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Taking Stock: Trump, Trade and Financial Volatility

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Regardless of what one may think of President Donald Trump, most would likely agree he is not a lazy individual. He is also not someone to back down on a course of action; rather, he doubles down when the going gets tough.

During political campaigns, candidates propose long lists of agenda items as part of their platforms. If elected, they may abort a number of these items, not because of political dishonesty, but because the policies may pose severe damage to the economy and are faced with strong (political and international) opposition. The policies now appear too impractical to implement. However, President Trump has been willing to pursue a variety of his pre-election agenda items despite backlash and possible economic risks.

Trade has been one of those controversial issues. Disruptions in the status quo may be very damaging to the United States, its trade partners and the global economy. However, from my Canadian perspective, I believe President Trump has a valid premise for his arguments on trade. His tough stance produces financial market volatility, but such pain may be worth it as he tries to fix some fundamental flaws in trade between countries. Otherwise, a country such as the United States could find itself in too big a financial hole and no longer able to borrow expeditiously to cover trade gaps.

Growing up in the 1970s, I recall how the Canadian economy was flooded with cheap Japanese cars. My father, an auto mechanic, considered such cars (at the time) to be of poor quality and advised anyone he could not to buy such vehicles. But the low price of such cars was just too compelling for many consumers. I also recall a relative, a part-time farmer, who bought a Soviet-made tractor because the price was too good to pass up. He later had trouble servicing it and getting parts. Foreign products can be quite inexpensive based on the lower labor and production costs in those countries. Government subsidies may play a part. In the case of products that came from the former Soviet Union, production costs did not necessarily have to tie into the sale price.

Over the past several decades, Canadians have seen many strong and healthy industries fall apart due to the import of various products. Many imports had artificially low prices due to foreign government financial assistance and from lower operating costs due to less stringent regulations in that economy. As an example, recall that some products from China posed health risks because China did not have sufficient standards in place to address safety, as would be found in the United States and Canada. In various aspects, China is still an emerging economy so it still needs to develop some of its national qualitative standards; we need to be patient with it in that regard. In the meantime, less regulation and fewer controls means lower operating costs.

Our Canadian industries suffered from the influx of very cheap imports, and our own government would often do very little about it. It may have been perceived to be too big an undertaking to fight back against “unfair” trade; the local voices of dissension were perhaps not loud enough; it smacked of protectionism to do something; we may have had tremendous faith in our own people to competitively fight back; and our local politicians would still get elected even if the issues were ignored (hence, no dire consequences). But many Canadians lost good jobs because other Canadians wanted to get a cheap deal (I admit, I was also lured into buying a very cheap foreign product). The U.S. environment and consumer psychology was similar.

Trade agreements had not fully removed the artificial trade barriers a country has established that work to the detriment of another country (hence trade imbalances can result).

According to Investopedia, “Free trade is a policy to eliminate discrimination against imports and exports. Buyers and sellers from different economies may voluntarily trade without a government applying tariffs, quotas, subsidies or prohibitions on goods and services. Free trade is the opposite of trade protectionism or economic isolationism.”¹ However, free trade in practice has often been a combination of free trade and protectionism (a sort of hybrid), yet it has still been called free trade (many would not be against free trade in principle, but it has become a misleading label in our economic jargon). Trade agreements had not fully removed the artificial trade barriers a country has established that work to the detriment of another country (hence trade imbalances can result). Therefore, a new term has been introduced called fair trade. One would think that free trade and fair trade would be consistent, but they are not

interchangeable given the practices of many countries today. President Trump has emphasized this difference in understanding (given that free trade is not completely applied), since his contention is that the United States has been put unfairly on the losing end of many business transactions far too often.

To fix decades of free trade that had not been fair trade would require strong political resolve—and produce dislocation in many industries and sectors. This, of course, translates into volatility in financial markets, as previous correlations and economic relationships are forced to change. The imposition of tariffs is unpleasant and the consumer ultimately has to pay for them, but it should be a temporary measure until other trade impediments are resolved. Various countries have not played fair, imposing duties and other charges on products that entered their economy (and have done so for decades). Foreign companies also may attempt to copy U.S. products while being protected locally from U.S. competition.

The United States, with its sizable economy, cannot continue to stay strong with such large trade deficits (some other developed economies face similar issues but likely on a smaller scale). The sooner this problem is addressed, the less painful the repairs will be. Fortunately, these adjustments are being made when the U.S. economy is robust. How successful the reforms will be is still hard to see, but I would argue that at least there is a movement in the right direction.

THE U.S. AS A PAYER OF LAST RESORT

Being from Canada, I do not have a political axe to grind in favor of one U.S. political party or another. However, it seems to me that the United States usually gets stuck with having to pay for much of everything. Carrying extra financial responsibilities (for any country) results in a combination of higher taxes (for both corporations and individuals), higher debt and higher interest rates. Extra costs will invariably make any country less economically competitive.

The U.S. is a major funder of the United Nations and many of its agencies. It supports multiple nations with grants and subsidies. Yet many of these nations, openly and without impunity, turn around and criticize the United States and its allies for a wide array of policies (and may even support activist and military groups that could put American citizens and soldiers in harm's way). There are often little to no repercussions from American politicians for the detrimental actions of these adversarial countries. Rather the money flow continues. There seems to be this strange sort of thinking in North America, that if we give money to people who hate us, they may like and respect us someday, but if we cut them off, they will just hate us more. (I would not give money to my enemies; they can use it against me and they may never change. I would rather engage enemies through diplomatic means.)

The United States is a major polluter, but I often feel it is being disproportionately singled out and is being expected to pay too much, unlike the case for all other countries who also create pollution. It sometimes seems that we give developing countries a free pass, even though they have a major part to play in contaminating our planet. I recall at one conference, pollution or climate change was described as a global problem, but in terms of the solution, the ultimate target became the developed economies (particularly the U.S.) and the domestic companies. The countries and companies were expected to cut back, thus saddling each economy with more requirements and regulation. A uniform solution was not applied to all countries.

And what about military defense? This is also a very large expenditure. If a country is not paying its fair share (such as for NATO), that country can divert its financial resources elsewhere, potentially benefitting the country as a whole. For decades, Canada has neglected its military to the point where it is not able to take care of many of its security needs and commitments and has been largely relying on its close neighbor, the United States, to respond to any major military conflict. I do occasionally feel sorry for how the U.S. is often stuck with all sorts of military burdens (granted, the United States sometimes has made some ill-advised and costly decisions, such as its past actions in Iraq). The globe has been experiencing peace in large part because of U.S. military commitments abroad. I always respect how many average Americans salute their armed forces in public places such as airports because military service is a sacrifice that not many people are willing to make, just as many countries chose not to sacrifice their resources to support the military.

KICKING THE CAN DOWN THE ROAD

The Society of Actuaries, jointly with the Canadian Institute of Actuaries, sponsored a recent study on Canadian health care.² Among other things, the news release for the report stated: “Using the current Canada Health Transfer (CHT), health care expenditures will equal 97 percent of total revenues available to provinces and territories at the end of 25 years. . . .”³ A very alarming result, that also, by implication, indicates Canadian provinces will not—after paying for health care—be able to afford much of anything else.

How did Canadian provinces respond to the SOA/CIA research project? Was the study widely read? Even if one had not seen the research, the average Canadian citizen likely realizes that with an aging population, health care costs are going to increase, probably dramatically.

But in the June 2018 election for the Canadian province of Ontario, the incumbent Liberal party promised “expanded” health coverage and more health benefits. Many observers conceded it was an effort to win votes, even if the province could



not afford to make more health care commitments (Ontario today has a debt about twice that of the state of California and at least 4.5 times California’s debt on a per capita basis⁴). But unless an issue becomes front and center in the public’s mind, it will not get enough attention, and politicians are normally not going to bring it up. At a pension conference, I recall speaking to a man in his 70s about the exorbitant costs of Canadian health care that will come 20 years from now, and he kept saying, “I don’t care, I don’t care. . . . I should be dead by then.” Whether it is health care, pollution, national security or something from a whole host of issues, we may not be able to solve these matters immediately and in an efficient way. But we should not consign ourselves to an attitude of not caring if it does not affect us personally and in our future wellbeing.

Unfortunately, some have this short-term oblivious attitude with trade. No one wants to worry about trade imbalances until their effects stare us in the face. In the meantime, kick the can down the road. Let another generation worry about it. We have dodged bullets before, so we can do it again. We will find a solution around the problem somehow, “down the road.” But I hate to rely on being lucky or on the prospect of human ingenuity—it is like planning for retirement by buying a lottery ticket.

UNFAIR TRADE COSTS MONEY

Unfair trade can bring an economy down. Any country would like to be on the winning side of any transaction. Perhaps a country is just initially motivated to build up its foreign currency reserves, and the United States dollar is an important and valuable reserve currency. But if a trade imbalance becomes too large and this trend is protracted for too long, both sides will suffer. I sometimes wish Canadian politicians took a greater stance against unfair trade the way President Trump is doing.

We can ignore the matter of unfair trade and let financial markets continue to appreciate in value—but, under the surface, our financial environment is unhealthy and will explode into something serious one day.

Volatility in financial markets can be expected as painful adjustments in trade agreements and relationships are made. That volatility is not too dire a price to pay. It is necessary to take action on trade as the trade imbalance issue has been going on far too long and the matter needs to be resolved one way or another. ■

This article is the sole opinion of the author and not of the Society of Actuaries or of the Financial Services Commission of Ontario.



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ENDNOTES

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