COMMITTEE ON WAYS AND MEANS

U.S. HOUSE OF REPRESENTATIVES

WASHINGTON, DC 20515

April 10, 2013

Ambassador Demetrios Marantis
Office of the United States Trade Representative
600 17th Street NW
Washington, DC 20508

Dear Ambassador Marantis:

I understand that the Administration is engaging in negotiations with Japan on a package of upfront measures and other commitments that could lead to Japan's participation in the Trans-Pacific Partnership (TPP) negotiations. I am deeply concerned that this approach is woefully insufficient to the economic challenges we confront with Japan. I strongly urge the Administration not to proceed further down this path without the clearest possible understanding of what is at stake and without the fullest possible engagement of Congress and stakeholders.

The basic question before us at this point is whether to accept Japan's bid to join TPP. To answer that question we need to consider the realities in a number of key sectors – including autos, agriculture, insurance, and others – where we have historically had significant trade concerns with Japan. Of these, the auto trade issue is the largest and, therefore, in need of particular focus.

(1) The Closed Japanese Market Has Dire Consequences for the U.S. Industry

The consequences of the closed Japanese market and the risks to the United States of being unable to open that market in the TPP talks are significant.

A growing trade imbalance: At present, we sell one American car in Japan for every 120 that Japan sells here. And, in 2012, the Big Three automakers sold less in Japan in one year (13,637 cars) than Japanese companies sold in a day in the United States (14,640 cars). Trade in auto parts is equally imbalanced ($15.5 billion in 2012). Unless we compel some real reform from Japan, we will surely lock in and exacerbate this one-way trade. Given that Japan accounts for our second largest trade deficit, after China, and that automotive products account for the lion's share (70 percent) of that deficit, a deepening automotive trade deficit with Japan could have serious implications for the U.S. economy.

Growing competitive disadvantages: Consequences beyond the impact on the U.S. trade balance have to be considered as well. Japan has the third largest auto market in the world. And Japanese automakers are guaranteed almost all sales in that market, year in and year out. This allows Japanese automakers to achieve economies of scale and drive down their costs in ways that American companies simply cannot.

We also need to examine the incentives that are created because of the closed Japanese market. For example, sanctuary markets typically create perfect conditions for dumping – where high prices are charged in the home market and used to subsidize low-priced sales in prized markets overseas. Certainly pricing data for Japanese automobiles are consistent with these kinds of predatory practices (e.g., the current price of a Lexus IS 350 is $50,037 in Japan, but only $40,220 in the United States). Do these pricing patterns result from the closed market and, if so, do they not evidence another unfair competitive advantage that Japanese automakers have over ours? Moreover, if, as it seems, Japanese automakers have higher profit margins on their Japanese sales, what are they able to do with those profits in terms of research and development, which would have even longer term implications for American automakers?

Diverted third country exports: The closed Japanese market could also have ramifications with respect to third country exports to the United States. For example, Korean automakers are just as closed out of the Japanese market as U.S. makers. Indeed, Hyundai-Kia, Korea's top automaker and a company that has been able to succeed in every other auto market, pulled out of Japan completely in 2009 because of struggling sales. Given that Korea is the fifth largest producer of automobiles in the world, a closed Japanese market forces Korean producers to turn increasingly to the U.S. market, further intensifying the competition faced by U.S. automakers.

(2) A Declining Yen Raises the Stakes

The Japanese yen has been rapidly depreciating over the last few months (from 78 yen/dollar on October 1, 2012 to 93 yen/dollar in February 2013). And the Japanese government has signaled a commitment to continuing the trend. Toyota has estimated that a one-yen decline against the dollar adds about 35 billion yen ($377 million) to its operating profit. Honda has stated that its operating income gains by 16 billion yen ($172 million) annually for every one-yen drop in the dollar rate. And Nissan has said that every one yen gain against the dollar cuts 20 billion yen ($228 million) from its operating profit.

At today's exchange rates, Japan's export-dependent automakers are enjoying billions in what is effectively a subsidy unavailable to American producers. This makes it all the more urgent and vital that we not reach the wrong conclusion in answering Japan's bid to join TPP.

More generally, exchange rate movements can in a matter of minutes wipe out tariff and other concessions that it takes trade negotiators years to negotiate, and currency manipulation has been a longstanding problem in the Trans-Pacific region. According to a recent paper by the Peterson Institute for International Economics, at least one half of excess unemployment in the United States today is attributable to currency manipulation – 1 million to 5 million lost jobs. Given these facts, how can a meaningful TPP agreement not effectively address this major distortion to trade and investment patterns?

(3) The Auto Sector is Vital to Japan's Economy and Depends on One-Way Trade

The automotive industry is one of the Japanese economy's core industrial sectors, accounting for more than 16 percent of total manufacturing and 8.1 percent of total Japanese employment. Japan's auto sector depends for its survival on one-way trade – on a completely closed home market and deep penetration of foreign export markets. Indeed, last year, Japan's auto industry produced approximately 10 million cars – and had the capacity to produce 11 million – despite having only a 5 million domestic car market.

There is no reason to believe this imbalance will change. In fact all the signals are to the contrary, as industry titans like Toyota announce that they intend to maintain their production targets, notwithstanding demand declines in their home market.

Given the extraordinary pressure on Japanese automakers to export, the importance of the auto industry to the Japanese economy, and the fact that profit margins in the auto industry are razor-thin, we cannot doubt that eliminating the U.S. tariffs on cars and trucks are a key Japanese objective for entering TPP.

Eliminating U.S. tariffs on cars, trucks, and parts would create a windfall for Japanese producers of more than $1 billion annually. That benefit to Japanese automakers – some might call it a subsidy – should not be granted unless and until there is actual and successful implementation of reforms by Japan.

(4) <u>Past Efforts to End One-Way Trade Have Failed</u>

Virtually every prior administration has turned to negotiations to try to unlock the Japanese auto market and has failed – from the 1987 Market-Oriented Sector-Specific (MOSS) Talks on Transportation Machinery under President Reagan, to the 1989 Structural Impediments Initiative under President George H.W. Bush, to the 1995 U.S.-Japan Auto Agreement under President Clinton. Notwithstanding these efforts, at the highest levels of the U.S. government, import penetration in Japan is barely any higher today than it was in the 1960s and 1970s when Japan maintained a full slate of prohibitive measures including high tariffs, a discriminatory commodity and road tax, and other limits. In fact, at five percent, Japan has the worst level of import penetration of any of the major OECD automobile producing countries.

In light of this, what basis do we have to believe that the result in the TPP talks would be any different from the agreements that preceded it? And what is the remedy if, in fact, the Japanese market remains as closed tomorrow as it has been for the last five decades? Should we not be sure that reforms are happening – rather than simply assured that they will happen – before we proceed?

American automakers and workers have taken dramatic steps to restructure and retool the American auto industry in the aftermath of the global financial crisis, with the Administration's active support. That work has required major sacrifices from workers and the support of American taxpayers. The American middle class was built in great part on a strong U.S. auto industry that valued the contributions of its workers. And the auto industry is vital to a strong U.S. manufacturing sector. TPP must work to further strengthen our economy, our auto industry, and the working conditions of workers, not undermine them.

Sincerely,

Sander M. Levin
Ranking Member
Ways and Means Committee