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Trump's tariffs, China's attitude spell trouble for world trade



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Illustration: Eric Lobbecke

For all his bellicose rhetoric, Donald Trump's trade policy is not a major departure from the traditional American stance. But with China mounting an aggressive response, the world trading system is under greater threat than it has been for decades.

Trump's claim is that American exporters are not being granted the level of access the US gives their foreign rivals. No claim has been a harder perennial in America's dealings with its trading partners; indeed, the insistent demand for reciprocity has shaped US trade policy from its earliest days.

As Douglas Irwin puts it in his magisterial history of American trade policy, while the founding fathers largely revered free trade, the fact the US, once it left the British Empire, faced many discriminatory barriers against its exports "indelibly marked American thinking about trade".

Responding to those barriers, Thomas Jefferson's report on commercial restrictions in 1793 set out the principle that the US would never countenance "unfair" foreign trade practices and would deploy all its resources to ensure they were dismantled.

That principle, repeatedly endorsed by subsequent administrations, acquired new force in the late 19th century when the European powers restricted American access to their expanding colonial possessions.

Removing these "imperial preferences" was a central objective of the Roosevelt administration's aptly named Reciprocal Tariff Act of 1934 which — after the proliferation of protectionist measures in the Depression — breathed new life into the international trading system, while making tariff reductions conditional on the US gaining reciprocal concessions.

The formation in the 1950s of what became the EU only cemented America's anxiety about reciprocal access. As the European countries and then Japan asserted themselves as competitors on world markets, American complaints about unfair trade practices became increasingly strident in the Johnson, Nixon and Carter administrations — and those administrations' recourse to retaliatory measures grew with them.

However, it was under Ronald Reagan that American concerns about reciprocal access reached fever pitch.

Reagan himself was an unequivocal advocate for free trade. But he was also deeply committed to building a "New Republican Party" that would "have room for the man and the woman in the factories". Understanding voters' fears at a time of rising unemployment, he vowed he "would not stand by and watch Americans lose their jobs because other nations do not play by the rules".

As a result, when a surging US dollar caused America's trade deficit to soar, Reagan did not hesitate to impose a broad range of restrictions, initially on imports from Japan and then — as imports from South Korea and Taiwan took their place — on other newly industrialising countries.

By 1984, those restrictions amounted to a 49 per cent tariff on the goods they covered.

There is little doubt that Reagan's trade policies contributed to his landslide victory in 1984, which swept him to re-election with 59 per cent of the popular vote. And it is equally certain that they prevented congress from imposing even more draconian trade restrictions.

However, as Arthur Dunkel, the then director-general of the General Agreement on Tarrifs and Trade, noted, their most enduring effect was in convincing America's trading partners to launch the Uruguay Round of global trade negotiations, whose outcomes Bill Clinton rightly hailed as "the largest, most comprehensive set of trade agreements in history".

In that way, Reagan's aggressive policies prepared the ground for far-reaching trade liberalisation, albeit at high cost.

But it would be rash to assume the Trump administration's assault on what it views as unfair trade policies will have the same impact.

After all, the primary target of the Reagan-era restrictions was Japan, a close ally that was entirely dependent on the US for its national security; the risk of the conflict escalating was therefore always slight.

Moreover, by then Japan was well on its way to catching up technologically, and perceived the market-opening measures to which it agreed as innocuous.

In contrast, China is an increasingly assertive global rival. Far from renouncing market-distorting interventions, it has vastly ramped up support for its "national champions" while subsidising a wide array of loss-making exporters. And with US producers tightly enmeshed in China's economy, it believes it can resist and rebuff American pressures, heightening the likelihood of escalation.

Adding to those risks, there is no prospect of a new multilateral round of trade negotiations, under GATT's successor the World Trade Organisation, that could defuse tensions as the Uruguay Round did. After a decade of paralysis, the last attempt at reaching multilateral agreement was put to rest in December 2015, marking the first time participants at this level had failed to conclude a trade negotiating round. The Europeans, who might have taken the lead in seeking to resuscitate the multilateral system, are too consumed by their internal woes; and even if they tried, they are unlikely to convince the US that such an effort would be worthwhile.

That doesn't mean the world will slide into protectionism: the disruption to global supply chains would be too great. But it does mean that we will see a move to forms of managed trade based on bilateral agreements between the US and its major trading partners.

For smaller trade-dependent economies, that isn't an outcome to celebrate: when the elephants dance, says the African proverb, the mice get trampled.

Yet it suits an era of diminished expectations, in which political elites can no more galvanise public support for trade liberalisation than they can secure the trust opening markets to international competition requires.

Electorates used to leave trade policy to governments, which pursued it with little regard to public opinion; that "permissive consensus" has vanished and won't return anytime soon. Little wonder, then, that financial markets are jittery. We should be, too.