

# US politics and foreign policy

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Chairman  
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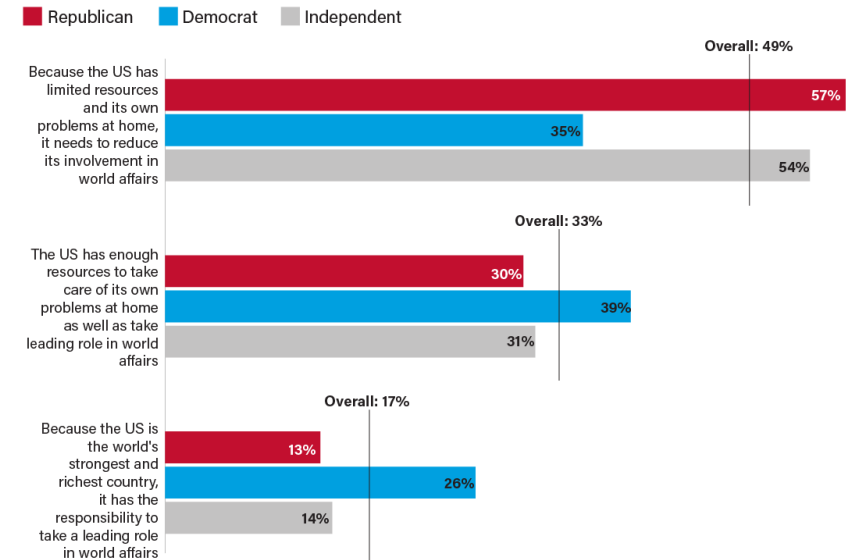
# The global order under Trump—G-Zero wins

- G-Zero world: when no one power or group of powers can drive a global agenda and maintain international order.
  - Endemic leadership deficit is growing critically dangerous. “Geopolitical recession,” or a period of rapidly declining global leadership.
  - The international order is weaker today than at any time since the 1930s.
  - Result of a G-Zero world is every nation for itself; US tariffs extend trend to geoeconomics.
- Main cause is that international institutions no longer reflect the underlying balance of global power:
  - 1) Trump's US; 2) Russia; 3) China; 4) populism.
- Little prospect for renewal of the global order; world faces endemic geopolitical instability and uncertainty.
  - Governance by US, China, Russia.
  - Use of hard power.

## US responsibility in world affairs

Overall, when it comes to maintaining the US role in the world, do you think:

**TOP  
RISKS  
2025**



## US domestic politics—expansion of executive power challenges rule of law

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- Key staff positions have mandate to disrupt the status quo.
- Expansion of executive power will challenge rule of law.



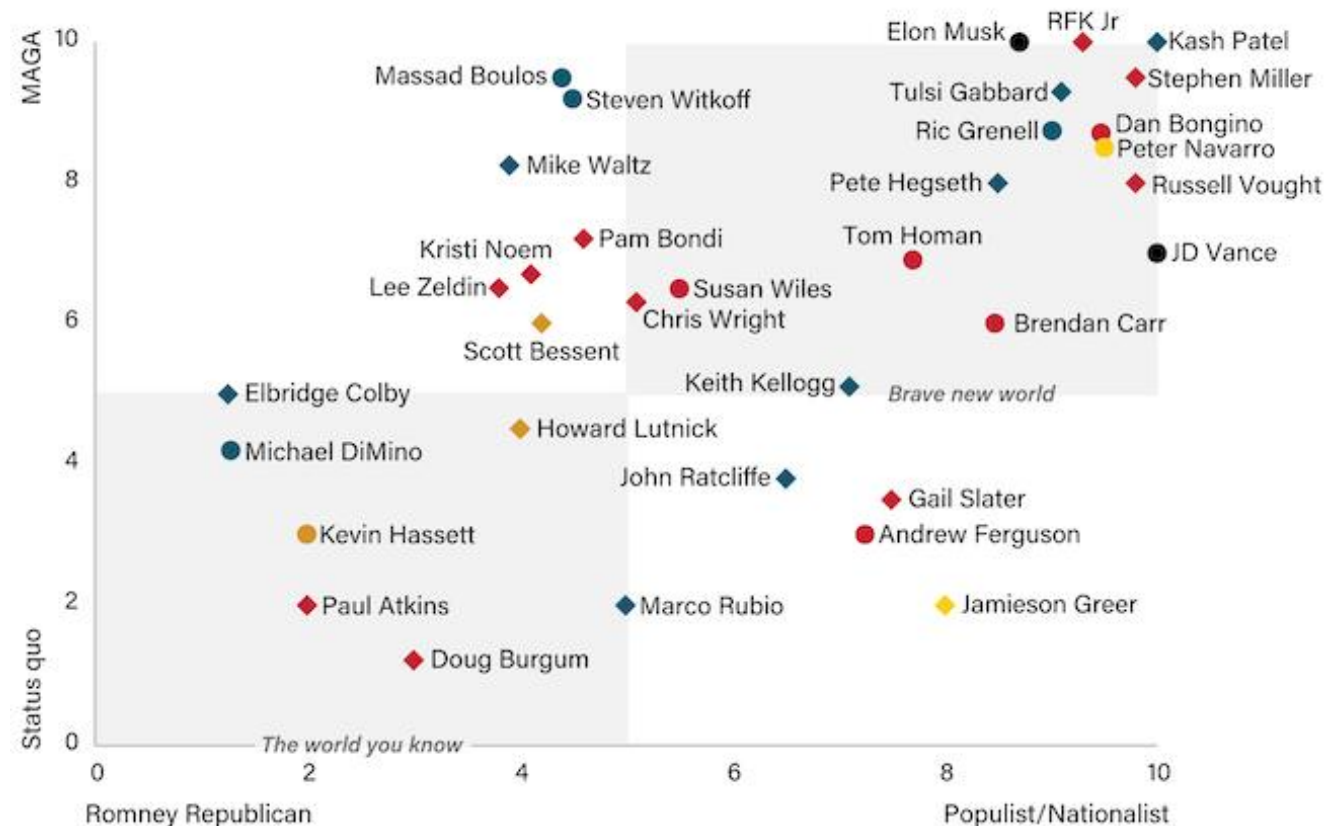
# Trump's key staff positions have a mandate to disrupt the status quo

## Trump nominees span the political spectrum

Trump's top tier of nominees, ranked according to their policy orientation and how disruptive they might be to the status quo

● Not Senate confirmed    ◆ Senate confirmed

Policy area    ● All    ● Domestic    ● Economic    ● Foreign    ● Trade



Note: Scores are Eurasia Group's evaluations of potential Trump nominees; names listed are not exhaustive of the universe of potential nominees.  
Source: Eurasia Group

Nominees reflect a range of ideological proclivities and willingness to disrupt *status quo*.  
*Informal advisors like Laura Loomer have impact.*

# Expansion of executive power is challenging rule of law

- US governance by personalistic rule; much more centralization of power.
  - Weak opposition, invulnerability.
- Trump has pushed the boundaries of the president's powers, violating norms and possibly laws.
  - Norms: Attacks on judiciary and law firms; student arrests; January 6 pardons.
  - Rule of law (possibly illegal): Evasion of court orders on deportations (politically popular); assault on Harvard; impoundment of spending; end birthright citizenship; TikTok law.
- Lower courts have tried to stop, setting up challenges at Supreme Court (Abrego Garcia case).
  - Goal is some form of unitary executive.
  - Courts move slowly; Trump's firehose approach means some borderline EOs will persist.



# Expansion of executive power is challenging rule of law

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- Attempts to silence critics are likely to grow.
  - Lawsuits against media organizations.
  - Viewpoint-based deportations.
  - *Signpost to watch:* Undermining organizations that fundraise for Democratic campaigns.
- Democracy will survive: courts, independent media, federalism, universities.
  - Worst case: competitive authoritarianism.
- Investor risk:
  - If proximity to power yields profits, will undermine US investment climate.
  - Institutional degradation of investment climate increases uncertainty: government contracts, attacks on Fed, erosion of legal protections.



# Trade policy

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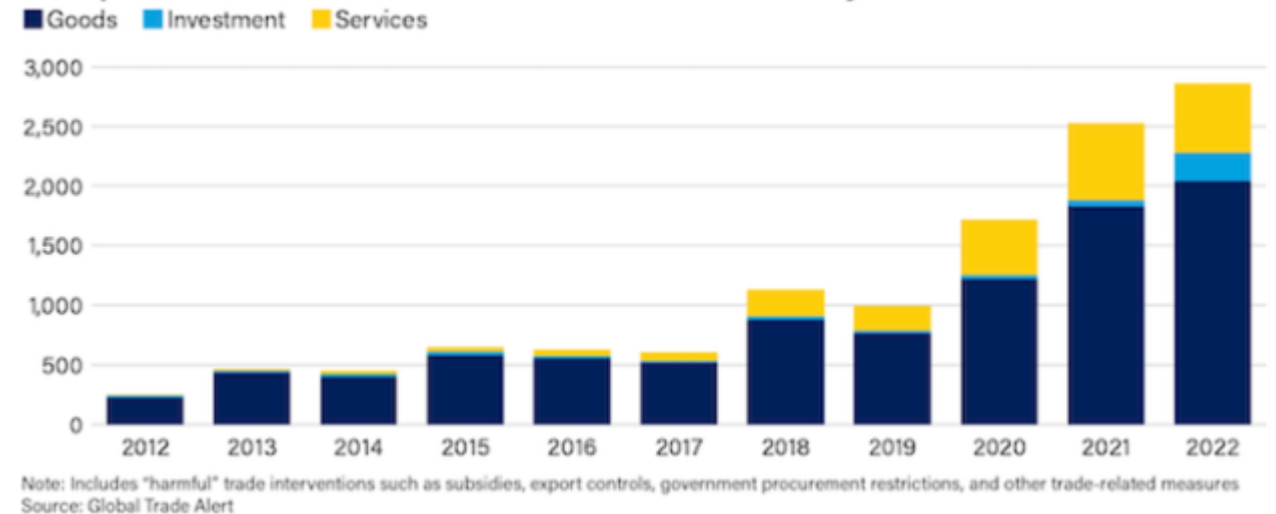
- Liberation Day is inflection point toward new tariff-centric US trade policy.
- Components of US trade policy.
- US average tariff at highest level in a century.
- Stagflation: Tariffs + Immigration.



# From a multilateral international economic system to fragmentation

- Trump's new tariff-based system relies on US market power to compel countries to reduce tariffs and invest in US.
- Tariffs erode trust in US and international system.
- Globalization unwinding: countries will seek to de-risk from China *and the US*.
- Military power, tech power, and trade relationships will preserve some links.
- Headed toward "country-first" policies. Fragmentation and tentative regional/new trading blocs.
- "Strategic incoherence"—policy formulation and implementation lacks coordination.
- Massive uncertainty; inflation, low growth.

New protectionist measures have increased in recent years



# “Tariff wall” is intended to reorient global trade, among other priorities

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## Tariff objectives

- Rebalance bilateral trade deficits.
  - Compel countries to reduce tariffs on US goods.
- Reshore US manufacturing.
  - Move auto industry from Mexico and Canada to lower Great Lakes states and southern states.
- Generate revenue to facilitate tax cuts.
- Combat Chinese overcapacity.
- Achieve foreign policy aims: deportations, increase defence spending, fentanyl (most "deal-able.")
- Groups of tariffs:
  - Country-targeted tariffs.
  - Product-specific tariffs (aluminum and steel, autos, semis, pharma).
- Tariffs motivated by multiple goals.

# Current status of tariffs

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- Trump's 9 April pause on tariffs: 145% on China; 10% floor for most countries; 25% sectoral tariffs with exclusion for electronics; Canada and Mexico remain at 25% except USMCA-compliant goods.
  - Tariffs on semiconductors, drugs, APIs coming.
- Trump reaction function to economic pain: 1) financial system/bond market; 2) stock market; 3) inflation—incumbent killer; 4) job losses among base—large layoffs or plant closings; 5) job approval in low 40% range.
- Viability of reshoring dropped significantly with pause on reciprocals.
- Country-wide Canada and Mexico probably deal-able in context of coming negotiations.
- Sectoral tariffs less deal-able, but US seeks to avoid broad disruptions.
- US entering many bilateral talks on reciprocals; talking with 34 countries this week: 1) South Korea and Japan early deals; 2) EU harder—possible escalation to on US services exports; 3) limited deal on China tariffs likely later this year. Huge downside risk.
- Tariffs highly inflationary; elevated expectations, Fed concerned.

# Record high US tariff level

## US average tariff still at 1909 levels despite electronics exemption

*Average tariff on all US imports (%), historical and current using 2024 volumes*



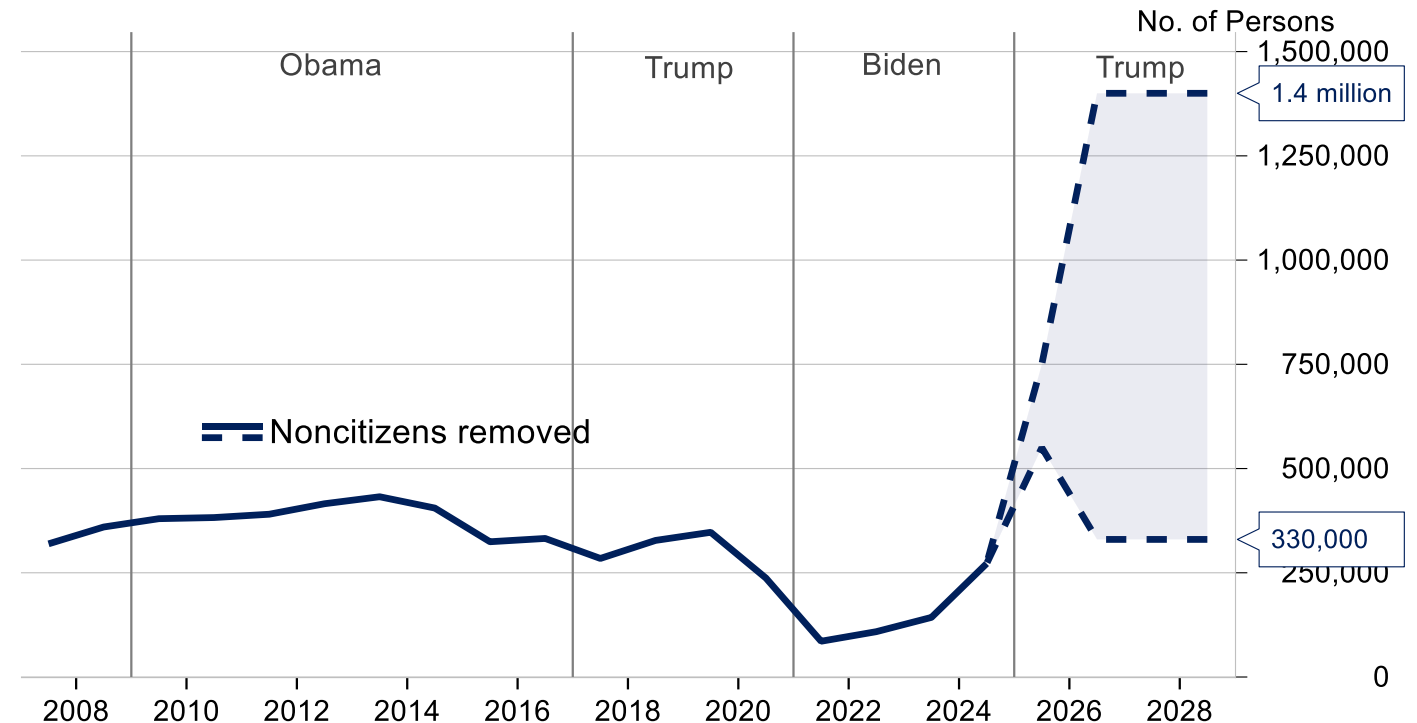
Source: Eurasia Group, Macrobond, Tax Foundation.

Note: Average tariff rate estimate based off 2024 volumes, before import substitution

# Tariffs + immigration policy will have significant stagflationary impacts

- 500,000-700,000 deportations likely this year—not "mass deportations," but still high.
- Rate of deportations will increase after reconciliation bill and new funding; ceiling of 1 million next year.
- Enforcement has led to minimal southern border crossings.
  - Voluntary returns also likely to increase in response to US enforcement.
- Policy will cause labor shortages in ag, construction, hospitality.
- **Tariffs + immigration could cause up to 2% increase in inflation and cut growth by up to 2% over the next year.**

## Trump is looking to at least double migrant removals



Source: Eurasia Group, Macrobond, DHS, BLS

# Fiscal policy

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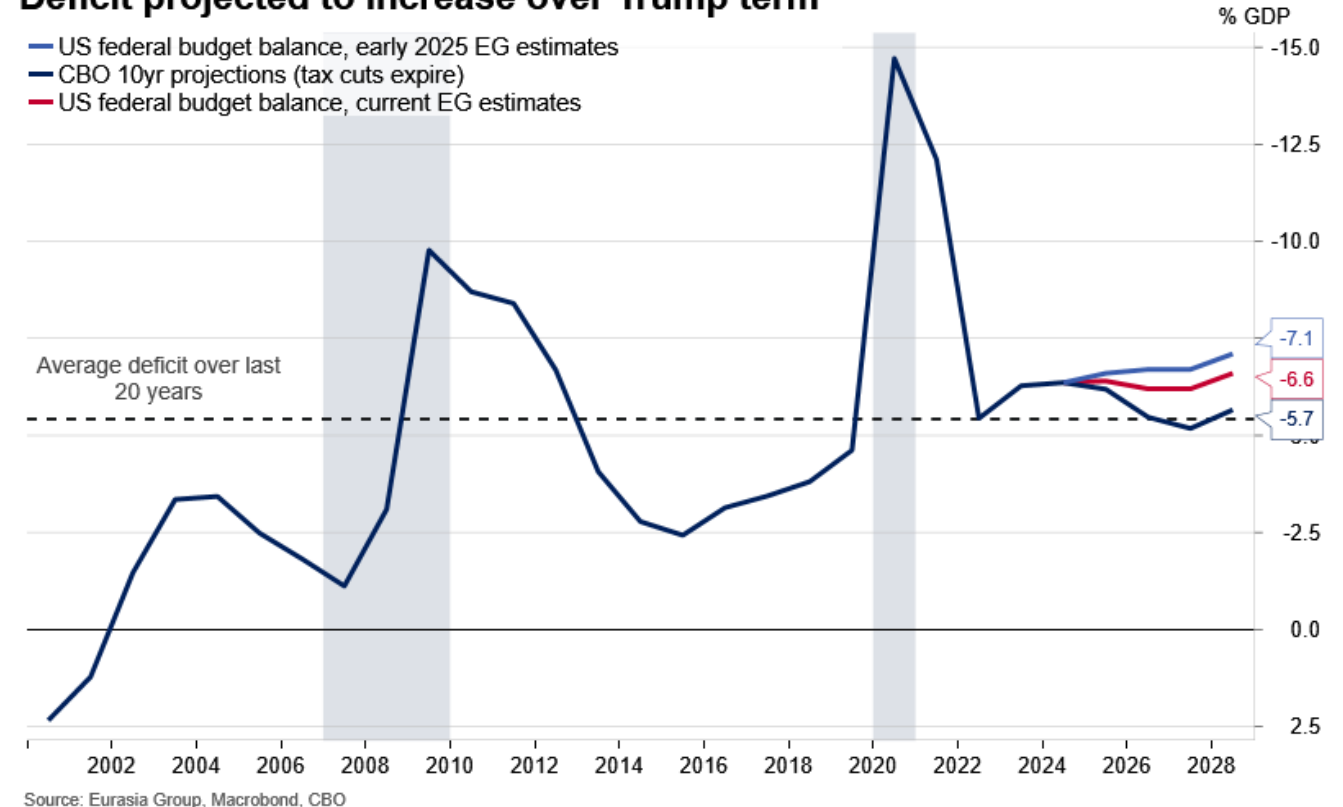
- Deficits likely to rise.
- Reconciliation bill likely to pass mid-year



# Deficits are likely to rise in Trump term

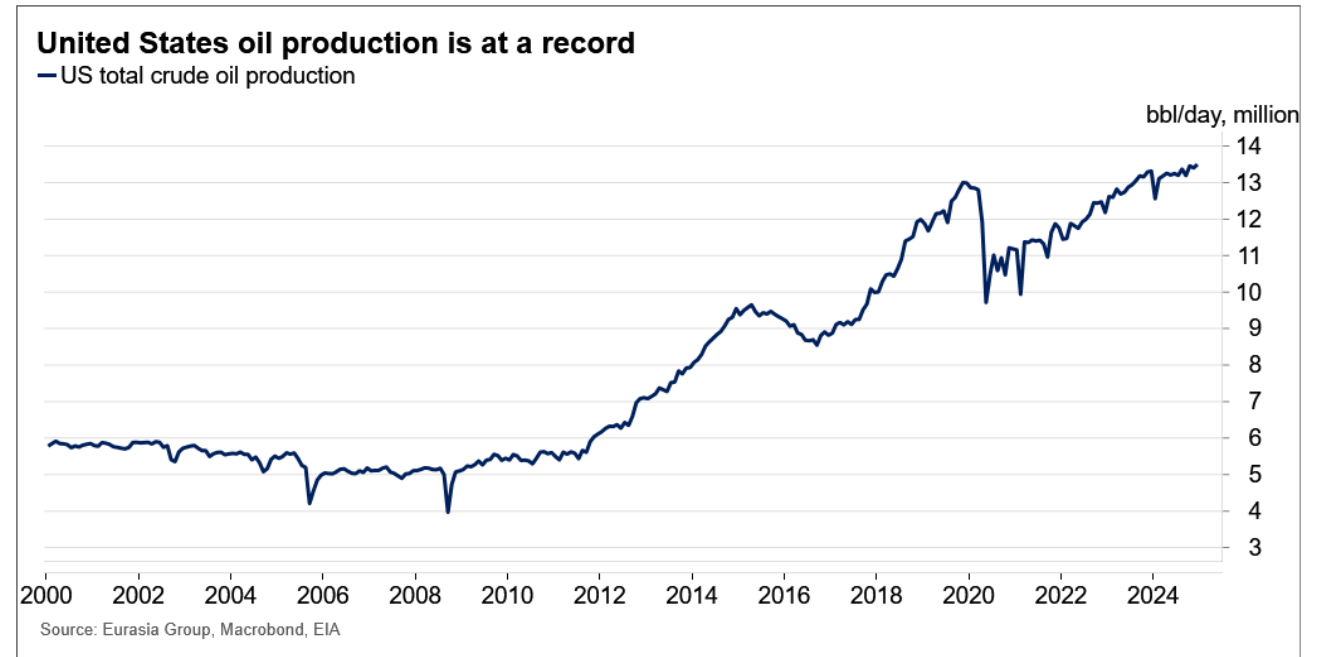
- Expiring tax provisions would add \$4.5 trillion to deficit over 10 years to extend.
  - Cuts to corporate rate unlikely.
  - Tariffs add additional revenue.
  - Additional tax cuts fully offset by IRA cuts.
- House conservatives promised \$1.5 trillion in spending cuts.
  - Requires deep cuts to Medicaid and SNAP.
  - “Big, beautiful” bill likely passes by midyear (70%).
- Tariff revenue + larger cuts contribute to better—though still tough—fiscal situation.
  - Economic downturn would pose serious fiscal challenge.

## Deficit projected to increase over Trump term



# Despite pro-oil agenda, output growth will stall in 2025

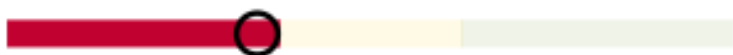
- Republicans will prioritize energy permitting reform in reconciliation process
- Despite pro-growth agenda, tariff uncertainty will undercut "drill baby, drill."
  - Trump has moved to support oil and gas industry:
    - Reversing ban on new LNG export terminals.
    - Opening up Arctic to drilling.
    - Expanding lease sales in the Gulf of Mexico.
- But low prices and uncertainty from tariffs will suppress US oil output growth for the year.
  - US oil production likely to stagnate at current level of 13.4 million bpd or fall slightly year on year.



# US short- and long-term political trajectory now negative

Short-term trajectory (6 months):

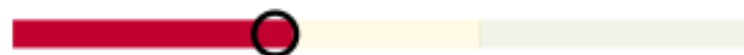
**Negative**      Neutral      Positive



- Disruption from tariffs and labor shortages will stoke inflation and reduce growth.
- Personalist presidency and tariffs will keep uncertainty very high throughout 2025.
- No short-run push from deregulation and tax cuts as they fall short of campaign promises.
- Increasing pressure on Fed to cut rates. Powell will resist near-term.
  - But recession now basecase; 2 rate cuts likely as Fed shifts to a focus on growth.

Long-term trajectory (24 months):

**Negative**      Neutral      Positive



- Concerns about rule of law and investable environment in US grow as government behaves more like an EM.
  - Modest drift away from dollar.
- Massive uncertainty persists—impairs growth and scrambles supply chains in US.
  - Trade partners hedge and unwind.
- Fiscal policy unlikely to be supportive while Treasury issuance remains high.
- Deregulation and tax reform unlikely to be strong enough tailwind to overcome policy-related headwinds

# Foreign policy

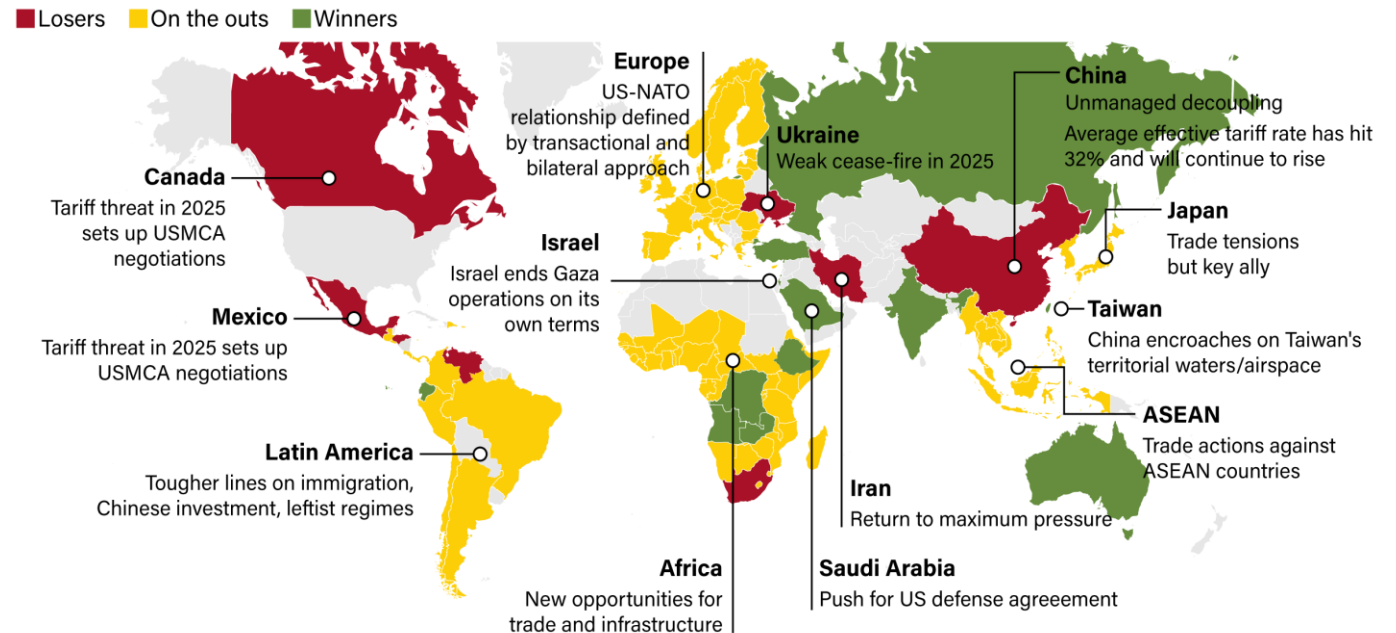
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- Trump foreign policy.
- US-China relations.
- Transatlantic relations: The war in Ukraine and Europe.
- US-Iran relations.
- US-Canada relations: what Trump wants, the tariffs, the future of USMCA.



# US foreign policy under Trump

- Trump opposition to alliances and international institutions puts G-Zero on jet skis.
- Muscular unilateralism.
  - The United States is comparatively stronger today relative to 2017, relative to both adversaries and allies.
- Trump is transactional and deal oriented.
  - Transactional with the strong (China, Russia); predatory with the weak (Ukraine, Mexico, Canada).
- Tariffs replace multilateralism as the primary vehicle of policy.
- More "strategic incoherence": Signal-gate.



# US foreign policy under Trump

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- US policy toward Western Hemisphere.
  - Top foreign policy priority is Latin America.
  - Streak of Monroe Doctrine in US policy.
    - China in LATAM, the Canal.
    - Mexico/border security/USMCA on a par with China as a foreign policy priority.
  - Conceives of US-Canada border as an "artificial line." Seeks:
    - 1) access to resources and market;
    - 2) more influence over Canadian Arctic sea lanes;
    - 3) increased defense spending.



Trump meets El Salvador President Nayib Bukele in the Oval Office, 14 April 2025.

# US-China breakdown: Maximum Xi vs Maximum Don

## Painful Truce:

- Bessent/Trump signal lower tariffs as current rates would surpass US pain threshold. But slow process.
- China wants a deal; won't initiate talks.
- Appointment of Bessent or other confidante.
- Applied average rates of 40-65%; exclusions focus on consumer goods; two-tiered; will begin in April or May.

## Full-scale decoupling:

- Trump pain threshold higher; China unlikely to retreat from perceived extremely aggressive Trump policy.
- Has prepared for decoupling for years.
- Would move up escalatory ladder; already signaled ordinary US companies at risk; CM export controls.
- Average applied over 65%.

## Military Crisis – inadvertent escalation

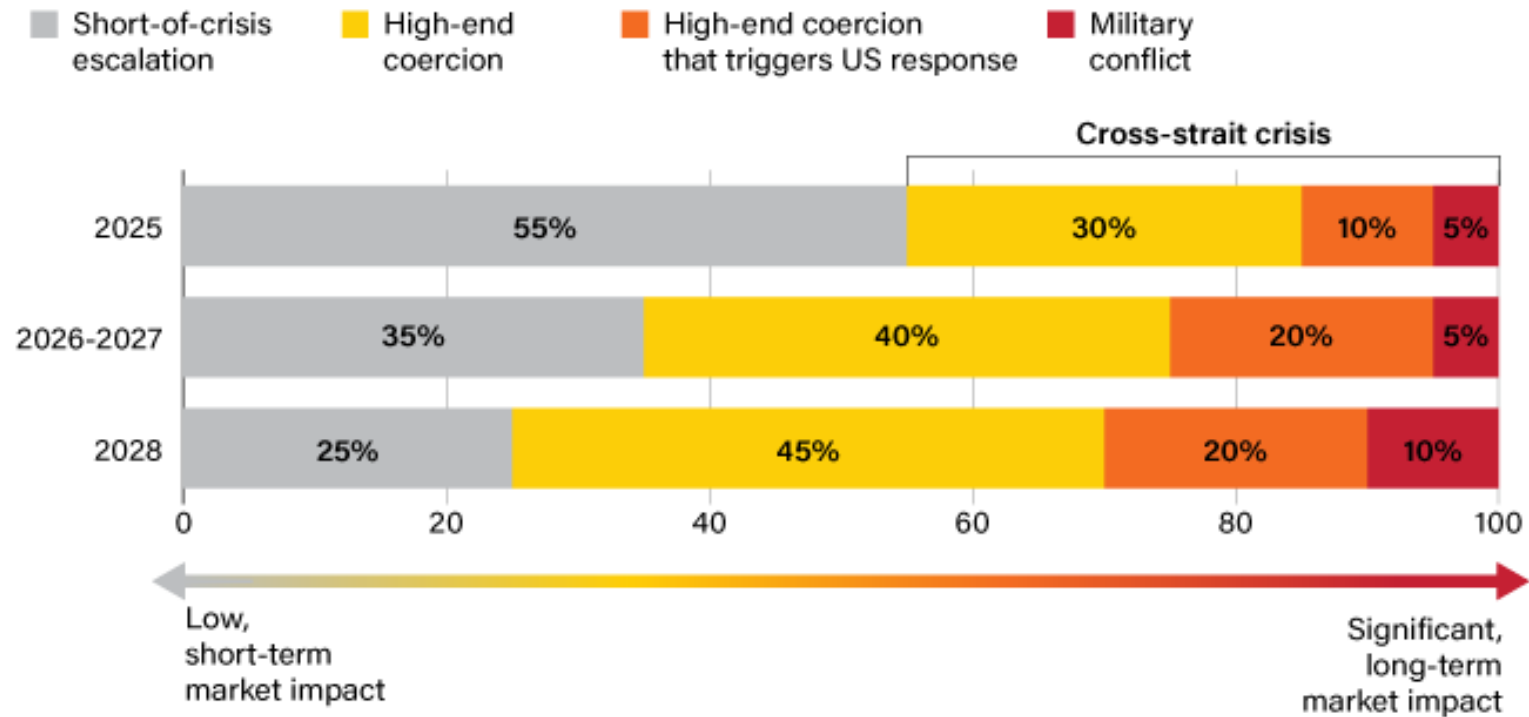
- Implication of current events

## Updated scenarios for US-China relations through mid-2025

|                                |  |
|--------------------------------|--|
| 1. Painful truce (55%)         | <ul style="list-style-type: none"><li>• Economic and political pressure force Trump to back down on tariffs, allowing both sides to roll back tariff hikes</li><li>• Diplomatic efforts allow for the establishment of working-level channels</li><li>• Negotiation of key issues pushed beyond 2025</li></ul>       |
| 2. Full-scale decoupling (35%) | <ul style="list-style-type: none"><li>• Diplomatic efforts break down</li><li>• Tariffs remain at high levels through 2025</li><li>• Other countries get deals involving tariffs or restrictions on China</li></ul>  |
| 3. Military crisis (10%)       | <ul style="list-style-type: none"><li>• The US intensifies military activities and cooperation in Asia or changes support for Taiwan (or Beijing perceives it is doing so)</li><li>• An aerial collision leads to heightened People's Liberation Army readiness in the absence of a communications channel</li></ul> |

# Taiwan—Cross-strait crisis unlikely in 2025, invasion risk very low

## Taiwan Strait risk scenarios and probabilities



- Tech Cold War, threats to CCP legitimacy, Taiwan.
- China military exercises off Taiwan in early April shows limited patience.
- Tail risk with moderate to significant, long-term market impact at 15% in 2025, 25% in 2026-27, 30% in 2028.
- Near-term efforts at dialogue (e.g., Trump-Xi call) not a long-term cure.
- A key mitigating variable is how long Xi's concerns with the economy distract him.

# Transatlantic relations: Russia-Ukraine war

- Putin unwilling to give Trump quick win; hewing to maximalist line: Ukrainian neutrality, limits on the size of and assistance to the Ukrainian Army; recognition of conquered land as part of Russia; conditions for Black Sea ceasefire.
- Russia has had continued success enlisting roughly 30,000 contract soldiers per month.
- Ukraine's use of drones improves prospects.
- Big picture is that the war will continue in some form as long as Putin leads Russia.
  - Model is Kashmir. Frozen conflict to hot war.
- Heavily armed line dividing Europe from Arctic to Black Sea. Ukrainian reconstruction will be difficult.
  - Tail risks to energy and grain markets.

## Scenarios until 7 July 2025

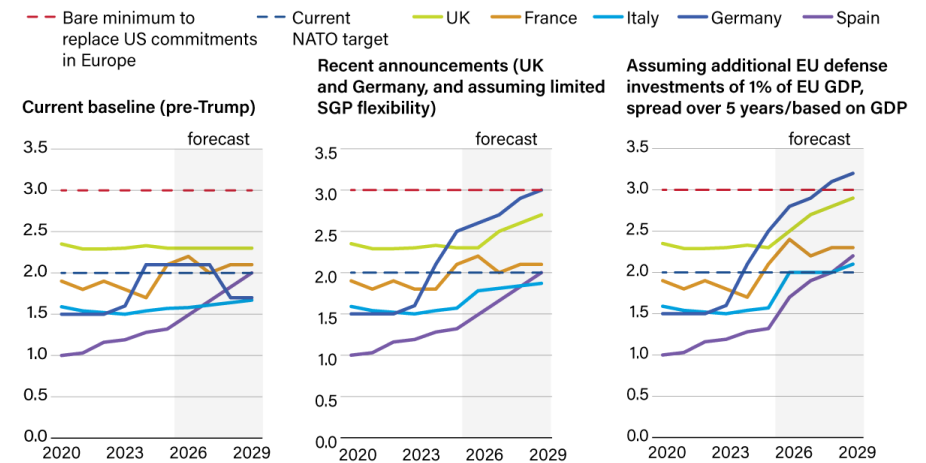
| Scenarios                    | Description   | Probability |
|------------------------------|---|-------------|
| US/Russia vs. Ukraine/Europe | The US and Russia conclude security and economic normalization agreements and a full cease-fire proposal. Ukraine and Europe reject the cease-fire terms. Any partial, temporary truce collapses within this timeframe. Ukraine defends against a Russian offensive with European military aid but without US support. The US agrees to a limited troop withdrawal from Europe. The US halts some sanctions enforcement against Russia; the EU and others do not. | 60%         |
| No Trump-Putin deal          | The US and Russia fail to reach any agreements. Russia launches an offensive; Ukraine defends with military aid from the US and Europe. The US and the EU do not ease sanctions.  | 30%         |
| Cease-fire takes hold        | The US and Russia conclude bilateral agreements and a cease-fire proposal that Ukraine and Europe accept. The deal is fragile but holds, and peace negotiations start. The US makes multiple security concessions to Russia, including on troop withdrawals. US sanctions easing covers a wider range of strictures. EU sanctions remain in place.  | 10%         |

Source: Eurasia Group

# Transatlantic relations: NATO

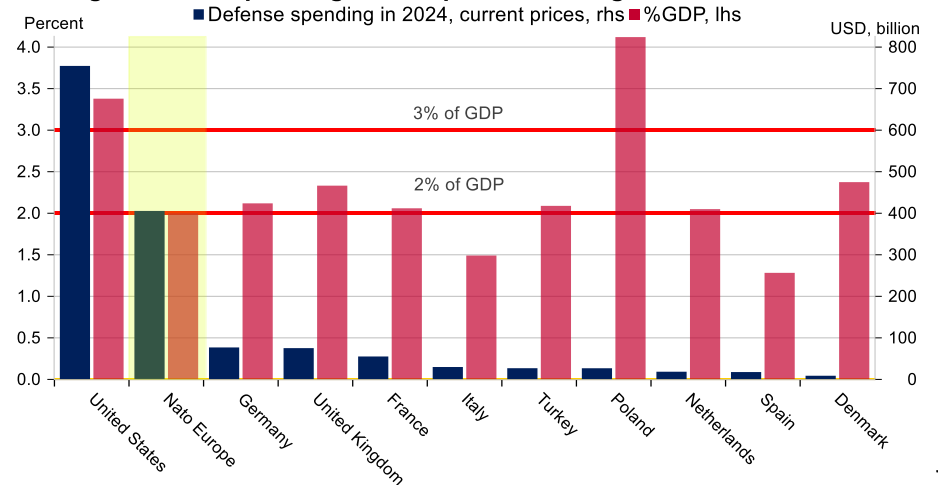
- US driving tensions with Europe. European leaders seeking to de-risk and build more autonomy.
- US will retrench and wants Europe (and Canada) to pay.
- EU taking on bigger role in common funding for defense—€150 bn in loans for European nations.
  - Canada can sell arms and participate in joint procurement, if it acquires EU partnership status.
- European nation-states increasing defense spending, especially Germany and the UK.
  - NATO is cornerstone of Canadian defense; "laggard" argument could grow stronger.
- Canada: Opportunity to hedge as part of European defense procurement. But geography makes hedging hard.
  - Will be difficult to diversify while maintaining interoperability with US and gaining it with Europe.

## EU defense spending



Source: NATO, national legislation, IMF, Eurasia Group

## Average defense spending of European NATO lags US



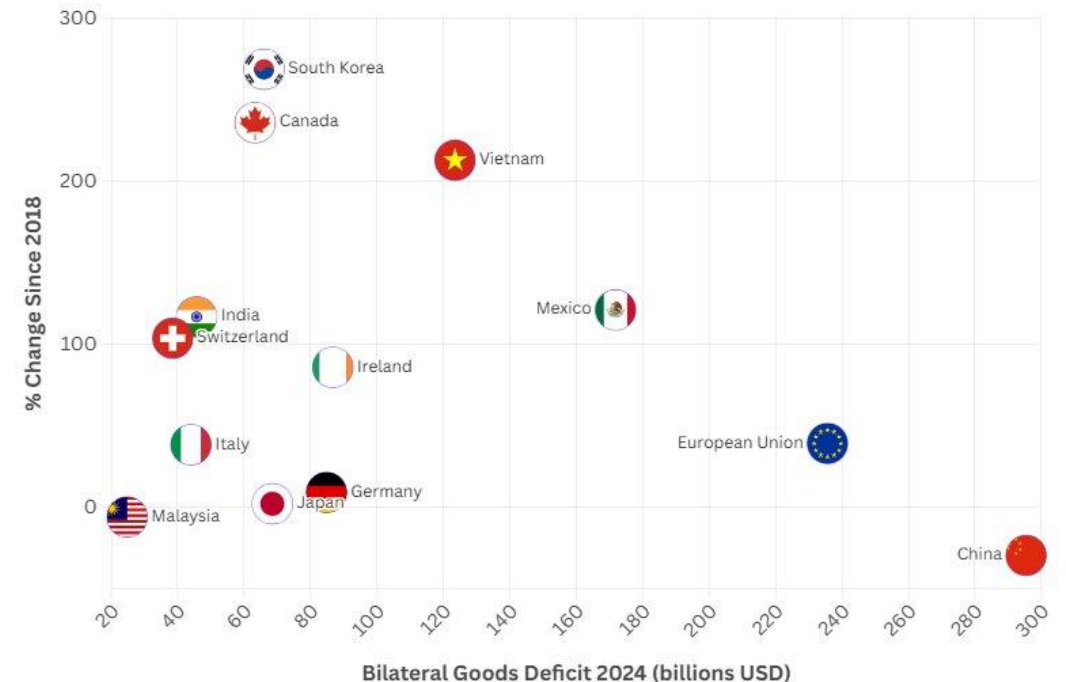
Notes/Source: Select NATO members. Eurasia Group, Macrobond, NATO.

# US-Canada

- What does Trump want – 51<sup>st</sup> state or market access?
  - Market access: dairy, banking, resources—including critical minerals
  - More defense spending: US subsidizing Canadian defense.
    - Canada's 1.4% of GDP spend makes it a target.
  - Influence over Canadian Arctic.
  - 51<sup>st</sup> state threats fit expansionist agenda (Greenland, Panama Canal) – but more to needle Trudeau.
  - Probably favors Poilievre over Carney due to closer political alignment.
- What are the goals of tariffs on Canada?
  - Threat of tariffs will remain through 2025, at least until USMCA resolution.
  - 25% across-the-board except USMCA-compliant mostly in service of market access, leverage in upcoming negotiations.
  - 25% steel, aluminum, autos – leverage + reshoring auto sector/manufacturing + combating Chinese overcapacity.

## 2024 U.S. Bilateral Goods Deficit and Change Since 2018

Supply Chain Diversification and Rising Deficits: Potential Targets under Trump 2.0



Source: Eurasia Group, [US Census](#)

# USMCA outlook

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- Scenario 1: Zombie USMCA (45%)
  - Both 25% sector-specific and country-wide tariffs the subject of bilateral negotiations that yield small reductions; tariff threats continue.
  - Current agreement and structure remain, USMCA-compliant goods retain status; subject to annual reviews, maximum US leverage.
  - USMCA punted to next US administration in 2029.
- Scenario 2: Weak USMCA 2.0 (30%)
  - USMCA renegotiated: restrictions on Chinese investments; rules of origin tightened; protection for US manufacturing.
  - Sector-specific and country-wide tariffs resolved at a common and lower level through trilateral diplomacy.
  - Treaty extended to 2042.
- Scenario 3: Trade war (15%)
  - No successful negotiation on sector tariffs, which leads to retaliation from Mexico and Canada and higher tariffs from US.
  - Blow up of USMCA potentially leads to separate trade deals.
- Scenario 4: Fortress North America (10%)
  - Renegotiation leads to deeper integration, with tariff levels close to full reversion.
  - Concessions from Canada and Mexico combined with US decoupling from China, Europe.

# Tips for CEOs

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- Pause large investments in the US because uncertainty will remain high for the foreseeable future.
  - Tariff levels.
  - US investment climate.
- Hedge US exposure where possible.
- Form a view on the extent to which the tariffs and other policies result from Trump policies (time bound) or tectonic plate shifts in US politics (more permanent).
- Placate the Trump administration where possible but push back privately and firmly when a demand is not feasible.
- Safety in numbers. Seek collective strategies to enhance effectiveness but reserve tactic for critical matters.
- Avoid large new exposures in China; tempting as a hedging strategy but given US-China tensions, risk of crossing Trump administration is too high.
- Neither Russia nor Ukraine will likely be investable over the medium term.



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