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ECONOMIC UPDATE

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February 3, 2012

The voice of the trade hawk is heard in the land

Some fear America is about to go protectionist. Others fear it won't. Where you stand on this issue depends on where you sit. Sit in the chair of the CEO of a major exporter, and you fear protectionism and the ever-rising spiral of retaliations. Sit in the chair of the president of a trade union, and you welcome what others call protectionism and you call fair trade. Sit in the chair of a Wal-Mart customer and you fear anything that will drive up prices, putting pressure on your over-stretched budget. Sit on the sofa of an unemployed worker whose lost job is being filled by a \$1-a-day Chinese worker, and protectionism is just what the nation needs -- unless you just paid \$69 for a made-in-China tire

that cost \$39 before the US imposed high tariffs on imports of these low-end tires.

There is little question that the voice of the trade hawk is heard in the land. President Obama used his State of the Union speech to announce plans to increase the tax burden on companies that are "moving jobs and profits overseas", and "start rewarding companies that create jobs right here in America" by lowering their taxes. He added a boast that his administration has brought trade cases against China "at nearly twice the rate as the last administration," and a promise to create an Enforcement Task Force to ferret out violations of WTO trade rules by China. Just what the

ferrets will do with their discoveries is unclear.

This is more than a broad hint to the trade unions to make some noise when China's vice president Xi Jinping, heir apparent to the regime's leadership, and touted as a free(ish) market sort, visits Washington on February 14. A group of top trade union leaders will announce on Tuesday a long-planned campaign to pressure Obama to bring a barrage of trade cases against China. They are emboldened not only by the President's speech, but by a victory in a WTO case involving China's curb on exports of some raw materials, the anger aroused by China's imposition of almost \$5 billion in annual tariffs on imports of sports utility vehicles and big cars, and by their congressional allies. "The Chinese have cheated," says Senator Sherrod Brown, Democrat from Ohio; they are currency manipulators, charges Senator Chuck Schumer, a New York Democrat.

Throw in the fact that this is an election year, in which Republicans who normally oppose protectionist measures are reluctant to antagonize the blue-collar workers whose defection from the Democrats propelled Ronald Reagan into the White House. Mitt Romney, the Republican most likely to get his party's nomination, promises to

crack down on China on his first day in the Oval Office.

Developments underlying this lurch towards protectionism are unlikely to go away. China remains under pressure to provide millions of jobs for its increasingly urbanized work force, and is being forced to counter social unrest by raising wages. That makes its exports more expensive, and increases pressure on the regime to compensate by maintaining an undervalued currency that keeps Chinese goods cheaper in foreign markets.

The Treasury continues to duck its legal responsibility to label China a currency manipulator, avoiding the logical conclusion of its finding that the yuan is "substantially undervalued" by citing a 12% rise in the Chinese currency against the dollar in the past 18 months, and China's promise of still more high-level meetings to discuss the matter, the latter a tactic successfully used by Iran and North Korea to persuade the Obama administration to acquiesce in the status quo in matters nuclear.

Meanwhile, an alliance of greens and the military will add to pressures to do something about China's trade practices. The military sees the regime's trade surpluses being converted into aircraft carriers and missile systems that threaten American

interests in Asia, and the greens its subsidization of China's wind and solar industries as destroying American firms. Never mind that this is a case of the green pot calling the Chinese kettle black: the greens successfully lobby for subsidies for America's producers of solar panels. The inability of several of those firms to compete with China's entrants into the market, especially those US companies in which contributors to the Obama campaign are prominent investors, is bringing into disrepute the tax payers' subsidization of green technologies that the market deems inefficient. So, end China's subsidies, but continue America's, a bit of environmentalists' hypocrisy. But let's be fair: the greens have a point when they claim that China's state-owned enterprises (SOEs) benefit from cheap credit, protection from imports, and all sorts of support from the government.

The disadvantage at which this Chinese model of economic development has put U.S. firms has at long last prodded our government into action -- not to mention the fact that this is an election year. In what John Neuffer of the Information Technology Industry Council called "a paradigm shift" in an interview with *The Wall Street Journal*, Secretary of State Hillary

Clinton and Under Secretary of State Robert Hormats have joined Treasury Secretary Timothy Geithner in attacking these "distortions" that hurt American firms. Unfortunately, the Chinese don't find this trio, or the U.S. government, sufficiently fearsome to change their policy. After all, Geithner conceded in Davos, "I don't have magic answers." In short, all of these threats are "words, words, words", famously dismissed as mere annoyances by Eliza Doolittle in one of her turns in "My Fair Lady".

Unemployed Americans, and others nervous about their futures, can be forgiven for being as unimpressed as the Chinese by the Clinton-Hormats-Geithner trio. They see little reason not to blame cheap Asian labor -- the word "coolie" reappears now and then -- for their troubles, especially when stories of the working conditions of Asian workers in iPhone and other factories hit the front pages of the papers. It is understandable that jobless workers conclude that these lower-paid workers, toiling in conditions unacceptable here, have displaced the better-paid Americans who were once the backbone of the aspirational middle class.

Never mind that the jobs market is improving. Last month the economy added 243,000 jobs, 257,000 in the private sector,

dropping the unemployment rate to its lowest level in three years -- to 8.3% from 8.5% last month and from 9.1% last August. Average hourly earnings also rose. Frosting on this cake is the report that earlier estimates of job creation in November and December were revised upward by 60,000. But close to 24 million Americans can't find full-time work, and some 5.5 million have been out of work for 27 weeks or longer. They remain a core constituency for protectionism.

Free trade, too, has its advocates, and not only CEOs of big multinationals. America's farmers are flourishing, in good part because exports of farm commodities are booming. The Distilled Spirits Council is trumpeting the virtues of the US-Korea Free Trade Agreement, which cut duties on whisky and bourbon imported by Korea's drinking class, resulting in a 16.4 increase in US exports, largely of "super-premium" brands. Korea, along with China -- yes, China -- Brazil, India and other developing countries now account for a majority of American exports, which are soaring.

My own guess is that we are destined to hear a great deal of protectionist noise in the run-up to the election. But nothing much of real consequence will happen until after November. After all, why

should trade issues be treated any differently from all of the other unattended problems we face?