

A Letter to President Trump

Policies needed to make America “Great”

Katsuyuki Hasegawa, Chief Market Economist

Dear Mr. President

Four months have passed since you won the Presidential election last fall. More than a month has passed since your inauguration. During that time, the market capitalization of the US stock market has risen and now stands 10% above pre-election levels, while even global stock markets have risen almost 10%. Ironically, there has been a favorable reception to the change from your predecessor, who ran on a platform of “Change” 8 years ago.

Prior to the election, the global economy was faced with stagnation signified by the 3Ls with ‘low growth, low inflation, and low interest rates’. There is hope that large tax cuts, infrastructure investment, and deregulation will be game changers not only for the US economy but also for the global economy.

I believe that the President is an extremely capable business leader. In general, CEOs are shamed by corporate bankruptcies. The President, however, has experienced bankruptcy 6 times. Despite moving bankers to tears, your indomitable spirit could be admired no matter how it manifests. According to the Forbe’s ranking of billionaires, you are the 113th richest person in the US, and a very successful business man.

Bringing such business acumen into the political world is extremely important for the reforms being called for by companies and the general public. On the other hand, differences in political management and business management are not insignificant. Some of the policies you have proposed as President are inevitably perplexing for economists.

There are three points that give me particular concern.

First, the policy to correct the trade deficit in the name of the America first policy, is clearly a protectionist policy. The US has the world’s largest trade and current account deficit, but it goes without saying that a deficit in the trade and current account for a nation is completely different from a deficit on the profit and loss statement for a company.

Although well known, I feel I should remind you that a country’s current account balance is determined by the difference between savings and investments on a macroeconomic level. While there may be arguments about the rights and wrongs of a cumulative current account deficit where the sustainability of such debt is called into question, a current account deficit of itself is not necessarily a problem. The US has enormous domestic demand,

and the current account deficit has resulted from the amount of investment exceeding domestic savings. This deficit is currently financed by the investment that is fascinated by the strong US economy.

The simple dichotomy of ‘exports are good, imports are evil’ is a mistake. Exports and imports are both the results of economic activity involving production and consumption by both companies and individuals. I have looked at your proposed border tax adjustment to “exempt exports and tax imports” that is also supported by the Republicans Party. However, given the globalization of corporate activities and the existing global supply chain that is centered in the US, as the world’s largest consumer market in the world, the introduction of a border tax adjustment can only lead to considerable turmoil. The impact will not be limited to specific industries such as apparel and retail. There should be substantial impact on the network of economic activity regardless of industry or nationality. The prices of imported raw materials, intermediate goods and finished products could all rise, which will most likely be negative for consumer prices and consumer spending from a macro perspective. Naturally, the border tax adjustment will also be seen as an export subsidy and/or import penalty, which would be in breach of World Trade Organization (WTO) agreements. There are also concerns that a suit filed in respect of the WTO could trigger international conflict. The introduction of the border tax adjustment needs to be done with careful consideration.

My second concern relates to US manufacturing policy. One reason for your success in the Presidential election was the strong support enjoyed from citizens living in the so-called rust belt, from the mid-west to the north-east of the US. While the support was not limited to rust belt states, as President, you have proposed a jobs first principle. This can also be interpreted as an aim to restore the manufacturing sector.

While Japan boasts about being a “manufacturing superpower” through craftsmanship, and I am a believer of the importance of manufacturing, I doubt the viability of the US aiming to become a manufacturing superpower. Historically, employment in the US manufacturing sector has been in decline from a peak of just under 20 million at the end of the 1970s to recent levels of just more than 12 million, a drop of close to 40%. Employment in the manufacturing sector has fallen to about 10% of the total US workforce.

The decline of employment in the manufacturing sector has been offset by increased employment in the services sector. While the issue of improving the quality of employment persists, the US currently has a situation that is close to full employment.

The type of manufacturing US should strengthen should not be grand large-scale manufacturing, nor should it be traditional manufacturing. While manufacturing activities requiring enormous sites for factories might have appeal for the real estate sector, which is the President’s area of expertise, areas that are currently in the limelight include the Internet of Things (IoT), Big Data, Artificial Intelligence (AI), robots, new energy, and new materials, etc. New demand can be created by merging these new technologies with traditional businesses. This requires the ability to innovate and build platforms, which has been the source of US production competitiveness.

All the world’s top 10 companies by stock market capitalization are US companies. 31 of the top 50 are US companies as of March 8. All these companies are renowned globally as innovators and transformers. They are akin to the goose that lay the golden egg.

For reference, Apple has the highest market capitalization in the world and produces iPhones mainly in China where components using the latest technologies are brought together from around the world, including these from Japan. What makes iPhone distinctively an iPhone is its design and software, not the hardware. I cannot see a scenario where it would be economically rational to assemble and produce iPhone in the US. What is important

for a company is its competitive advantage, but what is important for the economy is the use of each country's comparative advantage to increase the welfare of the entire world through trade.

My third concern is the attention that must also be paid to exclusive immigration policies. While I would not argue against the importance of controls to protect coastline border to prevent terrorism, US economic growth and competitiveness has been built on the back of immigrants.

Immigrants are also a precious resource for the working population. The US has more than 40 million immigrants, accounting for about 14% of the population and making the US a major immigrant country. The annual growth in the US working population is at most 2 to 3 million, so any reduction in the number of immigrants should be a constraint on growth.

Immigrants make major contribution to the US economy not only in terms of numbers but also in terms of quality. Many venture companies, including high profile companies in Silicon Valley, have been started by immigrants. The diversity and dynamism derived from the acceptance of immigrants with a strong desire to better themselves should be one of the strengths of the US. In an era when industry, government and academia join to foster venture companies, competition is heating up between cities around the world. In fact, policies that hinder the acceptance of immigrants are akin to throwing the baby out with the bath water.

There is a saying in the East that "a wise man changes his mind, a fool never will". Regardless of what you have said in the past, if America is truly to become a Great Country, I hope that you will embrace your role as President and institute a complete change, by making bold adjustments to your previously indicated direction in relation to trade, industry as well as immigration policy.

Yours sincerely

Katsuyuki Hasegawa

Chief Market Economist

Mizuho Research Institute

katsuyuki.hasegawa@mizuho-ri.co.jp

This publication is compiled solely for the purpose of providing readers with information and is in no way meant to encourage readers to buy or sell financial instruments. Although this publication is compiled on the basis of sources which we believe to be reliable and correct, the Mizuho Research Institute does not warrant its accuracy and certainty. Readers are requested to exercise their own judgment in the use of this publication. Please also note that the contents of this publication may be subject to change without prior notice.