

*(Draft Transcript)*

## **The U.S. Presidential Election and Its Economic and Security Implications<sup>1</sup>**

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As we know, we had an election yesterday in the United States. Donald Trump won the presidency. The Democrats had appealed that Hillary Clinton won the popular vote. But in the United States our mechanism for electing the President has an intermediary step or an intermediate step called the electoral college. Donald Trump has appeared to have won decisively with the electoral college. And he will become President in January.

In House Representatives, the House remains Republican; the Democrats have picked up some seats but not enough to take control. The Speaker, Paul Ryan, is in a weak position. He did not actively back Trump and there is some tension between him and Trump. In general the power of the Speaker of the House has been declining because of internal rules changes, for instance, no longer allowing earmarks and so on. It is likely that when there will be new Congress caucuses in January, there will be a challenge to Speaker Ryan; though I don't think that challenge will be successful.

In the Senate, the Republicans have held control narrowly although two seats are still not determined and they will probably pick up some more seats in 2018. The way that it works in the United States, we elect all the seats in the House of Representatives every two years but the terms in the Senate are six years and they are staggered, so you only elect a third of the Senators in each election. It just so happens in the election two years from now the Democrats will be defending many seats and the Republicans will not be defending so many. So it is likely the Republicans may pick up some additional seats in the Senate in 2018.

In the Senate, there is something called the filibuster and that is where someone has very strong objections to a measure can stand up and talk endlessly. You may have seen the old movies like "Mr. Smith goes to Washington" where people stand up and talk and talk; they read the Bible and whatever. Those rules were changed to allow people to effectively invoke a filibuster without actually having to stand up and talk. That means the filibuster has begun to be used very promiscuously. There were rules changes made a couple of years ago when the Senate was in control of the Democrats to make it possible to stop a filibuster or to shut it down with only a majority vote instead of a super majority.

What this means now is that on many issues the Democrat's ability to obstruct

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Republican initiatives is going to be limited. There are still some issues such as the confirmation of Supreme Court justices that require a super majority but the Democrats will not going to be able to just play an obstruction game. What this means is the Republicans now controls the Presidency and both Houses of Congress and they are going to have to govern and they will be responsible for what happens. One of the things people have been really upset about is so-called “gridlock”. Well, now one party controls everything and they actually have to govern.

Just in passing before I go on to talk about more substantive matters, just a note on how did it happen since this was not a predicted outcome, first of all, the voting turnout is down considerably. It was a very negative election and basically turned people off. The Republican popular vote totals over the last three elections have remained fairly flat. What has really changed is the Democrats have trimmed it down tremendously. In this electoral cycle African Americans simply did not come out to vote in the numbers that they had in the two previous elections when Barack Obama was on the ballot. Mrs. Clinton lost the working class decisively. She even lost working class women despite the fact that she is a woman and would have been the first woman president and despite the fact of Donald Trump’s widely reported misogynistic comments and behavior. She even lost working class women.

Trump won whites, a larger share of the electorate. He won the non-college educated and did surprisingly well among Hispanics. People thought the growth in Hispanic vote would be decisively Democratic. Trump actually ran better among Hispanics than Mitt Romney did four years ago. He had surprisingly long coattails. There has been a trend over time in the United States for people to vote so-called a “straight ticket”, the vote for a single political party for all the positions on the ballot. But Trump was so controversial that people thought that there might be a reversal of the trend and much more ticket splitting. That doesn’t seem to have happened and his success seems to have carried along some Republicans in the Senate and the House.

So what will we do? He actually didn’t emphasize many issues in the campaign. This campaign was actually remarkably content free. Neither candidate really addressed issues. It was mainly about personalities and name calling. But to the extent that Trump did emphasize issues, the issues that he emphasized and the issues that seemed to be most salient with the voters coming out of the poll booths in the exit polls were immigration and trade. So let me quickly focus a bit on immigration taxes because I think it is going to be an important part of what is going to happen especially from the Korean standpoint and trade.

Because of his inexperience – he has never served in the government, he has never served in the military, and I believe he is the first president to hold that distinction, his appointments are really going to matter. Chris Christie is the head of his transition team and he is a very important man at the moment. It is also the case that many of the traditional Republican foreign policy office holders signed public letters saying they will never work for Trump. So either these people are going to have to go back to their public statements or the set of appointees is going to be drawn from a significantly different pool than you see in the previous Republican administrations.

Among the names being mentioned for Treasury, the leading candidate by far seems to be Steven Mnuchin, a former Goldman Sachs executive and other names include Representative Jeb Hensarling from Texas and kind of a dark horse candidate is the elderly private equity investor Henry Kravis.

At State, John Bolton, who some of you may remember from the Bush Administration for his role in the UN with a big white moustache, is probably the leading candidate to become the Secretary of State. The most prominent Republican foreign policy guy who did not come out against Trump which everyone interpreted as him kind of keeping himself viable is Stephen Hadley, a former national security advisor; he is another name possibly mentioned at State or Defense. And other names include the former Speaker of the House, Newt Gingrich and Senator Bob Corker from Tennessee.

At Defense, the person who one would think is the leading candidate is Michael Flynn. The problem with General Flynn is he is technically ineligible. To serve in the Defense Department you have to be off of act of duty for 7 years. General Flynn has not been off of act of duty, so we will require a special measure of Congress to make him eligible. So it is possible he could get the job. Others include Senator Jeff Sessions of Alabama, Stephen Hadley who I already mentioned, and former Senator Jim Talent of Missouri.

It is interesting that no one has been mentioned as a potential USTR in the Trump administration. That could be a very interesting job.

But the point I would just emphasize is given his inexperience and given the lack of policy detail, these appointments are really going to matter because these people are going to make policy to a greater degree than might be the case in other administrations.

So what about substance?

The Trump signature issue is the forcible deportation of the 11 undocumented migrants and the building of a wall along our border with Mexico which the Mexicans would pay for. Over the course of the campaign, he backed away to those statements to the point that by the end honestly I could not tell the difference between the Trump policy and the policy of the Obama administration which has actually built some walls and deported a lot of people. So it is really hard to say what he will do on immigration. If he were to try to deport 11 million people, some of them are Koreans I might add, it would require basically the creation of a new police force and you would have to go door to door trying to find people and you would undoubtedly deport some American citizens along with the illegal aliens. And it will harm the economy because these undocumented migrants make up about 6% in the labor force.

So I don't think he is actually going to do what he says but he is going to have to do something having made that such a prominent part of his campaign. We will get a very early indication. I double checked his website this morning just to make sure I get the facts right. On his website, he says his first day in office, I guess in between getting sworn in and going to the inaugural balls, he is going to amend the Patriot Act by Executive Order to bring money transfer services such as Western Union under the Act to the Know Your Client provisions which will have the effect of effectively cutting off remittances from the United States to Mexico. Then he is going to tell the Mexicans, "All right, you pay for the wall, or I will have these provisions go into effect" at which point the Mexicans will pay for the wall, according to Trump.

The reason I raise this is because his claim is so specific and it is so early on that it will give you an indication about maybe how seriously to take the rest of these and if actually does try to go through with these, it will cause enormous trouble with our relations with Mexico. Interestingly enough, net flow of migrants now is from the United States to

Mexico, not the other way around.

And indeed as I get to the trade part, if he actually implements the trade policy he has campaigned on, he will put the Mexican economy into recession. And in fact the flows will reverse and we will have more Mexicans in the United States, along with more illicit activities, not less.

Now fiscal policy, taxes. He has promised personal income tax cuts but those are small peanuts compared to the corporate tax cuts that he has promised. He has promised to lower the corporate tax rate in the United States from 35% to 15%. Neutral third party observers estimate that the Trump tax policies would cost the US government \$2.6 trillion in revenue over 10 years. In addition to cutting taxes massively, he said he is going to rebuild our infrastructure and increase expenditures on defense. Certainly, the rebuilding of infrastructure is something he will probably get support among Democrats in the Congress. So if you put those two things together, massive tax cuts and increased spending, obviously, you are going to have rapidly growing budget deficits in the United States. What that will mean in the short run is probably accelerated growth in the United States and an appreciation of the dollar. So if you get accelerated growth in the United States and an appreciation of the dollar, you would get widening trade deficits, which brings me to the topic of trade.

Trade was another one of his signature issues and one of the two issues that were most salient with the Trump voters in the exit polls. He has promised to put punitive tariffs on China and Mexico. He says in his website that his first day in office, I guess, he is going to name China a currency manipulator and then put some sort of countervailing duty on China. It's a good idea but the problem is it is not consistent with the existing US law. Under US law, China today is not a currency manipulator and no country is under US law. But that's just a detail.

On punitive tariffs on China Mexico, he has actually even talked about having firm-specific tariffs which is a really strange idea and historically unprecedented. I believe it is unconstitutional, though I am not a lawyer, under our Equal Protection clause and certainly violate our WTO obligations. People are speculating why that is the case and they have noticed that some of his biggest advisers and financial backers own firms in Mexico that export to the United States. So perhaps that is the reason why he is thinking about firm-specific tariffs.

He is very upset about disastrous free trade agreements and obviously the worst is NAFTA and the second worst is KORUS. He and his campaign repeatedly referred to KORUS as a job killer which various times they have claimed to have killed 85,000-100,000 US jobs. Now the problem with these comments on both NAFTA and KORUS and other agreements is there is a lack of specificity. So, you can imagine a range of outcomes, ranging from that he abrogates NAFTA and abrogates KORUS, which is I think a real possibility to a situation which having made these statements and there are complaints on the US side about the implementation of KORUS that they essentially negotiate some side agreements with the Korean government so the agreements remains in place, the visa waiver program remains in place and it doesn't really disrupt the relations with Korea very much but there is some additional negotiations so there is a wide range of possibilities.

He has also said if he doesn't get his way – I think the real problems he is going to encounter is with China and Mexico, not with South Korea – if he doesn't get his way and

the WTO rules are against him, then he will withdraw from WTO. Unlike much of the immigration policy and unlike the tax and spending policies where he has got to work with the Congress, he can effectively do these trade policies by Executive fiat. One of my colleagues, Gary Hufbauer, who is not only a formidable economist but a lawyer, went through all the statutes and nearly about half a dozen statutes on the books where he can do that unilaterally without any kind of congressional oversight. Michael Gadbaw from the Georgetown Law Center who looked in the same issue reached the same conclusion. So in the trade area he has a lot of autonomy.

Needless to say, TPP is dead his concerns about currency manipulation could also entangle where Bank of Korea's behavior from the standpoint of the United States leaves something to be desired. So the bottom line is that this is shaping up to look like a really bad version of the first Reagan administration where you had a very expansionary fiscal policy, an appreciating dollar, widening trade deficits and then bad trade policy to try to compensate for the widening trade deficits. So if I'm a Korean – I am looking one to two years out, I would expect trade problems with the United States because of these basic context, plus there may be specific things having to do with trade wars with China or whatever.

Finally, let me just say a little bit about North Korea. As it says in my notes, who knows? One thing about Donald Trump is when you watch him he seems to have a remarkably transactional view of the world. At one point, he said yes, he would sit down with Kim Jong-un for a hamburger and coke and they will sort out the nuclear issue. And I think he probably does believe and I think he may well be right that in a one-on-one negotiation he will out-negotiate Kim Jong-un. Maybe he sits down for a hamburger and coke with Kim Jong-un and resolves the nuclear situation. He had also gone on CBS news on television and said that he thought China should assassinate Kim Jong-un to take care of the problem. So we've got a range of policy options running from killing Kim Jong-un to having a hamburger with Kim Jong-un. To go back to what I said earlier, who he appoints is really important because his inexperience and he is kind of all over the map, kind of pronouncements about policy means who's actually running the North Korean policy review and what kind of policy ideas are coming up with is going to be really important. Likewise, he doesn't like the exiting status of the forces agreements. He thinks Korea should pay more, so if I'm Korea, don't be surprised if the United States comes and wants to renegotiate the SOFA agreement.

He has made wild statements about nuclear weapons, basically saying that he thought Japan and South Korea having nuclear weapons will be a good idea and even making kind of light comments about nuclear exchange between North Korea and Japan. Again, who he appoints is going to really matter because his own views seems to be so over the map. On that presumably unsatisfying note, I will end my comments.

### **Q&As**

**Q:** I was interested in John Bolton maybe Secretary of State. His visits here over the years he has made a lot of tough comments about North Korea. I realize that it's very certain what Mr. Trump's policies will be. Do you think John Bolton will as Secretary of State he will be as toward North Korea as he sounded in his speeches in Seoul, in Washington and in the United Nations?

**A:** Everyone talks tough until they actually have the responsibility of action. This is not

personal with respect to Mr. Bolton. I think that one has to assume that when in office and when given responsibility people will temper some of the things they might say to a breakfast meeting where ultimately there's nothing at stake. That said, I will be remissive if I didn't communicate to this audience there is a growing frustration in the United States, and it is bipartisan. You would have gotten this if Mrs. Clinton has gotten elected as well. There is a growing frustration with North Korea and there is a growing frustration with China. And I think that the first step is going to be more aggressive secondary-ish sanctions against Chinese firms that do business with North Korea. I will just cite the recent report by the Council on Foreign Relations that has been a kind of a mainstream conventional group. So-called kinetic options with respect to North Korea are increasingly contemplated. Whether John Bolton would do everything once in office that he said he would or not would also depend on who the Secretary of Defense is. I don't know. But if I'm South Korean, I would be prepared for a harder line, a more aggressive stance towards North Korea than you have seen for the last eight years.

**Q:** When we have this Brexit vote, many experts believed that it is not a good idea to vote for Brexit but it turned out to be wrong. I guess many of us here also that it would be probably believed Hillary Clinton rather than Mr. Trump and we turned out to be wrong again. You came out with many factors that low turnout for Democrats and all. But somehow I get this feeling that we may be misreading the world which is changing at a very fundamental level. We keep missing it and coming up with different reason. We might be right on specifics but we may be missing a bigger picture. Are we actually on the wrong side of history?

**A:** I probably should have mentioned this in my remarks. I won a substantial amount of money last night from some of colleagues. One of my colleagues publicly stated that Donald Trump had a zero percent chance of winning. I said, "If that is the case, you should accept the bet of me betting \$2 against your entire personal estate if you think it really is that." And he backed off of that but we had got down to a reasonable bet. And the reason I was going to bet my colleagues was I thought the polls had it wrong. And the reason I thought the polls had it wrong was, in various terms for this, the Bradley effect, the Thatcher effect, the Brexit effect, the shy voter effect, that comes down to people were embarrassed to tell pollsters that we're going to vote for Trump. You don't want to admit that you're actually going to vote for this guy. The polls being wrong, together with Hillary Clinton not being able to mobilize African Americans in the way that Obama did and so and so forth, led to the outcome that we had. So on your deeper question, I think what's happened and I can speak most clearly to the United States, in the last two generations we've had a tripling of international trade in the economy. So the US economy has globalized dramatically. It has globalized dramatically and at the same time we have not expanded in any way the social safety net or increased adjustment programs for people who were disadvantaged by that expansion of trade. At the same time that's going on, immigration has been relatively high by historical standards and it's coming largely from non-European sources. So what have in the United States are a group of older white people who see their country they grew up disappearing before their eyes. They don't have the jobs they used to have; their kids don't have the jobs they used to have; and everybody who's moving into the neighborhood looks different than they do. It's different kind of food and they may speak a different language and so on. So there's a deep cultural apprehension among that older generation about these changes. If you look at the public opinion polling data in the United States, attitudes towards globalization have a very strong intergenerational trend. Young people are much more cosmopolitan, much more comfortable with it. Even the young people who were supporting Bernie Sanders were supporting him because of his authenticity and free college

education, not because of his opposition to TPP. They were supporting him in spite of his opposition to TPP. They are quite comfortable with globalization. But the older generation is not. I think what we saw in Britain which I don't know as well and certainly what we saw in the United States was a reaction or a revolt by the people who think they have been left behind by these changes and nobody has been listening to their problems. Donald Trump, for whatever you think about him, is a very effective political entrepreneur and managed to harness that anger and that disappointment. And he has ridden it to the White House.

**Q:** When I visited New York some months ago right after the Brexit vote, many of the friends objected to Trump except one who is a chief economist of an investment bank. He said Donald Trump could be elected president and he can be quite successful. When Ronald Reagan was elected, many Americans despised him initially and later he was liked by many Americans. Whether we like it or not, the election is over and we have to accept the result. DO you think Donald Trump can be a successful President for the United States and for the rest of the world?

**A:** Of course, I hope he is successful. This was an unbelievably nasty campaign. It violated norms that most of us thought were just embedded in stone. It brought extremist groups out of the wood work who we thought had been successfully repressed. This is truly ugly. Having said that, last night in his acceptance speech Trump did the pivot that people were expecting at the convention, a pivot towards greater inclusivity. Whether he is able to successfully carry that out is going to depend not only on himself but I can't overemphasize who he appoints. If he appoints reasonable politicians who I may not agree with on policy but are not crazy people like Mike Pence he may be able to manage this situation if he appoints people who have very strange views or kind of do not know how to speak in public this could be very, very messy. The one thing I would say about Ronald Reagan is Ronald Reagan had been both head of a screen actors' guild and governor of California. So Ronald Reagan had dealt with political roles in a broader sense before he became President. And certainly, governor of California is a very important position. Trump lacks any kind of conventional; political experience and honestly the other thing if I were expecting if I were Korean, I hope this is not the case truly as an American citizen and as somebody who cares about the world, but I would expect the amateur hour for first year that it's just going to be a chaos unless they do a very good job in this transition and they really get a y good set of people in very quickly. Otherwise, this could be a very different call. The one thing he has going for him I suppose is the Republicans control both houses of congress. So congressional relations will be fairly cordial he won't be fighting the congress every day the way that Hillary Clinton would have. I hope that for all of our stakes he has a successful presidency. I hope that his speech he gave last night is a signal that he has a capacity to turn and to re-orient himself and the people around him in a more constructive way than what they showed during this campaign.

**Q:** Are you going to see any strategic patience towards North Korea with the Trump administration?

**A:** Patience has worn very thin. That's the starting point. But remember Trump is an entirely transactional character. So if he can make a deal, he'll make a deal. It may be like Nixon going to China and Menachem Begin going to Egypt. It may take somebody who's assertive and crazy with hard line views as Donald Trump to make a deal with North Korea

## **Dr. Sung-won Sohn**

In a nutshell, I'm actually a bit more optimistic about Trump presidency abstracting away from foreign policy. It could actually be positive for the US economy. I think it's good that we have an outsider, not a person in Washington, a traditional politician running the US economy. I do have, obviously, some concerns as you will see in a minute. But my basic thesis is that it is not as bad as you think and it may actually be pretty positive for the US economy and the global economy.

Given the election, it's been a very controversial election especially because the so-called unfavorable rating was so high. If you look at the Trump's unfavorable rating right before the election was 63% and the Clinton's unfavorable rating was 55%. If you go back to 1960 when Barry Goldwater was running for president, the unfavorable rating was never this high. This really led to a lot of uncertainties. We had an unprecedented amount of uncertainties in the United States and elsewhere. That is very important for the financial markets and the economy. As we say in the financial markets and the economy, we can handle bad news but not uncertainties. I guess good news is that one of the major uncertainties is now out of the way. We know who the next US President is. As we get a better picture of the cabinet members and assistants in the White House, we will get a much better bearing on economic and foreign policy in the future. This is one of the reasons why the stock market has done very well yesterday. Dow Jones went up over 2% and financial services stocks which were really beaten down during the campaign in part because of uncertainties went up 5% in a single day. Financial markets reacted very positively.

Campaign rhetoric is rhetoric. This happens all the time. During the campaign, candidates say a lot of things. But they either backtrack or the staff would modify a lot of things. Simply because they said it during the campaign does not mean that that's they are going to do. That's when the reality begins. Since Trump is a relative newcomer to politics, whom he appoints as his lieutenants is going to be very, very important.

Let me just dive into Trump's economic programs. You see Trump's tax plan. It's actually a supply side incentive. Mr. Trump has borrowed a page from Ronald Reagan and he wants to cut taxes not for the poor but for the wealthy. He is going to rely on supply side so-called the trickle-down economics to make sure the economy does better. I'm not disparaging it and I happen to think that this is one of the ways that we can boost the US and the global economy. The other thing that I want to point out is that if you look at the tax cuts, most of the tax cuts go to the wealthy. People at the low end of the income spectrum are not going to get much. Again, it is a supply side program.

Clearly, as a result, the federal debt as a percentage of GDP which is already high will probably continue to rise. If there is a caveat, in economics, we talk about static and dynamic models. In static models, there is no follow through. Dynamic models will have supply side effects; it will have secondary positive effects. If you take that, I think we have a very different picture.

After Margaret Thatcher became Prime Minister in the United Kingdom in 1979, the stock market and the economy went up very nicely and positively. That's why today it's called the 'Thatcher Revolution' which spread beyond the British Isles. In the United States, something similar happened when Ronald Reagan was elected President in 1980. You see what happened to the stock market and the economy. We had supply side effects. My belief is that when Trump executes his program although I am not sure to what degree, his supply



side programs will have positive effects. There are concerns that budget deficits will go sky-high and that will mean doom and gloom for the US and the global economy. I don't think that's correct.

Clearly, supply side effects will not be positive for everybody. There will be winners and losers. There will be complainers. But on balance for macro-economy we will see fairly positive supply side consequences for the US economy.

There are other things that I see positive in Trump's economic programs. First of all, he says he is going to spend a lot of money on infrastructure, up to \$500 billion over the next 10 years. That's quite a bit of money. When you talk about infrastructure, we are not just talking about cements, excavators, etc. When you spend that much money on infrastructure, there are a lot of IT people. For example, they need a lot of software, computers, equipment and technology, so that this will have benefits throughout the economy, not only in the United States but hopefully through Asia including Korea. This is one of the major benefits.

The other thing is corporate tax reforms. The US corporate tax rate is one of the highest in the world. That is not right. That is one of the main reasons why many America's corporations including Apple and General Motors have money sitting overseas. When that money is brought back because of the corporate tax reform, it will be a spur, a stimulus, a positive for the US economy and also for the global economy.

The other thing that I really like about the Trump's programs is decrease in regulations. He said that we have too many regulations. Again, as I said, yesterday in the United States, the financial stocks, the bank stocks went up by 5%. One of the main reasons is Trump said "I'm going to dismantle regulations." That is also very positive. To me this is one of the best things any government can do in Korea and in the United States. The industries to benefit include healthcare, energy, and banking and finance. Without the fear of higher minimum wage, we will see more and more corporations including McDonald's hiring more low-wage employees, so this will be good for the economy.

Having said that, I see quite a bit of positives in a Trump presidency, not so much negatives. I think we all agree that there are some limits. That is what I call limits on the Trump plans. One of them is Congress. Now we have Republicans controlling the White House and both houses of congress. Theoretically, they can do anything they want. But Mr. Trump's Republicanism is very different from the philosophies of the Republicans on Capitol Hill, in the Senate and in Congress. And as a result, I don't necessarily think we will have a unified government. In fact, they are cold Republicans I really see them behaving more like a divided Washington, with the White House under the control of Donald Trump and in Congress the Republicans have the minds of their own. There are and there will be many differences.

What I'm saying is this is actually positive. The economy and the financial markets like a divided Washington and a divided Congress. They can't spend money and they can't pass a lot of regulations. Let me give you what happened since 1962. When we had a unified government, the stock market did not do very well. When we had a divided government, the stock market did much better. And I think this is what's going to happen.

We all agree that the biggest negative could be trade. I think the biggest worry is trade. I think it's fortunate that international trade has benefited everyone – Koreans, the

Chinese and the Americans. I think the American economy has done as well as it has in the past because of free trade and international trade. America's largest export item is agriculture and by the way that's where a lot of electoral college votes is. That's where Mr. Trump won. Also, for America's technology companies from Google to Microsoft, more than half of their income is coming from overseas. When you talk about international trade, one of the primary beneficiaries of international trade has been the United States. I hope we are not going to shoot ourselves in the foot. And that's one of my concerns.

But when you talk about Mr. Trump on trade, assuming that he will follow through what he preached during the campaign, he is just not anti-trade, he is just not a protectionist, but he is what I call an isolationist. He's saying, "America First and I'm going to build the walls not only along the Mexican border but trade walls as well." This is one area where the US President has a lot of discretionary authorities. We have trade agreements and that requires the act of Congress. On limited statutes the President can raise tariffs or impose trade sanctions on many countries and many products. In emergency situations he can almost do anything without the consent of Congress. This is where he can do a lot of damage. This is where Korea could be adversely affected as the Korean economy is very trade dependent.

On impact of trade war on growth, let's assume that Mr. Trump actually follows through with his threats and then also let's assume that we impose a 45% tariff on Chinese good and a 45% tariff on Korean goods and a 35% tariff on Mexican goods and etc. And also we assume that the Chinese, the Koreans and the Mexicans would retaliate. You can see what happens to economic growth in the below graph. The blue bar is a subtraction, a decrease in economic growth in the United States. The green bars assume that the United States imposes tariffs and sanctions and the Chinese, the Koreans and the Mexicans would not retaliate. Obviously, that's not going to be the case. But juts for the sake of explanation, even in that situation, that is bad for the United States. The United States and anyone else need trade for growth.



What's unfortunate is that if you have protectionism, it is not so much the rich who get hurt. But when you look at the low income in America, they need cheap Chinese goods, shoes, bicycles, light bulbs, etc. And they are the ones who are going to lose most jobs. So it is not really the rich but those at the lower end of the spectrum are the one who are going to be really hurt. In fact, as you recall, President Obama decided to impose tariffs on Chinese tyres 3-4 years ago. To make a long story short, here's an estimate from the Peterson Institute for International Economics. The Obama tariff on Chinese tyres saved 1,200 jobs, not created, but the study shows that it cost American taxpayers \$900,000 per job. A lot of people don't realize it and simply say, "Wow, that's great. We saved 1,200 jobs." Mr. Obama never talked that it cost almost a million dollars per job.

When you have less trade, not only the poor people who have to pay more because they need cheap imports but also they are the ones who lose jobs. Also, the Americans in general, the Koreans in general, and the Chinese in general get hurt because we have all monopolies and oligopolies. A good example in the United States is sugar. Sugar has a strong tariff and as a matter of fact quotas. You cannot import more than so much sugar into the United States. Why? Because the sugar industry has and continues to be very powerful. Sugar goes into everything from candy to all the cooking that we do. So the cost of sugar in the United States is very high for that reason. So with less trade, we will see more and more of these.

Having said that, free trade does not mean it is a panacea for everyone. There are losers by definition. When you have free trade, there will be winners and there will be losers by definition. The thing is that you want to take some of the benefits from the winners and give them to the poor. And that's really the idea and that's how it's supposed to work. But that has not exactly worked out. If you look at the US public non-financial firms' return on equity (ROE), you can see the large multinational firms have done very well and in Korea, chaebols have done very well because they have been the primary beneficiaries of free trade. But if you look at the lower end of the spectrum, people are losing the manufacturing jobs and they are the one suffering. In the United States, about 20% manufacturing jobs were lost to China. Unfortunately, we spent only 0.1% of GDP on training. I think we should be spending 5% of our GDP on training and education.

Even before Trump became a candidate, de-globalization was already occurring. De-globalization has been occurring and it predated Mr. Trump. Also, the Global Recession we went through in 2007-09 really gave a rise to more protectionism and de-globalization. You can see what's been happening. International trade has been moving sideways. It's going down. I'm afraid that might be the trend.

When we talk about populism, we talk about entire establishments. It's not about left or right. Bernie Sanders on the left was a populist. Donald Trump on the right is a populist. It is more about the open or closed economies rather than left or right. And the biggest issue of course is immigration. This has played a key role in Brexit and this again played a key role in America in electing Donald Trump. Between 2000 and 2015 people in the Midwest began to see many immigrants coming in which they were not used to. The total number of immigrants in the Midwest is small but the rate of change has been very high. And that's why they decided to vote for Mr. Trump.

What impact will this have on the Korean economy? Probably quite a bit. I will abstract away from foreign policy because that's not my expertise. We all agree Korea is a very open economy and very dependent on international trade. 24% of Korean exports go to

China and 12% go to the United States. Clearly, international trade is very important for Korea. So if we see more tariffs, more protectionism, and isolationism, Korea is one of the countries which are going to be affected most. So far Korea has been one of the primary beneficiaries of more liberal international open trade. In 2015, Korea was 6<sup>th</sup> largest trading partner for the United States accounting for about \$71 billion. In 2016, it's going to be greater, closer to \$80 billion. So that is at stake.

Even before the US election, the IMF said the probability of a global recession has really gone up; in the US 25%, in the euro area about 35%, in Japan about 40%, and in Latin America much higher. Even before the Trump election, the IMF was concerned about a possibility of a global recession. Korea is one of the countries which could be affected by that because Korea is so open and depends so heavily on global trade. What does Korea do? How will this affect Korea?

To begin with, Korea has a number of headwinds. First of all, the global economy is slowing. The global trade is slowing. The IMF says we are going to have a reasonable possibility of a global recession in 2017. So that's one of the problems. Korea obviously has some concerns to begin with. Second, Korea has some structural 3D – demographics, possibility of disinflation, and others. On top of that, we have a Trump factor. And Korea has the Choi-gate. We've got not only the global economy but also the political problems coming from the United States and also the internal problems in Korea.

So what does Korea do? Clearly, things will be different under President Trump. Korea I am assuming has begun to prepare for the renewed negotiations on trade and SOFA and other things with the United States. In fact, I was somewhat surprised yesterday in the wire report that Japan has already sent a vice prime minister to the United States to begin a new relationship. I'm not sure whether Korea has done but that's one of the things we should do. That is, try to build relationship as soon as possible and then try to find out what they have in mind, especially the lieutenants, the cabinet ministers who may become Mr. Trump's lieutenants.

Then of course, we need to think about our short term policy responses and long term policy responses in this situation. In terms of long term policy responses, one of the things is trying to find out what Korea is good at and what competitive advantages Korea has. We need to have a long term response given the global situation in the short run and in the long run and the political situations both in Korea and in the United States.

Given the time constraint, I just want to talk about short term responses. When I came here about a year ago, I talked about the Bank of Korea's monetary policy. In fact, I have been talking about more dramatic cut in the interest rates. To me that is a short term response. There has to be a long term response. In between you need to make sure that the economy doesn't go into a recession. You have to make sure you undergird the economy and that's when the monetary policy comes in. When I have been talking about the Bank of Korea cutting interest rates dramatically for the last two years, a lot of people have said, "You don't live in Korea. You don't know the situation. Korea has household debt problems." That might be so. Household debt is a serious concern. But the monetary policy should not be run based on household debt in Korea. It's a macroeconomic policy. So I think the Bank of Korea should run the monetary policy based on what is good for the macroeconomy, not for the household debt. You have to run the monetary policy based on global macroeconomy. You need a more stimulative policy from the Bank of Korea. When I talk about 0% interest rate, whether it is 0% or 0.5 doesn't matter. What I am saying is we need somebody, some

institution doing something important and something dramatic to boost psychology, so people in the street can say our government is doing something important.

Mr. Abe became Prime Minister and appointed Mr. Kuroda as the central bank governor in 2012 and they started a massive quantitative and qualitative easing program. The economy was caught by surprise positively. For a while, actually the stock market and the economy did very well. The key is having a positive psychological effect. Not so much about the interest rate or not so much about the money supply but having a positive psychological impact is what's important.

Mr. Bernanke did the three quantitative easing programs. The first one was very successful because we were caught by surprise. The financial markets, the stock market and the economy responded very favorably. The second and the third ones did not because people kind of knew about it already. When you have a dramatic cut in the interest rates by the central bank in Japan, in the United States and hopefully in Korea, that will have a very positive psychological effect.

People also ask me about the Fed's raising the interest rate. Yes, but they are not going to raise it by a lot. Last December the Fed raised it by a quarter percentage point. This December, maybe another quarter percentage point. And a year from now, another quarter percentage point. They are not raising a lot. Why should the Bank of Korea be so much concerned about what the Fed is doing? People say that means money will be leaving Korea to some other countries. I don't necessarily think so. A lot of money has been going into Japan because they have confidence that the Japanese economy is healthy, not strong but healthy. Money comes into the United States, Japan and Switzerland because they have much more confidence in the stability of the economies. That's what matters, not whether the interest rate is a quarter percentage point higher or lower. Those are some of the reasons I think it's very important for the Bank of Korea to move as soon as possible.

Two university professors in the United States did a research which was published in the Journal of Business and Economics in 2014. They went back to the US elections all the way back to President William McKinley. They examined how the stock market responded the day after. In the United States the election is held on Tuesday, so they looked at the stock market on the following day, Wednesday. If the stock market does well on that Wednesday, that's a very good indication how the economy and the stock market will do in the next four years. Until the mid-1980s the correlation was actually negative to zero, but since 1985 because of better communication, internet and etc. the correlation now is about 6-7%.

Let me conclude by saying that history tells me that I might be right. Despite what people have said, the stock market said they are actually feeling pretty good about a Trump presidency. They are seeing some positive things at least in the United State. Let's hope that the stock market, the financial markets and the economy will do well and clearly it will mean that Korea will benefit as well.

## **Q&As**

**Q:** Which Korean industries and companies do you think will benefit from and be adversely affected by Trump's protectionism?

**A:** Many of Korea's manufacturing output such as automobiles (even though quite a bit is produced in the United States) and auto related parts is one of the areas where Korea has done a very good job of exporting to the United States. And that's one of the areas where Mr. Trump and his people are very concerned about. So the other one is IT. A lot of Samsung IT, washers and dryers, TV sets and a lot of electronic goods are exported to the United States. If 45% tariffs are imposed on Korean goods, Korean goods will not be competitive at all. I hope that's just campaign rhetoric. But still there might be movement trying to raise tariffs on Korean goods. As I said, Mr. Trump as President can do it without the consent of the Congress. I think the Korean goods could possibly cost more make it less competitive in the United States. The other way around, Korea imports US agricultural goods, Boeing aircrafts, electronic goods, i-phones etc. That will be affected. Trade in both directions will be affected. The key items in the United States to Korea are agricultural goods and aircrafts. Going from Korea to the United States, I would say such as automobiles and electronic goods and shipbuilding will be most negatively affected.

**Q:** The Korean government has presented a 3% growth forecast for 2017. How will the new US administration's trade policy impact Korea's economic growth next year?

**A:** Even the Bank of Korea has lowered its economic projections to below 3%. I really felt that a 3% economic growth was way too high even before Trump presidency. With a Trump presidency and political uncertainties now coming from both the United States and Korea itself this will probably have a long term effect at least through to 2017. I'm looking at economic growth in Korea closer to 2%, not closer to 3%. That's one of the reasons why I said in the short run we need to do something fast. We saw what happened in the case of Japan. They kind of took their time and they let the economy fall into recession and deflation. Once they get in there, it's very hard to come out. It's very important that you prevent the economy from sliding into recession and sliding into deflation. As a short term measure, it's very important that the Bank of Korea cuts interest rates, not by a quarter percentage point but dramatically. I have been saying this many times in public that when you cut the interest rate a quarter percentage point every six months, you are really wasting your ammunition. In the last couple of years the Bank of Korea has been cutting interest rates by a quarter percentage point every six months, what have you accomplished? You simply wasted ammunition. We don't have a whole lot of ammunition left and I hope you utilize the ammunition more judiciously. The economic situation I think is much more serious than the Bank of Korea or the Finance Ministry or many people realize. I think Korea needs to move quickly, so that Korea becomes another Japan.

**Q:** Anti-immigration and anti-trade that we have seen during the US presidential election seem to me a manifestation of an increasing intolerance in the United States. As in the case of the Roman Empire and the Mongolian Empire, these were the symptoms of decline. Now can we see the increasing intolerance in the United States as a sign of its decline?

**A:** As an economist, we need more immigration, more economic growth, and more international trade. But I think you are right. We are in the process of de-globalization that is bad. Globalization is good. I think in the future economic growth is not going to be that healthy. As a matter of fact, I wrote a book in 2014 which was published in Korea and the main topic is about why I see long term stagnation. I talked about the demography. I talked about the productivity slowdown. I didn't get into politics. But I would say that based on economic fundamentals that I talked about in my book we will see long term stagnation around the world, including Korea. On top of that, if you overlay the political situation in the United States which is a reality and the political situation in Korea, I think that probably

will accelerate the long term trend that we have. It's very easy for an economist to say that. But in reality economists don't run the country except for Mr. SaKong. The economists don't run the White House, so you have to be realistic. Hopefully, Mr. Trump will not only take the political situation into consideration but the economic situation into consideration. His positions on immigration and international trade which are largely based on politics will be modified somewhat based on economic reality, which is that we already have economic slowdown and stagnation. Hopefully, he doesn't make it even worse.

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