President Trump's 'Secret Plan' To Grow The Trade Deficit

forbes.com/sites/phillevy/2018/08/13/president-trumps-secret-plan-to-grow-the-trade-deficit

Phil Levy

August 13, 2018

I am Senior Fellow on the Global Economy at the Chicago Council on Global Affairs, and teach International Business Strategy at Northwestern University's Kellogg School of Management. I have previously been Senior Economist for Trade for President George W. Bush's Council of Economic Advisers and handled international economic issues for Secretary of State Condoleeza Rice's Policy Planning Staff.

Zhang Peng/LightRocket via Getty Images

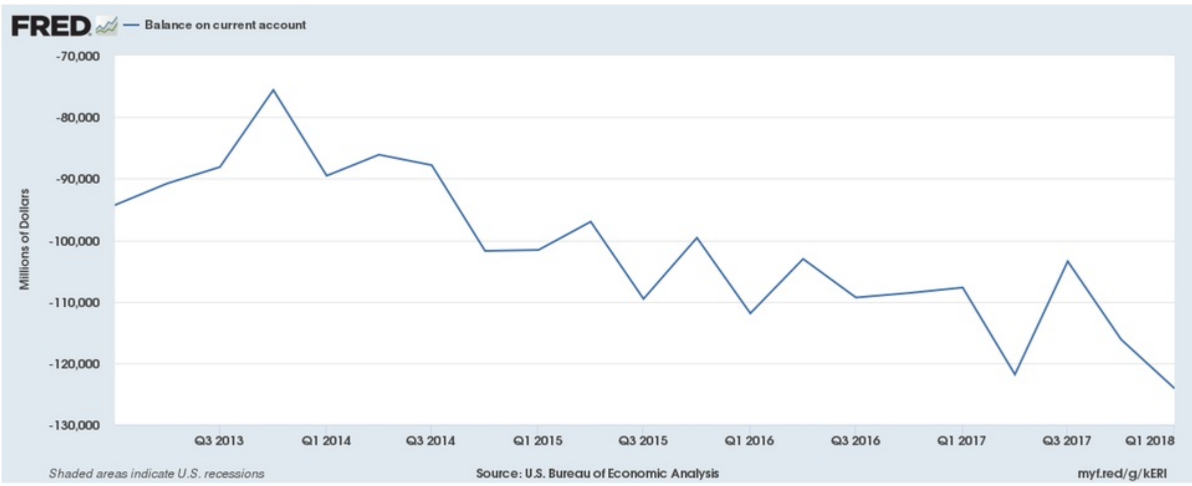
President Trump has repeatedly denounced trade deficits. He treats them as national balance sheet losses and promises to eradicate them wherever he can, mostly through an aggressive trade policy. But what if this were an elaborate ruse? What if his true objective were to grow the trade deficit as much as he could?

Paradoxically, his current course of action seems bound to have that effect.

If there were a three-part plan to increase the trade deficit, the first part would attempt to boost investment in the United States while trimming national saving. The U.S. trade deficit (more accurately, current account deficit) is equal to the gap between national savings and investment. That relationship is an accounting identity, not a theory. To boost investment, the President could restructure the tax code to increase incentives for corporations to invest at home. Cutting saving would be even easier; national saving is household and corporate and government saving combined. The trick to expanding the trade deficit would be to make sure that federal budget deficits increase. Unless there is an offsetting move in other domestic saving, this should cut national saving. The combination of investment incentives and government dissaving would be a strong start toward growing the trade deficit.

The second part of the plan would be to undercut growth in major trading partner economies. When economies are growing strongly, citizens and businesses tend to consume more of everything – both domestically-produced goods and imported goods. The flip side of this is that, when economies falter, they cut back on everything, including their imports. Other things equal, a plunge in one's own economy will shrink a trade deficit while a drop in a major trading partner's economy will grow the deficit. We saw this in the global financial crisis a decade ago, when the U.S. trade deficit shrank impressively. Back to the plan –the trick would be to instill doubt and foster economic turmoil in partners such as the European Union and China. If the United States could effectively destabilize those economies, U.S. exports should fall. If you pair that with rapid U.S. growth, it should also grow the U.S. trade deficit.

The third and final element would be to try and stoke a currency crisis of some sort. Perhaps find an emerging market that is teetering and see if you can push it over the edge. Not only will this directly affect trade with the target country – as its currency falls, its goods look cheaper for the United States to import and U.S. goods look more expensive for export – but there is a chance of contagion, in which other emerging markets see their currencies fall as well. Frequently, amid international financial panics, investors seek haven in U.S. Treasury bonds, thereby bidding up the value of the dollar more generally. This would complement the other strategies to boost the trade deficit, as a strong dollar makes life more difficult for U.S. exporters.



U.S. Bureau of Economic Analysis, Balance on current account [IEABC], retrieved from FRED, Federal Reserve Bank of St. Louis; https://fred.stlouisfed.org/series/IEABC, August 13, 2018.St. Louis Federal Reserve, FRED

In reality, there is (probably) no secret Trump plan to explode the trade deficit. The actions are more likely just a series of policy errors attributable to inexperience and the absence of a sensible strategy. But if there *were* a secret plan to blow up the trade deficit, it would look a lot like current U.S. policy.