How the Trump administration can stop the wild roller coaster of its China trade policy

Simon Lester

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After a brief interlude of "trade peace," the Trump administration is once again threatening to impose tariffs on $50 billion worth of Chinese imports. So far, the Trump administration's trade policy on China is like a wild roller coaster ride, and it is not clear the administration has a plan for how to get off.

The administration may find a better approach in a place it is unlikely to look: Nafta, which Trump has been so critical of and is trying to renegotiate. While Mexico 30 years ago and China today aren't in identical situations, there are important parallels between the U.S. trade relationship with Mexico then and China now. A trade liberalizing agreement with China could do the same for U.S.-China relations today that Nafta did for U.S.-Mexico relations back then.

Of course, a U.S.-China trade deal doesn't have to be exactly like Nafta. A U.S.-China deal could be bilateral, or regional, or multilateral. But regardless of the specific form it takes, a full-fledged trade agreement between the U.S. and China will be much more beneficial than the careening tariff threats and rumors of sectoral deals that we have seen so far.

Trade between developing and developed countries is often controversial, with both sides expressing concerns. Industries in the wealthier countries fear competition with low-wage workers, while industries in poorer countries worry about competition with high-skilled workers and lavishly subsidized companies.

With China, it is important to stay focused on the real problems in the relationship. Despite what some in the Trump administration believe, the U.S. bilateral trade deficit with China isn't a problem that needs to be fixed. Our trade deficit is caused primarily by factors and behavior that are outside of trade policy, including U.S. budget deficits, low personal savings rates by Americans, and the dollar's role as a reserve currency. At the same time, Chinese protectionism has been and remains a problem. For example, China's tariffs are around 10% on average; by comparison, U.S. tariffs are around 3.5%.

The Trump administration seems to think this tariff disparity puts the U.S. at a strategic disadvantage in negotiations. Commerce Secretary Wilbur Ross recently pointed to higher foreign tariffs as a reason other countries "have little incentive to negotiate" with the U.S.

But that's where the parallels with Mexico show a way forward. In the 1980s, Mexico was in a similar position to where China is now. Just prior to when it joined the GATT (the predecessor to the WTO) in 1986, Mexico's tariffs were around 25%. After its GATT accession, further liberalization brought these tariffs down to 13% by 1993 (much higher than those of the U.S.), just before it signed on to Nafta. And then, through the Nafta, these tariffs came down even further, as virtually all tariffs on trade between Canada, Mexico and the United States were bound at zero.

President Trump and his administration have made a big deal out of "reciprocity" in trade. While these demands for "reciprocity" sometimes feel like a call for higher U.S. tariffs, Nafta represents reciprocal free trade at its finest: A trade agreement that liberalizes trade in both directions, resulting in low, equal tariff rates.

A Nafta-like approach could work with China as well. As China began to undertake market reforms and negotiate its entry into the WTO, it lowered its average tariffs from 43.7% in 1988to 15.3% in 2001. Today its tariffs are around 10%. There is an opportunity for the United States and China to follow the same approach as the United States, Canada and Mexico did in Nafta and negotiate the rest of these tariffs away.

The current U.S. approach of issuing unilateral demands is unlikely to achieve much in terms of reducing China's protectionism, as China will find it politically uncomfortable to be seen as giving in to U.S. bullying. But a balanced deal with both sides offering something could succeed. The negotiations could cover a broader range of issues than just tariffs, with services and government procurement also up for liberalization.

In addition to these traditional areas of liberalization, new rules on state-owned enterprises should also be on the table. The Trans-Pacific Partnership has specific definitions and principles to guide the behavior of these organizations, which are prevalent in the Chinese economy. One of the long-term goals of U.S. trade policy should be to apply these rules to China, and an enforceable trade agreement is the most effective approach.

The Trump administration probably doesn't think of Nafta as a good model, as it is currently trying to unwind many of its provisions. But as the trade conflict with China drags on, and reality sets in about the flaws in the current approach, the administration may look around for new options. Vague demands and tariff threats aren't working. If the administration wants China to liberalize, the Nafta approach may be its best option.

Simon Lester is the associate director of the Cato Institute's Herbert A. Stiefel Center for Trade Policy Studies.