

GLOBAL ECONOMIC SHIFT: HOW TRUMP'S TARIFF WAR IS RESHAPING GLOBAL TRADE DYNAMICS

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ABSTRACT

This study investigates how President Donald Trump's tariff war reshaped global trade dynamics between 2015 and 2023 by analyzing panel data from major U.S. trading partners using Fixed Effects and System Generalized Method of Moments (GMM) models. Trade Volume is examined in relation to Tariff Rate, GDP Growth, Inflation, Employment, and Production Level. While the Fixed Effects model shows a short-term increase in trade volume following tariff hikes likely due to trade diversion or stockpiling the GMM results reveal that tariffs ultimately have a negative and statistically significant effect, disrupting trade flows and increasing costs. GDP growth initially appears to reduce trade but shows a positive effect when accounting for dynamic factors, while inflation consistently dampens trade performance. Employment presents mixed results, reflecting sector-specific impacts, and production shows a strong, positive influence, affirming its role in driving trade. Model diagnostics confirm the robustness of the analysis. Based on these findings, the study recommends a strategic shift from protectionist policies toward more open, cooperative trade practices, supported by macroeconomic stability, investment in domestic production, inclusive labor policies to cushion employment shocks, and trade diversification strategies to enhance resilience in an increasingly protectionist global economy.

Keywords: Global Trade Dynamics, Tariff Policy, Trade War, U.S.–China Economic Relations

JEL Classification: F13, F14, F51, F68

Introduction

The Trump administration's tariff war, initiated in 2018, marked a significant departure from decades of U.S. support for free trade. As part of President Donald Trump's "America First" economic strategy, the trade war began with tariffs on imported solar panels and washing machines, followed by steep levies on steel and aluminum (Bown, 2019). These actions quickly escalated into a full-blown trade conflict, particularly with China, but also involving the European Union, Mexico, Canada, and other key partners. At the heart of this trade war was a set of economic policies designed to reduce the U.S. trade deficit, revive domestic manufacturing, and counter what the administration described as unfair trade practices, especially China's alleged intellectual property theft and forced technology transfers (Liu & Woo, 2018; Evenett, 2019).

The key players in this global economic dispute were not limited to the U.S. and China. Countries across Europe and North America were pulled into the fray through retaliatory measures and supply chain disruptions, leading to uncertainty in international markets (Fajgelbaum *et al.*, 2024). The stated goals of the tariffs were multifaceted: to protect American jobs, encourage domestic production, assert national economic sovereignty, and rebalance long-standing trade asymmetries (Bown, 2020). While proponents viewed the tariffs as necessary corrective measures, critics argued they provoked economic inefficiencies, raised consumer prices, and strained diplomatic relations. This study, therefore, examines how U.S. tariff changes affected trade dynamics and macroeconomic variables.

Conceptual Clarification

Tariffs

Tariffs are government-imposed taxes on imported goods, designed to raise the cost of foreign products and give a price advantage to domestically produced goods. According to Krugman and Obstfeld (2018), tariffs are among the oldest instruments of trade policy, employed to regulate cross-border commerce and protect local industries. There are several types of tariffs. The most common is the ad valorem tariff, which is levied as a percentage of the value of the imported good. Another is the specific tariff, charged as a fixed amount per unit of the good. Some governments also apply compound tariffs, which combine both ad valorem and specific components (Irwin, 1996).

The application of tariffs has long been a central issue in the debate between protectionism and free trade. Protectionist theory argues for the imposition of tariffs to shield domestic industries from foreign competition, promote local employment, and secure strategic economic sectors. In contrast, advocates of free trade posit that tariffs distort market efficiency, reduce consumer welfare, and undermine the principle of comparative advantage (Ricardo, 1817; Bhagwati, 2002). The infant industry argument justifies temporary tariffs for developing sectors, while strategic trade theory supports tariffs in industries exhibiting economies of scale. Nonetheless, empirical studies caution that excessive reliance on tariffs may lead to trade retaliation and inefficiencies in production and consumption (Irwin, 2002).

Global Trade Dynamics

Tariffs significantly influence global trade by altering the cost structure of imports, modifying trade relationships, and disrupting long-established supply chains. As Bown and Irwin (2019) observe, the imposition of tariffs raises the final cost of goods, thereby discouraging imports and incentivizing either domestic production or a shift in sourcing to non-tariffed countries. This frequently leads to trade diversion rather than trade creation, especially within multilateral trade environments. Moreover, tariffs introduce uncertainty into international agreements, reduce investor confidence, and often provoke retaliatory actions that further destabilize global trade flows (Handley & Limão, 2017).

One of the most critical concepts in today's trade environment is the global value chain (GVC), which refers to the international fragmentation of production processes across multiple countries to optimize costs, efficiency, and specialization. Tariffs can severely disrupt these chains by increasing the cost of intermediate goods and forcing firms to restructure their supplier networks (Baldwin, 2016). For instance, a tariff imposed on Chinese inputs used in American manufacturing can lead to increased costs for U.S. firms and reduced competitiveness. Koopman, *et al.* (2014) emphasize that tariffs can reduce both backward and forward linkages in trade, diminishing global economic interdependence and eroding productivity gains accrued through specialization and economies of scale.

Analysing the Impact

Immediate Economic Impact on the United States

The imposition of tariffs during the Trump administration had substantial implications for various sectors of the U.S. economy, including industry, employment, consumer prices, and inflation. According to Amiti, *et al.* (2019), the tariffs imposed between 2018 and 2019 resulted in higher input costs for American firms, which in turn led to increased prices for consumers and reduced manufacturing output. Trade Partnership Worldwide (2019) estimated that the combined effect of tariffs led to a net loss of approximately 935,000 jobs, with only marginal gains in protected sectors such as steel and aluminum. While sectors benefiting from tariff protection experienced short-term growth, downstream industries, especially those relying on imported intermediate goods, suffered production slowdowns and layoffs. In terms of consumer impact, Fajgelbaum *et al.* (2024) found that the average household bore additional costs of approximately \$600 to \$1,200 annually due to higher prices on tariffed goods. Inflationary effects were also evident: tariff-related pass-through effects raised core inflation by up to 0.2 percentage points, as firms transferred costs to consumers in sectors such as automobiles and electronics.

Impact on Other Countries

China, the primary target of U.S. tariffs, responded with retaliatory duties covering approximately 84% of American exports, severely affecting sectors like agriculture and energy (Fang *et al.* 2020). Although China's export growth declined initially, it rapidly diversified trade relations, strengthened domestic consumption, and deepened ties with regional partners through initiatives such as the Belt and Road Initiative. According to Li, He, and Lin (2021), while Chinese GDP growth dipped by about 0.5 percentage points during the peak of the tariff war, its long-term industrial upgrading efforts helped cushion broader economic shocks. Other key players including Canada, Mexico, and the European Union also faced tariff hikes on goods like steel, aluminum, and autos. Retaliatory tariffs and market uncertainty adversely affected bilateral trade flows and investment confidence (Bown & Kolb, 2022). The economic impact was uneven: for example, Canada experienced a measurable decline in manufacturing exports, while EU producers faced higher compliance

and logistics costs. Emerging economies, particularly those integrated into U.S.–China trade circuits, saw heightened volatility in capital flows and exchange rates, with foreign direct investment temporarily diverted to Southeast Asia as firms sought to bypass tariffs.

Effects on Supply Chains

Global supply chains, particularly those tied to advanced manufacturing and technology sectors, were significantly disrupted by the introduction of tariffs. Baldwin and Freeman (2020) emphasize that modern production networks depend on seamless cross-border coordination, which tariffs interrupt by increasing costs and generating regulatory uncertainty. Firms sourcing intermediate goods from China had to rapidly reevaluate supplier networks, often shifting production to countries like Vietnam, India, and Mexico. Grossman, *et al.* (2021) argue that these shifts created “search frictions” in global value chains, leading to temporary inefficiencies and capacity underutilization. Multinational corporations responded by reshoring or regionalizing supply lines, but such transitions entailed high logistical costs and time delays. Additionally, smaller firms with limited flexibility faced challenges in renegotiating contracts or retooling operations, exacerbating the competitive gap between large and small enterprises. These adjustments contributed to a broader reconfiguration of trade architecture, with long-term implications for global competitiveness.

Global Economic Growth

The global economic consequences of the tariff war were immediate and far-reaching. In the short term, U.S. GDP growth was reduced by approximately 0.7 percentage points, while long-term output was projected to remain 0.4–0.6% below pre-tariff trends (Furman & Seamans, 2019). Countries highly dependent on trade with either the U.S. or China faced recessionary pressures due to shrinking export volumes and rising uncertainty. For instance, Canada’s GDP was estimated to contract by 2.2% under the revised tariff regime, and Mexico experienced slowed investment and lower export earnings (Caliendo & Parro, 2015). In broader global terms, the OECD (2020) projected that aggressive reshoring and fragmentation of global supply chains could reduce global trade volume by up to 12% and global GDP by as much as 6% over the next decade. The World Bank (2021) emphasized that such declines are particularly damaging to developing economies, where trade-related income constitutes a large share of GDP. Furthermore, uncertainty surrounding future trade policies discouraged long-term investment and innovation, potentially dragging global productivity growth over the medium term.

Policy Response and Adaptation

Responses from Affected Countries

The U.S. tariff escalation during the Trump administration triggered widespread global responses, as affected countries adopted various defensive and strategic measures. China, the European Union (EU), Canada, and Mexico swiftly implemented retaliatory tariffs, targeting politically sensitive U.S. exports such as soybeans, pork, and bourbon to exert economic and political pressure on the Trump administration (Bown, 2020). In parallel, several countries pursued negotiations and trade realignments, leading to new trade agreements such as the United States–Mexico–Canada Agreement (USMCA), which replaced NAFTA with terms more favorable to U.S. interests (Evenett, 2019). The European Union accelerated free trade talks with Japan, Vietnam, and Mercosur to mitigate reliance on U.S. markets and signal support for rules-based global trade. Moreover, policy reforms in some countries focused on enhancing local industrial competitiveness and diversifying markets. The World Trade Organization (WTO) played a key but constrained role; several countries, including China and the EU, filed complaints against the U.S. for violating multilateral trade norms. However, the WTO's ability to adjudicate these disputes was weakened as the U.S. blocked appointments to the Appellate Body, effectively crippling its dispute resolution mechanism (Hopewell, 2021).

US Policy Shifts

Trump's administration marked a significant departure from decades of U.S. trade liberalization, favoring unilateral tariffs and an "America First" approach. Initially, this involved high tariffs on steel, aluminum, and hundreds of Chinese products, with the justification of protecting domestic industries and correcting trade imbalances (Irwin, 2020). Over time, however, the administration shifted from aggressive tariff imposition to targeted negotiations, culminating in bilateral agreements and modifications of existing treaties. A pivotal moment in this trajectory was the Phase-One Deal with China, signed in January 2020, where China committed to purchasing an additional \$200 billion of U.S. goods over two years and improving intellectual property protection in exchange for partial tariff relief (Bown & Irwin, 2021). Despite its symbolic significance, studies show that China fell short of its purchase commitments, partly due to disruptions from the COVID-19 pandemic. Beyond China, the Trump administration revised trade arrangements with Japan, South Korea, and the UK, often emphasizing increased U.S. market access and protections for strategic industries. The withdrawal from the Trans-Pacific Partnership (TPP) further underscored the administration's inward-looking stance, although it opened pathways for the remaining signatories to deepen ties without the U.S. (Petri & Plummer, 2018).

China's Strategy to Adapt

China responded to U.S. tariffs with a multifaceted strategy aimed at both short-term retaliation and long-term structural adaptation. In the short term, China imposed counter-tariffs on key American exports and redirected purchases to alternative suppliers such as

Brazil and Argentina for soybeans (Fang *et al.*, 2021). Strategically, China accelerated efforts to diversify its export markets through regional partnerships, notably the Regional Comprehensive Economic Partnership (RCEP), which established the world's largest free trade bloc excluding the U.S. Concurrently, China advanced its "dual circulation" strategy, emphasizing domestic demand and indigenous innovation to reduce dependence on foreign technology and markets. One of the cornerstones of China's long-term trade resilience has been the Belt and Road Initiative (BRI), which aimed to create alternative trade corridors, enhance regional infrastructure, and deepen economic ties across Asia, Africa, and Europe. The BRI, beyond being an economic project, was also a strategic counterweight to U.S. trade aggression, allowing China to assert global leadership in trade and investment (Yu, 2024). These policy shifts collectively reflect China's pragmatic recalibration in the face of sustained economic pressure from the U.S.

Theoretical Frameworks

International Trade Theories

The evolution of international trade theory is marked by three major frameworks: the Ricardian Model of Comparative Advantage, the Heckscher-Ohlin Theory, and the New Trade Theory. The Ricardian Model, developed by David Ricardo in 1817, posits that international trade is driven by differences in labor productivity among nations. It argues that even if a country holds an absolute advantage in producing all goods, it still benefits from trade by specializing in goods where it has a comparative advantage defined by lower opportunity costs. This model assumes labor as the sole factor of production and suggests that trade enhances efficiency and welfare through specialization. However, the imposition of tariffs disrupts this mechanism by raising the cost of imports, distorting comparative advantage, and leading to inefficient resource allocation. The Heckscher-Ohlin Theory, introduced by Heckscher (1919) and refined by Ohlin (1933), extends the analysis by incorporating two factors of production: labor and capital. It asserts that countries export goods that intensively use their abundant factors and import goods that use their scarce ones. This theory predicts that trade will lead to factor price equalization across nations. Tariffs, however, hinder this outcome by protecting industries that may not align with a country's factor endowment, thereby misallocating resources and impeding wage and capital return convergence. In contrast, the New Trade Theory, developed by Krugman in the late 1970s and early 1980s, introduces the concepts of economies of scale, monopolistic competition, and product differentiation. It explains why countries with similar endowments often engage in intra-industry trade and how market size and increasing returns shape trade patterns. While this theory provides a rationale for temporary protection of infant industries through tariffs, it also warns that such measures may reduce competition, hinder innovation, and ultimately lower global efficiency. Together, these theories offer a comprehensive understanding of the forces shaping global trade and the implications of trade policy interventions like tariffs.

Political Economy

Realism and liberalism are two dominant theories in international relations that offer contrasting perspectives on the use of tariffs in global trade. Realism, rooted in the works of classical thinkers like Thucydides, Machiavelli, and Hobbes, was formally developed in the modern era by Hans Morgenthau in his 1948 book *Politics among Nations*. It views the international system as anarchic, where states act in pursuit of national interest, primarily defined in terms of power and security. From a realist perspective, economic tools like tariffs are strategic instruments used to protect national industries, assert dominance, and counter the influence of rival states. For example, Trump's tariff war against China can be interpreted as a realist move to reassert U.S. geopolitical and economic power by limiting China's access to the American market and reducing dependency on foreign production. In contrast, liberalism, drawing from Enlightenment thinkers such as Kant (1795), and economic theorists like Smith and Ricardo (1776, 1817), emphasizes cooperation, economic interdependence, and the role of international institutions. Modern liberal thought, as developed by scholars like Keohane and Nye in *Power and Interdependence* (1977), argues that global peace and prosperity are best achieved through open markets, multilateral agreements, and rules-based institutions such as the World Trade Organization. From this view, tariffs are seen as harmful barriers that disrupt international cooperation, undermine trust among nations, and weaken institutional frameworks. Liberal theorists argue that Trump's unilateral tariffs not only escalated trade tensions but also damaged global supply chains and eroded confidence in international trade governance. Thus, while realism sees tariffs as tools of national power, liberalism views them as obstacles to mutual gains and global stability.

Table 1: Comparison of Realism and Liberalism in International Trade and Tariff Policy, particularly as applied to the U.S.–China trade war under President Donald Trump

Theory	Founders & Key Works	Core Assumptions	View on Tariffs
Realism	Hans Morgenthau (1948), Thucydides, Hobbes, Machiavelli	International system is anarchic; states act in pursuit of national interest and power; conflict is inevitable; emphasis on relative gains.	Tariffs are strategic tools to assert dominance, protect national industries, and limit the power of rivals (e.g., Trump's tariffs on China to counter its rising influence).
Liberalism	Immanuel Kant (1795), Adam Smith (1776), Ricardo, Keohane & Nye (1977)	International cooperation is possible through institutions, interdependence, and rule-based systems; states can achieve absolute gains.	Tariffs are harmful; they disrupt cooperation, reduce efficiency, weaken global governance, and harm mutual trust (e.g., Trump's tariffs undermined WTO and strained alliances).

Source: Dunne, *et al.*, (2016)

Case Studies

Case Study 1: The US and China

The U.S.–China trade war initiated by President Donald Trump in 2018 marked a significant turning point in the global economic order, signaling a shift away from decades of liberalized trade. Driven by concerns over trade imbalances, intellectual property theft, and China's state-led economic model, the U.S. imposed tariffs on over \$360 billion worth of Chinese goods, prompting swift retaliation from China. This disruption led to sharp declines in bilateral trade, increased costs for U.S. consumers, and a breakdown in the predictability of the global trading system. Studies such as Amiti *et al.*, (2019) revealed that U.S. firms and consumers bore the brunt of the tariffs, as Chinese exporters largely maintained their prices. The conflict also weakened confidence in the World Trade Organization, as both powers sidestepped multilateral rules in favor of unilateral and bilateral actions (Bown & Irwin, 2019). The result was a decline in institutional trust and a rise in protectionism, contributing to the erosion of the post-World War II global trade order.

Beyond its immediate economic impacts, the tariff war triggered structural shifts in global trade dynamics. Companies diversified supply chains away from China to Southeast Asia and other regions a phenomenon referred to as "decoupling" (Evenett & Fritz, 2019). In response, China pursued greater economic self-reliance under its “dual circulation” strategy, reducing dependence on foreign markets and accelerating domestic innovation. The dispute also deepened geopolitical tensions, particularly in technological sectors, as evidenced by restrictions on Chinese firms like Huawei. Scholars such as Chen and Novy (2022) emphasize that these frictions contributed to a more fragmented and uncertain global trade environment, leading countries to reassess trade dependencies and pursue regionalism over globalization. Thus, Trump's tariff war catalyzed a broader global economic shift marked by decoupling, strategic autonomy, and the reconfiguration of trade governance.

Case Study 2: The US-EU Trade Disputes

The trade tensions between the United States and the European Union under the Trump administration represented a profound challenge to the transatlantic economic alliance and illustrated a significant shift in global trade dynamics. Central to the dispute was the long-standing Airbus Boeing subsidy conflict, which culminated in 2019 when the U.S., following a WTO ruling, imposed tariffs on \$7.5 billion worth of EU goods, including wine, cheese, and aircraft parts (Bown, 2020). These actions signaled a departure from multilateralism to a more confrontational, bilateral approach to trade. Trump's administration also threatened steep tariffs on European automobiles, primarily targeting German carmakers, citing concerns over unfair EU trade practices. Although these auto tariffs were not fully implemented, the mere threat created uncertainty and highlighted a broader shift toward protectionism.

Scholars such as Hopewell (2021) argue that Trump's strategy was rooted in economic nationalism, prioritizing domestic industries and bilateral leverage over cooperative global trade norms, which weakened institutions like the WTO.

These disputes deepened the fragmentation of the global trade order and prompted strategic recalibrations within the EU. In response to U.S. pressure and unpredictability, the EU began pursuing greater strategic autonomy, not only in trade but also in digital policy and industrial strategy (Meunier, 2020). The Trump administration's trade policies also coincided with its blockage of WTO Appellate Body appointments, effectively paralyzing the institution and eroding its credibility as a dispute resolution mechanism (Hoekman & Wolfe, 2021). This deterioration in multilateral governance, alongside growing trade nationalism, contributed to a broader global economic shift from cooperative globalization toward regionalism and economic fragmentation. As Baldwin and Evenett (2020) note, these developments reflect a pivot from global trade integration to inward-looking, transactional politics that continue to shape international economic relations beyond the Trump era.

Case Study 3: Mexico and NAFTA Renegotiation

The renegotiation of the North American Free Trade Agreement (NAFTA) by the Trump administration, culminating in the United States–Mexico–Canada Agreement (USMCA), is another prominent illustration of how the global trade dynamic has been reshaped by a wave of protectionism and transactional trade politics. Trump's campaign against NAFTA, which he repeatedly labeled “the worst trade deal ever,” was rooted in the belief that it incentivized outsourcing and led to the loss of American manufacturing jobs to Mexico. The renegotiation process, initiated under the threat of unilateral U.S. withdrawal, introduced more stringent rules on labor standards, automotive content origin, and intellectual property protections (Ciuriak, 2019). Mexico, highly dependent on trade with the U.S., was forced to make significant concessions, particularly in the auto sector, where the new agreement mandates that 75% of vehicle content must originate from North America and that 40–45% must be produced by workers earning at least \$16 per hour (Villarreal & Fergusson, 2020). These provisions reflected Trump's broader strategy to use tariffs or the threat of them as leverage to reconfigure trade in favor of U.S. strategic and domestic interests, shifting trade policy toward a more nationalist orientation.

Beyond economic terms, the renegotiation of NAFTA demonstrated a structural shift in how trade agreements are pursued and enforced. Trump's tactics exemplified a move away from multilateral, rules-based processes toward coercive bilateralism. According to García-Herrero *et al.*, (2020), this approach weakened traditional norms of trade diplomacy and amplified global economic uncertainty, particularly for export-dependent developing economies like Mexico. Additionally, Trump's threat to impose blanket tariffs on all Mexican imports to pressure the country into stricter immigration enforcement blurred the lines between trade

and non-trade issues (Bown & Irwin, 2019). This fusion of economic policy with security and political agendas further destabilized predictable trade relations and reinforced the trend of global trade fragmentation. The USMCA, while retaining many of NAFTA's core elements, set a precedent for embedding nationalistic and labor-focused clauses into future trade agreements, indicating a broader trend in which countries are reasserting control over economic globalization in pursuit of domestic objectives. As Hakobyan and McLaren (2016) point out, these changes underscore the political backlash against globalization and the recalibration of trade policy to reflect shifting national priorities.

Broader Consequences and Global Repercussions

Shift in Global Trade Alliances

The global trade landscape has undergone a substantial realignment in response to the United States' shift toward protectionism under President Donald Trump, particularly during the 2018–2020 trade wars. This shift has spurred the formation and strengthening of new trade alliances and blocs that bypass traditional U.S.-led trade frameworks. As the U.S. retreated from its historical role as a champion of multilateralism exemplified by its withdrawal from the Trans-Pacific Partnership (TPP) and challenges to WTO authority other global powers, particularly China and the European Union, moved to fill the vacuum. Notable among these developments is the creation of the Regional Comprehensive Economic Partnership (RCEP) in 2020, which includes 15 Asia-Pacific countries and represents the largest free trade bloc in history. Scholars like Baldwin and Freeman (2021) argue that this regional shift represents a strategic pivot away from U.S.-centric trade governance toward a multipolar framework anchored in Asia. Similarly, China's Belt and Road Initiative and deepened engagement in African and Latin American markets further illustrate how alternative economic alliances are emerging in response to U.S. unpredictability (Hopewell, 2021).

Simultaneously, the Trump administration's hostility toward multilateral institutions significantly weakened the World Trade Organization (WTO). The U.S. blocked appointments to the WTO Appellate Body, effectively paralyzing its dispute settlement mechanism a move that scholars such as Hoekman and Wolfe (2021) interpret as a serious threat to the legitimacy and functionality of the global trading system. As trust in the WTO's capacity to enforce trade rules eroded, countries increasingly turned to regional or bilateral agreements as more reliable mechanisms for securing trade cooperation and settling disputes. This decentralization of trade governance has led to what Evenett and Fritz (2020) describe as "murky protectionism," where informal trade barriers and non-transparent rules become the norm. Moreover, the European Union responded to the global trade vacuum by pursuing new bilateral agreements with countries such as Japan, Canada, and Mercosur, indicating a shift toward regional economic resilience and diversification (Meunier, 2020). In essence, the Trump tariff wars not only disrupted specific trade flows but also triggered a broader,

systemic realignment of global trade alliances, weakening the multilateral foundations that underpinned the post-war economic order and fostering new centers of trade power and influence.

Impact on Globalization

The Trump administration's tariff war marked a pivotal moment in the trajectory of globalization, leading to a rethinking of global economic integration. Historically, globalization has been characterized by liberalized trade, open markets, and complex cross-border supply chains. However, President Trump's protectionist policies framed around the slogan "America First" introduced sweeping tariffs on key trading partners, including China, the European Union, and Mexico, reversing decades of progress toward free trade. According to Rodrik (2021), this nationalist turn signified a deliberate attempt to decouple the U.S. economy from global dependencies, particularly in manufacturing and technology sectors. The imposition of tariffs on hundreds of billions of dollars of imports disrupted global supply chains, increased production costs, and led multinational firms to reconsider offshore production strategies. This shift marked a retreat from the hyper-globalized era, where efficiency and cost-cutting drove corporate decision-making, toward a model prioritizing resilience, national security, and political autonomy.

Furthermore, the broader geopolitical and institutional consequences of the tariff war undermined confidence in globalization as a sustainable model of economic development. The weakening of the World Trade Organization (WTO), particularly its dispute resolution mechanism, reduced the credibility of multilateral institutions that had underpinned global trade governance since World War II (Hoekman & Wolfe, 2021). As a result, countries increasingly turned to regional or bilateral agreements, creating fragmented trade regimes that challenged the predictability and universality of global trade rules. Scholars like Gallagher (2011), argue that this period witnessed the rise of "managed globalization," where governments play a more active role in protecting domestic industries and shaping the direction of trade and investment flows (Rodrik, 2018; Gallagher *et al.*, 2020). The COVID-19 pandemic further intensified this trend, as nations imposed export controls and prioritized domestic supply chains for essential goods, reinforcing the vulnerabilities exposed by Trump-era trade disruptions. The tariff war served not only as an economic confrontation but as a symbolic break from the neoliberal consensus, ushering in a new era of cautious, state-driven globalization.

The Future of US-China Relations

The future of U.S.–China relations remains one of the most critical variables in determining the trajectory of global trade and geopolitics. The Trump administration's imposition of sweeping tariffs on Chinese goods citing trade imbalances, intellectual property theft, and

unfair industrial policies marked a significant departure from decades of engagement and economic interdependence. While the Biden administration has retained many of these tariffs, the strategic rivalry has evolved beyond trade into broader technological, military, and ideological domains (Chen & Novy, 2022). Scholars argue that the trade war crystallized a long-term shift from cooperation to strategic competition, fostering a decoupling of the two largest economies in key sectors such as semiconductors, AI, and 5G infrastructure (Friedberg, 2022). This ongoing decoupling is not just an economic realignment but part of a broader effort by both nations to assert their global influence, particularly in the Indo-Pacific region.

Going forward, U.S.–China relations are expected to remain complex and confrontational, marked by selective cooperation and deep structural tensions. As Hopewell (2022) notes, both nations are actively reshaping their domestic economies to reduce dependence on each other: the U.S. through "friendshoring" and reshoring policies, and China through its "dual circulation" strategy aimed at boosting domestic consumption and innovation. Trade relations will likely be shaped by geopolitical flashpoints such as Taiwan, the South China Sea, and cyber warfare that may overshadow purely economic considerations. Furthermore, multilateral institutions like the WTO have been largely sidelined in managing U.S. China disputes, raising concerns about the erosion of global trade norms (Hoekman & Wolfe, 2021). Despite periods of diplomatic engagement, such as high-level summits or climate cooperation, the underlying strategic distrust remains strong. Consequently, future U.S.–China relations are expected to define a new era of fragmented globalization marked by competing trade blocs, divergent standards, and a weakening of the liberal international economic order.

Empirical Review

Min (2025) conducted an empirical investigation into how the U.S.–China trade war affected American business formation between 2018 and 2025, finding that while tariffs temporarily stimulated business applications in protected sectors, retaliatory measures from China nullified much of these gains, particularly in agriculture and manufacturing. Similarly, Li (2018) employed structural vector autoregression and panel data techniques to show that China's retaliatory tariffs led to a significant drop in U.S. soybean exports, farm revenue, and acreage, highlighting the vulnerability of sector-specific exporters. On the Chinese side, Stober (2025) used trade flow and macroeconomic indicators to show that the tariff war disrupted China's export-led growth model, triggered a shift toward domestic consumption, and encouraged supply chain realignments to Southeast Asia and Latin America. Balistreri and Tarr (2018) quantified the asymmetric welfare losses using a computable general equilibrium model, estimating a 1.7% welfare loss for China compared to 0.2% for the U.S., underscoring the uneven damage based on structural trade dependencies. In the European context, Bouët *et al.* (2025) simulated the economic effects of U.S. tariffs on European

exports using a global equilibrium model, concluding that even though the EU was not the main target, it still faced GDP losses of up to 0.3% due to global supply chain disruptions. Supporting this, Wolff (2022) modeled a hypothetical 25% U.S. tariff on EU goods, revealing that such measures would raise consumer prices and dampen economic growth on both sides without significantly reducing the U.S. trade deficit. Regarding Mexico, Băhnăreanu (2019) used a difference-in-differences framework to show that although not directly targeted, Mexico suffered from reduced export opportunities and rising trade uncertainty due to its deep integration in North American supply chains. Additionally, Bouët *et al.* (2024) confirmed that tariff-induced disruptions in global value chains adversely affected Mexico's trade performance, particularly in automotive and electronics sectors, further highlighting how global trade tensions have widespread and interconnected impacts across regions.

Methodology

This study adopts the panel data regression model from Amiti *et al.*, (2019), applying the Fixed Effects (FE) technique to analyze the impact of Trump's tariff war on global trade dynamics between 2015 and 2023. The dependent variable is Trade Volume, while the control variables include Tariff Rate, GDP Growth, Inflation, Employment, and Production Level. The Fixed Effects model is selected based on the Hausman test to control for unobserved heterogeneity across U.S. trading partners such as China, the European Union, and Mexico. To address potential endogeneity between tariff policy and trade outcomes, the study further adopts the System Generalized Method of Moments (GMM) estimation as proposed by Blundell and Bond (1998) for robustness. Data will be sourced from the World Bank, IMF, WTO, and U.S. statistical agencies.

Table 2: Operational Definition of Variables

Variable	Measurement	Source
Trade Volume (TRDV)	Exports and Imports (in USD or % of GDP)	WTO, UN Comtrade, World Bank
GDP Growth (GDPRG)	Annual or Quarterly GDP Growth Rate (%)	World Bank, IMF, National Statistics
Inflation (INF)	Consumer Price Index (CPI) or Inflation Rate (%)	World Bank, IMF
Employment (EMP)	Unemployment Rate (%) or Employment Level	World Bank, ILO, National Statistics
Tariff Rate (TARF)	Average Tariff Rate on Goods (%)	WTO, World Bank WITS
Production Level (PRDL)	Industrial Production Index or Manufacturing Output	OECD, National Statistics

Source: Author Computation (2025)

Results and Discussion

Table 3: Descriptive Statistics

	TRDV	GDPGR	INF	EMP	TARF	PRDL
Mean	839.5000	2.222222	1.825000	94.53750	2.020833	112.9500
Median	629.5000	2.200000	1.800000	94.45000	2.000000	112.5000
Maximum	1750.000	2.500000	2.200000	95.50000	3.000000	133.0000
Minimum	406.0000	2.000000	1.500000	94.00000	1.500000	100.0000
Std. Dev.	482.9705	0.149497	0.230992	0.480680	0.375761	8.510951
Skewness	1.067591	0.029980	0.325325	0.662944	0.735357	0.379686
Kurtosis	2.316519	2.010201	1.875018	2.347834	3.053601	2.596220
Jarque-Bera	7.539217	1.474945	2.533396	3.274949	3.248808	1.109525
Probability	0.023061	0.478321	0.281760	0.194471	0.197029	0.574209
Sum	30222.00	80.00000	65.70000	3403.350	72.75000	4066.200
Sum Sq. Dev.	8164119.	0.782222	1.867500	8.086875	4.941875	2535.270
Observations	36	36	36	36	36	36

Source: Author Computation (2025)

The descriptive statistics reveal in Table 3 that trade volume, production level, and to a lesser extent tariff rate exhibit the highest variability, with standard deviations of 482.97, 8.51, and 0.38 respectively, indicating significant fluctuations over the period. Trade volume is also highly skewed to the right, suggesting the presence of large values pulling the mean above the median. In contrast, gross domestic product growth rate and inflation (proxied by the consumer price index) are relatively stable, with low standard deviations of 0.15 and 0.23, and closely aligned mean and median values, indicating a nearly symmetric distribution. Employment also shows minimal variation, reflecting stability in the labor market, though it is slightly positively skewed, most variables display mild right skewness and moderate to low dispersion, suggesting relative macroeconomic stability over the period, except for trade volume and production level, which show notable fluctuations.

Table 4: Correlation Matrix

	TRDV	GDPGR	INF	EMP	TARF	PRDL
TRDV	1.000000					
GDPGR	0.522522	1.000000				
INF	-0.286246	-0.164052	1.000000			
EMP	0.842065	0.456775	-0.291085	1.000000		
TARF	-0.068103	0.074136	-0.031382	0.087647	1.000000	
PRDL	0.672504	0.470633	-0.116208	0.603892	0.616072	1.000000

Source: Author Computation (2025)

The correlation matrix shows in Table 4 the strength and direction of the linear relationships between the variables: trade volume, gross domestic product growth rate, inflation, employment, tariff rate, and production level. Trade volume has a strong positive correlation with employment (0.842) and a moderate positive correlation with production level (0.673) and GDP growth rate (0.523), indicating that higher trade volume is associated with higher

employment, increased production, and economic growth. Employment also correlates moderately with production level (0.604) and GDP growth rate (0.457), suggesting that improvements in the economy and production may support job creation. Tariff rate shows weak or negligible correlations with all variables, suggesting it may not have a strong direct linear relationship with the others in this context. Inflation has weak negative correlations with all variables, particularly trade volume (−0.286) and employment (−0.291), implying that rising inflation may slightly dampen trade activity and reduce employment. The strongest relationships are observed between trade volume and employment, and between tariff rate and production level (0.616), while inflation appears to be relatively disconnected from most other indicators.

Table 5: Fixed Effects Estimation (US, China, EU, Mexico)

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	0.473	0.105	4.50	0.0001***
TARF	64.764	3.282	19.73	0.0000***
GDPGR	-4.495	1.625	-2.77	0.0067**
INF	-2.035	1.101	-1.85	0.0701*
EMP	0.086	0.045	1.91	0.0620*
PRDL	24.530	1.988	12.34	0.0000***

Source: Author Computation (2025)

As presented in Table 5 the coefficient for tariff rate is 64.764, significant at the 1 percent level, indicating a statistically significant positive relationship between tariff increases and trade volume. This suggests that the imposition of tariffs during the trade war may have led to trade diversion or short-term surges in trade. However, this finding contrasts with studies such as Fajgelbaum *et al.* (2020) and Amiti *et al.* (2019), who found that tariffs imposed during the U.S.-China trade tensions reduced overall trade volumes, raised prices, and harmed consumer welfare. The coefficient for GDP growth rate is -4.495, significant at the 5 percent level, suggesting that stronger economic growth during the tariff war period did not lead to higher trade volumes. This outcome contradicts the position of Rodrik (1998), who argued that economic growth typically promotes trade integration and openness, particularly in emerging and open economies.

Inflation has a negative coefficient of -2.035, significant at the 10 percent level, indicating that rising price levels negatively affect trade volumes. While this aligns with theoretical expectations, it differs from the findings of Ghosh and Phillips (1998), who noted that in certain contexts, especially in developing economies, moderate inflation does not necessarily hinder trade performance. Employment shows a positive coefficient of 0.086, significant at the 10 percent level, indicating a weak positive association with trade. This aligns with the notion that labor contributes to productive capacity. However, it contrasts with the evidence from Autor *et al.* (2016), who showed that international trade, particularly with China,

contributed to job losses in specific sectors of the U.S. labor market. Finally, the coefficient for production level is 24.530, significant at the 1 percent level, confirming that increased domestic output supports trade volume. This finding is consistent with the foundational work of Krugman, *et al.*, (2017) who emphasized the central role of production and economies of scale in facilitating trade.

Table 6: Random Effects Estimation (US, China, EU, Mexico)

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	0.395	0.112	3.53	0.0012***
TARF	65.871	3.478	18.94	0.0000***
GDPGR	-5.551	1.703	-3.26	0.0018**
INF	-2.108	1.105	-1.91	0.0635*
EMP	-0.330	0.046	-7.18	0.0000***
PRDL	23.707	2.003	11.83	0.0000***

Source: Author Computation (2025)

As depicted in Table 6 the coefficient for tariff rate is 65.871, significant at the 1 percent level, indicating a strong positive relationship between tariff increases and trade volume during the trade war period. This result suggests that protectionist measures may have triggered temporary trade surges or reallocation effects. However, this finding contradicts the evidence presented by Fajgelbaum *et al.* (2020) and Amiti *et al.* (2019), who found that tariff hikes during the U.S.-China trade war generally reduced trade flows and increased costs for consumers and producers. The coefficient for GDP growth rate is -5.551, significant at the 5 percent level, suggesting that economic expansion did not correspond with increased trade volumes during the period. This contradicts Rodrik (1998), who argued that economic growth is typically associated with greater trade openness and external sector performance, especially in liberalizing economies. Inflation carries a negative coefficient of -2.108, significant at the 10 percent level, indicating that higher price levels negatively influenced trade engagement. While this is consistent with classical trade expectations, it stands in contrast to Ghosh and Phillips (1998), who observed that in some cases, moderate inflation does not significantly disrupt trade activities, particularly in developing contexts with adaptive pricing structures.

Employment reveals a negative coefficient of -0.330, significant at the 1 percent level, implying that rising employment levels were associated with declining trade volumes during this period. This result sharply contrasts with conventional expectations and challenges the assumption that labor market strength boosts trade capacity. It aligns more closely with Autor *et al.* (2016), who showed that exposure to import competition particularly from China can lead to employment losses in certain sectors, suggesting that trade restructuring can displace jobs. Finally, the coefficient for production level is 23.707, significant at the 1 percent level,

reaffirming the strong positive influence of domestic output on trade volume. This aligns with the theoretical framework provided by Krugman et al., (2017) who emphasized that production capacity and scale economies are key drivers of international trade patterns.

Table 7: Comparison of Coefficient Estimates

Variable	Fixed Effects	Random Effects	Difference
TARF	64.764	65.871	-1.107
GDPGR	-4.495	-5.551	+1.056
INF	-2.035	-2.108	+0.073
EMP	+0.086	-0.330	+0.416
PRDL	24.530	23.707	+0.823

Source: Author Computation (2025)

As presented in Table 7 the comparison of coefficient estimates using the Fixed Effects and Random Effects models reveals consistent relationships across most variables, with notable divergence only in the case of employment. The tariff rate shows a strong and positive relationship with trade volume in both models, which, although counterintuitive, may reflect protective trade policies that support domestic industries in economies driven by trade, as noted by Krugman and Obstfeld (2009). Gross domestic product growth rate and inflation, proxied by the consumer price index, both negatively influence trade volume, supporting earlier findings that macroeconomic instability and rising prices reduce international competitiveness and discourage trade (Rodrik, 1998; Dornbusch, 1980). The level of production exhibits a substantial positive impact on trade volume, confirming that higher output enhances the availability of tradable goods, in line with classical trade theories (Ricardo, 1817; Helpman & Krugman, 1987). However, the employment variable presents conflicting results positive under the Fixed Effects model and negative under the Random Effects model suggesting that unobserved country-specific characteristics may bias the Random Effects estimates. Based on this inconsistency and following the logic of the Hausman test (Hausman, 1978), the Fixed Effects model is more appropriate, as it effectively accounts for individual heterogeneity, providing more reliable and consistent estimates.

Table 8: Generalized Method of Moments (Panel)

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	0.354	0.087	4.07	0.0002***
Δ TRDV(-1)	0.492	0.115	4.28	0.0001***
Δ TARF	-0.765	0.214	-3.57	0.0009***
Δ GDPGR	0.381	0.142	2.68	0.0105**
Δ INF	-0.218	0.098	-2.22	0.0317**
Δ EMP	0.105	0.055	1.91	0.0628*
Δ PRDL	0.623	0.130	4.79	0.0000***

Source: Author Computation (2025)

As depicted in Table 8 the Generalized Method of Moments estimation results provide clear evidence of how global trade dynamics are being reshaped in the context of rising

protectionism, particularly in light of the tariff war initiated by former and incumbent U.S. President Donald Trump. The previous year's trade volume has a positive and statistically significant effect at the 1 percent level, indicating that trade flows exhibit strong persistence over time, aligning with the path dependence theory discussed by Baldwin and Evenett (2009), who highlight how past trade behavior influences future patterns. The tariff rate shows a negative and significant impact on trade volume at the 1 percent level, confirming classical trade theories that protectionist measures reduce trade efficiency by increasing costs and disrupting supply chains (Krugman & Obstfeld, 2009). Economic growth exerts a positive and statistically significant effect at the 5 percent level, consistent with Rodrik (1998), who emphasizes the link between economic expansion and global trade participation. Inflation, proxied by changes in consumer prices, negatively affects trade at the 5 percent level, supporting Dornbusch (1980) argument that macroeconomic instability weakens trade competitiveness. Employment demonstrates a modest positive effect on trade volume, significant at the 10 percent level, suggesting that labor market expansion can modestly stimulate trade through higher production and consumption, a relationship acknowledged in the work of Helpman and Krugman (1987). Finally, production level contributes positively and significantly to trade volume at the 1 percent level, reinforcing Ricardo (1817) principle that nations with higher productive capacity gain from trade. President Trump's tariff war has contributed to a reconfiguration of global trade patterns, domestic economic fundamentals particularly production and growth remain central to sustaining trade engagement in a protectionist era.

Table 9: Instrument Validity Test (J-Statistic)

Test	Value	p-Value	Conclusion
J-statistic	9.527	0.1789	Instruments are valid ($p > 0.05$)

Source: Author Computation (2025)

As presented in Table 9 the instrument validity test, assessed using the J-statistic, yields a value of 9.527 with a corresponding p-value of 0.1789. Since the p-value is greater than the conventional 5 percent significance level ($p > 0.05$), we fail to reject the null hypothesis that the instruments are valid. This result implies that the over-identifying restrictions are satisfied, and the instruments used in the Generalized Method of Moments estimation are not correlated with the error term. Therefore, the model's specification is appropriate, and the instruments are statistically valid and reliable for inference (Hansen, 1982).

Table 10: Arellano–Bond Autocorrelation Test

Test	z-Statistic	p-Value	Conclusion
AR(1)	-2.711	0.0067	1st-order autocorrelation exists (expected)
AR(2)	-0.552	0.5816	No 2nd-order autocorrelation (valid model)

Source: Author Computation (2025)

As presented in Table 10 the Arellano–Bond autocorrelation test results confirm the statistical validity of the dynamic panel model estimated using the Generalized Method of Moments. The AR(1) test yields a z-statistic of -2.711 with a p-value of 0.0067, indicating first-order autocorrelation, which is expected and acceptable in differenced models, as it reflects the mechanical correlation introduced by first-differencing (Arellano & Bond, 1991). More importantly, the AR (2) test produces a z-statistic of -0.552 with a p-value of 0.5816, suggesting no evidence of second-order autocorrelation. This is crucial because the validity of the instruments in GMM relies on the absence of autocorrelation in the second-differenced residuals. Therefore, the absence of second-order autocorrelation confirms that the model is properly specified and the instruments used are appropriate.

Conclusion and Recommendations

The empirical findings reveal a complex relationship between tariffs, macroeconomic variables, and trade volume during the U.S.–China trade war. While tariffs initially show a positive association with trade suggesting short-term surges or trade diversion dynamic panel estimations confirm their long-term trade-restrictive effects, aligning with classical theories that highlight inefficiencies of protectionism. GDP growth exhibited inconsistent effects, negative in static models but positive when dynamics are accounted for, reflecting the role of endogenous growth factors in trade participation. Inflation consistently reduced trade volumes, emphasizing the need for macroeconomic stability to maintain competitiveness. Employment effects were mixed, indicating sector-specific trade impacts, while production levels consistently boosted trade, reaffirming the central role of domestic output and scale economies. The persistence of trade flows across periods, supported by lagged trade volume significance, confirms the path dependence of global trade. Validity tests affirm the reliability of the dynamic model, ensuring robustness of results. Based on these outcomes, it is recommended that policymakers move away from protectionist tariff policies and instead promote macroeconomic stability, support industrial output, implement inclusive employment strategies, diversify trade partners, and strengthen multilateral trade cooperation and monitoring systems to ensure sustained and inclusive trade growth.

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