Casualty of the Trade War

BY KENT WHEILER

The US-China trade war has taken a heavy toll on American farmers and the wood products industry. Through August 2019, US exports of logs and lumber to China are down nearly one billion dollars ($940 million). Softwood lumber export volumes to China are down 63%, softwood logs down 38%, hardwood lumber down 40%, and hardwood logs down 35%. The impact has been a painful blow for the US industry and will have long-term implications.

Overcutting in China throughout much of the 20th century led to gradually declining domestic harvests and finally a total ban in 2017 on commercial harvests from natural forests. A growing economy, rising incomes, booming housing market, and a thriving furniture industry led to China becoming the world's largest importer of wood products. Exports to China were particularly important for US producers recovering from the 2008-2009 recession, especially hardwood lumber mills. In the years following the recession, US hardwood lumber exports to China grew five-fold, with China eventually taking one-fourth of all graded hardwood produced in America.

Storm clouds began gathering in early 2018 as the US imposed tariffs on solar panels, washing machines, steel, and aluminum. China retaliated with tariffs of 15-25% on $3 billion of US goods, but not lumber or logs. Another round of tariff increases and tit-for-tat retaliation during the summer of 2018 continued to spare wood products. But in September, the US imposed a 10% tariff on $200 billion of Chinese imports, scheduled to increase to 25% on January 1. China retaliated with 5-10% tariffs on $60 billion of US imports, this time including logs and lumber. The January 1 increase was delayed twice but went into effect on May 10, 2019. China retaliated on June 1, increasing tariffs to 10-25% on $60 billion of US imports, including most US log and lumber products.

The impact has been huge, with US log and lumber suppliers losing nearly one billion dollars in sales to China in the first eight months of 2019. To put this in perspective, the sales lost are nearly equal (96%) **to a total loss** of all US log and lumber exports to Mexico, Japan, Vietnam, and Western Europe **combined** over the same period. There is simply no other market or combination of markets that can absorb the lost volume.

Of course, this collapse in demand has had a negative effect on prices in all markets. At the end of August, prices in Washington state for Douglas-fir #2 sawlogs were down 19% from the prior year. Alder sawlog prices are down 30%. *Hardwood Review Weekly's* Green Price Index for hardwood lumber is down 20% and the Kiln Dried Index has dropped 17%. Mills are losing both volume and value.

Short-term fluctuations in volume can often be managed, but long-term loss of market share is difficult to recapture. China is turning to Europe, Russia, Africa, and Southeast Asia for supply. While China has increased average tariffs on US goods to over 20%, average tariffs on the rest of the world have dropped from 8% to 6%. As noted earlier, US softwood logs to China are down 38% August year-to-date, but China's total imports from around the world are up 3%. Likewise, American softwood lumber is down 63% but China's total imports are up 16%. China's total imports of hardwood logs and lumber are down 20% through August but have dropped nearly twice as much from the US.

The loss in market share is especially unfortunate because the nature of consumption in China has changed significantly over the past 20 years. The American Hardwood Export Council estimates that in 2000, 85% of US hardwoods sent to China were re-exported as furniture and other valueadded products back to the US or other global markets. Now it is nearly the opposite, with 80% of incoming US hardwoods staying in China and consumed domestically.

The change in supply channels also has negative environmental implications because many of the growing sources of supply in Russia, Africa, and S.E. Asia are not diligent about sustainable harvesting.

Certainly, there are real problems with some economic practices in China, including industrial subsidies and other support of state-owned enterprises, insufficient intellectual property protection, and forced technology transfer. But consider these points:

• For many years the forest products industry has had a trade surplus with China. To solve barriers faced by other industries, is it fair or wise to penalize businesses that have already developed profitable and net positive supply chains to China? Is it fair to damage their business in order to improve access for others?

• Tariffs are paid by the importer of record. Who ultimately pays depends on market conditions and alternatives for supply. If the supplier does not reduce prices, the importer must either cut their margin or raise prices, and then consumers ultimately pay. When consumers pay, it is a regressive form of taxation. Current research overwhelmingly indicates that US consumers are bearing the bulk of the increased tariff burden.

• Tariffs are a negligible source of revenue for the US government. In fiscal year 2019, total customs duties will be about $70 billion, representing 2% of federal tax revenue. And the increase in duties from the trade war has been largely offset by the $28 billion in relief given to US farmers—relief that was not shared with the forest products industry.

• A trade deficit is not itself evidence of trade barriers, nor is it true that "fair" trade will result in balanced trade. The US has often run a trade deficit during times of economic expansion, including over the past decade of economic growth and declining unemployment. Rather, the fundamental cause of a trade deficit is an imbalance between a country's savings and investment rates. The US consumes more than we produce. Private and public debt are growing. Money flowing out to pay for imports flows back in as investment or financing of the national debt. To reduce the trade deficit, Americans must save more and spend less. Otherwise, the trade imbalance merely shifts to other countries.

Threatening and implementing wholesale tariffs to force myriad changes, often unrelated to the products being taxed, is wreaking havoc on the global trading system and many US companies and farmers, including the forest products industry. The associated uncertainty retards investment and depresses economic growth. To effectively change Chinese government and business practices we need to work within the global trade system the US created and in cooperation with our allies. Let's fight for fair trade, but let's do so in an organized fair way that does not punish our industries that have already accomplished what we want for everyone. ◆

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