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THE WHITE HOUSE
CORRESPONDENCE TRACKING WORKSHEET

INCOMING

DATE RECEIVED: AUGUST 14, 1991

NAME OF CORRESPONDENT: THE HONORABLE JOHN J. LAFALCE

SUBJECT: SUGGESTS THAT THE GRANTING OF MOST-FAVORED-NATION STATUS TO CHINA SHOULD BE CONDITIONED SO THE CHINESE GOVERNMENT STOPS MANIPULATING ITS EXCHANGE RATE TO GAIN AN UNFAIR AND

ROUTE TO: OFFICE/AGENCY (STAFF NAME)	ACTION: ACT CODE	ACTION: DATE YY/MM/DD	DISPOSITION: TYPE RESP	DISPOSITION: C D	DISPOSITION: COMPLETED YY/MM/DD
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99 USTR	I	91/08/23		C	/ / TC
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COMMENTS:

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262408

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August 12, 1991

The President
The White House
Washington, DC 20500

Dear Mr. President:

As you are well aware, the House recently voted to impose conditions on any granting of Most Favored Nation (MFN) status to China. I concurred with the majority of my colleagues in this matter.

In my view, there are many reasons that an unconditional granting of MFN is inappropriate at this time. The serious violation of fundamental human rights by the Chinese government and the potential adverse consequences for this Nation's trade balance of an unconditional granting of MFN are chief among them.

However, there is another more narrow, but nonetheless vital, issue highlighted in a recent Treasury Department report which should give our government serious pause about any unconditional granting of MFN status.

In 1988, as part of the Omnibus Trade Act, a provision commonly known as the Competitive Exchange Rate Act, which I authored, was enacted into law. The law has several important purposes: (1) to monitor the impact of U.S. exchange rate policy on the competitive position of U.S. firms at home and abroad; (2) to foster continued international cooperation on economic and exchange rate policy through the G-7 process; and (3) to monitor the exchange rate policies of our competitors to ensure that those policies are not manipulated to obtain for them arbitrary competitive advantage. The law requires that the Treasury submit a semi-annual report to the Congress on international economic and exchange rate policy.

In its most recent report, the Treasury strongly suggests that China is manipulating its exchange rate to gain an unfair and arbitrary competitve advantage vis-a-vis the U.S. According to the Treasury, there are mounting indications that China may seek to run significant current account and trade surpluses by combining devaluations of their currency, the yuan, and tight controls over foreign exchange allocation with severe restrictions on imports.

The increasing imbalance in our trade position with China must be a serious cause for concern. According to U.S. customs value data, China has a large and growing trade surplus with the United States. China's bilateral trade surplus with the U.S. grew 67 percent to $10.4 billion in 1990. Last year, China's exports to the U.S. rose by 27 percent, following a 41 percent expansion in 1989. **These growth rates are significantly above those for China's global exports during the same period.** China's imports from the U.S. rose 16 percent in 1989, but contracted by 16 percent in 1990 due to China's desire to limit overall imports.

U.S. data reveal a $1.7 billion deficit with China in the first 2 months of this year, a 30 percent increase over last year. This was our second largest trade deficit, behind that with Japan, and bigger than the total deficit with the four Asian Newly Industrializing Economies (NIEs). U.S. imports from China rose by 19 percent, while U.S. exports to China grew by only 2 percent during the period compared to last year.

This disturbing trend stems largely from a significant increase in Chinese exports -- especially such items as clothing, footwear and consumer electronics -- to the United States. These are areas in which this country's competitive advantage has already deteriorated seriously and in which we can hardly afford further inroads.

It is Treasury's assessment that the principal cause of China's bilateral trade surplus and external surpluses appears to be generalized and pervasive administrative controls over external trade, which inhibit imports, including those from the United States, and promote exports, particularly to the United States, China's largest market. Treasury emphasizes that the manner in which foreign exchange is allocated, along with import license and other market access barriers, is an important means by which China controls the external trade sector.

Given the substantial reserves, there is no basis for the current rationing system except to restrict imports and control sources. Treasury contends that there is strong evidence to suggest that a shift in China's exchange rate policy has occurred which is aimed directly at reinforcing China's attempts to generate sizable external surpluses.

If China does not wish to be perceived as deliberately manipulating its exchange rate policy to procure arbitrary competitive advantage, there are practical steps it can take. First, China should make foreign exchange allocation automatically to companies which either have import licenses or are authorized to import without licenses, thus removing foreign exchange allocation as another administrative barrier to imports. Second, China should liberalize foreign exchange transactions by permitting more transactions in the swap markets and the unofficial market. China should also eliminate other barriers to obtaining foreign exchange such as the requirement for explicit authorization.

In the meantime, it would be irresponsible -- for this and other important reasons -- for this government to support an unconditional granting of MFN status to China. The competitive position of major sectors of the U.S. economy has seriously deteriorated in recent years. Some of that is our own fault. But the unfair trading practices of foreign governments are also a factor.

We cannot ignore the clear evidence that your own Treasury Department has cited suggesting that China is utilizing exchange rate policy to arbitrarily enhance its trade position vis-a-vis the U.S. Any granting of MFN status should be conditioned on a commitment by the Chinese government to cease such practices.

Sincerely,

JOHN J. LaFALCE
Member of Congress

August 15, 1991

Dear Congressman LaFalce:

Thank you for your recent letter to the President expressing your thoughts on the House vote to impose conditions on Most Favored Nation status to China.

We appreciate knowing of your perspective on this issue. I was pleased to share your comments about China's trade practices with the President's national security and foreign policy advisors so that they, too, are aware of your recommendations.

Thank you again for your interest in writing.

With best regards,

Sincerely,

Frederick D. McClure
Assistant to the President
for Legislative Affairs

The Honorable John J. LaFalce
House of Representatives
Washington, D.C. 20515

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