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China's Impact on the U.S. Auto and
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Erosion of the Industrial Base and its
National Security Implications

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Erosion of the U.S. Industrial Base and its National Security Implications

Chairman Bartholomew, Commissions Becker and Blumenthal, ladies and gentlemen. I'm honored to be here.

Today, the United States industrial base including the automotive sector is seriously eroding. This situation has national security implications because we are dependent on foreign countries for critical components and systems. We are losing our ability to design, engineer, and manufacture products as well as control our supply chains.

The defense portion of the industrial base cannot be separated from the overall base. The offshoring of the U.S. auto industry alone is exacerbating this situation – when it erodes, it takes most of the defense capability with it.

The United States is dependent on other countries for critical auto *and* weapons technology. It's conceivable that at some time in the future a government could tell its local companies not to sell critical components to the United States because they don't agree with U.S. foreign policy. If we were ever to have a war with China, we could experience difficulties simply by having them cut off shipments to the United States and hurting our economy without even firing a shot.

The federal government doesn't manage the country's industrial base as a "system" but it needs to at least

understand system behavior. We need DoD to understand its key weapon system supply chains down to raw materials. In many cases, we're unable to manufacture critical military equipment. This situation isn't officially documented or monitored, but it needs to be. Knowing industry averages, I suspect that there's a significant presence of Chinese parts in our weapon systems, but we don't know where they are. This risk is significant.

U.S. corporations increasingly act as large social systems with a global focus as they should. Ask the CEOs of the Fortune 500 to describe the issues on their minds and, more than likely, national security or the disintegration of the U.S. industrial base would not be among them. Under the American financial and regulatory system, public companies are supposed to rank their shareholders at the top of the loyalty scale, except in times of emergency.

Well, today's situation may be a national emergency. The very ability of the United States to remain a superpower is at stake.

General Motors, Ford, Delphi, Northrop-Grumman, Boeing, Lockheed Martin – they all share the bottom of the industrial base.

Globalization and the intense pressure applied by Wall Street to U.S. companies encourages indiscriminant cost cutting, a measure that frequently works in the short term, but can be disastrous in the long term.

The “better, faster, cheaper” mentality sometimes sacrifices long-term gains by forcing a company to offshore work to low-wage countries such as China in the near term. These decisions can come back to haunt a company when the work acquired is of inferior quality, a critical core competency of the company is lost or stolen when intellectual property disappears or the accessibility of an essential item is put in jeopardy. Many stories are known in the auto industry, but rarely will anyone come forward for fear of Wall Street reprisals or a customer losing confidence.

Global purchasing organizations in industry and the military are not sufficiently looking at the risks of potential disruption because of foreign sales or supply lines. They tend to be rewarded for getting everything less expensively, and nothing else. Just look at the results of the brief longshoremen’s strike a few years back on the West Coast and the billions of dollars that it cost the nation per day.

You will hear from my colleagues in the Department of Defense who are experts in the Diminishing Manufacturing Sources and Materiel Shortages or DMSMS community.

Mission capable systems and readiness are put at risk when DMSMS issues are left unresolved. What isn’t understood is the reality that the auto industry affects DMSMS because the industrial infrastructure that supports the Department of Defense is shared by the auto industry. When a tier supplier to the auto industry goes under whether it is a

machine tool company or in micro-electronics, it reduces DoD's ability to function whether we say so or not. I think we might as well say so!

When government R&D investment in an industry deteriorates, it's only a matter of time before an industry is in trouble. Manufacturing R&D by the federal government has almost disappeared.

Young people no longer view working in manufacturing as a possible career so we're losing our ability to train the next generation of scientists and engineers. We're losing critical to defense industries such as shipbuilding, machine tools, high performance explosives and explosive components, cartridge and propellant actuated devices, welding and even the nuclear industry. *All of these industries share the bottom of the base with the auto industry. And, that is what has become a national security issue.*

We need to maintain a capability to be globally competitive in product and process innovation – we must regain our manufacturing prowess and leadership. We need to reinvigorate the Manufacturing Extension Partnership program at the National Institute of Standards and Technology.

We need to prioritize those technologies that are critical to regaining and then maintaining leadership and competitive advantage in the overall industrial base so China does not become the world's leader in technologies we need to be a

superpower. China is rapidly becoming the manufacturing capital of the world. For example, Chinese officials have publicly stated they want to become the foundry capital of the world and have a world-wide monopoly on cast parts. They have a plan to win and we don't.

We need to increase our investment in R&D to produce the leading edge knowledge, capabilities and patents the country must have to remain an economic and military superpower. We must increase funding to the national laboratories especially the Departments of Energy, Commerce and Defense.

We need to rethink our trade, offset and CFIUS policies to encourage the maintenance of high value-added jobs inside the country and we need to reform those national systems that are keeping our industry uncompetitive including pension and health care, particularly in the auto industry. The bankruptcy of Delphi is only the first of many dominos to fall if nothing changes. CFIUS must be completely rethought. Having General Motors under the control of foreigners is not the answer. Many foreign entities buy U.S. assets not to use them, but to dismantle them. Even Daimler's takeover of Chrysler removed serious capabilities to Germany, though no one will go on the record with specifics.

Cooperation between government and industry is essential. Unless we look at the industrial base as a system, we don't even see the problem or the possible military implications.

We also are not even asking whether or not a U.S. “owned” industrial base matters, and we need to explore this issue as a nation.

The White House, Congress and the entire spectrum of the agencies and departments of the federal government need to understand these issues. I applaud your efforts because unless something changes, the U.S. may cease to be a superpower.

Thank you for listening, and I look forward to your questions.