Tariff Wave: Impact on Global Trade and India's Economy

by CA Farhad G Wadia JHS Consulting (10-04-25)

Trade Wars: History, Pros & Cons, and U.S.-China Example

What Is a Trade War?

A trade war is an economic dispute between two countries. It can occur when one country retaliates against another's perceived unfair trading practices with restrictions, such as tariffs, on imports.

Domestic trade unions or industry lobbyists can pressure politicians to make imported goods less attractive to consumers, pushing international policy toward a trade war.

Also, trade wars are often a result of a misunderstanding of the widespread benefits of free trade.

Key Takeaways

- A trade war occurs when one country retaliates against another by raising import tariffs or placing other restrictions on imports.
- Trade wars are a side effect of protectionist policies and are controversial.
- Advocates say trade wars protect national interests and provide advantages to domestic businesses.
- Critics of trade wars claim that they ultimately hurt local companies, consumers, and the economy.

Understanding a Trade War

Trade wars are usually considered a side effect of protectionism. Protectionism refers to government actions and policies that restrict international trade.

A country will generally undertake protectionist actions to shield domestic businesses and jobs from foreign competition. Protectionism is also a method used to balance trade deficits.

A trade deficit occurs when a country's imports exceed the amounts of its exports. A tariff is a tax or duty imposed on the goods imported into a nation.

Growth of Damaging Effects

In an era of global trade, a trade war can become very damaging to the consumers and businesses of both nations, and the contagion can grow to affect many aspects of both economies.

A trade war that begins in one sector can grow to affect other sectors. Likewise, a trade war that begins between two countries can affect other countries not initially involved in the trade war.

Trade War vs. Other Protectionist Actions

A trade war is distinct from other actions taken to control imports and exports, such as sanctions. The trade war has detrimental effects on the trading relationship between two countries because its goals are related specifically to trade. Sanctions may have philanthropic goals.

Other non-tariff protectionist policies can be implemented by placing a cap on import quotas, setting clear product standards, or implementing government subsidies for processes to deter outsourcing.

History of Trade Wars

Trade wars are not an invention of modern society. Such battles have been going on for as long as nations have conducted trade with one another.

For example, colonial powers fought with each other over the right to trade exclusively with overseas colonies in the 17th century.

British-China

The British Empire has a long history of such trade battles. One example is the opium wars of the 19th century with China.

The British had been sending India-produced opium into China for years when the Chinese emperor decreed it to be illegal. Attempts to settle the conflict failed, and the emperor eventually sent troops to confiscate the drugs.

However, the might of the British navy prevailed, and China conceded to the entry of additional foreign trade into the nation.

U.S.-Europe

In 1930, the United States enacted the Smoot-Hawley Tariff Act, raising tariffs to protect American farmers from European agricultural products.1

This act increased already hefty import duties to almost 40%. In response, several nations retaliated against the U.S. by imposing their own higher tariffs, and global trade declined worldwide.

As America entered the Great Depression, which was aided greatly by disastrous trade policies, President Roosevelt began to pass several acts to reduce trade barriers, including the Reciprocal Trade Agreements Act.2

U.S.-China and Others

Beginning in January 2018, President Trump imposed a series of tariffs on everything from steel and aluminum to solar panels and washing machines.3

Some of the effects impacted goods from the European Union (EU) and Canada, as well as China and Mexico. Canada retaliated by imposing a series of temporary duties on American steel and other products.

The EU also imposed tariffs on American agricultural imports and other products, including Harley Davidson motorcycles.4

By May 2019, tariffs on Chinese imports impacted nearly $200 billion of imports.5 As with all trade wars, China retaliated and imposed stiff duties on American imports.

A study by the International Monetary Fund (IMF) found that U.S. importers of goods primarily shouldered the cost of the tariffs on Chinese goods.6

These costs were eventually passed on to the American consumer in the form of higher prices, which was not what the trade war was intended to accomplish

Advantages and Disadvantages of a Trade War

The advantages and disadvantages of trade wars in particular, and protectionism in general, are the subject of fierce and ongoing debate.

Advantages

Proponents of protectionism argue that well-crafted policies provide competitive advantages. By blocking or discouraging imports, protective policies throw more business toward the domestic producers, which ultimately creates more American employment.

These policies can also serve to overcome a trade deficit. Additionally, proponents believe that painful tariffs and trade wars may be the only effective way to deal with a nation that continues unfair or unethical trading policies.

Disadvantages

Critics argue that protectionism often hurts the people it is intended to protect by choking off markets and slowing economic growth and cultural exchange.

Consumers may begin to have less choice in the marketplace. They may even face shortages if there is no ready domestic substitute for the imported goods that tariffs have impacted or eliminated.

Having to pay more for raw materials hurts manufacturers' profit margins. As a result, trade wars can lead to price increases, with manufactured goods, in particular, becoming more expensive. This can then spark inflation in the local economy, overall.

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Pros

- Protects domestic companies from unfair competition
- Increases demand for domestic goods
- Promotes local job growth
- Improves trade deficits
- Punishes nation with unethical trade policies

Cons

- Increases costs and induces inflation
- Causes marketplace shortages, reduces choice
- Discourages trade
- Slows economic growth
- Hurts diplomatic relations, cultural exchange

Example of a Trade War

While running for President in 2016, Donald Trump expressed his disdain for many current trade agreements, promising to bring manufacturing jobs back to the U.S. from other nations where they had been outsourced, such as China and India.

2018

After his election, he embarked on a protectionist campaign. President Trump also threatened to pull the U.S. out of the World Trade Organization (WTO), an impartial, international entity that regulates and arbitrates trade among the over 160 countries that belong to it.89

In early 2018, President Trump stepped up his efforts, particularly against China. He threatened a substantial fine over alleged intellectual property (IP) theft and significant tariffs. The Chinese retaliated with a 25% tax on over 100 U.S. products.10

Throughout 2018, the two nations continued to threaten each other, releasing lists of proposed tariffs on various goods. Although China responded with tariffs of its own, the American duties did have an impact on the Chinese economy, hurting manufacturers and causing a slowdown.

2019

In December, each nation agreed to halt the imposition of any new taxes. The tariff war cease-fire continued into 2019. In the spring, China and the U.S. seemed on the verge of a trade agreement.

At the beginning of May, Chinese officials took a new hard line in negotiations, refusing to make changes in their company-subsidizing laws and insisting on the lifting of the current tariffs.

Angered by this apparent backtracking, the President doubled down, announcing on May 5, 2019, that he was going to increase tariffs, as of May 10, from 10% to 25% on $200 billion worth of Chinese imports.5

He may have felt emboldened by the fact that the U.S. trade deficit with China had fallen to its lowest level since 2014.

China halted all imports of farm products by state-owned firms in retaliation. The Asian nation's central bank also weakened the yuan above the seven per dollar reference rate for the first time in over a decade, leading to concerns about a currency war.

2020

Perhaps realizing that this was mutually destructive, the U.S. and China agreed to a trade deal that was signed on Jan. 15, 2020.11

2024

However, the U.S. continued raising trade barriers. In 2024, President Biden raised the tariffs on electric vehicles to 100%, with solar cells and semiconductors facing tariffs of 50%.12

Other technology products also faced sharp tariff increases, causing China to pledge further retaliation.13

Is the United States in a Trade War With China?

Yes. In 2024, the U.S. implemented extreme tariffs that some experts described as a trade war. President Biden raised the tariff on Chinese electric vehicles to 100%, and increased the tariff on lithium-ion batteries to 25%. The tax rates on solar cells and semiconductors increased to 50%. These tariffs were meant to protect domestic industries, at the cost of denying Americans access to cheaper Chinese technologies. As of early 2025, it was expected that President Trump might continue to impose and/or raise tariffs, and not just on China, but on Mexico and Canada, as well.14

Reuters. "North America Braces for New Trump Tariffs as Saturday Deadline Nears."

How Do Tariffs Affect the Economy?

Like other trade policies, tariffs on trade have both winners and losers. Tariffs can generate billions of dollars of added revenue for a country. Domestic industries and manufacturers tend to benefit. Consumers and producers who use those products associated with tariffs have to pay higher prices, which can have an inflationary effect on the rest of the economy. As for retaliatory tariffs imposed by foreign countries on the U.S., they make exports more expensive to buyers in those countries but reduce U.S. GDP by a negligible amount.15

Are Tariffs Good or Bad for the Economy?

Most economists agree that tariffs are bad for the economy, since they prevent countries from reaping the benefits of economic specialization. However, there may be additional benefits to protecting certain domestic industries, such as manufacturing or defense. While it may be cheaper for a country to source arms on the world market, there are also strategic advantages to maintaining domestic production capacity, even if such products are available at lower prices elsewhere.

The Bottom Line

A trade war occurs when a government imposes punitive tariffs on another country, often in response to tariffs or protectionist trade policies raised by the other nation.

Trade wars tend to be mutually damaging, as higher costs of trade ultimately are paid by consumers. However, advocates believe that trade wars can help protect local industries.

What Are Tariffs?

A tariff is a type of tax levied by a country on an imported good at the border. Historically, tariffs have been used by governments to collect additional revenue. But they are also a way for governments to try to protect domestic producers.

As a protectionist tool, a tariff increases the prices of imports. Due to that, consumers may choose to buy other, relatively less expensive domestic goods instead.

Key Takeaways

- Tariffs are duties on imports imposed by governments to raise revenue, protect domestic industries, or exert political leverage over another country.
- Tariffs often result in unwanted side effects, such as higher consumer prices.
- Tariffs have a long and contentious history, and the debate over whether they represent good or bad policy rages on to this day.

Understanding Tariffs

In today's global economy, many products made in a home country consist of parts obtained from other countries. Or, these products might have been assembled overseas. As a result, tariffs can affect the prices of products made in the home country as well as those imported from other countries.

Many economists argue that tariffs create market distortions that can harm domestic consumers over time. They can also lead to a trade war if trading partners impose tit-for-tat tariffs.

The process of setting tariff rates involves a combination of economic, political, and strategic issues. Governments engage in complex negotiations and considerations of reciprocity with trading partners.

Tariffs also can be used as a political tool to manage relationships.

How a Tariff Works

Tariffs are used to restrict imports by increasing the price of goods and services purchased from another country. This makes them less attractive to domestic consumers. There are two types of tariffs:

- A specific tariff is levied as a fixed fee based on the type of item, such as a $1,000 tariff on a car.
- An ad valorem tariff is levied based on the item's value, such as 10% of the value of the vehicle.1

ScienceDirect. "Ad Valorem Tariff vs. Specific Tariff: Quality-Differentiated E-Tailers' Profitability and Social Welfare in Cross-Border E-Commerce."

Reasons for Tariffs

Governments may impose tariffs to raise revenue or protect domestic industries—especially nascent ones—from foreign competition. By making foreign-produced goods more expensive, tariffs can make domestically-produced alternatives more attractive.

Governments that use tariffs to benefit particular industries often do so to protect companies and jobs. Tariffs can also be used as an extension of foreign policy: Imposing tariffs on a trading partner's main exports is a way to exert economic leverage.

Side Effects

Tariffs can have unintended side effects:

- They can make domestic industries less efficient and innovative by reducing competition.
- They can hurt domestic consumers since a lack of competition tends to push up prices.
- They can also generate tensions by favoring certain industries, or geographic regions, over others.
- When used to pressure a rival country, a relationship can devolve into an unproductive cycle of retaliation, sometimes known as a trade war.

For example, tariffs designed to help manufacturers in cities may hurt consumers in rural areas who do not benefit from the policy and are likely to pay more for manufactured goods.

What Is an Example of a Tariff?

An example of a tariff could be a tax on steel imports. This means that any steel imported from another country would incur a cost—for example, 5% of the value of the imported goods—that would be paid by the individual or business importing the goods.

What Is the Purpose of a Tariff?

Tariffs are a way for governments to not only generate revenue but also protect domestic businesses. Tariffs increase the price of imported goods, making domestic goods cheaper in comparison.

Who Benefits From a Tariff?

The importing countries usually benefit from a tariff, as they are the ones imposing the tariff and collecting the revenue. Domestic businesses also benefit from tariffs because they make their goods cheaper than imported goods, hence driving up the demand for their products.

How Do Tariffs Hurt Consumers?

Tariffs hurt consumers in the country that imposes the tariff because of the increased prices of imported goods. Since an importer has to pay the cost of the tariff on the goods that they import, they pass this increased cost on to consumers in the form of higher prices.

How Do Tariffs Affect You?

If you are a consumer, tariffs affect you because they result in an increase in the price of imported goods.

If you are a domestic producer, tariffs can help you by making your goods cheaper compared to international goods, thus increasing your sales.

If you export your goods to other countries that impose tariffs, this may reduce the demand for your goods, thus hurting your business.

The Bottom Line

Tariffs are taxes imposed on imported goods. They often result in higher prices for consumers. They can impact various demographics, and in particular burden lower-income consumers. They pose challenges for small businesses reliant on imported materials.

The first Trump administration focused a great deal of its attention on imposing tariffs. Broadly speaking, most economists feel they had little impact, positive or negative, for the overall economy of the U.S.

Protectionism: Examples and Types of Trade Protections

What Is Protectionism?

Protectionism refers to government policies that restrict international trade to help domestic industries. Protectionist policies are usually implemented with the goal of improving economic activity within a domestic economy but can also be implemented for safety or quality concerns.

Key Takeaways

- **Protectionist policies place specific restrictions on international trade for the benefit of a domestic economy.**
- **Protectionist policies typically seek to improve economic activity but may also be the result of safety or quality concerns.**
- **The value of protectionism is a subject of debate among economists and policymakers.**
- **Tariffs, import quotas, product standards, and subsidies are some of the primary policy tools that a government can use in enacting protectionist policies.**
- **Understanding Protectionism**
- Protectionist policies are typically focused on imports but may also involve other aspects of internationa

Types of Protectionist Tools

Tariffs

Import tariffs are one of the top tools that a government uses when seeking to enact protectionist policies. There are three main countervailing import tariff concepts that can be theorized for protective measures. In general, all forms of import tariffs are charged to the importing country and documented at government customs. Import tariffs raise the price of imports for a country.

Import Quotas

Import quotas are nontariff barriers put in place to limit the number of products that can be imported over a set period of time. The purpose of quotas is to limit the supply of specified products provided by an exporter to an importer. This is typically a less drastic action that has a marginal effect on prices and leads to higher demand for domestic businesses to cover the shortfall.

Quotas may also be put in place to prevent dumping, which occurs when foreign producers export products at prices lower than production costs. An embargo, in which the importation of designated products is completely prohibited, is the most severe type of quota.

Product Standards

Product safety and low-quality products or materials are typically top concerns when enacting product standards. Product standard protectionism can be a barrier that limits imports based on a country's internal controls.

Some countries may have lower regulatory standards in the areas of food preparation, intellectual property enforcement, or materials production. This can lead to a product standard requirement or a blockage of certain imports due to regulatory enforcement. Overall, restricting imports through the implementation of product standards can often lead to a higher volume of production domestically.

For example, consider French cheeses made with raw instead of pasteurized milk, which must be aged for at least 60 days before being imported to the United States. Because the process for producing many French cheeses involves aging for 50 days or less, some of the most popular French cheeses are banned from the U.S., providing an advantage for U.S. producers.1

Government Subsidies

Government subsidies can come in various forms. Generally, they may be direct or indirect. Direct subsidies provide businesses with cash payments. Indirect subsidies come in the form of special savings such as interest-free loans and tax breaks.

Effects on India

"The odds are, the trade war the Trump administration is pursuing is likely going to — in economic terms — harm everybody else much more than the United States."

- Adam Posen, President Peterson Institute for International Economics.

India being the fastest growing economy in the world today will face the consequences of this trade war. The basic principles of Demand and Supply would come into the picture. The shortage of supply of a good, either finished or raw material will most likely increase the consumption price for the consumer. Further, the burden of additional taxes would also be borne by the end user. The effects won't be limited to a particular area or sector but they would be multifold:

Increase in Exports

The direct impact on the Indian market could be an increase in the India- US trade market as the US-China trade quota could fall given the situation of tariffs. The US could look forward to finding alternatives for Chinese products whose prices have gone to the sky post-tariff levying. India, which has a $60 billion trade deficit with China, may stand to benefit as Xi Jinping moves to slap levies on US goods such as soybean and simultaneously removes levies from Indian exports. (Beijing has recently slashed tariffs on soybean imported from India, South Korea, Bangladesh, Laos and Sri Lanka from the current three per cent to zero). If Chinese exports to the US slow down as a result of the trade war, India may be able to gain significant traction in textile, garments and gems and jewellery. However, China could still find crude oil from alternative sources such as West Africa which has a similar quality as US crude, the US would find it hard to find an alternative market as big as China. However, if crude oil prices fall as a result, then other things constant, India benefits from this perspective.

Increase in Interest Rates

Rising interest rates in America could mean a few bad days for the India's equity market. As higher interest rates in the US will lead to people withdrawing their money from bonds and equities from emerging markets like ours and investing it into their own economy which guarantees them with better and higher interest rates and returns. It can be said that a surge in our domestic inflows is a reassuring factor for our Indian equities but higher rates do make investing in the United States a better option as of now.

Volatile Markets

Increase in interest rates by the Federal Reserve in the United States, because of importers passing on their increased costs of raw material will affect emerging economies such as India, both for their debt and equity market. Even a minor disruption in the US financial markets has major implications for India. The three external risk factors – higher tariffs, rising interest rates and elevated bond sales are coming at a time when the Indian banking system is already stressed with NPAs. The economy of the country, especially the financial markets have to be ready for a lot of volatility and stress from the combined effects of global and domestic challenges. Increase in Supplies

Supply chain disruption is another threat which looms large, as the Chinese export to the the US is made up of 30% imports it makes and then finishes these intermediate products to final products. In the event of the export demand from the US going down, the imports will be affected directly. This could lead to excess supply in the emerging markets from where these are imported. India is one of these markets and imports a variety of intermediate Goods.

"India can become more competitive in segments such as textile, garments and gems and jewellery since India already has an edge," says says economist Upasna Bhardwaj of Kotak Mahindra Bank in a Livemint article. However, this is doubtful in the short run because China's exports to the US are much more diverse and it's a tall order for India to fill the gap.

Demand: Market Access

- Lower tariff and non-tariff barriers on U.S. exports
- Reduce +$300 billion trade deficit
- Stop subsidizing companies

Demand: IP Reform

- End forced tech transfers for JVs and foreign ventures
- Greater intellectual property rights enforcement
- Stop cyber-intrusions into U.S. companies, gov't

Demand: Enforcement Mechanism for Deal

- Tariffs gradually removed to ensure compliance
- Tariff "snap-back' if China reneges on commitments
- References to specific Chinese laws that must be changed

Response (to date):

- Resume purchases of U.S. soy beans, rice, and LNG
- Cut tariffs on U.S. cars and agricultural goods

Response (to date):

- Announce new expanded punishments for IP infringement
- Pledge to treat state, private and foreign firms equally
- Considering a law that would forbid the practice of forced tech transfer

Response (to date)

- Removal of all tariffs
- Last-minute revisions that scuttled deal reportedly removed references to specific Chinese laws in agreement

Increase in Customs Enforcement

- U.S. Customs and Border Protection ("CBP") has increased enforcement in response to China tariffs
  - Increase in CF-28s (requests for information) regarding classification, country of origin
  - New "Audit Survey Program" by CBP Centers of Excellence & Expertise focused on first sale programs
- Document any changes to classification, country of origin, first sale in anticipation of CF-28 or survey

IMPACT: Globalization and Its Future

1. The world economy does not (yet) appear to be de-gobalizing

2. Global trade was remarkably resilient in the face of COVID

3. The US-China trade war is finally impacting the geography of world trade (but less so value-added trade)

4. Friendshoring policies may dramatically backfire

5. Diversification or increased resilience would be very costly