



March 24, 2010

The Honorable Sander M. Levin  
Chairman  
Committee on Ways and Means  
United States House of Representatives  
1104 Longworth House Office Building  
Washington, DC 20515

RE: Hearing: China's Exchange Rate Policy

Dear Chairman Levin:

On behalf of its members in the U.S. retail industry, the National Retail Federation (NRF) welcomes the opportunity to submit these comments to the Ways and Means Committee regarding China's exchange rate policy.

The **National Retail Federation** is the world's largest retail trade association, with membership that comprises all retail formats and channels of distribution including department, specialty, discount, catalog, Internet, independent stores, chain restaurants, drug stores and grocery stores as well as the industry's key trading partners of retail goods and services. NRF represents an industry with nearly 1.6 million U.S. retail establishments, 24 million employees - about one in five American workers - and 2009 sales of more than \$4.1 trillion. As the industry umbrella group, NRF also represents over 100 state, national and international retail associations.

### **Retail Industry Profile**

Retailing represents one of the largest industries in the United States in terms of the number of companies, employment, and contribution to gross domestic product. According to the most recent annual (2009) statistics:

- The U.S. retail industry comprises more than 1.1 million retail companies;
- Among American retail companies, the vast majority (98.5 percent) are small businesses located in every Congressional district in the country;
- The U.S. retail industry had annual sales more than \$4.1 trillion;

- Of the more than two-thirds of U.S. GDP generated from consumer spending, over 41 percent of that spending (*i.e.*, nearly 30 percent of U.S. GDP) occurs in retail establishments;
- With 24 million employees – nearly one in five American workers – the retail industry provides more jobs than any other U.S. industry;
- Retail employees averaged \$16.77 per hour in total compensation (wages, salaries, and benefits).<sup>1</sup>

Like any other business, retailers face the daily challenge of creating value for their customers and shareholders, in an industry marked by cutthroat competition and an average profit margin of 2-3 percent. Currently, retailers are slowly climbing their way out of the worst economic environment for our industry in over 40 years. During the past 18 months, retailers suffered a huge number of bankruptcies, store closures, and over one fifth of all the job losses in the United States.

Retailing is also an extremely trade reliant industry that is directly impacted by the direction and operation of U.S. trade policy. Like other U.S. industries, including manufacturing and agriculture, every retailer, from the largest national chains to the smallest neighborhood shop, depends on a global supply chain to procure the products that its customers – the American consumer - need and want.

The commercial activity generated by global sourcing of consumer goods by American retailers supports good-paying, skilled blue and white collar jobs, many of them union jobs. These millions of American workers are employed not only in the retail industry, but also in many ancillary industries that support retail operations and supply chains – *e.g.*, manufacturing, farming, ports, rail, trucking, warehousing, air delivery, and logistics.<sup>2</sup>

As an industry engaged in importing, we would point out that, contrary to popular opinion, evidence shows that imports as a whole support millions of U.S. jobs, and help, not only retailers, but all U.S. companies involved in international commerce to enhance their productivity, competitiveness, and ability to expand employment. Research

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<sup>1</sup> Source, *Retail Industry Indicators*, Prepared for the NRF Foundation by The Trade Partnership.

<sup>2</sup> See, *Imports and America: The Rest of the Story*, prepared by The Trade Partnership for the National Retail Institute and the Council of the Americas, August 1998, and *Impact of Imports from China on U.S. Employment*, prepared by Trade Partnership Worldwide, LLC for the National Retail Federation, November 2005.

demonstrates that imports support more than 10 million American jobs, and that imports from China alone support nearly 1 million net jobs in the United States.<sup>3</sup>

## **U.S.-China Trade Relations**

Much of the national economic anxiety over trade and globalization is focused on issues in the U.S.-China trade relationship as China has become an increasingly significant player in the global economy. In the unfolding debate on the U.S.-China trade relationship, few U.S. industries have more at stake than retailers. Consumer goods comprise nearly 80 percent of all U.S. imports from China, and China is a key supplier, and sometimes the dominant supplier, in every consumer goods category. Moreover, retailers have been adversely impacted by a recent increase in trade remedies investigations (antidumping, countervailing duty and safeguards) against imported consumer products mainly targeting China. Indeed, many of the proposed changes to the trade remedies laws currently under consideration before this committee are intended primarily to target imports from China.

The retail industry acknowledges that there are serious and legitimate issues with China that need to be effectively addressed, including inadequate protection of intellectual property rights, proliferating market access barriers, the need for a monetary system that allows for more flexible exchange rates and a fully-convertible currency, ensuring that China abides by its obligations under international trade rules, and dealing with the difficulties inherent in China's transformation from an isolated, centrally-planned, non-market economy to a market-economy country. In considering how best to address these issues, the retail industry urges prudence and thoughtfulness on the part of policy makers. Policy makers should support appropriate action through diplomatic efforts and the use of multilateral mechanisms to address issues in the U.S.-China relationship that can yield effective progress and are consistent with World Trade Organization (WTO) rules.

However, we continue to see descriptions of issues in the U.S.-China trade relationship presented in the most reckless, sweeping, facile, and grossly exaggerated terms – China “cheats”; China has “stolen” “millions” of American jobs; China exports goods made by “slave labor” working for “pennies a day”; the “devastating” impact of China’s “enormous” subsidies and “massive” currency undervaluation; a “flood” of “unsafe and poisonous” Chinese products; etc.<sup>4</sup> Indeed, from the tone of many of these

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<sup>3</sup> See, e.g., *Imports and America*, *Ibid*.

<sup>4</sup> See e.g., AFL-CIO website, [www.aflcio.org](http://www.aflcio.org); American Trade Action Coalition (AMTAC) website, [www.amtadc.org](http://www.amtadc.org); National Council of Textile Organizations (NCTO) website, [www.ncto.org](http://www.ncto.org); Public

and other statements, one might be led to think that China is responsible for the loss of every manufacturing job in the United States, is largely to blame for the current state of the U.S. economy, and that China's exchange rate policy is the main reason behind the U.S. bilateral trade deficit with China. These are absurd propositions on their face.

Too frequently, the intention behind this hyperbole is not to propose serious solutions to any of the issues the United States has with China. Rather the goal is to justify a protectionist agenda – blocking imports from China and punishing U.S. companies that do business in China all purportedly in the emotionally-charged, but largely meaningless name of “fairness.” The U.S.-China trade relationship is simply too complex and important to be driven by such emotional rhetoric.

In looking at serious policy options to address issues in the U.S.-China trade relationship, NRF and the retail industry have consistently supported the Strategic and Economic Dialogue (SED) and recent actions by the U.S. Trade Representative's Office against China under the WTO dispute settlement mechanism over practices that violate WTO rules, and coordination at the multilateral level. We applaud statements by the Obama Administration and Chairman Levin emphasizing the use of all available diplomatic avenues and constructive dialogue with China to address issues such as currency policy and practices. By the same token, we believe it is appropriate for the United States to protect its rights by challenging China at the WTO where there are clear violations of international trade rules. Diplomatic avenues, such as the SED, and dispute settlement through the WTO may be slower processes than some may prefer, but are most likely to yield positive results while avoiding unintended consequences that could hurt the U.S. economy and jobs.

On the other hand, the Administration and Congress should reject unilateral, counterproductive, and WTO illegal restrictions on imports of Chinese goods as a policy tool to compel action by China. There is no evidence that these actions would be effective in addressing any of the issues in the U.S.-China trade relationship. Meanwhile, they would impose huge costs on the U.S. economy, seriously harm U.S. retailers, manufacturers, services providers and farmers that depend on trade with China and global supply chains, and adversely affect millions of American consumers.

## **Chinese Currency and Exchange Rate Policy**

The subject of this hearing – Chinese currency policy and the value of the yuan – are central issues in the debate over U.S.-China trade relations. Some claim that the

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Citizen website, [www.citizen.org](http://www.citizen.org); Stand Up For Steel website, [www.standupforsteel.org](http://www.standupforsteel.org); UNITE-HERE! website, [www.unitehere.org](http://www.unitehere.org).

yuan is greatly undervalued vis-à-vis the dollar, and blame it as the driving factor behind the sizable bilateral trade deficit with China and the loss of U.S. manufacturing jobs.<sup>5</sup> Among their proposed remedies is to impose trade barriers to imports from China through various means, including changes to the U.S. antidumping and countervailing duty laws. They would also essentially force the U.S. Trade Representative to initiate dispute settlement proceedings at the World Trade Organization (WTO) against Chinese currency policy and the Secretary of the Treasury to determine that China is a currency manipulator. Not surprisingly, these proposals are strongly endorsed by certain domestic industries, such as steel and textiles, that for decades have relied on, and continue to seek new means to impose trade barriers against imports, particularly from China.

There is no real disagreement that China must move toward a more flexible currency regime. The only disagreements are the means to effect that change and how quickly it can reasonably be accomplished without creating further turmoil in the financial sector, and adversely impacting the U.S. economy. As a guiding principle, we oppose unilateral, counterproductive, and WTO illegal restrictions on imports of Chinese goods as a policy tool to compel action by China. By the same token, we are convinced that the best course of action is dialogue and negotiation through mechanisms such as the SED and the Joint Commission on Commerce and Trade (JCCT). A deft diplomatic and multilateral strategy by the United States will ultimately be a much more effective tool in identifying mutually-beneficial goals, and moving the Chinese Government in a more constructive direction, while strengthening, rather than undermining the important U.S.-China economic relationship.

By the same token, we will continue to oppose the use of trade remedies as a means to address China's currency policy for two reasons. First, many of the proposed changes to the trade remedies laws would violate WTO rules. Second, there may be widespread consensus among economists that the Chinese currency is undervalued, but there clearly is no agreement over the extent to which the yuan is undervalued. Thus, any attempt to quantify the degree to which the yuan may be undervalued, with

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<sup>5</sup> Evidence does not support the claim that China's exchange rate is a significant factor in the size of the U.S. trade deficit or in the loss of "millions" of U.S. manufacturing jobs. As the US-China Business Council correctly observed in its paper, *China and the US Economy: Advancing a Winning Trade Agenda* (Jan. 2009), much of what is imported from China had been imported from other Asian countries. Moreover, while transportation and labor costs, as well as inflation had a significant impact on the price of imports from China in the first half of 2008, there is little evidence of such an impact from the 20 percent appreciation in the Yuan, which had the offsetting effect of lowering the cost of imports into China. Accordingly, it is simply not credible that forcing China to appreciate its currency further will reverse the U.S. trade deficit. The economic crisis itself resulted in a huge drop in Chinese exports – 17.5 percent in January 2009 – which adversely impacted both the U.S. and Chinese economies.

the degree of specificity required in an antidumping or CVD case, will result in an entirely arbitrary and inaccurate calculation.

One proposal to address the currency issue through the use of the trade remedies laws that raises particularly troubling concerns is legislation that would redefine countervailable subsidies to include the undervaluation of a foreign currency through exchange rate manipulation or misalignment. NRF has argued in the past that this unilateral attempt by Congress to redefine what constitutes a countervailable subsidy would conflict with WTO rules and invite trade retaliation or reciprocal action to the detriment of U.S. companies and workers.

The WTO Subsidies Code<sup>6</sup> identifies three types of subsidies – prohibited; actionable (*i.e.*, subject to countervailing duties); and non-actionable (*i.e.*, permitted). Articles 1 and 2 of the Subsidies Code specify that to be countervailable, a subsidy must be: (1) a financial contribution from a government (2) that provides a benefit (3) to a specific industry or industries or enterprise or group of enterprises.

Because the “benefit” from currency valuation is generally available to all economic players in a country, the proposed legislative change would conflict with the specificity requirement under WTO rules. Because currency policy does not involve the transfer of anything of tangible value from the government, the proposed legislation would also conflict with the financial contribution requirement under WTO rules. Currency policy also cannot meet the WTO definition of a prohibited subsidy because its benefit is not contingent on exportation and does not require the use of domestic goods.

Moreover, some proposals would direct that currency misalignment be determined on the basis of a country’s trade balance, amount of foreign direct investment, and foreign currency reserves. What these proposals fail to recognize is that these matters are influenced by many factors that may have nothing to do with a country’s currency policy.

In the end, defining a countervailable subsidy in a way that violates WTO rules would undermine efforts to ensure that other countries abide by international trade rules, expose exports of U.S. goods and services to possible trade sanctions, and does nothing to address the underlying issue in an effective manner.

Another troubling proposal with respect to the currency issue would require adjustments to antidumping margins in investigations and reviews to offset the amount

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<sup>6</sup> WTO Agreement on Subsidies and Countervailing Measures of the General Agreement on Tariffs and Trade 1994.

by which a country's currency may be undervalued or "misaligned." There is, however, no widely accepted benchmark for determining the extent to which a particular currency may be undervalued. In the case of China, it was claimed the Yuan was undervalued by 15 to 40 percent. That is a huge range that demonstrates the imprecision of the calculation. Thus, any calculation by the Commerce Department, that has no expertise on such matters, will be an entirely arbitrary exercise, and therefore subject to political influence.

However, the bigger threat from this proposal is the precedent it would set to allow any country to game the antidumping process by unilaterally setting an arbitrary value on another country's currency. The result will be to make the trade remedies system even more unpredictable for U.S. importers and exporters.

Another problem with this proposal is that it would violate Article 2.4.1 of the WTO Agreement on Antidumping (AD Agreement), which establishes the rule for currency conversion and adjustments by reference to the value set by currency markets:

"When the comparison [between export price and normal value] requires a conversion of currencies, such conversion should be made using the rate of exchange on the date of sale, provided that when a sale of foreign currency on forward markets is directly linked to the export sale involved, the rate of exchange in the forward sale shall be used." (emphasis added)

No other provision of the AD Agreement would permit this type of adjustment. Notably, Article VI.2 of the General Agreement on Tariffs and Trade applies only to multiple currency practices, not "fundamentally misaligned currencies."

In addition, the surrogate country methodology used in AD investigations against imports from China and other non-market economy (NME) countries already addresses the effect of any currency undervaluation. In calculating an AD margin in NME cases, the Commerce Department uses market-based values from a surrogate country to determine the normal value of the subject imports, which it then compares to the U.S. export price. As a result, the AD calculation effectively offsets the effect of the currency undervaluation on price. Requiring an additional adjustment would violate WTO rules by capturing the effect of the undervaluation twice.

Thus, we are left with the question of what would be an effective approach to the currency issue. We agree with several points on this issue raised in an article in the

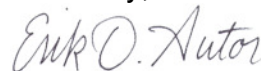
opinion section of the Wall Street Journal on March 18, 2010.<sup>7</sup> In particular, moving China to a fully-convertible currency and loosening capital controls are more important reforms than a futile attempt to force China to revalue or float the yuan. As pointed out in the article, lack of full convertibility and excessive capital controls are two factors spurring the Chinese government to buy huge amounts of U.S. Treasury notes and hindering efforts at further liberalization of the Chinese financial sector.

In any event, as also noted in the article, there is no assurance that a revaluation or full float of the Chinese currency will have any appreciable impact on the U.S. bilateral trade deficit with China, especially if the Chinese economy is adversely affected through deflation and imports into China decline as a result as happened under similar circumstances with Japan in the late 1980s and early 1990s. Indeed, appreciation or float of the yuan will certainly have no impact on the overall merchandise trade deficit as any Chinese production adversely impacted by a higher valuation of the yuan will likely simply move to another foreign country.

In conclusion, before acting on any legislation targeting Chinese currency policy, Congress and the Administration need to ask three questions: (1) Does the legislation conform to WTO rules?; (2) Will the legislation be effective in achieving the stated goal?; (3) Will any benefits of the legislation outweigh the harm it may inflict on U.S. companies, workers, and the economy? If the answers to any one of these questions is no, then the entire exercise will be seen as merely protectionist political posturing.

NRF appreciates the opportunity to comment on China's exchange rate policy. Should you have any questions please contact me at (202) 626-8104 or by e-mail at [autore@nrf.com](mailto:autore@nrf.com).

Sincerely,



Erik O. Autor  
Vice President  
International Trade Counsel

cc: The Honorable Dave Camp (R-MI), Ranking Member

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<sup>7</sup> *The Wall Street Journal*, Opinion: The Yuan Scapegoat, The U.S. establishment flirts with a currency and trade war with China (Mar. 18, 2010).



The Honorable Xavier Becerra (D-CA)  
The Honorable Shelley Berkley (D-NV)  
The Honorable Earl Blumenauer (D-OR)  
The Honorable Charles W. Boustany, Jr. (R-LA)  
The Honorable Kevin Brady (R-TX)  
The Honorable Ginny Brown-Waite (R-FL)  
The Honorable Eric Cantor (R-VA)  
The Honorable Joseph Crowley (D-NY)  
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