UNITED STATES DEPARTMENT OF COMMERCE
International Trade Administration
Washington. D.C. 20230

Revised June 14, 1999

PATRICK A. MULLOY
ASSISTANT SECRETARY
FOR MARKET ACCESS AND COMPLIANCE
INTERNATIONAL TRADE ADMINISTRATION
U.S. DEPARTMENT OF COMMERCE

Patrick A. Mulloy serves as the Assistant Secretary of Commerce for Market Access and Compliance in the Department of Commerce's International Trade Administration. Nominated by President Clinton and confirmed by the United States Senate, Mr. Mulloy was sworn into office in June 1998.

Assistant Secretary Mulloy directs a staff of some 170 international trade specialists dedicated to improving market access by U.S. companies to international markets by removing foreign barriers to U.S. exports and ensuring foreigu countries comply with trade agreements they have negotiated with the United States. Mr. Mulloy also advises both the Under Secretary of Commerce for International Tmde and the Secretary of Commerce on ways to strengthen the international tmde and investment poaition of the United States, On May 19, 1999, President Clinton named Assistant Secretary Mulloy a member of the Commission on Security and Cooperation in Europe.

Prior to his employment as Assistant Secretary, Mr. Mulloy served fifteen years in various seaior positions with the staff of the U.S. Senate Banking Committee including General Counsel and most recently Chief Democratic International Counsel. In those positions, he contributed to much of tbe international trade and finance legislation formulated by the Committee including the Export Enhancement Act of 1992 which created the Trade Promotion Coordinating Committee (TPCC) and titles of the Omnibus Trade and Competitiveness Act of 1988 dealing with foreign bribery, exchange rates and export controls. Before coming to the Senate, Mr. Mulloy nerved as an attorney with the Antitrust Division of the Depertmcnt of Justice and was a Foreign Service Officer witb the Department of State.

Mr. Mulloy, a native of Kingston, Pennsylvania, has a L.L.M from Harvard University Law School, a J.D. from George Washington University Law School, an M.A. from the University of Notre Dame, and a B.A. from King's College.

He resides in Alexandria, Virginia with his wife Marjorie and their three children.

ORAL REMARKS OF
THE HONORABLE PATRICK A. MULLOY
ASSISTANT SECRETARY OF COMMERCE FOR MARKET ACCESS AND COMPLIANCE

BEFORE THE
SUBCOMMITTEE ON INTERNATIONAL ECONOMIC POLICY AND TRADE
OF THE HOUSE COMMITTEE ON INTERNATIONAL RELATIONS

JULY 22, 1999

MADAM CHAIR, I AM PLEASED TO APPEAR BEFORE THIS SUBCOMMITTEE TODAY TO DISCUSS THE LARGE AND GROWING U.S. TRADE DEFICIT. I HAVE A PREPARED STATEMENT FOR THE RECORD AND SOME INTRODUCTORY REMARKS I WOULD LIKE TO MAKE AT THIS TIME.

LET ME BEGIN MY REMARKS BY SALUTING YOU FOR YOUR EFFORTS TO DRAW ATTENTION TO THIS IMPORTANT MATTER. YOU HAD A SIMILAR HEARING LAST JULY AND IN OCTOBER THE CONGRESS, RECOGNIZING THE KEY IMPORTANCE OF THIS ISSUE, ESTABLISHED THE TRADE DEFICIT REVIEW COMMISSION. THAT COMMISSION, COMPRISED OF SOME OF THE BEST TRADE AND ECONOMIC EXPERTS IN THE COUNTRY, WILL BEGIN ITS PUBLIC WORK ON AUGUST 19.

THIS WEEK, THE COMMERCE DEPARTMENT RELEASED DATA SHOWING THAT FOR THE FIRST FIVE MONTHS OF THIS YEAR THE DEFICIT IN GOODS AND SERVICES IS RUNNING AT AN ANNUAL RATE OF $225 BILLION -- UP 50 PERCENT OVER THE FIRST FIVE MONTHS OF LAST YEAR. THE MERCHANDISE DEFICIT SO FAR THIS YEAR IS AN ANNUAL RATE OF $307 BILLION.

IN UNDERSTANDING THESE HUGE FIGURES, THE MOST IMPORTANT POINT IS THAT THE RECENT GROWTH IN THE DEFICIT STEMS IN PART FROM THE FACT THE U.S. ECONOMY IS GROWING RAPIDLY -- AND OTHERS AREN'T.

THE SECOND IMPORTANT POINT TO NOTE IS THAT THE RECENT DEFICIT INCREASE STEMS PRINCIPALLY FROM THE EXPORT SIDE.

OVERALL IMPORTS SO FAR THIS YEAR ARE UP ONLY 6 PERCENT -- A VERY MODEST RATE. MOREOVER, IMPORT PENETRATION -- IMPORTS AS A PERCENT OF GDP -- HAVE NOT INCREASED SINCE 1997.

THIS IS NOT TO SAY THAT THERE HAVE NOT BEEN SOME SIGNIFICANT INCREASES IN INDIVIDUAL SECTORS -- SUCH AS STEEL, WHERE THE ADMINISTRATION HAS ACTED TO HALT THE FLOOD OF IMPORTS. BUT OVERALL, IMPORTS HAVE NOT RISEN RAPIDLY.

THE REAL DIFFICULTY IS IN EXPORTS. TYPICALLY OUR EXPORTS GROW ABOUT SEVEN PERCENT A YEAR. BUT THEY FELL 1 PERCENT LAST YEAR AND SO FAR THIS YEAR HAVE FALLEN A FURTHER 2.4 PERCENT. THIS DECLINE IS SERIOUS. IT IS AFFECTING JOBS IN AMERICA'S FARMS AND FACTORIES.

THE EXPORT DECLINE DOES NOT REFLECT A DROP IN U.S. COMPETITIVENESS. IN FACT, THE U.S. SHARE OF EXPORTS TO FOREIGN MARKETS LAST YEAR WAS 15.2 PERCENT -- UP SIGNIFICANTLY FROM THE 14 PERCENT AVERAGE IN RECENT YEARS.

WHAT IT REFLECTS IS HOW SLOW FOREIGN MARKETS ARE GROWING. NOT JUST IN ASIA, BUT IN EUROPE AS WELL, DOMESTIC GROWTH IS SLUGGISH, AND DEMAND FOR IMPORTS, INCLUDING FROM THE UNITED STATES, IS STAGNATING.

THE MOST DRAMATIC DROP IN EXPORTS TOOK PLACE IN ASIA WHERE 1998 EXPORTS FELL BY 15 PERCENT AND SO FAR IN 1999 THEY HAVE FALLEN A FURTHER 2 PERCENT.

ON A BILATERAL BASIS, THE LARGEST DEFICIT IS WITH JAPAN, WHERE OVER THE LAST 12 MONTHS IT HAS REACHED $66 BILLION.

OUR SECOND LARGEST BILATERAL DEFICIT -- $57 BILLION LAST YEAR -- IS WITH CHINA. WE IMPORT FIVE TIMES FROM CHINA WHAT WE EXPORT TO CHINA -- MEANING THAT JUST TO KEEP THE DEFICIT FROM GROWING ANY MORE, OUR EXPORT GROWTH RATE HAS TO BE FIVE TIMES AS LARGE AS THE IMPORT GROWTH RATE. IN THE LAST THREE YEARS, HOWEVER, THE IMPORT GROWTH RATE HAS BEEN 16 PERCENT A YEAR WHILE OUR EXPORT GROWTH RATE HAS BEEN 7 PERCENT -- AND SO FAR THIS YEAR OUR EXPORTS TO CHINA ARE DOWN 5 PERCENT.

AS I NOTED CHINA RUNS A $57 BILLION TRADE SURPLUS WITH THE UNITED STATES, BUT OVERALL HAS A GLOBAL TRADE SURPLUS OF $44 BILLION -- SO THEIR TRADE WITH US IS WHERE THEY ARE ACCRUING THEIR FOREIGN EXCHANGE EARNINGS.

WITH THE FOCUS ON ASIA, IT IS FREQUENTLY NOT REALIZED HOW MUCH OUR TRADE POSITION HAS DETERIORATED WITH EUROPE. IN 1991, THE UNITED STATES HAD A SURPLUS OF $19 BILLION WITH EUROPE; IN 1998, OUR DEFICIT HAD REACHED $32 BILLION – A NEGATIVE SWING OF $51 BILLION.

WITH RESPECT TO OUR NAFTA PARTNERS, THE STORY OF STRONG DOMESTIC U.S. GROWTH PULLING IN IMPORTS ALSO APPLIES. SO FAR IN 1999 THE TRADE DEFICIT WITH MEXICO IS $24 BILLION AT AN ANNUAL RATE COMPARED WITH $14 BILLION THIS TIME LAST YEAR, AND THE DEFICIT WITH CANADA IS $27 BILLION COMPARED WITH $13 BILLION A YEAR AGO. THE DECLINE OF THE CANADIAN DOLLAR AND MEXICAN PESO AGAINST THE U.S. DOLLAR OVER THE LAST THREE YEARS ALSO PLAYS A ROLE IN CREATING THESE

DEFICITS WITH OUR NAFTA PARTNERS.

OVERALL, THERE IS NOTHING ON THE IMMEDIATE HORIZON TO SUGGEST CHANGES IN OUR RECENT TRADE TRENDS. U.S. ECONOMIC GROWTH, EVEN THOUGH EXPECTED TO SLOW IN 1999 FROM 1998, SHOULD STILL BE RELATIVELY STRONG COMPARED TO MOST OF OUR MAJOR TRADING PARTNERS. IN EUROPE AND JAPAN EXPECTATIONS ARE FOR SLOW GROWTH.

WE CANNOT, HOWEVER, BLAME ALL OUR DEFICIT ON THE ASIAN FINANCIAL CRISIS AND ON THE RECENT DIFFERENCE BETWEEN U.S. AND FOREIGN ECONOMIC GROWTH.

LONGER TERM FORCES ARE ALSO AT WORK -- INCLUDING THE CONTINUED EXISTENCE OF TRADE BARRIERS THAT HAVE HELD BACK U.S. EXPORT OPPORTUNITIES. AMAZING THOUGH IT MAY NOW SEEM, FROM 1894 TO 1970 THE UNITED STATES HAD AN UNBROKEN STRING OF TRADE SURPLUSES, BUT SINCE 1970 WE HAVE HAD VIRTUALLY AN UNBROKEN STRING OF MERCHANDISE TRADE DEFICITS THAT HAVE CUMULATED TO OVER $2 TRILLION DOLLARS.

MOST OF OUR DEFICIT OCCURRED IN THE LAST FIFTEEN YEARS. NEARLY 80 PERCENT OF THE DEFICIT IS WITH ASIA – AND FULLY 40 PERCENT OF THE TOTAL WAS WITH ONE COUNTRY, JAPAN.

THE RECENT RISE IN THE TRADE DEFICIT REFLECTS, IN PART, THE HEALTH OF THE U.S. ECONOMY. OUR UNEMPLOYMENT RATE IS EXTREMELY LOW BY HISTORIC STANDARDS, INFLATION IS LOW, ECONOMIC GROWTH CONTINUES ABOVE ITS LONG TERM TREND, AND REAL INCOMES ARE RISING STRONGLY. IN ADDITION, THE RISE IN THE STOCK MARKET HAS ENCOURAGED CONSUMER SPENDING. THE BIGGEST NEGATIVE IS PROBABLY OUR PERSONAL SAVINGS

RATE WHICH IS CLOSE TO ZERO.

WHILE CURRENT ECONOMIC CONDITIONS, AT LEAST FOR THE UNITED STATES ARE EXCELLENT, WE CAN'T HELP BUT BE CONCERNED WITH RUNNING EXTREMELY HIGH CURRENT ACCOUNT DEFICITS LONG INTO THE FUTURE. TO FINANCE THESE DEFICITS WE MUST BORROW FROM ABROAD.

THUS, WE BECOME EVER MORE DEPENDENT UPON RECEIVING AND RETAINING FOREIGN CAPITAL. THE NET DEBTOR POSITION OF THE UNITED STATES, IN FACT, STOOD AT $1.2 TRILLION DOLLARS IN 1998 -- MORE THAN DOUBLING IN TWO YEARS. IF CURRENT TRENDS CONTINUE, OUR TOTAL FOREIGN DEBT WILL BE CLOSE TO ONE-AND-HALF TRILLION DOLLARS AT THE END OF 1999.

ANOTHER FACTOR THAT MUST BE CONSIDERED IS THE IMPACT OF TRADE DEFICITS ON THE COMPOSITION OF OUR EMPLOYMENT. THE DROP IN OUR EXPORTS HAS HAD A SERIOUS EFFECT ON MANUFACTURING EMPLOYMENT IN THE UNITED STATES. WHILE OVERALL EMPLOYMENT IN OUR COUNTRY IS AT RECORD LEVELS AND, IN FACT, HAS GROWN BY 2 MILLION JOBS IN THE LAST YEAR, THERE ARE 422,000 FEWER MANUFACTURING JOBS THAN A YEAR AGO. MANY OF THESE LOSSES ARE DIRECTLY ATTRIBUTABLE TO THE DECLINE IN U.S. EXPORTS GLOBALLY -- AND ESPECIALLY TO ASIA.

FEW ACTIONS WE CAN TAKE DOMESTICALLY WOULD HAVE AS GREAT AN IMPACT ON OUR TRADE DEFICIT POSITION AS RESTORATION OF GROWTH IN OUR MAJOR EXPORT MARKETS. THE KEY HERE IS IN ECONOMIC POLICIES IN EUROPE AND JAPAN THAT WOULD PROMOTE DOMESTIC-LED GROWTH IN THOSE COUNTRIES.

WHEN FORMER SECRETARY RUBIN SPOKE ON THIS ISSUE ON JUNE 10, HE SAID,

> "IT IS ALSO CRITICALLY IMPORTANT THAT EUROPE AND JAPAN DO THEIR PART BECAUSE THE INTERNATIONAL SYSTEM CANNOT SUSTAIN INDEFINITELY THE LARGE IMBALANCES CREATED BY THE DISPARITIES IN GROWTH AND OPENNESS BETWEEN THE U.S. AND ITS MAJOR TRADING PARTNERS."

ON JULY 13, SECRETARY SUMMERS SAID,

> "WE CONTINUE TO WATCH THE JAPANESE ECONOMY CAREFULLY AND TO BELIEVE THAT WHAT'S MOST IMPORTANT FOR JAPAN IS THE RESTORATION OF DOMESTIC DEMAND-LED GROWTH AND IT IS IMPORTANT THAT THE BASIS FOR GROWTH BE FIRMLY ESTABLISHED."

THE NEED FOR THESE OTHER LEADING ECONOMIES TO GROW IS CLEAR AS OUR CURRENT ACCOUNT DEFICIT POSITION IS UNSUSTAINABLE IN THE LONG RUN. CHAIRMAN OF THE FEDERAL RESERVE BOARD ALAN GREENSPAN SAID ON MAY 6,

> "THERE IS A LIMIT TO HOW LONG AND HOW FAR DEFICITS CAN BE SUSTAINED SINCE CURRENT ACCOUNT DEFICITS ADD TO NET FOREIGN CLAIMS ON THE UNITED STATES .... UNLESS REVERSED, OUR GROWING INTERNATIONAL IMBALANCES ARE APT TO CREATE SIGNIFICANT PROBLEMS FOR OUR ECONOMY."

IN HIS TESTIMONY TODAY BEFORE THE HOUSE BANKING AND FINANCIAL SERVICES COMMITTEE, HE NOTED:

> "AS U.S. INTERNATIONAL INDEBTEDNESS MOUNTS, HOWEVER, AND FOREIGN ECONOMIES REVIVE, CAPITAL INFLOWS FROM ABROAD THAT ENABLE DOMESTIC INVESTMENT TO EXCEED DOMESTIC SAVING MAY BE DIFFICULT TO SUSTAIN. ANY RESULTING DECLINE IN DEMAND FOR DOLLAR ASSETS COULD WELL BE ASSOCIATED WITH HIGHER MARKET INTEREST RATES, UNLESS DOMESTIC SAVING REBOUNDS."

CHAIRMAN GREENSPAN WENT ON TO REINFORCE FORMER SECRETARY RUBIN'S REMARKS THAT I CITED EARLIER IN MY TESTIMONY THAT:

> "WORKING TO OFFSET SOMEWHAT THIS ANTICIPATED SLOWING OF THE GROWTH OF DOMESTIC DEMAND, OUR EXPORT MARKETS CAN BE EXPECTED TO BE MORE BUOYANT BECAUSE OF THE REVIVAL IN GROWTH IN MANY OF OUR IMPORTANT TRADING PARTNERS."

•

WE NEED TO BE WORKING TO BRING THE DEFICIT DOWN OVER THE LONG TERM. WE MUST CONTINUE TO URGE OUR PARTNERS TO INITIATE DOMESTIC GROWTH POLICIES, AND WE MUST ALSO FOSTER CONDITIONS FOR A RESTORATION OF OUR TRADE POSITION WHEN FOREIGN MARKETS RECOVER BY ASSURING THAT FOREIGN MARKETS REMAIN OPEN BY ENFORCING OUR TRADE LAWS AND PROMOTING EXPORTS.

WHILE I DO NOT BELIEVE THAT NON-COMPLIANCE BY OUR TRADING PARTNERS WITH TRADE AGREEMENTS IS THE MAJOR FACTOR IN THE GROWTH OF OUR DEFICIT, WE MUST BE SURE THAT COUNTRIES ARE KEEPING MARKETS OPEN AND COMPLYING WITH THE TRADE AGREEMENTS THEY SIGN WITH US. WE NEED TO ASSURE AMERICANS THAT THE AGREEMENTS WE NEGOTIATE ARE HONORED AND THAT AMERICAN FIRMS AND WORKERS OBTAIN THE BENEFITS AND OPPORTUNITIES WE HAVE BARGAINED FOR.

THE COMMERCE DEPARTMENT, AS NEVER BEFORE, IS INCREASING ITS MONITORING OF OUR TRADE AGREEMENTS. WHEN WE FIND INDICATIONS OF VIOLATIONS, WE ARE BEING VERY AGGRESSIVE IN TAKING UP THESE MATTERS BILATERALLY OR WORKING WITH USTR TO HAVE THEM REFERRED TO APPROPRIATE DISPUTE SETTLEMENT FORA WHETHER IN THE WTO, NAFTA OR ELSEWHERE.

THE COMMERCE DEPARTMENT IS ALSO COMMITTED TO SWIFT ENFORCEMENT OF THE FAIR TRADE LAWS WHICH ENSURE THAT U.S. INDUSTRIES AND AMERICAN WORKERS ARE NOT INJURED BY IMPORTS OF UNFAIRLY PRICED OR SUBSIDIZED GOODS. DURING THE FIRST SIX MONTHS OF THIS YEAR ALONE, WE HAVE EITHER COMPLETED OR ARE IN THE PROCESS OF CONDUCTING MORE THAN 65 ANTIDUMPING OR COUNTERVAILING DUTY INVESTIGATIONS.

AS YOU ARE AWARE, STEEL IMPORTS SURGED DRAMATICALLY IN 1998, UP 33 PERCENT OVER 1997, RESULTING IN THE LOSS OF 11,000 JOBS. IN RESPONSE, THE ADMINISTRATION HAS PURSUED A TWO-PRONG STRATEGY COMBINING SWIFT AND VIGOROUS ENFORCEMENT OF OUR TRADE LAWS WITH BILATERAL PRESSURE ON OUR TRADING PARTNERS TO REDUCE SURGES OF STEEL EXPORTS. COMMERCE'S STRONG AND SWIFT ENFORCEMENT OF THE UNFAIR TRADE LAWS IS AN INTEGRAL PART OF THE ADMINISTRATION'S ACTION PLAN ON STEEL.

PRELIMINARY FIGURES FOR THE MONTH OF JUNE SHOW THAT STEEL IMPORTS DECREASED BY 13 PERCENT FROM MAY'S LEVEL, AND REMAIN WELL BELOW LAST YEAR'S SURGE LEVELS. OVERALL STEEL IMPORTS IN JUNE 1999 WERE 20 PERCENT BELOW JUNE 1998 LEVELS. IN THE FIRST SIX MONTHS OF THIS YEAR, STEEL IMPORTS ARE DOWN APPROXIMATELY 9 PERCENT COMPARED TO 1998 AND ARE LESS THAN 3 PERCENT ABOVE 1997'S PRE-CRISIS LEVELS.

COMMERCE CONTINUES TO ADMINISTER ITS ENHANCED EARLY WARNING SYSTEM TO MONITOR IMPORTS OF STEEL AND OTHER IMPORT-SENSITIVE PRODUCTS.

BEYOND COMPLIANCE AND ENFORCEMENT, WE MUST BE PREPARED TO TAKE ADVANTAGE OF EXPORT OPPORTUNITIES AS FOREIGN GROWTH RETURNS. U.S. FIRMS NEED TO TAKE MORE ADVANTAGE OF OVERSEAS MARKETS.

THE COMMERCE DEPARTMENT, WORKING WITH THE INTER-AGENCY TRADE PROMOTION COORDINATION COMMITTEE (TPCC), CONTINUES TO PRESS AHEAD WITH NEW STRATEGIES AND APPROACHES TO ASSISTING U.S. FIRMS AND WORKERS WITH TRADE PROMOTION. ITA'S UNITS, INCLUDING THE FOREIGN COMMERCIAL SERVICE, THE TRADE DEVELOPMENT UNIT AND MY MARKET ACCESS AND COMPLIANCE UNIT, ARE WORKING TOGETHER TO HELP SMALL AND MEDIUM SIZED FIRMS TAKE ADVANTAGE OF EXPORT OPPORTUNITIES.

BEFORE CLOSING, I WANT TO AGAIN THANK THE CHAIR AND OTHER MEMBERS OF THE SUBCOMMITTEE FOR YOUR ASSISTANCE, DURING THE INTERNATIONAL RELATIONS COMMITTEE'S REAUTHORIZATION OF THE COMMERCE DEPARTMENT'S INTERNATIONAL TRADE ADMINISTRATION. IN ADDITION, I THANK YOU FOR DRAWING ATTENTION TO THE CRITICAL WORK DONE BY THE MARKET ACCESS AND COMPLIANCE (MAC) UNIT WHICH I HEAD.

I AM PLEASED THAT YOU AND YOUR COLLEAGUES APPRECIATE OUR EFFORTS TO ACCESS FOREIGN MARKETS FOR AMERICAN FIRMS AND WORKERS AND TO ACHIEVE FULL COMPLIANCE BY OUR TRADING PARTNERS WITH THE TRADE AGREEMENTS THEY SIGN WITH OUR COUNTRY. IF WE CAN OBTAIN THE INCREASE IN FUNDING REQUESTED FOR US IN THE PRESIDENT'S FY 2000 BUDGET, WE WILL BE ABLE TO STRENGTHEN OUR EFFORTS TO HELP U.S. FIRMS, PARTICULARLY THE SMALL- AND MEDIUM-SIZED FIRMS THAT ARE THE ENGINES OF GROWTH IN OUR ECONOMY.

FINALLY, I AGAIN WANT TO SALUTE YOU, MADAM CHAIR, FOR YOUR WORK ON THE TRADE DEFICIT ISSUE. YOU MIGHT WANT TO HAVE YOUR STAFF PASS ON THE RECORDS OF YOUR HEARINGS TO THE CONGRESSIONALLY-CREATED TRADE DEFICIT REVIEW COMMISSION THAT I MENTIONED EARLIER IN MY TESTIMONY.

THANK YOU AND I WILL BE PLEASED TO ANSWER YOUR QUESTIONS.

Prepared Statement of
The Honorable Patrick A. Mulloy
Assistant Secretary of Commerce for Market Access and Compliance

before the
U.S. Trade Deficit Review Commission

December 10, 1999

Thank you very much for asking me to testify before this-Commission. In your invitation letter, you asked me to comment on the Causes, Consequences, Impacts and Solutions to the U.S. Trade Deficit. I have followed with interest the work of this Commission and the previous hearings you have held both in Washington and throughout our country. You have heard many points of view on the important matters Congress has called on you to study. Your work is very important to our national well-being and I salute you for the thorough approach you are taking in carrying it out.

My name is Patrick Mulloy. I head up the Market Access and Compliance unit at the Commerce Department's International Trade Administration. Before my appointment, I worked for many years on the staff of the U.S. Senate Banking Committee and developed a keen interest in the matters you have been charged by Congress to study and make recommendations. 1 am honored to be included among the distinguished witnesses you will hear from today.

The Market Access and Compliance unit plays a key role in U.S. Government efforts to secure a level playing field in foreign markets for American firms and workers. We work closely with the Office of the U.S. Trade Representative along with the State and Agriculture Departments and other federal agencies. The country specialists in my unit, together with our recently created Trade Compliance Center, work to identify and eliminate market access barriers around the globe as well as to ensure that U.S. firms and workers receive the benefits that we negotiated for under trade agreements signed by the United States. **My** service in this position has helped me to better understand the issues that you are presently examining.

Macroeconomic Forces Influencing Our Trade Deficit

The most important factor to trade is the pace of economic demand, both in the United States and abroad. Domestic economic growth is important because U.S. imports, like imports in most other industrial countries, tend to grow along with domestic demand. In 1991, when the United States was in a recession and our overall GDP declined 0.2 percent, imports of goods and services fell slightly over 1 percent in current dollars. The trade deficit in 1991 was only $31 billion, while only four years earlier the trade deficit was over $150 billion. Clearly, the strength of the domestic economy matters greatly for imports and for the trade balance.

But foreign economic growth is also important to U.S. exports and our trade balance. Plagued by economic problems in Asia, Russia, and in South America, world economic growth was only 2.0 percent in 1998. This was down considerably from the over 4 percent growth rates of the four prior years. The financial crisis in Asia that began in mid-1997 contracted the market for U.S. exports. Exports to the five Asian crisis countries declined 24 percent between 1996 and 1998, and the U.S. trade deficit with these countries worsened to $38 billion from $16 billion in 1996. It is difficult to sell products, regardless of their price or quality, in markets that are weak. In light of this factor, it is not at all surprising that U.S. export growth is weak and the trade deficit has widened substantially. Overall demand in the United States has increased 4.2 percent per year in the last three years, and Americans are buying more not only from U.S. producers, but from foreign producers as well. Imports of goods and services are up 10.2 percent in the first nine months of this year over the same period in 1998.

Review of Recent Trade Data

I would like briefly to summarize the current situation in our trade balance. The U.S. trade deficit has risen this year to an annual rate of $255 billion, from $164 billion in 1998 and an average of about $100 billion between 1994 and 1997. In 1998, exports of goods and services declined 0.5 percent while imports increased 5.3 percent. The last year when exports rose rapidly was in 1997, largely before the Asian crisis, when exports gained 10.4 percent and imports 9.3 percent. During the first nine months of 1999, exports have increased only 1.8 percent from the same period a year ago, while imports are up 10.2 percent.

Reflecting the crucial role of macroeconomic conditions on trade and the widespread economic slowdown outside the United States, the increase in the U.S. trade deficit has been broadly based, encompassing most geographic areas and industrial sectors. U.S. exports to the <u>Western Hemisuhere</u> are up only 1.3 percent thus far this year, while imports have risen 13.8 percent. Our trade deficit with the Western Hemisphere has reached an annual rate of $58 billion compared with $18 billion for the same period of 1998. The trade deficit with Canada has doubled to $30 billion; that with Mexico has grown to $25 billion; and the surplus with South America has fallen to a $3 billion deficit as exports to the region have dropped 20 percent.

U.S. exports to the <u>Euronean Union</u> are up less than one percent in the first nine months of 1999 as compared with the same period in 1998. Imports, however, are up 10.3 percent and the trade deficit is at an annual rate of $40 billion compared with $24 billion at this time last year. The trade balance has fallen even more with <u>**Asia**</u>, the source of the worldwide economic slowdown in 1997, where U.S. exports are up 1.8 percent from a year ago, while imports are up 8.9 percent and the deficit is at an annual rate of $2 10 billion. This is $29 billion higher than last year. Japan and China clearly account for the lion's share of this situation, but U.S. trade is also affected by a continued weakness in exports to the former "Asian crisis" countries as a group (Indonesia, Korea, Malaysia, Philippines, and Thailand).

There are also imbalances in all industrial sectors. The manufacturing sector has been the most significantly affected, as exports are only 1.6 percent higher than last year, while imports are up nearly 11 percent. The trade deficit in manufactured goods is $263 billion (annual rate) compared with $189 billion this time last year. Import growth exceeds export growth in chemicals, textiles, paper and paperboard, general industrial machinery, power generating machinery, specialized industrial machinery, autos, aircraft, computers, and scientific instruments, to mention some key sectors.

Our traditional surplus in agricultural commodities is down to $10 billion, from a high of $28 billion in 1996, reflecting the lower prices of wheat and corn and lost markets in Asia. With the price of crude oil back up to well over $20 per barrel, the deficit in this sector is again expanding. And in services, our large surplus has shrunk due to a weakness in tourism which is our biggest service export. Earnings from tourism far exceed those in financial services or professional services.

The Long-Term

Much of the testimony the Commission received in last August's hearings indicated that the growth in the U.S. trade deficit over the last couple of years is due largely to the difference between rapid U.S. economic growth and slow economic growth or recession abroad. The trade deficit, though, is not just a short-term economic phenomenon, and the time horizon for its examination should not be limited to just the last few years. However, it is important to note that the deficit has resulted from different causes at various times, and in the 1990's it has resulted principally from an investment boom in the United States.

From 1894 to 1970 the United States had an unbroken string of trade surpluses and we became the world's largest creditor nation. Since 1970 we have been in deficit. While our deficit has grown more rapidly in some years than in others -- and indeed has even improved in some years -- there is an unmistakable long-term increase in the spread between our exports and our imports, and hence a long-term trend toward increasing deficits. However, this trend is less pronounced when the deficit is viewed as a percentage of GDP.

This trend is not evenly distributed among our trading partners. Our bilateral 'trade deficit is concentrated in our trade with Asia. Since 1990, Asia has accounted for 33 percent of our trade, but 86 percent of our bilateral trade deficit. In other words, trade with the entire rest of the world -- which accounted for two-thirds of our trade, produced only 14 percent of our bilateral trade deficit, Since 1990, almost half of the 86 percent of the deficit that resulted from our trade with Asia came from Japan.

Our trade patterns have generally reflected changes in macroeconomic forces. We had sizeable deficits with the rest of the world in the mid-eighties, and then had smaller deficits in the late 1980's and early 1990's. Our deficit began growing again in 1992 as the growth of the U.S. economy significantly outpaced foreign economies.

Our bilateral trade with Asia, however, has behaved differently than our trade with the rest of the world, and has shown a long term deficit trend. An examination of the export and import patterns shows that since the mid-l 970% U.S. imports from Asia have consistently been above U.S. exports to Asia and the spread between the two has increased.

Export Barriers in Asia

The forces underlying our trade deficits with Asia are complex. In part, the pattern of our trade deficits reflects the pattern of comparative advantage in the world. In part the pattern reflects macroeconomic and demographic forces in many Asian economies, which has led them to have high savings rates in recent decades. In addition, however, tariff and non-tariff barriers have been important factors holding back our export growth to Asia. These barriers are not a surprise to anyone within the international community who is familiar with the history of our trade policies.

These barriers are costly to U.S. producers and workers. By distorting the allocation of resources, they reduce our income. Removing barriers are important, even if they do not affect our saving or investment rates. To the extent our bilateral balance with Asia may reflect their trade-targeted policies, these economies have themselves been paying a steep price for distorting the workings of their economies. Japan, in particular, is weak, while the U.S. economy remains strong.

Over the past 50 years, the United States has lowered trade barriers more aggressively than other countries. As a result, the openness of the U.S. market is greater than that of our trading partners.

Developing countries in Asia, for the most part, did not contribute to major tariff decreases during the successive rounds of tariff cutting in the GATT. The "Asian Tigers" developed, with strong export-led growth economies. Since 1975, our exports to this region (Asia except Japan) have grown considerably less rapidly than our imports from them. The spread between our export growth and import growth with developing Asia brought our trade deficit with them from $2 billion in 1975 to $112 billion last year.

Tariffs remain a serious barrier to our exports in developing Asia. The average tariff on our industrial exports there is 15 percent while our import duties average less than 2 percent.

Tariffs, however, don't tell the whole story. Japan, for example, has tariffs on industrial goods that average less than 3 percent, yet consistently ranks among the markets in the world that American and other exporters consider the least open.

The Institute for International Economics published a report in January 1995 on Japan's protectionist practices. It examined the difference between the prices of imported products and similar products that were domestically produced, and calculated the implied margin of protection that keeps imports out of the market. That study ("Measuring the Costs of Protection in Japan" by Yoko Sazanami, Shujiro Urata, and Hiroki Kawai, Institute for International Economics, Washington, D.C.) showed that Japan's invisible protection for machinery imports was equivalent to an average tariff of 140 percent. With these types of non-tariff barriers in place, it is not surprising that we and many other countries have great difficulties exporting industrial products to Japan. Progress is possible, however. From 1990 to 1997 Japan's industrial production fell 3 percent, while its imports grew 44 percent; but Japan's imports of manufactures are still a relatively small proportion of its GDP and in sharp contrast to other major developed nations.

This disparity in trade barriers emphasizes the need to make further progress in reducing trade barriers in Asia. Americans are competitors. But we need, more than anything else, to know that the rules of the game of international trade are fair and that the openness of markets around the world is roughly equal. More fairness is needed to ensure continued support for the current trading system from those countries that have opened their markets and have borne the weight of international competition.

President Clinton in a February 1993 speech stated the principles that would guide trade policy in his Administration. One such principle he said:

> "...will say to our trade partners that we value their business, but none of us should expect something for nothing. We will continue to welcome foreign products and services into our markets, but insist that our products and services be able to enter theirs on equal terms."

Opening markets is not only good for us, but for others as well. Competition encourages efficiency and provides the latest technology. Lagging economies that impose barriers to U.S. and other imports should consider the cost of resisting free and fair trade.

That is why this Administration has spent so much energy working to convince other countries that they must and should open their markets to our exporters. It is why my Market Access and Compliance unit and a similar enforcement unit in USTR were created. These two units, coupled with the government's trade promotion and financing activities, which are marshaled by the Congressionally-established Trade Promotion Coordinating Committee chaired by the Secretary of Commerce, are vital to such efforts.

Addressing Trade Opportunities -What Does It Take?

We need to expand economic opportunities by opening new markets to American goods and services. Trade is fundamental to American prosperity today and in the future. We need to see that increased trade continues to contribute to American prosperity in the 21st century by supporting higher paying jobs through exports in our most productive sectors. Our incomes could be higher still by further opening foreign markets. The job is especially important in key Asian markets.

What must happen to obtain trade expansion? First, and most important, the pace of foreign economic growth must improve. On this score, there have been some encouraging developments. The recovery in most of the emerging market economies in Asia is already taking hold, and the recession in Japan may have come **to an** end. However, the Asian economies need to continue to pursue structural reforms to ensure a sustained expansion.

In Latin America, an important trading partner for the United States, the recession in major countries this year has been less severe than expected earlier in the year, and the IMF looks for 3.9 percent growth in 2000 for the region as a whole.

Growth in Europe will also be higher, but Europe still needs to pursue structural reforms, particularly in labor markets, to ensure a positive environment for investment **and** to promote further job creation to reduce still high unemployment. A better climate for investment in Europe would allow stronger growth over the medium-term without inflation risks, and contribute to better markets for U.S. exports.

This better economic climate has resulted in an upward revision of the **IMF's** forecast for global growth in 2000. Now, the IMF is predicting global growth of 3.5 percent, up from a projected growth of 3.0 percent in 1999. All told, this improved economic picture should help improve the prospects for U.S. exports.

Secondly, we must make further progress in opening foreign markets. While trade deficits stem from macroeconomic factors, foreign trade barriers are hampering the expansion of U.S. exports and reduce our incomes, which include agriculture, services and sophisticated manufactured goods. An improved U.S. standard of living and strengthened investment both in plant and in research and development would result from an ability to utilize our comparative advantage more fully, and we should spare no effort to reduce foreign trade **barriers** and ensure that foreign countries live up to the trade agreements they negotiate with us.

Third, the economy must remain competitive. Recent improvements in our rate of productivity increase are the result of the pressure to excel and, need to be continued.

Conclusion

While we know the causes of the deficit are basically macroeconomic, we also know that U.S. firms and workers will benefit from the reduction of trade and investment barriers around the globe. Opening markets and removing barriers offers benefits to the United States and the world even apart from any effects on the trade balance. The Administration has worked vigorously to reduce those barriers. It has also worked to support our exporters by better coordinating government program which support them working through the interagency Trade Promotion Coordination Committee. We are outreaching to U.S. businesses throughout the nation to support their export activities through financing, promotion and market opening activities.

Thank you for giving me this opportunity to appear before you.

Chart 1

THE U.S. TRADE BALANCE AS A PERCENT OF GDP

Chart 2

U.S. TRADE WITH THE WORLD EXCEPT ASIA

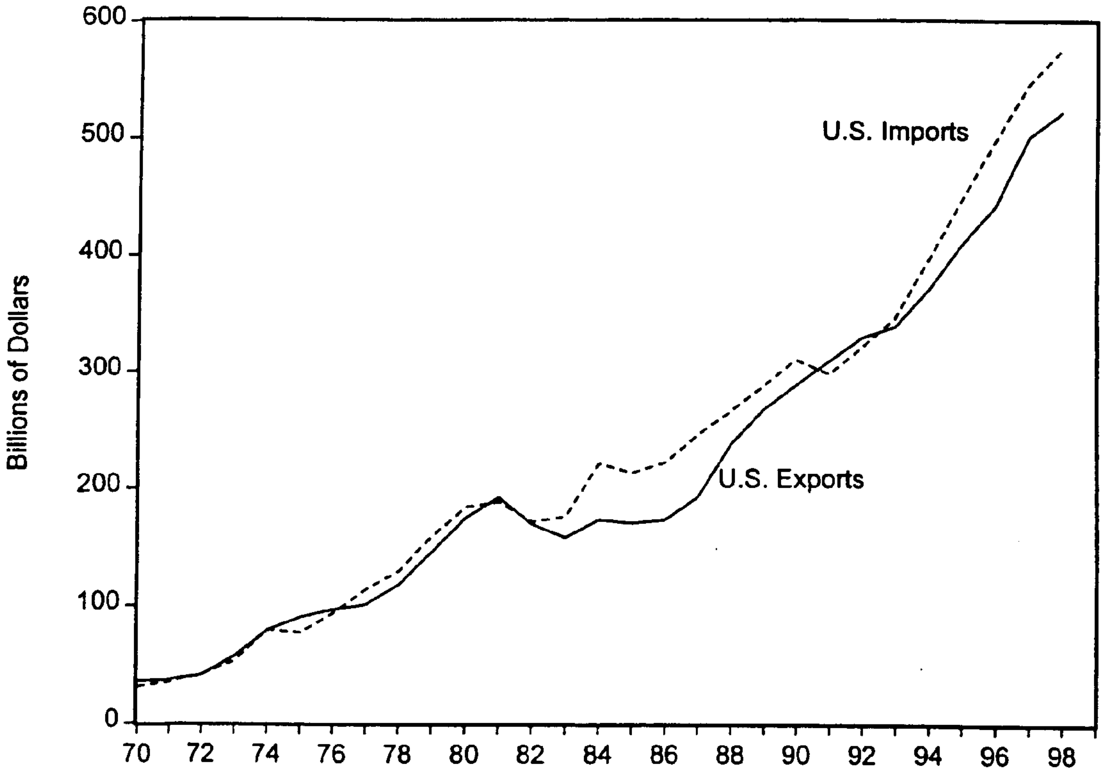

Chart 3

U.S. TRADE WITH ASIA

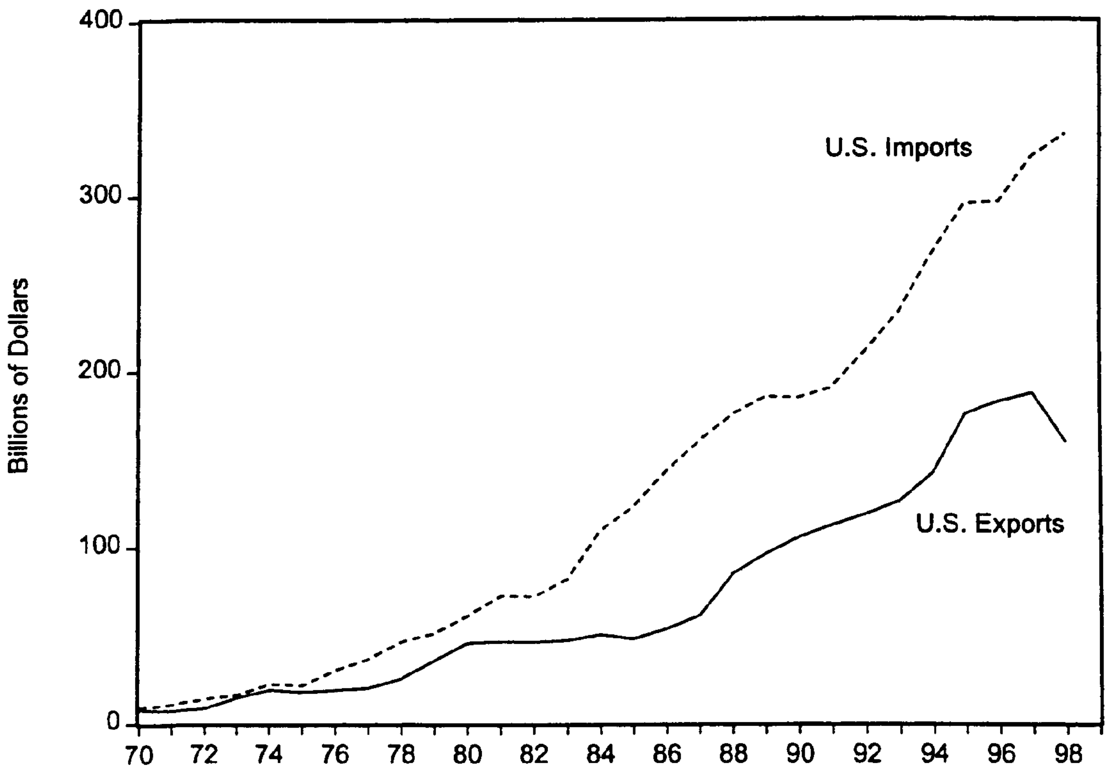

Chart 4

U.S. TRADE BALANCE WITH ASIA, AS A PERCENT OF U.S. GDP

Chart 5

U.S. TRADE BALANCE WITH WORLD EXCEPT ASIA AS A PERCENT OF GDP