

An Analysis of Trump's Tariff Policy

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Examining the rationale for Trump's tariffs, this article argues that while tariffs are problematic as a policy instrument, the Trump administration is strategically deploying them in an attempt to address large current account deficits. It identifies the countries that are most vulnerable to Trump's tariffs and measures vulnerability by calculating the share of each country's exports to the United States relative to their gross domestic product. As an exercise, it examines the bilateral trade of the us with Canada, China, India, and Mexico.

On the night of 5 November 2024, when it became evident that Donald Trump was likely to win the election, urgent calls were made from the United States (us) toy, shoe, apparel, and electronic items sellers to their respective agents in China, urging them to ship as many items as possible. These us importers of Chinese goods wanted to stock up on inventory before Trump's tariffs were implemented. A study by the National Retail Federation estimated that Trump's proposed tariffs on apparel, toys, furniture, appliances, footwear, and travel goods could cost consumers an additional \$46 billion to \$78 billion annually (NRF 2024). On 1 February 2025, Trump announced a 25% tariff on goods from Canada and Mexico, and a 10% tariff on China.¹ This 25% tariff applies to goods from Canada and Mexico that fail to meet the rules of origin (ROO) criteria under the 1994 Uruguay Round of the General Agreement on Tariffs and Trade (GATT), while products that comply with the United States–Mexico–Canada Agreement (USMCA) continue to benefit from 0% duty rates.² Two days later, Trump paused all tariffs on Canada and Mexico for 30 days, but a 10% tariff on China went into effect from 4 February. The paused tariffs on Canada and Mexico went into effect on 4 March, but many of those were suspended again after two days.

This imposition and the suspension of tariffs caused a lot of confusion among us trading partners and investors (Minsberg 2025). On 12 March, the us government implemented a 25% tariff on all foreign steel and aluminium products. On 2 April, Trump announced "Liberation Day tariffs," which are reciprocal tariffs that include a universal 10% base rate with additional

country-specific levies targeting approximately 90 countries. While Trump 1.0 (2017–21) used Sections 232 (national security) and 301 (unfair trade practices) to target specific products like steel and aluminium, Trump 2.0 (2025–29) employs the International Emergency Economic Powers Act (IEEPA), 1977 for sweeping tariffs on major trading partners.³

In this article, we examine the rationale for Trump's tariffs. While acknowledging that tariffs are problematic as a policy tool, we argue that the Trump administration is strategically deploying them to reduce current account deficits and restore us manufacturing jobs (Shakil 2025). Using data from the Office of the United States Trade Representatives (USTR), we identify the countries that are the most vulnerable to Trump's tariffs (USTR 2024). As an exercise, we examine the bilateral trade of the us with Canada, China, India, and Mexico. For China, one of its largest trading partners, tariffs have not been effective, with a reduced trade dependency on the us (Bown 2022). However, that may not be the case for the two other important trading partners, namely Canada and Mexico, whose trade dependence on the us has increased over time. This result aligns with the gravity model theory of international trade. The gravity model assumes that the volume of trade between two countries is directly related to their economic sizes (usually measured by GDP) and inversely related to the distance between them (Tinbergen 1962).

Tariff and Its Economic Impact

Trump's idea of imposing tariffs is built around the narrative of "Make America Great Again." He believes that tariffs will reduce the trade deficit by encouraging foreign companies to invest in the us, which will create more jobs and generate income.⁴ In 2017, when Trump took office for his first term, the us had a trade deficit with 116 countries (Gera 2025). In 2024, the us had its largest trade deficit with China, totalling \$295.4 billion, followed by Mexico, totalling \$171.8 billion, and a deficit of \$45.7 billion

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with India (USTR 2024). Geographically, there are several countries around the world that have historically maintained trade surpluses. For example, many countries in developing Asia, particularly China and Japan, as well as oil-producing nations in West Asia, are notable for this trend. On the other hand, the us and some European countries, such as Greece, Ireland, Italy, and Portugal, have trade deficits. This global trade imbalance has decreased over time, and the current account deficit of the us relative to the rest of the world is shrinking (Abraham and Ray 2020). However, Trump argues that there is a need for a further reduction in tariffs and noted: “Our allies are worse than our enemies when it comes to import taxes” (BBC 2025).

Contrary to Trump’s belief, a substantial body of academic literature suggests that tariffs are generally harmful to economic growth, global trade, and consumer welfare. One of the fundamental arguments against tariffs comes from classical economic theory, particularly from the works of Adam Smith and David Ricardo. Smith argued that free trade promotes specialisation and efficiency, while Ricardo demonstrated that countries benefit from comparative advantage. By hindering efficient resource allocation, tariffs result in higher prices for consumers.

During his previous presidency (Trump 1.0), imposition of tariffs resulted in a nearly complete pass-through of costs to the consumers, who paid higher prices (Amiti et al 2019). Higher tariffs are expected to increase domestic inflation, making it harder for the Federal Reserve to cut interest rates and increasing the cost of capital for American businesses.

In addition to the higher cost of capital, American businesses lose out as they are part of an integrated global supply chain network. Tariffs disrupt these supply chains by making inputs more expensive, reducing competitiveness in industries such as manufacturing and technology. Tariffs reduce firm-level productivity and discourage multinational investment, leading to long-term economic disadvantages (Yang et al 2021).

Tariffs-induced retaliatory measures and the ensuing trade wars can destabilise the global economy. The Smoot–Hawley Tariff Act, 1930 is a well-documented example, as it led to widespread retaliation from us trading partners and exacerbated the Great Depression of 1929. The us–China trade war demonstrated similar effects, as tariffs led to job losses in export-dependent industries and disruptions in global supply chains. The us exports to China supported 1.2 million jobs, while 1,97,000 people were employed by Chinese multinationals—both affected by tariff escalation (Lawder 2021).

Although tariffs generate revenue for the government, existing analyses find that, from a consumption perspective, low- and middle-income households benefit substantially more from trade than high-income households. This is largely because lower-income households spend a greater proportion of their income on tradable goods such as food and apparel (Fajgelbaum and Khandelwal 2016).

Although wto rules prohibit imposing differential most favoured nation (MFN) tariffs, any country can still adjust its applied tariffs as long as it remains below the bound rates (Table 1). Preferential tariffs are permitted under free trade agreements (FTAs) and custom unions. Section xxiv.8(b) of the GATT allows members to deviate from the MFN clause. Section xxiv.8(b) requires member countries to eliminate customs duties and other trade barriers on “substantially all the trade” within the FTA and customs union.⁵

It should be noted that tariffs alone may not create market access problems. Adding non-tariff measures (NTMs) such as anti-dumping and countervailing measures, safeguard duties, phytosanitary

sanctions, etc, on imports may restrict market access.⁶ Ever since the formation of the wto on 1 January 1995, tariffs have declined, while NTMs have increased (Banik 2001).

Rationale for Trump’s Tariff

Under the us Trade Facilitation and Trade Enforcement Act (TFTEA), 2015, the us Treasury places countries on the monitoring list based on five criteria: (i) a significant bilateral trade surplus with the us of at least \$20 billion; (ii) the trading partner’s current account surplus exceeds 3% of its GDP; (iii) intervention in the form of net purchases of foreign currency, which may occur when a higher trade deficit for the us results in less demand for the dollar, or the trading country is engaged in currency manipulation, for instance, undervaluing its currency; (iv) countries that may be engaging in unfair trade practices, such as providing subsidies to domestic industries, violations of intellectual property rights, or barriers to us exports; and (v) whether countries are adhering to international trade rules and agreements, including wto obligations and any bilateral or multilateral trade deals with the us (Neville 2016).

According to the latest report released by the USTR on 14 November 2024, no major trading partner met all five criteria for enhanced analysis under the TFTEA during the four quarters ending in June 2024 (us Treasury 2024). The Treasury reviewed and assessed the policies of major us trading partners, which account for approximately 78% of us foreign trade

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Table 1: Tariffs Structure of the Reference Countries, 2024

Countries	Simple Average		Number of MFN Applied Tariff Lines
	Bound ^a	MFN ^b	
China	10	7.5	9,004
Canada	6.6	3.8	7,106
India	50.8	17.0	12,302
US	3.4	3.3	11,960

a The bound tariff is the maximum MFN tariff level for a given commodity line.

b MFN tariffs are what countries promise to impose on imports from other members of the WTO, unless the country is part of a preferential trade agreement.

Source: World Trade Organization (2024).

in goods and services. The report identified seven economies on the “Monitoring List” on the basis of their currency trading practices and macroeconomic policies. These countries are China, Japan, South Korea, Singapore, Taiwan, Vietnam, and Germany, all of which have trade surpluses with the us. Additionally, the us Treasury is concerned about China’s failure to publish foreign exchange interventions and the broader lack of transparency regarding key aspects of its exchange rate policy. Although not included in the monitoring list, Trump began targeting Canada and Mexico within the first three months of taking office.

Analysing US Trade War

To understand which countries are more vulnerable to the us tariffs, we consider two criteria. First, we analyse the exports

Table 2: Exports from Trading Partners as a Percentage of US GDP

Years	Canada	China	India	Mexico
2009	1.6	2.0	0.15	1.2
2010	1.8	2.4	0.20	1.5
2011	2.0	2.6	0.23	1.7
2012	2.0	2.6	0.25	1.7
2013	2.0	2.6	0.25	1.7
2014	2.0	2.7	0.26	1.7
2015	1.6	2.6	0.24	1.6
2016	1.5	2.5	0.24	1.6
2017	1.5	2.6	0.25	1.6
2018	1.5	2.6	0.26	1.7
2019	1.5	2.1	0.27	1.7
2020	1.3	2.0	0.24	1.5
2021	1.5	2.1	0.31	1.6
2022	1.7	2.1	0.33	1.7
2023	1.5	1.5	0.30	1.7
2024	1.4	1.5	0.30	1.7

Source: United States Census Bureau, Federal Bank of St Louis (2022), and authors’ calculation.

Table 3: Trading Partners’ Exports to the US as a Percentage of Their GDP

Years	India	China	Mexico	Canada
2009	1.6	5.8	18.7	16.5
2010	1.8	6.0	20.8	17.2
2011	2.0	5.3	21.4	17.6
2012	2.2	5.0	22.1	17.7
2013	2.3	4.6	21.1	18.0
2014	2.2	4.5	21.7	19.3
2015	2.1	4.4	24.4	19.0
2016	2.0	4.1	26.4	18.2
2017	1.8	4.1	26.3	18.1
2018	2.0	3.9	27.4	18.5
2019	2.0	3.1	27.3	18.3
2020	1.9	2.9	28.9	16.3
2021	2.3	2.8	29.1	17.8
2022	2.6	3.0	30.9	20.2
2023	2.3	2.4	26.6	19.5
2024	2.5	2.4	28.3	19.3

Source: United States Census Bureau, Federal Bank of St Louis, and authors’ calculation.

from trading partners as a percentage of us GDP (Table 2). And second, we analyse trading partners’ exports to the us as a percentage of their GDP (Table 3). We argue that the higher the numbers, the more vulnerable the countries are to the us tariffs.

We consider the time period between 2009 and 2024 to observe the trade variables during the tenure of Obama (2009–17), Trump 1.0 (2017–21), and Biden (2021–25). Between 2009 and 2024, us-bound exports as a percentage of GDP increased significantly for Canada and Mexico, declined for China, and grew marginally for India.

In fact, data show that the us trade deficit with China continued to increase even after the major tariff announcement during Trump 1.0 (Figure 1). The average annual trade deficit with China was \$311 billion during Obama’s tenure, rose to \$361 billion during Trump 1.0, and decreased to \$327 billion under Biden (us Census Bureau 2024). Considering Canada, Mexico and India as trading partners, the us trade deficit continued to increase.

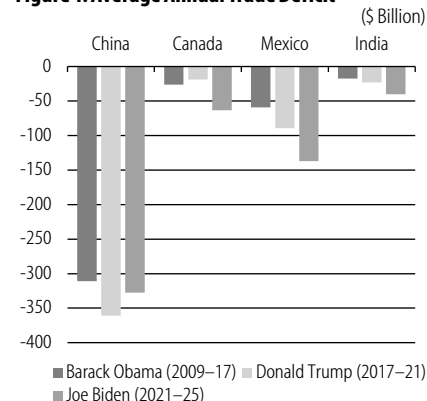
Tariffs War with China

From a higher 145% tariff on Chinese goods starting 2 April, the us subsequently reduced it to 30% following China’s threat to curtail rare earth mineral exports vital to American defence, automotive, and electronics sectors (Table 4). Following a Trump–Xi call in June, China agreed to lift rare earth export restrictions in exchange for the us removing chip-design software export bans. On 11 June, Trump announced that a trade deal with China that would maintain the current 20% “fentanyl” and 10% “reciprocal” tariffs, resulting in 30% overall tariffs on Chinese goods, while pausing higher tariffs for 60 days.

Table 4: Trump 2.0—Tariff Timeline for China in 2025

Dates	Action	Details
2 February	Initial tariffs announced	10% tariffs on imports from China
4 February	Tariffs implemented	10% increase in tariffs from China implemented
4 March	Second round of tariffs increased	Additional 10% increase in tariffs from China
2 April	Reciprocal tariffs	20% plus 125% in additional “reciprocal” tariffs under the Liberation Day Tariff programme, taking tariffs on Chinese goods to 145%
12 May	Tariffs pause agreement signed in Geneva	The US and China reached a 90-day tariff truce agreement, implementing substantial reductions—the US cut tariffs from 145% to 30% and China reduced rates from 125% to 10%

Figure 1: Average Annual Trade Deficit



Source: US Census Bureau, 2024, and authors’ calculation.

On 11 August, Trump announced that the increase in the reciprocal tariff to 125% would be paused for another 90 days. Trump also reversed his previous ban and permitted Nvidia to sell advanced chips to China, requiring the company to pay 15% of its China sales to the federal government (Kozul-Wright 2025).

Tariffs may not be effective in containing Chinese imports, as trade interdependence between the us and China has decreased during the past decade. Between 2018 and 2024, China’s share of trade with the us fell from 15.7% to 10.9% (Saito and Scott 2025). China is also able to overcome NTMs aimed at its exports. The Global Trade Alert (2024), a database tracking protectionist measures, reveals that the us has initiated more than 4,525 protectionist measures against Chinese exports. To evade these tariffs and NTMs, the Chinese firms have shifted their production base and started investing in Asia, Africa, Central America, and, to some extent, Latin America.

This strategy has led to two key outcomes. First, since production costs are lower in these regions, Chinese firms are benefiting from shifting their production bases outside of China, particularly

in Southeast Asia (Banik 2011). The loss in exports from China to the us is increasingly being offset by exports from countries in Southeast Asia, with us imports from the region rising by 12% between 2018 and 2022 (Freund et al 2024). Vietnam, Malaysia, and Thailand have emerged as primary beneficiaries. Vietnam's exports to the us surged by 40% between 2017 and 2020, reflecting the broader trend of Chinese manufacturers shifting final assembly to third-party countries in order to bypass tariffs (Antràs 2020).

Second, to benefit from the USMCA, Chinese firms are relocating their production base closer to the us. In April 2024, us Trade Representative Katherine Tai accused China of disguising its steel products as Mexican steel to enter the us market. In 2023, us imports of Mexican goods totalled \$475 billion, approximately \$20 billion more than in 2022 (Tai 2025). During the same time, the us imports of Chinese goods amounted to \$427 billion, around \$10 billion less. An estimated \$3.7 billion of Chinese FDI came to Mexico in 2023, significantly higher than the average flow of \$1.3 billion during the past decade. At least 30 Chinese firms now operate out of Mexico, including Chinese automobile giants such as BYD and Cherry International (Banik 2025). The flow of Chinese FDI to Mexico has also increased by 30% during the last two years.

Tariffs War with Canada and Mexico

For Canada, the us is the largest trading partner, making it highly vulnerable to tariff-based trade disruptions. In particular, due to a 25% tariff on steel and a 10% tariff on aluminium products imposed in March 2025, along with tariffs on various other goods such as Canadian lumber, the us automobile and aircraft manufacturers and home builders will face higher production costs.

As a retaliatory measure, Canada has announced immediate 25% tariffs on \$20.7 billion worth of us imports, with the potential to extend these measures to an additional \$86.2 billion if the us tariffs remain in place beyond 21 days (Lawder et al 2025). Canada

imposed tariffs on us products such as soybeans, dairy products, ketchup, whisky, and mattresses. Canada has threatened to impose a 100% tax on ev giant Tesla and surcharges on electricity to us customers (Lubin 2025). Mexico, similarly, faced significant trade disruptions (Table 5).

Tariffs War with India

During Trump 1.0, he labelled India as the “tariff king” and removed India from the Generalised System of Preferences (GSP). Under the GSP, established by the Trade Act, 1974, us policymakers allowed imports of around 3,500 products from designated beneficiary countries—

primarily low-income nations—at a preferential duty-free (zero-tariff) rate.⁷ A quick review of the items qualified under the GSP reveals that they primarily fall under categories such as textiles and apparel, watches, footwear, work gloves, automotive components, certain engineering goods (nuclear boilers, machinery, and mechanical appliances), and leather apparel. However, the value of these items as a proportion of total Indian exports to the us was relatively small. According to the estimates from the Ministry of Commerce, Government of India (GoI), India's exports to the us mainly comprised diamonds (19%), packaged medicaments (14%), refined

Table 5: Trump 2.0 Tariff Timeline for Canada and Mexico in 2025

Dates	Action	Details
20 January	Announcement of proposed tariffs	Trump announces his intent to impose 25% tariffs on imports from Canada and Mexico
1 February	Executive order signed	25% tariffs imposed on imports from Canada and Mexico
3 February	Tariffs paused	Trump pauses tariffs on Canada and Mexico for 30 days
27 February	Reinstatement of tariffs declared	Trump confirms tariffs on Mexico and Canada will go into effect starting 4 March
4 March	Tariffs go into effect	25% tariffs on all imports from Canada and Mexico were implemented
5 March	Pausing of automobile tariff	Under pressure from US automobile manufacturers, Trump pauses tariffs on autos and parts from Canada and Mexico
6 March	Broader tariffs suspension	Most Canadian and Mexican goods receive tariff relief, but steel and aluminium products remain subject to 25% tariffs starting 12 March
11 March	Tension with Canada	Trump threatens to double tariffs on Canadian steel and aluminium after Canada retaliates with electricity surcharges. Both sides de-escalate later
26 March	Global auto tariff	Trump imposed a 25% tariff on all cars and car parts, including products from Canada and Mexico
9 April	Suspension of reciprocal tariffs	Trump reversed course from his 2 April “reciprocal” tariff structure, returning to a flat 10% tariff rate for 90 days
11 July	New threat against Canada and Mexico	Trump announces intent to impose a 30% tariff on all Mexican imports and 35% on Canadian imports, effective 1 August 2025

Table 6: Impact of 50% US Tariffs on Merchandise Exports from India

SNo	Product Group	Exports to US (\$ bn, FY2025)	US Share in India's Exports (%)	US MFN Tariff (%)	New Trump Tariff (%)	Total Tariff Payable (%)	Impact on India
1	Shrimps	2	32.4	0	50	50	Very high
2	Petroleum products	4.1	4.3	6.9	0	6.9	Low
3	Organic chemicals	2.7	13.2	4	50	54	Very high
4	Pharmaceuticals	9.8	39.8	0	0	0	Low
5	Carpets	1.2	58.6	2.9	50	52.9	Very high
6	Apparel; knitted	2.7	34.5	13.9	50	63.9	Very high
7	Apparel; woven	2.7	32.2	10.3	50	60.3	Very high
8	Textiles, made up	3	48.4	9	50	59	Very high
9	Diamonds, gold and products	10	40	2.1	50	52.1	Very high
10	Steel, aluminium, copper	4.7	16.6	1.7	50	51.7	High
11	Machinery and mechanical appliances	6.7	20	1.3	50	51.3	Very high
12	Smartphones	10.6	43.9	0	0	0	Low
13	Vehicles, and parts	2.6	11.4	1	25	26	High
14	Furniture; bedding, mattresses	1.1	44.8	2.3	50	52.3	Very high
Total goods exports		86.5	19.8				

Source: GTRI and DGCI&S, GoI (2024).

petroleum products (8.9%), automotive components (2.1%), and textiles and apparel (3.7%). The percentages show each item's share of India's total exports to the US (GoI 2024).

However, if previous restrictive trade measures, including the withdrawal of GSP, are any indication, then the impact has been relatively modest. As evident from Tables 1 and 2, we observe that trade between India and the US continued to grow. As a percentage of India's trade with the world, approximately 19% occurs with the US, amounting to \$75.8 billion in 2022–23, \$77.5 billion in 2023–24, and \$86.5 billion in 2024–25. As part of the reciprocal tariffs programme initiated in April 2025, Trump implemented a 25% tariff on 6 August, with an additional 25% penalty tariff imposed on 27 August for India's purchases of Russian oil, bringing the total tariff to 50%. Sahoo et al (2025) analysed the impact of a 25% tariff on Indian goods and found that the following items are likely to face challenges post-tariff: gems and jewellery, mineral fuels, articles of iron and steel, nuclear reactors, and organic chemicals. Dhar (2025) examined the impact of the Trump-era tariffs on the Indian agriculture sector and found that reciprocal tariffs could weaken export competitiveness, harm rural livelihoods, and disrupt supply chains. As per the report by the Global Trade Research Initiative (GTRI), the impact of the 50% US tariffs will make India's exports costlier and could reduce US-bound exports by 40%–50% (Srivastava 2025). An estimated \$48.2 billion out of \$86.5 billion in total merchandise exports from India to the US will be subjected to 50% tariffs, translating to 1.5% of India's GDP (Table 6, p 40). Major export items, such as pharmaceuticals and smartphones, are exempted from this 50% tariff.

As during the Trump 1.0 era, we expect trade between India and the US will continue to grow, with tariff-related disruptions likely being phased out over time. Das and Rout (2025) argue that India possesses a strategic advantage because its consumption-driven economy is less dependent on exports than many other emerging Asian economies.

Also, most of India's key exports are income-sensitive, and a strong global demand can have a positive impact. In 2023, India became the second-largest exporter of refined petroleum, with exports valued at \$85 billion and a global market share of 12.6% (GoI 2024). Other major exports from India include insecticides and fungicides (10.5%), steel (12.7%), beet sugar (12.21%), rubber tyres (3.31%), and gemstones (36%) (GoI 2024).

In Conclusion

In this article, we examined the impact of the Trump 2.0 reciprocal tariff policy on key US trading partners, namely Canada, China, India, and Mexico. We found that Canada and Mexico are more likely to be impacted, and this result is consistent with the predictions of the gravity model of trade. In contrast, China and India are less likely to be impacted, with India being somewhat less insulated than China. China has actively reduced its trade reliance on the US and effectively circumvented tariffs by relocating production to other countries. India, although insulated by its large, consumption-driven domestic economy, can shift production of exports such as footwear and textiles to countries such as Bangladesh, Ethiopia, Oman, and Vietnam that face lower reciprocal Trump tariffs. Also, there is a need to implement comprehensive economic reforms. These should include further rationalisation of the goods and services tax, reforms to rigid labour laws, correction of the inverted duty structure on critical raw materials, and signing FTAs with key trading partners.

NOTES

- 1 The president's order does not include a full list of covered Harmonised Tariff Schedule of the United States (HTSUS) codes.
- 2 Before the recent tariff increases, many traders found it economically rational to pay the low 2%–3% US MFN tariffs rather than invest in ROO compliance infrastructure that often costs more than 3%, making the duty-free USMCA treatment less attractive than simply paying the tariff.
- 3 The legality of Trump's tariffs is now before the US Supreme Court, which will determine if the IEEPA can be used for peacetime negotiating leverage or is strictly limited to genuine national emergencies such as hostile actions, espionage, or terrorism. Pal and Ray (2025) argue that the

formula used to calculate "Liberation Day tariffs" is based on questionable parameters and lacks theoretical support.

- 4 The US is providing a legal justification for its reciprocal tariffs by claiming they are necessary to protect American national security. Article XXI of GATT allows countries to bypass their WTO obligations for the purpose of national security.
- 5 The term "substantially" is not explicitly defined in terms of the percentage of trade that qualifies as substantial, but it is generally understood to cover a high percentage of trade between member countries. However, bilateral trade agreements do not come under the purview of FTAs or customs unions.
- 6 Countries are using NTMs on the pretext of safeguarding the health of their consumers and to stop predatory pricing strategies, which are permissible under WTO rules. NTMs become non-tariff barriers (NTBs) if they are used to restrict market access rather than for the purposes they were codified under GATT. For example, the antidumping agreement codified during the Tokyo Round of GATT negotiations becomes an NTB if it is used not to prevent predatory pricing but to restrict market access.
- 7 According to the World Bank, a "low-income" country is one with a per capita income of less than \$1,045 per year in 2023.

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