

**“BREXIT and Future US Trade Policy:
What Impact on the Global Economic Outlook?”**

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Global Economic Growth

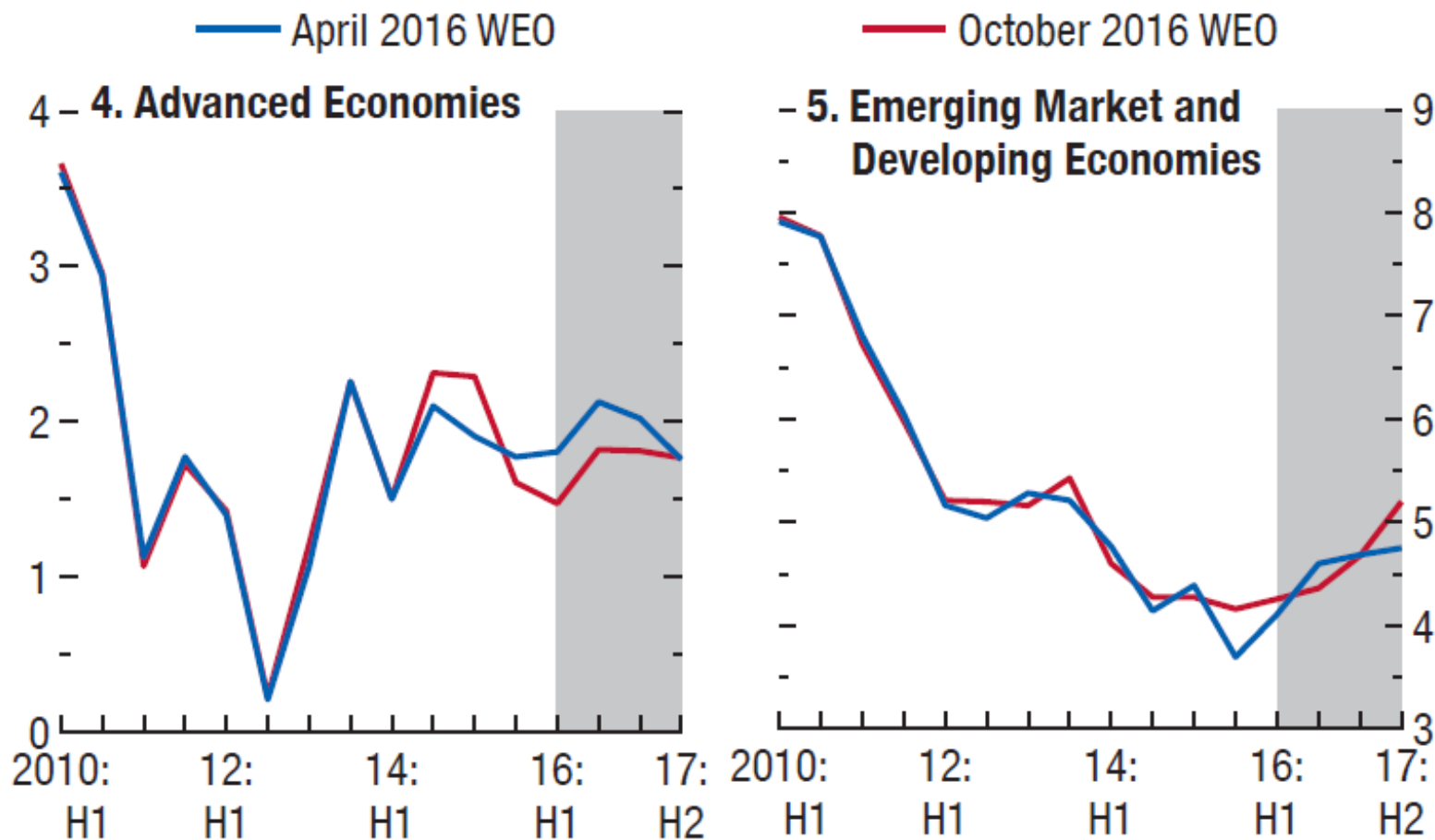


- **World output forecast to grow by 3.4% in 2017**
- **Emerging/developing market economies (4.6%), and advanced economies (1.8%)**
- **Pace of growth will vary across advanced economies: picks up in US (2.2%), slower in euro area (1.5%), and weak in Japan (0.6%)**
- **Resilience in Asia (6.5%), India (7.6%), China (6.2%), and improvement in stressed economies, e.g., Brazil (0.5%), and Russia (1.1%)**



Economic Growth Breakdown

GDP Growth (Annualized semiannual % change)



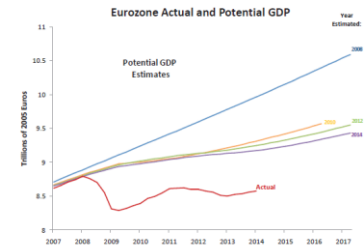
Source: IMF WEO (October 2016)

Downside Risks



- For many advanced economies: *secular stagnation*
- China's ongoing adjustment: potential for spillovers
- Inward-looking trade policies:
 - BREXIT vote in UK – creating uncertainty
 - Non-ratification of Trans-Pacific Partnership (TPP) and likely failure of Trans-Atlantic Trade and Investment Partnership (TTIP) negotiations
 - US moves toward protectionism

“Secular Stagnation”?



- Why have many economies not returned to pre-crisis growth rates despite near-zero interest rates?
 - Potential long-run growth rate may have fallen – slowdown in growth of productive inputs and technological progress (Gordon, 2014)
 - Persistent output gaps - weak private demand (Eggertsson and Summers, 2016))
 - Damage to potential output – unemployment has resulted in depreciation of human capital and “loss of talent” (Glaeser, 2014)

Implications of “Secular Stagnation”

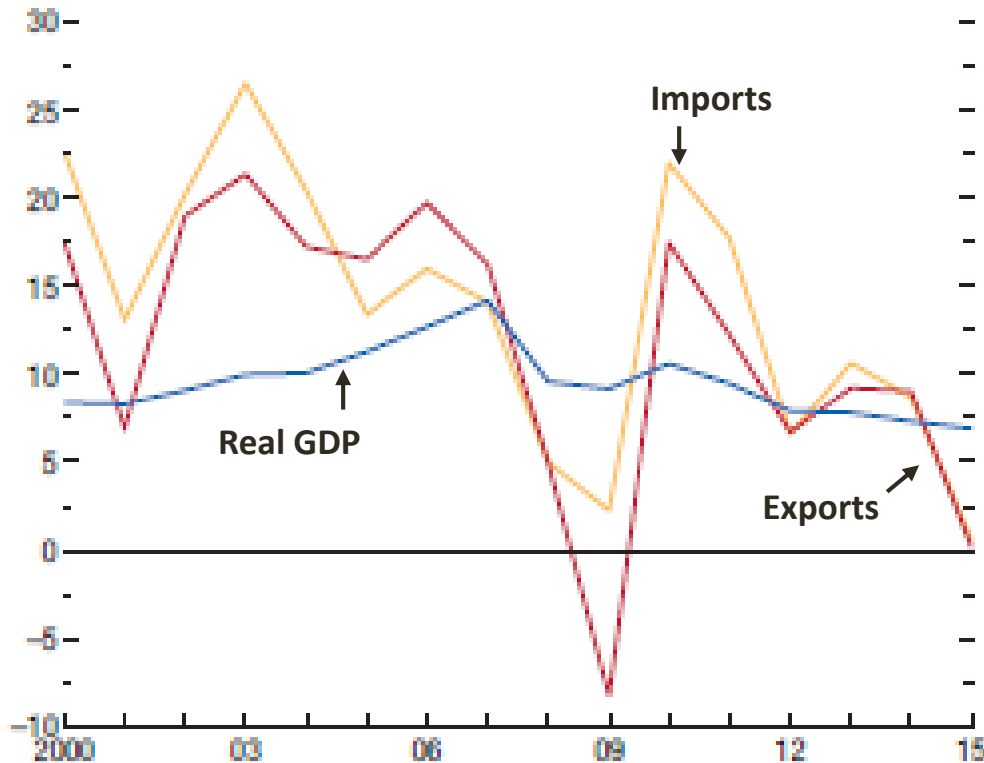


- Negative real interest rates may be needed to equate savings and investment with full employment - boost investment and discourages saving
- Harder to achieve full employment with low inflation and zero lower bound on policy interest rates
- If there is deflation, negative real rate of interest is arithmetically impossible
- May be difficult to achieve full employment, satisfactory growth and financial stability through conventional monetary policy

Chinese Economic Adjustment



China: GDP and Trade Growth
(% change, year on year)



- China in transition to services/consumption-based economy
- Impact on prices, trade, and profits across many global industries
- Will also affect asset prices, and investor sentiment

Source: IMF WEO (October 2016)



BREXIT – Creating Uncertainty

- UK Treasury (May 2016) focused on near-term impact of UK leaving EU over two-year period
- Evaluated combined effects of *transition* to new trading arrangement, *uncertainty* and feedback from changing *financial conditions*
- Two scenarios: “shock” assuming UK negotiates bilateral agreement with EU, and “severe shock”, assuming default to WTO membership
- Ignores additional downside risks of financial crisis and/or “sudden stop” due to current account deficit

BREXIT – Creating Uncertainty



Table 1: Immediate impact of BREXIT on UK after 2 years		
	“Shock”	Severe shock”
GDP	-3.6%	-6.0%
Inflation rate (% points)	+2.3	+2.7
Unemployment rate (% points)	+1.6	+2.4
Sterling exchange rate index	-12%	-15%

Source: UK Treasury (May, 2016)

BREXIT – An Object Lesson?



Table 2: Effect on UK trade/FDI/productivity/GDP after 15 years

	EEA	Bilateral	WTO
Trade (%)	-9	-19	-24
FDI (%)	-10	-20	-26
Productivity (%)	-2.8	-6.0	-7.7
GDP level (%)	-3.4 to -4.3	-4.6 to -7.8	-5.4 to -9.5

Source: UK Treasury (April, 2016)

BREXIT and UK Agriculture



- **Brexit means change in both trade relationship with EU, and nature of UK farm policy**
- **Due to UK being net importer of agricultural products from EU, average prices expected to increase by 5% (bilateral) and 8% (WTO) (van Berkum *et al.*, 2016)**
- **Increased trade costs and loss of access to import concessions under TRQs (sugar, dairy products)**
- **Farm income effects of higher UK prices will likely be offset by reduction in direct payments to farmers**

End of Regionalism for US?



- **TPP, signed in October 2015 covering US and 11 other countries, will not be ratified by Congress**
- **Forgoing expected \$130 billion increase in US GDP by 2030 (Petri and Plummer, 2016)**
- **TTIP negotiations between US and EU will likely not be concluded**
- **TTIP estimated to increase GDP/capita in long run by 4.9% in US, and average of 3.9% across EU member countries (Felbermayr *et al.*, 2015)**



US Agriculture: TPP and TTIP

- By 2025 TPP was expected to increase US agricultural exports by \$2.8 billion – a 33% increase in export market share (USDA/ERS, 2014)
- US agriculture would have gained market access to countries where it has no FTA, notably Japan
- EU has higher average agricultural import tariffs against US (12.9%) compared to the reverse (6.4%)
- TTIP forecast to generate higher agricultural export growth than TPP – 159% for US compared to 56% for the EU (Disdier *et al.*, 2015)



Wider Consequences of No TPP

- TPP had potential to impact future of Asia-Pacific trading system - template for regional integration
- Provided model for consolidating existing FTAs – i.e., way out of Asia-Pacific *noodle bowl*
- “...an American failure to ratify TPP would bring about the very thing critics of trade deals complain about: a more empowered China and bad terms for US goods and services...” (Singapore Prime Minister)
- Happening when growth in global trade slower than GDP growth for first time in 15 years (IMF, 2016)

Does Trade Affect Jobs?



- ***Number* of jobs a macroeconomic phenomenon, dependent on actions of Federal Reserve, i.e., trade affects composition *not* overall number**
- **Consensus that technological change *not* trade primary driver of recent US labor market changes**
- **However, China's accession to WTO contributed to surge in US imports, negatively affecting US manufacturing employment and wages**
- **1999-2011: US manufacturing employment declined by 5.8 million, $\approx 10\%$ due to Chinese import penetration (Acemoglu *et al.*, 2016)**



Possible Trade War?

- **Incoming administration *could*:**
 - **Place 35% tariff on Mexican imports**
 - **Place 45% tariff on Chinese imports**
 - **Renegotiate free trade agreements (FTAs)**
 - **Withdraw from WTO**
- **US statutes might allow higher import tariffs – Trade Expansion Act (1962) and Trade Act (1974)**
- **US can withdraw from NAFTA after 6 months notice – tariffs would revert to MFN rates**



Potential Effects of Trade War

- **Noland *et al.* (2016) simulate two scenarios:**
 - **“full trade war” – US employment falls by 4.8 million by 2019 due to recession, many states incurring reduced employment, e.g., Ohio 4%**
 - **“aborted trade war” – employment falls by 1.3 million, tariffs being removed after a year**
- **Estimates ignore: (i) role of global supply chains, (ii) renegotiation of FTAs/withdrawal from WTO, and (iii) impact of uncertainty on investment**