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Showdown Looms on China Trade

White House Opposes Coming Legislation That May Result in Punitive Action

By JOHN MCCARY in Washington and ANDREW BATSON in Beijing
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A showdown is brewing between the White House and Capitol Hill over how best to address China's undervalued currency and other alleged unfair trade practices.

With little progress made on the issue during the semiannual economic summit between the U.S. and China last month, lawmakers on both sides of the aisle are nearing completion on legislation that could result in punitive action against China.

TRADE TARGET

- **The Situation:** New U.S. legislation could punish China over allegedly unfair trade practices, after an economic summit made little progress.
- **The Debate:** Sponsors and industry want to slow the U.S. deficit with China without triggering a trade war.
- **The Bottom Line:** China's rivals in textiles and steel would benefit from punitive legislation but retailers and consumers could see higher prices.

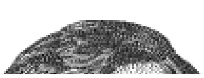
At least one bill, sponsored by Sens. Charles Schumer (D., N.Y.) and Lindsey Graham (R., S.C.) and due to be made public in mid-June if its backers can agree on its contents, has a real chance of passing, lawmakers and industry executives said.

"It's a pretty formidable task that's ahead of them" in drafting the legislation, said Erin Ennis, vice president of the U.S.-China Business Council, a lobbying group representing companies doing business in China. But the bill has an "extremely good chance of passage" given the prominence of its potential backers, which include Senate Finance Committee Chairman Max Baucus (D., Mont.) and ranking member Charles Grassley (R., Iowa), Ms. Ennis said.

Businesses are lining up on both sides of the fence, though with even some industry groups' members split on the issue, some of the groups are declining for now to take a position on any legislation.

Passage of punitive legislation could lead to a downturn in U.S.-China trade flows and reduce access for U.S. companies to China's booming markets. That could result in higher prices for U.S. businesses and consumers alike, especially in sectors with thin profit margins like textiles.

The White House says any protectionist legislation "is more likely to be counterproductive," and advocates continued economic dialogue and negotiations with the Chinese. But even if President Bush vetoes any such legislation, it could push the administration to take a tougher line on China -- and give it political cover to do so.



The U.S.'s trade deficit with China has surged in recent years, nearing $230 billion last year. Critics contend that a major factor behind the imbalance is China's alleged unfair trading practices, including its failure to allow its currency, the yuan, to appreciate at a faster rate. That keeps Chinese export prices unfairly low, giving them an advantage over rivals, critics say.

Earlier versions of the Schumer-Graham bill had proposed imposing a 27.5% import tariff on all Chinese goods, among other measures, in response to China's failure to boost the yuan's rate.

Sponsors have declined to comment on details of the latest Schumer-Graham bill, beyond saying that it will comply with rules of the World Trade Organization and that it will be "veto-proof." By holding China to promises it made in its accession to the WTO in 2001, the bill's sponsors hope to satisfy the diversified range of U.S. business interests in China.

"We have been very frustrated with China's lack of action," said Mr. Schumer. "We're working on tough, WTO-compliant legislation that will force China to do what it should be doing on its own."

Another bill, also with bipartisan backing from Reps. Artur Davis (D., Ala.) and Phil English (R., Pa.), seeks to clarify that countervailing duties can be applied to a nonmarket economy, such as China. Such duties are generally imposed to offset the impact of unfair government subsidies. Until recently, the U.S. government had taken the position that U.S. companies couldn't seek protection against unfair government subsidies of goods exported from "nonmarket" -- usually communist -- economies.

This spring, the Bush administration reversed that two-decade-old policy, allowing countervailing duties to be applied to certain Chinese paper imports. But critics have questioned whether the administration has authority to impose such duties. The Davis-English legislation would authorize it to do so.

The U.S. steel industry, which worries about cheap Chinese steel coming into the country, is backing the Davis-English bill.


Charles Schumer

Reps. Tim Ryan, an Ohio Democrat, and Duncan Hunter, an Ohio Republican, have reintroduced a bill to define currency manipulation as a kind of subsidy. That would allow the U.S. to seek redress for China's yuan policy under the rules of the WTO. Currency-manipulation issues fall under the domain of the International Monetary Fund, which has limited enforcement capabilities.

Plenty of challenges and complications face any legislation.

Legislation that is overly focused on currency appreciation may not work. "Chinese product is being delivered for less than the price of the raw materials. Even currency can't fix that," said Frank Vargo, vice president for international economic affairs at the National Association of Manufacturers, a Washington-based lobbying group.

Some Chinese companies play down the potential impact of any punitive legislation, saying they have already diversified after the U.S. previously imposed tariffs on Chinese goods. "Exports to the U.S. only account for around 10% of our whole export business, while the [European Union] is our key market, with more than 60% of our exported clothing," said a department manager at Hui Hong Knitting Import & Export Ltd., a unit of Jiangsu Huihong

International Group.

Qian Wang, an economist with J.P. Morgan Chase, said the Chinese government has, in fact, picked up the pace of yuan appreciation. "They recognize that if there is no appreciation, they will be hit by tariff increases. What China is trying to avoid is any sudden, one-off changes."

The yuan has appreciated 8% against the dollar since 2005, including a 2.1% boost engineered by Beijing in July 2001. It recently slightly widened the range within which the currency can trade daily.

Some U.S. companies are lobbying heavily for a legislative solution to the China trade issue. Members of the Precision Metalforming Association, an industry group with 1,200 companies which rely on globally competitive steel prices to make components, visited 85 congressional offices at the end of April to express their concerns about the Chinese currency. It is pushing for the Ryan-Hunter bill, which would define currency manipulation as a financial subsidy.

Many industries remain divided, with companies in various sectors and even within individual industry groups lining up on both sides of the issue.

The American Chamber of Commerce in China has voiced concern that overly political legislation could "undermine the international trade regime, derail constructive dialogue, and ultimately weaken the competitive position of U.S. business and the overall economy."

U.S. retailers may have the most to lose, both from rising import prices and from possible retaliatory measures by Beijing, such as restricting their access to the booming Chinese consumer market.

Even so, "I don't think anyone wants to defend the indefensible," said Stephanie Lester, vice president for international trade at the Retail Industry Leaders Association, referring to China's currency policy.

--Sue Feng in Beijing contributed to this article.

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