Flash Economics

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Does Donald Trump understand that he needs investment from non-residents?

Donald Trump has already backed many measures that would make the United States less attractive to non-residents:

- Higher tariffs, which will generate additional inflation and reduce household purchasing power and consumption;
- A more expansionary monetary policy, which would lead to a depreciation of the U.S. dollar;
- Section 899 of the tax bill (the 'Big Beautiful Bill Act'), which threatens to tax individuals, companies and foreign investors, including sovereign investors, operating in the United States (up to 20% additional tax) on their income in the United States; this proposal concerns corporate income (dividends) and bond income; it would apply to residents of countries with tax practices deemed 'discriminatory'.

If the U.S. dollar depreciates, or if US growth is slowed, or if financial assets (stocks, bonds, shares in companies) held by non-residents are taxed, demand from non-residents for US stocks, bonds and shares in companies will fall. And since the US public deficit will continue to be very high, there will be 'twin deficits' with a very high current account deficit. The risk is that the fall in demand for U.S. dollar-denominated assets from non-residents will lead to a balance of payments crisis in the United States, with capital inflows insufficient to finance the external deficit, or even with capital outflows from the United States.

The consequences of a balance of payments crisis are well known: recession, depreciation of the exchange rate, higher interest rates, all of which would help to rebalance foreign trade.

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Several economic policy decisions that could make the United States less attractive to non-residents

Donald Trump has taken several economic policy decisions or is supporting economic policy guidelines that will (or could) **reduce the attractiveness of the United States for non-residents**.

These include:

- The increase in tariffs, which will generate additional inflation (**Chart 1**), thereby reducing household purchasing power and consumption. We can already see the deterioration in the growth outlook (**Chart 2**) and the slowdown in job creation (**Chart 3**);

Chart 1
United States: Consumer's inflation expectations for the year ahead (as %, Conference Board)



Chart 2
United States: Manufacturing and Nonmanufacturers PMI (indices)

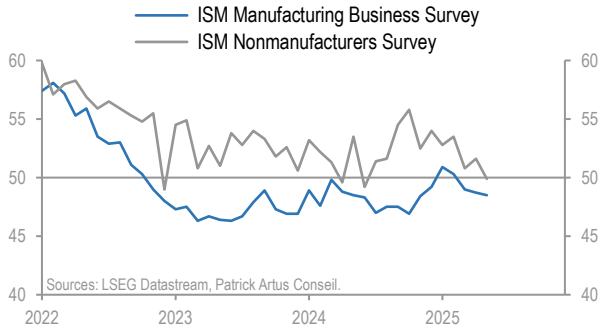
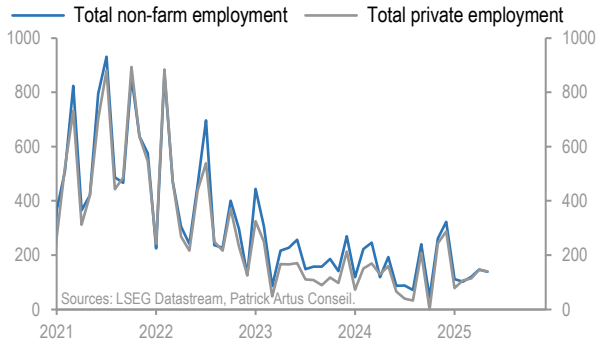


Chart 3
United States: Change in payroll employment (M/M, thousands of person)



- **A more expansionary monetary policy**, which is desired by Donald Trump, and which would lead to a depreciation of the U.S. dollar, (**Chart 4**);

Chart 4
Euro/dollar exchange rate (EUR 1 = USD...)



- **The proposal, already approved by the House of Representatives, to tax the income of non-residents** based on their holdings of shares in companies, stocks or bonds in the United States (section 899 of the Big Beautiful Bill) if the countries of origin of these non-residents have **discriminatory tax regimes** (for example, they adhere to the OECD's proposal for minimum taxation of multinationals, or the European proposal for taxation of digital companies, which is already being applied in France and Germany).

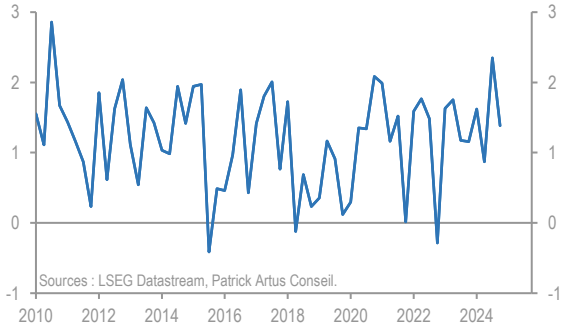
What are the consequences if these economic policy choices are made?

If indeed:

- Economic growth in the United States is slowed by tariffs and the resulting inflation ;
- The U.S. dollar depreciates as monetary policy becomes more expansionary following the departure of Jerome Powell;
- The income of non-residents generated in the United States is overtaxed;

We can expect **demand from non-residents for US equities, bonds and shares in US companies to fall** (**Chart 5**).

Chart 5
United States: Direct and portfolio investment inflows (as % of nominal GDP)

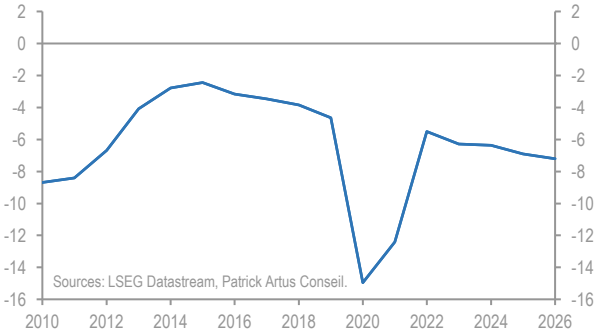


(*) Direct and portfolio investment inflows are capital inflows leading to an increase in liabilities (in this case for the United States) and therefore have a positive sign.

The United States will have twin deficits

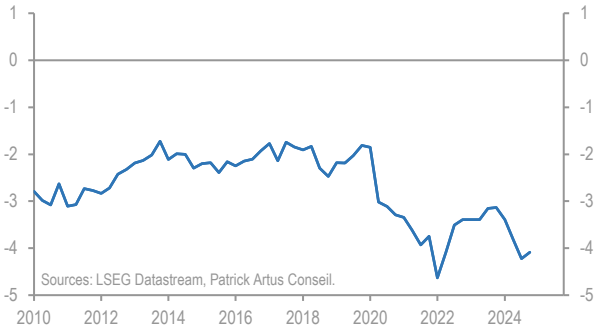
The fiscal policy proposed by the Trump administration is highly expansionary. With the tax cuts (extension of the Tax Cuts and Jobs Act tax cuts, exemption for tips and overtime) only very partially offset by a fall in public spending (reduction in the generosity of Medicaid), **the US public deficit will probably reach 6.9% of GDP in fiscal year 2025 and more than 7% of GDP in subsequent fiscal years** (**Chart 6**).

Chart 6
United States: Budget deficit (as % of nominal GDP)



This very large public deficit will **exacerbate the US savings deficit, resulting in a continuing large current account deficit** (**Chart 7**).

Chart 7
United States: Current account balance
(as % of nominal GDP)



Summary: if there is a fall in demand for US assets from non-residents, this current account deficit will not be financeable

If non-residents invest less (in stocks, bonds and shares in US companies), or even withdraw capital from the United States, such **a large current account deficit will not be financeable**.

The US current **account deficit will then have to be reduced rapidly, which implies**:

- Recession (Chart 2, above) ;
- Depreciation of the U.S. dollar (Chart 4, above) ;
- Higher long-term interest rates (**Chart 8**);

Chart 8
United States: Interest rate on 10-year government bonds
(as %)



All of which will help to reduce the US external deficit.

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