Assessing Trump Trade Policy

A Year of Rolling Tariffs, Macro Unknowns and FX Volatility

Bill Campbell | February 2025

As most emphatically evidenced in his tariff announcements, President Donald Trump has big plans for reorganizing global trade. Here is my take on where markets might be headed as the Trump administration embarks on a protracted rollout of tariffs and trade negotiations to address a wide array of commercial, fiscal and noncommercial policy objectives.

Analytical Framework

When the 45th president of the United States took the oath of office as the country's 47th president, my analytical framework for tariffs started with the question of whether President Trump's approach would be transactional, with tariffs as a bargaining device to negotiate new arrangements with foreign governments. Or would they be structural, with the imposition of tariffs being a foregone decision to more or less permanently curb imports to the U.S. for strategic reasons, such as the establishment of a revenue source for the federal government or narrowing trade deficits with countries whose governments he perceives as intransigent in unfairly limiting U.S. exporters access to their markets? It has become clear that the Trump administration intends to use tariffs to achieve a broader set of objectives.

I still believe the fundamental question of the tariffs remains which initiatives will be transactional or structural. However, underneath that either-or categorization, I further differentiate among types of tariffs. These include tariffs aimed at achieving national security versus negotiating leverage, and those that are reciprocal and thus more structural in nature. The latter would include tariffs aimed at redressing country-to-country trade imbalances such as with China. I also see a hybrid category in sectoral and currency tariffs that could fall into both the transactional and structural categories.

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Source: DoubleLine

National Security and Negotiating Leverage

The administration's first move on tariffs encompassed national security issues, including border-, immigration- and drug-related concerns. On Feb. 1, President Trump signed executive orders imposing tariffs on imports from Canada, Mexico and China. The tariffs on Canada and Mexico were subsequently delayed 30 days (until March 6) following negotiations and commitments by the Canadian and Mexican governments to enhance security on their respective borders with the U.S. Mexico agreed to the deployment of 10,000 National Guard troops to the Mexico-U.S. border, efforts to combat drug trafficking and collaboration with the U.S. on border security and immigration. Canada agreed to enhance coordination with U.S. law enforcement, with increased information-sharing, designation of drug cartels and terrorists and appointment of a "fentanyl czar" to address the opioid crisis.

Tariffs are also being used for negotiating leverage. To date, the example par excellence is the president's successful threat of tariffs in response to Colombian President Gustavo's refusal to allow U.S. deportation flights to return Colombian nationals to his country, a position that President Gustavo quickly reversed. By their nature, these tariffs are transactional. If a nation addresses Washington's demands, the tariffs can be avoided, as in the case of Colombia, or lifted.

Reciprocal Tariffs

On Feb. 13, President Trump signed a memorandum directing his administration to conduct a comprehensive review of tariffs and nontariff barriers imposed on U.S. exports by trading partners.[1] The plan aims to counter nonreciprocal trading arrangements by determining equivalent tariffs for each foreign trading partner. In addition, President Trump stated that value added taxes, which are widely used in Europe, will be considered tariffs under his reciprocal tariff plan. I view these tariffs as structural, as they are unlikely to be removed once implemented.

Not only has the White House announced the use of tariffs to "correct longstanding imbalances in international trade and ensure fairness across the board,"[2] the administration also plans to impose them to generate fiscal revenues for the U.S. To this effect, the president signed an executive order to create an External Revenue Service on the first day of his return to the Oval Office:

"(b) The Secretary of the Treasury, in consultation with the Secretary of Commerce and the Secretary of Homeland Security, shall investigate the feasibility of establishing and recommend the best methods for designing, building, and implementing an External Revenue Service (ERS) to collect tariffs, duties, and other foreign trade-related revenues."[3]

For these reasons, we view reciprocal tariffs as structural.

Sectoral Tariffs

On Feb. 12, President Trump signed executive orders to restore and expand Section 232 tariffs on steel and aluminum imports.[4] This order reinstated a 25% tariff on steel imports; increased tariffs on aluminum imports to 25% from a previous 10%; and eliminated exemptions for countries like Argentina, Australia, Brazil, Canada, Japan, Mexico, South Korea, Ukraine and the United Kingdom as well as the European Union.

President Trump has recently announced plans to impose additional sectoral tariffs on automobiles, pharmaceuticals and semiconductors. He plans to set tariffs at approximately 25% for automobiles (up from 2.5%), 25% or higher on imported pharmaceutical products and 25% on semiconductor chips. These tariffs are expected to go into effect in early April. The U.S. trade representative will be the official spearheading the sectoral and reciprocal tariffs. Thus, their implementation had likely been deferred pending the Senate's confirmation of Trump's nominee, Jamieson Greer, which occurred Feb. 25.

I regard sectoral tariffs as a hybrid of both structural, with the aim of repatriating manufacturing of these products to the United States, and transactional. President Trump posted on Truth Social on Feb. 15: "It is fair to all, no other Country can complain and, in some cases, if a Country feels that the United States would be getting too high a Tariff, all they have to do is reduce or terminate their Tariff against us. There are no Tariffs if you manufacture or build your product in the United States."[5]

China

China deserves a distinct discussion, as the White House is likely to follow a much more structural path toward the world's second largest economy. In President Trump's first term, China was the primary focus of his tariffs, culminating in a so-called Phase 1 trade deal. This marked a turning point for the U.S.'s stance toward China, from one that saw the nation as a benevolent trading partner to a strategic competitor, a posture that continued under the Biden administration.[6]

Trump 2.0 is likely to continue the structural approach to China. On Feb. 1, the president signed an executive order imposing a 10% tariff on all goods imported from China. In his Senate confirmation hearings, now-Secretary of Commerce Howard Lutnick testified that China had found ways to evade U.S. export controls, and he promised to address these issues with additional export controls and tariffs. The president himself has consistently criticized China's trade practices as unfair and harmful to American interests. Thus, in my view, Washington will treat China as a structural-trade adversary for the duration of President Trump's second term.

For its part, Beijing has implemented retaliatory tariffs, including a 15% tariff on U.S. coal and liquefied natural gas and 10% tariffs on U.S. crude oil, agricultural machinery and large-displacement vehicles. In addition, China implemented export controls on rare earth minerals, including tungsten, indium and molybdenum and filed a formal complaint with the World Trade Organization against the Trump tariffs. This is likely only the beginning of a tit-for-tat escalation in the trade relationship between the U.S. and China. I am monitoring this potentially open-ended contention between the world's first and second largest economies for spillover effects on global growth and inflation.

Currency Manipulation

U.S. Treasury Secretary Scott Bessent has indicated that countries that manipulate their currencies also will be tariffed. "We're going to come up with what is the equivalent of ... what I would call a reciprocal index: country by country, the outstanding tariffs, non-tariff, the trade barriers and currency manipulation," Bessent told Fox Business Network.[7] The Treasury periodically issues a report on macroeconomic and FX policies of America's trading partners. In the latest report, the Treasury did not label any nation a currency manipulator, but the department did identify countries it is monitoring: China, Germany, Japan, South Korea, Taiwan, Singapore and Vietnam.[8]

The Trump administration's currency policies with respect to different countries can be both transactional and structural depending on each country and if the administration is seeking to achieve additional objectives beyond trade. The comments by the Treasury secretary show the different potential purposes of tariffs are not mutually exclusive. I think tariffs can accomplish many of these goals, but the administration is unlikely to quickly complete its tariff policy. Instead, a steady rollout of tariffs over the coming quarters is more likely as the administration assesses these different tariff agendas in various parts of the globe.

Economic and Market Implications

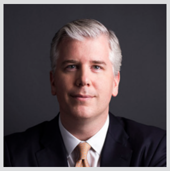
Tariffs appear to be President Trump's favored policy tool for accomplishing multiple international and domestic policy objectives. It appears to me that tariffs will be executed in a layered approach over time rather than in a one-and-done blitz. Targeted countries' responses to new U.S. tariff policies will also need to be watched closely. As China has already done, some might fire back with their own tariffs and other countermeasures; others might come to the dealmaking table. Such second and third derivative effects only add to the idea of nascent global trade disorder before the emergence of a new order, with layers of altered negotiated accords and adversarial relationships. This transition will heighten global economic uncertainty. It will be difficult for companies to engage in robust international investment planning, a potential drag on growth. President Trump's domestic economic policy, however, seeks to stimulate investment, which might help offset some of the near-term uncertainty.

The effect of tariffs on inflation also remains an open question. On the first pass, tariffs can be seen as inflationary if their costs are fully passed through to consumers by companies in the form of price increases. Given competitive market pressures, companies will often not be able to fully pass through their tariff-related costs. If growth outcomes turn out to be slower than currently expected, this also could reduce the impact of tariffs on inflation. Finally, some components of inflation are continuing to ease from very high levels. If disinflation persists, this by definition would help to offset the impact of tariff pass-throughs. For example, I think disinflation in shelter prices has a way to go. To be sure, inflation remains a risk that needs to be monitored closely, and DoubleLine will update the firm's inflation assessments as relevant data prints unfold.

The U.S. dollar is the most obvious outlet valve for markets to react to tariff announcements and rollouts, as currencies can be used by countries to offset their impact. By allowing its currency to devalue by the amount of a tariff, a country can effectively offset the economic impact from a tariff. I expect currency volatility to remain elevated as serial U.S. tariff announcements and possibly even countertariff announcements by affected trading partners roil markets in coming quarters. Tariff announcements have tended to support the dollar, while brief periods of dollar easing have followed decisions to delay tariffs or the reaching of bilateral agreements between the U.S. and targeted countries. Once the bulk of tariffs has been implemented, likely by the middle to end of the year, there could be a bigger dollar trade as the downside from trade policy probably will have been more fully priced in. In addition, the potential for a currency accord would also provide an interesting opportunity for investing in nondollar assets, but this, too, is unlikely until later in the year at the earliest.

In the quarters ahead, international investors and global business leaders face a high level of uncertainty around the ultimate impact of not only U.S. tariff policies but the responses to those policies by affected countries. Further, trade is hardly the only issue subject to a dramatic if not drastic rewriting of the rules of play for the U.S. Along with global trade, new immigration, budget, regulatory and geopolitical policies under the new administration all mean that the dispersion of potential economic outcomes remains wide. Until market participants gain more information about the details of these policies, I expect many markets to remain in their current ranges. This creates an environment where high-quality carry trades should continue to perform well.[9]

At DoubleLine, we acknowledge these uncertainties and construct our multi-sector fixed-income portfolios to perform under different scenarios, including outcomes that differ from our base-case scenarios. This includes a mix of assets from Treasury bonds, corporate bonds, structured products, international bonds or some subsets of those sectors. We also believe that now, more than ever, active management will be key to navigating markets. Within each of the categories listed, we are looking for idiosyncratic dislocations caused by the policy uncertainty to find value in specific bonds that show attractive reward-risk ratios. ■



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Endnotes

1. Fact Sheet: President Donald J. Trump Announces "Fair and Reciprocal Plan" on Trade, Feb. 13, 2025. https://www.whitehouse.gov/fact-sheets/2025/02/fact-sheet-president-donald-j-trump-announces-fair-and-reciprocal-plan-on-trade/
2. Ibid.
3. America First Trade Policy, White House memorandum, Jan. 20, 2025. https://www.whitehouse.gov/presidential-actions/2025/01/america-first-trade-policy/
4. Fact Sheet: President Donald J. Trump Restores Section 232 Tariffs, Feb. 11, 2025. https://www.whitehouse.gov/fact-sheets/2025/02/fact-sheet-president-donald-j-trump-restores-section-232-tariffs/
5. "President Trump looks to bring manufacturing back to US with tariffs," Fox Business, Feb. 18, 2025. https://www.foxbusiness.com/economy/president-trump-looks-bring-manufacturing-back-us-tariffs
6. The Biden administration pursued a three-pronged China strategy of strengthening alliances and building new partnerships, investing in industrial policy at home and limiting technology exports to that country. For a detailed retrospective on Biden policy on China, see "How will the Biden administration's China policy be remembered?" Ryan Hass, The Brookings Institution, Feb. 3, 2025. https://www.brookings.edu/articles/how-will-the-biden-administrations-china-policy-be-remembered/
7. "US looking at currency manipulation in tariff debate, Treasury chief says," Reuters, Feb. 14, 2025. https://www.aol.com/news/us-looking-currency-manipulation-tariff-130412729.html
8. Report to Congress: Macroeconomic and Foreign Exchange Policies of Major Partners of the United States, U.S. Department of the Treasury, Office of International Affairs, November 2024. https://home.treasury.gov/system/files/136/November-2024-FX-Report.pdf
9. A carry trade is any strategy by which an investor borrows capital at a lower interest rate to invest in assets with potentially higher returns. As a hypothetical example, if country A had interest rates set at 0% and country B had interest rates at 5%, an investor could borrow money in country A and buy the one-year government bonds of country B to earn an annual return of 5% if – and given the volatility of foreign exchange rate this is an important "if" – the exchange rate between countries A and B does not significantly change over the year.

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