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Tariffs Would Hurt American Consumers, Manufacturers and Economy

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Executive Summary

Tariffs are anti-growth policies that will harm American families. As of February 14th, President Trump has announced a 25 percent tariff on Colombia (rescinded), 25 percent tariffs on Canada and Mexico (delayed), 10 percent tariffs on China (implemented), a 25 percent tariff on steel and aluminum imports (announced), and a reciprocal tariff on all of our trading partners (announced). Given this flurry of activity, the President's campaign to disrupt international trade is well under way.

There are many unknowns regarding which announced tariffs will be implemented, and what new tariffs will be announced in the weeks and months ahead. One thing is known for certain, however. Whatever the justification, the proposed tariffs will have large adverse impacts on American families.

Under increased tariffs, U.S. economic activity will suffer. The consequences include: (1) higher costs for consumers; (2) a more expensive and less productive U.S. manufacturing sector; (3) failure to raise the desired revenues; (4) less investment into the U.S. economy; and (5) higher interest costs.

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Introduction

President Trump is clearly fulfilling his campaign promise to impose large tariffs on the goods and services Americans import. As of February 14th, President Trump has announced a 25 percent tariff on Colombia (rescinded), 25 percent tariffs on Canada and Mexico (delayed), 10 percent tariffs on China (implemented), a 25 percent tariff on steel and aluminum imports (announced), and a reciprocal tariff on all of our trading partners (announced). Few (if any) economists claim tariffs are sound economic policy. Apologists will claim that the adverse impacts from the tariffs will be muted and offset by the combination of comprehensive deregulation and sound fiscal policy.

Undoubtedly, broad-based deregulation and a return to a pro-growth fiscal policy that emphasizes spending restraint will generate large economic growth benefits. But those positives do not excuse the large negative consequences that will result from broad-based tariffs. On net, the imposition of broad-based tariffs will work against the Administration's efforts to incentivize an economic growth resurgence.

The purpose of this Issue Brief is to review the economics of imposing tariffs to demonstrate that, when the full impacts from tariffs are considered, they will neither raise production levels in the U.S. nor lead to an appreciable increase in federal revenues.

(Note: this analysis is current as of February 14, 2025. Any expansions or repeal of the proposed tariffs after that date will not be reflected in the text, however the fundamental economics driving the situation are still relevant. Additionally, the threat of tariffs will continue to hang over the global economy for the foreseeable future making an understanding of the underlying economics essential.)

Tariffs Will Fail to Achieve Administration's Stated Goals

The Trump Administration believes imposing tariffs can achieve three goals: (1) increase domestic production by reworking the supply chain; (2) raise revenues for the federal government; and (3) provide leverage in negotiations with other countries.

The third goal differs from the first two since it is not an economic argument per se. Advocates of the third goal claim that tariffs are a tool to extract other policies from our trading partners. These goals can vary from other countries lowering tariffs on U.S. products to their helping crack down on the illegal fentanyl trade. And the Trump Administration can claim that the January 2025 threat of an across-the-board 25 percent tariff on all exports to the U.S. convinced Colombia president Gustavo Petro to ultimately accept deportation flights from the U.S. Simply because the policy forced a sovereign country to change its behavior does not make the policy advisable.

Tariffs are nothing more than taxes on U.S. consumers and businesses. Canadian Prime Minister Justin Trudeau outlined the negative impacts that would be felt by Americans in a speech after the Trump administration announced its Canada-Mexico-China tariff plans:

> Tariffs against Canada will put your jobs at risk, potentially shutting down American auto assembly plants and other manufacturing facilities.
>
> They will raise costs for you, including food at the grocery stores and gas at the pump.
>
> They will impede your access to an affordable supply of vital goods crucial for U.S. security, such as nickel, potash, uranium, steel and aluminum.[1]

Consumers bear the costs of higher tariffs when they are forced to pay higher prices for the products their families regularly consume. Manufacturers bear the costs when they earn lower profits from their sales and pay more for the imported parts and raw materials that they rely on in their production processes. Companies will also suffer from fewer sales and less revenue when our trading partners inevitably impose retaliatory tariffs on the U.S. and the company's exported goods become less competitively priced.

Since tariffs are nothing more than taxes on U.S. consumption and U.S. production, when used as a negotiation tool, the threatened tariff is a promise that the Administration will harm U.S. consumers and businesses if other countries do not bend to the President's demands. This is hardly an effective negotiation position.

Eventually, some negotiation partner will realize that tariffs are taxes on U.S. consumers and, recognizing this reality, will call President Trump on these threats. Unless the President is willing to be caught bluffing, he will have no choice but to impose significant harm on consumers and broader economic prosperity. Either way, U.S. residents are worse off.

The insanity of the situation could worsen further, unfortunately. Many of our trading partners may also fail to recognize that tariffs are fundamental taxes on their own citizens. They may therefore respond to the U.S. threat with a tariff threat of their own. Should these threats turn into action, then citizens of both countries will be

harmed. Importantly, the adverse economic consequences on the U.S. outlined below will be worsened significantly should the threat of tariffs ignite a trade war.

Indeed, this was the response from Canada after the Trump administration announcement. Before the 30-day pause was announced on February 3, the Trudeau government announced that it was responding by implementing 25 percent tariffs against $155 billion worth of U.S. goods in two phases, on products ranging from orange juice and spirits to household appliances and raw building materials.[2]

Tariffs Are Direct Taxes on U.S. Consumption and U.S. Production

Since higher tariffs haven't really been a core U.S. economic strategy in over 90 years, there's a lot of confusion over how they would be imposed, who would pay, and what their impact would be on U.S. consumers, revenue, and jobs.

An October 2024 analysis of President Trump's proposed tariffs while he was campaigning for president by the nonpartisan Tax Foundation, provides as useful a benchmark as any for understanding what the ultimate average tariff rate on imports will be. The average tariff rate on all imports would be significantly higher in 2025 under Trump's proposed tariff plan from the campaign—increasing from 2.8 percent to 17.7 percent. As the Tax Foundation noted, "the United States has not seen an average tariff rate that high since 1934, amidst the Great Depression and the Smoot-Hawley tariffs."[3] In other words, President Trump's intentions appear to be consistent with imposing tariffs at rates so high that they will impose significant harm on the U.S. economy.

Instead of benefiting the U.S. economy, the implementation of tariffs will diminish domestic manufacturing production, reduce income growth, and jeopardize broad-based prosperity.

The proponents of tariffs typically refer to a static market process to justify the policy's economic benefits. For instance, if a 25 percent tariff rate, such as the currently delayed tariffs on Canada and Mexico, were ever implemented, importers would send the government a $5,000 check when importing products with a $20,000 wholesale price. On a static basis, this imported product will now cost $25,000.

The hope of the tariff advocates is that sales of the now more expensive foreign products will decline while the sales of the now relatively cheaper domestic products will increase. With increased sales, domestic production will then increase, raising economic growth and incomes in the United States.

But the static theory does not accurately reflect how markets work in practice. Taking a more dynamic look and we'll see that the alleged benefits of tariffs are illusory. Instead of benefiting the U.S. economy, the implementation of tariffs will diminish domestic manufacturing production, reduce income growth, and jeopardize broad-based prosperity.

Tariffs Increase the Cost of Living for Consumers

Wholesalers and retailers generate revenues by applying percentage mark-ups on their costs – all their costs, which includes tariffs. Consequently, a large U.S. tariff increase will significantly add to consumers costs. A typical wholesaler markup is around 20 percent, and a typical retailer markup is around 50 percent – although the actual markups will vary significantly by industry.[4]

Applied against a potential 25 percent tariff rate, and assuming that full tariff costs are fully borne by consumers, the average wholesale and retail markups would cause the prices of imports to increase by 45.0 percent. This is an increase that is 80 percent larger than the increase in the tariff rate. Therefore, accounting for the standard practices of actual businesses illustrates that the potential cost increases are significantly higher than the increase in the average tariff rate – and consumers could easily end up paying far more than the tariff increase itself!

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The reduced consumption bodes ill for the U.S. economy. Import businesses and retailers will be particularly hard hit as the higher consumer costs will reduce their sales. While sales volumes are lower, consumers will still be paying more for fewer goods and services; in other words, tariffs are making U.S. families worse off. Adding to the costs, the lower sales of imports will increase the number of layoffs increasing the U.S. unemployment rate. These negative impacts are ironic given that the tariffs are supposed to increase the volume of domestic economic activity.

While this analysis has assumed that the entire value of the tariff would be passed through to the direct users of the imports, in practice, some of the costs will be borne directly by the businesses – the extent borne by businesses varying depending on the product in question. Since higher business costs from tariffs will also reduce their profitability, there will still be a substantial negative impact on sales and employment regardless of whether it is consumers or businesses that directly bear the incidence of President Trump's comprehensive tariff policy. These higher costs and reduced profits will discourage overall economic growth, diminish job growth opportunities, decrease domestic production, and reduce families' incomes.

Tariffs Increase Costs for Domestic Manufacturers

The static theory of tariffs also fails to recognize that not all imports are final consumer goods. Many imports are intermediate goods that domestic businesses use when producing their products. Consequently, a Trump Administration tariff plan, if implemented, would directly increase the costs for families purchasing domestically produced goods and reduce the profitability of domestic manufacturers.

Measuring this issue, a study by the U.S. Commerce Department broke down the value of domestic manufacturing (referred to as gross output) for 2022.[5] According to this analysis, domestic manufacturing firms produced $6.9 trillion in gross output; of this gross output, imported inputs accounted for 20 percent of the final value. Based on these values, imports accounted for $1.38 trillion of domestic manufacturers' costs.

Applying the 25.0 percent tariff on the imports that domestic manufacturers use ($1.38 trillion), and domestic manufacturing costs will rise by $345 billion to $1.7 trillion. Assuming that the share of value added by U.S. manufacturers maintains a constant percentage, then the total costs for U.S. manufacturers would increase by 7.7 percent. Accounting for the impact on wholesaler and retailer markups, families would likely see a cost increase of 13.8 percent on domestically produced goods. To put these costs in perspective, a 13.8 percentage point increase in prices is about one half the growth in all consumer prices that occurred between May 2020 and December 2024 (24.2%).[6] These cost increases are in addition to the higher prices that would result from the tariffs imposed on imports that are directly used by consumers and worsen the overall economic consequences from the policy.

Table 1. Estimated Impact on the Costs of Manufacturer Gross Output Due to 25% Tariff on Imports (dollars in trillions)

	2022	After Trump Tariff	Manufacturer Price Increase	Price Increase to Consumers
Gross Output U.S. Manufacturers	$6.90	$7.43	7.7%	13.8%
Domestic Inputs	$3.11	$3.11		
Value Add	$2.42	$2.60		
Imported Inputs	$1.38	$1.73		

Source: Author calculations based on U.S. Department of Commerce study

Compounding this problem, before most final goods are produced, today's manufacturing process will often require the products to cross international borders multiple times. The production process for domestically produced cars exemplifies this process – many domestically manufactured cars are shipped between the U.S., Mexico, and Canada multiple times before the final automobile is completed. Due to this production process, a domestically manufactured car will be subject to multiple rounds of 25 percent tariffs if these levies were ever implemented. This compounding significantly increases the final retail price of domestically produced automobiles well above the increases estimated in Table 1.

Prices Will Also Increase for Domestic Manufacturers Competing with the Importers

Another consideration ignored by the static analysis is the responses of domestic manufacturers that compete with the imported goods. The static analysis assumes that domestic manufacturers that directly compete with the tariffed goods have the immediate capacity to expand their production and will do so without their costs increasing. The case of domestic steel manufacturers illustrates that this is typically not the case.

In February 2018, the Trump administration imposed a 25 percent tariff on steel. Domestic producers responded by increasing prices on U.S. consumers. As CNN Business reported in 2018, "steel companies are feasting on a price spike from Trump's 25 percent steel tariff. The benchmark price of US-made steel has zoomed 41 percent higher since the start of the year to $917 per short ton, according to S&P Global Platts."[7]

These impacts indicate that the tariffs harmed consumers both because the costs of imports increased and the costs of domestically produced steel increased. In effect, the Trump tariffs subsidized the domestic firm's profits while increasing costs on consumers of their products. In the case of steel, those consumers were other manufacturers that use manufactured steel as part of their production process. This meant that the costs of creating all sorts of products from automobiles to multi-family housing increased. The result was higher pricing pressures on households and lower profitability for businesses.

Another consideration ignored by the static analysis is the responses of domestic manufacturers that compete with the imported goods.

While the price impacts from these tariffs are overwhelmed by the subsequent inflationary surge that started in 2021, the annual producer price index for manufacturing industries did accelerate in 2018 following the imposition of the steel tariffs – in 2017 the producer prices for manufacturing industries increased 3.5 percent, which then accelerated to a 4.6 percent increase in 2018.[8] This one-time acceleration in manufacturing costs is precisely what would be expected from the Trump administration's 25 percent global tariff on steel and aluminum imports.

Broad-based tariffs applied to most (or all) of our trading partners would be expected to lead to a much larger price rise. This price spike would worsen the cost-of-living problems harming too many U.S. households.

Capital Market Impacts Worsen the Consequences

Missing from the above analysis are the responses in the capital and currency markets.

Starting with the capital markets, politicians typically focus on the flows of goods and services between countries while ignoring the flows of investment dollars. This provides an inaccurate view of international trade's full benefits.

From an accounting perspective, every country that runs a trade deficit is also running a capital surplus. This duality is an accounting identity. A capital surplus means that more businesses and investors from other countries are investing in the U.S. economy, on net. These dollar investments play a pivotal role spurring innovation and creating jobs in the U.S. The large dollar inflows purchasing U.S. Treasury debt also plays a key role keeping the cost of government debt lower. The lower costs of government debt encourage a lower interest rate environment overall so interest rates on home mortgages, automobile loans, and credit card debt are also lower.

These dollar inflows are tracked in the capital accounts. And if politicians focused on the capital account rather than the trade account, they may be obsessed with ensuring that the country runs a capital surplus rather than a trade surplus. Of course, a capital surplus is the same thing as a trade deficit. Such is the confusion that surrounds international trade statistics. Put differently, the U.S. trade deficit provides investors from other countries the resources they need to invest their capital into the U.S. economy.

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This all matters with respect to the Trump administration's tariff ideas because if successful at lowering the trade deficit, the proposals will also be reducing the capital surplus. Fewer foreign businesses and investors will be providing the resources necessary to drive the AI revolution or to fund the huge federal budget deficit. Several adverse consequences will result.

First, with less investment into key U.S. industries, productivity growth will suffer. A less productive economy would reduce the U.S.' long-run growth potential. Second, less demand for U.S. Treasuries will put upward pressure on the government's borrowing costs. The costs required to finance the federal budget deficit, already at excessive levels, will increase further. Third, the higher borrowing costs would not be confined just to the Treasury market. The costs for mortgages, car loans, and small business lending will rise in step. These higher costs will dampen economic growth.

The impact on the currency markets matters as well. Comprehensive tariffs reduce U.S. importers demand for foreign currencies, which will put pressure on those currencies to depreciate relative to the U.S. dollar – the dollar will relatively appreciate. An appreciating dollar reduces the disincentives to purchase imports (because the cost of imports declines when the dollar appreciates) that the tariffs created. How much these considerations matter will depend on the magnitude of the currency changes.

Net Revenues for the Government Are Unlikely to Grow

As noted above, one goal of levying tariffs is to raise revenues for the federal government. However, the actual revenues raised will likely significantly underperform estimates. First, the tariffs will discourage the consumption of imported goods and services by both consumers and manufacturers. Therefore, it is likely that the value of total imports will decline, reducing the total revenues directly raised by the tariffs.

Second, the adverse impacts on income growth and corporate profitability will reduce the income and corporate income taxes collected by the federal government, further eroding the estimated static increase in tariff revenues.

Third, the slower economic growth and rising levels of unemployment will increase spending on federal income support programs. These higher expenditures, while not a direct offset of revenues, will either further increase the budget deficit or reduce spending in other parts of the budget. Either way, these additional costs will further erode the fiscal health of the federal government.

Fourth, net revenues available to the government will be further constrained due to the higher interest rates that will force the government to devote a larger share of the budget toward interest payments.

Accounting for all these dynamic consequences, the proposed tariffs are not nearly the stable source of revenues that the static estimates would indicate.

Conclusion: Economic Losses from Tariffs Will Be More Than the Sum of the Parts

Tariffs are a tax on consumption and production. By raising costs and reducing efficiencies, tariffs are anti-growth policies that reduce income growth, increase the cost of living, and decrease job growth.

The Trump Administration's focus on increasing U.S. manufacturing through tariffs will not generate sustained income growth for families across the country. Consider that when excluding energy, the US has a $63 billion trade surplus with Canada as of 2023.[9] A trade war will surely jeopardize these sales to the detriment of U.S. manufacturers, workers, and consumers.

Instead of implementing these anti-growth policies, the best way for the Trump Administration to promote broad based prosperity is to implement a consistent pro-growth economic platform.

These policies would prioritize reining in out-of-control government spending (including entitlement reform), implementing a broad-based flat tax, reforming overly burdensome regulations, and promoting global free trade. Such an economic platform has demonstrated its ability to promote broad-based prosperity by meaningfully improving the incentives to work, save, and invest.

Endnotes

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Dr. Winegarden has 25 years of business, economic, and policy experience with an expertise in applying quantitative and macroeconomic analyses to create greater insights on corporate strategy, public policy, and strategic planning. He advises clients on the economic, business, and investment implications from changes in broader macroeconomic trends and government policies. Clients have included Fortune 500 companies, financial organizations, small businesses, state legislative leaders, political candidates and trade associations.

Dr. Winegarden's columns have been published in the *Wall Street Journal*, *Chicago Tribune*, *Investor's Business Daily*, *Forbes.com*, and *Townhall.com*. He was previously economics faculty at Marymount University, has testified before the U.S. Congress, has been interviewed and quoted in such media as CNN and Bloomberg Radio, and is asked to present his research findings at policy conferences and meetings. Previously, Dr. Winegarden worked as a business economist in Hong Kong and New York City; and a policy economist for policy and trade associations in Washington D.C. Dr. Winegarden received his Ph.D. in Economics from George Mason University.

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