

Emerging Markets

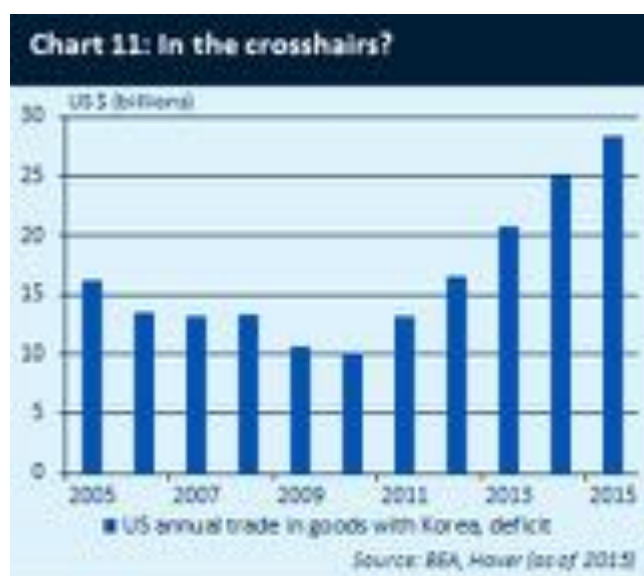
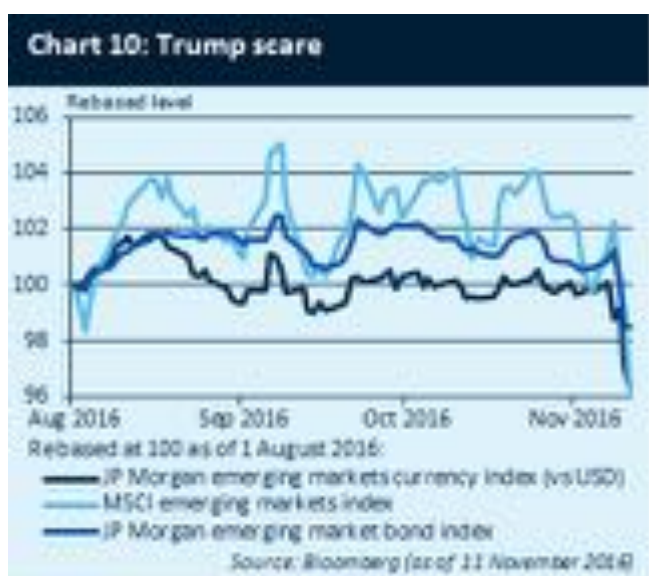


Known Unknowns

What will Trump mean for emerging markets? And more specifically, what will his election mean for the US-China relationship, arguably the most important bilateral relationship in the world? Although the campaign included three debates and countless hours of media coverage we were still left with vague policy proposals, especially on trade policy. Making matters more difficult, customarily there are large gaps between campaign statements and subsequent White House policy, and nowhere more so than on trade policy. Trump's election has already had an impact on the outlook for EM: the US yield curve has steepened, the dollar has broadly strengthened, and EM assets have sold-off (see Chart 10). **A continuation of these dynamics presents a risk to the EM outlook.** Making matters worse Trump has threatened to impose large tariffs on China, renegotiate or withdraw from NAFTA, and withdraw from other "unfair" free trade agreements (FTA). While the executive branch has significant leeway over trade policy and a president could theoretically withdraw from FTAs or impose punitive tariffs on a trading partner, the results would cause significant damage to the US economy. For this reason we deem a full-scale trade war including abrogation of NAFTA and 45% tariffs on Chinese imports unlikely; however, a move towards targeted protectionism remains a distinct possibility. To get a better sense of where policy might change we take a closer look at what actions a Trump White House could take on trade.

Starting with China, Trump has threatened to label China a currency manipulator and use that as justification for imposing across-the-board tariffs on Chinese goods. While this remains a possibility, the macro justification for the US Treasury (the agency responsible for making the decision) would be difficult considering China does not currently meet its stated criteria and it is currently intervening to support its currency not weaken it. Additionally, across-the-board tariffs, as stated above, would impose significant costs on the US consumer and could launch a trade war with disastrous consequences. **It's impossible at the moment to rule anything out but the potential for an economically and politically destructive outcome means that any measures taken against China or Mexico are more likely to be targeted in nature.**

This could entail trade actions against Chinese industries that are already under international pressure such as steel, aluminium, solar, chemicals, or glass; a more zealous enforcement of intellectual property rights; or targeting China's foreign content restrictions and technology transfer requirements, but fall short of large tariffs. How the Chinese respond is another question but it has significant leverage considering the importance of the Chinese market for US multinationals. Beyond China and Mexico, several other countries could be impacted should Trump follow through on implementing protectionist policies, particularly those with existing free trade agreements and a trade surplus with the US. Other than NAFTA, the US has an FTA with Chile, Jordan, Singapore, Bahrain, Morocco, Oman, Peru, Dominican Republic/Central America, Panama, Columbia, and South Korea. Of these countries, South Korea has been singled out during the campaign as a potential target for protectionist policies and stands out as the only free trade partner with a large US trade surplus (see Chart 11). Calling the Korea-US FTA a "jobs killer" during his campaign, and highlighting how the US trade deficit with Korea has surged following the FTA, puts Korea in a particularly vulnerable spot.



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