Global Counsel

The Trump trade gamble

Blog post by Senior Associate Guillaume Ferlet, 23 March 2018

For all of Donald Trump's flexibility on policy issues, US-China trade is one area where he has demonstrated surprisingly constant views over the years. Unlike the Washington political establishment, Trump and his group of trade advisers not only believe that the integration of the American and Chinese markets since China's 2001 entry into the WTO has not benefited both countries equally (not an unusual view in Washington), but that the US has not been assertive enough in rebalancing the relationship. The White House's announcement yesterday of a raft of economic and investment sanctions against China as a response to the country's "economic aggression", is Trump's attempt at doing this.

The Trump administration is now looking at applying a 25% tariff on $50bn in Chinese imports, introducing new restrictions on Chinese investments in the US to limit China's ability to buy US technologies and high-tech firms, and filing a case at the WTO against China's alleged discriminatory licensing practices for foreign companies. The objective is to force Beijing to abandon its allegedly restrictive trade and intellectual property policies. The Trump team invoke a failure of reciprocity that is also familiar from the EU's own political debate about China.

The big question is what happens next? With China already pledging to safeguard its interests, some countermeasures seem likely. However, beyond the question of the highly debatable WTO legality of this round of tit-for-tat, there is reason to think a trade war might not last – but also reasons to be unsure.

With 7 months to go until the November 2018 US midterm elections, there is plenty of time for the economic cost of Chinese retaliation to be felt in the US. Beijing's reprisal will be calibrated to specifically hit exports from those US states that contributed to elect Donald Trump in 2016 — principally the Farm Belt states and their agricultural exports to China — in order to impact the Republican party's electoral prospects. The Bush administration backed down quickly on its own steel tariffs in 2003 in the face of the threat of politically targeted EU countermeasures, once his administration had the political cover of a lost WTO case. The Trump administration may see the WTO differently, and Trump is personally unpredictable in a way Bush was not - but political pain is political pain.

To the extent that it matters, the policy will also probably not work. It is unlikely China will make the sort of wide-ranging policy practices the US seems to be asking for under duress. The Trump administration argues (rightly) that Beijing uses restrictive policies at home against US companies, combined with subsidisation of Chinese private businesses and state-owned enterprises competing abroad. This is a deliberate and systemic industrial policy. With China's goods exports to the US standing at $506bn in 2017 (and accounting for 2.5% of China's GDP that year), the US is preparing to hit roughly 10% of that. Will the Chinese leadership really consider abandoning established trade and investment practices for such an amount?

A more rational strategy would have been to build a coalition with the EU and others increasingly willing to take a tough line with China and to think what the exit strategy from a tit-for-tat tariff war might be. But events have moved past that. It would be easier to predict where this is heading if Trump was a more predictable actor.