

Potential Implications of a Trade War

Written by Ladenburg Thalmann Asset Management on 4/5/2018

Setting the stage

Before we dive into the implications of the most recent tariffs between the US and China it is best to understand the trading relationship between the two countries today and outline a timeline of what has happened so far. The US has a trade deficit with China of roughly \$375 billion. President Trump has committed to reducing this deficit since he took office. Further, based on a 2017 investigation into unfair trade practices by China, it is estimated that US property theft by China costs the US between \$225 and \$600 billion every year. This is what prompted the US to impose tariffs on imports so far in 2018.

So what has happened recently?

On March 23rd, US import tariffs of 25% on steel and 10% on aluminum took effect. Canada and Mexico were exempt from these tariffs. On April 2nd, China retaliated by imposing tariffs of 15% and 25% on a list of 128 US products worth around \$3 billion of imports. On April 3rd, the US published a list of 1,300 categories of Chinese products that would face a 25% tariff, including high-tech industrials and aircraft parts to name a few. These tariffs affect roughly \$50 billion of imports. Less than 24 hours later, on April 4th, China announced retaliatory tariffs of 25% on 106 US products, including soybeans (the largest US export to China), affecting roughly \$50 billion of imports. This latest levy by China brings the total amount of goods affected by these tariffs to approximately \$106 billion.

Our View:

It is important to understand that the US and China have the largest trading relationship in the world, so there is incentive to reach a fair solution and limit damage to both sides. We believe that threats of trade wars are mostly rhetoric at this point. The US administration seems politically committed to this issue, but the negotiation between the combatants will stretch over the next 6 months before tariffs on either side go into effect. Should a trade war begin, consumers and the stock markets of both nations will be negatively affected, which is not the end goal of either party. However, we may see periods of volatility in financial markets as trade negotiations grind on, especially with the added uncertainty from the Federal Reserve's interest rate policies.

Our investment team's view is to trade on fundamentals and not on politics or market noise. From a fundamental perspective, we remain bullish on risk assets as we continue to experience synchronized global economic growth. The tariffs proclaimed so far should not have a large impact on the domestic economy, as the United States' \$130 billion in exports to China represent just 0.7% of GDP, while China's \$506 billion in exports to the US represented 4% of its GDP last year. While we expect the impact to be minimal at their current magnitudes, we recognize that a trade war between two of the world's largest economies has the potential to escalate into a bigger economic problem as the situation develops. Even though there are many scenarios that could play out from here, if a trade war were to occur, LTAM would view this risk as significant to market volatility and would allocate our portfolios to a more conservative posture.

Although this market outlook has been prepared from public and private sources and data that LTAM believes to be reliable, LTAM makes no representation as to its accuracy or completeness. Investors should bear in mind that past performance is no guarantee of future results and there can be no assurance to achieve comparable results. Investment products are subject to investment risk, including possible loss of the principle amount invested and should review the prospectus before investing. The information and views expressed are given as at the date of the writing and are subject to change. This information is not to be used or considered as an offer or the solicitation of an offer to sell or buy any securities mentioned herein. Ladenburg Thalmann Asset Management Inc. is a registered investment advisor and subsidiary of Ladenburg Thalmann Financial Services Inc. which is traded on the NYSE American: LTS.

STEVEN P. LICHTBLAU

Partner, Private Wealth Advisor
SteveL@rbgold.com

D 602.230.1703 C 480.220.9698

CHRISTOPHER D. GEE

Private Wealth Advisor, Corporate Finance Associate
ChrisG@rbgold.com

D 602.230.4435 C 602.363.6845

MICHAEL S. WALLING

Partner, Private Wealth Advisor, Corporate Finance Director
MWalling@rbgold.com

D 602.230.1729 C 602.373.5881

ROY J. SCHIEFFER

Private Wealth Advisor, Insurance Specialist
RoyS@rbgold.com

D 602.956.6805 C 602.908.0157

C. TYLER WALLING

Private Wealth Advisor, Financial Planning Specialist
CTWalling@rbgold.com

D 480.386.0328 C 602.980.8686