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Inching For A Trade War: Worst is Yet to Come

By Kaewkamol Pitakdumrongkit

Synopsis:

Although the prospect of a trade war between US and other economies looms large, the actual confrontation could still be evaded. But even if a trade war does not occur, the world is not off the hook as the US is having another tool in the pipeline which may in the future be wielded against friends and foes alike.

Commentary

FEW OTHER things are making headlines as much as a potential trade war after President Donald Trump declared that the United States would impose tariffs on steel and aluminium from Canada, Mexico, the European Union (EU) and China. Such a move unsurprisingly has created uproar around the world.

The prospect looks grimmer when the trading partners vowed to retaliate. For example, Canada is planning to slap up to 25% tariffs on US\$13 billion of American goods targeting steel and whiskey. Mexico's tariffs are aimed at US steel and agricultural goods. EU's countermeasures consist of 25% duties on about 200 American products such as motorcycles, cigarette, and bourbon whiskey. As for China, the US Commerce Secretary Wilbur Ross' negotiation with Chinese Vice-Premier Liu He in Beijing recently yielded no new agreement.

Looming Trade War

Right after the talk, Beijing on 4 June 2018 warned that if Washington actually slapped tariffs on \$50 billion of its exports scheduled to take place later this month, "then all the economic and trade benefits negotiated by both sides are not going to take effect". In response to the Trump administration's plan to impose new tariff

measures aimed at China's high-tech manufacturing sectors, Beijing said it would counter with duties on several American products namely autos, soybeans, and airplanes.

As the world is inching closer to a trade war, one should, however, not feel entirely hopeless. Some efforts have been made to turn the tide in a more positive direction. For instance, French Finance Minister Bruno Le Maire announced after the G7 finance ministers' and central bank governors' meeting in Canada: "We still have a few days to take the necessary steps to avoid a trade war between the EU and the US, and to avoid a trade war among G7 members."

Economists and trade experts wasted no time to strongly oppose a trade war and pointed to evidence that no one would win from such a showdown. Mark Zandi, a chief economist at Moody's Analytics, posited that taking the Sino-US trade war alone, it would cost 190,000 American jobs. Moreover, Trump's tariffs triggered anxiety among certain American constituencies, namely wheat growers.

Every year the US produces about 60 million tonnes of wheat with almost half of which are geared for exports. Tariffs on US agricultural products will surely not bode well for these farmers especially when the harvesting season just starts.

The recent interplay suggests that the outcome can be one of these two possibilities – a trade war, or not. But despite scary prospects, such war may not happen. Perhaps Washington and the other countries may manage to evade it with adept diplomacy.

The US may come to realise the non-commercial consequences of its tariff policy such as alienating allies it needs to advance its security or defence cooperation, and hence reverse its course. Perhaps pressure and outcry from American farmers or voters can finally get President Trump's ear and change his mind. As a result, the world can once again breathe itself a sigh of relief.

If Tariffs Are Bad, Investment Restrictions Are Worse

Suppose a trade war does not occur, the world's economy is not yet off the hook. Future disruptions can still be caused by the US' restrictions on international investment between it and other economies. The bipartisan Foreign Investment Risk Review Modernisation Act (FIRRMA)'s two versions were approved by the House Financial Services Committee and the Senate Banking Committee on 22 and 24 May 2018 respectively.

Although some differences between these two bills need to be ironed out, the Act will likely expand the authority of the Committee on Foreign Investment in the United States (CFIUS) – an inter-agency committee mandated to review transactions that could lead to foreign acquisitions of American businesses to determine their effects on the U.S. national security.

In short, FIRRMA will extend the agency's oversight to cover more kinds of transactions including "investments where a foreign company would not necessarily gain control of a US firm [such as] joint ventures between US and foreign

companies, minority stake investments and transactions near military bases or US government facilities”.

This bill was mainly driven by Washington’s desire to prevent Chinese takeovers of American firms and access to US technology as evident by CFIUS’ blocking of the acquisition of an American chipmaker Qualcomm by the Singapore-based Broadcom in March on a national security ground.

However, nothing guarantees that acquisition cases in other industries will not fall under the mechanism’s scrutiny in the future. In short, the entity can come to assess or even block other foreign investment coming from other countries into the US.

Investment War Next?

If Washington begins to block more inward foreign investment, other states may retaliate and the world will witness an investment war which could potentially damage the global economy to a great extent. Because capital is a necessary factor for the broadening and deepening of transnational production networks, this investment showdown will ultimately undermine or disrupt cross-border trade.

In other words, investment must first take place to establish production facilities in several locations to then enable transnational supply chains to function. If capital flows are discouraged due to stricter rules and regulations, it would undermine production networks and trade between Washington and other countries around the world.

Tariff drama aside, the US is having another tool in the pipeline which may in the future be wielded against its friends and foes alike. The world may have to brace itself again for another impact.

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