Trump's Tariffs Capture a Plethora of Historic Mistakes

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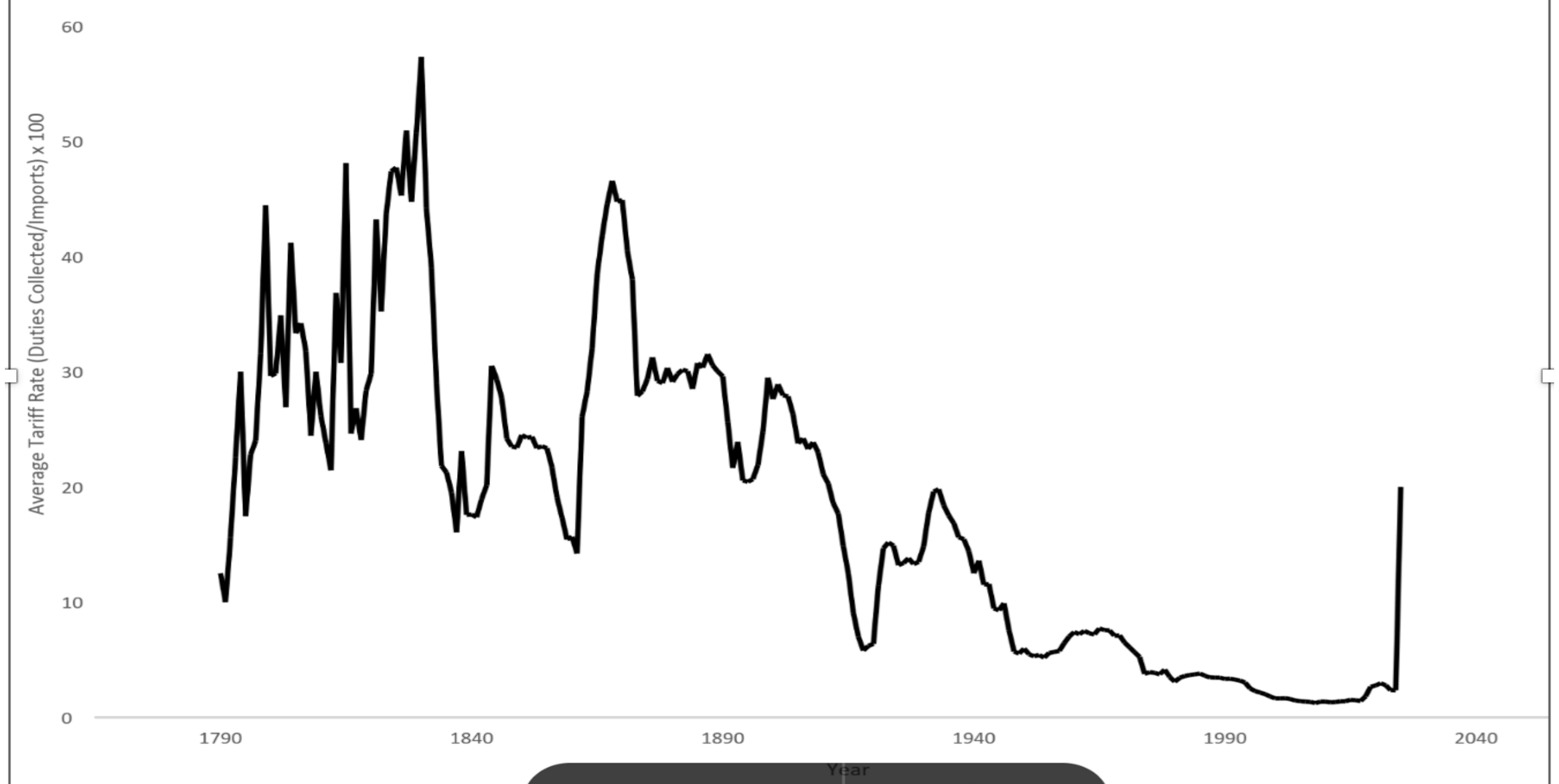
Average U.S. Tariff Rate, 1790 to Present



Sources: 1790-2000: Historical Statistics of the United States; (2000-2024): U.S. imports for consumption, duties collected, and ratio of duties to value, 1891-2024 (Table 1) US International Trade Commission. 2025: author's estimate

Chris Meissner, From One to Many: The Global Economy Since 1850, Oxford University Press, 2024

Ignoring an Abundance of Historic Analogies

- Trump is a mercantilist who views the world as a zero-sum game
- He wants to restore U.S. manufacturing as it was in the mid-20th C
- He believes in import substitution like Nehru's India and Prebish of Argentina
- Like Smoot-Hawley, Trump's tariffs provoke retaliation and threaten global recession
- In limited government 19th C, tariffs were used as protection and were a large portion revenues, but are no panacea now
- Trump aims to end 2nd era of globalization that has featured emergent power China and hollowing out of U.S. manufacturing
- This will isolate U.S.

Trump's Compounded Misguidance and Miscalculations

- Doctrines of mercantilism, perception of world as zero-sum game and maximizing balance of trade surplus refuted by Adam Smith's Wealth of Nations and Ricardo's Law of Comparative Advantage
- Infant industry argument (Hamilton) led to protected monopolies and rent seeking
- Tariffs' revenues would be insufficient to finance current deficits and would harm economy and generate significant inefficiencies
- Hope of returning to mid-20th C era of labor and capital-intensive U.S. manufacturing makes no sense—ignores technologic advances and U.S. comparative advantages and services
- The U.S. benefits from intl trade and relies on capital inflows to finance innovations; tariffs address symptoms and not causes of U.S.. problems

Historical Perspective: 1st Era of Globalization

- Free trade movement in UK (repeal of Corn Laws in 1846 and Chevalier Treaty of 1860), rise in intl trade benefit UK, Europe, U.S.
- U.S. ran large trade and current account deficits during industrial revolution 1865-1914 when rapid growth was driven by capital investment, productivity, and immigration
  - Imports of capital goods and financial capital inflows were critical to economic progress
- Pre-WWI backlash: U.S. workers felt threatened by immigration; Europe landowners threatened by New World agriculture
- Lead to tariffs and restrictions on immigration (U.S., Canada, etc.)

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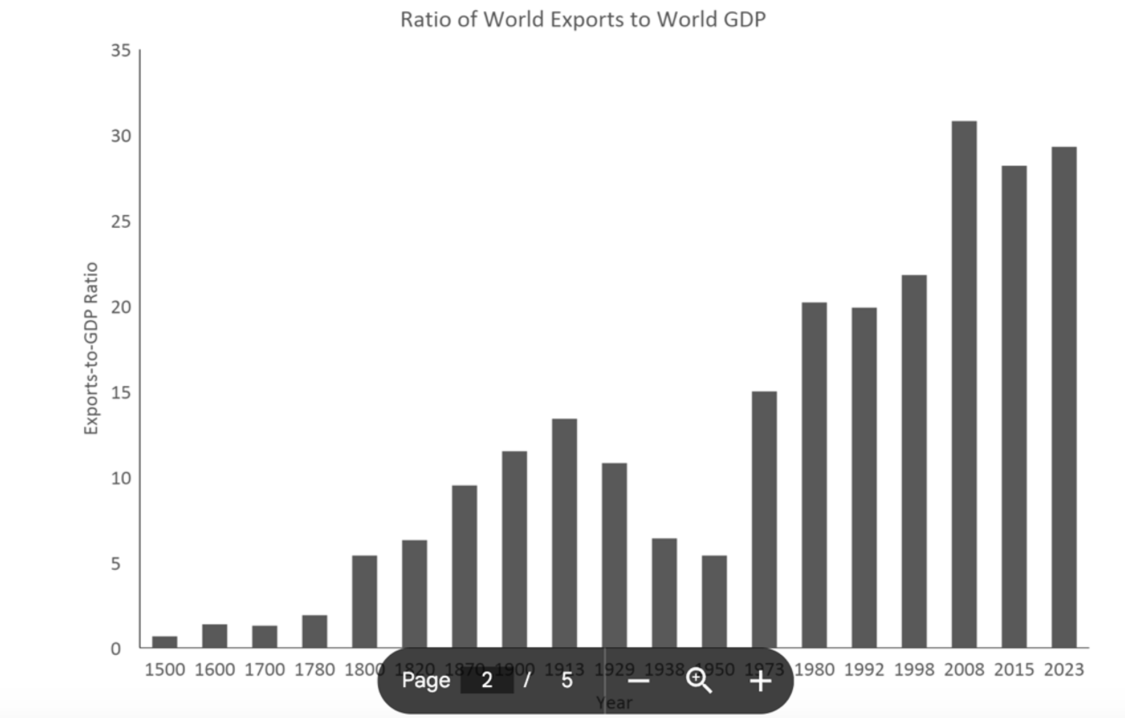
World Exports/World GDP , 1500 - 2023



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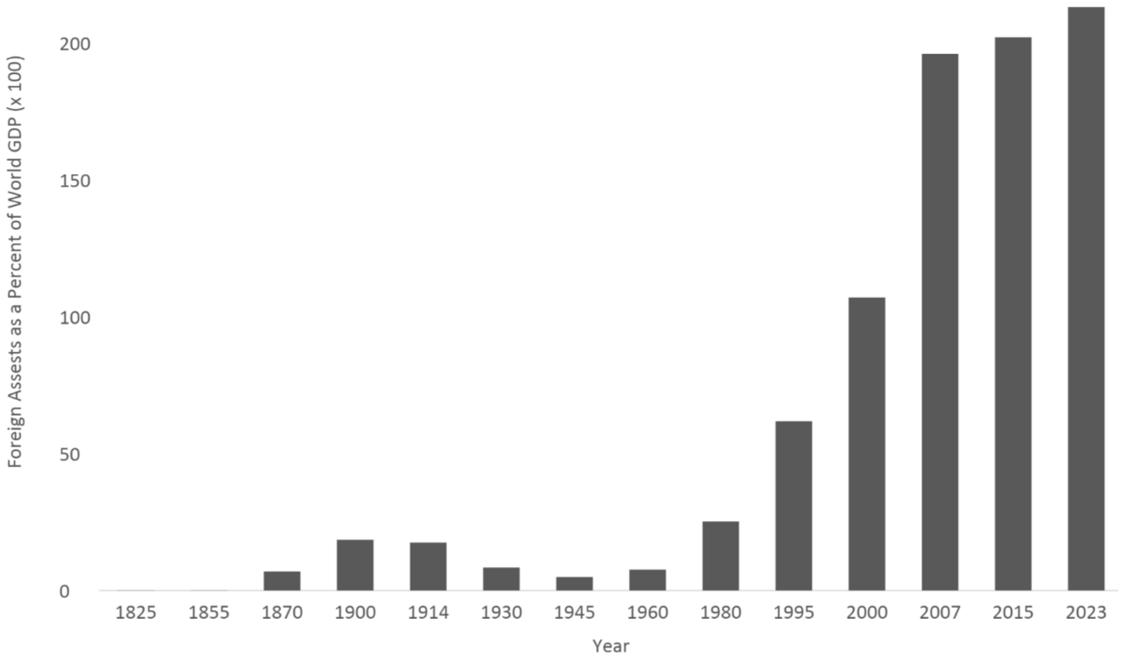
Foreign Assets/World GDP, 1825-2023



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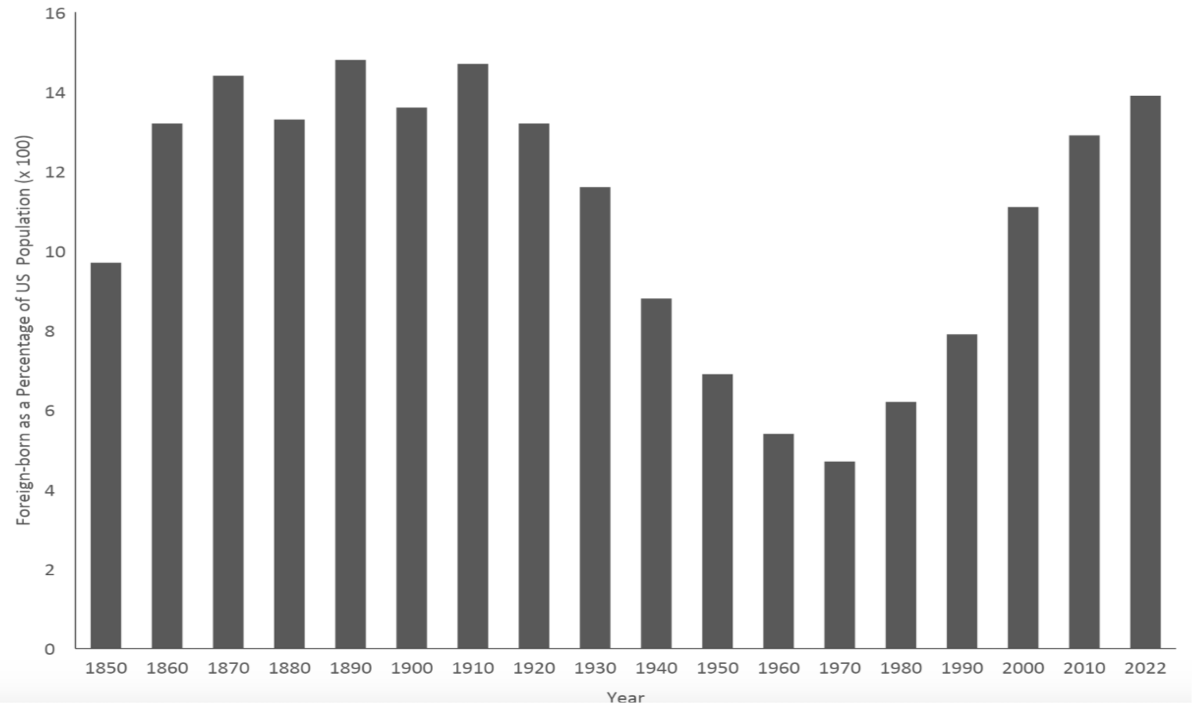
Foreign Born Share of U.S. Population

- In addition to tariffs, will Trump's immigration policies end the favorable era of rising foreign born share of U.S. population?

Foreign Born in the US (share of population), 1850 - 2022



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International Trade Interrupted

- Capital controls and other restrictions during WWI
- Post WWI: Fordney-McCumber Act of 1922 (14% on all U.S. imports) and then Smoot-Hawley (20% high)
- Leads to retaliation by Canada and creation of new trading blocs that exclude U.S. (Ottawa Agreement of 1931)
- Great Depression and collapse in global trade

Second Era of Globalization

- Booming trade and global growth; U.S. advances
- U.S.-led intl reforms: GATT, Bretton Woods, IMF, World Bank
- Notable departures:
- Import substitution (Raul Prebish of Argentina)--Latin America's economies stagnate under tariffs
- Ditto India and select other Less Developed Nations
- Their economies floundered

Trump's Policies Aim to Change World Order

- In addition to tariffs, Trump favors intervention into markets to achieve desired outcomes for US dollar and interest rates
- Wishes to maintain USD as world's reserve currency but favors a weak USD to aid U.S. exporters
- Favors low bond yields and wants ability to influence Federal Reserve
- Changes in U.S. policies and tone alter perceptions of U.S. and its global role:
  - Cuts in U.S. subsidies to European defense and soft-dollar subsidies to LDCs
  - Belligerence toward allies and U.S. backing out of global trade agreements
- New world order; new alliances would form, isolating the U.S. as they did in 1930s

Tests for Economy, Markets and Credibility

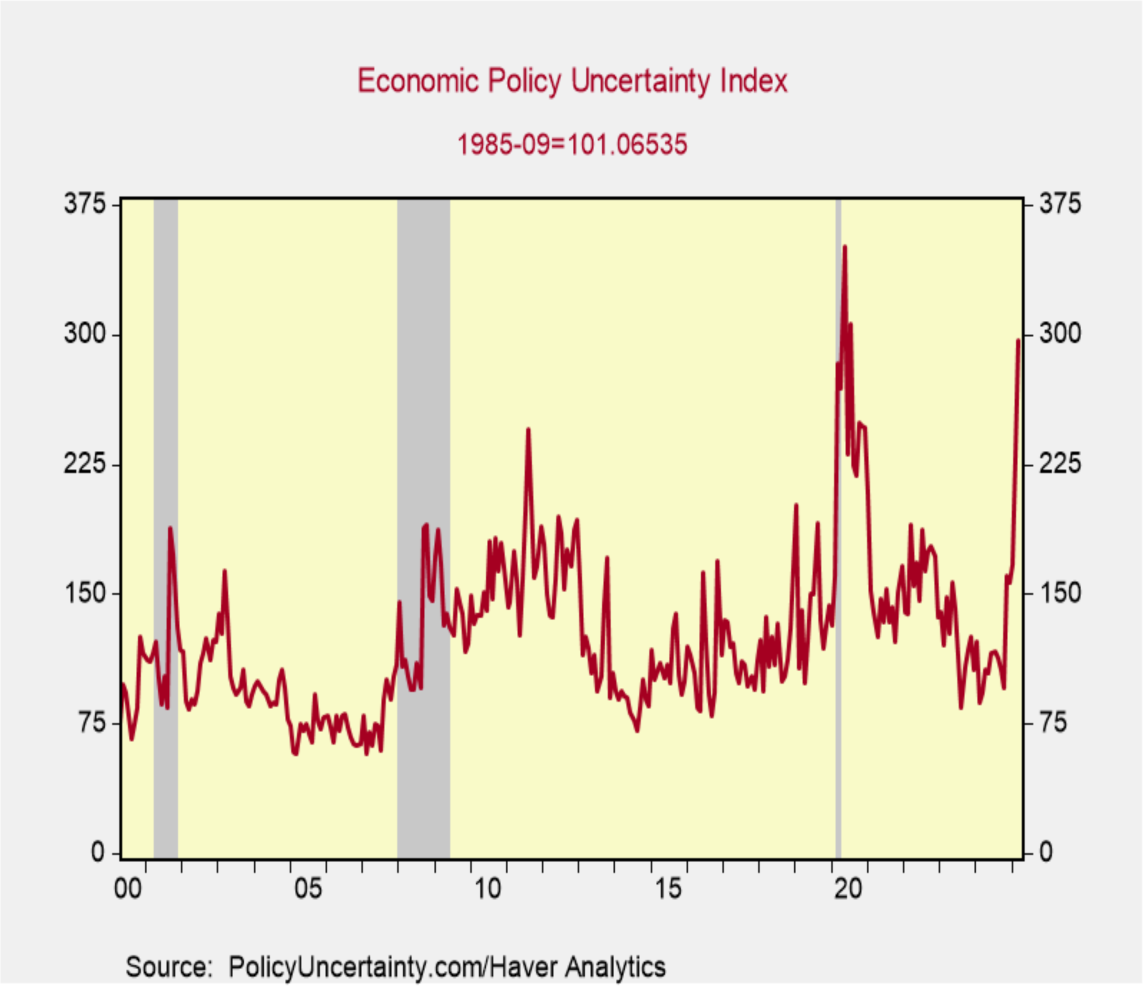
- Markets appropriately price in expectations of U.S. recession and lower profits
- Current tariffs on imported goods = $820 bil or 2.8% of current GDP (145% on China minus Phones, etc.; 10% on global; 25% on steel + aluminum); 25% of auto imports)
- Impact on real economy more than tax of same amount, reflecting heightened uncertainties + retaliations
- Trump's erratic behavior and policymaking has spiked harmful uncertainty
- Wide uncertainties about path of policies and impacts on real economy and inflation

Effective Tariff Rates and Uncertainty

Average Effective Tariff Rates By Country of Origin

Origin Country	Import Share	Tariffs 2024	January-March 2025	All 2025 Tariffs (Including April 9)
EU	18.5%	1.2	4.4	10.0
Mexico	15.5%	0.2	10.4	10.4
China	13.4%	10.7	31.4	135.9
Canada	12.6%	0.1	8.6	8.6
Japan	4.5%	1.5	10.4	15.8
Vietnam	4.2%	3.9	6.4	15.3
South Korea	4.0%	0.2	10.8	15.4
India	2.7%	2.4	4.1	11.2
UK	2.1%	1.0	6.3	12.1
Switzerland	1.9%	0.6	1.0	6.7
Thailand	1.9%	1.6	3.9	12.6
Malaysia	1.6%	0.6	3.5	10.2
AETR	**100.0%**	**2.3**	**9.9**	**27.5**

Marina Azzimonti, et al, Tariff Update: Incorporating the April 9 Announcements, Federal Reserve Bank of Richmond



Tariffs on Collision Course with Fed's Dual Mandate

- Hits to real C & I harm economic growth, raises unemployment rate
- Lowers real expected rates of return and real interest rates, raising Fed's current real policy rate
- Temporarily boosts inflation
- Doesn't add to persistent inflation unless inflationary expectations rise and become embedded in wage & price setting behavior
- Fed should not respond to policy-induced negative shock
- But it most likely will lower interest rates in response to higher unemployment

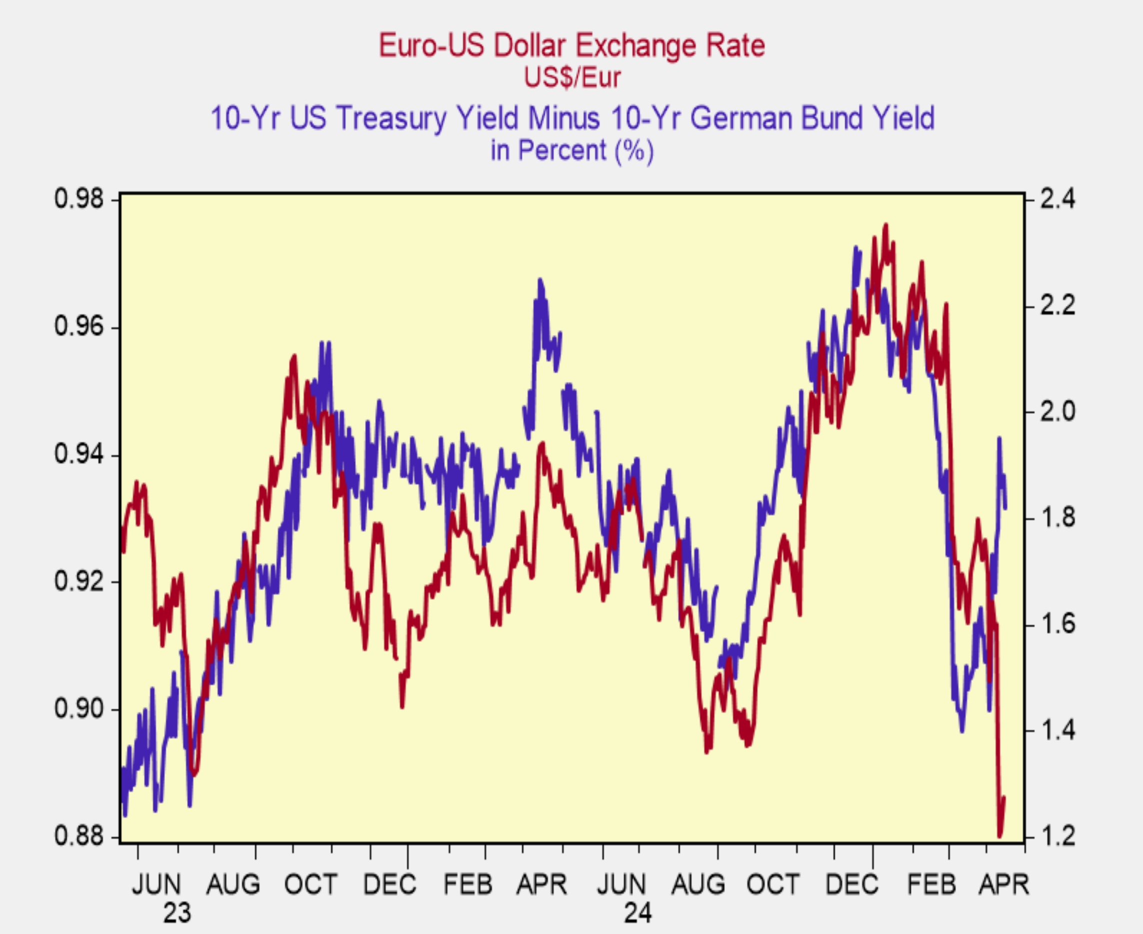
U.S. Credibility and Fiscal Burdens: A Vulnerable Weak Link

- Concerns about loss of U.S. government credibility/reliability and rising U.S. debt burdens are a potentially a toxic mix
- A material loss in credibility could jeopardize U.S. Treasuries as a safe-haven asset, putting U.S. debt and current account deficit at risk
- The loss of credibility reduces risk-adjusted expected rates of return on USD-denominated assets and has resulted in a falling USD
- This may reduce demand for U.S. debt securities at same time Treasury issuance is rising rapidly and the Fed is gradually reducing its ownership of Treasuries

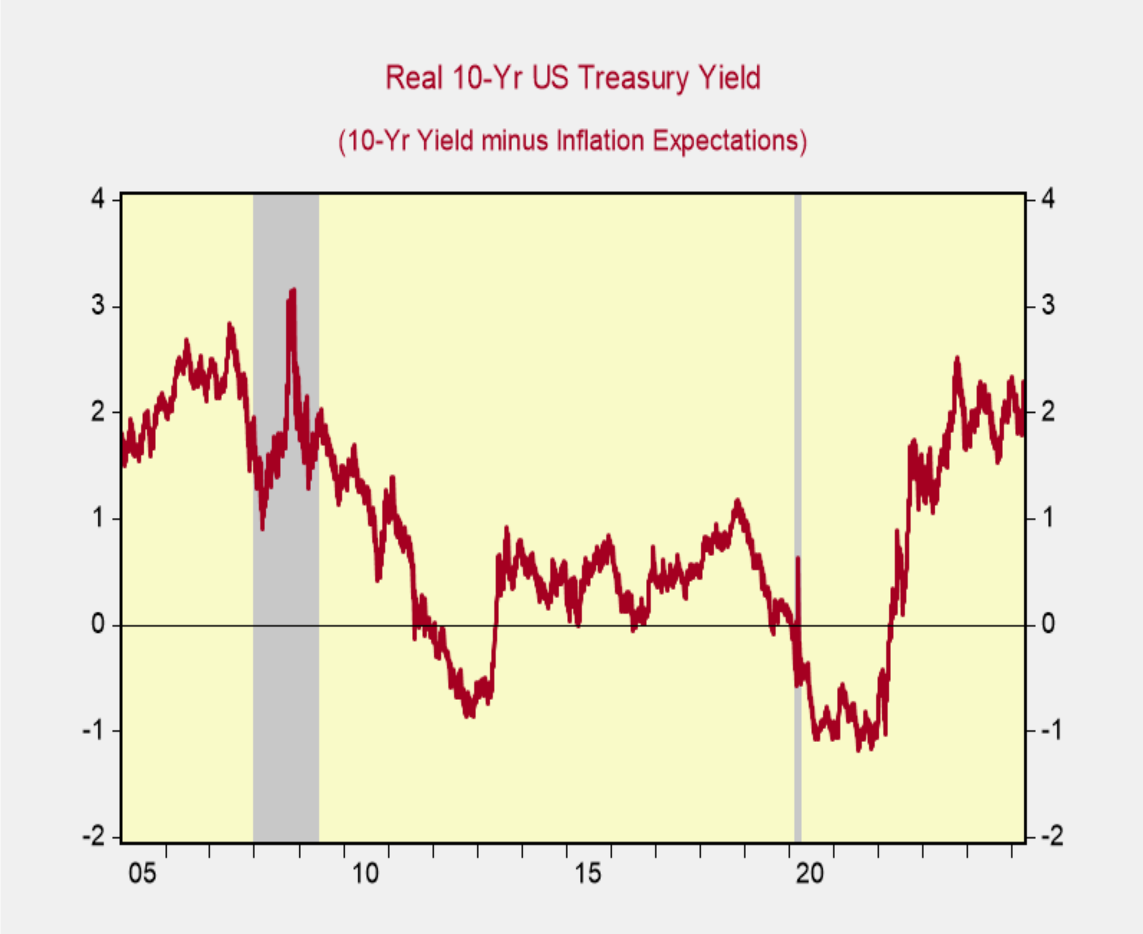
Credibility and Market Behavior

- Foreigners own 1/3rd of all outstanding publicly-held debt
- Market and real U.S. Treasury yields remain higher than other leading sovereign debt, but
- The sharp declines in the USD and recent spike in Treasury yields are potentially alarming
- Exorbitant privilege could go in reverse
- It takes a long time to build reputation and credibility but little time to destroy it (Ben Franklin)
- Highly undesired outcome if Fed is forced to stabilize markets

Interest and Exchange Rate Conditions



Source: Wall Street Journal/Haver Analytics



Source: Haver Analytics

Scenario Analysis

- Scenario 1. **Best outcome: mild negative**. 10% tariffs, negotiations reduce tariffs and trade barriers, economic slowdown/mild recession (prob=10%)
- Scenario 2. **Less-Worse Case**: current tariffs (roughly 25%), moderate retaliation and recession; ongoing uncertainties & distortions to production => moderate hit to longer-run potential growth (prob=75%)
- Scenario 3. **Worse case**: 25% tariffs + loss of U.S. credibility and reputation lead to U.S. Treasury debt and financial crisis with sizable stock declines; U.S. isolation and material harm to potential (prob=10%)
- Scenario 4. **Worse-Worse case**: Scenario #3 plus trade war with China escalates plus U.S. deports millions of immigrants and severely cuts U.S. government funding of research…U.S. exceptionalism erodes sharply (prob=5%)
- Probabilities are speculative and subject to change