Trump's Protectionism: Method to the Madness?

By Linda Lim

Synopsis

President Trump's surge towards US protectionism is threatening a global war and disrupting the international trading system. What is the real issue behind his seemingly reckless policies?

Commentary

WHAT ARE the motivations behind the current flurry of US trade policy actions — announced tariffs on imports of solar products, washing machines, steel and aluminium, and imminent actions expected against China for "intellectual property theft"? Motivations matter because they indicate what outcomes are desired and thus whether particular policies are likely to be sustained, enhanced or withdrawn.

The chorus of US objections to the Trump trade actions reflect the knowledge from repeated historical experience that trade protection hurts consumers and other industries more than it might benefit shareholders and employees of the protected industry, resulting in net national economic loss. Despite this empirical certainty, and the support of large majorities of the American public for trade and globalisation, every major candidate in recent US presidential elections has espoused some protectionist rhetoric on the campaign trail.

Anomaly in US Politics

Once elected, the president usually backs off from protection, though Republican George W. Bush imposed tariffs on steel from 2002-3, and Democrat Barack Obama on China-made tyres from 2009-12, despite their known pro-free-trade views. This anomaly is explained by the "winner-takes-all" nature of the US Electoral College system; the loser in the national popular vote tally (Bush in 2000, Trump in 2016) can

win if he captures the most votes in populous states which typically "swing" their support between the two major parties.

While northeast and west coastal states are reliably "Blue", voting Democratic in every presidential election, and southern and central states are reliably "Red", voting Republican, a handful of midwestern industrial states are "Purple", alternating between the two parties. This gives them an outsize importance in deciding presidential elections, so they receive a disproportionate amount of candidate and presidential attention.

Thus in 2016 Trump's electoral victory was decided by a mere 77,000 votes out of 136 million cast nationally, enabling him to win Pennsylvania and Wisconsin by 0.7% margins, and Michigan by 0.2%, in districts that had lost manufacturing jobs, mainly to China. He won by larger margins in Ohio and Indiana, where the steel industry is concentrated.

US 2016 Presidential Election and China

The 2016 election continued this pattern, with the added wrinkle that electoral districts most heavily impacted by Chinese import competition, a small minority of constituencies nationwide, voted most heavily for Trump. This reflects the "China trade shock" documented by economics professors David Autor, David Dorn and Gordon Hanson.

The authors showed that very large imports from China over a very short time caused 25% of the decline in US manufacturing employment from 1990-2007, and the associated fall in wages, rise in disability claims, and job loss in other sectors in heavily-impacted constituencies.

But today the US economy is booming, with widespread labour shortages including in manufacturing, so concern for jobs only partly explains the Trump administration's zeal for import protection. Rather, it is the president's own long-held and deeply-felt personal antipathy toward "unfair trade" that explains his actions, starting with his appointment of trade hawks with steel industry ties to key policy positions.

Peter Navarro, an economics professor given to sensationalist media punditry, obtained funding from steel company Nucor for a documentary film version of his 2011 book "Death By China", which was endorsed by pre-candidate Trump. Wilbur Ross, a private equity investor, made billions from the Bush steel tariffs when the company he formed from consolidating distressed US steel firms was sold to ArcelorMittal, the world's largest steel producer, on whose board he served until becoming Trump's Secretary of Commerce.

US Trade Representative Robert Lighthizer grew up in a depressed Ohio steel town and served as Ronald Reagan's Deputy Trade Representative, when he used the threat of tariffs to persuade Japan and other countries to reduce their steel exports to the US. He then practised as a lawyer representing US Steel and other steel companies seeking government protection from unfair foreign competition. Both Ross and Lighthizer have hired former steel-industry lobbyists in their agencies.

What binds Navarro, Ross, Lighthizer and Trump is their shared (erroneous) belief that trade deficits are caused by other countries' unfair trade practices (rather than by domestic savings and fiscal imbalances), which they assert have been tolerated, enabled or perpetuated by "bad trade agreements" such as NAFTA and the WTO.

Protectionism for National Security?

But the WTO exists in part to restrain unfair trade practices, with the US a major beneficiary in its many successful petitions under the WTO's dispute resolution process. The WTO allows both temporary "safeguards" against import surges, and anti-dumping and countervailing duties against predatory pricing and state subsidies, with steel and China being frequent targets by many countries around the world.

Eschewing these conventional measures, the Trump administration has instead resorted to "national security" as the justification for its steel and aluminium tariffs. This provision in both national and WTO trade rules has been little used because it is a "blunt instrument" of vague definition, and could apply to many industries, spurring copycat and retaliatory moves at home and abroad.

Invoking national security implies that the national interest is served by protection even if it inflicts net economic losses on the nation as a whole. The administration has already used this justification to block semiconductor company Broadcom's proposed acquisition of Qualcomm — an unprecedented move. It also underlies the expected sanctions forthcoming on China for alleged intellectual property theft and forced technology transfer.

In the case of steel and aluminium, the "national security" argument is a smokescreen for purely protectionist motivations. Defence industries' dependence on the imported metals is tiny, and the Defence Department opposes the tariffs, which undermine national security by hurting US allies – the largest source of imports – rather than its perceived strategic competitor, China.

The Real Issue: Existential Nationalism

So if jobs and national security are not the main motivation for these tariffs, what is? Trump sets great store by keeping his more extravagant electoral promises even if they do not make economic sense (like a Mexican border wall). That his supporters – disproportionately older, white, less-educated and lower-income – are more anti-trade than average would limit the electoral damage.

But electoral politics can be subverted by retaliation, as the European Union did by targeting punitive tariffs on exports from "Red" states in retaliation against the Bush steel tariffs, hastening their removal. In the current case, the EU has threatened retaliation against exports from Kentucky and Wisconsin (both states represented by Republican House leaders), while Trump-voting farm communities would suffer from retaliatory barriers against their export crops.

Harvard professor Martin Feldstein, a Republican who supports free trade, suggests that US trade negotiators are using the threat of tariffs on Chinese steel producers as

a way to persuade China's government to stop requiring foreign (non-steel) companies to transfer technology to Chinese parties in exchange for market access. In other words, steel is not the real issue here.

But the configuration of electoral politics and policymaker personalities outlined here suggest that it is. Many countries view steel as a strategic industry that deserves state protection and subsidy — hence the global excess capacity to which China is the largest but not only contributor. President Trump goes a step further in claiming: "If a country doesn't have steel, it doesn't have a country… This is more than just pure economics. This is about defence. This is about the country itself."

Such existential nationalism suggests that we may expect steel protectionism to endure, and to be followed by other protectionist actions, given four other enabling conditions. First, the currently strong, labour-short US economy, with rising wages and lower taxes, will mitigate the job losses and higher prices from protection. Second, strong growth and fiscal stimulus under tax reform will widen the trade deficit which to Trump and his aides signal that the US is "being taken advantage of" by the unfair trade practices of other countries, especially China.

Third, there is widespread government and business support in the US, EU and elsewhere for getting seriously tough on China for its longstanding unfair trade practices. Fourth and finally, those protectionist Midwest industrial states remain electorally strategic, and Trump is already working on his reelection campaign.

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