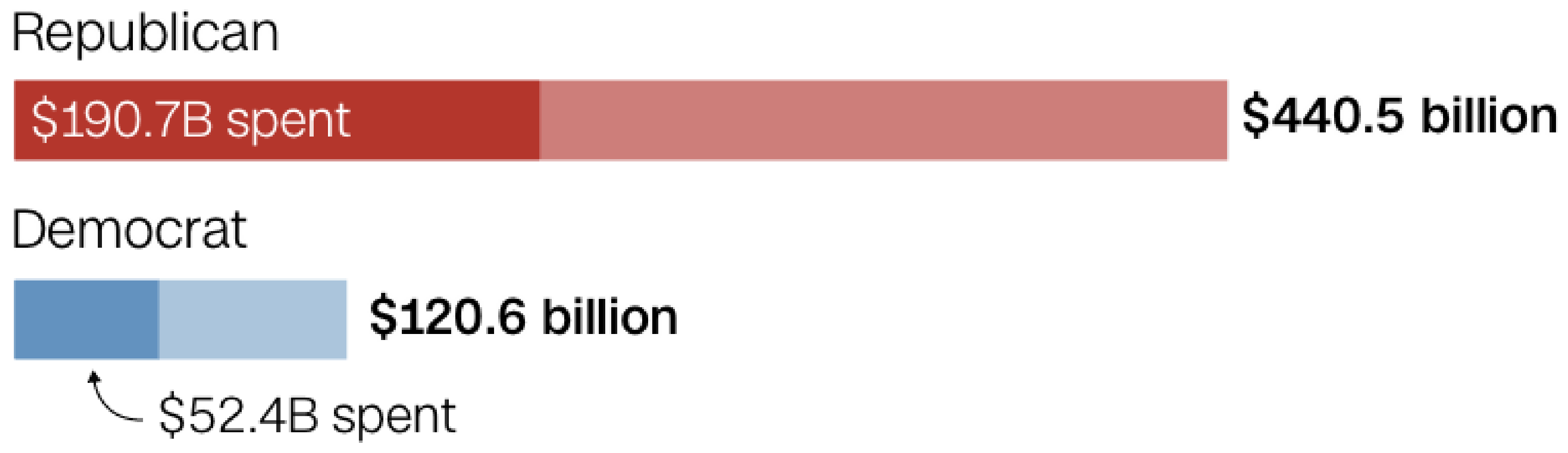
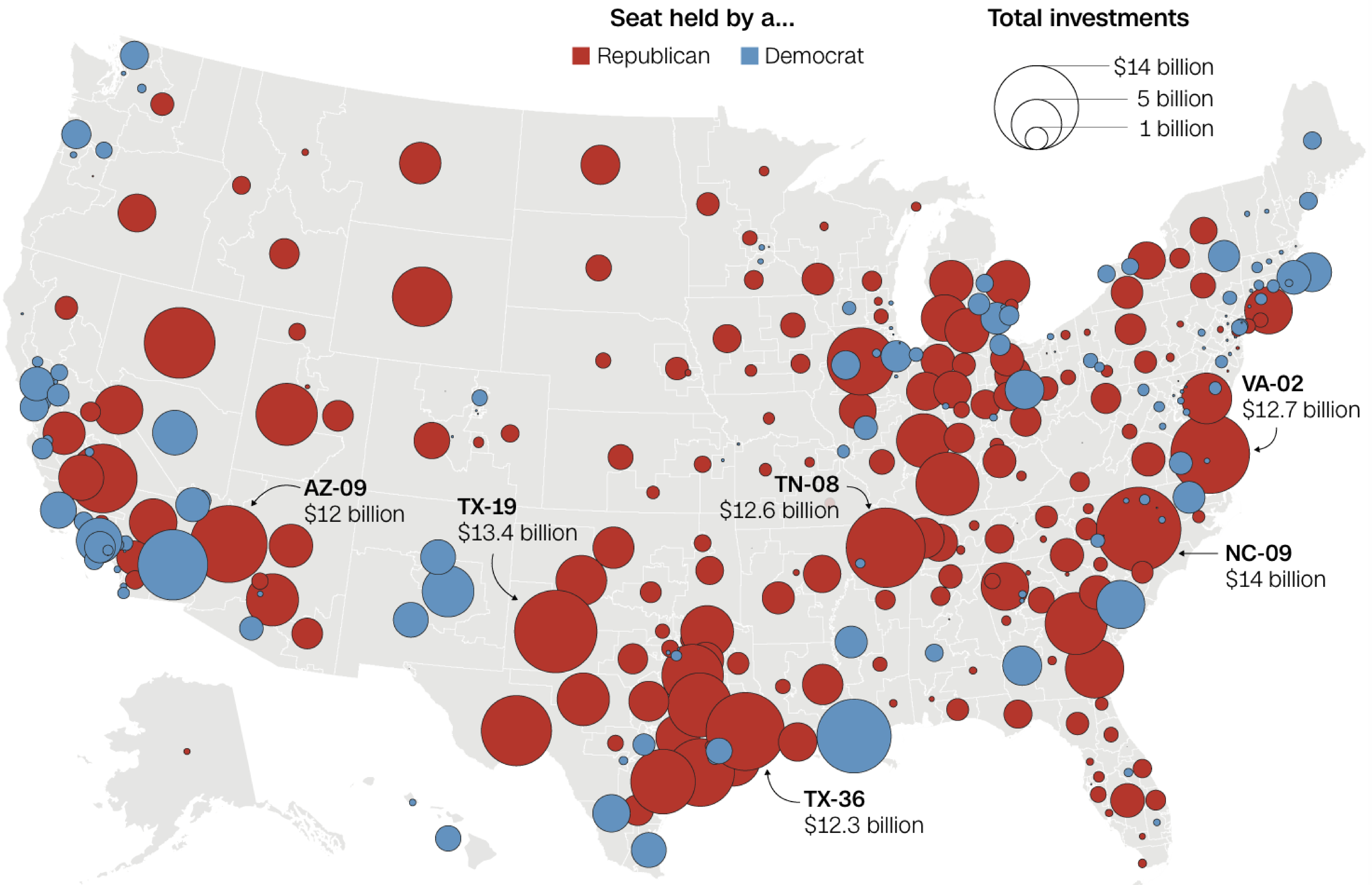
Industrial Policy and Trade Tensions

Jonas Nahm, January 2025

- The shortcomings of Biden’s industrial policy created pressures for tariffs
- Trump’s industrial policies will likely be tariffs but not all his tariffs are industrial policy.
- Industrial policies can benefit from trade, but institutional constraints make it hard to design them that way.



Announced investments by congressional district



FRED
Total Construction Spending: Manufacturing in the United States
240,000
200,000
160,000
120,000
80,000
40,000
0
Millions of Dollars
2004
2006
2008
2010
2012
2014
2016
2018
2020
2022
2024
2005
2010
2015
2020
Source: U.S. Census Bureau
fred.stlouisfed.org

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US industrial policy is not strategic

- Not based on existing strength
- IRA targets almost all clean tech technologies and supply chain segments
- Not all have a pathway to competitiveness

- To protect investments, demand for tariffs

US industrial policy not learning lessons from China

- Assumes that China's competitiveness is in all cases based on unfair government intervention, subsidies
- Infant industry argument applied universally, without temporal constraints
- No strategic emulation, catch up to Chinese strength

- To protect industries from unfair competition, demand for tariffs

No US discussion of industrial policy guardrails

- Makes discussions with China over industrial policies with negative spillovers for the global economy difficult to impossible
- Beggar-thy-neighbor policies have become the norm, here and elsewhere
- To protect industries from unfair competition, demand for tariffs

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- Tariffs are now the primary industrial policy tool of choice, as the incoming administration will try to undermine Biden’s industrial policy tool bills.
- Across-the-board tariffs are means of opening broad negotiations with other countries, including China. This is more about extracting overall concessions, some of which are not about economics (migration, drugs).

LEGO


FINLAND
SWEDEN
NORWAY
ARCTIC
OCEAN
ICELAND
UNITED
STATES
GREENLAND
(DEN.)
NUUK
CANADA
ATLANTIC
OCEAN

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- Impact of macro policy (strong dollar, higher-for-longer rates) will undermine domestic manufacturing, and create more incentives to rely on tariffs to protect domestic firms.

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It doesn’t have to be that way.

- Industrial policy can build on and amplify existing economic strengths. Such industrial policy to embrace trade can make firms more competitive, not protect them.

- This means targeted industrial policy to address specific market failures and economic frictions.
- This means temporary intervention until these market failures are resolved. But, hard to do politically -- how do you take things away?
- Finally, this means defining clear pathways to competitiveness for supported firms.

Institutional constraints get in the way

- United States: veto points, filibuster, budget reconciliation
- European Union: lack of taxation at EU level, fragmented responsibility
- China: subnational government incentives

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