEFENSE

However, as important as this industry is to the economic well being of the country, it is even more important to our national security. A healthy industry is an important component of defense production capabilities. We are the companies that produce the plastic injection molds that are used to build nuclear submarines, the ones that provide parts for our missile defense system, the wheels and joints on airplanes, the parts used to make rifles for our infantry.

Increasingly, defense prime contractors are subcontracting parts and tooling for defense systems to Asia. This practice is not being monitored by the Department of Defense and as a result the military is becoming dependent on foreign sources to supply critical parts and systems for weapons. I applaud the Chairman and Ranking member recognizing this as a problem. Your request for an investigation by GAO into this could prove to be an invaluable tool in fixing this situation.

We are aware of defense contractors subcontracting to foreign companies for precision machining jobs. Take for example the recent west coast longshoreman strike. Suppose a part was needed for a critical military weapon, the needed part would have been delayed somewhere off the coast of California. In this day and age, can we allow our country to be dependent on foreign nations to provide us with the parts needed to keep the very weapons that protect our nation operational?

Raising the Limits for Direct Expensing

Raising the limits for direct expensing would allow small tooling and machining companies to expense (fully deduct from taxable income) a limited amount of the cost of new business equipment in a year. Under current law, our small companies can expense up to $24,000 in a year for 2001 and 2002 and $25,000 a year for taxable years 2003 and beyond. This tax benefit is limited to small businesses by a provision of the law, which stipulates that the expensing amount is phased out dollar for dollar for any amount of investment above $200,000 in a given year. Under the current law, since the expensing caps have not been indexed and therefore their value has decreased overtime, too many members of NTMA are unable to take full advantage of Section 179. The bill solves this problem by increasing the expensing limit to $40,000 and the phase out to $325,000.

Increasing the expensing limits will entice our member companies to purchase new equipment and machinery. Raising expensing limits under Section 179 will encourage businesses to invest in new equipment and machinery.

Permanent Repeal of the Death Tax

On June 7, 2001 President Bush signed the bi-partisan "Economic Growth and Tax Relief Reconciliation Act of 2001" which included the elimination of the estate tax. However, because of the budget rules, the estate tax cut in the new law will "sunset" in 2011, one year after it is fully repealed.

The estate tax provisions enacted provide relief to businesses by bumping up the exemption and lowering the rates. The repeal provision does nothing to help small business. Unless it is made permanent, small business owners are still faced with estate planning challenges.

Skilled Workforce Enhancement Act

The Skilled Workforce Enhancement Act will give small employers, those employing 250 employees or fewer, the needed incentive to train individuals. It will provide financial encouragement to help employers bridge the gap as newly hired, relatively unskilled and unproductive apprentices are trained in the classroom, and on the job, to become highly skilled and highly compensated members of the American workforce. The amount of the direct tax credit to the business would be $15,000 per employee, per year.

Contract Bundling
From FY 1992-2001 the Department of Defense bundled over 55% of contract dollars appropriated to them. By taking several small contracts and rolling them into one larger one, they are freezing out many of our small companies that are not capable of performing these larger orders.

Legislation in previous Congresses have been introduced that would amend the Small Business Act to require the Administrator to submit certain disagreements to the Director of the Office of Management and Budget for resolution, and to establish a minimum period for the solicitation of offers for a bundled contract. We support efforts that allow the U.S. government to contract to all American companies, not just large ones.

Association Health Plans
Currently, small businesses and the self-employed do not have the advantage of spreading their health insurance costs over large numbers of people, as do health plans sponsored by large corporations. Corporate and union plans have economies of scale, substantial bargaining clout, administrative savings from regulatory uniformity, and greater health plan design flexibility. Small businesses do not have access to these advantages.

AHPs will rectify this inequity by allowing small businesses and the self-employed to participate in health plans sponsored by bona fide trade and professional associations under rules similar to those for corporations and unions. This will provide workers with the benefits of economies of scale, more bargaining power with large insurance companies, and savings from other operating efficiencies. The bill also contains strong new solvency standards and other consumer protections that will ensure that their benefits are secure.

It is time to level the playing field in health care benefits between America's Main Street small businesses and large corporations by enacting the Small Business Health Fairness Act.

Reliable Tracking Of Dies And Mold Imports
Enhance quantification of import data related to tools, dies, and industrial molds. Limitations in HTS statistical data were identified in the International Trade Commission's ("ITC") recent study on Tools, Dies and Industrial Molds ("TDM"). *See Tools, Dies, and Industrial Molds: Competitive Conditions in the United States and Selected Foreign Markets,* U.S. International Trade Commission, Inv. No. 332-435, Pub. 3556 (October 2002). The ITC reported two principal classification issues: (i) that quantity data are not collected for many TDM; and (ii) that the HTS is inconsistent in classifying TDMs and TDM parts and sub-assemblies. *See id.* at 3-39. Thus, the ITC reported that "[t]these classification issues affect import value data as well as quantity data, and explain industry concerns regarding the validity of import data [for these products]." *Id.* In short, the absence of accurate, relevant import data prevents interested parties from assessing the current conditions of the global TDM market. Congress should enact legislation that fixes the problems raised.

Sound Dollar Congressional Coalition
The sound dollar is a fundamental pre-requisite for the difficult climb out of this recession as well as maintaining a healthy U.S. and global economy. A sound dollar is one whose value relative to other major currencies is determined by market forces that reflect fundamental economic trends, such as trade balances, interest rates, GDP growth and other objective indicators of a country's performance.

Six years into a dramatic surge in the value of the U.S. dollar, U.S. manufacturing and agriculture are under siege, particularly by nations utilizing currency intervention and undervalued currency pegs in order to inflate exports and protect their domestic markets. Last year in Alberta, President Bush set a clear course for the Administration's approach on exchange rates when he called for the dollar to "seek its level based upon market forces." Prominent among the benefits of this approach, as described by the President was the "revitalization of the U.S. manufacturing base".

Since that time the U.S. dollar has gradually declined from its extremely overvalued level. The dollar peaked in February 2002 at 30 percent above its normal level. Today it is still more than 15 percent above its normal level. While that is a great improvement, the dollar still has to decline significantly just to reach the average that prevailed after the "Plaza Accord" of 1985 that sought to stabilize exchange rates near their equilibrium levels.

Most of the improvement, however, has resulted from the gradual appreciation of the euro from its very undervalued levels. There has been little upward movement of Asian currencies, principally due to deliberate steps taken by their governments to hold their currencies at rates lower than those that would be determined by market forces.

Japan, Korea and Taiwan, which represented about $100 billion of our trade deficit last year, have practiced widespread blatant currency interventions multiple times in 2001 and again in 2002. China, which represented another $100 billion of our trade deficit last year, has an artificially low fixed exchange rate that boosts its manufactured exports and retards imports.

We also urge you to pressure the Treasury to publicly condemn currency manipulation and intervention by countries seeking to gain trade advantage at U.S. expense through efforts to contravene the working of market forces in currency markets, and that it seek bilateral consultations at the highest levels with China, Korea, Taiwan and Japan on these interventions/manipulations.

In conclusion, the average age of workers in the tooling and machining industry is 50+ years of age. As the current workforce grows older and fewer people are trained, America stands to lose an industry that is the bedrock of economic stability and wealth creation. There needs to be emphasis from Congress and the Administration on promoting manufacturing to our schools and communities as a rewarding career and vital for healthy economy and national defense.

As we have heard today manufacturing in the United States is suffering and I believe undergoing a radical transformation. The world is shrinking and we are facing competition and demands that we never dreamed of twenty years ago. Congress and the President as our elected officials need to help us survive by leveling the global playing field.

COMMITTEE ON SMALL BUSINESS
U.S. HOUSE OF REPRESENTATIVES
APRIL 9, 2003
WRITTEN TESTIMONY OF ERIC ANDERBERG
GENERAL MANAGER OF DIAL MACHINE, INC.
ROCKFORD, IL

Introduction

Good afternoon and first off thank you Mr. Chairman and members of the Small Business Committee for the opportunity to be here today and to represent fellow small manufacturers at this hearing.

Pursuant to House Rule XI, clause 2(g)(4), I am required to report to you that Dial Machine has received $36,400 in fiscal 2003 from the United States Air Force for a fixture.

My name is Eric Anderberg and I am here to testify on behalf of my family business, Dial Machine of Rockford, Illinois. Dial Machine for the last thirty-seven years has provided contract machining of medium to large component parts for various capital equipment manufacturers from the construction and machine tool industries to aerospace, military and nuclear. We also manufacture and provide precision grinding machine tools for the same industries through our machine tool division. We currently have around forty employees at our organization; this number is down nearly fifty percent from five years ago.

The Rockford area has been hit quite hard by the reduction in the American manufacturing base and its employment, as Rockford has historically been a manufacturing town with better than 30% of its employment being directly tied to manufacturing.

I personally conducted a survey of over 200 small manufacturers in the Rockford area earlier this year. In the responses to the survey, 79.8% of small manufacturers said their sales have declined and 76.8% said their employment has decreased since 1998. Only 19.2% expect to hire additional workers this year, 13.1% will decrease their workforce and 66.7% expect their employment to stay the same. The news is not good from Rockford for small manufacturers.

On April 4th, the Department of Labor published unemployment data that showed there was a loss of 36,000 manufacturing sector jobs in March alone and that our industry has lost more than 2.2 million jobs since April 1998. These skilled workers that helped to produce the machines, components and end products in the U.S. for our economy and for our national defense are now scraping by on part-time service jobs with no benefits, health coverage or even a decent living wage.

The Net Effect

I know of one personal story of a gentleman that our company had to lay off because of lack of work that I would like to share with you. I realize that many of the members on this committee have very little if any manufacturing in your respective districts, and you are probably wondering how the decline in manufacturing affects your district. I believe that this story of one of my former employees will tie together this relationship.

The gentleman I speak of was laid off about two years ago from Dial Machine. Today he currently works at a national home improvement box store in Rockford. He has told me that he makes $7/hour at this store and he doesn't get any benefits because he isn't considered as full-time employment as he works less than 40 hours per week. This is a reduction in hourly pay of about half as he made $15/hour as a toolmaker at Dial Machine, plus we provided him with health insurance coverage, a 401K plan and full time employment.

This gentleman and his wife purchased a house about five years ago, she also works and it takes a lot more of the both of them to make ends meet and to make their mortgage payments. The net effect of losing his skilled manufacturing job at Dial Machine and having to work in the service sector is clear, at $7/hour and no benefits, how many vacations will this man and his wife take? How many airline tickets will they buy? How many hotel rooms will they stay in? What kind of insurance premiums can they afford? How will their weekly grocery bill be budgeted? What new automobiles can they afford? What new high technology computers, appliances, software or gadgets will they buy? How do they pay for health coverage? How many restaurants will they dine in over the course of a year? What amount, if any taxes will they pay State and Federally?

An owner of a very reputable restaurant adjacent to the industrial park that our company is in, told me last month that his business is down over 40% over the past two years and that this is consistent with the restaurant industry as a whole. He went on to tell me how he has seen many of his former lunch customers around town, and has asked them why they haven't been in his restaurant? The answer is consistent: "I lost my job, I got laid off!" I know that my former employee used to frequent this restaurant, he is obviously one of many in our area that no longer dine at this restaurant, the means to do so aren't there anymore.

The trickle down effect on the American economy is clear. Take the Labor Department's figures of unemployment and multiply this one example by 2.2 million, and it is clear what effect the loss of living-wage paying manufacturing jobs in the U.S. has had on our economy in aggregate. It is also the reason; I believe that the American economy will not recover without having a successful, sound manufacturing base.

The Cause

How did the manufacturing base in the United States get into such a terrible position? The answers and the reasons to this are many, and it would take countless hours to explain and argue. However, when I sit down every day and think about this situation and its causes, I discover there is a core or a center to the problem, and that core is here in this building in Washington D.C.

This very building, legislated all the rules, regulations, agencies, taxes, bankruptcy codes, tort law and governmental burdens, that we as manufacturers have to live by in America. This very institution controls our policies of export controls and the barriers to sell our goods abroad. This institution has taken away much of the incentives to invest and to manufacture in this country. This institution has made the cost of doing business in America, especially manufacturing very, very high. This institution then opened up our doors in America to unfettered international trade and left us in an uncompetitive position. Which leads me to a question that I would like to pose to this committee of congressmen. Did you, our congressmen, when approving the free trade initiatives really believe that we as small or mid-sized manufacturers could compete? When all of the fixed costs of government were placed upon us, did you think that we could compete with underdeveloped countries or with subsidized industries abroad? It astounds me that you wouldn't of thought that we as manufacturers, especially small, could compete with countries and governments that have no real rules or standards to bear in their industry.

We as manufacturers are at a disadvantage at the offset. American manufacturers, in effect have fixed costs laid upon us by our government that we cannot cut, we have no control! It is no wonder that the large Multi-National Corporations have fled their manufacturing facilities in America to seek out cheaper costs to produce abroad. The large multi-nationals have done this and they have done it under the guise of the free-trade initiatives and have left their employees, their vendors (small manufacturers) and their country holding the bag. At the same time they exploit cheap foreign labor and enjoy lax or non-existent regulations where they operate and ship those products back to the U.S. enjoying huge margins. In my view, it is a short-term scheme and one focused more on producing shareholder value for today than on producing product or maintaining long-term viability of their organizations for tomorrow. The free trade initiatives ended up being a vehicle for the large multi-national corporations to exploit no standard, cheap production and to fleece America of its wealth, employment and eventually its global economic status. I know some of congress is aware of this, especially Chairman Manzullo, as I have read the letter that he sent out last year addressing this situation to these large corporations.

Multi-National Exploitation

The only word that really describes what the multi-national corporations have done is exploitation, exploitation of the countries that they have fled to and exploitation of the American consumer market and their American suppliers.

I would like to provide one example of how this has affected Dial Machine. One of our customers is a medium sized manufacturer of components for the wind turbine generator industry. In a meeting two weeks ago, I was informed by the plant manager that Dial Machine would lose about 60% of the work we are doing for them because their customer, an American multi-national corporation (MNC) is demanding cuts in pricing. This work will now be done in the Czech Republic for half the cost of what we can do the work for and also our customer lowered the quality standards of the parts from the Czech company. Further their MNC customer told them that if they did not start to move operations or start sourcing from China, that they would lose their business with them, which happens to be 100% of my customer's output. What is really upsetting, is that the MNC produces large wind turbine generators for the United States market. The reason that there is a market for large wind turbine generators in the U.S. is the Production Tax Credit that was passed in the last Energy Bill by Congress. The Wind Energy Production Tax Credit gives the utility that installs the wind turbine a 1.5-cent/kilowatt hour Production Tax Credit. This makes wind energy competitive and actually more profitable in comparison to other sources of energy. So the taxpayer, the machinist who works on these parts, who could lose his job and will definitely have his working hours cut, will be subsidizing the greater profit of the MNC, because the pricing of the end unit has not come down. This is just one of too many stories and a good illustration of how the MNC's benefit from government policy at the expense of the taxpayer that they have abandoned.

A New Economy?

After submitting these arguments of unfair trade, exploitation, an uneven playing field and the high cost of manufacturing in America, many point to the fact that our economy is evolving and that we are moving out of a manufacturing economy and into a high technology/information age economy, otherwise touted as the New Economy. When thinking about those statements, I have always wondered what exactly is a technology or an information economy, what is the New Economy? And by that what exactly is the Old Economy? I have always believed that what we do in the manufacturing sector is high technology. Our company for example produces high-tech precision components for various industries. The more that I have thought about an economy based on technology I can still not see how the U.S. can develop or apply technology without manufacturing. Without the means to apply technology, what good is it?

Further the fact remains today that as manufacturing disappears, so does the engineering skill and the pool of engineering expertise. If there is no manufacturing, where will the engineers work to create new technology? China? Mexico? For example, information supplied to me by this committee's staffers claims that the percentage of college graduates today in engineering is about 6% in the U.S. where in China where they consider manufacturing to be their "core" the percentage is around 36%. How will the United States develop High Technology with so few engineers graduating from our colleges when China is graduating so many?

The fact that manufacturing is passé in our economy is false. Manufacturing is High Technology and we are the lead generator of wealth for the economy in terms of per capita output. Manufacturing is not only vital to our economy's strength it is vital to our Nation's Defense. What will this country do when all of the manufacturing is offshore and we are a 100% service economy as predicted by academic economists? How strong will America be when we will not be able to build the goods and armament necessary for our defense? If you stop and think about it, it is a scary proposition.

For example, everyone is proud of the cutting edge technology that was developed to produce the B2 Stealth Bomber. A key part of that technology is how the B2 is constructed with carbon fiber and carbon tape. Currently there are only two "Old Economy" companies left in the United States that have developed the High Technology machines that place the carbon fiber and lay the carbon tape to produce the wings, fuselage and main components of the B2. These "Old Economy" machine tool companies are Cincinnati Machine of Cincinnati, Ohio and Ingersoll Milling Machine of Rockford, Illinois. Unfortunately, both companies are hanging on by a thread, because of the many reasons I have already discussed and the fact that these companies cannot compete without a domestic manufacturing base and the weight of the costs applied to them by our government. If these companies fold, where will that technology and the equipment come from to build future B2's? China? Taiwan?

What Needs to Be Done

As you will hear today the manufacturing base of our economy is in deep trouble. How do we fix the situation? What can be done? I believe that the government needs to examine the policies that have put us in this position; unfortunately I believe that this will take more time than what our manufacturing base has left to survive.

The Tax Policy, our government needs to create incentives to keep manufacturing here and to not drive it out. Tax incentives need to be in place to give incentive for investment of capital equipment and improvements, but these incentive policies alone will not work without handshaking with trade reform. If there is no manufacturing or work left in the United States, tax incentives or tax cuts are useless.

The Trade Policies, particularly the Free Trade policies need to be examined and the problem of the widening trade deficits need to be addressed. The effect of the trade deficit is a deficit of employment and work in this country. Why aren't our supposed free trading partners buying our products? We need to have this addressed immediately and our partners need to reciprocate in trade.

Government Procurement Policy has to change to make sure tax payer dollars are being spent with taxpayers, it only makes sense for our government to keep dollars in the American economy employing American taxpayers.

Government must remove some of the roadblocks that it has created and those created by our foreign competition. The government must examine Export Controls and break down the barriers that it has created to get product out of this country. On a recent trip to China, Chinese officials told me that the Japanese and the Europeans use American Export Controls as a sales tool against American companies. Also, this country needs to enforce better currency valuations, other countries have kept their currencies devalued and it has been absolutely devastating to American manufacturing. We cannot sell to foreign countries, nor can we compete when our competition keeps their currencies valued so low to the U.S. dollar.

Regulatory Policies need to be raked over. From tort reform to reforming the way autonomous governmental agencies interact with American manufacturing needs to be changed. Why does the EPA have to sue companies that may have polluted pre-Superfund? Why can't the United States have good environmental practices and an agency that works with, instead of against American manufacturing. I cannot believe that our government considers the EPA to be an effective agency, when over 75% of the monies garnered from litigation go to "administrative fees" and the remaining actually goes to clean up.

The government also has to urge, either through incentives or penalties that MNC's source American and manufacture in America. As demonstrated earlier, as MNC's move offshore the trickle down will continue to dislocate the skilled manufacturing workforce in America and our economy will remain in the doldrums. As already evidenced on a micro level, the standard of living in this country will decrease as this country only sells what it buys and not sell what it makes.

China, a Solution?

As I stated, the suggestions above will take a lot of time to come to fruition. American manufacturing does not have the time left to wait for the government to change these policies, we need an answer and a solution now.

A month ago three other small manufacturers and myself returned from a trade mission to China. We were fortunate enough to have staffers from the Small Business Committee and the Speaker's district office with us on our mission. There were two businessmen from each district on the trip. The focus of the trip was to investigate and to try and procure business from China for small American manufacturing. For the most part small manufacturing has been frozen out of the China market by government regulations, export controls, lack of capital and by MNC barriers that have been erected.

What we discovered when we were there is an economy that is on the brink of an explosion. The China that I witnessed was much different then what I had expected. China is embracing the foundations of creating an open market in their country and the opportunities for American small business, especially small manufacturing is immense. I was extremely impressed with the fact that most of the top government and provincial officials either had an engineering degree of some discipline or were involved in manufacturing of one form or another. I think that this point drives home why industry is so important to the Chinese, because they have leaders in their government that understand industry's economic importance.

The Chinese truly understand the importance of industry to their economy and are making capital improvements a top priority. The Chinese government will be spending over $270 Billion U.S. on capital improvement and infrastructure projects this year alone. They will spend over $1.5 Trillion U.S. within the next five years. In one province alone, the Henan province, the government is going to build over 6000 miles of roads and highways in the next 5 to 10 years, remember there are 35 provinces total in China. The amount of capital equipment and infrastructure spending is truly mind-boggling. China in the same 5 to 10 year time frame is planning on building at least 50 airports, numerous subways, oil refineries, pipelines, railways, etc.

I believe capturing China's business is one of the keys for our American manufacturing industry to survive. And being that both the United States and China are large countries with similar geography, resources, and demographics, American ways of building airports, highways, subways, oil refineries and rail is more suitable for China than competitors from Japan, Europe or anywhere else for that matter. The presidents and executives of the major Chinese corporations that we met during our trip echoed this sentiment.

It was clear in our meetings with Chinese government and business leaders, that business is conducted in a different way in China. In China, much attention is provided to consensus and politics. This is a hurdle for individual small American manufacturers to overcome that will take much time to cross. While our MNC's have years of time and resources to develop their Chinese business, our smaller companies do not.

On our trip, we decided that the best way for us to procure business from China was to band together and form an association amongst us to offer our products and services to the Chinese executives that we met. In doing so, we took on an approach that didn't just represent our own companies, but all small American manufacturing. The concept worked, as our group signed Letters of Intent with two provincial trading groups worth $44 million U.S. These Letters of Intent are a pledge and an offer to get small American manufactured products into China. Fortunately, the Chinese government understands what is happening to our economy, and I believe that they understand our situation much better than our own government, the

MNC's and Wall Street. On this trip, we discovered that the Chinese are eager to buy American, but their access to our products is restricted. Yes, our congress opened the door to free trade but it hasn't done enough to let small business out and to participate in the Chinese explosion.

The Chinese view the European Union as freezing them out of the European market. China's past and current relationships with the Russians and the Japanese leave them lukewarm at best in wishing to conduct business with those countries. The Chinese officials told us that they see the U.S. as not only their biggest trading partner, but also their most important bilateral relationship on the globe. The Chinese are ready to reciprocate with real orders to American small manufacturers. The question is what can we do as small business and what will our government do to help us get there?

USCBA

Upon our return to the United States, our group decided to start the process of forming a non-profit association, the United States-China Business Association. This association will be made up of a qualified, paying membership of only Small American Business. The association will operate a unique model to ensure all member companies have a chance to bid on legitimate business from China, and competing not against the world, but against only other American companies. We will pursue more of the $1.5 trillion in projects over the next five years that we learned of and have already been given over $40 million of capital and infrastructure improvements for American companies to quote.

How will this association work? By uniting American companies, we are pooling together all the resources and expertise to win the major infrastructure and capital improvement projects in China. And for each project, we will divide it into multiple pieces so that member companies may bid for it. When an award is given to the USCBA, the association will disseminate the contracts to the winning associate members, work with the banks on the letters of credit and establish the financing and logistics for the members. In essence, through the USCBA, doing business with China will be relatively painless and relatively risk-free for small American business, it will be a lot like doing work for another American company. Also, the winning bidders must buy parts, tools and services from other association members, whenever possible.

Our group has put a lot of thought and effort into getting this association together. It will only work with the support of both the United States and Chinese governments. As I stated earlier, the Chinese understand what is happening to our economy and our manufacturing sector and they are concerned. They are concerned that if the trade imbalance isn't fixed, that our government will act to stop the gap. Our Association and our small manufacturers need the political leverage from this situation from our government to make sure that the Chinese come through on their commitments that they are making to us. Right now we are currently registering the USCBA in the State of Illinois and intend on starting bidding on Chinese projects yet this spring. While this is not the only solution to the manufacturing crisis in this country, it is one of the greatest opportunities that we as small American manufacturers have to getting a piece of that China market.

Again, thank you for the invitation to participate in today's hearing. I look forward to answering any of the questions you may have about the topics discussed here today or of any of the particular questions you may have about the USCBA.