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Deloitte Debates

Bring manufacturing jobs home!

Manufacturing jobs: To repatriate or not to repatriate, that is the question.
The gap in structural costs between U.S. and offshore manufacturing operations has shrunk significantly in recent years – down to 17.6 percent in 2008 from nearly 32 percent in 2006 [1]. Some say this trend creates new strategic options for facility and supply chain planning. Others argue that two of the structural drivers – energy costs and taxes – will make it impossible for U.S. manufacturing to regain competitive advantage. Which raises the question: Is it time to start bringing manufacturing jobs back to the U.S.?

Here's the debate:

	Point	Counterpoint
It's time to repatriate jobs. *The opportunity is real and immediate.*	Structural costs are heading in the right direction. Early movers in certain industries can capitalize on this trend to gain competitive advantage.	Seventeen percent is a big number. Until the gap gets closed and stays closed, there's no reason to place bets on an uncertain future.
	Industry leaders are pushing policy-makers for tax incentives and energy policy that will make U.S. manufacturing competitive again.	An industrial manufacturing facility can have an expected lifespan of up to 50 years. Meanwhile, the U.S. is unable to set and maintain a coherent, stable tax and energy policy. This is just wishful thinking.
	It's not all about cost. Quality and intellectual property are big risks in offshore manufacturing. So are supply chain disruptions. Customers won't wait 30 days for their orders to arrive from abroad.	You can cover a lot of risk with a 17 percent cost advantage.

	Point	Counterpoint
	The cost and supply of U.S. talent offer significant advantages right now. First movers will benefit from an eager labor pool – and the good will of American consumers.	Sure there are a ton of unemployed people, but top talent is still hard to come by in the U.S. Other countries have just as much talent to offer, if not more. And at a better price.
The good old days are gone. *The smart move is to stay focused on managing offshore manufacturing more effectively.*	Heavy manufacturing needs reliable, cheap and renewable energy. U.S. energy costs are simply too high.	When you factor in transportation expense and the risk of supply chain disruptions, the energy-cost differential between U.S. and offshore manufacturing largely disappears.
	The U.S. ranks behind every industrialized country (except France) in economic activity devoted to manufacturing – 13.9 percent, down 4 percentage points in a decade [2].	The trend is reversing. Six percent of U.S. manufacturing firms in the northeast moved outsourced jobs back to the states last year [3]. And it will continue to reverse. U.S. policy-makers know manufacturing is critical to long-term economic prosperity.
	The U.S. cost of talent dwarfs that of thriving offshore markets. That's a big piece of the puzzle... and it's not changing anytime soon.	It's changing already. Costs of labor in other countries are on the rise. Besides, it's not all about labor. Innovation, productivity and automation play a big role in reducing the overall impact of talent costs.

My take

Dmitri Shiry, Partner, Deloitte LLP

For the first time in years, American producers are seeing signs that their cost position relative to foreign rivals is improving. A recent study shows that the U.S. cost burden for five key structural elements has narrowed to 17.6 percent in 2008 from 31.7 percent in 2006 [4]. This means that domestic manufacturers spend 17.6 percent more on taxes, natural gas, employee benefits, torts and pollution abatement than a foreign competitor making a comparable product. Although the burden is still significant, the fact that the gap closed from 31.7 percent in just two years is meaningful change.

One reason for the improvement is that other countries are experiencing increases in non-wage costs. Canada and the United Kingdom are seeing health care benefits go up as supplemental private insurance becomes more popular. Increasing tort claims are impacting other European countries, and China is being affected by rising pollution control requirements. Another factor is that some costs in the U.S. are easing. For example, domestic manufacturers have softened benefit expenses by moving toward less expensive defined contribution plans.

For some manufacturers, though, the double hit of high energy costs and taxes can trump all other considerations. And unless policy-makers align incentives to encourage the repatriation of jobs, today's positive trends could be short-lived.

The U.S. tax rate is still among the highest overall corporate rate for industrialized countries. This is especially challenging because it has remained largely unchanged since 1986, while other countries have aggressively lowered their rates. High-tax environments may discourage capital investment.

In terms of energy costs, America has the ingredients to create a sustainable cost advantage. Ten years ago, for example, U.S. manufacturers enjoyed a cost benefit, paying less than their foreign counterparts for natural gas. Unfortunately, this advantage has largely dissipated. A revised energy policy regarding natural gas, a cleaner fuel compared to other energy sources, could help restore an energy cost advantage.

That said, some companies in some industries are looking hard at jumping on the repatriation bandwagon. This is especially true for those where the intellectual property and quality risks of offshore operations aren't worth the benefits of lower manufacturing costs. If the U.S. is going to reestablish manufacturing as a catalyst for growth during the next cycle of economic recovery, that trend will need to continue and expand.

A view from the talent perspective

Tom Morrison, Principal, Deloitte Consulting LLP

Manufacturers are facing a global talent crisis. The crisis is not about the availability of workers for jobs that require technical skills. It is about a mismatch of the availability of these skills where manufacturers want them most. This skills shortage is exacerbated by an aging workforce and the increasingly global nature of business. With each geographic region of the world presenting its own unique talent challenges, manufacturers need to weigh talent issues as part of any major business restructuring, including the repatriation debate. Quite simply, talent development, retention, and management are major priorities – no matter where jobs are located.

As companies consider and shift production to U.S. sites, they will face growing challenges in finding and keeping the right set of employees. Skilled technicians, plant operators, and engineers may be hard to find. Innovative approaches to training, development, and retention can help improve the availability of workers with the right skills and the incentive to stay. Relative to many countries around the world, the US and many states do not offer the types of training programs and incentives that can be found in other countries to assist in developing the right skills, exacerbating the shortage. Companies should consider investments and partnerships with local technical schools, community colleges and universities as a means of building talent pools and pipelines. We believe these training and development partnerships will be critical for new skilled workers and ongoing training to keep the workforce up to date. Companies and communities with plans and a commitment to skills development and retention will likely have a leg up.

A view from the tax perspective

Todd Izzo, Partner, Deloitte Tax LLP

Taxes can play an important role in encouraging companies to expand in the U.S. If the U.S. were to adopt tax policies that encouraged domestic investment in capital and labor, such actions could further reduce the structure gap in costs between U.S. firm and their foreign competitors. Unfortunately, U.S. tax policy currently discourages repatriation of foreign earnings both through its imposition of tax on a worldwide basis and by its high rate on corporate income.

Current policy debates in Washington are focused on raising taxes and reinforcing the current system rather than on new approaches to business taxation. The tax increase proposals put forward by the Obama Administration reflect ideas that have been discussed since the 1960's. Such proposals have been unacceptable to Congress in the past and will likely be largely unacceptable now. This continuing debate over proposed patches to the current system means that businesses, both domestic and international, experience the U.S. tax code as inherently unstable and unreliable. The result is that incentives are effective in shaping short-term behavior but blunted in their long-term impact.

Congress has an opportunity in the next few years to strengthen U.S. manufacturing by convert the conversation about raising business taxes into a serious conversation about fundamentally reforming business tax rules to encourage investment in labor and capital.

For more information, please visit: www.deloitte.com/us/debates/bringjobshome.

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A new cost study, released by The Manufacturers Alliance/MAPI and The Manufacturing Institute of the National Association of Manufacturers, updates the original ground-breaking study released in 2003 that benchmarks cost structures in the United States vs. the country's nine major foreign competitors. The study reveals that the corporate tax burden has widened steadily in the last five years, while the aggregate structural cost disadvantage to U.S. manufacturers subsided between 2006 and 2008.

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[1] The Tide Is Turning: An Update on Structural Cost Pressures Facing U.S. Manufacturers, The Manufacturers Alliance/MAPI and The Manufacturing Institute, November, 2008.
[2] Dale Buss, "Rethinking manufacturing strategy", Chief Executive Magazine, August 2009
[3] Dale Buss, "Rethinking manufacturing strategy", Chief Executive Magazine, August 2009
[4] The Tide Is Turning: An Update on Structural Cost Pressures Facing U.S. Manufacturers, The Manufacturers Alliance/MAPI and The Manufacturing Institute, November 2008