“Trumponomics” and Implications For the Korean Economy

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Overview of Today’s Remarks

1. Where is the U.S. economy now?

2. Trump’s surprise victory brought an uncertain policy environment and high risk of counter-productive trade and immigration policies.

3. Yet the U.S. economic outlook appears to have improved in the wake of the election. Why?
   • Several reasons, but I will focus on regulation.


5. How might South Korean policymakers respond?
Where Is the U.S. Economy Now?

1. Steady strengthening in labor markets since mid 2009. U.S. economy is at or near a cyclical notion of full employment.
2. Rising wage inflation since 2015. PCE inflation rate is now near the Fed’s “target” of 2 percent per year.
4. An unusually uncertain policy environment.
5. High risk of counter-productive trade and immigration policies.
6. Despite 5 and 6, Trump’s surprise election victory has improved the outlook for U.S. economic growth.
U.S. Labor Market Tightness, Five Quantity-Based Measures

January 2001 to December 2016

- Vacancy Duration (left axis)
- Rescaled quits rate
- V-U Ratio
- Vacancies to Short Term Unemployment
- Non-Employed+PTER, Rescaled

Short Term Unemployment is the number of persons unemployed for 26 weeks or less. The Quit Rate is rescaled to have the same mean and variance as the Vacancy-Unemployment Ratio from January 2001 to date. Non-Employment + PTER, an index developed by Hornstein, Kudlyak and Lange, reflects all persons who are not employed (weighted by labor force attachment) plus persons who are working part time for economic reasons and would prefer to work full time. Here, their index is multiplied by minus one and then rescaled to have the same standard deviation as the Vacancy-Unemployment Ratio.

Source: [http://dhihiringindicators.com](http://dhihiringindicators.com)
Recent wage gains are not limited to highly skilled workers. For example, average hourly earnings grew 4.2% in the leisure and hospitality sector for the 12 months ending in February 2017.

Newspaper-Based Policy Uncertainty Indices

- Get monthly counts of articles in domestic newspapers that contain at least one term in each of the E, P, U and C term sets. For the U.S., for example:
  
  **E:** \{economic or economy\}
  
  **P:** \{regulation or deficit or “federal reserve” or congress or legislation or “white house”\}
  
  **U:** \{uncertain or uncertainty\}
  
  **C:** \{category-specific terms\} (No C term set for overall economic policy uncertainty (EPU) index)
    
    Include “the Fed”, “regulatory” and other variants.

- Scale the raw newspaper-level EPUC counts by the count of all articles in the same newspaper and month.
- Average the scaled counts over papers by month to get EPUC index.
- Multiplicatively normalize EPUC index to a mean of 100 for the base period.
- See Baker, Bloom & Davis (Quarterly J. of Economics, 2016) for more information.
U.S. Monthly Economic Policy Uncertainty Index, January 1985 to February 2017

Revised U.S. Policy Outlook after November 2016 Elections

Favorable Shifts

1. Better prospects for business tax reform and rate cuts → improving the near-term and long-term macro outlook
2. New fiscal stimulus (tax cuts + more infrastructure spending) → improving the near-term macro outlook but intensifying concerns about the longer term U.S. fiscal stance.
3. New restraints on, and some rollback of, anti-business and anti-growth regulations → improving the near-term and long-term macro outlook.

More on regulation below.
Revised U.S. Policy Outlook after November 2016 Elections

Unfavorable and Worrisome Shifts

1. A wrong-headed shift toward mercantilist rhetoric and trade policies that inhibit supply chains, raise production costs and increase prices for consumers in a largely vain effort to protect U.S. jobs and wages.
   b. Much worse outcome: major new trade barriers, disruption of trade treaties and WTO, trade war → large negative effects on U.S. and global growth.

2. Immigration: Trump has softened rhetoric and plans, but there is a legacy of fear and ill will that may deter many desirable immigrants.

3. Ad hoc interference in business decision making (e.g., the Carrier episode) to advance Trump’s political agenda and burnish his populist and nationalist credentials.

More on trade policy below.
Remarks on the U.S. Regulatory System

1. The U.S. regulatory system grew enormously in scale, scope and complexity in recent decades.

2. Regulation and other government policy matters account for a growing share of business risks.

3. Trump’s election (and Republican control of the House & Senate) greatly increase the prospects for regulatory restraint and reform, with positive consequences for GDP growth.


Regulation as a Source of Business Risks: Using 10-K Filings to Quantify Its Importance

• Since 2006 (for FY 2005) the SEC has required most publicly held firms to include a separate discussion of “Risk Factors” in Part 1a of their annual 10-K filings.

• In explaining “How to Read a 10-K” at www.sec.gov/answers/reada10k.htm, the SEC describes Part 1a as follows:
  – **Item 1A - “Risk Factors”** includes information about the most significant risks that apply to the company or to its securities. Companies generally list the risk factors in order of their importance. In practice, this section focuses on the risks themselves, not how the company addresses those risks. Some risks may be true for the entire economy, some may apply only to the company’s industry sector or geographic region, and some may be unique to the company.

• **Quantification**: (a) Calculate the *share* of sentences in Part 1a of each 10-K filing that contains one or more regulation-related terms. (b) Compute the cross-firm average of this share by filing year. Plot the resulting time series.
Regulation and Other Government Policy Matters Account for a Growing Share of Business Risks, According to 10-K Filings

Note: In addition to regulatory matters, “All Government Policy Risks” include those related to fiscal policy, monetary policy, entitlement and welfare programs, trade policy and more.
Methodology:

1. Using the “Risk Factors” discussion in Section 1A of 10-K filings, calculate each firm’s loading on regulatory risks. For this exercises, set loading to share of sentences in Section 1A that contain “regulation” or “regulatory”.

2. Regress firm-level stock returns from November 8 (election day) to November 9 on a constant and the firm-level loading on regulatory risks. The regression sample has about 5,000 firm-level observations.

3. Use the regression results to estimate the differential stock return response between the 75th and 25th percentiles of the firm-level loadings on regulatory risks.
The implied post-election one-day return differential between the 75\textsuperscript{th} and 25\textsuperscript{th} percentiles is 112 basis points. According to prediction markets, Trump’s pre-election victory chances were about 22%.

Early Signs of Regulatory Rollback under Trump

Congressional Action

Using the Congressional Review Act, Republican lawmakers have moved to roll back dozens of federal regulations with 37 separate resolutions since Trump took office. That's more than any previous Congress attempted in an entire two-year term.

Trump Administration Moves and Rhetoric

1. Approval of Dakota pipeline permits
2. Suspension of DOL’s new fiduciary standards for financial advisors
3. February 3 Executive Order calling for more rigorous regulatory impact analyses.
4. Plan to eliminate 2 old regulations for each new one (bit of a gimmick, in my view)
5. Possible scaling back of Dodd-Frank provisions related to:
   • Consumer Financial Protection Bureau
   • Volker Rule on banks’ proprietary trading
   • SIFIs
   • Swaps & clearing houses
   • Bank capital requirements??
   • Disclosure mandates for hedge funds and private equity groups
6. Talk of exit from Paris Climate Accords
7. New EPA head (Scott Pruitt) aims to greatly alter direction of energy and environmental regulations, with Trump’s backing.
The direction of U.S. trade policies remains highly uncertain

2. There’s a struggle in the Administration between those who want to focus on removing barriers to U.S. exports and U.S. business activity abroad, and those who also want to curtail U.S. imports.

3. Anti-China sentiment is prominent in the Trump Administration’s trade policy rhetoric. A danger of spillover to South Korea, which runs a large bilateral trade surplus with the United States.

4. There are huge concerns in South Korea and elsewhere about the direction of U.S. trade policy.

5. U.S. trade policy uncertainty is already harming growth prospects in the United States and around the world.
Donald Trump

White House civil war breaks out over trade

‘Fiery meeting’ in Oval Office between economic nationalists and pro-trade moderates

MARCH 11, 2017 by Shawn Donnan and Demetri Sevastopulo in Washington

A civil war has broken out within the White House over trade, leading to what one official called “a fiery meeting” in the Oval Office pitting economic nationalists close to Donald Trump against pro-trade moderates from Wall Street.
Expresses a preference for bilateral trade deals.

Promises strict enforcement of American trade laws

Promises to defend American sovereignty over trade policy

Stresses that a WTO ruling need not lead to a change in U.S. law or practice

Complains about weakness of WTO rules, with an eye toward China

Takes note of possible trade actions against China under Trade Act of 1974:

- Sections 201 allows tariffs to protect American producers from a surge of imports. Affected companies must show “serious injury” but need not prove unfair practices.
  - Injury claims must meet a high legal threshold of proof, as adjudicated by the U.S. International Trade Commission, an independent U.S. agency.

- Section 301 allows actions against “unfair” trade practices, a vague concept.
On the Possibilities for Spillover and Retaliation

Anti-China rhetoric and trade policy could spill over to U.S. relations with Japan, South Korea and Taiwan, all of which run current account surpluses with the United States.

U.S. policy actions against Chinese imports and Chinese firms could trigger many forms of retaliation, including (a) Chinese actions to raise burdens on U.S. firms that operate in or sell to China, (b) cancelling plane purchases from Boeing, and (c) cutting agricultural imports from the United States.

On both American and Chinese sides, the rise of global supply chains may restrain protectionist impulses. (Let us hope.) Trade in intermediates gives rise to concentrated commercial interests that benefit from pro-trade policies. These interests will agitate against protectionist policies that penalize import-using producers. See Gawande et al. (2014).
Trade Policy Uncertainty

• The anti-trade tenor of the U.S. presidential election campaign, Trump’s surprise victory and several of his and his administration’s post-election pronouncements raise great fears about the direction of U.S. trade policy, continued U.S. participation in NAFTA, and U.S. support for the WTO and other international institutions (e.g., NATO, and alliances with Japan and South Korea) that undergird the global economic and security order.

• In my judgement, these sources of uncertainty are already inhibiting investments in trade-creating activities, slowing the further development of global supply chains, and working against future trade and output growth. This judgment finds support in a growing body of empirical evidence that policy uncertainty discourages and delays investment and that trade policy uncertainty, in particular, inhibits investments in trade-creating activities. See, for example, Handley and Limao (2015), Baker, Bloom and Davis (2016), Crowley, Song and Meng (2016), Feng, Li and Swenson (2016), Gulen and Ion (2016), Liu and Ma (2016).
A Hopeful Possibility for U.S. Trade Policy

• That senior members of the Trump administration recognize that, while the U.S. has legitimate grievances vis-à-vis China, they have little to do with currency manipulation and stealing jobs by selling goods at low prices. Instead, well-founded concerns relate to:

  1. Pressures on U.S. firms to relinquish technological know-how in exchange for operating or selling in China and, more generally, China’s practice of exploiting its large market to extract concessions from foreign firms.

  2. Hamstringing foreign firms in China in various ways. Examples: (a) Making it hard for Google to operate in China, benefiting Baidu; (b) blocking Twitter in China, benefiting Weibo; (c) banning Flickr, benefiting Bababian; (d) recent rule against internet publishing by foreign firms, forcing Apple to end sales of iBooks and iTunes movies in China; and (e) “Buy China” procurement practices of China’s SOEs.

  3. Weak efforts to deter theft of IP developed and owned by U.S. firms.
Notes: Index reflects scaled monthly counts of articles in six South Korean newspapers containing 'uncertain' or 'uncertainty', 'economic' or 'economy' or 'commerce', and one or more of the policy terms specified for South Korea in Appendix A of “Measuring Economic Policy Uncertainty” by Baker, Bloom and Davis. The series is normalized to mean 100 from 1995 to 2014.
Trade Policy Uncertainty Index for Japan, January 1987 to February 2017

Sources: Authors’ calculations.

US sanctions on Japanese semi-conductors
Deliberation on the Omnibus trade bill in the U.S. Congress
GATT Uruguay Round
Revival of the Super 301 provision of the Omnibus
Asian financial crisis
Conflict over TPP
PM Kan’s statement on TPP, Reshuffle of cabinet
Deliberation on "Buy American" provision in Congress
Uncertainty over TPP talks and ratification
Conflict over TPP talks and ratification
Brexit
US Presidential election

Global Economic Policy Uncertainty Index, January 1997 to February 2017

Using data for 18 countries that account for 2/3 of global GDP

Asian & Russian Financial Crises

9/11

Gulf War II

Global Financial Crisis

Global EPU, Current Prices GDP

Global EPU, PPP-Adjusted GDP

Notes: Global EPU calculated as the GDP-weighted average of monthly EPU index values for US, Canada, Brazil, Chile, UK, Germany, Italy, Spain, France, Netherlands, Russia, India, China, South Korea, Japan, Ireland, Sweden, and Australia, using GDP data from the IMF’s World Economic Outlook Database. National EPU index values are from www.PolicyUncertainty.com and Baker, Bloom and Davis (2016). Each national EPU Index is renormalized to a mean of 100 from 1997 to 2015 before calculating the
How Might South Korean Policymakers Respond?

• Recognize the gravity of the situation: South Korean political and policy uncertainty are at historically high levels for internal and external reasons. The global economic environment is also unusually uncertain and fraught with risks.

• There is great need to respect South Korean democratic institutions and chart a rapid return to political normalcy – including the reaffirmation of close economic and security ties with the U.S.

• South Korea’s new president should meet President Trump early on, hold joint press conference, remark on his brilliance, business acumen, political savvy, etc.

• Offer concessions that open South Korean markets to U.S. firms and U.S. goods and services.
  • Pick concessions that benefit South Korea’s economy by strengthening the supply chains of Korean firms and by providing lower prices and greater product selection for Korean consumers.
  • Attribute the concessions to Trump’s business savvy and negotiating skills.

• Highlight large Korean procurement contracts won by American firms.
  • Attribute the contract awards to Trump’s business savvy and negotiating skills.
End of Slides for Prepared Remarks
References


References


Liu, Qing and Hong Ma, 2016. “Trade Policy Uncertainty and Innovation: Firm-Level Evidence from China’s Accession to the WTO,” working paper, University of California, Davis.

In recent years, the CFR contains more than 1 million “commandments”: instances of “must”, “shall”, “may not”, “required” and “prohibited”. Commandments grow roughly in proportion to page counts.

Source: Author’s calculations, drawing on Dawson and Seater (2013) and Crews (2016).
Regulatory “Dark Matter”

*CFR* page counts **understate** the scale and growth of the regulatory state, because many important pronouncements by the regulators involve “guidance” rather than formal regulations.

As the D.C. Circuit Court observed in *Appalachian Power Co. v. EPA* (208 F.3d 1019 (D.C. Cir. 2000)):
“The phenomenon we see in this case is familiar. Congress passes a broadly worded statute. The agency follows with regulations containing broad language, open-ended phrases, ambiguous standards and the like. Then as years pass, the agency issues circulars or guidance or memoranda, explaining, interpreting, defining and often expanding the commands in regulations…. Several words in a regulation may spawn hundreds of pages of text as the agency offers more and more detail regarding what its regulations demand of regulated entities. Law is made, without notice and comment, without public participation, and without publication in the Federal Register or the Code of Federal Regulations.”

Trade Policy Instruments Available to President Trump

• Labelling China a currency manipulator – largely symbolic, but sets a hostile tone.
• Vigorous pursuit of anti-dumping complaints and alleged violations of trade agreements.
• Denying ”Market-Economy Status” to China 15 years after WTO accession.
• The President can withdraw from NAFTA (and other FTAs) on six month’s notice, raising tariffs on Mexican imports to MFN levels under the WTO.
• Under the Trade Act of 1974, the President can impose quotas or tariffs up to 15% for up to 150 days on imports across-the-board or against particular goods/countries.
• Under the Trade Expansion Act of 1962, the President can implement high targeted tariffs in certain industries, as Ronald Reagan did on steel imports.
• Trump threatens 45% tariffs on Chinese imports. He can levy such tariffs through executive action by declaring a “state of economic emergency” or that U.S. is in “a time of war”
• Trump wants a 35% tax on firms that fire American workers, build a factory in another country, and then seek to sell foreign-produced goods in the U.S. By my understanding, implementing this policy would require legislation.
• Even rhetoric along these lines and threats to raise tariffs chill the development of global supply chains and investments that promote trade.

See Hufbauer (2016) for a fuller discussion.