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Trade wars 2.0: further escalation or end in sight?

The US have been at the epicentre of the world of trade since President Trump imposed additional import duties on steel and aluminium, leading to retaliatory measures by several key trading partners, including China, Mexico as well as the EU. Things quickly shifted from bad to worse and with the Chinese and Mexican counter-tariffs the trade wars have spread to the dairy sector as well. The question is: has the turning point been reached with the partly more positive signals since July/August or is this only the beginning?

EU – US trade relations have entered a period of détente following Commission President Juncker's visit to Washington in July. It seems to be quite a fragile truce however and just yesterday President Macron reiterated his view that the EU should not be concluding any agreements with countries not respecting the Paris climate agreement. While the steel and aluminium tariffs (and the counter measures) remain in place for the time being, EU and US have begun informal talks in view of a trade deal eliminating tariffs on all industrial goods, possibly including cars as well. Commissioner Malmström and US Trade Representative Robert Lighthizer will meet again on Monday and are expected to chair a working group preparing the ground for formal negotiations to be launched in November. The US wish would be to extend the discussions to agriculture (no objections from us there!) which is apparently a no-go for Brussels. But Agriculture seems to be part of the talks already, with the highly mediatised increase of EU imports of US soybeans following the high-level July meeting (whether there is actually any link between the two is secondary) and the Commission proposal to launch talks to resolve the long standing hormone-free beef quota dispute with the US. This is officially an unrelated matter (the quota was introduced following a WTO ruling to compensate US exporters but is actually being used by other beef suppliers) but the timing makes you wonder.

In the beginning of September, the US administration announced a breakthrough in the NAFTA negotiations with Mexico, addressing notably the contentious issue of rules of origin for cars. The problem is that Canada is not on board yet. Talks about if and under what terms Canada would join the US-Mexico deal have continued this week. As always, dairy is one of the contentious issues, as the US try to force changes to Canadian dairy policy harming US exports. At the very least, the US is seeking to address the milk class 7 system subsidising Canadian dairy protein exports, while keeping imports of products such as ultrafiltered milk used in cheese making out. If Canada does not join the agreement, there might some hurdles to having the deal approved by congress as initially Trump's mandate covered a NAFTA renegotiation, not a new trade agreement with Mexico.

The question of more immediate importance from a dairy perspective is whether the NAFTA breakthrough means that the Mexican retaliatory tariffs on US cheeses will be removed and when that will happen. US export data for July does not show any impact of the Mexican 20% and 25% tariffs on export volumes but there are numerous accounts on the significant impact of those tariffs on US businesses. In some cases, the additional costs have reportedly been split but in others they have to be borne solely by the US exporter which is not sustainable for the companies concerned.

Meanwhile, Trump has also reiterated his threat to take US out of the WTO unless it "shapes up", while calling the agreement establishing the global trade body "the single-worst trade deal ever made". The changes demanded by the US relate mainly to the authority of the appellate body of which the US is currently blocking the nomination of members. The EU is currently preparing reform proposals of its own, partly in response to the US points of criticism, and a ministerial meeting of 12 likeminded WTO members will be hosted by Canada in October, with the aim to gather a critical mass to push forward necessary changes to the system designed some 25 years ago. Pulling out of the WTO would obviously have tremendous consequences as the relationship between the US and its trading partners would no longer be "rule based", leaving complete freedom as regards tariffs and other trade measures.

Finally, there seems to be no end in sight to the conflict with China as the list of products subject to additional tariffs keeps getting longer on both sides and is not like the underlying issues relating to intellectual property rights and state intervention in the economy and other ideological differences would go away any time soon. And this is a conflict with the potential to derail the global economy. Purely on dairy though, the additional 25% imposed on milk and whey powders, cheese and AMF will hurt the US exports of all these products (except for AMF which are non-existent to China) but whey will be the most affected since about half of US whey powder exports go to China. In July, first month of application of the tariffs, US dairy exports to China were down considerably across the board, whey by 27% and cheese by 56%.

Despite everything that is going on the other side of the pond, we should not lose sight of the single biggest potential trade disruption on our continent. The next two months will be absolutely decisive on Brexit as the EU and UK positions remain miles apart. Theresa May is defending her Chequers plan and refuses any compromise that is not in the UK's national interest. On the EU side, Barnier keeps on insisting the EU will not impair the single market and the customs union to the benefit of a soon to be ex-Member State. And the solutions put forward in the UK white paper – the facilitated customs arrangement and the common rulebook - would do just that. At this stage, there is no draft joint text regarding the future partnership and important parts of the withdrawal agreement (on Northern Ireland) are still under negotiation. Reminder: without the withdrawal agreement, there will be no transitional period, meaning that WTO trading terms would kick in on 29 March 2019 UNLESS the art.50 negotiations are prolonged. So anything could happen, but we would not want to end on an overly pessimistic note. In the end it is VERY MUCH in both the UK's and the EU's interest to keep trading (and other) ties as close as is possible with a non-member country.