The Global Economy

Simon Constable

A New Production Cycle

If you're making products in China that sell big in the US, the steady talk about tightening trade between the superpowers certainly can't be great news. In fact, it's terrible news.

But at least one company has already made news that analysts say will have a preemptive affect: a large maker of electronics announced plans to move a big plant to Wisconsin. Analysts say they think others will follow, raising these firms' labor costs but giving them local tax breaks and wiping out any tariff threat. "There's been a change in the zeitgeist that is pushing companies to manufacture closer to their customers," says Alan Tonelson, founder of public policy blog RealityChek and a veteran analyst of international trade.

It's one of those topics that is easy to gloss over: international trade. Indeed, despite widespread coverage on it in most business publications, even pretty savvy CEOs can tend to ignore it. But smart business leaders shouldn't avoid it. Trade poses a huge threat to businesses everywhere. For now, for example, it is creating a bundle of uncertainty for corporate chieftains who are trying to figure out future costs and potential roadblocks to business.

Trade restrictions have become ever looser over the past few decades. The 1994 passage of the North American Free Trade Agreement (NAFTA) has allowed the unfettered flow of goods between Mexico, Canada and the US for almost a quarter of a century. A year later, the World Trade Organization was created to help facilitate broader international trade. The 164-member group decides the rules that form the bedrock of cross-border business. More free trade is no accident. It came about to avoid a repeat of the deep trade war in the 1930s, which helped spark the Great Depression. The most famous trigger for that debacle was the Smoot-Hawley Act, which raised tariffs on imports into the US. No one wants a repeat performance, hence the move toward freer cross-border trade.

That is, until now. Last year's US election showed that many voters view free trade as a job-killer. Politicians—including one very notable one sitting in the White House—have taken notice and are now marching to the drumbeat of "fair trade," not "free trade." Meanwhile, the United Kingdom is negotiating its exit from the European Union. The country's prime minister, Theresa May, has repeatedly said, "'No deal' is

better than a bad deal," which may sound like a threat.

Does this mean the world will be plunged into a recessionary trade war? Hopefully cooler heads will prevail. People like May know that the cost of a full-scale trade war would be awful. But they also need to get reelected, which tends to blunt the resolve of lawmakers. The true saviors may be corporations, which will manage to work around the problem —after all, business is the practice of solving practical problems as opposed to theoretical ones.

While other firms fret, innovative companies will find ways to work around any global trade wars.

One such solution presents itself because there is no longer a need for one centralized location for production of goods that then have to be transported across national boundaries, perhaps incurring punitive tariffs. Like the large electronics firm moving to Wisconsin, some companies already are planning ahead based on the mere threat of tariffs. "Since Trump became president, we have had a number of companies announcing that they will move production to the US or are thinking about it," says Tonelson. That includes, by the way, one big name: Samsung, the South Korean multinational, which is planning to produce refrigerators in South Carolina.

But who says you have to move production? One trick, says Joe Brusuelas, chief economist at professional services firm RSM, is to "innovate" and rely on the relatively new technology of 3-D printing. It can easily allow small quantities of goods to be produced locally. More old-school would be to rely on more foreign partnerships and licensing agreements as well. General Motors and Toyota ran a partnership for decades, while British brewer Wells & Young brews Japanese beer Ichiban locally in the UK, as just two examples.

"What is really needed is to have a company that is truly multinational," says Don Coxe, chairman of financial advisory firm Coxe Advisors in Chicago, also noting the importance of managers with a different view about producing. "Since the beginning of the British and Dutch Empires, you have generations of young men learning to find the lowest cost area to produce wherever the company was based."

Corporate leaders, of course, can get ahead of any problems by consulting with political risk experts who have a clear idea of where trade negotiations are going, and make contingency plans. Whatever those plans, they need to remember this: The world is now different. "There has been a fundamental change," says Coxe. "Leaders need to accept the basic fact that we have passed the height of free trade."

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