# Trump Echoes Alexander Hamilton With Import Substitution Stance

by **Rich Miller**
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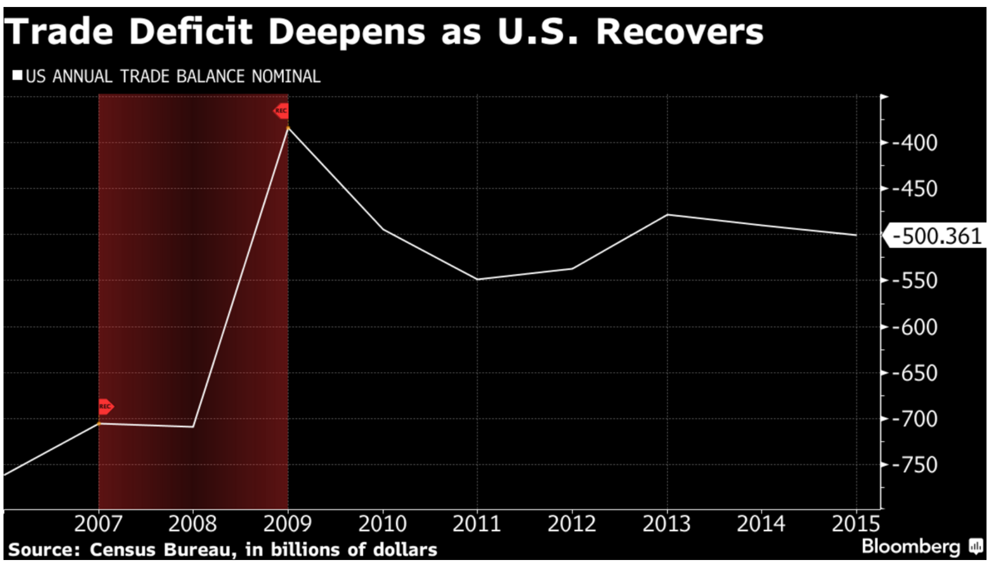
- President's throwback strategy roils currency market
- Bridgewater's Dalio voices concern of a 1930s replay

President Donald Trump. *Photographer: Andrew Harrer/Bloomberg*

When it comes to trade and economic policy, Donald Trump sounds a lot like he's singing from the same songbook as Alexander Hamilton -- and that's got the rest of the world worried.

Like the nation's first treasury secretary, the president proclaims the importance of manufacturing to the economy and wants the government to encourage it. And he is looking to do that through a Hamiltonian-style import substitution strategy -- one that rolls back globalization by replacing foreign-made goods in the U.S. market with domestically-produced ones.

"They certainly seem to want to move in that direction," said Dartmouth College Professor Douglas Irwin, who has written in-depth on Hamilton's "Report on the Subject of Manufactures," a seminal policy paper on the promotion of domestic industry that was delivered to Congress in 1791.




The throwback stance has fueled doubts about America's adherence to a strong dollar policy, roiling foreign exchange markets and drawing sharp responses from the leaders of Germany and Japan to Trump administration criticism last week of their currency practices.

The U.S. turn toward economic nationalism has also fanned fears of a replay of the 1930s, when populist governments pursued protectionist and militaristic policies that helped set the stage for World War II.

"We are increasingly concerned about the emerging policies of the Trump administration," billionaire hedge fund manager Ray Dalio and his co-Chief Investment Officer Bob Prince said in Jan. 31 note to Bridgewater

Associates' clients.

## U.S. Criticism

The developing U.S. strategy has manifested itself in Trump's haranguing of companies planning to move production overseas and his threats to slap tariffs on any goods exported back to the U.S. And it's shown up in his administration's willingness to criticize other countries for keeping their currencies too low.

Allianz SE Chief Economic Adviser Mohamed El-Erian calls the Trump program an import-substitution-plus approach that includes industrial policy to help specific sectors, such as automobiles.

While that has echoes to Hamilton, there are big differences, Dartmouth's Irwin said.

Hamilton wanted to make sure the newly-born nation had the capacity to make the weapons it needed to defend itself. And while he did back higher import tariffs, his main focus was on providing subsidies to infant U.S. industries.

Trump's aim is to lift economic growth and turbocharge job creation. The president has emphasized tariffs, rather than subsidies, as the means to that end.

## Immigration Difference

Another big difference: Hamilton is lionized as an immigrant hero in the hit Broadway musical of the same name, while Trump has been criticized for his executive order temporarily barring refugees and nationals from seven Middle Eastern and African nations from entering the U.S.

The most powerful potential weapon in Trump's trade arsenal is one he doesn't directly control and one which the Federal Reserve has more influence over than he does -- the exchange value of the dollar, Irwin said.

In a departure from the strong dollar stance that has been a staple of U.S. administrations since the mid-1990s, Trump and one of his senior economic advisers complained last week about the weakness of the euro and the Japanese yen.

The administration doesn't appear to be respecting the conventions of foreign-exchange diplomacy under which advanced countries refrain from openly criticizing each other, said Stephen Myrow, managing partner at research firm Beacon Policy Advisors LLC in Washington.

## Federal Reserve

Trump also flouted another long-standing dictum during the presidential campaign by sharply criticizing the independent Federal Reserve for being too political.

"They don't know where the usual bounds are, nor do they have any respect for the bounds in a lot of cases," Myrow, a former Treasury official, said about members of the Trump team. "They think the traditional conventions have failed us."

The administration's currency comments triggered ripostes from German Chancellor Angela Merkel and Japanese Prime Minister Shinzo Abe, who denied their nations were gaming the system for their own benefit.

Besides attacking Germany for using a "grossly-undervalued" euro to "exploit" the U.S., Trump trade adviser Peter Navarro also said Washington wants to revamp the global manufacturing supply chain and have more components made in the U.S, the Financial Times newspaper reported on Jan. 31.

## Domestic Content

The brouhaha over exchange rates comes after the U.S. clashed with Mexico over trade, immigration and a wall separating the two countries. Trump wants to renegotiate the North American Free Trade Agreement with Canada and Mexico, with some reports suggesting he'd like to raise the domestic content of goods sold in the U.S. under that accord.

The U.S. quarrel with Mexico, Germany and Japan is seen as a prelude to a bigger battle with China -- a favorite target of Trump and a military adversary, rather than ally, of America. Trump accuses China of manipulating its currency to keep it weak and its exports cheaper.

Paradoxically, Trump is aping a strategy long followed by China in pursuing an America-first approach to trade. Beijing also has been seeking to shorten Asian supply chains and produce more product components internally -- exactly the tactic that Trump is now adopting.

“There is certainly a convergence,” Cornell University professor and former International Monetary Fund economist Eswar Prasad said.

Import substitution strategies have a checkered history. When Latin America and other developing countries tried them in the 1950s and 1960s, “almost all failed and did better when they pulled out,” said Anne Krueger, a former IMF official now at the Johns Hopkins School of Advanced International Studies in Washington. That’s because the system spawned uncompetitive companies and crony-style capitalism, she said.

Even some economists who support such strategies question whether they would work as practiced by Trump. As was the case in post-Revolutionary War America, import substitution is supposed to cultivate nascent industries.

“The idea does not really apply to the U.S., since Trump wants to protect ‘old industries’ -- steel, automotive, garments," Harvard University professor Dani Rodrik said in an e-mail. “So even if he is successful, which I doubt, he will have propped up industries of the past, not the future.”