

## Article

The Scottish Whisky Association has said the planned U.S. tariffs on the spirit drink is disproportionate and will “undoubtedly damage” sales.

The U.S. has announced it will bring in a tariff of 25% on imports of single malt Scotch whisky and liqueurs from the U.K. The move follows a World Trade Organization (WTO) ruling that says the U.S. is entitled to recoup almost \$7.5 billion dollars a year via tariffs on EU imports.

The WTO decision was related to the accusation that several EU governments granted illegal subsidies to the plane maker Airbus as it looked to develop and sell planes. The WTO said the move had negatively impacted sales of U.S. made planes in the large and very large aircraft market.

“The tariff will undoubtedly damage the Scotch Whisky sector. The U.S. is our largest and most valuable single market, and over £1 billion of Scotch Whisky was exported there last year,” said Scottish Whisky Association chief executive Karen Betts, in a statement Thursday.

Several items from different European countries are being targeted but Betts said Scottish Whisky had come out of the decision particularly badly and would amount to \$460 million worth of tariffs annually.

“Despite the fact that this dispute is about aircraft subsidies, our sector has been hit hard, with Single Malt Scotch Whisky representing over half of the total value of U.K. products on the U.S. Government tariff list.”

Blended whisky is exempt from tariffs, meaning that Diageo’s popular Johnnie Walker brand is unaffected by U.S tariffs. Shares in Diageo, which also owns Smirnoff and Guinness, rose by nearly 1.5% in Thursday morning trade.

The USTR released a list Wednesday of products it plans to target from Oct. 18 onwards. The duties include:

- 10% tariffs on aircraft from France, Germany, Spain or the United Kingdom
- 25% duties on single-malt Irish and Scotch whiskies, various garments and blankets from the U.K.
- 25% tariffs on coffee and certain tools and machinery from Germany
- 25% duties on various cheeses, olive oil and frozen meat from Germany, Spain and the U.K.
- 25% tariffs on certain pork products, butter and yogurt from multiple countries

In 2018, the U.S. imported about \$488 billion in products from the EU while the U.S. sent about \$319 billion in goods to EU countries.

In its response to Wednesday’s decision, the U.K. government Department of Trade and Industry said: “resorting to tariffs is not in the interests of the U.K., EU or U.S.”

The U.K. government also claimed that the U.K. “and other Airbus nations” had taken steps to bring support for the plane maker into compliance.

It added that it had seen no effort by the United States to bring its support for Boeing into WTO compliance.

The WTO is expected to offer its ruling on the EU's subsidy case against Boeing in 2020.

## Analysis

The United States is imposing a 25% tariff on Scottish whisky. Tariffs are a tax imposed on imports which also causes a raise in government revenue. This is a protectionism measure — it protects domestic industries in the USA.

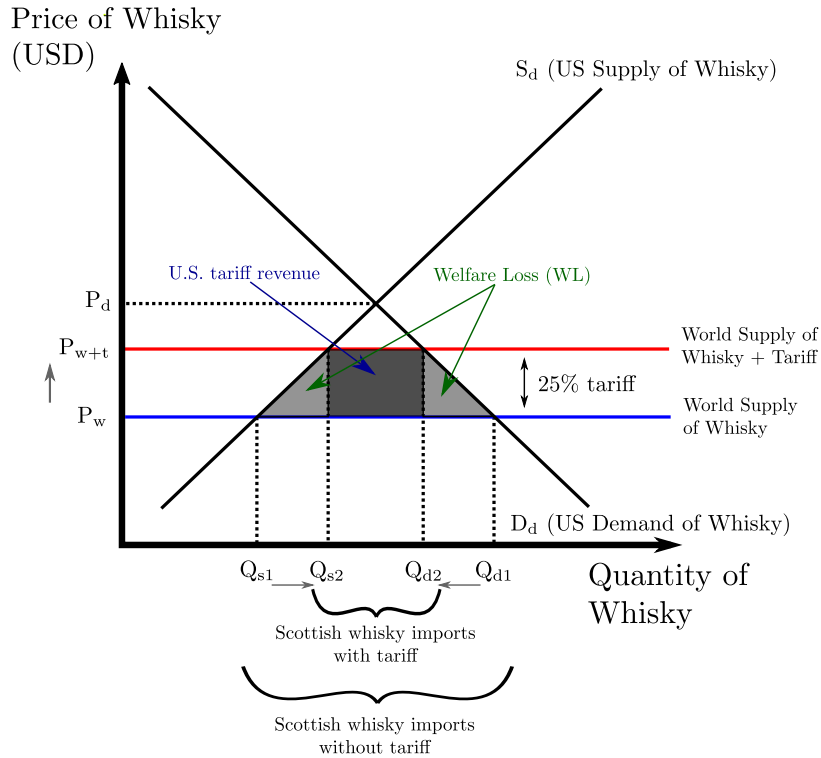


Figure 1: The impact of a tariff on the U.S. whisky market.

This tariff impacts the “£1 billion” annual market of the Scottish whisky sector and will “undoubtedly damage” this sector. In figure 1, we can see the effect this has on the U.S. economy. Scotland’s market price  $P_w$  is lower than the U.S. equilibrium price  $P_d$ , meaning that Scotland can produce at a lower price than the U.S and thus has a comparative advantage. At  $P_w$ , the domestic quantity supplied is  $Q_{s1}$  and the domestic quantity demanded is  $Q_{d1}$ , so  $(Q_{d1} - Q_{s1})$  represents the amount of imports prior to the tariff. However, due to the 25% tariff, the world price increases to  $P_{w+t}$ , causing an decrease in domestic quantity demanded from  $Q_{d1}$  to  $Q_{d2}$  and an increase in domestic quantity supplied from  $Q_{s1}$  to  $Q_{s2}$ .  $(Q_{d2} - Q_{s2})$  represents the amount of imports after the tariff was implemented.

The policy provides the U.S. government revenue of quantity of imports  $(Q_{d2} - Q_{s2})$  multiplied by the tariff per unit, however, causes a welfare loss WL due to an increase in inefficient domestic production.

The 25% tariff could be beneficial in protecting the U.S domestic economy. As imports are lower, the balance of trade improves, increasing aggregate demand in the U.S. economy. This causes an appreciation of the exchange rate, protecting domestic whisky producers. Additionally, the government also gets revenue from the tariff, allowing them to increase government expenditure to increase aggregate demand in the economy or improve the long run aggregate supply if these funds were directed towards education and healthcare. Moreover, because domestic producers sell a larger quantity of whisky, and that an increase in

output increases demand for labour, the unemployment rate decreases. The tariff could also decrease the risk of health and safety issues as the quantity of whisky imports that don't meet U.S. safety standards is lowered.

However, the tariff can also have a negative effect on the U.S. economy. The allocative inefficiency that the tariff causes by shifting production from efficient Scottish producers to inefficient U.S. producers leads to a welfare loss due to the misallocation of resources. If this continues, this could lead to a global misallocation of resources.

Furthermore, tariffs could worsen the distribution of income as they are a form of regressive taxation. This occurs because the percentage of the tariff on a consumer's income is higher for lower-income earners, which means that the tariff affects lower-income earners more than higher-income earners. The 25% tariff may also not have a significant impact on unemployment because the U.S. whisky industry is a niche market where workers need to be highly skilled, so the increase in output may not necessarily create a significant number of jobs.

In addition, the tariff lowers the level of overseas competition, so American whisky producers have less incentive to innovate, making U.S. whisky even less desirable in the global market if foreign producers continue to innovate. The tariff could lead to a trade war if the EU, which Scotland was a part of at the time, were to retaliate and implement increasingly strict protectionist measures. This would cause serious negative effects on the global economy, and would not be "in the interests of the U.K., EU or U.S."

One possible solution that the U.S. could implement instead of the tariff would be a subsidy. This would increase the competitiveness of American whisky producers on the global market as they are able to produce and sell at lower prices, boosting the domestic economy while retaining lower import prices at the same time. However, implementing a subsidy would have a very large opportunity cost for the U.S. government. As the subsidy would be paid for by the government, the government budget would need to be adjusted, and the money set aside for a whisky subsidy would be money not invested in healthcare, education or infrastructure, causing negative effects on the U.S. economy in the long run.

Ultimately, imposing a 25% tariff on Scottish whisky imports negatively affects customers. The U.S. could consider other policies such as a subsidy instead of a tariff, which reduces the risk of initiating trade wars, damaging foreign relations, and redistributing income regressively.

**Word Count:** 736