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FOOTWEAR DISTRIBUTORS AND RETAILERS OF AMERICA

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Customs and Trade Working Group

January 30th, 2018

10:00 a.m. – 4:00 p.m.

New York, New York

Critical Updates & Comprehensive Discussion of Footwear Legislative Priorities

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Administration's Trade Action

Completed In progress Stalled

TPP withdrawal
Trump issued an executive order withdrawing the US from the trade deal on January 23, 2017

NAFTA renegotiations
NAFTA negotiations continue, with an impasse in the Fall after the U.S. demanded strict rules of origin for autos and a new sunset clause.

China currency status
Trump has walked back his pledge to name China a currency manipulator in exchange for Chinese cooperation on North Korea

GSP

Generalized System of Preferences
Expired when Congress failed to pass an extension in 2017. Administration announced a new process for reviewing all GSP countries.

KORUS talks
Trump wants to revamp the Korea-U.S. Free Trade Agreement and held formal talks in January, to begin discussing "potential amendments and modifications" to the five-year-old trade deal.

Trade Enforcement
The Department of Commerce may propose new tariffs or countervailing duties against specific products or other countries that run trade surpluses with the United States

NAFTA – Setting the Tone on Trade

Key elements of North American Free Trade Agreement

NAFTA was created to **eliminate tariff barriers**, remove investment restrictions and protect intellectual property rights

When the 1994 agreement went into effect, around **50% of tariffs** were abolished immediately and the remaining tariffs were gradually eliminated

Because of restrictive footwear Rules of Origin (ROO), NAFTA is not heavily utilized by the footwear industry. Mexico and Canada supplied only 1.1 percent of pairs and 1.8 percent of dollars of total U.S. footwear imports in 2016

It also opened the **border and interior of Mexico** to US truckers and streamlined border processing and licensing requirements for commercial ground transportation

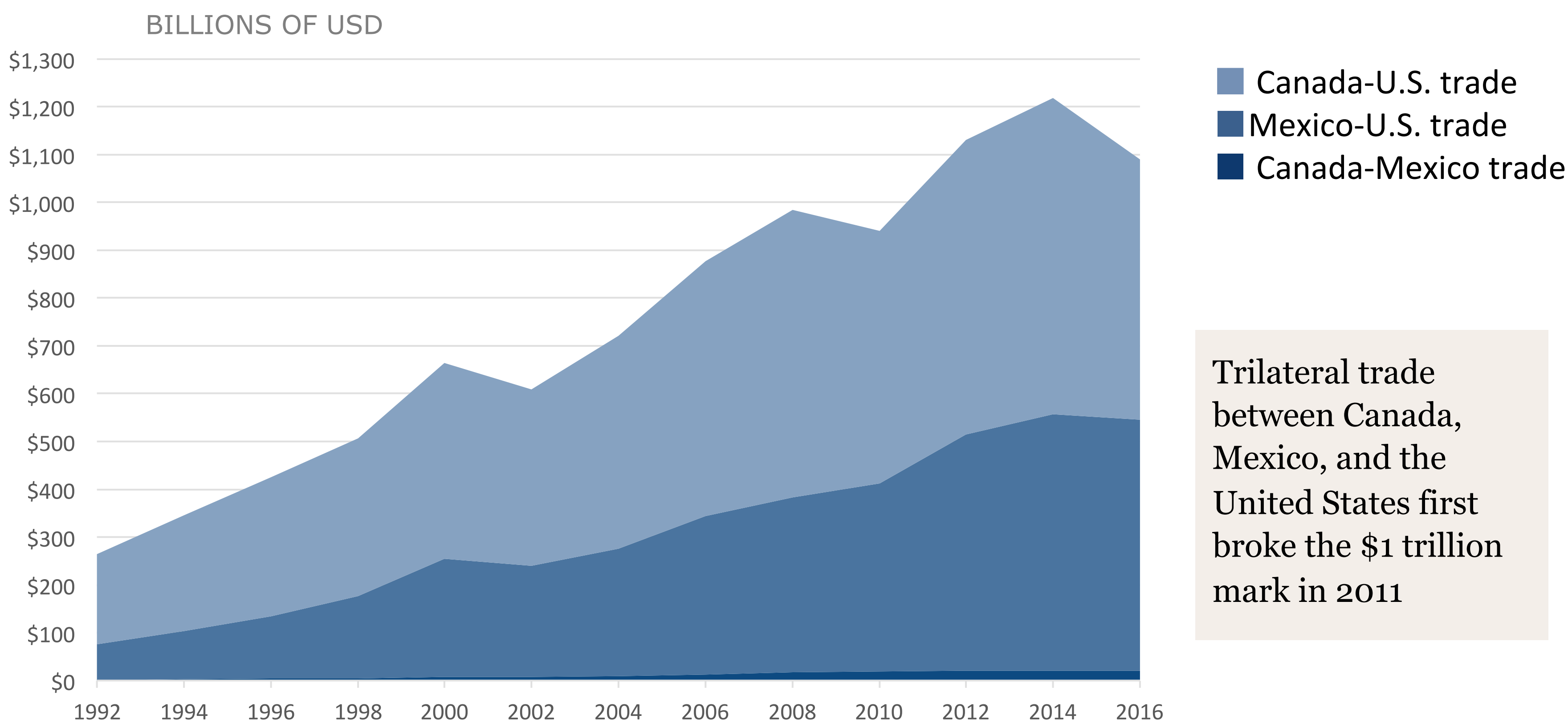
The three NAFTA countries agreed to **strengthen and standardize** health, safety and industrial standards

NAFTA also created commissions with the power to **impose fines against signatories** if they failed to implement the agreement’s labor and environmental standards

Key Factor 1: Significance of the Current Agreement

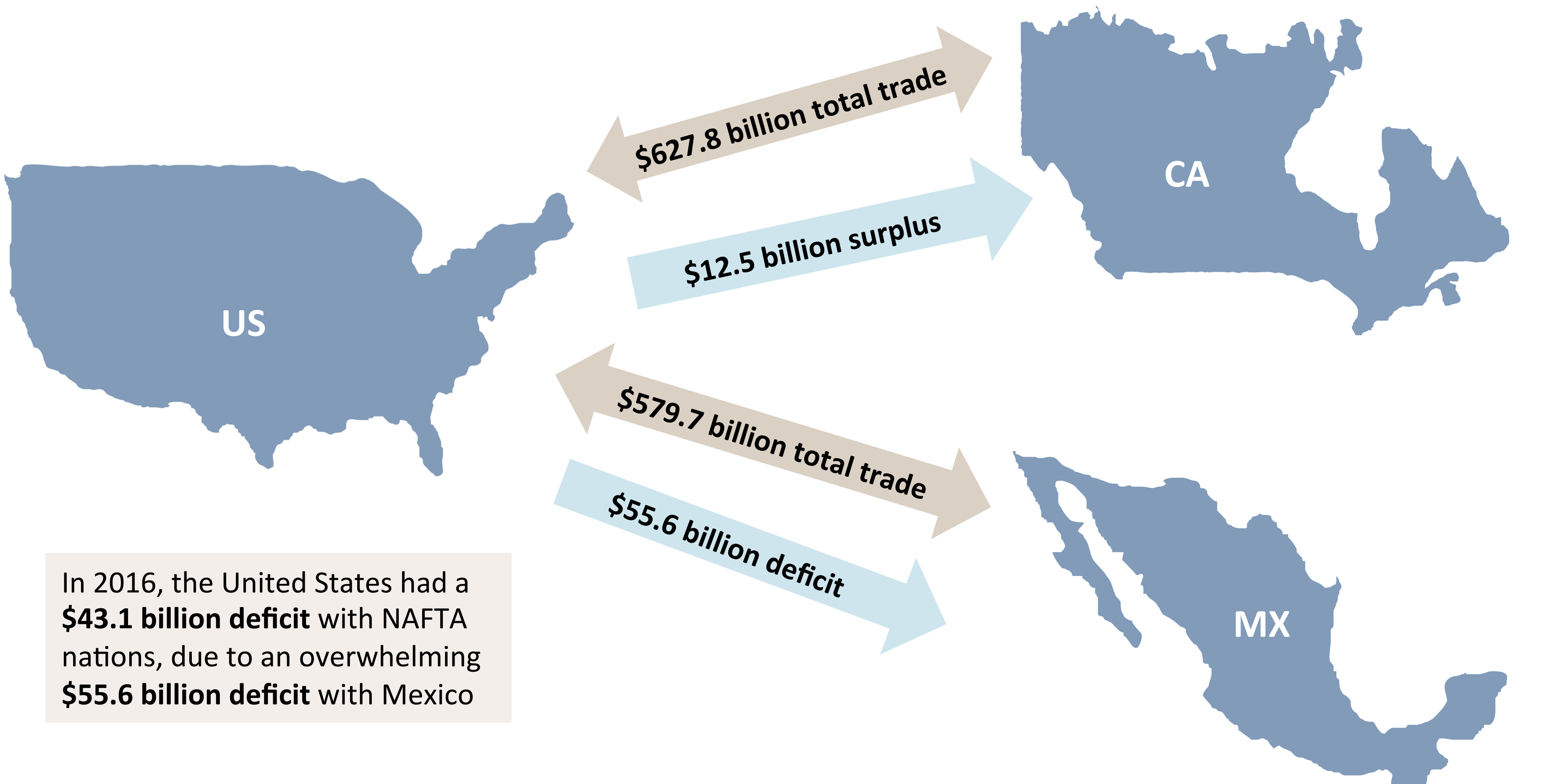
Trade between NAFTA countries has increased from around $350 billion in 1994 to over $1 trillion today

Trilateral trade between NAFTA countries



Trilateral trade between Canada, Mexico, and the United States first broke the $1 trillion mark in 2011

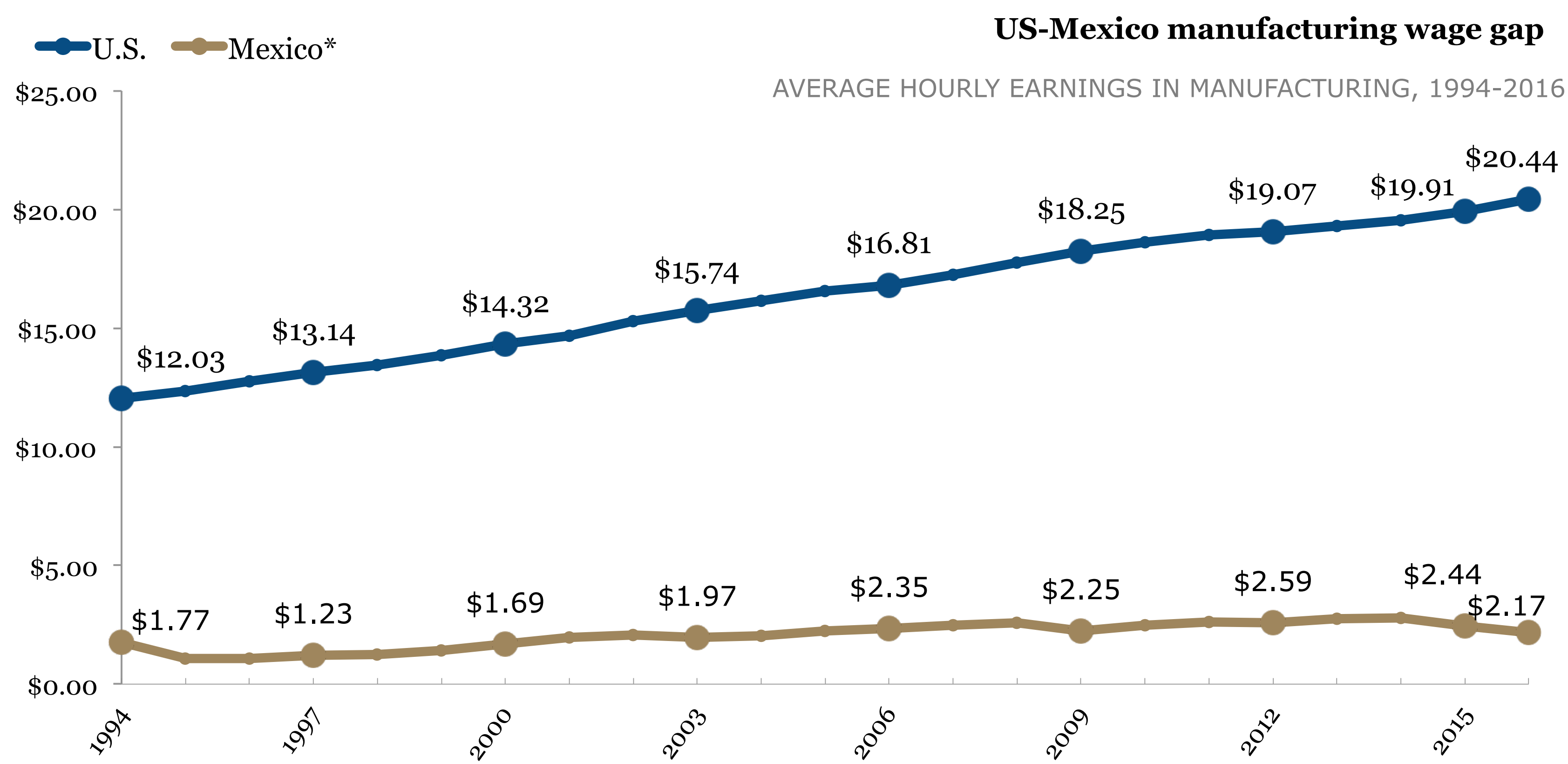
Key Factor #2: Trade deficits between NAFTA nations and the U.S.



In 2016, the United States had a **$43.1 billion deficit** with NAFTA nations, due to an overwhelming **$55.6 billion deficit** with Mexico

Key Factor #3: U.S. Manufacturing Emphasis

Mexico's Manufacturing Pay has remained low since NAFTA was signed



*Based on an eight-hour work day

Three buckets of issues on the table for NAFTA renegotiations

Standard modernization issues (TPP issues)

E-commerce

Digital trade

De Minimis

Historically contentious industries

Sugar

Dairy

New demands (Trump Administration Proposals)

Sunset clause

Tighter Rules of Origin for auto sector

Changing dispute settlement mechanisms for trading partners

Top Trump trade advisors leading NAFTA negotiations

Robert Lighthizer — *US Trade Representative*

- Responsible for conducting bilateral and multilateral trade negotiations
- Shares President Trump's skepticism of free trade
- Sees China as a potentially existential threat to the American economy, believes the US is the victim of unfair free trade agreements that favor other countries, and thinks the US should consider using aggressive tools like slapping punishing taxes on imports to protect American industries and workers
- A career trade lawyer and former US deputy trade representative under Reagan

Wilbur Ross — *Secretary of Commerce*

- When President Trump announced Secretary Ross' appointment, he asserted the investment banking and private equity tycoon would be in charge of his trade policy, a job traditionally held by the USTR
- Ross has been a vocal critic of NAFTA, especially the auto manufacturing components of the deal
- He has stated NAFTA should be abandoned if Mexico and Canada do not agree to making significant changes to the deal

John Melle — *Chief NAFTA negotiator*

- Responsible for the day-to-day negotiations at the staff level
- A USTR veteran, Melle worked on the original NAFTA agreement
- Unlike the president, he has defended and expressed positive views of the original NAFTA agreement
- Expert in Canadian, Mexican and U.S. trade policy

Pro-trade Republicans oppose some of Trump's NAFTA demands and pro-labor Democrats voice support

Republicans concerned by Trump Administration's demands

Sen. Orrin Hatch (R-UT), *Chairman of the Senate Finance Committee:* "I have concerns that some recent proposals by the United States…would have [a harmful] effect and wouldn't pass Congress. We have a real opportunity to improve Nafta, but to achieve that the administration must work with Congress …"

74 House Republicans signed a letter to President Trump opposing U.S. proposals on automotive rules of origin, which would require 50 percent U.S. content in NAFTA-built vehicles and 85 percent regional content. Other House Republicans have voiced concern over how a NAFTA withdrawal would impact their home districts' businesses negatively, especially representatives from agricultural districts.

Some Democrats have praised the Administration's tough stance on trade

Sen. Sherrod Brown (D-OH) — *Ranking member of the Banking, Housing & Urban Affairs Committee*
"Any trade proposal that makes multinational corporations nervous is a good sign that it's moving in the right direction for workers …" — Sen. Brown on the trade negotiations

Rep. Bill Pascrell (D-NJ) — *Ranking member of the House Ways and Means Trade Subcommittee*
"Some of those demands are in tune. We don't want to blow it up, Republicans don't want to blow it up. But we want substantial changes in the labor, the environmental, the currency, on how you come to an agreement when there's a dispute, and on problems of origin."

Possible NAFTA renegotiation outcomes

NAFTA failure

Trump triggers NAFTA exit

- As Trump has continually threatened, if NAFTA negotiations do not result in significant changes to the originally deal, he will end the pact. The president could announce his plan to withdraw and the agreement would end six months after that.
- If the U.S. exits NAFTA, tariffs will inevitably rise. For some goods, tariffs could go as high as 150 percent. That would cause prices to spike and cut into company profits. Additionally, consumers would see higher prices on many goods

Successful renegotiation

New agreement established in 2018

- Each nation could sign on to a new agreement by the established deadline
- In order to accomplish this, Canada and Mexico would have to agree to the U.S. demands they view as “non-starters,” or the U.S. will have to compromise on its demands

Renegotiation continue to stall

Negotiations pause or are extended

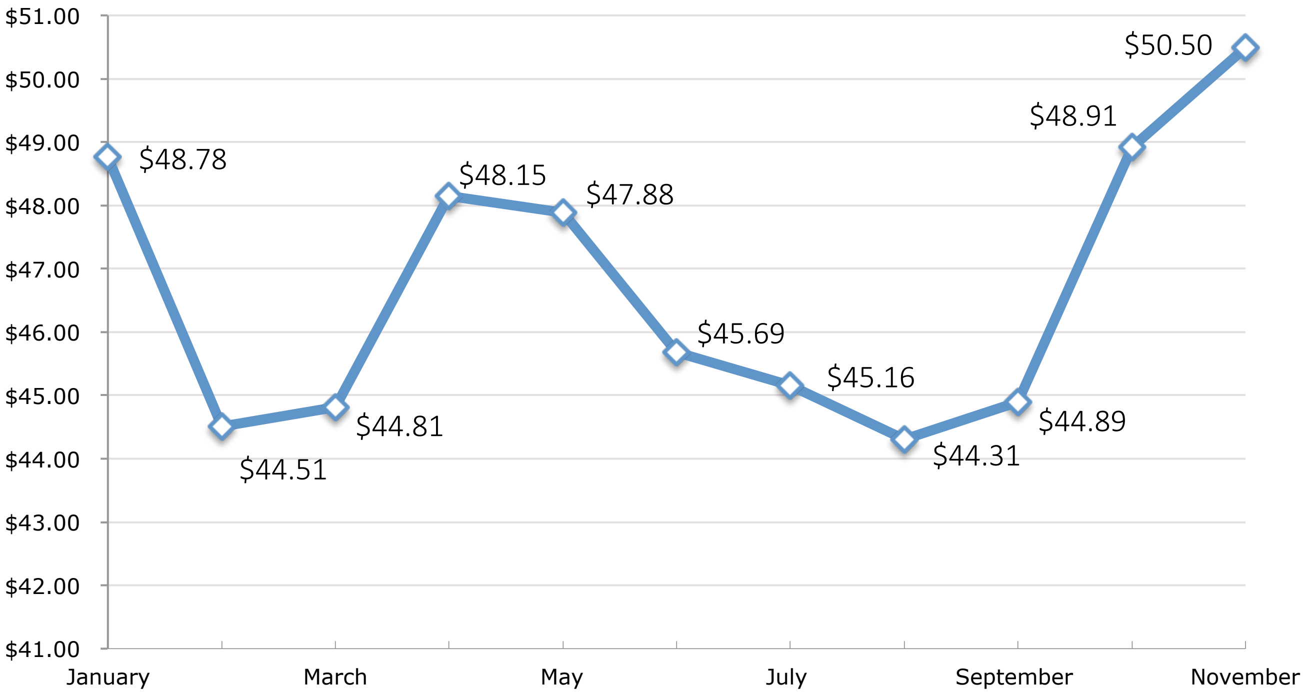
- The member nations could agree to extend the schedule once more, pushing negotiations farther into 2018
- 2018 elections the U.S. and Mexico could complicate the process

Concerns about Administrative Action on Trade

Trade deficit grows to widest gap since January 2012

US international trade deficit

NEGATIVE BILLIONS OF DOLLARS, JAN-NOV 2017



Key takeaways

- The trade deficit widened 3.2% from a month earlier to $50.5 billion, the highest since January 2012
- While both imports and exports rose, imports climbed 2.5% while exports increased 2.3%
- Busier international trade flows reflect strengthening economies in the U.S. and abroad, with major global regions growing in sync for the first time in years

Sources: Josh Mitchell and Eric Morath, "U.S. Trade Gap Grew 3.2% in November," WSJ, January 5, 2018; U.S. Census Bureau, January 2018.

Footwear Opportunity #1: Miscellaneous Tariff Bill

M
T
B

- **What is it?** Temporary duty-relief for certain products, ranging from manufacturing inputs to basic consumer goods like footwear, where there is:
  - ✓ No objections from a domestic producer AND
  - ✓ annual revenue loss to government is $500,000 or less.
- **Why do we have it?**

  American Manufacturing Competitiveness Act of 2016: "The HTS "*imposes duties on imported goods for which there is no domestic availability [and this] creates artificial distortions in the economy of the United States that negatively affect United States manufacturers and consumers.*
- **When did this start?** 1983 first MTB, 2016 new MTB process

Footwear Opportunity #2: U.S.-based FTZs and De Minimis

- **The problem with Section 321 (de minimis shipment provision)**: When goods are withdrawn from a U.S.-based Foreign Trade Zone (FTZ), and directly shipped to a U.S. person, despite meeting the de minimis value threshold of $800 or less per day, they are ineligible for Section 321 informal entry treatment.

- **New Coalition:** Formed to eliminate the discrimination favoring foreign suppliers and distribution centers, and to allow U.S.-based FTZ distribution centers to have the same opportunity to supply U.S. buyers with duty-free goods if they comply with the de minimis threshold.

- **Purpose**:
  - Educate key Congressional offices, Committees, Trump Administration officials and other essential stakeholders.
  - Encourage CBP to favorably consider a pending "ruling request" submitted in December 2016 that U.S.-based FTZs may equally utilize the Section 321 provision.
  - Develop and implement a proposal to end the discrimination through legislation.

- **Let us know if and how much you want to be involved in this effort.**

Footwear Opportunity #3: Tariff Reduction

What Are the Options?

- Full Footwear Duty Elimination
- Eliminate Only Children's Footwear Duty
- Revive the Affordable Footwear Act

International Trade Commission (ITC) Report

Key issue: nature of trade restraints

1 Leather goods and footwear have some of the highest tariffs on consumer goods in the United States. Over 90% of imports of these goods are dutiable.

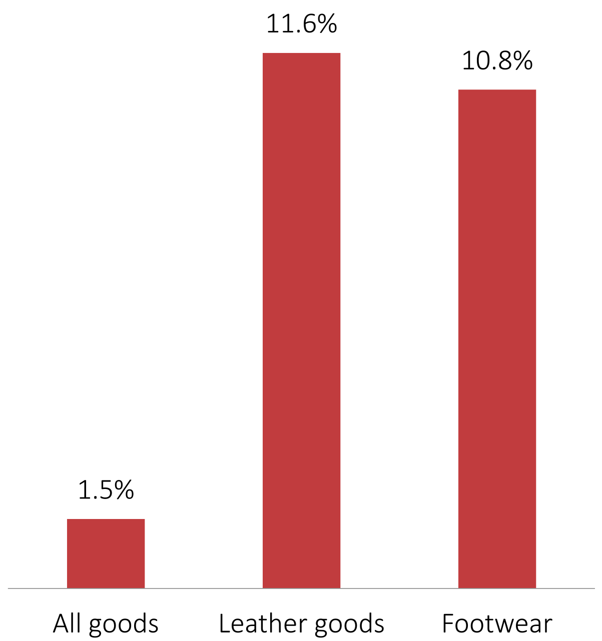
2 The U.S. industries producing leather goods and footwear have experienced significant import penetration and competition, despite average tariff rates that are much higher than those on most consumer goods, but with effective duty rates as high as nearly 70%.

3 Because production of finished leather goods and footwear is labor intensive, many firms moved manufacturing overseas decades ago to reduce costs. Imports now satisfy more than 95% of domestic consumption for these goods.

4 Although footwear imports account for only 1% of the total value of U.S. imports, they generate close to 9% of total U.S. tariff revenue. Tariffs on footwear can reach as high as 37.5%, 48%, and 67.5%, depending on the type of footwear.

5 Certain U.S. industry representatives contend that these tariffs limit the ability of U.S. footwear companies to compete globally, because they divert funds that could otherwise be allocated to investments in innovative design and processes to stay competitive.

Trade-weighted average ad valorem tariff, 2015



Projected increase in price of leather & allied product manufacturing imports due to restraints is 10.1% by 2020

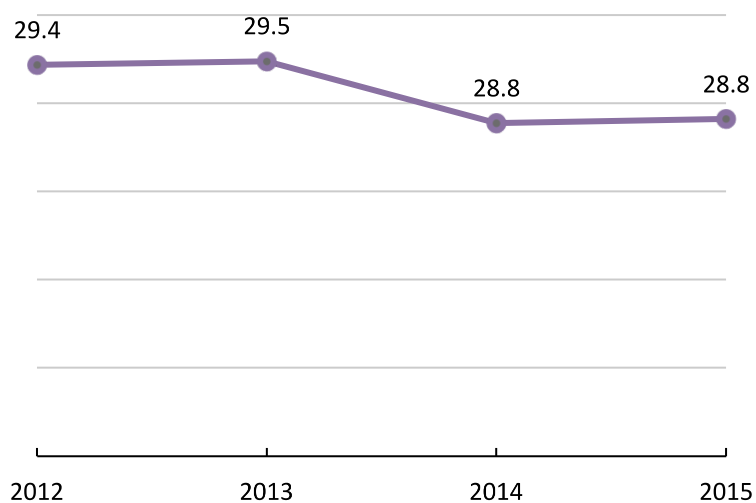
Source: United States International Trade Commission, "Publication 4726: the economic effects of significant U.S. import restraints ninth update 2017

International Trade Commission (ITC) Report

Leather and footwear industry summary data, 2015-2020

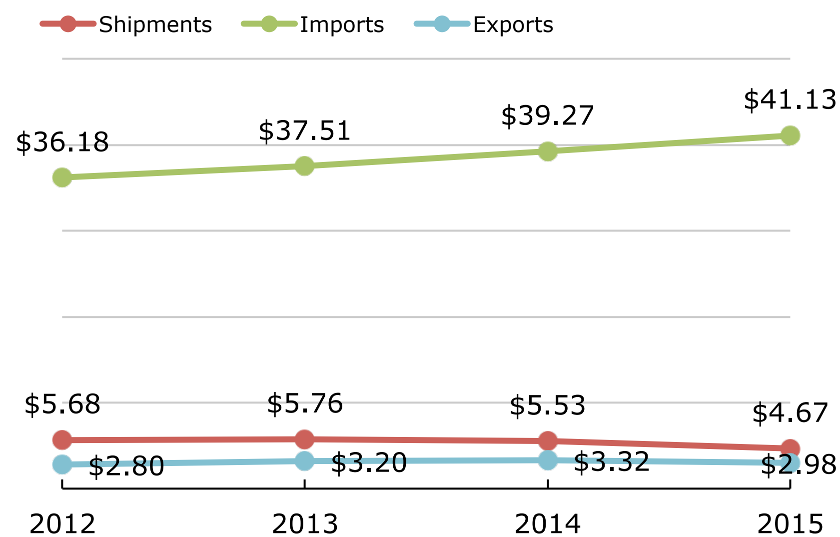
Employment levels

THOUSANDS OF FULL-TIME EQUIVALENT WORKERS, 2015-2020



Shipments, imports and exports

BILLIONS OF DOLLARS, 2015-2020



Domestic production accounts for only a small share of the U.S. market for leather goods and footwear and is primarily geared toward high-end fashion and niche markets, such as protective footwear and footwear for the military. Most U.S. leather goods and footwear companies focus on high-value activities, including design, branding, marketing, and distribution.

Total domestic output for the sector rebounded briefly following the U.S. economic recession of 2007 to 2009 and rose to almost $5.8 billion in 2013. However, shipments fell to $5.5 billion in 2014 and to $4.7 billion in 2015, which may indicate that the industry has resumed a general decline. Total sector employment fell by 2.1% during 2012–15, from 29,437 workers to 28,822 workers.

Source: United States International Trade Commission, "Publication 4726: the economic effects of significant U.S. import restraints ninth update 2017

International Trade Commission (ITC) Report

Estimated effects on removal of import barriers on the leather and footwear sector

	Baseline change (2015-2020)	Effect of liberalization
Employment	↓ -2.8%	↑ 1.8%
Shipments	↓ -5.0%	↑ 1.8%
Imports	↓ -5.0%	↑ 3.4%
Exports	↓ -2.0%	↑ 6.3%

Removing tariffs on imports of leather and allied products would boost U.S. exports by 6.3% relative to baseline, contributing to increases in employment and shipments of 1.8% each.

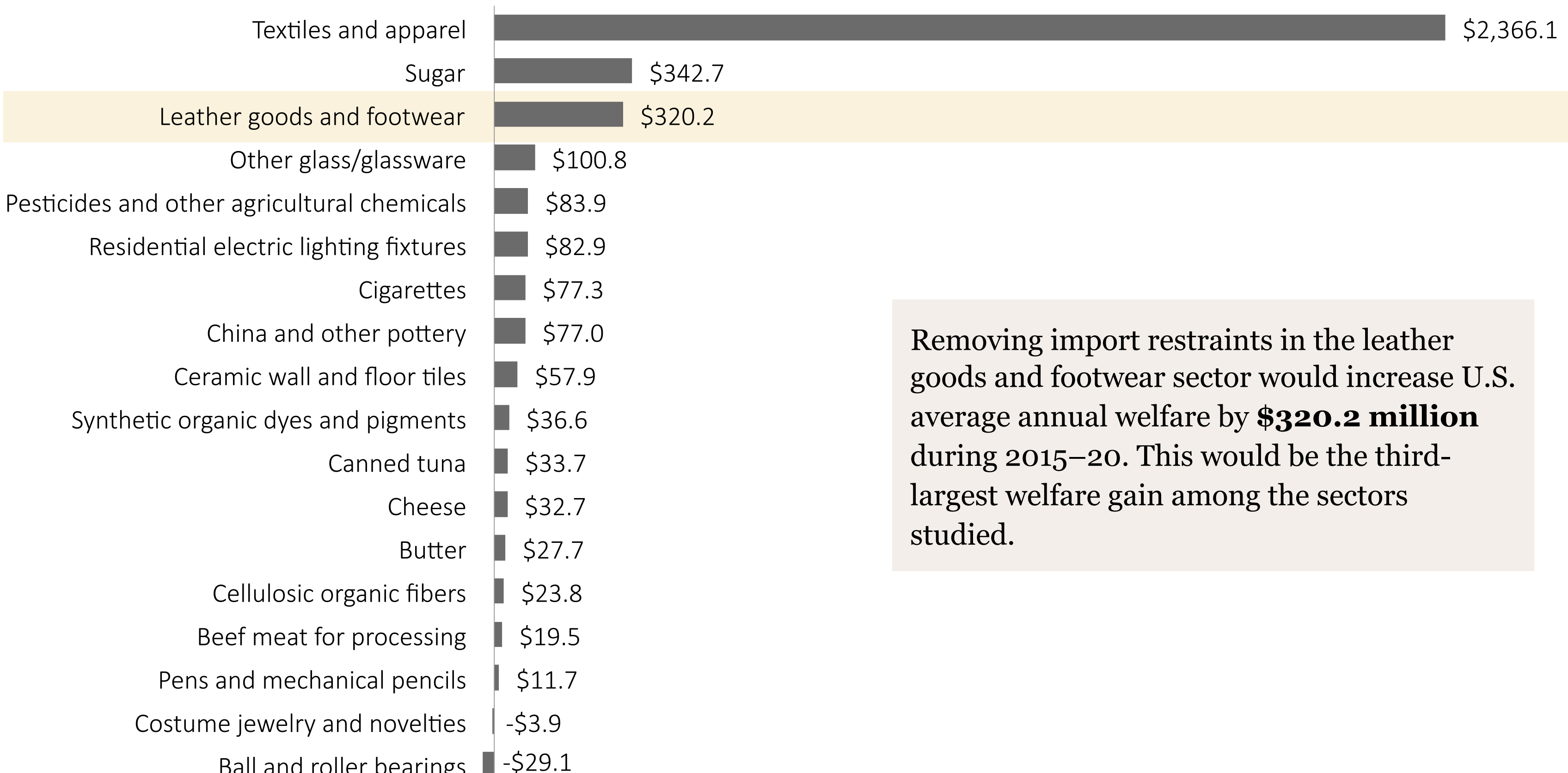
Imports supply over 95% of U.S. domestic demand for leather goods and footwear, which have some of the highest of all U.S. tariffs on consumer goods. The removal of tariffs is also projected to boost imports by 3.4% relative to baseline.

Source: United States International Trade Commission, “Publication 4726: the economic effects of significant U.S. import restraints ninth update 2017

International Trade Commission (ITC) Report

Average annual welfare gains from liberalizing import restraints by industry

MILLIONS OF DOLLARS, 2015-2020



Removing import restraints in the leather goods and footwear sector would increase U.S. average annual welfare by **$320.2 million** during 2015–20. This would be the third-largest welfare gain among the sectors studied.

Source: United States International Trade Commission, "Publication 4726: the economic effects of significant U.S. import restraints ninth update 2017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