Trade Protectionism

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After spending 2017 focusing on pro-growth policies (tax reform, deregulation), President Trump has shifted his tune in 2018 and appears to be making good on his campaign promises to rebalance global trade in America's favor.

Notably, President Trump announced his plans to impose $50 billion/year in tariffs on US imports from China – aimed at sectors where China is looking to take the global lead (including technology, aerospace, and machinery).

The direct impact of Trump's tariff announcement is actually quite small – and only impacts 2.5% of Chinese annual exports.

In response, China has announced plans for reciprocal tariffs on 128 products amounting to approximately $3 billion on US imports (including pork, recycled aluminum, steel pipes, fruit, and wine).

On a somewhat brighter note, the US administration has announced exemptions on steel/aluminum tariffs from a number of countries - including Europe, Australia, Argentina, Brazil, South Korea, Canada, and Mexico (in the clearest signal yet that the US is targeting China).

POLITICAL "NOISE" AT ODDS WITH SOUND FUNDAMENTAL BACKDROP

While escalating trade tensions between the US and China could potentially undermine synchronized global expansion, we continue to believe that the newly-announced tariffs from the Trump administration and the corresponding retaliatory measures from China are essentially a negotiating tactic.

As China has the most to lose in the event of further escalation, our view is that officials would prefer to diffuse tensions rather than instigate a full-blown trade war – and suggests a preference for a relatively restrained response from China.

Indeed, China's retaliation has been fairly measured thus far (amounting to only $3 billion of imports) and stopped short of including agricultural products (which would arguably create a bigger blowback).

As such, China's more tempered response suggests that while Beijing will not stand by idly and do nothing, officials likely do not want to act so aggressively as to put the global trading system at risk.

Furthermore, as the negative ramifications of a full-blown trade war would be in no-one's best interests, we have reason to believe that the US/China proposals will end up being watered down after a period of negotiations. This could simply be another example of President Trump announcing headline-grabbing policies only to scale them back shortly thereafter (case in point: 70% of steel/aluminum imports have now been exempted from the new tariffs, while the US is also making some important concessions on NAFTA). Is Trump's bark worse than his bite?

Another reason to believe that cooler heads will prevail and why a full-blown trade war is not our most likely scenario over the coming year is that Trump is a big advocate of stronger growth (higher stock markets) – and will ultimately choose the economy over a global trade war, in our view.

That said, somewhat alarming is the recent turnover at the White House – and the ascendency of an increasingly protectionist administration that's more anchored towards "America First" policies – which is likely to continue weighing on sentiment in the near term.

These latest trade disputes are creating a lot of noise and our expectation is that they will be felt more in the markets rather than the actual economy. While we expect the sound fundamental backdrop to outweigh these trade tensions longer-term, volatility and investor anxiety are likely to remain elevated in the near term - which we believe continues to warrant a cautious (aka neutral) investment positioning at this time.

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