

# INVESTING IN THE U.S. POST 2012 ELECTION

## OBSERVATIONS & PREDICTIONS

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# U.S. POLITICAL CLIMATE

## U.S. POLITICAL CAMPS' POSITION ON CHINA

### WINNERS

"I have always emphasized that we welcome China's peaceful rise, that we believe that a strong and prosperous China is one that can help to bring stability and prosperity to the region and to the world. And we expect to be able to continue on the cooperative track that we've tried to establish over the last three years." – President Obama

"The most critical relationship to get right is that between the United States and China. Every day, the affairs of our nations and the livelihoods of our citizens grow more connected." - Joe Biden

### LOSERS

"China is stealing our intellectual property, our patents, our designs, our know-how, our brand names. They're hacking into our computers, stealing information from not only corporate computers but from government computers. And they're manipulating their currency." - Mitt Romney

"China has been a currency manipulator for years and years. On my first day in office, I would label China a currency manipulator." He also accused China of "cheating" and pledged a "crack down on China." – Mitt Romney

# FISCAL CLIFF, TAX & BUDGET

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## > Fiscal Cliff, Tax & Budget

- The most important issue for Congress in the Lame Duck session is to compromise on a plan to avert the “Fiscal Cliff.” The fiscal cliff is the term used to refer to the combination of expiring tax provisions and across-the-board spending cuts (sequestration) that are scheduled to take effect at the end of the year unless Congress can agree upon a legislative solution.
  - Sequestration is set to take place on January 2, 2013. The cuts will total \$110 billion in spending across defense and domestic programs.
  - The Bush-era tax cuts, enacted in 2001 and 2003 and extended several times since then, include individual marginal, capital gains, estate and dividend tax rates, as well as a number of other provisions. Last extended for two years at the end of 2010, they are set to expire on December 31, 2012.

# FISCAL CLIFF, TAX & BUDGET

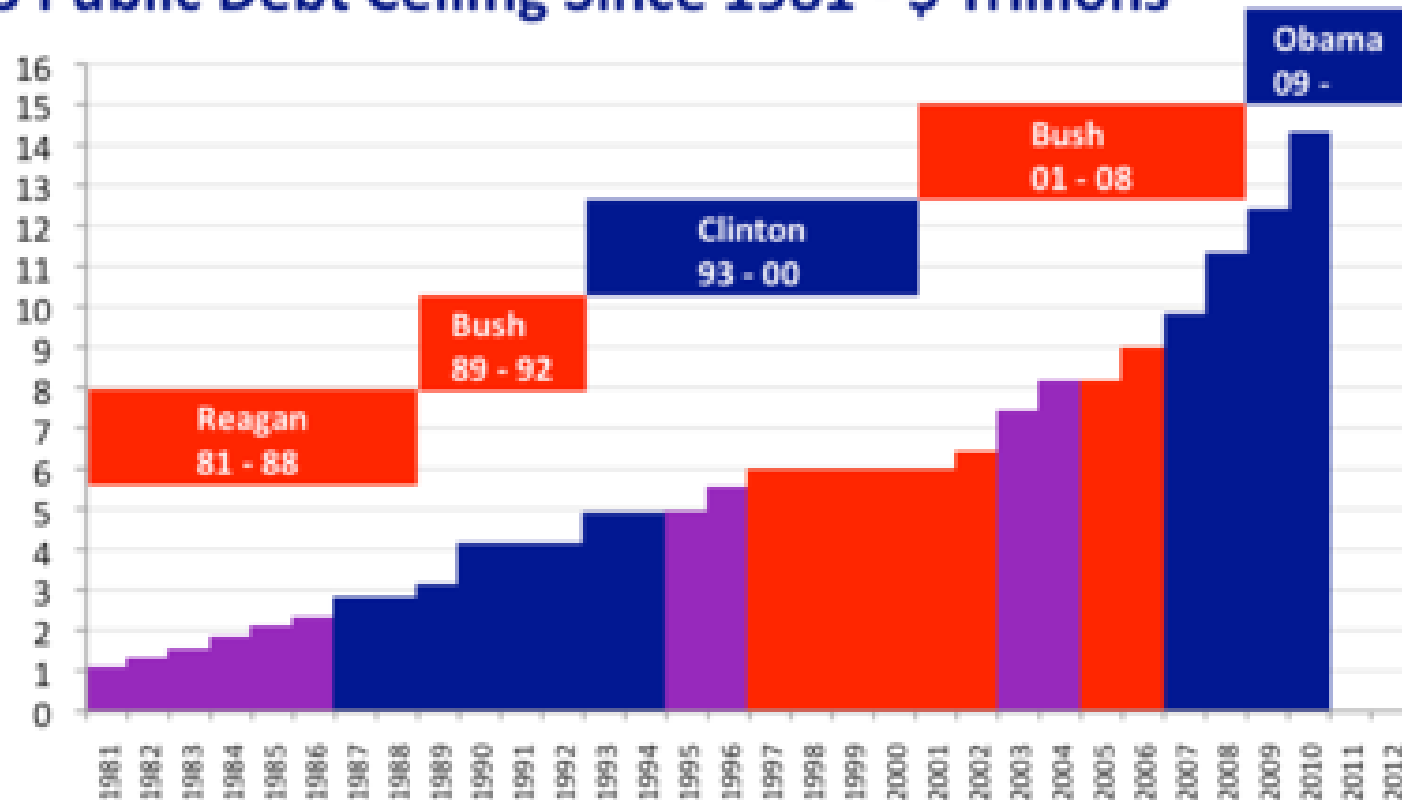
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## > Fiscal Cliff, Tax & Budget

- President Obama, along with Democrats and Republicans in Congress, will have to agree upon a basic framework for tax reform pertaining to individuals, business and international taxation.
- The debt-ceiling is expected to be reached in mid-January. Congress must agree to raise the debt-ceiling. Failure to do so would result in the Administration being unable to fund all its spending, and therefore would have to cancel or delay some spending – a situation sometimes referred as a partial government shut down.

# RISE OF THE U.S. DEBT CEILING

## US Public Debt Ceiling Since 1981 - \$ Trillions



Legend for control of Congress:

Split Congress

Republican Controlled

Democrat Controlled

# FISCAL CLIFF, TAX & BUDGET

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## > Fiscal Cliff, Tax & Budget

**OBSERVATIONS/PREDICTIONS:** A deal will be reached. It will likely not be a comprehensive solution covering tax reform as well as spending adjustments or entitlement programs e.g. Medicare, Social Security.

In spite of the political posturing all realize that top line GDP growth is necessary and indeed the thing that helps fix the economy.

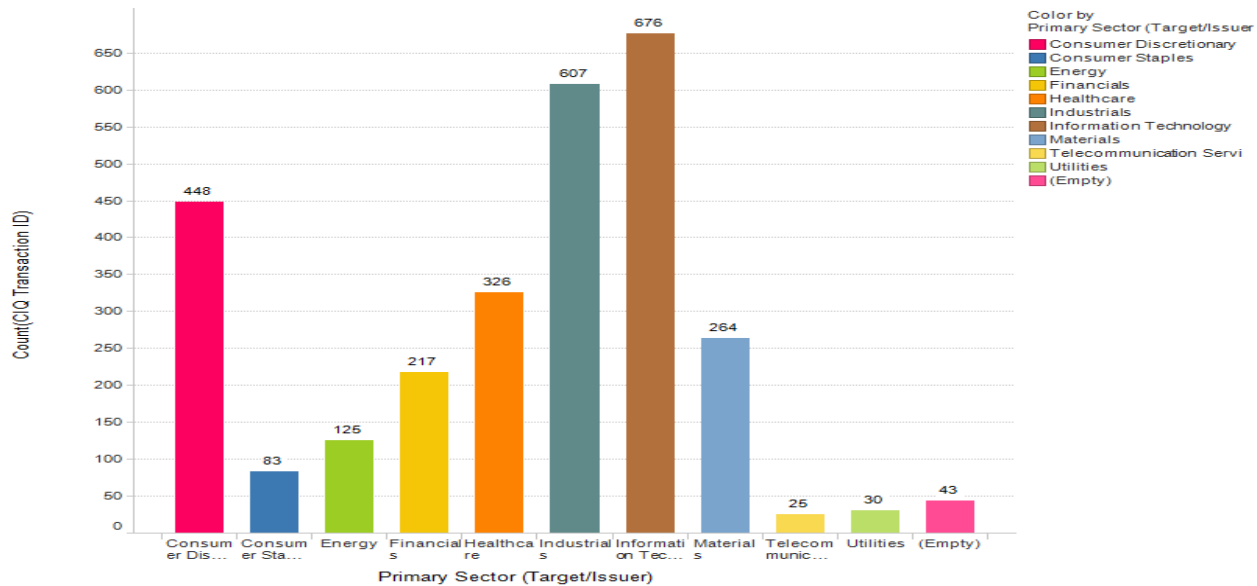
The Administration will be looking to foreign investment to help drive revenue growth.

# FOREIGN DIRECT INVESTMENT IN THE U.S.

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- > Broadly speaking, the U.S. has a fundamentally open economy and very small barriers to foreign direct investment (FDI).
  - The United States is the world's largest recipient of FDI.
  - U.S. FDI totaled \$194 billion in 2010.
  - 84% of FDI in the U.S. in 2010 came from or through eight countries:
    - Switzerland
    - United Kingdom
    - Japan
    - France
    - Germany
    - Luxembourg
    - Netherlands
    - Canada

# FOREIGN DIRECT INVESTMENT IN THE U.S.



- White House data reported in June 2011 found that a total of **5.7 million** workers were employed at facilities highly dependent on foreign direct investors.
- Thus, about **13%** of the American manufacturing workforce depended on such investments.
- The average pay of said jobs was found to be around **\$70,000** per worker, over **30%** higher than the average pay across the entire U.S.



## > Foreign Direct Investment in the U.S.

- Report to Congress on incentives and disincentives to foreign investment due on May 7, 2013.
- U.S. Position on investment in the U.S is complex. We want Chinese companies to invest – but are troubled by their desire to invest only in certain sectors (e.g. Telecommunications, high-tech, defense).
- Direct investment in the U.S. by a foreign entity may be subject to a national security review by the Committee on Foreign Investment in the United States (CFIUS). Depending on the results of that review, the U.S. government may block or require significant modification of a proposed transaction.

**OBSERVATION/PREDICTION:** Expanding the oversight of M&A deals by CFIUS is something that bears close observation. The Administration is thought to be more receptive to Chinese investment in certain sectors than Congress. This is due to the Administration's desire for investment growth in the U.S. to boost revenues. Who will win?

## > Trade Policy

- Despite some opposition in Congress, trade discussions with China have been progressing cautiously, despite opposition in Congress. It is expected that these talks will continue.

**OBSERVATION/PREDICTION:** This is considered a positive sign for Chinese investment in the U.S. by most observers, as a continued dialogue on trade agreements generally produces positive results.

## > Trade Policy

- Work will continue on the Trans-Pacific Partnership (TPP) with the goal of completing the multilateral TPP negotiations in 2013, and submitting a final agreement to Congress in 2014. Countries involved in the discussions include: Australia, Brunei, Canada, Chile, Malaysia, Mexico, New Zealand, Peru, Singapore, the U.S. and Vietnam. It is uncertain whether or not Japan and South Korea will join the agreement.
- Permanent Normal Trade Relations status for Russia and Moldova is likely to be granted.

**OBSERVATION/PREDICTION:** This development is instructive for Chinese investment across sectors. This normalization of trade status measure was not favored in Congress as recently as last year. It will eliminate trade bans for Russia that have existed since the beginning of the “Cold War.” If passed, it may symbolize a bi-partisan effort to remove trade barriers that bar goods, services and investments that would help boost revenues for other countries where there has been opposition in the past.

# U.S. TRADE POLICY

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## > Trade Policy

- Free Trade Agreement talks between the U.S. and EU are expected in 2013. The debt crisis in Europe and elusive American growth are pushing both sides to consider knocking down the final barriers to trade.
- The Obama Administration, particularly the Commerce Department, will continue to boost its National Export Initiative (NEI), in which the President has promised to double exports within five years. If the economy continues its gradual improvement, the Administration has a chance to meet its goal for the NEI.
- The Administration may also seek to complete work on a long-stalled Trade and Investment Framework Agreement (TIFA) with Taiwan. A successful TIFA with Taiwan could lead to discussions on a bilateral FTA, for which supporters of Taiwan in Congress have long advocated.

**OBSERVATION/PREDICTION:** Again it is possible that this Administration is signaling a broad theme of trade friendliness across numerous lines. This would seem to benefit U.S./China relations.

## > Financial Services

- Two years after the passage of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act), regulatory agencies such as the Commodity Futures Trading Commission (CFTC) and the Securities and Exchange Commission (SEC) continue working steadily to implement financial services reform in the United States.

**OBSERVATION/PREDICTION:** With growing criticism over the international implications of the law, the delayed rulemaking process, and potentially burdensome regulations, the 113th Congress will face important questions regarding whether to make technical, or even substantial, amendments to the law. There is support for legislation that softens or eliminates some of the harsh regulatory acts of Dodd-Frank. The prediction is that the Administration supports some changes in the law.

## > Defense and Foreign Policy

- The Administration and Congress are seeking a way to avoid the \$55 billion automatic defense spending cuts (Sequestration).
- In 2010, President Obama announced an Export Control Reform Initiative to modernize and streamline U.S. export controls on defense and dual-use goods and technologies. The defense industry widely supports the initiative, arguing that the existing export control regulations are complicated and burdensome and that, especially with respect to military products, U.S. export controls are overly detailed and intrusive.

**OBSERVATION/PREDICTION:** This initiative is another area where the Administration and Department of Defense are in alignment to eliminate burdensome anti-business regulations. Their sentiments are not shared by many members of Congress. Look for a hard-fought compromise on this issue. Analysts are not sure as to what effect, if any, this may have on Chinese investment. Foreign investment in “defense” related companies is generally disfavored and currently “defense” is broadly defined.

## > Defense and Foreign Policy

- Secretary of State, Hillary Clinton will depart as President Obama's second term begins. Possible replacements include Susan Rice, the current U.S. ambassador to the United Nations and U.S. Senator John Kerry. However, White House sources are now talking about Senator Kerry as a possible replacement for Leon Panetta as Secretary of Defense.
- The President now must deal with the unexpected departure of former General Patreus as head of the CIA.

**OBSERVATION/PREDICTION:** Unfortunately, there appears to be a battle looming between the Senate and President as he appears to be strongly advocating Susan Rice for the Secretary of State job. Her statements after the attack on our Consulate in Benghazi, Libya have made her a controversial figure with Capital Hill. Look for a compromise as a confirmation battle would be destabilizing and not in the best interest of the U.S. Recent comments support this as three key Senators who opposed Rice have signaled that they may support her if certain conditions are met.

## > Energy Policy

- U.S. energy production has increased over the past four years due to new energy projects such as the construction of wind and solar farms and an increase in hydraulic fracturing and horizontal drilling technologies.
- The Obama Administration is seeking to develop all energy sources: oil, gas, wind, solar, nuclear and biofuels. There is an emphasis to boost green energy initiatives and support energy research and development.

**OBSERVATION/PREDICTION:** The increase in U.S. energy production will likely have profound geopolitical ramifications. The dependence of the U.S. on foreign energy sources is decreasing faster than predicted. The geo-political ramifications of this need to be watched carefully. That said, the prospects for inbound investment in this sector will be very good – and favorably received by this Administration. There will be numerous incentives offered for foreign investment in this sector.



## > Energy Policy

- Congress has not passed a comprehensive, bipartisan energy bill since 2007 and is not likely to do so in the 113<sup>th</sup> Congress considering the divide between “pro-development” and “pro-conservation” Members of Congress.

**OBSERVATION/PREDICTION:** Energy legislation is less partisan than other issues – it is more driven by where the Member comes from than the party to which he or she belongs (e.g. Virginia, Texas, Oklahoma, West Virginia). A bill that combines pro-development provisions, pro-conservation provisions, and other consensus provisions could emerge in the Senate. However, it is doubtful if it would pass the House. Therefore, the Obama Administration is likely to use existing statutory authority to advance its energy agenda where possible. Two items where this is likely are the approval of the northern leg of the Keystone XL pipeline and the approval of one or more of the pending applications to build LNG export facilities. Approvals for these items are expected early in 2013. This may put the U.S. in conflict with the Chinese and their energy objective in Canada.

## > Environmental Policy

- In its first term, the Obama Administration accomplished much of the President's environmental agenda through agency action, without the need for new legislation.

**OBSERVATION/PREDICTION:** It is expected that the Administration will continue using its existing authority to effectuate its environmental goals of reducing GHG emissions and other pollutants, cleaning and restoring water resources, and, by extension, addressing climate change. The Obama Administration will continue to encourage energy production on public lands, reduce imports of crude oil, and mitigate potential environmental impacts of domestic production. The Obama Administration will utilize the grant-making process to further influence decisions made at the state and local level, as well to provide incentives for the private sector, including small businesses and entrepreneurs, to drive innovations in new technology. This would translate into providing incentive monies for inbound investment in this Sector.

## > Technology and Communications

- Cybersecurity will continue to be a major topic. Although legislation is not likely, the Obama Administration is currently developing an Executive Order that reportedly would require agencies with regulatory authority over critical infrastructure to develop cybersecurity standards.

**OBSERVATION/PREDICTION:** Efforts to enhance online consumer privacy protections remain a high priority. The framework for International Telecommunications Regulations (ITRs) will be reconsidered at the International Telecommunications Union in Dubai, United Arab Emirates, from December 3rd through December 14th, as part of the World Conference on International Telecommunications (WCIT).

## > Technology and Communications

- Despite bipartisan support for bills in the 112th Congress to combat piracy (the theft of intellectual property online) through the Stop Online Piracy Act (SOPA) and the Protect IP Act (PIPA), Congress was unable to enact these bills due to claims of censorship. However, it is anticipated that the legislation will resurface in the new Congress because it has found broad support among companies in the content, pharmaceutical, technology and fashion industries that rely on strong copyright protection.

**OBSERVATION/PREDICTION:** Foreign ownership of, and involvement in, domestic communications networks will be a significant topic of debate in 2013. It is doubtful that there will be any relaxation of the current position against Chinese ownership of domestic communication companies/networks.

# LABOR ISSUES

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## > Labor Issues

- Labor unions want the Obama Administration to raise taxes on wealthy Americans and avoid cuts into Social Security and Medicare. Unions are also pressing for new measures that might help boost their sagging membership, such as:
  - New investment in infrastructure that would bring construction jobs for trade unions.
  - Immigration reform (and a path to citizenship for 11 million of undocumented immigrants) would create a vast new pool of potential union members.
  - New regulations could remove some obstacles to union organizing.

# LABOR ISSUES

## > Labor Issues

- The Obama Administration may issue more regulations targeting workplace safety. These regulations may include reviving proposed rules to protect workers from cancer-causing and lung-damaging silica, often found in the dust at construction sites and glass manufacturing operations and new standards for combustible dust that can cause explosions. Business groups have opposed the regulations, saying they overreach and would raise employers' costs by millions of dollars.

**OBSERVATION/PREDICTION:** The Administration will be under significant pressure to increase Union membership in the private sector workforce which has sunk to an all time low of around 7%. Expect labor leaders to demand sweeping pro-labor initiatives. The Administration will likely not be able to get such bills through Congress. Expect more Executive Orders and Agency actions. These actions will be strongly opposed in all right-to-work and some non-right to work states, where a pro-business, pro-investment business climate exists.

# IMMIGRATION REFORM

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## > Immigration Reform

- Immigration reform is a hot topic after the recent elections due to the strong showing by the Latino and Asian-American population. Both parties have very different views on how to deal with the 11 million undocumented workers.
- House leaders plan to bring up a high-tech visa bill during the lame-duck session. The legislation would grant permanent residency to foreign graduates of American universities with advanced degrees in science, technology, engineering and mathematics, known as the STEM fields. If leaders manage to reach a bipartisan consensus, it could pave the way for more immigration agreements in the next Congress.

# IMMIGRATION REFORM

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## > Immigration Reform

- Family reunification is another area being discussed. One plan would allow the spouses and children of current holders of green cards to move to the United States without a work authorization until they get green cards of their own, according to lobbyists. Current rules force many families to live apart for several years while they await visas. Another proposal would split the 55,000 visas, with half going to high-tech foreign graduates and half to family reunification measures.

**OBSERVATION/PREDICTION:** There will be some level of Immigration Reform as there is bi-partisan support for this. Such reform could help skilled workers from the Pacific Rim to enter and remain in the U.S. to work.



# SECTORS FOR GROWTH

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- > Advanced Manufacturing
- > Aerospace - Shipbuilding
- > Core Industries
  - Paper
  - Coal
  - Automotive
  - Chemical
- > New Industries
  - Natural Gas
- > Growth Industries
  - Energy
  - Hospitality
  - Long Term Care

# M&A/PRIVATE EQUITY

- > M&A may remain the best way to enter the U.S. to begin to grow.
- > Private Equity looks promising.
  - Private equity deals 2012:
    - Q2 = \$17.1B (USD)
    - Q3 = \$45.0B (USD)
  - This volume has pushed purchase price multiples higher.
  - Prediction from many well regarded analysts is that 2013 could be a watershed year for deals involving private equity.
    - Low interest rates
    - Banks being more aggressive
    - Deal leverage has dropped in 2011 and 2012
- > U.S. Growth will continue and it will be a stable investment in an unpredictable world order. U.S. GDP is now expected to exceed 2% in 2013 and this is likely to produce a stable investment environment in the U.S. in an otherwise unpredictable world.

# CONCLUSION

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- > The election has confirmed that the majority of U.S. Voters want to end the gridlock in Washington.
- > Look for more bi-partisanship and compromise on most all of the areas discussed.
- > Job growth and renewed economic growth will be a top priority in Washington.
- > Unemployment remains at an unacceptable 8% and Congress has gotten the message from voters and their states to come to agreement on legislation to lower it.
- > Trade Policy discussion will be difficult as to China, as labor unions in particular will strongly oppose any expansion of China trade.
- > Energy will be a most-favored area of U.S. growth and inbound investment in clean energy will be well-received.

# CONCLUSION

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- > Core industry investment by Chinese companies in paper, pulp, mining and steel will be attractive.
- > Development of U.S. natural gas will be a priority and an attractive area for investments and incentives.
- > Long term care will continue to be a growth sector.
- > Hospitality will rebound quickly as the economy strengthens. This industry sector was hit very hard during the financial crisis and ensuing recession.
- > Immigration reform will take place and will likely have a positive impact on skilled Asian workers seeking jobs in the U.S. or seeking to remain in the U.S. Included in this reform is likely to be relief for Asian students graduating from U.S. colleges and universities who want to remain in the U.S. to work.
- > “Sideline” money will continue to flow at an increased rate and M&A activity will grow, aided by strong private equity funding opportunities.