



World trade and Trump

by Lorena Ruano

Upon taking office, President Donald Trump confirmed his intention to swiftly carry out some of his campaign promises on trade, which he blames for the loss of blue-collar jobs, as it allegedly exposes US workers to ‘unfair’ competition and lower standards from abroad. The first casualty was the Trans-Pacific Partnership (TPP), an agreement signed by Obama in 2015 after seven years of protracted negotiations with 11 partners that account for 44% of US exports. Still not ratified by Congress and criticised even by Hillary Clinton during the presidential campaign, TPP was a relatively easy target, so one of Trump’s first acts as President was to order the withdrawal of the US from it.

Immediately afterwards, driven by the hostility to Mexico that featured prominently during his campaign, came the announcement of Trump’s plans to re-negotiate (or scrap altogether) NAFTA (North American Free Trade Agreement), which he called the “worst trade deal ever”. He also threatened to impose a 20% tariff on imports coming from Mexico (the US’ third-largest trade partner) in order to curb the growing deficit the US runs with it – and make the Mexican people pay for the wall he intends to build along the border. Intense pressure was applied on specific companies, especially in the automobile sector, to dissuade them from investing in their southern neighbour. And while a trade war

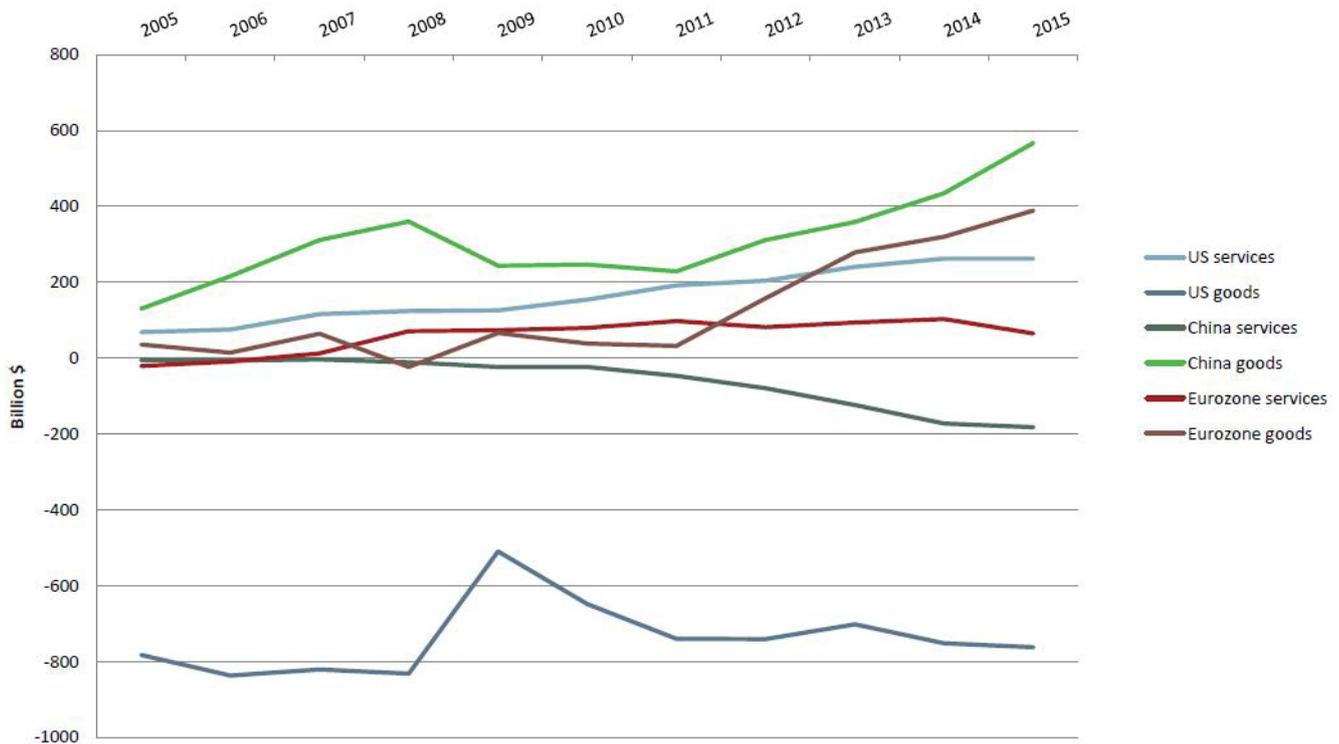
with Beijing has not yet materialised, Trump has been emphatic in his accusations of unfair competition, which he would counter with a proposed 35% tariff on goods manufactured in China – a measure that could have grave consequences for the world economy, as well as significant geopolitical repercussions.

Contested multilateralism

Next in the firing line was the World Trade Organisation (WTO), the 164 member-strong multilateral body that articulates global trade governance and which was painstakingly built under American leadership during the second half of the 20th century. On 1 March, the Office of the United States Trade Representative issued its Policy Agenda for 2017, stressing that the main objective in the coming years is ‘to expand trade in a way that is freer and *fairer* for all Americans’, while the means to achieve this will be by ‘focusing on *bilateral* negotiations rather than multilateral’ ones and using ‘*all possible sources of leverage* to encourage other countries to open their markets’. Moreover, the document sets the need to ‘defend US national sovereignty over trade policy’ as its number one priority, which means that decisions issued by WTO (or any other dispute resolution mechanism) will be disregarded if US goals are not met.



Main world trade players: net trade in goods and services, 2005-2015



Source: OECD data

Key among the new administration's grudges against the WTO is its possible classification of China as a market economy – a controversial decision that would constrain the potential use of anti-dumping measures. Such measures or threats are likely to proliferate in the coming months, not just against China, but against any other trade partner with which the US trade deficit is large or has been growing. It is true that the US has the largest trade deficit in the world, a fact that is viewed by the new administration as a major problem that needs to be corrected, at virtually any price.

In this context, it is also unlikely that negotiations with the EU over the Transatlantic Trade and Investment Partnership (TTIP) will produce any results. The talks had already been bogged down over several thorny issues such as agriculture, cultural products, and dispute resolution mechanisms, but had been kept alive because, together with the TPP, they were meant to advance the 'new trade agenda' in the face of stagnation at the WTO Doha round since 2003.

Both 'mega-regional' deals meant to go beyond tariffs and quotas (already low after several General Agreement on Tariffs and Trade (GATT) rounds – around 3.5% on average) to liberalise trade in services through *regulatory convergence*, i. e. equal legal treatment for foreign investors, intellectual property rights, environmental and labour rules. Trade in

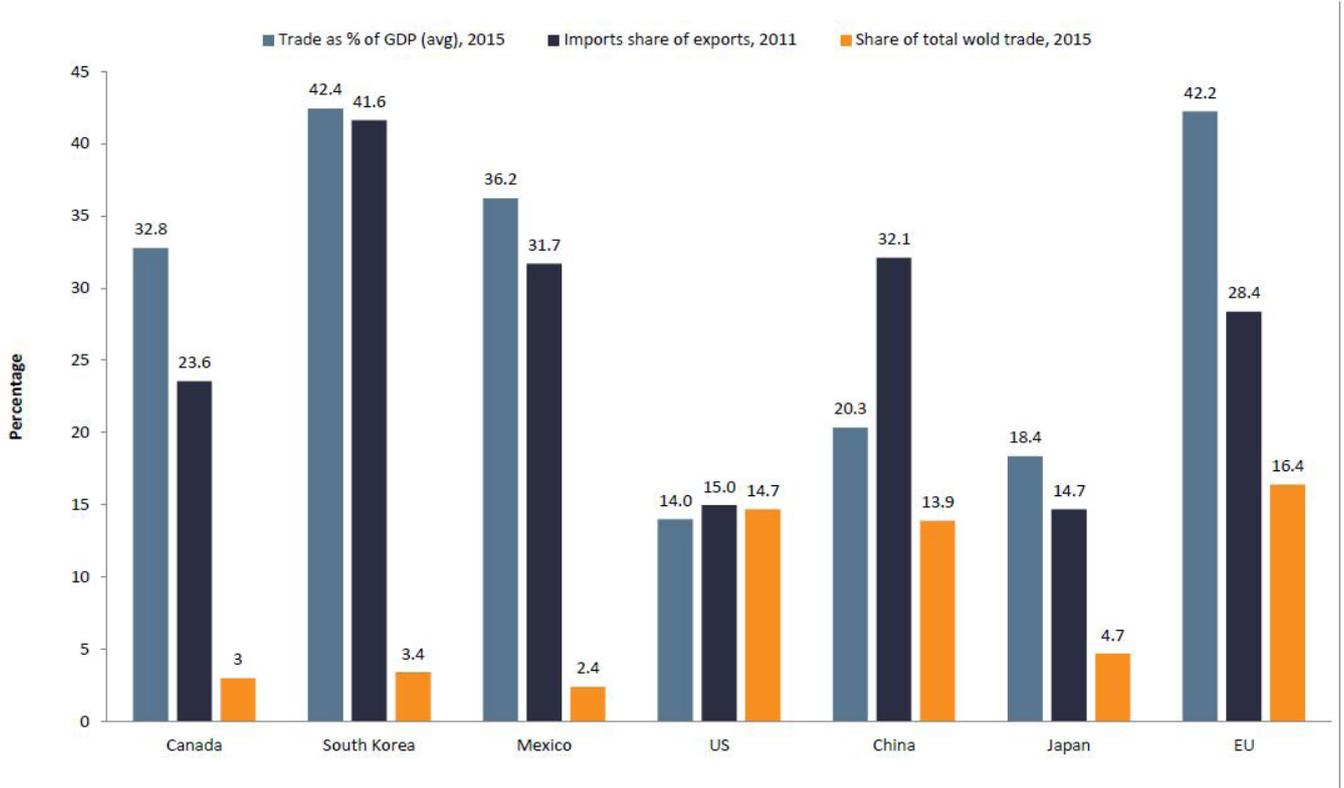
services had been growing much faster than that of goods in the developed world and had become an increasingly important element of GDP growth. It also produced surpluses for the US and Europe that somehow compensated the former's deficit in merchandise trade.

Supporters had hoped that this 'new trade agenda' would also help to create the regulatory 'level playing field' needed to alleviate job losses due to lower labour and environmental standards abroad. Whether that was to be case, or rather, as critics argued, such deals were just facilitating the movement of capital and operations offshore by multinationals, will now remain a theoretical debate. The new US administration seems to be going back to the 'old trade agenda' of tariffs, quotas, and anti-dumping measures, based on a neo-mercantilist view in which deficits are intrinsically bad, and deals should be struck bilaterally to extract better concessions from others, even if they violate global WTO rules.

This shift is problematic because a large proportion of merchandise trade today consists of semi-finished goods and takes place intra-firm and intra-industry, or within internationalised chains of production, such as the automobile industry in NAFTA. Imposing tariffs on Mexico or China will affect the competitiveness of US companies that import parts from these countries, which are then re-exported as finished goods. It would also hurt American



Main world trade players – selected variables



Source: OECD and WTO data

consumers, as they will have to pay higher prices for imported goods or for goods made out of imported parts. Moreover, a hike in tariffs and quotas is likely to trigger legal and policy responses from those affected. These could range from complaints at WTO panels – which the US will probably ignore – to a retaliatory rise in tariffs against goods coming from the US. In short, spark a trade war.

Although the US is better suited to deal with such a scenario since the share of trade in its GDP is much lower (14% on average) than for its partners (36% for Mexico, 20% for China), it will hurt its highly internationalised industries like the high-tech and automobile sectors. China and Mexico still seem to be waiting to see if Trump will really be able and/or willing to do what he says; they are counting on US companies and local authorities, whose welfare depends on trade with them, to moderate the federal government's actions. Interestingly, the debate seems to be spreading also *within* the new administration.

Uncertain bilateralism

Uncertainty is another characteristic of this new era. It is not clear yet what will happen to the free trade agreements (FTAs) that the US has with 19 other partners, since the new Trade Policy Agenda states openly that the US government is thinking about 'renegotiating and revising trade agreements

when our goals are not being met'. Such goals are, allegedly, to curb the deficit and to 'bring back' jobs from countries that are 'unfairly' snatching them away. Thus, it seems that small partners which recently signed FTAs with the US but do not run a large surplus – such as Colombia or Panama – are safe, at least as long as they do not fail to implement the labour clauses of their FTAs, like Guatemala.

South Korea, by contrast, runs a rapidly growing surplus, and is therefore mentioned in the 2017 Policy Agenda as a concern to the US. No action against South Korea has been announced so far, so Seoul has kept quiet, lest it suffer the protectionist wrath of its key military ally. Only Canada, facing large and imminent potential losses, has been quick to move. Prime Minister Justin Trudeau mounted a charm offensive in early February to ensure that, if NAFTA were to be abandoned by the US, his country would revert to the bilateral trade deal both countries signed in 1989.

Nor is there any clarity as to what other big players in world trade will do, either. The EU has shown that Brussels is still committed to ongoing free trade negotiations. The recently concluded agreement with Canada (CETA), was signed shortly before the US election and ratified by the European Parliament on 15 February, opening the way for its provisional implementation – national ratifications are still pending. In early February, the EU's Trade

Commissioner, Cecilia Malmström, announced that the EU will hasten the revision of the Global Agreement with Mexico – already underway for more than four years – as a gesture of solidarity with one of the EU's two Latin American Strategic Partners.

In theory, as the largest world trader, access to the EU's market remains one of the Union's most important sources of influence in the world. However, it remains to be seen whether in the face of sluggish growth and protectionist forces, similar to those that brought Trump to the White House, 'market power Europe' is able to push forward a vigorous and broad free trade agenda, beyond Mexico and South Korea. The latter are 'easy' cases, namely free trade believers that do not pose a threat to 'sensitive' sectors in Europe. Yet the bumpy ride of CETA's ratification shows that these are not easy times even for experienced and motivated trade negotiators.

A changing paradigm?

Will China, the other big player in world trade, become – as President Xi Jinping hinted in Davos – the new standard bearer of an open world economy? It might yet do so, if a trade war does not block it. Yet Beijing will not be paying as much attention to regulatory convergence or a 'level playing field' as Washington and Brussels. In spite of being export champions, the Chinese are used to a markedly lower degree of openness of their own market to foreigners, so their drive will inevitably be more modest than America's – and leave out services. Their proposed Regional Comprehensive Economic Partnership (RCEP) in Asia is not terribly ambitious, seeking a voluntary liberalisation amongst ASEAN members and three other countries of the South Pacific.

It is indeed foreseeable that more modest instruments than all-encompassing FTAs, aiming at regulatory convergence, will be needed to advance the trade agenda in the coming years. That will probably be the way forward for the countries that had negotiated TPP, which announced they will continue regardless of US withdrawal. However, they will have to overcome powerful opposition at home (e.g. by the agricultural sector in Japan) during the ratification process, especially given the absence of the most important incentive the treaty offered them: securing access to the US market.

The medium-term economic effects of all this are difficult to assess at the moment, as few concrete measures have been put in place. Still, signalling is important: the public announcements from the White House have brought much uncertainty.

WTO and FTAs were established precisely to offer predictability to economic actors, allowing them to plan in the middle and long term. If one of the main players in world trade announces that these rules are now to be disregarded, without offering clarity on what will replace them, it will undermine or even unravel transnational production chains.

Furthermore, trade is intimately linked with investment and finance, as well as currency rates, so uncertainty in trade rules will also affect investors' choices and exacerbate the volatility of already fragile financial markets. Mexico's investment grade could probably be downgraded in the next weeks, while investors have so far sought refuge in dollars, a move that paradoxically contributes to the hike in the US trade deficit.

Arguably, the political and security effects of this change in US trade policy could be even more serious than economic ones, since the world trade regime was built by the US as part of a broader foreign policy and security strategy. The multilateral regime of GATT/WTO was meant to spread and support economic liberalism in a Cold War context of confrontation with communism. TPP was part of a broader geo-political strategy of 'pivoting to Asia', as was the FTA with South Korea. TTIP, for its part, was a way to boost stagnant trade with Europe, but also to reinforce the transatlantic bond at a time when the latter was struggling on several fronts. And NAFTA was not just about making North America more competitive, it was also about making Mexico – which shares a 3,700 mile-long border with the US – more prosperous and thus less dangerous. It contributed to change Mexican elites' attitudes, turning a nationalist and often hostile country into the close cooperative partner it has been for the last two decades.

This formula has been reproduced with many political and military allies, not just to do business, but also to entrench political and economic liberalism, interdependence, and to empower friendly and like-minded elites. If these changes go ahead, both anti-Americanism and nationalism are likely to grow across the world. It is also likely that China and other powers will try and fill the void left by the declining presence of the US. Here lies a key challenge also for the EU.

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