



Business Roundtable

**Reestablishing a Consensus  
on U.S.-China Trade:  
A Principled and Realistic Approach  
for U.S. Policymakers**

September 2006



## Business Roundtable

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## Executive Summary

**Six years after Congress voted by a strong bipartisan margin to grant permanent normal trade relations (PNTR) to China and endorse its entry into the World Trade Organization (WTO), the consensus regarding trade policy with China is fraying.** In its place is a wide range of voices seeking everything from preservation of the status quo, to unilateral tariffs against all Chinese imports, to a revocation of PNTR.

The concerns are understandable – a record bilateral trade deficit, an undervalued Chinese currency, widespread infringement of intellectual property rights (IPR), discriminatory industrial and regulatory policies, and other trade issues augment anxieties about globalization and structural changes in the United States' economy. The desire by some to preserve the status quo is understandable as well – U.S. exports to China are increasing rapidly and China's economy is deeply intertwined with ours.

**There is too much at stake, however, to allow the consensus to fray regarding the U.S.-China economic relationship.** China is our third largest trading partner, our fourth largest export market, a rising regional (and, in some respects, global) power, and, with the U.S., a twin engine of global economic growth. How we manage this economic relationship will have profound implications for the U.S. and world economy.

**Business Roundtable, an association of 160 chief executive officers of leading U.S. companies, urges policymakers to work to repair the frayed consensus regarding U.S.-China trade, based on a balanced accounting of the relationship and maintaining consistency with core U.S. principles.** At the same time, Business Roundtable urges policymakers to use the intense concern regarding China trade, and broader anxieties about globalization, as an opportunity to finally enact and pursue an aggressive competitiveness agenda – to raise America's game and ensure that the U.S. continues to have the world's leading innovation economy.

## ***Recommendations for the U.S. Government***

**Key to reestablishing a consensus on U.S.-China trade is correctly distinguishing between issues of U.S.-China trade and broader policy challenges, and proceeding based on a factual, balanced accounting of our economic relations.** Business Roundtable suggests the following principles – explained more fully in Section V – for policy-makers as a basis for reestablishing a consensus on U.S.-China trade.

- ▶ *Stay true to core U.S. principles of open trade and investment.*
- ▶ *Deal realistically with China’s position.*
- ▶ *Hold China accountable to international trade rules.*
- ▶ *Address concerns regarding intellectual property comprehensively.*
- ▶ *Engage more actively with China on regulatory reform.*
- ▶ *Address the current account imbalance globally, rather than through a “China” lens.*
- ▶ *Ensure U.S. export controls facilitate exports to China without compromising national security.*
- ▶ *Maintain U.S. leadership in Asia.*
- ▶ *Keep the focus on job creation, not preservation of the status quo.*
- ▶ *Raise America’s game through an ambitious competitiveness agenda.*

# I. Introduction

Six years after Congress voted by a strong bipartisan margin to grant PNTR to China, the consensus regarding trade policy with China is fraying. In its place are now more than 20 bills that have already been introduced in the 109th Congress addressing trade with China – seeking everything from unilateral tariffs against all Chinese imports to a revocation of PNTR.

The Congressional and public concerns are understandable. China is no longer just an emerging economy or regional trader, but a major global economic player that poses not only opportunities, but also competitive challenges to the United States. In 1999, when Congress endorsed China's entry into the WTO, the U.S. business community was hopeful and mobilized to support a secure foundation for expanded U.S.-China economic relations. That sentiment has been replaced with a more sober recognition that change in China is uncertain and that as China's commercial footprint gets bigger, the impact of its problems – like rampant infringement of American know-how – becomes magnified. These concerns are coupled with public attention to the growing U.S. current account imbalance, which has reached a record level, and the \$200 billion bilateral imbalance with China.

At the same time, China is one of the key engines of global economic growth and represents a rapidly growing market for U.S. business. Its economy is deeply intertwined with ours.

There is too much at stake to have a frayed consensus regarding this critical economic relationship.

Business Roundtable, an association of 160 chief executive officers of leading U.S. companies, prepared this paper to help policymakers and opinion leaders properly define and navigate the China trade debate. With this paper, Business Roundtable hopes to untangle the issues that are being discussed under the rubric of China trade; place those issues in their proper context; and suggest principles for policymaking that will advance core U.S. interests.

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The paper is organized into five sections. Following this Introduction, Section II argues that policymakers, motivated by genuine concerns and fears, are taking on an overly broad range of issues under the rubric of U.S.-China trade, and that this shape to the debate creates a danger of bad policy outcomes. Section III aims to untangle these issues, analyzing the key challenges and problems in U.S.-China trade, on the one hand, and the broader challenges to the U.S. international economic position on the other. Section IV analyzes what's at stake in the bilateral economic relationship, as policymakers consider how to respond to these challenges. Finally, Section V suggests principles to guide policymakers as they grapple with these issues.

## II. The “China Problem”

Our trade relationship with China has understandably been a topic of active national discussion: China is now the United States' third largest trading partner, the world's second largest economy (in purchasing power parity terms), and the world's fastest growing major economy. China's economic emergence is remaking Asia and the world, with significant implications for the U.S., and has rightly attracted the attention of the Administration and Congress.

However, the evolving shape of the U.S. debate on China trade has created a serious danger of misapprehending the challenge from China. The intense focus on China trade issues has blurred broader policy challenges, and this fuzziness could lead to bad results for the national interest.

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**Regardless of the specific concerns with respect to China trade, the U.S. will continue to face macroeconomic challenges, including large global current account imbalances fueled by savings, investment and consumption patterns and relative economic growth rates.** Moreover, regardless of what trade policies the U.S. pursues with respect to China, the U.S. will continue to confront certain inexorable economic changes:

- ▶ Transition from lower-end manufacturing to capital-intensive, higher-end manufacturing and services;
- ▶ A globally integrated business environment; and
- ▶ An increasingly competitive Asia in which China plays a major role.

At the same time, the U.S. faces key problems in economic and trade relations with China:

- ▶ China maintains an artificial exchange rate that is not market-based;

- ▶ U.S. know-how is widely infringed in China, which has become the center of worldwide counterfeiting and piracy;
- ▶ China’s government intervenes in its economy to support local firms and technologies; and
- ▶ China’s regulatory environment for business is opaque, often arbitrary, and at times discriminatory.

Both sets of issues require high-level attention by the U.S. government. **If policymakers do not distinguish between these issues, we risk prescribing blunt solutions that neither address the broader economic challenges to the U.S. nor the particular challenges of U.S.-China trade.**

Americans have always been innovators and early adopters of new ideas and technology – whether in perfecting and deploying techniques that launched the Industrial Revolution, or inventing semiconductors and launching the information technology revolution. Americans have also always excelled in dynamic environments that demand flexibility and depend on openness and a diversity of ideas. In facing China’s economic emergence as well as broader transitions in the U.S. economy and global business environment, U.S. policymakers should tap into these American characteristics. Confronting these changes as opportunities is the only path that is both realistic and consistent with U.S. principles.

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*“The trade deficit and loss of American manufacturing jobs are very serious problems. It would be nice to think that [the problems] would self-correct if China would only change its ways. Nice, but wrong.”<sup>1</sup>*  
– New York Times

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### III. Challenges in U.S.-China Trade and the U.S. International Economic Position

#### A. Challenges in U.S.-China Trade

There are real challenges in our trade relations with China that warrant U.S. government attention. **U.S. firms and workers benefit from trade with China, but they also face unfair competition and a Chinese government that does not fully embrace its obligations as a leading international economic player.**

##### ***Reluctance to Commit to Further Trade and Investment Liberalization***

China is a major beneficiary of open trade and investment regimes and, as such, is rightly expected to nurture and promote them. While relatively open compared to many other countries' economies, China maintains far more restrictions and barriers to U.S. trade and investment than Chinese goods and services face in the U.S. As the U.S. Trade Representative put it recently, there needs to be some "rebalancing of opportunities" in the U.S.-China trade relationship.

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More generally, **China is not doing enough to advance trade liberalization at the WTO**, in particular the Doha Development Agenda negotiations. China effectively refuses to discuss further liberalization in many sectors, on the ground that it recently acceded to the WTO and should not be obligated to "pay again." China's WTO commitments were never considered an end point, just as is the case with any WTO member. A key role of the WTO is to serve as a forum and facilitator for ongoing trade liberalization, and China's stance is out of step.

China's position is of concern to U.S. businesses not just because improved commitments from China would be commercially meaningful. It is also of concern because when China refuses to step up to the plate, other (particularly developing country) WTO members feel they can do the same. In many countries, fear of China's new global economic might is driving a resurgence of protectionism; it will be challenging to get these countries to offer real improvements in market access if they do not see reciprocal commitments from China. China's attitude is having a quiet, though real, negative effect on WTO negotiations.

### ***Lax Enforcement of Intellectual Property Rights***

U.S. competitiveness depends on knowledge and innovation. U.S. companies, in turn, require adequate protection and enforcement of intellectual property rights to compete. From patented pharmaceuticals, automotive parts, and telecommunications equipment, to brand names and books, software, music and film, U.S. competitiveness demands IPR protection.

**Despite positive efforts and some success in this area, China is failing to adequately protect intellectual property.** Appropriation of intellectual property remains a significant feature of the Chinese economy and causes harm to U.S. businesses in almost every sector in China, the U.S., and many other countries as well. Businesses lose revenue, know-how, and the trust of their customers. The public faces health and safety risks, and governments lose tax revenue, as well as a means to control financing for illegal criminal networks. While making some real efforts, China's government does not have a handle on the IPR problem and has not taken sufficient steps to stem the problem.

### ***Non-Market-Based Currency***

China is the world's fastest growing major economy and third largest trader, yet many economists agree that its currency is undervalued. China's lack of a market-based exchange rate affects its trade and exacerbates, to some degree, global imbalances. China unfortunately is

not alone. Japan and other Asian countries also maintain non-market-based exchange rates; as discussed below, the currency issues are serious and need to be addressed on a broader basis to help ensure that global imbalances are brought into line.

### ***Incomplete Regulatory Reform***

**Extensive government intervention in the economy continues to be a major feature of China's business environment**, even though the Chinese economy is much freer than it was 25 years ago. At times by design, and other times in effect, government overreaching and unsound regulation disadvantage U.S. and other foreign businesses attempting to export to or invest in China.

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- ▶ Licenses and informal approval from officials are necessary for a wide variety of business activities. To a certain extent, China's government has recognized this problem. For instance, China disciplined the licensing process with the Administrative Licensing Law in 2004, and it has provided the legal means for private actors to sue government agencies and officials. However, excessive government interference in the economy is still a serious problem. China ranked 86th in the latest Cato Institute survey of economic freedom.<sup>2</sup>
- ▶ Lack of regulatory transparency makes it difficult for foreign businesses to determine applicable rules or have any certainty about how they will be applied.
- ▶ A closed and non-transparent rule-making process limits the ability of businesses to anticipate new rules or ensure that rules will accord with commercial reality.
- ▶ Provincial and local regulators and officials at times apply regulations so as to favor local firms.

- ▶ In many sectors, regulators have close ties with major state-owned and other enterprises, if not indirect financial interests.
- ▶ State-owned enterprises are subject to policy guidance, which can interfere with commercial decision-making.
- ▶ Corruption continues to be a prevalent characteristic of the Chinese business and regulatory environment, facilitated by the transparency problems noted above.

### ***Industrial Policies***

**While strict state planning is now a far smaller part of the Chinese economy, economic policymakers too often work to pick winners and losers.** This often works to the disadvantage of U.S. firms or technology. For instance, it is still possible for the government to manipulate a standards-setting process to favor domestic technology, or interfere with commercial negotiations to require technology transfer. The incomplete state of regulatory reform, including lack of regulatory transparency, facilitates China's ability to pursue this type of discriminatory policy.

### ***Unexpected Surges of Imports from China***

Changing patterns of trade and economic activity are natural, but new patterns can lead to unexpected surges in imports, which can cause real, concentrated pain to U.S. businesses and workers. **Such import surges warrant attention not only because of the economic pain they cause, but also because such pain can undermine broader public support for open trade and investment.** This is not an issue specific to trade with China – but given its rapid economic emergence, China is the most likely source of import surges in the U.S. today. Whether to provide relief for dislocations caused by such rapid trade pattern changes therefore has important implications for U.S.-China trade.

## ***B. Broader Challenges for the United States***

**The U.S. also faces a broader set of challenges in the international economic arena that are often confused with China trade concerns. These challenges must be addressed on their own terms** and with an understanding that the fundamental answers do not lie in U.S. trade policy toward China.

- ▶ *U.S. Trade Imbalance:* The U.S. global current account imbalance has been rising steadily from roughly \$100 billion in 1990 to nearly \$800 billion today, representing a historically unprecedented 6.4 percent of U.S. GDP. Such an imbalance is dangerous and requires the U.S. to depend heavily on foreign borrowing.

**U.S.-China trade contributes to the imbalance, but it is not the fundamental cause.**

- The increase in U.S. imports from China over the past several years has largely taken market share from other Asian countries rather than U.S. producers.<sup>3</sup>
- The share of the trade deficit represented by Asia Pacific (including China) has been falling – in 1999, it was 57 percent, and in 2005, it was 43 percent.<sup>4</sup>

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- While the U.S. goods trade deficit with China has been increasing, the U.S. trade deficit with the entire world has been increasing at an even faster rate.

There is wide agreement among economists that current account imbalances are not driven by trade policy – but instead by factors such as relative savings, investment, and consumption patterns and relative growth rates.<sup>5</sup> Exchange rates play an important role, and in this regard China’s exchange rate is rightly a subject of U.S. government priority attention. However, it is global exchange rates – and not just the renminbi-dollar rate – that are significant; China’s adoption of a market-based exchange rate by itself would be unlikely to significantly change the U.S. current account imbalance.<sup>6</sup> The trade imbalance is a broad problem that needs to be addressed comprehensively by U.S. domestic policy as well as in cooperation with other major economies.

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- ▶ **Structural Changes in the U.S. Economy:** The U.S. economy has been undergoing a shift from lower-end manufacturing to capital-intensive, higher-end manufacturing and services that will continue, regardless of trade policy with China. Manufacturing’s share of U.S. employment has been declining steadily since 1979 (from nearly 21 percent to 10.4 percent in 2004).<sup>7</sup> Most of this change is explained by automation, as U.S. manufacturing output has actually been increasing rapidly at the same time as employment has been dropping. Since 1970, U.S. manufacturing employment has fallen approximately 20 percent, while manufacturing production has more than doubled.<sup>8</sup>

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That being said, manufacturing still plays an important role in the U.S. economy, and U.S. economic policy should support innovation in this sector. Trade policy can play a role: the U.S. needs to continue to open foreign markets to U.S. manufactured goods and fight unfair trade practices, including in China. But **the structural changes in the U.S. economy cannot be undone through China trade policy.**

- ▶ *Globally Integrated Business Environment:* Technological advances in communications and transportation have revolutionized business. Goods and services contain inputs – parts, software, intellectual property – that now come from all over the world, such that many goods and services are truly international in origin. This new environment means a more significant role for trade: exports account for almost 30 percent of global GDP, and cross-border investment flows range from \$500 billion to \$1.5 trillion annually. The global business environment puts a premium on innovation, technological know-how, collaboration, and flexibility – skills that have always been American hallmarks (and with the proper national focus on education and research and development, can continue to be).

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**China, as a major emerging economy and trader, plays an important role in this new globally integrated business environment. Regardless of our trade policy with China, however, U.S. businesses will have to compete in this environment.**

- ▶ *Increasingly Competitive Asia:* Asia now accounts for one-third of the world's economy and is the world's most economically dynamic region. As the Cold War lines that divided Asia have disappeared, and as China has abandoned economic isolationism, a new Asia has emerged, combining the wealth and technology of Asia's early industrializers with the low costs and vast manpower of China.<sup>9</sup> China is facilitating this economic integration by pursuing an active regional trade agenda. It is negotiating or considering more than two dozen free trade agreements, including ongoing negotiations with the ASEAN countries, Australia, and New Zealand.

While this new Chinese engagement and regional integration pose competitive challenges to the U.S., they can also serve to promote broader trade and investment liberalization and reform and are reconcilable with U.S. interests. This contrasts with China's regional policy of an earlier era, which aimed to draw lines between China and the U.S. and much of Asia, and promote third world solidarity and socialism. China has come a long way from this "Bandung" diplomacy.

In all events, **this new Asian economic integration is not something that the U.S. can undo even if that were desirable.** The U.S. should be aggressively looking for opportunities created by Asian integration and at the same time ensure that the U.S. is not marginalized in the region. This new Asian competitiveness also makes it all the more important that the U.S. pursue a broad and ambitious competitiveness agenda at home.

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## IV. What's At Stake

**In evaluating our economic relations with China and devising strategies, policymakers need to look at both sides of the ledger.**

The United States needs to address the challenges squarely and honestly, with an appreciation of the positives and negatives in the economic relationship. Without a balanced evaluation and understanding of what's at stake, the U.S. risks adopting policy responses that cause more harm than good.

### ***China's General Openness to Trade and Investment***

When trade with China is debated in the U.S., it often begins from a mistaken premise: that China maintains a closed, mercantilist economy while exploiting open U.S. and international markets. This is a caricature – although there are some important exceptions that require U.S. government attention, China has generally embraced open trade and investment as critical to its economic development.

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- ▶ Based on the most common economic measure of openness (the ratio of imports to GDP), China exceeds other major economies: China's imports of goods are roughly one-third of GDP, compared to 10 percent for Japan, 12 percent for India, and 14 percent for the U.S.<sup>10</sup>
- ▶ China has a relatively open investment regime; China was the world's third largest destination for foreign direct investment in 2005, and approximately 30 percent of its goods output is manufactured by foreign-invested enterprises.<sup>11</sup>
- ▶ China's export growth has been astounding, but so has its import growth: in 2004, China's exports grew 35 percent, while imports grew 36 percent.<sup>12</sup>

- ▶ Since 2000, China has been the largest contributor to world (non-fuel) import growth,<sup>13</sup> and is the world's third largest importer of manufactured goods.<sup>14</sup>
- ▶ China's effective tariff protection for domestic firms is among the lowest of any developing country.<sup>15</sup>

This does not mean that, from a qualitative point of view, China's economy is as open as it should be – it is not, and China's policy of economic openness still requires further deepening and firmer legal grounding. Painting China as a closed-market mercantilist, however, does not reflect reality.

### ***Globally Integrated Business Operations Support High-Quality U.S. Jobs***

Around the world, firms have capitalized on open trade and investment policies to build globally integrated supply chains. This operational structure supports many high-wage, skilled jobs in the U.S., where products are imagined, designed, engineered, manufactured (to some degree), and marketed, while efficient global manufacturing helps firms tap further market opening abroad and foreign growth in a cost-competitive manner. At the same time, foreign businesses invest in the U.S., employing over 5 million Americans from new investments of \$80 billion in 2004.<sup>16</sup>

China has become an attractive point for final assembly within this globally integrated system, which explains why, while China's exports to the world have been increasing rapidly, so have its imports. The "Made in China" description on a final product masks a more complicated story: the vast majority of Chinese exports to the U.S. (roughly 70 percent) contain inputs from the U.S. or other countries.<sup>17</sup> For the processing sector as a whole, the value added in China is only one-third of the value of the output; the other two-thirds is the value of imported parts and components.<sup>18</sup>

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### ***Imports Lower Costs to U.S. Consumers and Producers***

Imports, including from China, have tended to keep prices down, allowing U.S. consumers to stretch their dollars further and, in effect, increasing Americans' purchasing power. Lower inflation gives policymakers less reason to raise interest rates dramatically, and the ensuing low rates provide a tangible benefit for consumers, homebuyers, and businesses seeking to finance growth and job creation.

China's exports are concentrated in goods relied on by working-class Americans. **Nearly 80 percent of imports from China are consumer goods**, and one-quarter of U.S. consumer good imports come from China.<sup>19</sup> Imports from China account for more than 80 percent by value of the U.S. toy market, half of the footwear market, and nearly half of the television and consumer electronics market.<sup>20</sup> In these cases, the primary alternative to Chinese imports is more expensive imports from other countries and not U.S. production.

Quantifying the aggregate price effects of imports from China is complicated, but economic studies have found a significant impact. Over the past four years, increased U.S. trade with China is estimated to have pushed U.S. prices down by 0.5 percent, and by 2010, that effect is estimated to reach 0.8 percent. These price reductions from U.S.-China trade are estimated to effectively increase U.S. household

real disposable income by approximately \$1,000 each year.<sup>21</sup> Total imports from China – as opposed to just recent increases – have had a larger effect, with U.S. price levels estimated to be 1.4 percent lower due to total imports from China.<sup>22</sup>

Americans instinctively recognize the benefits that open trade brings in terms of choice and lower prices. Seventy-five percent of Americans polled agreed that for families who watch what they spend, trade with China has made many products affordable that would otherwise be out of reach.<sup>23</sup>

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Just as Chinese imports keep costs down for U.S. consumers, they also benefit downstream U.S. producers. A U.S. company may rely on Chinese inputs that allow the company to focus on areas of core competence and remain internationally competitive.

### **China's Market Helps Drive U.S. Export Growth**

In the past decade, China has gone from being the subject of U.S. corporate day-dreaming to a serious opportunity, as long-held hopes of a one-billion-person market and a Chinese middle class are gradually turning into reality. **Since China joined the WTO in 2001, China has been our fastest growing major export market, albeit from low levels.**

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*“China’s economic development and market liberalization have been major contributors to the growth in U.S. exports.”<sup>24</sup>*

*– Government Accountability Office*

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- ▶ U.S. exports to China topped \$40 billion in 2005, with growing demand for U.S. capital equipment, high-tech products, agricultural commodities, and sophisticated services;
- ▶ Since 2001, U.S. exports to China have grown five times faster than to the rest of the world, and China has gone from being our ninth to our fourth biggest export market;
- ▶ There are now over 400 million Chinese cell phone users (nearly double the U.S. market) and China is adding 5 million new subscribers each month, as an urban middle class is emerging and even rural peasants are beginning to exercise market demand;

- ▶ One-third of U.S. soybean and cotton exports (\$2.3 billion and \$1.4 billion, respectively) went to China in 2005;<sup>25</sup>
- ▶ China is predicted to be the largest market for commercial aircraft outside of the U.S. for the next 20 years; and
- ▶ U.S. services exports to China have more than doubled since 1995, making China our seventh largest services market.

These expanding exports support good U.S. jobs. The average wage of export-supported jobs is estimated to be 13 to 18 percent higher than the average wage for the overall economy.

## V. Principles for U.S. Policymakers

As described above, there are serious challenges that the United States faces in its trade relations with China, as well as broader international economic challenges, and mixing those two distinct sets of challenges threatens the U.S. ability to tackle either successfully. Taking these challenges into consideration, together with ways in which current U.S.-China economic relations (even with their serious flaws) serve U.S. interests, this section sets forth key principles that should guide U.S. policymakers as they consider China trade issues.

▶ ***Stay true to core U.S. principles of open trade and investment.***

- Open trade and investment have been key drivers of U.S. growth and prosperity since World War II. Now is not the time to lose confidence in our ability to compete.
  - Since 1948, industrial countries' average tariff rates have dropped from 40 percent to 4 percent; during that period, world exports increased from \$58 billion to \$9 trillion, and U.S. real GDP per capita grew from \$12,000 to \$38,000.
  - Americans do not support economic isolationism: 79 percent polled agree that strong international trade helps grow the U.S. economy.<sup>26</sup>
- If imports from China were restricted across-the-board, they would primarily be replaced with other (higher-priced) imports rather than U.S. production. A 27.5 percent additional tariff on imports from China would cost nearly 300,000 net U.S. jobs.<sup>27</sup>

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*Americans do not support economic isolationism: 79 percent polled agree that strong international trade helps grow the U.S. economy.*

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▶ **Deal realistically with China's position.**

- China's economic emergence is here to stay – and cannot be legislated away. Let us deal realistically with China, and not on the basis of wishful thinking.

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*China's economic emergence is here to stay – and cannot be legislated away. Let us deal realistically with China, and not on the basis of wishful thinking.*

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- Policymakers should not fear or deny China's new heft – we need to acknowledge it, and

use it to encourage China to assume commensurate responsibilities in the international economic system. U.S. officials have articulated this theme well – the challenge now is to build on the rhetoric.

– This means pursuing deeper participation by China in WTO negotiations.

– This also means expanding China's role in the international economic architecture. Most notably, China, as the world's second-largest economy, should be a part of the G-8. China also should have greater responsibilities, and thus a larger role, in the International Monetary Fund (IMF). These steps would facilitate closer coordination of economic policy between China and the world's other major economies. If properly managed, G-8 membership and an expanded role at the IMF could help transform what are now "demands" on China – less likely to be met – to shared leadership responsibilities.

▶ **Hold China accountable to international trade rules.**

- USTR pledged a new phase of accountability and enforcement in its February 2006 “top-to-bottom” review of China trade policy; this is the right track. The U.S. should not hesitate to assert its rights at the WTO when China appears to be running afoul of international commitments in a way that is hurting U.S. economic interests.

▶ **Address IPR concerns comprehensively.**

- Policymakers need to hold China to its commitments on IPR, while also engaging in concrete cooperation and providing assistance where appropriate. Rampant IPR infringement in China is in part a problem of Chinese political will, but it is also a capacity issue and a cross-border issue that cannot be addressed in China alone.
- Many infringing goods are produced in China, but the infringing activities in China are often part of cross-border criminal activity: customers in other countries contract for the production of fake products, and international networks join forces with producers in China to distribute fakes around the world. China is the center of the activity, but this is not just a China problem.
  - An international problem requires international solutions to complement the stepped-up domestic actions that China needs to take. For instance, law enforcement authorities in China, the U.S., and other countries need to coordinate efforts and work together to effectively address problems.

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*Policymakers need to hold China to its commitments on IPR, while also engaging in concrete cooperation and providing assistance where appropriate.*

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- The U.S. should step up efforts to keep fakes out of this country. For instance, Congress and the Administration should increase resources at the U.S. border aimed at identifying and interdicting imports of infringing goods.

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*The U.S. should step up efforts to keep fakes out of this country.*

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► **Engage more actively with China on regulatory reform.**

- As China removes tariff and non-tariff barriers in accordance with its WTO commitments, it will be increasingly important for the U.S. to address regulatory barriers to trade and investment in China.
- The U.S. needs focused, high-level attention to help accelerate regulatory reform and ensure that China adopts regimes in line with U.S. or international approaches. As a complement to the U.S.-China Joint Commission on Commerce and Trade, the U.S. and China should launch a focused regulatory reform effort led at the Presidential level, along the lines of the U.S.-Japan Regulatory Reform and Competition Policy Initiative.

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*The U.S. and China should launch a focused regulatory reform effort led at the Presidential level.*

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- Business Roundtable appreciates that USTR identified increased focus on regulatory reform as a key action item flowing from the “top-to-bottom” review of China trade policy, and that some work is underway (e.g., financial regulators dialogue).<sup>28</sup> But more needs to be done – the European Union, for instance, has more actively engaged in regulatory exchanges and technical assistance and is promoting European regulatory models.

▶ **Address the current account imbalance globally, rather than through a “China” lens.**

- Policymakers need to address the low savings and investment levels in the U.S., with an intensified commitment to reducing the federal budget deficit.
- The Administration should continue to seek an adjustment to China’s exchange rate, but also should address exchange rates with Japan and other major Asian trading partners – to ensure that the values of the world’s major currencies reflect market forces. The issue should be addressed broadly rather than primarily under a U.S.-China rubric, utilizing, as appropriate, the IMF and other fora.
  - Four years ago, Business Roundtable urged the President to pursue a “sound dollar” initiative to protect U.S. competitiveness and reduce the U.S. current account imbalance.<sup>29</sup> Business Roundtable appreciates the steps that have been taken, but more action is needed.
  - A recent positive development is the April 22, 2006 decision of the IMF Board of Governors empowering the IMF to address global current account imbalances in a comprehensive manner. The multilateral consultations to be conducted by the IMF will need strong, high-level support in Washington and other major capitals to be successful.

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▶ ***Ensure U.S. export controls facilitate exports to China without compromising national security.***

- A key U.S. trade policy objective is to ensure full access to China's market and promote exports. The U.S. should not undercut that objective by imposing export controls unnecessary to, or ineffective in, protecting U.S. national security.
- The Administration has been considering an open-ended "catch-all" regulation to expand dual-use controls on exports to China and 18 other countries. Expansion of existing export controls should be undertaken very carefully. Imposing controls on exports of technology already available in the marketplace, or that other countries are selling to China, undermines U.S. commercial interests without advancing national security.
- Business Roundtable urges that export controls be reviewed to ensure that they:
  - Effectively advance national security interests;
  - Are transparent and predictable;
  - Are frequently reviewed to ensure ongoing effectiveness and need, in the light of technological developments and availability from alternative sources; and
  - Are administered efficiently and with private sector input.

Business Roundtable has set forth specific proposals for reform to ensure that these principles are met.<sup>30</sup>

▶ ***Maintain U.S. leadership in Asia.***

- China's emergence requires a proactive U.S. foreign economic policy, so that the U.S. is not left behind in Asia. China will continue to play a central role in Asia, but the U.S. should not cede its leadership position. This has implications for U.S. trade, economic, and security policy.

- On the trade policy front, USTR's initiation of free trade agreement (FTA) negotiations with Korea and Malaysia are good starts, but this needs to be followed by a sustained and ambitious focus on the region. The U.S. should deepen partnerships with other Asian economies to advance U.S. strategic and economic objectives.

- The U.S. should pursue FTAs and other initiatives in Asia as part of a geopolitical strategy to retain American competitiveness and influence, in concert with continued positive engagement with China and other Asian economies. The Administration and Congress should keep this strategic context in mind as it shapes and considers these agreements and initiatives.

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*The U.S. should pursue FTAs and other initiatives in Asia as part of a geopolitical strategy to retain American competitiveness and influence, in concert with continued positive engagement with China and other Asian economies.*

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- The U.S. should work to reinvigorate the Asia-Pacific Economic Cooperation (APEC) organization into a vehicle to advance trade and investment liberalization. In the 1994 Bogor Declaration, the leaders of APEC declared their intention to establish free trade and investment in the region by the year 2010 for industrialized members and 2020 for the others. Little progress has been made toward these goals.

- As one interim step toward APEC's longer term goal, the U.S. should integrate its existing FTAs in the region – for instance, by providing for “cumulation” of inputs among regional FTA partners in determining what goods receive the benefits of FTA treatment.

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*As one interim step toward APEC's longer term goal, the U.S. should integrate its existing FTAs in the region.*

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- The President's March trip to India and the initiation of the U.S.-India Trade Policy Forum are positive steps that need to be followed up by increased economic engagement with India.

▶ ***Keep the focus on job creation, not preservation of the status quo.***

- Successful U.S. economic policy has always been about job creation and growth, not about freezing the U.S. economy at any one stage. Open economic policy means a natural process of job loss accompanied by job creation.
- Government policy should aim to facilitate these ongoing structural transitions and ease the accompanying short-term pain.
  - Whether job losses occur principally because of technological change (which is the fact) or trade, the Administration and Congress should provide for robust assistance to affected firms and workers to help them adjust, obtain new skills, and reenter the workforce at high-paying employment. More needs to be done on this front.
  - Where market disruption due to unexpected surges of imports from China (or elsewhere) has been established, the government should be responsive to injured U.S. businesses and workers. In some cases, this may mean short-term WTO-consistent import limits that permit U.S. firms to adjust to the new competition. In any case, this should mean assistance to those firms and workers to help them retool or retrain.

▶ ***Raise America's game through an ambitious competitiveness agenda.***

- The U.S. has an innovation economy, but it is at serious risk.
  - Nearly half of technology patent applications are filed by foreign competitors.<sup>31</sup>
  - About one-third of all jobs in the U.S. require science or technology competency, but currently only 17 percent of Americans graduate with science or technology majors.<sup>32</sup>

– As a percentage of our GDP, U.S. federal research and development spending peaked *40 years ago* – in 1965, at just under two percent of GDP. Today it is about 0.8 percent of GDP.<sup>33</sup>

- There is a growing recognition that we are falling behind, but there has yet to be sufficient, concerted, high-level attention aimed at comprehensively addressing the problem.
- Policymakers need to enact and pursue a broad competitiveness agenda. In March 2004, Business Roundtable issued a report calling for policies to spur U.S. growth, including facilitating research and development, encouraging new investment in manufacturing technology, improving worker adjustment and education programs, and raising U.S. student achievement.
  - Various legislative proposals have been tabled, and in February 2006, the President launched the American Competitiveness Initiative. These are welcome steps, but they will require sustained, high-level attention by the Administration and Congress to come to fruition.
- The U.S. also needs to remove burdens that hinder international competitiveness of U.S. firms, like high health care costs. Per capita spending on health care in America is nearly two-and-a-half times the average in the industrialized world, and employers in America bear much of the cost of the rising number of uninsured Americans through cost-shifting.<sup>34</sup>

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*There is a growing recognition that we are falling behind, but there has yet to be sufficient, concerted, high-level attention aimed at comprehensively addressing the problem.*

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- The cost of a typical car produced by a U.S. auto company includes more than \$1,500 to fund health care costs for current and retired employees. For a leading Japanese car company with manufacturing facilities in North America, the comparable figure is approximately \$201, and \$97 when the car is built in Japan.<sup>35</sup>
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## VI. Conclusion

Key objectives for bringing China into the WTO were to “normalize” and “multilateralize” U.S. economic relations with China, and to help institutionalize and bind China’s domestic economic reform and opening program. In particular, with WTO accession, the United States aimed:

- ▶ To integrate China into an international system of trade liberalization, and thereby give China a vested interest to protect and expand that system;
- ▶ To ensure that China could not selectively open its market while benefiting from open markets abroad;
- ▶ To bring China into a rules-based system, dependent on the development of a rule of law, in which China could be held accountable by its major trading partners;
- ▶ To increase transparency in China’s economy and trade regime; and
- ▶ To help ground U.S.-China economic relations on a more secure, long-term foundation, and thereby help transform bilateral relations from the emotional to the mature.

This strategy culminated in the conclusion of China’s WTO negotiations and Congress’ broad bipartisan endorsement of PNTR for China. These aims were long-term and, not unexpectedly, have only been partially realized.

**As we seek solutions to the problems in U.S.-China trade, Business Roundtable urges policymakers to do so in the spirit of – and with the aim of promoting – the bipartisan objectives that underlay the PNTR consensus.**

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- <sup>1</sup> *New York Times*, April 21, 2005, p. A22.
  - <sup>2</sup> Cato Institute, *Economic Freedom of the World: 2005 Annual Report*, p. 3.
  - <sup>3</sup> Congressional Research Service, "China-U.S. Trade Issues", July 1, 2005, p. 4. See also CSIS and IIE, *China: The Balance Sheet* (2006), p. 116 ("The large and growing U.S. deficit in its trade with China largely reflects the relocation of labor-intensive assembly activities to China from elsewhere in Asia, rather than a Chinese policy of restricting access to its domestic market.").
  - <sup>4</sup> USTR, "Top-to-Bottom Review: U.S.-China Trade Relations", Feb. 2006, p. 4 (hereinafter "Top-to-Bottom Review").
  - <sup>5</sup> See, e.g., Menzie D. Chinn, "Getting Serious about the Twin Deficits", Council on Foreign Relations, Sept. 2005 (hereinafter "CFR"); Keith Bradsher, "As Trade Deficit Grows, So Do Tensions With China", *New York Times*, March 10, 2006.
  - <sup>6</sup> For instance, Oxford Economics estimates that a 25 percent revaluation of the renminbi would reduce the U.S.-China bilateral deficit by roughly \$20 billion and the U.S. global current account deficit by \$10-\$15 billion. Oxford Economics, pp. 8-9. See also CFR, p. 3.
  - <sup>7</sup> Oxford Economics, pp. 19, 21.
  - <sup>8</sup> Forbes Testimony, p. 10.
  - <sup>9</sup> Barshefsky and Gresser, "Revolutionary China, Complacent America", *Wall Street Journal*, Sept. 15, 2005, p. A20.
  - <sup>10</sup> Forbes Testimony, p. 5; Nicholas Lardy, "Trade Liberalization and Its Role in Chinese Economic Growth", Nov. 2003, p. 10 (India and U.S. stats). This figure may be somewhat overstated, as estimates of China's GDP have recently been adjusted upward.
  - <sup>11</sup> UNCTAD *2005 World Economic Report*, CSIS and IIE, *China: The Balance Sheet* (2006), p. 21.
  - <sup>12</sup> AmCham White Paper, p.14.
  - <sup>13</sup> Oxford Economics, p. 4.
  - <sup>14</sup> Forbes Testimony, p. 5.
  - <sup>15</sup> CSIS and IIE, *China: The Balance Sheet* (2006), p. 84.
  - <sup>16</sup> Department of State Fact Sheet, "How Foreign Direct Investment Benefits the United States", March 13, 2006; BEA Survey of Current Business Report, June 2005.
  - <sup>17</sup> AmCham White Paper, p. 24; Congressional Research Service, "China's Trade with the United States and the World", Sept. 13, 2005, p. 10.
  - <sup>18</sup> CSIS and IIE, *China: The Balance Sheet* (2006), p. 106.
  - <sup>19</sup> National Retail Federation, "Impact of Imports from China on U.S. Employment", Nov. 2005, pp. 2, 4 (including computers) (hereinafter "NRF").
  - <sup>20</sup> NRF, p. 5.
  - <sup>21</sup> Oxford Economics, pp. 16, 1.
  - <sup>22</sup> NRF, p. 10.
  - <sup>23</sup> Business Roundtable polling.
  - <sup>24</sup> government Accountability Office, *China Trade: U.S. Exports, Investment, Affiliate Sales Rising, but Export Share Falling*, Dec. 2005, p. 7 (hereinafter "GAO").
  - <sup>25</sup> Top-to-Bottom Review, p 10; GAO, p. 8.
  - <sup>26</sup> Business Roundtable polling.
  - <sup>27</sup> NRF, p. 14.
  - <sup>28</sup> Top-to-Bottom Review, p. 26.
  - <sup>29</sup> See Business Roundtable letter to the President, Feb. 13, 2002.
  - <sup>30</sup> <http://www.businessroundtable.org/pdf/501.pdf> (Feb. 2001 paper).
  - <sup>31</sup> U.S. Patent and Trademark Office, "Patenting in Technology Classes, Breakout by Geographic Origin, 2000-2004".
  - <sup>32</sup> Testimony of William R. Brody, "U.S. Competitiveness: The Innovation Challenge", House Committee on Science, July 21, 2005, p. 4.
  - <sup>33</sup> Brody Testimony, p. 4.
  - <sup>34</sup> Baucus Competitiveness Report, Dec. 2005, p. 18.
  - <sup>35</sup> Paul Krugman, "Bad for the Country", *New York Times*, Nov. 25, 2005 (citing A.T. Kearney study).







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