

Will Trump Push the Trade War Too Far?

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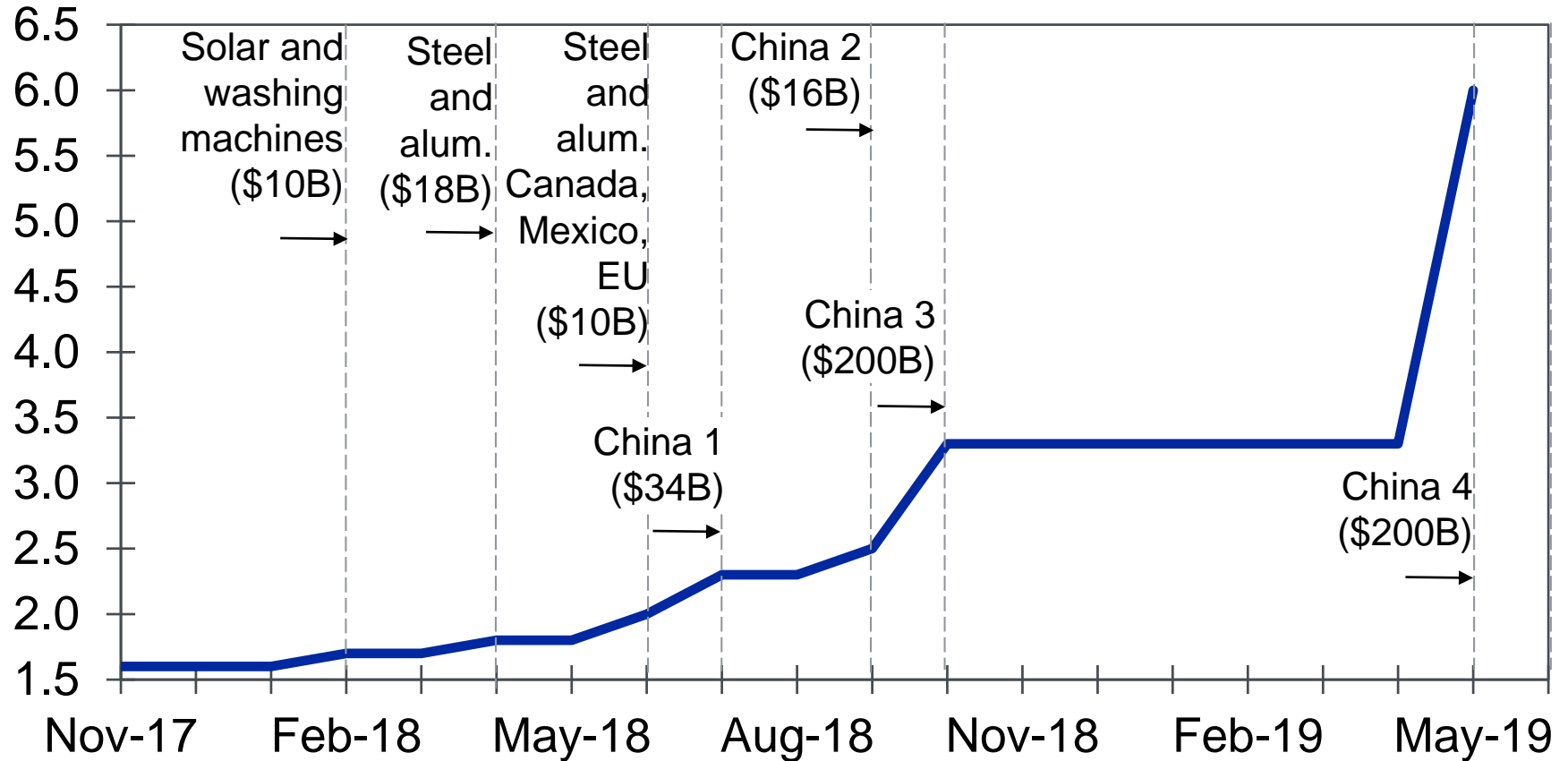
May 20, 2019

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How Did We Get Here?

The Trade War Escalates

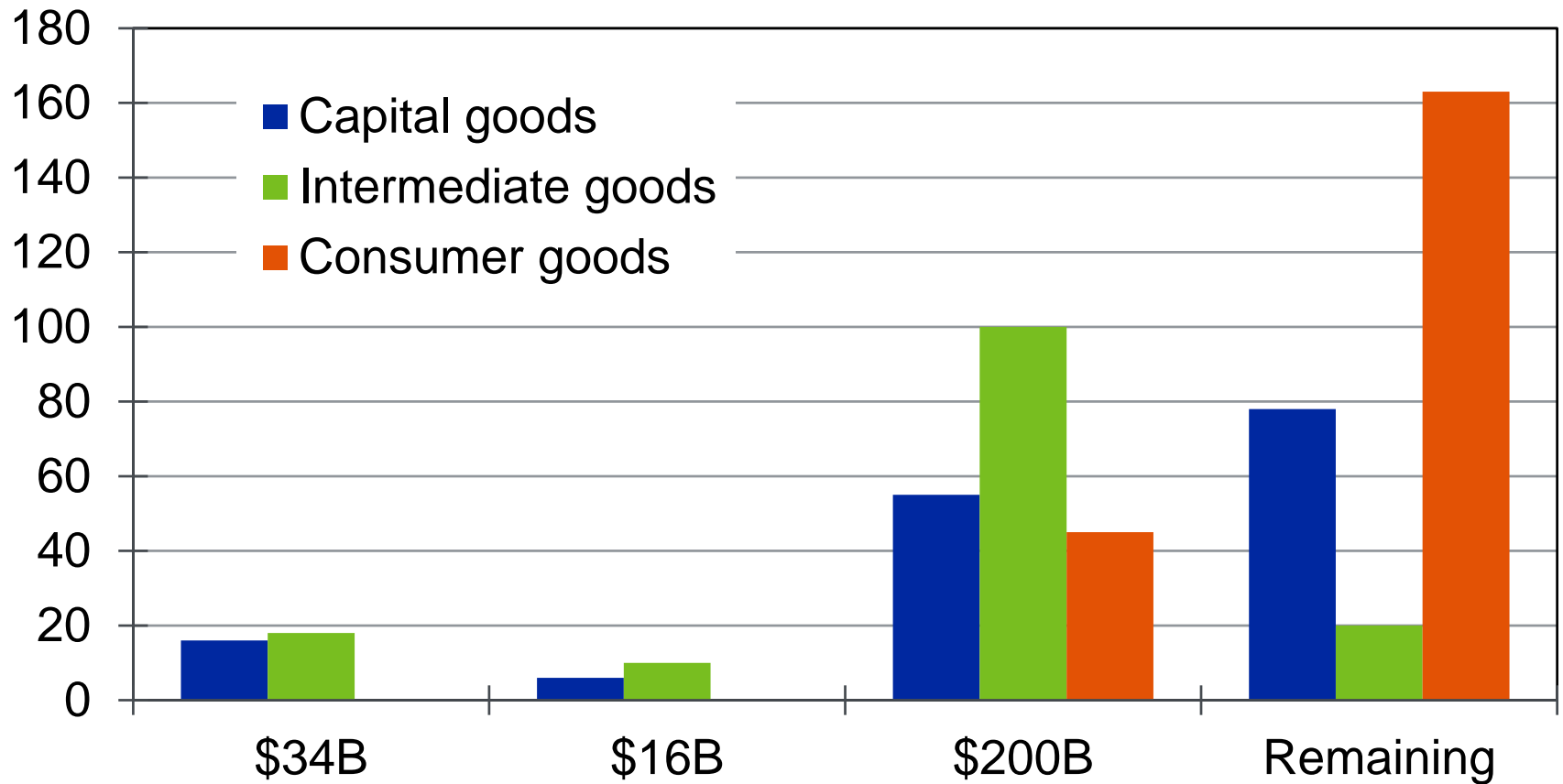
U.S. effective tariff rate, %



Sources: Census Bureau, USTR, USITC, Moody's Analytics

Who Bears the Brunt of the War

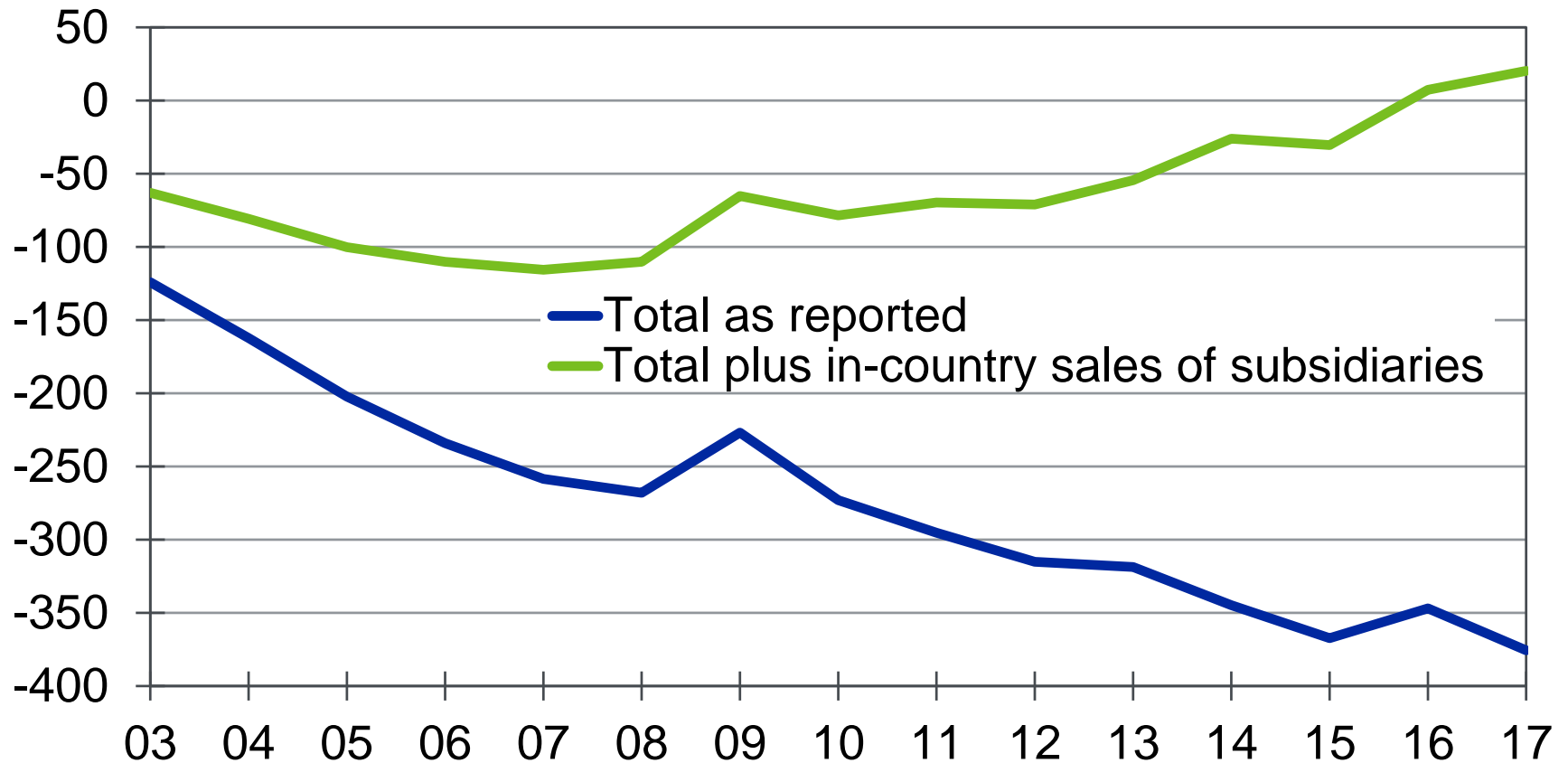
Chinese imported goods subject to tariffs by round, \$ bil



Sources: Commerce Department, Moody's Analytics

Balanced Trading Relationship

U.S.-China trade balance, \$ bil



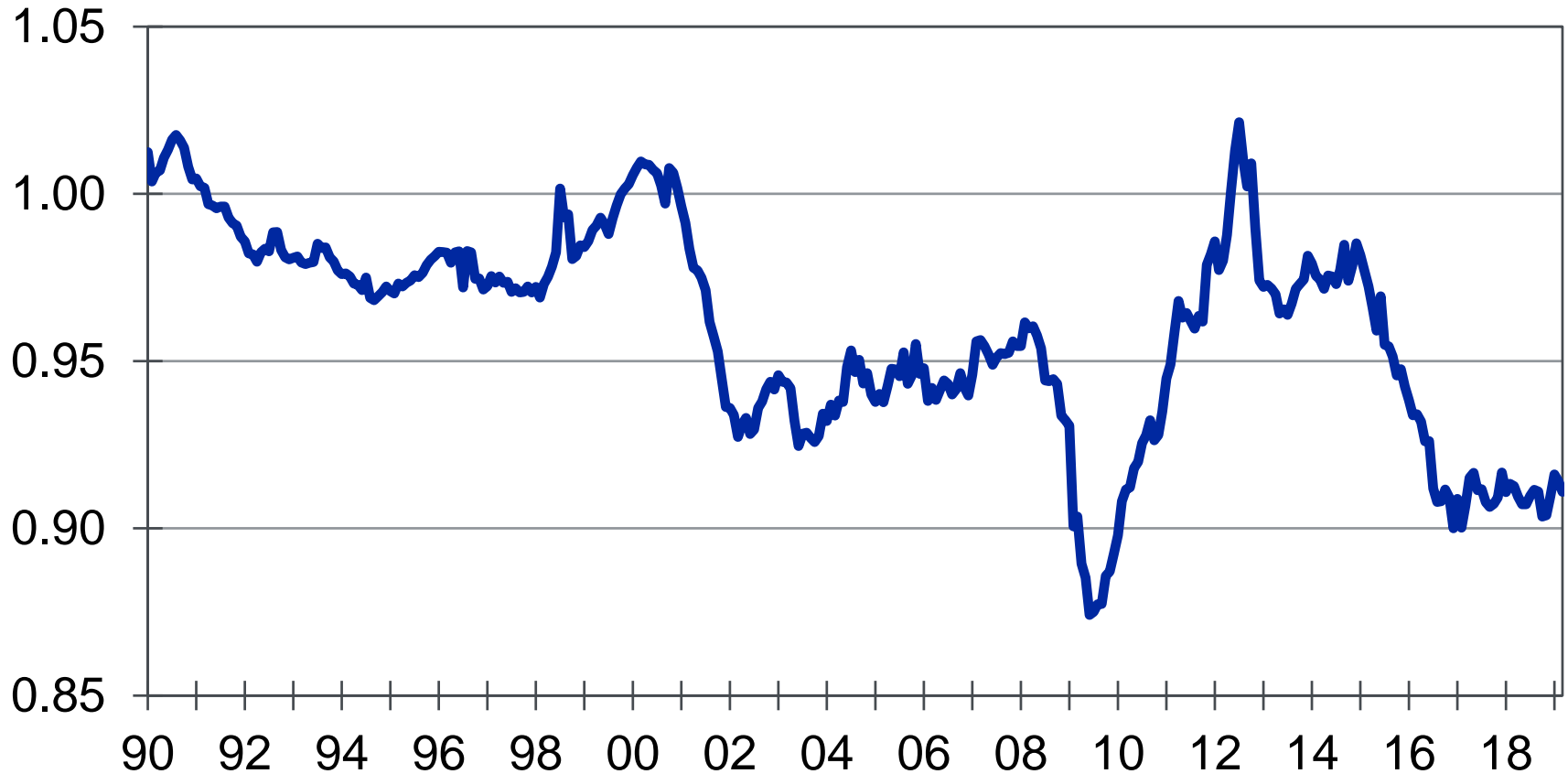
Sources: Census Bureau, Deutsche Bank, Moody's Analytics

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Economic Impact to Date

Tariffs Didn't Boost Employment

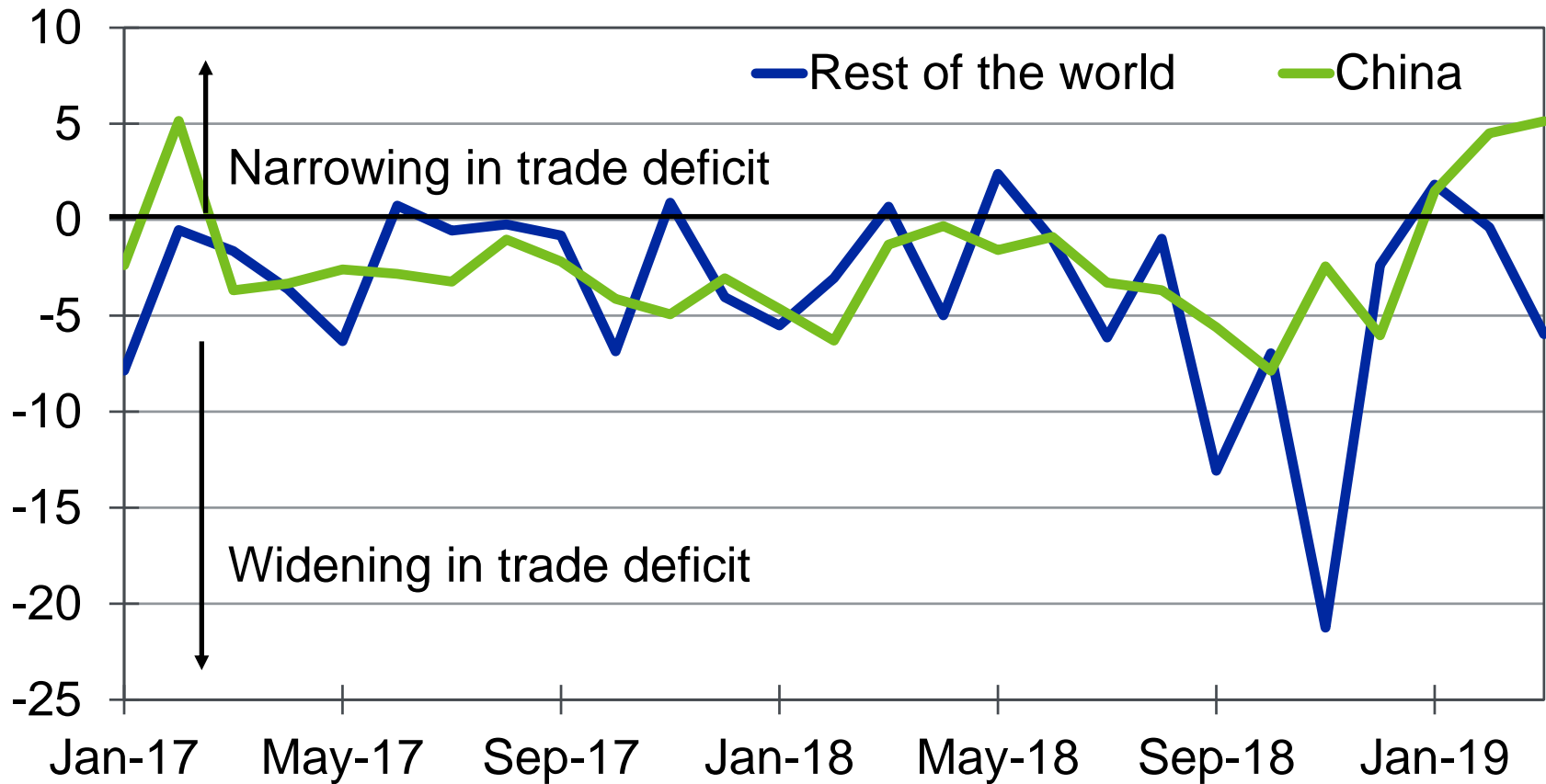
Steel and aluminum, share of U.S. manufacturing employment, %



Sources: BLS, Moody's Analytics

Shifting Trade Patterns

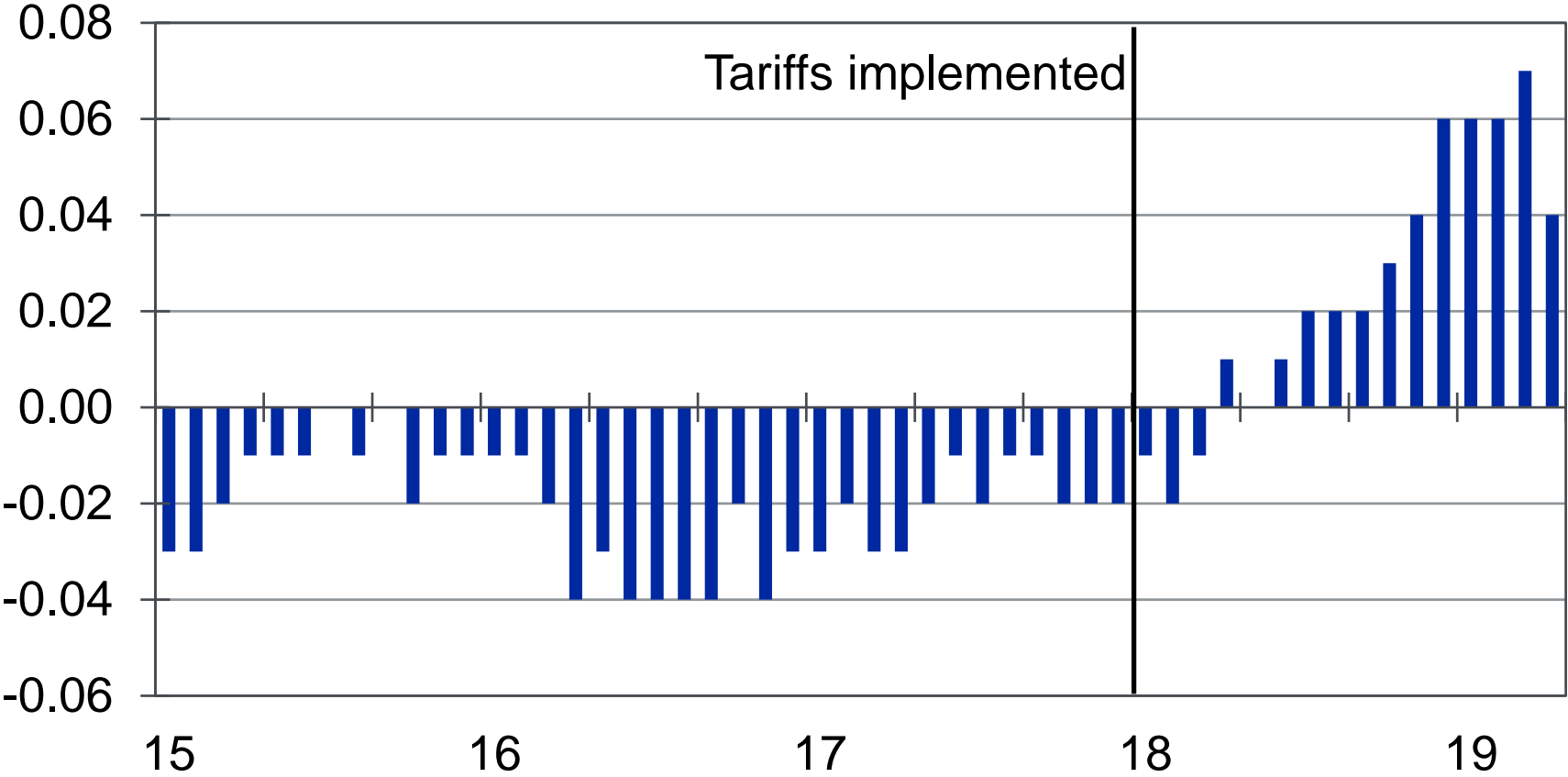
Nominal U.S. trade deficit, yr-to-yr difference, \$ bil, NSA



Sources: Census Bureau, Moody's Analytics

Composition Limits Impact on Inflation

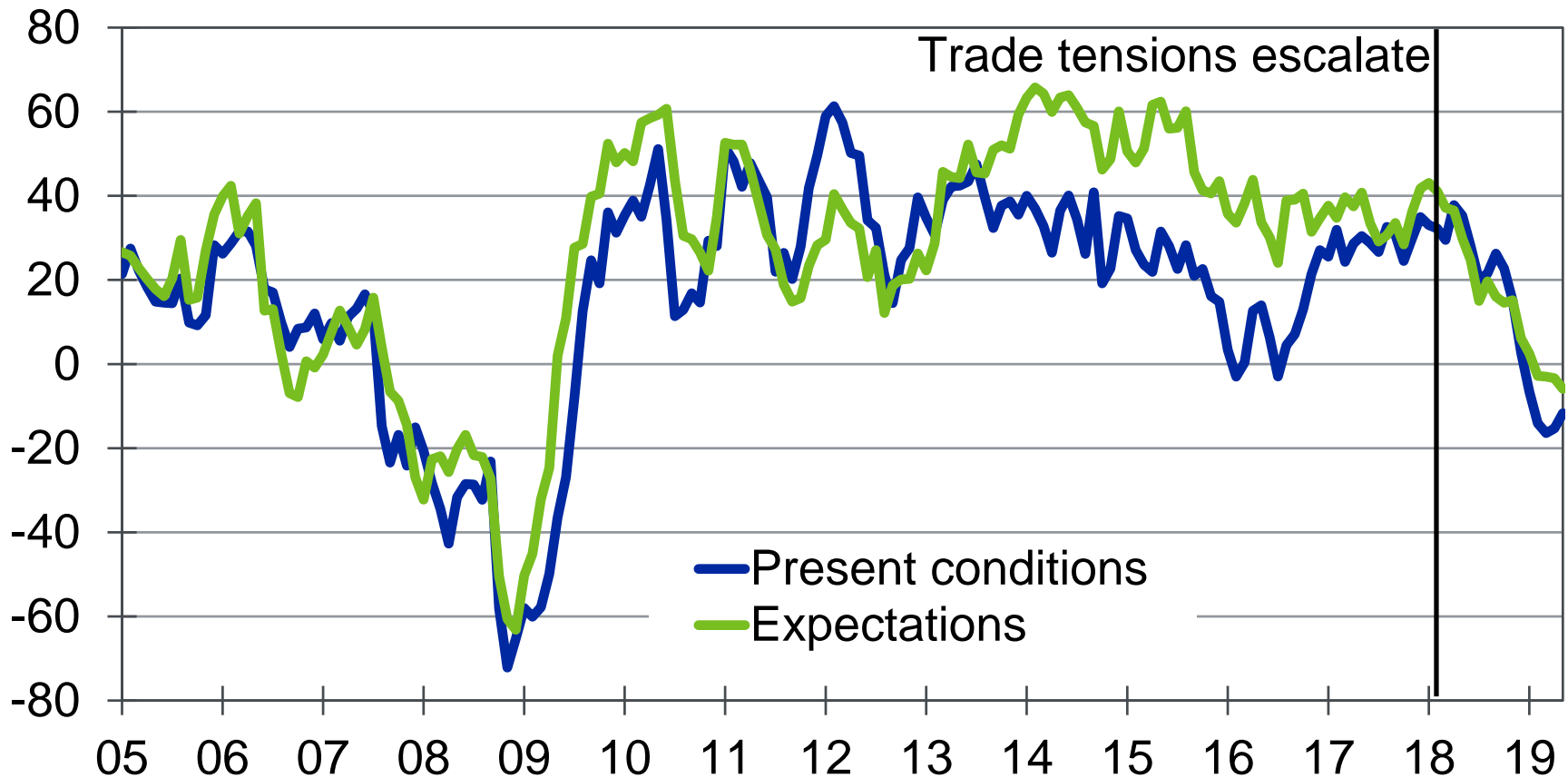
Tariff-impacted goods' contribution to CPI, % change yr ago, ppt



Sources: BLS, Moody's Analytics

Trade War Hits Business Sentiment

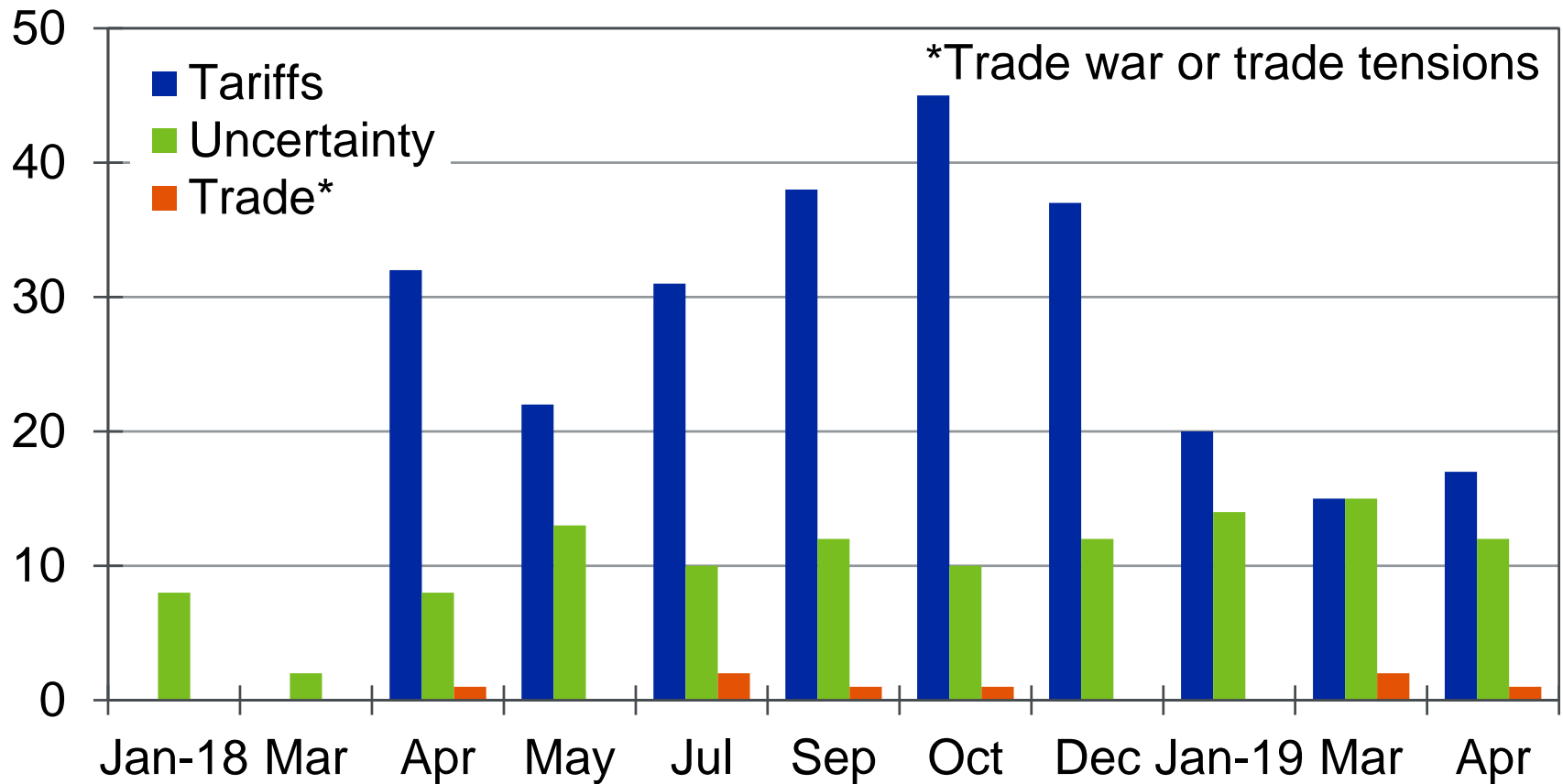
% difference between positive and negative responses



Source: Moody's Analytics

Focus on Tariffs Had Faded

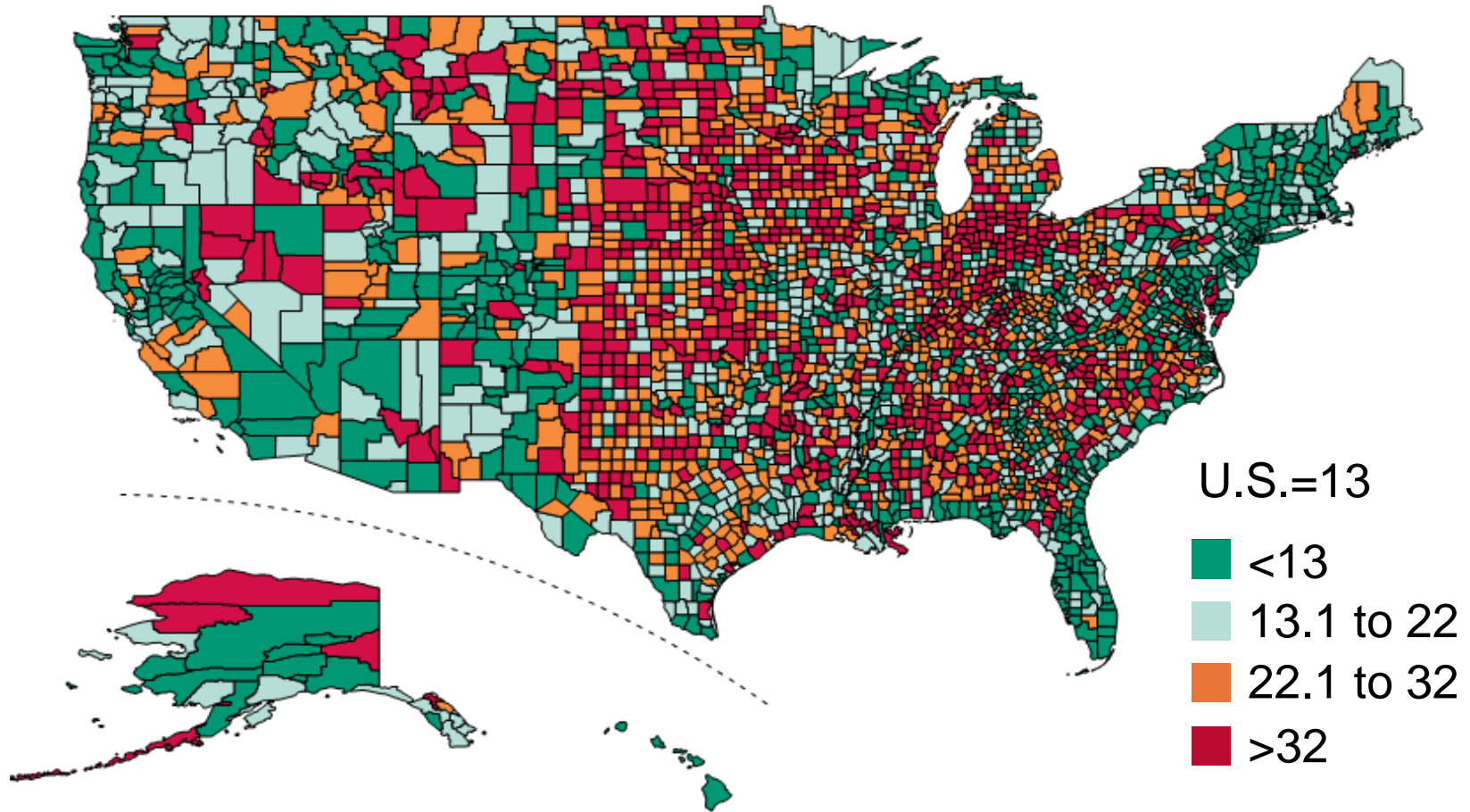
Fed's Beige Book references, word count, #



Sources: Federal Reserve, Moody's Analytics

Regional Casualties of the Trade War

% of GDP in industries impacted by Chinese retaliatory tariffs



Sources: BEA, Moody's Analytics

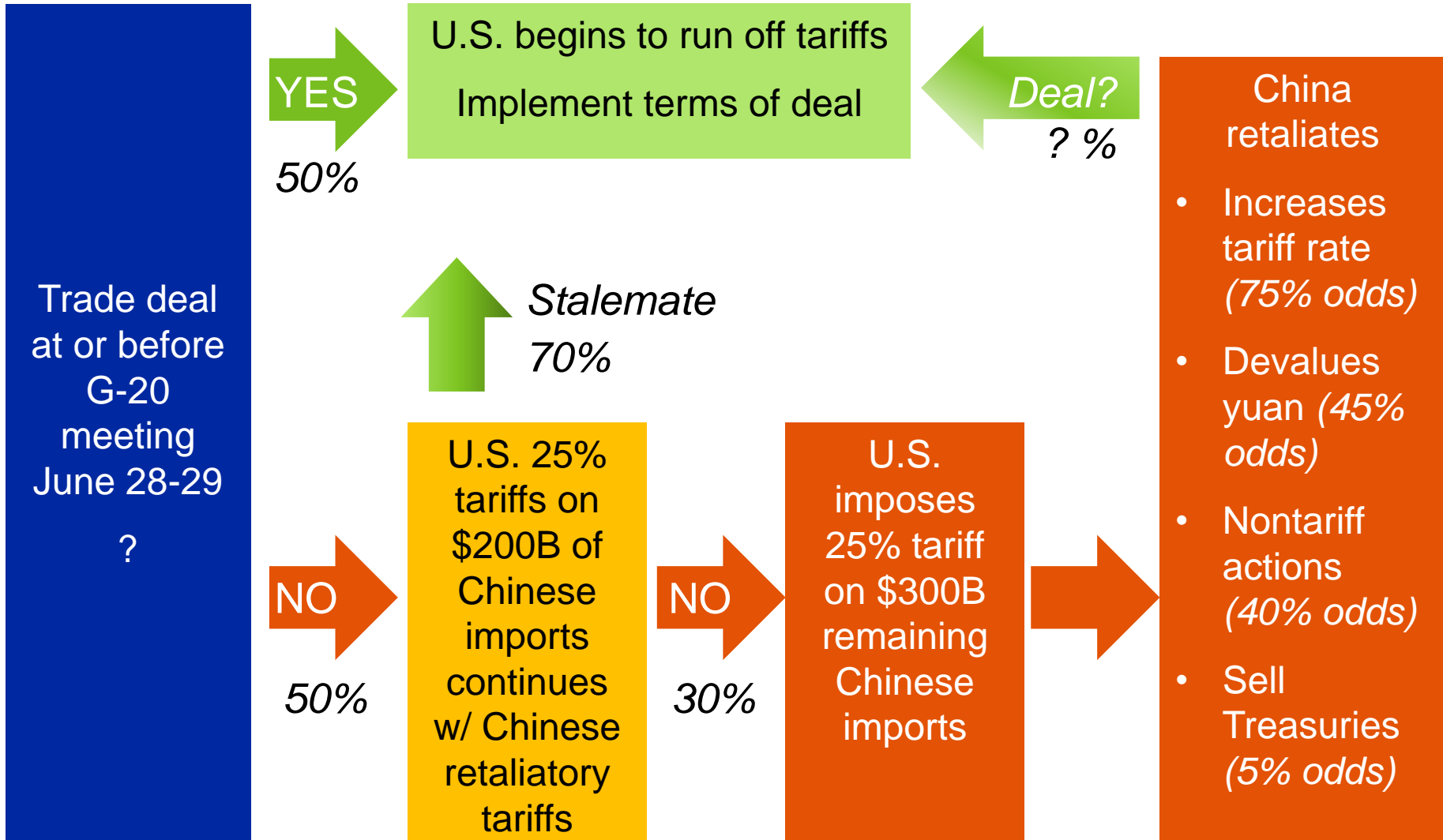
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Trade War Scenarios

Possible Scenarios

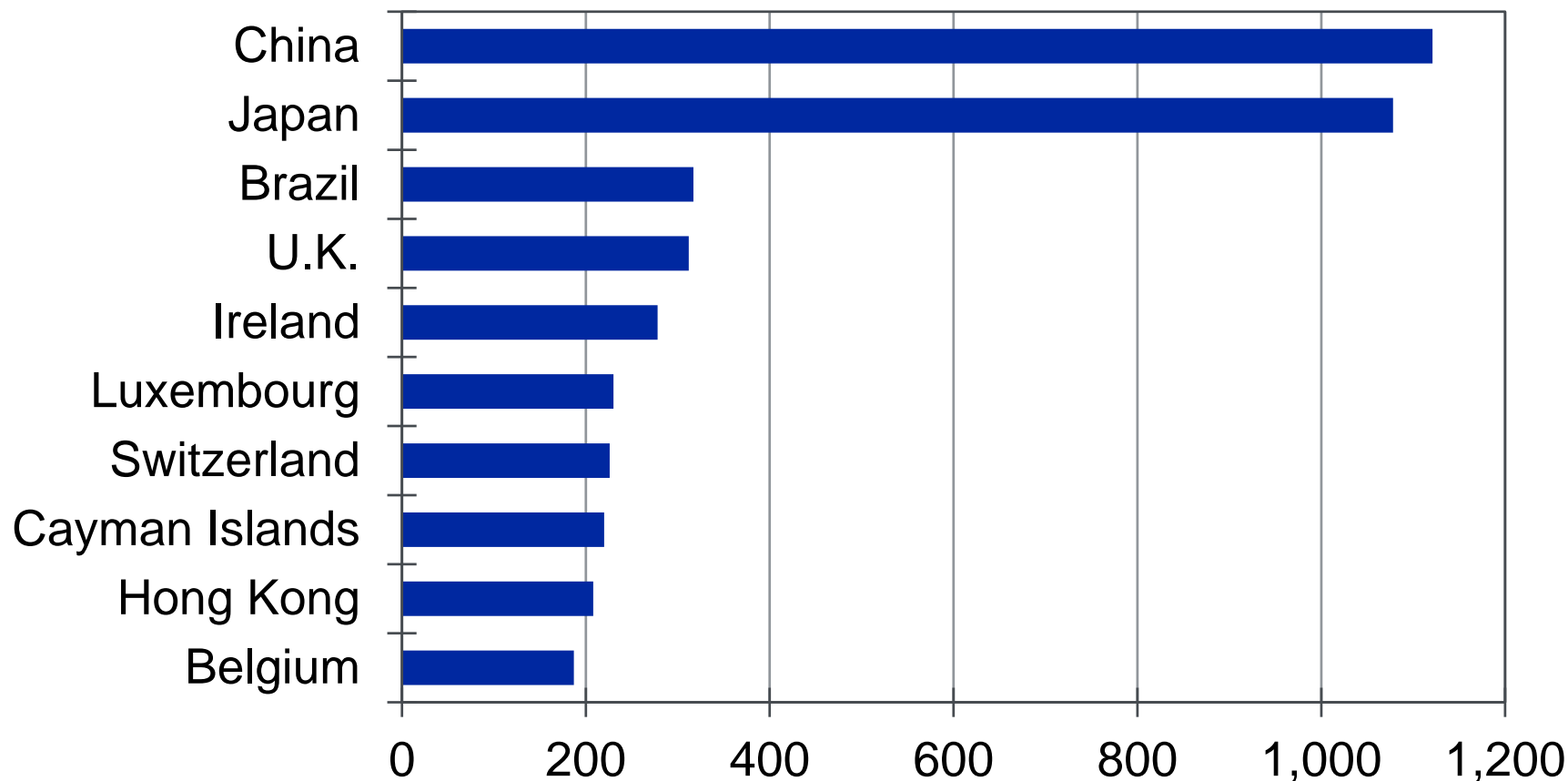
<u>Scenario description</u>	<u>Economic impact</u>	<u>Financial market implications</u>	<u>Value of \$</u>
<p>Deal</p> <ul style="list-style-type: none"> U.S and China reach a trade agreement by the end of the G-20 meeting in late June. U.S. and China agree to run off tariffs 	<ul style="list-style-type: none"> No change to the baseline. Potential upside risks as confidence rebounds and supply chain issues fade. 	<ul style="list-style-type: none"> U.S. and Chinese equity markets rally as unease about the trade tensions is removed. U.S. 10-year Treasury increases as markets reduce bets of a Fed rate cut. 	<ul style="list-style-type: none"> U.S. real trade-weighted dollar is little changed.
<p>No Deal – Stalemate</p> <ul style="list-style-type: none"> No deal is struck by the G-20 meeting. U.S. tariffs remain at 25% on \$200B worth of goods. Chinese retaliatory tariffs in effect. Tariffs remain in place through Trump’s first term. 	<ul style="list-style-type: none"> Reduces U.S. GDP growth by 0.5 of a percentage point. China GDP growth cut by 0.5 of a percentage point, and GDP grows less than 6%. China pursues additional stimulus. 	<ul style="list-style-type: none"> U.S. and Chinese equity markets decline. U.S. 10-year decreases as the term premium falls and markets increase bets on Fed rate cut. Inflation expectations increase, but the impact is modest on long-term rates. 	<ul style="list-style-type: none"> U.S. real trade-weighted dollar appreciates. China devalues its currency.
<p>No Deal - Escalation</p> <ul style="list-style-type: none"> Trump puts a 25% tariff on all remaining Chinese imports. U.S. puts a 25% tariff on all vehicle imports and parts, with exclusions for Mexico and Canada. Rest of the world retaliates in-kind to the U.S. actions. 	<ul style="list-style-type: none"> Pushes the U.S. and Chinese economies toward recession. Global trade flows decline significantly. The Federal Reserve attempts to cushion the economic blow by cutting rates, and Chinese increase monetary and fiscal stimulus; these efforts fall short. 	<ul style="list-style-type: none"> U.S. and Chinese equity markets decline sharply. U.S. 10-year Treasury decreases as the Fed cuts interest rates. Investor flight to quality further pushes down 10-year yield. 	<ul style="list-style-type: none"> U.S. real trade-weighted dollar appreciates. China devalues its currency.

Timeline for a Trade Deal or No Deal



Chinese Have Leverage...

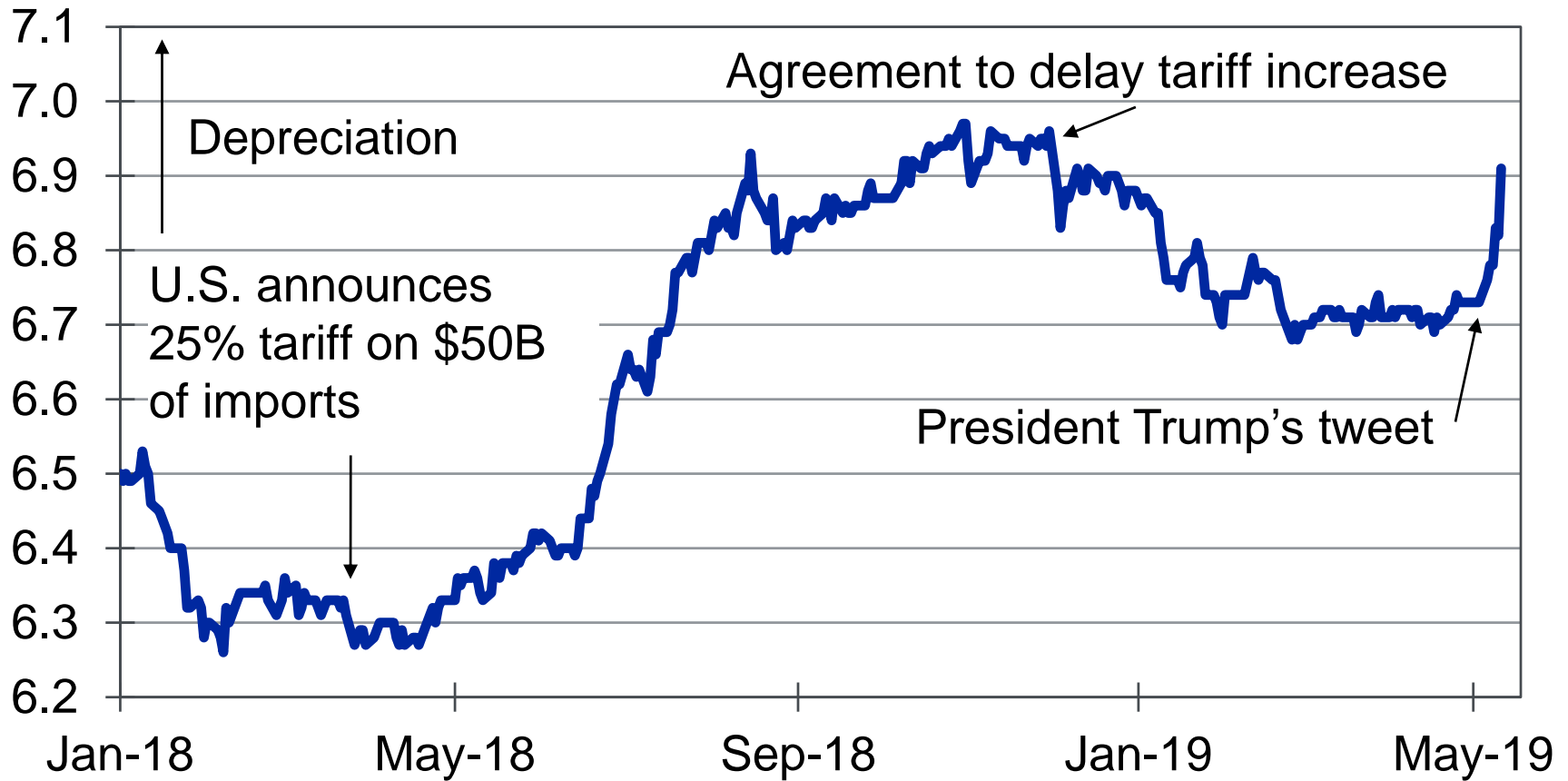
10 largest foreign holders of U.S. Treasuries, \$ bil



Sources: Treasury Department, Moody's Analytics

...Significant Leverage

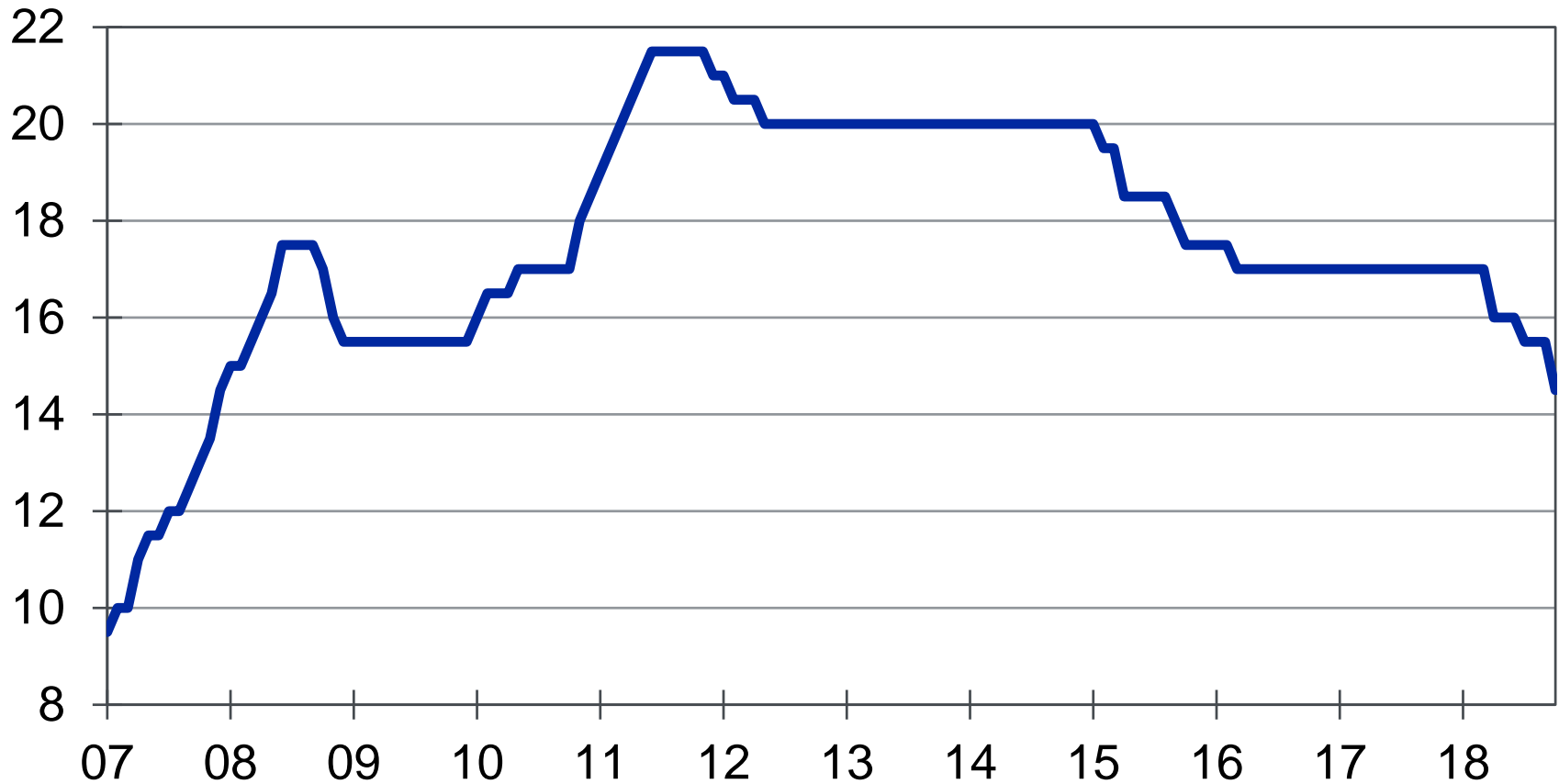
U.S./Renminbi exchange rate



Source: Moody's Analytics

China Should Be Able to Manage

China's reserve requirement ratio for major banks, %



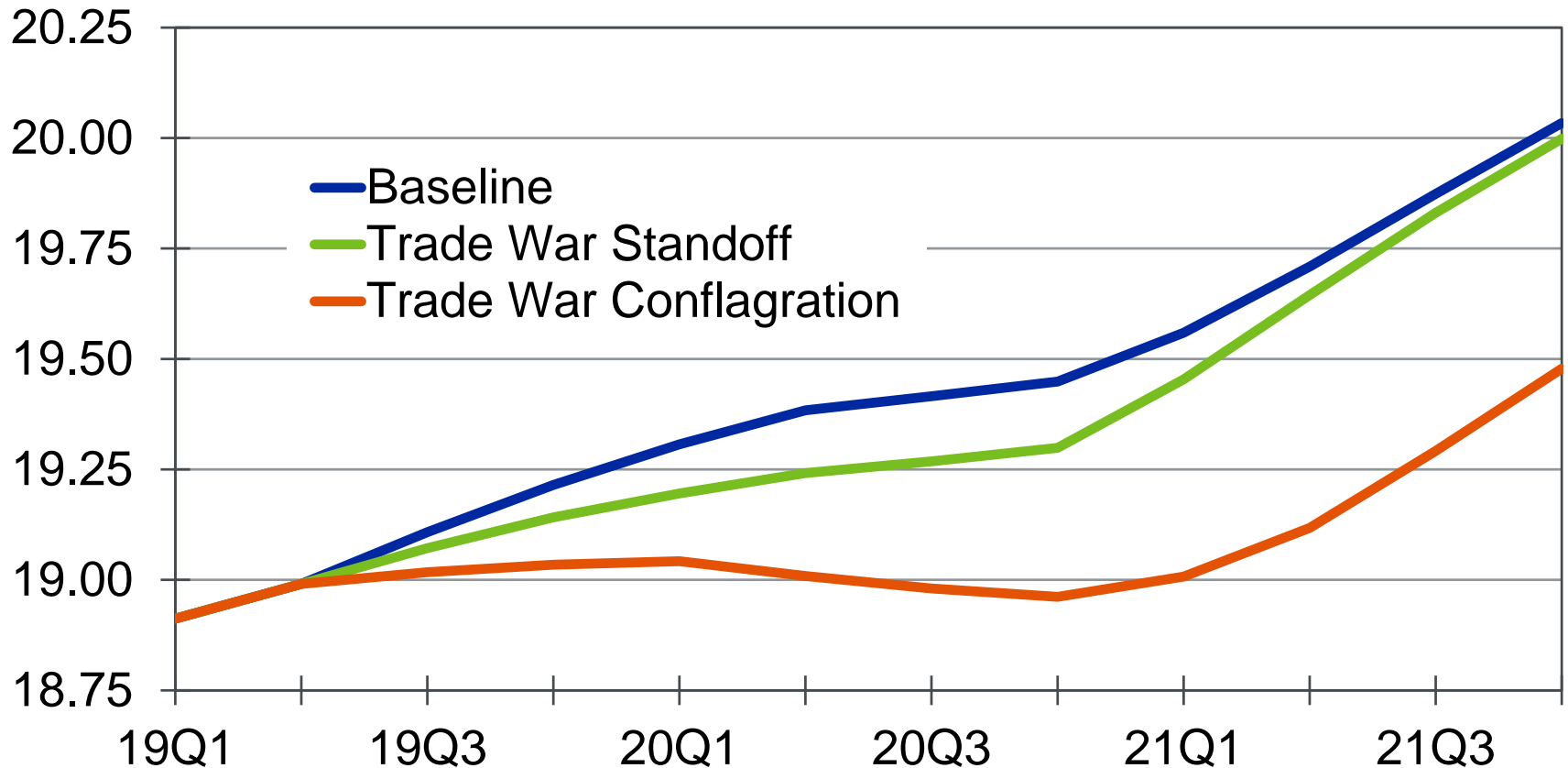
Sources: PBoC, Moody's Analytics

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Trade War Fallout

Trade War Scenarios Turn Darker

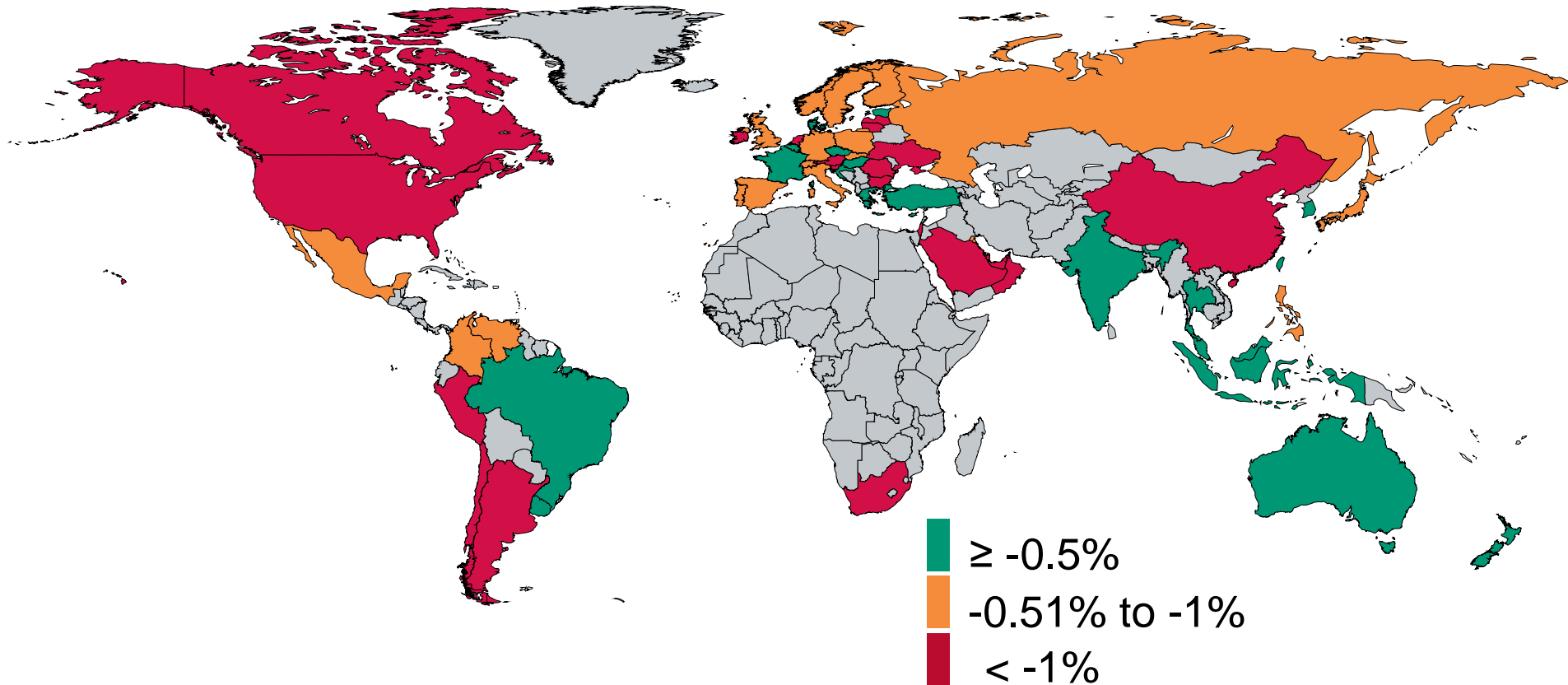
U.S. real GDP, 2012\$ tril



Sources: BEA, Moody's Analytics

Full-Blown Trade War Will Ignite Recession

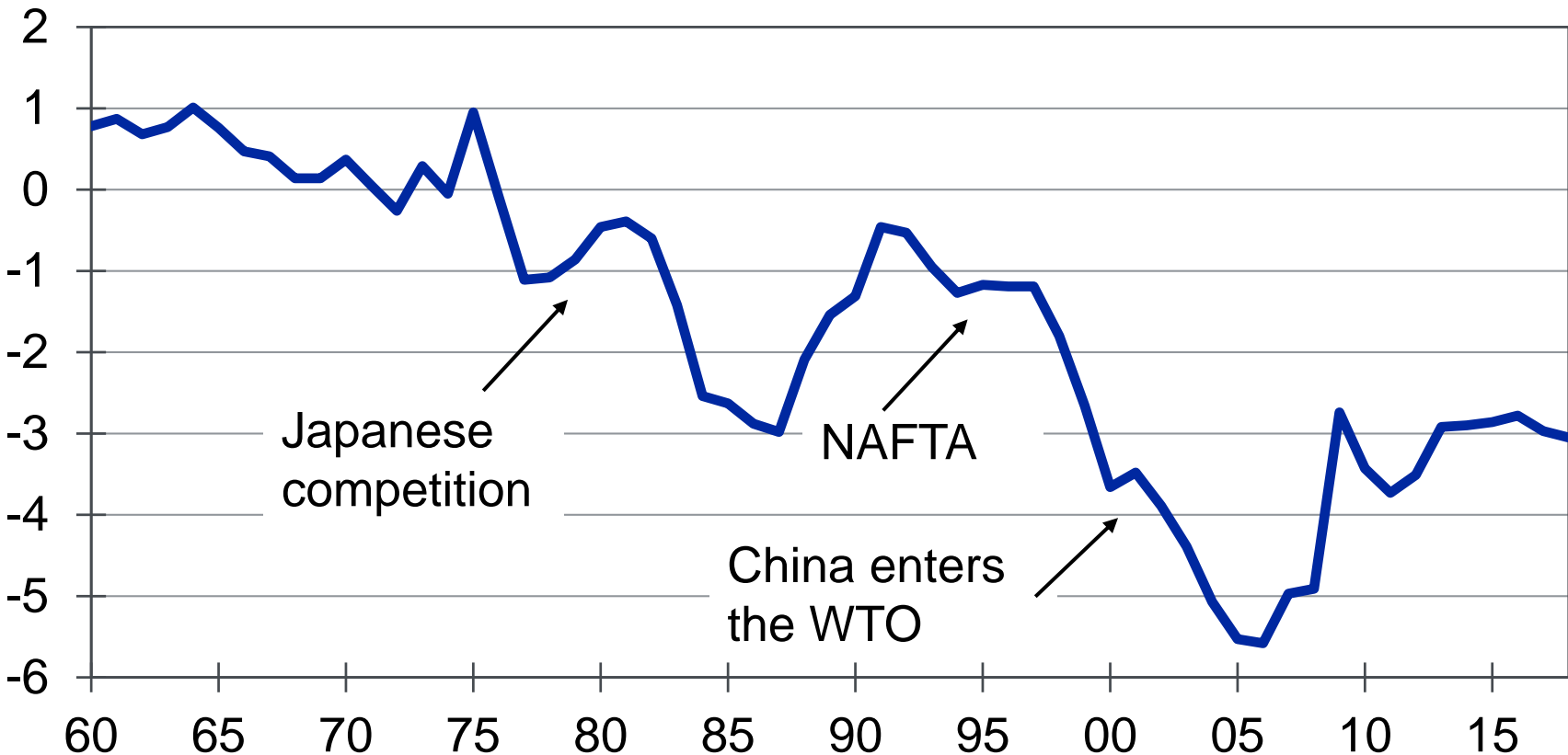
Diff in real GDP, 2020Q4, Trade Conflagration vs. No Tariff scenario



Source: Moody's Analytics

Fighting Yesterday's Battle...

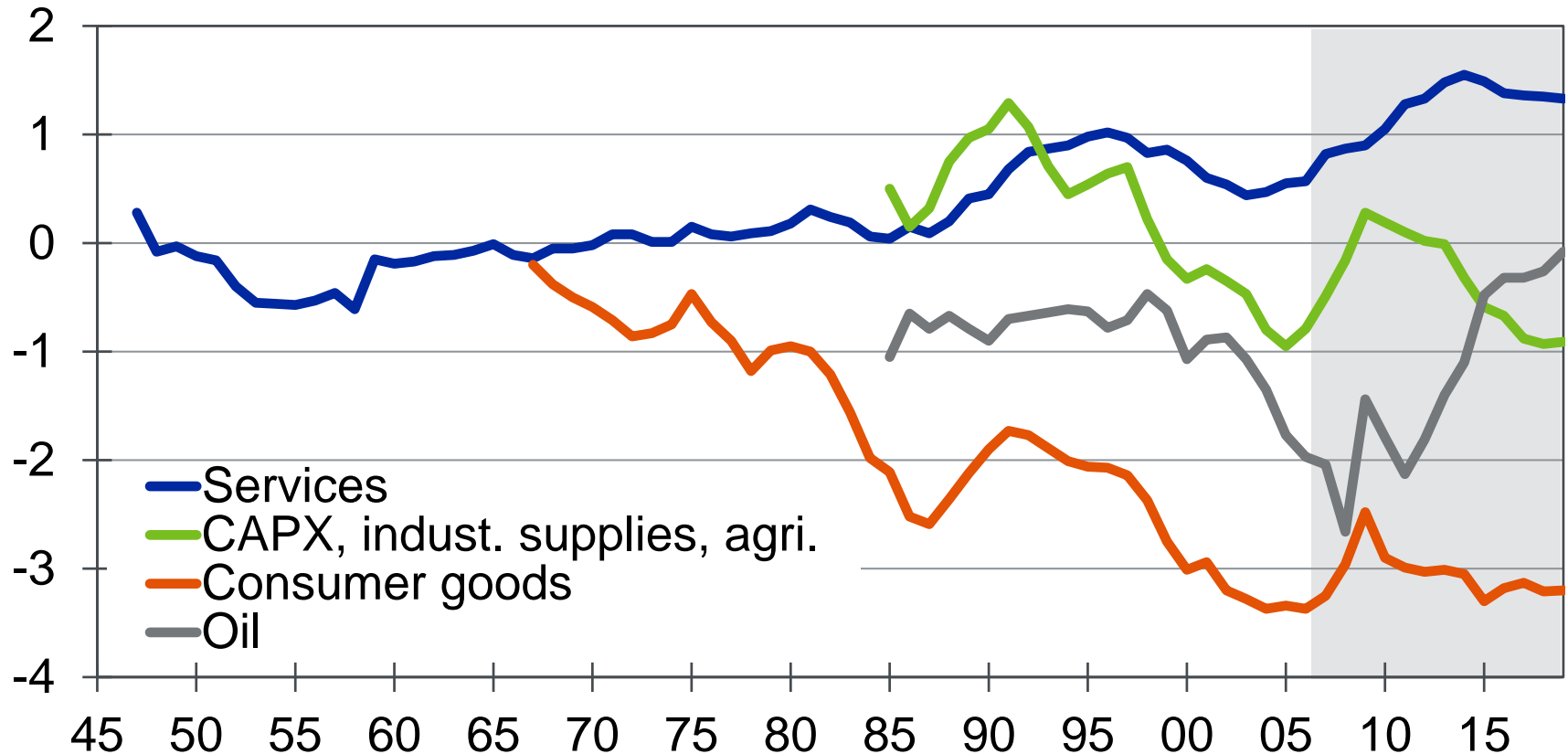
U.S. trade deficit as a % of GDP



Sources: BEA, Moody's Analytics

...Will Cost American Jobs

U.S. trade balance, % of GDP



Sources: BEA, Moody's Analytics

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