



Trump's Trade Wars Are Getting Worse (QQQ)

July 3, 2018

This past week, unfortunately, was no exception. In [my mid-year outlook](#), I mentioned that my outlook is predicated on the trade situation not worsening materially — so it's important that we closely follow trade developments. Last week, there were six trade developments that are helping to place downward pressure on stocks:

Key trade developments

1. It was reported June 29 that the US is considering leaving the World Trade Organization (WTO).¹ President Donald Trump's administration has reportedly drafted a bill that would enable the US to abandon its commitment to adhere to the rules of the WTO, and would also allow the Trump administration to unilaterally apply tariffs without the consent of Congress. It seems very unlikely that this bill would gain any traction in Congress, but the idea that a US administration would want to undermine the WTO is of grave concern. In a 2010 Cato Institute commentary titled "Americans Reaping Benefits of US Membership in WTO,"² it was explained that "A global rule of law for trade is one of the huge advantages we enjoy today compared with the 1930s, when the race to raise trade barriers was unchecked by either economic sense or international agreements." The commentary explained that the WTO has enabled the US to "remove barriers to the sale of US semiconductors in China, beef and rice in Mexico, genetically modified crops in the European Union, apples in Japan, milk in Canada, 2,700 specific product categories in India (including high-technology products, petrochemicals, textiles, and agricultural products), and copyrighted sound recordings in Japan." And it could be a useful tool today for the administration to address the legitimate issues it has around free trade and intellectual property violations. In my view, an interest in walking away from the WTO suggests a desire to return to the protectionist turmoil of the 1930s.
2. US motorcycle maker Harley Davidson announced it would be moving some of its motorcycle production – and therefore jobs — from the US to the European Union (EU) to avoid tariffs that were applied by the EU in retaliation for US tariffs.³ This was followed by an announcement from recreational vehicle manufacturer Polaris that it too was considering moving some of its motorcycle production to Poland for the same reason.⁴ These decisions confirmed my belief that economies will be hurt more than they are helped by protectionist policies.
3. On July 1, retaliatory tariffs that the Canadian government had previously announced on US\$12.6 billion in US goods went into effect.⁵ The tariffs are being applied to specific US products including steel, iron, and a number of household goods such as jam and ketchup.
4. On June 29, the Japanese government submitted a report to the US Department of Commerce warning that higher US tariffs on imported autos could hurt the US economy by reducing US

jobs — and that these tariffs could also hurt the global economy.⁶ Recall that Japanese and European automakers have invested significantly in production facilities in the US that employ many Americans. It is expected that this investment would be halted and even reversed if tariffs are applied by the US to imported autos and auto parts. This report cited a study by the Peterson Institute for International Economics that estimates that more than 600,000 Americans could lose their jobs in the US if a 25% tariff were applied to automobiles and auto parts, and other countries took retaliatory actions.

5. US automaker General Motors also submitted a report to the US Department of Commerce warning that if tariffs of up to 25% on automobiles and auto parts were applied, it could increase individual auto prices by thousands of dollars, hurting consumers and creating demand destruction.⁷ GM also asserted that “Increased import tariffs could lead to a smaller GM, a reduced presence at home and abroad for this iconic American company, and risk less — not more — US jobs.”

6. It appears that Andres Manuel Lopez Obrador, nicknamed AMLO, has won the election to be the next president of Mexico. AMLO ran on a left-wing populist platform that included standing up to the US on issues such as trade, and he has been described as a “Mexican Donald Trump.” I believe his election increases the likelihood that the North American Free Trade Agreement (NAFTA) will be dissolved, although I wouldn’t be surprised to see Mexico form a closer trade relationship with Canada.

Key takeaway

In short, protectionist actions threaten to counter the positive effects of last year’s tax reform legislation in the US — and negatively impact global growth. From my perspective, some of the scariest words in the English language this past year were that trade wars are good and easy to win. Not surprisingly, markets are getting spooked. I expect this market environment to continue until there’s a dialing down of trade rhetoric and actions.

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1 Source: Fortune, “Trump Said to Seek U.S. Withdrawal From the World Trade Organization,” June 29, 2018

2 Source: Daniel Griswold, Cato Institute, January 2010

3 Source: The New York Times, “Harley-Davidson, Blaming E.U. Tariffs, Will Move Some Production Out of U.S.,” June 25, 2018

4 Source, Minneapolis/St. Paul Business Journal, “Polaris motorcycles may follow Harley-Davidson out of U.S. to beat tariffs,” June 26, 2018

5 Source: CNBCTV18, “July 2: Here are 10 things you should know before the opening bell,” July 2, 2018

6 Source: USA Today, “Japan to US: Any new auto tariffs would damage US, world economy,” June 29, 2018

7 Source: Financial Times, “General Motors sounds warning on Trump tariff plans,” June 29, 2018

Important information

The opinions referenced above are those of Kristina Hooper as of **July 2, 2018**. These comments should not be construed as recommendations, but as an illustration of broader themes. Forward-looking statements are not guarantees of future results. They involve risks, uncertainties and assumptions; there can be no assurance that actual results will not differ materially from expectations.