



Written Testimony

of M. Brian O'Shaughnessy, Chairman, Revere Copper Products, Inc.

on behalf of Revere

and the Coalition for a Prosperous America

before the Investigation and Oversight Subcommittee

of the House Science and Technology Committee

on Globalizing Jobs and Technology

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Who Do You Represent?

Three and a half million manufacturing jobs have been lost in the USA since the year 2000. Some attribute it to increased productivity - but previous recoveries typically resulted in a loss of about one million jobs in spite of productivity increases. Some think it is our country's responsibility to support fledgling economies because we are the strongest, most powerful nation in the world. Some say we need to set a good example and others will follow. Make no mistake about it, protectionism should not be the end game but it seems to be an acceptable practice when used by everyone but the USA.

No matter how we try to rationalize it, millions of manufacturing jobs are going overseas.

I'm sure this committee is well aware of the significant connect between manufacturing and research and development. *Manufacturing and Technology News* just ran an article on May 16, 2008 that puts the foreign flight of technology in perspective. The article is titled, "China Displaces United States In Georgia Tech's Technology Index."

The article states, "China has surpassed the United States in a key measure of high tech competitiveness. The Georgia Institute of Technology's bi-annual *High-Tech Indicators* finds that China improved its technological standing by 9 points over the period of 2005 to 2007, with the United States and Japan suffering declines of 6.8 and 7.1 respectively. In Georgia Tech's scale of one to 100, China's technological standing now rests at 82.8, compared to the U.S. at 76.1. The United States peaked at 95.4 in 1999. China has increased from 22.5 in 1996 to 82.8 in 2007."

"The message speaks out pretty loudly," says Alan Porter, co-director of Georgia Tech's Technology Policy and Assessment Center, which produces the benchmark.

"I think the prospects are pretty scary."

My company is Revere Copper Products. We were founded in 1801 by Paul Revere and believe we are the oldest manufacturing company in the USA. Our factory is in Rome, New York and produces copper and brass sheet, strip, coil and extruded products for shipment to other manufacturing companies. Revere is a domestic manufacturing company and outsources nothing.

My unwillingness to outsource or sell out is based solely on loyalty and patriotism.

Please note that I also represent and serve on the Board of Directors of the Coalition for a Prosperous America (CPA). This coalition includes domestic manufacturing, organized labor, farming and ranching. You should visit CPA at www.prosperousamerica.org. My testimony includes positions on issues that have not yet been considered by CPA but are ever present in Revere's besieged financial results.

So Revere is part of the copper and brass industry of the USA. In December, 2006, China's State Assets Supervisory and Administration Commission (SASAC) which is second only to its politburo directed that this industry in China be designated a "heavyweight" and a "vital artery of the national economy and essential to national security."

Revere's founding was considered vital to US national security in 1800.

The US government loaned Paul Revere \$10,000 to construct the first copper rolling mill in North America. The War Department was concerned about another war with the British and worried about the domestic content of its naval vessels to wage such a war. The USS Constitution needed copper sheathing to prevent barnacles from growing on its sides underwater. Barnacles would slow the ship and cause extra time in dock to remove them. Such copper was previously rolled in Britain.

That's how Revere started and how the USS Constitution came to be sheathed with Revere Copper.

Today, many of Revere's customers are manufacturing companies located throughout the USA. Since 2000, about 30% of these customers have shut down, moved offshore or outsourced their production. Revere's customer mix is quite broad ranging from building and construction, transportation, electrical and electronics including weapon systems. Revere's engineers work on research and development projects regarding national defense applications including the nation's new aircraft carrier under construction, the *Gerald Ford*. But in the context of Revere's history, let's just describe what happened recently to the production of a simple silver bowl.

Of course, this silver bowl was designed by Paul Revere.

In the year 2000, Revere shipped copper coils about 20 miles to Oneida Ltd. Oneida cut and formed that copper into a bowl and plated it with silver to produce a *Paul Revere* silver bowl. Now, that product is as American as apple pie, right? Wrong. Today, that bowl is manufactured in China and shipped to Oneida and sold as a Paul Revere *replica*. You probably believe that the people of Revere just can't compete anymore with the people of China.

Let me explain why our people can compete but our government does not.

Let's assume the production cost of that silver bowl made in China is 100 yuan. China manipulates its currency so that the exchange is now about 7 yuan to \$1. So the production cost in China is \$14.28. But if the free market were to determine the rate of exchange, it would be about 4 yuan to \$1 and the production cost in China would be \$25.00.

In other words, China manipulates its currency so that it subsidizes the cost of manufacturing in China.

The current and the former US administration have refused to take any concrete action against such manipulation by China and have chosen instead to jawbone. The problem with this strategy is that currency manipulation by China is serving its best interests.

The manipulation of its currency reduces the competitiveness of every other product, good and service in the world when compared to its production in China.

This form of protectionism by China is reaping huge rewards as its export-based economy is growing 3 or 4 times faster than the rest of the world with factories being built at a pace beyond the imagination of anyone just a few years ago. Meanwhile, factory jobs are disappearing in the USA and the world. Even manufacturing plants in Mexico are moving to China.

But this is more than an economic battle.

Did you catch the statement by Congressman Tim Ryan of Ohio concerning the paper (“Unrestricted Warfare”) written by two Chinese military strategists? They suggested that military supremacy be achieved by undermining the manufacturing base of the United States by maintaining China’s currency at artificially low levels to gain an economic advantage for Chinese manufacturing and destroying the manufacturing base of the United States. Seems to be working, doesn’t it?

Personally, I admire the Chinese culture and believe that China does not need such a disruptive currency policy to compete in the world given its many other advantages. The Chinese economic policy is export driven by taxing its citizens through currency manipulation which drives inflation and takes away their disposable income. A market driven currency exchange rate policy would drive China’s economy toward domestic consumption and a better life for its citizens.

But make no mistake about it, China is waging a mercantile war on the world and the world is sleeping.

Why is the world sleeping? First, we must look at the role of the multinationals. Remember in the 1980s when Japan was such a fierce competitor in so many US markets. The reaction by our largest corporations was loud and largely one voice calling for tariffs and restraints. Contrast that with today as most of the largest US corporations are so much more international and especially with their investments in China. Many that do not have direct investments in China buy substantial numbers of components from China’s factories. Many have set their strategic plans to produce components or products in China.

It may surprise you to learn that I don’t have a problem with any company that sets up a plant offshore or imports components or products. But if manufacturing in America must compete with the protectionist policies of any foreign government, that is not fair. And if meaningful corrective action by the US government is thwarted by US manufacturing and financial service companies who gain from such protectionism, that is wrong. CEOs of multinational companies are put in a very difficult position by national trade policies.

They have to choose between their company and their country.

Let me explain. Earlier I mentioned that China practices a policy of managing its currency at artificially low levels to gain a competitive advantage for any export products or services produced in China...by as much as 40%! Now, you must realize a simple truth, a multinational that manufactures in China and benefits significantly from this advantage doesn’t want this to change.

It is not my intention to vilify multinationals or the capable CEOs who run them. These executives are charged with representing the best interests of their shareholders. Also, many of these CEOs of “American” companies are not US citizens nor are many of their shareholders. For example, the Chairman of Coca-Cola is Irish and its President is Turkish!

It is important to appreciate that it is in our nation’s best interest to have the corporate headquarters of a multinational located in the USA even if it has no remaining production facilities here. That is not so that they can be taxed and regulated and driven away but so that the high skilled, corporate level jobs are here not there...

So when issues such as patriotism are raised in this paper, it is really an appeal to US political leadership not that of multinational corporations.

Companies that manufacture in the USA and must compete with either multinationals or companies that outsource components from abroad believe currency manipulation is unfair and must be stopped. They see other US based manufacturing plants shutting down and are concerned that will be their fate. These domestic manufacturing companies want the US government to take effective action to right this wrong and the sooner, the better.

At a 2006 meeting I attended of an international economic policy committee of an association of manufacturing companies, one manufacturing company said that it buys components from China and does not want the current situation to change. Now there's a breath of honesty. Maybe not patriotic but at least he's honest.

Patriotic...why bring that word into the mix?

Well, you see the strength of manufacturing is an inherent strength of our country. Some economists believe our country is in a transition from a manufacturing economy to a service economy just as it transitioned from an agricultural economy to a manufacturing economy years ago. But maybe the manufacturing economy was simply layered on top of our agricultural economy just as the service economy is layered on the manufacturing economy. And it is certainly hard to argue against the proposition that a weak manufacturing sector threatens our national security.

Even so, some economists cite data that the manufacturing sector is doing just fine as it is producing more than ever before. Such data is misleading and you should consider the source. For example, statistics on US produced products include Dell computers which are merely assembled in the USA from components produced abroad. We could argue endlessly about this but the facts are the facts and the fact is we have become a nation with a colossal trade deficit. In 2005, for the first time in over a hundred years, our nation imported more food products than it exported and our trade deficit in manufactured goods continues to soar. Indeed, our nation's trade deficit is growing by \$2 billion a day! (More about this later...)

Sounds like our nation needs some help.

Or at least some good advice...and that leads me to integrity. You see when a CEO attempts to push an agenda that supports Chinese protectionism rather than an agenda that goes against that protectionism, maybe that CEO should declare that he or she is conflicted on this issue and should be recused from any forum that determines US trade policy. Many of these CEOs have plants in the USA which would benefit from freer trade but they support their growing investments in plants in China and outsource components from China by choosing their company's best short term interests over that of their own domestic plants and their country.

That's because they have to but you don't!

Supposedly, one issue before us today is how to stop China from managing its currency so as to give its production of goods and services an unfair competitive advantage. Or, is it? If you recall, earlier I mentioned the multinational delegate, the honest one...he said he was against a proposal that would raise his prices on the components he buys from China. I believe the real issue is, "Should the USA support measures that will not work so multinationals can support them or should the USA support measures that will work to cause China to change its policy of managing its currency?"

The multinationals have endless arguments for stretching out the process like.... “We don’t want to start a trade war now, do we?” *But we are already in a trade war, aren’t we?* Of course we are and we are losing. *We are pacifists in this war.* How about this one by the multinationals... “Your policies are protectionist!” Yes, they actually say that, can you imagine? Often the accuser benefits from China’s export subsidies which are clearly prohibited by the WTO as protectionist.

The irony is that domestic producers are the victims of protectionism not the beneficiaries.

Another argument we hear is, “What about their fragile banking system?” This one has been around for years and of course, it is impossible to amend an economic strategy let alone a banking system that depends on subsidization to such an extent without removing the subsidy, isn’t it? Besides, their banks are owned by the same government that is holding more than 1.7 trillion US dollars worth of official reserves. Maybe their banks are not quite as insolvent as you have been lead to believe...

China set up a system to manage the movement of its currency toward market levels and then used it to move its currency at rates about 4 % per year compared to estimates of an underlying rate of appreciation of 5% of its currency, thereby exacerbating the problem.

Even if China were immediately to stop manipulating its currency, there is nothing to deter China from returning to the policy at a time of its choosing. Equally, other countries would be free to continue or adopt similar mercantilist policies with impunity. In fact, the author of a paper published by the UN Conference on Trade and Development in “China in a Globalizing World” (2005) has advised developing countries that “China’s experience in the past decade can be seen as a model of a successful development strategy.”

The author continued, “As in other Asian countries in the past, fixing the real exchange rate at a favourable level and promoting exports offers the possibility of penetrating world markets rapidly and experiencing strong growth and capital accumulation. The penetration of foreign markets brings about the rise in income needed to finance increased investment without recourse to net foreign capital inflows.”

The experience so far is that China is going to delay as long as it can and make corrections in as small increments as it can get away with given its support.

Part of that support comes from US trade objectives which please the multinationals that are aligned with the trade policies of China. Never give in on trade issues, but, if ever, give slowly....

There is no easy solution to this Chinese puzzle. Even I have supported the verbal approach...for years. Our nation could simply slap a tariff on all imports from Chinese and other nations that manage their currency but I think we must take measured concrete steps that increase in severity before such a step.

China is not the only country that manipulates its currency to gain a competitive advantage. Other Asian nations also manipulate their currency partly as a defensive mechanism so their producers of goods and services can compete with goods and services originating from China.

It is important to understand that the end of currency manipulation will not end the depreciation of the US dollar against other currencies including China’s yuan.

For this reason, it is difficult and perhaps impossible to develop a coherent trade policy to deal with China without considering the tax policies of our own country. China uses a Value Added Tax (VAT) to protect its domestic production of goods and services and uses its revenues to fund government programs such as national health care. VATs are a tax but they are also a form of tariffs which are largely exempt from World Trade Organization (WTO) rules. The WTO was established to advance world trade. It has developed ground rules for international commerce and mediates trade disputes. Of course, China also employs a VAT tax but unlike everyone else, the VAT is applied in a discriminatory manner which is in direct violation of WTO rules.

Market determined exchange rates simply put all nations back at the starting gate for the race to determine who will win the battle to produce competitive goods and services *assuming all other things are equal*. Of course, all other things are *not* equal and because of this our nation's inability to compete with China and the rest of the world means that our currency will continue to depreciate and the standard of living of all Americans will decline and our nation will grow weaker.

This is because other trading nations use revenues generated by Value Added Taxes (VATs) to reduce the tax and health care burden on their production of goods and services and the most ambitious nations are developing energy policies which give them a competitive edge.

Here is a real world example of how VATs are used by other governments to protect their industry. Revere had an industrial plate mill in New Bedford, Massachusetts for 145 years. The plate was used in heat exchangers and in unique applications for US national defense. It was considered the best quality plate in the world. Its major competitors were located in Germany but could be located in China and the principles and the result would be the same. These competitors were able to undercut Revere's prices thanks to a VAT that the German government applies to all goods and services sold in Germany, domestic or imported.

When New Bedford shipped its plate to Germany for its consumption, that plate paid the 19% German VAT tax. If the German mills ship plate to the USA, the 19% VAT tax is rebated. VAT revenues allow the German Government to help fund national health care costs and reduce corporate taxes. So German competitors pay far less in taxes and medical costs. Medical costs alone amount to about \$10,000 per employee for Revere. Ironically and tragically, the New Bedford workers had to bear the burden of helping to pay for the health care of the German workers they competed with through the payment of German VATs on any Revere products shipped to Germany.

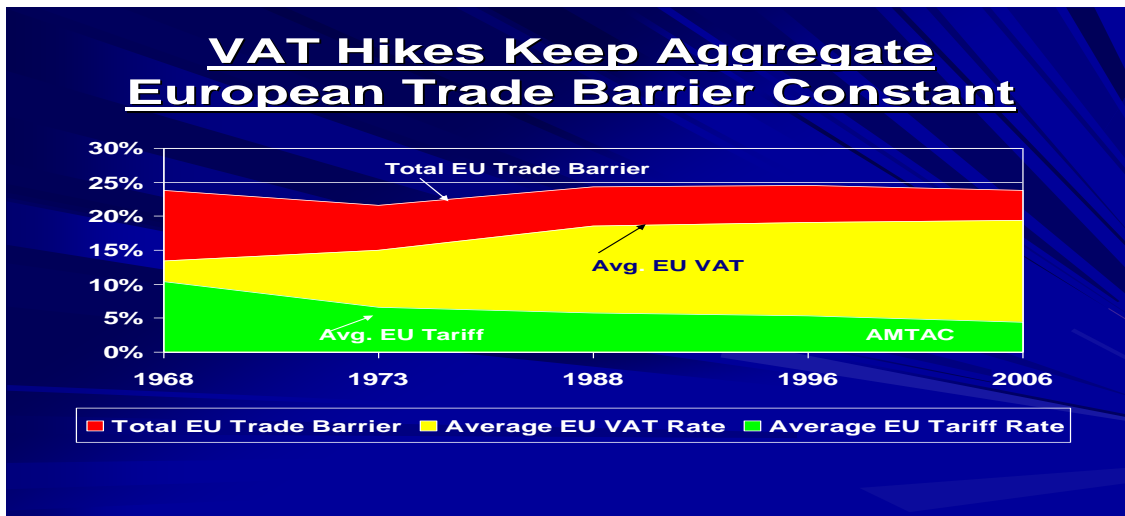
Naturally, Revere hardly shipped any product to Germany while its German competitors just loved the US market.

Meanwhile, the American worker is expected to respond to these pressures by increasing productivity and reducing waste. The people at Revere's New Bedford plant did that at an astonishing pace, averaging productivity improvement at the rate of 10 percent a year for the last six years. During this period the workers and management of this mill did everything that was asked.

Yet, even that wasn't enough---on March 5, 2007, Revere announced the closure of its New Bedford mill and the loss of 87 good paying jobs.

In recent years, the USA has been negotiating Free Trade Agreements (FTAs) in an effort to get other countries to lower tariffs. This has led to the North American Free Agreement (NAFTA) in which the US, Canada and Mexico reduced outright tariffs. Around the time of the negotiations, however, Canada instituted VAT taxes while Mexico increased its VAT rates. VATs are excluded.

How can the USA continue to negotiate trade agreements allowing other nations to offset tariff reductions with VATs and other forms of border adjustable taxes and manipulate their currency?



These VATs are applied on our products by over 140 foreign countries. The chart above shows how the European Union countries have managed to increase VATs while lowering other types of tariffs – keeping the effective tariff the same despite trade agreements. Mexico and Canada have made similar adjustments despite FTAs. Countries that sign FTAs are free to replace the tariffs they give up with VATs charged on our goods sold to them.

The revenues collected by the foreign countries help pay for the health care cost of their manufacturing workers that US workers must compete against. Foreign countries also have to collect VATs on their domestic production to comply with World Trade Organization (WTO) rules on trade but then use them to lower corporate and payroll taxes on domestic production of goods and services. Foreign producers gain even further as their nations refund their VATs on exports.

VATs protect the domestic production of goods and services in any country that has them. The lack of a VAT in the USA allows European nations to gain market share from the USA partially offsetting the impact of China's manipulation of its currency on the production of goods and services in Europe. That's one reason why Europe is less vocal about China's mercantile war. The lack of VATs in the USA also largely explains why the USA has a trading deficit with virtually every other trading nation in every class of goods.

VATs have been adopted by all of the world's major trading nations, excluding the USA and some oil producing Middle Eastern nations.

Another nail in the coffin of US manufacturing would be if the USA were to sign the Kyoto Treaty. The Kyoto Treaty exempts China, India, Brazil and other developing nations from its standards. But the carbon emissions per \$1,000 of GNP in China are seven times that of the USA while India emits three times as much. The Kyoto Treaty and other measures such as Regional & National Greenhouse Gas Initiatives and carbon cap and trade schemes drive manufacturing from developed countries with more strict standards to countries with much worse practices.

These treaties and regulations have the unintended consequence of increasing carbon emissions and global warming as factories are shutdown in the USA and Europe and production increases in China.

During the days of substantial aid programs by the USA to developing nations, the primary consideration was to build an infrastructure. That included large scale projects to supply low cost, economic energy. Of course, what is true for developing nations is also true for developed nations that must compete in a global economy....the provision of low cost, competitive power is essential to success.

The gigantic footprint of windmills, solar energy, bio-fuels, and hydropower is so vast and the costs so uneconomic that no nation that is serious about engaging in the global competition for skilled jobs is embarking on these power programs to the extent of the USA. Any energy source that must be mandated, subsidized and surcharged to such an extent cannot be economic, can it?

In my opinion, the best large scale, low cost source of clean energy is nuclear. China is planning 40 new nuclear power plants; Japan is building 10 more while France relies on nuclear for 80% of its electricity. Why? Nuclear power is clean and low cost if sitting and environmental concerns are managed. Nuclear waste is dangerous but can be contained in areas much smaller than most people realize. Thirty years of nuclear waste from a 1,000 MW plant would fit in an area the size of a high school gym. If other countries can do it, why can't the USA?

The loss of manufacturing jobs to date in the USA is only the tip of the iceberg. The impact of currency manipulation, VATs and environmental/energy costs are not limited to manufactured goods. Any goods and services that compete in global markets, either directly or as part of a supply chain, are exposed to these protectionist forces. Future losses will go far beyond the continued loss of manufacturing jobs and extend to the agriculture, food processing and service industries. Indeed, Alan Blinder, former Federal Reserve Vice Chairman, was quoted in the Wall Street Journal on March 28th saying that, "...as many as 40 million American jobs (are) at risk of being shipped out of the country in the next decade or two."

Policy makers and citizens must realize the urgency of the matter. The USA must see itself as a competing nation...competing in a global market for good paying jobs. But it's not only about jobs. It is also about national security and our entire economy. Factories producing goods and services necessary for US national defense are moving offshore. The US trade deficit is growing \$2 billion a day. China and Japan have *each* accumulated more than US\$1 trillion. The accumulation of US currency by China and other Asian nations is a *growing* bubble.

So, the looming question is, "What should be done to counter this offensive and protective behavior by other nations?"

First, the USA cannot continue to negotiate global or bilateral trade agreements as long as the other country is free to manipulate its currency and use VATs to offset any tariff reduction. Also labor, environmental, antitrust, quality and intellectual and other property standards in free trade agreements must be equivalent to the burden placed on manufacturing, farming and ranching in the USA or we just cannot compete and provide jobs in the USA.

Can you imagine competing in a global market that gives your competition an eight year head start? Yet, that is exactly what is being proposed to kill jobs in current House legislation for domestic manufacturing to cap and trade *and die*. If the environmental burden is unfair for foreign competitors, it's unfair for us.

In the global trade war, who do you represent?

Second, the manipulation of its currency by China or any nation is unacceptable. The first step should be to pass the Ryan Hunter bill (H.R. 2942) that would define currency manipulation as an illegal subsidy and allow the application of Countervailing Duties (CVDs) to offset the injurious impact of the currency manipulation. The Ryan Hunter bill is designed to be compliant with the rules of the WTO. That being said, if the WTO refuses for any reason to sanction the use of CVDs to offset currency manipulation, we must assume that the system that governs world trade is broken and must be fixed. Immediately!

If the use of CVDs to offset currency manipulation does not lead China to stop manipulating its currency, then the USA must take stronger measures, even if it means stepping outside WTO rules.

Third, the USA must reform its tax and health care systems and institute VATs on a scale that gives production of goods and services in the USA a competitive advantage.

A smart competitor never looks at where a competitor is and tries to match that position. A smart competitor might try to match where a competitor is going to be at a certain time. But the most intelligent competitor attempts to gain a competitive advantage by providing a product beyond where the competition is going to line up in the race.

In order to achieve this objective, the USA must significantly reduce or eliminate all national taxes, both corporate and personal, including income, dividend, capital gain, estate, FICA and unemployment taxes and replace them with a consumption tax like a VAT. Under current international trade rules, consumption taxes can be rebated on exports and imposed on imports. The US refuses to reciprocate, disadvantaging all American-made goods that compete with imports or are offered for export. No wonder, we have such a massive trade deficit!

The regressive nature of a VAT or consumption tax should also be offset by the provision of a national health care system to offset the unique American health care "tax on jobs."

A national health care system could utilize private insurance to provide the best choice to US consumers or we could adopt a system similar to that employed by Great Britain. It provides universal health care for all but allows any citizen to opt out to private care as long as they are willing to pay the cost. I am not aware of any nation that is considering dropping its health care system to adopt the system used in the USA which eats up twice as much GNP per capita and burdens the domestic production of goods and services. My concern is simply that health care cannot be paid for by job providers in the USA competing with job providers abroad who pay little if any health costs.

Either the US government solves this problem or outsourcing will resolve it.

Also, adverse impacts on charitable and lending institutions need to be offset by matching charitable grants and providing housing subsidies which could further offset the regressive VAT system and make it fair. The new system should be designed to be revenue neutral for all classes.

Fourth, the USA needs to ensure that its citizens and businesses have access to substantial, additional low cost, clean energy so that they are able to compete on the world stage *and* keep the environment clean. The USA should use a system similar to the one used by the Base Realignment and Closure (BRAC) Commission to determine the location of surviving military bases to site

nuclear power stations throughout the USA. Competing nations all over the world are building terminals and pipelines to receive natural gas to supply their manufacturing and economic base. So must the USA. We simply must not allow the events of 9/11 to destroy our nation's ability to compete by stifling the expansion of natural gas terminals and pipelines.

The U.S. is alone among major trading nations in the world without a national trade policy.

The result is that the U.S. is being defeated in international trade. American manufacturers are extremely efficient. Indeed, I would argue those still remaining are the most efficient in the world because they are surviving despite unfair foreign protectionist practices that general trade agreements like GATT and Free Trade Agreements (FTAs) allow to continue.

The demand in the U.S. for durable manufactured goods has soared about 400% since 1980 as our economy has grown. But U.S. production of these goods grew only 40%. Without foreign government trade cheating, U.S. production would have been far greater. Revere Copper's exports and domestic sales would have grown very large indeed.

Our nation's focus on general trade agreements and FTAs is misguided, inadequate and lacks strategic thinking. Although I am a proponent of free trade, the agreements to date compound the problem, while deceiving many who think free trade is being promoted.

China and the rest of the world are waging a mercantilist war on the U.S. and the U.S. is sleeping as its factories, farms and ranches are being systematically destroyed. We desperately need a national trade policy instead of a patchwork of trade agreements that deepen the current problems and enable foreign protectionism. That is what we should be hearing about from our Congress and the remaining Presidential candidates. We are running out of time. What a mess we are leaving our children. This is one problem that has real solutions.

Our government needs to focus on the big picture of global trade and address these problems with a national trade policy immediately.

When Paul Revere tried to rouse the countryside with his wake up call, what did the people do? They certainly didn't go back to sleep. We all need to wake up and listen. But we must be careful who we listen to...

Wake up, America!

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