STATEMENT

OF THE

ALLIANCE OF AUTOMOBILE MANUFACTURERS

BEFORE THE:

SENATE COMMITTEE ON FINANCE

SUBCOMMITTEE ON INTERNATIONAL TRADE, CUSTOMS AND GLOBAL COMPETITIVENESS

November 20, 2017

PRESENTED BY:

Mitch Bainwol

President & CEO

Thank you, Chairman Hatch, Chairman Cornyn and members of the Subcommittee. The Alliance of Automobile Manufacturers (Alliance) is a trade association of twelve car and light truck manufacturers comprised of BMW Group, FCA US LLC, Ford Motor Company, General Motors Company, Jaguar Land Rover, Mazda, Mercedes-Benz USA, Mitsubishi Motors, Porsche Cars, Toyota, Volkswagen Group and Volvo Cars. Together, Alliance members account for roughly three out of every four new vehicles sold in the U.S. each year.

On behalf of the Alliance, I appreciate the opportunity to offer our views on the modernization and re-negotiation of the North American Free Trade Agreement (NAFTA). The ongoing re-negotiations are at a critical juncture. The fifth round is currently taking place in Mexico City and this is the first time the three partners are re-grouping since the U.S. tabled a number of contentious proposals during the last round in early October. It is also very fitting that we are here in San Antonio, TX to discuss this important issue, as this is where the existing agreement was signed 25 years ago by President George H.W. Bush, Mexican President Carlos Salinas and Canadian Prime Minister Brian Mulroney. And, I remain hopeful that we will return here in 2018 to mark the signing of NAFTA 2.0 – a modernized NAFTA that builds on the agreement's existing benefits to further enhance this nation's global competitiveness and grow U.S. manufacturing and jobs.

Much has changed since 1992 and when NAFTA went into effect in 1994. Today, trilateral trade between the U.S., Canada and Mexico exceeds $1 trillion dollars – growing 370 percent since NAFTA went into effect.[1] Canada and Mexico are our largest export markets and 14 million U.S. jobs depend on trade with these two countries. In the auto sector, NAFTA has played a key role in our manufacturing renaissance. In 2016, 13 automakers manufactured 12.2 million vehicles in the U.S. –over one million more vehicles that were manufactured in the U.S. in the year before NAFTA took effect. The auto sector is the leading exporter of manufactured goods in the nation – shipping $137 billion in vehicles and parts to Mexico, Canada and the rest of the world in 2016. Last year, the industry invested $8 billion in U.S. plants and equipment

[1] Americas Society/Council of the Americas. http://infogram.com/nafta-by-the-numbers-1g9vp13ed6elm4y

and nearly $20 billion in R&D. In total, the U.S. auto industry currently supports more than 7 million American jobs – generating $500 billion in annual compensation and $205 billion annually in tax revenue. Thus, America's automotive industry has a significant economic stake in the outcome of the renegotiations of NAFTA – perhaps more than any U.S. industrial sector.

The significant growth of auto production in Mexico is often cited within the contentious debate surrounding the future of NAFTA. While, it is true that Mexico has experienced an increase in auto production since the implementation of NAFTA, the U.S. has seen major growth as well. According to the Organisation Internationale des Constructeurs d'Automobiles (OICA), in 2016, the U.S. ranked 2nd in total global vehicle production, Mexico 7th, and Canada 10th.

Since NAFTA took effect, 15 new manufacturing plants have been launched in the U.S. (more than Mexico and Canada, combined) and there has been substantial, multi-billion-dollar reinvestment in existing plants. These 15 new manufacturing plants have resulted in the creation of more than 50,000 direct and 350,000 indirect auto jobs throughout the U.S. In total, 13 automakers currently operate 44 assembly plants across 14 states and more are on the way – Volvo is currently constructing a $1.1 billion facility in South Carolina and Toyota-Mazda announced plans to build a new $1.6 billion facility in the U.S. as part of a new joint venture. Clearly, NAFTA has succeeded in attracting significant U.S. investment from within the global auto industry.

NAFTA has also incentivized investment in the North American region, as a whole, and strengthened the U.S. auto industry's global competitiveness. Global companies have shifted production from other automotive regions, like Asia and Eastern Europe, to North America to utilize the benefits of NAFTA and increasingly rely on North American supply chains. And it's important to note that facilities in Canada and Mexico support U.S. jobs as well. On average, a 10 percent increase in employment at a Mexican affiliate operation leads to a 1.3 percent increase in U.S. employment, a 1.7 percent increase in U.S. exports, and a 4.1 percent increase in U.S. R&D.[2] Auto manufacturing throughout the NAFTA region has helped anchor automaker

---

[2] Moran, T. H., and Oldenski, L., Peterson Institute for International Economics, *How U.S. Investments in Mexico have increased investment and jobs at home. In NAFTA, 20 Years Later*. July 2014

and supplier engineering and R&D operations largely within the U.S. In doing so, it creates and supports thousands of high-wage auto sector jobs.[3]

While NAFTA has provided numerous benefits to the automotive sector, automakers recognize that much has changed in the global economy since NAFTA went into effect in 1994. As such, we support the Administration's aim of modernizing this trilateral trade agreement and offer recommendations to further enhance the benefits of NAFTA. If implemented, these recommendations will significantly advance the guiding principles underlying the Administration's trade policy agenda by encouraging fair and free trade, increasing economic growth, promoting job creation in the U.S., and strengthening the U.S. manufacturing base:

- **Maintain strong and effective market access provisions within NAFTA:** Many of the aforementioned benefits created by NAFTA are due in part by the effective market access provisions granted for autos and auto parts. Specifically, duty-free access granted under the existing rules of origin generates the free flow of autos and auto parts throughout the North American region. It is important to note that the 62.5 percent regional vehicle content (RVC) requirement is the highest rule of origin of any trade agreement. A recent study by the Peterson Institute for International Economics concluded that making rules of origin stricter "would be bad for producers and lead to higher prices for consumers, without guaranteeing more US content will end up in final products.[4]"

- **Improve Regional Regulatory Cooperation:** A modernized NAFTA should encourage more effective regulatory cooperation on future standards to avoid unnecessary divergence. Regulatory streamlining across the region will further facilitate trade and reduce unnecessary costs and administrative burdens. Regulatory cooperation among the three NAFTA partners will help spur cooperation on the global stage, within the United Nations Working Party 29.

- **Formal recognition of U.S. motor vehicle safety standards (FMVSS) throughout the NAFTA region:** We recommend the U.S. utilize this opportunity to formally enshrine existing practice and include commitments in the agreement requiring Canada and

---

[3] Center for Automotive Research, *NAFTA Briefing: Trade benefits to the automotive industry and the potential consequences of withdrawal from the agreement.* January 2017

[4] Freund, C., Peterson Institute for International Economics, *Streamlining the Rules of Origin in NAFTA.* June 2017

Mexico to recognize FMVSS. This need not come at the expense or exclusion of other global standards.

- **Streamline customs procedures to facilitate cross-border trade flow:** As indicated above, in many cases automotive parts and components may cross the border as many as eight times before reaching final assembly. A modernized NAFTA should expressly allow true electronic signatures, (i.e. those that do not require the integration of a reproduced hand-written signature), requiring all three party-countries to accept them on NAFTA certificates. Reducing existing inefficiencies and burdensome border delays will help facilitate the free flow of these goods.

- **Update NAFTA's labor and environmental provisions:** The Alliance supports efforts to strengthen NAFTA's labor and environmental provisions to reflect a strong commitment to maintain a level playing field with parties to the agreement.

- **Promote cross-border data flows:** Since NAFTA is more than 20 years old, it lacks language on cross-border data flows. A modernized NAFTA should ensure that automakers are able to move data freely across borders to enable them to compete fairly to serve customers in North America and around the world.

While we support the Administration's goal to modernize NAFTA to bring the agreement into the 21st century, we remain concerned by the current trajectory of the re-negotiations. As previously noted, a number of contentious proposals were tabled by the U.S. during the last round of re-negotiations. I'd like to briefly discuss our industry concerns with two of the proposals: the auto rules of origin proposal and the proposed sunset provision.

With regards to rules of origin, it warrants emphasizing that the existing rule (62.5 percent regional vehicle content requirement) is the highest of any free trade agreement in the world. It has been effective in striking the right balance to ensure there are no free riders and that to take advantage of the NAFTA tariff preferences, manufacturers must source significantly from the North American region. During the previous round, it is our understanding that this Administration proposed the following changes to the auto rules of origin:

1) Increasing the RVC requirement from the existing 62.5 percent to 85 percent.
2) Establish a U.S. content requirement of 50 percent.
3) Expanding the "tracing list" to include all parts and materials using in the production of a vehicle or part.

Each element alone would have a negative impact on the auto sector. But, taken in its entirety, this proposal is unprecedented and would have significant ramifications on our industry and the U.S. economy, as a whole. No vehicle produced today could meet such an onerous standard. It is unlikely that any vehicle ever could, even if sourcing changes were made in an attempt to do so. Adding to the compliance challenge is the insufficient two-year phase-in of the requirements. Auto manufacturing is a very capital-intensive process with long lead-time requirements for production changes. Sourcing new components and implementing the necessary changes would certainly be a lengthy, multi-year process.

Rather than attempt to comply with such stringent rule of origin requirements, it may make more economic sense for manufacturers to pay the 2.5 percent vehicle tariff when exporting within NAFTA and/or shift production to other low-cost regions. This will increase an automaker's vehicle costs, but that increase is less than the cost of complying with the proposed U.S. rule of origin.

While we wholeheartedly support this Administration's goal of growing U.S. manufacturing and jobs, making NAFTA's auto rules of origin more stringent will have the opposite effect. By increasing vehicle costs and/or causing production to shift, the proposed rules of origin would reduce demand for U.S. built vehicles. This shift will have a cascading effect – leading to reductions in U.S. production, component sourcing, investment, exports and auto jobs, and ultimately increase vehicle costs for American consumers.

The Alliance wishes to echo the concerns of the broader business community regarding the Administration's proposal for a so-called sunset clause, which would cause NAFTA to expire every five years unless the three partners agree it should continue. If adopted, the resulting uncertainty would render any revised NAFTA agreement, meaningless – chilling investment in the US, Canada and Mexico and further weakening the region's competitiveness globally.

Such contentious proposals like those related to auto rules of origin and the proposed "sunset clause" beg the question, is an agreement amongst the three negotiating partners on a modernized NAFTA possible? Both Mexico and Canada have announced that they are strongly opposed to these provisions. At this point, it appears the re-negotiations are headed towards either an unworkable NAFTA or no NAFTA. Both outcomes would make the industry less competitive globally and raise vehicle costs.

Adding unnecessary costs to new vehicles is problematic in any circumstances. The average price of a passenger vehicle today is $35,000 and that figure is expected to continue to increase due to various safety and environmental requirements. Reduced U.S. sales volumes, increasing interest rates combined with extended loan terms and increasing lease rates are threatening vehicle affordability for consumers. Additional costs associated with an unworkable NAFTA rule of origin or no NAFTA would only add to this burden.

It should be noted that Mexico also has free trade agreements (FTAs) with 45 countries, giving automakers access to nearly half the global auto market tariff-free. The U.S., on the other hand, has FTAs with 20 countries, representing about nine percent of the global market. To grow U.S. jobs and reduce the trade deficit, the U.S. should be seeking to secure additional market access and new trade agreements with its key trading partners. The bottom line is, the problem isn't free trade, but rather it is that we don't have enough free trade agreements.

The Alliance stands ready to be a constructive stakeholder as the Administration moves forward with the modernization of NAFTA. In his remarks at the signing of NAFTA, 25 years ago, President George H.W. Bush declared "this agreement will remove barriers to trade and investment across the two largest undefended borders of the globe and link the United States in a permanent partnership of growth with our first and third largest trading partners." NAFTA has succeeded in creating a strong regional bloc and enhancing American competitiveness in this global economy. Modernizing this trade agreement provides a unique opportunity to expand the benefits that this North American partnership has provided to our nation's economy and further expand job creation within the U.S.

Thank you for the consideration of our views.