IMPACT ANALYSIS

Issues Impacting Global Business

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Dear Friends:

The American transportation infrastructure—including ports, roads, rail and airports—is in poor shape. Unless improved, efficiencies gained by the development of sophisticated American supply chains will be lost to global competitors (p1-2).

Most products we import from China are not really "Made in China" in any real sense of the term. Meaningful facts, which rarely surface, reveal we are more likely to be collaborators than competitors (p3).

Too often free trade proponents simply focus on exports and fail to make the moral case that voluntary economic exchange is inherently fair, benefits both parties, and allocates scarce resources more efficiently than a system that limits choices (p4-8).

I hope you find this issue informative and, as always, we welcome your comments.

Sincerely,

Byron Sutton
President and CEO
World Trade Center Orlando

America's Transportation Infrastructure Is in Need of Repair and Improvements

Deficient ports, highways, rail systems and airports drive up costs

By John Manzella

The American transportation infrastructure—including ports, roads, rail and airports—is in poor shape. In fact, according to a bipartisan panel of experts and two former secretaries of transportation, Norman Mineta and Samuel Skinner, an additional $134 billion to $262 billion must be spent per year through 2035 to rebuild roads, rail systems and air transportation. And that estimate doesn't include the costs to maintain and upgrade the nation's ports.

The costs to the country are enormous. Stated by the Texas Transportation Institute's 2009 Urban Mobility Report, in 2007 wasted fuel and lost productivity costs for U.S. drivers stuck in traffic reached $87.2 billion or $750 for every U.S. driver. This topped 2.8 billion gallons—three weeks worth of average gasoline consumption for every driver. Plus, the cumulative amount of time wasted in idling traffic for all drivers totaled 4.2 billion hours—nearly one full work week for each driver.

Impact on Global Competitiveness

"Transportation systems are the backbone of America: They keep our nation strong and moving. But we have not been taking good care of this resource. Lacking a coherent vision for our transportation future and chronically short of resources, we defer new investments, fail to plan and allow existing systems to fall into disrepair," according to the Miller Center of Public Affairs at the University of Virginia.

Very importantly, the Miller Center notes, "Our chief trading partners are making significant investments in their transportation infrastructure; America must do the same to remain competitive." To compete with

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For more information on World Trade Center Orlando services and events, please contact our office at 407.649.1899 or visit our website at www.worldtradecenter.org emerging economic powerhouses like China, the United States needs to become more efficient. And this includes making new investments in transportation infrastructure. Currently, as a percentage of its Gross Domestic Product, China spends approximately twice as much on capital investment as does the United States.

Stated by President Lyndon B. Johnson in 1966, "Modern transportation can be the rapid conduit of economic growth—or a bottleneck." In recent years, it appears to have become a bottleneck.

Two American Ports in Top Twenty

The level of transportation efficiency has a direct impact on the cost of U.S. goods and services—whether sold in the United States or abroad. According to a U.S. Department of Transportation report released January 2011, one container in every 11 engaged in global trade is either bound for or originates in the United States. This accounted for 9 percent of worldwide container traffic.

However, in 2009 only two U.S. ports—Los Angeles and Long Beach—ranked among the world's top 20 container ports as measured in TEUs (twenty-foot equivalent units), placing 16th and 18th respectively. The Port of New York/New Jersey ranked 22nd, falling from 20th in 2008, the report says.

Despite this, the United States continues to be the world's largest trading nation. Total U.S. container traffic more than doubled in volume between 1995 and 2007, from 22 million TEUs to an estimated 45 million, before falling to approximately 43 million in 2008 and to 37 million in 2009. Between 1995 and 2009, world container traffic more than tripled in volume, from 137 million TEUs to 432 million TEUs.

Shifts in Container Trade Patterns

With the expansion of the Panama Canal, which is scheduled to be completed in October 2014, larger post-panamax ships will be able to pass through with a maximum cargo of 12,500 TEUs. This represents three times more capacity than today. As a result, some U.S. east coast ports are expecting an increase in container traffic as ships departing from China and other Asian trading partners no longer will have to unload in California.

However, others believe that much of the shift from the west coast to eastern and southern ports that already has occurred for a variety of reasons is coming to an end, and is unlikely to be significantly impacted by the Panama Canal expansion. One reason: only a few ports, including Baltimore, Norfolk, and New York-New Jersey have the 50 ft. depths required to accommodate post-panamax ships. Unless more dredging is funded (the Port of Miami currently is seeking $75 million for what it calls the Deep Dredge), post-panamax ship calls on the east cost may be limited.

The Growth of Inland Ports

The efficient movement of containerized cargo involves much more than our nation's ports. Rail and highway capacity have an enormous impact, as well as our inland warehouses and distribution centers that provide logistical support for the entire multimodal freight supply chain.

According to the Miller Center of Public Affairs, approximately 60 percent of rail intermodal traffic consists of merchandise imports and exports that interchange between ship and rail at U.S. container ports. The remaining 40 percent of rail intermodal traffic is domestic.

As global trade increases, logistics providers are developing large integrated freight logistic distribution centers at inland locations, including Kansas City, Memphis, Columbus and Chicago, the Miller Center of Public Affairs says. And a large Buffalo bi-national logistic complex is in the planning stage.

Each day, thousands of imported containers are transported up to 2,000 miles to these hubs, mostly by rail on behalf of large-scale retailers and independent logistics providers. In addition, the Nation's Class I railroads are developing mega hubs and renovating some of their rail tracks and tunnels for double-stack trains.

Efficient Transportation Is Essential

No sector is more important to the American economy than transportation, said George H. W. Bush in 1990. As world trade grows even larger and we continue our leadership in an increasingly global society, he said, we will become even more dependent on transportation. President Bush was correct. With the acceleration of globalization, transportation has become even more essential to the American economy. Unfortunately, the U.S. trade and transportation infrastructure has not received the attention or the funding it requires.

Unless significantly more funds are invested in this nations highway, rail and port infrastructure, efficiency gained by the development of sophisticated American supply chains will be lost to our global competitors. ■

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John Manzella is a frequent speaker, author of "Grasping Globalization" and president of Manzella Trade Communications, a strategic communications and public affairs firm with expertise in global and economic-based issues. For information, visit www.ManzellaTrade.com.

U.S.-China Trade Is a Collaborative Effort

Meaningful facts are not well known

By Daniel Griswold

The recent visit of China's President Hu Jintao was considered a diplomatic success. But it seems only to have hardened the determination of New York Sen. Charles Schumer and other Chinese critics.

It's a mistake to see China as a monolithic economic rival to the U.S. And while certain U.S. companies do compete head to head with Chinese manufacturers, producers in both countries occupy different locations in an increasingly complex global supply chain. In fact, U.S. companies are more likely to be collaborators than competitors.

This also is true for East Asian firms. For the past two decades companies in Japan, South Korea, Taiwan and elsewhere have been slicing up their own supply chains, basing their lower-end, labor-intensive operations in China while retaining production of higher-end components and services in their home markets.

As a result, most products we import from China are not really "Made in China" in any real sense of the term. The consumer electronics and other more sophisticated products we buy from China typically are designed and engineered outside of China, and built with more expensive non-Chinese components. The products are assembled there, but even that lower-end work is usually performed in factories owned and managed by non-Chinese multinationals.

On a macro level, shifts in supply chain flows are reflected in trade numbers with the countries surrounding China. Imports from China have grown exponentially since 1990, from $15 billion to more than $300 billion in 2010. This has provided fodder for critics to claim we're being swamped by a tidal wave of low-cost imports that have displaced U.S. production.

What critics miss is the relative decline of imports to the U.S. from other major Asian economies. Thus, most of the products we import from China are not the type of things Americans were making 10 or 20 years ago, but rather the kinds of products we used to import directly from other Asian countries.

China has become the final assembly operation in a global factory. Since 1990, imports from China have grown from 3 percent of total U.S. imports to 17 percent—a huge increase.

While U.S. imports from China rose from 3% to 17% since 1990, U.S. imports from more developed Asian economies plummeted from 31% to 13%.

But that has come almost entirely at the expense of imports from China's Asian neighbors. During that same period, the share of U.S. imports from the more developed Asian economies—Japan, South Korea, Taiwan, Hong Kong and Malaysia—has plummeted from 31 percent to 13 percent of total U.S. imports. Overall, imports from those countries combined with China have remained a steady 30 percent of U.S. imports since China entered the World Trade Organization in 2001.

On a micro level, nothing better illustrates what is right with our trade relationship with China than the iPhone. Even though technically made in China, this is an American product in every meaningful sense of the word. It was created by Apple in California, and its success has been a boon to Apple employees and shareholders, application developers and the millions of consumers who enjoy the product every day.

According to iSuppli, a market-research firm in El Segundo, Calif., just a few dollars of value of an iPhone 4 is actually added in China during final assembly. The major components are from suppliers in Japan, South Korea, Taiwan, the U.S. and even Germany and Switzerland.

Of the $600 retail price, less than a third goes into hardware and assembly. The highest value added for the iPhone, as with most manufactured products today, is realized at the beginning and the end of the supply chain—in research, design and engineering at the front end, and distribution, retail, service and profit mark up at the back end.

If higher tariffs were imposed on Chinese imports, there would not be a repatriation of jobs to the United States, but instead, a massive disruption of intricate global supply chains that are benefiting American consumers, companies and workers every day. The cost of producing an iPhone would go up sharply, driving up the cost to consumers and reducing demand. In fact, without the ability to assemble the final product efficiently and economically in a place such as China, products like the iPhone may never be developed in the first place. ■

Daniel Griswold is director of the Cato Institute's Center for Trade Policy Studies and author of the 2009 book, "Mad About Trade: Why Main Street America Should Embrace Globalization."

Beyond Exports

A better case for free trade

By Daniel J. Ikenson and Scott Lincicome

After four years of stasis on the trade front, the new post-election environment is a welcome change. Removing barriers to trade—in both directions—is essential to sustained economic recovery and long-term growth.

But how long will this window of opportunity remain ajar? Despite trade's benefits, American sentiment toward it is lukewarm in the best of times, and always vulnerable to manipulation by politicians and media charlatans looking to blame foreigners for domestic shortcomings. Before the end of this year, the 2012 presidential election campaigns will be in high gear, and trade has been a particularly dirty word in stump speeches and political debates in the past. Indeed, one of the reasons for the energetic trade policy push in 2011 is that the political environment next year is expected to be less hospitable to trade initiatives.

The fact that public opinion about trade is so malleable and arguments for restricting it so resonant at times speaks to a failure of free trade's proponents to make their compelling message stick. It is sad, but true, that so many Americans need to be reminded of the benefits of being free to choose how and with whom to conduct commerce. But in an atmosphere where demagogues peddle myths to mislead the public into believing that it is preferable for government to limit their choices and direct their resources to chosen ends, it is crucial that the case for free trade be made more clearly, comprehensively, and consistently than it has been in the past.

Thus, in addition to securing the immediate goal of concluding and passing trade liberalizing agreements in 2011, advocates of trade in

Congress, the administration, the business community, think tanks, academia, and among the general public should update their arguments and invest in the process of winning the trade debate once and for all. Some of the most compelling arguments for free trade have been only modestly summoned or absent from the discussion for too long.

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The Message Matters

Most Americans enjoy the fruits of international trade and globalization every day: having more to save or spend because retailers pass on cost savings made possible by their access to thousands of foreign producers, designing and selling products that would never have been commercially viable without access to the cost efficiencies afforded by transnational production and supply chains, depositing bigger paychecks on account of their employers' growing sales to customers abroad, and enjoying salaries and benefits provided by employers that happen to be foreign-owned companies.

Nevertheless, public opinion polls routinely find tepid support among Americans for free trade. Regardless of the prevailing economic conditions or how the questions are phrased, most polls typically find that fewer than half of all Americans view trade favorably. And skeptical views have become more prevalent in recent years.

Some skepticism can be attributed to the perpetuation of myths about how unfair foreign trade practices have destroyed the U.S. manufacturing sector or about how the trade deficit reflects a failure of trade policy and constitutes a drag on economic growth—the staple arguments of most protectionists. However, we free trade advocates bear some responsibility for not winning Americans' hearts and minds. The factual arguments are compelling, but tend to get lost on a public that is more susceptible to depictions of worst-case scenarios and the ill-conceived bromides that follow. We need better salesmanship.

Poll data make clear that better salesmanship—or a better strategy—could change minds. Thus, at least 10 percent of the population changes their views on trade fairly regularly. Given that most Americans have not lost their jobs to import competition or outsourcing, nor do very many Americans know someone who has, it seems unlikely that deteriorating attitudes toward trade have much, if anything, to do with personal experience.

American attitudes toward trade are shaped largely by what Americans hear from their elected officials and what they absorb from the media. The dramatic decline in pro-trade sentiment between 2007 and 2008, for example, coincided with a U.S. presidential primary election campaign season in which the Democratic candidates routinely criticized U.S. trade policy and certain trade partners.

Perhaps most memorable was the late-February 2008 debate at Cleveland State University on the eve of the Ohio primary, when the late Tim Russert extracted renunciations of NAFTA and pledges from candidates Hillary Clinton and Barack Obama to reopen and renegotiate terms of the agreement.

The fairly significant increase in pro-trade sentiment during 2009 was likely attributable in part to the fact that a very public disavowal of protectionism took place on the international stage, as governments grappled with alternative policies to combat the recession. Throughout the year, economists exhorted politicians to avoid protectionist policy responses, reminding them of the deleterious impact on the global economy of the Smoot-Hawley tariff and the retaliatory policies it inspired in the 1930s. And politicians pledged to heed that advice before domestic audiences and before international institutions, such as the G-20. Throughout the year

those pledges were repeated and the public was reminded frequently of the dangers of protectionism.

Furthermore, in early 2009, President Obama visited heads of state in Canada and Mexico, offering reassurances that his campaign pledge to reopen NAFTA may have been a bit too hasty. And his instructions to Congress, at about the same time, that emerging Buy American provisions should not violate U.S. trade commitments, signaled to the public that the president might be less hostile to trade than he appeared to be during the previous year. The president's first Trade Policy Agenda, published one month later, revealed an administration far more approving than skeptical of free trade.

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The results of the 2009 Pew poll suggest that political leaders can indeed influence public opinion about trade. The greatest fluctuation in public support for trade between 2007 and 2009 came from self-identified Democrats—those paying most attention to the Democratic primary elections and President Obama's early speeches—with opposition swinging wildly from 37 percent in 2007 up to 50 percent in 2008 and down to 30 percent in 2009. Meanwhile, support among Republicans remained steady during this period, as the issue was almost nonexistent during the GOP primaries and rarely discussed by Republican nominee John McCain during the general election campaign.

The subsequent decline in public support between 2009 and 2010 might have had something to do with rising tensions in the U.S.-China trade relationship, which was covered intensively—perhaps even incited— by the media, and which spawned numerous congressional hearings into various Chinese policies and practices and a Democratic Party 2010 campaign strategy—"Make It In America"—that placed much of the blame for America's alleged manufacturing decline squarely on China.

Also, during this period, President Obama frequently asserted that China's "undervalued currency" was to blame for the U.S.-China trade deficit. These results support the theory that the attitudes of policymakers can shift public opinion, particularly among those who most closely identify with those policymakers.

The Stock Pro-Trade Message Contains the Seeds of Its Own Destruction

Despite the window of opportunity to move the trade agenda forward this year, it is fair to say that trade skeptics have the upper hand in the battle over messaging. One explanation: it is easier to whip up public opinion by playing to stereotypes and characterizing trade as a zero sum game between "us" (Americans) and "them" (foreigners) than it is to explain the process by which economic value is created and how free trade facilitates that process. Once the public's mind has been filled with images of shuttered factories and unemployed workers—regardless of the real cause of those conditions—it becomes more difficult to convey the truth about how Americans benefit from trade and how much poorer we would be without it.

But that hurdle can be overcome. The solution requires more than rationalization; it requires introspection, then change.

Many of trade's most vocal and active proponents in government and the private sector have relied too heavily and for too long on a faulty marketing strategy, which posits that more trade and more trade agreements mean more export opportunities, and more exports mean more economic growth and more jobs. The political appeal of that message is obvious, and there is nothing dishonest about it. Exports do contribute to economic growth, which is essential to job creation.

However, that message invites the following retort: if exports help grow the economy and create jobs, then imports must shrink the economy and cost jobs. In failing to explain why that conclusion about imports is wrong, trade proponents have yielded the floor to trade skeptics, who have been more than happy to manufacture talking points about the "deleterious" impact of imports on the U.S. economy. Most of those talking points are misleading or plain wrong, but there has been inadequate effort to correct the record. As a result, too many Americans accept the mercantilist fallacy that exports are good, imports are bad, and the trade account is a scoreboard.

The pervasive view that exports are good and imports are bad is a central misconception upon which rests the belief that trade negotiations and "reciprocity" are essential to trade liberalization. Under this formulation, an optimal trade agreement, from the perspective of U.S. negotiators, is one that maximizes U.S. access to foreign markets and minimizes foreign access to U.S. markets.

An agreement requiring large cuts to U.S. tariffs, which would deliver significant benefits to consumers, would not pass political muster unless it could be demonstrated that even larger export benefits were to be had. This misguided premise—that imports are the cost of exports and should be minimized—lies at the root of public skepticism about trade. Ironically, it is also a prominent feature of the favored pro-trade argument.

George W. Bush's last trade representative, Susan Schwab, in pitching to Congress the pending bilateral trade agreements with South Korea, Colombia, and Panama, cited the U.S. trade surplus with the dozen or so countries with whom free trade agreements were implemented during the Bush years. Implicit in her selling point was that a trade surplus is a measure of trade policy success, and that maximizing exports and minimizing imports are therefore worthy objectives. But if that is the proper metric, then it does not require sophisticated analysis to conclude that, with a $700-$800 billion aggregate trade deficit at the time, overall U.S. trade policy is an abject failure—the central argument of protectionists.

Ambassador Schwab is certainly not the only one to commit this messaging foul. Many prominent trade advocates have made similar arguments. In his State of the Union speech, President Obama referred to his administration's goal of doubling exports by 2014—a goal for which an entire bureaucracy has been erected—to make the point that "the more we export, the more jobs we create at home."

Many of trade's most vocal proponents in government and the private sector have relied too heavily and for too long on a faulty marketing strategy.

Not once in that speech did the president acknowledge the importance of imports to the bottom lines of those U.S. companies that he expects to create American jobs. The problem is not that export potential is used as a selling point. The problem is that it is too often the exclusive selling point. And that contributes to unfavorable impressions about imports and the trade deficit—two statistics, by the way, that typically increase when the economy is expanding and fall when the economy is contracting.

Likewise, in its efforts to promote trade, the business community tends to fixate on the export potential of this or that agreement. Of course, that is important information to disseminate. But in ignoring or downplaying the primary benefits of trade to consumers—that is, greater access to imports—the business community's message reinforces false impressions that trade only benefits rich corporations at the expense of working Americans.

A More Compelling Case for Free Trade

The case for free trade is much broader than the one that trumpets only export potential. And it is more elegant. The most principled case is a moral one: voluntary economic exchange is inherently fair, benefits both parties, and allocates scarce resources more efficiently than a system under which government dictates or limits choices.

Moreover, government intervention in voluntary economic exchange on behalf of some citizens necessarily comes at the expense of others and is inherently unfair, inefficient, and subverts the rule of law. At their core, trade barriers are the triumph of coercion and politics over free choice and economics. Trade barriers are the result of productive resources being diverted to achieve political ends and, in the process, taxing unsuspecting consumers to line the pockets of the special interests that succeeded in enlisting the weight of the government on their side.

Protectionism is akin to earmarks, but it comes out of the hides of American families and businesses instead of the general treasury. Policymakers on the right should support free trade because it is consistent with their principled opposition to higher taxes on American businesses and consumers and to big government telling people how and where they should spend their money.

A vote for free trade is a vote to cut taxes and to get government out of the business of picking winners and losers in the market. Policymakers on the left should support free trade because it is consistent with their opposition to corporate welfare and regressive taxation.

Beyond the moral case for free trade, when people are free to buy from, sell to, and invest with one another as they choose, they can achieve far more than when governments attempt to control their decisions. Widening the circle of people with whom we transact brings benefits to consumers in the form of lower prices, greater variety, and better quality, and it allows companies to reap the benefits of innovation, specialization, and economies of scale that larger markets afford. Free markets are essential to prosperity, and expanding free markets as much as possible enhances that prosperity.

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When goods, services and capital flow freely across U.S. borders, Americans can take full advantage of the opportunities of the international marketplace. They can buy the best or least expensive goods and services the world has to offer, they can sell to the most promising markets, they can choose among the best investment opportunities, and they can tap into the worldwide pool of labor and capital.

Study after study has shown that countries that are more open to the global economy grow faster and achieve higher incomes than those that are relatively closed.

Retorting Some Common Myths

In the bright light of these broader free trade arguments, it becomes clear that those seeking to restrict trade are trying to commit an offense. They are attempting to enlist the force of government—via higher taxes, more regulation, or corporate welfare—to prevent individuals from engaging in consensual, mutually beneficial exchange. And they should be forced to explain themselves in terms of the harm they would inflict on others through state coercion.

Regrettably, that never happens. Instead, those seeking protection claim immunity from the logic and equity of those moral and economic parameters, preferring to invoke claims of exceptional circumstances, labeling those opposed to their agenda as unpatriotic, or playing on fears about the consequences of exercising one's rights to trade. Of course free trade is ideal in theory, they will say, but reality demands special consideration in our case. Or, of course individuals should be free to choose with whom they transact, but their expressed preferences for imports imperil their jobs and America's future.

Trade skepticism is rooted in fear, which thrives on the propagation and acceptance of recycled myths. Thus, in making the case for free trade, proponents must be better prepared to refute the plausible-sounding fallacies about imports, trade deficits, and zero-sum games that have been allowed to linger for too long.

The allegation that imports have destroyed the U.S. manufacturing sector persists despite the wealth of evidence to the contrary. U.S. manufacturing took its lumps during the recent recession (as did all other sectors of the economy), but by all credible metrics it has been thriving for decades. In fact, U.S. factories account for more manufacturing value-added than the factories of any other country in the world.

If imports detract from growth and reduce the number of jobs in the economy, then why does import value tend to rise when the economy is expanding and adding jobs and fall when the economy is contracting and shedding jobs? Imports are vital to economic growth. U.S. producers account for the majority of imports. More than 55 percent of what Americans purchase from abroad is classified as industrial supplies or capital goods—inputs used in manufacturing and other value-added activities, such as the construction and transportation industries.

By limiting Americans' access to imports, production costs and other business costs would be higher, necessitating higher prices, lower wages, and other cost savings to make enterprises profitable. Consumers, businesses, and government would have less purchasing power, which would curtail economic growth and hurt U.S. companies trying to compete abroad, thus reducing exports. In fact, export sales would be even more difficult to come by, as foreigners, deprived of their sales to Americans, would have fewer dollars to spend on U.S. goods.

Contrary to some assertions, imports actually support jobs in U.S. manufacturing and in many other sectors of the economy. In addition to the imported intermediate goods that keep U.S. companies competitive and able to provide jobs, a significant percentage of U.S. imports are final goods that were simply assembled abroad from components produced, designs engineered, and ideas hatched in the United States. Without access to lower-cost labor in places like China, products like Apple's iPod, iPhone, and iPad might never have been commercially viable.

If imports detract from growth and eliminate jobs, then why does import value tend to rise when the economy is expanding and adding jobs, and fall when the economy is contracting and shedding jobs?

These ubiquitous products—which have spawned the creation of new industries producing dozens of accessory items (think docking stations and apps)—might have been too expensive to produce for mass consumption had all of the manufacturing and assembling been required to occur in the United States. Instead of \$300–\$400 iPhones, the devices might have retailed for double or triple that price and their consumer potential never realized.

The example of the iPhone production and supply chain also reveals the absurdity of hand wringing over trade deficits. The alleged U.S. high-tech trade deficit with China is simply a function of antiquated trade flow accounting that has failed to keep up with the reality of globalization. Even though each iPhone imported from China registers as a \$179 import (the full cost of its production), only \$6.50 of that amount represents the cost of Chinese inputs.

The bottom line is that each iPhone imported from China supports U.S. employment up and down the supply chain, from Apple's designers and engineers to independent component manufacturers to logistics providers, truckers, port workers, and retail employees. And misguided policies designed to "fix" the trade deficit would imperil this wealth-creating process. The arguments of trade's critics remain valid only to those who fail to examine the facts about our modern global economy. Illuminating those facts is the burden of free trade advocates. ■

Daniel Ikenson is associate director of the Center for Trade Policy Studies at the Cato Institute. Scott Lincicome is an international trade attorney with the law firm of White & Case, LLP, in Washington, D.C.

Produced in association with the World Trade Center Orlando, 550 North Bumby Ave., Suite 215, Orlando, FL 32803.
Tel 407.649.1899 info@worldtradecenterorlando.org