Skinny China Deal

The so-called “skinny” trade pact with China marks a truce in the U.S.–China trade war and could be a stepping stone to a broader agreement. Here are the key provisions.

The United States dropped plans to impose new tariffs on $156 billion of Chinese goods, including smartphones, consumer electronics, and toys, that were scheduled to go into effect on December 15. (China indicated it would drop plans for retaliatory tariffs.) It’s estimated that these tariffs would have cost U.S. households an average of $150 annually on top of the $400 annual costs of previous tariffs, so the pullback is good news for consumers. The United States also agreed to cut tariffs on $120 billion of Chinese goods from 15% to 7.5%. However, 25% tariffs on $250 billion of Chinese goods will remain in effect, providing leverage for future negotiations.[7–8]

In return for the tariff relief, China has agreed to purchase an additional $200 billion in U.S. goods and services over the next two years, with pre-tariff 2017 levels as a baseline.[9] This would include an additional $32 billion in agricultural goods over the two-year period, bringing total Chinese agricultural purchases to $40 billion annually, with China working to raise it to $50 billion.[10] After a difficult year of weather- and tariff-related losses, U.S. farmers welcomed the potential market expansion. Still, there are concerns about how China might reach these levels, which are significantly higher than peak agricultural imports before the tariffs.[11]

Although no details were released, the deal also addresses intellectual property rights, forced technology transfer, financial services barriers, and unfair currency practices.[12]

North American Market

The U.S.-Mexico-Canada Agreement regulates more than $1.2 trillion in annual trade among the three countries. The USMCA maintains the NAFTA framework of an open North American market, while adding additional controls aimed primarily at the auto industry, the Mexican labor market, and the Canadian dairy industry.[13]

To avoid tariffs under the USMCA, a car or truck must have 75% of its components manufactured in the United States, Canada, or Mexico, up from 62.5% under current rules. At least 30% of labor on a vehicle must be performed by workers earning a minimum of $16 per hour, about three times what Mexican workers currently earn, increasing to 40%

for cars by 2023. While these rules should help U.S. workers, they may also lead to higher auto prices and drive manufacturing of some small cars to Asia.[14]

Mexico will be required to make it easier for workers to form unions, which in theory should drive wages upward and make it less profitable for U.S. companies to move operations south of the border. Mexican trucks that cross the border will have to meet more stringent safety regulations. Stronger enforcement procedures on these promises were key to gaining support from U.S. labor unions, which generally have not supported free-trade agreements.[15]

Although much of Canada's protective dairy regulations remain in place, U.S. farmers will be able to sell more dairy products in Canada along with additional sales of U.S. eggs and poultry. For its part, Canada was able to retain a dispute process that has allowed it to successfully contest U.S. lumber restrictions.[16]

The USMCA also includes stronger and more modern protections for intellectual property and data, environmental measures such as protecting marine wildlife from pollution and overfishing, and enhanced provisions against currency manipulation.[17]

An analysis of an earlier version of the USMCA by the U.S. International Trade Commission projected that it would raise U.S. gross domestic product by a modest 0.35% and create 176,000 U.S. jobs over a six-year period, including 28,000 jobs in the auto industry. The Trump administration projects 76,000 new auto industry jobs.[18]

Looking Ahead

These agreements could reduce some of the uncertainty surrounding trade and provide new business opportunities that may help stimulate the U.S. economy. As with any agreement, however, their impact depends on compliance by all parties. The China deal is tenuous, and it remains to be seen whether China will fully comply with the phase-one agreement and — perhaps even more important — whether there will be a phase two that leads to a broader resolution of conflicts between the world's two largest economies.

All investing involves risk, including the possible loss of principal, and there is no guarantee that any investment strategy will be successful.

1, 7) *The Wall Street Journal*, December 13, 2019

2, 18) CNN, December 19, 2019

3) Fox Business, December 13, 2019

4) *The Guardian*, December 12, 2019

5–6) CNBC, December 13 and 16, 2019

8) China Briefing, December 16, 2019

9, 12) Office of the U.S. Trade Representative, 2019

10) *The Wall Street Journal*, December 14, 2019

11) CNN, December 16, 2019

13–17) *The Washington Post*, December 10, 2019

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