



GLOBALIZATION



By Klaus D. Oehler

President Trump has now shifted his attention to China, but Beijing is also going on the offensive. In response to US tariffs, China has imposed tariffs of between 15 and 25% on all US goods, including wine, pork and fruit. The tariffs will affect some 500 types of US imports. Beijing has also threatened further retaliation if Trump extends his tariffs to other Chinese tech imports. Whether these tariffs will go ahead is unclear. Tearing relations, many US industry and corporate groups warn against a fresh round of tariffs. With a total merchandise trade volume of \$410 billion, China was the US's most important trade partner in 2017. During that same year, however, China ran a record \$370 billion trade surplus with the US. Beijing has warned the Americans against launching a trade war. Speaking at a press conference on the last day of China's annual National

People's Congress, Premier Li Keqiang said, "We don't want to see a trade war. There will be no winner in a trade war."

This is not only China's view. Within the European Union, industry and politics are also worried about the prospect of a spiral of tariffs and counter-tariffs. On his visit to Washington, the German Economics Minister was joined by a number of his European colleagues. The EU governments agree that the problems of trade imbalances and unequal taxation must be solved jointly and in collaboration. Moreover, they do not dispute the existence of a trade imbalance. Germany has long been the focus of criticism in this respect. The global export champion has a large trade surplus. Nearly all key German industries have export quotas of well over 50%, and a large share of these exports flow to countries outside the European Union.

**Economic wars**

Germany's trade surplus depresses other countries of purchasing power and jobs. In a time when many Western economies are still struggling to emerge from the global finance crisis, politicians are naturally tempted to blame countries that boast a trade surplus for their own economic woes. As a result, protectionism has been on the rise for some years. Italy and France see themselves as victims of Germany's "internationalist" policies; the International Monetary Fund (IMF) believes that Germany's surpluses are one of the main sources of risk for the global economy.

For its part, German industry has repeatedly countered with the argument that its products are competitive on the global market and have a global reach.

Indeed, German automotive manufacturing, mechanical engineering and the chemical industry now account for as many jobs abroad as they do within Germany. German cars are popular in China. Chemicals giant BASF is the global market leader and German machinery and installations can also be found at every production site around the globe.

Nevertheless, trade imbalance is a legitimate topic of international negotiation and debate – but it must not take the form of a trade war. For example, the Americans have noted that the EU imposes a 25% import tar-

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iff on US bulk cars, while the US imposes only a 2.5% tariff on cars assembled in the EU. But, as the EU Commission has noted, in other areas the tariffs skew in the opposite direction. On average, the EU levies tariffs of 7% on US imports, while the average US tariff is 2.4%. For this reason, the EU believes that it should be possible to reach an amicable agreement with the US. French Economics Minister Bruno Le Maire has made it clear to US Treasury Secretary Steven Mnuchin that Europe is "waiting for a full exemption from these new American tariffs for the European Union as a whole." This goal, he said, is "difficult, but not out of reach."

**Potential countermeasures**

Nevertheless, the European Union has been laying the groundwork for potential countermeasures. The European Commission has proposed

new measures to tax large digital firms – a move that would have a major impact on US giants such as Google and Facebook. The proposals are targeted at profits made through activities such as selling user-generated data. For some time now, the Commission as well as individual Member States have been demanding fair taxation of these profits by moving to a system in which taxation is based on where the users are located, rather than where the companies are headquartered. Most digital giants are not headquartered in the countries in which they operate, and thus pay minimal taxes within the EU. The Commission has put forward two proposals. As an interim solution, Brussels wants to introduce a 2% tax on digital companies with total annual worldwide revenues of €750 million and EU revenues of €50 million. The tax would apply to revenues resulting from user activities in the broad sense of the term, including revenues achieved from online advertising.

Intermediary activities that facilitate the sale of goods and services, and the sale of data generated by user-provided information. Tax revenues would be collected by the Member States, based on the number of users in each country. The EU Commission emphasizes that this proposal would only tax revenues that until now have not been subject to tax.

Experts say the US government could also explore new approaches to making Trump's "America First" campaign slogan a reality. Much of the computer giant Apple's hardware is made in China. Google's software is maintained in India,

and so forth. This is the point at which the European Commission's new strategy is taking aim. The Commission wants to introduce the principle of a "digital presence" or virtual permanent establishment whereby profits would be taxed in the territory where they are generated. Reforms are urgently needed – currently, digital companies pay on average an effective tax rate of 2.4% within the EU, compared to 21.2% for traditional businesses. Social media behemoth Facebook had a turnover of \$260 billion last year, while Google's turnover was more than double. Although much of this revenue is generated from users in the European Union, these digital firms pay only minimal tax within the EU. This fact alone is further proof that there would be no winners in a trade war.

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**THE SPUDY COLUMN**

**Investing in Israel**

Private equity investments are an interesting asset class, especially for investors with long-term investment horizons, such as family portfolios. Such investments provide a better risk-return profile for the portfolio and generate higher average returns than shares, while displaying lower volatility. Through direct participation in innovative startups, investors may take part in the development of interesting fields such as medicine technology or digitization. In recent years, Israel has developed into an incubator for young and innovative companies with enormous potential in these exciting areas.

This success is no accident. In Israel, many university graduates prefer to grow their own ideas in their own companies, make their own decisions and assume responsibility rather than seeking a position in a large company and join an existing hierarchy. The formation of startups is also aided by the connections formed by young people with their peers during compulsory military service. Strong



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peer networks of young people with similar interests facilitate the founding of new companies. And, of course, Israel's exemplary

investment in research and development also plays a role. As a result, international investors are increasingly focusing on Israel's innovative potential. One recent example is the German automotive supplier Continental's takeover of the Israeli company Argus. Last year, Continental purchased the Israeli cybersecurity startup for an estimated price of over €300 million, with the aim of developing technologies for use in self-driving cars. For private equity investors who get in on the ground floor, such trajectories can prove especially lucrative.

At the same time, however, investors must accept that their capital will have limited fungibility. The investment risk is also higher, and in a worst-case scenario an entire investment could be lost. In many cases, potential investors also face an information gap when it comes to decision-making. For this reason, potential investors should remember that success in this area requires professional and systematic selection of investment options, as well as market knowledge and experience. Most importantly, they require independent advice and investment management, to include not only investment controlling but careful attention to tax and legal aspects.

Jens Spudy is executive partner of Spudy Family Office