TradeTalk: The state of play in the Game of Trade

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It seems the old adage rings true. The more things change, the more they stay the same.

The advent of new tariffs brings heightened pressure on already strained US-China economic relations. The effects of this large scale uncertainty, complex global supply chains and a volatile market look destined to continue.

The trade war has had broad impacts globally forcing businesses to play their hand. Many businesses have, to preserve profits and ensure their ongoing brand success, departed long standing economic and political locales to find safety afield.

Against the backdrop of this prevailing uncertainty is an unabating dogmatism that looks set to continue. The US Administration has threatened to make things worse for China, should a deal not be forthcoming. The pledge to place tariffs on the remainder of Chinese goods signals a clear intent - the US is not backing down.

What will this mean for China? The evident risk is that China will no longer be capable of implementing tariffs on the US. The US has a broader range of Chinese imports it can tax. Beijing may be forced to impose non-tariff measures on the US, which by their nature are more insidious and may be its sole method of retribution going forward. It may be coincidence, but already the trade war is having a severe impact on US businesses operating in China. In a recent survey of peak industry groups, more than 40 per cent of US companies declared their intention to relocate in the aftermath of - and ongoing escalation of - trade tensions between Washington and Beijing. This 'exodus' of US companies from China is a stark reminder of the impact trade wars have on business operations in overseas jurisdictions. Many big companies have already been 'spooked' by the ongoing uncertainty, and given tariffs haven't fully reached their zenith in terms of application, it is fair to suggest things are going to get worse before they get better.

The current situation makes for dire reading. It is one riddled with ambiguity which has the potential to derail global economic growth and plunge markets into turmoil. The US and China endgame is a fight that goes beyond both countries, and beyond just trade to technology, affecting global growth and political relations perhaps irreparably.

However, in the midst of this conflict is the often unheralded success of free trade and trade liberalisation. While it is no doubt under threat from the trade war and emerging protectionist sentiment, global views outside the US still seem skewed (mostly) favourably towards trade liberalisation and the reduction of barriers, rather than their adoption.

Fruitless dialogue

The resolution of the trade war is an ongoing struggle, with recent negotiations failing to soften the tension. Talks in Beijing held at the beginning of May fell short in halting the back and forth tariffs that continue to plague global markets.

The US demanded China reduce its subsidies on local industry; a request the Chinese regarded as too intrusive into its domestic affairs. The US seeks to increase the competitiveness of foreign businesses working in the Chinese market, and while China has agreed to allow foreign companies to bid for government contracts, its commitment to subsidising local industries is unlikely to end, needing to maintain favour with Chinese companies, SOE's and broader constituents.

In turn, the latest meetings failed to deliver an end to the enmity between the two sides and the global anxiety facing financial markets. This saw the US implement a further tariffs on USD200 billion of Chinese imports from May 10. Recent talks in Washington, also fell short and instead have come crashing to a halt. Washington outlined Beijing's backtrack on "firm commitments" to remove "market distorting subsidies", a claim Beijing strenuously denies.

Beijing has since retaliated, initiating tariffs on $60bn worth of US goods, from 1 June. These tariffs will affect more than 5,000 US products including beef, lamb and pork, vegetables as well as tea and coffee. The new rates imposed by Beijing will range from 5 per cent-25 per cent.

Looking ahead, should the US impose tariffs on the remainder of Chinese goods as it has already planned, the nature of Chinese retaliation could become more clandestine, impacting US investments and business operations in-country. Given the broad interconnectedness of global businesses, the repercussions this may have on global supply chains and country to country relations could be significant. As outlined above, this is already having broad ranging impacts on US businesses operating out of the middle kingdom.

The dogmatism from both sides seems set to continue for the foreseeable future and long term. There is speculation China is willing to wait it out on the assumption a Democrat President will win in 2020. This is however, a risky manoeuvre. President Trump flagged this on Twitter stating that any "deal will become far worse for (China) if it has to be negotiated in (his) second term". This is a signal of intent and indicates that the US will not back down.

What about Europe?

Meanwhile in Europe, among the swell of uncertainty surrounding Brexit, comes the preparation of retaliatory tariffs against the US. This comes after US subsidies provided to Boeing were followed by the EU's own subsidies for Airbus. The US has since threatened to slap tariffs of $11bn on European goods, including wine, roquefort cheese and aircraft parts. Transatlantic tensions are a further symptom of the growing malaise surrounding free trade and the benefits of trade liberalisation that have delivered dividends over the past 30 years.

The EU, it seems, is unwillingly being drawn into the global trade war. Within its common market, it is intended to be the embodiment of free trade and the benefits that flow from it. Yet, in its time of great vulnerability, assuming the UK does indeed 'Brexit', it is being tested further. In the eyes of many, this paints a pretty bleak view of the international trading landscape.

But is it all that bad?

While the current state of play is unsettling, it is not without a silver lining. The rise of protectionism has been swift and decisive. Notwithstanding the impact this has had on global markets, the majority of countries still favour the reduction of tariffs and recognise the benefits of free trade.

Illustrative of this is the success and implementation of the Comprehensive and Progressive Trans Pacific Partnership (or CPTPP). The US is a notable absentee, yet the agreement between the remaining parties signals a strong intent that mature markets are eager to operate independently and obtain the benefits of free trade, with or without the US. A decade or two earlier, such an agreement without the US would have been largely impossible. Now, pragmatism and the maturity of global markets has prevailed with the agreement coming into effect from 30 December, 2018.

Furthermore, FTA's are continually being ratified, negotiated or implemented. Australia is eagerly awaiting the implementation of the Australia-Indonesia FTA while also scoping the possibility of agreements with the EU, UK and India. The US too has lead the renegotiations of NAFTA (now USMCA) while Europe has recently broadened its free trade portfolio through an agreement with Mexico and Japan. This shows that while the trade war has seen a return to protectionist measures as mechanisms for compelling parties to the table, on reflection, this seems to be more of the exception rather than the rule.

US rhetoric does not match the broader international approach to free trade. Tariffs hurt businesses and therefore consumers, both domestic and external, this fact is not in dispute. Most of the world recognises this.

China, in its attempts to engage the WTO and international community, has demonstrated its appreciation for free trade flows and to maintain the status quo by unilaterally lowering tariffs on a range of goods in both January 2019 and July 2019 on over 2000 different types of goods. Instead, its efforts to comply and advocate for a norms based international order shows that in the midst of such aggression, and unease, the allure of free trade has not subsided.

Meanwhile, the Africa Continental Free Trade Area (AfCFTA) looks set to launch on 30th May 2019. If all African countries jump on board, it will become one of the world's largest single markets, accounting for around $4 trillion in spending and investment. This would be a mighty victory for trade liberalisation amongst the angst present in US-China trade relations.

Three cheers for trade!

You could be forgiven for thinking the global trade landscape was down and out. The trade war is one of the greatest challenges to the global trading system in recent memory. It has the potential to plunge the world's two largest economies and everyone else with it into a state of economic turbulence, one which the world can do without.

Yet, in the midst of this 'chaos' comes the silver lining and a pertinent reminder that the trade war, as a microcosm of protectionism as a whole, is itself the exception, not the rule.

The EU, while battered and bruised from protracted Brexit negotiations remains standing. Many countries, Australia, New Zealand and Korea for example pursue ongoing trade agreements. In addition, Africa is on the verge of a historic implementation of a single market mechanism that would have profound impacts on the continent.

Even as recent as last weekend, the US has appeared to have bucked its typically protectionist trend by suspending tariffs on industrial metal imports from both Mexico and Canada. Albeit, while this is a conciliatory approach designed to see the USMCA pass through congress, it is also a way for the US to launch a call of arms to its regional allies to act against Chinese steel being shipped to the US through either country. In turn, such protectionism is still in force against China, but at least there is some respite for the rest of us.

While it is wise to be wary of what is taking place, not is all as it seems. In spite of all the obstacles coming to the surface between the US and China, the trading landscape, the appetite of nations big and small to increase their trading flows and an almost uniform recognition of the benefits of free trade are not going anywhere.

Let's talk

For a deeper discussion of how these issues might affect your business, please contact:

Gary Dutton, Brisbane
+61 (7) 3257 8783
gary.dutton@pwc.com

Ben Lannan, Melbourne
+61 (3) 8603 2067
ben.lannan@pwc.com

Ross Thorpe, National
+61 (8) 9238 3117
ross.thorpe@pwc.com

Luke Branson, Melbourne
+61 (3) 8603 1993
luke.branson@pwc.com

Stephanie Males, Canberra
+61 (2) 6271 3414
stephanie.males@pwc.com