



Trump May Have China On The Mind With Brazil, Argentina Tariffs

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Steel and aluminum tariffs on Brazilian and Argentinian products will go back in place in America. President Donald Trump announced the decision almost a week ago in a series of tweets accusing both countries of devaluing their currencies and hurting American farmers. Trump also implored the Fed to cut rates in hopes of weakening the dollar against other currencies.

The tariff announcement is quite odd because the U.S. enjoys a trade surplus with both countries. The Office of the U.S. Trade Representative reported an \$11.6B trade surplus with Argentina last year while America's trade surplus with Brazil was \$30.6B. One would expect Trump to be quite gleeful on the statistics given his propensity to desire trade surpluses over deficits. Not this time, apparently, and it appears the President is quite irked over U.S. investment in the South American countries. Especially since Brazil is the 13th largest trading partner with the U.S.

Something about this announcement smells because it seems so indiscriminate. Neither country has a very strong economy. Brazilian officials had to brush off worries about their debt which was reported last week at 3% of the gross domestic product. Brazilian Economy Minister Paulo Guedes told reporters over a week ago the currency drop was due to lowering interest rates. Guedes was also in Washington last month for talks with Treasury Secretary Steven Mnuchin who praised the "important economic and trade relationship" between the two countries and how they can work closer together.

Argentina's bonds are in junk status and voters decided in October it was time to turn back to former populist, semi-socialist, and rumored to be corrupt president, Cristina Fernández de Kirchner for help following a massive economic slowdown under the previous administration. CFK will be *vice* president with former chief of staff, Alberto Fernandez, as president. They'll be sworn in on Tuesday. However, America and Argentina signed an agreement barely over a year ago which was supposed to increase trade opportunities for both countries. The U.S. also worked with Argentina over Venezuela over the summer.

There are two hypotheses in Washington on what influenced the President's thinking following a talk with Simon Lester from Cato Institute.

“The one theory is that Brazil and Argentina have been sort of big training partners with China and, to some extent, are supplying China with products that they used to get from the United States but aren’t now because of the tariff wars,” Lester told me over the phone shortly after the tariffs were announced. “So, this is to sort of make Brazil and Argentina take sides. Tell them, ‘Hey you’re either with China or with us. Pick one. You can’t have it both ways.’”

The theory makes sense, especially when one looks at the announcement from a nationalistic sense. China currently buys most of its soybeans from Brazil, and Chinese firms spent \$54B last year for a variety of projects. Beijing also touted its newly forged relationship with Argentina about a year ago including promises of cooperation on goods and services. Axios reported last Monday Trump wants China to say it will buy a ton of U.S. agricultural goods, meaning the money would go directly to America instead of the smaller countries. Pulling Brazil and Argentina closer to D.C. means China is forced to rely on bigger deals with America. There are indeed pacts with other economies (see the pending trade deal between China, Japan, Australia, South Korea, and other Asian-Pacific countries) but it could be Trump wants China to deal with America first before turning to other Western Hemisphere countries.

The biggest problem with this line of thinking is it only encourages more central planning and government-run (or propped up) industries both in the U.S. and abroad. Let’s not forget Trump’s bailout to farmers due to the tariffs. Brazil and Argentina have their own ‘incentive programs’ aka corporate welfare for companies. This almost mercantilist line of thinking only helps preferential businesses instead of giving everyone the chance at increasing wealth through free trade and no barriers. The trickle-down effect is simply more cronyism and encouraging businesses to hire lobbyists to get an ‘in’ with the government. Not the way a supposedly free-market country wants to go.

The other issue is the fact foreign companies aren’t paying for the tariffs. The New York Fed already published a study looking at the fact Chinese companies aren’t lowering prices on exports to America and just letting U.S. consumers cover the extra tax. This raises costs and leaves Americans with less money in their pockets. Which they could then use on other things or save it for later.

Speaking of the Fed, they fall into the second possibly going through Washington on the new tariffs because Trump mentioned currency manipulation.

“You know, he’s worried about all these other countries,” Lester opined to me. “They are lowering interest rates and, in the process, lowering the value of their currencies and, in his view, that puts us at a disadvantage. And so, the message here is really more towards the Fed that, ‘Hey, look at what these other countries are doing. We need to lower interest rates,’ and so he’s constantly making that case.”

Another economist I shared emails with suggested there might be a forthcoming Treasury Department report on Argentina and Brazil’s currency versus America’s.

This theory makes some sense because Brazil’s currency fluctuations were part of the discussion during their finance minister’s meeting with Mnuchin around Thanksgiving. However, it seems

like an odd decision to make these accusations against two countries that tend to work with the U.S. on a multitude of issues. Trump's anger with the Fed is well known but it's not known if the latter will respond to the president's demands. The Fed is expected to meet this week although AFP reported interest rates are expected to stay the same which means they'll buck the President again. One has to wonder what the reaction from Trump will be if interest rates remain level. Another Twitter rant more than likely.

The foreign policy angle is probably the most likely reason for Trump's tariff announcement, and one must expect the situation to stay turgid. It's more than likely Trump's tariff announcement on Brazil and Argentina will come to nothing unless either decides to be as uninterested in the President's demands as the Fed. Brazil will be most likely to acquiesce to Trump as Brazil President Jair Bolsonaro's politics are similar to Trump's. Argentina will be more interesting due to the recent electoral change. The only question is whether the Argentines will be more willing to cozy up to China more due to politics than listen to the White House. So much for free markets, one way or the other.