



'President Trump Is Right yet He May Be Wrong'

By Musafir

During the recent G-7 summit in Ottawa, Donald Trump cried foul about trade disparity with Canada and their levying stifling tariffs on US products. Trump's critics went haywire on the U.S. proposing to slap a 25-per-cent tariff on imported steel and a 10-per-cent tariff on imported aluminum. Lots of people in the U.S. were hurt because Mr. Trump flabbergasted all innocent, doll faced Justin Trudeau, the Prime Minister of Canada with harsh criticism about unfair trade on their part. Despite all the criticism and apocalyptic forecasts about repercussion of the Canadian wrath, Mr. Trump is right about the unfair trade. Here are some facts:

Canada charges 245% tariff on American cheese and 298% on American butter above tariff-rate-quota (TRQ levels). Canada provides milk components at discounted prices to domestic processors under the Special Milk Class Permit Program (SMCPP), but charges 275% tariff on the U.S. milk imported by Canada. There are restrictions on U.S. grains imported by Canada. There are barriers to market access by Canadian provinces on U.S. wine, beer and spirits. (Source Export.gov)

There are similar restrictions and tariffs imposed on the U.S agricultural products by the Europeans. I already mentioned those in my previous articles, so I am not going to repeat them here.

However, Mr. Trump's argument about overall U.S trade deficit may be flawed. To start with, we must distinguish between trade deficit and budget deficit. Trade deficit may not be necessarily bad whereas a long term and out of control budget deficit may be cataclysmic.

Trade deficits are not a sign of unfair trade practices or a lack of American competitiveness. This shows the willingness and affordability of the Americans to buy products from foreign countries. For example, we buy coffee from Starbucks because we want to and can afford so. We don't expect Starbucks to buy things from us of equal value. Thus, this transaction cannot be deemed unfair.

When Americans buy imported goods, foreigners must do something with the dollars they earn. They can either use the dollars to buy American exports or invest in American

assets, such as Treasury bills, stocks, real estate, and factories. One reason for a trade deficit is that the deficit country is growing faster than its trading partners. Faster growth attracts investment dollars, which, along with rising incomes, allow the deficit country to buy more imports on the global market.

Mr. Trump should be more worried about our country's budget deficit instead. Fiscal (budget) deficits arise whenever a government spends more money than it brings in during a given fiscal year. If the deficit arises because the government has engaged in extra spending projects – for example, infrastructure spending or grants to businesses – then those sectors chosen to receive the money receive a short-term boost in operations and profitability. However, if the deficit arises because receipts to the government have fallen, either through tax cuts or a decline in business activity, that can be disastrous in the long run.

All government deficits need to be financed. This is initially done through the sale of government securities, such as Treasury bonds (T-bonds). Individuals, businesses and other governments purchase these bonds and lend money to the government with the promise of future payment. So, the day of reckoning will come when the U.S. will have to honor the promised payment.

The scary part is that a major portion of U.S.A's collection goes towards the payment of interest on money that it borrowed. This is just like an individual paying interest alone on credit card debts.

Total government debt has real and negative long-term consequences. If interest payments on the debt ever become untenable through normal tax-and-borrow revenue streams, the government faces three options: cut spending and sell assets to make payments; print money to cover the shortfall; or default on loan obligations. We all know what happens to countries who print money to meet their spending. We don't want to become another Venezuela. Do we?