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"Trade with China: A Policy for the 21st Century", Business Coalition on U.S.-China Trade

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April-1997

Trade with China

(select subject from controlled vocabulary, if your office has one)

04/10/1997
Good morning. Today I will make the second in a series of three speeches on our relations with China. Last month I spoke on peace and security. I will continue next month with environmental policy, and today I will address our economic and trade agenda.

I began with peace and security simply because if we don’t have peace, everything else tends to fade into the background. And I concluded that in security relations with China, we are on reasonably firm ground. We are at peace. We have strong alliances in the Pacific. We have the domestic strength to support the world’s best military. And while we face difficult issues, from Korea to the Taiwan Strait, our policies are sound. If we are firm, fair and patient, we can keep the peace for years to come.

As we look toward the 21st century, trade is a bit of a contrast. Here our results are poor and our policies need a lot of work. And that work needs to be done soon -- because if we are able to keep the peace, nothing in our relations with China will mean more to jobs, prosperity and daily life in America than trade. And to explain why, before we dive into the details of tariffs, copyrights and export financing, let me step back and look at the broader context.

GROWING IMPORTANCE OF TRADE

Start with the obvious -- trade is growing fast. When I graduated from high school, imports and exports made up about a fifteenth of the economy. When I came to Congress in 1975, it was about an eighth. Today it is a third -- $835 billion in exports, $949 billion in imports -- and rising each year.

If you live in Montana, you see it every day. We’re selling more beef to Japan than ever before; but also importing more live cattle from Canada. One year a Japanese semiconductor firm comes to Butte, the next a Missoula golf bag maker moves to China. Trade affects more jobs, more farms and more families every day.

And in the next decade these trends will accelerate. Uruguay Round market access and investment agreements will phase in. Big countries shut out of world trade in the Cold War -- Russia, Ukraine, Kazakhstan and Vietnam -- will join the world economy. Developing countries will export and import more each year.
OUR CONFUSED POLICY

And our policy hasn’t kept up. On the positive side, the U.S. Trade Representative has the right strategic agenda and capable staff. The Commerce and Agriculture Departments, and our senior political officials, work hard to promote our products. We are tougher on foreign trade barriers, copyrights and so on than we were during the Cold War. And on imports, our anti-dumping and countervailing duty laws are in good shape.

But we often fail to monitor and enforce the agreements we reach. The American Chamber of Commerce in Japan, for example, found a few months ago that we do not even have a list of our trade agreements with Japan. We use unilateral trade sanctions far too often -- the National Association of Manufacturers counts sixty-one instances since 1993, or more than one a month. We restrict exports more severely than any other country. And we are far behind most of our trade rivals in export promotion and financing.

In sum, our policies are deeply confused, and the result is predictable. We export far less than we should. Our trade deficit hit $120 billion last year. The public is losing faith in trade policy, and with some reason.

So we need to match our negotiating strategy with equally good export promotion. Cut back on unilateral sanctions. Get even tougher on trade barriers. Commit ourselves to bring our trade into balance. And nowhere is the task more urgent than in China.

GREAT EXPECTATIONS ...

Our modem trade relationship with China really dates to 1980, when we signed our commercial agreement and granted MFN status. Since then, our bilateral trade with China has risen at an astonishing pace. It was about $4 billion then; it may top $70 billion this year. American companies invested nearly $12 billion in China in the past three years. Newspapers are full of headlines advertising new deals and new opportunities.

And the future offers a dazzling prospect. Only India matches China as a potential export market. China has a population of 1.2 billion, and is already among the world’s four largest economies. It has a growing middle class -- 300 million Chinese consumers already live in the cities and more come every day. And it is the fastest-growing big economy on earth.

A walk down the street in almost any Chinese city gives you the sense of limitless energy and growth. Every visitor to China comes back talking of the construction cranes dotting the skylines. Shiny new cars running on newly paved streets past newly erected billboards. Cellular phones. Stock exchanges. Farmers strapping color TVs to the back of their new motor scooters.

So we have great expectations. And rightly so. Our exports in everything from telecommunications to computers, environmental technology, autos and agriculture ought to be booming. But when you look at the figures, you find it isn’t so.
POOR RESULTS

China's potential as an export market has always been great. Back in 1776, Adam Smith wrote that China had a market "not much inferior to the market of all the different countries of Europe put together." American business took him very seriously; our first Yankee clipper, optimistically christened Empress of China, landed two years after the British surrender at Yorktown.

The result was our first trade deficit -- we sold a boatload of ginseng and bought a much more valuable cargo of silk, tea and porcelain. From then to World War II, despite all the color and excitement of the China trade, China was a minor market. It took at most 2% of our exports -- the same fraction it takes today. Reality never matched potential.

And the same is true today. Last year, the Commerce Department reported $12 billion in U.S. goods exports to China. With re-exports through Hong Kong, it may be $18 billion. That's up from about $2 billion in 1980. It sounds impressive. But actually it is pretty feeble.

In the short term, exports to China are flat. $11.7 billion in 1995, $12.0 billion in 1996. Thus, according to the Commerce figures, China was our 12th largest export market in 1993. It had fallen to 15th by last year. And if you add Hong Kong, the total is bigger but the trend is actually worse.

And in the long run, despite the headlines, things are no better. Since 1980, as our exports to China grew by $15 billion, our exports to the EU grew by about $70 billion. To Japan by $50 billion. And to the ASEAN countries by about $30 billion. In each case the gap is widening, not closing.

A SOLUTION IN THREE PARTS

So reality is miles behind the "China boom" hype. And at least in terms of exports -- and that's what a Member of Congress has to think about most -- the trends show no signs of improvement. So I conclude that without some big changes, the China market may never reach its potential. And the future could be one of rapidly increasing imports, flat exports, rapidly growing trade disputes, and ultimate disillusion.

But I am not a pessimist or a historical determinist. We can and will do much better. And I see a solution in three parts.

First, fix our own mistakes.

Second, take down Chinese trade barriers and end structural biases against imports through a sound World Trade Organization agreement.

And third, put the whole thing on a stable foundation by making MFN status permanent.
SELF-INFLICTED WOUNDS ...

Let’s start with the self-inflicted wounds. Statistics show that Japanese, European and Asian exports to China are growing much faster than ours. And that’s because some of the broad failings of our trade policy -- weak export promotion, too frequent resort to unilateral sanctions and so forth -- are at their worst in China.

We won’t let our trade promotion agencies -- OPIC, TDA, the Asian Environmental Partnership, sometimes the Ex-Im Bank -- help us sell to China. We restrict technology exports more tightly than anybody else, for example by refusing to sell nuclear power plants when Guangdong Province alone will buy twelve in the next decade. We have an anti-proliferation law that embargoes electronics exports if China sells missiles -- that is, if China misbehaves we sanction ourselves.

This won’t work. We cannot block export promotion; sanction our own companies; vote on cutting off all trade with China each year; and then expect a good trade balance. If we are serious about trade with China, we should eliminate the sanctions. Change our missile sale law so it hits proliferators instead of US exporters. And bring our export controls in line with the rest of the world, or bring them in line with us.

... AND CHINESE POLICIES

But that won’t be enough. Because as bad as our own mistakes may be, structural economic issues and deliberate Chinese trade barriers do much more to cut our exports.

Look at China’s economy today. The economic reforms of the past twenty years abolished Mao’s rural communes, state-assigned careers and ban on private business. They raised tens of millions of people from poverty. We should applaud them; but we should also realize they have not made China a market economy. Instead, as the Chinese say, they created "socialism with Chinese characteristics."

State-owned enterprises -- that is, about 100,000 factories and service providers operated by the government -- make up nearly half the economy and employ two thirds of all urban workers.

Subsidies are so pervasive as to be almost an irrelevant term when government officials, their relatives, and ministries themselves are in business. And prices reflect the real cost of labor and material inputs, as St. Paul puts it, "through a glass darkly."

Neither has reform created a rule of law which would let even half-developed markets work.

The government routinely tells foreign firms in China which inputs they can import, what they must buy from Chinese sources, and to whom they can sell.
Contracts are uncertain; the famous Beijing McDonald’s incident, in which the city tried to evict the restaurant when a Hong Kong company offered a better building lease, is an example.

Import decisions are often as much political as economic, when the government uses contract decisions on everything from grain to aircraft to publicly "punish" American companies for problems in broader US-China relations.

And trade barriers, from familiar tariff, quota and agricultural issues to species as unique to China as the giant panda, are everywhere.

**THE WTO: NO DEAL BETTER THAN A BAD DEAL**

Up to now we have used laws like Section 301 to fight the most flagrant abuses, along with defending our workers from dumping and subsidies through the anti-dumping and countervailing duty statutes. It won some results, especially on copyright piracy. But it is slow and frustrating, and it does little to address the structural issues of a semi-reformed communist economy. If we hope to make trade fair, we need a much better, much more comprehensive, approach to Chinese trade barriers.

And we have it at hand in China’s application to enter the World Trade Organization. The WTO already has rules on virtually all the problems we have in China trade -- everything from tariffs and quotas to subsidies and distribution. And if we get a good agreement, we may see results very quickly.

But we should remember that these talks come with risks. If we sign a bad agreement with lots of loopholes and exemptions, whatever we miss will stay there a long time. If we accept a bad deal, we should never expect much from the China market.

And to digress a bit, the consequences would go beyond China to other reforming communist countries. Russia, with its strong base in primary commodities, heavy industry and aerospace, hopes to enter the WTO next year. Further on are Ukraine, Kazakhstan and other newly independent nations. Then Vietnam, a nation of 80 million and already a foreign investment magnet. China’s WTO accession will define the terms under which nearly a third of the world’s people and industry conduct international trade. So we need to be firm and patient and hold out for a good deal.

**WHAT IS A GOOD DEAL?**

That raises an obvious question. What would a good deal be?

Essentially, since 1980 we have offered China a new Open Door policy on trade. And a good WTO deal would open the door in both directions. In the next century, we would find it just as easy to export and do business in China as Chinese find it here. And if that is to be the outcome, we need four things from China.
First, market access.

Second, fair rules and laws.

Third, safeguards against subsidies and dumping.

Fourth, results and enforcement.

MARKET ACCESS

Let us begin with market access. Today’s tariffs rise to 120% for a Land Cruiser and 80% on a pound of beef. They must go way down. We need to see much less restrictive quotas, particularly on agriculture. Abolition of unscientific barriers to farm products, like the charge that Pacific Northwest wheat is contaminated with a fungus called “TCK smut.” An end to all unpublished quotas and regulations. And abolition of the bizarre rules which make life miserable for importers -- for example, the Health Ministry’s rule requiring safety inspections on all imported musical instruments.

We must open China’s market to services like insurance, banks, law firms, air cargo and passenger flights, entertainment, and civil engineering. These industries make up a third of our exports to the world, but less than a tenth of our exports to China. A fair accession will mean vast new sales for Americans and a higher quality of life for Chinese, who now have to deal with inefficient state monopolies in almost every service sector.

And all this must be done fast. China has argued for special "developing country" treatment which would phase in market access commitments over many years. That would be a mistake. China should be able to call itself whatever it wants, but special treatment is inappropriate for China and -- I believe -- outdated for all but the very poorest countries in any case.

LEGAL REFORMS AND NATIONAL TREATMENT

Second, rules. Ministries and local governments must not be able to extort money or ignore national laws and customs rules. Tariffs, inspections and quotas must be the same in every port and province. Law enforcement must enforce our right to protect copyrights, patents, trademarks and semiconductor designs.

China’s restrictions on national treatment must be abolished completely. The government must abandon policies requiring investors to export all or part of their production rather than selling it to Chinese. There should be no required middlemen or restrictions on trading rights. Anyone who wants to sell grain to China must be able to sell straight to the mill without a government permit. Just as important, but often ignored, Chinese citizens who want to buy must be able to buy without a permit.
And technology transfer requirements must be outlawed. People who invent new manufacturing processes, software or machines must not have to turn them over in order to do business in China.

DUMPING AND SUBSIDIES

Third, subsidies. We need clear and visible separation between ministries, officials and public taxes on one hand, and private business on the other. Exporters must not be pitted against quasi-public, quasi-private companies which get endless revenue from the Chinese public.

Likewise, effective safeguards against export subsidies and dumping. In all the reforming communist countries, price mechanisms are weak and the cost of inputs far below their real value. Our anti-dumping law addresses this with special rules that calculate dumping from non-market economies. This is the right policy given the present state of economic reform in China, and we need to keep it in place.

RESULTS AND ENFORCEMENT

Fourth, results and enforcement. China’s central government has the theoretical and actual power to control all decisions. But China is so big that the central government can only concentrate on a few priorities at one time, giving local and provincial governments almost unchecked authority over everything else.

It is quite conceivable that China’s commitments, even when made in good faith, might not come through in reality because of recalcitrance on the part of ministries, provinces or local governments. So we ought to have some benchmarks to measure success, including objective measures of Chinese imports, and a pre-arranged system of consultation if we see things going wrong. And when problems arise, we must be ready to enforce our rights.

PERMANENT MFN STATUS

Of course, a good WTO accession works in both directions. And that brings me to the third part of a new China trade strategy.

From the founding of the General Agreement on Trade and Tariffs after World War II, to the WTO today, we have accepted one basic commitment with no exceptions. That is MFN tariffs for all members, permanently and without conditions. If China agrees to a commercially acceptable WTO protocol, the Chinese have the right to expect us to fulfill this commitment to them. It was the foundation of Secretary of State Hay’s Open Door Policy in 1900, and it should be the foundation of a New Open Door policy today.

It is good policy on the merits. And if China accepts a fair WTO deal, it is also the fair and honorable thing for us to do.
So I will soon introduce a short, simple bill to make MFN permanent. Passing it will be no easy task. If China will not make an acceptable WTO offer, I doubt the Administration will support it. And, of course, if China is not careful, anything from fundraising scandals to troubles in Hong Kong could stop Congress from passing it regardless of the Administration’s position. But if we get a good WTO deal, I will push this as hard as I can.

CONCLUSION

Let me then sum up.

The next decade, we know, will see a vast expansion of trade. It will touch nearly every American, from Montana farmers to Hollywood actresses, dock workers and chip designers. If our trade policy remains as inconsistent and contradictory as it is today, it may be an unsettling or even frightening epoch of job insecurity and growing resentment of foreigners. But if we get it right, these years can be the most prosperous and exciting in our history.

And there is no better place to start than in China. The world’s largest country. Its fastest-growing major economy. The source of our largest trade deficit. And with all our present difficulty -- with all the realism born of past disappointment -- still the market with the greatest potential on earth.

We need to match our negotiating strategy with a commitment to enforcement and export promotion. We need tough, patient work at the WTO talks. And we need to lay the foundation for it all with permanent MFN status. When we do it, we’ll have something to be proud of.

Thank you all very much, and let’s get to work.