Donald Trump's tax reform is putting the rest of the world under pressure to act. But copying the US model would be the wrong response from Europe

by Christian Kullmann

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No one is obligated to like Donald Trump or to approve of his political measures. His isolationist ideas, unilateral US initiatives, and tariff barriers are not blueprints that can be used to solve the global problems of our time. But in spite of the backward-looking ideology that shows through in Trump's program, we have to take his political actions seriously. And that obligation, of course, has consequences for the whole world.

With his tax policy, the US president has achieved his first major political success on the domestic front. Trump is a businessman, and he has done something that makes many businesspeople happy: He has drastically cut taxes. For companies all over the country, federal taxes have been lowered from 35 to 21 percent. If we add the varying tax rates in the individual states, US businesses will have a total tax rate of 25 percent on average. That's 13 percentage points less than before.

Opinions may differ as to why this tax cut is coming in the midst of an economic boom and about its long-term consequences, as it has massively increased the USA's debt burden. But Trump is defining the rules, and the world is reacting because it's being forced to react. China, the world's second-largest economy, immediately raised the possibility of lowering its taxes on investments. Other countries will follow its lead.

Is this the beginning of a golden age for companies? Absolutely not. In the first place, it's questionable how long the lower tax rates can be sustained by the US economy. The upward spiral of national debt cannot continue indefinitely. The US government, like other governments, is responsible for future generations. Secondly, it's true that low tax rates directly favor corporate investments. However, ultimately local market opportunities are the factor that determines lasting success. Favorable fiscal conditions are hardly a good basis for strategic growth plans, because they can quickly change as a result of the national budget situation and the composition of the government.

Finally, negative side effects of Trump's drastic measures can already be seen. The president is vehemently proclaiming import taxes on foreign products. Such plans simply ignore the fact that for large regions of the world free trade is a strong engine of prosperity. Thanks to years of increasing convergence, the tariffs on the transatlantic trade in goods now average two percent. That has especially benefited trade between North America and Germany. Only a few exceptional products still reflect the protectionism of bygone eras. But now we can expect a return to tariffs of 25 percent on US imports of steel, for example.

How should Europe, and Germany in particular, react to that? To put it plainly, neither the creation of new tariff barriers at the EU's outer borders nor Germany's entry into an international tax-dumping competition would be the right answer. The European Union depends on free trade, and it therefore should not respond to bad politics with bad countermeasures. In Germany, the focus on consolidating state finances after decades of lacking accountability has only just gained genuine political importance. This policy should not now be carelessly sacrificed; instead, it should continue to serve our long-term interests.

Rather than engaging in a race to the bottom with the USA and Asia regarding corporate taxes, Europe should harmonize the tax rates within the EU. At the moment, EU states that have close political ties are still competing with each other through their fiscal policies. Today, 25 years after the founding of the European single market, the tax landscape within Europe still looks like the patchwork of small countries of the prewar era. Many cross-border companies would benefit from a harmonization of corporate taxes at the EU level, if only because of the elimination of the related administrative costs.

This harmonization should not be oriented toward Irish dumping-level tax rates nor toward the highest bidders. Under President Macron, France is leading the way by lowering its corporate tax rate from 33 to 25 percent, thus moving in the direction of the European average. This is an exemplary response to the "going it alone" approach on the other side of the Atlantic. We need to forge ahead with the integration of the European economic region, while at the same time strengthening the competitiveness of the businesses within it.