



Will Tariffs Balance the Books?

Imagine a household that consistently spends more than it earns in income. To cover the cash flow deficit, the household borrows money to float the difference. The household believes that all it needs to do is to earn more money and it will be able to get out of its debt spiral. Alas, after months of searching, a member of the household attains a new job that pays 25% more. It now has more disposable income to put toward paying off debt. One year goes by and we check back in with its progress, but it appears nothing changed. In fact, the household debt level is higher than it was before the new job! What happened? It turns out, the behavior never changed. Although its income had increased by 25%, the household simply increased its spending, maintaining the same proportionate cash flow deficit and financing loop.

How does the above scenario relate in any way to the tariff policy implemented by the current White House Administration? Well, the current Administration has communicated several reasons for the implementation of its tariff policy; primarily to “close” the U.S. trade deficits with various countries and to reshore domestic production. What seems to be misunderstood is the fact that the U.S. trade deficits (synonymous with current account deficit in this report) are touted to be the result of unfair trade policies with U.S. trading partners, rather than an economic necessity since the U.S. as a country, in effect, spends more than it earns just like our hypothetical household. This is not to opine on the veracity of such tariff policy justifications or whether trade deficits are inherently good or bad. Rather, it is to explain that such tariffs will not accomplish its apparent task of “closing” trade deficits without a change in behavior.

To show this, let's look at some economic bookkeeping. The level of a country's economy or output is represented by its Gross Domestic Product (GDP), calculated using the expenditure approach:

$$GDP = C + I + G + (X - M)$$

C=Private Consumption; I=Private Domestic Investment; G=Government Expenditures; X - M=Net Exports

This formula captures: final household consumption of durable goods, nondurable goods, and services (**C**); private domestic investment of property, plant, & equipment, net change in inventories, and residential property construction (**I**); federal,

state, & local government expenditures on goods and services and investment of property, plant, & equipment, excluding transfer payments and interest payments (**G**); exports (**X**) minus imports (**M**) of goods and services.

A country's gross output must equal its gross income, or Gross National Income (GNI):

$$GNI = C + S + T$$

C=Private Consumption; S=Private Savings; T=Net Taxes

This formula captures: final household consumption of durable goods, nondurable goods, and services (**C**); private savings, i.e. the portion of income that is not spent on consumption or taxes (**S**); net taxes paid by households and businesses, i.e. gross taxes paid minus transfer payments, subsidies, & benefits received (**T**).

Since GDP must equal GNI, we can equate the two formulas and solve for net exports (in this context the current account deficit). By doing so, we get the following economic identity:

$$(X - M) = (S - I) + (T - G)$$

X - M=Current Account; S=Private Savings; I=Private Domestic Investment; T=Net Taxes; G=Government Expenditures

The current account is influenced by two major economic components: the net private savings by households and businesses (**S-I**) and the net public savings by federal, state, & local governments (**T-G**). For example, if both components are negative, the current account will be negative, since the country must import goods & services to fund domestic investments that exceed private savings (**S-I**) and government expenditures that exceed net tax receipts (**T-G**).

To put this economic identity into context, the U.S. reported a 2024 current account deficit of approximately $-\$1.11T$ ¹. Plugging in the components of the identity using data from the Bureau of Economic Analysis (BEA), you get the following approximation:

$$-\$1.11T = (\$6.2T - \$5.2T) + (\$3T - \$5.1T)$$

$$(X - M) = (S - I) + (T - G)$$

Condensing the formula further, you get the following:

$$-\$1.11T = \$0.96T - \$2.1T$$

Current Account = Net Private Savings + Net Government Savings

¹ <https://www.bea.gov/news/2025/us-international-transactions-4th-quarter-and-year-2024>

<i>\$ in Billions</i>	<i>Q4 2024</i>	<i>NIPA Table 5.1¹</i>
Net Private Savings	2,153	Line 3
Private Consumption of Fixed Capital	4,091	Line 14
Gross Private Savings (S)	\$6,244	
Gross Domestic Investment (I)	\$5,289	Line 22
Net Private Savings	\$955	

<i>\$ in Billions</i>	<i>Q4 2024</i>	<i>NIPA Table 3.1²</i>
Tax Receipts	5,836	Line 2
Social Insurance Contributions	1,931	Line 7
Gross Taxes	\$7,767	
Transfer Payments	(4,626)	Line 22
Subsidies	(94)	Line 30
Net Taxes (T)	\$3,046	
Consumption	3,997	Line 21
Investment	1,103	Line 39
Total Expenditures (G)	\$5,100	
Net Government Savings	(\$2,054)	

Although in 2024 the U.S. had positive net private savings of just under \$1 trillion, net government savings was negative \$2 trillion, resulting in the current account deficit of approximately \$1 trillion, which necessitated the importation of capital to fund the excess public expenditures.

Assuming the tariffs are successful in boosting domestic production and trade deals result in increased exports with trading partners, all else equal, would this in itself help to close the current account deficit? Not if net private savings and/or net government savings don't change. Or in other words, not if the U.S. continues to spend more than it earns in aggregate. Although the U.S. may be "richer" as a result of the increased domestic economic activity through increased GDP/GNI, that doesn't necessarily mean the level of savings will change. What's stopping private and government constituents from increasing their levels of consumption and investment proportionate with the increase in income, similar to our hypothetical household?

Of course this is just economic bookkeeping to help understand the economic drivers of the current account deficit and not behavioral causation. Pulling levers to try to affect the various components will ultimately have cascading behavioral effects on one another that could enhance or deter the original intent. With that being said, tariffs and trade deals alone will not close the current account deficit. The U.S. must either have higher gross private savings (**S**), lower domestic investment (**I**), higher net taxes (**T**), lower government expenditures (**G**), or a combination thereof. So far, "positive" changes to any of these in pursuit of closing the current account deficit remains to be seen, regardless if said changes to any of the above would actually be economically beneficial for the country.

1. [NIPA Table 5.1](#)

2. [NIPA Table 3.1](#)



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