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# U.S. Deficit With China Climbs on Eve of Trade War

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The U.S. and China are now embroiled in what Beijing has dubbed the "largest trade war in economic history" as President Donald Trump's long-threatened series of tariffs went into effect overnight, prompting a swift response from Asia's largest economy.

America's trade deficit with China, however, has continued to expand in recent months, leaving U.S. consumers who are buying increasingly more Chinese goods than the other way around vulnerable to price increases and American exporters eager to break into the Chinese market in the crosshairs for international retaliation.

Effective at midnight Thursday, the U.S. imposed duties of 25 percent on $34 billion of Chinese goods – with China immediately responding with accusations that the U.S. violated standards recognized by the World Trade Organization. Beijing also announced the implementation of its own tariffs on American shipments, hitting key U.S. agriculture exports such as soybeans and poultry.

"Both sides are currently spiraling towards a conflict that could drag down the entire global economy," Nick Marro, an Asia analyst at The Economist Intelligence Unit, said in a statement Friday. "However, the fact that the Chinese tariffs, and tariffs from the [European Union] and other markets, are targeting U.S. agriculture means that political pressure in the U.S. might be too much for Trump to bear before the midterms. There's still a very slim chance that both sides could press pause before things get any worse."

China is just the latest international trade partner to take issue with trade barriers and shakeups implemented by the Trump administration. EU officials have lashed out against plans to raise tariffs on foreign automobile imports to the U.S., and Canada and Mexico are embroiled in monthslong North American Free Trade Agreement renegotiations – despite the Trump administration's efforts to enact tariffs on steel and aluminum products imported from America's neighbors to the north and south.

The skirmishes have left China, which is exhibiting growing influence over the global economy, positioning itself as a champion of the rules-based international system and economic globalization, according to Louis Kuijs, head of the Asia Economics division at Oxford Economics.

"China hopes to get other global parties, including Europe and international business, on its side as the Trump administration seems ready to fight trade wars on multiple fronts," Kuijs wrote in a research note Friday.

In a statement, China's Ministry of Commerce on Friday accused the U.S. of using "bullying" tactics, "hindering the pace of global economic" growth. Beijing also vowed to take its case before the WTO, the international commerce body that Trump earlier this week threatened to withdraw from "if they don't treat us properly."

Trump's primary gripe with the WTO is that China is still technically recognized as a developing country, largely due to rampant poverty, granting it some exemptions that the U.S. and other "developed" countries cannot access. His main complaint about China – and about many of America's trade partners – is that the U.S. maintains a deficit in goods. But that complaint ignores the services trade in industries like education, tourism and entertainment in which America maintains a surplus.

But to this point in his presidency, America's goods deficit with the rest of the world has ballooned rather than eroded. Through the first five months of 2016, the Census Bureauestimated the U.S. maintained a $300.1 billion deficit with the rest of the world. But at the end of May 2017, that total had climbed to $327.1 billion before jumping to nearly $350.3 billion through the first five months of 2018.

Imports from China, in particular, have jumped during the Trump administration, with America's trade deficit in goods with that country hitting nearly $167 billion between January and May, up more than $14.5 billion year over year.

Bill Adams, a vice president and senior economist at The PNC Financial Services Group, suggested that U.S. manufacturers that compete against Chinese imports will benefit domestically from the tariffs. But he said that industries that rely on Chinese goods and companies caught up by Chinese retaliation will see "larger, albeit more diffuse, negative effects."

"The longer tariffs last and the wider they become, the more they will dampen hiring and investment by U.S. businesses engaged in global value chains," Adams said in a statement Friday.

The U.S. is now in relatively unfamiliar territory post-World War II – engaged in trade disputes with several of its closest allies and biggest international commerce partners in a series of conflicts that threatens to upend a trade system the U.S. played an integral role in constructing.

"In the long run, the largest potential cost of the tariffs is the risk that U.S. trading partners give up on the current system of world trade, whose rules were largely set by the United States, for alternatives that disadvantage American workers, businesses, or security interests," Adams said. "The U.S. export market's size would make this a costly choice, but not an impossible one: The U.S. today accounts for about a fifth of global GDP at market exchange rates, far less than the half it accounted for after World War II when the rest of the global economy was in tatters."

China in recent years has been proactive in reaching out to international partners to create a more Sino-centric trade landscape, playing proactive roles in the BRICS group of developing economies that also includes Brazil, Russia, India and South Africa, and in laying out a new Silk

Road commerce initiative that would beef up trade infrastructure along a route stretching through the Middle East to Europe.

In some cases, they have also appeared to play those ties to other countries against the U.S., recently slashing duties on soybeans and other agriculture products from nearby countries like India – effectively cutting into U.S. market share and limiting what U.S. farmers will be able to recoup in lost business even if the ongoing trade dispute ended tomorrow.

"The longer tariffs persist the more China will seek to strengthen its supply relationships with other partners and the less likely the U.S. is to regain market share," Dec Mullarkey, managing director of investment strategies at Sun Life Investment Management, said in a statement Friday. He also noted that investors spooked by the trade tension will likely buy up the dollar in search of stability – a development that would strengthen the greenback and mean U.S. exporters would face unfavorable exchange rates.

On some of his gripes related to China, in particular, Trump's administration has made points that have resounded with U.S. politicians on both sides of the aisle. Particularly as it relates to controversial Chinese intellectual property practices, Trump's condemnation of Beijing has found support among domestic lawmakers and officials in the EU and elsewhere who have previously complained about the hoops foreign companies have to jump through to do business in China.

But Trump has found bipartisan condemnation for stoking a trade war with China – and sparking disputes with international allies who under normal circumstances could help the U.S. apply pressure.

"Unfortunately, President Trump's dangerous misconceptions about the purpose and mechanics of trade have made him willing to play roulette with an economy that is otherwise thriving," Daniel Ikenson, director of the Stiefel Center for Trade Policy Studies at the libertarian Cato Institute, said in a statement Friday. "Unless he changes course soon, the president will find the benefits of his tax reform extinguished and the unemployment rate – especially among his supporters in the manufacturing and agricultural sectors – dramatically increased."