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Trump rails against trade deficit, but economists say there's no easy way for him to make it go away

By Ana Swanson March 7 at 5:01 PM

The Trump administration has railed against the trade deficit as evidence that America no longer wins. President Trump and his trade advisers have described the metric, the sum of what the U.S. exports minus what it imports, as the result of failed trade deals and promised to shrink it.

But as Trump navigates his second month in office, the prospect of significantly reducing the trade deficit looks remote.

Data released Tuesday showed the U.S. trade deficit swelling to its largest volume in nearly five years. The trade deficit rose to $48.5 billion in January, widening from $44.3 billion in December as the growth of imports outpaced that of exports. Economists say that, barring dramatic action from the Trump administration that could hurt the economy, the figure is probably set to continue increasing.

The U.S. economy is performing better than many other economies around the world, said Eswar Prasad, a senior professor of trade policy at Cornell University. That means that U.S. consumers have the ability to buy goods from abroad but consumers abroad are unlikely to buy much from the United States, a dynamic that increases the trade deficit.

In addition, the prospect of the Federal Reserve hiking interest rates, perhaps as soon as mid-March, is likely to attract more global investment to the United States, Prasad said. That would drive up the value of the dollar, which would make imports seem relatively cheap for U.S. consumers.

“Left to itself, the trade deficit would probably rise, simply because the U.S. economy is doing a lot better than most of its trading partners,” Prasad said.

Trump's own policies, such as a tax cut for individuals and corporations, could also encourage the trade deficit to rise, said Stan Veuger, a resident scholar at the American Enterprise Institute. Such policies would probably boost growth and attract foreign investment into the United States — factors that would push up the value of the dollar and boost the trade deficit.

In fact, economists say that one of the only ways the Trump administration could reliably reduce the trade deficit is by derailing trade itself. If the Trump administration enacts tariffs and other tough barriers to trade, that could potentially spark a trade war and cause imports and exports to fall. But in the process, the administration could also trigger a slowdown in the economy.

At a conference Monday morning in Washington, Peter Navarro, the director of Trump’s National Trade Council, reiterated the administration’s focus on the trade deficit. The Trump administration policy is one of “free and fair and truly reciprocal trade that begins and ends with the belief that bilateral trade deficits do indeed matter,” he said.

“Trade deficits not only matter when it comes to jobs and growth and national security, they matter a great deal,” Navarro said.

Many economists disagree with this claim, saying that the factors behind the trade balance can be complex — and that the trade deficit is far from the best economic metric for policymakers to target.

In January, for example, the increase in the deficit was a sign that the U.S. economy was doing well, said Fotios Raptis, a senior economist at TD Economics. Combined with a strong dollar, rebounding consumer demand drove

American shoppers to purchase more imports in the month. Imports of capital goods — products such as machinery that are not sold to consumers but are used to make other goods — also grew, suggesting U.S. businesses are responding to a better economy by investing and expanding, Raptis said.

In Raptis's estimates, the larger trade deficit could weigh on U.S. gross domestic product, a broad measure of economic growth, by 0.1 or 0.2 percentage points this year. That a trade deficit reduces economic growth is also central to the argument of Navarro, Trump and others in the administration.

Economists say the administration is correct in arguing that a larger trade deficit lowers GDP. But economists are quick to point out that the trade deficit doesn't actually reduce economic activity in such a clear, causal way — it's a product of the way GDP is calculated, not one of cause and effect.

GDP is the dollar value of everything a country produces. To calculate it, economists add up everything that households consume, add in business investment, government spending and exports, and then subtract the value of imports, which are obviously not produced inside the borders. In effect, this means that the more stuff Americans buy from abroad, the smaller GDP gets.

So imports reduce a country's GDP in an accounting sense, but that doesn't mean they necessarily *cause* GDP to be smaller, as economists from the University of Wisconsin at Madison and Tufts University have argued.

For example, if Americans feel poorer, they might buy less stuff from abroad. Imports and the trade deficit could fall. As many economists point out, the United States had a trade surplus during the Great Depression.

"By not consuming things that come from abroad, we don't automatically get to produce more," Veuger said.

Conversely, if Americans feel richer, they could buy more stuff from abroad, pushing up the trade deficit — which is what appeared to happen in the United States in January.

In an interview Monday, Angus Deaton, who won the Nobel Prize for economics in 2015, called the administration's attitude on trade deficits "an old-fashioned mercantilist position."

"If you stand on a platform, it makes you six inches taller," he said. "It's a ridiculous argument."