Impacts of Potential U.S. Trade & Tax Policy Changes on Automotive Trade Within The Great Lakes Region

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Today:

- Trump & trade
- NAFTA overview
- Will auto jobs come back to the United States?
- Other U.S. tax & trade policy proposals
- Ontario-Michigan cooperation
★ FIRST, I will announce my intention to renegotiate NAFTA or withdraw from the deal under Article 2205.
★ SECOND, I will announce our withdrawal from the Trans-Pacific Partnership.
★ THIRD, I will direct the Secretary of the Treasury to label China a currency manipulator.
★ FOURTH, I will direct the Secretary of Commerce and U.S. Trade Representative to identify all foreign trading abuses that unfairly impact American workers and direct them to use every tool under American and international law to end those abuses immediately.
NAFTA OVERVIEW
Brief NAFTA Automotive Trade Facts

- Top global vehicle producers:
  - U.S. ranks 2
  - Mexico ranks 7
  - Canada ranks 10
- NAFTA is a desirable global export base for automotive and parts:
  - U.S. has free trade agreements (FTAs) (20 countries)
  - Mexico has 17 FTAs with individual countries plus the EU (44 countries)
  - Canada has 12 FTAs with individual countries plus the EU (40 countries)
- 40% of U.S. light vehicles exported in 2015 were shipped to NAFTA partners
- 50% of U.S. light vehicles imported were shipped from NAFTA partners
- 75% of the value of U.S. automotive parts exports were shipped to NAFTA partners in 2015 (split roughly evenly between Canada and Mexico)
- 51% of the value of U.S. automotive parts imports came from NAFTA partners in 2015 (U.S. parts imports from Mexico represented three-quarters of these imports.)

Sources: (U.S. International Trade Administration, 2016); (World Input-Output Database, 2016) (Wilson C. E., 2011)
Share of Each Country’s Production That is Sold in the Same Country, 2015

Source: IHS Markit
U.S. Automotive Trade with Canada, 2011-2015
Imports and Exports for 3361 and 3363

Source: U.S. International Trade Administration
U.S. Automotive Trade with Mexico, 2015-2011
Imports and Exports for 3361 and 3363

Source: U.S. International Trade Administration
North American light vehicle production didn’t change much with introduction of NAFTA… but 2009 *did* change things

Canada and Mexico Light Vehicle Production: 1980-2016

Source: Ward’s Automotive
Mexican Automotive Wages are One-Eighth to One-Fifth the Wages Paid to U.S. Hourly Auto & Parts Workers

Average Hourly Wages for Production and Non-Supervisory Workers in Motor Vehicle and Parts in Current USD, 2007-2013/2014

Sources: U.S. Department of Labor, Bureau of Labor Statistics; Mexico National Institute of Statistics and Geography (INEGI: Instituto Nacional de Estadística y Geografía); CANSIM
Mexico is a Global Export Base for Autos and Parts

13 FTAs, 44 Countries

- North American Free Trade Agreement (NAFTA)
- Colombia - Mexico
- Costa Rica - Mexico
- European Union - Mexico
- Nicaragua - Mexico
- Chile - Mexico
- EFTA - Mexico
- Israel - Mexico
- Northern Triangle - Mexico
- Uruguay - Mexico
- Japan - Mexico
- Peru - Mexico
- Central America – Mexico

Note: Canada has FTAs with 40 countries; U.S. with 20 countries
Growth of Non-NAFTA Exports from Canada, Mexico & the United States: 2005-2023

Source: IHS Markit and Center for Automotive Research
Canada, Mexico & U.S. Light Vehicle Capacity Forecast, 2015-2023

Utilization

- United States: 95%, 94%, 98%
- Canada: 83%, 83%, 82%
- Mexico: 83%, 83%, 83%

Source: LMC Automotive
Every Global Auto Production Region Has a Low-Cost Source of Materials, Parts & Components

Share of Global Automotive Parts Exports (Total: $363B in 2014)

Source: BACI International Trade Database; Visualization from MIT Economic Complexity Observatory
# Automaker Investment Announcements

## 2009-2016

<table>
<thead>
<tr>
<th>Region</th>
<th>Total North American Investment Announcements</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Canada</td>
<td>$6.7 billion</td>
<td>6%</td>
</tr>
<tr>
<td>U.S.</td>
<td>$85.0 billion</td>
<td>73%</td>
</tr>
<tr>
<td>Michigan</td>
<td>$30.3 billion</td>
<td>26% of North America</td>
</tr>
<tr>
<td>Mexico</td>
<td>$24.7 billion</td>
<td>21%</td>
</tr>
</tbody>
</table>

Source: CAR “Book of Deals”
U.S. motor vehicle employment, output & productivity are up; is it technology, trade, or something else?

Rules of Origin Likely to Be a Focus of NAFTA Talks

- Current ROO = 62.5%
- Democrats proposal = 90%
- Possible “U.S. Peg”
- “Optical target” vs. “Hard Target”
come from the label

DOMESTIC CONTENT

\begin{itemize}
\item \textbf{Current ROO} = 62.5\%
\item \textbf{Democrats proposal} = 90\%
\item Possible “U.S. Peg”
\item “Optical target” vs. “Hard Target”
\end{itemize}

Tracing and calculation differences

Source: Center for Automotive Research Analysis; AALA, NAFTA & CAFE Rules & Regulations
U.S. & Canadian (AALA) Content by Segment

Sales-Weighted AALA Content Percentages, 2016

All Models

NAFTA 62.5% ROO

* Only Jeep Wrangler in this segment in 2016.

Source: Center for Automotive Research Analysis; AALA and Ward’s Auto.
WILL AUTO JOBS COME BACK TO THE UNITED STATES?
What Would It Mean to Bring Back Automotive Manufacturing from Mexico?

**Automakers**
Assume that small cars are produced elsewhere (45% of all Mexico exported vehicles to the U.S.), and that production facilities in Mexico that export to non-U.S. markets remain in Mexico

- Net add: 1 million additional units of U.S. capacity across 10 automakers
- Add 22,200 total automotive manufacturing related employees (17,640 hourly)
- New capacity investments would amount to an estimated $4.7B to $6.5B (CAR analysis due to current capacity utilization @94%)
- Costs could go higher—added U.S. capacity spread across 10 automakers

(http://www.cnn.com/2012/10/31/us/mexico-border-jeep/)
What Would It Mean to Bring Back Auto Parts Manufacturing from Mexico?

Suppliers
- Canada: largest export market for U.S. automotive parts ($22.0B); Mexico: a close second ($20.2B)
- 19% of Mexico suppliers are U.S.-based (18% Japanese, 12% Germany)
- Mexico’s auto supply industry employed just over 500,000 people in 2015 (460,000 hourly)
- Cannot determine what is OE/Aftermarket
- Potential to move back: JIT plants and other bulky, fragile, or otherwise difficult to ship parts and components

U.S. Automotive Parts Imports by System, 2015

<table>
<thead>
<tr>
<th>Parts Category</th>
<th>Mexico</th>
<th>Canada</th>
<th>Rest of World</th>
</tr>
</thead>
<tbody>
<tr>
<td>Engines &amp; engine parts</td>
<td></td>
<td></td>
<td>100%</td>
</tr>
<tr>
<td>Transmission &amp; powertrain parts</td>
<td></td>
<td></td>
<td>100%</td>
</tr>
<tr>
<td>Electrical &amp; electronic equipment</td>
<td></td>
<td></td>
<td>100%</td>
</tr>
<tr>
<td>Steering &amp; suspension parts</td>
<td></td>
<td></td>
<td>100%</td>
</tr>
<tr>
<td>Seating &amp; interior trim</td>
<td></td>
<td>20%</td>
<td>80%</td>
</tr>
<tr>
<td>Brake systems</td>
<td></td>
<td></td>
<td>100%</td>
</tr>
<tr>
<td>Automotive lighting equipment</td>
<td></td>
<td></td>
<td>100%</td>
</tr>
<tr>
<td>Parts not elsewhere specified or included</td>
<td>40%</td>
<td>60%</td>
<td>0%</td>
</tr>
</tbody>
</table>

Source: U.S. International Trade Administration
Reason #1 for pessimism: Talent

Unemployment Rates, 2000-2016

- # of Unemployed
- Transp. Equip. Unemp. Rate
- U.S. Unemp. Rate

Unemployment Rates, 2000-2016


Estimated Tooling Workload Hours Based on FCA, Ford & GM Planned Major/Minor Product Changes
Reason #2 for pessimism: It’s a truly global industry

If trade policy targets only Canada &/or Mexico, other countries will gain...

These countries are the top importers of parts, materials & machinery to the U.S.

**Global Locations of Top Six Automakers by Region, 2016**

- **TOYOTA**: 9 North America, 6 South America, 6 Europe, 31 Asia, 1 Africa, Total 44
- **GM**: 18 North America, 7 South America, 7 Europe, 6 Asia, 4 Africa, Total 24
- **NISSAN**: 5 North America, 1 South America, 5 Europe, 23 Asia, 4 Africa, Total 33
- **FORD**: 12 North America, 4 South America, 7 Europe, 8 Asia, 1 Africa, Total 20
- **FCA**: 11 North America, 5 South America, 12 Europe, 2 Asia, 2 Africa, Total 20
- **HONDA**: 8 North America, 2 South America, 2 Europe, 16 Asia, 2 Africa, Total 20

Source: U.S. International Trade Commission/Ward’s Automotive
Reason #3 for pessimism: We are at or near market peak

CAR U.S. Vehicle Production Forecast: 2016-2020

*Includes heavy duty trucks. Source: Ward’s Auto; CAR Research, October 2016
OTHER US TRADE & TAX POLICY PROPOSALS
35% Tariff With Mexico: Lower U.S. Sales Volume & Higher Prices

• Total 37,700 jobs lost minimum from 35% tariff
  – 450,000 fewer unit sales in U.S. (Implied loss of 6,700 U.S. assembly jobs)
  – In 2015, Mexican vehicle exports contained an average of 40.3 percent U.S. content (U.S. parts employment impact tied to parts & components adds another 20,000 U.S. parts jobs)
  – U.S. vehicle production contains an average of 11.7 percent Mexican content (add another 11,000 U.S. assembly jobs)

• There are two factors that could raise the jobs impact even further:
  – Parts and components cross the U.S.-Mexico border multiple times; taxing at each border crossing would multiply the impact of the tariff
  – Job losses would not be evenly distributed and would impact individual automakers’ and suppliers’ capacity utilization (plant closures and broader job impacts)
Border Adjustment Tax is Part of Several Comprehensive Corporate Tax Reform Proposals

A Better Way: Our Vision for a Confident America

- Lowers the effective corporate tax rate from 35 to 20 percent (Trump’s tax plan lowers the rate to 15 percent).
- Provides full and immediate depreciation for investments (tangible and intangible), which results in a zero percent tax rate on new investment.
- Cuts individual taxes on dividends and capital gains in half.
- Repeals the corporate alternative minimum tax (AMT).
- Eliminates most special tax deductions and credits.
- Includes and improves tax credits for domestic R&D.
- Ends the deduction for net income expense (can deduct interest expense against interest income and carry forward net income expenses).
- Includes a 100 percent exemption on repatriated profits from foreign subsidiaries.
- Implements the Border Adjustment Tax (BAT)

At this time, no legislation has been introduced
Border Adjustment Tax: Estimated Impact on U.S. Light Vehicle Prices

\[
(R_D + R_E) - (C_D + C_I) = TaxBase
\]
\[
R_D - C_D = TaxBase_{BAT}
\]

Methodology:

- Based on confidential financial data received from automakers representing over 50 percent of U.S. light vehicle sales
- Exchange rates constant; examined only a price response to the implementation of border adjustment
- Estimates of consumer price changes are based on:
  - Vehicle manufacturers’ change in effective taxable income
  - Changes in auto manufacturers’ input costs from the automotive parts sector
  - No change in unit sales or domestic production
  - No shifts in sourcing or production investments

Immediate responses to border adjustment:

- Automotive parts and material prices would increase by 8.4 percent
- U.S. light vehicle prices would increase 5.6 percent
- Average per vehicle price increases are estimated at $1,970
- Given 2016 U.S. sales at 17.5 million, the price increase represents an aggregate $34.6 billion in higher costs to consumers
Potential Obstacles to Implementing BAT

- International acceptance of, and reactions to, the adoption of a DCFT is an open question:
  - Is the DCFT a consumption tax, like the VATs employed in other countries, or
  - Is it an income tax?
- Will other countries
  - File objections with WTO?
  - Enact retaliatory measures?
ONTARIO-MICHIGAN COOPERATION
Greater Cooperation Between Ontario & Michigan

MOU recognizes mutual benefit from strong regional auto industry

- Concern about continued production (GM-Oshawa, FCA-Brampton & Warren)
- Continued improvement in border wait times—seamless supply chain
- Regional talent
  - Cooperation in skilled trades/TDM
  - Connected/automated vehicle technologies
Thank you

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