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Impact of Globalization and Trade with China on New York State Companies and Communities

My name is John Perrotti. I am President and Chief Executive Officer of Gleason Corporation ("Gleason") which is headquartered in Rochester, New York. Gleason, founded in 1865, is the world's leading provider of gear production solutions. Our company designs and manufactures advanced machinery and tooling used in producing all types of gears. We have approximately 8,000 customers around the world operating in a variety of industries including automotive, energy, truck, construction, industrial equipment, aerospace, marine and power tools.

Gleason is a global company. We have nine manufacturing plants around the world including three in the United States, four in Europe and three in Asia. Our three factories in Asia include two small facilities recently opened in Suzhou, China to support that rapidly expanding market. Gleason sells to over forty countries each year with 75% to 80% of our total sales outside of the United States. To support our global customer base we have 2,400 employees located in twenty countries throughout the world.

Gleason participates within an industry sector called "machine tools". Machine tools are metalworking machinery that have sophisticated computer-based motion control systems which allow the machine to perform a range of tasks with high productivity and repeatability while achieving high precision levels. Machine tools represent the "engine" of manufacturing and the advances in machine tool technology have been a vital part of the remarkable strides made in manufacturing productivity in the past decade. The United States as recently as the 1980s was the global leader in this technology and in the production of machine tools, but today with a general decline in manufacturing within our country, the United States is now barely in the top ten producing countries of machine tools. Japan and Germany, who consider machine tools as vital to their long-term economic prosperity, have emerged as the technology leaders. China and Taiwan are also top producers of machine tools, but typically with less technologically advanced products. In the past two years China has consumed 25% of all the machine tools produced in the world. China is purchasing more than two times the amount of machine tools compared to the next highest country. The United States had historically also been the largest global consumer of machine tools. This again highlights a worrisome trend about the state of manufacturing within our country.

With compelling statistics such as China purchasing one out of every four machine tools in the world it becomes apparent that participants within our industry need to actively serve this market. Fortunately for Gleason, we have a long history in China. My understanding is that Gleason was the second company (after Boeing) to ship product to China in the early 1970s after trade was established under the Nixon administration. Our sales and service branch in China started in 1985 and currently there are more than 2,000 of our machines installed in China. In 2008, Gleason Corporation on a global basis had record high new order levels with approximately one-third of those total orders coming from customers in China. In the second quarter ended June 30, 2009, China accounted for two-thirds of our new order volume for machines albeit at lower levels than last year due to the global recession.

Today, we have approximately 60 employees located throughout China supporting our sales and service activities. In the past two years, we have started producing machines and the consumable cutting tools used on our machines in Suzhou, China. Today our manufacturing presence in China is on a relatively small scale with about 40 employees and a few million dollars of sales from the products we produce there, but we realize to succeed in the long-term in this large and growing market we need to have an even greater local presence.

One of Gleason's largest factories is located here in Rochester. This factory makes advanced machinery for the production of bevel gears. This factory similar to our entire company counts China as one of its key markets. More than 70% of the total machines that Gleason has shipped to and installed in China over the past thirty five years were produced in our factory in Rochester.

I cannot state strongly enough that the Chinese market is critical to Gleason's future growth and survival. The growth in the Chinese economy has had a direct and significant benefit for Gleason in the past and its importance in the future appears even greater. However, Gleason is not alone in selling its products into the Chinese market. Because of the technical sophistication of our products most of our competitors are European and Japanese. These competitors are very aggressive in selling their products into China and are also establishing local operations to manufacture and support their products. There are Chinese companies manufacturing products similar to ours, but they are generally still perceived to be a level lower in terms of technology. Our local Chinese competitors are a mix of state-owned enterprises and privately owned Chinese companies. Today, our Chinese competitors are primarily serving their local market and are only exporting a small percentage of their products. However, each year they advance further in their technological development and no doubt will become global competitors in the not too distant future. These Chinese firms are aggressive and are continuing to invest with the ability to acquire the same advanced components and production equipment we use to manufacture our products. Chinese universities are graduating more than ten times the number of engineers compared to the U.S. which will form a strong and technically competent labor base for the future. I see the emergence of China as not totally different from the rise in the manufacturing base in Japan and Korea over the past decades.

Of course, one potential difference is the involvement of the Chinese central government in sponsoring these industries. The Chinese have certain industries which they see as critical to their long-term growth and security. They recognize machine tools as one of these key industries. As such the machine tool companies which are state-owned companies have access to capital which in a true free market would probably not be so readily available. Certain of these companies would not survive based upon their own financial performance. Universities are subsidized to support research and development of higher level engineers and certain incentives are offered to multinational companies, particularly those bringing advanced technology or R&D centers, to China. Incentives for companies to expand in China are not so different than those generally offered by state governments within the United States, including tax holidays, training grants and low-cost loans. In addition as a result of certain government policies many of the basic expenses of doing business, including health care, energy, acquisition of certain raw materials and regulatory costs are less in China compared to many other countries. As their currency is not freely traded, many economists estimate it is artificially weaker by some 40% further fueling Chinese manufacturers' ability to export. China also has significantly lower corporate tax rates than the United States, but this unfortunately is not that unusual as most of the industrialized world has lower corporate tax rates compared to our country and our state.

Why did Gleason decide to establish a local manufacturing presence in China? The primary reason being it is now the largest single global market for our products and still growing at a double digit percentage annual rate. Our European, Japanese and Chinese competitors continue to expand their capabilities in serving this market. Gleason to compete effectively must have a robust local infrastructure in order to provide price-competitive products and the required technical support to our customers. Because of the geographic distance and language barriers in doing business in China the only way to have significant market share for certain products is to be present in the local market. We manufacture some of the key sub-assemblies for the products we make in China here in Rochester creating incremental business which would otherwise not exist.

Gleason did not begin production in China to capitalize on low labor rates or to make it an export hub for our products. We may export from China in the future but our primary mission is to serve the large and growing local market. Another objective in expanding in China is to build our technical staff which can bring value to us not only in China, but on a global basis. With manufacturing becoming a smaller part of the overall U.S. economy, one of the unfortunate consequences is the supporting infrastructure including university research, supply chain and availability of technical talent is diminishing within our country. We find ourselves more and more looking abroad for higher level technical talent. Gleason positions itself as the technology leader within our industry so this is an area where can make no compromises. We must have the best and brightest engineers to maintain our market leadership.

So what government policies would Gleason like to see to support our continued success and ability to create jobs here in the United States? First, we cannot afford any form of protectionism, certainly not when our global competitors are under no such restrictions. We cannot let political agendas interfere with free trade. There are certain minimum expectations we should have of our trading partners, but these expectations need to be aligned with the global community or else we will put American companies at a severe disadvantage which will have far worse consequences than what one was trying to guard against in the first place. I have a personal core philosophy of "starting with the man in the mirror". Blaming China, for example, for the decline in our manufacturing base or job losses is energy largely wasted in my judgment. The majority of the manufacturing jobs lost in our country and state over the past two decades are generally not because the “jobs have been shipped to China” but because the jobs in many instances have been replaced by automated solutions. For example, a battery of five Gleason machines today can do what fifty machines used to do twenty years ago. Today there is typically one person operating the five machines compared to what may have been fifty operators creating the same output in the past. By the way, the Chinese today employ fewer in manufacturing jobs compared to just a few years ago because of the very same automated solutions which they now use in their factories. However, it is clear that building and maintaining a strong manufacturing sector seems to be a more critical priority for many countries, including China, than for the U.S.

Have U.S. companies shifted some of their manufacturing capacity to China; the answer is clearly “yes”. The reasons why will vary by company, but in part it is to support that growing market as is mainly the case with Gleason and in part it is because there is generally a significantly lower cost of doing business—all around, not just labor cost. For most producers the direct labor cost is a relatively small component of their overall product cost. It is all the items discussed previously including taxes, regulatory and health care costs where U.S. policy can help manufacturers.

In addition to lowering the costs of doing business, companies need the basic skill sets in their talent pool. Government needs to focus more intensely on education all the way from basic math and science skills to higher level research. Many of the qualified higher level engineers are from different countries that come here for their advanced education. We should be honored and look at this as a great opportunity to retain this talent to work and contribute to American companies. However, many of these talented young people face severe hurdles to remain in this country and to practice what they have learned here. Even if these uniquely talented individuals were allowed to remain in this country they may choose not to with growing tax burdens and the cost of living within the U.S. In today’s world, people are very mobile and we as a country need to be more competitive to incent people with advanced levels of education to live here. As I stated earlier, finding and developing high level engineering talent in the U.S. is one of Gleason’s foremost challenges.

To achieve long-term economic prosperity requires government policies which are not only pro-trade but recognize this as one of the cornerstones of economic growth and national security. Significant trade imbalances driven by tariff rates, for example, must be rectified over time. However, these decisions again must be guided by economic fairness for global consumers and not clouded by other issues.

The easing of policy restrictions in certain areas including with EXIM Bank which is used to finance product sales to developing countries and export control laws on technologically advanced products to certain end-users should also be considered to put American companies on even footing with foreign competitors.

In summary, doing the right things to help our economy at home in terms of creating a more "business friendly" environment – lower taxes, sensible regulation, improved education, and greater support of research at both the university and private levels—are what will allow American businesses to succeed by exporting more of their products and creating new jobs.