WITNESS STATEMENT OF
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for
THE NATIONAL COUNCIL OF TEXTILE ORGANIZATIONS

U.S.-CHINA ECONOMIC and SECURITY REVIEW COMMISSION

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Commissioner Fiedler and Commissioner Shea and other distinguished members of the Commission, thank you for the opportunity to appear today and outline China's impact on North Carolina's textile industry.

My name is Jim Chesnutt. I am President and CEO of National Spinning, an employee-owned textile manufacturer headquartered in Washington, North Carolina. We employ almost one thousand workers in facilities in North Carolina. National Spinning manufactures primarily acrylic yarns used in apparel, home furnishings, and industrial end products. I am also a member of the board of directors of the National Council of Textile Organizations.

U.S. Textile Industry Background

First, I would like to debunk some commonly held beliefs about the U.S. textile industry. I have often heard elected officials, so-called trade experts, and numerous retailers and importers refer to our industry as a dead or dying industry and one that is antiquated and not prepared to meet the challenges of manufacturing in the 21st Century. In fact, the exact opposite is true.

The U.S. textile sector continues to be one of the largest manufacturing employers in the United States. The overall textile sector employed nearly one million workers in 2005 and textile mills alone employed 383,000 workers.

Our industry is also the third largest exporter of textile products in the world exporting more than $16 billion in 2005. These exports went to more than 50 countries, with 20 countries buying more than $100 million a year.

In addition, the U.S. textile sector is a very important component of our national defense and supplies more than 8,000 different textile products a year to the U.S. military. The industry spends enormous resources on research and development each year to ensure that our military continues to be the most well-equipped and technologically advanced military in the world.

From 1994 to 2004, the U.S. textile industry invested more than $33 billion in new plants and equipment and has increased productivity by 49 percent over the last ten years. This investment has secured our second place ranking among all industrial sectors in productivity increases over the past ten years.

As you can see, the U.S. textile industry is an innovative, productive industry that can compete with anyone in the world if our government would not disadvantage us by supporting a trade environment that favors overseas producers to U.S. manufacturers.

That's the good news.

The bad news is that since China joined the WTO in 2001, the U.S. textile and apparel industries have lost 365,000 jobs, this represents a 38 percent decrease of our entire workforce. In fact, the industry lost 44,500 from 2005 to 2006 alone. North Carolina has been hardest hit by these plant closures and job losses and lost 11,365 jobs lost over just the last year, representing a 12 percent decrease of its entire textile workforce. The current environment is unsustainable long term, and not just for us, but for many other manufacturers as well.

U.S.-China Textile Trade

The purpose of this hearing is to evaluate the impact that trade with China, and the interventionist policies of the central government in Beijing, have had on workers, companies and communities in North Carolina. This is obviously an important issue for everyone in this room and particularly for those of us who continue to maintain a textile manufacturing presence in this state.

But this is not, in my opinion, the central issue. The central issue is not what policies or practices the central government in Beijing has undertaken; rather, the central issue is how our own government has responded, or, more accurately, has failed to respond to China's deliberate economic intervention on behalf of its citizens and its industry.

The U.S. government clearly has very limited, if any, direct control over events in Beijing. However, our government can and should defend itself, its workers, its companies, its communities and our own way of life from mercantilist policies that exploit democracy and the free-market system for its own gain. As the noted economist and Nobel Prize winner, Robert Samuelson recently stated: "It is not "protectionist" (I am a long-standing free-trader) to complain about policies that are predatory; China's are just that[1]." Our enormous trade deficit, the loss of more than one and half million manufacturing jobs[2] and the very real possibility that the Bank of China may soon have more control over our economy than the

[1] "*China's Trade Time Bomb*," Robert J. Samuelson, The Washington Post, Wednesday, May 9, 2007. Samuelson also noted:

> "China is already the world's third-largest trading nation and seems destined to become the largest. On its present course, it threatens to wreck the entire post-World War II trading system. Constructed largely by the United States, that system has flourished because its benefits are widely shared. Since 1950, global trade has expanded by a factor of 25. By contrast, China's trade is mercantilist: It's designed to benefit China even if it harms its trading partners."

[2] U.S.-China Trade, 1989-2003, Impact on Jobs and Industries: A Research Paper Prepared for the U.S.-China Economic and Security Review Commission. Economic Policy Institute, 2005.

Federal Reserve[3] is the disturbing legacy we face today as a result of decades of inaction by the U.S. government.

Recently, the costs of a do-nothing policy, both to our way of life as well as our country's economic and national security, have become more clear. Because of the efforts of this Commission and numerous other concerned individuals and groups, there appears to be a new interest from the Congress and, to a certain extent, from the Administration, to finally hold China to account. Only time will tell whether this new interest is real and will lead to meaningful action for U.S. workers and manufacturers.

In this context, I would like to focus my remarks today on actions the U.S. textile industry believes Congress and the government should take to rebalance the playing field and ensure that global trade rules are applied uniformly and in a way that ensures support for trade among U.S. workers and companies into the future. Absent such action, American workers will continue to question the benefits of trade and support for the trade agenda will remain on life support.

Before getting into specifics regarding what can be done to rebalance the trade equation with China, I should briefly explain how the Chinese government works to ensure that its textile sector dominates world trade in textiles and apparel.

The Chinese government's efforts are clearly defined in its 11th Five-Year Plan for the textile industry. This plan sets specific benchmarks for its textile and apparel sector over the next five years, continuing a pattern that has been in place for more than fifty years. These benchmarks include production, research, sales, fiber consumption, investment targets, among many others. Specific goals are established and specific policy instruments are introduced to ensure those goals are achieved.

How do these plans work? How can the Chinese government ensure success across such a broad and diversified manufacturing sector? NCTO has done an extensive review of the subsidies that China extends to its textile and apparel industries. According to various sources, the Chinese government offers its textile and apparel manufacturers 73 different subsidy programs and, as a result, has pumped tens of billions of government assistance into its textile sector over the last ten years (attachment 1). These subsidies are in addition to the enormous financial support which Beijing offers through its managed exchange rate, which most economist estimate is undervalued by 20 – 40 percent.

To better understand how these subsidy programs have enabled Chinese textile manufacturers to dominate the market, let's review a few key statistics – during the last ten years, the Chinese textile sector has purchased 65 percent of all knitting machines, 62 percent of all weaving machines and 46 percent of all spinning machines sold in the world.[4] To put this in another context, China's assistance to its textile industry has allowed Chinese

[3] *"Uncle Sam, Your Banker Will See You Now…*In the Hole to China", Paul Craig Roberts, The Baltimore Chronicle, 08/08/07.

[4] **"**International Textile Machinery Statistics", ITMF, Vol. 29, 2006.

manufacturers to buy an average of ten times more knitting, weaving and spinning machines than their next largest competitor.

These efforts by the central government in Beijing have reaped unparalleled rewards for its textile sector and have made China, by far, the largest producer and exporter of textile products in the world. From 2000 to 2005**,** China's worldwide exports of textiles and apparel jumped from $81 billion to $150 billion, an increase of $69 billion in just five years. As a result, China now controls over 40 percent of the global textile and apparel trade and nearly 50 percent of the apparel trade alone. And in product areas where China's exports have not been restrained either through safeguards or quotas, China's market share ranges from 66 percent (in the U.S. and EU) to nearly 90 percent (Japan and Australia).

The impact of China's government policies on the U.S. and North Carolina's textile industry has been nothing short of devastating. U.S. textile mill shipments have declined by 25 percent since 2000, and more than 160,000 textile workers have lost their jobs, with 11,365 workers losing their jobs in North Carolina in 2006. This has occurred despite aggressive efforts by the industry to modernize and streamline. Over the last ten years, the U.S. textile industry invested more than $30 billion in new plants and equipment – an investment rate that is 50 percent higher than the rest of the manufacturing sector.

But as the production and job loss statistics demonstrate, U.S. textile companies, as well as other manufacturing sectors, cannot survive when they are pitted against the Chinese government. As the Chinese government moves to progressively target the highest technology sectors of our economy (including aircraft, automobiles and semiconductors), we face the prospect of sector after sector in the United States falling before the Chinese onslaught.

We believe strongly, however, that this is not a battle that that the U.S. textile industry, or other sectors, has to lose. The U.S. consumer market is the single largest market in the world, a fact that China cannot ignore. In this sense, we control the cards. If we begin to play our own hand more skillfully, we could see a rebirth of manufacturing, including textile manufacturing, in this country. This will take a determination on the part of Congress and the Administration to force China to live by its own international obligations and to penalize China when it does not. In this vein, we recommend nine specific actions that we maintain could lead to a revitalization of U.S. manufacturing:

1. <u>Pass Strong Currency Legislation:</u> The Congress should pass and the President should sign into law meaningful and effective legislation that allows U.S. manufacturers to offset the benefits of the undervalued yuan. In our opinion, the most effective legislation currently before the U.S. Congress is a bill introduced by Representatives Ryan and Hunter – the Currency Reform for Fair Trade Act or H.R. 2942. This legislation would allow U.S. industry to file countervailing duty cases against China's currency manipulation. This is a reasonable, targeted approach which provides impacted industries with a means of defending themselves without penalizing unaffected parties. Other legislation, such as bills recently passed by the Senate Finance and Banking Committees are too weak because they do not address the subsidy component of

currency manipulation and provide numerous escape clauses which would allow the administration to “opt out” even when action is justified.

2. Extend or Replace the Current China Safeguard: Congress and the Administration should ensure that the textile safeguards currently in place against China are either extended or replaced until China fulfills all of its WTO-accession commitments. The textile safeguards, which have helped to prevent China from monopolizing the U.S. textile and apparel markets in key product categories, will expire on January 1, 2009, and they cannot, under WTO law, be unilaterally renewed. If China is allowed unfettered access in these categories, the consequences for U.S. textile companies and hundreds of thousands of textile workers will be catastrophic and North Carolina will likely be the hardest hit of all the textile-producing states. We know this will occur because during a five-month period in 2005 when China’s quotas were temporarily removed, prices of textile and apparel products from China fell by 40 percent while imports in key products increased by as much as 1,500 percent. If the government had not moved quickly to temporarily re-impose quotas, the industry would largely have been destroyed.

   The U.S. textile industry is facing this exact same scenario on January 1, 2009, but this time there is currently no recourse. As a result, the U.S. government must insist that China either agree to extend the current safeguards or face comprehensive dumping actions against apparel imports from China by the U.S. government when quotas are again removed. Anti-dumping actions must be self-initiated by the U.S. government because the U.S. textile industry lacks standing to take actions on apparel products and the U.S. apparel industry has largely moved offshore. Such punitive actions should stay in place until China fulfills the obligations of its WTO accession agreement.

   In addition, the U.S. government should expand third-country dumping provisions to grant apparel producers in the NAFTA/CAFTA regions the right to bring anti-dumping actions against Chinese apparel exporters who damage their own vital export markets in the United States. Since the passage of NAFTA and CAFTA, textile and apparel sectors in the region have become integrated with the U.S. supplying most of the yarns and fabrics and the NAFTA/CAFTA regions providing the apparel assembly. Ample precedent exists in the WTO for granting apparel producers in the entire region the right to seek redress for dumped goods.

3. Create a Comprehensive Subsidy Database: Establish a comprehensive subsidy database on China at the Department of Commerce that can be utilized by government and industry. The U.S. government still refuses to create a database of the subsidies the Chinese government provides to its industry. Instead, the government relies primarily on what China itself has notified as subsidies, a list that is laughably small and incomplete. And even then the Commerce Department’s database is not up to date – the government’s subsidy review page on the Commerce Department’s website has not been updated since 2004[5]. The most noteworthy observation here is that according to the Commerce Department website, China is not listed as employing a single subsidy!

[5] Commerce countervailing duty websites by country and type of subsidy: http://ia.ita.doc.gov/esel/index.html; http://ia.ita.doc.gov/esel/eselframes.html

4. Increase Dumping and CVD Assistance to Small and Medium-Sized Manufacturers: The government should increase assistance to small and medium-sized manufacturers so that they can afford to pursue dumping and countervailing duty (CVD) cases. CVD cases cost several hundred thousand dollars to file and dumping cases typically cost more than one million dollars - - costs that are too steep for most small and medium-sized businesses to pay, particularly when those businesses are already losing money because of dumping. The Commerce Department should follow the lead of the European Union by shouldering more of the administrative and financial burden in complying with the complex rules and regulations that the Department imposes.

5. Increase and Re-Prioritize Enforcement Efforts at USTR and the Department of Commerce: Today, trade enforcement is seen as a career dead end within the U.S. government; instead, negotiating new agreements rather than enforcing existing agreements is the best way to advance within the ranks. Commerce and USTR need to be restructured to give trade enforcement a higher priority and more status within the agencies. On top of enhanced focus on enforcement, these efforts also need to be greatly expanded. The U.S. government should be conducting ongoing reviews of Chinese government subsidy and support programs and taking action at the WTO and through U.S. trade remedies when warranted.

6. Review China's Government Support of Its State-Owned Industrial Sectors, Including Textiles, and Penalize Illegal Transactions: Over the past five years, China's government has forgiven tens of billions of dollars of debt in its state-owned manufacturing sector. This practice has salvaged countless unprofitable enterprises that would not have survived in a free market system. These enterprises, which comprise roughly half of China's textile assets, are notorious for suppressing prices to absurd levels, often below the cost of raw materials. In late 2005, China announced that it was liquidating almost $600 million in debt to a major Chinese textile manufacturer that it previously stated had been privatized.[6]

   These state-supported enterprises essentially operate as state employment agencies rather than market-based companies and their pricing practices have caused more damage to legitimate textile producers in the United States and elsewhere than anything else. Because of financial support from the Central Government, textile manufacturers in China can offer whatever price necessary to make the sell and grow its market share. A practice against which no other producer in the world can compete.

   In addition, China continues to effect privatization schemes which appear to transfer huge state-owned industrial enterprises to the private sector at virtually no cost. All of these actions are in direct conflict with China's WTO commitment to treat state-owned enterprises as if they were market entities.[7]

[6] "NCTO Decries Chinese Bailout of Textile Giant," 12/1/05, http://www.ncto.org/newsroom/pr200539.asp.

[7] Report of the Working Party on the Accession of China, 11/9/01, Chapter II, Paragraph 6, World Trade Organization.

7. Increase and Reform Customs Enforcement Efforts Targeting China: Recent newspaper headlines regarding widespread recalls of Chinese food and consumer products are yet another symptom of major enforcement issues involving China – primarily that U.S. Customs has become a trade facilitation, rather than trade enforcement, agency. With respect to textiles, this fact recently became all the more evident when the textile enforcement branch was transferred from the Operations Division into a trade facilitation office. This reorganization occurred despite strong opposition from U.S. industry and in direct conflict to the fact that more than half of all Customs fraud occurs in the textile and apparel sector and a majority of that is textile transshipment from China to avoid quotas and duties.

   Following that move, Customs has stopped reporting on textile enforcement efforts, halted data dissemination to the industry and cut back on key enforcement activities. CBP needs to intensify its enforcement efforts, particularly in the textile area. As with the Commerce Department and USTR, enforcement has now become a dead-end career path within Customs and this is not likely to change without a change in priority.

8. Develop a More Effective Enforcement System that Holds U.S. Importers and Consignees Responsible for the Products They Import and Provides for Stronger Penalties for Those Who Violate the Law: U.S. importers and consignees should and must be held responsible for the products they import.

   With respect to the recent spate of product recalls from China, fault does not lie with the Chinese manufacturer; rather, the fault lies with the U.S. company responsible for importing that product to the U.S. market. If the public at large and U.S. policymakers fail to recognize this important point, then any solutions will only be temporary band-aids that address a symptom but the not the underlying disease.

   U.S. laws and regulations can only effectively be applied to entities operating within U.S. borders. U.S. law enforcement and product safety officials do not have the authority to arrest someone in China or to levy fines on a business in China for poor practices. What they do have authority to do is to hold individuals or businesses operating in the U.S. to account when the products they import are found in violation of U.S. laws and regulations. These violations can be safety-related, but in the case of textiles and apparel could also include violations of rules of origin claims.

   With respect to textiles and apparel, rules of origin are the cornerstone of our free trade agreements and preference programs. In the history of the textile program, un-enforced rules have been a proven access point for large scale fraud which displaces legitimate production both in the U.S. and in the beneficiary country(s) involved. NCTO and our member companies have seen time and again how unscrupulous actors have knowingly violated rules and regulations governing U.S. preference and free trade programs to gain duty-free access to the U.S. market, with China being by far the worst offender. In fact, the textile and apparel trade has the highest fraud content of any manufactured good. Therefore, it is imperative that the rules and regulations governing this trade are effectively enforced and the only way to do this is through the importer or consignee.

U.S. regulations governing the importers, however, are weak and often times these importers will appear, disappear and then reappear under new names to avoid penalties and fines and the U.S. government does nothing about it. In considering future FTAs and other trade programs, Congress and the Administration should ensure that these agreements are written in a way that provides for meaningful and effective customs enforcement by requiring the ultimate consignee of the product, i.e. the retailer or the company owning the brand-name, responsible for rule of origin violations. In the 2005 ITC case U.S. v. The Pan Pacific Textile Group[1], the Court ruled that liability could be extended to the consignee when the consignee has direct input into how the transaction is structured. If the goal is to ensure that safety standards and rules of origin are adhered to then the law should be broadened to ensure that the consignee is also responsible for the products its sells or that bears its brand name.

9. Develop a System for Penalizing Companies Importing Products Which Were Made by Companies Who Pollute the Environment: A recent front page Wall Street Journal expose[8] on the Chinese textile industry revealed that continuing demands by U.S. importers for lower prices are playing a key role in the environmental catastrophe that is now unfolding across China. The Journal notes that "one way China's factories have historically kept costs down is by dumping waste water directly into rivers."

There are many other areas outside of China where new initiatives could help U.S. manufacturers and U.S. workers. These range from health care reform, reduced regulatory burdens, environmental reviews and the like. Equal to all of these is one little noticed, but extremely important issue – the inequity created through value-added tax systems. While the rest of the world employs a value-added tax system, including China, the U.S. corporate tax structure is a direct-tax system, meaning that we tax profits. As a result, U.S. exports are essentially double-taxed and U.S. imports enter our market tax-free. The current annual penalty that this discrepancy places on U.S. manufacturers equals nearly $400 billion.[9] U.S. manufacturers desperately need for this tax inequity to be addressed either by the U.S. adopting a value-added tax system or by being compensated for the costs imposed on them by the current system.

In conclusion, I would like to again thank the Commission for the leadership it has shown in the struggle to preserve U.S. jobs and U.S. manufacturing. Through your hard work, you have helped to lift the veil not only on the mercantilist practices of the Chinese government but the cost of those practices to workers across America. We look forward to working with you and other concerned groups to fashion a new trade policy that supports manufacturing and other jobs in this country.

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[8] "China Pays Steep Price as Textile Exports Boom," Wall Street Journal, August 31, 2007.
[9] "Industry Supports Border Tax Equity Act," AMTAC press release, 6/7/07.
http://www.amtacdc.org/SiteCollectionDocuments/Amtac/Press%20Room/06%2007%2007%20Border%20Tax%20Equity%20Act%20Press%20Statement.pdf