Written Testimony of

The Honorable Phil English
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Before

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Committee on Financial Services

"China's Exchange Rate Regime and Its Effects on the U.S. Economy"

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Chairman King, Ranking Member Maloney and Members of the Committee, it is my pleasure to appear here today to relay what I believe to be substantial negative effects to the U.S. economy as a result of Chinese monetary policy. Thank you for the opportunity to testify before you today.

When President Clinton approved China's entry into the WTO in 1999, many believed a new era of vast opportunity for U.S. businesses and workers had opened. Those in Congress, like myself, who were skeptical this opportunity would not come without substantial risks, voted to grant Permanent Normal Trade Relations to China only after insisting that special safeguards relating to Chinese imports be included.

Looking back from China's accession to the WTO until now, I would like to convey a clear message: few of the benefits intended for America have been realized because China has not abided by the terms of their international commitments. And while the current Administration has begun to develop a comprehensive strategy to ensure China plays by the rules, these steps must be accelerated, strengthened and enforced.

China has pegged its currency, the yuan, at a rate of approximately 8.3 to the dollar since 1994. As a result of this peg, other major currencies in East Asia have also been under tremendous pressure to intervene by infusing massive amounts of foreign currency into their reserve accounts or manipulate their currency to maintain stability. If China were to freely float its currency, it would deny other Asian countries a convenient excuse for manipulating their currencies. This would bring about a revaluation of Asian currencies against the dollar (and the Euro) which is needed to restore a balance among global currencies and reduce the threat of a hard landing for the dollar.

Misalignments in currency, particularly in the case of China, adversely affect the benefits gained from trade concessions. In fact, misalignments in currency caused by government policies intended to maintain an unfair trade advantage can impair and even nullify trade concessions. Many economists estimate that the Chinese yuan is undervalued against the dollar by as much as 40 percent. Essentially, this amounts to a 40 percent subsidy on all Chinese exports to the U.S. and a 40 percent tariff on all U.S. exports to China. U.S. exports to China currently face an average bound tariff of 15 percent. If recent estimates of China's currency undervaluation are correct, the effect of a free and open currency market would be more than twice as large as the effect of eliminating every tariff that China imposes on U.S. exports. Therefore, it is imperative countries allow their currencies to reflect their true value or else all of the benefits of bilateral trade are eliminated.

Because China's currency is pegged to the dollar, and other currencies have readjusted against the dollar, the economic effect of China's currency policy to the United States is more pronounced. To illustrate the point: since February, the dollar has fallen by approximately 25 percent against the Euro, but by 10 percent or less against the yen and most other Asian currencies. The dollar has, of course, remained unchanged against the yuan. At the same time, China's net exports to the U.S. have grown rapidly, but China's trade surplus with the world as a whole has actually been falling, and is down sharply this year. This strongly suggests that China's currency regime is contributing strongly to the rapidly ballooning trade imbalance between the U.S. and China. The U.S. – China trade deficit is projected to reach more than $120 billion in 2003, $17 billion over the previous year and the largest bilateral trade deficit in the world.

This is precisely why the practice of manipulating currency to obtain an unfair advantage in trade is illegal within the frameworks of two international bodies – the World Trade Organization and the International Monetary Fund – as well as U.S. law.

While each provision contained within international or domestic law defines this highly destructive practice slightly differently, the end goal of each provision of law is the same: to provide a mechanism to countries which play by the rules to address the egregious practice of currency manipulation and thereby restore the benefits of trade. As I have studied this issue further Mr. Chairman, I have found the international mechanisms to be inadequate.

For this reason, I have recently introduced – along with Representatives Cass Ballenger and Mark Green – H.R. 3058, *The Currency Harmonization Initiative through Neutralizing Action (CHINA) Act of 2003*. While there have been multiple bills and resolutions introduced in Congress on this topic, the CHINA Act enjoys the most robust co-sponsorship, currently supported by over 60 members of the House of Representatives.

The premise of the CHINA Act is straightforward: It requires the Secretary of the Treasury to determine if China is manipulating its currency to gain an advantage in trade. If the Secretary finds manipulation is occurring, then he is directed to impose a tariff equal to the degree of manipulation on all imports from China. This is in addition to any existing tariffs on Chinese products.

This is a measure that actually levels the playing field. It strips China of their ability to give themselves an arbitrary advantage. It is a flexible tariff and it can be adjusted to meet the actual extent of the distortions from the artificial undervaluation of the Yuan.

While I understand that participation in an open and fair global economic system is essential to U.S. economic growth and job opportunities, when China breaks the rules, the U.S. suffers the consequences. Through observing the direct effect China's state-sponsored mercantilism has had on my district in northwest Pennsylvania, it is very clear to me that China's currency regime is: neutralizing gains made through trade liberalization, heavily contributing to our bilateral trade deficit with China, subsidizing Chinese exports to the U.S., and taxing U.S. exports to China. Of potential greater consequence, however, is that this type of blatant disregard for international trade law will erode support within the U.S. for the WTO and the multi-lateral trading system. Very simply Mr. Chairman, Congress must ensure that the U.S. maintains the ability to police its own markets and force others to play by the rules.

Thank you again for the opportunity to appear before you today.