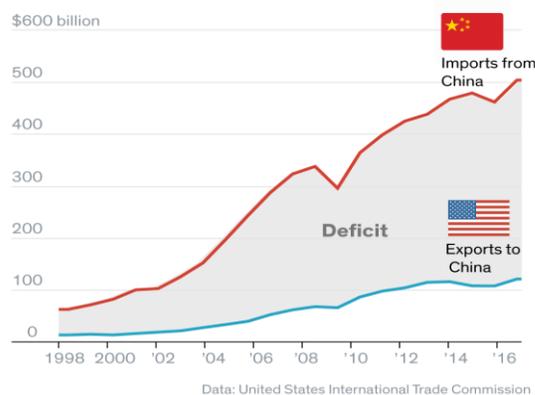


BCA Market Perspective © The Deficit Debate

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April 2018

Not all wars are fought on battlefields, and as we've come to find out in 2018, firing off a tweet can start a war just as quickly as pulling a trigger. One of the key campaign promises of the current administration is to get tough with China, and the recent announcements from the President seem to have escalated tensions between the two countries.

The widening trade gap



The gap between Chinese goods imported to the U.S. and American goods exported to China rose from \$347 billion to \$375 billion in 2017, raising the U.S. overall trade deficit to \$566 billion, the largest gap since 2008. On January 23rd, President Trump imposed tariffs on imported solar panels and washing machines. Then on March 22nd, the President signed a memorandum to apply \$50 billion in tariffs on Chinese goods to combat the theft of U.S. intellectual property. This announcement prompted the “Tariff Tantrum” in U.S. equity markets, an immediate drop of over 700 points in the Dow Jones Industrial Average, which finished the day down nearly 3%. China retaliated by announcing plans of their own to impose tariffs on 128 U.S. products, which they implemented on April 2nd. The situation continued to intensify with a series of “attack” and “counters”, as the U.S. Trade Representative’s (USTR) office published a list of 1,300+ Chinese goods to levy tariffs on. This was countered by China’s Customs Tariff Commission of the State Council announcing additional tariffs on 106 more U.S. goods. The President elected to answer this latest counter by directing the USTR to consider an additional \$100 billion in tariffs.

So how did the U.S. get to into such a large deficit with China and what does this administration hope to accomplish with tariffs and a potential trade war? China has been recognized as the World’s Manufacturer, producing goods at a fraction of the cost. To maintain its low-cost status, China’s central bank has been known to manipulate its currency, pegging the Yuan against the dollar. Separately, over the past decade, China is believed to have stolen billions worth of intellectual property and produced a countless number of counterfeit products. These types of unfair trade practices are what the U.S. is attempting to reverse through tariffs.

Economists universally regard tariffs to be inflationary and free trade to be deflationary. If the current “war of words” between U.S. and China escalates into more meaningful sectors of the markets, it will ultimately be the consumer who is burdened with a higher cost of living. Not to mention, increased trade tension certainly increases the fear of a possible recession in the short-term.