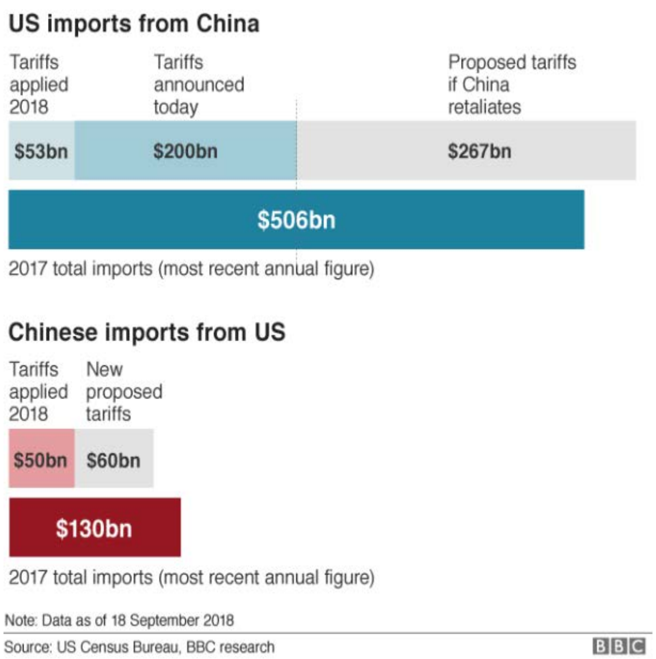
THOUGHT FOR THE WEEK

Tariffs Schmariffs?

Key Takeaways

- Once again tariffs and trade wars dominated the headlines. This week, the trade war between the United States and China escalated with the imposition of additional tariffs on more than $260 billion of goods.
- The domestic equity markets have shrugged off trade concerns as the U.S. economy enjoys the fiscal stimulus of the tax cuts paired with low unemployment numbers.
- Trade wars come with heightened uncertainty and risk, which is why it is important to have a properly diversified and well-balanced portfolio. Investors typically focus on their long-term financial goals and resist the temptation of making changes to their portfolio based on headline news alone as economic fundamentals don't change overnight.

On Monday, the Trump administration announced tariffs on an additional $200 billion of Chinese goods targeting products ranging from handbags to bicycle tires. The tariffs will start at 10% beginning Monday, September 24th and then rise to 25% by the end of 2018. In response, China has hit back by announcing new trade tariffs on $60 billion of U.S. goods. China will target goods including liquefied natural gas, meat, nuts, and auto parts.



In addition to the penalties enacted earlier this year, the latest round of tariffs covers $50 billion worth of Chinese goods. Taken together, it means nearly half of the products that China sells to the United States each year will be hit by American tariffs. In comparison, while China has not retaliated dollar-for-dollar, the total tariffs imposed by China on U.S. goods will represent nearly 85% of all goods they import from the U.S. Should China retaliate further, the Trump administration has threatened tariffs on another $267 billion worth of imported goods. The sum of the proposed tariffs, including the $267 billion that remains to be enacted, would be greater than the reported $506 billion total imports for 2017.

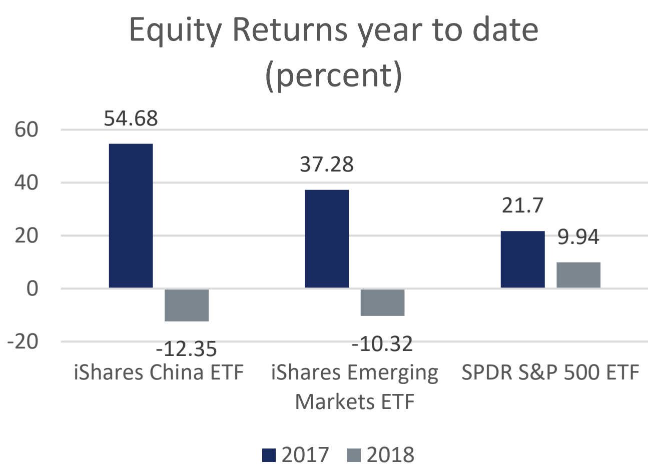
The tariffs are meant to punish China for alleged unfair trade practices, including intellectual property theft. Tariffs act like a tax and will make products made in China more expensive; thus prompting U.S. businesses and consumers to buy elsewhere.

The impact of the tariffs

According to the Tax Foundation, an independent tax policy research organization, the tariffs enacted by the administration this week would reduce long-term growth by 0.12% or $30.4 billion and eliminate 94,303 full time jobs. To put this into context, the U.S. economy is $19.4 trillion and has approximately 130 million people employed on a full-time basis.

Table 1. Impact of Trump Administration Enacted Tariffs

Tariff Revenue (Billions of 2018 Dollars)	$41.95
Long-run GDP	-0.12%
GDP (Billions of 2018 Dollars)	-$30.43
Wages	-0.08%
FTE Jobs	-94,303



Source: Morningstar as of 9/18/18.

Perhaps this is one of the reasons the U.S. markets have shrugged off the impact of the latest tariffs. The U.S. stock market, as represented by the S&P 500, has reached in new highs, but a quick glance at overseas markets in China and the emerging reveals a more sobering story. Equity markets in China have entered bear-market territory (dropped 20% from its previous high) this year driven by trade and tariff concerns and a strong dollar. The downturn in emerging market equities represents a dramatic shift in market returns, as it was the best performing broad market index in 2017.

Conclusion

The latest round of tariffs is an escalation of an already serious trade dispute. The extent of the tariffs' impact on investments will truly depend on how long the tariffs remain in place. If the current tariffs remain effective for a prolonged period, it could adversely affect both consumer and business sentiment. Alternately, if the tariffs have a significant negative impact on the economy, it is possible they could be removed just as they were created, remember we have a midterm election coming up. It remains too early to tell! The domestic equity markets have shrugged off trade concerns as the U.S. economy enjoys the fiscal stimulus of the tax cuts paired with low unemployment. In the short term, expect market volatility in some parts of your portfolio as global markets digest each set of headline news. Long-term investors should focus on their financial goals and resist the temptation of making changes to their portfolio based off of headline news alone because economic fundamentals don't change overnight.

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