

GUIDE TO SOTU ON EXPORTS, JOBS

Background Data for Obama State of the Union Speech, Which Is Expected to Focus on Jobs, Competitiveness, Exports, and Trade Agreements

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Whether trade creates U.S. jobs depends on net export gains and reducing the trade deficit, which our past policies have not done: The question is how to expand trade in a way that creates U.S. jobs. Under past trade policies and pacts, the U.S. has served as the target market for imports from around the world. This has resulted in a huge trade deficit – \$810 billion before the economic crisis-related collapse in trade and now again rising. U.S. exports have grown 18 percent in the past year as the global economy recovered, but the estimated \$1,266 billion in U.S. exports in 2010 still does not equal the pre-crash levels of \$1,316 billion in 2008. While exports have grown by an estimated \$209 billion since 2009, imports have grown by \$347 billion. Since the North American Free Trade Agreement (NAFTA) and the World Trade Organization (WTO), the U.S. has lost net 5.1 million manufacturing jobs with 43,000 factories closed. Doing more of the same – more NAFTA-style deals or continuing the unbalanced mode of China trade – is not going to reverse the past trade outcomes of job loss and deficits. As Paul Krugman wrote in a recent column "Trade Does Not Equal Jobs: "If you want a trade policy that helps employment, it has to be a policy that induces other countries to run bigger deficits or smaller surpluses. A countervailing duty on Chinese exports would be job-creating; a deal with South Korea, not."

<u>Countries with which we do not have FTAs</u>: President Barack Obama is expected to urge passage of more FTAs as a means to boost exports and create U.S. jobs. However, Public Citizen examined the relative U.S. export growth with the 17 countries with which we have FTAs to date and found, counterintuitively, that the FTAs are associated with an export growth penalty. U.S. exports to FTA partners grew only half as fast as exports to countries with which the United States does not have FTAs (0.8 percent vs. 2.2 percent on an annual average). If the difference between the FTA and non-FTA export growth rates for goods for each year were to be put in dollar terms, the total U.S. FTA export "penalty" would be \$72 billion over the past decade for the existing FTAs.

The U.S. International Trade Commission's official study of the Korea FTA that Obama will emphasize concluded that the deal would increase the U.S. trade deficit: The USITC, the independent federal body that analyzes likely effects of trade pacts for Congress and the executive branch, found that the Korea FTA would result in an increase in the total U.S. goods trade deficit of between \$308 million and \$416 million. Imports are projected to increase by \$5,100 million to \$5,692 million, and exports will increase by \$4,792 million to \$5,276 million. The bottomline USITC finding of an increased U.S. trade deficit contradicts Obama's stated purpose for passing the FTA – to promote his goal of doubling exports to create two million jobs. The ITC's projections can be thought of as the minimum level of trade deficit increase and employment displacement that the Korea FTA might bring about, given that past USITC projections have been overly optimistic. For example, a 1999 USITC study using roughly the same model estimated that China's WTO accession tariff offer would increase the U.S. trade deficit with China by only \$1 billion. In reality, the trade deficit with China skyrocketed by \$167 billion between 2001 and 2008.

Korea FTA's chief U.S. negotiator admitted it would not be a boon for U.S. exports: Ambassador Karan Bhatia noted in a speech to a Korean audience that it was a "myth" that "the U.S. will get the bulk of the benefits of the FTA." He said: "If history is any judge, it may well not turn out to be true that the U.S. will get the bulk of the benefits, if measured by increased exports." He added that, in the instance of Mexico and other countries, "the history of our FTAs is that bilateral trade surpluses of our trading partners go up," meaning that the U.S. trade deficit with those countries increased.

Beware of administration claim that the Korea FTA will "support" 70,000 jobs: President Obama's use of the term "support" is critical, as noted in a *New York Times* story, "Few New Jobs Expected Soon from Free-Trade Agreement with South Korea." The core question is what *net effect* the Korea FTA will have on U.S. employment. However, the figure Obama cites reflects only the ITC's projected gains of between \$10 billion and \$11 billion in U.S. exports to Korea. An exports-to-jobs ratio was then applied to that figure – without including the estimated increase in imports or the ITC's core conclusion that the FTA would increase the overall U.S. trade deficit. The same methodology using the net data yields a net loss of U.S. jobs, since the trade deficit will increase by between \$308 million and \$416 million.

EPI projects American job losses from the Korea FTA at 159,000: A study by the Economic Policy Institute examined the U.S. historical experience with major changes in bilateral trade policy – namely changes in trade flows with Mexico and China after NAFTA implementation and Chinese World Trade Organization (WTO) accession, respectively – to determine the likely impact of the Korea FTA on trade flows and U.S. jobs. EPI found that implementation of the Korea FTA would boost the U.S. trade deficit with Korea by \$13.9 billion over the next seven years. This rise in the trade deficit, in turn, would cost the U.S. economy about 159,000 net jobs. This is equivalent to losing 90 percent of the manufacturing jobs in Detroit.

The December 2010 Obama supplemental Korea trade deal does not alter the increased trade deficit, job loss findings. The supplemental talks and agreement extended the time period for but did not eliminate the tariff phase-out for certain autos and trucks. The USITC model looks at the change in trade flows when the agreement is fully implemented and tariffs are fully phased out. Given that the supplemental agreement did not alter ultimate tariff elimination, but only altered timelines for cuts, it does not alter the USITC findings of an increased U.S. trade deficit.

The USITC study identified nine losing U.S. economic sectors that include many high-wage industries, including auto and electronics manufacturing: The USITC estimates of the trade balance impact of the Korea FTA identified sectors of the U.S. economy where it projects the FTA will cause deficits: motor vehicles, electronic equipment, "other transportation equipment," iron, metal products, textiles and apparel.

Table 1: USITC Estimates of Trade Balance Effects of Korea FTA, Selected Industries		
,	Change in U.S. global trade	
	balance (millions of dollars) ¹⁵	
	Low	High
Motor vehicles and parts	(\$531)	(\$708)
Other transportation equipment	(\$340)	(\$293)
Electronic equipment	(\$790)	(\$762)
Metal products	(\$169)	(\$187)
Textiles	(\$169)	(\$190)
Apparel	(\$56)	(\$74)
Iron-containing metals	(\$65)	(\$75)
Total	(\$2,120)	(\$2,289)

The average hourly earnings of workers in the electronic equipment manufacturing industry, projected to lose a significant number of jobs, were \$30.38 in 2008. This was 40.5 percent greater than the average hourly earnings of all workers employed in the private sector. Table 1 shows what is driving these declines in employment in these industries: large rises in the trade deficit in these sectors, totaling up to \$2.3 billion for motor vehicles and parts, other transportation equipment, electronic equipment, metal products, textiles, apparel and iron-containing metals. The USITC also predicted that, were the Korea FTA implemented, there would be an absolute decline in the total value of exports in some manufacturing sectors, including electronic equipment, other transportation equipment and iron-containing metals – not just a worsening of the balance. For example, total U.S. exports of electronic equipment are

expected to decline by \$293 million to \$381 million. This is a particularly troubling development, since high-tech jobs are often touted as being the "jobs of the future."

Beware of the administration claim that the Korea FTA could reduce the U.S. trade deficit:

Given that the fundamental question is what the Korea FTA would mean for America's trade balance and thus jobs, it is worth understanding the seemingly conflicting data in the USITC report. At first glance the USITC study seems to suggest that the U.S. trade balance in goods (also known as merchandise) will improve by between \$3.3 billion and \$4 billion because this is the projected change in the *bilateral* trade balance with Korea. However, due to the way that bilateral trade pacts affect global trade flows, the Korea FTA's results for overall U.S. trade balance in goods are dramatically different from the change in the bilateral balance with Korea. Chapter 2 of the USITC report explains: "The last row in table 2.3 reports the simulated changes in total U.S. trade in sectors analyzed in this simulation. Total U.S. exports of these commodities is expected to be higher by between \$4.8 billion and \$5.3 billion, and total imports of commodities in this analysis is expected to be higher by between \$5.1 billion and \$5.7 billion." Subtracting the import figures from the exports figures reveals that the USITC study predicts the total U.S. trade deficit in goods will increase by between \$0.3 billion and \$0.5 billion under the FTA. This finding is thus that the effect of *trade diversion* on U.S. exports is greater than the effect on U.S. imports, so the U.S. trade balance with the world (including Korea) will worsen after the FTA goes into effect, but the balance with Korea alone improves.

The auto manufacturing industry may lose a significant number of workers due to the Korea FTA: The Korea Automobile Manufacturing Association (KAMA) celebrated the December 2010

supplemental deal: "The deal wiped off uncertainties in the world's largest automobile market and is forecast to drive up South Korean automakers' market share in the U.S. ... Small and mid-size auto parts makers will also benefit from the elimination of tariffs." The USITC study projected that once tariffs are phased out, the sizable bilateral trade deficit with Korea in autos and auto parts (Korean sent 500,000 autos here in 2010 while the U.S. exported less than 6,000 to Korea¹⁹) would increase by up to \$1.3 billion. Koreans have not been purchasers of foreign cars. Given both strong "Buy Korean" social preferences and various non-tariff barriers, total import penetration is four percent. To try to expand U.S. exports to Korea, the supplemental negotiations concluded in December 2010 included a four-year waiver of Korean auto fuel efficiency and emission standards for U.S. imports as well as a waiver of Korean auto safety standards for up to 25,000 U.S. autos per U.S. Big Three maker – if there were demand for such cars. (That is to say that there is no guaranteed access for 75,000 additional U.S. cars.) Other Korean policies identified by the industry and United Auto Workers as posing significant non-tariff barriers to entry were not waived. Further, the low 35 percent domestic content rule for vehicles to obtain duty-free treatment was not altered, meaning Korean assembled vehicles containing 65 percent Chinese and other inputs would gain duty-free entry into the U.S. market. (Korea's FTA with the European Union requires 55 percent domestic content to obtain favorable tariff treatment and

NAFTA requires 50 percent.) The elimination of U.S. auto and truck tariffs and the low rule of origin

2008, 9.2 percent greater than the average hourly earnings of all workers employed in the private sector

requirements raise the question of whether Korean auto firms now producing cars in the United States would continue their operations. The average hourly earnings of American workers in the auto industry was \$23.61 in

Lack of currency manipulation disciplines in the Korea FTA mean agriculture could also lose out:

(\$21.62). According to the U.S. Bureau of Labor Statistics (BLS), total hourly compensation per worker, which includes both wages and benefits, was \$36.35 for American workers in the auto sector and \$23.30 for Korean workers in the auto sector in 2007, so compensation for American auto workers is about 56 percent higher. 22

Proponents of the Korea FTA are advocating its congressional passage by highlighting prospective gains for the U.S. agricultural sector related to tariff cuts. However, especially given Korea's past history of significant currency manipulation, it is worth noting that if Korea again devalued its currency, it could effectively cancel the benefits of the tariff cuts. Unfortunately, despite calls from various U.S. economic sectors to include safeguards against such devaluations, ²³ the Korea FTA does not provide for penalties or adjustments if one party deliberately undervalues its currency. In other words, the new market access in Korea being promised by various government officials and agribusiness trade associations aimed at persuading farm state legislators to support the FTA could

well turn out to be completely hollow. Korea is one of only three countries (China and Taiwan being the others) that have ever been placed on the Treasury Department's list of currency manipulators. ²⁴ During the mid- to late-1980s, the Korean won was undervalued against the dollar by about 60 percent, meaning that all U.S. goods exported to Korea faced a barrier equivalent to a tariff of about 60 percent. ²⁵ In the early 1990s the value of the Korean won shifted so it was no longer undervalued, but in the late 1990s Korea rapidly acquired foreign exchange reserves and the won again became severely undervalued against the dollar by about 50 percent. ²⁶ If Korea again reverts to strategically undervaluing its currency to boost exports and reduce imports following implementation of the FTA tariffs cuts, for instance again by devaluing by 50 percent, then the FTA tariff cuts combined with the 50 percent devaluation of the Korean won would result in a net effective increase in Korean agricultural tariff equivalents of: 12 percent for beef; 25.2 percent for non-beef meat products; 46.7 percent for other animal products; 18.2 percent for vegetables, fruit and nuts; 10.4 percent for dairy products; and 40 percent for miscellaneous food products.

Such currency devaluation following FTA implementation has happened in the past. A year after NAFTA went into effect, Mexico suddenly devalued its currency by 50 percent. The devaluation of the peso negated NAFTA's tariff cuts, as noted by a former World Bank Chief Economist who wrote, "Nonetheless, it must be recognised that the real depreciation of the peso [in 1994], given its magnitude, was a larger influence on trade than was the entry into NAFTA. This is because the total reduction in tariffs at the end of 15 years would average only 10 per cent, in contrast with the 50 per cent real depreciation." Due to the peso devaluation, American products became much more expensive for Mexican consumers, and U.S. agricultural exports suffered. For example, U.S. exports of beef and pork to Mexico in the first three years of NAFTA were 13 and 20 percent lower, respectively, than beef and pork exports in the three years before NAFTA was enacted. Members of Congress should consider the NAFTA experience before making optimistic claims about supposed benefits to the beef and pork industries under the Korea FTA.

ENDNOTES

¹ U.S. Bureau of Labor Statistics, "Table B-1. Employees on nonfarm payrolls by major industry sector, historical," Accessed January 24, 2011, Available at: ftp://ftp.bls.gov/pub/suppl/empsit.ceseeb1.txt

and U.S. Bureau of Labor Statistics, "Quarterly Census of Employment and Wages," Series ID ENUUS0000051013, Available at ftp://ftp.bls.gov/pub/special.reguests/cew

² Paul Krugman, "Trade Does Not Equal Jobs," The New York Times, Dec. 6, 2010

³ Travis McArthur and Todd Tucker, "Lies, Damn Lies and Export Statistics: How Corporate Lobbyists Distort the Record of Flawed Trade Deals," Public Citizen, September 2010, Table 5, at 26. Available at: http://bit.ly/bx3JJn

⁴ U.S. International Trade Commission. "U.S.-Korea Free Trade Agreement: Potential Economy-wide and Selected Sectoral Effects." USITC

⁴ U.S. International Trade Commission. "U.S.-Korea Free Trade Agreement: Potential Economy-wide and Selected Sectoral Effects." USITC Publication 3949. September 2007, Corrected printing March 2010, at 2-14, Table 2.3, Available at: http://www.usitc.gov/publications/332/pub3949.pdf

⁵ U.S. International Trade Commission, "Assessment of the Economic Effects on the United States of China's Accession to the WTO," August 1999, at xi.

⁶ Trade flow data from the USITC DataWeb. Deficit calculated on a domestic imports minus imports for consumption basis. Figures inflation-adjusted to 2009 using the CPI-U-RS.

⁷ Remarks by Ambassador Karan Bhatia (Deputy U.S. Trade Representative) at Yonsei University, October 24,

^{2006,} Available at: http://ustraderep.gov/assets/Document Library/Transcripts/2006/October/asset upload file496 9901.pdf

⁸ Sewell Chan, "Few New Jobs Expected Soon From Free-Trade Agreement With South Korea", New York Times, December 7, 2010.

⁹ U.S. International Trade Commission. "U.S.-Korea Free Trade Agreement: Potential Economy-wide and Selected Sectoral Effects." USITC Publication 3949. September 2007, Corrected printing March 2010, at Table 2.2 on page 2-8.

¹⁰ A recent International Trade Administration report estimated that every \$150,000 in U.S. exports supports one American job. John Tschetter, "Exports Support American Jobs," International Trade Administration, International Trade Research Report No. 1, April 2010, at Table 1, Available at: http://trade.gov/publications/pdfs/exports-support-american-jobs.pdf

¹¹ Robert E. Scott, "Trade Policy and Job Loss," Economic Policy Institute, Working Paper #289, Feb. 25, 2010, Available at: http://www.epi.org/publications/entry/trade_policy_and_job_loss/

¹² Robert E. Scott, "Trade Policy and Job Loss," Economic Policy Institute, Working Paper #289, Feb. 25, 2010, Available at: http://www.epi.org/publications/entry/trade_policy_and_job_loss/, at 9, Table 4.

¹³ Robert E. Scott, "Trade Policy and Job Loss," Economic Policy Institute, Working Paper #289, Feb. 25, 2010, Available at: http://www.epi.org/publications/entry/trade_policy_and_job_loss/, at 10, Table 5.

¹⁴ See page 10 of http://www.bls.gov/sae/eetables/sae_annavg109.pdf

¹⁵ U.S. International Trade Commission. "U.S.-Korea Free Trade Agreement: Potential Economy-wide and Selected Sectoral Effects." USITC Publication 3949. September 2007, Corrected printing March 2010, at 2-14, Table 2.3.

¹⁶ U.S. International Trade Commission. "U.S.-Korea Free Trade Agreement: Potential Economy-wide and Selected Sectoral Effects." USITC Publication 3949. September 2007, Corrected printing March 2010, at 2-14, Table 2.3.

¹⁷ U.S. International Trade Commission. "U.S.-Korea Free Trade Agreement: Potential Economy-wide and Selected Sectoral Effects." USITC Publication 3949. September 2007, Corrected printing March 2010, at 2-13.

²² ftp://ftp.bls.gov/pub/special.requests/ForeignLabor/aeind336naics.txt

²³ See, for instance, National Farmers Union resolution on Trade Reform. Available at: http://nfu.org/wp-content/trade-reform.pdf

- ²⁴ The two other countries are China and Taiwan. Robert Scott, "Currency Manipulation—History Shows That Sanctions Are Needed," Economic Policy Institute, Policy Memorandum No. 164, April 29, 2010, at 3, Available at: http://www.epi.org/page/-/pm164/pm164.pdf
- ²⁵ Se-Eun Jeong and Jacques Mazier, "Exchange Rate Regimes and Equilibrium Exchange Rates in East Asia," *Revue économique*, vol. 54, No. 5, September 2003, at 1174 and 1176, Available at: http://www.cairn.info/load_pdf.php?ID_ARTICLE=RECO_545_1161
- ²⁶ Se-Eun Jeong and Jacques Mazier, "Exchange Rate Regimes and Equilibrium Exchange Rates in East Asia," *Revue économique*, vol. 54, No. 5, September 2003, at 1174 and 1176, Available at: http://www.cairn.info/load_pdf.php?ID_ARTICLE=RECO_545_1161 and Ernest H. Preeg, "Exchange Rate Manipulation to Gain an Unfair Competitive Advantage: The Case Against Japan and China," *Dollar Overvaluation and the World Economy*, eds. C. Fred Bergsten and John Williamson, Peterson Institute for International Economics, at 270, Available at: http://www.piie.com/publications/chapters_preview/360/13iie3519.pdf
- ²⁷ Juan R. Espana, "The Mexican peso crisis: impact on NAFTA and emerging markets," Business Economics, July 1995, Available at: http://findarticles.com/p/articles/mi_m1094/is_n3_v30/ai_17221265/
- ²⁸ Anne O. Krueger, "NAFTA's Effects: A Preliminary Assessment," *The World Economy*, Volume 23, Issue 6, at 764, June 2000.
- ²⁹ Author's calculations based on data obtained from the United States Department of Agriculture Foreign Agricultural Service's Global Agricultural Trade System on January 21, 2011. Data was inflation-adjusted using the Consumer Price Index-U-RS as estimated by the Congressional Budget Office in the backup data for Table C-1 of their "The Budget and Economic Outlook: An Update", released August 2010. FAS aggregations used for beef were "Beef & Veal,Fr/Ch/Fz" and "Beef&Veal, Prep/Pres". FAS aggregations used for pork were "Pork, Fr/Ch/Fz", "Pork,Hams/Shldrs,Crd", "Pork, Bacon, Cured", "Hog Sausage Casings", "Pork,Prep/Pres,Nt/Cn", and "Pork,Prep/Pres,Cannd"

¹⁸ "S. Korean automakers hail KORUS FTA," Yonhap, Dec. 5, 2010.

¹⁹ Sewell Chan, "U.S. and South Korea Have Reached Trade Deal," New York Times, Dec. 3, 2010.

²⁰ U.S. International Trade Commission. "U.S.-Korea Free Trade Agreement: Potential Economy-wide and Selected Sectoral Effects." USITC Publication 3949. September 2007, Corrected printing March 2010, at Table 2.2.

²¹ 2008 data from the Current Employment Statistics of the Bureau of Labor Statistics (http://data.bls.gov/cgi-bin/dsrv?ce). Average hourly earnings for "other transportation equipment" was obtained by multiplying the average hourly wage of the aerospace products and parts, ship and boat building, and other transportation equipment industries by the number of workers in that industry, then dividing by the total number of workers in all three industries.