

TIANA'S TAKE

US trade deficits are necessary to protect entitlements

April 16-23 2025

Printed
4-24-25

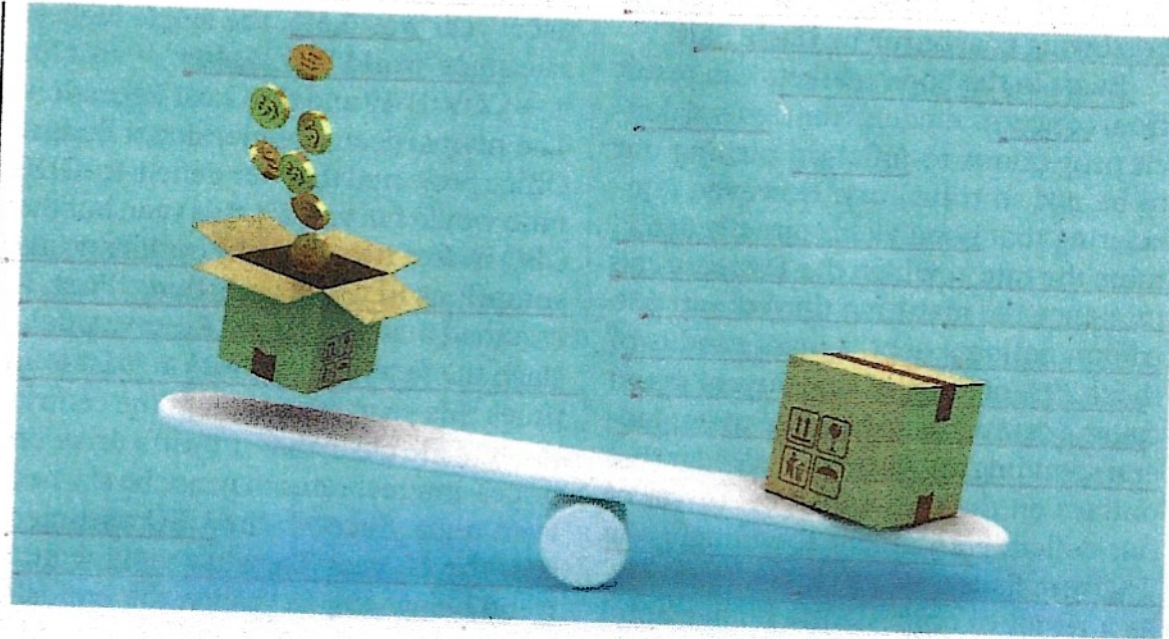


In the end, it wasn't the \$7 trillion in equities lost after "Liberation Day" that made President Donald Trump pause. He didn't dither over his congressional consiglieres' panic over whether the White House's impending trade war would jeopardize their crusade to extend the landmark 2017 Tax Cuts and Jobs Act. He didn't move because of his poll numbers. The only force of finance that ultimately compelled Trump to capitulate and pause his "reciprocal" tariffs on more than 60 nations, except for China, was the bond market.

"The bond market right now is beautiful, but yeah, I saw last night when people were getting a little queasy," Trump said after shocking the stock market into euphoria with his announcement of the pause. While the 10% minimum universal tariffs remain in place, with the White House saying it will entertain free trade deals in the 90-day interim, Trump took a dramatically different approach to his defiance over the weekend that the tariffs, far from being threats to negotiate a deal, were end goals to eliminate what he characterized as the ultimate evil: trade deficits.

"I spoke to a lot of leaders — European, Asian — from all over the world. They're dying to make a deal, but I said, 'We're not going to have deficits with your country,'" Trump said just three days prior to this about-face. "We're not going to do that because, to me, a deficit is a loss. We're going to have surpluses, or at worst, we're going to be breaking even."

For other countries, trade deficits are neither good nor bad. However, for America in particular, trade deficits aren't just good. They are necessary to bolster the bond market, as Trump began to learn with Monday and Tuesday's Treasury rout. If Trump insists on his refusal to reform our extensive entitlement state even though Social Security



and Medicare are both careening toward insolvency, that trade deficit keeping that bond market afloat is indispensable to financing America's (and Trump's) addiction to endless deficit spending.

More than half a century ago, Milton Friedman warned us that the jargon for discussing trade deficits was "upside-down." He explained that the real beneficiary in a trade relationship is the party that economics describes as having an "unfavorable balance of trade" or a trade deficit.

"What we send abroad, we can't eat, we can't wear, we can't use for our houses," Friedman said. "The goods and services we send abroad are goods and services not available to us. On the other hand, the goods and services we import provide us with TV sets we can watch, automobiles we can drive, and all sorts of nice things for us to use. The gain from foreign trade is what we import. What we export is the cost of getting those imports. And the proper objective for a nation, as Adam Smith put it, is to arrange things so that we get as large a volume of imports as possible, for as small a volume of exports as possible."

However, for America in particular, our trade deficit doesn't just mean cheaper luxuries but rather the baseline ability to finance one of the largest debt-to-GDP ratios on the planet.

The trade deficit doesn't exist in a vacuum. The balance of a nation's imports and exports, otherwise known as a current account, exists on one side of the ledger. On the opposite sits the capital and financial account, or the balance of assets ranging from stocks and bonds to foreign direct investment. Because the current account and the capital and financial account are supposed to even out to zero, our vast trade deficit

RESTORING AMERICA necessitates an extraordinary capital account surplus. When American consumers purchase foreign goods and services in U.S. dollars, foreigners either use those dollars as mediums of exchange, further bolstering the greenback's status as the world's reserve currency, or invest them, often in U.S. Treasuries. When the United States first began to maintain consistent trade deficits in the 1970s, foreigners held just 5% of the U.S. government's debt. By the end of 2023, that figure was 29%, roughly half of who were private investors and

the other half foreign governments.

The U.S. Treasury's status as the world's safe haven for investments is thus self-perpetuating. Because bond yields and bond values are inverse, the greater the demand for American bonds, the lower their yield or the lower the borrowing cost borne by Uncle Sam.

Busts in the bond markets can result from concerns ranging from federal deficit projections to inflation turning out to be not so transitory. However, considering that bond yields directly determine the rate at which the Treasury can refinance the maturing third of our \$36 trillion national debt, a mass exodus of those 29% of foreign bond buyers would cause a catastrophic increase to our federal spending projections. Consider that outlays on the current largest driver of our deficit, entitlement spending, grew 7% from fiscal 2023 to 2024. However, as a result of consistently higher bond yields (which in turn were impelled by

Treasury investors' fears of inflation and our debt trajectory), net interest payments on the federal debt increased by 34%. ✈

How does all of this play into projecting Trump's beloved entitlements? Well, our deficit-to-GDP ratio for the last fiscal year was 6.6%, the single highest rate since World War II after — wait for it — COVID-19 and the Great Recession. The nonpartisan Congressional Budget Office projected that our deficit-to-GDP ratio would fall to 6.2% this year, but the CBO makes two absurdly optimistic assumptions in those assertions. First, it assumed that the Federal Reserve would slash the federal funds rate at least four times this year, even though the central bank made clear that if tariffs drive up prices, interest rates may not be slashed even once. Second, the CBO assumed that the 10-year Treasury yield would trend below 4%. In reality, the imposition of the baseline 10% universal tariffs

coincided with the 10-year yield skyrocketing as foreign investors offloaded American bonds, driving their values downward.

There are other material defenses of the trade deficit, such as the fact that in the 30 years since NAFTA went into effect, our real GDP per capita adjusted for cost of living increased by 60%. Meanwhile, Canada's is up only 37%, and Mexico's is up a mere 19%. Further, a study of 137 countries across 20 years by the Peterson Institute found that tariffs were actually associated with increasing trade deficits.

However, for the immediate purposes of the president's priority of financing an unfettered federal deficit, the trade deficit is more than good for consumer convenience. It's the only way the government can bankroll its bloat. ★

Tiana Lowe Doescher is an economics columnist for the *Washington Examiner*.

Washington Examiner

Join Our Exclusive Subscriber Facebook Group

The *Washington Examiner* Facebook group is an exclusive online community for *Washington Examiner* subscribers designed to be your gateway to more than just our magazine.

This is a space to:

- Interact with our editors
- Share your thoughts
- Connect with other like-minded conservatives in a space free of the current woke culture



Log in to your account at [washingtonexaminer.com/login](https://www.washingtonexaminer.com/login) to sign up today.