Labor Day 2010:

The Impact of Anti-Labor Policies on Working Men and Women

NATIONAL ASSOCIATION OF Manufacturers

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Uncertainty is no friend to the American worker, and it is uncertainty that overshadows Labor Day 2010.

With the already slow recovery losing momentum, widespread economic uncertainty is discouraging the investment that must take place if U.S. employers are to hire more workers and increase employee compensation.

The most striking—and distressing—economic number this Labor Day is that national unemployment remains well above 9 percent for the second year in a row. There are few indications that the rate will fall substantially in the year ahead, and a distinct possibility exists that unemployment could again top 10 percent before Labor Day 2011.

At the same time, wages are stagnant and likely to remain flat.

In “Labor Day 2010,” the National Association of Manufacturers (NAM) examines how workers have fared in the recession and recent recovery, with a focus on the manufacturing sector. Written and researched by NAM Chief Economist David Huether, the report explores the roots of the uncertainty that figures so prominently in public discussion of the economy.

Any serious Labor Day analysis of the U.S. economy and employment must address the uncertainty factor. Costly tax and regulatory proposals enacted or being considered by Congress and the Obama Administration make employers apprehensive, investors cautious and consumers anxious. Policies that expand government, taxes and regulations also pose serious questions about the ability of business in the United States to compete in the global marketplace. The predictable result is a faltering recovery and troubling times for U.S. workers.

To the extent that there is a bright spot in the recovery, it comes from manufacturing. Production has risen since economic growth returned in early 2009, and manufacturers have been hiring back at a somewhat moderate pace. Exports of manufactured goods have been strong.

More than any other sector of the economy, manufacturing has the potential to produce long-term opportunities for U.S. workers. Manufacturing not only drives productivity, it increasingly requires highly skilled workers whose expertise demands a wage premium.

Manufacturing played a major role in previous, stronger recoveries. Accordingly, “Labor Day 2010” contrasts the current recovery to its counterparts of the early 1980s and 2003, which both were marked by federal policies that encouraged investment and hiring.

The “Labor Day 2010” report further examines specific legislation, laws and regulations magnifying the uncertainty that afflicts the economy. Additionally, if poorly handled, the following factors—to cite just a few—will have a significant, detrimental impact on American workers:

- Expiration of the 2001 and 2003 tax cuts
- The Environmental Protection Agency’s (EPA) proposed new regulatory regime to control greenhouse gas emissions and raise energy costs
- Government implementation of the new health care laws, with their numerous mandates on employers, insurers and consumers as well as a myriad of unintended consequences
- Failure to achieve an ambitious trade agenda necessary to ensure and expand global market share for U.S exporters
- Labor policies, such as the Employee Free Choice Act, that could rob the U.S. economy of its dynamic growth potential

Finally, “Labor Day 2010” examines policies that would provide more certainty and improve U.S. global competitiveness. After all, an uncompetitive nation hires fewer workers and pays lower wages than dynamic and competitive economies do.

The report closes by proposing policies to strengthen growth, employment and wages not just in 2011, but for the decade ahead. These policies were first outlined in the NAM’s “Manufacturing Strategy for Jobs and a Competitive America” released in June 2010.

On Labor Day, America honors its working men and women—the workers and employees who contribute so much to our nation’s history, prosperity and strength. On Labor Day 2010, the NAM believes that by pointing the way toward a more competitive, more productive and more certain economy, we honor our workers and build a better nation.

Sincerely,

John Engler
President and CEO
National Association of Manufacturers

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Labor Day 2010 arrives at a time of great trepidation. Much of the United States' fledgling recovery was fueled by temporary measures, such as fiscal stimuli and business inventory restocking. Today, job losses continue, and the unemployment rate sits idle at 9.5 percent, higher than a year ago.

Business confidence in the recovery remains tepid. While some of this is explained by the severity of the 2007-2009 recession, firms also are concerned about the underlying global competitiveness of the U.S. economy. The combination of policy action and inaction in Washington contributes to the uncertainty.

Unless policymakers make the United States more competitive in the global economy, the prospects for American workers and employment could be discouraging for many years to come.

Section I: Taking Stock of the Great Recession

A year ago, the U.S. economy was at the tail-end of the longest and deepest recession in the post-World War II era. Joining a downturn in housing that began in early 2006, simultaneous declines in business investment, exports and consumer purchases of goods in 2008 caused the U.S. economy to fall by 4.1 percent from the fourth quarter of 2007 to mid-2009—the largest economic decline since the Great Depression.

As producers of consumer goods, business equipment, exports and housing materials, the manufacturing sector was especially hard-hit: From December 2007 to June 2009, manufacturing production fell 17.5 percent, more than two-times deeper than the 2000-2001 downturn, three-times greater than the 1990-1991 downturn, close to double the 1981-1982 downturn and more than half as deep as the decline during the first 18 months of the Great Depression. The downturn in manufacturing was as diffuse as it was deep, with production and employment declines taking place in all 19 of the major manufacturing industries.

During the 24 months ending last December, employment in the United States fell 6.1 percent (8.4 million jobs)—the largest decline of the past 60 years both in absolute numbers as well as in percentage terms. At the same time, the unemployment rate doubled from 5 percent to 10 percent, the highest level of jobs lost in nearly three decades.

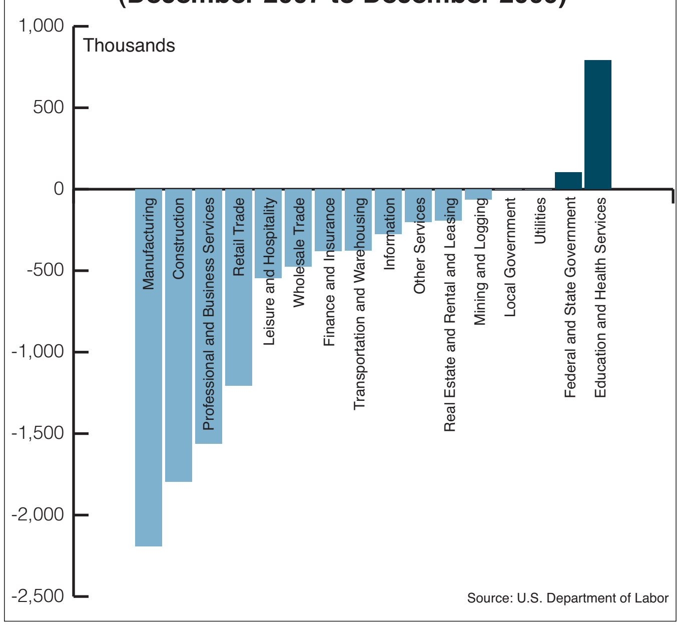
The depth of the employment declines during 2007-2009 was matched by their breadth. Of the 14 major private sectors of the economy, only one—education and health services—posted any significant job growth *(see Chart 1)*. The sectors hardest hit in the recession were manufacturing, construction, professional and business services and retail trade. Collectively, these sectors accounted for 40 percent of overall employment at the start of the recession but 80 percent of the losses by the end of 2009, with nearly one-half (48 percent) of the declines taking place in manufacturing (-2.2 million) and construction (-1.8 million) alone.

Section II: The Tepid Recovery

After declining for 20 consecutive months through August 2009, job losses continued through the end of last year, although the magnitude of the declines began to moderate as economic conditions finally began to improve.

The improvement was fueled largely by the beginning of an inventory rebuild after excess stocks were shed, a rebound in exports, eased lending standards by commercial banks and support from the American Recovery and Reinvest-

Chart 1: Employment Changes (December 2007 to December 2009)



ment Act (ARRA) of 2009 (the car allowance rebate system, homebuyer tax credits, Energy Star appliance tax rebates, temporary tax cuts for individuals and companies, extended unemployment benefits, aid to state and local governments, infrastructure projects, etc.).

After rising a modest 1.6 percent[1] in the third quarter of 2009 and accelerating to 5 percent growth in the fourth quarter, the recovery began to moderate in the first half of this year, slowing to 3.7 percent growth in the first quarter of 2010 and back to 1.6 percent growth in the second quarter, according to the Commerce Department's revised estimate.

While four consecutive quarters of GDP growth is good news, much of the increase was temporary in nature. More than one-half of the upturn in the economy over the past year was from business restocking inventories. Now, with inventory-to-sales ratios back to reasonable levels, this source of growth will likely fade.

In addition, some of the recovery in consumer spending was driven by short-term incentives. For example, the ARRA included $300 million in tax credits to purchase energy-efficient appliances. Most of these state-administered programs began in the first half of 2010, and consumers responded: Consumer purchases of major household appliances rose at a record 41 percent annual rate through the first four months of the year. However, 18 of these state programs have closed, and sales fell off significantly in May and June.

The end of the homebuyer tax credit in April caused a similar short-term surge in housing activity in the second quarter, with residential investment rising by 27 percent (SAAR). However, recent negative reports on building permits and housing starts early in the third quarter show that this program only provided a one-time improvement to the housing market.

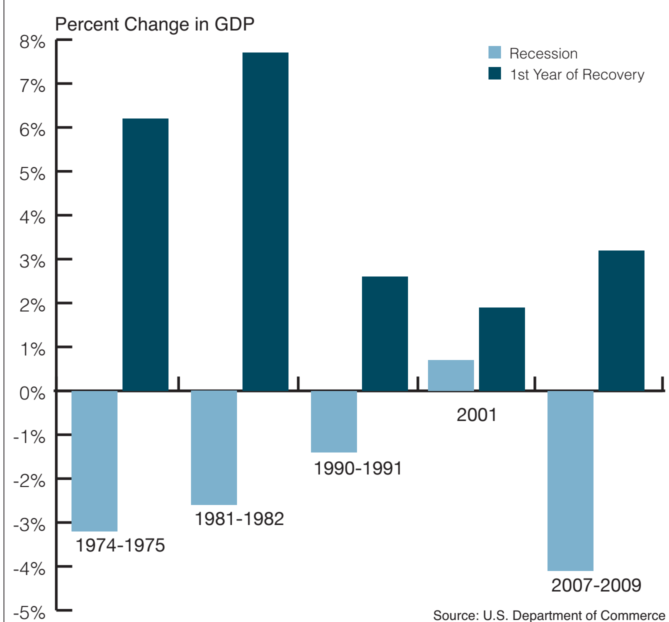
Finally, improvements in the global economy sparked a strong rebound in U.S. exports, which was very good news for manufacturers who account for nearly two-thirds of all U.S. exports. Rising at double-digit rates in each of the past four quarters, U.S. exports of goods increased 18.9 percent over the past year—the fastest four-quarter pace in more than two decades.

In short, after falling by 4.1 percent during the recession, the economy increased by 3 percent over the past year, due in large measure to the temporary factors mentioned above. And while the current rebound has been stronger than the initial upturns following the prior two recessions, which were mild by historic standards, it has been half as strong as the first-year recoveries following both the 1974-1975 and 1981-1982 recessions *(see Chart 2)*.

This pattern extends to the manufacturing sector. Due to the combined effects of inventory rebuilding, benefits from the ARRA and exports, manufacturing production increased 8.4 percent over the past year. Still, while the current recovery has been stronger than the initial year of growth following the 1990-1991 and 2001 recessions, it has lagged behind the recoveries that followed the 1981-1982 and 1974-1975 recessions. As a result, the level of manufacturing production remains 10 percent below the peak reached in the fourth quarter of 2007. By comparison, manufacturing rebounded to pre-recessionary levels of production after one year of recovery following three of the prior four recoveries.

If the pace over the past year is maintained going forward, U.S. manufacturing production will not reach its pre-recessionary peak until the fourth quarter of 2011, four years after the start of the recession. However, with much of the fuel from the ARRA already used, and most of the inventory rebuild now in the rear-view mirror, this outlook is not likely, especially given the fragile state of the labor market.

Chart 2: Recession-Recovery Comparisons



[1] Seasonally-adjusted annual rate (SAAR)

Section III: The Fragile Labor Market Demonstrates a Lack of Confidence

After falling for 23 of the 24 months in 2008 and 2009, the labor market slowly began to improve in 2010, with employment rising by 654,000 through the first seven months of the year. More than one-quarter of this increase was due to the hiring of temporary government workers to conduct the decennial Census. Many of these contracts have been fulfilled and the work completed.

Some employers are beginning to hire again, which is welcome news, but the pace of job creation thus far remains historically low. Following 2008-2009's employment decline—the largest (6.1 percent) of the post-World War II era—the employment increase during the first seven months of 2010 was the second-slowest pace on record since the late 1940s *(see Chart 3)*.

More than three-quarters of the 630,000 increase in private-sector employment so far this year occurred in the January-April period, when inventory rebuilding and fiscal stimuli were supporting growth. More recently, private-sector job growth slowed substantially: After increasing by 477,000 during the first four months of the year, private-sector payrolls edged up just 153,000 in the May-July period—a 68 percent decline in job growth. This anemic pace will not prevent the unemployment rate from rising in the coming months, which will weigh heavily on consumer confidence and spending in the near-term.

Another concern is that the job gains this year have not been very diffuse. Through the first seven months of 2010, 92 percent of the private-sector jobs created were concentrated in just three of the 14 major sectors of the economy: manufacturing, professional business services and education and health services. Collectively, the other 11 sectors,[2] which employ 59.8 million workers, or more than one-half of the private-sector workforce, increased payrolls by just 53,000 so far this year. Unfortunately, this trend is not on an upward path: After increasing by 105,000 during the first four months of the year, employment in these 11 sectors actually declined by 52,000 during the three months ending in July, clear evidence that employers' confidence in this fledgling recovery is faltering.

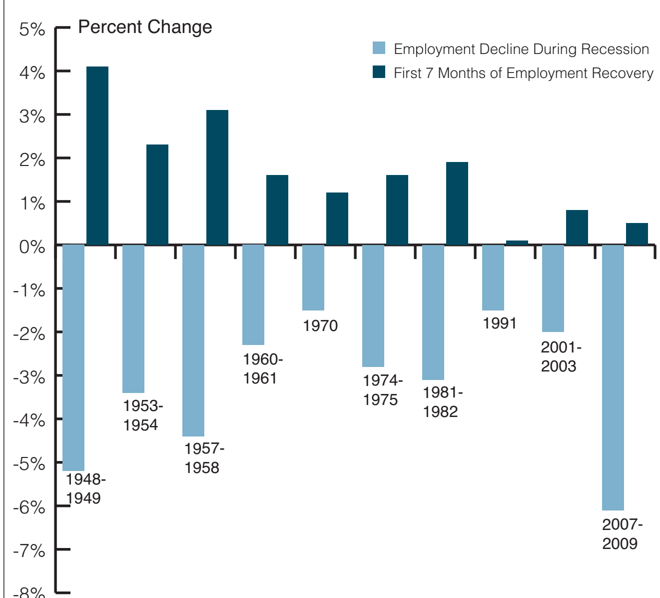
The rebound in manufacturing production generated employment gains on the factory floor in every month this year through July—a first in a dozen years. While encouraging, it amounts to just 8 percent of the manufacturing jobs lost during the 2007-2009 recession.

Moreover, the increase in manufacturing employment this year was concentrated in just five of the 19 major manufacturing industries: motor vehicles, fabricated metals, machinery, primary metals and plastics and rubber products. Collectively, these industries increased employment by 175,400 during the first seven months of 2010, accounting for 96 percent of the overall increase in manufacturing employment so far this year. Still, it is important to keep in mind that these industries alone lost over 1 million jobs in the recession, or close to one-half (47 percent) of the 2.2 million total manufacturing jobs lost in 2008 and 2009.

The modest employment increases in these industries are due to a number of factors, some of which were temporary in nature.

- First, plants in the motor vehicle industry were kept open in July when they typically are closed for retooling. This seasonal effect accounted for 40 percent of the gain in motor vehicle employment this year.
- Second, driven by 23 percent (SAAR) increases in both exports and domestic investment in industrial equipment, machinery output rose 19.8 percent (SAAR) through the first half of the year.
- These increases, along with a rise in construction activity in both residential and public infrastructure projects

Chart 3: Employment Comparisons



Source: U.S. Department of Labor

[2] Mining and logging, construction, wholesale trade, retail trade, transportation and warehousing, utilities, information, finance and insurance, real estate, leisure and hospitality, and other services

fueled by the ARRA, boosted the output of fabricated metals, primary metals and plastic and rubber products, which are inputs into motor vehicles, machinery and construction activity.

In the other 14 manufacturing industries,[3] which account for two-thirds of factory employment, job growth was virtually nonexistent, edging up just 6,700 so far this year.

With private-sector employment growth slowing, the unemployment rate remains uncomfortably high at 9.5 percent as of July *(see Chart 4)*, slightly above where it was a year ago (9.4 percent). Equally concerning is the fact that of those currently unemployed, nearly one-half (44.9 percent) have been out of work for at least six months. To put this number in context, prior to this recession, the percentage of Americans chronically out of work has not surpassed 26 percent of the total unemployed since the 1940s.

Unfortunately, there is little evidence that conditions will improve any time soon. After moderating last year, initial claims for unemployment have shown no sustainable improvement this year.

After edging down from a weekly average of 490,000 in January to 446,000 in April, initial claims rose to a weekly average of 482,000 in July, before surging to 504,000 for the week ending August 14, the highest level in nine months, before moderating slightly to 473,000 for the week ending August 21, still well above the historic threshold of 350,000 that is consistent with a healthy labor market. This is a worrisome sign that the labor market remains especially weak.

Section IV: Uncertainty — The Achilles Heel of the Recovery and Job Growth

The weak labor market has depressed both wage growth and consumer confidence. Over the past 12 months, real average hourly earnings edged up just 0.7 percent, while consumer confidence in July was 15 percent lower than it was at the end of last year and 40 percent below its level in the immediate aftermath of the September 11, 2001 terrorist attacks. This lack of confidence also extends to the business community. The latest (second quarter 2010) National Federation of Independent Business (NFIB) optimism index, while up from early 2009, is currently at a lower level than at any time during the prior three recessions.

The current level of business uncertainty is illustrated by the funds available to invest by companies sitting on the sidelines. As of the first quarter of 2010, net corporate cash flow (mainly undistributed profits and funds set aside to replace depreciating capital) stood at $1.5 trillion, or 10.5 percent of GDP. This level is significantly higher than any similar period (three quarters into an economic recovery) during the past 60 years and a clear sign that firms remain hesitant to expand operations due to concerns about the U.S. business climate *(see Chart 5)*.

Chart 4: The Current Employment Situation

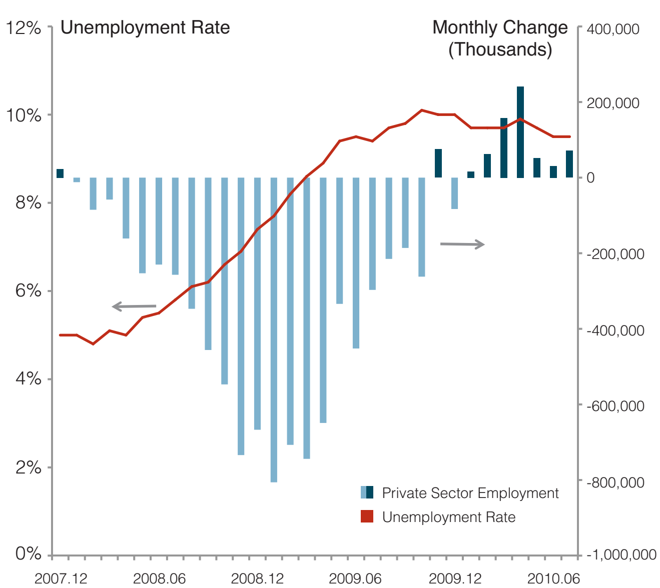
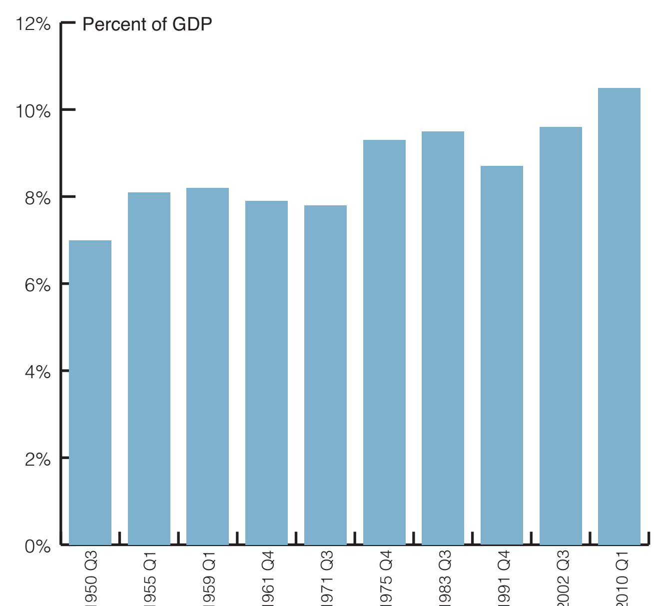


Chart 5: Corporate Net Cash Flow



[3] Electrical equipment, other transportation equipment, computer and electronic products, food and beverage products, textiles, petroleum and coal products, wood products, paper, apparel, nonmetallic minerals, printing, furniture, chemicals and miscellaneous manufacturing

Based on the results of the second quarter 2010 NAM/*IndustryWeek* Manufacturing Index, a survey of NAM member companies that began in late 1997, the causes of this anxiety appear to be two-fold.

Asked if uncertainty about the business outlook is delaying their plans to expand employment or capital spending, nearly three-quarters (74 percent) responded "yes." Of those who reported that uncertainty is affecting their expanding capital investment and hiring, the main areas of concern were the state of the U.S. economic recovery (46 percent) and possible regulatory or legislative changes from Washington (37 percent).

Businesses, workers and the American public simply have no clear sense of how actions by Congress and the Obama Administration could reshape the economy, employment and our country's ability to successfully compete in the global economy. Yet the impact on the economy and American workers of the following could be severe:

- Tax cuts passed in 2001 and 2003 are set to expire at the end of this year, increasing the tax rates for individual taxpayers and raising the maximum rate to nearly 40 percent. Nearly 70 percent of manufacturers are organized as pass-through entities, meaning they pay taxes at the individual rate and will be subject to these increases.

  Small businesses are America's job creators, responsible for 60 percent of the net new jobs created in the last decade. But uncertainty about looming tax hikes has stunted employment growth, and until Main Street begins to hire, the unemployment rate will remain unacceptably high.

- The United States now has the second highest statutory corporate tax rate among the major industrial countries in the Organization for Economic Cooperation and Development (OECD), trailing only Japan. Other countries have been regularly lowering their tax rates to encourage economic growth.
- Last year, the estate tax was finally repealed. However, without congressional action, the tax will return in 2011 with rates as high as 55 percent and an exemption of only $1 million not indexed to inflation. For family-owned manufacturers, planning for this tax takes money directly out of the business, making it difficult to expand and hire new employees.
- The research and development (R&D) tax credit, which encourages R&D activities that support high-skilled jobs in manufacturing as well as other businesses, expired at the end of last year and has not yet been renewed.
- Uncertainty surrounding a new regime from the EPA to regulate greenhouse gas emissions is curtailing new business investment and job creation.
- The health care reform package, enacted in March, continues to be implemented—some might even say written—by regulatory agencies. The size and scope of health care reform presents many challenges and uncertainties for employers, such as how the new laws will affect existing health plans sponsored by employers.

  It is unclear how much the changes in the laws will cost the average plan, but there is wide agreement that costs will increase for employers who wish to retain their status or purchase coverage that complies with the new benefit mandates and underwriting rules.

- Economic analysis of the Employee Free Choice Act (better known as "card check" legislation) by LEGC, a nonpartisan economics consulting firm, shows that if the bill were to become law, 600,000 jobs would be lost in the first year alone after its enactment. This analysis further shows that every 3 percentage points of growth in union density rates through card check schemes and binding interest arbitration would result in a percentage point rise in the national unemployment rate.
- The Paycheck Fairness Act would significantly expand the ability of trial lawyers to sue manufacturers for legitimate pay practices while doing little to address actual illegal acts of pay discrimination. This legislation would create a nebulous system of litigation for allegations of gender discrimination and would force employers to second-guess almost every pay decision they make.
- Successfully negotiating free trade agreements (FTAs) with Colombia, Panama and South Korea will increase U.S. manufacturers' export competitiveness. They have yet to be passed by Congress.

  Meanwhile, the European Union, which has 32 FTAs, recently concluded, is currently negotiating, or has announced FTAs with 17 additional countries. Beginning in January, the European Union's FTA with South Korea is expected to take hold and will begin to push U.S. exports out of the market.

  Assuming these FTAs are successfully negotiated, the U.S. will have FTAs with only 22 percent of the global economy and the European Union will have FTAs with 37 percent of the global economy.[4] By standing still, the U.S. is losing ground to our global competitors, resulting in heightened uncertainty about the competitiveness of the U.S. economy.

Section V: Policies Needed to Put the U.S. Economy and Manufacturing on Stronger Footing

In the aftermath of the deepest economic downturn since the Great Depression, and with the recovery showing new signs of weakness as the temporary boosts from fiscal stimuli and inventory restocking start to fade, now is not the time for policymakers in Washington to focus on an agenda that will increase costs, further elevate uncertainty and reduce the ability of our workers and companies to successfully compete in the global economy.

Instead, policymakers should focus their efforts on pro-growth, pro-worker and pro-manufacturing policies that structurally improve the competitiveness of the U.S. economy and increase the certainty that our country will remain the most competitive, dynamic and innovative economy in the world.

In June 2010, the NAM released a "Manufacturing Strategy for Jobs and a Competitive America" to address the fundamental challenges facing the U.S. economy. The Strategy highlights the need for:

- Tax policies to bring America more closely into alignment with major manufacturing competitors and foster innovation
- Government investments in infrastructure and innovation
- Trade initiatives to reduce barriers, open markets to U.S. exports and protect intellectual property
- A dynamic labor market that allows companies to attract the best, most talented workers from around the world to work in the United States
- A common-sense, fair approach to legal reform
- A regulatory environment that promotes certainty and economic growth
- A comprehensive energy strategy that embraces an "all of the above" approach to energy independence
- Health care reform that drives down costs

The U.S. economy, and manufacturers in particular, are part of a global economy. Our country's interdependence with the rest of the world poses significant challenges and offers huge opportunities. While companies' growth strategies were once domestic, they are now global. Now more than ever, it is critical that federal officials view their role in making economic policy through a global prism.

Our economy stands at a crossroads. The path our country takes will determine the long-term competitiveness of the U.S. economy and the American worker. With more competitive tax policies that encourage innovation and investment, lower and more certain costs in the areas of regulation, litigation and energy, and a committed effort to lower trade barriers overseas and support U.S. exporters, the prospects for a competitive U.S. economy that supports highly productive and compensated workers are very real. Without the right policies in place, the U.S. economy and the American worker will lose out to fierce global competition. The choice is ours to make.

[4] Outside the United States and the European Union

NATIONAL ASSOCIATION OF
Manufacturers

1331 Pennsylvania Ave NW, Suite 600, Washington, DC 20004 **P** 202•637•3000 **F** 202•637•3182 www.nam.org