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U.S.-CHINA TRADE WAR: FARMERS CAUGHT IN THE CROSSFIRE

Clark Packard

INTRODUCTION

It is becoming increasingly clear that there will be no quick resolution or permanent solution to the ongoing trade war between the United States and China, the world's two largest economies. From the start, a series of policy mistakes by the Trump administration have squandered a prime opportunity to address certain legitimately concerning Chinese commercial practices. And, while the administration's mitigation efforts may temporarily help a limited number of agricultural producers, it will do so at the long-term expense of our ability to open up foreign markets for American commodities and livestock.

Put simply, this means that America's farmers and ranchers find themselves caught in the crossfire.

To recap, in March of 2018, the United States Trade Representative (USTR) released a lengthy report documenting a number of problematic Chinese trade policy practices that burden American commerce.¹ The list includes intellectual property abuses and theft of trade secrets, discriminatory licensing practices, forced technology transfer, state-directed cyber hacking and intrusions into commercial networks.²

The Trump administration responded by issuing a series of unilateral tariffs, which in turn, prompted retaliation by the Chinese government.

However, rather than to issue unilateral tariffs that ultimately could only end in retaliation and escalation, the administration would have been far better served to put together a coalition of like-minded allies to pursue a multi-pronged approach against specific practices.³ Such an approach should include the initiation of aggressive cases against China at the World Trade Organization; rejoining the Trans-Pacific Partnership (TPP), a promising trade pact between Pacific Rim nations designed in part to pressure Beijing to raise its commercial standards; the limited use of investment restrictions through the Committee on Foreign Investment in the United States (CFIUS) and narrowly targeted export controls; and a more formal, binding agreement between Washington and Beijing with verifiable enforcement mechanisms. And while it is true that such a thoughtful, whole-of-government approach will require time and negotiation, given the negative impacts of the administration's alternative, it is imperative we get it right.

BEIJING STRIKES BACK

As the United States began its efforts to raise tariffs on Chinese goods, Beijing's response was entirely predictable. As demonstrated in Chart 1, it quickly retaliated against American exports, including heavy tariffs on agricultural products. More specifically, its raised tariffs between 5 percent and 25 percent "on more than 800 U.S. food and agricultural products."⁴

CHART 1: TIMELINE OF TRADE WAR ACTION BY U.S. AND CHINESE GOVERNMENTS

Date	Event
Aug. 18, 2017	The United States self-initiates a Section 301 investigation into Chinese unfair trade practices.
March 22, 2018	Trump indicates forthcoming Section 301 tariffs on up to \$60 billion of imports from China; the USTR releases Section 301 report.
April 3, 2018	The United States announces list of Chinese products worth \$50 billion over which it will impose Section 301 tariffs of 25 percent.
April 4, 2018	China announces its list of U.S. products worth \$50 billion over which it will impose tariffs of 25 percent in retaliation for U.S. Section 301 tariffs.
April 5, 2018	Trump instructs the USTR to consider whether an additional \$100 billion of imports from China should be subject to Section 301 tariffs and instructs the Dept. of Agriculture secretary to examine the possibility of subsidizing U.S. farmers hurt by tariff retaliation.

June 18, 2018	Trump instructs the USTR to identify an additional \$200 billion of imports from China that would be subject to 10 percent tariffs under Section 301.
July 6, 2018	The United States imposes Section 301 tariffs of 25 percent on a revised list of \$34 billion worth of imports from China.
July 6, 2018	China imposes tariffs of 25 percent on its own revised list of \$34 billion of imports from the United States in retaliation to the Section 301 tariffs of July 6.
July 10, 2018	The United States announces a list of Chinese products worth \$200 billion over which it will impose Section 301 tariffs of 10 percent.
Aug. 3, 2018	China announces its list of U.S. products worth \$60 billion over which it will impose tariffs of 5-25 percent, if the United States imposes the proposed July 10th tariffs.
Aug. 23, 2018	The United States imposes 25 percent tariffs on a revised list of \$16 billion worth of imports from China. Combined with the July 6th action, this completes the imposition of tariffs on the first \$50 billion of Chinese imports.
Aug. 23, 2018	China retaliates by imposing tariffs of 25 percent on a revised list of \$16 billion of imports from the United States.
Dec. 1, 2018	Trump and Xi announce the commencement of negotiations. The scheduled U.S. tariff increase from 10 to 25 percent on \$200 billion of imports from China is placed on hold for 90 days.
Feb. 24, 2019	Trump tweets he will delay the tariff increase from 10 to 25 percent that was scheduled to go into effect on March 1, 2019, and that he is planning a summit with Xi.
May 5, 2019	Trump tweets that the United States will increase the 10 percent tariff on \$200 billion of imports from China to 25 percent on May 10, 2019. He also indicates that more tariffs on imports from China may be coming.
May 10, 2019	The United States raises the tariff rate to 25 percent on \$200 billion of Chinese imports.
May 13, 2019	In response to the new tariffs, China announces it will raise its tariff rate covering the \$60 billion of imports from China already subject to duties on June 1, 2019.
June 1, 2019	The Chinese tariffs announced on May 13th go into effect.
June 29, 2019	President Trump and President Xi meet at the G20 summit in Osaka, Japan. Both sides agree to resume talks. The United States agrees not to move forward with additional tariffs and China agrees to purchase more farm goods.

SOURCE: Timeline derived from Chad P. Bown, "The 2018 US China Trade Conflict After 40 Years of Special Protection," Peterson Institute for International Economics, April 2019, p. 29.

Such a tit-for-tat trade war has been incredibly detrimental to U.S. farmers in particular, as certain American agriculture producers are extremely dependent upon Chinese market access (Chart 2).⁵

CHART 2: PRODUCTS DEPENDENT ON CHINESE MARKET ACCESS

Product Description	2017 Exports to China	Total U.S. Exports	Share of 2017 U.S. Exports Sent to China (percent)	Prior Tariff (percent)	New Tariff (percent)
Yellow soybeans and black soybeans	\$12.25 billion	\$21.58 billion	57	3	28
Cotton, not carded or combed	\$971.29 million	\$5.83 billion	17	1 in quota	26
				40 out of quota	65 out of quota
Grain sorghum	\$835.7 million	\$1.027 billion	81	2	27
Frozen other Pacific salmon	\$274.9 million	\$426.8 million	64	7	32
Whey and modified whey	\$235.2 million	\$624.1 million	38	2	27

SOURCE: Hopkinson, p. 6. <https://crsreports.congress.gov/product/pdf/R/R45448>.

In 2017, for example, 81 percent of sorghum exports ended up in China when the tariff was 2 percent.⁶ Today, China's tariff on U.S. sorghum is 27 percent.⁷ Likewise, after Beijing's tariffs on American soy increased from 3 to 28 percent, soy exports to China fell by 74 percent in 2018—from \$12.25 billion to \$3.4 billion.⁸

In fiscal year 2017, American farmers and ranchers sent \$22 billion worth of agriculture to China.⁹ In fiscal year 2018, those same exports dropped to \$16.3 billion, a decline of approximately 25 percent from the previous year.¹⁰ In March 2019, the U.S. Dept. of Agriculture (USDA) projected that American agricultural exports to China will be \$9 billion for fiscal year 2019—the lowest amount since 2007—and this estimate was before the recent ratcheting up of tariffs on both sides and thus it is likely still too high.¹¹

TRADE BAILOUT PARTICULARS

As farmers and ranchers continued to lose profits from exports, once again as it did last year, the Trump administration relied on a New Deal-era program, the Commodity Credit Corporation (CCC), to devise a bailout scheme designed to mitigate the harm caused to them by foreign trade retaliation. Accordingly, the USDA recently announced a three-segment program that will provide \$16 billion in relief to struggling farmers and ranchers who saw their personal income drop by the most since 2016 during the first quarter of this year.¹²

MFP—The central component of the agricultural trade bailout is the Market Facilitation Program (MFP), which is administered by the USDA's Farm Service Agency. The MFP

will provide direct payments to certain farmers and ranchers who produce the products facing increased foreign retaliation. This program will cost \$14.5 billion this year.¹³

Food Purchase and Distribution Program—Like last year’s bailout program, this year’s will also utilize the Food Purchase and Distribution Program, which is run through the USDA’s Agricultural Marketing Service, to “purchase surplus commodities affected by trade retaliation.”¹⁴ This program is used to provide food to food banks, schools and other groups that serve needy Americans. It will cost taxpayers \$1.4 billion this year.¹⁵

Agricultural Trade Promotion Program—Administered through the USDA’s Foreign Agriculture Service, the final component of the 2019 bailout will provide \$100 million for the Agricultural Trade Promotion Program “to assist in developing new export markets on behalf of producers.”

CONSEQUENCES

Over the last two years, the administration’s mitigation program will cost taxpayers approximately \$30 billion. But that’s just the beginning of the farming community’s troubles, as there are several other negative consequences that will only be compounded the longer the administration maintains its current course of action.

Lost Markets

First, it has taken years for American farmers and ranchers to develop strong commercial relations with buyers in China. In light of the retaliatory tariffs on U.S. products, Chinese purchasers are finding alternative suppliers. Brazil, for instance, has been a major supplier of soybeans in the wake of declining market access for American producers. It is an open question whether U.S. farmers and ranchers will regain their market share if the tariffs are lifted—or whether Chinese buyers will simply rely on their new (and perhaps more reliable) suppliers.

Barriers to Trade Liberalization

Although the trade-related problems with domestic agriculture subsidies predate the Trump administration, the recent bailout packages exacerbate an enormous barrier to widespread trade liberalization. For example, when WTO Members launched the multilateral Doha Development Round at the behest of the United States in 2001, a stated goal was to expand the freer trade of agricultural products. Completing Doha would have been a major boon to American agriculture. However, after 14 years of on-and-off negotiations, the WTO finally declared the Doha Round dead in December 2015. Although there were numerous reasons the negotiations failed, a major culprit was the unwillingness of the

United States and the European Union to curb their own domestic agriculture subsidies, while at the same time pressuring developing countries to cut their agriculture barriers. Perhaps not surprisingly, the Trump administration’s bailout program makes the prospect of multilateral trade liberalization that much more difficult.

Misuse of Taxpayer Funds

Under the terms of the bailout package, producers can receive MFP payments of up to \$125,000 per recipient for “eligible crop commodities, a combined \$125,000 for dairy production and hogs, and, separately, a combined \$125,000 for fresh sweet cherries and shelled almonds.”¹⁶ This applies whether the recipient is a natural person or a legal entity as long as the person or entity is “actively engaged in farming.”¹⁷ Despite this restriction, a recent investigation by the Associated Press (AP) found a number of recipients skirting the caps through loopholes in the “actively engaged in farming” standard and through creative uses of legal entities.¹⁸

That same report highlights one soybean farm in Missouri, for example, which was established as three legal entities at the same address, and received \$2.8 million in payouts.¹⁹ More than \$900,000 of MFP payments were sent to five businesses, including businesses in Indiana, Illinois, Tennessee and two in Texas.²⁰ These are just a few of the examples documented by the AP. This problem also plagues other agriculture subsidy programs authorized under various farm bills, but as the trade wars drag on and more payments are made, taxpayers should expect more of their money to end up in the hands of bad actors.

Put simply, at its core, the MFP is a “backdoor revival and expansion of the discredited direct payments program” in which farmers “received a payment every year regardless of market conditions.”²¹ Direct payments were phased out in the 2014 farm bill, but they are rearing their ugly heads once again.

Environmental Damage

In addition to the harm to taxpayers and trade relations, domestic agriculture subsidies harm the environment. Specifically, they create incentives for overproduction and for the utilization of marginal land for planting, including highly sensitive areas like wetlands. They also further encourage the use of environmentally damaging fertilizers and pesticides. The trade bailout package is no different; it will do significant damage to the environment on top of the damage from last year’s massive farm bill.

POLICY RESPONSES

If the United States truly wants to aggressively open for-

eign markets for agriculture products, there is a straightforward path. First, it should withdraw the president's tariffs on imports from China. Like Canada and Mexico after the Trump administration withdrew its steel and aluminum tariffs, China will remove their retaliatory tariffs, which have fallen particularly hard on the farming and ranching community. With the tariffs eliminated, the United States can cancel the recent bailout program. Getting back to the pre-2018 status quo is a good first step, but more can be done.

The administration's decision to withdraw from the TPP, which would have opened up notoriously closed agriculture markets in Asia to American producers, was a disaster for American farmers and ranchers. After the United States withdrew, the remaining countries moved forward and now U.S. farmers and ranchers are at a competitive disadvantage in the region. The United States may be able to regain some of what was lost with its bilateral negotiations underway with Japan, but if the administration really wants to help American farmers, it should quickly rejoin the TPP.

While a series of bilateral agreements can help, they would not be good enough. Ultimately, the United States has an enormous chip it can play to jumpstart multilateral liberalization at the WTO: curbing its own agriculture subsidies. The bottom line is that countries across the globe, particularly developing nations, will be willing to move forward with agricultural liberalization if the wealthiest country in the world takes credible steps to curb its own domestic agriculture subsidies and other trade barriers.

CONCLUSION

In managing the world's most important geostrategic relationship, there will be no silver bullet. Indeed, friction between Washington and Beijing are inevitable as China's wealth and power continue to rise. But this is precisely why a sober and tempered approach would be more likely to succeed than the Trump administration's more reckless and aggressive stance. In fact, unilateral tariffs on imports from China have mostly only emboldened hawks in the Chinese Communist Party to the detriment of market-oriented reformers and thus a continued confrontational approach likely portends a retrenchment on market liberalization efforts. For this reason, we must reverse course and make significant strides forward before the damage is too extensive to be undone. Domestic prosperity requires expanded market access abroad. However, instead of seizing the opportunity to push forward with efforts to open up foreign markets, from trade wars and protectionist bailout schemes, the Trump administration's policies have moved in the opposite direction to the great detriment of one of our greatest and most productive American assets—our ranchers and farmers.

ABOUT THE AUTHOR

Clark Packard is trade policy counsel in the Finance, Insurance and Trade Policy division at the R Street Institute, where he researches international trade and investment policy.

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