

**ECONOMICS:** US PERSPECTIVES—NOVEMBER 12, 2010

# US Must Woo Multinationals for Healthier Trade Balance

■ **Joseph G. Carson**

US Economist and Director—Global Economic Research, (212) 969 6886

In recent months, several major multinational companies announced plans to boost investment in the US. We think these moves may mark the start of a shift in global investment, production and trade patterns. But more incentives are needed to attract multinational manufacturing to the US, which could go a long way toward reducing the trade deficit.

The dynamics of global trade are changing rapidly. Domestic demand growth in the US is being outpaced by overseas markets. US manufacturing is benefiting from improved productivity and lower unit labor costs relative to its key trading partners. And a more competitive dollar makes US exports even more attractive. Global conditions are aligned for a steady and sustained reduction in the US trade deficit in the coming years.

But these trends will only translate into a healthier trade balance if multinational companies—both US and foreign—fully exploit the advantages of turning the US into a production base for exports or import substitution. Indeed, US multinational companies alone ran a \$172 billion trade deficit in 2008 (**Display 1**).

We think these companies, along with their non-US peers, have the capital and operational scale to trigger changes in global investment, production and trade

patterns. The good news is that important changes already appear to be unfolding.

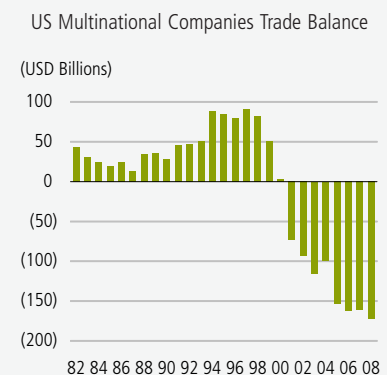
## New Investment Initiatives in US

In recent months, several major US and foreign multinational companies have announced plans to increase investment in the US, including some brand new “greenfield” facilities. The list of US-based companies includes Intel, Global Foundries, Caterpillar and GM, along with international household names such as Samsung of Korea as well as BMW and Volkswagen of Germany.

Some US-based firms are also beginning to export more from their US plants. But surprisingly, the key driver of US export growth in recent years has been US companies that are not multinational groups.

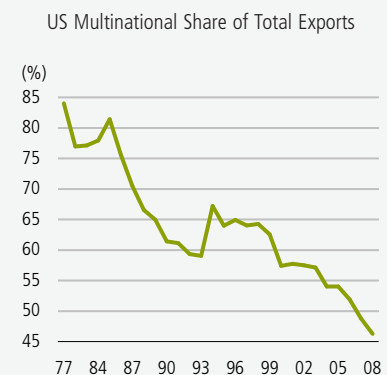
According to a recent report from the Bureau of Economic Analysis, exports by US multinational companies accounted for

Display 1  
Large US Firms Run Big Trade Deficit



As of December 2008  
Source: Haver Analytics and AllianceBernstein

Display 2  
Export Share of Top Companies Plunges



As of December 2008  
Source: Haver Analytics and AllianceBernstein

46.3% of all products shipped abroad in 2008, down 2.5 percentage points from 2007 (**Display 2**). This represented the lowest share since statistics on multinational trade were first collected in 1977. To put this shift in context, 10 years earlier, US multinational companies accounted for two-thirds of US exports, and in the early 1980s the share reached as high as 80%.

Importantly, one reason for the declining export share decline of US multinationals is because smaller and mid-sized firms are exporting more products to an increasing number of countries. That's a positive development for the US trade balance, and one that we expect to continue. But export growth of US multinationals has trailed other US firms by a wide margin. According to our analysis, exports of US multinationals have gained 3% each year on average over the past decade compared with 12% growth of other companies.

Why has export growth been so much slower for US multinationals? Perhaps multinational groups have large operations overseas which they use to meet foreign demand instead of shipping from the US? This is a plausible explanation, although most overseas units of US multinationals are in high-cost countries and most of the incremental demand has come from emerging markets.

### Efficiency Should Be a Magnet

Whatever the reason, we think US multinationals will increasingly find good strategic incentives to produce more for export from the US. For example, US manufacturing is extremely competitive and efficient, with average annual productivity gains over the past decade of about 5%. That's well above the average of other major industrialized economies and only topped by two countries, Korea and Taiwan.<sup>1</sup> In addition, over the same period, US unit labor costs in manufactur-

ing have fallen, when compared with the global average of industrialized economies, as wage growth stagnated (**Display 3**). The decline is even larger when the correction in the US currency is included.

These efficiency improvements, along with the sheer size of the US market, should be a magnet for non-US multinationals as well. We think international companies with significant sales in the US of products manufactured overseas will find increasingly compelling reasons to boost production and investment in the US.

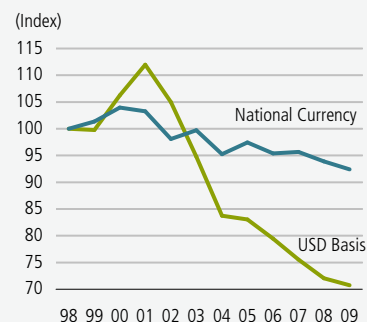
Even now, affiliates of foreign companies account for nearly 30% of all US imports, according to BEA. Of those imports, 80% represent intra-firm sales between the parent company and the US subsidiary. Companies no longer operate within the confines of national boundaries, and many international firms have much to gain by shifting more production to the US. It would help mitigate the impact of currency fluctuations and eliminate transportation costs. There are significant nonlabor costs savings to be captured as well because US manufacturing tends to rely more on relatively cheap natural gas for its key energy source, while European and Asian producers depend more on oil.

### US Tax Regime Remains a Problem

Many international companies are probably deterred from investing in the US because of an unfavorable tax regime. The US corporate tax rate is among the highest of OECD countries, although it tends to have more generous allowances for depreciation of equipment and structures that helps to reduce effective marginal tax rates. Still, we think the US could do better by offering more permanent investment incentives to attract more capital, or at least, to signal to multinational companies that the tax rate is not going to rise further in the near future.

Display 3  
US Manufacturing Has a Cost Advantage

US Manufacturing Unit Labor Costs Relative to 14 Competitors



As of December 2009  
Source: Census Bureau and Haver Analytics

In our view, recent moves by multinationals in the US mark the very early stages of a shift in investment, production and trade patterns. For the US to benefit from these changes, it will at least need to provide a stable set of tax rules—possibly along with a sweetener—to attract new capital, investment and technology.

Of course, multinational companies don't look at trade balances to run their businesses. But for policymakers, trade deficits reflect important investment and production patterns that could have a huge and enduring impact on employment if not reversed.

Eliminating the deficit of US-based multinational operations would cut the US trade deficit by a third, and we hope lawmakers understand just how important it is to make it easier for these companies to operate in the US. Discussions on tax policy in the coming months would be a good place to start drawing up better incentives that will position the US to benefit from the transition in global trade flows and promote a healthier balance of imports and exports. ■

1. The international comparison of manufacturing productivity published by the US Department of Labor does not include China in its calculation.

---

The information contained here reflects the views of AllianceBernstein L.P. or its affiliates and sources it believes are reliable as of the date of this publication. AllianceBernstein L.P. makes no representations or warranties concerning the accuracy of any data. There is no guarantee that any projection, forecast or opinion in this material will be realized. Past performance does not guarantee future results. The views expressed here may change at any time after the date of this publication. This document is for informational purposes only and does not constitute investment advice. AllianceBernstein L.P. does not provide tax, legal or accounting advice. It does not take an investor's personal investment objectives or financial situation into account; investors should discuss their individual circumstances with appropriate professionals before making any decisions. This information should not be construed as sales or marketing material or an offer of solicitation for the purchase or sale of any financial instrument, product or service sponsored by AllianceBernstein or its affiliates.

**Note to Canadian Readers:** AllianceBernstein provides its investment management services in Canada through its affiliates Sanford C. Bernstein & Co., LLC and AllianceBernstein Canada, Inc.

**Note to UK Readers:** UK readers should note that this document has been issued by AllianceBernstein Limited, which is authorised and regulated in the UK by the Financial Services Authority. The registered office of the firm is: 50 Berkeley Street, London W1J 8HA.

**Note to Australian and New Zealand Readers:** This document has been issued by AllianceBernstein Australia Limited (ABN 53 095 022 718 and AFSL 230698). Information in this document is intended for wholesale investors only, and is not to be construed as advice.

**Note to Readers in Vietnam, the Philippines, Brunei, Thailand, Indonesia and India:** This document is provided solely for the informational purposes of institutional investors and is not investment advice, nor is it intended to be an offer or solicitation, and does not pertain to the specific investment objectives, financial situation or particular needs of any person to whom it is sent. This document is not an advertisement and is not intended for public use or additional distribution. AllianceBernstein is not licensed to, and does not purport to, conduct any business or offer any services in any of the above countries.

**Note to Readers in Malaysia:** Nothing in this document should be construed as an invitation or offer to subscribe to or purchase any securities, nor is it an offering of fund management services, advice, analysis or a report concerning securities. AllianceBernstein is not licensed to, and does not purport to, conduct any business or offer any services in Malaysia. Without prejudice to the generality of the foregoing, AllianceBernstein does not hold a capital markets services license under the Capital Markets & Services Act 2007 of Malaysia, and does not, nor does it purport to, deal in securities, trade in futures contracts, manage funds, offer corporate finance or investment advice, or provide financial planning services in Malaysia.

**Note to Singapore Readers:** This document has been issued by AllianceBernstein (Singapore) Ltd. (Company Registration No. 199703364C). The Company is a holder of a Capital Markets Services Licence issued by the Monetary Authority of Singapore to conduct regulated activity in fund management.

**Note to Taiwan Readers:** This information is provided by AllianceBernstein funds Taiwan Master Agent, AllianceBernstein Taiwan Limited. SFB operating license No.: (97) FSC SICE no. 049. Address: 57F-1, 7 Xin Yi Road, Sec. 5, Taipei 110, Taiwan R.O.C. Telephone: 02-8758-3888. AllianceBernstein Taiwan Limited is a separate entity and independently operated business.

**Note to Hong Kong Readers:** The document has not been reviewed by the Hong Kong Securities and Futures Commission. The issuer of this document is AllianceBernstein Hong Kong Limited.