Trade Works[SM]

The Publication that Reveals How International Trade Works for Companies, Workers and Communities

Fall 2002/Winter 2003

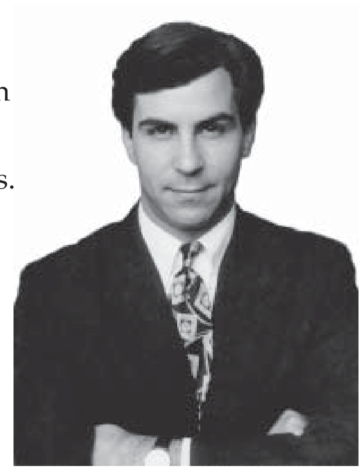
IN THIS ISSUE

Sponsored in part by The Business Roundtable

Distributed in association with *The Exporter* magazine and www.exporter.com

MANZELLA
TRADE COMMUNICATIONS, INC.

Dear Friends:



Welcome to the Fall 2002/Winter 2003 issue of *Trade Works,* a publication that features current trade issues and provides an understanding of the full impact international trade has on our workers, companies and communities.

Trade Works offers valuable information to employees on how trade supports their jobs and quality of life, to Members of Congress on the importance of supporting trade policies, and to the media on the positive impact of international trade.

Trade has been a vital factor in U.S. economic and world growth. And in addition to being a primary generator of business and job growth, trade also affords consumers greater disposable income, improving their standard of living.

However, through a variety of sophisticated tactics, anti-trade groups are increasingly disseminating misinformation. Consequently, a growing number of our Congressional Representatives are voting against important trade liberalization legislation. In this issue, Daniel Griswold, Associate Director of the Cato Institute's Center for Trade Policy Studies, reveals three disturbing trends in Congress.

While those who oppose trade bombard Congress, the media and the public with their views, there is little reader-friendly analysis on trade's positive economic impact. In response, we offer you *Trade Works.*

As our society struggles to make sense of our rapidly changing global environment, we believe the key to understanding trade and globalization is through education. *Trade Works* is a valuable resource that makes sense of seemingly unconnected economic events and trends, and provides straightforward analysis of trade's widely misunderstood impact.

I strongly encourage your comments. If you like this issue, tell me. If you don't, tell me why. If you wish to be put on the *Trade Works* electronic distribution list, please email me.

Sincerely,

John L. Manzella
Editor and Publisher
John@ManzellaTrade.com
www.ManzellaTrade.com

Disturbing Trade Trends in Congress Revealed

By Daniel Griswold

When voting on trade, members of Congress reflect the general ambivalence of the American public. In opinion polls, a majority of Americans typically express unease with the dismantling of trade barriers and the resulting expansion of trade, but that same public shows no enthusiasm for retreating behind protectionist walls.

Not surprisingly, voter ambivalence on trade finds expression in Congress, where passage of every major bill to expand trade is a struggle, yet there is no momentum to raise tariff barriers in a major way.

For those who favor trade expansion, recent trends in congressional voting provide some hope for progress — but they also sound a warning that America's post-war commitment to a more open global trading system rests on a fragile foundation.

The Good News

There is no trend in Congress to abandon America's commitment to trade with the rest of the world. Nothing like the Smoot-Hawley tariff bill of 1930 can get a hearing in Congress. Even as recently as the late 1980s, the House was debating and passing such anti-trade legislation as the Gephardt amendment, which would have imposed higher tariffs against goods from countries with which the United States ran persistent bilateral trade deficits.

A resolution in June 2000 to withdraw the United States from the World Trade Organization mustered a meager 56 votes in the House. Annual resolutions to rescind normal trade relations with Mainland China were rejected decisively in the late 1990s by increasing margins, and have now been superseded by permanent normal trade relations and China's membership in the WTO. Similar efforts to repeal normal trade relations with our one-time enemy Vietnam also have gone nowhere.

Modest progress has even been made against the sanctions fever that crested in the mid-1990s. Most members of Congress finally grasp that trade sanctions are an ineffective tool of foreign policy, and that they succeed only in hurting U.S. farmers, multinational companies and workers.

Congress has even begun to dismantle the embargo the U.S. has imposed against Cuba for 40 years. Last year, Congress approved cash sales of farm goods to Cuba, and this year the House voted by wide margins to lift the travel ban and the cap on remittances to Cuba. An amendment by Rep. Charles Rangel (D-N.Y.) to eliminate funding used to enforce the embargo entirely reached a new high-water mark of 204 votes in favor. Plus, export controls on high-technology items such as super computers have been relaxed.

The Bad News

Three disturbing trends have emerged in the past few sessions of Congress that could stymie progress toward a more open global economy. None of the trends point to a dramatic, Smoot-Hawley-style repudiation of free trade, but rather a gradual erosion of support for trade liberalization or a hardening of positions against it.

Disturbing Trend No. 1

Congress has displayed an increasing willingness to abandon U.S. leadership

"Trend No. 1" continued on page 4

"Trend No. 1" continued from page 3

in world trade under pressure from domestic special interests, most notably in agriculture.

In 1996, Congress made a serious attempt to wean U.S. agriculture from its perennial dependence on federal subsidies. Passage of the "Freedom of Farm" act that year decoupled subsidies from production and repealed most controls on what farmers could plant, with the promise that U.S. trade policy would open export markets abroad.

In the aftermath of the Asian financial crisis in 1997-1998, however, world demand for U.S. farm exports plunged along with global prices. Congress reacted by passing a series of emergency farm bills, culminating in the 2002 Farm Bill, which locked in subsidies at a level 80 percent higher than the 1996 law. The ratcheting up of trade-distorting subsidies won the approval of bipartisan, 2-1 majorities in both the House and the Senate.

The new farm bill has been universally decried by our trading partners abroad, both rich and poor countries alike, who rightly charged that the United States hypocritically preaches free trade and free markets in trade negotiations but practices subsidies and protectionism at home. Not surprisingly, America's ability to lead in the upcoming WTO negotiations on agriculture has been visibly compromised.

Agricultural trade is especially important to less-developed countries, where large shares of their populations still eek out a living on the farm. U.S. companies cannot expect poor countries to agree to reduce barriers to manufacturing and service exports in the new WTO round if the United States and other advanced countries maintain their higher barriers and subsidies to agricultural trade.

Yet the U.S. Congress cannot say no to the small but politically powerful farm lobby.

Disturbing Trend No. 2

Support in Congress for America's "unfair trade" laws has solidified. America's administrative trade laws, in particular its antidumping code, their anticompetitive behavior in rhetoric about "fair trade."

In a series of decisions, WTO dispute settlement panels have found that the U.S. government has applied our antidumping law in ways that violate WTO rules designed to limit abuses. The ongoing abuse of U.S. antidumping

U.S. companies cannot expect poor countries to agree to reduce barriers to manufacturing and service exports in the new WTO round if the United States and other advanced countries maintain their higher barriers and subsidies to agricultural trade.

are themselves unfair. They target foreign producers for engaging in practices, such as price discrimination and selling at below average cost, that are routine, legal and perfectly rational among domestic producers.

Our antidumping law has become the last refuge for naked protectionism. It allows certain domestic producers to cripple their foreign competitors with antidumping duties while cloaking

law, especially by the steel industry, has driven up costs for consumers and producers alike while encouraging the proliferation and abuse of antidumping laws abroad at the expense of U.S. exporters.

Instead of reforming and restricting U.S. antidumping law, Congress has affirmed the status quo. In November

"Trend No. 2" continued on page 5

"Trend No. 2" continued from page 4

2001, on the eve of the WTO ministerial meeting in Doha, Qatar, the House passed a resolution by a vote of 410-4 demanding that any new WTO agreement "preserve the ability of the United States to enforce rigorously its trade laws, including the antidumping and countervailing duty laws, and avoid agreements which lessen the effectiveness of domestic and international disciplines on unfair trade."

In May 2002, the Senate approved by a 61-38 margin the Dayton-Craig amendment to the Trade Promotion Authority bill (TPA). The amendment, which was later dropped in conference committee, would have required a separate vote on any trade agreement provision "that modifies or amends, or requires a modification of, or an amendment to," any U.S. antidumping or other "unfair trade" law.

Like the farm bill, the refusal of Congress to consider reforming our unfair and self-damaging trade remedy laws could be a major obstacle to opening markets abroad through any new WTO agreement.

Disturbing Trend No. 3

House Democrats have abandoned the party's traditional commitment to trade expansion.

Through most of America's history up until the 1960s, the Democratic Party championed the cause of expanded trade, while Republicans traditionally carried water for big businesses seeking protection at the expense of consumers and workers. Prominent Democrats such as Woodrow Wilson, Franklin Roosevelt and John F. Kennedy understood that trade not only benefited the U.S. economy but also served as a tool of foreign policy to spread American values and cement our post-war alliances.

In what may be the most disturbing trade trend of all, support for trade expansion among Democrats in the House has shriveled to a small knot of New Democrats.

As recently as a decade ago, Democrats were far more willing to vote for major trade bills than they are today. In 1993, 102 House Democrats, or 40 percent of the caucus, voted in favor of the North American Free Trade Agreement, and in 1994, 167, or more than 60 percent, voted in favor of the Uruguay Round Agreements Act. But by 1997, fewer than a quarter of the members of the caucus were willing to give President Clinton "Fast Track" Trade Promotion Authority, and when the House finally approved TPA last December, a mere 21 Democrats voted in favor.

If the three disturbing trends are not reversed or at least halted, America's post-war commitment to a more open global economy will be at risk.

TPA managed to pass by one vote only because of overwhelming support from Republicans. The bipartisan approach to trade that marked most of the post-war era has all but disappeared—a truly disturbing trend.

It would be unfair to say House Democrats are reflexively against all pro-trade legislation. A majority consistently voted against repealing normal trade relations with China (although only 35 percent supported making NTR permanent). More than 60 percent voted for the African Growth and Opportunity Act in 2000 (AGOA), which lowered tariffs on imports from certain Caribbean Basin and sub-Saharan African countries. And a solid majority of House Democrats favor lifting the Cuban trade embargo.

But affirming normal trade relations with China involved no reduction in U.S. trade barriers, the AGOA liberalization was modest and riddled with exceptions, and the Cuban embargo votes were at least as much about foreign policy and domestic politics as trade liberalization. Those scattered votes do not change the fact that a large and growing majority of House Democrats remain skeptical of the benefits of trade expansion.

With strong presidential leadership, the right arguments and the active support of U.S. multinational companies, progress can be made in advancing the cause of free trade. Despite the disturbing trends of recent years, Congress has managed to grudgingly open our markets a bit more to some goods important to the world's poorest countries, to clear the way for China's historic entry into the WTO, and to grant the president the authority he needs to negotiate new bilateral, regional and WTO trade agreements.

If the three disturbing trends are not reversed or at least halted, America's post-war commitment to a more open global economy will be at risk.

Daniel T. Griswold is associate director of the Center for Trade Policy Studies at the Cato Institute in Washington, D.C. He is author of "Free Trade, Free Markets," the center's biannual analysis of congressional voting on trade issues available at www.freetrade.org. Readers may contact him at dgriswold@cato.org. ■

The Latin American Perspective on the FTAA

Will It Derail the Deal?

By Professor James E. McConnell

Now that President Bush and U.S. Trade Representative Robert Zoellick have been given Trade Promotion Authority by Congress, how successful will they be in extending the North American Free Trade Area (NAFTA) southward? The answer may involve how well U.S. negotiators understand Latin America's perspective.

Latin America's Alternative Choices

With many Latin American countries facing financial crises, uncertain political futures and new North American trade barriers, many of them are questioning if it is prudent to formally ally themselves with NAFTA countries. Plus, with the U.S. government preoccupied with homeland security and fading business and consumer confidence, Latin Americans also are wondering how much attention the U.S. will give to creating a Free Trade Area of the Americas (FTAA).

From their perspective, they have several alternatives, including forging closer ties with the European Union (EU), or perhaps creating their own South American Free Trade Area.

Much Progress Has Been Made

Over the past decade, NAFTA countries and 34 other democratically elected governments in the Western Hemisphere have entered into formal discussions designed to create a single trade zone by 2005. Trade summits have been held in Miami (1994), Santiago (1998), Quebec City (2001), and Quito, Ecuador (November, 2002).

The breadth of these negotiations is unprecedented, even by the standards of the Uruguay Round. For example, nine negotiating groups are addressing issues related to agriculture, services and investments, subsidies, antidumping and countervailing duties, and very importantly, how smaller countries within the hemisphere will be able to benefit equally with the larger ones once trade liberalization has occurred. (See http://www.ftaa-alca.org).

Throughout the 1990s, NAFTA country leaders provided strong support for these negotiations. And until very recently, dramatic reforms in Latin America began to transform the region from autocratic rule and financial mismanagement into one of nascent democracy and economic promise. Furthermore, the success that the U.S. and Canada have achieved in integrating the less economically powerful Mexico into NAFTA has sent positive signals throughout the hemisphere that a workable and beneficial FTAA can be realized.

Unfortunately, the situation has changed. Since the millennium began, political and economic conditions within the Western Hemisphere have deteriorated, and short-term prospects for an expanded NAFTA appear less optimistic.

Perceptions and Realities Differ

One of the basic tenets of regional economic integration theory says: the greater the trade relationship among prospective member countries, and the higher their average tariffs levels, the greater likelihood that further specialization and trade creation will occur after an economic union takes place.

Based on this, an initial examination of the patterns of commodity trade among the Western Hemisphere countries suggests they are promising candidates for region-wide economic

integration. For example, approximately 58 percent of Western Hemisphere exports in 2000 were shipped within the Americas.

However, upon closer examination, it is revealed that the three NAFTA partners are the major recipients and originators of this trade. Moreover, intra-regional trade among the non-NAFTA members accounts for only 29 percent of total exports and 23 percent of imports. Equally revealing, only 7 percent of NAFTA country exports are destined for Latin America.

Surprising to many, Latin America's interest in entering into a trade agreement with NAFTA countries is not as compelling as it might, at first, seem. Current trade patterns reveal that NAFTA countries form a largely self-contained block while the other hemispheric nations have varying degrees of trade dependency upon NAFTA. In fact, non-NAFTA Latin nations are more dependent on the EU and themselves for both their exports and imports than on NAFTA countries.

Closer Ties With Europe

Given these trade realities, Latin America may choose to develop even stronger ties with the EU. Chile and Mercosur (the Southern Cone alliance

"Perspective" continued on page 7

"Perspective" continued from page 6

of Argentina, Brazil, Paraguay, and Uruguay), already have strong links with the European block, which has recently broadened the scope of its free trade talks to include the sticky issue of trade in agricultural products — an issue of paramount importance to most Latin American countries.

From the EU's perspective, cultural and linguistic ties, and even some shared values already exist with Argentina, Brazil and several more Central American and Caribbean nations. Plus, the EU likely would benefit from the new Doha Round of WTO trade talks with the United States if the Latin American nations are not formally tied to NAFTA.

The most important advantage of NAFTA membership would be the "rules of origin" provision. This would make direct investments in Latin America very attractive.

A South American Free Trade Area

The dream of a South American Free Trade Area (SAFTA) is an alternative for southern non-NAFTA nations — especially Brazil. Intra-hemispheric commodity trade patterns suggest that the effect of an FTAA on many of the non-NAFTA nations' manufacturing sectors, including Brazil's, would not come from creating more formal ties to NAFTA, but from the liberalization of trade among themselves.

Most Latin American non-NAFTA nations continue to be quite protectionist. If these impediments to trade can be reduced under the auspices of a SAFTA, Brazil's dream of leading a common Latin American front to extract better terms from the U.S. and the EU might be realized.

Brazil's Protests

Brazil's ambassador to the U.S. claims that America levies an average tariff of 46 percent on Brazil's top 15 world exports, whereas Brazil's average tariff on their American equivalents is just 14 percent. To protest this discrepancy, Brazil has opened cases at the WTO against American barriers to its orange juice, U.S. subsidies to soya and cotton growers, and most recently U.S. tariffs on Brazilian steel.

Such confrontations do not bode well for hemispheric integration, especially since Brazil and the United States will co-chair the final round of FTAA negotiations!

Role of Foreign Direct Investment

In these times of Latin American economic and political uncertainty, it is important for the U.S. to give careful attention to major weaknesses that plague many Latin American nations, namely their dependence upon foreign capital and their vulnerability to outside events.

For many of these nations, the most important advantage of NAFTA membership would not be tariff reductions, important as they would be, but rather, the "rules of origin" provision that would grant preferential access to the U.S. market. This would make direct investments in Latin America by multinationals from the rest of the world very attractive.

The U.S. Challenge Ahead

Given the Latin American alternatives of developing more formal ties with the EU or creating a broader alliance among themselves, the major U.S. challenge is to give very high priority to completing the FTAA on schedule, while seriously addressing Latin American concerns.

This will not be an easy task as other pressing issues, such as national security and the newly launched Doha Round of trade negotiations, likely will be distractions. Nevertheless, it is important for American leaders to realize that most Latin American nations are looking for signals regarding the predisposition of the U.S. toward the Western Hemisphere.

Signals from the United States

During the campaign trail in 2000, former Governor Bush said that Latin America often remains an afterthought of American foreign policy. Since then, the Bush Administration has made a visible and significant commitment to an FTAA and has begun to address the specific needs of Latin American countries.

Recent signs are encouraging. Congress recently passed the Trade Act of 2002, which expands trade benefits for developing countries by more than $1.2 billion. In September, the U.S. renewed and expanded the Andean trade preference program with Colombia, Bolivia and Peru, and in October, the USTR notified Congress that negotiations are underway to create free trade agreements with Chile and five Central American nations.

At a time when the region is vulnerable to internal and external disruptions, these are the kinds of actions that are likely to convince Latin American countries that the U.S. government is sensitive to their needs, and that strengthening their ties to NAFTA is in their best long-term interest.

James E. McConnell is associate director of the Canada-U.S. Trade Center at the University at Buffalo. Readers may contact him at geojem@acsu.buffalo.edu. ■

Trade Promotion Authority Becomes Law

Now the United States Must Play Catch-Up

Whoever said "If it ain't broke, don't fix it," probably lived in a simpler time. In today's rapidly changing global environment, the United States needs to be proactive and anticipate problems.

The U.S. Has Fallen Behind

Currently, the U.S. is behind the curve. We are a party to only three out of 150 free trade agreements in force around the world. Many of these agreements have evolved into trade blocs, such as the Association of Southeast Asian Nations (ASEAN) and the European Union (EU). And several blocs plan to expand.

For example, EU accession negotiations are underway to admit 13 Eastern European countries — a move that will make the EU's consumer base twice as large as the United States'.

Mercosur, the South American bloc, is negotiating with the EU to establish a trans-Atlantic free trade zone. And recently, ASEAN and China agreed to consider establishing a trade bloc that would represent a market of 1.7 billion consumers.

It's Time To Play Catch-Up

As our competitors establish larger trade blocs that eliminate import barriers among member countries, U.S. exports — which still incur duties — are placed at a competitive disadvantage. To remedy this, the U.S. needs to forge new trade agreements that level the playing field.

Unfortunately, from 1994 through September 2002, our ability to establish new trade agreements was compromised. This recently changed. Trade Promotion Authority (TPA), previously known as Fast Track, expired in 1994. But after several attempts, it was renewed in August 2002, thanks to those who advocated the importance of trade to their companies, jobs and communities. But nevertheless, the United States has fallen behind our global competitors and needs to play catch-up.

What Is Trade Promotion Authority?

TPA requires Congress to pass or reject trade agreements "as is." Without TPA, foreign governments have been reluctant to negotiate treaties that Congress could later change.

On December 6, 2001, the Trade Promotion Authority bill (HR 3005) passed in the House of Representatives by one vote (215 to 214). But because the Senate added amendments that effectively changed the bill, and passed it on May 23, 2002 (66 to 30), the legislation went to Conference where one version was hammered out.

The final version was passed in the House on July 27, 2002 (215 to 212) and in the Senate on August 1, 2002 (64 to 34). President Bush signed the legislation into law on August 6, 2002.

International Trade Supports Jobs

TPA is key because exports support more than 12 million higher-paying U.S. jobs, strengthen companies and farms, and improve our tax base, while sending export revenue to local communities through restaurants, retail stores, etc.

In 1950, trade accounted for less than 5.5% of U.S. economic growth. Today, it has become an integral part of everyday life, accounting for almost one-third of our economic growth. In fact, one in three acres of U.S. agricultural production is now exported.

The "Luddites" Are Back in Force

Some blame trade for job losses and industry restructuring. In reality, less than 2% of non-farm workers are at risk from imports. Technology, not imports, is the real displacer of jobs. Would we stop technological advancement because a small number of jobs will become obsolete?

In the early 19th century, the English Luddites attempted to destroy textile machines because they replaced weavers. Today, modern-day "Luddites" want to essentially do the same — but have mistaken the impact of technology for trade.

Entering the 19th Century... Again

Entering the 21st Century is in many ways similar to entering the 19th Century. The shift from an agrarian to an industrial economy compelled workers to leave farms in search of factory jobs. Industrialization created fear and demanded that workers learn new skills.

Today, with the advent of globalization, the U.S. is increasingly specializing in more complex, value-added goods and services. Consequently, new skills again are demanded. But for those who can't adapt, the expansion of trade adjustment assistance that's incorporated in TPA legislation is welcomed.

Congress Needs To Forge New FTAs

New trade agreements that knock down barriers will help U.S. companies export and create jobs. And companies that don't export will also benefit because portions of their components sold locally likely are incorporated into exported products. That's why Congress must negotiate new trade agreements that will get the United States off the sidelines. ■

Globalization Provides the Means To Build a Better Life

Proving the Skeptics Wrong

The Chinese proverb: "Give a man a fish and you feed him for a day, teach a man to fish and you feed him for a lifetime," has never been more relevant than today.

Globalization, the integration of national markets through international trade and investment, offers infinite possibilities, greater freedom, and new hope for the world's poor.

Developing Countries Prosper

Since globalization emerged in the 1970s, world infant mortality rates have fallen by almost half, adult literacy has increased more than a third, primary school enrollment has risen, and the average life span has shot up 11 years. In the short span of 1990 through 1998, the number of people living in extreme poverty in East Asia and the Pacific decreased 41% — one of the largest and most rapid reductions in history.

Due to successful efforts to lower global barriers, international trade and investment have become a primary engine of world growth. And growth is responsible for reducing poverty. In fact, studies indicate that developing countries with open economies grew by approximately 5% a year in the 1970s and 1980s, while those with closed economies grew less than 1% annually.

Today, 24 developing countries representing about 3 billion people, including China, India and Mexico, have adopted policies enabling their citizens to take advantage of globalization. The result: their economies are catching up with rich ones. The incomes of the least globalized countries, including Iran, Pakistan and North Korea, have dropped or remained static.

If remaining world merchandise trade barriers are eliminated, potential gains are estimated at $250 - $550 billion annually. About two-thirds of this would accrue to developing countries — more than twice their annual level of aid.

Positioning for Greater Growth

Helping the world's poorest countries to become globally integrated will position them for greater growth in the 21st Century. And who would know this better than former Mexican president Ernesto Zedillo, who said, "In every case where a poor nation has significantly overcome its poverty, this has been achieved while engaging in production for export markets and opening itself to the influx of foreign goods, investment and technology — that is, by participating in globalization."

The Effect on the United States

Powered by advances in telecommunications, transportation and finance, globalization empowers consumers to purchase the best the world has to offer and gives producers the tools to find buyers anywhere. Consequently, in the United States, resources have shifted to sectors with competitive advantages, productivity has reached new highs, and innovation has flourished. Self-directed teams now apply sophisticated skills to create and run new processes. This has transformed U.S. manufacturing and boosted demand for more highly-skilled workers.

There Is a Downside

But globalization has had negative consequences on some developing countries that don't have sound legal or financial systems. As a result, anti-globalists with good intentions but bad policy recommendations often brand globalization as the scapegoat for many of the world's ills.

The challenges introduced by globalization are similar to those introduced by the Industrial Revolution. Today, as the internet eliminates distance, we relive what the railroads and electricity brought to an earlier age. But, with change comes controversy. And just as the Industrial Revolution's detractors spawned Marxism, it is essential to correct globalization's defects before counter-forces destroy its promise.

Learning a New Way

To succeed in this highly technical environment, seize the benefits of globalization and reduce the risks, American workers must continually learn new skills, developing countries must welcome global integration, and all nations must provide safety nets. By teaching people and their nations to fish in the waters of globalization, billions will achieve the means to obtain a higher quality of life. ■

U.S. Investment in Developing Countries Spurs a Race to the Top — Not the Bottom

Anti-globalists protesting American commercial investment in developing nations have a notably heavy investment of their own in misinformation.

They would have you believe, for instance, that U.S. foreign direct investment (FDI) in developing countries is harmful to host country workers and the local environment. But a careful look at the record reveals that nothing could be further from the truth.

Higher Wages and Better Conditions

American manufacturers who invest in developing countries typically offer higher wages and better working conditions. This makes jobs at U.S. facilities highly prized, and, over time, leads to improved environmental and worker protection at all levels.

A case in point, is Procter & Gamble, which since 1991, has invested $85 million in a Czech Republic consumer products company that produces detergent and liquid cleaners. By applying P & G's worldwide environmental standards, the facility was able to reduce boiler emissions by 99 percent and solid waste by nearly 6,000 metric tons.

In addition to environmental improvements, P & G introduced a competitive compensation program and unique employee benefits, such as loans to renovate apartments and houses, supplementary income payments during illness, maternity leave, and language studies.

P & G also donates $120,000 annually to the development of local education, health care, environmental protection, and social institutions. So impressed with these practices, Czech Republic President Vaclav Havel recently said P& G "could serve as a model for other investors."

Other American corporations investing in facilities abroad typically promote similar ethical and responsible behaviors.

Nike, the Oregon athletic attire and shoemaker, pays about double the prevailing wage at its contract factories throughout Southeast Asia and scrupulously meets all local environmental and occupational safety and health laws.

To better serve the Chinese market, Eastman Kodak Co. built a state-of-art film and photo paper production plant that exceeds Chinese environmental standards. The U.S. firm pays its Chinese workers more than twice the state-owned company average wage and works with Chinese banks to help make loans available to local entrepreneurs interested in opening their own photo-processing shops.

Agents of Change

Through their operating standards, business practices, values, and principles, U.S. companies serve as agents of change, charting a path for other foreign and domestic companies to follow. And this strategy, which is good for business, results in greater employee loyalty, less absenteeism, higher morale, and increased productivity.

Anti-Globalist Logic Is Flawed

Although exceptions exist, anti-globalists promulgate the notion that, as a whole, U.S. manufacturers investing abroad seek low-cost facilities in order to cut labor and environmental costs. Although anti-globalists' intentions are good, their logic is flawed.

Their argument is based on the notion that weak environmental and worker standards give producers in poor countries a significant cost advantage. They also theorize that this puts pressure on other countries to lower their standards in order to compete, prompting a "race to the bottom."

If this were correct, investment would be flowing to underdeveloped countries with the poorest labor and environmental records. In reality, the opposite is true.

The Race to the Top

Developing countries tend to attract only a small portion of America's

"Investment" continued on page 11

"Investment" continued from page 10

foreign direct investment. For example, in 1999, 87 percent of U.S. manufacturing investment abroad was directed in high-wage countries. Political stability, education and productivity levels, communications and transportation infrastructure, the rule of law, proximity to market, and the ability to repatriate profits are the most important determinants of capital flows.

This is why developed countries, which pay the highest wages and have the strongest environmental laws, are the destinations for the vast majority of FDI — promoting a "race to the top."

Standards Go Up — Not Down

When a major trading partner raises standards, its partners typically follow. For example, when Germany raised its auto emission standards, other European countries did too. Likewise, California's aggressive environmental regulations have pulled other states up as well.

In reality, little incentive exists to establish facilities in countries with weak standards. Today, complying with environmental regulations typically accounts for less than 1 percent of production costs of industries in Western countries.

Furthermore, research indicates that countries with weak standards do not have a better global export performance than countries with higher standards.

This is not to say that environmental quality in some underdeveloped countries has not deteriorated ... it has. But studies show that after a country's per capita income reaches about $5,000, environmental degradation ceases, and then improves.

As living standards rise, an increasing percentage of the population becomes better educated and more politically aware. In turn, these people put greater pressure on government to establish and enforce stricter environmental regulations and to allocate more resources to environmental quality.

Educational levels also rise sharply. As incomes rise, families can more easily afford to send their children to school, rather than to work. In fact, research indicates that child labor declines sharply as the level of economic development increases.

Investment Creates Opportunity and Improves Quality of Life

U.S. manufacturing investment in developing countries leads to higher wages, improved labor standards, and provides millions of people with greater opportunities.

But those who do break the rules should beware. In addition to accounting concerns following the Enron scandal, institutional investors are increasingly aware of the importance of sound labor and environmental records of companies to which they provide investment. ■

Unshackle U.S. Exporters or Risk Job Losses

The Battle With Europe and the WTO Over the Extraterritorial Income Exclusion Act

What do you get when you continually change and manipulate tax codes? A big mess! Now, throw convoluted subsidies into the mix and you also end up with a lot of unintended consequences.

Thousands Could Lose Jobs

Today, that's the situation in both the United States and European Union (EU). And as a result, thousands of U.S. workers stand to lose their jobs at a time when the U.S. economic recovery appears shaky.

What's happening now is tied to actions of the past. For decades, EU industries, such as aerospace and telecommunications, have been subsidized to boost their international strength or to shield them from global competition. Additionally, the EU has exempted and continues to exempt its exporters from paying a substantial value added tax.

FSC and ETI

To counter these unfair actions, in 1984, the United States crafted the Foreign Sales Corporation (FSC) tax code so exporters could compete fairly in global markets. This proved beneficial, as evidenced by a National Foreign Trade Council report that said 3.5 million U.S. export-related jobs benefited from FSC tax incentives in 1999. Unfortunately, the EU challenged the FSC rule through the World Trade Organization, and won in 2000.

In an attempt to satisfy the global trade body, the U.S. repealed the law and in its place created the Extraterritorial Income Exclusion (ETI) Act of 2000. However, the new law still didn't satisfy the EU, who again challenged the law, and won.

Consequently, the EU is now authorized to impose sanctions of more than $4 billion annually on U.S. exports, which include steel, beef, sugar, wood and paper products, cotton, apparel, cosmetics, and electrical machinery.

Although Europe's tax loopholes and subsidies distort trade by artificially increasing the attractiveness of its goods and services on world markets, its indirect tax system is technically WTO-compliant. WTO language doesn't cover indirect taxes, only direct taxes like those used in the U.S.

Small Companies Are Impacted Most

So, what can the U.S. do? If Congress terminates ETI without establishing a suitable replacement, approximately 6,000 U.S. exporters who rely on ETI to compete will be hurt. And the majority of these firms are small.

Hutchinson Technology, Inc., headquartered in Minnesota, exports 90 percent of its computer disk drive components. If ETI is repealed, President and CEO Wayne Fortun, says "The company could be forced to move production operations to the Far East, resulting in the loss of 3,000 of our 3,400 employees."

Power Curbers, Inc., a manufacturer of concrete paving equipment, employs 130 workers at its North Carolina, Iowa and Tennessee facilities. Company President and CEO, Dwight Messinger, says "Without ETI, our exports would decrease, especially to Europe. This could result in layoffs of 5 to 10 percent of our workforce."

Small companies, many of which are struggling just to survive the economic downturn, aren't the only ones that stand to lose. Boeing alone estimates that repealing ETI will result in the loss of nearly 10,000 of its high-tech jobs, as well as 23,000 more jobs with its suppliers.

Airbus, Boeing's heavily subsidized European rival, has received more than $30 billion in EU financial support. This gives Airbus an unfair advantage, and affects the entire U.S. aerospace industry that employs nearly 800,000 highly-skilled workers.

The Mess Needs To Be Cleaned Up

There is no doubt that multiple layers of loopholes and convoluted subsidies artificially create winners and losers in international trade. That's why this mess needs to be cleaned up. The U.S. response to the ETI challenge is currently being debated in Congress. And one thing remains certain: U.S. exporters need a mechanism that counters their EU rivals' government handouts. Small and medium-size companies, which account for about 96 percent of all U.S. exporters, and large companies, as well as farmers, all need a level playing field.

Exports Are Key to Our Economy

Exports support more than 12 million higher-paying U.S. jobs, strengthen companies and farms, and improve the tax base, while sending important revenue to local communities. Plus, one in three acres of U.S. agricultural production is exported. In short, exports are a key piece of our economy.

Congress certainly has a difficult job ahead. In order to prevent the European Union from implementing $4 billion worth of trade sanctions against U.S. exports, our Congressional Representatives must act quickly. But they must do so in a way that unshackles our exporters from a system of unfair competition, does not force them out of business or offshore, and protects U.S. jobs. ■