

Why the U.S. Might Be Less Affected by a Trade War

The nature of our economy could help it withstand the disruption.

Provided by David H. Smith

A trade war does seem to be getting underway. Investors around the world see headwinds arising from newly enacted and planned tariffs, headwinds that could potentially exert a drag on global growth (and stock markets). How badly could these trade disputes hurt the American economy? Perhaps not as dramatically as some journalists and analysts warn.^{1,2}

Our business sector may be impacted most. Undeniably, tariffs on imported goods raise costs for manufacturers. Costlier imports may reduce business confidence, and less confidence implies less capital investment. The Federal Reserve Bank of Philadelphia, which regularly surveys firms to learn their plans for the next six months, learned in July that businesses anticipate investing less and hiring fewer employees during the second half of the year. The survey's index for future activity fell in July for the fourth month in a row. (Perhaps the outlook is not quite as negative as the Philadelphia Fed reports: a recent National Federation of Independent Business survey indicates that most companies have relatively stable spending plans for the near term.)^{1,2}

Fortunately, the U.S. economy is domestically driven. Consumer spending is its anchor: household purchases make up about two-thirds of it. Our economy is fairly "closed" compared to the economies of some of our key trading partners and rivals. Last year, trade accounted for just 27% of our gross domestic product. In contrast, it represented 37% of gross domestic product for China, 64% of growth for Canada, 78% of GDP for Mexico, and 87% of GDP for Germany.^{3,4}

Our stock markets have held up well so far. The trade spat between the U.S. and China cast some gloom over Wall Street during the second-quarter earnings season, yet the S&P 500 neared an all-time peak in early August.⁵

All this tariff talk has helped the dollar. Between February 7 and August 7, the U.S. Dollar Index rose 5.4%. A stronger greenback does potentially hurt U.S. exports and corporate earnings, and in the past, the impact has been felt notably in the energy, materials, and tech sectors.^{6,7}

As always, the future comes with question marks. No one can predict just how severe the impact from tariffs on our economy and other economies will be or how the narrative will play out. That said, it appears the U.S. may have a bit more economic insulation in the face of a trade war than other nations might have.

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Citations.

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