Comments Regarding Causes of Significant Trade Deficits for 2016
Docket No. DOC-2017-0003

Submitted by Business Roundtable
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INTRODUCTION

Business Roundtable is an association of chief executive officers of leading U.S. companies working to promote sound public policy and a thriving U.S. economy. Business Roundtable members lead companies that employ nearly 15 million people and produce more than $6 trillion in annual revenues. Comprising roughly one-quarter of total U.S. stock market capitalization, these companies invest more than $100 billion annually in research and development, equal to 30 percent of private U.S. research and development spending. In addition, Business Roundtable member companies pay more than $220 billion in dividends to shareholders and generate more than $400 billion in sales for small- and medium-sized businesses annually.
Business Roundtable appreciates the opportunity to provide comments and contribute to the Department of Commerce's upcoming *Omnibus Report on Significant Trade Deficits*.

SUMMARY OF COMMENTS

Business Roundtable shares the Administration's goals of robust U.S. economic growth, more economic opportunities and well-paying jobs for Americans and improved competitiveness for U.S. companies and workers. We also concur with the Administration's belief that the U.S. trade agenda should include high-standard and modern trade agreements, strong enforcement of U.S. trade laws and rights under U.S. trade agreements, and other initiatives to expand U.S. trade and investment opportunities and target unfair foreign trade and investment practices and unfair imports where they exist.

However, Business Roundtable is concerned that the upcoming report on the causes of the U.S. trade deficit may fail to achieve these objectives. Specifically, based on the experience of Business Roundtable members, we think the report's core assumption that bilateral trade deficits are the most important standard by which to measure the health of the U.S. economy or U.S. competitiveness in international trade is not an effective approach. Moreover, we are concerned that a narrow focus on trade deficits may result in flawed trade policy recommendations that will undermine achieving our shared objectives.

Business Roundtable concerns are based on the following principles:

- The trade deficit is mainly determined by an interaction of macroeconomic drivers, primarily saving and investment decisions made by U.S. households and businesses;

- The goods trade deficit is not an appropriate or sufficient indicator of U.S. private-sector job growth and the overall health of the U.S. economy;
- A focus on goods trade, to the exclusion of services sector trade, ignores the importance of services exports to the U.S. economy and the impact of foreign barriers to them, and can lead to misdirected and therefore sub-optimal policy actions;
- A focus on the goods trade deficit is also too narrow because U.S. exports face unfair foreign trade barriers in countries with which the United States has a trade surplus; and
- U.S. free trade agreements (FTAs) secure important advantages for U.S. businesses and enhance U.S. growth prospects. The United States runs an aggregate trade surplus (in goods and services) with its 20 FTA partner countries. Moreover, countries with which the United States has FTAs spend substantially larger shares of their GDP on U.S. exports than countries with which the United States does not have FTAs.

MAIN COMMENTS

I. The Trade Deficit Is Primarily Driven by Saving and Investment Flows, Not Unfair Trade Practices or Barriers to Trade

Any country's overall trade deficit is primarily determined by its saving and investment positions.[1] If the country chooses to invest more than it saves (say, by spending on new buildings, new equipment and research and development), it must rely on foreign financial inflows to make this possible. Indeed, for the United States to maintain its position as an attractive destination for foreign investors, who supply our economy with needed capital and help create new jobs, an excess of investment relative to saving may even be desirable. However, net foreign financial inflows, by accounting principle, require equal and offsetting trade deficits. That is, a country's international financial account and its international current account (its trade balance) are necessarily equal, except for a small statistical discrepancy.

- Because of this fundamental macroeconomic principle, focusing on the trade deficit as a policy target is fundamentally misguided. In fact, it is only adjustments to core macro drivers – such as encouraging higher rates of household saving or reducing government budget deficits – that can lead to lower overall trade deficits.

- As a result, treating specific bilateral trade deficits as direct policy targets is ineffective and can even be counter-productive. For example, it ignores the fact that some bilateral trade deficits could make sense for America – considering that 60 percent of U.S.

[1] The drivers of the U.S. trade deficit are complex, and there can be interactions among trade barriers, the value of the dollar, saving decisions, investment decisions, etc. The statistical discrepancy between the country's financial account and its current account can be large, reflecting the complexities of valuing primary factor flows, secondary factor flows, shifts in the value of derivatives, etc., that can make the relationship between financial account and the current account less than ironclad. Still, we believe that the most respected and accepted view of the vast majority of professional economists is that saving and investment decisions are the primary drivers of the country's trade deficit.

imports are inputs or components used by U.S. manufacturers and farmers to make products and sell them competitively in the United States and around the world.

- There also is a substantial risk that targeting bilateral trade deficits with trade measures may only lead to exchange rate fluctuations and a shifting of imports and exports to different countries, with no net change in the overall U.S. trade balance. It could also lead to foreign retaliation against U.S. goods and services exports.

- This is not to say that trade barriers and unfair trade practices impacting U.S. companies should not be addressed. They should be. In that regard, USTR's annual National Trade Estimate report, for example, is an already available comprehensive guide to the foreign trade and investment-related barriers that are restricting the growth of U.S. exports and undermining the competitiveness of American manufacturers and services providers. However, an analytical framework that assumes that the mere existence of a national trade deficit (or the existence of bilateral trade deficits) signals unfair trade practices and unfair imports is an approach that can lead to misdirected and sub-optimal policy actions. For example, it could suggest that a country with which the United States has a trade surplus is not engaging in unfair foreign trade practices, when in fact it is.

II. The Goods Trade Deficit Is Not an Appropriate or Sufficient Indicator of Economic Growth, Competitiveness or Job Creation

Economic data indicate that the relationship between goods trade deficits and economic growth, competitiveness and job creation is extremely weak. Much more important factors include trends in consumer spending, patterns of investment demand and other core macroeconomic drivers of an economy. Consider the following economic evidence, which shows that goods trade deficits and employment growth are not inversely related as is implied by the framework being pursued.

Figure 1 shows that in the 27 years from 1990 to present, there is virtually no relationship between the U.S. goods trade deficit as a share of GDP and private employment growth.[2]

- In the 17 years from 2000 to present, there is actually a slight positive correlation between the U.S. goods trade deficit as a share of the economy and private employment growth. That is, larger goods trade deficits have been associated with faster employment growth over the last 17 years.[3]

[2] The correlation between the goods trade deficit as a share of GDP and private employment growth (both at annual frequency) is -0.15 over the period 1990 to 2016, meaning that smaller trade deficits were only slightly associated with faster employment growth over this period.

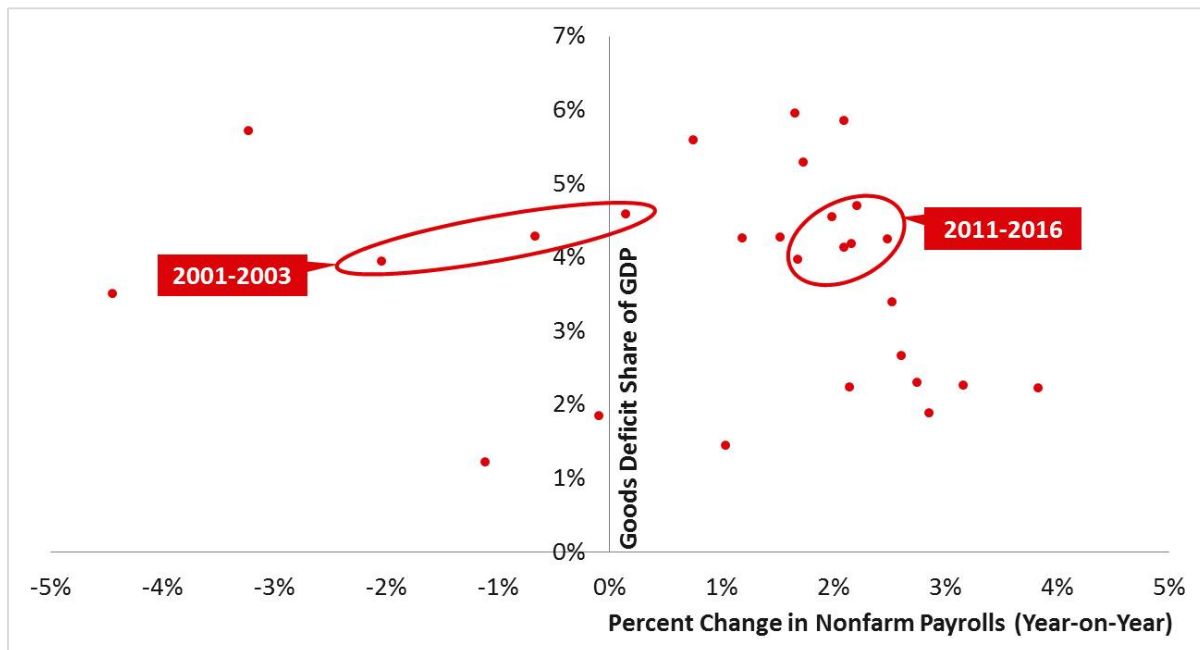
[3] The correlation between the goods trade deficit as a share of GDP and private employment growth (both at annual frequency) is 0.18 over the period 2000 to 2016, meaning that smaller trade deficits were slightly associated with slower employment growth over this period.

- More recently, the six-year period between 2011 and 2016 also shows a slight positive correlation between the deficit as a share of GDP and non-farm payrolls. Specifically, the goods trade deficit averaged 4.3 percent of GDP per year over this period – about twice the average trade deficit over the period since 1960 – while private payroll employment increased by a healthy 2.1 percent a year – significantly faster than average employment growth over the period since 1960.

- On the other hand, 1990 to 1993 was a period of relatively small goods trade deficits (average deficit of 1.6 percent of GDP per year) but also extremely weak job growth (an average of 0.6 percent growth per year).

The bottom line is that trade deficits do not cause weak job growth and have virtually no discernable relationship with non-farm payrolls.

Figure 1. Relationship of U.S. Goods Deficit with Payroll Growth



III. Services Exports Are Important, Too

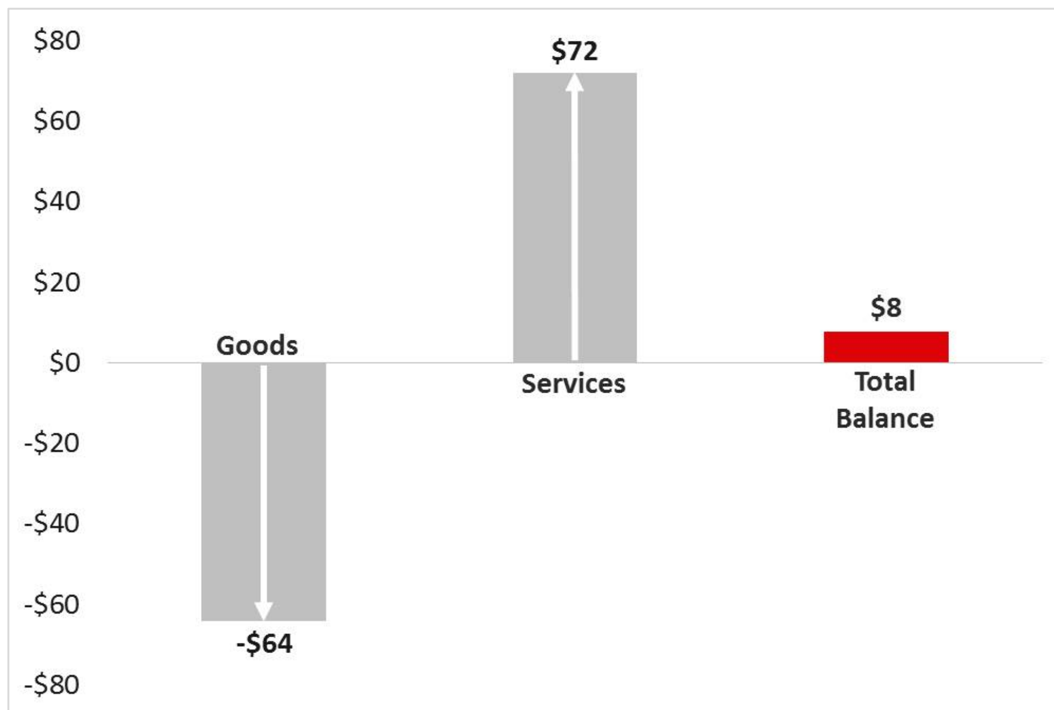
Notwithstanding our comments above about the need to focus on the macroeconomic drivers of the trade balance, we are also very concerned about the Administration's singular focus on goods trade balances, which exclude the vital contributions of services sector exports. In 2016, U.S. services exports ($752 billion) were equal to more than half of U.S. goods exports ($1,459 billion) and appear to be an important missing piece of the planned analysis of the causes of trade deficits. Indeed, in 2016, the United States ran a trade surplus of $249 billion in services, which offset a third of the goods trade deficit.

U.S. goods exports are important to the economy. However, any policy action that targets a zero balance or a surplus in goods trade with other countries ignores the contribution of services. This could lead to unrealistic policy expectations and risk destabilizing market access for U.S. services exporters – who are an important driver of job creation across the economy.

- For example, targeting a zero balance or a surplus in goods trade with key trading partners in the face of strong natural U.S. comparative advantages in services is almost certain to be impossible.
- Such an outcome would likely be possible only in a world of higher U.S. saving rates, smaller government budget deficits or reduced domestic investment plans.

Figure 2 illustrates that simply focusing on the goods trade balance can be misleading. Specifically, for countries with which the United States has an FTA, the surplus in trade in services is so large that it outweighs the goods trade deficit and resulted in an $8 billion total trade surplus in 2015.

Figure 2. U.S. Total Trade Surplus with FTA Partners, 2015



We also worry that this singular focus on goods trade seems to signal some sort of false superiority of goods exports over services exports. Both goods and services exports support excellent American jobs, pay high wages, signal U.S. comparative advantage in world-class businesses and help promote stronger U.S. economic growth.

IV. U.S. Free Trade Agreements Benefit U.S. Trade and Add Significant Value to the U.S. Economy

The United States currently has 14 FTAs with a total of 20 countries, including Israel, Canada, Mexico, Australia, Chile, Singapore, South Korea, Morocco and a set of Latin American and Middle Eastern countries. Business Roundtable believes that these FTAs have broadly benefitted our businesses and the overall U.S. economy. Indeed, a recent comprehensive study by the U.S. International Trade Commission found that on balance U.S. FTAs have increased total U.S. employment of both high- and low-skilled workers.[4] Other important facts regarding the value of FTAs to the trade balance and U.S. economy include:

- Countries with which the United States has FTAs spend significantly more of their income on American-made goods and services. For example, NAFTA countries (Canada and Mexico) spend an average of 20 percent of their GDP on U.S. exports, Central American and Dominican Republic Free Trade Agreement countries (CAFTA-DR) spend nearly 12 percent of their GDP on U.S. exports and Singapore spends roughly 10 percent of its GDP on U.S. exports. Meanwhile, Israel spends more than 6 percent of its GDP on U.S. exports and Korea spends nearly 5 percent of its GDP on U.S. exports. All of these ratios are substantially higher than the less than 2 percent of GDP that the European Union, Brazil, Japan, China and India (all non-FTA partners) spend on U.S. exports.

- In 2015, the United States had an aggregate $7.8 billion trade surplus in goods and services with its 20 FTA partners. This compares to a $509 billion U.S. deficit in goods and services trade with non-FTA countries. This suggests that FTAs are not key drivers of America's overall trade deficit.

- On a bilateral basis, in 2015, the United States ran a trade surplus in goods with 14 of its 20 FTA partners and a trade surplus in services with 15 of its FTA partners.

- While it is true that the United States had a collective goods trade deficit in 2015 with three FTA partners identified in the Federal Register notice as countries with which we have "Significant Trade Deficits" – Canada, Mexico and South Korea – the United States had a $46.4 billion trade surplus in services with these countries, which offset nearly half (44 percent) of the collective trade deficit. In fact, in 2015, the United States had an overall trade surplus (including services trade) of $11.9 billion with Canada.

BUSINESS ROUNDTABLE KEY TRADE POLICY PRINCIPLES

As the Administration reviews the country's trade policies, Business Roundtable recommends four key principles for expanding economic growth and job creation through international trade and investment. Business Roundtable member companies developed these principles to

[4] See United States International Trade Commission, "Economic Impact of Trade Agreements Implemented Under Trade Authorities Procedures, 2016 Report," Inv. No. 332-555, Pub. No. 4614, June 2016.

modernize and strengthen existing U.S. trade agreements, facilitate the completion of new trade agreements that will improve the competitiveness of U.S. companies and ensure strong and effective enforcement of U.S. trade laws and trade agreements. Specifically, Business Roundtable companies believe that:

1. Trade is a pillar of economic policy, and U.S. economic growth and jobs depend on domestic policy initiatives as well as expanded trade opportunities with other countries.

2. The United States needs more trade agreements to win the race for exports and jobs and ensure that we can shape the rules of the international trading system to our advantage.

3. High-standard and modern trade agreements are critical tools that American companies and workers need to access international markets for their U.S.-produced goods and services.

4. Enforcement is essential to creating a level playing field for U.S. companies and workers, and the United States should pursue strong and effective enforcement of trade and investment agreements and U.S. trade laws, consistent with U.S. statutory requirements and international trade obligations.

(See Appendix A for Business Roundtable's full report on its *Key Trade Policy Principles*)

CONCLUSION

Business Roundtable shares the Administration's goals of promoting strong economic growth, fostering rapid job growth for American workers and ensuring access to a fair and free trading system for American businesses and workers. As the Administration undertakes its review of the causes of the nation's trade deficit – in addition to targeting unfair foreign trade and investment practices and unfair imports that hurt U.S. companies – Business Roundtable recommends that the Administration also take into account fundamental macroeconomic drivers of the deficit, pay due attention to services sector trade and fully consider the many benefits of U.S. trade agreements. We look forward to working closely with the Administration to promote exports, strengthen our nation's international competitiveness and prevent unfair foreign trade and investment practices and unfair imports from injuring American companies, farmers and workers.

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APPENDIX A

Business Roundtable Key Trade Policy Principles

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It is in the national interest and imperative for the President, Congress and private sector to work together on economic initiatives that support stronger U.S. economic growth, create more economic opportunity and well-paying jobs for Americans and boost the competitiveness of U.S. companies and workers. To promote these goals, we need to move forward forcefully with a pro-growth economic agenda that includes a range of domestic initiatives and a proactive and constructive U.S. trade agenda.

That U.S. trade agenda should include supporting the rules-based international trading system and U.S. trade agreements that have shaped it, modernizing existing agreements and negotiating new high-standard agreements and strongly enforcing U.S. trade laws and agreements. Such an agenda should broadly aim to expand U.S. trade opportunities – exports and imports of goods and services – and address unfair foreign trade and investment practices and unfair imports, not narrowly focus on U.S. trade deficits. This document lays out key principles for U.S. leadership in achieving these objectives.

1) **Trade is a Pillar of Economic Policy:** ***U.S. Economic Growth and Jobs Depend on Domestic and International Policy Initiatives.*** The Administration, Congress and private sector need to collaborate on a range of domestic economic policy initiatives. These include modernizing the tax system, taking a smarter approach to regulation, investing in infrastructure and helping Americans develop new skills throughout their lifetime.

   We also need to recognize that the U.S. economy will not realize its full potential unless the United States does more to create trade opportunities with other countries and attract foreign direct investment to the United States. The U.S. economy and American jobs benefit from both U.S. exports and imports and their central role in global and regional supply chains, which also lower costs for U.S. consumers. Expanded trade will allow U.S. companies and workers to sell more American-made goods and services to the 95 percent of the world's consumers who live outside the United States. A fully functioning and globally competitive U.S. Export-Import Bank is a vital trade tool for maximizing such U.S. export opportunities and directly and indirectly supporting American jobs at U.S. companies of all sizes.

2) **We Need More Trade Agreements:** ***The United States Needs to Win the Race for Exports and Jobs.*** The United States needs a winning trade agreement negotiating strategy because our foreign economic competitors are not standing still. Such a strategy should rely on negotiating trade agreements – bilateral, regional, plurilateral and multilateral – that will maximize U.S. leverage and ensure the United States actively

shapes the international trading system so U.S. companies and workers are not disadvantaged.

There are now more than 270 bilateral and regional trade agreements between countries worldwide, and the United States is a party to only 14 of those agreements. These U.S. free trade agreements (FTAs) have greatly benefited the U.S. economy and American jobs by increasing U.S. exports and creating strong, enforceable rules for U.S. trade and investment with those countries. For example, while they include only six percent of the population outside the United States, the 20 U.S. FTA partner countries purchased nearly half of all U.S. goods exports worldwide in 2015. In that same year, the United States had a nearly $8 billion surplus in goods and services trade with FTA partner countries. This compares to a $509 billion U.S. deficit in goods and services trade with non-FTA countries. In the United States, U.S. trade and the trade agreements that help enable it support nearly 41 million U.S. manufacturing, services and other trade-related jobs – more than one in five.

Our foreign competitors are using their own FTA negotiations to advance their own national interests and gain competitive advantages over U.S. companies and workers by: (1) opening foreign markets and creating export opportunities on preferential terms for their companies and workers; (2) creating and supporting higher-paying domestic jobs tied to trade for their workers; (3) writing "free and fair" trade rules on their terms; and (4) advancing their foreign policy and national security goals.

Here are a few examples of other countries' FTA efforts around the globe. The European Union (EU) has completed FTAs with Singapore, Vietnam and Canada. The EU is also negotiating FTAs with Japan, India, Indonesia, Mercosur (Brazil, Argentina, Uruguay and Paraguay), the Philippines, Australia and New Zealand and modernizing its existing FTA with Mexico. China is negotiating the Regional Comprehensive Economic Partnership with 15 countries, including seven of the 11 Trans-Pacific Partnership countries, and a trilateral FTA with Japan and South Korea. Moreover, Mexico, which is the second-largest U.S. goods export market, has a network of FTAs with 44 countries.

3) **High Standard is the Only Standard: *The United States Must Negotiate High-Standard and Modern Trade Agreements.*** New U.S. trade agreements and existing U.S. trade agreements that need to be updated should achieve high standards, build on the rules-based international trading system and effectively address emerging economic and technological developments. They should ensure free and fair trade by breaking down foreign tariff and non-tariff barriers and addressing unfair foreign trade and investment practices and unfair imports.

   Existing U.S. trade agreements should be periodically reviewed to see if they should be strengthened and modernized to address any trade issues and challenges that have emerged since they were negotiated. Examples of newer trade issues and challenges include: (1) promoting e-commerce digital trade in goods and services, including the

elimination of foreign barriers, for all sectors, to the free flow of data and requirements to store data locally; (2) ensuring market access for new types of services; (3) strengthening intellectual property rights; (4) eliminating foreign localization policies and domestic content requirements for goods and services; (5) ensuring fair competition with foreign state-owned and controlled enterprises; (6) simplifying and harmonizing rules of origin across U.S. trade agreements; and (7) promoting regulatory cooperation and coherence between the United States and its trading partners.

If trade agreements are not fully and properly implemented, enforced and upgraded over time, they risk delivering less value to American businesses and workers. In updating existing U.S. trade agreements, it is critical to maintain these agreements and build on the many benefits they have created for the United States.

The key objectives for negotiating new U.S. trade agreements and modernizing and strengthening existing U.S. trade agreements are set out in the *Bipartisan Congressional Trade Priorities and Accountability Act of 2015* (TPA-2015 law). The TPA-2015 law also establishes procedures for: (1) congressional oversight and consultation as well as public input on trade negotiations; and (2) implementation of a completed trade agreement. These requirements ensure that negotiations on U.S. trade agreements are as transparent and informed by Congress and the public as possible.

4) **Enforcement is Essential:** ***The United States Needs an Effective Trade Enforcement Strategy.*** It is essential to create a level playing field for U.S. companies and workers by stopping unfair foreign trade and investment practices and unfair imports. This should involve strong and effective enforcement of U.S. trade and investment agreements – including World Trade Organization agreements – and U.S. trade laws and trade-related regulations, consistent with U.S. statutory requirements and international trade obligations.

   A successful enforcement strategy depends on the United States having strong trade agreements to enforce. This means strengthening and modernizing existing U.S. trade agreements and aggressively pursuing new U.S. trade deals.

   Such enforcement efforts provide an important opportunity to hold our trading partners accountable to strong trade rules. These efforts are also critical to opening international markets, halting unfair foreign trade and investment practices and unfair imports and addressing emerging economic and technological developments vital to U.S. innovation and competitiveness across all sectors of the economy.