Discussion of:

The U.S. Trade Deficit: Myths and Realities

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Brookings Papers on Economic Activity

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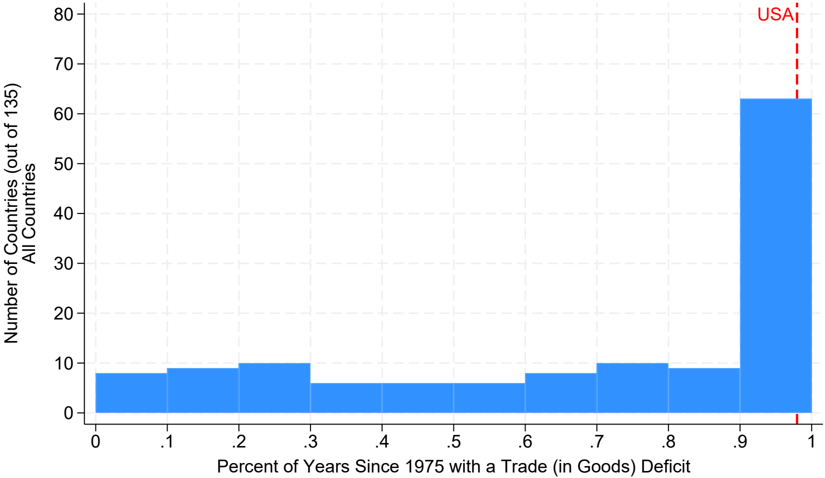
4. **Trump's motivations and policies to reduce deficit**

1) How unusual is persistence of U.S. deficit?



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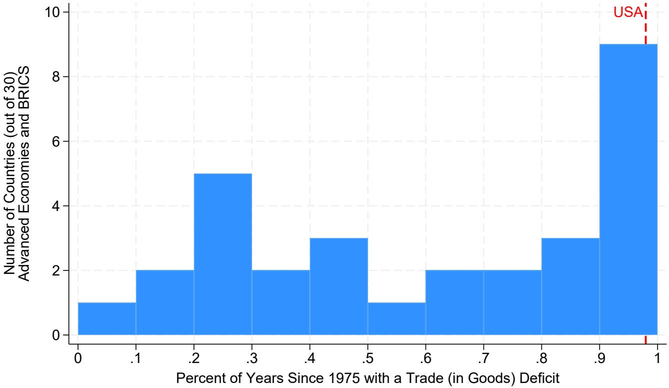

- Countries like India/UK also (almost) always run deficits
- Countires like China/Netherlands/Switzerland run surpluses

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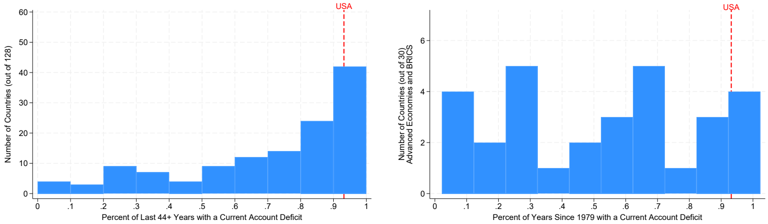

- Same point holds for current account deficits
- Goods and services would be better (tougher to get)

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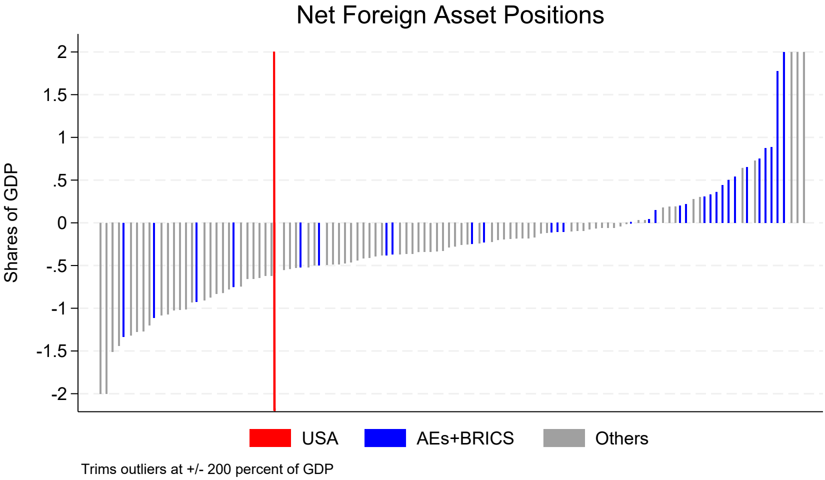
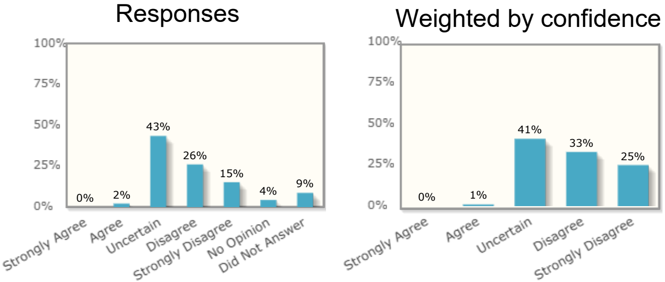


2) Should we be confident that tariffs won't reduce deficit?

- Quote from paper: "...are not major causes of the U.S. trade deficit, which will not respond strongly to new tariffs."
- Chicago Booth Clark Center survey:

  Matching US import tariffs to the tariffs, value-added taxes and non-tariff barriers imposed on US goods by other countries would substantially reduce the US trade deficit.



- Numerous Op-Eds: "Deficits reflect S/I, so are unaffected..."

2) Should we be confident that tariffs won't reduce deficit?

- I fully agree with paper's – and broader profession's – views on large costs of tariffs and suboptimality for this purpose.

- But, I'm *much less confident* that tariffs can't at least moderately reduce the deficit. How? Obstfeld-Rogoff (2000)!

- Just as with intratemporal trade, tariffs make intertemporal trade more expensive. Quantitative treatments?:
  - Reyes Heroles (2016)
  - Alessandria and Choi (JIE 2021)
  - Eaton, Kortum, Neiman (JEDC 2016)

- Also, role of uncertainty on U.S. investment?

2) Should we be confident that tariffs won't reduce deficit?

- What does argument on other side look like?
  - Quantitatively small?
  - Empirical evidence?

- More compelling is Lorenzoni (2019). Alternative to intertemporal approach, tariffs will not necessarily reduce deficits if they compensate for liquidity services. But requires:
  - Tariff changes are permanent
  - U.S. supply of liquidity (i.e. role of USD) is stable
  - There is full retailiation
  - Wealth effects are small

3) Lessons from Plaza for depreciation / Mar-a-Lago?

- From Paper: "Exchange rate effects are likely to be short-lived unless the promised changes in macroeconomic fundamentals are forthcoming."
- International Finance 101: You can manage the NER, but not the RER (over the long run).
- So I looked again at Plaza. Persistent effects could be:
  - Pre-Plaza NER was out of whack with fundamentals
  - Post-Plaza G5 coordinated on fiscal/structural
  - Issue with model – e.g. lags are a lot longer

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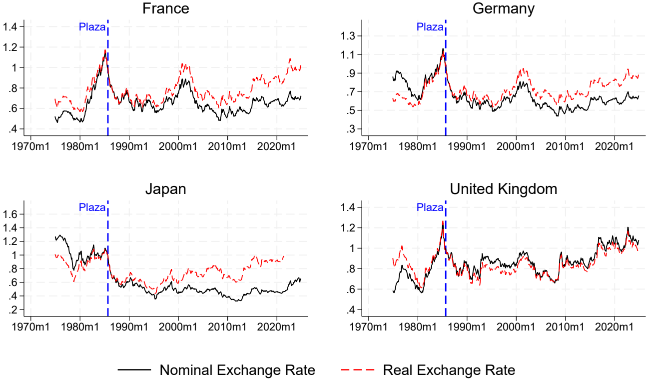

1. Eyeballing, RER adjustment was persistent
2. Speed of RER appreciation looks different pre-1985 vs. now
3. Levels may be incorrect comparison (Balasa-Samuelson, say)

3) Lessons from Plaza for depreciation / Mar-a-Lago?

- More likely now for economic policy tools to be deployed to maximize objective functions with non-economic elements.
- Struck by different tones in recent *International Economy*:
  - "A Mar-A-Lago Accord is not going to happen and it wouldn't work anyway."
  - "...Scott Bessent has one big advantage over Baker—his boss is more than willing to use sticks ... the Plaza Accord was [a] single agreement handily focused on currency depreciation, a Mar-a-Lago Accord could employ multiple policy tools... depreciation would play a supporting role..."

Concluding / Summarizing thoughts

- Nice paper that covers a lot of ground. Not much to critique or disagree with. Helpfully dispels myths.
- Discussion jumps to U.S.- or China- or CB-specific stories about persistent deficit (even in goods/manufacturing). Makes sense, but still helpful to note persistent deficits are not uncommon. (More on demographics, productivity, etc.?)
- Are we *so* sure tariffs won't reduce the deficit? For those of us that think a broad increase in tariffs would be bad, regardless of implications for deficits, we might shift emphasis a bit.