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Trump's Tariffs, Global Trade and Europe's Strategic Choice

The return of trade policy as an instrument of geopolitics has raised concerns about the future of the global trading system. But Trump's tariffs of 2025 have not led to a collapse of global trade. The key reason for this resilience is that Trump's tariffs are discriminatory, i.e. the US has a different tariff rate for each trading partner. Discriminatory tariffs have re-routed trade, imposing efficiency losses while leaving aggregate volumes largely intact. The economic costs of such tariffs fall predominantly on the country imposing them. Europe occupies a relatively favourable position under current US tariff structures, particularly vis-à-vis China. The historical experience suggests that second-round protectionism against diverted trade would be costly and much more damaging for the global trading system. This suggests for the EU that restraint and openness remain the most effective policies.

For much of the post-Second World War era, trade policy in advanced economies was deliberately insulated from geopolitics. The multilateral trading system created under the General Agreement on Tariffs and Trade (GATT) and later institutionalised in the World Trade Organization (WTO) rested on the principle of non-discrimination, embodied in the most-favoured-nation clause. Broad-based liberalisation under these rules contributed to a steady expansion of world trade and rising living standards. Trade was treated primarily as an economic policy tool, not as an instrument of power politics.

This separation has eroded sharply. Trade restrictions are increasingly motivated by strategic rivalry, national security concerns and domestic political considerations. The most visible turning point was the wave of tariffs imposed by the United States under the first presidency of Donald Trump beginning in 2018, initially targeted only at China and met with retaliatory measures.

The extensive use of sanctions after Russia's full-scale invasion of Ukraine constituted another example of security-driven trade policies. But the fundamental turning point came in April 2025 with the announcement of reciprocal tariffs at the beginning of the second Trump presidency. Not all tariffs that were announced initially were then implemented. But the increase in tariffs that were actually implemented was nevertheless close to those under the infamous Smoot-Hawley Tariff Act of 1930. Under the second Trump Administration, tariffs have become the Swiss army knife of economic policy. Sometimes the justification is to promote US manufacturing, sometimes it is for the revenue and more recently as a tool to cajole allies and other countries for geopolitical or personal reasons. Whatever these changing motives, tariffs have become an important part of the global economy.

Yet the effects of Trump's tariffs are often misunderstood. Public debate frequently assumes that tariffs necessarily reduce trade and that retaliation is an effective response.

This article challenges both assumptions and develops four arguments relevant for European policy. First, Trump's tariffs have not led to a decline in global trade volumes; data up to 2025 (UNCTAD, 2025) show continued growth, albeit at a slower and more volatile pace. Second, the limited visible macroeconomic impact of these tariffs suggests that the aggregate benefits of globalisation may have been overstated in political discourse, even though trade restrictions still impose real welfare losses. Third, the bulk of the economic cost of discriminatory tariffs falls

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Open Access funding provided by ZBW – Leibniz Information Centre for Economics.

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on the country imposing them, implying that retaliation increases domestic costs rather than shifting them abroad. Fourth, Europe may benefit in relative terms from the current structure of US tariffs – provided it avoids repeating the mistakes of the 1930s by erecting its own barriers against diverted Chinese exports.

Global trade after Trump's tariffs: Evidence up to 2025

A natural presumption is that high tariffs imposed by large economies should reduce global trade. Recent experience does not confirm this view. According to UNCTAD's Global Trade Update (December 2025), global trade flows are poised to reach record levels in 2025. Both goods and services trade expanded strongly, particularly in the second half of the year, despite persistent geopolitical tensions. World merchandise trade volumes continued to rise, and trade as a share of global GDP remained close to historical highs.

This resilience has been evident since the first round of Trump tariffs in 2018. Rather than a reversal of globalisation, the global economy has experienced over the last few years what might be termed "slowbalisation": trade continues to grow, but at a slower pace and with important regional reconfiguration. Supply chain disruptions and high shipping costs observed earlier in the decade (e.g. 2022) were not symptoms of collapsing trade, but rather of demand exceeding available logistics capacity.

A first explanation of this apparent irrelevance of tariffs for trade is that, at least so far, no other country has followed the US example and used tariffs extensively. The US is a large economy, but not very open. It accounts for only about one-sixth of global trade. Five-sixths have thus not been affected.

The persistence of high trade volumes has led some observers to argue that tariffs had no economic cost. This conclusion is misleading. The absence of a fall in aggregate trade volumes does not imply the absence of welfare losses. Recent trade restrictions are overwhelmingly discriminatory and targeted at specific countries rather than applied uniformly, which implies that there might be a lot of trade that is diverted, usually in an inefficient way.

Discriminatory tariffs, trade diversion and hidden costs

Discriminatory trade restrictions tend to divert trade rather than suppress it. When the United States imposed high tariffs on imports from China, firms responded by reorganising supply chains. Production stages were relocated to third countries such as Vietnam or Mexico, from which final goods could be exported to the US at lower tariff rates.

At the same time, these third countries increased their imports of intermediate goods from China. US imports from China declined, while imports from Southeast Asia and Mexico surged. China's exports of intermediate inputs to these countries increased substantially. As a result, global trade volumes remained robust, even as supply chains lengthened and production became less efficient.

Similar patterns can be observed in specific sectors. In electric vehicles, high US tariffs and subsidy rules under the Inflation Reduction Act have effectively excluded Chinese producers from the US market, while European producers retain relatively favourable access. Chinese exports have therefore been redirected towards Europe, while European firms have strengthened their position in the US market. In Europe's own sanctions regime against Russia, trade has similarly been re-routed through third countries, notably Turkey and parts of Central Asia.

These developments underline a crucial point: discriminatory trade barriers can increase measured trade volumes while reducing welfare. Longer supply chains, additional transport, and complex compliance structures raise costs. The apparent resilience of global trade thus masks significant efficiency losses.

By contrast, tariffs that apply uniformly on imports from all partners do not lead to this trade diversion. Uniform tariffs would thus have a much stronger impact on trade volumes. That trade diversion is costly has been recognised since the seminal contribution of Viner (1950). A discriminatory tariff can be viewed as an equivalent to a uniform tariff on all imports combined with an implicit subsidy for imports that are not tariffed (Gros, 2025a; Gardner & Kimbrough, 1990).

Who bears the cost of discriminatory trade policy?

Economic theory suggests that tariffs act as a subsidy for domestic producers as well as tax on domestic consumers and firms using imported inputs. A tariff thus distorts the choices of domestic consumers and producers, causing welfare losses. But economic theory also suggests that a large country can gain from a tariff if it forces foreign exporters to lower their price because the domestic market is so important for them. A large country could thus exploit its monopsony power to gain better terms of trade. The US is a large country. It still has the largest economy, but even so, its GDP accounts for about 25% of the global total. This implies that for exporters based abroad, the US is one market among many. Maybe the most important one, but not large enough to force them to lower prices.

A discriminatory tariff makes it even less likely that a tariff will improve the terms of trade because producers from other countries that face no or lower tariffs can still sell their products (making room for the products of the country hit by the discriminatory tariff elsewhere), and because foreign exporters can re-route production (Gros, 2025a; Gardner & Kimbrough, 1990). This implies that the country imposing discriminatory tariffs bears most of the cost, while third countries often benefit from trade diversion.

This logic is central to understanding the limited international opposition to Trump's tariffs. Countries such as Vietnam and Mexico have benefited from becoming intermediaries in reconfigured supply chains. They therefore have little incentive to oppose US trade policy. The same logic applies to sanctions: the EU bears the economic cost of its restrictions on Russia, while non-sanctioning countries capture diverted trade.

This logic also applies to retaliation, which means imposing discriminatory tariffs as a response. Most of the cost of retaliation falls on the country engaging in "tit for tat". This might be emotionally and politically satisfying but comes at a high economic cost.

Retaliatory measures can generate significant costs for the retaliating economy, with only marginal deterrence effects on the target country. The welfare losses associated with retaliation tend to exceed any strategic gains, particularly for open economies such as the EU.

From a systemic perspective, retaliation increases the risk of fragmentation. Once multiple actors engage in discriminatory trade policy, incentives arise to protect against diverted imports, setting the stage for a protectionist spiral.

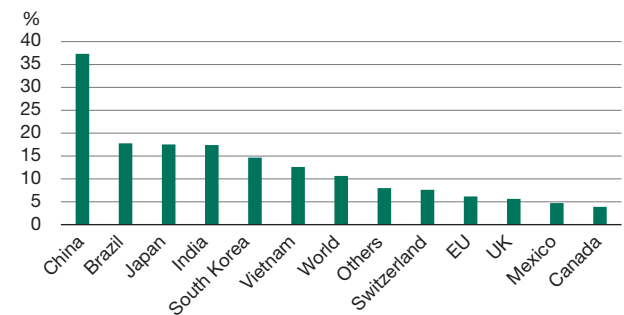
Europe's relative position under current US tariffs

The EU faced the choice of whether to retaliate or not in early 2025. In July, the EU then agreed to a "deal" with the US under which the US would impose tariffs of 15% on EU goods while the EU would reduce its own tariffs on the US (EU Commission, 2025). This asymmetry was widely interpreted as a capitulation, leaving the EU worse off (EPC, 2025). Contrary to a widespread narrative of European capitulation, however, the data show that the EU got a relatively good deal.

First, the data confirm the relatively advantageous position of the EU in terms of access to the US market. The official "deal" held that the US would impose a tariff of 15% on all EU goods, keeping the higher rate of 25% for cars. In reality, the US exempts a large part of EU exports from tariffs. The best way to measure what tariff is actually im-

Figure 1
Implicit average US tariff rates

Duties as a percentage of imports, September 2025



Source: Gros, 2025b.

posed is to simply divide tariff revenue by imports. This measure is also called the effective overall tariff rate; for US imports from the EU it has actually fallen since the so-called Turnberry agreement, now resting at around 6%, compared to 36% for China (see Figure 1). EU goods now face one of the lowest trade barriers on the US market. Only Mexico and Canada fare better, as most of their exports to the US remain duty-free. Other US allies, and industrial competitors, such as Japan or Korea, face much higher rates (about 15%).

Second, the market share of the EU in US imports has rebounded since July, and is now close to its average over the last few years. This rebound is significant as overall US imports are stabilising following the pre-tariff rush in March.

All in all, the reality is that the one-sided deal of July 2025 has not translated into economic losses. The EU, despite its perceived (and real) weakness and division, appears to have successfully navigated a difficult negotiation and secured the best outcome available, protecting its vital market access. It may not feel like a geopolitical victory, but the trade data suggests it was a very good deal.

The reason US trade policy vis-à-vis the EU has been rather cautious might be that the US depends on EU goods. A study by the German Economic Institute (Sultan & Matthes, 2025) has shown that there are thousands of product categories in which the EU provides more than one half of all US imports, more than categories in which Chinese products dominate. This includes many industrial goods, like machines, that are essential to keep the US economy running.

This advantage of EU producers in the US market relative to the competition from China implies that Europe may gain market share in the US at the expense of Chinese

producers. Moreover, as Chinese exports are redirected away from the US, prices in other markets may fall, benefiting European consumers. But this “flood of Chinese” imports also creates political tensions. The increase in imports from China concentrated in a few products is very visible, whereas export opportunities for EU producers are more diffuse. Moreover, the large bilateral surplus of China with the EU reinforces the political pressure to protect against this unfair competition.

Lessons from the 1930s: A warning against second-round protectionism

The interwar period offers a powerful warning. Following the Smoot–Hawley Tariff Act of 1930, the United States raised tariffs sharply. Trading partners initially retaliated against US exports. While damaging, this first round did not cause the collapse of world trade. The collapse occurred when other major economies, notably the United Kingdom, erected barriers against third countries to shield domestic markets from diverted exports. This second round of protectionism led to a dramatic contraction of global trade (Kindleberger, 1973; Eichengreen, 1989).

The lesson is clear: unilateral protectionism is harmful, but imitative protectionism is far worse. If the EU responds to US tariffs by raising barriers against Chinese imports, it risks triggering a similar spiral. By contrast, if the EU maintains openness while others impose discriminatory measures, most of the economic cost will fall on the initiators.

Conclusion: The Case for European Restraint

Trump’s tariffs have not reversed globalisation, but they have reshaped it. Trade has been diverted rather than reduced, imposing hidden costs while leaving aggregate volumes largely intact because these tariffs have been discriminatory with widely different rates across trading partners. Economic theory implies that the economic burden of discriminatory tariffs falls primarily on the countries that impose them. This implies also that retaliation multiplies inefficiencies.

For Europe, the strategic implication is clear. Retaliation against US tariffs or broad protection against Chinese imports would raise costs and risk systemic escalation. Europe’s relative position under the current US trade policy is stronger than often assumed, and its long-term interest lies in preserving an open, non-discriminatory trading system.

The experience of the 1930s demonstrates the dangers of second-round protectionism. In a world where geopolitics

increasingly shapes trade policy, European restraint and openness remain the most economically rational responses – both for Europe and the global trading system.

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