TRADE talks

A podcast about the economics of trade & policy
with Chad P. Bown

Episode 204. Is Europe Ready for Trump?

Episode webpage

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Transcript

(lightly edited)

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Chad Bown: When it comes to international trade, President Donald Trump has a special distaste for trade with the European Union.

At the first Cabinet meeting of his second term on February 26, the President was asked by a reporter about any import tariffs he had in mind for the EU:

Reporter: *Mr. President, on the EU tariffs. Mr. President, have you made a decision on what level you will seek on tariffs on the European Union?*

President Donald Trump: *We have made a decision, and we'll be announcing it very soon. And it'll be 25 percent, generally speaking, and that'll be on cars and all other things.*

And the European Union is a different case than Canada — different kind of case. They've really taken advantage of us in a different way. They don't accept our cars. They don't accept, essentially, our farm products. They use all sorts of reasons why not. And we accept everything from them, and we have about a $300 billion deficit with the European Union.

But European Union has been — it was formed in order to screw the United States. I mean, look, let's be honest. The European Union was formed in order to screw the United States. That's the purpose of it, and they've done a good job of it, but now I'm president.

Chad Bown: If, or maybe when, President Trump does impose tariffs on Europe, the big question becomes, how will Europe respond?

To help us understand Europe's position in all this, I will be joined by a very special guest.

Rupert Schlegelmilch: Rupert Schlegelmilch

Chad Bown: Rupert Schlegelmilch is a former European Commission trade official. While he worked in the Commission for over 30 years, for the last 5 years, he was DG Trade's main official in charge of trade relations with the United States.

Hi, Rupert.

Rupert Schlegelmilch: Hello, Chad.

Chad Bown: You are listening to an episode of *Trade Talks*, a podcast about the economics of trade and policy. I'm your host, Chad Bown, the Reginald Jones Senior Fellow at the Peterson Institute for International Economics in Washington.

THE EPISODE

Chad Bown: I want to provide a quick update on where things stand in President Trump's latest trade war.

Advertisement: If you have not already done so – do check out the Peterson Institute's new tariff tracker on the PIIE website titled "Trump's trade war timeline 2.0: An up-to-date guide."

OK, at the moment, President Trump has tariffs coming on European steel and aluminum under Section 232 – this is that national security law – and those are scheduled to go into effect on March 12th. Trump has ordered his US Trade Representative to look into EU member states' digital services taxes (DSTs) on American tech companies; so, we may see US tariffs on Europe there sometime in the future.

He also has the reciprocal tariffs investigation ongoing. That one is due to wrap up on April 1st. So we could see higher US tariffs on whatever European products have a higher current tariff rate than their US tariff equivalent through that rationale.

Or we could just see 25 percent tariffs on Europe, like President Trump said at the cabinet meeting.

There is obviously still a lot of uncertainty, but what we also know is the likelihood of President Trump imposing tariffs on Europe seems to be increasing by the day. On March 4th, he put another round of 10 percent tariffs on China. Much more surprising was President Trump's decision that day to also impose 25 percent tariffs on most everything the United States imports from Mexico and Canada, after initially pausing that tariff threat for 30 days back in February.

Apparently tariffs on historical US military allies are not just threats this time around. They are happening for real.

OK, Rupert, to Europe. Before we get into anything specific about tariffs, let's set the scene for some of the underlying economics here.

How interdependent are the US and European economies?

Rupert Schlegelmilch: First, the European Union is by far the most important economic partner of the United States.

The second point that I would like to make up front is our relationship is balanced. No one is taking advantage of the other. We actually have a shared interest to nurture this relationship, and it's going very well. What people also maybe don't know is that our bilateral trade in goods and services has doubled in the last 10 years. Where else do you have that growth? American exports to the EU in the last three years are up 35 percent, so that creates jobs and prosperity in the United States.

Sometimes there is the idea that because of a trade deficit in goods, there is an imbalance. But let me now start with something else, let me start with services. The US last year exported $462 billion worth of services to the EU. That leads to a surplus of $117 billion. We never talk about that. There is a goods deficit of $169 billion, but if you add up the sums, you're left with a $50 billion difference. That's not a lot in a $1.7 trillion relationship per year. It's only about 3 percent.

On the depth and the importance of the relationship, again, I don't want to overload the figures here. But be aware that over 50 percent – almost 60 percent – of what the US or the EU invest in the world goes to the partner across the Atlantic. And just to give you an example, there are three and a half million jobs directly dependent on EU investment in the United States. So, if you start messing with this relationship, you will actually affect jobs in the United States.

What people can really visualize is the biggest BMW plant in the world, which is in South Carolina. It's not in Munich. And there are similar examples of the deep investment relationship. So, that's my first point, a deep and balanced relationship.

Chad Bown: So, President Trump, when he's talking and focused on the unbalanced relationship in his view, he has a very, very narrow perspective, which is just looking at goods trade – i.e., all the cars coming in from Germany and the rest of Europe into the United States and many fewer cars going back in return. But there are a lot of cars produced by European companies in the United States.

And there's an imbalance in the other direction when it comes to services. And so those services are going to be things like Netflix and the Internet companies, as well as financial services. And when you put all those things together, the relationship is much more balanced.

That being said, it looks like there's a really good chance that President Trump is going to end up putting some sort of tariffs on European goods coming into the United States.

So what I want to ask you about next is Europe's preparedness for this.

Now, obviously, you were part of the Commission the first time around, when President Trump was in office between 2017 and early 2021. You didn't take up your job as head of the trade relationship with the United States until 2019. So you weren't there for all of it, but you got to see some of it.

What can you tell us about things that happened in the trade relationship with the first Trump administration and Europe that might be useful "lessons learned" for this time around?

Rupert Schlegelmilch: This is not the first time we are either threatened or experiencing US tariffs. And you refer to the Section 232 tariffs, which went into place on steel and aluminum and which were threatened on cars in that period.

I think the experiences were, at the time, twofold. First of all, you have to prepare yourself from a position where you can actually also take countermeasures. But even more importantly, you have to try to find a way to negotiate on these issues. And this is exactly what happened in 2018. We were able to – and let's start with the good news – to avert the car tariffs with a negotiation, doing a deal, which is one of the things that President Trump likes to do. So, we did a deal to buy more liquified natural gas (LNG) and to buy more soybeans from the United States in return for not having tariffs put on cars.

We were less successful on the other threat – and the implemented tariffs at the time – which were the tariffs on steel aluminum. And here we actually took countermeasures.

It took a while to do that because we have a procedure to go through. But we used a legal procedure – for the non-initiated, under the GATT/WTO safeguard rules – to countervail the tariffs with our own tariffs. And we did implement them. So, on the Trump administration, the first administration, we actually remained stuck with tariffs on both sides.

Chad Bown: I want to talk a little bit more about Europe's experience with countermeasures. As you mentioned, the EU was ultimately effective at being able to implement a rebalancing when it came to the US steel and aluminum tariffs. But just having this constant threat of other tariffs that were out there – during almost the entirety of that administration, there was a threat of 25 percent tariffs on cars, as you mentioned. There were also threats of potential tariffs if countries did digital services taxes.

From an outsider's view, it seems as if that was happening, it looks like Europe was learning that maybe didn't have all of the policy levers that it might want available should something like that happen again. Tell us a little bit about some of the new policy instruments that the European Union has developed in the meantime, since that first Trump administration.

Rupert Schlegelmilch: Yes, indeed, I think we learned a lesson from the first Trump administration. And that is that we might not have all the tools for a similar situation occurring in the future. With a similar situation, I mean what we call coercion – i.e., weaponizing of trade for any possible political objective – which was not done frequently or at all or a lot in the first 20 years of the WTO.

So, it's actually from the experience with the car tariffs, plus certain things also happening on the other side of the globe – i.e., China – that we thought we needed an instrument which allows us to counter any threats when we actually implement what we thought were legal, non-discriminatory, balanced, proportionate policies.

So we came up with this idea of an anti-coercion instrument (ACI), which is a tool which allows us to take measures after a quite detailed procedure and within the rules based international order, against what we would define as economic coercion.

One thing which also led to the creation of this instrument is the fact that WTO litigation, which is our preferred way to deal with any conflict, takes years. And there is no Appellate Body any longer, which would actually give a final ruling. So, we wanted to be quicker, but let's be clear, the anti-coercion instrument is not a rapid response mechanism.

Chad Bown: Let's get into some of the potential ways in which use of this new anti-coercion instrument might play out. So let's go through a hypothetical. Let's suppose President Trump decides to raise US tariffs on European exports – it could be for any number of reasons that he's proposed already, but let's suppose it's this reciprocity rationale where he's basically said to countries, "if you don't lower your tariffs to my level, I'm going to raise my tariffs to your level." Let's suppose he just does that.

How would the EU actually operationalize this anti-coercion instrument in practice? How does it work?

Rupert Schlegelmilch: It is a carefully tailored tool which starts with an investigation to establish the fact – i.e., is there coercion? Then it goes into a procedure where you will try to negotiate away the issue. So, it's not immediate, even if there is a finding of coercion, that you take countermeasures. You try to negotiate – i.e., talk softly with a big stick, maybe you can say that.

And only when that fails, then there is the possibility to take countermeasures. And what is also innovative here is that the countermeasures which can be authorized under this procedure are quite broad. So it's not only goods, because that might not be effective. And in any case, with a tariff on goods, you shoot yourself in the foot because it's a tax on your own imports.

So the instrument also allows countermeasures in other areas like services, government procurement, or the protection of intellectual property rights.

Chad Bown: Now, the European Commission has never actually utilized this anti-coercion instrument in practice. It's primarily a deterrent, so we don't have any experience for how it would do so. But it's an interesting intellectual exercise to think through how the retaliation actually might be used.

One option is, of course, just to impose tariffs on goods. But if your relationship is asymmetric and you don't have a lot of goods imports from the United States coming in that are easily replaceable, maybe that wouldn't be an effective deterrent. So maybe you'd go with something else.

Another option you suggested is maybe you try to put a discriminatory tax on US services exports. Some of the versions of the original digital services taxes (DSTs) coming from EU member states, like France, did seem really designed to target American big tech companies. If memory serves, French Finance Minister Bruno Le Maire called the French one the “GAFA tax” for targeting Google, Apple, Facebook, and Amazon at the time.

Or the third one you mentioned is maybe the EU retaliates by going after intellectual property rights protection. That one has always been a little unclear to me – i.e., how you would put that into practice.

For example, suppose the EU tries to punish the United States by withholding IP protection for American companies. Maybe the idea here is to try to hurt Hollywood by giving away free rights in France to show American movies. While French consumers might like that, to my mind, where the retaliation breaks down is France's own movie industry would likely be super annoyed. And that's because French citizens are now getting free American movies, so they're less likely to pay to watch French movies.

Anyway, these are interesting ideas, but perhaps still some kinks to work out in terms of implementation, but we will be tracking them closely.

OK, you also mentioned that the ACI is not a rapid response instrument. In response to Trump's tariffs this time around, we have seen countries like China and Canada retaliate in potentially just days. Do we have any sense at all for how long we're talking about here between when the EU begins an ACI investigation and the point at which countermeasures could be imposed?

Is it four weeks, six months, 18 months? How long are we thinking?

Rupert Schlegelmilch: Well, the regulation, if you look at it, has certain deadlines which run into several months normally. So I think it's safe to say it's not going to take four weeks, it's going to take longer for the investigation to conclude and to do all of this.

And this is the point that is difficult to verify – is how much time we can spend on negotiations, because I really want to put the cursor on the fact that we are dealing with an administration in the US who likes to do deals. So, we have stretched out our hands and say, we are ready to do deals, which is one phase of the instrument. Ultimately, it will take quite a while, also because of the politics involved.

Chad Bown: Let's go back to one other thing with the anti-coercion instrument. Talk us through how the European Commission thinks about this ACI instrument in a WTO context.

Normally one would say that if a country is going to do something to my trade that I don't like, my response isn't to take matters into my own hands, but it's to bring a dispute to Geneva and the WTO. And that's the line that I've understood the EU to be pushing for – not only for itself – but for others as well, for decades. How does the ACI fit into this?

Rupert Schlegelmilch: Yeah, make no mistake, we still push – and this is the possibility to do a little advertisement for the WTO, which is a little bit in the background now – we are still multilateralists and believe that conflicts should be solved wherever possible in the WTO. Because the value of the predictability of WTO rules is something we cherish a lot.

But we've also come to the conclusion that this is not always the only possible response to safeguard our rights. For the reasons I mentioned, WTO dispute settlement is not functioning. It wasn't meant to look at situations of economic coercion. It was meant to look at commercial disputes or mis-led legislation.

So what we did with the anti-coercion instrument to make sure that the legal basis is compatible with the WTO – if you look at the explanatory part of the regulation – it clearly sets out that this is based on international law, the UN Charter, the duties of countries to cooperate and refrain from coercion, et cetera, et cetera.

So we grounded it in public international law in order to have a solid base to react – not to act to react to a breach of law, and for this we needed the public of the international law scene because the WTO on its own doesn't provide the measures or the tools to actually react to this situation.

Chad Bown: Just as we've never seen the Commission operationalize use of the anti-coercion instrument in practice, we also haven't seen litigation under the WTO that might challenge the legality of the anti-coercion instrument actually play out in any WTO rulings to know just how consistent or inconsistent it might be. So that in itself is an open question.

DEAL-MAKING

Chad Bown: It's certainly the case that President Trump does like to do deals as well. What can you tell us about some of the other "lessons learned" from the EU side from the first Trump administration? Just reading the reporting, it seems as if some senior level officials have already come to Washington to meet their counterparts in the Trump administration to get some of these conversations going already.

Rupert Schlegelmilch: You will have seen that what one of the first things the EU's new Trade and Economic Security Commissioner – meaning minister of the EU – has done was go to the United States. And you will have seen that many other leaders from the European Union – i.e., heads of state – went to Washington to also pass along that message that we're open for business.

I think we are serious, from the EU side, to try to find something which would satisfy our American friends or the present American administration.

And you will have seen from the public statements that the first thing we always say is we're ready to look at your demands and negotiate. And there were actually things mentioned – e.g., cars was mentioned. On the passenger cars, we do have a higher tariff than the US and that has been a constant feature in some of the remarks of our American counterparts.

And there are other things that we can think about. Obviously, we have a strong interest to buy weapons. We already buy a lot of weapons from the US, and with the present situation, that will only increase.

Let me also add that last time the focus was on energy, where in any case we had to diversify and wean ourselves off of Russian supplies, which is now becoming even more important.

And the United States is now our biggest supplier already of LNG and there is a potential to do more. So there are actually real life interests here that we could look at and see what can be done. And that has been a constant approach from the EU side.

Chad Bown: One of the challenges, obviously, in the timing of what's happening here, with these tariff threats, is that simultaneously, you have major developments taking place in the Russia-Ukraine war. President Trump clearly wants to settle the war. He had a blow up in the Oval Office last week with Ukrainian President Zelenskyy. And the White House just announced it is at least temporarily suspending military aid to Ukraine. I think, as a policy matter, President

Trump wants to reduce US involvement in NATO and the US role in providing military security to Europe.

How do these other, non-trade issues – but nevertheless still issues between the United States and Europe that are incredibly important – how are they likely to affect Europe's trade response to any tariffs that the Trump administration might impose?

Rupert Schlegelmilch: I don't have the answer to that. I think the trade officials – and I'm a former trade official – we know that we are not acting in a vacuum. So, the bigger picture is always there. And it's true to say that we are at a very important and difficult point right now with the situation with the Russian aggression and the developments in the United States.

The European leaders – be it from the European Commission, be it from the member states – have been quite clear to say that a firm response would be needed – i.e., basically arguing a separation of the trade discussions from bigger political things, which was something which we were able to achieve in the last decades.

EUROPEAN UNION TRADE RELATIONS WITH THIRD COUNTRIES

Chad Bown: Now I want to turn to the European Union's relationship with third countries.

During President Trump's first term, there were a number of other countries out there who made a big show of being able to conclude free trade agreements in the absence of the United States – the message being something like, "hey, we can do trade liberalization without you." The EU itself closed an important deal with Japan, for example.

More recently, in December 2024, there was news that the European Commission had agreed to a deal with Mercosur. I think you covered not just trade relations with the United States, but everybody in the hemisphere, so the EU-Mercosur talks were one that you had a big role in.

What do you think? Should the United States be worried that there's going to be a proliferation of free trade agreements amongst everybody else this time around?

Rupert Schlegelmilch: I'm not sure whether they should be worried. And I just read that the Trump administration also gave up on APEP (Americas Partnership for Economic Prosperity), the Biden administration initiative with Latin America, if I'm correctly informed. So the Trump administration clearly doesn't want to do what we do.

But I think it is true that those countries who are interested in maintaining an open trading system based on rules, as well as predictable, stable relations might have more interest to work together. Let's put it as simple as that.

So, with the situation as it is now, there's a heightened or a better incentive to actually conclude deals built on trust with those partners that you do trust. And that means that also we from the EU are trying to finish the negotiations. And we have finished negotiations with New Zealand and the update to our agreement with Chile. I think there is a good chance that we will update the Mexico agreement because Mexico also has an interest having partners with a predictable policy environment.

And Mercosur is, of course, the biggest part. And I hasten to add that we're also restarting the discussions with India, which is, of course, also a hugely important partner. All of that, I think, in the present context, makes a lot of sense.

Chad Bown: There's another really important third country out there. That is of course, China.

Also during the Trump administration's first term, the EU, the United States and Japan were actually working together somewhat behind the scenes on something called "the trilateral." My understanding is you were a part of this, and the goal was to think hard about potential new rules to address some areas of common concern when it comes to China and, in particular, Chinese subsidies. Tell us more about that experience of working with the first Trump administration on that area of common concern.

Rupert Schlegelmilch: For much of the last years, there was no big disagreement about the analysis on what needs to be fixed in the rulebook in the WTO if you really want to address non-market economy practices as we have seen them develop over the last two decades.

The trilateral was one of the first attempts to look at the rulebook and say, "What would it be if we just sat together and found a way to deal with some of these practices?" And that was actually quite successful. And the idea was to spread this to like-minded countries and make an initiative and find a way to implement these things later on.

It didn't really go very far after this first trilateral ministerial meeting in early 2020. There was no follow up in the next couple of years.

Chad Bown: That was how the EU dealt with China with the first Trump administration. How did things change when the Biden administration arrived in early 2021? Was there any progress there between the EU and US on how to address, or at least how to think about, the China challenge in specific economic areas?

Rupert Schlegelmilch: We then had very long discussions in the context of the Trade and Technology Council (TTC) with the United States on the China challenge, with China being the predominant preoccupation of any US administration of the last 10-15 years.

And we were actually able to do a few things to coordinate and cooperate on China-related issues. Be it on medical devices where we jointly wrote to China on their practices on public procurement. Be it on trying to find ways to deal with some of the cyber threats and so on.

So what I think the difference is, is the response to these issues, because we didn't believe that putting tariffs on China were the answer. And don't forget the original justification for the US tariffs was a Section 301 intellectual property case (in 2018). We also have issues with that. But we tried to find other ways, and we have very active cooperation on intellectual property with China, which works or doesn't work – you can argue about that – but we wanted to stay within the rule book, which is quite complicated.

Chad Bown: What about Chinese steel and aluminum overcapacity? That was one that President Biden and European Commission President Ursula von der Leyen promised publicly back in 2021 that the US and EU would work on together. How did that work agenda go?

Rupert Schlegelmilch: The most promising enterprise in all of this, in my view – but maybe I'm biased because I was also involved in that – was the attempt to forge a coalition of the willing, starting with the EU and the US, on steel and aluminum, which was the most egregious case of overcapacity flooding world markets.

The OECD worked on it in a steel forum, and we were crafting rules, very detailed rules, again, on what kind of subsidies are allowed or not to keep your steel industry afloat, including what kind of steel you would like to favor for reasons of low carbon content. So there was a climate aspect.

Those negotiations went quite far in their level of detail. And I wouldn't say we were there to conclude, but we were close to concluding a deal. Also, because we would have to make some compromises on imposing in one way or the other higher tariffs on China.

While we differed sometimes on the means, I think we moved a lot closer on the analysis into what is wrong with Chinese behavior. We'll see how that goes. But it's clear that there will be further discussions on how best to deal with, in particular, overcapacity. Because what we have seen on steel and aluminum is only the beginning. There is enormous overcapacity in many sectors, something which we actually knew for a long time, but nobody really has a very convincing answer on how to deal with that because there are no rules on constraining many of China's practices.

Chad Bown: So, on that point, is it possible for policymakers and politicians to be working on both portfolios at the same time? If you're a European Commission trade official supposed to be dealing with the threats of tariffs coming in from the United States and how you have to respond to those and then at the same time working with the United States on a common challenge that is China, is it possible to segment and compartmentalize in a way that ultimately is going to allow you to make progress on that second issue in particular?

Rupert Schlegelmilch: I think it is on us to at least try to do that. I think we certainly were able to do this to some extent with the first Trump administration. Because doing nothing is not the default option. I mean the issue is there, and we are more effective if we deal with this together.

I can't really speak to the present administration. I have no idea whether they want to cooperate with anyone on China. I think we're going to find out. It's going to be complicated, that's clear.

Chad Bown: Media reports are that China is now reaching out to Europe, diplomatically, almost as if to say, "You're being bullied by your old friend, those Americans who seem to be going in a different direction. Why don't we be better friends? Put all those projects that you were working on with the Biden people, maybe the first Trump people, put that behind you, and let's do more together."

In light of all the US tariff threats, what do you think are the implications for Europe's relationship with China today?

Rupert Schlegelmilch: Well, maybe the first thing to say is that China is already experiencing the tariffs of 10 percent and now 20 percent. And that, of course, shows also that China has an interest to work with others to do something on this.

But I do think despite the charm offensive that actually did happen some months ago, and maybe is continuing, that we have to keep a cool head and look at our interests here. We have always maintained that we have to counter the unfair practices of China; but not everything China does is unfair, so we also have to cooperate in those areas where that is not at stake.

It's a big commercial partner; it will not go away. But we also have to be clear that there are limits, and the one thing which you can see in the European theater playing out is there are a lot more measures taken – i.e., anti-dumping, anti-subsidy, and the foreign subsidy regulation, we haven't mentioned that. So, I think we also intend to defend ourselves vis-a-vis the unfair practices of China.

Chad Bown: As my last question for you, it's one more about China. In your view, has the European perspective on China changed over the last few years?

Rupert Schlegelmilch: So, Chad, let me remind you that President von der Leyen, actually, at the World Economic Forum this year, talked about a "China shock" as a threat because of Chinese export subsidies. So I think the rhetoric has changed a little bit, also because we're a little bit clearer about some of the state-sponsored policies that we all are worried about.

We have certainly also taken a hard look at some of the things which happened in China, including that we were suffering from a coercion case on Lithuania. As I said, we have tried to separate out what is economically normal behavior, and where we do have to be careful.

I do think that we are a bit more critical about the effects of Chinese policies, and the way also they treat European companies in China, but without becoming paranoid. I think we really have to make a case, and this is why we took a long time to do a proper investigation on electric vehicles, for example.

On the one hand, we agree that there is an issue. But on the other hand, we did a proper investigation. We came up with a differentiated response. So we didn't slap a tariff on everyone. We really tried to keep to the rules vis-a-vis China where there are rules that we can use.

Chad Bown: Rupert, thank you very much.

Rupert Schlegelmilch: You're very welcome.

GOODBYE FOR NOW

Chad Bown: And that is all for *Trade Talks*.

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with Chad P. Bown

A huge thanks to Rupert Schlegelmilch, former trade official at the European Commission and now a visiting professor at the College of Europe.

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