Trump targets China with new tariffs announced

The Trump administration announced further tariffs on March 22nd, this time targeted specifically at China. President Trump announced the tariffs after blaming China for a significant decline in its manufacturing sector and a loss of American jobs. The proposed tariffs target sectors such as robotics, aerospace, maritime and modern rail equipment as well as electric vehicles, in a move that could escalate tensions with China. The renewed focus comes as U.S. Trade Representative Robert Lighthizer, Commerce Secretary Wilbur Ross and Peter Navarro, who was recently promoted to "assistant to the president" are the driving force behind the renewed focus on the bilateral trade deficit with China. The U.S. trade deficit with China rose to US$375 billion in 2017, which represents 47% of America's overall trade deficit1.

Trump will instruct Robert Lighthizer, to levy a proposed 25% tariff on approximately US$50-$60 billion in Chinese imports, which amounts to about US$12.5-$15 billion (25% of US$50-$60 billion). Trump will also impose new investment restrictions on Chinese companies within 60 days that will serve to block Chinese investment in similar strategic sectors. Following the ratification of the executive memo, Lighthizer will have 15 days to produce a list of proposed products that will face higher tariffs, targeting 10 strategic sectors identified by Beijing as part of a "Made in China 2025" strategic plan. The moves come after a seven-month investigation by the U.S. Trade Representative into allegations that China violates U.S. intellectual property under a rarely used section 301 of the 1974 Trade Act. Prior to tariffs becoming final, there will be a 30-day comment period.

The move by the U.S. administration had conjured fears over a global trade war and could undermine a broad global economic recovery that is well underway. However, China's initial response to the tariffs has been fairly minimal thus far as the Chinese government announced tariffs on only US$3 billion of U.S. exports to China. Business groups in the U.S. have warned that tariffs could raise prices for U.S. consumers in the U.S. and negatively impact financial markets. At this stage, inflation and output are unlikely to be materially impacted by the tariffs announced by both countries, though this could change as the situation continues to unfold and further trade and/or financial market restrictions are potentially announced. Financial markets on the other hand have fallen precipitously on the news.

The announcement by the U.S. administration follows tariffs that were imposed on steel and aluminum at the beginning of March, which had certain exemptions, including for Canada and Mexico. The U.S. administration has since expanded that list, which now includes the European Union and Brazil in an effort to build a trade coalition against China on several fronts.

China's reaction

In an effort to stem the looming U.S. tariffs announcement, Premier Li Keqiang stated earlier in the week that the nation will continue to open its economy, including the manufacturing sector, and pledged to further lower import tariffs and cut taxes. In opening the manufacturing sector further, China would not force foreign companies to transfer technology to domestic companies and affirmed that intellectual property would be protected. However, closer to Trump's announcement, China's Ministry of Commerce cautioned that a trade war can be "detrimental to both sides" and that "China will certainly take all necessary measures to resolutely defend its legitimate rights and interests". China may decide to place tariffs on or even divert large orders for aircraft and other goods away from U.S. manufacturers, slow the process of obtaining operating licenses or could target U.S. companies with antitrust investigations. It could also drop foreign-ownership limits on Chinese brokerages and insurers, something that the U.S. has requested of China in the past for gaining greater access to its financial markets. In the end, the U.S. maintains significant leverage as the ultimate buyer of goods, which Trump continues to use to America's advantage. This is partly evident in China's rather muted response to date and could limit any further retaliation on future tariffs, restrictions or perhaps even the divestment of U.S. Treasuries.

Conclusion

As Trump continues to deliver on his campaign promises and appeal to his base as mid-term elections approach, trade protectionism continues to remain front and centre. Markets have responded negatively to the announcement and volatility is likely to continue as uncertainty lingers. We continue to monitor the reaction of China and other U.S. trading partners and how that will impact the global economic expansion and potential for further market disruption, though we believe that any market dislocations can provide great potential opportunities for investors.

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