Tariffs

Throughout his campaign, President Trump stated that tariffs are needed to help the American economy and to "protect" the country from the "major threat of illegal aliens and deadly drugs". He argued that the tariffs will boost US manufacturing, protect jobs, raise tax revenue, and grow the economy. Tariffs are taxes charged on goods imported from other countries. These taxes are typically passed on to consumers in the form of higher prices. This may result in an increase in the purchase of domestic products which are not subject to tariffs. However, most economists agree that tariffs cause inflation. From 2018 to 2023, tariffs on imported washing machines led to a 34% increase on the price of laundry equipment according to official statistics, before falling once the tariffs expired.

Some experts suggest that these new tariffs could prompt a wider trade war and exacerbate inflation. Capitol Economics said the annual rate of inflation could increase from 2.9% to as high as 4% because of the tariffs.

This may be one of the reasons why interest rates went up in September even after the Fed cut rates because the bond market may have been pricing in the effects of anticipated inflation. Although stocks did not seem to price in the impact of tariffs, on February 2nd when President Trump announced sweeping tariffs against Mexico, Canada, and China, the markets dropped about 2% after all three countries announced retaliatory tariffs on American products.

However, those losses abated once Trump announced that he was holding off on the tariffs against Mexico and Canada after both countries agreed to beef up border security. For now, the US and China have announced tariffs against each other. Negotiations among the countries are ongoing. However, if those negotiations do not result in a final agreement tariffs will make prices increase and the Federal Reserve may have to increase interest rates to fight that inflation like they did in 2022. You may recall that when the fed raised rates both the S&P 500 and the U.S aggregate bond index were both down almost 20% that year.

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Sincerely,
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