

When Trump's tariffs backfire

By Hans Peter Schupp | Guest writer in Das Investment
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Donald Trump loves tariffs. His opponents regularly explain why this is not a good idea from an economic perspective: it is the importer who pays the tariff. This places a burden on businesses and consumers in his own country. According to Yale University's Budget Lab, the average statutory US tariff rate stands at 11.0 per cent. This permanently adds an estimated 0.7 per cent to consumer prices – for an average household, that amounts to around 1,100 US dollars a year. This is precisely where the first irony of 'America First' lies: a policy intended to strengthen America initially exacts a high price from the Americans themselves.

The political response to this is often: retaliatory tariffs. Yet economic logic does not change depending on the nationality of those imposing them. Retaliatory tariffs also make imports more expensive. They force businesses and consumers to opt for more expensive alternatives. This effectively turns one mistake into two.

Retaliatory tariffs do not solve the problem

Politically, however, tariffs can still be tempting, as political and economic logic are not one and the same. Tariffs demonstrate the state's ability to take action and generate revenue for the state. The IMF estimates that the higher US tariffs will generate government revenue of around 0.75 per cent of GDP in the short term. At the same time, they will reduce output by around 0.5 per cent. This may look tempting for the public purse, but less so for the economy as a whole.

In Europe, too, calls for greater state intervention are growing louder. This is reminiscent of 17th-century mercantilism. Then, as now, the promise is to strengthen domestic industry. The US is attempting to use tariffs to tie production and investment more closely to its own territory. China is promoting strategic industries and creating overcapacity that is flooding the European market.

Must Europe follow suit? At the end of July, the EU suspended its planned retaliatory measures against the US indefinitely. This need not be a sign of weakness. Anyone who responds to every American tariff with a counter-tariff risks shooting themselves in the foot.

Competitive pressure makes you stronger

The better response might be to make use of the pressure to adapt. A fall in exports is painful in the short term. In the long term, however, it forces companies to tap into new markets, become more efficient and use capital more productively. Germany is familiar with this mechanism from the pre-euro era: the strong Deutschmark meant constant competitive pressure for the export industry.

For Europe, Trump's trade policy could accelerate adjustments that have been put off for years. These include investment in infrastructure, energy, digitalisation, defence and industrial capital stock. Therein lies the second irony: the attempt to strengthen America through protectionism could, in the long term, strengthen its competitors.

Less trading, less financing

Fewer exports also mean fewer real goods in exchange for American IOUs. This is by no means insignificant for a country with a current account deficit of 3.7 per cent of GDP and gross public debt of 123.9 per cent. Ironically, 'America First' could lead to Trump's trading partners not only supplying America with fewer goods, but also tending to finance its deficits to a lesser extent.

For investors, the selection of individual companies is becoming increasingly important. The key factor is how resilient a business model is to tariffs, supply chain risks and political intervention. This is precisely where a fundamentally oriented, valuation-driven investment approach comes into play. The focus is on the company behind the share: is it trading at a price that underestimates its long-term earning power? The new mercantilism will produce winners and losers. For active investors, this is a call to take a closer look.

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