

Weekly Commentary 25

The Trade Wars – China vs the West. Who loses??

Last week, in my closing paragraph, I wrote about how the Smoot Hawley Act of 1930 hurt the countries which engaged in trade protectionism in the years after it was enacted, and deepened their economic woes during the Great Depression. In our commentary this week, I will elaborate on the futility of tariffs, and why it may not work in the Biden Administration's efforts to derail China's economic growth and suppress it from challenging US hegemony.

The Tariff Act of 1930, commonly known as the Smoot–Hawley Tariff was a law that implemented protectionist trade policies in the United States. Sponsored by Senator Reed Smoot and Representative Willis C. Hawley, it was signed by President Herbert Hoover on June 17, 1930. The act raised US tariffs on over 20,000 imported goods. 1930 was the start of the Great Depression.

I first heard about Smoot Hawley in my undergraduate class forty five years ago, and at that time, there was no doubt among historians that chapter of American economic history was a disaster. Since then, Milton Friedman's monetarism has become fashionable, and it seems that the theory that those tariffs worsened the Great Depression may now be heresy.

These tariffs were the second highest in United States history, exceeded by only the Tariff of 1828. The Act led to retaliatory tariffs by Canada and other countries. Smoot Hawley and the tariffs by America's trading partners to retaliate were the main reasons why American exports fell off a cliff in the early 1930's (by 67%) and imports also dropped significantly (by about the same amount) during the early years of the Great Depression. **Economic historians have a consensus view that the passage of the Smoot–Hawley Tariff worsened the effects of the Great Depression and that its negative impacts have been very real.**

By the late 1920s, the US economy had made exceptional gains in productivity because of electrification, which was a critical factor in mass production. Another contributing factor to economic growth was motorcars, trucks, and tractors replacing horses and mules. One sixth to one quarter of farmland, which had been devoted to feeding horses and mules, was freed up, contributing to a surplus in farm produce. Although nominal and real wages had increased, they did not keep up with productivity gains.

Senator Smoot contended that raising the tariff on imports would alleviate the overproduction problem, but the United States had actually been running a trade account surplus, and although manufactured goods imports were rising, manufactured exports were rising even faster. Food exports had been falling and were in trade account deficit, but the value of food imports were a little over half of the value of manufactured imports.

As the global economy entered the first stages of the Great Depression in late 1929, the main goal of the US was to protect its jobs and its workers from foreign competition. This is exactly as the Biden White House is trying to do today. Smoot championed another tariff increase within the United States in 1929, which became the Smoot–Hawley Tariff

Bill. In his memoirs, Smoot made it abundantly clear: “The world is paying for its ruthless destruction of life and property in the (First) World War and for its failure to adjust purchasing power to productive capacity during the industrial revolution of the decade following the war.”

While Hoover joined the economists in opposing the bill, calling it "vicious, extortionate, and obnoxious" because he felt it would undermine the commitment he had pledged to international cooperation, he eventually signed the bill after he yielded to influence from his own party, his Cabinet (who had threatened to resign), and business leaders. (This sounds familiar a century later, as there is bipartisan consensus in Washington today that China is a peer competitor which needs to be defeated, to prevent America from losing its perch at the top of the totem pole.)

In retaliation, Canada and other countries raised their own tariffs on American goods after the bill had become law.

Franklin D. Roosevelt spoke against the act during his campaign for President in 1932.

Retaliation

Most of the decline in trade was due to a plunge in GDP in the US and worldwide. However, beyond that was additional decline. Some countries protested and others also retaliated with trade restrictions and tariffs. American exports to the protesters fell 18% and exports to those who retaliated fell 31%.

Threats of retaliation by other countries began long before the bill was enacted into law in June 1930. As the House of Representatives passed it in May 1929, boycotts broke out, and foreign governments moved to increase rates against American products, although rates could be increased or decreased by the Senate or by the conference committee. By September 1929, Hoover's administration had received protest notes from 23 trading partners, but the threats of retaliatory actions were ignored. (Sounds familiar??)

In May 1930, Canada, America's most loyal trading partner, retaliated by imposing new tariffs on 16 products that accounted altogether for around 30% of US exports to Canada. Canada later also forged closer economic links with the British Empire via the British Empire Economic Conference of 1932, while France and Britain protested and developed new trade partners, and Germany developed a system of trade via clearing.

The depression worsened for workers and farmers despite Smoot and Hawley's promises of prosperity from high tariffs; consequently, Hawley lost re-nomination, while Smoot was one of 12 Republican Senators who lost their seats in the 1932 elections, with the swing being the largest in Senate history (being equaled in 1958 and 1980).

Economic analysis of the Tariff Act

The years 1920 to 1929 are widely described, incorrectly, as years in which protectionism gained ground in Europe. In fact, from a general point of view, according to Paul Bairoch, the period before the crisis in Europe can be considered to have been preceded by trade liberalization. The weighted average of tariffs applied to manufactured products remained practically the same as in the years before the First World War: 24.6% in 1913, compared to 24.9% in 1927. In addition, in 1928 and 1929, tariffs were reduced in almost all developed countries. Additionally, the Smoot–Hawley Tariff Act was signed by Hoover on June 17, 1930, while the Wall Street Crash occurred in the fall of 1929.

Paul Krugman writes that protectionism does not lead to recessions. According to him, the decrease in imports (which can happen by introducing tariffs) has an expansive (ie stimulative) effect, that is, it is favorable to growth. Thus, in a trade war, since exports and imports will decrease equally, for everyone, the negative effect of a decrease in exports will be offset by the expansionary effect of a decrease in imports. Therefore, a trade war does not cause a recession. Furthermore, he points out that the Smoot–Hawley tariff did not cause the Great Depression. The decline in trade between 1929 and 1933 "was almost entirely a consequence of the Depression, not a cause. Trade barriers were a response to the Depression, partly as a consequence of deflation." In other words, the new "wisdom" in the Biden White House that using tariffs to crush China's economy may produce exactly the opposite effect – since the enforced "decrease in exports will be offset by the expansionary effect of a decrease in imports in China, "a trade war may not cause a recession in China..." I hope the analogy to the argument above is clear.

As such, there will unlikely be a slowdown of economic growth in China because the US is trying to bring it about by reducing Chinese exports, which will undoubtedly be achieved since the tariffs are very high. Yes, Chinese exports to the US will go down, as this has been evident since the Trump tariffs were launched nearly 8 years ago. But that does not mean that China's economy will go into a tailspin. The problem for the US is that this decline in Chinese exports will also bring down Chinese imports from the US, as it happened in the 1930's and that would be "expansive", contrary to the intent of Biden's team. So instead of crimping China's growth, the Biden tariffs will not have any impact on the intended slowdown of Chinese GDP. Add to this the expectation that there will be some of the old contractionary effects of tariffs within the US economy, and in these Biden efforts to curtail China's development, the US may actually suffer from what most economists would expect from unintended recessionary effects of tariffs.

This will be a double whammy. –We can analyse it using some high school economics. In the equation, $\text{Change in GDP} = \text{Change in } (C + I + G + (X-M))$ where C is consumption, I Investment, G government expenditures and (X-M) is net exports, then on the Chinese side, X-M may actually increase, because M decreases, and Chinese GDP consequently go up, contrary to American intentions. And on the US side, X-M goes down because X decreases and US GDP may contract.

What??

In economic theory it goes like this:

Change in Chinese ,GDP = Change in $C+I+G+(X-M)$ and if M declines, GDP goes up.

Change in US GDP = Change in $C +I + G+(X-M)$ and if X declines, GDP in the US goes

This may not be exactly how it happens, but there is no certainty that this double whammy cannot happen. If the experience with Smoot Hawley is anything to go by, the same (X-M) effect may affect the two economies in opposite directions. And if that should happen, the US trade war against China will be counterproductive. As a matter of fact, this is happening in the trade war against Russia – after 2 years of

sanctions, the Russian economy has the strongest growth in all of Europe, demonstrating a 3.2 percent growth, as forecasted by the IMF.

Finally, the chronology of events in 1930 does not correspond to the thesis of the free traders... The bulk of the contraction of trade occurred between January 1930 and July 1932, that is, before the introduction of protectionist measures, even self-sufficient, in some countries, with the exception of those applied in the United States in the summer of 1930, but with limited negative effects. He noted that "the credit crunch is one of the main causes of the trade crunch." "In fact, international liquidity is the cause of the trade contraction. This liquidity collapsed in 1930 (-35.7%) and 1931 (-26.7%). A study by the National Bureau of Economic Research highlights the predominant influence of currency instability (which led to the international liquidity crisis) and the sudden rise in transportation costs in the decline of trade during the 1930s.

Milton Friedman was of the opinion that the 1930 Smoot–Hawley Tariff did not cause the Great Depression. Douglas A. Irwin writes: "Most economists, liberal and conservative alike, doubt that Smoot Hawley had much to do with the subsequent contraction."

William J. Bernstein wrote: Between 1929 and 1932, real GDP fell 17% worldwide, and 26% in the United States, but most economic historians now believe that only a minuscule part of that huge loss in both world GDP and US GDP can be attributed to tariff wars. .. At the time of Smoot–Hawley's passage, the volume of trade represented only about 9% of world economic output. If all international trade had been eliminated and no domestic use found for previously exported goods, world GDP would have fallen by the same amount: 9 percent. Between 1930 and 1933, the volume of world trade fell by between a third and a half. Depending on how the drop is measured, this equates to between 3 and 5 percent of global GDP, and these losses were partially offset by more expensive domestic goods. Thus, the damage caused could not have exceeded 1 or 2 percent of global GDP, or even close to the 17 percent drop seen during the Great Depression... **The inescapable conclusion: Contrary to public perception, Smoot–Hawley did not cause, or even significantly deepened, the Great Depression. On deeper analysis, as done above, we can even surmise that Smoot Hawley did not worsen the Great Depression and this may mean that the US is in trouble starting the latest trade war with China.**

After enactment

At first, the tariff seemed to be a success. According to historian Robert Sobel, "Factory payrolls, construction contracts, and industrial production all increased sharply." However, larger economic problems loomed in the guise of weak banks. When the Creditanstalt of Austria failed in 1931, the global deficiencies of the Smoot–Hawley Tariff became *apparent*.

US imports decreased 66% from \$4.4 billion (1929) to \$1.5 billion (1933), and exports decreased 61% from \$5.4 billion to \$2.1 billion. GNP fell from \$103.1 billion in 1929 to \$75.8 billion in 1931 and bottomed out at \$55.6 billion in 1933. Imports from Europe decreased from a 1929 high of \$1.3 billion to just \$390 million during 1932, and US exports to Europe decreased from \$2.3 billion in 1929 to \$784 million in 1932. Overall, world trade decreased by some 66% between 1929 and 1934.

Unemployment was 8% in 1930 when the Smoot–Hawley Act was passed, but the new law failed to lower it. The rate jumped to 16% in 1931 and 25% in 1932–1933. There is some contention about whether this can necessarily be attributed to the tariff, however.

It was only during World War II, when "the American economy expanded at an

unprecedented rate", that unemployment fell below 1930s levels.

Imports during 1929 were only 4.2% of the US GNP, and exports were only 5.0%. Monetarists, such as Milton Friedman, who emphasized the central role of the money supply in causing the depression, considered the Smoot–Hawley Act to be only a minor cause for the US Great Depression.

End of tariffs

The 1932 Democratic campaign platform pledged to lower tariffs. After winning the election, President Franklin Delano Roosevelt and the now-Democratic Congress passed Reciprocal Trade Agreements Act of 1934. This act allowed the President to negotiate tariff reductions on a bilateral basis and treated such a tariff agreement as regular legislation, requiring a majority, rather than as a treaty requiring a two-thirds vote. This was one of the core components of the trade negotiating framework that developed after World War II.

After World War II, that understanding supported a push towards multilateral trading agreements that would prevent similar situations in the future. While the Bretton Woods Agreement of 1944 focused on foreign exchange and did not directly address tariffs, those involved wanted a similar framework for international trade. President Harry S. Truman launched this process in November 1945 with negotiations for the creation of a proposed International Trade Organization (ITO).

As it happened, separate negotiations on the General Agreement on Tariffs and Trade (GATT) moved more quickly, with an agreement signed in October 1947; in the end, the United States never signed the ITO agreement. Adding a multilateral "most-favored-nation" component to that of reciprocity, the GATT s.

All in all, there is new wisdom in economic theory that major tariffs such as the Smoot Hawley Act may have surprising results. So the massive trade tariffs imposed by America on China can turn out to be counterproductive? Will it hurt China or will it hurt the US even more? Our analysis above seems to point in the direction that China will be hurt less than the US.

That are just the macro economic effects. At the industrial level, there will be even more problems for the Americans. The Biden Administration is hell bent on crippling China by putting tariffs on some of its best exports. Will these work? Let's study this problem.

Current Trade War A trade war happens when one country retaliates against another by raising import [tariffs](#) or placing other restrictions on the other country's imports.

Trade wars can commence if one country perceives that a competitor nation has unfair trading practices. Domestic trade unions or industry lobbyists can pressure politicians to make imported goods less attractive to consumers, pushing international policy toward a trade war. Also, trade wars are often a result of a misunderstanding of the widespread benefits of [free trade](#).

KEY TAKEAWAYS

- A trade war occurs when one country retaliates against another by raising import tariffs or placing other restrictions on the other country's imports.
- Trade wars are a side effect of protectionist policies and are controversial.
- Advocates say trade wars protect national interests and provide advantages to domestic businesses.
- Critics of trade wars claim they ultimately hurt local companies, consumers, and the economy.
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A trade war that begins in one sector can grow to affect other sectors. Likewise, a trade war that begins between two countries can affect other countries not initially involved in the trade war. As noted above, this import "tit-for-tat" battle can result from a protectionist penchant.

A trade war is distinct from other actions taken to control imports and exports, such as sanctions. Instead, the trade war has detrimental effects on the trading relationship between two countries because its goals are related specifically to trade. Sanctions, for example, may also have philanthropic goals.

In addition to tariffs, protectionist policies can be implemented by placing a cap on import quotas, setting clear product standards, or implementing government subsidies for processes to deter outsourcing.

Trade wars are not an invention of modern society. Such battles have been going on for as long as nations have conducted trade with one another. For example, colonial powers fought with each other over the right to trade exclusively with overseas colonies in the 17th century.

The British Empire has a long history of such trade battles. An example can be seen in the opium wars of the 19th century with China. The British had been sending India-produced opium into China for years when the Chinese emperor decreed it to be illegal. Attempts to settle the conflict failed, and the emperor eventually sent troops to confiscate the drugs. However, the might of the British navy prevailed, and China conceded additional entry of foreign trade into the nation.

In 1930, the United States enacted the Smoot-Hawley Tariff Act, raising tariffs to protect American farmers from European agricultural products. This act increased the already hefty import duties to almost 40%.² In response, several nations retaliated against the United States by imposing their own higher tariffs, and global trade declined worldwide. As America entered the Great Depression, aided greatly by disastrous trade policies, President Roosevelt began to pass several acts to reduce trade barriers, including the Reciprocal Trade Agreements Act.

Beginning in January 2018, former President Trump imposed a series of tariffs on everything from steel and aluminum to solar panels and washing machines. These duties impacted goods from the European Union (EU) and Canada, as well as China and Mexico. Canada retaliated by imposing a series of temporary duties on American steel and other products. The EU also imposed tariffs on American agricultural imports and other products, including Harley Davidson motorcycles.³

By May 2019, tariffs on Chinese imports impacted nearly \$200 billion of imports. As with all trade wars, China retaliated and imposed stiff duties on American imports. A study by the International Monetary Fund (IMF) shows that U.S. importers of goods have primarily shouldered the cost of the imposed tariffs on Chinese goods. **These costs are eventually passed on to the American consumer in the form of higher prices, which is the exact opposite of what the trade war is intended to accomplish.**

Although the United States and Russia are not engaged in a traditional trade war, U.S. President Joe Biden announced sanctions against Russia on Feb. 22, 2022, in response to Russia's military aggression against Ukraine. The sanctions include blocking two Russian banks that finance the military, market restrictions on Russian sovereign debt, and targeting individual Russian elites.⁶

The advantages and disadvantages of trade wars in particular, and protectionism in general, are the subjects of fierce and ongoing debate. Proponents of protectionism argue that well-crafted policies provide competitive advantages. By blocking or discouraging imports, protective policies throw more business toward the domestic producers, which ultimately creates more American employment. These policies also serve to overcome a trade deficit. Additionally, proponents believe that painful tariffs and trade wars may also be the only effective way to deal with a nation that continues to behave unfairly or unethically in its trading policies.

Pros

- Protects domestic companies from unfair competition
- Increases demand for domestic goods
- Promotes local job growth
- Improves trade deficits
- Punishes nation with unethical trade policies

Cons

- Increases costs and induces inflation
- Causes marketplace shortages, reduces choice
- Discourages trade
- Slows economic growth
- Hurts diplomatic relations, cultural exchange

Critics argue that protectionism often hurts the people it is intended to protect long term by choking off markets and slowing economic growth and cultural exchange. Here are some of the deleterious effects:

- 1) **Consumers may begin to have less choice in the marketplace.**
- 2) **They may even face shortages if there is no ready domestic substitute for the imported goods that tariffs have impacted or eliminated.**
- 3) **Having to pay more for raw materials hurts manufacturers' profit margins.**
- 4) **As a result, trade wars can lead to price increases—with manufactured goods, in particular, becoming more expensive—sparking inflation in the local economy overall.**

While running for President in 2016, President Donald Trump expressed his disdain for many current trade agreements, promising to bring manufacturing jobs back to the United States from other nations where they had been outsourced, such as China and India. After his election, he embarked on a protectionist campaign. President Trump also threatened to pull the United States out of the World Trade Organization (WTO), an impartial, international entity that regulates and arbitrates trade among the 164 countries that belong to it.⁷

In early 2018, President Trump stepped up his efforts, particularly against China, threatening a substantial fine over alleged intellectual property (IP) theft and significant tariffs. The Chinese retaliated with a 25% tax on over 100 U.S. products.

Throughout 2018, the two nations continued to threaten each other, releasing lists of proposed tariffs on various goods. Although China responded with tariffs of its own, the American duties did have an impact on the Chinese economy, hurting manufacturers and causing a slowdown. In December, each nation agreed to halt imposing any new taxes. The tariff war cease-fire continued into 2019. In the spring, China and the United States seemed on the verge of a trade agreement.

At the beginning of May, Chinese officials took a new hard line in negotiations, refusing to make changes in their company-subsidizing laws and insisting on the lifting of the current tariffs. Angered by this apparent backtracking, President Biden doubled down, announcing on May 5, 2019, that he was going to increase tariffs, as of May 10, from 10% to 25% on \$200 billion worth of Chinese imports.⁴ **He may have felt emboldened by the fact that the U.S. trade deficit with China had fallen to its lowest level since 2014. However at the end of the day, have the tariffs boosted American production of the tariffed items?**

- 1) The steel industry has not improved in the US since tariffs were imposed by Trump nearly a decade ago.. In 1967, steel production in China was just 3% of global output. Today, China produces 1 billion tons of steel, or 54 percent of global output. In contrast, since its peak, the US production of steel has declined by 40% and now stands at 6.8 million tons. To think that tariffs can revive American steel making even to its best days, and then beat China is delusional.
- 2) In aluminum, the US produces this output in the amounts achieved by Iceland which has 382,000 people or 80,000 tons and China does 42 million tons. For the US to catch up, it will take a herculean effort that cannot be organized behind tariff walls because young people in America don't want to do factory jobs (they prefer to earn money from making TikTok videos).
- 3) In solar panels the US produces around 2% of world output. In contrast, China's solar prowess is staggering. With a whopping 430 GW solar capacity the country is the largest producer of solar energy in the world and in solar panels, China accounts for 78 percent of all panels. And this has been accomplished as tariffs against China's solar industry has been ongoing for 12 years.
- 4) In EV car batteries, China makes 75% of all such batteries in the world. The US makes next to nothing outside of Tesla. And China leads, by a long shot, all the technologies in car batteries from the raw materials to entire chains integrated into ev production

5) Finally, the Chinese item that is effectively banned from the US is electric vehicles itself via the 100 percent tariff. China makes the best ev's in the world and they are inexpensive. The Biden measure to exclude Chinese evs will lead to eventual degradation of this American industry and it is not just consumers who won't have access to these excellent products. American business will not be able to buy industrial inputs such as electric trucks at low cost and this will increase the cost of production of all American business and render it uncompetitive.

- To think that tariffs can change this equation is just fantastical.

Here is an article from a think tank on this very important confrontation:

Four years into the trade war, are the US and China decoupling?

US imports of some Chinese products have tanked. Others are higher than ever. Trump's selective trade war continues to matter.

[Chad P. Bown](#) (Peterson Institute of International Economics)

October 20, 2022 5:00 AM

For many decades China and the United States have been locked in such a tight economic embrace that it is challenging to quantify whether, how, or why the embrace may be weakening. **Are the mounting tensions, bordering on hostility, between the two superpowers causing their economies to “decouple”?**

Yes and no. On the one hand, US imports of certain products from China—including semiconductors, some IT hardware, and consumer electronics—have fallen dramatically. Even clothing, footwear, and furniture imports are down.

But on the other, imports from China of laptops and computer monitors, phones, video game consoles, and toys are higher than ever. Demand for these products surged in response to the COVID-19 pandemic. Stuck at home, Americans switched their spending away from services and toward many of these goods manufactured in China.

US and Chinese policymakers certainly seem determined to reduce the two countries' economic interdependence, built over many decades but now buckling under the weight of their animosities. So far, the decoupling that is—and is not—occurring is partly the result of President Donald Trump's trade war, the selective way it was waged, and the continuation of many of those policies under the Biden administration. A more recent motivating factor that may be spurring decoupling is the desire for increased diversification of imports to make supply chains for certain goods more resilient. Other drivers include human rights, democracy, and geopolitical concerns.

But the data also show something else. Even if policymakers foresee long-run benefits in disentangling the two economies, their choices come with immediate costs. **These costs include product shortages, as supply chains struggle to adjust, as**

well as inflation, as companies find it expensive to establish new suppliers. Firms and ultimately consumers need to prepare to pay the price for the new policy-induced reality.

TOTAL US IMPORTS FROM CHINA HAVE BEEN DOWN SINCE THE ONSET OF THE TRADE WAR

For 15 months beginning in July 2018, the Trump administration applied tariffs to more and more imports from China. Thus far, the Biden administration has chosen to keep those duties in place.

Overall the trade war has reduced US goods imports from China (figure 1). Imports declined immediately after tariffs were imposed, falling further beginning in March 2020 as global trade collapsed in the wake of the COVID-19 pandemic, and have since recovered only slowly. Today, US imports from China (red line) remain well below the pre-trade war trend (dashed line), as defined (conservatively) by US imports from the world, and have only recently returned to pre-trade war levels of June 2018. **China is now the source of only 18 percent of total US goods imports, down from 22 percent at the onset of the trade war.**

In comparison, current US imports from the rest of the world are 38 percent *higher* than pre-trade war levels and are even *above* trend (blue line). With a few exceptions, these imports were not hit with new US tariffs.^[3] They have also recovered strongly following the onset of the pandemic.

After conducting an investigation under Section 301 of the Trade Act of 1974, the Trump administration began by imposing [tariffs](#) of 25 percent on products covering roughly \$34 billion of US imports from China in July 2018 (List 1) and on \$16 billion of imports in August (List 2).^[4] When China retaliated, the [trade war](#) continued with Trump imposing 10 percent tariffs on an additional \$200 billion of imports in September 2018 (List 3), increasing the rate of those duties to 25 percent in June 2019. In September 2019, Trump hit another \$102 billion of imports (List 4A) with 15 percent tariffs, subsequently reducing them to 7.5 percent upon implementation of the US-China Phase One agreement in February 2020. (The administration identified another set of products covering most of the rest of US imports from China of more than \$160 billion—List 4B—for which it scheduled tariffs to go into effect on December 15, 2019. It never imposed those duties and cancelled them upon the initial announcement of the Phase One agreement on December 13, 2019.)

TRUMP'S TRADE WAR TARIFFS AFFECTED IMPORTS IN EXPECTED WAYS

As expected, the trade war has had the largest impact on imports from China of products hit with the highest US tariffs. US imports from China of goods currently facing a 25 percent duty (Lists 1, 2, and 3) remain 22 percent below pre-trade war levels (figure 2). US imports of those same products from the rest of the world are now 34 percent *higher*. US imports from China of products currently subject to 7.5 percent tariffs (List 4A) remain 3 percent below levels in August 2019 (right before imposition of tariffs on those products), whereas comparable imports from the rest of the world are now 45 percent *higher*.

Yet, US imports from China of certain products have surged. Imports of products never hit with trade war tariffs are now 50 percent higher than immediately prior to the trade war (see again figure 2). (US imports from the rest of the world of those same products are also up but by only 38 percent.) **Products not facing tariffs made up roughly 33 percent of total US imports from China before the trade war and have grown to 47 percent today (see appendix table).**

US IMPORTS ARE SURGING FOR SOME CHINESE PRODUCTS NEVER HIT WITH TARIFFS

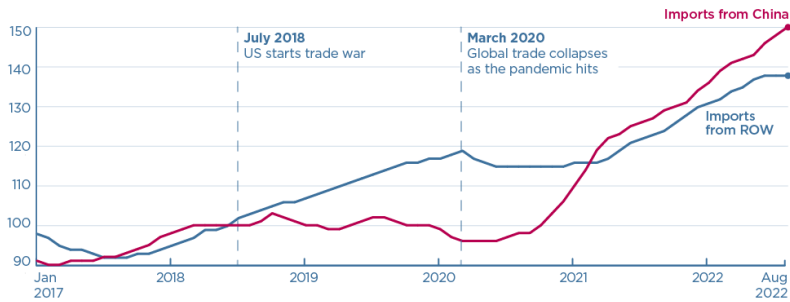
Beginning in 2020, COVID-19 lockdowns led many Americans to work, school, and play from home, which sharply increased demand for certain products, many of which were imported predominately from China. Laptops and computer monitors, phones, video game consoles, and toys are examples—combined they made up 21 percent of total US imports from China before the trade war, growing to 27 percent today (see appendix table). Coincidentally, the Trump administration had earlier decided to not apply trade war tariffs on these and other selected products. US imports from China of these goods have grown rapidly (figure 3, panel a). Though there is some evidence of diversification and changes to foreign sourcing in these products' supply chains, US-China decoupling is not quite evident here.

Take laptops and computer monitors. Growth in US imports from both China and the rest of the world has been strong, with imports from each up roughly 50 percent since prior to the trade war (figure 3, panel b). Thus, shares of US imports have barely budged—China remains the source of 92 percent of US imports of laptops and computer monitors, with Taiwan and Vietnam each making up roughly 2 to 3 percent (panel c).

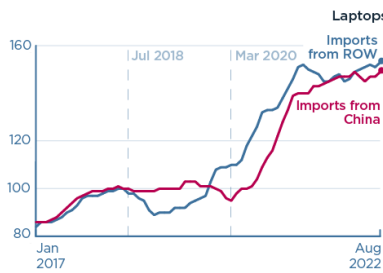
Figure 3

US imports from China of products not hit with any trade war tariffs have increased and show little evidence of decoupling

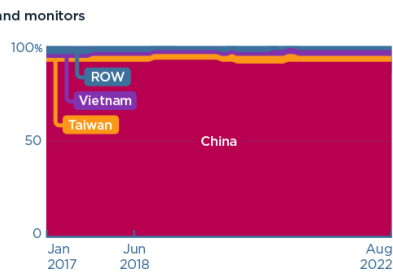
a. Value of US imports of products not hit with any trade war tariffs, 2017–2022 (June 2018 = 100)



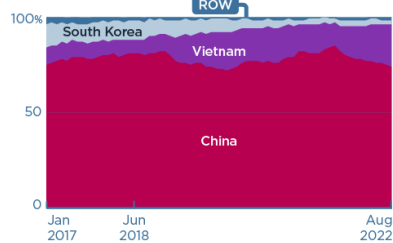
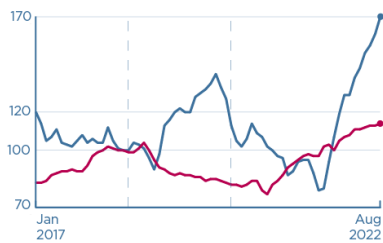
b. By product (June 2018 = 100)



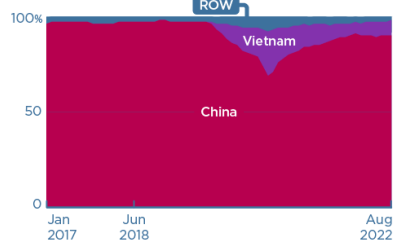
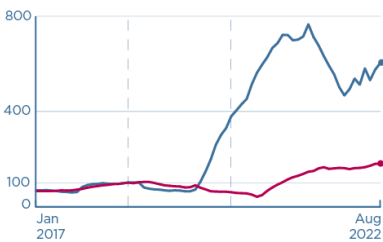
c. Trading partner share of imports by product



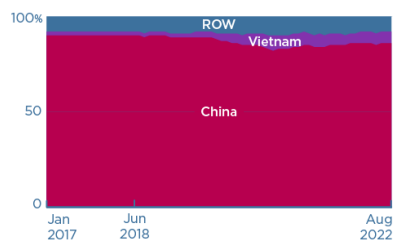
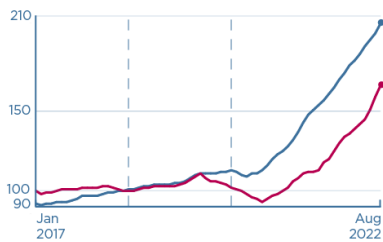
Phones, including smartphones



Video game consoles



Toys



ROW = Rest of world

Note: Indexed value of US monthly imports, not seasonally adjusted, 12-month trailing sums. Trade war tariffs refer to the group of products subject to the US tariffs imposed on imports from China under Section 301 of the Trade Act of 1974.

Source: Constructed by the author with US import data from US Bureau of the Census. For product definitions, see underlying data files.

US imports of phones—including smartphones—have increased from both China (14 percent) and the rest of the world (70 percent). While declining in relative terms, 74 percent of US imports of phones are still sourced from China. Most noticeable is Vietnam’s increased share of US phone imports from below 10 to 22 percent. In 2019, [Samsung](#) closed its last mobile phone plant in China, moving assembly to lower-cost locations like Vietnam (and India), in part, because it was reportedly also losing out in the Chinese market to Chinese firms like Huawei and Xiaomi. But Vietnam’s gain in US imports has come not only at the expense of China. In 2019, [LG](#) also moved its smartphone assembly to Vietnam from South Korea. (Apple has also [recently](#) diversified some of its iPhone assembly by firms like Foxconn and Wistron away from China to India.)

Video game consoles tell a similar story. US imports from China have increased by 82 percent. In 2019, however, [Nintendo](#) indicated it was moving some of its Switch assembly from China to Vietnam. (The *New York Times* [reported](#) some Microsoft Xbox consoles are now being shipped from Vietnam in addition to China.) Indeed, US imports of consoles from the rest of the world have grown five-fold since the onset of the trade war. Yet, because that growth started from such a low base, the United States still imports 90 percent of video game consoles from China.

US imports of toys like board games—e.g., chess, checkers, and backgammon—as well as playing cards from both China and the rest of the world are up considerably. Vietnam has increased its share of US toy imports from 3 to 6 percent. But China remains the source of 83 percent of US imports of toys overall.

During the trade war, the Trump administration deliberately chose not to impose tariffs on these products—most of which were on List 4B—worried that, for such identifiable goods, consumers would suffer price increases and attribute them to the tariffs.^[5] Trump [said](#) as much in August 2019, “What we’ve done is we’ve delayed [tariffs on List 4B] so they won’t be relevant in the Christmas shopping season.... Just in case they might have an impact on people.” Trump first [postponed](#) tariffs on those products until December 15, 2019—long after shipments would have arrived to stock shelves before the 2019 holidays—and then ultimately [canceled](#) them altogether upon announcement of the Phase One agreement.

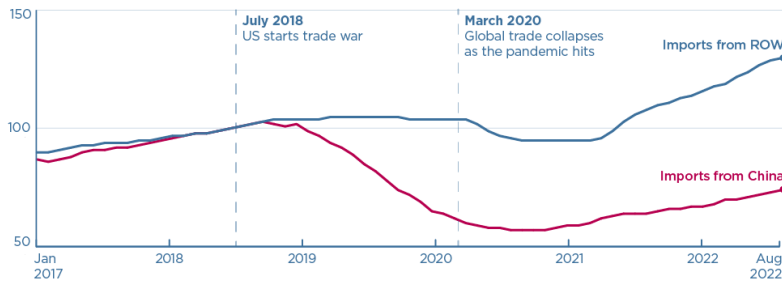
CHINESE PRODUCTS HIT WITH 25 PERCENT TARIFFS HAVE STRUGGLED

At the other extreme are the products that Trump hit with 25 percent tariffs. This group is [dominated](#) by intermediate inputs and capital equipment—much less visible to households—that firms use to make other consumer goods or to provide services. US imports of these products are down overall (figure 4, panel a). Some are lower despite surging US demand during the pandemic, contributing to shortages and higher costs for firms needing those inputs to continue their operations. Such companies were forced to either continue importing from China even with the tariff or spend to establish relationships with new suppliers elsewhere.

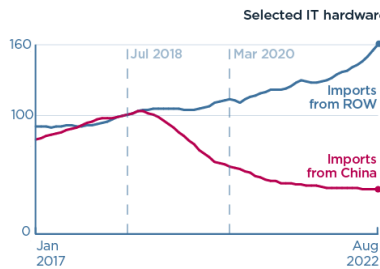
Figure 4

US imports from China of products facing high trade war tariffs show some signs of decoupling

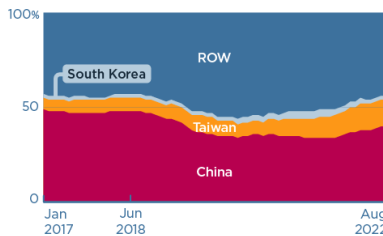
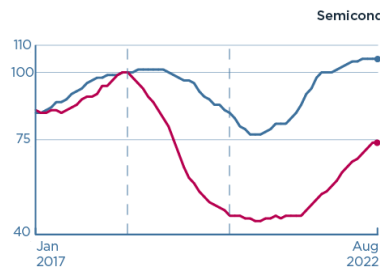
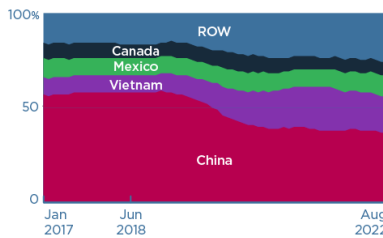
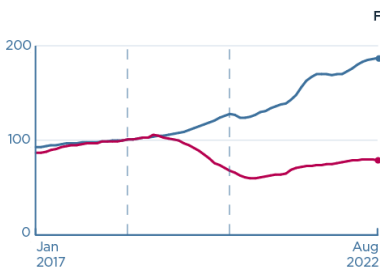
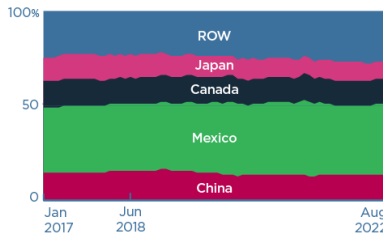
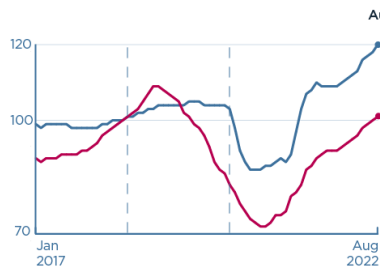
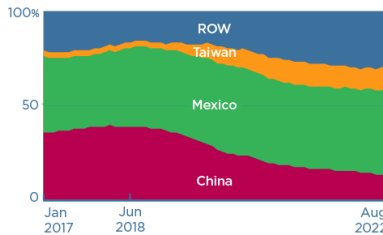
a. Value of US imports on Lists 1, 2, or 3 (25 percent tariffs), 2017–2022 (June 2018 = 100)



b. By product (June 2018 = 100)



c. Trading partner share of imports by product



ROW = Rest of world

Note: Indexed value of US monthly imports, not seasonally adjusted, 12-month trailing sums. Semiconductors only indexed from import volumes, not values. A "list" refers to the group of products subject to the US tariffs imposed on imports from China under Section 301 of the Trade Act of 1974.

Source: Constructed by the author with US import data from US Bureau of the Census. For product definitions, see underlying data files.

Take IT hardware and consumer electronics in higher demand with the pandemic lockdowns, such as network servers, modems, routers, as well as wireless headphones and smartwatches. US imports from China of these products are down 62 percent since the 25 percent tariffs were imposed, whereas imports from the rest of the world are now 60 percent higher (panel b).^[6] China's share of US imports of IT hardware and consumer electronics has been cut by nearly two-thirds, from 38 to 13 percent (panel c). Mexico is one sizeable alternate foreign supplier of such products. Taiwan has also substantially increased its share of the US import market.

Prior to the trade war, imported auto parts from China were a looming threat to the US industry. Imports from both China and the rest of world fell considerably during the early months of the pandemic, when the auto industry in North America suddenly [halted production](#) in response to the pandemic. US imports from the rest of the world have recovered and today are 20 percent higher, whereas imports from China subject to the tariffs have only just returned to pre-trade war levels. Nevertheless, China's share of US auto parts imports has only dropped from 15 to 13 percent. Unsurprisingly, Mexico and Canada continue to dominate the US market for parts due to the integrated North American auto supply chain.

Social distancing during the pandemic also led households to increase spending on home furnishings. US imports of furniture from the rest of the world have grown by 87 percent; imports from China hit with tariffs remain 21 percent lower. (China's share of US furniture imports has dropped from 57 to 36 percent.) Much of the new sourcing of US imports of furniture has come from Vietnam.

US IMPORTS OF SEMICONDUCTORS FROM CHINA CRATERED WITH US TARIFFS

Semiconductors are perhaps the most telling example of product shortages during the pandemic. The scarcity of chips led automakers to reduce their output in 2021, impacting employment through furloughs in a politically and economically important sector. (In figure 4, panels b and c, data for semiconductors alone are in volume, as opposed to dollar value, terms.)

US imports of semiconductors from China remain 26 percent lower than before the imposition of 25 percent tariffs (panel b). Though imports have increased recently, as late as June 2021, US import volumes from China remained more than 50 percent below pre-trade war levels. Prior to July 2018, China had 47 percent of the US import market in volume terms (panel c). This share fell immediately after the tariffs were imposed, reaching only 39 percent today. Yet, import volumes from the rest of the world have expanded only by 5 percent (see again panel b).

This problem became clear when just one missing chip kept the manufacturing of products ranging from [cars](#) to [refrigerators](#) to [washing machines](#) from being finished. In volume terms, lost imports of semiconductors from China were not being fully replaced from elsewhere.

One reason was that production could not be substituted between Chinese and other chipmakers. China's foundries [specialize](#) in "more mature nodes," producing high volumes of "legacy" chips for low profit margins. Leading foreign firms like Taiwan

Semiconductor Manufacturing Company (TSMC) or South Korea's Samsung manufacture more advanced (and profitable) semiconductors and both did not have idle capacity or an interest in switching to less profitable products. This likely explains why the US semiconductor industry also did not significantly expand production, in addition to the fact that it was running at close to [historical](#) levels of its capacity utilization rate. Given that legacy chips are not particularly profitable to manufacture, and if the United States does not want to import them from China,[\[7\]](#) then who will produce them? That is the question facing America's industrial consumers—like the auto sector—of large volumes of legacy chips.

In dollar terms as well, US chip imports from China remain 22 percent below their pre-trade war levels (not shown in figure 4). However, import values from the rest of the world are up 32 percent, mostly due to the price increase caused by heightened US demand for chips, as opposed to increased volumes offsetting lost imports from China.

To summarize, in each of these four examples of products hit with 25 percent US tariffs, US imports from China declined. Reduced imports were sometimes offset by imports from other foreign sources, but not yet in other cases. Yet, these examples were not unique. In value terms, US imports from China of *all other* products subject to 25 percent tariffs have fallen by 17 percent, even though imports of those goods from the rest of the world are now 33 percent higher (not shown).

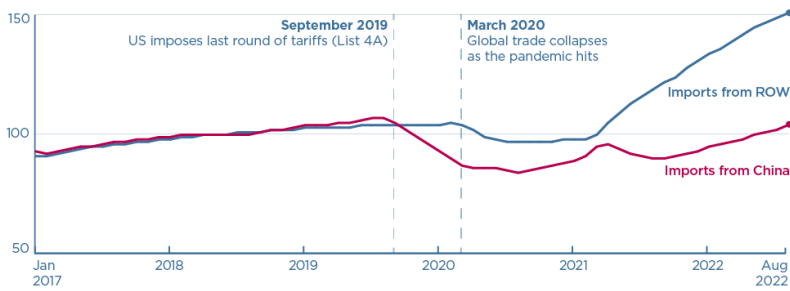
US IMPORTS OF CHINESE PRODUCTS SUBJECT TO LOWER TARIFFS HAVE BEEN UNEVEN

A final set of products, covering 20 percent of US imports from China at the onset of the trade war, were initially hit with 15 percent tariffs in September 2019, which were then reduced to 7.5 percent in February 2020. Overall, imports from China of these goods have only recently returned to their pre-trade war levels (figure 5, panel a). The smaller negative impact on these US imports was partly because the tariffs were imposed at lower rates at the outset, imposed later in the trade war, and subsequently reduced. Imports of these products from elsewhere are now 51 percent higher.

Figure 5

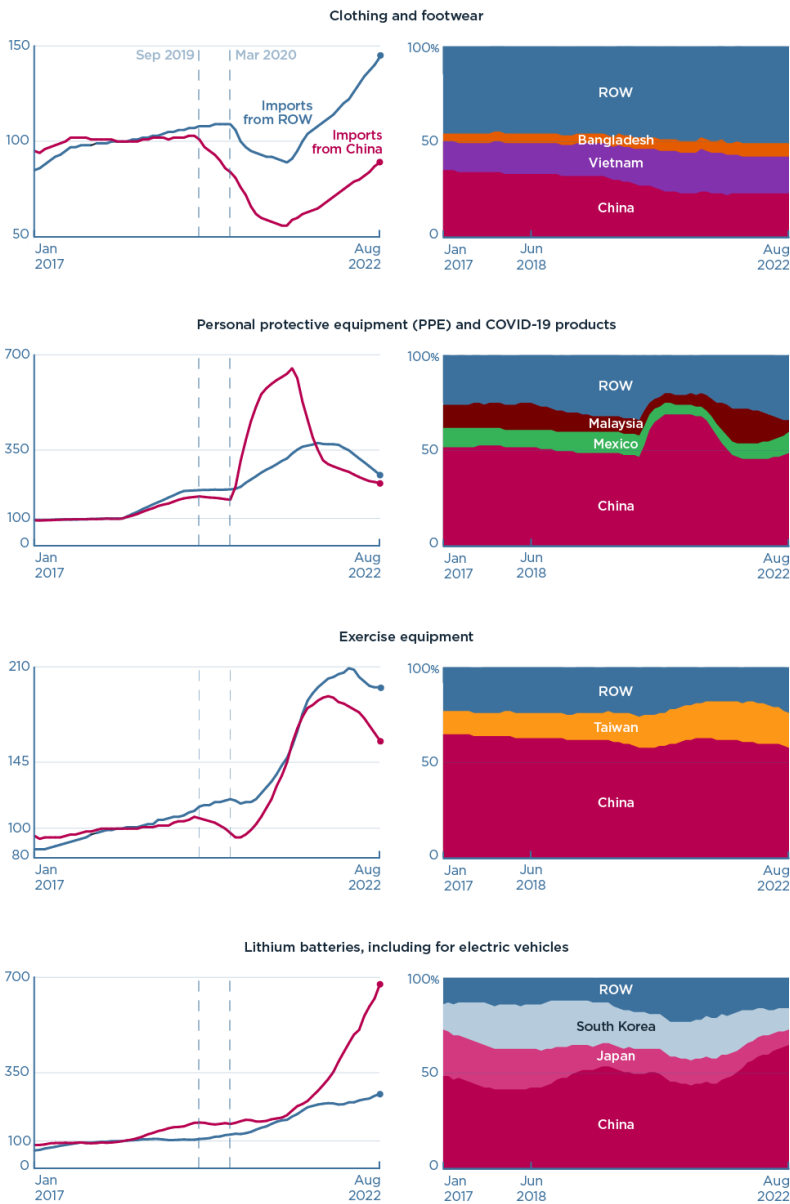
Products facing lower trade war tariffs show mixed signs of decoupling

a. Value of US imports on List 4A (7.5 percent tariffs), 2017–2022 (June 2018 = 100)



b. By product (June 2018 = 100)

c. Trading partner share of imports by product



ROW = Rest of world

Note: Indexed value of US monthly imports, not seasonally adjusted, 12-month trailing sums. A "list" refers to the group of products subject to the US tariffs imposed on imports from China under Section 301 of the Trade Act of 1974.

Source: Constructed by the author with US import data from US Bureau of the Census. For product definitions, see underlying data files.

Clothing and footwear are one example, making up about 7 percent of total US imports from China before the trade war. They remain 11 percent below pre-trade war levels, whereas US imports from the rest of the world are 44 percent higher (panel b). The tariffs may have accelerated an ongoing shift in production of some of these goods out of China's market, as rising labor costs associated with China's economic development were already moving such industries elsewhere. China's share of US clothing and footwear imports has fallen from 34 to 24 percent, while the shares of Vietnam and Bangladesh have increased (panel c).

Personal protective equipment (PPE) and related COVID-19 medical products are a slightly different story. China was the source of roughly 50 percent of US imports of [many](#) such products before the trade war. That dipped once the tariffs were imposed in late 2019—jeopardizing the [preparedness](#) of the US health care system in the face of a pandemic in early 2020. Eventually, the Trump administration did [exclude](#) such products from its trade war tariffs, and by April 2020, US imports from China had resumed, before exploding over much of the rest of 2020, given the increase in US demand. (Price increases were the dominant cause of the sharp increase in values, though volumes increased as well.)

Exercise equipment and lithium batteries are two additional products where imports from China have jumped considerably, despite the trade war tariffs.[\[9\]](#) For both, China is also the source of more than 50 percent of the US import market (panel c). The boom for products like exercise cycles, rowing machines, and treadmills may have been temporarily driven by the pandemic and the inability to access private gyms. The growth in lithium battery imports is partly due to the recent increased US demand for electric vehicles (EVs). However, this growth too may fade over time if the new supply chain sourcing [requirements](#) found in the August 2022 Inflation Reduction Act—explicitly offering subsidies for automakers that diversify their EV battery supply chains out of China—are successful.

These four examples show the additional difficulties of attempting to assess potential decoupling of US imports from China. This complexity is expected, given the size and diversity of the Chinese economy and its involvement in so many different types of products. (As for the other products on List 4A not shown, US imports from China remain 10 percent below pre-trade war levels, while imports from elsewhere are 50 percent higher.)

BENEFITS OF ANY US-CHINA DECOUPLING COME WITH COSTS

Numerous studies have documented the negative impact of the trade war tariffs on the US economy.[\[10\]](#) Tariffs have hurt US manufacturing output, employment, and exports.[\[11\]](#) While those duties may not have caused the inflation pressure that began in 2021, American importers did bear the costs of the tariffs, in the form of higher prices, when they were imposed beginning in 2018-19. (There is little evidence that the tariffs led Chinese exporters to reduce their prices to sell to US consumers.)

The US tariffs that remain in place continue to impede American companies' access to imports. The tariffs make those companies less attractive customers for Chinese firms, some of which may have had limited supplies to sell to other customers globally. Higher costs hurt American firms' competitiveness in the US and

international markets, relative to their non-Chinese competitors operating outside the United States.

INTERPRET THE EVIDENCE WITH CAUTION

For some products, the evidence here shows the United States increasingly sourcing imports assembled in countries other than China. It is partly the result of “trade diversion”—i.e., the United States now buys more expensive imports from third countries that it once bought but no longer buys from China because of the tariffs. The changes in imports shown here are consistent with other [evidence](#) that countries like Vietnam, as well as others in East and South Asia, are now trading more, including with the United States, in response to the US-China trade war.[\[12\]](#)

However, policymakers seeking to achieve “decoupling” need to carefully interpret the evidence documented here. Answers to the most important questions are still unknown.

US tariffs are not the only “cause” of the United States importing less from China. Some labor-intensive production closely associated with much of the clothing and footwear industry was likely relocating anyway, following a trend that was visible even before the trade war. China was losing competitiveness in this industry, relative to other emerging economies, as local wages have increased. (For other products, Vietnam may be rising as a source at the expense of other higher-income countries, such as South Korea.)

The full implications of any “movement” of economic activity that the data reveal also remain imperfect. For example, companies may be adding a separate assembly facility in Vietnam to service US consumers without having to pay the trade war tariffs. The same firms may also be keeping their Chinese facilities to continue to manufacture for the Chinese market as well as for other countries that have not imposed new tariffs on imports from China.

Such redundant investments may have complex and offsetting effects. On the one hand, such investments could improve resiliency if the diversification is useful. If the original US import arrangement involved single sourcing through concentrated suppliers in China, future buyers may find that adding non-Chinese assembly facilities lowers the risk of geographically concentrated disruptions due to climate change (floods, droughts, wildfires), health (pandemics), or geopolitics (military conflict).

On the other hand, redundant investments come with higher costs. There is the initial, one-time expenditure of establishing the new assembly plant. But there may also be additional (and ongoing) costs associated with operating two supply chains, each on a smaller scale than previously when it was all being done in China.[\[13\]](#)

Lastly, these data at most reveal changes only in the final assembly facility that is the source of US imports of a good. Precious little is yet known about any changes to the value-added content of that good the United States is importing. As an extreme example, suppose the final assembly of a consumer electronic product moves from China to Vietnam. The workers involved in the final assembly would change, but if

the product continues to derive the same amount of critical intermediate inputs from Chinese suppliers, who now ship to Vietnam for final assembly by, say, the subsidiary of a Chinese-headquartered firm, then how much is really different?

Policymakers therefore need to interpret even this preliminary evidence of some US-China “decoupling” with extreme caution. Policy decisions made today to reduce economic interdependence between the two countries will have profound implications for both economies, and neither will escape unscathed.

Appendix table: US imports from China subject to Section 301 tariffs, by product list (percent of total imports from China)

Product grouping	Percent of total imports from China	
	Year prior to trade war (July 2017-June 2018)	Most recent year (September 2021-August 2022)
Not subject to tariffs		
Total	33	47
Laptops and monitors	8	11
Phones, including smartphones	9	9
Video game consoles	1	2
Toys	3	5
Others not subject to tariffs	12	20
Subject to 25 percent tariff (Lists 1, 2, or 3)		
Total	47	34
Selected IT hardware and consumer electronics including data servers, modems, routers, wireless headphones, and smartwatches*	5	2
Auto parts	2	2
Furniture	6	4
Semiconductors	1	1
Others on Lists 1, 2, or 3	33	26
Subject to 7.5 percent tariff (List 4A)		
Total	20	19
Clothing and footwear	7	6
Personal protective equipment (PPE) and COVID-19 products**	1	2
Exercise equipment	1	1
Lithium batteries, including for electric vehicles	0	1
Others on List 4A	11	9

Notes: *Smartwatches were technically on List 4A but were not created as a separate 10-digit Harmonized Tariff Schedule (HTS) code until September 2018. For data prior to the trade war they were included with products on List 3 that were subject to 25 percent tariffs.

**Subject to exclusions from tariffs. The Excel file accompanying this blog post provides the exact HTS codes associated with each product grouping. Numbers may not sum to total due to rounding.

Our conclusion from the analysis of economic history is that it is not clear that the American tariffs on Chinese products will yield the desired effect. This is due to the fact that both sides will be impacted by the decrease in Net imports of X-M. Any decrease in X-M will grow GDP and this applies to both sides. In short, China will benefit from the tariffs macroeconomically, just as Russia has benefited from imports declining because of western sanctions since 2022. This is the hard analysis based on basic economics and the experience from the Smoot Hawley Act. America will lose further ground to the Chinese economic juggernaut even though wants to get ahead. The US has this tendency to shoot itself in the foot.

Then at the industrial level, this will be even more damaging to the US. There is the actual track record of the tariffs imposed on Chinese goods over the last decade. None of them have led to a revival of American industrial prowess and all the protected industries in the US have stagnated and in some cases have vanished into irrelevance, such as solar panels, steel or aluminum. And this will be even worse in the case for higher technology content businesses such as car batteries and ev's.

America faces a bleak future not because its industrialists and capitalists are no good, but because the political leadership looks for short cuts that don't work. The more the governments want to engage in protectionism, the worse it will become. Once industries are protected, they will get cosy and begin to stagnate. Tariffs as always are the beginning of the end.

And the US also lacks a working class that wants to engage in the hard work which fosters industrial excellence. In the United Auto Workers Union for example, workers want to work for \$100,000 per year and want to sell product behind a tariff wall. This will never work when Chinese workers will do the same work for a fraction of those wages. For the US, exceptionalism is almost over.

By:

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Fintech Entrepreneur, Money Manager and Blogger

Un-Influencer in a World full of Hubris

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