Cleveland Fed Conversations on Central Banking: Examining the Effects of Tariffs on the Economy

Welcome:
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Moderator:
Archie Hall, Britain Economics Correspondent, *The Economist*

Panelists:
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Steven B. Kamin, Senior Fellow, American Enterprise Institute
David Weinstein, Carl S. Shoup Professor of Japanese Economy, Columbia University

Damjan Pfajfar: Welcome everyone to the Cleveland Fed’s Conversation on Central Banking Series. I'm Damjan Pfajfar with the Cleveland Center for Inflation Research. Thank you all for joining us today.

This conversation is part of the work that we are doing at our center for inflation research to help researchers, policymakers and the public understand inflation and the monetary policy. We typically hold 2 or 3 events per year. Please subscribe to our newsletter to be informed about future editions of conversations on central banking and other news about inflation and the center.

Today's topic is examining the effects of tariffs on the economy. To give an overview of how tariffs can affect the economy. We'll be focusing on past episodes when tariffs were enacted and examine the effects tariffs had on inflation and economic growth.

We have an outstanding program today in a short format. We'll jump into that in just one moment before we start. I just want to let you know that these conversations are being recorded, and the recording should be up on the Center for Inflation Research website this afternoon. We'll now turn to Archie to introduce our panelists.

Archie Hall: Thank you so much, Damjan. I'm Archie. I write for the economist, and very excited to moderate this event, and promises to be extremely interesting. I'll keep this fairly short, but I'm very excited to hear from our 1st panelist, David Weinstein, of Columbia University.

David E. Weinstein: Great. Well, thanks very much. I'm going to just jump right in and just give a few short overview of what exactly has been happening with the tariffs that we've implemented, which I think provides a lot of guidance for what we should expect to happen in the future as we impose more tariffs. So I'm going to focus initially on the tariffs that were implemented by the Us in 2018 2019. And just give the audience some basic stylized facts about what happened. So, this plot that I'm showing you shows what happened to price changes of imports for goods that were not hit by tariffs that's in black. And then for all of the goods that were hit in the 2018 to 2019 trade war in colors, and on this plot 0 corresponds to the moment that the tariffs were applied. And what you can see pretty clearly is that there was not much movement in the prices of goods that were not hit by tariffs in the U.S. Market, but goods that were hit by tariffs saw their prices jump substantially in response to that. And so, what the tariffs did was they essentially raised the prices of largely Chinese products in the U.S. Market, and that was passed on as best we can measure it completely to consumers. Second thing, that there's been a lot of confusion about as we think about these tariffs is whether they help or hurt firms. And the basic answer to that question is, it depends a little on the on the tariffs. So often people think about output tariffs.

So, you might think about applying tariffs to automobiles, and when you apply those tariffs you raise the price of foreign automobiles relative to domestic, and that may be good for us producers of cars. But it's going to be bad for us consumers of cars. But what this simple notion of tariffs typically misses is that tariffs are heavily applied on inputs and goods like steel. And when that happens it raises the costs of us producers and hurts their profit margins. And you can see kind of how tariffs have impacted the U.S. economy in the following picture.

So, this, the blue bars correspond to the shares of imports from various countries in 2017, before the trade war began and the green bars correspond to the import shares in 2024. And so, you can see, starting on the left that the share of goods we got from China has fallen quite substantially, and then you can see that a lot of that was made up by importing from Mexico and Vietnam in particular, as well as some other non on some other developing countries.

So, what that's telling you is that the trade war shifted production from low cost locations like China to high-cost locations, and when it does shift towards places with low tariffs, you often don't get very much tariff revenue, but you do pay the extra costs. The second thing is, each blue bar is divided, or each bar is divided into a dark region. Which shows you what fraction of the goods were output tariffs and a lighter region, which is the input tariffs. And you can see that something like 50 to 60% of all imports.

Our intermediate inputs, things like steel. And so, when the tariffs hit those products, you should realize that that's undermining us, competitiveness in final goods industries. So, if the cost of iPhones from China goes up that hurts Apple computer because they have to pay more for each iPhone that they're importing.

Likewise, tariffs on steel are going to hurt us auto producers. So, the net impact of this in 2018 and 2019 were some pretty big movements in stock prices. So, this final table shows you what happened to stock returns on the 11 days in which there were announcements from either the United States or China on tariffs. So, there were about 6 announcements from the U.S. In the Trade war, and about 5 announcements. Excuse me from China. The second column shows you what happened to the percentage return in the U.S. Equity markets on those days, and you can see that of those 11 days. 9 of them resulted in fairly substantial drops in the market, and the market fell a cumulative 12 percentage points or 11.5 percentage points over the course of all these announcements, so kind of the volatility that we've been seeing in the stock market over the last month is pretty much par for the course for what happens when the U.S. Implements, tariffs, or China or other countries retaliate.

So, the other thing that we see in this and I'm sure Kyle is going to talk a lot more about this in his session is that when we decompose, why it is that the market is reacting that much. What we find is about half of that fall is due to greater uncertainty, and you can measure that uncertainty by using indexes like the vix and other related indexes which tell us how much companies kind of futures are potentially in peril as a result of that. So, if I if I have like 2 more minutes. I wanted to show 2 more slides. The last thing I want to just end with is just talking a little bit about job creation and tariffs.

And we can kind of think about steel as a case in point about what is causing job losses and how tariffs have impacted that. So, this 1st chart just shows you that over around 30 years Steel has received an enormous amount of protection. About 60% of all steel imports receive some sort of protection and very often that protection has targeted China, which is the red line in that about 100% of all Chinese steel is hit by tariffs and about 60% of world steel. But if you say, Okay, well, how much has that affected job growth in steel? You can just see that in a simple plot here which shows in blue what's happened to steel workers. So, the number of steelworkers between 1990 and the present has fallen pretty sharply. Steel output has not risen. It's basically flatlined. So, if you thought that the story of lost steel jobs was simply due to lower steel output. This plot tells you that's not what's going on. Steel output has been fairly constant over this time, but steel jobs have been disappearing. Why is that? It's because of automation that jobs that used to be done by people are now being done by machines, and those efficiency gains have resulted in smaller employment in steel, so at least as far as steel is concerned, don't look to tariffs as a means of increasing employment. Okay, I've gone a little over.

Archie Hall: Great. Thank you so much, David. Really, really interesting, and I'll hand it straight over now to Kyle Handley of U.C. San Diego, to continue.

Kyle Handley: Okay, thank you very much for having me. I don't have slides, so I'm going to talk through what I think are the main effects of what I call trade policy, uncertainty on trade, and just to give a little bit of background for a couple minutes, I want to talk about the original kind of motivating questions, for why I started working on trade policy, uncertainty. And this is work I've done with multiple different co-authors, but namely, Nuno Limao at Georgetown, but we were interested in how trade agreements seem to increase trade quite a bit, and increase entry of new firms into trade participation on both the export and the import side, even though, typically, when a country like the United States signs a trade agreement with Canada or Mexico or Australia, the reason they can make common cause and agree that we're going to lower tariffs is because typically their tariffs are already pretty low on each other. So, there's not too much to bargain down. But this also happens more broadly at the WTO. And its predecessor organization. The general agreement on tariffs and trade, where the countries that are part of the WTO part of the GATT are basically entering into an agreement not to raise tariffs above some certain ceiling. The WTO refers to these ceilings as bound tariff rates or bindings. That's actually what they negotiate over. They don't negotiate over applied tariffs. And so, these 2 things are connected.

So, if you sign a trade agreement like NAFTA, it's an agreement not to raise tariffs above 0 on products that satisfy the criteria that are set forth in the agreement, and if you're in the WTO. You've already agreed as part of your membership not to raise tariffs above some ceiling rates, and of course, there are lots of ways to sort of escape from this. We have anti-dumping duties and safeguards and things like that, and those have been heavily used by the U.S. And many other countries, but for the most part I would argue until around 2018, most countries were kind of abiding by the agreements that they'd already signed and they were exercising higher tariffs and increasing them occasionally, but within the frameworks that they had agreed to over the past like 50 or 60 years, and that all kind of ended starting in 2018, and has since, as I think, most of us know, gotten substantially worse. So, to go back to our original questions. It's like, why do these trade agreements increase trade so much when, as I just argued, the tariffs actually don't decrease that much than what we thought?

And I think we've shown in a number of papers is that the main thing that's happening? Well, I shouldn't say the main thing. But one of the many things that's happening when countries sign trade agreements is these commitments not to raise tariffs are valuable to firms and the businesses that are actually engaged in the business of international trade. And if they're going to make large investments into selling their products in new markets or large investments in sourcing inputs from other countries. It could be China or Vietnam, as David was just explaining to U.S. They want to know that their market access is secure.

And so a big part of what trade agreements do is they secure that market access through reciprocal commitments, not reciprocal tariffs, which we've been hearing a lot about lately, but the reciprocal commitment not to raise tariffs sort of outside the rules that are set forth in these agreements, and these things have been very important in a number of different contexts. And so, I'll just mention a few things and then talk about what I think is lessons for what might be happening now. But in in the WTO itself, and sort of the early sort of rounds of the GATT. So, one of the statements in the 1948 GATT charter is it explicitly says that binding against the increase of low duties or of duty-free treatment, shall in principle be recognized as a concession equivalent in value to the substantial reduction of high duties. And so, what they're saying is that sometimes promising not to raise a trade barrier can be just as lowering the tariff. And so, when I've looked at this in different contexts, so with respect to the WTO. Those bound tariff rates when they're reduced. And this has happened through multiple rounds at the WTO.

And its predecessor, the GATT that those promises not to raise tariffs also increase trade, and they increase trade participation in terms of the number of products that are traded and the number of firms that are exporting those products, but also through trade agreements. So, when the EU is expanded, the research that I've done has been on Portugal and Spain's accession.

In 1986, we saw a substantial increase in the value of trade between Portugal and the European Union, a substantial increase in the number of Portuguese firms that were exporting to the EU, which was the EC. At the time, but they didn't really get big tariff reductions. What they got was they secured preferences that they already had, because Portugal was trading on a duty-free basis with the EU because of a number of different agreements that have been extended, but only on a unilateral basis, and so, when those were made permanent, it was a rather large deal for Portuguese firms to have that secure market access. The same thing happened more recently in the 1990s, when the United States would threaten to revoke China's most favored nation status pretty much every year. In some years Congress actually passed some conditional, most favored nation (MFN) bills, but they were vetoed by President Bush. This went on for most of the nineties until China joined the WTO. And the United States granted them permanent MFN. as part of the agreement of China joining the WTO. And the U.S. treating them like they treat all other members, and what we found in our research is that for the increase in Chinese imports that the U.S. saw between about 2000, 2005 around 30% of it was due to reductions in uncertainty. Now, there's other things that were going on in China. At the same time they were lowering their own tariffs, making other commitments to join the WTO.

But it wasn't tariff reductions. It was a reduction in sort of this risk that Chinese firms faced, and the American importers would have faced that. Tariffs would have gone up, and us firms were going before Congress and doing similar things that they're doing right now and complaining that we're operating in an environment where you threaten to revoke MFN every year. But we plan in 5- or 10-year cycles, and these things are sort of inconsistent. And so, they hold back on investment. And so, what happened, I would say, through most of the eighties and nineties into the early 2000s is there was a large fall in trade policy, uncertainty worldwide and certainly with respect to how the U.S. Was treating a lot of other countries due to WTO accessions due to a number of trade agreements that the U.S. was signing. And then things started to increase again in 2018. And we're in an environment. Now, where there's a lot of us firms that are facing retaliation abroad, and other firms that might want to sell to the U.S.

That face, you know the risk of higher tariffs, or actually facing those tariffs right now. But if you're a firm in the United States, you don't know what your level of protection is going to be tomorrow or in 100 days from now. And we got this news last night. Actually, that a number of the tariffs that have been put in place have been ruled illegal by one court in the United States, and so the tariffs could maybe go back to 3 or 4% on a lot of countries within the next week.

Or there's some risk that they'll return to 10 or 30%, or even 145%. And so, what we have right now is basically 2-sided uncertainty where the firms in the domestic U.S. businesses don't know if they should invest in hiring new workers invest in new production capacity because they might be protected today. But they don't know what's going to happen next week. And then there are other businesses outside the United States, and other firms that are trying to make sourcing that don't know if they should be importing or exporting because they may face higher tariffs. And so, when you have that level of uncertainty, essentially, what happens is most firms kind of freeze up and wait to see what's going to happen and reduce investment along multiple dimensions in terms of capital investment in terms of hiring new workers, as I already mentioned, and also the large costs that they have to pay to sort of source inputs from a new market, or, you know, start exporting and tailoring their products, say, for China or Europe or Mexico.

A lot of those investments aren't happening now and we'll see the impact of that, probably not next month. But maybe in a few years when a bunch of foregone investment hasn't happened. And so that's all I have to say. At this point I'm looking forward to see what Stephen has to say next.

Archie Hall: Wonderful. Thank you so much, Carl. It's really interesting. And finally, to conclude, Stephen Kamin from the American Enterprise Institute.

Steven Kamin: Thank you. It's great to be here and chat with your audience. I'm going to go ahead and share my screen, which I think I've done, and everybody see my slides. Okay. yep, alright great.

I want to talk about the Fed's response to tariffs. Back in 2018 to 2020. I was on the Fed staff at the time the Board of Governors in Washington, so I was able to have a ringside seat for that. This slide here is just a summary of what David's already talked about. The many trade actions taken during that period, which included not only impositions of tariffs, but threats of future tariffs, as well as quite a few retractions from tariffs already either threatened or imposed.

So, in that environment of uncertainty is where the Fed had to act. Now, just to reprise. As David's discussed tariffs are a supply shock. They raise costs which is bad for inflation. They lower output not good for employment. So, the Fed's job to stabilize the economy needs to take those into account. The problem, of course, is well known. Monetary policy doesn't act right away, takes a while. And so, in principle, if the Fed anticipates, shocks down the road, it ought to act preemptively.

But how can it do that when the Fed has no clue about where terrorists are going to end up? What they're going to do to inflation, and what they're going to do to output? So, that was the situation that the FOMC. Was grappling with back in 2018 as well as the Fed staff where I was working in the International Department as we tried to construct our baseline projection for the U.S. Economy that we would then hand off to the FOMC. For their deliberations.

So, we given all the uncertainty, we didn't want to incorporate tariff effects into our baseline, and we didn't. Instead, what we did was we developed an alternative scenario for what would happen if there were 15% hikes in tariffs on all our trading partners, coupled with similar retaliation by our trading partners on imports for the United States, and these were included for the 1st time in the July 2018 Teal Book, where the teal Book is the briefing document we delivered then to the FOMC.

And these charts here are, you know, copied and pasted from that teal book. The solid lines in both charts indicate the Fed's base of the staff's baseline projection, and the light blue line labeled Higher Trade Barriers, represents that alternative scenario I talked about. As you can see, we modeled the effect of the tariff of a 15% tariff hike with retaliation as leading to a plunge in GDP growth into negative territory. A big increase in unemployment relative to baseline. Also, a soaring inflation rate up to 4% in a couple of quarters before then quickly subsiding, reflecting in large part the assumption of anchored inflation expectations and then finally, on the right, you can see that again. The light blue line, the Federal funds rate rising substantially above the baseline as the Fed responded to inflation and then falling below the baseline. As then, monetary policy responded to rising unemployment.

Now, in the event the tariffs that ended up taking place were not that huge. Okay, so this is a picture of average tariff rates. You can see it skyrocketing at the very end of the sample. But focus on the time around 2019 2020. And you can see basically just a bump in average tariffs of only a couple of percentage points. So not a big increase and therefore not a big increase in inflation. So that ended up not being a problem for the Fed and that lack of being a problem was reinforced by the fact that the Fed had spent the last decade struggling to get inflation up to its 2% target and to keep it there.

So, inflation ended up, not being a worry for the Fed, but at the same time, as Kyle has described trade policy. Uncertainty did rise substantially, and you can see that, you know, in the initial bump up in 2018 to 2020, obviously dwarfed by what happened a few years later, but at the time we thought that was a very big increase in uncertainty. And it wasn't just U.S. you know. Private businesses did, too, and in response to that uncertainty, as Kyle's described, investment fell off, and industrial production shown here fell off going negative and the combination of the weakening activity as well as the quiescent inflation allowed the Fed to start lowering interest rates by the middle of 2019.

So, a key factor in that was the quiescent inflation that I've been harping on all right, which was based in turn on well anchored inflation expectations now going further, bringing us into the present. That is, you know, that needs to be a key focus of Federal reserve deliberations, and I will stop there.

Archie Hall: Lovely. Thank you so much. Well, I mean just to start off on the questions I'd be keen to pick up on that final thought of yours, Steve, and kind of the question of when tariffs operate as a one off increase in the price level versus when tariffs kind of can shock the system enough to potentially cause a risk of longer term or persistent inflation, obviously, is a question that's sort of front of mind. And maybe actually, yeah, I mean, Steve, just to while you're here, be curious for your sense of I mean, obviously 2018 19 was a very particular case with inflation being quite well anchored. But what's your sense of what determines that that inflation relationship more generally.

Steven Kamin: Right? Well, it's interesting. You bring that up because when I presented those simulations to the FOMC, back in 2018, so yeah, one FOMC, member. This is all public. It’s a public transcript. One FOMC. Member said, well, you know, wouldn't the Fed look through that increase in inflation because it's like a 1-time supply shock. Okay?

And I responded, well, you know, there's a lot of uncertainty. There could be more tariff hikes coming down the road leading to a more gradual increase not entirely clear. You know how well anchored inflation expectations actually are so in the in the following FOMC in September, we actually did a look through scenario. Okay, where? Where we assumed the Fed did look through that increase in inflation. And it didn't actually change the pattern of inflation very much, but it led to much better output performance.

Now to your question. We don't really understand what drives inflation, expectations that well, and so we don't actually understand what drives inflation. That well, but my guess is that if you have a very large surge in inflation like took place a few years ago. And then, if you couple that with noting that the surveys of inflation expectations in the last few months have soared upwards. That would suggest to me that inflation, expectations, and inflation behavior are less well anchored than they were at the end of the previous decade, and that raises the risk of more persistent and kind of like second round effects of an increase in tariff costs on inflation.

Archie Hall: That makes sense. Just pulling in, David, I mean, I found your charts fairly striking of the kind of various 2018 19 tariffs. As a case study of this, I suppose the long term impacts we can't really see given the pandemic happened so soon afterwards. But what's your read of the evidence there, and what that, what that does suggest here.

David E. Weinstein: Well, I think. You know, I think I think current set of tariffs are much bigger than what we saw in 2018 and 2019. You know, it's very hard to do forecasts, because the tariff rates are constantly changing, you know, and today is just another good example. You know you prepare a set of slides by 5 Pm. The day before, and by the morning of the next day. They're somewhat outdated. So that has, you know, I agree with. I think I think there's kind of consensus that uncertainty is having a negative effect on investment.

I think it's also likely to make Americans feel worse off right that as you as you become uncertain about the future you're likely to you know, your welfare is likely to fall simply because, you know, we value uncertainty. So, it's kind of affecting investment. It's affecting consumption as well and you know it's very again, I think it also affects our ability to forecast, because we simply don't know what tariffs will be in 90 days. And that's a huge problem for academics. That's a huge problem for the Fed, as Steve was saying. And that's a huge problem for firms and consumers.

Archie Hall: That makes sense. Well, I'm pulling Kyle in on the uncertainty question. I mean, I'm calling in from London, which obviously is kind of on the long downslope for big increase in trade uncertainty, post Brexit, and gradually find more certainty there. I'm kind of selfishly then kind of curious for your view on kind of the decay time, as it were, here. I mean, you're talking about mostly kind of long-term reductions. Uncertainty through trade deals when there is a big upswing as there was in Brexit as there is right now. How long does that last in your experience?

Kyle Handley: Yeah. So, I mean, I think with respect to Brexit. So, I've also done research on Brexit uncertainty and specifically on prices and one of the things that we found is that Brexit uncertainty.

I mean one interesting thing about Brexit, and we have this now for the more recent episodes of, you know, with the new trump tariffs. But there were prediction markets and betting markets on, you know, is Britain going to leave the EU basically on the referendum. And so what that did for us is we were able to measure like the probability that this might happen. And then, you know, there's additional uncertainty because you don't know if they're actually gonna leave, or what shape the deal is. Gonna take.

It looked like in the data that we were using, which was high frequency monthly data on trade flows, you know, for the different products that might get hit with higher or lower tariffs if UK importers and exporters got hit with much higher, most favored nation rates and those we observed impacts in prices and trade participation even before the outcome of the referendum was known, just because we could see that the probability would go up, and then it would go down, and then it kind of went back up again right toward the end. And those things had had impacts on Uk prices import prices for sure, some of which may have increased prices for manufacturers on inputs by 2 or 3% and that's just the uncertainty from pre-Brexit, and then, I think, got extended further, although I can't put numbers on that. But I do think one thing that is important is that I kind of mentioned this earlier is that because investment for the most part happens on the margin. So, there are factories in the UK. And there's factories in Europe. And this is also true in the United States, where they're not just going to shut them down tomorrow.

But they're not going to make the investments that they maybe would have made to sort of retool them or make sure that the machines are running smoothly, or that they're fully staffed up. They might let workers go because they don't want to have excess overhead, and those are the sort of things that I think I guess, to use your terminology, maybe decay over time. And we'll look back, you know, over the longer run, or even the medium term, and see that there's there's less trade, potentially higher prices, fewer varieties available for consumers, which, you know, as David was mentioning, could be detrimental to welfare, because I think Americans like to go and see shelves that are full of different products, and some of those things may disappear, and those are the margins on which, over the longer term, I think we start to see the impacts of uncertainty because it's all the investments and new products and technology that just are not made. And so some of that is playing out in real time right now in the Uk.

And we may see scenarios like that in the U.S. Depending on what happens over the next few weeks or the next few months. But we'll be talking about that, probably in, you know, late 2026 during the election cycle about. You know. What are people mad about at the store? And we'll see. We'll see what's out. What's going on.

Archie Hall: Yeah. And what's your sense of kind of how? How long the scarring is of these sorts of uncertainty episodes? Because obviously, I mean, yeah.

Kyle Handley: Yeah.

Archie Hall: Moment, and then loss presumably gradually do get more certainty. How does that? How does that go.

Kyle Handley: I think the scarring is pretty deep. So, the way I think about this is that it took the United States almost 50 and if we go, you know, up to 2018, like 70 years to build up the rules-based trading system that was originally the GATT in the WTO. And then all these trade agreements that the U.S. Had signed and now has kind of backed off of.

And so that's a lot of goodwill and credibility that the U.S. Commitments were secure, and they weren't going to back off of them, and I think most of that has been in the last few months. Any goodwill that was left has been destroyed, but I think it was already, you know, cracking, and a lot of it had been lost as of 2018, 2019, and that will take a long time to rebuild, and the unfortunate side of that is, during the financial crisis. U.S. Trade with partners where we had trade agreements. So Canada, Mexico, Australia the Dominican Republic CAFTA agreement was pretty robust like we didn't see a lot of us firms like exiting the market. They didn't export as much because there was a big economic downturn, but they stayed in.

And one of the reasons for that was because if you have trade agreements, they basically decreased the correlation between bad economic shocks and sort of knee jerk protectionism and most of the G. 20 at the time was, you know, committed to like not repeating the historic mistakes of protectionism of the 19 thirties, they would put that in the communicate like every 3 months.

And that worked. And I think we're in an environment now, not just with respect to the Us, but the whole world, and Brexit is another good example where you know, countries are getting divorced when they spent the last 50 years. Getting married, and divorces are messy, and it's hard to rebuild that credibility. And I think, like we're we may spend. If we're going to go back to where we were, it could take another 50 years. And so, everything will just be a little bit less secure and stable for quite some time.

Archie Hall: David, you raised your hand. You want to pop in.

David E. Weinstein: I just wanted to build a little off of what Kyle was just saying, which is, I spent a lot of time in Asia, and one of the things that's shifted fairly remarkably is that when Asians, Asian nations, Asian nations, talk about risk, now they talk about managing the United States risk and de-risking their economy or reducing their exposure to the U.S. Economy, because they just see it as an unstable trading partner, that they don't know what the rules are going to be. They don't know what the visa restrictions are going to be, and this is giving China an enormous edge relative to the United States because they portray themselves as a stable trading partner. You know, whatever the vagaries of Chinese regulations are at this point. It's nothing like the volatility we've been seeing in terms of us trade policy. And so, I think this is going to.

You know, we're seeing the collapse of the world trading organization, which was the rules-based system, you know. For all intents and purposes, it's not able to regulate trade anymore. And we've moved into a wild West of U.S. Trade policy. And I think a lot of nations don't want to have that kind of exposure. This is going to fundamentally realign a lot of trade and political relationships, not just with Europe and Canada, but also in Asia, more broadly.

Steven Kamin: If I could pop in, I mean, I broadly agree with everything that David and Kyle is saying. At the same time, I think it's a little ironic. China is not like noted for its tremendous commitment, you know, to you know, the kind of unadulterated rule of law, and yet many countries do, as David's pointed out feel that they could probably have a more stable trading relationship with China than with the United States. I kind of wonder whether, you know, if our current, somewhat lawless trade policy environment persists whether eventually businesses would learn to work with it and maybe the damage might not be quite as egregious. You know, as maybe Kyle and David have pointed out.

Archie Hall: What are the sort of things you can imagine businesses doing to learn to accommodate this new world.

Steven Kamin: Well, I think they'd probably shift to what many businesses in many developing countries do, which is develop stronger you know, kind of rent, seeking relations with their governments and with other governments. Kinda again, work on a more transactional basis.

It's notable that businesses in in many, like, for example, Latin, American, and African countries work in environments that are way more tumultuous than you know in the United States and Europe. They do manage to get by. So, I'm not saying this is all a good thing. I'm only wondering whether, possibly, some of the downside scenarios are perhaps not as extreme as you could paint them to be.

Archie Hall: David, Kyle, curious. If you have immediate reactions to that.

David E. Weinstein: Yeah, I mean, I think you know, I think there's been one of the things that we're seeing is that the administration proposes things and then pulls back. You know, we saw enormous shifts around April second, when the Liberation Day tariffs were announced, and it started to look like we might face some sort of crisis in in terms of currencies. That you know, on some level, I think that is a that is a mitigating factor. And so, when one can be optimistic about it. But I think once you, once the trust in a country is lost. It is very hard to regain that right. It'll be very hard, you know, if you look at. Say U.S. policy towards Canada and Mexico. We signed a revised NAFTA, USMCA. And then the same President that signed that then wanted to tear that up. And so you ended up with you know, it's very hard now to go back to them and say, oh, actually, we want to go back to this. And apropos Kyle's comments and say, oh, and these tariffs are going to be in place.

These levels are going to be in place for the long run. And I think that many countries at this point would welcome lower us tariffs, I think that's clear, and that would likely be beneficial. But I don't know how you can unring a bell that's been rung that once we've done this. It's very hard to then convince people that this is the way it's going to be for the next 20 years, and I think that's going to be a challenge for us policymaking going forward. So again, I think that we may see some rollback of the tariffs. I think that's likely, but I think there's been, you know, significant amounts of damage done.

Archie Hall: Oh!

Kyle Handley: Yeah, my thinking would be that I mean a lot a lot of a lot of businesses. I mean, you have to think the big importers and exporters in the United States. They're all multinational firms. So, they're most of the employment. They're most of the imports. Most of the exports. There is heavily concentrated in these really big firms that don't just operate in the U.S. And so, to the extent that they'll adjust to it it's basically going to be by moving as much of their supply chain as they can out of the United States, because it's not reliable. And so will they continue to produce things for the domestic market like they absolutely will. But they'll move all the scale to other countries, and which are gonna probably continue to integrate without the United States as part of that and the U.S. Market is big enough that it can continue to support. You know some of these, you know, larger operations, and they'll continue to produce automobiles, you know, for the U.S.

Market, and maybe with high tariffs going back and forth between the U.S. And Mexico. But I think and I think harkening back to my earlier comments, I think what may happen is that you know. Now you can choose between probably 35, 40 different models of 4 door sedan for multiple different companies. And Americans may find that there's only 15 in another 10 years, you know, depending on what happens, and there will still be 30 or 40 or 50 models for everybody else in the rest of the world.

But there just won't be enough scale where we can have all these different varieties. And so, I mean, I think I think one example I use is, I think, the you, the

Kyle Handley: the that they only make the corvette, you know, in one factory which I can't remember where it is right now, but it's in the U.S. And they ship it all over the world.
And it may just not be practical to do that. If the world is not your market anymore. And that may be true for a lot of different car models and a lot of different products where I don't have, you know the underlying, accounting and balance sheet information to figure it out. But I think that that's what we will see, and that's where the adjustment will happen is we'll just be in a

different world from the perspective of the consumer. And the consumer in many cases is other us businesses that buy things from each other.

Archie Hall: That makes sense cool. I think we're getting towards the end of our time. But just to wrap up. I wanted to give both Dave and Steve a chance. If you do have any final thoughts, to share this with U.S.

Steven Kamin: Well, I made my pitch for a merely bad as opposed to a terrible scenario. but I'm not going to push it any further.

Archie Hall: Fair enough.

David E. Weinstein: I do think that there's going to be a realignment that's happening. I think we're. It's very hard again to kind of forecast the future, because we're seeing the end of a neoliberal order. That which was what I had grown up with and we're seeing the rise of something new. That's a lot more transactional, and I'm not sure where this is where this is going. But you know the others, you know. The other thing that you can also see is, if you look at equity markets, you know they haven't.

You know they've declined some, but it's not. It's not the Great Depression, or something like this. And so, you do want to. You want to take these predictions with a grain of salt. But you know that said there's been a there's been a fairly big decline, and I think it reflects that the uncertainty and the uncertainty of what the what the future is going to look like.

Archie Hall: Alright. I'll hand it back to you, Damjan.

Damjan Pfajfar: I would like to thank you all the panelists and Moderator Archie, for a very nice discussion today, and I would also like to emphasize that the views expressed during this program are those of the panelists, and not necessarily those of the Federal Reserve system. So, thank you very much. And looking forward to the next edition of the Conversation of Central Banking. Thank you.