



The Optimal Macro Tariff

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What is the optimal macroeconomic tariff when trade is imbalanced and the policy objectives go beyond social welfare and also include fiscal revenues, increasing the number of manufacturing jobs, and closing a trade deficit? We study these questions in an environment which allows for long-run bilateral and aggregate trade deficits that reflect the country's net foreign asset position and differential returns on foreign assets and liabilities (the "exorbitant privilege"). Only in special cases does the optimal tariff emerge as an increasing function of a trade deficit and for reasons unrelated to trade competitiveness. Instead, the planner trades off the conventional benefits of improved terms of trade with the costs from negative valuation effects on the country's *gross* financial position. This reduces the optimal tariff for the United States three-fold, from 34% to 9%, and acts as an effective hedge for its trade partners against a trade war. In contrast to the expenditure switching logic and Lerner symmetry, closing the trade imbalance calls for an appreciation of the dollar to a level that depends solely on the US external financial position, and not on trade shares or trade elasticities, and can be achieved by means of an import tariff or an export subsidy. Alternatively, financial and trade rebalancing may happen if a tariff war results in the loss of privilege and the associated dollar depreciation.