

Impact of Inward-Looking U.S. Policy on Japan

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Trump administration's trade policy stoking protectionism concerns

The Japan-US summit held on February 10, 2017 couldn't have been better for Japan, with both leaders pledging to make the Japan-US alliance for security stronger and US President Donald Trump refraining from making reference to Japan's trade surplus with the US and to yen-dollar exchange rates. Since his assumption of the presidency until the summit meeting, President Trump criticized Japan's auto industry and the yen's weakness. The latest Japan-US summit may have worked to cast aside concerns for the time being.

However, the outcome of the latest summit meeting should not be taken to indicate that potential US demands over bilateral trade ties can be held in check. Indeed, on March 1, the Trump administration unveiled *the National Trade Policy Agenda for 2017*, the first official document outlining its trade policy, stating that, "The overarching purpose of our trade policy...will be to expand trade in a way that is freer and fairer for all Americans." The message is clear, as can be construed from "for all Americans." It is that the US seeks bilateral negotiations and will focus only on whether existing arrangements will be conducive to US economic growth and creation of employment, and if the results prove unsatisfactory, it would not hesitate at renegotiating trade agreements. This is precisely the stance repeatedly advocated by President Trump and his key aides from early in the election campaign. Going forward, if the Trump administration determines that "fair and reciprocal market access" cannot be secured by bilateral negotiations, it is quite likely that the US will press for open markets by drawing on all of the measures it holds, including trade remedies and Section 301 of the US Trade Act.

Since the US economy is now in the recovery phase, there will not be a repeat of the situation where US industries make a chorus of protectionist demands. However, the white working class that proved to be the solid support base to bring about "President Trump" has strong grievances that globalization has deprived them of their jobs. It should be assumed that President Trump will take a hard-line stance on trade issues to some extent from the standpoint of making an appeal to the white working class.

The biggest victim of inward-looking US will be Japan's auto industry

If trade protectionism did actually manifest itself, how much of an impact should we expect to see? Looking at the value of Japanese exports to the US in 2016 by goods, automobiles accounted for 31% of the total value. This percentage represents only automobiles shipped directly from Japan to the US market. Even when automobiles exported via other countries for assembly reasons are included, the high ratio shows little change. In fact, if we look at the impact of a uniform 10% decline in US imports, including the indirect ripple effects through the global supply chain, the automobile sector stands out among Japanese industries that are expected to be affected [Chart

1].

Next, narrowing down the target to automobiles, we estimated the impact on automobile exporting countries if the US raised its tariffs by 10% globally [see **Chart 2**]. This shows that US consumers would be at the greatest disadvantage, but in terms of producers, or the automobile industry, Japan would be the biggest victim among major automobile-producing countries. The decline in producer profit would amount to \$4.3 billion, or ¥500 billion. Countries with the next largest losses following Japan are Mexico, Germany, Canada, China and South Korea—top countries exporting to the US. In terms of overall economic losses, including consumers, the loss for Japan would be \$1.5 billion, smaller than that for Mexico, Germany or Canada. This stems from the fact that in the case of Japan, the increase in consumer benefits would be larger than that in those countries. Consumer benefits would increase because automobile prices would fall due to a decline in the US's import demand associated with the hike in tariffs. It is considered that the consumer benefits turned out to be larger in Japan and China with the relatively large domestic automobile market.

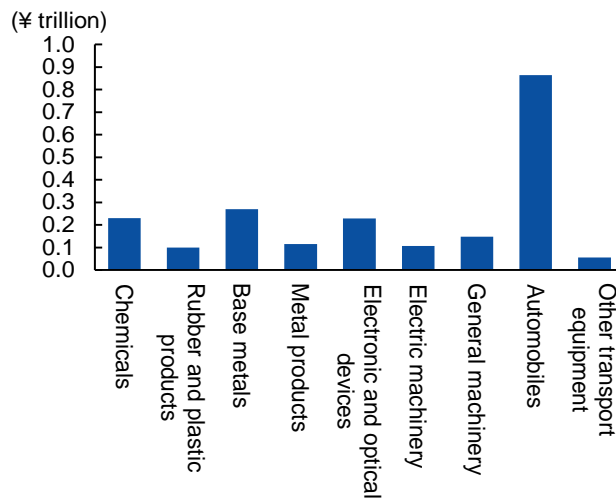
It should be also noted that the tariff hike by the US would bring about an economic loss of \$1.5 billion for the US itself as well. As demand shifts from imported vehicles to US-manufactured automobiles as a result of the tariff hike, producer profit for the US automobile industry would significantly increase. However, US consumers would suffer a loss to the extent that sales prices of automobiles rise in the US market. Since the fall in consumer benefits, or \$27.1 billion, slightly exceeds a sum of the increase in producer profit of \$9.1 billion and an increase in tariff revenue of \$17.6 billion, the US economy as a whole would see a small loss. Therefore, even if the US administration diverts the increase in tariff revenue to fund economic measures, unless such funds are spent on projects conducive to an enhancement of long-term growth potential, the tariff hike would prove to be negative for the US itself. Furthermore, if the increase in tariff revenue is diverted to projects that hamper economic growth, such as construction of walls along the border with Mexico, the economic loss for the US may turn out to be larger than our estimates in this article.

Protectionist trend in the US requires continuous watch

As discussed above, if the US raises the tariff rate on automobiles in a single uniform way, the negative impact on the Japanese automobile industry would be extremely large. Also, it can hardly be said that it would bring a positive impact on the US economy. While some may opine that the uniform tariff hike would not happen in reality, it must not be overlooked that the Republican Party has already proposed the “border adjustments” as part of corporate tax reform. The proposed adjustment is to tax imports from all countries (imports included in the taxation base without allowing import expenses deduction). If realized, the adjustment is likely to bring about the same effect as the tariff in a practical way. It will be necessary to continue closely monitoring inward-looking trends in the US.

[Chart 1 Ripple effect in Japanese industries]

When US imports from the world fall by 10%

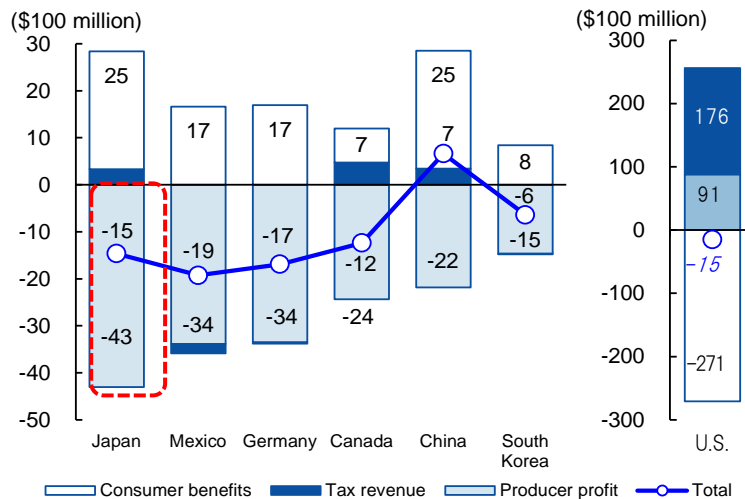


Note: As of 2014. The impact was translated into yen terms using the 2014 exchange rate.

Source: Compiled by Mizuho Research Institute Ltd. based on "World Input-Output Database (WIOD)," etc.

[Chart 2 Impact on the economies of other countries]

When US raises tariffs on automobile imports from the world by 10%



Note: Estimated by reflecting the latest data from the "World Input-Output Database (WIOD)" (trade data) and "TRAINS" (tariff data) in the GSIM model by Joseph Francois and Keith Hall.

Source: Compiled by Mizuho Research Institute Ltd. based on WIOD, UNCTAD

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