



US-China Trade War

Outline

- Analysis of economic data
- Background of the trade war
- Causes of the US trade deficit
- Economic impacts of the trade war
- Developing the DRQ

The background features abstract geometric shapes. The top half is divided by a diagonal line into a dark gray triangle on the left and a light gray trapezoid on the right. The bottom half is divided by a diagonal line into a light gray trapezoid on the left and a yellow triangle on the right.

Analysis of Economic Data



Data response questions

- Aim to test the ability of students to **apply their (economics) knowledge to unseen information** on statistical data, charts, line graphs and newspaper extracts and comics etc.

Analysis of Economic Data

➤ **Facts tell us something about the world, but nothing about relationships between variables.**

➤ **Economic theory** or hypothesis is to study the **causal relationship** between X and Y

- X variable **explains** (or **predicting**) Y variable, $Y = f(X)$,
- There may be **more than one X** variable.

➤ Presence of **Correlation** does **not** necessarily imply causality:

edu = f(income) or income = f(edu)?

CPI = f(PPI)? or PPI = f(CPI)? → Cost push or demand-pull inflation?

Correlation + a sensible theory suggests (but does not prove) **causality**

➤ **Correlation** itself may be **suggestive -- spurious correlation**

- **Caused by third variable:** drownings rise when ice cream sales rise ? (**Rising heat** may cause more people to **swim**, and **buy more ice cream**)
- **Non-stationary data** → cointegration?

Fallacies

➤ Post hoc fallacy

When two events occur in time sequence, the first event is **necessarily the cause** of the second event (indeed, it is not necessarily).

(鄭少秋效應?)

Skirt length “theory” in 1920s (If skirt lengths are long, the stock market is going down)?

➤ Fallacy of Composition

- What is **true for one individual** or part of a whole is necessarily true for a group of individuals or the whole, i.e., trade protection, paradox of saving
- What is **true for a group** of individuals or the whole is necessarily true for one individual or part of a whole, e.g., if all investors sold HSBC share, its stock price would fall. Therefore, if you sold HSBC share, its stock price must fall

Reference: McConnell et al. (2020)

➔ **Correlation should be based on theory**

Necessary factor

➤ Necessary factor

- If A **implies** B, or $A \rightarrow B$ or A **only if** B, or B is the necessary factor of A, we can say **if ‘not B’** then necessarily **‘not A’**.

Mother \rightarrow Female

Background Globalization of Resource Market

<https://outsourceworkers.com.au/offshoring-and-outsourcing/>

McConnell et al. (2018)

Globalization of resource market

- **Outsourcing of work abroad and Offshoring** (relocation of a business process from one country to another).
 - **Outsourcing:** car parts made in China
 - **Offshoring:** factory in China
- Economies of scale: allowing producers to **specialize in the specific steps in the production process** and increase the total production level
- Beneficial for all countries and become much more common with **technological improvements**
- Helping a firm **remain internationally competitive with lower costs** leading to **increased demand for complementary goods and jobs within the U.S.**
- **Increases flexibility** → by taking advantage of time zone differentials.

Globalization of resource market

➤ Disadvantage

- Part of the **revenue** of producing the good now **shifts** to foreign countries.
- Shifting work previously performed by American workers is now to workers in other countries, **taking away jobs from Americans and increasing U.S. unemployment**
- **Cultural and Social Differences** ➔ may have an adverse effect on productivity and communication
- **Security Issues:** (i) **Military self-insufficiency** (ii) **oversea data transmission** always at risk of security breach and compromised data integrity



Trade War

Trade War

- A trade war **occurs** when a country **imposes tariffs or quotas** on imports and foreign countries **retaliate** with similar forms of trade protectionism. It **reduces** international trade.
- A trade war **starts** when a country **aims to protect its local industry and create jobs**. With **lower relative prices**, tariffs and quotas give a **competitive advantage to local producers**, who would have **more domestic demand** from local customers and hence add more jobs.
- A trade war in the long run, however, would **depress economic growth** for all countries involved and **trigger inflation (stagflation) when tariffs cause higher import prices**.
- The Smoot-Hawley Tariff Act of **1930** raised US tariffs on over **20,000 imported goods (increased 900 tariffs by an average of 40% to 48%)**, leading to a **65% reduction** in international trade and worsen the **Great Depression**.

[https://www.thebalance.com/trade-wars-definition-how-it-affects-you-](https://www.thebalance.com/trade-wars-definition-how-it-affects-you-4159973#:~:text=A%20trade%20war%20is%20when,similar%20forms%20of%20trade%20protectionism.&text=But%20in%20the%20long%20run,increase%20the%20prices%20of%20imports)

[4159973#:~:text=A%20trade%20war%20is%20when,similar%20forms%20of%20trade%20protectionism.&text=But%20in%20the%20long%20run,increase%20the%20prices%20of%20imports](https://www.thebalance.com/trade-wars-definition-how-it-affects-you-4159973#:~:text=A%20trade%20war%20is%20when,similar%20forms%20of%20trade%20protectionism.&text=But%20in%20the%20long%20run,increase%20the%20prices%20of%20imports).

The Fallacy of Protectionism

Frederic Bastiat, a French economist (1801-1850)

- a. The candle makers petition the government to relieve them from the “foreign” competition of the sun, arguing that the sun provides light at lower prices than which the candle makers can offer.
- b. The petition further argues that **shutting out all-natural light will stimulate industries** that support the candle industry.



Timeline of the US-China Trade War

Trade friction

Krugman et al (2012)

Trade friction arises if countries (or trading blocs) implement protectionist trade policies.

Gengyan Tang (唐耕砚，四川省社会科学院新闻与传播研究所)

Trade friction is a **dynamic game process** between the two sides of trade

Joseph Stiglitz:

- **Intense** trade frictions will result in the **current account deficit** of a country with its trading partner **exceeding 1.5%** of the GNP.
- If the current account deficit of a country with its trading partner **exceeds 2%** of the GNP, it will lead to **retaliatory actions** from the deficit country.
- If a country's **trade surplus** with another **exceeds 25– 30%** of its trade volume, however, the problem is a **political** one instead.

Timeline

June 28, 2016

While **campaigning for the White House**, Trump laid out plans to counter “**unfair trade practices from China**” and threatened to apply tariffs under **sections 201 and 301** of U.S. trade legislation, which he subsequently did. **He said China’s entrance into the World Trade Organization** enabled the “**greatest jobs theft in history.**”

Section 201 of the US Trade Act of 1974—allows the President to impose **temporary duties and other trade measures** if the International Trade Commission (ITC) determines **a surge in imports is a substantial cause or threat of serious injury to a U.S. industry.**

<https://www.everycrsreport.com/reports/R45529.html#:~:text=Section%20201%20of%20the%20Trade,injury%20to%20a%20U.S.%20industry.>

Section 301 of the US Trade Act of 1974— authorizes the President to take all appropriate action, **including tariff-based and non-tariff-based retaliation**, to obtain the removal of any act, policy, or practice of a foreign government that **violates an international trade agreement** or is unjustified, unreasonable, or discriminatory, and that burdens or restricts U.S. commerce. https://en.wikipedia.org/wiki/Section_301_of_the_Trade_Act_of_1974

March 31, 2017

Trump signed two executive orders. One called for **tighter tariff enforcement** in anti-subsidy and anti-dumping trade cases. The other ordered a **review of U.S. trade deficits and their causes**.

April 7, 2017

Trump and Xi Jinping agreed to a 100-day plan for trade talks.

June 2017

Trump initiated a '**Section 232** investigation', for reasons of national security, on the import of steel and aluminum. Considering the huge production capacity of steel and aluminum in China, the investigation and the following additional tariff were believed to be targeting China.

Section 232 of the Trade Act of 1962 authorizes the President to **impose imports restrictions** on products, imported into the United States "**in such quantities or under such circumstances as to threaten to impair the national security**".

July 19, 2017

The US and China failed to agree on new steps to reduce the U.S. deficit with China after the 100 days of talks.

August 14, 2017

Trump ordered “**Section 301**” probe into alleged Chinese intellectual property theft, described as his **first** direct trade measure against Beijing

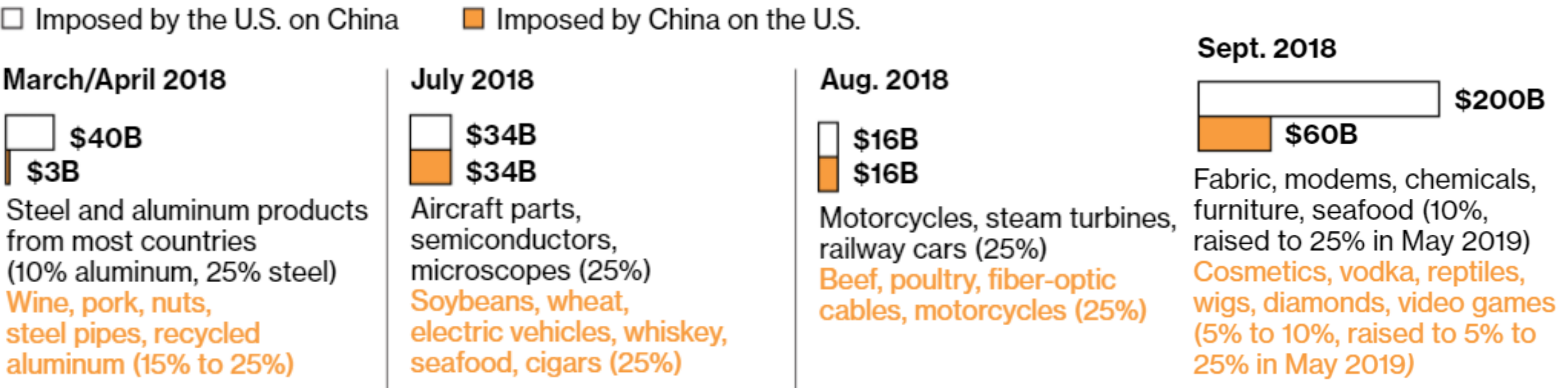
January 22, 2018

The US government-imposed safeguard tariffs on large residential washing machines, as well as solar cells and modules (not just those from China). These conflicts have engendered a full-fledged trade war.

Since March 2018

Tariffs, by percentage rate, imposed by the U.S. and China on each other

The US-China **trade war started** on 6 July 2018, when the US imposed a 25 per cent tariff on US\$34 billion of Chinese imports. In response, China made countermeasures on the same day and imposed a 25% additional tariff on imports from the US worth US\$ 34 billion, including soybean.



<https://www.bloomberg.com/news/articles/2020-09-15/wto-rules-that-u-s-tariffs-on-china-violate-trade-rules-kf4189y0>

December 1, 2018

The US and China agree on a **90-day halt** to new tariffs. Trump agreed to put off the January 1 scheduled increase on tariffs on \$200 billion of Chinese goods until early March while talks between the two countries take place. China agreed to buy a “very substantial” amount of U.S. products.

February 24, 2019

Trump extended the March 1 deadline, leaving the tariffs on \$200 billion of Chinese goods at 10% on an open-ended basis.

May 8, 2019

The Trump administration gave formal notice of its intent to raise tariffs on \$200 billion of Chinese imports to 25% from 10%, effective May 10.

June 18, 2019

Trump and Xi spoke by phone, and the two sides agreed **to rekindle trade talks** ahead of a planned meeting between the two leaders scheduled for the Group of 20 (G20) summit in Japan at the end of June.

June 18, 2019

At the G20 meeting in Osaka, the United States and China formally agreed to **restart trade talks** after concessions from both sides. Trump agreed to **no new tariffs and an easing of restrictions on** Chinese telecom powerhouse **Huawei Technologies Co. Ltd.** **China agreed to** unspecified **new purchases of U.S. farm products.**

August 1, 2019

Trump said China had not followed through on a promise to buy more U.S. farm products, he announced 10% tariffs on \$300 billion worth of Chinese imports, in addition to the 25% already levied on \$250 billion worth of Chinese goods. Trump said the talks between Washington and Beijing would continue despite the new tariffs, and that the rate could be increased above 25 percent in stages.

August 6, 2019

The People's Bank of China, said Beijing had not and **would not use the yuan to respond to trade frictions.**

August 9, 2019

Trump said he was not ready to make a deal with Beijing and suggested he may cancel in-person trade talks with China scheduled for Washington in September.

August 23, 2019

China announced that it would impose additional retaliatory tariffs against about \$75 billion worth of U.S. goods, putting as much as an extra 10% on top of existing rates in response to the U.S. tariffs announced earlier in August.

August 25, 2019

China's top trade negotiator Vice Premier Liu called for calm amid the recent escalation of trade war threats. **Trump said talks would proceed.**

September 1, 2019

Tariffs came in force as scheduled. The US began implementing tariffs on more than US\$125 billion worth of Chinese imports (list 4A) starting Sunday.

September 2, 2019

China lodged WTO tariff case against the US.

September 5, 2019

China and US agreed to 13th round of trade talks

□ Imposed by the U.S. on China

■ Imposed by China on the U.S.

Sept. 2019



Agricultural products, antiques, clothes, kitchenware, footwear (15%, dropping to 7.5% under an agreement announced Dec. 13 in which China promised a “corresponding” amount of tariff rollbacks)

Agricultural goods (5% to 10% on top of existing tariffs ranging up to 25%), crude oil (5%)

September 11, 2019

China unveiled **tariff exemption list for US imports**. China announced that it would exempt 16 types of US imports from additional tariffs.

September 19-20, 2019

US-China mid-level trade talks in Washington

September 20, 2019

US released new tariff exemption lists, which exempt over 400 Chinese goods from tariffs

October 11, 2019

US and China reached a “Phase 1” agreement. **China** would reportedly **purchase US\$40-50 billion in US agricultural products annually, strengthen intellectual property provisions, and issue new guidelines on how it manages its currency.** **Trump announced that the US would delay a tariff increase scheduled to go into effect on October 15.**

October 18, 2019

US tariff exclusion process for US\$300 billion of Chinese imports. The US announced tariff exclusion for certain Chinese products starting October 31, 2019 through to January 31, 2020.

The exclusion process will apply to Chinese products that were subject to an additional 15 percent tariff through the August 2019 action under Section 301, in effect since September 1, 2019.

November 1, 2019

The WTO said China could impose compensatory sanctions on US imports worth US\$3.6 billion for the US failure to abide by anti-dumping rules on Chinese products. The announcement centered on a WTO case that originated nearly six years ago, long before the trade war.

According to news sources, the US was disappointed in the decision and a US official responded by saying that the arbitration panel “overstates the amount of the impact on China” and that the WTO’s approach had “no foundation in economic analysis.”

November 7-8, 2019

The US and China have, in principle, agreed to discussing rolling back tariffs on each other's goods in phases. This will be done in the same proportion and simultaneously, once the two sides sign a “phase one” deal, according to China's Ministry of Commerce.

November 26, 2019

US released new regulatory guidelines for its telecom networks procedure to protect telecom networks from national security threats.

December 13, 2019

China and the US agreed to 'phase one deal' just before next tariff

China released second set of US products to be excluded from additional tariffs.

January 13, 2020

US officially dropped China's currency manipulator label

January 15, 2020

US, China signed phase one trade deal will cut US tariffs and boost China's purchases of US products.

February 7, 2020

China announced would halve tariffs on US\$75 billion worth of goods, in line with phase one deal

February 17, 2020

China granted tariff exemptions on 696 US goods to support purchases

February 21, 2020

China unveiled new tariff exemption lists for US imports

May 8, 2020

China and the US reaffirmed their phase one trade deal commitments over the phone

May 12, 2020

China announced new list of US commodities excluded from tariffs from May 19, 2020 to May 18, 2021

July 14, 2020

China booked record deal for US corn

July 22, 2020

The US sought public comments to exclude Chinese imports from Section 301 tariffs

August 15, 2020

The US and China postponed trade deal review

August 20, 2020

China said trade deal review to be rescheduled

August 25, 2020

The US and China held trade talks, act optimistic on phase one trade deal

15 September 2020

WTO said Trump's tariffs violated several global rules, including a provision that requires all WTO members to offer equal tariff rates among the body's trading partners.

Robert E. Lighthizer, the United States Trade Representative, blasted the World Trade Organization for trying to prevent the United States from helping its own workers. "This panel report confirms what the Trump administration has been saying for four years: The W.T.O. is completely inadequate to stop China's harmful practices. "Although the panel did not dispute the extensive evidence submitted by the US of intellectual property theft by China, its decision shows that the W.T.O. provides no remedy for such misconduct."

W.T.O. Said American Tariffs on China Broke Global Trade Rules

<https://www.nytimes.com/2020/09/15/business/economy/wto-trade-china-trump.html>

Background

Lesson from US-Japan trade conflicts

<https://news.cgtn.com/news/2019-07-11/Lessons-from-U-S-Japan-trade-war-of-1980s-IcWJh9RjAQ/index.html>

US trade deficit with Japan

- According to the **U.S.-Japan Security Treaty** signed in **1951**, the US had strict military control over Japan and political as well as diplomatic influence.
- After WWII, **Japan kept upgrading its industrial sectors**, also managed to capitalize on its edge in R&D investment and product quality to rapidly **expand its presence in the US market and outcompete American companies**.
- Japan's **export to the US** skyrocketed, such that the **U.S. had a trade deficit** with Japan for the **first time in 1965**.
- Japan “were forced to” sign a series of **voluntary export restrictions (in 1981)** on **agricultural products, textiles, steel, color televisions, automobiles, and semiconductors**
- Japan also opened up key markets such as **color TVs and automobiles** to the U.S., **signed trade liberalization agreements on beef and oranges** with the U.S., and relaxed restrictions on circulation.

Plaza Accord (廣場協議)

- The **1985 Plaza Accord** (廣場協議) : An agreement among the G-5 nations—France, Germany, the United States, the United Kingdom, and Japan—to **manipulate** exchange rates by depreciating the U.S. dollar relative to the Japanese yen and the German Deutsche mark.
- In **1987**, the US **trade deficit** reached **US\$56.7 billion** against Japan. It was around **1.2% of the US GDP** that year. (From 1985 to 1995, the US trade deficit with Japan accounted for **30–50% of the overall US trade deficit**)

Japanese companies grow up

- **Japanese companies grow up**

- ✓ E.g. Mitsubishi Real Estate from Japan purchased the historic American landmark Rockefeller Centre in 1989.
 - ✓ E.g. president of Japan's Sony Corporation, Akio Morita, published the **book “Japan Can Say No”**, reflecting the public sentiment in Japan towards the need to **improve its international status**.
-
- **Interest groups** formed by large **US domestic companies** utilized their political power to **lobby the government into waging trade “wars”** against Japan.

US government “counterattacked”

- “accused” Japan of **stealing** intellectual property from the U.S. and **dumping** products into the U.S. market, **illegally selling militarily-sensitive products** to the Soviet Union (“**security issues were lumped together with trade?**”)
- “forced” Japan to **sign agreements to share** semiconductor technologies and increase imports of American semiconductor products.
- The **US-Japan Structural Impediments Initiative** 《美日結構性障礙問題協定》 signed in 1989.
- ✓ An agreement on **removing structural trade barriers** between the US and Japan, e.g., promote the reform on **Japan’s anti-monopoly act and patent laws**, and alleviating the discriminatory treatment of imported goods and foreign companies etc.
- The United States and Japan have been involved in trade frictions over a number of products including **textiles, steel, automobiles, semi-conductors, and agricultural products** over the **last 50 years**. (Urata, 2020)

US-Japan trade conflict vs US-China trade war

➤ Similarities

- Both involve the world's largest and **second-largest** economies;
 - the largest trade surplus with the U.S.,
 - highly dependent on the U.S.
- Real economic conflict of interests between two countries -- could be a **long-term struggle**

➤ Dissimilarities

- Economically, **the industrial structures** are **not** the same for China and Japan in the 1980s.
- **Japan** took the lead in some **technology-intensive** industries, a very **large proportion** of **China's** exports still comes from business with **low added value**.
- Politically, **Japan** is a **key ally** of the US in East Asia.
- **China** is more like a **foe** to the US with different ideologies.

US–Japan trade frictions

- **The US mainly focused on two forms:**

- a. **restricted Japan's exports** to the US;
- b. **increased its exports to Japan** by “opening” the Japanese market.

- **Two main objectives:**

- a. **reduced** its trade deficit vis-à-vis Japan;
- b. protected and **promoted** US industries.

➤ The US **failed** to achieve the first objective (reduced its trade deficit vis-à-vis Japan), while **some success** was achieved **for protecting / promoting US industries**. (Urata, 2020).

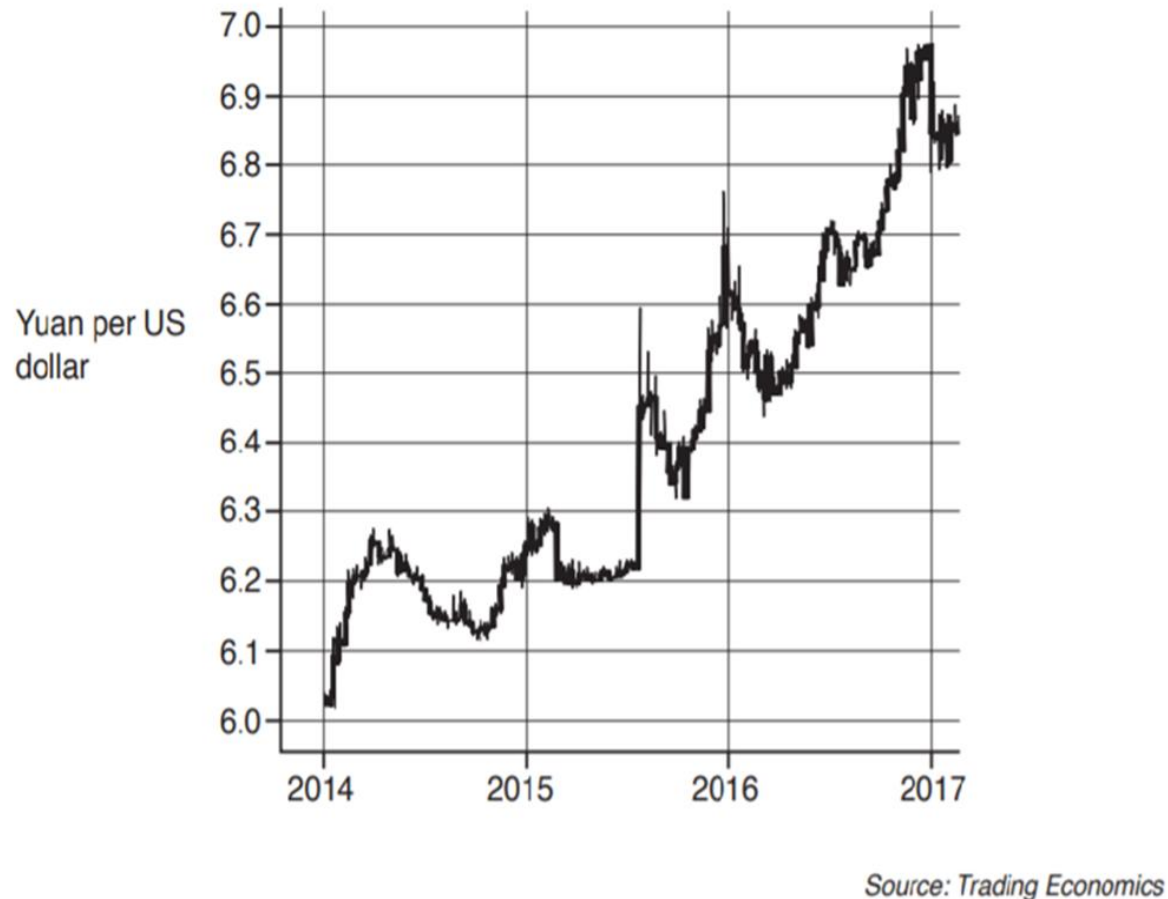
US– China trade war

- **Objectives?**
 - a. reducing the bilateral trade deficit
 - b. stopping “unfair trade practices” by Chinese firms such as violations of intellectual property rights and forced technology transfer.**
- Based on the experiences from the US–Japan trade frictions, the US may achieve some success for the second objective, but **not** for the first (**reduced** its trade deficit vis-à-vis China) (Urata, 2020).



Background Devaluation of RMB?

Accused China of devaluing its currency(Yuan per USD)



- **Trump (2016/17)** officially accused China of **intentionally devaluing the yuan**.
- **Yuan weakened significantly from 6.20 yuan per US dollar at the end of 2014 to 6.95 yuan (i.e., $\text{¥} / \$ \uparrow$ from 0.1613 into 0.1439) at the end of 2016** in order to boost **China's export** competitiveness.
- Noted that yuan devaluation also increased **China's import cost**, thus spurring the **production of domestic substitute products** and protect the domestic industry.

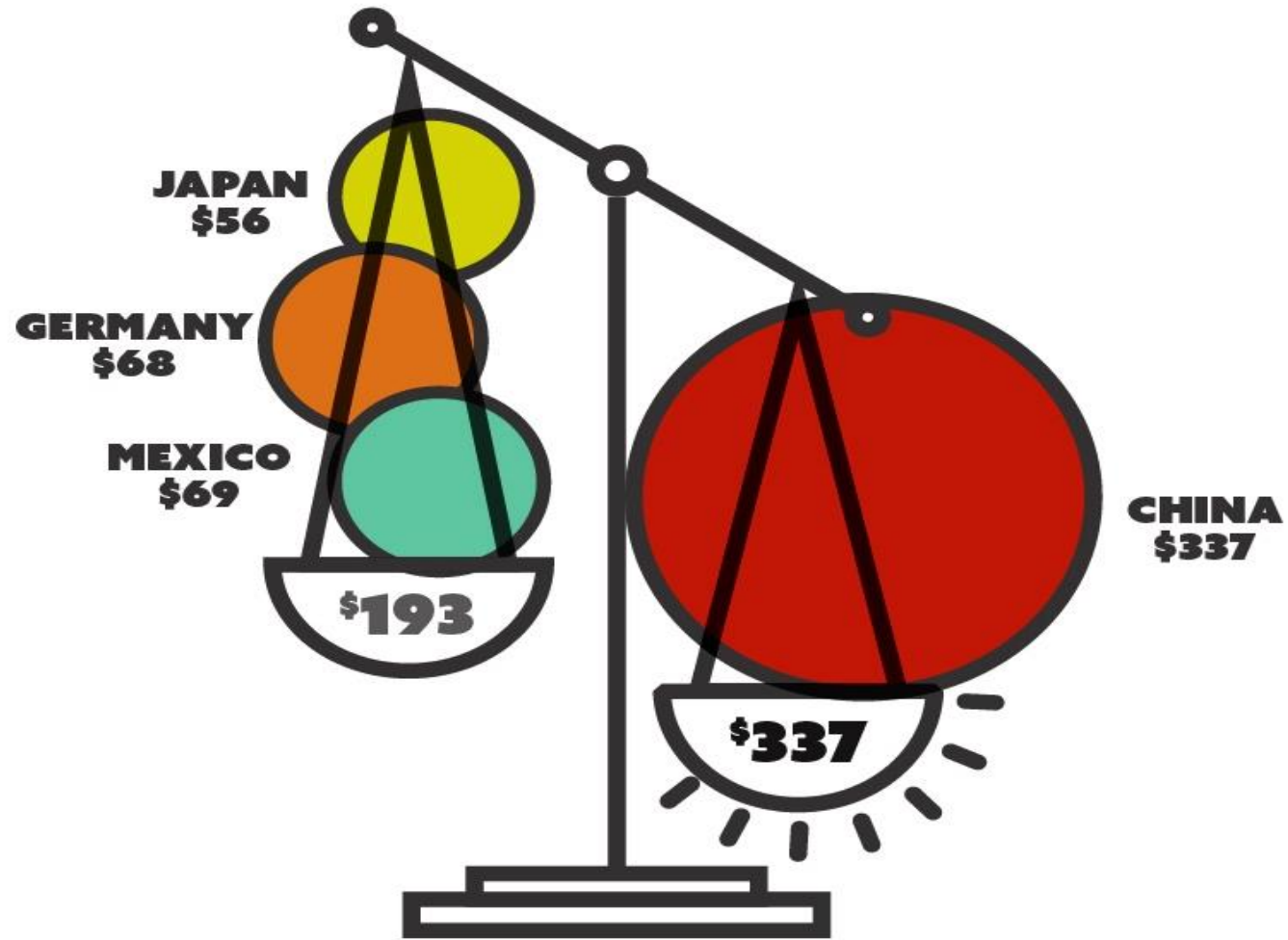
Trade figure

• **US trade data with China** in 2017


US Import from China	US Export to China
US\$ 477 billion dollars	US\$ 140 billion dollars

- ➔ US trade deficit = US\$ 337 billion dollars
- ➔ How about capital account?
- ➔ BOP -- US\$ 12.39 billion surplus

U.S. TRADE DEFICIT BY COUNTRY IN BILLIONS OF DOLLARS



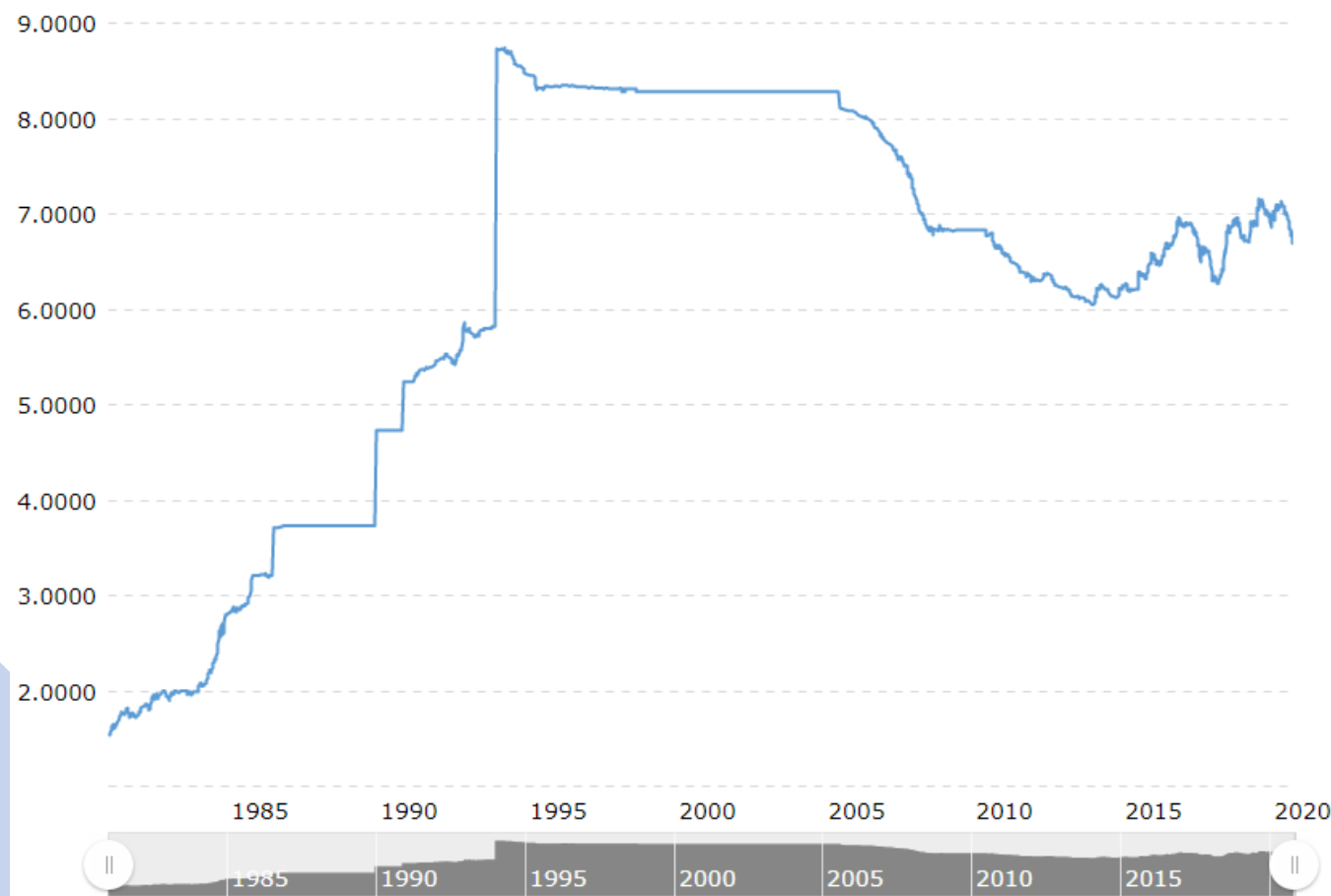
SOURCE: OFFICE OF THE U.S. TRADE REPRESENTATIVE



Why trade Deficit?
Was China Manipulating Its Currency?

Was China Manipulating Its Currency?

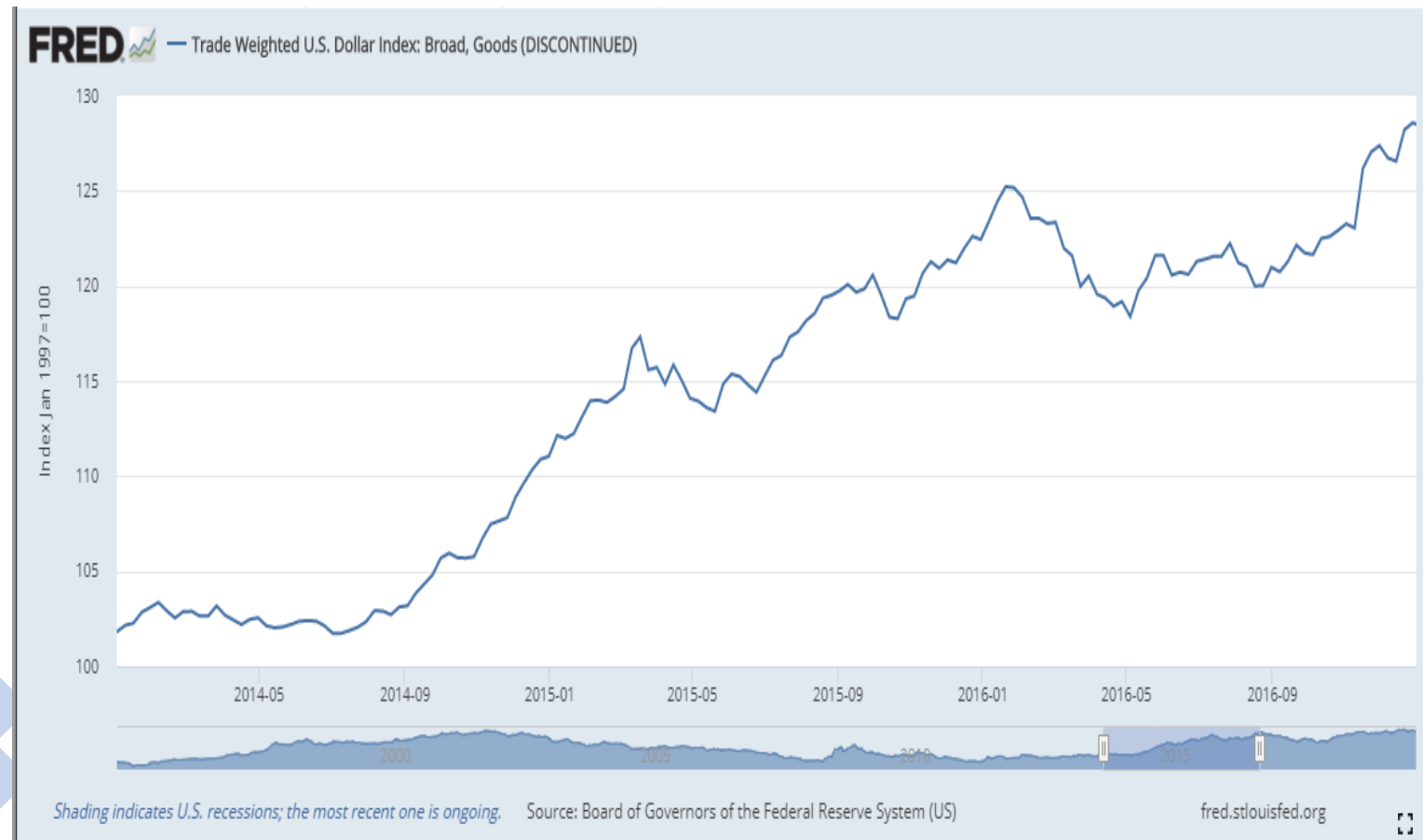
Chinese Yuan per US Dollar



- On August 11, 2015, the People's Bank of China (PBOC) surprised markets with **three consecutive devaluations** of the Chinese Yuan knocking over 3% off its value (i.e., ¥/\$ ↑)
- However, since 2005, Chinese yuan had **appreciated 33%** against the U.S. dollar (i.e., ¥/\$ ↓). After a decade of a steady appreciation against the US dollar, investors had become accustomed to the stability and growing strength of the yuan.
- 1984-1995 -- ¥/\$ ↑

US dollar index (only yuan weakened?)

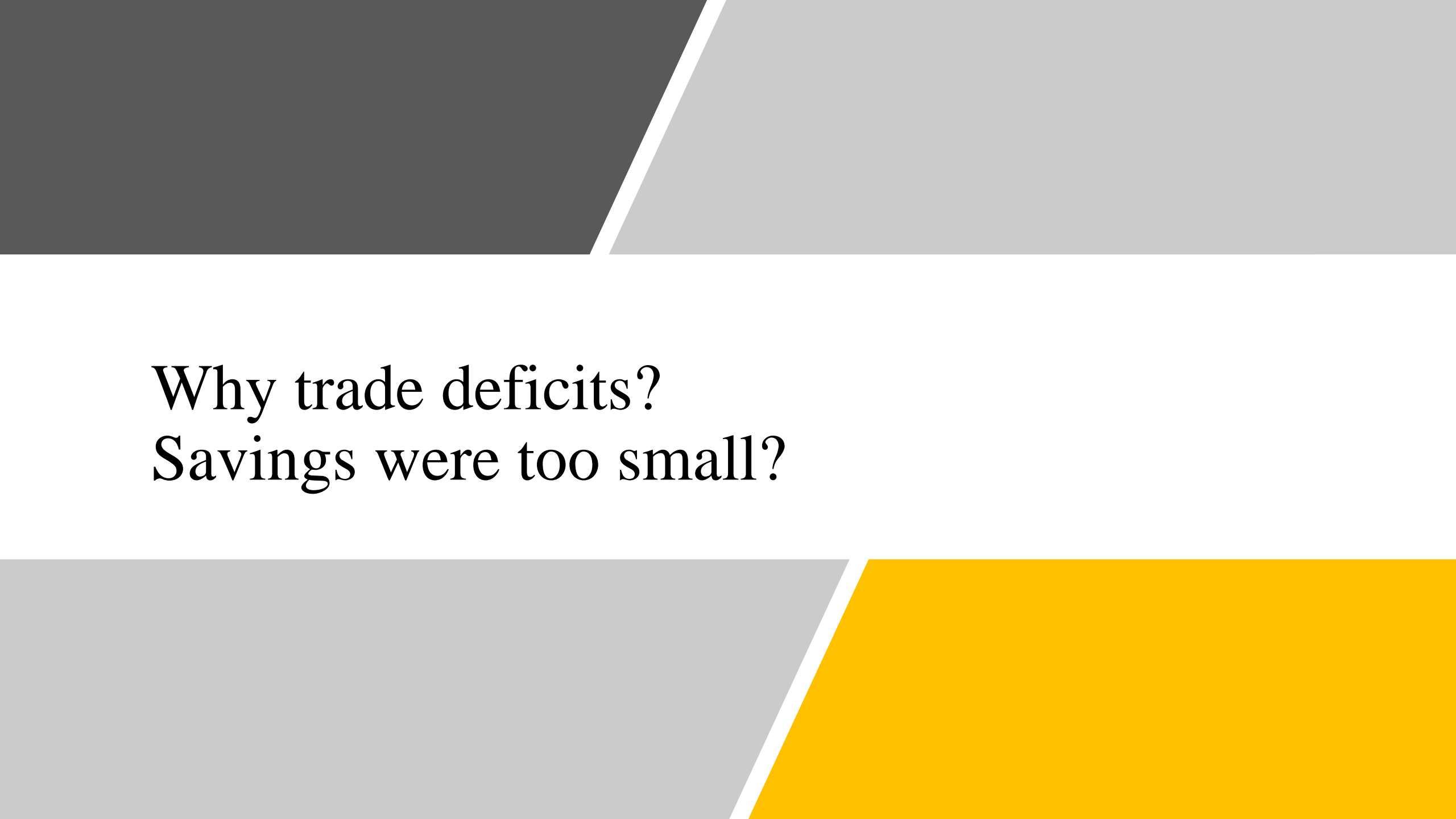
- However, during **2015-16**, the value of the **US dollar rose against most currencies**.



Was China Manipulating Its Currency?

- China's President Xi Jinping pledged the government's commitment to reform China's economy in a **more market-oriented** direction since he first took office in March 2013.
- **China's economy had slowed significantly** in the years **before** the devaluation while the **US economy had improved** (∴ **USD tended to appreciate?**)
- **IMF's response:** a continued rise in the yuan's value was **not** totally **counter** market fundamentals.

<https://www.investopedia.com/trading/chinese-devaluation-yuan/>)



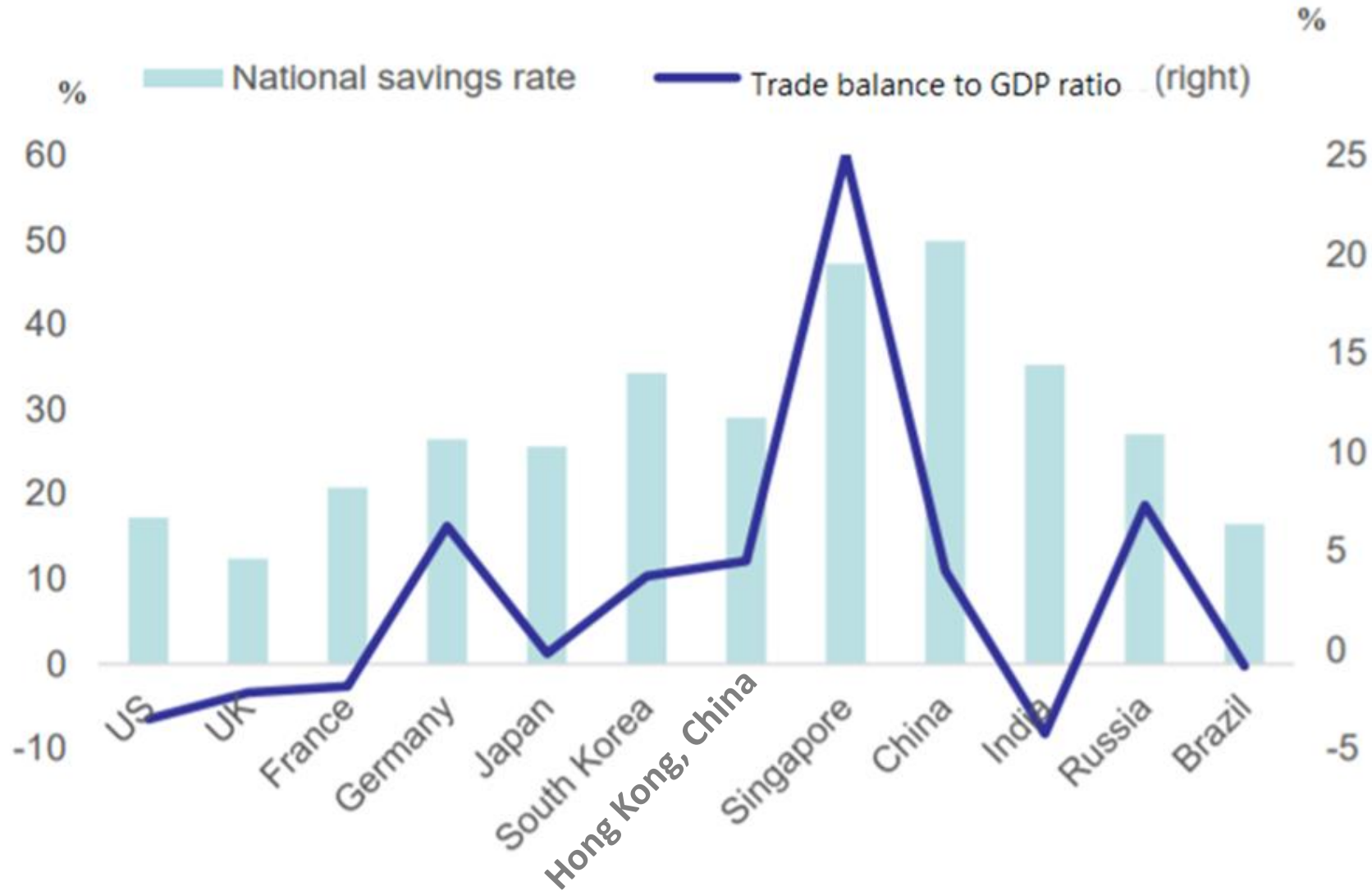
Why trade deficits?
Savings were too small?

Saving rate and trade balance

(Not within the scope of the Economics Curriculum)

- $I + G + X = S + T + M$
 $X - M = (S - I) + (T - G) = KO - KI$ (net capital outflow)
- **Trade balance** = net private saving + net government saving
= **national saving** (= net capital outflow)
Trade balance to GDP ratio = **National saving rate (to GDP)**
- Identity – necessarily true (tautology)
- **National saving and trade surplus are positively related.**
- With higher national saving, a country can sell their product/service to other countries (export), therefore it will have a favorable effect on the trade balance.
- Negative Saving (**excessive consumption**) and **trade deficit** are positively related
- Similar as Joseph Stiglitz suggests: the US runs a current account deficit because its **people save too little** to fund domestic investment.
- **However, the opponents against that, even if the US has a problem, but not necessarily is with China.**

Positive Relationship between Saving rate and trade balance



Source: China Finance 40 Forum

Reserve currency and Excessive Consumption:

- Because of the **dominant role** of the US in the world economy and its superior position in military and technology, the **US dollar is the international and reserve currency**, other countries need them.
- After adopting the **floating** exchange rate system in 1973, the US **does not need to control its money supply to maintain a trade balance**.

US dollar as the reserve currency:

- Hence, the **US can run trade deficits by printing more US dollars** to make payments for additional imports **since 1970**, which is the reason that the US has run a trade deficit. **“The dollar is our currency, but it’s your problem”** (John Connally, **Secretary of the Treasury** in 1971)
- **Paul Krugman**: “Americans **make a living** selling each other houses, **paid for with money borrowed from the Chinese**” (China bought US debt?)

<https://www.ipe.com/the-dollar-is-our-currency-but-its-your-problem/25599.article>

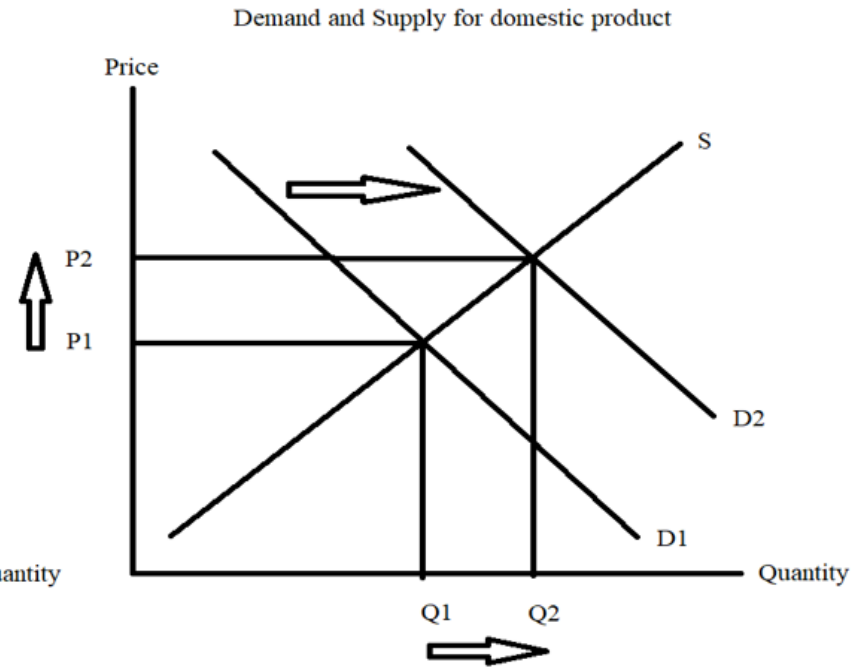
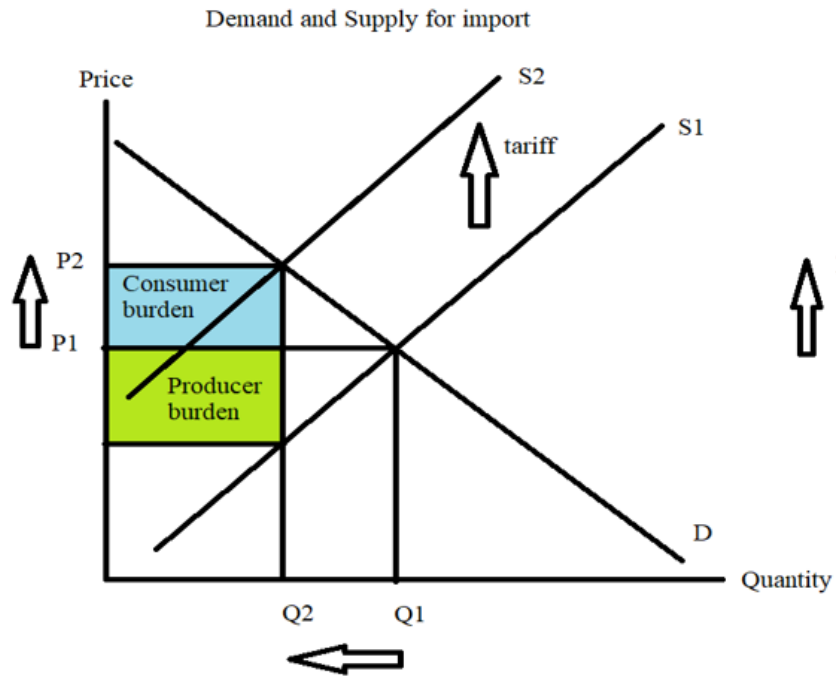
➔ **emergence of cryptocurrency?**

- **US dollar** slowly but may gradually **lost its dominant** role in the world economy



Impacts of Trade War

Theory: Impact of Tariffs on US import and domestic market



- Supply of **Chinese products** shifts upward (assume tariff is per unit tax).
- Price of the Chinese products \uparrow , Import volume from China \downarrow
- Lower production (and employment) in China
- Total revenue of Chinese producers \downarrow
- **Tax burden** (TB) on buyers /sellers \rightarrow depends on elasticity of D and S $\rightarrow \epsilon_d > \epsilon_s \rightarrow TB_s > TB_b$

- **US Domestic-Product** demand \uparrow (domestically produced goods are **substitutes** for imported Chinese goods).
- $P \uparrow, Q \uparrow$
- Higher production (and employment) in the US
- Total revenue of US domestic producers \uparrow

➤ **Retaliation \rightarrow Declined in bilateral trade, both China and the US lost**

International Monetary Fund (IMF) and United Nations Conference on Trade and Development (UNCTAD) Studies

Decline in bilateral trade:

- US **imports** from China **declined** in all three groups of the goods on which tariffs were imposed



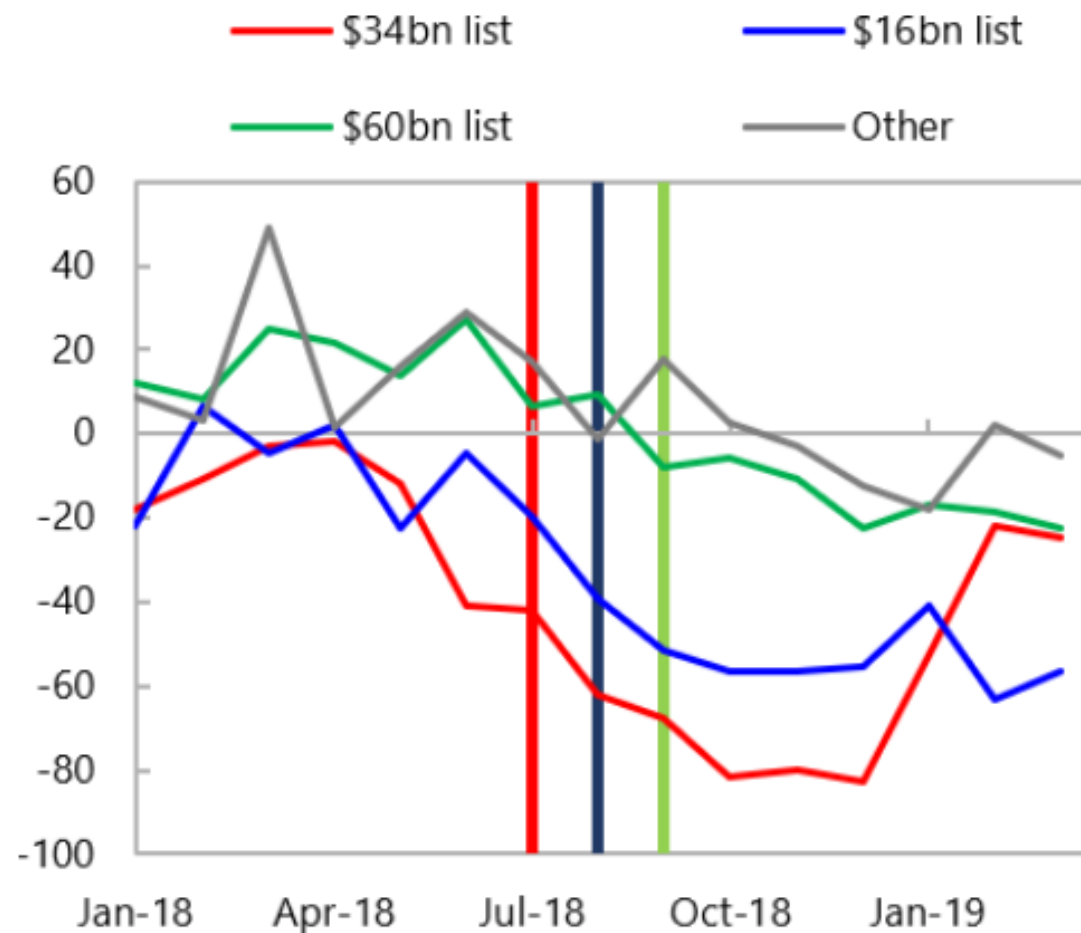
Sources: US Department of Commerce; and IMF staff calculations.

Decline in bilateral trade

- US **exports** to China **also declined** as China imposed retaliatory tariffs

Adopted from: IMFBlog -
<https://blogs.imf.org/2019/05/23/the-impact-of-us-china-trade-tensions/>)

(value of exports, year-on-year percent change)



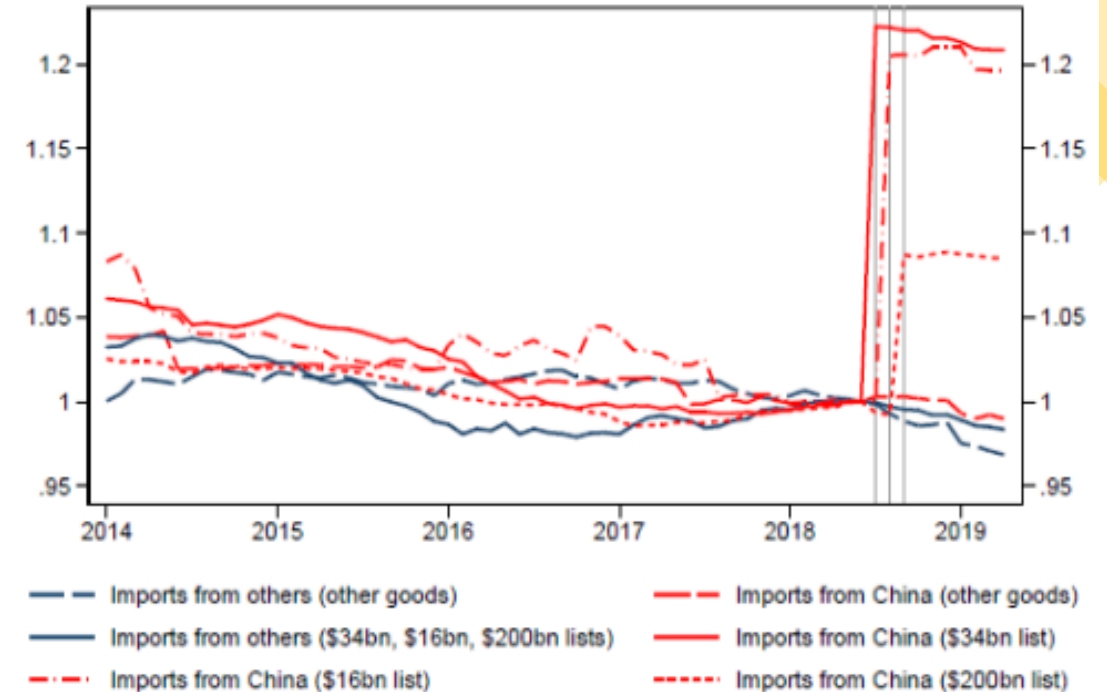
Sources: US Department of Commerce; and IMF staff calculations.

Higher prices for users

- **Sharp jump** in the **post-tariff import prices** matching the magnitude of the tariff
- **Little change** in the **ex-tariff border prices** of imports from China
- The US tariffs on China have been paid **almost entirely by US users (importers** /manufacturers/consumers). -- Demand has been much more inelastic (no choice in the short run?)
- Chinese firms have recently **started** absorbing **part of the costs** of the tariffs by **reducing the prices** of their exports -- Demand has become more elastic (more choices?).

Prices of imports in US

(average log price of imported goods in the US, June 2018 = 1)



Source: Cavallo, Gopinath, Neiman and Tang (2019), "Tariff Passthrough at the Border and at the Store: Evidence from US Trade Policy," mimeo.

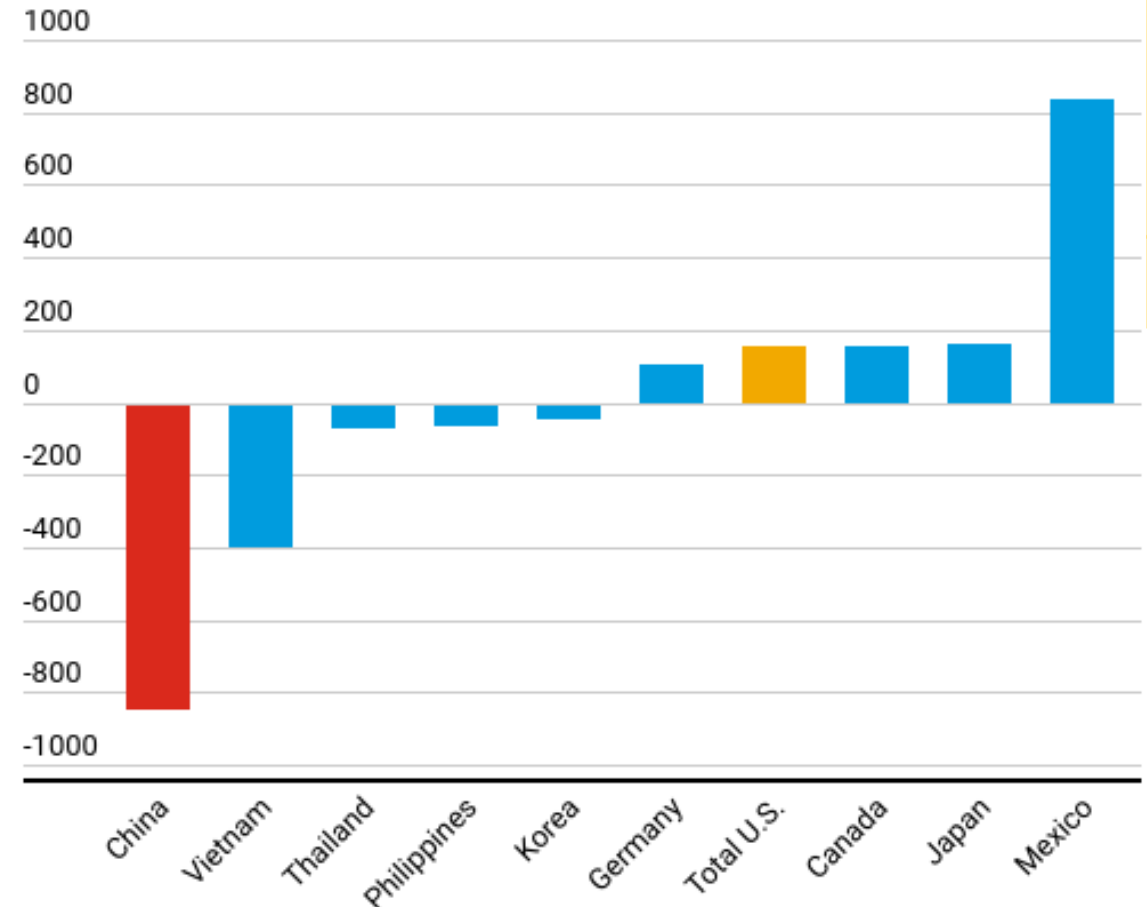
(Adopted from: IMFBlog - <https://blogs.imf.org/2019/05/23/the-impact-of-us-china-trade-tensions/>)

Trade diversion effects

- A decline in imports from China **offset** by an increase in imports from other countries (**substitute** goods especially from **Mexico**, the largest exporter to the US)
- Potential **winners**
 - Domestic producers competing against the tariffed Chinese products
 - Third country exporters (e.g., **Mexico**)
- Potential **losers: Domestic users**
 - **Domestic Consumers** of the goods affected by the tariffs
 - Domestic Producers that use those goods as intermediate inputs

Changes in imports in US

(millions of US dollars, change in Sep-Nov 2018 imports relative to Sep-Nov 2017, \$16 billion list)



Sources: US Department of Commerce; and IMF staff calculations.

(Adopted from: IMFBlog - <https://blogs.imf.org/2019/05/23/the-impact-of-us-china-trade-tensions/>)

Effects on trade deficit

- **Little effect of increasing tariff on improving US trade deficit** (**same conclusion** as the “Lesson from US-Japan trade conflicts”).
- Economists suggest **macroeconomic factors** play a much bigger role **than tariffs** in determining **bilateral** trade balances
 - Relative aggregate demand and supply in partner countries and their underlying drivers

US trade deficit

(China trade balance with US, billions of US dollars, 12-month moving sum)



Sources: US Department of Commerce; and IMF staff calculations.

(Adopted from: IMFBlog - <https://blogs.imf.org/2019/05/23/the-impact-of-us-china-trade-tensions/>)

Macroeconomic Impacts

- **Both countries** would experience a **decrease in sales**, which in turn put pressure on total **output and employment** in the short run.
- An **increase in the import price** decreases the SRAS as a result of higher production costs as the SRAS curve shifts to the left.
- Besides, the **wealth effect** of a fall in value of the stock market might decrease the consumption expenditure, and the fall in stock price might also **dampen the investment incentive**, and the investment expenditure decrease.
- As a result, the **AD decreases** and shifts to the left, **real output decreases and unemployment increases**.
- When the **magnitude** of the shift in SRAS is greater than that of the AD, the general price level will increase.
- Note that **LRAS** would also decrease as the productivity would fall due to misallocation of productive resources towards the protected industries.



The soybean case

The soybean case

- **March 22, 2018, US imposed tariffs** on imported goods from China, involving a total estimated value of **60 billion US dollars**.
- **July 6, 2018, imposed an additional 25% tariff** on Chinese exports worth US \$ **34 billion**.
- The Ministry of Commerce of **China** made **countermeasures** on the same day and imposed a **25% additional tariff on the US exports** worth US \$ 34 billion, including **soybean** from the US.

The soybean case

- **China** is almost **self-sufficient** in terms of **pork supply** although China's demand for **pork meat** makes up nearly **half** of the world's total output.
- For an **average Chinese family**, pork accounts for **two-thirds** of their meat consumption, and on average, a Chinese person consumes **120 pounds** of pork annually.
- Before **2018**, China is the world's **largest importer of soybeans from the US**. Soybean **is used** as the **raw material** for soybean oil, and the **main pig feed**.
- The **U.S. soybean** was one of the **items being charged tariff**, China's soybean **import** from the US in November 2018 dropped to almost **zero**.

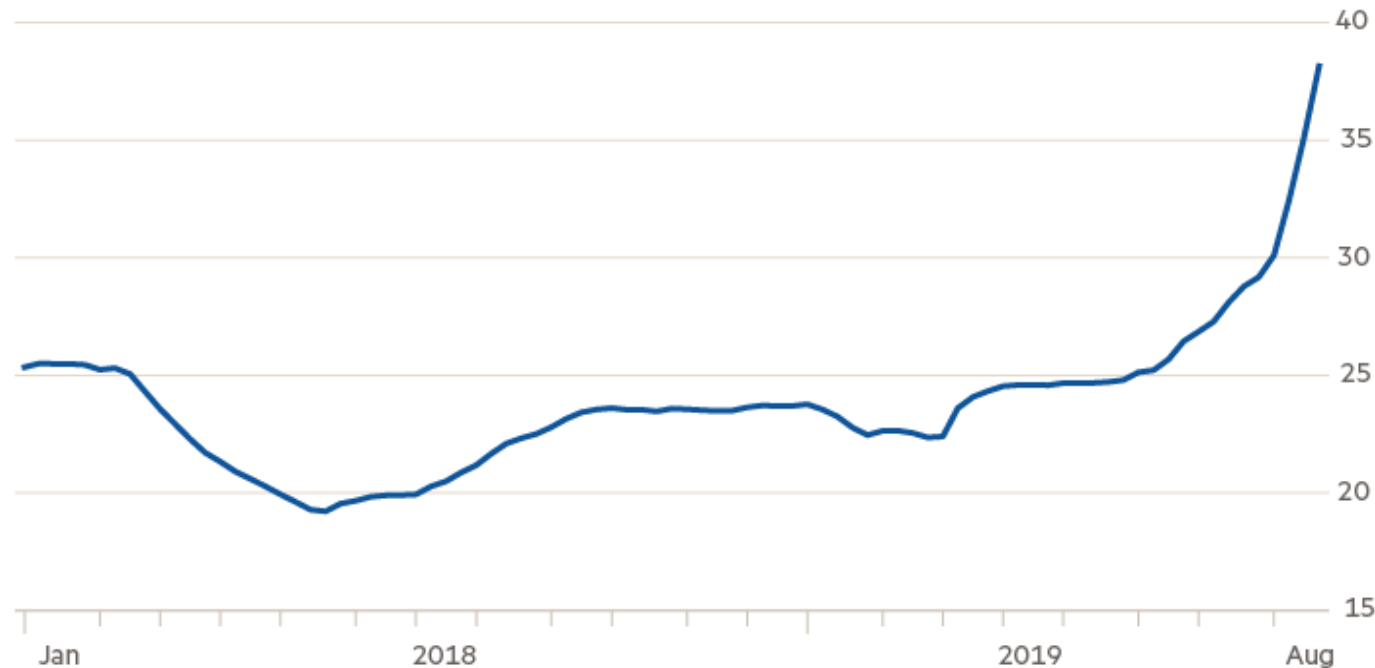
The soybean case

- For feeding pigs, **uncooked food scraps** is the **substitute** for soybean.
- Uncooked food scraps are **infected** with **African swine fever** (ASF) virus.
- The first **ASF outbreak** happened in **August 2018** in Shenyang, northeastern China. Through people feeding pigs, **ASF spread quickly in China**.
- The Chinese government **killed more than 100 million pigs** within one year. The **total output (supply) of pork dropped** about one-third of the total average.
- With a **high demand** for pork, **pork price rose**.

The soybean case

China pork price surges due to African Swine Fever

Price per kg



Source: China ministry of agriculture

© FT

According to the General Administration of Customs, PRC, in the first two quarters of **2020**, China's import volume in **US soybean** restored to the level before the trade war.

Other Issues

McConnell et al. (2018)

Regional Trading Blocs

- A **regional trading bloc** is a group of countries **within a geographical region** that **protect** themselves from imports from non-members.
- It is a type of **international agreement**, often part of a **regional intergovernmental** organization, such as the North American Free Trade Agreement (NAFTA) and the European Union (EU).
- **Trade barriers** (tariffs and others) are reduced or eliminated **among** the participating nations. Trading blocs lead to trade liberalisation and trade creation between members,
- i.e. trade **liberalisation within** trading blocs but trade **protection among** trading blocs.

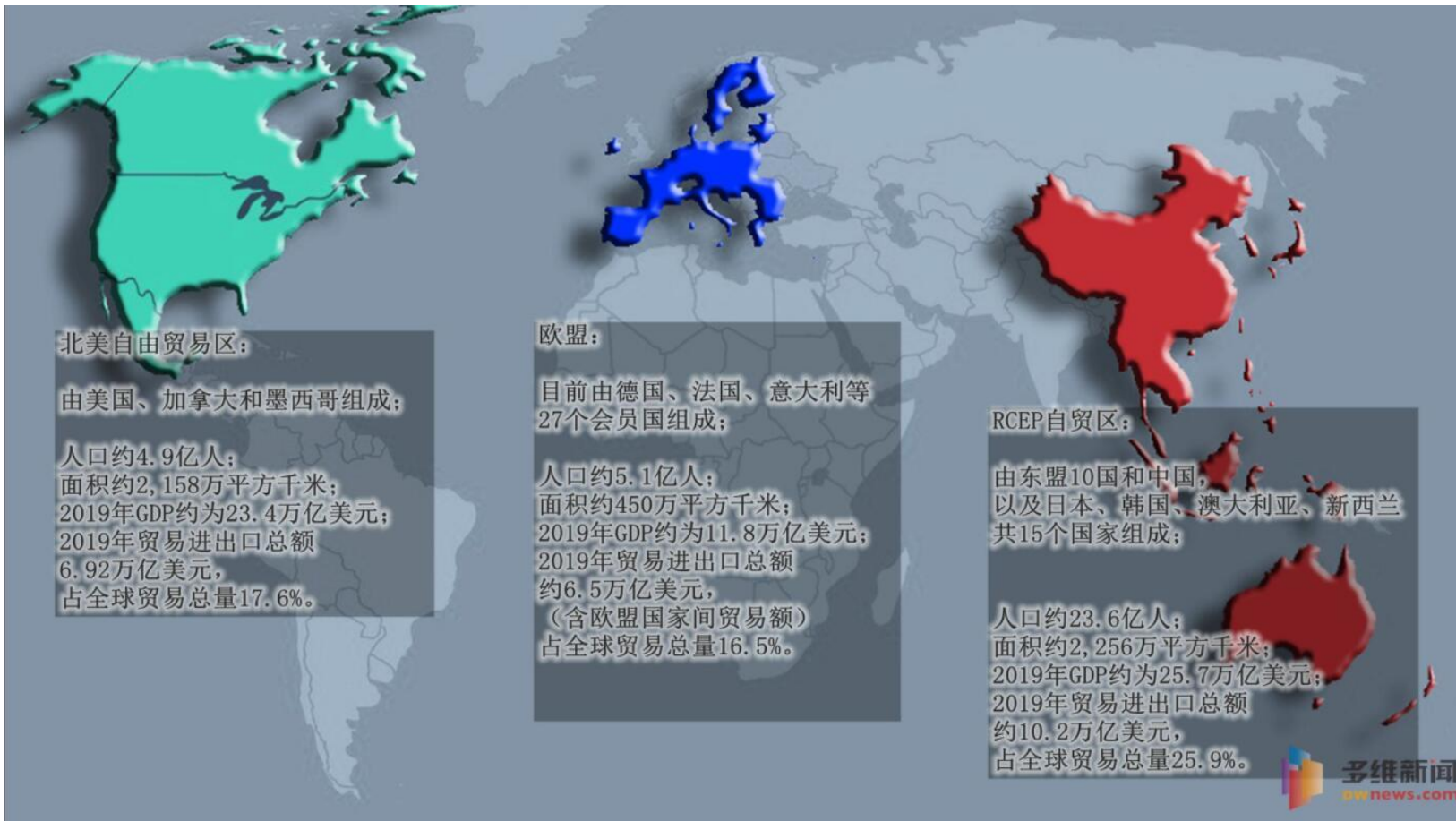
Regional Comprehensive Economic Partnership RCEP

<https://www.bbc.com/news/world-asia-54949260>

- 區域全面經濟夥伴協定
- 15 countries have formed the **world's largest trading bloc**, the Regional Comprehensive Economic Partnership (**RCEP**), covering more than **2 billion people** and has an economy of nearly **\$26 trillion**, or about **30% of global GDP**, making it the world's largest trade agreement in terms of GDP. RCEP also accounts for about **a third of the world's trade**.
- The **15** countries include the **10 members of ASEAN**東盟—Brunei-Darussalam, Cambodia, Indonesia, Laos, Malaysia, Myanmar, the Philippines, Singapore, Thailand and Viet Nam plus the **five countries with which ASEAN has free trade agreements**—Australia, China, Japan, South Korea, and New Zealand.
- RCEP was signed on 16/11/2020, expected The RCEP is expected to **eliminate a range of tariffs** on imports within 20 years. It **covers** a wide range of issues, including **trade in goods and services, investment, intellectual property rights, competition policy, e-commerce, rules of origin, dispute settlement, and economic and technical cooperation.**, but does not include environmental protection and labour rights.

世界三大自貿區鼎足：

RCEP自貿區與歐盟、北美自貿區的經濟實力對比。按照各自貿區實際GDP佔全球GDP的比重，顯示的區域面積。三大自貿區GDP總和幾乎佔到全球經濟的76.9%。（多維新聞）



世界三大自貿區
佔全球人口 (77.54 億):
43.33%
佔全球GDP: 76.9%
佔全球貿易總量: 60%

經濟融合(Economic Integration)進程



Regional Trading Blocs

Pre-condition:

Goods/Factor mobility

Purchasing Power Parity / Law of one price)

Transaction costs of trading goods between countries such as transport costs, logistics costs, imperfect competition, tariffs /non-tariff barriers, culture difference > **Gains from trade** → No trade

The level of **Transaction cost** is the **key** to closer economic integration.

Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP)

- Comprehensive and Progressive Agreement for Trans-Pacific Partnership (跨太平洋夥伴全面進步協定)
- 主要內容: **綜合性**的自由貿易協定，包括貨物貿易、原產地規則、貿易救濟措施、**衛生和植物衛生措施**、技術性貿易壁壘、**服務貿易**、智慧財產權、**政府採購和競爭政策**等。
- CPTPP原稱跨太平洋**戰略經濟伙伴關係協定**（TPP），最初由亞太經濟合作會議成員發起，從2002年開始醞釀的一組多邊關係的自由貿易協定，旨在促進亞太區貿易自由化。**2017年特朗普簽署行政命令退出TPP**，同年TPP改組為CPTPP。2018年3月8日，日本、加拿大、澳洲、新西蘭、馬來西亞、新加坡、越南、文萊、墨西哥、智利及秘魯11國在智利簽署該協定。
- 路透社報道，日本明年將擔任CPTPP輪值主席國，日本首相菅義偉在亞太經濟合作組織（APEC）首腦峰會的錄製視像講話中表示，「日本希望早日核准《區域全面經濟伙伴關係協定》（RCEP）的同時，能够穩步執行並擴大CPTPP自由貿易區」。據悉，**中國和英國都是CPTPP的潛在爭取對象**，中方將積極考慮加入CPTPP。明報2020年11月23日

- 美國和前蘇聯以及其他三十多個國家，於1992年簽訂《開放天空條約》，條約在2002年起生效，**允許簽約國之間的飛機飛越各國領空，進行非武裝空中偵察，監察各國控制軍備情況。**
- 今年5月，美國總統特朗普指由於俄羅斯沒遵守有關條約，美方會於六個月後退出。
- 美國國家安全顧問奧布萊恩在社交網站發文稱，美國通知退出《開放天空條約》已六個月，**現時不再是條約的成員國。**
- 國務卿蓬佩奧則指，美國退出條約後變得更加安全。俄羅斯外交部就發聲明指，美國退出條約既不利於歐洲安全，也不利於美國及其盟友的安全，又指美方早前指責俄方違反條約是毫無根據。

(資料來源：美國正式退出《開放天空條約》，Now 新聞，2020-11-23

<https://news.now.com/home/international/player?newsId=413892>)

- 拜登11月16日提到需要「與其他民主國家結盟.....這樣我們就可以制定規則，而不是讓中國和其他國家決定結果」，這與特朗普時期在貿易問題上四處開火、單打獨鬥形成了鮮明的對比。
- 德國和法國等歐洲盟友對拜登寄予希望，美歐關係有望得到修復。在RCEP簽署後，德國聯盟黨聯邦議院黨團外交發言人哈特（Jurgen Hardt）認為，「與美國達成貿易協定對於整個西方世界而言仍然至關重要，這應該是德國和歐盟對於新任美國總統的首要願望」，並且，歐洲政壇有關「聯美抗中」的聲音也頻頻響起。

(資料來源：拜登將全面顛覆特朗普，HK01，2020-11-20)

➤ **The level of Transaction cost would be the key to the success of closer economic integration.**

Reduce resistance to free trade: Trade Adjustment Assistance

Free Trade, on average, is associated with **poverty reduction** (operating through improved wages) in the long run.

However, the trade liberalization process can **adversely affect** workers and stakeholders in the **comparative-disadvantage** industries. (South Korean farmers protested against the liberalization of the rice trade in their country (2009).

Trade Adjustment Assistance (TAA) Programs in the US **provide assistance** to workers and stakeholders who have been adversely affected by foreign trade and **reduce** the damaging impact of imports **felt** by certain sectors of the economy.

Trade adjustment assistance (TAA) in the US **offers** job training, relocation allowances, income support and help with healthcare premiums and related benefits to workers **who lost jobs due to the effects of increased imports and offshoring**.

- However, jobs lost due to imports is such a small percentage of total jobs lost that it's **not fair** that these workers receive special benefits while other displaced workers do not.



Developing the DRQ



Data response questions

- **Aim:** test the ability of candidates to **apply their (economics) knowledge to unseen information** on statistical data, charts, line graphs and newspaper extracts and comics etc.
- **Topic:** current /big/ hot/ controversial....issue -- **US-China Trade War**
- **Based on academic materials (economic theory).**
<http://dolanecon.blogspot.com/p/index-of-slideshows.html>
- **Keywords related to the curriculum:**
balance of trade, exchange rate, **effects of tariff** (burden, import price, winners/losers, inflation, unemployment etc).
- **Global data: image search on the web.**
e.g. “**US china trade war**”

Data response questions



- Questions - **three** levels: gradually increase the level of difficulty
 - **Entry-level**: directly extract information (**observed facts**) from the materials without digestion, e.g. “**point out**” and “**describe**” the trend and change, “**calculate**”, “**measure**”.
 - **Medium-level**: select and generalise information, infer points of view, e.g., “**analyse**”, “**explain**” and “**elaborate**”, e.g., **Explain why price has increased (given observed outcome--data): caused by many factors (various possible answers - based on theory)**
 - **Advanced-level**: compare and analyse different information sources from multiple angles to demonstrate students’ understanding of the topic outside the material, e.g., “**compare**” and “**evaluate**
- **Start** from the “entry-level or “**advanced-level**” ?

https://www.edb.gov.hk/attachment/tc/curriculum-development/kla/pshe/references-and-resources/economics/A_DBQ_whole_Eng.pdf

Data response questions



➤ Are the material and questions **related**? – based on theory

➤ **Difficulties:**

- **Certain** questions expect students to **propose solutions**, but many students may **fail** to provide logical inferences for solving the problem.
- Real-world data are **not highly consistent with theory**.
- less-well known data /too many possible answers

➤ **Facilitate student's thinking:** Provide more information, assumptions and limitations

- **Provide “hints”** (use economic theory to think about the problem)

“**Explain** whether you support the legalization of drugs (such as cocaine) **from an economic perspective using the concepts** of supply, demand, and elasticity.”

- **Guide** students toward **identifying** the nature of the problem, the number of variable solutions, *compare the merits* of each solution, then **propose a final solution** and even **verify** the validity of the solution.
- **Use global data and qualitative data: dialogue / news/ media articles / comics**

Data response questions



- Is the quantity of the material appropriate – **neither insufficient nor excessive**:
 - **shouldn't** focus on students' ability to **speed-read** but the **ability to respond to the data-response questions**. conduct analysis based on theory, not just based on the data.
- **More daily practices** – **open-ended** discussions
- **Public Exam**: answers should be based on **data** provided and **economic theory**

https://www.edb.gov.hk/attachment/tc/curriculum-development/kla/pshe/references-and-resources/economics/A_DBQ_whole_Eng.pdf

Data response questions



➤ Factors and observed outcome:

- **Theory:** $Y = f(X_1, X_2..)$
- **Explain why** price has increased (**given observed outcome**): caused by many factors—different answers (tourists $\uparrow \rightarrow$ Demand $\uparrow \rightarrow P \uparrow$, but $P \uparrow$ not necessarily because tourists has increased)
- Inference from **theory**: **various possible outcomes** – different views
e.g., $P \uparrow$: total revenue may \uparrow or \downarrow , **depends on elasticities** of D/S
- **Explain why** total revenue \uparrow (**given observed outcome**)
- **Correlation /causality** – based on evidence and **theory**
- **Identity**: must be true for all values of the variable for which the equation is defined.
(unemployment rate = $U / (U + E)$)
- **Theory** \rightarrow conceivable to be false, many factors \rightarrow source with different views

DRQ on China-US trade war

- A DRQ developed by Dr. Lee can be downloaded from the link below:
(https://www.edb.gov.hk/en/curriculum-development/kla/pshe/references-and-resources/economics/China-US_Trade_War.html)



Sources for getting data

➤ **Keywords:** balance, trade, exchange rate, import prices, inflation, unemployment etc.

- Hong Kong Census and Statistics Department
- U.S. Bureau of Labor Statistics
- U.S. Census Bureau
- Bloomberg
- Reuters
- National Bureau of Statistics of China
- Ministry of Commerce People's Republic of China
- Bureau of Economic and Business Affairs
- U.S. Department of Commerce
- Bureau of Economic Analysis

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- <https://blogs.imf.org/2019/05/23/the-impact-of-us-china-trade-tensions/#:~:text=US%2DChina%20trade%20tensions%20have,trade%20deficit%20remains%20broadly%20unchanged>
- <https://unctad.org/en/pages/newsdetails.aspx?OriginalVersionID=2226>
- <https://www.investopedia.com/trading/chinese-devaluation-yuan/>
- <https://outsourceworkers.com.au/offshoring-and-outsourcing/>
- https://www.economicsonline.co.uk/Global_economics/Trading_blocs.html
- <https://www.thebalance.com/trade-wars-definition-how-it-affects-you-4159973>
- <https://www.reuters.com/article/us-usa-trade-china-timeline/timeline-key-dates-in-the-us-china-trade-war-idUSKCN1VD20A>
- <https://www.china-briefing.com/news/the-us-china-trade-war-a-timeline/>
- <https://news.cgtn.com/news/2019-07-11/Lessons-from-U-S-Japan-trade-war-of-1980s-IcWJh9RjAQ/index.html>

THE HISTORY OF US-JAPAN RELATIONS

From Perry to the Present

EDITED BY MAKOTO IOKIBE

English translation edited by

TOSH MINOHARA



Book Recommendation

- The History of US-Japan Relations: From Perry to the Present
- Authors:
 - Makoto Iokibe
 - Tosh Minohara

CHARTING A PATH FOR A STRONGER U.S.-JAPAN ECONOMIC PARTNERSHIP

By Saori N. Katada, Junji Nakagawa, and Ulrike Schaede



Book Recommendation

- “Charting a Path for a Stronger U.S.-Japan Economic Partnership”
- Authors:
Saori N. Katada, Junji Nakagawa, and Ulrike Schaede

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Thank you!