Global Economic Outlook: 
Risks from the Trade War

Ian Sheldon
Ohio State University
sheldon.1@osu.edu
https://aede.osu.edu/research/andersons-program

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Global Economic Outlook

- Over past year, broad-based slowdown in global economy in terms of industrial production and trade (Figure 1)

- Driven by:
  - Downturn in auto production and sales
  - Weak business confidence due to US-China trade war
  - Slowdown in Chinese economy

- Slowdown in industrial production has fed into decline in trade growth (Figure 2)
Industrial Production and Trade

Figure 1

(Year-over-year % change)

Source: IMF, October 2019
Contributions to Global Imports

Figure 2

Source: IMF, October 2019
Risks Skewed to Downside

- Risks: (i) disruptions to trade/supply chains, (ii) declines in risk appetite/flight to safe assets, (iii) political uncertainty and conflict

- IMF forecasts that if US-China trade war were to continue, cost to global economy of $700 billion by end of 2020

- About 1% knocked off US GDP growth since start of trade war (Figure 3)

- View of IMF, World Bank and others: reduce trade tensions and return to solving issues via multilateral system, i.e., WTO
Impact on Real US GDP

Figure 3 (% Deviation from 2017 base)

Source: IMF, October 2019
Context: US-China Trade Issues

Tensions have risen over Chinese trade and economic policies – key reason for current trade war:

- Extensive network of industrial policies that protect domestic sectors/firms – especially state-owned enterprises (SOEs)
- Failure to provide protection for intellectual property rights (IPRs) and forced technology transfer
- China has not met all obligations since accession to World Trade Organization (WTO) in 2001
- Exchange rate policy
Phase One Trade Deal with China

7 chapters in Phase One Trade Deal:

- **Intellectual Property**: commitment by China to prevent theft of IPRs
- **Technology Transfer**: commitment by China to stop forced transfer of technology as condition of market access
- **Agriculture**: removal of non-tariff barriers on US products such as meat and poultry
- **Financial Services**: removal of barriers to US providers of financial services
Phase One Trade Deal with China

• **Currency:** commitments by China to refrain from competitive devaluation of RMB

• **Expanding Trade:** China has committed to expanding imports of goods and services from US by $200 billion/annum over next two years

  Specific commitment to increase agricultural imports to $36.5 billion (2020) and $43.5 (2021)

• **Dispute Resolution:** arrangement to ensure effective implementation of agreement and timely resolution of bilateral disputes
Tariff Commitments

♦ US actions on tariffs:
  • 15% tariffs on $162 billion of imports, scheduled for December 15, not imposed
  • Tariffs on $100 billion of imports imposed on September 1, 2019 will be reduced to 7.5%
  • 25% tariffs on $250 billion introduced in 2018 will remain in place

♦ China’s actions on tariffs:
  • Will not impose retaliatory tariffs due on December 15
Assessment of Deal

◊ Tariffs:

• Pause in tariff escalation – but no removal of existing tariffs

• Average US tariff remains at 19.3%, covering 65% of imports from China

• Average Chinese tariff remains at 20.9% covering 57% of imports from US

◊ 2018-20 impact of tariffs:

• Costs borne by US producers and consumers in form of higher prices ≈ $138 billion
Pause in Tariff Escalation

Figure 4

Source: Bown, PIIE, 12/19/19
Assessment of Deal

- **Overall Import Commitments by China:**
  - Increasing imports up to $200 billion/annum seems inconsistent with China maintaining its average tariffs at 20.9%
  - Requires 92% increase in US exports of covered goods and services compared to 2017 (Figure 5)
  - Will probably require considerable trade diversion
  - China also likely to import goods and services not covered by deal from elsewhere – with potential for negative effects on US jobs
Overall Import Commitments

Figure 5

Total US goods and services exports to China, billions USD


Source: Bown, PIIE (1/21/20)
Assessment of Deal

Agricultural Import Commitments by China:

- Agriculture has been caught in crossfire of trade war affecting wide range of commodities (Figure 6)
- Significant loss of market share to other major exporters such as Brazil and Australia (Figure 7)
- If deal is met, would be significant boost to US agriculture – dwarfing forecast benefits of USMCA ($2.2 billion/annum increase in exports, USITC, 2019)
- Should be put in context: prior to trade war, China imported $24 billion in 2017, and record of $29.6 billion in 2013 (USDA)
Scope of Trade War

Figure 6: 2017 Value of US Agricultural Exports Facing Retaliation

Source: Grant et al. (2019)
Lost Market Share in China

Figure 7: US Loss of Market Share 2017-18

Source: Grant et al. (2019)
Assessment of Deal

Serious questions raised about agricultural import commitments by China:

- No commodity specifics in agreement
- Some skepticism China can import this much in relatively short period of time (Figure 8)
- Chinese reliance on “managed trade” – cedes a lot of control to them
- Potential for significant diversion of imports from Brazil and other exporters to US - could result in WTO dispute (Figure 9)
Figure 8: US Agricultural Exports to China

- 2018: $9 bn
- 2021: $43.5 bn

Source: Bown, PIIE (1/21/20)
Problems with Managed Trade

- Inconsistency between commitments and Chinese claim that they will import at market prices
- Voluntary import expansion can only work if China explicitly discriminates in favor of US
- If imports are managed through state trading agencies such as COFCO, link between supply and end-user is broken
- Risk of US suppliers switching from sustainable market relationships to riskier one with China
- Trade war has exposed risk of being overly-dependent on China as an export market
Potential for Trade Diversion

Figure 9: Chinese Imports by Sector and Country (2017)

Chinese imports by sector and country, 2017

<table>
<thead>
<tr>
<th>Agriculture</th>
<th>Amount, billions USD</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>US</td>
<td>Rest of world</td>
</tr>
<tr>
<td>Oilseeds</td>
<td>13.9</td>
<td>25.7</td>
</tr>
<tr>
<td>Meats</td>
<td>1.2</td>
<td>8.3</td>
</tr>
<tr>
<td>Seafood</td>
<td>1.3</td>
<td>6.9</td>
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<tr>
<td>Cereals</td>
<td>1.5</td>
<td>5.8</td>
</tr>
<tr>
<td>Cotton</td>
<td>1.0</td>
<td>1.3</td>
</tr>
<tr>
<td>Other agricultural commodities</td>
<td>5.1</td>
<td>51.9</td>
</tr>
</tbody>
</table>

Source: Bown, PIIE (1/21/20)
Conclusions

- Costs of trade war only partially reduced with Phase One Trade Deal, i.e., tariffs still in place
- Chinese commitments: IP protection, technology transfer, non-tariff barriers/agricultural imports, and trade in services
- Is “managed trade” sustainable?
- Will enforcement of deal work?
- No mention of China’s use of subsidies and role of SOEs – key to trade war starting in first place