# THE NEW POLITICAL ECONOMY OF US TRADE

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**Donald Trump has made** trade central to his economic and foreign policies. For decades, he has accused countries of exploiting the United States through unfair trade agreements. During his first term, he fought a trade war with China. During the 2024 campaign, he declared tariffs "the most beautiful word in the dictionary." Since returning to office, he has threatened, imposed, suspended, refunded, and again enacted tariffs on nearly all US trade partners. Tariff rates now vary by country, and sometimes by product, in ways that have little precedent in American trade policy.

The Trump administration's trade policies have far-reaching implications for the United States. They promise to create opportunities for some industries such as steel and aluminum, but threaten to impose substantial costs on others, including agriculture and automobiles. Consumers will face higher prices. The administration hopes that higher tariffs will remake portions of the country's industrial structure, although because manufacturing is heavily automated they will not create many new jobs. They may allow the Trump administration to extract concessions from other governments, but such concessions will limit its ability to protect American industries. The administration's strategy may remake the institutional structure of American trade policy, taking power away from Congress and lodging it in the presidency.

The Trump trade policies have faced a continuing series of legal challenges; most prominently, the Supreme Court ruled that the administration's signature "reciprocal" tariffs were unconstitutional, as the authority the administration claimed under the 1977 International Emergency Economic Powers Act does not permit the president to levy tariffs. Nonetheless, Trump has moved to enact similar tariffs using other legal authorities. These will also face legal challenges, leaving trade policy in a state of uncertainty.

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Nonetheless, it is clear that the administration intends to maintain a wide range of barriers to trade. This will change the nature of the US economy, the structure of the world economy, and the relationship between the two.

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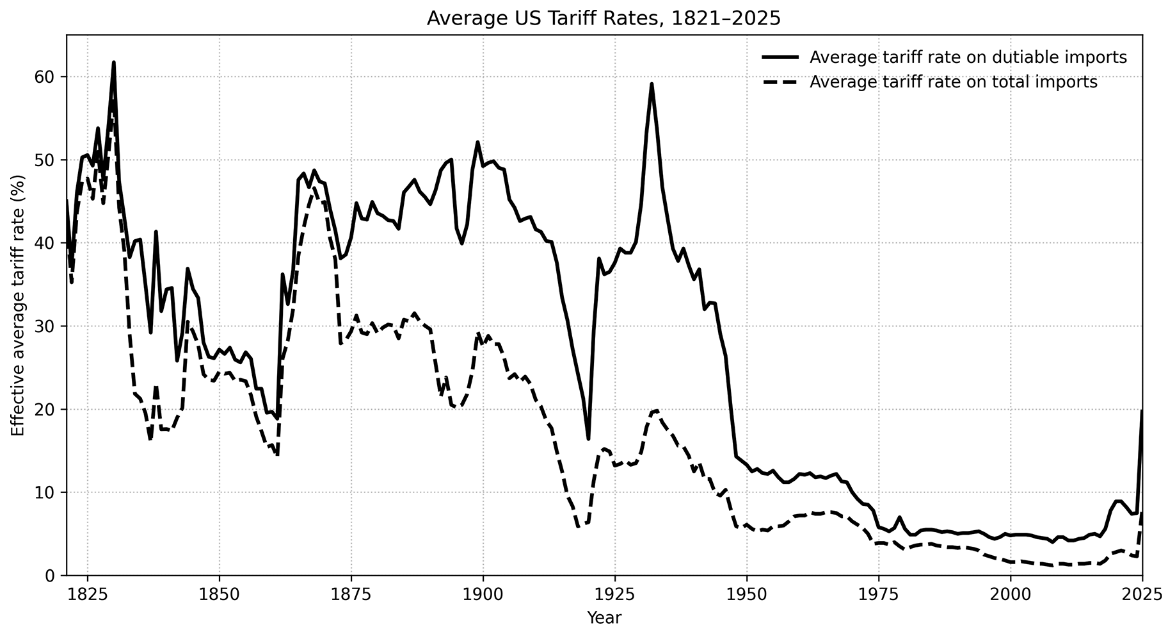
Tariffs have long been a feature of US economic policy, but until 2017 they had been declining for 70 years. The magnitude of the Trump tariffs and the ways in which they have been imposed are a striking departure from past US policy.

From roughly 1787 until 1861, Congress used its constitutionally assigned power to set taxes on imports. During this first era of US trade policy, tariffs varied over time, and were used primarily to fund the government, constituting between 80 and 90 percent of all federal revenue. As the North industrialized, it began to demand higher protection, resulting in the so-called Tariff of Abominations in 1828, which shielded northern industries from foreign (mainly British) competition. Opposed by the free-trade South, which was forced to pay more for goods, the act spurred the "Nullification Crisis" in 1832–33, which threatened to split the Union. The North backed down and tariff rates fell dramatically.

In the second era, beginning with the Civil War, the protectionist preferences of Northeastern and Midwestern industry dominated. Between 1861 and 1934 tariffs were largely set by logrolls in Congress, in which representatives traded votes to protect "their" industries in exchange for support for the industries of other representatives. Logrolls ratcheted tariff rates up, with the exception of raw materials and other inputs needed for manufacturing.

This system broke down during the Great Depression when Congress passed the infamous Smoot-Hawley Tariff Act of 1930, which produced some of the highest tariff rates in US history and set off a classic trade war. World trade spiraled downward by two-thirds as markets closed, exacerbating the effects of the Great Depression.

At the start of the third trade era, Congress passed the Reciprocal Trade Agreements Act (RTAA) in 1934, delegating much trade policymaking to the president. The need to negotiate reciprocal reductions in tariffs with other




Average US tariff rates (1821–2025). **1821–1890:** US Bureau of the Census, *Historical Statistics of the United States, 1789–1945*, series **M 68–74,** "Value of Merchandise Imports and Duties on Them," pp. 247–48. The two plotted columns are series M72, duties divided by total imports, and M73, duties divided by dutiable imports. Fiscal years. **1891–2025:** US International Trade Commission, *US Imports for Consumption, Duties Collected, and Ratio of Duties to Value, 1891–2025,* Table 1, March 2026. The USITC states that the table was compiled from official U.S. Department of Commerce statistics. Calendar years.

countries, and the desire to have trade policy reflect national rather than parochial interests, led Congress to give the executive considerable discretion. With trade policy now accountable to a national constituency, the president was generally expected to favor trade liberalization.

With the RTAA in place, President Franklin Delano Roosevelt swiftly signed agreements with 20 countries, covering 60 percent of US imports. Reciprocity transformed the politics of trade policy. While traditional labor-intensive industries like textiles and shoes opposed the RTAA, fearing greater foreign competition, capital-intensive industries like automobiles, machinery, and electrical equipment, as well as agriculture, benefited from increased exports.

After World War II ended, with European industry devastated and US manufacturing unrivaled, the United States led in creating the General Agreement on Tariffs and Trade (GATT) in 1947. Fueled by a belief that economic integration would strengthen US allies in the global struggle against the Soviet Union, the GATT dramatically lowered tariffs for nearly all industrialized countries. The most-favored-nation (MFN) principle meant that tariff concessions between two negotiating countries were automatically extended to all other GATT members. In 1947, before the first round of GATT negotiations, average tariff rates for 23 member countries were approximately 22 percent. By 1994, at the end of the Uruguay Round, average tariffs for 123 members were roughly 4 percent.

While the United States led the world toward freer trade, protectionist pressures grew at home. As East Asian countries industrialized, labor-intensive industries faced intense competition from foreign producers, spurring the United States to negotiate trade-restricting measures and impose "voluntary" export restraints on steel, automobiles, and electronics, especially from Japan. While generally liberalizing trade, the United States insisted on carve-outs to protect its own industries from what was regarded as excessive competition. These temporary barriers slowed but did not stop the process of liberalization.

In 1995 the GATT was reconvened as the World Trade Organization (WTO), whose primary innovation was a more elaborate and binding dispute settlement system. The WTO's dramatically increased membership, which now included numerous developing and former Soviet bloc countries, and eventually China, were required to accept all of the core agreements previously reached under the GATT, eliminating many special exemptions and standardizing the rules. The WTO also expanded its remit beyond tariffs on goods to include non-tariff barriers, services, investment, and intellectual property.

Overall, the WTO continued the drive for liberalization within a more formally defined set of legal rules and obligations. While the WTO has faced many challenges since its inception, its rules defined the basic structure of international trade—until Donald Trump retook the presidency in 2025.

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Since returning to office, Trump has reversed 90 years of trade liberalization, exploiting executive discretion to fundamentally change the direction of US trade policy. Trump justifies many of the administration's trade barriers, including those on steel and aluminum, on national security grounds. President Biden also used national security as a rationale for trade and industrial policy initiatives, but unlike Trump, Biden worked with Congress to enact the Inflation Reduction Act and the CHIPS Act ("Creating Helpful Incentives to Produce Semiconductors and Science") to subsidize the development of critical industries and create supply chain resilience.

Trump's global tariffs were first instituted under the International Emergency Economic Powers Act (IEEPA), which allows a president to regulate transactions with foreign entities once a national emergency is declared. In his first term, Trump used this authority to initiate a trade war with China. In his second, he went much further, claiming that a large and persistent trade deficit, illegal immigration, and fentanyl trafficking constitute emergencies. The Supreme Court ruled in February 2026 that the IEEPA did not authorize the president to impose tariffs, but Trump is employing other authorities to approximate the impact of the original round of tariffs.

What are Trump's goals? The proximate aim is to balance the flow of goods between the United States and its trading partners and make trade more "fair." More fundamentally, as part of his aim to appeal to regions where manufacturing jobs have been lost and to younger and less skilled workers, Trump says he wants to rebuild American manufacturing, especially in industries that "make things." The focus on physical goods ignores trade in services in which the United States typically runs a surplus. He also seeks to use tariffs, or the threat of tariffs, to extract concessions on trade and a variety of other issues and to generate revenue for the government, perhaps to help offset Republican tax cuts.

During Trump's first term, it was unclear whether he was using the trade war with China to try to open the Chinese market to US goods, services, and investment (pleasing investors and export-oriented businesses) or to protect US industry (pleasing import-competing sectors and their workers). Trump imposed tariffs on Chinese goods, China retaliated with tariffs on US goods, and duties spiraled up and trade spiraled down until the two sides called a ceasefire to preserve rates at their then elevated levels. All the while, American firms requested approximately 40,000 exemptions, which gave the administration a subtle but effective way to distribute benefits to firms that supported Trump's agenda.

Trump's trade policy today has three distinctive features. First, the Trump administration is bargaining *bilaterally* over trade, overturning the MFN principle under which US tariff rates were extended to all WTO members equally. Having abandoned MFN, the United States has also abandoned the multilateral trade regime, even as the rest of the world's governments continue largely to abide by it and negotiate trade agreements among themselves. The lower tariffs in these agreements will not automatically be extended to US producers, meaning that American firms may face higher duties in third-country markets than exporters from countries that still respect MFN.

The Trump administration has also attempted to negotiate a single tariff *per country*, not tariffs on particular products—a first in US history. While the Supreme Court invalidated the most direct attempts along these lines, the administration has made clear that it will attempt to replicate these country-specific tariffs as it bargains with other governments. For example, agreements with Japan and the European Union establish baseline tariff rates of 15 percent on their goods. This change from historic practice is likely driven by a desire to balance bilateral trade and to strengthen US bargaining leverage. But it risks disrupting global supply chains and hurting US manufacturers who source raw materials and intermediate inputs abroad.

The United States is also using bilateral bargaining to link tariffs to non-economic issues. Trade has been used in the past to achieve broader political goals, such as with the imposition of trade sanctions on hostile nations or tying trade agreements to policies that protect labor or human rights. Now, however, the Trump administration is using tariffs to coerce allies and adversaries, for goals that have little to do with the national interest as broadly understood. The president imposed tariffs on Brazil to halt the prosecution of former Brazilian President Jair Bolsonaro for having fomented a coup. He punished the Indian government with additional tariffs for failing to credit him for calming tensions with Pakistan. And he penalized the Canadian government because the province of Ontario ran an advertisement on American television pointing out that Ronald Reagan was a strong opponent of tariffs.

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Tariff levels will probably eventually settle somewhere in the range of 15 percent, possibly lower for most of the world, and higher for China. It has been a long time since the United States—or any developed country—had tariffs this high, which makes it hard to predict what their impact will be. Some broad indications, though, are already clear.

The most obvious impact of tariffs is that prices for American consumers will rise. Tariffs are, of course, taxes on trade paid at the border. How these taxes are absorbed can vary from industry to industry, firm to firm, and even product to product. Exporters, importers, wholesalers, or retailers may swallow some of the tax in order to avoid losing customers—or they may raise prices. Domestic producers may respond by raising their prices now that foreign goods are more expensive in the domestic market; this is, after all, how "protection" of domestic producers works!

All this depends on complex considerations and decisions made by the industries and firms involved. It will require in-depth studies to provide an accurate and detailed picture of how the Trump tariffs affect producers, intermediaries, and consumers.

Nonetheless, a picture is already emerging. Studies of the tariffs enacted during the first Trump administration, and early studies of the current tariffs, show that the duties have been passed through to domestic prices almost completely. This means that the brunt of the burden of the tariffs will be borne by American consumers—both intermediate consumers of inputs and consumers of end products. In 2018, for instance, tariffs on washing machines were passed through almost completely to consumers, with prices rising about 12 percent, or $86–92 per unit. The tariff on washers generated about $82 million in revenue for the government but cost consumers nearly $1.5 billion in higher prices. Domestic production of washers did increase, but mostly by foreign firms "tariff hopping" and setting up new plants in the United States, creating approximately 1,800 new jobs. Current estimates are that 85–95 percent of the 2025 tariffs are being passed through to consumers.

Evaluations of the overall impact of the tariffs on US economic growth are even more complex and difficult, but early analyses suggest a substantial negative impact in the medium to long run. Current tariffs are estimated to have increased inflation by about 0.7 percentage point when the consumer price index for 2025 was already running at 2.7 percent, raising overall prices by about 25 percent from the baseline.

Whether tariffs will foster a reindustrialization of the United States is an open question. Even if firms and industries bring back ("on-shore" or "re-shore") production that was previously moved off-shore, it is likely to be capital-intensive and highly automated, creating few jobs for low-skilled workers. Some American workers may benefit from trade protection, but even if there is a substantial increase in manufacturing output, it is unlikely to create many good blue-collar jobs or to significantly increase wages for less-skilled workers. US industries will always try to replace scarce (and expensive) labor with relatively abundant (and cheaper) capital and technology, for example by installing robots. Early evidence suggests that the US continues to lose manufacturing jobs despite the tariffs.

One of the central contradictions of Trump's trade policies is the purported goal of driving investment in American industry while using tariffs as bargaining chips with other governments. These two purposes are inconsistent. A tariff is useful as a bargaining chip only if it can be removed, and a tariff removed can no longer serve to stimulate investment. This contradiction has been widely noted in the business press. Investors are confused as to whether the tariffs should be seen as temporary—kept on until target countries concede—or permanent. This likely reduces incentives for investment in the United States and, once again, undercuts the administration's ambition to rebuild US manufacturing.

The attempt to remake the country's trade relations is also likely to affect capital flows. This is a particularly contradictory feature of the Trump administration's policies. Foreigners invest a great deal of money in the United States, and lend a lot of money to the US government—and the Trump administration wants to encourage this. But the more foreign money that flows into the United States, the bigger the trade deficit will be. This is because the inflow of funds drives up the value of the dollar, making foreign goods cheaper relative to domestic goods. Looked at another way, the United States borrows because it consumes more than it produces, and the borrowed funds are used to pay for this extra consumption, which has to be satisfied by imports. For tariffs to reduce the trade deficit, they must perforce reduce net capital inflows. And yet the administration has prominently featured commitments from other countries to invest in the United States, even while they reduce their surpluses with the United States. How this is mathematically, or economically, feasible is a mystery.

Finally, the Trump administration's actions on trade raise important domestic institutional considerations. The Constitution gives Congress the power "To lay and collect Taxes, Duties, Imposts and Excises," and "To regulate Commerce with foreign Nations." Although Congress delegated limited trade policy powers to the president and to agencies like the International Trade Commission, it could easily reclaim control. The current Republican Congress has chosen not to exercise its legislative powers, but future legislatures may decide to revise the procedures for making trade policy in ways that more strictly limit executive action. Indeed, Justice Neil Gorsuch's opinion in the IEEPA case calls on Congress to reclaim and reassert its powers in precisely this way.

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Trump's trade policies come at a time of crisis for the international trading system. The WTO has been hamstrung for decades. The Doha Round of trade neogitations began in 2001 and has been an almost complete failure. The WTO's dispute settlement mechanism has been immobilized by American objections since the Obama administration. This breakdown has led many WTO members to seek "minilateral" alternatives to the WTO's stalled multilateralism. The Trump administration, indeed, has justified its policies in part by arguing that the WTO does not serve its intended purpose.

If the Trump administration is abandoning multilateralism and norms of non-discrimination, the rest of the world continues to embrace them. Most countries are moving forward with some version of the existing system. The vast majority of world trade is still carried out on MFN principles. The European Union (EU) and several other countries have established an interim arbitration arrangement to serve as long as the WTO body remains inoperative. When the United States pulled out of the Trans-Pacific Partnership (TPP) in 2017, the remaining 11 members created the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP), which the United Kingdom has since also joined (other countries have also expressed interest in joining). Despite the fact that the original TPP was an American initiative, the CPTPP now excludes the United States because the first Trump administration withdrew from it.

While the Trump administration appears to want to remake the international trading system, it may not be able to remake it in its own image. The actions of other major trading powers, especially China and the European Union, will have a powerful impact on the future of international trade. The EU has concluded agreements with South American countries, Australia, India, and Indonesia. African governments are considering a continental free trade agreement. Canada and China have reached an interim deal and countries are queued up to join a regional trade agreement in Asia that already includes most Southeast Asian nations. At times it seems that the Trump administration, or at least elements of the administration, is happy to see much of the rest of the world go its own way.

In their trade with the US, many countries have accepted higher tariffs to avoid catastrophic ones. Prior to the 2025 agreement between the United States and the EU, for instance, the average tariff on goods from the European Union was less than 1 percent. In the face of a threatened rate of 50 percent, the EU settled for a baseline tariff rate of 15 percent. In other cases, Trump has extracted various concessions, including promises of increased investment in the United States. Most of the agreements announced so far are sketchy. Given ongoing uncertainty about the legal status of the administration's measures, governments may attempt to chip away at the American demands as negotiations continue.

China is the only country that has countered Trump's trade war directly and successfully. When Trump threatened tariffs of up to 145 percent, the Chinese government embargoed imports of American soybeans—denying American farmers an important market—and put restrictions on Chinese exports of rare earths, which are essential to many industries, including electronics and consumer tech, clean energy and electric vehicles, defense and aerospace, and medical devices. Eventually, Presidents Trump and Xi signed a "framework agreement," reducing the average tariff from 57 to 47 percent and boosting China's purchases of US soybeans. China also agreed to remove export controls on rare earths.

Most observers regard China as the victor, at least for now. President Xi has made it clear that he will meet fire with fire, using the dependence of the United States on Chinese supply chains to impose high costs on the United States should it escalate the conflict. Meanwhile, China's exports continue to rise, as it has diverted its trade from the United States to other parts of the world. It is a paradox that the United States' principal economic competitor seems to have been more successful at escaping the effects of Trump's trade policies than America's erstwhile allies.

Trump's policies and their consequences will not be temporary. The United States will not "snap back" to prior form and once again lead the world toward greater liberalization. President Biden maintained the first Trump administration's tariffs on China and embraced targeted industrial policies. Any new president in 2028 will likely continue at least some elements of the new trade policies. It may be too early to declare what a fourth era of US trade policy will look like, but it is quite clear that the United States has broken with the third era in ways that will be hard to undo.