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TRANSCRIPT

The Trade Guys Podcast

“The Trade War Rages On”

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Transcript by Rev.com

Scott Miller: I'm Scott.

Bill Reinsch: I'm Bill.

Group: We're The Trade Guys.

Andrew Schwartz: You're listening to The Trade Guys, a podcast produced by CSIS where we talk about trade in terms that everyone can understand. I'm H. Andrew Schwartz and I'm here with Scott Miller and Bill Reinsch, the CSIS Trade Guys. The Trade Guys are back and they're here to talk about all the eye-popping news between the US and China as the trade war rages on. Meanwhile, the US and Japan appear to have their trade relationship back on track with a new agreement. We'll talk about all of that, and more, on this episode of The Trade Guys.

Andrew Schwartz: The Trade Guys are back, school is in, and the trade war is escalating.

Scott Miller: And traffic is terrible.

Andrew Schwartz: Traffic's terrible.

Scott Miller: Yes.

Andrew Schwartz: It took me 45, 50 minutes to get in this morning.

Scott Miller: It's all those people turning left at your school.

Andrew Schwartz: That's right. They're all turning left. I left late today. My wife took the kids. I was in the pool and it still took me 45, 50 minutes to get here.

Bill Reinsch: Really?

Scott Miller: Yeah. It's the first day of everybody's new commuting pattern.

Andrew Schwartz: Well, nobody's going to like it because today the market is way down as we speak. It's Tuesday, obviously, the day school's back in Montgomery County and in DC. There's a lot going on with the trade war escalating. On Sunday, President Trump's trade war with China entered new territory and the next round of tariffs took effect. It's interesting, Peterson, our colleagues over at the Peterson Institute have now come up with a new piece of data. They say that this move will bring the average tariffs on Chinese imports to 21.2% up from only 3.1% when President Trump came into office. That's pretty big.

Bill Reinsch: That's huge, actually 20% on anything is going to be huge. It's going to get worse when the December ones go into effect.

Andrew Schwartz: But, we're near maximum coverage on tariffs, right?

Bill Reinsch: Yes, so-

Scott Miller: Not quite. We're about 65%, 70% of imported goods from China are affected by the tariff. The plan is by December 15th though, almost a 100%.

Bill Reinsch: I think it's like 97% will be covered by December 15th.

Scott Miller: By December 15th, but you're right the average trade weighted tariff, but the United States is basically an open market. Our average trade weighted tariff on an MFN basis is around 3% actual collections are about 1.7%, so we generally have low tariffs on everything, almost everything. Now tariffs on Chinese goods are getting to the point where everybody starts to notice.

Andrew Schwartz: I mean American tariffs on foreign goods have already climbed higher than any time since the '60s before Sunday. Then the United States imposes another new 15% tariff, and these levies are on food, clothing, lawn mowers, and thousands of other made in China products. This is almost nearly everything China ships to the United States.

Bill Reinsch: The ones on Sunday will be significant because for the first time there are a lot of consumer items that will attack people right in their pocket book, clothing, shoes.

Andrew Schwartz: This is stuff people buy Walmart.

Bill Reinsch: Toys, furniture, electronics.

Scott Miller: Toys are mostly in the December tranche and electronic stuff is mostly in the December tranche.

Andrew Schwartz: It's just in time for Christmas?

Bill Reinsch: Well, no, because it'll all be important before December 15th. I mean, the stuff that you're going to buy for Christmas presents that comes in in September and October, if not already in. In fact, shoppers today at Walmart may not. Well, it depends. They may not notice a difference because actually all the stuff that's there today certainly arrived before Sunday.

Scott Miller: Correct.

Bill Reinsch: Now that doesn't mean that Walmart won't take advantage of the situation and bump up a price or two in anticipation.

Scott Miller: But Bill's overall point is right, so far the consumers have really not seen much in pricing that it's affected them directly.

Andrew Schwartz: But now they're going to?

Scott Miller: Well, likely. I mean, look, the first year of the tariffs on China, many of us were surprised when the average import price to the United States actually declined in the first year. You look on the macro level, it's hard to find the disruption. Now product by product, I'm certain there's a lot happening and a lot of adjustments in supply chains. Now, given the scope of the new tariffs and the basically complete coverage by December, if we're ever going to notice, we'll notice now.

Bill Reinsch: It'll be interesting to go back and look at this six or eight months from now to see what happened, because it's an interesting example of the argument that we've exploded, I think on this podcast in the past, about who pays.

Andrew Schwartz: Yeah.

Bill Reinsch: Because Trump keeps getting the Chinese to pay and the fact is the Chinese don't pay the importer pays. But, it is also true that if you're an American buyer and you have a lot of market power, Walmart might be a good example, you can sometimes go back to your supplier and say, "Will you give us a deal because I'm going to buy 8,000 dozen of this kind of tee shirt? If you can't lower your price a little bit, maybe I won't do that." The big guys come out of this sometimes being able to force some of the costs back on the Chinese, whereas the little guys don't have any leverage and they can't do that. Clear that that's going to happen all the time. In the end it ends up being in the gray area where the Chinese will eat some, the retailer will eat some, and the consumer will eat some. It's not entirely clear cut. What is clear cut is the Chinese don't not pay at all, and we know that.

Scott Miller: The Chinese government?

Bill Reinsch: Chinese.

Andrew Schwartz: Are they hurting from this?

Bill Reinsch: Oh yeah.

Scott Miller: Yes. I mean, look, I think we've characterized it before as given the economic relationship, the US has more ability to inflict harm on China. China has more ability to absorb harm and then to absorb the pain. But, this is hurting, and you can see it in their economic numbers appear to be slowing down. This is a factor in it.

Bill Reinsch: But they'd been slowing down for other reasons.

Scott Miller: Yes.

Bill Reinsch: I mean, it's hard. These things always get complicated because you're trying to tease out a single cost when there are many. Their economy has been slowing down more or less for the last couple of years. Growth is still around 6%, which people here would kill for. For them it's a significant reduction-

Andrew Schwartz: It's low for them.

Bill Reinsch: From what it had been, and it's beginning to get worse. Wage rates have been rising anyway. We think that, I mean, I shouldn't speak for Scott, I think that the way that Xi Jinping is conducting the economy, which is channeling more credit to the state on enterprises, more credit to the unprofitable parts of the economy, and not to the vibrant private sector part, is only making things worse. There's a lot of things that are happening in the Chinese economy that are bad, one of which is tariffs but it's not the only thing,

Andrew Schwartz: The latest tariffs bring the total US tariffs on China to about 360 billion worth of imports. That's nothing to sneeze at.

Bill Reinsch: No.

Scott Miller: Well that's correct. It is a lot of what we import from China, but in the context of a \$22 trillion annual economy here. You got to keep all in perspective.

Andrew Schwartz: Right.

Scott Miller: This is the kind of pressure that the president intends to apply and force all the supply chain operators to revisit whether or not they want to relocate, whether they want to hedge and move production out of China. Once those decisions to move supply chain partners, and use partners that are not in China, those decisions kind of have semi-permanence to them. Once you've hedged, qualified a new supplier, gotten new production up and running, it probably doesn't revert back even with a removal of the tariffs.

Andrew Schwartz: So Scott, is it the administration's objective to push United States companies out of China or is it to force China to make concessions that result in US companies being treated more fairly in China?

Scott Miller: It seems to me that their objective is the latter. Their tactic is the former. In other words, they're using supply chain pressure, pressure on supply chain operators, including those with American headquarters to make different decisions to apply pressure to the government of China. What they're really looking for is fair treatment. Keep in mind, not every American company or every American enterprise that operates in China is a supply chain operator. There are many, KFC would be a good example, or Walmart operates a lot of stores in China. They basically are in China to serve the Chinese consumer.

Andrew Schwartz: I hear by order Kentucky Fried Chicken out of China.

Bill Reinsch: Why? It's not-

Scott Miller: Yeah, right. It's a really different business model. My general motors sells more cars in China than they sell in United States.

Andrew Schwartz: Yeah.

Scott Miller: So these companies that are in business to serve the Chinese consumer have a different profile and are certainly would like fairer treatment. On the other hand as pressures escalate from the United States, I think that we are likely to see a number of US firms in China face pressure from the Chinese government whether it's delayed regulatory approvals, or additional inspections, or whatever it might be. It's never been easy to operate in China. It's likely to get tougher for those firms.

Bill Reinsch: Yeah, I'd answer the question a different way. I think Scott is basically right, but I think within the administration there are differences of view about this. I think there are some people in the administration who think the decoupling, which is what you're talking about, is a good idea and that is what we should be pursuing. I don't think that's the President's goal. I think the President wants a deal. That's the way he thinks and what a deal is for him tends to change from time to time, which is why people are confused.

Sometimes a deal is let's buy a whole bunch of soybeans or let's sell them a whole bunch of soybeans. LNG airplanes, cut the deficit, declare victory. Other times there are these structural issues that we've talked about for weeks that really need to be addressed, and if the Chinese won't address them, we can't have a deal. He has not yet accepted big buys as a solution. On the other hand, you don't really know what he's prepared to accept as a solution. I think what he wants to be able to do is declare victory to the American people and say, "I've made things better for you," and decoupling, I think, is hard to say that's better for anybody. He wants to come back with a victory saying, "I forced them to change their practices. I forced them to buy more stuff," and he is the president, so that's the policy that will prevail.

Scott Miller: In the interim, he's basically saying, "Somebody had to do this. Okay, I wish one of my predecessors would have done it, but somebody had to and I'm the guy."

Andrew Schwartz: Okay, but so maybe he can say that, but hasn't the trade war turned into something of a quagmire at this point?

Bill Reinsch: Well, yes, they're locked in one of these embraces that they neither one can get out of, because right now I think it's not in the interest of either a to pull out. I mean, Trump has spent a year, two years, talking about how important this is, what a big deal it is, also how close to a deal we are, how much progress we're making, how much they're suffering, how anxious they are and make a deal. If he pulls out, that's failure, which is not really in his vocabulary, but that's admitting failure and exposes himself to enormous criticism.

Scott Miller: For the Chinese, the closer we get to our election, the closer they get to potentially having a different counterparty, so they're going to wait it out.

Bill Reinsch: If they pull out it allows Trump to blame it all on them, which gives him not really a victory but something he can call better than a defeat. It also, I think, undermines the role the Chinese are trying to play globally, which is to say, "Hey, we are the good guys. We are the sustainer of the trading system." I don't know that anybody believes that, but that's what they're saying. If they pull out, I think they undermine that. It gives Trump an excuse to blame them. And Scott is exactly right. I don't think they've figured out, as nobody has figured out, how our election is going to come out. It's got to be tempting for them to continue this for awhile.

Scott Miller: Just wait to see.

Bill Reinsch: Wait and see what happens, but you see Trump's going to wait and see what happens too. The best thing for him, I think, is to make a deal in October of 2020. Because if he does it sooner than that it has time to fall apart. It won't be a good agreement because they're not going to give us everything that he wants. So, he has a choice of a week agreement or continue the war. What he will do, I think, is take a weak agreement. Say it's a strong agreement, declare victory, and hope that nobody figures out that that's not true before they vote. But that means he has to drag these talks on for another year, because if he makes a deal this September or next month, it's going to fall apart in the intervening period. If he waits a year, maybe he gets away with it. I think he's in the talks for the long haul. The Chinese are in the talks for the long haul. It's what you said, it's a quagmire because neither one is going to agree to what the other one wants, but neither one is willing to pull out.

Andrew Schwartz: Meanwhile for Donald Trump, consumers may start to feel this, particularly his voters.

Scott Miller: Well they may, but keep-

Bill Reinsch: We say that, but look at the farmers.

Andrew Schwartz: Yeah, right they're feeling it and it hasn't shaken them in terms of their vote.

Scott Miller: They're still with him. A year from now, I mean, there's a term in consumer marketing called meeting and an initiative in the base. You launch it in January of one year, the next year it's part of your base period. He's going to meet the tariffs in the base right before the election. The economy, since all our comparisons are versus year ago may actually look rosy given the tariffs are in the base end of post. It's not a bad gamble on his part. Also, I would point out, there is no challenge to the substance of the policy from his political opponents, from Senator Schumer, to any of the democratic candidates for president.

Bill Reinsch: That's right only the implementation not the goal.

Scott Miller: There's criticism on the implementation, but not the policy itself.

Bill Reinsch: In fact, most of the politicians are falling all over themselves to take an even tougher line than he has.

Scott Miller: Right.

Bill Reinsch: For example, when he put or implied the Huawei was in play as a bargaining chip, he took enormous grief from his own party beginning with Senator Rubio but also Senator Schumer and host of Democrats who said, "It's a national security issue. You can't put it on the table."

Andrew Schwartz: Well, isn't there a case to be made also though that he's got problems coming at him from small business owners as well. I mean, something caught my eye this week too. Wall Street Journal survey that showed that economic confidence among small US businesses is at its lowest since November, 2012, so he's got heat coming from there as well.

Bill Reinsch: Still waiting for that to show up in political polling though.

Andrew Schwartz: Yeah.

Bill Reinsch: He's still got what, 90% support in most Republicans?

Scott Miller: 88% according to Gallup, but 90% is a good reference number among same party support. That's why there is no challenger for the party nomination.

Andrew Schwartz: He's not feeling the heat from the Democrats, not feeling the heat from his own party. He fine, he can work it out.

Scott Miller: The main street economy continues to be relatively strong.

Bill Reinsch: That's what I think things will turn on. Do we begin to slide into recession in the first part of next year, which will make everyone nervous? We seem to be going through these waves of recession panic. We went through one in February because there were fourth quarter of 2018 results were not so great. Everybody was predicting a recession either later this year or early next year. Then the next tranche of data looked pretty good, so in May and June people weren't talking about that anymore.

Scott Miller: There were earlier this month.

Bill Reinsch: Earlier this month, well last month in August, we had recession panic all over it.

Scott Miller: Yeah, the inverted yield curve sent everybody into a panic. But look, the basic consumer numbers are holding up. Employment is still strong. There's some things that indicate that how people feel about the economy may be different than what the numbers say.

Andrew Schwartz: Why do you think the Democrats aren't more critical of Trump and his erratic handling of the Chinese?

Bill Reinsch: You know, I asked one of them about that. There were multiple answers. One was, well, we are, but people aren't paying attention. Another one was, because we're spending way too much time responding to every tweet rather than looking at the bigger picture. The guy is a master at changing the subject. Every day he rolls out a new enemy, a new thing that you've got to deal with. A lot of them are not able to resist the temptation to go after the outrage of the moment instead of concentrating on the bigger picture.

Andrew Schwartz: They're basically saying he's rendered them powerless.

Bill Reinsch: They wouldn't put it that way.

Scott Miller: Keep in mind, on this issue, the issue of China, the American people, and Bruce Stokes as data shows this, the American people believe China is an unfair trading partner. Okay, they believe that, so if you're going to pick on somebody, that's fine. They do not perceive Europe, or Japan, or Canada, or Mexico that way, so the voters are basically saying the president's right about identifying them as an unfair trading partner. That's why nobody challenges the policy, I think.

Andrew Schwartz: Even though the way he's handling it is-

Scott Miller: Oh, they'll nitpick the way he handles it.

Bill Reinsch: They're criticizing the way he handles it.

Andrew Schwartz: Yeah, but it's not sustained. It's not loud. It's not, "This isn't the right guy to handle it."

Bill Reinsch: Maybe because everybody's been away. There hasn't been anybody here in Washington doing the daily briefing or anything. They've all been out meeting with constituents. The last debate was at the end of July, so we haven't had the candidates making nationwide public statements. They've all been at the Iowa State Fair or a various other places. I think once people come back into town, next week, you're going to hear a more coordinated approach.

Andrew Schwartz: Why haven't we heard more from business leaders? I mean, it's made the market uncertain at best. The market's been up, it's been down. It looks like Trump's playing with the market even. Why haven't we heard more from business leaders about this?

Bill Reinsch: Well, you've heard from the Roundtable and you've heard from the US Chamber. I can't remember if NAM has said anything recently.

Andrew Schwartz: Well, we're not hearing from major investors, are we?

Bill Reinsch: No, I don't know. I'm not.

Scott Miller: Well, it's a missing piece. Keep in mind, their experience with China is not all that different than voters. I mean, companies doing business in China, and you can see this in the US China business council surveys, are generally they're making money. They know they have to be there because of the size of the consumer market, but they're not happy about the way they're being treated, and they don't think it's going to improve anytime soon. So, for some companies in some respects, they probably agree with what the president's doing.

Andrew Schwartz: It sounds like you all think that there's some support for what President Trump's doing.

Bill Reinsch: There's support for his ideas, there's support for his goal. There's not a lot of support for tariffs as an instrument. Most people think that that's an instrument that's doomed to fail, that he's not going to achieve what he's wants. There's been a couple of surveys of American companies doing business in China recently and I mean, they say what, what Scott said, "They're all making money, but they're all unhappy because of the way they're being treated." Fewer of them than you might think are seriously considering leaving. But, of the ones that are seriously considering leaving, I think, all but 3% of them are considering going somewhere else other than the United States.

If the message from the President is come home, that's not being heard. They're not coming home. They're going to Vietnam, they're going to Bangladesh, they're going to India, they're going to Indonesia, they're going to 50 places, but not the United States.

Scott Miller: It's a lot of hedging, but if you're hedging, you don't want to be in the newspapers. You don't want to be making public statements. You want to just hedge.

Bill Reinsch: The ones that are not going are not going for the reason that Scott said. That is, despite all the talk here, they're not in China to import back into the United States. They're in China to meet the demands of Chinese consumers, to serve the Chinese market. Now, some of them ship stuff back here, and those are the people that Trump likes to attack. It's like KFC, they're not shipping chicken back to the United States. They're in China to sell chicken to Chinese.

Andrew Schwartz: All right, in this quagmire, what do you guys think happens next in the short term?

Scott Miller: Sound and fury signifying nothing.

Bill Reinsch: Yes, exactly, a lot of drama. They're locked in this embrace. I don't think they get out of it for a year, so we can have this conversation 12 more times at least.

Scott Miller: The US China tensions will be like the standard and poor 500 which has crossed the 2,900 mark about 30 times since January of 2017, or 2018.

Andrew Schwartz: Oh man, so we're for a ride here.

Scott Miller: You're in for a cycle here, buckle up.

Andrew Schwartz: Buckle up?

Scott Miller: Yeah.

Andrew Schwartz: All right. Let's turn to Japan quickly. What happened with Japan? Japan, that's a good news story, right?

Bill Reinsch: Well, maybe. It does reveal the tendency, I think, which transcends this administration to announce things before they're finished. In trade agreements that's dangerous. When they say we've reached an agreement in principle, what that means is we haven't agreed on the fine print yet.

Andrew Schwartz: That's not an agreement, right.

Bill Reinsch: There's a good bit of fine print in this beginning with will the Japanese get a commitment from Donald Trump not to impose automobile tariffs?

Andrew Schwartz: It's a big one.

Bill Reinsch: He has not said that he's committed to that. After the Mexican episode, which I put great stock in, where here's a case where we negotiate an agreement, painfully, sign it, and six months later he declares across the board tariffs on Mexicans, because of something completely different. Then he doesn't do it, but he declares it. Anybody watching that is going to say, "Why do I believe him?"

Scott Miller: But we've got to be prepared to cope with the difference in language between what the President says and what people, particularly in Washington who are in the trade business, hear. What we hear, a US Japan trade agreement. We see a stack of papers about 18 inches high with all kinds of detailed commitments and obligations that are mutually agreed and mutually reinforced. We see a lot of complexity. The President sees a deal. He's got a deal probably on a few products nobody really knows. The headlines are about a few products.

Bill Reinsch: Beef and pork.

Scott Miller: Beef and pork. We know there's not going to be zero tariffs on automobiles. The 2.5% tariff stays in place apparently, but we don't know any of the parameters. That stack of papers is not going to suddenly materialize. What the President wants to do is he wants deals. He does not want comprehensive trade agreements.

Andrew Schwartz: Does this thing stack up to the TPP or what?

Scott Miller: Oh, no.

Andrew Schwartz: Not at all?

Scott Miller: Apparently not.

Andrew Schwartz: It's just a smaller bilateral-

Bill Reinsch: Yes, but don't sell it off completely because the inclusion of digital trade language is important and useful. It's probably gold standard language. If it came from USMCA, or it's USMCA plus, and it's a good thing, but it's not comprehensive.

Scott Miller: Will there be coverage of services? We don't know. Will there be a chapter on investment? We don't know, probably not. Will there be chapters on conformity assessment and regulation? We don't know, to be determined.

Andrew Schwartz: When are you guys going to get the actual details on this and be able to geek out on it?

Scott Miller: Well, I'm counting on a Chairman Grassley and a Chairman Neal to demand it fairly soon.

Andrew Schwartz: Yeah, that's got to be coming.

Bill Reinsch: I think, well, they're not going to get anything until after UN General Assembly time when it's something that's signed or announced. I think, the big reveal is being delayed until Abe and Trump meet in New York at the end of September. Even then, I mean, I don't think there's going to be an agreement unless Abe gets what he wants on autos. And so, you can raise the question is anybody going to believe anything that the president says? But if he doesn't say it, I don't think there's going to be an agreement anyway.

Andrew Schwartz: Well, we'll have to watch that one too and wait for the fine print.

Scott Miller: Yes.

Andrew Schwartz: To be continued. Guys, it's good to be back. School is in and we'll have to watch out for the traffic.

Bill Reinsch: Indeed.

Andrew Schwartz: To our listeners. If you have a question for the Trade Guys, write us at tradeguys@csis.org. That's tradeguys@csis.org. We'll read some of your emails and have the trade guys react to it. We're also now on Spotify, so you can find us there when you're listening to the Rolling Stones, or you're listening to Tom Petty, or whatever you're listening to. Thank you, Trade Guys.

Scott Miller: Thanks, Andrew.

Andrew Schwartz: You've been listening to the Trade Guys, a CSIS podcast.