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How will they impact developing countries?

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Bonn, 23 March 2018. Friday last week saw the entry into force of the punitive tariffs on steel and aluminium imports agreed by the United States. During the first year of Donald Trump's presidency, US trade policy, while characterised by aggressive rhetoric, was barely followed up with any actions. The US pull-out from the Trans-Pacific Partnership (TPP) on Trump's first day in office and the forced renegotiation of the North American Free Trade Agreement (NAFTA) were the only events to cause a stir. The massive increase in tariffs on steel and aluminium and the measures announced last week against China have the potential to spark an escalation of protectionist measures. The impact that this will have on developing countries will largely depend on the responses of other trading powers, especially the European Union and the emerging economy of China.

Taking major emerging economies out of the equation, the short-term impact of tariff increases on developing countries should be minimal. While the United States is increasing tariffs on all steel and aluminium imports, this barely affects developing countries, as they only account for a very small proportion of global steel trade. It is primarily industrialised nations and emerging economies that are affected by the US tariff rises. It was therefore logical for the G20 finance ministers to discuss this topic at the G20 summit in Hamburg and this week in Argentina, albeit with limited success. The G20 would in fact provide the right context for negotiations. After all, the trade issue is associated with excess capacity (especially in China) and macroeconomic policies (primarily the massive German current account surpluses). This situation requires concessions on all sides if an open, cooperation-based trade system is to be maintained.

However, it is the medium- and long-term impacts of the US tariff increases that give developing countries more cause for concern. These nations are highly integrated in global value chains, at the top of which are companies from industrialised nations and, increasingly, from emerging economies. With the goal of improving the cost-effectiveness and efficiency of production, large and medium-sized firms have increasingly been splitting up production processes since the 1990s. In order to participate in global trade, companies from developing countries must specialise in individual tasks within global value chains instead of attempting to manufacture entire products themselves. As such, an upward spiral in tariffs between the United States, the EU and China would also have a negative impact on developing countries, transmitted through the value chains. This is because products manufactured by European and Chinese firms that can no longer be sold on the US market also contain intermediate products from developing countries. If we use the analogy of a moving train to depict the effect of tariffs on global value chains, then every impact at the head of the train can also be felt in the last carriage.

Developing countries would also be affected by the weakening of the multilateral trade system. Both Brussels and Beijing announced that they would be taking action against Washington's tariff increases at the World Trade Organization (WTO). While resolving trade conflicts within an independent, rule-based system is generally the correct course of action, the outcome of the international arbitration process is uncertain. This is primarily due to President Trump's explanation that it is necessary to increase tariffs on steel and aluminium imports in order to avert the threat to US national security. However, it is precisely the exemption criterion of national security that is ill-defined in WTO regulations.

If Trump's explanation prevails in a WTO process, companies from other sectors and countries could also be encouraged to push for tariff barriers in their own national security interests. Such legislated protectionism would also affect sectors of relevance to developing countries. Were the United States to be defeated in the arbitration proceedings, then Washington would likely take this as an opportunity to put the final nail in the coffin of the WTO. Since taking office, President Trump has not held back in expressing his dislike of the WTO and is currently blocking the appointment of key judges to the WTO's Appellate Body. Any further weakening of the WTO would be especially fatal for developing countries, as it is precisely the weak actors in the world trade system that rely on an institution guided by rules rather than the will of the powerful.

The situation appears muddled. The level of impact of Trump's protectionist tariffs on the trade system depends on the responses of the other major trade powers. It is justifiable for a country to take direct countermeasures in the steel and aluminium sector to guard itself against excess capacity and protect jobs. Further-reaching retaliatory measures, however, are counter-productive; they would merely provoke the next counter-blow from the United States. Such escalation must be prevented, not least in the interests of developing countries.