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Article

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Does Trump Know What He Wants from Europe or How to Get It?

Vice President JD Vance wants to restore American manufacturing. Treasury Secretary Scott Bessent intends to build a free trade coalition against China. Council of Economic Advisers Chairman Stephan Miran wants a weaker dollar. Commerce Secretary Howard Lutnick wants a permanent new revenue source. Adviser Peter Navarro wants to unleash dramatic change and possibly even chaos. But none of them are the President of the United States, and the President keeps changing his mind on both the broad goals and specific instruments of his international economic policy.

President Trump has had two consistent views about trade for decades. The first is that trade deficits in goods (he ignores one of America's strongest exports, services) reflect a net loss for the United States. This profit-and-loss statement shows a \$240 billion "loss" in 2024 (the trade deficit in goods) and has had consistent "losses" for decades. Of course, every economist knows this is not a loss; you could just as easily (and just as inaccurately) say that the European Union lost cars, perfume, machine tools and medical equipment to the United States. The idea that voluntary transactions might benefit both sides does not seem foremost on the President's mind.

The second view is that the trade deficit has come about because Europe has been "unfair" to the United States. Some of that alleged "unfairness" is, for example, a 10% tariff on imports of U.S. automobiles – something I agree is a mistaken European policy but one that Europeans suffer from more than Americans. Regardless, Europe and the United States have mostly low tariffs punctuated by a few high ones, averaging out to rates of about 2%, at least until the new trade war. Addressing these tariffs could be a feasible and desirable objective for policy, something I will return to.

However, Trump's more considerable contention is that Europe is unfair to the United States because of value-added taxes (VATs). The argument, which just about every economist disagrees with, is that VATs apply to imports but not to exports, so they discriminate against trade. VATs apply equally to domestic production and imports, so they are neutral, and that neutrality is cemented by exempting exports from VATs so they will not be double taxed when sent abroad. Regardless of the economics, getting Europe to eliminate its VATs is not a feasible or desirable policy objective. The trade war will never end if that is the United States' demand.

Trump's biggest contention is that the European Union itself was designed to take advantage of the United States. Not only is this a baseless slander – if anything, the United States was enthusiastic about the formation of the European Union – but getting Europe to dismantle the European Union is also an even less feasible or desirable policy objective than getting European countries to eliminate their VATs.

One possibility is that the United States wants greater market access. If the agreement were merely about lower tariffs, it would be technically easy to finish a quick negotiation; the upside for both economies would be relatively small, but still worthwhile. For this to happen, the United States must be willing to drop its 10% across-the-board tariff. A more considerable upside would come from deeper integration like the Transatlantic Trade and Investment Partnership (TTIP) that was under negotiation a decade ago. Still, I see little in-

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dication that this is Trump's endgame; it could take years to negotiate, and it was politically controversial in even major European export powerhouses like Germany a decade ago. The ascendancy of Trump to the U.S. presidency has likely only exacerbated the concerns about doing a deal with the United States.

Another possibility that, as of this writing, seems to be on the ascendant – with the caveat that it could change at any moment – is that the primary U.S. demand is not to increase market access for American companies operating in Europe, but is to reduce European economic integration with China. In some ways, this goes with the grain of the increased European skepticism of economic integration with China. Last year, for example, the European Union mirrored Biden's high tariffs on Chinese electric vehicles with its own very high tariffs. However, there is a limit: Europe's total trade exposure to China, exports plus imports, was €740 billion last year, the same order of magnitude as the €850 billion trade exposure to the United States. Perhaps more importantly, Europe – or some European countries – is considerably more open to Chinese foreign direct investment than the United States. And foreign direct investment could be the United States' biggest concern if they are trying to plug the holes in its Chinese tariff regime.

Not knowing what he wants from Europe is only one of Trump's problems in a successful negotiation. Even more serious is the asymmetry. The trade war will hurt the U.S. economy much more than the European economy. The reason is that the United States is now in conflict with basically every country in the world, while Europe is only facing significant issues with its trade with the United States. Trump's seeming indifference to short-term pain does help increase his leverage, but massively overestimating that leverage would be an obstacle to a deal. Europe's democratic decision-making and Trump's reputation for breaking his deals add further challenges.

The uncertainty of Trump's demands, whether grandiose like ending the European Union and acquiring Greenland or more modest like significant tariff reductions, adds to the unpredictability of the situation. The potential outcomes range from a token victory that aligns with the desires of the U.S. business community and markets to more significant sectoral tariffs, including pharmaceuticals, and possibly even the return of the Orwellianly named "reciprocal tariffs".

It is impossible to predict what Trump will want from Europe, and even harder to predict what he will get from Europe. However, one thing is sure: regardless of the outcome, Europe will still be, by Trump's reckoning, taking advantage of the United States by running a bilateral trade surplus for the foreseeable future. This means that Trump's focus on and complaints about Europe will remain a risk as long as he – or any successor who shares his mentality – is President.

What should Europe do? First, strive to secure a good deal. It may get lucky with token concessions, ideally ones that are not even concessions but beneficial for its economy. Second, prepare for uncertainty. Even if a good deal is reached, it may not last, and without an agreement, a wide range of changes are possible. Third, diversify economic integration with other partners around the world because the United States is now less reliable. Finally, and most importantly, meet the challenge from the United States by deepening integration within Europe and improving its own economic policies – including ideas from the Draghi report, stronger demand and investment in countries with fiscal space, and reforms and consolidation in countries without it. By doing so, Europe could emerge from this situation in a stronger position, despite the United States' actions.

With the correct response, Europe could come out of this better off, regardless of what the United States does. I cannot say the same for the United States' ability to recover unscathed from its massive self-inflicted wound.