Testimony for the Joint Informational Hearing of the

California State Assembly

Select Committee on International and Regional Agreements

and the Standing Committees on Agriculture and on Jobs and Economic Development

Introduction

I would like to thank Assemblymember Levine, the Select Committee, and the Standing Committees for the opportunity to talk with you today about the trade war between the United States and China, especially its impact on consumer budgets, jobs, and growth.

Impact on consumers

So far, the U.S. has levied 25 percent tariffs on about $250 billion worth of goods from China

- This is a 25 percent tax on the goods as they cross the border into the United States.
- Recent academic research by top trade economists suggests that the entire cost of this tax is born by U.S. firms and consumers.
    - We see full pass-through of the cost of the tariff into the price of the good paid by U.S. importers at the border (the unit values).
    - We also see that tariffs imposed so far have led to increases in both the Producer Price Index, which measures the prices that U.S. firms pay for inputs into production, as well as related groups of goods within the Consumer Price Index, which measures the prices that U.S. consumers pay for goods in stores and other venues.
- In addition to the direct cost of the tax, researchers have observed that firms from the U.S. or other countries whose goods are not subject to tariffs raise the prices of their goods when a Chinese competitor loses its cost advantage due to a tariff.
- A feasible range of possible costs of 25 percent tariffs on all $550 billion worth of U.S. imports from China for an average household making roughly 60,000 a year is between $300 and $800, without counting extra possible price hikes from producers who take advantage of the less competitive, tariff-protected environment.
    - The cost of the tariffs is similar to a hidden sales tax of between roughly ½ and 1 percent for the average household, but spread less evenly across goods.
    - Similar to a sales tax, tariffs appear to hit low- and middle-income households harder in the sense that these households spend a higher fraction of their income—more of their income is subject to the current tariffs compared to high-income households.
- If we count the hangups involved as households have to buy goods they like less, sourced from less cost-efficient producers—the costs are much higher. Economists can only compute the deadweight loss with complex models, but it at least doubles the overall cost to the average household.

- The goods targeted by the tariffs are not always the only ones where the tax increase shows up. Retailers spread the increased costs of tariff-targeted goods across other goods to minimize declines in the quantities they sell. This may ensure maximum pass-through of the costs to consumers.
- Goods already hit include furniture, lamps, vacuum cleaners, mattresses, television cameras, refrigerator-freezers, luggage and handbags, vinyl tile floor coverings.
- Goods in the $300 billion list that will go into effect if trade talks are not successful include laptops, cell phones, TVs, video game consoles, clothing, footwear, kitchenware, microwave ovens, lithium-ion batteries, ceiling fans, sporting gear

Jobs

- California exports $178 billion in goods to the world, supporting about 700,000 U.S. jobs.
- It is hard to estimate exactly how many firms in California export to China, but more than 70,000 firms export goods from California and China is the destination for nearly 10 percent of California's exports.
    - There are more than 53,000 jobs and 2,500 businesses located in California that are particularly vulnerable to retaliatory tariffs due to the fact that China is the destination for more than 20 percent of the industry's exports from California. These include logging and timber; swine, sheep, and goats; fish and marine products; oil and gas; mining and quarrying; industrial machinery; and motor vehicle manufacturing.
    - In addition, some industries are particularly vulnerable because their goods were moved to the 20-25 percent level for retaliatory tariffs by China last month. These include wood/logging, machinery, cosmetics and skincare, wine and spirits, beef, honey, and processed foods with vegetables and fruits
- Some jobs have been created by tariffs in the industries they protect from rival suppliers in China.
    - Due to the distortions and inefficiency introduced by using tariffs to create jobs, economists so far have found that each job created by recent tariffs on particular industries (steel and washing machines) costs U.S. consumers between $490,000 and more than $800,000 per year to maintain, even though the average salary for these jobs is between $50,000 and $60,000.
- Due to the efficiency losses of the distortionary taxes (tariffs) and retaliation, the balance of jobs created in expanding industries versus jobs lost in contracting industries is likely to be negative.
    - The Trade Partnership estimates that steel and aluminum tariffs plus a 25 the tariffs on Chinese goods currently in place may create 126,900 jobs over 3 years, but cause 1,061,400 workers to lose jobs due to retaliatory tariffs and other costs, with a net cost of $490,900 for each job created.
    - The Tax Foundation estimates that the tariffs currently in place will result in a net loss of 155,000 jobs.
    - Research from UCLA, Yale, and Columbia University shows that retaliatory tariffs have eroded real wages in the most exposed local labor markets, suggesting that retaliatory tariffs are largely offsetting protective effects of tariffs in local labor markets.

    - My own analysis shows that jobs located in California in industries that use steel as an input outnumber jobs in California involved in producing steel by 200 to 1.
- The tariffs are likely to shrink the size of the U.S. economy and be a headwind for U.S. GDP growth.
    - The Tax Foundation estimates the tariffs will shrink the overall size of the U.S. economy by $50 billion.
    - The Federal Reserve Bank of New York Liberty Street Blog published estimates from an academic study suggesting that the tariffs could shrink the size of the U.S. economy by $95 billion, the vast majority of this ($79 billion) coming only from last month's increase in tariffs from 10 to 25 percent on $200 billion of U.S. imports from China.
    - China accounts for 1/3 of global growth and is an important source of demand for many countries' exports. So any slowing in China could generate headwinds for U.S. GDP growth through its effect on global growth.