Tariffs, Trump and the passionate intensity of…

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Things fall apart; the centre cannot hold
Mere anarchy is loosed upon the world……

The best lack all conviction, while the worst are full of passionate intensity.

The Second Coming
A poem by W.B. Yeats (1865-1939)

Is Donald Trump's "Second Coming" as US President just "passionate intensity"?

The return of Donald Trump to the White House has generated alarm over the imposition of large tariffs for America's key trading partners as well as smaller players like Australia. Since President Trump took office on 20 January 2025, a 25% tariff has been announced for Canada and Mexico, 20% tariffs for China and a 25% tariff on all steel and aluminium imports into the US. President Trump has also signalled the intention to implement a 25% tariff on cars, semiconductor and pharmaceutical imports which would also dramatically impact global trade relationships.

Also concerning is the way President Trump is communicating these decisions. There has been an 'on again - off again' sequence of tariff announcements with President Trump on "Truth Social" in his first 50 days of the "Second Coming". This new megaphone for US economic policy under President Trump has been chaotic and confusing. One day the tariffs are due to start in March, the next day they are delayed till April - then the tariff is back on immediately.

Commentators are now calling this a "Trade War" So, the first casualty of this Trade War seems to be US share prices. Since their peak in mid-February, US share prices have fallen by circa 10% with fears that these new tariffs will cause the US economy to see rising inflation and potentially slide into recession. Australian shares have also seen sharp price falls.

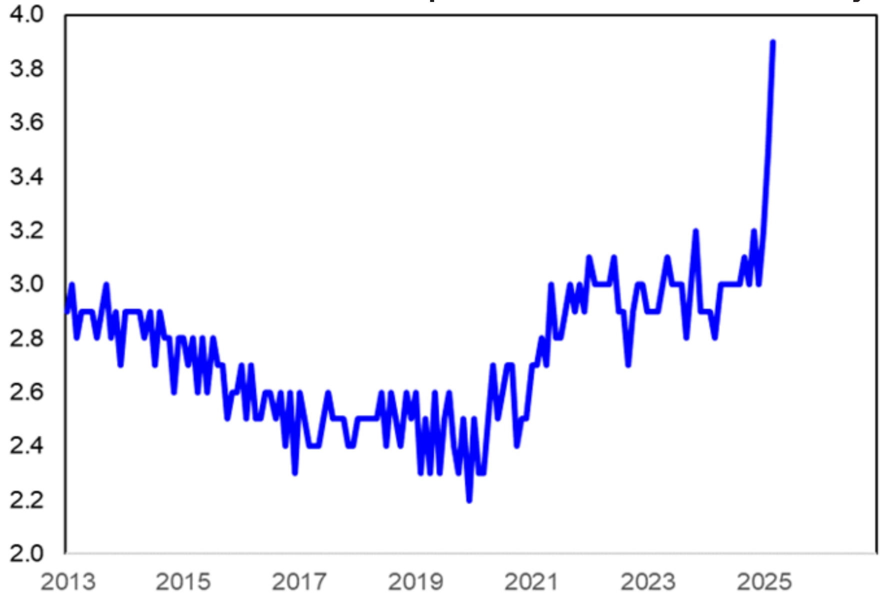
Tariffs come at a cost to economic activity and inflation

Why are investors worried about tariffs? Primarily because tariffs can raise consumer prices and generate inflation. Economics typically describes a tariff as a "*tax imposed on a good imported into a country."* [1] This tariff 'tax' is applied to the good and notionally paid by the importer. Trump states that the foreign suppliers of goods into the US - whether Canadian, Chinese, or Mexican - will pay the tariff. However, most of the evidence from the Trump Administration's first trade war in 2018-2019 is that US consumers ended up paying the extra tariff cost. This occurred whether the product was a solar panel or a washing machine. Only in a few rare cases like steel tariffs in 2018 did the foreign supplier absorb the tariff costs with the consumer not paying the cost.[2]

[1] 'Macmillan Dictionary of Modern Economics', Macmillan Press, 1986.
[2] 'Who's Paying for the US Tariffs? A Longer-Term Perspective', Amiti M, Redding SJ & Weinstein DE, Working Paper 26610, https://www.nber.org/papers/w26610, Issue Date January 2020.

While Trump's 2025 tariff proposals are yet to be fully implemented, there are already signs of increasing inflation risk. American consumers are now worried that Trump's tariffs will raise prices judging by the University of Michigan consumer sentiment survey responses.[3] For March, consumer expectations for US inflation over the next 5 to 10 years rose to 3.9% (Chart 1). In January, this inflation expectation was only 3.2%. So there has been a sharp rise of 0.7% in inflation expectations in the first two months of Trump's "Second Coming."

Chart 1: US consumer inflation expectations for the next 5 to 10 years



Source: University of Michigan

The key negative of Trump's tariffs is that they are generating confusion and doubt on economic prospects. Tariffs can cause businesses to be cautious about deploying future capital investment and providing employment opportunities. Even if you are a US manufacturer hoping to benefit by improved competitiveness with tariffs applied to foreign goods, your access to some cheaper foreign inputs such as aluminium and steel may be lost. Your export opportunities can also be curtailed by other countries imposing tariffs as retaliation. This is a 'lose-lose' proposition for US businesses. Consumers can also 'lose-lose' by having higher goods prices but also lower job opportunities.

The Peterson Institute for International Economics provided estimates of the economic activity impact of Trump's tariffs proposals in January 2025 with a 25% tariff on Canada and Mexico and 10% for China (Table 1).[4] This analysis suggests that US economic activity will be a cumulative -0.3% lower than potential over the next three years (2025 – 2027). Initially this seems a mild setback compared to the potential annual US Real Gross Domestic Product (Real GDP) growth rate of 1.8% estimated by the central bank. However, President Trump has the capacity to further raise tariffs beyond the current levels. The US central bank's interest rate response to a 0.7% increase in inflation over the next three years is also not known. If the US Federal Reserve (Fed) starts raising interest rates to curb the inflation impact, the downside risk to US economic activity becomes larger.

[3] 'University of Michigan Consumer Sentiment Index - Preliminary Results for March 2025', http://www.sca.isr.umich.edu/.

[4] 'Trump's threatened tariffs projected to damage economies of US, Canada, Mexico, and China', McKibbin WJ & Noland M, https://www.piie.com/blogs/realtime-economics/2025/trumps-threatened-tariffs-projected-damage-economies-us-canada-mexico, January 17, 2025.

Table 1: Estimates of the economic activity impact of Trump's January 2025 tariff proposals over the next three years

Impact of Trump's tariffs over 3 years (2025-2027)	Economic activity as measured by Real GDP (% change)	Consumer inflation (% change)
US	**-0.3**	**+0.7**
China (proposed 10% tariff)	**-0.2**	**+0.3**
Canada (proposed 25% tariff)	-2.5	+2.8
Mexico (proposed 25% tariff)	-2.0	+4.4

Source: Peterson Institute for International Economics.

For China, the impact on economic activity of -0.2% over three years for a 10% tariff (Table 1) appears similarly mild. However, we need to double this GDP impact to circa -0.4% given Trump raised China's tariff to 20% on 3 March. For Canada and Mexico, the impact is more severe with declines of 2.5% and 2% below potential GDP, respectively. As the Peterson Institute notes "*these figures likely underestimate the real damage to the three economies (US, Canada and Mexico), which are highly integrated."*

Trump's broader agenda beyond tariffs for the next few years is worrying investors

Even these economic estimates do not fully capture investors' concerns about President Trump's agenda for the next four years. The US Fed has recently signalled that US interest rates are on hold given the "uncertainty" over the impact of President Trump's agenda. US Fed Chair Jerome Powell summed up the challenges in trying to work out what exactly is the Trump Administration's agenda:

"Looking ahead, the new (Trump) Administration is in the process of implementing significant policy changes in four distinct areas: trade, immigration, fiscal policy, and regulation. It is the net effect of these policy changes that will matter for the economy and for the path of monetary policy." [5]

Hence the new reality is that investors have concerns on multiple fronts beyond tariffs. For example, President Trump's campaign promise was for the "mass deportation of undocumented migrants" which could be between 1.3 million and 8.3 million people. This would reduce the US labour supply in critical industries such as agriculture where 40% of the workforce is estimated to be 'undocumented migrants'. Hence there is further upside risk to US inflation.

Then we have the phenomena of the Trump's Department of Government Efficiency (aka 'DOGE'). DOGE is currently being run by the renowned part-time Tesla car manufacturer and Space X 'rocket man' Elon Musk. Trump has claimed that DOGE has already identified "*hundreds of billions of dollars of fraud*" and that Musk will lead the charge to find US$1 trillion in savings by cutting government spending. Neither Trump nor Musk have provided any compelling evidence of significant fraud.[6] DOGE is another dark cloud for US economic growth by signalling a reduction in government jobs and spending over the next four years.

[5] *Economic Outlook*, Federal Reserve Chair Jerome Powell, *March 7 2025, https://www.federalreserve.gov/newsevents/speech/powell20250307a.htm.*
[6] 'DOGE website offers error-filled window into Musk's government overhaul', Heath B & Read T, Reuters, https://www.reuters.com/world/us/doge-website-offers-error-filled-window-into-musks-government-overhaul-2025-03-04/, March 5, 2025.

Finally, we have Trump's executive order to reduce government regulations. This "*Unleashing Prosperity Through Deregulation*" mantra requires regulators to identify at least ten existing regulations for repeal when proposing a new regulation. Regulators must ensure that the net cost of all new regulations are "*significantly less than zero*." [7] This is a further example of the diminishing role of the US Federal Government planned under Trump.

Clearly the current Trump agenda - higher tariffs that impose more difficult trading conditions for the global economy, lower US immigration and population growth with "mass deportations," more restrictive US fiscal policy with cuts to government jobs and spending as well as the less regulatory involvement - is not a recipe for predictability and stability.

Remarkably tariffs are being applied to the close allies of the US in terms of Canada and Mexico as well as Europe and Australia. Contrast this with the way America's adversaries are being treated.

Russia is now seemingly a new best friend and Ukraine is a threat to starting 'World War 3'. This overlooks the reality that Russia began the Ukrainian war by invading Crimea back in 2014 and then assaulting eastern Ukraine in February 2022.

To call this as just the "Art of the Deal" is generous. President Trump's impulsive decision-making can reasonably be regarded as both a threat to the global economy as well as American political leadership in the world.

The new US President certainly has a "*passionate intensity*" that W.B. Yeats referred to in the "*Second Coming*", leaving the world's economic and political structures hostage to his impulses.

[7] 'President Trump's Executive Order Seeks to Reduce Federal Regulation', Sidley Austin LLP, https://www.sidley.com/en/insights/newsupdates/2025/02/president-trumps-executive-order-seeks-to-reduce-federal-regulation, February 11, 2025.