

Words put to action: How can the EU react to a protectionist US policy?

Briefing 15 February 2017

Donald Trump's announcement to become a president unlike any Washington has ever seen has materialised in relation to international trade and international relations: Trump wants to make America great again by means of protectionist measures. Which consequences may arise and how can the EU react?

Prosperity and strength by means of protectionism?

"Protection will lead to great prosperity and strength."

Trump made his attitude towards foreign trade and international relations clear in his inauguration speech on 20 January 2017. This attitude is at odds with the *Ricardian model*, according to which trading profits in international trade are based on the different degrees of productivity of the workforce in different countries and the resulting price advantages. The export of goods and services allows for trade profits, where a country enjoys comparative advantages. However, in order to realise these comparative advantages international free trade is required. This in turn is one of the founding principles of the World Trade Organisation (*WTO*).

Protective tariffs and other trade barriers contrary to WTO law are jeopardising the US's position as a pioneer in international trade. The US is currently the second biggest exporter and the biggest sales market for import worldwide, but risks suffering economic losses in the event that the international community takes countermeasures against Trump's protectionism. Moreover, Trump is disregarding the key to success of America's current trade regime: the achievements of the IT and technology sectors are based on recruiting foreign talent and the automobile industry's success is heavily reliant on international trade. Lastly, the President fails to correctly assess the importance of services in international trade; US firms are global market leaders in this field.

Therefore, it is highly likely that the protective duties, localisation duties and the preferential treatment of US companies and the US workforce will hamper international trade and economic growth, rather than lead to prosperity and strength.

Violations of public international law

Trump's strategy is also problematic with regard to international law. Trump's guiding principle serves as a good example of this: "*We will follow two simple rules – buy American and hire American*". If "*buy American*" is to be understood as an instruction to American authorities, such an order would violate the Government Procurement Agreement (*GPA*). The treaty regulates the access to public contracts and prohibits preferential treatment of domestic goods, services and providers (prohibition of discrimination, Art. IV sec. 1).

Furthermore, the movement of goods could be restricted by means of non-tariff barriers to trade, e.g. protective tariffs on German automobiles, which would be a violation of the General Agreement on Tariffs and Trade (*GATT*). The agreement proscribes the elimination of protective tariffs and other restrictive measures (Art. XI).

"*Hire American*" could be understood as an invitation to violate the *General Agreement on Trade in Services (GATS)*. Participating states to the GATS have to grant each other equal treatment (Art. II sec. 1).

The US is committed to these rules of international law since it is a member of the WTO (including membership of GATT and GATS) and a participating state in the GPA. With a violation of these rules, certain consequences, which are described in the following, will ensue:

Options for Action for the EU

How should – or better – how can the EU react to the new US trade policy? The US government has not yet established any punitive tariffs or other barriers to trade. Based on the example of signing an executive order to withdraw from the negotiating process of the Trans-Pacific Partnership (*TPP*), the President has demonstrated his eagerness to put his words into action. Thus, the protectionist measures announced by Trump might be implemented sooner than expected.

Option 1: Retaliation Measures

The EU could follow calls by some within the European media to take retaliation measures. Such measures would most likely entail punitive tariffs on American products and services. However, these would be in violation of WTO rules and EU law. Adopting retaliation measures would also contribute to the risk of instigating a full-fledged "trade war", as such measures would be viewed unfavourably by the US government.

Option 2: WTO Dispute Settlement

WTO member states can rebuke violations of another member state in the context of a dispute settlement procedure. Within the WTO regime, the Dispute Settlement Body (*DSB*) comprising member state representatives and independent experts as consultants, accepts such complaints. The EU could have the compliance of US protective measures with WTO law assessed in this multi-level process.

To have protective measures assessed in an international forum, such as the WTO dispute settlement mechanism, is a sensible and lawful option. However, such a process will be complex and protracted. Awards rendered in the course of the dispute settlement mechanism also face the issue of enforceability. According to recent estimates, only 25% of all restrictive measures found non-compliant in the WTO dispute settlement mechanism are lifted by the violating state in consequence thereof.

Option 3: The Gap-filler Strategy (When two people quarrel, a third rejoices.)

As another option, the EU could take the position of the “gap-filler” and fill-in as a reliable trade partner whenever the US government withdraws from trade deal negotiations. As an overall strategy, the EU could increasingly initiate trade deal negotiations with countries around the globe. A recently published [overview](#) of trade deals currently under negotiation suggests that such a strategy has already been adopted.

There would be no legal mechanism by which the US could contest the gap-filler strategy. In addition, such a strategy would ultimately boost free trade. As a result, the European economy would be strengthened and the presumed success of protectionism refuted. Although a protracted process, the advantages of free trade could be illustrated to Trump this way.

The solution: A robust multilateral trade regime

In conclusion, a retaliatory offensive led by the EU would be short-sighted. A sensible answer to protective measures by the EU could be a combination of the remaining two options presented: the WTO dispute settlement mechanism and filling the gaps left by the USA.

This is also the strategy of Mexican President Enrique Peña Nieto who views open dialogue in place of confrontation as a viable solution for re-opening negotiations on the North American Free Trade Agreement (*NAFTA*): Mexico increasingly wants to turn

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towards other global economic regions and strengthen ties with the remaining partners of the TPP. The EU should answer to protective measures by the US with international dispute settlement procedures within the framework of the WTO and likewise seek new ways to open the EU to international trade. Ultimately, only a robust multilateral trade regime will be able to withstand protectionist trade policies.

BLOMSTEIN will continue to monitor the developments in the US closely and will provide updates on any significant developments relating to sanctions or trade matters. Please do not hesitate to contact [Roland Stein](#) or [Sarah Bayer](#) if you have any questions.