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STATEMENT OF JOHN ANDREWS
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SUBCOMMITTEE ON INTERNATIONAL TRADE

Good morning, Mr. Chairman. My name is John Andrews, and I am President and CEO of ANSAC, a Webb-Pomerene Association composed of four of the largest U.S. producers of soda ash. I am pleased to have the opportunity to highlight some of the major foreign government barriers facing U.S. soda ash exports. The focus of my testimony this morning will be on such barriers in China, Brazil, and South Africa.

ANSAC – A STRONG SUPPORTER OF GLOBAL FREE TRADE

You will find no greater supporters of global free trade than ANSAC and the U.S. soda ash industry. Since ANSAC's founding, U.S. soda ash exports have increased from a base of 1.3 million MT valued at $138 million in 1984 to 4.5 million MT valued at $514 million in 2003. By any measure, ANSAC's story is an extraordinary one of exporting success. Blessed by the natural resource trona, U.S. soda ash has no competitive peer in the world. About 40% of U.S. production is exported, and soda ash contributed a surplus of more than half a billion dollars to the overall trade deficit of $536 billion last year.

This remarkable rise in U.S. exports has coincided with an equally remarkable surge in global trade liberalization and sharp reductions in once-impenetrable tariff barriers. Almost without exception, the successful efforts to eliminate or reduce government barriers to our exports have been accomplished with the efforts of the Wyoming Delegation, working closely with U.S. trade negotiators. Most recently this partnership resulted in the immediate elimination of Australia's soda ash tariff agreed to in the U.S.-Australia Free Trade Agreement (FTA) negotiations.

As you know, without the natural advantage of trona, the rest of the world produces soda ash through a synthetic process that is more expensive than American methods. In order to compete against U.S. soda ash, many inefficient foreign producers, some with connections to the highest levels of their governments, must rely on state protection to survive. They often do so to the detriment of their domestic industries and workers. Considering that soda ash comprises about 60% of the raw material cost of glass and 30% of the raw material cost of detergents, protected soda ash prices local value-added production out of export markets; subjects local value-added production to import competition, and passes higher prices on to the general population.

As tariffs fall, however, in many cases as mandated by negotiated trade agreements, governments must resort to ever-creative methods to protect inefficient domestic producers. Because of this, ANSAC strongly supports reducing the federal royalty payment in that it will contribute to making soda ash more globally competitive and better able to meet the new challenges facing U.S. exports overseas. Today I will concentrate my discussion on the illustrative examples of China, Brazil, and South Africa. These countries are prominent examples not just because of the egregious manner in which governments intervene to protect local producers but because of the substantial impact these state-sponsored measures have on U.S. exports.

Given that U.S. soda ash consumption has been essentially flat for years, it is vital that we grow exports in order to stabilize U.S. production and employment. The beneficial effects of soda ash manufacturing to the regional Wyoming economy and national economy cannot be overstated. It bears mentioning that a proposed reduction in the 6% federal royalty on soda ash, which Jim Pearce of the Wyoming Mining Association is speaking to today, will have a substantial positive impact on U.S. soda ash exports. Though the competitiveness of U.S. soda ash in the global marketplace is unquestioned, the malaise affecting other sectors of U.S. manufacturing threatens the U.S. soda ash industry as well This impacts not only the 2,300 workers directly employed in well-paying jobs right here in Wyoming but the thousands of workers employed in other soda-ash producing states, in value-added manufacturing and transportation, and in jobs dependent on the health of the regional economy. Adding insult to injury, the countries that have erected the highest barriers to U.S. soda ash in order to shield inefficient local producers are also among the largest, most-promising, and fastest growing markets in the world.

CHINA

Overall, China's policies aimed at expanding domestic production and exports have resulted in the loss of well over 1 million metric tons of business per year to this country. This, in turn, has led to hundreds of lost jobs in Wyoming and millions of dollars in lost tax revenues to the state. The U.S. soda ash industry has been at the losing end of an ambitious and targeted 15-year campaign, conducted at all levels of the Chinese government, to develop a massive domestic and export soda ash industry. This program has been an overwhelming success on almost all accounts, transforming a fledgling industry into what is now the world's largest soda ash producing nation. Since 1989, Chinese soda ash production has expanded more than three-fold from 3 million to 11 million MT in 2003 and is expected to expand by another 6.3% percent this year. Between 1999 through last year alone, annual Chinese soda ash production has expanded by more than 50%, or 3.7 million MT. By comparison, U.S. production expanded by a much more modest 0.3 million MT during the same period.

Broad and Targeted Government Intervention Shuts out U.S. Exports

China's impressive advances in soda ash production owe little to free market principles of innovation, efficiency, or profitability. Rather, since over 95% of China's soda ash is produced by state-owned enterprises, China's rise as a soda-ash producing powerhouse is a more a story of the power and efficacy of the government to intervene in the economy. China's domestic soda ash industry enjoys a level of state support that extends well beyond traditional protectionist measures such as high tariffs, which China has been obligated to gradually dismantle with its accession to the World Trade Organization (WTO).

Government-sponsored protection ranges from industry- and firm-specific support to policies of broad sectoral impact such as China's fixed exchange rate, which artificially undervalues the Chinese yuan relative to the U.S. dollar by between 15 to 40 percent, according to economists.

This undervaluation of China's currency amounts to an indirect subsidy, which negatively impacts not only soda ash but a wide range of U.S. manufacturing sectors, hurts the competitiveness of U.S. exports, and contributes to the highest bilateral trade deficits in history. Furthermore, like other state-owned firms, local soda ash producers benefit from subsidized financing from state-run banks, direct support from local and provincial governments that are driven by the need to maintain local employment, and a vertical supply-chain network of state-run firms. As has been widely documented, China's largely state-run banking system is notorious for issuing loans that do not have to be repaid, resulting in massive non-performing loan portfolios that are unsustainable and portend a potential banking crisis.

The billions of dollars of support from central, provincial, and local governments are being thrown at inefficient and environmentally-unfriendly enterprises. In effect, state support and financing is actually exacerbating larger problems pervading the rest of China's growing but fragile economy. Most of China's soda ash production is coal-based, which is notorious for its polluting effect on the environment. In fact, each ton of synthetically-produced soda ash generates a ton of calcium chloride, an environmentally-unfriendly byproduct. Chinese producers do not have to be concerned with complying with environmental laws or regulations. Moreover, since almost all producers are state-owned, profitability incentive and shareholder accountability are oftentimes elusive concepts, and many firms, especially smaller plants propped up by local governments, are simply money-losing vehicles for employment. The rapid expansion of inefficient Chinese production simply exhausts scarce Chinese capital, strains an already fragile banking system, and inefficiently allocates employment towards unproductive sectors.

U.S. Share Plummets While Chinese Soda Ash Demand Grows at Extraordinary Rates

Were it not for extraordinary levels of government protection and state support for domestic producers, China would be one of the largest and most promising foreign markets for U.S. soda ash. Already the world's largest soda ash market, Chinese soda ash consumption expanded by 18% in 2002 and by another 8% last year. Conversely, the U.S. share of the Chinese market has declined dramatically. In 1989, U.S. soda ash captured a 30% share of the Chinese market; 15 years later, our share stands at barely more than 1%. Though Chinese consumption has expanded from 4.0 million MT in 1989 to 10.1 million MT last year, a staggering 143% increase, the actual quantity of U.S. soda ash exports has <u>declined</u>, from 317,000 MT in 1989 to 280,000 MT last year. U.S. soda ash exports are expected to fall by another 30 to 40 percent this year, even though Chinese demand is expected to expand by another 2.2 million MT over the next four years, making China one of the few world markets expected to show solid growth in demand. To put these growth figures in perspective, 2.2 million MT equates to <u>35% of total U.S. consumption</u> in 2003.

Planned Capacity Expansions Far Outpace Projected Demand

While consumption growth is impressive, the Chinese soda ash industry plans to increase capacity at rates far outpacing projected demand. According to industry estimates, China is set to boost annual capacity by an additional 1.1 million MT this year and by 3.3 million MT (both over 2003 levels) by 2007. (To put these figures in perspective, 3.3 million MT equates to <u>52%</u>

of total U.S. soda ash consumption last year.) Given that demand is only expected to increase by 2 million MT, this excess soda ash, much of it financed by subsidized bank lending and indirect state support, will end up being exported at cut-rate prices to third-country markets in Northeast and Southeast Asia.

Chinese Exports are Eroding U.S. Share in Critical Third-Country Markets

While penetrating the Chinese market is difficult enough, U.S. exports are facing an increasing competitive threat from Chinese exports in third-country markets in East Asia and Latin America. Chinese exports have grown dramatically, doubling in the last five years, with rapid increases in production capacity. As of last year, about 11% of Chinese production was exported, yet this figure promises to grow with planned capacity additions over the next several years. Over 90% of Chinese exports are to key Asian markets such as Japan, Korea, and Southeast Asian countries such as Indonesia, Thailand and the Philippines. The trend has been dramatic in what were once the largest markets for U.S. soda ash. In 1996, the top four global markets for U.S. soda ash were Indonesia, Korea, Japan, and Thailand, respectively. Combined, they accounted for $190M in exports, comprising 37% of total U.S. exports. By 2003, this share had fallen to $106M, a drop of 44% over 1996 levels, and down to a 21% share of U.S. exports. Excluding Japan, which has stronger demand for higher-quality soda ash, the drop in exports to Indonesia (7th largest market in 2003), Korea (8th largest), and Thailand (13th largest) has been a staggering 54% over 1996 levels.

Addressing Broad Market Access Barriers Is a Challenge

Many of the government-imposed barriers restricting U.S. exports have a broad sectoral impact and are not directed at soda ash specifically. Given the pervasive nature of Chinese government protection and support of its soda ash industry, the U.S. industry shares the U.S. government's frustration at addressing market access barriers via specific policy prescriptions. Statutory protection, such as import tariffs, is easily quantifiable and addressed. In China's case, however, the 5.5% import tariff, while it does restrict trade is not the most significant barrier facing U.S. exports. Rather, soda ash is impacted by broad protectionist policies such as use of a fixed exchange rate that artificially undervalues the Chinese yuan relative to the U.S. dollar. Undervaluation of the yuan severely impacts all U.S. manufacturing sectors, not just soda ash, by hurting the competitiveness of U.S. export in China and by giving Chinese producers the advantage of a *de facto* 15-40% subsidy when importing to the United States. The U.S. soda ash industry strongly encourages efforts by the Administration and a bipartisan consensus in the U.S. Congress to push China towards market-based exchange rates and, at a minimum, a substantial upward adjustment in the fixed exchange rate. The U.S. industry would also benefit from greater transparency in the application of rule-of-law, a significant reduction in direct and indirect subsidization of industry, and most importantly, a rapid transition to a market-based economy, but it is fully cognizant that these changes are not forthcoming in the near future.

U.S. Industry Policy Proposal to "Level Playing Field" in Third-Country Markets

The fact remains that Chinese government officials and their provincial and local counterparts view soda ash as a vehicle for employment tens of thousands of Chinese workers and are unlikely to grant significant access to U.S. soda ash willingly. One area that can be addressed through targeted policy is in China's value-added tax (VAT) export rebate program. China currently offers a partial refund of the 17% VAT paid on soda ash that is exported or included in value-added products such as glass that are exported. China recently reduced the refund amount from about 87% of the total VAT paid down to 76%, primarily for fiscal reasons. The U.S. industry believes that one potential area of compromise rests in the elimination or a further significant reduction in the VAT rebate program for soda ash specifically. Implementing such a measure would: have a strong positive fiscal impact for the Chinese government; have no impact on the 10 million MT and growing domestic Chinese market; and allow U.S. soda ash to compete on a more level-playing field in critical East Asian third markets.

BRAZIL

Unlike China, Brazil resorts to more overt forms of government intervention to protect inefficient local soda ash production. These measures are easily shown to violate its WTO treaty obligations. Brazil was the fourth largest market for the U.S. soda ash industry in 2003, accounting for 312,000 MT valued at $44 million. But for more than 15 years, Brazil's sole soda ash producer Alcalis, formerly a state-owned company, has sought numerous and most recently creative ways to keep U.S. soda ash from competing in the Brazilian market on a level playing field. These efforts have included: (1) raising the country's import tariff from 10% to 25%, (2) filing an unsuccessful antidumping complaint, and (3) in its most recent and imaginative protectionist display yet, securing a state-level tax break that favors local production over imports. This would be like the state of Wyoming imposing a sales tax on Brazilian orange juice that is much higher than that imposed on orange juice from the United States.

Discriminatory ICMS Tax Protects Inefficient Local Soda Ash Producer

In April 2001, Brazil's State of Rio de Janeiro granted the local producer of soda ash a preferential rate for the Merchandise and Service Circulation Tax (ICMS), which is applied to both imports and domestic products. The ICMS rate for the local producer is 2%, while all other (imported) soda ash faces a 19% ICMS tax in Rio de Janeiro (the rate was increased from 18% in January, 2003) and similar high rates in the rest of Brazil. This 17 percentage point tax differential provides Brazil's sole domestic soda ash producer, Alcalis, a *de facto* subsidy estimated to range between $16-18 per metric ton. This allows Alcalis to retain market share at the expense of foreign suppliers. The discriminatory ICMS tax provisions flatly violates the WTO's national treatment provisions (GATT 1994, Article III), which specify that internal taxes must be equally applied to domestically-produced and imported goods.

The U.S. industry estimates that the impact of this discriminatory tax is lost exports of up to $15 million. Furthermore, the discriminatory tax has cost the state of Rio approximately $5 million in lost tax revenues.

U.S. Government Assistance is Needed

The U.S. industry has engaged the U.S. government for assistance since November of 2001. ANSAC and its member companies have met with senior officials in the Office of the United States Trade Representative and Commerce Departments to request that the U.S. government issue a demarche to the Brazilian government, requesting an official explanation and consultations on the matter. Letters encouraging the Administration to support the U.S. industry's efforts have been written to United States Trade Representative Robert Zoellick from the Wyoming Congressional Delegation and Senators Smith and Wyden from the state of Oregon.

The merits of this case bear a strong resemblance to a WTO case brought by the United States last month involving China's discriminatory taxes assessed on semiconductors. While the industry has also submitted a draft Section 301 petition to the Office of the U.S. Trade Representative, the intention of the U.S. industry is to resolve this matter through bilateral consultations and not via a trade war. After months of efforts, the U.S. government is to issue a demarche to the Government of Brazil, and hopefully consultations are forthcoming.

SOUTH AFRICA

South Africa presents yet another illustrative case study in how ever-creative forms of government intervention are used to protect favored producers with the aim of shutting U.S. soda ash out of the market. The decline in U.S. exports to South Africa, once one of the largest foreign markets, has been precipitous. This decline coincides with the formation in 1991 of a the politically connected soda ash producer (SAB) now Botash which is jointly owned by the Government of Botswana, the South African mining firms DeBeers and Anglo American, and a consortium of South African banks. In 1990, the year before Botash's precursor was formed, South Africa was the third largest export market for U.S. soda ash with $27.2M in exports. Last year, exports were $8.2M, a decline of 70%, pushing South Africa down to the 21st largest export market.

Evolving Protectionism Impedes Market Access for U.S. Soda Ash

Like Brazil and China, traditional import tariff protection has lost its efficacy with global trade liberalization. Prior to 1991, U.S. soda ash entered the South African market duty-free. With the formation of Botash's precursor SAB, however, the South African Government temporarily raised tariffs to 10% and had them permanently reinstated in 1994. Even with tariff protection, SAB was faced with bankruptcy and reformed as Botash in 1995. As mandated under its WTO Uruguay Round commitments, however, South Africa was obligated to reduce its soda ash tariff from 10% down to 5.5% by 2004. Nevertheless, Botash was able to obtain a five year standstill agreement keeping the tariff at 10% until January 2000.

Sensing the impending impact of trade liberalization and its competitive pressure, Botash initiated a baseless legal action under South African competition laws, which threatens to shut ANSAC out of the market. As with China and Brazil and numerous other global markets, the motives of protectionism are misguided and myopic. As Botash's only significant competition, removing ANSAC from the market would give Botash monopoly pricing power over its glass, detergent, and other customers. Higher prices would be passed on to South African consumers and price South African glass and detergent exports out of world markets. The impact on South Africa's workforce is further devastating, given that 75,000 South Africans are employed in the domestic glass industry and thousands more in other soda ash-dependent sectors such as detergent production. The Botash soda ash mine, which is actually located in Botswana, employs only 500 workers but presumably few South Africans.

SACU FTA Negotiations Provide Significant Leverage

South Africa, along with four neighboring countries that together comprise the South African Customs Union (SACU), is negotiating a free trade agreement with the United States. The United States should not sign free trade agreements with countries that refuse to recognize key aspects of U.S. law and that employ government intervention, including the use of its judicial system, to protect their markets from competition. Therefore, the U.S. industry's goals in U.S.-SACU FTA negotiations are: (1) to achieve an immediate elimination of the 5.5% SACU duty, and (2) to obtain commitments that South African laws not be enforced in a manner that conflicts with U.S. export promotion laws and that their laws aimed at fostering competition not be used to restrict U.S. trade.

CONCLUSION

In closing, I want to thank you for the opportunity to present the views of ANSAC. The U.S. industry has a global competitive advantage in soda ash production, and you will find no greater supporter of global free trade than ANSAC. With the support of the Wyoming Delegation, U.S. negotiators have accomplished much in bringing down market access barriers worldwide. However, as these barriers have come done significant and, in many ways, more daunting challenges remain. Once again, Mr. Chairman, I want to thank you and the Wyoming Delegation for your steadfast support of the U.S. industry and for giving me the opportunity to speak today.