



PIIE PETERSON INSTITUTE FOR
INTERNATIONAL ECONOMICS

THE ECONOMIC EFFECTS OF NORTH AMERICAN TARIFFS

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Presented at Dallas Fed-PIIE event, “Outlook for North American trade and immigration”

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Overview

- Joint work done with Warwick McKibbin
- Presentation draws on two publications
 - A PIIIE working paper, “The international economic implications of a second Trump presidency,” and
 - A PIIIE blog post, “US tariffs on Canada and Mexico would hurt all three economies; retaliation would worsen the damage”
 - Online dashboards allow further exploration
- The basic strategy was to take Trump at his word and eschew political judgments which are not our comparative advantage
- Fundamental result: the imposition of protection will slow growth, raise prices, and not contribute to reindustrialization

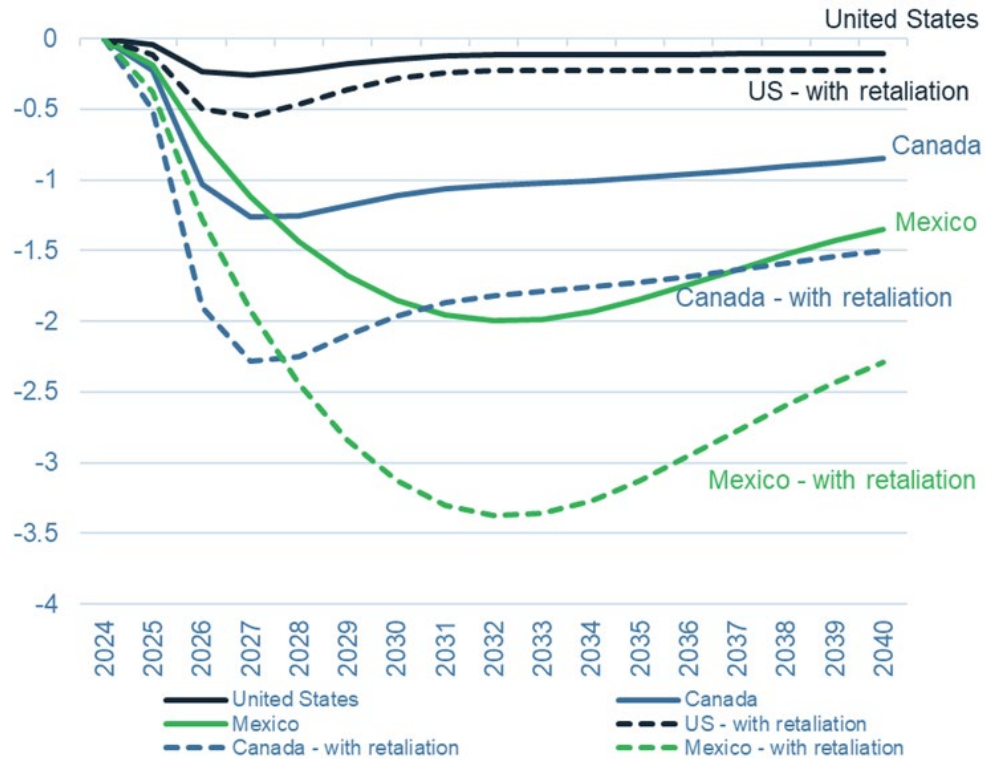
“Tariffs are the greatest thing ever invented”

- Multiple tariffs and proposed tariffs
 - Steel and aluminum tariffs; auto tariffs; perhaps special tariffs on pharmaceuticals, semiconductors, lumber et al.
 - Tariffs on Canada and Mexico—in partial abeyance
 - 10 percent global tariff, including on FTA partners (14 percent of imports) and additional so-called reciprocal tariffs on others (86 percent of imports)
 - Pre-existing tariffs, plus 20 percent, plus 34 percent “reciprocal” => 60+ percent tariff on China
 - China PNTR revocation
 - Tariff on the BRICS if reduce use of the US dollar
 - Possibility of retaliation in all cases
- Internally inconsistent rationales: protection, revenue, negotiating leverage
- We have modeled global tariffs, China actions, and tariffs against the BRICS and the EU; these do not line up precisely with 2 April announcement

The G-Cubed Model

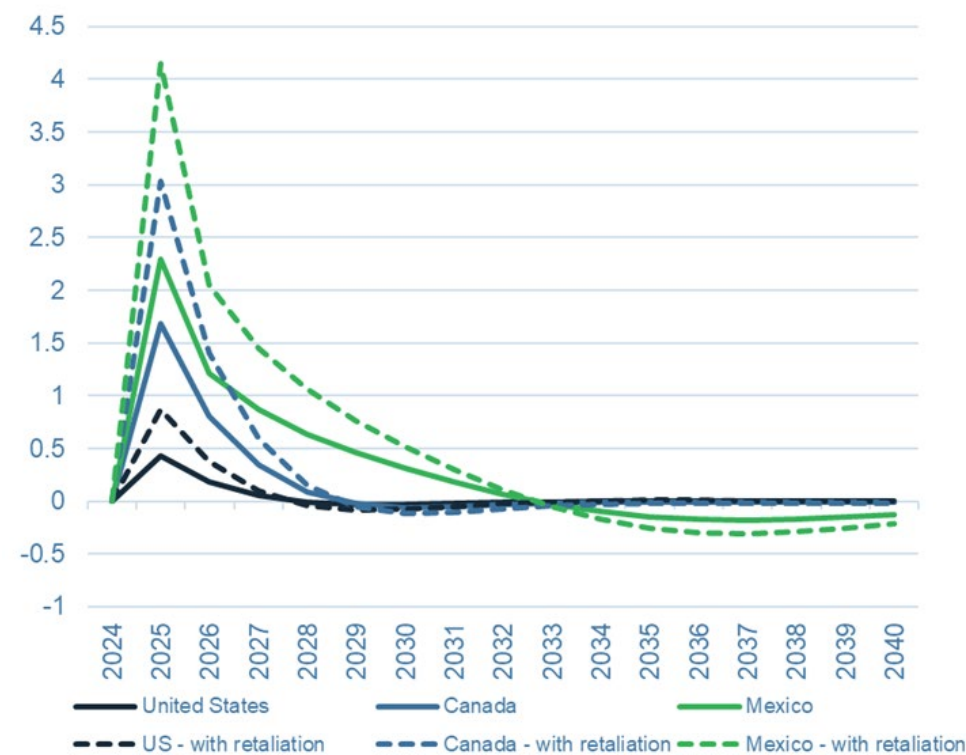
- Hybrid of a dynamic stochastic general equilibrium (DSGE) model (used by central banks) and a computable general equilibrium (CGE) model (sectoral detail).
- Models inter-industry linkages, international trade, capital flows, consumption, and investment.
- Annual macroeconomic and sectoral dynamics starting away from steady state.
- Captures frictions in labor market and capital accumulation.
 - Unemployment in the short run, full employment in the long run.
 - Physical capital is sector-specific and subject to adjustment costs.
- Labor mobile across sectors but not regions.

GDP impact of 25 percentage point tariff on Canada and Mexico

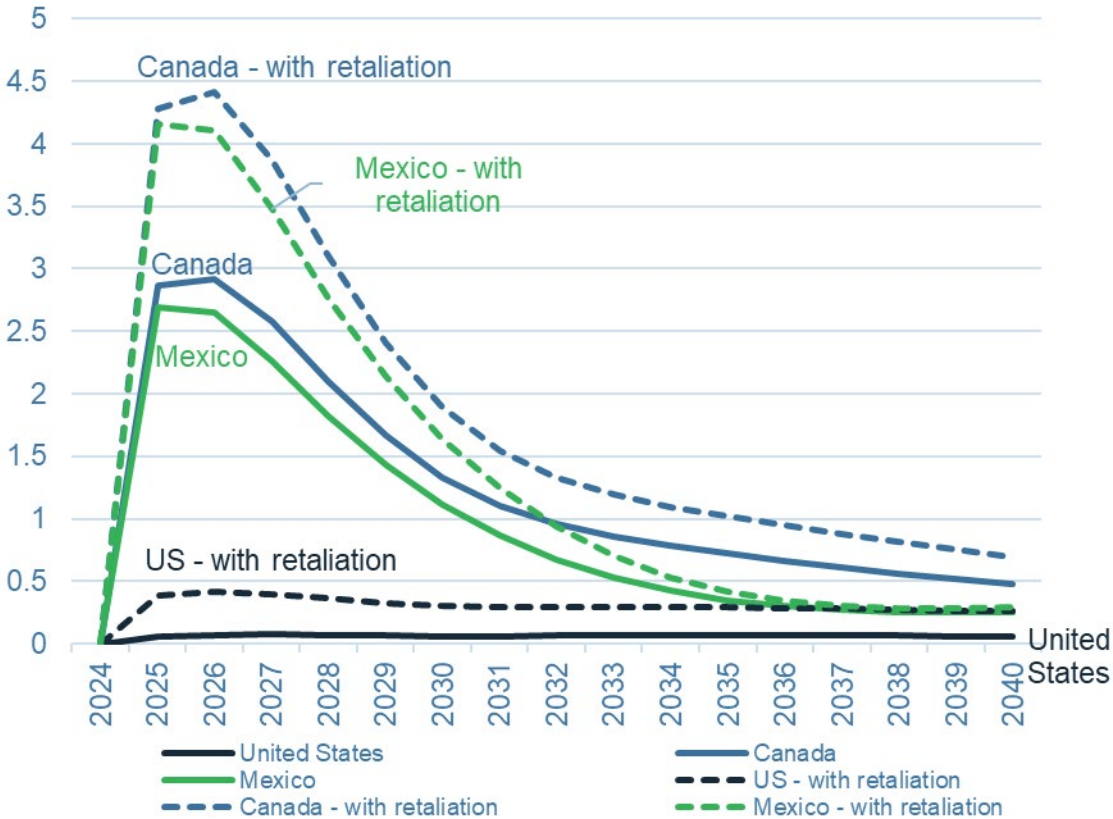


- Overstates current protection
- With and without retaliation
- GDP pushed below baseline in all three economies
- Smaller, more trade dependent economy, Mexico hurt the worst
- Mirror retaliation makes things worse
- Model may not adequately capture integrated supply chains

Inflation



Global trade balance



A detour into mass deportations

- Trump has repeatedly called for the largest mass deportation in history
 - Did not deport many people in first Administration, not deporting so many now
 - Promising new approaches, including the construction of vast new detention facilities, using active-duty military and mobilizing National Guard units, and utilizing expedited deportation procedures
- Two targets
 - Low goal: Largest previous deportation was “Operation Wetback;” 1.3 million people in 1950s
 - High goal: Estimated 8.3 million unauthorized workers in economy

Unauthorized immigrants in the US

Table 2: Shocks to US Labor supply under 1.3 million versus 8.3 million deportations

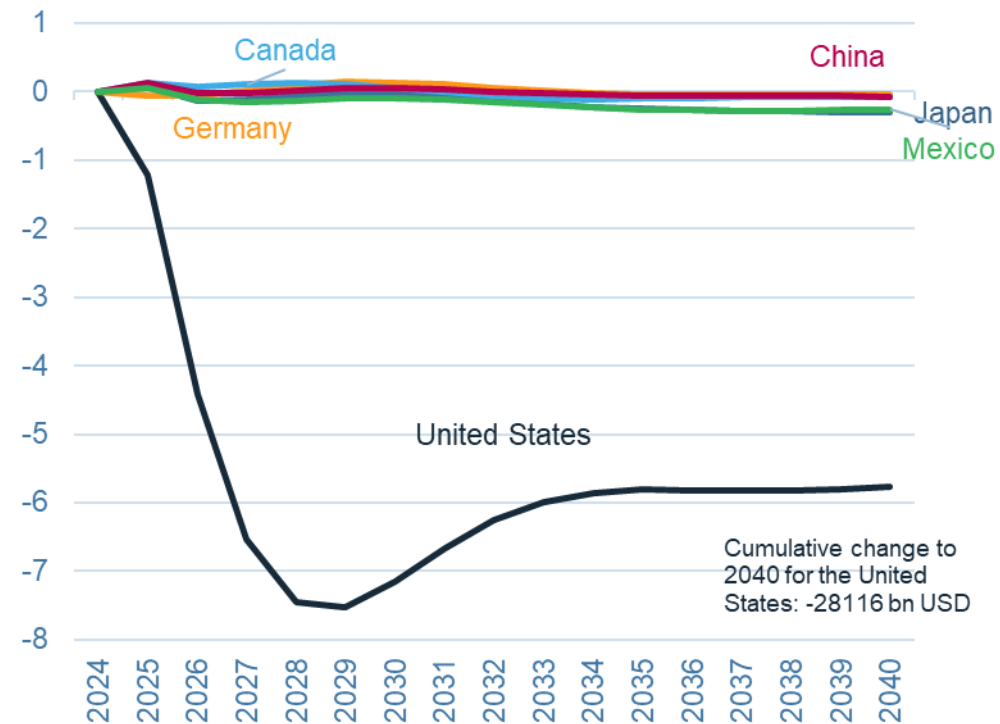
Source: Pew Research Center

G-Cubed sector	Civilian labor force (in thousands)				Share unauthorized immigrants	% change in sector labor	
	Total	US born	Legal immigrants	Unauthorized immigrants		1.3 million	8.3 million
Mining	760	670	65	25	3.3%	-0.57%	-3.65%
Agriculture	2,060	1,470	300	300	14.6%	-2.53%	-16.14%
Durable Manufacturing	8,180	6,605	1,100	463	5.7%	-0.98%	-6.27%
Non-durable Manufacturing	8,180	6,605	1,100	463	5.7%	-0.98%	-6.27%
Services	143,520	118,930	18,425	6,240	4.3%	-0.75%	-4.82%
	162,700	134,280	20,990	7,490	4.6%	-0.80%	-5.10%

US deports 1.3 versus 8.3 million workers

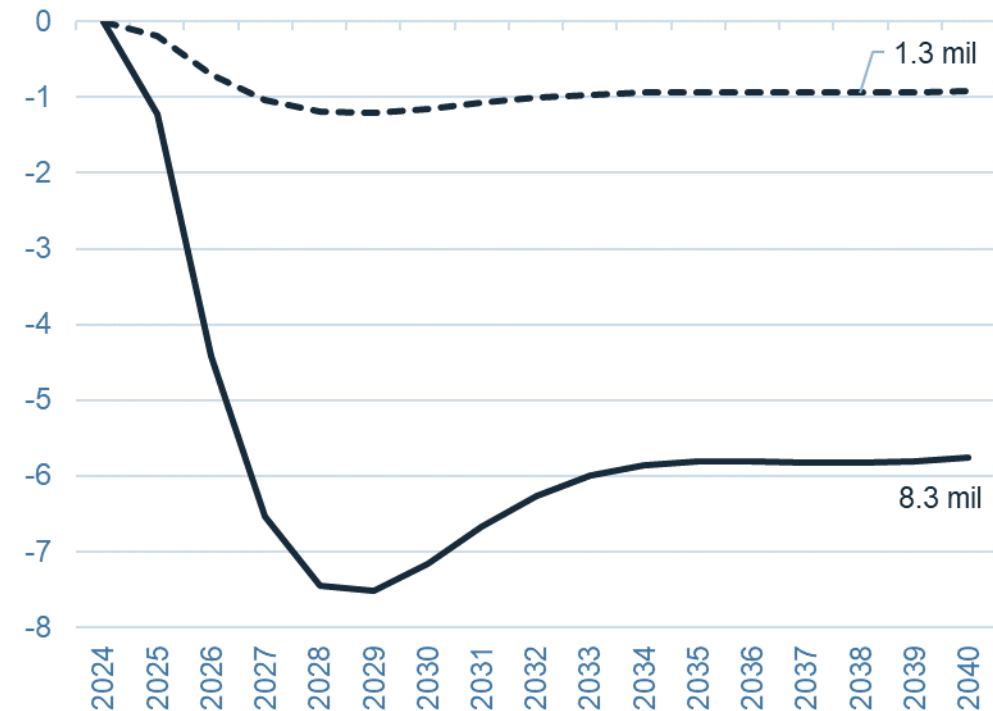
Real GDP (8.3 million)

Percentage deviation for each year



Real GDP (1.3 million vs 8.3 million)

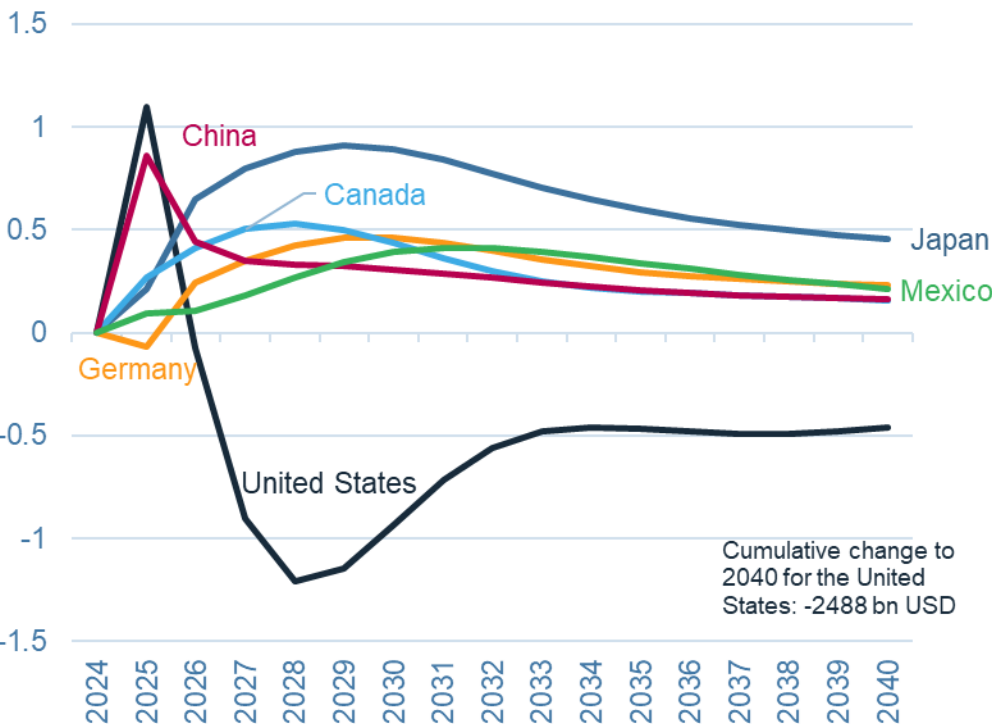
Percentage deviation for each year



A detour into erosion of Fed independence

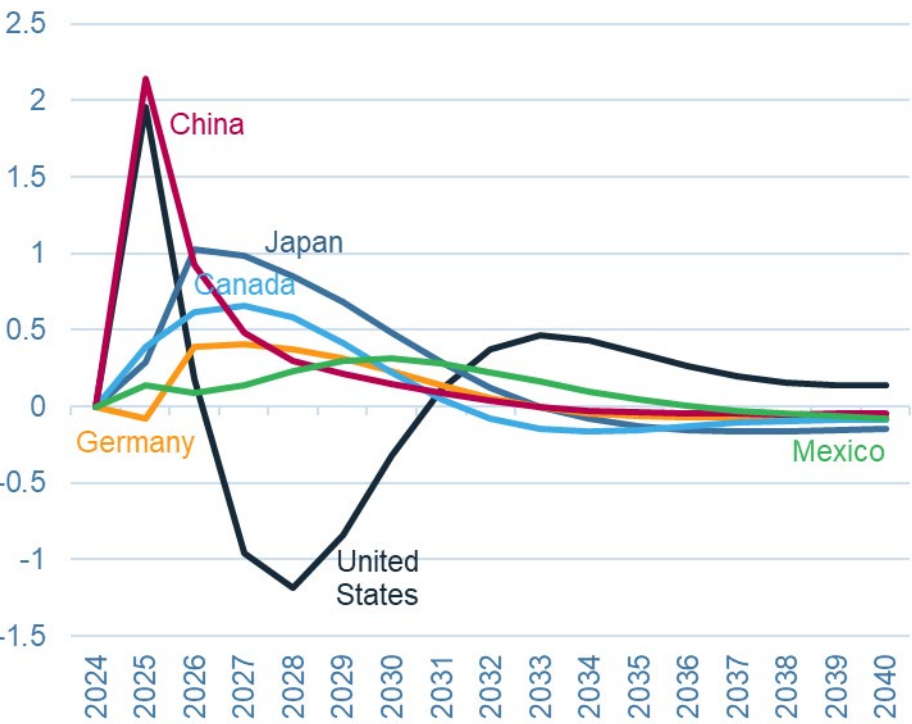
Real GDP

Percentage deviation for each year



Employment

Percentage deviation for each year



Conclusions

- The Trump program embodies considerable risk:
 - The tariff proposals all have negative downsides
 - The mass deportation proposal carries an even larger risk
 - The combination of the two could be highly disruptive and felt unevenly, hitting construction (lumber/workers), ag (supply/workers), and restaurants (supply/workers) particularly hard
 - Eroding Fed independence makes it all worse
 - The impact on Mexico is particularly pernicious
 - As is the damage to US credibility as a reliable partner
- Frankly, this is Nero without the fiddle