The Return to Protectionism

Pablo D. Fajgelbaum   Penny K. Goldberg
Patrick J. Kennedy   Amit K. Khandelwal

UCLA, Yale (on leave WB), Berkeley, Columbia GSB

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Introduction

- In 2018, the U.S. raised tariffs on 12.7% of its imports
  - Avg tariff ↑ from 2.6% to 16.6%

- Trade partners retaliated by raising tariffs on 8.2% of U.S. exports
  - Avg tariff ↑ from 7.3% to 20.4%

- Largest return to protectionism since ’30 Smoot-Hawley

- We study short-run impacts on U.S. economy
This Paper

- **What were the effects on trade volumes and prices?**
  - Use tariffs to identify import demand and export supply elasticities

- **What were the aggregate and regional impacts on the U.S. economy?**
  - Embed elasticities in G.E. model and compute impacts of trade war

- **Time span:**
  - Short-run analysis
  - From 2017m1 to 2019m4
This Paper

- What were the effects on trade volumes and prices?
  - Use tariffs to identify import demand and export supply elasticities

- What were the aggregate and regional impacts on the U.S. economy?
  - Embed elasticities in G.E. model and compute impacts of trade war

Main results:

1. Imports of targeted varieties: -31.7%
2. Tariffs completely passed to tariff-inclusive import price
3. Consumer loss: -.27% GDP
   - Aggregate effect -.04% GDP
4. Data: Higher import protection in electorally competitive counties
   - Republican counties most negatively affected due to retaliation
Road Map

- Data and Event Study
- Trade Elasticities
- Aggregate and Regional Impacts
<table>
<thead>
<tr>
<th>Tariff Wave</th>
<th>Date Enacted</th>
<th>Products (# HS-10)</th>
<th>2017 Imports (mil USD)</th>
<th>2017 (%)</th>
<th>Tariff (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Solar Panels</td>
<td>Feb 7, 2018</td>
<td>8</td>
<td>5,782</td>
<td>0.2</td>
<td>0.0</td>
</tr>
<tr>
<td>Washing Machines</td>
<td>Feb 7, 2018</td>
<td>8</td>
<td>2,105</td>
<td>0.1</td>
<td>1.3</td>
</tr>
<tr>
<td>Aluminum</td>
<td>Mar-Jun, 2018</td>
<td>67</td>
<td>17,685</td>
<td>0.7</td>
<td>2.0</td>
</tr>
<tr>
<td>Iron and Steel</td>
<td>Mar-Jun, 2018</td>
<td>753</td>
<td>30,523</td>
<td>1.3</td>
<td>0.0</td>
</tr>
<tr>
<td>China 1</td>
<td>Jul 6, 2018</td>
<td>1,672</td>
<td>33,510</td>
<td>1.4</td>
<td>1.3</td>
</tr>
<tr>
<td>China 2</td>
<td>Aug 23, 2018</td>
<td>433</td>
<td>14,101</td>
<td>0.6</td>
<td>2.7</td>
</tr>
<tr>
<td>China 3</td>
<td>Sep 24, 2018</td>
<td>9,102</td>
<td>199,264</td>
<td>8.3</td>
<td>3.3</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td></td>
<td><strong>12,043</strong></td>
<td><strong>302,970</strong></td>
<td><strong>12.7</strong></td>
<td><strong>2.6</strong></td>
</tr>
</tbody>
</table>
### Panel B: Retaliatory Tariffs on U.S. Exports Enacted by Trading Partners in 2018

<table>
<thead>
<tr>
<th>Retaliating Country</th>
<th>Date Enacted</th>
<th>Products (# HS-10)</th>
<th>2017 Exports (mil USD)</th>
<th>Tariff (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>China</td>
<td>Apr-Sep, 2018</td>
<td>7,474</td>
<td>92,518</td>
<td>6.0</td>
</tr>
<tr>
<td>Mexico</td>
<td>Jun 5, 2018</td>
<td>232</td>
<td>6,746</td>
<td>0.4</td>
</tr>
<tr>
<td>Turkey</td>
<td>Jun 21, 2018</td>
<td>244</td>
<td>1,554</td>
<td>0.1</td>
</tr>
<tr>
<td>European Union</td>
<td>Jun 22, 2018</td>
<td>303</td>
<td>8,244</td>
<td>0.5</td>
</tr>
<tr>
<td>Canada</td>
<td>Jul 1, 2018</td>
<td>325</td>
<td>17,818</td>
<td>1.2</td>
</tr>
<tr>
<td>Russia</td>
<td>Aug 6, 2018</td>
<td>163</td>
<td>268</td>
<td>0.0</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td></td>
<td><strong>8,073</strong></td>
<td><strong>127,149</strong></td>
<td><strong>8.2</strong></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th>2017</th>
<th>2018</th>
</tr>
</thead>
<tbody>
<tr>
<td>Retaliatory Tariff</td>
<td></td>
<td></td>
<td>8.4</td>
<td>18.9</td>
</tr>
<tr>
<td>Mexico</td>
<td></td>
<td></td>
<td>9.6</td>
<td>28.0</td>
</tr>
<tr>
<td>Turkey</td>
<td></td>
<td></td>
<td>9.7</td>
<td>31.8</td>
</tr>
<tr>
<td>European Union</td>
<td></td>
<td></td>
<td>3.9</td>
<td>29.2</td>
</tr>
<tr>
<td>Canada</td>
<td></td>
<td></td>
<td>2.1</td>
<td>20.2</td>
</tr>
<tr>
<td>Russia</td>
<td></td>
<td></td>
<td>5.2</td>
<td>36.8</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td></td>
<td></td>
<td>7.3</td>
<td>20.4</td>
</tr>
</tbody>
</table>
Trade War Timeline

U.S. Tariffs

Retaliatory Tariffs
Event Study

- Compare trends of targeted varieties relative to untargeted varieties:

\[ \ln y_{igt} = \alpha_{ig} + \alpha_{gt} + \alpha_{it} + \sum_{j=-6}^{3} \beta_{0j} I(event_{ig} = j) + \sum_{j=-6}^{3} \beta_{1j} I(event_{ig} = j) \times target_{ig} + \epsilon_{igt} \]

  - FEs: variety (\(\alpha_{ig}\)), product-time (\(\alpha_{gt}\)), country-time (\(\alpha_{it}\))
  - cluster: country, HS8

- Event date:
  - \(ig \in \) targeted products: assign date of tariff implementation
  - \(ig \notin \) targeted products:
    - assign earliest event date within NAICS4
    - if no NAICS4, use: NAICS3, NAICS2, or February 2018
Event Study: Imports
Road Map

- Data and Event Study
- Elasticity Estimates
- Aggregate and Regional Impacts
U.S. Demand System

- Nested Constant-Elasticity (CES) demand within tradeable sector
  - By origin within imports of a product
  - Across imported products
  - Between imports and domestic

- Tiers:
  - Bottom: HS10 Import demand: \( m_g = \left( \sum_{i} a_{ig} \frac{m_{ig}^{\sigma-1}}{\sigma-1} \right)^{\frac{\sigma}{\sigma-1}} \)
  - Middle: 4-digit NAICS import demand: \( M_s = \left( \sum_{g \in G_s} a_{Mg}^{\eta} m_{g}^{\eta-1} \right)^{\frac{\eta}{\eta-1}} \)
  - Upper: sector demand: \( C_s + I_s = \left( A_{D_s}^{\frac{1}{\kappa}} D_s^{\frac{\kappa-1}{\kappa}} + A_{M_s}^{\frac{1}{\kappa}} M_s^{\frac{\kappa-1}{\kappa}} \right)^{\frac{\kappa}{\kappa-1}} \)
Variety Import Demand and Export Supply

- Imports and exports of product $g$ from country $i$:

\[
m_{igt} = A_{igt} \left( (1 + \tau_{igt}) p_{igt}^* \right)^{-\sigma}
\]

\[
p_{igt}^* = z_{igt} m_{igt}^{\omega^*}
\]

- Estimate:

\[
\Delta \ln m_{igt} = \alpha^M_{gt} + \alpha^M_{it} + \alpha^M_{is} - \sigma \Delta \ln \left( (1 + \tau_{igt}) p_{igt}^* \right) + \varepsilon^M_{igt}
\]

\[
\Delta \ln p_{igt}^* = \alpha^X_{gt} + \alpha^X_{it} + \alpha^X_{is} + \omega^* \Delta \ln m_{igt} + \varepsilon^X_{igt}
\]

- $\tau_{igt}$ identifies both elasticities if uncorrelated with supply/demand shocks

  - Romalis 04, Zoutman et al. 18

- Checks

  - Correlation with pre-existing trends
  - Event study of targeted vs untargeted varieties
  - Allow for leads/lags
Import Demand, Foreign Export Supply \( \{\sigma, \omega^*\} \): Intuition

A denotes the pre-tariff equilibrium. If the tariff increases, import demand falls.

B denotes the price the exporter receives.

C denotes the price the importer pays.
Variety-Level Import Elasticities \( \{ \sigma, \omega^* \} \)

<table>
<thead>
<tr>
<th></th>
<th>(1) ( \Delta \ln m_{igt} )</th>
<th>(2) ( \Delta \ln p_{igt} )</th>
<th>(3) ( \Delta \ln p_{igt}^* )</th>
<th>(4) ( \Delta \ln m_{igt} )</th>
</tr>
</thead>
<tbody>
<tr>
<td>( \Delta \ln (1 + \tau_{igt}) )</td>
<td>-1.47***</td>
<td>0.58***</td>
<td>0.00</td>
<td>-2.53***</td>
</tr>
<tr>
<td>( \Delta \ln m_{igt} )</td>
<td>(0.24)</td>
<td>(0.13)</td>
<td></td>
<td>(0.05)</td>
</tr>
<tr>
<td>( \Delta \ln p_{igt} )</td>
<td></td>
<td></td>
<td></td>
<td>(0.26)</td>
</tr>
</tbody>
</table>

Product \( \times \) Time FE | Yes | Yes | Yes | Yes |
Country \( \times \) Time FE | Yes | Yes | Yes | Yes |
Country \( \times \) Sector FE | Yes | Yes | Yes | Yes |
1st-Stage F | 36.5 | 21.2 | | |
Bootstrap CI | | | [-0.14,0.10] | [1.75,3.02] |
R2 | 0.13 | 0.11 | 0.00 | . |
N | 2,454,023 | 2,454,023 | 2,454,023 | 2,454,023 |

Notes: cluster by country and hs8

- Implies: \( \Delta \ln (p_{igt}^* m_{igt}) = -\sigma \frac{1 + \omega^*}{1 + \omega^* \sigma} \Delta \ln (1 + \tau_{igt}) = -31.7\% \)
Other Elasticities

- Aggregate tariffs to product and sector level to estimate upper nests

- Across imported HS-10 products: \( s_{Mgt} = a_{Mg} \left( \frac{p_{Mg}}{P_{Ms}} \right)^{1-\eta} \)
  - Estimate \( \hat{\eta} = 1.53 \) (se 0.27)
  - Targeted product imports fall 2.5%
  - No impact of tariffs on product-level import price indexes

- Between imports and domestic in 4-digit NAICS: \( \frac{P_{Ms}M_s}{P_{Ds}D_s} = \frac{A_{Ms}}{A_{Ds}} \left( \frac{P_{Ms}}{P_{Ds}} \right)^{1-\kappa} \)
  - Estimate \( \hat{\kappa} = 1.19 \) (se 0.49)
  - Targeted sector imports fall 0.2%

- Variety-level exports: \( x_{ig} = a^*_i \left( \left( 1 + \tau^*_i \right) p^{X}_{ig} \right)^{-\sigma^*} \)
  - Estimate \( \hat{\sigma^*} = 1.04 \) (se 0.32)
  - Targeted variety exports fall 9.9%
Road Map

- Data and Event Study
- Trade Elasticities
- Aggregate and Regional Impacts
Aggregate Impacts

\[-m' \Delta p^M + x' \Delta p^X + \Delta R = EV\] (Dixit & Norman 80)

- **Neoclassical Model**
  - Static
  - Flexible prices
  - No labor mobility

- **U.S. demand**
  - Cobb-Douglas over 88 traded sectors, 1 NT sector
  - Within sector: CES ($\sigma, \eta, \kappa$) over products and countries

- **U.S. supply**
  - Cobb-Douglas in labor and capital (fixed), intermediate inputs (may adjust)
  - 3067 U.S. counties

- **Trade partners**
  - Movements along variety-level demand ($\sigma^*$) and supply ($\omega^*$)

- **Matched to 2016 County Business Patterns, I-O tables, trade**
Import Prices

\[
\hat{p}_{ig} = \frac{\omega^*}{1 + \omega^* \sigma} \left( \hat{E}_s + (\kappa - 1) \hat{P}_s + (\eta - \kappa) \hat{P}_{Ms} + (\sigma - \eta) \hat{p}_{gM} \right) + \frac{1}{1 + \omega^* \sigma} \frac{d\tau_{ig}}{1 + \tau_{ig}}
\]

\[
\approx \frac{d\tau_{ig}}{1 + \tau_{ig}}
\]

- Implies:
  - \( m' \Delta p^M = -.27\% \text{ of GDP} \)
  - \( = \text{import share of GDP (15\%) \times targeted share of imports (13\%) \times avg. \text{ tariff increase (14\%) } \)
Export Prices

\[ \hat{\rho}_s = \frac{1}{\Phi_s} \left( \text{DomExp}_s + \text{Tariff}_s + \text{Cost}_s \right) \]

where (imposing \( \omega = 0 \))

\[ \text{DomExp}_s \equiv P_{Ds} D_{s} \hat{E}_s \]

\[ \text{Tariff}_s \equiv (\kappa - 1) \sum_{g \in G_s} \sum_{i \in I} P_{Ds} D_{s} \frac{p_{ig} \hat{m}_{ig}}{p_{s} Q_{s}} \frac{d \tau_{ig}}{1 + \tau_{ig}} - \sigma^* \sum_{g \in G_s} \sum_{i \in I} P_{Dg} x_{ig} \frac{d \tau_{ig}^*}{1 + \tau_{ig}^*} \]

\[ \text{Cost}_s \equiv \frac{\alpha_{I,s}}{\alpha_{K,s}} \hat{\phi}_s + \sum_{r \in \mathcal{R}} \pi_r \frac{p_{s} Q_{sr}}{p_{s} Q_{s}} \frac{\alpha_{L,s}}{\alpha_{K,s}} \hat{w}_{sr} \]

\[ \Phi_s \equiv 1 - \frac{1 - \alpha_{K,s}}{\alpha_{K,s}} + \frac{P_{Ds} D_{s}}{p_{s} Q_{s}} \frac{P_{Ds} D_{s}}{E_{s}} + \frac{P_{Ds} D_{s}}{p_{s} Q_{s}} \left( 1 - \frac{P_{Ds} D_{s}}{E_{s}} \right) \kappa + \left( 1 - \frac{P_{Ds} D_{s}}{p_{s} Q_{s}} \right) \sigma^* \]

• Implies:
  - \( x' \Delta p^X = 0.05\% \) of GDP
  - export share of GDP (7%) \( \times \) export price increase (0.7%)
Export Prices, No Retaliation

\[ \hat{p}_{ig}^X = \hat{p}_s = \frac{1}{\Phi_s} \left( \text{Dom}\hat{\text{Exp}}_s + \text{Tariff}_s + \text{Cost}_s \right) \]

where (imposing \( \omega = 0 \))

\[ \text{Dom}\hat{\text{Exp}}_s \equiv \frac{P_{Ds}D_s}{p_s Q_s} \hat{E}_s \]

\[ \text{Tariff}_s \equiv (\kappa - 1) \sum_{g \in G} \sum_{i \in I} \frac{P_{Ds}D_s}{p_s Q_s} \frac{p_{ig} m_{ig}}{E_s} \frac{d \tau_{ig}}{1 + \tau_{ig}} \]

\[ \text{Cost}_s \equiv \frac{\alpha_{l,s}}{\alpha_{K,s}} \hat{\phi}_s + \sum_{r \in \mathcal{R}} \frac{p_s Q_{sr}}{p_s Q_s} \frac{\alpha_{L,s}}{\alpha_{K,s}} \hat{\omega}_{sr} \]

\[ \Phi_s \equiv \frac{1 - \alpha_{K,s}}{\alpha_{K,s}} + \frac{P_{Ds}D_s}{p_s Q_s} \frac{P_{Ds}D_s}{E_s} + \frac{P_{Ds}D_s}{p_s Q_s} \left( 1 - \frac{P_{Ds}D_s}{E_s} \right) \kappa + \left( 1 - \frac{P_{Ds}D_s}{p_s Q_s} \right) \sigma^* \]

Implies:

- \( x' \Delta p^X = 0.09\% \) of GDP
- = export share of GDP (7%) \( \times \) export price increase (1.2%)
Timeline: 2019 Waves

- $436b imports targeted, $203b retaliations

May 2019
- 15% tariff increase on $200b of already targeted Chinese varieties
- China retaliates on already targeted $60b of US exports
- US removes steel/aluminum tariffs on Canada and Mexico (but not EU/others)

June 2019
- US removes India from Generalized System of Preferences (GSP) list
- India retaliates with tariffs on $1.3b of US exports (mostly agriculture)

Sept 2019
- 10% tariff increase on ~$125b of previously untargeted Chinese varieties
- China retaliates on previously untargeted ~$75b of US exports

Oct 2019
- US enacts 10-25% tariffs increases on ~$7.5b imports from the EU.
- EU promises retaliation, but has not yet acted.

Dec 2019
- US and China call off further escalations. Both countries lower some, but not all, trade war tariffs. China commits to increase purchases of U.S. exports. Negotiations continue...
Aggregate Impacts: + 2019 Waves

\[ -m' \Delta p^M_{EV^M} + x' \Delta p^X_{EV^X} + \Delta R = EV \]

<table>
<thead>
<tr>
<th></th>
<th>EV^M</th>
<th>EV^X</th>
<th>\Delta R</th>
<th>EV</th>
</tr>
</thead>
<tbody>
<tr>
<td>(1) Full Trade War Change ($ b)</td>
<td>-65.2</td>
<td>13.0</td>
<td>44.7</td>
<td>-7.4</td>
</tr>
<tr>
<td>(2) Change (% GDP)</td>
<td>-0.35</td>
<td>0.07</td>
<td>0.24</td>
<td>-0.04</td>
</tr>
<tr>
<td>(3) With Retaliation Change ($ b)</td>
<td>-63.0</td>
<td>13.5</td>
<td>47.7</td>
<td>-1.8</td>
</tr>
<tr>
<td>(4) Change (% GDP)</td>
<td>-0.34</td>
<td>0.07</td>
<td>0.26</td>
<td>-0.01</td>
</tr>
</tbody>
</table>

top=\{\hat{\sigma} = 2.53, \hat{\eta} = 1.53, \hat{\kappa} = 1.19, \hat{\omega}^* = -0.00, \hat{\sigma}^* = 1.04\}.

bottom=\{\hat{\sigma} = 2.35, \hat{\eta} = 1.1, \hat{\kappa} = 1.19, \hat{\omega}^* = 0.06, \hat{\sigma}^* = 1.05\}. 
Regional Impacts in the News: Imports

The New York Times
‘How Long Can We Last?’ Trump’s Tariffs Hit Home in the U.S.

Chicago Tribune
As tariffs begin, Northwest Indiana auto workers and farmers share concerns

THE WALL STREET JOURNAL.
In a Pennsylvania Steel Town, Donald Trump’s Tariff Is a Winner

U.S. Steel to Expand Under Tariffs
Metal maker to restart construction at Alabama plant as higher profit

Swing State Steel
States with the biggest number of metal-refining furnace operators and tenders

- Indiana: 2,050.0
- Pennsylvania: 1,640.0
- Alabama: 1,200.0
- Ohio: 1,200.0
- Michigan: 1,020.0

Whirlpool Wanted Washer Tariffs. It Wasn’t Ready for a Trade Showdown.

Bloomberg Businessweek
You can’t find a clearer example of the steel industry’s disagreement over the Trump tariffs than in Canton, Ohio, where the tariffs are pitting Timken against Timken. TimkenSteel Corp., which makes steel
Regional Impacts in the News: Exports

The New York Times
A Farmer’s Tough Year on the Trade War’s Kansas Front
From planning to harvest, the grain belt’s rhythms and prospects have been disrupted by the government’s tariff battle with China.

The Washington Post
North Dakota soybean farmers, caught in the trade war, watch the season run out on their crop

Des Moines Register
Iowa farming’s $2.2 billion trade loss could ripple through state’s economy

THE WALL STREET JOURNAL.
Take Our Cheese, Please: American Cheese Makers Suffer Under New Tariffs
Chinese, Mexican tariffs on U.S. cheese and whey are hurting farmers and driving up stockpiles
Panel B: Tariff Increase on US Exports, 2017-2018
Weighted by Variety-Level US Export Share and County-Level 2016 Tradeable Sector Employee Wage Bill

Mean = 4.17 p.p., std = 2.67
Real wage decline across counties: avg. 1.0% (s.d. 0.5%).
Tradeable Wages and 2016 GOP Vote Share

Δ Real Tradeable Wage (%)

2016 GOP Presidential Vote Share

- Full War
- Without Retaliations
Conclusion

1. Large and declines in import and export values

2. No import price decline from targeted countries
   - Complete pass-through to import prices

3. Very small aggregate effect (-.04% GDP)
   - Consumer loss (final use+intermediate): -.27% GDP

4. Higher import protection in electorally competitive counties
   - but...Republican counties most negatively affected due to retaliation

Caveats

- Retail prices, uncertainty, country-level effects, longer run,...