4-4-25

WSJ Print Edition

The effective U.S. tariff rate is now higher than after Smoot-Hawley.

Trump and His 'Little Disturbance'

REVIEW & OUTLOOK

President Trump said there would be "a little disturbance" from his tariffs, but how does he define little? The stock mar--ket Thursday suffered its worst day since the government shut down the economy in March 2020. Not to worry, the White House says tariffs will eventually be worth the pain. Feeling better?

The S& P 500 fell 4.8% and the Nasdaq 6% in reaction to Mr. Trump's Wednesday tariff announcement of the largest tariff increase in a century. The biggest market casualties were retailers and manufacturers such as Apple (-9.3%), Nike (-14.4%) and Gap (-20.3%). Oil prices, the U.S. dollar and the 10-year Treasury yield also fell, likely signaling slower growth expectations.

Markets around the world spent Thursday absorbing the historic magnitude of Mr. Trump's tax on commerce. Evercore ISI estimates that Wednesday's news will raise the U.S. effective tariff rate to 24%, and 27% if he goes ahead with the sectoral tariffs he promises on drugs, copper and more. That's higher than after the Smoot-Hawley tariff of 1930.

Worse is the bizarre, slapdash way the White House calculated the tariff rates on individual countries. Everyone will pay 10%. Then the White House appears to have calculated each country's additional tariff rate by dividing its trade deficit with the U.S. by its exports to the U.S. This rate was then cut in half for most countries, which Mr. Trump calls a "discount." The discordant result is that U.S. adversaries like Iran (10%) and Venezuela (15%) will pay lower rates than friends in Europe (20%), Japan (24%) and Taiwan (32%).

The trade deficit is a long-time Trump fixation that he sees as a zero-sum game. Trade-deficit countries must be cheating somehow, but then what about countries like the U.K. and Australia that have a trade deficit with the U.S.? Why hit them with a 10% tariff?

The trade balance reflects many factors, including national comparative advantage. We sell things we are better at—services, high-tech goods—and buy things that can be made more cheaply elsewhere. The U.S. also spends more than it saves, which means it imports capital. This is the flip-side of the trade deficit in national accounts, so shrinking the trade deficit will mean less capital coming in.

Yet Mr. Trump claims his tariffs will unleash a flood of new investment in the U.S. Then why is the dollar falling in value (see nearby), recording its worst single-day loss in two years? Our guess is that investors are losing confidence in U.S. economic decisions.

The President complains about foreign currency manipulation, taxes that suppress consumption and non-tariff barriers. But if he wants other countries to open more to U.S. exports, he could negotiate. The stillborn Trans-Pacific Partnership would have reduced Japan's non-tariff barriers.

The Trump tariffs ironically will punish companies that have moved manufacturing out of China to other countries in Southeast Asia, which his first Administration encouraged them to do. About half of Nike's shoes are now made in Vietnam versus 18% in China.

Mr. Trump hits Vietnam with a 46% tariff, which means Nike will have to rethink where to make low-margin shoes. Mr. Trump seems to think they should be made in America. Mr. Trump's tariffs may have the U.S. investing to create jobs in shoe-making when it should invest in AI. This misallocation of capital will not make the U.S. more competitive against China.

The only silver lining we see is that imports from Canada and Mexico are exempt if they comply with the USMCA. But cars and trucks assembled in the two countries will still be taxed 25% on their non-U.S. components.

There is also the not-so-small matter of the rule of law. Mr. Trump justifies his tariffs by declaring a national emergency under the 1977 International Emergency Economic Powers Act. No previous President has used that law to impose tariffs. Mr. Trump is stretching his authority much as Joe Biden did with his student-loan forgiveness.

Congress has circumscribed the President's power to impose tariffs, allowing it on imports that threaten national security (Section 232) or in response to " large and serious" balance-ofpayments deficits (Section 122), a surge of imports that harms U.S. industry (201), and discriminatory trade practices (301).

None of these trade provisions empowers Mr. Trump to impose tariffs on all imports from all countries based on an arbitrary formula. Section 122 lets a President impose tariffs of up to 15% in response to trade deficits, but Congress must approve them after 150 days. Someone should sue to block his abuse of power.

Mr. Trump's tariffs are the biggest policy shock to the world trading system since Richard Nixon blew up Bretton Woods in 1971. As with that decision, Mr. Trump is acting with little understanding about the damage his tariffs will cause. The "disturbance" might not be as little as he imagines.

