Oral Testimony

Before the U.S. Department of Commerce

Trade Deficits Investigation

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Thank you for the invitation to testify today. ITIF commends the Trump administration for undertaking a serious investigation of the causes of U.S. trade deficits, which for too long have been dismissed as a problem. Yet a long-term trade deficit (just like the federal debt) represents a debt that future generations of Americans must repay, while also signaling possible challenges to U.S. competitiveness, systemic unfair foreign trade practices, the hollowing out of America's industrial commons, and erosion of its defense industrial basis. ITIF would therefore lay out three priorities for the Trump administration as it undertakes this investigation: focus on traded sectors, advanced technologies, and the innovation mercantilists.

First, the analysis should be on all of America's traded sectors—those industries and establishments which compete in international marketplaces and whose output is sold in part to nonresidents of the nation. This includes not just manufacturing, but also services, such as software and Internet-based platforms, and content, such as music, movies, and video games.

Second, the investigation should recognize that not all trade deficits are created equally, and place primary focus on countries aggressively using unfair, "innovation mercantilist" trade practices to disrupt market-based trade and disadvantage U.S. competitors. This means a substantial focus on China, a country single-handedly responsible for 50 percent of the total U.S. trade deficit in goods in 2016, and with whom the United States has accumulated a goods trade deficit of over $3.5 trillion over the past decade. In fact, America's $347 billion goods trade deficit with China in 2016 was five times the level of the goods trade deficit with Mexico and far more than the $13 billion pittance with Switzerland or Taiwan.

China represents a systemic threat to both the U.S. economy and to the international economic system. It fields every mercantilist policy imaginable, from forcing technology and intellectual property transfer as a condition of market access to massively subsidizing industries from solar and semiconductors to steel and auto. Moreover, China fundamentally rejects the notion of comparative advantage (on which market-based trade is grounded) and instead seeks absolute advantage, as reflected in the fact that China's Integrated Circuit Development Strategy explicitly calls for halving Chinese imports of U.S.-produced semiconductors in 10 years and eliminating them entirely within 20 years.

While unfair, such policies have had an effect, now making China the world's largest exporter of high-tech products, with a 24 percent global share, and explaining why, in 2011, the United States imported 560 percent more technologically advanced products from China than it exported to China. This trade imbalance has inflicted serious damage on the U.S. economy and employment, with analysts estimating that America's trade deficit with China cost 3.4 million American workers their jobs from 2001 to 2015, with nearly three-fourths of those in the manufacturing sector. China's innovation mercantilism also damages the global trading system, compelling other nations such as Indonesia or Malaysia to emulate China's mercantilist ways.

Third, attention should focus on trade deficits with countries, like China, where the imbalance is hollowing out America's high-tech industries such as aerospace, biopharmaceuticals, semiconductors, software, clean tech, and other advanced materials and manufacturing activities. These industries generate more value-added for the U.S. economy, pay higher wages, and fund the vast majority of the nation's R&D activity. But if America loses its base of advanced industries to foreign competitors, its industrial supply chains and industrial commons will be hollowed out, leaving America unable to manufacture a wide range of advanced-technology products.

Thus, America needs to confront its trade partners whenever their policies harm America's advanced industries, whether we run a trade deficit with those countries or not. For instance, Canada's so-called "promise doctrine" has harmed U.S. biopharmaceutical manufacturers by leading since 2005 to the invalidation of 25 patents underpinning innovative life-sciences drugs, costing U.S. companies over $1 billion in lost sales from the premature termination of patents. Similarly, Canada and the European Union have provided billions in subsidies to their domestic airplane manufacturers, costing U.S. aerospace jobs.

Finally, ITIF hopes this investigation leads to improved U.S. competitiveness, manufacturing, and trade policy. One outcome should be working with the Organization for Economic Cooperation and Development to develop better statistics on global trade-in-value-added. Another priority for the administration should be developing a U.S. traded-sector competitiveness strategy that assesses a range of tax, talent, technology, financial, regulatory, and trade policy issues to maximize the competitive capacity of American industry. More resources need to be devoted to trade enforcement, and the U.S. Trade Representative should be asked to develop a new report that marries elements of the Special 301 and National Trade Estimates reports to comprehensively rank the nations whose mercantilist policies are doing the most to damage the U.S. economy. Finally, the U.S. government must understand it has limited resources and political capital. We can't do this alone. We must work with like-minded allies such as Europe, Canada, and Japan who—despite some faults—generally believe in market-based trade and work with them both to develop new high-standard trade agreements and to collectively push back against China's innovation mercantilism.