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ECONOMICS: US PERSPECTIVES

US GROWTH DYNAMICS AND GLOBALIZATION

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While the US economy remains stuck in a slow growth path, policymakers and analysts are hard pressed to explain the sluggish performance. Up to now, they have focused mainly on debt dynamics and how large debt positions could potentially hamper growth prospects. Still, the growth problem may be much more complex, and powerful global forces may be equally, or even more, important.

Globalization and the US Economy

General Electric CEO Jeffrey Immelt gave an interesting speech titled "The World I See" to the graduates at New York University's Stern School of Business on May 20, 2016. The speech offers an insightful and thorough discussion of how GE, its workers, its shareholders and the US economy in general have benefited from globalization.

Immelt noted that when he joined GE in 1982, 80% of the company's revenue stemmed from sales in the US. In 2016, 70% of the company's revenue will come from sales outside the US. This global shift, he argues, "has helped us [GE] become more efficient, more competitive."

GE is certainly not the only US firm to expand its global footprint. Nor is it the only US company that has grown stronger and more effective by embracing the world markets. Nonetheless, it stands as a very good example of how a firm—and a nation's economy, for that matter—needs to innovate and expand beyond its borders to thrive and offer better job and income opportunities for its workers.

Prescient Pre-Brexit View on Global Distrust

Yet today, Immelt argues, the global strategies of companies (and governments) are being attacked everywhere in the world—compelling companies like GE to rethink their operating strategy. According to him, the economic benefits of globalization have come under fire, leading some countries to reposition themselves. As a result, potential trade barriers are rising.

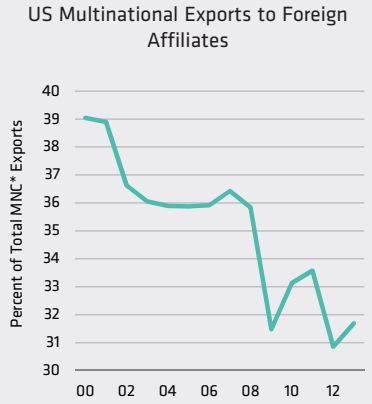
Immelt's speech took place about a month before the UK's Brexit vote. So his comments about the rising distrust building globally appear quite prescient.

In response to the global headwinds, Immelt said that GE will make a "bold pivot." For his company, that means "sustainable growth will require a local capability inside a global footprint." In other words, GE will seek "greater local production," requiring less global trade and fewer shipments from parent to affiliates and vice versa.

Globalization in Reverse—Going Local

Unfortunately, it's hard to get good real-time data to ascertain whether this "local initiative" is already under way among US multinational companies. But in checking trade flows for these companies (as published by the Bureau of Economic Analysis), our research does indicate that US companies have been "trading less" with their foreign affiliates for some time (*Display 1*). However, it's not readily apparent what the reasons are for this downshift. Nonetheless, if the GE "bold pivot" plan becomes the dominant operating strategy of US multinationals, the outward trade with overseas affiliates will continue to shrink.

Display 1
Less Trade Dims US Growth and Investment Prospects



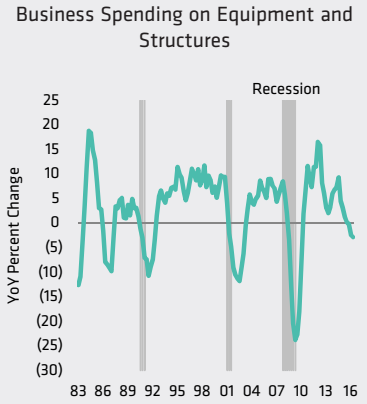
* Multinational Companies
Through December 31, 2013
Source: Bureau of Economic Analysis and Haver Analytics

Why is this important? History shows that US multinational companies have been at the forefront of innovation. They are also the largest investors in the American economy. Moreover, as these multinational companies have expanded their global footprint, activities of foreign affiliates have often complemented activities at home—leading to more growth opportunities for the parent companies and more investment in the home market.

Today, business investment in equipment and structures is contracting, having declined nearly 3% in the past year. At this stage of the business cycle, a decline in business investment is unusual, and one has to go back 30 years, to a period marked by the hollowing of the US manufacturing sector, to find another episode that is somewhat similar to today's trends (*Display 2*).

As policymakers and analysts continue to look for reasons why US economic growth remains subpar, we think it would make sense to focus on the factors behind the weak trends in US business investment. Companies seem to be unwilling to commit to new growth initiatives. And without a "bold pivot" on government trade policies that opens new markets and reduces trade barriers in existing ones, the US economy could well stay in a rut for some time to come. ■

Display 2
Has Going Local Hurt Investment at Home?



Through June 30, 2016
Source: Bureau of Economic Analysis and Haver Analytics