



Agricultural and Resource Economics ARE UPDATE

Giannini Foundation of Agricultural Economics, University of California

Vol. 27, No. 4 Mar/Apr 2024

ALSO IN THIS ISSUE

Does Seeing a Wind Turbine Depress Your Home Value? Wei Guo, Leonie Wenz, and Maximilian Auffhammer	5
Faculty Profile: Alexandra Hill	8
Conflicts in California's Food Safety and Sustainable Agricultural Practices Emily Zakowski, Rachael Goodhue, and Kevi Mace.....	9

Revoking China's Preferred Trade Status Would Be Costly for California Agriculture

Colin A. Carter and Sandro Steinbach

The U.S. House Select Committee on the Chinese Communist Party recently issued a report on China's economic policies. The committee suggested countering economic and security threats with U.S. trade policy changes aimed at China. A key recommendation was discontinuing the Permanent Normal Trade Relations (PNTR) status, which currently allows China to trade with the United States at most-favored-nation tariff rates. Revoking PNTR would likely provoke trade retaliation by China, potentially raising China's agricultural import tariffs by 9.5%, equivalent to the change in U.S. tariffs if China's PNTR status was revoked. This could result in the value of California's agricultural exports to China falling by one-third, with associated trade losses of \$1 billion annually.

There is a growing consensus among U.S. lawmakers on the need to reassess the U.S.-China trade relationship and possibly ramp up protectionism. This view is partly driven by concerns over some of China's political actions perceived as threats to U.S. national

security and human rights violations in China. In addition, of concern to the United States is that China has not evolved into a market economy, which contradicts many rules and objectives of the World Trade Organization (WTO). Calls to revoke China's Permanent Normal Trade Relations (PNTR) status would significantly raise U.S. import tariffs on products from China. As a result, China would be incentivized to respond by raising its import tariffs, leading to another trade war. This would be bad news for California agriculture because it would lead to lower farm prices, lost export opportunities, and lost jobs, as experienced during the trade wars in 2018/19 during the Trump administration. China is the world's largest importer of U.S. agricultural products, and U.S. farmer access to that large market is again at risk.

The economic relationship between the United States and China has evolved considerably since President Nixon's visit in 1972, leading to formal trade relations and China's eventual accession to the WTO in 2001. This journey, marked by President Clinton's enactment of H.R. 4444, granted China the most-favored-nation

status, aligning its tariff rates with other WTO members. The legislation resulted in profound changes in global trade dynamics, reducing China's average import tariffs and resulting in a substantial increase in bilateral trade between the United States and China. U.S. exports to China, particularly agriculture, machinery, and technology, have surged over the past two decades.

The U.S. criticism of China's WTO membership centers around non-compliance with WTO regulations and accession commitments. However, we note that the United States won all of its WTO disputes against China in the last twenty years, resulting in economic policy adjustments by China, demonstrating the WTO's effectiveness in enforcing compliance. Unfortunately, the WTO Appellate Body became defunct in 2019, mainly due to the United States blocking appointments of new appellate body judges. Since then, the ability to enforce trade rules with China has been severely undermined because the appeals mechanism is not functioning. Instead of going through the WTO to address trade concerns, the Trump Administration imposed import tariffs on

Chinese imports in response to intellectual property violations. This led to a cycle of retaliatory tariffs, with considerable negative implications for California agriculture. These retaliatory tariffs affected over \$32 billion worth of U.S. agricultural exports at the time of implementation without resulting in China altering its economic practices. The shift from multilateral WTO dispute resolution to unilateral tariff wars reflects a change in U.S.-China trade relations, raising questions about the future of international trade norms and enforcement. The United States turned its back on the WTO, which is unfortunate because other countries may follow suit and increase protectionism.

Following the 2018/19 trade war, U.S. lawmakers have implemented additional economic restrictions against China. For instance, the passing of the 2021 U.S. Uyghur Forced Labor Protection Act aimed to curtail U.S. imports of goods produced with forced labor in China. The 2022 U.S. export controls on advanced artificial intelligence (AI) semiconductor

chips have meaningfully impacted China's technological capabilities and the modernization of China's military. Amid these tensions, proposals to revoke China's PNTR status have gained momentum in Washington, D.C., reflecting a shift in U.S.-China economic relations before the presidential elections. This policy shift signals a critical reassessment of the U.S.-China economic engagement, with potentially significant implications for California farmers and ranchers.

California Agriculture Depends on Access to China's Market

Since China joined the WTO in December 2001, California's annual agricultural exports to China expanded from \$0.2 billion to more than \$2.6 billion in 2023. During the same period, the share of California agricultural exports to China grew from 2.4% to 9.9% of total California agricultural exports. The new market access contributed to shifts in California's agricultural production, with the area of cash crops expanding considerably. For example,

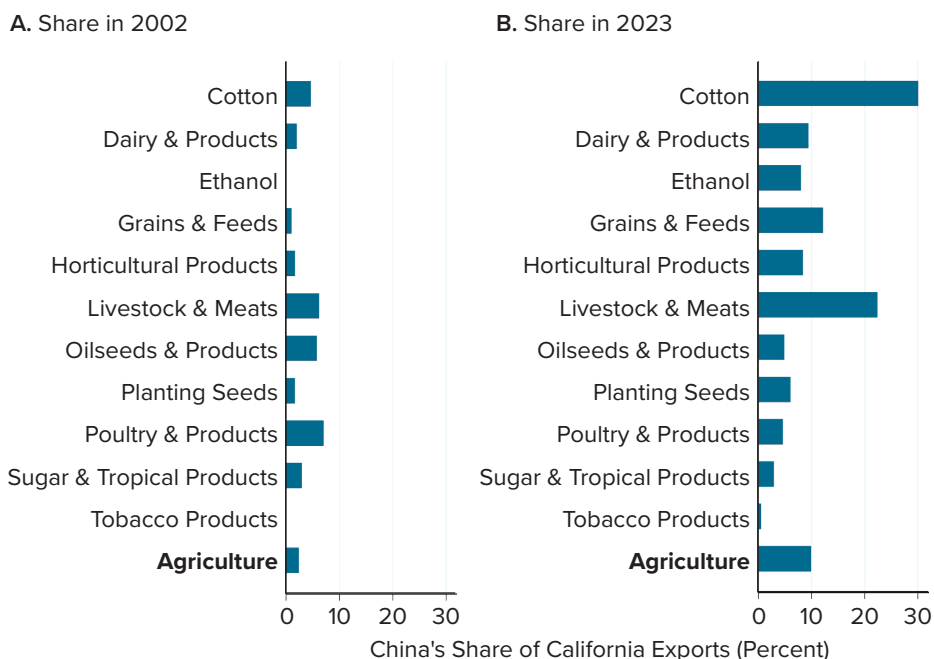
the almond-bearing acreage increased from 0.6 million in 2002 to 1.4 million in 2023. This period also saw sharp price increases for various export commodities, illustrated by the price of almonds, which increased from \$1.11 per pound in 2002 to \$4.00 per pound in 2014.

However, when the 2018/19 U.S.-China trade war broke out, trade retaliation resulted in declining export prices for various California cash crops. For instance, the price of almonds plummeted to \$1.40 per pound. Farmers in the midwestern United States were overcompensated with federal government subsidies to offset economic losses during the 2018/19 trade war, while California farmers were undercompensated.

Figure 1 shows that California's dependency on China as a market for agricultural products varies by product group. The figure plots China's share of California agricultural exports in 2002 versus 2023. As mentioned, the export dependency ratio has quadrupled from 2.4% to 9.9% since China's WTO accession. For certain product groups, the increase is significantly larger. For instance, about 8.4% of horticultural exports now go to China, a fivefold increase since 2002. The highest export dependencies are cotton (30.1%), livestock and meats (22.4%), and grains and feeds (12.2%).

While the 2018/19 trade war harmed California agriculture, certain sectors stand out as having experienced the brunt of the trade losses. Tree nut producers were among the most severely impacted. Previous economic studies found that California almond export losses in marketing years 2017/18 to 2021/22 exceeded \$755 million, leading to a considerable increase in U.S. almond inventories. This pattern from the previous trade war implies that the potential trade effects of PNTR removal are likely to be significant.

Figure 1. China's Share of California Agricultural Exports in 2002 versus 2023



Source: Authors' own calculations based on data from the U.S. Census Bureau (2024).

PNTR Removal Could Cost California Agriculture Dearly

Alternative proposals to revoking China’s PNTR status are being considered in Washington, D.C. Table 1 shows the average U.S. import tariff schedule with and without PNTR status. The leading proposal would elevate tariffs on all Chinese imports from the most-favored-nation rates (also known as column 1 rates) to higher column 2 rates of the U.S. Harmonized Tariff Schedule. The column 2 rates are exclusive to countries such as Cuba, North Korea, Russia, and Belarus. Cuba and North Korea face complete economic embargoes, while Russia and Belarus had their PNTR status withdrawn following the Russian invasion of Ukraine.

Implementing the PNTR revocation would raise the average import tariff on Chinese agricultural products by 9.5%—from 5.1% under column 1 to 14.6% under column 2. The impact on import tariffs for other non-agricultural sectors would be larger, with the average import tariff over all sectors going up from 3.9% to 32.5%. Horticultural products, dairy, livestock, and meats would experience steep increases in import tariffs. In addition to the proposal to remove PNTR status, and thus elevate U.S. import tariffs on all Chinese imports to the column 2 rates, another proposal was introduced during a recent debate by the Select Committee to establish a unique tariff regime for Chinese imports, necessitating regular Congressional approval. This outcome could be even worse for California agriculture.

To estimate the potential trade effects of removing China’s PNTR status, we assume a reciprocal and uniform ‘tit-for-tat’ trade response from China, which means that China would raise its import tariffs on inbound agricultural products by 9.5%. This assumption draws on the trade

Table 1. Potential Import Tariff Increases After PNTR Revocation

Product Groups	Column 1 Tariff Rate (%)	Column 2 Tariff Rate (%)
Cotton	0.8	0.8
Dairy & Products	6.9	17.3
Ethanol	1.9	20.0
Grains & Feeds	3.3	12.3
Horticultural Products	3.6	15.5
Livestock & Meats	2.1	11.4
Oilseeds & Products	8.8	17.9
Planting Seeds	0.1	0.4
Poultry & Products	0.7	3.0
Sugar & Tropical Products	3.5	11.8
Tobacco & Products	42.5	45.3
Agriculture	5.1	14.6
All Sectors	3.9	32.5

Source: Authors' own calculations based on 2023 tariff data from the U.S. International Trade Commission (2024).
Note: Column 1 rates reflect the most-favored-nation rates, while the higher column 2 rates reflect the U.S. Harmonized Tariff Schedule exclusive to countries such as Cuba, North Korea, Russia, and Belarus.

Table 2. Potential Impact of PNTR Revocation on California Agricultural Exports to China Based on 2023 Trade Flows

Product Groups	Trade Effects (Percent)		Export Value Effects (Millions of Dollars)	
	Lower Bound	Upper Bound	Lower Bound	Upper Bound
Cotton	-0.3	-0.4	-0.47	-0.57
Dairy & Products	-29.7	-36.4	-67.17	-82.23
Ethanol	-54.9	-67.2	-0.10	-0.12
Grains & Feeds	-28.4	-34.8	-82.99	-101.59
Horticultural Products	-37.3	-45.7	-527.59	-645.84
Livestock & Meats	-32.6	-39.9	-136.84	-167.52
Oilseeds & Products	-26.9	-32.9	-12.13	-14.85
Planting Seeds	-1.7	-2.1	-0.45	-0.55
Poultry & Products	-7.9	-9.7	-0.80	-0.98
Sugar & Tropical Products	-19.8	-24.2	-4.19	-5.13
Tobacco & Products	-16.4	-20.0	-0.01	-0.01
Agriculture	-28.4	-34.8	-832.74	-1,019.39

Source: Authors' own calculations based on column 1 and column 2 tariff data from the U.S. International Trade Commission (2024), 2023 California export data from the U.S. Census Bureau (2024), and retaliatory tariff data from the PRC Ministry of Finance (2024).

policy dynamics observed during the 2018/19 U.S.-China trade war, where China responded with equivalent tariff hikes on U.S. agricultural imports. Those retaliatory measures increased China’s agricultural import tariffs

by 19.1% in 2018/19. One previous Virginia Tech study estimated that these tariffs caused a 71% reduction in U.S. agricultural exports to China compared to their 2016/17 levels.

Another study by the USDA estimated a decline in U.S. agricultural exports to China from \$18.5 billion in crop year 2017/18 to \$7.8 billion in crop year 2018/19, marking a 58% decrease in export value. These figures provide a basis for our estimates in Table 2 (on page 3) of the potential consequences of China's response to the revocation of its PNTR status.

Table 2 shows the predicted trade effects (in value terms) of possible retaliation from China in response to PNTR removal. We assume China's new import tariffs would be equivalent to the higher U.S. tariffs they would face in the U.S. market, going up from column 1 to column 2 in Table 1. In Table 2, we show lower and upper bound estimates of trade losses based on the trade war tariff elasticities in the literature, which are -3.04 and -3.72, respectively. These elasticities measure how much trade values respond to a 1% increase in the ad valorem tariff rate. On average, California's agricultural export value to China would decline by 28.4% to 34.8% compared to a scenario without PNTR revocation. Based on 2023 California agricultural exports, this would result in trade losses between \$0.8 billion and almost \$1 billion, equal to about 4% of the value of the 2023 California agricultural shipments to all export destinations.

This impact may sound small, but in international agricultural markets, a relatively small change in trade volume can have significant price impacts. Interestingly, there are considerable differences between product groups, with horticultural products, livestock and meats, dairy, and grains and feeds facing the brunt of the potential trade damage. Over 60% of the trade losses would be concentrated on horticultural products. Producer groups that rely heavily on China, such as tree nuts, would see major impacts that could further exacerbate existing market challenges

caused by the lingering 2018/19 U.S.-China trade war, supply chain disruptions, and sluggish domestic demand.

Our estimates of trade losses are a lower bound of the potential economic impact caused by a 'tit-for-tat retaliation' scenario. For instance, U.S. almonds still face a 15% retaliatory tariff on top of the 10% most-favored-nation rate in the Chinese market. Pistachio exports from the United States to China face a 5% most-favored-nation tariff plus a 20% retaliatory tariff. These retaliatory tariffs are left over from the 2018/19 trade war and are called Section 232 retaliatory tariffs.

We believe our estimates are reasonable but may have a lower bound because we don't know how China would react to losing PNTR status. For instance, China might revoke the waiver for U.S. agricultural products granted in March 2020. These waivers nullified Section 301 retaliatory tariffs implemented in 2019 on top of Section 232 retaliatory tariffs. In the case of tree nuts, losing the Section 301 waiver would mean tariffs would increase by an additional 30%.

Conclusion

Since China joined the WTO over two decades ago, U.S. agricultural exports to China have surged. This market access was handed a significant setback in 2018/19, when the United States started a trade war that resulted in major trade retaliation by China. That trade war was a disaster from the U.S. perspective and resulted in lower farm prices, lost export opportunities, and job losses for California agriculture that continue to impact the industry.

The potential revocation of China's PNTR status and the associated implications of tariff escalations would further disrupt this trade relationship, risking substantial economic losses for California agriculture due

to reduced agricultural exports. This scenario underscores the need for informed trade policies that consider the complexities of international market dynamics and the essential role of trade relations in sustaining the vitality of California's agricultural economy. Once access to a market is lost, gaining it back is difficult, as the 2018/19 trade war has shown.

Suggested Citation:

Carter, Colin A. and Sandro Steinbach. 2024. "Revoking China's Preferred Trade Status Would Be Costly for California Agriculture." *ARE Update* 27(4): 1-4. University of California, Giannini Foundation of Agricultural Economics.

Authors' Bios

Colin A. Carter is a Distinguished Professor in the Department of Agricultural and Resource Economics at UC Davis. Sandro Steinbach is an associate professor in the Department of Agribusiness and Applied Economics and the Director of the Center for Agricultural Policy and Trade Studies at North Dakota State University. They can be reached at cacarter@ucdavis.edu and sandro.steinbach@ndsu.edu, respectively.

For additional information, the authors recommend:

Oxford Economics. 2023. "The Impact of China PNTR Repeal and Increased Tariffs on the U.S. Economy and American Jobs." A Report Prepared for the U.S.-China Business Council. Available at: <https://bit.ly/3xtkk6k>.

Carter, Colin A., Jiayi Dong, and Sandro Steinbach. 2020. "2018 Trade War, Mitigation Payments, and California Agriculture." *ARE Update* 24(2): 1-4. University of California Giannini Foundation of Agricultural Economics. Available at: <https://bit.ly/43SYGo0>.