

# U.S.–China Trade and Competition

## Testimony before the House Committee on Ways and Means

**Testimony** • By [Thea M. Lee](#) • February 26, 2020

### Summary

The history of U.S. trade policy toward China is one of missed opportunities and misplaced priorities. For decades both Democratic and Republican administrations have failed to articulate or implement a clear, consistent China strategy that prioritizes the interests of American workers, communities, and domestic producers. Under current conditions, the decentralized, mostly market-driven U.S. system cannot thrive when put into direct competition with China's state subsidies, interventions, lack of transparency, and systematic violations of workers' rights.

To effectively address this:

- Our trade enforcement measures should prioritize good jobs, workers' rights, democracy, environmental compliance, and consumer safety over outsourcing and short-term profits.
- We need to make sure that we have—and are willing to use—measures to address currency misalignment.
- We should use the purchasing power of the U.S. government more concertedly to support good jobs, workforce development, responsible employers, and forward-looking environmental policies.

## Testimony

Thank you, Chairman Neal, Ranking Member Brady, members of the Committee, for the invitation to participate in this important hearing. I am the president of the Economic Policy Institute (EPI), the nation's premier think tank for analyzing the effects of economic policy on America's working families. EPI has focused attention over many years on the impact of the imbalanced U.S. economic relationship with China on U.S. jobs and wages, as well as on American business and the long-term prospects for U.S. innovation and growth.

The U.S.–China trade relationship is at a crossroads. Almost two decades after China joined the World Trade Organization (WTO), the U.S. has continued to run large, lopsided, and upward-trending trade deficits in goods with China. According to EPI research, the growing U.S.–China trade deficit was responsible for the loss of 3.7 million U.S. jobs between 2001 and 2018. These job losses are spread across all 50 states and the District of Columbia—and every congressional district in America.<sup>1</sup>

As economists David Autor, David Dorn, and Gordon Hanson have documented, the impact of the “China Shock” on American workers and communities was deep and long-lasting, “with wages and labor-force participation rates remaining depressed and unemployment rates remaining elevated for at least a full decade after the China trade shock commence[d],” leading to reduced lifetime income for those impacted.<sup>2</sup>

Moreover, it has become increasingly apparent in recent years that the composition of the U.S. trade imbalance with China is of as much concern as the magnitude, and this has important implications as we look toward the future and address the question of how Congress and the administration should shape U.S. policy toward China and how that policy interacts with domestic policy decisions.

## History

The uncomfortable truth is that the history of U.S. trade policy toward China is one of missed opportunities and misplaced priorities. Despite bouts of election-season rhetoric, for decades both Democratic and Republican administrations have failed to articulate or implement a clear, consistent China strategy that prioritizes the interests of American workers, communities, and domestic producers.

Instead, U.S. policy toward China has focused on protecting the profits and overseas operations of multinational corporations with respect to investment protections, intellectual property rights, and financial services. This was evident in the terms of China's accession to the WTO, of which the U.S. was a prime architect. Unfortunately, it is also true of the recent U.S.–China phase one trade deal.

## Phase one trade deal

The Trump administration's more aggressive stance toward China, including the willingness to employ tariffs as leverage, has in many ways represented a welcome shift in approach from previous administrations' inaction and timidity. Ultimately, however, the phase one deal squandered that leverage and failed to address the key structural issues at the root of the U.S.–China economic relationship.

The phase one deal focused on e-commerce, intellectual property rights, trade secrets, and technology transfer. It established ambitious and specific two-year targets for China's purchase of American exports in agriculture, manufacturing, energy, and services.<sup>3</sup> While boosting U.S. exports to China is a worthwhile goal, it isn't clear that these targets can or will be met (given China's slowing economic growth, the disruptive impact of the coronavirus, and the sheer logistics involved in such large increases over a short period of time). And, in the absence of a more coherent and comprehensive strategy, meeting the targets could involve other undesirable distortions, such as decreases in the U.S. exports of goods and services not covered by the agreement or shifting trade patterns with other trading partners.

The phase one deal does address currency manipulation, which is one of the most important U.S.–China trade concerns, but the approach is problematic. The deal reiterated existing WTO and International Monetary Fund commitments with respect to currency manipulation, and bound both countries to “refrain from competitive devaluation” and using “large-scale, persistent, one-sided intervention in exchange markets.”

Unfortunately, without further clarification, this provision is likely to be ineffective or even counterproductive. Under U.S. law, the president possesses executive authority to realign the dollar when necessary, as President Nixon did in 1973 and President Reagan did in 1985.<sup>4</sup> By agreeing that the United States will not intervene in currency markets, President Trump could be sacrificing a useful and necessary tool for realigning the dollar and strengthening the U.S. manufacturing sector.

Equally problematic, the phase one deal does not address critical areas of friction, namely China's industrial subsidies, state-generated overcapacity, state-owned enterprises, and egregious workers' rights violations. These issues are central to defining appropriate terms of competition between the very different economic systems of China and the United States.

Given the dominance of the Chinese government and the Chinese Communist Party in directing economic activity, any viable “rules-based system,” whether multilateral or bilateral, needs to explicitly delineate acceptable and unacceptable competitive behavior, but the phase one deal instead focuses on opening financial services markets and setting export targets. The decentralized, mostly market-driven U.S. system cannot thrive when put into direct competition with state subsidies, interventions, lack of transparency, and systematic violations of workers' rights.

While the administration has stated that some of these issues will be addressed in a phase two deal,<sup>5</sup> it is unclear whether either government is motivated to return to the bargaining table any time soon. In the meantime, the United States will continue to lose market share in strategic sectors to China.

In sum, the phase one deal does not adequately confront the key challenges and problem areas in the U.S.–China trade relationship; it focuses instead on opening financial markets and setting possibly unrealistic export targets.

## Industrial policy

It is no secret that the Chinese government has a long-term economic strategy to build certain sectors through subsidies, as well as government purchasing, tax, and regulatory policies. These strategies—including pillar industries, strategic emerging industries, Made with China, and Made in China 2025—are announced publicly at regular intervals.<sup>6</sup> These strategic plans are variations on the theme of “picking winners,” also known as industrial policy. These plans set targets for indigenous production, use of technology, favorable treatment for state-owned enterprises, and discriminatory treatment of foreign brands and companies, among other things. These practices are deep and pervasive.

Of course, the Chinese government has a right to set its own strategic goals, and the U.S. can certainly be faulted for failing to articulate, let alone implement, its own coherent, long-term economic strategy.

But there are two problems here, and we should be careful to distinguish them. On the one hand, many of the Chinese government’s practices are inconsistent with international rules and norms—not just WTO rules on prohibited subsidies and dumping, but also international conventions on workers’ rights, public health, human rights, environmental protections, intellectual property rights, and consumer safety. The United States can and should insist on China’s compliance with relevant international rules—and, where those rules are inadequate or incomplete, the U.S. should use its international clout to press for improvements.

On the other hand, the United States could certainly benefit from long-term, “whole-of-government” strategic planning and adequate investment in infrastructure and human capital. This is not a trade issue, but rather one of domestic choices and priorities.

With respect to international norms, for the last several decades, the U.S. government has not meaningfully addressed, via trade tools or diplomatic channels, China’s failure to comply with its obligations as a member of the International Labor Organization (ILO) to “respect, promote, and realize” the core international workers’ rights outlined in the ILO Declaration on Fundamental Principles and Rights at Work: freedom of association, right to organize and bargain collectively, and freedom from child labor, forced labor, and discrimination.<sup>7</sup> This means that American workers and businesses are competing on a tilted playing field, since Chinese workers cannot exercise their rights to form independent and democratic unions, and the Chinese government has not enforced protections against forced labor and child labor.

The AFL-CIO filed a Section 301 case against China in 2004 and again in 2006, alleging that the Chinese government’s systematic repression of workers’ internationally recognized rights to freedom of association and collective bargaining constitutes an unfair trade practice, harming American workers and businesses.<sup>8</sup> The George W. Bush administration rejected the petitions without much justification, despite conceding that the factual basis of the petitions was sound. The Bush Department of Labor and U.S. Trade Representative (USTR) asserted that the allegations laid out in the Section 301 petitions would be addressed by other diplomatic actions, but there is no evidence that any such actions were pursued.<sup>9</sup>

The Chinese government’s repression of workers’ rights to unionize and reprisals against those who speak out against flagrant wage and hour violations artificially suppress wages, and this keeps prices of Chinese-produced goods artificially low. The U.S. government has consistently failed to make this unfair trade practice a priority in its bilateral negotiations with the Chinese government, including in the phase one deal.

It is important to recognize that—in addition to calling out unfair practices on the part of the Chinese government—the U.S. has its own responsibility to develop and implement a coherent long-term economic strategy with respect to manufacturing and services, both trade-related and domestic.

The U.S. government has failed to invest adequately in infrastructure and skills for decades, and business has not filled the void. We have a tax system that rewards capital over labor and outsourcing over domestic production. It remains riddled with unproductive loopholes, and—especially after the 2017 Tax Cuts and Jobs Act—it fails to raise adequate revenue to fund needed investments.

In this sense, there are potentially lessons for the United States to learn from China’s long-horizon strategic planning and willingness to invest in rising industries and human capital. The truth is that the United States already has an industrial policy of “picking winners and losers”: Our tax code rewards and punishes certain sectors, our education policy steers students in certain directions and discourages other choices, and we decide how much and whether to invest in renewable energy, public transportation, and affordable college and graduate education. Our failure to recognize that we have an industrial policy means that our policy is haphazard and not strategic.

The Chinese government is clearly playing a long game, while the U.S. is egregiously shortsighted. Our trade enforcement measures should prioritize good jobs, workers’ rights, democracy, environmental compliance, and consumer safety over outsourcing and short-term profits. We need to make sure that we have—and are willing to use—measures to address currency misalignment. We should use the purchasing power of the U.S. government more concertedly to support good jobs, workforce development, responsible employers, and forward-looking environmental policies.

The Trump administration’s aggressive tariff policy has demonstrated conclusively that the U.S. has effective leverage over China. The imposition of tariffs was clearly sufficient to bring China to the bargaining table and elicit significant concessions.

Unfortunately, they were not the right concessions. They focused more on the financial sector and blunt export targets than on addressing structural and competitive concerns. Our goal should be to use that leverage more strategically in service of a different set of objectives: 1) strengthening the ability of U.S. producers and workers to compete over the long term by leveling the playing field with respect to currency, subsidies, unfair pricing, workers' rights, environmental policies, and consumer safety; 2) engaging in medium- and long-term strategic planning to ensure that the U.S. has a fair shot of succeeding in the critical rising industries; and 3) coordinating with allies to develop and enforce fair international rules.

Thank you for your attention. I look forward to any questions you may have.

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## Notes

1. Robert E. Scott and Zane Mokhiber, *Growing China Trade Deficit Cost 3.7 Million American Jobs Between 2001 and 2018*, January 2020.
2. David H. Autor, David Dorn, Gordon H. Hanson, "The China Shock: Learning from Labor Market Adjustment to Large Changes in Trade," National Bureau of Economic Research Working Paper no. 21906, January 2016.
3. The text of the [phase one trade agreement](#) is on the U.S. Trade Representative website.
4. Kenneth N. Gilpin, "The Dollar's Wild Ride," *New York Times*, June 19, 1988; Edwin R. Dale, "The Dollar Slides Closer to Reality," *New York Times*, February 18, 1973.
5. Jessica Bursztynsky, "Trump Trade Advisor Peter Navarro Lists What the US Wants from China in 'Phase Two' Trade Deal," CNBC, January 16, 2020.
6. See, for example, State Council, People's Republic of China, "'Made in China 2025' Plan Issued," May 19, 2015; Yao Nian, "China's Opening Up in 40 Years: From 'Made for China' to 'Made with China'," CGTN.com, September 18, 2018; Victor Ban, "China Names Latest 'Strategic Emerging Industries,'" *Global Policy Watch*, March 6, 2017; and ShanghaiDaily.com, "New Pillar Industries," December 20, 2016.
7. The [Declaration text](#) is at the International Labor Organization website.
8. Albert B. Crenshaw, "AFL-CIO Goes After China on Labor," *New York Times*, March 17, 2004; Steven Greenhouse, "A.F.L.-C.I.O. Files a Trade Complaint Against China's Labor Practices," *New York Times*, June 9, 2006.
9. See Steven Greenhouse, "A.F.L.-C.I.O. Files a Trade Complaint Against China's Labor Practices," *New York Times*, June 9, 2006: "The federation filed a similar complaint two years ago, but Mr. Bush quickly rejected it, with administration officials saying they would use persuasion and cooperation, rather than confrontation, to deal with labor violations in China."