



Impeachment Could Be Both Bad News and Good News for Trade Policy

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We believe the impeachment inquiry could have an adverse impact on the ongoing U.S.–China trade conflict, but there may be a silver lining for NAFTA 2.0.

These are extraordinary times in Washington, D.C., in which President Donald Trump is only the fourth president in U.S. history to face an impeachment inquiry. Regardless of the outcome, the impeachment proceedings will likely dominate Washington for the foreseeable future. The common narrative in the financial markets is that impeachment will crowd out everything else and that nothing productive will get done in Washington, which will only reinforce the skittishness and uncertainty in markets. We think that assessment is more right than wrong, but we also note that there may be an underappreciated silver lining to the impeachment inquiry.

Clouded outlook for U.S.–China trade negotiations

First, the not so good: We believe impeachment could have an adverse impact on the ongoing U.S.–China trade conflict, the policy issue that has disproportionately weighed on financial markets over the past two years. PIMCO flagged trade policy as a likely source of uncertainty soon after President Trump's inauguration, reminding investors not to underestimate the president's long-standing belief that the U.S. has been shortchanged on trade with foreign countries – particularly China – for decades, not to mention his affinity for tariffs as a negotiating tool.

Fast-forward almost three years: The U.S. has already imposed tariffs on more than \$360 billion of imported Chinese goods, and the conflict could escalate after a scheduled tariff increase from 25% to 30% on \$250 billion of Chinese imports on October 15 and the possibility of a new round of tariffs on the remaining \$160 billion of goods scheduled for December 15.

There is some hope that the upcoming (13th) round of trade negotiations between the U.S. and China in Washington on October 10–11 could yield a breakthrough. While that is possible, we do not think it is likely, and in any event China is unlikely to offer significant concessions on the issues that are at the heart of the Section 301 investigation: forced technology transfer and the subsidization of national champion companies. We think the specter of impeachment and the perception of an embattled President Trump will make China even *more* reluctant to offer these structural concessions, thereby decreasing the chances of a substantive deal anytime soon, prolonging uncertainty, and risking escalation.

Possible silver lining: NAFTA 2.0 resolution

On a more positive note, we think the impeachment inquiry could actually help foster resolution of another trade issue that has plagued markets – the ratification of NAFTA's successor, the United States–Mexico–Canada Agreement (USMCA, also known as NAFTA 2.0). That is because House Speaker Nancy Pelosi and the so-called majority makers – the 31 Democrats who represent districts that voted for Trump in 2016 – want to show their constituents that they can indeed legislate. Specifically, even though most Democrats may support an impeachment inquiry – and may even vote for impeachment – they also want to be seen collaborating with the president to get important things done.

The future of the USMCA also depends on whether the ongoing negotiations between the Trump administration and Democrats continue to be constructive, as well as whether organized labor groups endorse the trade agreement. But we would argue that impeachment has changed the political calculus for Speaker Pelosi around the USMCA, and that there is now more pressure to bring the trade agreement up for a vote to demonstrate that Democrats, particularly centrist Democrats, can accomplish more than simply impeachment.

For the markets, this could be an important and welcome development since the ratification of the USMCA would effectively eliminate the chances that the president withdraws from the original NAFTA, thereby taking a large policy risk off the table. It could be a silver lining of impeachment.

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