



Written Testimony

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a Witness

on behalf of Revere *and the* China Currency Coalition (on China currency)

before the Ways and Means Subcommittee on Trade; *the* Financial Services Subcommittee on Domestic and International Monetary Policy, Trade, and Technology; *and the* Energy and Commerce Subcommittee on Commerce, Trade and Consumer Protection.

on Currency Manipulation and its effects on U.S. business and workers.

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International Trade: Myth vs. Reality

Three 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.

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. We have two plants. Our large mill is in Rome, New York and produces copper and brass sheet, strip and coil. Many of its customers are manufacturing companies located throughout the USA.

Since 2000, about 30% of these customers have shut down or moved offshore. You can see why if you simply go to any big box store and look at any item made of copper or brass. Turn it over and you will likely see that the product is now made in China. That's because the cost of manufacturing in China is so much cheaper, you believe. At least, that is what you have been told...

Once you start looking at the facts, however, you will see a very different picture.

Let's say the production cost of a brass doorknob in China is 100 yuan. If the exchange rate for converting yuan to dollars is controlled by the government of China at 8 yuan to \$1, then the production cost is equivalent to \$12.50. But if the exchange rate was allowed to be determined by market forces, it would be about 5 yuan to \$1 and the production cost in China would be equivalent to \$20. So a company that produces that doorknob for \$18 in the USA is going to lose market share and be shut down.

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 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 a significant number, but not all, 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 many 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.

This country is more than multinationals and financial service companies.

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 or traditional US based company 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 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 such as this hearing. 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 component imports 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, the 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?"

Those multinationals who gain from currency manipulation 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 same group of 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. According to a story in *USA Today* on May 3, 2007, Ralph Gomory, president of the Alfred P. Sloan Foundation and a former top executive at IBM, attacks a growing divergence between multinationals and US best interests.

The irony is that domestic manufacturing companies are the victims of protectionism not the benefactors.

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 almost a trillion US dollars. 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 3.5 % per year compared to estimates of an underlying rate of appreciation of 5% of its currency, thereby exacerbating the problem.

So, 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 policy which pleases the multinationals that are in alignment with the policy of China. Never, but, if ever, 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. Several other Asian nations also manipulate their currency for the same reasons and 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 has had an industrial plate mill in New Bedford, Massachusetts for 145 years. The plate is used in heat exchangers and in unique applications for US national defense. It is considered the best quality plate in the world. Its major competitors are located in Germany but they could be located in China and the principles and the result would be the same. These competitors are 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 ships its plate to Germany, that plate must pay the 19% German VAT tax. If the German mills ship plate to the USA, the 19% VAT tax does not apply. Revenues from VATs allow the German Government to help fund national health care costs and reduce corporate taxes. This means that Revere's German competitors pay far less in taxes and medical costs for their employees. Medical costs alone amount to about \$10,000 per employee for Revere. Ironically and tragically, the New Bedford workers must bear the burden of helping to pay for the health care of the German workers they compete with through the payment of German VATs on any Revere products shipped to Germany. Of course, the German government doesn't reduce taxes for the New Bedford plant nor does it provide any health care for the New Bedford workers.

Naturally, Revere hardly ships any product to Germany while its German competitors just love 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 of them and more.

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 tariffs but are excluded from NAFTA and other FTAs

How can the USA continue to negotiate Free Trade Agreements while other nations are free to offset their tariff reductions through employing VATs and other forms of border adjustable taxes and manipulate their currency?

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 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 are 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?

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 about US\$1 trillion in reserves. 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 FTAs as long as the other country is free to manipulate its currency and VATs to offset any tariff reduction.

Second, the manipulation of its currency by China or any nation is unacceptable. The first step should be to pass the Ryan/Hunter bill that would define currency manipulation as an illegal subsidy and allow the application of Countervailing Duties (CVDs) to offset the 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 eliminate all national taxes, both corporate and personal, including income, dividend, capital gain, estate, FICA and unemployment taxes as well as lifting the burden of health care costs off employers who provide jobs. A new national VAT system can replace these revenues. The regressive nature of a VAT system would be offset by the provision of a national health care system. 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.

A national health care system similar to that employed by Great Britain has features that would appeal to all Americans. 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.

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.

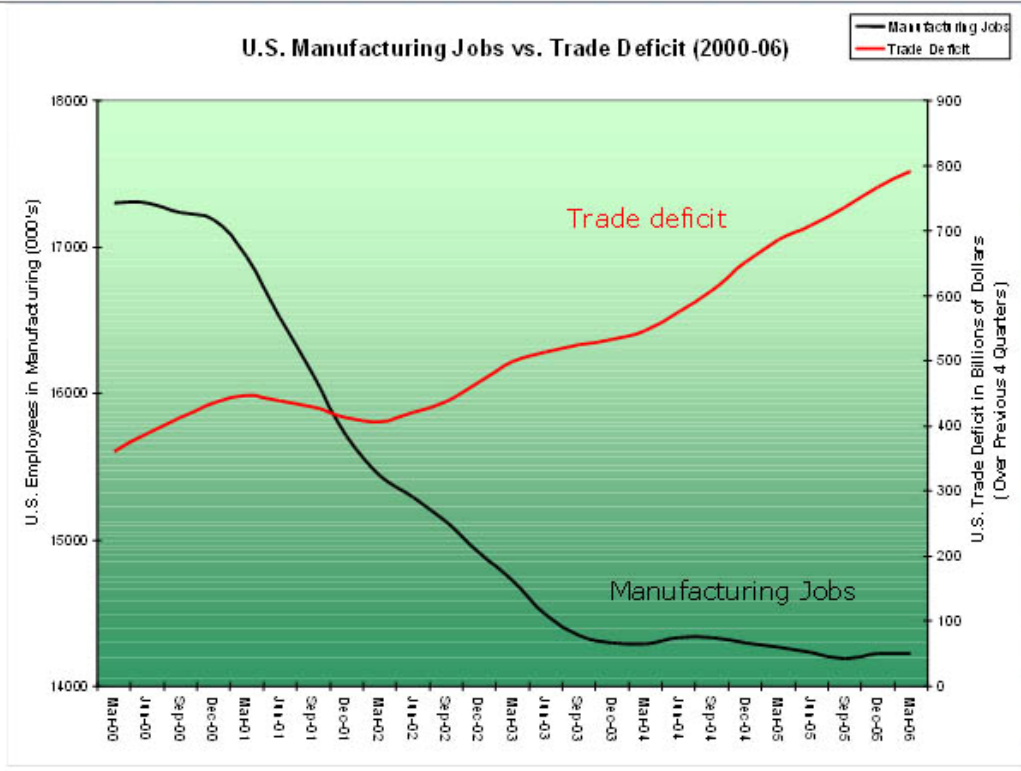
When Paul Revere tried to rouse the countryside with his wake up call, what did the people do? They certainly didn't go back to sleep. We all need to wake up and listen. But we must be careful who we listen to...

Wake up, America!

Visit: reverecopper.com and learn more

Schlage Lock
Kwikset Locks
Price Pfister
Carrier
Oneida Silversmith
Intri-Plex
Leviton Mfg

Notes: Since 2000, about 30% of the manufacturing plants that Revere shipped to have shutdown and/or moved offshore.



Notes: We do know that 3 million manufacturing jobs have been lost since 2000. Previous recoveries averaged about 1 million job losses.

Some Countries Using VAT Tax to Support Factory, Farm & Service Jobs

| | | | |
|----------------|---------|-------------|-----------------|
| Australia | Finland | Japan | Russia |
| Austria | France | Korea | Singapore |
| Belgium | Germany | Luxembourg | Slovak Republic |
| Brazil | Greece | Mexico | Spain |
| Belgium | Hungary | Netherlands | Sweden |
| Canada | Iceland | New Zealand | Switzerland |
| China | India | Norway | Thailand |
| Czech Republic | Ireland | Poland | Turkey |
| Denmark | Italy | Portugal | United Kingdom |

Notes: 139 countries have a border adjustable tax which discriminates in favor of domestic production of goods & services. One province in India boasts of a VAT tax over 50% in promoting itself as a prime location.

Countries Not

USA

Notes: The US currently has a trade deficit with almost **EVERY** trade competitor in almost **EVERY CLASS** of goods. Some Middle East oil producing nations have no VAT taxes but they have few, if any, other taxes.