United States House of Representatives
Committee on Financial Services
Subcommittee on International Monetary Policy and Trade

Testimony of Matthew J. Slaughter
"Legislative Proposals on Securing American Jobs through Exports: Export-Import Bank Reauthorization"

Tuesday, May 24, 2011 2128 Rayburn House Office Building

Introduction

Committee Chairman Bachus, Committee Ranking Member Frank, Subcommittee Chairman Miller, Subcommittee Ranking Member McCarthy, and fellow members, thank you very much for inviting me to testify on these important and timely issues regarding America's Export-Import Bank and the broader national economy.

My name is Matt Slaughter, and I am currently Associate Dean and Signal Companies' Professor of Management at the Tuck School of Business at Dartmouth, Research Associate at the National Bureau of Economic Research, and Senior Fellow at the Council on Foreign Relations. From 2005 to 2007, I also served as a Member on the Council of Economic Advisers, where my international portfolio spanned topics on the competitiveness of the American economy.[1]

For today's hearing, you requested that I comment on possible actions "to optimize the performance of the Bank and its ability to serve U.S. businesses, small and large, to increase U.S. exports and promote domestic job growth." Specific topics you cited here included "the evolving and global nature of supply chains and how businesses evolve to compete in this environment" and also "the impact U.S. exports have on the creation of U.S. jobs."

In my remarks, I will first offer some broader economic context for your re-authorization deliberations. After this, I will discuss two additional issues regarding the competitiveness of U.S. companies in today's global economy. Linked to each of these three points, I will offer a recommendation about how the Export-Import Bank can better foster job creation to benefit American workers and their families.

[1] Currently and in the past two years, I have not received any Federal research grants. Currently, in addition to the affiliations listed above I serve as a member of the academic advisory board of the International Tax Policy Forum; an academic advisor to the Deloitte Center on Cross-Border Investment; an academic advisor to the Organization for International Investment, and a member of the U.S. State Department's Advisory Committee on International Economic Policy. For many years I have consulted both to individual firms and also to industry organizations that support dialogue on issues of international trade, investment, and taxation. For a listing of such activities, please consult my curriculum vitae posted on my web page maintained by the Tuck School of Business at Dartmouth.

Broad Economic Context: Exports Are Needed to Help Heal the Damaged U.S. Labor Market

First, it is important to emphasize how damaged the U.S. labor market remains today. Unemployment still sits at 9.0%, with about 25 million Americans still unemployed or under-employed. The 108.9 million private-sector jobs today is the same number we had nearly 12 years ago. The last time we had just 11.7 million manufacturing jobs, like we do today? April of 1941. America needs to find a way to grow millions of jobs as soon as possible. But to re-balance the U.S. economy away from excessive consumption (and thus trade deficits) that helped create the World Financial Crisis, America needs to grow millions of jobs linked to the global economy via exporting and related capital investment.

Academic research has documented the many ways in which exporting companies are stronger than non-exporters—even in the same detailed industry. Exporters tend to have about twice as many employees and sales. On a per worker basis, they tend to be about 10% more capital- and skill-intensive; their productivity and wages are also about 10% higher. It is typically high-innovation, high-productivity firms that expand beyond home into global export markets. That kind of dynamism America needs to dramatically expand today by supporting growth in U.S. exports. The President's goal of doubling U.S. exports from 2010 to 2015 is admirable. But achieving this goal will be difficult without substantial policy support for exports—especially given the reality that unprecedented monetary easing and fiscal deficits will, sooner rather than later, need to be withdrawn and reduced.

In light of today's still-fragile economic recovery and the pressing need to create millions of jobs linked to exports and related investment, I recommend that you expand the Export-Import Bank's funding cap by 200%--i.e., that its total liability cap be increased from $100 billion to $300 billion. This magnitude of increase can help support the twin goals of general economic recovery and the structural shift in aggregate demand that America's economy needs. Given Ex-Im Bank's long-running record of prudent lending and net transfers to the U.S. Treasury, this tripling should present little risk to America's overall fiscal condition, dire as that condition is.

The Rich Complexity of the Global Supply Chains of U.S. Exporters

Let me now address one of the most discussed features of current Ex-Im operations: its domestic-content requirement, which exporters and lenders have characterized as the Bank's greatest weakness. Current practice is to limit the amount of support for any export transaction to only the domestic portion of a good when its foreign content exceeds 15% of its export value. This domestic-content requirement is increasingly at odds with the global production networks that U.S. exporters are part of, and as such constitute a major constraint on the ability of American companies to benefit from Ex-Im support.

This rich diversity of production capacities around the world enables U.S. companies to locate different operations in different countries and thereby to better compete globally. There is no single strategy that works best for all companies at all times. The optimal global production configuration varies widely both across companies and over time. Production arrangements that make one company globally competitive can be very different from what works for other firms.

U.S. companies must make strategic investment and employment decisions from a truly global perspective. Moreover, globally competitive business models are not "one size fits all"—neither at a point in time across companies nor even over time within each company itself. Each company has a uniquely rich history that informs its current structure and strategies. As such, to best grow—including grow jobs in America—each firm needs the freedom to respond differently to the evolving opportunities and pressures of globalization. Indeed, this dynamic process of discovery—where and how to hire, invest, research, and sell—is critical for U.S. companies achieving and sustaining global competitiveness.[2]

An excellent historical example of this dynamic process of discovery is the global production networks of information technology. IT companies have been at the forefront of establishing and expanding production networks linked by trade and investment around the globe. Up until 1980, America was good relative to the rest of the world at making computers and related machinery. But then IT firms, thanks to rising domestic competition and opening borders, began to establish and expand global production networks.

Both falling natural and political barriers to trade and investment have driven the global engagement of the IT industry. Indeed, since the creation of the WTO the only industry to enact a free-trade agreement has been IT. Signed in 1996 by dozens of countries accounting for nearly 95% of world IT trade, the Information Technology Agreement eliminated over four years all world tariffs in hundreds of IT capital goods, intermediate inputs, and final products. This trade agreement facilitated the reconfiguration of global production, with U.S. IT firms moving to higher value-added activities such as core R&D, initial manufacturing, design, and marketing. Integral to the productivity success of IT has also been cross-border flows of ideas and people. IT demonstrates the important general point that immigrant inflows have long been a major force spurring U.S. growth by creating new ideas, new companies, and new links to global markets.

What impact did all this have on the United States? The best way to answer is in terms of productivity, which is the single most important metric to gauge the standard of living for any country. From 1973 to 1995, output per worker hour in the U.S. non-farm business sector grew

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[2] Data on U.S. multinational companies shows this heterogeneity quite clearly. Consider 2004, a year in which there were a total of 2,237 U.S. multinationals. That year, in 24% of these companies employment at foreign affiliates accounted for less than 10% of total worldwide employment. At the other end of the spectrum, in 3% of these companies employment at foreign affiliates accounted for over 90% of total worldwide employment. And for every company, successful arrangements today are very likely to differ both from what worked well yesterday and also from what will work well tomorrow. This rich variation can also be seen looking across broad industry groups. In 2006, 71.6% of the total global output of U.S. multinationals was accounted for by U.S. parents—with just 28.4% total accounted for by foreign affiliates. This total masks substantial variation in the production strategy of different industries. Multinationals in the broad industry groups of information and finance displayed an even greater U.S. concentration, with 87.6% and 85.9% of their global output, respectively, accounted for by U.S. parents. The very-strong U.S. orientation of these companies likely reflects the underlying U.S. strengths of strong intellectual-property protection and deep capital markets. In contrast, multinationals in the broad industry groups of wholesale trade and mining produced more in their affiliates than in the parents, with U.S.-parent shares of output of just 48.2% and 33.4%, respectively. The data and discussion in this footnote are taken from Matthew J. Slaughter, *How U.S. Multinational Companies Strengthen the U.S. Economy,* Business Roundtable and United States Council Foundation research report, Washington, D.C., March 2009/updated March 2010.

at just 1.35% per year. Then in 1995, U.S. productivity growth began to accelerate. From 1996 through 2007 it doubled, to an average annual rate of 2.70%. Thanks to the magical math of compound interest, the importance of this productivity acceleration is difficult to overstate. At the previous generation's growth rate, average living standards required 52 years to double. At the current growth rate, average living standards need just 26 years to double. This difference of 26 years spans an entire generation, and so carries profound implications for the well-being of all Americans.

For the decade after 1995, America's productivity acceleration was driven by one industry: computers and office products. Between half to two-thirds of the economy-wide productivity acceleration was driven by IT hardware, through two channels: a productivity acceleration in America's IT firms themselves, and also a boom in IT capital investment by firms throughout the economy in response to the accelerated price declines in IT.

The globalization of IT hardware—trade deficits and all—has helped boost average U.S. living standards. Cause and effect run in many directions between global engagement and productivity, and the ITA offers a textbook example of the benefits trade liberalization can deliver: a competitive spur to price declines and productivity gains in firms, to the benefit of not just the firms themselves but also of firms and consumers economy-wide via lower prices and new varieties. An excellent summary of all this dynamism is how today the back of every iPhone reads, "Designed by Apple in California, Assembled in China." But would Apple today qualify for Ex-Im Bank support to finance iPhone sales abroad?

The heterogeneity of optimal global strategies acknowledged, the presumption that globally engaged U.S. companies tend to rely on a vanishingly small amount of domestic U.S. content is simply incorrect. Data for multinational companies operating in the United States show this quite clearly.

In 2008, the U.S. parent operations of U.S.-based multinationals purchased $6.33 trillion in intermediate inputs, which was 72.5% of their total sales that year of $8.73 trillion. Of this $6.33 trillion in total input purchases, 88.8%—$5.62 trillion—was bought from other companies in the United States. Contrary to the common assumption that the global engagement of U.S. multinationals has eliminated their ties to domestic suppliers, nearly 89 cents out of every dollar spent by U.S. parents on intermediate inputs is paid to other companies in the United States, not companies abroad. And this heavy reliance on domestic suppliers has been virtually unchanged for decades: in 1977, U.S. parents purchased 91.3% of their inputs from other U.S. companies.

It is also the case that many of these U.S.-parent input purchases are from small and medium-sized enterprises in America. The U.S.-parent operations of the typical U.S. multinational buys goods and services from over 6,000 American small businesses; buys a total of over $3 billion in inputs from these small-business suppliers; and relies on these small-business suppliers for over 24% of its total input purchases. Collectively, U.S. parents purchase an estimated $1.5 trillion in intermediate inputs from U.S. small businesses, which is about 12.3% of their total sales.[3]

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[3] These big-little supplier linkages are reported in Matthew J. Slaughter, *Small and Big Business: Working Together for America's Prosperity*, Business Roundtable research report, Washington, D.C., September 2010.

A similar pattern of input purchases applies for the U.S. affiliate operations of foreign-based multinationals. In 2008, these companies purchased $2.78 trillion in intermediate inputs, of which 79.6%—$2.21 trillion—was bought from other companies in the United States. Contrary to the common assumption that the U.S. subsidiaries of global companies have very little tie to U.S. suppliers, nearly 80 cents out of every dollar spent by these subsidiaries on intermediate inputs is paid to suppliers located in America, not companies abroad.

And it is important to stress that these U.S. subsidiaries of global companies are a major source of U.S. exports. In 2008, these companies accounted for 18.1% of total U.S. exports of goods--$232.4 billion. These companies also accounted that year for 11.3% of U.S. private-sector capital investment and 14.3% of U.S. private research and development—all while employing 5.6 million Americans at an average annual compensation of $73,023, nearly one-third above the U.S. private-sector total.

The rich variety of global supply configurations of U.S. exporters means that domestic-content requirements are increasingly a competitive barrier for these firms that will tend to harm, not expand, U.S. job creation. I recommend elimination of the Export-Import Bank's domestic-content requirements. This should spur more companies to seek Ex-Im support for more transactions, the result of which would be more export deals leading to more U.S. employment and other U.S. activities. Others have recommended reducing these domestic-content requirements to something like 50%, which would be more in line with the practice of all our major trading partners. But given the magnitude of the economic challenges facing America today, I recommend a much bolder policy change to better support the export—and thus employment—opportunities of companies in America, both U.S.-based and foreign-based alike.

The Increasing Importance of U.S. Services Trade

The Ex-Im Bank has historically focused on supporting the U.S. export of goods. Yet some of America's strongest export industries are in services, not in goods. It is widely estimated that in recent years the United States is the world's single largest exporter of services—in 2010, $510.1 billion. Moreover, the United States has long run a multilateral surplus in services trade—in 2010, of $155.5 billion. This surplus in services trade reflects America's comparative advantage in services that rely on American strengths including highly skilled labor, information technology, and organizational capital.

For America to create millions of jobs linked to exports, many of these jobs will have to be linked to services exports. Merchandise trade alone almost surely will not be sufficient, given the data I cited earlier that today only 11.7 million U.S. payroll jobs are in manufacturing—just 8.9% of America's total. There are many policy changes the United States will have to undertake to help expand our services trade. But one of these changes can be greater Ex-Im Bank support for services trade. *I recommend that the Ex-Im Bank endeavor to expand its lending for all types of services trade—both stand-alone services and also the services related to merchandise exports, such as after-sales technical support and maintenance.* The current Ex-Im Bank charter mandates full consideration of services exports, but this activity is only a small portion of overall Bank operations.

Conclusions

America's economic challenges today remain large. To fully recover from the Great Recession, we need to create millions of good jobs at good wages. To achieve this goal, America needs leaders with the vision and courage to craft innovative policies. Reauthorizing the Ex-Im Bank to be both larger and nimbler can be one such policy, and I have offered three tangible recommendations for how to do this.

Let me close by thanking you again for your time and interest in my testimony. I look forward to answering any questions that you may have.

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1. Name:	2. Organization or organizations you are representing:
Matthew J. Slaughter	Tuck School of Business at Dartmouth
3. Business Address and telephone number:	
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4. Have you received any Federal grants or contracts (including any subgrants and subcontracts) since October 1, 2008 related to the subject on which you have been invited to testify?	**5. Have any of the organizations you are representing received any Federal grants or contracts (including any subgrants and subcontracts) since October 1, 2008 related to the subject on which you have been invited to testify?**
☐ Yes ☑ No	☐ Yes ☑ No
6. If you answered .yes. to either item 4 or 5, please list the source and amount of each grant or contract, and indicate whether the recipient of such grant was you or the organization(s) you are representing. You may list additional grants or contracts on additional sheets.	
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