A US-China Trade Blowout Over Tires

Nicholas R. Lardy, analyzing the origins of the dispute with China over tire imports, warns that the fight could imperil future US-China economic and political cooperation.

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Steve Weisman: This is Steve Weisman at the Peterson Institute for International Economics. Nicholas Lardy, senior fellow at the Institute and coauthor of *China's Rise: Challenges and Opportunities,* is here to discuss an eruption of trade frictions between the United States and China. Thanks for joining me, Nick.

Nicholas R. Lardy: Thank you, Steve.

Steve Weisman: The trade dispute has occurred over an American move to impose duties on imported Chinese tires. China is threatening to retaliate on poultry and vehicles. How serious is this dispute?

Nicholas R. Lardy: It's potentially very serious. So far, we're in the early stages and the amount of product covered is not large and it's possible the two sides will be able to manage this, to contain it. But there's also a chance it could expand dramatically and become quite significant. I think it will have political repercussions, regardless of whether or not it expands to cover more products.

Steve Weisman: In what sense?

Nicholas R. Lardy: The Chinese are, to say the least, quite unhappy about this case for a number of reasons which we can go into. I think it's likely to mean it would be more difficult for them because of domestic political constraints to cooperate with the United States—across a fairly broad range of issues, trying to make progress on North Korea and Iran perhaps even extending into the economic domain in trying to coordinate on global recovery, reform of the international financial regulatory system and so forth.

Steve Weisman: To understand what's at stake and how this happened, let's retrace our steps and walk through it.

Nicholas R. Lardy: The basis for the action of the United States is the fact that imports of tires increased rapidly over the past few years. The union that represented the workers in that industry filed a case with the International Trade Commission.

Steve Weisman: Which is what, remind me?

Nicholas R. Lardy: The International Trade Commission (ITC) is part of the bureaucratic process for adjudicating trade disputes.

Steve Weisman: But it's an American institution….

Nicholas R. Lardy: It's an American institution. They made some recommendations to the President, which the President modified slightly, but did impose protectionism. Now the reason that the Chinese don't like this is that when they became a member of the World Trade Organization (WTO) in December of 2001, they had to agree to this safeguard provision that has now been used for the first time. And China is the only country in the world that has ever agreed to this provision. Most importantly, it allows the United States and other members of the WTO to put restrictions on imports of products from China much more easily than they could put on restrictions from goods coming from any other country.

Most notably, whoever brings the complaint does not have to show that there's any material injury to the industry or the workers in the industry. It is based on this concept of market disruption, and all you have to do is to show that imports of the product have been rising rapidly either in absolute terms or as a share of the total market. So you don't need much investigation to figure out whether workers in the industry or firms in the industry have been materially injured, which you'd normally have to do. All you have to do is come in with that numbers and say, OK, imports of these products have gone up substantially over some period, and the ITC can come to a finding that imports of these products should be restricted.

The other thing that's unique is that normally in a safeguard action, if you restrict imports of a product, you have to restrict them from all countries at the same time. This is a procedure that allows us to restrict imports coming only from China and we don't have to put restrictions—indeed under this procedure we cannot put restrictions on imports coming from any other country.

So Chinese—with some justification, I must say—see this as highly discriminatory. It is a violation of the most basic principle of the WTO, which is you have to treat every member equally. Now the United States says correctly that what we're doing is legal because the Chinese agreed to this special provision when they came in. So the United States can say we're acting in accordance with our trade laws and consistent with our WTO obligations and consistent with the agreements that China made when it came in to the WTO in 2001. The Chinese view, however, is that they were forced to agree to a highly discriminatory practice that fortunately from their point of view up until now has never been exercised. Now eight years in, they're getting hit with it for the first time. They're very upset.

Steve Weisman: As a practical consequence, because this only applies to tires from China, other cheap tires can come in from other countries and fill whatever gap is left by the exclusion of Chinese tires. Is that right?

Nicholas R. Lardy: Yes, and this is quite frankly one of the paradoxes. The union was bringing this case, and the President largely filed the recommendations of the International Trade Commission. Unfortunately there won't be any real benefits to US workers because it's very unlikely that production of these kinds of tires is going to increase in the United States. They're going to be brought in from Brazil or India or some other country.

Maybe not immediately, because the US tire market is very large, and those countries probably don't have the capacity to satisfy all the demand right away. So what that will mean is that prices grow up in the United States in the short run. Within a relatively short period of time I would expect production and third countries will expand, and imports will resume, but they will be coming not from China but from other countries. So it's very unlikely that any new jobs are going to be created in the United States as result to this decision by President Obama.

Steve Weisman: What type of tires are we talking about?

Nicholas R. Lardy: This is by and large the low end of the market, less expensive tires. It's an important segment of the market, but it's still a relatively small segment of the market.

Steve Weisman: Although if people who are hanging on to their cars and not buying new ones maybe they'll at least change the tires and get new cheap tires.

Nicholas R. Lardy: Well, the critics of this decision say that this is adverse for safety, because people who can't afford to buy good tires will no longer be able to buy less expensive tires, and so they'll be driving along on their worn out tires as a consequence of this decision.

Steve Weisman: Why did the Chinese agree to this kind of thing?

Nicholas R. Lardy: Well, this is a very interesting story. But I think the answer is basically that the premier at that time, Zhu Rongji, wanted to use China's membership in the WTO as a lever to accelerate domestic economic reform in China, to open up China more broadly to the international market. The United States and other members who were negotiating for China's entry absolutely insisted that China had to agree to two or three of these provisions. These are provisions that I refer to as "WTO Plus" because they make China's commitments far stronger than any other member that has become member of the WTO.

Steve Weisman: What other countries were the major ones that insisted on this?

Nicholas R. Lardy: The group of countries negotiating with China for its entry was a subset of the membership of the WTO, but it's a fairly large subset. At the end, there were 30 more countries, but there's no question that the United States was in the driver's seat on this issue and insisted on this provision.

Steve Weisman: So they had China over a barrel.

Nicholas R. Lardy: The argument of the administration at the time was, we cannot get a change in US domestic legislation, which would be required for us to recognize China as a WTO member. Unless China would agree to this very, very special provision, which would allow us to restrict Chinese imports practically at the drop of a hat without much investigation, without much transparency and not applied on a multilateral basis. So yes, I think we really had a gun at their head and, given their objectives, they held their nose and agreed to it, hoping that it would never be invoked. Now that hope has been dashed.

Steve Weisman: Did the Bush Administration signal that it was headed in this direction on tires?

Nicholas R. Lardy: No. In the Bush administration, there were four cases that were brought under this particular and very unusual safeguard provision, four cases at the International Trade Commission recommended to the President. And in each case President Bush declined. The President has the ultimate authority. So in the Bush administration there were four cases like this early on. The President said no to all of them and no further cases were filed.

Steve Weisman: Are there any others pending?

Nicholas R. Lardy: There are none pending at the moment. But this opens the door to a very large number of potential cases and in fact, the administration has given a green light to other products, because there are many, many products for which Chinese imports had been increasing rapidly in recent years. If you don't have to show any injury, you bring the data in, you win a ruling from the ITC, and it goes to the President's desk.

Steve Weisman: I remember in the paper case they showed that there was some unfair advantage, but they weren't able to show any injury as I recall.

Nicholas R. Lardy: That's right. In the normal cases of antidumping or safeguards, you have to show what is referred to as material injury. Not only that, you have to show that the increased imports were the most significant cause of the injury. Not changes in technology, or the market demand changed, or any one of a number of other potential factors. Or in the case of the antidumping, you have to prove that the firm in question in the foreign country is selling below cost. You have to have a rigorous investigation to figure out what their costs are and so forth. No such investigation is required in the case of this safeguard for products coming from China.

Steve Weisman: Is it possible that this could lead to some kind of accommodation by the two sides? Are they in the mood to compromise?

Nicholas R. Lardy: Both sides of course have their domestic political constraints. On the Chinese side, the Chinese government is being criticized: Why did China ever agree to this in the first place? Of course it's not the current leaders, it's their predecessors, but the question is still being raised quite strongly. The second question [for the Chinese] as well, given the fact that this provision discriminates against us, what are we going to do to retaliate? Are we going to let the United States kick sand in our face, or are we going to stand up and retaliate? So that certainly explains some of the strong rhetoric we've heard coming out of Beijing condemning the action of the United States, suggesting that China might initiate some proceedings on some products that are important to US firms.

Of course, on the US side, I think the President's decision was largely driven by domestic political considerations: payback for an industry that gave him a very strong support and a labor union that gave him a very strong support and that is helping him on healthcare and other domestic issues.

Steve Weisman: Right, and it's the union and not the industry.

Nicholas R. Lardy: That's right. It's the union. I misspoke. The industry actually did not support the case. They did not want the case filed. They did not want to have restrictions on the import of these less expensive tires coming from China because some of these tires are actually made by US companies that have relocated. The industry has decided they can't produce less expensive tires in the United States competitively. They're putting their resources in the better quality tires and importing the less expensive ones from China. So the industry certainly did not favor the action that was taken by the White House.

Steve Weisman: Nick, thanks for giving us a lesson on tires but also on globalization and trade.

Nicholas R. Lardy: Thank you, Steve.