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Does Trump Know Anything About Trade?

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Left Out, a podcast produced by Paul Sliker, Michael Palmieri, and Dante Dallavalle, creates in-depth conversations with the most interesting political thinkers, heterodox economists, and organizers on the Left.

The Hudson Report is a new weekly series produced by Left Out with the legendary economist Michael Hudson. Every episode we cover an economic or political issue that is either being ignored—or hotly debated—that week in the press.

In this week's episode we talk about the so-called "trade war" developing between the United States and China.

Paul Sliker: Professor Hudson. Welcome back to The Hudson Report.

Michael Hudson: It's good to be here.

Paul Sliker: So the latest breaking news in economics… Washington vs. Beijing. Xi Jinping vs. Donald Trump. A trade confrontation between the two world's largest economies.

China recently responded to President Trump's initial threat of imposing massive tariffs on imports–namely a 25 percent tariff or $50 billion in levy announcements on agricultural and manufactured products–by dismissing this threat and not capitulating to Trump and his trade team. Instead, China introduced plans of their own to impose tariffs of 25 percent on 106 types of U.S. products worth $50 billion including soybeans, aircraft and automobiles.

On Thursday this dispute escalated further after Trump threatened China with $100 billion in additional tariffs on imports. Beijing responded much tougher and quicker than most people in Washington and in the press even expected. The spokesman for th Ministry of Commerce for China was quoted on Friday saying, "China doesn't want a trade war, but we're not afraid to fight a trade war." They reiterated that China will use any measure to fight back and will not exclude any option.

And you know, Michael, we see all the buzz in the headlines of the major financial press and news networks. Things like, "Trump's tariffs gamble with China could be catastrophic for the economy." Some are surmising that this could be very detrimental to his own presidency and the entire Republican Party. It's also been upsetting financial markets to some degree.

All this is predicated on the idea of "unfair trade" practices or "unfair competition" between China and its competitors. So what exactly is going on here from your perspective? Can you give us an idea of what exactly "unfair competition" is from both your vantage point and that of China's competitors?

Michael Hudson: You've asked two questions, and I'll answer them in order. I think that Trump is somewhat out of his league in trying a "good cop/bad cop" bluff by putting a lot of nationalists around him. It is as if he thinks they can make a threat that is going to force China to give up its economic planning.

I think that all Trump really wanted was a symbolic public-relations win to defend his Art of Breaking the Deal strategy. He thought he could get Canada to give him something, even if it was only symbolic, so that he could claim that he had a public relations win. But by making his threat on Twitter and television, without any attempt to actually meet with Chinese trade officials, he led China and other countries to take his gang of nationalists seriously enough to prepare a defense plan of their own. What they've tried to do is say, "Don't even try to go along this route. You're talking about trade, but that has to be put in the context of the overall balance of payments."

What America is trying to do is push a dual standard on the world, just as it did repeatedly in the 60s and 70s: free trade for other countries, protectionism for the United States alone.

Your second question is about how to define unfair competition. From the point of view of a free-market neoliberal, a mixed economy is unfair. Trump considers it unfair for other countries to have public infrastructure investment to lower their cost of living and doing business. But that is exactly how the United States, Germany and every other leading industrial nation built up economic power in the 18th, 19th, and 20th centuries. What China is doing is what U.S. economic planning did in the late 19th and early 20th century. The government is investing in roads, education and basic infrastructure to provide key services at subsidized prices or freely. The objective is to minimize the cost of living and hence the basic wage level and other costs of doing business.

America was able to outcompete with England and other countries by having subsidized education. We built roads, we built huge infrastructure, and the Internet was basically developed by government and turned over to the private sector. America's pharmaceutical patents basically were developed by government laboratories and turned over to the pharmaceutical companies.

But when China provides public support for its own economy, America says that's unfair: You have to privatize everything, you have to tie your hands behind your back by turning China into a Thatcherite economy. It should operate all of its basic public services for profit. That obliges it not only cover its costs of production, it also is supposed to financialize by taking on the cost of credit and borrowing. The basic model is what the British water authorities did with their huge debt leveraging and interest charges.

That would make China so high-cost an economy that America's subsidized economy could undersell it and make it dependent on U.S. foreign policy. That's basically what Trump's saying to them. You can imagine China just laughing.

Paul Sliker: Michael, what exactly is "unfair trade"? I mean we just got into what "unfair competition" is, but what is unfair trade?

Michael Hudson: The way Trump talks "unfair trade" is running a trade surplus with the United States. But remember, the United States is a heavy foreign investor and creditor.

That means there's a huge remission of profits to the United States on capital account. There's a huge remission of debt service and profits from other countries to the United States. So the United States provides other countries with the money to pay their debt to the United States by running a trade deficit.

Let's assume for a minute that the United States had a trade balance with every country – which is what Trump said bilaterally he wants to achieve. If the trade is in balance and America has a huge balance of payments surplus from all the debt service that countries owe in dollars – plus a huge remission of profits by American companies that have bought out foreign industry – then the dollar's exchange rate would soar. As the dollar went up in price, that would mean that third world countries and Asian countries whose international debts are denominated in dollars would have to pay much more of their exports. That means much more of their labor to buy the high priced dollars to pay the debts they owe the United States and other creditors and remit profits on U.S. investments.

So what Trump is asking for is mathematically impossible without a global debt and monetary crisis. His demand for trade balance would price almost all American industry and agriculture out of world markets. It would force other countries to become independent in their food supply and just about everything else. It would be exactly the same balance-of payments tangle that occurred in the 1920s that broke down as a result of the Inter-Allied debts and the German reparations. My textbook on *Trade, Development and Foreign Debt* is all about that debate. John Maynard Keynes said that if you're going to insist in debts being repaid to the United States by the allies for World War I, you have to provide them with the money to pay. That means you have to open your markets. By importing more, you'll provide them with dollars so that they can pay you.

There's a circular flow. But Trump has no idea of how this circular flow works. He confuses the balance of payments with the balance of trade, and says it's unfair for other countries not to agree to drive the world economy bankrupt. He doesn't spell it out, but that would be the result.

What he thinks is unfair is so narrow-minded a tunnel vision that other countries – and American economists themselves – are looking at him and think, "My god, the guy has not a basic course in international trade and balance of payments theory. He's making it up in his mind, and doesn't have a clue that trade and payments are different things."

Paul Sliker: So it's economic illiteracy at its worst.

Michael Hudson: Well the reason the market is going down is that many American investors have invested in China. We run a trade deficit in China, but we also receive a lot of payments *from*China via the American financial institutions and business investors there. Let's say Walmart imports goods from China – $100 dollars worth of imports – maybe only $50 of these $100 (only half) is actually paid for, because the rest is kept here as profits on this trade. Of the remaining $50, maybe $25 consists in raw materials that China imports to make its exports. So what appears to be a trade deficit with China isn't really paid to it in the end. That's part of the fictitious gross national product (GNP) accounting that has twisted around the balance of payments analysis in a kind of "as if" misleading bit. I go into this in my trade theory books. It's hard to explain the tangled accounting that is glossed over in the press without spelling out the circular flow. That's why the press dumbs the issue down, and Trump gets this dumbed-down version from TV.

Paul Sliker: Right. And I think in a future episode we need to go a bit further into this. But Michael, the lay person who doesn't really have time to dive deeply into what all this means…they see these headlines flash across their TV screens, they pick up their daily papers, or scroll through their social media feeds, and they see these two superpowers exchanging language like "war," "battle" and "standoff" when it comes to this trade situation. To the average person, that might appear kind of frightening. I can imagine anyone seeing these two powers go at it with each other with this type of language and I'm sure it's concerning to some degree.

So what are we looking at? What can China do? Are we looking at an actual trade war like some press and pundits are suggesting? What can China do and what do you think is going to happen here?

Michael Hudson: First of all, it's not two powers going against each other. It's one power, the United States, going against China. China has not made any attempt even to reply, because it says there have been no negotiations or discussions with the United States. What Trump says is: America is becoming dependent on China and it's threatening the American way of life. He's defined that as a threat to American dominance. By "dominance," Trump means making other countries dependent on the United States. It means other countries letting the Americans monopolize all the high productivity, high technology, and economic-rent yielding industries, so that we [the United States] can get all the profits. They are supposed to produce the raw materials and manual-labor goods for us, and serve as customers, but we will be in control so that if we don't like China we can do what we did in the 1950s and 1960s and suddenly stop exporting to them. America can threaten to starve them if they don't follow the policies its trade strategists want. That's what it did in the 60s when Canada broke the U.S. sanctions and exported wheat to China to save it.

This idea that other countries are threatening our ability to strangle them is so perverse and so basically asymmetrical and evil that it's jaw dropping! They're not going to be dependent on basic needs on U.S. suppliers because the U.S. can do what it's doing to Russia or Iran, and did to Cuba for years. It can impose sanctions on basic needs that people must have to survive.

What China can do is simple. First of all, it realizes that America wants to make it dependent on the United States, and wants to buy its commanding heights but won't even let China buy gas stations here. So it's trying to achieve its own economic independence so that no other country can suddenly threaten it with sanctions such as has hurt Iran, Russia and other countries.

In terms of what you just read in the newspaper, it can say: OK we're going to put tariffs on soybeans.

Now let's look at what's already happened. Soybean prices have gone down I think 3 percent in one day. That's a huge amount of drop. soybean prices are going down because the markets think that if Trump really follows through with his threats, not just bragging, then China won't buy soybeans. This will cause a soybean oversupply.

China must be overjoyed with all this! Because it doesn't really think that America would dare have a trade war that it would lose. But if Trump does try to go this route, China can buy soybeans much cheaper! Because the soybean farmers and markets areso afraid that it will to retaliate that it can buy food cheaper as a result of the low soybean prices. So China can talk strong and then make contracts to buy soybeans more cheaply as the market fears domestic U.S. oversupply.

Suppose the United States imposes a 25 percent tariff on goods that China is sending to Walmart. China can impose export duties. It can say, "If the United States government is importing so cheaply that there's room for a 25 percent import tariff, we're going to put a 25 percent *export*duty, so that we'll get as much revenue from this private sector trade as the U.S. government is getting. Of course, that will vastly increase the price to American consumers. You can imagine the political response here.

Paul Sliker: I was just going to follow up on that point, Michael. Looking at this through the lens of the average American watching this story. I think you might have just answered a little bit there. What could this do to the average American in terms of the price of goods, or even in terms of jobs? It might have an effect on work and labor. What sort of outcomes could you see play out?

Michael Hudson: The trade flows have established such a mutual dependency that if there's any kind of a trade war or interruption of trade or tariffs, then consumer prices for the goods subject to tariffs are going to go up.

Trump has tried to avoid imposing tariffs on consumer goods because he realizes that that's unpopular. So he's put them on producer inputs. He's raised the tariffs on goods that American manufacturers need like steel and aluminum for starters. What that means is that there will be a world oversupply of steel and aluminum for rival manufacturers in other countries to enjoy. So what Trump is doing by his tariffs is to make America a higher-priced manufacturing country relative to other countries. He's giving the rest of the world – Europe and Asia – a cost advantage over American producers, at the same time he's raising the cost of living for American consumers.

So the effect of what he's trying to do is to be to make American workers earn less and consumers pay more.

Paul Sliker: Michael, I want to close this week's 'Hudson Report' by asking you, as an expert on trade and tax policy and someone who has advised several governments around the world on these policies, what is your idea of or proposal for a truly "fair trade" system?

Michael Hudson: Oone of the problems is what Trump has pointed to: intellectual property rights. What that means is monopoly rights.

I think that domestically, most countries have rules against monopoly pricing, because it's unfair. Monopoly pricing is charging something for nothing. It's much more than you actually need to pay. Some of the worst examples of these intellectual property rights are pharmaceuticals. I think that patent rights support this rent extracting system. So I would like to see an international trade rule that opposes monopoly rent extraction. No patent or intellectual property right would be recognized as being legal under international law if it produces a super-profit for a product that other countries can make with the same technology. Technology for making drugs and for making pharmaceuticals and for making basic needs should be available to everybody. Just doing it first should not be allowed to make other people dependent because of a monopoly privilege.

Ironically, it was Walt Disney that's been pressing to double all of the patent right time periods so that they can keep Mickey Mouse and the movie rights. So some intellectual property rights like Walt Disney are going to make super profits like Hollywood films. My anti-monopoly rent rule would apply largely to pharmaceuticals and basic needs for key producers whose only function is to maintain their monopoly rights to extract unfairly high prices from foreign countries dependent on these needs.

Fair pricing would be when countries sell, as they say in the textbooks, at the actual cost of production without special monopoly privileges such as the United States wants to build for its own exports, while wanting to block other countries from doing the same thing.

Paul Sliker: Well we'll be tracking this story closely Michael. I'm sure we'll have another opportunity to discuss this soon, as I don't think the story will be going away. But Professor Michael Hudson we will talk to you next week. As always, thank you very much for joining The Hudson Report.

Michael Hudson: Wel, it's good to follow the news this way.

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