EAST-WEST CENTER

ASIA PACIFIC BULLETIN

Number 714 | December 11, 2024

EastWestCenter.org/APB

The Economics of Revoking Permanent Normal Trade Relations (PNTR) for China

By Dr. Marcus Noland

The United States grants nearly every country in the world normal trade relations, née most favored nation, status. However, political pressure has been building to strip China of this treatment. Yet, recent modeling suggests that revoking permanent normal trade relations (PNTR) from China would not deliver economic benefits to the United States. Instead, it would have the opposite effect compared to what its proponents seek.

Dr. Marcus Noland, Non-Resident Senior Fellow at the East-West Center and a senior leader at Peterson Institute for International Economics, examines what revoking China's permanent normal trade relations (PNTR) status would mean for the US economy.

Starting in 1979, the United States moved China from Column 2 of the tariff schedule, the infamous Smoot-Hawley tariffs, to Column 1, most favored nation. Each year, Congress voted to maintain this status. In 2000, in connection to China's 2001 accession to the World Trade Organization (WTO), the United States granted China PNTR status, ending the practice of annual Congressional votes.

The reduction of uncertainty achieved by China entering the WTO and the United States granting PNTR led to significant growth in trade and investment. That expansion of trade and investment was associated with dislocation in import-competing sectors (the so-called China shock) and a rise in public disaffection.

These public concerns eventually manifested politically. In 2023 and 2024, bills were introduced in Congress to terminate PNTR. Republican presidential nominee Donald J. Trump embraced the elimination of PNTR and several related policies in his campaign. Of the 150 policy recommendations in the annual report of the bipartisan House Select Committee on the Strategic Competition between the United States and the Chinese Communist Party, the removal of PNTR led the list.

So, what would removing PNTR mean in reality? The default would be to put trade with China back in Column 2, the Smoot-Hawley tariffs. This change would mean a significant increase in the tariff, but one that would be felt unevenly across various sectors, with light manufacturing sectors such as apparel and footwear experiencing a 40-percentage point or more increase.

Returning China to Column 2 would not be Congress' only option. Some, including the House Select Committee, have floated the idea of raising the tariffs to levels short of Column 2 and then bargaining with China. Legislation has been introduced in both the House and Senate that would go even further, setting the tariff rate on specified products such as pharmaceuticals at 100 percent, effectively delinking the US and China from each other in specific sectors.

China would not stand pat. It could retaliate by imposing tariffs on US exports or targeting US firms with extensive operations in China, such as Apple.

Hogan, McKibbin, and Noland (2024) waded into this morass to try and determine the economic impact of PNTR revocation. They examined two scenarios: the first analyzed PNTR revocation independently, while the second incorporated in-kind retaliation by China. Each analysis used a global multi-country, multi-sector macro model, running the model out to 2040. With many Chinese imports

now under special protection, movement from Column 1 to Column 2 will overstate the marginal increase in protection with the removal of PNTR. The model assumes that the government absorbs the additional tariff revenue, implicitly paying down the debt. However, alternative assumptions, such as the revenue being returned to the public via tax cuts, would yield marginally different results. Thus, the results should be interpreted as indicative, not definitive. The medium-run results are summarized below.

Estimated Cumulative Impact on US Economy 2025-2028 (in billions 2018 USD)

	Revoking China's PNTR Status	Revoking China's PNTR Status plus Retaliation
GDP	-94.9	-158.7
Production		
Energy	-45.5	-40.7
Mining	-10.7	-11.5
Agriculture	-39.9	-70.1
Durable Manufacturing	-332.2	-532.2
Non-Durable Manufacturing	-89.9	-181.8
Services	-14.7	9.9
Percent Change in CPI by 2028	0.4	0.9

"...The rise in import prices caused by the increase in tariffs is partly offset by an appreciation of the dollar, but the dollar's increase in value depresses exports. As a result, both exports and imports decline. The increased cost of imported inputs and fall in exports depress investment and contributes to an overall economic slowdown."

According to the model, the rise in import prices caused by the increase in tariffs is partly offset by an appreciation of the dollar, but the dollar's increase in value depresses exports. As a result, both exports and imports decline. The increased cost of imported inputs and the fall in exports depress investment and contributes to an overall economic slowdown. As seen above, the revocation of PNTR reduces GDP and increases inflation, both of which are exacerbated by Chinese retaliation.

Highly trade-exposed sectors such as manufacturing and agriculture take the brunt of the slowdown. Employment declines in agriculture and industry and eventually migrates into services (via lower real wages). The geographic remoteness of some of these jobs in mining and agriculture from other centers of employment and possible skills mismatches means that this transformation may be less smooth than depicted in the model. Presumably, this is not the outcome that revocation proponents seek.

In relative terms, China is damaged more than the United States in these scenarios. The impact on third countries, particularly Mexico, is non-negligible. Over time, the manufacture of goods previously originating in China migrate to other countries such as Mexico and Vietnam, which are not separately broken out in the model. It is conceivable that if the increase of exports from Mexico to the United States were sufficiently large, the President or Congress might seek to tighten rules of origin under the USMCA, propagating the protectionist impact of PNTR revocation. Similar concerns apply to other third countries, such as Vietnam.

Proponents of revoking PNTR see it as a tool for promoting industrial revival. Ironically, the model reviewed suggests it would have the opposite effect.

Dr. Marcus Noland, Non-Resident Senior Fellow at the East-West Center and a senior leader at Peterson Institute for International Economics, can be contacted at mnoland@piie.com.

APB Series Founding Editor: Dr. Satu Limaye | APB Series Coordinator: Lance D. Jackson
The views expressed in this publication are those of the author and do not necessarily reflect the policy or position of the East-West Center or any organization with which the author is affiliated.

The East-West Center promotes better relations and understanding among the people and nations of the United States, Asia, and the Pacific through cooperative study, research, and dialogue. Established by the US Congress in 1960, the Center serves as a resource for information and analysis on critical issues of common concern, bringing people together to exchange views, build expertise, and develop policy options.

EWC Organizational