Registered Investment Advisor Firm

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Tariffs/ Trade Wars

The recent trade war carries a major risk of escalation that could weaken investments, depress spending, unsettle financial markets and slow the global economy. These initial tariffs are unlikely to inflict serious harm to the world's two biggest economies.

A tariff is a tax on goods coming into a country. In the US, many tariffs are paid at the time of entry into the US via customs brokers or agents. The idea of the tariff is to push up the price of foreign goods to make US goods more attractive.

For many businesses that use imported products, the cost to produce their items will increase, either because the company must use more expensive domestic parts or pay more for the finished product. The recent round of escalation is particularly damaging because they focus on intermediary goods, or parts. US firms, including many small- to medium-sized businesses, use the parts to make finished products. By increasing the cost of parts, the tariffs will force companies to either pass on the cost to customers in the form of higher prices, cut costs in other areas like the workforce, or shift operations outside of the US to avoid the tariffs.

Businesses that see the cost of goods rise have three options to make up the losses: cut costs in other areas; simply absorb the cost and accept lower profit margin or pass the cost onto the consumer.

The latter option could lead to a slowdown in consumer spending and an uptick in inflation.

Many firms would not and could not accept lower profit margins.

The increasing costs of inputs would raise the prices paid by consumers and the income paid to those consumers wouldn't stretch as far.

Escalating tariffs are likely to slow business investment as companies wait to see whether the parties can reach a truce. Some employers will probably put hiring on hold until the picture becomes clearer. The damage could risk undoing some of the economic benefit of last year's tax cuts.

Trade disruption is the greatest threat to global growth. The direct effect will be amplified as business confidence drops and investment decisions are delayed.

Economists expect the current round of tariffs to result in a modest drag on the US GDP growth. Markets are still hoping that the key players return to the negotiating table.

If all parties are able to negotiate a common ground to low- to-no tariffs, benefits of free trade could be achieved:
- Free trade enables countries to specialize in those goods where they have a comparative advantage.
- Trade creation occurs when consumption switches from high-cost to low-cost producers.
- Lower tariffs on exports will enable a higher quantity of exports boosting jobs and economic growth.
- The benefit of the economies of scale will ultimately lead to lower prices for consumers and greater efficiency for exporting firms.
- With more trade, domestic firms will face more competition from abroad, incentivizing to cut costs and increase efficiency.
- World trade is a significant contributor to economic growth.
- Surplus raw material is utilized more efficiently.
- With economic growth comes a rising stock market.

Lets' hope they all can reach an agreement.

If you need help or more information on this or any other financial matters, contact Bob Davis at (707) 648-2024.

FED Watch

The next Fed meeting should produce no action. Currently, the September meeting has a 91% probability for rates to rise and a 62% probability of the December meeting being another rate increase. The Fed will also continue the process of reversing quantitative easing by allowing assets to mature off their balance sheets, rather than re-investing them. They expect to be at $50 Billion quarterly by October 2018.

Next meetings:
July 31st and August 1st
September 25th and 26th

Castle Rock Wealth Management

Castle Rock Wealth Management is a Hybrid Advisory firm servicing the needs of clients across the United States.

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If you have questions or would like further information on this month's topics or any other financial or investment related subjects, including Social Security claiming strategies, please contact me by phone or through my email address at:
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