



MARKET UPDATE  
March 6, 2018

# OUR VIEW



## President Donald Trump announces plans to impose tariffs on steel and aluminum

President Trump announced a plan to impose 25% tariffs on imported steel and 10% on imported aluminum, following earlier trade actions targeting imported washing machines and solar panels. We have long expected Trump to take action on steel and aluminum, fulfilling a frequent campaign promise. The surprise to us is that tariffs on steel and aluminum will be imposed across-the-board, rather than directly targeting specific countries thought to be “dumping” the metals at below-cost prices. Trump’s statement that “trade wars are good, and easy to win” is a sign that fears about Trump’s protectionist leanings are becoming a reality. Another worrisome indication is the elevation of trade hawk Peter Navarro, author of the book “Death by China,” to a more influential position in the White House.

Tariffs on steel and aluminum may cause more harm than good for American workers, the U.S. economy, and global stock markets. Trump’s assertion about trade wars may be factually flawed, as historical experience provides evidence to the contrary. There may be considerable room to improve current trade pacts, particularly in the realm of intellectual property protection, however, the planned tariffs may be the wrong remedy.

The Wall Street Journal editorial page expressed their viewpoint, saying that tariffs will “make the U.S. an island of higher priced steel and aluminum.” Auto manufacturers, airplane manufacturers, construction companies and defense contractors are among the companies vulnerable to higher input costs. Canned goods manufacturers will also face rising costs. Consumers are likely to pay higher prices as a result, with tariffs in essence serving as a “tax” on consumers. There may also be unintended consequences from an employment perspective, as steel-using industries employ 6.5 million Americans, while steel and aluminum makers employ only 200,000. It is also not a certainty that U.S. steel and aluminum companies will boost payrolls as significantly as hoped. Capital substitution, in the form of robots and automation, is a primary explanation of why U.S. manufacturing output has grown in the past two decades amidst a dramatic fall in manufacturing employment. The benefits of firming prices and volumes may provide more of a benefit to investors in U.S. steel and aluminum companies than to steel and aluminum workers.

Canada, a significant U.S. trade partner, provides 16% of U.S. steel imports and 56% of aluminum imports. South Korea, a vital host to the U.S. military and buffer against North Korea, is the source of 10% of U.S. steel imports. Canada, the EU and the UK have reacted angrily to the announcement, and have promised to retaliate. Canada and China may retaliate against U.S. agricultural products. American agricultural exports to Canada in 2016 reached \$23 billion, and China spent more than \$12 billion on American soybeans. China also owns more than \$1 trillion of U.S. debt and is a major export destination for American planes and autos. China has more leverage against the U.S. than was the case in the early days of China’s emergence as an economic power. China’s exports to the U.S. were more than 40% of Chinese exports in 2000, today less than 25%. In addition, exports are a far smaller percentage of China’s GDP today.

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From the Wall Street Journal editorial page, "This tax increase will punish American workers, invite retaliation that will harm U.S. exports, divide his political coalition at home, anger allies abroad, and undermine his tax and regulatory reforms." Protectionism is a negative for the stock market, and we will be monitoring whether this is an initial negotiating ploy on Trump's part, or whether this is the start of a series of trade actions targeting multiple industries. We'll consider the likelihood that tariffs on steel and aluminum will spark a broader trade war, which would likely impact the global economic outlook, stock markets and inflation negatively. Then we would decide whether to modify asset allocation targets or investment holdings. We will keep you informed about our thinking and will notify you of any portfolio changes. Please contact me or your TFC advisor if you would like to discuss this in more detail.

Sincerely,

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Chief Investment Officer

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