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The Real Reason for Trump's Steel and Aluminum Tariffs  
March 15, 2018

By [MARTIN FELDSTEIN](#)

*The Trump administration's proposed tariffs on steel and aluminum imports will target China, but not the way most observers believe. For the US, the most important bilateral trade issue has nothing to do with the Chinese authorities' failure to reduce excess steel capacity, as promised, and stop subsidizing exports.*

CAMBRIDGE — Like almost all economists and most policy analysts, I prefer low trade tariffs or no tariffs at all. How, then, can US President Donald Trump's decision to impose substantial tariffs on imports of steel and aluminum be justified?

Trump no doubt sees potential political gains in steel- and aluminum-producing districts and in increasing the pressure on Canada and Mexico as his administration renegotiates the North American Free Trade Agreement. The European Union has announced plans to retaliate against US exports, but in the end the EU may negotiate – and agree to reduce current tariffs on US products that exceed US tariffs on European products.

But the real target of the steel and aluminum tariffs is China. The Chinese government has promised for years to reduce excess steel capacity, thereby cutting the surplus output that is sold to the United States at subsidized prices. Chinese policymakers have postponed doing so as a result of domestic pressure to protect China's own steel and aluminum jobs. The US tariffs will balance those domestic pressures and increase the likelihood that China will accelerate the reduction in subsidized excess capacity.

Because the tariffs are being levied under a provision of US trade law that applies to national security, rather than dumping or import surges, it will be possible to exempt imports from military allies in NATO, as well as Japan and South Korea, focusing the tariffs on China and avoiding the risk of a broader trade war. The administration has not yet said that it will focus the tariffs in this way; but, given that they are being introduced with a phase-in period, during which trade partners may seek exemptions, such targeting seems to be the likeliest scenario.

For the US, the most important trade issue with China concerns technology transfers, not Chinese exports of subsidized steel and aluminum. Although such subsidies hurt US producers of steel and aluminum, the resulting low prices also help US firms that use steel and aluminum, as well as US consumers that buy those products. But China unambiguously hurts US interests when it steals technology developed by US firms.

Until a few years ago, the Chinese government was using the Peoples Liberation Army's (PLA) sophisticated cyber skills to infiltrate American companies and steal technology. Chinese officials denied all wrongdoing until President Barack Obama and President Xi Jinping met in California in June 2013. Obama showed Xi detailed proof that the US had obtained through its own cyber espionage. Xi then agreed that the Chinese government would no longer use the PLA or other government agencies to steal US technology. Although it is difficult to know with certainty, it appears that such cyber theft has been reduced dramatically.

The current technology theft takes a different form. American firms that want to do business in China are often required to transfer their technology to Chinese firms as a condition of market entry. These firms “voluntarily” transfer production knowhow because they want access to a market of 1.3 billion people and an economy as large as that of the US.

These firms complain that the requirement of technology transfer is a form of extortion. Moreover, they worry that the Chinese government often delays their market access long enough for domestic firms to use their newly acquired technology to gain market share.

The US cannot use traditional remedies for trade disputes or World Trade Organization procedures to stop China's behavior. Nor can the US threaten to take Chinese technology or require Chinese firms to transfer it to American firms, because the Chinese do not have the kind of leading-edge technology that US firms have.

So, what can US policymakers do to help level the playing field?

This brings us back to the proposed tariffs on steel and aluminum. In my view, US negotiators will use the threat of imposing

the tariffs on Chinese producers as a way to persuade China's government to abandon the policy of "voluntary" technology transfers. If that happens, and US firms can do business in China without being compelled to pay such a steep competitive price, the threat of tariffs will have been a very successful tool of trade policy.

<https://www.project-syndicate.org/commentary/trump-steel-tariffs-targeting-china-by-martin-feldstein-2018-03>

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*Martin Feldstein, Professor of Economics at Harvard University and President Emeritus of the National Bureau of Economic Research, chaired President Ronald Reagan's Council of Economic Advisers from 1982 to 1984. In 2006, he was appointed to President Bush's Foreign Intelligence Advisory Board, and, in 2009, was appointed to President Obama's Economic Recovery Advisory Board. Currently, he is on the board of directors of the Council on Foreign Relations, the Trilateral Commission, and the Group of 30, a non-profit, international body that seeks greater understanding of global economic issues.*