

# **Increasing Puerto Rico's Capacity to Compete Globally in Exports through the Implementation of Existing State Export Promotion Models**

**Economic Recovery Support Function**

**Disaster Recovery 4339-PR**

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## **Introduction**

According to the U.S. Department of Commerce, in 2016 over 304,000 U.S. companies (including Puerto Rico based companies) exported their products overseas. Of those companies exporting 98% are companies with less than 500 employees.

In the U.S. the small & midsize enterprises (SME) sector was responsible for approximately 33-35% all goods exported in 2016. A profile of the average U.S. SMEs demonstrates the following traits:

- 59% export to one market
- 93% export from one location
- Canada is their top market, followed by Mexico
- 32% sell their products in Europe
- Colombia, So. Korea and Vietnam are top markets for U.S. exporters

**(DOC, U.S. Export Fact Sheet)**

## **Why States Promote Exports**

According to The Business Roundtable, an association that represents the chief executives of the top corporations in the U.S., 95% of all of the world's consumers and over 80% of the world's purchasing power is located outside the United States. From 2006 to 2016 exports in the U.S. have outpaced GDP growth and it is estimated by the Business Roundtable that international trade supports over 36 million American jobs. For example, since the signing of the North American Free Trade Agreement in 1993, U.S. exports to Mexico have grown from \$41 billion to

over \$231 billion per year in 2016 (CRS Report No.R42965, p.15, 2017). In 2016 total trade between Mexico, Canada and the United States reached \$1.3 trillion. (US Chamber of Commerce)

The following states led in jobs created by exports of goods:

| State         | Jobs    | State       | Jobs    |
|---------------|---------|-------------|---------|
| 1. Texas      | 910,306 | 6. Michigan | 271,300 |
| 2. California | 683,800 | 7. Ohio     | 249,000 |
| 3. Washington | 332,600 | 8. Florida  | 232,300 |
| 4. Illinois   | 325,400 | 9. Indiana  | 182,200 |
| 5. New York   | 295,300 | 10. Georgia | 181,700 |

(International Trade Administration: Industry & Analysis Division)

In recent years the field of economic development has refocused its efforts and resources from investment attraction strategies to assisting and strengthening their export promotion initiatives and programs. It is easier and more economical to offer assistance and incentives to existing exporters than to attract out of state or foreign investment. According to the International Economic Development Council, existing companies create over 70% of new jobs in a community and are the most effective way to increase local and state tax revenues.

Export Promotion is a very beneficial two-way street as many small and midsize exporters lack the resources and know-how required to establish an internal export sales department and compliance team to guide them through the proper steps. Consequently, they reach out to state export promotion agencies and/or to local federal government export promotion programs for training, counseling, guidance and access to foreign markets.

State export promotion agencies have developed a number of incentives and export accelerator programs. Some offer local exporters monetary incentives in covering the costs of export related expenses such as conducting market research, developing an export strategy, development of their export compliance program, travelling to trade missions and translation services. Others provide technical assistance including dealing with customs and trade tariffs.

State agencies have been very resourceful in identifying additional sources of funds to help companies fund export-related activities. For example, for fiscal year 2017 the Michigan's Economic Development Corporation not only received state assigned funds for export promotion, they added an additional \$900,000.00 from the U.S. Small Business Administration's State Trade Expansion Program (STEP) to run their Michigan- State Trade Expansion Program (MI-STEP). This program offers local exporters \$7,000 to \$15,000 in direct reimbursements for export related expenses (Michigan Economic Development Corporation).

The SBA STEP program continues to be a sought-after source of funds for export promotion initiatives. On September 19, 2018 the SBA announced that it had awarded \$18 million to fund STEP programs in 47 states. For 2018, the Puerto Rico Trade & Export Company received \$300,000.00 and matched those funds with \$100,000. Congress has extended the STEP Program until 2020. Many states use STEP as a primary source of funds for export promotion initiatives. However, other states have developed more sophisticated programs that use STEP as one component of an overall state export promotion strategy.

Funding from additional sources such as state legislative assignments, non-profit foundations and from other federal agencies enables such programs. The Virginia Economic Development Partnership (VEDP) obtained funds from the Department of Defense *Office of Economic Adjustment*, from STEP, the Virginia General Assembly, and from the JP Morgan Chase-Brookings Institute *Global Cities Initiative* for the development of metropolitan area export promotion programs. Virginia has followed a very aggressive model that focuses on exports as a key component of economic development and business retention. For example, it has a number of export promotion and export accelerator programs that run parallel, and targets specific industrial sectors.

For example:

- **Going Global with Defense Initiative** targets defense, cybersecurity and law and order/security industrial sector
- **VALET Program** targets small and midsize companies with some export experience or that are ready to enter the international markets
- **Going Global with Coal & Energy Technology Initiative** targets companies in the economically depressed coal mining industry that need to diversify and want to export their goods and services
- **STEP Program** available for any other exporting company not covered by one of the above mentioned programs

While other states have managed successful export promotion programs, The Virginia Economic Development Partnership has enhanced its international trade program to meet the needs of the State's export community. The award winning Virginia Leaders in Export Trade (VALET) program is considered the best export promotion program in the United States and it is now being emulated by other states. Therefore, for purposes of this report I will be discussing the workings of the VALET program and how components of this program could be implemented to help Puerto Rico based companies expand overseas and diversify their markets.

## **Puerto Rico as an Exporting Jurisdiction**

According to the Puerto Rico Planning Board (JPPR) the Island's exports to the rest of the world totaled over \$71 billion in 2017. This includes shipments to the United States which totaled \$30,668,200,000. If we included shipments to the Continental U.S. (CONUS) as true exports, Puerto Rico would be considered the 5<sup>th</sup> largest exporter in the Western Hemisphere (Workman, 2018). Since the island is part of the U.S. Customs Territory, products manufactured or produced are U.S. products, thus shipments to and from Puerto Rico are part of interstate commerce. However, for statistical purposes only, the U.S. Census Bureau's Foreign Trade Division requires that all companies shipping products from P.R. to the U.S. and vice versa file an electronic export information report (EEI) under the Automated Export System.

While Puerto Rico could be considered a major exporting jurisdiction, the reality is that the Island's business community lacks an export culture. Most exports originate from major manufacturing operations such as pharmaceutical, medical devices, chemicals, and electronics. Few Puerto Rican companies have a clear understanding of how an export transaction is conducted. Furthermore, few have established the internal procedures necessary to become an exporting company. Given the complexities of exporting and the changing nature of international trade, handling exports can lead to costly problems if comprehensive training is not provided to the parties involved.

Therefore, a possible solution to help increase the participation of local companies in exporting could be the implementation of a proven export promotion program that can help these companies grow internationally and diversify their sources of income. The Virginia VALET Program could be a fitting option for Puerto Rico.

The remainder of this document will describe the VALET Program and how it operates. While not all parts of the Program may be suitable to the local needs, it can serve as a blueprint for developing a Puerto Rican export accelerator initiative that could complement Puerto Rico Trade and Export Company's existing programs.

## **The Virginia Leaders in Export Trade Program**

The VALET Program is a two year export accelerator program created in 2002. The primary goal of VALET is helping Virginia based companies diversify by selling their products and services

overseas to new markets and in this manner assuring their long-term growth and global competitiveness. By increasing exports from Virginia based companies the VEDP looks to increase job creation in high-skilled jobs and increase the state's tax base. In 2017 exports in the Commonwealth of Virginia grew to \$35.9 billion and tax revenues from export reached over \$2 billion. (Virginia Economic Development Partnership)

While Virginia is still not among the top 20 exporting states, they have developed an award winning program which now serves as the model for other states and jurisdictions in the United States. As the author of this paper states, "During my time as program co-manager of the VALET Program I witness at least 10-15 visits from other states export promotion agencies wanting to learn from our best practices". The Program has a number of qualities that make it a unique and highly sought out initiative, but the key differentiator is that the VALET Program is not managed like a government program; it is run as a private enterprise. Both program managers make themselves available to meet or talk to clients 7 days a week. For example, if a VALET company is on a trade mission in the Middle East where Sundays are work days, program managers make themselves available to assist the client by phone and support the client's needs during weekend hours.

## **Components of the VALET Program**

The composition of the VALET Program is distinctive from other export promotion programs. It assists companies in speeding up their international trade efforts by accelerating the development of an export plan, offers reimbursement for export related expenses, provides access to expert guidance, provides for market research, and links the client to Virginia's overseas network of in-country consultants.

As previously stated, the VALET Program is a two year export accelerator program. The International Trade Division at VEDP selects 50 candidate companies. Prospective candidates must meet some minimum criteria to be considered for VALET.

Requirements for participation are:

- Minimum of 20 employees
- 3 years in business
- \$2,000,000 in annual sales
- Companies must commit to travel with VALET on a trade mission or international trade show
- Companies must invest in developing an export strategy and have a completed market research to a targeted country before entering the Program

- Complete the VALET Program application

Since Puerto Rico has a small export community, the above criteria may be customized to meet local needs.

### **First Step**

Candidate companies are pre-selected by the Virginia Economic Development Partnership's regional international trade managers. Candidates selected for the program have already had some experience working with regional trade managers and they are usually the "cream of the crop" of companies in that specific region. Some candidate may have no experience in exports, but the trade manager has identified their products and services as ripe for internationalization. Once the client is pre-selected, the VALET program manager has an introductory meeting with the candidate and presents the benefits of the program. If the candidate decides to apply, his application goes into a competitive selection process.

### **Second Step**

Candidates selected to VALET must complete and submit a number of additional documents as the program requires a high level of commitment that will guarantee completion of the VALET Program. In addition, candidates are eligible for monetary and non-monetary incentives.

### **Third Step**

Selected companies are brought in for a meet and greet and a full day of orientation where they will learn how the VALET Program operates, the procedures they must comply with and how to best take advantage of the Program. The second part of the day consists of scheduled roundtable meetings with the "VALET Program Partners". The Program partners are a group of firms that are experts in various fields and are there to assist the candidates in a number of areas such as legal matters, export compliance, marketing, accounting and logistics. Once the orientation is completed the participants will return to their offices and start the process of developing their plan of action.

### **Fourth Step**

Within a few weeks of the orientation meeting the program manager and research manager will meet with the VALET companies to develop an export strategy that best meets the objectives of the company. This meeting can take from two hours to a couple of or visits with the client. The objective is to produce a simple but detailed plan of action that covers all the client needs. Developing a strategic plan involves the following components:

1. Collecting initial data such as the number of jobs on day one, current international sales numbers, percentage of total sales that come from international sales
2. Export goals: identify target country/countries, list of action items that must be taken to achieve these goals and objectives, list of prospective trade missions, trade shows or travel to market/s
3. Market research needs and in-country research needs such as identifying prospective clients. This can be primary or secondary market research that can be done internally or with the assistance of an in-country consultant
4. Set up a schedule of meetings with VALET Program Partners to discuss gaps and strategic requirements such developing an export compliance program for the company, international tax implications from export sales, optimization or further website development to better reach international clients, translation of marketing materials
5. Set up call with in-country consultant from VEDP Network of overseas consultants to discuss opportunities within the specific market/s
6. Export / trade financing requirements

The preparation of an export strategy forces companies to conduct an export readiness self-assessment to determine if they are capable and ready for exporting. According to the Australia Trade Commission this is one of the most important components of an export strategy. It answers two important questions:

1. Does your company have the production capacity to fulfill the needs of the local market as well as the needs of a new market?
2. Does your company have a dedicated export team in place?

**(Australia Trade, 2019)**

At the VALET Program these questions come up during the pre-qualification meeting and not the strategic export plan of action meeting. This assessment should always be part of any export promotion initiative's qualification criteria.

## **Follow up After Initial Steps**

After the export strategy is defined and completed, the client can expect a minimum number of follow up meetings from the VALET team in support of their efforts. In essence, the VALET team acts as an export management team with the additional support of the Program Partners and other resources made available. VALET companies will participate in a number of programmatic events such as trade shows, webinars, annual VALET networking and educational seminars that include topics relevant to exporting. These events offer participants the opportunity to exchange experiences with other exporters and could lead to working together on an international bid or project, meet with experts to discuss specific problems and meetings with overseas consultants.

For example, seminars the VALET Program prepared for their clients include:

- Understanding NAFTA Rules & How to Navigate these market regulations
- Best Practices in Digital Marketing, Search Engine Optimization & Translation
- Developing a mobile website for the international market
- Getting Paid, Managing Risk in International Business
- How to Develop an Export Compliance System
- Picking Top Notch Markets
- Using IC-DISC as a tax savings for exporters

## **Resources Made Available to VALET Companies**

The final components of the VALET Program are the resources that make the Program unique in comparison to other export promotion programs in the States and gives Virginia exporters a competitive edge in contrast to other exporters in the United States.

These key resources are:

- Monetary reimbursement for export related expenses
- VALET Program Partners
- VEDP Network of In-Country Consultants
- VALET Program Research Services

## **Monetary Reimbursement**

Companies entering the VALET Program are offered \$30,000 to cover any export related costs incurred during their 2-year participation in the Program. Funds can be used to reimburse the following costs:



- Market research
- Expenses related to participation in trade shows
- Costs of Market visit (except transportation and lodging)
- Registration fees for trade missions
- Developing an export compliance system
- Legal work: distribution agreements, contracts
- Marketing & advertisement
- Translation services
- Custom brokerage and logistics advising (transportation of cargo to be sold is not reimbursable)
- Website development
- Fees for letters of credit and export documentation

A number of other expenses are allowable but companies must reach out to program managers for prior approval.

### **VALET Program Partners**

VALET Program Partners are one of the most unique components of the Program and is what most graduates refer to as the “most valuable component” of VALET. Program Partners are a list of firms with a special level of expertise in international trade that can offer counseling, advise and professional services in fields related to exporting. Program Partners cover the following areas:

- Accounting
- Financial Services – Banking for trade finance and foreign exchange
- Advertising & Marketing
- Web Design
- Custom Brokerage and Logistics Services
- Freight Forwarding
- Translation Services
- Insurance
- Corporate Strategy
- Legal Services
- Export Compliance Counseling

Companies participating in the VALET Program are allowed to use the VALET reimbursement funds to cover the cost of the program partner services. Program partners offered their services at a discounted rate.

## **VEDP Network of In-Country Consultants**

The Virginia Economic Development Partnership has a network of 57 overseas consultants that cover 75+ countries. They are hired for their extensive network of connections and knowledge of host country laws, regulations, distribution channels and ability to understand the maze of non-tariff barriers that affect the entry of products to their country.

They can assist Virginia based companies in conducting in-country primary market research and help in determining if a product or service is marketable in a given country. They also provide support in the preparation of market visits by setting up appointments. The consultants also coordinate the logistics for trade missions, trade shows and continues follow up meetings with prospective clients once a Virginia based company has completed their market visit and returned home.

## **VALET Program Research Services**

The final component of the VALET Program is the research services made available to VALET participating companies and any exporter in the Commonwealth of Virginia. The benefit to VALET participants is that research is free to them. Research conducted is divided into internal and external research.

Examples of Internal research include:

- Obtaining product Harmonized Tariff Schedule classification number
- Trade flow analysis
- Conducting client due diligence
- Market overview
- Identifying top international markets for specific products
- Competitor analysis

Examples of External research include:

- Identifying potential Partners
- Partner verification and due diligence
- Phytosanitary regulations for food products
- Identification of non-tariff barriers
- Field research
- Identifying distribution channels
- Identifying in-country government procurement trends

Participating companies meet with the program and research managers to identify the research needs that will allow the client to achieve their export objectives. The meeting will determine whether the client's research needs can be met with internal research or if reaching out to the VEDP Global Network of consultants is the best option.

## **Measuring Success in Virginia**

All of the above mentioned components are geared towards meeting the needs of the client. The success of the program is measured by the results of an exit interview conducted with clients upon graduation from the Program. The graduating class must achieve a class average 25% increase in international sales for the 2- year cycle to be considered a success. So far the Program has seen a 54% increase in international sales.

## **Applying the VALET Model to Puerto Rico**

The VALET export promotion model could be implemented in Puerto Rico as part of a strategy that looks to internationalize the local economy and diversify our economy from being too dependent on the local and CONUS markets. The question that needs further analysis is determining if the program should run as a stand-alone program under Puerto Rico's Department of Economic Development and Commerce (DDEC) or if it should be inserted as an additional program under Puerto Rico Trade and Export Company (PR Trade).

The first option may require identifying sources of funds to run the program and staffing of a team with experience in export management, international business research and public administration. Financing for this option would require sufficient funds to run the program for at least 2 to 3 cycles (4 to 6 years). Sources of funds could come from a mix of legislative assignments, capacity building funds from CDBG-DR, competitive federal funds, an assignment from the Government of Puerto Rico or an assignment from the Fiscal Oversight Management Board reconstruction funds. Additional support for this option could come from the team of international trade managers based at PR Trade. Puerto Rico Trade staff could identify the prospective companies and assist in the selection process. However, overall management of the program would be run by this stand-alone entity.

Second option, could be inserting the program under the wing of the Puerto Rico Trade and Export Company. The agency has previous experience in managing export promotion programs and probably still has an in-house team able to manage the initiative; however, recent

information seems to go against this possibility as it looks like PR Trade is only managing a STEP funded program and no other export related efforts seem to be visible. The STEP program is limited in its scope of work and present efforts are limited to identifying activities that are eligible for STEP funding and the management of these funds. An export accelerator program requires management by a team with extensive experience in exports not just managing funds disbursements.

## **Possible Implementation of an Export Accelerator**

### **Staffing Needs**

Staffing of an experience team is a key factor to the success of any export initiative. At a minimum, an accelerator would require one or two Program Managers with extensive experience in export management and a clear understanding of export regulations. Underneath the program manager/s ideally you could have a team of regional international trade managers supporting the day to day dealings of the selected clients and report the needs of the clients to program management team. The trade managers would be distributed geographically around the Island. For purposes of efficiency, the Island could be broken down into a determined number of regions. For example, the international trade manager for the eastern region could cover the municipalities from Carolina in the north to Patillas in the south including the islands of Vieques and Culebra.

Supporting the efforts of the program manager/s and the regional international trade managers is a team of researchers with experience in international business, exporting and business intelligence. The staffing of the research team could start with 2 employees. These employees are key to supporting clients with their research and market intelligence needs.

All members of the proposed program would need to have experience in conducting trade missions, consulting on regulatory export matters and able to conduct group and in-house training.

### **Getting the Program Started: Selection of Participating Companies**

While ideally one would expect the program to bring on board the highest number of participants, I would probably consider starting the accelerator with an initial class of 15 to 20 companies for a one to two year period. Based on the experience from the initial class, one can determine if the staffing needs and logistics of managing 15 to 20 companies from around the island need adjustments. If viable, future classes can then be increased to 25 participants.

The first incoming class could be a selection of the top exporting companies in Puerto Rico. By selecting the top local exporters one increases the possibilities of success and brings positive media coverage to the export accelerator program. Success attracts popularity and increases the possibility of more companies wanting to enter the next incoming classes.

### **Incentives Funds**

The VALET Program offers clients \$30,000 in funding for export related activities during a two year period. For Puerto Rico starting the funding at a \$15,000 - \$20,000 level could be a good start. Initially, the VALET Program started the funding at \$15,000 and then increased the funding to \$30,000. As previously mentioned, the funding sources could come from a variety of places. In the Commonwealth of Virginia, funding came from legislative, central government and competitive federal funds. Due to Puerto Rico's unique situation after Hurricane Maria, funds can come from a number of sources looking to make the Island's economy more robust.

### **Keeping the Program Relevant**

One of the keys to success is making sure the program is relevant to the needs of local exporters. Networking and educational events need to bring topics that offer participants the tools needed to succeed in the international markets. For example, topics such as how to navigate the new North American Trade Agreement or what are the new technologies being used to reach out to a new generation of clients can help participants become more competitive in the global marketplace.

Trade missions need to be more diverse. A possible trade mission instead of being country-specific, could target an industrial sector. As a case in point, rather than conducting a trade mission to the Dominican Republic, a possibility would be organizing a trade mission for Puerto Rican coffee producers to targeted high-income markets in Asia where Puerto Rican coffee is seen as a delicacy.

Hurricane Maria has opened the door for Puerto Rico to rethink how it does business. Local companies cannot continue to be inward looking, they must look to expand to new markets and take advantage of the publicity being created around Puerto Rico's situation. The goodwill seen towards the Island will not last forever.

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