FULL COMMITTEE HEARING ON SMALL BUSINESS EXPORTS IN THE CURRENT ECONOMIC CLIMATE

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FULL COMMITTEE HEARING ON SMALL BUSINESS EXPORTS IN THE CURRENT ECONOMIC CLIMATE

Thursday, June 19, 2008

U.S. HOUSE OF REPRESENTATIVES,
COMMITTEE ON SMALL BUSINESS,
Washington, DC.

The Committee met, pursuant to call, at 10:06 a.m., in Room 1539, Longworth House Office Building, Hon. Nydia M. Velázquez [Chair of the Committee] Presiding.

Present: Representatives Velázquez, Shuler, Larsen, Ellsworth, Chabot, Akin and Davis.

OPENING STATEMENT OF CHAIRWOMAN VELÁZQUEZ

Chairwoman VELÁZQUEZ. Good morning. I call this hearing of the House Small Business Committee to order.

It is no secret that the Nation's economy is struggling. Just last month, the unemployment rate reached 5.5 percent, hitting its highest point in 4 years; and with the rising costs of basic commodities, few Americans remain untouched by the increasingly fragile economy. During past downturns, America's small businesses have helped jump-start the economy through trade, but, unfortunately, that has not been the case today. In this hearing, we will review the current economic climate and explore the barriers hindering this vital sector. History has shown trade to be the silver lining in a weak economy.

In the early 1990s, for example, the country was reeling from a demoralizing recession. In fact, the situation was not at all that different from the one we face today. But rather than allowing the era's weak economy to hold them back, American businesses looked to opportunities abroad. As a result, U.S. trade led the way into the booms of the late '90s, when American exports skyrocketed from $535 million to just over $1 billion.

But today American exports are declining rather than rising, and the rate of decline has been extreme. In the 2 months between February and March of this year, U.S. exports dropped $2.5 billion. These figures are simply unbelievable.

To say that export numbers are declining would be an understatement. Export numbers, are not falling, they are plummeting. We now know that commerce is falling sharply for businesses in the areas of capital goods, industrial supplies, and advanced technology. Last month alone, these industries witnessed a $100 million drop-off in exports.

And these kind of declines are not industry isolated, either. Trade with NAFTA countries, the bread and butter for small business exporters, has also dropped off considerably. In fact, commerce has slowed to virtually every foreign port.

These declines are also manifesting themselves domestically, where trade with our major partners in our top 10 ports is down $100 million. Still, it seems the worst is yet to come. Export orders, a leading indicator of future trade, show no light at the end of the tunnel. Instead, recently they have dropped 6.5 percent for the service industry and slowed for manufacturers.

Members of this Committee are well aware of the integral role that small exporters can play in reversing these trends. Ninety-seven percent of America's small firms are exporters; and, in fact, one-third of all U.S. exports come from entrepreneurs. That means that any dent in American exports become a crater in the small business community.

Why then are exports declining in traditionally entrepreneur-driven industries? A number of factors have come into play, creating what now looks to be a perfect storm. At the heart of that storm are shrinking market stakes. On that front, the U.S. now stands in third place behind Germany and China. It should also be noted that 90 percent of small businesses export to only one country, a fact that has made them far more susceptible to economic volatility and market shifts. But perhaps most troubling is the damage that we have done to ourselves. Sadly, the current administration has failed its own small exporters by underfunding trade-friendly initiatives. In this morning's hearing we will further examine these barriers.

Trade may be on the decline and the economy may be suffering, but just as we used trade to turn the economy around in the '90s, it can serve as a catalyst today. And what better place to begin than with our entrepreneurs? After all, small firms are the backbone of American business. They have steered us out of past recessions, and they can lead the way again today.

I want to thank all the witnesses in advance for their testimony. The Committee is pleased they could join us this morning and looks forward to their insights on these issues.

With that, I now yield to Ranking Member Chabot for his opening statement.

OPENING STATEMENT OF MR. CHABOT

Mr. CHABOT. Thank you, Madam Chairwoman, for holding this important hearing on small business exports.

I would like to welcome our distinguished panel of witnesses and thank them for taking time out of their busy schedules to provide this Committee with their testimony. And we wish you all a good morning and welcome here to the Committee.

One of the most important functions of this Committee is to look for solutions to help entrepreneurs gain access to global markets. Not only do we look for new and innovative ways to help small businesses conduct international trade, but we must also conduct the requisite oversight to ensure our current programs are effectively keeping up with the changing times.

Last year, this Committee worked in unison in order to put together a piece of legislation, H.R. 2992, the SBA Trade Programs Act of 2007, that passed the House with broad bipartisan support. This legislation brings changes in the SBA's operation of its programs to enhance small business participation in the global economy. H.R. 2992 represents the Small Business Committee's continued commitment to promotion of international trade by America's small businesses.

The Small Business Administration has a number of general entrepreneurial assistance programs that provide technical advice to small business owners. However, international trade is an area that is fraught with regulatory hurdles, requiring specialized knowledge that may not be available from the SBA's entrepreneurial partners.

It is not surprising to find that the SBA created other programs to meet the needs of small business exporters that rely on personnel with specialized knowledge about the international trade regulatory regime. These programs, as well as the SBA efforts to coordinate with other agencies such as the Department of Commerce, have enhanced the worldwide profile of many U.S. exporters.

There are about a quarter of a million small businesses in the United States that export. There is no doubt that small businesses are playing a vital role in reducing America's trade deficit. Continuation of this success, and even greater emphasis on small business exporting, will undoubtedly benefit the American economy.

Additionally, this Congress has the opportunity to pass legislation enacting free trade agreements with several of our allied nations, including Colombia, Panama, and South Korea. I remain hopeful that Congress will work together to pass legislation that will implement these pending trade pacts. These agreements should be supported by Congress.

The administration, particularly former U.S. Trade Representative Rob Portman and the current USTR, Susan Schwab, have worked hard over the years to make sure the trade pacts addressed concerns about labor, environmental violations, and intellectual property theft in certain regions of the world. These pacts can also be useful in spurring negotiations for larger trade discussions, such as the Doha trade negotiations. Non-free trade countries may feel compelled to work with other nations to ensure that they are not isolated from the rest of the world.

In the U.S., free trade agreements have enabled local businesses to expand their market base, as well as provided consumers with greater access to different products at more competitive prices. In Ohio, my State, trade has enabled businesses to grow. More than 11,000 companies export goods from my home State to places all across the globe. Eighty-nine percent of those companies can be defined as small- and medium-sized businesses, ones that traditionally and rightly have been called the backbone of the American economy. In addition, one-fifth of all manufacturing workers in Ohio depend on exports for their jobs.

It appears clear to me that exporting is a critical part of building the American economy, especially for small businesses. We have an excellent panel with us today to help us identify some of the obstacles that remain in encouraging trade among small- and medium-sized businesses, and I think that we all look forward to hearing their testimony this morning and asking questions.

So thank you for holding this hearing, Madam Chairwoman. I yield back my time.

Chairwoman VELÁZQUEZ. Thank you, Mr. Chabot.

Now I have the pleasure of introducing Mr. Cass Johnson. Mr. Johnson is the President of the National Council of Textile Organizations. NCTO represents the entire domestic textile industry, including producers, manufacturers, and suppliers of these products.

You will have 5 minutes to make your presentation.

STATEMENT OF MR. CASS JOHNSON, PRESIDENT, NATIONAL COUNCIL OF TEXTILE ORGANIZATIONS

Mr. JOHNSON. Thank you very much, Chairwoman Velázquez and Ranking Member Chabot and distinguished members of the Committee. We look forward to testifying today and outlining the U.S. textile's industry's perspective on the state of small business exports.

As a sector, the textile industry is one of the Nation's most successful exporters. At $16 billion last year, we export one out of every three products we make. However, almost three-quarters of our exports go to the Western Hemisphere. Only one-quarter go to the rest of the world; and that includes the rapidly developing, rapidly growing economies in Asia, particularly China and India. In fact, we send China, a country with a population of 1.4 billion and which consumes more textile apparel products by far than any other country in the world, only $500 million a year in exports.

And China, in fact, looks great compared to India— 1.1 billion population, one of the largest textile apparel consumers in the world—where we send only $55 million a year in textile exports. We send more to the United Arab Emirates each year than we do to India.

Why is this happening? In the macro sense we see, in addition to high duties, we see three major barriers. These are the VAT, currency manipulation, and government subsidies. Of these three, probably the least understood is the VAT, or value-added tax.

The VAT is a tax that averages 15 percent that is levied on exports from the United States to countries with a VAT system, and that is most countries in the world. The problem with the VAT is that U.S. exports are essentially taxed twice. They are taxed at home, companies pay corporate income taxes, and then they are taxed when they go overseas. They get an average 15 percent tax in addition to the duty.

When goods are exported from VAT countries, they get no taxes. These countries rebate the 15 percent tax, and then they are not charged any U.S. corporate income tax. So you have a situation where our goods being exported are taxed twice, and goods coming from VAT countries have all taxes rebated from them. So it is a basic inequity.

It has been estimated that the VAT tax costs U.S. manufacturers $341 billion every year. That is a huge stealth tax that holds back exporting in the United States.

There is an answer to this. It is the Border Tax Equity Act, H.R. 2600, by Congressman Michaud, a member of this Committee. We request that you look carefully at this Act. It is a three-pronged approach to remove the VAT disadvantage from U.S. exporters.

The second barrier is currency manipulation, an issue that we have all heard about. One thing we haven't necessarily heard about is the tax this puts on exports. We all know that China can—we import a lot more from China because of manipulation of currency. The flip side of that equation is we can't export nearly as much to China because of the currency manipulation. It places the same 25 to 40 percent tax on exports as the advantage it gives to imports from China.

There is an answer to this problem. It is H.R. 2942, the Currency Reform for Fair Trade Act, co-sponsored by Tim Ryan and which has been supported by many members of this Committee. If Congress would pass this Act, it would send a strong signal, the most powerful we can imagine, that China needs to float its currency.

The third major problem are subsidies, particularly in China, India, and Vietnam. In a recent textile case, the government found that China offered its textile industry 24 different subsidies in order to export products cheaper to the United States, and they assigned countervailing duties of 27 to 359 percent. Most medium-sized—small- and medium-sized companies cannot afford to file CBD cases. They start at a million dollars apiece. The government needs to do more, and we suggest that Congress needs to send a strong signal that the government needs to do more.

NCTO sent to USTR a list of 63 subsidies that China offers it its textile industry. We sent that over a year ago. We are still waiting for a response. We know many of these subsidies are WTO illegal and should be the genesis of a case against China, but we have been told by USTR that they simply do not have the resources right now to go after these 63 subsidies.

We believe that Congress should change USTR's focus for the next 5 years from negotiating new agreements to reviewing and enforcing existing agreements. USTR's resources should be reoriented towards verifying China and others live up to the agreements they have signed; and, if they are not, they should file cases against them at the WTO.

With these steps, we believe we can usher in a new renaissance for the U.S. manufacturing sector and its workers, and we thank the Committee very much for looking at this very important issue.

[The prepared statement of Mr. Johnson may be found in the Appendix on page 32.]

Chairwoman VELÁZQUEZ. Thank you, Mr. Johnson.

Our next witness is Mr. Jameson French. Mr. French is the President of Northland Forest Products, which is a family run business selling hardwood products located in Kingston, New Hampshire. He also serves as Chair of the Board of Directors for the Hardwood Federation, which is an industry trade association that represents over 14,000 businesses, 30 trade associations, and over one million hardwood families. Welcome.

STATEMENT OF MR. JAMESON FRENCH, PRESIDENT, NORTHLAND FOREST PRODUCTS, KINGSTON, NEW HAMPSHIRE, ON BEHALF OF THE HARDWOOD FEDERATION

Mr. FRENCH. Thank you. Thank you very much, Madam Chairman and the Committee. I appreciate the opportunity to be here today. And thanks for the introduction. It saves me a few seconds of my time.

I would note that I am proud to be a fourth-generation member of the hardwood lumber industry. And we have a fifth generation coming along, but they are wondering whether it is going to be worth it because of the difficulties that our industry is facing, particularly—in all parts of the country, but in New England, where we saw the demise of the textile and shoe and the computer hardware businesses. And we wonder whether the forest products industry will be the next one to fall.

As you noted, the Hardwood Federation, 14,000 businesses around the country, small family businesses, key strong parts of the world's economy in many of the Eastern States. We actually have members in all 50 States, but the bulk of the forest resource, of course, is east of the Mississippi. We are a major exporter. About almost $3 billion worth of hardwood forest products are sent around the world, hardwood lumber, plywood, flooring, pallets, kitchen cabinets, all these types of products.

These are tough times for our industry, as you can imagine, with the housing crisis and all of the domestic economy recession. It has been a great challenge. And the export side of the business has been one of the most important sort of lifelines for people in a very difficult domestic economy.

You will see in my written testimony the key products that we export and the countries that we send them around the world. Of course, Asia has become very significant. Europe has the highest values.

Our industry represents a lot of very independent people in rural parts of this country. And we tend to be libertarian, and we tend to be very free trade people. But we are really concerned about the lack of a level playing field, and we want fair trade and a chance to compete in the global marketplaces.

There are three specific areas of concern, all of which are in my written testimony: the increase in fees from APHIS, the freight and shipping charges, and the foreign procurement policies, which particularly in Europe and Japan may require some documentation and some issues that involve legality and sustainability that may be very difficult for our members to comply with.

I won't spend much time at all on the fee issue. It is a relatively small thing. It doesn't sound like a lot, but you can imagine if you aren't making any money, to have a doubling of your export certificate fees could make a big difference.

The shipping problem is a huge one. The sudden rate increases that have occurred, doubling some of our container charges around the world in the last 6 months, has killed many of us. It is a huge problem if you have advance contracts, say, to China where you have sold many loads forward at a fixed price, and suddenly the rate goes up by 50 percent or more, and there is no containers.

And we are very concerned that the business practices of many of these foreign-owned shipping lines are dubious; and we would urge this Committee to investigate this area. Because we feel we have been unfairly penalized as to our low-value products, that they have substituted the higher-value products and left us hanging dry. It has been a big problem.

The procurement issue is quite complicated and hard to explain in a short bit of time, but I want you to know that we take this issue very, very seriously.

We have a wonderful, sustainable resource in this country. The eastern hardwood forest is the woodbasket of the world, and we are very concerned about illegal logging in foreign countries like Indonesia and Russia, and we are very appreciative of the support that has happened with this amendment to the Lacey Act, which we strongly supported with the environmental organizations. But there are some concerns that the European countries and others are going to force us to have more documentation about the sustainable or certification of our forest resource. This is very difficult for people, with 90 percent of all the land that's owned in this country in the forest is by small private landowners.

In my little State of New Hampshire, we have 22,000 people that own 25 acres or more. So it is very difficult for the chain of custody and the procurement policy to certify these kinds of lands, and it is a very diverse and fragmented industry. And the paperwork and the necessary costs to ensure legality and sustainability would be a great challenge.

We have a great story to tell. The U.S. Forest Service tells us we have 50 percent more growing than is being cut in the last 50 years, that we have independent studies showing our risk assessment is very low and that legality is very high. So we would really love to have some support around this issue to make sure that we do not face unfair and uncompetitive disadvantages abroad around this thing.

So we thank you for your interest. We want fair, level playing field trade. We are very grateful for the support of the American Hardwood Export Council funding for the FAS market promotion fund. This is an area that has been very well supported and funded, and we are grateful for that.

We thank you for your time. Thank you.

Chairwoman VELÁZQUEZ. Thank you, Mr. French.

[The prepared statement of Mr. French may be found in the Appendix on page 38.]

Chairwoman VELÁZQUEZ. Thank you, Mr. French.

Our next witness is Mr. Chuck Wetherington. Mr. Wetherington is the President and owner of BTE Technologies, located in Hanover, Maryland, which produces work simulation and physical therapy equipment. He is also a board member of the National Association of Manufacturers, representing small- and medium-sized manufacturers. Welcome.

STATEMENT OF MR. CHUCK WETHERINGTON, PRESIDENT AND OWNER, BTE TECHNOLOGIES, HANOVER, MARYLAND, ON BEHALF OF THE NATIONAL ASSOCIATION OF MANUFACTURERS

Mr. WETHERINGTON. Thank you. Good morning, Madam Chairman and members of the Committee.

I am Chuck Wetherington, as you said, President and an owner of BTE Technologies, a small company headquartered in Hanover, Maryland. We have offices in Denver, Colorado, as well.

I have prepared a statement for the record and will make my remarks brief at this time.

At BTE, we have 78 employees and produce a range of medical devices focused on physical therapy, industrial rehabilitation, and sports medicine. In 2001, we made a decision to place greater focus on exports. We have the good fortune of being in a product space where U.S.-flagged goods are held in very high esteem in the world marketplace.

I am happy to say that since 2002 our exports have grown tenfold, from 3 percent of our revenues to now 35 percent. We currently export to 28 countries in the world.

Exports, obviously, have been a key part of our company's strategy and success. So how important is small business to U.S. exports? Of U.S. companies that export, over 97 percent of them are small- and mid-sized businesses. Yet those companies only represent 30 percent of the total dollar value of all U.S. exports. This is because two-thirds of all smaller exporters sell to just one country, and two-thirds have fewer than five export sales per year. We have a lot of room to grow, and with the right conditions U.S. small companies can flourish in the global marketplace.

Today, I would like to mention four things that are critical for U.S. companies, especially small companies, to be able to successfully export.

First, we need currencies that reflect market values. When the dollar is excessively strong against other currencies, U.S. goods become expensive in global markets and exports decline. When the dollar has adjusted to a more realistic value, exports grow. Of course, this sounds like common sense, but it is a fact that is too often overlooked.

We have just seen this play itself out in the past decade. As the dollar came off its 2002 high, our exports have grown dramatically. NAM hears every day from companies who say the value of the dollar has allowed them to be internationally competitive again. Many companies, particularly small- and mid-size, say the primary reason they are doing well is their export performance, which has offset softening domestic demand.

Second, we need free trade agreements that open markets for U.S. goods. I recognize that there are concerns about our free trade agreements, but I must say, from the perspective of a small business trying to export, they have been very important to us. The United States is already open to the world. Much of the rest of the world has a higher tariff and non-tariff barriers to U.S. exports. We need these agreements to open foreign markets for our goods.

Third, it is very important that we see the removal of standards and regulatory barriers, one of those non-tariff barriers I spoke of, for the sale of U.S. goods in foreign markets. This is one of the big hurdles we face at BTE.

A good example is the medical device directive in the European Union. One would think that the EU would be about the easiest place after Canada and Mexico for the U.S. company to export, and in many ways it is. But this directive has made it very expensive and very difficult and time-consuming for us to be certified. We are seeing signs that others are starting to follow the EU's lead.

The government could help by working to develop some level of standardization. This might include negotiating global standards, or at least reaching agreements for reciprocity between certifying agencies. Multiple standards greatly increase the costs of production and the costs of bringing new products to market, and this would be especially helpful for small companies.

The fourth priority is the U.S. Government export assistance. At BTE, we have found a range of services provided by the U.S. Commercial Service to be instrumental in our success. We worked with the Baltimore Export Assistance Center to help us find distributors overseas, conduct background checks on potential customers and agents and do country analysis, identifying markets for our products.

I have to add at this point that this has also been a marvelous place for us to see State associations working with Federal associations through the Maryland Department of Business and Economic Development. Working hand in hand with Commercial Services, we have been able to get the best possible solutions for our needs.

For small companies, these services are essential to success in exporting. Most of us don't have the resources to have large export divisions or offices overseas to ferret out new business. One problem is the increasing shifting of costs of these promotion programs back to the U.S. businesses. This is in contrast to the support that other governments provide to their exporters.

Some of these countries pay up to 70 percent for their companies to attend trade shows. In BTE's experience, we have spent over $100,000 in just the last 4 years just to attend MEDICA, the annual trade show that covers our field.

The Australian Government, for example, recently announced that grants for economic export development would be boosted to $200 million. By contrast, the comparable U.S. program is funded at $2 million, although we have significantly more small companies that could benefit.

Another important export service is export financing. My company has taken advantage of small business services at EX-IM Bank, and it has made a significant difference in the number of our recent sales. I strongly encourage you to continue support for these import financing opportunities for small companies.

In conclusion, I would like to thank you and the members of the Subcommittee for this opportunity to testify on such an important issue. We are in a globalized world, and our small businesses need to be in a position to avail ourselves of global opportunities in order to improve the standard of living of all Americans. Certainly a determined export promotion effort, focusing on increased participation of America's small- and mid-sized companies in world markets should be an important endeavor. My prepared statement contains more specific suggestions.

Thank you, Madam Chairman.

[The prepared statement of Mr. Wetherington may be found in the Appendix on page 46.]

Chairwoman VELÁZQUEZ. Thank you, Mr. Wetherington.

Our next witness is Mr. Daniel T. Griswold. He is the Director of the Center for Trade Policy Studies for the Cato Institute. He has authored or co-authored studies in globalization, trade, and immigration.

STATEMENT OF MR. DANIEL T. GRISWOLD, DIRECTOR OF THE CENTER FOR TRADE POLICY STUDIES, THE CATO INSTITUTE

Mr. GRISWOLD. Chairwoman Velázquez, Ranking Member Chabot, thank you for inviting to testify here today.

Globalization is a fact of life in 21st century America, and our nation's small businesses should be allowed to take full advantage of the opportunities. Since 1990, exports have grown sharply as a share of the U.S. economy. Three-quarters of the world's spending power and 96 percent of the world's people live outside the United States. This represents a huge potential market for American business.

Our growing engagement in the global economy is one of the bright spots of the U.S. economy today, and we definitely need bright spots. Exports and earnings on foreign investment are booming. Exports of goods and services jumped by 12.6 percent last year from the year before, and earnings on U.S. investment abroad jumped 20 percent. That expanding opportunity to serve foreign markets has allowed U.S. companies, including small businesses, to better weather the current economic slowdown.

One of the most important and fastest-growing markets for U.S. companies, including small businesses, is China. Last year, Americans exported $65 billion worth of goods to China. China is our number three export market behind only our NAFTA partners Canada and Mexico. Since China's entry into the WTO in 2001, U.S. goods exports to China have grown at a compound rate of 22 percent. That is three times faster than our exports to the rest of the world, despite complaints about their currency.

Small- and medium-sized U.S. businesses are basking in this export success. Nearly 20,000 small- and medium-sized U.S. companies account for 35 percent of U.S. merchandise exports to China. If Congress enacts legislation that ignites a trade war with China, small businesses will be among the first casualties.

Far from a time out, Congress should work with this administration and the next to approve comprehensive trade agreements to abolish barriers and promote two-way foreign investment. Such agreements benefit U.S. small businesses in three particular ways.

First, trade agreements help to reduce red tape and increase transparency. Small businesses often lack the resources and the foreign partners abroad to navigate through the opaque legal systems and customs duties of foreign countries. Numerous fees and other non-tariff barriers can be deal-breakers for small companies.

Trade agreements streamline rules, reduce non-tariff barriers, and provide arbitration procedures.

Second, trade agreements open up opportunities for U.S. small businesses to compete for procurement contracts with foreign governments. And this is a huge market. Trade agreements guarantee U.S. companies a fair shake at the important government procurement market. They also lower thresholds so businesses, small businesses, can submit bids.

Third, trade agreements lower tariffs and other barriers to trade that are more difficult for small businesses to work around. You know, large multinationals can circumvent tariffs by locating production in affiliates abroad. Small U.S. companies don't have that option. Many of them export from a single domestic location here in the United States. The reduction and elimination of tariffs allows them to export from their domestic facilities without facing barriers that could be discriminatory and prohibitive.

The 110th Congress has the opportunity right now to enact three trade agreements with Colombia, Panama, and South Korea that will help small U.S. companies boost their exports. All three of these agreements would reduce barriers and eliminate tariffs while guaranteeing fair treatment for U.S. companies that invest abroad. They would streamline those customs procedures, enhance transparency, and open up government procurement for small U.S. businesses; and these agreements would allow thousands of U.S. small companies to export to these markets for the first time.

For example, nearly 8,000 small- and medium-sized U.S. companies already export to Colombia, accounting for more than one-third of our exports to that country. The Colombia agreement would eliminate the large majority of tariffs on those product. Their goods already enter the United States duty free because of the Andean Trade Preference Act. This would give us the level playing field that we all say we want. According to the U.S. International Trade Commission, the agreement would boost U.S. exports to Colombia by more than a billion dollars, with small businesses ready to claim a big slice of that expanding pie.

U.S. companies do not need Federal subsidies to compete effectively in global markets. We have a lot of advantages in this country. Those markets are currently awash in private capital, ready to finance new trade and investment opportunities. Congress and the administration, if they want to increase opportunities for U.S. small business, they need to work together to reduce barriers to international trade and investment, whether abroad or here in the United States.

Thank you very much.

[The prepared statement of Mr. Griswold may be found in the Appendix on page 56.]

Chairwoman VELÁZQUEZ. Thank you, Mr. Griswold.

And our next witness is Dr. Aaron K. Chatterji. Dr. Chatterji is an Assistant Professor at the Fuqua School of Business at Duke University and a Fellow at the Center for American Progress. His research focuses on innovation policy, entrepreneurship and small business issues, and corporate social responsibility. Welcome.

STATEMENT OF DR. AARON K. CHATTERJI, ASSISTANT PROFESSOR, THE FUQUA SCHOOL OF BUSINESS, DUKE UNIVERSITY, DURHAM, NORTH CAROLINA

Dr. CHATTERJI. Thank you very much.

Madam Chairwoman, members of the Committee, thank you for inviting me to testify on this important economic policy issue, one that, with the exception of the good work of this Committee, often does not receive the attention that it deserves.

In my view, American small businesses are not just the backbone of our economy. They are also the linchpin of our society. In the places I have lived across this country—upstate New York, where I was born and raised; northern California, where I did my graduate studies; and now the research triangle in North Carolina—I have seen that small businesses are one of the most are important variables affecting the overall economic health in a region. I have also observed that many immigrants to this country, like my parents, have started small businesses as a way to provide for their children. Finally, I have studied how global economic forces have changed the competitive landscape, yes, providing new threats to small businesses but also new opportunities.

However, in the current policy debates, American small businesses are often an afterthought. Some recommendations seem to be driven by the assumption that what is good for the Fortune 100 is obviously just going to trickle down to small businesses. I think the real story is a little bit more complicated than that, frankly.

I think Federal, State, and local governments have numerous tools at their disposal to help small businesses, especially in the current economic environment. At the end of the day, it will be the widely admired entrepreneurial initiative for the American people and their entrepreneurs that drives success, but the government can actually help to harness that initiative rather than hinder it. I think this is the difficult challenge of public policy that we face today.

In that spirit, let me offer a few thoughts on some of the issues being discussed today, in particular the export outlook for American small business.

While there are many reasons to be concerned about the future of the American economy—rising energy costs, the turmoil in the mortgage markets, and the increase in the unemployment rates—until recently American exports were one bright spot. They increased 16.6 percent from last year, although the chairwoman's new data suggests this year might not look as good. When we look beyond the data, we might be concerned that the majority of American businesses, namely small businesses, are not benefiting as much as they could be from what was a favorable climate for exports until recently.

According to the Small Business Export Association, 240,000 of our small businesses are exporting, accounting for $450 billion in value. That sounds like a big number, but these businesses only represent a small fraction of small businesses, less than 1 percent in most cases. Furthermore, over 60 percent, as mentioned in the chairwoman's opening statement, are only exporting to one country, which makes it much more volatile if local conditions in that country decline.

Also, as prefaced by the other remarks, most of these exports are also regionalized in the NAFTA countries, particularly Canada and Mexico. We have a lot of opportunities in China and India that are not being exploited.

When you had look at the ratio of exports coming from small businesses, it amount to about 29 percent of total value. I think that is an important number we need to keep in mind. It is not necessarily the number of small businesses exporting, it is the percentage of value that matters a lot as well. That percentage of 29 percent has stayed pretty constant over the last few years. I think there is a lot of room for growth.

On the other hand, during the same time we have seen double-digit increases in the overall value of exports, 1.4 trillion to 1.6 trillion last year, an increase of 12 percent. That is on top of another increase of 12 percent the year before. So as exports have been going up, small business's share has stayed pretty much the same.

I think that is where the focus of this Committee can lie. So while we hear some encouraging statistics here about the percentage of exports for small business, I encourage you to focus on percentage of total value.

I also think we need to look at those industries which are dominated by small businesses for special study. Ninety-four percent of machinery manufacturers are small businesses. Ninety-three percent of computer producers are small businesses. We have some disturbing data showing that exports in some of these industries are actually going down in 2008, in addition to lumber and textiles. These are the industries we need to be focusing on, where the majority are small businesses.

Now, I should caution you that there are several caveats and exceptions embedded in these data. But taken together with the current economic climate, they indicate, in my view, that we should consider policies to aid U.S. small businesses in accessing foreign markets. They clearly need the help, and there is potential for growth. So let me briefly conclude by describing a few of the challenges faced by small business and where I see some potential policy responses.

The first challenge is a general lack of awareness on the part of small business about the opportunities to do business abroad. You think about a multi-tasking entrepreneur who barely has time to run their own business and manage family affairs, much less think about entering a foreign market. We need more information for these small business owners and particularly the information about these tremendous opportunities abroad in China and India.

Large markets here like China and India have increasingly large aircraft markets, for example; and the U.S. machine tool industry could supply these markets. The fact of the matter is small businesses in developing countries are not technologically sophisticated enough to source the large businesses in their domestic regions. This is a huge opportunity for U.S. domestic producers if they can seize it.

Trade promotion at all levels of government needs to be consolidated and better coordinated and provide practical and clear information about foreign markets and foreign cultures as well. Let's not make missteps by not understanding foreign cultures when we are doing this.

Many people have said this, but I want to add one more thing. Entrepreneurship is a very social process. Most entrepreneurs founded firms based upon people they knew, raising money from friends and family. We need to leverage their social networks to get the word out about how to access foreign markets. Immigrant entrepreneurs have already established strong ties with their home countries that we can use to access foreign markets. These things need to be considered, the social network aspect of entrepreneurship, when we think about policy.

Finally, I think, while advances in technology have made communication easier, nothing replaces face-to-face contacts. It is just simply so expensive for small businesses to do the due diligence required to appraise foreign partners. The Gold Key Program by the U.S. Export Assistance Program is one good one; and, as the ranking member mentioned, I think it is a good idea to continuously evaluate these programs and see whether they continue to improve.

Finally, I will make a personal appeal, but it actually has broader implications. I think we need better data on small business. So much of the data here today that I was looking at in preparing for this testimony does not include very critical parts of the story. Service exports in particular might be as large as 40 percent of the overall picture, and are not included in the data. So I would like to see more of that data collected, and maybe this Committee can help on that account as well.

In conclusion, I think we all agree U.S. small businesses are a critical part of the economy. The question is how to harness that entrepreneurial initiative going forward. I think some of the policies suggested here today are a step in that direction.

I want to thank you for your time, and I look forward to your questions.

[The prepared statement of Dr. Chatterji may be found in the Appendix on page 61.]

Chairwoman VELÁZQUEZ. Thank you, Dr. Chatterji.

I would like to address my first question to Mr. Johnson.

In your testimony, you note that many countries pegged their own currency to ours, which effectively neutralizes any price advantage from a devalued dollar. Do you believe the U.S. should prompt these countries to cease manipulating their currency, or are there other alternatives you would recommend to promote U.S. exports?

Mr. JOHNSON. Well, I think this is probably the largest export barrier to goods coming from Asia. The problem is not just China. It is a mercantilist export regime that have been set up for decades in the Far East by countries—not only China—Taiwan, Korea, Japan, Indonesia, India, Pakistan. Many of the export powerhouses have manipulated and controlled their currencies in order to get an export advantage; and until we get that under control, we are simply not going to be able to export and take advantage of these rapidly growing markets like we should.

I think Alan Greenspan and Federal Chairman Bernanke have both said this is an export subsidy. H.R. 2442, the Ryan-Hunter

Act, will allow injured U.S. companies to file countervailing duty cases against countries that manipulate their currency. It is an export subsidy. We should have the tools to defend ourselves from it. I think if we get those tools it will encourage those countries, because the U.S. market is still the biggest market in the world, to allow their currencies to float and to allow free markets to finally prevail.

Chairwoman VELÁZQUEZ. You don't think we have tools at our disposal at this time that the U.S. Government can use to pressure those countries in terms of the manipulation of their currency?

Mr. JOHNSON. Absolutely not. I mean, the U.S. Government can and should file a WTO case, because this is an illegal subsidy. The Bush administration has refused.

Chairwoman VELÁZQUEZ. How many has this administration filed?

Mr. JOHNSON. I think it has been filed three times by Members of Congress as well. And after the first filing, we would be at the decision point at the WTO right now if that case had gone through, because I think it has been 3 years. So—

Chairwoman VELÁZQUEZ. Thank you, Mr. Johnson.

I am going to recognize Mr. Chabot, and then when we finish with our members here, I will come back and make a question to the other witnesses.

Mr. CHABOT. Thank you very much, Madam Chair.

Just following up on the same general area—and I will begin with you also, Mr. Johnson—what can we do, especially with respect to China and India, to help our corporations be more successful in exporting there? And other than the currency manipulation, because we have discussed that at some length.

Mr. JOHNSON. Well, I would add that looking at the VAT issue—and that is a very big issue to look at, but it has a very big impact. I mean, it is double taxation of U.S. exports. And how we get around that, there is one piece of legislation that I think people should seriously review, because it proposes some ways to do that.

The other issue that we point out is this problem of government subsidies. And I note with interest that Mr. Griswold in his testimony writes that—I thought I had it right here—writes, says, big headline, no export subsidies, no trade barriers. And he is talking about should the United States offer subsidies to its companies to allow them to export more and should the United States impose countervailing duties?

Well, I think where the argument fails is that he is not saying we should go after China. China has more export subsidies than any other country in the world. We have identified 63 just for the textile industry. And yet there is no suggestion on the other side of the table that these are harmful or prevent U.S. exporters from participating in these export markets.

We have a five-to-one trade disadvantage with China. China exports over $300 billion to us; we export 50, $60 billion to them. That is the most rapidly growing, largest, fastest-growing economy in the world. We should be exporting double or triple that much, but we can't when the Government of China layers subsidy after subsidy after subsidy onto its domestic manufacturers and makes it almost impossible for us to compete, particularly on the manufactured goods side.

So I think USTR needs to beef up its resources. The United States needs to look into these sector-specific subsidies, file WTO cases. Under the WTO, if a sector is benefiting from subsidies and damaging another sector overseas, a WTO case can be brought that that sector should remove the subsidies.

Mr. CHABOT. Okay. Let me go to my next question.

Mr. Griswold, let me go to you. Do you want to respond?

Mr. GRISWOLD. Yes. I have no doubt that China, as well as a lot of other governments around the world, as well as our own government, subsidizes domestic production; and I would like governments everywhere to stop doing that. I think the free enterprise system, the free market should determine trade flows. But just because other countries engage in self-damaging practices doesn't mean we should follow suit.

Let me talk a little bit about the currency. I think this excuse is rapidly dissipating. You know, the Chinese currency has appreciated by 20 percent within the last 2 years. That appreciation has been accelerating.

I think the textile industry appears to be an outlier among U.S. industry. As I pointed out, U.S. goods exports to China, manufactured goods, agricultural goods have been growing at a compound rate of 22 percent since China joined the WTO. That is three times faster than our exports to the rest of the world. So, clearly, a lot of U.S. companies of all sizes are enjoying a lot of success exporting to China.

I don't think we should step in and mess up that very beneficial relationship. I think legislation like the Ryan-Hunter bill would just raise barriers to trade and jeopardize those export gains that small businesses have made to China and elsewhere.

Mr. CHABOT. Okay. Thank you.

Mr. French, you had mentioned that one of the things that you are dealing with that is causing real problems in your industry is the high cost of energy, which is obviously affecting people at the gas pump, and diesel has gone out of sight, et cetera. And I think you mentioned that some of the containers in 6 months it will double. And what does one do about that? Would you talk about that briefly, how that does affect your industry?

Mr. FRENCH. It has been a huge impact. Of course, the lower-value products are more dramatically impacted by the percentage increase. So think of a relatively—and one of the issues with China that we have is a lot of the products that are going over there are the lower value end of the lumber products, because the Chinese want to buy the cheapest wood they possibly can to make into the cheapest furniture. That, of course, is putting the American furniture industry out of business.

But what has happened with these freight increases is that they have come very, very rapidly. And, yes, of course we know fuel prices have gone up, but they haven't gone up 100 percent in 6 months. And the global trade patterns, we have a relatively low-priced product. The fees have been relatively low over time. And several years ago, of course, they loved us. The freight lines wanted this bulk cargo because all of the imported goods were coming in from Asia, and there were lots of empty containers here, and they were delighted to take grain or wastepaper or logs or lumber back to Asia.

Those trade patterns have changed. There is less goods coming in because of the recession in the U.S. economy. And the shipping companies pretty arbitrarily suddenly decided, well, we don't want any of these low-market products. We have guys that are small family businesses, they don't have the sophistication of negotiating big deals with freight companies. They may be only shipping five or six or ten loads a month. And suddenly they have contracts that are forward at fixed prices, and they have a 500 or a 700 or a thousand dollar increase in a container with a value of only $20,000 on the container. That may be their entire profit. So it has been very arbitrary and random, and you know, no notice. It has been a huge impact on my own business.

Mr. CHABOT. Let me ask you this. In relation to energy—and I would like to ask the whole panel this question—obviously, you know, many of us believe that we need a comprehensive energy policy that we really follow through on that deals with alternative sources of energy and all the rest. But it has been Congress' policy not to allow us to go after the oil that is in ANWR and the Outer Continental Shelf for quite a few years now. Many of us have voted consistently for it. We haven't had the opportunity to vote in this Congress yet on that issue. I hope we do in the future. But do any of you all think that it is a good idea for small businesses or medium or large businesses in this country to keep ANWR and the Outer Continental Shelf off limits?

Chairwoman VELÁZQUEZ. Would the gentleman yield before—

Mr. CHABOT. Well, let me see if there is a show of hands.

Mr. FRENCH. I would be happy to respond. I think it is a very short-term solution, and it is not necessarily good environmental policy.

Mr. CHABOT. To keep it off limits, you mean?

Mr. FRENCH. We need to invest in alternative energy. And as wood energy looks at cellulosic ethanol, biomass and other types of things, it may be a savior for the hardwood lumber industry for some serious Federal investment in alternative energy, particularly utilization of wood.

Mr. CHABOT. Again, could I see by a show of hands if anybody here thinks that we ought to continue to keep ANWR and the Outer Continental Shelf off limits? Does anybody think we should?

Mr. FRENCH. Okay. I do.

Mr. CHABOT. You do. Two of you.

Mr. FRENCH. I think we need to be very guarded, whatever we do. And we made a commitment on ANWR. And it is a short-term, band-aid solution. It's not a long-term solution to our energy problems.

Mr. CHABOT. I can tell you that the two of you are not representative of the business folks, especially small business folks that have talked to me.

Mr. FRENCH. I am not speaking for my industry now. I am speaking as an individual—

Mr. CHABOT. For yourself. Okay.

Mr. FRENCH. —from the State of New Hampshire.

Mr. CHABOT. I would be happy to yield to the gentlelady.

Chairwoman VELÁZQUEZ. Let me just say I want the record to reflect it seems that ANWR is the answer for everything now, and next the gentleman will say that because we have not drilled in ANWR is the reason the Mets fired Mr. Willie Randolph.

Thank you for yielding.

Mr. CHABOT. One never knows. I haven't been able to make that point in the past, but I appreciate the gentlelady making that.

Chairwoman VELÁZQUEZ. And I am a Mets fan.

Mr. CHABOT. I am a Cincinnati Reds fan. I have some more questions, but I will yield back to allow some other panel members to ask their questions.

Chairwoman VELÁZQUEZ. Sure. Mr. Larsen.

Mr. LARSEN. Thank you, Madam Chair, for calling this hearing; and I appreciate the testimony.

Just a quick commercial for H.R. 3273, which is the Small and Medium-Sized Export Act of 2008 that several of us have introduced to increase our government's capacity to help small- and medium-sized exports to China. As I tell folks, whether you love China or hate China, you will love this bill, because this is designed to get our stuff into that market, not the other way around. So people can have any view they want on currency or subsidies from China and still support H.R. 3273. So I throw that in.

I am also pleased to hear that this hearing is more than just about currency manipulation versus free trade agreements, because it is hardly the debate we ought to be having. And but what I didn't hear more of is the idea of a competitiveness policy and what elements that would take. And, Dr. Chatterji, I would ask if you would have some thoughts on what it would take to maintain a foundation of competitiveness in this country. Because I think what some folks do in Congress or push in Congress on trade—and I generally have been supportive of trade agreements—have been a trade policy, but it is nowhere near a policy to keep us competitive.

Can you chat a little bit about that, Dr. Chatterji?

Dr. CHATTERJI. Thank you.

I think it is an excellent question and a point well taken that we have these conversations in isolation when we should probably be thinking about a competitiveness policy that includes trade, that includes workforce development, and also includes immigration, quite frankly, one of the most contentious issues, and particularly high-skilled immigration.

Around the world, several countries have programs based on a points basis so they can bring in high-skilled immigrants for specific jobs. That has been discussed. Bringing in people with specific skills is clearly important.

Also, the people we have here on H-1B visas. Why shouldn't we be stapling a visa to their diplomas when they do a Ph.D. in an advanced engineering subject?

Currently, more than 50 percent of engineering graduates, Ph.D. students, are from foreign countries. And increasingly I have seen at Duke University, in contrast in a generation ago, when my parents came here, the Indian students now are saying we are going to go back to India. We can have a better life in Bangalore than we can here in Durham. To me, that is sort of a tragedy of our immigration system today. They find it to be better going back to India than staying here, when they could be producing and contributing to our economy.

In addition, we can't forget about investing in the folks who are already here; and science and math education has got to be part of that. American students are lagging behind in those areas.

I think there is a lot of scare tactics talking about engineering graduates from China and India. Yeah, there is about a million a year in each place, but it is very variable in terms of the skills they actually have.

That being said, it is better to sort of be on our guard, even if the threat is not as large. I think we have to take this more seriously, especially among minority students, who are lagging behind in these areas.

Now, what is that going to take? It is going to take a strong commitment not just in sort of secondary education but all the way back to primary education. I don't think American students are challenged enough in the math and sciences at an early age, and it is going to take sort of a reformulation of the way we think about education. That would be the second part of it. So high-skilled immigration is one area, education and workforce development would be the other.

The last one is retraining programs. I think we talk a lot about it, but I am not sure if we are evaluating it the way we should. When someone loses their job in the textile industry, for example, in our State of North Carolina, you know, can they be retrained to do something in that industry or in another industry? What kind of guidance are they being given?

You know, we have a good experience in some aspects in North Carolina taking low-end textiles and actually moving up to the higher end; and we have been quite successful in that. How can we retrain folks who used to work at the old textile mill to work in the new one? That is a key issue. I don't think enough attention is being put into those. And your point is well taken, if we can think about those components along with trade policy we might end up with something better.

Mr. LARSEN. Mr. French, a question for you. Have you approached or talked to anybody at the Federal Maritime Commission regarding the ocean freight charges issue?

Mr. FRENCH. We haven't as a federation at the moment.

Mr. LARSEN. Are you planning on that?

Mr. FRENCH. I think it is something we need to do.

Mr. LARSEN. We have them before the Coast Guard Committee at 2 o'clock, if you are around this afternoon. I am sure they would love to hear from you. I am sure they wouldn't love to hear from you, but we can probably help them hear from you.

Just a last general question for the members, if anyone else wants to weigh in on my first question that Dr. Chatterji responded to. Mr. Griswold?

Mr. GRISWOLD. Congressman, I do think that is a very good point, that free trade, as important as it is, is not a magic bullet and it is not the single answer. We need to have as good a domestic business climate as possible; and that includes reasonable regulations, reasonable taxation.

And I just want to echo what my friend to my left here says about a skilled workforce, and I do think Congress should reexamine the H-1B program. This is important to small business. It just isn't a Fortune 500 issue. This is important to small business.

There was a study at Duke University a year or two ago that found that a quarter of U.S. high-tech and engineering start-up companies had a foreign-born person as a co-founder. If you want to encourage not just small business entrepreneurism generally but the high-tech, innovative kind, we need to reform our visa programs; and these companies often have connections abroad that encourage some of our highest-value exports to the rest of the world. So it is a package. You make a very good point.

Mr. LARSEN. Thank you.

Let's go to Mr. Wetherington and Mr. Johnson.

Mr. WETHERINGTON. Yes, I am a supporter of assistance to help with exports to China. I think it is a marvelous program. I have been a beneficiary, as I said, of those programs in a number of countries.

At the risk of throwing another log on the fire, though, the one fear that I do have that keeps me up at night, having a high-technology product, is that of intellectual property. Fortunately, my sales to China now are below the radar screen. My fear is that, with success, I would get to a point where it would become a point of interest; and it is very, very difficult for a small company to be able to deal with that and stay innovative enough to be ahead of the copying.

Mr. LARSEN. Thanks.

Mr. Johnson?

Mr. JOHNSON. Our members, the concerns they most raise are the price of energy, health care, and also taxation. If you are going to have a competitiveness policy, I suggest looking at those.

But I don't think you can ignore in a competitiveness policy the fact that the biggest exporters in the world have erected large industrial policies that make their goods—make it difficult for us to compete against their goods. And you can either raise barriers to those goods, you can subsidize the United States industry, which I don't think our country wants to do, or you can go after those subsidies. And until you start going after those subsidies, which are very often WTO illegal, and can be gone after, you are going to have our companies competing against State governments. And we can compete against the Chinese textile mills, but what we cannot compete against is the Government of China, and that is what is being set up for us.

The textile industry in China has now been gifted with its 11th 5-year plan for the textile industry by the Chinese Government. There are no plans for the textile industry in the United States, and we don't want them. But we do want a fair playing field, where the U.S. Government starts going after these 63 subsidies the Chinese Government is offering its domestic manufacturers.

Mr. LARSEN. I am sorry. I am out of time. So out of respect for the chairwoman I want to thank the chairwoman.

Folks, where I come from, Washington State, you know, we actually have a trade surplus with China. So it kind of depends where you sit sometimes in this country as well about how you approach these things.

Chairwoman VELÁZQUEZ. Mr. French.

Mr. LARSEN. Thank you.

Mr. FRENCH. Thank you.

I would just like to add a little bit on the complexity of the wood industry's relationship with China. Because, of course, they are a very, very important and large customer, but they are also a huge competitor, because of all of the products that they are making, some from our wood and some from other woods around the world.

Of course, some of that is illegally felled from places like Papua, New Guinea, and Indonesia and the Russian far east; and they have all of the subsidies that have been talked about in their factories. They have these products that are coming in from these dubious sources, and then they are selling their manufactured products to our potential customers in other parts of the world. So the stair part that might have used to have been made in the U.S. that was going to be shipped to Europe at a very high value ends up being made in China from perhaps illegally felled Russian logs, you know, in a factory of dubious environmental regulations, and shipped to Europe. And it puts us out of business in that marketplace. So it is very complicated.

Thank you, Madam Chairman.

Mr. LARSEN. Thank you, Madam Chair.

Chairwoman VELÁZQUEZ. Mr. Shuler.

Mr. SHULER. Thank you, Madam Chair.

Dr. Chatterji, you know, what provisions have we—you know, looking at future trade policies and agreements, what agreements should we be having to ensure that small businesses take advantage of the overseas markets?

Dr. CHATTERJI. It is a difficult policy question. I think that there is two things.

One is, despite all the fluctuations with currency, I don't think we can ever count on U.S. goods being the low-cost product in the market. I think we need to continue to focus on adding value to the products we provide. I think that is the only way.

Even China, if you look at a recent article today in the New York Times, it talked about how they are becoming a little too expensive for some folks and people are moving to Vietnam. And that process will continue to happen over time. U.S. cannot be sort of the low-cost provider. We have to add value. The question is how to do that.

I think you have to have an active Small Business Administration, an active trade procurement policy. You have to promote these things, to work with small business to identify new markets.

I think the gap right now is these industrial behemoths in China and India who need to be sourced. They need parts. They need supplies. They need people. American small businesses have an opportunity to source them.

Investor services is one area I have been reading a lot about. We have an opportunity to provide all these new companies with the type of value-added services that companies in their countries don't yet provide.

So I think it is a question of matching what we do well, which is going to be the high-value-added services, to what the developing country firms need; and I think that is going to take an active partnership between government and business. There really aren't any easy answers, but I don't think we can rely on currency fluctuations alone to guarantee our competitiveness.

Mr. SHULER. Thank you.

Mr. French, what has been your experience with the rates and availability of equipment in your dealings related to shipping products and exports?

Mr. FRENCH. As I mentioned, the rates have been very much increasing rapidly. I think one of the other areas is this lack of availability of equipment; and if you can imagine the sensitivity of some of the products we do ship, like logs from your area in North Carolina, it basically killed the business if the freight line said, well, sorry, we don't have any space for 6 weeks or 8 weeks and your product can't make it to the marketplace. So it has been the erratic and unstable ability to ship the product.

And you can imagine using wood. We don't have any alternatives besides the ocean carriers. So it has been an enormous—and, of course, the huge increase in diesel prices and the costs of inland transportation has clobbered people. It has been, again, the rapidness of it.

And the fact that we are a relatively low-value product has made us less desirable for people. Of course, if they are only going to take a certain number of runs in their trucks, they are going to get the highest-value cargo.

So it is a low-margin industry, and we are more dramatically hit by all of these costs, whether it be insurance costs, freight costs, trucking costs. All of these things have a much higher impact perhaps than on the more value-added manufacturing. And we need to continue to promote our value-added manufacturing. It is one of the things we have to do to survive.

Mr. SHULER. Madam Chair, just for the record—I would be happy to yield.

Chairwoman VELÁZQUEZ. If you would yield, Mr. French, I want you to know that, last month, the Committee held a hearing on freight and railroad costs for small businesses.

I yield back. Thank you for yielding.

Mr. SHULER. Thank you, Madam Chair.

Just for the record, we talk about subsidies that China continues to give. I mean, we have seen through this administration and still a continuation, the more money we borrow from China, the more opportunities they are going to be able to have to subsidize their companies. And so we have continued to see that over and over and over again. So we certainly have to put a stop to that in the future; and I am looking forward to that in the very near future, that we put a stop on borrowing the money from China and other countries that continue to take our textile businesses and our manufacturing businesses out of North Carolina. We lost over 300,000 jobs in North Carolina alone in the textile industries—300,000.

And, last comment, we got 10,000 permits on Federal lands to drill. Have at it. We don't need ANWR. Ten thousand permits. Ten thousand permits.

Mr. CHABOT. Would the gentleman yield?

Mr. SHULER. Absolutely, since this is an energy hearing.

Mr. CHABOT. Does the gentleman know on which of those 10,000 they have actually identified that there is oil there?

Mr. SHULER. On 250,000 acres. We just had the hearing in Natural Resources: 250,000 acres, 10,000 permits, no encumbrance from any type of environmental issues. They have been sitting there for 5 years unwilling to—and on top of that, we export our own petroleum, some 5.8 billion barrels a day.

Mr. CHABOT. But what I am saying, I don't know if the gentleman—maybe I didn't speak clearly enough, but when you say 250,000 acres, that is the total of all the permits. That is the acreage that is there. Correct?

Mr. SHULER. That is the acreage that is there that has been identified from the oil industry that there is available.

Mr. CHABOT. That there might be oil on—

Mr. SHULER. That there are available oils.

Mr. CHABOT. But they haven't determined on which of those places there is oil—

Mr. SHULER. Yes.

Mr. CHABOT. —until they drill or until they identify it.

Mr. SHULER. Well, there is geologists that obviously—that is why they have deemed it to be oil. Oil in North Carolina—

Mr. CHABOT. If the gentleman will continue to yield, because I have seen this talking point out this past week, and I saw Rahm Emanuel talking about 68 million acres or whatever he is talking about that they can already drill so they don't need to go in ANWR. But, oftentimes, oil hasn't been identified. That is just speculative as to where it might be. So it doesn't mean there is oil in all those particular locations. So it is somewhat misleading when Rahm throws out a number like 68 million and acts like, well, we don't need to go in ANWR or the Outer Continental Shelf because we have got all those places they are not drilling now.

Mr. SHULER. Madam Chair, reclaiming my time, reclaiming my time, thank you for holding this Small Business hearing; and we will get to energy policy.

Chairwoman VELÁZQUEZ. If the gentleman would yield for a second?

Mr. SHULER. I would be happy to.

Chairwoman VELÁZQUEZ. But I would like to ask a question to the ranking member. If we go into ANWR, will that bring us relief, immediate relief, that we need?

Mr. CHABOT. Will the gentlelady yield?

Chairwoman VELÁZQUEZ. Yes. I am asking you a question.

Mr. CHABOT. I thank the gentlelady for yielding, because the point that I have heard about we don't—even if we drill in ANWR now we won't see that oil for another 5 years or 10 years, that is why we should have done this 5 or 10 years ago; and I voted 11 times in the last 14 years to do that. Now, so, no, we are not going to have that oil for a couple years.

However, much of the price, for example, $58 a barrel to $140 a barrel in the last year or so, is speculation as to what we think oil is going to be available in the future. So if we passed—and I would urge the Speaker to do that, to allow Congress to have a vote and we passed going into ANWR, I think you would see an immediate impact in the price out there because it would say that we are finally serious. And apparently we weren't very serious at 2.30 a gallon. We sure as heck ought to be serious at $4 a gallon.

Chairwoman VELÁZQUEZ. Reclaiming my time, let me just say there has been legislative initiatives that passed through the House, are sitting at the President's desk, and others that have been signed into law and have not been implemented. H.R. 6, for example.

Mr. CHABOT. Does that allow us to drill in ANWR?

Chairwoman VELÁZQUEZ. I am sorry? We are not talking about ANWR. We are talking about price gouging. We are talking about providing relief to small businesses to be able to purchase technology that will bring their electricity consumption down. That is the type of legislation that has been signed into law and that the administration refuses.

Yield back.

Mr. SHULER. Madam Chair, this is, of course, my first term in Congress. Could you just tell me which party was in total control of the White House, the Senate, and the House?

Chairwoman VELÁZQUEZ. I am sorry, I wasn't listening.

Mr. SHULER. This is my first term. Can you tell me which party was controlling the White House and the Congress for the last 12 years?

Chairwoman VELÁZQUEZ. For the last 12 years, the Congress was controlled by the Republicans, and for the last 8 years the White House.

Mr. SHULER. I yield back.

Chairwoman VELÁZQUEZ. Well, I guess that we have to go back to trade.

Mr. CHABOT. It is our side's turn for questioning, right?

Chairwoman VELÁZQUEZ. Yes, it is your side for questioning.

Mr. Akin?

Mr. AKIN. Are we going to talk about the Small Business hearing or you want to talk about energy? I am all ready to go on energy. Let's talk about the fact that the Republicans passed a bill year after year to develop American energy, and it was killed by the Democrats in the Senate. When you add up all the votes on American energy, you find out the bottom line is that Republicans 90 percent of the time supported American energy, and Democrats 90 percent of the time have voted against all different kinds of things, from ANWR to nuclear to recycling nuclear to coal shale.

Chairwoman VELÁZQUEZ. Would the gentleman yield?

Mr. AKIN. Yes, I will be happy to. We will have a little discussion here.

Chairwoman VELÁZQUEZ. Last thing I know is that the Senate was controlled by the Republicans 2 years ago. So how did they the Democrats kill the bill?

Mr. AKIN. Certainly you know, but maybe other people in the room don't, and that is because all you have to have—you have to have 60 votes to pass a bill. The Democrats killed that energy bill in 2001. The Democrat Senators killed it in 2002. They killed it in 2003. They killed it in 2004. We aren't picking winners and losers.

But it had the whole thing in there. Finally, a watered-down version in 2005.

Chairwoman VELÁZQUEZ. There was a lot of subsidies for oil companies.

Mr. AKIN. It wasn't subsidies for oil companies. People jump in with this deal about, oh, the obscene profits of the oil companies. The only reason they are making obscene profits is because we don't have enough supply. If there is more supply, they couldn't charge those high prices. So what we need to be doing is developing American energy in a whole lot of different forms.

But I didn't really have a question for our witness, Madam Chair. I just thought we could talk about that a little bit if you want.

Chairwoman VELÁZQUEZ. Enough said?

Okay. Mr. Davis?

Mr. DAVIS. Thank you, Madam Chairwoman; and I do appreciate the panelists being here.

And, as you can see, energy is on a lot of people's minds here in Congress; and I think it is on a lot of people's minds across America. It is definitely on people's minds back in east Tennessee. Just a month ago, I met with Earl Humphreys, who owns Lawn Boyz Lawn Care Center; and he is talking about having to close his business because of the high cost of energy.

Since you are here to testify, and could you tell me what energy costs actually does to each one of your industries? And what would happen if we could actually become an energy policy that would bring it down from $4 a gallon maybe to $2 a gallon, where it was when the Democrat majority took over last year?

Mr. JOHNSON. I can just say that energy prices have a huge impact on the textile industry. We are a very large consumer of energy because of the weaving, and particularly the dyeing and printing of textile materials require enormous amounts of energy.

So when they go up and, you know, they don't go up overseas, and one of the—I don't want to keep bringing China in, but they are our biggest competitor. When China starts increasing its subsidies for energy, as I think has been well documented by the steel industry, that China is now subsidizing the electrical costs for its manufacturing sector by hundreds of millions of dollars a year, we become less competitive.

But I would like to mention—I don't know about the bill and about the small business energy upgrades—we have a very large mill in Trion, Georgia, one of the most impressive mills in the United States, one of the largest mills, and it makes apparel yarns and fabrics, goods for the U.S. military, and they cannot afford to upgrade to get more energy efficiency out of their furnaces. And they know how to do it. They know they need to do it. They don't have the money to do it.

So if there is some assistance that you can give to smaller companies so that they could get the energy efficiencies that are available out there, I think that would be very, very important. They mentioned that to me specifically, is if you can find a way to help me increase my energy efficiencies, this plant may stand a good chance of surviving.

Mr. DAVIS. That is very good. Thank you.

Mr. French?

Mr. FRENCH. Of course, it is a huge, huge problem for industry, our industry, loggers, everything else. But we need to recognize that the Europeans have paid double the prices we have paid for a long time. I think the shock is the rapid increase and the fact that, quite honestly, we have been living with very low energy costs in this country for a long time. And I would really urge and I think a lot of small businesses would benefit from government support in grants in terms of conservation, in terms of alternative energy issues, investment in alternative energies.

We have got to solve this. We have got to reduce our dependency on the fossil fuel economy, and we need to get other products and other energy sources into the marketplace as quickly as we possibly can. And I think you have got an industry on the wood industry side that is very eager to work with the government in looking at these alternative fuels and things like geothermal, solar, wind, all these alternative energies, and getting government support for small businesses to use those alternatives.

At the moment, the payback is pretty long. But if we had some tax and other incentives to invest in these things in our plants and put in wood boilers and put in windmills and other things, and we got some support in the short term, in the long-term we would be dealing with climate change, we would be dealing with energy efficiency, and we would be making these businesses more profitable.

So I think there is a lot of positive things that can come out of this, and I hope that the Congress will look at these things and think about it.

Mr. DAVIS. I certainly agree with what you just said. I do think we have to have all of the above. I think we need green energy. I certainly support it as a conservative in Congress.

My main question was, gas prices have gone from $2 to $4 a gallon. What has it done? What impact has it had on the Hardwood Federation.

Mr. FRENCH. It has had a huge negative impact, particularly the internal costs of fuel and the diesel increase in such a rapid way.

Mr. DAVIS. Has it cost jobs in your industry?

Mr. FRENCH. It has cost jobs in our industry, yes.

Mr. DAVIS. We need an energy policy. That was my point. And I yield back.

Chairwoman VELÁZQUEZ. Okay. Time has expired.

Mr. Johnson and Mr. French, as part of the H.R. 6 bill that we passed, the energy bill, we included in that package legislation that we reported out of this Committee, and it was a well-thought-out package that includes financial relief for small businesses to purchase technologies that would allow for them to bring those prices down.

And this is the time to implement it. It was signed into law. So what we need is to get the Small Business Administration, the White House to implement the program.

Mr. Griswold, you mentioned that currency manipulation is a regular practice among countries and, further, that China has increased the value of the yuan over the last couple of years. But American manufacturers still contend that the yuan is undervalued by as much as 40 percent. Clearly, there is market intervention.

Our responsibility is to work to help our businesses be competitive. What is your suggestion to upset this disadvantage?

And, Mr. Johnson, you know, they all mentioned the disadvantage that their industries are facing due to not only currency manipulation but the tax imposed to the products. So what do you offer? How can we provide a level playing field?

Mr. GRISWOLD. Madam Chairwoman, thank you.

I don't think I used the phrase "currency manipulation." You know, half the countries in the world have a fixed currency or some kind of a hard peg. So it isn't that unusual. And the U.S. and the other Western countries had fixed currencies for several decades after World War II.

I do think freely floating exchange rates are the ideal. I think Milton Friedman was right. They work the best.

But China is making progress. You know, they are in many ways still a developing and underdeveloped economy. They have a poorly developed financial system. I don't think a freely floating exchange rate is probably the right idea for them right now. But let's give them credit. They are moving rapidly in the right direction.

A 20 percent appreciation is significant, this at a time when the U.S. dollar has been depreciating. I would say let's not put too much stock in exchange rates. Let's not worship at the altar of a depreciated currency.

This is where trade and energy come together. One reason why the price of oil has gone up so much in the last few years is the depreciating dollar. When dollars are worth less, oil producers are going to demand more dollars. This feeds through to the costs.

Over half of what we import to the United States are imported by businesses. They are raw materials, wood, energy. They are intermediate products, parts that go into final products. They are capital equipment. And small businesses are importing those things.

So a depreciated currency that we have, our U.S. currency has depreciated significantly, that is a two-edged sword. It helps us export, but it is also feeding into raising the costs that these gentlemen's industries are paying.

So I don't think that we can wave a billy club over China's head and tell them they need to appreciate their currency another 20 percent. It is not going to make a dramatic difference. Our exports to China are booming despite their currency policies.

Chairwoman VELÁZQUEZ. Mr. French and Mr. Johnson, you know, we have some trade agreements pending: Korea, Panama and Colombia. If there is a provision that you feel that should be made part of that agreement that will provide a level playing field for small businesses, and particularly for the industries that you represent, what will that be?

Mr. JOHNSON. Well, I mean, I will go back to the issue of currency manipulation. Korea was one of the originators of the export scheme to devalue your currency so you could export more. And USTR had guidance in Trade Promotion Authority saying that it needed to address currency manipulation practices. And there was nothing in that agreement that says Korea cannot do whatever it wants with its currency, regardless of the damage it can do to U.S.

business. So I think that tends to undermine even the possibility of benefits from an agreement.

Mr. FRENCH. I don't have anything specific. Korea is the only one of those countries that is a reasonably significant market for lumber products, and we haven't had too many difficulties there. But I will ask our people here to see if there is anything specific and get back to you.

Chairwoman VELÁZQUEZ. Thank you.

Well, gentlemen, thank you all for being here today.

I ask unanimous consent that members will have 5 days to submit a statement and supportive materials for the record.

Without objection, so ordered.

This hearing is now adjourned. Thank you.

[Whereupon, at 11:26 a.m., the Committee was adjourned.]

NYDIA M. VELAZQUEZ, NEW YORK
CHAIRWOMAN

STEVE CHABOT, OHIO
RANKING MEMBER

Congress of the United States
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STATEMENT
Of the Honorable Nydia M. Velazquez, Chairwoman
United States House of Representatives, Committee on Small Business
Full Committee Hearing: "Small Business Exports in the Current Economic Climate"
Thursday, June 19, 2008

It's no secret that the nation's economy is struggling. Just last month, the unemployment rate reached 5.5 percent, hitting its highest point in four years. And with the rising costs of basic commodities, few Americans remain untouched by the increasingly fragile economy.

During past downturns, America's small businesses have helped jumpstart the economy through trade. But unfortunately, that has not been the case today. In this hearing, we will review the current economic climate and explore the barriers hindering this vital sector.

History has shown trade to be the silver lining in a weak economy. In the early 1990's, for example, the country was reeling from a demoralizing recession. In fact, the situation was not all that different from the one we face today. But rather than allowing the era's weak economy to hold them back, American businesses looked to opportunities abroad. As a result, U.S. trade led the way into the boom of the late 90's, when American exports skyrocketed from $535 million to just over $1 billion.

But today, American exports are declining rather than rising. And the rate of decline has been extreme-- In the two months between February and March of this year, U.S. exports dropped $2.5 billion.

These figures are simply unbelievable. To say that export numbers are declining would be an understatement—export numbers are not falling, they are plummeting.

We now know that commerce is falling sharply for businesses in the areas of capital goods, industrial supplies and advanced technology. Last month alone, these industries witnessed a $100 million drop-off in exports.

And these kinds of declines are not industry-isolated, either. Trade with NAFTA countries, the bread and butter for many small exporters, has also dropped off considerably. In fact, commerce has slowed to virtually *every* foreign port. These declines are also manifesting themselves domestically, where trade at our top ten ports is down $100 million.

Still, it seems the worst is yet to come. Export orders, a leading indicator of future trade, show no light at the end of the tunnel. Instead, they have dropped 6.5 percent for the service industry and slowed for manufacturers.

Members of this committee are well aware of the integral role that small exporters can play in reversing these trends. Ninety-seven percent of America's small firms are exporters. And in fact, one third of all U.S. exports come from entrepreneurs. That means that any dent in American exports becomes a crater in the small business community.

Why, then, are exports declining in traditionally entrepreneur-driven industries?

A number of factors have come into play, creating what now looks to be a perfect storm. At the heart of that storm are shrinking market stakes. On that front, the U.S. now stands in third place behind Germany and China. It should also be noted that 90 percent of small businesses export to only one country, a fact that has made them far more susceptible to economic volatility and market shifts. But perhaps most troubling is the damage that we have done to ourselves—sadly, the current administration has failed its own small exporters by under funding trade-friendly initiatives.

In this morning's hearing, we will further examine these barriers.

Trade may be on the decline and the economy may be suffering, but just as we used trade to turn the economy around in the 90's, it can serve as a catalyst today. And what better place to begin than with our entrepreneurs? After all, small firms are the backbone of American business. They have steered us out of past recessions, and they can lead the way again today.

I want to thank all the witnesses in advance for their testimony. The Committee is pleased they could join us this morning, and looks forward to their insights on the issue. With that, I now yield to Ranking Member Chabot for his opening statement.

U.S. House of Representatives

SMALL BUSINESS COMMITTEE

Thursday, June 19, 2008

Representative Steve Chabot, Republican Leader

Opening Statement of Ranking Member Steve Chabot

Small Business Exports in the Current Economic Climate

Thank you, Madam Chairwoman, and thank you for holding this important hearing on small business exports. I'd like to welcome our distinguished panel of witnesses and thank them for taking time out of their schedules to provide this committee with testimony. Good morning to all of you, and thank you for being here.

One of the most important functions of this Committee is to look for solutions to help entrepreneurs gain access to global markets. Not only do we look for new and innovative ways to help small businesses conduct international trade, but we must also conduct the requisite oversight to ensure our current programs are effectively keeping up with the changing times.

Last year, this committee worked in unison in order to put together a piece of legislation--H.R. 2992, the "SBA Trade Programs Act of 2007"—that passed the House with broad bipartisan support. This legislation brings changes in the SBA's operation of its programs to enhance small business participation in the global economy. H.R. 2992 represents the Small Business Committee's continued commitment to promotion of international trade by America's small businesses.

The Small Business Administration has a number of general entrepreneurial assistance programs that provide technical advice to small business owners. However, international trade is an area that is fraught with regulatory hurdles requiring specialized knowledge that may not be available from the SBA's entrepreneurial partners.

It is not surprising to find that the SBA created other programs to meet the needs of small business exporters that rely on personnel with specialized knowledge about the international trade regulatory regime. These programs, as well as the SBA efforts to coordinate with other agencies such as the Department of Commerce, have enhanced the worldwide profile of many U.S. exporters.

There are about a quarter of a million small businesses in the United States that export. There's no doubt that small businesses are playing a vital role in reducing America's trade deficit. Continuation of this success and even greater emphasis on small business exporting will undoubtedly benefit the American economy.

Additionally, this Congress has the opportunity to pass legislation enacting free trade agree agreements with several of our allied nations--including Colombia, Panama, and South Korea. I remain hopeful that Congress will work together to pass legislation that will implement these pending trade pacts.

These agreements should be supported by Congress. The Administration, particularly former U.S. Trade Representative Rob Portman and the current USTR Susan Schwab have worked hard over the years to make sure the trade pacts addressed concerns about labor, environmental violations, and intellectual property theft in certain regions of the world.

These pacts can also be useful in spurring negotiations for larger trade discussions, such as the Doha trade negotiations. Non-free trade countries may feel compelled to work with other nations to ensure that they are not isolated from the rest of the world.

In the U.S., free trade agreements have enabled local businesses to expand their market base as well as provided consumers with greater access to different products at more competitive prices. In Ohio, trade has enabled businesses to grow. More than 11,000 companies export goods from my home state to places all over the world. Eighty nine percent of those companies can be defined as small and medium sized businesses—ones that traditionally (and rightly) have been called the backbone of the American economy. In addition, one-fifth of all manufacturing workers in Ohio depend on exports for their jobs.

It appears clear to me that exporting is a critical part of building the American economy, especially for small businesses. We have an excellent panel with us today to help us identify some of the obstacles that remain to encouraging trade among small and medium sized businesses. I look forward to their testimony and yield back.

NATIONAL COUNCIL of TEXTILE ORGANIZATIONS

WITNESS STATEMENT OF
MR. CASS JOHNSON
PRESIDENT
NATIONAL COUNCIL OF TEXTILE ORGANIZATIONS

HOUSE COMMITTEE ON SMALL BUSINESS

June 19, 2008

Chairwoman Velazquez, Ranking Member Chabot, and distinguished members of the Committee, thank you for the opportunity to appear today and outline the U.S. textile industry's perspective on the state of small business exports.

My name is Cass Johnson and I am President of the National Council of Textile Organizations (NCTO). NCTO is a not-for-profit trade association established to represent the entire spectrum of the United States textile sector, from fibers to yarns to fabrics to finished products, as well as suppliers in the textile machinery, chemical and other such sectors which have a stake in the prosperity and survival of the U.S. textile sector. NCTO is headquartered in Washington, D.C., and also maintains an office in Gastonia, North Carolina.

The U.S. textile industry is comprised almost entirely of small- and medium-sized businesses and most of the products produced by NCTO's member companies are exported overseas, so we are very appreciative that the Committee is addressing the vital issue of the barriers to exporting that small- and medium-sized businesses face.

As a sector, the U.S. textile industry is one of this nation's most successful exporters. At $16 billion last year, we are the third largest exporter of textile products in the world and export about one out of every three textile products we produce. On the apparel component side of the equation, our export percentage is even higher, with probably nine out of ten yards of U.S. fabric manufactured for use in apparel being exported overseas.

If we drill down into these numbers still further, we can see why this hearing is so important. Almost three quarters or $12 billion of all U.S. textile exports go to countries in the Western Hemisphere where free trade agreements or preference programs provide duty-free access to the U.S. market and where these countries have established assembly platforms for shipping finished garments back to the United States. Only one quarter, or $4 billion, in U.S. textile exports go to the rest of the world. This includes Europe, Japan, India, China and Brazil.

In fact, we send China, a country with a population of more than 1.4 billion people and which consumes more textile and apparel products than any other country by far and which also has a textile and apparel complex employing 15 million people, only $500 million a year in U.S. textile products. Compared to India, however, our export figures to China appear strong. India, a country with 1.1 billion people, only imports $55 million a year in U.S. textile products. We export more textile products to the United Arab Emirates annually than we do to India.

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Something is clearly not right here. While we do not expect that our textile and apparel trade with India or China should necessarily be balanced, particularly because of the high labor content in apparel, we do expect we should be able to take advantage of countries which have rapidly growing economies, large increases in per capita income, and dramatic increases in consumption of textile products. And yet that is not happening to any significant degree.

What is happening? In addition to the problem of high duties[1], we see three major non-market barriers at work. These are all imposed by foreign governments to both protect their domestic markets from import penetration and to encourage growth in their exports, and they are all costing us valuable export opportunities and that means U.S. jobs.

These three barriers are the VAT, currency manipulation and other government subsidies. Each one is significant in its own right – the combination of all three makes these large and growing markets virtually impenetrable. And the problem is not just limited to China and India though these countries represent the biggest lost opportunities. The problem extends to Brazil, Indonesia, Korea, Taiwan and, in an important degree, to the European Union.

VALUE ADDED TAX

Of these three, perhaps the most unacknowledged and least understood is the VAT or Value-Added Tax. The VAT is a tax, which averages 15 percent, that is leveled on exports from the United States (as well as other countries) to countries with a VAT system. Because virtually every country in the world has adopted a VAT (148 countries) over the last four decades, this means that virtually every product we export gets hit by the VAT.

The problem with the VAT is that U.S. exports are essentially taxed twice – first U.S. exporters pay direct taxes at home and then they pay an average 15 percent VAT assessment when those goods enter another country. The opposite is the case for products being exported to the United States. First, countries that employ a VAT, rebate the VAT when goods produced in that country are exported and then they are not required to pay a VAT or border tax when those goods are imported into the United States. This means that U.S. exports are taxed twice while imports into this country are free of most taxes incurred by U.S. producers.

Under normal WTO rules, the VAT would be considered an export subsidy and therefore be banned. WTO rules say that countries are not allowed to provide export subsidies in the form of tax rebates. But the United States, unwisely in our opinion, agreed in 1960 to exempt VAT taxes from this rule. Since that time, most countries have moved to a VAT system and, in fact, the United States is the only major trading country today not to employ a VAT.

While this is something of a stealth issue, the impact is enormous. According to calculations done by the American Manufacturing Trade Action Coalition[2], the VAT inequity cost U.S. producers and service providers $341 billion in additional taxes on U.S. exports. These are extra taxes that U.S. exporters pay to do business overseas that their competition does not have to pay. That means an awfully lot of lost business for U.S. manufacturers and is a significant barrier for small- and medium-sized business who want to export their products.

[1] Most developing countries put high duties on U.S. exports of manufactured goods, usually 15 percent or more. In the case of textiles, duties are usually much higher, starting at 20 percent and, in the case of India, reaching as high as 400 percent (on woven shirts). The Doha Development Round of World Trade Organization talks has ground to a halt on the issue of developing countries being willing to open their markets to manufacturing exports. Currently, India, China and Brazil are refusing to support anything more than token cuts to their actual duty rates and, additionally, are asking for the ability to shield entire sectors, including textiles, from making any duty cuts. At present, U.S. exporters stand little hope of gaining any real market access from these talks.

[2] See www.amtacdc.org; also see www.bordertaxinequity.net for a thorough review of the VAT problem and how to solve it.

NCTO believes the VAT disadvantage is one of the major reasons that U.S. exporters are not doing better overseas and that U.S. producers are facing such tough competition from China and others in the U.S. market. In fact, it cannot be otherwise – a 15 percent margin is simply too big an obstacle to overcome for many U.S. manufacturers. Profit margins in U.S. manufacturing average less than six percent and in the textile industry they typically range from two to three percent. Giving your competitor a 15 percent price break because they are bringing goods in from offshore is usually tantamount to giving the sale away.

It may not be surprising that the biggest winners from the VAT problem also run the largest trade deficits with the United States:

VAT Disadvantage Leads to Large Trade Deficits ($ bil.)		
	VAT Disadvantage	U.S. Trade Deficit
China	$48	$201
Mexico	$41	$120
Canada	$33	$78
Germany	$18	$51
Source: OECD, U.S. Census, 2005.		

Finally, another significant problem with the VAT is that it provides a convenient loophole for countries to negate duty concessions made as part of a bilateral, regional or multilateral trade agreement. For instance, declines in applied tariff rates in the European Union have been mirrored by increases in standard VAT rates. This has led to a situation where total charges to imports from a country like the United States are almost identical to what they were forty years ago despite declining tariffs.

There is a short term answer to the VAT disadvantage. It is the Border Tax Equity Act, H.R. 2600 introduced by Congressmen Bill Pascrell (D-NJ) and Mike Michaud (D-ME), a member of this committee, as well as Congressmen Duncan Hunter (R-CA), and Walter Jones (R-NC). The Act would negate the VAT disadvantage to U.S. producers and has three basic components. First, it would direct the United States Trade Representative (USTR) to negotiate a remedy for the VAT inequity through the WTO by 2009. Second, if there is no negotiated solution by that specified date, the United States then would begin charging an offsetting tax on goods and services at the U.S. border equal to the VAT rebated by the exporting country. Third, the U.S. government would rebate taxes to U.S. companies exporting goods to foreign countries at the same rate as those countries impose a VAT at their borders. NCTO strongly supports the Act and hopes the Committee members will review it with an eye towards correcting a fundamental inequity and spurring export growth among small and medium sized businesses in the United States.

CURRENCY MANIPULATION

The problem of currency manipulation has become better known as the trade deficit with China has grown to what must once have seemed unimaginable levels. The trade deficit with China has grown by 60 percent during the last three years and increased by 26 percent in April alone; it now stands at over $250 billion a year and consumes one third of the entire U.S. trade deficit.

China's manipulation of its currency is an export subsidy. Currency manipulation gives China's manufacturers a substantial unfair trade advantage, and the fact that U.S. manufacturing workers are the primary victims of China's policies is no longer disputed. President Bush, Alan

Greenspan, the International Monetary Fund and a long list of economists, politicians, think tanks and government institutions have all agreed that China should stop manipulating its currency and distorting world trade.

The swing side of the currency manipulation problem is that manipulation not only gives a huge bonus to imports from China but it also places a huge tax on exports from the United States. Just as U.S. imports from China get a price break of 25 to 40 percent from China's undervalued currency, U.S. companies trying to export to China are paying 25 to 40 percent more to sell their goods[3] in the Chinese market. This is a significant factor in the a trade balance where China exports five times as much to the U.S. as the U.S. exports to China.

What is less understood is that the Chinese model of suppressing its currency in order to build export markets is not an isolated case. China copied its Asian neighbors - Korea, Japan, Taiwan and others – when it began using its currency in the 1980s as an economic weapon to achieve higher living standards for its people. The export powerhouses in Asia have long practiced an economic mercantilist model for growth, one which depends on the development of export, rather than consumer, markets. The key strategies employed by these countries have been to develop national industrial strategies and marry them to undervalued currencies in order to dominate manufacturers in their home markets in the United States and Europe.

The problem is therefore not just with China but with economies across Asia that manage their currencies. And the answer to the problem is one step away from resolution – H.R. 2942, the Currency Reform for Fair Trade Act of 2007 sponsored by Congressmen Tim Ryan (D-OH) and Duncan Hunter (R-CA). This bill, which has been strongly supported by members of this committee,[4] would give U.S. manufacturers the tools to combat currency manipulation by China and others. This tool is simply the legal ability for injured U.S. manufacturers to seek countervailing duties based on the damage that currency manipulation has caused their companies. The enactment of the Ryan-Hunter bill would send the most powerful message possible that the U.S. Congress will not allow China in particular to continue to wreak havoc in the U.S. manufacturing sector and that Congress intends to begin to redress the 1.5 million manufacturing jobs that have been lost to China over the last ten years[5].

GOVERNMENT SUBSIDIES

The third major government barrier that U.S. exports face is the presence of government subsidies to domestic producers. These subsidies, which in the case of China, Vietnam and India, are significant in size and scope, make it extremely difficult for U.S. exporters to compete in these foreign markets. And these are, unfortunately, precisely the markets where the greatest economic growth is occurring today. By using subsidies to support domestic producers, these countries are essentially walling off a large portion of their economies from U.S. exporters.

China is of course the iconic model for how to subsidize an industry, indeed an entire economy, into a world export powerhouse. As a non-market economy, China has decades of experience in using central government command and control policies to shape industrial growth. In textiles, to cite one example, China has now embarked on its ELEVENTH Five Year Plan for the textile sector.

[3] Regarding the amount of undervaluation of the Chinese yuan, the most widely used figure is 40 percent. Since China began increasing the value of the yuan in 2006, the yuan has appreciated by 19 percent, though in nominal trade-weighted terms, which are more accurate, the appreciation is only 12 percent.
[4] This bill superseded the Fair Currency Act of 2007, HR 782. Fourteen members of the HSBC co-sponsored either one or both of these acts.
[5] http://www.uscc.gov/researchpapers/comm_research_archive.php, U.S.-China Economic and Security Review Commission, Feb 2005.

It was not until recently that we were able to get a more comprehensive picture of precisely how China directs and supports its manufacturing sector. This picture has been unfolding steadily since the U.S. government overturned existing policy late in 2006 and began allowing U.S. industry to file countervailing duty cases against China.

The picture that has emerged is deeply troubling. China's government subsidies are now known to be available in every area that impacts the cost of a manufactured good -- from the cost of labor to the cost of capitol, from the cost of electricity to the cost of land, from the cost of new machinery to the cost of advertising and promotion. CVD cases brought by U.S. industry have identified dozens of subsidies that the Chinese government offers companies that export goods to the United States.

As an example, in a textile products case involving laminated woven sacks, the U.S. government found that the Chinese government offered 24 different subsidies to its domestic producers. As a result, the government imposed countervailing duties ranging from 27 to 359 percent on Chinese exporters of these products.

The U.S. government's decision to allow CVD cases to be filed against non-market economies like China was an important step in addressing the problem of China's government intervention in its economy. But it is only a first step. It is only a first step because it does not prevent China from subsidizing its manufacturers; it only deters those few producers whose specific products have countervailing duty imposed against them. For most small and medium sized manufacturers, CVD cases are simply too expensive and time consuming to file. The cost to simply prepare a case for filing typically runs over one million dollars.

What the government needs to do is to go after China in the World Trade Organization both where China's subsidies are de facto illegal but also in cases where China's subsidies can be ruled as illegal because of the damage they cause to U.S. industry. The U.S. government has stepped up its prosecution of some de facto illegal subsidies over the past several years but still has not allocated the resources to make this a major initiative. For example, over one year ago, NCTO sent the Office of the United States Trade Representative (USTR) a list of 63 subsidies (attached) that China offers its domestic textile industry and requested USTR to investigate whether the subsidies were de facto illegal. We are still waiting for an answer. The problem, we have been told, is resource allocation. It is still unfortunately the case at USTR and elsewhere that significantly more resources are devoted to negotiating new trade agreements than in enforcing existing ones.

On this front, Congress can also play a significant role. Congress should change USTR's focus for the next five years from negotiating new agreements to reviewing and enforcing existing agreements. USTR's resources should be re-oriented towards verifying that China and others are living up to the agreements that they have signed and, if they are not, they should file cases against them at the WTO.

CONCLUSION

The United States exported almost $1.2 trillion dollars last year, an impressive level of exports by any standard. Most of those exports went to Europe, Canada and Mexico while exports to China, India, Brazil and other rapidly growing markets remain far behind. And the U.S. manufacturing sector, not so long ago the world's greatest exporter, has now been displaced by China which continues to grow at double digit rates.

The principal reasons are a trifecta of barriers to U.S. exporters that have been erected by these rapidly growing and developing economies. These include the VAT, currency manipulation and subsidy regimes. As outlined in this testimony, Congress today has legislation in hand that can begin to roll back these barriers and usher in a new renaissance for the U.S. manufacturing sector and its workers. We thank the Committee for its continuing efforts to highlight the importance of the U.S. manufacturing sector and for holding a hearing on this important subject.

Mr. Jameson French
Northland Forest Products
36 Depot Rd.
Kingston, NH 03848

Current State of Small Business Exports

U.S. House of Representatives
Committee on Small Business

June 19, 2008

Madam Chairman and members of the Committee, thank you very much for the opportunity today to address the export trends for small businesses. My name is Jamey French and I am President of Northland Forest Products, a family-run hardwood business which was founded in 1970, and with a history dating back to the late 19th century. Northland Forest Products continues today with domestic operations in New Hampshire and Virginia. We are a high-volume hardwood manufacturer with exports representing 45% of our total sales. We have served customers in 24 countries and provide top-quality Northern and Appalachian hardwoods.

I also serve as Chair of the Board of Directors for the Hardwood Federation which is an industry trade association that represents over 14,000 businesses, 30 trade associations and over one million hardwood families. The majority of these organizations are engaged in the manufacturing, wholesaling, or distribution of North American hardwood lumber, veneer, plywood, flooring, pallets, kitchen cabinets and related products. Hardwood facilities are located in every state in the union, in fact, 341 hardwood facilities are found in the districts of members on this committee.

As a representative of the hardwood industry and a company owner, I am here today to testify on the export trends and trade challenges that face the small hardwood business owners. The U.S. hardwood industry is a major exporter. The total volume of hardwood exported in 2007 was 2.94 billion. Exports are the livelihood for many hardwood businesses. In fact, the near-term future of the hardwood industry depends upon exports. The decline of the U.S. furniture industry and the recent housing crisis are major reasons why hardwood exports are increasingly important for the U.S. hardwood industry. We are constantly looking for new potential markets, like India and the Middle East. We need to expand growth opportunities in the Far East and Europe. For example, China and much of the Far East has a growing high end market interest in the beautiful, luxury products manufactured from U.S. hardwoods. We also see possible opportunities emerging from a stronger middle class wealth in Eastern Europe which could increase imports from the U.S. of specialty hardwood products.

In order to capitalize on these marketplace opportunities, we need to maintain a level playing field in order to be competitive internationally. Recent export challenges we face interfere with our ability to compete globally. These include possible increase in certification export fees, increased freight and shipping charges, and a shortage of shipping containers. All of these factors have contributed to industry woes. In addition, we are concerned with the recent foreign procurement policies, specifically in the European Union, requiring documentation for legal and sustainable hardwoods. I will be providing you more detail on all of these challenges, but first a brief overview of hardwood export market.

Hardwood exports include lumber, logs, veneer, flooring, plywood, molding and siding. Lumber dominates exports with 13% of production volume now being exported. This is up from 6% in 1997. Important to note, however, is the value basis of lumber exports is approximately 25% of production and that percentage is rising. This is due to the fact that the lower grade hardwood stock tends to not be exported. Following are details on hardwood exports and major markets. In summary, the EU is currently the largest export market in terms of value as well as highest unit value market.

Export data for the specific hardwood products:

Lumber: $1.4 billion (down from $1.6bn in 2006)
Logs: $806 million (up 30% from '06)
Veneer: $447 million (up 4% from '06)
Flooring: $92 million
Hardwood Plywood: $87 million
Chips, molding and siding make up balance of around $85 million combined.

The major export markets are as follows:

Export markets for Lumber:
1) Canada: $370 million*
2) China: $222 million
3) Italy: $111 million
4) Mexico: $98 million
5) Spain: $85 million
6) Vietnam: $66 million
7) UK: $64 million

Export Markets for Logs:
1) China: $189 million (up 35% from '06)
2) Canada: $136 million (down 23% from 2006. In '07, China surpassed Canada for first time)*
3) Italy: $58 million
4) Germany $51 million
5) Spain: $48 million
6) Hong Kong: $46 million

Export Markets for Veneer
1) Canada: $143 million*
2) Spain: $55 million
3) Germany: $54 million
4) Italy: $31 million
5) China: $30 million

** Overwhelming majority of US exports to Canada return to the US as further manufactured products or are re-exported to EU, Asia.*

Now, a review of some of the export challenges we face as an industry. First, I would like to address the potential increase in export fees. The USDA Animal and Plant Health Inspection Service (APHIS) provide the industry with a Phytosanitary Certificate which was developed to satisfy foreign regulatory standards. Our industry is required to issue a certificate for each container of lumber they ship into a country that requires a Phytosanitary Certificate to ensure that the wood is free from invasive pests. Certificate costs last year, at a rate of $50.00 per container, were close to $100,000 for some hardwood exporters. A cost we recognize is part of doing business in many foreign markets. However, APHIS has announced a proposal to raise this export certification fee by nearly 100%. As proposed, the fee hike would raise the certification fee for an export shipment from the current rate of $50 to $99. With already tight margins, it has been estimated that this increase could cost some exporters up to $200,000 a year. To address this increase, we have been working closely with APHIS on an alternative cost savings plan that would offer a Kiln Drying (KD) certification system in lieu of the APHIS Phytosanitary Certificate. This is an acceptable treatment process to control invasive pests and is recognized by USDA for its effectiveness. APHIS has sent letters to China, Vietnam and Australia asking for their acceptance of the KD certificate in lieu of the APHIS Phytosanitary Certificate and we are awaiting their response. (Please find enclosed an estimate of Phytosanitary Certification costs vs KD costs and a copy of the USDA letter to Vietnam requesting acceptance of KD certificate.)

Of importance to note with this issue is our largest challenge remains with our largest market. The EU currently requires the Phytosanitary Certificates for Oaks, Maples, Sycamore, Poplar, Chestnut and Ash. This is a very significant percentage of the market and our industry views the EU's acceptance of KD Certification in lieu of the government sponsored Phytosanitary Certificate a priority. While we are encouraged by the possibility of opening markets to the option of the KD certificate, in the short-term we are concerned about the increase in export fees currently proposed by APHIS. This type of increase would put a tremendous burden on the hardwood lumber businesses.

The industry requests the committee encourage USDA/APHIS to carefully consider the status of the development of the KD certification program along with the current economic condition of the industry before implementing the proposed increase. In addition, we would welcome your support in identifying effective strategies to encourage other countries to accept the KD certificate.

Second challenge of significant importance to the industry is the added freight charges hardwood industry exporters are experiencing. There is a growing concern for the increasing problems with ocean freight. This unexpected rise in charges from freight forwarding companies is creating a very difficult situation for our industry. It is an exorbitant cost for small business owners and one that cannot be passed on to the customer and remain competitive.

One North Carolina company tells the following story of what has been happening: Over the past six months, their business has experienced an increase in freight transportation booking fees by 141 percent. Here is a typical scenario we are seeing across the industry. Please note, the container values have remained stable and all have been shipped from Charleston, SC to Liverpool:

- December 3, 2007, freight charge of $1,450, with an additional fee of $200 once it arrived at the port.
- March 27, 2008 (3 months later) freight charge is $2,400. Almost $1,000 more, again with an additional fee of $200 when it arrived at the port.
- June 3, 2008 freight charge estimated at $3,200-$3,550, again almost a $1,000 increase with additional fees likely once the freight arrives at the port. Vessel is expected to sail on July 13, 2008.

The shipping companies and freight forwarders are demanding additional fees from $200-$1,000 to load containers of hardwood lumber that were already under contract. These contracts now state that all shipments are "subject to carrier and / or port security fees in effect at the time of shipment". In addition to these fee increases, the industry is experiencing bookings that were contracted and then cancelled within 24 hours of the vessel sail date after the container has arrived at the port.

Lumber exporters have little to no idea what it will cost to ship goods internationally. Sales are made and contracts signed today for fees that are not honored. Lumber exporters have no recourse but to pay the additional fee to move the goods or cancel the order and lose the sale. This is happening repeatedly at the domestic ports.

We would like to request the Committee encourage regulatory bodies to review the business practices of shipping companies and their transportation charges to ensure responsible business practices are being followed and small businesses are not being unfairly penalized.

Just as a side note, to further complicate the issue, is the shortage of containers our industry is facing. The shortage of shipping containers has hindered the industry's ability to get their products to market. Shipping lines are 'bumping' wood products from ships in order to put on higher value commodities. With a strong U.S. economy an abundant supply of containers were available at a low price as ship lines would look for outbound goods. A weakening U.S. economy has decreased goods being imported and thereby decreased the containers available.

- The euro has strengthened against the Yuan, stimulating record shipments of Chinese goods to the EU, and diverting ships previously bound for the U.S.
- Massive growth in developing Asian countries has caused steamship lines to dedicate more trade lanes within Asia instead of to and from the U.S.

The third challenge I would like to address today is foreign procurement requirements for certified wood. In certain export markets, most notably in Europe and Japan, government procurement policies are requiring that wood products be shown to be from legal and sustainable sources. Private market purchasers are increasingly requesting similar assurances.

Certification often provides an accepted demonstration of legality and sustainability. While there are U.S. hardwood businesses that have been successful in attaining 3rd party certification, this is a complicating factor for most in the industry. Unlike many countries where forest land is controlled by governments, and where deforestation and illegal logging have been identified as issues, US forest ownership and hardwood supply is mainly private. US hardwood production is concentrated east of the Mississippi River but some hardwood species are commercially produced in the West as well. Over 90% of US hardwoods are supplied by private landowners, mainly by small family forest owners with an average holding of less than 25 acres. Most family forests are owned for reasons other that timber production -- as part of a farm, for recreation or other reasons. Thus, certification is generally not something that appeals to small forest owners who will only harvest irregularly, if at all, and perhaps only once or twice in a generation. Hardwood timber operators purchase from hundreds of different landowners each year, usually in small quantities. Much is sold through wood dealers who amass logs from many different sources and merchandize them by species as the market allows. This makes chain of custody tracking for certification challenging if not extremely difficult.

We are working to address this unique problem with 3rd party certificate programs. However, until these obstacles can be addressed the U.S. hardwood industry needs support to assure the legality and sustainability of U.S. hardwoods. Following are some of the key resources to support the industry's record of legality and sustainability:

- U.S. hardwoods are demonstrated through the yearly U.S. Forest Service Forest Inventory and Analysis Program to be abundant and inherently sustainable
- Despite development pressure and cropland needs, USDA data shows that the US hardwood inventory has more than *doubled* over the past 50 years. The annual hardwood growth exceeds removals by a significant margin of 1.9 to one, and net annual growth has exceeded removals continuously since 1952

- A recent independent study of the US hardwood resource concluded that "there can be a high confidence that rights of timber ownership are well-established and respected" while the World Bank ranks the US in the top 10% of all countries for government effectiveness, regulatory quality and rule of law
- U.S. hardwoods are awarded the highest conservation crop rating available under the USDA Environmental Benefits Index

The Hardwood Federation is currently working with members of Congress to address the importance of recognizing the sustainability and legality of U.S. hardwoods, and assure that the small businesses dominating lumber production as well as small landowners do not face an unfair and unwarranted competitive disadvantage abroad.

I would like to emphasize to Committee members the importance of maintaining a healthy export market for the hardwood industry and thank you again for taking the time to understand our export challenges. I hope these insights into our business have left you with a better understanding of the international competitiveness for small hardwood businesses. Before closing, I do want to mention a very important export promotion program our industry currently receives under the Foreign Agriculture Service. This funding recently passed in the farm bill provides small family owned businesses the opportunity to promote their products in the foreign marketplace through the American Hardwood Export Council (AHEC). Without this type of support, these small family businesses would not be financially equipped to cultivate international customers. With a slumping housing market and economy, foreign demand for U.S. hardwoods is essential to maintaining a healthy wood products industry. It is essential to the health of our industry that Congress continue to fully fund and USDA efficiently allocate the Market Access Programs of the Foreign Agriculture Service.

Thank you for your support.

Number of Containers (yearly)	Phyto Cert Costs $50	Phyto Cert Costs $100	NHLA KD*	KD Savings from Phyto $50	KD Savings from Phyto $100
4000	$200,000	$400,000	$83,600	$116,400	$316,400
2000	$100,000	$200,000	$43,600	$56,400	$156,400
1000	$50,000	$100,000	$23,600	$26,400	$76,400
500	$25,000	$50,000	$13,600	$11,400	$36,400
100	$5,000	$10,000	$5,600	-$600	$4,400

*NOTE: KD Costs are $220 monthly for service, approximately $80 monthly for travel, and $20 per KD certificate used.

USDA

United States
Department of
Agriculture

Marketing and
Regulatory
Programs

Animal and
Plant Health
Inspection
Service

4700 River Road
Riverdale, MD 20737

January 29, 2008

Mr. Dam Quoc Tru
Deputy Director General
Plant Protection Department
Ministry of Agriculture and Rural Development
149, Ho Dac Di Street
Dong Da District Hanoi, Viet Nam

Dear Mr. Tru:

We are writing to request that Vietnam accept industry certificates for hardwood lumber, from an Animal and Plant Health Inspection Services (APHIS) approved certification system, in lieu of a phytosanitary certificate. The certification system, developed to satisfy the Australian regulatory standards, is controlled through a Memorandum of Understanding between APHIS and the National Hardwood Lumber Association. The system mirrors the successful seven year old softwood certification program developed for the European Union, and requires the following:

- Kiln drying to less than twenty percent moisture by weight;
- Verification through inspection of the kiln drying process;
- Maintenance of signed agreements with participating facilities;
- Maintenance of a listing, both paper and on-line, of these facilities and the authorized personnel at each;
- On-site inspections of registered facilities' equipment and the skill base of the kiln operator;
- Inspectors that are industry-certified and independent of the treatment facility;
- Industry-certified inspectors must perform inspections each month during which a facility has a shipment scheduled;
- Inspected facilities make files and records available for APHIS inspection;
- Retention of inspection records for three years after the close of the Federal fiscal year in which the inspection occurred;
- Bi-annual audits performed by APHIS headquarters;
- Bi-annual inspections of participating facilities and inspection companies by APHIS inspectors;
- Bundle bands with unique serial numbers for shipment authentication; and
- Random inspections of shipments by APHIS inspectors.

Each facility inspection, both by industry-certified inspectors and APHIS inspectors involves the following:

- Document verification to insure every board foot of treated lumber is accountable;
- Review of kiln treatment records;
- Moisture testing;
- Lot number verification on bundle bands of a representative sample present;
- Review of treated product segregation and inspection practices; and
- Submission of a written report on the facility audit findings and suggestions.

The bi-annual audit performed by APHIS headquarters ensures the industry-certified inspection agencies are as follows:

- Independent of the mills;
- Using industry-certified inspectors; and
- Maintaining proper and current inspection files, records, training, and certification.

The operational training includes the following requirements:

- Kiln calibration;
- Probe placement and numbers;
- Use of moisture meters;
- Recording and filing of product and inspection information;
- Product positioning within the kiln;
- Product storage; and
- Review of shipping and training documentation.

The certification system is dedicated to maintaining the agricultural integrity of our trading partners. We believe industry certificates from the APHIS approved certification system would be instrumental in meeting the demands of Vietnam's expanding markets. We appreciate your consideration of this important issue and await your favorable response.

Sincerely,

Craig T. Fedchock
Assistant Deputy Administrator
Phytosanitary Issues Management
Plant Protection and Quarantine

Testimony of Charles Wetherington

President

BTE Technologies, Inc.

On Behalf of

The National Association of Manufacturers

Before the

House Committee on Small Business

Hearing on

"Small Business Exports in the Current Economic Climate "

Thursday, June 19, 2008

Good morning Madam Chairman and members of the Committee. I appreciate the opportunity to participate in this very important panel on "Small Business Exports in the Current Economic Climate". I am Charles Wetherington, President and Owner of BTE Technologies, a small company headquartered in Hanover, Maryland, with offices in Denver, Colorado.

We have a total of 78 employees and produce a range of medical devices focused on physical therapy, industrial rehabilitation and sports medicine. We have the good fortune to be in a product space where U.S. flagged goods are held in very high esteem in the world marketplace. Exports have been a key part of our company's strategy and success. In this we are not alone. It is critical to small business in the United States that we achieve faster growth in our exports.

BTE Technologies is an active member of the National Association of Manufacturers (NAM) and I am pleased to have the opportunity to testify on behalf of the NAM this morning. The NAM is the nation's largest industrial trade association, representing small and large manufacturers in every industrial sector and in all 50 states. I particularly applaud this Committee's active interest in small business exports because exporting is vital to American manufacturing and to the NAM, which was founded in 1895 U.S. manufacturers to find markets abroad for their products.

Importance of Exports

Last year, U.S. manufactured goods exports were $982 billion, 60 percent of all U.S. exports of goods and services. Services accounted for $479 billion – 29 percent of the total; and agricultural exports were $92 billion – 6 percent.

Exports are vitally important to the U.S. economy – in fact last year they accounted for 40 percent of the growth of U.S. real GDP, offsetting the housing decline. Exports are very important to the manufacturing sector, and by NAM estimates, account for over one-fifth of manufacturing output.

Yet the United States runs a huge trade deficit – a deficiency of exports compared to imports. We have been falling short, and will continue to fall short unless our exports close the gap with our imports. On the import side, we have to ensure that imports are fairly traded, and have to deal firmly with subsidies and other unfair trade practices.

I believe, though, that our biggest trade problem is how to get our exports to grow much faster and allow us to pay for our imports through exports rather than by borrowing more from other countries. We cannot go on running such huge trade deficits. Our deficit did fall last year, as export growth exceeded imports, particularly for manufactured goods, in which the deficit fell nearly $30 billion. For the first four months of this year, the manufactured goods deficit declined another $17 billion. This is still only a modest improvement, though, and much more is needed.

Given the likelihood of continued large imports of oil and of foreign manufactured goods, we need a huge ramp-up of our exports, most of which will have to be manufactured goods. This should be a government priority as we look at the projections for continued growth in a number of major international markets. We need a national export expansion strategy designed to achieve a large and sustained increase in our exports.

There are a number of key factors in the success of U.S. exports over which the government has oversight or control. They are: currencies that reflect market values; multilateral and bilateral free trade agreements that open markets for U.S. goods by bringing down foreign tariffs; the removal of standards and regulatory barriers that limit the sale of U.S. goods in foreign markets; and U.S. government services that assist companies to export their goods.

Importance of Small Business

Before examining these factors, it is important at today's hearing to consider, in light of the export data, how important is small business to that picture? Of U.S. companies that export, over 97% of them are small and mid-sized businesses, yet those companies only represent 30% of the dollar value of all U.S. exports. This can be accounted for by the fact that about two-thirds of all smaller exporters sell to just one country and two-thirds have fewer than five export sales per year.

The Small Business Exporters Association, an NAM member association, calculates that last year, small companies exported over $450 billion worth of U.S. goods and services. When you consider that one of the most difficult parts of exporting for a small company is that first export, those companies that have already learned how should be prime targets for export expansion efforts. If most of the small companies that are making a few sales in one foreign country were to make a few more in that country and /or an equivalent level of sales in a second country, we could probably bring that figure up to $625 billion a year, even without adding any new exporters. That would cut the current trade deficit by about 25%.

Altogether, there are over 220,000 American small businesses that export. This is certainly a remarkable figure – it's tripled in the last 20 years. Yet, there are 26.8 million small businesses in this country overall, which means that over 99% of U.S. small businesses don't export. Recognizing that many small businesses will never export, if the number of small business exporters is increased by half, increasing the percentage from 1% of small businesses to 1.5% and if that new group could become 75% as successful as the current small exporters, then we will have reduced our trade deficit by an additional $170 billion.

So two steps – increasing incremental sales by current small business exporters and increasing the number of small business exporters by half – could eliminate almost half of the U.S. trade deficit of $700 billion.

This kind of a step up in small business exporting would also have a major impact at home. Data show that export-related jobs pay 13-18% more, on average, than non-trade-related ones. And every $1 billion in exports creates more than 9,000 jobs. So another $500 billion in exports equals 4.5 million of these good jobs.

The NAM has made outreach to its small companies with export assistance one of its member priorities. Currently, there is a full time U.S. and Foreign Commercial Service officer posted at the NAM for two years to direct this effort.

BTE Technologies Experience

I would like to take a few minutes to describe our experiences at BTE Technologies. In 2001, after purchasing the company, we diversified in two very important ways. Because the production of capital goods is cyclical, we expanded by offering professional services, in our case, assistance with workers' comp cost controls. This portion of our business has grown dramatically in the United States, to 25 - 30 percent of our revenues, and we are looking to export these services with a pilot project in Italy.

The other change we made was to place greater focus on exports. I am happy to say that, since 2002, our exports have grown ten times. At that time, exports represented three percent of our revenues and now they represent 35 percent. We currently export to 28 countries in the world.

We have used a range of services provided by the Commerce Department's Commercial Service and have found them to be instrumental in our success. We worked with the Baltimore Export Assistance Center, to help us find distributors overseas, conduct background checks on potential customers and agents, and do country analysis identifying markets for our products.

For small companies, these services are essential to success in exporting. Most of us don't have the resources to have large export divisions or offices overseas to ferret out new business.

One of our breakthroughs has been that we have to be there, feet on the ground, once or twice a year in order to maintain the relationships necessary to making repeat sales. That is time-consuming and expensive, but it is essential in our business, and we have found the benefits outweigh the costs in the long term.

Importance of Currency

Absolutely essential to the competitiveness of U.S. goods are currencies that are aligned with market forces. The NAM Board of Directors has long held the policy position that currencies should be market determined, free of government intervention. When the dollar is excessively strong against other global currencies, U.S. goods become expensive in global markets and exports decline. When the dollar has adjusted to a more realistic value, exports grow. This sounds like common sense, but it is a fact too often overlooked in this discussion.

We have just seen this phenomenon occur over the past decade. During the 1997-2002 period, the era of the so-called "strong dollar", the dollar ran up to 25% over its equilibrium value. During this period, the trade deficit spiraled upward and U.S. exports dropped off a cliff.

The dollar peaked in 2002 and began the readjustment that we are still seeing today. There is, of course, a lag in the effect of currency on exports, but the export growth we are now seeing is a direct result of this readjustment of the dollar. The NAM hears every day from companies who say the value of the dollar has allowed them to be competitive internationally again and export more. Many companies, particularly small and mid-sized, say that the primary reason they are doing well at the present time is their export performance.

Multilateral and Bilateral Free Trade Agreements

I recognize that there have been concerns raised about our free trade agreements, but I must say from the perspective of a small company trying to export, they have been very important for us. The United States is already open to the world; it has been for decades. It's much of the rest of the world that has higher tariff and non-tariff barriers to U.S. exports. Our free trade agreements have opened foreign markets to U.S.-made goods.

The NAM has looked at the data and it confirms how important these agreements are to U.S. manufacturers. Our manufactured goods trade deficit with our free trade partners is a small fraction of the total and in fact is smaller today than six years ago. The manufactured goods deficit with all our free trade partners together – NAFTA, CAFTA, and all the others – was $34 billion in 2001 and $27 billion in 2007. That is a 20 percent improvement, while our manufactured goods deficit with the rest of the world - with which we have no trade agreements - grew by $200 billion – up 70 percent. The contrast between our trade with our trade agreement partners and the rest of the world is so striking that manufacturers hope we can continue opening markets with new agreements.

Standards and Regulatory Issues

One of the big hurdles we at BTE face in exporting are regulatory and standards barriers. A good example is the Medical Device Directive in the European Union (EU). One would think the EU should be about the easiest place after Canada and Mexico for a U.S. company to export, and in many ways it is.

But this directive has made it very expensive for us to get certified. And we are seeing signs that others are starting to follow the EU's lead. In Russia, for example, there has been a changeover in the Health Ministry and we have reason to believe there may be a change coming in the regulations that will require our recertification. Last year, we spent $25,000 to be certified there for a $200,000 sale. That may not sound like a lot, but if we have to do this on an annual basis, there will be no profit in the sales for us.

How could the government help with this? Several ways: first, work hard to develop some level of standardization. This might include negotiating global standards in a range of products requiring these kinds of certifications, or reaching agreements for reciprocity between certifying agencies. This is especially helpful for small companies, that we are able to make our products to one set of specifications that can be sold globally. Multiple standards greatly increase the costs of production and this could help many of us, large and small, who export.

Second, it would be very helpful if the Commerce Department were able to help alleviate the problem faced by small companies when required to do duplicate testing and certification overseas because the usual U.S. testing process is not accepted by the importing country.

U.S. Government Services to Exporters

Finally, let me point out that the U.S. export promotion strategy has for a number of years been one aimed at increasingly shifting the cost of various marketing research and promotion programs to users of trade missions, market research, participation in trade fairs, and the like. The U.S. approach has taken a step toward making promotion services more attractively priced for smaller companies, however, with the new fee schedule implemented May 1st of this year

Even this welcome step, though, leaves the U.S. program in contrast to the support that other governments provide. For example, one NAM member company relayed this story with regard to their competitors' government assistance:

> "In our industry (packaging machinery) participation in international trade shows is key when entering new markets. Currently our members have to pay a significant amount of money to participate in these events. However we know that competitors from other countries, mainly European, have strong support from their governments based on trade promotion programs. This is leaving our members in a weak position to compete internationally. We consistently find country pavilions at international trade shows that are heavily subsidized by their governments. We have found this mainly from European countries including Spain, Italy, UK and Germany. We have learned that some of these countries pay up to 70% of space, decoration, freight and staff transportation for companies to attend a trade show."

This member also provided a copy of a new UK Government program that provides funding to British companies that seek to enter new markets, underwriting much of the cost of participating in trade fairs or undertaking other export marketing steps to expand their overseas sales. In BTE's experience, we have spent over $100,000 in the last 4 years just to attend MEDICA, the annual tradeshow that covers our field.

My attention was also drawn to an Australian news report earlier this year stating that Australian government grants for export market development will be boosted by $50 million to a total of more than $200 million. Australian Trade Minister Crean, in announcing the increase, said that Australia has to engage much better, "with the fastest growing area of opportunity – world trade." I note that Australia's exports of manufactured goods last year were about $60 billion – 1/16th the amount of U.S. manufactured goods exports, so Australia's $200 million program is the equivalent of announcing a $3.2 billion U.S. program.

So while U.S. export promotion programs provide little if any financial assistance to exporters, our competitors have a totally different philosophy about promoting exports. In doing some research for my appearance before the Committee, I have to confess I was startled to learn that it was not only our competitors who were able to provide financial incentives and support to enter trade shows and seek new markets, but also the U.S. Department of Agriculture.

Under the Foreign Market Development Cooperator Program (FMD) and the Market Access Program (MAP) agricultural trade associations engaged in market development and export promotion activities for both generic and branded products are eligible for a range of supports. As part of the MAP, for example, the Export Incentive Program (EIP) provides reimbursement to qualifying small companies for airfare to foreign trade shows, trade show participation costs such as rental of space and equipment, promotional and advertising costs, and packaging costs if necessary to meet importing country requirements. This is quite similar to what is characteristic of the support available to many foreign firms. However, under current programs and funding, none of this is available to U.S. manufacturers seeking to expand their exports.

In addition, we need promotion assistance and resources both in Europe and in China, as well as in other rapidly-growing markets such as the Middle East, India, Brazil, etc. But those resources simply are not available. The NAM believes that with the present value of the euro, we cannot afford to overlook the opportunity to get more U.S. manufacturers to export to more European countries. The NAM is teaming up with the Commercial Service to utilize our outreach resources along with some of Commerce's programs to help find European customers and distributors in what we call "Europe NOW" in the hopes of generating more U.S. export marketing to Europe.

The NAM also suggested to the Commerce Department a far-reaching set of ideas for ramping up export promotion in China, but these ideas are outside the scope of present resource availability. They include establishing American Trade Centers, utilizing the Export Trading Company Act to form China Trading Companies in which groups of U.S. companies would establish marketing and distribution centers, use of creative financing, and the like.

If a sudden increase in priorities and resources for export promotion were to become available, one program we believe could be ramped up very quickly is the Market Development Cooperator Program (MDCP). This program offers grants to vertical trade associations or other groups for programs or promotional offices designed to enhance exports. The grants fund up to one-third of the cost and last for three years. The MDCP program has been a real success, even though it is starved for funds. I understand that Commerce's analysis has shown that for every federal dollar invested, $100 in exports has been generated. Since 1997, this program has generated $2.65 billion in U.S. exports, with an outlay of $20 million or less over that time period. I estimate that amount of exports generated additional tax revenue to the U.S. government amounting to almost $100 million – not a bad return on the taxpayer's investment – especially since this is seed money for what become self-sustaining promotion centers.

Consider, for example, the experience of the Association for Manufacturing Technology (AMT), an NAM member association representing the machine tool industry. More than 80% of its members are small or medium-sized companies. With the help of an MDCP grant, AMT opened a center in Shanghai, China, which is now one of the world's largest markets for machine tools. The Center provides exhibition, meeting and storage space, as well as services such as translation, invoicing and sales for companies that otherwise could not afford to have their own offices in China. Since 2004, the Center has generated $41 million in sales of U.S.-made machine tools. The MDCP grant totaled $225,100.

The current budget for the MDCP is $2 million. When the MDCP was founded in the early 1990's, its budget was $2 million. Fifteen years later its budget remains the same – in fact the program is so starved for funds that it cannot make any new grants in 2008, although there is hope that some new grants may be possible in 2009. With such a record of success, it is our view that this is a program that should be greatly expanded. By contrast, in 2007, the U.S. government spent $240 million for two generally comparable programs that promote agriculture exports. A comparably funded program for manufactured goods, which are 10 times as large as agricultural exports, would have been $2.4 billion – 1200 times larger than the actual budget of $2 million. It would also be useful to see programs that focus on promoting U.S. products and industries that are highly competitive and have superior reputations globally.

I again want to make clear that my comments are not intended to be a criticism of promotion funds for U.S. agricultural goods. My remarks are meant to highlight the paucity of funding to promote manufactured goods exports and to illustrate what a comparably funded Commerce program would be, scaled to the size of exports.

As another example of a promotion program NAM members think could be expanded quickly if there were additional funds is the Foreign Buyers Program. This program promotes foreign buyer attendance at U.S. trade shows, and is an attractive way of promoting small and medium-sized firms' products because these firms don't have to travel overseas to exhibit their products. The prospective buyers come here, to U.S. shows at which the U.S. companies are already exhibiting. Only 20 shows per year qualify for the program, but given its success, I believe it should be considered a key part of any expanded export promotion program. In addition to expanding the number of eligible U.S. trade shows, it would also be helpful to provide special and expedited visa processing for foreign buyers.

Export Finance

Another key factor in export success is export finance and credit. Agencies such as the Export Import Bank, OPIC and the Small Business Administration offer valuable services and products to U.S. exporters. Each of them also has programs specifically geared to small companies and their special needs. For example the ExIm Bank, under current chairman Jim Lambright, has instituted a new department headed by a senior vice president solely devoted to outreach and service to small companies.

My company has taken advantage of these services at ExIm and it has made a significant difference in a number of our recent sales. I strongly encourage you to continue support for these important financing opportunities for small companies. However, it would be helpful if the rates charged by ExIm reflected our efforts in managing risk. Premiums paid to ExIm are fixed based on the dollar amount of protection and are not indexed to our loss experience, either favorably or unfavorably.

Customs "10+2" Rule

Although we are today discussing export issues, I want to highlight for the committee one current customs issue of great importance. Many manufacturers, including small manufacturers, are able to maintain their global competitiveness by importing some of their inputs. These are assembled here, often with domestic parts as well, and then exported to foreign customers.

Customs and Border Protection (CBP) has proposed a new filing obligation for importers before merchandise is even loaded into a container. It would mandate the submission of an Importer Security Filing ("ISF") 24 hours prior to container loading. Industry is very concerned that this new requirement would alter the way many companies do business. In addition, the NAM has determined that there will be substantial additional costs for U.S. manufacturers – as much as $8.5 billion per day - that were not adequately assessed by CBP.

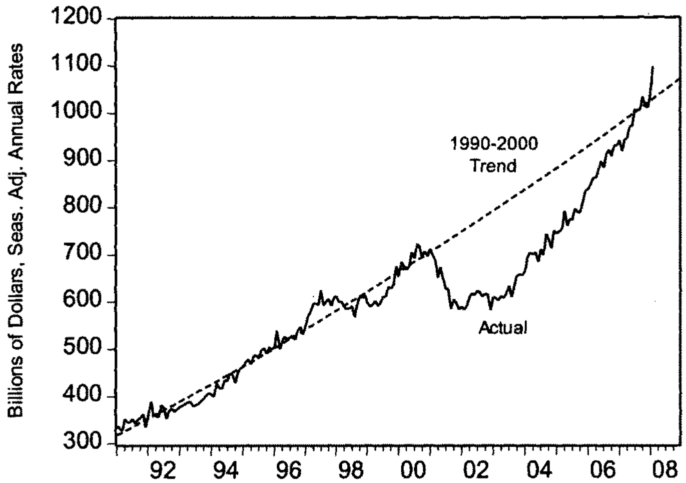
The NAM fully supports initiatives to ensure national security and has made a number of proposals to CBP that could achieve the desired goal while addressing the concerns of industry. These include: further analysis of the effect of this proposed rule on the movement of shipments and further guidance on implementation; conducting a prototype of the proposed rule with importers all of sizes from all sectors participating to assess the efficacy and costs followed by a phase-in period; and recognition of companies participating in the CTPAT program. I encourage the Committee to look into this issue as an important one affecting U.S. companies' global competitiveness.

Conclusion

In conclusion, Madam Chairman, I would like to thank you and the members of the Subcommittee again for this opportunity to testify on such an important issue. We are in a globalized world. We don't get to vote yes or no on this. What we can do, however, is to put ourselves in a better position to avail ourselves of the global opportunities in a way that promotes the standard of living of all Americans. Certainly a determined promotion effort that would increase the participation of American small and mid-sized companies in world markets must be an important part of this endeavor.

Thank you, Madam Chairman.

EXHIBIT 1
U.S. EXPORTS OF MANUFACTURED GOODS
Trend and Actual



Source: U.S. Census Bureau, Seasonally Adjusted by NAM, employing Census X-11 seasonal adjustment program

NATIONAL ASSOCIATION OF MANUFACTURERS

The importance of paying attention to U.S. exports is obvious by looking at this exhibit. Exhibit 1 shows the 1990-2000 growth trend of U.S. exports of manufactured goods and depicts how badly we have fallen behind for the last six years or so because of the severe misalignment of global currencies. Only in the last few months have we returned to the growth path we should have been on.

"Opening the World of Export Opportunity to U.S. Small Businesses"

Testimony by Daniel Griswold
The Cato Institute
Before the House Small Business Committee Hearing
On "Small Business Exports in the Current Economic Climate."
June 19, 2008

Chairwoman Velázquez, Ranking Member Chabot, and other members of the House Small Business Committee, thank you for inviting a scholar from the Cato Institute to testify a today's hearing on "Small Business Exports in the Current Economic Climate."

Expanding Exports a Bright Spot for Economy

Globalization is a fact of life in 21st century America, and America's small businesses should be allowed to take full advantage of its opportunities. Since 1990, the share of U.S. GDP that Americans have earned abroad though exports of goods and services and earnings on foreign investment has jumped from 12 percent to 17.4 percent. That is the highest ratio of exports to GDP in our history. Americans have never earned or spent a higher share of our income in the global economy than we do today. Three quarters of the world's spending power and 96 percent of its people live outside the United States. This represents a huge potential market for U.S. producers in general and hundreds of thousands of American small businesses in particular.

Our growing engagement in global markets is one of the bright spots in the U.S. economy today. As the housing and financial sectors have tanked, exports and earnings on foreign investment are booming. While the economy as a whole has slowed dramatically, exports of goods and services jumped by 12.6 percent last year, and earnings on U.S. investments abroad soared by 20 percent. The healthy growth in exports has continued into the first quarter of this year, according Commerce Department data released just this week. That expanding opportunity to serve foreign markets has allowed U.S. companies, including small businesses, to better weather the current slowdown.

Driving this increase in demand for U.S. exports has been strong growth abroad, especially in emerging markets. The global poverty rate has been cut by more than half since 1981, with much of the credit is due to market-reforms in developing countries, including unilateral trade liberalization. Hundreds of millions of people have joined the rising middle class in China, India and the more reform-minded countries elsewhere in Asia, Latin America, Africa, and the Middle East. American companies and workers are reaping the benefits of expanding global trade and development.

Small Businesses Reaching Global Customers

Opponents of free trade dismiss it as a policy that only favors Fortune 500 companies. That claim is becoming more false every day. A quarter of a million U.S. companies export to foreign markets, the large majority of them small and medium-sized enterprises

(SMEs) that employ 500 or fewer workers. According to the U.S. Chamber of Commerce, more than 230,000 SMEs now account for nearly 30 percent of U.S. merchandise exports. The number of such companies exporting has more than doubled since 1992.

This growth has been propelled not only by the expansion of global trade generally but also by technological developments especially favorable to smaller exporters. On the cutting edge of this development has been the spread of the Internet and e-commerce. There are now more than 1.3 billion Internet users in the world today, and the number is growing rapidly. Of those, 85 percent shop online. With the assistance of delivery services such as FedEx and UPS, small businesses are able to reach global markets without the daunting expense of establishing sales teams and distribution networks in foreign countries. The Internet has also facilitated the slicing up of global supply chains, creating more opportunities for smaller U.S. companies to find profitable niches as suppliers for larger multinationals.

One of the most important and fastest growing markets for America's small-business exporters is China. Last year, Americans exported $65 billion worth of goods to China, making it our third largest customer for U.S. goods in the world, behind only our NAFTA partners Canada and Mexico. Since China's entry into the WTO in 2001, U.S. goods exports to China have grown at an annual compound rate of 22.6 percent. That is triple the growth rate of U.S. exports to the rest of the world. China is now a major market not only for U.S. agricultural products, but also for plastic materials, chemicals, industrial machines, semiconductors, telecommunications equipment, and computer accessories.

Small and medium-sized U.S. companies are basking in this export success. In 2004 (according to the most recent figures we have), 19,210 SMEs in the United States were exporting to China. That is more than six times the number that were exporting in 1992. The share of U.S. companies exporting to China that are small or medium-sized enterprises has grown during that time from about three-quarters to more than 90 percent. SMEs accounted for 35 percent of U.S. merchandise exports to China in 2004, a higher share than their 29 percent share of exports overall. Board any flight from the United States bound for China and you will probably be sitting near somebody representing a small-sized U.S. company heading off to buy and sell in the world's fastest growing major market.

Despite loud complaints from certain U.S. producers, the undervalued yuan does not appear to have dampened the ability of U.S. companies—large, small or in between—to sell in China's expanding market. If Congress enacts legislation that ignites a trade war with China, small U.S. exporters will be among the front-line casualties.

An Agenda to Promote Small Business Exporters

What can Congress do to help promote the ability of small U.S. companies to compete successfully in global markets?

Congress should seek to lower trade barriers to our own market so that U.S companies can access raw materials, industrial supplies, and capital machinery at the lowest possible global prices. A more open U.S. market also feeds back into more export opportunities in foreign markets. Foreign producers who can sell more freely in the U.S. market thus earn more dollars in which to spend on U.S. products and services for export. U.S. producers made more efficient by facing global competition are better able to gain and expand market share abroad. And reducing our own trade barriers sets a good example for other countries and helps to set the stage for trade agreements that also lower trade barriers abroad.

Far from calling a trade "time out," Congress should work with this administration and the next to approve comprehensive trade agreements to abolish trade barriers and promote two-way foreign investment. Agreements to reduce trade barriers and facilitate investment certainly do benefit big U.S. multinationals—and no apology is necessary for that—but they benefit smaller U.S. companies just as much if not more. Those agreements benefit smaller U.S. exporters in three important ways.

First, trade agreements help to reduce red tape and increase transparency. Small businesses lack the resources and foreign business partners available to large companies to navigate through opaque customs and legal systems to reach their customers. Numerous fees and other non-tariff barriers that can be no more than a nuisance to large multinationals can be deal-breaker for small companies. Trade agreements streamline rules, reduce non-tariff barriers and provide arbitration procedures so that even small U.S. exporters can successfully participate in foreign markets. As a new study by my Cato colleague Daniel Ikenson found, improving "trade facilitation" can do more to bolster U.S. trade than actual tariff cuts.[1]

Second, trade agreements open up opportunities for small U.S. exporters to compete for foreign government contracts. Previous and proposed trade agreements guarantee U.S. companies a fair shake at the important government procurement market. Such agreements can help to lower the threshold at which contracts must be put out for competitive bid, ensuring that even small U.S. companies can be part of the process. Some of those contracts—for roads, schools, clinics, distance learning, and medical equipment, for example—can be ideally suited to smaller U.S. companies.

Third, trade agreements lower tariffs and other barriers to trade that are more difficult for small exporters to work around. Many large multinationals have the option of relocating production facilities to foreign affiliates, circumventing border barriers. Most SMEs, in contrast, export from a single domestic location. The reduction and elimination of tariffs allows them to export from their domestic facilities without facing barriers that can often be discriminatory and prohibitive.

Opportunities in South Korea, Panama, and Colombia

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[1] Daniel Ikenson, "While Doha Sleeps: Securing Economic Growth through Trade Facilitation," Cato Trade Policy Analysis no. 37, June 17, 2008, available at www.freetrade.org.

The 110th Congress has the opportunity right now to enact three important trade agreements—with Colombia, South Korea, and Panama—that will help small U.S. companies boost their exports. All three of these agreements would reduce and eliminate tariffs on U.S. exports to each of those markets while guaranteeing fair treatment for U.S. companies that investment abroad. They would streamline customs procedures, enhance transparency, and open up government procurement markets for bid by U.S. companies of all sizes. These agreements would allow thousands of small business in the U.S. to export to these markets for the first time.

U.S. small businesses are already exporting to all three of those markets, although they currently face trade barriers that are significantly higher than those imposed by the United States.

- In South Korea, nearly 17,000 small and medium-sized U.S. companies already export to what is America's seventh-largest market abroad. SMEs account for almost a third of U.S. exports to Korea. The agreement would be especially helpful for U.S. exporters of electronics, 94 percent of them SMEs.
- In Panama, 5,600 U.S. companies are already exporting there, with 80 percent of them small and medium-sized enterprises. Since 2002, U.S. exports to Panama have been growing more than twice as fast as exports to the rest of the world.
- In Colombia, 7,705 small and medium-sized U.S. companies are already exporting, accounting for 35 percent of American goods sold in that country. Almost all Colombian goods already enter the United States duty free because of the Andean Trade Preferences Act. The U.S.-Colombia trade agreement would eliminate Colombian tariffs that currently range as high as 35 percent, delivering the "level playing field" so many members of Congress say they want. According to the U.S. International Trade Commission, the agreement would boost U.S. exports to Colombia by $1.1 billion a year. American small businesses are ready to claim a big slice of that expanding pie.

Say 'No' to Trade Barriers and Export Subsidies

What U.S. small businesses do not need are higher trade barriers to our domestic market or more federal subsidies to supposedly promote exports or foreign investment. Punitive tariffs against a country such as China would threaten to drive up costs for U.S. small businesses that import intermediate products from that country. Escalating trade tensions would also jeopardize export opportunities in growing markets abroad. Antidumping orders and other tariffs against such imports as steel or agricultural commodities drive up costs for domestic producers, many of them small businesses, who use those imports in their final products.[2] For the same reasons, a weak U.S. dollar, while benefiting certain

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[2] For the impact of steel tariffs, see Daniel Ikenson, "Ready to Compete: Completing the Steel Industry's Rehabilitation," Cato Trade Briefing Paper no. 20, June 22, 2004, pp. 5-6; for the impact of agricultural trade barriers on U.S. producers, see Daniel Griswold, Stephen Slivinski and Christopher Preble, "Ripe for Reform: Six Good Reasons to Lower U.S. Farm Subsidies and Trade Barriers," Cato Trade Policy Analysis no. 30, September 5, 2005, pp. 4-6.

U.S. exporters, has driven up production costs that U.S. small businesses pay for imported energy, parts and capital machinery.

Nor do U.S. small businesses need a larger share of federal subsidies for international trade. While small and medium-sized companies do qualify for such programs as the Export-Import Bank and the Market Access Program, they account for a small dollar share of total federal support.

U.S. companies do not need federal subsidies to compete effectively in global markets. Our research at Cato has shown that U.S. exporters have outperformed their counterparts in Great Britain, Germany, France, Canada and Japan even though the share of U.S. exports receiving government support is much lower than exports from those countries. Most U.S. export subsidies go to firms that do not experience subsidized competition abroad. [3] U.S. and global markets are currently awash in private capital ready to finance new trade and investment opportunities. Federal export subsidies do not promote more exports but only reshuffle the export pie in favor of larger U.S. companies, crowding out smaller exporters.

If Congress and the administration want to increase opportunities for U.S. small businesses to compete and thrive during the current, challenging economic climate, they should work together to reduce barriers to international trade and investment whether in the United States or in other countries.

[3] Aaron Lukas and Ian Vásquez, "Rethinking the Export-Import Bank," Cato Trade Briefing Paper no. 15, March 15, 2002.

Testimony of Dr. Aaron K. Chatterji, Ph.D.

Assistant Professor at the Fuqua School of Business, Duke University and Fellow at the Center for American Progress, Washington D.C.

U.S. House of Representatives, Committee on Small Business
June 19th, 2008

"Small Business Exports in the Current Economic Climate."

Chairwoman Velazquez and members of the committee, thank you for inviting me to testify today about this important economic policy issue, one that, with the notable exception of the work of this committee, does not always get the attention it deserves.

My name is Aaron Chatterji and I am an assistant professor at Duke University's Fuqua School of Business, where my research focuses on entrepreneurship and small business. I am also a Fellow at the Center for American Progress in Washington D.C., where I am an economic policy adviser, working on issues related to the intersection of business and public policy.

In my view, American small businesses are not just the backbone of our economy, but also a lynchpin in our broader society, creating millions of jobs and anchoring our local communities. In the various places I have lived across the country, whether in Upstate NY where I was born and raised, northern California where I attended graduate school, or the Research Triangle in North Carolina where I live today, I have seen firsthand how the fortunes of small businesses can be a critical variable in the overall economic health of a region. I have also observed that immigrants to our country, like my parents, have often started small businesses as a means of moving up the economic ladder and providing a better life for their children. Finally, I have studied how global economic forces are changing the competitive landscape for our small businesses, presenting new threats but also new opportunities.

However, in current economic policy debates, American small businesses are often an afterthought. Some recommendations seem to be driven by the assumption that what benefits the Fortune 100 will automatically trickle down to America's 26 million small businesses. I think the real story is more complicated than that and I believe that federal, state, and local governments have numerous tools at their disposal that can help small businesses grow and prosper. Of course, the widely admired entrepreneurial initiative of America's small business owners will be the most important driver of success. The difficult challenge for government policy will be to harness that initiative rather than hinder it.

In the spirit, let me offer a few thoughts on the issue being discussed here today, the export outlook for American small business. While there are many reasons to be concerned about the future of the American economy, rising energy costs, the turmoil in the mortgage market, an increase in the unemployment rate, American exports have fared quite well, in part due to the declining value of the U.S. dollar. The weakening dollar makes our goods cheaper to foreigners, and as a result, American exports are up 16.6% compared to last year according to Commerce Department data from January 2008. This is a bright spot in our economy with the potential to make a dent in our $700 billion trade deficit and has accounted for a large part of our economic growth in recent quarters.

Upon closer inspection of the data however, we might be concerned that the majority of American businesses, specifically small businesses, are not benefiting as much as they could be from the favorable climate for exports. According to the Small Business Exporting Association, 240,000 of our small businesses are exporting, accounting for $450 billion in value. But these businesses represent a tiny fraction, less than 1% of all small businesses. Furthermore, over 60% of the exporting small businesses are selling to only one nation, with the most popular destinations being Canada and Mexico. In total, our small businesses account for 29% of the total value of all exports, and that number, according to various sources has stayed relatively stable over the last few years. On the other hand, we have seen double digit increases in the overall value of exports, from $1.4 trillion to $1.6 trillion, an increase of 12% in 2007. This followed another 12% increase in 2006, according to the Commerce Department.

So, while we might hear encouraging statistics about the percentage of exporters that are small businesses, we should also look at the percentage of total value accounted for by smaller firms. Also, we should closely examine those industries where small businesses make up the majority of firms, like the 94% of machinery manufacturers and 93% of computer producers.[1] Interestingly, in some of these industries, including lumber and textiles, we currently see a decline in exports compared to 2007.[2] While we can never expect complete parity with large businesses in terms of export value, these numbers indicates that there is room to grow. We have a huge interest in promoting exporting among small business, because of its association with higher wages and more steady firm performance.

While I should caution you that there are several caveats and exceptions embedded in these data, taken together with the current economic climate, they indicate that we should consider policies to aid U.S. small businesses in accessing foreign markets. Let me briefly conclude by describing a few of the challenges faced by small business and potential policy responses.

The first challenge is a general lack of awareness on the part of small business as to the opportunities to do business abroad. Imagine an entrepreneur who manages a small company, and only reads about the competitive threats from foreign economies, rather

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[1] Data from Small Business Administration (sba.gov)

[2] U.S. Census, U.S. Bureau of Economic Analysis, June 2008

than the huge potential market for her own company. With so many day to day business needs, most business owners simply do not think about the possibility of exporting.

However, the opportunities for doing business abroad are only increasing. Large markets such as China and India are well suited for our small businesses because small businesses in these developing nations often lack the technical sophistication to supply larger firms. For just one example, think about the growing Chinese airline market and how important this market could be to American machine tool manufacturers.[3] Emerging markets all across the world will be growing and liberalizing, and these developments present huge opportunities for U.S. small business if we can improve our trade promotion initiatives.

The trade promotion initiatives at all levels of government should be better coordinated and ought to provide practical and clear information about foreign markets and cultures, concrete steps to begin the process of exporting, and additional services to those needing more information. Many people have said this before, but I want to add one insight from my own research and the academic literature on entrepreneurship. Entrepreneurship is a highly social process. Most small businesses are not founded by two guys in a garage. Rather, prospective entrepreneurs rely on their own social networks for advice, capital, and identifying new business opportunities. Immigrant entrepreneurs in particular have already established strong business links to their native lands, and could be leveraged to increase U.S. exports to a wide variety of countries. I believe that our trade promotion assistance programs could do a better job of taking these factors into account, perhaps identifying key small business owners across the country to act as conduits between the government and the 99% of small businesses that do not export.

The second challenge facing small businesses looking to export is the transaction costs associated with selling goods abroad. Custom fees, physical presence requirements, and other costs of doing business tend to hurt smaller firms more than large ones.[4] Innovations in both the private and public sector in recent years have lowered these transaction costs. The rise of the Internet, and more specifically e-commerce, has allowed small businesses to expand their reach globally. For example, the Associated Press reported on an antique coin company in Holland, Pennsylvania that saw its sales to foreigners grow by 65% in 2007.[5]

While advances in technology have dramatically lowered the costs of connecting American small businesses and foreign customers, small businesses still often find it costly to do the due diligence required to screen potential buyers. Social networking tools and cheap communication methods like instant messenger and Skype can help to build

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[3] Fredenberg, Paul."Are we losing the China market?" American Machinist, June 11th, 2008 (http://www.americanmachinist.com/304/Issue/Article/False/80860/Issue)

[4]Testimony to the Committee on Foreign Affairs in the U.S. House of Representatives, James Morrison, Small Business Exporters Association (http://www.nsba.biz/docs/sbea_testimony__hfac__24_apr_08_final.pdf)

[5]"Weak dollar helping some web businesses." The Associated Press, Oct. 30, 2007 http://www.msnbc.msn.com/id/21548226/

these relationships[6], but there is still no substitute for face to face meetings. The U.S. Export Assistance Center offers the gold key service which helps efficiently match small businesses with pre-screened customers abroad. The Export-Import Bank has an insurance program to guard against the risks of doing business abroad as well. These programs, especially gold key, seem to be well received and should continue to be evaluated.

Finally, let me also make what may sound like a personal appeal, but actually has broader implications. We need better data on small businesses. This will not just benefit researchers, but also policymakers, who will be better able to separate out real trends from statistical artifacts. One example is how we account for service exports, which do not seem to be accurately captured in the current data.[7] We might be missing a large percentage of small business exports, in areas like financial and technology services. For example, the New York Times reported earlier this year on a small investor relations firm, MBS Value Partners, which is finding that midsize European businesses are interested in their services because of the declining dollar. If we could accurately capture service exports, we might find a vastly different picture of small business exporting, requiring different policy responses.

In conclusion, we all agree that small businesses are a critical part of our economy and a tremendous driver of job creation and economic growth. With so many Americans working for small businesses, and so many communities dependent on them, the goal of increasing exports for these firms should be a top priority. Moreover, given current economic conditions, it seems that the time is right to enact policies to help American small businesses expand their scope globally. If we can succeed in increasing the number of small businesses that export and increase the number of countries they export to, we will have a stronger, more resilient economy. By refining our trade promotion activities, lowering the costs of doing business abroad, and increasing our understanding of the reality behind our imperfect data, I believe we can achieve this goal.

Thank you for inviting me and I will take any questions you might have at this time.

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[6] Bandyk, Matthew. "Tips for Small Businesses Looking Abroad." U.S. News and World Report, February 22nd, 2008
(http://www.usnews.com/articles/business/small-business-entrepreneurs/2008/02/22/tips-for-small-businesses-looking-abroad.html)
[7] Testimony to the Committee on Foreign Affairs in the U.S. House of Representatives, James Morrison, Small Business Exporters Association
(http://www.nsba.biz/docs/sbea_testimony__hfac__24_apr_08_final.pdf)