UNDERSTANDING THE ECONOMIC AND POLITICAL EFFECTS OF TRUMP'S CHINA TARIFFS

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Although President Trump has persistently claimed that China is paying billions of dollars in tariffs imposed on Chinese imports to the United States, empirical evidence indicates that U.S. consumers are bearing the cost of the tariffs. The unilateral power-based approach to trade used by the Trump Administration has also resulted in unexpected economic and political costs in key Midwestern states that helped propel Trump to the U.S. presidency in 2016. These costs have led to reverses for the Trump Administration in the mid-term elections of 2018 and could ensue in further electoral losses.

As both political parties currently hold little affection for China, the United States could continue to use tariffs against China as trade policy no matter which party controls the U.S. presidency. For these reasons, a study of how to most effectively use a power-based approach to trade is both useful and timely.

This study indicates that a power-based approach can be used most effectively against countries that lack either the economic power or the political will to engage the United States in a prolonged trade standoff. While most nations appear to fall into one or both of these categories, China is not one of them. China has the economic power to fight a trade war and China believes that it must stand up to the United States. When used against China, the power-based approach carries greater risks because its economic and political effects are difficult to predict and because this approach is inherently more uncertain than the cooperative approach of the World Trade Organization that the United States has rejected. Using a power-based approach against China could backfire because China has the economic power and political will to endure a prolonged battle and play a dangerous game of mutual pain and destruction with the United States.

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I. INTRODUCTION

The Trump Administration has persistently boasted that the billions of dollars in punitive tariffs imposed on imported Chinese goods as part of the U.S.-China Trade War begun in 2018 are being paid by China to the U.S. Treasury. For example, on February 14, 2020, President Trump stated the following in his remarks to state governors:

> China is paying us, right now, billions and billions of tariffs a month. Every month, billions of dollars. I love it. Personally, I love it. But they're paying billions of dollars. And it's hurting them; it's not good for them.[1]

Trump has made this bold claim repeatedly without offering any explanation or elaboration.[2] Yet, this claim is inconsistent with orthodox economic theory, widely accepted by economists and trade lawyers alike, which holds that the consumers of the country imposing the tariffs -- the United States -- bear the brunt of the tariffs.[3]

Under orthodox theory, a tariff is a tax on an import that must be paid before the import is allowed to exit the customs port of entry and enter into the internal market.[4] The importer of record, a U.S. entity, must pay the tax (or post a bond).[5] The exporter is not responsible for the tariff,

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[1] Brooks Jackson, *Does China Pay Tariffs?*, FACTCHECK.ORG (Feb. 28, 2019), https://www.factcheck.org/2019/02/does-china-pay-tariffs/. A more detailed breakdown of the tariffs in set forth below. *See infra* Part III.

[2] Trump has made this claim over 100 times. *See* Ben Werschkul, *Trump Made This False Claim About China and Tariffs at Least 108 Times in 2019*, YAHOO (Dec. 27, 2019), https://www.yahoo.com/now/trump-has-made-this-false-claim-about-china-and-tariffs-at-least-100-times-182318319.html (noting that Trump claimed at least 108 times n 2019 that China was paying for tariffs).

[3] DANIEL C.K. CHOW & THOMAS J. SCHOENBAUM, INTERNATIONAL TRADE LAW 201–02 (3d ed. 2017). Most observers reject this claim and assert that U.S. consumers are paying for the tariffs. *See* Jeanna Smialek & Ana Swanson, *American Consumers, Not China, Are Paying for Trump's Tariffs*, N.Y. TIMES (Jan. 6, 2020), https://www.nytimes.com/2020/01/06/business/economy/trade-war-tariffs.html; Howard Schneider, *Americas Not Chinese Pay Trump Tariffs, NY Fed Says*, REUTERS (Nov. 25, 2019), https://www.reuters.com/article/us-usa-fed-tariffs/americans-not-chinese-pay-trump-tariffs-ny-fed-study-idUSKBN1XZ2A4; Asher Stockler, *New Study Confirms That Trump's Claim About China Paying for Cost of U.S. Tariffs Is Untrue*, NEWSWEEK (Aug. 7, 2019), https://www.newsweek.com/trump-trade-war-china-tariffs-study-1453160.

[4] CHOW & SCHOENBAUM, *supra* note 3, at 213.

[5] *Id.* Most exporters and importers will hire a freight forwarder, a professional service provider, to handle the logistics of the export-importer transaction, including compliance with Customs. On the export side, the freight forwarder handles the customs issues for the exporter and arranges for multimodal transportation, including ocean carriage and inland transport (and insurance if required) of the goods from the nation of the exporter to the nation of the importer. On the import side, the freight forwarder will file the paperwork for the importer with Customs and pay the tariff or post a bond. The freight forward makes the initial tariff

which is normally the responsibility of the importer.[6] The importer then normally passes on the cost of the tariff by including it in the price charged to the wholesale distributor or retailer of the goods.[7] In turn, the distributor or retailer then passes on the cost of the tariff to the consumer, the ultimate purchaser.[8] All domestic producers protected by the tariff, efficient and inefficient alike, will also raise their prices so that the tariff acts as a subsidy to all domestic producers and the increase in domestic prices is an additional "tax" on consumers.[9] The tariff can also have a negative impact on the country of the exporters as it reduces demand for their products; tariffs are a form trade protectionism that protects domestic industry by limiting import competition.[10]

The tariff that is collected by the Customs authorities is revenue for the U.S. government that is paid by the consumer, who ultimately bears the cost.[11] The standard textbook result is that the gains to the U.S. government and domestic producers are less than the loss to consumers resulting in an overall deadweight loss to the U.S. economy.[12] Although the tariff normally results in a deadweight loss, the tariff could have highly visible beneficial effects on the protected domestic industry, especially if it was in obvious financial distress.[13]

Although this is an overview of how most economists view the costs of tariffs, this is a theory of rational human behavior that can, of course, vary in any particular case. If the tariff is a temporary measure, it is possible that the importer or the distributor might decide to absorb the cost of the tariff or pass on only a portion of the tariff to the consumer. This would mean that the importer or distributor would earn lower profits, but such a decision can be a rational one if the market conditions dictate, for example, that either no increase or only a small increase in price will be tolerated by consumers in the short term. It is also possible that the exporter will discount its prices, at least temporarily, to the U.S. importer to help offset the price increases to the distributor or consumer. The exporter might also agree in the sales contract to reimburse the importer in part or in whole for the tariff paid.[14] At this point, the costs of the tariffs are shared between the exporting nation and the importing nation. In all scenarios, a change in any of these variables will affect the ultimate costs of the tariffs and who bears them. Basic economic theory also does not

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determination and calculation of the tariff. The final computation of the tariff, made by U.S. Customs authorities, is called "liquidation" and full payment of the tariff must be made before the goods are released. Computation can take several days or longer so most importers will file a summary entry form and post a bond as security for the tariff due that will allow the goods to be immediately released. *See id.*

[6] *Id.* at 213.

[7] *Id.* at 201–02, 213–14.

[8] *Id.*

[9] CHOW & SCHOENBAUM, *supra* note 3, at 201. Efficient producers are those low cost producers that, due to superior technology or management, are not harmed by the imports. They do not need the protection of the tariff and do not need to raise their prices because they are already profitable. Only inefficient high cost producers need the protection of the tariff. However, because the tariff on the imports and price increases by inefficient producers allow them to increase prices, most efficient producers will raise their prices in order to earn higher profits.

[10] *Id.* at 202.

[11] *Id.* at 201.

[12] *Id.* For one view of the economic losses and the effect on GDP, see Erica York, *Tracking the Impact of U.S. Tariffs and Retaliatory Actions*, TARIFF FOUNDATION (Feb. 14, 2020), https://taxfoundation.org/tariffs-trump-trade-war/.

[13] CHOW & SCHOENBAUM, *supra* note 3, at 202.

[14] *See* Century Importers, Inc. v. United States, 205 F.3d 1308 (2000) (under sales contract, importer paid the tariff to clear customs but would later be reimbursed by exporter).

account for any political effects of tariffs, such as on mid-term U.S. elections in 2018. Only an in-depth empirical study of these variables can clarify which entity or entities bear the cost of the China tariffs imposed by the Trump Administration, the total amount of the costs, particular industries or groups bearing disproportionate costs, and the political effects of the tariffs.

This Article sets forth the results of detailed empirical economic studies of the redistributive effects of the U.S. tariffs imposed on Chinese imports by the Trump Administration as part of the ongoing U.S.-China Trade War that began in 2018.[15] The Article also examines the economic effects of the retaliatory tariffs imposed by China on U.S. imports.[16] In addition, as the economic effects of tariffs often have political consequences, this Article also examines the political effects of the China tariffs in post-2016 elections, including the mid-term elections of 2018.[17] This study is timely because the United States is likely to continue to use tariffs as a matter of trade policy against China, no matter which political party controls the U.S. presidency. In setting forth this study, this Article emphasizes the following three major points.

First, the Trump Administration's power-based approach to tariffs, which involves the unilateral imposition of punitive tariffs, often without legal justification, is most effective when the targeted nation, as in the case of South Korea, immediately capitulates and offers trade concessions.[18] A power-based approach is less effective against a country like China, which for economic and political reasons, refuses to immediately make concessions to avoid punitive tariffs, but is willing to engage the United States in a prolonged standoff. In the case of the China tariffs, empirical analysis shows unequivocally that the cost of the tariffs has been passed almost entirely to the U.S. consumer, contrary to the assertion of the Trump Administration.[19] In addition to saddling U.S. consumers, the tariffs have resulted in a deadweight loss (or aggregate loss) of $7.3 billion to the U.S. economy.[20] At the same time, China has also suffered economic losses as the tariffs have reduced demand for Chinese imports, leading to a contraction in China's export driven economy for this same period.[21] The China tariffs indicate that when the targeted country engages the United States in a standoff, the economies of both countries suffer mutual destruction by the unilaterally U.S. imposed tariffs. The country that concedes first and capitulates will be the country that is unable or unwilling to bear further economic harm. As the United States has the most powerful economy in the world, the United States may be able to use a power-based approach against many, if not most, other countries as these countries may lack the economic power or political will (or both) to engage the United States in a standoff.

Second, when the targeted country not only engages the United States in a prolonged standoff but also imposes retaliatory tariffs on the United States, the economic effects become even more unpredictable and uncertain.[22] In the U.S.-China Trade War, China has imposed retaliatory tariffs on U.S. agricultural products to cause maximum pain and distress. U.S. agricultural exports, such as soybeans, are particularly vulnerable to retaliation as China buys

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[15] *See infra* Part III.

[16] *See id.*

[17] *See id.*

[18] For a detailed discussion of South Korea and U.S. trade pressure, see *infra* Part IV.

[19] *See infra* Part III.

[20] *See id.*

[21] Kenneth Rapoza, *Here Is How China is Really 'Paying' for Tariffs*, FORBES (May 17, 2019), https://www.forbes.com/sites/kenrapoza/2019/05/17/here-is-how-china-is-really-paying-for-tariffs/#11711b3a1fae.

[22] *See infra* Part III.

about 50 percent of all U.S. soybean exports.[23] Although the costs of the tariffs on U.S. agricultural imports will also be passed on to Chinese consumers, China has been able to avoid the bulk of these ill effects as China has met its demand through trade diversion, i.e., by buying soybeans from other sources, such as Brazil and Argentina.[24] The data indicate that significant volumes of trade in soybeans has been diverted from the United States mostly to Brazil and other countries.[25] For the United States, the result of the China retaliatory tariffs on soybeans and other agricultural products is reduced demand for U.S. production.[26] The reduction in U.S. exports to China has also caused additional economic harm that must be added to the economic harm caused to U.S. consumers by the U.S. tariffs on Chinese imports. The additional harm from retaliation to the United States could tip the balance of harms in favor of the targeted nation in some cases.

Third, the political effects of the tariffs and retaliatory tariffs of the U.S.-China Trade War were also hard to predict at the start of the conflict. The data indicate that much of the economic harm from both the U.S. imposed tariffs and the retaliatory tariffs has been concentrated in the Midwestern region of the United States that helped propel Trump to the presidency in the 2016 election.[27] The United States has attempted to offset some of these harms by providing subsidies, i.e., financial payments, to U.S. farmers, but the subsidies have been unable to completely offset losses.[28] The United States has also attempted to ameliorate the harm caused by China's agricultural tariffs by extracting a commitment from China to purchase in 2020 and 2021 respectively, $36.5 and $43.5 billion in U.S. agricultural products under the 2020 U.S.-China Trade Agreement (USCTA) reached on January 14, 2020.[29] However, the data also indicate that it is unlikely that China will be able to fully meet these commitments and that the effects of the retaliatory tariffs will continue to burden key Midwestern states.[30] These data indicate that the U.S.-instigated trade war with China may backfire on the Trump Administration by eroding support in states that voted for Trump in 2016.[31] These data also indicate that the use of a power-based approach to trade is risky and can lead to unpredictable and unintended consequences when the targeted nation has the political will and economic ability to engage in a prolonged standoff with the United States.

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[23] *Id.*

[24] *Id.*

[25] *Id.*

[26] *Id.*

[27] *Id.*

[28] *See infra* Part III.

[29] The USCTA also suspended some of the U.S. tariffs and China also agreed to suspend some tariffs on the United States. The effect of the USCTA is to suspend the U.S.-China Trade War, at least in part. (Many of the tariffs on both sides still exist). *See infra* text accompanying notes 52 & 53. The official text of the USCTA is available at Office of the U.S. Trade Representative, Economic and Trade Agreement Between the Government of the United States of American and the Government of the People's Republic of China (2020), https://ustr.gov/sites/default/files/files/agreements/phase%20one%20agreement/Economic_And_Trade_Agreement_Between_The_United_States_And_China_Text.pdf [hereinafter "USCTA"].

[30] Laura Reiley, *China Could Purchase Much Less U.S. Farm Product Than Thought*, WASH. POST (Feb. 20, 2020), https://www.washingtonpost.com/business/2020/02/20/china-could-purchase-much-less-us-farm-product-than-thought-new-usda-estimate-suggests/

[31] *See* Matt Egan, *It's an Insane Time for Trump to Pick (Another) Fight with China*, CNN (May 4, 2020), https://www.cnn.com/2020/05/01/business/trump-china-coronavirus-trade-war/index.html; *see also infra* Part III.

This study of the economic and political effects of a power-based approach to trade is timely because although the Trump Administration was the first to use this approach with China, U.S. hostility towards China did not start with and will likely not end with President Trump. The current United States Trade Representative (USTR) Robert Lighthizer, a well-known China and World Trade Organization (WTO) critic, and the chief architect of current U.S. trade policy, was approved by both houses of Congress by overwhelming majorities.[32] Skepticism about China is one of the few issues that both political parties in Congress find common ground.[33] Given the current hostile attitude towards China in both political parties, the United States may continue to use a power-based approach to trade with China regardless of which political party wins the U.S. presidency. For these reasons, it is useful to evaluate the risks and utility associated with such an approach.

The limits of a power-based approach do not mean that it cannot be an effective strategy for the United States. Aside from questions of its legality under the WTO,[34] the United States can use such an approach effectively if it first carefully analyzes the political and economic status of the targeted country as well as areas in which trade retaliation may occur. Our conclusion, based on the data, is that the power-based approach can be used most effectively against countries that lack the political will or economic ability to engage the United States in a standoff.[35] The power-based approach involves more risk when used against countries, such as China, that for political and economic reasons believes that it must stand up to the United States and engage the United States in a prolonged standoff. Against these types of countries, the power-based approach could lead to greater uncertainty and less unpredictability in economic and political results, and could backfire.[36] A careful study of the probable responses of the targeted country may reduce some of these uncertainties, but may not eliminate them entirely as a power-based approach involves many different variables and so is inherently less predictable than the cooperative approach, based on treaty negotiation, that is the hallmark of trade under the WTO.[37]

This Article will develop these main points by proceeding as follows. Part II will explain the background to the U.S.-China Trade War and will explain in further detail how the tariff system of the United States works in practice. Part II will also examine the power-based approach of the United States used in defiance of its legal obligations under the WTO. A key component of this approach is that the United States has been able to disable the dispute settlement system of the WTO by paralyzing the WTO Appellate Body. The United States has installed a parallel system of dispute resolution involving China's USCTA and WTO obligations that is under the complete control and domination by the United States. Part III examines the empirical effects of the tariffs.

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[32] *On the Nomination (Confirmation Robert Lighthizer, of Florida, to be United States Trade Representative)*, U.S. SENATE (May 11, 2017), https://www.senate.gov/legislative/LIS/roll_call_lists/roll_call_vote_cfm.cfm?congress=115&session=1& vote=00127; Andrew Restuccia & Megan Cassella, *'Ideological Soulmates': How a China Skeptic Sold Trump on a Trade War*, POLITICO (Dec. 26, 2018), https://www.politico.com/story/2018/12/26/trump-lighthizer-china-trade-war-1075221.

[33] Jennifer Haberkorn & Tracy Wilkinson, *Congress Debates Ways to Punish China over Virus*, L.A. TIMES (May 1, 2020), at A-6.

[34] Such an approach is inconsistent with the obligations of the United States under the WTO, although this issue does not seem to be much of a concern to the United States. *See infra* Part II.B.

[35] For examples involving the effective us of the power-based approach against South Korea and the European Union, see *infra* Part IV.

[36] *See infra* Part III.

[37] In contrast to a power-based approach favored by the United States, the WTO model of trade relations is based on multilateralism, negotiation, and consensus. See CHOW & SCHOENBAUM, supra note 3, at 26–29.

The tariffs have resulted in some unexpected economic and political costs and may backfire. Part IV will give some policy recommendations based on the conclusions reached in Part II to help guide further U.S. tariff policy.

II. BACKGROUND TO THE U.S.-CHINA TRADE WAR

A. *The Trump Administration and Economic Nationalism*

Although the United States has long been critical of China's trade practices, U.S. policy reached a new level of assertiveness with the ascension of Donald J. Trump to the U.S. presidency in 2016.[38] A signature slogan of the Trump Administration during the election process was "America First," a set of policies that echo economic nationalism from the 1930s, a period in which trade protectionism reached a peak that preceded the Second World War.[39] Trump was able to exploit simmering resentment against China and the negative impact of trade effects that had been building up for years and that fueled a rising populism. His message that the United States was being exploited by China and other trading partners who reaped the major benefits of trade to the detriment of the United States resonated with a large segment of the electorate.[40] Trump's assertiveness against China and his call for a revival of economic nationalism was a key component of his election to the U.S. presidency.[41]

Although the United States has complaints against many trading partners, the United States singled out China for especially harsh criticism. The Trump Administration focused on the following problematic aspects of China's trade policies: (1) unfair Chinese trade practices that increased the U.S. trade deficit with China to a record $420 billion in 2018;[42] (2) state intervention in the internal market to favor China's state-owned enterprises (SOEs) at the expense of U.S. companies;[43] and (3) state policies that encouraged the theft of U.S. intellectual property and forced technology transfer.[44] Trump also castigated prior U.S. administration for weak policies that allowed China to exploit its trading relationship with the United States.

In following up on his campaign positions, Trump took aggressive measures to pressure U.S. trading partners into reordering their trading relationship with the United States. In 2018, the

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[38] *See* Daniel C.K. Chow, *A New and Controversial Approach to Dispute Resolution under the 2020 United States-China Trade Agreement*, HARV. NEGOT. L. REV. at 3–4 (forthcoming 2020).

[39] *See* Daniel C.K. Chow, Ian M. Sheldon, & William McGuire, *The Revival of Economic Nationalism and the Global Trading System*, 40 CARDOZO L. REV. 2133 (2019).

[40] CHATHAM HOUSE REPORT, AMERICA'S INTERNATIONAL ROLE UNDER DONALD TRUMP 1, 10–11, & 19–20 (Xenia Wicket ed., 2017), https://www.chathamhouse.org/sites/default/files/publications/research/2017-01-18-americas-international-role-trump-wickett-final2.pdf.

[41] *See* Luis Da Vinta, *Competition, Conflict, and Conformity: Foreign Policy Making in the First Year of the Trump Presidency*, 49 Presidential Studies Q. 280 (2019); Edward Alden, *The Roots of Trump's Trade Rage*, Politico (Jan. 16, 2017), https://www.politico.com/magazine/story/2017/01/the-roots-of-trumps-trade-rage-214639.

[42] *U.S.-China Trade Facts*, OFFICE OF THE U.S. TRADE REPRESENTATIVE (2018), https://ustr.gov/countries-regions/china-mongolia-taiwan/peoples-republic-china#:~:text=The%20U.S.%20goods%20trade%20deficit,was%20%2440.5%20billion%20in%202018.

[43] *See* Daniel C.K. Chow, *The Myth of China's Open Market Reforms and the World Trade Organization*, 41 U. PENN. J. INT'L L. 939, 948–51 (2020).

[44] *Id.*

United States began to impose tariffs on a worldwide basis. On February 7, 2018, the United States imposed "global safeguard tariffs" by placing a 30 percent tariffs on all imports of solar panels worth $8.5 billion (except those from Canada) and a 20 percent tariff on all imports of washing machines worth $1.8 billion.[45] On March 23, 2018, the United States imposed a tariff of 25 percent on all worldwide steel imports (except from Argentina, Australia, Brazil, and South Korea) and a 10 percent tariff on all worldwide aluminum imports (except from Argentina and Australia).[46]

      The United States singled out China for especially dacronian treatment to pressure it into making trade concessions: In escalating fashion, the United States proposed "trade actions lists" of tariffs on selected Chinese goods of $34 billion (April 16, 2018),[47] $16 billion (June 20, 2018),[48] $200 billion (July 17, 2018),[49] and $300 billion (August 1, 2019).[50] In total, tariffs were to be imposed on $550 billion of imports or virtually *all* imports from China. In response, China imposed tariffs on $150 billion of imports from the United States.[51] Subsequently, as a result of signing Phase I of the USCTA on January 14, 2020, the United States suspended or reduced tariffs on $300 billion of Chinese imports, leaving tariffs on $250 billion in place with further reductions linked to future agreement by China on Phase II of the USCTA.[52] In exchange, under the USCTA, China agreed to purchase $200 billion in U.S. goods and services; China also agreed a proportionate reduction of its tariffs on U.S. goods.[53]

      The Trump Administration's aggressive use of trade sanctions has been controversial on several fronts. Not only did the severity and scope of the sanctions shock U.S. trading partners, the sanctions were in breach of and inconsistent with the rules of the multilateral trading system established by the WTO and its predecessor the General Agreement on Tariffs and Trade (GATT) that have governed international trade for nearly seven decades. The United States' response to claims of illegality under the WTO was to launch a decisive attack on the WTO and to assert a bold defiance of established WTO norms.

B. *Tariffs and Trade Under the WTO*

      The use of tariffs on imports is a component of the trade policy of most nations in the modern global economy. Each of the 164 member nations of the WTO use tariffs and has a tariff schedule that is filed with the WTO[54] and is made part of annexes to the GATT, which regulates

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[45] Dorcas Wong & Alexander Chipman Koty, *The US-China Trade War: A Timeline*, CHINA BRIEFING (May 13, 2020), https://www.china-briefing.com/news/the-us-china-trade-war-a-timeline.

[46] *Id.*

[47] *China Section 301–Tariff Actions and Exclusion Process*, OFFICE OF THE U.S. TRADE REPRESENTATIVE (2020), https://ustr.gov/issue-areas/enforcement/section-301-investigations/tariff-actions.

[48] *Id.*

[49] *Id.*

[50] *Id.*

[51] CONG. RESEARCH SERV., CRS-R45949, U.S.-CHINA TARIFF ACTIONS BY THE NUMBERS, fig. 1 (Oct. 9, 2019), https://fas.org/sgp/crs/row/R45949.pdf.

[52] Wong & Koty, *supra* note 45.

[53] *Id.*

[54] An official publication of the WTO explains GATT/WTO schedules for goods and services. *See* WORLD TRADE ORG., WHAT IS A WTO SCHEDULE (2017), https://www.wto.org/english/news_e/news17_e/mark_27jul17_e.pdf. The tariff schedule of each WTO members and other tariff information can be accessed from the official website on the member's country

international trade in goods.[55] Each tariff schedule sets forth tariff rates for each imported product and it is possible to classify all products under these schedules.[56] Goods are classified in accordance with the International Convention on the Harmonized Commodity Description and Coding System of 1988, a unified system known as the Harmonized Convention.[57] All WTO countries have adopted the Harmonized Convention; the United States adopted the Convention as the basis for the Harmonized Tariff Schedule of the United States (HTSUS).[58] Once a good is classified in accordance with the HTSUS, then the tariff rate associated with that classification is applied.[59] Under the HTSUS, the United States uses a 10 digit system of classification.[60] The tariff is determined at the 8 digit level known as the "tariff line."[61] The 10 digit number is used for information gathering purposes and is not related to the calculation of the amount of the tariff.[62] Under the Harmonized Convention, all tariff classifications are uniform among WTO countries up to the 6 digit level;[63] beyond that level, national variations are allowed to occur.[64] As a result, a high level of international uniformity and predictability in the use of tariffs has been achieved with the help of the WTO.

Goods imported from China and all other WTO members into the United States are subject to tariffs determined in accordance with the HTSUS. The HTSUS represents a bargain that the United States made with all other WTO members to apply the agreed upon ("bound") rates and not higher rates. Under the WTO, like all other members, the United States is allowed to depart from its agreed upon tariffs in the HTSUS and to impose a higher tariff only under carefully circumscribed limits set forth in the GATT and other WTO agreements. For example, if the United States experiences a sudden and unexpected surge in imports from Country A, the United States

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page on the WTO website. For the United States, see *United States of America and the WTO*, WORLD TRADE ORG. (2020), https://www.wto.org/english/thewto_e/countries_e/usa_e.htm.

[55] *See* General Agreement on Tariffs and Trade,Oct. 30, 1947, 61 Stat. A-11, 55 U.N.T.S. 194 (1947); General Agreement on Tariffs and Trade 1994, art. I, Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex 1A, 1867 U.N.T.S. 187, 33 I.L.M. 1153 (1994) [hereinafter "GATT 1994"].

[56] For example, for China's tariff schedules, see China's goods schedules on China's country webpage, *China and the WTO*, WORLD TRADE ORG. (2020, https://www.wto.org/english/thewto_e/countries_e/china_e.htm.

[57] *See* DANIEL C.K. CHOW & THOMAS J. SCHOENBAUM, INTERNATIONAL BUSINESS TRANSACTIONS 152–53 (4th ed. 2020).

[58] *Id.*

[59] *Id.*

[60] *Id.* The first two digits are the broadest category indicating a chapter. There are 99 chapters with the lower numbers indicating goods closer to nature and higher numbers indicating increasing complexity and industrialization of the goods. For example "04" indicates dairy products, such as eggs. The next two digits indicate a heading under the chapter so "0403" refers to products derived from milk. The next two digits then indicate a subheading within the chapter and heading, e.g. "040310" is the subheading for yoghurt. At this point – the six digit line – this classification is uniform throughout all WTO countries. Beyond the six digit number, national variations are allowed to occur. An example of an eight digit line is "0403.10.11" (e.g. low fat yoghurt"). This is the tariff line or the line at which the tariff is imposed. The ten digit line used by the United States is for information purposes only. *See Get Tariff Data*, WORLD TRADE ORG. (2020), https://www.wto.org/english/tratop_e/tariffs_e/tariff_data_e.htm.

[61] CHOW & SCHOENBAUM, *supra* note 57, at 152–53.

[62] *Id.*

[63] *Id.*

[64] *Id.*

could suffer harm to its domestic industries.[65] If imports flood the internal market, prices will be driven downward and domestic manufacturers of products that compete with the imports could suffer financial losses.[66] To allow these domestic companies some breathing room, the United States is allow to use a "safeguard" and depart from its HTSUS tariff rate for the import.[67] As a safeguard, the United States is allowed by the WTO to impose a higher tariff or to impose a quantitative limit or a quota on the imports on a temporary basis.[68] Other examples that justify the imposition of a higher tariff is an anti-dumping duty, which is an additional tariff to offset "dumped" imports, i.e. imports sold at artificially low prices to secure a foothold in the import market.[69] An additional tariff, known as a countervailing duty, is also allowed when used to offset subsidies, i.e. financial contributions, made by the government of the exporter to allow the exporter to charge a lower price for its export and to gain an economic advantage over domestic competitors in the import market.[70] The types of tariffs, called safeguards, anti-dumping duties, and countervailing duties, are the most common types of additional tariffs used in international trade that are justified departures from the tariff rates set forth in national schedules.

In the case of China, the United States imposed a wide-ranging set of tariffs that did not fit into any of the categories of justified tariff increases discussed above. The United States justified most of the China tariffs through use of Section 301 of the Trade Act of 1974,[71] which authorizes the United States to impose trade sanctions if an investigation determines that a country has violated its WTO obligations, has engaged in acts, policies, or practices that are unjustified, unreasonable, or discriminatory and that burden or restrict U.S. commerce.[72]

A problematic component of Section 301 is that it appears to authorize the United States to find a violation of another country's WTO obligations, which violates one of the most fundamental principles of the WTO. This is the basic principle that prohibits unilateralism.[73] Only

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[65] *See* CHOW & SCHOENBAUM, *supra* note 3, at 399.

[66] *Id.*

[67] 19 U.S.C. § 2251. Safeguards are authorized by GATT Art. XIX and the WTO Agreement on Safeguards (1994), https://www.wto.org/english/docs_e/legal_e/25-safeg_e.htm.

[68] 19 U.S.C. § 1673.

[69] *See id*.; CHOW & SCHOENBAUM, *supra* note 3, at 467–70. Anti-dumping duties are authorized by GATT Art. VI and the WTO Anti-Dumping Agreement (Agreement on Implementation of Article VI of the General Agreement on Tariffs and Trade (1994)), https://www.wto.org/english/res_e/publications_e/ai17_e/anti_dumping_e.htm.

[70] *See* 19 U.S.C. § 1671; CHOW & SCHOENBAUM, *supra* note 3, at 467–68. Countervailing duties are authorized by GATT Art. VI and the WTO Agreement on Subsidies and Countervailing Measures, https://www.wto.org/english/tratop_e/scm_e/subs_e.htm.

[71] 19 U.S.C. § 2411.

[72] *Id.*

[73] This principle is contained in Article 23 of the WTO Dispute Settlement Understanding, which provides in relevant part:

> Members shall . . . not make a determination to the effect that a violation has occurred, that benefits have been nullified or impaired or that the attainment of any objective of the covered agreements has been impeded, except through recourse to dispute settlement in accordance of the rules and procedures of this Understanding, and shall make any such determination consistent with the findings contained in the panel or Appellate Body report adopted by the DSB [Dispute Settlement Body] or an arbitration award rendered under this Understanding[.]

the WTO has the authority or jurisdiction to decide issues of WTO law;[74] all WTO members must defer to and base their actions on the WTO's determination of WTO law;[75] if individual states could decide issues of WTO law on their own, then these actions would undermine the WTO and the WTO would become irrelevant.

Section 301 deals with the issue of unilateralism by providing that upon the initiation of a 301 investigation, the United States will file a parallel action in the dispute settlement system of the WTO.[76] The two actions will proceed simultaneously with the United States action to be based on the result of the WTO case.[77] The issue of whether this mechanism was sufficient to deal with the problem of unilateralism was squarely raised by the EU before the WTO panel in *United States –Sections 301-310 of the Trade Act of 1974*.[78] The EU argued that time deadlines under Section 301 could require a decision by the United States on issues of WTO law before the WTO dispute settlement body could reach its decision.[79] The WTO panel rejected this argument because it found that a U.S. administrative interpretation required the United States to wait for a decision by the WTO before the Section 301 investigation could make any of its findings.[80] Thus, Section 301 was not in violation of the principle prohibiting unilateralism because any decisions of the United States on WTO law would be based on a prior ruling by the WTO.

Although the WTO provided clear direction on how Section 301 can be applied consistent with the WTO, the United States has ignored this mandate in the U.S.-China Trade War. For the past twenty years, the United States brought a parallel case in the WTO in every Section 301 investigation,[81] but the Trump Administration never filed a WTO case in the Section 301 investigations leading to the China tariffs. Instead, the United States acted unilaterally and made findings under Section 301, including findings that implicated issues of WTO law, which were not based on a prior WTO ruling. The United States then imposed trade sanctions on China based upon such Section 301 findings. These sanctions are in breach of the WTO principle prohibiting unilateralism and are without legal justification.

C. *Paralysis of the WTO Dispute Settlement Body*

U.S. defiance of the WTO can be understood only by also considering the events set in place by the United States leading up to December 10, 2019 when the WTO lurched into a crisis with the paralysis of the WTO Appellate Body.[82] U.S. dissatisfaction with the WTO began almost immediately after the WTO's inception on January 1, 1995.[83] The United States' criticism of the

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Understanding on Rules and Procedures Governing the Settlement of Disputes, art. 23.1(a), Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex 2, 1869 U.N.T.S. 401, 33 I.L.M. 1125 (1994) [hereinafter "DSU"]. For a discussion of United States unilateralism, see Daniel C.K. Chow, *United States Unilateralism and the World Trade Organization*, 37 B.U. INT'L L. J. 1 (2019).

[74] *Id.*

[75] *Id.*

[76] *See* Chow, *supra* note 73, at 12.

[77] *Id.*

[78] WT/DS153/R (adopted on Jan. 27, 2000).Id. at ¶ 7.112.

[79] Id. at ¶ 7.29.

[80] Id. at ¶ 7.112.

[81] See Chow, *supra* note 73, at 12.

[82] See Daniel C.K. Chow, *United States Trade Infallibility and the World Trade Organization*, MICH. ST. L. REV. at 2 (forthcoming 2020).

[83] *Id.* at 4.

WTO focuses on three elements: (1) the "judicial activism" of the Appellate Body that exceeds its powers and results in creating new law; (2) WTO decisions that reject U.S. trade law remedies and require repeal of venerable U.S. trade statutes; and (3) various violations by the Appellate Body of its own rules and procedures.[84] Debate continues to rage over the role of the Appellate Body, although most current attention focuses on how to resuscitate the Appellate Body and save the WTO.[85]

The WTO decides cases through panels, which act as trial courts, and an Appellate Body, which acts as a high court of international trade.[86] On May 12, 2016, President Barack Obama took the unprecedented step of blocking new appointments to the WTO Appellate Body to replace retiring panelists.[87] The Trump Administration continued this policy of U.S. intransigence with the result that on December 10, 2019, the number of remaining active panelists fell below that needed to constitute a quorum in the Appellate Body.[88] As a result, the Appellate Body was unable to convene and hear appeals of cases from WTO panels.

Panel decisions that are not appealed are not affected by the paralysis of the Appellate Body.[89] Panel decisions that are appealed, however, are launched into a legal limbo.[90] The Appellate Body is unable to convene to hear the appeal and the rules of the WTO make clear that once an appeal is filed, the WTO decision cannot take legal effect until the appeal is completed.[91] As it is now impossible to complete the appeal, any decisions that are appealed, are suspended indefinitely and have no legal effect.

The most important consequence of the crippling of the Appellate Body is that WTO obligations have become in effect unenforceable. For example, suppose that China wishes to contest a U.S. tariff imposed in defiance of the WTO. If China wins a decision against the United States from a WTO panel, the United States can simply file an appeal and suspend the decision indefinitely, making it unenforceable.

One month after the paralysis of the WTO, the United States and China entered into the USCTA on January 14, 2020, which completed the United States' plan to seize power over dispute resolution involving China from the WTO.[92] Under the USCTA, the United States has created a parallel dispute resolution system, one that is under U.S. complete control and domination, which can be used by the United States to unilaterally impose sanctions to resolve both USCTA and

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[84] *Id.* at 19–26.

[85] *Id.* at 9–13.

[86] *Id.* at 6.

[87] *Id.* at 8.

[88] Chow, *supra* note 82, at 8.

[89] *Id.*

[90] *Id.*

[91] Article 16.4 of the DSU states in relevant part: "If a party has notified of its decision to appeal, the report by the panel shall not be considered for adoption by the DSB [Dispute Settlement Body] until the appeal is completed." DSU, *supra* note 73, at art. 16.4. A panel or Appellate Body decision becomes effective when it has been adopted by the DSB, which consists of the entire membership of the WTO. Under the principle of reverse consensus, the DSB must adopt the decision unless a consensus of all members decide not to adopt it. Thus, so long as *one* member votes to adopt the decision must be adopted. In practice, this means that it is highly likely that all WTO panel or Appellate Body decisions will be adopted by the DSB. *See* CHOW & SCHOENBAUM, *supra* note 3, at 84. However, adoption cannot occur so long as an appeal is still pending.

[92] *See* Chow, *supra* note 38, at 1.

WTO obligations involving China. [93]

D. *The U.S. Power-Based Approach to International Trade*

      This discussion of the background to the U.S.-China Trade War illustrates the main strategic positions taken by the United States as part of its power-based approach to international trade. First, cripple the WTO dispute settlement system so that WTO obligations become unenforceable. Second, impose unilateral trade sanctions on U.S. trading partners in defiance of WTO law that can no longer be challenged due to the paralysis of the Appellate Body. Third, create a parallel dispute settlement system in a bilateral treaty, which is under the complete control of the United States.[94] With this strategy in place, the United States can use unilateral sanctions to pressure China and other U.S. trading partners into making trade concessions and to reorder trading relationships with the United States established under prior U.S. administrations. While the United States has been able to successfully create the legal conditions to allow the United States to pursue its power-based approach, the next part of this Article examines whether the power-based approach has been able to achieve the economic and political results sought by the United States.

III. ECONOMIC AND POLITICAL IMPACT OF THE U.S.-CHINA TRADE WAR

A. *Power-Based Bargaining and Tariffs*

      Analysis of President Trump's trade policy choices has typically interpreted them in terms of a zero-sum game, i.e., rather than generating mutual benefits in a positive-sum game, international trade is a game where economically, one country is a winner while the other must be a loser.[95] However, trade economists Aaditya Mattoo and Robert Staiger offer an alternative explanation for these actions: the Trump administration has chosen to move from "rules-based" to "power-based" bargaining over tariffs as a means of dealing with what they call "latecomers" to the GATT/WTO.[96] The concern here is that by switching from rules-based to power-based bargaining, the United States is putting the future of the post-war trading system at risk, as well as inflicting economic costs on both itself and its trading partners.

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[93] *See id.* (explaining that the United States' had a three part strategy: first, cripple the WTO dispute settlement system; second, engage in WTO inconsistent behavior that can no longer be challenged by pressuring China to purchase $200 billion in U.S. goods and services; and third, create a parallel dispute resolution system over USCTA and WTO disputes under the USCTA that authorizes unilateral U.S. actions against China).

[94] These arguments are developed in Chow, *supra* note 92, at 13–26.

[95] *See* Daniel C.K. Chow & Ian Sheldon, *Is Strict Reciprocity Required for Fair Trade?*, 52 VAND. J. TRANSNAT'L L. 1, 33–38 (2019).

[96] *See* Aaditya Mattoo & Robert W. Staiger, *Trade Wars: What Do They Mean? Why Are They Happening Now? What Are the Costs?*, at 1–2 (NBER, Working Paper No. 25762, 2019). The Most Favored Nation principle is enshrined in GATT, Article I. GATT 1994, *supra* note 55, art. I. The MFN principle provides that any advantage given to any other country must be immediately and unconditionally given to all GATT/WTO members. For example, if the United States gives the benefit of a low tariff to any country, the United States must immediately and unconditionally extend the same low tariff to all WTO members. The MFN universalizes trade benefits and is an inducement to join the GATT/WTO. *See* CHOW & SCHOENBAUM, *supra* note 3, at 150.

Key to the functioning of the GATT/WTO have been the most favored nation (MFN) principle and reciprocity, both acting as a constraint on exercise of bargaining power by a powerful country such as the United States.[97] Specifically, MFN dilutes bargaining power by ensuring that tariff commitments to either one country or a sub-set of countries in the GATT/WTO are then offered to all other countries in the GATT/WTO, and at the same time reciprocity establishes the idea that there will be a balance of tariff concessions in any negotiating round of GATT/WTO. By committing to such a set of rules, the United States has helped induce other weaker/smaller countries to successively lower their tariffs under GATT/WTO.[98]

In 2017, the United States' average MFN tariff was 3.4 percent, which compared to China's average MFN tariff of 9.6 percent.[99] Given this asymmetry in average bound tariffs, the current administration perceived that it had little left to offer a latecomer to the WTO such as China in terms of reciprocity, and instead it has resorted to unilaterally raising its tariffs as a means to inducing China to cut their tariffs. However, in switching to unilateralism, the United States is following a "myopic logic", i.e., by using bargaining tariffs, the United States seems to have ignored the real possibility that other countries such as China would likely resort to the same strategy, thereby undermining the multilateral trading system.

U.S. strategy ignores the basic principles of game theory, and the economic argument for why the GATT/WTO has, until now, been largely successful in its promotion and governance of international trade. The underlying logic of the GATT/WTO has been explained by trade economists in terms of the resolution to a prisoner's dilemma. Imagine a non-cooperative world where the strategic choice of one country is to maximize its own objective function through tariff policy, given the tariff policy of the other country(ies). To understand its strategic choices, it is important to think through the economic effects of a tariff and why any country would rationally choose to apply one.[100]

Assuming exporters do not adjust their price, an import tariff has the following effects: it raises the domestic price of the good being imported, but it also generates tariff revenue on that good. Once the transfer of revenue to the domestic exchequer has been accounted for, the net effect of the tariff generates what economists denote as a "deadweight loss", i.e., there is a reduction in domestic consumers' real income, with redistribution to both import-competing firms and the government.[101] In other words, the incidence of the tariff is borne entirely by consumers of the imported good, thereby reducing domestic economic welfare. The rationale for a country to follow a strategy that fails to maximize national income can only be political, i.e., governments adopt protectionist policies for electoral reasons. For example, protectionist policies can be chosen to target either sector-specific lobby groups who provide campaign contributions to political parties or specific voter groups who are close to being indifferent between candidates.[102]

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[97] *See id.* at 2.

[98] *See id.* at 8.

[99] *See* Chad P. Bown, *The 2018 US-China Trade Conflict After Forty Years of Special Protection*, 12 CHINA ECON. J. 109, 111–12 (2019).

[100] Mary Amiti, Stephen J. Redding, & David E. Weinstein, *The Impact of the 2018 Tariffs on Prices and Welfare*, 33 J. ECON. PERSPECTIVES 187, 189–91 (2019).

[101] *See id.* at 189–90.

[102] *See* Gene M. Grossman & Elhanan Helpman, *Protection for Sale*, 84 AM. ECON. REV. 833, 834 (1994); Gene M. Grossman & Elhanan Helpman, *A Protectionist Bias in Majoritarian Politics*, 120 Q. J. ECON. 1239, 1239–41 (2005).

However, if exporting firms do reduce their prices in response to the tariff, there will be a terms-of-trade benefit to the importing country, captured in the form of additional tariff revenue. In this case, the incidence of the tariff is partially borne by exporting firms, and it is quite possible for the terms-of-trade gain to outweigh the deadweight loss of the tariff, domestic economic welfare increasing.[103] The optimal import tariff, and hence the extent of the terms-of-trade gain, will depend on the slope of the export supply function, i.e., what economists define as the price elasticity of supply, which measures the rate at which firms change their supply in response to a change in prices.[104]

Essentially, the tariff game has the structure of a prisoner's dilemma: in the absence of cooperation, both countries, in choosing to maximize their payoffs, have a unilateral incentive to utilize a tariff, whatever the strategic choice of the other country. Each country seeks to improve its terms-of-trade, knowing that the other country will rationally adopt that same strategy, the outcome being a Nash equilibrium where no country can unilaterally change their tariff strategy and be better off.[105] The net result is that each country loses market access to the other country's market because of tariffs, the reduction in the volume of international trade being economically inefficient.

The latter result suggests that it would be Pareto-improving for countries to agree to reduce their tariffs, and in the absence of a binding bilateral agreement between countries, the GATT/WTO has essentially neutralized the terms-of-trade incentive for countries to raise tariffs.[106] In other words, if terms-of-trade effects have been removed from any country's objective function, it will set tariffs to satisfy domestic political objectives alone.[107] These would be either zero if a country seeks to maximize its national income through free trade, or they would be positive in order to satisfy domestic political constraints, but importantly, they are lower than those in a non-cooperative game.[108] Therefore, if countries enter into a trade agreement, they will seek mutual reductions in tariffs generating an increase in national and global economic welfare.

The lower tariff equilibrium under GATT/WTO has also been supported by a credible enforcement mechanism embodied in the dispute settlement process. Standard game theory suggests that countries would have an incentive to deviate from a low-tariff equilibrium. However, in a repeated game, the punishment for not adhering to a trade agreement is reversion to the static Nash equilibrium of high tariffs, i.e., what game theorists term a trigger strategy.[109] In practice, the rules of GATT/WTO seek to maintain the balance of tariff concessions and avoid the use of punitive, and therefore economically destructive actions.[110] Essentially, if one country were to raise its tariff, this would imply a loss of previously negotiated market access for the foreign

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[103] *See* Amiti, Redding, & Weinstein, *supra* note 96, at 189.

[104] *See* Christian Broda, Nuno Limão, & David E. Weinstein, *Optimal Tariffs and Market Power*, 98 AM. ECON. REV. 2032, 2032–34 (2008).

[105] *See* Ben Zissimos, *The GATT and Gradualism*, 71 J. INTERNAT'L ECON. 410, 413 (2007). The Nash Equilibrium, considered one of the great breakthroughs in the history of social science, is named after Princeton University mathematician John Nash. *See* Roger B. Myerson, *Nash Equilibrium and the History of Economic Theory*, 37 J. ECON. LIT. 1067, 1069–70 (1999).

[106] *See* Kyle Bagwell & Robert W. Staiger, *An Economic Theory of GATT*, 89 AM. ECON. REV. 215, 226–27 (1999).

[107] *See id.* at 222–23.

[108] *See id.* at 222–24.

[109] *See* Zissimos, *supra* note 105, at 413.

[110] *See* ROBERT W. STAIGER, INTERNATIONAL RULES AND INSTITUTIONS FOR TRADE POLICY 1501 (Gene M. Grossman & Kenneth Rogoff eds., 1995).

country. Assuming that this action is not "abusive", under GATT/WTO rules, the other country can withdraw an equivalent amount of market access, a punishment path that is subgame perfect.[111] However, if a country deviates in an "abusive" manner, there is reversion to the trigger strategy, i.e., there is an indefinite suspension of GATT/WTO obligations, both countries setting Nash equilibrium tariffs.[112] In other words, the objective of GATT/WTO rules is to ensure that retaliation by one country against the unilateral action of another is proportionate, thereby minimizing the chance of a trade war.

By unilaterally raising tariffs to such an extent in 2018, an action that was clearly "abusive", the United States simply provoked a trigger strategy reaction on the part of China. Instead of cutting its tariffs in response to the U.S. raising tariffs, China (and other countries) retaliated in kind by raising tariffs against the U.S., their average tariff reaching 18.3 percent by 2018,[113] and while the two countries did halt escalation of the trade war in early-2020 through Phase 1 of the USCTA, neither side has actually reduced tariffs to their pre-2018 level. Essentially, power-based bargaining by the U.S. has failed in the sense that the bilateral relationship with China has been pushed closer towards the higher tariff, non-cooperative Nash equilibrium, thereby putting the multilateral trading system at risk.[114]

B. *The Economic Costs of Power-Based Bargaining*

Given this substantive breach of the multilateral trading system, it is logical to ask: at what cost? Essentially, the U.S.-China Trade War represents a natural experiment in the sense that we have not seen such wide-ranging increases in tariffs since the 1930s, when Congress passed the Smoot-Hawley Tariff Act.[115] Not surprisingly, applied trade economists have already conducted in-depth research on the impact of the trade war on the U.S. economy, the most notable being those by Mary Amiti, Stephen Redding, and David Weinstein, Alberto Cavallo *et al*., and Pablo Fajgelbaum *et al*.[116]

Of the studies cited, the latter is perhaps the most detailed. The authors constructed a monthly panel data set using publicly available tariff schedules issued by the U.S. International Trade Commission (USITC) along with U.S. import and export data published by the U.S. Census Bureau, where the tariff data are defined at the 8 digit level of the HTSUS, and the import data are defined at the HTSUS-10 digit level.[117] In addition, data on retaliatory tariffs were collected from the Ministry of Finance for China, the Department of Finance of Canada, the Office of the

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[111] *See* Zissimos, *supra* note 105, at 412.

[112] *See id.* at 416.

[113] *See* Chad P. Bown, *US-China Trade War Tariffs: An-Up-To-Date Chart*, PETERSON INST. FOR INTERNAT'L ECON. (Feb. 14, 2020), https://www.piie.com/research/piie-charts/us-china-trade-war-tariffs-date-chart.

[114] *See* Mattoo & Staiger, *supra* note 96, at 1.

[115] *See* Chad P. Bown & Y. Zhang*, Trump's 2019 Protection Could Push China Back to Smoot-Hawley Tariff Levels*, PETERSON INST. FOR INTERNAT'L ECON. (May 14, 2019). https://www.piie.com/blogs/trade-and-investment-policy-watch/trumps-2019-protection-could-push-china-back-smoot-hawley.

[116] *See* Amiti, Redding, & Weinstein, *supra* note 100; Alberto Cavallo, Gita Gopinath, Brent Naiman, & Jenny Tang, Tariff Passthrough at the Border and at the Store: Evidence from U.S. Trade Policy, at 1–35 (NBER, Working Paper No. 26396, 2019); Pablo D. Fajgelbaum, P.K. Goldberg, P.J. Kennedy, & A.K. Khandelwal, *The Return to Protectionism*, 135 Q. J. ECON. 1, 1–55 (2020).

[117] For a discussion of the Harmonized System, see *supra* text accompany notes 54–70.

President of Mexico, and the WTO (covering the EU, Russia, and Turkey), tariffs being measured by China at the 6 digit level of the Harmonized Convention.[118]

During 2018, U.S. tariffs were targeted at 12,043 specific products at the HTSUS-10 digit level, where in 2017, these imports were valued at $303 billion, accounting for 12.7 percent of total U.S. imports. The average *ad valorem* tariff increased by from 2.6 to 16.6 percent. In terms of retaliatory tariffs on U.S. exports by Canada, China, Mexico, Russia, Turkey, and the EU, these accounted for $127 billion of U.S. exports, 8.2 percent of total exports, covering 8,073 products.[119]

It is very clear from the data that the U.S. tariffs were mostly targeted at China, and Chinese retaliatory tariffs against the U.S. dominate, supporting the contention that the trade war is essentially between these two countries. In 2018, the U.S. targeted 11,207 products accounting for 49 percent of total imports from China, tariffs increasing on average from 3.0 to 15.5 percent, while China targeted 7,474 products, tariffs increasing on average from 8.4 to 18.9 percent.[120] The data also show that the most protected U.S. sectors were primary metals, machinery, computer products, and electrical equipment and appliances, while U.S. trading partners targeted different products, most notably agricultural imports.[121]

Interestingly though, there was not much variation in tariff rate changes across sectors in either the United States or the retaliating countries. Almost all U.S. imports were targeted with either 10 or 25 percent tariff changes, and likewise for retaliatory tariff increases. This has two important implications: first, if either side in the trade war were seeking to maximize terms-of-trade effects, tariff changes would likely vary across sectors depending on the price elasticity of supply;[122] and, second, the lack of variation in U.S. tariff increases point to their not being driven by sector-specific lobbying.[123]

Given their monthly panel data set, Fajgelbaum *et al*. undertook a detailed empirical analysis of the effects of the trade war on the U.S. economy. They conducted an "event" study which consisted of comparing targeted and non-targeted U.S. imports and exports. In the case of imports, the results indicate their value and quantity declined by 20 and 23 percent, respectively.[124] Importantly, they also present initial evidence that the incidence of U.S. import tariffs was borne entirely by U.S. consumers, tariff-inclusive unit values of imports increasing significantly as compared to before-tariff unit values which did not change.[125] These authors also found a similar pattern in the case of exports, where their value and quantity fell by 24 and 25 percent respectively, with no change in their before-tariff unit values, i.e., there was, complete passthrough of retaliatory tariffs to foreign consumers.[126]

Fajgelbaum *et al*. also used econometric methods to evaluate the impact of tariff increases on U.S. import demand and foreign export supply. Their results, which are statistically significant, show that both the value and quantity of U.S. imports declined in response to the application of

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[118] This is due to HTSUS-8 codes not being directly comparable across countries.

[119] *See* Fajgelbaum, Goldberg, Kennedy, & Khandelwal, *supra* note 116, at 8–9.

[120] *See id.* at 9.

[121] *See id.* at 9–13.

[122] *See id.* at 13. Formally, the less sensitive firms are to price changes, the higher the optimal tariff.

[123] *See id. at* 14; *see also* Grossman & Helpman, *supra* note 106.

[124] *See* Fajgelbaum, Goldberg, Kennedy, & Khandelwal, *supra* note 116, at 15; *see also* Amiti, Redding, & Weinstein, *supra* note 104, at 195. They find in their analysis that the value of U.S. imports fell by 25 to 30 percent after imposition of the tariffs.

[125] *See* Fajgelbaum, Goldberg, Kennedy, & Khandelwal, *supra* note 116, at 15.

[126] *See id.* at 16.

tariffs, Amiti, Redding, and Weinstein finding similar effects in their study.[127] However, Fajgelbaum *et al.* also found that there was no impact of U.S. tariffs on before-tariff unit values.[128] The latter result provides further support for the argument that there was complete passthrough of the tariffs to tariff-inclusive prices borne by U.S. consumers. Similar results are reported for the impact of retaliatory tariffs on U.S. exports – there were significant declines in both the value and quantity of exports, but there was no reduction in before-tariff unit values by U.S. exporters.[129] By contrast, Cavallo *et al.* (2019) found that there was imperfect passthrough of these tariffs to Chinese import prices of agricultural products.[130]

The finding that incidence of U.S. tariffs was almost entirely borne by U.S. consumers is consistent with the results of other studies using different estimation methodologies.[131] It is also a surprising result given the importance placed on the terms-of-trade argument in the international economic analysis of optimal tariffs, as well as the empirical literature that has found less than complete passthrough of exchange rate shocks.[132] Over a longer time period, it might be expected that exporters would eventually cut before-tariff prices, especially if there was resolution of exporter uncertainty about how long the tariffs will remain in place.[133] Interestingly, a follow-up study with data for 2019, shows that there is some variation across sectors, e.g., U.S. tariffs led foreign steel exporters to lower their before-tariff prices.[134]

The final step in the analysis of Fajgelbaum *et al.* was to quantify the effects of the trade war in 2018 using a computable general equilibrium model of the U.S. economy calibrated at the county level. Their results were as follows: first, U.S. consumers of imported goods in aggregate lost $51 billion due to higher prices; second, U.S. exporters saw an increase in their income of $9.4 billion; and, third, U.S. tariff revenue totaled $34.3 billion.[135] Therefore, the net effect of the trade war was an aggregate loss of U.S. real income of $7.3 billion, which can be thought of as an approximation of the deadweight loss referred to earlier.[136] The latter number compares to Amiti, Redding, and Weinstein's estimated net real income loss of $8.2 billion.[137] As is often the case in applied trade analysis, the net economic effects are relatively small, but the re-distributional impact of tariffs on consumers is substantial. Other research by Michael Waugh suggests that subsequently this had a significant impact on consumption behavior, measured by reductions in county-level automobile sales.[138]

Importantly, contrary to what President Trump has claimed, the results reported in Fajgelbaum *et al.*, and in similar studies, clearly shows that the incidence of import tariffs implemented in 2018 was entirely borne by U.S. consumers, any terms-of-trade effects on the

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[127] *See id.* at 26; Amiti, Redding, & Weinstein, *supra* note 100, at 198–99.

[128] *See* Fajgelbaum, Goldberg, Kennedy, & Khandelwal, *supra* note 116, at 26–27.

[129] *See id.* at 31.

[130] *See* Cavallo, Gopinath, Naiman, & Tang, *supra* note 116, at 29–30.

[131] *See* Amiti, Redding, & Weinstein, *supra* note 100, at 198–99; *id.* at 1.

[132] *See* Pinelopi, K. Knetter & Michael M. Knetter, *Goods Prices and Exchange Rates: What Have We Learned?*, 35 J. ECON. LIT. 1243, 1243–45 (1997).

[133] *See* Amiti, Redding, & Weinstein, *supra* note 100, at 198.

[134] *See* Mary Amiti, Stephen J. Redding, & David E. Weinstein, *Who's Paying for the U.S. Tariffs? A Longer-Term Perspective*, at 1–8 (NBER, Working Paper No. 26610, 2020).

[135] *See* Fajgelbaum, Goldberg, Kennedy, & Khandelwal, *supra* note 116, at 42–45.

[136] *See id.* at 44–45.

[137] *See* Amiti, Redding, & Weinstein, *supra* note 100, at 199–200.

[138] *See* Michael E, Waugh, *The Consumption Response to Trade Shocks: Evidence From the US-China Trade War*, at 2 (NBER, Working Paper No. 26353, 2019).

import side being insignificant.[139] Also, if there had been no retaliation by China and other countries, there would have been a modest U.S. real income gain of $0.5 billion in 2018 due to significant terms-of-trade effects on the export side.[140] In other words, the logic of power-based bargaining only ever had the potential to work if China had not adopted a trigger strategy in response to the increase in U.S. tariffs.

As a precursor to later discussion of the estimated political costs of the Administration's adoption of power-based bargaining, it is also worth summarizing Fajgelbaum *et al.*'s findings on the U.S. regional economic effects of the trade war. As previously noted, tariffs affect consumers through higher prices, but workers in the protected import-competing sectors may also benefit from higher producer and export prices. In addition, U.S. tariffs were heavily targeted towards imports of intermediate inputs which may be used more intensively in some regions compared to others. [141] Any regional effects of U.S. import tariffs will also have been affected by the regional structure of retaliatory tariffs.

In order to analyze regional effects, Fajgelbaum *et al*. utilized annual industry employment and wage data at the county-by-sector level for all non-farm sectors, collected from the Census County Business Patterns (CBP) database, while county-level data for the farm sector were collected from the Bureau of Economic Analysis (BEA) Local Area Personal Income and Employment database. In addition, county-level demographic statistics were obtained from the U.S. Census Bureau American Community Survey, and county-level voting data were collected from the U.S. Federal Election Commission.

Several key results come out of the regional analysis.[142] First, there is considerable variation across counties in their exposure to the trade war, with the Great Lakes region of the Midwest, and industrial areas of the Northeast receiving higher tariff protection while rural areas in the Midwestern plains and Mountain West were subject to higher tariff retaliation.[143] Second, every county in the U.S. suffered a reduction in its real wage, the counties with lower losses being in the Rust Belt and Southeast, while counties in the Midwestern Plains were hit with the largest reductions in real wages due to the structure of retaliatory tariffs.[144] Third, there is evidence that the Administration targeted tariffs at politically competitive counties, with a view to disproportionately affecting those voters important in determining electoral outcomes. Specifically, counties with a 40-60 percent Republican vote were targeted with higher tariffs than counties that leaned heavily to either the Republicans or Democrats.[145] In terms of economic impact, workers located in counties where the Republican vote share was 85-90 percent, incurred the greatest cost due to the trade war.[146] Reinforcing this, Waugh's analysis shows that the

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[139] *See* Fajgelbaum, Goldberg, Kennedy, & Khandelwal, *supra* note 116, at 3.

[140] *See id.* at 41–45. The argument here is as follows: when the U.S. imposes tariffs on a range of products, U.S. consumers reallocate consumption to the U.S. versions of these products. The net effect is to raise world demand for the U.S. version of the products relative to world demand for the Chinese version of the products, resulting in a terms-of-trade benefit to U.S. producers.

[141] *See* Thiemo Fetzer & Carlo Schwarz, *Tariffs and Politics: Evidence from Trumps' Trade Wars*, at 1 (CEPR, Discussion Paper No. 13579, 2019), who find that the geographic incidence of the 2018 tariffs was correlated with the Republican's prior electoral performance.

[142] *See* Fajgelbaum, Goldberg, Kennedy, & Khandelwal, *supra* note 116, at 45–52.

[143] *See id.* at 45–47.

[144] *See id.* at 47–49.

[145] *See id.* at 49. See also Grossman & Helpman, *supra* note 102, at 1239–40.

[146] *See* Fajgelbaum, Goldberg, Kennedy, & Khandelwal, *supra* note 116, at 51–52.

consumption impact of U.S. trade policy varied regionally, with high-tariff counties experiencing larger declines in automobile sales relative to low-tariff counties.[147]

C. *The Impact of Retaliatory Tariffs on U.S. Agriculture*

Given the recorded negative effect of the trade war on counties in the Midwestern plains, and the importance of the rural and farm sector to Donald Trump's political base, it is important to dig a little deeper into the extent to which the U.S. agricultural sector was disproportionately affected by retaliation to U.S. implementation of tariffs in 2018. The most detailed analysis of the effect of this retaliation is provided by agricultural economists Colin Carter and Sandro Steinbach.[148] In their study, they used a monthly panel dataset of tariffs targeted against U.S. products at the HTSUS-8 and HTSUS-10 digit levels, collected from the finance and trade ministries of Canada, China, the EU, India, Mexico, Russia and Turkey. These tariff data were matched with U.S. export data from the Global Trade Atlas. The data indicate that average tariffs on U.S. agricultural products increased from 8.3 to 28.6 percent on 908 products accounting for $32 billion worth of U.S. exports.[149] Retaliatory tariffs disproportionately affected agricultural products compared to other sectors, and the tariff increases were also steeper, the average *ad valorem* tariff increasing from 8.3 to 28.6 percent. Notably, the most significant retaliation was by China, who imposed tariffs on $25.5 billion of U.S. imports.[150]

In their empirical analysis, Carter and Steinbach also used an "event" study to identify the impact of the retaliatory tariffs on U.S. agricultural exports, based on exploiting differences in export quantities, values, and unit values between targeted and non-targeted products over time. Their reported results indicate that retaliatory tariffs had a significant impact on agricultural trade. First, the United States saw a 55 percent reduction in its exports to retaliating countries worth -$15.6 billion (trade destruction), which was only partially offset by a 0.8 percent increase in exports worth $1.2 billion to countries that did not implement tariffs (trade deflection), i.e., net destruction of U.S. agricultural exports was -$14.4 billion.[151] Second, non-retaliating countries experienced a 31 percent expansion of their exports to retaliating countries worth $13.5 billion (trade diversion).[152] These effects were also very concentrated at the product level, with trade destruction and trade diversion being particularly significant for soybeans at -$7.1 billion and $3.7 billion respectively, trade in pork products and coarse grains such as corn also being affected.[153] Overall, U.S. exporters appeared to have had difficulty in adapting their supply chains to non-retaliating countries, while other exporting countries were able to increase their market share in retaliating countries at the expense of the U.S.[154]

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[147] *See* Waugh, *supra* note 138, at 2.

[148] *See* Colin A. Carter & Sandro Steinbach, *The Impact of Retaliatory Tariffs on Agricultural and Food Trade*, at 1–47 (NBER, Working Paper No. 27147, 2020).
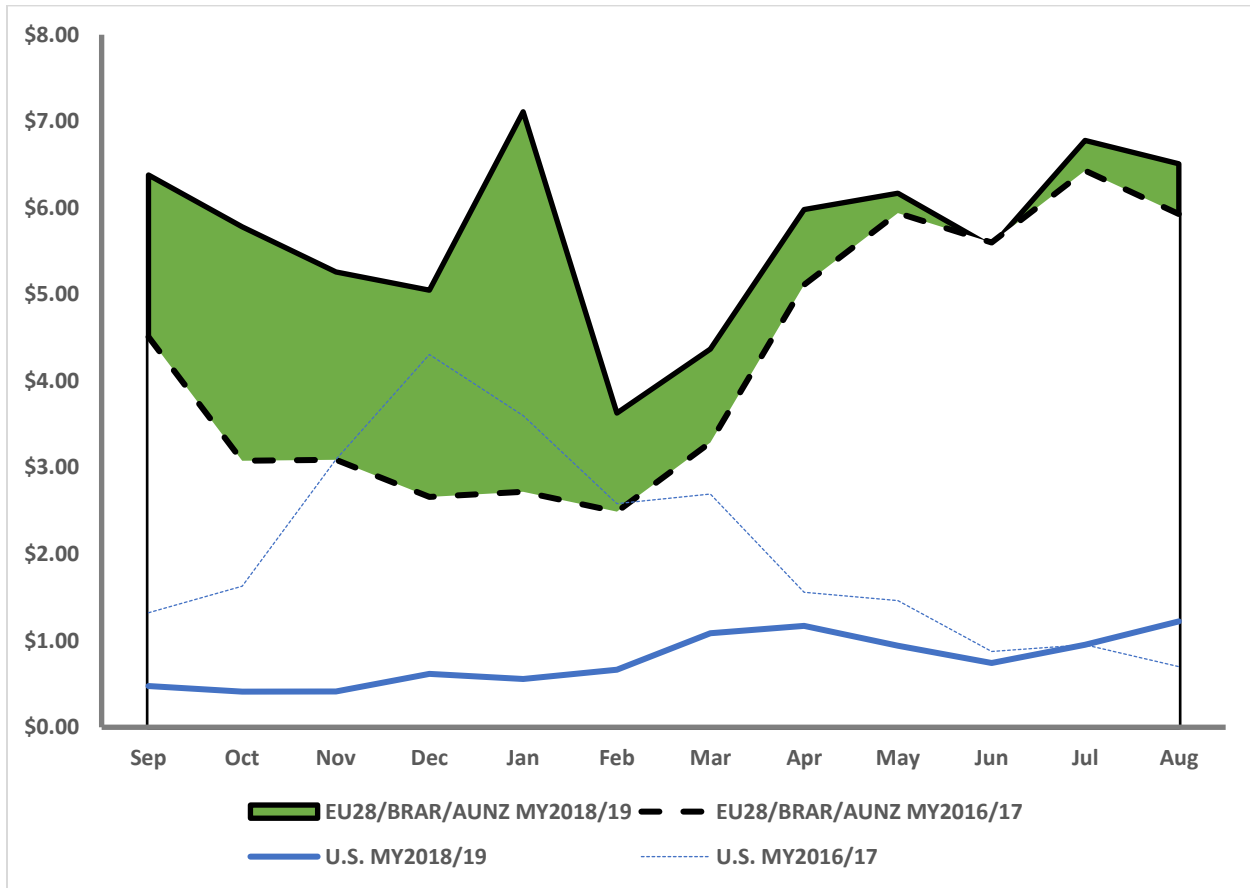
[149] *See id.* at 1.

[150] *See id.*

[151] *See id.* at 16–17.

[152] *See id.*

[153] *See id.* at 17.

[154] *See* Carter & Sandro Steinbach, *supra* note 148, at 17.

Figure 1. Trade Diversion Gains by Competing Suppliers during the U.S. - China Trade War, Marketing Year 2016/17 through Marketing Year 2018/19 ($ Billion)

Source: Sheldon and Grant.[155]
Notes: EU28 denotes the 28 member countries of the European Union; BRAR denotes Brazil and Argentina; AUNZ denotes Australia and New Zealand. Marketing years for the U.S. and other Northern Hemisphere countries typically run from September 1 through August 31 of the following year.

China's role in agricultural trade destruction and diversion has been very prominent.[156] Figure 1 plots the 2016/17 and 2018/19 agricultural marketing year (September-August), monthly values of combined exports to China by the EU28, Brazil and Argentina (BRAR), and Australia and New Zealand (AUNZ) alongside the monthly value of U.S. exports to China. The dotted lines trace export values to China in a typical marketing year prior to the dispute (2016/17), and the solid lines represent export values to China during the dispute (2018/19).[157] While trade diversion to the EU28, BRAR and AUNZ (shaded area) is not a perfect one-to-one displacement of what is normally the U.S.'s peak export marketing period, Figure 1 shows clearly the shift in sourcing of China's imports during the dispute.[158] At the peak of this shift in January 2019, China imported

[155] *See* IAN M. SHELDON & JASON GRANT, CAST COMMENTARY, GLOBAL TRADE IN AGRICULTURAL PRODUCTS THE LIKELY IMPACT OF COVID-19, at 7 (2020), https://aede.osu.edu/sites/aede/files/imce/images/QTA2020-3-COVID-Impacts.pdf.
[156] *See id.* at 5–9.
[157] *See id.* at 7.
[158] *See id.*

2.6 times ($7.1 billion total) more from competing suppliers compared to January 2017. The loss of market share in China has been particularly acute for U.S. soybean exports, the value of which fell from $12.2 to $4.5 billion over 2017-19.[159] Brazil was the key beneficiary from trade diversion between the U.S. and the rest of the world with soybean exports to China initially increasing from $20.3 billion in 2017 to $27.3 billion in 2018, before falling back in 2019 to $20.5 billion due to the outbreak of African Swine Fever in late 2018.[160]

As already discussed, tariff increases by a large country such as China usually depress world prices, resulting in a transfer from exporting to importing country(ies). This was certainly the case with China's retaliatory tariff of 25 percent imposed on imports of U.S. soybeans, and it is hard to over-emphasize the economic and political importance of soybean production and exports to the U.S. agricultural sector.[161] Prior to the start of the trade war, the United States exported $23.8 billion worth of soybeans, two and a half times greater than its exports of corn.[162] Under normal trading conditions, the United States would export approximately 50 percent of the soybeans it produced, with over half of those exports going to China, e.g., in the 2016/17 marketing year, the United States exported 36 million metric tons (MMT) of soybeans to China, 61 percent of total soybean exports – about one-in-three rows of harvested soybeans.[163] Compared to average soybean exports to China of 31 MMT over the three marketing years prior to 2018/19, U.S. exports fell by 65 percent after implementation of the tariff.[164] Given the modest increase in U.S. soybean exports to other countries such as Argentina, the EU, and Egypt, U.S. soybean exports fell overall by 10.4 MMT in 2018/19.[165]

Combined with a strong harvest in 2018 and the loss of market share to Brazil, the United States saw a significant decline in cash prices received by U.S. soybean farmers in the 2018/19 marketing year.[166] In many parts of the agricultural producing regions of the United States, there was a weakening of the "basis", i.e., the difference between what farmers are paid at their local elevator and the nearest futures price listed on the Chicago Board of Trade (CBOT).[167] The basis is a function of multiple factors, including, yields at harvest, transport costs, crop quality, seasonality, and the extent and cost of storage.[168] Given that the Chinese tariff displaced a significant proportion of U.S. soybean exports, this put downward pressure on the cash prices offered by the major commodity handling firms, which resulted in weakening of the basis.[169] By the beginning of September 2018, U.S. soybean producers were being quoted an average cash price of 95 cents/bushel below the futures contract for delivery that November, 30 cents/bushel lower than the previous year.[170]

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[159] *See id.* at 8.
[160] *See id.*
[161] *See* Michael K. Adjemian, Shawn Arita, Vince Breneman, Rob Johansson, & Ryan Williams, *Tariff Retaliation Weakened the U.S. Soybean Basis*, 34 CHOICES 1 (2019), https://www.choicesmagazine.org/UserFiles/file/cmsarticle_722.pdf.
[162] *See id.* at 1.
[163] *See id.*
[164] *See id.*
[165] *See id.*
[166] *See id.* at 2.
[167] See Adjemian, Arita, Breneman,Johansson, & Williams, *supra* note 161, at 2.
[168] *See id.*
[169] *See id.* at 2–3.
[170] *See id.* at 3.

In addition, with exports to China from U.S. ports on the Pacific coast falling by 94 percent in the second half of 2018, there was a significant spatial effect on cash prices received by soybean farmers in the upper Midwest, a region that lacks soybean crushing capacity and high transport costs to alternative ports on the Gulf. In addition, farm financial constraints and a lack of on-farm storage forced many farmers to sell their soybean crop at lower cash prices.[171] For example, by the end of September 2018, the average cash price of soybeans in North Dakota was over $2/bushel below the November futures price, a dollar less than the price offered the year before.[172] This confirms the empirical findings of Cavallo *et al.* reported earlier that there was imperfect passthrough of tariffs to Chinese import prices for agricultural commodities, i.e., U.S. soybean farmers bore a significant incidence of these tariffs.[173]

D. *U.S. Agriculture and the U.S.-China Trade Agreement*

Due to its political influence in the U.S., it is not surprising that agriculture was a critical component of Phase I of the USCTA that went into effect on January 14, 2020.[174] Specifically, China committed to purchasing an additional $12.5 and $19.5 billion worth of U.S. agricultural products above 2017 levels in 2020 and 2021, respectively, implying total agricultural imports of $36.5 billion in 2020 and $43.5 billion in 2021.[175] Essentially, these commitments by China constitute a voluntary import expansion (VIE), harking back to the era of managed trade between the United States and Japan in the 1980s.[176]

As a trade policy instrument, VIEs have rarely been used by policymakers, and are not even covered by typical undergraduate textbooks in international economics.[177] In principle, a Chinese agricultural VIE would work as follows: the targeted level of imports results in China's import demand curve shifting out, driving up the price received by U.S. exporters, and at the same time driving down the internal Chinese price, in order that its market can clear.[178] In other words, in the absence of an import subsidy from the Chinese government, agricultural commodity traders operating in China will incur a loss as they will have to sell the mandated extra imports at a loss. Part of this loss is transferred to Chinese consumers who benefit from lower prices, and part is transferred to U.S. exporters in the form of higher prices, the remainder being the deadweight loss due to inefficient U.S. production and Chinese consumption.[179]

In research reported by Robert Feenstra and Chang Hong, it has been calculated that, depending on a range of forecasts for Chinese economic growth, the gap between prices paid to U.S. exporters at the Chinese border and the price importers can charge Chinese consumers would require import subsidies paid by the Chinese government in the range 12-23 percent for 2020, and

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[171] *See id.* at 4.
[172] *See id.*
[173] *See* Cavallo, Gopinath, Naiman, & Tang, *supra* note 116, at 29–30.
[174] *See* USCTA, *supra* note 29.
[175] *See id.* at 6-1.
[176] *See* Chad P. Bown & Soumaya Keynes, *Why Trump Shot the Sheriffs: The End of WTO Dispute Settlement 1.0*, at 5 (Peterson Inst. for Internat'l Econ., Working Paper No. 20-4, 2020).
[177] *See* Steven M. Suranovic, *Price Effects of a Voluntary Import Expansion (VIE) / Import Subsidy: Large Country Case*, Ch. 90-30, INTERNATIONAL TRADE THEORY AND POLICY (1997), http://internationalecon.com/Trade/Tch90/T90-30.php.
[178] *See id.*
[179] *See id.*

42-59 percent in 2021, in order that Chinese commodity traders could break even.[180] This would represent a significant distortion to international agricultural commodity markets, with trade diversion to U.S. exporters away from other exporting countries, including Australia, Brazil, and Canada.[181]

Of course, these are implicit import subsidies, the only realistic way for China to meet their agricultural import commitments being through mandates to SOEs such as the China Oil and Foodstuffs Corporation (COFCO). However, as a practical matter, two interdependent factors militate against relying on SOEs to satisfy the import targets. First, private trading firms are mostly responsible for purchasing Chinese agricultural imports, for example, in 2015, they accounted for 72, 69, and 92 percent of Chinese imports of soybeans, cotton, and meat products, respectively.[182] Second, despite the USCTA, China has not reduced its retaliatory tariffs against U.S. imports, therefore private trading firms will have an incentive to purchase commodities from the world market at lower prices, thereby undermining the VIE.

Even before the COVID-19 pandemic, many observers suggested that meeting such agricultural import growth targets would be difficult.[183] Based on China's growth rate prior to the pandemic, it has been predicted that by 2021, there will be a shortfall of $10.5 billion in imports from the United States relative to the target, and based on a declining trend projection, the shortfall will be even larger at $23.6 billion.[184] This expected shortfall has already been borne out in the January-May 2020 China Customs Statistics. While improving on 2019 totals at the height of the trade war, 2020 January-May totals of $7.5 billion suggest Chinese agricultural imports from the United States are running at 50 percent below the Agreement's year-to-date target.[185] In light of the COVID-19 pandemic shock to the global economy, the WTO's forecast for China's real GDP growth in 2020 of -4.0 to -9.9 percent,[186] it seems very unlikely it will meet its import commitments under the USCTA, and even if it were able to do so, it would imply significant distortion to agricultural trade.

E. *Domestic Political Effects of the U.S.-China Trade War*

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[180] *See* Robert Feenstra & Chang Hong, *China's Import Demand for Agricultural Products: The Impact of the Phase One Trade Agreement*, at 1–2 (NBER, Working Paper No. 27383, 2020).

[181] *See id.* at 3.

[182] *See* Chad P. Bown & Mary E. Lovely, *Trump's Phase One Deal Relies on Chinese State-Owned Enterprises,* PETERSON INST. FOR INTERNAT'L ECON. (Mar. 3, 2020), https://www.piie.com/blogs/trade-and-investment-policy-watch/trumps-phase-one-deal-relies-chinas-state-owned-enterprises.

[183] *See America and China Reach a "Phase One" Trade Deal*, THE ECONOMIST (Dec. 14, 2019), https://www.economist.com/finance-and-economics/2019/12/14/america-and-china-reach-a-phase-one-trade-deal.

[184] *See* Chad P. Bown, *Unappreciated Hazards of the U.S.-China Phase One Dea*, PETERSON INST. FOR INTERNAT'L ECON. (Jan. 21, 2020), https://www.piie.com/blogs/trade-and-investment-policy-watch/unappreciated-hazards-us-china-phase-one-deal.

[185] *See* Chad P. Bown, *U.S.-China Phase One Tracker: China's Purchases of U.S. Goods*, PETERSON INST. FOR INTERNAT'L ECON. (July 2, 2020), https://www.piie.com/research/piie-charts/us-china-phase-one-tracker-chinas-purchases-us-goods.

[186] *See* EDDY BECKERS, ALEXANDER KECK, ROBERT KOOPMAN, & COLEMAN NEE, ECONOMIC RESEARCH AND STATISTICS DIVISION, WORLD TRADE ORGANIZATION, METHODOLOGY FOR THE WTO TRADE FORECAST OF APRIL 8, 2020, at 1–25 (2020), https://www.wto.org/english/news_e/pres20_e/methodpr855_e.pdf.

1. *Trade Liberalization and Economic Nationalism*

In evaluating the impact of the U.S.-China Trade War on U.S. political outcomes, it is important to understand how Chinese import penetration prior to the financial crisis, was a factor in pushing U.S. politics towards overt economic nationalism.[187] Trade liberalization in the post-war period has created both winners and losers in the United States, i.e., consumers and resources employed in the export-competing sectors have gained while resources such as less-skilled labor employed in the import-competing sectors have suffered the costs of job displacement and reduced incomes.[188] From the perspective of cost-benefit analysis, it is straightforward to demonstrate the gains from trade by appealing to the so-called Kaldor-Hicks compensation principle. Specifically, as long as benefits of trade liberalization outweigh the losses, in principle it is possible for the winners to compensate the losers and still be better off, i.e., there is the potential for a Pareto improvement whereby some agents in the U.S. economy are made better off without the remaining agents being made any worse off.[189]

The obvious problem with this principle is highlighted when compensation of losers is either insufficient or does not actually occur. This creates the potential for populism to gain ground, the political outcome being economic nationalism, i.e., opposition to free trade and increased isolationism, and a strong nationalist stance. As redistribution policies have either become less feasible or more costly, the mechanism for compensating losers from trade liberalization switches to protectionism. This also gets wrapped up in a political narrative of authoritarian nationalism drawing on populist grievances.[190]

Populism can be defined as a political movement that involves a combination, but not necessarily all, of anti-elitism, authoritarianism and nativism, as well as opposition to trade liberalization.[191] A key to populism is that society is seen as being divided into two groups: the people and the elite, the latter controlling government, business and the financial sector, who are perceived as not acting in the best interests of the people. This idea was clearly captured in speeches made by Donald Trump both before and after his election as U.S. president. Populists believe that only they represent the "true people", and as a consequence some set of voting citizens can be convinced to reject the "moral legitimacy" of the elite.[192]

Trade economists Gene Grossman and Elhanan Helpman argue that populism is a specific form of "identity politics", such that voters' preferences over trade policy reflect both their economic self-interest as well as their concerns for the groups in society with whom they identify.[193] The authors then posit a "populist revolution" driven by a significant external event such as the China import shock to the U.S. economy which widens the income distribution. As a

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[187] *See* Steve McCorriston & Ian M. Sheldon, *Economic Nationalism: U.S. Trade Policy vs. Brexit*, 14 OHIO ST. BUS. L.J. 64, 65–70 (2020).

[188] *See* Dani Rodrik, *Populism and the Economics of Globalization*, 1 J. INTERNAT'L BUS. POL'Y 12, 17–18 (2018); Pol Antràs, Alonso de Gortari, & Oleg Itskhoki, *Globalization, Inequality and Welfare*, 108 J. INTERNAT'L ECON. 387, 387–412 (2017).

[189] *See id.* at 388.

[190] *See* Italo Colantone & Piero Stanig, *The Trade Origins of Economic Nationalism: Import Competition and Voting Behavior in Western Europe*, 62 AM. J. POL. SCI. 936, 938 (2018).

[191] BARRY EICHENGREEN, THE POPULIST TEMPTATION: ECONOMIC GRIEVANCE AND POLITICAL REACTION IN THE MODERN ERA 1 (2018); *see* Rodrik, *supra* note 188, at 16.

[192] *See* JAN-WERNER MÜLLER, WHAT IS POPULISM? 1–6 (2016).

[193] *See* Gene M. Grossman & Elhanan Helpman, *Identity Politics and Trade Policy*, at 1–2 (NBER, Working Paper No. 25348, 2018).

result, less-skilled workers reject the legitimacy of the elites, and instead see the nation as synonymous with their type. From this they show how a dramatic rise in populism could lead to a substantive shift in a country's trade policy towards protectionism. The political-economic outcome is one where a political party running on a populist platform implements a discrete jump in tariffs imposed on imported goods.[194]

There is now a growing body of research examining the impact of the China import shock on U.S. employment and other metrics.[195] For example, Justin Pierce and David Schott have shown that U.S. extension of permanent normal trade relations (PNTR) to China in 2000 in anticipation of China's entry into the GATT/WTO in 2001 was associated with a sharp drop in U.S. manufacturing employment between 2000 and 2003, the effect being stronger in industries most affected by a reduction in uncertainty about tariff rates.[196] Other researchers have found a link between the China import shock and a wider range of economic and social issues including crime rates,[197] increases in household debt,[198] declines in marriage rates,[199] and increased death from drug overdoses.[200]

Probably the most significant insights into the domestic consequences of the China "shock" are associated with David Autor and colleagues in a series of articles.[201,202] Their work on the U.S. measures the geographic exposure of labor markets across the United States to the increase in imports from China. The "shock" feature of Chinese imports relates to the rapid rise primarily in manufacturing imports from China up to 2007.[203] The rising international competitiveness of China has been associated with increased openness in China that allowed Western firms to outsource production activities to China, the relaxation of central planning, accession to the WTO in 2001 and possible manipulation of their exchange rate.[204] Not only has the rise in China's competitiveness given rise to concerns about "unfair" trade, but the extent and speed of the rise in imports from China forced considerable adjustment in the United States with the resulting impact on regional labor markets where manufacturing activities are located.

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[194] *See id.* at 3–4.

[195] *See* Justin R. Pierce & Peter K. Schott, *The Costs of U.S. Trade Liberalisation with China Have Been Acute for Some Workers*, at 13–18, *in* MEREDITH A. CROWLEY, TRADE WAR: THE CLASH OF ECONOMIC SYSTEMS ENDANGERING GLOBAL PROSPERITY (2019), https://voxeu.org/content/trade-war-clash-economic-systems-threatening-global-prosperity.

[196] *See* Justin R. Pierce & Peter K. Schott, *The Surprisingly Swift Decline of US Manufacturing Employment*, 106 AM. ECON. REV. 1632, 1632–35 (2016).

[197] *See* Yi Che & Xun Xu, *The China Syndrome in US: Import Competition, Crime, and Government Transfer*, at 1–4 (MPRA, Paper No. 68135, 2015).

[198] *See* Jean-Nöel Barrot, Erik Loualiche, Matthew Plosser, & Julien Sauvagnat, *Import Competition and Household Debt*, Federal Reserve Bank of New York Staff Reports, Staff Report No. 821, at 1-4 (2017), https://www.newyorkfed.org/medialibrary/media/research/staff_reports/sr821.pdf.

[199] *See* David H. Autor, David Dorn, & Gordon H. Hanson, *When Work Disappears: Manufacturing Decline and the Falling Marriage-Value of Men*, at 1–2 (NBER ,Working Paper No. 23173, 2018).

[200] *See* Justin R. Pierce & Peter K. Schott, *Trade Liberalization and Mortality: Evidence from U.S. Counties*, at 1 –3 (NBER, Working Paper No. 22849, 2016).

[201] *See* David H. Autor, David Dorn, & Gordon H. Hanson, *The China Shock: Learning from Labor Market Adjustment to Large Changes in Trade*, 8 ANN. REV. ECON. 205, 207 (2016).

[202] *See* David H. Autor, David Dorn, & Gordon H. Hanson, *The China Syndrome: Local Labor Market Effects of Import Competition in the United States*, 103 AM. ECON. REV. 2121, 2122 (2013).

[203] *See* Bown, supra note 96, at 112–13.

[204] *See* Autor, Dorn, & Hanson, *supra* note 201, at 209–15.

Due to labor immobility in the U.S., the impact of Chinese imports was particularly strong across certain U.S. states: wages fell dramatically, women withdrew from the workforce, there was an increase in demand for social benefits and disability allowances and when workers were re-engaged in the same locality, re-hiring was at wages much lower than previous employment.[205] This was the main feature of the China import shock: the geography was felt dramatically in several, typically southern and eastern states while other states escaped the impact of the rise of China given the differences in industrial structure. In sum, looking beyond the aggregate of "national" welfare, the impact of the rapid growth of China, had a significant effect on certain parts of the United States.

How did the China shock affect polarization of U.S. voting patterns? Autor *et al*. address this issue by extending their analysis of the China "shock" to an examination of voting patterns across the United States.[206] Using detailed data on voting in congressional and presidential elections, they report two main results. First, while accounting for other determinants of voting patterns, e.g., education, age, white collar etc., due to the dramatic rise in imports from China, voters were less likely to support moderate candidates of either main political party. There was a swing to either end of the political spectrum reflecting an increase in polarization in the U.S. political environment. Second, in presidential elections, in the districts most exposed to competition from Chinese imports, there was an increase in support for Republican candidates.[207] Although there may be other factors that have contributed to the divisiveness of U.S. politics in recent years, these authors have established a clear link between trade liberalization and political outcomes and ties closely with the "America First" slogan and the targeting of tariffs by President Trump. As Autor *et al*. point out, both presidential candidates in 2016 explicitly highlighted competition from China in their electoral campaigns, the results here suggesting that the competition from China favored the Republican candidate.[208]

2. *The Trade War and U.S. Voting Behavior*

As described in a series of articles by Chad Bown and co-authors, the Administration's approach to trade policy has also been driven by: first, a broad range of technical and legal concerns about Chinese industrial policy, including the role of SOEs and subsidies, theft of intellectual property, and forcible acquisition of technology;[209] second, the inability of GATT/WTO rules to effectively address such policy concerns, especially China's use of subsidies;[210] and, third, broader concerns about the WTO dispute settlement system, notably perceived judicial over-reach by the Appellate Body.[211]

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[205] *See* Autor, Dorn, & Hanson, *supra* note 202, at 2158–59.

[206] *See* David Autor, David Dorn, Gordon Hanson, & Kaveh Majlesi, Importing Political Polarization? The Electoral Consequences of Rising Trade Exposure, at 1–2 (NBER, Working Paper No. 22637, 2017); *see also* Yi Che, Yi Lu, Justin R. Pierce, Peter K. Schott, & Z. Tao, *Does Trade Liberalization with China Influence U.S. Elections?*, at 1–40 (NBER, Working Paper No. 22178, 2016).

[207] *See id.* at 1–6.

[208] *See id.* at 4.

[209] *See* Bown, supra note 99, at 128–30.

[210] *See* Chad P. Bown & Jennifer A. Hillman, *WTOing a Resolution to the China Subsidy Problem*, 22 J. INTERNAT'L ECON. L. 557, 558–59 (2019).

[211] *See* Bown & Keynes, *supra* note 176, at 11–13; OFFICE OF THE U.S. TRADE REPRESENTATIVE, 2018 TRADE POLICY AGENDA AND 2017 ANNUAL REPORT OF THE PRESIDENT OF THE UNITED STATES ON THE TRADE AGREEMENTS PROGRAM 2, 28 (2018),

However, given President Trump's anti-China rhetoric, and the outcome of the 2016 election, it is not surprising that his administration chose to follow a strategy of power-based bargaining in the form of higher tariffs against China, as opposed to seeking a broad coalition with other countries to pursue a case against China at the WTO.[212] The previous discussion of the evidence presented in Fajgelbaum *et al.* suggests that tariffs were targeted for maximum electoral impact,[213] which leads to a natural question: did the trade war affect the outcome of the 2018 mid-term elections?

The available empirical evidence suggests the answer to this question is that it did. The most detailed analysis has been conducted by economists Emily Blanchard, Chad Bown, and Davin Chor.[214] The focus of their statistical analysis is on the relationship between U.S. voting patterns and county-level policy exposure, the latter being measured by the extent to which counties were protected by tariffs on U.S. imports, the extent to which they were affected by retaliatory tariffs on U.S. exports, and the degree to which they stood to gain from subsidies extended to farmers under the 2018 Market Facilitation Program (MFP).[215] The latter policy was put in place in response to tariffs placed on U.S. agricultural exports. In addition, their analysis also controls for the extent to which local health insurance coverage was at risk from repeal of the Affordable Care Act (ACA).[216]

Using data from David Liep's U.S. Election Atlas, the authors constructed a dependent variable measuring the county-level vote share received by Republican candidates for each of the 2012-2018 elections to the U.S. House of Representatives, plus the 2016 Presidential election.[217] The voting pattern variable is then related to a series of independent variables:

(1) Import tariff shocks were defined as a county's average per-worker exposure to increased U.S. tariffs, measured at the HTSUS 8 digit level, and the retaliatory tariff shock was defined as per-worker exposure to retaliatory tariffs by Canada, China, the EU, and Mexico.[218] These tariff increases were combined with initial bilateral trade volumes by industry and country, which were then mapped into a measure of a county's share of national employment in a specific industry using the 2016 U.S. County Business Patterns.[219]

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https://ustr.gov/sites/default/files/files/Press/Reports/2018/AR/2018%20Annual%20Report%20FINAL.PDF. *See also infra* text accompanying notes 00.

[212] *See* Jennifer Hillman, Testimony Before the U.S.-China Economic and Review Security Commission, The Best Way to Address China's Unfair Policies and Practices Is Through a Big, Bold Multilateral Case at the WTO, at 2 (June 8, 2018). https://www.uscc.gov/sites/default/files/Hillman%20Testimony%20US%20China%20Comm%20w%20Appendix%20A.pdf?mod=article_inline; *see also* Robert Z. Lawrence, Policy Brief 18-17, *How the United States Should Confront China Without Threatening the Global Trading System*, PETERSON INST. FOR INTERNAT'L ECON. 6–7 (2018). https://www.piie.com/system/files/documents/pb18-17.pdf.

[213] *See* Fajgelbaum, Goldberg, Kennedy, & Khandelwal, *supra* note 112, at 49–52.

[214] *See* Emily J. Blanchard, Chad P. Bown, & Davin Chor, *Did Trump's Trade War Impact the 2018 Election?*, at 1–35 (NBER, Working Paper No. 26434, 2019).

[215] *See id.* at 2.

[216] *See id.* at 2.

[217] *See id.* at 4.

[218] *See id.* at 4–7, 20.

[219] *See id.* at 20–21. The trade data come from the World Bank WITS database.

(2) Given MFP, which in 2018 consisted of the U.S. Department of Agriculture (USDA) administering the payment of $12 billion in subsidies to producers of soybeans, sorghum, corn, wheat and some other commodities, a variable was constructed to measure the total farm subsidy received by a county weighted by its working age population.[220]

(3) Two county-level healthcare variables were constructed based on the U.S. Census Bureau American Community Survey, one measuring the share of the population having health insurance just prior to the 2018 mid-term election, and a second measuring the change in the share of those having health insurance since ACA came into effect in 2010.[221]

(4) A set of county-level demographic (age, gender, and race) and socioeconomic (employment shares, unemployment rate, mean income, education) control variables were used, drawing on the U.S. Census, the County Business Patterns dataset, and the U.S. Census Bureau American Community Survey.[222]

The key econometric result reported in this study was that greater local exposure to the economic impact of the trade war was associated with a decline in support and loss of seats in the House of Representatives for Republican candidates in the 2018 mid-term elections.[223] Importantly, this result was mostly a function of the extent to which a county was affected by the retaliatory tariffs on U.S. agricultural exports, especially to China, most notably in counties where Trump had narrowly lost the popular vote in the 2016 Presidential election.[224] The agricultural subsidies offered by the MFP partially offset the decline in Republican vote share, but due to the concentrated set of counties where these were targeted, they had no significant effect on the swing in seats.[225] In addition, the results were statistically robust to inclusion of healthcare variables.[226]

The political impact of retaliatory tariffs against U.S. agricultural exports, particularly soybeans, also shows up in the research of political scientists Olga Chyzh and Robert Urbatsch.[227] In their empirical analysis, they analyzed the impact of a county's reliance on soybean production on the change in the Republican vote share in the 2016 and 2018 elections to the House of Representatives.[228] The latter variable was constructed as an odds ratio of Republican-to-Democrat county-level votes between the two elections, based on data collected from Secretaries of State or equivalents,[229] while the former variable was measured in both soybean bushels and value of soybean sales, using 2012 data from USDA.[230] In addition, other control variables included

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[220] Blanchard, Bown, & Chor, *supra* note 214, at 22. The MFP subsidy rates are drawn from the Congressional Research Service, while county-level commodity production comes from USDA's National Agricultural Statistics Service (NASS).

[221] *See id.* at 8–9.

[222] *See id.* at 9.

[223] *See id.* at 18.

[224] *See id.* at 18.

[225] *See id.*

[226] Blanchard, Bown, & Chor, *supra* note 214, at 18.

[227] *See* Olga Chyzh & Robert B. Urbatsch, *Bean Counters: The Effect of Soy Tariffs on Change in Republican Vote Share Between the 206 and 2018 Elections*, at 1–16 (Digital Repository Iowa State University, 2019), https://lib.dr.iastate.edu/cgi/viewcontent.cgi?article=1056&context=pols_pubs.

[228] *See id.* at 2.

[229] *See id.* at 4–5.

[230] *See id.* at 6–7.

county-level GDP per capita, unemployment, education, urbanization, ethnicity, and percent of population who voted for Donald Trump in the 2016 Presidential election.[231] The latter data were drawn from the BEA and U.S. Census Bureau American Community Survey, and the Cook Political Report's Partisan Voting Index. The key econometric result of this study is that there was a direct negative relationship between a county's economic reliance on soybean production and the decrease in Republican vote share between 2016 and 2018.[232]

This empirical research adds another dimension to the argument that the Trump Administration's choice of power-based bargaining over trade policy was rather short-sighted, generating a whole sequence of unintended consequences. Not only has the resulting trade war inflicted non-trivial economic damage on the U.S. economy, but at the local level the economic damage has also resulted in political damage to the incumbent political party. Notwithstanding the fact that the China import shock resulted in greater political polarization in the United States, and concomitant support for nationalist and protectionist trade policies, the use of tariffs by the Administration appears to have backfired. Importantly, retaliating countries such as China, in specifically targeting U.S. agricultural exports, seem to have neutralized any potential political benefits from protecting some sectors of the U.S. economy.[233]

In this context, it is not surprising that President Trump has placed so much public emphasis on the Phase I of USCTA, and China's commitment to substantially increasing their agricultural imports from the United States in 2020 and 2021. However, the potential for extensive trade diversion due to the USCTA runs the risk of negatively affected exporting countries such as Brazil filing a complaint at the WTO. In addition, the subsidies targeted at U.S. farmers through the MFP program, designed to cushion them from the effects of retaliatory tariffs, could find the United States being in breach of the WTO's Agreement on Agriculture (AoA).[234] Under the AoA, the United States has committed to not spending more than $19.1 billion per year on trade-distorting farm subsidies, but analysis by the Environmental Working Group (EWG) indicates federal farm payments for the 2018/19 crop year will reach $34 billion, 78 percent above the cap, with payments in the 2019/20 crop year also likely to exceed the cap.[235] Australia, Brazil, Canada, the EU, and New Zealand have already complained that U.S. farm subsidies are in breach of the AoA.[236] With the crippling of the WTO dispute settlement system, there is a very real risk that members such as the EU will unilaterally retaliate with tit-for-tat farm subsidies, creating a new front in the trade war.[237]

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[231] *See id.* at 7–8.

[232] *See id.* at 10.

[233] *See* Fetzer &Schwarz, *supra* note 141, at 5–6. These authors present empirical evidence that targeted retaliation by China and other countries has been effective, Republican candidates faring worse in the 2018 mid-term elections.

[234] *See* Agreement on Agriculture, Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex 1A, 1867 U.N.T.S. 410.

[235] *See* Jared Hayes, *Farm Bailout Payments Could Ignite New Front in Trade War*, ENVIRON. WORKING GRP. AGMAG (June 17, 2020), https://www.ewg.org/agmag/2020/06/farm-bailout-payments-could-ignite-new-front-trade-war.

[236] *See* Bryce Baschuk, *Trump's $16 billion Farm Bailout Criticized at WTO*, BLOOMBERG (June 17, 2019). https://www.bloomberg.com/news/articles/2019-06-17/eu-china-push-back-against-trump-s-16-billion-farm-bailout.

[237] *See* Mike Dorning, *Trump Farm Bailouts Raise Risks of Reprisals from Trade Partners*, BLOOMBERG (June 18, 2020), https://www.bloomberg.com/news/articles/2020-06-18/trump-farm-bailouts-raise-risks-of-reprisals-from-trade-partners.

IV. CONCLUSION

The United States' power-based approach to trade has achieved some notable successes in the legal arena of international trade. The United States was able to decommission the WTO Appellate Body and to immunize itself from legal challenges to its acts in defiance of WTO law. In the area of economics and politics, however, the U.S. power-based approach has achieved mixed results, due to the unpredictable and uncertain variables involved in these areas.

This study indicates that the U.S. power-based approach to China has led to some negative economic and political effects on the United States. In particular, contrary to the assertion by the Trump Administration, the empirical evidence indicates unequivocally that tariffs imposed on China are not paid for by China but constitute a tax on U.S. consumers. This evidence suggests that the most effective use of a power-based approach may be against countries that lack the political will or economic power to engage the United States in a prolonged trade war or standoff. For example, when faced with U.S. tariffs imposed on steel and aluminum imposed in 2018, South Korea immediately renegotiated the terms of the Korea-United States Trade Agreement (KORUS) and offered new trade concessions to the United States.[238] South Korea agreed to limit its exports of steel to 2.68 tons or roughly 70 percent of the volume of steel exports from Korea to the United States for the years 2015-17.[239] The United States immediately declared that the concessions by South Korea vindicated its approach.[240] Treasury Secretary Steve Mnuchin boasted, "I think that the strategy has worked, quite frankly. We announced the tariff. We said we were going to proceed. But, again, we said we'd simultaneously negotiate."[241] Mnuchin claimed that South Korea's concessions were a "win-win" situation for both countries.[242] When faced with the same steel and aluminum tariffs, the EU also swiftly agreed to negotiations, leading the Trump Administration to "declare a resounding victory for Trump and his confrontational stance."[243] Commerce Secretary Wilbur Ross proclaimed, "This is a real vindication of the president's trade policy."[244] Unlike South Korea, the EU had the economic power to engage in a standoff with the United States, but it lacked the political will.

By contrast, China is a nation that has the economic power to fight a costly trade war. It is also a nation whose leaders, the Communist Party, cannot accept the perception of being bullied by the United States, but is willing to play a dangerous game of mutual destruction instead. This Article has indicated that the U.S.-China Trade War was costly to the United States resulting in a heavy tax on U.S. consumers and losses of at least $7.3 billion dollars in 2018 alone. The distribution of the costs of U.S. tariffs was also unexpected as it was not possible to determine beforehand that the costs would fall on areas of the United States that were vital to the political support of the current Administration.

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[238] Chow, *supra* note 73, at 28–29.

[239] *Id.*

[240] *Id.*

[241] *Id.*

[242] *Id.*

[243] *Trump Declares Victory for Farmers in Trade Spat with EU*, EURACTIV (July 27, 2018), https://www.euractiv.com/section/economy-jobs/news/trump-declares-victory-for-farmers-in-trade-spat-with-eu/.

[244] *Id.*

China's retaliatory tariffs greatly increased the uncertainties of the costs of the trade war. China chose to impose tariffs in an area to cause maximum pain and distress: agricultural products and, in particular, U.S. soybean production. Coincidentally, the farmers in Midwestern states most affected by the tariffs were a key constituency that helped propel Trump to the U.S. presidency in 2016. Although China's imposition of tariffs on U.S. imports would also inflict losses on its consumers, China was able to avoid many of these losses by finding alternative sources of soybeans from Brazil, and other countries. The loss of its major export markets for soybeans caused serious financial losses for U.S. farmers in the Midwest that may have contributed to reverses for the Republican Party in the mid-term elections of 2018.

As both political parties in the United States seem to harbor little affection for China and the WTO, it is far from certain that the United States will abandon its power-based approach to trade with China after the presidential election of 2020, no matter who wins. It was the Democrat Administration of Barack Obama that set in motion the events that led to the crippling of the WTO dispute settlement system and the ascendance of the U.S. power-based approach in the legal arena of international trade dispute resolution.[245]

The lessons gleaned from this Article suggest that a power-based approach is most effective when the target of confrontation trade tactics lacks the economic power, such as South Korea, or the political will, such as the EU, to engage in a trade standoff with the United States. The United States may be able draw assurance from the knowledge that many, if not most, other nations fall in either one of these two categories, but China is not one of them.

The benefits of using a power-based approach are far less certain and considerably riskier when faced with an opponent such as China. With such an opponent, the United States must carefully assess where the potential economic and political costs will fall but the United States must be cautioned that it is difficult, if not impossible, to predict with accuracy the economic or political costs of such a battle. There are too many variables to make such a prediction certain and the power-based approach is inherently more unpredictable than the negotiation approach of the WTO that the United States rejects and seeks to replace. It already appears that the unanticipated economic and political costs of the China tariffs may have backfired in the 2018 mid-term elections and that additional electoral losses might further ensue. The risks of using a power-based approach to trade are the highest when faced with a country such as China that has the economic power and political will to endure a prolonged battle and play a dangerous game of mutual pain and destruction with the United States.

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[245] *See supra* note 87.