

“U.S. Trade Policy: Where are we Heading?”

Ian Sheldon (Ohio State University)

sheldon.1@osu.edu

<https://aede.osu.edu/research/andersons-program>

Featured Presentation



Agricultural Outlook Conference

August 14-15, 2019

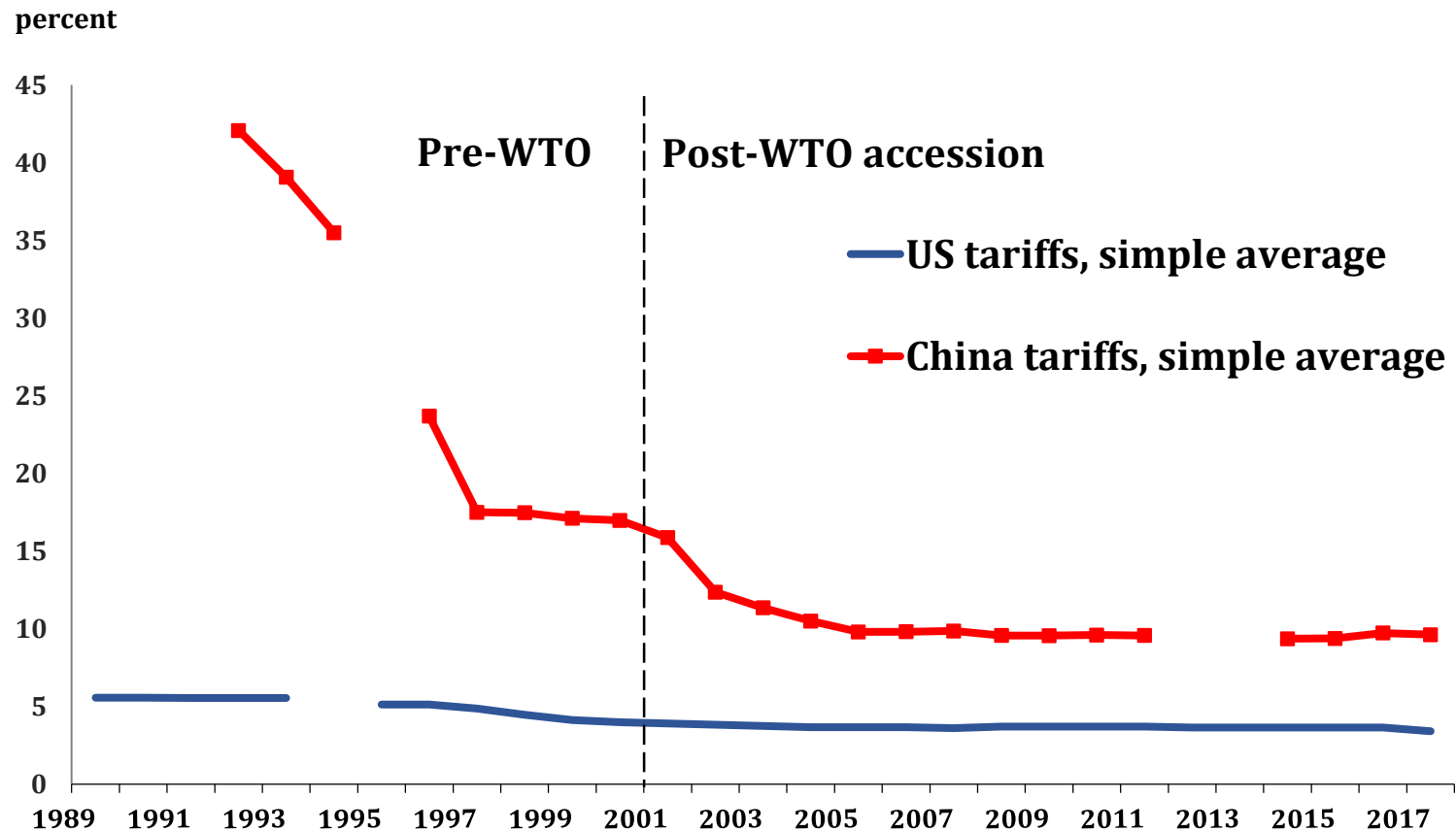
Cincinnati, OH



US trade policy: rules-based



 US  OECD	LOW TARIFFS	HIGHTARIFFS
LOW TARIFFS	<u>GATT/WTO:</u> High trade volume	Beggar-thy-neighbor
HIGHTARIFFS	Beggar-thy-neighbor	<u>Inter-war period:</u> Low trade volume

Tariffs: US vs. China



Source: Bown (April, 2019)

US trade policy: rules-based to power-based

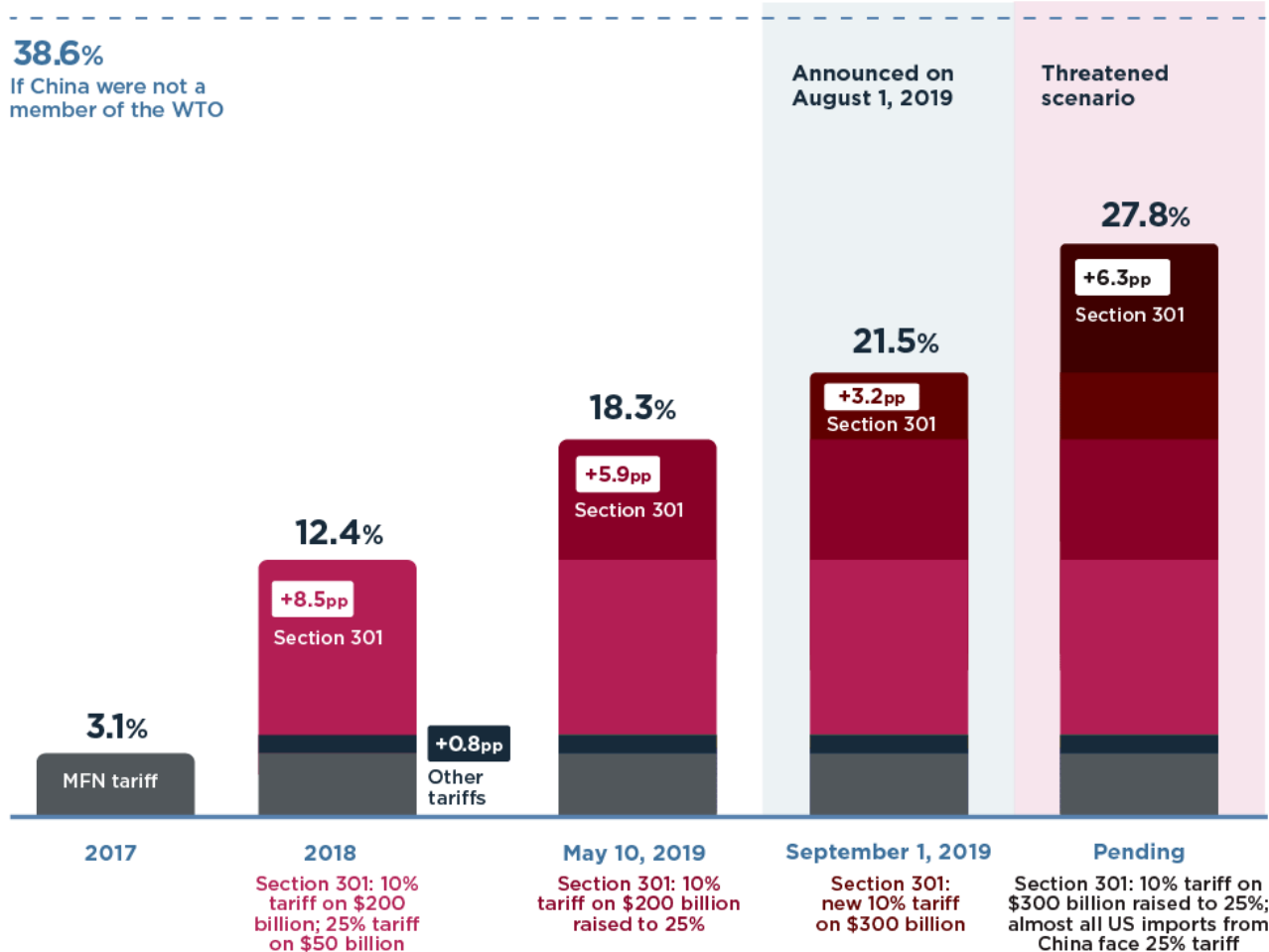
<div> US</div> <div> China</div>	LOWER AVERAGE TARIFFS	HIGHER AVERAGE TARIFFS
LOWER AVERAGE TARIFFS	GATT/WTO Average MFN=3.4%	Power-based Bargaining
HIGHER AVERAGE TARIFFS	Accession to WTO Average MFN=9.6%	Trade war

Level of tariffs against China

Trump's Latest Trade War Escalation Will Push Average Tariffs on China Above 20 Percent

38.6%

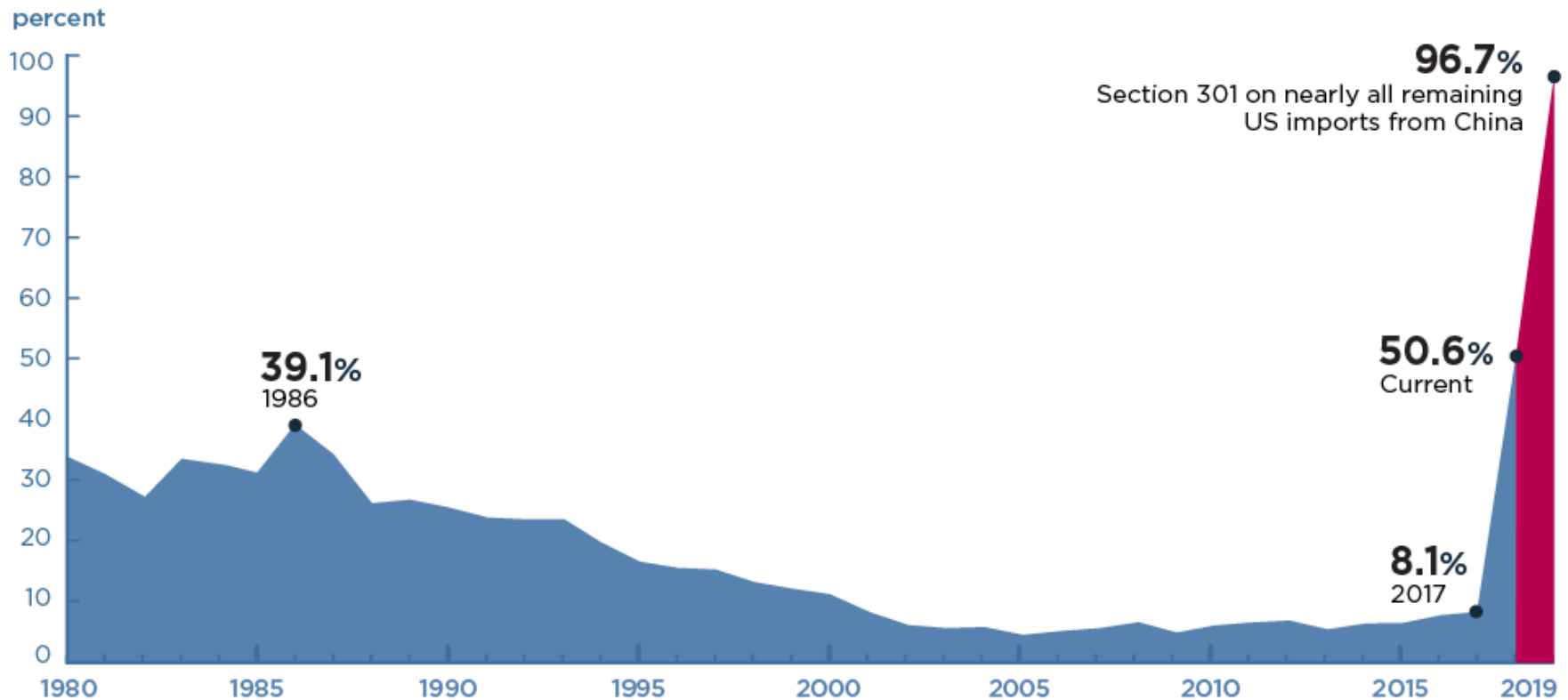
If China were not a member of the WTO



Source: Bown and Zhang (August, 2019)

Coverage of tariffs against China

Tariffs on almost all remaining US imports from China would raise special trade protection coverage to unprecedented level

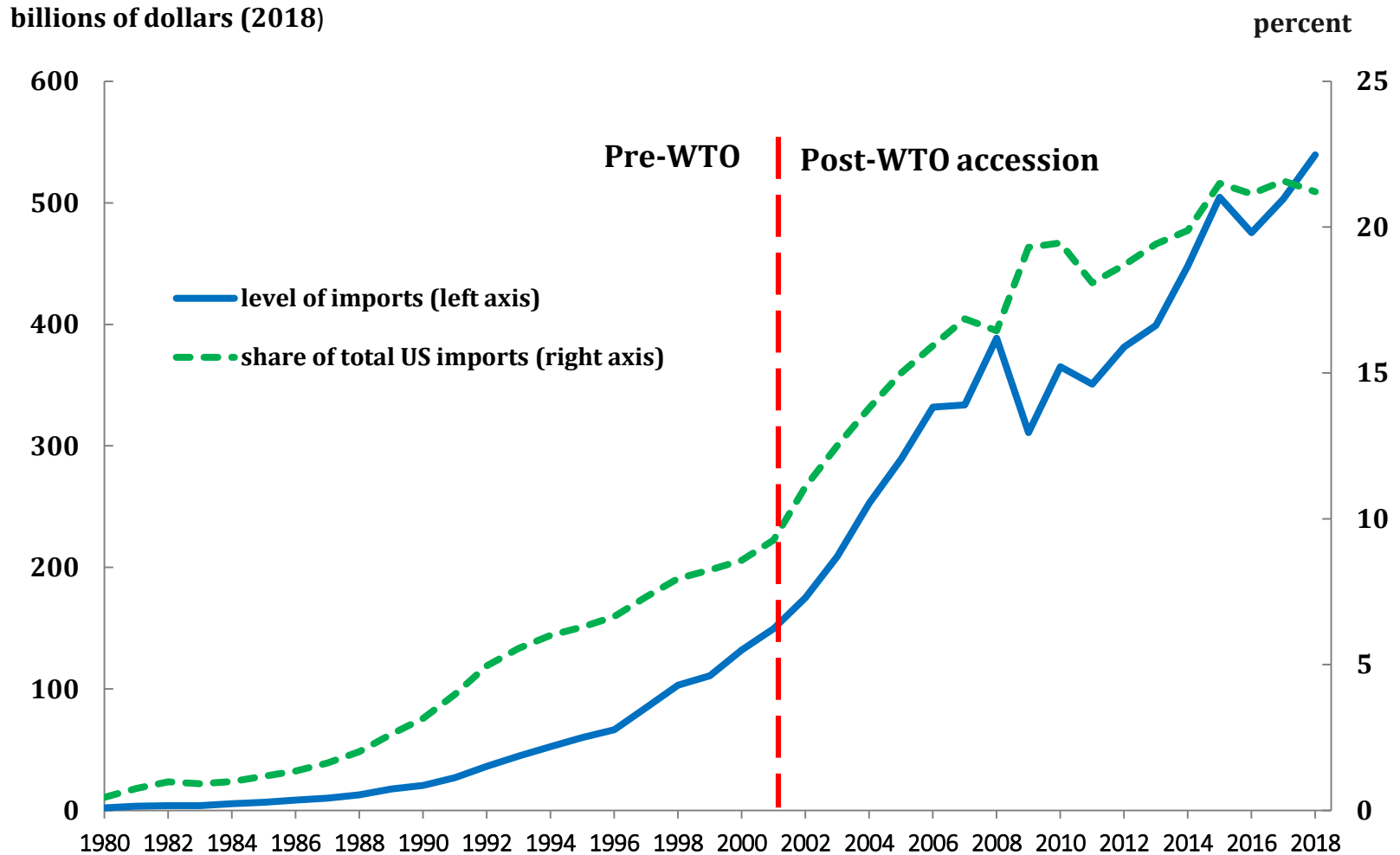


Source: Bown and Zhang (May, 2019)

Impact of “China shock” on US political economy

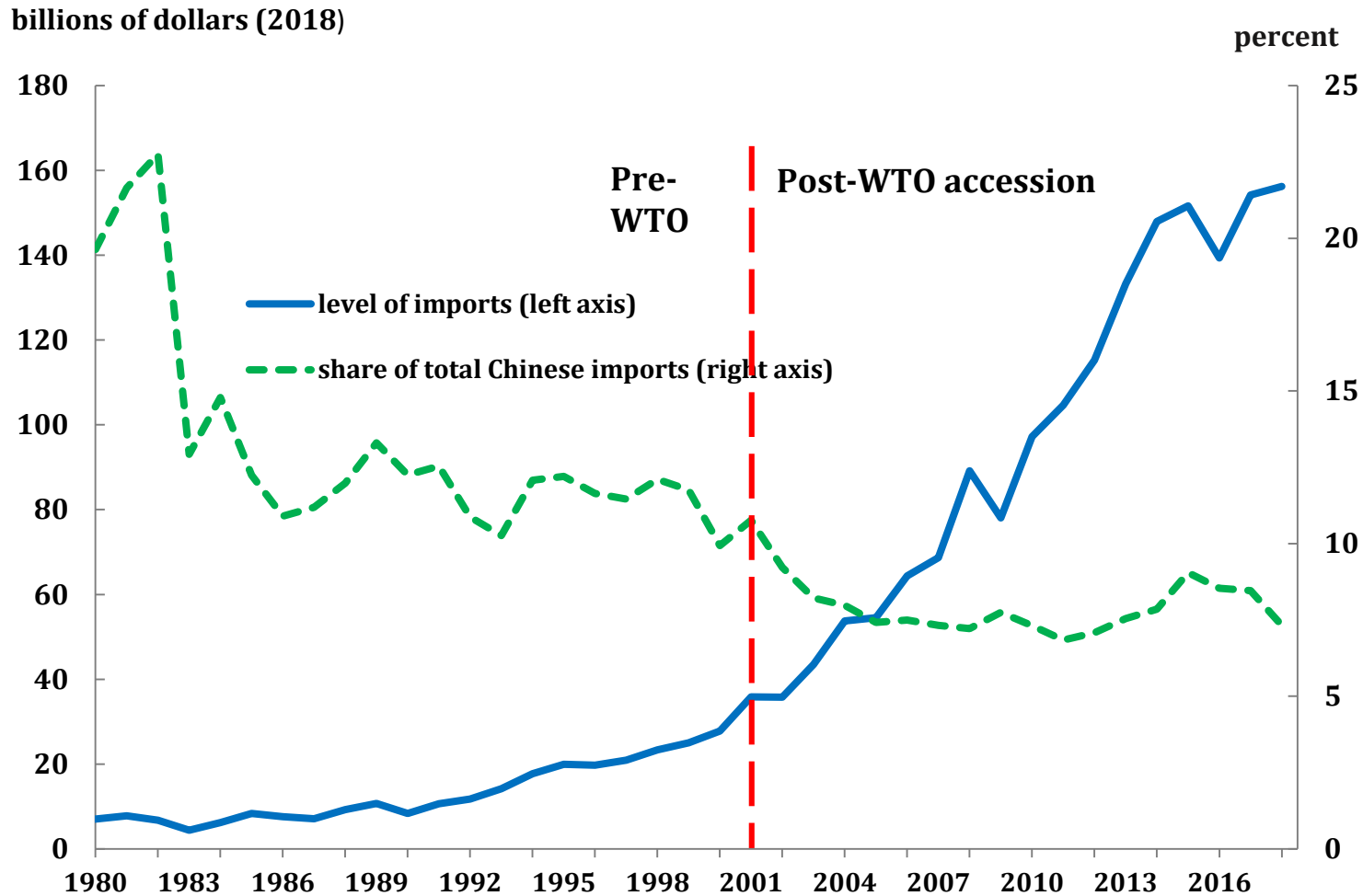
- Post-2000–increase in US imports from China not offset by increase in US exports (Autor *et al.*, 2016)
- Effect of China import shock well-documented, Autor *et al.* (2013), and Pierce and Schott (2016)
- Trade exposure contributed to growth of *populism* (Grossman and Helpman, 2018) and polarization in US politics (Autor *et al.*, 2017)
- Populism reflected in *anti-elitism* (Eichengreen, 2018) and shift to *economic nationalism* (Colantone and Stanig, 2018) – i.e., opposition to free trade
- China targeted over its trade policies, e.g., level of tariffs, exchange rate policy, and trade surplus

US imports from China



Source: Bown (April, 2019)

China's imports from US



Source: Bown (April, 2019)

Chinese market distortion and WTO

- **US concerns about China's trade practices well-documented (USTR, 2018; Morrison, 2018):**
 - **Forced technology transfer**
 - **Discriminatory licensing restrictions**
 - **Theft of intellectual property**
 - **Investment restrictions**
 - **Subsidies to state-owned enterprises (SOEs)**
- **WTO case could be built against China that one or more Chinese government measures “nullify or impair” benefits of US and other WTO members (GATT Article XXIII:1(a))**

“China, Inc.”

- **China’s economy structured in ways not anticipated by WTO negotiators (Wu, 2016):**
 - **Party controls “commanding heights” of economy**
 - **Party controls and directs largest banks**
 - **Party coordinates government agencies and firms**
 - **Party-set performance metrics of SOEs, banks etc.**
 - **Informal linkages between Party and private firms**
- **Party controls economy while still taking advantage of benefits of market mechanism, i.e., control is not via state**

“China, Inc.”

- **WTO case could also be made against China under “non-violation nullification or impairment” (NVNI) clause of GATT (Article XXIII:1(b)) (Hillman, 2018)**
- **Argued only way to approach this is through “grand coalition” of countries (Hillman, 2018; Lawrence, 2018)**
- **Problem with US unilateral approach:**
 - **“Shallow” deal (Hillman, 2018)**
 - **“Free-riding” (Bown, 2018)**
 - **Potential to undermine WTO (Mattoo and Staiger, 2019)**

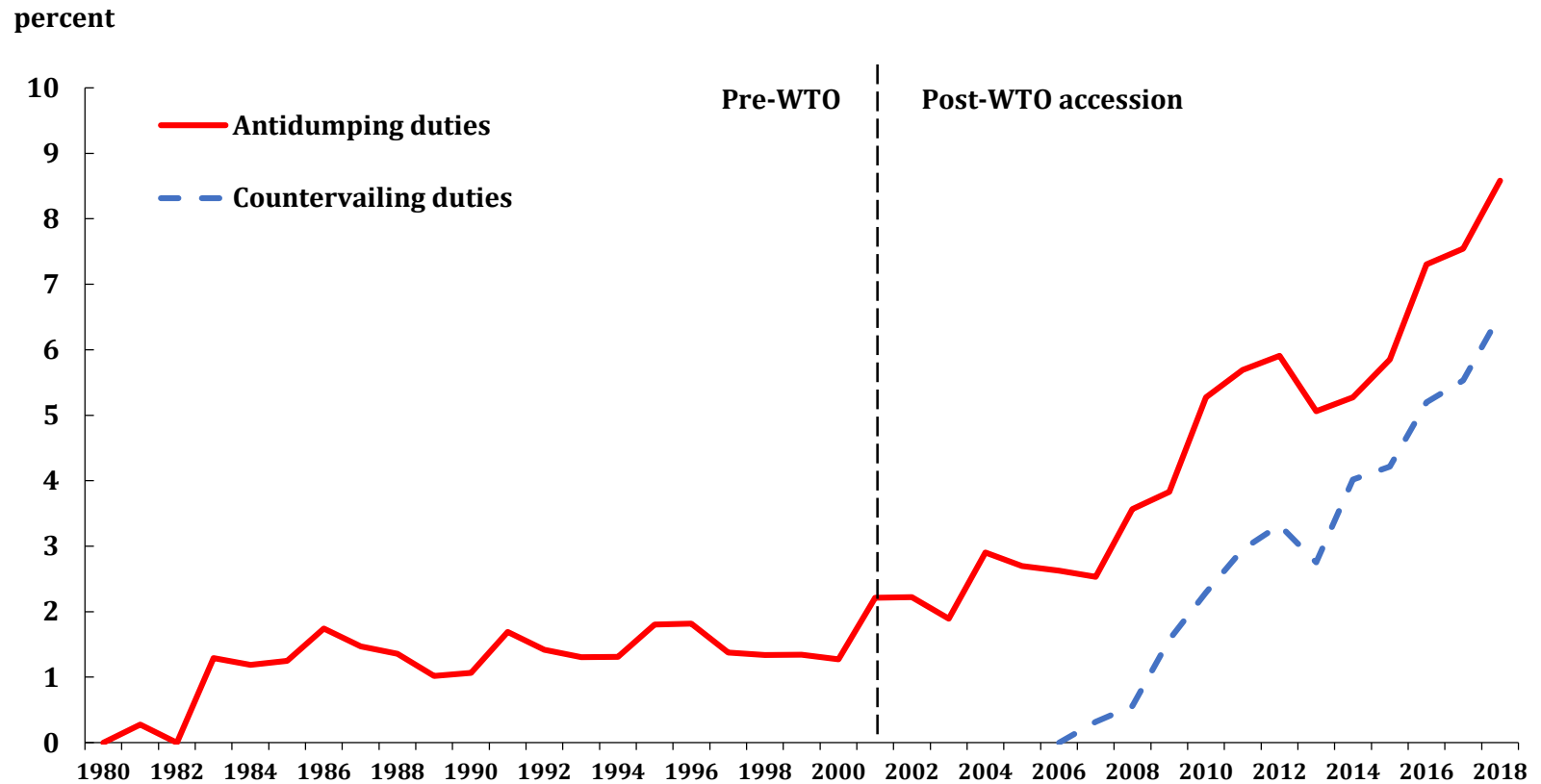
Provoking a trade war

- **Conventional wisdom - US has deliberately poked holes in weakest spots of WTO (Bown, 2019):**
 - **Imposed tariffs on steel and aluminum in 2018 on grounds of national security – US argued these would be “non-justiciable”, i.e., cannot be questioned as with anti-dumping duties**
 - **US unilaterally implemented tariffs on \$250 billion of Chinese imports after internal investigation by USTR (2018) – based on Section 301 of US Trade Act**
 - **US chose to block judicial appointments to WTO Appellate Body (AB)**

Trade war and WTO dispute settlement

- **US imposed national security tariffs in part because of Chinese economic model (Bown, 2019):**
 - **Chinese trade practices had to be countered**
 - **Anti-dumping duties had not worked**
 - **Safeguard tariffs would have been stopped by WTO**
 - **US would not win case at WTO due to “China, Inc.”**
- **Counter-argument – US gave up on formal dispute settlement too soon, i.e., specifically, it should have appealed to NVNI clause**
- **Requires AB to deal with complex interactions in non-market economy**

US anti-dumping duties and China



Source: Bown (April, 2019)

Failure of WTO dispute settlement

- Concerns over “judicial over-reach” in AB, and emergence of principle of *stare decisis* in WTO case law (Payosova *et al.*, 2018)
- Dispute settlement will break down by end of 2019, i.e., any member will be able to block panel rulings
- Members should agree on procedures for AB to submit uncertain legal issues arising on appeal to respective WTO committees – *legislative remand*
- Emphasizes need for permanent negotiations in WTO
- Also requires US to stop “...kicking at the working leg of a limping institution...” (The Economist, December 7, 2017)

Costs of trade war

- Initial economic effects (Fajgelbaum *et al.*, 2019):
 - Loss from higher prices - -\$68.8 billion
 - Terms of trade gains - +\$23.0 billion
 - Tariff revenue - +\$39.4 billion
 - Aggregate loss to US - -\$6.4 billion
- Potential to undermine WTO – reputation, and norms of cooperation matter in a rules-based system (Mattoo and Staiger, 2019)
- Even if multilateral trading system is maintained, return to GATT-type system would allow countries with bargaining power to veto disputes (Bown, 2019)

Tariffs are a small source of revenue

US tariff revenue as percent of total government revenue, 1795–May 2019



Source: Bown and Irwin (July 16, 2019)

Conclusions

- Trade war already imposing costs on US, which will increase as height/breadth of tariffs increases
- Potential to increase downside risk to global economy (IMF, July 23, 2019)
- US-China trade deal likely to be “shallow”, targeted at trade deficit with little focus “behind the border”
- A coalition of WTO members would likely be more appropriate way to deal with “China Inc.”
- Failure of US to follow rules-based trading system runs risk China will not follow system if (when) it becomes dominant economic power

Citations

1. Autor, D.H., D. Dorn, and G.H. Hanson. (2013). “The China Syndrome: Local Labor Market Effects of Import Competition in the United States”, *American Economic Review* 103(6): 2121-2168.
2. Autor, D.H., D. Dorn, and G.H. Hanson (2016). “The China Shock: Learning from Labor Market Adjustment to Large Changes in Trade”, *Annual Review of Economics*.
3. Autor, D.H., D. Dorn, G.H. Hanson, and K. Majlesi. (2017). “Importing Political Polarization? The Electoral Consequences of Rising Trade Exposure”, NBER Working Paper 22637.
4. Bown, C.P. (December 11, 2018). “Why the U.S. needs Allies in a Trade War Against China”, *Harvard Business Review*, <https://hbr.org/2018/12/why-the-u-s-needs-allies-in-a-trade-war-against-china>
5. Bown, C.P. (2019). “The 2018 trade war and the end of dispute settlement as we knew it”, in M.A. Crowley (ed.), *Trade War: The Clash of Economic Systems Endangering Global Prosperity*, Vox.EU Book, CEPR Press.
6. Bown, C.P. (April 2019). “The 2018 US-China Trade Conflict After 40 Years of Special Protection”, Working paper 19-7, Peterson Institute for International Economics.
7. Bown, C.P., and E. Zhang (May 14, 2019). “Trump’s 2019 Protection Could Push China Back to Smoot-Hawley Tariff Levels”, *Trade and Investment Policy Watch*, Peterson Institute for International Economics.
8. Bown, C.P., and D.A. Irwin (July 16, 2019). “Tariff revenue and Trump tweets – 5 things you need to know”, *The Washington Post*, <https://www.washingtonpost.com/politics/2019/07/16/tariff-revenue-trump-tweets-things-you-need-know/>

Citations contd.

9. Bown, C.P. and E. Zhang (August 6, 2019). “Trump’s Latest Trade War Escalation Will Push Average Tariffs on China Above 20 Percent”, Peterson Institute for International Economics.
10. Colantone, I., and P. Stanig. (2018). “The Trade Origins of Economic Nationalism: Import Competition and Voting Behavior in Western Europe”, *American Journal of Political Science* 62(4): 936-953.
11. The Economist (December 7, 2017). “As WTO members meet in Argentina, the organization is in trouble”.
12. Eichengreen, B. (2018). *The Populist Temptation: Economic Grievance and Political Reaction in the Modern Era*, Oxford University Press.
13. Fajgelbaum, P.D., P.K. Goldberg, P.J. Kennedy, and A.K. Khandelwal. (March 3, 2019). “The Return to Protectionism”, NBER Working Paper No. 25638.
14. Hillman, J. (June 8, 2018). *Testimony Before the U.S.-China Economic and Review Security Commission*, Washington DC.
15. Grossman, G.M., and E. Helpman. (2018). “Identity Politics and Trade Policy”, NBER Working Paper 25348.
16. IMF. (July 23, 2019). “Still Sluggish Global Growth”, World Economic Outlook Update.
17. Lawrence, R.Z. (August 2018). “How the United States Should Confront China Without Threatening the Global Trading System”, *Policy Brief*, Peterson Institute for International Economics.

Citations contd.

18. Mattoo, A., and R.W. Staiger. "Understanding trade wars", in Meredith A. Crowley (ed.), *Trade War: The Clash of Economic Systems Endangering Global Prosperity*, VoxEU Book, CEPR Press.
19. Morrison, W.M. (2018). "China-U.S. Trade Issues", Congressional Research Service, 7-7500.
20. Payosova, T, G.C. Hufbauer, and J.J. Schott. (March 2018). "The Dispute Settlement Crisis in the World Trade Organization", *Policy Brief*, Peterson Institute for International Economics.
21. Pierce, J.R., and P.K. Schott. (2016). "The Surprisingly Swift Decline of U.S. Manufacturing Employment", *American Economic Review* 106(7): 1632-1662.
22. US Trade Representative's Office (USTR). (March 22, 2018). "Findings of the Investigation Into China's Acts, Policies, and Practices Related to Technology Transfer, Intellectual Property, And Innovation Under Section 301 of the Trade Act of 1974",
<https://ustr.gov/sites/default/files/Section%20301%20FINAL.PDF>
23. Wu, M. (2016). "The 'China, Inc.' Challenge to Global Trade Governance", *Harvard International Law Journal*, 57(2): 261-324.