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Trade Disputes: Why Trump's Position Is Much Weaker against EU than China*

US President Donald Trump insists that his country is being treated unfairly by both the EU and China in terms of commercial trade. By this he means that European and Chinese companies and their employees live on exports to the USA, while Americans benefit far less from market access to Europe and China. This is why Trump is threatening to start a trade war. He sees himself as in the stronger negotiating position – he thinks that isolation would damage China and Europe more than it would the USA. This reasoning is not only flawed because imports of foreign products are extremely useful to the demand-side, which includes both consumers and companies.

It is also misguided since the EU at least does not earn any more income in the USA than the USA does in Europe. This impression can only arise by focusing exclusively on trade with goods and services. Revenues, however, are also generated by US companies via profits of their subsidiaries in Europe. The current account between the US and the EU, which includes not only trade in goods and services, but also the profits generated in a specific foreign market, is actually balanced. Believe it or not, there is no US deficit. In trade in goods with the USA the EU ran a surplus of 153 billion US dollars in 2017. In services, by contrast, the USA posted a surplus of 51 billion US dollars, and in so-called primary income, which mainly consists of corporate profits, the US surplus was as high as 106 billion US dollars.

So overall, the Americans generated slightly higher revenues in the EU than vice-versa. The main reason for this is that US companies with subsidiaries in Europe earn far more money than European companies in the USA. The fact that corporate profits play a greater role for the USA than export-based revenues is due to the fact that the US economy is more focused on digital business models and immaterial assets. A comparatively high number of US companies, for example, hold patent and brand rights in EU countries with attractive tax laws like, for example, The Netherlands, and generate high profits there by granting licences in other EU countries. These profits are not shown in the balance of trade, but do feature in the current account, which covers the entire exchange of goods and services.

This is clearly illustrated by the current account balance between The Netherlands and the USA. Like Germany, The Netherlands is often criticised for its trade surplus. In fact it is running an astronomical current account deficit of 98 billion US dollars against the USA. This is primarily due to the fact that US companies in The Netherlands generate a surplus of 68 billion US dollars in corporate profits, which accounts for two thirds of the surplus generated in Europe as a whole. This illustrates that it makes no sense for the USA to look at bilateral deficits or surpluses with individual European countries. US companies tend to pool their profits generated across the entire EU in The Netherlands for tax reasons. That is why the US deficit against Germany in trade in goods gives an incomplete picture of economic relations.

Overall, the idea that the USA benefits less from market access to the EU than vice-versa is a fairy tale. That is why Trump is mistaken if he believes that he can blackmail the EU with the advantages of US market access. The USA stands to lose at least as much as the EU by blocking this access. In case of a trade war, the EU would just need to make use of other instruments next to tariffs, like taxing the revenues of internet giants like Google and Facebook, for example. But it would of course be far better to avoid such a conflict.

The US position vis-à-vis China is different. Chinese companies exported goods worth 506 billion US dollars to the USA in 2017, while the USA sold a total of just 130 billion US dollars-worth of goods in China. In services the USA generated a surplus of 38 billion US dollars, but in terms of corporate profits China was once again streets ahead. Chinese companies earned 34 billion US dollars with their activities in the USA, while American companies in China earned only around half of this figure.

The USA's overall current account deficit against China totalled 358 billion US dollars in 2017, which is effectively very imbalanced. This is primarily due to the fact that China has long since restricted investment by foreign companies in the Chinese market; and has failed to adequately protect the intellectual property of foreign investors. If the USA were to use its negotiating power against China to encourage the country to open up its markets, all concerned would ultimately benefit.

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