

TRADE

# Tariffs don't change U.S. economic outlook

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With talk of tariffs and trade wars commanding front-page headlines all week, it's important for investors to pause, take a breath and evaluate the events through a long-term lens. What are the actual, lasting impacts of tariffs on the United States and other countries? Will they outweigh other factors driving the growth of the world's largest economy? And what happens next?

Feedback

Three Capital Group professionals with a close eye on trade policy offer their views.

## The Benjamin Button economy continues

– *Jared Franz, economist*

Tariff announcements over the past few days, and the subsequent agreements to delay them, do not change my overall positive view on the [outlook for the U.S. economy](#). Higher tariffs have been part of my base case for quite a while, even before U.S. President Donald Trump's election victory in November. Trade barriers have been rising since the end of the global financial crisis in 2009, with sharp increases under both Trump and President Biden. So the writing has been on the wall for several years.

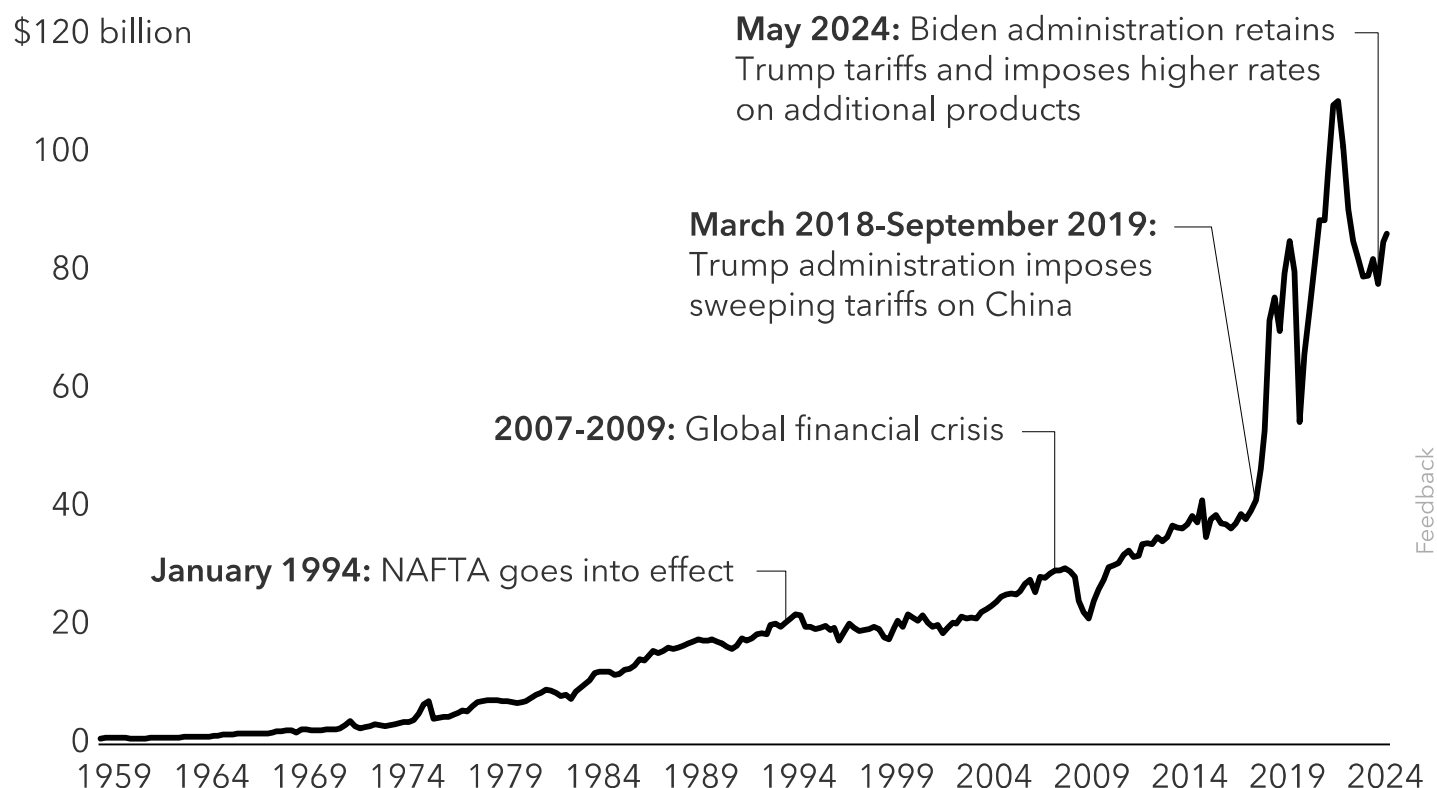
The initial tariffs aimed at Canada and Mexico this week were higher than I had expected, but those have been delayed for at least a month and may be decreased or even disappear. Conversely, the tariffs aimed at China are lower than I had anticipated. It's still not clear what the final effective tariff rates will be, to which goods they will apply, and when or if they will be implemented. In my view, Trump is more concerned with reaction from the U.S. stock market than he is the bond market. That may rein in his inclination to impose crippling trade barriers for extended periods of time.

With this in mind, I stand by my optimistic assessment. I expect the U.S. economy to continue on a path toward healthy expansion in 2025, roughly in the range of 3% GDP growth. As I explained late last year, I believe the U.S. business cycle is aging in reverse, transitioning from a late-cycle to a mid-cycle path, characterized by rising corporate profits, accelerating credit demand and generally neutral monetary policy. Most important, I do not see a recession on the horizon.

All the tariff talk this week changes nothing in that positive assessment.

## Trade barriers: U.S. tariffs have risen sharply in recent years

### Total U.S. customs duties on production and imports



Sources: Capital Group, Bureau of Economic Analysis, Federal Reserve Bank of St. Louis. As of December 31, 2024.

## What happens next?

– Tom Cooney, international policy advisor, and Tryggvi Gudmundsson, economist

To understand what happens next, it is important to ascertain the underlying reason for imposing the tariffs. If Trump is using tariffs as a negotiation tactic as seen during his first term and more recently with tariff threats to Colombia, we could see negotiations that further postpone, avoid or reduce these tariffs – as has already happened with Canada and Mexico.

As part of these negotiations, it seems likely that a review of the U.S.-Mexico-Canada Agreement (USMCA) trade pact scheduled for 2026 could be moved up to reduce North American trade uncertainty. Our base case is still that the pact survives but with significant alterations that endorse some new level of U.S. tariffs, restrictions on Chinese investment in Mexico, further

tightening of the automotive rules of origin, strengthening of border security or a commitment by Mexico to attack and weaken the drug cartels.

On the other hand, the potential for these tariffs to be permanently shelved or meaningfully reduced is much less likely if the motivation is to create revenue to fund tax cuts or reduce the U.S. trade deficit. (Although Canada runs a trade deficit with the U.S., excluding oil.) In this case, tariffs are likely to go up as the countries retaliate and then may moderate as agreements are reached. Notably, the tariff negotiation and implementation process with China in 2018 and 2019 involved shifting deadlines and considerations of exclusions.

If measures like those announced on February 1 eventually go into effect, they would likely impact Mexico and Canada more than the U.S. or China. The U.S. accounts for around 80% of Mexican and Canadian exports, while Mexico and Canada account for around 15% of U.S. imports each. Furthermore, the majority of trade within the USMCA is conducted in dollars, which minimizes the ability of the Canadian dollar and Mexican peso to act as adjustment mechanisms.

That said, the U.S. is significantly reliant on specific imports, including horticultural products from Mexico and energy from Canada. Not only does Canada account for almost 20% of U.S. oil supply and more than half of total U.S. oil imports, but it is also a convenient source for U.S. importers, given the refinement infrastructure.

Modeling the impact of the tariffs relies heavily on various assumptions, but economic history suggests that both consumers and companies would be negatively impacted.

As was the case in the prior Trump administration, things are moving quickly, and it is difficult to predict how situations may change. It is unclear how long these measures will stick, even if implemented. That said, it seems likely that some level of heightened tariffs could remain for years to come. The tariffs announced February 1 appear to be an opening salvo, with more clarity on longer term policy likely to come in the weeks ahead.

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