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A new frontier of trade tensions as US turns attention to Europe

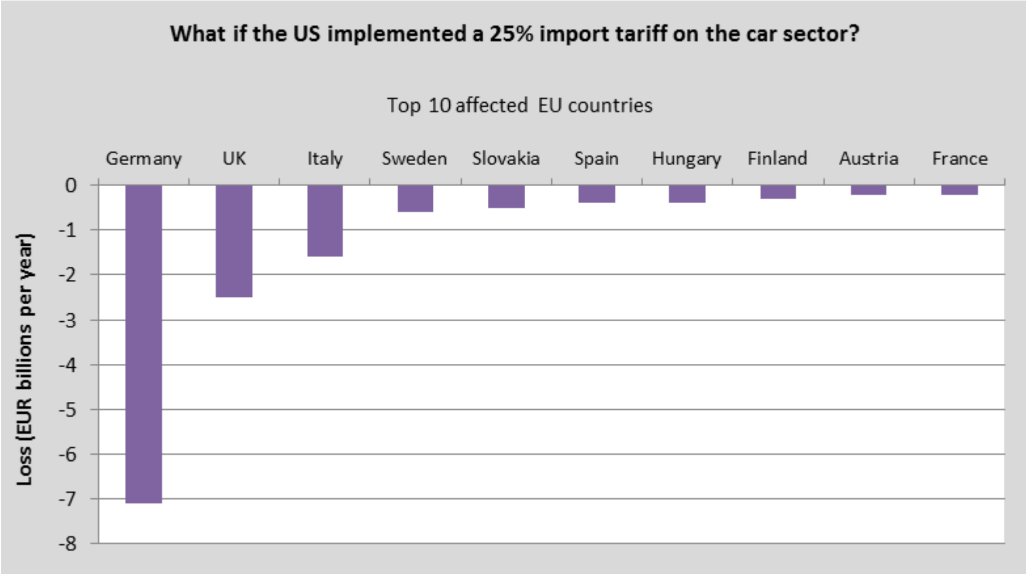
As

a trade deal between the US and China comes within striking distance, it doesn't look like the Trump administration is about to hang up its hat and call it a day with regard to its protectionist push. Rather, it seems to be saddling up to go into a fresh tussle, this time with the EU.

Tensions
flared up after a series of accidents spurred European aviation authorities to ground Boeing 737 Max aircrafts – which belong to the US firm's best-selling family of models. This breathed new life into dispute that's dragged on for more than a decade under WTO adjudication: Both sides accuse each other of offering domestic aircraft manufacturers (Airbus in Europe and Boeing in the US) illegal aid.

Following
a WTO ruling that found EU subsidies to Airbus have had an adverse impact on the US, the US has threatened tariffs on some $11Bn worth of EU goods. The product list (which will be finalized after the WTO arbiter evaluates the claims) covers mainly agricultural products:
salmon, lemons, an array of cheeses from Pecorino to Stilton, olive oil, Marsala wine... For now, the market reaction has been minimal and our equity analysts believe this is because such goods are mainly produced by private firms that don't trade on the stock exchange – farms, fisheries, dairies... There is also some reassurance in the fact that the US is going through the correct channels (the WTO). Last year, it attracted severe criticism following the way it rolled out steel tariffs – the EU Trade Commissioner Pascal Lamy was quoted as saying:
'*The world steel market is not the wild west, where people do as they like. There are rules to guarantee the multilateral system*.'

The EU has come out with retaliatory tariffs totaling over $22 billion on items such as plums, mangoes, planes, beeswax, tractors and car parts. Now, the danger is further escalation. The US-China spat began with trivial items like washing machines, but before long, the value of goods caught in the US' lasso was worth $250 billion, with $267 billion more threatened. The US is currently considering tariffs on auto imports - a move that could really imperil the EU economy, hitting Germany the hardest as the below chart shows. Germany's export-oriented economy is already feeling the fall-out from the US-China dispute which weighed on global trade.



Source: Chelem, World Bank, Euler Hermes, *BIL*

Over the longer term, the result may be that the US pushes the EU to forge stronger ties in the east. Already, Europe has formed the world's largest trading pact with Japan, covering roughly one-third of global GDP. As it stands, the EU is China's largest trading partner, and on April 9th, the two agreed to furthers strengthen their trade relationship and widen market access. Italy has become the first G7 nation to sign on to China's Belt and Road Initiative and last week Germany's telecoms regulator gave its clearest signal yet that Huawei will not be excluded from the buildout of 5G networks, despite pressure from the US.

In the shorter-term, a tariff standoff risks putting a dent in both business and investor confidence. And the problem with confidence is that all too often, it leaves on horseback and returns on foot…

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