



ALSTON & BIRD LLP

**China Apparel
Trade**

New York

November 16, 2010

Copyright © 2010 Jonathan M. Fee All Rights Reserved

China – the Most Outside Outsider

- China, with about 40 percent of U.S. apparel imports, is under spirited, unrelenting attack by U.S. domestic industry and U.S. Congress
- Regardless whether the attack is justified, it is a relative advantage to be just about anyone but China in the business of selling garments to the United States



NCTO Website on China

- China has spent “tens of billions of dollars” to create a textile and apparel sector with which “no nation on earth can compete”
- “Intense collaboration” with government allows “Chinese exporters to under price competitors”
- Chinese behavior is “mercantilist and predatory;” China uses “government organs to undermine ... free market principles”
- “Millions of workers” are being “put out of their jobs” because China “makes it impossible for their companies to thrive”



Currency Manipulation

- The dollar has mostly fallen against other major currencies in the last few years, making U.S. goods relatively cheap and foreign goods expensive
- But the Chinese have mostly pegged the Yuan to the Dollar since 2008, with only modest recent adjustments, making Chinese goods relatively cheap in the United States
- Thus, keeping the rate unchanged since 2008 is “manipulation”



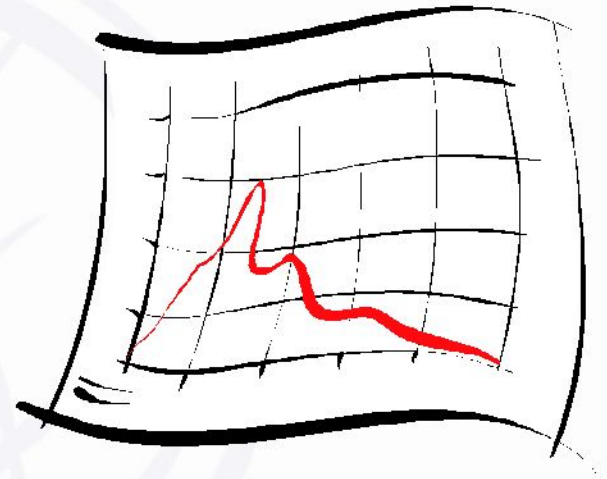
Hamburger Economics

- A recent tongue in cheek article in *The Economist* magazine compared MacDonald's hamburger prices in the two countries and concluded that the Chinese Yuan is undervalued by 40 percent
- But rising Chinese labor costs, relative to the U.S., and U.S. productivity gains, suggest U.S. manufacturers are less impacted than the nominal exchange rate indicates



What is China Expected to Do?

- Critics say that China should let its currency float (more) against the dollar, just like the dollar floats against the Euro, Yen and other major currencies
- Theoretically, a free market for currency would bring trade accounts into balance – about 4/5ths of the overall U.S. non-oil trade deficit is with China



Geithner's View

- Treasury Secretary Timothy Geithner says China will float its currency as a matter of self interest, to develop independent monetary policy, combat inflation, and improve trade imbalance with the U.S. and other trade partners
- In fact, in September 2010, the Yuan posted its biggest monthly gain, 1.74 percent, against the dollar since July 2005



He Could Be Right

- Holding down the Yuan fuels Chinese inflation, as China prints more currency to buy incoming dollars
- Last month, China's central bank raised interest rates for the first time in three years as an anti-inflation move
- The next logical move could be to allow the Yuan to rise, making imports cheaper, further reducing inflation, and giving the central bank more control over China's money supply



China Inflation

- Real estate prices, labor shortages and unrest, and rising consumer prices are signals of inflation in China
- China allowed its currency to rise by about 20 percent against the Dollar from 2005 to 2008, quelling inflation even while it enjoyed double digit growth
- It could do so again, without pressure from the U.S. and other countries



U.S. Quantitative Easing

- Meanwhile, the U.S. Federal Reserve announced a second round of “quantitative easing” (QE2), in November, saying it would buy about \$600 billion in long term treasuries with newly printed money, lowering long term yields and spurring investment in alternative investments
- Three intended effects: (1) spur borrowing and lending, (2) boost share prices, and (3) lower the dollar to help exports



G-20 and Irony

- President Obama was rebuffed in currency talks in Seoul last week – China resisted currency manipulation claims and other countries did not join the U.S. in its efforts to persuade China to let the Yuan rise
- Is it ironic that QE 2 has some of the same effects on the Dollar that China's policy has on the Yuan?



Currency Reform for Fair Trade Act

- The House passed H.R. 2378, on September 29, which would allow the Commerce Department to treat a “fundamentally undervalued currency” as an export subsidy in countervailing duty cases
- The bill, if passed by the Senate and signed into law, would reverse previous findings that undervaluation is not a subsidy because it impacts other aspects of the country’s economy



More from Lindsey Graham

"Clearly, China does manipulate the value of the Yuan to get an advantage in exports. They already have enough advantages. I was disappointed with the other nations who would not get behind President Obama to push the Chinese to change their currency policy. And I think you're going to see the Congress get more involved on the currency front after this trip"

Sen. Lindsey Graham (D-SC)



Doubtful Passage in Lame Duck

- It's possible that currency manipulation could be addressed by the Senate in the lame duck session
- Consideration is more likely in the 112th Congress – look for support from Senate Finance Chair Max Baucus (D-MT) and incoming House Ways and Means Chair Dave Camp (R-MI)



Wild Card in 112th Congress

- Incoming House Speaker John Boehner could be the wild card in the 112th Congress
- He did not support the House bill, citing fears of retaliation by China and violation of international obligations, and could slow consideration of currency manipulation legislation if it is reintroduced



More Potential Trade Remedies

- Section 421 of the Trade Act of 1974, which China accepted in its WTO accession agreement, lets the United States impose safeguards against import surges that cause or threaten market disruption
- Two important considerations: Section 421 expires in 2013, and relief requires presidential discretion
- Only one case actually imposed higher duties against automobile and light truck tires



ADD and CVD

- Speculation over the years has been whether there are viable domestic apparel makers to act as petitioners, and whether textile suppliers to CAFTA and NAFTA producers have standing to bring cases
- For China, the issue will be whether currency manipulation can be a countervailable subsidy



Foreign Manufacturers Legal Accountability Act

- A House version of this bill was approved by the Energy and Commerce Committee
- Has broad bipartisan support; aimed at product safety
- Would require any foreign manufacturer to register a U.S. agent for service of process before it could ship products to the United States



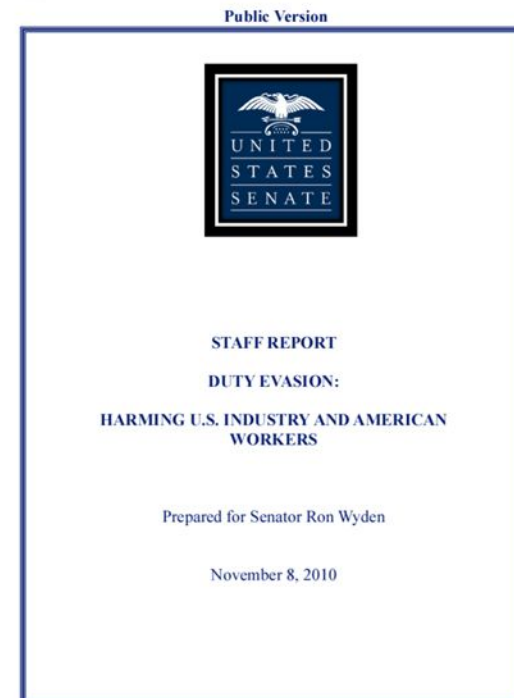
ITC Investigations

Earlier in the 2010 Congress, Senators Max Baucus (D-MT) and Charles Grassley (R-IL) requested International Trade Commission investigations of the effects on American business of China's intellectual property rights infringement and its "indigenous innovation" program favoring Chinese over U.S. products in the Chinese market



Widen Staff Report

- Sen. Ron Widen's (D-OR) staff published a report this month: "Duty Evasion: Harming U.S. Industry and American Workers"
- It mostly focuses on ADD and CVD; but some of the examples are of broader implication
- Staff pretended to be a U.S. importer, "AvisOne," an anagram for "Evasion"



Widen Report Example

Company E (cont'd)

From: ***

Sent: Wed, September 15, 2010 4:26 AM

To: "Paul Union" <avisonetraders@gmail.com>

Subject: Our product

Dear Paul,

Thank you for your reply !

I am sorry so late reply you ! we have no experience to avoid paying the anti-dumping duties ,besides we make the commerical invoice , we write that the value of products is less than the factual cost .

Await for your prompt reply !

Best regard !

Explanation:

In this email, Company E states that it does not know how to avoid paying antidumping duties, but professes that it undervalues products on commercial invoices, which is a form of duty evasion.

Further Comments

- ADD and CVD are unlikely; but the currency manipulation bill could pressure the Administration into urging China to float its currency
- Rising prices are likely, indicating that diversification of sourcing venues is a good idea
- First sale is always worth considering, if available





Jon Fee

Alston & Bird LLP
950 F Street, N.W.
Washington, D.C. 20004
202 239 3387
jon.fee@alston.com