Flash Economics

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Normal expectations for the US economy

The economic policy being pursued in the United States is likely to have a significant negative impact on the US economy in both the short and long term:

- In the short term, the increase in tariffs (estimated by Yale University at 16 points after the agreement with the European Union) should generate an inflation surplus (of the order of one point) and a slowdown in growth (with inflation not passed on to wages);
- In the short term, immigration restrictions, the depreciation of the U.S. Dollar and the expansionary fiscal policy pursued at full employment will also be inflationary;
- Finally, in the long term, the reduction in federal subsidies to research institutions and universities, and the attacks on research programmes, will reduce the capacity for innovation and therefore the long-term growth of the US economy.

All in all, we can expect:

- Higher inflation, especially in the short term (the inflationary effects of tariffs are transitory);
- A decline in growth, both in the short and long term;
- A less attractive US economy for non-resident investment.

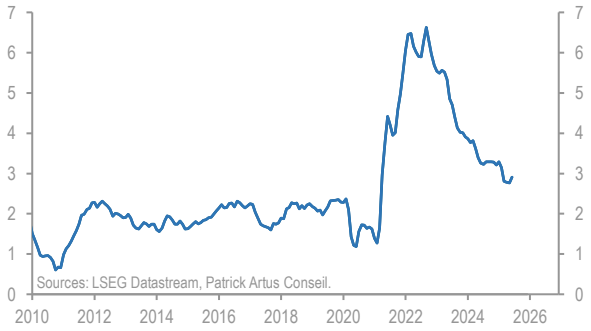
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Effects of the rise in tariffs

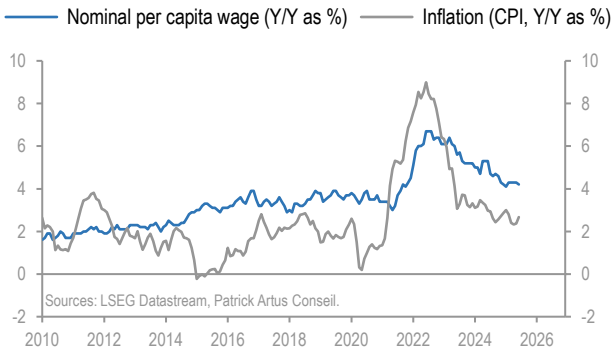
The rise in tariffs (calculated on all US imports) is now 16 points, bringing the tariffs imposed on US imports to around 18%. **The pass-through** is almost 1-for-1, and given the weight of imports in GDP, and the fact that if import prices rise, distributors reduce their profit margins, **the effect of the rise in tariffs on core inflation will be an increase of almost 1 point in core inflation**. Core inflation should be well above 3.5% by the end of 2025 (**Chart 1**) and should normally rise to 3.8%.

Chart 1
United States: Core inflation
(CPI excl. food and energy, Y/Y as %)



A rise in inflation is not followed by a similar rise in wages in the United States (Chart 2).

Chart 2
United States: Nominal per capita wage and inflation



More inflation therefore implies a fall in **household consumption** (**Charts 3A/B**) and hence a fall in growth.

Chart 3A
United States: Household consumption
(in volume terms, Q/Q as % annualised)

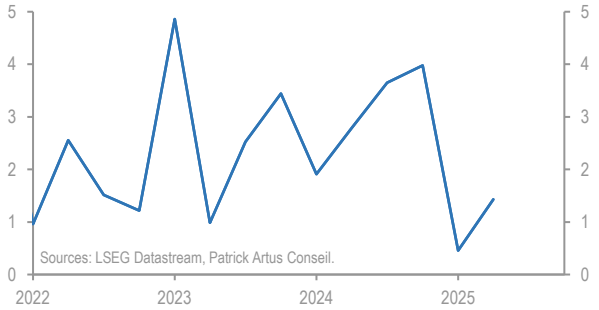
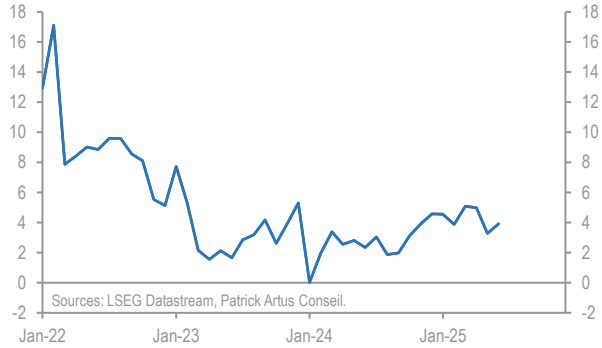


Chart 3B
United States: Retail sales (in value terms, Y/Y as %)



Effects of the anti-immigration policy and the highly expansionary fiscal policy

Immigration has been very high under Joe Biden's presidency: on average, net immigration (including departures) has reached 1,500,000 people per year (Chart 4).

Chart 4
United States: foreign-born population
(as % of the total population)



However, the Trump administration is hostile to immigration and, since the fertility rate has fallen sharply in the United States (Chart 5), without immigration there will be increasing tension on the labour market and greater recruitment difficulties (which are not yet apparent, Chart 6).

Chart 5
United States: Fertility rate (births per woman)

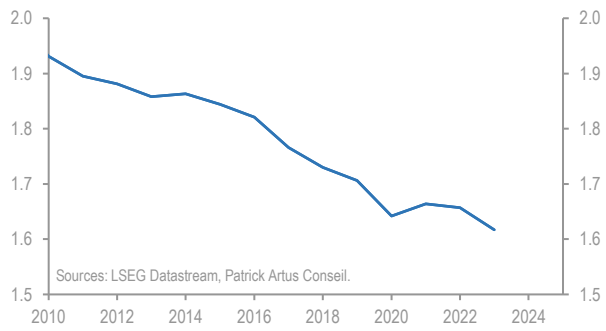
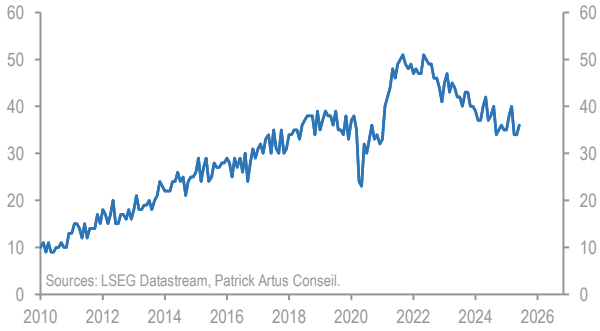


Chart 6
United States: Proportion of companies experiencing recruitment difficulties (as %)



Moreover, with the tax cuts (extension of the Tax Cuts and Jobs Act, tax exemption for tips and overtime pay, tax deductibility of interest on car loans) far exceeding the revenue from the rise in tariffs and the fall in health spending (Medicaid), **fiscal policy will be very expansionary (Chart 7) at a time when the US economy is at full employment** (Chart 8).

Chart 7
United States: Budget deficit (as % of nominal GDP)

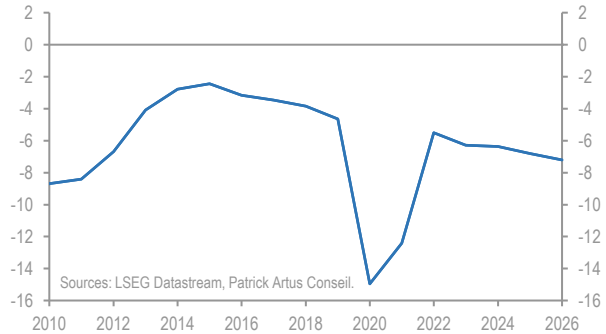
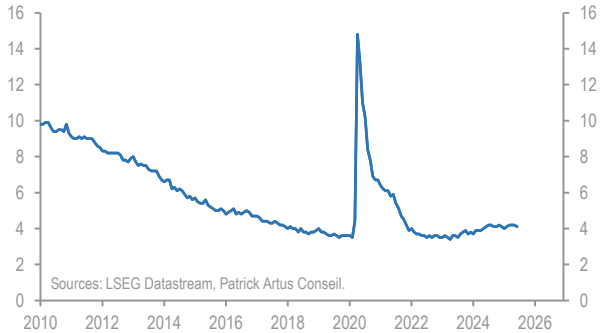


Chart 8
United States: Unemployment rate (as %)



All in all, **with the sharp slowdown in immigration and the very expansionary fiscal policy at full employment, there are two additional sources of inflation**.

Policies hostile to research institutions and universities

The considerable reduction in federal funding for public research institutions - estimated at 33% in total - will have major consequences. The draft budget, which looks set to be rejected by Congress, includes cuts of 25% in funding for NASA, 56% for the National Science Foundation, 55% for the National Institutes of Health, and the complete elimination of research funding for the Environmental Protection Agency. The attacks on elite universities (freezing of research funds, ban on enrolling foreign students) and the reduction in federal funding will result in cuts in staff numbers and research activities, **and in the medium term will slow down innovation and therefore reduce productivity gains** (**Charts 9/10**).

Chart 9
United States: R&D expenditures in the business, government, and higher education sectors (as % of nominal GDP)

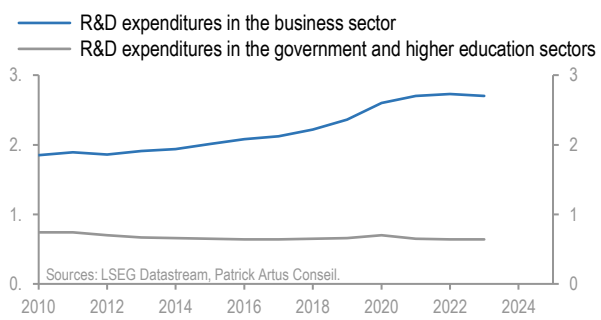


Chart 10
United States: Productivity per head (2002.Q1 = 100)

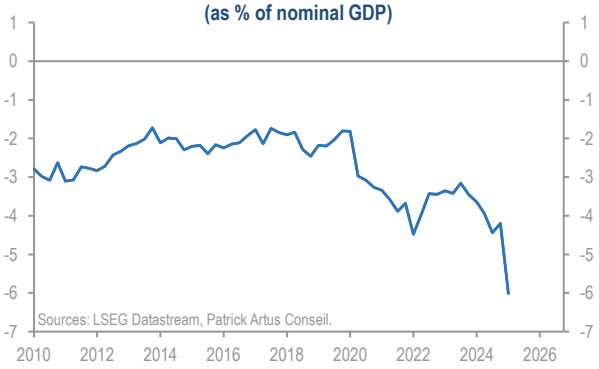


Summary: All in all, what can we expect for the US economy?

As can be seen from the above, the US economy is likely to experience:

- **Higher inflation**, with the short-term effect of the sharp rise in tariffs and the medium-term effects of immigration restrictions and expansionary fiscal policy at full employment;
- **A fall in growth**, with the negative impact of inflation on household consumption and, in the medium and long term, the impact of the decline in federal funding for public research institutions and universities;
- **A decline in the attractiveness of the US economy to non-resident investors**, with a decline in growth and innovation. This decline in the attractiveness of the US is particularly serious, because it jeopardises the US's ability to finance its current account deficit (Chart 11).

Chart 11
United States: Current account balance (as % of nominal GDP)



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