

# ISAS Insights

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## **Donald Trump's Unilateral Tariff Imposition: Damage to the World Trading Order**

*Much of the discussion on the several steps taken by the President of the United States (US), Donald Trump, in the area of international commerce has focused on the unilateral moves on tariffs imposed by the US as an instrument of diplomacy. The American leader is determined to go alone, convinced that the deals made bilaterally are advantageous for a country such as his that outmatches any other in terms of its economic and military strength. This way of proceeding is weakening the international economic, financial and trade order the US was deeply involved in creating. This paper suggests that all the world nations, including South Asia, should draw up a plan of action to save the world order from the assault by the US.*

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Tariffs can be imposed, raised, lowered or eliminated. These moves can be done unilaterally, in which case they violate the established international law. That is especially so if they are aimed at one country or a group of nations. In such a situation, the actions taken are against the principle of the most-favoured nation (MFN) provision of the international agreements

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that eventually led to the creation of the World Trade Organization (WTO) in 1995. Under the accepted international commerce law, actions directed at one country, against it or in its favour, must be adopted for all nations that are members of the WTO.

While these up or down moves can be temporary, depending upon the mood of the nation adopting them, the damage done to the international trading system can last a long time. This is likely to be the result of the actions taken by the United States' (US) President Donald Trump and his trade advisers. In most writings and commentaries on what the Trump administration has done to international commerce, the focus has been on the damage inflicted on individual countries by these tit-for-tat actions. Not much has been said on how the rule-based international system is being hurt.

This system was developed in the 73-year period since the end of the Second World War. The founding principle of the order was that actions will be taken on the basis of consensus reached among the nations that became the members of the organisations established after the wars in Europe and Asia. No country dominated international decision-making. That these moves – collective action and consensus building – became the founding principle of the post-Second World War world order was a testimony to the US' foresight and leadership.

This line of thinking was a departure from that adopted by the victors of the First World War. The approach then was that defeat on the battlefield was not enough; those defeated had to be punished even after the war was over. Germany and its allies in the war had to pay reparations to the countries they had fought. A lot of damage had been done by the defeated nations and they had to pay for it. However, the result was the rise of extreme nationalism in Germany and Italy. They were overtaken by fascism which ultimately led to the Second World War. However, a lesson had been learnt, especially by people such as John Maynard Keynes, the British economist, who had studied the economic consequences of the policies adopted by the victors. He persuaded those who had won the war to help the defeated nations to rebuild their economies and to create a system that would prevent the occurrence of world financial crises. The first objective was achieved by the creation of the International Bank for Reconstruction and Development (IBRD). For the second, the victors meeting at the resort of Bretton Woods, located in the hills of the US state of New Hampshire, agreed to establish the International Monetary Fund. The IBRD subsequently acquired more functions and became the World Bank Group.

The nations that attended the Bretton Woods deliberations also wanted to create an institution that could manage international commerce. However, an agreement was not possible. Trade is always a more difficult subject on which agreement can be reached. Complicating the situation was that, after the war, the financially weakened colonial European states of Britain and France did not have the means to manage vast empires. They began the process of decolonisation that led to the emergence of dozens of new states in Asia and Africa. These countries were not prepared to open their markets to imports from the states that had once ruled over them. They sought protection from this competition so as to create space in which they could develop their own industries. This led to the acceptance of the ‘infant industry’ argument which was incorporated in the various rounds of trade negotiations, leading to significant reductions in tariffs in trade among the developed nations. Ultimately, agreement was reached to create an international trade institution. At the conclusion of the Uruguay Round of trade talks in the meeting at Marrakesh in Morocco in 1995, the assembled nations agreed to create the WTO. The most important part of the WTO was to establish a dispute resolution mechanism, where a panel of experts working as quasi-judges could adjudicate disputes. At the insistence of the US, the WTO adopted the provision for nations creating regional trading pacts in which the MFN principle was not applied. The global economic, financial and trade structure was thus completed in 50 years.

The US has been governed by 10 presidents since the global conflict ended in 1944-45. Nine of them promoted the development of the global order. It is only the 10<sup>th</sup>, Trump, who has shown total contempt for the system that has governed the world. Without the US’ support, the global system will not work. For instance, Washington has not nominated its representatives to the WTO panel that hears and decides upon the complaints from a member state or states that believe that some of their trading partners are not fully observing the rules that govern international commerce.

The tit-for-tat actions initiated by Washington under Trump have by now involved most of its major trading partners and have been the subject of comments and analysis in hundreds of columns that have appeared in the world press. During the campaign for the presidency, Trump had promised those who came out in support of his candidacy that he will get their jobs back from the countries that had stolen them because, as he repeatedly put it in the many rallies he addressed, of the “unfair” deals the US had signed with a number of its trading partners. He criticised the Trans-Pacific Partnership (TPP) agreement concluded by President

Barack Obama after two years of intense negotiations with 11 other countries on the Pacific Rim. The TPP had two important features, both of great significance for the US. It excluded China that had, over the years, emerged as the world's most important trading nation. China was not brought into the agreement since the TPP signatories believed that its economy was not following the rules and practices of the free market place. That was the necessary condition for joining the agreement. Second, the TPP would have enforced the US' regulatory requirements in the areas of labour practices and environment on all member nations. These were tremendous concessions made by the signatories in return for getting even better access to the enormously large American markets and to the country's rapidly developing technologies. However, none of this was understood by Trump, the candidate, or Trump, the president. One of his first actions upon moving into the White House was to pull his country out of the TPP agreement. Those who had signed the agreement decided to continue with it and now call it the Comprehensive and Progressive Agreement for Trans-Pacific Partnership.

There is agreement amongst most economists that the jobs Trump had promised to bring back to the country were not because of the relocation of many US industries to places such as China and Mexico – even though some of that had happened – but because of several significant technological developments. Automation such as robotics were replacing workers with machines, a process that would not change by the imposition of punishing tariffs on some of the major imports into the US.

The tone of exchanges between the US and China became sharper as the tit-for-tat actions continued. The overseas edition of the ruling Communist Party's *People's Daily* newspaper singled out Trump in an editorial published on 5 August 2018, saying the American leader was starring in his own “street fighter deceitful drama of extortion and intimidation”.<sup>2</sup> This sharply-worded criticism came after Chinese state media on the preceding day accused the US and said a proposed set of differential tariffs on US\$60 billion (S\$82.4 billion) worth of US imports showed rational restraint. The Chinese response included proposed tariff increases, ranging from liquefied natural gas to some aircraft parts. This proposal followed

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<sup>2</sup> “Trump's trade ‘extortion’ won't work, China state media says”, Andrew Galbraith and Michael Martina, *Reuters*, 6 August 2018. <https://www.reuters.com/article/us-usa-trade-china/trumps-trade-extortion-wont-work-china-state-media-says-idUSKBN1KR096>. Accessed on 11 August 2018.

the one by the US of levying 25 per cent higher tariffs on US\$200 billion (S\$274.6 billion) worth of Chinese imports to America.

China is not the only country in Trump's sight in terms of bringing about significant changes in the old global order. Trump also moved against Canada and Mexico, which, with the US, are the members of the North American Free Trade Area. He also threatened to impose tariffs on the import into the US of steel and aluminum. European cars may also be taxed. The latest example of using tariff-escalation is Turkey. Trump has ordered the doubling of tariffs on the import of steel from Turkey in the dispute involving the incarceration of an American citizen by Ankara.

It is appropriate for the world nations to impose tariffs of their own imports from the US. However, a much more meaningful response would be to take collective action to save and improve upon the working of the WTO. At the conclusion of the Uruguay Round of trade talks that led to the creation of the WTO, it was agreed that the agency's work-space would be expanded to include three more areas – services, intellectual property rights and factoring in trade as a contributor to development.

The US, under the Trump administration, is focused on the "America First" approach in its contacts with the world. In its absence from the international scene, the remaining WTO members may contemplate convening another round of discussions to determine how the agency would work if the US leaves.

Why and how should the South Asian region join this effort? Let us first take up the 'why' part of this question. While the miracle economies of East Asia, including China, benefited enormously from the process of globalisation that resulted in the lowering of tariffs in trade among nations, as well as in the settlement of trade-related disputes, South Asia did not take much part in the process. Consequently, its trade to gross domestic product (GDP) ratio is relatively low, about 30 per cent compared to say, 160 per cent for Vietnam. As economists never tire of emphasising, trade is an important contributor to growth.

With multilateralism in trade now under threat, the South Asians will be left to satisfy the bilateral interest of major commercial powers such as the US, the European Union and China, and getting very little in return. To meet those bilaterally will be inefficient and costly. The

South Asians should move collectively and put real teeth in the South Asian Free Trade Area, which has not met the objectives for which it was set or realised its potential.

While South Asia has benefitted from the general lowering of tariffs on trade with developed nations, there is now the need to move on three fronts to gain from globalisation. They need the trade in services to be regulated in a way that India and, to a lesser extent, Pakistan are not discriminated against. For India, the ratio of trade in services to GDP is less than 15 per cent compared to Singapore's 90 per cent. Also, there is a danger that countries such as the US that have invested heavily in developing intellectual properties will be able to deny, acting unilaterally, access to them. This deprivation would hurt the development of industries such as pharmaceuticals in places such as India and Pakistan. An agreement reached with the WTO framework would be definitely preferable.

The WTO is also needed within South Asia to systemise the use of non-tariff barriers (NTBs) to promote regional trade. Pakistan has not granted the MFN status to India on the ground that the vast array of NTBs India has in place would hurt its producers.

In conclusion, it needs to be understood that the WTO would continue to serve well for the poorly-integrated South Asian states both within the region as well in the globalised world. Hurting the WTO would be immeasurably disadvantageous not only for much of the world, but also for the South Asian subcontinent.

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