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Trade Update: Expect the Unexpected

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We have the following comments about President-elect Trump's posts last night on Truth Social regarding tariffs on China, Mexico and Canada:

- We doubt that Trump's call for an additional 10% tariff on Chinese products due to the fentanyl crisis will be the final word on the matter. In our view, higher tariffs on Chinese products should be expected that come closer to his ~60% number he touted during the campaign.

- While Trump mentioned that all products from China will face the announced 10% tariffs, we still expect to see exemptions for consumer- facing products in any subsequent tariff announcement.

- With regard to Canada and Mexico, Trump is also calling for across-the-board tariffs but set at 25%. These levels are likely short-lived as the incoming Trump administration will have to work with these two countries and China to address border issues. This would be especially true if Trump provides few exceptions to tariffs, though despite his post, we think that Trump will provide some exceptions. For example, Canada's largest export to the U.S. is oil. We doubt Trump wants gas prices to rise due to tariffs on Canadian oil.

- In response to the post, we expect Canada and Mexico to immediately begin negotiations with the incoming Trump team, hoping to either reach an agreement before January 20 or soon thereafter. We would expect similar engagement by China as well.

- We believe the suggested tariffs violate the USMCA, but that legal obstacle probably doesn't matter to Trump, who is likely to impose tariffs anyway until his administration reaches an agreement with Canada and Mexico.

- While Trump mentioned immigration last night in his post, recall that one of his biggest concerns with Mexico is country-of-origin issues. He has long complained that Chinese goods are being exported into Mexico, then slightly modified, and ultimately sent to the U.S. Sooner or later, Trump is going after the country-of-origin issues.

- To put it in context, Mexico, China and Canada respectively are the United States' largest trading partners. In 2023, Mexico became the largest importer to the U.S., selling $475 billion worth of goods and services. China, who had been first, was second at $437 billion. Canada was just behind at $419 billion.

- In addition, importantly, according to Semafor, 79% of Mexico's exports went to the U.S., while 75% of Canada's did and only 15% of China's.

- Trump could cite his powers under the International Emergency Economic Power Act (IEEP) to impose these tariffs. Recall he used Section 301 of the U.S. Trade Act of 1974 against China during his previous administration. He has options.

- Separate from the above proposed tariff levels, we still see tariffs on the rest of the world as still in play next year. However, we think there's a decent chance that there is at least an attempt to add these rest-of-world tariffs to a **tax bill** done under reconciliation as a revenue raiser. However, we doubt they would actually be enacted by a Republican Congress, leaving Trump to act on his own.

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