Executive Memorandum
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# THE STOCK MARKET'S MESSAGE TO CONGRESS ON FAST TRACK

Robert P. O'Quinn
Policy Analyst

On Monday, October 27, 1997, stock markets melted down around the world. The closely watched Dow Jones Industrial Index plummeted by 555.26 points, or 7.18 percent, to 7161.16 in its largest single-day point decline and ninth-largest single-day loss in market value. Although the market rebounded a day later, economists attributed the turmoil in part to investors' fears that Asia's financial crisis will slow economic growth in the United States as demand for U.S. exports and investment in Asia drops.

But U.S. investors also should be concerned about the diminishing prospects for passage of fast-track trade negotiating authority. Failure to pass fast track would deny the United States the ability to open new markets to American exports and investment as established Asian markets shrink. To minimize damage to the U.S. economy from the Asian crisis, President Clinton should press Congress to pass fast-track legislation immediately, and Asian countries to liberalize their banking markets in the ongoing World Trade Organization (WTO) financial services negotiations.

**Trade Spurs U.S. Economic Growth.** International trade and investment are increasingly important to American well-being. Two-way international trade, broadly defined, comprised 13 percent of U.S. gross domestic product (GDP) in 1970. Expanding twice as fast as GDP over the next quarter-century, it exploded to 30 percent of GDP by 1996. U.S. exports of goods and services reached a record $836 billion in 1996, employing 16.7 million American workers. The Clinton Administration estimates that more than 25 percent of all U.S. economic growth during the past four years is directly attributable to the 35 percent rise in American exports since 1992.

Booming Asian economies and successful trade liberalization—particularly the North American Free Trade Agreement (NAFTA) and Uruguay Round Agreements—fueled America's export-led expansion. Asia supplanted Europe as the largest U.S. regional export market, accounting for 33.7 percent of U.S. two-way trade. More than 4 million American jobs now depend on exports to Asia.

**Asia's Sick "Tigers."** Southeast Asian countries developed serious banking and monetary problems in the mid-1990s. Governments compelled local banks to extend below-market interest rate loans to politically connected individuals, companies, or industries with little regard to their ability to service debt. They also largely closed their financial services markets to American and other foreign firms so their citizens would have to continue to rely on local banks. As many banks began to sink under the weight of bad loans, governments looked the other way.

Southeast Asian central banks tried to maintain fixed exchange rates between local currencies and the U.S. dollar while inflating their local currencies through massive credit expansions. As pressure built, Thailand was forced

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to break its dollar peg on July 2 and allowed the Baht to depreciate. Indonesia, Malaysia, and the Philippines soon followed. Throughout Southeast Asia, local companies had contracted loans in U.S. dollars or Japanese yen. As local currency values collapsed, the real value of foreign-denominated debt skyrocketed, putting many firms into bankruptcy. Accustomed to 6 percent to 10 percent annual growth, Indonesia, Malaysia, the Philippines, and Thailand will suffer economic slowdowns or recessions during the next two to three years, causing American trade with Southeast Asia, which had ballooned by 59 percent between 1993 and 1996, to rise far more slowly. Investors consequently downgraded their sales and profit expectations for major American companies that trade with Asia, driving down share prices.

**No Fast Track?** The other pillar of export-led expansion—trade liberalization—was under assault in the House of Representatives. For nine months, Representative Richard Gephardt (D–MO) and the AFL–CIO leadership mounted a campaign against fast track. When the Administration and House Republican leaders finally agreed on fast-track language on October 8, proponents hoped that the President finally would launch a counterattack to win the Democrat votes needed to pass fast track. Instead, he has wasted his energy on less pressing issues like global warming. If fast track is not passed this year, investors fear that it will not be brought up again until 2001, after the next presidential election.

Despite the common misperception, fast track is not just a hemispheric issue. President Clinton needs it to enter negotiations for a Free Trade Area of the Americas and to expand NAFTA in 1998 to include Chile. But he also needs it to extend NAFTA across the Pacific to embrace Australia and New Zealand and to begin new WTO negotiations in 2000. Thus, without fast track, the trade liberalization that investors have counted on to sustain economic expansion into the next century might not occur.

**Action Needed.** As the stock market meltdown shows, Asia's financial crisis threatens export-led U.S. economic expansion. Without trade liberalization, Asia's problems eventually could send the U.S. economy into recession. The President therefore should:

- **Make fast-track legislation a top priority.** President Clinton should make an all-out effort to convince Democrats in Congress to approve fast track.

- **Press Asian countries to liberalize their financial markets in the ongoing WTO financial services negotiations.** Opening Southeast Asian financial services markets would let American banks rescue failing local banks, thereby speeding a general economic recovery. Without foreign capital, Southeast Asian countries may be unable to find enough local investors to restore these banks to financial health. And without sound banking sectors, their economies will continue to limp along at the brink of recession for years just as Japan has done in the 1990s.

"The astounding worldwide stock market turmoil of the past week signals a watershed in global economic development," observes *Los Angeles Times* Senior Economics Editor James Flanigan. "It is a demand by global investors that all countries adapt their economies to the dictates of open markets." In other words, the U.S. economy is linked to the Asian (and global) economy and must grow by expanding into global markets. Every Member of Congress should know that denying the President fast-track authority, and subsequently not expanding U.S. trade agreements, could help cause a U.S. economic recession in two or three years. To shield America from Asia's economic hard times, fast track is essential.