ASIA TRADE ISSUES

HEARING

BEFORE THE

SUBCOMMITTEE ON TRADE

OF THE

COMMITTEE ON WAYS AND MEANS
HOUSE OF REPRESENTATIVES

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ASIA TRADE ISSUES

TUESDAY, FEBRUARY 24, 1998

HOUSE OF REPRESENTATIVES,
COMMITTEE ON WAYS AND MEANS,
SUBCOMMITTEE ON TRADE,
Washington, DC.

The Subcommittee met, pursuant to notice, at 11 a.m., in room 1100, Longworth House Office Building, Hon. Philip Crane (Chairman of the Subcommittee) presiding.

[The advisory announcing the hearing follows:]

ADVISORY

FROM THE COMMITTEE ON WAYS AND MEANS

SUBCOMMITTEE ON TRADE

FOR IMMEDIATE RELEASE CONTACT: (202) 225–1721
January 30, 1998
No. TR–21

Crane Announces Hearing on Asia Trade Issues

Congressman Philip M. Crane (R–IL), Chairman, Subcommittee on Trade of the Committee on Ways and Means, today announced that the Subcommittee will hold a hearing on trade issues with Asia, including the progress of the Asia-Pacific Economic Cooperation forum as well as the effects of the Asian financial crisis on U.S. trade. The hearing will take place on Tuesday, February 24, 1998, in the main Committee hearing room, 1100 Longworth House Office Building, beginning at 11:00 a.m.

Oral testimony at this hearing will be from both invited and public witnesses. In addition, any individual or organization not scheduled for an oral appearance may submit a written statement for consideration by the Committee or for inclusion in the printed record of the hearing.

BACKGROUND:

The Asian Pacific Rim has been our second fastest growing export market in recent years. U.S. exports to the area were over $200 billion in 1996, representing nearly one-third of U.S. exports, and imports totaled over $312 billion.

The Asia-Pacific Economic Cooperation (APEC) forum, an association of 18 economies bordering the Pacific Ocean working cooperatively to reduce barriers to trade and investment, has declared its intention to establish free trade and investment in the region by the year 2010 for industrialized members and 2020 for others. In November 1997, APEC members held a Joint Ministerial Meeting and Leaders Summit in Vancouver, at which they identified 15 areas of trade for further liberalization. Members are to finalize plans in the first half of 1998 to cut tariffs and other barriers to trade, with implementation of market-opening initiatives to begin in 1999, in the following 9 sectors: environmental goods and services, medical equipment, chemicals, energy, forest products, fish and fish products, toys, gems and jewelry, as well as a Mutual Recognition Agreement for telecommunications products and systems among APEC members. APEC members will continue to develop proposals for review by Ministers in June, for possible action by APEC Leaders next November, in the following 6 sectors: oilseeds and oilseeds products, food products, natural and synthetic rubber, fertilizers, automotive and civil aircraft.

As 1997 ended, many of the economies of East Asia faced a significant financial crisis, manifested in plummeting currency values, declines in the stock markets of those countries, and bankruptcies. That crisis has continued into 1998. The International Monetary Fund has developed financial support packages for several of these countries containing a number of conditions, including measures to increase trade liberalization.

Observers have noted that the crisis will have an impact on the U.S. economy and on U.S. businesses and workers. Although the effects of this crisis have not yet been reflected in the U.S. trade deficit, concerns have been raised that the deficit will increase as exports from Asia continue to increase and U.S. exports to Asia decline as a result of currency devaluations and slowdowns in the Asian economies. The continued crisis also raises concerns about unresolved trade and market access issues with these countries.

In announcing the hearing, Chairman Crane stated: "Free and open trade and investment policies have become an important pillar in the foundation underlying world peace, security, and economic stability. Asia continues to be a major market for U.S. goods, services, and investment. I have been greatly encouraged by the developments within APEC, which will increase our access to those markets and knock down trade barriers. We must view the Asian financial crisis as an opportunity to continue to work towards trade liberalization in these markets, to make systemic changes that will open markets and increase transparency, and increase confidence through the power of free trade."

FOCUS OF THE HEARING:

The hearing will focus on recent developments in trade with Asia, including: (1) the results of the APEC summit held in Vancouver in November; (2) the impact of the Asian financial crisis on trade with the United States, on the U.S. economy overall, and on particular sectors; (3) U.S. efforts to ensure that Asian countries pursue further liberalization of trade and investment barriers; (4) the extent to which market access issues for U.S. goods, services, and investment are being addressed during the crisis; (5) the likelihood that the countries undergoing the crisis will undertake the necessary systemic reforms and whether they seek to alleviate the situation by increasing exports to the United States; and (6) the impact of the crisis on other U.S. trading partners in the region.

DETAILS FOR SUBMISSIONS OF REQUESTS TO BE HEARD:

Requests to be heard at the hearing must be made by telephone to Traci Altman or Bradley Schreiber at (202) 225–1721 no later than the close of business, Monday, February 16, 1998. The telephone request should be followed by a formal written request to A.L. Singleton, Chief of Staff, Committee on Ways and Means, U.S. House of Representatives, 1102 Longworth House Office Building, Washington, D.C. 20515. The staff of the Subcommittee on Trade will notify by telephone those scheduled to appear as soon as possible after the filing deadline. Any questions concerning a scheduled appearance should be directed to the Subcommittee on Trade staff at (202) 225–6649.

In view of the limited time available to hear witnesses, the Subcommittee may not be able to accommodate all requests to be heard. Those persons and organizations not scheduled for an oral appearance are encouraged to submit written statements for the record of the hearing. All persons requesting to be heard, whether they are scheduled for oral testimony or not, will be notified as soon as possible after the filing deadline.

Witnesses scheduled to present oral testimony are required to summarize briefly their written statements in no more than five minutes. THE FIVE-MINUTE RULE WILL BE STRICTLY ENFORCED. The full written statement of each witness will be included in the printed record, in accordance with House Rules.

In order to assure the most productive use of the limited amount of time available to question witnesses, all witnesses scheduled to appear before the Subcommittee are required to submit 200 copies of their prepared statement and an IBM compatible 3.5-inch diskette in ASCII DOS Text or WordPerfect 5.1 format, for review by Members prior to the hearing. Testimony should arrive at the Subcommittee on Trade office, room 1104 Longworth House Office Building, no later than 5:00 p.m., Friday, February 20. Failure to do so may result in the witness being denied the opportunity to testify in person.

WRITTEN STATEMENTS IN LIEU OF PERSONAL APPEARANCE:

Any person or organization wishing to submit a written statement for the printed record of the hearing should submit at least six (6) single-space legal-size copies of their statement, along with an IBM compatible 3.5-inch diskette in ASCII DOS Text or WordPerfect 5.1 format only, with their name, address, and hearing date noted on a label, by the close of business, Tuesday, March 10, 1998, to A.L. Singleton, Chief of Staff, Committee on Ways and Means, U.S. House of Representatives, 1102 Longworth House Office Building, Washington, D.C. 20515. If those filing written statements wish to have their statements distributed to the press and interested public at the hearing, they may deliver 200 additional copies for this purpose to the Subcommittee on Trade office, room 1104 Longworth House Office Building, at least one hour before the hearing begins.

FORMATTING REQUIREMENTS:

Each statement presented for printing to the Committee by a witness, any written statement or exhibit submitted for the printed record or any written comments in response to a request for written comments must conform to the guidelines listed below. Any statement or exhibit not in compliance with these guidelines will not be printed, but will be maintained in the Committee files for review and use by the Committee.

1. All statements and any accompanying exhibits for printing must be typed in single space on legal-size paper and may not exceed a total of 10 pages including attachments. At the same time written statements are submitted to the Committee, witnesses are now requested to submit their statements on an IBM compatible 3.5-inch diskette in ASCII DOS or WordPerfect 5.1 format. Witnesses are advised that the Committee will rely on electronic submissions for printing the official hearing record.

2. Copies of whole documents submitted as exhibit material will not be accepted for printing. Instead, exhibit material should be referenced and quoted or paraphrased. All exhibit material not meeting these specifications will be maintained in the Committee files for review and use by the Committee.

3. A witness appearing at a public hearing, or submitting a statement for the record of a public hearing, or submitting written comments in response to a published request for comments by the Committee, must include on his statement or submission a list of all clients, persons, or organizations on whose behalf the witness appears.

4. A supplemental sheet must accompany each statement listing the name, full address, a telephone number where the witness or the designated representative may be reached and a topical outline or summary of the comments and recommendations in the full statement. This supplemental sheet will not be included in the printed record.

The above restrictions and limitations apply only to material being submitted for printing. Statements and exhibits or supplementary material submitted solely for distribution to the Members, the press and the public during the course of a public hearing may be submitted in other forms.

Note: All Committee advisories and news releases are available on the World Wide Web at 'HTTP://WWW.HOUSE.GOV/WAYS __MEANS/'.

The Committee seeks to make its facilities accessible to persons with disabilities. If you are in need of special accommodations, please call 202–225–1721 or 202–226–3411 TTD/TTY in advance of the event (four business days notice is requested). Questions with regard to special accommodation needs in general (including availability of Committee materials in alternative formats) may be directed to the Committee as noted above.

Chairman CRANE [presiding]. The Subcommittee will now come to order, and before we start with our first witness, Ms. Barshefsky, I would like to alert everyone to the fact that Mr. Matsui and I, unfortunately, owing to longstanding prior commitments, will be gone from roughly noon, sharp, until 1 p.m. However, the Subcommittee meeting will continue and will be presided over by other Members of the Subcommittee, and so we apologize to those that we may miss during that hour.

But we are pleased today to welcome to the Ways and Means Trade Subcommittee hearing on trade issues with Asia, as I indicated earlier, our distinguished friend and advocate of the advancement of U.S. trade interests. The purpose of this hearing is to examine the results of the Asia-Pacific Economic Cooperation, or APEC, summit in Vancouver last November. In addition, we'll examine the impact of the Asian financial crisis on trade with the United States, the economy overall, and particular sectors.

The Asian financial crisis has proven that the fate of our companies and workers is closely liked to their Asian counterparts. This interdependence does not make us vulnerable but instead increases opportunities and maximizes efficiency for Americans. A solid U.S. trade policy in which we continue to seek the elimination of trade barriers to our goods and services is the solution to the crisis.

The crisis is likely, at least in the short term, however, to increase our trade deficit. But, we should not be overly concerned because our economy is fundamentally strong and much of the deficit is generated not by an excess in U.S. consumption of imports, but by wise investment in growth opportunities abroad.

I do worry that misplaced concern about the deficit will paralyze our trade policy and make protectionist legislation tempting. We must resist the urge to close our market at this delicate time. Shutting our doors through protectionism would set a bad example for Asia and for the rest of the world that closed trade is an acceptable policy in difficult economic times.

Instead, we must pursue trade liberalizations abroad by bilateral action and by encouraging developments within APEC to increase our access to Asian markets. We should be on the lookout for increased Asian trade barriers. We should not tolerate policies that limit imports of our goods and services, and we should not permit Asia to increase United States-bound exports excessively to the detriment of our companies and workers.

We must also encourage Japan to open its market to absorb some excess capacity from its neighbors. We must urge China to continue its structural reforms and strengthen its currency. And we must keep a careful eye on Hong Kong and Taiwan.

In short, we have to do everything we can to get the Asian region back to health so that its consumers may continue to purchase our goods and services and create opportunities for our companies and workers. The Asian financial crisis is an opportunity to foster trade liberalization in these markets and make systematic changes that will open markets that will increase transparency and bolster confidence through the power of free trade.

Free trade is not to blame for the crisis. It is the solution.

[The opening statement follows:]

Opening Statement of Hon. Phil Crane, a Representative in Congress from the State of Illinois

Good morning, and welcome to the Ways and Means Trade Subcommittee hearing on trade issues with Asia. The purpose of this hearing is to examine the results of the Asia-Pacific Economic Cooperation (or "APEC") summit in Vancouver last November. In addition, we will examine the impact of the Asian financial crisis on trade with the United States, the economy overall, and particular sectors.

The Asia financial crisis has proven that the fate of our companies and workers is closely linked to their Asian counterparts. This interdependence does not make us vulnerable, but instead increases opportunities and maximizes efficiencies for Americans. A solid U.S. trade policy in which we continue to seek the elimination of trade barriers to our goods and services is the solution to the crisis.

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I now recognize our distinguished Ranking Member, Mr. Matsui, for any statement he would like to make.

Chairman CRANE. I now recognize our distinguished Ranking Member, Mr. Matsui, for any statement he would like to make.

Mr. MATSUI. Thank you very much, Mr. Chairman, and thank you for holding these hearings today. I think they are extremely important and extremely timely. I have a statement that I would like to submit for the record for time reasons, if I may.

Chairman CRANE. Without objection, so ordered.

Mr. MATSUI. Thank you. I would like to reiterate what you just said in terms of the issue the potential trade deficit that may occur or increase as a result of the financial crisis in Asia. I really hope, as you have stated, that we don't preoccupy ourselves with that and become immobilized or perhaps paralyzed with a focus on this trade deficit issue because certainly it's important, it's a factor in terms of the U.S. economy, our strength. On the other hand, it will, in fact, keep interest rates down, inflation down and, to some extent, it may even point out the strengths of the U.S. economy. As all of us know, the trade deficit in and of itself is not necessarily the only relevant factor in the entire discussion of one's economy and one's relationship with their trading partners—investment patterns, the budget deficit, savings rates throughout the world, and particularly in the United States, all these are critical elements.

I appreciate the fact that the Chair has indicated that we must not preoccupy ourselves with the trade deficit in and of itself.

Thank you, Mr. Chairman.

[The opening statement follows:]

Opening Statement of Hon. Robert T. Matsui, a Representative in Congress from the State of California

Mr. Chairman, it is important and timely that the Subcommittee is holding this hearing today on United States trade relations with Asia. Nearly one-third of our total trade is with East Asian countries, which are our second fastest-growing export market. The United States and Asian economies are inextricably linked. Therefore, the impact of the Asian financial crisis on our trade and overall economy, the impact on other economies, and the nature and timing of our response to that crisis are of crucial importance for our businesses and workers.

I Support the administration's request for congressional approval of $18 billion in additional funding for the IMF as soon as possible in order to promote economic stability in Asia and to prevent the effects of the crisis from spreading globally. But it is essential as a condition for IMF support that the Asian economies undertake the fundamental structural reforms necessary to ensure that the current problem does not become a recurring one, including measures to liberalize their trade regimes. It is also important that the sector market-opening initiatives launched at the Vancouver Summit of the APEC last November proceed as planned toward the goal of eventual free trade and investment in the region.

I welcome Ambassador Barshefsky back to the Subcommittee and look forward to the testimony of all the witnesses regarding the impact of the Asian crisis on our trade and economy and the prospects for future trade liberalization in the region.

Chairman CRANE. Thank you, Mr. Matsui. Today we'll hear from a number of distinguished witnesses, and in the interests of time, I ask that you try to keep your oral testimony in the neighborhood of 5 minutes, and we'll include all the longer written statements in the record. And our first witness is our dear friend, and distinguished Ambassador, Charlene Barshefsky, the U.S. Trade Representative. Because of scheduling problems, she'll be followed by Mr. Bergsten and Mr. Sweeney. Under Secretaries Eizenstat and Lipton will follow at roughly 1 o'clock. And now we yield the floor to our distinguished Ambassador.

STATEMENT OF HON. CHARLENE BARSHEFSKY, U.S. TRADE REPRESENTATIVE

Ms. BARSHEFSKY. Thank you very much, Mr. Chairman, Mr. Matsui, Mr. McDermott, Ms. Dunn. I'm pleased to appear before you to discuss the implications of the financial situation in Asia for United States trade policy, and the importance of rapid congressional action on the administration's request for the IMF quota subscription and the augmented backup facility, the New Arrangements to Borrow.

By any measure, the Asian economy has experienced a dramatic reversal of fortune these last 6 months. Countries which had high rates of growth over the past decade, 7 to 10 percent, now face minimal or even negative growth in 1998 and perhaps beyond. The financial crisis has also resulted in a dramatic currency depreciation.

Before turning to a discussion of the crisis, let me make a few preliminary observations. First of all, as the Chairman has pointed out, the U.S. economy is as strong as it has been in almost 30 years. Our ability to weather this storm in Asia is, therefore, better than at any time.

Second, U.S. prosperity is no small part the result of the export opportunities we've created in Asia and around the globe, including through the negotiation of some 245 trade agreements since 1993. Today, exports support an estimated 12.1 million higher paying American jobs. Our economic interests at home demand that we continue to open foreign markets and lead in the global economy.

The causes of the Asian financial crisis are, of course, complex and multifaceted. But in each country and across the region, we find a common web: inadequate supervision of financial institutions; speculative real estate and equity booms; excessively close times between governments, banks, and corporations.

These relationships and, in some countries, a deep-seated resistance to competition, including open trade and investment, resulted in a misallocation of capital. Many investments that led to insolvency would never have been made under more competitive conditions. Investments flowed into the region as if on autopilot, quadrupling in less than a decade to expand capacity well in excess of current or projected global demands with no basis in market reality. You then have a fundamental mismatch between short-term bank funding fueled by foreign investments, and long-term lending transactions for projects of dubious merit, a phenomenon that Federal Chairman Alan Greenspan called "a pattern of conspicuous construction." This broad combination of factors proved combustible.

In response to the crisis, the IMF moved quickly to stabilize the economies and create the conditions for stabilized currencies in the affected countries. While these measures were taken to restore financial stability and an early return to sustainable growth, a stable Asia is also the most important policy objective we can have.

The region is a principle United States customer supporting millions of United States jobs, about 28 percent of our exports went to Asia last year. We cannot sell to Asia if Asia cannot buy. The IMF is, therefore, critical in trade terms for this most basic and fundamental reason, and that is to stabilize the Asian economies and to create the conditions for stabilized currencies. Not doing so only further undermines our export opportunities and a return to sustainable economic growth in Asia. Not doing so also puts additional pressure on our domestic industries that must compete with cheaper imports. But beyond this, structural reform must be put in place to build a longer term foundation for economic stability in Asia.

The stabilization program for the IMF reflects this goal and includes measures to strengthen financial sectors, rationalize business-government linkages, improve transparency, open markets to foreign investors, and reduce trade barriers. If effectively implemented, these programs complement and reinforce longstanding U.S. trade policy goals.

In this regard, let me review for you briefly the broader systemic trade policy issues that have arisen in Korea and Indonesia in particular, and the intersection of these issues with the IMF structural adjustment program.

First let us examine Korea, which is one of our most important markets. In Korea, the relationship between governments, banks and commercial enterprises resulted in a misallocation of capital to economic ventures of questionable merit, nonetheless being central to industrial policy goals. This misallocation of capital fueled the expansion of the chaebols—the conglomerates—into lines of business of dubious value, in routine overproduction, and in excessive exports in such targeted industries as autos, steel, semiconductors, and ships. This misallocation exacerbated, in turn, market excess problems in Korea, including import clearance and certification hurdles, import licensing procedures, anticompetitive practices, and other barriers to market access.

The Korean stabilization package negotiated by the IMF should help to open and expand competition in the Korean economy. Indeed, Korea is moving forward strongly and decisively to implement the IMF Program. It still faces many challenges but the incoming President, Prime Minister Kim Dae Jung, has demonstrated a strong commitment to market opening and economic restructuring that are at the heart of the reform program.

The IMF reforms will put a stop to government-directed lending for industrial policy goals, will ease restrictions on foreign investment, and will simplify regulatory requirements to allow greater competition from imported goods. Other more specific IMF reforms will reinforce and expand upon Korea's commitments in the WTO and the OECD, including the elimination of trade subsidies and preferential tax treatment, opening further the financial services sector, and liberalizing rules on import licensing and certification—all longstanding U.S. trade policy concerns.

Let me turn for a moment to Indonesia. As in Korea, the IMF stabilization program, if faithfully implemented, should move the country in the direction of more open markets, transparency, and increased competition. Additionally, the structural focus of the package that the IMF has put together goes to the heart of some of the most vexing trade problems. Key elements of that program include the immediate elimination of special tax privileges to the national car project; the removal of foreign investment restrictions on wholesale and retail trade; the reduction of custom duties and border nontariff measures on imports and exports, including in the agricultural sector; the elimination of commodity import and export monopolies for sugar, wheat, and other commodities; the removal of certain internal marketing arrangements and export quotas. These commitments address practices that have long been the subject of the administration's bilateral trade policy.

In the short term, as you've pointed out, Mr. Chairman, and as Mr. Matsui pointed out, the forces unleashed by the withdrawal of capital from the Asian market reflected in part from depreciating currencies and a slowdown in economic activity in the region, will, of necessity, result in increased exports from the region and import contraction in Asia. Because the United States today is the strongest economy in the world, and the most open, we can expect a short-term increase in imports from the region, and our exports will decline. The expected short-term deterioration in the trade balance must not, however politically appealing, open the way to protectionism or isolationism. To go down this path would immediately undermine our primary goal which is to stabilize the immediate crisis and minimize its negative effects on the U.S. economy. We would also jeopardize the real possibility of longer term structural reforms of these economies. We will keep our markets open, but we must also see other countries respond by opening their markets and stimulating domestic demand, and in this regard, Japan, as the second largest economy in the world, has an especially crucial role to play.

We see the need for action by Japan in three areas. First, we strongly agree with the view of the IMF that fiscal stimulus is needed to support Japan's economy and make it a potential source of confidence for the region. Second, it is crucial for Japan to act clearly and decisively to strengthen its financial system with the infusion of public money. Finally, it is equally important that

Japan deregulate financial and other sectors to open up the Japanese market.

The United States cannot be the only engine of global growth. The United States cannot be the sole buyer of goods to absorb the tremendous production capability of Asia. Japan must act in the interest of the region and the global economy.

This administration has spent the past 5 years, and this Subcommittee has spent the past 5 years and many years before that, focusing considerable attention on the Asian markets, particularly the substantial barriers to market access, the lack of procompetitive mechanisms, the need for comprehensive deregulation, and greater transparency. Systemic reforms of these economies through implementation of the IMF structural measures will only intensify the benefits of an already aggressive trade policy aimed at opening these markets.

I outline in some detail in my testimony the market opening measures that the administration with the Subcommittee have taken with respect to Japan, China, Korea, the other Asian economies, bilaterally, as well as in APEC and the WTO. And I also outline in my testimony the enforcement efforts we have undertaken with respect to the agreements we've negotiated—some 75 enforcement actions since 1993.

But let me turn, instead, for this last minute, to U.S. monitoring of the IMF packages themselves. Monitoring the implementation of the commitments made to the IMF is central to ensuring a reformed Asia. Only with full and faithful implementation will the causes of the immediate crisis be addressed and long-term stability restored. This monitoring will occur in several contexts, including through the IMF, the administration, U.S. industry, and the WTO. Let me take each in turn.

First, the IMF monitors and ensures implementation of the conditions in its stabilization packages through periodic reviews. A failure to adhere to the commitments may result in the withholding of disbursement of further funds. Even after full disbursement, evidence suggests very little backsliding on IMF commitments, and that's because countries don't want to jeopardize or impair their relationship with the IMF. Market pressures also effectively avoid a retreat from the commitments made because any such retreat could again erode investor confidence.

Second, the administration is coordinating its monitoring efforts. Specifically, USTR and Commerce have units charged with monitoring and implementation to ensure compliance with agreements made. It is through these units that we are actively monitoring compliance with the IMF trade-related commitments. The State and Treasury Departments are also actively involved. Through the Treasury representative to the international financial institutions, the administration will provide the information it collects on recipient country's implementation. We will be particularly sensitive to ensure that the credit the financial institutions provide to these countries is not being used to provide export incentives or subsidies, particularly those that are WTO inconsistent. Additionally, when the commitments made by a recipient country overlap with commitments it makes to the WTO or the OECD or in our trade agreements, we will use the means available in these traditional fora for ensuring implementation. The administration's continued pursuit of the WTO case concerning Indonesia's national car project is illustrative, as is our pending action against Korea Autos.

Third, we're working closely with the U.S. business community, both through our formal advisory boards and through the Commerce Department, to obtain the benefit of their experiences in the relevant countries.

And, last, the WTO has substantial existing mechanisms to compliment and reinforce IMF and administration efforts. I will be meeting with the director general of the WTO next week on this very issue. This comprehensive monitoring effort will help to ensure that the commitments made are fully and faithfully implemented.

Let me conclude by saying that the administration will continue to set an aggressive agenda for U.S. engagement in Asia through the twofold strategy of stabilization and broad structural and market-opening reforms. Financial stabilization is an inseparable objective from deregulation, transparency, and competition. IMF replenishment, broad trade negotiating authority for the President, and an insistence that Japan also undertake fundamental economic reform, stimulate domestic demand and open its market, remain our highest priority. In both the long run and in the short run, our approach recognizes that a strong global economy is fundamentally in the U.S. domestic interest.

Thank you, Mr. Chairman.

[The prepared statement follows:]

Statement of Hon. Charlene Barshefsky, U.S. Trade Representative

Thank you, Mr. Chairman, for this opportunity to discuss the implications of the financial situation in Asia for U.S. trade policy and the importance of rapid Congressional action on the Administration requests for a commitment for our IMF quota subscription and an augmented back-up facility, the New Arrangements to Borrow (NAB).

The starting point for a discussion about trade with Asia is necessarily very different than it would have been just six months ago. Today, we begin by asking how economies that have seen impressive economic growth for three decades could experience such economic difficulties so quickly? Is this the end of the Asian miracle? And, what does this mean for the United States?

By any measure the Asian economies have experienced a dramatic reversal of fortune. Countries which had high rates of growth over the past decade—7 to 10 percent annual growth in many cases—now face minimal or even negative growth in 1998, and perhaps beyond. The financial crisis has also resulted in a dramatic depreciation in the value of the currencies of many of these countries. Before turning to a discussion of the crisis, let me make a few preliminary observations.

First, the U.S. economy is strong—as strong as it has been in almost 30 years. Our ability to weather the storm in Asia is therefore better than at any time. U.S. employment is up 14.7 million jobs since the President took office; 3.3 million jobs in just the last twelve months. Importantly, interest rates have come down so significantly that American homeowners are re-financing their homes in record numbers, realizing significant purchasing power which otherwise would have been eaten up by mortgage payments. Real industrial production is up 28% since 1992, and 7.0% in just the last twelve months. Inflation is of little concern. Economic growth in the U.S., which has been remarkably robust, will continue in 1998, along with continued job creation.

Second, U.S. prosperity is in no small part the result of the export opportunities that we have created in Asia and around the globe, including those gained through the negotiation of some 245 trade agreements since 1993. Today, exports support an estimated 12.1 million American jobs. As President Clinton has said, the only way we can sustain our standard of living at home—as four percent of the world's population—is to sell our goods and services to those ninety-six percent of the consumers beyond our borders. Exports not only grow this economy, but shift the locus of job creation to higher wage jobs—employment supported by goods exports pay 13–16% higher than the U.S. national average wage.

Even in a period of sustained prosperity, however,—and to date, minimal impact from the Asian financial crisis—we cannot isolate ourselves from the global economy. In 1970, trade as measured in imports and exports had a value of about 13% of U.S. GDP. Today the value of our trade has reached the equivalent of more than 30% of our economic activity. Our economic interests demand that we continue to open foreign markets and lead in the global economy.

THE ASIA FINANCIAL CRISIS

As Treasury Secretary Rubin and others have noted, the causes of the Asian financial crisis are complex and multi-faceted. However, in each country and across the region, we find a common web—inadequate supervision of Asian financial institutions, speculative real estate and equity booms, excessively close ties between governments, banks and corporations. These relationships—and in some countries—a deep-seated resistance to competition, including open trade and investment practices, resulted in a misallocation of capital. Many investments that led to insolvency would never have been made under more competitive conditions. Investment flowed in as if on auto pilot, quadrupling in less than a decade, to expand capacity well in excess of current or projected global demand with no basis in market realities. The result was a fundamental mismatch between short term bank funding (fueled by foreign investment) and long term lending transactions for projects of dubious merit—a phenomenon Fed Chairman Alan Greenspan called a pattern of "conspicuous construction." This broad combination of factors proved combustible, as Secretary Rubin has said, and the consequences have played out in on-going front page news.

In response to the crisis, the IMF moved quickly to stabilize the economies and create the conditions for stabilized currencies in the affected countries. While these measures were taken to restore financial stability and promote an early return to sustainable economic growth, a stable Asia is also the single most important trade policy objective. The region is a principal U.S. customer, supporting millions of U.S. jobs. In 1997, Asia accounted for 28% of total U.S. exports. We cannot sell to Asia if Asians cannot buy. The IMF is, therefore, critical in trade terms for this most basic and fundamental reason. The immediate objective must be to stabilize Asian economies and create the conditions for stabilized currencies. Not doing so only further undermines our export opportunities and a return to sustainable Asian economic growth. Not doing so also puts additional pressure on our domestic industries that must compete with cheaper imports.

But, beyond this immediate and most critical objective, structural reform must be put in place to build a longer-term foundation for economic stability in Asia. The stabilization programs that the IMF is financing in Asia reflect this goal; they are more heavily focused on structural reforms than on adjustment to macroeconomic policies. Such reforms include measures to strengthen financial sectors, business-government linkages, improve transparency and open markets to foreign investment and reduce trade barriers.

The IMF concluded that microeconomic barriers to competition helped to worsen the financial problems. The seeds of the Asian financial crisis find their parallel in the trade realm. Structural reform leading to systemic change, including greater competition engendered by market opening measures, transparency, and economic deregulation all intersect with the broader goals of market stabilization.

It is thus not surprising that many of the structural reform components of the IMF packages will contribute directly to improvements in the trade regimes of these countries. If effectively implemented, these programs will complement and reinforce our trade policy goals. For all of these reasons, it is imperative that the IMF funding requests now before the Congress be approved as soon as possible.

Let me review for you briefly the broader systemic trade policy issues previously identified with respect to Korea and Indonesia and the intersection of these issues with IMF structural adjustment. I intentionally omit Thailand because, unlike Korea and Indonesia, misdirected trade policy and industrial promotion were not seen as among the primary causes of Thailand's economic crisis. Nonetheless, Thailand has made commitments to restructure public enterprises and accelerate privatization of certain key sectors—including energy, transportation, utilities and communications—which will enhance market-driven competition and deregulation. We expect these structural reforms to create new business opportunities for U.S. firms.

Korea

Korea is one of our most important markets: it is the fifth largest purchaser of U.S. products and the fourth largest purchaser of U.S. agricultural commodities. That said, Korea is one of the toughest places in the world to do business.

In Korea, the relationship between government, banks, and commercial enterprises resulted in a misallocation of capital to economic ventures of questionable merit, nonetheless deemed central to industrial policy goals. Under the Korean system, for example, banks provided preferential financing to industries judged to be of "strategic" importance regardless of internal or world market conditions.

Such misallocation of capital fueled the expansion of the chaebols into lines of business of dubious value, and into overproduction and excessive exporting of targeted industrial products, including autos, steel, semiconductors, and ships. This misallocation, in turn, exacerbated the market access problems in Korea and impeded U.S. companies' ability to sell products in third country markets.

Policy-driven, rather than market-driven economic activity, also meant that U.S. industry encountered many specific structural barriers to trade, investment, and competition in Korea. For example, Korea maintained restrictions on foreign ownership and operation, and had a list of market access impediments that included:

- import clearance and certification hurdles;
- restrictive import licensing procedures, particularly for agricultural products;
- anti-competitive practices, such as Korean industry associations controlling the entry and distribution of imports; and
- other barriers to market access, including in the financial services sector.

The Korea stabilization package, negotiated by the IMF in December 1997, should help to open and expand competition in Korea by creating a more market-driven economy. Korea is moving forward strongly and decisively to implement the IMF program. Korea still faces many challenges but, if it continues on the path to reform there will be important benefits not only for Korea but also for the United States. The incoming President Kim Dae Jung has demonstrated a strong commitment to market opening and economic restructuring that are at the heart of the economic reform program. We look forward to working with him in this effort.

The reforms will put a stop to government-directed lending for industrial policy goals, will ease restrictions on foreign investment, and will simplify licensing and certification requirements to allow greater competition from imported goods.

The IMF-directed restructuring of the Korean financial and corporate systems to make them more sound, transparent, and efficient already is addressing the systemic problem of government-prompted loans to non-economic uses, including those to the *chaebols.*

The financial sector reforms, coupled with tighter rules on corporate governance and transparency, will force banks to assess the creditworthiness of potential borrowers and their commercial viability. The banks are now under pressure to increase their capital asset ratios and thus, are unlikely to be an easy source of new financing for already overextended conglomerates. This, in turn, should provide incentives to scale back business lines and to tailor capacity, production, and export decisions to *market* cues.

Korea's agreement to liberalize foreign ownership rules should expose the Korean economy to more outside influence, thereby offsetting the Korean penchant for providing preferences to "strategic" domestic industries.

Furthermore, more specific, structural reforms in Korea's IMF package will complement the U.S. trade agenda by reinforcing and expanding upon Korea's commitments in the WTO and in the OECD. Specifically, Korea has agreed to:

- accelerate implementation of its commitments to WTO members on the elimination of trade-related subsidies and its import diversification program;
- bind in the WTO, the commitments it made in the OECD on financial sector market access; and
- liberalize its rules on import licensing and certification, which could help alleviate entry and distribution barriers for agricultural commodities, food, distilled spirits, and industrial products including autos, pharmaceuticals, and cosmetics.

In sum, the financial, corporate, and foreign investment conditions in Korea's IMF package, along with the specific trade-related commitments, should help to (1) improve market access in Korea, and (2) correct the overcapacity and aggressive exporting patterns of the Korean *chaebols.* Our companies will be better able to compete with their Korean competitors on a more level playing field.

Indonesia

Indonesia is also an important U.S. trading partner and was an export destination for approximately $4.5 billion in U.S. goods exports in 1997. But in Indonesia, too, market access for U.S. goods and services is limited by a host of barriers that distort competition.

U.S. trade policy concerns have centered on:

- Indonesia's "interventionist" automotive policies involving trade distorting subsidies and discriminatory tax and tariff benefits granted in exchange for meeting levels of local content;
- restrictions on internal distribution and retail marketing arrangements;
- excessive tariff levels on certain products;
- commodity import and marketing monopolies, domestic cartels, licensing and other non-tariff measures; and
- the national aircraft project.

Like the Korean stabilization package, the IMF stabilization program for Indonesia contemplates far-reaching changes to Indonesian policies and practices which, if faithfully implemented, should move the country in the direction of more open markets, transparency, and increased competition. Additionally, the package contains trade and investment provisions that go to the heart of some of the most vexing trade problems I just mentioned.

Key elements of the IMF program include:

- the immediate elimination of special tax, customs or credit privileges granted to the "National Car" project;
- implementation, ahead of schedule, of the WTO panel ruling on the National Car project and elimination by 2000 of tariff preferences tied to local content levels for auto producers;
- the immediate elimination of any budgetary and extra-budgetary support and credit privileges for the "strategic" national aircraft project;
- the removal of foreign investment restrictions on wholesale and retail trade by March 1998;
- the reduction of customs duties and border non-tariff measures on both imports and exports, including agricultural and food products;
- the elimination of local content requirements on dairy products;
- domestic market deregulation in the form of the elimination of commodity import and marketing monopolies for sugar, wheat, wheat flour, soybeans and garlic (leaving only rice so restricted);
- the removal of restrictive internal marketing arrangements for such products as cement, paper and plywood; and
- the removal of export quotas for cement, plywood, sawn timber, processed wood and the abolition of wood shipping cartels.

These commitments address practices that have long been the subject of this Administration's bilateral trade policy as reflected in the Administration's National Trade Estimates Report on Foreign Trade Barriers, which has identified many of the barriers that are addressed in the IMF package. Most notable in this respect is the commitment by Indonesia to eliminate the tax, tariff and credit privileges provided to the national car project. We have challenged this very program in the WTO. Additionally, the IMF program seeks broad reform of Indonesian trade and investment policy, like the aircraft project, monopolies and domestic trade restrictive practices, that stifle competition by limiting access for foreign goods and services.

Impact on the Trade Agenda

In the short term, the forces unleashed by the withdrawal of capital from the Asian markets, reflected in part in depreciating currencies and a slowdown in economic activity in the region, will of necessity, result in increased exports from the region and import contraction in Asia. Because the United States is today the strongest economy in the world, and the most open, we can expect a short-term increase in imports from the region and a decline in our exports. We will keep our markets open, but we need to see other countries respond by opening their markets and stimulating demand as well. In this regard, I will say more about Japan in a moment.

The expected short-term deterioration in the trade balance must not, however politically tempting, open the way to protectionism or isolationism. To go down this path would immediately undermine our primary goal which is to stabilize the immediate crisis. We would also jeopardize the real possibility of longer-term structural reform of these markets.

The U.S. has critical economic and national security interests in a stable and reformed Asia. The region is a principal U.S. customer, supporting millions of U.S. jobs. Beyond Asia, more than 40% of US exports go to emerging markets. Any further contagion effect of the crisis will only exacerbate the negative impact on our own domestic economic health. And, of course, our national security interests in

Asia are very well understood. Political, social, or economic instability in Asia will affect prosperity and security around the world. For these reasons, our broad national interest and the interests of American workers, farmers and businesses dictate that we adequately capitalize the IMF and participate in the New Arrangements to Borrow (NAB). Support for the IMF also sends the important message that America will continue to lead in the global economy, a message that is particularly critical today.

ADMINISTRATION'S ASIAN TRADE POLICY

The Clinton Administration has spent the past five years focusing considerable attention on the Asian markets: the substantial barriers to market access for U.S. and foreign goods and services, the lack of pro-competitive mechanisms, and the need for comprehensive deregulation and greater transparency. Systemic reform of the Asian economies through the implementation of the IMF structural measures will intensify the benefits of an already aggressive trade policy and it is to that policy that I will now turn.

The Administration has applied and will continue to exercise a full range of tools to achieve constructive market opening results in Asia through bilateral, regional, and multilateral means. Quite apart from but complementary to the IMF reform, new trade agreements and the enforcement of existing agreements play a part in a more stable and secure Asia. Let me briefly take each in turn:

We have a large array of bilateral agreements in Asia aimed at the goals of deregulation, market access and transparency.

Japan: We have negotiated 34 trade agreements with Japan under which we have achieved important and substantial market-opening results. From 1993 to 1996 exports increased by 41% to Japan, reaching in excess of $67 billion. The growth rate of exports to Japan over this period exceeded the still strong growth rate of U.S. exports to the world by nearly one quarter. In 1997, however, exports to Japan declined by 3 percent, while our exports to the rest of the world grew by nearly 12 percent. We are naturally concerned about this drop off in our exports to Japan. The Japanese economy which enjoyed a single year's growth spurt of 4 percent in 1996, fell back to a bare 0.6 percent increase in 1997 and, on current policies, is widely believed to be facing a growth rate well under one percent this year.

Japan, the second largest economy in the world, has an especially crucial role to play. We see the need for action in three areas. First, we strongly agree with the view of the IMF that fiscal stimulus is needed to support Japan's economy and to make it a potential source of confidence for the region. Second, it is crucial for Japan to act clearly and decisively to strengthen its financial system with an infusion of public money. Finally, it is equally important for Japan to deregulate financial and other sectors to open up the Japanese economy.

The U.S. cannot be the only engine of global growth or the sole buyer of goods to absorb the tremendous productive capacity of the Asian region.

The Administration has consistently sought a range of market access and deregulation measures to open Japan's market and spur domestic demand in Japan, and we will continue to do so. We have an immediate deregulation agenda with Japan affecting critical areas of the Japanese economy—financial services, telecommunications, housing, medical equipment and pharmaceuticals—where we are aiming for decisive action on the part of the Japanese government in the first half of this year.

China: U.S. trade policy has been geared to encourage China to establish the rule of law, open its economy to imports and investment, and reform its trading regime pursuant to the rules and obligations of the World Trade Organization. We have pursued a complementary policy that combines bilateral, regional (APEC) and multilateral trade initiatives. Embedded in our bilateral agreements—in particular a hallmark of the intellectual property rights agreements—are broader international norms to which China has committed: transparency of laws and procedures, access to administrative and judicial decision making, and curbs on the arbitrary exercise of administrative discretion. Each of our ongoing negotiations—in the context of the WTO and bilaterally, on services, market access and IPR—is also grounded in international norms and practices and in the necessity of adherence to a rules-based regime.

Taiwan: Last week we reached a comprehensive market opening agreement with Taiwan which will dramatically open Taiwan's markets to U.S. agricultural products, services, and industrial goods. U.S. farmers will see new markets for pork, chicken, and other meat products that have never been open to any foreign imports. U.S. exporters of industrial products will achieve levels of market access comparable to those available in other developed economies. And, Taiwan will provide broad access for the full range of services, including financial and telecommunications services. Once all members of the WTO have completed their bilateral market access negotiations with Taiwan, multilateral negotiations will ensue to work out the full range of rules-related commitments Taiwan must make to formally enter the WTO.

APEC: Regionally, we are pursuing initiatives that mark concrete progress toward the ambitious APEC goal set out in Indonesia three years ago to establish free and open trade across the Asia-Pacific region. We have launched a market opening agenda across 9 sectors of trade encompassing $1.5 trillion in global activity, including environmental goods and services, energy, medical equipment, scientific instruments, and certain natural resources products—all areas where the U.S. is a leading competitor. Six additional sectors are to follow.

We have established a working group on biotechnology trade to create scientific, timely, and transparent procedures for the licensing and importation of new agricultural products. We are also working with our APEC partners and others on a global electronic commerce initiative to expand Internet access and establish the principle of duty-free cyberspace.

WTO: Multilaterally, the conclusion of the Uruguay Round marked strong Asian participation. Recent achievements in the WTO sectoral agenda—global agreements on ITA, telecommunications and financial services—encompassing tens of trillions of dollars in trade could not have been realized without the strong participation of Asian countries. The ITA covers $500 billion in global technology trade. We are also pursuing "ITA II" to build upon last year's (December 1996) successful Information Technology Agreement, the completion of which was largely attributable to APEC leadership. Under the telecom agreement, a world-wide industry worth $675 billion today will double or triple in size within the next decade. And, the financial services package will open tens of trillions of dollars of opportunities in banking, securities and insurance. Together these agreements represent the foundation of the twenty-first century economy. The global agenda ahead is equally important: IPR, government procurement, agriculture and services.

We will also seek to expand the global trading system to include such major economies as China, Russia and Taiwan, and through the disciplines of the international trading system, including transparency and the rule of law, expand opportunities for U.S. goods and services in these markets.

Implementation of Existing Trade Agreements and Monitoring of IMF Obligations

At the center of the trade agenda is our commitment to monitor and enforce existing agreements. The United States has taken more than 75 enforcement action on behalf of our goods and services providers around the world. We have initiated more than 35 cases in the World Trade Organization affecting a broad range of industries. We have won or settled on favorable terms important cases against Japan on intellectual property rights and discriminatory tax policies. In Korea, we gained important reforms in agricultural shelf-life restrictions, import clearance procedures, and restrictions against telecommunications providers. In China, we have applied bilateral enforcement measures to achieve an unprecedented crackdown against IPR piracy and textile transhipments.

Our overall enforcement agenda has delivered dollars and cents results across the board for U.S. industries. As plaintiff in the WTO, our win-loss record is 17–1. And even in the Japan film case, in which we did not prevail, we will continue to push for aggressive market-opening reform, using as the baseline the formal representations made by the Government of Japan to the WTO about the operation of its film market.

Monitoring the implementation of the commitments made in the IMF stabilization packages is equally central. Only with full and faithful implementation of the commitments will the causes of the immediate crisis be addressed and long-term stability ensured. This monitoring will occur in several contexts including through the IMF, the Administration, U.S. industry, and the WTO. In this regard, recipient countries such as Korea have welcomed monitoring, as they can tolerate backsliding even less than we can.

First, the IMF monitors and ensures implementation of the conditions in its stabilization packages through periodic reviews; a failure to adhere to the commitments may result in withholding the disbursement of further funds. Even after full disbursement, experience suggests that there tends to be little backsliding on IMF commitments; countries do not wish to impair their relationship with the IMF. Market pressures also effectively avoid a retreat from the commitments; any such retreat could again erode investor confidence.

Second, the Administration is coordinating its monitoring efforts. Specifically, the existing USTR and Commerce units charged with monitoring and ensuring compliance with trade agreements are actively monitoring compliance with the IMF trade-related commitments. The State Department has instructed our Embassies to supplement these efforts in the relevant markets. Treasury Department and other Administration officials, including we at USTR, have intensified visits to the region. Through its Treasury representatives to the IFIs, the Administration will provide the information it collects on recipient countries' implementation. We will be particularly sensitive to ensure that the credit the IFIs are providing to the recipient countries' central banks is not being used to provide export incentives or subsidies, particularly those that are WTO-inconsistent, that would encourage exports from sensitive industries.

Additionally, when the commitments made by a recipient country overlap with its commitments in the WTO, OECD, or in bilateral trade agreements, the Administration will use the means available in these traditional trade fora for ensuring implementation. The Administration's continued pursuit of the WTO case concerning Indonesia's "national car project" is illustrative, as is our pending action against Korean autos.

Third, we are working closely with the U.S. business community, both through our formal advisory groups and through the Commerce Department, to obtain the benefit of their experiences in the relevant market.

Finally, the WTO has substantial existing mechanisms to complement IMF and Administration efforts. The various Committees that oversee the WTO Agreements along with the country-specific trade policy reviews will work to monitor changes in a country's trade regime. We will be working with the WTO not only towards effective monitoring, but also to explore ways to strengthen the relationship between the WTO and the IFIs.

This comprehensive monitoring effort will ensure that the commitments made are fully and faithfully implemented.

Conclusion

The Clinton Administration will continue to set an aggressive agenda for U.S. engagement in Asia through the two-fold strategy of stabilization and broad, structural market-opening reforms. Financial stabilization is an inseparable objective from deregulation, transparency, and competition. IMF replenishment, broad trade negotiating authority for the President, and an insistence that Japan also undertake fundamental economic reforms to stimulate domestic demand remain our highest priorities. In both the long run and the short run, our approach recognizes that a strong global economy is fundamentally in the U.S. domestic interest.

Thank you for the opportunity to appear before you; I welcome your questions.

Chairman CRANE. Thank you, Madame Ambassador. What will the role of the WTO be in monitoring compliance with the IMF package?

Ms. BARSHEFSKY. There are really two ways in which the WTO will become involved. One is that the WTO has a variety of Committees that monitor a country's implementation of the various commitments made. Those Committees will of course also look at the IMF-required commitments in that context. Second, the WTO undertakes periodic trade reviews of the countries that are members, particularly the major trading economies, including Korea. And through those reviews, the WTO will also become actively involved in the monitoring process.

I would add that there is a long and close collaboration between many of the international financial institutions and the WTO, and, most particularly, between the IMF and the WTO, and there will be further discussions between those institutions as to further efforts.

Chairman CRANE. In your view, how can the United States best pursue trade liberalizations in the countries affected by the Asian crisis? I'm bunching some questions here that are germane—and to what extent does the Asian financial crisis represent a setback to the prospects of trade liberalization in the region? And has the crisis already led to any backsliding on previously agreed-upon trade measures, especially in the financial services sector? And how patient should we be while these countries go through their recovery?

Ms. BARSHEFSKY. Thus far, we've not seen any backsliding by the Asian countries. They remain committed to the APEC process of opening further their markets in the 9 sectors designated. We see, for example, in the case of Korea, it has now agreed to go further in its WTO commitments in connection with financial services than it was willing to do just several months ago. And we think that's a very positive development.

These economies, I think, recognize that in order to build confidence and in order to restore growth, continued trade liberalization, and market openings, the introduction of competition and deregulation will have to proceed. It is painful, it is difficult, but these structural reforms are long in coming in many of these countries, and ultimately to the good.

Chairman CRANE. Thank you very much, and I now yield to our distinguished Ranking Member, Mr. Matsui.

Mr. MATSUI. Thank you, Mr. Chairman. I'd like to thank you, Ambassador Barshefsky, for your fine testimony today and obviously for being here.

I just have two general areas. One is—let me say this, in my opening statement which I submitted for the record, I support the entire $18 billion funding for the IMF. On the other hand, I do reserve the right, at any future time before the matter comes to the floor, to change my mind depending on how well the Asian countries meet some of the conditions that we and some of the other countries are laying out. I have to say that the Japanese, particularly, have not been forthcoming. Perhaps their economy and their government is a basket case at this particular time, but nevertheless, they have an international obligation, and you mentioned the three areas—fiscal stimulus, issue of market opening, and, certainly, the restructure of their financial system. Could you relate, if it's possible in an open meeting like this, how much progress they're making on all three of these areas? And do we have any expectation that by the time this matter is resolved in the Congress and with administration, in terms of the funding, that they will have reached satisfactory results on the conditions of these three areas, or do you feel that this is an ongoing situation with them?

Ms. BARSHEFSKY. I think the situation is ongoing. I can certainly make several comments, and I would suspect the Treasury panel that testifies later this afternoon might wish to make some comments.

With respect to the question of fiscal stimulus, Japan has applied some fiscal stimulus in the form of a one-time tax cut. While we applaud that measure, we find it to be inadequate to stimulate the economy to the degree needed, and for that reason, the IMF and we, as well as Europe and many Asian countries, have called for dramatic fiscal stimulus by the Japanese Government.

With respect to reform of its financial sector, there is a plan in place. With respect to the use of funds, there is some concern that has been expressed whether this will lead to financial sector restructuring, which is to say, will it lead to a cleaning up of the banking system, or will it simply protect not just depositors but also the banks, and that is something that is unfolding.

Third, with respect to deregulation, while Japan has undertaken from time to time some important deregulatory initiatives, we believe that its deregulation efforts to date have been inadequate, insufficient for the degree of deregulation needed, and to the extent that deregulation has occurred, it has not served the goal of further opening the Japanese market to an appreciable degree. We have a very broad deregulation agenda with the Japanese Government, and we look to them to achieve concrete progress on deregulation by the time of the G–7 summit in Birmingham, England, in the spring of this year.

Mr. MATSUI. Thank you. If I could just follow up on this, it's my understanding, as you stated, that they only intend to have a onetime tax cut, and almost every economist in the world that is involved with this issue thinks it must be a permanent or, at least, a multiyear tax cut for it to make any sense at all. In your discussions, and in the administration's discussions, do you see any progress in that area? Frankly, if it's just a one-shot deal, it probably won't have the kind of impact that's required if, in fact, they want to stimulate their economy.

Second, if I may just go on, in terms of their whole issue of deregulation, as you well know, it was about 3 years ago when you entered into and came up with a rather far-reaching market opening agreement with respect to autos and auto parts, and I understand that it isn't working particularly well now because it's the implementation that's creating this real problem for us. And certainly, I think you've stated the problem in terms of their lack of effort in the financial services area, even though they have a sizable sum of—what is it, $57, $60 billion, or in that range—it's going into the wrong area, and perhaps you can further discuss that because I frankly think if the Japanese aren't going to be forthcoming, whatever effort we make will probably not be enough because there has to be more than one engine, and that is the United States engine, to make this thing work.

Ms. BARSHEFSKY. Let me, if I can, comment on a couple of the items that you raised. Certainly, many countries have expressed to Japan that a one-time, relatively modest tax cut will not sufficiently stimulate the Japanese economy, and that remains our view. Whether Japan will be more forthcoming with respect to further fiscal stimulus, we have yet to see, but certainly Japan is well apprised of the views of the international community and of the United States.

With respect to autos and auto parts, Japan had undertaken some important deregulatory efforts which helped to create increased sales of vehicles as well as of parts. On the parts side, those sales remain relatively strong, although we have registered to Japan our deep concern that deregulatory efforts have slowed considerably. This is not acceptable, but I will say that exports of auto parts to Japan remain relatively strong.

It's on the vehicle side that United States exports have declined appreciably, by about 20 percent, and of course Japanese exports to the United States continue at a fairly high rate. We've long been concerned about the limited number of dealerships in Japan that carry foreign vehicles, and we're in the process of working with the Japanese Government on this now.

Mr. MATSUI. Thank you. If I may just very briefly turn over to the second area, and that is one of the concerns, I think, many of us have is to set a precedent—I know this has been discussed within the administration, so it's not like it's in our interest that we're discussing this—but it seems that there are two problems. One was that some really bad lending practices in some of the Asian countries occurred—very, very bad practices. And, second, obviously, some of the structural problems that these countries have had.

If, in fact, we lend assistance, and I agree strongly with your observation that it's in our interest to help and make this work, how are we going to prevent these problems from coming back again 3, 5, 10 years from now?

I think Mexico is a unique situation. I don't blame the Mexican Government. It was circumstances that put Mexico in the problem that they had, so when we gave them assistance in terms of shoring up their peso, it was an act that most people, I think, realize was in the interest of all countries, and very little blame should be put in that situation.

But in this case, it was clearly a case of Asian nations obviously watching out for its own interest by keeping their markets relatively closed, having an export strategy, and in addition to those bad loans which the people of their country benefited from, to some extent, to the loss of the rest of the world. How are we going to prevent this from happening again?

This is somewhat unprecedented given the shape and size of the world trading community today, but what I would hate to see is 3 or 4 years form now, another region of the world, perhaps even Asian countries themselves, coming back, saying, we need more from the IMF or the World Bank.

Ms. BARSHEFSKY. First off, let me start by saying, as you've reiterated as well, it is critical that we stabilize these economies, and stabilize the conditions for the currencies in these economies, and that we minimize, to the extent possible, the negative impact of this crisis on the U.S. economy.

Having said that, a number of commentators and you, now, have raised this issue of so-called hazard: If these countries are bailed out, will other countries just do this again and expect to be bailed out later? And let me make three general comments.

One is, these countries are taking a massive hit for their interventionist, industrial policy-driven lending practices, and for this very close and tight collaboration between governments, industries, and the banks. There is no question that the pain of adjustment that will be necessitated will be long remembered and itself will act as something of a deterrent force.

Second of all, as I said in my testimony, we intend to rigorously monitor the implementation of the commitments made to ensure that these countries in fact reform per the IMF prescriptions. That also sends a powerful message to other countries that they should not expect to be let off the hook for similar kinds of practices.

And last, as Secretary Rubin has said, the United States is itself working with its G–7 partners and other trading nations to determine what architectural changes are needed in the current international regime with respect to the international financial institutions so that there is burden sharing when a crisis of this sort happens, between government and the banks and private parties, and to ensure that stronger mechanisms are in place, including much better early warning devices, so that problems can be corrected along the way, not boil over to the extent we've seen here.

And I think in all those three ways, we should expect to see that this crisis will serve to dissuade any other such crises in the future.

Mr. MATSUI. Thank you, Ambassador Barshefsky.

Chairman CRANE. Ms. Dunn.

Ms. DUNN. Thank you very much, Mr. Chairman, and thank you again for your analysis of the problem. You do a great job, and I think we all appreciate the work you're doing on behalf of the country.

Ambassador, you mentioned and commented on the trade deficit and the fact that this crisis is going to exacerbate the trade gap, and I'm very concerned about that because I have some very, very good pieces on why a trade deficit is not a bad thing for our Nation—in a growth economy, we purchase more products.

I would like to know what the administration thinks about this. Is this a bad occurrence? And if you agree that a deficit is not the worst thing in the world, how will you plan to educate the public on this?

Ms. BARSHEFSKY. I think you're asking the $54,000 question with respect to educating the public. The extent of our trade deficit now and the fact it might increase is not an adverse reflection on the strength of the U.S. economy or on our competitiveness, and this contrasts quite sharply with the situation in the mid- and late-1980's where our fundamental competitiveness was called into question. We were also still running very high budget deficits at that time.

We have here a trade deficit which is the excess of investment over what we save. We are pulling in capital at an enormous rate in this country. Most of that capital is going into productive enterprise rather than real estate; that's to the good. And when we are joined in capital of this amount, we will run a corresponding trade deficit, that's simply how the numbers work. It is not a cause of concern. It is instead, at this period especially, a demonstration of how strong this economy is relative to that of our trading partners which have seen very sluggish growth and, as we see in Asia, investment in nonproductive, speculative enterprises. That is to say, a misallocation of the savings of its own people.

Educating the public on this is difficult because it is not intuitive that a trade deficit, given the economy that we have, is not of particular concern. It's not intuitive to people that trade deficits are largely a function of macroeconomic factors and have relatively little to do with trade policy or with trade agreements. To put it another way, trade agreements are particularly helpful to those sectors in which agreements are negotiated. We've seen this time and again, including in Japan where trade agreements tend to open up sectoral opportunities that were not available before. But even if you put all those sectoral opportunities together, they don't really move the aggregate numbers that much. They are important to the industries, important to the workers, important to the jobs they create, but don't move the aggregate balances that much because those aggregate balances are a function of factors totally different from trade policy or trade agreements. That message needs to be carefully articulated and formally articulated, or else, instead of the right policy prescriptions for what economic problems we do have, we end up barking up the wrong tree.

Ms. DUNN. And I hope that's something the administration will take advantage of and use its bully pulpit to let people know.

Thank you.

I wanted to ask you, too, I've heard talk about building confidence, I think you've used this term yourself, in the Asian economy, and today we'll hear testimony about how the administration is proposing to build that confidence, and that is, of course, additional funds to the IMF.

Ms. BARSHEFSKY. Yes.

Ms. DUNN. There is another way, and that is U.S. trade policy, so I'm interested in your evaluation on how U.S. trade policy can also play a role in building that confidence.

Ms. BARSHEFSKY. I think confidence is enhanced as these countries embrace market economics, as they embrace competition, as they embrace deregulation, as they embrace a series of economic policies that are market driven, not crony driven. And trade policy can move these countries in that direction, whether through sectoral reform and trade agreements, or through the APEC process where together we agree to open up markets further and reduce certain barriers, or through enhanced commitments or accelerated commitments in the WTO.

Confidence is restored when these markets operate on a transparent, on a knowable basis. That has not been the case in many of these countries, but confidence can certainly be restored to the extent that these countries embrace the kind of transparency and competition that has helped our own economy grow to this tremendous extent.

Ms. DUNN. Thank you, and last, a specific question on Korea. I've been told there are lots of United States companies which are in the motion picture industry, who are ready to revitalize and expand the commercial film sector in Korea, as they have in other Asian countries, but they cannot proceed until Korea lifts the quotas it now has that require Korean films be shown 146 days out of the year. As you have reported in your most recent assessment of foreign trade barriers, this requirement imposes artificial limitations on commercially attractive film series and films, and it serves as a deterrent to the construction of cinema theaters, which we think is needed to expand the distribution in Korea. Has any effort been made to alter or eliminate the government of Korea's screen quotas or to help the government in understanding the effects of such policies on foreign investment?

Ms. BARSHEFSKY. We have had quite extensive discussions with Korea on the issue of screen quotas. The industry has been very active, including in demonstrating to the Koreans by reference to other countries that when these quotas are lifted, you tend to see actually an increase in activities among the home countries indigenous film producers as well. There tends to be a rather creative boost in energy occasioned also in part by joint venture arrangements that tend to arise when things like screen quotas are lifted. We continue to work with our industry on this important issue, and it is one we will keep on the front burner with Korea.

Ms. DUNN. Thank you, and you receive our appreciation. Thank you, Mr. Chairman.

Chairman CRANE. Mr. McDermott.

Mr. MCDERMOTT. Thank you, Mr. Chairman. Madame Ambassador, I just got back the latter part of January from Japan at which time the Japanese opposition party had closed their doors and folded up, and so you essentially have LDP and a few small parties. And one of the things, I think, the Subcommittee and I would benefit from is understanding your perspective on why it is that the Japanese to a larger level have this need for a stimulus package for their economy.

You look at the United States when we used to go over there and get lectures on our competitiveness and our savings rate and other things, we don't hear that anymore when you go to Japan. You look at Korea where the new prime minister is responding to this crisis very strongly, but you look at Indonesia where it's very unclear whether they're going to respond to what needs to be done. Why is Japan, which is such a large economy, why are they not responding more adequately?

Ms. BARSHEFSKY. I think that's a difficult question to answer. Certainly, I would expect that if it were the Japanese Government here rather than me, they would indicate to you they have responded. And they might indicate they would consider further response at an appropriate time, but they would not delineate what that further response might be or when the time might be appropriate.

Japan has for some time focused on what it views as perhaps one of the most important social policy problems, and that is an aging population. It is loathe to engage in deficit spending. It wishes to shore up its economy in a way that can handle an aging population, and this has been a priority for Japan now for some time. It is further a priority that Prime Minister Hashimoto has underscored at every opportunity.

Beyond that, it is hard for me to comment, except to say that as the world's second largest economy, as an economy that holds the majority of global savings, Japan is most assuredly in a position to do much more than it is doing now. We see a significant rise in its global current account surplus at a time when other countries are baring the burden. That is simply not right, and Japan needs to do more.

Mr. MCDERMOTT. The natural followup question to that is, What kind of levers do we have to, I suppose the strongest word we'll use is, encourage them to take a more active role as the second largest economy in the world? It seems as though the mentality is one that says, we're worried, and yet they are the second largest economy in the world. What avenues do we have besides sitting at the table and saying, You ought to do better.

Ms. BARSHEFSKY. As you know, the administration has let its views be known to Japan in very strong terms. Secretary Rubin, Secretary Albright, Secretary Cohen, and others, including myself, have underscored to Japan the necessity for action.

What is significant most recently, is that Europe has come forward and has said to Japan that it is simply not in a position to absorb increased Japanese exports, particularly in light of Japan's failure to further deregulate and open its economy. Other Asian countries have communicated to Japan that it must open its markets and be a buyer, a purchaser of first resort for the Asian countries that, after all, live in its neighborhood.

This is very unusual. That is to say, to have an emerging global view that Japan is not doing enough. You'll recall over the years it is typically the United States that has let its views with respect to the Japanese economy be known, often to the disagreement by Europe or other Asian nations. This is a unique situation that we have now and one that we hope can create sufficient pressure on Japan to move forward in a more constructive manner.

Mr. MCDERMOTT. The other part of the Asian puzzle that you've not commented on very much is the Chinese. The Chinese have so far not devalued their currency. Where do we stand with respect to recognizing that as being a responsible participant in the global economy, and how does that affect our view about whether or when they get into the WTO?

Ms. BARSHEFSKY. Certainly, we think that the actions of the Japanese Government in not devaluing——

Mr. MCDERMOTT. You mean the Chinese Government?

Ms. BARSHEFSKY. The Chinese Government. I'm sorry. The actions of the Chinese Government in not devaluing its currency are very constructive and very positive, and the representations and commitments that it has made are extremely encouraging in that regard. China, of course, faces its own difficult problems, particularly in connection with state-owned enterprise reform and in connection with banking reform. China's banks hold an awful lot of bad debt, much of which is from poorly performing state-owned enterprises. China is now undertaking some banking reform, moving more to a federal-type system, trying by that to separate financial lending decisions from the authority of provincial governments so that those lending decisions are less politicized than they otherwise would be. As you know, China has also embarked on a fairly massive reform of its state-owned enterprises—that's the good news. The news of concern is that they may also be moving to a chaebol-type system, that is moving to a system that given a weak financial underpinning, has now been largely discredited. We will obviously be watching that.

With respect to its WTO accession, that accession has to stand or fall on its own merits. We have made, I think, some important progress with China on it, particularly in the case of goods, market access, as well as certain other WTO rules. We have a long way to go with respect to additional market access issues including services and agriculture, and with respect to additional rules commitments. We would like to see China in the WTO, but the terms have to be the right terms. We're not there yet, but we're working with them.

But that accession will rise or fall on its own, and is not in any way bound up with the question of state-owned enterprise reform or financial reform in China, or with their commitment with respect to their own currency.

Mr. McDERMOTT. May I ask one other question which is a little bit, maybe, off the point but not exactly. One of the criticisms of the African trade bill is that the textile people say that because of the Asian crisis, all of this textile production in Asia is going to move to Africa and it will be used as a transhipment point. What is your view of the Asian crisis in terms of what it does to the textile market, generally?

Ms. BARSHEFSKY. As you know, we have in place quotas for most of the major textile exporting, producing, and exporting nations, including two quotas among the African countries, Mauritius and Kenya. Those quotas are fixed. There are growth rates that will mean that we don't expect to see a surge of textile exports or apparel exports from Asia.

With respect to the question of transhipment, we have, I think, strong rules in place, as does our customs service. On the question of transhipment, particularly where there is a question of circumventing quotas. We will keep a sharp eye.

Mr. McDERMOTT. Thank you.

Chairman CRANE. Thank you. Just on quickie followup on that. Do you feel confident, because I've had the same input that Jim was just referring to, about transhipment through African countries? We're going to be bringing the African trade bill up tomorrow before our Full Committee, and I know there are other colleagues that are worried about the supervision of any effort at transhipment from Asian through expanded African country opportunities. Can we monitor that?

Ms. BARSHEFSKY. I think we feel very good about the transhipment rules and procedures that are currently in place, and of course, let me just add that the bill could always be clarified to ensure that transhipment is not an acceptable outcome. I think we feel pretty good about where we are right not.

Chairman CRANE. Very good.

Mr. Nussle.

Mr. NUSSLE. Thank you, Mr. Chairman. And I want to thank you, Ambassador, for your testimony today and most especially for the clarity of your testimony. I've had a chance to speak to a number of different experts on the topic of what is happening over in Asia with our Asian markets and I complement you on the clarity of your comments and the matter-of-factness. You don't pull any punches, you never have, and I, for one, appreciate that.

I would like to be parochial for a moment on the issue of agriculture. There's going to be a witness testify later on today on another panel who represents the Farm Bureau in Mississippi, and while I'm not familiar with agriculture in Mississippi, I think his comments are very pointed and actually over the last 24 hours or so, may be even outdated, which is what concerns me.

He says the Asian-Pacific region is becoming the most important growth market, as well as one of the major economic regions of the world, particularly in agricultural. In 1996 the total trade across the Pacific was estimated to be more than 75 percent greater than that across the Atlantic. He goes on to say the Asian market accounts for over 40 percent of our agricultural exports worldwide.

This totaled over $23 billion in export sales in 1997. I know you're familiar with these figures, but I wanted to amplify one point in particular. He says that current USDA estimates show that a reduction of $500 million in sales to Asia so far this year, the total impact may exceed $1.5 to $2 billion before the crisis is over. And just today in a local paper back home in Iowa, it was reported through the U.S. Department of Agriculture that U.S. agricultural exports will fall $2.5 billion below projections made only a few weeks ago for 1998, and the drop is obviously largely a result of the worsening Asian crisis. Corn and pork will be, probably, the major commodities to suffer.

What I'm getting at here, and you mentioned it in your testimony, are two things. One is, Could you please amplify for myself and my constituents the concerns for agriculture in this crisis, number one. And number two, what, if anything, we can do about that, either from an administration standpoint or from a congressional standpoint. What is the impact and what can we do about that?

Thank you.

Ms. BARSHEFSKY. I think we don't yet know fully the impact except to say that we know as a general matter, exports will decline to Asia as those economies contract sharply, and as their currencies have depreciated, making imports into those countries very expensive. We know also that agricultural exports will fall. The extent of the fall is very, very difficult to estimate and the reason for that is, we aren't yet sure what the full extent of the slowdown in the Asian economies will be; we're not sure fully of the effect of the depreciation of the currencies; we are not sure how quickly these economies will turn around and will begin to recover.

We know, generally speaking, that as we look at an increase in our trade deficit, the deficit will increase more because of lowered export performance than it will because of increased imports. But I would simply caution that it is very difficult to predict at this juncture the extent of the shifts in the trade balance, including in agriculture.

What can we do? Number one, stabilize these economies and the currencies. If the economies don't stabilize, if the currencies further depreciate, that will simply further decrease our export opportunities; it will increase the price of our goods, including agricultural products, that we send to Asia. So step one, as I said in my testimony, the most important trade goal arising from the Asian crisis is precisely the goal of the IMF which is to stabilize the economies and to stabilize the currency condition in these countries.

Second, we have to continue to pursue bilateral market-opening agreements with these countries, including in the agriculture sector. The APEC process will help as we look at commodities like fish, but apart from that, we've just concluded a further market access agreement with the Philippines on pork. We have just concluded, last Friday, a very comprehensive market access agreement with Taiwan, which will form part of its eventual WTO accession. It covers industrial goods, government procurement, services, and agriculture. And in the agriculture sector, we will gain immediate, upfront access beginning now, with respect to pork, poultry, and beef. We'll also gain market access for rice, as well as, of course, for a number of other agricultural commodities we export to Taiwan. These are areas where we've had problems in the past which this agreement will now rectify. We will continue to pursue those market-opening agreements, and we intend to do just that.

Mr. NUSSLE. I thank you for that, and part of the struggle for all of us, I think, is that this is such a complicated issue for so many, including me, including all of us, to understand and get our arms around, often times when you're out getting ready to plant this spring and you're not really sure how it impacts you, every once in awhile it helps to amplify that. And I'm glad one of the things you mentioned in your testimony was that this expected short-term deterioration of the trade balance must not, however, as politically tempting as it may be, open the way to more protectionism or isolationism. I would agree with that and I hope that this continues to be a lesson for more work in the area of expanding trade and not—and recognizing that interdependence that we have, and not pull back. So, I appreciate your comments today and I'll try to continue to educate my constituents as to the impact this has, and we'll work together to try to get this done, so, thank you.

Ms. BARSHEFSKY. Congressman, may I add one further point which is, as you may be aware, USDA has also begun to utilize export credits with respect to the purchases of agricultural commodities, particularly from Korea or by Korea, I should say. That is yet another way to try to minimize the adverse impact on agriculture of the Asian financial crisis.

[The following question was submitted by Congressman Houghton and Ms. Barshefsky's response follows:]

Question. I understand that the GSP Subcommittee is developing a recommendation on whether to grant various Russian government petitions to extend GSP (duty free) treatment to imports to Russian wrought and unwrought titanium products. What is the status of the review?

Answer. Last October we held a hearing on all of the petitions for changes in GSP eligibility that were accepted for the 1997 GSP Products Review. The titanium petitions were the subject of much discussion to both supporters and opponents. In addition, we received many prehearing and posthearing briefs.

The U.S. International Trade Commission (USITC) prepared a report on the probable economic impact of taking the action requested in the petitions. Public comments on this advice were received in January. The GSP interagency committee is reviewing all materials relating to the titanium petitions prior to my submitting recommendations to the President.

The President will announce his decisions in May. They will take effect on July 1, 1998.

Mr. NUSSLE. Thank you, very much. Thank you, Madame Chairwoman.

Chairwoman DUNN [presiding]. Thank you very much, Mr. Nussle. And thank you, Madame Ambassador. As the Chairman mentioned earlier, we're going to take our next panel out of order so we'd like to call to the table Fred Bergsten who is director of the Institute for International Economics and John Sweeney who is a policy analysis at the Heritage Foundation.

We're not finding our next set of witnesses here, so we'll declare a recess for one-half hour. We'll meet here again at 12:35.

[Recess.]

Chairwoman DUNN [presiding]. We're going to continue our panels this morning. We have John Sweeney who is a policy analyst for the international trade and economics with the Heritage Foundation. And we also have with us Michael Gadbaw who is vice president and senior counsel for international law and public policy with the General Electric Co. and chairman of the US-Indonesian Business Committee, the US–ASEAN Business Council, on behalf of the US–ASEAN Business Council and the National Foreign Trade Council. And, gentlemen, if you will forgive us, you are being thrown together because you are here, and we are eager to hear what you have to say. As you understand, we have a continuation of the previous plan at 1 o'clock, so we are eager to hear your testimony, ask you a few questions, and then I'm sure you will be happy to be excused at 1 o'clock. So why don't we begin the testimony with Mr. Sweeney.

STATEMENT OF JOHN P. SWEENEY, POLICY ANALYST, INTERNATIONAL TRADE AND ECONOMICS, HERITAGE FOUNDATION

Mr. SWEENEY. Madame Chairwoman, thank you very much for the invitation to testify today before this congressional Subcommittee. I'm not going to speak about the IMF, I think there's plenty of people who can talk for and against that issue. I want to talk about U.S. trade policy in the context of U.S. trade issues.

First, the United States economy is not showing many signs of slowing down despite the deepening financial crisis in countries like South Korea and Asia. Many economists, including the WEFA group, however, feel that the United States economic growth may still slow to below 2.5 percent if the Asian economies do not recover quickly, and if they're recovery is more dependent than currently expected on trade adjustments with the United States.

I believe American policymakers should be cautious about assessing the probable global economic aftershocks of the Asian financial crisis until better information becomes available. Nevertheless, some general observations can be made about the evolution of the Asian crisis during 1998 and how this may impact on global trade patterns. First, we believe the Asian crisis is a long way from being over. United States policymakers should pay close attention to political developments in Indonesia where the danger of ethnic violence has increased dramatically in recent weeks. Some 40 Indonesian towns have already experienced rioting and looting. A social and political explosion in Indonesia could easily spill over to neighboring Singapore and Malaysia.

United States policymakers should also follow developments in Japan now in its seventh consecutive year of very sluggish economic growth. Many Asian countries will be in recession during 1998 and 1999. We believe real GDP growth for the Pacific region, excluding China, will be close to zero in 1998, with Thailand, Indonesia, and South Korea experiencing declines of between 2 percent and 6 percent. Growth in 1999 for this area is rejected at less than 3 percent.

We see the Asian crisis lowering expectations for growth worldwide, nevertheless, fears that the economic slowdown in Asia may lead to a deflationary recession in the rest of the world are clearly exaggerated. Based on purchasing power parity evaluation, developing Asia, as a whole, accounts for about 22½-percent world output according to the WEFA group. However, excluding China and

India which, so far, have remained relatively immune from the Asian currency crisis, the rest of developing Asia accounts for only 7.3 percent of global GDP and only 4.4. percent of world exports of goods and services. This suggests that even a severe recession in the most effected Asian economies should have a relatively modest impact on global economic growth. Asia will be severely affected by a credit crunch, however, and this, in turn, will affect growth expectations in Latin America, particular in Brazil and Argentina. We see world economic growth in 1998 and 1999 slowing to around 2.6 percent and 2.9 percent, respectively, from over 3 percent in 1997, and we see growth in Latin America declining from about 5 percent last year to between 3 and 3½ percent in 1998 and 1999, respectively. Lower international commodity prices plus increased competition from Asian exports will have some negative impact on Latin America's terms of trade.

We see United States exports to Asia falling by at least 10 percent this year compared to last, while United States imports from Asia, including Japan, will increase. However, while the U.S. trade deficit will undoubtedly increase above the level $133.7 billion reported for last year, we do not believe the deficit will climb as high as $200 billion as some critics have warned.

Our greatest concern is the possible response of United States policymakers to the Asian crisis. Following last November's congressional defeat of President Clinton's request for new fast track negotiating authority, it is quite clear that American trade policy has stalled, and we are concerned that this paralysis may continue for the foreseeable future as opponents of free trade in the United States utilize the Asian crisis as an excuse to continue chipping away at America's global economic leadership.

America today is the largest exporter of goods and services in the world. Last year, we exported over $933 billion in goods and services and more than 20.5 million owe their job to these exports. America's trade deficit which is always the subject of great concern to Congress is minuscule when compared to the size of the U.S. economy which, adjusted for inflation, totaled $7.1 trillion last year. In contrast, the goods and services deficit of $133.7 billion for last year amounted to barely 1.85 percent of GNP, and that's roughly 18 cents for each $1 million of GNP.

Now, what should the United States be doing in terms of helping Asia and, more importantly, helping America. We need to get America back on the road to free trade. Specifically, we need to renew the executive's fast track negotiating authority. Without such authority, the United States is not a player anywhere in the world—not in Latin America, not in Asia, not in Europe—and without such authority, our ability to influence other governments, other countries like those in Asia currently in crisis, is severely curtailed and limited. Second, we do need to support the accession of the People's Republic of China and Republic of China and Taiwan to the World Trade Organization on a commercially viable basis. Third, we need to demand an end to China's practice of forcing foreign firms to transfer technology as a condition of investing. We need to expand NAFTA to Chile and other countries. And, most importantly, I feel, here in the United States, Congress needs to undertake a process of upgrading the capacity of U.S. Federal agencies to compile and report trade data at the national, State, and local levels. Such capabilities no longer exist. They have been defunded progressively over the last 4 years, and today it is nearly impossible to accurately gauge what we are accomplishing in trade in terms of exports, in terms of jobs, and how our congressional districts are faring.

Thank you.

[The prepared statement follows:]

Statement of John P. Sweeney, Policy Analyst, International Trade and Economics, Heritage Foundation

The U.S. economy is not showing many signs of slowing down despite the deepening financial crisis in countries like South Korea and Asia. However, the extent to which the American economy's growth may slow eventually depends on how quickly the Asian economies recover, and on how much their export prices fall. Many economists, including the WEFA Group, feel that U.S. economic growth could still slow to below 2.5 percent if the Asian economies do not recover quickly, and if their recovery is more dependent than is currently expected on trade adjustments with the United States.

Many economists expect that the steep devaluations Asian currencies have suffered since mid-1997 will led to a rise in U.S. imports from Asia and a slowdown in U.S. exports to Asian markets, resulting in a steep increase in America's trade deficit. However, while a higher U.S. trade deficit can be anticipated in both 1998 and 1999, many U.S. importers who expected bargain prices on goods from countries like Indonesia, Malaysia and South Korea are seeing absolutely the opposite effect from what they expected. In Indonesia, for example, apparel manufacturers are seeing their production costs skyrocket because their devalued currency not only makes imported fabric more expensive, but also inflates the repayment cost of loans they borrowed in dollars months ago before their currencies melted down.

While this situation involving Indonesian apparel producers may not hold true in the coming months for all Asian countries exporting goods to the United States, it does suggest that American policymakers should be cautious about assessing the probable global economic aftershocks of the Asian financial crisis until better information becomes available. Nevertheless, some general observations can be made about the evolution of the Asian crisis during 1998 and how this may impact on global trade patterns:

- The Asian crisis is a long way from being over. U.S. policymakers should pay close attention to political developments in Indonesia, where the danger of ethnic violence has increased dramatically in recent weeks. Some 40 Indonesian towns have already experienced rioting and looting. A social and political explosion in Indonesia could easily spill over to neighboring Singapore and Malaysia.
- U.S. policymakers also should follow developments in Japan, now in its seventh consecutive year of very sluggish economic growth. Although Japan is America's second largest trading partner as well as the linchpin of Asia's eventual economic recovery, the Japanese government has been exceedingly timid in terms of sorting out the crisis in Japan's financial system, and in exercising its regional economic leadership.
- Many Asian countries will be in recession during 1998 and 1999. Real GDP growth for the Pacific region (excluding China) will be close to zero in 1998 with Thailand, Indonesia and South Korea experiencing declines of between two percent and six percent. Growth in 1999 is projected at less than 3.5 percent.
- The Asian crisis will lower expectations for growth worldwide. Nevertheless, fears that the economic slowdown in Asia may lead to a deflationary recession in the rest of the world are clearly exaggerated. Based on purchasing power parity valuation, developing Asia as a whole accounts for about 22.5 percent of world output, according to the WEFA Group. However, excluding China and India, which so far have remained relatively immune from the Asian currency crisis, the rest of developing Asia accounts for only 7.3 percent of global GDP and only 4.4 percent of world exports of goods and services. This suggests that even a severe recession in the most affected Asian economies should have a relatively modest impact on global economic growth.
- Asia will be severely affected by a credit crunch, however, and this in turn will affect growth expectations in Latin America, particularly Brazil and Argentina. World economic growth in 1998 and 1999 is likely to slow to around 2.6 percent and 2.9 percent, respectively, from over 3 percent in 1997. Growth in Latin America should decline from about 5 percent in 1997 to between 3 percent and 3.5 percent

in 1998 and 1999, respectively. Lower international commodity prices, plus increased competition from Asian exports, will affect some negative effect on Latin America's terms of trade.

- U.S. exports to Asia will fall by at least 10 percent this year, compared to 1997, while U.S. imports from Asia (including Japan) will increase. The drop in U.S. exports to Asia could shave about 0.3 percentage points off America's GDP growth for 1998. However, while the U.S. trade deficit will undoubtedly increase above the level of $113.7 billion recorded in 1997, we do not believe the deficit will climb as high as $200 billion, as some critics have warned.
- Our greatest concern is the possible response of American policymakers to the Asian crisis. Following last November's congressional defeat of President Clinton's request for new fast track negotiating authority, American trade policy clearly has stalled, and we are concerned that this paralysis may continue for the foreseeable future as opponents of free trade in the United States utilize the Asian crisis as an excuse to continue chipping away at America's global economic leadership.

FREE TRADE BENEFITS THE AMERICAN ECONOMY, WORKERS AND CONSUMERS.

America has grown into an industrial giant partly because of international trade, which now accounts for nearly one-third of the national wealth.[1]

With increased reliance on global markets, the U.S. is trying to expand its exports by involving itself in agreements such as the North American Free Trade Agreement (NAFTA), and both global and regional trading organizations such as the World Trade Organization (WTO) and the Asia Pacific Economic Cooperation (APEC) group.

While America has been largely a free-trade nation, the principles of free trade today are under siege. On one side of the argument are those who advocate free trade because it creates jobs, promotes economic growth, and maximizes efficiency and individual wealth. On the other are those who argue that free trade forces American manufacturing overseas, and leads to lost jobs in the United States, declining wealth, and increased national suffering.

Proponents of free trade believe that free trade promotes economic growth and creates jobs for Americans. Virtually all economists argue that free trade increases competition, spurs innovation, lowers prices, accelerates economic growth, and on balance creates more jobs than are lost to foreign competition.

Opponents of free trade advocate closed borders and argue that cutting off or restricting trade with other nations is in America's interest. While they admit that tariffs and import quotas raise consumer prices, they believe that such measures also safeguard American jobs.

The outcome of this debate is vitally important to America's future. The choice before the U.S. is whether to continue or abandon its standard of living and its position as the world's leading economy. A false move on the trade front could have disastrous consequences for the U.S. economy. It should be recalled that the protectionism of the 1930s was a major factor in bringing about the Great Depression.

The challenge for America is whether it will embrace free trade as a key to its continuing prosperity. Linked to this challenge are such issues as expanding NAFTA to include Chile and other countries, expanding free trade in Asia through APEC, expanding trade across the Atlantic with Europe, and dealing with the entry of the People's Republic of China (PRC) and Republic of China on Taiwan (ROC) into the WTO. Generally, free traders have been disappointed in President Clinton's handling of all these trade issues. They accuse him of dragging his feet on expanding NAFTA to include Chile, and of trying to force "managed" trade deals with the Japanese over auto parts.

THE FACTS

- America is the largest exporter of goods and services in the world. It exports over $933 billion in goods and services each year, and over 20.5 million Americans are employed in producing these exports.
- One out of every five American workers owes his or her job to international trade.
- America's trade deficit is minuscule when compared to the size of the U.S. economy, which—adjusted for inflation—totaled $7.19 trillion in 1997. In contrast, the goods and services deficit of $113.7 billion for 1997 amounted to only 1.85 percent of the U.S. gross national product (GNP), or roughly 0.18 cents for each $1 million of GNP.

[1] Exports, plus imports, plus earnings on U.S. foreign investments.

• The U.S. trades more with Asia than any other region in the world. U.S. two-way trade in merchandise goods with Asia was over $738.8 billion in 1997, or nearly 47.5 percent of total U.S. two-way merchandise trade worldwide. Merchandise exports to Asia support over 6.54 million American jobs.

• Japan is a big customer for the U.S. manufacturing industry.Over 60 percent of U.S. exports to Japan are manufactured goods, and Japan's purchases of these goods support nearly 1 million American manufacturing jobs. Two-way merchandise trade between the U.S. and Japan totaled $187.2 billion in 1997, including $65.6 billion in U.S. exports of merchandise goods to that country, which supported over 1.44 million American jobs.

• The Western Hemisphere is America's second-largest export market, after Asia. From 1990 to 1997, U.S. exports of merchandise goods to all countries in the Western Hemisphere—including Canada—more than doubled from $137 billion in 1990 to over $285.8 billion in 1997. In all, U.S. goods exports to all Western Hemisphere countries during 1997 supported over 6.28 million American jobs.

• Latin America's economies are among the fastest-growing in the world, and the United States has been one of the principal beneficiaries of this growth. Between 1988 and 1997, U.S. goods exports to Latin America tripled, rising from $46.4 billion in 1988 to over $134.4 billion in 1997. U.S. exports of merchandise goods to Latin America supported more than 2.95 million American jobs in 1997.

• Since NAFTA went into effect on January 1, 1994, total growth in North American trade has surpassed even the most wildly optimistic forecasts, rising from $293 billion in 1993 to over $475 billion in 1997, an increase of $182 billion or 62 percent in just four years. Two-way merchandise goods trade between the U.S. and Canada totaled $318.16 billion during 1997, including $151.4 billion in U.S. goods exports which supported over 3.3 million American jobs. Moreover, two-way merchandise trade between the U.S. and Mexico during 1997 totaled $157.29 billion, including $71.3 billion in U.S. merchandise goods exports which supported over 1.56 million U.S. jobs.

The expansion of free trade and investment in the Western Hemisphere, Asia and Europe has been the core foundation of U.S. foreign policy since the end of World War Two. U.S. trade policy has advanced American economic interests around the world on four parallel tracks, including 1) unilateral initiatives such as the Generalized System of Preferences (GSP) and Most Favored Nation (MFN) status for eligible countries; 2) bilateral initiatives through agreements such as the U.S.-Israel Free Trade Agreement of 1985, the U.S.-Canada Free Trade Agreement of 1988, and the North American Free Trade Agreement (NAFTA) with Mexico in 1992–1993; 3) regional initiatives such as the Free Trade Area of the Americas (FTAA) in the Western Hemisphere and the Asia Pacific Economic Cooperation (APEC) group in Asia; and 4) multilateral initiatives at the level of the World Trade Organization (WTO), which was created in January 1995 by the Uruguay Round trade agreements.

The overarching goal of these American trade initiatives has been to liberalize trade and investment flows around the world by eliminating tariff and non-tariff barriers to trade as quickly as possible; to establish free-market and open trade policies with appropriate regulatory frameworks as the standard benchmark for all countries engaged in international trade; and to propagate American values of freedom and capitalist democracy around the world. The degree to which the U.S. has succeeded in achieving these goals is shown by these historical facts:

• Over 75 percent of the international trading rules in effect today were written fundamentally by U.S. trade negotiators over the past 50 years.

• World trade has expanded from less than $100 billion in the late 1940s to over $6.3 trillion in 1996. Moreover, the volume of world trade in merchandise goods and services totaled an estimated $6.6 trillion in 1997.

• The Soviet communist empire collapsed in 1989 when the Berlin Wall came down, and today even the few remaining communist regimes in the world—including the Republic of China and Cuba—have been compelled to introduce free-market economic policies which, in turn, are gradually raising pressures for political freedom in these countries.

In Latin America, the Enterprise for the Americas Initiative (EAI) launched by former President George Bush in 1989 laid out the goal of creating an American-led, free-trade area encompassing the entire Western Hemisphere, from Alaska in North America to Tierra del Fuego in South America. The first step in creating a Free Trade Area of the Americas (FTAA) was taken by the Bush Administration in 1990 with the announcement that the U.S. would negotiate a free-trade agreement with Mexico. The North American Free Trade Agreement (NAFTA) was approved by the U.S. Congress in 1993 and implemented as of January 1, 1994. Subsequently, at the Summit of the Americas held in Miami, Florida, from December 9–11, 1994, President Clinton and all of the democratically elected leaders of Latin America, the Caribbean, and Canada pledged unanimously to create an FTAA by the year 2005; President Clinton also pledged that Chile would become NAFTA's fourth member by 1995, thus confirming to the region's leaders that the U.S. was firmly committed to hemispheric trade expansion.

Nine days after the Miami Summit concluded, however, the collapse of the Mexican peso derailed NAFTA's expansion to Chile and other countries in the Western Hemisphere. Although the FTAA negotiating process begun at the Miami Summit has continued from 1995 to 1998, the Clinton Administration's inability to obtain fast-track negotiating authority in order to expand NAFTA to Chile has undermined American influence and leadership in the negotiating process. The second Summit of the Americas is scheduled to be held in the Chilean capital city of Santiago at the end of April 1998, and a hemisphere-wide agreement has already been reached to launch formal FTAA trade negotiations at the summit with the objective of finally establishing the FTAA in 2005. Without fast track negotiating authority, however, U.S. leadership at the summit will be severely diminished, and prospects for creating an FTAA based on NAFTA as the benchmark trade agreement have nearly vanished.

In retrospect, the Clinton Administration's ambitious international trade policy peaked at the end of 1994. Although U.S. exports of merchandise goods and services have continued to expand rapidly throughout the 1990s—totaling over $933 billion in 1997—these gains were largely the result of major trade liberalization initiatives undertaken by previous administrations. Moreover, while President Clinton deserves credit for pushing through Congress the approval of NAFTA in 1993 and the Uruguay Round Agreements in 1994, no major new trade liberalization initiatives have been completed by the Clinton Administration in more than three years. And the reason for this is that President Clinton has been without fast track negotiating authority since 1994. Without fast track authority to launch new trade negotiations bilaterally, regionally and multilaterally, the United States is not a player in the continuing fast-paced game of global trade and investment expansion.

President Clinton's lack of fast track trade authority has already damaged American economic interests around the world. In Latin America, for example, the dynamics of free trade expansion have changed dramatically since 1995. Instead of accepting the U.S. position that the region's greatest prospects lie in accelerated trade liberalization based on an expanded NAFTA model, many countries in South America are now looking instead towards the South American Common Market (Mercosur) as the preferred vehicle for regional trade liberalization. Mercosur is a Brazil-led customs union that also includes Argentina, Uruguay, and Paraguay. Chile and Bolivia became associate members in 1997, and currently Venezuela and Colombia are also negotiating their accession to Mercosur. In addition, both Mexico and Canada are pursuing free trade negotiations with the Mercosur countries. And, moreover, Mercosur has announced a formal decision to seek a free trade agreement with the European Union before entering into any future trade negotiations with the United States aimed at establishing a hemisphere-wide FTAA.

The only country not involved in the expansion of Mercosur is the United States, which is subject to the higher tariffs of Mercosur's common external tariff (CET) and therefore loses competitiveness against goods manufactured inside Mercosur or in countries which have free trade pacts with Mercosur. While this exclusion may not affect large U.S.-owned multinationals who have the financial and technological resources to build new production facilities within the Mercosur region, it does affect the thousands of small and medium-sized American export businesses which cannot re-locate or establish subsidiary operations in South America. Similarly, the exclusion from Mercosur markets also affects workers at small and medium-sized export businesses who may see their employment and wage-growth opportunities curtailed by the inability to expand exports to South America.

The Clinton Administration's lack of fast track negotiating authority has also affected U.S. economic interests at the level of the WTO and APEC. In April 1994, the United States signed the Uruguay Round trade agreements creating the World Trade Organization (WTO), which went into force on January 1, 1995. The Reagan Administration initiated these trade negotiations in 1986 as part of an ongoing series of talks under the General Agreement on Tariffs and Trade (GATT). This was the eighth "round" of GATT trade talks that started in 1947. The WTO is a forum in which countries can seek peaceful solutions to trade disputes without resorting to trade protectionism. Thus, instead of occasional international trade negotiations like the eight previous rounds of GATT talks, the WTO allows for ongoing negotiations.

Since the WTO went into effect on January 1, 1995, the U.S. has completed and signed multilateral sectoral agreements covering Telecommunications, Financial

Services, and the first stage of an International Technology Agreement (ITA). However, the Clinton Administration has exhausted its residual negotiating authority at a time when the task of trade liberalization is far from being concluded. For example, the U.S. needs to pursue further liberalization in telecommunications, financial services and ITA issues. Moreover, the U.S. also must negotiate sectoral agreements within the WTO covering the areas of investment safeguards, competition policy and government procurement. Finally, the WTO is presently scheduled to launch two major new sectoral negotiations at the end of 1999 and the end of 2000, covering agriculture and services. All of these sectoral negotiations encompass industries and economic sectors where the United States is the world's leading competitor, enjoying major advantages in terms of technology development, productivity, product quality and market share. If the U.S. Administration does not have fast track trade authority to participate actively in these sectoral negotiations, it runs the risk that other groups of countries—such as the European Union—will write the rules for tomorrow's global trading system, in detriment of U.S. economic and national security interests around the world.

The forum for Asia Pacific Economic Cooperation (APEC) is America's institutional link to fast-growing Asian economies. Formed in 1989, APEC encompasses Australia, Brunei, Canada, Chile, China, Hong Kong, Indonesia, Japan, Malaysia, Mexico, New Zealand, Papua New Guinea, the Philippines, Singapore, South Korea, Taiwan, Thailand, and the United States. The leaders of APEC's member economies, including President Bill Clinton, in 1994 set as their goal achieving "free trade and investment in the Asia Pacific" region by 2010 for developed members and by 2020 for developing members. Since 1994, however, all of the easy unilateral liberalization measures that could be accomplished within APEC have been achieved. At the most recent summit of APEC's heads of state, held in Vancouver, Canada during November 1997, it was agreed that the forum would look into future liberalization talks covering a number of sectors, including environmental goods, fish and related products, gems and jewelry, toys, forest products, telecommunications, energy oils and oilseeds, chemicals, and food products, among others. Without fast track authority, however, America's prospects for advancing these talks will fade quickly, particularly in light of the Asian financial crisis which threatens to engulf Indonesia in ethnic and political turmoil that could spread to other Asian countries. APEC began as a promising new regional trade liberalization forum, but without strong U.S. leadership backed by a fast track authority that provides the U.S. president a clear mandate to negotiate trade agreements, APEC runs the risk of turning into an irrelevant entity without a purpose. If this occurs, American prospects for expanding trade and investment more quickly in the Asia Pacific region could be derailed for years.

WHAT SHOULD CONGRESS AND THE U.S. ADMINISTRATION DO?

America needs to be put back on the road to free trade. Specifically, the U.S. should:

Renew the Executive's fast track negotiating authority. Without fast track authority, no president can initiate and complete vital trade negotiations in Latin America, Asia, and Europe. Moreover, without fast track, the U.S. will be sidelined in vital upcoming WTO negotiations covering many sectors in which America today is the undisputed technology and market leader. If the U.S. does not remain at the vanguard of global trade and investment liberalization, America's economic prosperity will suffer. Export growth will slow, new employment opportunities will be lost, the nation's competitive technology edge will dull, inflation and interest rates will certainly rise as economic activity turns more sluggish, and American leadership around the world will decline. Congress should grant the U.S. president a broad fast track authority to undertake trade negotiations in Latin America, Asia and Europe, and within the WTO. However, Congress should not include in the Executive's fast track negotiating authority any provisions unrelated to trade, such as labor and environmental standards.

Establish free-trade areas between the United States and its trading partners. NAFTA should be expanded to incorporate Chile and other Latin American countries, and Caribbean nations should receive trading parity with NAFTA members. The U.S. also should pursue free trade negotiations with countries such as Australia, New Zealand and Singapore. The U.S. should cooperate with other APEC members and take more concrete steps to liberalize trade in Asia. Finally, the U.S. should offer a Transatlantic Free Trade Area to interested European countries, including the recently freed nations in Eastern and Central Europe.

Support the accession of both the People's Republic of China and the Republic of China on Taiwan to the World Trade Organization on a commercially viable basis.

In 1986, Beijing applied to resume China's seat in the General Agreement on Tariffs and Trade, the predecessor of the WTO, which the Republic of China on Taiwan had abandoned in 1950. In 1990, Taiwan also applied to join the GATT. Following Hong Kong's example, Taiwan elected to apply as the autonomous customs territory of "Chinese Taipei," rather than as a sovereign country. This move was intended to finesse Beijing's sensitivities over questions of sovereignty. Beijing insists that Taiwan not join the WTO before the PRC, but has offered as its first act as a WTO member to sponsor Taiwan. Joining the WTO is an economic, not political, act. Therefore, Beijing should not be allowed to block Taiwan's entry; each application should be considered on its own merits. Although negotiations with Taiwan have progressed further, neither China nor Taiwan has offered sufficient concessions to warrant WTO membership.

Demand an end to China's practice of forcing foreign firms to transfer technology as a condition of investing. The leverage that China can exert with its huge market makes it difficult even for large industrial firms to resist this form of government-sponsored theft. The U.S. must also insist that all existing bilateral trade agreements, especially the 1995 Intellectual Property Rights Memorandum of Understanding, be fully enforced before approving China's accession to the WTO.

Repeal the outdated Jackson-Vanik Amendment to the Trade Act of 1975.The Jackson-Vanik Trade Act was designed to encourage the Soviet Union and its Eastern European satellites to lift restrictions on Jewish emigration to Israel and the U.S. It withdraws America's most-favored-nation trading status from any country that restricts immigration. Threatening to deny MFN status to China because of human rights abuses has become an annual ritual in Congress. But maintaining MFN with China is clearly in America's economic interest. At stake are billions of dollars in trade. It also encourages the liberalization of China's political system. Trade forces China to open up to the outside world and therefore serves the long-run cause of human rights.

Include Chile in NAFTA. Chile has enjoyed the fastest economic growth and the greatest economic stability of any country in Latin America since the mid-1980s. It is in the forefront of economic and democratic reform in the Americas, having successfully achieved the transition from military dictatorship to civilian democracy. Chile now has bilateral free trade agreements in effect with Canada and Mexico, it is a member of APEC, and an associate member of Mercosur.

Submit more accurate trade reports. The United States Trade Representative (USTR) produces an annual report on foreign trade barriers. This report is important because it identifies the barriers that U.S. exporters face when selling their products overseas. However, it tells only one side of the story. America maintains a host of import restrictions such as trade quotas, high tariffs, and import bans that are not described in the report. They should be. By including such information, the U.S. government would be presenting a more open picture of the status of free trade and of where reforms are still needed, including within the U.S. Moreover, such USTR reports should incorporate a scorecard of the current cost to the economy of each of these U.S. restrictions on trade.

Upgrade the capacity of U.S. federal agencies to compile and report trade data at the national, state and local levels. Since the early 1990s, budget cuts at the Census, Department of Commerce and Bureau of Economic Analysis have caused the elimination of important data-gathering programs capable of producing credible and accurate statistics—at the national, state and local levels—relating to exports, jobs and exporters. The U.S. currently has the capacity to generate manufactured export data at the national level, and in a limited way at the state level. However, the U.S. does not have the capacity to compile and disseminate data relating to service exports. Moreover, due to budget cuts in federal data-gathering agencies, the U.S. lacks the capability to compile and analyze export-related data below the level of two-digit Standard Industrial Classification (SIC) ranking on a state-by-state basis. American policymakers, state governments, exporters and investors are in urgent need of reliable data capable of quantifying exports, jobs and exporting firms at the level of congressional districts and metropolitan areas.

Chairwoman DUNN. Thank you very much, Mr. Sweeney.

Mr. Gadbaw.

STATEMENT OF R. MICHAEL GADBAW, US–ASEAN BUSINESS COUNCIL, AND NATIONAL FOREIGN TRADE COUNCIL

Mr. GADBAW. Thank you, very much for this opportunity to address the critical policy issues arising from the Asian crisis. I'd like to make three basic points.

First, Congress should support the IMF package that is being presented by the administration because it is in the U.S. interest.

Second, Congress should look carefully at the details of the economic reforms in Asia and discuss it with companies like those represented in the US–ASEAN Business Council and the National Foreign Trade Council because you will find that the reforms that have been undertaken are fully consistent with the objectives of the U.S. Government and the private sector in opening those markets for trade, investment, and finance.

And, third, we must remember that reform is a generational process. We would like to work with Congress to improve the workings of the IMF and U.S. Government in way s that will facilitate the kind of ongoing reforms in Asia and elsewhere that will restore growth to that region and preserve the healthy growth we have achieved here in the United States.

Let me start with what I think is the most important issue; namely the IMF replenishment package that is before Congress. In our view, it is vitally important that Congress move expeditiously to approve the $3.5 billion contribution to the New Arrangements to Borrow and the $14.5 quota increase.

First, the IMF, while not a perfect institution, has been a key component of stability in global financial markets for the past 50 years. We should not forget the reasons for its creation, including avoidance of worldwide competitive devaluations, a surefire way to global depression. In some respects the IMF is to the global monetary system what the Federal Reserve is to the domestic financial system; it is also what the WTO is to the global trade system. It has served us well historically, it would have to be recreated if it did not exist, and it has operated at no cost to the American taxpayer or U.S. Government.

Second, it is not fair to reject the IMF package as a bailout. The IMF is providing loans to these countries to allow time for the economic reforms to take effect. In time, it is these reforms that will restore market confidence and encourage return to robust prosperity.

I encourage every Member of the Subcommittee and Full Committee to examine the letters of intent which encompass the various commitments that have been made by the countries in Asia, particularly Korea, Thailand, and Indonesia. As I would like to explain in more detail, these commitments are completely in-line with reforms American business has been pursuing with our regional counterparts.

Deputy Secretary of Treasury Larry Summers has focused our attention on what is new about this crisis: "Relative to nearly all of the crises we have seen in recent years," he said, "the problems that must be fixed in Asia are much more microeconomic than macroeconomic, and involve the private sector more and the public sector less."

In 1995 the US–ASEAN Council's Indonesia Committee started a bilateral private sector dialog with KIKAS, the American Committee of the Indonesian Chamber of Commerce. Each year we identified areas of mutual interest which would facilitate increased trade and investment, and made recommendations to each government for reforms in those areas. In the second year we identified privatization and deregulation in three sectors, energy, financial services, and agriculture, as our major areas of interest.

Indonesia's deregulation packages over the past several months, as well as the reforms committed to in their letter of intent with the IMF, address virtually all of the areas we and KIKAS had identified for reform. Indonesia is now facing the most serious economic crisis in its history. Developments that had their origins in economic breakdowns in other parts of the region came to focus on some of the weaknesses of the Indonesian economic model, particularly in the financial sector. In response, Indonesia has agreed with the IMF to accelerate and expand its economic reforms. Over the last month and a half, more reform has been achieved in Indonesia than in the last two decades—all in the direction that United States business has supported.

My experience leads me to believe that if engaged appropriately and patiently, the most recent processes of reform will be realized. Similar reforms have been undertaken in other parts of the region.

Allow me to make three points with respect to the IMF package. We are opposed to imposing additional conditions on the IMF in connection to its funding package. I agree with Paul Wolfowitz who said last month, the time to reorganize the fire department or to question whether fire insurance makes people careless about fire prevention is not when the whole neighborhood is burning down. We support a healthy debate on the conditions involved in the IMF reform packages as they relate to these countries and their implications of U.S. interests. As we have discussed, we believe the reforms that have been embraced by Korea, Thailand, and Indonesia are very consistent with initiatives on which we have been working with cooperation with our business counterparts, and we would support an effort to examine ways to improve the process by which the IMF operates and the ways it ensures transparency to the market. As IMF officials have recognized in both private and public conversations, there are ways to improve this process provided that effort does not interfere with the need to act expeditiously in the current crisis. Thank you.

[The prepared statement follows:]

Statement of R. Michael Gadbaw, US–ASEAN Business Council, and National Foreign Trade Council

I am pleased to be here today on behalf of the US–ASEAN Business Council (USABC) and the National Foreign Trade Council (NFTC). The US–ASEAN Business Council is a private, non-profit organization of more than 350 member-companies which works to expand trade and investment between the US and the member countries of the Association of Southeast East Asian Nations (ASEAN). The NFTC, on whose Board I serve, is a broadly based trade association of over 550 US companies dealing directly with US public policy affecting international trade and investment. As you will see, both organizations are solidly agreed on the basic message of my testimony on the need for US leadership and support for the IMF funding package before the Congress.

Since I last testified before the House of Representatives in May of last year, much of East Asia has entered a period of economic retrenchment. A great deal has changed in 10 months—the single most significant development being the financial crisis that has swept the region and dramatically reversed its historical growth patterns. This is the development that today most occupies the observers of the region, US businesses operating there, and US policy makers. The impact of this crisis on US business and the importance of your support for the Administration's IMF funding package, therefore, are the focus of my remarks today.

Let me start with what I think is the most important issue, namely the IMF replenishment package that is before Congress. In our view, it is vitally important that the Congress move expeditiously to approve the $3.5 billion contribution to the New Arrangements to Borrow (NAB) and the $14.5 billion quota increase. I believe the other witnesses will elaborate at length on the many reasons why we should approve the entire request this year, so I will be brief in highlighting several overall reasons why the request deserves the full support of the Congress.

First, the IMF, while not a perfect institution, has been a key component of stability in global financial markets for the past 50 years. We should not forget the reasons for its creation, including avoidance of worldwide competitive devaluations—a sure fire way to global depression. In some respects, the IMF is to the global monetary system what the Federal Reserve is to the domestic financial system; it is also what the WTO is to the global trade system. It has served us well historically, it would have to be recreated if it did not exist, and it has operated at *no* cost to the American taxpayer or US government.

Second, it is not fair to reject the IMF package as a "bail out." The IMF is providing loans to these countries to allow time for their economic reforms to take effect. In time, it is these reforms that will restore market confidence and encourage a return to robust prosperity. It is also wrong in that it suggests an act of charity, when in fact, the IMF is acting in the interest of international economic stability. It thereby acts in the US interest. Moreover, no U.S. taxpayer money will be used. The budgetary impact of funding for the IMF is zero. And yet, our contribution is leveraged six-to-one by other contributors. For a total cost of zero, meeting our commitments to the IMF puts the US in a leadership position. The IMF increases our leverage by exerting forceful multilateral pressure for undertaking otherwise unpopular and painful reforms.

I encourage every member of the Subcommittee and full Committee to examine the letters of intent which encompass the various commitments that have been made. As I would like to explain in more detail, these commitments are completely in line with reforms American business has been pursuing with our regional counterparts.

Deputy Secretary of the Treasury Larry Summers has focused our attention on what is new about this crisis. "Relative to nearly all of the crises we have seen in recent years, the problems that must be fixed (in Asia) are much more microeconomic than macroeconomic, and involve the private sector more and the public sector less." While recognizing the important role of macroeconomic stability, microeconomic reform is precisely the area where the real work of Asia's recovery is to be done. Adopting the right policies to promote structural reform and monitoring carefully their impact on the market are the keys to restoring economic growth throughout Asia and especially in Indonesia, Thailand and South Korea.

Because I am most familiar with Indonesia, I would like to begin with a discussion of that country as a lead in to the issues raised throughout the region. I would like to focus this portion of my testimony on how the private and public sectors can work together toward growth oriented economic reform and development.

For the last several years, I have served as the Chairman of the US–ASEAN Business Council's US-Indonesia Business Committee. This Committee is comprised of Council member companies with a significant stake in trade and investment in Indonesia and representing sectors as diverse as oil, mining, energy, manufacturing, apparel, high technology and agriculture.

In 1995 the U.S.–ASEAN Council's Indonesia Committee started a bilateral private sector dialog with KIKAS, the American Committee of the Indonesian Chamber of Commerce. Each year we have identified areas of mutual interest which would facilitate increased trade and investment, and have made recommendations to each government for reforms in those areas. In the first year we identified customs reform, distribution liberalization and renegotiation of the tax treaty as three key priorities.

Because of the responsiveness of Indonesian business and the Indonesian government, we were extremely successful that first year and achieved an initial liberalization of Indonesia's distribution regime, the signing of a new bilateral tax treaty in late 1996, as well as the initiation of a program of technical assistance between the U.S. and Indonesian customs service.

In the second year we identified privatization and deregulation in three sectors—energy, financial services, and agriculture, as our major areas of interest. Indonesia's deregulation packages over the past several months as well as the reforms committed to in their letter of intent with the IMF address virtually all the areas we and KIKAS had identified for reform. We have been especially gratified to see a complete lifting of all the distribution restrictions, a dismantling of Bulog, the local agricultural monopoly, together with an elimination of a web of subsidies for the agricultural and commodity sectors, restructuring of the financial sector, including lifting all restrictions on branching of foreign banks, and gradual elimination of key subsidies in the energy sector. While there is still work to be done, we are been pleased with the process created of bilateral private sector exchange and input to the government, and see this as a model for continuing to work these issues in Indonesia and throughout the region.

Indonesia is facing the most serious economic crisis in its history. Developments that had their origins in economic breakdowns in other parts of the region came to focus on some of the weaknesses of the Indonesian economic model, particularly in the financial sector. In response, Indonesia has agreed with the IMF to accelerate and expand its economic reforms. Over the last month and a half, more reform has been achieved in Indonesia than over the last two decades, all in the direction that US business has supported. My experience leads me to believe that, if engaged appropriately, and patiently, the most recent processes of reform will be realized.

It is impossible to understand the current situation in Indonesia without taking a quick look at the historical record. Prior to 1997, Indonesia averaged for 25 years an economic growth rate of 7%. It had reduced the incidence of poverty to 14%—this from an average of 70% in 1970. And it has created a middle-class conservatively estimated at 20 million. Indonesia's economic performance so impressed the world that the U.S. Department of Commerce in 1995 named it one of the world's ten big emerging markets, and the World Bank just last year estimated that it could become the world's sixth largest economy by the year 2010.

The events of the last six months have brought home to the Indonesians that the system that provided them so much prosperity also contains some fundamental structural weaknesses. A victim of its own success, the pace of reform in Indonesia simply could not move along fast enough to productively accommodate the ever increasing flow of capital.

Since January 15th when President Suharto pledged a reform program unprecedented in Indonesia for its scope, the Government of Indonesia has moved to address this situation. The reforms now underway tap into issues and interests that are deeply entrenched in Indonesian society. To give you an idea of the full scope of these reforms allow me to briefly summarize the measures President Suharto agreed to last month. They have not in my opinion been very well publicized. (1) The privatization of state owned enterprises will be accelerated. (2) Twelve major infrastructure projects were canceled. (3) Funding and credit privileges for Indonesia's state airplane projects were canceled. (4) All special tax, customs, and credit privileges for the National Car were canceled. (This had been an issue of such great concern to Indonesia's trading partners, that the US, the EU and Japan had been contesting at the WTO for more than a year. The IMF, in consultations with the Government of Indonesia, managed to achieve something the efforts of three governments and the processes of the WTO had thus far failed to resolve.) (5) Accounts once off budget, such as the Reforestation and Investment Funds, were brought on budget. (6) The government monopoly on the import and distribution of sugar and wheat was abolished, leaving only rice subject to monopoly. (7) The cement, paper, and plywood cartels were slated for dissolution. And (8), the government agreed to the removal of all restrictions on investment in wholesale and retail trade.

These are just to mention a few of the changes underway. And they are underway. The Government of Indonesia has issued more than 30 regulations implementing various parts of its agreement with the IMF.

Similar reforms have been undertaken in the other nations most afflicted by the Asian currency crisis and the economic tide seems to be turning in a positive direction. Thailand has committed to greater privatization, reductions in subsidies, and a loosening of limitations on foreign ownership and exchange controls. Korea has agreed to eliminate unfair subsidies to exporters, relax import licensing and customs procedures, and ease foreign ownership restrictions. Perhaps most significantly, given the nature of the crisis in Korea, the government has agreed to end government-directed noneconomic lending. Reform of South Korea's chaebol system is something the US has been pursuing for years.

If these reforms are so dramatic, it is fair to ask why the crisis is not over? Every day we read about new developments, some of which test our faith in the ongoing commitment of governments in the region to stick to their commitments. The fact is that with microeconomic reforms of this type, the market response is critical and it is essential to have accurate feedback on the market implementation and response to these measures. That does not mean, however, that we should react to every story that appears in the media, I appeal to the subcommittee to keep in perspective the unprecedented challenges posed by these changes. In the case of Indonesia, the bulk of them are only a little more than a month old.

In the cases of Korea and Thailand, no less than Indonesia, we are asking these countries to change practices that profoundly affect commercial, economic, social and political relationships. We must exercise patience and understanding. A more accurate picture of the region's commitment to this new phase of economic reform will emerge in the course of the year. Mindful of this realistic time frame, we should resist the temptation to leap on each anecdote as a sign of rejection. Instead, we should monitor the situation and build on our record of engagement. When we discover that developments on the ground are not in accordance with the promises made by authorities, we should take it up with our friends in the region and encourage them to move forward.

Congress is doing its part to monitor the situation. I find the number of hearings since Congress returned from its Christmas recess reassuring, and I commend the leadership of this subcommittee for holding a hearing to help gather the facts.

It also falls to Congress to remain engaged. This can best be done by providing the resources needed by the IMF. The IMF's capital base is at an historical low, with $10–15 billion currently available. Whether we like it or not, we are the preeminent world leader and we must lead the way. We are the largest contributor to the IMF. This not only means that we have the largest amount of influence, but it also means we have the largest responsibility. It is essential to preventing the Asian flu from spreading into a broader contagion. Do we really want to take the chance that there is no danger of the situation deteriorating and deteriorating fast? There are, moreover, broader strategic and political reasons—the countries affected are major allies and security partners of the United States. Our Asian partners will remember our actions or lack thereof at a time of dire need and encouragement.

American businesses and the workers they employ have too much at stake in Asian prosperity to risk its recovery. Companies with business in Asia have seen contracts canceled or postponed, our agricultural exports to Asia are declining, and other important markets—such as Latin America—appear to be slowing down. US financial institutions are also taking their fair share of losses.

GE is, in may ways, a good reflection of U.S. business, given that our businesses include infrastructure, consumer products, and financial services. Our exports to the Pacific Basin last year were $3.176 billion (supporting over 45,000 jobs), as part of our overall $6.3 billion trade surplus as a company. These exports include turbines from Schenectady, NY and Greenville, SC, locomotives from Erie, Pennsylvania, aircraft engines from Cincinnati, OH and medical diagnostic equipment from Milwaukee, WI.

With Asia's large population and rapidly emerging middle class, Asia was and continues to be a key market for GE's future. We remain committed to these markets and are pleased to see many market reforms which will facilitate our sales over the long-term. In the near-term, it is clear that companies operating in the region will see an impact on their sales as these countries trim their budgets for big-ticket items and the middle classes have less discretionary income to spend on imported products. In this regard, I would underscore the critical need of the US Export-Import Bank and other US agencies and government functions which support US exports. Export opportunities are down, private commercial trade finance is scarce in key markets, and our trading competitors, with the strong backing of their governments, will fight aggressively to secure the remaining opportunities that exist.

This year, Indonesia, Thailand, and South Korea are all expected to register negative growth rates. I trust that in a couple of years, with proper guidance, the region will once again become a driving force behind American exports, but the region will recover only if we do not undermine it by failing to support the international organizations that are critical to its recovery.

Passage of the IMF funding request has also prompted a debate over IMF conditionality. In this regard, I agree with CRS analyst, Patricia Wertman: "The Asian crisis has made the often sterile debate over IMF conditionality into a debate of historic significance with serious consequences." In this regard, I speak for the broad cross section of USABC and NFTC member companies in stating:

- We are opposed to imposing additional conditions on the IMF in connection with this funding package. I agree with my friend Paul Wolfowitz, who said last month before the Banking Committee that "The time to reorganize the fire department or to question whether fire insurance makes people careless about fire prevention is not when the whole neighborhood is burning down."

• We support a healthy debate on the conditions involved in the IMF reform packages as they relate to these countries and their implications for US interests. As we have discussed above, we believe the reforms that have been embraced by Korea, Thailand and Indonesia are very consistent with initiatives on which we have been working in cooperation with our business counterparts in the region.

• We would support an effort to examine ways to improve the process by which the IMF operates and the ways it ensures transparency to the market. As IMF officials have recognized in both private and public conversations over the last month, there are ways to improve this process, provided that effort does not interfere with the need to act expeditiously in the current crisis.

At the same time that we are reviewing the way the IMF operates, it would be desirable to examine ways to improve the working of the US Government in its approach to this crisis. A key lesson is the need for policy integration, particularly as it relates to tying together our interests in trade, investment and financial sector liberalization. The agencies of the US Government working these areas need to develop more effective means for obtaining input from the private sector and harnessing the leverage market forces can bring in support of necessary reforms. The USABC and the NFTC are made up of member companies with direct insight into the market response to the policy changes being undertaken in Asia. As we move to an active phase of monitoring the implementation of these reforms, there will be a critical need for real time information on how the market is responding and what further policy measures may be needed to achieve the objectives of reform.

Toward this end, the US–ASEAN Business Council commissioned last month a report on reforms in Indonesia which analyzes the reforms Indonesia has made over the last three years. Because of the timeliness of this report, I would ask the Committee that the report by attorneys Robert Hornick and Mark Nelson be submitted for the record. The Council has also inaugurated a series of conference calls with the AmChams in Indonesia and Thailand to maintain an on-the-ground private sector perspective of the region's compliance. This initiative supplements a continuing series of conference calls we have conducted with the U.S. embassy in Jakarta over the last two years to solicit the Ambassador's views and, most recently, focus on the impact of the IMF reforms.

Finally, I would like to say a word about the role that our friends in China and Japan have to play in helping East Asia in its recovery. I have been quite encouraged by Chinese reassurances that it will not devalue its own currency in an effort to compete with the devalued exports of its neighbors. They are to be commended for their responsible position.

With regard to the Japanese, I can only echo the calls for Japan to strengthen domestic demand, further liberalize imports, deregulate its economy and effectively address its own financial difficulties. Its own reform is the most important contribution Japan can make to the recovery of its neighbors. It is difficult to imagine a full recovery for Asian economies with Japan continuing at growth rates of less than 1%. Japan must serve as a locomotive of growth in the region. As the world's second largest economy and most important trade and investment partner throughout Asia, it must share in the responsibilities that go along with such status. An export-led strategy will not work in resolving the serious economic problems in the region and could exacerbate trade tensions between our two countries.

By way of closing, I would like to reiterate my faith in Asia's ultimate recovery. Until the crisis diverted attention from the long-term picture, the most ardent advocates of the region ceaselessly touted the region's economic prospects. In the case of ASEAN, we talked about a region by the year 2010 with a population of 560 million and a trillion dollar GDP and two-way trade with the US of more than $300 billion per year. I speak for the US–ASEAN Business Council and the National Foreign Trade Council when I say that I still believe in that vision. It may not arrive as soon as we expected, but with proper international leadership, it is not much farther away.

Chairwoman DUNN. Thank you, Mr. Gadbaw. Let's move now to the gentleman who has joined our panel, C. Fred Bergsten, who is the director of the Institute of International Economics.

Mr. Bergsten.

STATEMENT OF C. FRED BERGSTEN, DIRECTOR, INSTITUTE FOR INTERNATIONAL ECONOMICS

Mr. BERGSTEN. Thank you very much, Madame Chairwoman. Let me apologize for getting here late. I was in the middle of a hot debate on the IMF legislative proposal before some of your colleagues at the Joint Economic Committee, and I apologize. I'll be very brief. I've given you a full written statement.

I was asked to address the impact of the Asian crisis on United States trade and the outlook for trade policy and I'll try to do that, very quickly, across three time horizons: the short run, the long run, and, where I think the difficulties lie, in the medium run.

It is too early for the financial crisis, and the policy responses to it, to have much impact on trade flow. Korea and Thailand have shifted into current account surplus and our exports to Korea have fallen sharply in the last couple of months. Our own trade balance so far, however, remains on about the same plateau of the last 18 months—a merchandise deficit of about $200 billion and a goods and services deficit of about a $110 billion. So far that has stayed put, although I think it's likely to increase in the near future. I'll come back to that in a moment.

The Asian crisis so far, however, has had some very positive effects on trade policy. Despite concerns in some quarters that liberalization of national financial markets was a cause of the crisis, all of the members of the World Trade Organization, including all the crisis countries in Asia, agreed in December to further opening of that sector. A second positive development was the decision of the 18 APEC countries at their annual summit meeting in Vancouver in November to designate 15 major sectors—including autos, chemicals, energy goods and services, environmental goods and services, medical equipment—for early liberalization. And they agreed that detailed plans for eliminating barriers in nine of those sectors totaling over $1.5 trillion of global trade, should be agreed by the middle of 1998 and implemented in early 1999.

Some of the Asian members of APEC are of course the countries hit most directly by the crisis. It is thus extremely encouraging that they are willing to continue and even accelerate their progress toward achieving the agreed APEC goal of free and open trade and investment in the region by 2010. In fact, APEC's Vancouver pledge to eliminate barriers in nine additional sectors this year represents the major progress toward free trade that is now being pursued anywhere in the world.

In the long term, I think there is a silver lining on the current crisis cloud. That is the considerable further liberalization that countries will have to adopt to restore the economic prospects and to overcome their crises. It is noteworthy that every problem country in Asia has clearly indicated its intention to move in this direction, i.e., further liberalization, whether with the IMF or to avoid it, as in the case of Malaysia. These reforms include increased transparency, reductions of impediments to trade and investment, and the corresponding domestic measures.

A key point for the Congress to keep in mind is that the international institutions in which we participate, like APEC and particularly the International Monetary Fund, insist on further trade liberalization and further opening of markets. They are therefore very supporting of U.S. interests. We ought to be strongly supportive of them, as, for example, at present, through further funding for the IMF.

There may be major problems in the medium run, however, both in the crisis countries themselves and in the rest of the world as a result of the impact of the crisis on trade flows. Over the next year or so, the huge currency depreciations in Asia will sharply improve the competitive position of every country in the region. As part of the adjustment, those countries are going to face recessions, with zero or negative growth over the next year or so, which also will dampen their imports and increase their zeal to export to the rest of the world. This is a natural, inescapable part of the adjustment process, but it will lead to some swings in trade balances.

We've just published a new study at the Institute for International Economics that tries to quantify these effects. You have to make some guesses where the exchange rates wind up but we've done that and we have come to the following conclusions: Over the next year or so, there will be an increase of about $50 billion in the U.S. trade deficit as a result of the Asian crisis. There will be a similar adverse swing in the trade position of Europe—they happen to start from a surplus, but they'll be hit by about the amount we are. On the positive side, Korea will probably get an improvement of about $40 to $50 billion, moving it from the large deficit it had prior to the crisis to a modest surplus. And there will be a pickup of about $50 billion in the trade position of Japan.

These swings occur at a time when trade policy is already under substantial pressure. The Congress did not approve new fast track authority last year, despite the good performance of our own economy. Europe continues to face high employment and is preoccupied with internal matters, so it's not going to do much on the trade front.

The biggest problem is Japan. As the world's largest surplus and creditor country, Japan should be reducing rather than increasing its surplus to help facilitate the adjustment of the other countries in Asia. That would be the major contribution Japan could make to the crisis. It has to be continually pushed to move in that direction.

But the bottom line in all this is that the adverse swing in our own trade balance and in Europe, exacerbated by Japan's further increases, could derail us from the proper course of trade policy in this country over the next couple of years. In my view, it's essential for us, particularly because of the crisis, to reconsider and pass fast track legislation. We have to signal that our markets are going to continue to be open if we're going to be able to credibly push the Asian countries to keep opening their markets. We are going to have to absorb some additional imports, given our good economic conditions, to enable them to overcome their crisis.

A particular casualty if we do not move forward could be the APEC liberalization program that I talked about above. We need new negotiating authority to pursue a number of the sectoral initiatives to which APEC has already agreed. The program simply cannot proceed without the United States—we have to be in it. It would be the height of folly if the United States were to let the APEC trade liberalization program collapse. American exporters have enormous opportunities in a very wide range of sectors that our APEC partners have already agreed to liberalize. That's because of the strong competitive position of our firms and also because many of the Asian countries still have high barriers.

If Congress were unable to pass full fast track authority, which I support, it should still authorize the administration to pursue the agreed APEC sectors on a fast track basis that would enable us to seize that very real, very tangible opportunity that now exists for us to expand our sales and recoup our trade position. It would take advantage of the willingness of our partners in the Asian countries to open their markets further despite the crisis.

Thank you very much.

[The prepared statement follows:]

Statement of C. Fred Bergsten,* Director, Institute for International Economics

United States trade with Asia is being significantly affected by a series of cross-cutting developments. On the one hand, the financial crisis is the region will have a substantial negative impact on our trade balance for the next year or so. On the other hand, APEC has accelerated the pace of its trade liberalization and the IMF programs in the region require even faster reduction of barriers in some cases. Hence the immediate, medium-term and long-run implications of current Asian developments for our economy are likely to differ substantially.

APEC AND THE IMF: CONTINUED LIBERALIZATION IN THE SHORT RUN

It is still too early for the financial crisis and policy responses to it to have had much impact on trade *flows.* Korea and Thailand have already shifted into current account surplus and our exports to Korea have fallen sharply in the last couple of months. Our own trade balance remains on the plateau of the past eighteen months, however, with the merchandise deficit running at an annual rate of about $200 billion and the current account deficit at about $160 billion. But major changes in our position will show up later this year and I will address them below.

The crisis has had some effects on trade policy, however, and to date they have been largely positive. Despite concerns in some quarters that liberalization of national financial markets was a cause of the crisis itself, the members of the World Trade Organization—including all of the crisis countries in Asia—agreed in early December to further opening of that key sector.[1]

The crisis in fact seems to have had a favorable impact. Weaknesses in financial sectors were a central cause of the difficulties in every Asian country. It was universally recognized that further reforms, including opening to foreign institutions, was a necessary component of adjustment programs that would restore confidence in the countries' currencies and economies.

The crisis promoted financial liberalization in two very direct ways. The heightened need for foreign investment, to finance continuing current account deficits in a sustainable manner and to recapitalize weak banking systems, added powerfully to the case for liberalization. And the International Monetary Fund strongly reinforced the WTO agreement, and in a number of instances required reforms that went much further in its support packages for the troubled countries.

A second positive development was the decision of the 18 APEC countries, at their annual summit in Vancouver in November, to designate 15 major sectors—including automobiles, chemicals, energy goods and services, environmental goods and services, and medical equipment—for early liberalization. They also agreed that detailed plans for eliminating barriers in nine of these sectors, totaling over $1.5 trillion of global trade, should be agreed by the middle of 1998 and implemented in early 1999. Some of the Asian members of APEC are of course the countries hit most directly by the crisis and it is extremely encouraging that they were willing to con-

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[1] A comprehensive analysis will be presented in Wendy Dobson and Pierre Jacquet, *Evaluating the Financial Services Agreement*, Washington: Institute for International Economics, forthcoming April 1998.

tinue, and even accelerate, their progress toward achieving the agreed APEC goal of "free and open trade and investment in the region" by 2010/2020.[2]

Despite the crisis, APEC thus remains one of the leading forces in the world for trade liberalization. Given the fact that its members account for half of the world economy, its commitment to achieve free trade by 2010/2020 remains potentially the most far-reaching trade agreement in history. Its creation played a central role in bringing the Uruguay Round to successful conclusion in the GAT in 1993. Its agreement to eliminate tariffs on a wide range of high-tech goods and services galvanized the global Information Technology Agreement in 1996. As noted, it played an important role in the global agreement on liberalization of financial services in 1997. *APEC's Vancouver pledge to eliminate barriers in nine additional major sectors in 1998 represents the major progress toward freeing trade that is now being pursued anywhere in the world."*[3]

To be sure, there has been some modest increase in trade barriers as well since the Asian crisis erupted. Most notably, Mercosur increased its common external tariff by 25 percent—from 12 to 15 percent—as part of its effort to avoid greater contagion from Asia. The failure of the United States to pass fast track legislation last year was also a negative development, to which I return later.

On balance, however, the bicycle of trade liberalization has continued to move forward over the past six to eight months despite the Asian crisis. APEC has been the most prominent factor in the progress despite its region's being the locus of the crisis, and continues to deserve strong support from the United States. The bottom line is "so far, so good."

A Better Policy Framework in the Long Run

The potential long-term silver lining on the current cloud is the considerable further liberalization that countries will have to adopt to restore their economic prospects and thus to overcome the crisis.

It is noteworthy that every problem country in Asia has clearly indicated its intention to move in this direction, whether with the IMF (Indonesia, Korea, Philippines, Thailand) or to avoid it (Malaysia, perhaps China). The reforms will include increased transparency and accountability of financial systems and corporate governance, reduction of impediments to trade and investment, and corresponding domestic measures.

At the end of the day, the trade and investment climate should be considerably stronger throughout Asia as a result of the crisis and policy responses to it. As Senator Roth and I concluded in our recent op-ed on the topic, "the crisis will accomplish enormously more for trade expansion than decades of effort by US negotiators."[4]

A word on China is appropriate in this context. China had avoided being hit directly by the crisis because its currency is inconvertible on capital account and is therefore not subject to direct market attacks. Nevertheless, it has clearly read the message of the markets and has substantially accelerated the pace of its marketization reforms. Premier Li Peng has in fact set a goal of full marketization of the Chinese economy by 2010.

China has not yet moved far enough to qualify for membership in the WTO. It is making rapid progress in the right direction, however, and is in fact the main hero of the current crisis by avoiding the temptation to devalue its currency as well as speeding its internal reforms. This is another beneficial long-term effect of the crisis for the United States and for the world trading system.

Trouble in the Medium Term

There may be major problems in the medium run, however, both in the crisis countries themselves and in the rest of the world, as a result of impact of the crisis on trade flows. Over the next year or so, the huge currency depreciations in Asia

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[2] It should be noted that APEC has also played a very important role in responding directly to the financial crisis. The Vancouver summit endorsed the Manila Framework, worked out a few days earlier by Deputy Finance Ministers of the bulk of the APEC countries, that invented the IMF's new Supplemental Reserve Facility, which was used to provide rapid disbursement of a much higher level of IMF resources to Korea than would have been available previously, and set up a new regional surveillance mechanism that will try to head off future crises by generating peer pressure on countries to take preventative action when trouble is brewing.

[3] For an appraisal of the current status and outlook for APEC see C. Fred Bergsten, *Whither APEC? The Progress to Date and Agenda for the Future.* Washington: Institute for International Economics, October 1997.

[4] William V. Roth, Jr. and Fred Bergsten, "The (Potential) Asian Silver Lining," *The Washington Post,* December 28, 1997.

will sharply improve the competitive position of virtually every country in the region. These exchange rate swings, along with the recessions that are likely to hit every northeast and southeast Asian economy in 1998, will produce very large changes in national trade balances.

A new study by my Institute colleagues Marcus Noland and Ligang Liu, along with Sherman Robinson and Zhi Wang, uses a computable general equilibrium (CGE) model to assess the prospects for trade even if the Asian currencies rebound to some extent from their present levels.[5] Their results include:

• an increase of about $50 billion in the United States deficit in dollar terms[6] and as much as $100 billion in real terms;

• a similar reduction in the surplus of the European Union;

• an increase of about $50 billion in the surplus of Japan; and

• a similar swing of almost $50 billion in the position of Korea, converting it from large deficit to large surplus.

These swings will occur at a time when trade policy is already under substantial pressure in many countries. The Congress of course failed to approve new "fast track" negotiating authority in 1997 despite the stellar performance of the American economy, and the prospects seem dim for resurrecting the legislation this year.[7] Europe continues to face very high unemployment and is preoccupied with the creation of the euro and the expansion of its membership. As noted, Brazil and its Mercosur partners raised their common external tariff by a quarter as part of their effort to avoid contagion from Asia.

The largest problem is Japan. As the world's largest surplus and creditor country, it should be *reducing* its trade surplus sharply rather than increasing it. In addition to proposing new funds that would make more capital available to the rest of Asia, it should be importing billions of dollars' worth of additional products from the region. China, Taiwan and Hong Kong could also afford to run modest deficits, rather than their current sizable surpluses, to help the regional adjustment process.

The first trade policy casualty of this process will probably be the second Summit of the Americas, in Chile in April. Negotiations to create a Free Trade Area of the Americas, as agreed at Miami in December 1994, could still be launched but nothing serious will happen until the United States obtains fast track authority and Mercosur decides to extend its liberalization beyond the grouping itself. A second casualty could be the WTO Ministerial Conference in Geneva in May; the fiftieth anniversary celebration of the GATT/WTO could be reduced to nostalgic platitudes rather than commencing serious planning for Sir Leon Brittan's proposed Millennium Round.

A third casualty, of particular importance for this hearing, could be the APEC liberalization program cited above. The United States needs new negotiating authority to pursue a number of the sectoral initiatives that were agreed in Vancouver. The program cannot proceed without the United States and some Asian countries may even retreat from it if the United States is unable to participate effectively.

It would be the height of folly if the United States were to let the APEC liberalization program collapse. American exporters have enormous opportunities in a number of the sectors that our APEC partners have agreed to liberalize, both because of the strong competitive positions of our firms and because many of the Asian countries still have high barriers in these industries. *Even if the Congress is unable to pass full fast track authority, it should authorize the Administration to pursue the agreed APEC sectors on that basis.*

More broadly, the United States and European Union will have to accept temporary deteriorations in their trade balances to enable the emerging market economies in Asia to successfully engineer the needed improvements in their own external positions. Congressional rejection of fast track authority would signal that the United States may not be prepared to do so. This could induce Asian policymakers to reconsider their commitment to market-oriented strategies—jeopardizing both their prospects for resolving the current crisis and the favorable long-term outlook cited above. Indeed, the major long-term risk from the current crisis is that some of the most important emerging market economies might turn their backs on the

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[5] See Li-Gang Liu, Marcus Noland, Sherman Robinson, and Zhi Wang, *Asian Competitive Devaluations.* Working Paper 98–2. Washington: Institute for International Economics, January 1998.

[6] The nominal impact will be less because of large favorable changes in the US terms of trade, i.e., as the dollar strengthens considerably with respect to the Asian currencies and enables us to buy more imports with fewer dollars. Changes in the real impact are what count for GDP growth and job creation, however, and thus probably for trade policy sentiments as well.

[7] An analysis that includes the full spectrum of Congressional views will appear in *Whither Fast Track?*, Washington: Institute for International Economics, forthcoming April 1998, a special report on a conference held on Capitol Hill on February 3.

liberal policy approaches that they need to accelerate instead. We certainly do not want to take steps that would foster that outcome.

The World Trade Organization will also be severely challenged by the new trade policy threat. It has completed the carryover business from the Uruguay Round with its sectoral agreements on telecommunications, information technology and financial services. New initiatives are now needed to keep the bicycle moving forward and the still-new institution from becoming moribund for a prolonged period, as its predecessor GATT did after completion of the Kennedy and Tokyo Rounds.

At a minimum, the major industrial countries—the United States, the European Union, Japan and Canada—should agree to avoid adopting any new trade restrictions in the wake of the Asian crisis. The OECD members took a similar "trade pledge" after the oil shock of 1973 when they realized that it would be foolish to try to pass around the resulting deficits among themselves. *The impact of the Asian crisis could be at least as sizable as that initial oil shock and the OECD membership, at its upcoming Ministerial meeting, should resolve to avoid beggar-thy-neighbor trade responses.*

All this implies a major challenge to the continued march of globalization. Anti-globalization forces are mounting in both the industrial countries, where they are celebrating the defeat of fast track negotiating authority in the United States as a "historic turnaround in attitudes toward international integration," and in many emerging market economies due to the onslaught of yet another financial crisis. Both the intellectual underpinnings of globalization, and the policies to implement it, are likely to be questioned more severely than at any other time in the past two decades. The global outcome for several decades ahead will turn on the outcome.

CONCLUSION

There are thus a number of potentially significant trade implications from the Asian crisis. We will shortly be moving into the period where countries both inside and outside the region may be tempted to turn to trade restrictions, or at least to avoid new trade liberalization, to help them through the difficult adjustment period.

In such a situation, the best defense is a good offense. The crisis countries must liberalize further, to restore market confidence in their economies and to fulfill their IMF programs. The industrial countries need to do so too, to make clear that they will accept increased Asian exports and to encourage the Asians to maintain their market-oriented adjustment strategies. New initiatives to maintain the momentum of liberalization are acutely needed, particularly in the WTO but in regional contexts such as the FTAA and especially APEC—which has already made very specific commitments to liberalize further—as well.

The United States must lead this process. For all our problems, we have by far the strongest economy in the world. Our large trade deficit is in fact a reflection of the strength of our economy, compared with the ongoing sluggishness in many of our major markets abroad, rather than of American weakness.

Moreover, some of our major competitors (including Japan) have now been weakened substantially by the crisis. Hence further trade liberalization is highly desirable from our standpoint because it will enable us to fully exploit our strong competitive position. Any US backing away from our previous commitments, particularly the pursuit of free trade in the Asia Pacific region and the Vancouver commitment to reduce barriers substantially further in 1998, would send an enormously counterproductive signal to weaker economies that they too could—and even should—backslide.

Hence the coming year or two will present both major challenges to, and major opportunities for, the trade policy of the United States. I urge this Committee to continue its strong leadership of a constructive approach that will enable the world, as well as the United States itself, to emerge from this period in an even stronger position. Rapid passage of fast track authority, along with the provision of resources for the International Monetary Fund, is the place to start.

Chairwoman DUNN. Thank you very much, Mr. Bergsten.

Mr. Bergsten and Mr. Sweeney, I want to ask you a question about savings. Several, many of these Asian nations that are now in crisis have or have had a high domestic savings rate, and I am concerned about its effect on the crisis, if it serves as a buffer, do they matter, do savings rates matter? Does it sends us a lesson about United States policy on savings when we're at a point in our history were we considering reforming a tax system and replacing the income tax system with one that incentivizes savings, when we're looking at personalizing and modernizing the Social Security system and that provides us an opportunity to increase domestic savings, what would you say?

Mr. BERGSTEN. The high savings rates in Asia have been one of the great underpinnings of their economic success over the past three decades. We cannot let the current crisis obscure the fact that this has been the most successful economic development story in history, starting with Japan and running through the newly industrialized countries into Southeast Asia. One of the fundamentals underlying that has been the high savings rates. It enabled those countries to invest very large amounts of their national product. That enabled them to have high productivity growth. That enabled them to have high economic growth and rising per capita incomes unparalleled in human history.

They have now had a crisis. What happened? What happened was that some small but significant portion of those savings got invested in imprudent and noneconomic ways. That was partly because their banking systems were not very effective in channeling the savings to the most appropriate and profitable investment returns. It was partly because their corporate structures led some of the lending into unproductive uses and crony kinds of capitalism, insider kinds of projects and the like, which finally came to a screeching halt. But the high savings rates, far from being blamed for the crisis, should be giver credit for much of their success. The continuation of those savings rates is probably the single strongest reason why we can expect the Asian countries to recover from their crisis and get back on a rapid growth track within the next few years, assuming we, the IMF, and everybody else helps them through this difficult adjustment period.

Mr. SWEENEY. I concur with what Dr. Bergsten is saying. I would add, by way of contrast, that if you compared the situation in Asia today in terms of their savings rates, and you compare the situation in Latin American, you find that many of the same causes of the Asian crisis were present in Latin America when they went through their crisis in the eighties—imprudent investments, lack of financial transparency, crony capitalism, governments intervening too much in the markets, lack of deregulation, only in the case of Latin America, they had extremely low savings rate and Latin America financed much of its imprudent activity with foreign borrowing. Today, Latin America, despite all the reforms that have been made, is still struggling to get out of the hole. They're way, way behind the curve and years will pass before they catch up, and one of the reasons is that they have such a low savings rate. So I do agree entirely with what Dr. Bergsten is saying.

Chairwoman DUNN. Thank you, and, actually, that, with the exception of Chile, that has a high savings rate and actually was well-buffered against that very effect.

Mr. SWEENEY. Which they did by privatizing their Social Security system which is something that I'd like to see our legislators do.

Chairwoman DUNN. Exactly.

Mr. McDermott.

Mr. MCDERMOTT. I just have one question since we have two experts, Mr. Sweeney and Mr. Bergsten, here—economist-type experts. Most Americans look at the this bailout as being similar to the bailout of savings and loans where the U.S. Government got stuck for billions of dollars. I would like to hear your explanation because Mr. Gadbaw said the IMF has never cost the taxpayers a penny and if it's no cost—well, then why do we have to put $18 billion into it. You answer my constituents, cause I get that question on the stump and I think that's the biggest obstacle for getting the support of the House of Representatives, is how do you answer to people on the stump in your district, well, what's the $18 billion go for if I'm not paying for those rotten banks in Indonesia? So, right, it's a fair question, and Mr. Gadbaw's right. Let me try to explain it. Tell me how it works in layman's language.

Mr. BERGSTEN. The IMF money that is lent to Korea enables Korea to overcome a cash crunch, a liquidity crisis. Korean banks and firms borrowed much more money in foreign exchange—in dollars—than they had dollars in hand to repay. When confidence collapsed and the foreign lenders, rather than rolling over those loans, wanted to collect, the Koreans didn't have enough dollars. It's a cash crunch and liquidity problem.

That is totally different from the insolvent situation of a lot of Korean banks and companies. Insolvency, meaning bankruptcy is not illiquidity. The country Korea is not bankrupt. It's not insolvent. It's got tremendous assets, but it over borrowed at short maturity and ran into a liquidity crunch. So the IMF lends Korea, the country, money to overcome its liquidity crisis.

Korea, the country, meanwhile, is doing with its banks and its companies what we did internally with our S&L's. The Korean Government is going to have to put up a lot of money to take the bad loans off the books of its domestic banks. But that's an internal transfer within Korea. All that the external side does is help tide it through the liquidity crunch, give it time to put constructive, sustainable economic reform measures in place so it can come out of the crisis in a reasonably healthy way.

Mr. MCDERMOTT. And when do they pay back the money to the IMF?

Mr. BERGSTEN. They pay back on the IMF schedule which will require them to divert some small portion of their export earnings over the next 3 to 5 years, like they repay the private banks that have lent them money and any other foreigner. But, again, that's the country Korea taking some of the country's export earnings and channeling them to repay the foreign creditors. That's a completely separate set of transactions from the internal resolution of their bankruptcies and insolvent bank conditions.

Mr. MCDERMOTT. So, basically, you're banking on the fact that the Korean economy ultimately will get back up on its feet and therefore be able to pay the IMF back at some point.

Mr. BERGSTEN. That is correct. The IMF's objective is to enable the Koreans to get back on their feet in a healthy way, avoiding excessive depression, excessive decline in the exchange rate, import controls, and so forth, to do it in a healthier and constructive way, reform their banking system, reform their corporate governance. All this takes time which the IMF liquidity support provides the basis for doing. If they didn't have the external help from the IMF or us or anybody, they'd have to do something precipitous, and that would mean import controls and deep recession—what happened in the thirties, and what the IMF was created to avoid.

Mr. MCDERMOTT. Let me go then to the second part of it. One of the things that was said was that we shouldn't put conditionality on the IMF. What harm would it do for the Congress to say to the IMF, If you give money to a country, they have to do x, y, and z, in their banking sector?

Mr. BERGSTEN. The IMF does that.

Mr. MCDERMOTT. I know they do that, but we're just gilding the lily. Why do people oppose us putting that in the language when we put the money out there? It makes some Members more comfortable to say, I don't want you bailing out any of those imprudent Korean banks or whomever. What's the harm in doing that?

Mr. BERGSTEN. If you look at the IMF program for Korea that now exists, it says in three different places Korea has to adopt the so-called Basel core principles which are 25 internationally agreed principles that guide the creation and implementation of a sound domestic banking system. It includes letting bad banks go bust. It means taking bad loans off the books of the good banks. I don't see why anybody would object.

Mr. MCDERMOTT. So what you're basically saying is that most Congress people don't understand what the IMF Program is really all about, it's already being done. You wouldn't say that, right?

Mr. BERGSTEN. I didn't say that. [Laughter.]

Mr. MCDERMOTT. Mr. Sweeney, do you want——

Mr. SWEENEY. Well, I don't know if I can give a more articulate answer than Dr. Bergsten can give. I will say though that we can assume that South Korea is going to do the right thing. Certainly, they appear to be moving in the right direction. But then, of course, you've got the case of countries like Indonesia where there is considerable resistance at the government level to implementing with or without IMF aid, the kinds of reforms that Dr. Bergsten is talking about that are so necessary for the region.

And I come from a slightly different position. I think the Heritage Foundation's position on the IMF bailout and the IMF itself is well known; I won't go into that. I brought some literature with me that you may read at your convenience, sir. But I will point out as a person who has lived for 33 years in countries, many of which were candidates for IMF bailouts, the problem I have with such bailouts is that they do distort the market mechanism; they do delay market-driven reforms and solutions to problems that lead to these financial crises in the first place.

A specific case of Mexico, it's been bailed out four times in 20 years. I believe they'll be back in Washington in the year 2000 or 2001 asking for another bailout. In the specific case of Venezuela that took a bailout in 1989, or an IMF Program in 1989, there were riots in that country in 1992, there were two military coup attempts and the president was impeached and removed from office in what amounted to a constitutional coup.

And the issue is that if you accept that the market is 99 percent psychology, when a country is in crisis, and it goes to the IMF and it accepts the IMF Program, these reforms are always politically unpalatable, especially in countries which aren't very democratic or have weak democratic institutions. When the market turns up again, and psychology investor confidence recovers, and money starts coming back into the country, governments invariably put off carrying out the kind of institutional reforms that were needed to prevent these crises from occurring in the first place. And what's left are populations in these countries that are very impoverished, very resentful socially and politically, and which contribute to a great extent to political instability.

That is the case in Mexico today. I think you will see, despite the fact that Mexico's been growing quite well in the last 2 years, over the next 4 or 5 years a gradual increase in political instability in that country. That is the case in other countries like Venezuela where I see more problems on the horizon.

That's what concerns me about the IMF bailout. I think that by distorting the market, you are basically laying the seeds for future disorder and unrest, and that, in and of itself, is also not good for investment in these countries.

Chairman CRANE. I want to thank you for your testimony and apologize for Mr. Matsui for not being able to be here while you guys testified, but we appreciate it and I would now like to invite our next panel of witnesses, Hon. Stuart Eizenstat, the Under Secretary for Economic, Business and Agricultural Affairs at the State Department, and Hon. David Lipton, Under Secretary for International Affairs at the Treasury Department. And you gentlemen may proceed in order. I know you're on tight time constraints too, so fire when ready.

STATEMENT OF HON. STUART E. EIZENSTAT, UNDER SECRETARY FOR ECONOMIC, BUSINESS, AND AGRICULTURAL AFFAIRS, U.S. DEPARTMENT OF STATE

Mr. EIZENSTAT. Thank you, Mr. Chairman. As I explained to you when my time was rescheduled from this morning, I have to leave at 1:45, and I appreciate your accommodation.

It is in our interest to lead and act in the international effort to address the financial crisis in East Asia. This is not just a test of our leadership in the IMF, or our international economic leadership, but it is a test of our political leadership in a changing global environment as we enter the 21st century.

Our engagement at this time of financial unease helps assure our ability to mobilize support in the future for a whole range of issues important to the United States, and enhances our capacity to promote greater openness, democracy, and support for human rights in Asia.

If we shrink away from our leadership responsibilities as we would be doing if we did not pass the IMF package, other forces will fill the vacuum in Asia. Our own security is closely linked to peace and stability in East Asia. In a little over 50 years, we fought three costly wars. Nearly one-half of the Earth's population lives in countries bordering the Asian-Pacific region, and over one-half of all economic activity in the world takes place there. Four of the world's major powers rub shoulders in Northeast Asia while some of the most important sea lanes on the globe pass through the confined waters of Southeast Asia and specifically, next to and through

Indonesia. And this chart that we have demonstrates the vital sea lanes that are involved.

We are as much a Pacific as we are an Atlantic nation, and what happens in this region directly affects and has a profound impact on the United States. We have 100,000 troops in the Western Asian-Pacific region. Our forward military presence helps bolster stability in the region. And this stability has been the essential foundation for unprecedented economic, political, and social progress in East Asia over the past several decades. A part of the world once known for authoritarian governments, for internal strife, and international tension, is now increasingly characterized by viable and exciting democracies in the Philippines, in Thailand, in South Korea, and in Taiwan, that are adopting more open economic policies, alleviating poverty, and modernizing.

The current economic difficulties, if not halted, could threaten this stability and much of the progress made over a generation. The markets are not only looking for economic adjustments but also for the political will in these countries to implement tough structural reforms. The economic and political dimensions of this crisis are closely intertwined. The countries hardest hit are among our closest and most vital friends and allies.

South Korea is our fifth largest export market with whom we've had a $26 billion trade surplus over the past 3 years. We have 37,000 American troops deployed there. A South Korea weakened by economic distress would raise the risk of miscalculation by North Korea and of conflict on the volatile Korean Peninsula. It would make the vitally important efforts to dismantle North Korea's dangerous nuclear program more difficult.

Thailand is one of our closest friends in the region and a supportive ally for many decades. We've had a treaty relationship with Thailand since 1954. We enjoy a very close military-to-military relations, and access to strategic airbases in Thailand. I think it would be important at this time to remind everyone that Thailand provided essential overflight clearances and the use of airbases during the gulf war.

Indonesia is the world's fourth most populous country. In recent decades, it's played an increasingly constructive and influential role in the region. It spans important seaways and airways, and possesses rich natural resources. It's provided moderate leadership which has allowed ASEAN to prosper and more recently has been a driving force within APEC in favor of trade liberalization. It has contributed to peacekeeping efforts in Bosnia and Angola. And, just as important, it's a moderate secular state. It has the world's largest Muslim population. More Muslims live in Indonesia than in all the other Middle Eastern nations combined. Because security, economics, and politics are so closely intertwined, we have repeatedly emphasized to the Indonesian Government the importance of full implementation of the IMF structural reform program, as well as the importance of putting in place a knowledgeable, experienced economic reform team which will have the confidence of the markets. This is a message that Ambassador Mondale will be delivering when he is in Indonesia next week.

The core countries of ASEAN—whom you see on this map, Thailand, the Philippines, Malaysia, Singapore, and Indonesia—are longtime friends whose prosperity and progress have contributed to increasing regional stability. ASEAN, founded 30 years ago to bolster regional stability, has done just that, and it's continued to grow in stature. But we must not take that for granted.

Only a few decades ago, this was an area characterized by bloody insurgencies, shooting wars, Indonesia's confrontation with its neighbors, and communal killings. The changes since then have been astounding, but prolonged economic crisis could revive internal instability in these countries and provide fertile ground for extremism. Millions of foreign guest workers work in these economies. Prolonged instability will generate an increased flow of economic refugees. In a region where old suspicions and ethnic rivalries persist the risk of instability spreading is very real.

A peaceful and stable Asian-Pacific is a region that will remain open to United States influence, ideas, and trade. If we appear unengaged, we will cede, however, to the political and diplomatic influence of others, and the economic opportunities that go with it.

The economic health of East Asia is also important to our prosperity. Since 1993 increases in United States exports have accounted for one-third of total United States economic growth and created one of every seven new jobs, but almost 20 percent of those exports go to the East Asian emerging market. A large portion of the exports from the west coast go to East Asia. In 1996 almost 60 percent from Washington State—almost 60 percent—almost 60 percent from Oregon, 51 percent from California, and States that you wouldn't think of having large impacts: 45 percent from Nebraska, 42 percent from Utah, 37 percent from Louisiana, 26 percent, Mr. Chairman, from Illinois.

Continuing deterioration of the economies will mean lower exports and ultimately job loss here at home. We'll see a noticeable increase in our trade and current account deficits. This will create economic challenges and political problems and fuel protectionist pressures. The longer this instability persists, the more chance there is that other economies will also be pulled down as the contagion spreads increasing the global costs. Only the international community and its multilateral institutions like the IMF and the World Bank can perform the task of stabilizing these economies.

Most importantly, we have engaged in assisting Asia through the IMF. As my colleague David Lipton will explain in more detail, these structural programs, if fully implemented, offer the best chance for these countries to resume their impressive economic growth.

It's not only in our economic, but also in our political and security interests to support the New Arrangements to Borrow and the quota increase. Neither will cost the U.S. taxpayer a dime over 50 years, indeed, Congressman McDermott, in answer to your question, we get back special drawing rights as an asset, which ve have used before. In 1978 when I was in the White House, we actually borrowed against that.

If we should appear to turn our back on an institution we have created just when the IMF is playing an essential role in this recovery, we will send a negative signal to the markets and a devastating message about U.S. leadership and engagement in this critical area. Many of the measures required by the IMF to restructure the economies of East Asia will provide expanded opportunities for United States companies, and David Lipton will describe in detail how this helps our own security and how they are performing what we for decades have tried with less success to do. With a stroke of a pen, the IMF has been able to open these economies.

Less tangible but of equal importance is the fact that many of the countries in deepest crisis are societies that have been opening up not only economically, but politically. Thailand, South Korea, and the Philippines are shining examples. Why has that happened? It has happened because over the last several decades a middle class has been created in these countries and that middle class is dedicated to human rights and to the protection of democratic institutions. These are the very groups most at risk if we allow these countries to go under economically.

The course of development that we prefer—open, more democratic societies coupled with open and competitive economies—would be jeopardized if the turmoil continued. It is critical also that less open countries in this region—China, Vietnam, Burma—not draw the wrong conclusions from the difficulties of these democracies.

We have enjoyed many of the benefits of leadership on the world stage—the ability to protect our interests, to prosper from the global reach of our economic power, and to see the values and principles we hold most dear not only endure but spread. But leadership is not divisible. We cannot expect to lead these countries on security issues, expect Thailand to help us with basing rights, and then when they are in trouble, turn our backs, abdicate leadership in the more difficult and often messy international economic area. As leaders of the international system, we have much to gain and they look to us to provide leadership.

To turn from the task at hand would not only risk stability abroad but threaten our prosperity at home. It would mean resentment from our friends, turning our backs on them at the time of their plight. We'd lose credibility and goodwill, hurting us not only in terms of pushing needed reforms, but in pushing our broader agenda.

So to sum up, we must be involved in leading this effort as our vital security and political, not just economic, interests are at stake. We must support the IMF Programs. We must provide political support and technical assistance to help with their reforms. We must remain committed to opening markets at a time when the current account deficit will rise, and recognize that an increase in our current account deficit is a natural consequence of the crisis, and that the IMF Programs are the best way to restore demand for U.S. exports in the affected countries. We must continue to promote their openness and transparency and accountability. At a time when they are saying, Should we continue on this course given this crisis, we need to answer with a resounding, Yes.

We should encourage other countries—the Europeans, China and Japan—to join us and do their share. We should welcome Chinese assurance that they will maintain a stable exchange rate, a very important contribution they are willing to make. We should urge Japan to take broader responsibility as the main engine of growth in the region. Just as we are willing to do our part, Japan must do the same to stimulate domestic-led growth and open its market. Most important to this effort is trade liberalization, effective deregulation, a genuine tax reduction, and resolution of its banking problems.

Thank you very much, Mr. Chairman. I appreciate your time and will defer now to my colleague, David Lipton.

[The prepared statement and attachment follow:]

Statement of Hon. Stuart E. Eizenstat, Under Secretary of State for Economic, Business, and Agricultural Affairs, U.S. Department of State

ASIAN FINANCIAL CRISIS: BROADER IMPLICATIIONS

Mr. Chairman and members of the Committee. It is a privilege to appear before you today. By including the Department of State in a hearing on the Asian financial crisis you recognize that for the United States, the ramifications of the current economic difficulties in Asia affect much broader interests.

Mr. Chairman, as we consider the United States' proper role in confronting this situation and what actions are necessary and appropriate for us to take, we must fully understand the broad dimensions and implications of this crisis. Vital U.S. interests of great importance to the security, the prosperity and the values of the American people we all serve are at stake. Therefore, we believe strongly that it is in our own interest to lead and act in the international effort to address the financial crisis in East Asia. In this effort, the leadership of the Congress is also crucial and we look forward to working with you on this important issue.

The role of the United States is not just a test of our IMF leadership or international economic leadership, but our political leadership in a changing global environment as we enter the 21st century. Our engagement at this time of financial unease helps assure our ability to mobilize support in the future for a whole range of issues important to the United States and enhances our capacity to promote greater openness, democracy, and support for human rights in Asia. On the other hand, if we shrink away from our leadership responsibilities, other forces may prevail.

SECURITY

Mr. Chairman, our own security is closely linked to peace and stability in East Asia—in a little over fifty years we have fought three costly wars there. Since World War II our security policy in the Western Pacific has stressed stability and the deterrence of conflict. Nearly one half of the earth's people live in countries bordering the Asia Pacific region and over one-half of all economic activity in the world takes place there. Four of the world's major powers rub shoulders in Northeast Asia while some of the most important sea lanes on the globe pass through the confined waters of Southeast Asia and specifically, next to or through Indonesia. We are just as much a Pacific nation as an Atlantic nation, and what happens in the Asia Pacific region directly affects us and has a profound impact in the U.S. and throughout the world.

Today we have 100,000 troops in the western Asia Pacific region. Our forward military presence and active engagement in the western Pacific has increased and bolstered stability in the region. This stability has been the essential foundation for unprecedented economic, political and social progress in East Asia over the past several decades—progress from which we have greatly benefited.

However, it goes further. Just as increasing peace and stability have enabled economic progress, so too have economic progress and the better life it has brought to hundreds of millions of people reinforced peace and stability. A part of the world once known for authoritarian governments, internal strife and international tension is one now characterized by viable exciting democracies—in the Philippines, Thailand and South Korea—that are adopting more open economic policies, alleviating poverty and modernizing.

Mr. Chairman, the current economic difficulties, if not halted, could threaten this stability and much of the progress made over a generation. The markets are not only looking for economic adjustments, but also for the political will in these countries to implement tough structural reforms. The economic and political dimensions of this crisis are closely intertwined—the markets will respond favorably when they see the sustained political will to make the reforms work.

The countries hardest hit are among our closest and most vital friends and allies—including South Korea where 37,000 American troops remain deployed to ensure an uneasy peace in the face of the continuing threat from North Korea. A South Korea weakened by economic distress raises the risk of miscalculation by North Korea and conflict on the volatile Korean Peninsula. While we anticipate that the South Koreans will stand by their commitments, it makes more difficult our vitally important effort through the Agreed Framework of 1994 and the Korean Peninsula Energy Development Organization (KEDO) to dismantle the dangerous North Korean nuclear program, where a large contribution from South Korea will be necessary. It could well complicate our delicate efforts through the Four Party Talks to secure a permanent peace and bring the Korean War to a formal end. The economic crisis could also strain the ability of countries such as South Korea and Japan to continue to share the financial burden of maintaining security in the region.

Thailand is one of our oldest friends in the region and has been a close, supportive ally for many decades—from the Korean War through the Indochina conflict all the way to the present day. We have a treaty relationship with Thailand dating from 1954. We enjoy very close military-to-military relations and access to strategic airbases in Thailand. Thailand provided essential overflight clearance and the use of airbases during the Gulf War and subsequent actions against Iraq. Our longstanding friendship has resulted in close cooperation on a broad range of issues, including most recently in counternarcotics where Thailand has extradited an unprecedented 11 indicted traffickers to the U.S. since 1996, environmental protection, medical research and improved intellectual property rights enforcement.

Indonesia, the world's fourth most populous country, has in recent decades played an influential and constructive role in the region, which serves our interests as well as those of the people throughout the region. Indonesia spans important seaways and airways and possesses rich natural resources, which give Indonesia broad strategic value. Where its assertive nationalism once unnerved its smaller neighbors, in recent decades Indonesia has provided the moderate leadership which has allowed ASEAN to prosper and more recently has been a driving force within APEC in favor of trade liberalization. Indonesia has also contributed to peacekeeping efforts in Bosnia and Angola, supported nonproliferation efforts such as the Comprehensive Test Ban Treaty, and joined KEDO. Just as importantly, Indonesia, a land of many diverse peoples, languages and cultures, is a moderate secular state—with the world's largest Muslim population—more than in the Middle East nations combined.

We want to help Indonesia overcome its social problems—problems which could exacerbate social tensions and rekindle nationalistic excess. Because security, economics and politics are so closely intertwined, we have repeatedly emphasized to the Government of Indonesia the importance of full implementation of the IMF structural reform program, as well as the importance of putting in place a knowledgeable, experienced economic reform team which will have the confidence of the markets.

The Philippines has not been as hard-hit by the financial turmoil as Thailand and Indonesia, but remains vulnerable to continued turmoil in the region. The Philippines has been a close friend since its independence in 1946 and a treaty ally since 1952. In recent years it has achieved remarkable success in the difficult task of rebuilding its democracy and economy following the final, chaotic Marcos years. We do not want that record of success undermined.

The core countries of ASEAN—Thailand, the Philippines, Malaysia, Singapore and Indonesia—are long-time friends whose prosperity and progress have contributed to increasing regional stability. ASEAN, founded 30 years ago to bolster regional stability, continues to grow in stature. Evidence of its growing maturity is ASEAN's continuing constructive role in Cambodia. Through our bilateral ties with the individual members, our participation in the ASEAN Regional Forum, our other high-level dialogues with ASEAN and by our active role in APEC, the United States has been able to strengthen its overall relationship with ASEAN.

We should not take ASEAN's success for granted. The peace and progress it has helped bring to Southeast Asia may seem natural. But go back to the mid-1960s—there was tension, there were bloody insurgencies, there were shooting wars, such as the Indochina conflict and Indonesia's confrontation with its neighbors, and there were communal killings. The changes since then have been astounding, but prolonged economic crisis and the attendant joblessness, impoverishment and despair could revive internal instability in these countries and provide fertile ground for extremism. Millions of foreign guest workers work in some of these economies, while other ASEAN countries provide large number of workers to their neighbors. There already exists increasing pressure to send them home. Prolonged instability will generate an increased flow of economic refugees. In a region where old suspicions and ethnic rivalries persist, the risk of instability spreading is real.

With the end of the Cold War the security landscape in East Asia is evolving. During this delicate transition period it is important that the nations of the region remain strong and that confidence in U.S. leadership remain firm. A peaceful and stable Asia Pacific is a region that will remain open to American influence, American ideas and American trade, if we show continued leadership. But if we appear disinterested or unengaged, we will cede to others political and diplomatic influence—and the economic opportunities that go with this influence.

PROSPERITY

Mr. Chairman, I have begun by discussing security and political issues. However, security is not just an end in itself but a means of assuring the welfare and prosperity of our own citizens, one of the principal duties of any government. The economic health of East Asia is important to our own prosperity. The dynamism of the region has provided increasing trade and investment opportunities to American companies, creating jobs here at home. The growth of exports has helped fuel our economic expansion. In recent years, our participation in the global economy has been fundamental to our sustained growth, low unemployment and low inflation.

Let me share with you just a few statistics, Mr. Chairman, which illustrate the importance of trade and exports to our economic well-being:

- Last year total imports and exports reached about 25 percent of our gross domestic product—up from just 8 percent in 1950 and 11 percent in 1970.
- Since 1993, the increase in U.S. exports has accounted for more than one-third of total U.S. economic growth and created one in seven new jobs; almost 20 percent of U.S. exports go to the East Asian emerging markets (Korea, Thailand, Indonesia, Malaysia, Philippines, Singapore, China, Hong Kong and Taiwan).
- In global terms, more than eleven million Americans now work in jobs supported by exports; these jobs pay 13–16 percent above the national average wage. The western Pacific (the above mentioned countries, Japan, Australia and New Zealand) is our most important regional market taking 30 percent of U.S. exports.

A look at individual state figures further underscores the importance of trade to this region. A large portion of the exports from our west coast states goes to East Asia—in 1996, nearly 58 percent for Washington, 57 percent for Oregon and 51 percent for California in 1996, with a total value of some $76 billion. Even more remarkable are the high numbers in other parts of the country—45 percent for Nebraska, 42 percent for Utah, 37 percent for Louisiana, 26 percent for Illinois and 21 percent for New York.

The benefits of this growing trade have been widely spread, and so would be the costs of a downturn. Continuing deterioration of the Asian economies, and the further depreciation of their currencies which makes their goods cheaper and hurts our competitiveness, will mean lower U.S. exports, fewer contracts for U.S.-supplied services and ultimately job loss here at home. There will be more pressure on our balance of payments as Asian economies buy less but seek to export more. We will see a noticeable increase in our trade and current account deficits. This will create economic challenges and political problems as well, fueling protectionist pressures.

A further hazard from the financial crisis lies in the fact that the longer the uncertainty and instability persist, the more chance there is that other economies will be pulled down as well. This contagion factor could spread the crisis beyond the immediate region, increasing the likelihood of more severe global costs and more severe costs to us. Mr. Chairman, when an infectious disease breaks out, counteraction to limit the spread of the disease and panic must be swift, determined and comprehensive. Only the international community and its multilateral institutions can perform this critical task—again underscoring the critical importance of Congressional approval of the IMF package. Only the United States can provide the leadership for this effort.

In the exercise of this leadership, we are encouraging other nations to contribute as well. Working with the G–7, the European Union and the Organization of Economic Cooperation and Development, we have agreed on the importance of maintaining an open global trading and finance system to help the affected Asian economies recover. With the G–7, we are putting together an initiative to provide urgently needed short-term trade finance (described in more detail below). China has made an important contribution to regional stability by agreeing to maintain its exchange rate at current levels.

We are also urging Japan to step up its efforts. We strongly agree with the view of the IMF that fiscal stimulus is needed to support Japan's economy and make it a potential source of confidence for the region. Japan is the economic engine for Asia. Since the beginning of the Asian financial crisis last July, Japan has been in the forefront of countries assisting in the IMF-led debt relief and structural adjustment programs. However, the most important contributions Japan can make to regional economic recovery are to strengthen domestic demand, deregulate its economy, open its markets to imports of goods and services, and strengthen its financial system.

Most importantly, we have been engaged in assisting Asia to recover through our economic leadership in the International Monetary Fund (IMF), in addition to offering a second line of defense to Korea and Indonesia, not only because they are our customers, but because they are our security partners. The IMF structural reform programs, if fully implemented, offer the best chance for these countries to resume their impressive economic growth—that made them the envy of the world—on a more sound, sustainable basis. For this reason, it is not only in our economic interests, but our political and security interests, to support the IMF New Arrangements to Borrow and the Quota Increase—neither of which will cost the U.S. taxpayer a dime, but will pay rich dividends over time.

As a founder and the largest shareholder, our active involvement and support is essential to the IMF's efforts to solve the East Asia economic crisis. Mr. Chairman, the IMF has changed and adapted through the years, and it will continue to do so. Indeed, President Clinton has called for a meeting of Finance Ministers to consider how the international community can better address such challenges. However, if we should appear to turn our back on an institution we created just when the IMF is playing an essential role in this recovery, we will send a negative signal to the markets and a devastating message about U.S. leadership and engagement in the post-Cold War era.

BENEFITS FOR U.S. TRADE AND INVESTMENT

For years we have argued that open trade and more open economies are the path to greater prosperity. There has been resistance to this view—the political and economic structural reforms needed to accomplish this can be difficult and painful for all of us. This crisis has shown the merits of more open, transparent and rational economies and the cost of allowing distortions to continue. The reforms and corrections required in IMF-led programs address these issues and should lead to greater trade and investment opportunities for all of us—including the United States.

Many of the measures required by the IMF to restructure the domestic economies of East Asia will provide expanded opportunities for U.S. companies. In the end, their economies will be more open, transparent, and predictable. Indeed, the IMF has accomplished in a few short months what the U.S. has pressed for years, even decades:

- from elimination of trade-related subsidies to harmonizing import certificate procedures in accord with WTO standards;
- from binding liberalization of financial services to increasing opportunities for foreign investment;
- from eliminating import monopolies to reducing tariff levels.
- from eliminating restrictive import licensing practices to ending directed lending based on political factors, which had led to over-capacity in some sectors that compete with U.S. producers.

Recognizing that a lack of financing restricts trade flows in the various Asian economies, has a detrimental effect on their local economies, and limits the export of goods and services to these key markets, the G–7 Export Credit Agencies, including the Export-Import Bank of the United States, meeting in London on February 21 approved a practical and immediate initiative to help stabilize Asian markets. This initiative will provide continued and if possible expanded, short-term credits to Indonesia, Korea and Thailand to support trade financing for critical imports.

A senior Korean official told me that the inability of businesses to secure this vital financing meant that businesses could not produce. As a result, in Korea imports had plunged 40 percent, while exports had increased less than 2 percent. In addition, the U.S. Department of Agriculture is providing the affected countries this year over $2 billion in commercial export credit guarantees for critical food and agricultural imports. Our export credit assistance not only helps these countries keep their businesses in operation, but also helps to maintain the export linkages U.S. companies have established in these markets.

U.S. VALUES AND CREDIBILITY

Less tangible but of equal importance is the fact that many of the countries in deepest crisis are societies that have been opening up not only economically but, in many cases, politically as well. This is certainly true of Thailand, South Korea and the Philippines where major advances in democratization have been made. Indeed, I should note that, in these three countries, the institutionalization of accountable government has given their leaders a clear incentive to craft effective responses to their economic distress.

The downturn in these countries will have its greatest impact on the emerging middle class and those struggling to climb up from poverty. One of the greatest successes of the so-called Asian miracle has been to lift tens of millions of families out of abject poverty over the past 20 years. These groups represent the region's greatest hopes for the development of more democratic institutions and greater respect for human rights. The course of development we prefer—open, more democratic societies coupled with open, competitive economies—is jeopardized by the present turmoil. This is true not only within these countries, but for others in the region as well. It is critical that less open countries such as China, Vietnam and Burma not draw the wrong conclusion from the current difficulties.

In this regard the environment, labor standards and human rights are critically important issues which we have been advancing in many ways. We work with the international financial institutions and others throughout the world to promote progress in these areas. In themselves, IMF-led programs commit governments to increase transparency and good governance and promote dialogue within societies, including with labor. These measures promote accountability, the wider sharing of power and citizen participation and the effects can go well beyond the financial realm. The immediate crisis is economic and IMF programs must of necessity focus on immediate actions to restore economic stability and market confidence. To overburden IMF programs with too many goals in other areas during a crisis would complicate and delay the process, greatly reducing the chance of success.

We are nonetheless committed to pursuing these other goals by other means. We will continue to raise human rights and worker rights concerns wherever they arise. In addition, we must be sensitive to the social ramifications of these IMF programs in terms of increased unemployment and widening income inequality, which could lead to political instability. Therefore, we believe it essential to work with the World Bank and the Asian Development Bank to implement supporting programs to establish a social safety net. In this regard the role of the World Bank is as large as the IMF on the financial side.

Mr. Chairman, we have enjoyed many of the benefits of leadership on the world stage—an ability to protect our interests, to prosper from the global reach of our economic power and to see the values and principles we hold most dear not only endure, but indeed spread. However, this leadership is not divisible. We cannot lead on critical security issues, or in opening markets, while abdicating the lead in the sometimes messy work of maintaining the international financial system. This leadership brings responsibilities and burdens. As the leader of an international system from which we gain so much, others look to us to provide the leadership and our fair share of the resources necessary for the success of the international effort underway.

Early in his Administration President Clinton described his vision of a Pacific community of nations, one in which shared burdens and shared benefits lift us all. To turn from the task at hand not only risks stability abroad, but threatens prosperity at home. Moreover, it would also breed resentment toward what would be seen as our indifference to the plight of friends. With that will be a loss of credibility and goodwill that not only hurts our ability to push needed reforms, but also can affect our broader interests—economic and political—including cooperation on security and other important issues in the region and beyond.

This means more than just cooperating in hard times. It also means moving forward on goals set at the APEC Leaders Meeting in Bogor, Indonesia in 1994—a vision of free and open trade and investment in the region by 2010/2020. We have been working in APEC to turn this vision into a reality. The political support of APEC leaders has been critical to the conclusion of the Uruguay Round and the Information Technology Agreement, opening up markets worth billions of dollars to U.S. businesses and workers. APEC's leadership on the world's trade agenda and its goal of regional trade and investment liberalization could be jeopardized by a persistent, festering financial crisis.

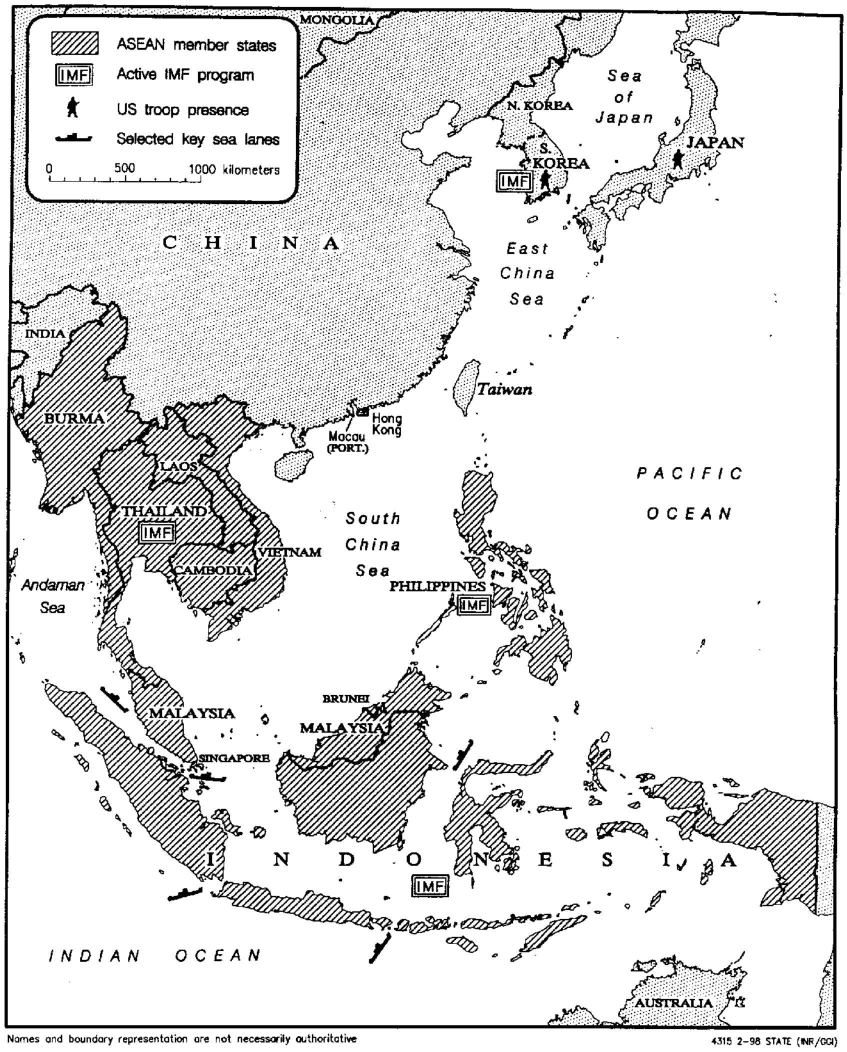
CONCLUSION

Let me sum up what we are doing, should be doing, and should be encouraging others to do to solve the East Asian financial crisis:

- We must be involved in leading this effort as our vital economic, security and political interests are at stake.
- Support the IMF programs underway and ensure that the programs of other international financial institutions, and our own bilateral efforts, help to ameliorate the human cost of these painful economic reforms.

- Provide political support and, where appropriate, technical assistance to help with the necessary reforms.
- Remain committed to open markets at a time when the current account deficit will be on the rise.
- Continue to promote greater openness, transparency and accountability by governments and the private sector to stabilize markets, secure sustainable economic growth, improve the quality of life for the people of the region, and avoid these crises in the future.
- Recognize that an increase in our current account deficit is a natural consequence of this crisis and that the IMF programs will prove the best way to restore demand for U.S. exports in the affected countries.
- Encourage other nations—the Europeans, China and Japan to help us and join these efforts.
- Welcome Chinese assurances that they will maintain a stable exchange rate.
- Urge Japan to take broader responsibility as the main engine of growth in the region. Just as we are willing to do our part, Japan must do the same to stimulate domestic-led growth and open its markets. Most important to this effort are trade liberalization, effective deregulation, and resolution of its banking problems.

Mr. Chairman, I thank you for the invitation to give testimony on this very important issue, and I welcome your questions at this time.



Chairman CRANE. Thank you.
Mr. Lipton.

STATEMENT OF HON. DAVID A. LIPTON, UNDER SECRETARY FOR INTERNATIONAL AFFAIRS, U.S. DEPARTMENT OF TREASURY

Mr. LIPTON. Thank you, Mr. Chairman. I'm pleased to have this opportunity to discuss the recent developments in Asian financial markets, the effects on our economy, and the role of the IMF. As the President said in his State of the Union address, the Asians are our customers, our competitors, and our allies. Nearly one-third of our exports go to Asia, more than we sell to Europe. Already, many small businesses and some major Fortune 500 companies are seeing reduced export demand in the wake of the instability in Asia. Reduced demand translates into fewer new jobs for American workers.

Fortunately, our economy is in strong shape today so we can expect to withstand the likely short-term effects of this crisis as it has unfolded so far. But the cost would be larger if the Asian economies prove unable to restore stability and the crisis spreads to emerging markets in other regions.

Our approach for resolving the crisis rests on four principles. First, the Asian countries bear the major responsibility for taking action and overcoming the crisis. Second, the international community should offer temporary, conditioned financial support to provide breathing space for countries carrying out needed actions. Third, the major industrialized nations, particularly Japan, must promote balanced growth in their own economies to support the return of market confidence and help accommodate transitional trade imbalances in crisis-affected countries. And fourth, the architecture of the international financial system must be modernized to make us better able to prevent and manage crises.

Bearing in mind the strong interest of this Subcommittee in the trade aspects of programs for the Asian countries, let me turn to that subject. The Asian reform programs contain important liberalization steps aimed at openness and competitiveness. Indonesia's IMF Program commits the government to eliminating a range of officially sanctioned import and export monopolies, removing export taxes on resource products, reforming the government procurement process, and accelerating the pace of privatization. Tariffs on food imports have been cut to a maximum of 5 percent effective immediately.

Similarly, the Thai program includes a greater emphasis on privatization, measures to reduce subsidies to state enterprises, and the loosening of the limitations on foreign ownership and exchange control.

The Korean program includes pledges to eliminate subsidies to Korean exporters, ease export licensing and cumbersome customs procedures, end the government directed noneconomic lending, and substantially ease restrictions on foreign ownership of Korean companies.

Mr. Chairman, it's worth taking a step back to consider what these changes represent. Take the case of Korea. The close relationship between the government, banks, and the chaebol conglomerates has been one of the salient characteristics of the Korean economy for decades. That relationship has been at the root of our persistent trade problems with the country because it resulted in poor market access, uneconomic investments, excessive concentration, and excess capacity in key industries. Tackling these practices has been very difficult using traditional trade policy tools, and that's because those practices could not be changed without altering, fundamentally, the relationship between government and business.

Now, President-elect Kim Dae Jung has embraced an IMF Program that aims not only to overcome Korea's financial crisis, but to break up this preferential relationship once and for all. I believe that development is good for America.

More broadly, our approach to resolving financial crises depends critically on the central role of the IMF. That's why we ask you to support two requests: An increase in our IMF quota subscription, and U.S. participation in an augmented back up facility called the New Arrangements to Borrow, which supplements ordinary IMF resources.

Why is the IMF central to resolving the Asian crisis? By imposing policy conditions, the IMF supports the right policies. By injecting short-term finance, it prevents further currency depreciation and supports the return of long-term growth. It promotes changes that are in our long-term interests such as making these economies more open to foreign trade and reducing domestic subsidies. And it provides us maximum burden sharing; each dollar we contribute leverages four or five from the rest of the world.

I thought it would be helpful for me to say a few words about the financing structure of the IMF. I understand there were questions on this in earlier panels. In some ways the IMF operates like a credit union. We extend a credit line to the IMF which it can draw on. Any drawings by the IMF give us a claim, much like a deposit in the IMF, which is of equal value, pays interest, and is backed by over 30 billion dollars' worth of gold, and which we can withdraw, essentially, on demand, if necessary.

For these reasons, the U.S. participation in the IMF is treated as an exchange of financial assets. U.S. transfers to the IMF are not scored as budget outlays and do not come at the expense of domestic programs. The IMF now needs additional resources to be in a position to respond to any worsening of this crisis or to deal with any future crises that might arise.

The likelihood of such developments may be small, but the consequences for America would be large and we cannot afford that risk. Moreover, failure to provide these resources could shake confidence in American leadership in the global economy just at a time when confidence in American leadership is so important in reestablishing stability in Asia.

Looking to the longer term, the United States has taken a lead role in modernizing our tools for dealing with crises. At President Clinton's initiative, the United States will be convening a meeting later this spring with finance ministers and central bank Governors from 22 countries to continue these efforts and start developing a consensus on policies to deal with new challenges facing the international financial system.

Just last weekend, the G–7 finance ministers discussed this subject of modernizing financial architecture at their meeting in London. The issues for discussion included: how to promote more efficient global markets; steps to increase disclosure and transparency; measures to strengthen financial systems, both globally and in individual countries; national policy management to prevent and manage crises; the international community's role in times of crisis; and appropriate burdensharing by the private sector to treat the so-called moral hazard problem.

These issues are as complex as they are important. Some will take time to work through and then to reach consensus with others in the international community. Given the high stakes involved, we cannot risk pushing through major reforms before the consequences can be thoroughly examined, nor can we afford to leave the IMF ill prepared to respond until these issues are resolved.

Mr. Chairman, the globalization of financial markets has been a breathtaking development. Huge amounts of capital flow quickly among closely integrated financial systems. Technological change has made possible flows of information and finance on a vast scale. Globalization has thrust the private sector into a predominant role in finance and development around the world. Private capital has financed great advances in productivity and has raised living standards, and in doing so, created new markets for U.S. goods. Globalization has created great new opportunities for Americans. At the same time, globalization brings new risk.

The Asian crisis will likely be viewed as the first crisis of the new global economy. Making the most of our opportunities while minimizing the risks will be a central issue for this Subcommittee and the nation in the years ahead.

Thank you.

[The prepared statement follows:]

Statement of Hon. David A. Lipton, Under Secretary for International Affairs, U.S. Department of Treasury

Mr Chairman, I am pleased to have this opportunity to discuss recent developments in Asian financial markets and the effects on our economy.

Today I would like to focus my testimony on the Administration's strategy for restoring stability in Asia. I would also like to speak about the critical need to support the IMF so we can maintain our capacity to respond to financial crises around the world.

I. The Risks Posed by the Instability in Asia

As the President said in his State of the Union Address, the Asian economies are our customers, our competitors and our allies. The financial turmoil in the region is affecting growth in our economy, and thus is affecting the well-being of American workers, businesses and farmers. Our aim is to restore stability for these key markets as soon as possible.

Nearly one third of our exports go to Asia—more than we sell to Europe. Already many small businesses and some major Fortune 500 companies are seeing reduced export demand in the wake of the instability in Asia. Reduced demand translates into fewer new jobs for American workers.

Our economy is in strong shape today, so we can expect to withstand likely short-term effects of the crisis as it has unfolded thus far. But the costs could be much larger if Asian economies prove unable to restore stability and if the crisis were to spread to emerging markets in other regions. Prolonged instability in Asian and other markets could:

- lead to a cycle of competitive depreciation and trade barriers;
- threaten American exports and the jobs that depend on them;
- affect our own financial markets, imperiling those who rely on them for investment finance, personal incomes and mortgages for new homes; and
- raise national security concerns, if the financial crisis were to lead to broader conflicts. Under Secretary Eizenstat addresses this risk in some detail in his testimony for today's hearing.

In short, the risk of failing to respond to this crisis—the risk for our economy, the stability of our financial markets and our broader national security—far exceeds the risk of action. We can, and we must, work with the international community to help restore confidence and growth as soon as possible—so that these nations can continue to be strong markets and stable allies for the United States.

II. THE UNITED STATES' APPROACH

As Ambassador Barshefsky mentioned earlier, the U.S. economy is strong and our ability to weather the Asian crisis is better at this time than virtually any other time. However, we are highly integrated into the global economy and rely upon these markets for a significant share of our exports. Therefore, it is in our interest to strengthen the markets in Asia. Our approach rests on four principles:

- first, the major responsibility for overcoming crisis rests with the countries themselves and the actions they are prepared to take;
- second, the international community should be prepared to provide temporary, conditioned financial support for countries to provide breathing space for carrying out reforms;
- third, the major industrialized nations, particularly Japan, must promote balanced growth in their own economies to support the return of market confidence and to help accommodate transitional trade imbalances in crisis-affected countries; and
- fourth, the architecture of the international financial system must be modernized to make us better able to prevent and manage crises.

Let me give you a more detailed explanation of these principles, focussing on the first two, which involve the IMF.

A strong domestic response in the countries facing crisis is the absolute prerequisite for restoring stability. The reform programs we have supported in Thailand, Indonesia and Korea commit these countries to concrete actions to restore stability and lay a surer foundation for long-term growth.

While each program is tailored to address the specific causes of that country's crisis, the focus throughout has been on making economies more market-oriented and better able to allocate capital and to allow market forces to operate. Important, long overdue changes need to be made in the structure of these economies—changes which have been welcomed, in many cases, by officials in the countries themselves. The major reform areas include:

- restoration of appropriate monetary and fiscal policies, and agreement on stable and transparent rules for policy makers for the longer term.
- measures to strengthen the domestic financial system, (through financial sector restructuring, improved transparency, and supervision), elimination of interrelationships between government and business that lead to inefficiencies and corruption, and opening of domestic capital markets.
- structural reforms to break up commodity monopolies and open protected sectors to foreign competition.

Bearing in mind the strong interest of this committee in the trade aspects of these programs, let me say a little more on that subject.

Indonesia's stabilization package commits the government to eliminating a range of officially-sanctioned import and export monopolies, removing export taxes on resource products, reforming the government procurement process, and accelerating the pace of privatization. Tariffs on food imports have been cut to a maximum of 5 percent, effective immediately.

Similarly, the Thai program includes a greater emphasis on privatization, measures to reduce subsidies to state enterprises, and loosening of the limitations on foreign ownership and exchange controls.

As part of its IMF program, the Korean government has pledged, among other things, to eliminate subsidies to Korean exporters, ease up on import licensing and cumbersome customs procedures, end government-directed non-economic lending and substantially ease restrictions on foreign ownership of Korean companies.

Mr Chairman, it is worth taking a step back to consider what these changes represent. The close relationship between the government, the banks and the chaebol conglomerates has been one of the salient characteristics of the Korean economy for years. That relationship has been at the root of our persistent trade problems with the country, because it resulted in poor market access, uneconomic investment, excessive concentration, and excess capacity in key industries. Tackling these practices has been very difficult using traditional trade policy tools. That is because these practices could not be changed without altering fundamentally the relationship between the government and business. Now, President-elect Kim Dae Jung has embraced to an IMF program that aims not only to overcome Korea's financial crisis, but to break up this preferential relationship once and for all.

More broadly, the design of reform programs and the provision of assistance is centered around the IMF. That is why we ask you to support two critical requests: an increase in our IMF quota subscription, and U.S. participation in an augmented back-up facility, the New Arrangements to Borrow, to supplement the IMF's resources. These additional resources need to be put in place as quickly as possible to enable the international community to be in a position to respond to any worsening of this crisis, or to deal with any future crisis that might arise. The likelihood of such developments may be small, but the consequences for America would be large. We cannot afford that risk. Moreover, failure to provide these resources could shake confidence in American leadership in the global economy just at a time when confidence and American leadership are so important in re-establishing stability in Asia.

The IMF has been and must continue to be the institution we rely upon to support countries with severe balance of payments problems. Its conditional finance, bolstered by additional support from the World Bank and the regional development banks, is key to our approach to crisis management. Moreover, our reliance on the IMF and other international financial institutions has ensured international burden-sharing. In contrast to the Mexican support program three years ago where the United States took the lead, the international financial institutions have been responsible for the bulk of the financing provided.

The industrialized nations are also directly responding to the crisis by helping to support trade flows in the region. At present domestic recession in the affected Asian economies is being exacerbated by a shortage of short-term trade finance. Weighed down by debt, some financial systems virtually ceased to function—making it all but impossible for businesses to obtain credit to import vital goods and materials.

Our own Export-Import Bank is leading a global effort to provide needed trade finance. Providing this support is truly a win-win proposition for the United States: it gives immediate protection to American exports and jobs, while at the same time speeding the long-term recovery of these important markets. Ex-Im has offered enhanced short-term export insurance in Korea and recently announced $3 billion in additional loans and loan guarantees for sale of American products to Korea, Thailand and Indonesia. Other export credit agencies have also joined in the multilateral initiative to support the region's import financing needs.

III. Long-Term Agenda

Mr. Chairman, recent events in Asia leave in their wake an important long-term agenda for the international community. We need to work to reduce the risk of financial crisis and learn to manage them more effectively when they do occur. We need, in Secretary Rubin's words, an international financial architecture as "modern as the markets it serves."

President Clinton began this effort four years ago at the G-7 Summit in Naples. The next year in Halifax, we launched a broad international effort to strengthen safeguards in the global financial system. Two important parts of this initiative were an international program to strengthen disclosure and the development of core principles for supervision of emerging market financial systems.

The United States continues to take a lead role in modernizing our tools for dealing with the crisis. One outgrowth of the Halifax process, the Emergency Financing Mechanism of the IMF, has enabled the institution to respond quickly to problems in a number of Asian countries. More recently, the IMF membership agreed to establish a new set of financing parameters, through the Supplemental Reserve Facility, which provide for shorter maturities and premium interest rates on exceptional programs—this facility is being utilized for much of the program for Korea.

At President Clinton's initiative, the United States will convene a meeting later this spring of Finance Ministers and Central Bank Governors from 22 countries to continue these efforts and start developing a consensus on policies to deal with new challenges to the international financial system. A week ago, Deputy Secretary Summers held a productive, preparatory meeting with his counterparts from these countries. And just last weekend, the G–7 Finance Ministers discussed the subject of modernizing financial architecture in their meeting in London.

In shaping that agenda, we aim:

- to promote measures to make global markets function more efficient, for example through enhanced surveillance and enhanced national supervision and regulation;
- to increase transparency and disclosure, including for a broader range of central bank and commercial bank data;
- to strengthen financial systems in emerging markets and globally, for example, through strengthened banking supervision and wider adoption of Basle Core Principles;
- to improve domestic policy management in emerging market countries;
- to strengthen the role of the international financial institutions in preventing and responding to financial crises; and

• to ensure that the private sector plays an essential role in the resolution of crises.

These issues are as complex as they are important. Some will take time to work through and then to reach consensus with others in the international community. Given the high stakes involved, we cannot risk pushing through major reforms before the consequences have been thoroughly examined. Nor can we afford to leave the IMF ill-prepared to respond until these issues are resolved.

We are already making progress—even in the midst of crisis—on some items in this agenda:

• to strengthen crisis prevention in the future, we have reached agreement with Asian governments on the development of a regional surveillance mechanism to promote Asian financial stability and increase financial market transparency.

• to promote transparency, as a condition for disbursements of financial support in Thailand, Indonesia and Korea, we strongly, and successfully, urged that governments publish their "Letter of Intent" outlining the reform measures agreed with the IMF.

• to reduce moral hazard, we created a new IMF lending facility (mentioned earlier) under which much of the IMF financing is provided at shorter maturities and a premium interest, increasing the incentive for borrowing countries to restore their creditworthiness quickly and regain access to private capital markets.

• to enlist the private sector to play a greater role in crisis resolution, we catalyzed a major private sector effort to extend credit maturities for Korean commercial banks.

To repeat, Mr Chairman, these and other steps must be seen as part of a rolling but accelerated reform agenda to which we are fully committed as an urgent priority.

IV. SUPPORT FOR IMF

Mr. Chairman as I stated earlier, we need to ensure adequate funding for the IMF at this critical time. The President asked, as a supplementary request, for Congress to support the IMF in two important ways: first, through an increase in our quota subscription, and second, by contributing to an augmented emergency facility, the New Arrangements to Borrow.

Mr. Chairman, we have responded to these crises because they raise important risks for our core economic and national security interests, risks that will increase the longer the instability continues—and the further it spreads. We must support the IMF as we work through this crisis, and ensure it is ready to respond to any future crises, because it is, quite simply, the cheapest, most effective way for us to promote those core American interests.

Without the IMF, at times of crisis, there would be greater pressure on the United States to act unilaterally with taxpayer resources to protect our interests without the global leverage the IMF provides.

Today, as much as when it was established with U.S. leadership more than 50 years ago, the IMF acts to promote out economic values and interests. The IMF helped Poland recover from the collapse of communism and become one of the fastest growing economies of Europe and brought Russia back from the brink if hyperinflation. In Argentina, the IMF supported Argentina's economic transformation from a country characterized by anemic growth and hyperinflation to one that enjoys strong growth (8% in 1997), near zero inflation, declining fiscal deficits, and a more private-sector oriented economy. And in Uganda, it has helped promote ten years of successful economic reforms which have generated average annual growth rates, in real terms, of over six percent a year.

By imposing conditions, the IMF supports the right policies. By injecting short-term finance it prevents further currency depreciation—and supports the return of long-term growth. It promotes changes that are in our long-term interest: such as making these economies more open to foreign trade and reducing domestic subsidies. And it provides us maximum leverage: each dollar we contribute levers four to five from the rest of the world. Even with these new funds, the IMF's resources would still represent well under half a percent of global output, less than half of what they were 15 years ago (1983). In relation to private capital flows going to developing countries they are one-twentieth as large as they were 15 years ago.

I thought that it may be helpful for me to say a few words about the financing structure of the IMF. In some ways, the IMF operates like a credit union. We extend a credit line—for most of our quota subscription and for our proposed NAB commitment—which the IMF can draw on. Any drawing by the IMF gives us a claim—not unlike a deposit—in the IMF, which is of equal value, pays interest, is supported by over $30 billion in gold, and which we can withdraw essentially on demand if necessary. For these reasons, U.S. participation in the IMF is treated as an exchange of financial assets. U.S. transfers to the IMF are not scored as budget outlays, and do not come at the expense of domestic programs.

A number of concerns have been raised about our continued support of the IMF. Let me take a little time to address two of these.

Some have expressed the concern that IMF stabilization programs in Asia have been excessively contractionary and focused too little on the need to restore growth and provide for rising individual incomes and opportunities in these countries.

The hardships that have come with the "slowdown" in growth in Asia stem mainly from domestic policy mismanagement and the ensuing loss of market confidence, not from the involvement of the IMF. The IMF has offered finance and, in Korea, Thailand and the Philippines, has triggered a restoration of confidence that is already lessening the burden of adjustment. The primary focus of these programs is structural—on the promotion of policies that will promote growth by allowing markets to operate and market forces to operate.

Macroeconomic programs must always weigh what is needed to stop a free-falling currency, and what can be done to maintain production. As we go forward the United States will watching closely to ensure the right balance is being struck as conditions change and confidence is improved. But be clear: these programs are designed with the objective of quickly restoring stability, which is the surest route to a restoration of growth.

Another concern is that the international financial institutions work to ensure that the impact of adjustment on the poor is cushioned. This is being addresses in several respects:

- in the Indonesian and Thai programs, spending on health, education and social programs have been expressly protected from any fiscal consolidation, and where possible, efforts to target spending on the poorest segments of society have been intensified.
- In Korea, the program commits the government to strengthening the labor insurance system, and the promotion of active labor market policies to lessen the shock to employment due to the crisis;
- in designing programs to supplement the IMF program, both the World Bank and the Asian Development Bank have been acutely aware of the need to focus on the impact of policy on the most vulnerable, both in the new lending provided to these countries and through the restructuring of existing lending programs to promote urban and rural employment and basic health services. New World Bank lending to Thailand and Indonesia, for example, foresees upwards of $600 million in new loans for improving the social safety net in each of these countries.

IV. Concluding Remarks

Mr. Chairman, the globalization of financial markets has been a breathtaking development. Huge amounts of capital flow quickly among closely integrated financial systems. Technological change has made possible flows of information and finance on a vast scale. Globalization has thrust the private sector into a predominant role in financing development around the world. Private capital has financed great advances in productivity and has raised living standards, and created new markets for U.S. goods. Globalization has created great new opportunities for America.

At the same time, globalization brings new risks. The Asian crisis will likely be viewed as the first crisis of the new global economy. To date, the impact of the crisis on our country is moderate, and manageable. We are in a strong position to withstand the effects of this crisis: our economic performance is the best in a generation and unrivaled among the major industrialized economies. But, if instability were to spread or intensify, the potential risks to American jobs, American financial markets and our national security could be much greater. Given the risks involved, we have a responsibility to protect America's core economic and security interests, by working to restore stability with the most effective mechanisms available to us.

To fail to fund the IMF adequately and promptly would risk our not being able to respond with adequate financial support in the event that this crisis were to spread. And it could risk a further shock to the confidence of international investors at a time of considerable market fragility. These are not risks we should take.

Mr. Chairman global markets of the twenty first century present both opportunities and risks for the American people. Making the most of those opportunities, while minimizing the risks, will be a central issue for this Committee, and the nation, in the years ahead. U.S. leadership in these matters will be indispensable for fostering growth and stability around the world—and protecting and promoting the interests of the American people. Thank you very much.

Chairman CRANE. Thank you, Mr. Lipton. I know that a lot of these Asian countries that are affected by this financial crisis are encouraging exports to build up their current accounts and, in fact, I read a report that Korea is using IMF funds for export loans. Is this correct, and, if so, how do you intend to treat the issue?

Mr. LIPTON. I don't know of any explicit loan programs that support exports. In fact, in the IMF Program, Korea has pledged not to engage in directed lending where the government tries to channel funds to particular companies or particular banks.

I think it is natural that there will be an expansion of the current account balance in Korea and other countries both because of the significant contraction in domestic incomes and because of the depreciation that has taken the won to a very low level and from which it really has not yet fully stabilized.

I think that we have in the IMF Program the monitoring capability to make sure that there aren't subsidies or directed loans that distort trade in the direction of exports in a way that would be a violation of the program and undesirable for them and for America.

Mr. EIZENSTAT. If I may just add one point on that, Mr. Chairman, and that is that in South Korea, the change in their current account deficit has occurred almost entirely on the import side. They had about a 40-percent drop in the amount they can import because their economy has deteriorated. Their exports have gone up about 2 percent.

Chairman CRANE. But you can't categorically say that Korea isn't using IMF funds for that purpose?

Mr. LIPTON. Well, I can say it is not to our knowledge. It would be a violation of the IMF Program. I'm happy to check with the IMF to see if they have any knowledge of violations, but I don't believe that there are any.

Chairman CRANE. All right. Mr. Eizenstat, you've suggested that the markets are looking for both economic adjustments and the political will to implement reform. Do you believe the lack of fast track compromises our ability to press others to implement economic and political reforms?

Mr. EIZENSTAT. I do believe the absence of fast track authority makes it more difficult not only in Asia, but in Latin America and other developing markets to press for reform, Mr. Chairman. It is ironic that at the very time the developing world has bought the bipartisan religion—if I can put it that way—that we have lived by for 50 years, namely the liberalization, opening markets, privatization, that we appear by not moving on fast track to be retreating from that which we have been so successful in selling.

Chairman CRANE. And what specific actions will the United States take to monitor the Asian crisis and compliance with the IMF proposals?

Mr. LIPTON. We will rely, in the first instance, on the IMF which now has had missions present in Asia since the beginning of the crisis and will continue to for some time. We also have a very extensive set of visits to Asia by Treasury Department staff and officials. I've been to Korea twice, myself, and we've had staff in Thailand and Indonesia in the past week. I believe that we are establishing information flows and interactions with these governments that will give us a very good sense of whether or not they're implementing their commitments.

Chairman CRANE. Thank you, Mr. Matsui.

Mr. MATSUI. Thank you, Chairman. Mr. Neal was not able to be here today and he's asked me to submit for the record three questions to be directed at Secretary Eizenstat, so I'll put these in the record and get these copied to you and perhaps you can answer them.

Mr. EIZENSTAT. Thank you.

[The following questions submitted by Congressman Neal and Mr. Eizenstat's responses follow:]

Question. 1. It is important to make progress in improving our exports to China in order to reduce our trade deficit, but would you agree that such progress can be undone if we impose unilateral controls on U.S. exports to China? In Massachusetts, a number of companies have complained that they cannot sell machine tools to China that they know are freely being sold by the European competitors. Would it be better to have a position on machine tool sales to China that is endorsed and, indeed, followed by our allies and trade competitors?

Answer. We share your commitment to fostering U.S. exports to China. That said, the goal of U.S. export control policy is to support an overall strategy of engagement with China and to promote creation of high-paying, export-based jobs in the U.S., while denying licenses for exports that could contribute to activities of potential national security concern to the United States.

Evidence is mixed as to whether export controls and the denial of export licenses have a substantial effect on the size of the U.S. trade deficit with China. China has benefited more than most other countries from the Administration's liberalization of licensing requirements in 1994, which eliminated export controls on an estimated $2 billion annually in trade with China. In 1997, U.S. exports to China totaled $12.8 billion and the U.S. approved $1.1 billion in export licenses. Only $38 million in licenses were denied. However, difficulties in obtaining export licenses were one factor in decisions to award some very large projects to non-U.S. suppliers.

Obviously we prefer to coordinate to the extent possible with our allies on export control policies and our participation in multilateral control regimes such as the Wassenaar Arrangement is designed to do that. However, whether to impose requirements for individual licenses for controlled items, whether to grant licenses for those items, and whether to unilaterally control items beyond those on the Wassenaar Arrangement lists are national decisions and, in the U.S., remain subject to normal interagency deliberations.

Question. 2. It is my understanding that the U.S. position on machine tool export controls to China is not shared by our allies and this results in U.S. manufacturers losing hundreds of millions of dollars worth of exports every year. Do you have a comment on this?

Answer. We share your interest in expanding our exports to China when that is compatible with our other policy interests. Exports to China have been increasing. For the most part, we share a common position with our allies on export control policies. However, the U.S. makes decisions on export licenses for sophisticated machine tools very carefully, reviewing both the end user and whether that end user could use the item for other than civilian end uses. Some of our allies have more liberal licensing policies.

Despite the low market share for U.S. tool manufacturers in China, it is significant that U.S. manufacturers actually have a higher share in China than in some countries to which U.S. machine tools exports are not restricted, such as South Korea, and that other nations that have a smaller world market share have a higher share of the Chinese market than the U.S. The reasons may have as much to do with regional trading patterns and foreign direct investment as export controls.

Question. 3. The multilateral machine tool control list that was agreed upon in 1996 is scheduled to expire in November of this year. It seems that the U.S. government and U.S. machine exporters will be even worse off than they are today, with no officially recognized export control list to guide our allies. What is our government planning to do to address this situation?

Answer. We share your interest in not unduly disadvantaging U.S. exporters by our export control policies. As you are aware, Wassenaar Arrangement members will be considering this year whether to revise the current controls on sophisticated machine tools. Discussions on this subject began March 2 in Vienna and indications are that we will reach some agreement to preserve machine tool controls.

The U.S. is developing its position on machine tools for the Wassenaar Arrangement discussions and will seek generally to maintain current control levels. We are seeking to build a consensus for this position among our regime partners. However, we expect other countries will have alternate proposals and there will be a broad debate on the issue in the coming months.

Mr. MATSUI. I'm going to be very brief. I just want to ask both of you, and I think most of us favor at least the $3½ billion funding for the IMF, and some of us favor the entire $18 billion. I certainly favor the entire $18 billion. On the other hand, I think all of us agree and I know that the administration feels very strongly about this, that reforms must occur to make this ultimately work. And I'm wondering if there'll be a point when we say this is not in our interest.

The Japanese, and I mentioned this today when Ambassador Barshefsky testified, have really not fulfilled their obligations, at least as the other industrialized countries have suggested, in the three areas that I think both of you mentioned, or at least one of you mentioned: the fiscal stimulus; the tax bill, it's not permanent or multiyear, it's just a 1-year tax cut; the whole issue of market opening and obviously the issue of strengthening their financial institutions and putting reforms into their financial institutions. And obviously, with the exception of the United States, the Japanese is the other engine to make this thing work.

The Indonesians are a basket case; they're not doing anything now. In fact, we're having significant problems there. The Koreans are doing a great job. Their new leader is obviously trying to work through this in a very constructive fashion.

But, generally speaking, the two large countries, one economically and the other by population, have not been forthcoming. And I understand that no matter what happens, there is going to be, obviously, suffering. I mean, their public will suffer, the country will suffer, the countries involved will suffer, but is that enough?

I don't agree with the gentleman from the Heritage Foundation at all. I think there is a point where some of us who are very strong free traders and support the administration's position are concerned that we might set a precedent that we may, 10 years or 5 years from now live to—not regret, but at least be concerned about it. Perhaps both of you can, or one of you can respond.

Mr. LIPTON. We are doing all we can to encourage Japan to fulfill its responsibilities. There have been high-level contacts including most recently at the G–7 meeting where, I believe, the Japanese heard a united view of the other 6 members of the G–7 and have seen that the IMF itself has stated that Japan should—that the best thing for Japan and for the region would be for it to—engage in a fiscal stimulus program to restore domestic demand. They were also pressed very hard on the issue of resolving problems in their financial system and opening up the rest of their economy with deregulation. We don't believe that Japan should continue on the path that it's on, that it's a very contractionary path that leaves Japan weak and that its weakness is bad for Asia. This is a subject we will continue to press and press firmly until they adopt a more responsible course of action.

In the case of Indonesia, the problems are a combination of political and economic problems with perhaps greater difficulty in the political area right now. All I can say about that is that the IMF will insist that Indonesia fulfill the spirit and letter of the agreements if they wish to continue to get financial support from the IMF. In a sense, Indonesia will have to make choices about the direction of its policy that will determine whether it gets continuing support from the international financial community. I think the best thing we can do in the case of Indonesia is to try to describe, as clearly as we can, a course of action that will help restore confidence in that country and permit a restoration of economic activity. To that end, the President, I understand, has now asked former Vice President Mondale to travel to Indonesia to try to convey a message.

Mr. EIZENSTAT. I would just add a couple of points to those with which I firmly agree with Under Secretary Lipton. Japan has participated as perhaps the largest contributor to the standby programs——

Mr. MATSUI. Right.

Mr. EIZENSTAT. And they recently agreed in London to participate with our Ex-Im Bank in what, I think, can be the most important at this point, Congressman Matsui and Mr. Chairman, for these countries and that is to help them with short-term credit needs. They can't activate letters of credit to import anything—food stuffs, inputs for eventual exports, and the like. But, with respect to their overall contribution, much more needs to be done in the areas of deregulation and the areas of stimulating domestic demand by deregulation and by tax reductions, and, as Mr. Lipton said, also in the financial stability area. They have a $100 billion current account surplus with the world, and as Asia's largest economy, they have a responsibility to bear their share of the burden of absorbing these Asian exports.

With respect to Indonesia, it clearly is a mixed political and economic situation, and that is one of the reasons that Ambassador Mondale is going. At the same time, Indonesia has complied with many of its program obligations, although many initiatives still require more aggressive implementation. Their financial sector restructuring plan looks solid but still requires implementation guidelines. They've begun some corporate debt restructuring plans. They've cut import tariffs on 650 food and agricultural items and other key products including textiles, chemicals, garments, and equipment. Their interest rates have risen somewhat compared with recent levels, their fiscal compliance has been reasonably strong, and they've issued structural reform decrees, including ending the monopoly power for BULOG and other such groups. And the compliance with the letter of the agreement in this respect is fairly strong, so it is a mixed picture. More needs to be done and Mr. Lipton is certainly correct that it needs to be not only on the economic side, but it needs to be demonstrated by the markets that there is an experienced economic team that will have the desire to implement this and the political backing in the country to do so.

Mr. MATSUI. I'd like to thank both of you for your testimony. I appreciate it very much.

Chairman CRANE. I, too, want to express appreciation to both of you for your testimony, and also appreciation for adjusting your schedules. And I think you're out of here 1 minute before our planned schedule, so you should make your next appointment right on time. [Laughter.]

And with that, I look forward to a continuing working relationship with you both.

Mr. EIZENSTAT. Thank you, Mr. Chairman.

Mr. LIPTON. Thank you very much.

Chairman CRANE. And our final panel includes Hon. Henson Moore, former colleague and president and chief executive officer of the American Forest and Paper Association; William Hudson, president and chief executive officer of AMP, Inc., on behalf of the American Electronics Association, the National Association of Manufacturers, the U.S. Pacific Basin Economic Council; Frederick Webber, president and chief executive officer of the Chemical Manufacturers Association; David Waide, the president of the Mississippi Farm Bureau Association on behalf of the American Farm Bureau Association; and, Mary Sophos, senior vice president of government affairs for the Grocery Manufacturers of America. And, after you people take your seats there, we will start with our distinguished former colleague, Henson Moore, and proceed in the order that I presented you before the Subcommittee.

STATEMENT OF HON. W. HENSON MOORE, PRESIDENT AND CHIEF EXECUTIVE OFFICER, AMERICAN FOREST AND PAPER ASSOCIATION; AND FORMER MEMBER OF CONGRESS

Mr. MOORE. Thank you, Mr. Chairman. Mr. Chairman, I am the president of the American Forest and Paper Association which is the national trade association representing the nation's forest products industry, both lumber and paper.

I'd like to point out to the Subcommittee that we are the largest industry of our kind in the world. We outproduce the next three countries combined. We employ about 1.6 million Americans and rank as one of the top 10 manufacturers in 46 States in the Union.

Asia is a very important market to us. Forty percent of our worldwide exports go to Asia, but Asian countries are also producers that rank among our most formidable worldwide competitors, and they're adding capacity at a very vigorous rate. Historically, our companies have faced a very formidable array of trade barriers including tariffs, nontariff barriers, and discriminatory standards, in these very markets.

Recently, the APEC tariff initiative that was endorsed in Vancouver in the summit last November offers a very unique opportunity to begin to bring some measure of free trade for our industry to that part of the world. We think this is a very remarkable event for which we are very complimentary of Ambassador Charlene Barshefsky, the U.S. Trade Representative, and also Under Secretary Stuart Eizenstat and the State Department, for the work that they've been doing in this area. We very much appreciate their efforts.

We note, however, that while a number of countries are moving toward endorsement of the APEC initiative, there are two countries that so far have not; two real leaders in that part of the world, Japan and Korea. Thus far, we fail to see either one of those countries exercising the leadership which the times and their position in that region of the world require. Winning their early and firm commitment to the APEC sectorial initiatives must be a major objective of U.S. trade, financial and security policy in dealing with this crisis.

The crisis may be used, we fear, by protectionists in those countries in order to be able to stall trade liberalization of the region. The U.S. forest products industry urges this Subcommittee to ensure that the United States policy response to the current financial difficulties in Asia goes beyond the immediate need to restore financial stability and focuses on the more fundamental requirement for genuine market-based reform. Monetary and trade policy interests must be coordinated and integrated. Asian countries must be pressed hard to open their economies, not only to banking and investment, but to competition and goods. Protective tariffs, nontariff barriers, collusive business practices, cronyism, state trading, are all part of the problem which has caused the current crisis in Asia. You couldn't find a better time to bring down these trade barriers in terms of tariffs. The sharp devaluation of their currencies in that part of the world has made producers in those countries hypercompetitive. There could really be no better time to eliminate tariff barriers than now.

I also want to point out that most economists generally agree that substantially increased exports from these Asian countries to the United States will soon occur. The United States really can't afford to stand alone as the market of first and last resort for the Asian export machine.

We believe that open markets must be the hallmark of the Asian recovery. We urge this Subcommittee to ensure that the United States and the multilateral institutions which we support place greater emphasis on the market-opening measures, and the APEC sectoral initiatives in particular, as critical elements in achieving long-term, stable growth in this important region of the world.

Thank you, Mr. Chairman.

[The prepared statement follows:]

Statement of Hon. W. Henson Moore, President & CEO, American Forest & Paper Association; and Former Member of Congress

My name is Henson Moore. I am President and CEO of the American Forest & Paper Association (AF&PA). AF&PA, the national trade association of the forest, pulp, paper, paperboard, and wood products industry, represents more than 100 companies. The vital national industry which AF&PA represents accounts for 8% of total U.S. manufacturing output. The industry employs approximately 1.6 million people and ranks among the top 10 manufacturing employers in 46 states. Its annual payroll is about $50 billion, and sales of forest and paper products top $200 billion annually in the U.S. and abroad. We are the largest producer of forest products in the world.

It is a privilege for me to testify today on a matter of urgent concern to our member companies.

The U.S. forest products industry has an important stake in Asia. Asia currently accounts for 40% of our worldwide export sales. Asian producers rank among our most formidable worldwide competitors, and are adding additional capacity at a vigorous rate.

Historically, our companies have faced a formidable array of trade barriers—including tariffs, non-tariff barriers, and discriminatory standards—in these markets.

A prime example is the 20% tariff on kraft linerboard (used in the manufacture of corrugated shipping containers) imposed by Malaysia in 1994, expressly designed to preclude foreign competition with a local production facility. For wood products, the issue of tariff escalation—the application of zero tariffs on raw materials and higher tariffs at progressive stages of processing—has meant that market access for our higher value-added products has been restricted.

These tariffs are particularly unfair in view of the fact that U.S. tariffs on paper products are at or near zero, and are very low for wood products. Moreover, a substantial number of these countries benefit from duty free access to the U.S. market under the U.S. Generalized System of Preferences (GSP).

Over the past year, our industry has worked closely with the Office of the U.S. Trade Representative (USTR) and our industry counterparts in Canada, New Zealand and Indonesia to craft a comprehensive program which would eliminate tariff and non-tariff barriers, as well as discriminatory standards throughout the Asian region. The Asia Pacific Economic Cooperation forum (APEC) Forest Products Initiative—which was endorsed at the Vancouver Summit in November of last year—offers the potential to establish a truly barrier free market for our products in the APEC region by 2004. By opening participation to other trading partners under WTO auspices, it could create a global free market in this industry.

We view this as a remarkable achievement—a testament to both the extraordinary negotiating skill of USTR Barshefsky and the growing economic sophistication of the APEC member economies. It must be emphasized that the APEC leaders took this decision, in full light of the unfolding financial crisis, precisely and explicitly because they understood that market liberalization is sound economics and that a commitment to achieve completely free trade in the region's most important sectors would send a strong, confidence-boosting signal to world financial markets.

We are further encouraged by the results of recent APEC meetings in Penang, where Senior officials reaffirmed their commitment to achieve the goals set in Vancouver. At the same time, however, we note that some of the developed countries in the region—especially Japan and Korea—have so far failed to exercise the leadership which the times and their position in the region require. Winning their early and firm commitment to the APEC sectoral initiative must be a major objective of U.S. trade, financial and security policy in dealing with this crisis.

We remain concerned that the crisis may be used by protectionists as an excuse to stall trade liberalization in the region. The U.S. forest products industry urges this Committee to ensure that the U.S. policy response to the current financial difficulties in Asia goes beyond the immediate need to restore financial stability and focuses on the more fundamental requirement for genuine market-based reform.

Monetary and trade policy interests must be coordinated and integrated. Asian countries must be pressed hard to open their economies, not only to banking and investment, but to competition in goods. The U.S. must use its leverage, including its position in multilateral institutions, to this end.

It must be remembered that protective tariffs, non-tariff barriers, collusive business practices and state trading are all part of the problem which led to the current crisis. There can be no meaningful, sustainable recovery in the region unless and until these are rooted out.

Where they exist, anticompetitive practices (such as the keiretsu system in Japan; the chaebol in Korea; and the plywood cartel in Indonesia) subsidies or other non-market based financial incentives for capital investment which have thwarted market function, and contributed to the current problems, must not be allowed to continue. Making such policies transparent is not the answer; they must be eliminated, and markets opened to foreign trade and investment on equal terms. The U.S. and multilateral lending agencies must ensure that needed adjustments are made on the basis of fully open, contestable markets.

The discipline of open markets, which the APEC Forest Products Initiative will provide, must be combined with closer scrutiny of lending policies by U.S. Government and multilateral donor agencies to ensure sustainability in this sector. Investment and production decisions must be subject to market—not political—forces.

The recent IMF agreement for Indonesia is a step in the right direction, but needs continuing surveillance. By calling for the dismantling of the plywood cartel (APKINDO) and the elimination of export taxes, it opens the way for enhanced competition in panel products' markets around the world. But, for Indonesia and for other countries in crisis, the IMF must go further. It must press for the elimination of tariff and non tariff barriers, before it can be satisfied that the underlying causes of the current difficulties are being effectively—and permanently—addressed.

The benefits for the regional economies are clear: The elimination of tariff and non-tariff barriers, and the rationalization of building standards, would mean lower input costs for export oriented industries; reduced prices to consumers on products ranging from housing and furniture to printed materials; improved efficiency in the utilization of precious forest resources; more realistic selection of investment projects and improved returns on capital invested; and wider markets for value added wood and paper products.

These outcomes would appear to be necessary ingredients in any recovery program and are especially important in view of the significance of the forest products industry in some of the hardest hit countries of the region such as Indonesia, Malaysia, and the Philippines.

In fact, the opportunity side of this particular crisis may be that it diminishes the perceived economic risk for these countries in eliminating tariff and other trade barriers. The sharp devaluation of their currencies has made producers in these countries hyper competitive. There may be no better time to eliminate tariff barriers than the present.

Indeed, the U.S. can ill afford any delay in opening these markets. Economists are agreed in their predictions of substantially increased exports from Asian countries to the U.S. But the U.S. cannot afford to stand alone as the market of first and last resort for the Asian export machine. Particular pressure must be put on Japan, as the premier developed country in the region, to open its markets to regional suppliers. Domestic demand stimulation will not suffice absent a strong market-growing component, Japanese stimulative measures have historically led to increased output by Japanese industry—and even greater pressure on U.S. domestic markets. Korea, Taiwan and even China have a role to play as well.

The U.S. forest products industry has consistently supported U.S. policies designed to open world markets. During the 1980's, we initiated the zero-for-zero concept, offering to completely eliminate U.S. tariffs on our products. This past year, we worked closely with the Congress to obtain fast track authority which would have made new trade initiatives possible.

We believe that open markets must be the hallmark of Asian recovery. We urge this Committee to ensure that the U.S., and the multilateral institutions which we support, place greater emphasis on market opening measures, and the APEC sectoral initiatives in particular, as critical elements in achieving long term stable growth in this important region.

Chairman CRANE. Thank you.
Next in line was Mr. Hudson.

STATEMENT OF WILLIAM J. HUDSON, PRESIDENT AND CHIEF EXECUTIVE OFFICER, AMP, INC., HARRISBURG, PENNSYLVANIA; ON BEHALF OF AMERICAN ELECTRONICS ASSOCIATION, NATIONAL ASSOCIATION OF MANUFACTURERS, AND U.S. PACIFIC BASIN ECONOMIC COUNCIL

Mr. HUDSON. Thank you, Mr. Chairman. I appreciate this opportunity to testify, and thank you for convening this very timely hearing on the crisis in Asia. I appear before you as a member of the American Electronics Association, as the vice chairman of the National Association of Manufacturers, as the chairman of the U.S. Member Committee of the Pacific Basin Economic Council, and of course, as president and chief executive officer of AMP, Inc.

Our company, AMP, one of AEA's more than 3,000 U.S. members, is the world leader in the production of electrical and electronic connectors and interconnection systems. Today we are a $5.75 billion company with offices in 50 countries and sales in over 100. I would mention that I lived in Japan for 7½ years, and that during that time I set up eight new greenfield operations in the region, and maintained AMP's top market-share position in Japan and in Asia.

On Sunday I returned from a week in Thailand, where I received briefings from AMP leaders throughout the Asian-Pacific region. Before I left, I stated publicly my belief that Congress should quickly provide the IMF funding requested by the administration. Today, I am even more convinced of the importance of following through on that policy.

The American electronics industry is a phenomenal success story. U.S. employment in our industry has grown by 7 percent in the last 6 years, creating 290,000 new jobs. To a large extent, this has resulted from demand abroad. Many high-tech companies—indeed, many Fortune 500 companies—generate high percentages of their revenues from overseas sales.

At AMP, 55 percent of our sales are outside the United States. The same is true at Digital. At Motorola that number is higher, around 60 percent. This same phenomena can be seen in many small companies and in some startups.

Barringer Technologies, for example, is a maker of advanced trace detection technology for security and law enforcement applications. It attributes 45 percent of its $25 million in sales to non-U.S. orders. Endgate Technology is a California-based startup manufacturer of wireless telecommunications equipment. Eighty percent of their sales are to customers abroad.

While the larger portion of our sales are outside the United States, the majority of our work force is here. That is true for AMP, and it is true for the U.S. electronics industry generally. This industry is the largest U.S. manufacturing employer—with 1.9 million U.S. workers. Those numbers swell to 4.2 million when we include high-tech services employment.

In 1996 approximately 40 percent of the U.S. high-tech industry's exports went to Asia—far more than to any other region. Asia is important to the growth of this industry and to its tremendous success in creating jobs and generating revenue.

As noted earlier, the Asian-Pacific region's economic well-being is important to the continued success and growth of America's high-tech industries. A financial meltdown and recession in Asia could affect United States competitiveness, exports, and jobs. It could also affect pension plans here which are tied to the performance of U.S. companies.

Our task should be to try to avoid any further spread of the currency devaluations of Asia and to enact policies that will build confidence in the region. The troubled economies of the Western Pacific are like patients in an emergency room, and the first job of the doctors should be to stabilize the patients, not to argue about the hospital admission process.

The immediate challenge is to strengthen the currencies in the affected countries as quickly as possible. Without this kind of fundamental improvement, China and Hong Kong may not be able to retain the exchange rate relationships of the dollar to which they both are now committed. If they devalue, exports from the region will accelerate, creating new pressures on the United States economy and on the economies of Europe. These pressures will have deleterious effects on the quality of life, the character of policy, and the levels of international cooperation throughout the world. We also need to support the IMF in its demand that the countries getting IMF assistance agree to and adhere to certain conditions.

At this point let me summarize the main concerns of the American Electronics Association and the other organizations for which I am appearing. AEA, NAM, and PBEC support funding the total request of $18 billion for IMF. They believe it would be counterproductive for the United States to put new, unilateral conditions on its contribution to the IMF. They also believe, though, that the IMF conditions do advance important U.S. interests. They further believe that the IMF conditions must be closely monitored, not only by the IMF, but by U.S. agencies as well.

Finally, these groups are concerned, as I am, by the fact that the countries in the region, including Japan, continue to rely too heavily on export-led growth. While America's interests are clearly an issue, other countries must demonstrate leadership as well. Japan needs to stimulate its economy and further open its markets. China must continue to play a responsible role. The recent assurances by Chinese officials confirming their commitment to exchange rate stability have been both significant and welcome. Europe, too, has been affected by the Asian crisis and must do its part to counteract it.

In conclusion, Mr. Chairman, let me return to the key point of these remarks. The action you take now will be critical to America's future. By nature, business leaders are optimists; investors have to be. They see opportunities and potential. The opportunities for all parties in the Pacific partnership that links America to the Western Pacific are enormous. As a country, though, we run the risk of squandering those opportunities if we pull back from our long-term commitment to the region and to the IMF. I urge you not to do that, but to approve the President's request.

Thank you.

[The prepared statement follows:]

Statement of William J. Hudson, President and Chief Executive Officer, AMP, Inc.; Harrisburg, Pennsylvania; on Behalf of American Electronics Association, National Association of Manufacturers, and U.S. Pacific Basin Economic Council

OPENING AND INTRODUCTION

Thank you, Mr. Chairman. I am pleased to be here on behalf of the American Electronics Association to discuss the vital issues of Asia, its currency situation and the progress of Asia Pacific Economic Council (APEC). This committee is critically important in guiding U.S. policy throughout the world. Today I would like to thank you, Mr. Chairman, and the Members of the Subcommittee for convening this very timely hearing on the crisis in Asia. I appear before you today not only as a member of the American Electronics Association, but also as the Vice Chairman of the National Association of Manufacturers (NAM) and as the Chairman of the U.S. Member Committee of the Pacific Basin Economic Council (PBEC). The views expressed here are shared by each of these groups.

The American Electronics Association represents more than 3,000 member companies across the spectrum of electronics and information technology companies—from semiconductors and software to computers and telecommunication systems. As the largest high-tech trade association in the United States, AEA represents American high-tech companies nationally through 17 council offices and globally through our offices in Tokyo, Brussels and Beijing.

Let me also take the opportunity to tell you about AMP, Incorporated. AMP is a global enterprise and world leader in the production of electrical and electronic connectors and interconnections systems. When I started with AMP in 1961, we were primarily a Pennsylvania company with a few foreign operations, mainly in

France and Japan. Today, we are a $5.75 billion company, with offices in 50 countries and sales in over 100. AMP has grown at 13.7 percent compound annual growth for the last 40 years. That is, of course, better than the recent growth rates of the U.S. economy and even better than the rapid annual growth we have seen in many of the Asian economies over the past decade.

You should also know that I lived in Japan for seven and half years. During that time I set up eight new greenfield operations in the region and maintained AMP's top market share position in Japan and Asia.

Mr. Chairman, the work of the Trade Subcommittee is vitally important to the competitiveness of the United States. The issues facing this subcommittee and Congress are more challenging and complex as a result of the globalization of the economy and the increasing interdependence of global markets—which the Asia crisis vividly demonstrates. There is a temptation to view each issue—whether it is the role of the International Monetary Fund (IMF) in Asia, fast track, Most Favored Nation (MFN) status for China, Africa, or the Generalized System of Preferences (GSP)—as independent, isolated measures or worse, as tradeoffs. In fact, they are interrelated policies that work together to create the level playing field and open markets which are critical to the continued success and competitiveness of U.S. companies and of the United States.

THE U.S. HIGH-TECH INDUSTRY IN THE GLOBAL ECONOMY

The interdependence and complexity of the global economy is evident when we look at the high-tech industry and its role in U.S. and global economy. The U.S. high-tech industry is the single largest manufacturing industry in the United States, with 1.9 million manufacturing jobs. When computer and communications services are included, the combined employment swells to 4.2 million workers. These are high-skill, high-wage jobs. The average wage of these jobs is almost $50,000 ($49,586), which is 73% higher than the average private sector wage of about $29,000 ($28,582). This industry represents 6.2 percent of the U.S. GDP, with total annual sales of $866 billion in 1996. Finally, with $150 billion in exports, the American high-tech industry is the single largest merchandise export industry in the United States.

This industry's U.S. success story is largely a story of international sales. U.S. employment in our industry has grown by 7 percent in the last six years, creating 290,000 new jobs. This has been largely a result of demand abroad for U.S. products and services. Many high-tech companies—indeed many Fortune 500 companies generally—generate a high percentage of their revenue from overseas sales. For AMP, 55 percent of our sales are outside the U.S. For Digital, non-US revenue accounts for 55% of the total and for Motorola, that number is even higher at 60%. While it may not be surprising that some of the large corporations generate a significant portion of their business overseas, small companies like Barringer Technologies, makers of advanced trace detection technology for security and law enforcement applications, with $25 million in sales attributes 45 percent to non-U.S. sales. Even start-ups depend on global sales. Endgate Technology, a California-based manufacturer of wireless local loop telecommunications equipment, attributes 80 percent of their sales to customers outside the U.S. I would emphasize that while a large portion of our sales are outside the U.S., the majority of our workforce is based here in the United States. That is true for AMP, and it is true for the U.S. electronics industry as a whole as mentioned above.

I would add that the value of AMP exports from the United States is over five times the value of AMP imports and that over 40 percent of those exports go to buyers in the Asia Pacific region. As you know, U.S. exports of goods and services support over 12 million U.S. jobs. A certain number of those are jobs at AMP, in the companies that supply us and in the communities that are home to AMP employees.

In 1996, the U.S. high technology industry exported more to Asia-Pacific (excluding China and Japan) region than we did to our traditional largest trading partner, the European Union—$40 billion compared to $36 billion. The total exports to Asia, including China and Japan, are approximately $60 billion or forty percent of the industry's $150 billion in exports. Clearly, Asia is important to the growth of this industry and to its tremendous success in job creation and revenue generation.

ASIAN PACIFIC ECONOMIC COOPERATION (APEC)

Given the importance of Asia not only to the high-tech industry but to the entire U.S. economy, it is understandable that AEA, NAM and PBEC have all been attentive to the APEC process and the progress of the negotiations.

The events of the last six months have been a lesson in the concept of global interdependence.

It is clear, for example, that the economic events in South Korea have affected both companies and markets in the United States. In the past few decades, the Pacific region has seen astounding growth. As the region has grown, it has become more interdependent. Growth has also led the economies to recognize that continued improvement in their standards of living is best pursued by effective trade and investment liberalization. APEC continues to be the forum for achieving trade and investment liberalization. Indeed, APEC was instrumental in securing the Information Technology Agreement (ITA) and continues to be a pivotal player in the implementation and expansion of the ITA and ITA–2. As you know, the ITA is intended to be a living instrument to accommodate new IT products.

On the subject of investment, I would like to express my sincere disappointment over the fact that we have not seen more progress on the Multilateral Agreement on Investment (MAI). To my knowledge this is not an urgent, bottom-line issue for any American company. It is, however, the best opportunity that the world has to establish solid rules for the treatment of international investment. If the hands off, open principles of the MAI had been in place for the last several years in Asia, some of today's problems might well have been averted. At the very least, the United States would not have to contend with some of the beggar-thy-neighbor investment policies that are, regrettably, still widespread in the world. I am thinking here, for example, of the demands that various countries have imposed on investors for technology transfers, product exports, and the use of local suppliers.

On the other hand, the Clinton Administration's reinvigoration of APEC, beginning with the Seattle meeting of 1993, has proven to be of great benefit to the entire region. With the current decline in the value of Asian currencies, there has been an urgent need to continue the process of regional economic liberalization. APEC has provided the forum for doing this and for sending the world the all important message that it is being done. The APEC process and APEC leadership remain essential to the growth of the region's economies and to the global economy.

ASIA CURRENCY CRISIS AND THE ROLE OF THE IMF

As noted earlier, the Asia-Pacific region's economic well-being is important to the continued success and economic growth of the U.S. high-tech industry. A financial meltdown and recession in Asia has a direct effect on U.S. competitiveness, exports and jobs, not to mention our pension plans, which are heavily dependent on the U.S. and global stock market performance. We must avoid further spread of the currency devaluation and enact policies that will build confidence in the region. I liken the Asian situation to a patient in the emergency room. As doctors, the first measure is to stabilize the patient, it is not to argue about the hospital admission process.

Consequently, the U.S. must demonstrate its leadership in stabilizing the patient. We can do this by supporting the reforms necessary to strengthen these economies and by increasing IMF funding so that we are prepared in the event that further destabilization occurs. U.S. funding for the IMF is critical to the success of the entire stabilization effort. It is essential to both America's interests and America's leadership in the region. The IMF has been able to persuade countries to address issues and to accept reforms that the United States has not been able to secure in bilateral negotiations with these same countries. As the largest contributor in the IMF, the U.S. can have significant influence on the conditions to ensure that they are appropriate and significant.

Important as these new liberalization measures may be, the immediate and frankly more important challenge is to strengthen the currencies in the affected countries as quickly as possible. Without this kind of fundamental improvement, it may be impossible for China and Hong Kong to retain the exchange rate relationships to the U.S. dollar to which they are both currently committed. If China and Hong Kong devalue, exports from the region will accelerate, creating new pressures on the U.S. economy and on the economies of Europe. These pressures will have deleterious effects on the quality of life, the character of policy, and the levels of international cooperation throughout the world.

In this context, it is sobering to note that the extremely large—almost $200 billion—U.S. trade deficit of 1997 does not reflect the adverse consequences of falling Asian currencies. The way these things work, the first effect from such devaluations is a lowering of the import bill for the country with the stronger currency.

In these circumstances, AEA supports funding the total request of $18 billion for the IMF—the $3.5 billion New Arrangements to Borrow, and the $14.5 billion which is a quota increase. The U.S. contribution will result in a pro rata contribution will leverage others—fostering a six-fold contribution from other countries that will create the critical mass needed to guarantee the long-term viability of the IMF.

AEA does not believe it is appropriate to pre-condition the IMF funding on specific reforms in countries receiving IMF assistance or on changes in how the IMF operates. Further, the imposition of unrelated policy objectives, however meritorious, undermines the broader objectives of effectiveness and timeliness. As exporters and investors, AEA members have a strong interest in seeing that the IMF continues to require borrowing countries to adopt substantial structural reforms. This focus, however, must not be allowed to obscure the even higher priority of stabilization. And there is some danger of it doing so. There is a danger that we will become more concerned with the "hospital admission procedures" than with the action necessary to save the patient and restore confidence.

AEA members do believe that the IMF conditions advance important U.S. market access interests. Specifically, they can help countries avoid future unwise economic behavior, breaking-up monopolies and ending preferential treatment. Market access is a fundamental aspect of the financial and commercial reforms demanded by the IMF as conditions for restabilizing the financial systems of affected countries.

In the final analysis, it is the IMF itself that must monitor and enforce adherence to the conditions it negotiated with various countries. In addition, however, AEA expects Treasury, the United States Trade Representative (USTR) and the Department of Commerce to closely monitor the progress of reforms and to report to Congress routinely on the effectiveness of reforms. To date, the USTR has been a vigorous advocate for market access, and we would expect them continue to play a significant role in this area. We believe focus on the fundamental reforms is crucial. We are concerned by the fact that the countries in the region, including Japan, continue to rely too heavily on export-led growth. Uncorrected, this is a harbinger of long-term economic disaster.

Even though the high-tech industry tends to be particularly focused on the economic effects of Asia situation, American leadership is necessary not only to ensure our commercial interests but vital to our national security interests as well. We are talking here about an array of solid relationships with important countries such as South Korea, Thailand, Indonesia, and Malaysia. In diplomatic terms, our inaction would be seen throughout the region as a failure in U.S. leadership at a time of extreme need—thereby undermining support for continued U.S. political military and commercial engagements. In human terms, America would be seen as the erstwhile partner who had turned his back on friends in need.

The Role of Other Countries

While America's interests are clearly at issue, other countries must demonstrate leadership as well.

Japan needs to demonstrate its ability to exercise its leadership and stimulate its own economy and open up its market. As the second largest economy in the world, Japan must take the necessary steps to deal with its financial systems, to generate solid growth in domestic demand and further open its markets. It is in Japan's interest, Asia interests and the global economic interests for Japan to take strong action.

China also plays a crucial role in Asia's economic stability and, in fact, the global economy. I have already referred to the recent assurances by Chinese officials confirming their commitment to exchange rate stability. These have been both significant and welcome. Additionally, it is important that this major economic and trading partner be brought into the global trading system, by acceding to the World Trade Organization (WTO) on commercially viable terms. AEA, as it stated before this subcommittee last November, wants to work closely with the Administration and Congress to ensure that we have, as soon as possible, a successful conclusion to these negotiations, assuming a strong protocol that adequately addresses our commercial concerns.

Europe, also affected by the Asian crisis, is seeing economic growth and must continue to take necessary steps toward structural reform that will strengthen its recovery. As Europe strengthens its economy, it too can become an engine of global growth.

Conclusion

We are faced with a serious challenge in Asia. The actions we take now are critical to our economic and national security. Big U.S. interests are at stake leadership is required. AEA, the NAM and the U.S. Member Comcil are ready to work with Congress and the Administration to ensure an effective response to this crisis and to prevent further destabilization in the region and elsewhere around the world. Thank you, Mr. Chairman.

Chairman CRANE. Thank you.
Mr. Webber.

STATEMENT OF FREDERICK L. WEBBER, PRESIDENT AND CHIEF EXECUTIVE OFFICER, CHEMICAL MANUFACTURERS ASSOCIATION

Mr. WEBBER. Thank you, Mr. Chairman, and good afternoon. My name is Fred Webber. I'm president and chief executive officer of the Chemical Manufacturers Association.

In this age of the global economy, the importance of Asian markets for United States industry in general, and the chemical industry in particular, cannot be overemphasized. The U.S. chemical industry is our Nation's largest exporting industry—exporting more each year than either America's farms or America's aerospace firms. Chemical exports account for more than $1 of every $10 of U.S. exports, and we as an industry have a trade surplus in each of the last 75 years. What's more, the jobs of about 182,000 of our industry's total work force of 1 million is supported by exports.

Asian markets are critical to our industry's continued strength and its future growth. Chemical exports to APEC markets in 1996 were more than $36 billion, or more than one-half of the industry's total 1996 exports of nearly $62 billion. Our industry's 1997 exports totaled $69.5 billion. We expect similar results in 1997 for exports to APEC nations.

The current Asian financial crisis will have an effect on our industry. What isn't so clear, at least not yet, is how the crisis will affect our industry and the approximately 1 million men and women who are employed by the chemical industry in high-wage jobs in the United States. These are high stakes for the U.S. chemical industry. Our growth markets, indeed, are in Asia and Latin America. That's why we urge congressional support for a United States-led initiative underway within the Asia-Pacific Economic Cooperation Forum, which, once implemented, will dramatically improve the United States access to key chemical export markets in the Asia-Pacific region. The agreement has the potential to eliminate tariff and nontariff trade barriers.

APEC has recently decided to include chemicals among the list of nine sectors slated for accelerated tariff reductions under its early voluntary sector liberalization, or EVSL. By expanding coverage through the Pacific rim countries of the existing chemical tariff harmonization agreement, we will significantly lower chemical tariffs throughout APEC, and hopefully, reduce many of the nontariff barriers as well. The EVSL package includes a proposal to align regulations covering chemical safety and testing standards as a first effort to ensure better consistency and safety.

Mr. Chairman, your inclusion of chemical tariff harmonization in the Uruguay round Agreements Act resulted in CMA working with the Office of the U.S. Trade Representative to begin discussions in 1996 within APEC, seeking to generate support for existing CTHA to cover all APEC members.

Last week in Malaysia, CMA convened the third Asian-Pacific industrywide conference. We were encouraged to see a high level of industry participation, even from countries experiencing severe economic problems. Expanding trade and lowering chemical tariffs will not only benefit the United States, but will also provide substantial benefits for these Asian nations.

We view the early voluntary sector liberalization as a win/win situation for United States exporters and our Asian-Pacific trading partners alike. We hope that Congress will support the administration's effort to ensure this process moves forward successfully.

Finally, no discussion of the global economy and world trade would be complete without mentioning fast track. The chemical industry believes that the United States should seek out, and take advantage of, trade liberalization whenever possible. Without renewal of fast track, the United States will watch from the sidelines as lucrative trade deals are negotiated by our trading partners.

Even with EVSL, liberalization of key sectors may not take place or take into account the interests of U.S. producers. This denies our member companies an equal opportunity to compete in today's emerging markets. That's why we're disappointed by reports that the administration has all but abandoned congressional approval of a fast track renewal bill prior to the Summit of Americas in April. It is also disheartening that so many Members of Congress still oppose fast track, which will greatly benefit the entire U.S. economy. With your leadership, Mr. Chairman, and with the leadership of Members of this Subcommittee, I sincerely hope that we will get the fast track debate back on track and win the day for U.S. exporters and U.S. workers who make these exports.

Thank you for allowing me to appear before you today. I would welcome any questions you have about my testimony.

[The prepared statement follows:]'

Frederick L. Webber, President and Chief Executive Officer, Chemical Manufacturers Association

Mr. Chairman, Members of the Committee, my name is Frederick L. Webber. I am President and Chief Executive Officer of the Chemical Manufacturers Association (CMA), whose more than 190 members account for 90 percent of the industrial chemicals produced in the United States.

The chemical industry has for some years been the largest U.S. export sector—yes, even larger than agriculture, even larger than aerospace—supplying over one out of every ten dollars of U.S. goods exports and achieving substantial annual trade surpluses for the past 75 years. Given the central role that exports play in our commercial operations overall, U.S. chemical companies and CMA have long been proponents of greater liberalized trade. I want to thank you Mr. Chairman for convening this important hearing to discuss the current trade and economic situation in Asia.

As part of my testimony today, I want to highlight the importance of the Asian market to U.S. chemical producers. In addition, I would like to discuss and urge Congressional support for a U.S.-led initiative currently underway within the Asia-Pacific Economic Cooperation (APEC) forum which, once implemented, will dramatically improve U.S. access to the key chemical export markets in the Asia-Pacific.

These markets are critical to U.S. chemical producers' future growth. Unlike Europe, which is already a relatively mature market, Asian countries are just beginning to expand their consumption of U.S. chemicals. Consequently, we expect the growth trend in the Asia region to continue, and even accelerate, through the turn of the century.

To give you a sense of how important Asia is for our industry, I would note that U.S. chemical exports to the other 17 APEC partners exceeded $36 billion in 1996. This figure represents over half of the $61.8 billion in total U.S. chemical exports world-wide for the same period. Equally important, these markets offer tremendous future potential for our exporters.

In this regard, it is instructive to look at the potential for growth in China alone. In China, a country of over 1.2 billion people, per capita sales of chemicals and related products stand at about $70, compared with U.S. per capita chemical consumption of $1,340 annually. Likewise, consumption of plastics is about 5 kilograms per capita in China, compared with 120 kilograms in the United States.

As these statistics illustrate, China's chemical market is virtually in its infancy, and we see a similar situation in other developing countries in the region including Indonesia, Malaysia, Thailand and the Philippines, just to name a few. Given this vast untapped potential, U.S. chemical producers have a clear interest in ensuring that these and other Asian nations prosper so that their economies can continue to grow, thereby providing the increased demand for the products exported by the CMA members I represent today.

With that in mind, I would like to take a moment to discuss the current financial crisis in Asia and its possible ramifications for our industry. Given that the crisis is only just beginning to affect trade flows in the region, we are still assessing the extent to which the crisis will reduce U.S. chemical exports. However, as I am sure you have all seen, financial turmoil has already prompted many countries such as Indonesia and Malaysia to suspend large-scale industrial development projects and to take other measures to curb spending. Likewise, private sector entities, which include many of our customers, have been forced to delay their expansion plans. As a result, we expect our exports to Asia to suffer, at least to some degree, until the financial crisis begins to subside.

Given the high stakes involved, we at CMA are considering whether to take a public position in support of the various IMF assistance programs designed to help our Asian trading partners back to fiscal health. We are also considering whether to support continued U.S. participation in the IMF and believe that the Administration's recent request for $18 billion in additional U.S. funding for IMF replenishment is warranted as an insurance policy to ensure that the financial crisis does not deepen or spread to other emerging markets in Latin America and beyond.

That said, we also see a need for major structural reforms in many of the affected Asian nations. Many still need to make progress in eliminating tariff and non-tariff barriers to trade and to take additional steps to open their economies to U.S. chemical exports. We believe that the U.S. should aggressively pursue such discussions with the key economies now, while they are still recovering from the financial turmoil.

This brings me to the second topic I would like to discuss today—APEC's decision to include chemicals among a list of nine sectors slated for accelerated tariff reductions under APEC's Early Voluntary Sectoral Liberalization (EVSL) initiatives. In short, by expanding the country coverage around the Pacific Rim of the existing Chemical Tariff Harmonization Agreement (CTHA), we will significantly lower chemical tariffs throughout APEC. Our initiative also aims to reduce many of the onerous non-tariff barriers currently impeding trade within the region.

By way of brief background, the United States, EU, Japan and some two dozen other countries representing 70 percent of world chemical trade negotiated the CTHA as one element of the Uruguay Round. CMA was a driving force behind the negotiation of the CTHA, which requires signatories to reduce their tariffs on virtually all chemicals to levels of between 5.5 and 6.5 percent by 2004. Given that many of the tariffs in place at that time were well over 10 percent, the agreement as it currently stands has the potential to generate significant cost savings for U.S. producers.

However, many of our important trading partners in Asia did not join the CTHA during the Uruguay Round. Mr. Chairman, you recognized the importance of incorporating fast-growing and emerging economies in this initiative, and included chemical tariff harmonization in the Uruguay Round Agreements Act. As a result, CMA, working with officials at the Office of the U.S. Trade Representative (USTR) began discussions within APEC in 1996 seeking to generate support within the chemical industries of APEC member countries for extending the CTHA to cover all APEC members. APEC leaders approved this objective last November, and we are now working on the detailed tariff packages for each APEC economy. The APEC agreement is slated to enter into force in 1999, when APEC members will agree to bring their chemical tariffs into conformity with the rates established in the CTHA in two stages.

When our industry developed the CTHA during the Uruguay Round negotiations, we proposed that economies would have five years to phase down tariffs currently under 10 percent to levels between 5.5 and 6.5 percent. As for applied tariff rates between 10 and 25 percent, we foresaw that reductions to these same levels could occur over as many as 10 years—with up to 15 years allowed for tariffs currently in excess of 25 percent. We are willing to apply similar flexibility now, to permit the APEC economies to reach the harmonized rates over a longer period of time, if doing so will make it possible to reach a "critical mass" of participation in the CTHA initiative. After we have succeeded in reducing the bulk of the world's chemical tariffs to levels at or below the 5.5 percent −6.5 percent called for under the CTHA, we also hope that additional tariff reductions would be negotiated in the sector, leading ideally to the eventual elimination of chemical tariffs world-wide. In addition, APEC leaders have agreed to initiate a work program to explore ways to reduce non-tariff barriers to trade in the chemical sector, with a particular emphasis on initiatives aimed at harmonizing chemical safety and testing standards as a first effort.

Given the tremendous cost savings this initiative offers U.S. chemical producers and its potential importance to our industry, CMA recently sent a delegation to Malaysia to assist U.S. officials during the meeting of the APEC chemicals working group which met in Penang last week. CMA also convened an Asia-Pacific industry-wide conference in Kuala Lumpur which brought together numerous delegations representing the regional chemical industry. I am pleased to report that we were encouraged to see a high level of industry participation in these events, even from countries that currently are experiencing severe economic downturns.

The strong interest in the EVSL from the Asian region's chemical producers bodes well for its final success. As tariff and non-tariff barriers begin to come down in the Asia-Pacific area, we expect U.S. chemical exports to the region to take off accordingly. While expanding trade opportunities certainly will benefit U.S. producers, we also firmly believe that lowering chemical tariffs provides substantial benefits for Asian nations themselves.

Chemicals are upstream components in the production of a wide range of products manufactured in Asia and the rest of the world. Currently, many Asian nations experiencing major devaluations in their currencies are having difficulty securing the funds or credit necessary to purchase key raw materials including chemicals. Lowering tariffs on chemical products reduces the cost of imports and mitigates inflationary pressures. Tariff liberalization will help to create more efficient and competitive production in the region as well.

The increased competition resulting from the reduction of trade barriers in the chemical sector will apply additional market pressure on Asian economies to streamline their own chemical industries, which currently are relatively inefficient and operating at over capacity. Consequently, we view the EVSL as a "win-win" situation for U.S. exporters and for our Asia-Pacific trading partners alike. We hope that Congress will support the Administration's efforts to ensure that this process moves forward successfully.

This brings me to my final point. Negotiations to liberalize trade such as the APEC initiative I have been discussing, are critical to the long-term health of the U.S. chemical industry. We as an industry believe the United States should seek out and take advantage of these trade liberalizing opportunities whenever possible. Fortunately, the APEC chemicals EVSL can move forward without reauthorization of fast-track negotiating authority. But, as we know, all sectors are not covered. Without a renewal of fast-track, the United States will be forced increasingly to watch from the sidelines while our trading partners move forward with their own trade deals. Because chemicals are used so widely, liberalization of key sectors may not take place, and certainly would not proceed in ways that take into account the interests of U.S. producers. This will deny the companies I represent today an equal opportunity to compete in the emerging markets so critical to our industry's future.

For this reason, I certainly was disappointed to read reports in the press suggesting that the Administration has given up hope for securing Congressional approval of a fast track renewal bill prior to the Summit of Americas in April. I also am disheartened to see that so many Members of Congress still oppose fast track, which is simply a procedural tool necessary to allow the United States to continue to play the leadership role in trade liberalizing efforts. Strong U.S. engagement in the free trade process has proven in the past to be highly beneficial to U.S. chemical producers and the U.S. economy as a whole. With your leadership Mr. Chairman and the leadership of others on this Subcommittee, I hope that we will be able to get the fast track debate back on track and eventually win the day for U.S. exporters, and for U.S. workers making those exports.

In the meantime, I would like to thank you again for allowing me the opportunity to appear before this Subcommittee today. I would welcome any questions you may have regarding my testimony.

Chairman CRANE. Thank you very much, Mr. Webber, and we'll get to you momentarily.

Mr. Waide.

STATEMENT OF DAVID WAIDE, PRESIDENT, MISSISSIPPI FARM BUREAU FEDERATION; ON BEHALF OF AMERICAN FARM BUREAU ASSOCIATION

Mr. WAIDE. Thank you, Mr. Chairman, for the opportunity to be here. As you know, I represent the Mississippi Farm Bureau Federation and serve on the American Farm Bureau Federation board, and I'm here today speaking as a witness on their behalf.

In addition to that, I'm a farmer in north Mississippi, and I produce most of the row crops grown in our region—cotton, corn, soybeans, wheat, oats, and also cattle. And the area that we're dealing with today is absolutely essential if agriculture is to continue the growth that it has enjoyed in the past. It's essential if we're going to be able to have the export market that we've been promised.

I know in a previous administration we had the promise of being able to produce fence row to fence row, and we were going to be able to sell those commodities that we produced. Unfortunately, that changed, and food was used as a weapon, and we lost a much-needed market in part of those countries that we had come to depend on.

I know that this area, the Asian-Pacific region, is becoming our most important growth market, as well as one of the major economic regions of the world. It's been the fastest growing economic region of the world over the past several years, and the thing, I think, that's most important to agriculture is that it has the greatest numbers of consumers.

The Asia-Pacific Economic Cooperation, APEC, the forum has the potential to create greater market access for United States exports and must play a stabilizing role in the current economic crisis in this region. APEC members must not be allowed to back away from the commitments to expand and liberalize trade.

American farmers and ranchers depend on international markets for over 30 percent of their income. The Asian market accounts for over 40 percent of our agricultural exports worldwide. This totaled over $23 billion in export sales in 1997.

Three-fifths of the world's population growth and one-half its income growth through 2010 are projected to occur in East and Southeast Asia. This is America's fastest growing agricultural market and should continue to be for some time, if we can resolve this crisis.

The events in Asia are already affecting sales of agricultural goods in 10 Asian markets that have seen their currencies devalued over the past 6 months. Devalued currencies result in increased consumer prices which directly translate into less market demand. The Asian consumer's purchasing power has been greatly reduced. Lost sales mean lower income for our producers and economic pressures on rural economies.

Each country's situation is unique, and each has different needs and prospects for recovery. The arsenal of tools needed to help our trading partners in Asia resolve their crisis must be fully utilized. These tools include developing and putting into place sound monetary practices, which, when coupled with credit guarantees in programs like the USDA export credit guarantee programs, as well as the IMF assistance plans without further devaluations, should stabilize these economies.

The IMF Programs can be successful. They're not charitable bailouts. These are loans, repayable with interest, with requirements for internal structural change. I believe that for IMF Programs to be successful they must be adequately funded and focused on requiring the recipient countries to make the long-term internal adjustments that will lead to sound domestic economic systems, which include stable currencies, stable taxes, and private property rights upheld.

Inaction in this matter is not acceptable. IMF-led assistance programs are critical to the overall recovery in the region, and fast track is critical to picking up lost market share and expanding access to worldwide markets. Ours now is truly a global economy. U.S. agriculture's ability to gain and maintain market share is based on many factors, including good trade agreements, the administration's ability to negotiate freer and fair market access with fast track authority, sound monetary policies, and the ability to utilize market-stabilizing tools, such as a properly functioning IMF.

I urge you to provide the funding necessary for the IMF to address the needs of our trading partners in Asia, and later this spring to grant the administration fast track authority to continue to open markets for all sectors.

Thank you, Mr. Chairman.

[The prepared statement and attachment follow:]

Statement of David Waide, President, Mississippi Farm Bureau Federation; on Behalf of American Farm Bureau Federation

Mr. Chairman, I am David Waide, president of the Mississippi Farm Bureau Federation. I am here today on behalf of the American Farm Bureau Federation. The American Farm Bureau is the nation's largest general farm organization with member state Farm Bureaus in 50 states and Puerto Rico, representing 4.7 million member families.

Farm Bureau farmers and ranchers produce virtually every agricultural commodity produced commercially in the United States. Among other purposes, AFBF was organized to assist Farm Bureau members in attaining economic opportunities through domestic and international markets.

I want to thank you for holding this hearing and providing the opportunity to discuss the importance of the Asian market to American agriculture and the critical need to resolve the Asian fiscal crisis as quickly as possible.

The Asia Pacific region is becoming our most important growth market as well as one of the major economic regions of the world. It has been the fastest growing economic region of the world over the past several years, as well as having the greatest number of consumers. In 1996, total U.S. trade across the Pacific was estimated to be more than 75 percent greater than that across the Atlantic.

The Asia-Pacific Economic Cooperative (APEC) forum has the potential to create greater market access for U.S. exports and must play a stabilizing role in the current economic crisis in this region. APEC members must not be allowed to back away from commitments to expand and liberalize trade. We are optimistic about the potential for APEC to provide increased market opportunities only if agriculture remains on the full agenda.

Your role in helping to shape the direction of trade agendas of APEC and programs such as the International Monetary Fund (IMF) will have a major impact on the economic stability of American agriculture in the Asian marketplace.

The financial crisis in Asia is of paramount concern to Farm Bureau members. America's farmers and ranchers depend on international markets for over 30 percent of their income. The Asian market accounts for over 40 percent of our agricultural exports worldwide. This totaled over $23 billion in export sales in 1997.

Eastern and Southeast Asia is a region with a ratio of people to land six times higher than North America. Current financial turmoil and harmful currency devaluations must not be allowed to obscure the economic and demographic focus at work in this region. Three-fifths of the world's likely population growth and half of its income growth through 2010 are projected to occur in East and Southeast Asia. Aggregate food demand is projected to grow 100–150 percent in this region over the next 25 years. This is America's fastest growing agriculture market and should continue to be for some time—if the fiscal crisis can quickly be reversed.

Asia has been a growth market for traditional bulk commodities such as soybeans, corn, rice and wheat. But, in 1997, the fastest growing U.S. agricultural exports were in what we call value-added products. These include meat, horticultural, fruits and vegetables and processed foods. Value-added products account for millions of U.S. jobs in processing, packaging, advertising, and shipping. These are off-farm jobs that support rural communities and a broad scope of interrelated industries.

The events in Asia are already affecting sales of agricultural goods in the 10 Asian markets that have seen their currencies devalued over the past six months. Devalued currencies result in increased consumer prices which directly translates into less market demand. The Asian consumer's purchasing power has been greatly reduced. Lost sales mean lower incomes for our producers and economic pressures on rural economies.

Current USDA estimates show a reduction of $500 million in sales to Asia so far this year. The total impact may exceed $1.5 to $2 billion before the crisis is over.

Let's look at some specifics of what is taking place in some of the Asian markets.

According to experts in the Asian offices of the U.S. Meat Export Federation (USMEF), the financial crisis has induced a frugality campaign in South Korea. This includes calls for consumers to buy domestic instead of imported products. This has resulted in many Koreans avoiding fast-food franchises which are major users of U.S. value-added products. As an effort to attract customers, a French discount store is running ad campaigns stating that 95 percent of goods sold are domestic.

Imported beef prices to Korea have risen as much as 20-30 percent higher than in December. Restaurants serving U.S. or Australian beef do not want to pass on the increased prices for fear of driving away customers. Imported beef prices are expected to climb even higher next month.

The Indonesian rupiah's drop against the U.S. dollar currently means as much as 30-35 percent reduction in consumer purchasing power and higher interest rates and inflation. USMEF's Asian manager reports that sales of U.S. beef in Indonesia's five-star hotels have dropped about 10 to 15 percent. He estimates that Indonesia will suffer the crisis for two or three years. The hotel food and beverage businesses have also slowed. Major U.S. chains have reported a 10-15 percent decrease while the lesser-known establishments are seeing as much as a 39 percent drop in business. Importers are stocking less as they are experiencing credit problems. Banks are reluctant, or are unable, to issue letters of credit for imported goods.

Each country's situation is unique and each has different needs and prospects for recovery, but stable currency is needed for viable long-term markets. The arsenal of tools needed to help our trading partners in Asia resolve their crises must be fully utilized. These tools include developing and putting into place sound monetary practices which, when coupled with credit guarantees and programs like the USDA export credit guarantee programs as well as the IMF assistance plans without further devaluations, should stabilize these economies.

IMF programs can be successful. These are not charitable bail-out programs. These are loans, repayable with interest and with requirements for internal structural changes. I believe that for IMF programs to be successful, they must be adequately funded and focused on requiring the recipient countries to make the long-term internal adjustments that will lead to sound domestic economic systems which include stable currencies, stable taxes, and private property rights upheld.

I want to call your attention to a Senate letter to Secretary of the Treasury Rubin which is attached to your copy of my testimony. I support these senators in their request for greater access for foreign agriculture products as part of these countries' reform packages. This has not only been our fastest growing market, but also one of the most difficult markets in which to attain market access.

IMF loans are not an expense to the taxpayer, but an investment. According to USDA, agriculture will lose at the very least three to six percent of our hard-earned market share in Asia—even with IMF programs in place. The market may also take several years to recover. These loan programs are an investment in our future as well as that of our trading partners.

Where do we go with our products from lost market share and normal production growth in the meantime? As these programs take shape we must also look to expanding existing market access and opening new markets. Our negotiators must have fast track negotiating authority to do this.

Inaction in this matter is not acceptable. Tremendous resources and efforts have been expended to create these markets for U.S. agricultural products whose sales support millions of U.S. workers. A loss of 30 to 40 percent of our agriculture export market would destabilize our industry. IMF-led assistance programs are critical to the overall recovery in the region and fast track is critical to picking up lost market share and expanding access to worldwide markets.

Ours is truly a global economy. When our strongest customers face grave fiscal and financial crisis, as those now occurring in Asia, agriculture is the first to feel the effect as our customers lose purchasing power. Although America's farmers and ranchers are the most efficient and productive in the world, they are not positioned to make production decisions to protect themselves from drastic currency fluctuations in major markets.

U.S. agriculture's ability to gain and maintain market share is based on many factors, including good trade agreements, the administration's ability to negotiate freer and fairer market access with fast track authority, sound monetary policies and the ability to utilize market stabilizing tools such as a properly functioning IMF.

I firmly believe an IMF that lives up to its original charter and fast track negotiating authority are critical tools that the administration must have to protect and keep the U.S. economy stable. These are even more important while our trading partners struggle to restructure their economies. It is extremely important to U.S. agriculture and the nation's economic strength that you do the right thing and pass both of these trade measures early in this session of Congress.

I urge you to provide the funding necessary for the IMF to address the needs of our trading partners in Asia and later this spring to grant the administration fast track authority to continue to open markets for all sectors.

Thank you.

PAT ROBERTS
KANSAS
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COMMITTEES:
ARMED SERVICES
AGRICULTURE
INTELLIGENCE
ETHICS

United States Senate

WASHINGTON, DC 20510–1605

January 27, 1998

The Honorable Robert E. Rubin
Secretary
Department Of the Treasury
1500 Pennsylvania Ave NW
Washington, DC 20220

Dear Mr. Secretary:

In response to the assistance provided to Thailand, Indonesia and South Korea in recent months, we are compelled to comment on the pervasive system of trade barriers imposed on American agricultural products by those and other Asian countries.

We recognize the critical importance of Asia to world economic growth. Likewise, we understand that many Asian businesses and workers will surely suffer as a result of the recent economic crisis and that economic recovery in Asia is important to American exports. However, while the United States must carefully consider its role in assisting financially troubled nations, one of our primary responsibilities should be to represent America's farmers and ranchers.

Within the past year, the Treasury Department has committed approximately $9.7 billion in bilateral lending to troubled Asian economies as part of an International Monetary Fund (IMF) program designed to produce major, structural reforms in their economic practices. However, the restructuring programs reportedly do not include substantial changes that require the recipient countries to provide greater access to foreign agriculture products as part of their reform measures. We believe such a requirement would represent both a fair action on behalf of U.S. producers and a major step toward improving Asia's overall economic health.

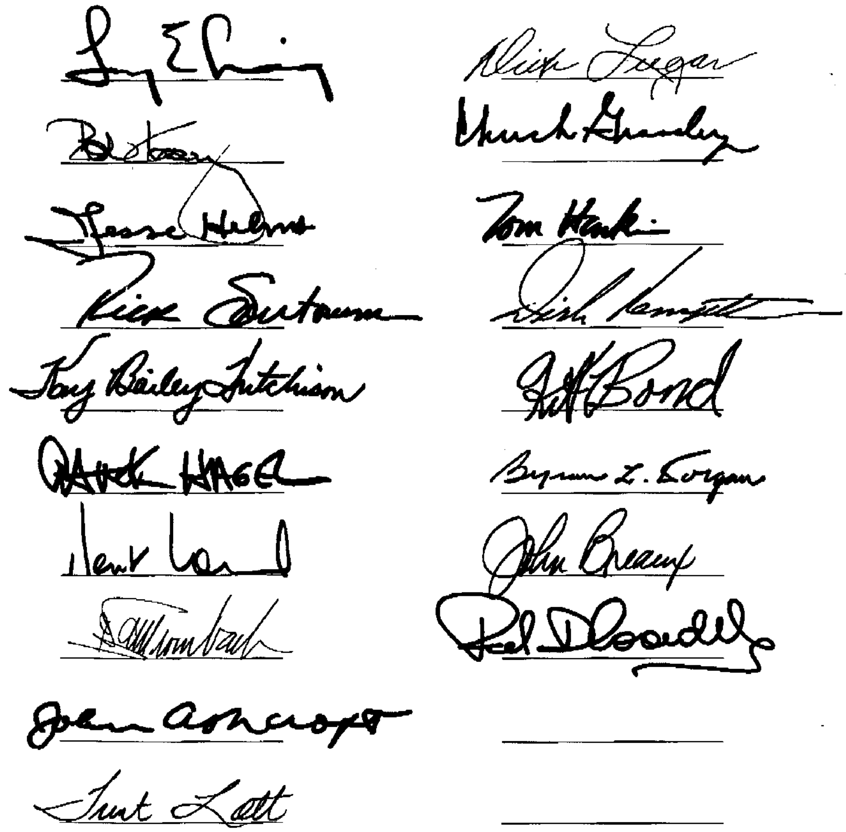
Many Americans will question U.S. assistance for Asian businesses without concurrent efforts to remove the barriers that prohibit American products from reaching Asia. Furthermore, since China, Russia and Japan may ultimately be affected by this global economic problem, it is imperative that you consider the importance of unfair barriers to market access for U.S. producers. Therefore, we respectfully request an opportunity to meet with you to discuss specific issues relating to market access on a country-by-country basis.

Sincerely,

Pat Roberts

Max Baucus

cc: Dan Glickman, Secretary of Agriculture
Charlene Barshefsky, U.S. Trade Representative



Chairman CRANE. Thank you, Mr. Waide.
And now for Hon. Mary Sophos.

STATEMENT OF HON. MARY C. SOPHOS, SENIOR VICE PRESIDENT, GOVERNMENT AFFAIRS, GROCERY MANUFACTURERS OF AMERICA; AND FORMER ASSISTANT SECRETARY FOR LEGISLATIVE AFFAIRS, U.S. DEPARTMENT OF TREASURY

Ms. SOPHOS. Good afternoon, and thank you for the opportunity to testify on the importance of the APEC sectoral liberalization process to the food industry and to the stability of the Asian economies. I'm Mary Sophos, senior vice president, government affairs, of the Grocery Manufacturers of America. GMA represents companies that make and market the world's best-known brands in food and beverages. Our member companies have sales of $400 billion, representing 90 percent of all food and consumer package goods sold in the United States.

GMA has strongly supported trade liberalization in food products at the multilateral level, and we hope that Congress will pass both renewal of the fast track negotiating authority and replenishment of the International Monetary Fund, to ensure that we can continue to expand markets outside the United States.

The Uruguay round and NAFTA made substantial progress in liberalizing world food trade, a $526 billion global market, but foreign food and agriculture remains heavily protected and subsidized. Fast track puts the United States in a position to make liberalization of trade and food a key element of the upcoming review of the WTO agricultural agreement. A strong IMF will help ensure healthy markets for U.S. exports.

While broad-based, multilateral liberalization offers the greatest long-term opportunities and benefits for U.S. food producers, efforts to liberalize at the regional level are also important. Efforts such as the APEC process not only offer the opportunity for immediate progress on key goals, but also provide momentum for complementary efforts at the multilateral level.

Real benefits will result from liberalization of food sector trade. In 1996 agricultural exports generated $60 billion and the largest positive trade balance of any trade sector, $27 billion. USDA estimates that these exports generated an additional $79.5 billion in U.S. economic activity, including $6.7 billion in the food processing sector.

Only 5 percent of the world's consumers live in the United States. If GMA member companies are to continue to grow, they must have access to the exploding food markets of the world. In 1996, $10.7 billion of food and kindred products were exported to East Asia, and this can only increase. Aggregate food demand is projected to grow 100 to 150 percent in East and Southeast Asia over the next 25 years.

In Asia consumers can spend 25 to 50 percent of their disposable income on food. By comparison, U.S. citizens spend less than 10 percent of their disposable income on food. Opening markets will enable these consumers to get more for their money, more value-added food products with greater nutritional value, while spending less of their disposable income on food, allowing more to be spent for nonfood purchases and creating additional U.S. export opportunities.

Trade in processed food products is becoming increasingly important. In 1985 trade in processed food accounted for 50 percent of global agricultural trade. In the year 2000, that percentage is expected to increase to 75 percent.

GMA endorses APEC's sectoral liberalization as an important additional way to stay the trade and investment climate in Asia and strongly supports the administration's efforts in this regard. We welcome the decision taken by the trade ministers at the November 1997 ministerial to identify 15 sectors, including the food products sector, for accelerated market-opening initiatives. We were, however, disappointed that the food products sector was not among the nine sectors for which final liberalization plans are to be concluded in 1998. Australia has been a leader on the food sector liberalization efforts, and interregional food trade is significant. Australia's proposal values it at approximately $100 billion.

The food sector proposal which Australia sponsors would affect specifically agreed upon subsectors. GMA endorses this approach, which also has attracted support from seven other APEC members, including the United States. GMA urges the United States to exercise its strong leadership to ensure that at the APEC leaders' meeting in November of this year the food sector is included among APEC liberalization priorities for 1999.

Our members would greatly benefit from tariff reductions in the processed food sector in APEC countries. Three areas, in particular, show bright promise—soups, processed vegetables, and pet food. Without a considered effort at liberalization of tariff and nontariff barriers, our members will continue to face substantial impediments to trade in Asia.

In the tariff area, the tariff rates on processed food products range from 40 to 60 percent, as compared with an average U.S. import tariff of 6.3 percent for a wide range of both processed foods and commodities. There are extensive regulatory and technical impediments to food sector trade, including product health, quarantine, labeling standards, and inspection requirements.

In conclusion, promoting APEC liberalization in the food sector significantly advances several key U.S. goals. It's fully consistent with, and supportive of, larger trade liberalization objectives, such as the upcoming WTO negotiations in agriculture. It reinforces related efforts to stabilize Asian economies, and it promotes United States trade in one of the most important sectors of our economy. Continued active engagement will ensure that this important sector can realize its true potential in the near term.

Thank you very much.

[The prepared statement follows:]

Statement of Hon. Mary C. Sophos, Senior Vice President, Government Affairs, Grocery Manufacturers of America; and Former Assistant Secretary for Legislative Affairs, U.S. Department of Treasury

Good morning, and thank you for the opportunity to testify on the importance of the APEC Sectoral Liberalization process to the food industry and to the stability of the Asian economies. I am Mary Sophos, Senior Vice President, Government Affairs, of the Grocery Manufacturers of America. GMA represents companies that make and market the world's best-known brands of food and beverages. GMA member companies have sales of $400 billion, representing 90% of all food and consumer packaged goods sold in the U.S.

GMA is proud of its solid record of support for trade liberalization in food products at the multilateral level. Consistent with this history, GMA fully endorses renewal of fast track negotiating authority and replenishment of the International Monetary Fund. We hope that Congress will pass these important measures, to ensure the U.S. can continue to expand markets outside the U.S. The Uruguay Round and NAFTA made substantial progress in liberalizing world food trade. But foreign food and agriculture remains heavily protected and subsidized. This is a $526 billion global market. Fast track puts the U.S. in a position to make liberalization of trade in food a key element of the upcoming review of the WTO Agricultural Agreement. A strong IMF will help ensure healthy markets for U.S. exports.

While broad-based multilateral liberalization offers the greatest, long-term opportunities and benefits for U.S. food producers, efforts to liberalize at the regional level are also important. Efforts such as the APEC process not only offer the opportunity for immediate progress on key goals, but also provide momentum for complementary efforts at the multilateral level.

IMPORTANCE OF FOOD TRADE IN ASIA

The U.S. economy will greatly benefit from liberalization of food sector trade. In 1996, agricultural exports generated $60 billion and the largest positive trade balance of any sector—$27 billion. USDA estimates that these exports generated an additional $79.5 billion in U.S. economic activity and generated 859,000 jobs here in the U.S. Said another way, each dollar received from agricultural exports in 1996 stimulated another $1.32 in supporting activities. In 1996, that included $6.7 billion in the food-processing sector, $15.5 billion in other manufacturing sectors, and $9.7 billion in the trade and transportation sector.

Only five percent of the world's consumers live in the U.S. If GMA member companies are to continue to grow, they must have access to the exploding food markets of the world. Asia is one of the regions with the most significant potential for our members. According to Department of Treasury statistics for 1996, $10.7 billion of food and kindred products was exported to East Asia and this can only increase. Three-fifths of the world's likely population growth and half its income growth through 2010 are projected to occur in East and Southeast Asia. Aggregate food demand is projected to grow 100 to 150% in this region over the next 25 years. Asia is the fastest growing market for U.S. food products. According to the WTO, in 1996, Asia accounted for 23% of world food imports and 18% of world food exports, placing it second only to Western Europe.

Market access barriers limit overall exports and stifle market development that enhances consumer choice. Reducing or eliminating market barriers for our members' products will lower costs to consumers and increase the variety of products offered. In Asia, consumers can spend from 25% to 50% of their disposable income on food. For example, in the Philippines, 47% of total private consumption is spent on food; in Thailand, 29.1%; and in South Korea, 26.9%. By comparison, U.S. citizens spend less than 10% of their disposable income on food, according to 1997 World Bank statistics. Opening markets will enable these consumers to get more for their money—more value-added food products with greater nutritional value—while spending less of their disposable income on food. That frees up some of their disposable income for nonfood purchases. Thus, improving the efficiency of the food sector will have a beneficial, ripple effect on all other sectors, creating additional U.S. export opportunities.

The Asian financial crisis illustrates how closely our economies are interrelated and how financial stability is inextricably intertwined with trade and open markets. Southeast Asia and Korea account for 12% of total U.S. agricultural exports; without a financially stable environment, commercial trade would be severely disrupted. Fortunately, IMF-led assistance programs are helping to stabilize the financial environment and at the same time ensure that austerity does not lead to closed markets. IMF programs are enabling importers to utilize USDA export credit guarantees; IMF-led trade liberalization measures and structural reforms are helping to ensure U.S. products will continue to enjoy access to these markets. GMA fully supports these IMF loans as an investment in our future and supports legislation to increase U.S. funding to the IMF. For the same reasons, GMA endorses APEC sectoral liberalization as an important additional way to steady the trade and investment climate in Asia.

EXPEDITED LIBERALIZATION IN APEC

GMA strongly supports the Administration's efforts to promote APEC sectoral trade liberalization. We welcome the decision taken by the Trade Ministers at the November 1997 Ministerial to identify 15 sectors, including the food products sector, for accelerated market opening initiatives. We were, however, disappointed that the food products sector was not among the nine sectors for which final liberalization plans are to be concluded in 1998.

GMA salutes Australia for its leadership on food sector liberalization within APEC. Australia's proposal includes liberalization of both tariff and nontariff measures. The liberalization would affect specifically agreed upon subsectors. GMA endorses this approach. Intra-regional food trade is significant—Australia's proposal values it at approximately $100 billion. Liberalization of trade in food would increase sectoral trade and investment, decrease prices in food-importing countries, and increase the availability, variety and quality of food products.

The food sector proposal, which Australia sponsored, has attracted support from seven members, including the U.S., New Zealand, Hong Kong, Singapore, Thailand, New Guinea, and Brunei. GMA urges the U.S. to exercise its strong leadership to ensure that at the APEC leaders' meeting in November of this year, the food sector is included among APEC liberalization priorities for 1999.

Our members would greatly benefit from tariff reductions in the processed food subsector in APEC countries. Three areas show bright promise—soups, processed vegetables, and pet foods. APEC countries are a major potential market for soups and broths. In China and Taiwan, high duties are a major barrier to trade. This sector has great promise if liberalized—soup consumption is high and consumers are beginning to demand convenience foods as their standard of living improves. Certain processed vegetables are also of interest. For example, frozen french fried potatoes are the leading processed potato export from the U.S. Tariff liberalization would provide the U.S. processed potato industry and U.S. potato growers new opportunities for growth. Finally, pet food is an area of great interest to our members. U.S. pet food exports to APEC countries represent two thirds of total U.S. exports. U.S. exports grew nearly 80% in the last four years. Commercially prepared pet food is a high value, value-added agricultural product, and our members are the most competitive in the pet food industry.

Without a concerted effort at liberalization of tariff and nontariff barriers, our members will continue to face substantial impediments to trade in Asia.

Tariff Barriers

In the tariff area, the tariff rates on processed food products range from 40% to 60%, as compared with an average trade weighted tariff of 3.5% for industrial products. Many sensitive items have high tariffs, such as basic and processed dairy products. Thailand's tariffs on high-value fresh and processed food products will remain high (in the 30% to 40% range) even after reductions of between 33% and 50% from current rates under the WTO rules. Taiwan maintains tariffs high enough to be a significant export barrier, such as 40–42% on fresh fruit, 35–40% on processed vegetables, including juice, and 21–24% on sunflower seeds and oil. Malaysia regulates chicken imports with a tariff rate quota that ranges from 50% to 70%. In comparison, according to a report prepared by USDA's Economic Research Service entitled: APEC Situation and Outlook, the average U.S. import tariff for a wide range of both processed foods and commodities is 6.3%.

Non-tariff Barriers

There are extensive regulatory and technical impediments to food sector trade. These include product, health, quarantine and labeling standards, and inspection requirements. Among barriers to food and agriculture trade in Asia identified in the most recent USTR National Trade Estimates report are the following:

- Taiwan restricts importation of agricultural items; Taiwan requires special prior approval, amounting to a *de facto* ban. Taiwan also maintains unreasonable quarantine restrictions on fresh and frozen chicken, certain cuts of pork, peanuts, live dairy cattle vaccinated against brucellosis, and adzuki beans.
- China's sanitary and phytosanitary (SPS) measures prohibit imports of U.S. citrus, plums, grapes and Pacific Northwest wheat. China's restrictions on imports of citrus and pacific Northwest wheat are not based on sound science, and USTR has been actively pursuing these issues.

As an aside, on the issue of SPS measures, we applaud the results of the Uruguay Round—in particular the requirement to base such measures on scientific evidence and urge the U.S. government in the upcoming review of this agreement to ensure and maintain the strength of this requirement.

- Japan continues to restrict entry of numerous U.S. fresh fruits and vegetables, for phytosanitary reasons. Tomatoes, potatoes and plums are banned outright.
- Korea maintains quotas and tariff rate quotas with prohibitively high rates for agricultural and fishery products. Also, contrary to international practice, Korea approves food additives on a case-by-case basis, rather than allowing additives that are "generally recognized as safe" to be used in *all* food products. In particular, the Food Additives Code will often allow a food additive in a traditional Korean food product and not allow it in an imported product.
- In Malaysia, the sole authorized importer of agriculture and food products is a government corporation. The corporation is responsible for ensuring purchases of domestic products and therefore has broad powers to limit imports.

Trade in processed food products is becoming increasingly important. In 1985 trade in processed food accounted for 50% of global agricultural trade. In the year 2000, that percentage is expected to increase to 75%. Lack of market access is a major constraint to increased trade. Removing tariff peaks and confronting nontariff barriers would help ensure the healthy growth of the high value-added processed food sector.

CONCLUSION

GMA applauds the efforts of USTR to date to promote expanded global trade in food. Promoting APEC liberalization in the food sector significantly advances several key U.S. goals: it is fully consistent with and supportive of larger trade liberalization objectives—such as the upcoming WTO negotiations in agriculture; it reinforces related efforts to stabilize Asian economies so critical to our exporters; it promotes increased U.S. trade in one of the most important sectors of our economy; and it has a beneficial ripple effect on other sectors by opening overseas markets to competitively priced food products and thereby freeing up consumer disposable income for purchases in other sectors. Continued, active engagement will ensure that this important sector can realize its true potential in the near term. The APEC liberalization process can serve as a catalyst for promoting global cooperation in reducing barriers to trade and investment. This will reinforce the multilateral trading system and the WTO. It will also help to ensure that the upcoming WTO Agricultural Round is well positioned to tackle these issues effectively.

Chairman CRANE. Thank you, Mary.

Mr. Webber, you mentioned approximately 185,000 jobs in the chemical industry that are immediately and directly related to trade, to exports?

Mr. WEBBER. Exactly. Yes, sir.

Chairman CRANE. I would like to raise the question with all of you, because I don't know what the numbers are, nor the percentages of members of the work force in the various industries you represent: Do those 185,000 know that their jobs are directly related to exports?

Mr. WEBBER. I hope so. We make——

Chairman CRANE. Well, now, wait 1 second. You hope so?

Mr. WEBBER. We make every effort with our 200 member companies to make sure they get the word out in terms of where their sales go. It's hard for me to imagine that the folks in a typical chemical company don't understand that sales make up——

Chairman CRANE. Well, to be sure, but then that reminds me of the AFL–CIO members that worked for Boeing that were out protesting against fast track renewal, when Boeing is totally dependent upon exports to guarantee both its survival and the employment of the guys that were out protesting. This is one of the frustrations I think all of us that went through that fast track battle last November experienced. And that is the monumental ignorance in this country on the importance of our exports.

A big part of that—and I've got the same problem back home. I've got the corporate headquarters of Ameritech, Sears, Motorola. We've got giants like that, but they're not the ones that are the major source of our exports out of my home State of Illinois. We're the fifth largest export State in the Union, and yet over 90 percent of our exporters are companies employing 500 or less.

You bring up an issue like trade at a town meeting and people start snoring in the audience, because of a lack of understanding of the importance of exports. That is why I've been trying to urge chief executive officer's and people in the business community to get that information transmitted on how vital it is to the business involved, how vital it is to the jobs that are affected. I think, frankly, we have not succeeded nearly as well as the demagogs on the opposite side of that debate that try and scare the socks off of everybody about letting any foreign goods cross our borders.

Let me throw a couple of generic questions out to all of you, and one has to do with bribery and corruption, because we've heard of a lot of that as a basis for some of the Asian economic instability. To what extent can, in your estimation, that crisis in Asian countries be directly linked to bribery and corruption? Have you any input on that? Any of you?

Mr. MOORE. Mr. Chairman, I can't speak to that, but we can speak to our competition in certain countries, where maybe it's not bribery and corruption, but it's the cronyism.

Chairman CRANE. Good old boy networks?

Mr. MOORE. Yes, exactly. We have competitors in certain countries that got into business and have protective trade barriers that are supported by the governments of those countries. So that may be close to what you're talking about, but that does affect us in a number of countries in the Asian region, in particular.

Chairman CRANE. Yes. Have all the rest of you had similar experiences like that butting up against good old boy networks?

Mr. HUDSON. I think it's more cronyism than bribery and corruption in the high-tech area that tends to affect things. We certainly, in Japan, for example, in the communications industry saw a great protection when NTT pretty much had control of the market. Even though they privatized, there's still these very cronyistic tendencies to continue to use their same sources of Japanese supply, rather than United States suppliers. We're wearing away at it, but it's still there. I don't think corruption, however, played a big role in that.

Chairman CRANE. Anybody else got a point to add?

Mr. WEBBER. Well, I would identify with this gentleman's comments. Cronyism is a problem, and it's always there; it may always be there, for all we know. It's something, I suspect, in the final analysis we're going to have to confront.

In terms of bribery and corruption, we have no direct reports that we've run into that problem in our trade efforts overseas.

Chairman CRANE. OK. To what extent do you think Japan will be able to absorb exports from some of these devastated Asian countries? I mean with their devastated economies. To what extent do you think Japan can absorb some of their exports rather than all of them coming here?

Mr. HUDSON. Sir, without stimulus, I don't think there's much capacity to do that. I think the Japanese public is very demoralized and quite concerned about their financial stability. And until they see some fresh signs of a reviving economy and some direction of continual growth, I don't think they can absorb a great deal.

Chairman CRANE. Anyone else have any comment on that?

Mr. MOORE. Well, Mr. Chairman, I mentioned in my testimony, I think that China and Korea and Japan have got to step up to the bat. They've got to open up their markets more to absorb some of what we see as the threat of increased exports from Asia. We can't be the recipient of everything that comes out of Asia. That just can't be the case. Those economies have had their strong days, and they need to step up and do their part. We don't see the regional leadership right now going on that one would expect.

Chairman CRANE. Well, do you think that Japan's trade policy historically had anything to do with helping to contribute to the current crisis?

Mr. MOORE. Surely. Surely, it does. I'd agree with that, Mr. Chairman.

Mr. WEBBER. In terms of chemicals, Mr. Chairman, it's hard to imagine Japan being able to absorb chemicals. Their chemical production is quite significant. Their export efforts, of course, are well known. So it's hard for me to imagine there'd be any absorption, at least from the chemical industry, in that part of the world.

Mr. HUDSON. In terms of Japan's being a very large investor in other parts of Asia, to a large degree, there was too much capital flowing into those economies, and when you have too much capital flowing into economies, you don't necessarily get the best investment environment. So in that sense, maybe they were part of it, but they certainly had a lot of help from, I think, some European investors and perhaps even some American investors in that regard.

Chairman CRANE. Mr. Matsui.

Mr. MATSUI. Thank you, Mr. Chairman.

I would just like to follow up on Mr. Crane's observation or question, and your response to it. The scenario that I fear is that we'll have minimal success in getting the Asian countries to agree to conditions, or perhaps they'll say they'll do these things and end up perhaps not implementing them. And we give the $3.5 billion, and then maybe later this year, or perhaps next year, we give the balance of $14.5 billion. So it's $18 billion. The trade deficit in this country explodes because the reforms don't occur. The Japanese don't stimulate their economy. They keep it closed, and the Chinese economy slows down, and so the hit is on Western Europe and the United States.

Then what happens is that the protection sentiment, which is not good here anyway, will explode, and that will be a real problem for all of us. I only mention this because I would just like to reiterate, I think, what the Chairman has said, and I think what all of you know—so I'm really preaching to the choir—that the private sector will have to do a better job in terms of informing its membership—that is, the employee base of all the companies that we're talking about here; we've got literally the whole U.S. industrial base here—in informing their membership of the value of trade. One-third of the growth in the United States in the last 5 years has been based upon export opportunities, and people just don't know that. As Chairman Crane has said, they either fall asleep or they're screaming at you for losing U.S. jobs by supporting fast track or free trade initiatives.

And I might also, Mr. Webber, clarify—well, at least from my perspective—clarify an observation you made. The President and the administration is not abandoning fast track. What it is is that, since November 14, when we left the Congress in recess, I know for a fact that Mr. Bowles, the Chief of Staff, Ms. Barshefsky, and others in the administration have been trying to find some way to add 1 or 2 or 15 votes to the number we had when we were not able to bring it forth and have not been successful.

I think we've hit a wall. I don't think fast track is going to happen this year. I think it may not happen next year. I think Bill Archer has said before that it may not happen until after 2000, 2001, since we didn't get it last year.

I think rather than lament, we should really use this as an opportunity to start the educational process. I've come to the conclusion that every generation we have to redebate the whole issue of the value of trade and internationalism in this country, and we are probably at that point again.

I'd like to say to the American Farm Bureau—and I said this, I think, 2 or 3 weeks ago, when we had an agriculture hearing in this Subcommittee—that the agriculture industry was very late, and as a result of that, Members who should have supported us from the agriculture-producing regions of the United States were not there. And the reason for it—and I don't blame you; you were just a participant in your overall association. I blame the California Farm Bureau. I blame all the Farm Bureaus. What they did was they held out. They wanted to get every ounce of lemon out of that lemonade. They squeezed it dry. Then they came onboard, but by that time, the horses had left the barn.

I think we have to just put fast track a little higher in our priorities. We can't say that it's important, but we want something else. Because, frankly, the whole concept of APEC, the Summit of the Americas—all of these initiatives that we saw 3 or 4 years ago will be meaningless unless we give the President negotiating authority. It just seems incomprehensible that we can't communicate that, but that's the reality of the situation.

And I don't know if anyone wants to comment, but I'd be happy to take an observation or two.

Ms. SOPHOS. Well, I just wanted to say, I think it is our responsibility to do a better job of communicating with employees in our industries. I think some of our member companies have been better at it than others, but I think it could be improved. There also should be commitment on the part of the Congress to address it in a time to be able, realistically, to let us mobilize support.

I also think you're absolutely right; if there's no fast track negotiating authority, it's very unlikely that we'll see any productive agriculture round in 1999.

Mr. MATSUI. Right. Right. Absolutely.

And I might just say, the real problem we face on the lack of fast track is that there's no big bang. It's not going to create an economic catastrophe. It's not going to have any appreciable impact on growth. It's just that 3 years from now we'll all say, Geez, what happened? The Japanese or the Europeans have captured the Latin American market. The Asian market is slowly going someplace else. And then I'll feel, all of a sudden, we're finding that our research, development, and our basic research will start to diminish because we're not doing the whole cyclical aspect of basic research to manufacturing, to marketing, to sales. We'll begin to lose those opportunities.

I know, Mr. Webber, you want to respond.

Mr. WEBBER. Well, first of all, I find your comments reassuring when they come to fast track, although even 2001, 2002, a lot could happen between now and then, as we sit on the sidelines.

Mr. MATSUI. All we need is about 50 more votes.

Mr. WEBBER. But we're going to continue to work at it. The Chairman was probably not impressed with my comment when I said I hope our employees are aware of the fact that their jobs are tied to exports. Mickey Kantor, last November, addressed our major November conference in Houston and said that the chief executive officer's ought to write on every paycheck the percentage of the employee's pay that is related to exports. That's probably not a bad idea.

The only other thing I would add is, during the NAFTA debate, we flew planeloads of blue collar employees into this town to walk the corridors and meet with our Members of Congress. The shining example was NALCO, from your home State of Illinois, talking to Members of Congress about the importance of NAFTA and the importance of exports. So most of us have got the message, but I agree, we can do a better job, and we'll continue to try.

Mr. MATSUI. If I can just say this, we're not throwing—neither of us, and I don't think anybody is trying to blame the private sector for the loss of fact track. That is not at all what I hope you gather from this discussion, because, as I said, I just don't think that all of us, including myself and I think Members of Congress who support free and open trade, do not realize the depth of the lack of knowledge throughout the United States on this issue.

I participated—I know Phil did as well—at a recent conference of the Institute of International Economics. We started from the basics again. How do we communicate the values of this? Someone suggested Oprah; I don't know if that's a good idea after Ohio. [Laughter.]

That might be counterproductive. But at least we need to get back to the basics. We can't rely upon foreign policy experts like the Council of Foreign Relations up in New York any longer to sell this whole concept of internationalism. I think that day is long gone. It's all kind of Main Street USA now. How we get to them, I don't know. I wouldn't want anyone to think, leaving this hearing today, that there's any blame being thrown. I fully take responsibility for our loss, and I think all of us just have to find a way to turn it around.

Mr. HUDSON. I really would like to add some comments to it and give you some assurances. I think, in a way, success with NAFTA and the involvement of our employees in that, we kind of let go a little bit and assumed that that message was still in place——

Mr. MATSUI. Right. That's a good point.

Mr. HUDSON [continuing]. And that when it came to fast track, it would smoothly go in there, and we didn't anticipate the very strong effort by the AFL–CIO to try to counter that.

In the case of the employees in my company, they not only know the material goes overseas, but they are talking to their counterparts by telephone overseas on quality issues and delivery issues. During the fast track debate, our employees wrote, telephoned, wired. I will tell you, I was very disappointed with some of the responses that they got back from Congressmen who were claiming certain things were in fast track that weren't there, and we're going to follow up with those Congressmen, I assure you, and get that straightened out.

But trade in our company has been a very high-growth sector in our United States operation, and our people are very sensitive to that because one of our largest trading partners is our Japanese company who has a very, very high requirement on zero-defect product and ontime delivery. So there's a constant dialog going back and forth in that area.

The trade associations that I represent also have an education program because we're trying to convey the whole trade message in an orderly fashion, to not only our direct employees, but also to the numerous small business suppliers that support our businesses, because I don't think some of them realize that if they're making a mold for one of my molding plants, that that molded part is actually going over to Asia, and the fact they've got that mold to produce is very much tied into trade and that issue, because I don't think that message got out as well as it should.

So we all certainly got a lesson on this problem back in November, and I think a lot of us have awakened to the fact we've just got to keep at it.

Chairman CRANE. Well, and I think something else to keep in mind and get the message out is that trade constitutes one-third of our total national economy. It's been the fastest growing component of our national economy——

Mr. HUDSON. Right.

Chairman CRANE [continuing]. And with this fast track setback, God forbid, if we're not negotiating any extended trade agreements until the next millennium, who knows what kind of an economic hit we could take.

And the other thing, I think, to stress—and I mentioned this before—if you look at the history of our parties, Matsui's party were the free traders and Republicans were the total protectionists until after World War II, and now the union influence really——

Mr. MATSUI. Don't point to me.

Chairman CRANE. Well, no, you had the guts to stand up and be counted. I'm proud of you, Bob, and you're not alone there.

But, on the other hand, that has had a diminishing impact on the Democrats' commitment, and the Republicans still have our Smoots and Hawleys. I won't identify them specifically here in public hearing, but we still have Smoots and Hawleys on our side. Getting a better understanding out there, and to get the American people to focus on the realization. This is not a party issue; it has nothing to do with Democrats versus Republicans. It's what's in the best interest of our National economy. It requires a big educational effort, and we appreciate all that you folks have contributed thus far, and look forward to working with you in the future.

And with that, I will thank you all for your testimony, and that concludes our hearing for today. And the record will be open until March 10, and thank you all for your involvement. We appreciate it.

[Whereupon, at 2:32 p.m., the hearing was adjourned, subject to the call of the Chair.]

[Submissions for the record follow:]

Statement of Phil M. Condit, Chairman and Chief Executive Officer, Boeing Co., Arlington, Virginia

Mr. Chairman, Members of the Subcommittee. Thank you for providing me with the opportunity to share The Boeing Company perspective on the critical issue of trade with Asia. This is an issue that has taken on heightened importance to our country and our company with the recent economic turmoil in Asia. I applaud you for scheduling this important hearing.

I would like to place my remarks about trade with Asia within my company's frame of reference. The new Boeing is the world's largest aerospace company. While Boeing is widely recognized as a world leader in the production of some of the world's finest commercial airplanes, our recent mergers with McDonnell Douglas and Rockwell North America dramatically expanded our expertise in the areas of military aircraft, missiles, information systems and space systems. My comments on trade policy are principally oriented toward our commercial aircraft business. But, there is little doubt that our defense and space sales are also affected by U.S. trade policies toward the region.

The Boeing Company's most important international challenge today is to maintain access to the global market. Exporting is not a luxury for Boeing. It is our lifeblood. Without success overseas, we cannot remain the world's premier aerospace company. Nor can we continue to support the hundreds of thousands of high quality jobs we do across our nation.

Today, the Boeing Company is one of America's largest exporters. Historically our export share has been about 65 percent of our business. In the next twenty years, nearly three-quarters—or 75 percent—of future business will be outside North America. While we sell the majority of our commercial aircraft overseas, approximately 85 percent of the value of our airplanes is U.S. made, provided by thousands of U.S. suppliers located in every state of the union.

Mr. Chairman and Members of the Committee, if there is a single message I could leave with you today it is this—the United States must continue to play a leadership role in liberalizing trade worldwide and we must lead by example. Without continued strong leadership by the United States, the enormous progress we have made to date to advance open trade will begin to slip backwards. And such a development would significantly hurt the economy of the world's largest exporting and trading nation—the United States—to say nothing of what it would do to the economies of all the other countries in the world.

Having just returned from Asia, where I met directly with our customers and government officials, I cannot stress enough the importance of continued open trade to Asia's economic recovery, and in turn to our own continued success in that important market.

In the months ahead, currency devaluations in Asia are likely to lead to ballooning trade deficits with several Asian nations. And those deficits, in turn, are likely to create enormous pressures on the United States to limit the access that Asian businesses have to the U.S. market. You must resist those pressures. Not only will they severely damage Asia's ability to recover from its current economic troubles, but ultimately they will hurt the U.S. economy, U.S. exporters and U.S. consumers as well. Protectionist economic policies embraced earlier in this century proved disastrous. We do not want to repeat past mistakes. Apart from supplemental IMF funding which the Boeing Company strongly supports, the single most important step the United States can do to help Asia recover from the current economic turmoil is to keep its market open to Asian goods and services. And stabilizing Asia is essential to keeping the global economy—our own economy included—growing and prospering.

Some may criticize such a policy as one that gives Asia a blank check to export its way out of its economic troubles. You no doubt will hear calls in the months ahead for a trade policy that is "fair" as well as "free." Well, the Boeing Company is as interested as anyone in policies that ensure a level playing field. Frankly, we see in Asia's current economic crisis an opportunity to advance our fair trade goals. Asia needs to pursue policies that stem the outflow of foreign investment capital. It needs to restore investor confidence in the region and strengthen Asian currencies. And economic reform is key to achieving those goals. There's no getting around this fact. So, in our view, there is a silver lining to this dark cloud. We can and must act to both stabilize Asia and advance the economic reforms that, in the long run, will make the Asian economies more like our own—market-driven, decentralized and open.

Mr. Chairman, we cannot turn our backs on those Asian economies that are actively executing painful prescriptions for economic recovery—a recovery that will involve some degree of export growth. To do so would hurt them and damage our own economic interests.

I now would like to give you a sense of the importance of Asia to The Boeing Company and then outline some of the trade policy measures that we believe will be critical to restoring confidence in Asia and, in turn, ensure that Asia remains a vibrant market for The Boeing Company and the hundreds of thousands of workers we employ directly and indirectly.

Mr. Chairman, no one region is more important to Boeing's fortunes than the Asia Pacific region. Over the next twenty years, the Asia Pacific market will represent 35 percent of the world's market for commercial aircraft—making this region the largest in the world and moving the historic leaders, North America and Europe to second and third positions. Through the year 2016, Asian carriers are expected to purchase $390 billion or 4733 commercial aircraft—over one third of the $1.1 trillion retail value of the world's requirement for aircraft.

The Asian market is also important for our Information, Space and Defense Systems group, which is focused on maintaining and expanding its involvement in several key areas including space launch services and communications infrastructure—primarily space based. These technologies and the markets they create are destined to become as important as the commercial aviation industry is to our domestic economy. These markets have high entry barriers and once missed, opportunities to effectively compete will be gone forever. Policies that preclude U.S. contractors, and in particular Boeing, from competing fairly with international competitors will have a long-term adverse impact on the United States. The Boeing Company has important customers in virtually every Asian country, and our ability to sell our products internationally means more competitive prices for our U.S. Government customer as well as strengthened U.S. political and military ties with our allies.

While the magnitude of the numbers is impressive, they do not tell the full story about the importance of the Asian market for our business. For our commercial airplane business, five out of the top ten international commercial jet markets are in Asia including China, Japan, Korea, Singapore and Australia. China is projected to be our largest international market with $124 billion worth of projected sales over the next 20 years. Last year alone, we sold close to $5 billion in planes to China. Japan has historically been our largest non-U.S. market and will continue to be a critical market for commercial airplanes with market projections exceeding $85 billion.

We have numerous airline customers in this region and are currently planning for more than 300 deliveries to airlines in Asia for 1998, 1999, and 2000. This represents approximately one-fifth of our total production over the same period.

Our Asian customers are among the most customer-focused and profitable airlines in the world, including such premier carriers as Japan Airlines, All Nippon Airways, Japan Air Systems, Korean Airlines, Asiana, Thai Airways International, Malaysia Airlines, Garuda Indonesia, Philippine Airlines, Singapore Airlines, EVA Airways, China Airlines, Cathay Pacific Airways, Qantas and Air New Zealand, and 34 jet-operating airlines in China.

These airlines comprise the world's largest operators and customers of Boeing widebody aircraft including 747s, 777s and 767s. China will be our largest non-U.S. country market potentially for single-aisle 737s and 757s.

In addition to the Asia Pacific region being the key market for 777s, this year the 777–300 will be introduced to a number of Asian carriers. The 777 remains remarkably healthy even with the present situation in Asia.

With the Asia/Pacific region having the world's highest traffic growth and densest routes, Asian airline customers are highly competitive and focused on quality, reliability, excellent airplane economics, customer service and passenger comfort. When we successfully meet the high demands of our discriminating Asian customers, we increase our sales prospects elsewhere.

Mr. Chairman, there is little doubt that our continued access to this critical market is being affected by the economic turmoil in Asia. The Boeing Company has forecast both the near and longer-term effects on our commercial airplane business of the Asian economic problems.

Our most recent analysis shows that over the next three years we expect 60 fewer commercial aircraft deliveries to Asia. For the most part, Asian airlines are indicating that they will take their 1998 deliveries. This implies that most of the vulnerability to our production planning resides in the 1999 and 2000 time frame, or beyond, and is limited primarily to the 747 and 777 lines. The demand for those aircraft in other parts of the world is robust and we have confidence that we will be at the levels of production in that time frame that we enjoy today. Additionally, those deliveries are far enough into the future that we can proactively manage our production. We do not envision a significant reduction in near-term sales for our defense and space business although some future orders may be delayed.

However, while the near-term economic effects on The Boeing Company and its workforce of the Asian financial crisis may be manageable, I cannot overstate the key role of the U.S. Government in developing constructive solutions to the problems facing this region. If the Asian economies fail to recover or the situation in Asia worsens or spreads, Boeing will have to revise our analysis.

Mr. Chairman, there has been considerable attention focused on the critical importance of restoring near-term market confidence and the role of supplemental IMF funding to ensuring global financial stability. The Administration has done an outstanding job in moving quickly to lay the groundwork for containing the turmoil in Asia. There is little doubt that there would be damaging financial and export market effects if the United States failed to provide the financial support for the IMF. It is in the interests of all Americans to ensure such funding is provided.

But as I noted earlier, IMF funding is not the sole answer to the problems facing Asia. We need to work with the countries in the region to rebuild their economies in a manner that strengthens our ties with this important region. And a key element of that prescription is U.S. trade policy.

At the beginning of my remarks, I underscored that open trade is Boeing's lifeblood. Our ability to sell aircraft to countries in Asia depends very much on a country's overall economic growth rates, which are directly affected by their ability to export. This is particularly important now given currency devaluations that have made U.S. products to Asia, including airplanes, more expensive. While it may be simplistic for this knowlegeable Committee, open trade means our customers can sell us their products and, in turn, buy our airplanes, and numerous other U.S. products and services—like computers, medical equipment, insurance and agricultural goods.

I spoke earlier about the need for the United States to maintain its commitment to open trade. I want to acknowledge the Herculean efforts of Ambassador Barshefsky and specifically highlight her efforts to conclude the World Trade Organization (WTO) Financial Services Agreement and to secure additional trade liberalization initiatives at the most recent Asia Pacific Economic Cooperation (APEC) meeting in Vancouver. These agreements are a clear endorsement of the desire of most countries to move toward greater trade liberalization and market opening—especially under difficult economic circumstances.

We cannot allow this trend to be reversed or even slowed. To the contrary, we should press the case for free trade. As I mentioned at the outset, Asia's current economic troubles provide an opening for the United States to aggressively pursue a number of trade initiatives that will help increase U.S. firms' access to the Asian market to make sure that trade flows in both directions.

One of the most imminent and important trade liberalization/market access initiatives before the United States today is the negotiation on China's accession to the World Trade Organization. After years of arduous negotiations, it now appears that there is movement on both sides to work toward a commercially-acceptable protocol that would enable China to become a full member of the international trading system. Recent Chinese offers in the areas of financial services and distribution, coupled with their agreement to take on the obligations of the Information Technology Agreement, are welcome signs of China's commitment to open its market to foreign goods and services.

China's accession to the WTO—which will include a commitment to fundamental GATT/WTO principles; a good market access package that will better ensure that U.S. businesses and agricultural interests can sell and distribute in China; and effective safeguards—will be a key event in ongoing efforts to further liberalize trade in Asia and to ensure that U.S. firms fully benefit from this agreement, we will also need to extend MFN unconditionally to China. Without it, U.S. firms and workers will not be able to take full advantage of improved market access or the multilateral dispute settlement procedures that will be key to safeguarding access to this market.

The time is also ripe to normalize commercial relations with Vietnam. The President should issue and the Congress support a Jackson-Vanik waiver for Vietnam along with the appropriate waivers to open the Export-Import Bank and the Overseas Private Investment Corporation. Without access to Eximbank, U.S. firms and workers will be at a serious competitive disadvantage in this growing market as compared to their European and Japanese competitors.

I would like to spend a moment on U.S.-Japan trade relations, given the heightened attention that we anticipate as Japan's exports to the United States continue to climb. We believe it is important that Japan clearly understand the gravity that the world attaches to its playing its role as the engine of growth in the Asian arena. The Administration's stance toward Japan has been firm in demanding the opening of its markets and deregulation as part of a broader program to stimulate economic growth. The style in which we convey the necessity for harsh reforms in Japan should be accompanied by public words of praise on the amount of contributions the Japanese government and people have pledged to help Asian economies stabilize and recover. We remain convinced that it would send the wrong signal for the United States to take action to limit Japan's access to our market. Other measures for addressing Japan's unwillingness to implement constructive economic policies must be found.

Mr. Chairman, with respect to other Asian countries, I would note that recent IMF agreements work to liberalize trade and open markets in Asia. During the upcoming months, it will be difficult for Asian leaders to take these appropriate, but sometimes difficult, measures to open trade. It will be politically impossible for them to pursue these initiatives if the United States takes action that could be interpreted as moving away from open trade.

In conclusion, I want to reiterate the important role that trade must play in restoring economic vitality to the Asian region. The United States must show vision in developing and implementing trade policies that will advance the interests of the U.S. economy into the next century. Now is not the time to retreat from our historical commitment to open trade and the benefits that have accrued to the U.S. economy, U.S. industry and U.S. workers.

Thank you.

Statement of Joseph D. Russo, President, IPSCO Steel Inc., Muscatine, Iowa

Chairman Crane and Members of the Trade Subcommittee, this testimony is submitted to the Committee on behalf of IPSCO Steel Inc. As President of IPSCO Steel Inc. I am pleased to express our views about the Asian financial crisis and its potential impact on the steel industry.

IPSCO operates a new 1.2 million ton per year steel mini-mill in Montpelier, Iowa that produces flat plate and hot-rolled steel coils. The company has invested $450 million in land, buildings, equipment and working capital for this greenfield facility. Its sister company, IPSCO Tubulars Inc., operates a pipe facility in Camanche, Iowa and a pipe mill in Geneva, Nebraska whose combined production capacity is 345,000 tons per year. IPSCO is also in the process of constructing a facility with an annual capacity of 300,000 tons per year in Blytheville, Arkansas. In addition, another sister company PaperCal Steel Co. operates a 200,000 ton per year coil processing facility in St. Paul, Minnesota. We directly employ between 800 and 1000 employees in these operations and create thousands of additional jobs through the construction, supply of materials, services, and transportation of products to and from our mills.

We are a member of the Committee on Pipe and Tube Imports ("CPTI"), a twenty nine member organization of U.S. steel pipe and tube producers that represents about 80% of pipe and tube production.

Mr. Chairman and members of the Committee, we are confident and so are steel analysts that our Iowa plant is one of the lowest cost producers of flat plate and hot-rolled coils in the world. Therefore, we fear no fair competition, domestic or foreign. IPSCO would like to express its concerns about unfair foreign competition and government-distorted trade policies that have and can severely impact our return on investment and our ability to expand low cost capacity to serve the U.S. and world markets. The success of the IMF package for Korea and other Asian countries in a way that not only alleviates the near-term liquidity crisis but also eradicates government directed lending practices that target favored industries is critical to the future success of our company, our workers, and the entire U.S. steel industry.

According to the International Iron and Steel Institute ("IISI") statistics, in 1997, South Korea, a country with 46 million people was the sixth leading steel producer in the world at 42.2 million metric tons, behind only China, Japan, the U.S., Russia and Germany. Korean steel production per capita is 2.5 times greater than the U.S. In addition, Pohang Iron and Steel Company (POSCO), founded by the Korean government in just 1967, is forecast to be the largest single steel producer in the world in 1998 with estimated production of over 28 million tons.

The Korean government still owns 36% of POSCO, which gives it a controlling interest in the company and the ability to direct the company. The Korean government has clearly strongly supported and targeted a build up of its steel industry, but never more so than the case of Hanbo Steel, Korea's second largest steel company. Hanbo is certainly the poster child for the entire Asian economic crisis. Between 1992 and 1996, Korean banks, led by the government-owned Korean Development Bank, loaned almost 5.8 billion dollars to Hanbo to build a greenfield 9 million ton steel complex on Asan Bay in Tangjin, Korea.

At the start of this period, Hanbo's debt-equity ratio was already 5 to 1. By the time the company declared bankruptcy in January 1997, the debt-equity ratio had ballooned to over 22 to 1. Hanbo, a clearly uncreditworthy company, obtained these loans because of government directed lending practices and the Korean government policy to expand the steel industry. There can be no doubt that these loans were government directed. The largest creditor was a government owned bank and a number of Hanbo executives, government officials and bankers have been sentenced to jail in Korea for bribery. You simply don't bribe government officials to get you bank loans unless government officials can get you bank loans. Even after the company filed for bankruptcy, the government continued with subsidies. As Trade Minister Han Seung Soon stated on February 4, 1997 "The priority is to finish the construction of Hanbo's steel mill by the end of this year through additional financing and commissioned management by Pohang Iron and Steel." Another Finance Ministry official, Yoon Tue Yong, said that, "for the benefit of the national economy, we must keep the plant operating."

On February 18, 1997, the Committee on Pipe and Tube Imports and three U.S. flat rolled steel producers filed a request with USTR and the Department of Commerce to pursue a dispute settlement case at the WTO for Korean government Subsidies Code violations with regard to Hanbo subsidies. The administration has not taken any action yet and to the best of our knowledge this is largely because, once again, foreign policy and national security concerns within the administration have been able to outweigh our trade policy interests.

The Korean government has admitted that it has paid off small and medium sized trade creditors of Hanbo so that they would not also go into bankruptcy. While the goal may be laudable, the direct payment by a government of the company's debts represents a direct subsidy to Hanbo steel. For the past year, Hanbo has not, to our knowledge, published any financial statements so we have no idea how much the company conovernment controlled POSCO and Dongbu Steel had jointly bid 1.8 billion dollars for the assets of Hanbo. However, amidst suspicions that the government was forcing POSCO to make the bid and after extremely adverse world market reactions to the bid, the sale never materialized. At this point, it is clear that Hanbo can never reorganize itself and go back into business. What is unclear is whether the bankruptcy trustees in Korea are free enough from government control to fairly represent the creditors interests and sell Hanbo's assets to the highest bidders regardless of whether they intend to operate the equipment in Korea or move the equipment to another country.

Various committees in Congress have already heard enough testimony as to why the financial crisis occurred and how the IMF and Treasury Department plan on solving it. However, since the inception of the discussions with the IMF, our trade counsel and our associations have pressed the Treasury Department to make sure that U.S. taxpayer dollars would not be used to subsidize our competitors in Korea. Initially, we were very pleased with the conditions announced by the Korean government and the IMF. These included:

- "The commercial orientation of bank lending will be fully respected, and the government will not intervene in bank management and lending decisions. Remaining directed lending will be eliminated immediately.
- No government subsidized support or tax privileges will be provided to bail out individual corporations."

If the Korean government lived up to these commitments it would radically transform the manner in which business is conducted in Korea and return competition between U.S. and Korean companies to a level playing field. Although we are encouraged that the Administration is committed to enforcing the IMF conditions, our greatest concern is that neither the IMF nor the Treasury Department have the resouces to monitor the trade aspects of the agreement. We are also concerned that the administration and the IMF may not have the fortitude to enforce the agreement or pull additional funding when violations of the agreement occur. It appears our concerns are well founded. In a January 15, 1998 *Wall Street Journal* article, IMF president Michel Camdessus said the IMF "wouldn't object to special loans to the export sector ...." Obviously, IMF president Camdessus is unaware that Article 3.1 of the Subsidies Code specifically prohibits export subsidies.

In early February we shared these same views with members of the House Banking and Financial Services Committee. It is extremely important to our company and ot others in the U.S. Steel industry that the conditions of the IMF agreement be enforce. Therefore, we recommend the following:

In summary, we would ask the Committee and the Congress to do the following:

Make sure there is strict wnforcement of the IMF conditions and require quarterly reports from the Treasury Department and Department of Commerce that verify that no U.S. or IMF funds are being used to subsidize Korean industry.

If the IMG allows the Korean government to use IMF funds for export subsidies in direct violations of the Subsidies Code, the U.S. Congress should refuse to appropriate more funds to the IMF.

Congress should urge the administration to pursue WTO dispute settlement over past Subsidies Code violations concerning Hanbo Steel and to aggressively police and prosecute all Subsidies Code violations by our trading partners.

Mr. Chairman, IPSCO, is proud to have invested almost half a billion dollars in Iowa and has plans for additional investments expanding our steel capacity in the U.S. We did this based on a belief that the U.S. government is committed to fair trade so that low cost and high quality, nor government subsidies determine who gets the sale.

Statement of National Cattlemen's Beef Association

NCBA commends Chairman Crane and the Subcommittee for holding hearings to address the status of beef trade and projections for trade in light of the recent financial crisis in Asia, and for your continuing efforts to improve the export outlook for U.S. agricultural products. Expanded access to international markets is critical to the economic growth of U.S. agriculture. During 1996, beef exports accounted for approximately 8 percent of total U.S. production and more than 12 percent of beef's wholesale value.

Only 4 percent of the world's population lives within U.S. borders. Population demographics suggest that the U.S. generally, and agriculture specifically, need to aggressively prepare to seize opportunities to market products in countries with younger, fast-growing populations with increasingly disposable incomes. In spite of the current crisis, expansion of marketing opportunities continue to exist in many Asian countries. During 1996, beef and beef variety meat exports totaled $3.05 billion and generated a trade surplus of $1.27 billion. When cattle and by-product values are included—tallow and untanned hides (not leather and manufactured goods)—the value of beef-related exports totaled $4.8 billion during 1996 with a trade surplus of more than $1.8 billion.

Asian Crisis: During 1996, approximately 76 percent of all U.S. beef exports were sold into the Asian markets that are now in various stages of currency devaluation, economic reforms and recession. The price of U.S. beef has more than doubled to many Asian consumers due to currency devaluation. The Asian crisis will likely impact the already struggling economy in Japan. In the absence of expanded economic reforms and tax cuts, the continued strength of the U.S. dollar versus the yen and increasing unemployment increase the likelihood of recession in Japan. As the Asian economies slow and the devaluation of Asian currencies reduces the purchasing power of consumers in those countries, demand for U.S. agricultural products will falter. In the case of beef, this reduced demand will be further compounded by the fact that the Australian dollar and the Canadian dollar have also devaluated relative to the U.S. dollar, adding to the price advantage for beef from U.S. competitors.

The value of beef by-products (approximately $100/head of cattle) will also be affected by currency devaluation. During 1996, the total value of U.S. cattle hide exports totaled more than $1.125 billion. Korea purchased 40.2 percent of all 1996 U.S. cattle hide exports. Japan, Taiwan, China/Hong Kong, and Thailand combined to purchase another 39 percent. The cost of hides to processors throughout Asia has approximately doubled due to the devaluation of various currencies. In recent weeks, the decreased demand for hides and variety meats has contributed to a $30/head decline in value.

European Access: The World Trade Organization appellate panel on January 15, 1998 released a final ruling that the European Union (EU) ban on beef produced with growth promotants is a nontariff trade barrier that does not comply with WTO guidelines. The appeal was filed during September 1997 subsequent to a May 1997 WTO ruling that the EU ban was not based on sound science. Under WTO rules, the EU now must modify its regulations to comply with the ruling or the United States can retaliate. The EU has until mid-March 1998 to state whether or not it intends to comply with the ruling.

The EU has banned beef produced with growth promotants since 1989. When the ban was initiated, U.S. beef producers lost $100 million in beef trade to the EU annually. The value of that trade is now expected to be hundreds of millions of dollars. During the past decade, the EU has not been able to cite scientifically valid reasons for the ban. Scientific evidence clearly shows growth promotants used by the U.S. beef industry are safe. The U.S. filed its formal complaint with the WTO in January 1996, claiming the beef ban was a nontariff trade barrier. Argentina, Australia, and New Zealand joined the United States in the action by signing the complaint. Canada filed a separate case, and the final report addressed issues raised in both (U.S. and Canadian) cases.

The ruling is a milestone for U.S. beef producers, but additional work must be completed before access to the EU market becomes a reality. NCBA requests continued support from Congress to urge the U.S. Department of Agriculture and the Office of the U.S. Trade Representative to pre-empt European strategies and to bring this issue to closure.

In a separate, but closely related issue, on April 30, 1997 the United States and the EU agreed, in principal, on red meat inspection standards for trade, resolving some EU nontariff trade restrictions under its Third Country Directive. The U.S.

negotiated with the EU for more than three years to establish an inspection equivalence agreement for a number of agricultural sectors including meat, poultry, dairy, and pet food. The EU had maintained that, in a number of key areas, U.S. safety and inspection procedures were not equivalent to EU procedures. This position was not based on sound science but on political science, and therefore functioned as a nontariff trade barrier depriving the U.S. access to a large export market.

The veterinary equivalency agreement creates a framework to resolve other trade problems, and helped establish science-based inspection standards as the basis for trade agreements. The agreement was originally scheduled to be implemented during October 1997, but the EU did not meet the deadline. USDA Secretary Dan Glickman met with EU Agricultural Commissioner Franz Fischler during January 1998 to urge implementation of the agreement. Fischler has since said that he expects the agreement to be addressed during the February meeting of EU farm ministers. When the agreement is implemented, U.S. processors will be qualified to export to the EU based upon USDA's inspection and approval rather than subjected to arbitrary EU plant inspections.

NCBA urges that full access to the EU beef market be facilitated as soon as possible. The USTR must continue to devote adequate resources to assure resolutions to these issues that are favorable to the U.S. beef industry. Access to the European beef market is the ultimate objective and compensation is not an acceptable alternative. NCBA urges continued, coordinated pressure by Congress and the Administration to assure that the EU lives up to its responsibilities, as a full-fledged member of the WTO and the world trading community.

Requested Action: In addition to continued efforts to resolve access issues to existing markets the following action is needed:

Increase GSM Funding: Before the main impact of the Asian financial crisis became evident, Korea was the fourth largest export market for beef and beef variety meats. Through November 1997, exports of these products to Korea totaled nearly $287 million, an increase of more than 23.5 percent compared to the same time in 1996. NCBA is confident that Korea remains a long-term growth market for beef that is being disrupted by short-term currency fluctuations and financial circumstances.

Swift, decisive and bi-partisan action will be required to minimize effects of the Asian financial crisis on the U.S. beef industry and the broader U.S. agricultural economy. NCBA and other meat industry representatives met with USDA officials early in the crisis to request that GSM funds be made available for credit guarantees to Asian customers. The industry's original request was for $500 million in credit for exports of beef and pork to Korea. USDA subsequently allocated $100 million to beef, pork, poultry and horticultural products out of a total $1 billion GSM funding for Korea. Another $1 billion of GSM funding was made available to other Asian countries.

Nearly all of the $50 million GSM credit guarantees made available a few weeks ago for meat and certain horticultural products was immediately exhausted. It is NCBA's understanding that the Korean government requested most of that allocation for beef and other value-added meat products. NCBA urged USDA to make the additional $50 million of the original GSM allocation for meat and horticultural products immediately available for Korean customers and those funds were designated within one hour. *NCBA urges USDA to immediately allocate an additional $400 million for GSM credit guarantee resources targeted for export of beef and other value-added meat products.* Australia recently announced a credit guarantee program for Korea, and other competitors are sure to follow. Increasing the allocation for GSM credit guarantees now will build additional loyalty among Korean customers and increase future U.S. market share.

Approve IMF Funding Package: IMF-led financial assistance plans in Thailand, Indonesia and Korea are critical to the success of GSM credit guarantee packages. The impact of the Asian financial crisis on U.S. agricultural exports will depend on the success of IMF efforts to stabilize the Asian economies and bring about structural reforms and trade liberalization as called for by the IMF and World Bank reform packages. In the short term, the IMF-mandated trade and investment reforms will help stabilize the Asian banking system and help ensure the financial stability. In the long term, IMF-mandated structural reforms will help ensure economic growth and greater access to those markets through liberalized trade measures and policies.

The IMF plans to improve financial stability should help make it possible for importers from Asian countries to utilize the GSM export guarantee program. The IMF plan, combined with the GSM export credit guarantees, will enable the U.S. to keep servicing those markets thereby ensuring that the U.S. is seen as a reliable supplier of agricultural products, including beef. Without the IMF package, the GSM credit program would be of little use in helping resolve the Asian economic crisis.

NCBA urges the Administration to continue pressuring the Asian countries to improve access for U.S. products into markets in countries receiving IMF and GSM assistance. We have provided a list of access issues and tariff rates in each of the affected countries to USDA and Treasury officials and to Congressional agricultural committee staff. Some will likely question and criticize U.S. assistance to Asian businesses. It is important that Congressional leaders and U.S. business interests work to educate the public that this assistance—i.e., these long-term loans—is designed to alleviate short-term credit shortages. Experience suggests these type of loans have an excellent record of being repaid with interest. It is also important for the public to understand that, by including in these plans efforts to eliminate restrictive trade barriers for U.S. agricultural products, we not only increase demand for our goods, but we also can benefit consumers in the affected countries by providing a greater supply of food at a lower price.

Reinstate Fast Track Negotiation Authority: IMF stabilization packages and GSM credit guarantees will help reduce the impacts from the Asian financial crisis on U.S. agriculture. But even with these measures fully funded and in place, it is likely that U.S. agricultural exports to the Asian region during the next several years will decline. USDA is now projecting a 5 percent decrease in the value of total U.S. beef exports during 1998. Declines of 10 percent and 25 percent are projected for Japan and Korea, respectively. USDA now projects 1998 fed-cattle prices to increase only 3 percent above the 1997 average of $66.10/cwt.—down from earlier projections of a 10 percent price increase.

Realistically, it will take two to five years for the Asian economies to recover. In the case of Mexico, U.S. beef exports declined by approximately 60 percent during 1995, the first year after devaluation of the peso (approximately 50 percent decline in purchasing power). Beef exports to Mexico recovered part of that loss during 1996 and, during 1997, U.S. beef exports to Mexico were on target to reach record levels. Recovery in Asia will depend on the willingness and political ability of the various governments to implement economic reforms—closely associated with the willingness of international lenders to extend credit—and the extent to which competitive devaluation of international currencies continues.

An additional key to sustaining export market growth is gaining and maintaining access to emerging international markets in Europe and Latin America. Access to these markets will be increasingly critical to help off-set expected declines in historically important Asian export markets. The U.S. must continue to be aggressive in gaining access to new markets around the world. Fast Track authority is a critical element of that strategy.

The U.S. must also hold its trading partners to commitments agreed to in previous trade agreements. NCBA appreciates the initiatives that have been undertaken to gain access to international markets and to resolve lingering issues that restrict the ability of the U.S. beef industry to offer its products to international consumers. Without fast track authority, the U.S. will lose the initiative in gaining access to emerging markets and enforcing existing trade agreements.

The National Cattlemen's Beef Association is prepared to participate in the process of evaluating critical trade issues within the beef industry. NCBA looks forward to providing additional input as the U.S. addresses other trade issues, including accession of China to the WTO, resolving a host of access issues with the European Union and passing "Fast Track" legislation to provide authority to negotiate additional trade agreements. Thank you for the opportunity to present this information.

Shannon S.S. Herzfeld, Senior Vice President, International Affairs, Pharmaceutical Research and Manufacturers of America

On behalf of the Pharmaceutical Research and Manufacturers of America (PhRMA), I am submitting this written statement of our industry's position on the recent developments in trade with Asia, as requested by the subcommittee on Trade of the House Committee on Ways and Means.

PhRMA represents the country's major research-based pharmaceutical and biotechnology companies, which are leading the way in the search for new cures and treatments that will enable patients to lead longer, healthier, and more productive lives. PhRMA companies invest over $20 billion a year in the discovery and development of new medicines, and are the source of more than nine out of 10 prescription drugs used in the United States, as well as a great many of those used outside the U.S. The success of our companies in the $US 84 billion pharmaceutical market in the Asia-Pacific region is crucial to the industry's ability to invest in R&D now and in the future.

Pharmaceutical R&D is costly, lengthy, and risky. On average it takes more than $US 500 million and 12 to 15 years to discover, develop, and obtain approval of a new medicine. Moreover, only one in 5,000 compounds ever makes it to market. Because of these risks and considerable costs, it is very important for our industry, in the Asia-Pacific region, as in the rest of the world, to be able to rely on a foundation with three solid sides:

1. Strong intellectual property protection and enforcement;
2. Appropriate rewards for innovation and cost containment systems that recognize the value of patented medicines in health care.
3. Regulatory systems that offer rapid and reliable approvals.

In terms of our industry's interests in the Asia Pacific region, we believe improvement in all these areas is necessary to ensuring the continued success of the research-based pharmaceutical industry there. The problems we have encountered may be described as follows:

• *First, strong intellectual property protection and enforcement of such protection.* In many countries in which our companies operate, especially in the Asia-Pacific region, there have been notable improvements in the legal framework providing for adequate and effective intellectual property rights (IPR) protection, both for patented products and for trademarks. Yet, our industry often finds that, after the legal framework has been established, host governments often do not enforce the laws which are "on the books, or try to weaken the laws through other means. The issue of enforcement is terribly important for our industry, and we are very appreciative of the efforts made by the USTR, as well as other agencies of the U.S. Government, with the support of the U.S. Congress, to assist our industry in improving enforcement mechanisms both inside and outside of the Asia-Pacific region. Moreover, in many countries, there is no or little protection of proprietary data that are part of the product registration package usually filed with national regulatory authorities. In many countries in the region, the deficiencies in IPR appear in the provisions governing the use of compulsory licenses and the non-allowance of importation to satisfy the definition of the "working requirements for a patent. For our industry, the countries in the Asia-Pacific region in which little or no protection of product patent rights exist may be found in India, Pakistan and Sri Lanka. The countries in which we believe greater enforcement of IPR is needed include: China and Thailand. Data protection continues to be sorely lacking in Japan, Australia and most of the countries of Southeast Asia.

• *Second, appropriate rewards for innovation and cost-containment systems that recognize the value of patented medicines in health care.* This means that,, while our industry recognizes the need of governments throughout the Asia-Pacific region and the rest of the world to contain costs, we also believe that the products which we bring to health care systems can actually lower such costs and achieve significant improvements in both health outcomes and quality of life. We believe that, in certain countries in the Asia-Pacific region, policies now in place, or those that are planned for implementation in the near future, do not do enough to recognize the value of innovation and the contribution that our industry makes to finding cost-effective solutions to health care problems. These countries include: Japan, Taiwan, Australia, China and New Zealand.

• *Lastly, regulatory systems that offer rapid and reliable approvals for medicines that are safe, efficacious and of high quality.* In the Asia-Pacific region, as in other parts of the world, we are concerned about the often lengthy and unnecessary regulatory delays faced by our member companies, which serve to de-value the intellectual property protection that our industry has worked long and hard to achieve. This is especially true in Japan, where all our companies have experienced a significant "drug lag" in product approvals. In Japan today, a drug can take longer than 40 months to get through the regulatory process, compared with the U.S., where the Food and Drug Administration (FDA) has worked very hard to bring this average number down to 15.5. In many countries in the Asia-Pacific region, we also are seeing efforts by national governments to expedite the approval of generics. Our industry fully recognizes a role for generic products, as originators' products reach the end of their full and effective 20-year patent term. However, we are concerned that, in many countries, the standards for bioequivalency and bioavailability testing are inadequate to ensuring good quality generic products, even after the expiry of the originator's patent rights. Our industry views the regulatory process to be particularly troublesome in countries such as China, Japan, Korea and Thailand.

I have mentioned here that several countries have used "other means" to de-value the protection that are inherent in national patent laws, and that appear in the form of non-tariff trade barriers. I would like to draw attention in this regard to

Korea as a particular example of this problem. Korea's drug reimbursement policies within that country's health care system generally does not permit imported drugs to be listed on the Korean Medical Reimbursement Schedule.

If imported pharmaceuticals do make it on to this Schedule, doctors and hospitals are not permitted to earn any profit margin for those medicines. Moreover, hospitals, clinics and pharmacies which dispense imported drugs must comply with additional administrative procedures to receive reimbursement. These additional procedures discourage the use of imported drugs and limit the choices available to Koreans.

PhRMA is working very hard with U.S. Government officials in several agencies to try to change these and other discriminatory rules maintained by the Korea Government in relation to non-Korean medicines. If these shortcomings are not repaired by the end of the summer, our industry will have to consider more forceful action against the Korean Government.

Despite these impediments, PhRMA companies continue to lead the world in pharmaceutical innovation. This year, PhRMA companies are investing a record $20 billion in research and development—nearly 20 percent of sales. But to maximize benefits of biomedical innovation, our industry believes that the U.S. Government should pursue a trade strategy that builds on our national and industrial strengths, especially in the area of intellectual property.

The success that we enjoy now may not be the same in future years unless we are able to ensure that the IPR, in which our industry has invested nearly $100 billion in the past six years, are fully protected and enforced; that our industry's patented medicines are appropriately rewarded and that our industry's products are approved by regulatory authorities in unencumbered regulatory systems.

We understand that the Subcommittee on Trade of the House Ways and Means Committee has expressed an interest in two particular areas: (1) our industry's involvement in the Asia-Pacific Economic Cooperation forum, and APEC's potential role in improving the environment in the Asia-Pacific region for our industry and (2) the effect of the Asia financial crisis on our industry in that part of the world. I would like to address these two issues below.

APEC AND THE RESEARCH-BASED PHARMACEUTICAL INDUSTRY

PhRMA strongly supports the 18-member APEC forum and the principles of free trade on which it was founded. Specifically, we support APEC's efforts to develop more transparent trade and investment systems, streamline approval and registration processes, and eliminate tariffs. APEC also reinforces WTO commitments to ensuring the development of free and fair international trade practices.

At the 1997 November APEC Ministerial in Vancouver, the APEC leaders decided to initiate a program of early voluntary liberalization for 15 selected sectors of significant importance to the 18 member countries of APEC as well as to the region as a whole. The pharmaceutical industry, under the chemicals sector, was chosen as one of the areas for "sector liberalization." The inclusion of our industry in this initiative is a clear indication of the importance that APEC governments are attaching to the health care sector, as they consider future options for trade liberalization in the region.

For the pharmaceutical sector, the estimated market size of the APEC region in 1997 was $US 178.4 billion, including the United States, Chile and Mexico. Our industry's active participation in, and support for the APEC forum and the APEC Early Voluntary Liberalization Program will foster goodwill and strategic conditions in the region as well as have a significant positive effect upon the growth and efficiency of modern health care infrastructures in the Asia Pacific region.

It is well-known that doing business in the Asia Pacific region is fraught with difficulty and ambiguity, especially for the research-based pharmaceutical industry which is heavily regulated and dependent on high standards of intellectual property protection. It can be difficult to determine what tariffs and commercial regulations apply to particular transactions or what government agency is responsible for granting licenses. The result is costly legal entanglements, time wasted, and bad business decisions.

APEC seeks to ameliorate some of these problems through efforts to harmonize members regulatory and approval processes across a wide range of industry sectors. This will facilitate business transactions and reduce the time and money spent on launching a new product in the region. Utilizing the APEC forum, and particularly the Early Voluntary Liberalization Program, to generate greater market access and harmonization will also enhance regional economic recovery from the Asian financial crisis by providing opportunities for investment as well as trade. More specifically, liberalization initiative for the pharmaceutical sector supports:

1. A competition-based, market driven environment by promoting the free flow of goods across borders.

2. New economic growth opportunities by bringing increased investment to the region as well as higher standards of living and the development of more efficient health care infrastructures.

3. The creation of new jobs throughout the industry and an increased the demand for technical skills and training opportunities.

4. Strengthened intra-regional cooperation through greater private sector participation resulting in deregulation of market forces.

In addition to the Early Liberalization Initiative, PhRMA supports the APEC Business Advisory Committee's establishment of a Financial Subcommittee devoted to developing policy guidelines and assistance programs for those APEC members experiencing economic difficulties. Along with the advisory mechanisms of the APEC Finance Ministers, the Finance Subcommittee can guide APEC's developing countries as their economies expand to prevent a crisis situation from developing in the future.

IMPACT OF THE ASIA FINANCIAL CRISIS ON THE RESEARCH-BASED PHARMACEUTICAL INDUSTRY

PhRMA believes that, as countries in the region struggle to manage fiscal expenditures and regain some of the economic instability lost—and being lost—in the 1997–1998 Asian financial crisis, it is important for those countries' leaders to understand the importance in continuing to provide access for their citizens to quality health care and quality medicines. The effects of the Asian financial crisis on our industry, however, seem to indicate that some of the region's government bureaucrats see the crisis as an opportunity to protect and favor their own national industries at the expense of the international pharmaceutical sector, and, more importantly, at the expenses of citizens in their own countries.

Although the Asia financial crisis has adversely affected all sectors, the pharmaceutical sector has particular concerns. Currency devaluations in Korea,

Thailand and Indonesia are severely affecting the ability of U.S. companies to purchase their raw materials which must be paid in U.S. dollars.

Unlike most other industries, pharmaceutical companies are less able to compensate for the devaluations by adjusting prices since the industry is heavily regulated in the prices which they can ask for their medicines. This especially is true in cases where medicines are reimbursed by national health authorities, as in the case of Korea, but also is true in Thailand and Indonesia, where companies must seek carefully guarded permission to adjust prices.

Our industry's situation in the Korean pharmaceutical sector provides an unusually poignant example of this problem. During the past six months, the Korean Won has devalued by 40 per cent. However, the pharmaceutical industry has been able to achieve only a 10 per cent price increase, while other industry sectors have been able to achieve increases of up to 60 per cent to compensate for the severe devaluation. Moreover, the industry has been battling severe market access barriers as well as discrimination in pharmaceutical trade throughout the region.

As a condition to receiving lines of credit from the International Monetary Fund (IMF), the Governments of Korea, Thailand and Indonesia agreed to implement fiscal austerity measures to reduce fiscal expenditures as well as streamline and deregulate the financial sector, and increase the openness of the domestic market to imports. Unfortunately, as the Finance Ministries in Korea, Thailand and Indonesia are agreeing to these conditions and accepting lines of credit, the government regulatory agencies are implementing "Buy National" policies to cut social welfare expenditures and protect domestic industries, especially in the health care sector.

Government sponsored "Buy National" policies in Korea and Thailand target not only imported products, but foreign manufactured products produced from operations in country. The basis of the policies is to substitute brand-name imported pharmaceuticals with cheaper domestic generics and to delist foreign medicines from the reimbursement schedule.

In Korea, this development signifies a definite move to discriminate even further against imported products and therefore poses a problem in terms of the Korean Government obligations to equal treatment rules of the WTO. The delisting of foreign medicines from the reimbursement schedule is an indisputable market access barrier to trade. Furthermore, the "Buy National" activities are is direct contravention to the Korean Government's commitments toward market opening, trade liberalization and deregulation as agreed to in the conditionality arrangement with the IMF. The severity of this problem is intensified for our industry in Korea, as it appears with the existing barriers to entry that our industry faces, and which I discussed earlier in this statement.

The Royal Thai Government also recently invoked similar "Buy Thai" regulations which have had a very serious and detrimental impact on our industry in Thailand. Although Thailand is not a signatory to the WTO Government Procurement Code, the "Buy Thai" policies clearly violate WTO Article III (i.e., National Treatment) provisions and undermine the principles on which the GATT and WTO were founded.

While the U.S. pharmaceutical industry supports U.S. Government participation in the IMF recovery programs for Asia economies, it is imperative that the appropriate trade liberalization measures be enforced to guarantee market access and, more simply, national treatment for the U.S. research-based pharmaceutical industry in Asia. The IMF economic recovery programs traditionally have included a vigorous combination of macroeconomic policies, financial sector restructuring, corporate sector reforms, capitol account liberalization, labor market reform, trade liberalization and information provision measures.

Unfortunately, IMF-imposed trade liberalization measures have targeted only trade-related subsidies and import certification procedures for Korea, and were never even a consideration for Thailand. As a result, it appears that those U.S. industries which face onerous non-tariff barriers to market access in these countries will not receive any real or meaningful progress in terms of opening markets to foreign competition in these countries.

The resistance of some Asian countries to open their economies is inherent in their traditional business practices The U.S. research-based pharmaceutical industry has experienced the effects of this resistance to reform first hand since the financial crisis hit Korea in 1997. We believe that the success of the IMF reform programs will depend not so much on the extent of full financial support of the international community, but on the determination and commitment of the Asian nations to restructuring and opening their economies, and on the level of "peer pressure" that the international economy can generate for their compliance.

We have asked that the U.S. Treasury Department be vigilant in its pursuit of market opening measures in Korea, Thailand and Indonesia; and seek to eliminate any special provisions which protect "essential" industries at home (i.e., health care, etc.) from the conditionality arrangements. Moreover, we believe that the IMF and the international community should demand that all "Buy National" policies be rescinded immediately, and that the appropriate market opening measures to enhance competition and efficiency are implemented within a specific time-frame.

CONCLUSION

I appreciate this opportunity to provide PhRMA's views and objectives on U.S. trade policy for the Asia Pacific region, which we hope to achieve by working with the members of the Subcommittee on Trade of the House Ways and Means Committee, as well as other agencies of the U.S. Government and officials in the Administration. PhRMA believes that the U.S. Government's participation in and support of the IMF and Asia Pacific regional trading arrangements, such as APEC, will be crucial to the success of the U.S. research-based pharmaceutical industry in the region. Whatever support is afforded to the IMF or for APEC, we hope that your Committee will support our industry's efforts to ensure that existing barriers to trade in innovative medicines are removed before such support is finalized, and that measures are put in place to ensure that no new barriers to trade are erected.

Statement of Semiconductor Equipment and Materials International

Semiconductor Equipment and Materials International (SEMI) represents over 2100 companies specializing in the manufacture of capital equipment and materials for the production of semiconductors. Our members include approximately 1263 U.S. companies located in 41 states, contributing over 70,000 jobs to the American economy. We appreciate the opportunity to provide comments to the Committee on the current financial crisis in Asia, and the impact of continuing instability in that region on our industry.

In the United States, our industry is composed mainly of small, privately held firms which are technology intensive, specializing in the production of a particular tool or material used in the semiconductor manufacturing process. Over 80 percent of our members are companies with annual sales of less than $50 million. Although small, these firms develop the enabling technology for the nation's semiconductor sector, providing the equipment and materials necessary to perform the complex fabrication steps that turn raw silicon into an integrated circuit.

As the powerful technology of semiconductors become more pervasive in consumer electronics, semiconductor device makers are relentlessly pressing for more powerful chips. The semiconductor equipment and materials industry is a strategic partner in achieving that goal. Once an industry that simply created tools according to specifications from our customers, today our companies' research and development generates many of the strategic process advances which increase chip information density, reliability and yields.

During the 1980s the U.S. semiconductor equipment and materials industry (SEM) faced tremendous pressure from abroad, and we responded to that pressure by expanding the global reach of our industry and by focusing our companies on developing highly competitive tools and materials. That strategy succeeded—today, SEM companies in the U.S. account for 55 percent of the world's sales of semiconductor equipment and export on average 40 percent of their sales annually, much of which flows into the dynamic Asia Pacific region. Asia (excluding Japan) currently accounts for nearly 30 percent of semiconductor equipment consumption. (See attached charts.)

The recovery of U.S. competitiveness, however, would not have been possible without access to sales in the important export markets of the Asia Pacific. Without sales to worldwide markets, our industry would have been unable to support the high R&D costs that are the crucial investment in keeping pace with rapid technology development. That paradigm continues to govern the current market environment. No leading semiconductor equipment or materials company can survive on the U.S. market alone.

SEMI firmly believes that the U.S. commitment to free trade and open markets has played a large role in helping our industry thrive in new markets such as those emerging in the Asia Pacific region. We have strongly supported the government's insistence on market oriented reforms in emerging economies as a part of global trade negotiations, and the drive to reduce tariff and non-tariff barriers to trade.

Now, with financial instability threatening many of the Asian economies, we believe that the U.S. government, along with our allies in Europe and Japan, should work with the International Monetary Fund to quickly stabilize and revitalize the Asian economies. To allow the crisis to linger, and perhaps spread as we fear it will without strong American leadership, is to risk not only the inroads we have made into those markets, but the American jobs that depend on continued exports to the Asia Pacific region.

To that end, we urge Congress to approve both the $3.5 billion contribution to the New Arrangements to Borrow and the $14.5 billion quota increase. Doing so ensures that funding will be available to respond if the crisis does spread. It also provides breathing room for the governments of nations like Korea to begin to implement the market oriented reforms called for under the IMF loan arrangements that are crucial to preventing future crises.

ASIAN MARKETS CRUCIAL TO OUR INDUSTRY:

The markets of the Asia Pacific region, particularly Korea, Taiwan and China, are just beginning to become significant forces within the semiconductor device making community. Despite the current turmoil, we expect the region to be a dynamic source of growth for our industry for many years. However, with approximately 30 percent of our worldwide sales dependent on Asia, and particularly Korea, any slowdown in those economies can not help but reverberate here. Already U.S. SEM companies are experiencing downturns in orders from many of our Asian customers, which, if continued, could affect our ability to continue to be growth drivers for the U.S. economy as a whole.

To remain competitive in the semiconductor equipment and materials industry—indeed to survive in the environment of ever changing technology—our companies must invest heavily in research and development for the next generation of tools. To do so requires revenues raised from world wide semiconductor equipment markets. Similarly, our customers in the device industry must be able to invest in the advanced capital equipment necessary to produce the next generation of chips. Failure to do so on their part could also engender a significant loss in competitiveness

As many of the Asian nations were seeking to enter the semiconductor market, capital investment decisions were not always made on the basis of market forces, leading to overcapacity in certain industry sectors such as the DRAM market. Clearly, the overcapacity problem must be addressed in order to stabilize semiconductor markets. However, in order to stay abreast of technology, chipmakers in Asia must invest in the next generation of equipment, regardless of continued overcapacity. In turn, their investment is vital to our industry's long-term health and stability.

SEMI believes that the IMF programs will not only address the structural problems facing the Asian economies—particularly government directed investment decisions unrelated to market forces—but also will do so in a manner that will allow critical capital investment and will further global competition over the long-term.

We are pleased that China has to date avoided financial crisis, and is taking steps to address structural weaknesses in its banking system. We believe that rapid stabilization of the other economies in the area will lessen the likelihood that the growing China market will also descend into turmoil.

Key facts on the importance of the Asia Pacific economies to our industry include:

Korea:

- Korea captured nearly $10 billion in DRAM sales in 1996 (30% of the world total), and has become a leader in state-of-the art 64 Mbit DRAMs.
- Korea's market for semiconductor equipment has grown from $1.3 billion (US Dollars) in 1993 to $3.5 billion in 1997. (source: Korean Semiconductor Industry Association, KSIA)
- Korea's market for semiconductor materials has more than doubled in the same time period, moving from $1 billion in 1993 to $2.8 billion in 1997 (KSIA data).
- According to KSIA, semiconductor equipment purchases for 1997 were down 13%. Because of the financial crisis, and continued overcapacity in the DRAM market, SEMI is predicting that 1998 will see similar, if not greater, decreases.

Japan:

- The U.S. has captured approximately 17% of the equipment market; nearly 33% if joint ventures are included.
- Japan produces about 35% of worldwide semiconductor equipment.
- Japan in 1997 consumed nearly 25% of the $27.6 billion semiconductor equipment market.
- With a stagnating economy and weak banking system, continued instability in other Asia nations could spread to Japan, which would in turn severely impact U.S. equipment and materials companies.

China:

- While China is still in the early stages of building a domestic microelectronics industry, recent statistics show that China's electronics output is soaring, and in combination with Hong Kong, it is predicted to rank as the third largest electronic producer in the world by 2005, after the U.S. and Japan.
- Currently China produces only about 20 percent of the semiconductors it consumes, but SEMI estimates that by the year 2000, China's IC demand will total 4 billion units, with approximately one half of these units produced domestically.
- Dataquest has estimated that the Chinese market for semiconductors was $7 billion in 1996 and will increase to $8.3 billion in 1997 and $17 billion by the year 2000.
- The demand for semiconductor equipment generated by China's microelectronics industry is estimated by SEMI to be $700 million in 1997 and over $2 billion in the year 2000.

Taiwan:

- Of the total $27.6 billion in semiconductor equipment sales in 1997, $3.7 billion went to the Taiwanese market, which positions Taiwan at approximately 13.4% of the total worldwide equipment market.
- Taiwan accounts for only about 5% of the $21 billion in estimated materials sales, but because of aggressive investment that figure is expected to increase as semiconductor production increases.
- Taiwan's integrated circuit manufacturers have announced plans for $40 billion in investment between 1997 and 2007 for future facilities.
- Because of long-standing relationships between U.S. and Taiwanese firms, U.S. equipment suppliers should win a substantial amount of the business for supplying the tool sets for those new facilities.

Next Steps: Fulfilling our IMF Obligations

SEMI believes that the Asian markets are an integral part of the global economy, and that, if open markets are to be achieved, it is appropriate for the IMF, the U.S. Government, and other world economic leaders to help stabilize the overall economic health of the region. In today's global economy, we cannot fail to do so if our trade with those nations is to continue to be a positive force for growth here at home.

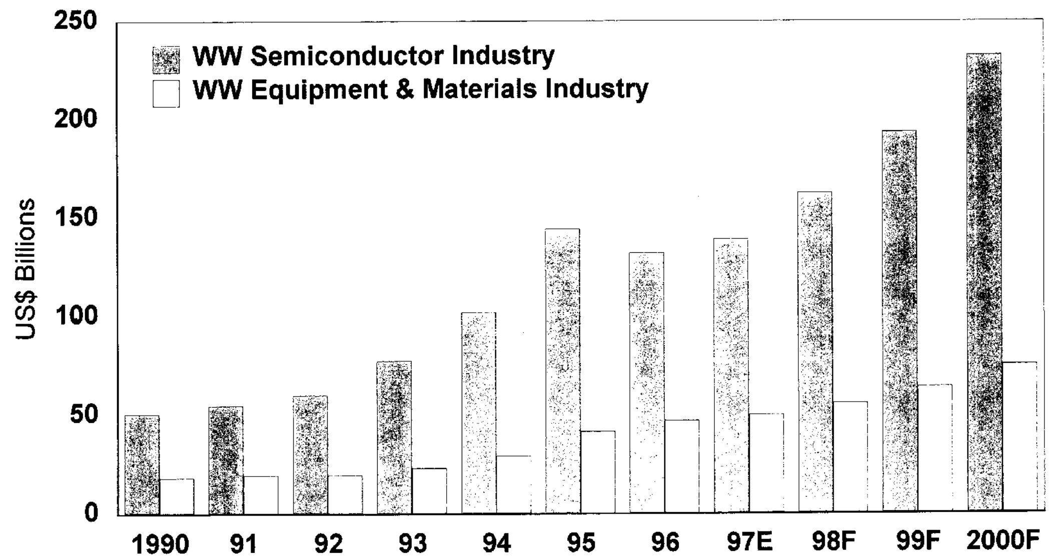
In moving forward, it is important to recognize that the IMF funding request is not a "bailout" for Asia. The assistance package is in the form of loans that must be repaid and which require structural changes in each nation's financial system that will help prevent the current economic turmoil from recurring. Loans through the IMF are not an expense to the U.S. taxpayer, but an investment in global economic security that has a payoff in American economic stability, and in stability for our export markets. The IMF has played a key role for the past 50 years in maintaining global financial stability, preventing such practices as competitive currency devaluations. Fulfilling our obligations to the IMF will allow continued U.S. leadership in shaping the role of that institution for the next 50 years.

Our customers, and in some cases our competitors, reside in the Asian nations now in crisis. But we believe that such competition makes U.S. industry stronger, and that programs designed to set these economies on a more stable, market-oriented course for growth will, in the long run, provide continued trade opportunities for U.S. semiconductor equipment and materials companies.

IMF funding provides breathing room for the difficult transitions that lie ahead for the recipient economies. Equally valuable, U.S. commitment to new and continued funding provides a signal that our government is fully committed to playing a leadership role in international economic affairs.

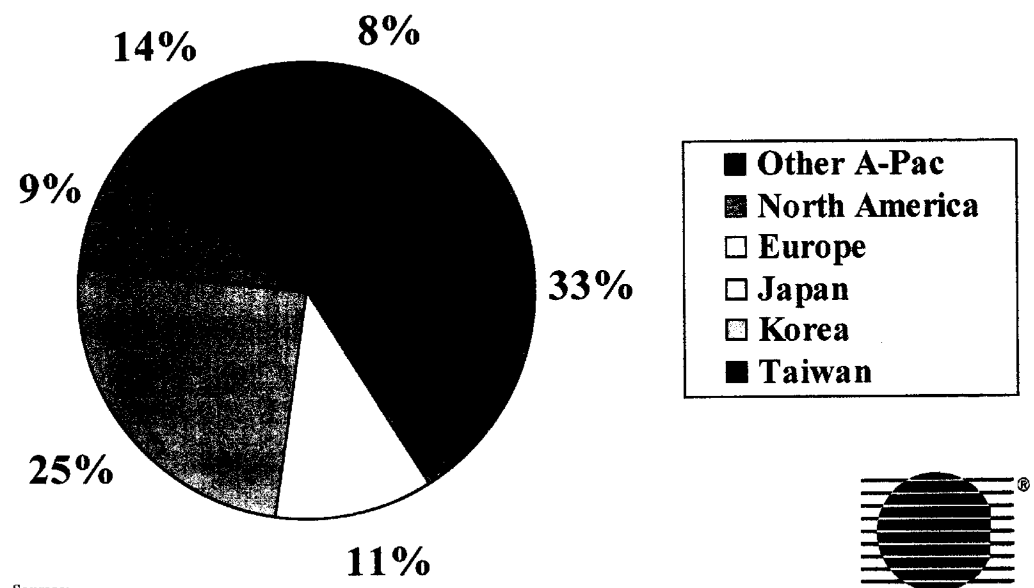
SEMI would like to thank the Committee for the opportunity to provide written testimony on this topic. We would be please to answer any questions that arise from our statement, and to provide any additional information necessary.

Semiconductors Tracked by Semiconductor Equipment and Materials



Sources: Semiconductor Industry Actuals & Forecast - SIA (WSTS) & SIA Consensus Forecast
Semiconductor Equipment Industry Actuals & Forecast SEMI/SEAJ & Consensus Forecast

Semiconductor Equipment Market Regions
Asia Pacific



Sources:
Semiconductor Equipment Industry Actuals & Forecast SEMI/SEAJ & Consensus Forecast
Korea Data - KSIA & SEMI/SEAJ

Presentation 11

Top Asian Chip Makers

(in millions of dollars)

Company	Chip Sales			Capital Expenditures		
	1996	1997E	1998F	1996	1997E	1998F
LG Semicon	2392	2094	2906	1543	1100	1000
Hyundai	2379	2199	2976	1414	1350	1100
Samsung	6566	6205	8107	1743	1350	1333
TSMC	1435	1478	1818	797	982	1348

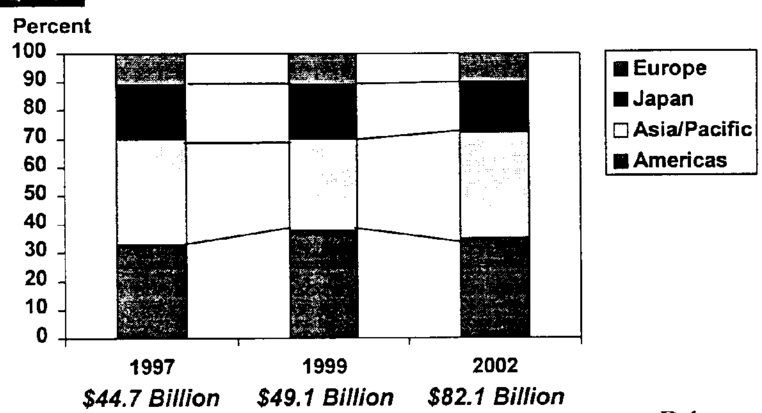
Top 10 Capital Spenders in 1997

1996 Rank	1997 Rank		Projected 1997 Spending ($M)	Percentage Change
1	1	Intel	4,500	50
2	2	LG Semicon	2,282	-17
3	3	Samsung	1,903	-15
11	4	Motorola	1,800	27
13	5	Siemens AG	1,730	33
4	6	Hyundai	1,726	-18
6	7	NEC	1,583	-12
7	8	Fujitsu	1,525	-10
9	9	Toshiba	1,416	-9
10	10	IBM Microelectronics	1,400	-10

Source: Dataquest

Dataquest

Capital Spending Trend Near Term Favors U.S. over Asia/Pacific



Source: Dataquest

Dataquest

Statement of George Scalise, President, Semiconductor Industry Association

I appreciate the opportunity to appear before the Subcommittee on Trade of the Committee on Ways and Means to present the views of the Semiconductor Industry Association (SIA) on issues affecting U.S.-Asia trade. A primary interest of the SIA is China's accession to the WTO, on which I testified before this Subcommittee last year. But I understand that the subcommittee's chief interest today is the Asian financial crisis and its effects on the American economy—so I will focus my remarks today on this topic.

THE U.S. SEMICONDUCTOR INDUSTRY

Semiconductors are an increasingly pervasive aspect of everyday life, enabling the creation of the information superhighway and the functioning of everything from automobiles to modern defense systems.

U.S. semiconductor makers employ about 260,000 people nationwide, and the presence of the industry is widespread—35 states have direct semiconductor industry employment. Semiconductor products are the enabling technology behind the U.S. electronics industry, which provides employment for 4.2 million Americans, in all 50 states.

U.S. semiconductor producers are highly committed to maintaining their lead in both semiconductor manufacturing and technology. The U.S. semiconductor industry devotes on average 20 percent of its revenues to capital spending and another 11 percent to research and development—among the highest of any U.S. industry.

While investing heavily in the industry's future competitiveness and technological capabilities, SIA members also have actively sought open markets around the world. Because the semiconductor industry is so global in nature—roughly half of the U.S. industry's revenues are derived from overseas sales—the SIA has been dedicated since its inception to promoting free trade and opening world markets. Since the early 1980s, SIA has worked for a global tariff-free environment. The U.S.-Japan semiconductor negotiations in Vancouver in 1996 led directly to the conclusion of the Information Technology Agreement last year.

Historically, Japan has been the most important export market for the U.S. semiconductor industry. But the rest of Asia is becoming increasingly vital to the health of U.S. semiconductor producers. The Asia-Pacific region is home to some of the most rapidly growing markets for semiconductors. The continued growth—and openness—of these key markets is important to the future success of the U.S. semiconductor industry.

IMF FINANCIAL ASSISTANCE PACKAGES

The growth of the world economy and economic stability must be the number one economic priority for both the U.S. government and American business. SIA therefore supports the IMF-led financial assistance programs announced in the last several months for a number of troubled Asian economies. Stable financial markets promote world economic growth. IMF financial assistance can play an essential role in reestablishing stability in financial markets. In the long term however, this assistance can only succeed if tied to serious commitments to market-oriented reforms in the recipient countries. Therefore certain conditions must be placed on any such financial assistance.

This crisis is most often addressed in terms of macroeconomic factors, but there are distinct microeconomic causes and microeconomic effects as well. To be specific, while this had been a decade of explosive growth for Asia, at the core of this dramatic growth were deep-seated problems: inadequate governmental supervision of Asia's financial institutions; unsound loans; speculative real estate and equity booms; and most importantly, close links between governments, banks and corporations, and manipulation of credit markets to benefit favored industries. Indeed, as many have observed, the government practices underlying the Asian financial crisis are in some circumstances the very same practices that have given rise to distorted patterns of investment, production and trade in Asia.

South Korea's current economic crisis, for example, stems in part from the Korean government's practice of directing lending on non-commercial terms to promote the rapid expansion of favored export-oriented sectors.[1] When world markets could not absorb the resulting excess production capacity, the prices for Korea's major export products declined sharply, thereby threatening Korea's ability to repay foreign currency loans used to underwrite the aggressive capacity expansion.

Backed by government-directed borrowing, and targeting 90 percent of its production for the export market, the Korean semiconductor industry rose in a few years from an insignificant producer to one of the world's largest, capturing nearly 40 percent of the worldwide market for memory chips. The three Korean semiconductor producers achieved this by aggressive, highly-leveraged investment in new production capacity at a rate far exceeding that of any other country, and at a rate that is economically questionable. Alan Greenspan, Chairman of the Federal Reserve, recognized the role played by the Korean semiconductor industry in precipitating this crisis in his testimony before the Joint Economic Committee on October 29, 1997, noting that "the glut of semiconductors in 1996 suppressed export growth, exerting further pressure on highly leveraged business."

Whatever the specific role of individual industries, perhaps the most positive development coming out of the current Asian financial crisis is that an opportunity has been created for systemic reform. But the major effort will be long-term. To be effective in re-establishing the confidence of world markets, basic market-oriented reforms—some of which are contained in the agreement between the IMF and the Government of Korea—must be fully *implemented, monitored* and *enforced*.

THE GOAL OF THE IMF SUPPORT PACKAGES MUST BE TO ALLOW MARKETS TO WORK

The goal of the IMF reforms—of letting market forces operate freely— must be realized in order to deal effectively with the Asian crisis.

Investment, production and exports must take place on the basis of market forces—not as a result of subsidies or other commercially unjustified support. If companies in troubled Asian markets cannot sustain themselves based on market principles, they should, for example, be allowed to fail or be sold to other firms—just as would happen in the United States or any other open-market economy. This must be a fundamental principle underlying any long-term solution.

This principle mandates that any new financing for industries in these troubled economies be commercially justifiable and not government-directed. Any new loans must: (1) be fully market-based; (2) not fall below a commercially-justifiable benchmark rate based on the credit-worthiness of each borrower; and (3) not be government directed, government supported or government guaranteed. In particular, none of the funds should result in commercially unjustifiable support of the Korean semiconductor industry in any form.

In their current financial condition, many Asian manufacturers may not be creditworthy. For example, the debt-to-equity ratio of the Korean semiconductor industry reportedly averages over 350 percent, nearly ten times the average ratio for U.S. semiconductor producers. This debt financed a huge capital expansion—in 1996 alone, Korean firms invested $7.3 billion in new plants and equipment, an amount which was almost 60 percent of their $12.4 billion in sales.

It is no longer fashionable—and it has never been accurate—to look upon Asian industry as entirely free to operate on a different economic model than their market-driven competitors. Ultimately, absent government intervention, market disciplines apply equally to producers regardless of nationality.

Without an end to government-directed lending, the current debt problems facing these countries will not be solved. Instead, market forces must be permitted to determine financial transactions. Government-directed lending to entities that could not receive commercial financing must not be allowed. Allocation of credit to favored export industries can only result in investment and additional capacity totally unjustified by domestic or international market conditions, which can lead to dumping and other injurious trade effects.

Allowing IMF and other assistance funds to subsidize debt-ridden Asian manufacturers would not only perpetuate the underlying economic problems, but would do so at the direct expense of U.S. companies. These Asian countries must commit to end the use of subsidized support or tax privileges to bail out individual corporations.

It is important to note here that the IMF assistance package for Korea does include several conditions to address this problem. For example, the package includes commitments by the Korean government that the commercial orientation of bank

[1] For much of the information on the Korean economy and the Korean semiconductor industry, SIA has relied extensively on the research provided by Micron Technology, Incorporated, a member of SIA.

lending will be fully respected, and the government will not intervene in bank management and lending decisions. Importantly, this package also states that remaining "directed lending" will be eliminated immediately, and that no government subsidized support or tax privileges will be provided to bail out individual corporations.

One of the essential elements of what is needed now is adequate attention and sufficient resources directed to enforcing these IMF-mandated conditions. Enforcement, in turn, requires effective and vigorous monitoring. This requires increased transparency in the Korean financial system, as well as careful oversight by both IMF and U.S. government officials.

ECONOMIC RECOVERY IN ASIA CANNOT COME THROUGH EXPORTS ALONE

The troubled Asian economies should not seek economic recovery solely through increased exports. Subsidization of exports or government-directed export targets will only further distort Asian economies, harm market-based competitors—and will not result in an effective and long-term solution. Government-directed lending to selected firms has already produced excess capacity in the affected sectors, and continued lending can only exacerbate this oversupply. This, in turn could lead to depressed world prices and operating losses for producers both in and out of Asia. The semiconductor industry has been and clearly remains a prime candidate for lending that is not commercially justified.

Unfortunately, there are some indications that many of these countries continue to look to export-led growth to solve their current economic problems. In Korea, for example—despite operating losses and massive debt—Korean semiconductor producers have announced plans to significantly increase export levels in 1998. The Government of Korea has in fact explicitly encouraged export plans. The director of the export division of the Korean Ministry of Trade, Industry and Energy recently suggested: "to overcome this crisis, export promotion is the most important policy of the country."

In addition, the Wall Street Journal reported on February 17, 1998, that the IMF may permit South Korean banks to use IMF loans to back South Korean exports. This must not be allowed to happen. Korean exporters already benefit from a decline of nearly 50 percent in the value of their currency, which makes their exports that much cheaper in dollar terms. They should not be permitted to use IMF funds to further expand exports, particularly when this gives them an unfair competitive advantage over competitors in other countries. The WTO Subsidies Agreement, in fact, explicitly prohibits export subsidies, and the IMF should ensure that Korea lives up to its WTO commitments.

The U.S. Government and the IMF must take steps to discourage such plans, and to promote domestic growth in these countries. There is a limit to how much in the way of increased exports other markets can absorb. Increasing below-cost exports from Asian companies will only worsen the crisis. Asian countries that are already suffering losses will see further distortion of their economies, while market-based competitors will face a flood of underpriced goods.

INTERNATIONAL PARTICIPATION IS ESSENTIAL

An effective and long-term solution requires international participation. The IMF-led bailout efforts will succeed only if other countries join the United States in contributing to the solution—both through provision of funds and by accepting a share of the increased level of exports from the troubled Asian economies. The United States cannot—and must not—undertake this role alone. Other major industrial countries must take steps to promote growth in their domestic economies—which can in turn be catalysts for global growth. In particular, within Asia, the Administration should continue to encourage Japan and China to make the structural reforms necessary to strengthen this recovery.

The participation of Japan—with the largest economy in Asia and the second largest in the world—is essential. Japan has far more at risk in the current crisis than the United States, and has the most to gain from an Asian recovery. A strong Japanese economy and open Japanese markets are critical to regional recovery.

The U.S. Government should insist that Japan open its market to exports from these Asian countries generally, as well as from the United States—both to share more equitably the burden of responding to the Asian financial crisis and to reduce trade distortions that damage the U.S. and other economies. In this respect—to give credit where credit is due—very substantial progress has been made under the U.S.-Japan Semiconductor Agreements to open the Japanese market to foreign semiconductors.

Emerging markets also have a role to play. Short-term stabilization of the current crisis requires that the United States stop the so-called "contagion effect"—a spreading of this crisis from one region to another. China has played a constructive role in this regard by committing to avoid devaluation of its currency. The Administration should continue to work closely with these and other governments to promote structural, financial, and macroeconomic policies that are vital to stability and world economic growth.

INCREASED TRANSPARENCY IS CRITICAL TO SUCCESSFUL REFORM

As part of overall reform efforts, beneficiary countries must promptly improve the transparency and accuracy of corporate balance sheets, including profit and loss accounts—by the adoption and implementation of internationally-recognized accounting standards. This is a condition which is in the IMF agreement with Korea. However, Korea reportedly adopted in 1996 an accounting standard that permitted companies to hide foreign exchange losses by taking them off their income statements, thus distorting the firms' true financial positions. More recently, it has been reported that Korea adopted a standard that permits foreign exchange losses to be spread over some future period, creating further distortions. These accounting standards should be modified to comply with internationally-recognized standards to permit markets to monitor effectively the financial health of these firms.

More generally, such internationally-recognized accounting standards must be adopted and implemented immediately in all respects by the Korean government. Quarterly financial result reports should be required, beginning with the first quarter of 1998, and continuing forward, and such reports must be monitored by the U.S. Government and international financial officials.

CONCLUSION

The Asian financial crisis confers on the international community awesome responsibilities. As a global industry dependent on exports, the U.S. semiconductor industry fully supports measures to end the financial crisis in Asia, assuming reasonable conditions are imposed. International rescue plans, however, must seek effective and long-term solutions. There must be market-oriented reforms, and there must be monitoring and enforcement mechanisms to ensure these reforms are carried out. U.S. and international assistance cannot permit the unsound practices that have harmed both Asian countries and U.S. industries to be perpetuated.

For the Congress, this raises a number of questions which I urge you to consider:

- Does the IMF have an effective plan to monitor developments in the affected Asian countries so as to ensure commitments made to the IMF are being carried out?
- Does the U.S. Government have in place effective mechanisms to itself monitor the IMF reform programs and condition its own assistance on effective implementation of these reforms?
- Are all key agencies, including trade agencies—USTR and the Department of Commerce—engaged in the oversight of the IMF reform programs? Is a special interagency enforcement effort needed?
- Have adequate resources been provided in the Executive Branch to accomplish the necessary monitoring and enforcement to make the IMF reform program a success?

The answers to these questions will determine whether U.S. industry—including the U.S. semiconductor industry—is in the long run harmed or permitted to compete on a level playing field as a result of the IMF bailouts. I urge you to give these questions your serious consideration as you consider legislation related to this important issue.

Thank you for this opportunity to testify.