

Trump Tariffs Threaten the Japanese Economy

On April 9, US President Trump announced a 90-day suspension of the additional reciprocal tariffs that were to be charged on imports by country corresponding to each country's tariffs and non-tariff barriers on US goods on top of the universal tariff (10%) on imports from each country. Nonetheless, the 10% universal tariff, the additional 25% tariff specifically targeting automobiles, and the additional tariffs on imports from Canada and Mexico (25%) were maintained. Notably, an extremely high-level additional tariff of 145% was imposed on imports from China, which had countered the US reciprocal tariff with a retaliatory tariff. (This article is based on the information as of noon on April 11, Japan Standard Time).

For Japan, the 14% additional reciprocal tariff was suspended, keeping the tariff to 10%, but the US still took very wide-ranging tariff measures including the increase in tariffs on automobiles, Japan's key industry. It is also important to note that depending on the results of negotiations the additional reciprocal tariff may be imposed 90 days later. President Trump is building his criticism mentioning the existence of the US trade deficit with Japan and the number of US automobiles that are imported into Japan, so we cannot be optimistic.

In response to the US measures, Canada decided to impose retaliatory tariffs and the EU has also announced that it is considering countermeasures, but what stands out in particular are the measures taken by China. China's retaliatory tariff against the US reciprocal tariff was initially 34%, but when the US increased the reciprocal tariff by 50 percentage points, China immediately responded by increasing its retaliatory tariff to 84%. That led to the US hiking its total additional tariffs against China to 145%. The developments around the series of Trump tariffs have cast a spotlight on the friction between the US and China.

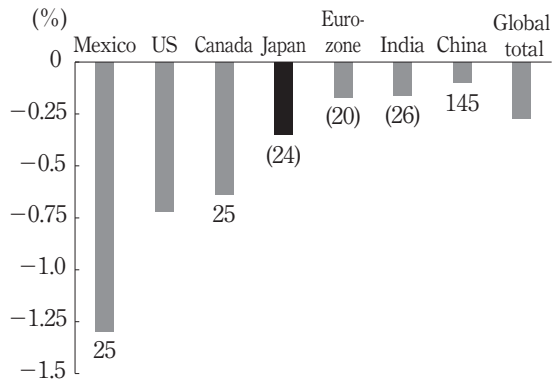
Then, what would the impact be if a series of tariff measures are implemented? The OECD presented an estimate regarding the impact of higher tariffs on March 17, before the automobile tariffs and reciprocal tariffs were imposed. The estimate predicts that if the US boosts tariffs by 10% and all its trading partners respond with retaliatory tariffs of 10%, global GDP will decline by around 0.3% from the baseline scenario in the third year after the tariffs are implemented, and this will lead to an average 0.4 percentage point increase in the inflation rate during those three years. Regarding the impact on Japan, the prediction is that GDP will decline by around 0.4% and the inflation rate will increase by 0.2 percentage points (see Figures 1 and 2). What should be noted regarding the impact on Japan's GDP is that while not as great as the impact on Mexico, the US, and Canada, it is predicted to be greater than the impact on the eurozone. The impact on prices is projected to be smaller than the impact on GDP, but regardless of the scale, this will throw cold water on rises in real wages. Moreover, what differs greatly from the OECD projections is that the impact on the US and China will be huge because both countries have embarked on an exchange of high tariff rates. If that is the case, there will certainly be a large impact on Japan, which is highly reliant on trade with both the US and China, as well. Furthermore, we must be aware of the viewpoint that the heightened sense of the uncertainty of the global economy and the dampening of corporate and consumer sentiment caused by the imposition of the series of tariffs will further amplify the negative impacts on the global economy. In fact, some Japanese think tanks are predicting that if the reciprocal tariffs are imposed as originally planned or a tariff war becomes prolonged, the Japanese economy may fall into negative growth.

Over the 90 days from April 9 each country will negotiate with the US regarding its own tariffs and

non-tariff barriers and request cancellation of the additional reciprocal tariffs. Japan is said to have priority in negotiations, but as long as there is no outlook for achieving a reduction in the US trade deficit with Japan, we should probably assume that the imposition of the additional reciprocal tariffs will not be averted. Beyond that, it should also be noted that barriers to agricultural goods imports and the exchange rate may

also be on the discussion table. It is crucial that Japanese companies assume that the series of Trump tariffs will become prolonged, including the risk that the reciprocal tariffs will be imposed. Japanese companies must begin to rebuild their supply chains and to review their investment strategies in preparation for the case where the global economy is forced into a slump with a large decline in international trade.

Figure 1: Impact on GDP from Retaliatory Exchange of 10% Tariffs (impact in year three)



Note: The numbers in Figure 1 show the additional tariff rates by the US. The figures in parentheses show the totals of 10% (the uniform reciprocal tariff) plus the additional reciprocal tariffs that have been suspended for 90 days.

Source: *OECD Economic Outlook* by OECD

Figure 2: Impact on Consumer Price from Retaliatory Exchange of 10% Tariffs (average annual impact in the first three years)

