

## Trump tariffs threaten world economy

US economy not immune from financial meltdown

by Desmond Lachman in Washington

Wed 12 Jun 2019

In the run-up to the 2018 mid-term Congressional election, US President Donald Trump made the crucial mistake of not making the strong US economy the central theme of that campaign. That cost him Republican-control of the House of Representatives.

Ahead of the 2020 ballot, he seems to be making the opposite mistake. He is putting the US economy at the forefront of his re-election campaign at a time when the world economy is beset by an unusual constellation of risks in systemically important economies. That could very well cost him his presidency if any of those risks were to materialise before November 2020.

Among the more immediate threats to the global economy is one of Trump's making. His hard-line stance on the China trade issue could lead to a slowing in the world's second largest economy. This is especially the case as China tries to rebalance its economy and wean it off excessive credit growth.

Any marked slowing in the Chinese economy is bound to have spillover effects on economies with which the country has strong trade links. It also could contribute to global financial market instability.

In Europe, any stumbling of the German and UK economies could trigger another, more dangerous round of the European sovereign debt crisis. The Italian economy, which is 10 times the size of the Greek economy, is already in recession. It is struggling with high public debt and has a weak banking system. It hardly provides comfort to think that Italy now has a populist government that would have difficulty in dealing with a real economic crisis, or that Italy might be too large an economy to be bailed out by Europe.

The risks to the global economy are not limited to China and western Europe. The Argentine, Turkish, and Venezuelan economies are all in the grips of accelerating currency crises. The new Brazilian government is showing increasing signs of being unable or unwilling to address the country's serious public finance problem. Also casting a dark cloud over the global economy are the rising geopolitical risks from countries like Iran and North Korea.

Seemingly oblivious to the lessons from the collapse of Lehman Brothers during the 2008 financial crisis, Trump appears to think that the US economy is insulated from the rest of the world economy and is immune from a global financial market meltdown. This indifference is all the more difficult to understand considering that years of ultra-unorthodox monetary policy by the world's major central banks has created global asset price bubbles and led to the major mispricing of global credit risk.

James Carville famously said in reference to US elections, 'It's the economy, stupid.' Before crafting their electoral campaigns for the 2020 election, the presidential candidates might want to reflect on how rapidly economic conditions changed for the worse ahead of the 2008 election. They also might want to consider that the months between now and the November 2020 election is a long time for any of major global economic risks to be triggered.

These considerations might give them pause about premising their election campaigns on the presumption that today's strength in the US economy will persist into 2020.

Desmond Lachman is a Resident Fellow at the American Enterprise Institute. He was formerly a Deputy Director in the International Monetary Fund's Policy Development and Review Department and the Chief Emerging Market Economic Strategist at Salomon Smith Barney.