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PHILEQUITY CORNER

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The tariff sheriff arrives

Trump rattled global markets when he announced tariffs on Canada, Mexico, and China, reigniting fears of an escalating trade war. However, global equities and currencies recovered when Trump paused the tariffs on Canada and Mexico for 30 days.

Pause on tariffs on Canada and Mexico

The pause on the tariffs came as Canada and Mexico agreed to improve border security and implement steps to prevent the trafficking of fentanyl to the US. Canada said that it would implement its \$1.3b border plan and the deployment of nearly 10,000 personnel to protect the border. Canada also put on hold its plan to impose a 25% tariff on \$155b of US goods. Mexico agreed to immediately send 10,000 National Guard troops to the country's northern border to stem shipments of fentanyl and other drugs to the US.

A welcome development

The pause on tariffs on Canada and Mexico is a welcome development for financial markets and the global economy. Canada and Mexico are the top two trading partners of the US with over \$1.6t in total trade. The proposed tariffs are far-reaching and cut across many sectors. Economists fear that an escalating trade war with the US will push Canada and Mexico into recession. After agreeing to a deal with Canada, Trump said, "I am very pleased with this initial outcome, and the tariffs announced on Saturday will be paused for a 30-day period to see whether or not a final economic deal with Canada can be structured."

Tariffs on China take effect

While the tariffs on Canada and Mexico were put on hold, the 10% blanket tariffs on China took effect last week. China exports more than \$400b of goods to the US annually. Among China's top exports to the US are electrical and electronic equipment, machinery, nuclear reactors and boilers, broadcasting equipment and computers, and toys and games.

China retaliates

China said that it would challenge the tariffs imposed by the US at the World Trade Organization (WTO). It also launched an investigation on Google for alleged violations of China's anti-monopoly law. More importantly, China announced 15% tariffs on American coal and liquefied natural gas, and 10% tariffs on crude oil, farm equipment, and some vehicles starting February 10.

Europe is the next target

Aside from Canada, Mexico, and China, Trump mentioned Europe as the next target of his tariffs. Trump said, "They don't take our cars, they don't take our farm products, they take almost nothing, and we take everything from them." Europe exports more than \$500b annually to the US and has a trade surplus of \$160b with the US. Trump claimed that Europe has taken advantage of its relationship with the US. European leaders said that they would respond firmly in a proportionate way. Economists estimate that a trade war with the US would shave off 0.5-1.0% off the region's GDP. Considering Europe's tepid economic growth, a tariff war with the US would plunge Europe into recession.

The power of the tariff

Trump clearly sees tariffs as a negotiating tool. He uses the threat of tariffs to force trading partners to renegotiate trade agreements and other matters. Goldman Sachs said that a full-blown tariff war with Canada, Mexico, and China would add 0.7% to core inflation and slash 0.4% from US GDP. The prospective tariffs were estimated to increase household spending by \$800 to \$1200 per family. Despite the clear risks posed by a tariff war to the US economy, Trump remains undaunted with his tariff pronouncements. He is willing to gamble that tariffs would compel the country's top trading partners to make a deal with the US. Trump said, "You see the power of the tariff. No one can compete with us because we have by far the biggest piggy bank."

Global equities recover as US stocks pull back

Global market sentiment improved after the pause on tariffs on Canada and Mexico was announced. Other sectors and countries recovered as part of a broadening move. The PSEi bounced back strongly from its recent low caused by index rebalancing, marking a potential bottom for Philippine stocks. However, US stocks pulled back due to news on inflation and tariffs. Goldman Sachs warned of correction risk in US stocks due to higher equity valuations, a less friendly macro environment, higher policy uncertainty, tariff moves, and the advent of a new AI competitor in China.

Reciprocal tariffs

Trump said that he was planning to impose reciprocal tariffs on US trading partners. The tariff sheriff has not only targeted China, but also other US trading partners such as Europe and Japan. Trump said that this is part of his pursuit for a fair deal for US consumers. Trump's unconventional ways and unpredictable nature will result in more market volatility in the coming weeks.