

Policy Analysis Focus 25-4
Macroeconomic Policy Implication of US Tariff Hikes¹

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I. Introduction

There is rising concern that the recent series of United States (US) tariff hikes would adversely affect the world economy including the US economy. Future economic development would be uncertain, heightening the anxiety of economic agents worldwide. Each economy would consider its management of macroeconomic policy including fiscal and monetary policies in response to US tariff hikes alongside trade policy including retaliation. The US would utilize increasing tariff revenues from additional tariffs. US monetary and foreign exchange policies as well as fiscal policy would be watched vis-à-vis business downturn despite possible inflation.

This article quantitatively investigates the macroeconomic policy implications of US tariff hikes based on simulation studies using a computable general equilibrium (CGE) model of global trade.²

II. Fiscal policy

US President Trump has argued that increased tariff revenues resulting from additional tariffs would be utilized as financial resources for an economic policy package. That said, if US imports decreased due to additional tariffs, tariff revenues would not necessarily increase. The Laffer curve, a theoretical relationship between tax rate and tax

¹ This is a supplementary report to Kawasaki (2024), “Economic Impact of Further US Tariff Hikes,” GRIPS Discussion Paper 24-12, GRIPS, December 2024. The views expressed in this article are the author’s own and do not represent those of GRIPS Alliance or other organizations to which the author belongs.

² The framework of model simulations remains unchanged from that in Kawasaki (2024). The Global Trade Analysis Project (GTAP) 7 model (based on GTAP 11c Data Base) is solved using GEMPACK software referred to in Horridge, Jerie, Mustakinov & Schiffmann (2018), GEMPACK Manual, ISBN 978-1-921654-34-3, incorporating dynamic effects of capital and labor. The baseline data for GDP and population are updated to those for 2025 based on the World Economic Outlook (WEO) Database, October 2024, International Monetary Fund (IMF).

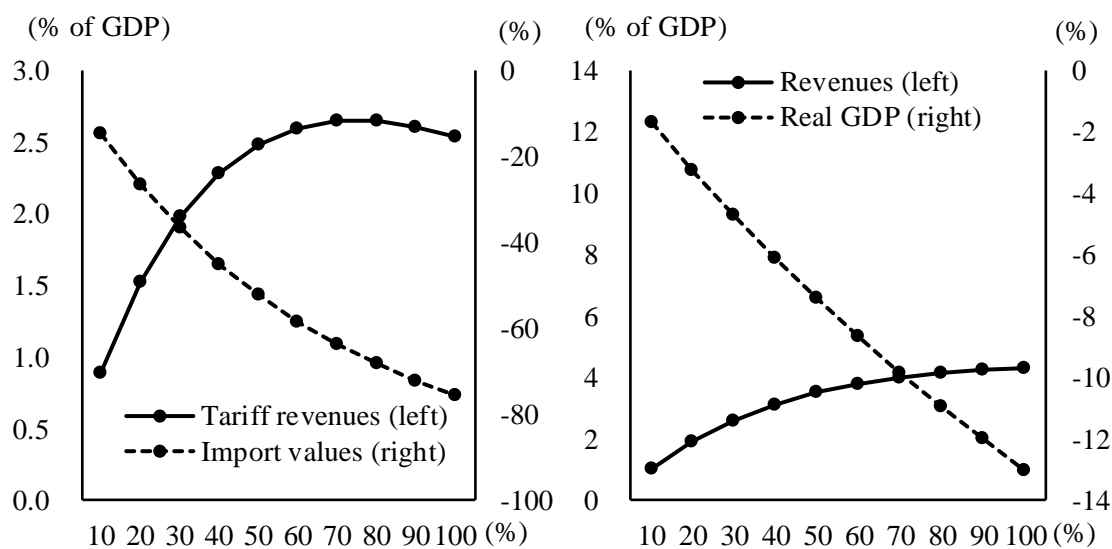
revenues, indicates that government could maximize tax revenues at an optimal tax rate.³

On April 9 the US announced the suspension of reciprocal tariffs on some economies, but uniformly imposed an additional 10% tariff on all economies worldwide. If uniform additional tariffs were raised by 10% each from the original 10%, amounting to a 100% increase, the value of US imports from the world is estimated to decrease by 75.5% as is shown in Chart 1. Tariff revenues would increase as a result of higher tariffs, as the impact of increases in tariff rates would be larger than the impact of decreases in import values until the additional tariff rate exceeded 70%. Tariff revenues would be considered to increase within the realistic range of additional tariff rates.

According to US Treasury data, in 2024 US federal government revenues amounted to 28.8 trillion US dollars (USD), accounting for around 17% of GDP,⁴ of which personal income tax occupied the largest ratio (49.3%). If tariffs were hiked, real GDP would decrease but nominal GDP would increase due to rising prices as discussed later here and total revenues are suggested to increase even in the case of tariffs higher than 70%.

That said, revenue increases are estimated to be limited to 1.0% of GDP under an additional 10% tariff and to 4.3% of GDP under an additional 100% tariff. On the other

Chart 1 Impact of tariff hikes on tariff and revenues



Source: Author's simulations.

³ Optimal tariff rate is different from this optimal tax rate: it maximizes social welfare balancing changes in debt weight losses of consumer's surplus and producer's surplus and government tariff revenues including terms of trade effects.

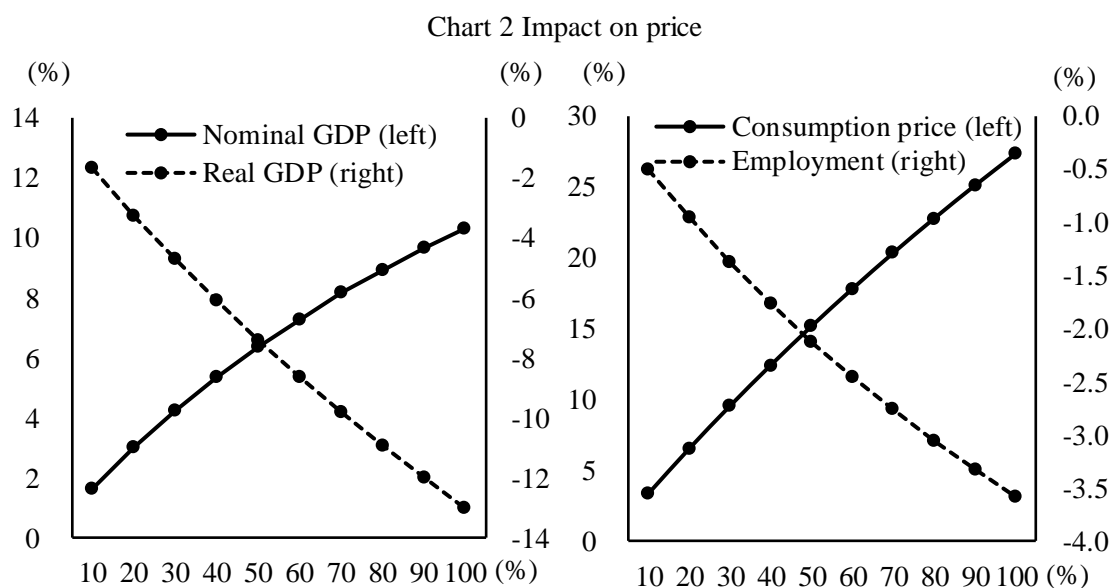
⁴ <https://fiscaldata.treasury.gov/americas-finance-guide/government-revenue/>

hand, real GDP is estimated to decrease by 1.7% under an additional 10% tariff and by 13.0% under an additional 100% tariff. It is suggested that the implementation of effective fiscal policy (employing increases in revenues as financial resources) whose multiplier effect accounts for around 1.6 to 3.0,⁵ would be required to offset the above substantial real GDP decrease.

III. Monetary policy

US tariff hikes would substantially decrease real GDP, but nominal GDP would increase by a magnitude similar to that of real GDP decrease as domestic product price rose by around twice real GDP decreases as is shown in Chart 2. It is estimated that consumption price would be increased by 3% per 10% point tariff rate increase. On the other hand, employment would decrease by 1.6% under an additional 10% tariff and by 3.0% under an additional 20% tariff alongside substantially large decreases in real GDP. There is concern that the US economy would fall into stagflation.

That said, US presidential Council of Economic Advisers (CEA) chair Miran stated in a paper⁶ released in November 2024, shortly after President Trump was elected,



Source: Author's simulations.

⁵ It is estimated in Sakamaki, T. et al (2022), “The ESRI Short-Run Macroeconometric Model of the Japanese Economy (2022version): Basic Structure, Multipliers, and Economic Policy Analyses,” ESRI Research Note No. 72, Cabinet Office, December 2022 (in Japanese) that real GDP multiplier would account for 1.04 to 1.11 by an increase in government expenditures, for 0.21 to 0.33 by personal income tax cut, and for 0.35 to 0.59 by corporate income tax cut.

⁶ Miran, S., (2024), A User’s Guide to Restructuring the Global Trading System, Hudson Bay Capital, November 2024.

that “tariffs provide revenue, and if offset by currency adjustments, present minimal inflationary ...consistent with the experience in 2018–2019.” It is pointed out that the US tariff rate on China increased by 17.9% points in 2019, but the Chinese renminbi depreciated by 13.7% against USD, and Consumer Price Index (CPI) inflation continued to move at around 2%.

The aim of the monetary policy of the Federal Reserve (Fed) System (the US central bank system) is “maximum employment, stable prices, and moderate long-term interest rates,”⁷ — different from “price stability,” which is the primary aim of the Bank of Japan (BOJ) and European Central Bank (ECB). There is concern that US jobs would be lost if the interest rate were hiked to reduce inflation.

Meanwhile, if the exchange rate appreciated due to rising interest rate, import price inflation would be mitigated but trade deficits would not improve, as decreases in imports resulting from price effects would be offset. It would be possible to stimulate the US domestic economy by securing financial resources through increased tariff revenues, but that would be dependent on the effectiveness of fiscal policy as discussed above—and would not be easy. Meanwhile, it would be difficult to overlook adverse economic impact from the perspective of other economies as international trade policy was used to distort trade so as to secure financial resources for implementation of the US domestic economic policy package.

IV. Concluding remarks

US tariff hikes would increase US revenues including tariff revenues. That said, effective fiscal policy, which could overcome substantial adverse macroeconomic impact, would be required to stimulate domestic economy. Meanwhile, if the exchange rate were appreciated by means of monetary and other policies, inflation would be mitigated but massive trade deficits would not improve. Quantitative studies using economic models will be useful for consideration of the impact of international trade policy on world economy and macroeconomic policy responses including the fiscal and monetary policies of each economy.

⁷ <https://www.federalreserve.gov/monetarypolicy.htm>