Trade War: How It Will Impact The Global Economy

Gianna Quatromoni

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Dr. Honeker

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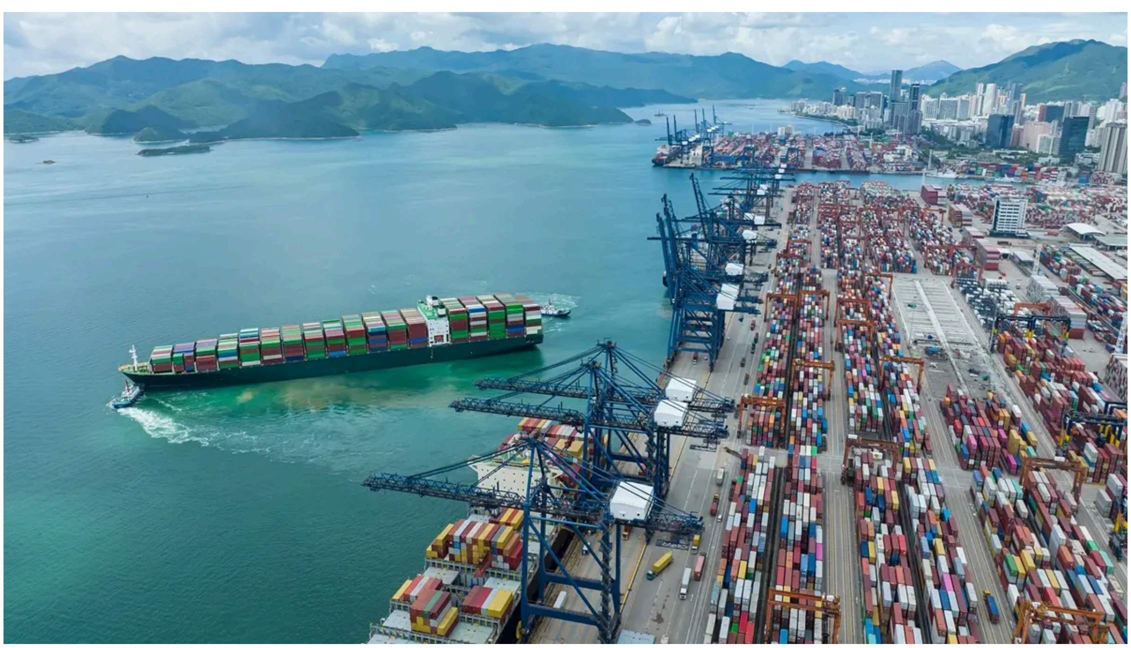


Background Information

The WTO has stated that Donald Trump's tariffs will send international trade into reverse this year, depressing global economic growth (WTO, 2025). Since the 1870s, globalization has rapidly increased. Today, we see a multi-trillion-dollar international trade market with economies integrated more than ever. Unfortunately, this well-structured and efficient market has been hit by President Donald Trump's tariffs and everything from consumers to supply chains are bearing the costs. We are now faced with a rise of vulnerabilities and chaos in the global market due to a hegemon behaving in a protectionist way with politically motivated policies. In early 2025 the Trump administration announced a series of tariffs that would be implemented starting on April 2, also referred to as "Liberation Day". On Liberation Day, a blanket tariff of at least 10% would be implemented on all countries' imports and even higher rates for 60 countries or trading blocs that have a trade deficit with the United States. Trump also threatened another round of tariffs, but this time retaliatory. Raising the once 125% tariff on Chinese imports to 145%, 27% on Indian products, 24% on Japanese products, 26% on products from South Korea, and threats of new tariffs on Mexico and France have led to global economic discord and is poorly reflected back on the United States. Due to the hit to stocks, worry in FDI, rising geopolitical tensions, and rumors of inflation potentially leading to a recession from the implementation of trade blocs; Trump decided to put a 90 day delay on the retaliation tariffs while keeping the 10% blanket in place. Countries have responded in two main ways: by seeking compromise or by imposing retaliatory action. Nations like Japan, South Korea, and Vietnam have attempted to pursue diplomatic negotiations in an effort to reduce the tariff rates. Nations like China, the European Union, and Canada have taken a more aggressive approach. In response to Liberation day, China imposed a 34% tariff on American goods, which has sparked a vicious trade war between the nations. The conflict has a tit-for-tat structure, as Trump then raised the tariff to 125%. The EU is speculated to retaliate as well but has taken a delayed approach. Member states recently voted on retaliatory levies on approximately 23 billion USD in goods. The commission has decided to not immediately put the trade blocs in place, yet stagger its implementation (Grantham-Philips, 2025). Lastly, Canada has retaliated with a 25% levy on auto imports that do not comply with United States-Mexico-Canada Agreement.

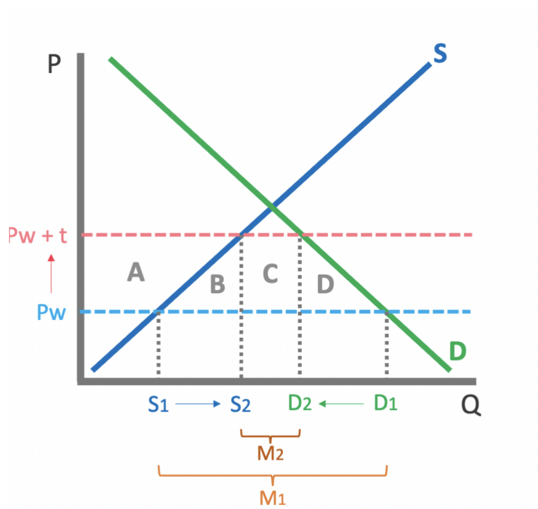
Actors

With our global economy being increasingly interconnected, the Trump Tariffs are essentially affecting most countries' economies and their relationship with the United States. China is being hit the hardest due to their immediate retaliation tariff placed on U.S. imports. Their manufacturing sector is bearing the brunt of the impact, which is an especially damaging outcome given that China remains the world's largest manufacturer. Their exports to the U.S. have decreased in the first two quarters of 2025. The factories with strong ties to U.S. companies have recently announced they've had to cancel contracts and operating hours (Business Insider, 2025). The pharmaceutical sector is also seeing the effects of the tariffs. Trump imposed a +20% levy on fentanyl. The administration justified its actions as an effort to combat the drug addiction crisis in the U.S.; however, the measures effectively targeted pharmaceutical and chemical manufacturers in China (The White House, 2025). Steel, aluminum, and tile sectors are taking a hit as well. The Guardian reported in early April that "steel, aluminum, tiles, and furniture exports to the U.S. are down approximately 40% in Q1 2025 due to import costs and new 'Buy American' mandates" (Stewart, 2025). China can produce goods in these sectors at significantly lower costs than the U.S., making American products relatively uncompetitive. By imposing tariffs on these imports; the U.S. effectively protects its domestic steel, aluminum, tile, and furniture industries. Tariffs in the high-tech and semiconductor industries have startled companies. For example, in response to the 10% tariff, Apple flew five cargo planes from China and India filled with over 600 tons of iPhones and other products back to the United States (India, 2025). For Canada, they have tariffs ultimately across the board, just USMCA compliant goods are exempted. Canada has issued warnings of possible retaliation against the United States. The European Union's automotive industry is being significantly impacted. The United States is a crucial partner for the EU's automotive industry. In 2023, European car manufacturers exported 23 billion euros worth of vehicles and components to the states. After Trump raised tariffs from 2.5%-25%, costs of European cars increased in U.S. markets which is now leading to their decline in competitiveness relative to other countries. *Oxford Economics* has drafted a GTPA analysis that predicts the implications on the European Automotive Industry after the 25% tariff. Because Germany and Italy are the most reliant on the United States, their exports could fall by 7.1% and 6.6% (Li, 2025). Spain and France are expected to see a roughly 2.3% decrease in their exports (Li, 2025). These declines could be detrimental to the EU's economy due to the large portion of their income coming from automotive exportation.

These tariffs are not just affecting countries economically, geopolitical tensions are rising on all fronts. The United States has increasingly found itself navigating diplomatic tensions with formerly friendly nations, and is now facing the consequences of those strained relationships. Canada views these tariffs as a betrayal to a true ally. China views it as a threat to their competition with the United States economy. Overall, it has caused countries to lose trust in the U.S. and see their government as unstable and relatively untrustworthy. In turn, countries are pulling out of the states, the day after Trump's liberation day, S&D 500 index of large American firms fell by approximately 5% (The Economist, 2025). China is debating on barring several large technology companies from investing in the nation. Also, even though nasdaq-100 surged by 12%, investors are still increasingly worried about the volatility of stocks (The Economist, 2025). With countries pulling out of the United States, they are losing money and their money is losing value. On April 3rd, the day after Trump implemented his tariffs, the USD fell from 104.068 to roughly 101.971 on the US Dollar Currency Index (Investopedia, 2025). The dollar has further depreciated since then and as of April 21, the dollar has fallen to the lowest value it has been in three years of 97.92 (Investopedia, 2025).

Policy Alternatives

The main suggestion in response to Trump's tariffs is retaliation. As mentioned previously, China has responded to Trump's tariffs with their own. The EU has threatened retaliation, but is delaying their response to regroup their economy after the initial levying. In an interview in the Oval office, Trump has stated that he would never implement tariffs too high in fear that people will "stop buying" (Sheffey, 2025). This is exactly right, if Tariffs were to go "too high" consumers would eventually stop buying due to increased prices. Refer to the graph below.



Before implementation of tariffs consumers are purchasing products at price *Pw*. After implementation consumers are purchasing products at price *Pw+t*, clearly higher than before.

Their consumer surplus decreases by *A+B+C+D*. If the increase were to continue, there would reach a point where the cost of the product outweighs the value the consumer places on the product and price they are willing to pay, essentially causing the market to collapse. If consumers can't afford products, either inflation will occur and the dollar could depreciate or markets will disappear. Both leading to firms and governments losing in the long run as well as the consumer.

Another response to the tariffs is forming bilateral trade agreements. Countries like India and Japan are among the first to propose these agreements. India has proposed the idea of partnering with the U.S. to avoid Trump's 26% tariff on exports. On April 21st, J.D. Vance traveled to India to discuss the agreements and claims they are very close (The Economist, 2025). On April 7, the Trump Administration announced that the U.S. and Japan had begun talks of trade agreements. The conversations centered mainly around tariffs, non-tariff barriers, currency issues, and government subsidies (Cimino, 2025). If successful, these trade agreements could bring a lot of positives. To start, the consumer will benefit from lower prices and access to a variety of products. Exporters from countries like Mexico, China, and Canada; the United State's main importers, will benefit from less trade barriers and which will allow them to generate more profit from their exports. Investors will also benefit from free trade because trade will increase and there will be higher returns on capital. Unfortunately, some domestic sectors will be impacted negatively, specifically steel. Due to increased competition, the U.S. steel sector could suffer because many other countries can produce the goods at a lower price. Domestic firms could also lose jobs, specifically jobs in the agricultural, steel, and textile sectors. Free trade would also go against one of Trump's main goals throughout his campaign, "Buy American", which aimed to bring back economic development to domestic companies.

Policy Proposal

The Trump administration's 2025 trade policy reflects the United States' role as a hegemon—exercising dominant influence over global economic and political systems. The overall goal of a new policy is to bring global trade back to a stable and conflict lacking environment. A potential way to do this is to combine the two policy alternatives mentioned. There should be a focus on scaling back the severity of the tariffs and shifting away from blanket or retaliatory measures. Instead, tariffs could be applied more strategically to support specific noncompetitive industries in the U.S. that are in need of targeted protection. These areas can be identified by looking at what industries in the U.S. do not have a comparative advantage producing in certain sectors and compare their prices relative to other nations. If U.S. production costs are significantly higher, this may indicate the need for targeted protectionist measures, such as sector-specific tariffs. At the same time, the U.S. can honor and propose new trade agreements in areas that would give the U.S. and partnering countries access to lower prices and a variety of products. For example, countries like Japan would be able to offer the U.S different products than their main trade partners, Canada and Mexico. This proposal would be a prime example of the Hegemonic Stability Theory. By implementing strategic tariffs on noncompetitive industries important to the nation’s economy, like steel and technology, while also negotiating new trade agreements, the U.S. is exerting hegemonic power to rebalance global trade relationships. The effects of this policy would not only improve the U.S. economy but also encourage growth in other nations, reflecting their leadership in maintaining a stable and growing international economy.

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