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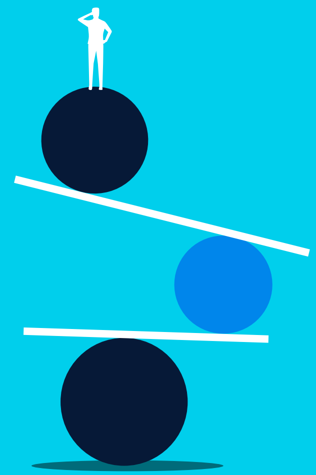

Trump’s tariffs: More detail, less certainty

In the Loop

Key Insights

- Despite Trump’s tariff unveiling, we are closer to the beginning of trade-related uncertainty than to the end.
- The administration’s focus on trade deficits, as opposed to trade barriers, suggests that the tariff regime could prove to be more durable.
- Economic and political pain eventually could lead to some tariff relief, but a return to normal seems unlikely.

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Now that we’ve had a few days to absorb the impact of President Trump’s Liberation Day tariffs announced on April 2, questions have quickly shifted to the durability of the tariff regime.

Unfortunately, even with the specifics finally out in the open, we appear to be closer to the beginning of trade uncertainty than to the end.

Why the uncertainty is here to stay

The rollout made clear that the tariffs are not about trade barriers, but are about trade deficits.

The U.S. administration appears to view trade deficits as prima-facie evidence of trade barriers and foul play. This supports a bit more durability because the vast majority of trade deficits will not—or cannot—be negotiated away. It is unlikely that the U.S. will ever run a balanced trade with Vietnam, for example, and no negotiation or removal of trade barriers will change that. It will take time to see a framework change from the administration.

Peter Navarro, President Trump’s trade adviser and one of the main forces behind the policy, has repeatedly said: “This isn’t a negotiation; it’s a national emergency.” Again, this raises the bar for the administration to change its mind and begin to reverse course.

The president’s announcement also explicitly excluded copper, pharmaceuticals, semiconductors, and lumber, which suggests that future tariffs for those products are likely. If the administration’s recent levies on steel and aluminum are any indication, these sector-focused tariffs could extend to the value of non-U.S. content in finished products, such as consumer electronics.

What’s next?

We believe the administration could eventually change course because of the long-term political unsustainability of these policies.

The market has already strongly signaled that the economy will weaken while inflation mechanically increases.

Given the difficulty of cutting interest rates when prices are rising, we do not expect to see monetary policy relief for a while. However, there is likely to be increasing pressure on Federal Reserve Chair Jerome Powell from the White House, to which markets may not respond well.

Falling asset prices, higher unemployment, and higher inflation are a politically untenable combination, but things will probably have to get (much) worse before they can get (a little) better.

We believe we could see some deals start to trickle in. Reaching an agreement with Australia, with which the U.S. has a small trade surplus, and smaller trading partners could be relatively easy. However, negotiations with larger economies, such as China and the European Union, could prove more difficult, with the potential for headline risk along the way.

When tariffs come down from an effective tariff rate of 25% to 30%, our view is that we will not see a return to normal. A reduction to a 10% or 15% effective tariff rate, for example, would still be 5x what it was before.

Moreover, every business and economic decision made going forward will occur under the shadow of the April 2 tariff announcement. Companies will likely factor in that they can no longer produce all their goods outside the U.S.

What could expanded tariffs mean for fiscal policy?

Technically, tariffs cannot be counted as revenue in the budget reconciliation process because they are not legislated. However, the administration and congressional Republicans can point to potential tariff proceeds and efforts to cut government spending as ways to help pay for extending the tax cuts from Trump's first term in office. It will be worth monitoring whether this narrative coverage is sufficient to support additional fiscal stimulus.

Bottom line: The potential for trade-related risks and market volatility is likely to remain elevated.

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