Peterson Institute for International Economics

CEPR e-book launch: The Great Trade Hack by Richard Baldwin

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[00:00:16.11] - Mary E. Lovely

Good morning, everyone. Thank you for joining us. We're coming to you from a still quite hot but a little less steamy Washington, and it is my great pleasure today to be joined by our main speaker today and the man we will be drilling with questions, Professor Richard Baldwin. Richard is now at the IMD Business School in Lausanne. He is, of course, well known to all of us in the trade world as the author of many great and interesting and fun books. Richard, you have a special place on my bookshelf. This is an ebook that we're going to be talking about today, so I— short of putting my iPad up in the bookshelf, it will definitely be, in a sense, on on my— yeah, there you go. Oh, it's okay, it's coming out in real hard copy. Okay, you'll have to tell us about that. This book is from CEPR Press, um, and it's available for our audience to, to read. Um, I have to say, Richard, that I read it with great interest and found an extremely readable book. Uh, thank you for making it so easy to, to read and to really enjoy. Of course, I've always come to enjoy your books.

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Um, they are fun to read and informative and filled with interesting observations. So without much ado, I would like to turn it over to Richard, who will give us a, a relatively brief overview of this interesting, uh, piece of work. And that will be followed by the Reginald Jones Senior Fellow here at the Peterson Institute for International Economics, my wonderful colleague Chad Bowne. So Richard, let me turn it over to you to start, and then we'll hear from Chad. Richard, please.

[00:02:05.03] - Richard Baldwin

Thank you very much, Mary, for those kind words of introduction and calling my book interesting, which is about as good as you can. I mean, if somebody reads it, has a look, it's an easy read, that's really what I want to do. And, you know, this book was an instant book. It collected together some LinkedIn columns I'd been doing for a number of months, but it was fast

and it's already out of date. But I'm glad to give it before July 9th because it might be really out of date by July 9th. We'll see. So that's the kind of way I want to take this. I want to provoke thinking. I want to make people think a little bit harder about some of the narratives that you're getting in the media and perhaps look a little deeper. That's the basic of the whole thing, and I'm going to try and go through the book in about 20 minutes. Okay, so here is— by the way, that's the scan code. You can download this thing for free. That's one of the downsides of an instance book. You don't get any royalties on it, so but there it is.

[00:03:04.19]

The outline: I'm going to argue that the 2 April tariffs were a historic start of a post-US trade leadership era. So that these—

[00:03:14.23] - Chad P. Bown

Sure, I'm going to interrupt if you're trying to show us a slide, we're not seeing it yet.

[00:03:19.14] - Richard Baldwin

No slides? I see. Okay, let me see, do share. Let's see, there we go. Share. And how about that? There we go. So you can see there's a scan code. I'll do that. I'll do this again. The scan code there in case you want to take a picture. And the scan code reoccurs during the, uh, the, uh, presentation. Okay, so I'm gonna first argue that this thing is historic, and that's why I called it the trade hack rather than a trade war or something else. I think it's distinctly different. I think your grandchildren will be reading about April 2nd in the history books as the beginning of the post-American trade leadership era. The second bit is I want to go through some discussion to what I— to help understand President Trump's policies and to understand them as following emotional grievance, not economic goals. Next, I'm going to talk about 4 scenarios for the world trading system as it may go forward. And if we have time, I want to talk a little bit about China's rare earth magnets export restrictions. Maybe this is a new trade Cold War, maybe it's not, we'll see. That slide unfortunately mysteriously got erased from my tech, so I didn't have time to reconstitute it, but I think maybe it's best if just we leave that for a discussion.

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But what I'm working to, and this isn't in the book, is the idea that that the United States, with its tariffs against the entire world, and China, with its export restrictions against the entire world, has sort of reproduced a Cold War situation where mutually assured destruction keeps the peace. At least that's the optimistic me, and that this idea that the trade war won't get much worse will be held up by these two conflicting forces. So I'll leave that to the end. Okay, now

what I'm going to do is simplify to clarify, or maybe some people will think oversimplify to clarify, but I think it's really important to narrow things down, make them less complicated, because the real problem most of us have, especially in fast-developing stories, is that you don't know what to focus on. And I'm going to suggest a few things to focus on, and the consequence of that will be that I'll be skipping over some important things that I hope Chad in the Q&A will bring out. So first of all, I want to make the argument that this great trade hack is a historic thing. This is the infographic I'd like you to see.

[00:05:48.16]

I think from 1947 to 2005 was the American leadership era. The leadership of the trade system was not charity. It was enlightened self-interest that boosted American power, which was useful during the Cold War, the War on Terror, the War on Drugs, all sorts of power of the United States was boosted by its leadership of the trade system. I think April 2nd stopped that, and I think afterwards— and I'll make an argument that it's not just Trump— that the U.S. will withdraw from leadership of the trading system, and that will put us into a different era. So, come down. The Great Track— Trade Hack. So why this title? What was Trump trying to do? Was he trying to reform the system? Was he trying to renegotiate tariffs? No, my answer is he was hacking the whole trade system. He was trying to bypass the code, short-circuit the rules, and brute force a quick fix using tariffs that were big, bold, and everywhere at once. This was not a normal thing. Why were the second April tariffs different? If you look before April 2nd, Trump tariffs and other Biden tariffs, lot of other tariffs were about specific problems with specific partners.

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They weren't historic. And in fact, many nations have done that before. After April 2nd, we had massively intentionally broken every trade promise the US made on with anybody anywhere, all the WTO commitments, all the free trade agreements, without excuse. One signature, 2 minutes, they were gone. This wasn't a trade war. This was a war on the rules-based trading system by the largest trader in the world. So let's get this— okay, I want to argue that this is not going away, that the trade hostility is not new, and it will continue. So here's the argument, the historical development. The US switched from super pro-trade trade hesitant with the global financial crisis and the Great Recession. So let's start in 1981 to 1993. Reagan and Bush Senior were super pro-trade. I was in the Council of Economic Advisers as a senior staff economist during Bush Senior, and everything was super pro-trade, especially was very respectful of trade law. And although we were involved in a trade war with Japan, there was a great deal of support for the World Trading System and for bringing in Eastern European countries, et cetera. And then switched to a Democratic administration under Clinton.

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And between '94 and 2008, the US was also super pro-trade. Clinton pushed through NAFTA. Clinton got the GATT turned into the WTO. During this time, China joined the WTO. And up to Bush Jr., the US still remained super pro-trade, pursuing regionalism, multilateralism, and very respectful of international trade rules.. Then came the Great Recession. But let me argue first that the middle-class malaise which is underpinning the populism that President Trump is riding on, that started to build with globalization and automation shocks during this 1994 to 2008 period. Though, and in America, those shocks were faced without a social policy to facilitate adjustment. In other advanced economies, they got the same shocks but they had social policies like universal healthcare, free university, active labor market policies, reasonable pensions, good local schools, stuff like that that helped people adjust. Not in the United States. And that was— that lack of support for the middle class despite the shocks was Democrats, Republicans, Democrats. It was not one side or the other. Then came the global financial crisis, and I believe the victimhood narrative strengthens. So if you remember, the global financial crisis which led to the Great Recession was very bad for America's middle class.

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America— many Americans lost their homes. They lost their health care. They were— their incomes were devastated. But the banks got bailed out. The car companies got bailed out. None of the bankers went to jail. There was a sort of beginning that the system was rigged against the middle class of America. And I think that's where it really started going. But in any case, because of the middle-class malaise, Obama I switched from pro-trade to trade hesitancy. And I personally don't know, don't think that that was because of an ideological thing. I think he was one of the Davos kind of people, but it was politically impossible to be pro-free trade at the time. Obama II, he restarted a few little things, but he didn't get, for instance, the Trans-Pacific Partnership over the line before his presidency ended. And then Trump came in and it switched, switched from trade hesitancy to trade hostility. And then when Biden came in, it switched back to trade hesitancy. But very few of the tariffs that Trump put on were actually taken off, especially against China. And Biden also sharpened and intensified the anti-China trade policies during his term. Then trade comes in and we have super trade hostility.

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But as you'll notice, this is 4 presidential cycles, the US has not been pro-trade, has not been a real leader of the trading system. That's my argument, is it's not new, and it's not likely to go. Now, I don't live in Washington like you guys, but I can't see an American presidential candidate

standing up and said, no, let's take off all those tariffs from China, that was a mistake. Let's get the WTO back again, that was a mistake. I think right now, anti-globalization has a bipartisan consensus that's going to continue for a good long time. Okay, so that's why I think this is the start of the post-American trade leadership. Before, US was universally regarded as a steward of the system. It set it up, it guided it, defended the rules-based system since 1948. And this was enlightened self-interest, as I mentioned. This— people thought it was credible because the US was getting a lot out of it. Just to give you a fact, the US is the only advanced economy whose share of world GDP has stayed stable over the last 25 years. All the other ones have declined. After April 2nd, US is now universally regarded with suspicion.

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I talked to governments in all over the world, and people just are a little befuddled as to what happened, but they're very suspicious of what the US is doing on trade. Okay, so now what I want to do is go on to motives, and I think this may be the most controversial but perhaps the most useful part of the book. I want to argue that Trump's policy is economically incoherent but emotionally coherent. So if you're thinking about Trump trade policy as if it was trade policy, you'll hear words like erratic, chaotic, self-defeating, volatile, all these things.. But if you think about it as it's a grievance, redressing grievance, it makes perfect sense. So let me make that argument a little bit more in detail. So the grievance doctrine drives— guides President's trade policy. I believe you cannot make sense of President Trump's actions without grasping how grievance drives them. So this is what I call the grievance doctrine, unlocks the internal logic of the great trade hack, what drives it how it unfolds, and where it leads. But the grievance doctrine isn't a strategy, it's a story. It's a myth. It's a mythic tale where a naive America played by the rules and got played by globalists abroad and traitorous globalists at home.

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America was humiliated, factory jobs were stolen, and the middle class paid the price. This myth comes with a mandate to stop the steal and erase the humiliation. Now, these are not words that I felt very comfortable writing down or speaking about to a trade audience because it doesn't seem right. But I'll show you in a moment, these are actually the words that the administration is using in describing their policy. So, yeah, I think we have to get used to the idea that these words are not a marketing slogan to get people to pay attention to a trade policy that has standard economic goals behind them. This is angry people slashing out against what they view as great grievances. Okay, so here it is written out. It was in the President's 2025 Trade Policy Agenda, which was published in March 2025. The first chapter— this is what most everybody in the audience here knows. This is an annual report, and usually it's filled with boring bureaucraties and complaints about chlorine chickens and intellectual property.

Generally a very dull bureaucratic policy.. But this one, the first chapter, reads like a drama. So here, let me just read you the narrative that comes out of this.

[00:14:42.09]

The United— this is the first sentence of the report: The United States of America is the most extraordinary nation the world has ever known. In the previous century, it saved the entire world. That's the first sentence. Then it describes the fall. It's like a Greek myth. Today, the upward mobility offered by manufacturing sector is not widely available to the working class much of our industrial might has moved overseas. And then it identifies the villains. These trends are the product of a withering decades-long assault by globalist elites who have pursued policies, including trade policies, with the aim of enriching themselves at the expense of the working people of the United States. As a result, the middle class atrophied. So you see, the middle class malaise is a result of this globalization, and in particular the globalist elite. Then comes the hero. President Trump alone recognized the role that trade policy played in creating these challenges and how trade policy can fix them. And then comes the retribution. The trade challenge— challenges facing our country will be, quote, annihilated because from this moment on, America's decline is over. Trump's words when he announced these tariffs on April 2nd are even stronger.

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It sounds like he's talking about war crimes. He says, our country has been looted, pillaged, raped, and plundered by nations near and far, both friends and foe alike. American steelworkers, autoworkers, farmers, skilled craftsmen watched in anguish as foreign leaders have stolen our jobs, foreign cheaters have ransacked our factories, and foreign scavengers have torn apart our once beautiful American dream. Though, you know, when I— when you read that, at first you go, well, that's just, you know, stump speech. But if you go back to 2016, it was more or less exactly the same words. And even if you go back to the '80s, Trump had essentially the same idea that the world trading system was rigged to rip off America. So it sounds strange that the trade policy of the United States is driven by an emotional grievance. But give it a try. It makes sense. So the April 2nd tariffs make perfect sense in this world. Tariffs are beautiful because they stop the steal by eliminating the deficit. They end the humiliation by reindustrializing the US. They help the middle class by protecting jobs, and they extract reparations from the foreign villains via tariff revenue.

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Moreover, the flip-flops make perfect sense. The base-ism is strong in outraging globalist elite with the tariffs and wise in showing flexibility by forcing foreigners to submit to his will. So all this stuff that looks chaotic and erratic makes perfect sense from this. Now notice that there are no specific economic goals. The tariffs are aimed at redressing emotional grievances of his base. A number of goals are mentioned, but nothing specific enough to hold to it. Okay, now here I want to make this argument that U.S. trade hesitance and hostility is not new and is here to stay. So I already made the argument that it's not new. What I want to make now is the argument that it's here to stay. So let's start at the top of this thing. I think the root problem of the populist, anti-trade globalization policies that are in America and have been for the last 4 presidential cycles of increasing magnitude is middle-class malaise. The American middle class is doing very poorly. Frequent school shootings, obesity epidemics, drug overdoses, deaths of despair, medical bankruptcies, crushing student debt, on and on and on. The middle class is not doing well. So there's really two ways of fixing this.

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They could have— America could have a social and active labor market policy, say like Canada or Europe, to fix the malaise. But that would require higher taxes and bigger government, which, as you all know better than me, is completely off the table in Washington. The alternative then is to go to anti-globalism, to blame globalism for the problems of the American middle class. Now, since protection won't fix the problems of the middle class— in fact, it might make it worse— the protection fails to fix the middle malaise, and we go back up to the loop where the root problem that caused it will continue. So here, anti-globalization— globalism is a policy placebo, and the policy persists politically because it's ineffective economically. And in the book, I make the argument that it cannot help the middle class. I don't have the time to go through those arguments, but I'd be happy to talk about it with Q&A. So now I want to move on quickly to 4 scenarios for the world trading system and ripple effects. So these, these tariffs were so large that they're starting to change tariffs in the whole rest of the world in two ways.

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So the ripple effects from trade deflection— so this is trade deflection— is what happens when America puts up barriers and exports, say, from China can no longer be sold in the United States. Since the factories who are making those exports don't shut down, those exports go somewhere else. And this is coming from work that Chad Bown had done in previous— especially on steel. So from this you get cascading protection, where the diverted trade leads to import surges and new import protectionist pressures, mostly anti-dumping duties. So the trade deflection can lead to more protection in third countries. Now, I've got a typo in the slide here, but the same trade deflection can lead to domino liberalization. So the diverted trade leads to—

and forget about import surges— it leads exporters to seek new markets because they want to resell the stuff that doesn't go to the US. And that puts new political economy pressure on their governments to sign free trade agreements. And indeed, since April 2nd, China and Brazil signed a free trade agreement. The UK and India finally finished a deal that they've been talking about for years because their exporters now are looking for new markets.

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And I think both More liberalization and more anti-dumping will continue as a result of this. Okay, so how does this play out at the world level? Um, there's one ugly scenario, one unlikely scenario. That's the 1930s all over again. That happens if other nations ignore the WTO rules and allow grievance to guide trade policy. And as we all know, there are plenty of grievances out there. The EU against China, China against many people, many people against the United States. If this grievance thing starts going and people put on protection or do liberalization not following the rules, it could start to fall apart. Because the great thing about the WTO rules is it put guardrails on what can be done and tends to reduce the retaliation as long as it sticks to the rules. So the possible triggers are this cascading protection we talked about, if it doesn't follow the rules and thus provokes retaliation. Another very specific one is that China may retaliate against the anti-China provisions that the US is asking for in agreements like the US-UK agreement, which asked UK to strip China out of its steel supply chain. Doesn't say so explicitly, but that's what it's about.

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And China said very explicitly, it won't put up with these kind of anti-China provisions it would retaliate against them. And now with its rare earth magnets, it can in a very specific, very precise way. Now, I don't think that's going to happen because the US only accounts for, say, 15% of world trade. And the countries who account for the other 85% of world trade like the system. They do not feel that they're being victimized. The system— every single one of them have some grievance, some commercial disputes, but they're working through it in the way they have for the last 50 years. So as long as those 85 countries accounting for the 85% of world trade continue to follow WTO rules, the world rules-based trading system will continue. So the first of the scenarios, what I call managed multilateral drift, and that's what's underway, we're going to get more protection and liberalization, but only the U.S. violates the WTO rules on purpose. So in essence, the rest of the world isn't multilateral-centric. It becomes more bilateral and more regional, but it's not violating the WTO system. In some sense, it may be going back to the early 2000s when all the action was outside of Geneva, was regional.

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The second one is more scary where the blocs break up and start fighting among each other, say a US bloc, EU bloc, and a Chinese bloc. And instead of just liberalizing among themselves, they start putting up tariffs against each other, and the thing falls out of— spins out of control as everybody disrespects the WTO rules. Now, the last one, I don't know how likely this is, depends upon how long it lasts, is the United States keeps its big tariffs up and other people have some retaliation against it, and the United States just becomes a more closed economy, but the whole rest of the world moves on. Now remember, India and China were very closed up into the 1990s, but the whole rest of the world did just fine without India and China. And it was better, you know, prosperity worldwide grew when they joined the world economy, but the world lived on without them. And would— and it's possible, it's likely that the world would live on without America. Now, I don't know how likely that is, but that's my third scenario. So I'm going to end right there. Thank you for listening. Most important of all— this is, by the way, the scan code for my freely downloadable book— most important thing for things like this, which is about the future, what nobody knows, is to have conversations with people with many different perspectives.

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And that's what I would like to do, or would hope my book provokes: conversations that allows people to develop their own insights rather than, you know, that my provocations lead you to think harder about what's going on. And I'll stop right there. Thank you very much.

[00:24:58.25] - Mary E. Lovely

Thank you so much, Richard, for that quick overview of this interesting work. I should have said that Richard is a non-resident senior fellow at the Peterson Institute, something we're very proud of. So I'm glad to see it in your name tag at the bottom. I'd like to turn the floor over now to Chad Bown, the Reginald Jones Senior Fellow here at PIIE. Chad?

[00:25:21.25] - Chad P. Bown

Thanks, Mary. So first, a huge congratulations to Richard. The Great Trade Hack is an incredible timely book. It's a fun and as Mary said, it's a really lively read. And as is commensurate with Richard's style, if you haven't read his earlier books, I highly recommend it. Highly recommend them in addition to this one too. So Richard, this book is really needed right now. So congratulations for putting in the time and work to making it happen. Um, what Richard does in this book is a lot of things, uh, and he only briefly touched on them, so you actually are going to have to go and read the book, uh, even after, even after we get through this. But let me kind of summarize, and then I'm going to ask Richard two big questions that I want him to think

about. So what he does is he works through what we know from economic research about why the United States is in the position it's in right now. Um, but he also, I think, usefully works through what policymakers have misdiagnosed about the underlying problems the United States faces, right? The book is also one part explainer about why tariffs are unlikely to achieve some of the objectives that, at least notionally, the president and the administration has put forward as policy goals.

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So, for example, um, Richard lays out why tariffs cannot fix the trade deficit. Richard lays out why tariffs cannot help the middle class, and Richard lays out why tariffs cannot revive manufacturing. My first question is going to be on that last point. On the last one, I want you to say a bit more about what could revive manufacturing. So one thing I really liked about the book is that unlike a lot of other pieces of work at the moment. There is some recognition in your book that countries like the United States— but I don't think this is a uniquely US phenomenon. Similar arguments are happening in Europe and other places as well— that these countries do need a bit more manufacturing of certain strategic things, maybe for reasons of national security in this new era of geopolitical conflict. It might be for reasons of supply chain resilience, right? Having lived through the pandemic, it might be to ensure interdependence and not dependence, excessive dependence, to head off problems of market dominance being weaponized by countries of concern. So the basic economic idea, as I understand it, is we may need to accept some efficiency losses from our old supply chains of, you know, hyper-specialization, um, where in the future we get fewer of the benefits of agglomeration economies.

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And you may need to do this to kind of insure yourself against something. But if it's not tariffs, what policies could it be? Should it be, right? So that's first question. Seems like a really hard problem to solve, but I want you to tell us more about how to proactively do it. The second question is going to stem from the fact that another thing this book does, which, which Richard didn't talk about, but it's another reason why you should read it, is it presents an important diagnosis of what the problem with the US-China economic relationship actually is. And that is that it's a clash of two economic systems, as Richard puts it. And in this world, there's kind of— there's no winning. It's really just a question of How do we manage the relationship better? And he sets out a, a list of ways that could stabilize the relationship. First, to set realistic objectives. So think of your Washington policymakers, set realistic objectives. Second, accept the systemic differences between the two different systems. No one is going to change the Chinese economic system, so stop trying. If you're Washington, commit to institutionalized dialogue. To prevent spiraling and escalation.

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I think Washington and Beijing should commit to these things. If you're Washington, maybe look inward, invest in domestic strength, and then finally take the long view. So those are policy recommendations, and I think there's a lot of good stuff in there. But when we look at the trajectory that we're currently on, the United States doesn't seem to be headed down that path in following those recommendations. It looks like for better or for worse, the United States is in a stage of denial, that not recognizing that those are the things that needs to happen. And it's pushing toward with this tariff world, overcorrecting in the other direction of disengaging itself too much from China, especially on trade, not maybe the decoupling is too far, but certainly probably going too far in the other direction. Okay. So my question for you, Richard, is, If we accept as given the United States is just going to do that, what should the rest of the world do? And it's not obvious to me that we know, right? So take Europe, for example. You pointed out trade deflection, more surge of imports from China. The rest of the world's economies are much closer to the American system, market-oriented.

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Than they are to the Chinese system. If this is really a clash of systems, and if the United States is refusing to engage in that issue of how to fix it, and it's pushing more of the problems onto the rest of the world, and the rest of the world also has the American market-oriented system, what's your advice for the rest of the world? What do they do right now? I read the book is trade agreements, rules-based system, okay, but that doesn't really confront the clash of systems question. And I'm not going to let you duck the question in the way the United States is ducking the question. What's your advice to the rest of the world in dealing with the clash of economic systems? And with that, I'll turn it back to you. Great book.

[00:31:33.09] - Richard Baldwin

Let me— is that okay? Can I respond, Mary?

[00:31:36.06] - Mary E. Lovely

Thank you.

[00:31:37.10] - Richard Baldwin

So let me get to that specific question at the end. And I, I can't remember if I left it in the book or not, but I did a whole thing on subsidies. And deep down, I think if we could somehow put

guardrails on industrial subsidies of China, that would be okay. And it reminds me a little bit of the Green Line Agreement on aircraft that the EU and the US dealt with. They took it outside the WTO. They said, okay, everybody's going to be subsidizing. This is a strange industry, but there are limits. And I think to a certain extent, if Europe and the US could talk with China, get a bit more transparency on what the subsidies are and put some limits on those, accepting that their system is different and they're not going to just let everything go, but putting guardrails on them, that together with standard anti, you know, countervailing duties and dumping duties that China would have to understand would be part and parcel of this whole thing of offsetting them. But I think a fundamental way that, that Chinese industry is being supported is turning the— like, if you want to say one thing, it's subsidies.

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So some sort of a subsidy agreement would, would be useful, and it might very well be just the EU and China doing this to start with, and the US might or might not get involved. But I would have to say that I think China now has an incredibly precise instrument to strike back at countries at a company level with their rare earth magnets. They can shut down anybody's auto sector. They can shut down their military production by company, by shipment. And that tool, I think they will use to try and prevent things from changing too much. But I also think that China really likes the rules-based system, and it's been extremely good for them. And so in some sense, if we could come to a deal like the US and Japan did, where the US and Japan had different systems. Neither one changed their system. And through structural impediments, they came to some sort of entendre of what was allowed and what wasn't. So I'm hopeful for that. But it might take a long time. I agree with that. And certainly would be much, much easier if the US and Europe got together to try and talk about this.

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Not to gang up on China, but to say, you know, look, we have problems too. You have problems, how can we find a modus vivendi? On the first one, thank you for— I did feel, you know, I feel that there's just a lot of the underlying motive of what Trump is trying to do is valid. The middle class in the US is suffering. Something has to be done. I personally don't think what he's doing is going to work. But if it does, that would be great because something has to be done. And the other thing about the industrial— I mean, the US Somehow or another, the way I think of it is we thought the world was nicer than it actually was. There was this end of history dream when China was a panda and Russia joined the G7. Everybody was converging to democracy and pro-market. Well, as it turned out, the world is a dangerous place for good particular reasons. And so the US can't make its own information infrastructure. It has no

capacity to produce 5G equipment. Unbelievable. That's the backbone of the entire modern economy, and the US can't do it. What, what was, what was the thinking there?

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The US actually can't make the ships that it needs, would need in wartime or anything like that, because it allowed that shipping. There was a basically over-belief in the market, and therefore certain strategic industries were lost. So in some sense, this is the way I like to think about it. Governments have never anywhere trusted the market on farms and arms. They're expensive, intrusive, bipartisan policies that promote localization of some food and some military equipment. It's just that now a number of other industries like semiconductors, maybe medical supplies, have tipped over into that. But the free market fundamentalism that was characterizing lots of things meant that it was just left to the market. In any case, the world was a very happy, nice place where you could— it was perfectly sensible to put 90% of your rare earth source in China, or source 90% of your APIs or pharmaceutical inputs from China and then India. That was just fine. So I think we have to go back with that. Now, how to do it? I believe that Biden was doing it reasonably well. Biden got a bipartisan consensus, 10-year plan, lots of money, and he chose strategic industries to start with.

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Now, the big— you know, when you want more industry, you need more workers, you need more infrastructure. This— you can't build one factory at a time because it's a whole cluster and a base, so it needs coordination that the industry itself won't do. So I think it needs an intelligent industrial policy which starts with a few industries and moves forward. And that's, I think, US isn't the only one, as you pointed out. Japan has realized that they should have had more semiconductors than they do now. And Europe is the same thing, and UK is the same thing. So this end-of-history dream put a lot of people to sleep, and I think we need this. But the main, the main thing is, is it's a 10-year project, and it has to be bipartisan. It has to be something that industry thinks investing several hundred billion dollars over 10 years is a good bet, that it will be reliable, the policies will support it. So whether it's pharmaceutical intermediates or it's shipbuilding or whatever it is, the policy, they can rely on it. So that's where I would go with it. So I don't know if I answered your question, but at least I talked a little while.

[00:37:25.28] - Mary E. Lovely

Let me hop in with a question there, Richard, because I have so many, and we see some coming in the Q&A as well. Um, so one of the interesting things for me in the book is that you turn the spotlight away from unfair trade as the cause of this middle-class malaise, or at least as

the only cause or the prime cause. And particularly, you turn away from China's entry into the global trading system, something that is a very commonplace a placeholder for the source of our grievances. And you turn it toward the behavior of US corporates, and in particular, their response to automation and their choice of offshoring. I would add that it's more than US corporates, and it's actually global multinationals who bring us the things that we get from China and have been at least important players in the overdependence that you referred to. So my question is the following: Why hasn't this narrative been more widely embraced? Is it just that we prefer to put it on them as opposed to us? Or is it that there are many people who actually benefited from offshoring and automation? We fail to often acknowledge that many people actually moved up into the upper middle class, just as many people were forced into what we might think of as the working class or the paycheck-by-paycheck folks.

[00:38:53.28]

We're on the verge in the United States of seeing his, you know, Trump-won tax cuts extended and enhanced with the so-called Big Beautiful Bill Act. Why are corporates being rewarded when you're putting them, your finger on them as part of the culprit?

[00:39:10.24] - Richard Baldwin

Okay, so I'm not an expert on the internal workings of the U.S. political system, but It seems that it's easy to blame foreigners. And basically, any other policy which could fix this would require a Canadian-style social policy, at least, if not European. Certainly more active policy. And that, for reasons that are a little hard to understand, over the decades has turned into the third rail— you touch it and you die in American politics. So once you take anything that costs a lot of money off the table, you're left with very few ways of redressing the middle-class malaise. Now, let me come back to your specific point, which is somewhat separate, of the causes of this and the offshoring. And I like to tell— this is in my 2016 book, The Great Convergence— is about a soccer team. So think about globalization before offshoring as, you know, two teams. Who decide, sit down, and they're going to trade players. And maybe one has too many forwards and one has an extra goalie who's really good, and they exchange. And if they actually do that trade, both teams win. That's the idea, it's players for players. Now, in the second, this is like globalization.

[00:40:27.07]

It's like the, the coach of the better team goes and starts training up the less good team on the weekends. Now, this, this— so it's the multinationals who take their technology and combine it with low-wage labor abroad, technology that may have been subsidized by American tax

breaks. That's the coach. Now, for the coach, that's wonderful. The coach gets to sell his to both, and actually the fans like it because the level of the game goes up. In other words, prices go down. People are happy with that. The people who are not happy about it is the players on the better team. Because their monopoly on the technology of the G7 firms has been eroded. So I think that's how it worked. But the political economy of the whole thing is, first of all, many people didn't even see this happening. Offshoring was part of globalization. It was part of, you know, Obama and Clinton thought of that as good stuff. But so I think it was a little bit unnoticed. But I think the political economy wasn't allowing that to move differently. In some sense, trade was never above the radar, the real radar. Most of us, all three of us on this screen, spent our lives, like, struggling to get anybody to care about trade policy.

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It was too boring. But then it was almost like a Maoist revolution. The middle class got so upset and so angry. The traditional Democrats, the traditional Republicans, they weren't addressing the problems. And some guy comes along and says, I'll fix your problem. And populism is not about analysis. It's about anger. So they weren't thinking hard about how to fix it. They were thinking, let's get somebody who says they're going to fix it and give it a go because it can't get any worse. So that's where I would go with that. I think it's kind of the anger spilled over and we no longer were talking rationally.

[00:42:17.20] - Mary E. Lovely

That's very interesting, Richard, and I think it causes all of us to pay attention to the words that are used as we see what happens as the tariffs face the next deadline. Many people are asking other questions, but, but what I have is about cascading protection. You talk about cascading protection where the cascading is coming from the US to other countries who then adopt protectionist policies, and you spoke about that in your opening remarks. But isn't there another form of cascading production, which is to downstream sectors? And it looks like the Trump administration is actually turbocharging this cycle that you're talking about, where they're offering protection to the downstream sectors immediately. We see it with steel, where recently, you know, home appliances have now received a 50% tariff, which is going to cost American households quite a bit of money. So are there any seeds of a counterrevolution, a pushback coming within the United States? The picture you paint is actually fairly bleak for Americans. And for our trading partners, our friends and allies who see this as a process that can't be undone. But isn't there some possibility—

[00:43:35.10] - Richard Baldwin

I'm gonna jump on that. Yeah, so I have a couple thoughts on that. I'm an optimist at heart, so this is why I don't cry myself to sleep every single night. So first of all, tariffs are, inflation is going up and some people just distinguish how much is tariffs and how not. I mean, people like you guys make very careful calculations the Fed does. But in any case, inflation's going up when Trump promised the prices would actually go down. And unlike the first administration, his fingerprints are all over this price rise. He said some people may have to pay $2 more for their Barbie doll, so that when the prices do go up, the middle class may turn against tariffs as a solution to their problem. The second thing is, I think once the big beautiful bill gets passed, this incredible cohesion of Congress will disappear, that the Republicans really are— do not agree. Many Republicans don't agree with these tariff things. Many of them don't agree with other policies. But they're all sticking together because they have to get this bill passed, because, as you know better than me, in Washington, it's not a tax cut.

[00:44:40.04]

If they don't pass this bill, the taxes go back up on the upper middle class, and the Republican will be destroyed for a generation, because why would you ever vote Republican if they can't keep your taxes low? So once that gets passed, and in the first administration, once he passed his tax cuts, he didn't really do anything else that required Congress. So it's possible people in Congress start asking about it. It's possible that the people start thinking that tariffs aren't the be-all and end-all. And it's also possible that these tariffs could kick the United States into a recession. And again, the Trump administration has said, you know, there may be some pain in the short run, but long-run gain. So the fingerprints of the recession and the inflation could be on, on Trump. And one thing we know about Trump is he's a pragmatist. He's willing to back off and declare victory. And so my hope is that the inflation and potential slowdown, maybe even recession, would lead him to at least back off or at least stay at 10%. But the point you said about cascading downstate in the United States, that's just going to accelerate this kind of pressure.

[00:45:43.28]

The second thing is it's almost sure that the Republicans will lose the House in the midterm election. Even if it was a totally normal average presidency, the swing is, is enough that they would lose the majority. And since so much of the promises about lower inflation and not getting involved in foreign wars, since those are pretty obviously not holding, I think the swing will go. And then once the Democrats have the chairmanships of those committees, questions will start to be asked, and it's possible that some of this will get unrolled. So what I believe is that Trump won't back off his 10%, but 50% on steel, 50%— that those, those might get backed off, just like he backed off on China. He's threatening 50% on EU. I don't think he's going to do that either.

But in any case, if he sticks with his 10%, he's happy he has his tariffs. The dollar will offset a lot of that in terms of the cost of living. And then hopefully the world will move on. That's, that's my, my dream at night.

[00:46:41.12] - Mary E. Lovely

Thank you, Richard. So we're at time. You can see that this is a rich conversation. I know, Richard, you'll be speaking in other fora. We have many other events here at the Peterson Institute that we hope everyone joining us online today joins again. Keep the conversation going. I think that's a big part of what Richard intends with this lively and interesting book. Thank you again, Richard, for writing it and giving us this opportunity at the Peterson Institute to host you. I want to thank my colleague Chad Bown for joining and asking such interesting questions. Richard, thanks again, and I wish everybody a great day wherever you are. Stay cool, we're still having a heat wave in the U.S. So many thanks to Richard and to the team here at PIIE.

[00:47:29.20] - Richard Baldwin

Thank you, Mary. Thank you, Chad.

[00:47:31.20] - Mary E. Lovely

You're most welcome.