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AUGUST TRADE DEFICITS

HEARING

BEFORE THE

JOINT ECONOMIC COMMITTEE
CONGRESS OF THE UNITED STATES

NINETY-NINTH CONGRESS

FIRST SESSION

SEPTEMBER 27, 1985

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FRIDAY, SEPTEMBER 27, 1985

AUGUST TRADE DEFICITS

FRIDAY, SEPTEMBER 27, 1985

CONGRESS OF THE UNITED STATES,
JOINT ECONOMIC COMMITTEE,
Washington, DC.

The committee met, pursuant to notice, at 9:35 a.m., in room 2118, Rayburn House Office Building, Hon. David R. Obey (chairman of the committee) presiding.

Present: Representative Obey and Senator Wilson.

OPENING STATEMENT OF REPRESENTATIVE OBEY, CHAIRMAN

Representative OBEY. Good morning.

This morning we are pleased to have Commerce Secretary Baldrige with us to present the August trade statistics.

For many years the Joint Economic Committee has conducted similar hearings on monthly unemployment figures, and the trade figures and what they say about America's economy are obviously beginning to take on similar importance for the American people and the Congress of the United States.

In fact, as I think has become obvious, trade is what Members heard most about over the August recess when all of us were back in our districts. A good many Members have come back to Washington from that recess feeling under considerable pressure to take legislative action to deal with what most Americans see as a very significant and growing problem.

In response to that congressional pressure, as the Secretary will testify in just a few minutes, the administration announced its own program to deal with the growing trade deficit.

The President, in his recent speech Saturday, announced the initiation or acceleration of five unfair trade practice cases and announced a number of other actions as well.

Mr. Secretary, I think it is fair to say that a number of people on Capitol Hill, while they welcome the newfound aggressiveness on the part of the President in trade matters, a number of us would very much like to be reassured that the main target of the President's announcement is not the Congress and action pending here rather than dealing with the real problems we still face in the trade arena.

I think it is also safe to say that some of us are concerned that while the President may certainly genuinely be interested in trade problems, that nonetheless there is a strategy on the part of the administration to keep the dollar high in order to help finance the very large deficit which we will be incurring this year.

Some of us are really wondering just how intent the administration really is in bringing that dollar down significantly over something other than a long period of time.

Mr. Secretary, we are delighted to have you with us this moring. As a successful businessman, you have been on the firing line of foreign competition in a personal way. From your first days in the administration, you have been heavily involved in making and implementing U.S. trade policy. You bring to the trade problem an unusual mix of practical and policy experience. You also being to the room here this morning a reputation for being a straight shooter, and we are very happy to have you here.

I am pleased, from what I understand, that the numbers you will be discussing this morning—I am pleased to see that the trade deficit this month from last has declined somewhat, but I would agree with your comment in your statement that the figures being released this morning are nonetheless still an indication of a trend which—at least, a long-term trend—has to be of concern to us all.

At this point, I will place in the hearing record Senator D'Amato's written opening statement, at his request, who could not be present for today's hearing.

[The written opening statement of Senator D'Amato follows:]

WRITTEN OPENING STATEMENT OF SENATOR D'AMATO

MR. CHAIRMAN, I COMMEND YOU FOR HOLDING THIS HEARING TODAY ON THE U.S. TRADE DEFICIT. I ALSO WELCOME SECRETARY BALDRIDGE FOR TAKING TIME FROM HIS BUSY SCHEDULE TO SHARE HIS VIEWS ON THIS IMPORTANT MATTER WITH US.

THE UNITED STATES IS PRESENTLY FACING DIFFICULT TIMES IN INTERNATIONAL TRADE. MY CONCERN FOR THE UNITED STATES' POSTURE IN ITS TRADE RELATIONS IS HEIGHTENED BY A RECENT COMMERCE DEPARTMENT REPORT INDICATING THAT WHAT WE HAVE FEARED WOULD HAPPEN FOR SOME TIME NOW HAS, IN FACT, COME TO PASS! THE UNITED STATES IS NOW A NET DEBTOR NATION.

ALTHOUGH AS RECENTLY AS 1983, U.S. CITIZENS HAD MORE THAN $100 BILLION MORE MONEY INVESTED ABROAD THAN FOREIGNERS HAD INVESTED IN THIS COUNTRY, THE HUGE TRADE DEFICITS HAVE WIPED OUT THIS POSITIVE POSITION.

MR. CHAIRMAN, THE UNITED STATES POSTED AN UNPRECEDENTED \$123 BILLION MERCHANDISE TRADE DEFICIT DURING 1984 AND IT IS WORSENING. DURING THE SECOND QUARTER OF THIS YEAR, THE MERCHANDISE TRADE DEFICIT ROSE \$3.5 BILLION TO A RECORD \$33 BILLION. IT IS PROJECTED THAT, BY THE END OF THIS YEAR, THE TRADE DEFICIT WILL EXCEED \$150 BILLION.

DURING THE MONTH OF AUGUST, I HELD HEARINGS ON INTERNATIONAL TRADE IN MY HOME STATE OF NEW YORK. I WAS DISMAYED AND ANGRY AT THE TESTIMONY I HEARD FROM BOTH FEDERAL OFFICIALS AND BUSINESSMEN. IN UTTER FRUSTRATION, THEY DESCRIBED THEIR LACK OF ACCESS TO FOREIGN MARKETS, AND THE UNFAIR AND ILLEGAL TRADE PRACTICES THAT MANY OF OUR TRADING PARTNERS USE AGAINST US.

ONE WITNESS, WHOSE COMPANY IS A PIONEER IN CERAMICS, DESCRIBED THE RUN AROUND THAT U.S. COMPANIES ARE GIVEN IN TRYING TO OBTAIN A PATENT IN JAPAN. VERY BRIEFLY, THE LIFE OF A JAPANESE PATENT CANNOT EXTEND FOR MORE THAN 20 YEARS FROM THE DATE OF ORIGINAL FILING, <u>NOT</u> FROM THE DATE OF APPROVAL OF THE PATENT. THE INITIAL APPLICATION PROCESS TAKES BETWEEN 5 - 7 YEARS, THE OPPOSITION PROCESS CAN TAKE ANOTHER 5 YEARS, AND REVOCATION PROCEEDINGS CAN CUT THE LIFE OF A PATENT BY AN ADDITIONAL 9 YEARS. THIS MEANS THAT THE POSSIBLE 20 YEAR

PATENT TERM CAN EXPIRE BEFORE A U.S. APPLICANT EVEN HAS AN ENFORCEABLE PATENT.

DURING THE TIME THAT A U.S. COMPANY IS TRYING TO OBTAIN AN ENFORCEABLE JAPANESE PATENT, JAPANESE FIRMS HAVE THE OPPORTUNITY TO COPY THE COMPANY'S PRODUCT. THESE COPIES ARE THEN SOLD, NOT ONLY IN JAPAN, BUT ALSO IN THE U.S. MARKET WHERE THEY COMPETE DIRECTLY WITH THE U.S. PATENT HOLDER'S PRODUCTS.

THE UNITED STATES HAS BECOME A VICTIM OF A ONE-WAY POLICY OF FREE TRADE. WHILE OTHER COUNTRIES ENJOY EASY ACCESS TO OUR MARKETPLACE, U.S. BUSINESSES ARE DENIED THE SLIGHTEST OPPORTUNITY TO ENTER THEIR MARKETS. OBVIOUSLY, NOT ALL OF OUR TRADING PARTNERS ARE PLAYING BY THE SAME RULES AS WE ARE.

MR. CHAIRMAN, THESE UNFAIR TRADE PRACTICES AND THE HIGH VALUE OF THE U.S. DOLLAR CONTRIBUTE TO THE GROWING TRADE DEFICIT AND THE BLEAK AUGUST TRADE FIGURES. I BELIEVE THAT THE U.S. MUST TAKE DECISIVE ACTION TO ENCOURAGE OUR TRADING PARTNERS TO HONOR THEIR TRADE OBLIGATIONS BY DEMANDING RECIPROCAL ACCESS TO FOREIGN MARKETS FOR ALL NATION'S GOODS -- BEGINNING WITH OUR OWN. WE, ALSO MUST SEE TO IT THAT OUR TECHNOLOGY IS PROTECTED, BOTH IN THE UNITED STATES AND IN FOREIGN MARKETS. I AM CONFIDENT THAT THESE ACTIONS WOULD BEGIN TO BRING A REDUCTION IN OUR TRADING ACCOUNT; OUR ECONOMIC SURVIVAL DEPENDS UPON IT.

THANK YOU, MR. CHAIRMAN.

Representative OBEY. Mr. Secretary, why don't you proceed with your statement.

STATEMENT OF HON. MALCOLM BALDRIGE, SECRETARY OF COMMERCE

Secretary BALDRIGE. Thank you, Mr. Chairman.

I appreciate being called a straight shooter. It all depends on what target you aiming for, I guess.

But today we are talking about, among other things, the merchandise trade deficit for the year. Today it is $91.2 billion, about 9 percent greater than for the same period last year.

However, the merchandise trade deficit in August was $9.9 billion. That is $1.7 billion less than that average for the first 7 months of 1985.

Exports were about 3 percent less in August than the average for the first 7 months of 1985. Imports were about 8 percent less.

These figures are simply one more indication of a trend that should concern us all. As this committee will appreciate, they reflect the erosion of our trading position worldwide. They confirm that the United States continues to buy more than it sells abroad.

In addition, we are becoming increasingly dependent on heavy foreign capital inflows to sustain and finance our economy. This is a problem that must be resolved if this country is to continue to grow and prosper.

Earlier this week, Mr. Chairman, the President announced his trade policy plan of action. I can't think of one element—short of establishing tariffs and quotas, which we don't want to do—that wasn't included in that statement.

It is a plan to open markets, not to close markets. Obviously, the President has continually stated and continues to stand for free trade.

Free trade produces more jobs. It is more productive use of our Nation's resources, more rapid innovation, and a higher standard of living for our citizens.

It advances our national security interests by strengthening the economic and political systems of our allies.

Since World War II, this country has benefited from free trade more than any other nation, and we have made significnat progress in developing an open, worldwide trading system. This system has been principally responsible for the development of the postwar economies of all of our major trading partners. The President is committed to maintaining this system.

Second, the President is for fair trade. Trade just can't be free if it is not fair. Fair trade, based on mutually accepted rules, is essential if we are going to have free trade on a global basis, and without fair trade, we would lose our constituency for free trade.

In our actions announced this week, as well as those announced previously, the President had demonstrated his resolve to take vigorous against trading practices that deny U.S. businesses the opportunity to compete freely and fairly in world markets.

This President has taken the unprecedented action of using section 301 of the 1974 Trade Act to address unfair practices. Section 301 is the most powerful trade law we have, and while the President will use it with restraint, our trading partners must also understand that we are prepared to use section 301 wherever necessary to ensure fair trade opportunities for our industries.

They must also understand, as the President does, that to pry open foreign markets we may have to threaten to actually close ours.

Our policy is to support open markets here and abroad, and to do everything in our power to eliminate unfair obstacles imposed by other governments. We are going to be more aggressive in assuring and insisting that our trading partners play by internationally accepted rules.

Restricted markets and subsidized production are protectionist measures by which governments intrude on free trade for their own parochial benefit—but that benefit is a short-term gain and a long-term loser.

The President's plan contains other elements that I think are very important: a $300 million fund which can be employed to suppport up to $1 billion in mixed credits to offset unfair foreign competition.

The intent is to discourage our trading partners from seeking unfair advantage by using predatory credits to subsidize their exports. We will use this fund wherever we need to assure fair export opportunities for our demestic industries, while doing our best to negotiate an end to this practice by our trading partners.

We will increase efforts to protect U.S.-generated intellectual property rights worldwide. The Congress recognized the importance of intellectual property by giving us the authority to consider this in connection with the GSP, and made it clear that recognition and protection of intellectual property rights should be an important goal in our trade negotiations with other countries. Since the international competitiveness increasingly depends on the protection of intellectual property, it is critical that we make significant and immediate progress in this area.

The President has outlined a number of new steps we will take to improve protection for process patents and strengthen our laws dealing with imports that infringe on domestic patent rights.

We are going to seek aggressively the removal of foreign barriers to U.S. trade in goods and services in high-technology industries—we have as significant competitive advantage in this area—as well as barriers to U.S. direct investment abroad.

The President will name a strike force to seek out unfair practices across the board.

In addition to vigorously asserting our trading rights, we are going to be stepping up our efforts to start a new round of trade talks. We want to strengthen international discipline and extend it to new areas where our competitive advantage is being undermined by the lack of agreed-upon rules.

At the same time, we will look at bilateral and plurilateral trade talks where these appear advantageous.

We are going to promote exports aggressively in every way we can. We will look very carefully at extending the benefits of the Foreign Sales Corporation, which replaced DISC, to exports of services.

We will seek to clarify the Foreign Corrupt Practices Act so that its objectives can be achieved without losing export opportunities.

We are going to work harder with the States in their efforts to promote exports.

And in addition—and in my view this is particularly significant—we are going to take cooperative action with the other major industrial countries to strengthen their currencies relative to the dollar and to foster growth in our export markets.

We saw this effort begin Sunday, when Secretary Baker met with a group of his counterparts and Chairman Volcker. A lower dollar is one of the major essentials to produce a lower trade deficit.

Finally, Mr. Chairman, this administration has reiterated its commitment to reducing Federal budgets and for tax reform. There is no question that a significant basis for the current high value of the dollar has been our mounting Federal deficits, and the high dollar is, of course, the major contributor to our trade deficit.

I have made this point in other committees and with many of you individually, but I have to make it one more time.

Budget deficits on the order of what we are now seeing cannot be sustained. They must be reduced if we are going to get our economy in shape, reduce our trade deficits, and remain competitive with our trading partners.

Mr. Chairman, we have to consider the trade implications of everything we do as a government, whether our actions will hinder or enhance the ability of our industries to compete, and we have to afford our industries the ability to compete in the world market without one hand tied behind their back.

For example, one issue that the President has promised to look at carefully is reforming our antitrust laws to permit U.S. industries to adjust to compete more effectively in the global marketplace. We have been slow to recognize the rate at which the American economy has been integrated into the world economy, and it is clear that our antitrust laws, designed to prevent anticompetitive practices in an isolated domestic market, should now receive careful scrutiny if our major industries are going to go up against those of our most aggressive and sophisticated trading partners.

I am also going to ask the President to look carefully at amending section 201 of the 1974 Trade Act to offer limited antitrust exemption to industries that are injured as a result of imports. Such an alternative remedy may help such industries adjust, restructure and adjust to new economic circumstances and is less protectionist than the remedies presently available under section 201.

Mr. Chairman, this Congress may represent a turning point in the way the United States views its obligations toward the free world and our trading partners around the globe. With imports growing more rapidly than exports, and a growing trade deficit, we are faced with an almost overwhelming temptation to protect ourselves by erecting barriers to imports.

There is no question that, in certain circumstances, some degree or form of protection may be in the national interest, but we have to recognize the price we pay for protectionism.

Protectionism raises the cost of living for the American consumer and thus lowers our standard of living. This is true of everything from automobiles to textiles to steel. Protectionism will simply shelter some industries in the short term while passing on the expense to the rest of the economy for the short and long term, forcing us to subsidize the jobs of workers in these industries while permitting them to avoid competition.

Our industries are productive and can be competitive. Asking the American consumer to protect these industries from healthy competition is not in our best interest. Instead, we need to work vigorously with our trading partners to ensure that the responsibilities as well as the benefits of an open trading system are equitably shared. We must see our trading partners join us in opening markets to improve the system of trade that has contributed to the growth of our economy and strengthened the national security of both the United States and our allies.

This President is moving forward with a new trade policy to ensure fair trade and open markets, and he is using the tools provided by Congress, section 301 of the 1974 Trade Act, firmly and vigorously to end unfair trading practices.

He has proposed the establishment of a $300 million fund to combat predatory pricing practices.

He will establish a high-level strike force to fight other unfair trading practices.

We are going to vigorously assert our very valuable intellectual property rights and demand their full protection.

We are going to strengthen and revitalize the GATT. We will work for the initiating of a new round, and he will consider proposals to review our antitrust laws and make changes where necessary.

And, finally, the President will work with the Congress to develop any legislation appropriate to reach these objectives.

All of these steps, Mr. Chairman, as well as others, we will be carrying out in the months ahead, and I hope we will have your support.

Thank you very much, sir.

Representative OBEY. Thank you, Mr. Secretary, for your statement.

I know that you have an appointment this morning, so we will try to avoid keeping you too long.

Let me start out by making a few comments of my own. I have tried to be as close as possible to a free trader all my life. I have not, for instance, signed on to the Bentsen-Gephardt-Rostenkowski bill because I have significant questions about it.

But I have to say that I share the frustration which I think these other groups that developed that legislation and some 300 other pieces of legislation must feel. But I guess—since most of your testimony this morning was focused on the President's recent actions, I guess I would like to focus my questions on that as well.

Earlier this year, the President described the overvalued dollar as a foreign vote of confidence in the American economy. In June of this year, your former Under Secretary for International Trade, Lionel Olmer, said in his end-of-the-year report: "If the dollar remains at its present strong levels for another year or two, the erosion that has already started in the breadth and depth of the United States manufacturing base will worsen seriously."

I certainly agree with that statement. The President now seems to be responding to that view and other concerns as well.

I guess my question would be: Why did it take so long for that message from Secretary Olmer and others to have sufficient impact to get some action taken before Congress was so far down the road in stating these other options? Why wasn't action taken 7, 8, or 9 months earlier when people could clearly see this was going to be a significant problem?

Secretary BALDRIGE. First, Mr. Chairman, there really isn't any inconsistency in the President's statement and former Under Secretary Olmer's statement. The President was correct when he said that the strength of the dollar is a vote in the strength of this country—whatever the exact phrasing was.

This is the strongest, most secure country, the best place to invest, and that does strengthen the dollar and it is a vote of confidence.

So that statement, I can't fault that at all.

It is also true that if a strong dollar keeps on for too long a period of time, the comparative strength it has against the rest of the world's countries, it means that our economies are out of line and this will hurt American exporters and bring in more imports.

The fact that we grew our GNP almost 7 percent last year and the European countries were growing at 1.8 or 1.9 percent has a strong effect on that value.

It is hard to answer why any particular decision wasn't made 3 months ago or 10 months ago, but it has been made now.

Secretary Baker's meeting last week I thought was very significant because it meant that the five largest industrialized nations agreed that the fundamentals as they presently exist and the future policy decisions that we are all going to make were not reflected in the various currency bases that affect the four other industrialized nations, who should make every effort in terms of realignment to raise their currencies against the dollar.

So that step has been taken, and another step was taken there that I think is very important. That is the one begun by the President at the Bonn summit, of course, but, following up strongly, is urging our indusrialized trading partners to increase the growth of their GNP.

Representative OBEY. That is one of the things I would like to get at.

Secretary BALDRIGE. More than they have now.

Representative OBEY. Let me ask you. What I am trying to get at is this, Mr. Secretary. I am trying to figure out where we are going to be a year from now. I am trying to figure out how long—given the fact this decision for the administration to take some action was delayed so long, how long is it going to be before we have seen the real action?

What I would like to ask you in specific terms would be this: When we look at the record a year from now and see whether our projections were on or off, or whatever, what would your projections be for the 1985 trade deficit? How big do you think that will wind up being?

Secretary BALDRIGE. That is very hard to be accurate about now, with 2 months to go yet. I think it will be in the $145 to $150 billion range.

Representative OBEY. $145 to $150 billion?

Secretary BALDRIGE. $145 to $150 billion.

Representative OBEY. What do you expect we could reasonably expect for 1986?

Secretary BALDRIGE. You do know how to ask the hard questions, Mr. Chairman. You know, I will give you an answer, but I have to put these caveats around it first.

So much of that depends on what literally happens next year with the growth of other economies outside the United States, how well they do, and that means how many of our exports they accept.

So much of it depends on what happens with what the Congress and the administration finally end up with the budget deficit reduction package next year, how that is going to go, because that will affect the strength of the dollar.

And I can go on and on with the "if's."

After having carefully made those caveats, let me say that if this year's budget, if I am correct, the range of this year's deficit being $145 to $150 billion, without the President's program, without any action by the Congress, we, let's say, went back to a month or two ago, I would have said that next year, 1986, would be $5 to $10 billion higher. You can call that the same range roughly, but I would say it would be higher, on the higher side. We wouldn't know whether it would be $5 or $10 billion.

Now, I think that if we are able to see reasonable action on the budget deficit, and so forth, we should see that trade deficit begin to go down next year. I don't think it will be a tremendous decrease next year because trade flows don't work that quickly, but I think we can see—I have said $145 to $150 billion—but we could see $130 billion, something like that, $135 billion. The trend would be in the right direction.

In closing, just let me say that those trade flows take literally, perhaps, an average of 18 months to 2 years to show up once the dollar has begun to decline.

Representative OBEY. That is precisely why I asked my first question because it seems to me you have indicated that even if the President's program announced last week works in a pluperfect way we are still looking at trade deficits of more than $100 billion for a significant period of time, at least 2, 3, or 4 years, and I think the public needs to know that, and I think the fact that the administration's expectations are that they will continue to be at such a high level will indicate that that isn't going to head off significantly any efforts of the Congress to do something more.

Secretary BALDRIGE. Well, I think the important thing is to get it headed the right way. I think this program absolutely will do that. How fast it goes depends on the growth of other countries around the world, too.

Represetative OBEY. Let's take a look then at that program. As you know, the President's speech refers to accelerating the growth abroad, talks in terms of stable, sound fiscal and monetary policy.

To me, that would appear to be an emphasis upon long-term rather than near-term shifts in macroeconomic policy of other countries. According to press reports, much of the same phrased mission of growth is contained in the appendix to last Sunday's announcement by the G5.

I guess my question would be: What did really get tied down in terms of specific actions on the part of our trading partners to increase their growth? Do we have any specific bottom line figures from any of the countries? If so, what are they? Is there something more here than just simply rhetorical pledges to "do something"?

Secretary BALDRIGE. I think it is definitely more than a rhetorical exercise. Our trading partners want our dollar to go down as much as we. They see the long-term bad consequences to themselves if it doesn't. So we both have the same goal. I mean, I can say this is more than an exercise in rhetoric.

Now, when you are dealing with heads of state as he was at Bonn or finance ministers as was the case last weekend, I don't look on that agreement, from what I have read about it and heard about it from Secretary Baker, as one in any way signed in blood. The financial ministers and their heads of state say they are looking into how they should increase their own GNP by noninflationary means. They all said they would do that.

I don't know if I would describe that as a treaty or anything of that sort, but it is all in their own self-interest. They agree with it, and it is in our self-interest. I think each of them has their own different political problems in getting there and each has different economic problems, but the intent was very clear, Mr. Chairman.

Representative OBEY. I guess my time is almost up on the first round, but let me ask one last question before I turn it over to Senator Wilson.

What I hear you saying—at least what I am concerned that I hear you saying is that we really don't have any commitments tied down.

As you know, the agreements have been characterized by some people—or some people say that if you look at the language it is simply a recitation of what our trading partners say that they are already doing in terms of their own macroeconomic policy.

We have been jawboning the Japanese, the previous administration and this one, for 6 years. If you take a look at what Japan has imported by way of American goods—which is certainly related, not only to its own trade practices but to the growth in their own economy—you see they have imported from us less than they imported a year ago last August.

So isn't it understandable to the administration—and the legislation is now certainly here—that there may be an inclination to get to that bottom line and say we are not going to focus on little practice A, little practice B, or little practice C; what we are trying to look at is what the sum total of all those practices are in terms of your trade imbalance, not just with us but with the rest of the world? And in the absence of any specific tied down agreements to change even macroeconomic policy, isn't it inevitable that you are going to continue to get movement up here for legislation that presses for something more specific than the administration has apparently done?

Secretary BALDRIGE. Well, I know the political pressures and economic pressures are great. There is no question about that, and I have a great deal of sympathy for those.

But bill after bill that I see attempting to address what is seen as the problem ends us up in worse shape than if we hadn't done it. The cure is worse than the ill in the first place.

I think that is what we have to be afraid of in this common search. I think it should be a common search, a joint effort between the administration and Congress, to work out a common policy on this.

I think the President, the administration, has necessary trade laws on the book that act very strongly in this situation, and section 301 is a very strong trade law. But there you have Executive discretion about putting on and taking off various remedies in order to achieve your needs.

It is very difficult for the Congress to put in quotas on anything and ever get them off again, even if the other country responded by opening the markets. In the meantime, we will see a rise in worldwide protectionism.

If I have another minute, Mr. Chairman, I would like to make a point.

I am not so worried as some are about direct, angry retaliation against some of these protectionist bills by other countries, where the other country would get—the politicians would get angry and in that spirit say, well, we will go out and do something to really try to hurt the United States. I worry much more about the slippery slope toward worldwide protectionism.

Just let me give one example.

In Western Europe, where they have the parliamentary form of government for the most part, where literally the prime minister could be thrown out tomorrow morning if he can't get a vote of confidence, there is tremendous pressure for protectionism. I have seen that in my travels there all the time.

But they have been able to resist most of it because of the leadership the United States has given. It has been the beacon that has enabled them to say no. If we went down this road and the United States is still for free trade, there would probably be some action taken against us, or it wouldn't work out right.

But anyway, if we passed a major protectionist bill, I think the political pressures, begining in Europe, would be almost impossible for them to overcome.

Why do you resist this kind of a bill now, Mr. Minister, when the United States has already started?

And that gets us into a growing worldwide situation that is going to end up with very bad results for the developing countries, their ability to export, and it takes the whole economic pie worldwide.

Protectionism does and says it is not going to grow; let's just slice up each part and argue over that. And unless we embark on economic ideas that will make the whole pie grow without protectionism, we will end up in much worse shape than we are now.

Representative OBEY. Mr. Secretary, I understand. That's the same speech I've been giving for years, but my concern, and let me summarize it before I turn it over to Senator Wilson.

The hearing this morning is to look at the trade numbers for August. In your statement, you've laid out what the President has done, and you've characterized it as seriously what you think to be very comprehensive and effective steps, yet what I'm trying to find out is—beyond this $300 million, what I'm trying to find out is, in terms of the things you say have happened, we haven't even got into our own debt situation, but in terms of growth that has to take place in other countries, and other macroeconomic changes that have to take place, what I'm looking for is if, in fact, that's correct, what did come out of that agreement last week.

I'm not blaming you for it. It wasn't your agreement, but I'm looking for specifics and so are a lot of other people in this town, not just in Congress, but in the press, in business, are looking for specifics to indicate that there was something more here than simply an effort to head off Congress' doing something.

And for the life of me, I'd like to find something that's usable here. That's my concern.

Secretary BALDRIGE. I think the most dramatic change to come from that meeting was the clear agreement by the five leading industrial countries to agree in recognizing the fact that the fundamentals support different realigned currencies in an agreement to cooperate. That's a different policy than we and the other ministers of the other countries involved had before. I think that's a change that's specific and serious and a very good change.

The other major part coming up was on economic stimulation by noninflationary means.

As I say, you'll have to ask Secretary Baker or Paul Volcker how that was actually couched, but I think it's a further, stronger reaffirmation, when the subject came up of the Bonn summit meeting.

Representative OBEY. Senator Wilson.

Senator WILSON. Thank you very much, Mr. Chairman. And thank you, Mr. Secretary.

I first want to commend you, Mr. Chairman, for the idea of holding hearings on these statistics to afford us the opportunity to keep a more or less constant tab on a subject that's clearly going to occupy both the executive and congressional branches.

Mr. Secretary, reading your testimony, I find one particular statement that I have to agree with very strongly. In your statement, you say:

> We have to recognize the price we pay for protectionism. Protectionism raises the cost of living for the American consumer and thus lowers our standard of living. This is true of everything from autombiles to textiles to steel. Protectionism will simply shelter some industries for the short term while passing on the expenses to the rest of the economy for the short and long term, forcing us to subsidize jobs of workers in these industries, while permitting them to avoid competition.

I agree with that statement.

My concern has to do with the fact that the administration's overall trade position, while consistent with your announced position here, in one instance indirectly works exactly the other way in certain cases. One of these is—this is not a surprise to you, and it's a problem to which you've directed attention, for which I'm grateful—with respect to the steel industry.

You and other members of the Cabinet have made your position clear with respect to textiles and the impact of that kind of protectionism. The protectionism that is being sought is just exactly, I think, what you state: the impact is substantial and harmful. But in the case of the steel user—and this is a western regional problem in the United States, where the fabricators of steel products are in need of basic steel—the impact of the President's steel program indirectly achieves the kind of harm you are talking about.

With consumer goods, like shoes and textiles, the impact is obvious. But with the restraints on steel, the effects may be less direct and less obvious, but the effect on the ultimate consumer, I think, is convincing.

In the response that you have made to steel users, you have sought to assist them as you could, but what I'll ask is that you revisit that problem in the context of your statement here. You know what has happened here is that those, for example, who seek to make the kind of products that depend upon a supply of wire rods are finding that they simply can't get it. The response that you made to some that you think they are unwilling to pay a fair price for it.

But what I think we have in this country is a problem of real unavailability, at least in the economic sense, because the eastern mills that will provide the basic steel—there are not many mills in the west that are capable of doing that—encounter a cost barrier in the form of transportation across the United States that make the imports not just cheaper, but significantly cheaper. And so, there is a basic problem of supply.

If the purpose of the President's steel program is to save the steel industry, must we not take account of the fact that, as the former U.S. Trade Representative, now Secretary of Labor, Brock indicated when he was testifying against the Heinz legislation, the Fair Trade in Steel Act, that you must bear in mind there are 20 times as many people employed in the United States fabricating steel products from basic steel as are employed in the production of basic steel?

Now my question to you is, don't you think that we are engaging in protectionism with respect to the basic steel industry in a way that is inevitably going to have consumer repercussions of the kind that you're seeking to avoid in your clear statement here?

Secretary BALDRIGE. Yes; I think it's a case of the least and worse alternatives, as bad as that image is, that you get faced with in some of these cases. There are 150 to 200 million tons of excess steel capacity in this world now. That has provoked a situation where so many developing countries have jumped into the steel business as a matter of national pride. Steel is just overbuilt. At the same time, other materials have taken part of their market. Everybody is lightening up their end product. Those have had a tremendous effect on the steel market.

Now with all that as background, we ran into the situation where, by far the majority of countries involved were subsidizing their steel. I forget how many countries now, but there must be 30 or 40 at least involved in subsidizing steel exports to the United States. That was the situation we were facing, when our alternative was either to shut all those people out by use of the subsidy law, in some cases dumping, or with agreement on both sides that the steel industry itself was being injured, that we're going to negotiate a settlement on restraint of shipments.

That's what I call the least worst alternative, and nothing is perfect, because, like any form of protectionism, it has its prices too. If we were to allow another 650,000 tons of wire rod into this country, that's almost double—they'd like to get it from Mexico, but that's almost double the Mexican arrangement. We have checked on this very carefully. There's no doubt in our mind that if we did that, allowed that in, that those subsidy cases would immediately be instituted on wire rod. The fact is, that there were such shipments into this country. And I understand Davis-Walker's position. We spent hours working with them trying to see if there wasn't some way that we could try to ameliorate their situation. Unfortunately, there wasn't, and I finally had to say, unless you wanted to do away with the whole system of import restraints we have now, that there was a way to acquiesce to the Davis-Walkers.

They can and do have the ability, and there is the capacity, to buy wire rod in this country. It's at a higher price than they pay by buying subsidized import rod. There's no question about that, but in a way, that's what the steel agreement stands for.

Senator WILSON. I would only ask that you closely monitor the situation. I had hoped that they could buy steel in this country. But they cannot. And, without foreign steel, I think what is going to happen is that they're simply going to have to curtail production, in which case no one would have benefited. So I think that's going to require some ongoing attention.

Since you have focused on the subject of subsidies, let me talk about another unfair activity practiced against us by our trading partners. I recently took part in hearings held by the Senate Foreign Relations Committee on the agreement entered into by the United States and Japan affecting civil air service.

In those hearings, it was apparent that the new Japanese competitor, the freight carrier Nippon Cargo Airways, is the child of a vertically and horizontally integrated and very collusive effort by Japanese firms, who are being encouraged, by the way, by the Japanese Government. If you look at the ownership of this new entity, Nippon Cargo Airways, by freight forwarders, shippers, trucking companies, and others, it would be flatly in violation of U.S. antitrust laws.

When we pressed some of the representatives of the agencies who have entered into this agreement on behalf of the United States, one of them made the response to me, as I expressed some outrage, he said, "Well, we can't, of course, enforce our laws on the Japanese." That struck me as a rather glib oversimplication to begin with, but it totally ignores the fact that we are at least entitled to call for the Japanese to enforce their own laws.

Nor one of the things that it seems not many people understand is that the Japanese have on their books equivalents of the Clayton and Sherman antitrust laws that are a legacy of General MacArthur. They have an FTC Act, but unfortunately, the Japanese Fair Trade Commission, which is their enforcement agency, is a real weak sister, while MITI is encouraging these collusive activities.

Recently, I participated in a congressional delegation visiting the Far East. Most of our time and effort was focused upon Japan, but

I must say that I came away with the feeling, while Premier Nakasone understands the problem and is making genuine efforts to change, his ministers do not, and they're not going to change. In particular, they seem quite clear in their intent to go ahead, not only with this new air carrier, but with any number of other companies such as semiconductor manufacturers.

I must say that I think it of passing strangeness that while we have 55 percent of the world's semiconductor chip market, we have had for the last 20 years, a flat 11 percent of the Japanese market. They're just ignoring this antitrust aspect.

In your judgment, is there not some way that we can press the Japanese to more forcefully enforce their own antitrust laws? I am not aware that we have done so in the past, and I think that is a dereliction on our part.

Secretary BALDRIGE. Well, as you know, the aviation protocols between countries, the negotiations are handled by the State Department. And the Transportation Department, Commerce, all the other interagency groups, participate in that process. I think what we're facing out here in this particular case you mentioned, is a difference in the method that the Japanese and the United States look at their antitrust laws. And I would say that more countries around the world probably are more similar to the Japanese approach than to the United States approach.

We still, in our antitrust laws, have and should have, in my opinion, Sherman, unchanged since 1915. It is the bedrock of our antitrust laws. Clayton, where the language is so vague that most proposed mergers that are talked about—I won't say most, but too many of them, never get out of the chute. People are afraid of the way, the haziness of that Clayton law, where it says if a merger might tend to, in quotation marks, or might 10 years down the road involve a potential dividing of markets or prices. Companies just aren't willing to do that here.

We ought to renew those laws. We are going to. In my opinion, Clayton 7 is not good law in today's international global competition. Other companies in other countries around the world do not believe that big is bad and do not believe, as we do, on those mergers. So it's perfectly natural for most countries to allow their companies to merge, to get together for export purposes. We had some very difficult negotiations with the Japanese on this opening up of their markets. It did end up with our getting more access, as they did to our markets. We left out, in the case of the freight carriers, the whole hub of Chicago.

It's true that the Japanese can get into other hubs. We thought, as an administration, that that was a fair trade offer. Any ideas on moves by the United States in our market, I think should be watched very closely. I think the present agreement, however, is at least reasonable.

Senator WILSON. Mr. Secretary, I had used that particular example. But let me say that I think there are widespread examples of this kind of thing. And the Japanese response is to say, well, we really should be exonerated from blame in that because we don't direct our industries. That's utter nonsense. That's like saying that we wouldn't blame the Department of Justice if Ford and GM were to undertake a merger, and we simply said, you know, we have a hand's-off policy. There is no enforcement.

Secretary BALDRIGE. Let's just take that case. Maybe we should have a hand's-off policy, in view of the fact that we are in an international global market now. Our companies are not involved in a struggle just for domestic supremacy, and domestic companies' share of the market, compared to other domestic companies should not be the overriding factor it has been in the past. We are in a global market with global companies struggling all over the world, and if we handicap our people by not allowing them to merge when other countries allow theirs to merge, we're going to see other countries get larger entities, more money for research and development, more money for marketing development, and we will suffer as a result.

Senator WILSON. Well, I will tell you this, I think that whatever the policy may be on a particular merger, unless you're going to totally throw the doctrine out the window, and unless the administration policy is to not enforce any antitrust laws, then I think that you're inescapably in the situation where, if you are going to continue to honor the legislation that's on our books and not change it, we are entitled to look at Japan, who has almost identical legislation, because it was taken virtually word for word, and ask why it is that they are not going to enforce it. We are simply playing by different rules here.

Your response has been that perhaps we ought to change our own laws. Maybe we should but not on as broad a front, I think, as your answer might indicate.

Secretary BALDRIGE. I'm sorry if I left the impression that I thought we ought to change our whole antitrust law. I didn't. I was careful to say earlier, I was very much in the favor of the administration reviewing them, and where there are roadblocks to our being internationally competitive, they should be removed. Nobody's talking about Sherman. We're talking about the vagueness of Clayton or possibly taking a look at Robinson-Patman. Under 201, for instance, under "Injury," where the President now has the final decision where you give protection or you don't give protection. It's either one or the other. Maybe those companies should be allowed to restructure, but not for a 5-year period, without being bound by the antitrust laws in the express industry.

Those are the kinds of things we are talking about, but I think we ought to look at the whole antitrust problem—and here's my only point—in the light of today's world and the competition around the world, and what other countries are actually doing, for us to go over and try to have them enforce their own antitrust laws, when they have a different reading than we do, I will promise you is a most difficult task, and I'm not sure how well we'd do it.

Senator WILSON. Well, all right. I'll only suggest to you that we should, in fact, play by the same rules with the same laws. That is simply a case of nonenforcement. I don't think we've been nearly tough enough in applying pressure on them to play by the same rules, to enforce the same laws.

Secretary BALDRIGE. I certainly agree with you, Senator. We should try. It's just that our track record in that has not been very good.

Senator WILSON. Thank you, Mr. Chairman.

Representative OBEY. Thank you, Senator.

Mr. Secretary, let me try to get back to exactly what we have right now by way of specific, concrete, nonrhetorical agreements, not only with our trading partners, but in our own peculiar system of government, as it relates to the Fed.

I know this isn't directly your responsibility, obviously, but can you tell me—two questions—how much do you think that this coordinated intervention will bring down the dollar from its current level, will accomplish? How much do you think we could reasonably expect to see the dollar decline, as a result of the agreement for the coordinated intervention? And along with that, let me ask you, is there a specific agreement tied down to the Fed, so that, in fact, there will not be any offset of any effort to bring the dollar down by Fed action in a different direction?

Secretary BALDRIGE. One would have to be a lot smarter than I am to be able to predict accurately how much the dollar would fall, as a result of last week's meeting. I think it is clear that there is resolve on the part of the largest five industrial nations to cooperate toward a realignment. I don't know how successful that would be. I would say that downward pressures on the dollar now must be more than the upward pressures. In other words, pressure going in both directions. I think we'd all expect—I think it's reasonable to expect—a further drop. I couldn't estimate what it would be. I know that a good many manufacturers have estimated to me that it would take a drop of about 25 percent in the dollar for them to be competitive in the world market. We don't have any exact figures on that, but that's the feeling of most of the industrialists, whether it will get there or not, I couldn't say.

I think the other part of your question was, will the Fed accommodate that kind of a drop, if I'm stating it correctly, or a continuing fall in the dollar. Obviously, that depends on a lot of things. I think we could all answer that question with more surety, if we were positive that very strong steps are going to be taken to reduce the budget deficit.

Representative OBEY. That's something which you can both talk about till the cows come home, and given the fact that the farm bill is on the floor right now, for instance, but my specific question is, in terms of the agreement reached last week, are we assured that the Fed, in fact, agrees with what happened, or that they are tied down, and that you won't see the Fed, in fact, tightening money supplies to take into account or offset any effect of exchange market intervention, for instance?

We assume that that is the case. Are we sure that it's the case? Maybe I shouldn't assume it's the case. I don't know.

Secretary BALDRIGE. I don't know either. I think the Fed, so far, has certainly seemed to be moving in that direction, to be positive about the whole meeting last week, but I can't guess what future Fed policy would be.

Representative OBEY. Let me just ask, you indicated what the President's package is. My question is, Is there any part of our trade deficit, as you see it, that is related or due to a lack of growth in controlled activity on the part of our own manufacturing sector?

Secretary BALDRIGE. Yes. We're seeing a comeback now, after a period of, I think, two decades, where we lost our leadership, productivity increases, quality control, and items of that nature that are necessary to be competitive worldwide. We have lost, I think, as I mentioned before, through some of the applications, guidelines and the antitrust laws, the ability for companies to get together that would really enhance that competition.

I don't think the example Senator Wilson used of GM and Ford was a practical example. I don't think anyone would want to see them get together under our antitrust laws, but there are a lot of medium-sized companies or larger companies with smaller ones that could enhance productivity and competitiveness that way. I think that American management now, overall, completely understands the necessity to get back our quality lead that we used to have in the 1950's and began to slip in the 1960's and 1970's.

Representative OBEY. Excuse me for interrupting, but I know you have to leave, and I don't want to have you miss your appointment. I have three more questions. So I'll try to keep it short, if you'll try to keep the response short.

I understand that, and I've seen you quoted on occasion, including your very specific concerns about productivity.

I guess my question as it relates to the trade issue and as it relates to whatever agreement or whatever policy the President has now announced, would be this. Is that a significant question, then let me ask you, what is there in the President's package that would respond to, for instance, his own Commission on Global Competition, the Young Commission, which indicated in January, when the issue was before it, that we need to have more attention paid to increased training, to increased trade adjustment, increased education, things like that.

Is there anything in the administration's plan that is responsive to those aspects of this report? If there isn't, to your knowledge, is there anything that we might be expecting the administration to produce in the future along those lines?

Secretary BALDRIGE. The administration is reviewing trade adjustment assistance now at the interagency level. So I can't say what will come out of that review that the President might decide to follow through on, but we see increases in research expenditures by the United States Government in the field of basic research that are quite sensible. We see the R&D tax credits, which first came through in 1981 and are in the present Presidential package here to encourage the use of research and development. The administration took the initiative in the joint venture on research and development law, the National Cooperative Research Act, on joint ventures in R&D and export trading companies, where you get together for export abroad.

I think all of those are big steps in competitiveness, because that does have to start with the innovation of new products and new techniques that come essentially to the question in basic research.

Representative OBEY. I must say that that doesn't address itself to the question of what we are going to do to sufficiently train our society and educate the work force in society for the kind of economic changes we expect.

Secretary BALDRIGE. That's far better done, in our opinion, by the private sector, and it's being done.

Representative OBEY. I would agree with that, but I would point out that I think this report made it quite clear that there was a role for everybody to play, and I don't see a significant role being played by the Government.

But let me ask my bottom-line question now on our own deficit, because I think you've indicated that we aren't going to make much progress on the trade deficit, until we deal with our own budget deficit. We have now what appears to be round 2 in the round robin, and we have a tax package moving through the Ways and Means Committee, for which I have minimum high regard, to put it kindly.

I guess my question is this. If it is true that we need more macroeconomic policies changes from other countries, we don't know if we have anything tied down in the agreement at present that we talked about last week. If it is true that our best way of demonstrating the need for other countries to change their macroeconomic policies is that we change our own, then I have a question on the tax bill.

You indicated in your statement that as part of your listing of what the President's program has done, you say, "The administration has reiterated its commitment to reducing the Federal budget deficit and for tax reform."

My problem is, that when you look at that tax reform bill, if you stretch your imagination, it may be revenue neutral for the first 5 years or so. Beyond that, there are substantial questions as to whether, in fact, it isn't a revenue loser or won't be by the time he's finished with it, and there are a lot of people up on the Hill who feel that instead of continuing to dance around the question of how we're going to give people another rate reduction. A lot of people feel, if we really want to do something about trade, if we want to avoid making the mistake of the kind of protectionist legislation you're talking about, that we would be far better to take whatever revenues are raised from a base broadening and use them, not to give people another round of tax cuts, which might be nice, but which we think we can't afford to give, and simply apply whatever is raised through base broadening for straight deficit reduction.

Wouldn't that be the most immediate way that we could get action quickly, given the fact that a big defense budget seems to be off the table, Social Security seems to be off the table, and we're not sure what's tied down on the monetary side?

Secretary BALDRIGE. Obviously, I support the administration's position on tax reform. I do think it's necessary. I see more businessmen for this bill than are against it. I see a predominance for it.

Representative OBEY. But in terms of the trade deficit—you mentioned doing something on the trade deficit. Wouldn't we do something more directly to eliminate our budget deficit or to reduce our deficit and have a positive impact on our trade deficit, as a remedy for deficit reductions?

Secretary BALDRIGE. If we tried to do that by raising taxes——

Representative OBEY. I'm not talking about raising tax rates, I'm talking about whatever revenues are picked up by closing some of the anomalies that everyone agrees ought to be closed.

Secretary BALDRIGE. The revenues you pick up that way, either you reduce taxes, or in your view, put it against the budget deficit. Well, I think we'd get more bang for the buck by reducing individual rates. What we're trying to do here is stimulate not just normal consumption, we're trying to stimulate investment. I think everything we do to reduce that budget deficit that lets government spending reductions off the hook, doesn't make long-range sense. We're in this boat because spending has increased, not because the tax base has decreased.

Representative OBEY. With all due respect, that's not correct. If you look at the baseline from 1980, it has increased by almost 2 percent of GNP. And the overall base has declined as a percentage of GNP. So we're in this boat, because we've gone up on both sides of the ledger.

Secretary BALDRIGE. Yes, sir, but when you go back to the last two times that the budget was anywhere near balanced, one of them was when John Kennedy was President and one of them was in the early 1970's I forget the exact year.

Representative OBEY. President Johnson's last year.

Secretary BALDRIGE. Both those times, government revenue was about 19 percent of the GNP and expenditures were 19 to 20 percent. Now we still have today, under this bill, if I remember the figures correctly, 19 percent revenues coming into the United States from taxes and spending is up at 24-25 percent.

Representative OBEY. Mr. Secretary, let me simply respond and turn the mike over to Senator Wilson. I guess that really centralizes the bigger problem, because we're told the administration has an itemized package to deal with the trade deficit, that it's comprehensive. We're told that it needs supplementing by further reduction in our own deficit, but we haven't seen much that's tied down by way of specifics that other countries are supposed to meet by way of changes in their budget policies.

We don't know what the Feds are going to do. We're told, in effect, well, yes, we ought to reduce the deficit, but only if we can do it a certain way. To me, what that translates to is a lack of political will to really get at the deficit problem. I mean, I agree with currency alignment. I agree with some of these other things, but it seems to me they're all nibbling around the edges. Unless we're willing to go for it, and we keep finding ways that we're not going to go for it. That seems to be a prescription. It's a guarantee that that trade deficit we're talking about is going to stay up there, and that's a guarantee our budget deficit is going to stay up there in the triple digit range.

Secretary BALDRIGE. Mr. Chairman, do I have time to make just a short comment on that?

Representative OBEY. Surely.

Secretary BALDRIGE. The present program as concerns the effect on the trade deficit, it's like turning the *Queen Mary* around. The President's program will turn that ship around and start it in the other direction. It will take, because of the normal amount of time that it takes for trade flows, services will benefit first and manufactured goods later. It will take some time to turn that around. That's why you can't guarantee astounding results in the first year. Three, four, or five years down the road, we'll be a lot better off with a lower deficit than we are now.

On the other hand, if we went the protectionist route, the first effect would be to strengthen the dollar, which would put us back in the soup.

Representative OBEY. Excuse me. My point is, I don't see the administration doing a lot, except a quickie media event. I honestly don't think the administration is doing a lot to avoid having what you're concerned is going to happen—to prevent that from happening out there where you're concerned it's going to happen.

I'm looking beyond the pronouncements. What are we really going to do?

Secretary BALDRIGE. I'd be glad to listen to any suggestions. I thought this policy was an excellent one.

Representative OBEY. Senator Wilson.

Senator WILSON. Mr. Secretary, a quick question about the relationship between taxation and productivity that you're concerned about. In his report which he submitted earlier this year, John Young, chairman of the President's Task Force on Competitiveness, made the point that there appears to be a very distinct correlation between the taxation of consumption rather than earnings, which is the hallmark of the tax structure of our Japanese and West European allies and competitors. In those countries there is a much higher rate of savings and a higher rate of investment and higher rate of plant modernization, and in many industries, by no means all, but many, a higher rate of productivity and competitiveness than we have achieved, and there is a correlation there that many people think is valid.

On the Federal level, we tax earnings in this country. We tax consumption at the State level and the local level. Has it occurred to anyone in the administration that a revenue neutral tax shift from earnings to consumption might well result in the same kind of correlation here?

Secretary BALDRIGE. Well, Senator, this tax bill was debated at some length inside the administration. I think every viewpoint, certainly the ones that you brought up, has been brought up and considered. It's like any other piece of legislation. I agreed with most of it. Some of it, I didn't but in totality, it's a bill that I most definitely strongly support.

My fear about the tax bill is that if it gets into Congress and begins to be changed substantially, I would certainly have to oppose any large movement toward giving some kind of breaks elsewhere, and then having the business somehow pay for it, but business is the job creation agency of this country, and if they're not doing well, we're not going to have a good program.

Senator WILSON. Well, I think a tax on consumption just like all corporate taxes, would ultimately be paid by consumers. Let me ask your opinion, not in the context of the President's tax proposal, but simply in terms of what you think its impact would be on our export programs, if there were a value-added tax, which, of course, is added to purchases of imports and rebatable on exports. What effect do you think that would have?

Secretary BALDRIGE. It would have a plus. The Europeans use that system, as you know. They tax various steps in the value added process. Then if it's for export, they will rebate to the manufacturer. I think it averages as high as 12 or 14 percent. It's a significant incentive to export. It's legal under the GATT. We had to go through a lot of work to get our present DISC, but it's legal under the GATT. So it's worked, as far as encouraging exports. There's no question about it.

Senator WILSON. The administration has not embraced that as one of the means by which we might deal with our own trade deficit.

Secretary BALDRIGE. I haven't seen the administration embrace any kind of tax increase.

Representative OBEY. This wouldn't have to be a tax increase. It could be a tax shift, revenue neutral.

Secretary BALDRIGE. Well, we haven't backed it.

Senator WILSON. Thank you, Mr. Secretary. I know that we've kept you.

Representative OBEY. Thank you, Mr. Secretary.

I would urge you, just as one representative of the administration, to please take another look at the trade situation and the possibility of using some of the revenues that might be picked up from base broadening toward a straight deficit reduction rather than a rate reduction, because you indicated you don't want to raise rates, but the fact is that package does, and it would be a mistake. It eliminates the State and local tax reduction. And given the other rate levels in the administration's buildup, a lot of people in my State are going to be paying more taxes.

So that means you get the worst of both worlds—a tax increase and no reduction in the deficit. That's not just bad for my people but bad for the country.

I thank you for appearing here very much. We appreciate it.

Secretary BALDRIGE. Thank you for the opportunity. I appreciate it.

[Whereupon, at 11 a.m., the committee adjourned, subject to the call of the Chair.]

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