

Trump must 'get real on trade'

US trade deficit is 'made in America'

by Steve Hanke in Baltimore

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In March two stunning economic headlines were printed in the US press. The first appeared in the Wall Street Journal: 'US budget gap widened 77% in first four months of fiscal year.' The second, from Bloomberg, read: 'US trade gap surged to \$621bn in 2018, 10-year high.'

President Donald Trump and his team of protectionists must learn that these two headlines are interconnected. If the government runs a big fiscal deficit, the US will run a big trade deficit. Alas, this fact has never crossed the president's mind.

Trump, and most in his administration, believes the deficit is a 'bad' thing caused by foreigners who engage in unfair trade practices. For them, the solution is US-imposed tariffs and other anti-trade measures. But these will not change the overall US trade balance.

The trade deficit is equal to the excess of private sector investment minus savings, plus government spending minus tax revenue. So, the counterpart of the trade deficit is the sum of the private sector deficit and the government deficit (federal plus state and local). The US trade deficit, therefore, is the mirror image of what is happening in the US domestic economy. If expenditures in the US exceed the incomes produced, which they do, the excess expenditures will be met by an excess of imports over exports (a trade deficit).

Between 1975-2016 the US accrued a cumulative trade deficit of around \$11.2tn, and the total investment minus savings deficit is around \$10.4tn.

Trump can bully countries he identifies as unfair traders, and he can impose all the restrictions that his heart desires on trading partners, but it won't change the trade balance. Never mind the fact that most economists think the president's ideas on trade are rubbish. When it comes to trade, Trump is the master of the message and the optics. In consequence, his base is with him on trade, and so are a surprising number of others.

The problem is that Trump's trade prattle is tailor-made for delivery on Twitter and television. Those media outlets are suitable for 'sound bites', not complex arguments and data points.

That is why economics is at a disadvantage. Nevertheless, this is what economics has to say about the trade deficit bugaboo. First, it is not a 'problem'. The US has run a trade deficit every year since 1976, and has done relatively well since then. Second, the trade deficit is not made by foreigners who engage in unfair trade practices; it is homegrown, made in America. To the extent that domestic savings in the US falls short of domestic investments, the economy must import more than its exports, resulting in a negative trade balance.

The administration's fiscal policies will continue to complicate Trump's approach to trade. If his fiscal deficits are not offset by an increase in private savings relative to private investment, increases in the federal deficit will translate into larger trade deficits. So the trade deficit will be not only homegrown, it will be made by Trump himself. It's time for the president to connect the dots and get real on trade.

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