Keeping America on the Frontier of Competitiveness

By Frederick W. Smith, Chairman and CEO, FedEx

Thank you for this wonderful award. I am honored to receive it on behalf of more than 400,000 FedEx team members around the world.

FedEx fully supports the long-standing goal of the Council—to gather a broad coalition of leaders in industry, higher education, labor, and government to help shape policies that make the United States more competitive. This requires innovation, greater private and government capital investment, and effective education.

The strength of our economy over 40 years has enabled FedEx to connect people and possibilities around the world. Please take a look at this video, which sums up in a couple of minutes what FedEx does in the world every day.

A key factor in FedEx's growth and success as shown in the video is America's participation in an open, global marketplace. Our involvement in world trade, so important now in the age of e-commerce, stems from a series of innovative economic and trade decisions that distinguished America from the old economic models of the Western world.

As you know, President Trump campaigned on the promise to "Make America Great Again." I think it's time to review what made America great in the first place.

- Four major factors gave the United States advantages that transformed us into the most prosperous nation in the history of the world:
    - First, the rule of law in the Constitution and specifically the Commerce Clause;
    - Second, being a market-based economy vs. a centrally-directed economy;
    - Third, establishing the best educational system, especially higher education; and
    - Fourth, pursuing a path of open trade that helped grow America into the world's most prosperous country and a world power, particularly post-World War II.

The Founders established the rule of law in our Constitution and enshrined within it the **Commerce Clause**. It gave Congress the power to regulate commerce with foreign nations and among states. In those days, I believe history shows the word regulate meant "to make regular." It did *not* mean to control commerce among the states, a point I'll talk more about later.

- The Commerce Clause was an innovative idea in its day and a stark departure from Europe's highly balkanized trading system based on countries, provinces, and cities setting their own local rules for customs, tariffs, and goods crossing their borders.
- In the 1700s, Europe was still lumbering along under a system largely unchanged since the Middle Ages.

- The genius of the Commerce Clause was that it covered all the American states and prevented the type of restrictions on commerce practiced in Europe.
    - Take, for example, a famous 1824 case, Gibbons vs. Ogden. The state of New York had granted Ogden an exclusive license to operate his steamships between New York and New Jersey. Gibbons, another steamboat operator, ran two ships along the same route. Ogden filed an injunction against Gibbons. The case went all the way to the Supreme Court which ruled in Gibbons' favor citing the Commerce Clause as giving Congress, not the states, the right to regulate trade.
- The Commerce Clause gave American citizens the unfettered right to trade across state borders with each other and other countries with any tariffs on commerce set by the Federal versus any state government. Our open market was a major reason the United States spawned great innovations, inventions, and a proliferation of new products and services, and created a strong vein of entrepreneurship throughout our history.
- A present day example of similar regulatory reform is underway in India which recently enacted a Goods and Services Tax (GST). It supersedes all state and local tariffs to make the inter-state movement of goods simpler and faster—India's own commerce clause so to speak. Its goal is to remove bottlenecks, optimize distribution networks, and speed up commerce which, for decades, has been slowed by multiple border crossings and inspections. I think the GST will help streamline supply chains and be a major factor in India's future economic growth.

- On the other side of the coin, China's economy, even though it's the second-largest, still has a restrictive intra-country logistics system similar to what Europe and India had with lots of local regulations that add cost and pain to the trade process. As a result, China's logistics costs are estimated at 18-20% of their economy compared to about 9% in the United States.

The second thing that's kept America great is our **market-based economy** vs. a centrally directed or government-controlled economy which history has proven conclusively simply does not and cannot work.

- Once again, a lesson from the past: In Middle Ages Europe, wealth was amassed, controlled, and regulated in most cases by royals or aristocrats. Those who held wealth made innumerable rules for those who didn't.
    - Prices and profits were fixed, and the local ruler took what he wanted. There were so many regulations for merchants, they saw paying fines as just a cost of doing business. Read Barbara Tuchman's *A Distant Mirror* about the absurd regulations governing commercial life in those days.
- Only a few countries today still have a centrally directed economy—notably Cuba, Venezuela, and North Korea—all economic basket cases. Others have communist governments, particularly China, with many market-based economic sectors introduced over the last quarter century.
- The great communist experiment that started in 1917 after the Bolshevik Revolution in Russia ultimately failed with the fall of the Soviet Union in 1991. China followed the same economic path from 1948 until 1979 when market-based reforms began. In the course of these enormous social

upheavals, tens of millions of people were killed in pursuit of making them conform to a central government's rules as to how lives must be led and the economy should be managed.

- The incredible growth of China due to its move to a mostly market-driven economy should put to rest any lingering questions about the folly of state-directed economies.
- Read *I, Pencil*, Leonard Read's brilliant essay about the impossibility of a complex economy being centrally managed.

In the U.S., the Commerce Clause kept our economy mostly market-based. However, both internationally and domestically, our own history has sometimes detoured from a market-driven approach.

- Look at the 19th century railroads. They were the first entity to stitch our nation together so that all products could be bought and sold everywhere in the country.
    - Unfortunately, some of the railroad industry's unsavory practices victimized investors, consumers, and employees.
    - Congress tried to tame the wild and wooly railroad system in 1887 by establishing the Interstate Commerce Commission or ICC, which sought to regulate the industry—turning the generally accepted purpose of the Commerce Clause until then on its head.
    - While the ICC did improve overall conditions, it began to redefine the words in the Commerce Clause to mean "control" vs. to keep open or "make regular" business among the states.

  - The ICC thus imposed strict regulations on the rates, routes, and services of the railroads. Its power expanded well into the 20th century reaching beyond railroads to trucking in 1935. The ICC regulated with such a heavy hand that it strangled competition in both industries. By the 1960s, a third of the U.S. rail industry was bankrupt or close to it, and competition in trucking had been squelched for several decades as well.

Aviation was on a parallel track. Beginning in 1938 the Civil Aeronautics Board or CAB was established to regulate airline routes and rates and control competition.

- In the 70s, FedEx became the catalyst for Congressional deregulation in the air cargo industry—and passenger airline deregulation soon followed. Through the 80s and 90s, the same liberalization was legislated for railroads and trucking.
- With deregulation, America was getting back to its roots—open markets—which had stimulated growth from the beginnings of our history.
- The ICC and CAB were both sunset in 1995 and 1985 respectively.
- The result of deregulation of transportation was a surge of innovation and competition in air, truck, and rail industries that created a fertile environment for the evolution of companies such as FedEx, Southwest, and Walmart into business powerhouses.
  - For instance, at FedEx we knew that information about the package was as important as the package itself. So we invented the ability to track and trace shipments while in transit. Now businesses could

monitor their inventory in motion or at rest. This revolutionized the entire logistics landscape.

  - The combination of new logistics systems like FedEx, Walmart, and the new truckload carriers—meeting market versus regulators' demands— and the real-time inventory systems made possible by FedEx's tracking innovations pushed national logistics costs down from 16% to 9% of GDP with great benefits to the U.S. economy.
  - The same happened in air passenger transportation with ticket prices halved between 1978 and 2000. New aviation technology combined with market-based economics gave millions the opportunity to fly who otherwise could never have afforded it under the old CAB system.

Unfortunately, in the last few years, we've seen a hailstorm of government regulations that have choked the average 3% growth rate America had enjoyed from 1948 up until the Great Recession.

- To quote a recent op-ed by Phil Gramm and Michael Solon in the *Wall Street Journal*:
  - "A tidal wave of new rules and regulations across health care, financial services, energy, and manufacturing forced companies to spend billions on new capital and labor that served government and not consumers. . . . In a world of higher costs, productivity plummeted."
  - The authors contend that bad policies drove down productivity, and that changing regulatory and tax policies could reverse our low

growth and get it back to the 3% rates we enjoyed under Reagan and Clinton.

- We wholeheartedly agree and must always remember that business is the engine of job growth and prosperity through its innovations and inventions. Perhaps Winston Churchill said it best: "Some people regard private enterprise as a predatory tiger to be shot. Others look at it as a cow they can milk. Not enough people see it as a healthy horse pulling a sturdy wagon."

The third factor that made America great was its **educational system**, particularly our colleges and universities.

- When universal K-12 public education became government-funded and compulsory in all states, and many great public and private universities emerged out of the 19th century, the American system became a model for the rest of the world.
- Our workforce, engineers, scientists, inventors, and entrepreneurs who trained in this unique system created the incredible inventions, innovations, products, and services that truly made America the greatest success story in human history.
- Unfortunately, over the last few decades, our K-12 system has deteriorated for a variety of reasons, and we've been losing ground in producing an educated citizenry.
- But good old American ingenuity is coming to the rescue and changing the paradigms of public education by way of charter schools.

- According to a recent *Wall Street Journal* opinion piece, "American cities that have most improved their schools are those that have embraced charters wholeheartedly." New Orleans will be 100% charter schools next year, and studies have shown that their schools have doubled or tripled their effectiveness—more kids are graduating and going to college.
- Inspired by such success, Denver, Washington D.C., and Memphis, where FedEx is headquartered, have created models that include large numbers of charter schools as well as public high schools being managed more flexibly due to new state laws and regulations.

- Regarding higher education, the U.S. has developed a system of unique and varied colleges and universities admired worldwide. Many other countries provide more standardized higher education across the board for their students. American institutions specialize in specific areas of excellence. If you want to be an engineer, you might go to Cal Tech, RPI, or be a rambling wreck from Georgia Tech. If you're interested in liberal arts, try the Ivies, Williams, Amherst, Pepperdine, William and Mary, or Rhodes College in Memphis. Want to be a doctor? Go to John Hopkins, the University of Tennessee, Mayo, or any of our outstanding medical schools.
- The relative autonomy of our universities to build centers of excellence and to draw the best and brightest have resulted in American institutions usually taking seven or eight slots on the list of top colleges *worldwide*.
- For high school graduates who don't want to go on to the university level, there's a strong community college system in the U. S. I'm proud to say that Tennessee was the first state to provide tuition-free community

college education to high school graduates so that people who want good jobs can get the training they need. Other states are beginning to follow suit. This trend will grow as more people seek re-training for the jobs of tomorrow.

- For instance, FedEx supports a program at a nearby community college that provides apprentice aircraft mechanic training because we and other air carriers have a need for those technicians. These are great jobs with great benefits.

The fourth key to America's greatness has been our modern commitment to **open global trade**. Just like the Commerce Clause allowed American business to compete at scale nationwide in the 19th and early 20th centuries, the world has become the marketplace of the post-World War II era due to modern transport and technology.

- Products from Sony, Volkswagen, and Samsung stand alongside those of U.S. companies such as Apple, Ford, and Boeing in the American marketplace. These foreign products in the U.S. as well as many American goods sold virtually everywhere represent a global political vision that began in the early 30s.
- Through most of the 19th century, the U.S. used tariffs to protect home industries and fund the government. Over time, the vast public benefits of trade eventually led Congress to reduce those taxes on imported goods with new taxes on incomes replacing tariffs to fund the Federal government.
- World trade and global prosperity grew rapidly through the 1890s until

World War I.

- In 1934, President Roosevelt and Secretary of State Cordell Hull (from Tennessee) proposed, and Congress passed, the Trade Agreement Act, which lowered tariffs and again stimulated world trade. "When goods cross borders, armies seldom do," is a quote often attributed to Hull, and it describes the philosophy about trade he shared with Roosevelt. The TAA legislation was the antidote for the disastrous 1930 Smoot-Hawley Tariff Act, which had created a staggering decline in world trade that had grown during the 1920s. This ill-advised anti-trade legislation was a major cause of the Great Depression, the rise of Fascist Germany, and ultimately World War II.
- After the war, the U.S. supported the establishment of the United Nations, the International Money Fund, the World Bank, and the 1947 General Agreement on Trade and Tariffs. The GATT was signed by 23 countries and committed the U.S. to steadily liberalizing world trade. In the 70s and 80s, increased U.S. trade, combined with the deregulation in transport, created enormous economic gains for the entire world and lifted hundreds of millions of people out of poverty, especially those in countries devastated by World War II.
- All told, the benefits of open trade far outdistance the drawbacks. Between 1950 and 2016, trade has added $2.1 trillion to U.S. GDP. And between 1960 and 2015 trade rose as a percent of U.S. economic activity from 9% to more than 28%. NAFTA alone saw economic trade among the U.S., Canada, and Mexico grow from roughly $290 billion in 1993 when it was signed to more than $1.1 trillion in 2016.

- But if trade is so great, why are many people so mad about it?" It's mainly because the *pain of trade is localized*—we see factories closing, for example, although technology is the bigger culprit by far than trade in this respect. In either case, the U.S. must better address the issues of displaced workers through robust retraining programs that educate them for new jobs and better interim assistance.
- In contrast to local pain, the *benefits of trade are widespread*. Today, in the United States, about 25% of U.S. jobs are trade related. And those jobs pay an average of about 18% more than non-trade-related jobs. Furthermore, trade has added about $13,000 a year in purchasing power for the average American household.
- The recent rapid economic expansion and rise of China which is without precedent in human history, and the low-cost products that resulted have improved living standards for consumers worldwide and particularly in this country.
- And contrary to general perceptions, America remains a manufacturing powerhouse producing about $2.2 trillion worth of products, doubling our output from 1984, but with fewer people employed in the sector due to automation and technology.

- Back to a little history: In 1994, the GATT evolved into today's World Trade Organization, which provides global trade rules for the benefit of all member countries. The WTO is the forum for negotiating new global trade measures and has a rigorous dispute-settlement process to address violations.

- China joined the WTO in 2001 but still practices the mercantilist policies they renounced when they joined. We along with many others supported China's entrance into the WTO, but the Chinese have remained disappointingly protectionist and mercantilist when it comes to many WTO rules governing trade, investment, and forced technology transfers.
- China's 2006 "indigenous innovation" initiative favors and subsidizes Chinese companies at the expense of foreign businesses around the world. This type of discriminatory treatment is prohibited in the WTO agreement China signed. The U.S. must insist that trade be kept fair and that China keep its WTO promises.
- In fact, it is China's protectionism and mercantilism modeled on similar practices by Japan in the 80s and 90s that have been most responsible for the political backlash in the U.S. against trade which has otherwise produced so many benefits for America.
- I should add, as part of the Trans Pacific Partnership Agreement, Japan finally agreed to more liberal trade policies which had been fiercely resisted for decades by local Japanese interests.

- Despite political challenges, history shows that trade made easy, affordable and fast always begets more trade, more jobs, and more prosperity.
- Remember: 80% of the world's purchasing power and 95% of consumers lie outside the U.S. So we must do everything in our power to ensure the United States is efficiently connected to the vast global market and work with other nations to ensure the rules of trade are enforced and equitable. The United States' historical leadership in ensuring multilateral support for

trade *must* continue if we are to improve the wellbeing of the American people.

- In this regard, let's hope China—now a great nation and the world's second-largest economy—will embrace more liberal market policies and reduce various trade barriers. President Xi has said he is committed to these principles so there is reason for cautious optimism. History shows this is the best path for the peace and prosperity of the world and the U.S-Sino relationship—arguably now the most important in the world.

In summary, these four things have made America great: the Commerce Clause in our Constitution, our market-based economy, our educational system, and since 1934, our open trade policy.

Unfortunately, the current administration is veering away from open trade policies.

- President Trump has threatened to abandon the U.S.-Korea Free Trade Agreement. If that happens South Korea could raise tariffs up to 14%, much higher than average U.S. tariffs.
- I believe the U.S. walking away from the Trans Pacific Partnership was a mistake as the TPP's main focus was to make the rest of the Asia Pacific—excluding China—a more open, rules-based trading system whose economic growth would hopefully induce China into a less mercantilist posture. TPP significantly lowered many tariffs and eliminated many non-tariff barriers for U.S. exports among the participating countries.
- Hopefully, the President will mend, not break NAFTA, which, despite its flaws, has made North America a trade juggernaut. Since it began in 1994,

NAFTA has added more than 29 million private sector jobs to the United States. According to Peterson Institute economist Gary Hufbauer, NAFTA makes the U.S. $127 billion richer every year.

- Leaning into trade will keep America at the frontier of competitiveness and allow our industries to grow by serving a world market of more than seven billion people vs. just 480 million, the domestic populations of Canada, Mexico, and the United States.

Clearly, we must deal with significant challenges to maintain America's competitive edge. Some of you may have seen the *Wall Street Journal* op-ed piece that UPS CEO David Abney and I co-authored last month.

- We took the unusual step of jointly writing this essay because, even though we are fierce competitors, we also fiercely agree on basic policies to keep the United States competitive.
- The actions we endorsed in the essay will make government policy simpler, more equitable, and more growth-oriented, and we hope both sides of the Congressional aisle can reach a consensus and take action on the following:
    1) Reform and lower business taxes to increase GDP and wages by incentivizing investment, the main driver for increasing middle-class and blue-collar incomes. Investment has been far too low since the financial meltdown of 2008, and lack of investment is a major cause of wage stagnation for those Americans. We must also adopt a territorial versus global tax system to allow the flow of capital back to the United States economy to create more jobs and put the U.S. tax

system on par with our major trading partners. The U.S. is one of only three countries with major economies that have a worldwide tax system, and the other two countries have a much lower corporate tax rate than we do.

2) Invest in infrastructure. Federal government investment as a percent of GDP is slightly lower than in 1948. Let me give you a fact to illustrate the scope of the problem: A FedEx Ground tire lasts roughly half the time it did 20 years ago, due to the deterioration of our highways. Better infrastructure will make us faster to market, save money, and make our goods and services more competitive worldwide.
3) Fix our K-12 educational system and expand our community college system so that workers displaced by technology can get the retraining they need. And improve trade-adjustment assistance for workers displaced by trade which benefits our entire population.
4) Negotiate to ensure more open global trade. Establishing the right framework for commerce with all countries must be an essential part of American economic policy. Currently, we have free-trade agreements with 20 countries and enjoy a surplus with those partners in manufacturing, agriculture, and services. On a per-capita basis these 20 countries buy 13 times as many U.S. goods and services as other nations. The way forward is more free trade agreements, not less trade!

Businesses, government, industry experts, educational institutions, labor, and others must come together to support these policies to keep America competitive. History is clear: These are the policies necessary to ensure economic growth and rising incomes for all our citizens, and that's what made America great in the first place!

Thank you.