

An unexpected cost

Many well-intentioned government policies have harmful unintended consequences. For instance, generally, when laws required people to wear seatbelts while driving, people felt safer in their cars and drove more recklessly. This reckless driving reduced, in part, some of the beneficial effects of the seat belts. When the federal government raised the income tax rate, many people realized that they got to keep less of their income, so they worked less. This decrease in hours worked reduced the extra money the government raised compared to what they would have raised had people continued to work the same number of hours. When the state government raised sales taxes, goods and services became more expensive, so many people bought fewer of them. This drop in consumption lowered the amount of extra revenue the government raised from the higher sales tax. In short, government policies change incentives, often in ways that politicians ignore. But people do not ignore the changing incentives, they alter their behavior.

In my last column, I spelled out the economic costs of tariffs. This is a hot topic now that Trump is threatening to impose so many of them. But the costs of tariffs that I laid out in that column are well

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known, at least by those who know a little bit of economics. To remind you, my argument was that tariffs increase prices and slow economic growth. But the way Trump is implementing tariffs places another cost on the economy. It is an unintended cost that is not obvious to most people – even to those who know some economics.

Trump is creating uncertainty. First, he imposed 25 percent tariffs on two of our closest allies (Canada and Mexico). Then soon after, he delayed when the tariffs would take effect by a month. At about the same time, Trump imposed 10 percent tariffs on China. At the time I write this, the Chinese tariffs are still in place. Will he delay their implementation like he did for the Mexican and Canadian tariffs? Nobody knows. This uncertainty is the unintended cost of the way he is implementing his tariffs. By using tariffs as a bargaining chip and by threatening to implement them and then sometimes backing off, businesses do not know what economic environment they are operating in.

A Michigan manufacturing plant that uses Canadian parts may want

to expand production if it believes Trump won't impose tariffs on imports from Canada. But if the firm believes Trump will impose tariffs on Canada, it might want to build a new plant in Vietnam. And if it has no idea what Trump will do on tariffs, then it will wait and do nothing until it has better information on what the U.S. tariff policy will be.

This is a general point. In the face of uncertainty, firms and people delay decisions until they get better information and much of the uncertainty has gone away. Look for Trump's constantly changing tariff policy to reduce the investments by firms in the U.S. This lower level of investment will hurt worker productivity. Workers won't have the most efficient equipment. They will continue using older, less efficient equipment. Trump's dithering will reduce economic growth in the U.S. This unintended cost of his bargaining strategy will make our nation poorer.

I would encourage Trump's advisers to help him develop clear predictable policies that encourage investment in the U.S. Reducing uncertainty will create a better business environment and help our nation.

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