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Market View
A tariff-induced market shock

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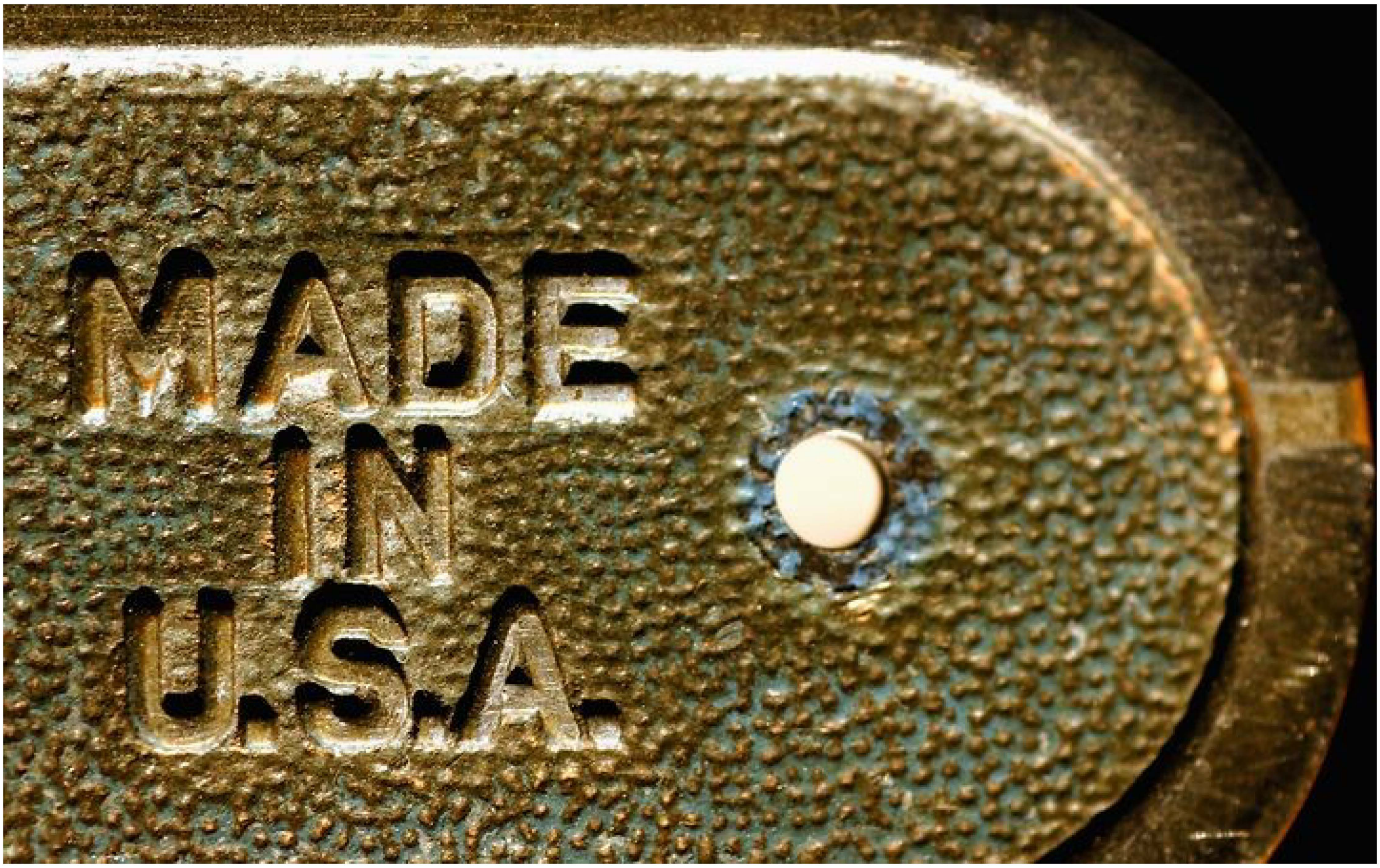

At a glance

- Despite an initial boost to the US economy following Trump's re-election, the array of tariff announcements has led to market volatility.
- Previous US presidents have employed tariff policies to raise funds externally, to mitigate costs for US citizens, with mixed results.
- The reshoring of US industries and supply chains is forecast to dampen growth.

The early equity market euphoria following Donald Trump's election win has faded. It has been a volatile week for stocks, with the Nasdaq losing 4% on 10 March, the sharpest decline since September 2022.[1] Investors are becoming increasingly concerned that waning consumer and business confidence combined with tariff uncertainty could pare back growth in the United States, shifting the country towards a more stagflationary backdrop or even a recession. All the post-election gains in equity markets have been erased. As of 13 March, the S&P 500 entered technical correction territory, with the index down over 10% from its peak last month.

This begs the question: what is Trump's end goal with tariffs? To recap on recent developments, Trump imposed 25% tariffs on steel and aluminium this week, hitting every country that sells steel and aluminium to the US.[2] Subsequently, on 13 March, the European Union and Canada announced billions of dollars in retaliatory tariffs on US exports, which economists say could dent economic growth and raise consumer prices—fuelling concerns of an emerging global trade war.[3] This tit-for-tat has only ratcheted up with Trump threatening 200% tariffs on European alcohol, indicating he will not back down from the escalating trade war.

One has to go back almost a century to find comparable tariff increases. This week, we take a closer look at how tariffs have been used in the past in the US and what could possibly be prompting Trump to keep hitting some of the US's closest allies with tariffs.

History of US tariffs

Following World War I, the US economy was booming, and there was a push for protectionist policies. This led to the introduction of the Fordney-McCumber Tariff of 1922, a key piece of legislation that raised rates on many imported goods to provide protection for American industries and agriculture. It increased the average duty rate to about 38.5%, much higher than previous tariffs.[4] During this time, the federal government relied on tariffs as the main source of revenue as there was no income tax collection.

The 1930s brought the Great Depression, when the US government implemented even more tariffs to protect jobs and stimulate economic recovery. The introduction of the Smoot-Hawley Tariff Act of 1930, often cited as one of the most significant tariff measures in US history, was intended to protect American jobs and industries, and raised duties on more than 20,000 imported products.[5] Although the impact was to shield the American economy from foreign competition, it resulted in retaliatory tariffs from other countries, reduced international trade and some historians argue worsened the global depression.[6]

The New Deal

Tariffs were the main source of revenue for the US government throughout the 19th and early 20th centuries. However, in 1913, the 16th Amendment was introduced which allowed Congress to collect income taxes as an additional source of revenue.[7] Tariffs remained the dominant source of revenue for the government throughout the 1920s and 1930s, but under President Franklin D. Roosevelt's New Deal era, there was a shift towards income taxation and a reduction of tariffs as the government's main source of revenue over subsequent decades.

The New Deal, a series of programs, public work projects, financial reforms and regulations, were designed to provide relief to the unemployed, recover the economy and reform the financial system to prevent further depressions. It was clear that relying on tariffs as the main source of revenue was not reliable, underscored by the Great Depression. The US had to find a more stable source of revenue. This led to income tax gaining in prominence, along with the introduction of payroll taxes, which provided a more stable and reliable revenue stream for the government. Several reciprocal trade agreements also helped reduce tariffs, allowing the president to negotiate trade agreements with other countries. This marked a shift towards a global trade policy and increased international cooperation.

The end goal

In his Inaugural Address in January, Trump spoke admiringly of President William McKinley, who pushed for large tariffs in the 1890s.[8] He believes that rather than taxing Americans to enrich other countries, the US should impose tariffs and tax foreign countries to enrich Americans.[9]

Most economists agree however, that relying on tariffs as the main source of government revenue is unlikely to succeed. The world is more interconnected than ever before, and international trade has increased. For example, car parts often move a dozen times over the border with Canada before final installation in an American-produced vehicle. Reshoring all industry would likely dampen global economic growth, owing to loss of supply chain efficiencies, and the increased costs associated with relocating entire industries.

Economists and investors remain very divided on the endgame here and until there is clarity on the trajectory of Trump's upcoming second round of tariffs, markets will continue to view them as either a negotiation tool or a longer-term change in US tax policy that could ultimately bring material changes to the US economy. For investors, ongoing volatility is likely to remain a feature of the investment climate. This means focussing on businesses that are less sensitive to tariff threats and can still continue to compound earnings over time.

[1] Bloomberg

[2] New York Times: https://www.nytimes.com/2025/03/12/us/politics/trump-tariffs-steel-aluminum.html

[3] New York Times: https://www.nytimes.com/live/2025/03/12/business/trump-tariffs-steel-aluminum

[4] Economic History Association: https://eh.net/encyclopedia/the-fordney-mccumber-tariff-of-1922/

[5] Corporate Finance Institute: https://corporatefinanceinstitute.com/resources/economics/smoot-hawley-tariff-act/

[6] Corporate Finance Institute: https://corporatefinanceinstitute.com/resources/economics/smoot-hawley-tariff-act/

[7] Ronald Reagan Library: https://www.reaganlibrary.gov/constitutional-amendments-amendment-16-income-taxes

[8] White House: https://www.whitehouse.gov/remarks/2025/01/the-inaugural-address/

[9] New York Times: https://www.nytimes.com/2025/03/13/us/politics/trump-manufacturing-economy-risk.html?smid=nytcore-ios-share&referringSource=articleShare