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Research Report

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SWP Comment

NO.36 SEPTEMBER 2018

On US Government Trade Policy

Trump's 'America First' Policy Puts Pressure on the EU

Laura von Daniels

Given the US tariffs on steel and aluminium and further tariff threats, the transatlantic trade relationship remains tense. While EU Commission President Jean-Claude Juncker and US President Donald Trump agreed at their meeting on 26 July to start negotiations to reduce tariffs in several industrial sectors over a period of 120 days, it remains uncertain they can reach a compromise that allows both sides to save face. At the same time, Europe is struggling with an important, but as yet, unanswered question: Is the US government's trade policy the result of a strategy designed to weaken geopolitical rivals like China, even if it adversely affects close partners such as the EU? Or does Trump really want to break away from the liberal multilateral order? The EU needs to prepare for both possibilities. Support could come increasingly from US companies.

Since the start of the year, the US government has been taking unilateral action hurting its trading partners. But the measures are not surprising. In his trading strategy from March 2017, President Trump announced the US was ready to push through its interests with little regard for international trade rules. Washington's actions against different trade partners including the EU, Japan and China have triggered a spiral of escalation. Soon, US protectionist tariffs and retaliatory measures by several of its trading partners could affect trade flows worth more than 850 billion euros (see Figure 1, p. 2).

US trade measures and goals

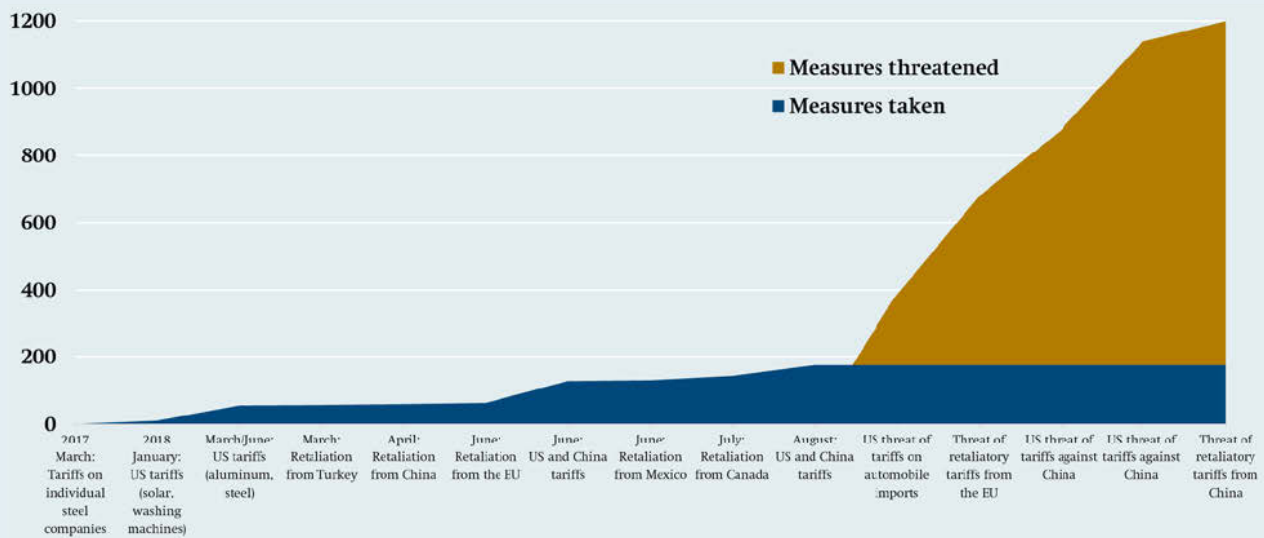
The US president is often said to have an erratic political style. However, with the trade policy measures implemented to date, he is pursuing clear objectives, some of which are domestic policy and others foreign policy.

Firstly, on 22 January 2018, the US introduced 20 to 50 percent protective tariffs and import quotas on washing machines and solar panels. US Secretary of Commerce, Wilbur Ross, said the tariffs, which impact trade worth around ten billion US dollars, were necessary to protect domestic industries against cheaper imports. In line



Figure 1

**Total trade volume affected by the global trade conflict since March 2017
(in billions of US dollars)**



Source: Own diagram, based on data from the Peterson Institute for International Economics (2018), *New York Times* (13 July 2018), *Frankfurter Allgemeine Zeitung* (11 July 2018).

with national legislation (Section 201 of the US Trade Act of 1974), Trump was able to impose the tariffs without the consent of Congress. As a result, this was the first time the president had been able to push through his policy despite criticism from Republicans, who traditionally advocate free trade.

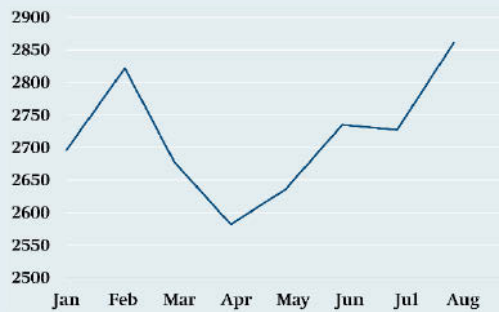
The second, even more serious, customs decision followed shortly thereafter. On 8 March, the US government imposed tariffs of 25 percent on steel imports and ten percent on aluminium imports. Once again, Trump resorted to national legislation (Section 232 of the 1962 Trade Expansion Act) in order to wave through the tariffs without consulting Congress. The US government justified the metal tariffs on the grounds that cheap imports to the domestic economy were an increasing “threat to national security”. Although this argument seems weak, it is impossible to say for sure whether the US has broken international trade law until a ruling has been made on the WTO case. At the same time, Washington’s actions have left its partners with few options, other than imposing their own tariffs to signal their resolve to protect EU interests.

By initially granting customs exemptions to individual partners and offering bilateral negotiations, the US government has also succeeded in driving a wedge between the injured parties. Recent negotiations on the North American Free Trade Agreement (NAFTA) provide a similar example of Trump’s divide and rule approach. Initially, Mexico and Canada both rejected the US imposed conditions for exemption from the metal tariffs and refused to make far-reaching concessions on NAFTA. But after the US and Mexico announced on 27 August that they have reached a bilateral trade agreement, Canada is under pressure to equally accept US conditions. Giving up the trade deal would create immense economic costs. Also, domestic political costs for the government could rise quickly, a bit more than a year before federal elections.

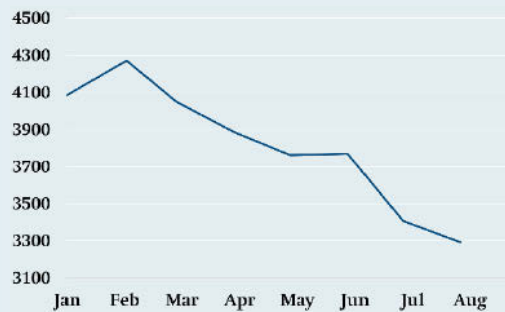
Trump could also succeed in forcing the EU to agree to either self-imposed export restrictions that he hopes would reduce the US trade deficit or to a major reduction of tariffs and entry barriers on US exports. There is no political consensus in the EU on whether to oppose the US or make concessions. Earlier this year, European Commis-

Figure 2

S&P 500 (USA), January–August 2018



CSI 300 (China), January–August 2018



Source: <http://www.bloomberg.com>.

sion President, Jean-Claude Juncker, stated that the EU refuses to negotiate a trade deal for as long as the US applies tariffs on EU metal exports. This position was pushed particularly by France. But on the other hand, Germany and other countries that count the US among their primary export destinations have any interest to prevent additional US tariffs, in particular on automobiles.

The third radical US tariff decision is directed at China, but also affects EU interests. Since 6 July, the US government has imposed tariffs of 25 percent on Chinese imports, initially affecting goods worth around 34 billion US dollars. On 23 August, a second tranche of tariffs of 25 percent on Chinese goods worth 16 billion US dollars was implemented. In prior statements, Trump also threatened to extend a 25-percent tariff on Chinese imports worth an additional 200 billion US dollars, after Beijing reacted with tariffs, particularly hurting US agricultural producers exporting soybeans to China. The US Department of Commerce justified the tariffs due to what it called “unfair trading practices” and more specifically, the systematic theft of intellectual property, Chinese-imposed technology transfer and other government measures that impede market access for US companies. In this case, too, the president may act without consulting Congress in line with Section 301 of the 1974 Trade Act. Trump is apparently willing to impose tariffs on goods worth more than 500 billion US dol-

lars, which corresponds to China’s total exports to the US last year. It is true that China, like the EU, is one economic area that could make up the trade losses relatively easily with internal demand. Nevertheless, uncertainty in the financial markets driven by the trade dispute has already been detrimental to Chinese companies (see Figure 2). Given China’s high and rapidly growing private debt further uncertainty might even trigger a financial crisis that could see China’s development held back considerably. However, Beijing has so far showed no signs of budging on US demands.

Possible next steps

Should the US President be unsatisfied with the results of negotiations with the EU over a tariff agreement he is likely to renew his threat of imposing tariffs on automobiles and parts. On 23 May, Secretary of Commerce Wilbur Ross was instructed by the president to consider initiating an investigation into tariffs of 20 to 25 percent on automobiles and automobile parts “to determine their effects on America’s national security”. These tariffs would affect not only the EU, but also Canada, Mexico, Japan, South Korea and China. Again, the US government argued there was a threat to national security (in line with Section 232 of the 1962 Trade Expansion Act). A threat to national security can hardly be used as justification for tariffs on automobile im-

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ports. And import tariffs on automobile parts could even negatively affect US automobile manufacturers. Presently, domestic products can only fully replace imports at considerable cost. Clearly, if the costs increase then jobs will be at risk. US economists estimate that a 25-percent tariff on automobiles alone would put nearly 200,000 US jobs at risk. And if trade partners impose counter-tariffs, job losses could be three times higher. For these reasons, car lobbyists including the Alliance of Automobile Manufacturers, representing General Motors and Ford, have warned the administration against tariffs. Following protests, the Commerce Department has announced that it needs additional time to finish a comprehensive report initially due in late August.

Finally, speculation about a US exit from the WTO has caused significant uncertainty. At the end of June, US newsletter Axios reported that the US government was working on a bill which was very close to fulfilling Trump's repeated desire for the US to withdraw from the WTO. Initially, several members of the government denied the report. A short time later, President Trump declared he was not seeking to withdraw from the WTO. In fact, he would not have had the authority to do so single-handedly. US legislation on the WTO provides for a congressional decision. Nevertheless, it is striking that Trump seems to be repeatedly trying to lend credence to his threat of withdrawal.

Where is US policy headed?

The US midterm elections will be held on 6 November. While Trump effortlessly "serves" his political base with bold tariffs, free-market advocates have it tougher. This applies to opponents of the tariffs from the ranks of the Republicans who, according to election analyses, can expect to lose votes if they deviate from Trump's positions. But it applies equally to Democrats. Trump's policy not only targets their goals, such as

increased control over foreign investors. Particularly for Democrats running for office in areas that mostly voted for Trump, it would be politically risky to oppose his 'America First' policy. As a result, legislative initiatives such as that of Republican Senator Bob Corker have little chance of success: He wants to send the president's tariff decisions on matters of "national security" back to Congress, especially if they concern US allies. So far Corker even failed to get support from Republican leaders for a vote on his legislative proposal.

However, there is mounting opposition to Trump's trade policy from major US corporations and leading associations such as the American Chamber of Commerce, the Alliance of Automobile Manufacturers and the Internet Association, the umbrella organisation for the digital economy. Support is still lacking for the campaign against import tariffs launched in June by influential brothers Charles and David Koch who control multi-billion dollar Koch Industries. They are promoting political initiatives and candidates who are committed to opposing Trump's policies. Given that, at first glance, the US economy seems to be booming, US companies have had little reason to protest so far. Looking at average development of the share prices of the largest US companies listed on the S&P 500, it would appear that Donald Trump's economic policy has produced only winners. Major companies, in particular, have clearly benefitted from last year's tax reform. By contrast, Chinese share prices are plummeting (see Figure 2, p. 3). However, if one takes a closer look at the US stock market, a different picture emerges. Gains on the leading US market index S&P 500 in the first quarter of 2018 were largely due to above-average performances by the five major technology stocks, Facebook, Apple, Amazon, Netflix and Google. Most other US companies, however, are suffering from the trade conflict. Trump could soon encounter resistance from these corporations.

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