



Trump Starts a New Trade Fight in the Middle of an Old One

Keith Johnson

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The surprise threat by U.S. President Donald Trump to levy increasingly high tariffs on Mexico, coming on top of a worsening trade war with China, could undermine growth prospects in the United States and globally—just in time for Trump’s reelection battle next year. Beyond that, Trump may well be jeopardizing his coveted replacement for the NAFTA trade deal, as well as all the other major trade agreements the administration hopes to clinch with China, Europe, and Japan.

All in all, experts say, a perfect storm of economic headwinds may be brewing just in time for the 2020 election season.

Trump announced late Thursday that he would slap tariffs—starting at 5 percent and rising every month to reach 25 percent—on all Mexican imports until Mexico curbs illegal immigration into the United States. The tariffs, which the administration hopes to apply using a decades-old emergency powers provision, are slated to start on June 10, giving both countries a little time to walk back from the brink.

Mexican President Andrés Manuel López Obrador is certainly trying. In a conciliatory press conference Friday morning, coming on the heels of a letter he sent Trump late Thursday, López Obrador said he hoped to convince U.S. officials that Mexico is taking steps to secure its border and would hold off on taking legal or economic reprisals against the United States while seeking a negotiated solution.

But Trump’s surprise announcement came the same day that the Mexican Senate began deliberating on the new United States-Mexico-Canada Agreement (USMCA), Trump’s slightly modified NAFTA that he hopes to pass this year and get ratified by all three countries. Though López Obrador said the law is still being studied despite the tariff threat, Trump’s new trade war doesn’t seem calculated to win political support in Mexico (or among House Democrats) for USMCA.

“The whole point of being part of USMCA is to prevent actions like this,” said Simon Lester, a trade expert at the Cato Institute. “If the tariffs do go into effect, I don’t see how the Mexican Senate can approve it.”

Meanwhile, China, Europe, and Japan are watching. All are currently in trade talks at some level with the United States, and all are learning that for the Trump administration, no deal is ever binding.

“If anything, this should strengthen Chinese resolve, as it seriously diminishes the chances of the United States forming an effective anti-China coalition,” said Phil Levy, an expert on trade and the global economy at the Chicago Council on Global Affairs.

“I imagine Japan and the EU must be watching the Mexican episode and thinking they will be next. It’s not hard at all to see what the next pretext will be,” he said. The Trump administration is still brandishing the threat of sweeping tariffs on cars and car parts that would be especially painful for Japan and the European Union. “This will disabuse them of any notion that a trade deal with the Trump administration buys more than a brief peace,” he said.

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Even though the Mexico tariffs for now are just a threat—and Trump has repeatedly used the threat of tariffs to browbeat other countries without actually pulling the trigger—global stock and bond markets shuddered, with shares in firms exposed to U.S.-Mexico cross-border trade (like General Motors, Toyota, and Hyundai) especially hard-hit. Investors are realizing that trade tensions aren’t limited to the battle between the United States and China and could have a much bigger contagion effect on a global economy already facing plenty of headwinds.

The University of Chicago trade expert Robert Gulotty says the global trading system will likely survive, though it has never before had to fend off the country that built it.

As the U.S. trade war with China escalates, a growing number of GOP lawmakers want final say on tariffs.

The economic impact—and political future—of the '94 trade deal's successor is utterly unclear.

“There was a school of thought that the president was resolving other disputes so he could focus on the China trade war,” said Levy, who was a trade advisor in the George W. Bush administration. “This shows an eagerness to open up another front in a broader trade war. As such, it strongly suggests that it is primarily protectionism motivating these trade wars, rather than some particular security concerns about China.”

So far, much of the U.S. economy has been insulated from the trade war with China—in part because some imports have instead come through Mexico. But with the broadening of the trade war, things could start to get real, with potentially serious economic consequences at a time when Trump is banking on a healthy economy to offset his dismal approval rating. The United States and Mexico have a two-way trade of about \$1.7 billion every day, and many U.S. firms are utterly reliant on goods from Mexico to make their finished products, especially cars and car parts.

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Levying import duties under the International Emergency Economic Powers Act (IEEPA) as a way to pressure Mexico to change its migration policies has plenty of problems, beyond the higher taxes U.S. consumers and businesses may have to pay for cars, machinery, clothing, and agricultural goods. One big problem is that the move may be illegal, and it is certainly in violation of existing free trade deals the United States has with Mexico and Canada.

IEEPA is generally used to apply economic sanctions and seize assets from countries deemed a threat, such as in the wake of the 1979 Iranian hostage crisis. The statute doesn't explicitly authorize the president to levy duties on imports, which might be why no president has ever used IEEPA to raise tariffs.

Congress could override the president's decision with a joint resolution—at a time when lawmakers are already poring over several bills meant to wrest back trade authority from a tariff-happy president. Those bills had languished for two years, but the salvo launched at the biggest U.S. trading partner might be enough to spur lawmakers from both sides into action.

"I always thought there were red lines the administration couldn't cross" when it came to using national security excuses to disrupt trade, Lester said. "This is the kind of thing that could get Democrats and Republicans together—if anything could do it, it's this."

At the same time, if the Trump administration is seeking to stem flows of impoverished people across the border, making the Mexican economy and employers there less competitive likely isn't the best approach, as experts keep pointing out—especially when the Trump administration just slashed aid for the Central American countries that are at the root of the exodus in the first place.

But Trump's Mexican tariffs, if he follows through, could have even more worrisome longer-term consequences. U.S. relations with Mexico had reached something of a nadir in the 1980s, which NAFTA helped fix a decade later by closely integrating the two economies. By the early 20th century, decades of bad blood, wars, invasions, annexations, and expropriations had largely been put to rest. Now, if the tariffs go into effect, that could all be at risk.

"This could really derail the relationship. I was part of a generation that reset relations" thanks to the original NAFTA, said Antonio Ortiz-Mena, a Mexican trade negotiator who worked on the first NAFTA. "If this goes through, this could have a severe and long-lasting impact on U.S.-Mexico relations," especially among older and younger Mexicans who feel the United States has again "betrayed them."

There could be even worse in store if the tariffs are ultimately imposed, said Ortiz-Mena, now at Albright Stonebridge Group, a consultancy. Historically, Mexico has been more of a competitor than a partner with China, especially when its economic lifeblood was tied up with the United States. But Mexico's new, left-wing president is eager to fulfill ambitious campaign promises of sweeping economic development and may start glancing across the Pacific rather than across the Gulf of Mexico.

"López Obrador wants an oil refinery, he wants high speed trains in Yucatán, he wants infrastructure investment, he wants a logistics corridor from the Pacific coast to Veracruz. Now, who can do that?" Ortiz-Mena said.

“This pushes Mexico right into the arms of China. From that strategic perspective, it’s one of the most counterproductive moves that could be made.”