



Indian Council of World Affairs
Sapru House, Barakhamba Road
New Delhi

Special Report

on

Emerging Trends in Trade War: Causes and Consequences

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Abstract

Through an analysis of positions of major world economies – China, the European Union, Canada, and Mexico - on tariffs and patterns of their trade relations vis-à-vis the United States (US), the paper attempts to examine the causes and consequences of a looming trade war. Building on the notion of complex interdependence, the paper observes that trade is not a zero-sum game where one benefits at the cost of others. On the contrary, trade war will result in loss of all, albeit in varying degrees, depending on trade intensity and participation in global supply and value chains.

Introduction

With both the United States (US) and China imposing tariffs on each other's products on July 6, 2018, the first tranche of retaliatory measures became effective, heightening the fear of escalation of the ongoing trade war. While the US imposed 25 per cent duties on \$34 billion worth Chinese products, including machinery electronics and hi-tech equipments, China retaliated by imposing equivalent tariffs on US imports including soybeans, pork and electric vehicles.

A cursory glance at the trends leading to the trade retaliation indicates that US President Donald Trump, in keeping with his election campaign, underscored in his inaugural address that economic nationalism would be the key pillar of his trade policy. He remarked,

“From this moment on, it's going to be America First. Every decision on trade, on taxes, on immigration, on foreign affairs, will be made to benefit American workers and American families. We must protect our borders from the ravages of other countries making

our products, stealing our companies, and destroying our jobs. Protection will lead to great prosperity and strength.”

Accordingly, and within days of his assuming office, President Trump withdrew from the Trans-Pacific Partnership (TPP)² and announced the re-negotiation of North American Free Trade Agreement (NAFTA) or withdrawal, in case of failure to strike a better deal.³ Continuing with his policy, in May 2018, he announced the imposition of tariffs on steel and aluminium on countries including the European Union (EU), China, Canada and Mexico, triggering a trade war marked by retaliatory actions.

In light of these developments, the paper attempts to analyse the ongoing trade war with special focus on the US, China, the EU, Canada, and Mexico. In doing so, an analysis of the emerging trends in the trade war among these countries has been undertaken. Through an analysis of speeches and statements of the leaders of these countries, the paper attempts to understand the positions and patterns of trade retaliation. It further seeks to understand the consequences of trade war on each of these countries.

In the process, the paper is divided into three major parts: Part I maps the positions of countries on trade war. Part II explores the ‘Complex’ Matrix of ‘Interdependence’ in international trade by analysing the trade patterns among these economies. Part III provides a review of the analysis and underlines the way ahead.

Part I

Mapping the Positions of Countries on Trade War: The Chain Reaction

The initial US decision to reconsider trade dynamics commenced with the publication of United States Trade Representative (USTR) on China’s WTO Compliance on January 18, 2018. The report clearly stated that “the United States erred in supporting China’s entry into the WTO on terms that have proven to be ineffective in securing China’s embrace of an open, market-oriented trade regime”.⁴

Explicating on China’s Compliance to the World Trade Organisation (WTO), the report maintained that even after almost two decades of pledging to support the multilateral trading system of the WTO, “*the Chinese government pursues a wide array of continually evolving interventionist policies and practices aimed at limiting market access for imported goods and services and foreign manufacturers and service suppliers*” and continues “*to pursue industrial policies that promote, guide and support domestic industries while simultaneously and actively seeking to impede, disadvantage and harm their foreign counterparts*” including the use of a wide array of state intervention and support.⁵

Thereafter, on January 22, 2018, President Trump approved recommendations to impose safeguard tariffs on imported residential washing machines and solar cells and modules.⁶ This was the first step towards revamping trade relations with China. Gradually,

the initial step resulted in successive decisions to revisit trade relations involving other countries including the EU, Canada, Mexico, and other countries in due course of time.

Table 1 indicates that US positions on tariffs have resulted in retaliatory actions by other countries – China, the EU, Canada, Mexico, Russia and India – bringing the world to the brink of a trade war. Beginning with the imposition of tariffs on washing machines and solar photovoltaic by the US, especially targeting China, in January 2018, to the imposition of tariffs on steel and aluminium, the tariff war was limited in its reach. Thereafter, each decision by the US President Trump on imposition of tariffs over different sectors, including technology, was greeted by other countries' retaliatory actions. For instance, on March 23, 2018, China announced a list of products as a retaliatory action a day after the US move to impose tariffs on steel and aluminium. Accordingly, China raised its tariffs from 15% to 25% on various US products amounting to \$3 billion in 2017, including meat (pork & its products), fruits, steel pipes and others. It was only at the fag end of May that the tariff war intensified with other countries including the EU, Canada, Mexico, and India resorting to retaliatory tactics. Concurrently, the countries gradually lodged WTO complaints against such measures.

An analysis of the positions on trade war by the US, China, the EU, Canada, Mexico, Russia and India suggests that the 'America's First Policy' is the immediate reason triggering the tariff war. As has been mentioned, since the inaugural speech, President Trump has made it clear that his policies would be driven by the rationale of economic nationalism. He remarked: "*January 20th 2017, will be remembered as the day the people became the rulers of this nation again*" and "*From this moment on, it's going to be America First....Every decision on trade, on taxes, on immigration, on foreign affairs, will be made to benefit American workers and American families*".⁷ The ostensible reasons provided by the US administration for such moves are trade deficit and national security.

One of the important reasons for waging the tariff war is to reduce the 'unfair trade practices', which have resulted in trade deficit between the US and the rest of the countries, particularly China. It is noteworthy that despite a series of meetings, the US and China failed to resolve bilateral trade deficit concerns. In his Presidential Memorandum dated August 14, 2017, President Trump clearly stated,

*"China has implemented laws, policies, and practices and has taken actions related to intellectual property, innovation, and technology that may encourage or require the transfer of American technology and intellectual property to enterprises in China or that may otherwise negatively affect American economic interests. These laws, policies, practices, and actions may inhibit United States exports, deprive United States citizens of fair remuneration for their innovations, divert American jobs to workers in China, contribute to our trade deficit with China, and otherwise undermine American manufacturing, services, and innovation."*⁸

National security is another reason cited by the US administration for the imposition of tariffs. Providing justification for the imposition of tariffs on steel and aluminium, Commerce Secretary Wilbur Ross on March 9, 2018, maintained, "*The president*

acted because steel and aluminium imports have helped erode the domestic industry to the point that it threatens national security". He further went on to say that unfair practices adopted by countries have eroded America's steel and aluminium industries, increased unemployment, and threaten national security. In order to redress this situation, imposition of tariffs, particularly on steel and aluminium becomes important.⁹

Table 1: Positions of Different Countries on Trade War

United States	China	The European Union	India	NAFTA Members (Canada and Mexico)	Russia
<p>January 22, 2018 President Trump approves imposition of tariffs on imports of large residential washing machines and solar photovoltaic (PV) cells and modules.</p> <p>March 8, 2018: President Trump announced a proclamation imposing additional tariffs on steel (25 %) and aluminum (10%), under Section 232 of Trade Expansion Act, excluding Canada, Mexico and European union.¹⁰</p> <p>March 22, 2018: President Trump signed a Presidential Memorandum Targeting China's Economic</p>	<p>March 23, 2018: China announced a list of products as a retaliatory action against US action to impose tariffs on steel and aluminium by raising tariffs from 15% to 25% on various US products amounting to \$ 3 billion in 2017, including meat (pork & its products), fruits, steel pipes and others.²²</p> <p>April 3, 2018: The Customs Tariff Commission of the State Council decided to slap additional tariff of</p>	<p>European Union (EU) May 31, 2018 In response to the announcement of US imposition of tariffs on steel and aluminium, the EU said it will impose duties “on a number of imports from the United States,” referring to a 10-page list of targets for retaliation it published in March, which included bourbon and Harley-Davidson motorcycles.</p> <p>European leaders also vowed to proceed with a complaint to the World Trade Organisation.³¹</p> <p>June 6, 2018</p>	<p>May 23, 2018: India has requested WTO dispute consultations with the United States (US) regarding US duties on certain imported steel and aluminium products. The request was circulated to WTO members on May 23, 2018. India claims the US duties of 25% and 10% on imports of steel and aluminium products respectively are inconsistent with</p>	<p>Canada May 31, 2018 Canada slapped surtax on \$12.8 billion of American steel, aluminum, coffee, candy, pizza and quiche.³⁸</p> <p>June 6, 2018: Canada has requested WTO dispute consultations with the United States regarding US duties on certain imported steel and aluminium</p>	<p>Russia June 19, 2018: In response to US tariffs on steel and aluminium, Russia announced that it would impose import duties on US including road-building machinery.⁴²</p> <p>July 2, 2018: Russia requested WTO dispute consultations with the United States regarding US duties on certain imported</p>

Aggression under Section 301. It included 25% increase in tariffs on certain Chinese products, new restrictions on Chinese Investments in US technologies, and filing a WTO dispute settlement case against China over discriminatory IPR policies.¹¹

March 30, 2018:

USTR issued the *National Trade estimates Report on Foreign Trade Barriers* highlighting in particular concerns over Chinese technology transfer practices, industrial policies (as underlined in made in China 2025 Initiative), excess capacity, restrictive cyber security measures and others.¹²

April 3, 2018

On April 3, 2018, the USTR announced approximately \$50 billion in proposed tariffs on imports from

15% or 25% on 128 items of products imported from the US since April 2, 2018.²³.

April 4, 2018:

In response to the tariff imposition worth \$50 billion, China retaliated by announcing an additional 25% tariff on 106 items with a trade value of \$50 billion of US imports including soybeans, automobiles, chemicals and aircrafts.²⁴

April 5, 2018:

China files WTO complaint over the United States' tariff measures on Chinese goods in various sectors including machinery,

The European Union has requested WTO dispute consultations with the United States regarding US duties on certain imported steel and aluminium products, claiming that the US duties of 25% and 10% on imports of steel and aluminium products respectively are inconsistent with provisions of the WTO's General Agreement on Tariffs and Trade (GATT) 1994 and the Agreement on Safeguards.³²

June 15, 2018:

The European Union (EU) in retaliation imposed tariffs on €2.8bn (\$3.26 bn and £2.4bn) worth of US goods such as bourbon whiskey, motorcycles and orange juice on

provisions of the WTO's General Agreement on Tariffs and Trade (GATT) 1994 and of the Agreement on Safeguards.³⁶

June 20, 2018:

The Indian government on June 20, 2018 slapped higher duties on a number of items including apples, almonds, walnuts, diagnostic reagents and certain steel products.³⁷

products, claiming that the US duties of 25% and 10% on imports of steel and aluminium products respectively are inconsistent with provisions of the WTO's General Agreement on Tariffs and Trade (GATT) 1994 and the Agreement on Safeguards.³⁹

Mexico

May 31, 2018

The Mexican government said it would levy import taxes on U.S. exports of pork bellies,

steel and aluminium products. The request was circulated to WTO members on July 2, 2018.⁴³

July 6, 2018:

Russia imposed duties of 25 to 40 per cent on US products which have Russian substitutes. These include road construction equipment, oil and gas equipment, tools for metal processing and rock drilling, as well as fibre optics.⁴⁴

China including industries such as aerospace, information and communication technology, robotics, and machinery as an initial means to obtain the elimination of unfair policies and practices.¹³

April 5, 2018:

President Trump instructed the USTR to consider whether \$100 billion of additional tariffs are appropriate under section 301.¹⁴

May-17-18, 2018:

US administration begins a series of meetings with a delegation from the government of China. At the end of the consultations, China will significantly increase purchases of United States goods and services. This will help support growth and employment in the United

electronics, etc. originating in China.²⁵

April 9, 2018:

China initiates WTO dispute complaint against US tariffs on steel and aluminium products under Section 232. China claims the duties of 25% and 10% on imports of steel and aluminium products respectively are inconsistent with provisions of the WTO's General Agreement on Tariffs and Trade (GATT) 1994 and of the Agreement on Safeguards.²⁶

June 3, 2018:

On June 3, 2018, China said that President Donald

June 15, 2018.³³

June 29, 2018:

The European Union on June 29, 2018, submitted written comments to the US Department of Commerce in the framework of the ongoing Section 232 National Security Investigation of imports of automobiles, including cars, SUVs, vans, light trucks and automotive parts.³⁴

July 2, 2018:

The European Union warned the United States that imposing import tariffs on cars and car parts would harm its own automotive industry and likely lead to counter-measures by its trading partners on \$294 billion of U.S. exports.³⁵

apples, cranberries, grapes, certain cheeses and various types of steel.⁴⁰

7 June 2018

Mexico has requested WTO dispute consultations with the United States regarding US duties on certain imported steel and aluminium products.⁴¹

States.¹⁵

May 23, 2018:

In a statement, President Trump ordered probe initiating a Section 232 investigation into imports of automobiles, including trucks, and automotive parts to determine their effects on America's national security.¹⁶

May 31, 2018:

President Trump signs proclamations extending tariffs on steel and aluminium on Canada, Mexico and the European Union to be effective on June 1, 2018.¹⁷

June 15, 2018:

President Trump announced additional 25 percent tariff on \$50 billion of goods from China that contain industrially significant technologies.

Trump's plan to impose tariffs on \$50 billion of Chinese exports threatens to wipe out progress made in trade talks between Beijing and Washington.²⁷

June 15, 2018:

In response to US tariffs, China announced retaliatory tariffs on \$34 billion worth of US goods, including agriculture products to be effective on July 6, 2018.²⁸

July 6, 2018:

China immediately retaliates with tariffs on its \$34 billion list of goods issued, including soybeans, pork and electric vehicles.²⁹

This includes goods related to China's *Made in China 2025 Plan*.

June 27, 2018:

Trump to use U.S. security review panel to curb China tech investments.¹⁸

July 5, 2018:

Trump announced imposition of tariffs on \$500 billion worth of Chinese goods in case of retaliatory actions for imposing tariffs of \$34 billion.¹⁹

July 6, 2018:

US tariffs of 25 % on \$34 billion worth of Chinese goods launched, including water boilers, X-ray machine components, airplane tires and various other industrial part.²⁰

July 10, 2018:

US threatens to slap tariffs on extra \$200 billion of

July 11, 2018:

China vowed to retaliate as US threatens tariffs on further \$200bn of goods.³⁰

Chinese imports, including hundreds of food products as well as tobacco, chemicals, coal, steel and aluminium and other consumer goods such as consumer goods ranging from car tires, furniture, wood products, handbags and suitcases, to dog and cat food, baseball gloves, carpets, doors, bicycles, skis, golf bags, toilet paper and beauty products..²¹

Source: Compiled by the author from different sources.

Part II

Trade: A 'Complex' Matrix of 'Interdependence'

Complex Interdependence implies that trading states will not fight each other as trade relationships are based on the notion of comparative advantage. As per this assumption, products are produced based on specialisation of a country, creating in that process an intertwined global supply and value chains. This has made the notion of trade even more complex in contemporary times. Apple products illustrate the deep rooted nature of global supply and value chains and the increasing failure to reflect the actual benefits accrued from trade. According to a 2010 study by the Asian Development Bank (ADB), China exported 11.3 million iPhones to the US at a shipping price of \$179 per unit with a total export value of \$2 billion. However, 94.4 per cent of the value added was attributed to foreign suppliers and producers of components and parts, including the US (\$122 million).⁴⁵

Similarly, one-quarter of US imports from Canada consist of value added from the US itself, and a huge 40 per cent of US final good imports from Mexico consist of its own value added. Together, these two NAFTA partners account for three quarters of all US value added returned from abroad. Over 96 per cent of the returned US value from Canada and Mexico was exported directly to these countries.⁴⁶ According to OECD estimates the foreign content of US exports was 15.3 per cent in 2014 while domestic value added to gross exports of US stood at 84.7 per cent.⁴⁷ This reflects that the countries are very tightly integrated into global production networks.

Understood in this sense, international trade is not a zero-sum game wherein one country benefits at the expense of others. Implicit, trade war will result in loss to all countries, albeit in varying degrees, depending on the level of trade intensity and integration into the global supply and value chains. Thus, a brief overview of trade relationship of the major economies would help ascertain the extent of impact of a potential trade war.

US -China Trade and Investment Relations

As a result of such tariff wars, US-China trade relations have come to be strained. In 2017, the total bilateral trade between the US and China (goods and services) stood at \$711 billion. The bilateral merchandise trade between the US and China has increased exponentially from \$4 billion in 1980 to \$636 billion in 2017, making China the largest trading partner of the US. However, along with the increase in trade, the trade deficit has also seen proportional increase, tilting in favour of China. From a trade surplus of \$2.7 billion in 1980, US trade with China has resulted in a trade deficit amounting to \$375 billion in 2017. Total US merchandise exports stood at \$130.4 billion in 2017. The major US goods exports to China include aerospace (civilian aircraft and parts); oils seeds and grains (mostly soybeans); motor vehicles; semi-conductors and electronic components; and waste and scrap. Out of the total US agricultural export to China, 63 per cent consisted of soybeans, making it the second-largest destination of US agricultural exports standing at \$19.6 billion in 2017.⁴⁸

In terms of imports, China was the largest source of US merchandise imports in 2017 accounting for \$505.6 billion. The major US imports from China include communications equipment; computer equipment; miscellaneous manufactured commodities (toys and games); apparel; and semi-conductors and other electronic components. China is also the fourth largest source of agricultural imports for the US accounting for \$4.5 billion.⁴⁹

According to the US Census Bureau, US imports of 'advanced technology products' (ATP) from China in 2017 was \$171.1 billion, constituting 36.9 per cent of total ATP imports and 33.8 per cent of total merchandise imports from China. Information and Communications products were the largest US import from China. US ATP exports to China stood at \$35.7 billion, resulting in a trade deficit of \$135.5 billion. This accounted for 27.4 per cent of total US exports to China and 10.1 per cent of global ATP exports.⁵⁰

In 2017, US had a surplus in trade in services with China accounting for \$40.2 billion. China was the fourth largest service partner of the US with total trade in services (exports and imports) at \$75 billion. US exports of services to China stood at \$57.6 billion and imports of services stood at \$17.4 billion.⁵¹

US stock of FDI flows in China stood at \$92.4 billion in 2016, a significant increase from \$0.4 billion in 1989, making it the 12th largest destination of US FDI.⁵² Similarly, China's FDI stock in the US stood at \$27.4 billion in 2016, which is a significant increase from \$0.087 billion in 1989.⁵³

US-NAFTA Trade and Investment Relations

In May 2018, a year since the re-negotiation process of NAFTA, President Trump announced the imposition of tariffs on steel and aluminium on Canada and Mexico. Noteworthy, the decision to renegotiate NAFTA in May 2017 by President Trump has already strained its relationship with Canada and Mexico.

In terms of trade relations, in 2017, US-Canada trade in goods (exports and imports) was \$581.5 billion, making it the second largest trading partner of the US. From \$100.4 billion in 1993, US exports in goods to Canada increased to \$282.2 billion in 2017. US imports in goods also increased from \$111.2 billion in 1993 to \$299.3 billion in 2017. Canada was the largest goods export market and third largest import market in 2017.⁵⁴ US had a trade deficit in goods amounting to \$17.1 billion. In 2017, US-Canada trade in services (exports and imports) was \$91.4 billion. Services exports were \$58.4 billion while services imports were \$33 billion. The US services trade surplus with Canada was \$25.4 billion in 2017.⁵⁵ US enjoyed a trade surplus of goods and services to the tune of \$8.3 billion.

The major US exports were vehicles (\$51 billion), machinery (\$42 billion), electrical machinery (\$25 billion), mineral fuels (\$19 billion), and plastics (\$13 billion). The major imports included mineral fuels (\$73 billion), vehicles (\$56 billion), machinery (\$21 billion), special other (returns) (\$14 billion), and plastics (\$11 billion). As far as agricultural products are concerned, Canada was the largest agricultural export market accounting for \$24 billion and second largest supplier of agricultural imports, accounting for \$22 billion in 2017.⁵⁶

US-Mexico trade in goods stood at \$557.5 billion in 2017, making it the third largest goods trading partner of the US. Exports totalled \$243.3 billion while imports were \$314.2 billion. Mexico was the second largest goods export and import market of the US in 2017.⁵⁷ In 2017, US-Mexico trade in services (exports and imports) was \$58.2 billion. While, on one hand, the US goods trade deficit with Mexico was \$70.9 billion in 2017, on the other, the US services trade surplus with Mexico was \$7.4 billion in 2017.⁵⁸

The major export products were machinery (\$43 billion), electrical machinery (\$41 billion), mineral fuels (\$26 billion), vehicles (\$21 billion), and plastics (\$17 billion). The main imports included vehicles (\$84 billion), electrical machinery (\$62 billion), machinery (\$54 billion), optical and medical instruments (\$14 billion), and mineral fuels (\$11 billion). Mexico was the third largest export market for US agricultural products, accounting for \$19 billion and the largest agricultural import market totalling \$25 billion in 2017.⁵⁹

As far as investment is concerned, the share of US FDI is the largest in both Canada and Mexico, but the share of FDI from NAFTA partners to the US is low, and much lower for Mexico. The US is the largest source of FDI in Canada with investment reaching \$363.9 billion in 2016, which is more than five-fold increase from a total stock \$69.9 billion in 1993.⁶⁰ For Canada, the US is one of the largest destinations of FDI in 2016 with a stock of \$371.4 billion, up from a stock of \$40.3 billion in 1993.⁶¹ The United States is the largest source of FDI in Mexico. The stock of US FDI increased from \$15.2 billion in 1993 to \$87.6 billion in 2016. Mexican FDI stock in the US stood at \$16.7 billion in 2016.⁶²

US - European Union (EU) Trade and Investment Relations

US-EU trade in goods (exports and imports) has seen an increase from \$304.7 billion in 1997 to \$717.8 billion in 2017. US exports stood at \$283.2 billion and imports stood at \$434.6 billion in 2017, with a trade deficit of \$151.4 billion.⁶³ Similarly, US-EU trade in services has seen an upward trend, an increase from \$163.8 billion in 1999 to \$435.3 billion in 2017. US exports were \$243.4 billion and imports were \$191.9 billion, with a trade surplus of \$51.4 billion.⁶⁴ US-EU also shares the largest investment relationship. US stock of FDI flows in the EU stood at \$2921.7 billion and EU's FDI into the US stood at \$2233.4 billion in 2016.⁶⁵

The major US exports to the EU in 2016 included aircraft (\$38.5 billion), machinery (\$29.4 billion), pharmaceutical products (\$26.4 billion), optic and medical instruments (\$25.6 billion), and electrical machinery (\$20.8 billion). The major imports included machinery (\$64.9 billion), pharmaceuticals products (\$55.2 billion), vehicles (\$54.6 billion), optic and medical equipment (\$27.5 billion), and electrical machinery (\$26.8 billion). The EU was the fourth largest agricultural export market totalling \$11.5 billion and third largest agricultural import market totalling \$20.6 billion for the US in 2016.⁶⁶

Trade War: Is it a Zero-sum Game?

An analysis of trade patterns of countries – China, the EU, Canada and Mexico – with the US suggests that bilateral trade has significantly increased over the years, integrating them into the larger global supply and value chains. Therefore, a trade war among these countries would adversely impact the individual countries as well as disrupt global supply chains.

According to an estimate by Peterson Institute for International Economics (PIIE), Trump's steel and aluminium tariffs would impose trade losses on partners equal to \$14.2 billion per year. Around \$7.5 billion loss would be incurred by traditional US military allies, including Canada, the EU, South Korea and Japan, defeating the stated argument of national security. The countries which would be hit the hardest are Canada (\$3.2 billion), the EU (\$2.6 billion), South Korea (\$1.1 billion) and Mexico (\$1.0 billion). China, the main target of Trump's tariffs, would only suffer \$689 million in estimated trade losses on account of the antidumping and countervailing duties imposed earlier which have curtailed US imports from China of those products.⁶⁷

Canada is the largest exporter of steel and aluminium to the US worth \$12 billion which is followed by the EU with exports worth \$7 billion. China exports only \$976 million worth of steel and \$1.8 billion worth of aluminium to the US, which constitutes only 6 per cent of total US imports of these two metals.⁶⁸ As far India is concerned, the US imports steel items worth approximately \$795 million and aluminium products worth \$424 million from India – lesser than China which would be impacted minimally.⁶⁹ While India will lose \$0.4 billion - \$0.3 billion in steel and \$0.1 billion in aluminium exports respectively - on account of the tariffs, China's loss will be \$0.7 billion. Russia's loss is estimated at \$0.8 billion.⁷⁰

However, the US also would not be immune to such adverse impacts. For instance, some estimates maintain that there are roughly 140,000 Americans who work in steel production and about 2 million who work in industries that use steel as a major input.⁷¹ Consequently, imposition of tariffs on steel would also impact these latter industries negatively.

Additionally, domestic dissent is also emerging in the US against such protectionist measures, defeating the very argument of reviving the American economy, particularly the manufacturing sector. For instance, Harley-Davidson motorcycles in June 2018 announced the relocation of production to avoid tariffs imposed by the EU in response to US tariffs on steel and aluminium. Elaborating on the impact of such tariffs, the company maintained that the EU retaliatory tariffs of 25 percent would result in a tariff of 31 percent, up from 6 percent, leading to an average cost increase of \$2,200 per motorcycle. The estimated cost of relocation for 2018 is expected to be approximately \$30 to \$45 million and the aggregate annual impact due to the EU tariffs to be approximately \$90 to \$100 million.⁷² On June 27, 2018, a coalition of major foreign automakers, including Toyota Motor Corp, Volkswagen AG, BMW AG, and Hyundai Motor Co, has also explained that the US administration imposition of tariffs on motor vehicles would cost hundreds of thousands of auto jobs and threaten the industry.⁷³

According to a report by the US Chamber of Commerce, US imposition of tariffs would adversely impact American businesses and consumers and stymie the progress of the economy, including manufacturers, farmers, and technology companies. Retaliatory measures on US exports will make American-made goods more expensive, resulting in loss of sales and jobs. For instance, as half of all US manufacturing jobs depend on exports, the

proposed trade actions by the Trump administration would threaten as many as 2.6 million American jobs.⁷⁴ While states with large automobile production facilities, such as Michigan and South Carolina, would face the brunt of it, other states, like Alabama and Pennsylvania, will face agricultural pressures in addition to concerns over steel and aluminium products. Out of the \$3.6 billion worth of exports from Texas exposed to retaliatory measures, \$1.6 billion would be from Mexico and \$1.4 billion from China respectively.⁷⁵

The Shifting Politics of Trade War: The Iran Factor

It has been also observed that ever since US President Trump announced its America First Policy, there has been a shift in the politics of trade. For instance, penalties on Chinese telecom firm, Zhongxing Telecommunications Equipment (ZTE), became a bargaining chip for potential concessions on trade. The US Commerce Department on March 7, 2017 announced a penalty of \$1 billion for illegally shipping telecommunication equipment to Iran and North Korea in violation of the Export Administration Regulations (EAR) and the Iranian Transactions and Sanctions Regulations (ITSR).⁷⁶ Thereafter, and pursuant to the previous order, on April 16, 2018, the US banned American firms from selling parts and software to China's ZTE Corp for seven years for violating US sanctions by illegally shipping US goods and technology to Iran.⁷⁷ However, the US administration retracted its decision on June 7, 2018. In this regard, Wilbur Ross, the US Commerce Secretary, announced that the administration had reached a deal to lift restrictions imposed on ZTE.⁷⁸

On similar lines, the US has asked all countries, including India and China to cease buying oil from Iran from November 4.⁷⁹ The EU is expected to be hit the hardest because of Iran sanctions. With bilateral trade of \$25 billion in 2017, European companies including France's Total and Royal Dutch Shell, Airbus and automobile manufacturer Renault have invested heavily in Iran. For instance, automobile manufacturer Renault signed a \$780 million deal with Iran in 2017 which also includes a production plant capable of producing 150,000 vehicles a year.⁸⁰

Part III Way Ahead

The major trends that emerged from the analysis are:

1. The main rationale for President Trump to launch tariffs measures has emerged from his America First Policy and is mainly based on the justification of correcting trade deficit impinging on its national security.
2. It also indicates that beginning with the imposition of tariffs on washing machines and solar photovoltaic by the US, especially targeting China, in January 2018 to the imposition of tariffs on steel and aluminium, the other countries maintained restraint, avoiding any tariff retaliatory tactics. Thereafter, after each decision by President Trump on imposition of tariffs over different sectors, including technology, other countries resorted to retaliatory actions. For instance, it was on

March 23, 2018, that China announced the first list of products in a retaliatory action against the US move to impose tariffs on steel and aluminium. It announced tariff hikes from 15% to 25% on various US products amounting to \$3 billion in 2017, including meat (pork & its products), fruits, steel pipes and others. Also, it was only at the fag end of May that the tariff war intensified with other countries including the EU, Mexico, Canada and India resorting to retaliatory tactics.

3. The analysis of trade trends of the US with major countries – China, the European Union, Canada and Mexico – reveals the tightly knitted and deep rooted bilateral trade and investment relationship among these countries which have seen an upward trajectory over the years. It also suggests that while US has trade deficit in goods with these countries, it also enjoys trade surpluses in services trade. There is also indication of the pervasive nature of integration into the larger global supply and value chains. Therefore, a trade war among these countries would adversely impact the individual countries as well as disrupt the global supply chains.
4. The tariff war is going to impact all countries in varying degrees depending on the trade intensity among these countries, particularly on the commodities and products affected by the imposition of tariffs by the US, and participation in the global supply and value chains. For instance, the countries which are going to be worst affected because of tariffs on steel and aluminium include Canada, the EU, South Korea and Mexico. China which has been the main target of such tariffs would be hit relatively little. Overall, President Trump's steel and aluminium tariffs would impose trade losses on partners equal to \$14.2 billion per year. Contrary to his national security justification, around \$7.5 billion loss would be incurred by traditional US military allies, including Canada, the EU, South Korea and Japan.
5. US itself will be affected by such measures and counter measures with some estimates stating that there are roughly 140,000 Americans who work in steel production and about 2 million who work in industries that use steel as a major input. Similarly, the estimated cost of relocation of Harley-Davidson production for 2018 is expected to be approximately \$30 to \$45 million and the aggregate annual impact due to the EU tariffs to be approximately \$90 to \$100 million.

The first tranche of tariff retaliation by two of the largest economies – the US and China – on July 6, 2018, may be the opening of further skirmishes in the trade war. It also shows that previous attempts at trade negotiations between the two countries have not been constructive. It is also likely that the way ahead might turn worse with more retaliatory actions. Noteworthy, President Trump has already announced imposition of tariffs on \$200 billion, which could reach to \$500 billion worth of Chinese goods in case of retaliatory actions by China. The US administration is further considering curbs on Chinese investments in US technology. Additionally, President Trump has expressed his intention to impose tariffs on cars and car parts which will impact the automotive industry. To this, EU has threatened retaliatory tariffs worth \$294 billion.

Countries, including China and India, have expressed their intent to engage in more talks with the US on trade issues to diffuse tensions and prevent a full-fledged trade war.⁸¹ While bilateral talks between India and the US are underway, bilateral trade talks between the US and China were inconclusive. In order to cope with a possible trade war, countries are also seeking alternative supplies of the commodities that will be affected by the US tariffs. For instance, China has agreed to cut tariffs on 8549 goods, including soybeans, soymeal, soybean cake, rapeseed and fishmeal, from India along with four other Asian nations – Bangladesh, Sri Lanka, Laos, and South Korea - from July 1.⁸²

At this point, the primary concern is the retaliation and the threat of an intensified trade war. Depending on how reactions unfold, there could be stronger implications for economic activity. However, it remains to be seen if there could be a de-escalation of trade war through intensive negotiations or there would be further rounds of measures and counter-measures on trade. The coming months would determine the direction and the extent of impact of such trade war.

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Disclaimer: The views expressed are that of the Researcher and not of the Council.

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