FINANCIAL MARKETS

TRADE TENSIONS & THE MARKETS

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Founded in 2010, we now have global presence in over 90 countries, with main offices in the separately regulated markets of Australia, Cyprus, New Zealand and the United Kingdom.

We believe that sound investment and trading decisions begin with a strong grounding in financial education. Our goal is to make this available to everyone - and this free eBook is part of that commitment.

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ESCALATING TRADE TENSIONS

FOREWORD

Global trade tensions are dominating the financial markets. In recent weeks, these tensions have escalated beyond the US and China.

So what's behind the rise of protectionist trade - and can it really be described as a full-blown trade war?

In this eBook, we'll analyse what's behind current trade tensions and compare it with other periods in history.

With this understanding, we'll explore what today's situation could mean for the financial markets.

Patrick Latchford
CEO, Blackwell Global Investments (UK) Limited

CHANGING GLOBAL TRADE

EXPLORING TRADE TENSIONS

Those monitoring the financial markets will have noticed the phrase 'trade war' in the media.

It's with good reason. The world looks set to enter a new period of protectionist trade. Understandably, this is making many investors anxious.

But what is a trade war - and is it something to worry about?

Well, it's quite simple - it's when two or more countries aggress each other's trade. This is generally done by introducing tariffs and quotas on certain industry imports.

Tariffs are taxes on imported products from other countries. When one country introduces or raises tariffs, the others involved will respond with tariffs of their own. These steps become cyclical, where countries look to protect domestic businesses and consumers.

If tariffs are in introduced, imported products generally become more expensive - so people are less likely to purchase them. This can encourage people to buy domestic products for cheaper, which can help economic growth and job creation.

At the same time, tariffs can cause serious harm to a nation's economy by disrupting international supply chains. They can also build political tension internationally.

Remember - trade tariffs are often justified as a means of protecting domestic manufacturing and jobs. However, this is a fine balance. Retaliatory tariffs from other countries can hurt domestic businesses that rely on exports.

ARE WE IN A TRADE WAR?

Experts are still debating whether or not we are officially in a 'trade war'.

Despite mixed opinions, what we can say is that global trade is changing. It's this change that has (and will continue to) cause volatility in the markets.

So how did this change come about?

In short, it all starts with US trade policy. During the presidential campaign, US President Donald Trump promised to renegotiate trade deals that he saw as unfair to US businesses and workers.

So far, he's largely kept his promise.

First of all, he pulled out of the Trans-Pacific Partnership (a trade agreement signed by Barack Obama) in January 2018.

Next, there were (long-held) suspicions that China was stealing American Intellectual Property Rights, so President Trump ordered an investigation.

By March 2018, President Trump announced that the US would impose 25% steel import tariffs and 10% aluminium import tariffs on all countries.

More recently, President Trump threatened China with an extra $200 billion worth of new import tariffs. Although tensions seemed to cool in May 2018, further tariffs since then have stoked further 'trade war' fears.

Keep in mind that these tariffs have been introduced to encourage US manufacturing and job creation. A good example is the US steel industry. By making foreign steel more expensive, the US hopes that domestic steel will see an increase in demand.

The US also wants to reduce its trade deficit. A deficit indicates that a country imports more than it exports in monetary terms. However, there is a reason the US has a trade deficit - and it's to do with its rate of economic growth and consumption. In simple terms, the US needs to import products to meet domestic demand. The US deficit is an indicator of the US economy's strength.

Trade tensions between the US and China are nothing new. But disagreements between the US, European Union, Canada and Mexico certainly are.

US import tariffs on steel and aluminium have angered traditional trading partners. In response, these countries have introduced retaliatory import tariffs on selected US products.

For instance, the European Union has imposed import tariffs on US jeans, motorbikes and bourbon whiskey. This equates to $2.8 billion worth of US products.

The EU has also said that they will consider an extra €3.6 billion worth of import tariffs if US trade policy does not change.

Canada has also decided to impose import tariffs on the US. These are equal to $12.5 billion worth of retaliatory tariffs on American exports. As well as this, Mexico has decided to respond by adding sanctions to US products including steel, pork and bourbon whisky.

It is because of these retaliations that some commentators believe the world is gripped in a trade war.

SHOULD INVESTORS WORRY?

HOW THE MARKETS HAVE REACTED

The markets aren't responding well to the ongoing trade tensions.

On the Tuesday following President Trump's threat of $200 billion worth of new tariffs on China, there was a noticeable market reaction.

First, we saw the Dow drop by 400 points. It ended up closing 237 points down. This wiped the entire year's gains in just one day. Furthermore, it continued to drop for days following the announcement.

Some of the worst affected companies were US exporters. This included Boeing, which dropped 3%, Caterpillar (a construction and mining company) which lost 2.7% and major tech company, Apple, which fell by 1.5%.

Chinese stocks also saw a significant fall. It was their biggest drop since the trade tensions began. We saw the Shanghai Composite Index drop 3.8% - reaching the lowest point in two years. The Yuan also took a tumble, falling to its lowest level against the US dollar in five months.

Europe wasn't left out either. The FTSE closed 0.4% lower, while France's CAC was down 1.1%. The DAX also slacked by 1.2%.

After significant growth in recent months, oil prices took a dip following the news. Investors fear that a trade war could damage economic growth, causing a fall in demand for oil.

Our advice to traders is to watch for further retaliatory tariffs from Europe, China, Canada and Mexico. These are likely to cause volatility in the markets - and could cause downward pressure on US stocks and the US dollar.


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We offer access to multiple asset classes including more than 60 currency pairs, precious metals and other contracts for differences. As a global broker, we are always striving to achieve excellence in our customer service, as well as developing innovative technology to support our customers needs.

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