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U.S. DEPARTMENT OF THE TREASURY'S REPORT TO CONGRESS ON INTERNATIONAL ECONOMIC AND EXCHANGE RATE POLICY

HEARING

BEFORE THE

COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS UNITED STATES SENATE

ONE HUNDRED SEVENTH CONGRESS

SECOND SESSION

ON

THE U.S. DEPARTMENT OF THE TREASURY'S REPORT TO CONGRESS ON INTERNATIONAL ECONOMIC AND EXCHANGE RATE POLICY

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U.S. DEPARTMENT OF THE TREASURY'S REPORT TO CONGRESS ON INTERNATIONAL ECONOMIC AND EXCHANGE RATE POLICY

WEDNESDAY, MAY 1, 2002

U.S. SENATE,
COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS,
Washington, DC.

The Committee met at 10:02 a.m. in room SD–538 of the Dirksen Senate Office Building, Senator Paul S. Sarbanes (Chairman of the Committee) presiding.

OPENING STATEMENT OF CHAIRMAN PAUL S. SARBANES

Chairman SARBANES. The hearing will come to order.

We are very pleased to welcome Treasury Secretary O'Neill to the Committee this morning to testify on the Treasury Department's Report to Congress on International Economic and Exchange Rate Policy.

He will be followed by a panel of representatives of American manufacturers, workers, farmers, and academics, who will comment on the impact of the exchange rate of the dollar on U.S. trade, employment, and long-term economic stability.

Mr. Secretary, we apologize. We had a vote and we had no alternative in terms of when to start. And I understand that you have some time pressures and we are mindful of those. So when the time comes that you have to leave, we will certainly recognize that.

The Omnibus Trade and Competitiveness Act of 1988 requires the Treasury Department to submit a report to Congress annually in October, with an update after 6 months, on international economic policy, including exchange rate policy.

The Banking Committee originally planned to hold this hearing last October, at the time of the submission of the annual report, but delayed it because of the events following September 11.

This morning's hearing is technically on the 6 month update of that annual report, but obviously, will encompass the report as well. It is important to just take a moment, and I will be very brief here because I know we want to move along, to understand the origin of this reporting requirement, so we can understand its purpose.

The report required in the 1988 Act was a response to the experience in the early 1980's when the exchange rate of the dollar rose

to very high levels and there was a sharp deterioration in the U.S. trade and current account balance.

Initially, there was a denial that there was any issue, any concern. But the Treasury Department—this is in the Reagan years, Secretary Baker—shifted positions and organized an effort by the Group of 7 industrial countries in 1985, known as the Plaza Accord, to address lowering the value of the dollar and begin to ease the deterioration in the U.S. current account.

In the aftermath of that experience, the Congress realized that it did not have a mechanism by which the Treasury Department would regularly report or testify on the conduct of international economic policy. There was a recognition that this was a critical area of economic policy and that a mechanism similar to the requirement that the Federal Reserve report to Congress semiannually on the conduct of monetary policy, was needed. This report was the result of that rationale. We regard this report as a serious matter. We intend for the Committee to conduct regular oversight on this important issue.

I want to commend Secretary O'Neill and the Treasury Department for the timely submission of the report and its 6 month update since the current Administration took office. In this regard, they have been quite responsive to the requirements of the statute. I am not going to go through the different requirements of that statute, many of which have been met specifically in the reporting requirement. There are some that were not addressed and I may make reference to those in the question session.

The purpose of the report is for Treasury to present its views in writing to the Congress and the reasoning behind these views, and we look forward to hearing from the Secretary this morning.

Senator Bunning.

COMMENTS OF SENATOR JIM BUNNING

Senator BUNNING. Thank you, Mr. Chairman. First of all, thank you for holding this hearing and thank you, Secretary O'Neill, and all our other witnesses for being here. This is an important hearing and I would like to thank everyone here for testifying.

I am entering this hearing with an open mind. There is a divergent opinion on this issue and we need to hear from everyone who is affected by this. I believe our economy, though growing, is still rather fragile and we could slide into what is known as a double-dip recession if we are not careful. We need to make sure that we make the right decisions so we do not jeopardize this recovery.

I believe your testimony today can help us figure out how to keep the recovery going. I look forward to hearing from you and all the other witnesses, and I thank you, Mr. Chairman, for holding the hearing.

Chairman SARBANES. Thank you, Senator Bunning.

Senator Johnson.

STATEMENT OF SENATOR TIM JOHNSON

Senator JOHNSON. Thank you, Chairman Sarbanes, and thank you, Secretary O'Neill, for joining us here today.

This is an important hearing to discuss international economic conditions and exchange rate policy. Monetary policy and the

strength of the dollar relative to foreign currencies play a critical role in America's ability to compete in a free trade environment.

I think it is fair to say that in my home State of South Dakota, that the appreciating value of the dollar, the differential that increasingly occurs, is significantly undermining support for free trade negotiations, as our farmers and ranchers in particular find increasingly that the problem that they have that results in an unlevel playing field in their perspective is not so much the issue of tariffs and other nontrade barriers, as it is currency differentials.

I want to focus a bit today on the local economic impact that the strong U.S. dollar has in my State. I am concerned that, in the face of cheaper meat imports, cattle and sheep prices continue to fall and exports stagnate. I am also concerned about small manufacturing firms as well that are unable to compete effectively against foreign competitors due to the sustained appreciation of the dollar against other currencies.

This past year, my State saw an 11.6 percent decline in manufacturing employment and a 27 percent increase in personal bankruptcy filings. Some of this, of course, is due to the business cycle and the recent recession. But the depreciation of the dollar and the consequent depression in commodity prices appears to be a principal reason why the ag economy did not share in the economic prosperity that most sectors enjoyed between 1995 and 1999.

Last year, I requested the USDA to complete a study on the U.S. sheep industry, its future and the factors that have led to its decline. The study focused on the rapid increase in lamb imports in the mid-1990's that resulted from price manipulation by New Zealand and Australia. As a result of arbitration, the United States established a 3 year tariff rate quota, TRQ, on lamb imports from these countries in July 1999.

Despite implementation of the TRQ, imports did not slow because the effects of the tariff were almost entirely offset by the strong United States dollar and unusually weak Australian and New Zealand currencies, in 1998, when the United States dollar appreciated against the Australian and New Zealand currencies by more than 18 percent and 24 percent, respectively.

In light of these developments and the impact that it has on U.S. trade, and the impact it has on the willingness of the American people to pursue trade agreements that do not take into consideration currency differentials, I think it is very important that we take a hard look at this, and I welcome, Secretary O'Neill, your report and your willingness to testify to this Committee today.

Chairman SARBANES. Thank you very much, Senator Johnson.

Senator Miller.

COMMENTS OF SENATOR ZELL MILLER

Senator MILLER. Thank you, Mr. Chairman, for holding this hearing. I will pass on a statement. But I do want the Secretary to know how glad we are to have him with us and thank him for his service.

Chairman SARBANES. Senator Corzine.

COMMENTS OF SENATOR JON S. CORZINE

Senator CORZINE. Mr. Chairman, I thank you for holding this hearing, and it is always good to see the Secretary.

This is an important topic that really has a true impact on our economy and I look forward to his remarks and the other witnesses' remarks as well.

Thank you.

Chairman SARBANES. Good.

Senator Akaka.

COMMENTS OF SENATOR DANIEL K. AKAKA

Senator AKAKA. Thank you very much, Mr. Chairman. I will also be brief.

I want to welcome the Secretary and I look forward to your report to us on International Economic and Exchange Rate Policy. I also welcome the other witnesses.

During today's discussion, Mr. Chairman, I am particularly interested in the current account deficit and the potential problems that it may cause.

Given the divergence of opinion on the significance of the current account deficit, I look forward to an examination of the consequences of the deficit on our economy. Secretary O'Neill, you have stated that the current account deficit is a meaningless concept. The International Monetary Fund's chief economist has called the U.S. current account deficit, and the possibility of a correction, a significant risk to the global economy.

The Wall Street Journal described the nightmare scenario involving the reversal in account deficit and the possibility of foreign investors withdrawing their money out of the U.S. economy. This could lead to a weakening of the dollar and stock markets, and higher interest rates.

I welcome, Mr. Chairman, the witnesses' assessments of the potential adverse impact of the current account deficit on the global economic outlook and the consequences of account reversal.

Mr. Chairman, I thank you very much for holding this hearing.

Chairman SARBANES. Thank you, Senator Akaka.

Secretary O'Neill, we would be happy to hear from you.

STATEMENT OF PAUL H. O'NEILL, SECRETARY U.S. DEPARTMENT OF THE TREASURY

Secretary O'NEILL. Chairman Sarbanes, Ranking Member Gramm, Members of the Committee, thank you for this opportunity to appear before you to discuss our international economic policy. With the Committee's permission, I will submit my full testimony for the record and make an abbreviated oral statement to allow more time for questions.

Chairman SARBANES. Thank you very much, that will be fine. We appreciate that.

Secretary O'NEILL. Thank you, Mr. Chairman.

At the outset, I think maybe it is important for me to say, because I want to have an opportunity to have a full and clear engagement with the Chairman and Members of the Committee, that whatever one might try to imply from what I say today, there is no intent in anything that I say that should give comfort to those

who think we are going to change our policy today. I say that to you because, as I read the wire clips from around the world this morning, there is apparently some breathless anticipation that I am going to say something to intentionally indicate a change in policy position or direction.

I want to assure you at the outset that whatever I may say, that is not the intent. And again, I want to make it really clear because the people who benefit from roiling the world currency markets are speculators. And as far as I am concerned, they provide not much useful value to the furtherance of advancing the cause of improving living standards around the world. So, I do not want to give them any ammunition to say that there is a basis for roiling the world currency markets out of our conversation here this morning.

I would like to touch on several of the Administration's policy initiatives for increasing economic growth and reducing economic instability abroad. They are of vital interests to the United States.

First, we are working to reduce barriers to international trade. Total U.S. trade amounts to about one quarter of our domestic product, and trade touches every part of our economy and creates millions of American jobs, paying above-average wages.

To bolster growth and create new exports and job opportunities for America, the Senate should pass trade promotion authority so that President Bush can work with nations around the world to reduce trade barriers and open markets to U.S. exports.

Second, we are also working with the International Monetary Fund to give emphasis to their role in crisis prevention. When crises do occur, we need a more orderly process for resolving them so that capital continues to flow to emerging markets. We are working with others in the official sector to implement a market-oriented approach to the sovereign debt restructuring process. We also support continued work on the Fund's statutory approach to sovereign debt restructuring.

Regarding the multilateral development banks, we believe they can deliver better results by investing in high-impact, productivity-enhancing activities.

President Bush has proposed that we transform the World Bank and other development bank funds for the poorest countries into grants rather than loans. Investments in crucial social sectors, such as health, education, water supplies, and sanitation, are crucial to private enterprise-led growth and a necessary basis for development. But they do not directly generate the revenues that service new debt. As a result, the recipient government is forced to repay the loan by taking resources from citizens subsisting on less than a dollar a day. By piling loans on these nations, we are simply generating the next generation's debt-forgiveness program. We ought to recognize that projects that do not generate economic returns should be funded by grants and not loans.

President Bush recently announced his new compact for development, a major new initiative for development based on the shared interests of developed and developing nations in peace, security, and prosperity.

The compact creates a new development assistance fund called the Millennium Challenge Account. To access account funds, developing countries would have to commit to policies that promote

growth and development, including governing justly, investing in people, and promoting economic freedom. We intend to put our development assistance funds into environments where they can make a difference. Another important aspect of our international economic agenda is the financial war on terrorism.

Since September 11, the Treasury Department has thwarted supporters of Al Quaeda and other terrorist organizations by freezing $34 million in assets directly and assisting our allies to freeze another $70 million. Recent joint discussions with our allies mark a new level of coordination in the fight against international terrorism.

I would like to now turn briefly to global economic conditions. The world economy is still in the early stage of recovery. The GDP figures released last week confirm that we are on the path back to sustainable growth of 3 to 3½ percent per year.

I also want to reiterate my feelings on the U.S. current account deficit. The current account represents the gap between domestic savings and investment. It is financed by international capital flows which have risen because of foreign interest in investing in the United States. As long as we continue to have the best investment climate in the world, people in other nations will send their savings here, where those resources fuel our economic growth and job creation.

I believe we should strive in both the private and public sectors to always be the best place on earth to invest. As long as we are the most productive economy in the world, our Nation will continue to be prosperous.

I thank you again for this opportunity to testify and I would be delighted to take your questions.

Chairman SARBANES. Well, thank you very much, Mr. Secretary.

I want to focus on the current account deficit. I am really seeking a better understanding of your views. The current account deficit now as a percent of GDP is higher today than it was at its peak during the 1980's. In fact, we have some charts that show a really dramatic deterioration in the current account deficit as a percent of the gross domestic product.

This is back in the 1980's and then this is what has happened in the 1990's (indicating).

You have been quoted as saying—"I do not know." I will let you address the quote—that you view the current account deficit as meaningless or irrelevant. Would you explain to us the rationale behind this view?

Secretary O'NEILL. I am sure I must have said that some place. I am not sure what the context was of when I might have said something that fits between those quote marks. My view of the current account deficit is this. I think, first of all, one needs to examine what the origins of the idea of the current account deficit are.

I think the answer to that question is, it is a derivative part of the notions that were put in place in the late 1930's and early 1940's about how we should assemble data to look at how the world works, and to try to draw from the data in these various conventions that we have adopted correlations with good and bad economic activity in the world. When I look at it, I, first of all, ask myself, is the world the way it was in 1939 or 1940, when Simon

Kuznets and his associates put it together? My own answer to that is that it is not. And it is not in these important ways.

I think in the 1930's and 1940's and, in fact, I think one could argue maybe even through the 1950's, that the world in fact was relatively aligned with the ideas that suggested that the world is run on a nation-state basis, and that nations are basically independent of each other in an economic sense, and that in fact, it is possible for one nation to substantially change its economic position by playing off of other nations because of the separateness.

I do not find that to be the way the world is any more. Having run a corporation with operations in 36 nations, I will tell you what—I never spent a minute thinking that somehow, I could go to some of these, any of these other countries, and act as though that country were independent of the rest of the world.

I did not find that it was possible to do that here in the United States. In fact, I do not think it is possible for anyone to do it. It is possible for people to continue to think it, but it is not real world in terms of the way world economic activities work any more. So, I have a problem with the construct before I ever get to what the implications of adding up all of these numbers are? And then I would submit this—that it is said that the current account deficit is a U.S. current account deficit.

Now my question is, what does that mean? Does the U.S. Government have a deficit with other countries? That is to say, have we in the Federal Government gone out and borrowed money from other countries that they can jerk out from under us?

The answer to that is no.

Who owns the so-called current account deficit? Millions, or maybe even billions of individual investors who have made decisions around the world to own these investments. Again, in my brief oral statement, I made the point that the reason money comes here is because it is treated better than any place in the world, as measured by the risk-adjusted rate of return on investments that are made in the United States.

I have a lot of trouble with the construct that, if you accepted at face value that somehow this is a deliberate decision of the United States to do something, this is an analogy to an individual deciding to borrow too much money. I find it is a false analogy. So, when I have said these words about my problem with the current account deficit, it is this stream of thinking that I had in mind.

It does not mean that I do not think there is some legitimate value in thinking about relative capital flows around the world and the implications that has for interest rates and other important determinants of where money goes. But it does mean that I do not think the simple correlations that are made are not meaningful or useful and, in fact, I think are a dangerous basis for making policy prescriptions.

Chairman SARBANES. Let's just sharpen the debate for a minute. I know you are a man who likes to engage in vigorous intellectual debate. I want to quote to you from *The Economist* just a week ago, an editorial. This is what they say:

The International Monetary Fund says that America's current account deficit poses one of the biggest risks to the world economy. Paul O'Neill, America's Treasury Secretary, reckons that the Fund's economists do not know what they are talk-

ing about. He says the current account deficit is a meaningless concept. Policymakers should pay no attention to it.

Mr. O'Neill's views fly in the face of experience. A deficit that will require America to borrow from abroad almost $2 billion a day by 2003 can hardly be ignored. The consequences for the dollar if foreigners' appetite for American assets even wanes would give a Treasury Secretary who knew what he was talking about sleepless nights.

Now, I put that out there because this is one serious commentary and I would be interested in your response to it.

Secretary O'NEILL. If you do not mind, I have two different things I would like to say about that.

First of all, last November, the International Monetary Fund—we got the World Bank and the International Monetary Fund, the G–7, together—made a public pronouncement that growth in the United States in 2002 would be 0.7 percent.

And on the spot, I said to the managing director of the IMF, I am going to bet you a dinner in a restaurant of your choice that we are going to far exceed that number. They have now decided that the number is going to be 2.4 percent. So, at the time, I was saying we were going to be some place like where, in fact, we are on the glidepath. And so, maybe you would prefer their economic judgment to mine. So far, they have not been right.

Now to a different point on this. It is not that I think we should pay no attention to this issue. But I would ask the question, if you do not like the current account deficit, what policy instruments would one use to change the current account deficit? And then, what is the most meaningful question—are you willing to suffer the consequences of treating the current account deficit as the objective variable in the equation?

What I mean by that is this. One way to fix the current account deficit is to reduce imports. I do not know anyone who wants to do that because the implications of reducing imports is we become a more isolated and insulated society. Our citizens pay more money for goods. The reason goods are coming here is because they are valued by consumers at the prices they are offered at, as compared to alternatives.

So if you do not like the current account deficit, we could say, bugger them, the U.S. citizens. We here in Washington know better. They should not be buying so much stuff from outside the country. That would fix the current account deficit. That does not seem like a brilliant thing to me to do.

If you look at the academic work, what I consider to be the best academic work on this subject, there is a report I would submit to you by Allan Sinai that was done in December 2000, that basically says, if you run all the econometric equations and treat the current account deficit as the dependent variable and you seek to reduce the current account deficit, every single intervention hurts the U.S. economy, as compared to leaving the current account deficit alone.

I have not seen academic work that suggests itself to me that produces a different answer. And so, it is part of the reason why I am mystified that there seem to be so many people that want to treat the current account deficit as the objective function for our society, when doing so. This is not a partisan report from Sinai. This is an academically solid, legitimate report. I do not know of something to counter Alan's findings.

Chairman SARBANES. Well, we could go on at great length, but my time has expired, and I am going to yield.

I would just note that the panel that is coming along behind you feels pretty strongly, at least a number of them do, that the currency is manipulated by some of our trading partners, very much to the U.S. disadvantage, and that is affecting the balance of trade in a very substantial way. And, of course, that is one of the things that we are trying to get at in these reports.

Senator Bunning.

Senator BUNNING. Thank you, Mr. Chairman.

Secretary O'Neill, the Treasury Report said there was no current manipulation by our major trading partners last year. How does this jibe with the reports saying China purchased $50 billion, Japan bought $39 billion, and South Korea bought $9 billion last year? In other words, if there is no importance to that fact, how does that jibe with your report?

Secretary O'NEILL. By the definitions of law, as we understand it, the individual actions that have been taken do not amount to manipulation under the statute. And I think, in a broader sense, if you look at the Chinese currency against world currencies, they are running kind of a soft peg.

I do think this. The markets are grinding so finely, and they are so interlaced any more, that it is not possible any more to actually fool the market for very long. That is to say, to create an artificial situation that is not in line with the judgment of the market about the discounted present value of productivity improvements relative to other countries.

Senator BUNNING. Currently, I do not disagree with you.

What happens with China having that large a reserve of U.S. dollars—what happens in a time of crisis, such as a confrontation at the Taiwan Straits that the Chinese could dump dollars onto the world market in an attempt to destabilize our economy?

Secretary O'NEILL. First of all, it presumes that the dollars are held by an authority that has the ability——

Senator BUNNING. The Chinese government.

Secretary O'NEILL. But the Chinese government I think does not actually hold that money. I think if you go look at how that money is held, you are looking at first-order effects. Look at the second-order effects. What did the Chinese do with that money?

I will tell you one thing that they did with it. They built new factories. Now where do they get the technology for the new factories? They bought it in the UK or they bought it here, or they bought it—you know, it is in German hands or it is in Brazilian hands. It is in somebody else's hands.

It is another problem that I have with the current account deficit. It assumes the world is static and that first-order effects never become second-order effects.

Senator BUNNING. I do not consider it static. But I understand that if they do use that currency as hard dollars to do other things, that they are replacing them with hard dollars. And we are talking about a fixed period of time where they measured the amount of dollars that the Chinese had under their control. Are you telling me that that is not important?

Secretary O'NEILL. I do not think so.

Senator BUNNING. You do not think so? In other words, if they got up to $100 billion, you would not think so? Or $200 billion, it would have no effect?

Secretary O'NEILL. No, I do not think it is a material amount, in an economy that is a $10 or $11 trillion economy. $100 billion—I am trying to think about it.

Senator BUNNING. As long as the situation in the world is like it is, I do not disagree with you. But if we have a confrontation, I think it would have a serious effect on the dumping and devaluing in our economy of the U.S. dollar, if they dumped that on the world market.

Secretary O'NEILL. I think if it is true that one sovereign had the ability to make an instantaneous decision, you might be right. I do not think that is the case.

Senator BUNNING. In the mid-1980's, our Government worked on a similar problem through the Plaza Accord. In what circumstances would you have considered to take a similar action?

Secretary O'NEILL. Well, first, you are going to hear from panel members and I am sure they will have their own and probably different views.

Senator BUNNING. I want yours. I do not want the panel's.

Secretary O'NEILL. I just wanted to say, it is not clear to me that the implication of your question about the Plaza Accord has substance behind it, in this sense: I think it is a real speculation to know, in fact, whether conditions and trends were moving in the direction that the Plaza Accord simply hopped on the back of.

What comes to mind is the metaphor of the caterpillar riding on a log down the stream and thinking they are steering. I think you have to be really careful in assigning causality to supposed political interventions. I am not sure that those causalities exist.

Senator BUNNING. In other words, our political intervention in Afghanistan——

Secretary O'NEILL. I did not say that.

Senator BUNNING. There is no consequences to Afghanistan?

Secretary O'NEILL. No, I did not say that.

Senator BUNNING. What are you saying, then?

Secretary O'NEILL. I am talking directly about intervention attempts in world financial markets. I am saying, I think there is a real doubt about the effectiveness of interventions or words about interventions—although I would grant you one thing. It is why I made my statement at the beginning—it was not my intent to roil the financial markets today. There is nothing the speculators like better than to roil the financial markets. And I think it is true, by changing rhetoric, you can roil or even maybe give direction to the financial markets over some limited period of time.

But coming from the part of the economy that produces real tangible things you can take home and put on the table, I believe at the end of the day, while monetary affairs are not incidental, the real long-run economics of the world depends on the physical production of goods and services and therefore, you can have as much rhetoric as you want; eventually the world is going to stabilize around the real production of goods and services.

Senator BUNNING. You may believe that, but I will guarantee you, the Chairman of the Federal Reserve does not believe that.

Thank you, Mr. Chairman.

Chairman SARBANES. Thank you very much, Senator Bunning.

Before I yield to Senator Miller, Mr. Secretary, I am prompted to quote President O'Neill of the International Paper Company in 1985.

The strong dollar has turned the world on its head. We have suffered a major loss in competition position because of the loss in exchange rates. And then O'Neill explained that in the last few years, a strong dollar has dramatically eroded the U.S. forest products industry's natural advantage in world trade.

This is what we are hearing from all of your former colleagues, or people who currently hold comparable positions in the business world. And of course, that is what you were saying in 1985.

Secretary O'NEILL. Do you have the rest of what I said then?

Chairman SARBANES. Well, what else did you say then?

Secretary O'NEILL. What else I said then was, "what we in the industry need to do is we need to take matters in our own hands and we need to create conditions in the goodness of what we do, the exceptional excellence of what we do, so that we can prosper no matter what is happening with exchange rates. We need to use our brain power to figure out how to create goods in the currency that we sell them. And we need to take this responsibility on ourself."

I do not think you will be able to find any place where I called on the Government to intervene in the financial markets. I was basically calling attention to the fact that, indeed, currency relations had changed and those who were going to prosper were going to have to assume the responsibility for their own individual companies and industries to fix the problem, not look to Government to make a temporary intervention that would make life sweeter for us.

Chairman SARBANES. Well, Paul H. O'Neill, *Los Angeles Times,* International's President, doubts that paper prices will rise in step with the dollar's decline. But he definitely sees happier days ahead. "Exchange rates moving back to normal levels would be very good news for our industry, he says. We would recoup most, if not all, of our export volume."

Secretary O'NEILL. That is a statement of fact. It is not a prescription for the Government to intervene.

And if you go look at the record, which you will find both at IP and Alcoa, there is a performance. Let me remind you of rate spread. The Japanese yen–United States dollar rate, as I recall, in 1985, was 240 or something on that order of magnitude. We reached a low relationship of 80 yen to the dollar, I think, a couple of years ago.

Through that whole time, the companies I was associated with prospered, became leaders in the world. And we did not do it by coming down here asking somebody to fix the world, to make it easier for us. We did it with our fingernails in 36 different countries around the world.

Chairman SARBANES. Well, it doesn't square. You have the Plaza Accord and that helped you tremendously, you and other exporters, and John Gorges, who was with you at International Paper. Correct?

Secretary O'NEILL. He was the Chairman.

Chairman SARBANES. Yes. One of the toughest problems we face is the very strong dollar, which impacts our export products and prices a good deal. There are major uncertainties. If the dollar weakened, we could compete better. And it is not just us. It is other exporters, too.

Senator Miller.

Senator MILLER. Mr. Secretary, I guess I am going to continue along that same kind of questioning. I want to say that I understand how you have to look at the really big picture. I appreciate that and I respect that.

As a Senator from Georgia, though, I have to be a little bit more parochial. I have to look at those 8 million people in Georgia. There are some industries in our State, forestry is one of the key ones, agriculture, textiles. They all have complained to me pretty loudly that the dollar is making it difficult for them to export profitably, and making it easier for imports to take the market share here in the United States.

Continuing on this line the paper industry which the Chairman mentioned, has seen more than 90 percent of the growth in their U.S. markets captured by imports, they tell me. I guess my question is, and I know you have to look at it from a different angle, but how would you respond to my constituent industries that are so very concerned about this matter?

Secretary O'NEILL. You know, when I come around and I sit on your side of the table, I understand the pressure that not just you, but you are reflecting what your constituents are telling you. I understand the pressure that creates.

I said that while I was at Alcoa, we prospered. But it does not mean that we did not have dislocations. In fact, we did have dislocations because not in every place were we able to push our costs down enough to compete in the whole world on a competitive basis with changes in exchange rate positions over time.

I know these are issues where your heart breaks for the people that are directly affected by these things. And I suppose it is no solace at all to the individuals who are directly affected. But I think it is demonstrably clear that in fact we in the United States, the U.S. citizens as a body, and the world as a body, are better off if we let competition and best value products lead the world.

It is not an easy thing to follow in practice and that is why we have lots of people coming to Washington to tell us how they are hurting. And I think we have to be sympathetic with that. But I think at the same time we are better off to help the casualties if it produces a better economic outcome for the whole society than to let the casualties become the control on our ability to succeed as a total country.

Senator MILLER. Thank you. I do not have any other questions.

Chairman SARBANES. Senator Gramm.

STATEMENT OF SENATOR PHIL GRAMM

Senator GRAMM. Well, Mr. Chairman, I was over trying to participate in the negotiations to bring our trade promotion authority bill to the floor, and so I missed our opening statements. So, I would like to take my time to make a statement.

First of all, every day on the world currency market, as I understand it, there are about $1.2 trillion worth of dollar transactions. This is the purest market in the world in that it has the most participants and it has the largest volumes.

My own belief is that even a country as rich as the United States of America could affect currency values, could affect the value of the dollar, only for a very short period of time, just as I could lower real estate values in my neighborhood if I were mad at everybody else and wanted to hurt them, by selling my house for $100. But once the house is sold, then real estate values are basically back as they were.

I not only believe we cannot affect the value of the dollar, except by changing policy that would affect people's perception and the reality of the American economy, but also that currency intervention is a nonfeasible policy, even if it were desirable, would be my first thesis.

Second, this is a perfect market, for all practical purposes, where every day people are buying and selling dollars. Why do they buy dollars? They buy dollars to buy American goods and they buy dollars to invest in America. And they sell dollars and buy foreign currency to invest abroad or to buy foreign goods.

So when we say we have a current account surplus, by definition, we have a capital account. We have a huge inflow of capital. Were that not the case, the value of the dollar would change and the surplus would be eliminated. What you are seeing is a mirror image of capital inflow versus a current account deficit. Now is the capital inflow bad? Who's against investment? Every once in a while people say, well, my God, foreigners own some building in New York. I have found ownership is not what it is cracked up to be.

[Laughter.]

First, try moving that building back to Japan. Second, I do not think anybody is willing to come out here and say: Investment is a bad thing and we want less of it. Then what about loans? Aren't you a debtor when you get a loan?

Well, it depends on what you do with the loan. If you invest it productively, it is an avenue to riches. If you invest it poorly, it is a path to poverty. The only kind of loan I would be concerned about is if our Government were borrowing money to invest in Government and they expected value of the investment would be far less than the service cost alone. And exactly the opposite is true.

This idea about what you said about forest products in my mind is totally consistent with what you are saying today. There is no doubt that at any given time there are many industries that would benefit if the dollar was cheaper. There are industries that would benefit if the dollar were more valuable. But the question—you are not here today representing the forestry industry.

Secretary O'NEILL. That is right.

Senator GRAMM. You are here today representing the American economy. And the point is that if you could snap your fingers and make the dollar cheaper, there would be some people who would gain. There would be some people who would lose. So, I do not see an inconsistency there.

Finally, I, quite frankly, do not have a problem with what *The Economist* says. For the world economy, looking at the world now, is it good that all this investment is coming to America?

If you just look at the world economy now, maybe you would want to redistribute this investment differently. It may be risky for the world that America gets richer and more prosperous and our real wages rise and we become more dominant in the world, depending on your perspective. But our question is not the world. Our question is the United States of America. It seems to me that when we look at American interest, that it is very clear that we want investment, that we want to have open markets, and that we are succeeding economically as a result of it.

So, I do not disagree with my colleague from Georgia. We have 60,000 jobs in Texas in the forestry industry. A lower value for the dollar, if you could just wish it and have it, would be beneficial to them.

But for everybody going to Wal-Mart, it would be a bad thing. And in this case, there is nothing that we could really do to change it, other than we could have our Navy blockade our ports. That would improve our situation. The enemy would do it in war, but we could do it in peacetime. Or we could stop foreign investment. I would submit, we do not want to do either one of those things.

I think we need to keep our eye on current account deficit. If it becomes clear that it is a Government policy that is driving it, such as we are getting foreign loans to finance Government or foreign investment—if something artificial is happening, then I think it is something that we should be concerned about.

But the thing I am never concerned about is that somehow, somebody is going to manipulate a market where there is $1.2 trillion worth of transactions every day. Even as much money as you control, you would be a bit player in this market. And foreign countries that try to manipulate the value of the dollar are trying to get water to run up a rope. It just cannot be done.

The only final point I would make is that we could have a dollar for exports and a dollar for imports. You could have one that was valuable and you could have one that was cheap.

The problem is that then you would have to have an exchange rate between the two dollars. And in the end, I think this is a thing where individual industries can say, I wish markets were different. But, A, I do not think there is anything you can do about it and, B, even if you could do something about it, you might want to do it if you were in the paper industry. But if you are Secretary of the Treasury, you do not want to.

I would say that we have been blessed with Rubin and Summers and with you, Secretary O'Neill, that on this one issue, that there has never been an equivocation. There has never been any politics involved in it. I think that the country has benefited a great deal, even though individual parts of the economy might benefit, but at a great expense to everybody else. I guess that is my view. I worry about this. But by the time I get to it on my list, every night I am asleep.

[Laughter.]

Chairman SARBANES. Senator Corzine.

Senator CORZINE. Well, I do not fall asleep thinking about the dollar, either, in that particular category of concerns.

But I do wonder when you think about the current account, which I basically think is reflective of the underlying trade imbalances that we have, and it has some other elements in it, that a lot of the financing that goes on in the world, these flows which are covered by this $1.2 trillion, which you say is a lot of—I am a little more comfortable with speculators based on where I came from than maybe you are.

[Laughter.]

In the sense that it allows for the transition of the flow of dollars from one place to another, or assets. But it strikes me that while managing the dollar is not necessarily the issue, worrying about that underlying trade deficit is a real issue.

And if it were to change our views with respect to how people look at the capital markets in the United States because they do not feel they are as secure as they might have thought they were at another point in time, which can happen for political reasons or it can happen for underlying economic conditions, the kind of deficits that Senator Gramm is concerned about, which, by the way, seemed to be reappearing in relatively substantial amounts.

You can then have a completely serious series of events, like changing price levels and higher interest rates. I think we will hear Mr. Bergsten talk about that kind of scenario.

Those things do happen. They have happened in history, that other countries ran large trade deficits. I think that there are reasons to be concerned about underlying trade conditions that work against our Nation, even at a macrolevel. Get away from the forestry because, cumulatively, these things end up setting a vulnerability that is actually more serious than the Chinese reserves building up $50 billion, which I think is a drop in the bucket.

But if the investors in American stocks and bonds decide to get out, that is a lot easier to do than selling that building. Only one holder of those is the central banks or the reserve holders. And that is a serious concern. It is a serious concern if we see an erosion in our stock market because people do not have confidence in our accounting systems or our financial policies.

That to me is a bigger worry than where the dollar is at a given point in time. And that is why it concerns me when you say it is irrelevant because it is relevant to the underlying economic conditions, which I agree with you, ultimately, are what determine where people want to put their money.

There are issues here that could change people's perceptions about the United States, our fiscal policy, the management of our internal structures that surround our markets, the accounting issue being one that I am concerned about. And so, isn't that shock issue a real concern for anyone who is responsible for policy, and shouldn't we do things that try to advance more security with regard to those in the long run?

Secretary O'NEILL. Indeed, I think I am very sympathetic to your notion that we should look at underlying trade relationships. I also am frankly much more interested in what we can do to advance the cause of more exports from the United States. And with that, the development of the world.

I am sure you all know this, there is still 1.2 billion people in the world living on less than a dollar a day. And if you can imagine raising their standard of living so that they could demand plywood from the United States and plumbing fixtures and the other things that we all take for granted, we would quickly get rid of the worry about current account deficit because we would be exporting goods and we would be creating well-paying jobs for people here in the United States that are demanded by people who are growing into something approaching our standard of living.

So, I see this in a fuller sense because I am not really infatuated with finance as the prism for thinking about everything. For me, it is a derivative question. Finance is a derivative question, not a primary question.

I am very interested in your notion that, yes, we should be worried about this and we should be working on passing the trade promotion authority so we can get on with opening up markets to U.S. goods. And we can be helping people to realize a decent life instead of the misery so many of them are living in today.

On your other question about the concern that investors would make what I would characterize as a cliff decision to withdraw from the U.S. market, indeed, I do think that we have to be very careful about the mix of monetary and fiscal policy so that investors outside of the United States look at what we are doing and take comfort in what we are doing, that we are not running unsustainable excesses that would weaken their claim on U.S. goods and services because we are running policy that is a folly.

So, I think, indeed, we have to pay a lot of attention at the Government level to running sensible, sustainable fiscal and monetary policies and giving every bit of encouragement we can to the continuation of the extraordinary level of productivity growth that we are seeing now.

We are expecting when the final numbers are completed, that the first quarter rate of productivity growth in the United States is better than the 5.2 percent that we saw in the fourth quarter, which is truly extraordinary and I think should give lots of comfort to investors around the world, that the differential rate between productivity growth in the United States and every place else is just phenomenal.

And when I sit down and talk with the chancellor of the UK and Eddie George, the Governor of the Bank of England, they just cannot figure out how we can be doing so extraordinarily well in productivity growth while they are still limping along in the 2 percent range, and have been for a very long time. It is not even a subject in Continental Europe. They just cannot imagine how their productivity growth could begin to approach what we have demonstrated we can do.

Senator CORZINE. Two observations.

First, these shocks do occasionally happen. We had one in 1987 that was pretty clear when people evacuated markets at a given point in time. And it has real impact on the underlying economy. I know you are aware of that.

Second, if you are concerned about the underdeveloped world, the United States—and I think investment is great for the United States. But the idea that we are sucking up most of the capital

that is freely formed is an issue that I think can be a concern for the development of a lot of the underdeveloped world.

Frankly, I do not know that that relates to TPA. I think it has a lot to do with those internal structures and viabilities and political stability of a lot of the countries. So one has to figure out what is the most important ingredient to actually change what those conditions involve.

Secretary O'NEILL. I believe, these things are very much related to each other. And it probably escaped your notice because it did not get much attention, but when the G–7 was here 10 days ago, we did something which I think is profoundly important.

We resolved that we are going to work with the developing world to move them all toward a condition of investment grade sovereign debt. And you will understand and you have indicated by what you just said, in order to do that, there has to be a real rule of law and there has to be enforceable contracts, and there has to be an attack on corruption. And with those conditions, we can begin to help them create a basis for better competing for capital flows.

Now, I also believe this. I do not believe economics is a zero-sum game. I think the amount of money that is available for capital formation and capital investment is not limited to the amount that we are now producing.

If we can grow our own economy at 3½, or maybe even a little better than that percent of annual growth, we will throw off more capital and that capital in turn, if it is properly invested, will produce more economic growth and more economic growth will throw off the capital that is required to bring others along.

I really do believe the idea that capitalism at its best is a perpetual motion machine, or as close as the mind of man has been able to come, and that we are not doomed to live with the amount of capital that is now available as a limit for the whole world's growth.

Senator CORZINE. Thank you. Mr. Chairman.

Chairman SARBANES. Mr. Secretary, I want to come back to this basic point. I am really taken aback that we have a Secretary of the Treasury who does not perceive any problems associated with this large current account deficit. Now that flies directly contrary to what virtually every other economic observer is telling us.

Business Week recently ran an article: "U.S. Debt Overseas Stirs Up Trouble At Home." The growing current account deficit might set the United States up for a fall. And they say the following:

> The United States mounting external debt is clearly the most crucial structural problem facing the economy. And unlike other recent economic troubles, there may be no easy way out.
>
> The January and February increase in imported goods was the largest 2 month rise in two decades. Last year's current account gap hit 4.1 percent of gross domestic product and it could reach 5 percent by the end of 2002. That would be the largest rate in the industrialized world and larger than in many emerging market nations.

Now, we asked Chairman Greenspan about this at the Joint Economic Committee, the consequences to the U.S. economy of a growing current account deficit. This is what he responded.

> The current account deficit is also a measure of the increase in the level of net claims, primarily debt claims, that foreigners have on our assets. As the stock of such claims grows, an even larger flow of interest payments must be provided to the foreign suppliers of this capital.

Countries that have gone down this path have invariably run into trouble. And so would we. Eventually, the current account deficit will have to be restrained.

Do you differ with that?

Secretary O'NEILL. That is all he said? He did not say at what level he thinks we have to do restraint or how he would restrain the current account deficit?

Chairman SARBANES. Are you prepared to concede that at some level it would need to be restrained? At some point is it a problem? Are you saying to me, it is not a problem right now, but it could be a problem? *Or,* are you saying to me, look, this is a meaningless concept. It is really irrelevant. It is not something we should worry about now or in the future or at any time. Forget this kind of thinking. That is the approach you originally took, I think. Is that your position?

Secretary O'NEILL. Well, I would want to look at the composition of where the money is and the circumstances that exist in the rest of the world.

The implication of saying, yes, we should constrain the current account deficit is, as I said, as I have looked at the best academic work I know of, all the interventions that have been modeled would do damage to the U.S. economy if we decided to reduce the size of the current account deficit.

I do not find it very appealing to say that we are going to cut off our arm because some day we might get a disease in it, and this is an anticipatory move. I just do not understand the thinking that treats what I consider to be an artificial, intellectually useful construct, and then take it to a policy conclusion that does damage, that we decide to do damage to our own economy because of this artificial construct. I do not find that appealing, no.

Chairman SARBANES. Let me go to another line of questioning. This issue leaves me very concerned because we have a Secretary of the Treasury who just says there is no problem. Everyone else is telling us there is a problem in varying degrees, and they have different approaches as to how to deal with it. But they are not saying, look, just forget about it. Just go on about your business.

On the currency manipulation, and the Treasury found that there wasn't any, but there is a general view that the net purchases of foreign exchange by the Bank of Japan in recent years probably held the yen at a significantly lower level than would have prevailed based on market forces alone.

China, which has had a running current account surplus of about 2 percent of GDP, so they are running a very large trade surplus, they have also had an enormous inflow of foreign direct investment. In fact, the Treasury found that their bilateral trade surplus with the United States was $46 billion, just for the second half of 2001.

Ordinarily, with a sizable trade and current account surplus, and a large inflow of foreign direct investment, your currency would appreciate. But that has not happened in China. They have avoided that by acquiring huge amounts of foreign assets, in effect, doing what the Japanese are doing. In fact, your own report says that they expanded foreign reserves by $32 billion in just the second half of 2001.

Now why doesn't this represent a concerted policy on the part of China, to get the trade surplus, to get the foreign direct investment and sustain that position by making the purchases, huge purchases of foreign assets, in order to hold their currency in place, all to their advantage? That is not the workings of the market forces. They are intervening in the workings of the market forces in order to sustain an advantage, are they not?

Secretary O'NEILL. I do not know. What would you prescribe as a policy intervention? Which one of those things would you see us changing somehow?

Chairman SARBANES. I think you have to look at something like the Plaza Accord again. You have to address, in effect, the overvalue of the U.S. dollar in relationship to that. If they won't, in effect, allow their currency to depreciate, if they seek to sustain it in this way, then you have to do it on the American side.

You are putting our manufacturers in an incredible position, it seems to me. They may be quite competitive. You talked about the productivity improvements. It is a real tribute to labor and to management that have been doing that. But they are coming and they are saying to us, look, we are just at a 25, 30, 35 percent handicap because of the currency. Not because of the underlying economic realities.

Then you say, well, the currency value is going to be set by the market. But then we look at what some of these major trading partners are doing who are running these very large trade surpluses with us and it looks as though, pretty clearly to me, that they are intervening in ways to affect the currency relationship in order to sustain a very substantial and significant trade advantage.

I will concede to you, on many of these problems, just as you said earlier about the current account deficit, it is a very difficult call to figure out what to do. I do not gainsay you on that. But that is different than saying there is no problem here. That is different than saying, it is all irrelevant. It really dosn't matter. The whole concept is faulty and we are just not paying any attention to it.

Secretary O'NEILL. I think, just as you said, it makes a lot of sense to pay attention to this issue, but at the level of detail that we are talking about it now.

When you mentioned the elements of what China is doing, I would submit to you, at least for myself, looking at this data, it is not at all clear to me that China has been able to change the relation of its currency to the dollar because of the combination of policies that they are running. In fact, it is not clear to me that any nation has enough reserves any more to run even an intermediate length intervention program that the market does not believe is associated pretty directly with the expectations for discounted productivity expectations as between countries.

It is true that I think it is clear on the face of it, I have been to China and sat down with the Governor of the Bank of China and talked with them about their currency regime and their intentions toward the rest of the world. And it is true that they are running what I would characterize as a semisoft peg. But I do not think, however much of their reserves may be, that they can get away very long with, in effect, defeating the market or producing a different relationship between their currency and the other major cur-

rencies in the world by using reserves to do it. And I think if it were true, then Argentina would not be where it is today.

Chairman SARBANES. First, I think the Chinese and Japanese are very skillful about this.

Second, if the United States is not resisting what they are doing, but, in effect, is going along with it, which is essentially what would flow out of an attitude that says, this is an irrelevant concept and there is no problem here, it makes it easier for them to work this game to their advantage. That is what is happening.

The figures just will not sustain, it seems to me, the position you are coming from. I think there is a problem. You keep saying, no problem. Manufacturers say that there is a problem. Economic commentators say there is a problem. You say, no problem. Well, look, as long as you say no problem, then their ability to have an impact is enhanced, not diminished, in my view.

Secretary O'NEILL. Senator, may I say just one word to that?

Chairman SARBANES. Sure.

Secretary O'NEILL. Again, I look at the objective evidence and I hear Japan. And I noticed this. In the last 12 years, the Japanese economy has performed dismally at something close to an average GDP growth of zero, as compared to a spectacular performance by historical measure for the U.S. economy over the same period of time. And we appear to be headed back toward our potential rate.

The same facts pertain to Western Europe. I do not find a basis for deciding that what we have been doing is fundamentally wrong in the experience that we have had as an economy as compared to any other economy in the world.

Chairman SARBANES. We have heard you talk about short-term benefits and long-term vision and so forth in a different context in talking about the budget, having sort of self-discipline and so forth. The fact of the matter is that we are building up these large obligations. We will have to pay or service those obligations into the future. So the gap between what we must produce and what we can reserve of that production for ourselves is growing because more and more of it is going to have to be committed to servicing these foreign claims that we have built up.

You may say, well, the economy is going well. Everything's hunky dory, and so forth and so on. But, nevertheless, this burden continues to build. And it carries with it, it seems to me, potentially very severe problems in the future. And you are the only one I find who denies that. Alan Greenspan says, at some point, we have a problem. Most everybody says that. I cannot even get you to say here today that at some point, we would have a problem. It is still no problem.

Senator Gramm.

Secretary O'NEILL. As you know, Senator, I am not reluctant to be alone.

[Laughter.]

Chairman SARBANES. I understand that. That is pretty clear. But you worry when the Secretary of the Treasury of the leading economic power in the world is pursuing an attitude and a policy that no one else thinks is on all fours.

Senator GRAMM. First, I would like to say, Paul, that I appreciate what you said today. I think it is very important, it is very tempt-

ing in this world we live in, in politics, what I guess would be the politics of political correctness, for people to say, oh, yes, there is a problem.

You fall in love with somebody and they fall in love with you. Well, there is a problem because something could happen to them. There is a problem at the bottom of every good thing. To me the problem with going around talking about the problem is that there are people who have a vested interest to create a problem for their own benefit. I do not blame them. I am not being critical of them.

It seems to me that the cold reality is that even if you wanted to manipulate the value of the dollar, that you could manipulate it maybe for a week. And that is for our financial position, and it would be money completely squandered. I think that that is the first place I am coming from.

Second, we are all accustomed from early age, neither a borrower, nor a lender be. The plain truth is our country was built with foreign money from the time the first Pilgrim stepped on Plymouth Rock. At least until a couple of years after World War I, we were far and away the greatest debtor nation in the world.

The British built our railroads. They built our canals. They built post roads. They invested in our manufacturing. But all those were good investments. So it was true, we had to pay all this money to Britain, but we made more money. Maybe I am so poor because I have never been a debtor. But I was never confident enough that I would have known what to do with the money any way.

The one thing we could do that would clearly lower the value of the dollar would be increase domestic savings rates, no question about it. If we could get Americans to save more money, we would depress real interest rates and we would change the flow of capital. And that would be a positive for the world, as well as for us. So trying to create incentives or an environment to encourage thrift, I think all those would be very positive things. But I think, in the end, when you get right down to it, obviously, there are a combination of circumstances whereby current account deficits could become a problem.

Chairman SARBANES. Were you nodding your head to that?

Secretary O'NEILL. I was. I agree with this formulation.

[Laughter.]

Senator GRAMM. It depends on what is causing it.

Secretary O'NEILL. Right.

Senator GRAMM. That is the factor. Looking at the underlying things. And as I look at this trade deficit, I do not see anything right now we would want to change that is causing it. It is not as if it doesn't accrue benefit to some people.

The other day, I had left a shovel I was using in a truck, the shovel was gone. I had a limited amount of time, so I went to Home Depot and I was going to buy a shovel. I bought a shovel for $4.52. Now, I would say that never in the history of the world, has a quality product sold for less than that. The plain truth is we live in a golden age. Now if I were manufacturing shovels, I would be damned unhappy about it.

[Laughter.]

I would be calling me up, if I were a manufacturer in Texas—I do not think we have any shovel manufacturers in Texas. But,

I would be saying, we need to do something about it because I am going out of the shovel business. And if you are in the shovel business, it is a terrible thing. But if you are buying shovels, it is not a terrible thing. And Government has got to balance all these interests.

The only way I know to balance them is do it in a way that in the long-term benefits the most people. And it seems the way to do that is freedom and trade and that in the long-term, that is what benefits people the most.

So there is a dark side of it. If you are trying to sell products on the world market or compete against imports, this high-value dollar with this massive inflow of capital, which, God knows, we do not want to stop and we could use more of it in Texas. The dark side of it is it does hurt some people. But any change in any policy hurts somebody. The vacationer is hurt by rain. The farmer is helped by rain. Anything you do has advantages and disadvantages.

I guess if you are going to worry about it, you can. But in the end, I do not know under the circumstances we face now, I guess my view, and I will stop, Mr. Chairman, is I do not know what we could do differently other than better Government policies that would encourage more thrift in the United States.

I do not think we ought to be discouraging people from investing in America. I do not think we ought to blockade our ports or impose tariffs. In fact, I am not sure a tariff would do anything to this problem. If you put a tariff on everything, exchange rates would change and it would have no effect. Only if you put it on some things not on others, do you help anybody.

So, I think it is so tempting to say under these circumstances, yes, there is a problem. And I do not know exactly what Chairman Greenspan was referring to, but I just think that it is important to have somebody, and this happens to be you today, who says, I do not see a problem as to where we are now with this that we would want to fix. I think that is right. And I agree with it. But I do not agree with you about speculators.

Secretary O'NEILL. You do not?

Senator GRAMM. No. I knew you were a manufacturer when you said that.

[Laughter.]

Speculators are public benefactors who make money by making markets work better. And God bless 'em.

Secretary O'NEILL. Let me substitute manipulator for speculator.

Senator GRAMM. Well, manipulators in a market like this lose their shirt.

Secretary O'NEILL. That is what I want.

Senator CORZINE. Senator Gramm, I have never loved you so much.

[Laughter.]

Senator GRAMM. Well, I give credit where it is due.

[Laughter.]

Secretary O'NEILL. May I make just two quick points?

Senator GRAMM. You did not get rich without providing value.

Secretary O'NEILL. Just two quick points, Senator. Thank you very much for your comments.

First, on the issue of current account deficit. Economists—we did not know what this was back in the 1800's. But it turns out we had a huge, overwhelming current account deficit in the late 1800's. I guess it is a good thing that we did not know about it. We might have stopped the British investment.

Chairman SARBANES. Well, does the same thing work today? The world's most advanced economy, as opposed to a nation seeking to develop itself. You apply the same test.

Senator GRAMM. You develop it.

Secretary O'NEILL. One of the things that I find, frankly, a little disconcerting about the notion of a current account deficit, and, again, I think it is a static concept.

I have to tell you what I was doing when I was running Alcoa. Yes, I was borrowing money and getting more equity investment. But I was taking it around the world. So the idea that it was stuck here, the fact that ownership here did not mean it was stuck here. It was helping to create economic development around the world.

Second, the other point I wanted to make was about this issue of savings. Inherent in that is a sense that we here in Washington know better than what individuals are now doing collectively they ought to do. I think that if you really stop and think about it, you really believe we here in Washington know better what individuals ought to do about savings and how we measure savings.

Many people think their home is a savings and in fact, the evidence has demonstrated that people are getting real savings and ascension into the middle class by homeownership, which is an important form of savings. The other face of that, of course, is that we have more savings and we have less consumption. So these are not questions without consequence.

Chairman SARBANES. Senator Bunning.

Senator BUNNING. Chairman Sarbanes, thank you. I have heard enough conversation. I pass.

Chairman SARBANES. Jon.

Senator CORZINE. Mr. Secretary, I want to go back.

Chairman SARBANES. I told the Secretary that we would have him out in short order. Go ahead.

Senator CORZINE. Okay. It strikes me that we have a risk by this current account cumulative element that has built up over the years. And that is a dynamic. It keeps growing and our trade issues are ones, and it is a problem at a microlevel for a lot of individuals. There is no trade adjustment kinds of facilities that are accompanying a lot of the problems that end up occurring as a function of exchange rates. And if they are sustained at relatively high levels, whatever that might be, then I think we have reason as public policymakers to wonder whether the system is working fairly.

We have talked about China with the soft peg. And the fact is that that is an intervention into the market, not because of their purchases of dollars on the market, although, you know, at the margins some place, that increases the value. But if their currency depreciates versus the dollar, even within their pegged range, it undermines our manufacturers' ability to compete fairly in a marketplace, if one is talking about fair markets.

So, I think that is a legitimate problem. And if you put that cumulatively across a lot of different countries in the world, and there are places where there are soft pegs in other areas—you look in a lot of the developing world, there are soft relationships on what currencies are.

I do not know. I think that is the case in Korea. I think that is the case in Taiwan. I think that is the case in the Hong Kong manufacturing areas.

And with smaller currencies, it is easier to manipulate and opposed to how it is with respect to the yen or the dollar or the Euro.

I think that there are other structural elements of the marketplace which you are trying to address here. But I think our manufacturers and our workers end up on the short end of the stick with regard to how these systems work.

I am not arguing that we ought to be in the manipulation of the currency markets. But I think we have a real policy responsibility to do something about changes in some of these structures that work to the disadvantage of American workers and American business. I do not think that all of those are not necessarily in the trade arena. They are in structural reforms that I think we have the impact to have real change brought to bear on how some of these markets work.

A lot of these things do not even hit the radar screen of trade agreements. They are the regulations that slow down the flow of how people can participate in the markets. And that I think is a serious problem and I think it contributes to the long-term risk which has to do with what is the nature of the structure of American markets, whether people lose confidence in our markets because our accounting statements do not make sense or that we end up running huge deficits at the Federal Government that competes for that flow of inflow of capital. I think these things are serious and they are potentially riskier in a dynamic context because we build up these current account deficits over a period of time. I guess I am siding with the Chairman here that we have something to be concerned about.

Senator GRAMM. That is a smart thing to do. That is a very smart thing to do.

[Laughter.]

Chairman SARBANES. Mr. Secretary, we promised you that we would have you out, actually a little sooner. This has been a very interesting session, as it invariably is when we have the opportunity to exchange views with you. As you depart, I want to leave you with one image in your mind. This is the real foreign exchange value of the dollar. This is 1980. This is 2002.

This was the Plaza Accord. And we have heard this morning that if you try to do something, it won't sustain itself. But it worked for quite a period of time. Now, we are back up here. My anticipation is that this is going to go, it will be above where we were at the time of the Plaza Accord. So, I leave that with you. The Treasury, in effect, brought others together and took an initiative to try to address that.

Secretary O'NEILL. May I make one observation about the basing point in the chart for 1980?

Chairman SARBANES. Sure.

Secretary O'NEILL. I would remind you, that around 1980, the interest rate in the United States was 20 percent and the unemployment rate was 11 percent.

And so, if 1980 is a desirable position, that is not my notion of desirable economic circumstances. In fact, if you look at the period since—it is hard for me to see from here, but it looks like 1994, 1995, when the value started rising. We have arguably had among maybe the five best years in our economic performance in modern history.

Chairman SARBANES. Well, accepting all of that, we still have, it seems to me, a real problem here.

Thank you very much.

Secretary O'NEILL. Thank you. I will read the transcript of what follows very carefully because I want you to know that I do not have a closed mind on these subjects. I am open to listen to information and insights that can help us advance policy in a constructive way. So, I do not want you to take from what I have said that I think I have the answer. No one else knows what they are talking about. I just have not seen compelling evidence that is connected to possible public policy levers that would advance the cause of our society.

Chairman SARBANES. We have some very good panelists coming, and I am encouraged to hear that you intend to look carefully at their testimony and the transcript.

Thank you very much for being with us this morning.

Secretary O'NEILL. Sure.

Chairman SARBANES. If the panel would come forward and take their places, we will continue.

[Pause.]

Chairman SARBANES. We are pleased to have a distinguished panel now to address this issue. I believe they were all here at least during part of the Secretary's testimony and exchange. So, we will proceed now, and I will introduce each as we move across the panel, instead of everyone at once.

First, we will hear from Richard Trumka, the Secretary Treasurer of the AFL–CIO.

STATEMENT OF RICHARD L. TRUMKA
SECRETARY–TREASURER
AMERICAN FEDERATION OF LABOR AND CONGRESS OF INDUSTRIAL ORGANIZATIONS

Mr. TRUMKA. Thank you, Mr. Chairman, and Members of the Committee.

Chairman SARBANES. And I would say to the panel, your full statements will be included in the record, and if you can summarize them, we would appreciate that very much.

Mr. TRUMKA. I will do just that, Mr. Chairman.

I am glad to have the opportunity to talk with you today on behalf of the 13 million working men and women of the AFL–CIO, about the economic impacts of the overvalued dollar.

As we struggle to escape the grip of recession, the overvalued dollar represents a serious problem. It is also causing long-term damage by destroying our manufacturing base. Failure to redress

the problem risks undermining our fragile recovery and pushing us into a double-dip recession.

Manufacturing is ground zero of the recession, and its troubles are intimately connected to the dollar. Since March 2001, we have lost 1.4 million jobs, of which 1.3 million have been manufacturing jobs. Manufacturing has therefore accounted for 93 percent of all job losses despite being only 14 percent of total employment. Today, manufacturing employment is at its lowest level since March 1962.

Business has slammed on the brake of investment spending, but fortunately the American consumer has kept the recession milder than anticipated. However, a strong recovery that restores full employment needs a pick-up in investment spending, and that will not happen as long as currency markets give a 30 percent subsidy to our international competition.

Over the last 5 years, our goods trade deficit has exploded, costing good jobs across a wide array of industries. Last year, in the paper industry there were mill and machine closures at 52 locations, all considered permanent, indefinite or long-term. In the textile industry, 2 mills per week closed in 2001, and closures continue this year.

The weakening of the yen has given Japanese car companies a huge price advantage. The result has been loss of market share by our Big Three automakers that threatens some of the best jobs in America.

Boeing, which operates at the cutting edge of technology, is losing market share to Europe's Airbus. And losses today mean future losses because airlines work on a fleet principle. They will therefore order Airbus aircraft 5 years from now when they expand their fleets.

Moreover, job losses are not restricted to manufacturing. Tourism and hotels are hurt by the strong dollar, and film production is moving offshore to cheaper destinations such as Canada, Australia, and New Zealand.

Many of these jobs will never come back. These are high paying jobs that have been the ladder of the American Dream for millions of Americans. But now we are kicking the ladder away.

Manufacturing has faster productivity growth, and productivity growth is the engine of rising living standards. But now we are shrinking our manufacturing base, and that is bad for future living standards.

The Administration, as previously noticed, has refused to address these problems. Arguments for a strong dollar, in our opinion, simply do not wash.

Inflation is not a problem, and there is no evidence that a lower dollar will lower the stock market or raise interest rates. Those who say we need a strong dollar to finance the trade deficit have the reasoning backward. We need to finance the trade deficit because we have an overvalued dollar.

It is time for a new policy that puts American jobs and American workers first. It is unacceptable that Japan depreciates its currency. This will not solve Japan's problems, and will only export them to its neighbors and to us.

China exemplifies all that is wrong with currency markets. It has a massive trade surplus and vast inflows of foreign direct invest-

ment. In a free market, China's currency should appreciate, but it does not because of government manipulation. This is a problem that appears in different shades in many countries.

American workers are paying the price for currency manipulation. Trade cannot be fair when we allow countries to manipulate exchange rates to win illegitimate competitive advantage.

Those who argue that we can do nothing about exchange rates abdicate, I believe, the national interest. The historic record and the 1985 Plaza Accord intervention show that we can. Academic research shows the same. Just as we manage interest rates, so too we can manage exchange rates.

Currency markets are speculative and respond to policy signals. The Treasury and the Federal Reserve must take immediate action with their international partners. The upcoming G–7 summit provides an appropriate moment to do so.

Beyond intervention today, we must avoid a repeat of today's overvalued dollar, just as today's problems are a repeat of mistakes made in the 1980's. The dollar must be a permanent focus of policy, and the Treasury and the Federal Reserve must be made explicitly accountable.

Every trade agreement, Mr. Chairman, must include strong language that rules out sudden currency depreciations that more than nullify the benefits of any tariff reductions.

The Senate Banking Committee has a vital oversight role to play in ensuring that the Treasury and the Federal Reserve live up to these obligations.

Thank you for the opportunity to testify and submit a report, and I would be happy to answer any questions that you may have.

Chairman SARBANES. Thank you very much. We appreciate your testimony.

Next, we will hear from Jerry Jasinowski, President of the National Association of Manufacturers. Jerry has been before the Committee a number of times in the past. We are pleased to welcome him back.

STATEMENT OF JERRY J. JASINOWSKI
PRESIDENT, NATIONAL ASSOCIATION OF MANUFACTURERS

Mr. JASINOWSKI. Thank you very much, Mr. Chairman, Senator Gramm, and all the other Members of the Committee for your leadership on this important issue.

I have enormous respect for Paul O'Neill. He is an old friend. I think his leadership and his dedication to the country have been extraordinary. And I think that it is only in the spirit that he himself invoked, which is to say, he is welcoming a debate, that I would like to confine my oral remarks to a fairly direct response to what the Secretary said, because I think that will be the most useful thing to the Committee.

My prepared statement makes the case for why we think the dollar has run amok, not just for manufacturers, but also for this broad coalition here—and why it is bad for the economy. It is not just a matter of a few special interests indicating that this is important. There is a growing global consensus.

Let me make five points that go fairly directly to what Secretary O'Neill talked about, that I think will be useful to the Committee.

The points all go to the argument that, essentially, the Secretary is not addressing the reality that we see and the growing consensus in the world sees.

The first reality is, there is an extraordinary consensus now of academics, business leaders, union leaders, international leaders, and others, who say the dollar is overvalued. And in my statement, I talk about everybody from the IMF to particular economists who say it is overvalued by historic standards.

I think for the purposes of the Committee, though, the Big Mac index illustrates most dramatically the reality. This is an index the *Economist Magazine* uses to determine the extent to which the dollar is overvalued. It is the cost of a Big Mac in places around the world. The index is, according to the *Economist Magazine* now, more overvalued than it has ever been in history.

I think the chart you showed, Mr. Chairman, reflects this. The Big Mac index reflects the reality in terms of real products and is similar to the kinds of issues associated with products that manufacturers and agriculture face very broadly.

The second reality that I think the Secretary really does not address is the fact that the current account is a growing problem and that it is directly related to the exchange rate.

I have here a chart, which is in my testimony as well. The chart essentially tracks, as you can see, the ratio of imports to exports, and the exchange rate for the dollar index.

What you see is an unequivocal correlation between——

Chairman SARBANES. Which line is which in that?

Mr. JASINOWSKI. The top line, the darker line, shows you the ratio of imports to exports, and that is a rough proxy for the trade deficit.

Chairman SARBANES. Right.

Mr. JASINOWSKI. What we are talking about is the current account. Unequivocally, you see that the dollar exchange rate affects that.

Now the Secretary says in his report, and others will say, that the current account and our trade problems are affected by interest rates, growth, and all the things you, Mr. Chairman, and the Committee, know very well. But I am here to say that, right now, the most important thing affecting the current account problems, the growing trade deficit that we have heard so much about, and our enormous loss of exports, is the exchange rate.

The third reality that the Secretary does not address is the enormous negative effect that this is having, not just on manufacturing, but also on the entire economy. It affects the trade deficit. It affects employment. It affects growth. It affects the international global stability on which we are all resting our hopes for a recovery in the economy. That is why the IMF and many others have suggested there is a problem.

The fourth reality, and this gets to the heart of what do you do about this, is that the Secretary is a major part of the problem through his statements that fail to recognize the problems associated with the dollar trade and the current account. This misinformation distorts the markets that in fact are supposed to be functioning correctly.

I am here to argue that we do not have a perfect market in terms of the currency markets. We do not, principally because the Treasury has taken the policy position that it is not a problem. Second, and most importantly, by being for a strong dollar, you put a floor under the currency. So, I would argue that we do not have a perfect market in the exchange rate for that reason, and that the Treasury is part of the problem.

My final point, Mr. Chairman, is that the solution is therefore, at least in a first instance, pretty simple. That is, that the Treasury ought to simply acknowledge that the current account is a problem, the dollar is a problem, and it ought to get out of advocating a strong dollar and instead say it is for a sound dollar based on market fundamentals. If we do that, I assure you we will not have a huge drop in the dollar. We will have a gradual movement back toward the equilibrium that all of us that are part of a sound dollar coalition are for. And I think that would mean less Government intervention in this market, in some respects, and a return to a truly perfect market.

Thank you, Mr. Chairman.

Chairman SARBANES. Thank you very much. Also, we want to thank you for this very well considered prepared statement, which we very much appreciate having. But I think it was helpful for you to directly address some of the points that the Secretary made.

Our next witness is Bob Stallman, President of the American Farm Bureau Federation. We do not usually have you before our Committee, Mr. Stallman, but we are pleased you are here today. We would be happy to hear from you.

Senator GRAMM. Mr. Chairman, could I just say a word about Bob Stallman, and I will be brief?

Chairman SARBANES. Certainly.

Senator GRAMM. I have known Bob since he was a rice farmer in our State. He started out as a farmer talking to his neighbors, became involved in the county farm bureau, became President of the Texas Farm Bureau, and became President of the American Farm Bureau.

I am sure Bob and I are not going to agree on the subject today, but I would like to say that Bob Stallman is living proof that talent wins out in America, if you have ability and ideas and you feel passionate about stuff, that your neighbors will elevate you and that starting out as a rice farmer in southeast Texas, you can become the spokesman for American agriculture if you have what it takes to become that. So it just reassures me, having known somebody this has happened to. Bob, we appreciate your being here.

Chairman SARBANES. Thank you.

Mr. Stallman.

STATEMENT OF BOB STALLMAN
PRESIDENT, AMERICAN FARM BUREAU FEDERATION

Mr. STALLMAN. Mr. Chairman, Senator Gramm, thank you for the kind words. Incidentally, for the record, I still am a rice farmer, though just not to the extent I used to be. It is a pleasure to be before this Committee today.

As the Nation's largest agricultural organization, our farmer members produce nearly every type of farm commodity grown in

America and depend on access to foreign markets for our economic viability.

We certainly appreciate this opportunity to testify on the importance of the exchange rate to U.S. agriculture. The exchange rate is the single most important determinant of the competitiveness of our exports. U.S. farmers and ranchers have been losing export sales for the past 3 years because the dollar is pricing our products out of the market, both at home and abroad.

Agriculture is one of the most trade-dependent sectors of our economy. Our sector has maintained a trade surplus for over two decades, but that surplus is rapidly shrinking. One of the primary factors affecting our declining trade balance is the strong value of the dollar.

We are also deeply concerned about countries that engage in currency devaluations in order to gain an export advantage for their producers. The real trade-weighted exchange rates for agricultural exports from our major competitors have exhibited a long-term trend of depreciation against the dollar, leaving it hard to conclude that this is not a deliberate monetary policy of these and other governments.

U.S. agriculture relies on exports for one-quarter of its income. In addition, and coincidentally, about 25 percent of the agricultural production in the United States is destined for a foreign market. With a strong dollar, we have the double challenge of our products being less competitive in foreign markets, while products from other countries are more competitive in U.S. markets.

There is a strong relationship between the value of the dollar and the domestic price of our commodities. As the value of the dollar rises, foreign buyers must spend more of their currency to purchase our exports, which causes them to decrease their consumption of our commodities, or buy from our competitors instead. The resulting drop in consumption drives U.S. commodity prices down even further.

The increasing strength of the dollar, and steady depreciation of the currencies of our major export competitors, has had a profound impact on our ability to export. In fact, the rising appreciation of the dollar is one of the primary reasons why the agricultural economy did not experience the economic prosperity that most other sectors of the U.S. economy enjoyed between 1995 and 1999. This is also a jobs issue. USDA estimates that 14,300 jobs are lost for every one billion dollar decline in agricultural exports. As a result, agricultural employment lost 87,000 jobs between fiscal years 1997 through 2000, a period wherein the real agricultural exchange rate was rising rapidly and U.S. agricultural exports were stagnating.

For some commodities, the rising value of the dollar has directly contributed to the export competitiveness of our foreign rivals. The strong dollar enables our competitors to expand their production and gain market share at our expense. Let me give you a few commodity-specific examples.

Beef: Since 1995, the dollar has appreciated 42 percent against the currencies of beef producing countries. And I know we had the Big Mac index over here, but that U.S. McDonald's Big Mac is going to have more foreign beef in it, given their recent announcement to purchase more beef from Australia. The relative exchange

rate, strong value of the dollar, has caused that economic decision to be implemented.

Fruits: From 1995 to 2000, U.S. imports of fruits and nuts jumped 33 percent, largely due to the dollar's 18 percent gain with respect to the currencies of foreign suppliers of these commodities to the United States.

Corn: The U.S. dollar appreciated 39 percent relative to the Japanese yen from 1995 to 1998, adversely affecting our corn exports to that market.

Soybeans: The cost of U.S. soybeans to Japanese buyers increased 8 percent from 1996 to 1998, due to the appreciation of the U.S. dollar, even though U.S. prices fell 18½ percent during the same period.

In conclusion, America's farmers are the most productive in the world. However, the comparative advantages that our producers generally enjoy are certainly mitigated by the rising appreciation of the dollar.

Exchange rate issues are certain to increase in importance for our sector, and if these issues are not resolved by macroeconomic policies, there will be continued pressure to find solutions in traditional farm and trade policies.

The effect of long-range financial planning at the farm and ranch level and the overall economic health of U.S. agriculture depends on more stable exchange rates that do not overvalue the U.S. dollar against our competitors' currencies.

Thank you, and I look forward to answering any questions at the conclusion of the presentations.

Chairman SARBANES. Thank you very much, sir.

Our next panelist is Fred Bergsten, who is the Director of the Institute for International Economics, and a frequent contributor to our discussions. We are very pleased to have you here, Fred.

STATEMENT OF C. FRED BERGSTEN
DIRECTOR, INSTITUTE FOR INTERNATIONAL ECONOMICS

Mr. BERGSTEN. Mr. Chairman, thank you very much. As I listened to the discussion this morning, there seemed to be two questions before the House.

Chairman SARBANES. Before the Senate.

Mr. BERGSTEN. Excuse me? Sorry. Before the Senate.

[Laughter.]

Bad error.

[Laughter.]

Change the words in the transcript.

[Laughter.]

Two questions before the Senate. One, is it a problem? And two, is there something you can do about it?

My answer to both is a resounding yes, and let me briefly summarize my statement in trying to answer those questions.

First, is it a problem?

We have to keep clearly in mind that there are not one, but two problems, a real economy problem and a financial risk problem.

The real side problem is the loss of output, loss of jobs, and loss of agriculture that were talked about. The financial risk problem

is the possibility that all this could come crashing down in a huge financial crisis with enormous consequences for the economy.

Now what is the size of the problem?

Since the dollar hit its all-time record lows in 1995, it has risen by 40 to 50 percent against the various trade-weighted averages that the Fed calculates every day. And that is like a rise in 40 to 50 percent in prices of the entire economy in world trade. When a company sees its prices go up 40 to 50 percent in a few years against its main competition, it is usually in Chapter 11. That is what has happened to the United States as a whole.

Every rise of 1 percent in the trade-weighted average of the dollar produces an increase of at least $10 billion in our current account deficit. And so it is clear that this rise of 40 to 50 percent in the exchange rate over the last 6 or 7 years explains the vast bulk of the half-trillion dollar trade deficit that we face today and which is getting bigger.

Indeed, we have projected the current account over the next few years on reasonable economic assumptions, and assuming no policy change, more of what we heard from the Secretary this morning, and no untoward external events, the deficit would hit 7 percent of GDP—that is $800 billion—by 2005 or 2006.

Every study ever done, including by the Federal Reserve itself, and they published this, shows that once you hit 4 to 5 percent of GDP, you are in the danger zone.

Indeed, the big crashes of the dollar which have occurred once per decade since the early 1970's, have occurred without our current account deficit ever getting to 4 percent of GDP, the all-time high in the mid-1980's, before the Plaza Accord Agreement, and the 50 percent correction in 2 years, was 3.8 percent. We are well beyond that. We are headed toward twice that. We are clearly on an unsustainable path.

Now, in financing terms, what this requires is even worse than you think because we not only have to import $500 billion of capital each year to finance our current account deficit but we also have to cover our capital outflows.

Remember that the United States itself invests lots of money abroad. This is a good thing. I am certainly not criticizing it. But that amount is another half-trillion dollars a year. So the result is that the U.S. imports a trillion dollars of foreign capital per year, to balance the books, which is a little more than $4 billion every working day.

It is certainly not a bad thing. The point is, if that $4 billion per day dropped to just $3 billion, let alone reversed into an outflow, the dollar would fall sharply. And it would fall, by our calculations, at least 20–25 percent to get back to some kind of sustainable equilibrium level. Since markets overshoot, it would probably go much more than that in the short run.

That would cause sharp inflation, a sharp rise in interest rates by several percentage points, and a sharp fall in the stock market—a triple-whammy that would hit the economy. That is why I agree with the statements you made before that this is the single biggest risk to the U.S. economic outlook, and that the Secretary of the Treasury certainly ought to be concerned about it.

It is stunning that he said the things you quoted this morning that he did say. It is reminiscent—this is a nonpolitical statement, just an economic analysis—of what happened in the first Reagan Administration, with Secretary Don Regan and Beryl Sprinkel, which was the epitome of benign neglect.

That turned out to be so wrong and so costly to the economy that the second Reagan Administration had to reverse it, do the Plaza Accord Agreement, and drive the dollar down by 50 percent in the next 2 years. So it is not as if we have not seen this happen before. We have seen exactly this happen before. The Administration that permitted it to happen then had to reverse itself 180 degrees, enlist the rest of the world to help to save us from the enormous costs of that policy.

Second question, is there something we can do about it, as Senator Gramm, Secretary O'Neill, and others raised, and you yourself acknowledge? That is the more difficult question.

I believe there are policy changes that can rectify the situation substantially without significant adverse costs elsewhere in the economy. And that is because I believe, and I will try to document briefly, that sterilized intervention in the exchange markets works and can change currency movements in important terms.

The Secretary mentioned Allan Sinai and economic theory. There is something now in economic theory called multiple equilibria.

Economists have now realized that for any given set of economic fundamentals, there is in fact, a large set of possible market outcomes, glorified by the term multiple equilibria, indicates there is firm theoretical basis for what I am about to say. I would suggest a four-part change in policy.

First is what Jerry Jasinowski just said—change the rhetoric, absolutely.

Second, if the dollar were to rise further, as it may because of the rapid U.S. recovery, the United States and the G–7 should certainly lean against the wind of any new dollar rise. That would make it worse.

Third, however, and more importantly, we should now begin easing the dollar down toward equilibrium levels, and I will explain briefly why I think now is the time to do it.

Fourth, we should of course make it very clear to other countries that we will not tolerate efforts to competitively depreciate their currencies.

The Treasury Report is stunning in that it acknowledges huge intervention by the Japanese, but does nothing about it. I can tell you that immediately after the rise in the yen last fall, the Japanese began talking it down. I thought they had quit, but they are at it again this week.

The leadership of Japan's Ministry of Finance has been saying very clearly this week, after the yen rose four or five yen against the dollar, that any further rise would be inconsistent with our economic fundamentals and they are against it. They are again trying to avoid any rise in the exchange rate of the yen. And we should make clear that that is verboten and will not be accepted.

On U.S. currency policy itself, it was encouraging that Secretary O'Neill today, as for many months, did not repeat the term, "strong dollar." You will notice that he has assiduously avoided saying that

for some time now. However, he said, there will be no change in policy, so I suppose it has the same implication.

I would agree with what Jerry Jasinowski said, that the Administration should change the wording and now start supporting a sound dollar or some equivalent that made clear that they wanted to see it in sustainable equilibrium terms, in terms of our external position.

The presumed reason they do not want to change is they are afraid that the dollar would then collapse. But at a time when the U.S. economy is booming, as the Secretary said, with huge productivity growth, at a time when there is no dramatic growth in Europe or Japan to suck money away, I think it is very unlikely that a change in rhetoric would lead to a free fall, and that is why this is the ideal time to make the change—when we are doing well, when we are recovering strongly, and when the others are not doing so well, unfortunately. Now is the time to do it.

The worst policy is to wait until there is an inevitable change in economic circumstances that drives the dollar down when we are not in such good shape, when we cannot accept it so well, which would cause enormous costs to our economy. And so, it seems to me that now is the time to do it.

Final point, again, how do you do it? Change in rhetoric and direct intervention.

Notice that the Rubin–Summers Treasury intervened on three and only three occasions, from 1995 through the end of its tenure in 2000. Every one of those changes, in my view, worked like a textbook.

In 1995, when the yen was rising too far, got to 80, the dollar in fact was at its all-time record lows against both yen and Deutschmark. We intervened jointly with the G–7. We stopped the rise of those other currencies, stopped the fall of the dollar, turned it around, and within a few months, the dollar was headed up, and in fact, it has never stopped since. We were 100 percent successful.

In 1998, the yen was becoming too weak, just like it is today. It got to 145. The United Stated intervened, along with Japan, and stopped the decline of the yen. It stabilized in that range for a couple of months and then rose back to 100. It was a total success.

Third intervention, September 2000. The Euro fell to its all-time lows. The Europeans got upset. Again, that was pushing the dollar to get further overvalued. Joint U.S.–E.U. intervention stopped the decline on a dime. The Euro turned around, rose 10 percent, subsequently fell back halfway. It has been there ever since.

On my reading, in all three cases, three out of three, it worked. I believe, incidentally, the Plaza Accord was a huge success and the notion ex-post that it was just riding along going down the stream, frankly, is post hoc ergo propter hoc reasoning, and was not clearly in the minds of the people who did it at the time, who saw an enormous need to change the trend and do something about it.

There has been scholarly work by Franckel and Domingues at my institute. The Banca d'Italia's working with classified data suggested that every major intervention in the 1980's and 1990's worked and turned the currency relationships around in the desired direction.

So my conclusion is very simple. There is a big problem and there are policy tools available to deal with the problem without adversely affecting other parts of our economy.

At a minimum, we should try it. The costs are too high. The risks of trying this I think are very modest if it were to fail, but the prospects for success are very strong and I think that alternative policies should be pursued.

Thank you.

Chairman SARBANES. Thank you very much.

Our next panelist is Ernest Preeg, who is the Senior Fellow at the Manufacturers Alliance. We would be happy to hear from you.

STATEMENT OF ERNEST H. PREEG
SENIOR FELLOW IN TRADE AND PRODUCTIVITY
MANUFACTURERS ALLIANCE/MAPI, INC.

Mr. PREEG. Thank you very much, Mr. Chairman. It is a pleasure to be here today.

I will focus my remarks on one particularly disturbing aspect of the trade deficit, namely currency manipulation to commercial advantage by certain trading partners, and in particular, by China.

I do want to say, though, as in my written statement, that I see the current account deficit and accumulated foreign debt as a problem. The most immediate concern is that a rapid rise in our trade deficit this year, almost all of which will be in the manufacturing sector, could be the Achilles's heel for the hoped-for sustained recovery because it is hitting our investment sector particularly hard, and that is the lagging sector.

As for currency manipulation, the IMF clearly proscribes it. There is an IMF statute that members should not be manipulating their exchange rates to gain an unfair competitive advantage. And a principal indictor of such manipulation under IMF surveillance procedures is very precise. It says that members should not make protracted, large-scale interventions in the market in one direction—namely, to buy dollars and other foreign currencies—to keep their currencies down and to gain an unfair competitive advantage.

Japan has gotten the most attention on this because for several years, they have made such protracted, large-scale interventions, $250 billion all told. Fred has given some examples of this.

And I should state here, to clarify earlier discussion, what I call the great asymmetry in central bank intervention. If you are trying to keep your currency up, as Argentina did with the peso, you have to sell dollars. Everybody thus knows when you are going to run out of dollar holdings, and it is a limited time.

In the other direction, as we are talking here, when you want to keep your currency down low, that is manipulate it down, you can buy unlimited dollars year after year, indefinitely, as Japan and China have been doing—as much as $50 billion each year—to offset the market forces in the other direction stemming from a trade surplus, for example.

Turning to China, they have also manipulated their currency, but it is a more complicated situation. It has not received as much attention perhaps for that reason, because China has a fixed rate, but the currency is not convertible on capital account. In effect, the exchange rate is not really market-oriented.

But the facts are nevertheless very clear, as was cited earlier by Senator Bunning. Last year, for example, China had a $25 billion trade surplus, globally, and a $45 billion inflow of foreign direct investment. This would put major upward pressure on the exchange rate. At the same time, however, the central bank bought $50 billion, to take dollars off the market and ease the pressure.

More precisely, the Chinese central bank has taken away three-quarters of the upward pressure on its currency from the trade surplus and foreign direct investment. And here, again, another technical comment on the earlier discussion. What counts are not the gross flows in markets, a trillion dollars a day. Most of this is just in and out, offsetting. It is the net flow of trade and foreign direct investment, and the net borrowing of central banks that needs to be considered. And on this net basis, the numbers for Japan and China have been very large and have had substantial impact in keeping the exchange rate down.

So the net result, in my judgment, is that China has a substantially under-valued exchange rate for the yuan and the direct impact, of course, is a larger trade surplus with us—export jobs they gain and export and import-competing jobs we lose. There are several other benefits to China from its currency manipulation in my statement. I won't go into detail. One was mentioned earlier, that perhaps at some future point, they could use their excessive currency holdings for foreign policy leverage.

A more immediate benefit for China is that with $220 billion in their central bank—fungible money—there is no financial constraint to buying large amounts of armaments from Russia or elsewhere. They have huge amounts of money in the bank that they could use it for this, and for several other reasons as explained in my statement.

I agree with the others that we need a clear and forceful response to this now chronic trade deficit. It is headed toward record levels over the next couple of years. And a $3 trillion net foreign debt accumulation is headed toward $5 trillion by mid-decade. What should we do?

First, as Senator Gramm mentioned, we have to save more because we are currently living beyond our means. The foreign borrowing is not being used for investment, as was indicated, but mostly for immediate consumption. Eighty percent of our foreign borrowing, more or less, is for immediate consumption and we leave the consequent foreign debt to our children and grandchildren to pay interest and principle. I do not think that is right.

So, we need to save more. And at the same time, we have to get trading partners such as China and Japan to save less and consume more, so that their economies do not have to be dependent on a large trade surplus, for which they manipulate their currency. They don't now have a domestic economy growing fast enough, and thus rely on a chronic trade surplus to maintain growth. We need to achieve a better balance, to save more and not spend beyond our means. And others need to do the opposite.

The other immediate objective, in my view, is to stop others from manipulating their currencies so as to have bigger trade surpluses than they would have based on market forces alone.

We have a clear opportunity to do this in the IMF based on very explicit surveillance criteria. All we have to do is ask for a consultation to say that the others should stop their currency manipulation. We have never done that.

There is even an article in the GATT and the World Trade Organization, I believe Article XII, along the same lines. We have never thought seriously about that, either.

We should take steps, both through bilateral consultations, and within the IMF context in a more formal way, to try, particularly with East Asians including Japan and China to stop further currency manipulation, which distorts exchange rates from what markets would determine.

And for China, finally, the bilateral consultations should be a very high priority. We have a mutual interest in reducing the very lopsided, 5:1 trade imbalance, with $100 billion U.S. imports and only $20 billion exports, last year, and we should begin with the question—why is the bilateral trade so imbalanced?

We should request, clearly, of China, that the central bank stop buying dollars at $50 billion a year, and that they bring their exchange rate up by 10 percent, 20 percent, or whatever is a reasonable first step.

The longer-term transition of China to a fully convertible floating rate relationship with the dollar should also be discussed. We should look at this seriously because that is what I believe the longer-term objective should be. It is a mutual interest and it is the best way to avoid trade conflict from further unjustified Chinese currency manipulation.

Thank you, Mr. Chairman.

Chairman SARBANES. Thank you very much.

Our concluding panelist is Steve Hanke, a Professor of Applied Economics at Johns Hopkins University.

Mr. Hanke.

STATEMENT OF STEVE H. HANKE
PROFESSOR OF APPLIED ECONOMICS
JOHNS HOPKINS UNIVERSITY

Mr. HANKE. Thank you, Mr. Chairman, Senator Gramm.

Let me just briefly make a few points that pick up on some of the things that have been discussed in the morning session. My remarks will highlight points that are developed in my prepared statement.

Chairman SARBANES. We will include your full prepared statement in the record and we appreciate your condensing it.

Mr. HANKE. Thank you, Mr. Chairman.

We have hearings in which "exchange rate policy" is stated, as one of the phrases in the title of the hearings themselves. And interestingly enough, if you look at the U.S. evolution of exchange rate policy in general, we really did not have any coherent policy stated in the United States, until 1999, when Secretary Rubin, in April, articulated the policy.

Then Summers followed in September 1999, after he was appointed Secretary, and Stanley Fischer at the IMF weighed in with essentially the same conclusion in January 2001.

Now what did they say about exchange rate policy and why are their statements important?

There are three generic types of exchange rates—a floating rate, which Rubin and company said was suitable for the United States. And that is a rate in which the exchange rate itself is on autopilot. You only have a monetary policy. You have no exchange rate policy under a floating exchange rate regime.

At the other extreme, you have an absolutely fixed exchange rate regime in which an exchange rate policy exists, but monetary policy is on autopilot. And that would be things like orthodox currency boards or dollarized systems.

Rubin, Summers, and Fischer came to the conclusion that I think all economists have come to, and that is, in a world of mobile capital and free capital flows, those two extreme free-market, automatic systems are desirable. And everything else in between is undesirable.

Now what is in the middle?

A pegged-type system is in the middle. For example, Secretary O'Neill mentioned that China has a soft peg. Well, they do have a soft peg. And the reason the thing doesn't blow apart is that China has extremely rigorous capital controls—the capital account is completely controlled.

So those are the three systems and as you can see, as a matter of principle, the Chinese system would be undesirable, according to Rubin, Summers, Fischer and most economists, certainly the major consensus.

What does this have to do with the hearings?

Well, it has a couple of things to do with the hearings. The Bush Administration has never gotten around to articulating and reaffirming what Rubin and Summers did. And Krueger has never reaffirmed what Fischer did. So, we need some clarity. I think you should push Secretary O'Neill to come forward with some clarity on the U.S. broad policy position.

For the United States, we accept floating. Now that has some implications, especially for the strong dollar rhetoric. Our exchange rate policy is a floating exchange rate. It is not a strong dollar policy. A strong dollar policy is nothing but rhetoric and absolute economic nonsense. It doesn't mean anything in economic terms. The dollar's value is determined in the market and under a floating exchange rate, that determination is on autopilot.

So, I would agree with Jerry and Fred on this thing. Any adjective for the dollar—whether it is strong, sound, or weak—doesn't mean anything if you accept free capital mobility and a floating exchange rate because the dollar's price is simply on autopilot.

I think, Mr. Chairman, I see a red light on your little gauge.

Chairman SARBANES. Why don't you go ahead if you have a few more points you want to make.

Mr. HANKE. This rhetorical point would be one thing on which, oddly enough, Fred, we are in agreement.

Now let me mention something on which Fred and I probably would not agree. The world is already very much unofficially dollarized. That means that 90 percent of all foreign exchange transactions have the dollar on one side of the trade. Ninety percent of all commodities traded in the world are invoiced in dollars.

So, you do not have this so-called exchange rate problem that we have been discussing. They are buying and selling in dollars and invoicing in dollars.

Now, in terms of manufactured goods, Mr. Chairman, the issue gets a little bit tricky to sort out and make generalizations. But I can tell you that about 35 percent of exports from Japan are actually invoiced in dollars. They are dollarized. And almost 65 percent of all the imports going into Japan are dollarized.

The point here is, if you really want to get around these problems with exchange rates, Fred, and the competitiveness, uncompetitiveness, competitive devaluations and so forth, what we should do is try to encourage the official dollarization of most smaller countries—I am not suggesting Japan or Euroland because that would put them in the same currency bloc as the United States and we would not have to spend much time with these conversations because everyone would be buying and selling and invoicing and dealing in dollars. I would point out that, generally, the U.S. dollar can be characterized as a vehicle currency in the world that is truly dominant in staggering ways.

We had an earlier conversation about dollar reserves held at the Chinese central bank, as well as the Bank of Japan and changes in those. About 66 percent of all the foreign reserves held at central banks in the world are in dollars or assets denominated in dollars. So, I think if we go after every central bank using dollars in this way, in an official way, we have a lot of villains out there that we are going to have to go after, just not Japan and China.

Mr. Chairman, I appreciate your letting me overindulge on time. I think I have made some of the main points I wanted to make, in any case. Thank you for giving me the extra time.

Chairman SARBANES. Thank you very much, Professor Hanke.

I might mention that the Committee has received a number of letters from across the country from various manufacturers and producers with respect to this hearing, expressing their viewpoint which has been expressed by some of our earlier panelists here today, which we will place in the hearing record. What is the response to this dollarization statement that Professor Hanke made?

Mr. JASINOWSKI. I think it makes general sense. I do not know how far it can go in terms of dealing with the central problem of the strong dollar policy being advocated by the Treasury. But it does, I think, help on the demand side with respect to dollars. And therefore, I think it is good in that sense. It is also good in the sense of the dollar currency being a more stable currency than most. So, I would initially be positive toward that.

Chairman SARBANES. As I understand it, the assertion is that a good part of the Japanese trade is invoiced in dollars. I take it you then draw from that the conclusion that the exchange rate difference is not affecting the trade balance. Is that right?

Mr. BERGSTEN. Mr. Chairman, let me take a stab at that.

In this context, dollarization is a narcotic because, with most of the world's trade financed in dollars and with most of the reserves in central banks held in dollars it is very easy for us to finance these big deficits relative to other countries whose currencies are not widely used in international finance.

Charles de Gaulle 35 years ago said that the United States ran deficits without tears. And the reason he said that was because he argued, and he was right then, and it is happening right now—that foreigners acquire dollars as they run their trade surpluses, tend to hold them in dollar terms, and that, ipso facto, finances our deficit.

So it is quite easy for us, relative to anybody else, to finance these huge boxcar deficits, and there is no secret, in fact, to why we have been able to run them. In part, it is because the dollar is the world's currency.

The flip side of that, however, is that it is quite difficult for the United States to change its exchange rate if it decides it wants to do so because its exchange rate—our dollar exchange rate—is essentially in the hands of other countries.

As Hanke said, we float freely. So if Japan wants to intervene and buy dollars for their reserves, they have the perfect right to do that under the way the system works.

We then have to take an initiative to counter that and say, quoting Ernie Preeg, but that is not consistent with the IMF rules and with international equilibrium. But we are in a free-floating system where the kind of debate we are having around this table today is replicated in every G–7 and other meeting where they address this, because there are really no rules of the game and there is no notion of what is an equilibrium exchange rate.

That is why for many years I have supported a target zone exchange rate system. I do not agree with Hanke that there is a consensus on the so-called two corners approach. The world has been moving very rapidly away from that because it realizes the shortcomings. But that is for a different day.

The point is when the United States decides that it needs to do something about its current account and the exchange rate, it has to take a major initiative.

John Connally did it in 1971 and brought down the Bretton Woods system of fixed rates in order to get the dollar depreciated.

Jim Baker did it at the Plaza Accord in 1985. To bring the dollar down, he had to get G–7 agreement to bring the dollar down. The United States could not do it by itself.

I am thinking now of Senator Gramm's comment about the cheap shovel. The fact that the dollar is international currency makes it much easier for us to buy the cheap shovel and that has big consumer benefits. But the fact that it does create deficits without tears and makes it easy to finance, makes it easy for the dollar to get overvalued and to cause the problems that we are talking about today.

One other historical example that proves the point is the U.K. All through the period of the sterling's dominance as the world's currency, in the 19th century, and into the early 20th century, the exchange rate of the sterling was vastly overvalued.

The British manufacturing sector ran into the ground and here they are 100 years later without much. I hope we do not go that way. It is a slow process. It is more like termites in the woodwork than it is a crashing crisis, although every once in a while the sterling and the dollar had a crisis.

But the role of the dollar is actually, in this context, rather insidious, and it sets us up for the kind of competitive problems we have and the occasional crash in the exchange rate, which I repeat, we have experienced once a decade now throughout the modern postwar period.

Chairman SARBANES. Mr. Preeg.

Mr. PREEG. Mr. Chairman, in response to your question about when should countries dollarize, it is their choice. This goes back to the optimum currency area discussions and analysis of 40 or 50 years ago.

My own assessment, and it is widely shared, is that smaller economies that are very open to trade investment, and that are predominantly dependent on one major trading partner like the United States, are the most apt to be net beneficiaries of dollarization. There are pluses and minuses that have be considered, and this is a net assessment.

In my judgment, the countries of the Caribbean Basin, and I believe also Canada and Mexico, based on the numbers, plus and minus, would thus benefit from dollarization. Argentina is not in that category and has paid a heavy price.

The second point, trade is invoiced in dollars, but that is not, in my judgment, relevant because it is the dollar prices that count.

Toyota car exports to the United States may be invoiced in dollars, but at what dollar price? And if Japan keeps the exchange rate down, Toyota can maintain lower dollar prices.

Chairman SARBANES. That is the point I was trying to make. The fact that you are invoicing in dollars does not take out of the picture the problem of a mismatch in the exchange rates. Is that correct?

Mr. JASINOWSKI. I think that is right, Mr. Chairman, it does not. I should have said that myself, and that is what Ernie's saying.

Chairman SARBANES. Yes. Did you want to add something?

Mr. HANKE. If I may. One thing you asked, is it desirable to dollarize?

Chairman SARBANES. Now, I wasn't really addressing that question because I think that depends a lot on the countries and the nature of the trade. I was trying to get to the question, the assertion that the Japanese were invoicing in dollars. You gave some figures of the percent of trade.

Mr. HANKE. Right.

Chairman SARBANES. I was really trying to explore whether that means that it renders the exchange rate discrepancy irrelevant.

I think Mr. Preeg essentially answered that question because it is still relevant in terms of what dollar level you place on the invoice, so to speak. So that is affected by the exchange rates.

Mr. BERGSTEN. The exchange rate would become irrelevant only for a country that dollarized and adopted the dollar as its official currency, not one that just invoices dollars. You are right, the invoicing is a technical thing.

Chairman SARBANES. Well, that is what I was trying to get at.

Mr. HANKE. It gets a little bit tricky because, let's say you are importing, one big import, and it is oil. And it is priced in dollars. Well, that affects your cost structure because that is an input that you are bringing into your economy. It is purely priced in dollars.

Chairman SARBANES. That is a reasonable point on oil. But we do not have that in either the Japan or China trade where we are running these extremely large deficits.

I am struck by how disproportionate the trading relationship is. It is 5:1 in China and it is about 2:1, I think, in Japan. With the Europeans, they are at about 45 percent, I guess, of the trade is our exports and 55. So that is in a much narrower range. But this China and Japan trade, particularly China now because that is a growing trade, the disproportion, I do not know how long you can sustain that disproportion.

Mr. HANKE. I have spoken at least to Under Secretary Taylor privately about this, and he has an appreciation for the bipolar view expressed by Rubin and Summers. If we adhere to that, we should be putting a lot of pressure on the Chinese to change their exchange rate set-up and get rid of capital controls. Right?

Mr. PREEG. Right. Short of that, they should stop intervening now and bring their currency down 10 or 20 percent.

Mr. HANKE. Now one thing I would like to ask Fred——

Mr. PREEG. Well——

Mr. HANKE. If I could ask Fred——

Chairman SARBANES. Let me regain control here because, as interesting as this is——

[Laughter.]

Time is passing us by and I want to make sure Senator Gramm gets his shot.

Senator GRAMM. Mr. Chairman, I appreciate that. I do not want to miss my cheap lunch.

[Laughter.]

Let me first say that I never met anybody who said to me, I want to have a strong dollar. If there is such a person out there, I never met them. I have to believe that this strong dollar business is a strawman. I represent 21 million people and they have greatly diverse views. Some of them even oppose me.

[Laughter.]

But I cannot help but believe that, out of 21 million people, there would be some strong dollar guy and I would have heard from him. So, I am just mystified by all this strong dollar business. And I have to conclude that it is a strawman.

Second, we have not had a crisis in the dollar since we went on flexible exchange rates. I remember I was an economist and I took the world very seriously.

[Laughter.]

I remember when Nixon went on price controls. We got a group of people together, my sweet wife, who is also an economist, and several of our colleagues, and we decided, since the world was going to hell, a Republican president had gone on wage and price controls and they had not worked since Diacletian, or the Code of Hammarabbi, that there was reason to be disturbed.

So in 1971, we went out to eat, and we did note that one thing about flexible exchange rates, and there was a debate then that the dollarization debate then was the gold standard. There was a little debate, should we be on a gold standard flexible exchange rate? But nobody with any sense thought we ought to have pegged exchange rates, because we were always defending the dollar.

Though I would have to say, when I was a graduate student, I thought, well, maybe I would want to defend the dollar. It sounds exciting. You have your sword. You are defending it. We have had no crisis in the dollar that I can see, and I have been here. I have watched every day. My keen observations, I have not seen it.

Now let me turn to this chart. I cannot afford one of these big charts. But I see a lot of different things on this chart than other people see.

First of all, let's just go 3 years on either side of 1985. In 1982, 1983, 1984, and 1985, the economy was blowing and going and the value of the dollar was just shooting right through the roof. Did a crisis occur and the value of the dollar just collapse in 1985? Well, if it did, I missed it, and I was here.

In 1985, the value of the dollar falls right through the floor and yet, I remember no crisis. And the economy was about as good in 1986, 1987, and 1988 as it was in 1983, 1984, and 1985. Now what does that tell me? Well, it tells me that market forces produced the high-value dollar and market forces produced the low-value dollar and market forces generate what market forces generate in terms of underlying economic forces. In fact, I could have a theory based on these numbers that elections determine the value of the dollar.

When Ronald Reagan was elected President and a Republican Senate was elected, the value of the dollar went up like a rocket. And when Republicans lost control of the Senate, the value of the dollar collapsed.

[Laughter.]

And when Republicans won control of the House and Senate in 1995, the value of the dollar went up like a rocket.

Now do I really believe that there is an election theory of currency values? Well, I believe it more than I believe that there is manipulation of exchange rates. I think there is more scientific basis to it because there is a logic to it.

Where would you get $50 billion a year to put into currency manipulation, Mr. Preeg?

Mr. PREEG. What they do to keep their currency down is you buy dollars.

Senator GRAMM. Yes, but where do you get the money to buy it?

Mr. PREEG. With the Chinese printing press.

Senator GRAMM. Fifty billion dollars—printing? They do not print dollars.

Mr. PREEG. No, yuan. They are buying dollars, paying out their currency in order to take those dollars off the market and keep the exchange rate down.

It is the opposite of what Argentina went through. China is simply taking those dollars off the market because people have all these dollars from the trade surplus and the FDI. The dollar holders want to convert them into yuan. And the capital account is constricted.

So what the Chinese central bank does is to print yuan, $50 billion last year, and give it to these people who give the central bank in return the $50 billion. The dollars are thus taken off the market and there is less upward pressure on the exchange rate in formal and informal markets.

That is the great asymmetry, as I said before. There is an entirely different situation when you are trying to defend an overvalued currency and you only have so many dollars to sell. But when you are buying dollars that people are willing to sell, as has been happening in Japan and China, there is no limit to the official purchases.

Senator GRAMM. Why does it work in China and fail in Japan?

Mr. PREEG. It has been working in Japan the last 5 years, too.

Senator GRAMM. Well, the economy has gone to hell. How is it working? Why haven't they protected all these manufacturing jobs that we are exporting?

Mr. PREEG. No, they haven't. The objective is simply to keep a big trade surplus. We economists call it mercantilist.

Senator GRAMM. Is that your objective?

Mr. PREEG. No, that is the Japanese objective.

Senator GRAMM. But our objective is prosperity. Right?

Mr. PREEG. Well——

Senator GRAMM. It is mine. Is that yours?

Mr. PREEG. My objective is to have market-oriented exchange rates.

For the Japanese, it may be a foolish policy, but they have kept the largest trade surplus in the world over the past 5 years, to a large extent because they have manipulated their currency below market-determined levels.

You may say that they shouldn't do that. I would say that they shouldn't do that. You shouldn't make your economy dependent on a large trade surplus as they have. They should do the structural reforms that everybody advises them to do.

Senator GRAMM. I am running out of time and I am not going to get into an argument with you. But let me tell you what I think is happening.

Chairman SARBANES. Actually, the Japanese now are looking for the trade to pull their economy up.

Senator GRAMM. I would say that Japan has had a huge net capital outflow because people are not investing there and people there that are able are investing here, and that has been the determining factor.

Mr. BERGSTEN. Except, Senator, that, as he said, part of their, "capital outflow," has been a huge build-up in the official reserves of the Bank of Japan, which now exceed $400 billion. It has——

Senator GRAMM. I am glad they have it. The policy in China under your thesis would be it would be just as good to not sell us the goods, but take them out to sea and throw them overboard.

Mr. BERGSTEN. No. In their case——

Senator GRAMM. And print the money to pay for them, and just go right on.

Mr. BERGSTEN. Just to elaborate on what Ernie said, in the Chinese case, because of exchange controls, they require the export earnings of a Chinese exporter to be sold to the central bank for local currency.

Senator GRAMM. I understand they do that. Their economy would be better if they did not. Are you proposing that we do it?

Mr. PREEG. No.

Mr. BERGSTEN. I am proposing that we suggest they not do it.

Mr. PREEG. Right.

Senator GRAMM. I do not mind suggesting they not do it.

Mr. BERGSTEN. That is what we are saying.

Senator GRAMM. If you are in China, do not do it. It is stupid.

Mr. BERGSTEN. That is what we are saying.

[Laughter.]

But the implication would then be an appreciation of the renminbi and some modest depreciation of the dollar, which would help solve the problem that we are talking about here. But it would be through their change in that case, and likewise, with Japan.

Chairman SARBANES. Jerry, did you want to add something?

Mr. JASINOWSKI. Since Senator Gramm liked the chart, and certainly saw a number of things in it beyond what I saw, I wanted to just say, Senator, the chart always reflected the fact that there are a number of variables that influence trade, as you know better than anyone, from growth to interest rates to the performance of the economy—and the chart reflects that. And therefore, your comments are correct.

We are not here to say that the exchange rate is the only determinant of trade, I should say. We are here to say, though, that anybody who says that the exchange rate does not affect trade—that is our position—is dead wrong.

Senator GRAMM. Oh, of course it does. But what affects exchange rates? That is where we differ.

Mr. JASINOWSKI. Okay. But then I want to go on to repeat the point that I said earlier. If you have a Treasury policy, and we certainly have heard it and we would be happy to document it for the Committee, about a strong dollar, and the rhetoric——

Senator GRAMM. The Secretary never uttered strong dollar when he was here. And he was belligerent and he would have said it had he meant it.

Mr. JASINOWSKI. Well, I also can tell you if you go back to the Reagan Administration, I was involved with the Plaza Accord. I was involved with Secretary Baker and others and there were comments that came out of that Administration about a strong dollar and how wonderful it was. If you have any Administration that is shouting from the rooftop, even if they do not use the term, "strong dollar" about how unmitigated higher and higher exchange rates for the dollar are desirable you are going to affect trade flows. That is the only point that I would make.

Senator GRAMM. Well, the only thing I would say is that, of all the times that I met with President Reagan, and of all the conversations that I listened to, I never heard him mention strong dollar. I never heard him mention it.

Mr. BERGSTEN. Mr. Chairman, could I say one other thing to Senator Gramm because you said, "Senator, you had not experienced any crises under floating exchange rates?"

Senator GRAMM. I did not see one in 1985.

Mr. BERGSTEN. I want to give you two examples.

Senator GRAMM. Okay.

Mr. BERGSTEN. If the chart went back a couple of years earlier—and I have scars on my back because I was in the Carter treasury—there was a dollar crisis in the late 1970's under floating rates. The dollar collapsed——

Senator GRAMM. Because of inflation.

Mr. BERGSTEN. Because of inflation and it added, then, to the inflation and it pushed up interest rates, and we had to do a huge intervention in the exchange markets in addition to doing things on the domestic front.

Paul Volcker finally came to the Fed.

That was a real crisis under floating rates. But I want to make a more subtle point. There was a crisis in 1985 with that strong dollar, even aside from jobs and all that. The crisis was in trade policy.

You may remember, friends of mine in the House—I cannot quote any Senators—said, if the Smoot–Hawley tariff itself had come to the floor at that time, it would have passed, because of the huge decline in our competitive position.

You remember, there were Gephardt amendments——

Senator GRAMM. Listen, I remember the automobile industry came to me and said, we are going to have to go out of business. General Motors could go broke. We were producing crappy cars. We were producing crappy trucks. The guys on Monday were thinking about the weekend. The guys on Friday were thinking about the weekend to come. They were having—what is the country song—daydreams about night things in the middle of the afternoon.

[Laughter.]

We got the hell kicked out of us. They came here and said to Reagan, protect us. And Reagan, in essence, said, compete or die.

Mr. BERGSTEN. No.

Senator GRAMM. And now we make the best trucks in the world and our cars are as good as anybody's in the world. Why? Because we had to.

Mr. BERGSTEN. No, but Senator——

Senator GRAMM. You all created the crisis in the Carter Administration.

Mr. BERGSTEN. No. President Reagan put import controls on cars. He had the Japanese do the so-called voluntary export restraints that limited car exports here for 10 years. He did it on steel.

Senator GRAMM. He did it absolutely as little as he could get away with. He jawboned.

Chairman SARBANES. How much did the Plaza——

Mr. BERGSTEN. It was because of the overvalued dollar.

Chairman SARBANES. By how much did the Plaza Accord, done during the Reagan Administration by Secretary Baker, affect this relationship of currencies?

Mr. BERGSTEN. The dollar came down 50 percent on average over the next 2 years.

Chairman SARBANES. Fifty percent.

Mr. BERGSTEN. Fifty percent, having gone up 50 percent from 1980 to 1985. I am not criticizing President Reagan. I am——

Senator GRAMM. Cause, or did it just happen?

Mr. BERGSTEN. It was a response to the policy mix of the huge budget deficits and very high interest rates that brought in huge amounts of capital, drove the dollar sky high, and I actually had sympathy with the Reagan Administration when they went for import controls on autos, steel, machine tools, all those things. But

it was because the exchange rate had driven the firms into an uncompetitive position. My point is simply, that is what we are confronting again today.

Chairman SARBANES. Mr. Preeg, you wanted to add something?

Mr. PREEG. Just a technical correction. I believe it was closer to 40 percent. But it had already come down 10 percent before the Plaza meeting. The Plaza participants agreed that the dollar should go another 12 percent, which is an awfully precise projection. And there was a very modest intervention. They were very small numbers compared with today. And then the dollar overshot and went down another 30 percent.

So my judgment is that the market forces were already in play because the dollar had already come down 10 percent, and we may be starting that way today. Very heavy market forces were in play, although the official intervention did help.

Also, politically, calling for G–7 intervention is something I would advocate today. Rather, we should say that it is in our mutual interest to gradually bring down the U.S. trade deficit. If we once said that and let the market forces respond, I believe that the dollar would begin to move down somewhat.

Senator GRAMM. Mr. Chairman, I am going to lunch. But I want to thank you. It was an excellent hearing.

Chairman SARBANES. Yes. We are going to draw it to a close.

I want to read into the record an interview that Secretary O'Neill had with the *AFX News Limited Service.* These are quotes. Of course, the Secretary is not here and I guess he could argue that he has been misquoted, but anyhow, this is what people read and this is what they take their message or signals from. This was on March 15, so it was not that long ago:

We have a so-called strong dollar policy and it is consistent and constant and there is no change, he said, suggesting he is immune to U.S. industry complaints. I do not feel pressured to change the strong dollar policy, he stressed.

That is because, earlier, they asked him about whether he was experiencing a lot of pressure. Actually, he said, O'Neill would not comment on whether he expects the rebound in U.S. manufacturing to help ease the pressure manufacturers have put on the Bush Administration to change the strong dollar policy. I hadn't noticed, he facetiously said of the repeated lobbying attempts by manufacturing associations and U.S. automakers to get the Administration to abandon his policy. And then he went on with this quote about a strong dollar and not feeling pressure.

The Treasury Secretary also said he does not regard the current account deficit to be a risk to the economy because it is irrelevant. I just think it is a meaningless concept in a globalized economy, he said, despite some forecasts that the deficit could reach 6 percent of GDP within the next 3 years. Economic policymakers should not pay attention to the deficit, he said, explaining that the only reason that I pay attention to it at all is because there are so many people who mistakenly do so.

I think today was more or less consistent with these statements.

Let me ask this question. Do you think that the exchange rates, that a Plaza-like effort, or a major effort—has the economy developed in such a way worldwide that your ability to have an impact

has been diminished or undercut? Or if you prepared to move ahead with an active policy, could you have an impact?

Mr. JASINOWSKI. Mr. Chairman, let me just start the response by saying that most of us have stressed a several part policy correction. The first part of the correction is for the Secretary of the Treasury to acknowledge the problem, to stop talking about a strong dollar, and to allow markets to make some judgment—apart from the Treasury putting a floor under the dollar.

Words do make a difference. Rhetoric affects the markets. That is policy step number one. And that will clearly work. There is wide consensus on that. In fact, there is a quote in my testimony about how much the market-makers believe the dollar would adjust by that alone.

The second step, which Fred has emphasized, is that if we proceeded with an effort to get agreement among our major trading partners and have them support a new set of policies that would stress fundamental factors, and intervention, yes, it could have an effect.

Mr. BERGSTEN. Just to echo what I said earlier, Mr. Chairman, I actually think the prospects for intervention working now are at least as good as in the past at the time of the Plaza Accord.

I noted that the Rubin–Summers Treasury tried it only three times in 5 years. I think it worked just like a textbook would say, on all three cases. The fact that they have not intervened much actually means that, if they were to do it now, it would clearly have more effect. If intervention is done every day routinely——

Chairman SARBANES. It would require a joint effort, I take it, by the G–7.

Mr. BERGSTEN. There are several criteria. It has to be sustained, cooperative, well-coordinated. The rhetoric has to be consistent.

Chairman SARBANES. Do you think it is likely we would get a cooperative, well-coordinated effort on the part of the others?

Mr. BERGSTEN. I think the Europeans clearly would agree to intervene to strengthen the Euro. There would be difficulty with them on how much. The Europeans would agree to move the Euro back at least to 1:1 against the dollar. They might begin to get hesitant beyond that, even though more than that is clearly necessary, but I think they would clearly agree to start it.

Japan, given the weakness of its economy that we have talked about, and the fact that it is scrambling for any scrap of positive news, would be reluctant right now. But they have the world's biggest trade surplus. It is soaring again because of the recent decline in the yen. We would simply have to insist that they cooperated, which, incidentally, would then put more pressure on them to make the kind of domestic structural reforms they need, anyway, and I think would be beneficial in the broader sense as well.

Chairman SARBANES. Mr. Preeg.

Mr. PREEG. I think the interventions that Fred mentioned earlier are really token interventions of a few billion, $5 or $10 billion.

Mr. BERGSTEN. Which is so amazing why they work.

Mr. PREEG. They give a political signal, and it is not the economics. And the comparison of figures, again back to China. China intervened with $50 billion last year, while China has one-fifth the trade that we do. So for a comparable impact on our trade or our

exchange rate, we would need $250 billion of U.S. intervention per year. And we are talking about $2 or $3 billion during the decade of the 1990's.

The orders of magnitude compared with what Japan and China are doing, comparing their trade levels and ours, indicates token U.S. intervention in economic terms. But even token intervention can have political significance in that markets would sense that the dollar is going to go down.

Chairman SARBANES. At any rate, I take it it is your view that even just the rhetoric that we are using is helping to skew this thing in the wrong direction.

Mr. BERGSTEN. That is clear, and the market people say that repeatedly. One question another time to ask the Secretary is, what would be the downside of changing your rhetoric? Why does he not want to change his rhetoric?

The reason is he fears he would drive the dollar down too far, too fast. Now, I think that is not a realistic fear, but that is the reason. That is the only argument he and his predecessors could make for not changing the rhetoric when they were implored to do so. They clearly think it would have an impact, or else they would accept to do it.

Ernie made also a very important point. The three cases I mentioned, the amounts of intervention were very modest. And to me, that makes it all the more clear how effective the tool is. You do not have to spend a lot of money. It is the signaling effect. It is indicating with your money where your mouth is. You want to see a change. You want to correct the current account problem.

Mr. JASINOWSKI. Mr. Chairman.

Chairman SARBANES. We have to draw this to a close.

Mr. JASINOWSKI. One suggestion to make along these lines, going back to a point that Steve made, is to seek a precise written statement from the Treasury as to what our policy or nonpolicy is, which is what I have been arguing in part for that would help clarify where we are.

Here we have one of the most important policy issues before the country and nobody is quite sure what the Treasury policy is. And it does seem to me greater clarity is essential.

Chairman SARBANES. The Secretary says there is no problem.

Mr. JASINOWSKI. Well, I think there is.

Chairman SARBANES. I am going to have to draw to a close. Did you want to add anything?

Mr. HANKE. I would like to briefly make a remark on this last round of things.

Chairman SARBANES. If you could keep it brief.

Mr. HANKE. Yes. I think if we have an exchange rate policy that is a floating exchange rate policy, the Secretary should refrain from all open-mouth operations in all respects and just keep quiet—say absolutely nothing on it.

The second point, Mr. Chairman, is, I think I detect in your view, and the views of my colleagues here, that, well, somehow, the balance of payments is getting a little bit out of whack and extreme values are showing up and we have to do something about it.

My own view on that is a little bit different. That is, a little bit more like the Secretary's. We have a floating exchange rate policy,

which acts automatically. And therefore, these balance of payments adjustments just take care of themselves, Fred.

Mr. BERGSTEN. Yes, but they do not.

Chairman SARBANES. They won't take care of themselves if the currencies are being overvalued for one reason or another, either because we are making these pronouncements about the strong dollar and/or because China and Japan are sort of working against the way the market forces work in order to make the purchases. My perception is that the market is not working pure and simple as a market. It is being impinged upon in a lot of ways.

Mr. HANKE. Fred, let me make my third point because it fits into this. We agree on this thing.

Chairman SARBANES. Yes.

Mr. HANKE. My view is we should become neutral and sanitized on the whole exchange rate comment thing. Let the balance of payments accounts adjust naturally and over time, market forces will take care of that, too.

Back to your question, Mr. Chairman, about whether some kind of policy change now, intervention, three-part thing like Jerry says, would work. My view is that the market is set up to be taken down.

So right now, I am Chairman of the Friedberg Mercantile Group. Our business is trading currencies. And we are short the dollar against 10 very peripheral currencies. And the reason it is a great trade is because we pick up the carry and make interest carrying a short position against the so-called strong dollar.

The war on terrorism has changed things enormously. And the perception that people have in the world about the United States and how great the prospects might be in the future for the U.S. economy—cranking up a big war machine against an enemy that even our Secretary of Defense says is elusive—is that we are in a war of indeterminate duration that is going to start eating up real resources in the economy and start whacking away at productivity in the economy.

The story we are getting about the economy has been very rosy and that is why there have been deficits without tears, Fred.

But this thing, I think, is a little bit on a pivot now. So even though I disagree with Fred and Jerry in terms of an activist policy to correct the balance of payments imbalances, I would have to agree that, if you were going to do it, I think now is a great time to do it, in a technical sense.

Chairman SARBANES. Well, this has been a very helpful panel, obviously.

Mr. Trumka and Mr. Stallman, I just want to say to you, when we were talking about the cheap shovel, I was thinking to myself, if we do away with these jobs, who is going to have a paycheck that will enable them to buy the shovel, whether it is a worker or a farmer? So, we have to keep that in mind as well.

Thank you all very much. It has been a very good panel. The hearing is adjourned.

[Whereupon, at 12:58 p.m., the hearing was adjourned.]

[Prepared statements, response to written questions, and additional material supplied for the record follow:]

PREPARED STATEMENT OF SENATOR DEBBIE STABENOW

Thank you, Mr. Chairman. I welcome the opportunity to discuss exchange rate policy and I appreciate that the Treasury Secretary and our other witnesses have come to testify before us today.

The issue of exchange rates and, in particular, currency manipulation is one that has a profound impact on my home State of Michigan, especially as it relates to the automotive sector. I am concerned that the Administration does not seem to be aggressively addressing this issue.

It is not a coincidence that the on-going weakening of the yen has occurred at the same time that Japanese automakers are experiencing record profits and American automakers are facing significant losses. Indeed, recently, the weakened yen has effectively given Japanese automakers up to a 30 percent cost advantage over U.S. manufacturers.

On the floor of the Senate, we are beginning a discussion on promoting trade. Free and fair trade can be good for our country, but we must be outspoken about anticompetitive tools in the global marketplace. Currency manipulation is one of those anticompetitive tools.

Japan intervened in the currency market a staggering 11 times last September alone. This resulted in an 11 percent decline in the value of the yen against the dollar. I understand that the Japanese face difficult economic challenges that create incentives for them to devalue their currency, but our Government cannot stand idly by and watch our domestic manufacturers lose out.

It is not fair to our domestic auto manufacturers who deserve to compete on a fair and level playing field. It is not fair to our auto workers who will lose jobs due to this invisible tariff caused by currency manipulation. Indeed, Mr. Chairman, it is not fair to a whole number of industries who suffer unfairly.

I look forward to hearing from the Treasury Secretary today about what the Bush Administration is going to do about this problem and I also look forward to hearing the perspectives of our other witnesses.

PREPARED STATEMENT OF SENATOR CHUCK HAGEL

Thank you, Mr. Chairman, for holding this hearing today to explore concerns about the value of the dollar against other currencies.

I know there are sectors of the economy that have been hit hard over the last year by the recession and September 11. Farmers, textile workers, manufacturers, and all exporters have especially been impacted.

There are several factors that have helped create this situation, including the trade barriers of other countries, production subsidies that distort markets both here and abroad, technological advances that have lowered the prices of production, and lower demand in other countries that are going through recessions. Some will also say the blame lies with the strong dollar. I am not persuaded that the strong dollar is a primary factor attributing to the difficulties in our economy. There are down sides to a strong dollar. However, an appreciating dollar can be compatible with a rising value of exports, a falling value of imports, a growing trade surplus, and increased employment.

Given the degree in which traders around the world value the dollar, can one say that the dollar is overvalued? It is true that the dollar is at a stronger level relative to other currencies, but this reflects the productivity, creativity, and value of American labor and resources.

I am concerned about the unintended consequences of intervention in the value of the dollar. For instance, how will our interest rates, Government expenditures, and capital inflow be impacted?

There are many benefits to having a strong dollar. Most importantly, a strong dollar attracts investment which provides new capital resulting in new jobs and increased productivity in the United States.

One reason for the current strength of the dollar is that foreign investors desire to purchase American assets. In large part, this is due to the increase in national productivity that has raised the rate of return on American capital.

I am looking forward to hearing Secretary O'Neill and our other panelists discuss these issues today.

Because the strength of the economy is based on many different factors, attempting to manage one of those factors will have an impact on all of the others. We need to be cautious when we talk about intervening in the market when there is no way

to be even relatively certain of how other pieces of the market will move as a result of any action taken.

PREPARED STATEMENT OF PAUL H. O'NEILL

SECRETARY, U.S. DEPARTMENT OF THE TREASURY

MAY 1, 2002

Chairman Sarbanes, Ranking Member Gramm, Members of the Banking Committee, I thank you for this opportunity to appear before you this morning to discuss our International Economic and Exchange Rate Policy.

The April 2002 Report reviews global economic developments in the second half of 2001. This interval and the most recent months encompass a turbulent period in which the events of September 11 and their aftermath shook the United States and world economies, and a period when the underlying strength in the U.S. economy showed itself forcefully, leading the world back to recovery. I have said before that creating economic growth and jobs in the U.S. economy is our overriding concern and that getting our economic policies right at home is one of the best contributions we can make to global economic growth.

Increasing economic growth and reducing economic instability are vital interests of the United States. For this reason, I would like to touch on several of the Administration's broad policy initiatives for facilitating growth and stability.

Reducing Barriers to International Trade

The global economic slowdown, from which we are recovering, brings into sharp focus the importance of international trade. Total U.S. trade in goods and services amounts to about one quarter of GDP. It now touches almost all parts of our economy and is a vital ingredient in its health, creating millions of jobs that pay above-average wages.

President Bush achieved a key objective in his trade agenda with the WTO Ministerial decision in Doha to launch multilateral trade negotiations. Negotiations are already underway for a Free Trade Area of the Americas (FTAA) and for Free Trade Agreements (FTA's) with Chile and Singapore. In January 2002, the United States announced that it will explore an FTA with the countries of Central America. An FTAA, when combined with existing free trade agreements, and bilateral FTA's with Chile and Singapore, will fully open market access overseas for nearly 50 percent of U.S. exports.

The Treasury has a special interest in promoting further liberalization of trade in financial services. The growth potential in many countries is being held back by a lack of deep and liquid capital markets. The swift removal of barriers in key markets will help strengthen financial systems internationally. It will also mean more American jobs in a sector with above-average wages.

In sum, both to help bolster growth and create new export and job opportunities for America, it is vital for the Senate to pass, and the Congress to expeditiously enact, Trade Promotion Authority.

Reform of the International Monetary Fund

The primary role of the International Monetary Fund is to foster conditions in the international economic and financial system that support growth. First and foremost, the IMF must seek to prevent crises that undermine and reverse growth. The IMF is making progress in enhancing crisis prevention, including through increased transparency. For example, nearly all countries borrowing from the IMF now release the details of their reform programs, but more steps are needed to release information and encourage policymakers to take quick action to avert potential crises. Indeed, no matter how good the IMF's analysis and policy advice are, their impact will be limited if they do not serve to inform the public and markets. We look forward to further progress on transparency in coming months.

To help prevent financial crises and better resolve them when they occur, we are working with others in the official sector to implement a market-oriented approach to the sovereign debt restructuring process. This contractual approach would incorporate new clauses, which would describe as precisely as possible what would happen in the event of a sovereign debt restructuring process, into debt contracts. We have proposed three clauses: Super majority decisionmaking by creditors; a process by which a sovereign would initiate a restructuring or rescheduling—including a cooling-off, or standstill, period; and a description of how creditors would engage with borrowers. While we believe it is important to move forward with this contractual approach as expeditiously as possible, we also support continued work on the

IMF's statutory approach to sovereign debt restructuring. We believe that the two approaches are complementary.

Reform of the Multilateral Development Banks

Rising productivity is the driving force behind increases in economic growth and rising per capita income. The multilateral development banks (MDB's) can deliver better results by being rigorously selective in their lending, focusing their activities on a discrete set of high-impact, productivity-enhancing activities that diversify the sources of growth, foster competitive and open markets, promote accountable governance, raise human productivity, and expand access of the poor to physical infrastructure, new productive technologies and social services.

Education and private sector development in particular need to feature more prominently as a critical element in lifting people out of poverty.

Private capital flows now dwarf official development assistance; the challenge is to deploy development assistance in areas where we know it will unleash the entrepreneurial and creative capacities of people living in the poorest countries and to encourage individual investment. Investment climate reforms and capacity-building at the Government and enterprise level should be at the front and center of development policies. The scale of global poverty and unrealized human potential underscores the importance of the MDB's (and all other donors) focusing much greater attention on improving the effectiveness of their assistance. Delivering results means insisting on rigorous quantifiable measures of each aid project and accountability from each aid institution's impact in improving living standards. An incentive structure must exist where performance will be rewarded and nonperformance will not. The United States has proposed such a structure for the IDA–13 replenishment in which the U.S. base-case annual contribution to IDA can be increased if specified input and output triggers are met in priority growth and poverty-reduction areas such as private sector development, primary education and health.

President Bush proposed that up to 50 percent of the World Bank and other MDB funds for the poorest countries be provided as grants rather than as loans. Investments in crucial social sectors (e.g., health, education, water supply and sanitation) do not directly or sufficiently generate the revenue needed to service new debt. Grants are the best way to help poor countries make such productive investments without saddling them with ever-larger debt burdens.

Millennium Challenge Account

Effective assistance means delivering against a set of priority objectives that is measurable. It requires a solid partnership between donors and client countries on priority reforms that drive growth and poverty reduction, while underscoring the need to measure the impact and accountability of those reforms.

On March 14, President Bush outlined a major new vision for development based on the shared interests of developed nations alike in peace, security, and prosperity.

The President's compact for global development proposes a truly historic, shared commitment to stop the cycle of poverty in the developing world and is defined by a new partnership between developed and developing countries to achieve measurable development *results*.

The compact creates a separate development assistance account called the Millennium Challenge Account. It will be funded by substantial increases over and above the approximately $10 billion in existing U.S. development assistance (better known as Official Development Assistance or ODA).

To take advantage of Millennium Challenge Account funds, developing countries must be committed to sound policies that promote growth and development, including the need to fight poverty. We will channel these funds only to developing countries that demonstrate a strong commitment to:

- Governing justly (e.g., rule of law, anticorruption measures, upholding human rights).
- Investing in people (e.g., investment in education and healthcare).
- Economic freedom (e.g., more open markets, sustainable budget policies, strong support for development, policies promoting enterprise).

Experience has shown that policies that are effective in promoting these goals underpin successful growth, productivity increases, and poverty reduction. Further, these goals are mutually reinforcing.

Over the coming months we will be asking for ideas from our development partners—donors, developing countries, academics, NGO's—on developing a set of clear, concrete, and objective criteria for measuring progress in these areas.

Combatting Financing of Terrorism

Depriving terrorists of financial resources is critical to the war on terrorism. The President has directed me to take all measures necessary to pursue this goal.

On September 23, 2001, President Bush issued an Executive Order listing 27 terrorist organizations and individuals and directing the blocking of their property. This Executive Order has now been extended to a total of 202 individuals and entities. To date, all but a handful of countries have committed to join this effort. There are now 161 countries and jurisdictions that have blocking orders on terrorist assets in force and over $104 million in terrorist assets has been frozen globally since September 11—some $34 million here in the United States, and another $70 million by other countries or jurisdictions. A portion of that amount linked to the Taliban has recently been unblocked for use by the new Afghan Interim Authority.

On April 19, I announced with my counterparts from the Group of Seven an unprecedented joint listing of terrorist targets. In March, the United States and Saudi Arabia designated jointly the Bosnia and Somalia offices of the Saudi-based charity Al-Haramain. These joint designations mark a new level of coordination in the fight against international terrorism.

Cooperation on International Tax Matters

International cooperation and coordination on tax matters are critically important for reducing investment distortions and for promoting the proper functioning of financial markets and systems. Tax rules should not serve as an artificial barrier to cross-border investment.

The United States has bilateral income tax treaties with approximately 60 countries. The purpose of those treaties is to coordinate our respective income tax systems so as to avoid double taxation and to reduce or eliminate tax "toll charges" on cross-border investment. We are working to update and modernize existing tax treaties and to expand our treaty network.

As I have said many times, we have an absolute obligation to enforce the tax laws of the United States, because failing to do so undermines the confidence of honest taxpayers in the fairness of our tax system. This can be done more efficiently, given the increasingly global nature of economic activities, with the cooperation of other countries. Currently, we have effective tax information exchange arrangements with many of the world's financial centers. We are working to extend and deepen this network.

International Economic Conditions

I would like to turn now to global economic conditions.

As you know, the U.S. economy began slowing in the summer of 2000 and this weakness extended through the first half of 2001. Then, the terrorist attacks of September 11 set off disruptions that quickly swept through our economy. The events battered consumption as consumers stayed at home, and with our passenger transport system significantly impacted, many associated industries such as tourism and hotels were badly hit. Activity fell at a 1.3 percent annual rate in the third quarter.

Prior to September 11, I had been optimistic about the prospects for U.S. recovery. My optimism now appears to have been well justified. The fourth quarter showed a healthy rebound at a 1.7 percent annual rate. Economic indicators for 2002 already paint a hopeful picture of an economy bouncing back. I believe that the data will show in the final analysis that last year's downturn in real GDP will be the shortest, shallowest on record.

Why was the optimistic view well founded? Even before September 11, the economy appeared to be moving forward at a slow, but positive rate. The inventory overhang was being reduced. The Administration and Congress had responded with timely relief action. The tax rebates and rate cuts from the Economic Growth and Tax Relief Reconciliation Act of 2001 had put money in people's pockets and increased incentives in the economy to work, save, and invest. The Federal Reserve had aggressively lowered interest rates and energy prices were then coming down.

Most importantly, the fundamental strengths of our economic system remain well intact—the American people are hard working; our markets are the most flexible and dynamic in the world; and our macroeconomic policies are sound. Our economy is the most advanced in the world because our economic structures are predicated on the recognition that the private sector drives growth, and that the role of Government is to provide a framework that promotes competition and encourages individual decisionmaking. This has produced, among other things, financial markets that are the deepest and most liquid in the world.

The confluence of these factors is reflected in the remarkable productivity growth of our economy. Unlike in past recessions, productivity continued to rise last year and posted an extraordinary 5.2 percent gain at an annual rate in the fourth quar-

ter. Meanwhile, trend productivity growth remains around 2½ percent, sharply higher than the 1½ percent trend rate from 1973 through 1995, keeping inflation pressures well at bay.

I am convinced that the United States has regained its economic footing. In fact, the figures released just last week showed real GDP rising at an exceptionally strong 5.8 percent annual rate. This performance is a testimony to the inherent resilience of our economy that over the past 6 months has continually surprised on the upside.

So far, I have focused on the United States. The world economy, while beginning to recover from the recent slowdown, is still in the early stage of recovery. Last year, global growth was highly anemic, at roughly 2½ percent. Prospects for 2002 are somewhat better but strong growth may not be fully visible until the second half of the year.

Before becoming the Secretary of the Treasury, I had the pleasure of gaining a special appreciation for the strength of the Japanese economy and its people. Over the last decade, however, Japan's economic performance has been well below its potential. The resulting cost has been high not only for Japan, but also for the world economy. Restoring strong Japanese growth is one of the keys to unlocking strong global growth.

President Bush has expressed support for Prime Minister Koizumi's commitment to reform. The United States also shares his view that it is important for Japan to increase price competition through deregulation and structural reform and to vigorously tackle its banking sector problems. We in the United States learned from the S&L crisis the importance of comprehensively addressing banking sector problems and returning distressed assets to private hands by selling loan claims and underlying collateral rapidly in the market.

We also learned that these reforms can take place only in a supportive macroeconomic environment. For the last 7 years, except for 1997 in response to a one-time tax increase, Japan's economy has been mired in deflation. Last March, the Bank of Japan committed to expand the money supply until the CPI was either stable or increased slightly on a year on year basis. Since then, a welcome and sharp expansion in monetary aggregates has indeed taken place. So far, however, deflation remains entrenched.

The Euro-zone recorded its best growth in a decade in 2000. Going into 2001, there was substantial optimism that the foundations for sustained growth were well in place. But despite these expectations, Euro-zone growth slowed markedly and was negative in the fourth quarter. While Europe too was affected by the events of September 11, Europe's slowdown in 2001 underscored the fact that the interactions and transmission mechanisms among our economies run deep and extend well beyond the realm of trade.

The Euro-zone is poised to begin growing anew. However, the consensus outlook is that the recovery will lag and be slower than the U.S. upturn. That said, it is in many respects difficult to speak about the Euro-area as a single entity. Indeed, there are many very successful pockets of reform, such as Ireland, Spain, and the Netherlands. But European policymakers recognize the need more generally to implement tax reforms within the context of efforts aimed at achieving medium-term fiscal stability and to undertake structural reforms targeted especially at increasing employment and raising potential growth.

On April 19–20, I hosted a meeting of the G–7 Finance Ministers and Central Bank Governors. We recognized that a recovery is already underway in our economies, influenced by macroeconomic policies put in place last year. Nonetheless, while confident about our collective prospects, we also agreed that downside risks remain, especially those arising from oil markets. In this spirit, we agreed that each of our countries has a responsibility to implement sound macroeconomic policies and structural reforms to sustain recovery and support strengthened productivity growth in our own economies and in the global economy.

The U.S. current account deficit was around 1½ percent GDP in the mid-1990's. It rose to 4½ percent in 2000 before falling, during last year's global slowdown, to just over 4 percent in 2001. We have all heard the view that this is a threat to America's economic fortunes and global financial stability. I believe that this view ignores forces that are working in the market. The current account represents the gap between domestic savings and investment and has grown in the face of a productivity-fed U.S. investment boom for the past decade. It is financed by international capital inflows that have risen over this period due to strong foreign interest in investing in the United States.

In the last 2 years, these capital inflows were sustained despite a slowing of U.S. economic activity, a fall in U.S. interest rates, and a decline in equity prices. This is a clear demonstration that foreigners regard investment in the United States as

continuing to offer extremely attractive rates of return. These inflows are attracted by the long-term soundness and relative strength of our economy's fundamentals: Our underlying productivity growth, our low inflation and sound macroeconomic policies, our flexible labor markets, and our financial markets which are the deepest and most liquid of any in the world. As I often say, these investments in our economy's future are not a gift. They are made because of the prospect of a sound return.

Emerging market and developing economies also felt the effects of the slowdown in the major economies in 2001, and their prospects were also set back by the uncertainties stemming from the events of September 11. However, I am hopeful that their prospects will brighten over the course of this year. The truth is that many emerging markets have not performed well in recent years and investment flows going to these markets have declined sharply. On the positive side, though, many emerging market economies are now better able to withstand external shocks, having reduced short-term external liabilities and built up reserves. Many countries, such as Brazil, Indonesia, and South Korea, have moved to more flexible exchange rates regimes, which allow their exchange rates to absorb the brunt of external shocks. I think there is a much greater appreciation throughout these countries on the need to run sound policies. And there has been very little contagion from recent events in Argentina.

I would also like to submit for the record the Report to Congress on International Economic and Exchange Rate Policies as mandated by Section 3004 of the Omnibus Trade and Competitiveness Act of 1988.

In conclusion, I thank you again for this opportunity to testify before you. I would be delighted to answer any questions you may have.

The Department of the Treasury

Report to Congress on International Economic and Exchange Rate Policies

For the period July 1, 2001, through December 31, 2001

THIS REPORT IS REQUIRED UNDER SECTION 3005 OF THE OMNIBUS TRADE AND COMPETITIVENESS ACT OF 1988 (THE "ACT"). THIS REPORT REVIEWS DEVELOPMENTS IN U.S. INTERNATIONAL ECONOMIC POLICY, INCLUDING EXCHANGE RATE POLICY.

Major Findings

- **U.S. economic growth over the period of July 1, 2001 through December 31, 2001[1] was disrupted by the September 11 terrorist attack.** Although the economic slowdown worsened, with real GDP declining in the third quarter of 2001, the U.S. economy bounced back in the fourth quarter, supported by favorable fiscal and monetary policies, and growth is continuing into 2002.

- **Global growth continued to slow overall during the period, leading to export and import contraction in all key economies.** U.S. imports contracted at a faster rate than exports and the current account deficit narrowed in the second half.

- **Trade-weighted indices of the dollar showed little change over the period.** Net capital flows into the United States remained robust, reflecting continued strong global investor confidence in the health, dynamism and attraction of U.S. markets.

- **No major trading partners of the United States manipulated exchange rates under the terms of Section 3004 of the Act during the period.** Treasury continues to monitor the exchange rate practices of major U.S. trading partners and to encourage moves to more flexible exchange rate regimes when appropriate.

The United States Economy

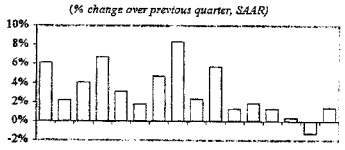
Overview of the U.S. Domestic Economy

Although the U.S. economy was slowing through the second half of 2000 and the first half of 2001, there were signs of firming early in the third quarter of 2001 suggesting that growth might strengthen. The September 11 terrorist attack and its aftermath caused the economy to retrench. Consumers pulled back on spending and capital investment continued to decline. Real GDP in the third quarter fell at a 1.3% annual rate, the first decline in nearly a decade.

Fiscal and monetary policies were already in place to counteract the effects of the slowing economy and those policies contributed to a return to growth in the fourth quarter. Tax rebate checks and lower marginal rates reduced taxpayers' liability by about $44 billion last year. The Federal Reserve lowered interest rates six times in the first half of the year, and cut rates another five times during the period. After growing at a 1.0% annual rate in the third quarter, consumer spending surged at a 6.1% rate in the fourth, and real GDP rebounded at a 1.7% rate. GDP growth continued to strengthen going into 2002.

Productivity rose even as the economy contracted, an unusual development, and accelerated sharply from a 1.1% annual rate increase in the third quarter to an

U.S. Real Gross Domestic Product 1997-2001
(% change over previous quarter, SAAR)



Source: Bureau of Economic Analysis (BEA)

[1] "The period" means July 1, 2001 through December 31, 2001 in this report, unless otherwise indicated.

outsized 5.2% pace in the fourth quarter. Solid productivity gains at about the 2.4% trend rate of growth since 1995 are expected to continue.

Overview of U.S. International Sector

Current Account

The current account deficit fell to $417 billion, or 4.1% of GDP, in 2001 from a $445 billion, or 4.5% of GDP, level in 2000. The narrowed deficit was the net result of significant reductions in imports and exports, both depressed by the slowdown in global activity. The contraction in trade was particularly severe for capital goods in both the United States and its trading partners.

U.S. Balance of Payments and Trade
($ billions, SA, unless otherwise indicated)

			2001			
	2000	2001	Q1	Q2	Q3	Q4
Balance on Current Account						
Billions of $	-444.7	-417.4	-112.1	-107.9	-98.5	-98.8
Per Cent GDP	-4.5	-4.1	-4.4	-4.2	-3.9	-3.9
Select Financial Flows						
Net Direct Investment	135.2	1.9	11.7	24.3	-20.6	-13.5
Net Sales of US Securities to Non Official Foreigners	432.9	514.2	149.5	131.8	73.3	159.6
Net US Banking Flows	-50.5	-9.1	-102.9	44.2	-.2	49.8
Trade in Goods						
Balance	-452.2	-428.8	-112.8	-107.8	-105.5	-100.7
Total Exports	772.2	720.8	194.5	185.5	173.4	167.4
of which:						
Agricultural Products	52.8	55.0	13.6	13.5	13.7	14.1
Capital Goods Ex Autos	357.0	322.3	91.5	82.9	75.9	72.0
Automotive Products	80.2	74.6	17.9	19.1	19.3	18.3
Total Imports	1224.4	1147.4	307.2	293.2	279.0	268.1
of which:						
Petroleum Products	120.2	109.7	29.3	28.5	25.8	20.3
Capital Goods Ex Autos	346.7	297.8	86.2	74.7	69.1	67.8
Automotive Products	195.9	189.7	46.7	47.8	48.0	47.2
Advanced Technology (NSA)						
Balance	5.3	4.8	4.8	3.5	-1.1	-2.3
Exports	227.4	200.1	57.1	51.8	45.8	45.6
Imports	222.1	195.3	52.4	48.0	46.7	48.2

Financial Flows

Net financial flows into the United States remained strong throughout 2001, although the composition of the flows varied over the course of the year. These inflows easily financed the U.S. current account deficit and reflected international investors' continued strong interest in investment opportunities in the U.S. market.

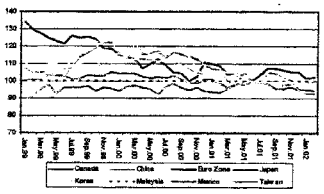
International Investment Position

The net investment position of the United States at the end of 2000, the latest date for which data are available, was a negative $2.2 trillion with direct investment evaluated at market value. Net investment income payments to foreigners, however, amounted to only $13.7 billion in 2001, as net receipts of $95.2 billion from direct investment offset net payments on portfolio investment.

The Dollar in Foreign Exchange Markets

The dollar, on a trade-weighted basis, showed little change over the period notwithstanding a temporary increase in uncertainties about the U.S. economy and U.S. markets in the wake of the September 11 terrorist attacks. The Federal Reserve Board's broad nominal dollar index indicated that the dollar appreciated 0.3% on a trade-weighted basis, after appreciating 4.0% the first half of 2001. The real dollar index depreciated 0.6% during the period, after appreciating 4.4% during the first half of the year. The dollar moved from ¥125 per dollar to ¥131 per

Bilateral Exchange Rates
(Dollars per Foreign Currency Unit, June 2001 = 100)



dollar and from $0.85 per euro to $0.89 per euro over the period.

In the July-September quarter, the dollar depreciated on expectations of a protracted cyclical downturn in the United States. In an atmosphere of slowing global growth, market participants became more risk-averse and pulled back from higher risk assets generally. Some market participants, fearing greater economic dislocation after the September 11 terrorist attacks, sought to reduce their economic exposure to U.S. markets. Some investors shifted assets into war and conflict safe-havens, while others merely reduced their external exposure.

However, in the October-December quarter, market participants grew increasingly convinced that the United States would adapt its economic policies quickly to reduce the risks of a protracted downturn. Data releases during November reinforced an emerging sentiment that the US would lead the cycle and prompted upward revisions of market forecasts of U.S. growth. The rapid success of U.S. military efforts in Afghanistan was also a factor supporting the dollar. In contrast, economic data from Europe

were not viewed as offering assurance about a prompt return to growth, while Japanese data pointed to continued depressed activity.

During the period G-7, Finance Ministers and Central Bank Governors referred to exchange rates among the major currencies in two communiqués (July 7, 2001, and October 6, 2001), each time stating: "We will continue to monitor developments closely and to cooperate as appropriate."

Major Industrial Economies

The growth of industrial economies fell sharply in 2001. G-7 countries, as a whole, experienced negative growth in all but the first quarter of 2001. Inflation in G-7 countries fell to a 1.2% y/y (year on year) rate in December 2001 compared with 2.5% in June 2001 and 2.4 % in December 2000.

Euro Zone Countries

Euro Zone growth slowed to 1.5% in 2001, down sharply from 3.4% in 2000. Growth dipped to a minus 0.7% (seasonally adjusted at an annual rate or saar) rate in Q4 from 0.8% in Q3. Of the eight largest Euro-12 countries, only Spain avoided at least one quarter of negative growth. Early confidence that the Euro Zone could escape the global slowing was unduly optimistic. The area-wide unemployment rate was 8.5% in December, up from a ten-year low of 8.3% reached early last year. During the second half of 2001, the ECB cut its key lending rates by 125 basis points in response to slower growth.

The rate of increase in the consumer price index spiked above a 3% y/y rate in the late spring of 2001 from a combination of food price increases and continued high oil prices; the core inflation rate remained over 2% through the end of 2001.

The euro appreciated 5% against the dollar during the period, having depreciated nearly 10% during the first half of 2001. The euro appreciated early in the period but was able to maintain levels consistently above $0.90 from only mid-August to mid-October. The euro's failure to sustain an appreciation against the dollar during 2001 was, at least partially, attributable to Europe's vulnerability to the worldwide slowdown.

Japan

The Japanese economy fell back into recession in the second quarter of 2001 following a brief and shallow recovery from the 1997-98 downturn. Real GDP declined 1.7% in the second half of 2001, as both private and public domestic demand contracted and declining net exports also contributed to the downturn. For the year as a whole, real GDP shrank 0.5% as declines in net exports and public demand offset marginal growth in private demand. Deflation remained entrenched, with consumer prices down 0.7% in 2001, the third consecutive year of decline.

The Bank of Japan, in an effort to end persistent deflation, increased the liquidity it provided the money market by raising its bank reserves target in stages from ¥5 trillion to a ¥10-15 trillion range by the end of the year. Short-term interest rates remained virtually at zero throughout the period, and the monetary base grew at a 22% annualized rate. However, growth in broader monetary aggregates remained slow (M2+CDs grew 2.8% saar) and there was no sign of easing deflationary pressures. The weakness in the growth in broad money is a reflection of the weak balance sheets of Japan's financial and corporate sectors. Vigorous action is needed to tackle these twin problems.

Japan's current account surpluses have declined in recent years, from $119 billion or 3.0% of GDP in 1998 to $87 billion or 2.3% of GDP in 2001.

The yen depreciated 5.8% against the dollar over the period, ending the year at ¥131.8, while also depreciating 5.7% in real trade-weighted terms. Despite the weaker yen, Japan's trade surplus narrowed from $36.0 billion (sa) in the first half of 2001 to $35.5 billion in the second half, as declining exports more than offset a $16.6 billion (8.3%) decline in imports. In contrast, the current account surplus widened to $46.9 billion from $41.6 billion, as a narrowing services deficit and a widening surplus on investment income more than offset the modest decline in the trade balance. In real terms there was a 7.9% fall in net exports from the first to the second half of 2001 contributing to the downturn in real GDP.

The U.S. bilateral trade deficit with Japan in 2001 fell sharply to $70.6 billion (BOP basis) from the $82.9 billion level posted in 2000.

Japanese foreign exchange intervention in 2001 was confined to September 17 – 28, in the aftermath of

the September 11 attacks. Ministry of Finance data indicate sales of $27 billion equivalent of yen were made.

Canada

Economic developments in Canada paralleled those in the United States in 2001. The Canadian economy slipped from a slow growth rate of 0.9% saar in the second quarter into negative growth of 0.6% saar during the third quarter, rebounding to a 2.0% saar growth rate in the fourth. Inflation remained low, dipping to 0.7% y/y in December 2001 from 2.6% at the end of the third, 3.3 % at the end of the second, and 2.6% at the end of the first quarter. The Bank of Canada (BoC) lowered interest rates in the second half of the year as the economy weakened and inflation remained subdued, although the spread of Canadian interest rates over U.S. rates widened.

During the period, the overall current account surplus fell to 1.3% of GDP from 4.0% of GDP in the first half of 2001.

The Government of Canada (GOC) has pursued sound reforms during the past decade, placing the Canadian economy on a much stronger footing than in previous years. In the early 1990s, interest rates were in double digits, employment declining, fiscal deficits were large and inflation high. The past decade has seen remarkable improvements in each of these areas. Productivity levels have improved in Canada, and some sectors have levels comparable to those in the United States. However, due importantly to developments in the information and technology (IT) sector, U.S. productivity remained much stronger, thus supporting continued investment flows from Canada to the United States.

The Canadian dollar fell 4.7% against the U.S. dollar and 9.3% against the euro, while rising 1.5% against the yen, during the period. Although the Canadian dollar fell sharply against the euro during the period, it has risen overall against the European currencies during the past decade.

The BoC identifies the long-term decline in inflation-adjusted (or real) non-energy commodity prices as a significant factor in explaining the long-term decline in the U.S.$/C$ exchange rate. A BoC price index tracking these commodities fell 16.4% during the period, reaching a level not seen since 1987. Although widening interest rate differentials vis a vis the United States might have provided some support to the Canadian dollar, the market did not regard these increased spreads as sufficiently attractive to stimulate large scale inflows to Canada.

The Canadian dollar freely floats. A 1998 study by the BoC of its foreign exchange intervention concluded that its prior policy of regular intervention had very limited impact on foreign exchange rates. The BoC has not intervened in foreign exchange markets since 1998.

Other Industrial and Emerging Market Economies:

Overview of Emerging Market Finances

Risk aversion measures increased significantly after the terrorist attacks on September 11th. According to some measures, the risk premia paid on emerging market debt reached or were near record highs. These increases in measures of risk were driven more by a "flight-to-quality" and less by a "flight-to-liquidity". However, following the September attacks, there was no widespread, panicked selling of all emerging market asset classes as occurred in the 1998 Russia-LTCM crisis. By November 2001, risk levels had declined to levels maintained over 2000 and the first part of 2001. The yield spread over U.S. Treasuries of JP Morgan's Emerging Market Bond Index Plus (EMBI+) peaked at 1,005 basis points at the end of the third quarter, and declined in 4Q/2001 to a level lower than that recorded at end 2000.

In 4Q/2001, in spite of the turmoil created by developments in Argentina, bond markets performed strongly and equity markets, on average, outperformed their developed market counterparts. Contagion from Argentina was not widespread during the period, as investors discriminated among risks. Investors, in particular, took underweight positions in risky credits (Argentina and initially

Financial Developments in Emerging Markets

	2000	2001	1Q/01	2Q/01	3Q/01	4Q/01
Issuance (US$ bil.)	216.4	163.2	42.2	50.1	27.2	43.7
Bonds	80.5	88.6	26.8	28.7	11.6	21.5
Equities	41.7	11.2	2.3	5.3	1	2.6
Loans	94.2	63.4	13.1	16.1	14.6	19.6
Secondary Bond Markets (end period spread in bps)						
EMBI+	756	731	784	766	1005	731
Asia	489	356	450	397	494	356
Latin America	706	833	763	803	1103	833
Em. Europe	988	621	957	766	874	621
Stock Market Returns (%)						
MSCI EM Free	-31.8	-4.9	-6.2	3.1	-22.1	26.3
Asia	-42.5	4.2	-0.1	-1.6	-20.1	32.8
Latin Ameriva	-18.4	-4.3	-3.5	7.1	-24	21.8
Em. Eur./M. East	-23.4	-17.7	-22	4.5	-25.8	36.3

Brazil) while going overweight in those that seemed more stable (primarily Asia and eastern Europe).

In 3Q/2001, unsettled financial conditions in Argentina and Turkey and the September terrorist attacks on the United States sharply reduced the gross volume of emerging market fundraising in international capital markets, which fell to levels last seen at the time of the Russia-LTCM crisis. While 4Q/2001 saw some issuance rebound, the total emerging market issuance ended the year at levels comparable to the abnormally low years of the Asian and Russian crises.

Latin America

Growth in Latin America weakened substantially during the period, as the global decline in demand and adverse country-specific factors intensified. Mexico's growth turned negative, weighed down by the U.S. recession. Argentina suffered a real GDP contraction and progressive deterioration of financial conditions, leading to a financial crisis in January 2002. A central feature of the events leading to this crisis was the government's continuing failure to achieve a degree of fiscal discipline that markets considered sufficient. In Brazil, overall growth turned negative, despite a strong improvement in net export performance. On a regional level, the IMF projects that real growth slipped to about 1% for 2001, much lower than the 4% rise experienced in 2000. Only Ecuador recorded more rapid growth in 2001 than in 2000.

However, Latin American access to external capital was surprisingly resilient. Bond issuance declined by only $2 billion in 2001, to $41 billion, and EMBI+ sovereign spreads widened just 30 basis points (bps) during the period to 833bps over comparable U.S. Treasuries. Nonetheless, there was increased pressure on floating exchange rates and depletion of international reserves in those countries with fixed exchange rates.

Argentina

Significant economic, financial, and political turmoil erupted in Argentina at the end of 2001, culminating in January 2002 in a default on external obligations, an end to foreign exchange convertibility (pegging the peso to the dollar at 1:1). Following the decision to float, the peso depreciated from an initial level of 1.40 pesos per dollar to as low as 3.25 pesos per dollar in late March 2002 (3.75 in mid-day trading). The peso has been bolstered recently by additional foreign exchange restrictions imposed by the Central Bank. Events leading up to this crisis resulted largely from deteriorating monetary conditions during the period. Large-scale bank deposit outflows ($18 billion in 2001) weakened Argentina's foreign reserve position, the credibility of its exchange rate regime, and the solvency of its banking system. The Government imposed comprehensive deposit controls in early December 2001. Financial indicators weakened significantly throughout the year -- the Merval stock index fell by 50% in 2001, EMBI+ spreads widened from 800 bps in the first quarter of the year to 4,500 bps by year end, while short-term interbank rates rose from an average of 11% in 2001 to 29% by year's end.

Underlying Argentina's financial crisis was its continued poor growth and weak fiscal performance. Output in 2001 contracted by 3.3%, with the decline increasing to nearly 5%, at an annualized rate, during the period. This was the third consecutive year of falling output. The unemployment rate rose to 18% in 2001 from 15% the year before; consumer price deflation (y/y -1.0%) continued; Argentina's fiscal deficit widened. Although Argentina's trade balance strengthened by $6 billion through the first three quarters of the year, its current account balance declined by $5 billion (to -2.9% of GDP) due largely to rising interest payments and service imports. The real, trade-weighted appreciation of the peso by roughly 6% in 2001 followed a 15% rise during the two previous years. Argentina's inability to meet program performance standards led the IMF to suspend funding in December. President de la Rua resigned soon thereafter, and, following a succession of interim leaders, Eduardo Duhalde assumed the presidency on January 2.

Brazil

The short term political, external, and fiscal risks that plagued Brazil throughout much of 2001 subsided toward year-end and in early 2002. In late September, financial markets began to "decouple" Brazil from Argentina. This was due to Brazil's stronger economic fundamentals, anticipation of reduced debt payments in 2002, and a variety of technical factors that increased demand for liquid emerging market debt. The result was both a decline in new sovereign borrowing costs (from about 1,250 bps to a still-high 800 bps above U.S. Treasuries) and ongoing access to capital markets during the height of Argentine volatility.

Real GDP growth slowed to 1.5% in 2001 from 4.5% in 2000. On a seasonally adjusted basis, q/q growth was –0.8% and –1.6% in the third and fourth quarters, respectively. This deterioration was due largely to a worsening global environment, high domestic interest rates, and a domestic energy crisis. In 2001, Brazil's trade surplus was $2.6 billion (0.5% of GDP)—the first surplus since 1994. The current account deficit was $23.2 billion in 2001 (4.6% of GDP), versus $24.7 billion in 2000. Foreign Direct Investment (FDI) fell to $22.6 billion in 2001 (97% of the current account balance), down from $32.8 billion in 2000.

The CPI increased about 7.7% in 2001 and exceeded the upper band of the official target (2%-6% band), owing both to substantial increases in public enterprise charges and the 45% depreciation in the exchange rate in the year to end-September. The *real* reversed its course and appreciated 18% from mid-September to close the year at 2.3 real/US$--the same level as end-June. The Central Bank of Brazil (BCB) sought to limit inflation by minimizing exchange rate depreciation through the sale of dollar-linked debt ($9.4bn net in the period) and spot foreign exchange reserves ($6b in the period). During 2001, the inflation adjusted trade-weighted exchange rate depreciated 5.1%.

Net international reserves (excluding dollar-linked liabilities of the BCB) increased during the period by $2.1 billion to $36.2 billion. Short-term external debt (residual maturity) was 119% of reserves. As a percent of M2, net reserves decreased from 27.6% to 21.1%.

Mexico

Negative growth in Mexico was primarily driven by the slowdown in the U.S. economy, which lowered the demand for its exports during the period. Real growth slowed to -1.6% y/y in 4Q/2001 (compared with 4.7% y/y in 4Q/2000), bringing real annual growth for the year down to -0.3%. A low annual inflation rate of 4.4% for the year allowed the Bank of Mexico to ease monetary policy to help stimulate growth.

During 2001, the current account deficit reached US$17.5 billion or 2.8% of GDP, down from 3.1% of GDP in 2000. The capital account surplus of $22.7 billion was dominated by a historically high $24.7 billion FDI inflow, of which $12.5 billion was associated with Citigroup's acquisition of Banco National de Mexico.

The authorities let the exchange rate float freely in the period and the peso depreciated a modest 1.3% against the U.S. dollar to 9.16 pesos/$. Net international reserves rose $2 billion during the period to $42 billion (14.2% of M2 and three months of import cover).

Central and Eastern Europe

The region of Central and Eastern Europe continued to experience solid growth in 2001, even if at a slightly slower pace than in 2000. Growth in Southeastern Europe is expected to show the greatest acceleration in the area, led by a strong expansion in Romania. Of the largest or more advanced economies, only Poland came close to slipping into a recession. Ukraine was one of the best performers, with the economy growing by 9% in real terms, while in Russia growth slowed from 8.5% to 5% in 2001. Polish GDP growth dropped from 4.2% in 2000 to 1.1% in 2001 due to a cyclical downturn and tight monetary policy. The other advanced transition economies, Hungary and the Czech Republic, grew by 3.8% and 3.5%, respectively (compared to 5.2% and 2.9% in 2000).

Countries in this region experienced very different exchange rate pressures in 2001. A sharp decline in oil prices after September reduced upward pressure on Russia's exchange rate during the period, and the ruble depreciated from 28.2 R/$ at the end of 2000 and 29.2 R/$ at the end of June 2001 to 30.5 R/$ at the end of 2001. Overall, the ruble's real appreciation was an estimated 7% in 2001, compared to 22% in 2000. The CBR's intervention in the foreign exchange market helped boost reserves $8.5 billion to $36.5 billion in 2001, although reserve growth stagnated after September due to early debt payments to the IMF and a worsening external balance. In Ukraine, the hryvnia remained stable during the period, strengthening slightly from 5.4/$ to 5.32/$. There were no significant interventions by the central bank.

In the key Central European economies, the prospect of future EU membership and inflows of capital in the form of privatization payments and FDI have resulted in a strengthening of the currencies in nominal and real terms. Both Poland and Hungary saw a brief, sharp drop in their currencies in July but by year-end both the zloty and the forint had strengthened. In the Czech Republic, the main policy preoccupation during the period was a concern with excessive crown appreciation in the face of the

inflow of privatization receipts and EU accession-related funds, but the government did not undertake any significant steps to limit the strength of the crown. The strengthening of these three currencies helped to bring inflation down in the region, with the average inflation rate in 2001 in these three countries only 4.8%, compared to 7.5% in 2000.

Asia

Growth in Asia remained subdued during 2001, with several emerging Asian economies experiencing recessions due to the weakening in global demand, though it picked up considerably by year-end. Exports experienced double-digit declines (from the second half of 2000), particularly in economies dependent on IT exports (Korea, Singapore, Taiwan, and Malaysia). However, imports in many economies fell even more sharply due to the high import content of manufactured exports and weak investment owing to excess capacity and an overhang of corporate debt. As a result, current account surpluses in these economies either remained relatively unchanged or increased as a percent of GDP.

Given weak growth and low inflation, Asian countries eased monetary policies in line with the Federal Reserve. However, monetary stimulus did not translate into stronger credit growth in most countries, given that many financial institutions remained capital constrained and many corporations remained overly indebted. Monetary easing did lead to nominal exchange rate depreciation against the U.S. dollar in some countries. Movements in real effective exchange rates for most economies with floating exchange rate regimes were mixed, while real effective rates in economies with fixed exchange rate regimes tended to appreciate. Given weak growth and the threat of deflation, central banks accumulated reserves to limit the appreciation of their currencies.

Monetary authorities in most countries continued their move toward inflation-targeting regimes. In the Philippines, the authorities made final preparations toward formally adopting an inflation targeting framework. In Korea, the central bank adhered to an inflation-targeting framework, with limited exchange rate intervention. However, in Thailand, central bank authorities, while nominally maintaining an inflation-targeting regime, appear to have returned to a greater focus on exchange rate stability and capital flows, raising interest rates early in the period despite core inflation in the lower half of the target range. In general, inflation targeting should lead monetary authorities to focus less on short-term exchange rate movements and more on the medium-term inflation outlook. However, given the large effect exchange rate changes have on inflation in most Asian economies, monetary authorities will continue to adjust monetary policy in response to exchange rate changes.

China

According to officially reported data, China's GDP growth slowed to 6.8% y/y from 7.9% in the period. The deceleration was mainly due to a decline in the growth of consumption and merchandise exports. Exports were adversely affected by the global downturn, with export growth falling to 5.0% year/year compared to 8.8% during the first half of 2001. However, the slowdown in domestic demand caused import growth during the period to decline faster than exports. The trade surplus for the second half of the year (FOB-CIF) was 2.4% of GDP, compared to 2.0% a year earlier. China's current account surplus for 2001 is expected to have declined slightly from 2.0% of GDP a year earlier. Using U.S. data, China's bilateral trade surplus with the U.S. was a non-seasonally adjusted $46 billion during the period, compared to $37 billion during the first half of 2001 and $84 billion in 2000.

China implements a de facto currency peg to the dollar, which it has maintained within a tight band since 1995. In real effective terms, the Renminbi depreciated 2% during the period. Gross foreign reserves grew $32 billion to $212 billion in the reporting period as FDI inflows increased 15% to $46.8 billion, reflecting China's accession to the WTO. Gross reserves at the end of the period were relatively low, equivalent to 12% of M2, compared to 10% at the end of June 2001. According to BIS figures, reserves measured 650% of short-term external debt (residual maturity) at end-June 2001; similar data for end-December 2001 are not yet available. China continues to maintain wide-ranging controls on both capital outflows and inflows.

Korea

Real GDP recovered in the period, growing at 5.1% and 5.9% (estimated) in the third and fourth quarters, respectively (*q/q, saar*), following 1.2% and 1.8% growth in the first and second quarters. This rebound in growth was driven by domestic demand, primarily private consumption supported by stimulative

monetary and fiscal policies. Merchandise exports fell 19.4% during the period, compared to a year earlier, due to weak global demand, while imports fell 16.2% largely as a result of sluggish import-intensive exports and weak investment. Accordingly, Korea's current account surplus as a percent of GDP declined from 2.4% in 2000 and 2.6% in the first half of 2001 to 0.7% in the period.

Korea maintains a floating exchange rate and uses inflation targeting to set monetary policy, generally intervening in the foreign exchange market only to smooth what it considers excessive volatility. During the period, the won depreciated 1% against the U.S. dollar; however the real effective exchange rate appreciated by 1.1%. The Bank of Korea reduced policy interest rates by 100 basis points in the third quarter to respond to weak economic conditions and low inflation. Consumer prices rose 4.3% and 3.7% (projected) in the third and fourth quarters (*q/q, saar*). Despite Korea's early repayment in August of the outstanding balance of its IMF loans, gross reserves increased by $8.6 billion during the reporting period to $102.8 billion at year-end. This increase was due mostly to interest earnings and repayment of exceptional loans to Korean banks extended during the Asian crisis rather than direct central bank intervention in the foreign exchange market. As of December 2001, reserves were 284% of short-term external debt (residual maturity basis) compared to 229% in June 2001. The ratio of reserves to broad money (M3) was 13% in December, and was relatively constant over 2001. Korea has relatively few restrictions on capital flows.

Malaysia

After entering a technical recession in the first half of 2001, Malaysia's economy contracted 0.5% in the third quarter and grew 5.3% in the fourth quarter (q/q, sa) – a relatively favorable result compared to other export-dependent economies in the region that were negatively affected by the global IT slump. An expansionary fiscal policy helped to strengthen domestic demand and cushion the downturn. Despite negative merchandise export growth (down 16% y/y in the period), the current account surplus remained relatively unchanged at 9% of GDP in 3Q01 (latest data available), as slowing exports were matched by decelerating imports.

Malaysia has maintained a fixed peg to the dollar since September 1998, when it also imposed capital controls. Controls have since been relaxed, but offshore trading of the ringgit remains prohibited and foreign portfolio investment by residents continues to be restricted. To limit short-selling, ringgit borrowing by non-residents is also restricted. The Malaysian authorities maintained the peg throughout 2001 despite occasional periods of downward pressure on the ringgit. Such pressure intensified in the first half of the year, as regional currencies weakened and substantial capital outflows led to a sharp decline in reserves. Pressure on the ringgit subsided during the period following successive cuts in U.S. interest rates, stabilization of regional currencies, and capital inflows attracted by progress toward corporate restructuring in Malaysia. At the end of the period, reserves stood at $31 billion, equal to 352% of short-term external debt (residual maturity) and 32% of M2, up from $26 billion, or 299% of short-term external debt and 28% of M2, at the end of June 2001. Due to the strengthening of the U.S. dollar during the period, the ringgit appreciated 1.4% on a real trade-weighted basis.

Taiwan

Real GDP declined 1.9% during 2001, the result of the global downturn, particularly in the market for IT products. Declining investment severely dampened domestic demand as well. This was the sharpest drop in GDP since the 1970s. The economy declined 4% (saar) in the third quarter but picked up during the final quarter of 2001, growing an estimated 6% (saar) as exports of computer and electronics goods rose. Merchandise exports in the second half were still 23% below the same period in 2000. With domestic demand still weak, the current account surplus rose to 8% of GDP during the second half of 2001 compared to 6% of GDP during the same period of 2000.

During the reporting period, given weak growth and limited inflation (with consumer prices rising at less than a 2% annual rate) Taiwan significantly eased policy interest rates. A weak banking system and overly indebted corporations in non-IT sectors hampered the stimulatory effect of monetary easing on credit growth. However, monetary easing and associated foreign exchange market intervention led to a depreciation of the Taiwan dollar by 1.6% against the U.S. dollar and by 4% on a trade weighted basis. Gross foreign reserves rose $13 billion during the period to $126.6 billion. As a percentage of M2, reserves rose from 20.2% to 22.5%, while as a percentage of short-term external debt (residual maturity) they declined from 474% to an estimated 457% during the period. Taiwan maintains a series of capital and administrative controls including limits

on capital transactions by a citizen, select controls on FDI inflows and outflows, restrictions on offshore borrowing of the Taiwan dollar and at times limits on large single foreign exchange transactions.

Elements of Manipulation

Section 3004 of the Omnibus Trade and Competitiveness Act of 1988 (the Act) requires the Treasury to analyze annually the exchange rate policies of foreign countries, in consultation with the IMF, and to consider whether countries manipulate the rate of exchange between their currency and the dollar for purposes of preventing effective balance of payments adjustments or gaining unfair competitive advantage in international trade. The Secretary of the Treasury is required to undertake negotiations with those manipulating countries that have material global current account surpluses and significant bilateral trade surpluses with the United States, unless there would be a serious detrimental impact on vital national economic and security interests.

- Treasury undertook a broad review of the performance of major trading partners of the United States and concluded that no major trading partners of the United States manipulated exchange rates under the terms of Section 3004 of the Act during the period.

PREPARED STATEMENT OF RICHARD L. TRUMKA

SECRETARY–TREASURER
AMERICAN FEDERATION OF LABOR AND
CONGRESS OF INDUSTRIAL ORGANIZATIONS

MAY 1, 2002

Chairman Sarbanes, Members of the Committee, I am glad to have the opportunity to talk with you today on behalf of the 13 million working men and women of the AFL–CIO about the economic impacts of the overvalued dollar.

As we struggle to escape the grip of recession, the overvalued dollar represents a serious problem. It is also causing long-term damage by destroying our manufacturing base. If we fail to redress the problem there is a danger that our fragile recovery will be short-lived, pushing us into a double-dip recession.

Manufacturing is ground-zero of the recession, and its troubles are intimately connected to the dollar. Since March 2001, we have lost 1.4 million jobs, of which 1.3 million have been manufacturing jobs. Manufacturing has therefore accounted for 93 percent of all job losses despite being only 14 percent of total employment. Today, manufacturing employment is at its lowest level since March 1962.

Business has slammed the brake on investment spending, but fortunately the American consumer has kept the recession milder than anticipated. However, a strong recovery that restores full employment needs a pick-up in investment spending. And that will not happen as long as currency markets give a 30 percent subsidy to our international competition.

Over the last 5 years our goods trade deficit has exploded from $198 billion to $427 billion, costing good jobs across a wide array of industries.

- Last year, in the paper industry there were mill and machine closures at 52 locations. All are considered permanent, indefinite or long-term.
- In the textile industry two mills per week closed in 2001, and closures have continued this year.
- The weakening of the yen has given Japanese car companies a huge price advantage. The result has been loss of market share by our Big Three automakers that threatens some of the best jobs in America.
- Boeing, which operates at the cutting edge of technology, is losing market share to Europe's Airbus. And losses today mean future losses because airlines work on a fleet principle. They will therefore order Airbus aircraft 5 years from now when they expand their fleets.
- Moreover, job losses are not restricted to manufacturing. Tourism and hotels are hurt by the strong dollar, and film production is moving offshore to cheaper destinations such as Canada, Australia, and New Zealand.

Many of these jobs will never come back. These are higher paying jobs that have been the ladder to the American Dream for millions of Americans. But now we are kicking away that ladder.

Manufacturing has faster productivity growth, and productivity growth is the engine of rising living standards. But now we are shrinking our manufacturing base, and that is bad for future living standards.

The Administration has shown blind indifference to these problems. Arguments for a "strong dollar" do not wash.

Inflation is not a problem, and there is no evidence that a lower dollar will lower the stock market or raise interest rates. Those who say we need a strong dollar to finance the trade deficit have the reasoning back-to-front. We need to finance the trade deficit because we have an overvalued dollar.

It is time for a new policy that puts American jobs and American workers first.

It is unacceptable that Japan depreciate its currency. This will not solve Japan's problems, and will only export them to its neighbors and us.

China exemplifies all that is wrong with currency markets. It has a massive trade surplus and vast inflows of foreign direct investment. In a free market, China's currency should appreciate, but it does not because of government manipulation. This is a problem that appears in different shades in many countries.

American workers are paying the price of currency manipulation. Trade cannot be "fair" when we allow countries to manipulate exchange rates to win illegitimate competitive advantage.

Those who argue we can do nothing about exchange rates abdicate the national interest. The historical record and the 1985 Plaza Accord intervention show we can. Academic research shows the same. Just as we manage interest rates, so too we can manage exchange rates.

Currency markets are speculative and respond to policy signals. The Treasury and the Federal Reserve must take immediate action with their international partners. The upcoming G–7 summit provides an appropriate moment to do so.

Beyond intervention today, we must avoid a repeat of today's overvalued dollar, just as today's problems are a repeat of mistakes made in the 1980's. The dollar must be a permanent focus of policy, and the Treasury and the Federal Reserve must be made explicitly accountable.

And every trade agreement must include strong specific language that rules out sudden currency depreciations that more than nullify the benefits of any tariff reductions. We have been NAFTA-ed once, and that is more than enough.

The Senate Banking Committee has a vital oversight role to play in ensuring that the Treasury and the Federal Reserve live up to these obligations.

I thank you for the opportunity to testify before you, and I will be happy to answer any questions you may have.

THE OVER-VALUED DOLLAR AND THE DANGER TO ECONOMIC RECOVERY

A Report submitted as part of the Testimony of Richard L. Trumka
Secretary-Treasurer
American Federation of Labor and Congress of Industrial Organization
Before the Senate Committee on Banking, Housing, and Urban Affairs
On the Impact of the Exchange Rate on the United States Balance of Trade, Economic Growth and Employment

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Abstract

The over-valued dollar poses a grave danger to the U.S. economy. Though there is evidence that the U.S. economy has now emerged from its recent recession, the current recovery is weak and built on the temporary stimulus of inventory re-building. A strong and durable recovery requires a recovery in business fixed investment. However, this is being obstructed by the over-valued dollar which has undermined exports and allowed imports to take market share from U.S. manufacturers. The over-valued dollar is also causing long term damage to the U.S. economy by permanently eroding the manufacturing base. Manufacturing is a key engine of productivity growth, and a smaller manufacturing sector means lower future growth and living standards. It is time for a new policy that abandons the rhetoric of a "strong" dollar. Such rhetoric has sent misleading signals to foreign exchange markets and contributed to the dollar's over-valuation. The Federal Reserve must work with its international counter-part central banks to lower the value of the dollar to a reasonable level. China's currency is under-valued and must be revalued upward, and Japan must cease using yen devaluation to try and escape its domestic recession. Looking beyond this, central banks must establish a system of exchange rate management that prevents future mis-alignments of exchange rates which are so damaging. Finally, trade agreements must have exchange rate provisions that guard against sudden devaluations and depreciations which swamp agreed tariff reductions.

THE OVER-VALUED DOLLAR AND THE DANGER TO ECONOMIC RECOVERY

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I Introduction: the continuing dollar bubble

Over the last seven years the value of the dollar has appreciated dramatically against almost all major currencies, and this appreciation has continued unabated this year. Between April 1995 and April 2002 the real value of the dollar rose 34 percent against a broad basket of currencies that includes all major trading partners in Europe, East Asia and Latin America.[1] And over the same period the real value of the dollar rose 49 percent against the currencies of major industrial countries. As shown in figure 1, this appreciation has pushed the dollar to a sixteen year high that is now approaching the record levels of over-valuation that prevailed at the beginning of 1985.

For much of the last seven years the U.S. economy was in the grip of a powerful and long-lived economic expansion that obscured the accumulating negative effects of this appreciation. While the economy was expanding, the rising dollar did help control inflation by keeping the lid on import prices, and this was a benefit. But at the same time, it also cost manufacturing jobs which began to decline in early 1998, and it helped fuel the equity market price inflation which many U.S. households are now paying for. Even if a strengthening dollar could once have been justified, that justification has long since ceased. Today the U.S. economy is struggling to escape the grip of recession, and the over-valued dollar is making this escape more tenuous by undermining the viability of America's manufacturing industries. Fortunately, continued robust consumption spending - financed by home price appreciation - has helped mitigate the slump, but now there is a real danger that continued over-valuation of the dollar could trigger a double-dip

[1]. These exchange rate indexes are maintained by the Federal Reserve. Each country is given a weight in the index equal to its share of trade with the U.S., and the exchange rate is also adjusted to take account of differences in cross-country inflation rates.

or W-recession. Unwinding the dollar's over-valuation must therefore become an immediate priority of policymakers.

In the aftermath of the bursting of the NASDAQ stock market bubble, many have wondered about resemblances between the U.S. economy and Japan. There can be no doubt that the U.S. is different in both the scale of its bubble and its capital market arrangements. That said, there are similarities, and one similarity may be the exchange rate. Japan's asset bubble burst in 1990, yet the yen continued appreciating through to 1995. This appreciation contributed to deepening Japan's economic difficulties. The broader lesson is that exchange rates can appreciate long after a domestic asset bubble has burst, and this lesson is directly relevant for U.S. policy today. The U.S. market bubble burst in the first half of 2000, and since then stock prices have been coming down. But as in Japan it is taking time for the new awareness to spread from the stock market to currency markets. Thus, the dollar continues to be subject to a bubble psychology long after the stock market bubble has burst.

Most disturbing is the fact that the U.S. Treasury may have contributed to this bubble through its rhetoric of a "strong" dollar. This has likely created expectations among market participants that the Treasury stands ready to intervene in the event of dollar weakness. When linked with the fact that many foreign governments have been willing to accept weaker currencies to gain international competitive advantage, this has created a "one way" bet in currency markets that has put persistent upward pressure on the dollar.

II Short term damage: the over-valued dollar and the danger of a double-dip recession

The over-valued dollar is inflicting both short and long term damage on the U.S. economy. This damage is inflicted via the impact of the over-valued dollar on exports, imports, and the

trade deficit. The trade deficit is exclusively accounted for by a deficit in goods trade, and the deficit in goods trade is essentially a deficit in manufactured goods. Thus, goods exports constitute 70% of all exports, and goods imports constitute 90% of all imports. Moreover, non-agricultural goods exports are 93% of goods exports, and non-petroleum imports are 90% of goods imports. These figures mean that the damage from the over-valued dollar is heavily centered in manufacturing which dominates the pattern of trade.

The immediate short term damage comes from loss of manufacturing jobs and the draining of demand out of the economy at a time when demand is weak. Since April 1998 the U.S. has lost almost 2.1 million manufacturing jobs, and 1.7 million of these have been lost since July 2000. These losses can be substantially attributed to the over-valued dollar which has reduced export demand for U.S. manufactures, while simultaneously displacing domestic production through increased U.S. imports of foreign manufactures. Prior to 1998 manufacturing jobs were increasing, but since then the dramatic appreciation of the dollar has put continuous downward pressure on manufacturing employment despite the fact that the broader economy actually enjoyed tremendous boom conditions for much of this period. The U.S. has some of the most efficient manufacturing industry in the world, and for the last several years U.S. manufacturing has posted strong productivity growth that has lowered unit labor costs. However, these efficiency gains have been swamped by the dollar's appreciation which has lowered prices of foreign competitors. The bottom line is that even U.S. industry cannot compete when confronted by a 30 percent price disadvantage imposed by currency markets.

The impact of the over-valued dollar on manufacturing is documented in a recent study released by the National Association of Manufacturers (March 2002). That study reports that

U.S. exports have fallen $140 billion since August 2000, accounting for the loss of over 500,000 factory jobs. Moreover, these job loss effects of declining exports are just one side of the ledger. In addition, there are job losses resulting from surging imports that have grabbed market share domestic manufacturers. In 2001 the deficit in goods trade was $426.7 billion, equaling approximately 25% of manufacturing GDP. Reducing this deficit by $200 billion to the level that prevailed in 1997-98 before the impact of the over-valued dollar began to bite, would add 12.5% to manufacturing GDP. This would in turn translate into approximately 2.1 million additional jobs.[2] This calculation shows how the entire job loss in manufacturing over the last four and one-half years can be attributed to the ballooning trade deficit.

The impact of the dollar works via the twin channels of exports and imports, and this effect is clearly shown in figure 2. The solid line represents the Federal Reserve's broad trade weighted real dollar index. This index includes exchange rates for all the U.S.'s major trading partners, and it is adjusted for cross-country differences in inflation. The broken line represents the ratio of U.S. goods imports to goods exports. When the dollar is strong, imports go up and exports go down, and the ratio therefore rises. Inspection of figure 2 shows a clear and robust relation. Increases in the broad real dollar index are followed by increases in the import - export ratio, and this visual conclusion is supported by the following regression:

$$(1)\ D(GM/GX) = \underset{(1.10)}{1.91} + \underset{(3.70)}{1.07}D(\text{Broad exchange rate}(-1)) \qquad Adj.R2 = 0.41 \quad DW = 2.16$$

where D(GM/GX = change in goods import- goods export ratio, and D(Broad exchange rate(-1))

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[2]. Manufacturing GDP in 2000 was $1,567 billion. Reducing the goods trade deficit by $200 billion to $226 billion represents 12.8% of manufacturing GDP. Manufacturing employment in April 2002 was 16.8 million, and increasing this by 12.8% would add 2.14 million additional manufacturing jobs.

= change in lagged broad exchange rate. Figures in parentheses are t-statistics, and the coefficient of D(Broad exchange rate(-1)) is significant at the 1% level. The regression says that a one point increase in the broad exchange rate results in a 1.07 point increase in the import-export ratio.

Furthermore, the impact of exchange rate movements has become larger because over the last two decades the U.S. economy has become more open and more dependent on international trade. This is shown in figure 3 which shows exports and imports as a share of GDP. In 1980 exports and imports were 18.3% of GDP, but by 2001 they were 23.8% of GDP. Even more dramatic is the change in manufacturing openness, defined as manufacturing exports and imports as a share of manufacturing GDP. This is shown in figure 4.[3] In 1980 manufacturing exports and imports were 60% of manufacturing GDP, but by 2002 they had risen to 116% of manufacturing GDP. The value of manufacturing trade (exports plus imports) now exceeds the total value of manufacturing output. Manufacturing exports are 46% of manufacturing output, and manufacturing imports are 70% of manufacturing output. Given this massive exposure to exports and imports, over-valuation of the dollar now whipsaws the manufacturing sector. Mis-alignments of the dollar, resulting from market speculation or policy mis-judgements, therefore have a larger and more dangerous effect.

The over-valuation of the dollar, with its dire impact on manufacturing, has been a major causal factor behind the current recession. Looking forward, the over-valuation risks triggering a double-dip recession. The current recession began in March 2001, and between March 2001 and March 2002 total employment fell by 1.4 million jobs. Over that same period, manufacturing

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[3]. Manufacturing exports are defined as goods exports minus agricultural exports. Manufacturing imports are defined as goods imports minus petroleum and petroleum based products.

employment fell by 1.3 million jobs. Thus, manufacturing accounted for 92% of total job losses despite constituting just 14% of total employment. This illustrates how the recession has been concentrated in manufacturing.

In addition to the trade deficit, the other driving factor behind the recession has been a collapse in business investment spending. In the first quarter of 2002 the economy rebounded with annualized growth of 5.8%, driven by continued strong consumer spending and inventory re-building. However, non-residential fixed investment spending continues to be a negative. At this stage there is a danger that unless business investment spending turns positive, the temporary spur of inventory re-building could dry up, pushing the economy into a double-dip recession. With manufacturing capacity utilization running at just73.2% in February 2002, and total industry capacity utilization running at 74.8%, business has little incentive to add to capacity. The over-valued dollar is a key factor, since it contributes to reduced exports and increased imports which displace production for the domestic market.

The policy implication is clear. The over-valued dollar has contributed to the current recession, and it is now threatening to trigger a double-dip recession. The benefits of Federal Reserve monetary easing, Treasury tax cuts, and increased government spending, are being diverted into import spending as a result of the dollar's over-valuation. The rebuilding of inventory, though a positive force, is temporary. Moreover, some of it is also likely being done through increased imports. The bottom line is that a strong and sustained recovery requires renewed business investment spending, but this is unlikely to transpire as long as the over-valued dollar undermines the competitive position of domestic manufacturers, and actually gives them the incentive to shift production off-shore.

III Long term damage: the effects of the over-valued dollar on manufacturing and financial stability

Not only is the over-valued dollar doing short run damage to the U.S. economy, but so too it is doing long run damage that will be with us long after the current slowdown is over. In March 2002 U.S. manufacturing employment fell to 16.4 million jobs, equal to the level that prevailed in March 1962.

The loss of manufacturing jobs is damaging the long run commercial outlook for the U.S. economy. This is illustrated in the aircraft industry, where Boeing has been forced to make significantly larger cuts to its production schedule than has Airbus. Given that airlines often order on a "fleet" principle, sales lost today mean lost future sales. This is because when making future orders, airlines will tend to stick with the aircraft manufacturer currently supplying their fleet. In the textile industry, there were on average two mill closures a week in 2001, and this rate of closure has continued in 2002. Modern textile making equipment from these closures is now being sold overseas in second hand markets at rock bottom prices. In this fashion, U.S. manufacturing capacity is being permanently reduced while that of foreign competitors is built up.

Loss of manufacturing jobs carries a high cost. Manufacturing is widely recognized as a principal engine of productivity growth, and there is evidence of positive productivity spill-overs from manufacturing to non-manufacturing. There is also emerging evidence that some of the greatest gains from new economy information technologies may come from application of these technologies to manufacturing. Shrinking the manufacturing sector results in a smaller base on which to build productivity growth and on which to apply the new information technologies.

Consequently, the U.S. stands to have slower future productivity growth, which will result in a lower future standard of living.

Another cost of lost manufacturing jobs concerns wages and income distribution. Historically, manufacturing jobs have been "good" jobs - in the sense of paying above average wages and health benefits. Moreover, these jobs have gone disproportionately to those with an educational attainment of a high school diploma or less, and this group still constitutes 75 percent of the labor force. In effect, manufacturing jobs have provided a ladder to the middle class for this large group of workers, and there is solid empirical evidence that increasing the share of manufacturing jobs in total employment improves income distribution. Eliminating these jobs is tantamount to kicking away the ladder, and the shrinking of manufacturing jobs stands to entrench America's deteriorated income distribution.

There is a widespread misapprehension that the decline of manufacturing employment is an inevitable feature of economic development. While it is true that the "share" of employment tends to decline owing to greater productivity growth in manufacturing and owing to the tendency for faster demand growth in services, this does not mean that the "absolute" level of manufacturing employment need fall. Instead, manufacturing employment can actually grow slightly over time. This is clearly illustrated by the Canadian experience. Figure 5 shows manufacturing employment in the U.S. and Canada for the period 1990 to March 2002. Following the recession of the early 1990s, manufacturing employment in both countries bottomed out in 1993. Thereafter, in Canada it proceeded to rise steadily and robustly from 1.786 million in 1993 to 2.28 million in 2000, making for a 28% gain over seven years. Moreover, manufacturing employment has stayed at approximately this level since then, being 2.304 million

in March 2002. This contrasts with the U.S., where employment rose from 18.075 million in 1993 to 18.805 million in 1998, but thereafter started falling. Between 1998 and 2000 the fall was gradual, but since 2000 there has been a rapid collapse and U.S. manufacturing employment stood at 16.831 million in March 2002.

The difference between the Canadian and U.S. experiences holds a number of important lessons. First, there is no automatic tendency for manufacturing employment to fall. Canada and the U.S. have similar economic endowments, measured in terms of quality of governance, capital stock, and educational attainment of the labor force. Yet, Canada has managed to grow its manufacturing employment significantly, while the U.S. has not. During the 1990s the U.S. even had more favorable macroeconomic conditions than Canada, since it enjoyed a stronger consumption and investment boom, and it also had lower interest rates. The one significant difference was the exchange rate, with the U.S. dollar showing sustained appreciation while the Canadian dollar was consistently weak.

The second lesson from figure 5 concerns the causes of the current loss of U.S. manufacturing jobs. Some have claimed that the loss of U.S. manufacturing jobs is due to a slowdown in the global economy, which has reduced U.S. exports. But if this were so, there should have been a similar loss of jobs in Canadian manufacturing. However, Canadian manufacturing employment has actually risen from 2.28 million in 2000 to 2.304 million in March 2002. Nor can the U.S. recession entirely explain the loss of jobs, since Canadian manufacturing is enormously dependent on the U.S. market. If the recession were decisive, then Canadian manufacturing should also have been negatively impacted.

As noted earlier, the over-valued dollar and the decline of manufacturing both link

intimately with the problem of the trade deficit. Almost ninety percent of the U.S. trade deficit is accounted for by just twelve industries, ten of which are manufacturing industries. The largest contributor is autos and parts: the two non-manufacturing industries are energy and petroleum products. A declining manufacturing base threatens to entrench structurally the U.S.'s large trade deficit, and this in turn risks lowering future growth and creating conditions conducive to financial instability. The ability to run a trade deficit requires a willingness of foreigners to finance the deficit. If that willingness diminishes, the U.S. will be forced to reduce its deficit. At that stage, lacking a domestic manufacturing base capable of replacing imported goods, policy makers could be forced to grow the economy more slowly and with higher unemployment so as to restrict imports to the level for which financing is available.

This danger is illustrated in figure 6 which shows the manufacturing trade deficit as a percentage of manufacturing output. In 1980 the U.S. had a small surplus on manufacturing trade equal to 2.04% of manufacturing GDP, but since then this surplus has turned into a widening deficit. As of 2000, the deficit in manufacturing trade was 24.56% of manufacturing GDP. The massive size of this deficit reveals how the U.S. could potentially find itself constrained in its access to manufacturing goods. Allowing this deficit to grow exposes the U.S. to the future risk of constrained growth and inflation (i.e. stagflation), resulting from an interruption of foreign supplies of manufactured goods and lack of domestic manufacturing capacity to replace those supplies.

Foreign unwillingness to finance our massive trade deficit could also result in an eruption of financial instability. For much of the last twenty years the U.S. has run large current account deficits, and financing these deficits has involved a combination of borrowing heavily from

abroad and selling U.S. owned assets to foreigners. Having been the world's largest creditor in 1980, the U.S. has now become the world's largest debtor. In 1990 foreign entities owned 18% of the publicly held federal debt, but by 1998 this had risen to 32%, and the record large trade deficits of the last two years have surely pushed it higher still. This changed financial circumstance has feedbacks for the current account since the U.S. must now pay interest and dividends to foreigners. As a result, the balance on international income turned negative in 1998 for the first time since before World War II, and this change compounds the problem of financing the trade deficit. The changed position is illustrated in figure 7. In 2001 the income account was in deficit to the tune of $19.1 billion. This income deficit has been growing rapidly over the last several years, and it promises to continue to grow owing to the power of compounding as foreign nationals earn income on the loans and investments they have made to finance past trade deficits.

From a financial stability perspective, reliance on foreign financing exposes the U.S. economy to international financial risk. In the event that foreign investors lose their appetite for U.S. financial assets, U.S. financial markets will stand exposed to reduced demand that will lower asset prices and raise interest rates. At this stage the dollar could weaken precipitously as asset holders seek to exit U.S. markets, thereby creating further financial turmoil. The U.S. would also be exposed to significant imported inflation owing to its dependence on imported manufactured goods which would now cost more, and the result could be a period of stagflation.

The trade deficit - financial instability nexus can be understood through the metaphor of a bath tub. Water in the tub represents accumulated indebtedness, while water flowing in through the tap represents new borrowing. As long as there is room in the tub, more water (i.e. new debt) can flow in. But once the tub reaches its limit, the water immediately starts to overflow. This

metaphor captures the nature of financial crises. One minute everything appears sound, the next financial markets are in turmoil. No one knows exactly where the financial instability threshold for the U.S. is, but the U.S. has run huge trade deficits for twenty years and the current account deficit was 4.5% of GDP in 2000 and 4.1% of GDP.in 2001. Historically, deficits of this magnitude have proved harbingers of instability. Policy prudence therefore suggests a course of smooth gradual adjustment now, rather than run the risk of large disruptions later that leave a debt over-hang from which it is more difficult to escape.

IV Global implications of the over-valued dollar

It is not only the domestic economy that is being hurt by the over-valued dollar. So too is the global economy, and in this sense the over-valued dollar represents lose - lose policy for everyone. For foreign economies the benefit of an over-valued dollar is that it increases their exports to the U.S. by lowering their prices relative to those of U.S. producers. Balanced against this are several costs, the most important of which is imported inflation resulting from the fact that most commodities are priced in dollars. This is clearly illustrated for Europe which saw a surge in inflation owing to higher oil prices following the introduction of the euro in January 1999. The near-tripling of dollar denominated oil prices that took place over the period 1999 - 2001 interacted with the 35 percent fall in the value of the euro relative to the dollar, causing higher inflation. This in turn prompted the European Central Bank to raise interest rates, which contributed to a slowing of the European economy, the costs of which surely outweighed the benefit of a few additional exports to the U.S. market.

A second region that has been hurt by the over-valued dollar is the southern cone region of Latin America. Here, much damage has already been largely done. The main problem in Latin

America has been Argentina whose currency board arrangement tied the Argentine peso at a fixed rate to the dollar. Consequently, as the dollar appreciated, so too did the Argentine peso. The result was disastrous for the Argentine economy which was priced out of world markets. Just as America's manufacturing industry is having difficulty competing, so too did Argentina's -- only the problem was worse because Argentina's industry is far less efficient and its exports are tilted toward European markets rather than U.S. markets. Moreover, Argentina is a major commodity exporter, and the rising dollar priced its exports out of these ultra-competitive markets. The net result was a deep and prolonged recession, and this recession has also had negative spill-over impacts on neighboring Brazil which is a major trading partner.

Argentina's recession, combined with the fact that Europe is its largest export market, made it even more difficult for Argentina to service its huge dollar denominated foreign debts. Now, as a result of the over-valued dollar, Argentina has been forced into default and abandonment of its currency board arrangement. Though freed of the link to the dollar, Argentina's economy has been reduced to a shambles as a result of the process of first tying its currency to the dollar, and then being forced to abandon that link.

Argentina's default has in turn contributed to ripples of contagion that have kept loan rates higher for all developing countries. These higher rates, in conjunction with the fact that the most developing country foreign debt is dollar denominated, have then raised the level of financial distress throughout the developing world. Finally, as with Europe, developing countries have also been hit by higher oil prices which are dollar denominated, and this is a problem that persists as long as the dollar continues to be over-valued.

Most importantly, the U.S. economy is the locomotive of the global economy. Though

there are hopeful signs that the U.S. recession of 2001 has ended, there are real dangers that the U.S. economy could be subject to a double-dip recession if business investment does not pick up. The main factor holding back such investment is massive excess capacity in U.S. manufacturing, which in turn is significantly attributable to the over-valued dollar. If the U.S. economy does take a double-dip, the consequences will be negative and profound for the entire global economy. These consequences will far outweigh any marginal gains in export sales to the U.S. that foreign economies may experience as a result of the over-valued dollar. Put simply, cannibalizing the U.S. economic locomotive through an over-valued dollar is not a sustainable strategy for global growth.

V Arguments for a "strong" dollar do not wash

The arguments against an over-valued dollar are compelling, yet some continue to argue that a "strong" dollar is desirable. One argument is that the strong dollar helps keep down inflation by lowering import prices and keeping the lid on prices of domestic manufacturers. This argument had some support in the late 1990s when the U.S. was in the midst of a huge credit-driven boom, but that is no longer the case and inflation is not an imminent economic danger.

A second argument is that a strong dollar is needed to finance the trade deficit. However, this argument has the reasoning back to front. There is a need to finance the trade deficit because the dollar is hugely over-valued. Absent this over-valuation exports would be higher and imports lower, which would diminish the trade deficit and the amount needed to finance it.

A third argument for the strong dollar is that it contributes to a strong stock market, and any weakening of the dollar would cause the stock market to collapse. But here too there is no evidence. Figure 8 shows the time path of the Dow Jones industrial average of thirty stocks and

the broad exchange rate. It shows no relationship between the stock market and the exchange rate. The stock market rose throughout the early 1990s when the exchange rate fell, and in 2000-01 the stock market has fallen while the dollar has risen. Rather than an orderly reduction in the value of the dollar causing a stock market collapse, a more plausible argument is that failure to address the real problems caused by the over-valued dollar will eventually so undermine economic fundamentals, that a market collapse will follow.

Finally, a fourth argument for the strong dollar is that it lowers interest rates. But here too there is no evidence. Figure 9 shows the broad exchange rate and the 10 year treasury interest rate. In the late 1980s real interest rates fell even as the dollar depreciated rapidly. The evidence suggests that real interest rates are unaffected by the dollar, and are instead driven by Federal Reserve monetary policy and domestic economic conditions. Here too, as with the argument about the dollar and the stock market, there are grounds for believing that it is failure to deal with the problems of the dollar that could become the driver of higher interest rates by promoting eventual financial crisis.

VI Exchange rate intervention works

Having made the case that an over-valued dollar is economically damaging, it is time to turn to the problem of what is to be done. The objective is to engineer an orderly and smooth depreciation of the dollar of the order of 25%.

Some argue that a foreign exchange market flows are simply too large, and that effective intervention is no longer feasible in a world of globalized financial markets. In making this claim, intervention opponents point to the many instances where massive intervention has failed to sustain exchange rates. Most recently, there is the case of Turkey. In 1999 there was Brazil, in

1998 there was Russia, and before that there were the East Asian economies. In each instance market forces proved too powerful.

Missing in the discussion of dollar intervention is the fact that this is a case where intervention is designed to lower the value of a currency rather than support it. This is a huge difference. Turkey, Brazil, Russia and East Asia were all cases where national central banks were pitted against market participants in an attempt to defend exchange rates. The resources available to these banks were their limited holdings of foreign reserves, and given the huge leverage possessed by market participants, they were inevitably defeated. However, intervention by a strong currency bank is a different matter. A strong currency central bank is selling its own currency, of which it has unlimited supplies, and this means market speculators can always be defeated.

Evidence for the success of intervention is provided by the Plaza Exchange Rate Accord of September 1985 when the G-7 finance ministers agreed to bring down the value of the dollar, and there followed a smooth depreciation that lasted eighteen months. On a more systematic level, research by Frankel and Dominguez shows that successful exchange rate intervention is feasible. This is confirmed by a state-of-the-art survey of the literature on exchange rate intervention by Sarno and Taylor published in the September 2001 issue of the Journal of Economic Literature. Currency markets appear to be significantly driven by psychology, momentum trading, and herd behavior, which results in long sustained swings. Robust coordinated central bank market interventions accompanied by coordinated central bank "open-mouth operations" can change market psychology and the direction in which the herd is moving.

Proof of the effectiveness of open mouth operations may even be discerned in the U.S.

Treasury's current "strong dollar" rhetoric. As described earlier, this has created a belief among market participants that the Treasury stands ready to intervene in the event of dollar weakness, which in turn has placed a permanent updraft under the dollar. This points to the role of policy signaling. It suggests that simply abandoning the rhetoric of a strong dollar, and replacing it with one of a "sound" or "fairly priced" dollar, could help transition the dollar to a new desired path.

Successful exchange rate intervention is feasible. That leaves the question of when intervention is warranted. This is an issue that Federal Reserve Chairman Alan Greenspan has mused over in connection with domestic equity markets. Thus, in his June 1999 testimony to the Joint Economic Committee of the U.S. Congress Greenspan commented:

> "But bubbles generally are perceptible only after the fact. To spot a bubble in advance requires a judgement that hundreds of thousands of informed investors have it all wrong."

This argument certainly deserves consideration, but it does not warrant abandoning the public interest. In domestic stock markets there are indicators such as price to earnings ratios that can guide policy makers. When it comes to exchange rate settings, policy makers can be guided by real exchange rate measures that track the real value of currencies and take account of difference in country inflation rates. The views of those who are economically impacted also need to be recognized, and it is noteworthy that the National Association of Manufacturers, the AFL-CIO, and the American Farm Bureau Federation are all calling for a weakening of the dollar.

Economic policy making involves judgements. Adjusting interest rates is the dual of adjusting asset prices, and Chairman Greenspan has no problems about this because of his recognition of the pervasive effect that interest rates have on economic activity. The same holds for the exchange rate. Just as interest rate policy is set on the basis of sensible and informed

judgement about the economy, so too exchange rate policy should be informed in similar fashion. Additionally, it is worth noting that intervention today which lowered the value of the dollar would work to reinforce the direction of monetary policy. For the last several months the Federal Reserve has adopted a course of monetary easing. Selling dollars to weaken the exchange rate would complement this strategy.

VII China and Japan: two special policy concerns

The value of the dollar needs to be brought down against the broad index of currencies. But two country's currencies are especially problematic because of the tendency of their governments to engage in strategic interventions to gain competitive trade advantages, without regard to the impact on the global economy.

In recent months the Bank of Japan appears to have successfully pushed the value of the yen from below 120 to the dollar in November 2001 to above 130 in April 2002. The Japanese government hopes that this depreciation will sufficiently stimulate the economy to pull it out of recession. However, the reality is that Japan is a relatively closed economy, with exports constituting just 11 percent of GDP, while a significant portion of imports are non-substitutable primary products. This means that yen depreciation cannot solve Japan's domestic economic problems because the base on which such depreciation operates is too small. Instead, it risks exporting Japan's problems to the U.S. and other East Asian trading rivals. This in turn could trigger financial instability by starting a cycle of competitive devaluation in the East Asia region. The clear policy implication is that Japan must be obliged to abandon its attempt to devalue its way out of recession.

The second problem country is China. According to IMF Direction of Trade Statistics

Yearbook (2000), China had a trade surplus with the U.S of $68.7 billion in 1999, and a surplus with the European Union of $28.7 billion.[4] It is also a massive recipient of foreign direct investment (FDI), bieng the dominant destination in the developing world. Under these conditions, in a free market, China's exchange rate should appreciate. However, China has pursued an aggressive interventionist and mercantilist exchange rate strategy that has prevented its currency from appreciating. The result has been continuing trade surpluses that threaten global deflation. Jobs are being lost in the U.S. manufacturing sector. Beyond that, China is effectively sucking all the demand out of the global economy, leaving nothing for other developing countries. In this fashion, the developing economies are being pushed into permanent stagnation. Once again the policy implication is clear. As a member of the international economic community, China must abandon its mercantilist interference in exchange rate markets and allow its currency to appreciate as market forces dictate.

VIII Time to restore exchange rate stability and put exchange rates in trade agreements

The recognition that currency markets can damage economic activity points to broader issues of international economic governance The existing international policy framework treats trade and finance as separate independent arenas, yet it is clear that trade outcomes are profoundly impacted by currency markets. Nowhere is this more clearly illustrated than NAFTA, where the halving of the value of the Mexican peso following the inauguration of the NAFTA swamped any benefits to U.S. industry of the reduction in tariffs.

Milton Friedman's old view that exchange rates are determined by market fundamentals, and that market speculators will inevitably pull exchange rates back to levels warranted by these

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[4]. These are the latest available numbers.

fundamentals, is now discredited. Instead, exchange rates appear to behave like asset market prices, and exchange rate bubbles driven by speculative expectations can persist for long periods. The current dollar bubble shows that the problem of exchange rate misalignment is not just a problem for developing countries, and it points to a need for permanent co-ordinated exchange rate policies. Acting together, with the onus of intervention falling predominantly on central banks of stronger currencies, the international community should establish procedures to prevent future damaging currency misalignments. American workers suffered from the dollar bubble of the mid-1980s, and they are suffering again from today's dollar bubble. Exchange rates are too important and potentially disruptive to be left to unfettered speculation, and the community of central banks should establish proceedures for monitoring and correcting exchange rate excesses.

In addition, there is a need to reconsider existing arrangements of unfettered capital mobility. The goal should not be to prevent capital mobility, but rather to give central banks the ability to slow inflows when they deem necessary. One possibility is application of speed bumps in the form of temporary non-remunerated reserve requirements on capital inflows, which have been used to such good effect in Chile.

The fact that exchanges rates can become significantly distorted also points to the need for exchange rate considerations to be addressed in trade agreements. In serial fashion across countries, exchange rate depreciations have destroyed U.S. manufacturing jobs and capital investments without regard to underlying productive efficiency. Such depreciations swamp the benefit of tariff reductions achieved through trade negotiations, and amount to an "exchange rate subsidy" for U.S. competitors. Trade policy must explicitly address this problem and can no longer be pursued as if trade and exchange rates are unrelated.

In the global trade - exchange rate game U.S. policy makers have consistently abdicated their responsibilities, leaving U.S. manufacturers unprotected against the exchange rate manipulations of rival governments. Some of our major manufacturing trading partners, such as Japan and Korea, manipulate their currencies to give their exports a competitive edge. Guillermo Calvo, of the University of Maryland, has documented what he terms "fear of floating," whereby governments nominally commit to a floating exchange rate regime but then engage in systematic intervention to prevent appreciations.

The old Bretton Woods system of fixed exchange rates guarded against this type of unfair practice, but that system suffered from the need for large disruptive periodic exchange rate adjustments, and it could not withstand the powers of speculation created by liberalization of capital flows. The system that has replaced Bretton Woods encourages unfair exchange rate gaming, and it also allows exchange rates to be set by capital flows irrespective of trade deficits. The result is a system that is dysfunctional. This is illustrated by the current conditions which have seen the dollar appreciate strongly despite a record trade deficit that has conventional early warning financial crisis indicators flashing red.

There is no going back to the Bretton Woods arrangements. But placing exchange rate provisions in trade agreements, having co-ordinated G-7 exchange rate policy that is predicated on strong currency central banks doing the intervening, and making small modifications to the rules governing capital flows so as to allow central banks to slow inflows, would go a long way to making the international financial system work more fairly and productively. But before this agenda can be effected, policy makers will have to escape an ideology of financial markets that has them abdicating their powers of responsible intervention and governance. In the meantime, this ideology promotes a policy of dollar complacency that is deepening America's economic slump.

Figure 1 Broad trade weighted real dollar index, 1980 - 2001.

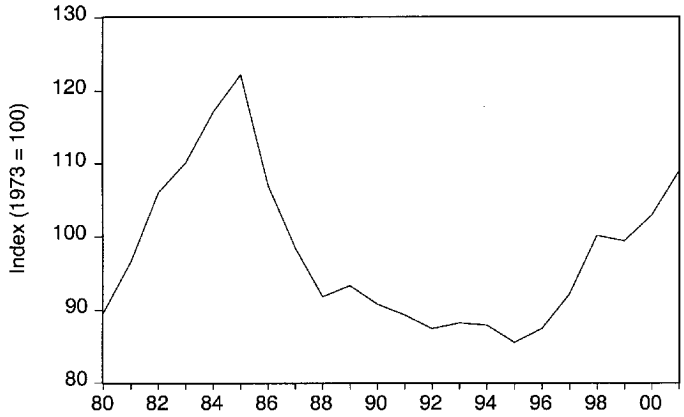


Figure 2 Real broad dollar index and Import/Export ratio, 1980 - 2001.

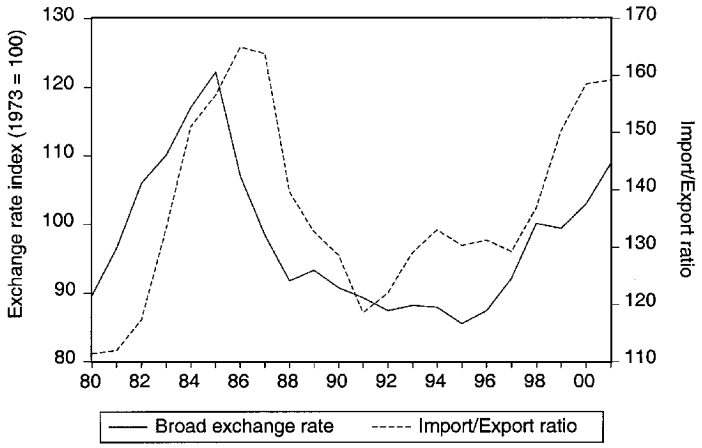


Figure 3 Exports plus imports as a percent of GDP, 1980 - 2001.

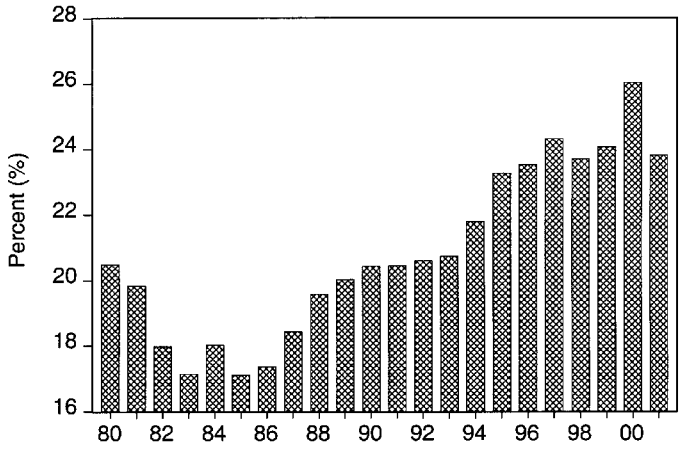


Figure 4 Manufacturing exports plus imports as a percent of manufacturing GDP, 1980 - 2000.

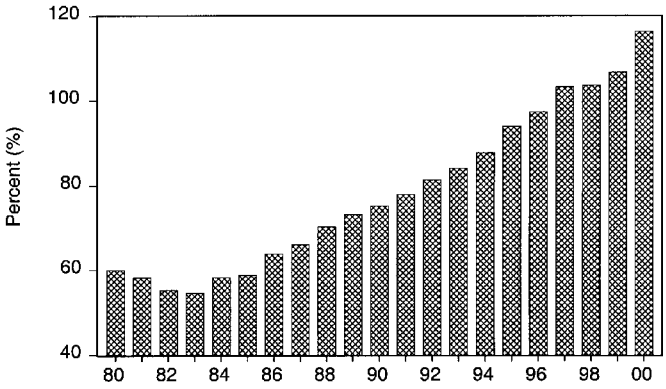


Figure 5 Manufacturing employment in the U.S. and Canada, 1990 - March 2002.

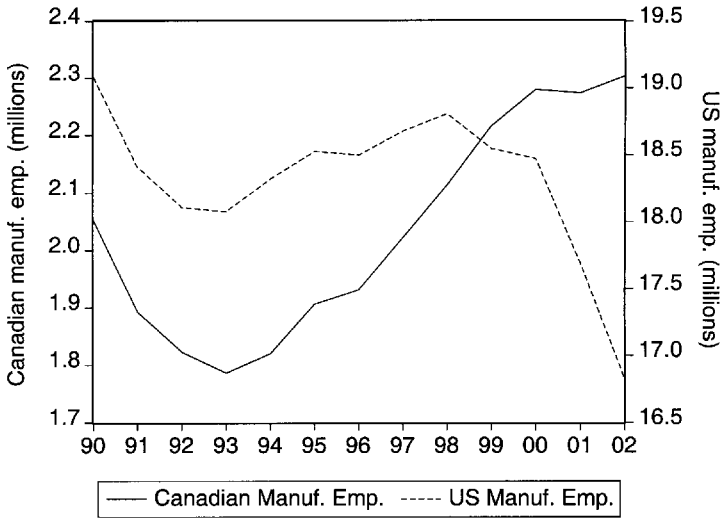


Figure 6 Manufacturing trade deficit as a share of manufacturing output, 1980 - 2000.

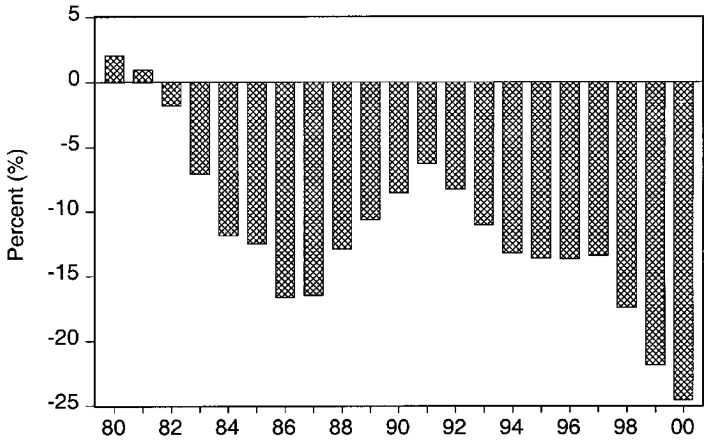


Figure 7 Balance on U.S. foreign income account, 1980 - 2001.

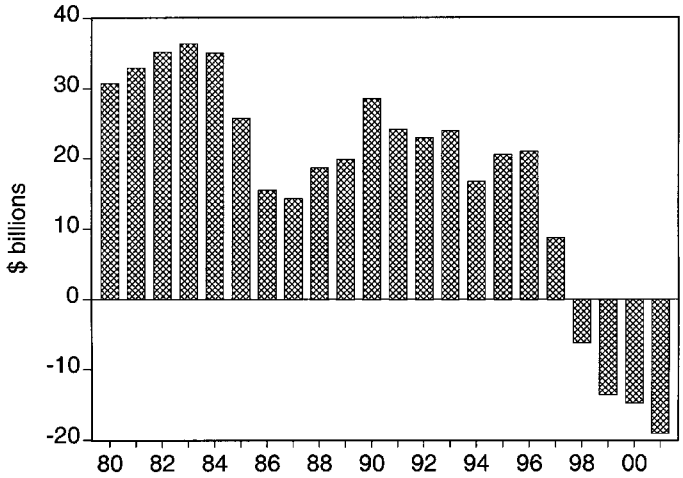


Figure 8 The Dow Jones Index and the real broad exchange rate, 1980 - 2001.

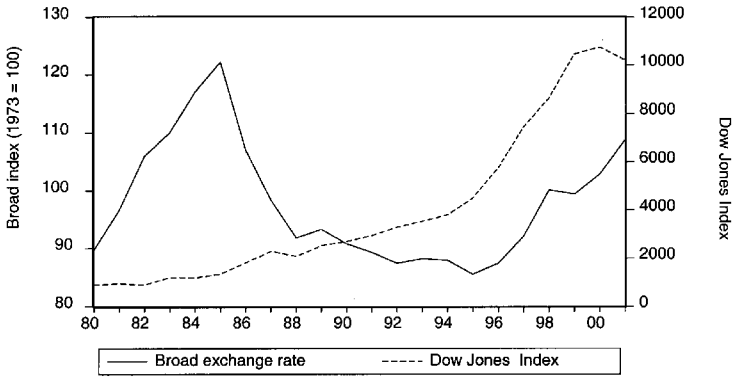
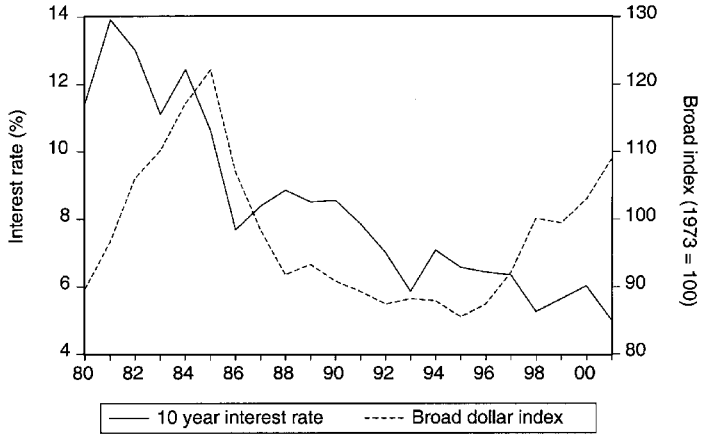


Figure 9 Real Broad dollar index and 10 year treasury interest rate, 1980 - 2001.



PREPARED STATEMENT OF JERRY J. JASINOWSKI

PRESIDENT, NATIONAL ASSOCIATION OF MANUFACTURERS

MAY 1, 2002

Mr. Chairman, Members of the Committee, I am pleased to be here this morning on behalf of America's manufacturers to participate in this discussion of U.S. International Economic and Exchange Rate Policy. U.S. manufacturing is suffering very strong negative effects from current U.S. exchange rate policy, and we appreciate the opportunity to state our views on the value of the U.S. dollar and the impact it is having on American industry.

The National Association of Manufacturers represents 14,000 American firms—10,000 of which are small- and medium-sized companies. Manufacturing is vital to America. It comprises one-fifth of all the goods and services produced by the U.S. economy and directly supports 56 million Americans—the nearly 18 million American men and woman who make things in America and their families.

I am pleased to join the other members of this panel today, and am particularly pleased to be testifying along with Richard Trumka, the Secretary-Treasurer of the AFL–CIO. The National Association of Manufacturers and the AFL–CIO differ on many things, but we are united in lock-step in our need to have the dollar begin reflecting economic fundamentals.

The Dollar is Overvalued, and Everybody Knows It

Mr. Chairman, I would like to make three points today: First, the U.S. dollar is very overvalued; second, this overvaluation is having a devastating effect on U.S. manufacturing and on jobs; and third, the overvaluation is fixable—for it is the result of market imperfections that are preventing the dollar from adjusting to a more normal level. How do we know the dollar is overvalued?

To begin with, NAM members are on the cutting edge of U.S. trade; and our members have been telling us that after years of being highly competitive in world markets, their customers are now saying the foreign currency price of made-in-the-USA products have become 25–30 percent more expensive than foreign products. This did not happen because U.S. producers became less productive or efficient. And it did not happen because they raised their dollar prices. It happened only because the price of the dollar rose in terms of foreign currencies.

About two-thirds of the companies represented at the recent NAM Board of Directors meeting said that the dollar is having serious effects on their firms, and this is an important reason why the NAM Board passed a resolution calling on the Administration to act to correct the dollar's overvaluation. A copy is attached to my statement.

The dollar is now at its highest level in 16 years. After remaining fairly stable for the better part of a decade, the dollar began a sharp climb starting in January 1997. It has now appreciated about 30 percent against major currencies, as measured by the Federal Reserve Board's widely-used price-adjusted index of major currencies. The sharp rise in the dollar is clearly evident in Figure 1, appended to my statement. This graph makes it plain that the dollar is not in any sense in "normal territory." In fact, the extent of the post-1997 climb of the dollar has been exceeded only once before—the severe overvaluation of the dollar in 1982–1985 that put U.S. trade into a tailspin. Unfortunately, a close look at Figure 1 shows an uncomfortable parallel to the path followed by the dollar in the early 1980's.

The dollar's rise has exactly the same effect as the sudden imposition of a new 30 percent tariff against U.S.-made goods. Congress and the Administration would howl with anger if Europe, Japan, Canada, and others were to slap such huge new tariffs on United States products—yet there has so far been little concern for an overvalued dollar that is doing the same thing. Worse, the dollar is also making many foreign products artificially cheap in the U.S. market. The Bureau of Labor Statistics' capital goods import price index, for example, has fallen nearly 20 percent in the last few years.

The NAM may have been the first in saying that the dollar was overvalued, but we are now in growing company. We are joined by over 50 trade associations representing manufacturing and agriculture, who have come together in the Coali tion for a Sound Dollar—advocating a dollar that is consistent with economic fundamentals.

We are also joined by the International Monetary Fund, whose just-released Global Economic Outlook says that one of the principal risks to the sustainability and durability of the upturn in the United States and elsewhere is the overvaluation of the dollar. The European Central Bank concurs in saying the Euro is "very undervalued" and the dollar is "very overvalued." The Chairman of the Bank

of England and of the G–10 Group of Central Bankers also said the dollar is overvalued.

U.S. Government officials have also commented. New York Fed President McDonough has said the dollar is overvalued. The Chairman of the President's Council of Economic Advisors, Glenn Hubbard, told the press that the strong dollar is bad for U.S. manufacturers.

The President's Trade Representative, Ambassador Zoellick, has said the strong dollar is leading to a flood of imports and providing export-led growth to other countries. Former Federal Reserve Board Chairman Paul Volcker testified last year that maintaining a stable U.S. economy might require "strengthening of the Euro and the yen relative to the dollar." And Keith Collins, Chief Economist, U.S. Department of Agriculture, said "The high value of the dollar is expected to continue to impair the U.S. competitive position in world markets. . . . The strong dollar not only makes U.S. products more expensive, it insulates foreign competitors from market price declines . . ."

Additionally, we are joined by the financial community. For example, Larry Kantor, Global Head of Currency Strategy for J.P. Morgan Chase told National Public Radio that, "We judge the dollar to be high relative to its fundamentals, something on the order of 20 percent at most . . ." And Morgan Stanley currency expert Joachim Fels, stated flatly to *Fortune Magazine* that, "The dollar is overvalued, and everybody knows it."

Then, finally, there is the Big Mac Index. Don't laugh, *The Economist Magazine's* Big Mac Index, comparing Big Mac prices around the world, has consistently been among the most accurate indicators of currency valuation and future currency changes. The current issue of the *Economist* says, "Overall, the dollar now looks more overvalued against the average of the other big currencies than at any time in the life of the Big Mac Index."

Even Paul O'Neill has commented on dollar overvaluation, and has in the past agreed that the dollar can become overvalued and depart from its normal level—harming U.S. industry. Of course, he wasn't Secretary of the Treasury when he said so. Nevertheless, his words from 1985 are surely indicative of his belief. When the dollar became badly overvalued in 1985, he said the strong dollar ". . . has turned the world on its head. We have suffered a major loss in competitive position because of exchange rates." He went on to say, "Exchange rates moving back to *normal* levels would be very good news for our industry. We would recoup most if not all of our export volume."

Mr. O'Neill's words were good advice then, and are just as relevant today.

The Overvalued Dollar is Having a Huge Effect

The overvaluation of the dollar is one of the most serious economic problems—perhaps the single most serious economic problem—now facing manufacturing in this country. It is decimating U.S. manufactured goods exports, artificially stimulating imports, and putting hundreds of thousands of American workers out of work. It is leading to plant closures and to the offshore movement of production away from the United States, with harmful long-term consequences for future U.S. economic leadership.

This is a matter to be taken seriously not only because of the cost in terms of jobs that have been lost, but also because manufactured goods comprise over 85 percent of all U.S. goods exports—and two-thirds of all exports of goods and services. America's ability to pay its international bills depends on America's manufacturing industry.

Effect on Trade and Jobs

The effect on U.S. manufacturing has been huge, as is detailed in the NAM analysis titled, "Overvalued U.S. Dollar Puts Hundreds of Thousands Out of Work," which I ask be made part of the record of this hearing. That report shows the dollar's overvaluation has had a major impact on exports, imports, the trade balance, and jobs.

Exports of U.S. manufactured goods have plunged $140 billion in the last 18 months, at an annual rate—the largest such fall in U.S. history (Figure 2). This fall, which is more than a 20 percent drop, is so huge that it accounts for close to two-fifths of the entire fall in U.S. manufacturing output and jobs in the current manufacturing recession—over 500,000 lost factory jobs.

The recession from which we are beginning to emerge was, to a remarkable degree, a manufacturing recession. Comprising 14 percent of the American workforce, the manufacturing sector accounted for 80 percent of the job loss in the entire U.S. economy. Manufacturing lost about 1,500,000 jobs—and over 500,000 of them were directly due to the unprecedented fall in American exports. The export losses, prin-

cipally due to the overvalued dollar, are a key factor explaining why the manufacturing sector has fared so much more poorly than the rest of the economy in this recession.

To put the $140 billion export drop in a different perspective, it is instructive to realize that the NAM estimates a successful Free Trade Area of the Americas agreement (FTAA) could triple U.S. exports to South America from $60 billion to $200 billion within 10 years of implementation—which is scheduled to begin in 2006. Thus over the next *14 years,* the FTAA may result in a $140 billion increase in U.S. exports. American exports have fallen by that much in just the *last 18 months!*

Additional hundreds of thousands of jobs have been lost on the import-competing side as well, though this is more difficult to measure. From the beginning of 1997 through the first quarter of 2002, U.S. manufacturing output rose 12 percent, while the volume of goods imports soared 45 percent—almost four times as fast. Much of this is due to the fact that import prices fell 10 percent relative to domestic manufacturer's prices. Import prices fell even more rapidly in some sectors—such as in imported capital goods, where they fell 17 percent, reflecting the rising dollar.

This is evident in what has happened to some individual industries. For example, prior to 1997 the U.S. paper industry routinely supplied about 80 percent of the growth in the U.S. market for paper. Since 1997, however, 90 percent of the growth in demand for paper in the United States has been met by imports. The U.S. paper industry has closed 60 plants since 1998.

The U.S. textile industry, through large investments and productivity improvements, and generally stable prices for Asian imports, had been able to hold its own until 1997. Since the dollar began to rise in that year, dollar import prices for textile products fell 23 percent, imports from Asia soared, and 177,000 U.S. textile jobs were lost.

The Treasury Department's periodic examinations of exchange rates and trade curiously have not mentioned any effect of exchange rates on trade. Instead the Treasury attributes all the U.S. trade changes solely to faster economic growth in the United States than abroad. While slower economic growth abroad certainly has contributed to the U.S. export slowdown, it has been a subordinate cause, and the principal cause has been the huge shift in relative prices brought about by the rise of the dollar.

For example, U.S. exports to the European Union dropped 20 percent over the last year and a half. European industrial production declined only about 4 percent during that time period. While this slowdown certainly had some influence on declining U.S. exports, typically each 1 percent change in European industrial production results in a little less than a 2 percent shift in U.S. exports. Thus, the decline in European industrial production should have cut U.S. exports by about 7 percent—leaving a 13 percent residual that can only be explained by the dollar's overvaluation.

A much stronger relationship exists between currency misalignment and trade shifts, as is depicted in Figure 3, attached to my statement, which clearly shows how dollar overvaluation affects trade flows. The graph shows two economic series: (1) the ratio of U.S. imports to U.S. exports—i.e., how much larger imports are than exports; and (2) the Federal Reserve Board index of the value of the dollar. Even a cursory examination of the graph shows the close relationship. The time lag between a change in exchange rates and a change in trade patterns is visible as well, particularly in the exchange rate peak in 1985 that resulted in imports cresting at being 80 percent larger than exports in 1987.

Largely as a result of the import and export effects of the overvalued dollar, the manufactured goods trade deficit has grown so much that it has reached a record 21 percent of U.S. manufacturing GDP (gross value added in manufacturing)—more than double what it was in 1997.

Treasury Secretary O'Neill was quoted recently in the press as saying that he thought the trade deficit was of no consequence because capital inflows are strong. We differ sharply with this statement, as does the International Monetary Fund and the vast preponderance of economic evidence. The current account deficit has three very significant consequences. The first is that the continuing deficit generates an ever-increasing load of foreign debt that one day will have to be paid, and at large cost. Federal Reserve Chairman Greenspan and many others, including a worried International Monetary Fund, have pointed out that there could be serious consequences on the United States and global economies.

The second aspect is its damage to U.S. industry—particularly to manufacturing. Perhaps one of the most worrisome aspects of the dollar-induced shift in the U.S. trade balance is what has happened to U.S. trade in technology-intensive products. This is America's most competitive sector, and is based on the best of American re-

search and development, productivity, and innovation. It is always a sector we have taken for granted in trade.

Indeed, as recently as 1997 it generated a $40 billion trade surplus for the United States. That surplus has been declining at an accelerating rate, and has now, for the first time in our history, moved into a substantial deficit, running at an annual rate of $20 billion. If the United States cannot compete in knowledge-intensive, technology-intensive trade, where can it compete?

The third aspect is that dollar overvaluation and the consequent huge trade and current account deficits erode support for free trade policies and contribute to rising protectionist sentiments. When industries and displaced workers see their sales and jobs disappearing because of falling exports and rising imports despite their best efforts to be competitive, their natural reaction is to urge that trade policies be changed. America's historic support for free trade policies was threatened in the 1980's overvaluation, and the current overvaluation and trade deficits are the principal reasons why public support for further trade liberalization is weak.

Effect on Small- and Medium-Sized Firms

While manufactured goods exports are widely assumed to be associated with large firms, in truth more than 95 percent of all exporters are small- or medium-sized firms. Exporting has been a major source of growth for small-manufacturers. For example, according to the NAM's surveys of small- and medium-sized member companies, the proportion of these companies that generated at least 25 percent of their total business from exports grew from 5 percent in 1993 to almost 10 percent in 1998—nearly doubling. With 95 percent of the world's consumers outside our country's borders, small manufacturers have found world markets to be a major source of growth and jobs.

Unfortunately, the sharp rise in the dollar over the last few years has led to a major reversal. Based on the most recent NAM survey of its small and medium membership, all the export gains since 1993 have been erased. Last year the proportion of smaller companies exporting at least 25 percent of their production fell to only 4.2 percent. And for this year, only 3.8 percent anticipate exports to be at least 25 percent of their business.

Effect on Earnings

Finally, American firms' profits have been strongly affected, including from the fact that profits from overseas operations have been reduced sharply as earnings from abroad are converted back into dollars. After recovering from a drop due to the Asian financial crisis in 1997, manufacturing after-tax earnings peaked at $76 billion in the first quarter of 2000. By the first quarter of 2001, earnings had collapsed to $−1.7 billion, a level not seen since the 1st quarter of 1992. Reduced exports, heightened import competition, and the conversion into dollars from operations abroad have had a major impact. Foreign operations, especially in Europe, represent a sizable proportion of global sales and profits for many large American firms. As foreign earnings are converted into dollars and have had to be marked down 30 percent or more because of the shift in currency values, the impact on total corporate profits has been huge. Corporate releases in recent weeks have been replete with reports of reduced earnings because of the overvalued dollar.

How Individual Companies Have Been Affected

To understand the real extent of the injury being caused to U.S. manufacturers it is necessary to look at the effect dollar overvaluation is actually having on individual companies and their employees. Many NAM member companies have written to the Treasury Department urging action to bring relief from the overvalued dollar.

Typically they relate that after having been competitive in world markets for years, they are now losing their foreign business. Many tell of export decreases of 25 percent, and some have lost almost all their export business.

Some letters are from large companies that are world industry leaders. Others are from small companies, many of them family-owned. They tell a story of being unable to compete not because of a decline in product quality or productivity and not because of any price increases in dollar terms—but only because of the rise in the dollar's value relative to other currencies. All of them are losing sales overseas or find they can no longer compete against imports into the U.S. market. Many of them are having to reduce their workforces. Others say they have no choice but to close their U.S. plant and start production overseas. This is the cost of having an overvalued currency.

These are not poorly-managed companies. They are not "whiners." They are among the best U.S. manufacturers, and many had built large export markets, won Government export awards, installed the latest machinery and technology, and

proudly sold their American-made products around the world. I have appended about a dozen of these stories to my testimony.

Correcting the Currency Misalignment

Currency values should—and over the longer term do—reflect economic fundamentals. However, the normal market adjustment mechanisms appear to have been thwarted in the case of the dollar's recent rise. While about one-fourth of the dollar appreciation since 1997 took place during 1997–1998 as capital fled to the safety of the U.S. economy in the wake of the Asian financial crisis, three-quarters of the rise in the dollar took place after 1998 in spite of, not because of, the economic fundamentals of the United States. In the face of slowing economic growth, declining interest rates, and rising manufacturing unemployment, the dollar has remained high.

Interest rate differentials are one of the key factors normally expected to affect exchange rates. In June 1999, the U.S. Federal Funds rate stood at 5 percent, roughly 2 percentage points above the European Central Bank's key lending rate. This was certainly a factor contributing to dollar strength. However, repeated interest rate cuts have now put the Federal Funds rate fully 1½ percentage points *below* European rates. Why hasn't the dollar fallen relative to the Euro?

Economic growth differentials are another important factor. In the late 1990's, U.S. economic growth averaged more than 4 percent, outpacing our major trading partners. However, U.S. economic growth slowed substantially beginning in the second half of 2000. By comparison, while economic growth in Europe and the Pacific Rim has also slowed, most analysts now expect economic growth to favor our trading partners overseas after the 1st quarter of 2002. Clearly, the impressive growth disparity between the United States and economies abroad in the late 1990's has shifted. Why hasn't this been reflected in exchange rates?

Trade and current account balances are important as well. The U.S. trade deficit now stands at more than $400 billion, or 4.4 percent of real GDP—up significantly from just 1.4 percent in 1997. During the late 1990's the outflow of U.S. dollars, which is the flip side of a large trade deficit, was largely used to acquire U.S. assets—primarily U.S. plant and equipment in the form of direct investment. However, business investment demand in the United States has been negative for 5 quarters running. Combined with continuing large trade deficits, this translates into an oversupply of dollars in the world financial system which should put downward pressure on the value of the dollar. Why hasn't that happened?

Unless economic theory is to be rewritten, clearly there are market imperfections at work. By far the most important factor interfering with the market is the Treasury's maintenance of a "strong dollar no matter what" policy, a carryover from the Clinton Administration. This rhetoric is artificially propping up the dollar—and causing severe economic dislocation especially for manufacturing.

The Treasury's statements are inherently contradictory. On the one hand it says that a strong dollar policy is necessary in order to continue to attract the capital needed to finance the trade deficit (which is caused by the strong dollar). On the other hand, its says that the dollar is strong because the United States is the best place to invest, and rapid foreign capital inflows are driving up the dollar through the free operation of the marketplace.

But if the latter were true—that the dollar remains strong because of market forces—then it wouldn't matter if the Treasury said the United States had a strong dollar policy, a weak dollar policy, or even no dollar policy at all. Markets would only care about the economic fundamentals of U.S. growth, productivity, and returns to capital.

But what would really happen if the Treasury announced it no longer had a strong dollar policy and was adopting a policy of benign neglect—letting the markets set the dollar wherever they thought it should be?

Larry Kantor, Global Head of Currency Strategy for J.P. Morgan Chase, answered that on National Public Radio recently, when he said that if markets, "hear even a slight change in the rhetoric, it does risk a pretty sharp fall in the dollar." Why? Because the dollar is very high compared to its economic fundamentals. It should have been adjusting for some time now, but has not.

If markets no longer believed the Treasury would keep the dollar at its present levels, market expectations would change overnight, realism would take hold, and the dollar's correction would begin immediately. As Morgan Stanley told *Fortune Magazine,* "the dollar is overvalued, and everybody knows it." Thus, we believe the Treasury's policy is in effect distorting the market and preventing market forces from working. It is time to end this policy and to allow the market to correct the valuation of the dollar.

Accordingly, we believe the Administration should stop and take the following steps:

1. Announce clearly that exchange rates are not reflecting economic fundamentals, that the Treasury is adopting a sound dollar policy of benign neglect, and that the United States will not intervene in exchange markets to maintain the value of the dollar.

2. Seek cooperation with other major economies in obtaining common agreement and public statements that their currencies need to appreciate against the dollar.

3. Make clear that the United States will resist, and take offsetting action as necessary, foreign country interventions designed to retard movement of currencies toward equilibrium.

4. Seek agreement that the G–8 countries should state their intention to work together, as they stated in 1985 when the dollar was badly overvalued, and to make a clear and unambiguous announcement at their next meeting, in June, that:

- external imbalances have become too great and are contributing to protectionist pressures which, if not resisted, could lead to serious damage to the world economy; and
- exchange rates should play a role in adjusting external imbalances and in order to do this exchange rates should better reflect fundamental economic conditions than has been the case.

Should currencies begin adjusting too rapidly, coordinated intervention in the market can assure an orderly movement. When countries coordinate intervention and clearly state their intentions, markets react. The experience of the 1985 Plaza Accord is instructive. This Accord restored currency stability and broke the back of the rising protectionism. The preponderance of economic research, meticulously reviewed in the September 2001 issue of the American Economic Association's highly respected Review of Economic Literature, makes it plain that highly visible coordinated action, including intervention, does work.

The Treasury's Report on Exchange Rate Policy

In concluding my remarks, Mr. Chairman, I would like to offer some views on the Treasury's Annual Report on International Economic and Exchange Rate Policy. Section 3005 of the Omnibus Trade and Competitiveness Act of 1988 requires the Secretary of the Treasury to provide Congress with periodic reports on exchange rates and economic policies.

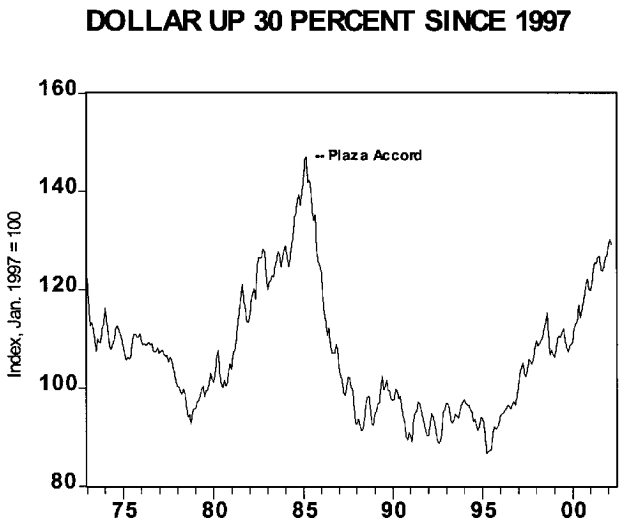
Of particular interest to the NAM is the requirement (Section 3005(b)(4)) that the Treasury's report include an assessment of the impact of the exchange rate of the dollar on production and employment in the United States and on the international competitive performance of U.S. industries. We have been disappointed consistently that the Treasury's reports have not, and do not, contain such an assessment. The reports have contained no discussion at all of the effect the appreciation of the dollar has had on trade in U.S. manufactured goods or in farm commodities.

More transparency and visibility is desirable here, both for policymakers and for the public. The NAM, therefore, recommends that the Commerce Department and the Agriculture Department be required by the Congress to begin preparing semiannual reports directly analyzing the effect of exchange rates on U.S. trade, production, and employment. These reports would be separate from the Treasury's macroeconomic reports, and would be produced independently by the Commerce and Agriculture Departments. Moreover, as part of their reports, they should be required to survey what private sector economists are saying about the effect of exchange rates on trade and production.

Mr. Chairman, I appreciate the opportunity of appearing before this Committee; and we look forward to working with you to persuade the Administration to drop its pegging of the dollar through its "strong dollar" policy and to adopt a "sound dollar" policy in which markets set currency rates based on economic fundamentals. The longer this change is delayed, the worse matters will get.

Thank you, Mr. Chairman.

Figure 1



Overvaluation beginning to rival the 1980's, when U.S. and other governments cooperated in the "Plaza Accord" to restore currency stability

Source: Federal Reserve Board Price-adjusted Major Currencies Dollar Index, re-based to Jan. 1997=100

Figure 2

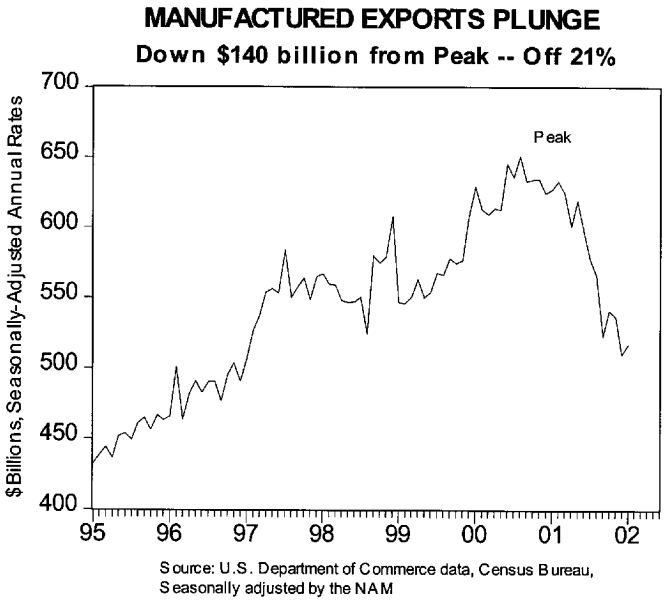
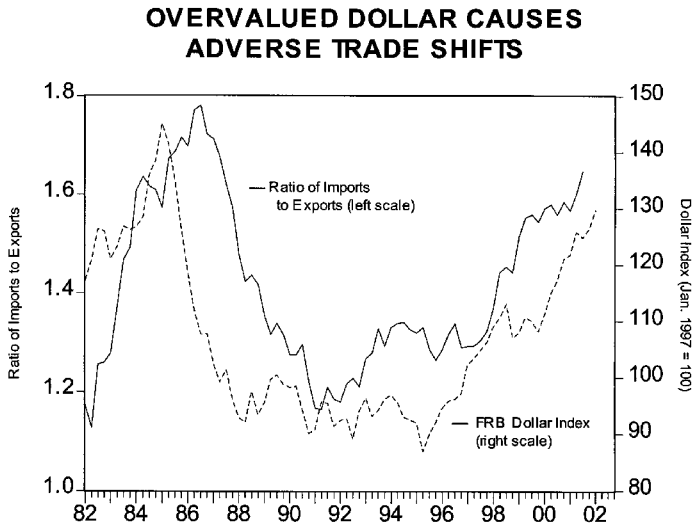

MANUFACTURED EXPORTS PLUNGE
Down $140 billion from Peak -- Off 21%
$Billions, Seasonally-Adjusted Annual Rates
700
650
600
550
500
450
400
Peak
95
96
97
98
99
00
01
02
Source: U.S. Department of Commerce data, Census Bureau,
Seasonally adjusted by the NAM

Figure 3



Imports Now 65% Larger Than Exports --
Closing in on Disaster of Mid-1980's Overvaluation

NAM Board Resolution
on Promoting a Sound Dollar

Whereas the National Association of Manufacturers favors a sound dollar that reflects economic fundamentals, but not one that is so excessively strong as to be overvalued;

Whereas the value of the U.S. dollar against other major currencies has risen 30 percent since 1997 and has reached the highest level in 16 years despite the fact that economic fundamentals have moved in the opposite direction;

Whereas this rise in the value of the dollar is imposing the equivalent of a 30 percent added tariff on U.S. exports and permits imports to be sold at artificially low prices in the United States – with the effect of severely hampering the exports of American manufactured goods, artificially increasing imports above what they otherwise would be, and distorting the earnings of U.S. affiliates overseas;

Whereas since August 2000 U.S. manufactured goods exports fell $140 billion – accounting for nearly 40 percent of the decline in U.S. manufacturing production and employment – accounting for the loss of over 500,000 factory jobs;

Whereas a broad range of U.S. industries have seen a sharp decline in their ability to compete against imports since the dollar began its climb in 1997, with commensurate additional losses of American jobs; and

Whereas small companies as well as large are being affected and, after rising steadily throughout the 1990's, the proportion of small and medium-sized companies exporting at least 25% of their production has now declined to the lowest level since the NAM began surveying;

Whereas the trade and job losses related to the excessive strength of the dollar are decreasing support for free trade policies and leading to increased pressures for protectionism;

Whereas the value of the dollar has failed to move in the direction of an equilibrium that would end trade distortions, principally because of market imperfections such as a belief that governments will intervene to keep currency relationships at their present levels --

Now therefore be it resolved that the National Association of Manufacturers urges the Administration to consider actions that can be taken to enable the dollar and other major currencies to move toward their equilibrium rates by correcting market imperfections, countering foreign country currency manipulations, and seeking cooperation among major countries in taking coordinated actions as appropriate.

Approved by the NAM Board of Directors March 9, 2002

APPENDIX:

Companies All Over the United States Are Being Injured by the Overvalued Dollar

Selected Examples Provided by Members of the NATIONAL ASSOCIATION OF MANUFACTURERS

To understand the real extent of the injury being caused to U.S. manufacturers it is necessary to look at the effect dollar overvaluation is actually having on individual companies and their employees. Many NAM member companies have written to the Treasury Department in recent months, urging action to bring relief from the overvalued dollar. Typically they relate that after having been competitive in world markets for years, they are now losing their foreign business. Many tell of export decreases of 25%, and some have lost almost all their export business.

Some of the letters are from large companies that are world industry leaders. Others are from small companies, many of them family-owned. They tell a story of being unable to compete not because of a decline in product quality or productivity and not because of any price increases in dollar terms – but only because of the rise in the dollar's value relative to other currencies. All of them are losing sales overseas or find they can no longer compete against imports into the U.S. market. Many of them are having to reduce their workforces. Others say they have no choice but to close their U.S. plant and start production overseas. This is the cost of having an overvalued currency.

These are not poorly-managed companies. They are not "whiners". They are among the best U.S. manufacturers, and many had built large export markets, won government export awards, installed the latest machinery and technology, and proudly sold their American-made products around the world.

Consider, for example, the following excerpts from letters NAM members sent to Secretary O'Neill:

- A small South Dakota firm that has received the President's "E" and "E-star" awards (the highest export excellence awards given by the U.S. government) said "The value of the U.S. dollar now makes us uncompetitive in almost all world markets…The 30% change in currency value is making us uncompetitive even in our own home market. We are a small business with our only manufacturing facility in South Dakota. We have been forced to make substantial layoffs of production and support personnel to adjust to this catastrophic problem."

- The president of an 82-year-old Green Bay Wisconsin manufacturing firm that exports to 70 countries and also has received the President's coveted "E" award, wrote that, "the strength of the dollar has had a profound effect upon our business, especially in the area of employment.

A year ago at this time we employed 1,625 people in the Green Bay area. Today that number is down by over 500 people… As this environment of a strong dollar has continued, we have been forced to consider relocating our manufacturing capabilities offshore."

- "Before the rise of the dollar, our exports were 70% of our business. Now exports are down to 15%", wrote a New Iberia, Louisiana capital equipment manufacturer.

- A major U.S. paper company wrote, "In the mid '90's about 10% of U.S. coated paper demand was satisfied by imports… most of it from Canada. Now, about 25% of the demand is satisfied by imports… much of it from Scandinavia and Korea… This isn't happening due to poor quality, or due to productivity differences or to information technology investments. It is a direct result of the disparity between the U.S. dollar and the euro and the won."

- An Ohio machine tool maker wrote about "the devastating impact" of the undervalued euro on his company and his industry. "Between 1990 and 1998 our exports represented an average of 25% of our total business. In 1999 exports represented only 7% of our bookings and there have been NO export orders in 2000. Our employment is down 33 percent."

- A Kentucky producer of automotive parts related how they had built a business exporting to two auto manufacturers in Germany, but as the dollar appreciated after 1997, their prices in deutschemarks rose up to 50%. As a result, they have not received any new orders from one of their German customers in the last two years. To keep their other customer, they are moving production out of the United States. "Because of the exchange rate, jobs will be lost at our Kentucky plant," they wrote.

- A $2 billion medical equipment manufacturer said, "…approximately 45% of our sales are overseas with a large portion being in Europe. Consequently the strong dollar with respect to the euro has caused us significant impact." If the situation remains, they said, "we will seriously consider alternatives … that will include moving jobs from the United States to foreign locations. Although we do not wish to engage in such a move, it may become imperative."

- "We started exporting our products in 1957 and by the early '70's export accounted for between 30% and 50% of our production," wrote the president of a New Orleans, Louisiana, "E-star" award winner. "Our machinery can be found just about any place in the world you can think of." But the overvalued dollar has made the company's t prospects "dismal", and killed off much of its overseas sales. "Our employment topped out at about 1,040 in the mid '90's, but presently stands at about 720".

- "Our manufacturing company was founded in 1897 and has met many challenges during these years," wrote a North Carolina company, "but we are not at all sure we can continue to meet the persistent negative of the overvalued U.S. dollar. Since 1998 our exports have decreased substantially…the price impact on many of our products has been 30-35% due to the overvalued dollar."

- An Indiana maker of veneer machinery had an even more dire story. "The dollar has risen almost 30% since 1997…foreign companies tell us they wish to buy our machinery but cannot afford it with the difference in currency value. Our foreign sales have dropped over 90% in the last four years…We cannot continue to survive without foreign markets…We need your help desperately."

- "We are a proud U.S. manufacturer of hardwood veneer located in Princeton West Virginia… our 190 employees have helped us gain a good reputation as a quality supplier to companies in 25 foreign countries." We are efficient manufacturers with some of the newest and most advanced machinery in the world.. but cannot offset the nearly 30% price increase due to the value of the dollar", the company's president said. "Since we export more than 60% of our total production, and most of this to Europe, you can imagine the impact the strong dollar is having on our company and small West Virginia community."

- "European competitors who at most were a 'fly in the ointment' over the years have now entered, with strength, the U.S. market due to the weakening of the euro", wrote a Massachusetts maker of specialty papers. "If something is not done to bring the dollar in line with the euro, it is likely that big companies will get smaller and small companies will disappear."

- Typical of many small companies, a Chicago manufacturer informed Secretary O'Neill that, "The current strength of the dollar is quite literally putting me out of business. When the German mark fell below $.60, I lost the business I had exporting to Canada…now I have lost the ability to manufacture a new part because my customer can import the product from Austria. The Austrian schilling is worth six cents in U.S. currency. If the Austrian schilling were above nine cents, as it was two years ago, I would easily have received the order….Since May of 1998 I have gone from 24 employees to currently 11."

- A Chattanooga, Tennessee, manufacturer said that despite modifying its products to meet European standards and hiring export sales personnel, they have been unable to keep European customers. "We find ourselves unable to price our products even within 30-40% of the price of comparable European or Japanese products… Without a doubt the reason for our higher prices in the export market is the inflated value of the dollar… We have had no choice but to cut production and lay off workers."

- And a Keokuk, Iowa, producer summed it up, saying he can not compete against a Swedish firm that has garnered a huge advantage as the Swedish kroner has gone from 7 to the dollar to 11 to the dollar in the last couple of years: "There is no way on God's green earth you can compete in a global market with that much disparity in currency…which means more down-sizing and loss of American jobs, not because they are not productive, but because of a currency factor which is totally unfair!!"

PREPARED STATEMENT OF BOB STALLMAN

PRESIDENT, AMERICAN FARM BUREAU FEDERATION

MAY 1, 2002

Mr. Chairman, Members of the Committee, I am Bob Stallman, President of the American Farm Bureau Federation and a rice and cattle producer from Columbus, Texas. AFBF represents more than 5.1 million member families in all 50 States and Puerto Rico. Our members produce nearly every type of farm commodity grown in America and depend on access to foreign markets for our economic viability.

We appreciate the opportunity to testify on the importance of the exchange rate to U.S. agriculture. Over-valuation of the dollar is one of the most pressing international economic problems facing America's agriculture and manufacturing sectors. U.S. farmers and ranchers have been losing export sales for the past 3 years because the dollar is pricing our products out of the market—both at home and abroad. In addition, the higher exchange rate of the U.S. dollar has resulted in rising agricultural imports due to increased purchasing power. The purchasing power of the dollar grew 21 percent from 1995 to 2000 in comparison to the exchange rate value of those nations that supply food to our country.

Agriculture is one of the most trade dependent sectors of our economy. Our sector has maintained a trade surplus for over two decades, but that surplus is shrinking. One of the primary factors affecting our declining trade balance is the strong value of the dollar.

In addition, the value of the dollar has significantly impacted agricultural employment. According to a recent USDA study, agricultural employment lost 87,000 jobs between fiscal years 1997 and 2000, a period in which the real agricultural exchange rate was rising rapidly and U.S. agricultural exports were stagnant.

The sharp rise of the dollar since 1995 has reduced our ability to compete in foreign markets. In 1996, U.S. agricultural exports reached a record $60 billion, but declined sharply to a low of $49 billion in 1999. This decline came as the U.S. dollar strengthened. USDA estimates that 14,300 jobs are lost for every $1 billion decline in agricultural exports. The short-term outlook for agricultural exports is not expected to improve significantly. Slow United States and global economic growth in 2001–2002 and a strong U.S. dollar will result in weak prices for the agricultural sector, according to USDA. The continued strength of the U.S. dollar will be a primary constraint on agricultural export growth.

We are deeply concerned about countries that engage in currency devaluations in order to gain an export advantage for their producers. The real trade-weighted exchange rates for agricultural exports from all of the major competitor countries, including Canada, Australia, Argentina, China, and Malaysia, have exhibited a long-term trend of depreciation against the dollar, contrary to market fundamentals. This trend has persisted over several decades, leaving it hard to conclude that this is not a deliberate monetary policy of these and other governments.

U.S. agriculture relies on exports for one-quarter of its income. In addition, about 25 percent of agricultural production in the United States is destined for a foreign market. A number of our commodities are highly dependent on trade for a sizable portion of their production. Some crops, like walnuts and wheat, about one out of two acres is exported. Exports now account for nearly one-quarter of our apple, beef and corn production and more than one-third of grapefruit and soybean production.

As productivity growth of U.S. farms and ranches continues to exceed the growth in U.S. population, our dependence on trade will increase. Only 4 percent of the world's consumers live in the United States. It is estimated that 99 percent of the growth in the global demand for food over the next 25 years will be in foreign markets.

Our country is also a major importer of food and fiber. The aggregate import share of U.S. food consumption has been rising steadily, along with the strength of the U.S. dollar. For nearly 20 years, imports accounted for 7.5 percent of total U.S. food consumption. The share of imports climbed to 8.6 percent in 1996 and 9.3 percent in 1999. These jumps in import share coincided with the strong value of the dollar and U.S. economic growth.

With a strong dollar, we have the double challenge of our products being less competitive in other markets while products from other countries are more competitive in U.S. markets.

In addition, there is a strong relationship between the value of the dollar and the domestic price of our commodities. As the value of the dollar rises, foreign buyers must spend more of their currency to purchase our exports. This causes foreign buyers to decrease their consumption of U.S. commodities or buy from our competitors

instead. The resulting drop in consumption drives U.S. commodity prices down even further.

Net farm income is not directly tied to the rise and fall of the U.S. exchange rate; rather it is the exchange rate that affects the price competitiveness of our exports. The resulting change in the volume of trade—increased exports when exchange rates are low and decreased exports when exchange rates are high—directly impacts farm income. As you know, U.S. agricultural commodity prices are the lowest they have been in over two decades. Further price depressions stemming from the strong value of the dollar are exacerbating an already dire situation.

The exchange rate is the single most important determinant of the competitiveness of our exports. Other important determinants of U.S. agricultural export values include income growth rates in developing countries, the growth and productivity of the foreign agricultural sectors against which we compete, export subsidies use by our competitors and weather conditions.

USDA's Economic Research Service estimates that movements in exchange rates have historically accounted for 25 percent of the change in U.S. agricultural exports. The elasticity of export demand for all agricultural products with respect to the value of the dollar is 1.38. This means that a 1 percent increase in the value of the dollar is associated with a 1.38 percent reduction in the value of U.S. agricultural exports.

The elasticity of export demand for individual agricultural commodities is 1.77, thus resulting in a 1.77 percent decline in the export value of specific commodities when the U.S. dollar appreciates 1 percent. The export dependency of U.S. agriculture, combined with the highly elastic response of U.S. agricultural export values to changes in the exchange rate underscore the need to maintain a stable exchange rate policy without overstating the value of the dollar.

The increasing strength of the dollar, and steady depreciation of the currencies of our major export competitors, has had a profound impact on our ability to export. In fact, the rising appreciation of the dollar is one of the primary reasons why the agricultural economy did not experience the economic prosperity that most other sectors of the U.S. economy enjoyed between 1995 and 1999. The dollar's increased purchasing power, and rising U.S. disposable income encouraged Americans to buy more imported products, while high prices of U.S. food and agricultural exports, in foreign currency terms, discouraged demand for our goods. As a result of the rapidly appreciating dollar, our competitors gained an advantage in third-country markets over our exports without even adjusting their sales price.

It is abundantly clear that the strong dollar is severely handicapping our ability to compete. Agricultural analysts note that macroeconomic fundamentals point to continued weak export performance in the near future.

For some commodities, the rising value of the dollar has directly contributed to the export competitiveness of our foreign rivals. Sharply depreciating currencies such as the Canadian and Australian dollars, the European Euro, the Brazilian real and the Korean won have enabled our competitors to out-compete us in a number of third-country markets.

The strong dollar is enabling our competitors to expand their production and gain market share at our expense. Recent USDA estimates note that U.S. corn export sales have fallen 3 percent and wheat shipments 10.5 percent as a result of the appreciation of the dollar.

Meats

Since 1995, the dollar has appreciated 42 percent against the currencies of beef producing countries. The rise in red meat imports from 6.4 percent in 1996 to 8.9 percent in 2000 is explained in part by the strength of the dollar. In addition, the recent announcement by McDonald's to buy imported beef was largely driven by the price advantage it faced vis-à-vis its competitors, other U.S. fast food chains that have historically used imported beef trimmings. Imported trimmings are cheaper than U.S. trimmings due to the strong U.S. dollar.

Horticultural Products

During the period 1995–2000, U.S. imports of fruits and nuts jumped 33 percent, largely due to the dollar's 18 percent gain with respect to the currencies of foreign suppliers of these commodities to the United States. The dollar rose only 3 percent against currencies of foreign vegetable importers to the United States. The appreciation of the Mexican peso in price adjusted terms helped to mitigate the strength of the dollar against the currency of Mexico, the country that supplies the majority of U.S. vegetable imports.

A Farm Bureau-commissioned study documented the impact of the exchange rate on corn, wheat, soybeans, and melons.

Corn

United States corn prices in Japan have been affected by adverse exchange rate movements. The U.S. landed corn price decreased from $3.64/bu in 1995 to $3.31/bu in 1998. The United States dollar appreciated 39 percent relative to the Japanese yen, from ¥94.23/$ to ¥130.81/$. The yen price of U.S. corn increased from ¥343/bu to ¥4331bu, an increase of 26 percent even though the U.S. dollar price had declined 9.1 percent. United States exports of corn to Japan fell 11.3 percent, from 16 mmt to 14.2 mmt.

Wheat

Exchange rates had similar impacts on the Mexican wheat market. Between 1995 and 1999, the price of United States wheat delivered to Mexico declined from $3.95/bu to $3.20/bu. The United States dollar appreciated 48 percent relative to the Mexican peso (NP) during this period from NP6.45/$ to NP9.58/$. This appreciation led to a 20 percent increase in the peso price of U.S. wheat from NP25.46/bu to NP30.64/bu, though the U.S. dollar price of wheat declined 19 percent. However, even with higher prices in peso terms, the volume of United States wheat exports to Mexico rose significantly during this time, from 791,000 mt to 1.8 mmt (130 percent). This contrasts with the Japanese results for two main reasons. First, Japan is a mature market with an established demand, extremely sensitive to price and geographically distant from major grain suppliers. Second, the growth of the Mexican market, coupled with its proximity to United States suppliers, has more than compensated for the increase in peso wheat prices.

Soybeans

Between 1996 and 1998 the U.S. average annual farm price for soybeans declined from $7.27/bushel (bu) to $5.93/bu, an 18.5 percent drop. Over the same period, the United States dollar appreciated 20 percent relative to the Japanese yen, going from ¥108.81/$ to ¥130.82/$. When the yen price of United States soybeans landed in Japan is compared over this period of time it is important to note that the price of U.S. soybeans in dollars fell from $9.09/bu to $8.16/bu, but in yen the landed price actually *increased* from ¥989/bu to ¥1,068/bu, an increase of 8 percent. The cost of United States soybeans to Japanese buyers increased primarily due to the appreciation of the United States dollar even though United States prices had fallen significantly. The result was higher priced United States soybeans in Japan when compared to soybeans from Brazil, which fell from ¥986/bu to ¥958/bu, allowing Brazilian soybeans to be sold in Japan for about $1.00/bu less than United States soybeans. United States soybean exports to Japan declined during this period from 3.9 million metric tons (mmt) to 3.7 mmt (200,000 mt, or 5 percent), while exports from Brazil increased from 379,000 mt to 524,000 mt (145,000 mt, or 38 percent).

Poultry

Recent empirical evidence supports the strong relationship between exchange rates and agricultural trade. Kapombe and Colyer[1] found that a 1 percent increase in the Japanese yen–United States dollar exchange rate led to a .96 reduction in Japanese demand for United States broilers. In addition, they also found that a 1 percent increase in the Hong Kong–United States exchange rate resulted in a .56 percent decline in Hong Kong demand for United States broilers, while a similar change in the Mexican peso–-United States dollar exchange rate led to a .58 drop in Mexican demand.

Melons

Other empirical studies have also documented the importance of the Mexican peso–United States dollar exchange rate in influencing United States imports of melons (Espinosa-Arellano, Fuller, and Malaga).[2] Their results suggest that the 1994–1995 Mexican peso devaluation increased United States imports of watermelon, honeydew, and cantaloupe by 36, 18 and 4 percent, respectively in the short run. In fact, a survey of historical empirical literature since the early 1970's has revealed that in 32 separate studies of the role of exchange rates on U.S. agricultural

[1] Kapombe, C.M. and D. Coyler. "A Structural Time Series Analysis of U.S. Broiler Exports." *American Journal of Agricultural Economics,* 21 (December 1999): 295–307.

[2] Espinosa-Arellano, J.J., S. Fuller and J. Malaga. "Analysis of Forces Affecting Competitiveness of Mexico in Supplying U.S. Winter Melon Market." *International Food and Agribusiness Management Review* 1, No. 4 (1998): 495–507.

trade, the exchange rate was found to be an important explanatory variable in 24 of the studies (Kristinek).[3]

Conclusion

American farmers are the most productive in the world. However, the comparative advantages that our producers generally enjoy, abundant, fertile natural resources, access to high-quality inputs and technology, for example, are mitigated by the rising appreciation of the dollar. The strong value of the dollar has, in many instances, shut our exports out of foreign markets and increased import competition in the U.S. market.

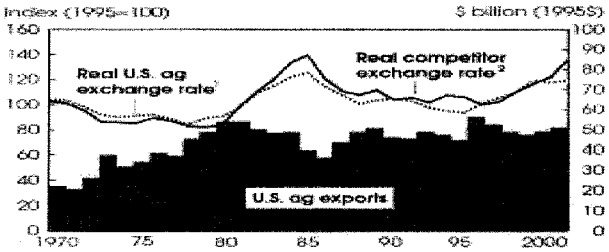
In short, U.S. agriculture is part of a worldwide food production system. We do not advocate isolation as a means to shield our sector from the economic forces that shape world trade. However, we cannot effectively plan our farming and ranching enterprises in a world where exchange rates suddenly depreciate by 50 percent, as happened with the Mexican peso in late 1994, or shift more slowly, such as the 50 percent decline in the Brazilian real from 1995 to 2000.

Exchange rate issues are certain to increase in importance as U.S. agriculture produces more for export markets and U.S. food and fiber markets become more open to imports. If these issues are not resolved by macroeconomic policies, there will be continued pressure to find solutions in traditional farm policies.

Effective long-range financial planning at the farm and ranch level and the overall economic health of U.S. agriculture depends on more stable exchange rates that do not overvalue the U.S. dollar against our competitors' currencies.

[3] Kristinek, Jennifer. "The Impact of Exchange Rates of Beef and Cattle Trade in North America." Texas A&M University, 2001.

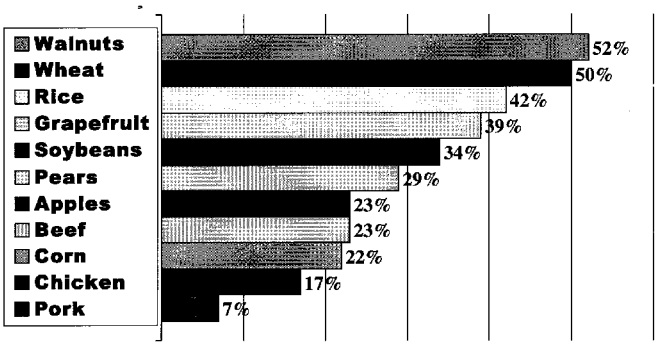
U.S. Ag Exports Remain Below Mid-1990's Peak As Dollar Strengthens



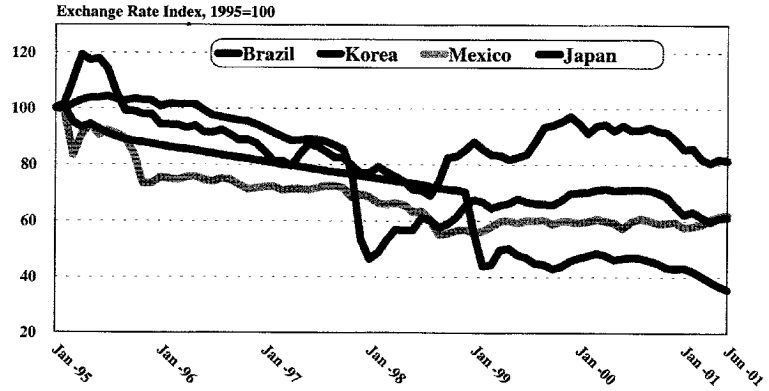
Total U.S. exports, 2000 preliminary.
1. Index of bilateral U.S. dollar exchange rates (U.S.-export market countries), adjusted for inflation and weighted by country shares of U.S. exports.
2. Index of bilateral U.S. dollar exchange rates (U.S.-competitor countries), adjusted for inflation and weighted by countries' export shares of world exports (excluding U.S.).

Economic Research Service, USDA

Percent of Production Exported

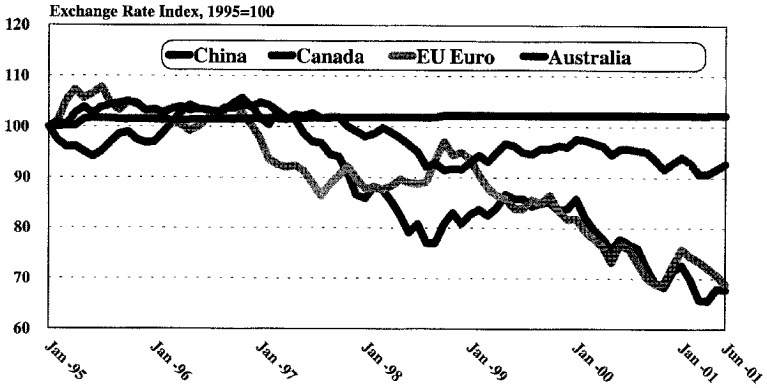


Selected Exchange Rate Indices, Foreign Currency/U.S. Dollar

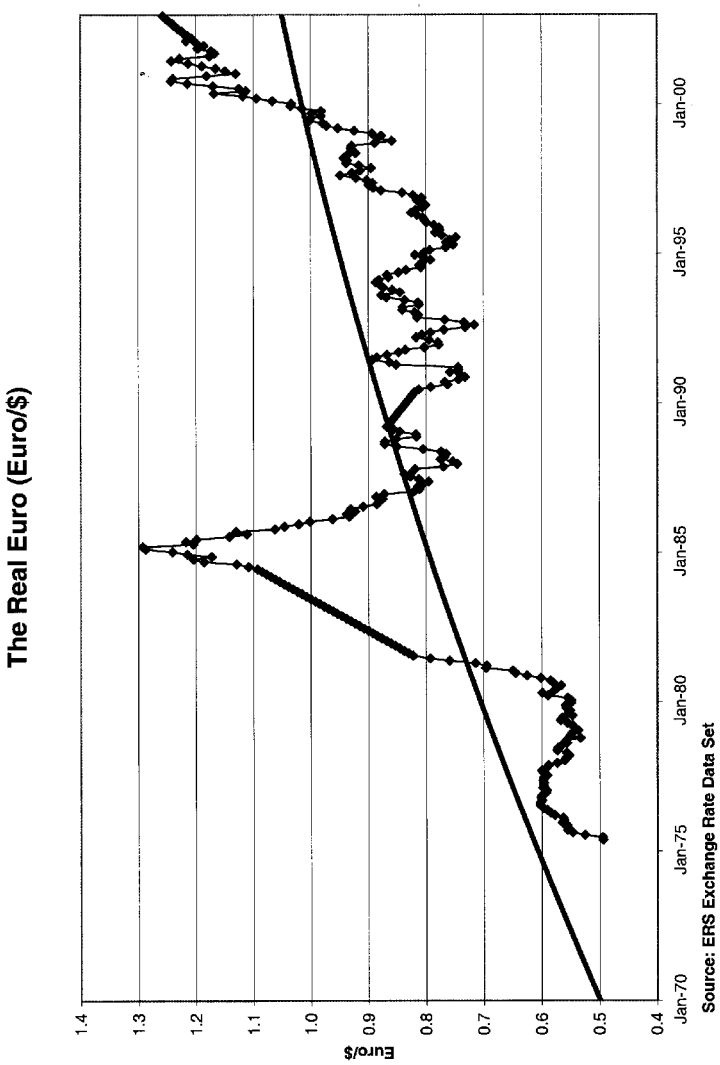


Federal Reserve Bank, St. Louis

Selected Exchange Rate Indices, Foreign Currency/U.S. Dollar



Federal Reserve Bank, St. Louis. Prior to 1999 the euro was the ECU.


The Real Euro (Euro/$)
Euro/$
1.4
1.3
1.2
1.1
1.0
0.9
0.8
0.7
0.6
0.5
0.4
Jan-70
Jan-75
Jan-80
Jan-85
Jan-90
Jan-95
Jan-00
Source: ERS Exchange Rate Data Set

PREPARED STATEMENT OF C. FRED BERGSTEN

DIRECTOR, INSTITUTE OF INTERNATIONAL ECONOMICS

MAY 1, 2002

The Rise of the Dollar

Since hitting its all-time lows in early 1995, the dollar has risen by a trade-weighted average of 40–50 percent in real terms against larger and smaller baskets of currencies of its trading partners. It has climbed by well over 50 percent against the yen and the European currencies. It could rise considerably further over the next year if the United States continues to recover more quickly and more robustly than Europe and Japan (or anybody else) from last year's worldwide slowdown, as is quite likely.

Every rise of 1 percent in the trade-weighted dollar produces a rise of at least $10 billion in the U.S. current account deficit.[1] Hence the currency's appreciation over the past 7 years accounts for a large share of the total external imbalance, which will probably approximate $500 billion this year and be close to 5 percent of GDP, entering the traditional "danger zone" where the United States and other OECD countries have traditionally experienced correction of their external deficits.[2] The deficits rose at an average rate of $100 billion (or over 50 percent) per year during the late 1990's, an explosive and obviously unsustainable path that may now have resumed. They dropped back to annual rates closer to $400 billion during 2001, with the drop in U.S. economic growth and hence import levels, but rose again sharply in the first quarter of this year (and in fact subtracted 1.2 percentage points from our economic growth in that period).

Our latest projections at the Institute for International Economics suggest that, absent any corrective action, the U.S. current account deficit will rise to 7 percent of GDP by 2006 (about $800 billion).[3] The previous sharp falls in the dollar, which have occurred about once per decade since the early 1970's, were triggered by external imbalances that never even reached 4 percent of GDP. Our latest calculation is that the dollar is overvalued in trade terms by 20–25 percent, i.e., a depreciation of that magnitude would reduce the current account deficit to the level of around 2–2½ percent of GDP that is likely to prove sustainable over the longer run.[4]

These annual imbalances add to the negative net international investment position of the United States, which reached $2.2 trillion at the end of 2000 as a cumulative result of the deficits of the past 20 years. As recently as 1980, the United States was the world's largest creditor country. It has now been the world's largest debtor for some time. Its negative international investment position is rising by 20–25 percent per year. This trajectory too is clearly unsustainable.

The Impact of the Strong Dollar

These external deficits and debts levy several significant costs on the United States:

- Over the longer run, they mean that *we will pay rising annual amounts of debt service to the rest of the world* with a consequent decline in our national income. These payouts are surprisingly small so far, amounting to only about $14 billion in 2001, because foreign investment by Americans yields a substantially higher return than foreigners' investments here. However, the numbers are clearly negative and will become substantially larger over time.
- In the short run, any *increases in the deficit subtract from our gross domestic product.* Export output falls and domestic demand that could be met by domestic output is instead satisfied by higher imports. U.S. output and employment suffer as a result and must be of concern unless the economy is at full employment because of booming domestic demand, as in the late 1990's (on which, see more below) but not now. Since most of our goods trade is in manufactured products, the deterioration of the trade balance has contributed substantially to the large,

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[1] William R. Cline, *American Trade Adjustment: The Global Impact,* Policy Analyses in International Economics 26, Washington: Institute for International Economics, 1989.

[2] See Catherine L. Mann, *Is the U.S. Trade Deficit Sustainable?,* Washington: Institute for International Economics, September 1999, especially pp. 156–57, and Caroline Freund *"Current Account Adjustment in Industrial Countries" International Finance Discussion Papers 692:* Federal Reserve Board of Governors, December 2001.

[3] Catherine L. Mann, "How Long the Strong Dollar?" Institute for International Economics, March 2002.

[4] Simon Wren-Lewis, *Exchange Rates for the Dollar, Yen and Euro,* International Economics Policy Brief 98–3, Institute for International Economics, Washington, July 1998. The International Monetary Fund has publicly expressed a similar view, e.g., in its *World Economic Outlook* of May 2001.

and perhaps permanent, loss of employment in that high-paying sector—whose wages average 13 percent higher and benefits average close to 40 percent higher than for the manufacturing sector as a whole.[5]

- At almost any time, markets could decide that the deficits and debt are unsustainable and reduce their new investments in dollars sufficiently to drive the exchange rate down sharply. The United States must attract about $2 billion of *net* capital inflow every working day to finance the deficits at their current level. Since gross U.S. capital outflows have been running about as large as the current account deficit, *our gross capital inflows must average about $4 billion per working day*—and totaled about $1 trillion in 2000. Any decline in the level of these inflows, let alone their reversal via a selloff from the $10 trillion of outstanding dollar holdings of foreigners, would produce increases in the U.S. price level and higher interest rates (and almost certainly a fall in the stock market as well). This "triple whammy" would severely hurt the U.S. economy.[6]
- In terms of domestic policy, large *external deficits and the overvalued dollar that produces them have been the most accurate leading indicator of resistance to trade liberalization* throughout the postwar period. Paul Volcker has recently noted, for example, the correlation between the roughly 30 percent tariffs on steel just imposed by President Bush and the decline of roughly 30 percent in the value of the Euro since its creation in 1999. The deficits generated relatively little concern in the late 1990's, because growth was so strong and unemployment so low, but are clearly doing so now as indicated by the other statements to the Committee this morning. Antitrade pressures will almost certainly rise again if the economy fails to resume rapid growth on a sustained basis and especially if unemployment fails to fall much from its current levels.
- It should also be noted that *a disorderly correction of the dollar's overvaluation would produce major foreign policy problems,* especially with Europe. A decline of 20–25 percent in the average value of the dollar would require a much larger decline against the Euro because the currencies of many of our closest trading partners (such as Canada and Mexico) would fall at least part of the way with the dollar itself. A complete dollar correction would in fact require the Euro to rise well beyond its initial starting point in 1999 and more than 30 percent above current levels. This would sharply reduce Europe's competitive position and trigger major complaints there, deeply exacerbating the transatlantic trade conflict that is already so severe.[7]

At the same time, it must be recognized that the external deficits and dollar appreciation provided important benefits to the U.S. economy during the boom period of the late 1990's. With growth at 5–6 percent in those years, and unemployment falling to a 30 year low of 4 percent, the sharp rise in net imports and the climb in the dollar itself helped to dampen inflationary pressures. The capital inflows that financed the deficit funded part of our investment boom and held interest rates in check, permitting monetary policy to accommodate the rapid growth. Under such circumstances, the "strong dollar" policy enunciated by the Clinton Administration (though never defined nor made operational) was defensible.[8]

No such defense is possible under current circumstances, however. The economic slowdown and rise in unemployment in 2000–2001 underlined the costs of the external deficit. The absence of inflationary pressure obviates the chief benefit of large net imports. The sharp reduction in interest rates over the past year reduces the need for large capital inflows. Investment is now limited by excess capacity and lagging demand, rather than by any shortage of capital, so that particular benefit of the earlier inflows has largely disappeared.

It is thus stunning that Secretary O'Neill, in an interview published on March 15, suggested that the current account deficit is "a meaningless concept" and that "the only reason I pay attention to it at all is because there are so many people who mistakenly do"—a very different view that he expressed as CEO of International Paper in the middle 1980's when the dollar was also hugely overvalued and he could observe its impact directly. Similar statements of "benign neglect" by his predecessor Secretary Donald Regan (and especially Under Secretary Beryl Sprinkle) in the first Reagan Administration turned out to be so wrong, and so costly for the economy, that they had to be totally reversed by the second Reagan Administration

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[5] Howard Lewis, III and J. David Richardson, *Why Global Commitment Really Matters!* Institute for International Economics, October 2001.

[6] For a more optimistic view, see Richard N. Cooper, *Is the U.S. Current Account Deficit Sustainable? Will It Be Sustained?* Brookings Papers on Economic Activity 2001:1, pp. 217–26.

[7] C. Fred Bergsten, "The Need for A TransAtlantic G–2," *The Washington Post,* April 2002.

[8] C. Fred Bergsten, "Strong Dollar, Weak Policy," *The International Economy,* July/August 2001 and "Ducking a Dollar Crisis," *The International Economy,* September/October 2001.

via the Plaza Accord in 1985 to drive the dollar down by 50 percent over the succeeding 2 years.

A New Dollar Policy

It is thus time for a change in the dollar policy of the United States. There is no basis for maintaining the "strong dollar" mantra of the prior boom period. *At a minimum, the United States and its G–7 partners should "lean against the wind" of any renewed dollar appreciation* to keep the problem from getting worse. Indeed, *they should now begin easing the dollar down toward its long-run equilibrium level* through a combination of altered rhetoric and direct intervention to support other currencies, especially the Euro.

The new policy should also make clear to other countries that the United States will not accept any efforts to competitively depreciate their currencies against the dollar. This dimension is particularly needed because Japan intervened massively last fall, once again, to keep the yen from rising as documented in the Treasury's latest Report to Congress on International Economic and Exchange Rate Policy. After halting the yen's rise, at about 116:1 against the dollar, the Japanese then actively talked it down to about 135:1. This latest episode of competitive depreciation of the yen apparently ended in January but it clearly had a major impact in the currency's level that persists today.

The Japanese characterized this intervention as part of an effort to combat deflation by pumping more yen into their economy. However, there are many other assets that the Bank of Japan could buy to expand domestic liquidity—even if one thought that doing so could be effective when demand for money is so low due to the depressed state of the Japanese economy. Moreover, it appears that the Bank of Japan sterilized the monetary effects of the currency intervention (as usual) so it made little or no contribution toward easing monetary conditions anyway.

The more plausible explanation of the intervention is that Japan was once again seeking to export its domestic economic problems to the rest of the world, as it has done on numerous occasions in the past. One can readily sympathize with Japan's plight, in light of its economy's "decade of decline" and the failure of so many of its efforts to use traditional monetary and fiscal instruments to restore growth.[9] One might even countenance a temporary decline in the yen that resulted from implementation of needed reforms in Japan, as suggested by the Administration during its early days.

But the renewed rise of Japan's trade surplus that is already evident will *ease* pressure on the country to take the decisive steps needed to deal with the huge problems of its banking system—the fundamental requirement to get its economy back on track—and cannot be accepted as an *alternative* to such reforms. Moreover, especially in the context of last year's global economic slowdown, any such exporting of Japan's problems to other countries is highly inappropriate and must be resisted—through all the relevant multilateral forums, notably the IMF and G–7, as well as bilaterally by the United States.[10] *It is thus disturbing that the new Treasury Report ignores the problem even after identifying and acknowledging the existence of the massive intervention last fall,* and indeed implies that it was somehow related to the terrorist attacks of September 11 and thus excusable.

On the broader issue of U.S. currency policy, *it is encouraging that neither Secretary O'Neill nor any other Administration official has repeated the "strong dollar" rhetoric since September 11, or even for some time before.* Though the Treasury denies that there has been any change in policy, the absence of "strong dollar" language is promising. *The Administration should now substitute advocacy of a "sound dollar," or some equivalent, to signal a substantive change in attitude.*

The presumed reason for the Administration's reluctance to embrace such a shift is a fear that the dollar could then shift course abruptly and go into a sharp decline that would trigger some of the deleterious consequences cited above. There is little risk of any such "free fall" for the foreseeable future, however, in light of the far stronger fundamentals of the United States economy (vis-à-vis both Europe and Japan) that have in fact held the dollar so high for so long. The dollar in fact remained quite strong during 2000–2001 despite the sharp falls in U.S. economic growth, interest rates, and equity prices—all of which would have traditionally been expected to produce a depreciation of the exchange rate. At the same time, there are no foreseeable sharp pickups in Europe or Japan (or anywhere else) that would

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[9] Adam Posen, *Restoring Japan's Economic Growth,* Washington: Institute for International Economics, 1998.

[10] C. Fred Bergsten, Marcus Noland and Takatoshi Ito, *No More Bashing: Building a New Japan—United States Economic Relationship,* Washington: Institute for International Economics, 2001.

pull large amounts of investment away from the United States. *Hence this is an excellent time to start easing the dollar down toward its sustainable equilibrium level,* especially as it has already fallen by 3–4 percent over the past few months and that "leaning with the wind" is most likely to be effective.

The worst policy course is to wait until the inevitable change in economic fortunes, whenever it comes, triggers a shift in market sentiment against the dollar. Coming on top of the huge underlying imbalance, such an alteration of investor views could indeed trigger a very sharp fall in our currency and a "hard landing" for the economy. There is in fact a third factor that could then also kick in and make the ensuing adjustment even nastier: The likely structural portfolio shift into Euros that will almost certainly occur at some point due to the likelihood that that currency, based on an economy as large as the United States and with even greater trade, will move up alongside the dollar as a global key currency.[11]

The risk of maintaining the Administration's policy of "benign neglect" would be substantially increased if the likely strong recovery of our economy over the next year or so were to trigger a renewed appreciation of the currency that, in combination with the growth pickup itself, would send our external deficits soaring even further.[12] Under such circumstances, continuation of the "strong dollar" rhetoric would be particularly inappropriate because it would encourage an even greater rise in the currency's overvaluation. It would be a huge mistake to let the dollar rise to levels from which it would be even more certain to come crashing down.

Such a situation would be reminiscent of what actually occurred in 1984–1985. Even after the "Reagan dollar" had risen by about 25 percent in 1981–1983, and already shifted the U.S. current account from balance in 1980 toward a deficit of over $100 billion, the dollar rose by another 25 percent or so in what all subsequent analysts have characterized as a purely "speculative bubble." The Reagan Administration itself was then forced to engineer the Plaza Accord in September 1985 to drive the dollar down by more than 50 percent against the other main currencies by the end of 1987.

There are of course those who doubt the effectiveness of sterilized intervention in the currency markets. Such a view ignores the fact that *all three cases of intervention by the Rubin–Summers Treasury worked in textbook fashion.* Joint United States–Japan intervention stopped and reversed the excessive strengthening of the yen in 1995. Similar intervention stopped and sharply reversed the excessive weakening of the yen in 1998. Joint U.S.–EU intervention in late 2000 stopped the slide of the Euro and prompted a 10 percent rebound. But the best evidence comes from the Administration itself: Why is it so afraid to alter the "strong dollar" mantra if it believes there would be no impact from doing so? Does anyone really think that the dollar would fail to decline toward a more desirable level if Secretary O'Neill and his G–7 colleagues were to start calling for such a correction? An effective alternative policy is clearly available.

We also know that currency depreciation, supported by sound domestic policies, produces the desired changes in current account balances with a lag of 2 or 3 years. The large dollar decline of 1985–1987, for example, led to virtual elimination of the U.S. current account deficit in the early 1990's. The sharp appreciation of the yen produced a similar correction in the Japanese surplus.

Hence there is a strong case for a new U.S. policy toward the dollar. Virtually every sector of the economy is now calling for such a change, as indicated at this hearing: The business community through the National Association of Manufacturers, labor through the AFL–CIO, agriculture through the American Farm Bureau. Important parts of Wall Street, including former Fed Chairman Paul Volcker and the chief economist of Goldman Sachs, have issued similar calls. It is time for the Administration to change its policy toward the dollar, to improve the prospects for the U.S. economy and U.S. trade policy, and to reduce the risks of the much more severe adjustment that will inevitably hammer us later if it continues to ignore the problem.

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[11] C. Fred Bergsten, "The Dollar and the Euro," *Foreign Affairs,* July/August 1997.

[12] The sharp reduction in the U.S. budget surplus, resulting from the tax cuts of early 2001 and the post-September 11 stimulus package, further enhances the prospect of larger trade deficits via a strong dollar. The fall in the surplus means that Government saving will decline sharply, by perhaps 2–3 percent of GDP, and that an equivalent amount of additional foreign capital will have to be imported—implying a similar jump in the trade deficit—unless private saving were to rise by a like amount, which is not only unlikely but also undesirable since the goal of the stimulus efforts is to promote *increased* consumer demand and thus a restoration of rapid economic growth. See C. Fred Bergsten, "Can the United States Afford the Tax Cuts of 2001?" American Economic Association, January 5, 2002.

PREPARED STATEMENT OF ERNEST H. PREEG

SENIOR FELLOW IN TRADE AND PRODUCTIVITY
MANUFACTURERS ALLIANCE/MAPI, INC.

MAY 1, 2002

Thank you, Mr. Chairman, for this opportunity to appear before your Committee to address the impact of the dollar on the U.S. balance of trade, economic growth, and long-term economic stability. I will focus my presentation heavily on one particularly disturbing aspect of the trade deficit, namely currency manipulation to commercial advantage by some trading partners, and in particular by China, the nation with whom we have the largest and most lopsided trade deficit. To put this issue in broader context, however, I begin with brief comments on three basic concerns I have about the chronic and very large overall U.S. trade deficit.

Three Basic Concerns About the Trade Deficit

The first, most immediate concern, is the impact of a larger trade deficit on U.S. economic recovery this year and next. The U.S. trade deficit was $345 billion in 2001, and could rise sharply to $400 billion or more this year, as a result of a faster initial rate of economic recovery in the United States compared with our major trading partners and the time-lagged adverse trade impact of the strengthening of the dollar over the past 2 years. More than 80 percent of the deficit—in the order of $350 billion this year—will fall on the manufacturing sector, which has been hardest hit by the economic slump of the past 18 months. U.S. manufacturing industry, through new product innovation and capital investment, is the engine for overall growth in the U.S. economy, and a major increase in the trade deficit for manufactures could be the Achilles' heel for the hoped-for strong rebound in such productivity-enhancing investment and sustained overall growth.

The second, somewhat longer term concern, is that the longer we maintain a trade deficit—or more precisely current account deficit—in the prospective order of 5–6 percent of GDP, the larger becomes the U.S. international debtor position, and the greater becomes the likelihood of a more disruptive "hard landing" for the dollar and the U.S. economy when the inevitable downward adjustment on trade account finally occurs. The chronic trade deficit has transformed the United States from the largest net creditor nation in the mid-1980's to the unprecedented largest net debtor nation approaching $3 trillion of net foreign debt today, projected to $5 trillion by mid-decade. There is near consensus that this foreign debt accumulation course is unsustainable and the question is rather how and when we will confront the point of unsustainability. I believe an earlier downward adjustment in the trade deficit—which would entail a depreciation of the dollar exchange rate by perhaps 10–20 percent—would be less disruptive and better for longer term economic stability, in the United States and for the world economy, than a prolonged further debt buildup until financial markets finally react against the dollar under the cloud of a $5 trillion U.S. foreign debt.

My third and even longer term—but no less important—concern about the trade deficit and the consequent buildup of foreign debt is the social inequity we are imposing on our children and grandchildren. A current account deficit of $500 billion per year means we are living beyond our means by roughly 5 percent of GDP, mostly for immediate personal consumption and to a lesser extent for investment.[1] This consumer binge is being paid for through foreign borrowing comparable to the current account deficit, and the resulting $3–$5 trillion buildup of foreign debt is being left to our children and grandchildren to service indefinitely or to pay off fully in principal. With a younger generation of Americans already concerned about paying rising Social Security and Medicare commitments to the current older generation, the foreign debt buildup is one more intergenerational income transfer being undertaken essentially by stealth.

These are my three principal concerns about the trade deficit. As to what we can or should do to reduce the deficit, there are two principal remedies. The first is to increase domestic savings, thereby reducing the need to borrow abroad, about which there is more in the concluding section of this presentation. The second and more immediate way to reduce the trade deficit is to restrain others from "manipulating" their exchange rates to commercial advantage.

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[1] Actually, about 80 percent consumption and 20 percent investment. For a full explanation of this important yet often misunderstood relationship, see Ernest H. Preeg, *The Trade Deficit, the Dollar, and the U.S. National Interest* (Hudson Institute, 2000), Chapter 4; a briefer explanation by the author is in "A rose-tinted view of the deficit," *Financial Times,* June 22, 2000.

U.S. Benign Neglect of Currency Manipulation by Others

We currently have a predominantly floating exchange rate international financial system. The United States has a basically free float policy, with official market intervention rare and in only token amounts. The EU, Canada, and Mexico have similarly followed a free float during the past several years. Others, however, particularly in East Asia, implement a heavily managed float through large scale official purchases of foreign exchange, principally dollars, in order to keep their exchange rates lower than they would be subject to market forces alone, and consequently to push the dollar higher. This managed approach is "mercantilist" in that the objective is to maintain a large trade surplus as a matter of national policy, and the result for the United States is a trade deficit larger than it would be based on market forces alone.

Article IV of the IMF Articles of Agreement states that members shall, "avoid manipulating exchange rates to gain an unfair competitive advantage," and, under IMF surveillance procedures, a principal indicator of such manipulation is "protracted large scale intervention in one direction in the exchange market." Protracted purchases of dollars by certain East Asian central banks would thus clearly qualify as currency manipulation, under the IMF definition, but the U.S. Treasury has rarely raised the issue, preferring a policy of benign neglect.

Japan, the largest trade surplus nation in the world, is an outstanding example of such currency manipulation, with $250 billion of official foreign exchange purchases (almost all dollars) since 1995, including $33 billion in September and October 2001 alone when market forces were putting upward pressure on the yen. The yen, meanwhile, declined by 15 percent vis-à-vis the dollar during 2001. South Korea is another more recent example of such currency manipulation. The Korean central bank bought $9 billion of foreign exchange during 2001 while the nation recorded a $9 billion trade surplus. In effect, the central bank purchases entirely offset any upward pressure on the won from the trade surplus, and the Korean currency, in fact, depreciated 5 percent against the dollar during the year.

This form of currency manipulation does not, of course, explain all of the strengthening of the dollar vis-à-vis these currencies in recent years, but currency traders know that the central banks involved will not let their currencies strengthen significantly, and therefore they hold back speculative purchases even when market conditions would otherwise indicate a currency appreciation. It is also noteworthy that the relevant indicators involved are *net* figures, whether for central bank intervention, trade flows, or capital market transactions, and on this basis the net purchases of foreign exchange by the Bank of Japan in recent years have probably held the yen at a significantly lower level than would have prevailed based on market forces alone. And consequently, Japan has likewise maintained a significantly larger trade surplus with the United States, especially in price-sensitive industries such as the automotive sector.

The Uniquely Powerful Chinese Currency Manipulation

Chinese exchange rate policy is an important special case which spells currency manipulation in a different way. The Chinese currency has a fixed rate to the dollar but is nonconvertible on capital account. Over the past year, there has been a $25 billion trade surplus, a $45 billion net inflow of foreign direct investment—which also puts upward market pressures on the exchange rate—and over $50 billion of central bank purchases of foreign exchange. In this case, the central bank purchases offset almost three-quarters of market-generated upward pressure on the yuan from the trade surplus and the FDI inflow combined. Moreover, these official foreign exchange purchases may have been even larger except for an unfolding financial scandal involving billions of dollars of missing reserves.[2]

Based on the IMF definition, China has clearly been manipulating its currency for mercantilist purposes. The Bank of China has made protracted large scale purchases of foreign exchange—$150 billion since 1995—in order to maintain a large trade surplus as an offset to poor growth performance in the domestic economy. A direct measure of the manipulation is not possible because of the nonconvertible fixed exchange rate. There is no doubt, however, that if the central bank had not purchased $50 billion in 2001, there would have been strong upward pressures on the yuan in formal and informal markets. The bottom line is that the Chinese yuan is substantially undervalued and should certainly not be devalued as the Chinese government occasionally threatens to do.

[2] See the *Financial Times,* January 16, 2002, "Banker's fall throws spotlight on China's missing billions."

The Benefits and Costs of Chinese Currency Manipulation

The unique form of Chinese currency manipulation provides a mix of benefits and costs for China and for the United States. The most direct result is a larger trade surplus for China, which means more export-oriented jobs in the Chinese economy. From the United States point of view, of course, it means a larger trade deficit with China and the loss of export-oriented and import-competing jobs. In 2001, United States imports from China were $102 billion, or more than five times larger than the $19 billion of United States exports to China.

One problem for China in implementing currency manipulation through a fixed but nonconvertible exchange rate is that it creates breathtaking opportunities for official corruption, as noted above. A floating rate, however heavily managed, would do the manipulation job more efficiently, as it does for Japan, and China will, for this and other reasons, likely move in this direction as its economy becomes progressively more open to international trade and investment.

Additional benefits to China from its cumulative purchase of foreign exchange accrue in other areas of foreign policy. With $220 billion of ready cash in the central bank—far greater than any measure of "adequate" reserves for commercial purposes[3]—Chinese purchases of weapons and other military equipment abroad, as regularly received from Russia, in particular, can be made without financial constraint.

A similar conclusion can and should be drawn about China as an economic aid "graduate." There is no longer any justification for China to receive several billion dollars per year in long-term loans on favorable terms from the World Bank, the Asian Development Bank, and some bilateral donors, when there are $220 billion of unutilized funds stashed away in the Central Bank. And yet the development banks continue to lend large sums to China!

Another geo-economic advantage to China from its large reserves is the ability to offer concessionary trade and investment finance to other Asian nations, particularly in Southeast Asia, as a means of strengthening Chinese economic engagement in the region at the expense of the United States. Some first steps along these lines have been taken together with Japan, to weaken "United States economic hegemony," and such trade-related incentives will likely be expanded in support of the recent Chinese initiative for a free trade arrangement with the Association of Southeast Asian Nations (ASEAN).

Finally, and more speculatively, China at some future point could use its official dollar holdings as foreign policy leverage against the United States by threatening to sell large quantities of dollars on the market, or merely shift its reserves away from dollars and into Euros and yen. This will not happen anytime soon because the result would be a decline in the dollar and an adverse impact on Chinese exports. At some future point, however, if China were to become less dependent on exports to the United States for economic growth, such a threat could become credible. For example, the threat of substantial Chinese sales of dollars, with its implications for a disruptive decline in the dollar and the U.S. stock market, especially during a downward phase in the U.S. economy and/or an election year, could influence the course of U.S. policy toward Taiwan. Chinese military officers, in fact, in their studies of nonconventional defense strategies, include reference to George Soros and his attack on the British pound in 1992 as a template for disrupting a rival's (i.e., the United States) economic system.

Thus, the Chinese currency manipulation is very real and substantial, with wide-ranging implications, and it deserves, as a policy response, something more than the total official neglect it has received up to this point.

A Long Overdue Policy Response

The United States should adopt a clear and forceful strategy for reducing its chronically large external deficit. Indeed, such an initiative is long overdue.

The first step in such a strategy would be to have frank discussions with major trading partners as to why it is a mutual interest to reduce current imbalances on current account. These consultations could take place within the G–7 finance ministers' framework and with key trading partners, including China, Mexico, and South Korea.

The substance of the strategy should begin with a joint commitment to a free or very lightly managed floating exchange rate relationship, except for those nations engaged in full monetary union. Within this international financial framework, the macroeconomic response would be for the United States to take steps to increase its domestic savings while other, large trade surplus countries would take cor-

[3] The World Bank rule of thumb for adequate reserves is 25 percent of annual imports; China and Japan now have foreign exchange reserves of approximately 100 percent of annual imports.

responding steps to increase domestic consumption. These domestic steps would force adjustment in the trade imbalances, in large part through downward movement of the dollar exchange rate.

The U.S. policy objective for the exchange rate would consequently change from current categoric support for a strong dollar to a neutral reliance on market forces to establish the rate, with the expectation of some downward adjustment of the dollar in parallel with a declining trade deficit. Such a United States stated objective, in conjunction with complementary statements by major trading partners, would, in itself, likely lead to some decline in the dollar and the beginning of the trade adjustment process.

Another immediate objective should be to restrain others from further currency manipulation to competitive advantage. This could be done through G–7 and bilateral discussions and, in parallel, more formal consultations within the IMF. The point of departure would be that nations with persistently large trade surpluses—and even more so if they have large FDI inflows as well—should cease official purchases of foreign exchange or any other actions that would maintain their currencies below market-determined levels. A joint announcement to this effect should further influence financial market behavior, with upward pressures on floating currencies that have recently been subject to substantial manipulation, such as the yen and the Korean won, and corresponding downward movement of the dollar.

China, once again, is an important special case in view of its nonconvertible fixed rate to the dollar, and should thus be given a very high priority for bilateral consultations. The mutual interest in reducing the extremely lopsided bilateral trade account should be assessed in detail, starting with the question as to why China has such a large trade surplus with the United States and moderate trade deficits with most other trading partners. A United States request to China to cease official foreign exchange purchases and to adjust its fixed rate upward would define the immediate United States objectives. The longer term transition of China toward a fully convertible, floating rate relationship with the dollar should also be examined seriously, as a mutual interest, and as the best way to avoid trade conflict resulting from further unjustified Chinese currency manipulation.

PREPARED STATEMENT OF STEVE H. HANKE

PROFESSOR OF APPLIED ECONOMICS
JOHNS HOPKINS UNIVERSITY

MAY 1, 2002

Mr. Chairman, thank you for this opportunity to express my views on exchange rate policies. Commentary about exchange rate policies often originates in polemical, and more or less political, attempts at self-justification. In consequence, the discourse is often confused and confusing. In an attempt to bring some clarity to the topic, I will begin by presenting some principles and characteristics of exchange rate regimes.

Exchange Rate Regimes

There are three types of exchange rate regimes: Floating, fixed, and pegged rates. Each type has different characteristics and generates different results. Although floating and fixed rates appear to be dissimilar, they are members of the same family. Both are "automatic" free-market mechanisms for international payments. With a "clean" floating rate, a monetary authority sets a monetary policy, but has no exchange rate policy—the exchange rate is on autopilot. In consequence, the monetary base is determined domestically by a monetary authority. In other words, when a central bank purchases bonds or bills and increases its net domestic assets, the monetary base increases and vice versa. Whereas, with a fixed rate, a monetary authority sets the exchange rate, but has no monetary policy—monetary policy is on autopilot. In consequence, under a fixed-rate regime, the monetary base is determined by the balance of payments. In other words, when a country's official net foreign reserves increase, its monetary base increases and vice versa. With both of these free-market exchange rate mechanisms, there cannot be conflicts between exchange rate and monetary policies, and balance-of-payments crises cannot rear their ugly heads. Market forces automatically rebalance financial flows and avert balance-of-payments crises.

Floating- and fixed-rate regimes are equally desirable in principle. However, floating rates, unlike fixed rates, have rarely performed well in developing countries because these countries lack (in varying degrees) strong independent institutions,

coherent and predictable systems of governance and the rule of law. Accordingly, they cannot establish confidence in their currencies. Indeed, they usually lack either a sound past performance or credible guarantees for future monetary stability. In consequence, a floating currency usually becomes a sinking currency in a developing country.

Fixed and pegged rates appear to be the same. However, they are fundamentally different. Pegged rates are not free-market mechanisms for international payments. Pegged rates (adjustable pegs, bands, crawling pegs, managed floats, etc.), require the monetary authority to manage the exchange rate and monetary policy simultaneously. With a pegged rate, the monetary base contains both domestic (domestic assets) and foreign (foreign reserves) components. Unlike floating and fixed rates, pegged rates almost always result in conflicts between exchange rate and monetary policies. For example, when capital inflows become "excessive" under a pegged system, a monetary authority often attempts to sterilize the ensuing increase in the foreign component of the monetary base by reducing the domestic component of the monetary base. And when outflows become "excessive," an authority attempts to offset the decrease in the foreign component of the base with an increase in the domestic component of the monetary base. Balance-of-payments crises erupt as a monetary authority begins to offset more and more of the reduction in the foreign component of the monetary base with domestically created base money. When this occurs in a country with free capital mobility, it is only a matter of time before market participants spot the contradictions between exchange rate and monetary policies and force a devaluation. Table 1 summarizes the main characteristics and results anticipated with floating, fixed, and pegged exchange rates, when free capital mobility is allowed.

The Evolution of U.S. Exchange Rate Regime Policies

If a country adopts a fixed exchange rate regime (either an orthodox currency board[1] or official "dollarization") and allows free capital mobility, it must give up monetary autonomy. Alternatively, if a country wants monetary autonomy and free capital mobility, it must adopt a floating exchange rate. If a country has a pegged exchange rate, it must restrict capital mobility to avoid balance of payments and currency crises.

Over the past decade, the advantages of free capital mobility have become clear, and restrictions of capital mobility have been dramatically reduced. However, most developing countries have continued to employ some variant of pegged exchange rates. And not surprisingly, major balance of payments and currency crises have occurred frequently in the 1990's.

In a world of increasing capital mobility, the U.S. Government had no coherent policy on exchange rates until the late 1990's. Motivated by criticism from a small group of economists (including myself), Former Senator Connie Mack's campaign for official dollarization in countries with low quality currencies, and the fallout from the currency crises that engulfed Mexico, Asia, and Russia, the U.S. Treasury finally produced a clear policy statement on exchange rate regimes. Given that the U.S. embraces free capital mobility, Treasury Secretary Robert Rubin correctly concluded, in a speech made at The Johns Hopkins University on April 21, 1999, that either floating or fixed exchange rates were acceptable, but that pegged rates were not. And shortly after Lawrence Summers became Treasury Secretary, he presented the same policy conclusions at an address he delivered at Yale University on September 22, 1999. Stanley Fischer, the Former Deputy Managing Director of the International Monetary Fund, weighed in with the same message, when he delivered the Distinguished Lecture on Economics in Government at the annual meeting of the American Economic Association in New Orleans on January 6, 2001.

With these policy pronouncements, the U.S. Treasury's (and the IMF's) position on exchange rates became clear. In principle, the position was correct. In practice, it was (and continues to be) applied correctly in the case of the U.S. dollar, where a floating exchange rate regime continues to be embraced. In developing countries, however, the United States and the IMF have not adhered to the position with any rigor. For example, Brazil and Turkey were both given the green light to continue or establish pegged exchange rate regimes shortly after U.S. officials indicated that these set-ups were, in principle, unacceptable.

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[1] Contrary to the popular impression, Argentina's convertibility system was not an orthodox currency board. Some students of currency board systems pointed this out almost a decade ago. They anticipated that Argentina's convertibility system would eventually degenerate into a pegged exchange rate system and that it would blow up. See Steve H. Hanke, Lars Jonung and Kurt Schuler, *Russian Currency and Finance: A Currency Board Approach to Reform.* London: Routledge, 1993, pp. 72–77.

The Bush Administration has not yet articulated a clear policy on exchange rate regimes. Secretary O'Neill would do well to clear the air and make a statement along the same lines as Messrs. Rubin and Summers. Indeed, since the United States espouses free capital mobility, the only logical course is for U.S. policy to embrace floating rates or fixed rates (orthodox currency boards or official dollarization), and to reject pegged rates. With the departure of Stanley Fischer, the IMF's position on exchange rate regimes has become fuzzy. Anne Krueger, Fischer's successor, would do well to follow his lead and reaffirm Fischer's conclusions.

The "Strong" Dollar Mantra

The exchange rate—the nominal exchange rate quoted in the market—is a price. With a floating exchange rate policy, the price freely adjusts to changes in individuals' and business' expectations about conditions here and abroad. The dollar broadly strengthened against other currencies after the mid-1990's because market participants expected to receive higher rates of return on their investments in the United States than abroad. For example, consider for a moment the fate of the Euro versus the dollar since the Euro's launch on January 1, 1999. Then, the exchange rate was 1.17 dollars per Euro; today it's about 0.90. The dollar strengthened by 30 percent against the Euro primarily because market participants anticipated brighter prospects and higher rates of return in the United States than in Euroland, and capital flowed out of Euro-denominated assets into equities, bonds, and other U.S. investments.

This brings me to the "strong dollar" mantra. This rhetorical phrase, which was prompted by the dollar's broad strength in the markets, is unfortunate and confusing, at best. The combination of a floating exchange rate and the pursuit of low inflation, which the United States has had for many years now, is a policy. The "strong dollar" is not. Indeed, given a floating exchange rate regime, it is impossible to know what a so-called strong dollar policy *is* because the price of the dollar on foreign-exchange markets is on autopilot. The price is (or should be) determined by buyers and sellers, and U.S. Government officials should refrain from trying to influence it by "open-mouth operations." As long as the United States embraces a floating exchange rate policy, the Treasury Secretary should strike the term "strong dollar" from his lexicon when engaging in discourses about exchange rate policies. The phrase "strong dollar" is meaningless and leads to no end of confusion.

The Dollar's Dominance

So under a floating-rate policy, one in which the dollar's price is on autopilot, what can be said about the dollar? We can say that the dollar is the world's dominant currency, more so with each passing year.

Consider some facts about the U.S. dollar and its role in the world's monetary affairs. Thanks to its stability, liquidity and low transactions costs, the dollar occupies a commanding role. It is the world's dominant international currency, a unique feature that gives the United States an edge in attracting capital inflows to finance current account deficits at a relatively low cost. This prompted Charles de Gaulle, when he was President of France, to characterize the benefits derived from the dollar's dominant position as an "exorbitant privilege."[2]

- Ninety percent of all internationally-traded commodities are invoiced and priced in dollars.
- The invoicing and pricing of manufactured goods in international trade presents a much more complicated picture. The dollar, however, dominates. For example, 37 percent of the United Kingdom's exports to Germany are invoiced in dollars, not Euros or Sterling.
- The dollar is employed on one side of 90 percent of all foreign exchange transactions.
- Over 66 percent of all central bank reserves are denominated in dollars, and that percentage has been steadily increasing since 1990.
- The second most popular hand-to-hand currency used by foreigners is the dollar, with their own domestic currencies in first place. That explains why an estimated 50–70 percent of all dollar notes circulate overseas.
- The dollar is the second most popular denomination used by foreigners for onshore bank accounts, with their domestic unit of account usually in first place. According to the IMF, the average ratio of dollar-denominated bank accounts to broad money in highly dollarized countries is 0.59, and for moderated dollarized countries, the ratio is 0.18. Not surprisingly, the dollar is the king of off-shore bank accounts.
- Fifty percent of the internationally-traded bonds are denominated in U.S. dollars.

[2] I thank Fred Bergsten for reminding me of de Gaulle's astute observation.

- The dollar also dominates the world's equity markets, with 60 percent of the capitalized value of all traded companies in the world denominated in dollars. And that is not all. Capital markets throughout the world are rapidly shifting into dollars. To lower their cost of capital, foreign companies are beating a path to the New York Stock Exchange and Nasdaq, which of course both trade in dollars. Many traditional foreign companies now issue American Depositary Receipts in New York. These ADR's, representing claims on shares in foreign companies, are traded in dollars, and dividends are paid in dollars. For example, 58.7 percent of the total capitalization of all traded Latin American companies is denominated in dollars, and for the two largest Latin economies, Brazil and Mexico, the dollarized percentages are 69.9 percent and 42 percent, respectively.

All this boils down to a simple fact: The world is already highly and unofficially dollarized. And unless the quality of the dollar deteriorates, that is the way things will stay. If more countries with low-quality currencies would officially replace their domestic currencies with the dollar, the competitive devaluations that so many fret about would come to an abrupt halt. And exchange rate crises that frequently engulf countries with half-baked currencies would be a thing of the past. After all, countries that are officially dollarized do not have an exchange rate vis-à-vis the dollar.

The Dollar's Price

The dollar's strength against major currencies since 1995 and particularly since the start of 2000 has persuaded many, particularly the dollar bears, that the dollar's price is too "high" and unsustainable. The dollar's "high" price has also generated predictable howls from those who assert that the "strong dollar" has made their businesses uncompetitive and squeezed their margins.

Just how "high" is the dollar's price? It depends on how you measure it. If we use the Federal Reserve's broad dollar index or IMF's dollar index, it appears that the dollar is at a "high" level and perhaps not sustainable (see Chart 1). However, if we use ABN–AMRO's trade-weighted dollar index, the dollar does not appear to be as "strong" as many believe. The weighting used by ABN–AMRO is more representative of the realities (see Table 2). Indeed, ABN–AMRO's dollar index more accurately reflects the dollar's trade weighted price than do either the IMF's or the Fed's dollar indexes.[3] Perhaps that explains why the dollar bears have been disappointed so often in the past few years: They have been looking at the wrong indexes.

Yet another way to look at the dollar indexes, which are constructed by a few experts, is through the lens of the Austrian School of Economics. As Friedrich von Hayek, a leader of the Austrian School, observed, the most important function of a market is to process widely dispersed bits of information from many market participants to generate an easily understood metric—a price. Not surprisingly, the judgments of many market participants, who are putting real money at risk, are deemed to be more important, as they should be, than artificial constructs produced by a small group of experts. Accordingly, the dollar's price is where buyers and sellers agree it should be. To the extent that the dollar's price is too "high" simply means that the consensus of the many market participants differs from the few who are in the business of constructing artificial indexes.

Under a floating exchange rate regime, the future course of the dollar will be determined by expectations about prospective rates of return in the United States and overseas, as well as the risks involved. Judgments about future returns and risks are, of course, difficult and highly dependent on, as Lord Keynes put it, the state of confidence. In this respect, all we know is that the United States engaged in a new, long war against an elusive enemy which will consume meaningful real resources, eventually becoming a drag on productivity. This suggests that capital flows to the United States (as evidenced by recent data), might not be as forthcoming in the future as they were during the past few years. If that is the case, the floating dollar will weaken in the markets and market forces will automatically cause those "troubling" U.S. current account deficits to shrink.

In closing, under floating rates, the less said in Washington, DC about the level and course of the dollar's price, the better. After all, under floating, the dollar's exchange rate is on autopilot. Alas, this is probably asking for too much. When it

[3] The ABN–AMRO index is based on the Fed 'broad' index weighting system. To avoid creating an unwieldy index and to reduce susceptibility to potential distortions from sharp fluctuations in nominal values in developing economies, the ABN–AMRO index does not explicitly include weights for minor U.S. trading partners. It does, however, include weights for medium-sized trading partners such as the UK, Mexico, China, Hong Kong, and Malaysia.

comes to exchange rates and adjustments in the balance of payments, many of the cognoscenti in Washington have a distaste for automaticity. For them, the consequences of a country's balance of payments should not spread themselves out inconspicuously in time and scope. Instead, they should remain concentrated and visible as a signal for policy changes and as a pivot for expert consultations.

Table 1: Exchange Rate Regimes

Type of Regime	Exchange Rate Policy	Monetary Policy Adjustment	Source of Change in Monetary Base	Conflicts Between Exchange Rate and Monetary Policy	Balance of Payments
Floating Rate	No	Yes	Net Domestic Assets (NDA)	No	Automatic
Fixed Rate	Yes	No	Foreign Reserves (FR)	No	Automatic
Pegged Rate	Yes	Yes	NDA and FR	Yes	Crisis Prone

Table 2: Weightings Used in US Dollar Indices

	ABN AMRO	IMF	Fed Broad
Japan (JPY)	31.6	30.3	13.3
Europe (EUR)	21.0	29.9	16.3
Canada (CAD)	17.2	25.0	17.0
Mexico (MXN)	13.3	0.0	10.4
UK (GBP)	4.6	9.0	4.3
China (CNY)	7.4	0.0	8.0
Hong Kong (HKD)	2.6	0.0	2.6
Malaysia (MYR)	2.3	0.0	2.4
Other	0.0	0.0	25.8
Total	100.0	100.0	100.0

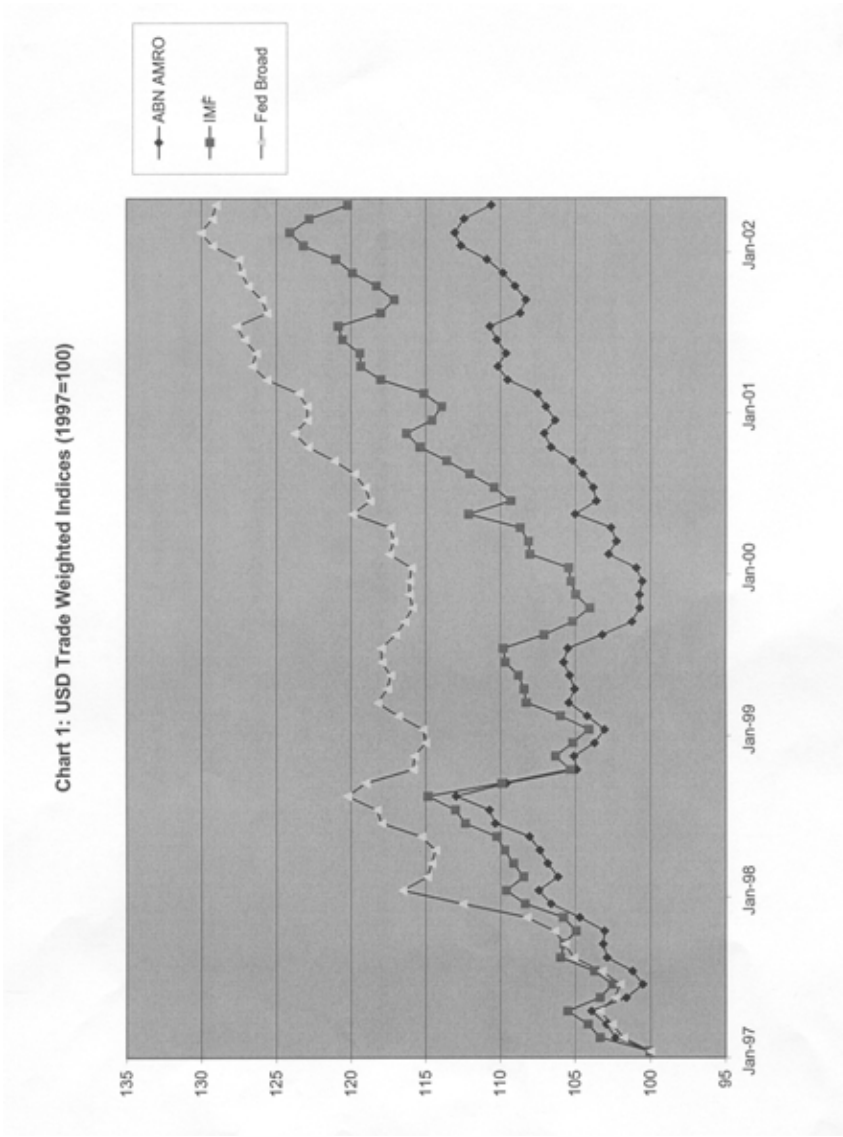


Chart 1: USD Trade Weighted Indices (1997=100)
ABN AMRO
IMF
Fed Broad
135
130
125
120
115
110
105
100
95
Jan-97
Jan-98
Jan-99
Jan-00
Jan-01
Jan-02

RESPONSE TO WRITTEN QUESTION OF SENATOR AKAKA FROM PAUL H. O'NEILL

Q.1. This week the *Associated Press* reported that the Treasury Department would borrow one billion dollars instead of retiring $89 billion of the national debt, which had been projected in January. This was the first time since 1995 that the Government needed to borrow money in the April–June quarter. Three-quarters of the increase in borrowing was due to lower-than-expected tax revenue. In the fourth quarter of last year, foreign investors purchased $33.3 billion in U.S. Treasury Securities. This debt adds to the current account deficit. What are the impacts of the Federal budget deficit and the tax cuts enacted last year on the current account deficit?

A.1. There is no direct connection between the Federal budget and current account deficits. The current account reflects the balance between savings and investment in the economy. This fiscal year's Federal deficit is related to the recent downturn in the U.S. economy and the spending requirements of the war on terrorism. The deficit is not large by international standards. The decline in revenue that naturally occurs during cyclical downturns, and the Administration's tax cuts, were critical in stimulating the timely recovery of the U.S. economy, and ensuring that the recent recession was among the mildest and shortest on record.

RESPONSE TO WRITTEN QUESTIONS OF SENATOR BUNNING FROM RICHARD L. TRUMKA

Q.1. What happens if the Secretary decides to "talk down" the dollar, but foreign investors still look at our economy as the strongest in the world and the best return for their investment? Won't the foreign investors still send their money here, and keep the dollar at a high rate against other currencies?

A.1. That foreigners view the U.S. economy as the strongest in the world is a strength and advantage to us. That said, it is still possible for the dollar to get out of alignment owing to speculative pressures, and there are many empirical measures that show the dollar is overvalued today.

Foreign investor attitudes toward the United States are one reason for the high value of the dollar. But equally important is Treasury's policy toward the dollar. By constantly talking about a "strong dollar," and by failing to speak out against the many countries who intervene to keep their currencies low in order to gain competitive advantage, the Treasury has encouraged speculators to think that they face a "one way bet." That is, the dollar will remain strong and other currencies will remain weak. This policy must end, and ending it is fully consistent with the United States remaining an attractive place for foreign investment.

Q.2. If the Treasury went to an aggressive policy to lower the dollar, it would raise import prices for the consumer. Would we not risk increased inflation under such a scenario?

A.2. There are three reasons to discount the "inflation risk" scenario:

First, a lower dollar will cause import prices to rise slightly because foreign firms pass through part of the exchange rate change. But that need not translate into damaging generalized price infla-

tion. Most U.S. manufacturing firms have massive excess capacity and stand ready to step into the breach and fill the gap left by importing firms. As a result of this substitution, the net impact on inflation and consumers stands to be quite moderate. Moreover, any increase in import prices will be a one-off increase, and therefore will not generate continuing inflation.

Second, the current environment is one of very low inflation, bordering on deflation. At these levels, even if a small increase in inflation were to materialize it might actually be a good thing by pushing the economy away from a deflation—which is economically disastrous in an environment where business and firms are heavily indebted.

Finally, an important consideration is that the real issue is "dollar adjustment now" versus "dollar adjustment later." It is widely agreed that the dollar and the trade deficit are unsustainable at current levels. Doing nothing risks a damaging and painful adjustment down the road, and in the meantime the overvalued dollar will have hollowed out our manufacturing sector, destroyed good manufacturing jobs, and undermined our economic recovery. A better strategy is to manage the adjustment, avoid the damaging economic effects of delay, and avoid a possible financial crash that might occur when markets ultimately decide to correct.

RESPONSE TO WRITTEN QUESTIONS OF SENATOR BUNNING FROM JERRY J. JASINOWSKI

Q.1. What happens if the Secretary decides to "talk down" the dollar, but foreign investors still look at our economy as the strongest in the world and the best return for their investment? Won't the foreign investors still send their money here, and keep the dollar at a high rate against other currencies?

A.1. The fundamental force which drives investment flows is access to developed and thriving markets. And with the expectation that productivity growth (the main driver behind a sustainable growth and increased living standards) will continue to be robust in coming years, there is no doubt that the United States will continue to be an attractive market for worldwide investment. While this outlook does not support a weak dollar, it also does not support a dollar 30 percent above its level in 1997—a level reach in February 2002. The record actually shows that investment inflows do not react to changes in the dollar—but rather to changes in the outlook for the economy.

Capital will continue to flow into the United States as the dollar returns to normal, and, in fact, direct investment inflows may actually increase. That is what happened after the 1985 correction of the dollar. During 1985–1987 the dollar fell 40 percent—returning to normal levels prevailing prior to 1985. During the time the dollar was appreciating—up until mid-1985—foreign direct investment into the United States averaged $4.5 billion per quarter. But after the dollar started to fall, direct investment inflows nearly tripled, to $12.3 billion per quarter. Why? Because the dollar's return to normalcy made the United States a better place to invest.

Q.2. If the Treasury went to an aggressive policy to lower the dollar, it would raise import prices for the consumer. Would we not risk increased inflation under such a scenario?

A.2. Certainly a declining dollar will put some upward pressure on prices, for we have been having a free ride for several years while the dollar became increasingly overvalued. The adjustment, however, will be mild. According to NAM estimates based on the widely-used Washington University Macro Model, a 15 percent dollar devaluation over the next year and a half would only result in a one-time increase in the GDP deflator (the widest measure of prices in the U.S. economy) of less than 1 percent.

This is because inflation has been held down principally by the high productivity growth of U.S. industry—especially manufacturing. Declining import prices for consumer goods have actually not had that much of an inflation-restraining impact. Bureau of Labor Statistics data show that despite the 30 percent rise in the dollar since 1997, consumer goods import prices have fallen only 6 percent. Part of the explanation for this is in the fact that a significant proportion of consumer goods imports come from China, whose currency has remained pegged to the dollar. Additionally, a significant part of the consumer price index is related to energy imports, and these are denominated in dollars—thus being impervious to fluctuations in the value of the dollar.

Import prices for capital goods, however, have fallen 25 percent, which has put U.S. capital goods industries at an enormous disadvantage. As the prices of these imports rise, we would anticipate a shift back to U.S. production and a reduced rate of import growth. Inflation will also be restrained by the huge capacity overhang in the U.S. economy. Federal Reserve Board data shows capacity utilization to be extremely low—less than 75 percent. This makes it very difficult to raise prices, showing that this is actually a good time for the dollar to decline to more normal levels. The worst time for the dollar to decline would be during a period of overheated boom.

A mild inflationary response to a dollar devaluation is supported not only by econometric modeling, but also by history. After a sharp appreciation in the early 1980's, the dollar fell by 40 percent in 2 years starting in mid-1985. While a strengthening dollar played a role in bringing down inflation, which was running near double digits in the early 1980's to a more moderate 3.1 percent by 1985, no significant pickup in inflation accompanied the 1985–1987 correction. In fact, between 1986 and 1988, the inflation rate actually averaged 0.3 percentage points lower than the inflation rate at the height of the dollar's peak in 1985.

Thus, while a weak or devaluing dollar falling to abnormally low levels may cause inflation, the evidence indicates that a dollar declining to normal levels has little inflationary impact.

RESPONSE TO WRITTEN QUESTIONS OF SENATOR BUNNING FROM BOB STALLMAN

Q.1. What happens if the Secretary decides to "talk down" the dollar, but foreign investors still look at our economy as the strongest in the world and the best return for their investment? Won't the

foreign investors still send their money here and keep the dollar at a high rate against other currencies?

A.1. The American Farm Bureau Federation (AFBF) does not favor the Secretary either "talking up" or "talking down" the value of the dollar. We also recognize the importance of maintaining a vibrant economy, one that attracts ample foreign investment. It is equally important to ensure that all sectors of the U.S. economy have the opportunity to thrive in a manner that is not impaired by an overvalued dollar.

The strong dollar is severely affecting sectors, like agriculture, that are highly dependent on exports. For this reason, we support a Congressionally mandated study of the impact of the value of the dollar on the U.S. economy. Such a study should take into account the ability of the United States to attract foreign investment and not only maintain, but also increase, exports.

Q.2. If the Treasury went to an aggressive policy to lower the dollar, it would raise import prices for the consumer. Would we not risk increased inflation under such a scenario?

A.2. AFBF does not support pursuing an aggressive policy to lower the dollar. Such a policy is not likely to be effective in today's technology-based global economy wherein massive intervention would be required, but would not have long lasting effects. We remain concerned, however, with the actions taken by some U.S. trading partners to intervene repeatedly in international exchange markets in a concerted attempt to devalue their currencies vis-à-vis the dollar and believe that the United States should respond to these currency manipulation attempts by other countries.

AFBF believes that the value of the dollar should be set by the market without interference by either our Government or a foreign government trying to manage the dollars value it to achieve a certain economic outcome.

Thank you very much for the opportunity to clarify our position on this issue.

RESPONSE TO WRITTEN QUESTIONS OF SENATOR BUNNING FROM ERNEST H. PREEG

Q.1. What happens if the Secretary decides to "talk down" the dollar, but foreign investors still look at our economy as the strongest in the world and the best return for their investment? Won't the foreign investors still send their money here, and keep the dollar at a high rate against other currencies?

A.1. The phrase "talk down" is ambiguous. If it implies follow-up actions, such as large and persistent United States official financial market intervention to bring the dollar rate down below a market-based rate (as do Japan and China, for example), such a statement would make foreign investors hesitate in anticipation of such a "manipulated" lower dollar. I oppose such a talk down/intervention strategy, and I do not believe Secretary O'Neill has any intention of doing so. If, in contrast, "talk down" simply means a personal assessment by the Secretary that market forces are likely to lead to a lower dollar, related to the unsustainability of the record trade deficit, investors would likely maintain their existing assessment

as to whether the U.S. economy offered the best rate of return on their investments.

Q.2. If the Treasury went to an aggressive policy to lower the dollar, it would raise import prices for the consumer. Would we not risk increased inflation under such a scenario?

A.2. If the dollar declined for any reason, import prices would rise for the consumer, and there would be some corresponding rise in the overall rate of inflation. In the context of a 10–20 percent decline in the dollar, however, it would be a relatively small, one-time upward blip in the inflation trend.

RESPONSE TO WRITTEN QUESTIONS OF SENATOR BUNNING FROM STEVE H. HANKE

Q.1. What happens if the Secretary decides to "talk down" the dollar, but foreign investors still look at our economy as the strongest in the world and the best return for their investment? Won't the foreign investors still send their money here, and keep the dollar at a high rate against other currencies?

A.1. If the Secretary decides to "talk down" the dollar, which I believe would be imprudent, net financial flows that favor the United States would be disrupted temporarily and the dollar would probably weaken temporarily. But if rates of return on capital, adjusted for risk, are anticipated to be superior in the United States, net financial flows will continue to favor the United States. Given that the United States has a floating exchange rate regime, the value of the dollar is determined in the market. It is on autopilot. Accordingly, under the scenario sketched above, the current account deficit as a percent of GDP will continue to increase and so will the dollar's nominal exchange rate. This should not be cause for alarm. It would simply be a reflection of the superior underlying economic fundamentals in the United States vis-à-vis those in the rest of the world.

Q.2. If the Treasury went to an aggressive policy to lower the dollar, it would raise import prices for the consumer. Would we not risk increased inflation under such a scenario?

A.2. On the assumption that the U.S. Treasury possesses the policy levers to aggressively lower the value of the dollar—a highly questionable assumption—and that these bear fruit, the dollar would weaken and import prices would rise for the consumer. And, yes, inflation would be higher than would otherwise be the case. This set of events would tend to motivate the Federal Reserve to attempt to fight inflation with higher short-term interest rates. This would bring forth howls of protest from those who advocate an aggressive Treasury policy to lower the value of the dollar because many of the "weak dollar" advocates also tend to embrace "low" interest rate policies.

PREPARED STATEMENT OF THE AMERICAN FOREST & PAPER ASSOCIATION

MAY 1, 2002

The American Forest & Paper Association (AF&PA) appreciates the opportunity to comment on how U.S. exchange rate policies are negatively impacting the forest products industry. The wood and paper products business is highly sensitive to exchange rate fluctuations. The Committee's long-term engagement on this issue has been helpful in focusing attention on trade and exchange rate linkages and their effect on the global competitiveness of the U.S. economy. Our statement today will recommend additional measures which, we believe are necessary to correct unsustainable trade and exchange rate imbalances—and restore the ability of American manufacturing to fuel U.S. economic growth.

AF&PA is the national trade association representing the forestry, pulp, paper, paperboard and wood products industry in the United States. This industry accounts for approximately 7 percent of total U.S. manufacturing output and employs approximately 1.5 million people in 42 States, with an annual estimated payroll of $64 billion. Industry sales exceed $250 billion annually in the United States and export markets. AF&PA's membership encompasses the full spectrum of U.S. businesses ranging from small family owned manufacturing and tree farm businesses to large integrated companies.

Many of the leading economists, including several represented at today's hearing, believe the U.S. dollar is currently overvalued relative to a basket of major currencies—and that the extent of the imbalance is somewhere around 25–30 percent. We agree that it is substantial.

At these levels, U.S. industry is, in effect, paying a 30 percent "overvalued dollar tax" on all shipments—whether they are going to foreign or domestic customers. Few U.S.-based producers can compete for long under those circumstances. Just a few of the devastating effects of this "tax" are described in the following examples:

- Our companies have had to exit export markets they have served for decades. For example, United States kraft linerboard exports to Europe have plunged by 48 percent in the 1997–2001 period, to $207.6 million. At the same time, U.S. hardwood exporters have lost key European markets based solely on the price differential caused by the value of the dollar. The U.S. product is of a higher quality and its delivery is more reliable than other competitors who are now taking market share based on price alone. And, new Eastern European production facilities are now being constructed to ensure that U.S. manufacturers do not retake that market share when the Euro-dollar exchange rate returns to balance.
- Simultaneously, competitors have been taking advantage of their relatively cheap currencies to capture an ever-widening share of the U.S. domestic market. Over the period 1997–2001, United States imports of European coated printing paper soared by 50 percent, to $730.6 million. In the 1997–2000 period, imports took more than 90 percent of the growth in the U.S. paper market. (Exhibit 1)
- Similarly, the wood products sector has also been battered by cheap imports, which has resulted in a ripple effect across manufacturing interests. The domestic furniture industry, one of the largest traditional users of hardwood lumber and veneer, has been contracting rapidly as a result of substantial lower priced furniture imports. (Exhibit 2)
- As a result, the U.S. net imports of paper and of wood products have more than doubled from a negative $6 billion in 1997 to a negative $13.6 billion last year. (Exhibit 3)

During this period, none of the factors which shape the underlying competitiveness of the U.S. forest products industry have changed—except the value of the dollar. On the contrary, our companies have scrapped uneconomic capacity and upgraded technology to significantly improve competitive performance. Nevertheless, a report by Salomon-Smith-Barney states that the exchange rate is robbing U.S. paper companies of their long-held competitive advantage vis-à-vis European producers. (Exhibit 4) The report further states that companies will not return to profitability unless and until exchange rates are adjusted to more appropriate levels.

The combined effect of weakening export markets and surging imports has put unprecedented downward pressure on paper and wood product prices. Faced with this kind of challenge, the only option available to many of our companies is to close mills. Since 1997, American paper companies have had to close 72 mills or an average of 14 mills per year—compared to an average of less than four in the early 1990's. (Exhibit 5) Employment at paper industry mills has declined by 32,000 jobs since 1997. (Exhibit 6) In the last year alone, more than 20 wood processing facili-

ties with a capacity of 1.7 billion board feet were shutdown permanently. In the last 3 years, the wood sector has lost 51,000 jobs. (Exhibit 7) These were high paying jobs in rural communities where wood and paper manufacturing mills serve as the backbone of small-town economies.

Data prepared by the National Association of Manufacturers (NAM) shows an estimated 500,000 jobs lost since mid-2000 as a result of the drop in manufactured goods exports. This job loss was principally due to the overvalued dollar and makes clear that this pattern is not unique to the forest products industry but is repeated in sectors as diverse as automobiles, aerospace, steel, textiles, and machine tools to name a few.

Looking ahead, there are no signs of future improvement. U.S. producers of wood and paper products are closing capacity here in the United States while foreign competitors—especially in Europe and East Asia—are rapidly building more, often with their government's financial support.

The real long-term danger is a hollowing out of American industry as a result of the persistence of an overvalued dollar. This is what adds a compelling urgency to our call for action today.

The American Forest & Paper Association supports policies that encourage exchange rates to be set by market fundamentals. But, when other countries are purposely taking action to keep their currencies artificially low, the United States must step in to ensure that the dollar is not overvalued as a result of these non-market actions by foreign governments. We believe U.S. exchange rate policy must address two major sources of dysfunction in currency markets:

- A widespread perception in exchange rate markets that there is no upper boundary to United States support for the dollar.
- Manipulation of currencies by U.S. trading partners for competitive advantage.

In currency markets, rhetoric matters. The statements by U.S. Treasury officials indicating a totally hands off attitude toward the value of the dollar have resulted in a widespread belief that there is no point at which the U.S. Government will consider taking any action to stop the rise. Signals from the U.S. Treasury that it supports a sound dollar consistent with the competitive fundamentals of the U.S. economy would go a long way toward erasing the current expectation that the dollar will continue to rise in value.

Currency Manipulation

Ambassador Ernest Preeg has provided solid empirical evidence of currency manipulation by U.S. trading partners—and its effect on the U.S. economy. In a recent 12 month period, East Asian economies had a cumulative current account surplus of $218 billion, while their central banks together added an aggregate $165 billion in foreign exchange reserves. Japan alone has accumulated $95 billion in foreign reserves. This means that about three-quarters of the net foreign exchange inflow resulting from Asian current account surpluses was taken off the market through central bank purchases, with the result of lower exchange rates and larger trade surpluses than otherwise would have been the case. The dollar share of the aggregate foreign reserve accumulation was estimated at 80 to 90 percent.

Japanese officials also have been actively talking down the yen. In recent months, China has become more outspoken in calling attention to the effect Japanese policies could have on the global economy, by triggering a race to the bottom among key Asian countries that compete with Japan for export markets.

Provisions in the Trade Act of 1988 requiring surveillance of exchange rate policies by U.S. trading partners have undoubtedly had a positive effect in addressing more egregious practices. However, the data cited above make it clear that further action is needed. The Senate version of Trade Promotion Authority recognizes that significant or unanticipated changes in exchange rates can negate U.S. market access gains in trade agreements. The legislation provides for the establishment of consultative mechanisms among parties to trade agreements to protect against currency manipulation by foreign governments. We believe this step is necessary to ensure that, in future trade agreements, the balance of benefits USTR negotiates—and the U.S. Congress approves—cannot be upset by subsequent exchange rate manipulation. We strongly support this provision of the bill.

G–8 Collaboration

Concerted action by major economies worked in 1985 with the Plaza Accord and we believe it can work again today. The G–8 meeting in Canada next month offers an opportunity for action to address the twin imbalances—the overvalued U.S. dollar and the U.S. trade deficit—which are widely recognized as posing a major threat to global economic stability. Indeed, the just released IMF *World Economic Outlook*

concluded that the overvaluation of the U.S. dollar and the large U.S. current account deficit pose significant risk to the sustainability and durability of the incipient economic upturn, both in the United States and globally. There are also mounting indications that some of our trading partners share this concern about trade and currency imbalances, and might be prepared to work with us to ensure a "soft landing" which minimizes the real economic pain associated with an unmanaged or "hard landing" adjustment.

Such a concerted approach, combined with enhanced Trade Promotion Authority provisions, would improve the prospects for long-term market-sustainable exchange market rate equilibrium.

Agreement on a joint plan of action would represent a substantial, positive G–8 outcome. Alternatively, failure to deal with the issue at the G–8, in the face of the clear warning signals, risks exposing the still fragile United States and the global economic recovery to an unpredictable and potentially unmanageable market adjustment.

The Time for Action is Now

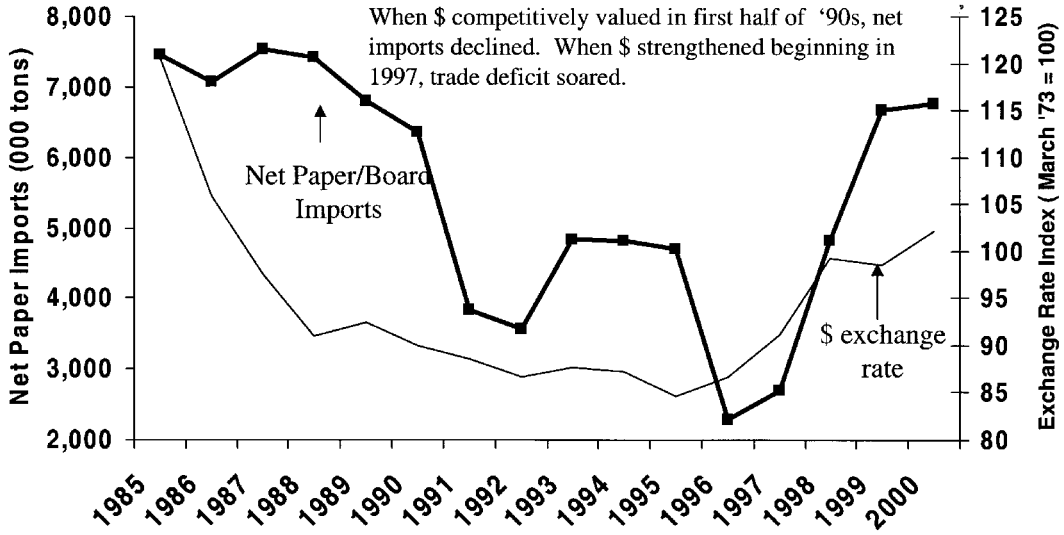
There is a striking similarity between the situation in 1985 and today in terms of the impact of the overvalued dollar on the U.S. economy and the forest products industry's trade balance. But there is also an important difference: Today, the U.S. economy is more dependent on trade than ever before. An indication of this is that U.S. trade exposure (i.e., total imports and exports) was 17 percent of GDP in 1985, while today it accounts for 24 percent. The forest products industry reflects this trend as well. In 1985, the trade exposure for paper was 23 percent, but reached 33 percent in 2001. (Exhibit 8)

Notwithstanding the challenges of the past year, the American economy is sound. There are increasing signs that the economy is coming out of recession. The incipient recovery will not thrive without a robust and sustainable rebound in U.S. manufacturing. For the U.S. forest products and other manufacturing industries, this will require exchange rate policies which ensure that the value of the dollar is consistent with the underlying economic fundamentals. It will also call for action to prevent future currency misalignment, which rob our companies of the competitiveness they and their workers have built.

We appreciate the opportunity to present these views and look forward to working with the Committee and the Administration in reaching solutions that will ensure a strong and vibrant U.S. forest products industry.

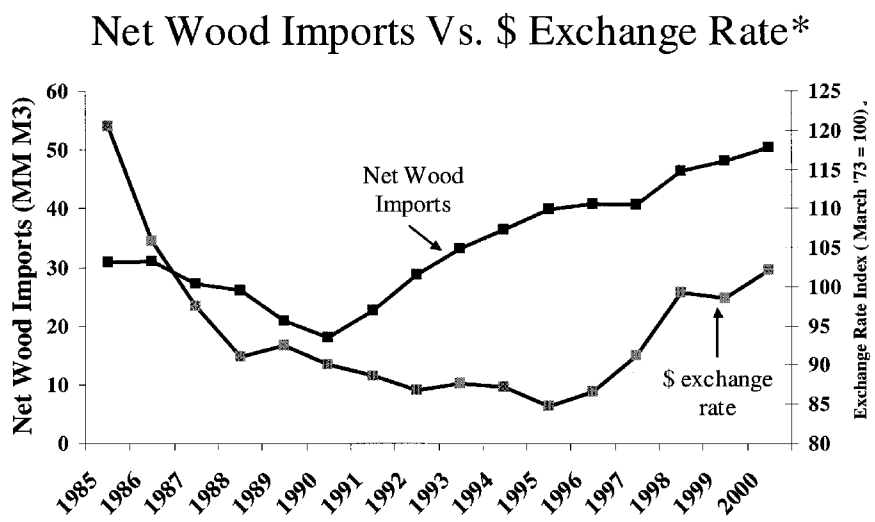
Exhibit 1

NET U.S. PAPER AND PAPERBOARD IMPORTS VS. $ EXCHANGE RATE



Sources: Bureau of the Census/Federal Reserve Board/AF&PA Economics Dept.

Exhibit 2



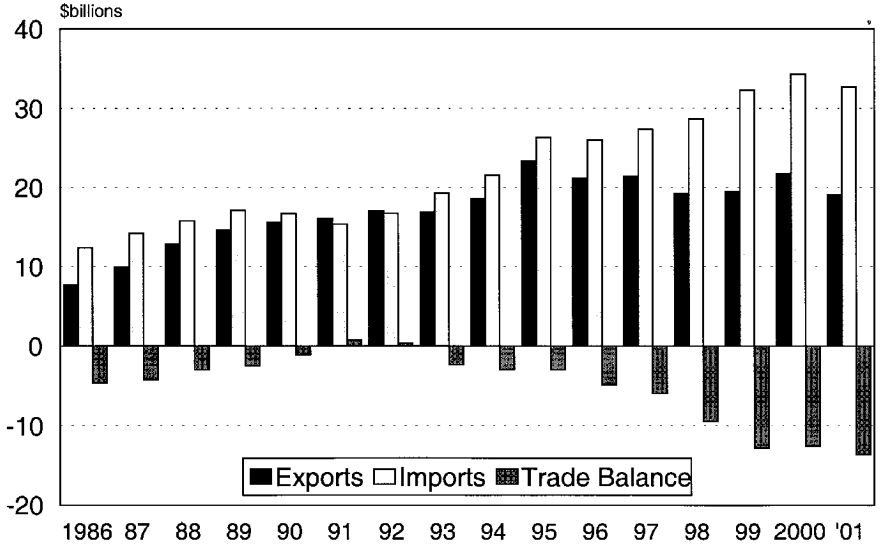
* Inflation-adjusted exchange index of $ relative to37 currencies;
Wood imports of major value-added products

Sources: Bureau of the Census/Federal Reserve Board/AF&PA

Exhibit 3

U.S. INTERNATIONAL TRADE IN PULP, PAPER, PAPERBOARD AND WOOD PRODUCTS

1986-2001



Source: U.S. Bureau of the Census

SALOMON SMITH BARNEY

EQUITY
RESEARCH:
UNITED STATES

Paper & Forest Products

June 28, 2001

C.A. Dillon, III, CFA
212-816-2793
c.a.dillon@ssmb.com

Luisa Lau
212-816-3437
luisa.lau@ssmb.com

Richard J. Holohan
212-816-3046
richard.j.holohan@ssmb.com

Timothy W. Thein
212-816-6706

Global Paper & Forest Products Team

Asia-Pacific
Peter Cain

Europe
Thomas Brodin

Japan
Paul Blamire

Latin America
Jennifer Corrou

New Zealand
Stephen Hudson

North America
C.A. Dillon, III
Luisa Lau
Richard J. Holohan

The Strong U.S. Dollar: Issue No. 1 for This Paper Cycle

A Weaker Greenback Equals Stronger Profits

- **From 1996 to 1998, the currencies of the major European paper-producing countries fell 15%–20% versus the U.S. dollar, virtually eliminating the U.S. producers' long-held cost advantage.**
- **Since the inception of the euro in January 1999, these currencies lost another 25%–30% of their value vis-à-vis the dollar. As a result, the European paper industry now has much lower average production costs than the U.S. industry.**
- **Unless the dollar weakens substantially (25% or more) versus the euro, we believe U.S. paper companies will not even come close to producing the operating margins seen in the 1988–89 and 1995 peaks.**
- **Despite the dollar's strength and weak pulp and paper pricing, U.S. paper stocks had performed well since October 2000, prompting us to downgrade several U.S. paper stocks on May 24.**
- **Within the U.S. forest products industry, we continue to favor the more wood-oriented names, such as Buy-rated Weyerhaeuser and Louisiana-Pacific.**

North America

A member of citigroup

Executive Summary

When we declared a more cautious stance on the paper-intensive stocks within our universe in late May, we pointed to the strong relative stock market performance as well as the high-flying value of the dollar versus the euro as the major reasons for the downgrade. While the former was easily quantified in the more than 50% relative outperformance since mid-October, we believe Wall Street has not fully grasped the ramifications of a resilient greenback on the profitability of the U.S. paper and forest products industry. Unless we see a substantial decline in the value of the dollar versus the euro, we believe the U.S. paper industry's expected 2003 peak profits will fall well short of the levels seen at prior peaks. Our goal is to illustrate how a weakening in the value of the almighty U.S. dollar is paramount to higher U.S. pulp/paper profits.

We recently changed our stance on the paper-intensive stocks.
On May 24, Salomon Smith Barney's global pulp and paper research team lowered its 2001 and 2002 pulp price forecast, owing largely to the strong dollar vis-à-vis the euro. In addition, we lowered the investment ratings on several companies in our U.S. coverage universe with heavy paper exposure due to the stocks' strong relative performance, but also due to concerns surrounding the continued high value of the dollar versus the euro.

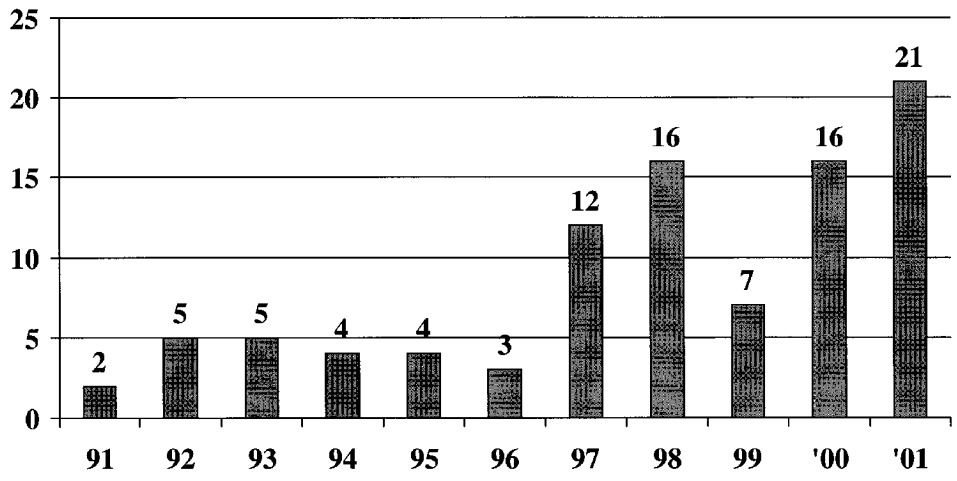
The Europeans have seen profitability surpass the U.S. companies' profitability.
While the European paper industry has widened its lead in operating margin performance versus the United States, it has also moved ahead on the basis of return on equity. The U.S. industry generated higher ROEs during the previous three cyclical peaks. However, with the dollar having strengthened dramatically versus most European currencies since the mid-1990s, European ROEs are expected to exceed the U.S. paper industry average in 2001 and 2002. In 2003, the next expected peak year, SSB's global paper and forest products research team expects European paper and forest products ROEs to exceed ROEs in the U.S. industry even though the U.S. industry is generally "more cyclical" due to its heavier exposure to pulp and containerboard (which traditionally have been among the more volatile grades).

We see substantial upside potential if the dollar were to weaken significantly versus the euro.
We believe the No. 1 issue facing the U.S. paper and forest products industry is the strong dollar, which, for U.S. manufacturers, is limiting pricing power and raising relative costs. However, a key question is: What would happen if the U.S. dollar experienced a substantial (i.e., 25% or more) drop vis-à-vis the euro? The short answer is that U.S. producer profitability would shoot up sharply as dollar price increases would be easier to attain even as the European producer costs increase in dollar terms.

Exhibit 5

U.S. Paper Mill Shutdowns by Year

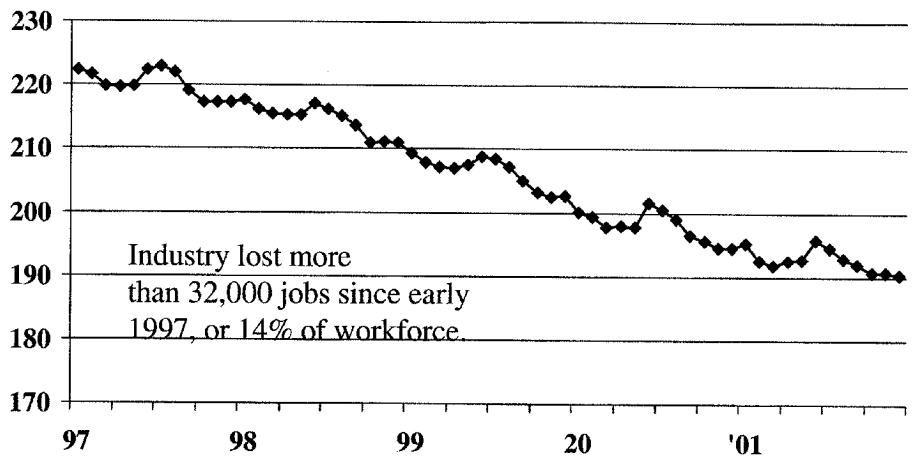
1991-2001



Source: American Forest & Paper Association

Exhibit 6

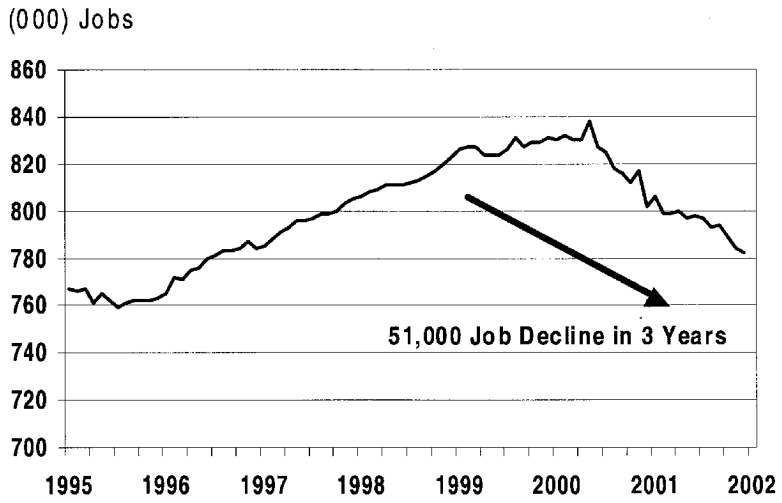
Employment At Pulp, Paper and Paperboard Mills



Source: Bureau of Labor Statistics

Exhibit 7

Lumber & Wood Industry Employment

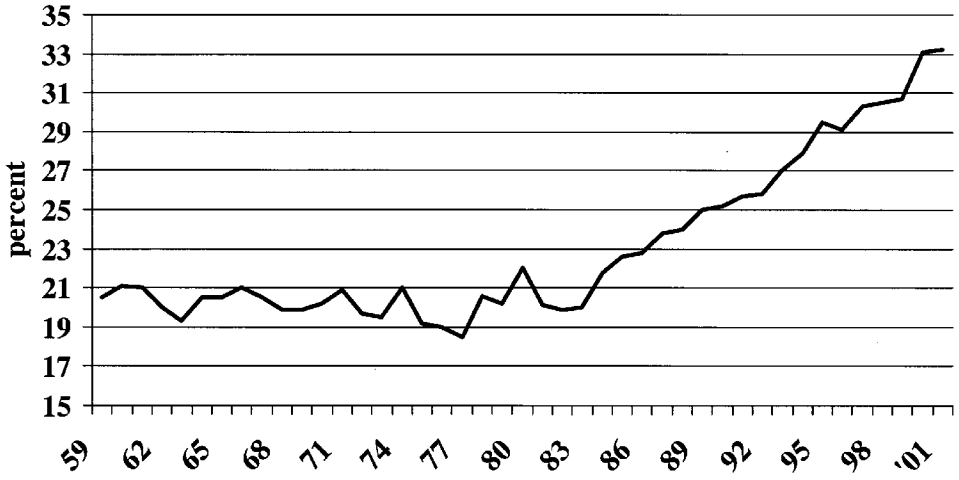


Source: Bureau of Labor Statistics

Exhibit 8

Trade Exposure:

Paper Imports Plus Exports As % of Production



PREPARED STATEMENT OF THE AMERICAN TEXTILE MANUFACTURERS INSTITUTE (ATMI)

MAY 1, 2002

The American Textile Manufacturers Institute (ATMI) submits this statement to the Senate Committee on Banking in regards to the May 1 hearing on the release of the Treasury Department's Foreign Exchange Report. ATMI is the national trade association of the U.S. textile industry, one of the largest manufacturing sectors in the United States.

ATMI is writing to describe the devastating impact that the overvalued dollar, now at a 16 year high, is having on the U.S. textile sector and to urge the Committee and the Administration to take immediate steps to bring the dollar back down to normal, historic levels.

The U.S. textile industry is suffering its worst economic crisis since the Great Depression. Since the dollar began to surge in value in 1997, over 175,000 textile workers have lost their jobs and over 215 textile plants in the United States have closed.

The Asian currency devaluation in 1997–1998 and the "strong U.S. dollar" policy instituted at that time are the root cause for this devastation. As of last year, the dollar had increased in value by an average of 40 percent against the leading Asian textile exporting countries. Prior to the dollar's surge, the U.S. textile industry was enjoying some of its best years in history and recording new highs for shipments, profits, and exports.

Since that time, the strength of the dollar has allowed Asian exporters to cut their prices by an average of 23 percent and caused Asian textile and apparel exports to the United States to increase by an astonishing 6 billion square meters, an increase of 65 percent.

As a result, U.S. textile profits have virtually disappeared, shipments have declined by 25 percent or $12 billion, exports have fallen by $2 billion and a swath of misery has spread across the Southeast.[1]

This impact has hit not only domestic textile manufacturers but U.S. cotton and wool growers, textile machinery suppliers and man-made fiber manufacturers. It has also devastated small towns across the Southeast that have depended for generations on domestic textile manufacturing.

In addition, the problem of the overvalued dollar impacts virtually every manufacturing and agriculture sector in the United States. The National Association of Manufacturers estimates that half a million manufacturing jobs have been lost in the last 18 months just from lost export orders. That figure does not include hundreds of thousands of jobs lost because of a surge in artificially low-priced imports.

We also note that the International Monetary Fund (IMF), the Organization for Economic Development (OECD), the European and Canadian Central Banks and even members of the Federal Reserve in the United States have all expressed alarm over the continuing rise in the dollar's value.

In February, despite stagnant economic activity, rising imports and a dramatic jump in the current accounts deficit, the Federal Reserve reported that the dollar had hit a new high, with a 31 percent increase in value against the world's major currencies since 1997.

It is clear that economic fundamentals are being overridden by a belief in the market that the U.S. Treasury will act to support a "strong dollar." This policy is now having a devastating impact on the textile sector.

The last time the dollar surged to such heights was in the mid-1980's during the Reagan Administration. At that time, Treasury Secretary Jim Baker took strong action, in concert with other major trading nations, to restore the dollar to sound, stable levels. That action set the stage for a decade of dollar stability and U.S. export growth.

ATMI firmly believes that for the textile crisis to end and for the industry to return to health, the U.S. Government *must act* to return the dollar to its normal, historic range. We strongly urge the Committee and the Administration to act quickly to accomplish this.

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[1] We have attached a one-pager on the impact of the dollar on textiles for your review.

"Strong Dollar" Policy Devastates U.S. Textiles

- Props Up and Supports Competitive Asian Currency Devaluations -

The textile industry, one of the largest manufacturing sectors in the United States, employing almost half a million workers, has been devastated by the rise in the value of the dollar.

Last year, 116 textile mills were closed and 67,000 workers – 13% of the sector's entire workforce – lost their jobs. Since the dollar began its rise in 1997, 177,000 textile jobs have been lost and 215 textile mills have been closed in the United States.

Price pressures that began with competitive Asian currency devaluations in 1997 and a strong dollar policy since that time have caused a 4-year cycle of deflation in U.S. textile prices.

As a result, since 1997, near-record industry profits have turned to losses and losses have turned to mill closures, job layoffs and textile bankruptcies. The dollar's relentless rise has been a key factor in plunging the industry into its worst economic crisis since the Great Depression.

A number of the country's largest and most modern textile firms have gone bankrupt – including, during the last six months, Burlington Industries, Guilford Mills, Malden Mills, CMI Industries and Galey & Lord.

Day and Night for the Industry: 1997 vs 2001

Prior to the dollar's rise, the industry was healthy and growing. In 1997, industry fiber consumption was a record 17 billion lbs, industry shipments were a record $84 billion, capital expenditures were a near record $2.7 billion, textile exports (including cut pieces) were almost $17 billion, a new record.

Since that time, the dollar's relentless rise, particularly against the currencies of major Asian exporters, has shattered the competitive structure of the industry, causing a huge import surge while collapsing major export markets.

Over the past five years, the dollar has appreciated in value by an average 40% against the top ten Asian textile-exporting countries[1]. The dollar has also risen strongly against the euro and the Canadian dollar.

As imports have surged (see box), major textile export markets have collapsed. Since 1997, U.S. textile exports to Asia have fallen 26% while exports to the EU are down 27%. Textile exports to the industry's two largest markets, Canada and Mexico, fell 8% and 13% last year.

[1]Includes an appreciation of the dollar of 41% against the Korean won, 47% against the Pakistani rupee and 76% against the Indonesian rupiah. China, has *de facto* devalued by sharply boosting its "export tax rebates" to all time highs.

Dollar's Rise is Key Cause of New Destructive Cycle in Textiles

1. As Asian Currencies Fall, Asian Prices Drop

	Change in Prices During:	
	Stable Dollar (91-96)	Overvalued Dollar (97-01)
Asian yarn	8%	-27%
Asian woven fabric	38%	-14%
Asian knit fabric	4%	-33%
Asian apparel	3%	-17%

2. Asian Price Drops Cause Asian Import Surge (millions of units)

	Change in Imports During:	
	Stable Dollar (91-96)	Overvalued Dollar (97-01)
Yarn (kg)	9	45
Woven fabric (sme)	-54	150
Knit fabric (sme)	58	67
Apparel (doz)	64	220

3. With Prices Way Down and Imports Surging, U.S. Textiles Are Devastated

	Change During:	
	Stable Dollar (91-96)	Overvalued Dollar (97-01)
U.S. plant closings	n/a	215
U.S. textile shipments	$7 billion	-$13 bil
U.S. textile exports	$6 bil	-$2 bil*
U.S. textile job losses	-36,000	-177,000

*Sources: Import price and volume data – USITC; plant closings – ATMI; textile shipments and job losses – Census; textile exports – Dept. of Commerce. *decline in 2001.*

For more information on the impact of the overvalued dollar on U.S. textiles, click on "the topic is trade" link at www.atmi.org

For information on the impact on U.S. manufacturing, go to www.nam.org and click on "international trade issues"

PREPARED STATEMENT OF THE COALITION FOR A SOUND DOLLAR

MAY 1, 2002

Mr. Chairman, we the undersigned organizations comprising the Coalition for a Sound Dollar appreciate the opportunity to submit a statement for the record for the Committee's May 1, 2002 hearing on the release of the Treasury Department's Foreign Exchange Report.

The Coalition represents a broad array of manufacturing and agricultural interests which employ millions of U.S. workers and which have been deeply impacted by the overvaluation of the U.S. dollar over the past 5 years. *As of this date, job losses from the overvalued dollar are almost certainly in excess of three-quarters of a million U.S. workers.*

Indeed, the damage caused by the dollar's prolonged surge has become so great that U.S. manufacturing and agriculture, two fundamental legs of the U.S. economy, are unlikely to rebound as a result of the economic recovery. Recent statistics show that despite a surge in first quarter GDP, durable goods orders and business investment remain down and that the bump up caused by inventory restocking was a one time event. In addition, despite increased economic growth overseas, both manufacturing and agricultural exports have continued to decline.

The Coalition members believe that a sound dollar is a fundamental prerequisite for maintaining a healthy United States and global economy. A sound dollar is one whose value relative to other major currencies is determined by market forces that reflect fundamental economic trends, such as trade balances, interest rates, GDP growth, and other objective indicators of a country's performance.

The disturbing reality is that for several years the dollar has *not* been reflecting economic fundamentals. In 1997, after 8 years of stability, the dollar began to appreciate sharply against other major currencies. The appreciation has continued despite a U.S. economic downturn, a yawning current accounts deficit and, in many cases, higher comparable GDP growth overseas. Today, the dollar stands 30 percent higher than in 1997—its highest level in 16 years. The dollar is now approaching the calamitous levels last seen in 1985, which provoked intervention on an international scale.

As a result of the 30 percent dollar "tax," many U.S. made goods have been literally priced out of markets at home and abroad. For example, U.S. manufacturing exports have dropped by an annual rate of more than $140 billion over the past 18 months. *The National Association of Manufacturers estimates that half a million manufacturing jobs have disappeared simply as a result of the export decline,* principally due to the fact that the dollar has taxed U.S. exporters, rightly proclaimed by the U.S. Government as the most productive in the world, out of market after market.

Indeed, the conventional wisdom that the U.S. advantage in high-technology products is a key to future U.S. economic growth has been gutted by the dollar's impact. U.S. Government statistics show that over the past 5 years, a healthy U.S. surplus in these products has vanished into a deficit of $20 billion.

Winners of the President's vaunted "E-awards" given to top U.S. exporters have not been spared either. In letters sent to Secretary O'Neill, these E-award winners, among many other top exporters, said:

- "The value of the U.S. dollar now makes us uncompetitive in almost all world markets . . . The 30 percent change in currency value is making us uncompetitive even in our own home market. We are a small business with our only manufacturing facility in South Dakota. We have been forced to make substantial layoffs of production and support personnel to adjust to this catastrophic problem."
- "The strength of the dollar has had a profound effect upon our business, especially in the area of employment. A year ago at this time we employed 1,625 people in the Green Bay area. Today that number is down by over 500 people . . . As this environment of a strong dollar has continued, we have been forced to consider relocating our manufacturing capabilities offshore."

U.S. agriculture, which suffers from the same "Made in the U.S.A." dollar tax, estimates that nearly 100,000 agricultural workers have been displaced because of the overvalued dollar. From cotton to rice to wheat, the U.S. breadbasket is seeing its major export markets dwindle and imports increase because of the dollar's sustained rise.

The damage extends to industries where there have been significant import surges with the overvalued dollar acting as an enormous import subsidy. *Sectors such as textiles, paper and forest products, automobiles, nonferrous castings, steel and furniture have, in total, lost hundreds of thousands of workers as imports have ridden the currency wave by cutting prices or increasing incentives.* Many of these

jobs have been lost in rural communities that often depend on local manufacturing or agricultural as their major source of employment.

In particular, textiles have seen Asian prices drop by an average of 23 percent since 1997—prior to 1997, Asian prices were showing moderate growth. Since the dollar's rise, job losses in the textile sector have totaled more than 175,000.

U.S. automakers are being forced by the dollar penalty to pay out billions of dollars in incentives in an expensive effort to slow a sharp decline in market share. At the same time, they are being treated to reports of record profits by Japanese automakers who have tacked billions of dollars in currency-generated profits to their bottom lines.

Paper mills, many with state-of-the-art equipment, have been closed by the dozen as dollar-cheapened imports now take 90 percent of the growth in the U.S. paper market.

The truth is that the overvalued dollar is increasingly forcing manufacturing permanently off-shore as well as displacing increasing numbers of farmers. Jobs, not goods, are now being exported as a result of the dollar tax.

Long term, a 30 percent dollar tax on goods produced in this country is simply not by the majority of U.S. companies and farmers. A key policy question for this Committee and the Government is whether shrinkage of the U.S. manufacturing and agriculture base is an acceptable cost for supporting the out-of-kilter dollar.

The Coalition contends that the U.S. Treasury's policy of a "strong dollar" regardless of economic fundamentals or the dollar's cost to U.S. workers and their families is not good or sound policy. Indeed, this policy has already led to an increase in the current accounts deficit to new record highs, now almost 4.5 percent of U.S. real GDP, more than triple the deficit's level before the dollar began to rise in 1997.

The Coalition notes that Secretary O'Neill, in his previous incarnation as President of International Paper during the 1980's run-up in the dollar's value, complained that the dollar "had turned the world on its head." Today, when the dollar is now reaching the very heights it did during 1980's, the Secretary calls U.S. manufacturers "whiners," expressing "no sympathy" for the burdens the overvalued dollar policy has created. This is not the message that hard-working American families should be hearing.

We firmly believe that sound currency values can be restored and that manufacturing and agriculture can again thrive in this country. To do this, the Treasury should:

- State publicly that the dollar is out of line with economic fundamentals.
- Firmly state that its policy is to seek a market-determined dollar that is consistent with underlying global economic fundamentals, including the competitiveness of America's farms and industries.
- Seek cooperation with other major economies in obtaining common agreement and public statements that their currencies need to appreciate against the dollar.
- Make clear that the United States will resist, and take offsetting action as necessary, foreign country interventions designed to retard movement of currencies toward equilibrium.

The Coalition notes that when the Treasury faced a similar situation more than 15 years ago, it took decisive and successful action. In crafting the "Plaza Accord" of 1985, Treasury Secretary James Baker was able to restore currency equilibrium and launched renewed global growth. It was possible then, and is possible now.

Sincerely,

Aerospace Industries Association
American Brush Manufacturers Association
American Cotton Shippers Association
American Fiber Manufacturers Association
American Forest & Paper Association
American Furniture Manufacturers Association
American Hardware Manufacturers Association
American Iron and Steel Institute
American Paper Machinery Association
American Pipe Fittings Association
American Textile Machinery Association
American Textile Manufacturers Institute
Associated Industries of Florida
The Association for Manufacturing Technology
Automotive Trade Policy Council
Business and Industry Association of New Hampshire
The Business Council of New York State

The Business Roundtable
The Carpet and Rug Institute
Composite Can and Tube Institute
Copper and Brass Fabricators Council
Fiber Box Association
Industrial Fabrics Association International
IPC—Association Connecting Electronics Industries
Mississippi Manufacturers Association
Motor and Equipment Manufacturers Association
National Association of Manufacturers
National Cotton Council of America
National Marine Manufacturers Association
New Jersey Business and Industry Association
Non-ferrous Founders' Society
North Carolina Citizens for Business and Industry
North Carolina Manufacturers Association
Ohio Manufacturers Association
Packaging Machinery Manufacturers Institute
Paperboard Packaging Council
Precision Machined Products Association
Process Equipment Manufacturers' Association
Secondary Materials and Recycled Textiles Association
Southern Forest Products Association
Steel Manufacturers Association
Textile Distributors Association
Tooling and Manufacturing Association
USA Rice Federation
Utah Manufacturers Association
Virginia Manufacturers Association
Waste Treatment Technology Association
Wheat Export Trade Education Committee
Wood Component Manufacturers Association
Wood Machinery Manufacturers of America

For more information about the Coalition for a Sound Dollar, contact Frank Vargo at 202–637–3182 or visit the Coalition's website at *www.sounddollar. org.*

CACO PACIFIC CORPORATION

April 25, 2002
The Honorable Paul S. Sarbanes
370 Russell Senate Office Building
Washington, DC 20510-4302

Re: High Dollar Value

Dear Honorable Paul S. Sarbanes,

I am part owner of an ESOP company in Covina, CA (Caco Pacific Corp). We manufacture tooling for the plastics injection industry, worldwide. Three years ago we employed 220 people and had gross sales of $34,000,000. Of this we exported about $15,000,000. Today we employ 130 people and are currently on an annualized sales projection of $12,000,000. We are barely hanging on. In the last 6 months we have only made a profit of $46,000.

Our problem is the high cost of the dollar. Because of this it has become almost impossible to compete with the foreign competition, mainly the European and then the Asian Mold Makers. Now the material that is standard in our industry, and has been for the last twenty years, has risen from 10% to 30% in costs because of the Section 201 tariff. This material is tool steel, mainly Stainless Steel 420 grade tool steel. Not only has the imported steel companies already raised their prices, so have the domestic suppliers. Try staying in business, under these conditions, especially when I am trying to compete with my foreign competition that bids on the same jobs I do, with a discounted dollar value.

Please get in touch with me, as I would very much like to discuss these issues with you. Also the next time you are in Covina, I would be honored to give you a plant tour of what used to be the largest Mold Making business west of the Mississippi River.

Sincerely,

Paul A. Cockrell
V.P. Engineering

813 North Cummings Road, Covina, CA 91724-2506 USA
Tel 1.626.331.3361 · Fax 1.626.966.4219
www.cacopacific.com

TAYLOR FORGE ENGINEERED SYSTEMS, INC.

First & Iron Streets • Paola, Kansas 66071
Tel: 913-294-5331 • Telex: 62192610
FAX: 913-294-5337

ISO 9001
Certificate Number 30083

April 25, 2002

The Honorable Paul Sarbanes
Chairman, Senate Banking Cte.
Attn: Laurie Better

The Honorable Phil Gramm
Ranking Minority Member, Senate Banking Cte.

Room 534, Dirksen Senate Office Building,
Washington, DC 20510

Reference: The Too Almighty Dollar

Gentlemen:

As the owner of a small manufacturing company who exports over 50% of what we produce, I have been beating the drum of the overvalued U.S. dollar for more than a year now. I now write to you with my cause, as I believe there is enough support behind this issue to start to get attention in Congress, at the Treasury, and in the Administration.

We are fabricators of steel plate, and our industry has been complaining about unfair trade practices by our foreign competitors for the past couple years. And though I am convinced this is in fact happening, making meaningful progress toward solving this problem is difficult, long, expensive, and political. The equally debilitating problem is the rise in the dollar over the past 24 to 36 months.

Several issues have lined up in support of a weaker dollar. If we expect our economy to recover, we need to bring our trade deficit closer to balance. I do not believe this means import less, but export more. As a fabricator of steel plate, if we have any hopes for the Section 201 trade case succeeding, nullifying the penalties with a stronger dollar will sink this effort. If the administration expects to get results from their energy policy, they are going to need domestic capacity. Many companies like ours have gone out of business over the past 2-3 years and we will be incapable of supporting a program increase.

The direct effect on our company is seen on both domestic and international projects. In 1998 over 30% of our total sales were going to Korea. Today, 0% is going to Korea. In 1998, we had minimal competition from Italy, some from Canada, and none from Korea for domestic business. Today, almost 40% (by weight) of the steam drums purchased for combined cycle power plants in the U.S. are coming from Korea; over 50% of the reactors for refinery

applications are coming from Japan, Italy and Belgium. Canada is able to buy "dumped plate" and circumvent the trade case sanctions and penalties by shipping in fabricated product at $0.63 Canadian to $1.00 USD.

It appears to me that the dollar is not moving in step with the rest of the economy. History has shown that minimal action by Congress, the Treasury, or the Administration regarding an overvalued dollar is enough to make some impact. More aggressive steps are necessary, but a policy statement would be a start. Open markets, fair trade, and free trade, apply to monetary policy as well manufactured goods.

My hope is that mine becomes one of many voices from the U.S. manufacturing industry voicing the same concerns. Thank you for your time. I would be happy to hear your comments.

Very truly yours,
TAYLOR FORGE ENGINEERED SYSTEMS, INC.

Michael G. Kilkenny
President

P.L. PORTER

P.L. Porter Controls, Inc.
6355 DeSoto Ave.
Woodland Hills, CA 91367-2687 USA
www.plporter.com

Facsimile Transmission

Date:	April 25, 2002	**From:**	Gregory P. Lennox, CEO
To:	The Honorable Paul Sarbanes The Honorable Phil Gramm Senate Banking Committee	**Voice #:**	+1-818-313-6037
Fax: #	**202-224-2080** **202-224-7391**	**Fax #:**	+1-818-610-1821
Company:		**e-mail:**	glennox@plporter.com
cc:	Coalition for a Sound Dollar	**Pages:**	1, including cover sheet
Subject:	**Human Impact of Strong Dollar**	**If you do not receive all pages, please contact sender.**	

Gentlemen,

I am the third generation president of a manufacturing business started in Los Angeles by my grandfather in 1947. We supply aircraft seating mechanisms (the little round button seat recliners) to customers worldwide.

In the past 15 years, most aircraft seat production has shifted from the USA to Europe. As a result, most of our direct competitors are European companies. You already know the unfair competitive advantage our European competitors have gained since the introduction of the Euro.

We don't want to move our company to Europe to remain competitive. That would mean the loss of hundreds of jobs, at our company and at our suppliers' companies. We successfully reduced costs through product and manufacturing process innovation—in dollar terms—but we still lost ground against the Europeans in Euro terms.

We estimate that 100 jobs have been lost at our company alone due to the unrealistically low value of the Euro against the dollar. So doing "nothing" has a great cost—for me as a business owner, and for you as government leaders, and, most notably, for the individuals affected.

A strong dollar is good for the consumer economy for only a short time. When enough economic dislocation occurs, there won't be jobs for American consumers to hold. In the l-o-n-g run, this will reduce the value of the dollar and bring everything into economic equilibrium, but at what cost to society? Too great a cost in human terms, in my opinion.

I strongly encourage you to take a leadership position to ensure foreign currencies are not artificially depressed to stimulate export industries like commercial aviation in Europe and elsewhere.

Sincerely,

Gregory P. Lennox
Chairman & CEO

REDMON

April 25, 2002

The Honorable Paul Sarbanes
Chairman, Senate Banking Cte
Attn: Laurie Better
Room 534, Dirksen Senate Office Building
Washington D.C. 20510

Dear Mr. Sarbanes,

The Redmon Company, a 118-year-old privately held U.S. manufacture of consumer goods, is being hurt by the unusually high value of the dollar on the world markets.

It's a two-edge sword! On one side we are less able to export our product around the world because of the increased cost to our customers abroad as the dollar increases. On the other side our large U.S. customers like K-Mart, Wal-Mart, Sears, and J.C. Penney are buying direct from abroad rather than from us because the price is much better due to exchange rates.

The over valuation is hurting not only the economy, but companies like ours who are providing American jobs. Would you please address this issue by intervening to bring the dollar down to a more acceptable level?

U.S. Patriot,

Peter Redmon, President
W.C. Redmon Company

Metal

Engineered Products
4180 South Creek Road • Chattanooga, TN 37406 USA
Phone: 423/622-4131 • Fax: 423/622-2227
E-Mail: ken.schorle@metaltekint.com

April 26, 2002

The Honorable Paul Sarbanes
Chairman, Senate Banking Cte.
Attn: Laurie Better
Room 534, Dirksen Senate Office
Washington, DC 20510

RE: SOUND DOLLAR COALITION

Dear Sir:

We are a small non-ferrous foundry and machining facility in Chattanooga, Tennessee.

I am writing to ask your help in reducing the value of the dollar to a level which would help U.S. companies compete with foreign competition.

We are in very competitive manufacturing markets and have invested in people and capital tools to increase productivity. With the dollar overvalued, it is making it extremely difficult to compete with foreign competition.

A year ago we employed 104; we currently employ 67 people. September 11th certainly had a negative effect on us. The over valuing of the dollar has also had a negative impact on our industry.

We see competition from New Zealand that generally is 30% below current U.S. market pricing.

Also I'm enclosing a current advertisement that ran in one of our trade association magazines. It shows competition from Chile wanting sales representation to sell direct into the States.

Please make every effort to help our employees and our companies in the United States compete on a level playing field.

Sincerely,

Kenneth Schorle
President

HELP WANTED

SALES TO SALES MANAGER – Iron foundry looking for someone to fill open Sales Position that will evolve into Sales Manager position in three to five years. Foundry background and experience a plus. **Box 2698, c/o modern casting, 505 State St., Des Plaines, IL 60016-8399.**

PATTERNMAKER/JOURNEYMAN – Wood/metal/plastic. Sunny SW. **915/877-3343, Fax 915/877-7071.**
E-mail: info@mfi-usa.com
Web Site: www.mfi-usa.com

QUOTING ENGINEER – Ward Corporation, specializing in aluminum sand, and permanent mold castings, is seeking a qualified Quoting Engineer. Qualifications: Experience in foundry engineering, basic tooling design and process engineering. Must have thorough understanding of blueprints and geometric tolerancing. Capable of processing casting quotation from blueprints or CAD files, basic knowledge of CNC machining. Ability to work as a team member, ability to communicate with customers, supply engineers and purchasing. We offer a competitive salary, group health and life insurance, tuition reimbursement, paid holidays and vacations. Send resume to: **Ward Corporation, 642 Growth Ave., Fort Wayne, IN 46808. Fax 219-420-1919.**
E-mail: marcb@wardcorp.com
Web site: www.wardcorp.com

COREROOM SUPERVISOR – Green sand nobake foundry looking for Coreroom Supervisor. Must have experience in hot, cold, and nobake processes. Salary based on experience. Please submit resume along with salary requirements to: **Human Resources Department, McConway & Torley, 109 48th St., Pittsburgh, PA 15201.** ***EEO/AA.***

REPS WANTED

MACHINE SHOP – Established (38 years in business) CNC horizontal and vertical machining center job shop working on ferrous and nonferrous castings, forgings, wrought parts, etc., is seeking qualified representation outside of Wisconsin. Shop is non-union, has QA manual and is working toward ISO 9000 certification. Fax or mail your coverage, resume and references to: **TMC, 2222 S. Calhoun Rd., New Berlin, WI 53151. Fax 262/782-7150.**

SALES REPS WANTED – Large gray iron, ductile iron, aluminum sand casting foundry in Ontario, Canada specializing in highly-cored castings is seeking experienced representation throughout the U.S. Technical and sales background in ferrous and aluminum castings a plus. Please submit reply to **John Vickers, Vice President & General Manager, Wabtec Foundry Limited, 40 Mason Street, Wallaceburg, Ontario N8A 4M1.**

REPS WANTED

SALES REPRESENTATION needed for Texas, Oklahoma, and possibly other SW states. We are building a national sales network, and this is your opportunity to get aboard. Principal is Macaulay Foundry, a pioneer of large, highly complex gray, ductile, and high alloy iron castings. Reply with resume and references via email to: **macaulay@metalcasting.com**

SALES REPS NEEDED – Paragon Metals, Inc. is a, Charlotte, North Carolina based, global supplier of engineered products including ductile, malleable and gray iron, medium to high volume castings for automotive, railroad freight car, Class 8 trucks, automotive transmission, tire molds, earthmoving equipment and other industrial markets. We maintain a number of joint ventures and strategic alliances with partners in China, South Korea, Taiwan and South Africa. In addition, we are nearing completion of NVF, a new world class, joint venture iron foundry in Korea, equipped with a 230C DISA high speed molding machine and a LOI continuous type heat treat. We specialize in ductile, gray and malleable iron castings up to 30 lbs.; with capabilities for heavier castings up to 1200 lbs. or more. We also manufacture aluminum die-castings, closed die forgings, automotive leaf springs and pole line suspension hardware. All castings are sold F.O.B. Paragon Metals' Charlotte or other regional warehouse, or to the customer's plant. We are seeking dynamic and product knowledgeable rep group(s) to cover northern and southern California, the Pacific Northwest and British Columbia, Canada. The ideal multi-person agency will have 10 years experience selling castings and a solid familiarity with the industrial base in the territory. Please fax or email your letter of introduction to: **Jack Richards, Director, International Sales & Marketing, Paragon Metals, Inc., 7910 Crescent Executive Drive, Suite 200, Charlotte, NC. 29217. Phone: 980/235-1452, Fax: (980) 235-1415. E-mail: jack.richards@paragonmetals.com**

MANUFACTURER SALES REPRESENTATIVES – OPPORTUNITIES NATIONWIDE – Q Cast Aluminum based in New Berlin, PA is a quality aluminum sand casting company serving the park and playground, transportation, construction, machinery and many other industries. We are looking for independent Manufacturer's Representatives for territories in the U.S. We are on a quest to expand our presence nationwide and are seeking professional representatives to grow with us. This is our 47th year. Though we are a very well established company, the company is young, aggressive and aiming towards continued future success. We are ISO 9002 registered, have excellent employees and have earned our top customer supplier award in quality, delivery and service. Come join us and be part of our success. For consideration, please send information to: **General Manager, Q Cast Aluminum, 809 Market St., PO Box 525, New Berlin, PA 17855 or E-mail: dlpowers@qe-man.com**

REPS WANTED

REPS WANTED – Established in 1941 as a non-ferrous foundry, **SORENA** has become a major producer of bronze parts for heavy industry in Chile and the rest of South America. We are currently establishing an office in the USA to develop business relationships with OEM's who produce heavy equipment for such industries as: ore crushers, pumps, off-road equipment, cranes, heavy duty conveyors, gear blanks and speed reducers, turbine seals, bearing cages and machine tool parts. SORENA has a sand foundry, centrifugal capacity to 53" and vertical and horizontal continuous cast machines, a CNC shop and conventional equipment to machine up to 130" diameter. Currently most MANA territories are open. **Please contact Tom at 800-478-0887 or fax 609-599-1424.**

MANUFACTURERS REPRESENTATIVES WANTED – Sand, investment castings and die-castings. We offer parts to print, as cast, machined, painted, plated and assembled to customer specifications. Excellent prices on parts and tooling from Asia shipped to and inspected in our U.S. warehouse. All import paperwork handled by us. Parts shipped FOB Columbus, MS. ISO certified sources and U.S. sales and technical support from G.C.R. with over 20 years foundry experience. Send resume and line card to **Global Casting Resources, 118 S McCrary Rd., #109, Columbus, MS. Fax 662/328-2274.**
Web Site: globalcastingresources.com

ESTABLISHED INVESTMENT CASTING foundry seeking Manufacturers Representatives on account basis. All replies confidential. **Box 2690, c/o modern casting, 505 State St., Des Plaines, IL 60016-8399.**

REPS WANTED – Manufacturer of powerful industrial vacuums seeks Manufacturers and Sales Representatives to promote its products. **Stephen Schoenberger, Vector Technologies Ltd., Vacuum Engineering Group, 800/832-4010.**
E-mail: sales@vector-vacuums.com

SALES REPS WANTED – For sale of ferrous and nonferrous castings, forgings, and machine parts from China and Mexico. Very attractive pricing on raw or machined parts. Excellent sales and engineering support. Many areas are still available. This is a great opportunity for reps interested in offering offshore sources to their customers. Please send resume to: **Genny Johnson, Oversea Link, 5605 Route 96, PO Box 25340, Farmington NY 14425.**

SALES REPRESENTATIVES: SAND & INVESTMENT CASTINGS – High quality, competitively priced supplier of steel and all stainless grades is happy to reward you for your strong personal contacts. We offer a strong commission schedule for your relationships with the people making the buying decisions. **Ferralloy, Inc. 440/331-3900, Fax 440/331-3901.**
Website: www.ferralloy.com

Shurtape®
PRESSURE SENSITIVE TAPES

April 26, 2002

Honorable Paul Sarbanes. Chairman
Senate Banking Committee
Fax: 202-224-7391

We are a privately held company with its headquarters located in western North Carolina. Our roots are in textiles but, mostly because of imports, some years ago we began to shift our resources toward manufacturing a variety of adhesive tape products. As part of this transition, we have built a substantial export business. We now have distribution facilities in six foreign countries.

We have worked hard at exporting because we knew we were truly part of a global market and we believed there was huge growth potential in exports. More recently the unreasonably strong dollar has drastically changed the economics and, not only is it impossible to compete in textiles, but our adhesive tape products are experiencing the same effect. All the technology, investment and marketing efforts cannot overcome a 25-40% disadvantage in currency. The current strong dollar policy will eventually drive most manufacturing off shore. This situation is extremely difficult for us and I cannot believe it is good for our country. I do not understand why it is that we are so frequently put at a disadvantage by our own government.

Very truly yours,

Pope Shuford
Chairman

Q.Carolina Mills Inc

P.O. BOX 157
MAIDEN, NC 28650-0157
828-428-9911

April 26, 2002

The Honorable Paul Sarbanes
Chairman, Senate Banking Committee
Attn: Laurie Better

FAX: 202-224-2080

Dear Mr. Sarbanes:

I am enclosing a copy of an article from the April 19th issue of The Gaston Gazette, the local newspaper for Gastonia, North Carolina. The article outlines yet another plant closing by our company, Carolina Mills, Inc., and the devastating impact on some very good people and the surrounding community.

Over the last two years we have closed eight plants displacing more than 1,200 employees. Since 1997 the textile industry has closed more than 200 plants and displaced more than 170,000 employees.

I have been in the textile business for over thirty years and we have always fought cheap labor and foreign imports. We had been very successful up until 1997-1998 by aggressively modernizing and automating our plants to remain competitive. However, since the Asian crisis and resulting devaluation of currencies, we have seen a precipitous drop in demand and incredible price pressure from products all over the world. In many cases today if we put "ZERO" cost in for labor we cannot compete. This makes it crystal clear that other factors such as the strong dollar (as much as 40% change in some cases), foreign government subsidies, illegal shipments, and manufacturing conditions which would be illegal in our country have all combined to crush our industry.

It should be obvious that our overvalued dollar and these other factors, if left unchecked, will eventually eliminate all manufacturing sectors of our economy. The loss of jobs and the resulting loss of revenue are already seriously impacting local, state, and federal budgets. This loss of revenue will accelerate with more people out of work and more companies either not profitable or in bankruptcy. At the same time the demand for services and assistance will grow exponentially, thereby exploding deficits.

I would respectfully ask that you and your committee make every effort to bring the dollar to a sound, but more reasonable level before it is too late to save our strategically important manufacturing base.

Very truly yours,

Steve Dobbins
President and CEO

fhe

CRAFTED WITH PRIDE IN U.S.A.

Friday
April 19, 2002

TODAY'S HIGH 88°
LOW 62°

Today
Late rain possible
Details, 2A

The Gaston Gazette

Prepared to peck

An expectant couple of Killdeer birds found a home in Lowell, and aren't letting humans take it away.

Hometown Page 1B

Ranlo plant closing; 170 jobs los

Carolina Mills says Ranlo operations to be consolidated

By Thomas L. Morgan
Gazette Business Editor

RANLO — For the third time in less than a year, news concerning the local Carolina Mills plants is not good.

Maiden-based Carolina Mills announced Thursday it will close plant No. 24 in Ranlo and shut down certain departments in neighboring Plant No. 21 by the end of June. The moves are expected to affect about 170 jobs.

"This is just one more example of jobs lost due to a U.S. monetary policy that gives foreign competitors as much as a 30- to 40-percent advantage in currency exchange in addition to their low wages and few benefits," said Steve Dobbins, president and CEO, in a prepared statement, "and a U.S. trade policy that for years has been willing to trade textile, apparel and other manufacturing jobs to gain favor with other nations."

After this move, Carolina Mills will have eight facilities and 1,300 workers in North Carolina, Dobbins said after spending Thursday at the Ranlo plants. Those facilities produce synthetic yarn, primarily polyester.

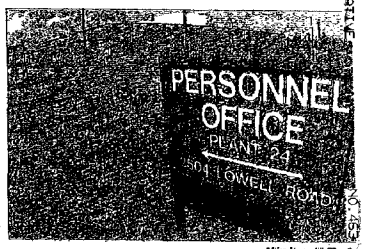
"What we've had is about 420 people in three plants there and it will become basically one plant with about 250 employees," Dobbins said. "This is basically the aftershock of what happened to big companies like Burlington Industries and Malden Mills and Gayley & Lord — all of those were customers of ours, which means less demand, so we're losing our customer base because they're affected by the imports.

"We're still in the process of trying to re-invent ourselves," he added. "We have some very good people in Ranlo and this is through no fault of their own."

Carolina Mills has facilities in Lincoln, Catawba, Iredell and Burke counties, and Dobbins said there would be an effort to place former Ranlo employees wherever possible. The company also promised "transitional and retraining programs."

Last May, Carolina Mills announced it would close its No. 5 Lincolnton plant by the end of June, laying off about 120 employees.

▶See Plant closing/Page 6A



Mike Horsell/The Ga

Carolina Mills Plant No. 24 on Lowell Road in Ranlo will be closing

Plant closing

continued from Page 1A

Last August, the company announced the closing of its No. 23 Ranlo plant, with 100 jobs affected. Also announced at that time was the closing of the St. Pauls plant, located in Robeson County, southeast of Fayetteville and north of Lumberton. About 320 jobs were lost there.

"We're going to continue to face declines in the textile business," said Donny Hicks, executive director of the Gaston County Economic Development Commission. "This is a pretty strong trend. We're still working with (U.S. Rep.) Sue Myrick's office on a weekly basis, but this is so strong, we're not sure what can be done to stop it."

About 7,400 people have lost jobs here since 1999, according to the Gaston office of the North Carolina Employment Security Commission. Gaston has lost more than 4,700 manufacturing jobs in the past two calendar years, 2,336 of those in textiles.

In January, the Gaston jobless rate hit at least 10 percent for the first time since 1983. That dropped to 8.1 in February. The county saw at least 8 percent unemployment four times in 2001.

Also in January, 457 local job losses were announced, 90 of those from the closing of the Burlington Industries plant in Mount Holly. That was finalized in March, a month in which the Spring Ford plant in Gastonia that once employed 100 people announced it would cease operation.

In February, Grant Aldonas of the U.S. Commerce Department presided over a textiles roundtable held at the Carolina Mills home office in Maiden, with Dobbins and board chairman George Moretz acting as hosts.

"I think what this reflects is the weakness the industry has experienced over the last couple of years, the result of which is people have to realign their manufacturing facilities based on current demand," said Jim Conner, a veteran of more than 30 years with the American Yarn Spinners Association, which leases its office space from Carolina Mills in Ranlo.

"It's unfortunate and we hate to see this happen to such a fine company and their employees, who are our neighbors," Conner said.

The affected mills were part of A.M. Smyre Manufacturing Co. from 1916 to 1981, according to Fred L. Smyre III, whose grandfather was the founder.

"We're in a global society and a global economy," said Smyre, known locally as "Rick," "and one of the reasons we sold the mills was the anticipation of this. It's a credit to those still competing, like Parkdale and Pharr and others, to be able to do so while so many key players in that industry have either gone out of business or declared bankruptcy."

You can reach Thomas J. Monigan at (704) 869-1836.

Lakeside

To: (HTTP://CAPWIZ.COM/NAM/ISSUES/ALERT/?ALERTID=14172...

Subject: OVERVALUED DOLLAR

04/26/02

Please take into consideration the problems caused for the textile industry due to the overvalued dollar. Our industry has suffered tremendously with plant closings and lay-offs with many employees unable to find work in other industries due to the suffering the same fate as our industry.
Please understand that the textile industry is in deep trouble directly due to imports. This industry has been the back bone of the economy for many years. Employees and ex-employees now have the feeling that our very own government has sold out the industry.
In 2001, 116 textile mills were closed and 67,000 employees lost jobs. Since the rise of the dollar in 1997, [illegible] closed and 177,000 employees were displaced. All this is due to imports from countries that have no human rights concern for their employees other than the amount of production that can be made.

Why do want to run us out of business? Textile plants and employees have been good corporate citizens, have paid taxes, and help to make this country what it is today. Will you please help us stay afloat and allow for U.S. citizens to build productive lives.

Secretary O'Neil is staunchly in favor of the strong dollar even with all the information available to him. He has referred to U.S. companies as whiners and states that he has no sympathy for any of us. Why then, in 1985 during a similar rise in the dollar, did he say "the strong dollar has turned the world on it's head". He made this statement at the time Mr. O"Neil was president of International Paper and was, at that time, in touch with reality. The situation at that time was affecting him. It evidently does not now.

Joey Seaborn
TNS MILLS, INC.
334/687-2491 (Phone)
334/687-0751(Fax)

Kvaerner Songer

April 26, 2002

The Honorable Paul Sarbanes
(FAX: 202-224-2080)
Chairman, Senate Banking Cte.
Room 534, Dirksen Senate Office Building
Washington, DC 20510

The Honorable Phil Gramm
(FAX: 202-224-7391)
Ranking Minority Member, Senate Banking Cte.
Room 534, Dirksen Senate Office Building
Washington, DC 20510

Attention: Laurie Better

Subject: Coalition for a Sound Dollar

Gentlemen,

The U.S. dollar has soared nearly 30 percent over the last few years, and badly hurts U.S. manufacturing, farmers and many service workers. Kvaerner Songer stands behind The Coalition for a Sound Dollar, in its efforts for a change in U.S. dollar policy.

Kvaerner Songer is an industrial construction company that has been a dominant player within the steel industry. The drop in exports over the past few years, within the steel market, has not only effected Kvaerner Songer, but many other companies associated with the industrial construction market. If the industrial marketplace loses or has significantly less export capabilities due to the increasing dollar value, industrial construction loses as well. (no money, no upgrades, no work)

We challenge the U.S. government to stand up and state publicly that the dollar is out of line with economic fundamentals; to stop giving the impression the government is pleased with the dollar, no matter how strong; and to commit to cooperating with other major countries to ensure that market forces can work to bring about more realistic exchange rates.

We are asking for your help.

Sincerely,

KVAERNER SONGER, INC.

James H. Miller,
President

JHM:tma

COALITIONforaSOUNDDOLLAR_jhm_4_26_02.doc

KVÆRNER

Southern Mills

Southern Mills, Inc.
6501 Mall Boulevard
P.O. Box 289
Union City, Georgia 30291

770-969-1000
FAX: 770-969-6846
philv@somills.com

Philip S. Vincent
President & CEO

April 26, 2002

Honorable Paul Sarbanes
Chairman, Senate Banking Committee
United States Senate
309 Hart Building
Washington, DC 20515

Via Fax: 202-224-2080

Attention: Laurie Better

Dear Senator Sarbanes:

Re: Strong U. S. Dollar

Southern Mills makes inherently flame resistant protective fabric for such applications as firemen's bunker gear, including all of the fabrics for the New York Fire Department. Our fabrics helped save thousands of lives on September 11, 2001.

Unfortunately, our biggest competitor is in Canada. We are continuing to lose business to the Canadian company because of the overly strong dollar versus the Canadian dollar. In the fire service industry we have lost 20% market share to our Canadian competitor in the past five years.

This also applies to our industrial customer base – companies who use our flame resistant fabrics to make safety garments for petrochemical and utility workers in the U. S. We have lost 15% of this market share over the same time period. I vividly recall the 1970's when we were exporting a lot of textile products to the Canadians when the Canadian dollar was at a premium to the U. S. dollar. Business was good in those days.

These same protective fabrics go into military apparel for the Army, Navy and Air Force. We have already been forced to close down one plant due to lost revenue and profit. There will come a day when our military will need U. S. made textile products. China will not be willing to sell us textiles if they happen to be the enemy.

Surely you are interested in preserving the American manufacturing sector that has made America great. The service industry, which has grown so much in the last 20-30 years, does not add value to the great natural resources and agriculturally produced products that the U. S. is blessed with. Manufacturing does add value to our economy. The continued loss of manufacturing to foreign countries is bringing down our economic dominance. One day China will rule the world the way the United States has for the past 100 years.

Please change your policy of a stronger and stronger dollar. It is destroying the very important manufacturing sector of our economy and putting many Americans out of work. Since 1997 when the dollar started to rise, the textile industry alone has lost 177,000 textile jobs and 215 textile mills have been closed in the United States.

On May 1 please think of Americans first and work to reduce this very damaging strong dollar. Our industry is counting on you.

Best regards,

Philip S. Vincent

TNS Mills

FAX

To: Honorable Paul Sarbanes
Chairman, Senate Banking Committee
Attn: Laurie Better
Fax 1-202-224-2080

Alan R Austin

From: Alan R. Austin
General Manager Finance and Accounting
Office: 864-255-3524
Fax: 864-298-0235

Date: April 26, 2002

Ref: Over-valued dollar

Pages: 1 including cover page

Fact - In the past year TNS has closed 15 of 23 textile plant operations (65%).

Fact - Reduced the total number of employees from 2,400 to 890 (63%).

Fact - Sales have fallen from $28.9 M in March 2001 to $13.4 M in March 2002 (54%).

This is due in large part to the OVER-VALUED DOLLAR.

Government is always doing something for the guy overseas.

What is the guy overseas doing for us?

Not a lot.

How about doing something to protect our future and that of our children!

We'll be paying closer attention to what you, who are suppose to be our representatives, are or are not doing for us.

Leigh

LEIGH FIBERS, INC.
P. O. Box 1132, Spartanburg, S.C. 29304
Telephone: (864) 439-4111 / Fax: (864) 439-4118

April 26, 2002

Honorable Paul Sarbanes
Chairman, Senate Banking Committee

FAX: (202) 224-2080

ATTN: Laurie Better

The flood of low priced Asian imports has hurt our company, Leigh Fibers, and caused us to reduce our workforce. We now employ 20% fewer people than 1 year ago, and even fewer compared to 3 or 4 years ago.

The weak Asian currencies, or conversely the exceptionally strong U.S. dollar, is a major part of the reason behind our company's contraction. Our firm recycles the industrial fiber scrap of textile, fiber and apparel companies, and their business has been decimated by imports. We are hurt in turn.

We don't need a weak U.S. dollar, just a dollar fairly priced relative to historical levels. Please let the value of the U.S. dollar decline a bit, so that we, and the rest of the manufacturing sector, can remain in business in the U.S.

Sincerely,

Carl P. Lehner
CEO, Leigh Fibers, Inc.

/mt

7910 WOODMONT
BETHESDA,
PHONE: 301/650-
FAX: 301/650-10
E-MAIL: smartasn@erols.com
WEBPAGE: www.smartasn.org

April 26, 2002

The Honorable Paul Sarbanes
Chairman, Senate Banking Committee
Room 534
Dirksen Senate Office Building
Washington, DC 20510

By Fax: 202/224-2080

Dear Senator Sarbanes,

Industry members whose livelihoods depend on exporting recycled textile materials have been hurt badly during the past few years from the strong dollar. Many of these companies are located in Maryland, as well as nationwide, and are involved with recycling clothing, mill ends, remnants, and manufacturing industrial wipers.

U.S. exports have dropped $140 billion in the last 18 months alone forcing many companies nationwide to layoff workers or shut down completely. Our industry in particular has been hard hit! Action must be taken immediately to bring the dollar in line with other international economies. We ask that you use your influence to make a commitment to work with other [illegible] countries to ensure that market forces are free to bring about more realistic exchange rates.

Should you or your staff need additional information, please let me know. Thank you for your assistance in this matter.

Sincerely yours,

Bernard D. Brill
Executive Vice President

CHERAW YARN MILLS, Inc.

Manufacturers Of Quality Yarns

EST. 19[illegible]

Honorable Paul Sarbanes
Chairman, Senate Banking Committee
Atten: Laurie Better
Fax: 202-224-2080

Dear Senator Sarbanes,

I am writing to you to express my concern about the over valued dollar and the disastrous impact on our company.

Here are specifies:

(1) Our employment is down 40 jobs (15%) as a direct result of the Asian currency fall. Asian yarn is so cheap that sometime it is less than our raw material cost here in the United States.

(2) The impact on our town of 5000 in rural South Carolina has hit hard. We are the oldest manufacturer in our county and have supported our community for many years. We have done very little since the late 1990's as we have not been profitable. This is a direct result of the dollar strength and the weakness of the Asian currencies.

We need help promptly to bring the dollar back down to normal levels. This is a critical issue for all of us in manufacturing. Thank you for your support.

Sincerely Yours,
CHERAW YARN MILLS, INC.

H Malloy Evans

H. Malloy Evans
President and Treasurer

April 26, 2002

Honorable Paul Sarbanes
Chairman
Senate Banking Committee
Washington, D.C. 20515

Subject: OPPOSITION OF "Strong Dollar" Policy

Dear Senator Sarbanes:

Mount Vernon Mills, Fresno Fabrics facility, is the only textile mill located west of Texas and is proud to be part of Mount Vernon Mills Inc., with corporate offices in Greenville, S.C. As a textile company we are extremely concerned about the current administration's strong dollar policy and the effect it has had on our industry.

Due to the current economic situation in our country, this plant was forced to reduce our workforce by 10%. In addition, during the summer of 2001 we were forced to run our plant on a reduced workweek schedule for three long months which was hard on both our employees and our business. In order to compete we need your help to begin to give American manufacturers a more level playing field!

As an "American Company" we need this administration's support to help us turn our economy around and to keep America strong! One of the best things we can do is to keep producing "American Made" products with the American workforce. However, this strong dollar policy is NOT helping the textile industry!

Please help us compete in the world market and to keep our manufacturing facilities open! Join us in opposing this policy!

Sincerely,

Patty Alves
Human Resources Manager

I am the Human Resources Manager for Mount Vernon Mills, Inc., a textile company that currently employs 150 employees in Cleveland, Georgia. I am very concerned about the effect that the current administration's strong dollar policy has had on the manufacturing sector of the country, and particularly on the textile industry.

The dollar is up 30 percent against major currencies since 1997 (and much more than that against major textile manufacturing countries like Pakistan). That's just like placing a new 30 percent tariff on U.S. products. U.S. goods, and particularly goods in the textile industry, are being priced out of foreign markets - and even out of our own markets. Manufacturers are being particularly hard hit, and are losing sales and laying off workers. In the past two years, Mount Vernon as a whole has decreased our workforce by close to 10% (including 50 employees from our own facility here in Cleveland, GA), much of it related to decreasing operating shifts at various divisions due to lower demand for our products - directly related to imports from countries whose weak currency makes it very hard to compete. The playing field was never level, but has been tilted even further due to the strong dollar - especially in comparison to Asian currencies.

Can we compete? Given anything close to a level playing field, we at Mount Vernon know that we can compete with and beat anyone in the world. It is time to stand up for manufacturers (and the textile industry in particular) and begin to level the field for a change. I do not think we want to be dependent on other countries for all manufacturing. If you believe otherwise, I think this country is in real trouble.

The Administration needs to acknowledge that the problem is serious and should stop saying it is happy with the dollar no matter how much it rises.

Matt Umbehant
Human Resource Manager
Mount Vernon Mills
245 Hulsey Rd
PO Box 2149
Cleveland, GA 30528
Tel: (706) 865 - 2322
Fax: (706) 865 - 6213

American Iron and Steel Institute

1101 17th Street, NW
Suite 1300
Washington, DC 20036-4700
Phone 202.452.7146
Fax 202.463.6573
E-mail ashurkey@steel.org

www.steel.org

Andrew G. Sharkey, III
President and CEO

April 26, 2002

The Honorable Paul Sarbanes
Chairman,
Senate Banking Committee
Attn: Laurie Better
Room 534 Dirksen Senate Office Building
Washington, DC 20510
By FAX 202-224-2080

The Honorable Phil Gramm
Ranking Minority Member
Senate Banking Committee
Room 534, Dirksen Senate Office
Washington, DC 20510
By FAX: 202-224-7391

Dear Senators Sarbanes and Gramm:

I write on behalf of the U.S. member companies of the American Iron and Steel Institute, who together account for more than two-thirds of the raw steel produced annually in the United States. Thank you for agreeing to hold a hearing on May 1 to hear important testimony on the problem of the overvalued U.S. dollar.

The overvalued dollar is a significant problem for America's steel producers. For an industry that is already suffering unprecedented injury due to unfair and disruptive, illegally traded steel imports, the overvalued dollar is making matters worse.

It is not only harming U.S. steel producers directly in the form of increased imports, decreased exports, lost production and lost jobs, but is also hurting our industry indirectly through the serious negative effects it is having on our U.S. customer base. Attached is a one-pager that summarizes the issue from a steel industry standpoint.

Unless the Administration changes course in its current "strong dollar" policy, new free trade initiatives will be in substantial jeopardy. We thank you for giving careful consideration to our concerns and to the views of the National Association of Manufacturers and other industry experts who will be testifying on the dollar problem at the May 1 Senate Banking Committee hearing.

Sincerely,

Andrew G. Sharkey, III

Attachment

May 1, 2002

STEEL – IMPACT OF THE OVERVALUED DOLLAR

Introduction

The steel industry in the United States is in crisis. An unprecedented surge of dumped, subsidized, disruptive -- and illegally traded -- imports has caused severe and long-standing damage to America's competitive steel companies, employees and communities. Much of the industry has been driven into bankruptcy, parts into liquidation, and more will follow if there is no change from current trends. There is an urgent need for the industry to continue transforming itself through a combination of ongoing self-help efforts and sound public policy.

The Exchange Rate Issue

There are diverse variables that affect comparative costs of steelmaking, with exchange rate differentials being the major factor in global comparative cost analysis, particularly in the last several years. In this regard, there is no question that the overvalued U.S. dollar has adversely affected the competitive position of U.S. steelmakers, as shown in the most recent "cost curve" analyses by World Steel Dynamics (WSD) and Donald Barnett of Economic Associates Inc., which take into account the current elevated exchange rate of the U.S. dollar against other currencies. These numbers show an exchange rate penalty of approximately $50 on a $300 product. This is on top of the injury steel is suffering from unfair and disruptive, illegally traded imports.

Exchange rate data from the Federal Reserve for major steel-producing countries illustrate the impact of the overvalued U.S. dollar over the last three years. Between January 1999 and January 2002, the U.S. dollar appreciated in value by 17 percent against the yen (Japan), 31 percent against the euro (EU), 57 percent against the real (Brazil), 12 percent against the won (South Korea), and [illegible] percent against the Taiwan dollar. Also, just this year, the de-linking of the Argentina peso to the U.S. dollar has resulted in that currency losing 70 percent of its value against the U.S. dollar.

A good example of what can happen when a troubled economy devalues its currency and how this simply transfers the problem to the U.S. steel industry occurred in 1998. That year, when Russia devalued the ruble by 75 percent against the U.S. dollar, extremely inefficient Russian steelmakers suddenly went from being high cost producers to among the lowest cost in the global steel industry -- and they did it without investing a single ruble in increased productivity. This is a major reason why the WSD rating has moved Russian steel mills to their current "low cost" status. Compare this artificial boost in competitiveness with the more than $60 billion spent by U.S. steel producers since 1980 to modernize and improve steelmaking facilities in our country.

The overvalued dollar is also hurting the U.S. steel industry indirectly. America's "indirect steel trade" balance (our country's imports and exports of steel-containing products, expressed in tons of steel) has deteriorated by millions of tons in recent years. This deterioration in our indirect steel trade balance is of serious concern to U.S. steel producers. However, it does not result from a genuine decline in competitiveness among steel's U.S. customer base because, in many categories U.S. manufacturers continue to rank among the world's most competitive producers of high quality steel-containing goods. Rather, this deterioration in America's indirect steel trade balance is due largely to macroeconomic factors including, in particular, the overvalued U.S. dollar.

April 26, 2002

The Honorable Paul Sarbanes, Chairman
United States Senate Banking Committee
Attention: Lauri Better
Fax Number: (202) 224-2080

Dear Senator Sarbanes:

On behalf of the South Carolina Manufacturers Alliance, its more than 85 members and representing more than 85,000 employees in the state of South Carolina, I urge you to help us change the treasuries strong dollar policy and to act quickly to bring the dollar back down to normal and competitive levels.

As you know, this policy has caused the dollar to hit a new 16-year high and as a result has made many American-made goods overvalued and costly to consumers, especially overseas. A recent National Association of Manufacturers study shows that the dollar's rise has caused the loss of more than one million manufacturing jobs. These are American jobs, many of which will not return.

We must not give away our manufacturing base. Manufacturing jobs not only create wealth in America, but also are among the highest paid and receive the most benefits of any job class.

As the Senate Banking Committee proceeds with these hearings, we again urge you to reverse the strong dollar policy and help us keep, maintain and create jobs for Americans.

Sincerely,

Todd K. Atwater
Executive Vice President

Gary Williams
VP of Human Resources
Mount Vernon Mills, Inc.
113 Thistledown Way
Taylors, SC 29687.

April 26, 2002

Chairman Senate Banking Committee

534 Dirksen Senate Office Building
Washington, DC 20510

Chairman Committee:

I am the Vice President of Human Resources for Mount Vernon Mills, Inc., a textile company that currently employs 5,700 employees in California, Texas, Mississippi, Alabama, Georgia and South Carolina. I am very concerned about the effect that the current administration's strong dollar policy has had on the manufacturing sector of the country, and particularly on the textile industry.

The dollar is up 30 percent against major currencies since 1997 (and much more than that against major textile manufacturing countries like Pakistan). That's just like placing a new 30 percent tariff on U.S. products. U.S. goods, and particularly goods in the textile industry, are being priced out of foreign markets – and even out of our own markets. Manufacturers are being particularly hard hit, and are losing sales and laying off workers. In the past two years, Mount Vernon has decreased our workforce by close to 10%, much of it related to decreasing operating shifts at various divisions due to lower demand for our products - directly related to imports from countries whose weak currency makes it very hard to compete. The playing field was never level, but has been tilted even further due to the strong dollar - especially in comparison to Asian currencies.

Can we compete? Given anything close to a level playing field, we at Mount Vernon know that we can compete with and beat anyone in the world. It is time to stand up for manufacturers (and the textile industry in particular) and begin to level the field for a change. I do not think we want to be dependent on other countries for all manufacturing. If you believe otherwise, I think this country is in real trouble.

The Administration needs to acknowledge that the problem is serious and should stop saying it is happy with the dollar no matter how much it rises.

Sincerely,

Gary R. Williams
VP of Human Resources
Mount Vernon Mills, Inc.

Received: from mailsims1.senate.gov ([156.33.203.10]) by mailexc2.senate.gov with SMTP
(IMA Internet Exchange 3.13) id 009430D7; Fri, 26 Apr 2002 11:01:02 -0400

Bethlehem Steel Corporation

1170 EIGHTH AVENUE
BETHLEHEM, PA 18016-7699

ROBERT S. MILLER, JR.
CHAIRMAN OF THE BOARD
CHIEF EXECUTIVE OFFICER

Direct Dial: (610) 694-2108
Facsimile: (610) 694-3686
E-Mail: rs.miller@bethsteel.com

April 29, 2002

The Honorable Paul S. Sarbanes
United States Senate
Washington, DC 20510

Dear Senator Sarbanes,

We at Bethlehem Steel are concerned about the appreciation of the dollar that has occurred since 1997. This is an important issue relative to the steel industry and to the overall health of the U.S. manufacturing base.

The dollar has strengthened to the point where it is imposing a large cost on the economy and in particular the manufacturing sector. The trade imbalance caused by an over-valued dollar causes loss of jobs and long term structural damage to manufacturing companies. Companies can be forced to reduce production or close U.S. factories not because they are inefficient but rather because of the strong dollar exchange rate.

We urge consideration of an exchange rate policy that does not put U.S. manufacturing companies at a significant disadvantage relative to our international competitors.

I would be glad to help and offer support to this important cause.

Sincerely,

Past Presidents
W.H. NEWTON 1958-1978
H.E. NEWTON 1946-1958
W.H. NEWTON 1928-1946
J.W. NEWTON 1917-1928
R.P. BROOKS 1899-1917

HOWELL [illegible]
President

Trio MANUFACTURING COMPANY
2 NORTH JACKSON STREET
POST OFFICE DRAWER 270
FORSYTH, GEORGIA 31029-0270
(478) 994-2871 • FAX (478) 994-0508
E-MAIL: trioyarn@hotmail.com

April 29, 2002

Senator Paul Sarbanes
Chairman, Senate Banking Committee
Attention Laurie Better
Via Fax: 202-224-2080

Re: Banking Committee Dollar Hearing on May 1, 2002

Dear Senator Sarbanes:

As the president of a small 103 year old family textile business located in the heart of middle Georgia which is still somewhat a rural community, I am gravely concerned about what is happening to our industry due to the policy of our country to support a strong dollar. The year 1999 was a record year for our company, however, as the beginning of the year 2000 unfolded we saw tremendous troubles on the horizon.

Our company is a 100% cotton sales yarn manufacturer that sells principally cotton yarn to the home furnishing trade in this country. We attempt to export our product when possible. Lately this has been completely impossible due to the strong dollar versus other foreign currencies.

The most damaging aspect we have seen is the flood of imports of cheap scatter rugs into this [illegible]. This has displaced the need for yarn by our customers since the retailer is buying the finished product at a cheaper price than can be manufactured in this country.

In 2000 we operated slightly at a break even and 2001 was an absolute disaster. The first three [illegible] 2002 have not changed at all even given the fact that our economy seems to be recovering [illegible] recession. To us, what we have experienced is a depression.

In January of this year we were forced to have a permanent lay off involving 15% of our associates. Many of these individuals had been with our company for as many as 20 years. This was an absolutely devastating decision that we were forced to make, but one which was completely necessary to preserve the remaining jobs. Our company has invested significant dollars in new equipment and technology over the past two to three years. We are a modern textile manufacturing company. We simply can not compete in the world due to the policies our government has adopted in reference to the strong dollar and trade.

Please challenge Treasury Secretary O'Neill as he appears before your committee to discuss this matter on May 1st. Thank you for your attention to this request.

Sincerely,

Howell W. Newton
President

WOOD COMPONENT MANUFACTURERS ASSOCIATION

1000 Johnson Ferry Rd., Suite A-130
Marietta, GA 30068
Tel: (770) 565-6660 • Fax: 770-565-6663
Webpage: *www.woodcomponents.org* Email: *skelawser@a*

F A X C O V E R S H E E T

Date:	April 29, 2002
From:	Steve Lawser, Executive Director
To:	The Honorable Paul Sarbanes
	Chairman, Senate Banking Committee
	Attn: Laurie Better
Fax:	202-224-2080

Number of pages including cover sheet: 2

Message

The Wood Component Manufacturers Association represents 150 manufacturers of wood component products supplying the furniture, cabinet, building products and specialty wood product industries. These companies are located throughout the United States and Canada.

The majority of our members are (or were) involved in international markets. The value of the U.S. dollar is up 30% against major currencies since 1997. That's just like placing a 30% tariff on the products our members' exports and, at the same time, gives our foreign competitors a 30% price advantage on the products they are selling to U.S. customers. Our members' products are being priced out of foreign markets and also out of our own domestic markets. As a result, nearly 60% of our member companies have lost sales and laid off workers according to our recent Market Survey.

To make matters worse, many of our furniture manufacturers & customers are being forced to import components and finished furniture in order to compete with offshore furniture suppliers. It's shocking to think that we cannot compete in our own domestic markets considering our timber resources are second to none. Our furniture and woodworking industries CAN compete with offshore competitors if we had a level playing field. The 30% currency advantage that foreign companies have is simply too much to overcome, no matter how efficient and productive we are. Furthermore, our foreign competitors are using their lower exchange rate as a "crutch" to unfairly compete with us and takeover our markets (see attached article from Canada's Financial Post).

We ask that the Administration make currency realignment a major priority and actively work with our trading partners to address the disparity in exchange rate markets. These cooperative efforts worked in the 1985 Plaza Accord that brought stability to exchange rate markets and can work again. We need your help on this critical issue in order to save American manufacturing jobs.

Low dollar a crutch for business, Manley says

Currency falls after Minister's remarks on productivity

By Alan Toulin

OTTAWA • The low value of the Canadian dollar is a crutch that allows Canadian companies to remain competitive even if they are inefficient, the Deputy Prime Minister said yesterday.

John Manley said many companies cannot compete and would fold if the currency increased in value against the U.S. dollar.

"I worry that too many Canadian firms are profiting mightily from a 62¢ dollar and would be hard-pressed to compete at an 80¢ dollar," Mr. Manley said, adding that productivity is the country's most pressing economic concern.

"If they don't make the investments in research and development and technology and innovation, when the dollar gets to that level they'll be out of business."

Mr. Manley's comments helped sink the Canadian dollar on foreign exchange markets yesterday, analysts said. The currency closed at US62.63¢, down nearly half a cent from its previous close of US63.04¢ on Tuesday.

Analysts applauded Mr. Manley's frankness in admitting the low dollar has held back productivity growth, but added that the government needs to play its part by reducing regulation and taxes.

"I find it cynical in the extreme for the government to be saying this because there's a lot of people who believe there has been a deliberate low dollar policy pursued over the last number of years in Canada by the government," Catherine Swift, president of the Canadian Federation of Independent Business (CFIB), said yesterday.

See DOLLAR on Page A11

More coverage, Page FP1

Article that appeared in the March 14, 2002 issue of the Financial Post in Canada

s up to industry, Manley says

DOLLAR

Continued from Page A1

"They seem amazingly resistant to changing things in their purview – the regulatory structure which is so burdensome and costly in Canada, our whole tax environment which continues to be highly uncompetitive with our major economic partner to the south."

Mr. Manley said government is doing its part to boost the dollar by improving Ottawa's fiscal circumstances but it is up to industry to invest if productivity is to go up.

"It's not up to us. The private sector has got to make the investments," Mr. Manley said.

The Canadian dollar has fallen steadily for 20 years against the U.S. dollar, but the Liberal government has always said the economic fundamentals of the country are sound and they should eventually be reflected in the exchange value of the currency.

The Liberal government did become concerned about the low value of the currency in January when it fell to US61.75¢.

Jean Chrétien, the Prime Minister, Paul Martin, the Minister of Finance, and David Dodge, the Governor of the Bank of Canada, embarked on an unprecedented campaign to talk up the dollar. The currency experienced a short-lived rally but began to slip again a short time later.

In February, Allan Rock, the Minister of Industry, acknowledged that Canadians measure their prosperity and economic standing against the United States and that Canadians' standard of living [illegible] been declining for 20 years.

Previously, the Liberal government had denied or downplayed suggestions that economic policy may need to be revamped in order to catch up to the United States.

Last spring, the Commons industry committee issued a report on the currency that said the low dollar was having a negative effect on productivity by making the cost of imported machinery and technology prohibitive and by discouraging Canadian business from investing in their factories and their workforce.

Canada's productivity growth rate was only about half the U.S. rate in the 1990s. Critics of government policy have said the low value of the Canadian dollar is [illegible] symptom of this problem, [illegible] formance.

Ms. Swift of the CFIB said the federal government may have reduced personal income taxes slightly but the high level of taxation on property, payrolls and capital reduces profit that could be spent on productivity-enhancing technology.

She said lack of co-ordination among all levels of government on business issues results in layer upon layer of regulation.

Mike Murphy, senior vice-president of policy at the Canadian Chamber of Commerce in Ottawa, said three things make Canada less competitive on the world stage – high government debt levels, high taxes and high government spending.

National Post, with files from Jacqueline Thorpe

STS STEEL, INC.

ENGINEERS • FABRICATORS • ERECTORS

The Honorable Paul Sarbanes
Chairman, Senate Banking Committee
Rm. 534, Dirksen Senate Office Building
Washington, DC 20410
Attn: Laurie Better

via email

4/29/02

re: US Dollar Overvaluation

Dear Chairman Sarbanes,

It has come to our attention that the Senate Banking Committee which you Chair will hold a meeting on May 1, 2002 regarding the strength of the US dollar. This is an issue of vital interest to the steel fabrication industry, particularly those of us in the Northeast. STS Steel, of which I am President, has lost many projects to Canadian fabricators over the last few years including projects funded by taxpayer dollars such as schools in both New York and Connecticut. We regularly see loads of steel coming down the Northway (I-87) headed for New York City where the Canadians now dominate the steel construction industry. It is my understanding that the first building planned to be rebuilt in lower Manhattan, WTC #7, is contracted to ADF, a large Canadian firm which boasts openly of it's desire to dominate the US market. If you look into it you'll find that fabricated steel for major projects all across the US is coming from North of the border. Examples include stadiums and/or convention centers in Philadelphia, Detroit, Miami, Pittsburgh. I could go on.

While Canadian fabricators have certain advantages in being able to purchase cheap offshore raw material which is restricted by anti-dumping regulations from being shipped to the States, by far their biggest advantage is the overvaluation of the US dollar relative to their own currency. This makes the labor rates in their shops and drawing rooms 30 to 40% less than comparable rates in the States. The additional shipping costs for a load of steel traveling 400 miles in lieu of 200 miles is nominal. Our equipment is just as good, our workers just as productive, but we can't compete under these handicaps in an industry that averages less than 4% net income after taxes (as a % of sales), in good years! We expect many small family owned fabrication businesses, in the Northeast particularly, will not make it through the next few years without relief of some kind.

We appreciate your interest and beg for your assistance in bringing the exchange rate with Canada into a more realistic ratio.

Sincerely,

James A. Stori, PE
President

cc: Honorable Phil Gramm
Fax – 202-224-7391
Coalition for a Sound Dollar
sounddollar@nam.org

AISC ACTIVE MEMBER

SMITH AND WATERS, INC.
P. O. Box 570
Ware Shoals, SC 29692

APRIL 29, 2002

Honorable Phil Graham
Ranking Minority Member
Senate Banking Committee

Since the September 11, 2001 incident our business has been terrible in the trucking industry. I believe the economy is affected by the value of the dollar allowing the imports. We need a money policy that helps not hurts.

Thank you for your help.

Smith and Waters, Inc.

Danny Riddle
President

Forté, Dupee, Sawyer Co.

NOILS · WOOL · MOHAIR

4 MECHANIC STREET, SUITE 203
NATICK, MASSACHUSETTS 01760

TELEPHONE 508-653-2700, FAX 508-653-0998, E-MAIL: WOOL@FORTEWOOL.COM

April 29, 2002 VIA FAX: 202-224-2080

Honorable Paul Sarbanes
Chairman, Senate Banking Committee
Attn: Ms Laurie Better

Dear Senator Sarbanes:

It is my understanding that the Senate Banking Committee is scheduled to meet on May 1 to discuss the value of the US dollar.

The strong US dollar has had a terrible effect on my business as a result of many of my customers closing their mill operations and others idling machinery, laying off employees resulting in a great reduction in domestic demand for our scoured wool. As a result we have trimmed our work force in Boston by 70%, and the scouring plant in Brady, Texas has reduced its workforce by more than half.

To further compound the problem, the strong dollar has made it very difficult to export our scoured wool to users in other countries. The demand for our product in China and India is virtually without bound; however, the strong dollar has made our pricing uncompetitive.

I urge the Committee to please consider revising the Treasury's dollar policy to bring the value of the dollar back to normal levels.

Thank you for your consideration.

Sincerely,

William R. Forté, Jr.
President

Springfield LLC

Honorable Paul Sarbanes April 29, 2002
Chairman, Senate Banking Committee
ATT: Laurie Better

Honorable Phil Gramm
Ranking Minority Member, Senate Banking Committee

Coalition for a Sound Dollar

Dear Sir:

Springfield LLC. is a (3) three-year-old textile mill operation that employs about 300 people. The STRONG dollar has definitely contributed to the growth of imports of textiles and apparel. This is devastating the"textile" industry. The policy of maintaining an artificially STRONG dollar is a policy of economic destruction to segments of our economy. We urge the government to change Treasury's policy and to act quickly to bring the dollar back down to normal levels.

Leonard C Fishman
Sr. Vice President
Springfield LLC.

MOUNT VERNON MILLS, INC.
Cleveland Fabrics - Commerce Plant
P. O. Box 700 Commerce, GA 30529 (706) 335-3171 FAX # (706) [illegible]

April 29, 2002

Honorable Paul Sarbanes, Chariman
Senate Banking Committee

Attn: Laurie Better

I have recently been made aware that the Senate Banking Committee will soon be holding hearings to look at problems that are being caused by the strong dollar.

My understanding is that the value of the dollar has increased by 30 percent over the last five years. Obviously this puts manufacturers in this country at a strong disadvantage in both exporting goods and trying to compete against foreign imports.

As I am sure you are aware the U. S. textile industry of which our company is a part, was decimated during 2001 with 116 plants closing and 67,000 workers or 13% of the textile workers losing their jobs.

We are fortunate that our plant is continuing to operate, however, our work force in the last year has dropped from 230 to 110. In talking with people we have laid off many of them have had a tough time finding jobs comparable to the one they had here.

I am very fearful for the future of all manufacturing in our country if something is not done about the strength of the dollar. America is fast losing its strong manufacturing base which we have always had. If this trend continues it cannot help but seriously weaken our country and its economy.

Please, support American industry and workers who are still the world's most productive by working to have the strength of the dollar reduced to a level that will allow American industry to continue to lead the world which ultimately works for the good of every person in this country.

Thank you for your interest and concern.

Sincerely,

Brenda Puckett
Human Resources Manager

Johnny Klugh, Jr
Plant Manager

PARKDALE
P.O. DRAWER 1787
GASTONIA, NC 28053
704-874-5100
W. DUKE KIMBRELL
CHAIRMAN

April 29, 2002

The Honorable Paul Sarbanes
Chairman, Senate Banking Committee
Attention Laurie Better

Fax No. 202-224-2080

Subject: Senate Banking Committee Hearing May 1, 2002

As Chairman of the largest cotton yarn manufacturing corporation in the United States, I urge your prompt attention to the value of our currency as compared to the Asian currencies. For the first time in history, we have been required to shut down two mills because of the unfair competition from Pakistan, Indonesia, China and other Asian countries. Our mills are the most automated, computerized mills in the world, but we cannot be competitive even if our labor was completely eliminated because of the value of the dollar.

Since 1997, Asian currencies have all been devalued. It's time for us to cope with this currency differential or we are confronted with losing the manufacturing segment of the United States. I urge your immediate support.

In Gaston County, North Carolina, population approximately 145,000, we have had 19 manufacturing companies to default in the past two years costing in excess of 7,000 jobs – all because of foreign imports.

Sincerely,

Duke Kimbrell

Cattron Group Incorporated
140 West Shenango Street
Sharpsville, PA 16150
Tel: (724) 962-3578 Fax: (724-962-[illegible]

April 29, 2002

The Honorable Paul Sarbanes
Chairman, Senate Banking Committee
Attn Laurie Better
Room 534, Dirksen Senate Office Building
Washington, DC 20510

Dear Senator Sarbanes:

We are a small business located in Northwestern Pennsylvania, founded in 1946. At our location in Sharpsville (Mercer County) we design, manufacture, market and service remote control equipment for industrial equipment such as cranes and locomotives. In the mid 80's we began making export sales, and in the early 1990's we sought to increase our market opportunities by setting up operations in foreign countries to satisfy our customers' needs. In our global economy, more and more of our large customers, have global operations and need to deal with a supplier who can supply them with products and technical services worldwide. We currently have operations in five foreign locations – Canada, UK, South Africa, Brazil, and Germany.

Results in the early years of our experience were very encouraging, with export sales increasing and the foreign entities performing above expectations. However, as the dollar strengthened, these operations have found it more and more difficult to compete because they purchase virtually all their engineering of services and goods from our manufacturing facility in Sharpsville, Pennsylvania. Even though their cost may be the same, a domestic manufacturer, or one from a country with a weak currency, can offer equipment at a much lower price and still make a profit.

This has caused our international sales to fall, resulting in fewer orders to the US plant, and fewer workers needed in Pennsylvania to supply our foreign affiliates. In addition, the sales that are made are at a much lower profit margin, allowing little or no profits to be brought back to the US parent company.

Since they must buy from us in US dollars, last year our Brazilian and South African operations had translation losses equal to 43% of their sales volume. These two regions have some of the highest potential for industrial development and sales, but obviously, it is impossible to develop a foreign affiliate with these costs. In addition to giving up valuable opportunities for future growth, if we are forced to close these operations we will see immediately reduction in manpower needs (employment levels) in Pennsylvania.
We need your action to stop this cycle and strongly urge you to:

- State publicly the dollar is out of line with economic fundamentals
- Stop giving the impression we are happy with the dollar, no matter how strong
- Commit to cooperate with other major countries to ensure that market forces can work to bring about more realistic exchange rates.

Respectfully,

James C. Robertson
President and Chief Operating Officer
Cattron Group Inc.

dem

cc: Senator Phil Gramm
Senator Arlen Spector
Senator Rick Santorum
Congressman Phil English
Coalition for a Sound Dollar

The Honorable John W. Douglass
President and Chief Executive Officer

April 29, 2002

The Honorable Paul Sarbanes
Chairman, Senate Banking, Housing and Urban Affairs Committee
Dirksen Senate Office Building, Room 534
Washington, DC 20510

Dear Chairman Sarbanes,

On behalf of the Aerospace Industries Association (AIA) and its member companies, I am writing to express our appreciation for your committee's hearings on the release of the Treasury Department's Foreign Exchange Report and to encourage you to seek ways to address problems of what we believe to be an overvalued U.S. dollar. The AIA represents the nation's major manufacturers of commercial, military and business aircraft, helicopters, aircraft engines, missiles, spacecraft, materiels, and related components and equipment (see attached list).

The export market is essential to the U.S. aerospace industry. Last year, American aerospace manufacturers generated more than $144 billion in sales, with nearly $60 billion in exports. In particular, 63 percent of our commercial products are sold to foreign customers. However, a rather significant drop in our export surplus has coincided with the U.S. dollar appreciation. The U.S. aerospace industry surplus (exports less imports) totaled $41 billion in 1998 and has declined steadily since - falling below $26 billion last year. A sound dollar policy adopted by the U.S. government could reverse this negative trend.

Because European competitors of the U.S. aerospace industry price their goods in dollars, but pay their vendors and suppliers in a local currency that is undervalued relative to the dollar, they have the ability to undercut the prices of U.S. aerospace products. Furthermore, aerospace products are not as fungible as other durable goods, and once a customer buys a particular class of aircraft from one supplier, it is unlikely to change suppliers for future purchases of similar aircraft. Hence a misalignment of the dollar in our industry can have a ripple effect for two decades or more. As long as the dollar continues to be overvalued, U.S. aerospace manufactures will lose market share and therefore jobs to competitors overseas.

Thank you again for addressing these currency issues. Our association would be pleased to work with you and your committee staff in any way possible.

With warmest regards,
and very Respectfully
John
John W. Douglass

AEROSPACE INDUSTRIES ASSOCIATION

AIA Member Companies

AAI Corporation
The Aerostructures Corporation
Alliant Techsystems Inc.
American Pacific Corporation
Analytical Graphics, Inc.
Areté Associates
Argo-Tech Corporation
Atlantic Research Corporation
Aviall, Inc.
BAE SYSTEMS North America Inc.
Ball Aerospace & Technologies Corp.
Barnes Aerospace
B.H. Aircraft Company, Inc.
The Boeing Company
Computer Sciences Corporation
Cordiem, LLC
Crane Aerospace
Cubic Corporation
Curtiss-Wright Corporation
Curtiss-Wright Flight Systems, Inc.
Metal Improvement Company
Dassault Falcon Jet Corporation
Davis Tool, Inc.
DRS Technologies, Inc.
Ducommun Incorporated
DuPont Company
EDO Corporation
Embraer Aircraft Corporation
Esterline Technologies
Exostar LLC
Fairchild Dornier Corporation
Fairchild Fasteners
GenCorp
General Atomics Aeronautical Sys. Inc.
General Dynamics Corporation
General Electric Company
GKN Aerospace Services
Goodrich Corporation
Aerostructures & Aviation Technical Svcs.
Electronic Systems
Engine and Safety Systems
Landing Systems
Groen Brothers Aviation, Inc.
Harris Corporation
HEICO Corporation
Hexcel Corporation
Honeywell
i2 Technologies
ITT Industries
Defense and Electronics
Kaman Aerospace Corporation
Kistler Aerospace Corporation
L-3 Communications Holdings, Inc.
Lockheed Martin Corporation
Martin-Baker America Inc.
MatrixOne, Inc.
MD Helicopters, Inc.
MOOG Inc.
Northrop Grumman Corporation
Omega Air, Inc.
Orbital Sciences Corporation
Advanced Systems Division
Parker Aerospace
The Purdy Corporation
Raytheon Company
Rockwell Collins, Inc.
Rolls-Royce North America Inc.
Smiths Aerospace Actuation Systems
Los Angeles
Space Access, LLC
Spectrum Astro, Inc.
Swales Aerospace
Teleflex, Inc./TFX Sermatech
Mal Tool & Engineering
Textron Inc.
Triumph Group, Inc.
TRW Inc.
United Defense
United Technologies Corporation
Hamilton Sundstrand
Pratt & Whitney
Sikorsky
Vought Aircraft Industries, Inc.
W.L. Gore & Associates
Woodward Governor Company

MOUNT VERNON MILLS, INC.
Apparel Fabrics Group - Alto Fabric Plant
P.O. Box 649 Alto, GA 30510 (706) 778-2141 FAX # (706) 776-5394

April 29, 2002

Honorable Paul Sarbanes, Chairman
Senate Banking Committee

Dear Honorable Sarbanes:

I am the General Manager of Greige Manufacturing for Mount Vernon Mills, Inc., a textile company that employees 5,700 people in Georgia, South Carolina, Alabama, Mississippi, Texas and California. I am very concerned about the negative impact our textile industry has had to endure for the last six years. Mount Vernon has always been a very strong company financially and in every business sense, but even we have been hurt in recent years by governmental decisions that are hurting all manufacturing in the U.S.

The strong dollar policy is destroying the manufacturing structure of the U.S. We in textiles have seen very strong companies being forced to lay off people and shut down plants. In the last year, 116 textile mills have shut down and 67,000 workers terminated. At Mount Vernon, we have seen profits plummet and schedules drastically reduced resulting in about 10 percent of our workforce being terminated.

I strongly urge the current administration to reverse the strong dollar policy so foreign countries will not be given an unfair advantage in competing in our domestic market place. All we want is an even playing field in which to compete. This means honoring trade agreements, preventing transshipments, fair currency policy, and legislation that doesn't always help the foreign countries. The United States of America cannot support the whole world. We need to protect our own economy, so it will be as strong in the future as it has been in the past.

Your support is desperately needed to reverse the administrations' strong dollar policy.

Sincerely,

Larry Porter

Larry Porter
General Manager
Greige Fabrics

Apparel Fabrics Group – Alto Fabric Plant
P.O. Box 649 Alto, GA 30510 (706) 778-2141 FAX # (706) 776-

April 29, 2002

Honorable Paul Sarbanes, Chairman

Dear Honorable Sarbanes:

I am the Human Resources Manager of the Alto Fabric, Alto Yarn, Cleveland and Commerce Plants for Mount Vernon Mills, Inc., a textile company that employees 5,700 people in Georgia, South Carolina, Alabama, Mississippi, Texas and California. I am very concerned about the negative impact our textile industry has had to endure for the last six years. Mount Vernon has always been a very strong company financially and in every business sense, but even we have been hurt in recent years by governmental decisions that are hurting all manufacturing in the U.S.

The strong dollar policy is destroying the manufacturing structure of the U.S. We in textiles have seen very strong companies being forced to lay off people and shut down plants. In the last year, 116 textile mills have shut down and 67,000 workers terminated. At Mount Vernon, we have seen profits plummet and schedules drastically reduced resulting in about 10 percent of our workforce being terminated. We are currently facing the termination of approximately 100 people in our Alto Yarn Plant alone in June of this year. This is quite devastating to these people.

I strongly urge the current administration to reverse the strong dollar policy so foreign economics will not be given an unfair advantage in competing in our domestic market place. All we want is an even playing field in which to compete. This means honoring trade agreements, preventing transshipments, fair currency policy, and legislation that doesn't always help the foreign countries. The United States of America cannot support the whole world. We need to protect our own economy, so it will be as strong in the future as it has been in the past.

Your support is desperately needed to reverse the administrations' strong dollar policy.

Sincerely,

Shirley B. Wilkinson

Shirley B. Wilkinson
Human Resource Manager

MOUNT VERNON MILLS, INC.
P. O. BOX 649
ALTO, GA. 30510
(706) 778-2141
(706) 776-5394 FAX

April 29, 2002

Honorable Paul Sarbanes
Chairman, Senate Banking Committee
Washington, D.C.

Dear Chairman Sarbanes:

On March 28, 2002, an announcement was made that we were losing 104 jobs at the textile plant, where I have been working for 17 years. Previously I had worked for another textile company in this area, and in 1985 it closed its doors and 350 people were suddenly out of a job. Some of the people who are losing their jobs in June do not understand what is happening, and due to other textile related closings in this same community, will find it difficult to find employment elsewhere without moving away.

There are many reasons our textile jobs are being eliminated. First there was the flood of imports, the unfair trade bills where we as an industry have been "sold out", the loss of major export markets, the smuggling of goods into this country, and now the dollar has become terribly overvalued. Our industry has been devastated! Now the dollar's relentless rise has become a key factor in plunging an already "injured" industry into its worst economic crisis since the Great Depression.

It is time that you, the leaders of this nation, take a strong stand to support an industry that has traditionally supported this great nation of ours. It is my understanding that Treasury Secretary Paul O'Neill is committed to a "strong dollar policy". PLEASE STOP HIM! This could mean as many as 1,000,000 people will lose their jobs, and this is not fair to our industry and the people who will be unfairly forced out of their jobs.

Thanks for taking the time to read my plea, and I will be counting on you representing my views on May 1.

Sincerely,

Gail Bell
Mount Vernon Mills, Inc.

MINSTER.
THE MINSTER MACHINE COMPANY

JOHN J. WINCH
PRESIDENT

April 29, 2002

The Honorable Paul Sarbanes
Chairman, Senate Banking Cte.
Attn: Laurie Better
Room 534, Dirksen Senate Office Building
Washington, DC 20510

Dear Senator Sarbanes:

I am writing to you to express my concerns regarding the value of the U.S. dollar. We are a 106-year old domestic manufacturer of machinery and have exported machines to over 62 countries throughout the world. Over the past two years, we have been dealt a double blow. First by the recession in manufacturing/capital goods and then by the 30% premium on the dollar. Our exports have dropped from an average of 30% of sales to less than 10%. Our annual revenues are off over 50% and we have reduced our workforce from approximately 1000 to 300 people. We have great people that make great products-but at a 30% (dollar based) cost disadvantage to the Canadians, Europeans and Japanese-we find it very difficult to compete.

Please take action so that we do not lose all of our manufacturing base and capabilities to foreign markets.

I appreciate your time and consideration to this plea. Please feel free to contact me at 419-628-2331 to further discuss this situation.

Sincerely,

John J. Winch
President

cv

pc: The Honorable Phil Gramm

78 Congress Circle West
Roselle, IL 60172-3911
(630) 351-7676
Fax (630) 351-9958
Website:
www.arometal.com

Tooling

Stamping

Assembly

Engineering

ISO 9002 Certified

April 29, 2002

The Honorable Paul Sarbanes
Chairman, Senate Banking Cte.
Attn: Laurie Better
Room 534, Dirksen Senate Office uilding
Washington, DC 20510

RE: Hearing on the Dollar Valuation

Dear Senator Sarbanes:

I'm writing to express my view on the current value of the dollar and how it impacts my small manufacturing business. Over the last few years the dollar has risen over 30% against foreign currencies. Here is how that impacts my business:

- I've had to layoff 25 people in the last 18 months. That is nearly 50% of my workforce.
- My sales are down 40% from what they were just 2 years ago.
- Many of my customers are going to off-shore suppliers (some European, some Asian) for the same items they used to purchase from me. Even in cases where I can manufacture the product at a lower cost, by the time they factor in the exchange rate, it is cheaper to buy from the foreign source.
- More importantly, many of my customers are moving entire product lines off-shore for the same reason.

I'd like to see the administration and the Congress state publicly that the dollar is over-valued when looked at in terms of economic fundamentals.

I'd like to see a commitment to working with other countries to ensure that market forces can bring about more realistic exchange rates.

The administration needs to stop giving the impression that it is happy with the dollar no matter how strong. By doing that, they ignore the devastating damage done to manufacturers and others.

Thank you for considering my comments.

Respectfully,

Tony Dandequie
President
Aro Metal Stamping Co., Inc.

AVONDALE
AVONDALE MILLS, INC.
GRANITEVILLE FABRICS
133 Marshall Street
Graniteville, S.C. 29829

April 29, 2002

Honorable Paul Sarbanes, Chairman,
Senate Banking Committee

ATT: Laurie Better
Fax: 202/224-2080

Dear Senator Sarbanes:

I am writing in regards to the Senate Banking Committee's Congressional hearing on the overvalued dollar scheduled for Wednesday, May 1.

You have probably already received mail on this important issue; however, I also wanted to voice our opinion on the devastation that our Treasury Department's "strong dollar" policy is causing to our textile companies and also to other U. S. companies and workers.

My Company has felt the impact of low-priced Asian imports, and we have had to close several of our plants, in addition to laying off workers. Our communities have been affected due to these shutdowns and layoffs. We have lost thousands of dollars.

As a textile employee, I URGE you to use your input in changing the Treasury's d[illegible] policy and to act quickly in order to bring the dollar back down to normal levels.

Respectfully,

M. S. Bonner

M. S. Bonner,
Executive Vice President

Neuwer Tool Corporation

Phone 847-392-0110
Fax 847-392-1048

April 30, 2002

The Honorable Paul Serbanes
Chairman, Senate Banking Cte.
Attn:Laurie Better
Room 534, Dirksen Senate Office Building
Washington, DC 20510

Dear Honorable Serbanes,

In the past 2 years my exports of finished product have dropped by 100%. We used to do about $30,000 a years with several companies in Canada. But with the vast difference in the exchange rate we are no longer doing that. I fully believe that if the American dollar were to be devalued I could regain that business. Not only would I regain that business but I would be able to hire back the people that I had to lay off due to lack of work.

Yours truly,

Joe Wersching

April 30, 2002

The Honorable Paul Sarbanes
Chairman, Banking Committee
of the United States Senate
Room 534, Dirksen Office Building
Washington, D.C. 20510

Attention: Laurie Better

Dear Senator Sarbanes:

It is our understanding that the Senate Banking Committee has scheduled hearings on the Overvalued American Dollar on May 1st and that key members of the Administration will be called to testify, including Treasury Secretary Paul O'Neill.

We wish to be on record that we strongly object to a government policy that favors a strong dollar.

Diamond Packaging is a regional manufacturer of packaging made from paperboard selling primarily to Fortune 500 customers as well as international customers. We have lost two bids in the last year totaling in excess of $6,000,000 due directly to the current overvalued dollar. The bids were awarded to foreign corporations. The result of these lost bids is that we have had to lay off approximately 5% of our workforce. Had we been successful in winning the bids it would have more than made up for the lower sales that resulted from the economic slowdown being experienced.

In addition, we urge the U.S. government to commit to cooperating with other major countries to ensure that market forces can work to bring about more realistic exchange rates.

We look to you and your committee to help set an agenda for resolving this issue.

Sincerely,

James W. Stenger
Vice President – Finance & CFO

C: H. Voss
E. Voss
L. Palvino

FALCON STEEL CO.

• FORT WORTH
• KAUFMAN
• LUBBOCK

POST OFFICE BOX 162589 • FORT WORTH, TEXAS 76161-2689 • (817) 581-9500

April 30, 2002

Subj: Sound Dollar Coalition

Fax: 202-224-2080
The Honorable Paul Sarbanes
Chairman, Senate Banking Cte.
Room 534, Dirksen Senate Office Building
Washington, DC 20510

Dear Mr. Sarbanes;

Please register our support for the views of the "Coalition for a Sound Dollar".

Since our Federal Government has given the "green light" to companies in Mexico and Canada to raid our markets, imports have gained a significant share of the electrical transmission tower business in the United States, particularly in Texas, California, Ohio, and Michigan.

The largest contract awarded in the last 12 months went to a Mexican Company.

The last time we bid in the world market (Philippine job), our bid was beaten so bad it looked like we weren't bidding the same project as the Korean companies. Puerto Rico results are similar.

It is hard to compete against Mexican and Asian labor costs, particularly with an over-valued dollar.

Your consideration of this situation is respectfully requested.

Yours very truly,
FALCON STEEL COMPANY

J. L. Milligan,
Chairman

MULLEN INDUSTRIES

April 30, 2002

The Honorable Paul Sarbanes
Chairman, Senate Banking Cte.
Attn: Laurie Better
Room 534, Dirksen Senate Office Building
Washington, DC 20510

Dear Senator Sarbanes,

I am part of a small machining company located in St. Clair Missouri. Within the last couple of years there has been much competition to keep our type of machine parts manufactured in the U.S. This is due in part to the strong dollar, which definitely gives the advantage to the importing countries. The second disadvantage was the recent tariff placed on the imported steel that we have to use to compete with those overseas companies that make these same type of precision machine parts, and ship into the U.S.

You are in a position to help this situation with regards to the dollar. I am not sure how long small businesses in our line will be able to keep going if we are going to be afforded a level playing field but it is a real struggle. We are competing worldwide, and from our vantage point this is an uphill battle with all of the cards stacked against us.

I believe that your committee must:
Recognize the dollar is out of line with the economic fundamentals.
Don't continue to give the impression that everything is okay with dollar no matter how strong.
Make a commitment to cooperate with other major countries to ensure that market forces can work to bring about more realistic exchange rates.

For the sake of our small operation and others in the United States please direct your attention to the above.

Sincerely,
Ken Grothoff
Ken Grothoff
Executive Vice President

DIEBEL MANUFACTURING
6505 OAKTON STREET / MORTON GROVE, ILLINOIS 60053
P.O. BOX 459
847/967-5578 / FAX: 847/967-0666
WWW.DIEBEL.COM

April 30, 2002

The Honorable Paul Sarbanes
Chairman, Senate Banking Cte.
Attn: Laurie Better
Room 534, Dirksen Senate Office Building,
Washington, DC 20510

I am the president of a metal stamping company called Diebel Manufacturing Co. We are located in Morton Grove, IL. We are currently under a threat from foreign competition to lose over 20% of our business due to pricing. If the dollar was not overvalued we would not have this threat. Please focus on interest rates to weaken the dollar. I urge the government to state publicly that the dollar is out of line with economic fundamentals. The government should stop giving the impression that it is happy with the dollar no matter how strong it gets. The government should commit to cooperating with other major countries to ensure that market forces can work to bring about more realistic exchange rates.

Sincerely,

Rohn A. Schaefer
President
Diebel Manufacturing Company
6505 West Oakton Street
Morton Grove, IL 60053

Fax To: 202-224-2080

The Honorable Paul Sarbanes
Chairman, Senate Banking Committee
Attn: Laurie Better
Room 534, Dirksen Senate Office Building
Washington, DC 20510

Dear Senator Sarbanes:

The soaring value of the U.S. dollar over the last several years has adversely affected manufacturing companies like my firm, Nu-Way Industries, Inc., along with many others in the farming and service industries.

The devastating impact of the decline in U.S. exports, over $140 billion in the last 18 months, is largely because of the overvalued dollar. And, this situation has caused at least 500,000 U.S. factory workers to lose their jobs, including about 100 people at our company. Plus, you also need to consider the thousands of additional jobs lost in the farming and service areas.

We have recently explored contractual relationships which would enable us to produce products in other countries. However this was not a matter of choice, but a matter of necessity. We would prefer to bolster manufacturing and jobs here in the U.S., as has been our privilege for over 30 years of operation. However, without your support and assistance, this is not possible. I urge you to work aggressively with your associates to forge a plan with other major countries that insures that market forces work to bring about more realistic exchange rates.

This action is essential to revitalizing the U.S. manufacturing sector and to restoring the hundreds of thousands of lost jobs. Please do all you can to contribute to this most important undertaking.

Sincerely,

Steve Southwell
President

The Honorable Paul Sarbanes
Chairman, Senate Banking Cte.

Attn: Laurie Better
Room 534, Dirksen Senate Office Building,
Washington, DC 20510

SUBJECT: SENATE BANKING COMMITTEE HEARINGS
"THE OVERVALUED AMERICAN DOLLAR"
POSITION: Strongly in Favor of Adjusting the Dollar to Appropriate Value

Dear Senator Sarganes;

On May 1, the Senate Banking Committee will be holding crucial hearings with Treasury Secretary O'Neill and many industry leaders on the valuation of the American dollar. There could not be may economists who would seriously argue that the dollar is not substantially overvalued at this time. We have just gone through 12-14 months of recession during which the dollar actually gained strength. I have lived through a score of recessions and can not recall this situation having ever occurred.

My company manufactures industrial cutting tools. For the past 5 years the strengthening dollar has dramatically raised the price of my products in relation to those imported by my European (mostly German) competitors. In order to remain competitive we have been force to decrease the percentage of products we manufacture by 25% and increase the percentage of products we import by like proportion. This has resulted in the loss of approximately 125 manufacturing jobs in our company. The greatest single impact on this trend is the overvalued dollar.

I urge you to take action to move the dollar toward more appropriate valuation based on economic fundamentals. This will require a decrease in valuation of between 20-25%.

Sincerely,

John M. Segal

John M. Segal
President

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"More Than Just A Cutting Tool"

NORTH AMERICAN PRODUCTS
1180 Wernsing Road – P.O. box 647 – Jasper, IN 47546-0647
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NORTH AMERICAN
TOUGH CUTTING TOOLS

Steven A. Segal, Chairman

The Honorable Paul Sarbanes

Chairman, Senate Banking Cte.

Attn: Laurie Better
Room 534, Dirksen Senate Office Building,
Washington, DC 20510

ISSUE: The U.S. dollar has soared nearly 30 percent over the last few years and is badly hurting U.S. manufacturing, farmers, and many service workers.

Dear Senator Sarbanes:

The artificially strong dollar is having a devastating affect on the productive capabilities of the United States. In the past 18 months alone U.S. exports have dropped $140 billion basically because of the overvalued dollar, and at least 500,000 U.S. factory workers have been unemployed by this development – 2/5 of the entire loss in U.S. factory jobs.

Our manufacturing company employed 555 people in January of 2000. Our present level of employment stands at 399 jobs. In May of 2001 the Germans dropped the price of circular carbide tipped saw blades they import into U.S. industry by 25% to 30%. Our saw blade sales dropped 20% in June of 2000..

The situation is not isolated and unknown as is oblivious by the following quotes from very influential people:

- *"The dollar is overvalued, and everybody knows it," -- Joachim Fels, currency expert at Morgan Stanley*
- *"There are significant risks to the sustainability and durability of the upturn in the United States and elsewhere, ...notably the large U.S. current account deficit and ...the overvaluation of the dollar..." – International Monetary Fund World Economic Outlook, April 2002*

In the 38 years I have been running this company our sales and employment has always grown. We are fighting hard to regain that tradition of expanding employment and opportunity for our people and our community. Please help us by addressing the over valued dollar. Please help us compete in this new world economy. Give us a level playing field – we'll do the rest!

Yours truly,

Steven A. Segal, chairman

PHONE 423-764-6127 FAX 423-764-6241
P. O. BOX 919 BRISTOL, TENNESSEE 37621 OR 1320 GEORGIA AVE. BRISTOL, TENNESSEE 37620

MANUFACTURERS OF HIGH QUALITY GLUED-UP DIMENSION AND WOOD PARTS FROM APPALACHIAN HARDWOODS

April 30, 2002

The Honorable Paul Sarbanes, Chairman, Senate Banking Cte.
Attn: Laurie Better
Room 534, Dirksen Senate Office Building
Washington, DC 20510

Via Fax: (202) 224-2060

Dear Senator Sarbanes:

Cortrim manufactures wood parts for the furniture industry and it's own line of wood burial caskets and cremation urns. I am still struggling to survive but Cortrim has filed under Chapter 11 of the Bankruptcy code because foreign trade has literally stolen my business.

The fact is that the United States has given foreign manufacturers advantages over Cortrim in many ways. We must comply with myriad regulations and provide numerous benefits which our foreign competitors just don't have. Additionally, we are contending with a grossly overvalued US currency and foreign competitors who deliberately use the exchange rate as a crutch in order to displace American businesses and jobs.

America runs the best-managed forests in the world. The quality and integrity of our wood products are second to none, but Cortrim can't sell wood products because our markets are flooded by cheap foreign products. Most large American furniture manufacturers have moved their factories to China and Malaysia or sought out sources for wood parts in those countries. My casket markets have been raided by cheap Canadian imports. I just can't beat the 30% exchange rate advantage they enjoy over my products.

My company is an 86-year-old, 4-generation wood products manufacturer in Bristol, TN. This past year, I have watched in desperation as my markets disappear, my company is drained of nearly a century of assets and dignity, and as 170 of my good people lost their jobs.

Please sir, won't you give us a fighting chance? Will you admit that the dollar is out of line with realistic economic fundamentals and commit to bringing about more realistic rates?

Sincerely,

Robert D. Spiegle Jr.

Robert D. Spiegle Jr.
President

PARKDALE
P.O. DRAWER 1787
GASTONIA, NC 28053
® 704-874-5100
ANDERSON D. WARLICK
PRESIDENT
CHIEF EXECUTIVE OFFICER

April 30, 2002

The Honorable Paul Sarbanes
Chairman, Senate Banking Committee
Attn: Laurie Better
Fax No. 202-224-2080

Dear Senator Sarbanes:

As a manufacturer in the United States, I am finding it very difficult to remain in business with the value of the U.S. dollar. We have closed two (2) plants as a result of inexpensive Asian imports, and, if currencies around the world continue to depreciate themselves against the dollar, we will be forced to shut down additional manufacturing and move remaining investments to foreign countries that routinely subsidize their manufacturing industries. If the intent of the Administration is to eliminate manufacturing in this country, please let me know so that we can have as orderly of a liquidation of our company as possible.

I do not understand why the Treasury allows the U.S. dollar to be manipulated for foreign governments' gain. I have never seen what I believe is more economic treason than what is being practiced by the Treasury. If I look at the U.S. economy and look at the profits of corporations other than banks, I would say the Treasury is doing a miserable job. If the objective is to transfer wealth from the masses into a few individuals, I would say they are doing a great job.

Sincerely,

Anderson D. Warlick

ALICE MANUFACTURING COMPANY, INC.
P.O. BOX 369 EASLEY, SOUTH CAROLINA 29641 • 864-859-5323

E. SMYTH MCKISSICK III
PRESIDENT

April 30, 2002

The Honorable Paul Sarbanes
Chairman, Senate Banking Committee

Attn: Laurie Better

Dear Mr. Sarbanes:

I am the CEO of a mid-sized fabric and home products producer in Easley, S.C. We have four modern manufacturing plants, and with approximately 1450 associates, we are among our region's largest employers.

Our country's "overvalued dollar" policy has been absolutely devastating to the U.S. textile industry. Even though our plants are "ultra modern" and among the most productive in the world, we are losing market share to "sub-standard" producers who are receiving incredible pricing advantages due to the overvalued dollar. Also, our export business is being negatively impacted.

Please take the necessary actions to bring the dollar down to a more historically normal level before we destroy the entire manufacturing base of our country.

Thank you.

Sincerely,

E. Smyth McKissick III

cv

NTMA PRECISION

National Tooling & Machining Association

9300 Livingston Road, Ft. Washington, MD 20744-4998 (301) 248-6200
(800) 248-[illegible]
Fax: (301) 248-7104
http://www.ntma.org

April 30, 2002

The Honorable Paul Sarbanes
Chairman, Senate Banking Committee
Attn: Laurie Better
Room 534, Dirksen Senate Office Building,
Washington, DC 20510

Dear Mr. Chairman:

On behalf of the 2,500 member companies that comprise the National Tooling and Machining Association, I want to thank you for scheduling a hearing to examine the continued overvaluation of the dollar.

The U.S. tooling and machining industry is primarily a family-run industry, often two or more generations work at the same plant. This is not to say we are the local mom and pop shop on the corner. Many in our industry operate the latest technology and high levels of automation. They must do this because highly customized products are created and to produce them we must consult directly with the customers and make critical decisions to keep the manufacturing process on the right track and within budget.

A solid economy is dependent on the success of the tooling and machining industry. Nearly every manufacturing company in the country, in the world, does business with our industry. The U.S. tooling and machining industry employs close to 450,000 people nationwide and accounted for shipments in excess of $43 billion. The metalworking industry includes precision machinists, die makers, mold makers, as well as tool and die designers. Without them, the mass production of manufactured goods would not be possible.

The U.S. has been experiencing severe economic hardships this past year. The nation's tooling and machining industry is bearing the brunt of these problems. Orders by U.S. companies for machine tools fell in November to lower levels than during the recession years of 1980-81, underscoring the weakness in manufacturing. Bookings for U.S.- and foreign-made tools fell 16.6 percent to $156.2 million for the month. That surpassed a two-decade low of $181.4 million in July. In August we hit our 14th month of negative growth

NTMA believes that a sound dollar is a fundamental pre-requisite for the difficult climb out of this recession as well as maintaining a healthy U.S. and global economy. A sound dollar is one whose value relative to other major currencies is determined by

market forces that reflect fundamental economic trends, such as trade balances, interest rates, GDP growth and other objective indicators of a country's performance.

The disturbing reality is that for several years the dollar has not been reflecting economic fundamentals. Since 1997, the dollar has risen by 25-30% relative to a basket of major world currencies. The dollar is now at a sixteen year high and is approaching the overvaluation of the mid-1980's.

The overvalued dollar is effectively subsidizing our foreign competitors. Despite concerns over quality and delivery, Asia and Canada have emerged as significant competitors to our precision machining and mold makers. As a result, a Canadian mold maker can essentially offer the same product for 30% less than an American mold maker based on the currency exchange alone.

NTMA firmly believes that sound currency values can be restored and that manufacturing can again thrive in this country. To do this, the Treasury should:

- State publicly that the dollar is out of line with economic fundamentals;

- Firmly state that its policy is to seek a market-determined dollar that is consistent with underlying global economic fundamentals, including the competitiveness of America's farms and industries;

- Seek cooperation with other major economies in obtaining common agreement and public statements that their currencies need to appreciate against the dollar; and

- Make clear that the United States will resist, and take offsetting action as necessary, foreign country interventions designed to retard movement of currencies toward equilibrium

The overvalued dollar is a serious threat to the economic viability of our industry. Urgent and effective action to restore the U.S. dollar to a level, which reflects the underlying fundamentals, is essential to restoring a competitive U.S. tooling and machining industry.

Sincerely,

Shane C. Downey
Manager, Small Business Economic Development

PLATTSBURGH, NY
POTSDAM, NY
WILLISTON, VT

April 30, 2002

The Honorable Paul Sarbanes
Chairman, Senate Banking Cte
Attn: Laurie Better
Room 534, Dirksen Senate Office Building,
Washington, DC 20510

The Honorable Phil Gramm
Ranking Minority Member, Senate Banking Cte.
Room 534, Dirksen Senate Office Building,
Washington, DC 20510

Subject: Overvalued Dollar

Dear Representative:

Jeffords Steel and Engineering has two locations in upstate New York and one in Vermont, serving the needs of the Steel Industry through Steel fabrication and design. We are deeply concerned about the strong dollar as it relates to other currencies, especially Canada.

The large disparity between the Canadian and US dollar continues to create unfair competition for us as a US Fabricator versus a Canadian Fabricator. These fabricators from across the border are delivering steel to our customers at a 40% discount. We are finding it practically impossible to compete in the highly competitive bid market for major jobs in the local market (a recent bid showed three US fabricators within $20,000, while a Canadian was $200,000 less). This includes Schools, Hospitals, and community buildings that our tax dollars help support. Canadian Fabricators do not pay Workman's compensation and the Government pays for Health insurance. With the Canadian Fabricators beating our pricing by 40%, will we continue to have jobs for our employees in the near future? These are the same employees that are supplying the tax base for local construction and who also support the local economy.

Over the years this company has prospered and grown while making major purchases to support its operation. This medium size business is very proud of its state of the art facility that is as efficient as any operation in North America. This was developed by a management style that is aggressive, yet responsible, while creating a strong customer base. Having owned and operated this business since 1985, we are deeply concerned about its future unless some restrictions are imposed on the Canadian competition, we must insure that we are competing on a level playing field. Some form of dollar devaluation must be imposed to protect our industry and similar industries from this migration of business to the north.

You must review the state of the strong dollar to ensure that exchange rates will allow us to maintain our work force and our business without jeopardizing our future in this industry.

Jeffords Steel and Engineering Company,

Larry Jeffords
President

Cc; Coalition for a Sound Dollar

April 30, 2002

To Whom It May Concern:

I would like to take this time to encourage the government to change Treasury's dollar policy. I have been in textiles for twenty years, my entire career. As a concerned plant manager of three of local textile plants, I have never experienced the industry in such turmoil as it currently is in.

We have three plants supplying yarn to the apparel industry. We normally operate seven days a week and employ over 500 employees. Due to the dramatic increase of imports (primarily Asian) and the declining export markets, we have recently experienced down sizing in our company. The strong American dollar compounds this problem. Not only have we experienced numerous weeks of curtailment because of this, but we have also reduced the total number of employees by 25%. Several of our employees have maximized their unemployment benefits leaving them with no other source of income. This also has a snowball affect on the local economy. Local industries loose revenue as well as the utility companies.
Due to recent profit losses with in our company, we our now operating 6 of 18 original plants. For the above reasons solely, we have regrettably closed 12 plants. This has affected approximately 1500 people.

In closing, I would like to ask you again to please act quickly to bring the U.S. dollar to normal levels in order for our industry to remain competitive globally. We can not revisit the "Hoover Days" again in this country!

Respectfully,

Todd Gunter

Saurer Inc.

Honorable Paul Sarbanes
Chairman, Senate Banking Committee
Attn: Laurie Better

Fax: 202-224-2080

Re: May 1 Hearing on the Overvalued Dollar

Dear Senator Sarbanes:

As CEO of the five U.S. subsidiaries in the Saurer Group's Textile Systems Division, I have seen very directly the devastating effects of the rise of the dollar on the textile industry in this country and on its suppliers in the textile machinery sector.

The effects on our customers, the textile manufacturers in the United States, have been well documented. As Asian prices for textiles have dropped and imports risen dramatically, U.S. textile mills have closed, close to 200,000 textile jobs have been lost, companies have gone out of business, and the surviving textile manufacturers have been forced to relocate many facilities to lower-wage and lower-price countries.

As a direct effect, the five companies for which I am responsible have been forced to reduce staffs by half, dropping from a total of 300 employees to 150. These are not large numbers by comparison, but they are representative of ripple-effect losses being suffered by companies throughout the country.

I hope and trust that concern for the economy and the citizens of our country will guide you as the Senate Banking Committee addresses the Treasury Department on the policy that has been a major cause of the catastrophic decline of the manufacturing industry in the U.S.

I wish you and your committee success in finding solutions to these very real problems.

Sincerely,

Dan W. Loftis

Dan W. Loftis
President & CEO
Saurer Inc.

DWL/mm

cc: Senator Jesse Helms (202-228-1339)
Senator John Edwards (202-228-1374)
Coalition for a Sound Dollar (202-637-3182)

ACSA

1725 K Street, N.W.
Suite 1404
Washington, D.C. 20006

Phone (202) 296-7116
Fax (202) 659-5322

American Cotton Shippers Association

April 30, 2002

Hon. Paul S. Sarbanes, Chairman
Committee on Banking, Housing & Urban Affairs
United States Senate
Attention of: Laurie Better
Room 534, Dirksen Senate Office Building
Washington DC 20510
Fax (202) 224 2080

Re: Support for a $ound Dollar

Dear Chairman Sarbanes:

On behalf of the American Cotton Shippers Association I urge you and the members of your Committee to urge President Bush to establish a monetary policy that values the dollar at its long-term equilibrium level to encourage exports and to provide domestic manufacturing industries with the opportunity to compete against imports.

Interest of ACSA

ACSA was founded in 1924 and is composed of primary buyers, mill service agents, merchants, shippers, and exporters of raw cotton who are members of four federated associations located in sixteen states throughout the cotton belt:

Atlantic Cotton Association (AL, FL, GA, NC, SC, & VA)
Southern Cotton Association (AR, LA, MS, MO, & TN)
Texas Cotton Association (OK & TX)
Western Cotton Shippers Association (AZ, CA, & NM)

ACSA member firms handle over 80% of the U.S. cotton sold in domestic and export markets. In 2001-2002, domestic mills will consume approximately 7.3 million bales and almost 11 million bales will be shipped to foreign mills. Because of their involvement in the sale and shipment of cotton, ACSA members and their producer and textile mill customers are directly impacted by the monetary policy of the Administration. Therefore, any action taken by the Congress that will convince the Administration to change its harmful monetary policy will improve the economic and competitive climate faced by America's producers and textile manufacturers.

Detrimental Impact On US Textile Industry

The U.S. textile industry, one of the largest manufacturing sectors in the United States and a key partner with the cotton industry, has been devastated by the rise in the value of the dollar. In 2001, 116 textile mills were closed and 67,000 workers – 13% of the industry's workforce – lost their jobs. The start of the Asian currency crisis in 1997 began a 4-year cycle of deflation in U.S. textile prices that has resulted in a total loss of 177,000 textile jobs and 215 textile mill closings. Simply put, the dollar's continual rise has been a major contributor to the textile industry's worst economic crisis since the Great Depression.

In 1997, at the outset of the Asian Financial Contagion our domestic textile mills were consuming 11.4 million bales of raw cotton produced in the United States. In contrast, the domestic consumption of U.S. cotton has now dropped to 7.3 million bales – a decrease of 4.1 million bales or 35.5%, an amount equal to the total production last year in Texas, our most productive cotton producing state.

Before the dollar's rise, the textile industry was thriving with industry fiber consumption at a record 17 billion pounds, industry shipments at a record $84 billion, capital expenditures at a near record $2.7 billion, and textile exports at a record of almost $17 billion. Regrettably, since 1997 the dollar has appreciated in value by an average of 40% against the currencies of the top ten Asian textile–exporting countries and also against the euro and the Canadian dollar. This has destroyed the competitive structure of the industry and caused a major import surge while collapsing major export markets. Textile exports to Asia have dropped 26% and exports to the European Union (EU) are down 27% since 1997. Finally, exports to Canada and Mexico fell 8% and 13% respectively last year.

The American Cotton Shippers Association urges the Congress and the Administration to work to lower the value of the dollar, which will serve to level the playing field not only for the U.S. textile industry, but for all other manufacturing industries that are vital to our nation's economic well-being.

Respectfully Submitted,

Neal P. Gillen,
Executive Vice President &
General Counsel

PACKAGING MACHINERY MANUFACTURERS INSTITUTE

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April 30, 2002

The Honorable Paul Sarbanes
Chairman, Senate Banking Committee
ATTN: Laurie Better
Room 534, Dirksen Senate Office Building
Washington, DC 20510 VIA FACSIMILE: 202-224-2080

Dear Senator Sarbanes:

The Packaging Machinery Manufacturers Institute (PMMI) represents 512 original equipment manufacturers in the United States and Canada. More than 65% of these companies have revenues of less than $10 million a year. Just under 85% of them export machinery to European Union countries, Mexico, Brazil, China and other areas around the world.

PMMI members are at a competitive disadvantage internationally due to the United States' strong dollar policy. In some cases their prices are 20-30% higher than the local competition, simply because of the strong dollar.

As a result, PMMI has seen the packaging machinery trade imbalance grow to $248 million, up 37% from 1998. In addition, PMMI members' exports have dropped 20% from their high in 1998, to $849 million.

Companies cannot continue to be active exporters in the face of the artificially imposed "tariff" that the strong dollar creates.

Please support PMMI member companies, and other companies facing the same issue, by stating publicly that the dollar is out of line with economic fundamentals. And please commit to cooperating with other major countries to ensure that market forces can work to bring about more realistic exchange rates.

Why not give it a try and see if the manufacturing sector can follow the consumer part of the economy and "turn around?"

Respectfully,

Charles D. Yuska
President, PMMI

April 30, 2002

The Honorable Phil Gramm
Ranking Minority Member, Senate Banking Cte.
Room 534, Dirksen Senate Office Building
Washington, DC 20510

Gentlemen:

As a result of the US dollar being significantly overvalued a number of negative consequences are being experienced by New England Fabricators and the tax-paying public. First and foremost, as a result of the overvalued dollar it is virtually impossible for New England Fabricators to compete with Canadian Fabricators in the New England market. This has resulted and will continue to result in the loss of jobs and the closure of businesses in this region. Secondly, as a large segment of this type of work is at least partially state funded, the bitter reality is that our hard earned tax dollars are being exported to Canada along with our jobs.

Please consider taking immediate and significant action to address this critical situation. As our organization has invested considerable energies relative to this problem we would be more than happy to provide further assistance or input. If we can be of further help please contact me at your earliest convenience.

Sincerely,

Jack Klimp
President
SSFNE

Slitco Metal Processing & Sales Corporation

Specializing in Ferrous and Non-Ferrous Metals

The Honorable Paul Sarbanes
Chairman, Senate Banking Cte.
Attention: Laurie Better
Room 534, Dirksen Senate Office Building
Washington, DC 20510

April 30, 2002

Mr. Sarbanes,

We are a small metal service center that is being directly affected by the over valuation of the strong dollar. We have seen a significant loss in sales to our customers in the metal stamping industry. They have lost programs to other countries. They have not lost them due to poor service or quality. They have lost them because of the imbalance created by the inflated value of our currency. The situation is critical.

The 30% increase in the dollar over the last few years has created an imbalance from a competitive perspective. Our industry is eroding because of this format. We need you do something about this immediately. Our market is very competitive and the difference in the strong dollar is higher than our margins of profit. Foreign competitors have a major advantage right out of the gate based merely on currency conversions. Our industries cannot get into the race if our overseas competitors are just about at the finish line when the starting gun sounds.

The economic fundamentals are critically out of line. We need you help and we need it now. Thank you for taking the time to listen.

Respectfully,

Ronald J. Buzinski
President/Owner

April 30, 2002

Honorable Paul Sarbanes
Chairman, Senate Banking Committee
Attn: Laurie Better

Honorable Phil Gramm
Ranking Minority Member
Senate Banking Committee

Coalition for a Sound Dollar

Dear Senator Sarbanes, Senator Phil Gramm and Coalition for a Sound Dollar:

Our company presently operates seven manufacturing facilities in North Carolina and one in Georgia employing more than 1,900 people.

It is becoming increasingly difficult to maintain production in our plants due to being severely impacted by the strong U.S. dollar that, no doubt, is over valued when compared to other currencies and especially those in Asia. Recently we have been unable to work full schedules in our plants with the result that our associates have not been able to enjoy the benefits of a full work-week.

I URGE YOU TO USE YOUR INFLUENCE to change the U.S. Treasury's strong dollar policy and to act quickly to bring the dollar back down to normal levels. The Reagan Administration was successful when Treasury Secretary Jim Baker changed U.S. policy … it can be accomplished by the Bush Administration!

This action is critical to all manufacturing in the U.S. and especially to the textile industry.

Sincerely,

James W. Chesnutt

James W. Chesnutt
President/C.E.O.

pc: AYSA NCMA ATMI
Honorable Jesse Helms
Honorable John Edwards
Honorable Hillary Clinton
Honorable Zell Miller
Honorable Nathan Deal
Jimmy Broughton
Honorable Charles Schumer
Honorable Max Cleland
Honorable Walter Jones
Honorable Carolyn Maloney

Screw Machine Products

April 30, 2002

The Honorable Paul Sarbanes
Chairman, Senate Banking Commitee.
Attn: Laurie Better
Room 534, Dirksen Senate Office Building,
Washington, DC 20510

Dear Senator Sabanes:

I am writing this urgent letter to ask for your help during the Senate Banking Committee hearing tomorrow May 1, 2002.

The soaring US Dollar is breaking the back of manufacturing companies like mine. We are no longer able to compete with imported manufactured products and our major OEM customers are sourcing more of there products to overseas companies. Additionally, the recent steel tariffs have increased the prices of our domestic steel making us even more uncompetetive.

The manufacturing base in this country is eroding at an alarming rate. We need more realistic exchange rates to bring our economic fundamentals in line.

I urge you to support the United States Manufacturing Base and help put an end to the economic unbalance cause by the rising US dollar

Sincerely,

Gary Soloway, CEO
Sphere Industries

Zimmerman Metals Inc.
Over 60 Years of Quality Workmanship and Service

April 30, 2002

The Honorable Phil Gramm
Ranking Minority Member, Senate Banking Cte.
Room 554, Dirksen Senate Office Building,
Washington, DC 20510

Reference: Our Strong Dollar

Dear Senator,

The AISC, an organization that represents thousands of companies and workers in the steel construction industry, has asked me to voice an opinion on the strong dollar.

Introduction

Let me begin by stating that I am an advocate for free trade and fair competition. The tariffs that were recently instated (once again) against foreign steel producers have hurt our company because we now pay *more* for raw steel subjected to those tariffs than our foreign counterparts. Further, there are far more jobs involved in the *use* of raw steel than those protected jobs that *generate* raw steel.

Governments have used many flawed tools in an attempt to control their economies in the past. Some of these include extremely high taxes (or tariffs) and price controls. The history of our country (and others, such as The Soviet Union) is filled with examples of the inefficiency and unintended side effects of these tools.

On the other hand, it is obvious that government *needs* to take a role to ensure stability in the economy – our own most dramatic example is The Great Depression. We have learned that the threat of tariffs may have been an instigator in The Great Depression, but we have also learned very powerfully that fiscal and monetary policy are the tools that government should use to balance the economy and trade.

The recent dramatic rise in the value of the dollar has destabilized our economy, and should be corrected. Potential short-term side effects are inflationary pressure (which is presently low), but long-term side effects will be a more hospitable environment for job growth, export growth and import reduction.

Zimmerman Metals Inc.
Over 60 Years of Quality Workmanship and Service

Our Experience

Steel Fabrication:
The recent recession has affected us, but like many other small companies we have focused our attentions to new markets (such as Public Work). We have seen an increase in competition from Northern States for this work. When asked, companies from Montana and elsewhere explain, "Canadian Fabricators take all of the jobs in our home state; it is easier for us to compete here than at home."

Manufacturing:
The past year for manufacturing has been dismal. Companies that have specialized in this area have been going out of business or moving to other markets. Several times weekly an auction notice will arrive in the mail for a large, well established machining or manufacturing company that has gone out of business. The frequency with which these auction notices are received has steadily increased over time, and the work they performed is moving to Asia.

Industrial Work:
With the recent concerns over energy, we felt we should investigate power plant and industrial work. Typically, large multi-national corporations run these projects and have the resources to buy the steel more cheaply from foreign fabricators. Sadly, the only industrial work we have landed is to fix some poorly fabricated steel from Malaysia for a power plant in our own backyard.

Conclusion and The Big Picture

Every time we have bid on a job against a foreign fabricator, we have found their costs to be substantially (25% or more) below ours. We do not have these kinds of margins in our work. In fact, our labor and markup often amount to only 33% of our price. It is reasonable to expect foreign wages to be cheaper than those in the United States, but those advantages are offset by high shipping costs. Something bigger than "inefficient American companies" is at the heart of this matter. The difference in our prices has steadily risen with tariffs and the strength of the dollar.

Thank you for your attention to this matter.
Sincerely,

Zimmerman Metals, Inc.

Mark Zimmerman
President

www.nccbi.org

North Carolina Citizens for Business & Industry

Executive Committee:
- William Cavanaugh III *Raleigh*
- James J. Cook *Winston-Salem*
- Nancy W. Dunn *Winston-Salem*
- Frank E. Emory *Charlotte*
- Barry W. Eveland *RTP*
- [illegible] Fordham Jr. [illegible]
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- [illegible] Oswald [illegible]
- [illegible] Stead [illegible]
- [illegible] K. Shelton *Greensboro*
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- [illegible] Still Thrift *Winston-Salem*
- Paul M. Wiles *Winston-Salem*
- [illegible] Wilmoth [illegible]
- [illegible] Wooldshaw Jr. [illegible]
- [illegible] H. Daugherty *Raleigh*
- Malenim E. Everett III *Charlotte*
- John O. McNairy *Kinston*
- [illegible] S. Myers [illegible]
- [illegible] Phillips Jr. *Fort Mill*
- Sherwood H. Smith Jr. *Raleigh*
- G. Smedes York *Raleigh*
- Charles E. Zeigler Jr. *Charlotte*
- Stephen R. Zelnak Jr. *Raleigh*
- [illegible] *Emeriti:* [illegible]
- [illegible] Jenkins Jr. [illegible]

April 30, 2002

The Honorable Paul Sarbanes
Chairman, Senate Banking Committee
Attention Laurie Better
Room 534, Dirksen Senate Office Building
Washington, D.C. 20510

Dear Senator Sarbanes:

It is my understanding that the Senate Banking Committee will hold a hearing on Wednesday, May 1, concerning the value of the U.S. dollar.

As a representative of North Carolina's major businesses, North Carolina Citizens for Business and Industry is concerned about the number of manufacturing jobs being lost in our state and across the nation.

The U.S. dollar has soared nearly 30% over the past few years and we believe this is hurting all U.S. manufacturers and making it more difficult for us to be competitive in the global market.

North Carolina has been a world leader in textile and furniture manufacturing, but that position has changed dramatically over the past few years. This change in our economy has come about in part because of the over valued U.S. dollar.

We urge you to act as quickly as possible to address concerns over the U.S. dollar and to address U.S. dollar policy in a way that will keep us competitive and restore jobs and stability in our state's economy and across the nation.

Thank you for your work on these efforts.

Sincerely,

Leslie H. Bevacqua
Vice President of Governmental Affairs

cc: Senator Jesse Helms
Congresswoman Eva Clayton
Congressman Walter Jones
Congressman Richard Burr
Congressman Mike McIntyre
Congresswoman Sue Myrick
Congressman Charles Taylor
Senator John Edwards
Congressman Bob Etheridge
Congressman David Price
Congressman Howard Coble
Congressman Robin Hayes
Congressman Cass Ballenger
Congressman Melvin Watt

Fax To: 202-224-2080

The Honorable Paul Sarbanes
Chairman, Senate Banking Committee
Attn: Laurie Better
Room 534, Dirksen Senate Office Building
Washington, DC 20510

Dear Senator Sarbanes:

The soaring value of the U.S. dollar over the last several years has adversely affected manufacturing companies like my firm, Nu-Way Industries, Inc., along with many others in the farming and service industries.

The devastating impact of the decline in U.S. exports, over $140 billion in the last 18 months, is largely because of the overvalued dollar. And, this situation has caused at least 500,000 U.S. factory workers to lose their jobs, including about 100 people at our company. Plus, you also need to consider the thousands of additional jobs lost in the farming and service areas.

We have recently explored contractual relationships which would enable us to produce products in other countries. However this was not a matter of choice, but a matter of necessity. We would prefer to bolster manufacturing and jobs here in the U.S., as has been our privilege for over 30 years of operation. However, without your support and assistance, this is not possible. I urge you to work aggressively with your associates to forge a plan with other major countries that insures that market forces work to bring about more realistic exchange rates.

This action is essential to revitalizing the U.S. manufacturing sector and to restoring the hundreds of thousands of lost jobs. Please do all you can to contribute to this most important undertaking.

Sincerely,

Mary Howard
Executive Vice President

April 30, 2002

The Honorable Paul Sarbanes, Chairman
Senate Banking Committee
Attn: Laurie Better
Dirksen Senate Office Building, Room 534
Washington DC 20510

Dear Mr. Sarbanes:

I am extremely concerned that the dollar continues strong against foreign currencies.

I am CEO for Packaging Technologies and our export business volume is down and what export business we have is much lower margins due to the strength of the dollar.

There are currently several opportunities in China for our products (capital equipment for the packaging industry); however, we compete with the Japanese in that market. The weak yen renders a 30% price advantage for the Japanese competitor and virtually eliminates our ability to compete in China.

You should give serious consideration to using all means to bring the dollar back in line with the global economic fundamentals.

Thank you for your consideration.

Sincerely,

Barry W. Shoulders
President and CEO

raf

Structural Steel • Miscellaneous Iron • Field Services

April 30, 2002

The Honorable Paul Sarbanes
Chairman, Senate Banking Committee
Attn: Laurie Better
Room 534, Dirksen Senate Office Building
Washington, DC 20510

Re: Overvalued U.S. Dollar

Structural Welding & Engineering, Inc is a structural steel fabrication and erection company operating in the northeast United States.

The growing disparity between the value of the U.S. dollar and the Canadian dollar has created a crisis situation in the steel fabrication industry. American fabricators cannot compete with Canadian fabricators due to the overvalued U.S. dollar.

Examples of recent projects that were awarded to Canadian fabricators are the Chicopee High School project in Chicopee, Massachusetts and the Basketball Hall of Fame project in Springfield, Massachusetts. In both cases no American fabricators could compete with the "below cost" prices offered by several Canadian companies. These scenarios are playing out on a daily basis throughout the northeast. Each construction project that bids, public or private, can have up to 20 or 30 Canadian steel fabrication bidders. The number of Canadian fabricators bidding on projects has exploded over the past three years due to the overvalued U.S. dollar.

The sharp increase in foreign competition and the overvalued dollar have forced our company to cut jobs by 10%, freeze all cost of living pay increases and consider future job cuts.

Unless government implements corrective measures restoring parity, the survival of our company and the steel fabrication industry in the northeast is in jeopardy. We urge the U.S. government to:

- Publicly state that the dollar is out of line with economic fundamentals.
- Stop giving the impression the U.S. government is happy with the dollar no matter how strong.
- Commit to cooperating with other major countries to ensure that market forces can work to bring about realistic exchange rates.

This crisis requires the immediate attention and action of the U.S. government.

Sincerely,

Paul R. Labbe
Comptroller

Chairman of the Board
Stanley C. Plzak
SMTC Manufacturing Corporation
Appleton, WI

Chairman-Elect
Peter J. Murphy
Parlex Corporation
Methuen, MA

Treasurer
Leo Reynolds
Electronic Systems Inc.
Sioux Falls, SD

Immediate
Past Chairman
Ron Underwood
Circuit Center Inc.
Dayton, OH

President
Dennis P. McGuirk

Chairman of the
Technical Activities
Executive Committee
Michael Hill
Dynamic Details, Inc
Sterling, VA

IPC Government Relations
Office

Fern Abrams
Director, Environmental Policy

John Kania
Director, Government Relations

April 30, 2002

The Honorable Paul Sarbanes
Chairman, Senate Banking Committee
Room 534, Dirksen Senate Office Building
Washington, DC 20510

Dear Chairman Sarbanes:

On behalf of the IPC, Association Connecting Electronics Industries, I am writing to you to express our concern regarding the over-value of the dollar. IPC is a U.S.-based trade association dedicated to the competitive excellence and financial success of its more than 2,500 member companies which represent all facets of the electronic interconnection industry, including design, printed wiring board manufacturing and electronics assembly. As a member-driven organization and leading source for industry standards, training, market research and public policy advocacy, IPC supports programs to meet the needs of a $44 billion U.S. industry employing more than 400,000 people.

The electronic interconnection industry has experienced fierce competition from Asian competitors, in particular, China and Taiwan. Currently, these countries are able to manufacture printed circuit boards and assemblies at considerably lower costs than their American counterparts. In many cases they have a 40 to 50 percent advantage. One of the major factors in this advantage is the strength of the U.S. dollar. The value of the dollar is up 30 percent against major currencies since 1997. That's just like placing a new 30 percent tariff on U.S. products. U.S. produced printed circuit boards and assemblies are being priced out of foreign markets – and even out of our own markets.

Nearly, 60 percent of IPC members are made up of small- and medium-sized manufacturers. With exports falling at a steady rate for the past eighteen months, these are the businesses that are suffering the most.

The over-inflated value of the dollar is hurting the U.S. manufacturing sector more and more while the Administration continues to advocate a strong dollar policy. I urge you to examine the current U.S policy toward the strong dollar. It is imperative that the U.S. reassesses its policy and realigns the dollar to accurately reflect its value in the global market. Until that happens, American manufacturers will continue to falter.

Sincerely,

Dennis P. McGuirk
President

Andrea Piana
General Mgr.
Tintoria Piana US Inc.
220 S. Erwin Street
Cartersville, GA 30120

April 30, 2002

Chairman Senate Banking Committee

534 Dirksen Senate Office Building
Washington, DC 20510

Chairman Committee:

The dollar is up 30 percent against major currencies since 1997. That's just like placing a new 30 percent tariff on U.S. products. U.S. goods are being priced out of foreign markets – and even out of our own markets. Manufacturers are being particularly hard hit, and are losing sales and laying off workers.

Our company during 1998 ran a 7 day work week with 4 shifts operating 24 hours a day. At this current time we are operating only 2 shifts - 4 days a week for a total of 20 hours a day. Our sales, along with our customer base, have been greatly reduced since that time. We have seen our customers reduced their personnel along with their operation facilities. Our exports are way down from the prior years.

The Administration should: (a) firmly state it seeks a sound dollar that is consistent with underlying economic fundamentals, including competitiveness of America’s farms and industries; (b) request cooperation with other major countries on a joint effort to more realistically realign their currency values to the dollar; and (c) loudly object when other countries seek to resist market correction of their currencies upward.

Sincerely,

Andrea Piana, General Mgr. and the employess of Tintoria Piana US Inc., Cartersville, GA General Mgr. Tintoria Piana US Inc.

Received: from mailsims1.senate.gov ([156.33.203.10]) by imaexch.senate.gov with
SMTP
(IMA Internet Exchange 3.13) id 0061121D; Tue, 30 Apr 2002 16:30:09 -0400
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(Sun Internet Mail Server sims.3.5.2000.03.23.18.03.p10)
with SMTP id <0GVE001BCEFGMY@mailsims1.senate.gov> for
laurie_better@banking.senate.gov; Tue, 30 Apr 2002 16:33:17 -0400 (EDT)
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with SMTP id B65CC59ABE for <laurie_better@banking.senate.gov>; Tue,
30 Apr 2002 16:28:34 -0400 (EDT)
Date: Tue, 30 Apr 2002 16:25:43 -0400
From: Andrea Piana <tpdyer@aol.com>
Subject: Comments for May 1 Hearing on Dollar Policy

Raymond Nadolny
Vice President Sales
Corey Steel Co.
2800 S. 61st. Ct.
Cicero, IL 60804-2091

April 30, 2002

Chairman Senate Banking Committee

534 Dirksen Senate Office Building
Washington, DC 20510

Chairman Committee:

The dollar is up 30 percent against major currencies since 1997. That's just like placing a new 30 percent tariff on U.S. products. U.S. goods are being priced out of foreign markets – and even out of our own markets. Manufacturers are being particularly hard hit, and are losing sales and laying off workers.

The Administration should: (a) firmly state it seeks a sound dollar that is consistent with underlying economic fundamentals, including competitiveness of America’s farms and industries; (b) request cooperation with other major countries on a joint effort to more realistically realign their currency values to the dollar; and (c) loudly object when other countries seek to resist market correction of their currencies upward.

Sincerely,

RAY NADOLNY
Vice President Sales
Corey Steel Co.

Received: from mailsims1.senate.gov ([156.33.203.10]) by imaexch.senate.gov with
SMTP
(IMA Internet Exchange 3.13) id 0060E8AC; Tue, 30 Apr 2002 12:59:25 -0400
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laurie_better@banking.senate.gov; Tue, 30 Apr 2002 12:30:27 -0400 (EDT)
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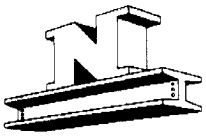
with SMTP id BEF5459A81 for <laurie_better@banking.senate.gov>; Tue,
30 Apr 2002 12:25:44 -0400 (EDT)
Date: Tue, 30 Apr 2002 12:22:54 -0400
From: Raymond Nadolny <rnadolny@corysteel.com>
Subject: Comments for May 1 Hearing on Dollar Policy
To: Chairman Senate Banking Committee <laurie_better@banking.senate.gov>
Message-id: <20020430162544.BEF5459A81@outbound.capwiz.com>
MIME-version: 1.0
X-Mailer: SMTP-Mailer



NOVEL IRON WORKS, INC.

May 1, 2002

The Honorable Paul Sarbanes
Chairman, Senate Banking Committee
Attn: Laurie Better
Room 534, Dirsen Senate Office Bldg.
Washington, D.C. 20510

Dear Mr. Chairman,

I am writing this letter to apprise you of a very serious situation threatening the Structural Steel Fabrication Industry in the United States.

The Canadian Government has systematically targeted our industry and has developed programs for their country's fabricators. These programs have been so successful, that the Canadians have now become the dominant force in the Structural Steel industry in the United States.

The overwhelming advantage the Canadians have is the monetary exchange rate. As it currently exists, the $1.58 Canadian Dollar opposed to the $1.00 American Dollar allows the Canadians to "target" and win any project they choose. The fact that many of these projects are publicly funded, by either Federal, State or Local agencies adds insult to injury.

We believe the Canadian Government is artificially manipulating the exchange rate to benefit their population at the expense of American workers.

It is our belief that this manipulation goes against the principles of fair trade practice. Therefore, we feel justified in asking the Senate Banking Committee to take the necessary steps to ensure a more equitable exchange rate between our countries. A more equitable exchange rate would reduce the Canadian advantage in the Structural Steel market.

On behalf of all the people involved in our industry, I thank you for your time and consideration regarding this urgent matter.

Sincerely,

Thomas A. Heaney
Executive Vice President

Megquier & Jones, Inc.

STRUCTURAL STEEL

1156 BROADWAY • SOUTH PORTLAND, MAINE 04106

May 1, 2002

The Honorable Paul Sarbanes
Chairman, Senate Banking Committee
Rm. 534, Dirksen Senate Office Building
Washington, DC 20410

Attn: Laurie Better

Re: US Dollar Overvaluation

Dear Chairman Sarbanes,

It has come to our attention that the Senate Banking Committee which you Chair will hold a meeting on May 1, 2002 regarding the strength of the US dollar. This is an issue of vial interest to the steel fabrication industry, particularly those of us in the Northeast. Our company, being a border state has been dealing with this issue for a decade and each year it becomes worse.

Imports of fabricated structural steel from Canada have increased from 129,000 short tons in [illegible] to 348,000 short tons in 2000. Canada is far and away the largest exporter of fabricated structural steel to the United States. Much of this increase has been in the Northeast which is my Company's primary market. The reason for this increase is simply the exchange rate. Produce in Canadian dollars, drive a few hundred miles at a nominal cost (in some cases subsidized by Provincial Governments) and get paid in U.S. dollars – an absolute windfall at the cost of U.S. jobs.

Our Company has been in this business since 1895 and is able to compete with any of the fabricators when on a "level playing field." We have a modern automated plant with motivated employees. However, when we bid projects that we already have a disadvantage of 25 – 30% on bid day, we are soundly beaten on a regular basis.

Sincerely,

MEGQUIER & JONES, INC.

John C. Yohe
President

cc: Honorable Phil Gramm

JCY/plm

WELLMAN, INC.

May 1, 2002

The Honorable Paul Sarbanes, Chairman
Senate Banking Committee
Attention: Lauri Better
Fax Number: (202)224-2080

Dear Sir:

I am writing to express my serious concern regarding the Treasury Department's ongoing "Strong Dollar Policy".

It is my personal opinion, supported by many manufacturers I talk to, that this policy is detrimental to U.S. manufacturing and fair trade.

A National Association of Manufacturers study indicates the dollar's rise has caused a loss of nearly 1.3 million manufacturing jobs in the last year alone. This policy has caused the dollar to hit a 16 year high, an increase in value of 30% in the last 5 years.

Wellman, Inc. has been directly impacted by this policy, and it has contributed to our decision to close two plants in the Carolinas, in the near future.

We, like all U.S. manufacturers, want to operate with a "level playing field" and compete in a fair trade environment. The overly strong dollar is a handicap to business growth in the future and is a major threat to current employment.

Sincerely,

Ian K. Shaw
Plant Manager

May 1, 2002

The Honorable Paul Sarbanes
Chairman, Senate Banking Committee
ATTN: Laurie Better
Room 534, Dirsen Senate Office Building
Washington, DC 20510

Dear Senator Sarbanes:

Thank you for taking the time to review our serious problem. U.S. fabricators and especially those in New England are facing unfair competition from Canadian fabricators that are taking virtually all of their work. This includes many publicly funded jobs such as schools, courthouses and airports etc. Although this problem has existed for some time, it has been overlooked up until recently since most U.S. fabricators have also been busy due to the strong economy and the Big Dig. With the current building slowdown the affect of the Canadian Fabricators is being felt by large and small shops since the large shops are being forced to bid the smaller jobs because the Canadian Fabricators have taken all of their work.

The Canadian trade advantage is threefold:

- Unlike the U.S., Canada does not produce any of their own beams and therefore has no pending tariffs blocking imported beams. A Canadian fabricator can buy imported beams for significantly less per pound than what a U.S. Fabricator must pay for same beam. The cost can be as low as 40% below what Fabricators in the U.S. have to pay for the same section of wide flange beams.
- In Canada, Workman's Compensation and Health Insurance is fully provided for by the Government. Workman's Compensation and Health Insurance is a major expense to U.S. Fabricators that can add as much as 45% to their labor costs.
- One U.S. Dollar is currently worth 1.58 Canadian Dollars. This is the greatest disparity in recent history. In Europe they are also now experiencing free trade between nations but with one big difference – One currency - the Euro Dollar!

I have explained the problem in detail in my enclosed Newsletter. I have also enclosed lists of recent projects awarded to a few of the Canadian fabricators that show that a majority of their work is fabricating steel for delivery to jobs in the U.S.A.

Canadian Fabricators, due to the recent slow down and their above advantages are now underbidding U.S. Fabricators buy more than a third. Many U. S. fabricators have given up bidding any structural jobs. Some have no idea what to bid on since they know they will get underbid by Canadian's on any job that is new construction, which requires minimal change orders and a therefore a minimal local presence. Many have had to lay off employees and others have no more than a few months of back log on their books and are very concerned about this upcoming year. **The situation is extremely urgent and must be addressed immediately.**

What needs to happen?

On a Federal Level:

1. U. S. has to levy heavy duties on steel fabricated in Canada to make up for their currency, labor and steel purchasing advantages.
2. As was done in Europe via the Euro Dollar, all NAFTA countries' currencies should exchange at par. Unless the Canadian Dollar exchanges at par with the U.S. Dollar we will not have a fair U.S./Canadian trade policy.

On a State Level:

1. To speed up the relief, the New England States should immediately pass legislation which prevents steel fabricated outside the U.S. from being used in new structures such as schools that receive state funding

Thank you,

John G. de Vries
President, CEO
Central Steel Supply Co., Inc.

CENTRAL STEEL SUPPLY COMPANY

CENTRAL STEEL JOUR

"Keeping you informed of changes in the world of Ste

John Doe can't win a fabricating job!

Why John Doe USA Iron Works is not bidding on the new Local High School?

John Doe's story would inspire any hard working person with a dream for success and the sweat to get there. After working his way up from welder, to shop foreman, to estimator and then second in command of a large fabrication shop, John went out on his own about ten years ago. His steel fabrication shop is called John Doe USA Iron Works.

Marriot Inn, Boston, MA
Steel Fabricator:
Ocean Steel, NB CANADA

Independence has not been easy for John but he wisely reinvested most of his past profits back into the business in the form of estimating software, new plant facilities, and saws etc. John recently expanded his shop and installed a new beam line. He is very proud of his state of the art steel fabrication shop; it is well laid out and is as efficient as any medium sized Miscellaneous/Structural Steel Fabrication shop in North America.

With hard work and a well-paid team, John Doe has built a reputation for quality and reliable delivery times that has earned him the edge in winning jobs from contractors and property owners throughout New England. He has reached middle age now and is looking forward to teaching his son, a recent civil engineering graduate from UMASS Lowell, the business so he can retire in ten years.

But somehow the business is beginning to change and is becoming much more competitive. Although in the past John averaged 6 months to over a year in back log, he now has only 2 ½ months of work left on the books. He has not won a significant bid in over 6 months. Has the economy come to a halt due to September 11th and the demise of the Dot-Coms? Not so says John – the Dodge report is still loaded with work that John has bid, including lots of new schools and bio-tech facilities. **But why is John Doe USA Iron Works not winning any new work?** The answer lies north of the border. Unlike the U.S., Canada does not produce any of their own beams and therefore has no pending tariffs blocking imported beams. A Canadian fabricator can buy imported beams for significantly less per pound than what a U.S. Fabricator must pay for same beam. The cost can be as low as 40% below what Fabricators in the U.S. have to pay for the same section of wide flange beams.

Boston Convention Center
Steel Fabricator: Canam Steel, QC Canada
Miscellaneous Iron: SuperMetals, QC Can

This is a huge purchasing advantage, but it is only part of the problem. In Canada, Workman's Compensation and Health Insurance is fully provided for by the Government. What does that convert to in labor cost savings? Add that to the fact that the Canadian dollar is worth only 62 U.S. cents gives our friends to the north an unfair advantage. The Canadian government is in effect exporting their own unemployment to the U.S.! **A significant and continually increasing amount of the U.S. Steel Fabrication work is going to Canadian Fabricators. In many cases they are under bidding U.S. Fabricators by more than a third!**

Canadian Steel Fabricators have set up mega production shops mostly in eastern Canada to take advantage of the profitable market in the United States. They have estimators and sales teams with local U.S. offices to make sure they do not miss bidding on any of our jobs. **Last year about 840,000 Tons of Structural Steel was imported from over seas into Canada; their own annual usage for this steel is only about 650,000 Tons! Where do you think the rest of the steel went?**

Without paying significant Dumping Duties, U.S. Fabricators cannot buy most imported steel, especially beams, off the pier in Montreal and truck it south over the border for fabrication. On the other hand, Canadian Fabricators are buying imported steel from over seas at a lower price, fabricating it in Canada with much lower labor costs and then exporting it in a fabricated form into the U.S. while not paying any significant duty.

Up until the recent slow down the fact that Canadians have taken so many U.S. Steel Fabrication jobs has gone unnoticed because Fabricators in the U.S. still had plenty of work. **But as construction continues to slow the same Canadian Fabricators have started to under bid and win more and more of the smaller "Miscellaneous" iron jobs.** They have no choice but to take the smaller jobs if they want to maintain the volumes that are required to keep their large Canadian operations efficient.

Montachusett HS, Fitchburg, MA 340 Tons
Steel Fabricator: Cherubini Group, NS Canada

John Doe has given up on bidding any new public work. He is tired of coming in above Canadian Fabricators on every bid. Just recently, John bid on the new high school in Falmouth, MA - a project that will eventually result in a 10 - 15% increase in John's personal home property tax. Again, there were five Canadian Fabricators who submitted lower bids than John's. The sad thing is that the highest of the Canadian bids was over $150,000 below his bid and John had the lowest bid submitted by any U.S. Fabricator!

Although John Doe USA Iron Works obviously does not really exist, **all of the above examples are taken from real cases** and a very similar story with varying degrees of pain is being played out throughout the United States especially in New England. New England and U.S. Steel Fabricators are in big trouble and, if fair trade does not intervene, the picture is going to get a lot worse.

Logan Airport – Expansion, Boston, MA
2000 Tons
Steel Fabricator: ADF Group, QC Canada

Although the American Institute of Steel Construction attempted to have Canadian Fabricated Steel included in the section 201 trade action recommendations to the President, the International Trade Commission ("ITC") failed to understand the severity of the problem and did not address the issue in their final trade action recommendations. Any pending action to further protect U.S. steel mills will only raise domestic steel prices/costs for U.S. Fabricators and increase Canada's already huge advantage. **The time has come for the U. S. to levy heavy duties on steel fabricated in Canada to make up for their currency, labor and steel purchasing advantages. Also, as was done in Europe via the Euro Dollar, all NAFTA countries' currencies should exchange at par. To speed [illegible] relief, the New England States should immed[illegible] pass legislation which prevents steel fabricat[illegible] outside the U.S. from being used in new structu[illegible] such as schools that receive state funding.** NA[illegible] is great idea, but was it created to let the Canad[illegible] advantage of us? If the ITC, President Bush and [illegible] New England State Legislatures ignore this prob[illegible] than the future of the U.S. Steel Fabricator is not just uncertain but soon may be coming to an end. Can New England afford to lose any more manufacturing jobs to unfair foreign competition?

Where can U.S. Steel Fabricators turn for help? Join one or more of the following trade organizations:

Structural Steel Fabricators of New England:
www.ssfne.org

American Institute of Steel Construction:
www.aisc.org

National Ornamental & Miscellaneous Metals Association: www.nomma.org

Write your U.S./Local State Representative/Sen[illegible] and the U.S. Ambassador to Canada:

www.house.gov/writerep www.state.ma.us

www.senate.gov/contacting/index.cfm

www.usembassycanada.gov

Subs[illegible] VT, R[illegible] ME, etc. wh[illegible] me is to contact your state legislators.

I invite you to call me to discuss this very significant issue.

John G. de Vries
President, CEO
Central Steel Supply Co., Inc.

Serving the Steel needs of New England Industry Since 1945!

Central Steel Supply Co., Inc.
99 Foley Street, Somerville, MA 02145
617.625.3232 800.345.3232 Fax 617.666.3027

Member: NORTH AMERICAN STEEL ALLIANCE
The Independent Al[illegible]

Company Information

The Cherubini Group of Companies is a wholly owned and operated Nova Scotia based steel fabrication operation. The fabrication group includes the following divisions:

- **Cherubini Metal Works Limited**, Dartmouth, NS
- **Rendan Fabricators Limited**, Dartmouth, NS
- **Amherst Fabricators Limited**, Amherst, NS

The Cherubini Group, operating since 1967, presently employs approximately 310 people. Officers include Danilo Gasparetto, President, Renato Gasparetto, Secretary-Treasurer and Stephen Ross, General Manager. In 2000, we were ranked 52nd on the listing of the Top 101 Companies of Atlantic Canada and were included on the Top 20 listing of the region's fastest growing companies.

Our main focus of construction is related to heavy and light structural steel, bridges, platework, transmission towers and miscellaneous fabrications. Versatility of the Company is demonstrated with its ship refit contract completed for Secunda Marine Services Limited. We are a member of the Canadian Institute of Steel Construction, the Canadian Welding Bureau (Division 1), the American Institute of Steel Construction and have been awarded ISO 9002 certification.

The Group's Dartmouth, N.S. production facilities of 80,000 sq. ft. and Newfoundland's production facility of 10,000 sq. ft. house some of the most technologically advanced computer numerically controlled fabrication equipment. With equipment ranging from beam lines to burning tables, these locations allow for the production of 15,000 - 20,000 tons of quality fabricated product per year. The May 1999 opening of a 74,000 square foot production facility in Amherst, N.S. has doubled the Company's capacity to produce fabricated steel.

The Dartmouth facility, together with CSI Fabricators Inc. in Newfoundland and Amherst Fabricators Limited, form alliances with Argo Protective Coatings Inc. providing quality coating paint systems, finishes and hot dipped galvanizing and Rendan Fabricators Limited providing rebar fabrication and placing, ensures customers a full service Group of Companies.

Our advanced fabrication process, well trained work force and strategic alliances continue to be the key ingredients in allowing Cherubini to provide a quality product, delivered on time and at a reasonable price. Over the past few years, Cherubini has strengthened its international markets with the successful completion of many projects with contractors in the North Eastern United States and Bermuda. Past and current projects include the delivery of steel to job sites in Massachusetts, Maine, New Jersey, New York and Connecticut. The Amherst facility, positioned close to the U. S. border, will provide an effective distribution to Cherubini's growing marketplace.

Cherubini takes pride in the fact that we were a major supplier for the Confederation Bridge linking New Brunswick and Prince Edward Island. Our expertise with bridges has been enhanced with the supply and install of structural steel for the Hillsborough River Bridge project and is reinforced by the 1999 Macdonald Bridge upgrade project for the

Halifax-Dartmouth Bridge Commission.

Facilities:

14,000 SF Dartmouth Tower Shop
25,000 SF Dartmouth Main Shop
22,000 SF Dartmouth Bridge Shop
21,000 SF Dartmouth Mixed Use Buildings
74,000 SF Amherst Shop
5 acres of Yard Storage

For general inquiries please see the contact information below. If you would like a brochure, please provide us with your full address.

Telephone:
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Fax:
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Email:
cmw@cherubinigroup.com

Postal Address:
Cherubini Group of Companies
50 Joseph Zatzman Dr.
Dartmouth, NS
B3B 1N8
Canada

CHERUBINI GROUP OF COMPANIES

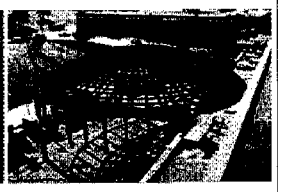
Project Experience

Click on any of the pictures below to view the full picture.		
CURRENT STEEL PROJECTS	WEIGHT IN TONS	CONTACT
Nautica Charlestown, MA	1250	Suffolk Construction
Conduit Supports New York, NY	28	Koch Skanska
Marshall House Bermuda Hamilton, Bermuda	8	MR Construction
Temporary Tower Supports Bronx, NY	55	DeFoe Corporation
Sole Plates JFK Airport, NY	7	AirRail Transit
Hornes Brook Viaduct Alma, NS	115	Dineen Construction
MWRA North Maintenance Facility Chelsea, MA	770	Suffolk Construction
Expansion Joints Carteret, NJ	77	Koch Skanska
Olin College – Bldg D Needham, MA	587	Richard White Sons
Calpine Ross / Spring Street Substations Westbrook/Gorham, ME	10	Central Maine Power
Approach Bracket Repair Outerbridge Crossing, NY/NJ	30	Koch Skanska
US Airways Boston, MA	600	Daniel Marr & Sons
Fort Banks Elementary School Boston, MA	400	TR White
Scuppers – Outerbridge Crossing New York, NY	230	Koch Skanska Inc.
Brackets – Outerbridge Crossing New York, NY	200	Koch Skanska Inc.
Northbridge High School Northbridge, MA	1000	Jackson Construction
Esso Pier Upgrade Bermuda	100	Correia Construction
Office Expansion – Clearwater	200	Corkum Construction

Bedford, NS		
Office Complex Cayman Islands	250	Gibbons Management
Terra Nova Offshore	5	Offshore International
Production Assemblies Offshore	5	Offshore International
Logan Airport Boston, MA	600	ADF International
Musquodobit School Musquodobit, NS	102	Tidewater Construction
Bio Square Parking Garage Boston, MA	975	Suffolk Construction
Central Square Cambridge, MA	1050	Suffolk Construction
6th and 7th Avenue Bridges Bronx, NY	815	Quickway Metal Fabricators
Hopkinton High School Hopkinton, MA	442	Callaghan & Sons
Boston Latin School Boston, MA	493	Suffolk Construction
Travellers Form St. Louis, MI	320	Walter Construction
Bruckener Temporary Overpass New York, NY	522	DeFoe Corporation
Parapet Connection JFK Airport, NY	439	AirRail Transit Consortium
Landmark Center Boston, MA	1100	Daniel Marr & Son
Clayton Park West Apartment Building Halifax, NS	Unit Price	Steve Hanias
COMPLETED STEEL PROJECTS	WEIGHT IN TONS	CONTACT
Exterior Stage Space Frame Dartmouth, NS	55	Halifax Regional Municipality
Buxton / Biddeford Substations Buxton / Biddeford, ME	10	Central Maine Power
St. John's Civic Centre St. John's, NFLD	900	City of St. John's, NFLD

St. John's Civic Centre

Holyoke College Athletic Facility Holyoke, MA	276	Fontaine Bros., Inc.
Westbrook Substation Westbrook, ME	40	Central Maine Power
Bedford Place Mall Joist Repairs Bedford, NS	Site Work	Dorchester Oaks Property Management
Alcan Project Alma, QC	760	Canam Manac Group
Fitzgerald School Cambridge, MA	260	Peabody Construction
Casino Pedway Halifax, NS	46	J.W. Lindsay Enterprises Ltd.
Bruckener Temporary Structures Bruckener Expressway, NY	574	DeFoe Corporation
Waterfront, Misc. Metals Hamilton, Bermuda	75	BCM McAlpine
CA/T Underpinning Fabrication Boston, MA	100	Maritime Steel
Retail Complex Bayers Lake, NS	70	WM Fares and Associates
New Ditson Elementary School Billerica, MA	462	P.J. Stella Construction
Concrete Forms Vancouver, BC	603	Deal S.R.L.
Waterfront Casino Halifax, NS	1100	J.W. Lindsay Enterprises Ltd.



Halifax Waterfront Casino

Macdonald Bridge Upgrade Halifax, NS	6000	Halifax / Dartmouth Bridge Commission

Macdonald Bridge Upgrade

Pier Cable Framing – St. Louis St. Louis, MI	195	Walter Construction
South Gorham & Surowiec Substations South Gorham & Surowiec, ME	2.4	Central Maine Power
Beacon Project Amherst, NS	300	Breton Steel
Charles River Square Building Watertown, MA	1055	Prime Steel Erectors
Martin Marietta Aulds Cove, NS	12	Beaver Marine
Skylight Trusses Yarmouth Residence Yarmouth, NS	8	Clemmensen & Associates Ltd.
McCurdy Printing Loading Dock Dartmouth, NS	5	L.B. Stevens Group
Conference Hall Wolfville, NS	140	Old Orchard Inn
Whale Beam Boston, MA	1000	Perini Kiewit Cashman
Buxton Substation Steel Buxton, ME	Unit Price	Central Maine Power
Logan Airport Cooling & Heating Upgrade Boston, MA	335	Peabody Construction Co.
Phelps Property Renovations Hamilton, Bermuda	Unit Price	Gibbons Deposit Company
South Shore Regional Hospital Bridgewater, NS	2	Bremner's Plumbing & Heating
Deck Framing & Railing Elmsdale, NS	2	Airport Hotel
Bone Lattice – Lewiston Substation Lewiston, ME	100	Central Maine Power
Tuft's Cove Gas Addition Project Tuft's Cove, NS	Installation	Nova Scotia Power Inc.
Your Father's Moustache Halifax, NS	10	Mannex Projects

Pier 21 – Misc. Metals Halifax, NS	50	Robert McAlpine Atlantic Ltd.
Lewiston Substation Lewiston, ME	30	Central Main Power
Amherst High School Amherst, NS	374	Meridian Construction
Overhead Pipe Trusses Dartmouth, NS	22	Imperial Oil
Hanger Door Cladding Algeria	41	Entra Tech Inc.
Lord Nelson Hotel Halifax, NS	Unit Price	Universal Properties
MV Trinity Sea – Refit Dartmouth, NS	N/A	Secunda Marine Services
Erection Trusses JFK Airport, NY	766	AirRail Transit Consortium

Erection Trusses - JFK Airport

Shim Plates – Central Artery Boston, MA	320	Perini Kiewit Cashman
Truck Dumper St. Stephen, NB	75	Phelps Industries, Inc.

Truck Dumper

Sunrise of Clarkstown Clarkstown, NY	196	Suffolk Construction
Point Tupper Pipe Racks Point Tupper, NS	120	BBA Joint Venture

Yarmouth Regional Hospital Yarmouth, NS	170	Western Regional Health Board
LOM Office Structure Hamilton, Bermuda	150	D & J Construction
Independent Living Facility Plainsboro, NJ	1300	Suffolk Construction
Pier 21 Centre Halifax, NS	55	Pier 21 Society
Montachusett High School Fitchburg, MA	340	TLT Construction
Screening Facility Windsor, NS	147	Fundy Gypsum Miller Creek
Central Artery Deck Beams Boston, MA	1000	Perini, Kiewit, Cashman
MV Trinity & Burin Sea Dartmouth, NS	328	Secunda Marine Services
Sunrise of Stamford Stanford, CT	215	Suffolk Construction
Sunrise of Wilton Wilton, CT	154	Suffolk Construction
Target Store Danvers, MA	70	Prime Steel Erectors
Alderney Landing, Misc. Metals Dartmouth, NS	50	Halifax Regional Municipality
Cole Harbour Place Dartmouth, NS	22	Dineen Construction
Boggy Brook Transmission Tower Ellsworth Falls, ME	30	Union Water Power Co.
Mega-Doors Halifax, NS	31	Halifax Shipyard Limited
Hanger Doors Algeria	450	EntraTech Inc.
Glen Arbour Clubhouse Glen Arbour, NS	50	Annapolis Basin Group Inc.
First Lake Shopping Centre Sackville, NS	50	Westdale Construction
Bayer's Road Shopping Centre Halifax, NS	500	Dineen Construction
Halifax Shopping Centre Addition Halifax, NS	1500	Fraser Brace
Plant Expansion, Stora Port Hawksbury, NS	160	Stora Forest

Astral Drive School Dartmouth, NS	206	Erskine Builders
Burnaby Street Building Hamilton, Bermuda	75	Triangle Exports
Nova Scotia Youth Centre Kentville, NS	200	Dineen Construction
Cole Harbour Place Dartmouth, NS	725	Dineen Construction
Leon's Furniture Store Dartmouth, NS	320	Ellis-Don Atlantic
Metropolitan Place Dartmouth, NS	275	Delcor
Sackville Sportsplex Sackville, NS	450	Dineen Construction
Boat Haul Out Cradles Yarmouth, NS	125	Annapolis Development Commission
Pipe Supports Dartmouth, NS	210	I.O.E.L
Power Substation St. Pierre-et-Miquelon	125	St. Pierre
Power Substations Various - Newfoundland	225	Newfoundland Hydro
Transmission Towers Cape Breton, NS	200	Nova Scotia Power Inc.
Pratt & Whitney Plant Elmsdale, NS	747.5	Fraser Brace
Eastern Passage School Dartmouth, NS	235	Ellis-Don Atlantic
Health & Welfare Building Dartmouth, NS	225	Dineen Construction
Cow Head Fabrication Facility St. John's, NFLD	848	Gildart Construction
Transmission Towers Cape Breton, NS	3250	Nova Scotia Power Inc.
Transmission Towers Various - Newfoundland	1100	New Brunswick Power
G.S.T. Headquarters Summerside, PEI	1094	Public Works Canada
Woolco Store Sackville, NS	500	Maxim Construction
Cabot Institute St. John's, NFLD	165	Triad Fabricators
Cole Harbour School	315	Dineen Construction

Dartmouth, NS		
R.C.M.P. Headquarters St. John's, NFLD	500	Maxim Construction
Sir Wilfred Grenfell College St. Anthony, NFLD	237.5	Merit Management
Aberdeen Hospital New Glasgow, NS	375	Ellis-Don
Superstore Halifax, NS	325	IPCF Properties
Chain Link Building Halifax, NS	350	W.M. Fares and Associates
Confederation Bridge PEI Northumberland Strait	1500	Umacs Canada
Confederation Bridge PEI Northumberland Strait	5000	Strait Crossing

Confederation Bridge PEI

Whitney Institute Hamilton, Bermuda	47	Fred Petty & Associates
Ferry Terminal Upgrade Port-Aux-Basque, NFLD	160	Meridian Management
Boom, Crutches, Pedestals Dartmouth, NS	150	Secunda Marine
155 Chain Lake Drive Halifax, NS	350	W.M. Fares and Associates
Hillsborough Bridge Charlottetown, PEI	1000	Strait Crossing Inc.
Point Webster School Quincy, MA	220	Bonfatti Construction
Natick Centre Natick, MA	493	R.W. Granger
Stora Forest Products Port Hawksbury, NS	1000	Maxim Construction
Waterfront, Pitts Bay Hamilton, Bermuda	1500	BCM McAlpine
ALL School Worchester, MA	1000	Peabody Construction
JFK Airport Columns New York, NY	75	Quickway Metal Fabricators
Kimberley Clarke Truck Dumpers Port Hawksbury, NS	75	Phelps Industries, Inc.

BELTON
INDUSTRIES

May 1, 2002

The Honorable Paul Sarbanes, Chairman
Senate Banking Committee

Attention: Lauri Better

FAX: 202 224 2080

Dear Senator Sarbanes:

We are proud members of the National Association of Manufacturers and are confident that in the next few days you will hear quite compelling testimony concerning the overvalued dollar from them and a coalition of associations representing the major wealth building engines of our economy. Our company is a small manufacturing concern in the business of manufacturing for over eighty five years. The company has stayed in business by being flexible and willing to change directions as markets and customer needs changed. We are quite comfortable in a free market environment where the playing field is level.

I agree with the notion that markets should decide currency's value. However, when a government, steps in and artificially controls its currency, it is then out of the market arena, and the consequences of their actions are spread to other countries. Thus a government that presides over a country that is economically out of control, and forces a major devaluation of its currency as a quick remedy, creates an action that may begin to help its citizens, but at the expense of manufacturing jobs in this country and elsewhere. Since economy-wide employment peaked in March 2001 a total of over 1.2 million jobs have been lost in the manufacturing sector. In our small company we have been forced to scale back production and with it over one third of our work force. We did not loose customers, but as our customer base lost volume, they had to reduce their off take from us. A large portion of our customer base made products for the export market. Their business decline started back in 1997 and became increasingly worse as the dollar began to appreciate rapidly. Over time domestic markets were caused to shift to overseas sources causing erosion of business in that sector of their business as well.

I see this as a modern version of the old trick used by governments of old. For hundreds of years, when things got sticky internally, rulers frequently stirred up trouble on the border to bring its subjects together in a defensive (and hence more loyal) mode. A major currency devaluation certainly stirs up things on the border, and though making imported articles more expensive, does fuel job growth in their manufacturing sector, which begins to build wealth within their country. If we on the other side of the border do nothing, we can expect to see imports become cheaper, but our consumers will become less affluent as they loose the good paying manufacturing jobs. In our case, especially since we are trade debtor nation, the cheaper imports keep prices down and in the short term buffer the hurt of the many who are made less affluent by the loss of higher paying jobs. Finally the loss of wealth in this country will take its toll. Then eventually our country is forced into the position of the nation that fired the "devaluation shot" at us. Seems to me we entered into an era of currency/trade wars in the mid to late 90s and to date are losing.

It is a government to government induced problem; thus the expectation for a government resolution. I applaud the hearing you are giving this matter, and hope that you and your colleagues will take to heart the gravity of the situation.

Respectfully,

Carroll B. Hart, Sr.
President

MEMO

TIMKEN

Mark W. Propst
General Manager
Gaffney Bearing Plant

WORLDWIDE LEADER IN BEARINGS AND STEEL

May 1, 2002

TO: The Honorable Paul Sarbanes, Chairman
Senate Banking Committee
Attention: Lauri Better

SUBJECT: Strong Dollar Policy

In the last two years there have been many factors that have contributed to the U.S. manufacturing recession. One of the principal reasons has been the value of the dollar. In the past year nearly 1.4 million manufacturing jobs have been lost in the U.S. During the same recent period, the dollar has risen 30%. This can not be viewed as coincidence, but rather directly related.

I am writing to ask for your action to address this problem. The manufacturing strength of the U.S. is at stake. The Administration should take immediate steps with the benefit of congressional support:

- Announce clearly that the market should set the value of the dollar, that the dollar is too high and the Treasury will not intervene in foreign exchange markets to prevent the dollar from adjusting.
- State that the United States will oppose foreign country interventions designed to slow movement of currencies toward equilibrium.
- Seek agreement that the G8 countries should work together to achieve currency alignment.

Your attention to this problem is urgently needed.

01 May 2002

The Honorable Paul Sarbarnes
Chairman, Senate Banking Committee
Attn: Laurie Better
Room 534, Dirksen Senate Office Building
Washington, DC 20510

The Honorable Phil Gramm
Ranking Minority Leader, Senate Banking Committee
Room 534, Dirksen Senate Office Building
Washington, DC 20510

Gentlemen:

I am a structural engineering consultant to an organization of 45 New England structural steel fabricators that, for about eight years, have been facing increasingly unfair trade with Canadian fabricators from the Eastern Provinces.

Since the NAFTA Agreement, the Canadian dollar has been decreasing in value relative to U.S. currency. For the past several years it has hovered in the $.60 US $.70 US range. There does not seem to be any fundamental economic reasons for their dollar to be worth so little relative to ours. There are about 30 Canadian fabricators bidding and taking structural steel work for buildings in New England. Many of these projects are schools that are funded by local tax revenues collected from local American workers.

Mainly because of the weak Canadian dollar, Canadians can bid work 10% to 25% less that New England fabricators. Now that the strong construction market has slowed down, the viability of yet another manufacturing industry in the Northeast (and nationwide) is threatened.

The Canadians do not produce a better product, nor are they more efficient than American companies. The deplorable Canadian dollar is the main factor causing the unfair trade balance in our industry. Any help you can provide to level the playing field would be very welcomed.

Emile W.J. Troup, P.E., Consultant
Structural Steel Fabricators of New England
www.ssfne.org

RESEARCH AUTOMATION INCORPORATED

ENGINEERS & BUILDERS
AUTOMATION MACHINERY & SYSTEMS
TOOLS, DIES & EDM

May 3, 2002

The Honorable Paul Sarbanes
Chairman, Senate Banking Cte.
Attn: Laurie Better
Room 534
Dirksen Senate Office Building
Washington, DC 20510

Dear Senator Sarbanes,

We need your help.

For the first time in 31 years, I have been forced to lay off skilled craftsmen who were engaged in designing and building the machinery and equipment that Manufacturing uses to achieve the productivity that gives all Americans the standard of living we have come to expect and enjoy.

The overvalued dollar is a prime factor in the demise of Manufacturing and Manufacturing Jobs in this country.

We all need your help NOW!

Sincerely,

Stephen P. Arbizzani
President
RESEARCH AUTOMATION INC.
SPA/sk

MEMBER
TMA
TOOLING & MANUFACTURING ASSOCIATION

ASTENJOHNSON

May 3, 2002

Via fax: 202-224-2080

The Honorable Paul Sarbanes, Chairman
Senate Banking Committee
Attention; Lauri Better

Dear Senator Sarbanes:

The Treasury Department's "strong dollar" policy is making us weak! This policy has caused the dollar to hit a 16-year high and the value of the dollar has increased by 30 percent over the last five years. This has cost over 1.3 manufacturing jobs just in the last year alone.

In today's competitive global marketplace, we need to support legislation that will help our domestic producers compete.

As a result of this policy, we have had to close plants and layoff workers. We ask that you please reconsider this policy and help us keep US jobs and US plants open.

Sincerely,

William A. Finn

MARTIN BRASS FOUNDRY

May 3, 2002

The Honorable PhilGramm
Ranking Minority Member
Senate Banking Cte.
Room 534, Dirksen Senate Office
Washington, DC 20510

Dear Sir:

I am writing to you to inform you of my opinion that the dollar is overvalued. Martin Brass Foundry is a Los Angeles, Ca. based brass foundry which employes 80-100 people.

We are facing increasing competition from overseas, resulting in a production decline and the laying off of 25-30 employees. Eventhough we are environmentaly correct, the cost of complying with environmental issues added to a 20% decline in production places us in a difficult position. We are unable to pass such costs on to our customers, as we are in a competitive market.

Foreign competition is going after the customers that order high volume items. Since they don't have to contend with all of our governmental regulations and fees, higher labor costs, etc. we are in a no win position.

As a U.S. corporation how are we going to compete?

Sincerely,

Roland Martin
Pres.

BERTSCHE ENGINEERING CORP.

May 8, 2002

The Honorable Paul Sarbanes
Chairman, Senate Banking Cte.
Attn: Laurie Better
Room 534, Dirksen Senate Office Building
Washington, DC 20510
FAX: 202-224-2080
Laurie better@banking.senate.gov

To the Honorable Paul Sarbanes:

As a company that designs and manufactures machine tools in the U.S., we are facing the most serious crisis in our 30 years of existence. We are faced with tremendous competition from overseas which is aided by both lower manufacturing costs and more importantly, by an overvalued dollar which has inflicted serious harm to our company's ability to compete on a level playing field. The importance of manufacturing to the general welfare of the U.S. economy cannot be overemphasized. The importance that the machine tool industry plays in making manufacturers more competitive is a recognized fact in every industrialized country except the U.S. When countries such as Germany, France and Switzerland, which have higher costs to manufacture, must transport their goods, pay duties and freight and can still undersell us by 20 to 30% in our own backyard, then something is wrong. Today we are unknowingly (knowingly) sacrificing our own domestic industries for short-term gain. U.S. companies must compete fiercely in a global economy where most countries only think globally when it comes to selling their products cheaply in the U.S. I urge you to take whatever measures are necessary to bring the value of the U.S. dollar back to its true value.

Sincerely,

Richard W. Bertsche
Bertsche Engineering Corporation