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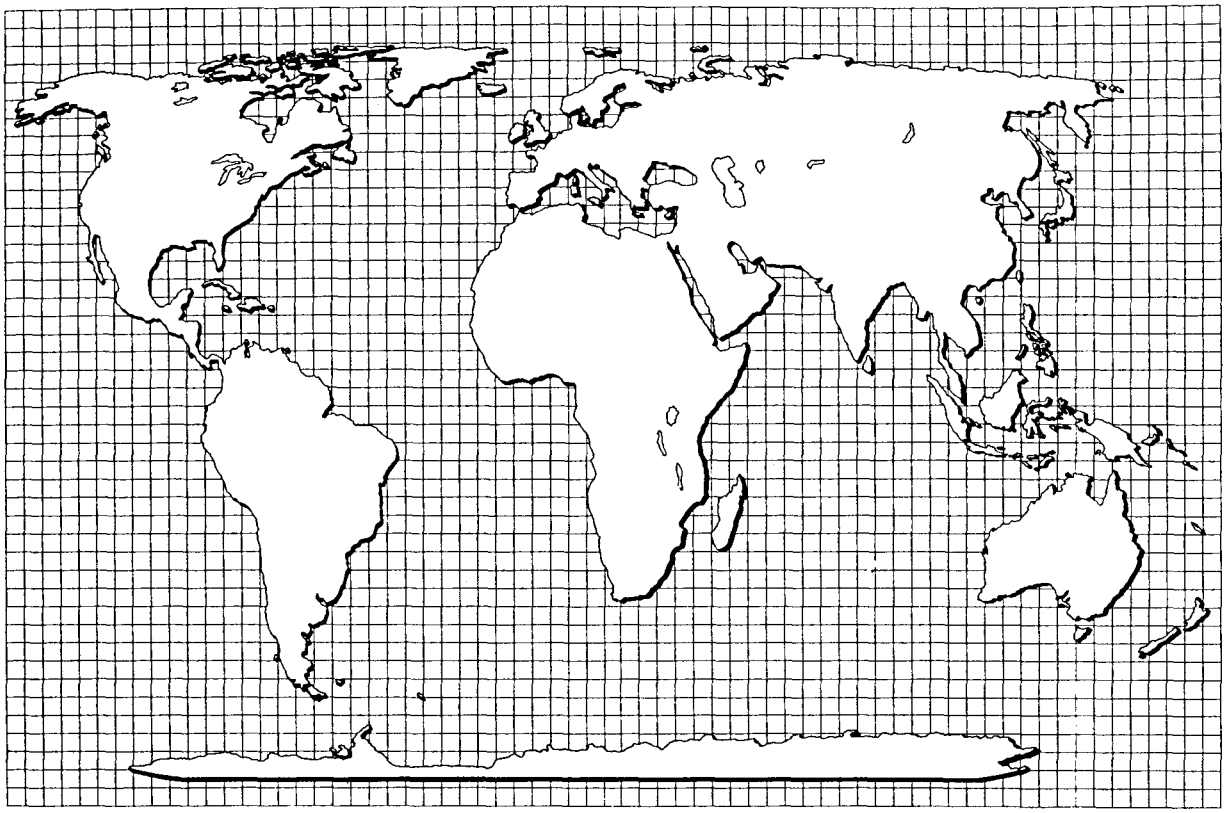

The Great Globe Itself

Introduction

Carla Sydney Stone

It is often said that the only way to get the attention of the American people is to hit them over their heads with two-by-fours. When the subject is international economics, the October 19 market crash is downright providential. If it hadn't happened, it would have had to be invented.

Before "Black Monday", about the only business news to be found in the commercial broadcast media was an announcement of the day's closing Dow Jones Industrial Average. International trade coverage consisted of BMW, Mercedes, or Cuisinart advertisements. Newspapers and magazines didn't do much better. The business section of most local papers was tucked between the sports pages and the comics. It took up several pages, but only because stock transactions are printed. Something as complex as international finance was reduced to a picture of LIVE AID.

Since October 19, journalists have become instant experts, business is the new "hot beat", and economists are the media darlings. The new buzzword in corporate America is "global competitiveness". Not since the Arab oil embargoes in the 1970s has international business received so much attention. It has taken two major economic disruptions within the last 15 years, but it finally has been made clear to the media and the American people, if not to our policymakers, that our economy is inextricably bound up with those of other nations.

No one event was responsible for the panic selling on the international exchanges. Many analysts attribute the steep decline to computerized program trading and portfolio insurance schemes that automatically force share sales without the benefit of human intervention. Whether computers and the automated linkages among trading houses and exchanges located around the globe exacerbated the effects of trading losses may never be known. It is clear, however, that the central issue touching off the correction to a five-year bull market was a world-wide concern about U.S. economic policy. But why now and not a year ago?

Much of the world looks the same as it did last year. Many Third World countries are threatening to default on their loan payments to commercial (primarily American and European) banks. The World Bank is embroiled in a fight over permitting its loans to be profitable. The International Monetary Fund is continuing to advance structural adjustment loans to its poorest members while advising, but not forcing

austerity programs. There are droughts in the SubSahara and people are starving even as food rots on the docks.

Interestingly enough America doesn't look all that different either. Now as then the U.S. has record trade and budget deficits. The U.S. dollar is dropping. Congress has just passed compromise tax legislation to cure our economic malaise. American business leaders are driving to Washington in $75,000 Mercedes to lambaste Congress over its inaction on trade issues. American teenagers listen to the latest rage on Sony Walkmans. Americans wear Asian-made clothes, eat imported fruits and vegetables, buy foreign cars, and scream that their jobs are endangered by other countries' unfair trading practices.

While on the surface it seems as if nothing has changed, there is a greater sense of urgency among the public to force policy changes that will permit the United States to deal with the twin trade and budget deficits. Most important, strident "Japan bashing" is being replaced by a more careful analysis of our bilateral economic and political relations as well as new understanding of our relationships with our European and North American allies.

The United States is the world's richest market. More than half of the merchandise exports from Canada, Latin America, and the Caribbean are destined for our shores. Thirty-five percent of our exports go to these areas. While Japan supplies 20 percent of our imports, it takes only 10.5 percent of our exports. This mess will result in a U.S. trade deficit of $159 billion for 1987.

Two years ago, in response to the increasing trade deficit, which government policymakers and business leaders ascribed to an overvalued dollar, the U.S. met with four of its strongest allies (England, France, West Germany, and Japan) to hammer out a plan to manage the fall of the dollar. The next year Italy and Canada (our largest trading partner) joined the negotiations. Since February 1985 the value of the dollar has dropped 40 percent against European currencies and 50 percent against the Japanese yen. While a depreciated dollar does mean that U.S. exports will be cheaper and imports will be more expensive, a devalued American dollar is no panacea for the trade deficit.

During the year September 1986 to 1987, imports to Japan rose by 20 percent in yen terms and 30 percent in devalued dollar terms. However, the United States, which is Japan's largest trading partner, was not the beneficiary of Japan's increased appetite for foreign products. During the first nine months of 1987, American imports rose three percent in dollars; South Korea, 47 percent; Hong Kong, 49 percent; and Taiwan's imports went up a staggering 55 percent. Imports from the EEC rose a remarkable 11 percent even when measured in yen. More forces than the strength of the dollar are at work: the U.S. internal economic structure and the growing internationalization of Japanese corporations are most important of these.

The United States is a capital goods economy, despite the shift from large-scale manufacturing to the service sector during the last ten years. We produce commodities such as chemicals and grains, and manufacture capital-intensive products such as airplanes, mainframe computers, and earthmoving equipment. However, we buy consumer goods such as stereo equipment, clothing, and appliances. Over 80 percent of U.S. imports are manufactured goods and finished products. Only 42 percent of Japanese imports are manufactured goods, consistent with Japan's status as the world's premier producer of consumer goods.

The 1987 *White Paper on International Trade,* published by the Japanese Ministry of International Trade and Industry, identifies four trends contributing to Japan's improved competitiveness even in the face of an appreciated yen:

1. An increasing advance into the United States and the newly industrialized Asian nations;
2. An increase in overseas procurement of parts and raw materials;
3. Changes in forms of investment;
4. An increase in overseas investment by small and medium sized firms.

The Japanese first began to build offshore plants in the 1950s. This trend accelerated during the 1970s as the country shifted its domestic industrial priorities from low-tech and energy-intensive industries to the high technology and service sectors. The most visible evidences of the move are automobile assembly plants in

(Continued on next page)

This issue of DELAWARE LAWYER is a series of cautionary tales about a world very different from the one we confronted in power and a deep sense of self-satisfaction at the end of World War II.

The design of this issue was the work of Carla Sydney Stone. She is exceptionally well qualified to address our changing roles in the world economy, the pitfalls and opportunities of change, and the implications for our profession.

Carla Stone holds a Baccaulaureate degree in mining engineering and a Masters degree in mineral economics from Columbia. She has had further post-graduate training in finance, economics, and Japanese. Her company, Business & Policy Associates, Inc., is an Asian trade consulting firm, headquartered in Greenville with a representative office in Hong Kong. She also teaches an over-subscribed course in international trade management at the College of Business & Economics of the University of Delaware. She is an accomplished editor (e.g. the recent fourth edition of Economics of the Mineral Industries*) and a regularly featured speaker at economic and trade symposia. She is a member of the Governor's International Trade Council, and was recently honored by the United States Small Business Administration as Exporter of the Year 1987 for Delaware.*

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INTRODUCTION
(Continued)

the United States and electronics and appliance plants in Korea and Taiwan. Imports of components and finished manufactured goods from other Asian locations already are commonplace as Japan takes advantage of lower wage and currency rates in the newly industrialized countries. Honda has announced that it plans to export cars from the U.S. to Japan in order to take advantage of the cheaper American dollar. Most Japanese companies envision a time when production can be shifted from one country to another to take advantage of labor, materials, our currency rates, or to be closer to their markets, as American companies have done for the last 20 years. IBM and DuPont are often named as successful competitors in Japan, notwithstanding the high cost of doing business in Japan. Skadden Arps, the first American law firm to set up shop in Japan, hopes to emulate their successes. *(See "Getting Started").*

In 1986, Shiro Miyamoto, the president of Japan External Trade Organization, said that the U.S. trade deficit is the result of our addiction to imports and to "American managerial mindset, including the transnational behavior of U.S. companies." This behavior, he felt, conflicts with the overall needs of our country. Export-linked competitiveness, which is good for the nation as a whole, may be detrimental to the objectives of the profit-linked competitiveness of individual U.S. companies.[1] It is not surprising that his prescriptions for curing our deficit are similar to those developed in Geoffrey Gamble's and Theodore F. Killheffer's article at page 7 and W.P. Schmoe's speech at page 14. They are to make trade a number one priority; to lower the cost of capital formation; to place greater emphasis on research and development and new technology; to improve U.S. educational standards by providing more opportunities for vocational training.[2]

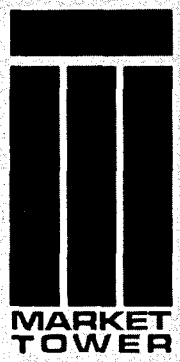
However, the picture is not entirely bleak. Americans are taking steps to reduce the trade deficit. Corporations are placing greater emphasis on quality and marketing. Universities are offering courses and special programs (Lesley Suddard's review of "Global Competitiveness in the 1990s" at page 22.) that will prepare their graduates to compete in the international workplace. As Ben Irvin points out (page 18) Congressional adoption of the Harmonized System will place U.S. traders on more equal footing with their partners overseas and will help the U.S. in trade negotiations and enforcing agreements.

Even those workers who have been displaced as a result of increased foreign competition (Eleanor Craig at page 31) find jobs in other industries, such as banking, the focus of Delaware's economic development programs. (David Swayze, page 28 and Andrew G. Knox, page 26).

I'm happy to report that *DELAWARE LAWYER* did not need the market crash to turn its attention to international trade. This issue has been in the planning for over a year. And what a year it has been! ■

[1] Miyamoto, Shiro, "Is the U.S. Serious about Its Balance of Payments?", *Journal of Japanese Trade & Industry: No. 6, 1986*, November/December 1986, p. 35-37.

[2] *Ibid.*



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The Enemies Of United States' Trade Competitiveness

A Lawyer's Perspective

Geoffrey Gamble and Theodore F. Killheffer

Many who read these pages may be too young to recall the Hollywood singer and comedian, Phil Harris. He's quite old now. Several years ago, he gave a performance and in the middle of it he turned, out of breath, to the audience and said, "You know, if I knew I was going to live this long, I would have taken better care of myself!" In many ways, any lawyer writing about international trade has to feel like Phil Harris. If he knew he was going to end up some day writing about international trade, he would have paid more attention to economics in college. Even that might not have been enough. International trade today is an interdisciplinary phenomenon. In addition to its economic and legal aspects, it involves politics, culture, societies and even geography.

THE PROBLEM
Present Situation: U.S. Deindustrialization

For some time now, U.S. production has been undersold by foreign production. Our production (and our jobs) have shifted to other countries in such sectors as steel, autos, machinery, textiles, and shoes. Certainly the United States has not experienced a net loss of jobs; unfortunately, however, lost jobs in major manufacturing industries have often been replaced by lower-paid service industry jobs.

Why is this happening? It is because the United States, since World War II, has suffered what might be called an "economic superiority complex". There has been a misinterpretation of our world economic dominance ever since the end of World War II. We were told that our high standard of living reflected high productivity and that we would always be more productive than others if only we and our partners engaged in "free trade". The fact of the matter is that our high standard of living resulted not from our "productivity" but because the rest of the world was either devastated by war or newly emerging from colonial status. We simply have not reacted quickly enough to these changed circumstances.

Comparative Advantage

The principle underlying the economists' rationale for free trade is called "comparative advantage". It was first proposed by David Ricardo in 1817 and may be best summed up as "doing what you do best". If both the English and the Portuguese, to use Ricardo's example, enjoy woolen clothes with port wine, the English should produce the sheep and the Portuguese should work the vineyards. If both countries reject trade and insist on self-sufficiency, the Portuguese will be chilly, drinking their port, and the English will be warm and sober—certainly an undesirable state by any standard of living.

Mutually beneficial trade today doesn't seem to occur automatically as the theory might suggest. If there were only two nations in the world—one producing wool and the other producing port—any imbalance would be unlikely. If England wanted port, Portugal would expect wool of equivalent value. If England said that it would send an IOU instead of wool, it is improbable that the Portuguese would let their casks of port even leave the quay.

The American Dream?

We Americans trade, instead, in a world that has *willingly* accepted American IOUs in exchange for our goods. That is a privilege denied to most countries of the world, such as Brazil or Mexico. America's ability to charge its huge foreign purchases is a reward for past diligence. Nevertheless, an unlimited credit card is an economic narcotic; promiscuous use has inevitable, though often delayed, consequences. Won't the world, though, react to the erosion in the value of our IOUs by eventually refusing to accept them? Here, again, our good reputation plays a perverse role. A world that finally rejects our IOUs will eagerly accept ownership of our *assets* instead. In contrast, creditors of Bolivia are understandably reluctant to trade large amounts of goods or IOUs for fixed assets within Bolivia. Why? Because the creditors are likely—at some point—to have their property confiscated. The United States is viewed differently. Other nations will confidently trade their consumer products for our real estate and for equity in our corporations. Foreigners' trust in our IOUs may eventually weaken, but trust in America will remain strong. Staggering shifts in ownership have already begun to occur.

Let's take a look at the clock attached to the time bomb ticking away on us. The equity value of all public companies in America is just under $3 trillion,* which is the equivalent of less than 20 years of our current merchandise trade imbalance. Income from these foreign investments, as well as investments in

(Continued on next page)

**Give or take a trillion, depending on Wall Street - The Editors*

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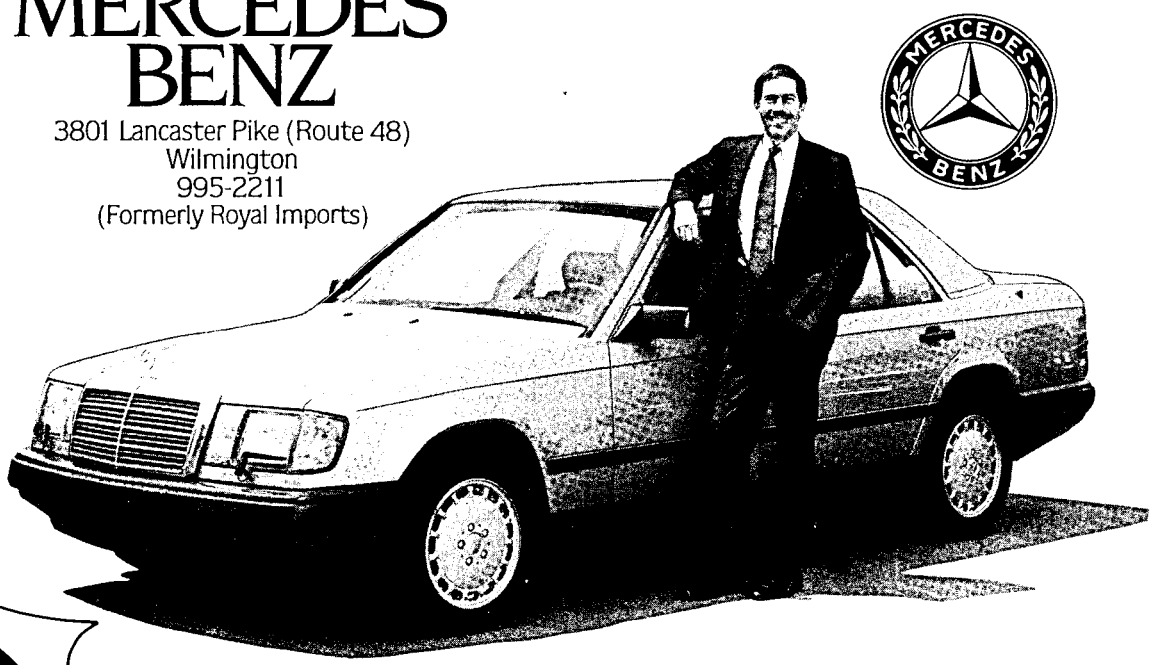

GET THE PRICE ADVANTAGE

Trade Competitiveness
(continued)

Treasury bills and other forms of debt, will grow correspondingly and add to the buying power that foreigners are amassing from their trade surplus. Ownership means control. Foreigners may and indeed are likely to exercise that control over American assets in a way that is not necessarily in the best interest of the United States or its people. Our wealth in America is a bane in our attempts to achieve a trade balance. We are in many ways like a once wealthy plantation family that annually sells acreage so that it can sustain a lifestyle unwarranted by its current output. In the end, the family will have traded the life of an owner for the life of a tenant farmer. Like the ruined Blanche duBois, we cannot indefinitely depend upon the kindness of strangers.

If our children are to enjoy a ... satisfying life in America in the 21st Century, we're all going to have to pay more taxes and ... tell our representatives in Congress that they must spend less money.

What Have Other Countries Done?

The Third World is now in a position to undercut the developed world in many manufacturing sectors. After World War II the U.S. embarked upon a "free trade" course. Asia did not. Countries such as Japan, Taiwan, South Korea, and Singapore oriented themselves towards raising the economic status of their people quickly by producing for markets of high-income nations. Their policy has been called "mercantilism" and sometimes "managed trade". In contrast, U.S. trade policy bore no relation to economic reality. We were caught up in a "free trade" (considered good) versus "protectionism" (considered bad) axis. At the time, there was considerable justification for such policies. Excessive trade restrictions had prolonged the depression of the 1930s. Furthermore, an open United States market was needed to fuel the post-war recovery of the rest of the world.

Successive Administrations failed to come to grips with the world trade situation as it has changed and have failed to protect the economic interests of the American people. Today, many people believe the United States practices "free trade" and that the rest of the world deals with us unfairly. In fact, if we look at government-created market distortions around the world, we see that, with the possible exception of Hong Kong, no one practices "free trade". The real question is the *degree* of market intervention by governments. The United States, Canada, Germany, and some of the Scandinavian countries might be characterized as having *moderate* government intervention. The rest of the Common Market, Latin America, Africa, and most of Asia, could be characterized as having *extensive* intervention by their respective governments, and the remainder of the world consists of the nonmarket economies of communist nations.

Where Is The World Going?

Much of the world is moving towards the Japanese model of mercantilism, not towards unrestricted trade. We would differ from some in Congress: Japan is not to be condemned, but admired. Japan and other Asian countries did not possess natural comparative advantages of the traditional kind, so they consciously combined what advantages they did have—chiefly cheap and abundant labor and governments willing to provide financing, trade incentives, and domestic industry protection—to create an internationally competitive position. This has been called "dynamic comparative advantage". Congressional Japan-bashing and ranting about unfair trade practices is wrong because it represents a *negative* policy. What we need is a cohesive, *positive* policy.

The task of restoring balance in United States trade is a formidable one, and the difficulties must not be underestimated. Foreign suppliers have become entrenched not only in our domestic markets but in our traditional export markets as well. They will not go away without a fight. Look, for example, at the sale of Japanese cars in the United States. In spite of the dramatic shift in the dollar/yen exchange rates, the Japanese share in the U.S. auto market has remained virtually unchanged. The Japanese have cut their margins to maintain the position they have earned in our market.

Looking around the world, we get some idea of the changes that face us in

(Continued on next page)

Well, talk about versatility! Back in the September Bicentennial issue Geoffrey Gamble was enlightening us about wicked King John, the Magna Carta, and the ins and outs of heraldic decor. In this issue he rejoins us in the late 20th century in a searching inquiry into our behavior as the wastrel heirs of rich and once prudent parents.

Mr. Gamble's collaborator, Theodore Killheffer is Managing Counsel-Tax in the DuPont Company Legal Department. In his more than thirty years with DuPont, he has had an extremely broad range of experience, beginning as a computer operator, progressing through tax accountancy, to a variety of assignments in the Legal Department. His perspectives, reflected in this article, doubtless have been seasoned by his former role as Senior Counsel to the International Department and his experience as Chairman of the Industry Sector Advisory Committee on Chemicals and Allied Products for Foreign Trade Policy Matters, to which he was first appointed by former Secretary of Commerce Baldridge and subsequently by U.S. Trade Representative Brock. Mr. Killheffer is a member of the Pennsylvania Bar.

Trade Competitiveness
(continued)

penetrating export markets. Countries accounting for 40 percent of U.S. imports have not allowed their currencies to strengthen against the dollar, so recent currency adjustments will not help our trade with those countries. These include Canada, South Korea and Taiwan. Expanded trade with Japan is inhibited not only by conventional trade barriers but also by characteristics of Japanese culture: The Japanese regard the purchase of manufactured goods from abroad almost as unpatriotic, and their propensity to save rather than to consume is the highest in the world.

Europe faces problems of high costs, significant unemployment, and stagnating industries. The cheaper dollar will help us regain lost European markets, but political realities suggest that our opportunity to reverse the trade imbalance at the expense of the Europeans is limited.

For Latin America, with its huge indebtedness, it is imperative to generate large positive trade balances. There is little opportunity there for U.S. exports to increase significantly and indeed, in the 1980s, imports from Latin America into the U.S. have soared more than 50 percent.

The United States cannot become more competitive in world markets overnight. But we must get to work quickly to restore the trade balance. Fortunately, the tools are within our hands. We must develop a consciousness of the importance of the U.S. stake in international trade. Recognizing that, we need to change some aspects of United States economic policy that inhibit our trade performance. These are the real enemies.

ENEMY NO. 1 - U.S. MACROECONOMIC POLICY

The major cause of our declining trade performance is U.S. Government fiscal policy. As we have incurred unprecedented federal budget deficits, the United States has required a massive infusion of foreign capital to finance federal spending. The low level of U.S. savings has simply been overwhelmed by federal deficits. These borrowings have sustained U.S. interest rates and put upward pressure on the dollar. As a consequence of the dollar falling in value more slowly than trade pressures would normally require, U.S. goods have become less competitive both in our own market and abroad.

This fact suggests that unless we get our federal budget into better balance, we can expect little real progress on our trade deficit. Attention to fiscal policy is very much an essential element of the trade issue. As the U.S. Government moves to address the budget deficit, the international competitiveness of U.S. products must be an important consideration. Until the fiscal deficit is corrected, however, there will be pressure on interest rates, cost of capital, and a demand for foreign goods. One might go so far as to say that the *only* way we can raise

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Our tax laws, too, ignore the realities of international trade. The Tax Reform Act of 1986 first and foremost did nothing to address the budget deficit problem. Beyond that, it reduced incentives to invest in plants, machinery and equipment, discouraged U.S. firms from pursuing overseas markets and raised the tax burdens on savings and investment. We must have a tax policy that complements our efforts to enhance U.S. competitiveness in world markets.

both investment and international competitiveness simultaneously is to increase national savings by deficit reduction.

The restoration of the dollar to its present value was a necessary step, but it will not fully correct the trade imbalance since it does not deal with the underlying economic disequilibria. Furthermore, with 40 percent of imports coming into the United States originating in countries whose currencies have not strengthened against the dollar, efforts in exchange rate adjustments must include those currencies pegged to our dollar.

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If our children are to enjoy a reasonably satisfying life in America in the 21st Century, we're all going to have to pay more taxes and we are going to have to tell our representatives in Congress that they must spend less money. There is no other way. As the 1988 election season gets underway, we should put trade very near the top of our list and demand straight answers from Presidential and Congressional candidates about their commitment to American competitiveness.

Enemy No. 2 - U.S. Foreign Policy

Application of U.S. national security and foreign policy sanctions to foreign trade and investment of U.S. multinational enterprises in an attempt to influence foreign countries has been plagued by inconsistent policies, ineffectiveness, outright failures, and the sacrifice of long-term national interests. We are dealing primarily here with two laws—the International Emergency Economic Powers Act of 1977 (IEEPA) and the Export Administration Act of 1979 (EAA).

For example, in 1979 President Carter imposed sanctions under the EAA. The immediate effect was the loss of over $2.3 billion in export sales of U.S. farmers and $2.5 billion in costs of the U.S. Government (in other words, all of us) to take over grain that otherwise would have been sold to the Soviets. The U.S. economy lost $11.4 billion in national output and $3.1 billion in personal income. In 1981 the GAO concluded that the Soviets had been able to replace most of the embargoed U.S. grain from Argentina, Australia, and Canada. The U.S. became a marginal supplier of Soviet grain. After six months, the embargo was lifted. As you know, the Soviets are still in Afghanistan, and the U.S. has lost many more billions of dollars in sales of grain that otherwise would have been made to the Soviet Union over the past seven years. Furthermore, like the stinger of a bee, the grain embargo was a weapon we could only use once. Now that we are a marginal supplier, reuse of this particular embargo would be totally ineffective.

Under the IEEPA, President Reagan in 1986 issued an Executive Order terminating all commerce with Libya. U.S. companies with Libyan investments were required to sell their assets, thus enriching the government of Libya. Thanks to the help of our friends in Europe, Libya was not prevented from producing and marketing oil in quantities up to its agreed-to OPEC quota and Mr. Khadafy remains in power. A degree of cynicism in recounting these instances should not obscure the issue; what the Soviets did in Afghanistan was wrong and Col. Khadafy's terrorist activities around the world should clearly be punished. The

(Continued on next page)

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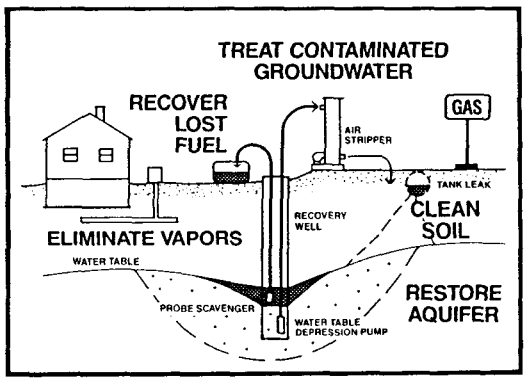

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Trade Competitiveness
(continued)

point is that the sanctions the United States chose to apply were ineffective, expensive, and harmful to American competitiveness.

What makes this particular enemy of competitiveness so troublesome is that we all generally agree with the nobleness of the causes. Most of us abhor apartheid in South Africa. Most of us deplore discrimination against minorities in Northern Ireland. Nevertheless, using American multinationals as tools for public and private foreign policy diminishes vital competitiveness and to date has been ineffective. Our friends and allies seem to do much better in being able to "lightning-rod" political causes away from international competition.

When we get caught up in a cause, however noble, we must step back for a moment and ask ourselves how *effective* is the proposed economic sanction really going to be. We should ask those proposing the sanctions exactly how much it is going to cost America and its people as a whole. Lastly, we should ask what our allies are doing to support the proposed sanctions and what alternative foreign policy sanctions are available. What we need when economic sanctions are proposed is, in effect, an "environmental impact statement" before any action is taken.

Americans have been told for so long that they do not have a culture that we actually believe it. This is a dangerous thing. Call it what you like: Judeo—Christian—Greco—European-melting pot, but it is a culture. We tend to take what we consider to be universal principles (democracy, ethics, egalitarianism, upward mobility) and enforce them wherever we can around the world. Many of us feel deep down that the system of ethical, political, and economic principles upon which America is built is the correct one and that the rest of the world is at various stages of imperfection moving towards, and sometimes away from, our goal.

We do not hesitate, either as individual Americans or as a government, to indulge in cultural ignorance, which the rest of the world perceives as cultural arrogance. In 1977 Congress enacted the Foreign Corrupt Practices Act, which prohibits bribery of foreign government officials to obtain or retain business. Few would quarrel with that. However, it goes beyond the individual activities of U.S. firms and covers the affairs of their foreign distributors and customers as well if the U.S. company has "reason to know" that bribery is going on. In many Third World countries, such as Indonesia, gratuities are a way of life. Far from trying to help U.S. companies find legitimate ways to compete with their Japanese and European counterparts in this problem area, one agency of the U.S. Government, the Department of Justice, has actually gone so far as to state that it doesn't want to issue guidelines because it is afraid it will be easier to "get around" the Act if guidelines are issued!

ENEMY NO. 3 - LACK OF A NATIONAL TRADE STRATEGY

The federal government does not so much *need a trade policy as it does to make* trade its policy. Trade performance simply must have a higher national priority. Trade concerns have often lost out when they are at cross purposes with defense concerns and with public and private foreign policy. The cost to international competitiveness for American companies of this insensitivity to trade on the part of our government is incremental, not monumental, but it is adding up. Author Kevin Phillips has called for a new "economic nationalism" for the United States. Peter Drucker has said that the time has come to build an awareness of trade and comparative U.S. economic strength into official policymaking.

As a nation, we must come to terms at long last with our own finite resources. We no longer have an unlimited frontier in which to expand. We can no longer take in unlimited waves of immigration to enrich our citizenry. We must do what others have done before us. We must take a long, hard look at ourselves and our resources and marshal them in a way that we can effectively and successfully exist and compete in this world. We have to stop the dislocation and exportation of industries that are necessary for U.S. economic well-being. It is against our nation's survival instincts to allow its basic industries to crumble. Our strategy must be a synthesis—a careful and reasonable nationalism and a partnership between the private and public sectors. A practical first step is to

identify threatened industries and examine past experience with managed sectors. What has worked? What has not? Why?

The U.S. Government must establish a forthright trade strategy that puts our major trading partners on notice that we assign the highest priority to reversing our international trade deficit. We, as a nation, should actively seek to dismantle trade barriers facing American exports and investment. We should focus on countries with persistently high bilateral trade surpluses. Where good faith efforts fail to reduce obstacles to trade and investment flows, the U.S. should retaliate in full and in kind as provided for under U.S. trade laws and under the provisions of our international treaty obligations. In this regard, there should be a more constructive response to trade remedy petitioners by the U.S. Government. While the government must honor U.S. international obligations, it need not turn each proceeding into a politicized, adversarial one between a petitioner and his government.

ENEMY NO. 4 - PRIVATE SECTOR COMPLACENCY

We who work in the private sector cannot put the total blame for the current trade imbalance on others. We must get our own house in order and change the way we think. Despite what some people might tell us, there is nothing immoral about labor and industry uniting and working together in common interest. There is nothing meritorious about government bureaucrats who think that in order to be successful they must be the adversaries of the private sector. In the interest of enhancing domestic productivity, relationships among government, industry-labor and other sectors of the public must become more positive and productive.

Even though many industrial sectors in this country are going through a very tough period, they can't be crying to the government to preserve the status quo. What they need to do is look at their world-wide competition, emulate the successes, and learn from their mistakes. If they are in a state of crisis and have to come to the government for relief, they should come with organized and realistic plans outlining the parameters of the relief sought and a timetable for an end to the relief. Many of these sectors have to take a sobering look at their future.

Private industry must make every effort to meet and exceed the competition internationally. Innovation, quality, service, price and cost containment should be constantly reevaluated and improved.

Here are the enemies of international competition and some possible solutions. These are not *all* of the enemies, nor have we exhausted the list of solutions. No one has a monopoly on those. Debate is healthy; it serves as a means not only of hammering out options but also of exposing us all to different points of view. Albert Einstein once said something to the effect that everything has changed but our thinking. Our thinking about international trade will have to change if we are to achieve consensus on goals broad enough and big enough to be worthy of our state and of our nation. ■

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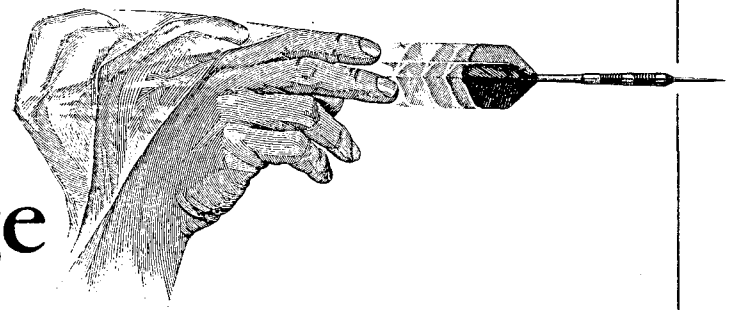
Reflections on the Global Village



Wilfred P. Schmoe

(Remarks delivered at the College of Business, University of Delaware on October 28, 1987)

Let me begin with a personal perspective of internationalism in general. Since my wife and I first set up house we've moved 17 times answering the call of business. We have lived all over this country, of course, and in other parts of the world as well. Nowadays this is not at all unusual in corporate life. One thing that my wife and I have learned in this moving around is that people all over the world are not really that much different in terms of their hopes and aspirations. There is no good reason why we should not be able to get along with almost anybody, anywhere. That has been our experience, and we have been very fortunate in meeting a lot of fine people of all shapes, sizes, and hues, and making many friends. Another observation that I would like to make is that wherever I travel—here, in Europe or in Asia, I do not remember having made one trip in recent years without bumping into a friend, a colleague, or a competitor in a hotel lobby or on the street. There are two points here. One is that business is a wonderful common denominator among all the peoples of the world. And the second point is that this *is* a small world, and it's growing smaller.

In terms of business and commerce, we have already become what Marshall McLuhan called "a global village". The reasons are fairly widely understood, and we need not take up a lot of time this evening in discussing them. A listing of reasons under the heading "political/diplomatic initiatives" would have to include the Marshall Plan—that enlightened program that helped nations ravaged by World War II get back on their feet—the General Agreement on Tariffs and Trade, formation of institutions such as the International Monetary Fund and the World Bank, and the creation of multinational trading groups such as the European Common Market.

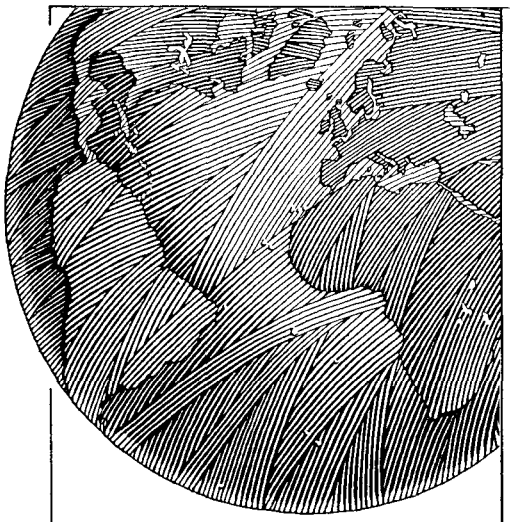
In addition, the world has become vastly more interdependent in the past two decades as mature industrial nations such as the United States find they can no longer meet their own needs for natural resources. The most obvious example of interdependence is oil, of which America now imports about 40 percent of its needs. But oil is by no means the only case in point. The United States needs to import *most* of its strategic minerals—in fact, more than 70 percent of the 16 most critical strategic minerals comes from abroad, according to the Bureau of Mines. So this country is a part of the global market as a result of political choice and logistical necessity. We couldn't manage without the other folks, even if we wanted to.

In the past decade the major force drawing the world closer together has been technology. It has made possible not only rapid travel, but near-instantaneous transfer of funds, know-how, and culture to the four corners of the world. Electronic impulses send tidal waves of money washing around the globe, leaving pools in areas of attractive potential, followed by new industries, new jobs, and new prosperity. In jungle villages in Indonesia where only a few years ago people were close to the Stone Age, they're now wearing blue jeans, listening to rock and roll, buying new VCRs for their TVs, and eating fast food. This may not seem like an unmitigated blessing to us, but it's certainly a change for the better for the people who were living in primitive poverty and isolation.

There are many other, perhaps clearer, benefits stemming form the trends I have mentioned. These include the evolution of a rich and diverse world market, overflowing with goods and services, readily accessible, and at competitive prices. Think about this for a few seconds. What you're wearing and where it came from, the car you came in, the food in your fridge, maybe the fridge itself, your TV, and maybe your favorite program on PBS—the inventory is very international. Never before has so much been available from such a variety of sources, and within economic reach of so many people. This is true not only in this country; it is increasingly true of many other countries, where consumer buying power is rising in the wake of industrialization.

Of course, there's a price to be paid for these blessings. The United States has lost the advantages that naturally accrued to it after World War II, when the rest of the world owed us money, when we had what was probably the only remaining vigorous and undamaged industrial base, and when we were the undisputed technology leader. Today, dynamic industrial economies that arose out of the ashes of World War II have overtaken us, and new industrial economies are flowering around the Pacific Rim. Money and know-how are widely available, almost anywhere in the world. And if performance is judged solely by trade surpluses and deficits, and by who owes how much to whom, we would have to admit that America is in sad shape.

By these yardsticks money and know-how are being used a lot more effectively by others. It's tempting to blame those others for our current problems in international trade, and to suggest that the rich variety of goods and services being offered to us from all over the world is the root of the problem. The real problem, of course, is that we are not selling enough of our own goods and services in the world marketplace.



In short, we are now in the position of *having* to compete on more or less equal terms with other nations, but the evidence suggests that we are not yet prepared to compete to the degree necessary, or to adjust our attitudes and policies to reflect the loss of our former privileges and advantages. There is absolutely no doubt in my mind that if the United States really made a concerted effort to turn the trade deficit around, we could do it, and probably be surprised at how quickly. However, it's no easy task to prevail upon an *ad hoc* committee of 240 million people to focus on such arcane problems as trade deficits, particularly when most members of that committee are enjoying unprecedented personal prosperity. Indeed, as we approach the 60th month of one of the longest economic expansions that America has enjoyed since we began keeping these kinds of records in 1854, we do seem to be well-served. But I'm sure we all have our doubts as to how long we can keep on piling up trade deficits and debts without rupturing the system—doubts demonstrably shared by Wall Street earlier this month.

The fact is, the problem of relative performance in the world market means different things to different people. To the average American, this nation's lack of ability to compete is less worrying than how he or she can meet the mortgage payment, although these two factors may be related.

To those in government, the problem is measured in trade deficits, borrowing needs, interest rates, and the value of the dollar in relation to other currencies.

To a company such as Du Pont, it's all these things. The survival of the company as we know it depends on our ability to compete effectively in world markets. In this sense, the challenge is as unequivocal as meeting the mortgage payment. Mainly, the outcome is up to us. But we're helped or hindered to a considerable degree by the actions of government in a wide range of areas including fiscal and monetary policy.

Business has responded to the challenge in time-honored fashion. It has seized upon a buzzword, "globalization". Congratulations are in order for whoever came up with the word, because business thinking and planning on a global scale are *exactly* what we need in this country.

At Du Pont, we may not take the term terribly seriously but we do take the concept *very* seriously indeed. We did agree that we needed to put a label on our own concept of a global business strategy, and, yes, we did embrace the word "globalization". We also recognized that the word itself means different things to different people. Here's how we have defined it for purposes of discussion within our own management. I quote:

"Globalization is the effective deployment and utilization of worldwide resources, including human resources, matched with opportunities, across national boundaries, to achieve competitive advantage and superior business results."

Translated into action that means Du Pont is developing global strategy for research and development, manufacturing, and marketing for all major businesses, instead of having master plans with the U.S. at the center and the rest of the world as an appendage.

I believe it is true to say that just a few years ago the traditional view in most American industries was that overseas markets were incremental and/or opportunistic. In other words, if a company had products that were salable overseas, that company might let the overseas market have some of its widgets. But products were very seldom developed for specific overseas markets. American manufacturers did not tailor products to suit foreign market needs, tastes, or styles. Regrettably, this is still true to some extent.

By contrast, the trading partners about whom we tend to complain the most, because of their trade surpluses with us, are the ones who most carefully study and cater to our needs and desires. The point is, foreign industries have wooed and pursued American buyers, while American industries selling overseas have had, by and large, a "take it or leave it" attitude. This attitude has changed somewhat in recent years, but not soon enough or to the extent necessary to make a dent in the trade deficits.

You know, at Du Pont we have been multinational for a long, long time, in the sense that we do business in many countries. But being multinational is not the same as being globalized as we define the word. In the past, our approach has been basically opportunistic, as Dick Heckert, our chairman, has pointed out. We began by selling our products overseas as and when the opportunity arose — and we were multinational in this respect 'way back in 1805. In response to market demands, we followed up by establishing service facilities overseas in support of the products being sold. And we did establish manufacturing facilities where this was necessary to gain market share or to avoid import restrictions in those countries that we considered attractive.

But by and large we were not planning on a global scale. We were planning as an American company with overseas interests. This not intended as a criticism. Our U.S. planning posture made perfect sense at a time when most of the growth opportunities were here in the United States, when there was little competition in foreign markets, and when we could more or less just pick the markets where we wanted to sell our highly desirable products and just go ahead and do it.

Things are different today. The competition is hot. For many of our products, the markets of greatest potential growth are not in the United States, but overseas. In fact, Du Pont's overseas businesses as a whole are outpacing growth in our U.S. markets. Overseas sales already account for more than 40 percent of our business, and this number will be up to 50 percent within a few years.

I don't think I'll be giving away any corporate secrets if I tell you we're looking at how we can round out our product lines in the 50 countries where we already have operations, and how we can expand into new markets — including mainland China. We're also looking to create full-service operations where this would be advantageous, and establish business teams with worldwide scope and responsibilities.

Under this team concept, the leader of each business would be headquar-

(Continued on next page)

Global Village
(continued)

tered in the country with the leading market. In any case, he or she should be as close as possible to the market. Thus, we would be in a better position to foresee trends, capitalize on opportunities, and serve customers. This is globalization at the grass roots — getting our facilities and our people close to the customer, wherever that may be.

So far I've talked about the need for globalization in general terms. Now let's be more specific. I'm on safe ground here because these specifics have already been enunciated by the chairman of the board. There are many reasons why globalization is necessary for Du Pont. Here are six of the most important:

Pressure from governments. Some governments offer investment grants, tax breaks, and other preferential treatment for companies that manufacture locally, and sometimes penalize those that don't. Some insist on having a certain percentage of local ownership of the overseas subsidiary.

Customer preference. In some cases our customers insist on having a local source of supply and full technical support.

Competition. Our competitors are ready, willing and able to provide local sources of supply and full support services almost anywhere in the world. Failure to compete with them on these terms would be like giving up without a fight. It would be like throwing in the towel in the markets in question. And there is no way we would pull out of world markets, because this would undermine our entire cost base and leave us at a competitive disadvantage not only overseas but in our U.S. markets as well.

Logistics. One of the bones of contention about globalization is that it sometimes entails operating manufacturing facilities outside of the United States. Often, common sense leaves no choice. Let me give you an example from my experience with our oil business. We have crude oil production in the North Sea, an oil refinery on the North Sea coast of England, and a combined U.K. and Western European market on the doorstep. This combination of raw materials, manufacturing facilities, and proximity to customers helps us compete in a market with a population of 350 million and a GNP of some $4 trillion.

Technology transfer. Being close to all our markets keeps us in touch with the new technologies that are being developed, not just in the United States, but in many other countries as well. We need to be where the action is in order to stay at the leading edge of technology in all our businesses. Technology transfer really is a two-way street nowadays.

Currency values. Globalization helps balance the risks associated with periodic misalignment of currency values.

The bottom line here is that it will be virtually impossible to be a major force in the U.S. market, or any other single national market, without having a broad, multi-market, multinational base over which to spread the high costs of research and development and overhead. Du Pont is competing with companies that do have a wide geographic spread and can therefore enter the U.S. market on a very cost-competitive basis.

This sounds cut-and-dried, but we've had our problems with the globalization concept. We don't have all the answers, but we have had to work a few things out, including some typically American psychological problems. We've had to adjust our view of the world and, to some extent the way we feel about ourselves. We've had to balance strong feelings of national pride with the understanding that other people are as smart as we are, and maybe smarter in some things. We've had to recognize that in some instances it is better to build a plant overseas to serve a specific market than to lose that market altogether.

We're almost fanatical about proprietary information. But we also know that we can add to our knowledge by some selective give and take. We cannot afford to ignore what is going on in the rest of the world or we will fall behind in the technology race, and if we do that we fail ourselves and our country. We are already globalized in research to the extent that we now have technical centers in Europe and Asia.

So these are some of the things Du Pont is doing in response to global competition. Other U.S.-based companies of similar size probably will be under-

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taking similar measures, if they don't already have global strategies in place, because the trend is inevitable — dictated by economics, technology, and logistics.

Perhaps you'll agree that Du Pont is doing a good job in responding to the challenge of international competition when I tell you that we exported $2.6 billion worth of products from the U.S. last year, while our imports — mainly raw materials — totaled $800 million. This gives Du Pont a U.S. surplus in international trade of $1.8 billion.

Now I won't read the full laundry list of what business wants government to do to help the *nation's* competitive position in world trade, because anyone with an interest in international business is surely familiar with the litany. Sufficient to say that the United States continues to be severely handicapped by the lack of balance between fiscal and monetary policies, which creates budget deficits, increases debt, and adds to the cost of money. And we still don't have equal access to other markets or a level playing field at home. If Congress were really serious about our trade position, every piece of legislation would be considered at least to some extent in light of its potential effect on America's competitive position. Policies should be viewed in the same way.

How society as a whole responds to the challenge will determine our right to a future of economic prosperity.

Energy is a case in point. Petroleum imports probably will add up to about $40 billion for this year as a whole. This is major money, even when compared with the overall trade deficit, which is estimated at $165 billion. To what extent do government policies contribute to the energy component of the trade deficit, by hampering production and use of U.S. energy? Congressional opposition to oil leasing and restrictions on the use of natural gas are two negative factors that come to mind.

I'm not suggesting the equivalent of a trade environmental impact statement as a precursor to any and all legislation, but simply that the larger picture should be considered. In short, our elected representatives need to acknowledge — like Ethel Merman in the musical "Gypsy" —"small world, isn't it?" and develop an appropriate global perspective.

And *all* of us, business, government, parents, grandparents, children — all components of society — must wake up to the dangers of an under-educated population. We need to stop worrying about such things as whether Beatrix Potter's children's stories need to be rewritten to make them more "relevant" and focus on the real problem, which is that many high school students and even some high school graduates couldn't read Peter Rabbit no matter how it was written. People who are not functionally literate cause terrible problems in the workplace, in terms of productivity and safety. Workers who cannot read warnings are walking hazards.

It is *not* the proper role of universities to provide remedial reading and writing. Yet, unless much greater progress is made at the high school level, we may reach a point where the bachelor's degree replaces the high school diploma as evidence of competence in the fundamental skills. The problem is exacerbated by the increasing complexity of our technological society, and by the fact that we are an aging nation, which suggests a future tight supply of competent people of working age.

These issues properly are topics for other discussions, but they obviously do have a bearing on America's ability to compete successfully in the global village.

Now let's look in the assets column, before we get too depressed. Actually, the assets could certainly more than outweigh the debits if they were exploited effectively. For example, we have a large and rich market, which other people are always trying to enter. We could more aggressively use access to this market as a lever in negotiating fair play and equal access issues with our trading partners. Furthermore, we are still the leader in R&D investment and in entrepreneurial skills, we have a stable democratic capitalist system that continues to be a haven for world investment, and we have a powerful economy. So far.

Also, there is another side even to the education issue. One reason why we're not getting a good crop of job market entrants from high school is that a greater proportion of people are going on to college. This may well mean that in the future there will be more blue-collar baccalaureates. I've even heard of Ph.D.s who paint houses for a living. That's great — but maybe it's *not* the most cost-efficient use of educational resources.

Wilfred P. Schmoe, Executive Vice President of the duPont Company, was formerly Vice Chairman and Chief Operating Officer of Conoco, Inc. His credentials for discussing international trade are impeccable: in 1975 his career with Conoco took him to London as Executive Vice President of Conoco North Sea. He was elected Vice President for International Production in 1980 and returned to Houston, Texas. He became a Chief Operating Officer of duPont and a member of the duPont Board of Directors in May, 1983.

Of course, if America is to remain affluent, we're going to have to do better than this. We're going to have to make more effective use of all our assets, including the high school system.

We could talk about these interrelated problems all night. I believe I've spoken long enough to at least provide some points for discussion. Let me sum up quickly with the observation that global strategic planning by some companies is a positive response to the challenge of international competition, but it's only one aspect of the picture. How society as a whole responds to the challenge will determine our right to a future of economic prosperity. Perhaps the biggest challenge for Americans will be to adjust to the fact that we must re-earn our affluence, on more or less equal terms with the other people who inhabit this shrinking planet. This is the price of membership in the world market. ■

Streamlining Commerce

Ben L. Irvin

Ben L. Irvin

The Harmonized System

Our special issue editor sat down with Ben Irvin to discuss a promising new device for easing some of the difficulties traditionally associated with the conduct of international trade. That discussion, cast in question and answer form below, alerts us to what promises to be a significant change and improvement.

Ben Irvin, who maintains offices in Washington and in Silver Spring, Maryland, is a highly experienced international trade and customs attorney. His previous service with the U.S. Department of Commerce, the U.S. Customs Service, the Executive Office of the President, and the Treasury Department give him a depth of knowledge essential to this intricate branch of the law.

What is the Harmonized System?

The Harmonized System (HS) is a complete product or merchandise classification system. It employs a numbering or coding system consistent with its organizational arrangement. It provides manufacturers, transporters, exporters, importers, Customs, statisticians, and others with a multipurpose system for classifying goods moving in international trade under a single commodity code. In effect it is the international bar code for merchandise moving in international trade.

Why is the Harmonized System needed?

There are many obvious drawbacks to not having a common system:

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1. Traders, commercial interests, and government are unable to cross compare trade statistics and tariff rates.
2. Under the present system as merchandise moves through international trade, one shipment of a commodity may be described as many as 17 times.
3. Multiple classification systems result in errors that affect the quality of statistics, correctness of customs, and freight tariffs, etc.
4. The different systems make it costly, as well as difficult, to verify and correct commodity coding errors.
5. Different classification systems make detailed comparisons difficult and complicate international trade negotiations.
6. The electronic transmission of data is hampered.
7. The movement of goods can be delayed.

Who will be able to use the HS?

While it was developed primarily for Customs purposes, it takes the interests of others into account. It is intended to serve as a "core" system, which can be used "as is" or expanded for specific uses (tariffs, freight rates, statistics, etc.) by anyone engaged in international trade.

Would you provide some background on the development of the Harmonized System?

For years, the trading community and governmental analysts have been struggling with the different classification or nomenclature systems, for goods moving in international trade, depending on where they go and whether they are imported or exported. This has complicated the preparation of customs and transport documents, impeded wider use of electronic data processing in transactions, hampered analysis of trade data, and created uncertainty in the negotiation and interpretation of trade agreements.

The explosion of world trade in the 1960s and the growth of computerization in international commerce reinforced the demand for a single global classification system. In 1970, the Customs Cooperation Council (CCC) sponsored a study for a universal system and found that such a system was feasible and essential. At a meeting of the Economic Commission for Europe, it was agreed that the CCC was the organization best suited to study commodity description and coding with a view to developing a system sufficient for the requirements of customs authorities, statisticians, carriers, and producers.

Since 1973 the CCC has been developing the "Harmonized Commodity Description and Coding System," more commonly known as the Harmonized System. It has been designed as a comprehensive up-to-date system for customs tariffs, statistical, and perhaps for transport documentation purposes.

(Continued on page 20)

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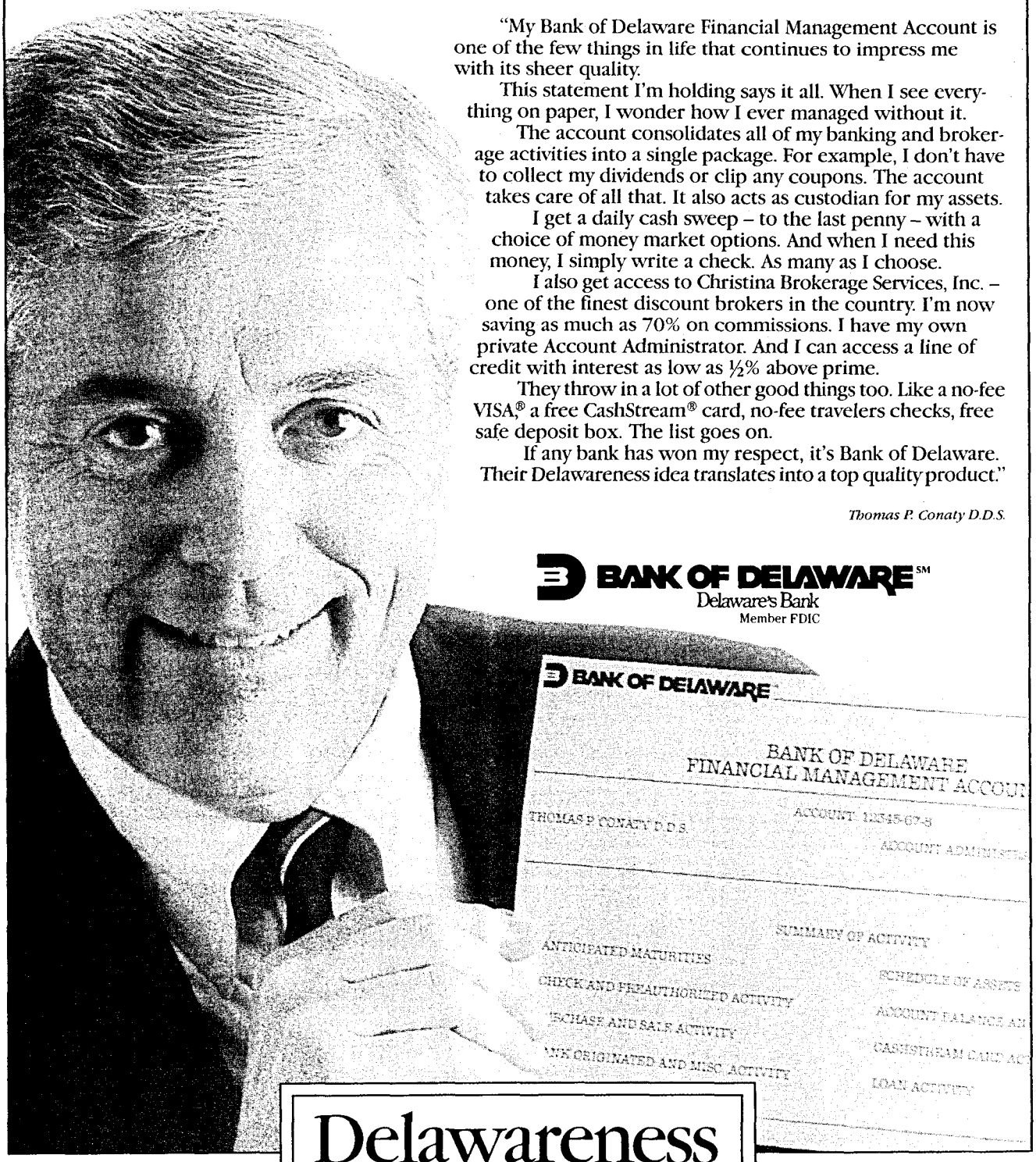

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IT'S A GREAT STATE OF MIND

Streamlining Commerce
(continued)

The United States Government has been active in the development of HS under section 608 of the Trade Act of 1974, and U.S. private sector groups have participated in the international work on the system. All draft chapters have been made available for public comment. Sixty countries, fourteen government international organizations, nine private international organizations, and two national trade facilitation organizations have participated.

When does HS go into effect?

The target date is January 1, 1988, but Congressional approval must be obtained first. Unfortunately, the Harmonized System proposal is mired in the legislative process along with the Omnibus Trade Bill (H.R. 3).

As of early December 1987, U.S. manufacturers, importers, and exporters began a last minute effort to pass a uniform tariff classification scheme, independent of the trade bill. This would necessitate removal of the Harmonized System provision from the trade bill, and separate Congressional approval. Business groups, such as the national Association of Manufacturers, the Chamber of Commerce, and the Joint Industry Group (on customs matters), have sent letters to committee chairmen to exert pressure for expeditious action.

Failure to pass the Harmonized Systems by January 1, 1988 could cause problems. First, it could lead to cargo back-ups at U.S. ports as paperwork for imports arrive with the new HS classifications that the U.S. would not be using. Second, U.S. business could bear a heavy cost if it must keep, or use, two separate and distinct classification and statistical records to reflect the U.S. system and the new international, or HS system.

Will adoption of the Harmonized System change duty rates?

If you ask the government authorities (e.g. Customs, International Trade Commission, and Special Trade Representative) they will tell you that the adoption of HS will be as rate neutral as possible. In a few instances, however, duty rates may increase slightly but some will be reduced. When two or three distinct duty rate provisions are collapsed into a single duty rate item, some rates will rise, others will fall, and some probably won't change. An importer will be pleased with a "windfall" rate reduction but be very upset with an unwarranted rate increase merely for the sake of "harmonization."

The real answer to the duty rate question is that the result depends on a variety of factors, including industrial sectors, product composition, etc. My first recommendation to any importing company or corporation would be to obtain a binding classification opinion from the Customs Service. In the August 25, 1987 edition of the *Federal Register* (52 Fed. Reg. 32092), the Customs Service announced that, beginning immediately, tariff classification rulings issued to the public upon request under the provisions of Part 177, Customs Regulations (19 C.F.R. Part 177), will contain binding classification under both the current TSUS and the HS.

Second, there is a major philosophic or interpretative change from the TSUS to the HS. The general philosophy behind TSUS is that the "chief *value*" of an article controls its classification. Under the HS, classification will be determined by "chief *weight*."

Let us assume that you import a 'widget" which is by *value* 51 percent steel and 49 percent gold. Under the current tariff schedules, this widget would be classified as a "steel widget." However, if this same widget by *weight* is 51 percent gold and 49 percent steel, under HS it would be classified as a "gold widget."

What are the benefits of HS?

The HS will facilitate the classification of goods because the international six-digit classification code will be placed on commercial documents. The HS in effect creates a common tariff language. The United States and its trading partners will be using the same tariff language through the first six digits of the Harmonized System commodity codes.

The use of the same code for imports and exports, as well as transportation purposes, will save considerable time and money because goods will not have to be re-coded and re-described as they move from country to country, and from system to system in commerce. Use of HS will also increase the accuracy of international trade statistics, making it easier to compare trade data, increasing certainty and understanding in international trade negotiations, and simplifying the verification of product classification. Use of HS will allow use of standardized international forms, which will make paperwork easier and more precise.

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What are the disadvantages and potential problems with the Harmonized System?

Any new system that will broadly affect traditional business and government practices will create disruption, discontent, and expense. This is especially the case when the new system supplants known systems that work and adequately meet many needs. The Harmonized System replacing the Tariff Schedules of the United States (TSUS) is no exception. There will be start-up problems in training, disputes and test cases, and conversion costs.

TRAINING. The retraining requirements for government and industry participants have been, and will continue to be, herculean. Thousands of importers, exporters, attorneys, customhouse brokers, freight forwarders, and traffic managers will have to learn not only an entirely new code, but the rules of classification or interpretation under the new system, and so will governmental authorities.

CONVERSION COSTS. HS will require republication of tariff codes, and the rewriting of regulations, proclamations, internal instructions, public publications, corporate procedural manuals, etc. Of no less importance, reprograming automated data processing systems will be extremely expensive for private industry and government. The documentation and data processing issues permeate every aspect of international trade: commodity codes are usually a primary reference key to most trade information sources.

DISPUTES AND TEST CASES. Classification questions will arise from confusion caused by the new rules, new interpretations, legitimate differences of opinion, and from test cases to seek avoidance of tariff levels, quotas, textile categories, etc. There will likely be an explosion of ruling requests during the first years, which will consume the energies of government agencies, international organizations, and industry officials.

LOSS OF HISTORICAL TRENDS. Conversion to the Harmonized System will mean building an entirely new statistical data base that cannot be accurately compared with existing historical data. The ability to isolate trends and fluctuations in trade is a major analytical tool. It will be lost until a new historical base develops.

Will there by any increase in taxes owing by U.S. corporations because of changes in classification?

As you no doubt know, Customs charges are called "duties" rather than taxes. Customs collects for other governmental agencies certain taxes, such as Federal Excise taxes, and internal-revenue taxes on beer, wine, and distilled spirits. The issue of duty rate changes will be the subject of a separate question. However, if one is interested in possible tax changes due to Customs related activities, a prudent lawyer or corporate counsel would be well advised to study a recent (September 3, 1987) notice of proposed rulemaking published in the *Federal Register* (52 Fed. Reg. 33427-33431) concerning income taxes — limitation on taxpayer's basis or inventory cost in property imported from related persons. Basically, Code Section 1059A provides that a U.S. taxpayer who imports property into the U.S. in a transaction (directly or indirectly) from a person or persons related to the taxpayer, within the meaning of section 482 of the Code, may not claim, for purposes of computing the basis or inventory cost of the property, a greater cost than the amount of the cost taken into account for customs valuation purposes.

When will copies of the new tariff schedule be available?

Immediately. You can obtain a copy of the "Harmonized Tariff Schedules of the United States Annotated for Statistical Reporting Purposes (HTS)" by writing to the Superintendent of Documents, U.S. Government Printing Office, Washington, D.C. 20402-9325 and enclosing a check for $56.00 for mailing within the United States.

The November 1987 edition contains the legal text of the Harmonized Tariff Schedules of the United States. However, until the HTS is enacted into law, this edition of the HTS is being published without an effective date.

The HTS has been annotated to include such matters as may be necessary for reporting statistics formulated pursuant to section 484(e), Tariff Act of 1930, as amended (19 U.S.C. 1484 (e)). The statistical annotations contained in the HTS prescribe the statistical information to be supplied on customs entry and withdrawal forms with respect to articles imported into the customs territory of the United States. Thus, this publication is designed to enable importers, customs brokers, customs officers, and other interested persons to determine (1) the classifications and rates of duty applicable to imported articles and (2) the requirements for reporting statistical data with respect to such imports. This publication may also be used in place of the reporting codes of Schedule B for reporting exports on the Shipper's Export Declaration or under the program for electronic reporting of exports.

Can you make cross comparisons between the Tariff Schedules of the United States Annotated (TSUSA) and the Harmonized Tariff Schedule of the United States (HTS)?

Yes. The U.S. International Trade Commission (ITC) is preparing a cross-reference to facilitate the United States' expected ratification of the harmonized system, an international standard of six-digit classification codes designed to make tariff nomenclature uniform worldwide, on January 1, 1988. The ITC will also compile statistical tables for U.S. import and export trade for the years 1983-1987 using the proposed eight-digit HTS subheadings and ten-digit Harmonized System-based Schedule B numbers. ■

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Global Competitiveness in the 1990s

In which the author reports on recent speeches at the University of Delaware by three knowledgeable practitioners of international trade.

Lesley Ann Suddard

Lesley Ann Suddard is well prepared for the rigors of a global economy. A chemistry major with a minor in business administration, she graduated in January from the University of Delaware. She is literate in computer science, fluent in Spanish and French, and experienced as a paralegal. She has studied medieval history in France and general education at Duke University. Presumably she is the sort of renaissance type who must confront the uncertainties and perils of our national future.

☐ BJORN BAYLEY, President IKEA, North America

Unless one has lived the life of a hermit for the past three years, there is no way he could have missed the American debut of IKEA, the Swedish home furnishings retailer. The Plymouth Meeting Mall "hypermarket", a store offering only one category of products, has been a smashing success. Sales have surpassed all expectations by a wide margin. IKEA N.A. president Bjorn Bayley said that "We should sell furniture of good quality and design at prices so low that most people can afford to buy it." Evidently, most people in the Delaware Valley (and around the world) can and do.

IKEA operates in 18 countries, including the United States, Canada, Iceland, Europe, Africa, Singapore, and Australia. IKEA stores are mostly company owned. Only those located furthest from Sweden operate as franchises. "Prosumerism", that is making the consumer part of the production process, is the basis for IKEA's competitive strategy. IKEA does not do any of its own manufacturing or transportation. "IKEA is not in the business of shipping air around the world," says Bayley. Most IKEA furniture is shipped in flat boxes and requires some assembly by the consumer. In this way IKEA keeps prices down by reducing production and shipping costs. Although ninety percent of all items sold are designed in house, IKEA contracts with outside manufacturers to produce and to ship the finished product to IKEA distribution centers. IKEA, a retailer only, leaves the headaches of manufacturing and shipping to specialists and concentrates on marketing and selling.

The annual catalog, the heart of IKEA advertising, accounts for approximately 50 percent of the total marketing expense. Studies suggest that 58 percent

Bjorn Bayley

of those receiving their catalog keep it for three months or longer. Because the catalog binds prices for a year, IKEA tries to negotiate contracts with manufacturers at fixed prices for a year as well. To hedge against exchange rate fluctuations, IKEA buys futures in foreign currencies for a year at a time.

While the catalog is the primary tool for attracting people to the stores, the stores themselves are designed so that, according to Delaware shoppers, the merchandise "...falls off the shelves and into the shopping cart and out the door." Since IKEA's target market is families with children, it provides free babysitting and diaper-changing services, and a children's menu (including baby food and formula), allowing parents more time to shop.

On the sales floor, products are displayed in room settings, both to show different possibilities for furniture use and to provide decorating ideas. IKEA sells everything shown in their displays (except the appliances and electronic equipment), including fabrics, floor coverings, wall hangings, lighting, even

house plants. The price tags attached to the display furniture tell the customer just about everything that IKEA knows about the product: materials used, durability and recommended frequency of use, and package size and weight. There is a central information desk where additional questions can be answered, and where furniture too large to be handled in the self-serve warehouse bins can be ordered. Home delivery is available as well as assembly services, something particularly useful for business customers. IKEA charges separately for these specialized services instead of spreading the costs among all customers for services used by only a few.

There are other companies with self service or knock-down furniture stores, but no competitor has been able to duplicate the strong customer identification and recognition accorded IKEA, primarily because IKEA emphasizes its Swedish origins while promoting a "global village" marketing strategy. All items are available in all countries and catalogs are printed in the local language or dialect.

In many ways, IKEA is a victim of its own success. It is strapped for warehousing space, and customers have found many items out of stock, often for months at a time. Increasing the number of distribution centers to ease current supply shortages is crucial to IKEA's North American expansion plans, as is finding motivated and qualified workers.

A company with a corporate style that can only be described as casual, IKEA is nevertheless an impressive competitor, unwilling to overanalyze or get bogged down in details, lest a competitor beat it to the marketplace. For IKEA, speed as well as quality and prices, will determine who succeeds in the 1990s. ■

□ HARRY CORLESS, Chairman ICI Americas

Harry Corless, Chairman of ICI Americas (the American subsidiary of the English company, Imperial Chemicals), describes himself as a "total, absolute, unfettered, unambiguous advocate of world trade and free trade." He claims that the world as we know it today was discovered and developed by the drive to establish world trade.

International trade has had benefits beyond the merely material. Corless states, "International trade is the catalyst that has helped this interchange of goods,

Harry Corless

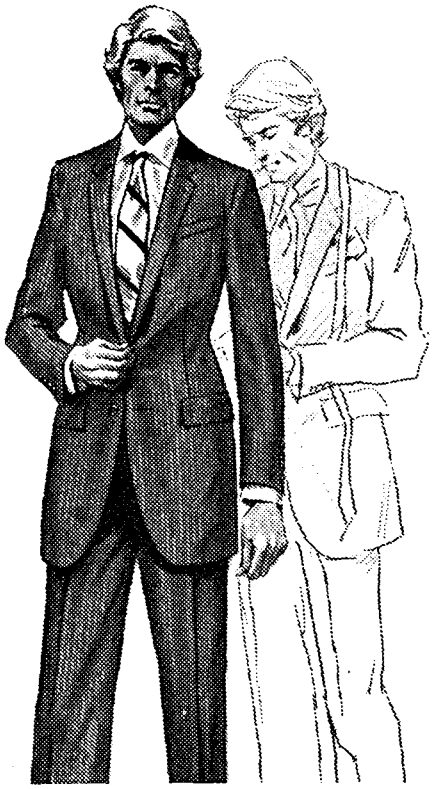
ideas, and cultures. It's the cement that holds international relationships together. And, in my view, this increasing dependency and interdependency of the world's nations is the most important single means of insuring a peaceful coexistence and avoidance of another major holocaust." He contends that economic factors have been a major cause of wars. The healthy global trade today shows that there is still a lot of trust between trading partners, as well as a lot of prosperity being created around the world.

The United States is facing significant challenges. Corless claims that a slowdown in productivity has resulted in American manufacturers becoming less competitive world-wide. Although U.S. manufacturers complain about "level playing fields", he feels that if they first took care of improving their own productivity and competitiveness, many of the problems would disappear. He is greatly troubled by the current pressure within the United States for increased protectionist legislation, citing the harm inflicted by the 1930 Smoot-Hawley Act.

Corless prescribes a simple regimen for United States manufacturers in pursuit of recovery: concentrate on "managing business properly, improving efficiency, effectiveness, and productivity, and being competitive in that way." He chided American management for its exaggerated concern over protecting its own backyard, even though the U.S. market is 30 to 40 percent of the entire world market.

Corless points out that ICI is based in a market (England) with only five percent of the world market. Founded in 1926, ICI concentrated on the U.K. market until 1971, when it acquired the Atlas Chemical Company in Wilmington and

(Continued on next page)



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