

Why Donald Trump's steel trade war is just the start

Geoff Winestock

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History shows that, with a bit of common sense, trade spats like the steel and aluminium tariffs Donald Trump has announced can be contained. But the question is whether Trump is listening to history.

We have been here before. In March 2002, exactly 16 years ago, the George W. Bush administration imposed penalty tariffs of 8 to 30 per cent on steel imports. It was a transparent tactic to shore up the Republican vote in blue-collar swing states ahead of the mid-term elections.

That traumatised US steel consumers and set off a global chain reaction. All the steel that was locked out of the US flooded onto other markets. The EU and other countries, including Australia, sought protection action against these import surges and imposed tariffs of their own.

It took a while but Bush eventually saw reason. The tariffs were supposed to last three years but the European Union, New Zealand and six other countries immediately protested in the World Trade Organisation and the EU published a hit list of \$US2.2 billion of imports from the US, including Harley-Davidson motorcycles and bourbon, against which they promised to retaliate.

By November 2003 the WTO ruled that the US was in breach of WTO rules and a few days before the EU retaliation was to take effect the US buckled and dropped the tariffs.

The Howard government – which convinced the Bush White House to exempt about 70 per cent of our steel exports, especially after we backed the US war against Iraq – did not join the case against the US tariffs in the WTO but cheered when they were lifted.

It was disruptive, especially in the US, where 16 per cent of manufacturers said they had decided to start buying some finished products with a high steel content offshore. But overall it was seen as a victory for the world trade system.

The optimistic view is that things will play out this time in a similar way. Trump on Thursday night, in announcing the measures, said he would "do something" for his loyal ally Australia.

Optimists also point out that Australia has less to fear from a flood of diverted steel this time because, under pressure from BlueScope and OneSteel, it has already erected tariff barriers against many countries using so-called anti-dumping measures. Australia talks free trade but it has become the fifth biggest user of protectionist anti-dumping actions in the world according to the WTO.

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The head of the Anti-dumping Commission, which will have the task of stopping a surge of diverted steel, flew to the US this weekend with BlueScope and OneSteel where he might be able to work out a strategy.

"A lot of steel products are covered by anti-dumping measures already. I think the risk of diversion is relatively minor," says Andrew Hudson, a trade lawyer for Rigby Cooke.

Optimists will hope the dispute will be resolved this time by the WTO, just like in 2003. The US will eventually back down just like Bush.

But that does not take account of Trump's protectionist America First agenda. Unlike Bush, who was a free trader and a believer in alliances, Trump hates the idea that America is bound by any prior trade deals or even that the US might, from time to time, run a trade deficit.

A report by the US-based Peterson Institute for International Economics estimated that if Trump implemented all the things he has talked about, including withdrawal from NAFTA and a 45 per cent tariff on China, it would cost 4.8 million US jobs and cut US investment by 15 per cent.

In 2002 the US steel tariffs were clearly a matter the WTO could handle. The US claimed they were temporary "safeguards" against a surge in imports and actually complied with WTO rules. In fact, imports weren't surging, which is why the US lost its WTO case.

This time, however, knowing it has no case under normal WTO rules to strike at Canada or Germany, the US has invoked a completely untested, unprecedented and quite bizarre WTO provision allowing protectionism for "national security". It is not clear if a case could even be heard. Because this is supposedly about hush-hush national security, WTO rules say the US can even refuse to disclose the secret report on which steel tariffs are based.

Daniel Ikenson of the pro-free trade Cato Institute in the US warns Trump's reliance on national security as a trade weapon will open up a Pandora's Box. "Beijing certainly sees its dependence on foreign semiconductors and other technologies to represent a threat to China's national security. Trump's restrictions on steel or aluminium could give license to the Chinese government to harass, compel technology transfer, and discriminate against foreign companies on a grand scale under the rubric of protecting national security."

Trade war concerns

Because they think the US national security is clearly an abuse of WTO processes, EU, Canada and now China have threatened to retaliate immediately without waiting for a court case. China last month also "coincidentally" opened an anti-dumping investigation into \$US1 billion of US sorghum exports, which is theoretically unrelated to the steel issue but hangs in the air.

Gary Hufbauer, senior fellow of the Peterson Institute, says unilateral retaliation would break WTO rules but the dilemma for the rest of the world is that if Trump is able to raise tariffs on steel with impunity it will only empower him to go further. "Trump will say look, 'We won!' He is already tweeting about it."



Hufbauer believes Trump can only be stopped in two ways. First, the Republican majority in Congress, frightened by retaliations and the disruption to US steel and aluminium consumers, will force more carve-outs and exemptions, similar to those Trump has already offered to negotiate.

Or financial markets crash in fear of major damage to the global economy. The steel tariffs have not worried markets too much but Hufbauer says Trump's next moves against China could turn markets sour. Trump has demanded that China reduce its annual trade surplus with the US by \$US100 billion a year, which is about seven times more than the US steel and aluminium imports at stake in this dispute. And Trump is talking about some broad measures that will punish China for alleged breaches of intellectual property. A China-US trade war is the big worry.

"This could turn into a very big shock for the global economy," Reserve Bank of Australia governor Phil Lowe said this week.

Yet if Trump wants to fight China it is not clear why he has started by attacking some of his closest allies. Instead of building a coalition against Chinese protectionism, he has started a fight with like-minded countries such as Canada and the EU and is antagonising South Korea at a time he wants to pressure North Korea over the nuclear issue.

"Geopolitically this is a disaster. It makes no sense to antagonise close allies," says Hufbauer.

The whole system of interrelated trade deals including the WTO is at risk, including perhaps the Trans-Pacific Partnership with countries such as Mexico that Australia has just signed. If Mexico, a major supplier to the US, diverts its steel to Australia and Australia imposes anti-dumping duties Mexico could complain even before the TPP comes into effect. The US is already threatening to withdraw from NAFTA and a free trade deal with Korea, which could cause a cascade of other trade shockwaves.

It is not clear how far Trump will push or whether this is all just bluster and noise. Lowe seemed to argue this week that Trump should be left to burn himself out. "The best thing for everyone to

do, and perhaps the hardest thing to do, is just to sit still and do nothing, to not respond and just advocate for a rules-based international trading system," Lowe said.

But a lot depends on Trump himself and he seems indifferent to the lessons of history. At a meeting last month one Republican senator asked him if he agreed that Bush's tariffs in 2002 had done more damage to the broader American economy than the temporary help they gave to US steel makers. Trump replied mysteriously: "It didn't work for Bush, but it worked for others."