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How Trump's Wall could beckon a global trade war

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President Donald Trump's plans to pay for a Mexican border wall could trigger the global trade war he has long threatened.

A House Republican plan he embraced Thursday as a means of paying for the barrier would slap imported goods with a 20 percent tax — a levy aimed at boosting consumption of domestic products that could backfire by angering allies and upending the entire global trading system.

Longtime trading partners — not just Mexico — could retaliate, making American consumers pay more for everything from food to electronics and putting U.S. companies out of business. The so-called border adjustment tax could trigger cases before the World Trade Organization, spur other countries to slap levies on American products and put some U.S. companies at a disadvantage with international competitors.

Trump's embrace of the tax proposal comes as he moves forward with plans to shake up decades of carefully negotiated agreements that bind the global economy together. On Monday, he pulled out of the Trans-Pacific Partnership — a sweeping trade deal among Pacific Rim nations — and reaffirmed his intention to reopen the North American Freee Trade Agreement. Then, on Thursday, a spat with Mexican president Enrique Peña Nieto over Trump's claim he would force Mexico to pay for the border wall escalated to the point that Peña Nieto canceled a trip to the U.S. to meet with Trump next week.

"Would they retaliate immediately?" asked Dan Ikenson, director of the trade policy center at the free-market Cato Institute, referring to the response of trading partners to the border tax plan. "In the age of Trump, governments may not have the manners that they once had and may just unilaterally go after U.S. products. That's quite possible."

By raising the cost of imported goods, the tax would push Americans away from buying products that come from outside the United States — from avocados, which are heavily sourced from Mexico, to cheap household appliances shipped in from China and sold at Wal-Mart. The resulting hit to the economies of foreign nations that depend on the massive American marketplace to gobble up their goods could prompt those governments to retaliate.

And their methods could take myriad forms.

They could launch trade enforcement cases at the World Trade Organization — an option that could take years and still not be successful, given the likelihood that lawmakers would try to write the tax in such a way as to fall within the global trading body's regulations.

Or foreign countries, especially larger U.S. trading partners that would bear the brunt of the lost sales, could move to retaliate against the United States outside the WTO system. That includes China, which accounted for about 22 percent of the $2.25 trillion in U.S. imports in 2015, and Canada and Mexico, which represented slightly more than 13 percent apiece.

Mexico, as the United States' third-largest trading partner, could disrupt the trading system by levying a reciprocal tax on imports of American goods, an idea that some mainstream Republicans are already warning against.

"Any tariff we can levy they can levy," Sen. Lindsey Graham (R-S.C.) posted on Twitter on Thursday evening. "Huge barrier to econ[omic] growth."

But Mexico — or other trading partners — could try to punish Trump and other supporters of the tax by targeting goods in politically sensitive areas, said Gary Hufbauer, a senior fellow at the Peterson Institute for International Economics.

"The Mexican minds will be thinking about what they could do that would give President Trump the most pain in his political base," he said, adding that that might mean "stopping imports of certain products made in Indiana or Michigan or wherever."

And they could go after areas not directly associated with legal trade.

"They can do all sorts of things we don't like," Hufbauer said. "They can legalize marijuana. They can legalize cocaine. They can stop cooperating with the U.S. with respect to refugees from Guatemala, Honduras and so forth."

The plan, which would target imports while allowing tax-free exports, would boost the value of the dollar, giving customers more purchasing power to manage the higher costs, supporters say.

But some say the costs of the tax would hit wallets immediately, well before the value of the dollar rises: The levy on imported agricultural products, for example, would mean that a $100 grocery bill for a shopping cart full of bananas, mangoes and other produce not grown within the United States would rise to $120.

But Americans could mitigate the rise in costs simply by changing what they buy, Ikenson said. "If we import oranges but we produce our apples domestically, apple prices are going to go down and orange prices are going to go up."

And proponents maintain the costs would even out eventually, even with what Ikenson called a likely "adjustment period" at the start.

Ways and Means Committee Chairman Kevin Brady, the top tax writer in the House and a supporter of the plan, told Fox News in an interview Thursday night that he was “convinced this world economy recognizes changes.

“We will strengthen our made-in-America exports,” Brady said. “Our dollar will appreciate. Imports — you will be buying more of them at a lower price. I think it balances out in a major way.”

Businesses could protect consumers from the higher prices by swallowing the costs themselves — but those that are heavily dependent on imports, particularly small businesses and retailers, say they won’t be able to handle the adjustment.

“We’re sort of a poster child for victims of this,” said Rick Woldenberg, chief executive of Learning Resources, a small Illinois company that manufactures educational toys in China and sells them in 80 countries around the world. “We’re in a cutthroat business.”

“I’m in favor of tax reform. Come on, this is obvious,” Woldenberg said during a discussion Thursday on the Republican plan hosted by the Washington International Trade Association. “But 97 percent of American importers are small businesses, [companies] with under 500 employees. ... Small businesses are in the center of the bulls eye in this law.”