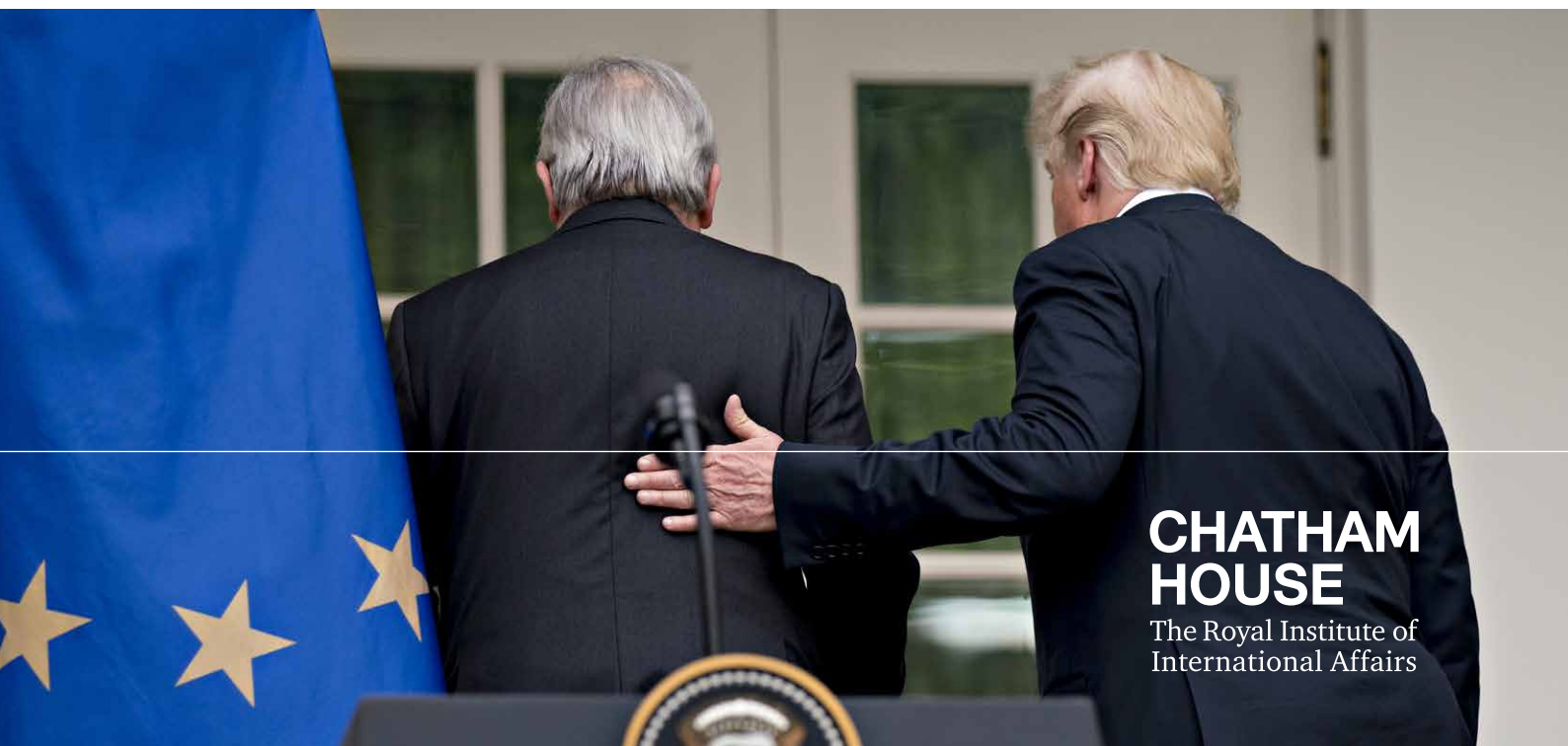


US–EU Trade Relations in the Trump Era Which Way Forward?



**CHATHAM
HOUSE**

The Royal Institute of
International Affairs

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Summary

- Although the US and the EU remain each other's largest trade and investment partners, there has latterly been some turbulence in transatlantic economic and political relations. A major source of friction have been the US tariffs on imports of steel and aluminium, introduced by the Trump administration in the name of national security, and the EU's retaliatory tariffs. President Trump's threat to impose tariffs of up to 25 per cent on imports of automobiles and automotive parts is on hold for now, but remains another source of tension. The EU and its member states also regard the Trump administration's attitudes and actions towards the rules-based international trading architecture – especially the WTO – as a great challenge.
- A key driver of President Trump's trade policy towards the EU and its member states – Germany in particular – is the large US trade deficit in goods. Trump and his team see the EU as both adversary and potential ally. Not only has the EU become a primary target of US trade action; it is also vulnerable to collateral damage in the US's trade war with China. All the same, the US recognizes the EU as a potential partner in tackling unfair trade practices – widely understood to implicate China – and to reform the global trading system.
- Tensions over trade have been somewhat reduced since July 2018, when President Trump and European Commission President Juncker stepped back from the brink of a trade war. Subsequent steps by both the US and the EU have opened the door for future trade talks. For now, however, the two sides' negotiating objectives diverge fundamentally in their potential scope – especially on whether to include agriculture and the automobile sector.
- While the US administration has an interest in agreeing a US–EU trade deal to showcase President Trump's deal-making abilities ahead of the US presidential election in 2020, the EU is interested in achieving a swift agreement primarily to forestall the potential imposition of automotive tariffs.
- Although new trade talks will not be a revival of the TTIP negotiations, many of the sticking points encountered during those negotiations are likely to resurface. Instead of a single-track undertaking, future US–EU trade talks might be more productively conducted via parallel tracks where each issue is addressed according to its own timetable.
- Critical to the success of future transatlantic trade negotiations will be whether the EU is able to speak with one voice when dealing with the US. Other recent US trade negotiations (in particular the new United States–Mexico–Canada Agreement – the successor to NAFTA) will also have an impact on US–EU talks. And beyond the pursuit of a bilateral free-trade agreement, the most significant issue for US–EU cooperation will be their capacity and willingness to work together, and with like-minded partners, to address global challenges of common concern.
- Building on a simulation exercise on US–EU trade talks in an era of protectionism, convened by Chatham House in September 2018, this paper concludes with a set of policy recommendations. A multifaceted approach aimed at both the transatlantic market and the global trading system could provide the best way forward in the current political and economic environment.

1. Introduction: Recent Episodes in Transatlantic Economic Relations

Since the election of President Trump in 2016 and the adoption of his ‘America First’ trade policy, the transatlantic trade relationship has been experiencing turbulent times. Although the trade and investment links between the US and the EU are deep and extensive, the imposition of US tariffs – and retaliatory tariffs by the EU – threatens to diminish economic prospects on both sides of the Atlantic, damages transatlantic political ties, and undermines the rules-based international trading system. But since July 2018 there have also been some positive signs that could mark an important turning point. If a new phase in the bilateral trade relationship can be launched, this could potentially lead to a deeper integration of the transatlantic marketplace, recement the US–EU relationship, and help address the shortcomings of the architecture and rules of global trading. As the US and the EU decide which way to move their trade relationship forward, the stakes are high for both sides, and indeed for the rest of the world.

The US and the EU remain each other’s largest trade and investment partners, notwithstanding the rise of China, and together represent the largest bilateral economic relationship in the world.¹ Trade in goods and services (exports plus imports) between the US and the EU surpassed \$1.1 trillion in 2017.² Investment ties are even more substantial, with US foreign direct investment (FDI) in the EU totalling \$3.2 trillion and outflows of FDI from the EU to the US standing at \$2.3 trillion in 2016.³ Total US investment in the EU is three times higher than in Asia.⁴ The US and EU economies together account for approximately half of global GDP, and for nearly a third of world trade flows.⁵

The US and the EU remain each other’s largest trade and investment partners, notwithstanding the rise of China, and together represent the largest bilateral economic relationship in the world.

Given the scale and level of integration of the transatlantic economy, there has been continued interest in formalizing the framework that underpins the US–EU economic relationship. The Transatlantic Economic Council was set up in 2007 in order to guide efforts to strengthen economic ties between the US and the EU. Negotiations for the Transatlantic Trade and Investment Partnership (TTIP) were formally launched in 2013. However, following 15 rounds of negotiations, the talks were suspended at the end of 2016. This was in part due to the change of administration in the US. However, TTIP was in trouble even before the election of Donald Trump, with negotiations having stalled over contentious issues such as agriculture, public procurement and investment protection. Growing public concern over TTIP –

¹ Ilias Akhtar, S. (2018), ‘U.S.-EU Trade and Investment Ties: Magnitude and Scope’, Congressional Research Service, <https://fas.org/sgp/crs/row/IF10930.pdf> (accessed 20 Nov. 2018).

² US Bureau of Economic Analysis (2018), ‘U.S. Trade in Goods and Services by Selected Countries and Areas, 1999-present’, <https://www.bea.gov/system/files/2018-12/trad-geo-time-series-1018.xlsx> (accessed 20 Nov. 2018).

³ Ilias Akhtar (2018), ‘U.S.-EU Trade and Investment Ties: Magnitude and Scope’.

⁴ European Commission (2018), ‘United States – Trade picture’, http://ec.europa.eu/trade/policy/countries-and-regions/countries/united-states/index_en.htm (accessed 20 Nov. 2018).

⁵ Ibid.

especially, on the European side, worries about investment protection provisions and fears of a potential lowering of health and environmental safety standards – also played a major part in the negotiations being put on hold.

Neither the US nor the EU has officially withdrawn from the TTIP negotiations. Whereas the EU Trade Commissioner considers the negotiations to be ‘in the freezer’,⁶ the Trump administration has declared that the talks remain under consideration.⁷ All the same, while the economic and strategic arguments for deepening the transatlantic trade and investment relationship remain strong, TTIP is unlikely to be revived in the current environment.⁸ Under the Trump administration, trade and economic relations between the US and the EU are experiencing friction.

A major area of transatlantic trade tension is steel and aluminium tariffs (imposed by the US on imports at rates of 25 per cent and 10 per cent respectively), which the Trump administration introduced in March 2018 under Section 232 of the Trade Expansion Act of 1962, citing US national security concerns. The EU received a temporary exemption, and tariffs came into force on 1 June 2018.

The EU regards the US steel and aluminium tariffs as unjustified and inconsistent with the rules of the World Trade Organization.

The EU regards the US steel and aluminium tariffs as unjustified and inconsistent with the rules of the World Trade Organization (WTO). In response to the US’s action, the EU has taken three measures: launching legal proceedings against the US at the WTO; applying retaliatory tariffs on US products (including on iconic and politically sensitive products such as Harley-Davidson motorcycles and bourbon whiskey, respectively produced in Wisconsin and Kentucky, the home states of former Speaker of the House of Representatives Paul Ryan and of Senate Majority Leader Mitch McConnell); and opening a safeguard investigation into potential damage stemming from additional imports coming into the EU as a result of the US market being closed off to a greater extent.⁹ The US is challenging the EU’s (and other countries’) retaliatory tariffs through a dispute settlement action at the WTO. Despite a trade détente reached between President Trump and the President of the European Commission, Jean-Claude Juncker, in July 2018, the US steel and aluminium tariffs and the EU’s retaliatory tariffs remained in force at the time of publication of this paper.

Another area of transatlantic trade friction is President Trump’s repeated threat to impose up to 25 per cent tariffs on imports of automobiles and automotive parts. In May 2018 the US Department of Commerce initiated a Section 232 investigation to determine whether automotive imports threaten to impair US national security.¹⁰ The department submitted its report to the White House

⁶ EURACTIV.com with Reuters and AFP (2016), ‘Malmström: EU-US trade deal ‘frozen’ after Trump vote’, 12 November 2016, <https://www.euractiv.com/section/trade-society/news/malmstrom-eu-us-trade-deal-frozen-after-trump-vote/> (accessed 20 Nov. 2018).

⁷ Office of the United States Trade Representative (2017), *2017 Trade Policy Agenda and 2016 Annual Report of the President of the United States on the Trade Agreements Program*, <https://ustr.gov/sites/default/files/files/reports/2017/AnnualReport/AnnualReport2017.pdf> (accessed 20 Nov. 2018).

⁸ Various studies have shown that TTIP would have helped to generate jobs and economic growth in the US and the EU – though the estimated gains were not huge. According to an independent study for the European Commission, GDP was projected to be approximately 0.5 per cent higher each year for the EU, and 0.4 per cent higher for the US, as a result of TTIP. The broader advantages of TTIP would have been the potential strategic benefits – such as cementing the transatlantic partnership and setting the rules and standards for trade in the 21st century. See Ecorys (2017), *SIA in support of the negotiations on a Transatlantic Trade and Investment Partnership (TTIP)*, Final Report prepared for the European Commission, <http://www.trade-sia.com/ttip/wp-content/uploads/sites/6/2017/03/TSIA-TTIP-Final-Report-03-17.pdf> (accessed 20 Nov. 2018).

⁹ European Commission (2018), ‘EU adopts rebalancing measures in reaction to US steel and aluminium tariffs’, 20 June 2018, http://europa.eu/rapid/press-release_IP-18-4220_en.htm (accessed 20 Nov. 2018).

¹⁰ US Department of Commerce (2018), ‘U.S. Department of Commerce Initiates Section 232 Investigation into Auto Imports’, 23 May 2018, <https://www.commerce.gov/news/press-releases/2018/05/us-department-commerce-initiates-section-232-investigation-auto-imports> (accessed 20 Nov. 2018).

in mid-February 2019, but did not publicly release the findings and recommendations. The president has 90 days to decide on a course of action. Notwithstanding the US–EU agreement to refrain from imposing new tariffs on each other as part of the July 2018 trade truce, the EU fears that the automotive tariffs by the US may yet be implemented.¹¹

In addition to these unilateral tariff measures by the US, the EU's leaders are worried about the Trump administration's attitudes and actions towards the rules-based international trading architecture, specifically the WTO. Even though the US government's blocking of appointments to the WTO's Appellate Body precedes the current administration, President Trump is willing to push US concerns much further. In particular, the US government believes that Appellate Body members should be obligated to end their activities when their mandate expires. The US has also raised concerns about the Appellate Body overstepping its authority through its 'expansive interpretations that effectively create new WTO law'.¹²

The Appellate Body impasse has now reached a critical juncture as a result of the US's continued blocking of appointments: as of 30 September 2018, the number of judges on the roster of the Appellate Body (each of whom serves a four-year term, renewable once) has been reduced from the usual seven to three – the minimum required for the system to function. The caseload has thus become very difficult to manage, and the WTO dispute settlement process is grinding to a halt. Once the roster of the WTO Appellate Body falls to two members, as is due to happen in December 2019, it can no longer formally operate. Developments such as this risk in effect hollowing out the WTO. Meanwhile, the current US administration is also endangering the global trading system in more direct ways: President Trump has repeatedly threatened to pull the US out of the WTO. Although the incumbent US Trade Representative (USTR) Robert Lighthizer still sees value in the institution, he is seeking a course correction and has stated that the US would not comply with adverse WTO rulings.

Another source of friction has been President Trump's decision to withdraw the US from the Joint Comprehensive Plan of Action (JCPOA – the Iran nuclear deal agreed in July 2015 between Iran, the EU and the five permanent members of the UN Security Council) and the extraterritorial effect of US economic sanctions against Iran. EU leaders have been trying to shield European businesses operating in Iran from the US measures without causing a major rift in the fraught transatlantic relationship. More broadly, many EU governments view the US's shift away from international economic cooperation with concern. Their worries are fuelled, for example, by President Trump's withdrawal of support from the joint communiqué released at the end of the G7 summit in June 2018.¹³

Transatlantic tensions over trade were to some degree de-escalated in late July 2018, as President Trump and European Commission President Juncker stepped back from the brink of a trade war and announced, in a joint statement, their intention to 'launch a new phase in the relationship between the United States and the European Union'.¹⁴ The two leaders announced lofty ambitions 'to work

¹¹ Shalal, A. and Dalgleish, J. (2018), 'German industry warns U.S. auto tariffs not completely off table yet', Reuters, 25 July 2018, <https://www.reuters.com/article/us-usa-trade-eu-industry/german-industry-warns-u-s-auto-tariffs-not-completely-off-table-yet-idUSKBN1KF30E> (accessed 20 Nov. 2018).

¹² US Mission to International Organizations in Geneva (2018), 'Ambassador Dennis Shea's Statement at the WTO General Council', 8 May 2018, <https://geneva.usmission.gov/2018/05/08/ambassador-dennis-sheas-statement-at-the-wto-general-council/> (accessed 20 Nov. 2018).

¹³ Differences between the US and the other G7 members over the former's tariffs on steel and aluminium seemed to have been concealed by the language of the joint communiqué, which called for a 'rules-based trading system'. During a post-summit news conference, the Canadian host, Prime Minister Justin Trudeau, vowed to move forward with retaliatory tariffs. In response, President Trump, who was already en route to his next scheduled meeting in Singapore, announced via Twitter that he had instructed US officials not to endorse the communiqué, and that the US was considering imposing tariffs on automobiles.

¹⁴ European Commission (2018), 'Joint U.S.-EU Statement following President Juncker's visit to the White House', 25 July 2018, http://europa.eu/rapid/press-release_STATEMENT-18-4687_en.htm (accessed 20 Nov. 2018).

together toward zero tariffs, zero non-tariff barriers, and zero subsidies on non-auto industrial goods’, as well as to reduce barriers and increase trade in specific sectors (including services, chemicals, pharmaceuticals, medical products and soybeans). As already noted, the two sides agreed ‘to resolve the steel and aluminum tariff issues and retaliatory tariffs’, and to refrain from imposing further tariffs (particularly on automobiles and automotive parts) while negotiations are in progress. Trump and Juncker also announced their intention to strengthen bilateral cooperation with respect to energy, to launch a dialogue on standards, and to ‘work closely together with like-minded partners to reform the WTO and to address unfair trading practices’ such as intellectual property theft and forced technology transfer.¹⁵ To move this joint agenda forward, the leaders set up an Executive Working Group – led by USTR Lighthizer and European Commissioner for Trade Cecilia Malmström.

The Executive Working Group has met subsequently to explore how to best implement the joint statement. The European Commission has been following up on different elements of the joint statement by reporting on increases in imports of US soybeans¹⁶ and imports of US liquefied natural gas.¹⁷ Moreover, the EU member states have authorized the Commission to open negotiations with the US regarding imports of hormone-free beef into the EU – the size of the quota for which has been a persistent source of conflict between the two sides.¹⁸

The question now is whether the recent trade rapprochement between the US and the EU can be turned into a genuine and lasting deal, or whether it is only a temporary truce in the transatlantic trade dispute.

In October 2018 USTR Lighthizer notified Congress that the Trump administration intended to negotiate a trade agreement with the EU.¹⁹ Then, in January 2019, the administration released its negotiating objectives for trade talks with the EU.²⁰ These steps are in line with Trade Promotion Authority (TPA) legislative requirements.²¹

For its part, the European Commission has presented to the Council of the EU draft negotiating mandates for trade talks with the US, which will have to be approved by the member states before negotiations can begin.²² The Council is expected to adopt a decision authorizing the Commission to open negotiations with the US in the coming weeks. Meanwhile, in mid-February 2019 the European Parliament’s International Trade Committee voted in favour of a resolution calling for US–EU trade talks to commence if certain

¹⁵ Ibid.

¹⁶ The EU has put in place a reporting mechanism whereby it publishes the changes of EU imports of US soybeans every two months. For the first report, see European Commission (2018), ‘Follow-up to the EU-U.S. Joint Statement of 25 July: Imports of U.S. soybeans increase by over 280%’, 1 August 2018, http://europa.eu/rapid/press-release_IP-18-4768_en.htm (accessed 20 Nov. 2018).

¹⁷ European Commission (2018), ‘EU-U.S. Joint Statement of 25 July: European Union imports of U.S. Liquefied Natural Gas (LNG) are on the rise’, 9 August 2018, http://europa.eu/rapid/press-release_IP-18-4920_en.htm (accessed 20 Nov. 2018).

¹⁸ European Commission (2018), ‘European Commission welcomes Member States’ support to settle WTO dispute with the United States’, 19 October 2018, http://europa.eu/rapid/press-release_IP-18-6103_en.htm (accessed 20 Nov. 2018).

¹⁹ Office of the United States Trade Representative (2018), ‘Trump Administration Announces Intent to Negotiate Trade Agreements with Japan, the European Union and the United Kingdom’, 16 October 2018, <https://ustr.gov/about-us/policy-offices/press-office/press-releases/2018/october/trump-administration-announces> (accessed 20 Nov. 2018).

²⁰ Office of the United States Trade Representative (2019), ‘United States–European Union Negotiations: Summary of Specific Negotiating Objectives’, 11 January 2019, https://ustr.gov/sites/default/files/01.11.2019_Summary_of_U.S.-EU_Negotiating_Objectives.pdf (accessed 17 Jan. 2019).

²¹ According to TPA laws, the USTR must notify Congress 90 days prior to initiating negotiations and release detailed negotiating objectives 30 days prior to the start of trade negotiations.

²² European Commission (2019), ‘EU-U.S. Trade Talks: European Commission presents draft negotiating mandates’, 18 January 2019, http://europa.eu/rapid/press-release_IP-19-502_en.htm (accessed 18 Jan. 2019).

conditions are met.²³ The parliament is expected to adopt its position on the Commission's mandates in March; and though non-binding, its stance carries weight given the parliament's role in approving any final transatlantic trade agreements.

The question now is whether the recent trade rapprochement can be turned into a genuine and lasting deal, or whether it is only a temporary truce in the transatlantic trade dispute.

This paper focuses on the bilateral US–EU trade relationship. The greatest challenge presented by the Trump administration is to the multilateral, rules-based international trading system, but a new phase of closer collaboration and stronger trade relations between the US and the EU could help to address constructively some of the shortcomings of the current architecture and rules of the global trading system.

²³ European Parliament (2019), 'Trade negotiations with US can start under certain conditions', 19 February 2019, <http://www.europarl.europa.eu/news/en/press-room/20190219IPR27357/trade-negotiations-with-us-can-start-under-certain-conditions> (accessed 19 Feb. 2019).

2. Drivers of Trump's Trade Policy Towards Europe

Less than a fortnight before agreeing the trade truce with Juncker, Trump had called the EU a 'foe' of the US for 'what they do to us in trade'.²⁴ He has since also claimed that the EU 'was formed in order to take advantage of us on trade'.²⁵ While these statements are both incendiary and factually incorrect, some concrete concerns raised by the Trump administration have a kernel of truth.

Trade balance and perceived unfair trade practices

President Trump has prioritized reducing the US trade deficit and tackling unfair trade practices. He blames the EU for the US's trade deficit with the bloc and with certain of its member states.

The US's overall trade deficit with the EU has widened since 2009. In 2017 it stood at \$101.2 billion – with the trade deficit in goods (\$152.6 billion) partially offset by the trade surplus in services (\$51.4 billion).²⁶ The trade deficit with the EU as a bloc is the US's second largest after China (\$335.7 billion in 2017). A key driver is the US's trade deficit in goods with Germany, which reached \$64.1 billion in 2017; the overall deficit with that country being \$66.7 billion, or nearly two-thirds of the EU total.²⁷

President Trump is highly critical of Germany over trade, and has repeatedly taken to Twitter to denounce the country's trade surplus. Other EU member states – notably Italy and France – with which the US runs overall trade deficits have so far largely remained off Trump's radar.

President Trump is highly critical of Germany over trade, and has repeatedly taken to Twitter to denounce the country's trade surplus.²⁸ Other EU member states – notably Italy and France – with which the US runs overall trade deficits (see Figure 1) have so far largely remained off Trump's radar. When bemoaning the trade deficit, Trump is usually focused solely on merchandise trade. He ignores the overall US trade surplus in services. However, in the case of Germany (and also Italy), the US runs a trade deficit in both goods and services.

²⁴ CBS News (2018), 'I think the European Union is a foe,' Trump says ahead of Putin meeting in Helsinki', 15 July 2018, <https://www.cbsnews.com/news/donald-trump-interview-cbs-news-european-union-is-a-foe-ahead-of-putin-meeting-in-helsinki-jeff-glor/> (accessed 20 Nov. 2018).

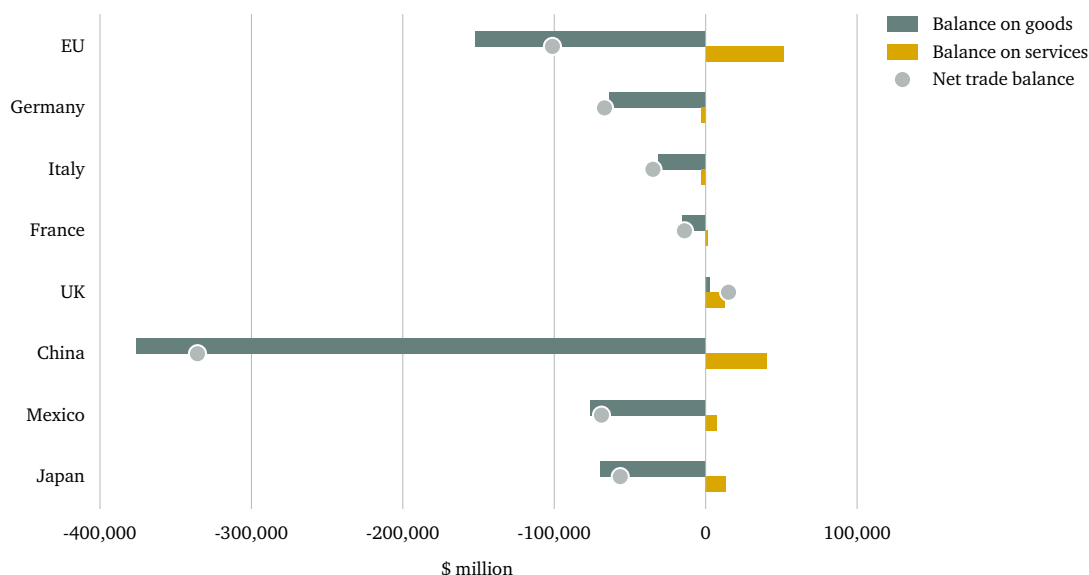
²⁵ CBS News (2018), 'President Trump on Christine Blasey Ford, his relationships with Vladimir Putin and Kim Jong Un and more', 15 October 2018, <https://www.cbsnews.com/news/donald-trump-full-interview-60-minutes-transcript-lesley-stahl-2018-10-14/> (accessed 20 Nov. 2018).

²⁶ US Bureau of Economic Analysis (2018), 'U.S. Trade in Goods and Services by Selected Countries and Areas, 1999-present'.

²⁷ Ibid.

²⁸ See for example Trump, D. (@realDonaldTrump) (2017), 'We have a MASSIVE trade deficit with Germany, plus they pay FAR LESS than they should on NATO & military. Very bad for U.S. This will change', tweet, 30 May 2017, <https://twitter.com/realdonaldtrump/status/869503804307275776?lang=en> (accessed 20 Nov. 2018).

Figure 1: US international trade balance with selected partners (2017)



Source: US Bureau of Economic Analysis (2018), 'Table 6. U.S. International Trade by Selected Countries and Areas – Balance on Goods', 'Table 9. U.S. International Trade by Selected Countries and Areas – Balance on Services', https://www.bea.gov/system/files/2018-09/trad_geo_time_series_0718.xlsx (accessed 20 Nov. 2018).

Most economists agree that while global trade imbalances matter, Trump's focus on the bilateral trade deficit is misplaced. The US trade deficit is not driven by a specific country's (or bloc's) trade policy, but by macroeconomic forces related to national savings and investment. Thus, attempting to alter the trade deficit through bilateral efforts without addressing the underlying macroeconomic issues is unlikely to lead to the desired outcome.

It is important to note here that there are valid concerns regarding Germany's global trade surplus, which stood at 7.6 per cent of the country's GDP in 2017.²⁹ This issue has been raised for years by the IMF and many G20 countries, as well as within the EU itself. For instance, the chief economist at the IMF warned in August 2018 that Germany's reluctance to reduce its structural trade surplus was contributing to trade tensions.³⁰ In other words, despite many flaws – and lack of rhetorical nuance – in Trump's trade logic, the administration is right to single out Germany for criticism. To alleviate global concerns, but also to support its own long-term outlook, Germany needs to further boost domestic demand and investment, for example by increasing spending on public infrastructure, education, and research and development. This would not only help to reduce global economic imbalances, but also boost the country's economic growth and competitiveness in the long term.³¹

²⁹ World Bank (2018), 'External balance on goods and services (% of GDP)', <https://data.worldbank.org/indicator/NE.RSB.GNFS.ZS?view=chart> (accessed 20 Nov. 2018).

³⁰ Deutsche Welle (2018), 'IMF blames German trade surplus for trade tensions', 6 August 2018, <https://www.dw.com/en/imf-blames-german-trade-surplus-for-trade-tensions/a-44964156> (accessed 20 Nov. 2018).

³¹ Schneider-Petsinger, M. (2017), 'Policy Recommendations for Strengthening Transatlantic Trade in Challenging Times', in Dreher, V., Kantel, A. J., Kirchner, M., Langenbacher, E., Rizzo, R. and Schneider-Petsinger, M. (2017), *The Specter of Uncertainty: Policies for Strengthening the Transatlantic Relationship from the Next Generation of Leaders*, Washington, DC: American Institute for Contemporary German Studies, <http://www.aicgs.org/site/wp-content/uploads/2017/06/PR65-ERP-Next-Gen-FY17-1.pdf> (accessed 20 Nov. 2018).

A related source of tension between the US and Germany is the Trump administration's claim that Germany 'exploit[s]' a 'grossly undervalued' euro to gain an unfair trade advantage.³² Since 2016, the Department of the Treasury has included Germany on its Monitoring List of trading partners.³³ The Trump administration recognizes that 'Germany does not exercise its own monetary policy',³⁴ and that the independent European Central Bank (ECB) conducts monetary policy for the eurozone. The overall weakness in the euro *vis-à-vis* the dollar has in part been driven by the divergence between monetary policy in the US and that in the eurozone, with the US Federal Reserve raising interest rates gradually since 2015 while the ECB has kept rates low. It is right to state that German exporters have benefited from an undervalued euro in their country, which the IMF estimated in July 2018 to be 10–20 per cent weaker than it should be.³⁵ However, this is not the result of a deliberate currency manipulation; rather, it is due to mechanisms such as tight controls on the labour market, which have prevented real wages from keeping pace with productivity, that amount to an internal devaluation and help Germany's international competitiveness. Thus, the US – and others, including the IMF – are essentially correct when they argue that if Germany took steps to let wages move in line with improvements in productivity, and also increased its domestic demand, higher wages and prices would appreciate Germany's real effective exchange rate.

The current US administration seems to be unwilling to acknowledge that EU automotive companies operate factories in the US – with Mercedes, BMW and Volkswagen together directly employing more than 20,000 US workers.

Trump has complained about German cars on the streets of New York City since the 1990s. He regards the transatlantic trade in automobiles and automotive parts as unbalanced. As president, he has repeatedly criticized disparate tariff levels: the EU imposes tariffs of 10 per cent on US- and other foreign-built cars, while the US levies a 2.5 per cent tariff on cars built in Europe. However, he ignores the fact that the US has higher trade barriers for trucks: the EU tariff is 22 per cent, as against the US tariff of 25 per cent.³⁶

It is unclear what the Trump administration's ultimate goal actually is when it comes to automotive tariffs. In August 2018 the president rebuffed an offer by the EU to eliminate tariffs on cars, deeming this 'not good enough', because European 'consumer habits are to buy their cars, not to buy our cars'.³⁷ Moreover, the current administration seems to be unwilling to acknowledge that EU automotive companies operate factories in the US – with Mercedes, BMW and Volkswagen together directly employing more than 20,000 US workers.³⁸ If the Trump administration was to go ahead with additional tariffs on imported automobiles and automotive parts under Section 232 of the Trade Expansion Act

³² Donnan, S. (2017), 'Trump's top trade adviser accuses Germany of currency exploitation', *Financial Times*, 31 January 2017, <https://www.ft.com/content/57f104d2-e742-11e6-893c-082c54a7f539> (accessed 20 Nov. 2018).

³³ As of October 2018, the six countries on the US Treasury Department's Monitoring List of major trading partners meriting close attention to their currency practices and macroeconomic policies were: China, Germany, India, Japan, the Republic of Korea and Switzerland. US Department of the Treasury, Office of International Affairs (2018), *Report to Congress: Macroeconomic and Foreign Exchange Policies of Major Trading Partners of the United States*, 17 October 2018, Washington, DC: US Department of the Treasury, <https://home.treasury.gov/system/files/206/2018-10-17-%28Fall-2018-FX%20Report%29.pdf> (accessed 20 Nov. 2018).

³⁴ *Ibid.*

³⁵ International Monetary Fund (2018), *External Sector Report: Tackling Global Imbalances amid Rising Trade Tensions*, Washington, DC: International Monetary Fund, p. 60, <https://www.imf.org/~media/Files/Publications/ESR/2018/text.ashx?la=en> (accessed 20 Nov. 2018).

³⁶ Ilias Akhtar, S. (2018), 'U.S.-EU Trade and Economic Issues', Congressional Research Service, <https://fas.org/sgp/crs/row/IF10931.pdf> (accessed 20 Nov. 2018).

³⁷ Bloomberg News (2018), 'Here Are All the Highlights From Trump's Oval Office Interview', 31 August 2018, <https://www.bloomberg.com/news/articles/2018-08-31/here-s-everything-donald-trump-said-in-his-oval-office-interview?srnd=premium-europe> (accessed 20 Nov. 2018).

³⁸ Isidore, C. (2018), 'Tariffs on European cars would hurt US auto jobs', CNN, 22 June 2018, <https://money.cnn.com/2018/06/22/news/companies/trump-european-car-tariffs/index.html> (accessed 20 Nov. 2018).

of 1962, there is the risk that European companies might reduce investment and cut their workforce in the US.³⁹ It remains to be seen what the Department of Commerce has found in its investigation, and what course of action it recommends. But most commentators – including leading Republicans in Congress, such as the recently retired chairman of the Senate Committee on Foreign Relations, Senator Bob Corker – do not regard the national security provisions as a valid justification for the introduction of automotive tariffs.⁴⁰

The jury is still out on the question of whether the imposition and threat of tariffs is a means to an end or the end *per se*. Larry Kudlow – the current director of the National Economic Council and a former television host with critical views of tariffs generally – has argued that President Trump has a vision of ‘free and open trade’.⁴¹ Wilbur Ross, the Secretary of Commerce, has similarly made the case that the president’s objective is to ‘reduce tariffs, reduce trade barriers and make an open level playing field for U.S. companies all around the world’.⁴² Trump has, notably, credited the successful renegotiation of the North American Free Trade Agreement (NAFTA) to the US’s imposition of steel and aluminium tariffs, as well as to its threat of introducing automotive tariffs.⁴³ This suggests that the Trump administration is using tariffs as a negotiating tactic to press other countries into making concessions. However, the Trump administration’s refusal to revoke the steel and aluminium tariffs on Mexico and Canada immediately after signing the new United States–Mexico–Canada Agreement (USMCA)⁴⁴ in November 2018, as well as Trump’s self-designation as ‘Tariff Man’ in a tweet lauding the positive impact of tariff revenues for the US, shortly after reaching a 90-day tariff truce with China,⁴⁵ suggests that the current US administration is prepared to impose and maintain tariffs for some time yet.

Competing views within the Trump administration

The Trump administration’s practice of going back and forth in its trade talks – asking the EU to eliminate its automotive tariffs and then snubbing its offer to do so, or officially putting new tariffs on hold but continuing to hint at their possible imposition, to some extent reflects the fact that President Trump likes to keep the opposition around the negotiating table ‘off balance’. But it also reflects the reality that there are various factions within the administration that have different views on trade.

There are broadly two camps within President Trump’s trade team. The first includes National Economic Council Director Larry Kudlow and Secretary of the Treasury Steven Mnuchin as the voices in the current administration that are, relatively speaking, the most in favour of free trade – although both have backtracked on their previous commitment to free trade and internationalist principles since joining Trump’s team. The other camp comprises President Trump’s trade adviser Peter Navarro and USTR

³⁹ Bryan, V. and Oziel, C. (2018), ‘BMW says U.S. tariffs on EU cars may hit investment there’, Reuters, 30 June 2018, <https://uk.reuters.com/article/us-usa-trade-autos-bmw/bmw-says-u-s-tariffs-on-eu-cars-may-hit-investment-there-idUKKBN1JQ0EZ> (accessed 20 Nov. 2018).

⁴⁰ Levy, P. (2018), ‘Et Tu, Autos? The Case For National Security Tariffs Is Weak’, Forbes, 24 May 2018, <https://www.forbes.com/sites/phillevy/2018/05/24/et-tu-autos-more-national-security-tariffs/#ee926959b4ed> (accessed 20 Nov. 2018).

⁴¹ Fox News (2018), ‘Trump wants ‘free and open trade’, but tariffs have an end goal: Kudlow’, 29 June 2018, <https://www.foxbusiness.com/politics/trump-wants-free-and-open-trade-but-tariffs-have-an-end-goal-kudlow> (accessed 20 Nov. 2018).

⁴² Kim, T. (2018), ‘Commerce Secretary Ross: “The ultimate objective of the president is to reduce tariffs”’, CNBC, 21 June 2018, <https://www.cnbc.com/2018/06/21/commerce-secretary-ross-the-ultimate-objective-of-the-president-is-to-reduce-tariffs.html> (accessed 20 Nov. 2018).

⁴³ Bryan, B. (2018), ‘Trump lashes out at ‘babies’ complaining about tariffs, which he says led to the massive new trade deal with Canada and Mexico’, Business Insider, 1 October 2018, <http://uk.businessinsider.com/trump-babies-tariffs-complaints-touts-us-mexico-canada-usmca-trade-deal-2018-10?r=US&IR=T> (accessed 20 Nov. 2018).

⁴⁴ The new agreement remains subject to ratification by all three countries before it can take effect.

⁴⁵ Trump, D. (@realDonaldTrump) (2018), ‘....I am a Tariff Man. When people or countries come in to raid the great wealth of our Nation, I want them to pay for the privilege of doing so. It will always be the best way to max out our economic power. We are right now taking in \$billions in Tariffs. MAKE AMERICA RICH AGAIN’, tweet, 4 December 2018, <https://twitter.com/realDonaldTrump/status/1069970500535902208> (accessed 17 Jan. 2019).

Robert Lighthizer, whose stance on trade is more protectionist and hawkish. Navarro (who serves as the Assistant to the President and Director of the Office of Trade and Manufacturing Policy) is concerned with the US industrial base, and favours a decoupling of the US and Chinese economies. Lighthizer – a long-standing critic of China's trade practices – might be prepared to strike a deal with Beijing if it addresses some of the issues at stake. Meanwhile, Commerce Secretary Wilbur Ross oscillates between these two camps, but often sides with the latter group. He is best described as a more old-fashioned protectionist, under whose leadership the Department of Commerce has made more aggressive use of traditional – but also rarely used – trade remedies (such as self-initiating the first anti-dumping and countervailing probes in decades, or initiating the Section 232 national security investigations).

Although leaders in other countries know that ultimately it is President Trump who calls the shots on trade, it is important for them to know who within the administration has the president's ear. For the Europeans, the main interlocutor is USTR Lighthizer, who is the US lead on the US–EU Executive Working Group. Lighthizer's primary target has been China's practices regarding forced technology transfer, intellectual property theft, and perceived efforts to dominate future technology sectors. European officials thus believe that Lighthizer is more amenable to collaborating and forming a united US–EU front against China.⁴⁶

Another major point of contact for European officials is Wilbur Ross. As Commerce Secretary, his primary goal is more narrowly focused on the US trade deficit and on trying to increase US exports to the EU. Because of the Department of Commerce's determination that steel and aluminium tariffs are a threat to US national security – which ultimately led to the imposition of tariffs affecting the EU and other allies – the relationship between Ross and EU officials seems more fraught. This was evident in a tense meeting between Ross and European Commissioner for Trade Cecilia Malmström, in October 2018, during which Ross emphasized that President Trump's 'patience was not unlimited' and his EU counterpart accused Washington of deliberately delaying the negotiation process.⁴⁷

The US preference for bilateral deals and a transactional approach

President Trump has repeatedly emphasized that he favours bilateral deals over mega-regional or multilateral agreements. Because the European Commission has exclusive competence over the EU's trade policy, a deal between the US and the EU would technically fit with this preference. However, Peter Navarro has previously criticized TTIP as being a 'multilateral deal in bilateral dress'.⁴⁸ Since then, Trump has reportedly offered France a bilateral trade deal with better terms than those available to the EU as a whole – on condition that the country pulls out of the bloc.⁴⁹ So far, the EU and its member states have been unanimous in emphasizing that any negotiations must take place at the EU level and not with individual countries.

The Trump administration has also adopted an approach that is much more transactional in nature than those of its predecessors. Notably, it has conflated trade and defence issues, linking concerns over the US's trade deficit with the EU to frustration over some EU member states' failure, thus far, to meet

⁴⁶ Bradsher, K. (2018), 'Within Trump's Trade Factions, Nations Look for a Friendly Face', *New York Times*, 2 June 2018, <https://www.nytimes.com/2018/06/02/business/trump-trade-china-europe-whiplash.html> (accessed 20 Nov. 2018).

⁴⁷ Brunsden, J. (2018), 'Negotiators warn Trump-Juncker trade agreement at risk', *Financial Times*, 17 October 2018, <https://www.ft.com/content/3bb7dad2-d225-11e8-a9f2-7574db66bcd5> (accessed 20 Nov. 2018).

⁴⁸ Donnan (2017), 'Trump's top trade adviser accuses Germany of currency exploitation'.

⁴⁹ Rogin, J. (2018), 'Trump is trying to destabilize the European Union', *Washington Post*, 28 June 2018, https://www.washingtonpost.com/opinions/global-opinions/trump-is-trying-to-destabilize-the-european-union/2018/06/28/729cb066-7b10-11e8-aeec-4d04c8ac6158_story.html?utm_term=.8b1bbfcb8e60 (accessed 20 Nov. 2018).

the NATO pledge (agreed at the alliance’s 2014 summit in Newport, Wales) of increasing defence spending to 2 per cent of GDP by 2024.⁵⁰ While this approach has alienated the US’s allies, the EU has been able to react with remarkable unity.⁵¹

The EU as a primary target – and the risks of collateral damage

Given the US government’s concerns over both the country’s trade deficit with the EU and what it has framed as Germany’s manipulation of the euro to its own advantage, the EU and its member states are a primary target of the Trump administration’s trade rhetoric and actions. At the same time, the EU has since early 2018 been caught in the crossfire of the trade war between the US and China, and may suffer collateral damage.

Compared with the impact of the steel and aluminium tariffs on the European economy, new unilateral US tariffs on automobiles and automotive part imports from the EU would have much more severe economic effects. The US measures on steel and aluminium affect EU exports worth €6.4 billion, but the EU’s exports of cars and automotive parts to the US are worth more than €50 billion annually.⁵² Germany – given the importance of its car manufacturing sector and its exposure to the US market – would be especially badly hit by automotive tariffs. However, the complexity of supply chains means that the impact of US tariffs would be felt in Europe more broadly. A recent report by five renowned German economic institutes, commissioned by the German government, found that an escalation of the trade conflict would be likely to trigger a severe recession in Germany and more widely in Europe.⁵³

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Even if the transatlantic tariff dispute does not intensify, a further deepening of the US–China trade war would have adverse consequences for EU economies. The US currently imposes tariffs on imports of Chinese steel and aluminium in the name of national security. It has also imposed tariffs on \$250 billion worth of Chinese products, based on Section 301 of the Trade Act of 1974.⁵⁴ China has raised retaliatory tariffs on \$110 billion worth of US products. Despite the 90-day ‘ceasefire’ agreed between President Trump and President Xi in early December 2018, and Trump’s subsequent decision, in late

⁵⁰ Trump, D. (@realDonaldTrump) (2018), ‘The European Union makes it impossible for our farmers and workers and companies to do business in Europe (U.S. has a \$151 Billion trade deficit), and then they want us to happily defend them through NATO, and nicely pay for it. Just doesn’t work!’, tweet, 10 July 2018, <https://twitter.com/realdonaldtrump/status/1016757033071079424?lang=en> (accessed 20 Nov. 2018).

⁵¹ Dempsey, J. (2018), ‘Trump may be doing the European Union and NATO a big favor’, *Washington Post*, 6 July 2018, https://www.washingtonpost.com/news/global-opinions/wp/2018/07/06/trump-may-be-doing-the-european-union-and-nato-a-big-favor/?utm_term=.d5bd317b9c05 (accessed 20 Nov. 2018).

⁵² European Commission (2018), ‘Transatlantic Trade in Turbulent Times – Speech by Cecilia Malmström, European Commissioner for Trade’, 19 July 2018, http://europa.eu/rapid/press-release_SPEECH-18-4604_en.htm (accessed 20 Nov. 2018).

⁵³ Deutsches Institut für Wirtschaftsforschung, ifo Institut, Institut für Weltwirtschaft an der Universität Kiel, Leibniz-Institut für Wirtschaftsforschung Halle, RWI – Leibniz-Institut für Wirtschaftsforschung Essen (2018), *ifo Schnelldienst 19/2018*, Gemeinschaftsdiagnose Herbst 2018: Aufschwung verliert an Fahrt – Weltwirtschaftliches Klima wird rauer, <http://www.cesifo-group.de/DocDL/sd-2018-19-10-11.pdf> (accessed 20 Nov. 2018). See also Riedel, D., Specht, F. and Gray, J. (2018), ‘German economic institutes warn of recession if trade dispute worsens’, *Handelsblatt*, 26 September 2018, <https://global.handelsblatt.com/finance/german-economic-institutes-warn-recession-trade-dispute-worsens-967184> (accessed 20 Nov. 2018).

⁵⁴ Section 301 of the U.S. Trade Act of 1974 authorizes the President to take action to enforce US rights under trade agreements or to address unjustifiable foreign barriers that burden or restrict US commerce. See Morrison, W. (2018), ‘Enforcing U.S. Trade Laws: Section 301 and China’, Congressional Research Service, <https://fas.org/sgp/crs/row/IF10708.pdf> (accessed 20 Nov. 2018).

February 2019, to defer a tariff increase,⁵⁵ a further escalation of the trade dispute cannot be ruled out, as both sides will find it difficult to address long-standing issues around China's trade practices. Thus, the Trump administration may yet carry out its threat to impose tariffs on a further \$267 billion worth of Chinese imports. The indirect effects of this tit-for-tat US–China trade war on the EU and its member states could be significant. It would disrupt global supply chains and, in all probability, would lead to a slowdown in global trade and economic growth.⁵⁶

It should also be borne in mind that while the current US steel and aluminium tariffs are aimed at China, they miss the mark because they do little to address the real issue of China's excess steel capacity. China is not among the leading 10 supplier countries for US imports of steel. Rather, US steel imports come primarily from Canada, Brazil and South Korea.⁵⁷ However, these three countries received initial exemptions from the tariffs, with the latter two having secured a permanent exemption by agreeing to a quota.

On the matter of trade, the Trump administration sees the EU as both adversary and potential ally. The EU has become a primary target of US trade action, and is also vulnerable to collateral damage in the US's trade war with China. At the same time, the US recognizes the EU as a potential partner against China's trade practices, and in pressing for reform of the global trading system.

The US and the EU share concerns regarding China's overcapacity in the steel sector, market-distorting subsidies to industry, the role of state-owned enterprises, policies on forced technology transfer and theft of intellectual property. While initially it seemed as though Trump's trade wars, on multiple fronts, were pushing the EU and China closer together and strengthening their economic ties, more recently the US and the EU have signalled their intention 'to join forces to protect American and European companies better from unfair global trade practices'.⁵⁸

Moreover, the US and the EU, along with Japan, have intensified their discussions on tackling shared concerns about China's trade practices, as well as on reforming the WTO, and have issued a number of joint statements since 2017.⁵⁹ While neither the 2018 Trump–Juncker agreement nor the joint US–EU–Japan statements make direct reference to China, these efforts suggest that the US and the EU may be willing to overcome their trade dispute and work together to stand up to China's trade practices.

To sum up, on the matter of trade, the Trump administration sees the EU as both adversary and potential ally. The EU has become a primary target of US trade action, and is also vulnerable to collateral damage in the US's trade war with China. At the same time, the US recognizes the EU as a potential partner against China's trade practices, and in pressing for reform of the global trading system.

⁵⁵ Mason, J. and Lawder, D. (2019), 'Trump delays tariff hike on Chinese goods, citing trade talk progress', 24 February 2019, <https://uk.reuters.com/article/us-usa-trade-china/trump-raises-hopes-of-trade-deal-on-final-day-of-u-s-china-talks-idUKKCN1QD0L0> (accessed 27 Feb. 2019).

⁵⁶ Lawder, D. (2018), 'IMF's Lagarde warns trade conflicts dimming global growth outlook', Reuters, 1 October 2018, <https://uk.reuters.com/article/uk-imf-g20-lagarde/imfs-lagarde-warns-trade-conflicts-dimming-global-growth-outlook-idUKKCN1MB32N> (accessed 20 Nov. 2018).

⁵⁷ US Department of Commerce, Bureau of Industry and Security (2018), *The Effect of Imports of Steel on the National Security*, Washington, DC: US Department of Commerce, https://www.commerce.gov/sites/default/files/the_effect_of_imports_of_steel_on_the_national_security_-_with_redactions_-_20180111.pdf (accessed 20 Nov. 2018).

⁵⁸ European Commission (2018), 'Joint U.S.-EU Statement following President Juncker's visit to the White House'.

⁵⁹ For the most recent statement, see Office of the United States Trade Representative (2019), 'Joint Statement of the Trilateral Meeting of the Trade Ministers of the European Union, Japan and the United States', 9 January 2019, <https://ustr.gov/about-us/policy-offices/press-office/press-releases/2019/january/joint-statement-trilateral-meeting> (accessed 17 Jan. 2019).

3. Prospects for US–EU Trade Talks in the Trump Era

At their July 2018 meeting, President Trump and European Commission President Juncker opened the door for new US–EU trade talks. As already noted, with USTR Lighthizer having officially notified Congress of the administration's intent to negotiate a trade agreement with the EU in October 2018, and with the publication of the detailed negotiating objectives in January 2019, the US could have theoretically started official negotiations with the EU as early as mid-February 2019. The European Commission has also been following up on different elements of the joint statement from July 2018, including the submission of draft negotiating mandates – one concerning the elimination of tariffs for industrial goods, and the other regarding conformity assessment – to the Council of the European Union. The EU national governments now have to approve the mandates – which is expected to happen in March 2019 – before official negotiations can begin.⁶⁰

In the preparatory phase of trade negotiations, the European Commission usually conducts an informal scoping exercise, which sets out the content and level of ambition of what both parties wish to negotiate, before getting the Council's green light on the negotiating mandate.⁶¹ However, during the 90-day period of consultation required by TPA, the US was unable to conduct a scoping exercise. At the time of publication of this paper, both sides had not yet agreed on the scope of the trade negotiations.

Whether a US–EU trade agreement can be reached will largely depend on the results and speed of forthcoming negotiations. If no rapid progress can be made, President Trump's patience with the EU may run out, leading to renewed tension over transatlantic trade. Trump has already shown signs of impatience with the EU, again raising the threat, in October 2018, of US tariffs on imports of cars and automotive parts from the EU.⁶²

The European Commission has warned that it will suspend negotiations with the US if the Trump administration does not respect the commitment made in July 2018 to abstain from adopting new measures against the EU.

In the event that the US does hit the EU with automotive tariffs, transatlantic trade talks would derail. The European Commission has warned that it will suspend negotiations with the US if the Trump administration does not respect the commitment made in July 2018 to abstain from adopting new measures against the EU.⁶³ In other words, unilateral tariffs on imports of automobiles and automotive parts represent the ultimate obstacle to a US–EU trade agreement.

⁶⁰ European Parliament (2019), 'Trade negotiations with US can start under certain conditions'.

⁶¹ European Commission (undated), 'Negotiating EU trade agreements: Who does what and how we reach a final deal', http://trade.ec.europa.eu/doclib/docs/2012/june/tradoc_149616.pdf (accessed 23 Jan. 2019).

⁶² White House (2018), 'Remarks by President Trump on the United States–Mexico–Canada Agreement', 1 October 2018, <https://www.whitehouse.gov/briefings-statements/remarks-president-trump-united-states-mexico-canada-agreement/> (accessed 20 Nov. 2018).

⁶³ European Commission (2019), 'Recommendation for a Council decision authorising the opening of negotiations of an agreement with the United States of America on the elimination of tariffs for industrial goods', 18 January 2019, http://trade.ec.europa.eu/doclib/docs/2019/january/tradoc_157628.pdf (accessed 23 Jan. 2019).

Limited scope

As outlined in the joint statement by Trump and Juncker, the US and the EU are ‘work[ing] together toward zero tariffs, zero non-tariff barriers, and zero subsidies on non-auto industrial goods’.⁶⁴ But the prospects for such an agreement look slim, for a number of reasons.

First, an agreement that excludes agriculture and automotives may violate the rules of the WTO, which stipulate that free-trade agreements should cover ‘substantially all the trade’ between the negotiating parties.⁶⁵

Second, for now, the US and the EU differ greatly on the potential scope of trade talks. Within days of the July 2018 meeting between Trump and Juncker, fissures appeared over whether to include agriculture.⁶⁶ These differences remain. While the US negotiating objectives call for securing ‘comprehensive market access for U.S. agricultural goods in the EU’,⁶⁷ the European Commission is aiming for a trade agreement that is ‘strictly focused on the removal of tariffs on industrial goods, excluding agricultural products’.⁶⁸

Third, many within the EU believe that the talks will eventually need to include the automotive sector and address public procurement (to better enable EU firms to bid for public contracts in the US), which would be anathema to US negotiators.⁶⁹ The Trump administration’s negotiating objectives make it very clear that the US will exclude state and local governments from public procurement commitments being negotiated and keep in place domestic preferential purchasing programmes such as ‘Buy America’.⁷⁰ These same issues obstructed the TTIP talks and threaten to derail the impending talks yet again.

Fourth, a resumption of the TTIP negotiations – even under another name – would revive public opposition to the deal. Civil society organizations such as Friends of the Earth Europe have criticized the Trump–Juncker agreement as a TTIP revival that could undermine European regulations.⁷¹ They fear that many controversial aspects of the TTIP talks – including the potential compromising of European restrictions on genetically modified food or the EU regime to control the use of toxic chemicals – would be back on the negotiating table. Unsurprisingly, EU officials were quick to emphasize that the trade deal they plan to negotiate with the US ‘is not TTIP 2.0’.⁷²

These significant differences and developments indicate that the agreement between the US and the EU would have a more limited scope than the TTIP negotiations, and perhaps be even more restricted than initially set out in July 2018. Already, the USTR notification letter sent to Congress in October 2018 and the negotiating objectives from January 2019 appear to have a narrower focus than the Trump–Juncker communiqué, pointing only to the aim to ‘address both tariff and non-tariff barriers and to achieve fairer, more balanced trade’; no reference was made to the more ambitious goals of

⁶⁴ European Commission (2018), ‘Joint U.S.-EU Statement following President Juncker’s visit to the White House’.

⁶⁵ See Article XXIV of the General Agreement on Tariffs and Trade (GATT).

⁶⁶ von der Burchard, H. and Hanke, J. (2018), ‘EU-US trade truce falters on Day 1 over farming’, Politico, 26 July 2018, <https://www.politico.eu/article/eu-us-trade-truce-falters-on-day-1-over-farming/> (accessed 20 Nov. 2018).

⁶⁷ Office of the United States Trade Representative (2019), ‘United States–European Union Negotiations: Summary of Specific Negotiating Objectives’.

⁶⁸ European Commission (2019), ‘EU-U.S. Trade Talks: European Commission presents draft negotiating mandates’.

⁶⁹ Stratfor (2018), ‘Truce Aside, U.S.-EU Trade Relations Are In for a Bumpy Ride’, 30 July 2018, <https://worldview.stratfor.com/article/truce-aside-us-eu-trade-relations-are-bumpy-ride> (accessed 20 Nov. 2018).

⁷⁰ Office of the United States Trade Representative (2019), ‘United States–European Union Negotiations: Summary of Specific Negotiating Objectives’.

⁷¹ Friends of the Earth (@foeeurope) (2018), ‘Results of the Juncker-Trump meeting on trade: – The EU commits to importing more fracked gas and GM soy – #TTIP is back and European regulations are in the firing line’, tweet, 26 July 2018, <https://twitter.com/foeeurope/status/1022420047946543106> (accessed 20 Nov. 2018).

⁷² Stratfor (2018), ‘Truce Aside, U.S.-EU Trade Relations Are In for a Bumpy Ride’.

zero tariffs and zero non-tariff barriers; nor was there any mention of subsidies.⁷³ The European Commission's draft negotiating mandates are also very narrow: one focusing on the elimination of tariffs for industrial goods; and the other on conformity assessment, which would help make it 'easier for companies to prove their products meet technical requirements on both sides of the Atlantic'.⁷⁴

Parallel negotiating tracks

The USTR letter to Congress and the negotiating objectives state that the US could pursue talks with the EU 'in stages, as appropriate'.⁷⁵ Rather than following the traditional approach – i.e. striking a comprehensive trade deal by means of a single-track negotiation where nothing is agreed until everything is agreed – future US–EU trade talks may be pursued via parallel tracks where each issue is addressed according to its own timetable.⁷⁶

Rather than following the traditional approach – i.e. striking a comprehensive trade deal by means of a single-track negotiation where nothing is agreed until everything is agreed – future US–EU trade talks may be pursued via parallel tracks where each issue is addressed according to its own timetable.

US and EU negotiators seem to be willing to go down this path, as both parties to the Executive Working Group have indicated that it may be possible to reap 'an early harvest in the area of technical barriers to trade'.⁷⁷ Any future trade negotiations could then lead to 'a more limited trade agreement, focused on tariffs on goods only'.⁷⁸ The talks concerning regulatory engagement are largely influenced by a paper from the European Commission outlining areas of cooperation with the US on topics including pharmaceuticals, medical devices, car safety, cybersecurity and (to some extent) food safety.⁷⁹

The advantages of a more piecemeal, parallel-track approach, building on previous preparatory work, are numerous. A joint US–EU report on the progress of the TTIP talks from January 2017 (when the negotiations were essentially frozen) highlights 'common ground' and 'good progress' on regulatory cooperation.⁸⁰ Rapid progress could be made in some areas of the negotiations by harvesting the low-hanging fruit first. This could potentially create the goodwill that may help the EU keep the threatened US tariffs on automobiles and automotive parts at bay.

⁷³ Office of the United States Trade Representative (2018), 'Trump Administration Announces Intent to Negotiate Trade Agreements with Japan, the European Union and the United Kingdom'. Office of the United States Trade Representative (2019), 'United States–European Union Negotiations: Summary of Specific Negotiating Objectives'.

⁷⁴ European Commission (2019), 'EU-U.S. Trade Talks: European Commission presents draft negotiating mandates'.

⁷⁵ Office of the United States Trade Representative (2018), 'Trump Administration Announces Intent to Negotiate Trade Agreements with Japan, the European Union and the United Kingdom'. Office of the United States Trade Representative (2019), 'United States–European Union Negotiations: Summary of Specific Negotiating Objectives'.

⁷⁶ Rashish, P. (2018), *Making the Atlantic Great (Again)? Prospects for New U.S.-EU Trade Negotiations*, Washington, DC: American Institute for Contemporary German Studies, <https://www.aicgs.org/site/wp-content/uploads/2018/09/IB-58-Rashish-MAGA.pdf> (accessed 20 Nov. 2018).

⁷⁷ Politi, J. and Brunsten, J. (2018), 'US trade talks with EU on course for partial deal in November', *Financial Times*, 10 September 2018, <https://www.ft.com/content/c0b6bb52-b508-11e8-bbc3-ccd7de085ffe> (accessed 20 Nov. 2018).

⁷⁸ Valero, J. (2018), 'EU willing to agree on zero car tariffs with Trump', EURACTIV.com, 31 August 2018, <https://www.euractiv.com/section/economy-jobs/news/eu-willing-to-agree-on-zero-car-tariffs-with-trump/> (accessed 20 Nov. 2018).

⁷⁹ Stearns, J. (2018), 'EU Eyes Closer U.S. Ties Regulating Sectors From Cars to Drugs', Bloomberg, 19 October 2018, <https://www.bloomberg.com/news/articles/2018-10-19/eu-eyes-closer-u-s-ties-regulating-sectors-from-cars-to-drugs> (accessed 20 Nov. 2018).

⁸⁰ European Commission and Executive Office of the President of the United States (2017), 'U.S.-EU Joint Report on TTIP Progress to Date', 17 January 2017, http://trade.ec.europa.eu/doclib/docs/2017/january/tradoc_155242.pdf (accessed 20 Nov. 2018).

But while a deal on regulatory cooperation with regard to car safety might be achievable quickly (given that the US and the EU made a lot of progress on this front during the TTIP negotiations), any negotiations about regulatory cooperation in other areas – in particular chemicals that may be harmful to humans or the environment, and cosmetics – would be likely to encounter the same hurdles and backlash as they did during the TTIP talks. Thus, the conclusion of any deal focused on broader regulatory cooperation would be a slow and difficult process. Previous efforts towards regulatory cooperation, dating back to the 1990s, have highlighted that it is a sensitive and controversial issue that raises legitimate questions about a potential lowering of protection for consumers and the environment, or about the ability to regulate in the public interest.

In short, the focus on regulatory cooperation, and a quick win in the area of automotive safety regulations, is mostly a political gesture that offers a near-term opportunity. Notably, some regulatory issues will be highly contentious, and will likely contribute to an arduous process in the longer term.

Can the EU speak with one voice?

The prospects of success in future transatlantic trade negotiations will also depend on whether the EU is able to speak as one. Differences between France and Germany over how best to respond to the US steel and aluminium tariffs notably revealed internal fissures within the EU. Given its dependence on exports, Germany was much more willing to strike a deal in order to avoid increased tensions that might result in the US imposing tariffs on imports of automobiles and automotive parts. In contrast, France took a much tougher line, stating that the EU would have no choice but to enter into a trade war with the US.⁸¹

Italy's present government, a Eurosceptic coalition of the Lega and the populist Five Star Movement, could also undermine the EU's ability to hold a unanimous line on trade. For instance, Italy has threatened to block the ratification of the EU–Canada Comprehensive Economic and Trade Agreement (CETA), which needs to be approved by all EU member states to fully enter into force, over concerns that the deal does not adequately guarantee that speciality food or beverages originating from specific locations in Europe are the only products allowed to be sold under their respective names.⁸² Thus, strong interests concerning the protection of these so-called geographical indications by Italy (and other EU member states such as Greece, Spain and Portugal) could become a sticking point in future US–EU trade negotiations – as occurred during the TTIP talks.

The fact that the EU has started negotiations with the US even though the latter did not remove the steel and aluminium tariffs has exposed the abandonment by the EU of its initial assurance to not negotiate 'with a gun at its head'.

Despite these internal divisions, the EU has so far responded to the Trump administration's action on trade with a united front. But any cracks may widen, as US–EU trade talks intensify, as long as the metal tariffs remain in place. The fact that the EU has started negotiations with the US even though the latter did not remove the steel and aluminium tariffs has exposed the abandonment by the EU of its initial

⁸¹ Donnan, S. (2018), 'US fires first shot in trade war with allies', *Financial Times*, 31 May 2018, <https://www.ft.com/content/7ba37aa2-64ac-11e8-a39d-4df188287fff> (accessed 20 Nov. 2018).

⁸² Guarascio, F. and Blenkinsop, P. (2018), 'Italy in no rush to reject EU-Canada trade deal – farm minister', *Reuters*, 16 July 2018, <https://uk.reuters.com/article/uk-eu-canada-italy/italy-in-no-rush-to-reject-eu-canada-trade-deal-farm-minister-idUKKBN1K61IX> (accessed 20 Nov. 2018).

assurance to not negotiate ‘with a gun at its head’.⁸³ On this occasion, President Trump’s pressure tactics have given the US a small tactical victory. Moreover, the EU risks demonstrating a further volte-face as regards its pledge not to sign free-trade agreements with countries that do not ratify the 2015 Paris Agreement on climate change, from which the US has withdrawn under Trump.⁸⁴

The UK’s impending withdrawal from the EU – which will mean the loss of a significant pro-free-trade voice within the bloc – also has consequences for the EU’s ability to speak with one voice in negotiations with the US. Brexit, and its implications for the future of UK–EU relations, causes uncertainty over the degree to which the UK will continue to be a gateway for the US to the EU27 single market. This, in turn, has consequences for any concessions that the EU and the US may be willing to make in their bilateral trade talks. President Trump has been a vocal supporter of the UK’s decision to leave the EU, and the US administration has expressed its desire to strike a bilateral trade deal with the UK after Brexit.

Complicating matters still further will be the forthcoming elections to the European Parliament in May 2019. There can be expected to be significant changes – not only to the complexion and tone of discourse of the legislative body that will ultimately have to approve any future EU trade deal with the US, but also in terms of the selection of the next president of the European Commission – the executive body that prepares and negotiates the EU’s international trade agreements.

From mid-2019, there could be a significant shake-up in the composition of the EU Parliament, with UK parties no longer represented, traditional social democratic parties losing support in many countries, new parties entering the parliament for the first time (including, it may be expected, French President Emmanuel Macron’s *En Marche*) and Eurosceptic and anti-EU forces expected to squeeze traditional centrist groups. Even though the pro-trade, centre-right European People’s Party (EPP) is likely to remain the largest grouping overall, members from far-right and far-left parties could add their voices to reservations already being expressed in the European Parliament about a potential US–EU free-trade deal. The appointment of a new European Commission, including a potential replacement for Cecilia Malmström, whose term as Commissioner for Trade will end on 31 October 2019, could have implications for transatlantic trade negotiations. If no significant progress in the trade talks can be made before the elections to the European Parliament, they are unlikely to advance until after 2019.

Lessons from other trade negotiations

Other recent US trade negotiations – and ongoing trade disputes – will also have an impact on US–EU talks. For instance, the US may want to use certain aspects of the recently renegotiated United States–Korea Free Trade Agreement (KORUS) or the USMCA as a template for its talks with the EU. So far, however, the EU has been unwilling to bow to what it perceives as troublesome demands by the Trump administration in its most recent trade negotiations.⁸⁵ For instance, as part of the updated KORUS agreement, South

⁸³ Simon, F. (2018), ‘Macron: We won’t negotiate ‘with a gun to our head’ over US tariffs’, EURACTIV.com, 26 March 2018, <https://www.euractiv.com/section/economy-jobs/news/macron-we-wont-negotiate-with-a-gun-to-our-head-over-us-tariffs/> (accessed 17 Jan. 2019).

⁸⁴ President Trump announced his intention to withdraw the US from the Paris climate accord in June 2017, but the process of withdrawal, under Article 28 of the agreement, can only begin the day after the next US presidential election in November 2020.

⁸⁵ Bravo, R., Leonard, J. and Donnan, S. (2018), ‘Trump’s EU Trade Talks Quickly Become Contentious’, Bloomberg, 22 October 2018, <https://www.bloomberg.com/news/articles/2018-10-21/trump-s-european-union-trade-talks-quickly-become-contentious> (accessed 20 Nov. 2018).

Korea agreed to a quota set at 70 per cent of the average annual volume of its steel exports to the US in 2015–17. In exchange, South Korea received a permanent exemption from US steel tariffs.⁸⁶ The EU believes that the use of such voluntary export restraints violates WTO rules.⁸⁷

The USMCA also contains lessons for the EU as it contemplates its trade talks with the US.⁸⁸ On the positive side, one important implication is that a trilateral deal was reached despite the US's preference (and earlier efforts) to strike separate, bilateral agreements with Mexico and Canada. Another inference is that the USMCA kept most of the old NAFTA framework in place, with some additional provisions originating from the proposed Trans-Pacific Partnership (TPP – from which Trump withdrew the US shortly after his inauguration in January 2017). This highlights some willingness in the US administration, notwithstanding the Trumpian trade ideology, to be flexible and to make compromises.

At the same time, if the US uses the USMCA as a blueprint for an agreement with the EU, this could have negative repercussions for the EU. Two particular USMCA provisions stand out as being potentially problematic for the EU if the US attempts to use similar language in a US–EU deal. First, the USMCA's Article 32.10 states that any one of the three parties must inform the other two in advance if it intends to start free-trade negotiations with a 'non-market economy' (such as China), and that the other partners can terminate the USMCA if those negotiations lead to a free-trade agreement.⁸⁹ As such, if a transatlantic trade agreement were to follow this line – and the US negotiating objectives point in that direction⁹⁰ – it would render more difficult any future EU trade talks with China, which is now the bloc's second largest trading partner (after the US). Additionally, the USMCA has a 16-year 'sunset' clause, which implies that the terms of the agreement will expire once that period has elapsed unless each party confirms its wish to continue the agreement. The three parties will meet six years after the USMCA comes into force to decide whether to renew the agreement for a further 16 years.⁹¹ While the renewable 16-year term is significantly longer than the five-year 'sunset' clause initially advocated by the US, it does suggest that a future US–EU trade deal would also come with an expiry date.

A final lesson that the USMCA holds for the EU concerns the exemption from tariffs. Even though Mexico and Canada sought an exemption from the US's steel and aluminium tariffs, the tariffs remain in place. Mexico and Canada did, however, persuade the US to enter into side agreements that would protect them from tariffs on imported automobiles and automotive parts.⁹² This suggests that the EU may have to be willing to submit to continued US tariffs, even in the event that transatlantic trade talks progress and a deal is concluded.

⁸⁶ Office of the United States Trade Representative (2018), 'New U.S. Trade Policy and National Security Outcomes with the Republic of Korea', 28 March 2018, <https://ustr.gov/about-us/policy-offices/press-office/fact-sheets/2018/march/new-us-trade-policy-and-national> (accessed 20 Nov. 2018).

⁸⁷ Malmström, C. (2018), 'Friends Don't Let Friends Impose Tariffs', *Wall Street Journal*, 7 June 2018, <https://www.wsj.com/articles/friends-dont-let-friends-impose-tariffs-1528411740> (accessed 17 Jan. 2019).

⁸⁸ The USMCA is expected to take effect on 1 January 2020, but requires ratification by all three countries before then. Given the outcome of the US midterm elections in November 2018, the new Democratic majority in the House of Representatives may choose to hold up the ratification process.

⁸⁹ Office of the United States Trade Representative (2018), *USMCA – Chapter 32, Exceptions and General Provisions*, https://ustr.gov/sites/default/files/files/agreements/FTA/USMCA/Text/32_Exceptions_and_General_Provisions.pdf (accessed 20 Nov. 2018).

⁹⁰ The US's negotiating objectives call for 'a mechanism to ensure transparency and take appropriate action if the EU negotiates a free trade agreement with a non-market country'. Office of the United States Trade Representative (2019), 'United States–European Union Negotiations: Summary of Specific Negotiating Objectives'.

⁹¹ Office of the United States Trade Representative (2018), *USMCA – Chapter 34, Final Provisions*, https://ustr.gov/sites/default/files/files/agreements/FTA/USMCA/Text/34_Final_Provisions.pdf (accessed 20 Nov. 2018).

⁹² Bryan, B. (2018), 'The US, Canada, and Mexico's newly signed trade pact looks a lot like NAFTA. Here are the key differences between them.', *Business Insider*, 1 October 2018, <http://uk.businessinsider.com/us-canada-mexico-trade-deal-usmca-nafta-details-dairy-auto-dispute-resolution-2018-10> (accessed 20 Nov. 2018).

Meanwhile, EU officials have stated that tactics used by President Trump to pressure Mexico and Canada into concessions during the USMCA negotiations will not work in transatlantic trade talks. They believe that the EU's size and trading power put the bloc on a more equal footing with the US.⁹³ However, unless the bloc's member states speak with one voice, the EU and US will not be an equal match. The US would quickly be able to take advantage of any internal fissures within the EU and use these as pressure points in the negotiations.

A simulation of US–EU trade talks in an era of protectionism

Simulation overview

In order to better understand how US–EU trade talks might play out in an era of protectionism, Chatham House organized a simulation exercise. The event, conducted on 6 September 2018, involved a group of early- to mid-career specialists drawn from think-tanks, academia, businesses and NGOs, from across Europe and the US.

Simulation exercises facilitate the modelling of the potential behaviours of different actors in a negotiation, in terms of the key interests they might adopt, and the tactics by which they might pursue those negotiation demands. They also enable the testing of how the various actors might respond to changes in the hypothetical negotiation environment and react to new developments as they occur.

This exercise, set in April 2019, simulated multilevel negotiations in the lead-up to and during a meeting of US and European trade representatives in Brussels. Negotiations proceeded in two stages: the first stage focused on the 'domestic level', and the second stage on the 'international level'. During the first stage of negotiations, the US and EU teams, meeting separately, were asked to come up with an initial position statement (i.e. a list of negotiation demands and 'red lines' for their delegation). The second stage of the simulation involved the bilateral negotiations between the US and EU teams. At the end of the simulation, the lead negotiators were tasked with announcing whether or not they would recommend that the US and the EU should formally launch transatlantic trade negotiations, in accordance with their respective domestic procedures; and, if so, to state what should be the scope and level of ambition for the future trade talks.

Throughout both stages of the simulation, interest groups sought to influence the negotiations. The US and EU lead negotiators also consulted closely with their respective legislatures and other relevant government representatives. In addition, participants were required to take into consideration and respond to interjects, designed to reflect real-life negotiation pressures.

Simulation methodology and observations

Since the purpose of the simulation was to model how the US and the EU might negotiate in an early phase of potential future trade talks, participants were selected with relevant experience to play the roles of key government representatives and other stakeholders. In advance of the simulation, each participant received a brief of the negotiation interests for their individual role. These interests were based on extensive research by Chatham House staff. Participants were free to interpret the list of interests as they saw fit, but were directed not to act in complete opposition to their role's perceived interests. They were authorized to use any tools or instruments within their remit to influence the negotiations.

Each team was headed by two lead negotiators from the US–EU Executive Working Group. These lead negotiators were the main interlocutors, and were tasked with achieving an agreement that met the interests of their entire delegation. The lead negotiators focused on striking compromises and seeking concessions – both within their own team during the first stage of the negotiations, and with the other team during the second stage. They requested stakeholder input, outlined offensive and defensive interests as well as red lines, and communicated their delegation's positions in public and private statements and meetings.

⁹³ Peker, E. (2018), 'Europe Tells Trump: Don't Bully Us on Trade', *Wall Street Journal*, 5 October 2018, <https://www.wsj.com/articles/europe-tells-trump-dont-bully-us-on-trade-1538750247> (accessed 20 Nov. 2018).

The public-sector representatives (delegates from key US government departments, trade ministers from influential EU member states, and members of the US Congress and the European Parliament) played a critical role in the decision-making process. As such, they sought to advance their national or political interests in public and private communications with the lead negotiators, with their counterparts on the other team, or with relevant stakeholders among the business and NGO communities. Representatives from the US and EU legislative branches also reminded the lead negotiators of their role in setting the mandate for negotiations, and threatened to veto any future deal that crossed their red lines.

The private interest groups – including business, agriculture, environmental, consumer and labour representatives – tried to influence the negotiations through direct lobbying and other activities (such as announcing protests and releasing reports to influence other players and public opinion). Moreover, they built transnational coalitions with like-minded interest groups from the other team.

The US and European Commission presidents did not play an active role in the simulated negotiations. However, they featured in the exercise in a virtual sense, through interjects by Chatham House researchers.

Simulation analysis

Overall, the efforts by the US and the EU did not lead to a breakthrough agreement – at least not within the time frame of the simulation exercise. The lead negotiators from both sides deemed it premature to recommend the start of formal negotiations. Instead, they agreed to set up a Joint Regulatory Dialogue with the aim of enhancing engagement on standards and regulations for goods and services.

The simulation highlighted a number of issues. It displayed the **variety of tools available for influencing negotiations** as described in the observations above. Notably, one instrument that was not used in this simulation was the leaking of documents (whether to members of the other delegation, to interest groups or to the press). And while negotiators did at various points threaten to walk away from the talks, they ultimately did not do so and generally kept disruptions to a minimum. This could potentially indicate a bias in the simulated negotiation whereby participants have an inherent tendency to try to broker a consensus position because they work on transatlantic trade issues and broadly support increased cooperation and economic ties. Real-life negotiations could potentially be more fraught.

By simulating negotiations at the domestic and international level, the exercise modelled multilevel bargaining. The progress of the simulation underscored how disaggregated domestic interests and national veto players affect international trade negotiations, and highlighted that the US and the EU do not always operate as unified actors. In this respect, **maintaining a united front was more of a challenge for the EU than for the US side**. All the same, despite efforts by the US to engage in bilateral talks, the member states of the EU mostly deferred to the EU lead negotiators. Only on one occasion did Italy, France and Germany hold a separate discussion with US representatives without the EU lead negotiators being involved. Otherwise, the EU side took meetings together and coordinated internally. However, disagreement between the member states – particularly France and Germany – over how best to resolve the issue of US steel and aluminium tariffs in the name of national security revealed fissures, which made it difficult for the EU to maintain a united position during discussions with the US. Tactics – for instance, whether a guarantee by the US to not impose tariffs on automobile and automotive parts imports from the EU should be a prerequisite for transatlantic trade negotiations to start – were deliberated by the EU team in great detail.

Although their role in the negotiations was limited, **non-governmental interest groups sought to leverage their influence by building transnational coalitions**. For instance, the US and EU business lobby groups formed an alliance, as did civil society organizations on both sides of the Atlantic. Building on experience from the TTIP negotiations, they emphasized the need for stakeholder engagement and transparency in trade negotiations. But as the simulated talks were in an early stage, the US and EU lead negotiators' response was minimal.

The simulation also underscored the **issues that could potentially become sticking points in future US–EU trade talks**. The two sides' negotiators had to **deal with concerns raised by the 'America First' agenda** of the Trump administration. In particular, they tried to resolve the issue of US steel and aluminium tariffs in the name of national security, and that of the EU's retaliatory tariffs. They also attempted to settle issues regarding a permanent exemption for the EU from tariffs on automobile and automotive parts imports, which the US had introduced prior to the talks (as part of the simulation setting). But those more recent issues were bracketed during the simulated negotiations to be discussed at a later point.

Instead, **long-standing issues already highlighted during the TTIP negotiations proved to be the major stumbling blocks** in the simulated negotiations. Agriculture and the related issues of geographical indications and food safety standards were the main sources of disagreement – both between the US and the EU, but also between various EU member states. Moreover, the opening up of public procurement markets was a contentious issue. The US had listed a chapter on investor–state dispute settlement (ISDS) among its offensive interests for a future trade agreement with the EU, but investment protection did not become a focus during the simulated negotiations – at least during the limited time frame of the exercise.

Participants largely ignored President Trump’s antics, which were simulated via interjects. For instance, a tweet by the US president criticizing Germany for widening the US’s trade deficit while not meeting its NATO defence spending commitments provoked little reaction, as did a tweet by Trump threatening to pull out of the WTO. Such interjects prompted brief debate among participants as to how best to respond, but the negotiations then continued relatively unchanged. This finding seems to parallel the real-world situation in which **EU leaders focus on the actions of key US representatives, rather than on Trump’s own, often-shifting rhetoric**.

Issues of shared global concern were barely addressed in the negotiations, which focused almost exclusively on efforts to further integrate the transatlantic marketplace. While each team briefly discussed the goals for reforming the WTO or tackling China’s unfair trade practices during the first stage of the negotiations (i.e. at the domestic level), the parties did not talk about increased cooperation on those issues during the international negotiation stage – again perhaps given the time constraints of the simulation.

Overall, the simulation provides insights into how future US–EU trade talks might play out in the dual context of the legacy of the TTIP discussions and the current US administration’s protectionism and ‘America First’ rhetoric. The simulation exercise also offers lessons for policymakers to adopt in real-life negotiations, as set out in the conclusion to this paper.

Transatlantic cooperation beyond a bilateral trade deal

In addition to pursuing a transatlantic free-trade agreement, the US and the EU are jointly committed to work closely together with like-minded partners to tackle unfair trade practices (widely understood to implicate China) and to reform the WTO.⁹⁴ This is an encouraging sign that transatlantic cooperation on trade is not just limited to a future bilateral deal, and it harbours the potential to tackle the two issues that are arguably the most pressing and important for the future of the global trading system. Since the US and the EU are China’s two most important trading partners, a united US–EU front could potentially lead to real progress and compel Beijing to change its trade practices. But for this to happen, the US and the EU need to not only have a shared assessment concerning the problems, but also find common ground on viable solutions.

Since the US and the EU are China’s two most important trading partners, a united US–EU front could potentially lead to real progress and compel Beijing to change its trade practices.

In working with the US to address China’s trade practices, the EU is performing multiple balancing acts. First, while the EU shares the concerns of the Trump administration with regard to China, the bloc also opposes the US’s approach of using tariffs to force China to change its behaviour. At the same time, some voices within the EU and among its member states have acknowledged that even if they

⁹⁴ European Commission (2018), ‘Joint U.S.-EU Statement following President Juncker’s visit to the White House’.

do not agree with the use of tariffs as a negotiating tactic, President Trump's high-pressure approach may prove effective.⁹⁵ The next balancing act involves the EU engaging with the US to tackle common concerns regarding China, while also trying to convince Trump to roll back the steel and aluminium tariffs and prevent the imposition of further tariffs. Finally, the EU is balancing its relationships with the US and with China – its two biggest trading partners – and will want to maintain a degree of cooperation with both. In the months and years ahead, it is likely to try to avoid a clear choice in siding with the US or China, and may opt for a hedging strategy.

As regards reforming the WTO, the EU has tabled some proposals with the goal of updating the rules so as to achieve a more level playing field and countering market distortions by China (though the country is not named directly).⁹⁶ The EU's proposals also seek to overcome the imminent deadlock of the dispute settlement system, due to the US's blocking of appointments to the Appellate Body of the WTO (as described earlier in this paper). However, the US has already indicated its rejection of some of the EU's suggestions.⁹⁷ In light of the disagreement between the US and the EU, and the fact that all 164 WTO members need to reach a consensus on reform, the EU's attempts at modernizing the global international trade body are likely to encounter many hurdles.

⁹⁵ Wu, W. (2018), 'China 'keeping wary eye' on US and EU as trade pressure mounts', *South China Morning Post*, 28 August 2018, <https://www.scmp.com/news/china/diplomacy-defence/article/2161329/china-keeping-wary-eye-us-and-eu-trade-pressure-mounts> (accessed 20 Nov. 2018).

⁹⁶ European Commission (2018), *Concept Paper – WTO Modernisation*, http://trade.ec.europa.eu/doclib/docs/2018/september/tradoc_157331.pdf (accessed 20 Nov. 2018).

⁹⁷ EURACTIV.com with Reuters (2018), 'US says it cannot support some of EU's ideas for WTO reform', 5 October 2018, <https://www.euractiv.com/section/economy-jobs/news/us-says-it-cannot-support-some-of-eus-ideas-for-wto-reform/> (accessed 20 Nov. 2018).

4. Conclusion: The Way Forward on Transatlantic Trade Cooperation

US President Trump and European Commission President Juncker agreed a trade truce in July 2018. Since then, however, disagreement has emerged during exploratory talks over what issues to include in future transatlantic trade negotiations. Moreover, while the US has (for now) shelved its threat to impose tariffs on automobiles and automotive parts, President Trump has warned that they could come into play again if the transatlantic trade talks do not display significant momentum.

If the US–EU free-trade talks are to have a real prospect of success, the recommendations set out in this chapter may offer a guide to the way forward. They are drawn from the preceding analysis and the lessons offered by the Chatham House simulation exercise on transatlantic trade talks in an era of protectionism (described in the previous chapter).

The best way forward in the current political and economic environment is a more multifaceted approach aimed at both the transatlantic market and global challenges of common concern.

Whereas policy recommendations put forward elsewhere have tended to focus on specific challenges – such as concrete steps to avoid an escalation of trade tensions between the US and the EU,⁹⁸ or technical proposals to build out the bilateral economic ties⁹⁹ – the case made here is that the best way forward in the current political and economic environment is a more multifaceted approach aimed at both the transatlantic market and global challenges of common concern. These recommendations are not intended to be comprehensive; rather the aim is to help establish a framework for strengthening US–EU trade relations.

Fold ‘quick wins’ into a longer-term deal

A successful path might be to ‘think small’ and get rapid results – for instance by focusing on regulatory cooperation in the area of car safety. This would build on the July 2018 trade détente, and set a foundation for negotiating a trade agreement on industrial goods in the longer term. With a parallel-track approach, issues would be resolved according to their individual schedule.

The history of TTIP and the current protectionist tendencies of the Trump administration both suggest that achieving a fully fledged US–EU free-trade agreement on a single track is almost impossible at this point. But given that the US and EU markets are already closely interlinked, and trade barriers are for the most part low, there is no need to rush into formalizing the transatlantic trade relationship from an economic point of view. At the same time, however, securing some quick wins would be politically

⁹⁸ Münchau, W. (2018), ‘Europe should weigh its response to US tariff threats with care’, *Financial Times*, 22 July 2018, <https://www.ft.com/content/c1911400-8bfa-11e8-b18d-0181731a0340> (accessed 23 Jan. 2019).

⁹⁹ American Chamber of Commerce to the European Union (2018), *A new agenda for transatlantic economic cooperation: Recommendations from the US business community in Europe*, November 2018, http://www.amchameu.eu/system/files/position_papers/a_new_agenda_for_transatlantic_cooperation_november18_final.pdf (accessed 23 Jan. 2019).

expedient. While the US administration has an interest in agreeing a US–EU trade deal to showcase President Trump’s deal-making abilities ahead of the US presidential election in 2020, the EU is interested in a swift agreement primarily to forestall the potential imposition of automotive tariffs. More broadly, quick wins in the coming months would create critical momentum for a more ambitious and comprehensive US–EU free-trade agreement in the future.

Apply lessons learned from TTIP

While the logic behind TTIP (in terms of both economic gains and wider strategic benefits) is still valid, future US–EU trade negotiations should not be ‘TTIP 2.0’. This implies not just relaunching TTIP under a different name, but excluding the most controversial issues (such as agriculture or ISDS) that hampered progress on TTIP. In seeking a US–EU trade agreement, a critical balance must be struck between a deal that is narrow enough to be viable but also sufficiently broad to cover ‘substantially all the trade’ in line with WTO rules. Transatlantic trade negotiations should also apply the lessons of TTIP with regard to the negotiating process (particularly concerning transparency and stakeholder engagement). On the EU side, the publication of the draft negotiating mandates at the same time as they were submitted to the member states for approval is an important positive step.

Avoid the risk of further transatlantic division

Transatlantic trade talks will require significant political investment from both sides. But with an ‘America First’ trade policy and a critical political calendar for the EU in the first half of 2019 (in the context of the UK’s intended withdrawal, and the forthcoming elections to the European Parliament), this will be hard to guarantee. If the talks struggle to make progress, the US is likely to act on its threat to impose tariffs on imports of cars and automotive parts from the EU. This would strain the transatlantic relationship severely. Thus, the biggest risk is that the current efforts to further integrate the transatlantic marketplace will backfire. In other words, rather than strengthening transatlantic ties, a futile attempt to negotiate a free-trade agreement would further divide the US and the EU at a time when both sides need to face shared global concerns together.

Adopt a common approach for systemic global trade problems

In addition to focusing on the transatlantic market, the US and the EU should use their trade talks as a forum to discuss ways to set a constructive agenda to address shared concerns regarding the global trading system – such as the need for reform of the WTO, and China’s trade practices. Achieving quick progress on US–EU bilateral trade issues would strengthen any joint efforts on more systemic problems.

The best way to tackle joint concerns arising from China’s global steel overcapacity, the operations of certain state-owned enterprises, or practices related to forced technology transfers and intellectual property theft is for a group of countries to work together – both inside and outside the WTO – to bring about reforms. In particular, the existing cooperation between the EU, Japan and the US should be enhanced. This trilateral cooperation could be the foundation for a ‘big, bold, comprehensive case at the WTO filed by a broad coalition of countries that share the United States’ substantive concerns about

China’.¹⁰⁰ A broad coalition of countries – even if some are opposed to the Trump administration’s unilateral tactics – offers the best chance to put sufficient pressure on China to change its policies and practices. At the same time, the successful dispute settlement of such a comprehensive case at the WTO would restore confidence in the organization that governs international trade.¹⁰¹

For the EU: adopt a balanced approach to engaging with Trump

In engaging with the Trump administration, the EU needs to speak with one voice. In particular, this means overcoming Franco-German divisions over how best to respond to the current and any future unilateral tariffs imposed by the US. A balanced strategy would be to retaliate in accordance with WTO rules but without escalating the dispute. To increase internal EU cohesion, Germany should also undertake measures to address its structural trade surplus. This is a valid concern that has been raised not only by the Trump administration, but also by the IMF and by other EU member states.

A better strategy for the EU would be to fill the void now left by the US in the global trade arena.

The EU should not bide its time and simply wait out the term of the Trump administration. Such a tactic may prove futile, not least as Trump could be a two-term president. And even if the Democrats do retake the White House in 2020, some of the current protectionist tendencies are likely to linger. A better strategy for the EU would therefore be to fill the void now left by the US in the global trade arena. Already, the EU has recently signed separate trade deals with Canada and Japan, and has opened negotiations with Australia and New Zealand. The EU should also continue to collaborate with partners around the world – including the UK after Brexit – in defence of the multilateral rules-based international trading system.

These recommendations for transatlantic economic cooperation potentially offer a way to end the ‘tug of war’ between the US and the EU, and instead allow both transatlantic partners to better align their goals. This would help to strengthen not only the bilateral trade relationship, but global commerce as well.

¹⁰⁰ Hillman, J. (2018), ‘Testimony before the U.S.-China Economic and Review Security Commission’, 8 June 2018, <https://www.uscc.gov/sites/default/files/Hillman%20Testimony%20US%20China%20Comm%20w%20Appendix%20A.pdf> (accessed 20 Nov. 2018).

¹⁰¹ Ibid.

About the Author

Marianne Schneider-Petsinger is Geoeconomics Fellow in the US and the Americas Programme at Chatham House, responsible for analysis at the nexus of political and economic issues. She writes and speaks on global trade, transatlantic economic cooperation, and the US's use of geoeconomic strategies and tools. Marianne is a regular speaker and panellist at events and conferences, as well as a guest commentator on broadcast news.

Before joining Chatham House in 2016, she managed the Transatlantic Consumer Dialogue, an international membership body representing consumer organizations in the EU and the US. She also previously worked for a think-tank on transatlantic affairs in the US, and for an economics ministry in Germany.

Marianne holds a BA in international affairs and economics from the University of Maine. She completed her master's degree, focusing on international trade and finance, at the Fletcher School of Law and Diplomacy at Tufts University and the John F. Kennedy School of Government at Harvard University.

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Cover image: US President Donald Trump and President of the European Commission Jean-Claude Juncker walk away after the conclusion of a joint statement in the Rose Garden of the White House in Washington, DC on 25 July 2018.

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The Royal Institute of International Affairs
Chatham House
10 St James's Square, London SW1Y 4LE
T +44 (0)20 7957 5700 F +44 (0)20 7957 5710
contact@chathamhouse.org www.chathamhouse.org

Charity Registration Number: 208223