

Michael P. Stritch, CFA, Chief Investment Officer, BMO Wealth Management - U.S.

Yung-Yu Ma, Ph.D, Chief Investment Strategist, BMO Wealth Management - U.S.

Thursday, March 8, 2018

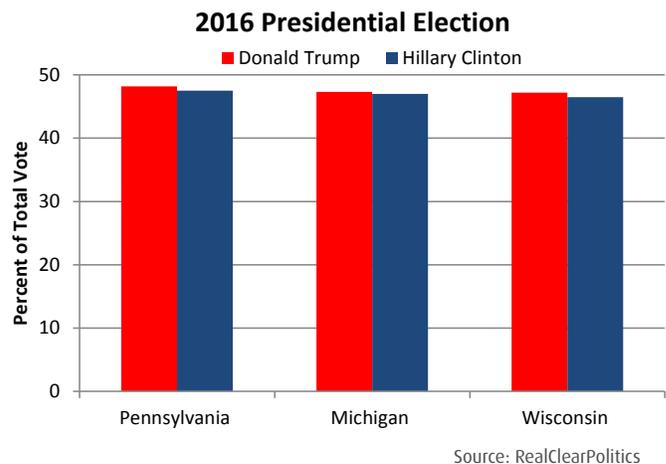
Trump & Tariffs: Odds favor skirmishes, not all out trade war

President Trump kicked off the month of March by announcing import tariffs of 10% on aluminum and 25% on steel. Trade policy, including ongoing NAFTA negotiations, is one of the key risks highlighted in our 2018 Outlook. The U.S. financial markets, as expected, reacted negatively to the initial announcement with the Dow Jones Index falling over 400 points and major aluminum and steel users such as Ford and GM being particularly hard hit. Canada and the EU, the two largest exporters of steel to the United States, came out strongly against the tariffs, with the EU proposing retaliatory actions on certain U.S. goods in response. Notably, the formal justification for the tariffs was “national security,” with President Trump taking to Twitter to proclaim, “If you don’t have steel, you don’t have a country.” We believe that the current developments are unlikely to lead to a trade war characterized by successive rounds of tit-for-tat measures that become increasingly hostile. Rather, in the near term, we expect trade frictions that are unwelcome, but not especially damaging to overall global markets. Nonetheless, there remains an element of uncertainty that could play out in different directions over time.

Our outlook is supported by a series of comments that emerged in the days following the initial release. In other words, the devil is in the details. President Trump indicated that Canada and Mexico will receive an exemption and that other potential carve outs could exist. Additionally, key Republicans such as Paul Ryan came out urging the president to make tariffs “more targeted,” and Commerce Secretary Wilbur Ross stated, “We’re not looking for a trade war. We’re going to have very sensible relations with our allies.” Treasury Secretary Steven Mnuchin added to the moderating voices stating, “We’re going to manage through this so it’s not detrimental.” Then, on March 7th,

President Trump tweeted, “China has been asked to develop a plan for the year of a One Billion Dollar reduction in their massive Trade Deficit with the United States. Our relationship with China has been a very good one.” Given an annual trade deficit with China of over \$300 billion, finding a way to shave off \$1 billion isn’t a particularly big ask. It’s barely a rounding error. Putting it all together, we believe a broad application of the steel and aluminum tariffs, accompanied by an exclusion and exemption process overseen by the Department of Commerce, will be considered a win-win by the administration. This allows President Trump to score a highly publicized victory in the rust belt, an area that significantly contributed to his 2016 election win (*see Exhibit #1*), while retaining an ability to refine the specific application over time to avoid dire economic consequences.

Exhibit 1: America first campaign won the day in three key states



For more insights and information, follow - [BMO Wealth Management - U.S. LinkedIn](#)

It's important not to be too complacent, however, about how trade frictions might develop. First, China is currently under a "Section 301" investigation for intellectual property infringement, and President Trump recently tweeted, "The U.S. is acting swiftly on Intellectual Property theft. We cannot allow this to happen as it has for many years!". Under Section 301 of America's Trade Act of 1974, the president can take unilateral measures such as tariffs, fines, M&A restrictions, import quotas, etc. Given that typical loss estimates from Chinese IP infringements reach into the hundreds of billions of dollars per year, this issue is certain to have bigger consequences for trade with China than imports of steel and aluminum. A second concern is that the EU has already indicated it will challenge the recent tariff justification of "national security" at the WTO. If the WTO allows a low bar for national security tariff justifications, this has negative

implications for subsequent tariff actions by other countries. If the WTO, however, rules against the United States, then it's hard to imagine President Trump accepting such a ruling on U.S. national security from an international body. Either way, there's longer-term potential for weakening the fabric of international trade.

Finally, it's important to remember that handicapping the different scenarios is particularly challenging with the current administration. When being interviewed on March 4th, Commerce Secretary Wilbur Ross was Zen-like in his framing of the president's tariff announcement, "Whatever his final decision is, is what will happen. What he has said, he has said. If he says something different, it'll be something different. If he for some reason should change his mind, then it will change." And that's coming from the commerce secretary, who is presumably as close to the issue as anyone.

Disclosure

This report contains our opinion as of the date of the report. It is for general information purposes only and is not intended to predict or guarantee the future performance of any investment, investment manager, market sector, or the markets generally. We will not update this report or advise you if there is any change in this report or our opinion. The information, ratings, and opinions in this report are based on numerous sources believed to be reliable, such as investment managers, custodians, mutual fund companies, and third-party data and service providers. We do not represent or warrant that the report is accurate or complete.

To the extent this report contains information about specific companies or securities, including whether they are profitable or not, it is being provided as a means of illustrating the investment manager's investment thesis. The investment manager may or may not have invested in these securities at the time this report was prepared or is accessed by the reader. References to specific companies or securities are not a complete list of securities selected and not all securities selected in the referenced timeframe were profitable.

Other Bank of Montreal affiliates, and their agents and employees, may provide oral or written market commentary or trading strategies to clients that reflect opinions that are contrary to the opinions expressed in this report. These same persons and affiliates may make investment decisions that are inconsistent with the recommendations or views expressed in this report. We and our affiliates, directors, officers, employees and members of their households, will from time to time have long or short positions in, act as principal in, and buy or sell, the securities referred to in this report. We and our affiliates, directors, officers, employees and members of their households, may have positions in the securities mentioned that are inconsistent with the views expressed by this report.

This report is not intended to be a client-specific suitability analysis or recommendation, an offer to participate in any investment, a recommendation to buy, hold or sell securities, or a recommendation of any investment manager or investment strategy. Do not use this report as the sole basis for your investment decisions. Do not select an asset class, investment product, or investment manager based on performance alone. Consider all relevant information, including your existing portfolio, investment objectives, risk tolerance, liquidity needs and investment time horizon.

Any forward-looking statements in this report involve known and unknown risks, uncertainties and other factors that may cause the actual performance of future markets to differ materially from the projections depicted in the report. Past performance is not indicative of future results and current performance may be higher or lower than that shown in the report. There can be no certainty as to the extent or depth of any market downturn, nor any assurance regarding the nature, extent or timing of markets rebounding. When evaluating the report, you are cautioned not to place undue reliance on these forward-looking statements, which reflect judgments only as of the date of the report. Investment returns fluctuate, and investments when redeemed, may be worth more or less than the original investment.

Standardized performance returns include reinvestment of dividends, other income and capital gains, which depict performance without adjusting for the effects of taxation or the timing of purchases and sales. Performance data is presented without deducting the investment advisory fees and other charges that may be applicable. The deduction of such fees and other charges (and the compounding effect thereof over time) will reduce portfolio return. Unless otherwise indicated, traditional investment performance data generally represents a composite or representative portfolio return and is shown gross of the investment manager's advisory fees. Unless otherwise indicated, alternative investment performance data is shown as net of fund

expenses, management fees, and incentive fees. Index performance data is shown as total return. You cannot invest directly in an index. Due to a system conversion, the ability to manipulate or restate client specific performance data prior to December 31, 2007, may be limited.

Any discussions of specific securities, investment managers, or strategies are for informational purposes only and should not be considered investment advice. The report does not constitute an offer to sell or a solicitation to buy any security or investment product. Any offer to sell or solicitation to buy an interest in any private security, investment product or fund may only be made by receiving a confidential private offering memorandum, prospectus, investment advisory agreement or similar documents from the investment manager, which describes the material terms and various considerations and risks relating to such security, investment product or fund.

Alternative investments, such as private equity and hedge funds, contain risks that are amplified when compared with other asset classes, such as illiquidity, stock or sector concentration, financial leverage, difficulties in valuation, and short selling. Alternative investment vehicles have minimal regulatory oversight and alternative managers have the latitude to employ numerous investment strategies with varying degrees of risk.

We are not licensed or registered with any financial services regulatory authority outside of the United States. Non-U.S. residents who maintain U.S.-based financial services accounts with us may not be afforded certain protections conferred by legislation and regulations in their country of residence with respect to any investments, investment solicitations, investment transactions or communications made with us.

You may not copy this report or distribute or disclose the information contained in the report to any third party, except with our express written consent or as required by law or any regulatory authority.

BMO Wealth Management is a brand name that refers to BMO Harris Bank N.A. and certain of its affiliates that provide certain investment, investment advisory, trust, banking, securities, insurance and brokerage products and services. Not all products and services are offered in every state and/or location. Capital Advisory Services are offered by a division of BMO Harris Bank, N.A. Member FDIC.



NMLS #401052

CFA® and Chartered Financial Analyst® are registered trademarks owned by CFA Institute.

Securities, investment advisory services and insurance products are offered through BMO Harris Financial Advisors, Inc. Member FINRA/SIPC. SEC-registered investment adviser. BMO Harris Financial Advisors, Inc. and BMO Harris Bank N.A. are affiliated companies. Securities and insurance products offered are: **NOT FDIC INSURED - NOT BANK GUARANTEED - NOT A DEPOSIT - MAY LOSE VALUE.**

Not all products and services are available in every state or location or through all entities within BMO Wealth Management or CTC | myCFO. Securities, investment, and insurance products offered are: **NOT A DEPOSIT - NOT INSURED BY THE FDIC OR ANY FEDERAL GOVERNMENT AGENCY - NOT GUARANTEED BY ANY BANK - MAY LOSE VALUE.**