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**Article**

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Alessandro Bellocchi and Giuseppe Travaglini

# The Trade Deficit Delusion: Why Tariffs Will Not Make America Great Again

This study analyses the protectionist trade policies of the Trump Administration, focusing on tariffs' impact on the US trade deficit and broader economic consequences for its trade partners. By highlighting five stylised facts characterising the US economy, the analysis shows that the trade deficit primarily arises from the persistent gap between national saving and domestic investment, rather than unfair foreign trade practices. Using open economy accounting, the study demonstrates that tariff policies are ineffective for correcting trade imbalances and could exacerbate them, negatively affecting both US and European economies through disrupted trade flows, increased economic uncertainty, and instability in financial markets. The study also explores several possible scenarios resulting from these policies and suggests that protectionist measures represent an “impossible theorem” for rebalancing trade deficits and pose significant risks also for the economic stability of US trade partners.

In March 2017, during his first presidential term, Donald Trump signed an executive order aimed at identifying the causes of the growing US trade deficit. Trump and his administration started from the assumption that the imbalance between exports and imports in the American economy was primarily due to unfair trade practices adopted by international partners. According to Trump, high foreign tariffs, implicit duties and non-tariff barriers imposed by foreign governments, along with domestic policies that restrained consumption, prevented the expansion of US exports to the rest of the world, thereby hindering the rebalancing of the American trade deficit. In line with this interpretation, the following year, Trump signed a memorandum that launched a tariff offensive against China, imposing duties on a wide range of imported goods. Tariffs were introduced on Chinese goods amounting to over US \$300 billion, particularly in the technology and intellectual property sectors (Chad & Zhang, 2019).

Today, in his second presidential term, Trump has launched a new wave of protectionism. The federal government has introduced a universal 10% tariff on all goods imported into the United States, along with higher duties on goods from 57 specific trading partners.<sup>1</sup> According to data of the Tax Foundation (a Washington DC based think tank), the average tariff<sup>2</sup> applied to imports is expected to rise from 2.5% in 2024 to 16.5% in 2025 under Trump's proposed trade policies, the highest rate since 1937 (Figure 1). In this scenario, the tariffs would reduce US imports by more than US \$800 billion in 2025, equivalent to 25% of current import volumes (York & Durante, 2025).

In the current vision of the Republican Party, trade deficits are inherently negative and should be eliminated.<sup>3</sup> The Administration argues that the US trade deficit stems from foreign regulatory barriers on US goods and services, restrictive environmental regulations of trade partners, differences in consumption tax rates, additional compliance costs (i.e. VAT) and foreign currency manipulation (Obstfeld, 2025). This reflects a more mercantilist than lib-

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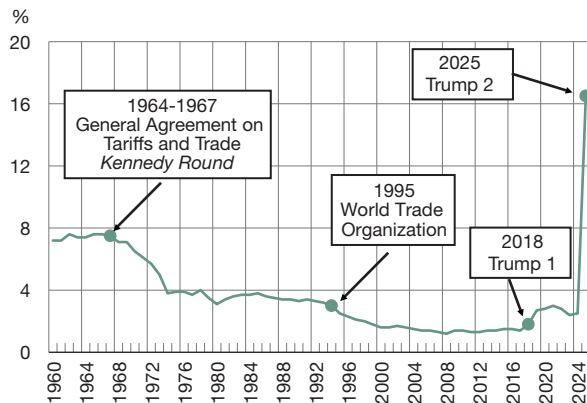
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- 1 On 9 April, President Trump announced a 90-day suspension of most tariffs to reopen trade negotiations. This was followed by a major US-China truce on 12 May, with both sides agreeing to sharply lower tariffs. The move marks a de-escalation in global trade tensions.
- 2 The weighted average tariff is calculated based on actual applied rates, weighted by the share of imports from each trade partner.
- 3 The formula used is:  $\Delta T_i = (x_i - m_i) / (\epsilon \cdot \phi \cdot m_i)$ , where  $x_i - m_i$  is the bilateral trade balance with a given country,  $m_i$  is the volume of US imports from that country,  $\epsilon$  is the price elasticity of import demand and  $\phi$  is the price elasticity of imports with respect to tariffs. These two parameters were set respectively at 4 and 1/4.

Figure 1  
US average effective tariff rate



Notes: Data for 2025 is projected. The graph includes IEEPA (International Emergency Economic Powers Act) tariffs on Canada, Mexico and China; the “reciprocal” tariffs of 2 April 2025; and the tariffs on steel, aluminum and cars.

Source: Authors’ elaboration on data from the Tax Foundation.

eral view of international trade. It also represents a naïve conception of the international macroeconomic system, not only regarding the exchange of goods and services but also the movements of capital and the flows of savings, which are the natural counterpart to the trade balance.

Will Trump’s policy be effective in correcting the US trade deficit? Or is the tariff policy merely an “impossible theorem”? In what follows, we show that the US trade imbalance is only marginally attributable to the “predatory” factors hypothesised by the US government. Rather, it largely reflects a persistent, decades-long gap between national savings and domestic investment (the so-called saving-investment gap).

If this explanation holds, it carries a crucial implication: efforts to reduce the trade deficit through protectionist policies may backfire, ultimately widening the deficit and triggering adverse effects on economic growth and inflation.

As we show below, the global reach of Trump’s trade policy extends far beyond bilateral frictions with China. Europe, being both a major trading partner and geopolitical ally of the United States, is likely to be affected by these measures. In the short term, European exporters may suffer from the reduction in US import demand, particularly in the automotive, machinery and luxury goods sectors. In addition, if Trump’s tariff plan triggers retaliatory measures or broader trade fragmentation, European firms could face rising input costs and supply chain disruptions (Furman, 2025).

More structurally, an entrenched protectionist stance by the US may accelerate the reconfiguration of global value chains and trade alliances – pushing Europe to deepen trade relations with China and other emerging markets, while increasing pressure on the EU to assert a more autonomous commercial and industrial policy. These developments could not only reshape the transatlantic economic relationship but also test the resilience of the multilateral trade system itself (Gros, 2025).

This article first presents key stylised facts about the macroeconomic structure of the United States. It then examines the historical evolution of the US trade deficit and explores the trade balance, emphasising the role of tariff policies in shaping both internal and external equilibrium. This is followed by a critical assessment of the effectiveness of tariffs in reducing the trade deficit. The analysis outlines three potential scenarios for the US in the face of rising protectionism, and concludes with reflections on the prospects for the US trade balance, the legacy of Trump-era tariff policies and the long-term sustainability of the global economic order.

### Stylised facts

In this section, we present five stylised facts about the macroeconomic structure of the United States that we consider crucial for interpreting the current American trade deficit.

First, the US economy has historically been characterised by a high level of private consumption, low public expenditure and a low degree of openness to international trade. In 2024, the *degree of openness* of the economy, measured as the sum of exports and imports as a percentage of GDP, was only 25%, significantly lower than that of the United Kingdom (60%), the European Union (50%) and Japan (45%).

Second, private consumption represents the main component of US GDP, amounting to 68% in 2024 (compared to 62% in the UK, 54% in Japan and 53% in the EU). The *average propensity to consume*, stable during the 1960–1980 period at around 90% of personal income, has increased in recent years to about 95%.<sup>4</sup> The high level of private consumption is a major driver of household indebtedness, which in 2024 stood at 72% of national income.

Third, *final government consumption expenditure* is historically low and accounted for only 13% of GDP at the end of 2024. This underscores the limited role of the public

<sup>4</sup> Personal savings is measured as a ratio of savings to per capita GDP (Obstfeld, 2025).

**Table 1**  
**Composition of US aggregate demand (% of GDP)**

Years	Private consumption	Investment	Government consumption	Exports	Imports
1960-1969	60.4	22.3	16.7	5.1	4.5
1970-1979	60.9	22.3	16.9	7.5	7.7
1980-1989	62.8	22.9	16.0	8.3	10.0
1990-1999	65.1	21.3	15.1	10.2	11.7
2000-2009	67.5	21.6	15.4	10.6	15.0
2010-2019	67.8	20.4	14.8	12.5	15.5
2020-2025	67.8	21.5	13.9	10.9	14.1

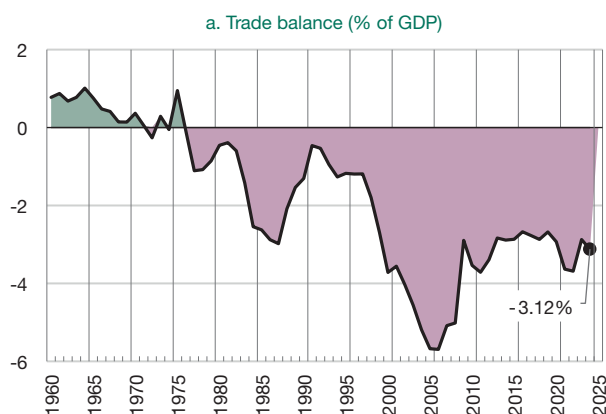
Notes: The table presents ten-year average values. The latest figure (2025) in the 2020-2025 average includes estimated values provided by the macroeconomic forecasts of the European Commission.

Source: Authors' calculations based on AMECO data.

sector in the US economy compared to other advanced economies (20%-21% in the EU, UK and Japan). Nevertheless, public saving (i.e. the difference between tax revenues and government expenditure) remains negative. According to the latest available data, the federal budget balance was -6.3% of GDP in 2023.

Fourth, high domestic consumption has been accompanied by a decline in *household savings rates* and an increase in investment (in capital goods and technology) necessary to support long-term production growth. Net fixed investment currently amounts to 5.2% of GDP, higher than in the EU (3%), the UK (2.5%) and Japan (0.8%). The US saving rate (as a share of GDP) remains relatively low compared to that of other major advanced economies.

**Figure 2**  
**US trade balance and the saving-investment gap**



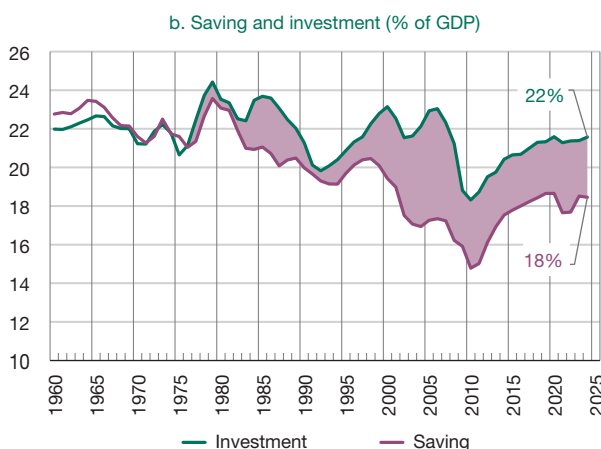
Fifth, the *trade balance* – defined as the difference between exports and imports – has steadily deteriorated since the 1980s. The current account balance has progressively worsened to the present day. Within this context, the trade balance for services remains in surplus.

These five stylised facts, summarised in Table 1, in our view, provide the key to understanding the underlying causes of the US trade deficit and the impact of Trump's protectionist policies.

### The US trade deficit

Over the past 50 years, the United States has experienced large and persistent trade deficits. As of December 2024, at the end of President Biden's term, the US current account deficit had reached US \$918 billion, equivalent to 3.1% of GDP (Figure 2a). The continuous growth of imports relative to exports over time has been financed through net borrowing from the rest of the world and by selling US assets to foreign investors (Figure 2b). As a result, the United States has gone from being a global creditor to a net debtor.

This change unfolded over a relatively long period of time. As early as the late 1960s – following the development of the so-called American model, which had sustained the post-war European recovery (Marshall Plan), and later with the oil crisis of the following decade – the first signs of a deteriorating trade balance began to emerge (Travaglini, 2024). The deficit widened during this time and became structural in the 1980s, in part due to the expansionary fiscal policies of the Reagan Administration (Reaganomics), which included major income tax cuts (based on the so-



Source: Authors' elaboration on data from BEA.

called Laffer curve) that were not accompanied by equivalent reductions in public spending (Blanchard, 1987).

The combined effect of these changes was twofold: on the one hand, they revitalised national production and incomes after the stagnation of the 1970s; on the other, they led to a decline in both private saving – as American households increased consumption – and public saving, due to rising federal deficits. Eventually, this led to a decrease in national savings (the sum of private and public savings). Economic growth also sustained greater demand for imported goods by firms and households, further worsening the trade deficit and giving rise to the phenomenon of twin deficits: the simultaneous occurrence of trade and budget deficits (Miller & Russek, 1989).

Only in the 1990s did a temporary reversal occur. A renewed commitment to fiscal discipline, embraced by both the Republican administration of George H. W. Bush and the Democratic administration of Bill Clinton, resulted in higher taxes and stricter public spending controls. At the same time, the information and communication technology (ICT) revolution led to a renewed surge in US productivity, boosting incomes and tax revenues and briefly returning the federal budget to surplus. However, the increase in national saving was still not sufficient to offset the growing trade deficit, which continued to rise due to internal investment driven by the explosive growth of the ICT sector (Mann, 1999).

In the early 2000s, national saving declined again, due to the Bush Administration's tax cuts and increased public spending tied to the global "war on terror". This period saw the trade deficit deepen further, narrowing only temporarily during the 2008 financial crisis and the resulting collapse of residential investment in the US. The subsequent US \$800 billion fiscal stimulus initiated by President Obama (known as the American Recovery and Reinvestment Act) helped lift the economy out of the crisis, but also widened the federal deficit, compounded by increased welfare spending associated with the new public health coverage programs (Obamacare; Davis, 2011).

Today, following the transition in leadership from Trump and Biden, the US trade deficit has stabilised, yet remains substantial. Further, the issue of twin deficits is still unresolved. The current Republican administration has inherited a prolonged phase of economic expansion, with GDP growth rates averaging above 3%.

It is in this context that Trump's protectionist policy agenda made a comeback, with the goal of eliminating the trade deficit (and rebalancing the federal budget). These are complex and, in the short term, contradictory goals

that will reshape both the international trade landscape and US domestic saving dynamics (Obstfeld, 2025).

### Tariffs and trade balance

The balance of payments reflects international flows of goods and services as well as changes in a country's net foreign wealth. These flows are inherently interconnected. Let us start with the current account. Measured in nominal terms, the current account (or net export –  $NX$ ) is the difference between total exports  $X$  and imports  $IM$ . This value can also be expressed as the difference between GDP ( $Y$ ) and domestic demand

$$NX = Y - (C + I + G), \quad (1)$$

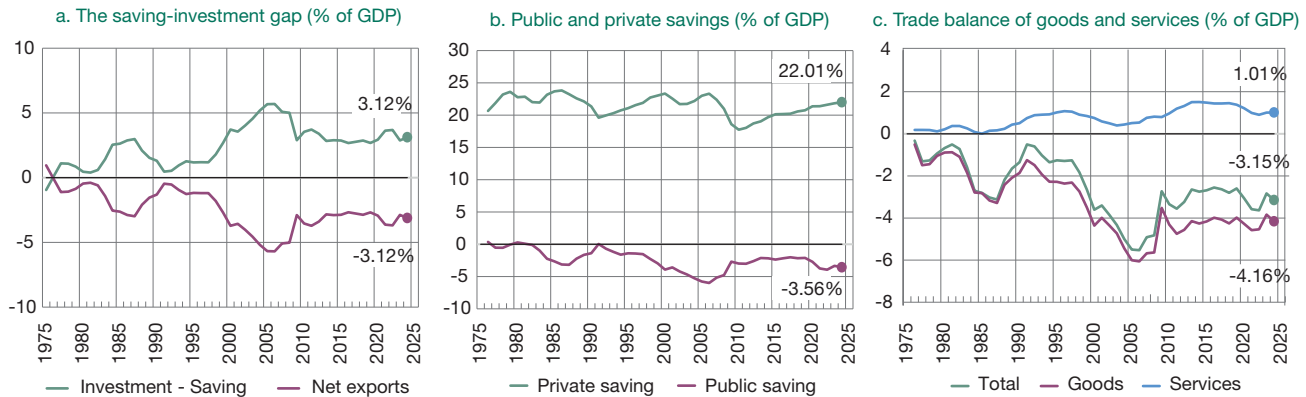
where  $C$  is private consumption,  $I$  investment and  $G$  government spending. This identity provides two important insights. First, a trade deficit ( $NX < 0$ ) does not necessarily signal excessive consumption today at the expense of tomorrow. It may reflect high investment, public or private, to raise future productive capacity. Alternatively, it could result from high public spending. Second, policies aimed at improving the trade balance – whether through tariffs or currency devaluation – must operate through the macroeconomic channel, increasing  $Y$  relative to domestic absorption ( $C + I + G$ ).

This last point can be developed through the lens of the open macroeconomic model (Blanchard, 2024). Imports are the part of domestic demand that falls on foreign goods. They depend positively on domestic income and are influenced by the real exchange rate, that is, the relative price of domestic goods compared to foreign goods. The less expensive domestic goods are relative to foreign goods, the smaller the domestic demand for foreign goods is. On the other hand, higher foreign income means higher foreign demand for all goods, both foreign and domestic. So, higher foreign income leads to higher exports. However, exports also critically depend on the real exchange rate. Specifically, the higher the price of domestic goods in terms of foreign goods, the lower the foreign demand for domestic goods. In other words, the higher the real exchange rate, the lower exports are.

According to this framework, net exports  $NX$  decrease with domestic output and increase with foreign income. A depreciation of the real exchange rate makes exports more competitive.<sup>5</sup> Tariffs act as an artificial change in

<sup>5</sup> Assuming the Marshall–Lerner condition holds. In the short run, the low-price elasticity of import and export demand due to contractual rigidities and consumer habits could still result in a temporary worsening of the trade balance (J-curve).

Figure 3  
US saving, investment and the trade balance



Source: Authors' calculations based on AMECO data.

relative prices: by making foreign goods more expensive, they mimic real depreciation and improve the competitiveness of domestic products.

This logic underlies Trump's protectionist strategy: imposing tariffs to improve the US trade balance by redirecting international trade flows towards American producers.

In this "Trumpian" vision, tariff policy appears to deliver its promise: boosting output and shrinking the trade deficit. But is it so simple? As we discuss below, underlying macroeconomic dynamics complicate this narrative and can lead to outcomes that diverge significantly from the policy's intended goals.

### Trump's "impossible theorem"

Although economists often debate the merits of specific policy measures, everyone recognises the logic of accounting identities. One of the most revealing identities applies to international trade: the trade balance is also equal to national saving minus investment

$$NX = S_N - I, \quad (2)$$

where national saving  $S_N$  is the sum of private saving and the government's budget balance ( $T - G$ ), with  $T$  measuring tax revenue. This identity is valuable in explaining the relationship between the trade balance and changes in a country's saving and net wealth.

When a country saves more than it invests ( $NX > 0$ ), the excess saving flows abroad resulting in a trade surplus. Conversely, if it invests more than it saves ( $NX < 0$ ), it must borrow the difference from the rest of the world, leading to

a trade deficit. Therefore, the trade balance is the mirror image of a country's saving and investment decisions.

For the US, this trend ( $S_N - I$ ) has been persistently negative. For over four decades, the country has invested more than it saved, financing this gap with foreign capital. The trade deficit has been the natural consequence of a national saving shortfall.

Macroeconomic data confirms this pattern. According to the Bureau of Economic Analysis (BEA), since 1976, investment has averaged 21.7% of GDP, while national saving has lagged at just 19.1%. That 2.6% gap shows up almost identically in the current account deficit (Figure 3a).

Behind the saving shortfall lie deeper trends. Public saving has been negative for years, as persistent budget deficits drag down national saving. In 2024, the federal government's budget balance stood at -3.6% of GDP. At the same time, household saving rates remain historically low (5% of disposable income), reflecting a consumption-driven growth model that leaves little room for financial surpluses (Figure 3b).

This imbalance is mirrored in the structure of international trade. The US runs a persistent deficit in goods (-4.2% of GDP), partially offset by a surplus in services (around +1%), including sectors like tech, finance and AI. But overall, the demand for imported goods overwhelms the gains from exporting services (Figure 3c).

What are the implications of these facts for Trump's tariff strategy? Three key insights follow from the saving-investment identity:



First, if investment continues to outpace savings, whether due to low household saving, large fiscal deficits, or both, then trade deficits are inevitable. The US cannot reduce imports without changing the underlying flows of capital.

Second, even if tariffs succeed in reducing imports (which is far from guaranteed), the only way to generate a trade surplus would be to either increase saving or reduce investment. However, the Trump Administration never proposed policies that would achieve either. Instead, it supported tax cuts and pushed for more domestic investment.

Third, the dream of “twin surpluses” – a shrinking budget deficit and a shrinking trade deficit – is unattainable without either a sharp increase in household saving or a collapse in investment. Neither outcome is likely, nor would either be desirable.

This is the “impossible theorem” of Trump’s trade policy. It promised a trade surplus in the short run, without the financial adjustments that such a surplus requires. Tariffs alone cannot solve a trade deficit that is deeply rooted in structural macroeconomic forces.

Finally, it is important to note that accounting identities do not explain what happens when tariffs are imposed. They do not tell us whether saving will rise, or investment will fall. But they do define the boundaries of what is possible, at least in the short run. In an economy like the US, where consumption and investment drive growth, there is limited room for trade rebalancing without either accepting slower growth or implementing sweeping fiscal reforms.

### Possible scenarios

Tariffs affect the trade balance, national saving and investment. Among the various possible future outcomes for the US and the global economy, we describe three main scenarios as potential consequences of the introduction of new American tariffs.

#### Tariffs drive re-shoring. Other countries do not retaliate.

*Short run.* After tariffs, imports decline and exports increase. The trade balance improves. National income rises in the US, boosting both saving and investment. Therefore, the interest rate increases. The exchange rate appreciates as well. Tax revenues rise due to higher domestic production. Investment must grow by less than national saving to fill the gap previously covered by foreign capital.

*Medium run.* Inflation, fueled by tariffs and internal demand, reduces the real value of incomes. Additionally, rising input

costs (from imported goods) and higher interest rates (if the FED responds to inflation) may reduce investment, consumption and employment, possibly causing further real appreciation of the dollar. The outcome of this scenario is a tariff driven “stagflation”: a balanced (or even surplus) trade account, but at the cost of a recession. This is reminiscent of South Korea in 1998, when a trade surplus was achieved amid a deep economic and financial crisis (Krugman & Obstfeld, 2021).

#### Tariffs drive re-shoring. Other countries retaliate.

*Short term.* In response to US tariffs, other countries impose their own tariffs or other forms of non-tariff barriers. This would reduce US exports, unexpectedly worsening the trade balance and triggering an economic slowdown. Some (ex)trading partners might respond by devaluing their currencies to regain export competitiveness. Such depreciation would make US goods more expensive abroad, reducing exports and worsening the US trade deficit. This is the strategy currently adopted by China. The same path could be taken by European countries in the absence of a satisfactory agreement.

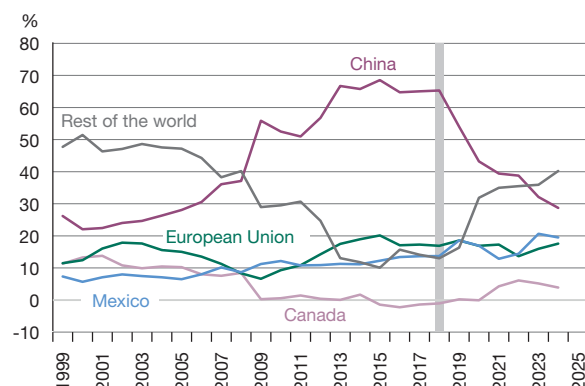
*Medium term.* Former US trading partners may seek to form or strengthen regional economic alliances to create self-sufficient trading blocs capable of withstanding US trade pressure. China could become the leading economic partner of these coalitions. This scenario may potentially result in a more fragmented global trade and financial system, with capital and trade flows increasingly polarised across regions. It may also lead to a redistribution of trade balances among non-US partners (Casarini, 2024).

#### Despite tariffs, firms do not re-shore. Other countries retaliate.

*Short term.* If US firms do not bring production back, the country remains dependent on global supply chains, particularly for goods, whose prices are now artificially inflated by tariffs. In this scenario, the effectiveness of tariffs in protecting domestic industry proves limited as global value chains are too interconnected to be quickly restructured without significant costs. A precedent occurred in 2018, when tariffs on Chinese imports did not reduce the trade deficit but merely altered its geographic composition, shifting trade imbalances to other countries (Figure 4). The overall effect was a worsening of the trade deficit, partly due to the decline in exports. Domestic production suffered, while trade uncertainty increased financial market volatility and reduced credit to households and firms.

*Medium term.* Persistent political and trade uncertainty decreases confidence among households and inves-

**Figure 4**  
**US bilateral goods trade deficits (% of total)**



Note: Change in trade flows following the 2018-2019 tariffs.

Source: Authors' elaboration based on BEA data.

tors — both domestic and foreign — leading to a decline in investment and a rise in precautionary forms of saving. The US economy enters a phase of stagnation or even stagflation due to falling exports, reduced investment and rising costs. US financial assets are no longer seen as a “safe haven”, causing interest rates to rise, and possibly raising the risk of a public finance crisis. The United States could become further isolated in a more unstable global economic and financial environment. American global leadership could be called into question, as new alliances and trade blocs emerge as alternatives to US markets and influence.

### US global role and the MAGA doctrine

The preceding analysis rests on the premise that, in the short run, any change in the trade balance must be offset by an adjustment in national saving, domestic investment, or both. To eliminate the trade deficit, the Trump Administration would need to implement policies that either boost national saving or reduce domestic investment. Higher national saving could result from lower private consumption or a shift to a federal budget surplus. However, such measures are largely incompatible with the Make America Great Again (MAGA) agenda, which emphasises increased domestic growth, investment and consumption in the short term.

The attractiveness of the United States as a destination for direct investment and its structural need to import capital from abroad to sustain technology advancement, innovations and economic growth both contribute to the widening of the trade deficit. This trend has two important consequences. On the one hand, the inflow of financial

resources from abroad supports American productivity and income. On the other, it exacerbates commercial and financial imbalances, increasing the country's net debtor position vis-à-vis the rest of the world.

Given the current stance of the US government, ensuring the medium- and long-term sustainability of the twin deficits will require structural reforms that enhance trade flexibility and expand access to global markets for US services. However, as our analysis has shown, tariffs and protectionist measures are ill-suited to achieve these goals. Rather than fostering competitiveness, such policies generate uncertainty in both financial and real markets. Moreover, they risk alienating key trading partners, who may increasingly seek to establish alternative trade alliances, potentially centered around China, the United States' principal strategic and economic rival.

This last point warrants further reflections. It has recently been observed that if the objective behind the so-called Mar-a-Lago Accord was to diminish the global appeal of the dollar (PIIE, 2025), that goal may have already been “inadvertently” accomplished. Recent capital flight from the dollar and US Treasury bonds, spurred by Trump's protectionist policies, suggests a decline in investor confidence. Historically, however, a central aim of US trade policy has been the expansion of global markets for American goods and services, even at the expense of persistent trade deficits. As De Cecco (2012) noted, the White House has rarely prioritised global market supremacy over national sovereignty. For over seventy years, the US has presided over the international economic order, with the dollar's reserve currency status underpinned not only by economic strength, but also by institutional credibility and military dominance. Within this imperial vision, US policymakers have long tolerated both trade and fiscal deficits, understanding that a negative trade balance is essential to ensure the global circulation of the dollar.

Today, that vision appears increasingly undermined by Trump's agenda, which signals not only a potential end to the postwar US-led economic order, but also a possible shift in global leadership. De-dollarisation is no longer an academic prospect. It is becoming a tangible reality, driven by mounting global mistrust of unilateral American tariffs, the renewed push for monetary sovereignty among emerging economies and the accelerating impact of technology and innovation.

In this contest for global economic primacy, China has emerged as the principal challenger to US dominance. Chinese exports now reach virtually every corner of the globe, forging new trade linkages, even with traditional



US partners in Europe, while China's own domestic demand for foreign goods remains limited, thereby failing to offset the persistent US trade deficit. Beijing's strategy is not merely commercial; it is deeply geopolitical. The structural imbalance in global trade is exacerbated by a growing reliance on Chinese industrial inputs, particularly in high-tech sectors, and by China's substantial holdings of US Treasury securities, estimated at \$700 billion. It is no coincidence that China recently announced the full integration of its digital currency, the digital yuan, into international payment systems. The digital renminbi is already being used in cross-border transactions with ten ASEAN nations and six countries in the Middle East. As a result, more than 38% of global trade could potentially be conducted outside the SWIFT network, and critically, without reliance on the US dollar. This is more than a technology innovation: it is a strategic change. Beijing is actively constructing parallel financial architecture that is faster, cheaper and, most importantly, autonomous from the dollar-based system.

What would happen if the dollar were to experience a significant devaluation? Even though such a devaluation might quickly eliminate the trade deficit, by shifting consumer demand from imported goods and services to domestic alternatives, it would overheat US labour markets. The combination of rising wages and a falling dollar would fuel inflation. The Fed would respond by raising interest rates, curbing US growth. A rapid change in the real value of the dollar and rising interest rates would increase financial market volatility, with spillover effects on credit, consumption and investment both in the US and global economy.

Therefore, a real depreciation of the dollar alone would not place the trade balance on a sustainable trajectory. Without structural adjustments in the United States (specifically, a shift in the balance between national saving and investment) and stronger external demand for US exports, a sharp depreciation could set off a dangerous cycle. While the trade deficit might narrow temporarily, it would soon widen again as underlying imbalances re-surface, now amplified by heightened financial and credit instability.

Over the past two decades, US trade deficits have expanded in tandem with robust domestic economic growth and the emergence of China as a global economic powerhouse. As long as globalisation fueled US productivity and the country remained the anchor of international markets, these deficits were broadly viewed as sustainable. Today, however, persistent internal and external imbalances in the US economy, coupled with China's increasing dominance in global trade, finance and payment systems, are

contributing to a more fragile international environment. In this context, both political and market sensitivities to continued US trade deficits may trigger crises of confidence in American fiscal and external stability, particularly in the absence of credible leadership and a coordinated global strategy for trade rebalancing.

Failure to address the political and structural challenges – both domestically and internationally – raises the risk that the eventual adjustment of the US trade imbalance will be abrupt, costly and disruptive for the global economy.

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