# Trade War Blues

## Uncertainty and Business Investment

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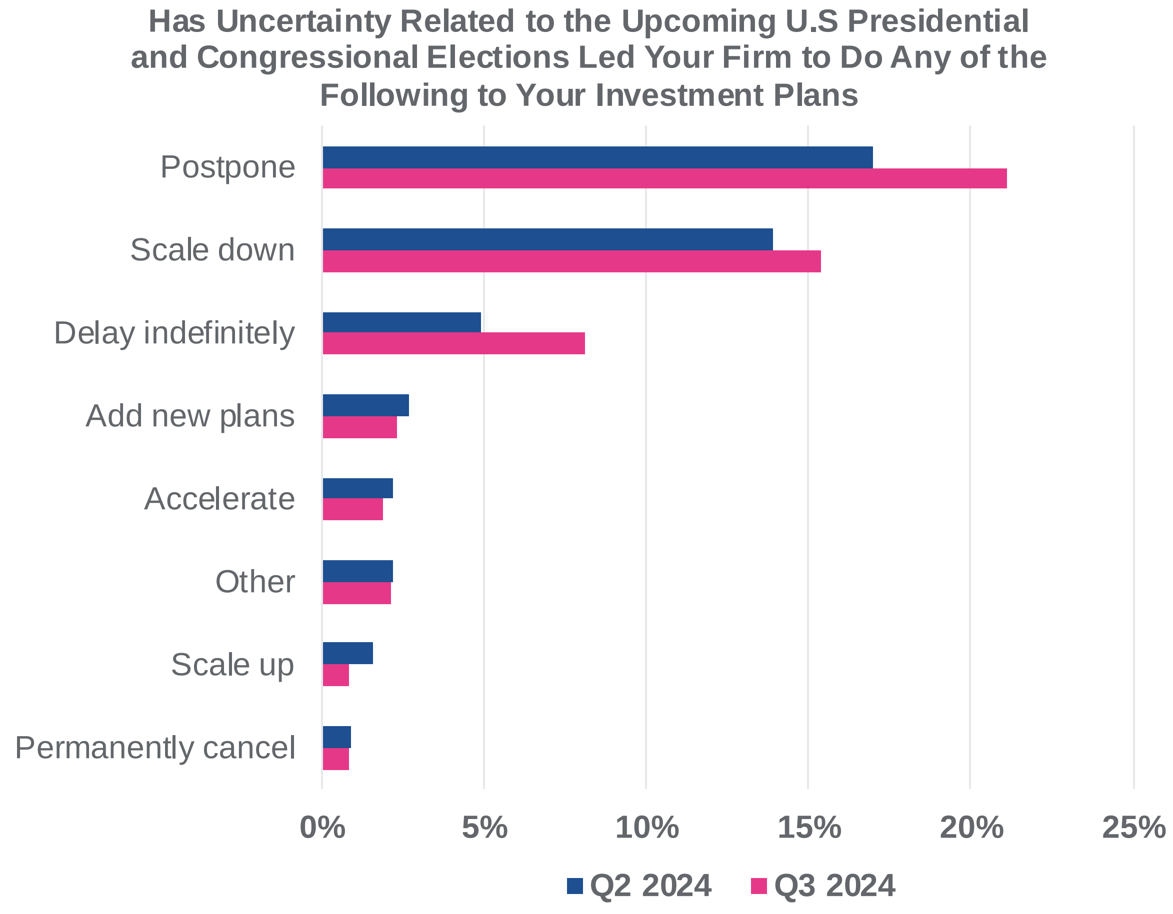
# Overview and Key Takeaways

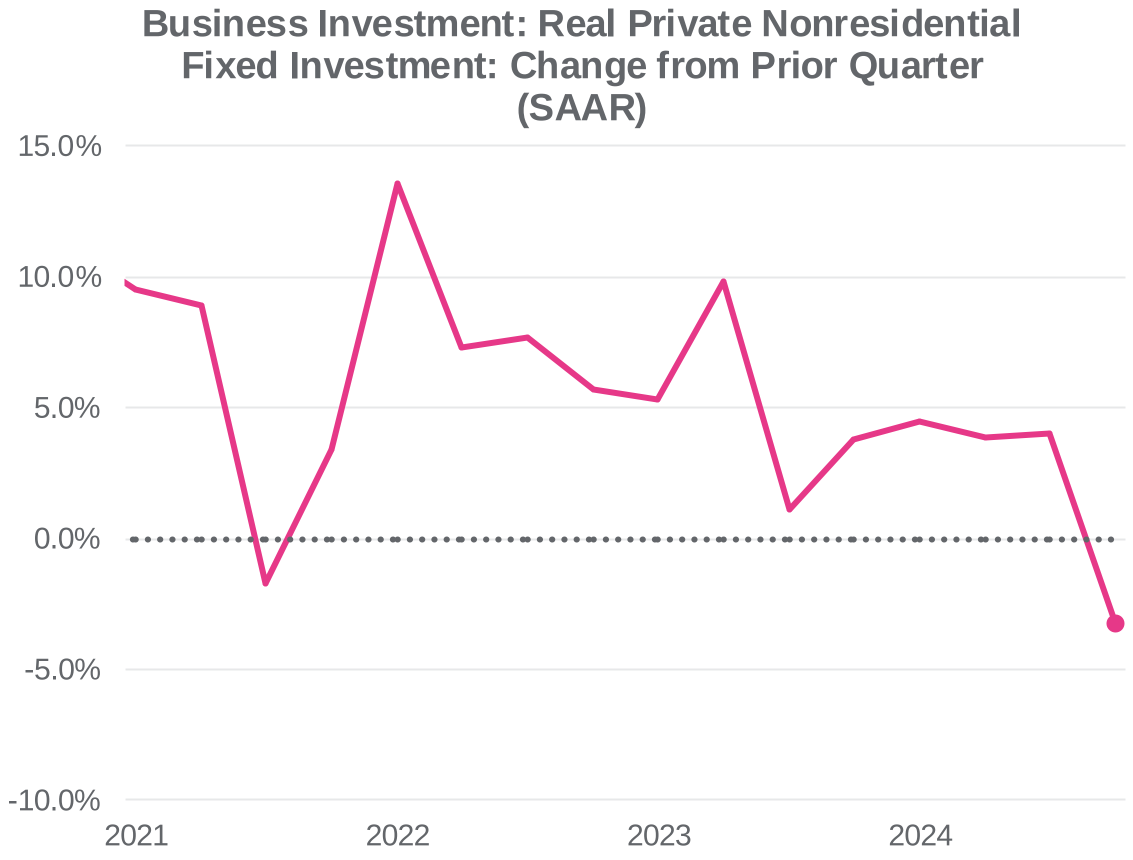
The rise of the trade war and tit-for-tat tariffs between nations has driven uncertainty skyward and fueled concern over the US economic outlook. While numerous surveys have pointed out rising pessimism among consumers, the more immediate impact may turn out to be a decline in business investment as both businesses and lenders remain cautious in the face of uncertainty. Less business investment would weigh on the economy both the short and long-runs and could perpetuate other risks – like low levels of hiring, which leaves the economy susceptible to rapid rises in unemployment.

- Even before the start of the trade war in early 2025, business investment was slowing. With trade uncertainty recently hitting an all-time high it's likely that businesses and lenders will remain cautious until we gain more clarity around the policy path forward.
- History shows that banks cut bank on lending to businesses during the last trade war and there are reasons why that dynamic may be larger this time. Banks entered 2025 with tight lending standards, business delinquency is on the rise, and some banks are still dealing with large unrealized losses in their securities portfolios - which can reduce their lending capacity.
- While the labor market remains on decent footing, it has been struggling with a low hiring rate and is slow to absorb people looking for work. Weaker business investment could continue to drive this trend, which leaves the economy vulnerable to a rapid rise in unemployment if layoffs pick up.

# Businesses were already postponing projects prior to start of trade war

— Business investment shrank in Q4 2024 for the first time since 2021

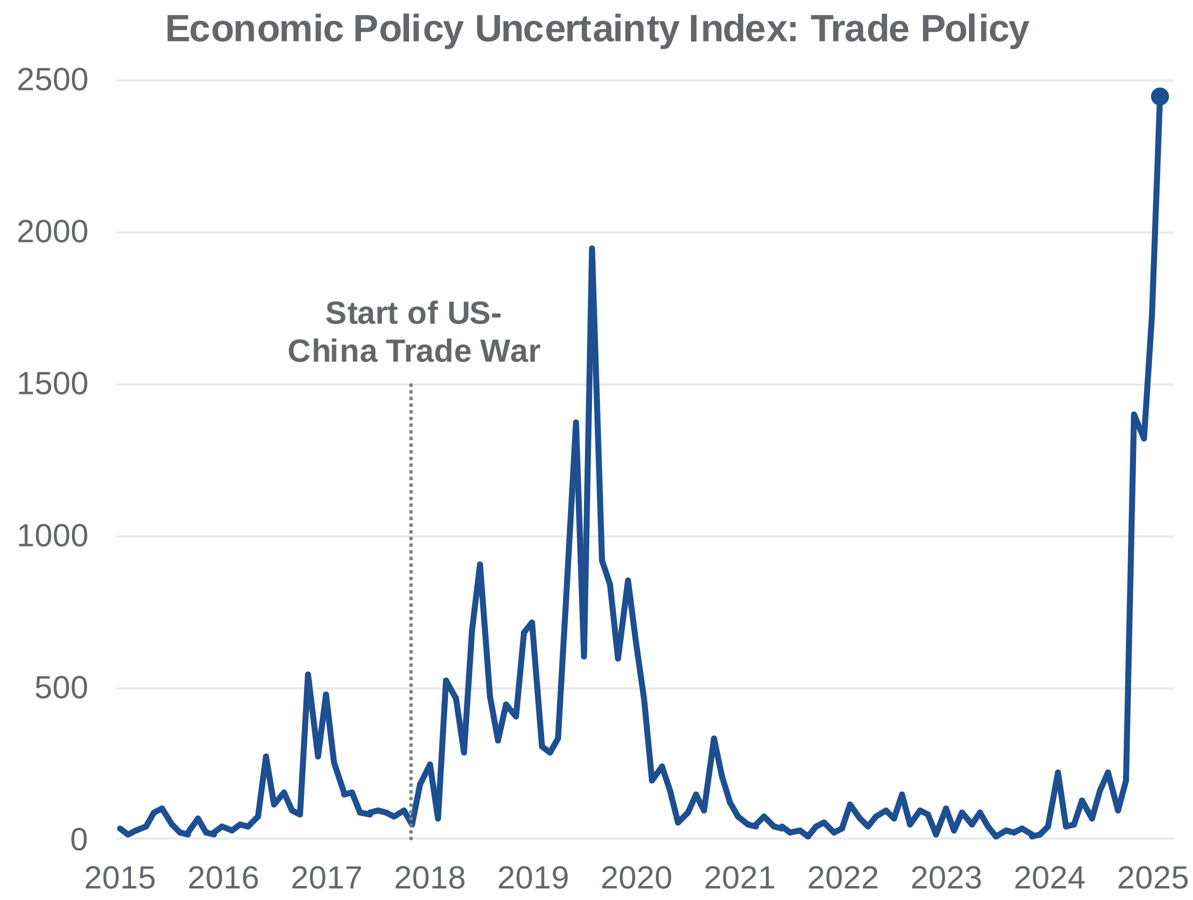



*Source: Federal Reserve Bank of Atlanta: "How Does Election Uncertainty Impact Firms" , Bureau of Economic Analysis and Experian Economic Strategy Group*

# Trade uncertainty hits highest level on record in February

— History shows that banks pulled back from lending during the last trade war




### Lessons From the 2018-2019 US-China Trade War

"…**banks exposed to trade uncertainty contracted lending during the trade war period** (2018–19) relative to the preceding period (2016–17). Banks more exposed to trade uncertainty also increased interest rates on new loans. **Importantly, these results hold for all borrowers and for borrowers in sectors not as directly affected by trade uncertainty.** Thus, banks exposed to trade uncertainty do not appear to differentiate across borrowers in their lending behavior. **Instead, banks facing a rise in uncertainty adopt a wait-and-see approach by contracting credit for all borrowers**."

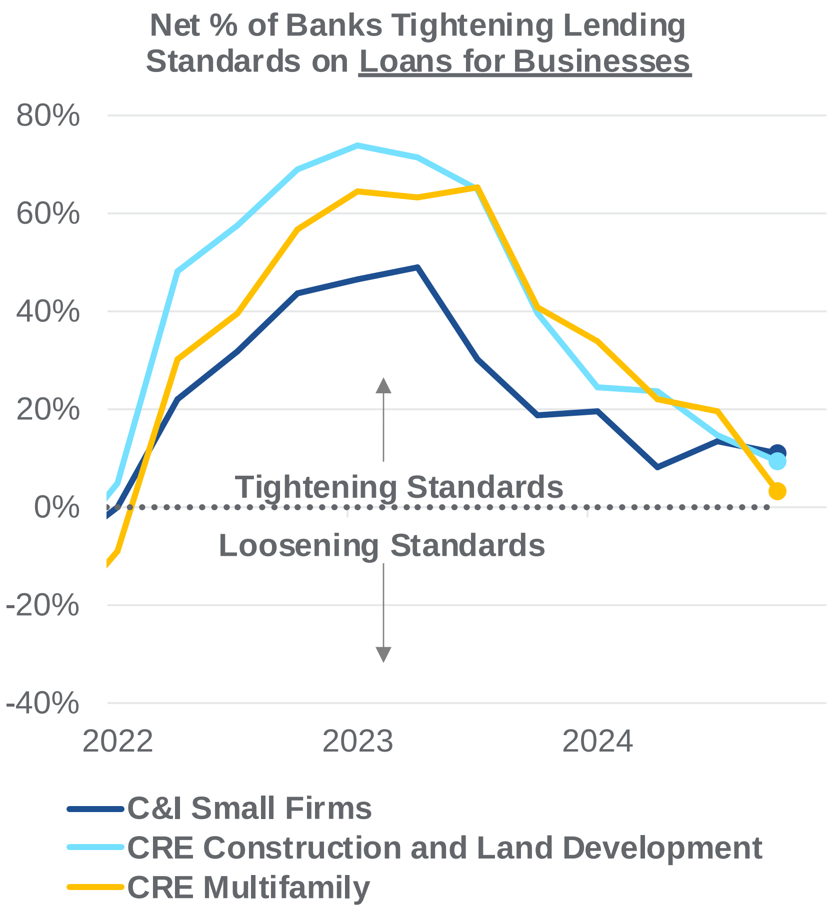
**— Federal Reserve Bank of Atlanta**

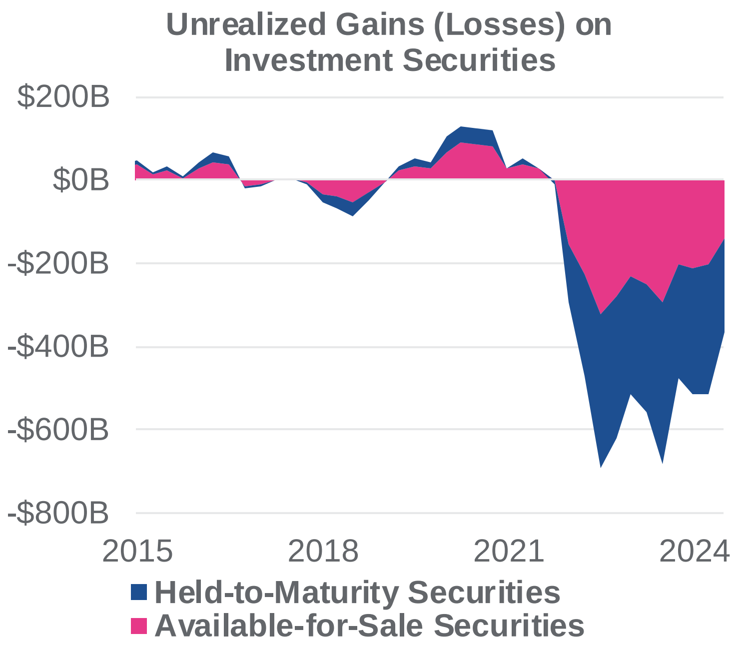
*Source: Economic Policy Uncertainty Index (Scott Baker, Nick Bloom, Stephen Davis), Federal Reserve Bank of Atlanta: "Does Trade Uncertainty Affect Bank Lending", and Experian Economic Strategy Group*

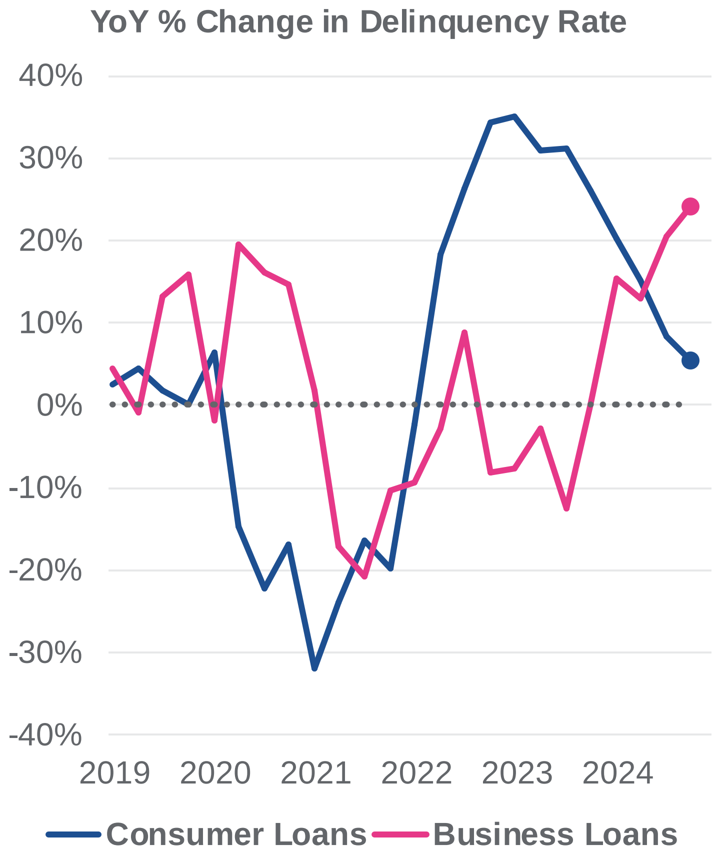
# Current dynamics may mean an outsized impact on business lending

— While the pace of lending standard tightening has slowed, conditions remain tight. Unrealized losses on banks' balance sheets and rising delinquencies may drive enhanced caution.




> **"As unrealized losses increase, lending constraints can tighten, reducing economic growth**—and potentially motivating monetary policymakers to adjust their policy stance."
>
> **— Federal Reserve Bank of Kansas City**

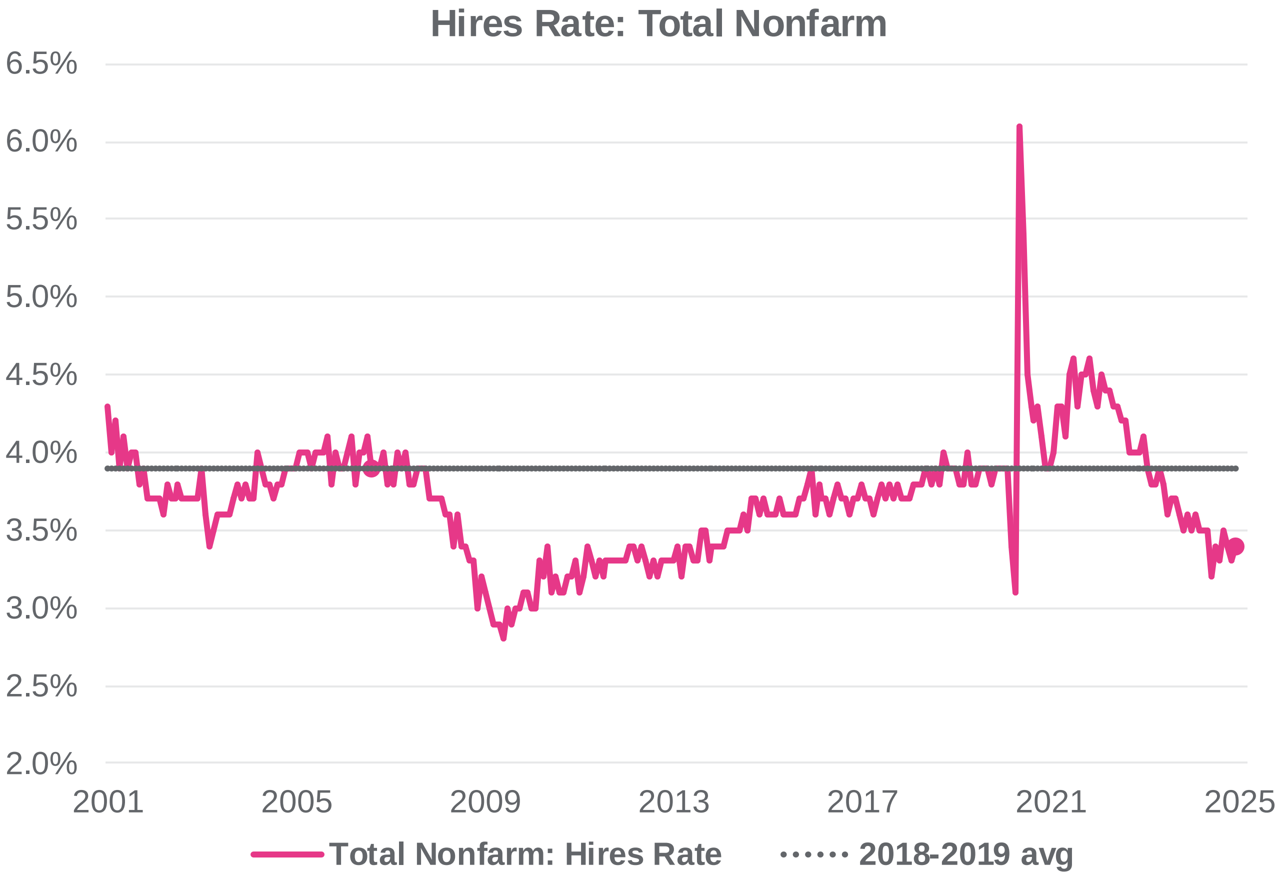



*Source: Federal Reserve, FDIC and Experian Economic Strategy Group*

# A pullback in business investment could perpetuate low rate of hiring

— Low rate of hiring means the labor market is slow to absorb people who are looking for work and is the primary driver of rising unemployment. This dynamic leaves the economy susceptible if layoffs pick up.




"It's a low-hiring environment. **So if you have a job, it's all good, but if you have to find a job, the hiring rates have come down.** It's not overheated anymore. We don't think we need it to cool off anymore. We do watch it extremely carefully."

**"If there were to be a spike in layoffs,** if companies were to start to reduce headcount, **you would see unemployment go up pretty quickly, because the hiring rate is quite low."**

**— Jerome Powell, Federal Reserve Chairman**

*Source: Bureau of Labor Statistics, FOMC January 29th 2025 Press Conference Transcript, and Experian Economic Strategy Group*