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Trump Tariffs Ruled Unconstitutional

Trump Administration Announces Alternative Tariffs

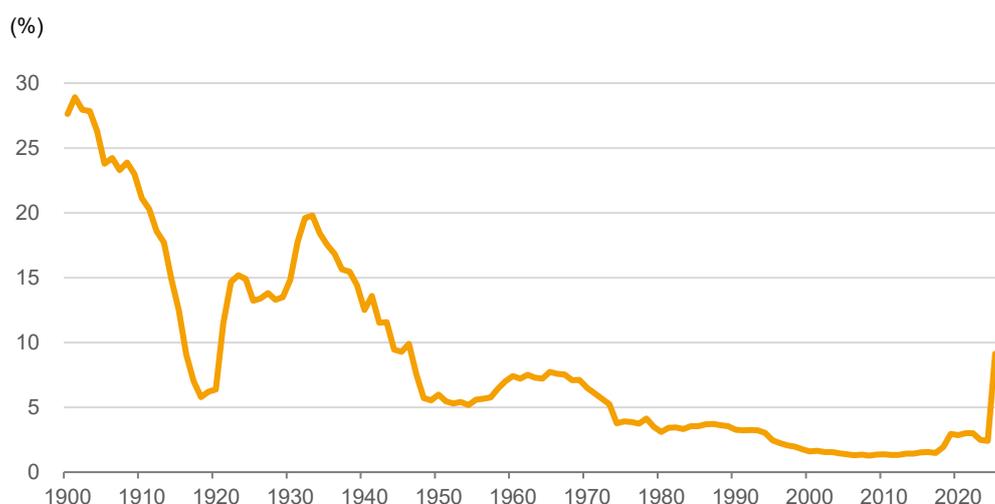
Limited Impact Expected on Japanese Equities

On February 20, the US Supreme Court ruled that tariffs imposed under the International Emergency Economic Powers Act (IEEPA), including reciprocal tariffs and fentanyl-related tariffs, are unconstitutional. The ruling stated, "While IEEPA grants the President economic tools such as import restrictions, it does not grant the authority to impose tariffs. The US Constitution vests the authority to impose tariffs solely in Congress." The Court did not rule on whether tariffs collected to date should be refunded. Sector-specific tariffs on automobiles, steel, and other products imposed under the Trade Act are not affected by this ruling.

In response to the ruling, the Trump administration announced on February 20 that it would impose a 10% tariff on imports under Section 122 of the Trade Act, followed by an announcement on February 21 raising the tariff rate to 15%. Section 122 allows tariffs of up to 15% to be imposed for a maximum of 150 days, with the possibility of extension subject to congressional approval. Although Section 122 has a time limit, it is expected that preparations will be made during this period to rely on other provisions of the Trade Act, such as Sections 232 or 301, allowing tariffs to continue under alternative legal grounds.

If tariffs are eliminated, lower tariff costs would directly benefit corporate earnings. Should previously collected tariffs be refunded, this would also provide an additional boost to earnings. US import prices are expected to decline, easing inflationary pressures and supporting US consumer demand. On the other hand, the loss of tariff revenue could raise concerns about fiscal deterioration, potentially pushing up long-term interest rates. In such a scenario, higher interest rates would pose a headwind to equity valuations, particularly for growth stocks. Nevertheless, we believe that the overall impact on the Japanese equity market is likely to be limited.

US Average Effective Tariff Rate



※Latest confirmed data are as of end-2024; the most recent figures are estimates as of February 21, based on the assumption that tariffs imposed under the IEEPA are abolished and that Section 122 of the Trade Act is introduced and expires after 150 days

Source: The Budget Lab at Yale; Compiled by Daiwa Asset Management

Tariffs on steel, aluminum, and Japan's core industries—automobiles and auto parts—are based on laws separate from the IEEPA, as mentioned earlier, and their tariff rates remain unchanged. Furthermore, reciprocal tariffs are expected to be replaced by alternative provisions such as Section 122 or Section 301. While this ruling may slightly lower the effective US tariff rate, it is unlikely to significantly alter the earnings outlook for Japanese companies. The reaction in the US bond market has been limited, as tariffs will continue to be collected through alternative legal measures. While it is true that tariffs imposed by the Trump administration have served as leverage in negotiations with trading partners, the Japan-US Trade Agreement and the planned \$550 billion investment in the US are expected to remain in place.

From a market perspective, the key point is that the US Supreme Court's unconstitutional ruling and the Trump administration's subsequent response were widely anticipated. As the market had largely priced this in, no significant price movements accompanied the ruling. However, it is true that uncertainty surrounding tariff policy has risen again. Companies may adopt a more wait-and-see stance, potentially leading to stagnation in capital spending and M&A activity. Caution is warranted as this heightened uncertainty could weigh on the stock market. Regarding the refund of tariffs already collected, President Trump has stated he will contest this in court, and we will continue to monitor developments closely .

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