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Barry Eichengreen

The Economic Policies of the Next US President

Every US presidential election is consequential, but American voters will face an exceptionally weighty decision in November 2024. The outcome will have implications for US foreign policy, social policy, and the integrity of the political system.

And then there's economic policy. Vice President Kamala Harris is the candidate of economic policy continuity. While she lacks experience and a lengthy record of statements on economic policy issues, the best bet is that she will maintain many of the policies of President Joe Biden. Her opponent, former President Donald Trump, is a candidate of continuity as well – continuity with the low-tax, high-tariff, business-friendly policies of the Trump term from 2017 through 2020.

DEBTS AND DEFICITS

The next president, whomever he or she may be, is likely to inherit an economy with low unemployment, an inflation rate converging toward 2 percent, and a growth rate that is the envy of most any European economy. But he or she will preside over an economy with a large public debt (debt in the hands of the public on the order of 100 percent of GDP) and a budget deficit that the nonpartisan Congressional Budget Office projects, given no changes in current law, will approach 6.5 percent of GDP in 2025, down only marginally from 2024. Assuming a real interest rate of 1 percent and a real GDP growth rate of 2 percent, the primary (non-interest) deficit will have to be reduced by 2 percentage points of GDP to prevent the debt ratio from rising further. One respect in which the two candidates' economic policy positions are aligned is that neither has a realistic plan for closing this gap.

The CBO's projections assume that the 2017 Tax Cuts and Jobs Act will expire at the end of 2025, as scheduled under current law. That act, passed during the earlier Trump term, cut the corporate tax rate to 21 percent from 35 percent, reduced individual income tax rates, and increased the standard deduction available to income taxpayers who do not itemize deductions. Trump is unlikely to endorse higher taxes; on the contrary, he has indicated a desire to make his earlier tax cuts permanent. In his speech accepting the nomination at the Republican National Convention, he proposed reducing the corporate income tax rate further to 15 percent. In contrast, Harris would raise taxes on the well off, defined as households making more than USD 400,000 annually, increase

the tax rate on capital gains, and impose a largely symbolic minimum tax rate on incomes of billionaires, all along the lines of the Biden Administration's earlier budget. The Biden White House's proposed budget for the fiscal year running from July 2024 through June 2025 would also have hiked the corporate tax rate from 21 to 28 percent, reversing out half of the rate reduction between pre- and post-Trump years, and the Harris campaign has signaled support for this idea. These and related proposals would reduce the deficit by USD 75 billion in 2025, according to independent estimates, where the overall deficit, again pace the CBO, is slated to be on the order of USD 2 trillion. The additional revenue, then, is what tax specialists politely refer to as a drop in the bucket.

Equally, there will be limited scope for the next president to reduce public spending. Some 59 percent of federal outlays are on pensions (Social Security), health care programs (such as Medicare for the elderly and Medicaid for low-income individuals), and other mandatory items. Another 13 percent of the

KEY MESSAGES

- **The next president of the United States will have to address the country's chronic budget deficits and spiraling debt. Unfortunately, neither candidate has a coherent plan**
- **Neither candidate is committed to free trade. Whereas Trump's trade policies will be conditioned by animosity toward China, Harris's will be shaped by climate and labor standards**
- **A dramatic difference between the two candidates is on climate policy, where Trump proposes to again withdraw the US from the Paris Agreement and to expand the use of oil and gas, whereas Harris was a proponent of the 2019 New Green Deal**
- **Trump promises to reduce the cost of living by eliminating red tape and restrictions on oil and gas exploration and extraction, while Harris has promised to eliminate price gouging and other anti-competitive practices and to provide subsidies for affordable housing**



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budget goes to defense, and a further 14 percent pays interest on the debt. Basic arithmetic suggests that this leaves only a small fraction of the budget for forms of discretionary spending that might be cut. Trump has suggested sharp reductions in government employment and alluded to equally sharp reductions in defense spending. Whether domestic politics will permit the former, foreign politics the latter, is an open question, to put the matter in the most positive possible way.

Harris for her part has advocated in favor of Biden's programs providing subsidies for the domestic production of semiconductors and other advanced products on both national security and good-manufacturing-jobs grounds. She would implement so-called place-based policies that subsidize investment and small business operations in urban and rural communities that have fallen behind the rest of the country in terms of income and employment growth. She has proposed expanded tax credits for parents, paid parental leave, public spending on childcare, and more funding for education. She would add a USD 6,000 tax credit for newborns in their first year of life and make permanent the temporary pandemic-era tax credit for children that the Congress subsequently allowed to expire.

Recent research has pointed to positive returns from place-based policies, early childhood education, and reductions in child poverty (where such reductions make for better adult health and higher incomes). More precisely, it has pointed to positive returns when the policies and programs in question are well designed. Harris has emphasized this "return on investment" (her words); her campaign has suggested that many of these programs will pay for themselves. But appropriate design and high returns are not to be taken for granted. The experience of European countries that have similar programs in place suggests that these will have to be financed, at least in part, to avoid further widening the budget gap. Financing such programs will be no mean feat: making the pandemic-era tax credit for children permanent, by itself, would cost more than USD 1.2 trillion in revenues over ten years, according to the nonpartisan Committee for a Responsible Federal Budget. It is worth recalling, moreover, that all bills for raising revenue must originate in the House of Representatives and be passed by both Houses of Congress. The US president, of whatever party and inclination, cannot address the country's fiscal imbalance on his or her own. This is a reminder that November 2024 will see the election of not just the president but also one-third of the Senate and the entire House.

TRADE POLICY

Candidate Trump has also mused about a more radical fiscal idea, namely replacing the federal income tax in its entirety with a tax on imports, which he as-

serts will be paid in whole or large part by foreigners. Most economists will dismiss this idea out of hand. Replacing USD 2 trillion of individual and corporate tax revenue with taxes on USD 3 trillion of US imports would require an enormously high tariff, even assuming no decline in US import demand, no foreign retaliation, and no corollary damage to the US economy. Although Republicans in Congress no longer pledge allegiance to the Laffer Curve, even they will find it hard to deny that an import tax rate in excess of 67 percent will be on the wrong side of that relationship. Even the revenue-maximizing tariff, which is on the order of 50 percent given conventional assumptions about the elasticity of import demand, would replace barely one-third of existing individual and corporate tax revenues. As for the assertion that this import tax will be paid by foreigners, studies have shown that the largest share of the costs of Trump's first-term tariffs were passed through to US consumers and producers. Shifting from a graduated income tax to what would effectively be a de facto consumption tax would have the most dramatic negative effects on low-income US households, who devote the largest share of their incomes to consumption.

Alternatively, Trump has proposed a 10 percent tariff on all US imports and a 60 percent tariff on imports from China. The comprehensiveness of a 10 percent across-the-board tariff and the height of a 60 percent Chinese tariff would be escalations of policies followed in the earlier Trump term, when only certain imports were taxed and tariffs on imports from China ranged from 10 to 25 percent.

It is relevant here that Biden in his presidential term did not roll back Trump's tariffs in their entirety. Not only did he retain his predecessor's tariffs on imports from China, but he increased those duties on steel, aluminum, and clean-energy products, even quadrupling tariffs on Chinese electric vehicles. To be sure, in 2021 the Biden Administration negotiated an agreement with the EU suspending US tariffs on European aircraft and agricultural products and replaced US tariffs on European and Japanese steel and aluminum with a tariff-rate-quota system, where only imports above the designated quota are taxed. But, whatever the outcome, the 2024 election will not herald a return to free trade in the United States. The global trading system will remain under strain. Decoupling between the US and China will continue.

It is worth recalling in this context that Vice President Harris has stated that she would have voted against the 1992 North American Free Trade Agreement (NAFTA) and the proposed 2016 Trans-Pacific Partnership. While serving in the Senate in 2020, she voted against the successor to NAFTA, the United States-Mexico-Canada Agreement (USCMA). In explaining her opposition to NAFTA, Harris cited its failure to protect American workers from low wages and lax labor standards abroad. In voting against US-MCA, Harris cited the agreement's inadequate envi-

ronmental protections, and that free trade between the US and Mexico enabled dirty industries to operate freely south of the border. This suggests that under a Harris Administration future US trade conditions and agreements will be conditioned on labor and environmental standards.

CLIMATE POLICY

This observation points to what is perhaps the most consequential economic policy difference between the two candidates, namely their positions on climate policy. President Trump pulled the United States out of the Paris Climate Accord in 2019, while the US under President Biden reentered it. Trump has vowed to expand oil and gas production, and his campaign has stated that he would withdraw the US from the Paris Accord a second time if granted another term. In contrast, Harris supported the Green New Deal while serving in the Senate and investigated the oil industry while California Attorney General, securing a settlement from British Petroleum subsidiaries in compensation for underground gas tank ruptures and indictments against a Texas-based pipeline operator for an environmentally damaging oil leak.

Thus, under a President Harris the United States is likely to attempt to revive US-EU negotiations seeking to link trade and decarbonization. Those negotiations were suspended in early 2024, partly owing to seemingly irreconcilable differences between the negotiating partners, and partly due to the difficulty of passing a new trade agreement into law given a divided Congress and a US presidential election year. The fundamental difficulty lies in the two economies' very different approaches to limiting carbon emissions. Europe is putting in place a carbon border adjustment mechanism that will tax imports of emission-laden products at the same rate as domestically produced substitutes subject to the EU's cap-and-trade emissions system. The US Congress has blocked cap-and-trade, so US negotiators have instead proposed symmetrical subsidies for low-carbon production of steel, aluminum, and other products, together with the elimination of both Europe's carbon border adjustment system and US tariffs on steel and aluminum, and tariffs on imports from other countries that do not subsidize or otherwise move to low-carbon production. Whether a Harris Administration could reconcile these two different approaches is unclear. But it is likely to try. The alternative is more US-EU commercial tension and headwinds for the global trading system.

THE DOLLAR

Another issue for the next president of great consequence for the rest of the world is policy toward the dollar. Trump, his vice presidential running mate J. D. Vance, and his former trade negotiator (and pro-

spective treasury secretary) Robert Lighthizer have complained that the high value of the dollar handicaps the efforts of US exporters. Given the limited resources of the Exchange Stabilization Fund of the US Treasury, it is unclear whether intervention in the foreign exchange market in pursuit of a lower dollar would succeed. Trump's advisors have suggested the possibility of tariffs on imports from countries that prevent their currencies from appreciating against the greenback, or alternatively a tax on foreign purchases of US treasury securities and other assets, purchases that have the effect of supporting the dollar on foreign exchange markets. The first measure could be destabilizing for the global trading system, since Trump's initial 10 percent tariff would itself push up the dollar, insofar as it did nothing to alter the balance between US saving and investment and therefore the current account balance. More tariffs would then make for a stronger dollar, and in turn still more tariffs, continuing without obvious end.

Alternatively, taxing foreign purchases of US treasuries would undermine the international and reserve currency role of the dollar. There being no adequate substitute for the dollar as a source of global liquidity, global finance as well as global trade would be at risk. Yet another possibility is President Trump pressuring the Federal Reserve to lower interest rates so as to weaken the dollar, Trump in the past having raised questions about the independence of the central bank. A serious challenge to the independence of the Fed would in turn weaken confidence in the integrity and stability of the dollar as an international currency, again with ominous implications for the global trade and financial systems. President Biden has adhered to the so-called "strong dollar policy" of US administrations since the 1990s – which mainly amounts to not commenting on the dollar. He has not questioned the independence of the Fed. Vice President Harris has not shown signs of departing from this line. As she put it in the late days of last summer, "The Fed is an independent entity and as president I would never interfere in the decisions that the Fed makes."

THE COST OF LIVING

The Federal Reserve notwithstanding, inflation is an issue of great concern to American voters and hence to both presidential candidates. Trump has promised to bring down the cost of living – effectively, to reverse past inflation. He has not provided much detail on specific policies to achieve this, other than eliminating costly regulation and removing limits on oil and gas exploration and extraction. Harris has focused on food prices and housing costs. She proposes a federal ban on price gouging for groceries, a measure that seems somewhat redundant, since many states already have laws prohibiting predatory pricing in the wake of hurricanes and other natural disasters. Allusions to "new federal enforcement tools" to punish

companies that opportunistically push up the prices of food are open to various interpretations. Best would be to simply use existing enforcement tools, such as the existing antitrust, pro-competition powers of the Justice Department and the Federal Trade Commission. Reassuringly, Harris alluded to this alternative as well, asserting in her maiden economic address in August that “We will help the food industry become more competitive because I believe competition is the lifeblood of our economy.”

On housing, Harris would send up to USD 25,000 of down-payment assistance to qualifying first-time home buyers. (Who exactly would qualify is yet to be specified.) She would provide tax credits to companies that build starter homes, and direct USD 40 billion to local governments that encourage the construction of affordable housing. Increasing the supply of homes is an admirable goal in a country where, for many, housing is unaffordable. The USD 40 billion fund can be leveraged to counter local government resistance in areas where NIMBY (“not in my back yard”) sentiment is strong. But down-payment assistance will only increase the demand for homes. Basic incidence analysis suggests that the benefits will accrue heavily to home builders and sellers, and not to first-time buyers, insofar as supply remains inelastic.

POLICY CONCLUSIONS

No question, the upcoming US election will have far-reaching implications for the global trading system, for US-EU economic relations, and for climate policy. It will determine whether there is regress, progress, or perhaps just stasis in redressing the imbalance in US fiscal policy. It could reshape the position of the dollar and more generally of the United States in the world economy. It will affect US-China relations and the fate of globalization. Clearly, much is at stake.