Macro research

Reflections

Friday, March 9, 2018

Trump's tariffs – more domestic politics than foreign policy

World trade growth is currently in an acceleration phase. During the past 15-20 years, globalisation has narrowed the economic gaps between countries. Growing protectionism and de-globalisation would isolate economies and cause efficiency losses in the world economy. The trade barriers now being enacted by the United States are ominous signs. They have a lot to do with American domestic politics ahead of next autumn's midterm elections. **But viewed in a larger perspective, the trade barriers announced so far pose no serious threat to economic growth in the US, Europe and the rest of the world**. Instead, the huge US fiscal stimulus – and major US dollar movements – will play a bigger role for growth, inflation and monetary policy. Yet it will be important to long-term stability in the global financial and monetary system if the US manages to shrink its current account deficits and its big foreign debt (net international investment position or NIIP), which totals about 40 per cent of GDP.

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Trump's tariffs unfortunate but manageable

President Donald Trump's decision to impose tariffs on imported steel and aluminium – and countermeasures by other countries and trade blocs – are **unfortunate and will cause uncertainty** for companies that work both domestically and as part of global production chains. Citing "national security" in order to get around World Trade Organisation (WTO) rules, as the US is now doing, is of course a clear exaggeration. But these tariffs are currently **not expected to decisively change the GDP growth and inflation outlook**. Steel and aluminium account for only 2 per cent of total US imports. Higher import prices will thus barely affect the Federal Reserve's key interest rate hiking strategy: SEB is sticking to its forecast of four rate hikes in 2018 to 2.50 per cent and one in 2019.

Instead, Trump's **pro-cyclical tax cuts** of USD 1.5 trillion and yearly **federal spending hikes** of 0.4 per cent of GDP in 2018 and 2019 (totalling USD 300 billion) will have more impact on growth and inflation. All else being equal, this fiscal stimulus will contribute to higher US imports of consumer and investment goods, lifting global GDP by 0.2 percentage points. Steel tariffs are a way of **decreasing US import leakage** and trying to ensure that the effects of the tax reform and other measures stay inside the US, but the proposed tariffs are expected to have very little impact on import leakage.

The major **US dollar** exchange rate movements of recent years will have a larger and broader impact on the US and global economies than Trump's proposed tariffs. Between autumn 2011 and the end of 2016, **the dollar appreciated by nearly 30 per cent** in effective terms. During 2017 and to date, the USD has instead **lost nearly 10 per cent of its value**. Our forecast is that **the dollar will depreciate by another 6 per cent** over the next two years – despite Fed rate hikes – in what may be regarded as a normalisation of earlier excessive appreciation, which may ease global imbalances.

US net foreign debt moving in wrong direction

The US **current account deficit** is expected to total 530 billion dollars this year, or about **2.5 per cent of GDP**; the deficit has thus more than halved in the past decade. During the same period, the country's **net international investment position (NIIP) has climbed from USD 1 trillion to USD 8 trillion, or nearly 40 per cent of GDP**. This heavy foreign debt reflects persistent deficits in US financial savings (the current account balance). NIIP has thus surpassed the critical 35 per cent level, which risks exposing the country to funding difficulties due to credibility problems.

It is thus in the best interest of the international community to avoid further increases in such imbalances. This may also explain why – at their Hamburg summit in July 2017 – the G20 heads of state and government accepted US "demands" that their communiqué should state that not all countries had yet benefited sufficiently from international trade. It is also obvious from the communiqué of its September 2016 summit in Hangzhou that the G20 has failed to reduce global excess capacity in steel production. World trade growth has accelerated during the past year and global economic growth is unusually synchronised; such conditions are normally not fertile ground for protectionism. The globalisation of the past 15-20 years has obviously narrowed economic inequality between countries but widened it in some advanced economies. This can trigger populism, raising the risk of more widespread trade war.

Fulfilling a campaign promise – but jeopardising trade

Our main scenario is that **countermeasures by other countries will be viewed as moderate and responsible enough not to trigger further US tariffs**, despite heated rhetoric. There are many indications that Trump's decision is a tactical move ahead of the November 6 US midterm elections largely aimed at appeasing swing voters in rustbelt states, which raises the risk of further initiatives. There is also strong resistance to trade wars among high-level Republicans, though US laws give the president great powers on international trade matters without congressional approval.