the budget lab

The Fiscal, Economic, and Distributional Effects of 20% Tariffs on China and 25% Tariffs on Canada and Mexico

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Key Takeaways

1. The Budget Lab modeled the total effect of the planned 25% Canada & Mexico tariffs and the 10% China tariffs, as well as the 10% China tariffs already in effect.
2. The policy is the equivalent of a 7 percentage point hike in the US effective tariff rate, raising it to the highest since 1943.
3. The price level rises by 1.0-1.2%, the equivalent of an average per household consumer loss of $1,600–2,000 in 2024$.
4. Real GDP growth is 0.6 lower in 2025. In the long-run, the US economy is persistently 0.3-0.4% smaller, the equivalent of $80-110 billion annually in 2024$.
5. The tariffs to date raise $1.4-1.5 trillion over 2026-35 conventionally-scored, and $300-360 billion less if dynamic revenue effects are taken into account.
6. Tariffs are regressive taxes. Losses for households at the bottom of the income distribution would range between $900–1,100.
7. Electronics and clothing are disproportionately affected. Motor vehicles and food see above-average price increases as well.

Introduction

The Trump Administration has announced that this week they will institute the previously-paused 25% tariffs on Canada and Mexico, as well as levy an additional 10% broad tariff on all Chinese imports. This would come on top of the 10% China tariff that went into effect February 1.

This analysis presents the fiscal and economic effects of all tariffs announced by the second Trump Administration to date, assuming the new China, Canada, and Mexico tariffs go into effect as scheduled this week. This comprised a 20% total tariff on Chinese imports (the February 1 10% plus this week's 10%) and the 25% on Canada and Mexico. The Budget Lab (TBL) modeled these tariffs under two assumptions: "limited retaliation", in which the only retaliatory tariffs are those announced by China as of February 28, and "full retaliation", where each of the three countries responds tit-for-tat with matching tariffs on each commodity. TBL's methodology largely follows prior tariff analysis.

Results

The table below summarizes TBL's fiscal and economic results.

Table 1. Summary Economic & Fiscal Effects of 20% China + 25% Mexico & Canada Tariffs

	Conventional Score****					
	2026-35		In Equilibrium			
	$billions	% of GDP	% Change in PCE Price Level*	Decline in Average Real Disposable Income per Household (2024$)**	Add'l Effective Tariff Rate (p.p.)***	Chang Q4-(GDP (I
Limited Retaliation*	**$1,480**	**0.4%**	**0.97%**	**-$1,602**	**7.0**	**-(**
Full Retaliation	**$1,365**	**0.4%**	**1.22%**	**-$2,002**	**7.2**	**-(**

** Assumes China retaliation measures announced as of February 28. ** Pre-substitution. *** Post-substitution. **** Under relaxed conventional assumptions.*

Table: The Budget Lab • Source: Congressional Budget Office, S&P Global, GTAP v7 [Corong et al (2017)], GTAP-RD, The Budget Lab analysis. • Created with Datawrapper

Aggregate price impact

Under the full suite of tariffs to date, PCE prices rise by 1% in the short-term under limited retaliation and by 1.2% under full retaliation, assuming the Federal Reserve does not respond (in either direction) to the tariffs' economic effects. This is equivalent to a consumer loss of $1,600-$2,000 per household on average in 2024 dollars. These are short-run, pre-substitution effects—before consumers make the difficult choices about how to shift spending habits—which is the best way to measure the effect on consumer welfare. Post-substitution, the effect on prices settles somewhat, to 0.7-0.9%, still a $1,100-$1,400 average consumer loss per household.

Output effects

The tariffs reduce the short- and long-run level of real GDP; this effect is more pronounced in the first two years after enactment. Real GDP growth is -0.6pp lower in calendar year 2025 and -0.1pp lower in calendar year 2026. After 2026, the level of GDP begins to recover modestly as production and supply chains reoptimize. But in the long-run, US output is still -0.3% lower with limited retaliation and -0.4% with full retaliation. That's the equivalent of the US economy being permanently smaller by $80-$110 billion annually in 2024 dollars.

Figure 1. Real GDP Level Effects of 20% China + 25% Mexico & Canada Tariffs

Percentage point change against baseline

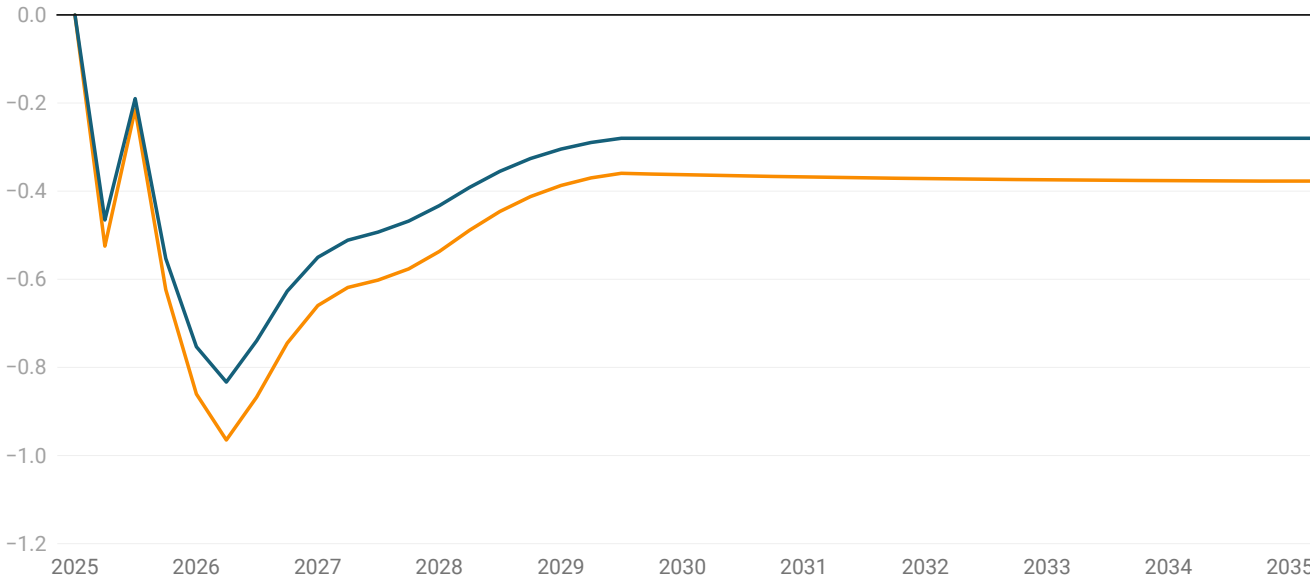


Chart: The Budget Lab • Source: S&P Global, GTAP v7, GTAP-RD, The Budget Lab analysis. • Created with Datawrapper

Fiscal impact

The tariffs are the equivalent of a rise in the effective tariff rate of 7 percentage points, bringing it to its highest level since 1943 (see chart below). Were they to remain in place, the tariffs would raise $1.4-1.5 trillion over 2026-35 conventionally-scored.[1]

Figure 2. U.S. Average Effective Tariff Rate Since 1790

Customs duty revenue as a percent of goods imports

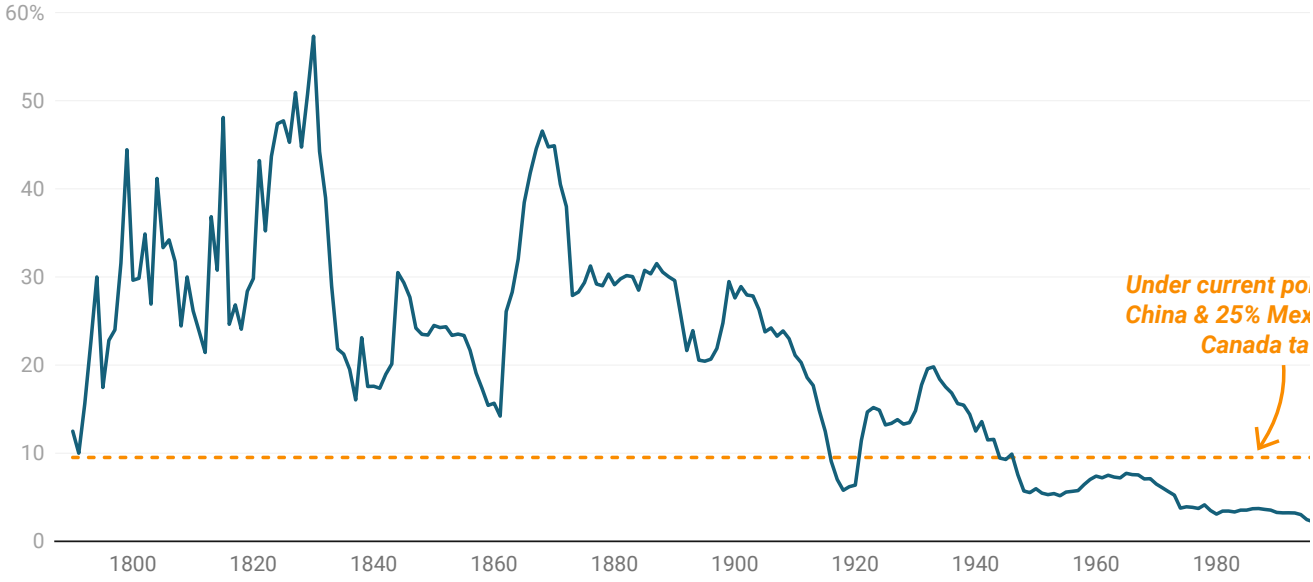


Chart: The Budget Lab • Source: Historical Statistics of the United States Ea424-434, Monthly Treasury Statement, Bureau of Economic Analysis, The Budget Lab analysis. • Created with Datawrapper

Given the negative output effects of the tariffs to date, there would be additional dynamic reductions in tax revenue as a result. Based on Congressional Budget Office rules-of-thumb, TBL estimates that these effects would range between $300 billion under limited retaliation to $360 billion with.

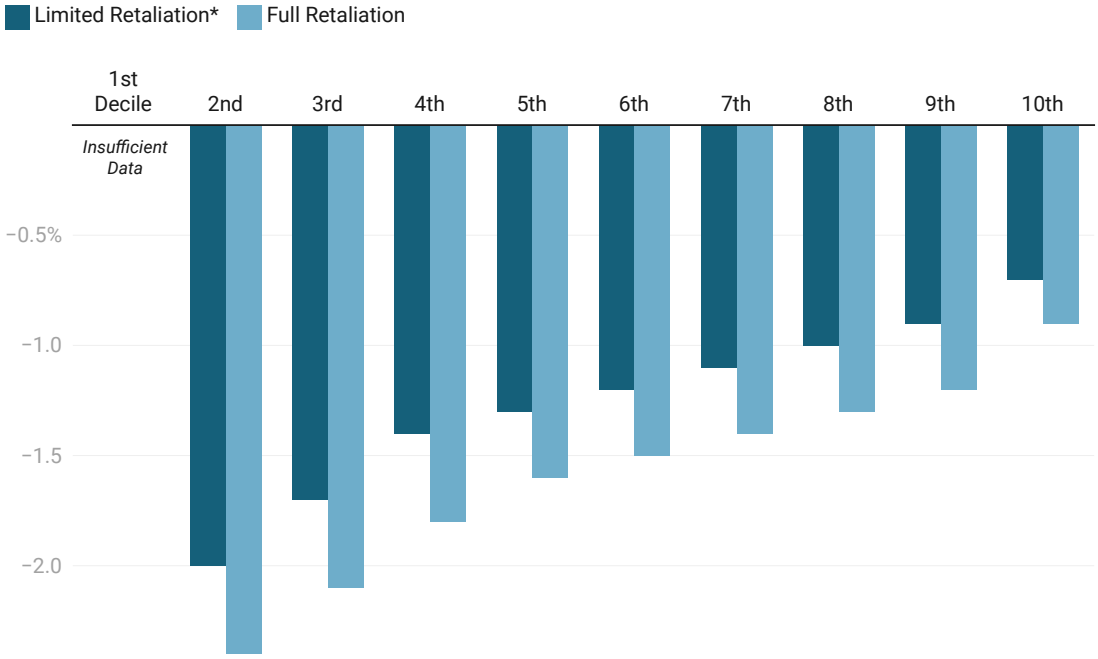
Short-run distributional impact

Tariffs are a regressive tax, especially in the short-run. This means that tariffs burden households at the bottom of the income ladder more than those at the top as a share of income. In this case, the percent change in disposable income resulting from the tariffs is almost 3x as much for households in the second decile by income as it is for households in the top decile-- -2.5% versus -0.9% in the case of tariffs with full retaliation (see top panel of chart below).

Because income rises across the distribution more steeply than the tariff burden falls, the tariff burden in dollar terms is higher at higher incomes (bottom panel). For a household in the second lowest income decile, the tariff proposal leads to consumer loss of just under $1,100 per household on average when China, Canada, and Mexico fully retaliate. For households in the middle, the burden rises to $1,800 per household on average, and for those in the top tenth, it averages $4,700 per household.

Figure 3. Short-Run Distributional Effects of 20% China & 25% Mexico & Canada Tariffs

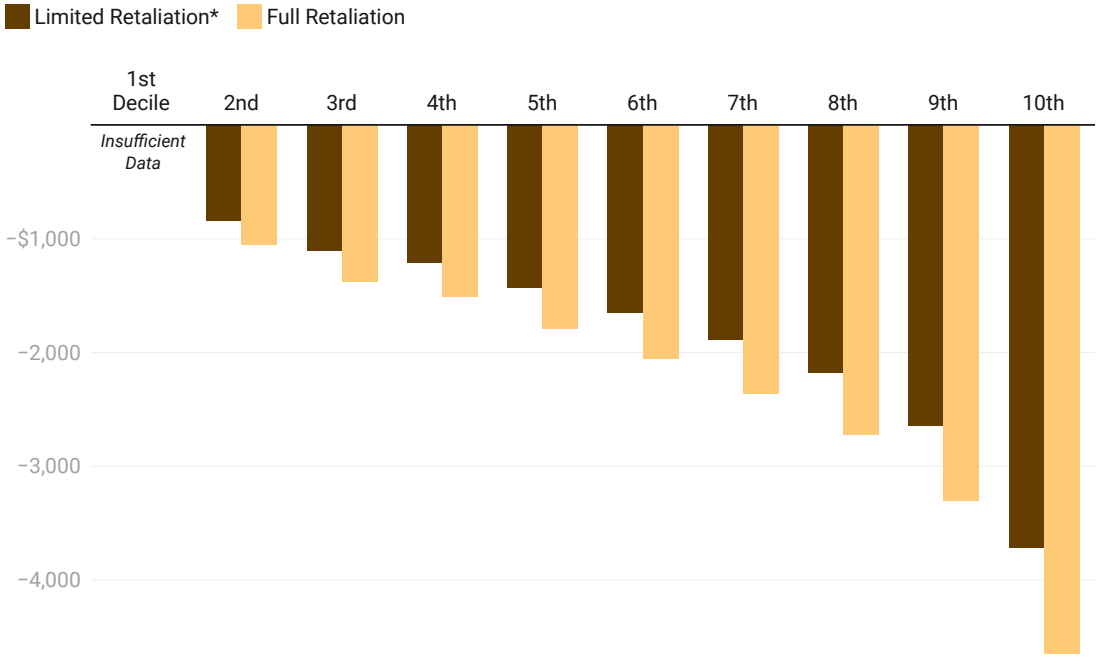
Percentage points of disposable income by household income decile



** Only includes China retaliation measures announced as of February 28.*

Chart: The Budget Lab • Source: GTAP v7, Census, BLS, BEA, The Budget Lab analysis. • Created with Datawrapper

Constant 2024$ of Average Disposable Income per Household



** Only includes China retaliation measures announced as of February 28.*

Chart: The Budget Lab • Source: GTAP v7, Census, BLS, BEA, The Budget Lab analysis. • Created with Datawrapper

Tariffs are more distributionally-ambiguous in the longer-run. Tariffs reduce both labor income and above-normal returns to capital, or rents. We assume that owners of capital hold rents rather than consume them in the short-run, but consume them over their lifecycle in the long-run. The implication is that the tariff burden is more regressive in the short-run and more evenly-distributed across households in the long-run

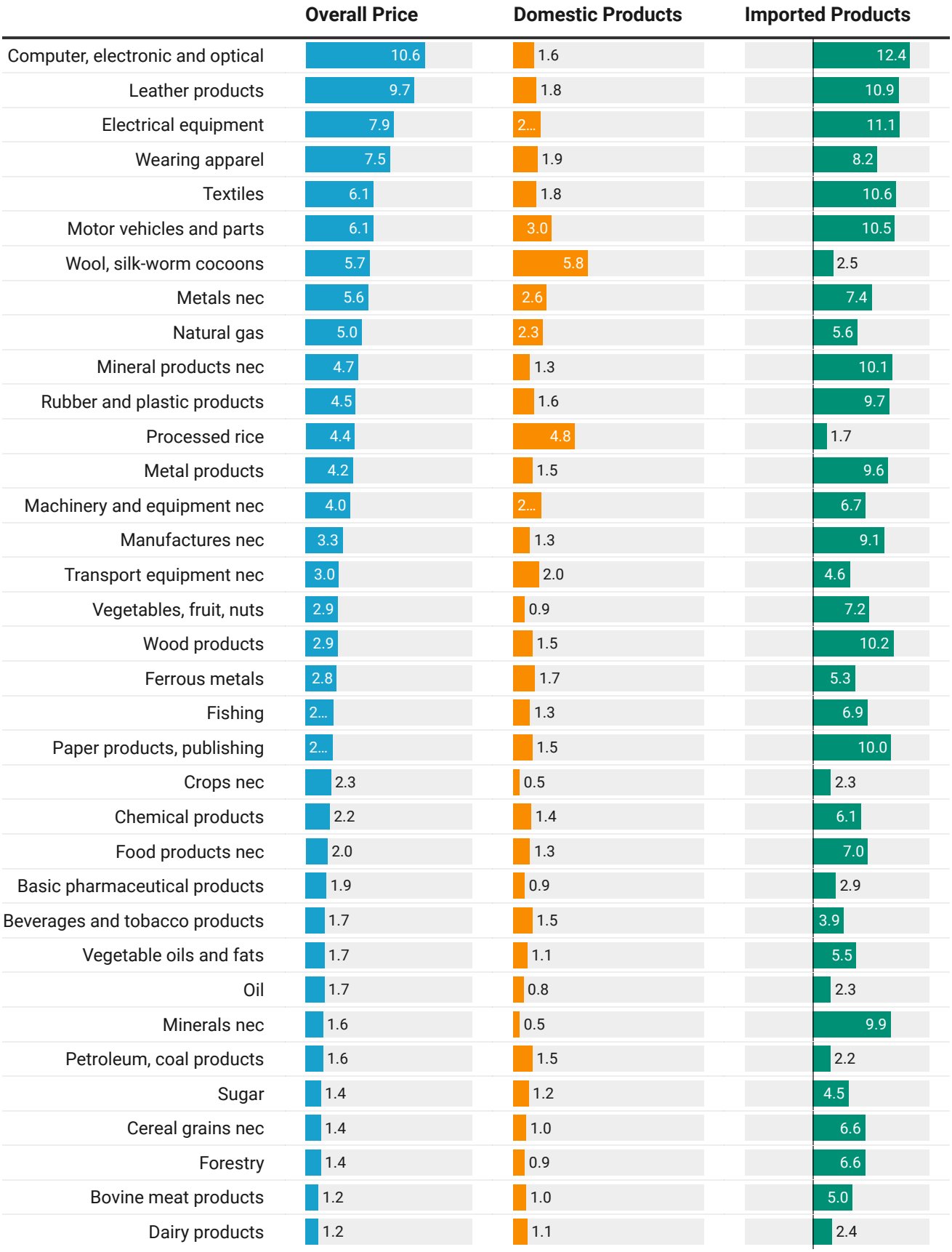
Commodity price effects

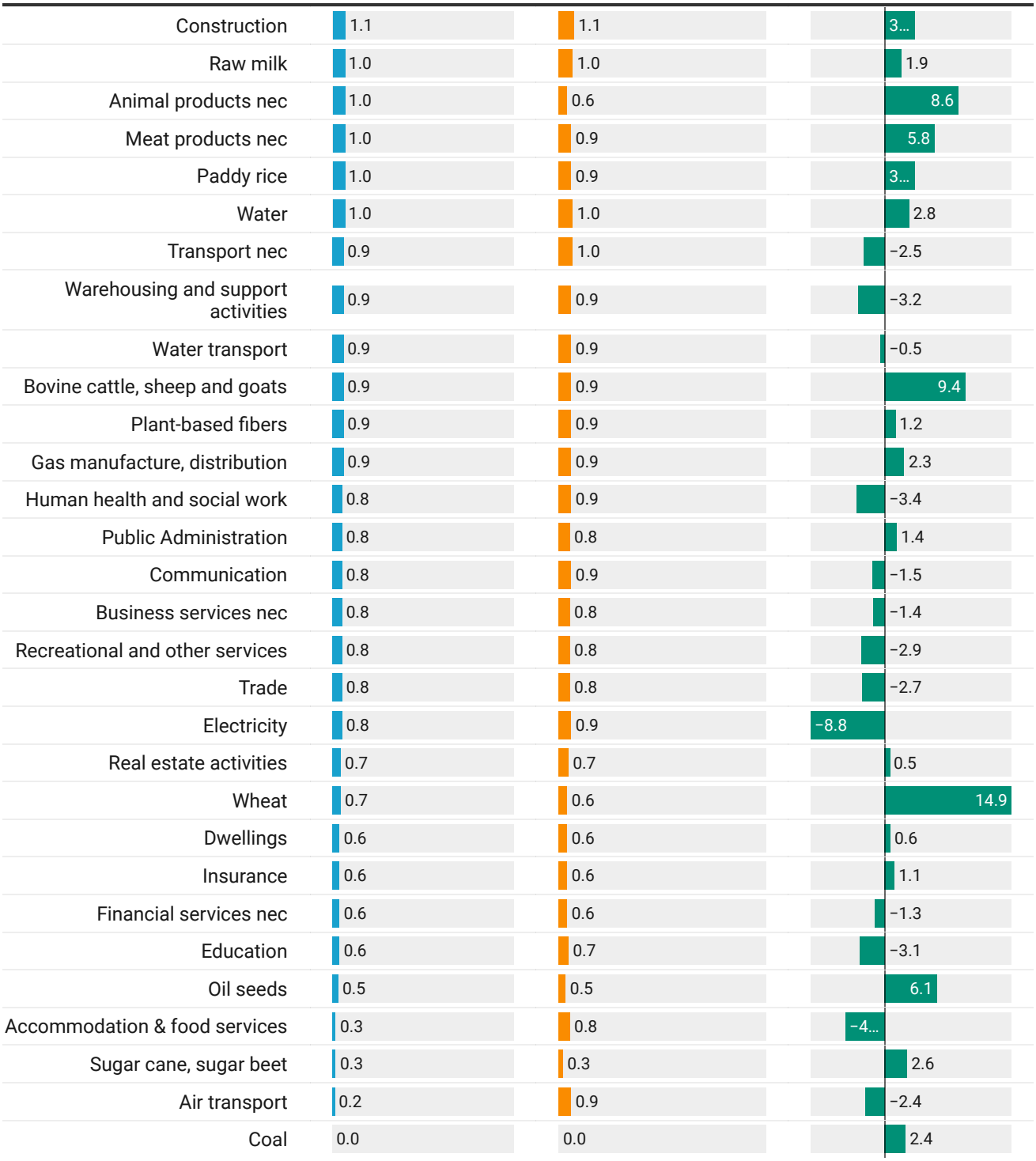
Post-substitution, the aggregate price level is 1.2% higher with full retaliation. The figure below shows how that longer-run 1.2% effect breaks down by 65 individual goods and services. A few high-level observations:

- Electronics prices rise 10% overall. Five of the top seven overall price growth categories are electronics or clothing.
- Motor vehicle prices rise 6.1%. Assuming an average selling price of $48,000 that translates to an extra $2,900, though the actual effect would depend on the exposure of different models to Canadian, Mexican, and Chinese parts & production.
- Food prices overall rise 1.7%. Fresh produce goes up 2.9%, while rice rises 4.4%.

Figure 4. Commodity Price Effects from 20% China + 25% Mexico & Canada Tariffs

Percent change to price level





"nec" = "Not elsewhere classified"

Table: The Budget Lab • Source: Source: GTAP v7 [Corong et al (2017)], The Budget Lab analysis. • Created with Datawrapper

Footnotes

1. TBL employs a "relaxed conventional" assumption for the retaliation scenario, whereby foreign income is permitted to fall but US income remains fixed.