

Macroeconomic effects of import tariffs on the euro area

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Abstract

This policy brief presents findings from the paper by [Bartocci et al. \(2025\)](#) that analyzes the macroeconomic effects of imports tariffs on the euro area with a multi-country New Keynesian model of the world economy. The main findings are the following: (i) tariffs imposed by the US reduce euro-area GDP and retaliation further amplifies that decline; (ii) trade policy uncertainty dampens investment and demand, reinforcing recessionary pressures; (iii) portfolio rebalancing from US to euro-area assets tends to offset some of the economic contraction but exerts downward pressure on inflation via exchange rate appreciation.

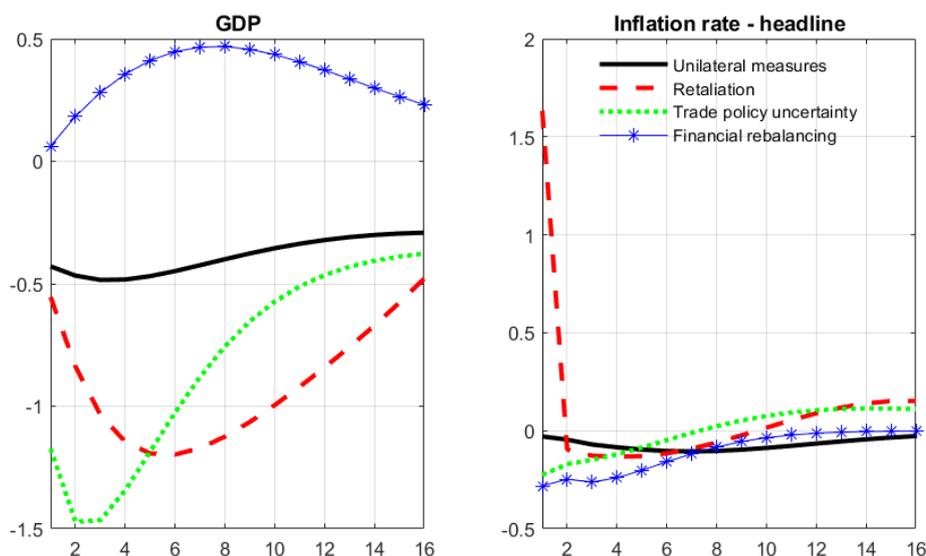
Disclaimer: This brief is based on the paper by the same authors, entitled "[The macroeconomic effects of import tariffs on the euro area: a model-based assessment](#)", published as Bank of Italy Occasional Paper No. 960, September 2025. The views expressed here are those of the authors and do not necessarily represent the views of the Bank of Italy.

The recent increase in US import tariffs – and potential retaliation by trading partners – has revived the debate on the international macroeconomic effects of tariffs. A proper assessment of the effects of US tariff policy should consider not only the *direct effects* - distinguishing unilateral measures from retaliatory responses - but also the *uncertainty effects* stemming from the sequence of announcements, suspensions and new measures, which has heightened global trade-policy uncertainty. Moreover, unlike past episodes, the rise in uncertainty has occurred alongside a progressive weakening of the US dollar vis-à-vis most currencies (*financial rebalancing effects*).

Bartocci et al. (2025) employ a four-region New Keynesian model of the global economy (including euro area, US, China, and the rest of the world) to quantify the macroeconomic effects of US tariff policy on the euro-area economy. Four scenarios are simulated, calibrated to tariff measures announced as of mid-February 2025.¹ All simulations start in 2025Q1, and tariff increases are assumed to remain in place for four years. In the *Unilateral measures* scenario, the US raises tariffs on imports of goods from the euro area, China and the rest of the world. In the *Retaliation* scenario, the three regions impose symmetric retaliatory tariffs on US goods. The *Trade-policy uncertainty* scenario evaluates the impact of the repeated announcements and suspensions of higher tariffs by the US administration. Finally, the *Financial rebalancing* scenario quantifies the effects of an international portfolio rebalancing by non-US investors that reduce their US dollars exposures, inducing a depreciation of the US dollar.²

Main results and transmission channels: euro area GDP and inflation

Figure 1.



Note: quarters on the horizontal axis; on the vertical axis: output in percent deviations, inflation rate in annualized percentage-point deviations from the baseline

According to our simulations, U.S. tariffs have significant adverse effects on euro-area economic activity: euro-area GDP falls by about 0.5% at peak in the first year of higher tariff rates (Figure 1; black line). The effect is twice as large under retaliation, reflecting a sharper decline in global demand (red dashed line). These losses are only partially offset by higher euro-area exports to China and the rest of the world, where consumers and firms substitute euro-area goods for US goods which have become more expensive due to retaliation. Euro-area inflation declines modestly in the unilateral scenario; under retaliation, it overshoots (only) in the initial period, owing to the mechanical pass-through of higher tariffs on US imports to consumer prices. Monetary policy in all regions follows a standard Taylor rule.

¹ Specifically, the paper assumes increases in tariffs on US goods imports from the euro area, the rest of the world and China, equal to 25, 9 and 45 percentage points respectively. These increases correspond to an effective US tariff rate of 16.4%, which is very close to the current one. Cfr. [Yale Budget Lab](#).

² The US dollar depreciation has been unusual by historical standards. The rebalancing of portfolio flows away from dollar assets has been identified as one important factor underlying the US dollar depreciation observed since 2025 Q1. It accelerated in the aftermath of the April 2025 tariff-related turbulence (“Liberation Day”, 2 April 2025) and came to a halt in July after the announcement of the US fiscal package (“One Big Beautiful Bill Act”, 4 July 2025). Cfr. [BIS Quarterly Review, September 2025](#).

Accordingly, in the retaliation case the ECB policy rate mildly increases to bring inflation back to target - further weighing on GDP – whereas, in the unilateral case it eases, as both output and inflation weaken.

Uncertainty associated to tariff-related news has increased sharply since 2025Q1, as reflected in the [Caldara et al. \(2020\)](#) Trade Policy Uncertainty (TPU) index, which has reached unprecedented levels. To capture the effects of this rise, we simulate an exogenous decline in private investment in physical capital, computed using the elasticity of investment expenditures to TPU shocks estimated in [Caldara et al. \(2020\)](#). Specifically, we feed the model with eight-quarter negative investment-specific shocks that hit all countries simultaneously and generate a 5% decline in private investment in each region. As a result, GDP falls by over 1% in the first year (green dotted line). Inflation is lower than in the unilateral scenario, reflecting weaker demand. These effects should be viewed as upper bounds, since firms may adapt to persistently high TPU, attenuating the impact over time.

To capture the effect of both the uncertainty on the tariff policy and the post-announcement weakening of the US dollar, we feed the model with negative risk-premium shocks on US dollar-denominated bonds issued by euro area, China, and the rest of the world over the first 20 quarters. The resulting international portfolio shift toward non-US assets lowers financing costs in those regions and induces a 10% dollar depreciation in the first year, consistent with recent evidence. In our simulation, these developments support euro area economic activity, mitigating the adverse direct effects of tariffs and uncertainty (blue starred line). The euro appreciation pushes inflation further below its baseline level over the entire simulation period.

All in all, our simulations suggest that higher US tariffs have significant negative effects on economic activity in the euro area. These are exacerbated by retaliation and higher trade policy uncertainty, whereas the possible financial rebalancing effects could mitigate the overall impact. Importantly, our model abstracts from strategic interactions, preventing analysis of potential feedback effects from retaliatory trade policies.

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