FX, Fixed income, Econ, Facts & Fallacies

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Is Trump's trade war just a negotiation tactic?

- Donald Trump's second term as US President has sparked a new round of trade tensions as he pushes for a fairer trade deal. China, Mexico, and Canada are the first three targets for tariff increases announced by the US. However, the decision for Mexico and Canada was later delayed by 30 days after they reached a border control agreement. The EU, along with Asian economies like Thailand, are also at risk from US tariffs.
- However, US tariff hikes would also impact the US economy, primarily through rising prices, especially for goods the US heavily depends on, such as Canada's oil and Mexico's automotive exports. As a result, the US is likely to proceed cautiously and avoid raising tariffs to extreme levels. Ultimately, tariffs may simply serve as a negotiation tool. It's also important to remember that one of the reasons Trump won the election was the high cost of living Americans faced, meaning one thing he wants to avoid is high inflation.

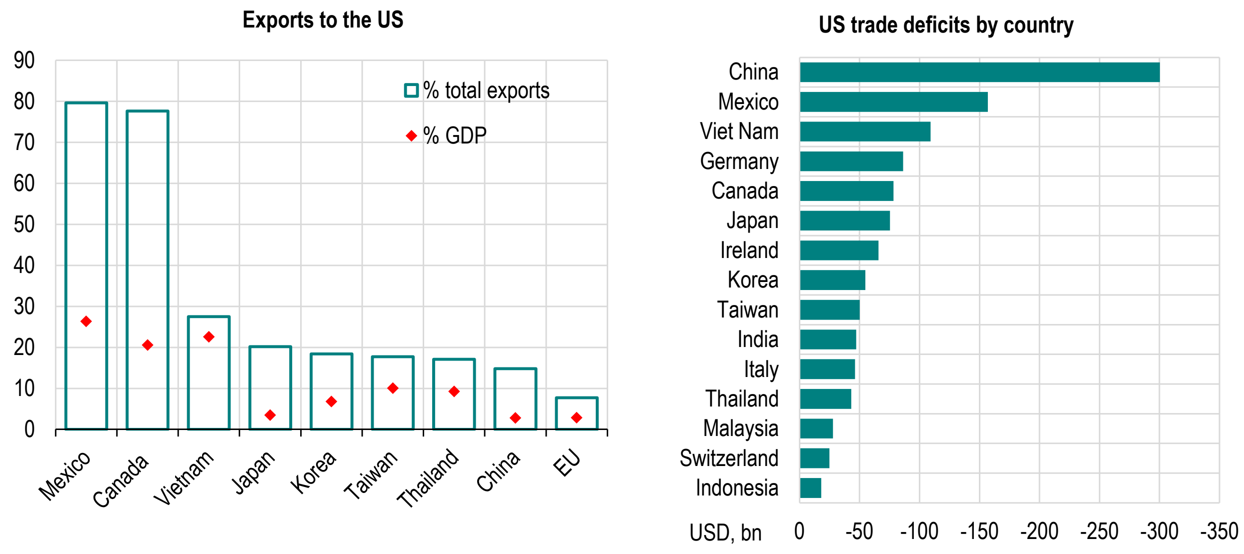
Trump 2.0 ushers in a new phase of the trade war, sparking a 'golden age' for the US.

Donald Trump's second term as US President has sparked a new round of trade tensions as he pushes for a fairer trade deal in the wake of massive annual trade deficits exceeding USD 1 trillion (around 4% of GDP). He also aims to bring jobs and manufacturing back to the US. **The key strategy is increasing tariffs on imported goods.** Trump proposed a 60% tariff on China, 25% on Mexico and Canada, and 10-20% on other trade partners in his campaign. This move raises concerns and risks for countries heavily dependent on US trade, particularly Mexico and Canada, where exports to the US account for 26% and 21% of GDP, respectively—giving the US significant negotiating power. For Thailand, exports to the US represent around 9% of GDP, a noteworthy share (Figure 1, left).

Indeed, the US has focused its trade attention on countries with significant trade deficits, with China topping the list, followed by Mexico. Canada ranks fifth (Figure 1, right). **These three countries were the first targets for tariff increases announced by the US in late January,** set to take effect on February 4. **However, the decision was later delayed by 30 days for Mexico and Canada after they reached a border control agreement.** This delay eased some market fears, suggesting that this new trade war phase may simply be a negotiation tactic by Trump to secure a fairer trade deal, with the tariff hikes potentially not as severe as initially threatened during his campaign.

Other countries at risk from US tariffs include the EU, which Trump has stated will 'definitely' face tariffs, and **Asian economies like Thailand**, which are highly dependent on the US.

Figure 1: US and trade partners



Source: Trademap, Trading Economics, and KBank; data are based on 2023.

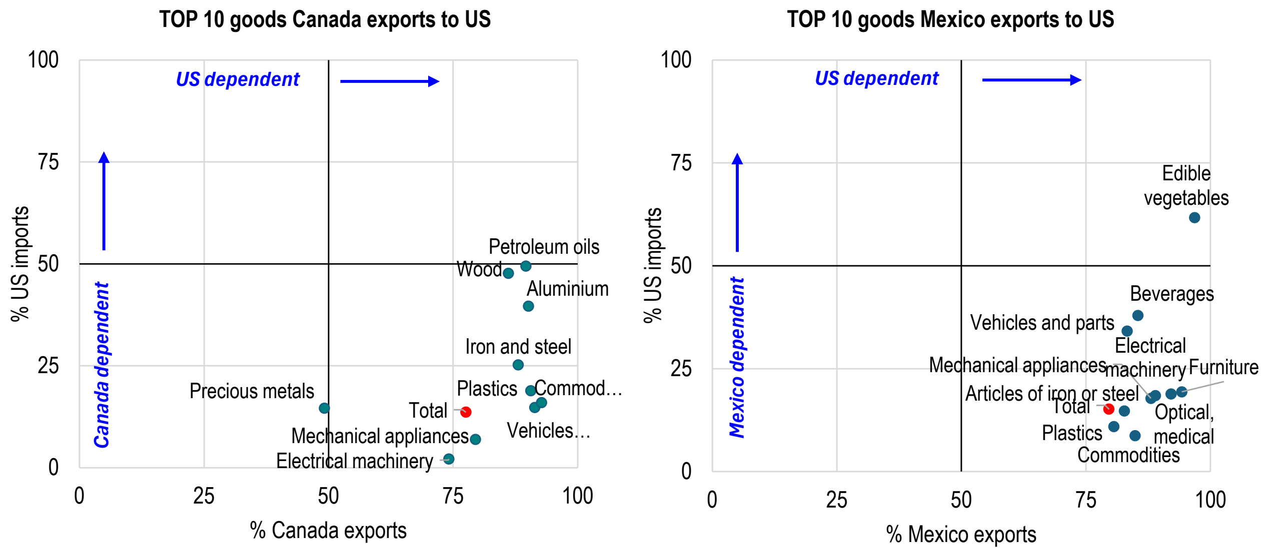
Mexico and Canada would be hardest hit by Trump's tariffs, with the US also impacted, especially in the automotive sector.

As mentioned earlier, US tariffs will severely affect Mexico and Canada due to their proximity and the USMCA trade agreement.

A closer look at the top ten export categories (Figure 2) reveals that both countries are highly dependent on the US, with over 50% of their total exports going there. Of particular economic significance are Canada's oil, automotive, and electronics sectors and Mexico's automotive, electrical appliances, and electronics sectors, which have high economic value for both countries (Figure 3).

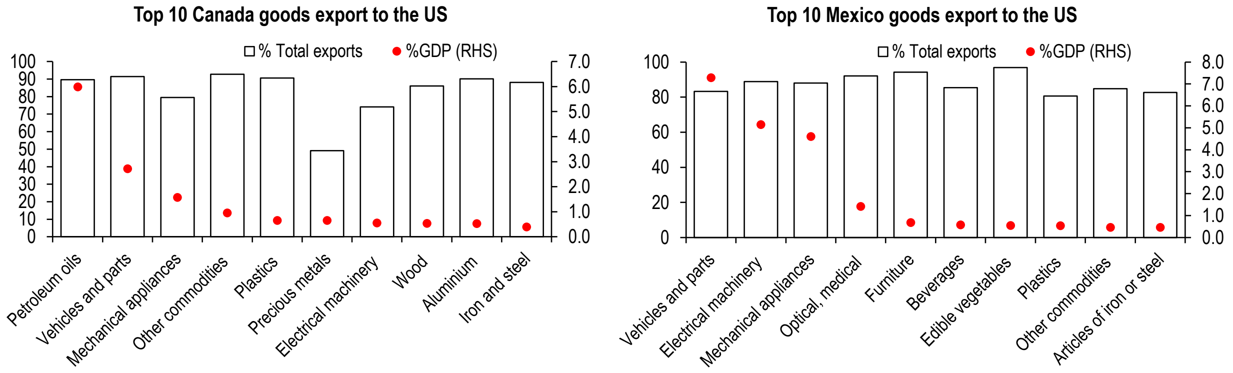
The US will also be impacted, as it relies heavily on both Canada and Mexico for some categories (Figure 2), **such as oil, wood, and aluminum from Canada, and edible vegetables, beverages, and automotive products from Mexico.** Raising tariffs would increase prices in these sectors, adding inflationary pressure and making Fed rate cuts more challenging. **Notably, the US depends on both countries for nearly 50% of automotive parts, mostly for US-brand cars** (Figure 4), so higher tariffs could disrupt the US auto industry.

Figure 2: Trade between US and Canada, Mexico



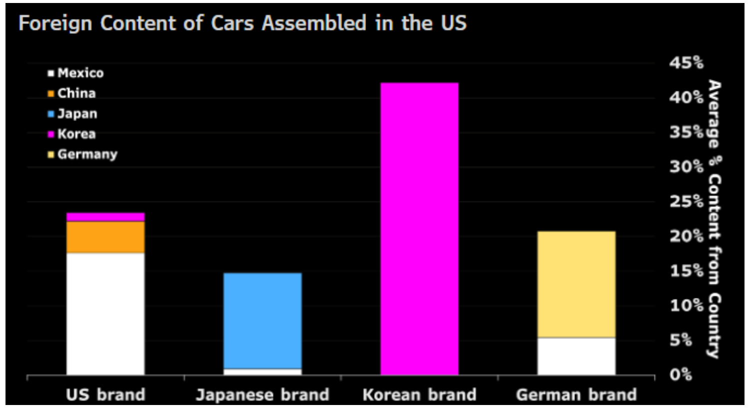
Source: Trademap, Trading Economics, and KBank; data are based on 2023.

Figure 3: Top ten goods Canada and Mexico exports to the US



Source: Trademap, Trading Economics and KBank; data are based on 2023

Figure 4: US brand cars were those heavily rely on Mexico Auto part



Source: Bloomberg Economics

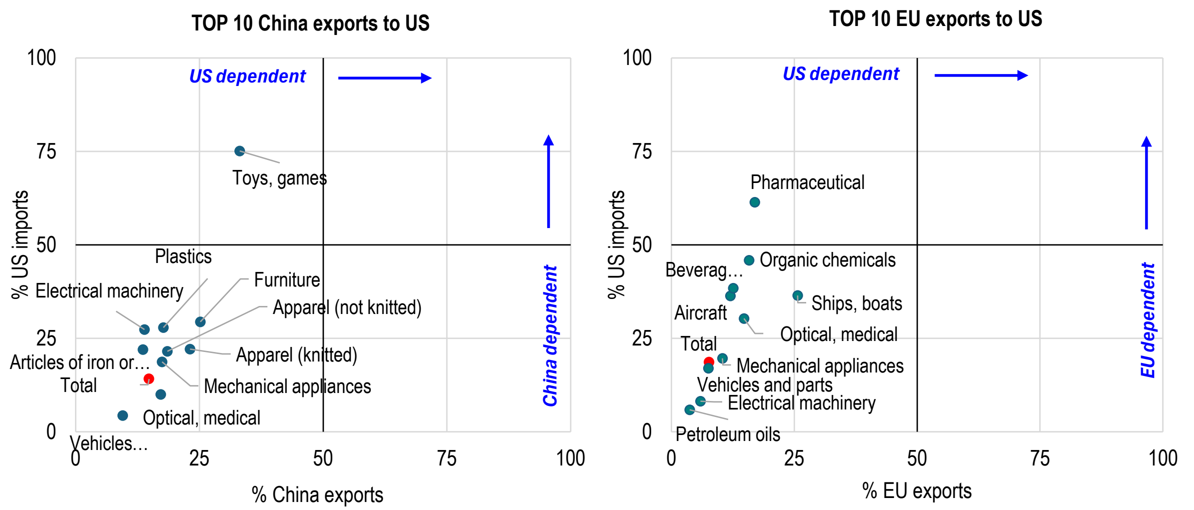
The impact on China and the EU will be less than on Mexico and Canada

Exports to the US account for 2.8% of China's GDP and 2.9% of the EU's GDP, so the **economic impact of US tariffs is much less than for Mexico and Canada.** Additionally, each of the top ten exports to the US makes up less than 25% of total exports (Figure 5).

The **Chinese sectors most affected include electronics, electrical appliances, furniture, and toys,** which have significant economic value (high GDP share). The most exposed sectors for the EU **are electrical appliances, pharmaceuticals, automotive, electronics, optical, and chemicals** (Figure 6).

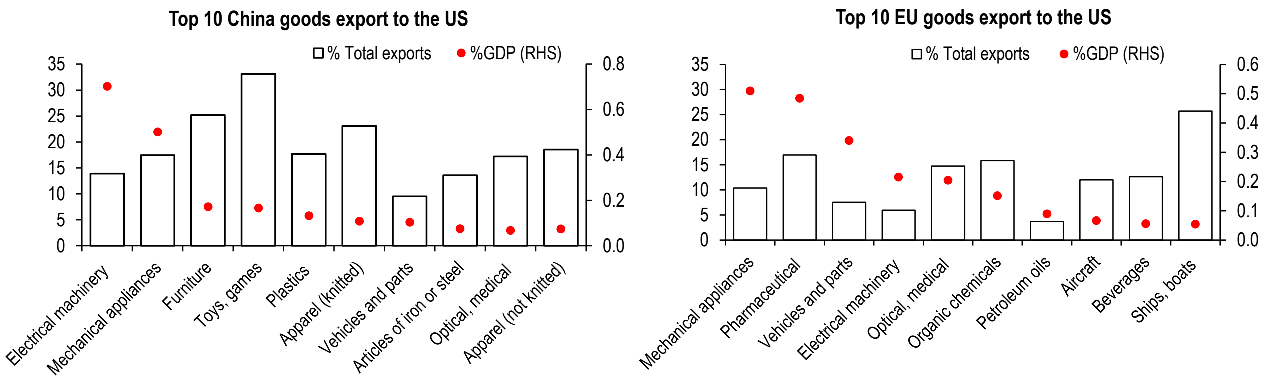
Nonetheless, **the US will also feel some impact from tariffs on both economies, particularly on toys (75% of imports from China)** and electronics, plastics, furniture, and apparel (20% from China). **The US relies heavily on pharmaceuticals, chemicals, beverages, ships, and optical products for the EU.** Raising tariffs will likely drive up prices, especially in the early days of the tariffs.

Figure 5: Trade between US and China, EU



Source: Trademap, Trading Economics and KBank; data are based on 2023

Figure 6: Top ten goods China and EU exports to the US



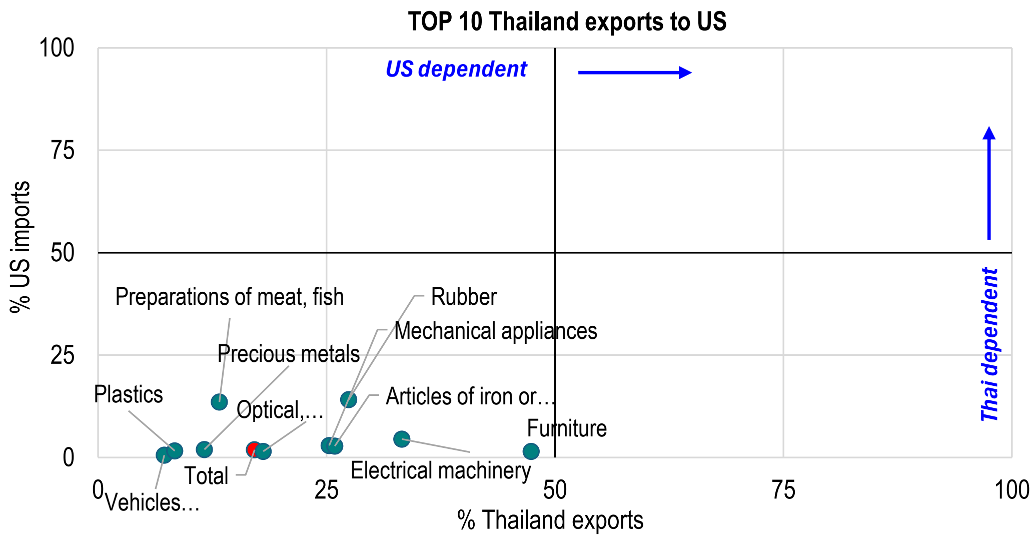
Source: Trademap, Trading Economics and KBank; data are based on 2023

The impact on the Thai economy is not negligible

Thailand is one of the countries with which the US has a large trade deficit, exceeding USD 40 billion, putting it at risk of US tariffs. The impact on the Thai economy could be significant, as exports to the US account for 9% of Thailand's GDP. Meanwhile, the US relies less on Thai goods (Figure 7), giving it high negotiating power. This position makes Thailand more vulnerable to US tariffs, with the impact being even more severe if tariffs are imposed directly on Thailand rather than across all countries.

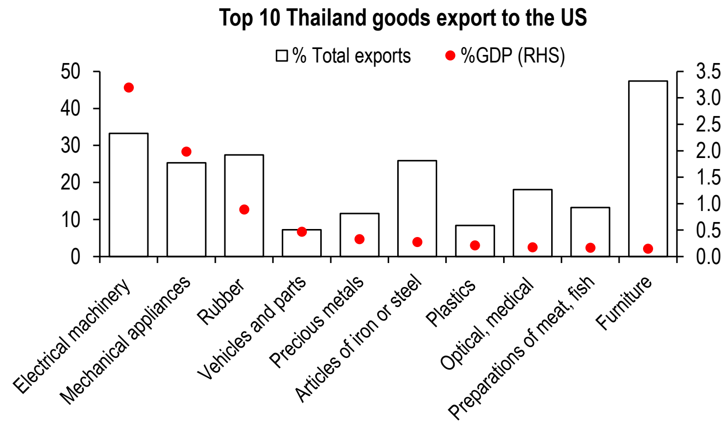
By product, **the most affected goods by US tariffs are electronics, electrical appliances, rubber, and automotive. Furniture** will also face a high impact, with nearly 50% of exports going to the US.

Figure 7: Trade between US and Thailand



Source: Trademap, Trading Economics and KBank; data are based on 2023

Figure 8: Top ten goods Thailand exports to the US



Source: Trademap, Trading Economics, and KBank; data are based on 2023

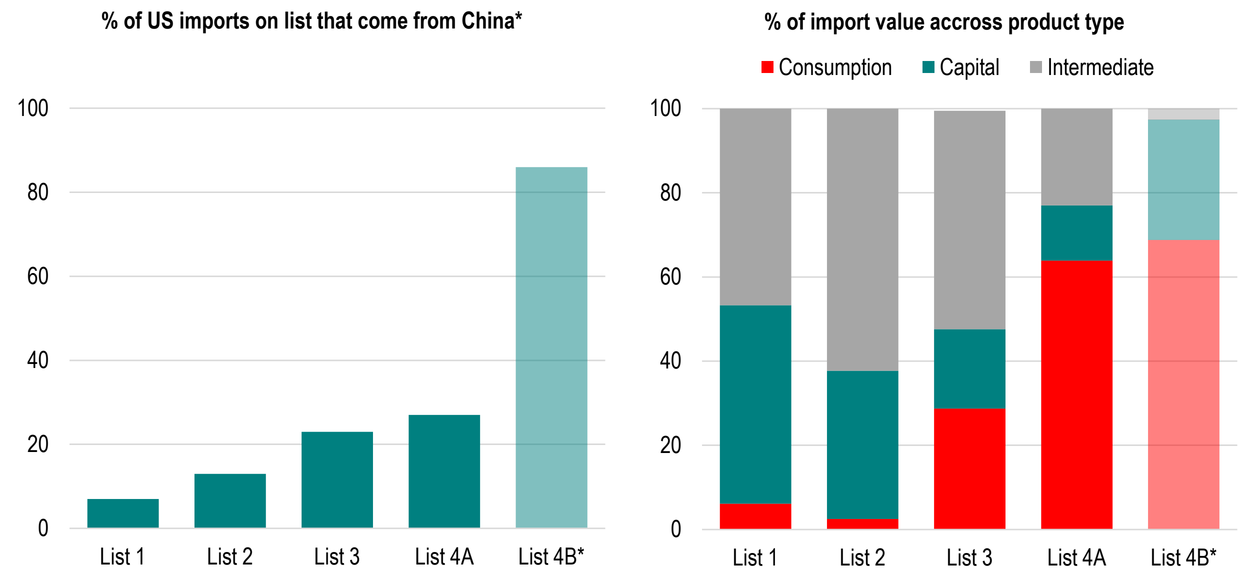
US tariffs may be a negotiation tool

"The study above shows that **US tariff hikes would also impact the US economy, primarily through rising prices of goods. As a result, the US is likely to proceed cautiously and avoid raising tariffs to extreme levels**, such as the 60% on China that Trump threatened during his campaign. Moreover, the US may selectively target products for higher tariffs, as seen in the first trade war, where tariffs were raised on goods less critical to the US and consumer goods were largely spared (Figure 9).

The **US is currently investigating its trade partners and whether China has adhered to the Phase 1 trade deal. The report is expected to be sent to President Trump by April 1,** after which the tariff path should become clearer.

However, **in the end, tariffs may serve as a negotiation tool,** consistent with Trump's business style. We must also remember that **one of the reasons Trump won the election was the high cost of living Americans experienced** under Biden's administration. **Therefore, one thing Trump likely wants to avoid is high inflation.**

Figure 9: US avoids incrase tariffs on goods highly depend on China during the first trade war



Source: Bloomberg Economics and KBank

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