Introduction

Over the past few decades, globalization has been a big contributor to worldwide disinflation and global growth as more companies have sought cheaper labor in other countries in place of manufacturing here on our own shores. It has lowered costs for U.S. consumers and has also helped lift millions out of poverty in countries where the jobs have been created. More recently, however, there has been a shift in favor of bringing manufacturing back to North America. In this piece we will look at what has transpired over the last few years to make this so, what sectors could be beneficiaries, and what impediments and benefits come with “reshoring.”

The Genesis of the Recent Hyper-globalization

The fall of the Berlin Wall and the Soviet Union collapse in the 1980s helped shape the World Trade Organization (WTO). This organization encouraged nations across the globe to enter free-trade agreements with one another. China joined the WTO in 2001, marking a significant milestone in the country’s integration into the global economy. Upon joining the WTO in 2001, China’s gross domestic product accounted for only 3 to 4 percent of global GDP. By 2020, China accounted for 14.7 percent of global exports of goods¹, versus just 8.1 percent for U.S (see Figure 1.).

Figure 1: Leaders in Global Exports

![Figure 1: Leaders in Global Exports](https://regionsinvestmentmanagement.com/wp-content/uploads/2023/04/Regions-Manufacturing-Reshoring-Deglobalization-How-Fast-Are-We-Getting-There.pdf)

A Change in Sentiment Away from Globalization

Globalization opened the doors to production efficiencies and profitability, but deglobalization, reshoring, nearshoring, and friend-shoring are all terms that have gained momentum with corporations, shareholders, news outlets and politicians over the past few years. While there has always been a concern over the tradeoffs between free trade and national interests, these terms have come to the forefront during the Trump presidency due to rising trade tensions between the US & China and the belief that globalization is bad for the American workforce. Fast forward to the end of the Trump presidency when the COVID-19 pandemic arrived at the beginning of the year in 2020. The pandemic brought on lockdowns across the globe, which inevitably caused supply chains to breakdown. Empty containers piling up on docks and an inability to operate businesses in a timely manner raised awareness of the risks we take when relying on outside sources for key goods and inputs. According to a Bank of America survey, an estimated 80 percent of global sectors experienced supply chain interruptions due to the pandemic causing 75 percent of companies to re-think their

Author: Chris Walker, CFA
Regions Investment Management, Equity Analyst

Fran Smitherman, CFA
Regions Investment Management, Director of Equity Research
In the technology sector, as detailed in a previous RIM publication, the Chips and Science Act of 2022 addressed concerns of our dependence on foreign semiconductor manufacturing, and this act is supplying funds to invest in domestic production opportunities that could have benefits as soon as 2023. Clearly more and more attention is being drawn to this issue, and the investment implications could be significant.

The United States is not alone in facing these concerns, and information technology is not the only sector of focus. At the beginning of 2022, Russia invaded Ukraine, exacerbating supply chain issues for oil & gas, fertilizers, and food products. The high dependence on Russian oil & gas, which supplies 40 percent of Europe’s natural gas, caused liquefied natural gas prices and the price of oil to skyrocket. Thankfully, the price of oil has come down from the highs of June, and Europe has experienced one of its mildest winters in decades. However, the problem of dependence on Russian energy still exists for many European countries.

The last few years have made it evident that countries need to become more self-reliant.

What are the Benefits of Deglobalization/Reshoring/Friend-shoring and Which Sectors Stand to Benefit the Most?

Industrials and construction seem to be the clearest potential beneficiaries of the move to re-shore, but it has been estimated that for every durable goods manufacturing job that is brought back to the U.S., an estimated seven indirect jobs would be created in industries like banking, retail, and more. Recently, there has been progress made already with the construction of the $12 billion Taiwan Semiconductor manufacturing facility in Phoenix, as well as eight other semiconductor plants expected to follow. The expectation is that all plants will be completed by 2026.

Many economists believe tech manufacturing has the potential to be the biggest driver of a reshoring boom. Although the apparel sector has seen the worst declines going back to 2000, U.S. tech manufacturing has fallen by over fifty percent during the same period. The tech sector accounted for over twenty percent of U.S. durable goods output in 2000, however, today the tech sector only accounts for roughly 13 percent.

With technological advancements that have been made since the turn of the century, opponents of reshoring will argue that automation has killed many of the manufacturing jobs that could return to the U.S. Since the pandemic brought on “The Great Resignation” where employees started quitting their jobs at record rates in 2021, this has caused employers to change their business models to rely more on automation and less on people. The manufacturing job market is at a seminal point in time, where the rise of robotics and other automated technologies will continue to be adopted by companies and require a more highly skilled workforce. According to a ThomasNet survey, 55 percent of companies plan to invest in some sort of automated technology in the next 12 months. This presents companies with an opportunity to invest in their current workforce and partner with trade schools, community colleges, and universities to better prepare students for high tech manufacturing job opportunities for graduates.

Protection of intellectual property is another top concern for multinational company executives as more evidence is brought to light of the blatant theft of companies’ trade secrets by the Chinese government. How China goes about IP theft is through their mandatory certification, China Compulsory Certificate mark, commonly known as the CCC mark. This mark is required for almost twenty percent of U.S. exports to China for products that include electrical equipment, information technology equipment, and automobile parts. Earning the CCC mark involves Chinese officials reviewing samples of production units that potentially can be reversed engineered, thus increasing the level of IP theft risk. Reshoring or friend-shoring can help alleviate this risk. It is becoming more apparent that company executives are opening up to the idea of reshoring based on a Kearney survey that states 92 percent of executives are receptive to the idea of reshoring.

In our view, Industrial companies with ties to manufacturing and automation could benefit from the building phase, and trucking companies can benefit from the near-shoring efforts, especially if more plants are built in neighboring Mexico.

Inflation and Labor Costs are the Impediments

The idiom of “Rome was not built in a day” comes to mind when thinking some of the main downsides to reshoring. Moving manufacturing operations out of a country and back to the U.S. will take considerable time and effort for
companies. Finding the most tax advantageous destinations for your company’s facilities, the inevitable delays a company will face in dealing with state and local governments in building a facility, and finding skilled labor are all reasons why reshoring will not happen overnight.

A contributing factor to globalization was lower labor costs found in other emerging countries, which still holds true today. Currently in the U.S., the federal minimum wage is $7.25/hr, however, on January 1st, 2023, 23 states and Washington D.C. saw their minimum wage increase by anywhere from $0.23 to $1.50 per hour. The state of Washington now carries the honor of having the highest minimum wage in the U.S. at $15.74 an hour. In China, current minimum wage is almost $8/hr, up almost 13% since 2017. Many U.S. companies have moved away from China and into other countries in Asia (e.g. Vietnam, India) for their manufacturing imports not only because of rising wages and the U.S.-China trade war, but because companies want to diversify away their country specific supply chain risk. Even though the minimum wage in China has picked up in recent years, there are still other countries where companies can have their products manufactured while saving on labor costs versus moving all operations back to the U.S.

Even with a slightly cooler than expected consumer price index reading for the month of December, the 6.6 percent inflation print on year-over-year basis is still exorbitantly high from a historical perspective, having not seen inflation at these levels since the late 1970s. If this high inflationary environment persists, companies might have to reconsider reshoring as it could intensify inflationary pressures. Surveys have shown that consumers favor products manufactured domestically, yet they were hesitant to pay more for products and would rather purchase cheaper foreign made goods. If reshoring leads to an increase in wages, it could lead to an increase in the cost of production, which could then be passed on to consumers in the form of higher prices. Overall, reshoring may have an impact on inflation, but it depends on factors such as the size and timing of reshoring, the condition of the economy, and the availability of skilled workers and resources will all play in determining the effect on inflation.

Naturally, productivity and labor cost efficiencies cannot be the only driver of a company’s decision to move manufacturing closer to home, but globalization’s impact on inflation cannot be overstated and deglobalization would most likely result in higher inflation generally. The key question is what will the consumer bear?

How Fast Can All of this Happen?

Corporate mention of reshoring has picked up on conference calls. But while companies are talking about it (as are shareholders), how fast can reshoring actually happen? The Kearney Reshoring Index is perhaps one of the most useful resources in tracking how quickly corporate America is putting their money where their mouth is.

According to Kearney, which measures the extent to which America is bringing manufacturing back from low-cost countries, the challenges are significant to do so, but the benefits of mitigating supply chain disruptions and increasing sustainability are gaining momentum and understanding. Things were heading in the right direction in 2018 and 2019 but since 2020, the direction of the index has reversed. Nevertheless, Kearney believes that due to the pandemic, trade wars and ongoing supply chain disruptions, American companies are getting more serious. We will continue to watch the Kearney Index to see if the 2022 and 2023 reports show any signs of progress.

Conclusion: What is the Happy Medium?

Companies will ultimately need to find the right balance between the benefits and drawbacks of reshoring. In order to achieve a happy medium, companies will need to conduct a cost-benefit analysis on reshoring and make decisions about which products and operations to reshere, and which to keep offshore. Companies can bring some operations closer to home while still outsourcing less critical components to countries where labor is cheaper and the risk to intellectual property is low.

What we do know is reshoring will not happen overnight, and the more complex the product or operation, the longer the advancement of reshoring will take. However, it is fair to say that the reshoring of manufacturing jobs has the potential to create many indirect jobs across a myriad of sectors, benefitting the local economy and having a clear impact on overall employment and economic growth.

References:
1. Bank of America: https://rsch.baml.com/report?q=JSjoKAJHh7CgWz2d7j-Uw&ps=true&pv=validated
2. UNCTAD: https://unctad.org/news/china-rise-trade-tit
Domestic Manufacturing

© Regions Bank, Member FDIC. This publication has been prepared by Regions Investment Management, Inc. (RIM) for Regions Bank for distribution to, among others, Regions Wealth Management clients. RIM is an Investment Adviser registered with the U.S. Securities & Exchange Commission pursuant to the Investment Advisers Act of 1940. RIM is a wholly owned subsidiary of Regions Bank, which in turn, is a wholly owned subsidiary of Regions Financial Corporation. While the commentary accurately reflects the opinions of the Analyst by whom it is written, it does not necessarily reflect those of Regions Bank or RIM. This publication is solely for information and educational purposes and nothing contained in this publication constitutes an offer or solicitation to purchase any security, the recommendation of any particular security or strategy or a complete analysis of any security, company or industry or constitutes tax, accounting or legal advice. Information is based on sources believed by RIM to be reliable but is not guaranteed as to accuracy by Regions Bank, RIM or any of their affiliates. Commentary and opinions provided in this publication reflect the judgment of the authors as of the date of this publication and are subject to change without notice. Certain sections of this publication contain forward looking statements that are based on the reasonable expectations, estimates, projections and assumptions of the authors, but forward-looking statements are not guarantees of future performance and involve risks and uncertainties, which are difficult to predict. Investment ideas and strategies presented may not be suitable for all investors. No responsibility or liability is assumed by Regions Bank, RIM or their affiliates for any loss that may directly or indirectly result from use of information, commentary or opinions in this publication by you or any other person. Trust and investment management services are offered through Regions Wealth Management, a business group within Regions Bank. Investment advisory services are offered through RIM. Employees of RIM may have positions in securities or their derivatives that may be mentioned in this report or in their personal accounts. There could also be times that some securities mentioned in this report are held in a RIM model portfolio. The companies mentioned specifically are sample companies, noted for illustrative purposes only. The mention of the companies should not be construed as a recommendation to buy, hold or sell positions in your investment portfolio.

In some cases, RIM’s investment management services and/or strategies will be utilized by Regions Wealth Management for its trust and investment management clients. RIM receives compensation from Regions Bank for providing certain services, including market commentary. When applicable, RIM receives additional compensation based upon the assets in Regions Wealth Management client accounts managed according to RIM’s strategies. For additional information concerning RIM or its strategies, please see RIM’s Form ADV Part 2A, which is available by calling 205-264-6735. Neither Regions Bank, nor Regions Asset Management (collectively, “Regions”) nor the Regions Bank subsidiary, Regions Investment Management, Inc. (RIM), are registered municipal advisors, nor provide advice to municipal entities or obligated persons with respect to municipal financial products or the issuance of municipal securities (including regarding the structure, timing, terms and similar matters concerning municipal financial products or municipal securities issuances) or engage in the solicitation of municipal entities or obligated persons for such services. With respect to this presentation and any other information, materials or communications provided by Regions or RIM, (a) Regions and RIM are not recommending an action to any municipal entity or obligated person, (b) Regions and RIM are not acting as an advisor to any municipal entity or obligated person and do not owe a fiduciary duty pursuant to Section 15B of the Securities Exchange Act of 1934 to any municipal entity or obligated person with respect to such presentation, information, materials or communications, (c) Regions and RIM are acting for their own interests, and (d) you should discuss this presentation and any such other information, materials or communications with any and all internal and external advisors and experts that you deem appropriate before acting on this presentation or any such other information, materials or communications.