PETERSON INSTITUTE FOR INTERNATIONAL ECONOMICS

Status Report on the US-China Trade War

Mary E. Lovely
Syracuse University &
Peterson Institute for International Economics

Where we are and what it means

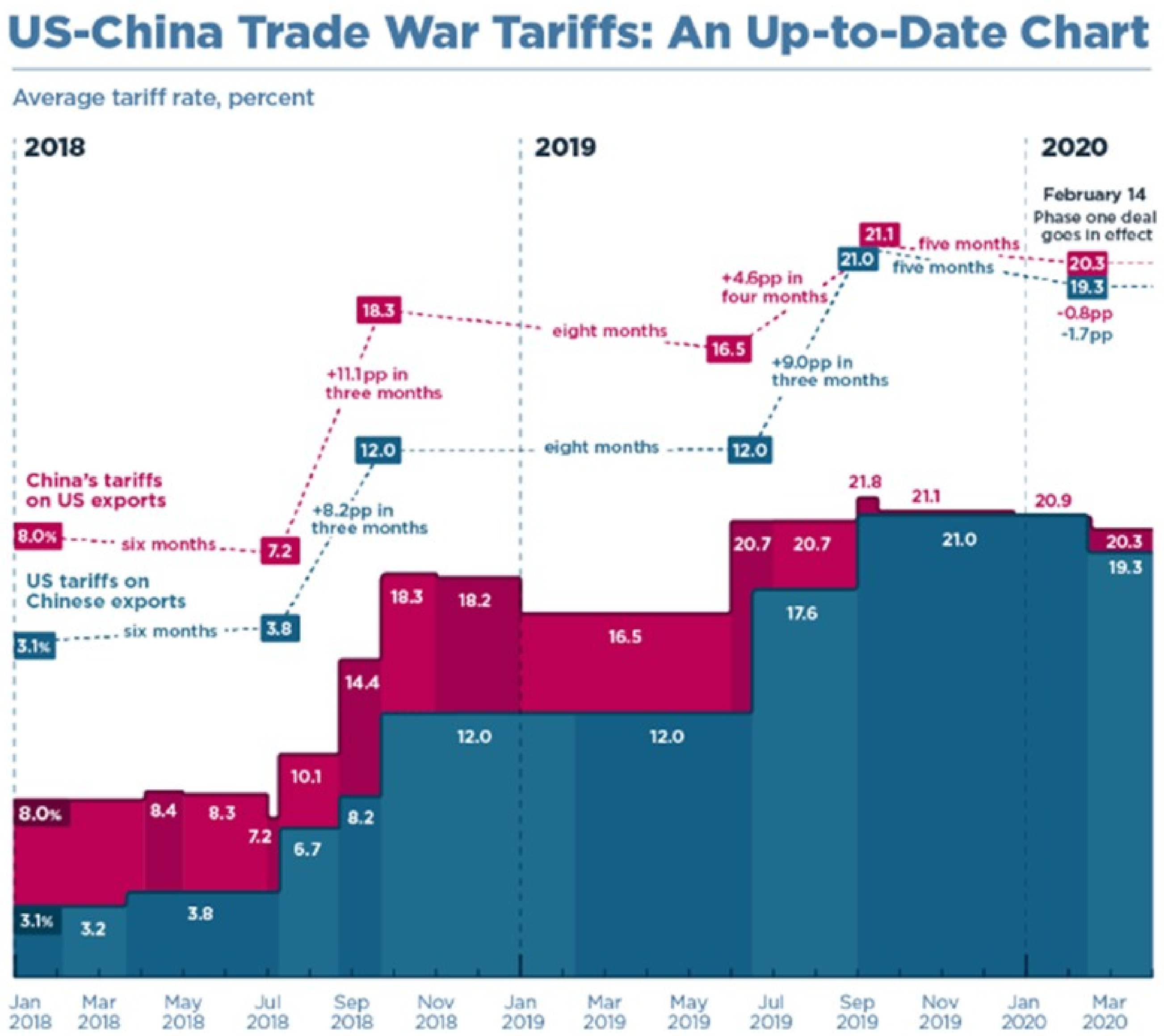
1. The US-China trade war weaponized protection
2. How the trade war hurts the US and China (hint: it’s an own goal)
3. Will the trade war bring supply chains “home”?

Weaponized Protectionism

The United States and China set the pace

US and China weaponize tariffs

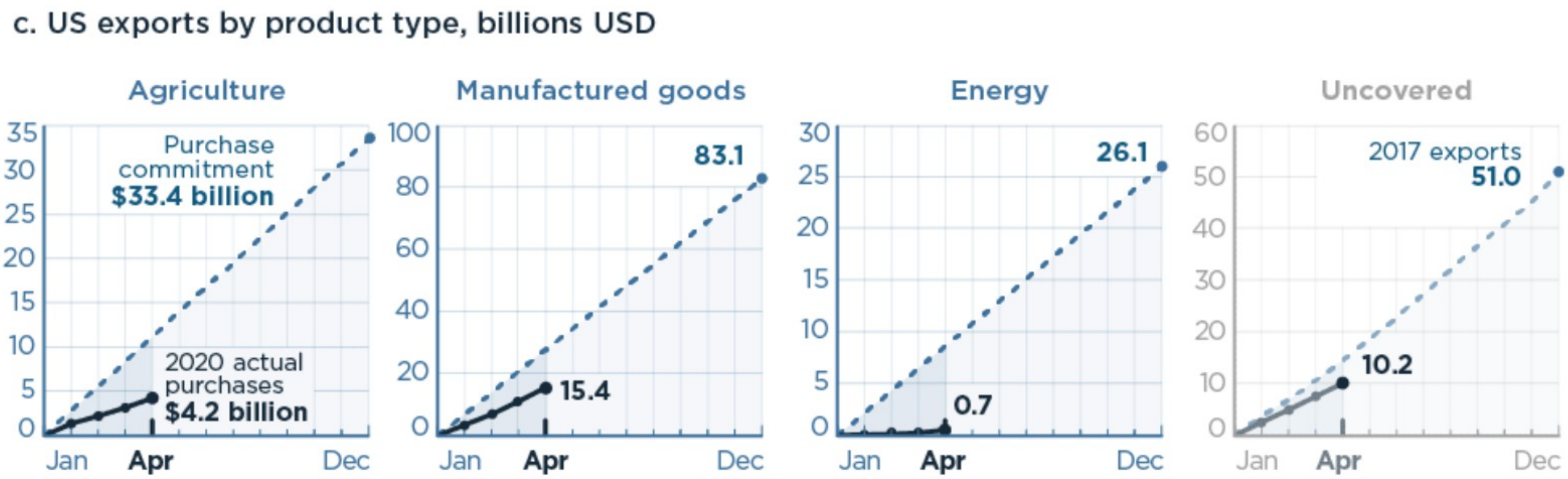
- US weaponizes tariffs on Chinese exports in pursuit of other trade-related goals centered on forced technology transfer.
- China retaliates, with focus on US agricultural exports.
- Through a series of escalating tariff rounds, both sides have erected high tariff walls against each other's exports.



Through rounds of tit-for-tat tariffs, China and the US maintain an average of 20% tariffs on each other's exports.

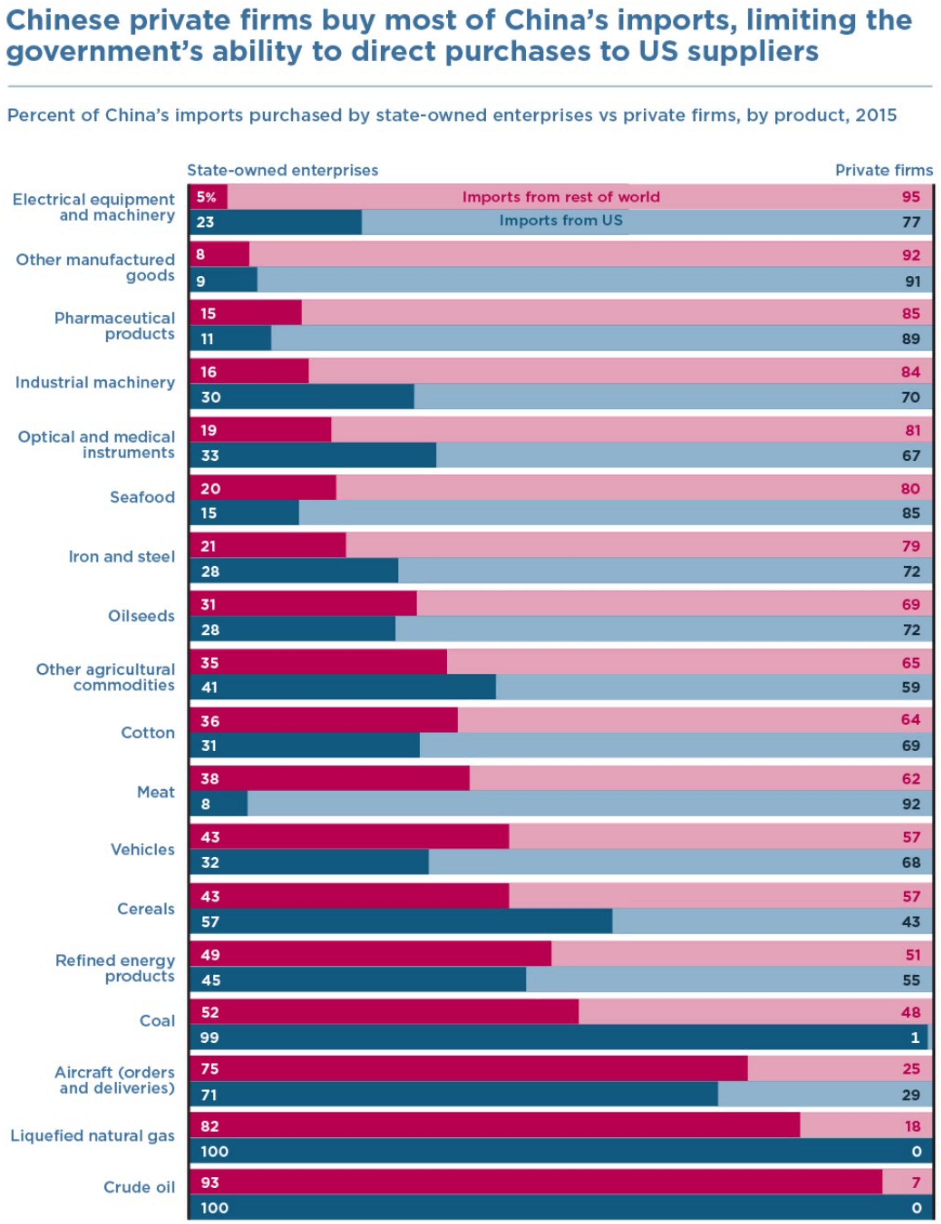
https://www.piie.com/research/piie-charts/us-china-trade-war-tariffs-date-chart

Phase 1 Deal Purchases “Ambitious”



https://www.piie.com/research/piie-charts/us-china-phase-one-tracker-chinas-purchases-us-goods

Phase 1 purchases mandate managed trade – not market driven trade.



https://www.piie.com/blogs/trade-and-investment-policy-watch/trumps-phase-one-deal-relies-chinas-state-owned-enterprises

Did the trade war inflict damage on the US?

US tariffs on China fall heavily on manufacturing supply chain.

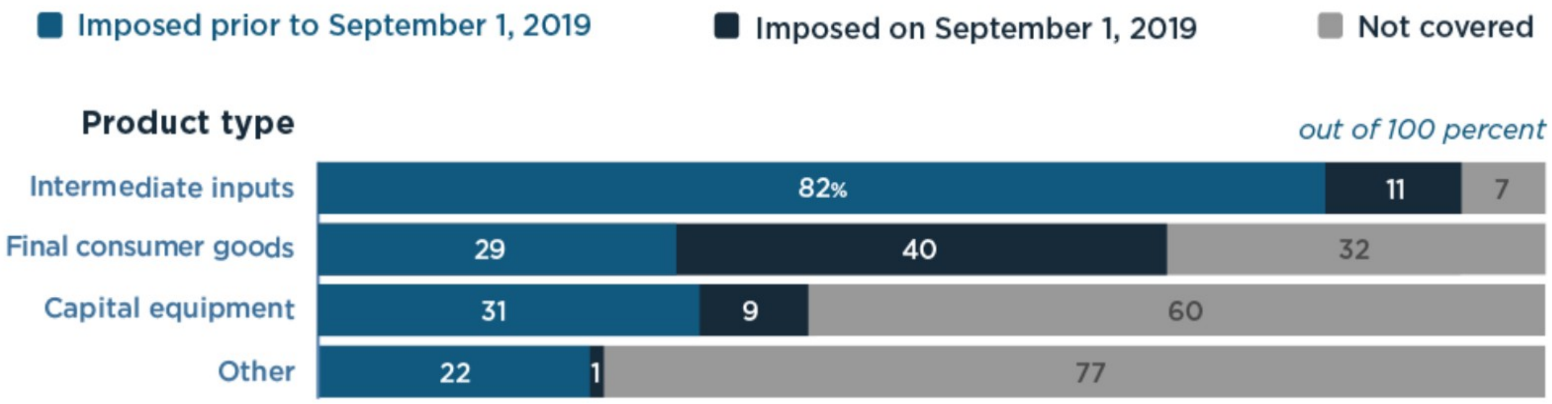
These products largely shipped from foreign factories in China.

Related-party flows are high, signaling direct link to firms operating in the US.

Figure 3

Remaining US tariffs on China aim largely at intermediate inputs

Percent of US imports from China that remain covered by Section 301 tariffs under phase one deal



China does not pay for the tariff – US businesses and consumer do.

- Detailed studies looking at the prices paid to Chinese exporters consistently find that these prices did not fall to absorb the tariff.

- Instead, the tariffs were passed through to US importers, who then passed what they could to US buyers.

Tariffs did not protect US jobs

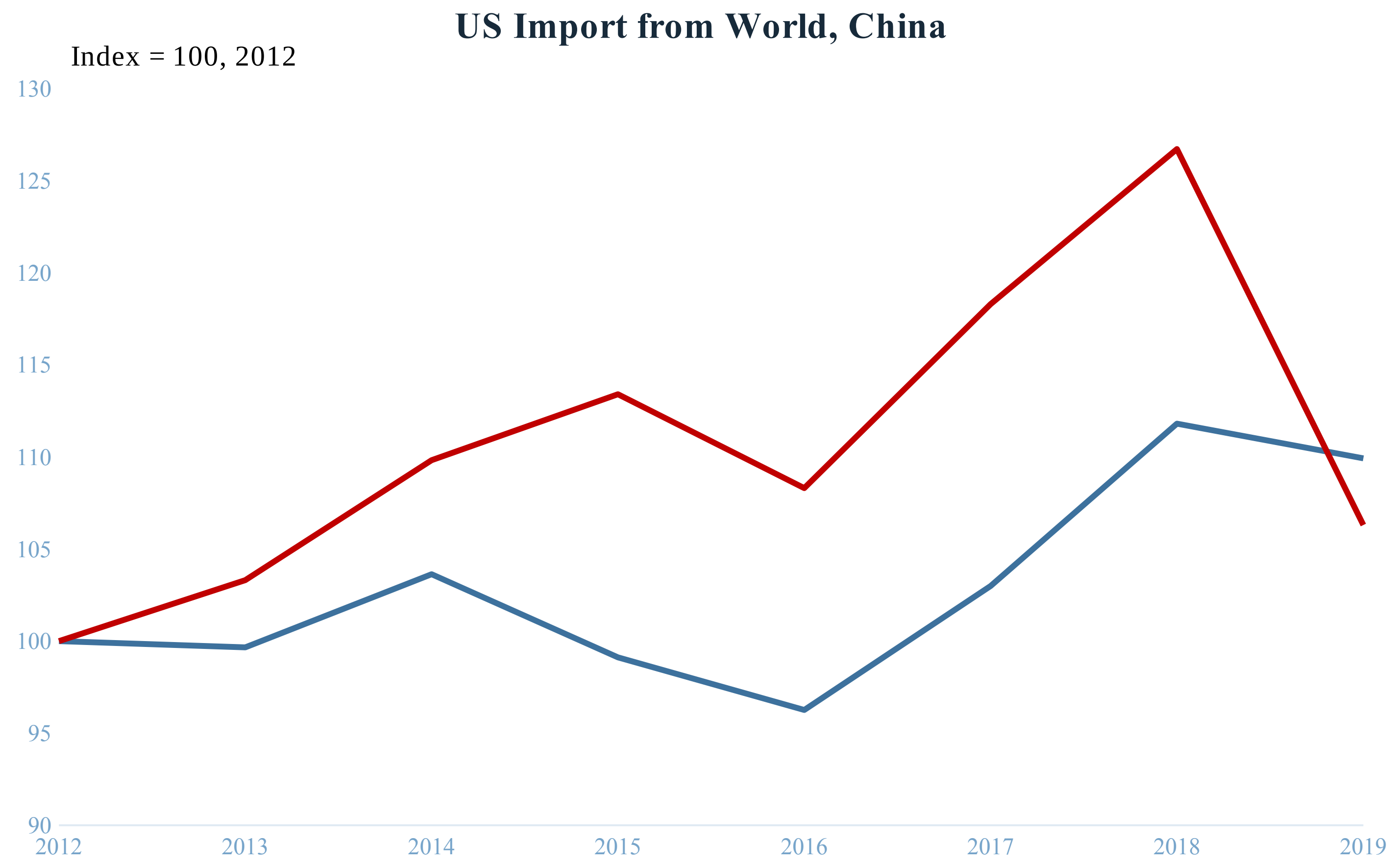
- New study using firm-level data: Firms that eventually faced tariff increases on their imports accounted for 84% of all exports and represented 65% of manufacturing employment. For all affected firms, the implied cost is $900 per worker. http://webuser.bus.umich.edu/handleyk/HandleyKamalMonarch_RisingImportTariffs_FallingExportGrowth.pdf
- Second study using firm-level data: positive effects of tariffs are more than offset by the negative effects of higher prices companies must pay to import components from China, and the retaliatory tariffs China placed on the United States. https://www.federalreserve.gov/econres/feds/files/2019086pap.pdf

Did the trade war inflict damage on China?

Chinese importers paid the Chinese tariffs

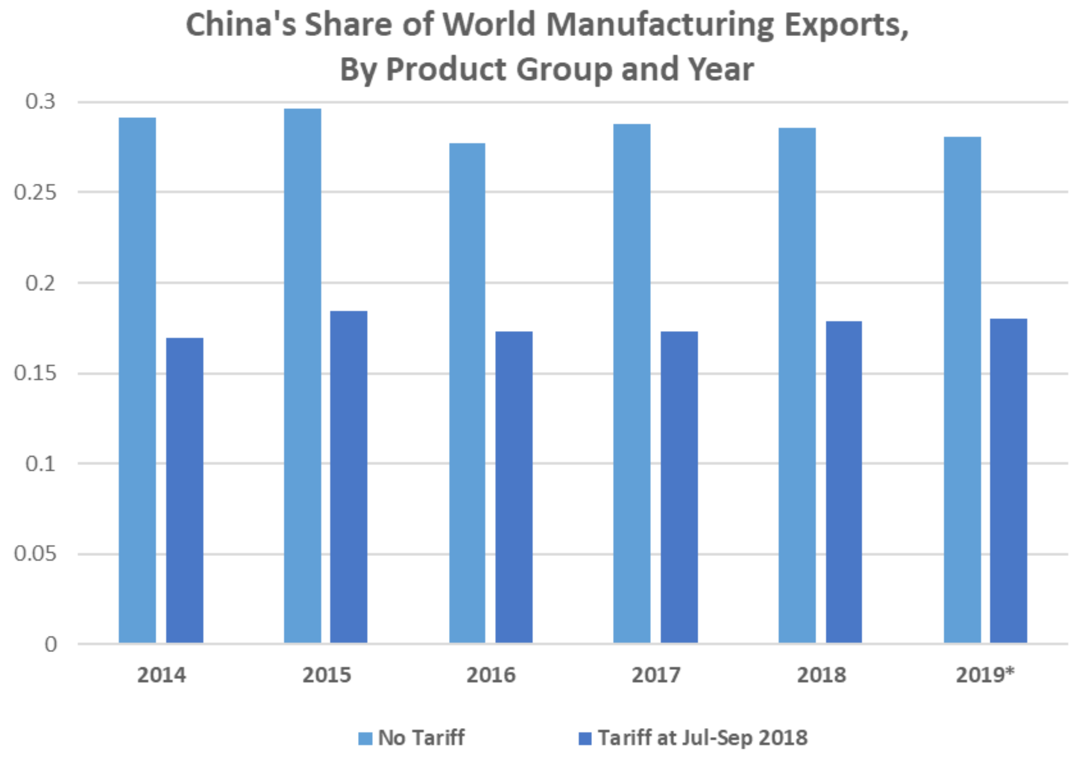
- Studies of US export prices show that these prices did not fall in response to Chinese tariffs.
- Chinese importers absorbed the Chinese tariffs.
- There were job losses in Chinese manufacturing centers as US imports fell, but these jobs are a small share of Chinese economy.

US Imports from China & World, 2012 – 2019



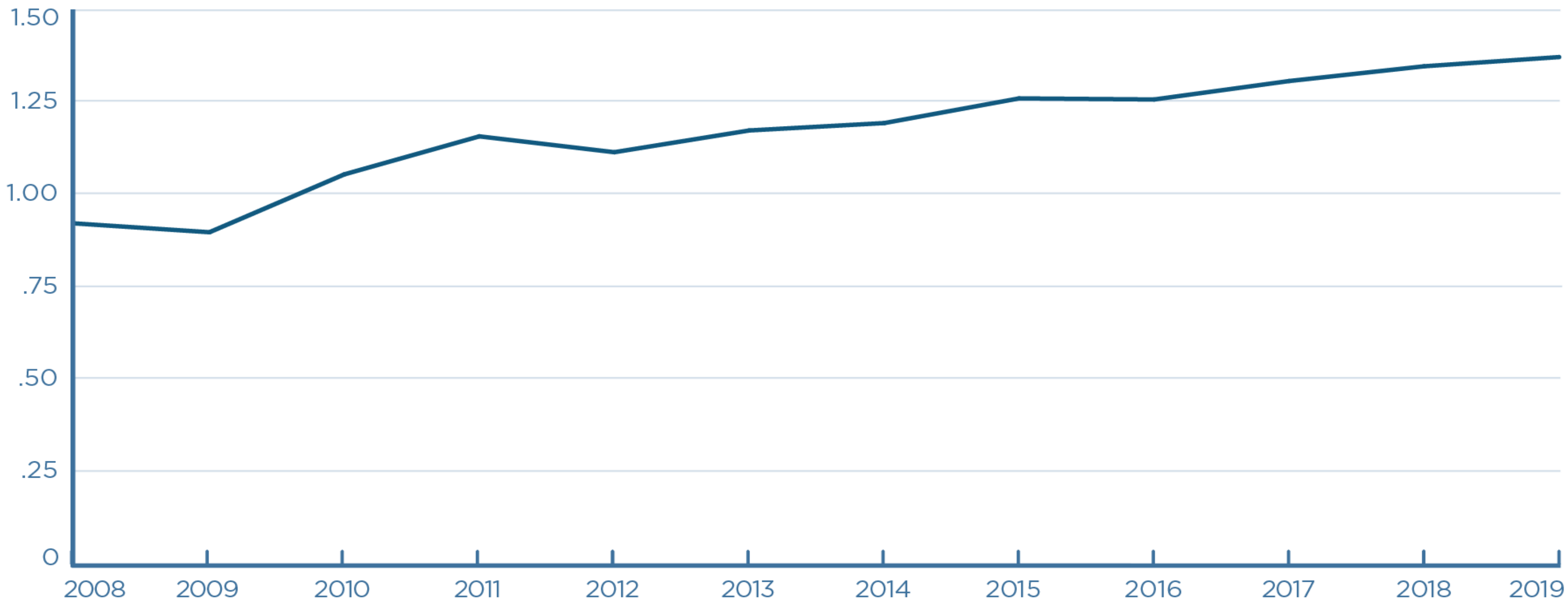
Source: BEA. US monthly imports, 12-month trailing sums

China maintains global market share



Note: Shares for 2019 calculated through October using data for 53 countries due to data availability. These 53 countries accounted for 80% of global exports in 2018. Source: Trade Map and Market Access Map (International Trade Centre, marketanalysis.intracen.org), Bown (2019) (https://www.piie.com/blogs/trade-

Actually utilized FDI into China, 2008 - 2019, billions USD



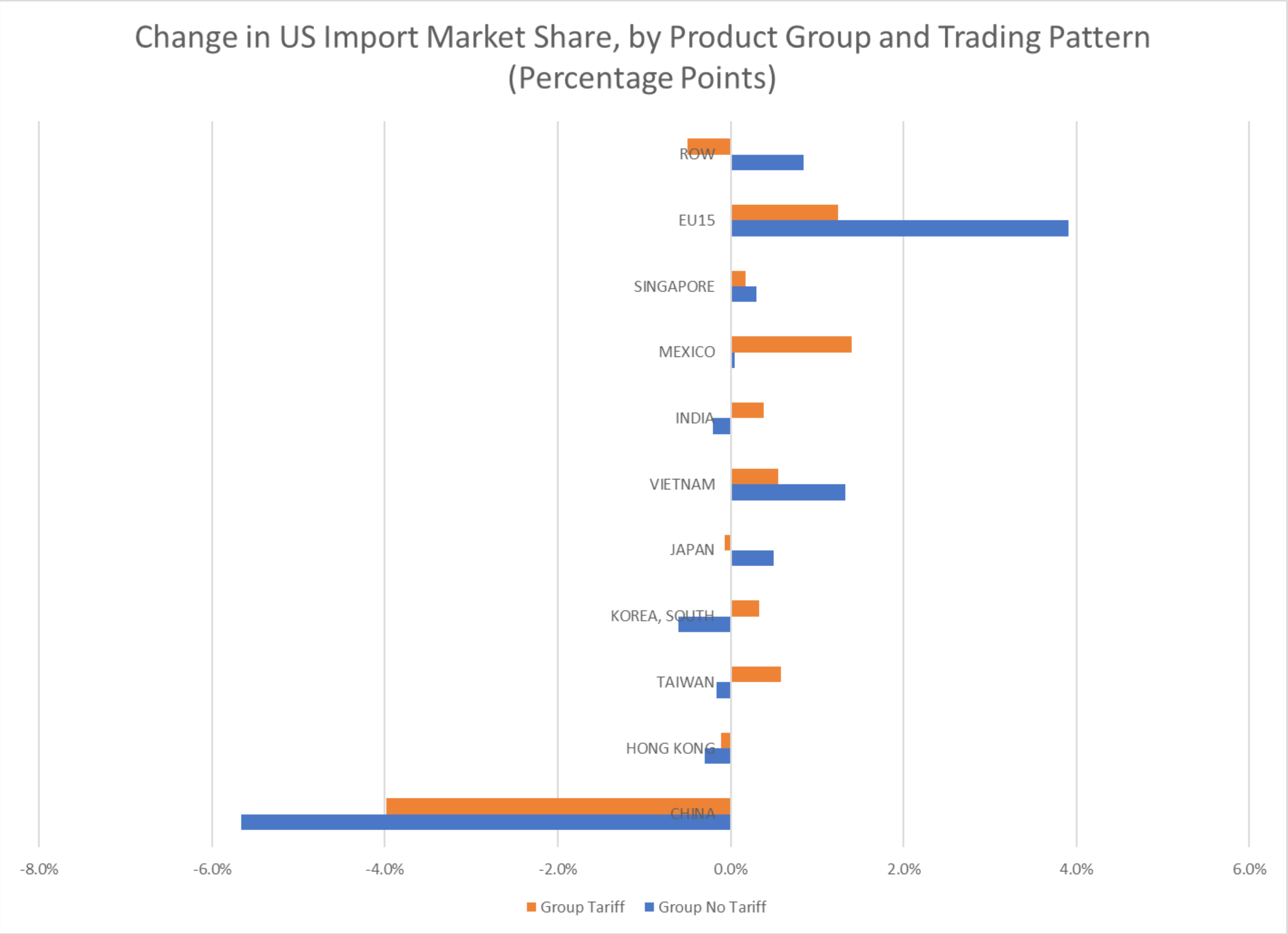
Source: Ministry of Commerce in China.

Will Supply Chains Come Home?

No, unless the barriers and costs are very high

Evidence from the US-China Trade war:

1. China's lost 4% of the US market for newly tariffed good but it lost 5.7% for no-tariff goods.
2. US market share of tariffed goods gained by Mexico, Vietnam, EU, and Taiwan.
3. US market share in goods not subject to tariffs gained by EU, Vietnam, and Japan.



Other tools for decoupling

- Relations continue to deteriorate, with growing demands for decoupling to preserve domestic security and prevent aiding potential enemies.
- **Investment blocks** will reduce cross-border M&A activity in sensitive technologies. Uncertainty over "sensitive" will grow.
- **Export controls** will become more stringent and go deeper into supply chains.
- **Buy America** push motivated by deteriorating US-China relations and activated by response to virus.

Can the US decouple from China or isolate itself from the rest of the world?

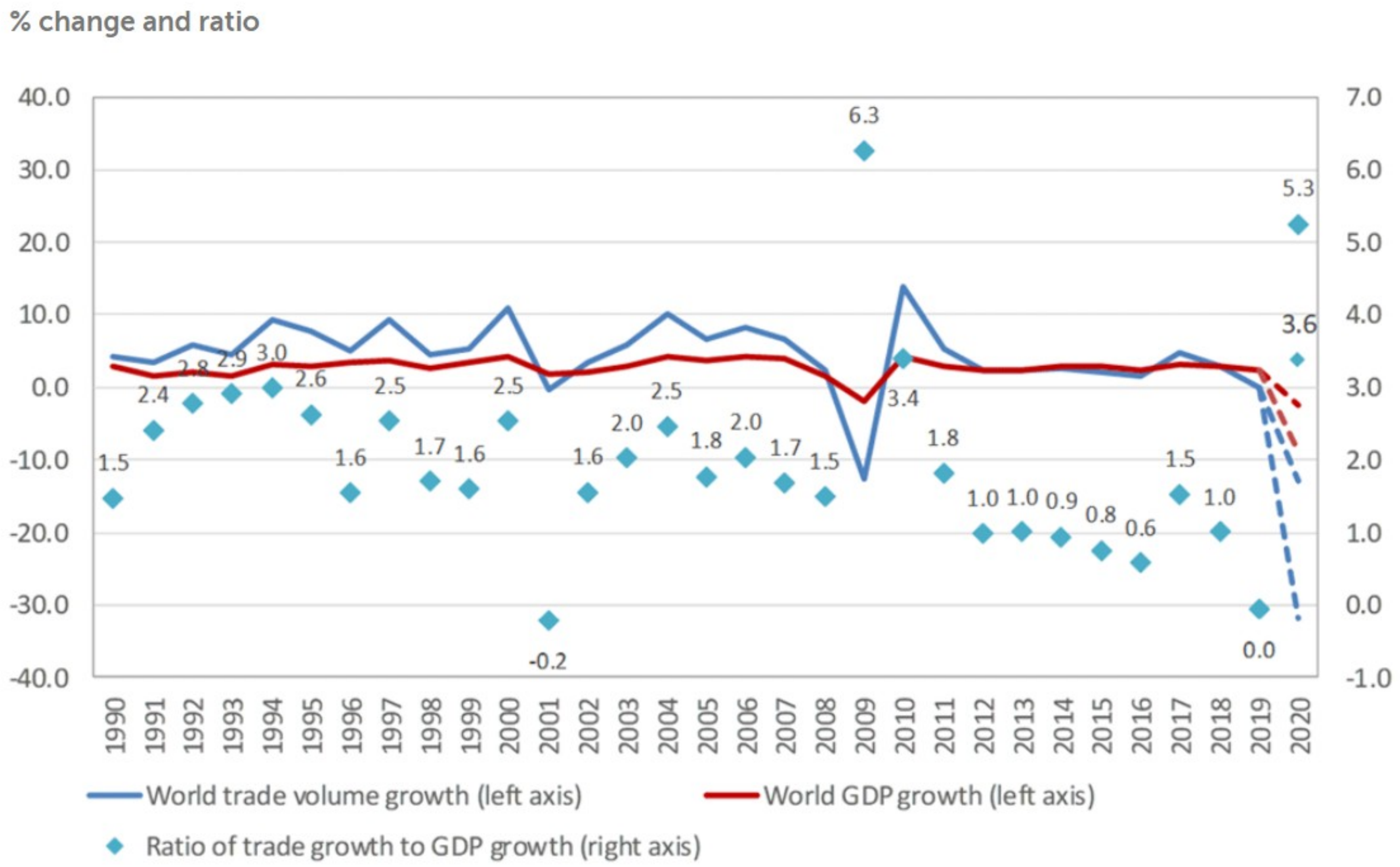
- No other country followed the US lead by imposing tariffs on China for IP related violations.
- Other countries seek to take China’s place in US supply chains, without decoupling from China.
- In a March 2020 AmCham China report, based on a survey carried out at the end of 2019, only 9% of US businesses have started relocating manufacturing or sourcing outside of China, with another 8% considering the move
- Many expect to invest more in China over next few years.

Now back to Sonni

Trade and investment flows during 2020 Pandemic

Trade and investment track world income growth

Trade Volumes Fall Faster than GDP



Source: WTO Secretariat for trade and consensus estimates for historical GDP. Projections for GDP based on scenarios simulated with WTO Global Trade Model.

Global investment flows collapsing

- Cross-border investment flows slowed before the current crisis.
- Global FDI fell by 13% in 2018 and fell again by 1% in 2019, according to UNCTAD
- OECD expects FDI flows to fall by more than 30% in 2020 even under the most optimistic scenario