



## **Economic Resilience for Facing Trump Tariffs**

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As the Trump tariff saga unravels, policy-makers and economists are often reminded of the "Wolf and the Lamb" fable. A lamb was drinking water peacefully downstream, way up in the stream, and a wolf was watching it and thinking about dinner. Suddenly, the wolf accused the lamb of muddying the water he was drinking. The lamb said that it was not possible, as he was downstream. The hungry wolf replied, 'In that case, someone from your tribe must have done it.' With that excuse, he got ready to pounce on the lamb. In the current story, which till date has been bloodless, the show of fangs has been enough. Japan, EU and UK have more or less acquiesced, without much ado. After all, 20% of Japanese exports go to the USA, 21% of EU exports go to the USA, and for the UK, the corresponding figure is 13%. All these "advanced" economies have agreed to Trump tariffs, for the UK it is 10% and for the EU and Japan the rate is 15%. That does not complete the picture, in some items their own rates for imports from the US have to be brought down to a nil level. Further, they will have to buy energy and defence items, as the case may be, from USA and make investments in the USA. Smaller countries have more or less fallen in line, the question remains about the BRICS Countries, will Trump make lambs out of them?.

For Brazil and India, the rate is 50%, and for South Africa 30%. China is still negotiating; they have the advantage of possessing rare earth materials. Russia is out of the picture because of sanctions, etc.

Before we focus on India, it might be useful to understand the economic perspective. The first question that arises is how these Trump tariffs are going to serve American Macroeconomic interests as well as consumers and businesses.

When a country like the USA lives beyond its means, and has growing budget deficits, imports are bound to go up. In the next stage, it borrows from the rest of the world to finance consumption. It already has \$28 trillion in debt. On the other hand, this borrowing makes the dollar overvalued and dampens exports and keeps trade deficits high. Rolling in of tariffs cannot solve the problem. It is at best a 'sticking plaster' solution with political visibility. Further, erratic policies like sudden sanctions or tariffs can shake the faith in US Treasury bonds. Once that confidence becomes a question mark due to a trust deficit, it will be a different story altogether. This can even lead to an upheaval in the bond market. That is how it is going to play out in the long run. However, in the short run, dollars could roll in on account of higher tariffs provided exporters in other countries absorb at least a certain amount of additional cost. What are the emerging scenarios about GDP and jobs? Firstly, the Trump tariffs are on both inputs and outputs. Take the US automobile industry for example, not only would auto components sourced from vendors outside the USA be costlier, but so would steel and aluminium. These could create competitive disadvantages in export markets. At the same time, domestic prices would go up in the USA. So far as consumers are concerned, the price of food items, a significant part of which are imported, would go up. The items vulnerable to inflationary pressure are groceries, textiles, shoes and appliances. In many cases, where exporters are selling at marginal cost, they would try to diversify into other markets, or there would be a price pass-through to US consumers on account of higher tariffs. Lastly, when it comes to foreign investment in the USA, for buttressing higher growth in output and employment, which private sector company will invest substantially when the policy environment is unstable and uncertain?.

Given this overall scenario, it is apparent for India that one is not getting into a straightforward trade negotiation with the USA. After all the tenets of multilateral trade negotiations have been tossed out the window. Trade is now weaponised for foreign policy gains for the USA or scoring a point to the MAGA audience. Nor can we offer much for the transactional gains of the USA defence and energy sectors. Further, unlike China, we do not have the leverage of rare earth materials.

Fortunately, we are not an export-oriented economy; our exports to the USA are around 2% of GDP. Till date, about 1/3rd of it is covered by exemptions, e.g., pharma, electronics including smart phones, jet fuel and certain refinery products. So the impact will be on the other two-thirds in terms of growth and employment, which includes gems and jewellery, textiles, shoes and leather products, auto components, seafood, some engineering products and chemicals. A part of it can be mitigated by rerouting.

The overall GDP growth impact should not be more than 0.4% if other things remain unchanged. Firstly, Indian businesses have always been resilient, the option of diversifying to other markets like UAE, UK, EU and China are being explored, their shares can be increased from the present level, the same is true of the new FTAs. This may require Government support to certain export-oriented units. The scope of PLI can be expanded to include such units. Further internal reforms in terms of the cost of doing business and logistics costs would require necessary emphasis.

As Indian manufacturing prowess develops, particularly in areas requiring high-skill man-power, American firms too can take advantage of this. Apple has been one of the early birds. Our core strength lies in the availability of low-cost design and engineering skills.

Finally, the domestic demand needs to expand, including consumption and private investment demand, to protect against blips in the external sector. In other words, given our emerging economic resilience, we can continue with our economic policy and foreign policy autonomy.

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