Virginie ROBERT

Let us start with the assessment of damages, because this trade war has been going on for some time now, and it has caused a lot of difficulties. The Head of the IMF was saying that GDP growth is slowing down, but commercial growth is slowing down. Therefore, Mr Bark, what do you see as the first damages of this trade war already, and we will go back to the reasons afterwards.

Taeho BARK

Yes, the damages, at the beginning, looked insignificant, but as time goes by, especially in the view of economists, the negative effects of cross-tariff retaliation are spreading rapidly into the whole US economy. Of course, the same also applied to China. Therefore, direct damages are taking place in both the US and China. I think in the case of China, producers whose products are exporting to the US are most hurt. This is so because, according to my simple calculation, out of China's total export, 19% is going to the US. It is not a small number. Therefore, exporters in China are hurt very much. These exporters include not only Chinese but also other foreign companies operating in China.

In the case of the US, as Marcus pointed out, the consumers and the users of goods imported from China, and also the US farmers who are exporting agricultural products to China are hurt. We can easily understand this from the simple fact that out of the US total imports, almost 22% is coming from China. It is a large number, and that is why I am saying the US consumers and producers are hurting. Also, the US farmers are hurt because 17% of the total US agricultural exports are going to China.

Therefore, these two countries are clearly hurting. These days many researchers are analysing economic effects on the third countries. For example, Korea, as Dr. ŠaKong mentioned this morning, hurts severely because of the US-China trade disputes. China and the US are Korea's number one and number two trading partners respectively, so Korea is caught by these two big giants. According to the recent WTO report, for the first seven months from January to July this year, Korea's exports were reduced by almost 9%. This is the worst among the top 10 world exporting countries.

How about Korea's exports to China? In the same period, Korean exports to China experienced almost 17% reduction, compared to that of the same period of the previous year. Therefore, Korea is really hurt. Also, if you look at the details, Korean producers of parts, components and equipment which are being exported to China, are seriously hurt because out of our total exports to China, almost 79% are those kinds of items. These are some examples of damages I can provide.

Virginie ROBERT

Yes, those are pretty impressive figures. This morning, around the round table, you were moderating, Gabriel. One of the consequences was also on FDI, direct investments. Can you tell us, or whoever wants to, about the effect that the trade war has on that because of the absurdity it creates?

Gabriel FELBERMAYR

Exactly, so I mean if you look at the big macroeconomic aggregates, investment is by far the most volatile, and it reacts most to news or to changed information, and also to uncertainty. You can postpone investment but you cannot postpone consumption so much; people need to eat and so on.

Therefore this procrastination is what matters so much now, as Olivier Blanchard explained this morning. I mean if you look at Korea, another striking feature of the Korean economy right now is how much investment is suffering. It has
been negative for the last quarters, I think three or four quarters already, and that simply reflects the fact that if you do not know what the markets are in the future, whether there are tariffs or no tariffs, what can you do as an entrepreneur? You can only wait.

What you can also do, and that is the counterargument, and that is valid for example for the United States, you can say if there is a large net importing market, like the United States, and you face, as an exporter from Europe, you face uncertainty about the market access conditions, about the tariffs, then the only you have is actually to produce more in the United States. If you talk to the German car manufacturers, what do they do? They say, ‘Well, we need to restructure our operations in the United States’.

Virginie ROBERT

Therefore it is relocation of factories?

Gabriel FELBERMAYR

Yes, but they do not invest more, because, you know, they traditionally also produce their SUVs in Spartanburg let us say, for the Chinese market, and that market is going down, so it is getting closed off. Therefore, there are two things, there is procrastination, and then there is investment redirection into large markets where you can use investment as a hedge. Therefore, theoretically, the effect of investment is vigorous, but if you go through simple models, the direct effect, so the procrastination effect is much larger, so it is not good for investment.

Virginie ROBERT

Marcus, do you want to add something?

Marcus NOLAND

Sure, so we know that since the United States initiated these tariff wars, the Treasury has collected about USD35 to USD36 billion in tariff revenue, from the special protection, that is a fact.

We have economic models that are now coming out where people are trying to model the effects of this, and obtaining, negative, though not particularly large, results. There is reason to believe that those models are underestimating the effects for two reasons. The first one is the one Olivier spoke about this morning: we have a really hard time capturing in our models the impact of fundamental policy uncertainty, particularly through the impact on investment. That inadequacy we know.

The second thing is supply chains. When Donald Trump was running for president in the summer of 2016, my institution did a project where we tried to model the trade policy proposals of the two major candidates. In the case of Trump, we took his statements at face value, and we were trying to figure out how to model them. We ended up talking to some of our corporate supporters and had some really interesting conversations with them, and I am not going to name the firm, but we had a conversation with one that went something like this: ‘Okay, if Donald Trump puts a 30% tariff on Mexico’, which is what he was threatening to do, and we estimate, or we assess that it is not going to last more than six months, we will just wait it out, and we will lose USDX billion a month. If it is going to last more than six months, then we have to get out of Mexico. Now, if we are going to shut down activities in Mexico, where are we going to start them again?”

The corporate leadership found out they did not understand their own supply chains. To actually make their contingency plans, they had to drill down to the level of individual product line managers, and in the case of this firm, they decided, well, a lot of that production in Mexico would be moved to Singapore. Well, to make room in Singapore, we are going to have to move things out of Singapore, some of that is going to go to China, some of it was going to go to central Europe, I think the Czech Republic.

Therefore, you had a situation in which threatened action against Mexico could end up with increased production in the Czech Republic. There is no way any economist, using a model and publicly-available data, is going to come up with
that result. Therefore, we know that protectionism is bad, but our models are not good at capturing some of the basic channels through which these policies operate.

Virginie ROBERT

Okay, Gabriel and then Karl, yes.

Gabriel FELBERMAYR

Just, you are totally right Marcus, but what this does is it gives huge incentives to us economists, and you know, there is a lot of research now in how to incorporate supply chains into models, and that is a good thing about Donald Trump. It creates a lot of variance in the data, and it creates a lot of things that we thought are not worthwhile investigating, and now we think we need really to understand those old-fashioned items like tariffs. That is the only positive that I have.

Marcus NOLAND

Or we should give Donald Trump and Boris Johnson the Nobel Prize in Economics for the stimulation of new research.

Virginie ROBERT

They are doing good for your profession, yes. Karl?

Karl BRAUNER

Yes, I only wanted to point out the 37 billion that the Treasury collected, they collected from the American consumer. They did not collect it from the Chinese or from anybody. I see your hand movement. I know your studies on it. You say that there is a benefit because the Chinese lower their prices, but the fact remains that 37 billion were collected from the American consumer.

Taeho BARK

Can I add one more thing about international investment, although this is not my research area? We know that the US has been emphasising the importance of the return of the US companies operating abroad back to the US again. President Obama mentioned “Remaking America”, and also President Trump advocated for “America First.” Both administrations have provided lots of incentives to induce the US companies who are operating abroad to come back to the US.

Virginie ROBERT

Has that happened?

Taeho BARK

That is what I am going to explain. I do not have any statistics about recent years. But from 2010 to 2016, a global consulting company A.T. Kearny actually investigated the cumulative numbers for that six-year period and found more than 800 firms returned back to the US. They are talking about this phenomenon as “reshoring” rather than foreign investment. That could actually happen. I visited Taipei before I came here, and Taiwan is also doing the same thing. Lots of Taiwanese companies which were operating in China returned to Taiwan. Of course the government provides numerous incentives. In other words, under this kind of uncertain world trade environment, the governments of many countries are really pursuing so-called “inward looking” trade and investment policies. Then the global investments which will go everywhere in the world will be reduced. Eventually this will give negative impacts on the world economic growth in the future.

Virginie ROBERT
It is interesting, what you were saying about the dismantling of the value chain, because there was a report from the World Bank, last week actually, asking for more globalisation, saying that globalisation had been the way to take countries out of poverty, and if you start breaking the value chains, you are going to put them back where they were, or you are not going to help everybody rising. Do you agree with that opinion?

Gabriel FELBERMAYR

Yes, absolutely. I think the multilateral order that we had let us say until 2010 or so produced convergence, you know, and the period of hyper-globalisation some say led to the great convergence. In a world where power dominates, and where international rules are no longer taken for granted, can be changed all the time, all this uncertainty, this hurts small countries most. The largest countries have big, uniform, single market at least. Therefore, it is maybe not a surprise that the country with the largest single market, the United States, is doing this, but we should expect that this breakdown of multilateral order hurts the poor, smallest countries most, to the extent that they are not able to organise themselves. If you look at initiatives like the African continental free trade area, you know, that could counterbalance that, but if that is not going on then we will see this convergence process stopped.

Actually, there are already signs of that, because the trading world has become very weak. We are not getting the stimulus from trade to those economies as we used to.

Virginie ROBERT

Karl?

Karl BRAUNER

Yes, I wanted to point out that the value chains are of course disturbed by tariffs, but they are also very strongly disturbed by rules of origin. The new agreement, the US MCA is one of the examples where you have rules of origin that I would call perverted, and they have a real effect also on what can be sourced. I had a meeting with BOSH, and BOSH has set up a huge data centre in Vietnam where they want to optimise the components that they deliver to other producers in order to make sure that the rules of origin are met. This is highly complex and is getting more complex.

Virginie ROBERT

Yes, Marcus.

Marcus NOLAND

Trump is a protectionist, so one of the characteristics of the renegotiations, or the negotiations of these trade deals is they move them away from free trade. Therefore, in the case of the United States Korea deal, we moved it away from free trade by extending the periods of liberalisation. In the case of the agreement that we have with Canada and Mexico, we did it through rules or origin and other measures, such that we call it NAFTA 0.8, because it is actually moving away from free trade. You see the same pattern with respect to some of these other deals as well.

Virginie ROBERT

I was wondering, you know, I am just going to ask my question and you can answer it right away. Well, go ahead.

Taeho BARK

Actually, I want to make a comment on Karl’s point. I would like to draw your attention to a specific clause included in the USMCA. This clause is on trade in automobiles and their parts. It says that if you want to use USMCA, in other words, if you would like to export automobile by paying no tariff, 35-40% value of the outputs must be produced locally by labourers whose hourly wages are above USD 16. We have never seen such very specific conditions included in any trade agreements. That means, considering that Mexican hourly wage is very low, automobile manufacturers in
Mexico must import some of parts and components from the US and produce final goods using these and export them back to the US.

**Virginie ROBERT**

Yes, which is a little stupid because the idea was to raise salaries.

**Gabriel FELBERMAYR**

Let me add a little anecdote from research. I have done some work on rules of origin, and what we can find there is that almost always, rules of origin have no real economic justification. I mean they are usually meant to be there to avoid bilateral preferential trade agreements that the third countries don’t benefit from the trade preferences. However, we know there is some-

**Virginie ROBERT**

Well, it is a defence mechanism, is it not?

**Gabriel FELBERMAYR**

Yes, but in most cases, really in most cases there is no danger of the so-called trade deflection anyway because it is costly to transport goods, and because the tariff structure is not such that it makes this deflection very profitable. Therefore, you know, we have outrageous cases of rules of origin, like in the US that are clearly protectionist, but I would say that almost all rules of origin is hundreds of pages. Also, in EU trade agreements, you know, it is a lot of stuff, and most of it has no rational-

**Virginie ROBERT**

Well, the French care a lot about it, you know?

**Gabriel FELBERMAYR**

-because trade deflection would not happen. Yes, I know, it is protectionist.

**Virginie ROBERT**

Our cheese, our wine, you know, we like to protect it.

**Gabriel FELBERMAYR**

Well, I mean there are others. There is the GIs that protect these food items, but the point is that, you know, there is a legitimate case for rules of origin to avoid trade deflection, but there is no economic basis for that, very rarely. Therefore, what then remains is really just the protectionist element, and that has been the case for the last 30 years. Now, the Trump administration is playing it very hard on that, but it is not a new feature. The EU knows that quite as well. If you look at those rules of origin, how detailed they are, you know? Sometimes it is really ridiculous, and that is true also for example in the EU/Korea trade agreement. It is not something that we can blame on the current US administration alone.