Trump 2.0: A nightmare for macroeconomic policymakers

Trump 2.0 is proving to be more disruptive for the world than his first innings

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President Trump remains steadfast in his mission to compel countries with substantial trade surpluses with the US to increase their imports of American goods

Highlights

- *US President Trump's chaotic and abrupt policies and executive orders have disrupted the global economy*
- *Trump's tariffs pose immediate challenges to businesses within the US and other countries*
- *DOGE's efforts to reduce government spending and increase efficiency involved firing many workers*
- *Layoffs could crimp consumer spending in the US, posing risks to growth*
- *Investors across the globe would have to deal with heightened uncertainties for many months to come*

The return of Trump 2.0 has ushered in a whirlwind of executive orders and announcements, leaving the world grappling to understand their wide-ranging effects on the global economy. The impact of these policies varies greatly, with some yielding positive outcomes, while others bring about significant challenges. The sheer volume and complexity of these changes make it nearly impossible to determine the overall net effect.

The turbulence created by Trump's unpredictable and chaotic decisions has led to widespread concern regarding economic impacts and macroeconomic policy reactions of national governments. As a result, investment spending, particularly within the private sector, is likely to face disruptions in the short term. Such disruptions pose a substantial risk to global growth and development, as investors and businesses navigate an environment of heightened uncertainty. Until the dust settles on Trump's announcements, the world must brace for potential economic turbulence and its far-reaching consequences.

The biggest concern on everyone's mind stems from President Trump's announcement of tariffs. These include general tariffs on steel and aluminum as well as unilateral tariffs on China, Mexico and Canada (which were paused soon after). There is furthermore an air of uncertainty around whether Trump might use tariffs in response to non-tariff barriers and national value-added taxes, affecting many countries, including the EU.

Additionally, reciprocal tariffs on countries like India could have significant repercussions on Indian exports and, consequently, fresh investments in crucial industries such as pharmaceuticals, textiles, electronic and auto components. If India reduces tariffs on US goods, Indian manufacturers could face increased competition, given the current state of aggregate consumption spending, which may lead to a slump in new investments. As a start, India cut import duty on US bourbon whiskies from 150% to 100%. The Confederation of Indian Alcoholic Beverage Companies (CIABC) is already concerned and has asked the government to reduce import duty cuts in a phased manner as well as withdraw excise duty concessions given to foreign liquors by state governments.

However, these are just the first-order effects of heightened tariffs. The imposition of tariffs and possible retaliation, particularly from China, could trigger inflationary pressures in the US. In response, the Federal Reserve might want to raise interest rates to curb inflation. This could exacerbate tensions between the Fed and Trump, putting a question mark over the future of central bank independence and monetary policy in the US. All this raises the uncertainty in countries like India whether interest rates hikes will be required and if so, the impact on their currencies and the possibility of imported inflation.

Former President Donald Trump remains steadfast in his mission to compel countries with substantial trade surpluses with the US to increase their imports of American goods. This was notably evident when India agreed to purchase more oil and gas from the US in an effort to reduce the trade deficit. Trump has also utilized tariffs as a strategy to attract foreign investment to the US, exemplified by Taiwan's immediate commitment to invest more in the US semiconductor industry, and Japan's promise to boost investments in the US to the tune of a trillion dollars.

However, investing in the US under Trump's policies presents uncertainties for global companies. What if tariffs are lowered or withdrawn, as was witnessed in 2019 during Trump's first term? Furthermore, tariffs coupled with the elimination of US trade deficits, foreign investments in the US and threatening countries, especially those in the BRICS group, from seeking alternatives to the US dollar will cumulatively result in a scarcity of global dollar liquidity that will cause the US dollar to appreciate significantly, while other currencies depreciate. Ultimately, this movement in exchange rates would neither encourage US exports nor be conducive for foreign direct investment flows into the US.

Meanwhile, the Department of Economic Efficiency (DOGE) has unleashed abrupt and ruthless spending cuts and layoffs. It began with USAID earlier this month, but last Thursday the Trump administration announced that probationary workers who have been on the job for less than a year "were being dismissed and then instructed to leave the building within a half-hour." This notice could apply to more than 200,000 probationary workers! Keynesian economics 101 articulates that this would have a recessionary impact from an immediate decline in aggregate spending. And all this is perhaps only the beginning with such spending cuts being expected in various departments from education to defense to Green New Deal projects.

On the fiscal front, there are indications of massive tax cuts to the tune of some $4.5 trillion along with spending cuts of $2 trillion. The debt ceiling would be raised by another $4 trillion from its present level of $36 trillion to accommodate these changes. Whether the tax cuts can be successful in spurring US economic growth to nullify the deflationary impact of the spending cuts is another question mark.

Trump's "drill baby drill" reverie has been given a push through the creation of the National Energy Dominance Council this week. Its mandate includes boosting production and consumption of oil and gas both within the US and "to sell more oil and gas to allies in Europe and around the globe." This could not only ease global oil prices but also enable India to bridge the trade deficit gap with the US through more imports. However, the oil market has complex geopolitical repercussions across the world, and how Trump's initiative plays out over the next few years remains uncertain at this point of time.

Amidst these economic uncertainties, the world must also grapple with the New Order that Trump seems bent on creating. The future of NATO, forcing European nations to increase defense spending, and the open support to the far-right in Europe and their anti-immigrant stance could even lead to the disintegration of the EU. The ramifications of these changes on the rest of the world are perhaps too early to comprehend but cannot be ignored.

Although uncertainty has long posed a significant challenge for economists, the present era of disruptive changes, unpredictable events, and intricate interdependencies necessitates them to now confront chaos.

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