MAARTEN SMEETS

The trade and tariff war: Implications for the EU and the World Trade Organization's multilateral trading system

The world is marked by geopolitical tensions, trade wars and a significant rise of nationalism driven by 'national economic security' considerations. Creating a competitive environment with new technologies and artificial intelligence requires access to critical minerals, including rare earths. Protectionism is on the rise, with high tariffs, import and export restrictions, foreign direct investment commitments by foreign enterprises, the (forced) relocation of production, limitations in technology transfers (chips) and new industrial policies, including subsidy programmes aimed at creating winners in the high-tech sectors. Nationalistic policies and bilateral trade agreements negotiated by the US with its trading partners, including with the European Union, lead to an increasingly fragmented and polarised world. There is an urgent need to return to a stable, predictable and inclusive trading environment. The world needs more cooperation and coherent approaches, as all policies are interconnected and cannot be solved by one country alone. Individualistic approaches exacerbate fragmentation.

The beginning of a new trade policy era

Following the election of US President Donald Trump in the autumn of 2024, 2025 was marked by major geopolitical tensions and trade wars. As outlined by the US Trade Representative, Ambassador Jamieson Greer, in his *New York Times* op-ed on 7 August 2025, "Why we remade the Global Order", the US Administration pursues the goal of establishing a trade balance with its trading partners. The so-called 'reciprocal tariffs' applied by the US are driven by the motivation and belief that the US has been taken advantage of by its trading partners and that this needs to be rectified. These policies are reinforced and increasingly driven by 'national security' considerations, and in that sense, the US is not alone: governments, in the interest of national (economic) security, feel obliged to implement policies that secure domestic production and employment in critical sectors of the economy. This need has become more pressing and urgent with the emergence of new technologies and the rapid rise of artificial intelligence (AI), which increasingly determines a country's competitiveness in international markets. Access to critical inputs, especially rare earth minerals, is essential for inputs in the production process and national security. These considerations have also led to the reintroduction of industrial policies, including subsidy programmes aimed at creating winners in the high-tech sectors.

A particular concern for many countries, including the US and Europe, has been the spectacular rise of China on the international scene. Since its accession to the World Trade Organization (WTO) in 2001, it has secured an increasingly dominant position in international trade, especially in high-technology goods. The huge trade surplus it developed with the US is at the origin of geopolitical tensions and the trade war, as well as the corrective measures under Trump I, which were expanded under the Biden administration and significantly strengthened under Trump II. The main concern today is China's fierce competition in many critical sectors, especially in high technology. While subsidy programmes exist on both sides of the Pacific, it is argued that China grants significant amounts of subsidies through its state-owned enterprises to its high-tech industries, distorting competitive conditions. A particular concern for the US is the strict control China exercises over its access to rare earths, especially through export restrictions, which limits the production capacity of foreign enterprises that rely on this critical input for the production of high-technology goods and are considered essential to national security.

While China is the US's main target, all countries are affected by US policies in its attempt to redress its trade (im-)balance. The US has negotiated and concluded a series of bilateral trade agreements with its trading partners, including both developed and developing countries. In addition to tariffs, the agreements include a variety of policy instruments, for example, import and export restrictions; foreign direct investment (FDI) commitments by foreign enterprises into the US; the (forced) relocation of production, often referred to as home-shoring and friend-shoring; and limitations in technology transfers, including chips.

Through these bilateral agreements, the US's trading partners attempt to find mutually agreeable solutions and mitigate the impact of trade measures on their economies. These negotiations are often lengthy, complex and challenging. The negotiations with China, especially, have turned out to be far more complex and challenging, given China's economic power, its near monopoly on rare earths and its capacity to retaliate. On several occasions, the US and China reached an understanding and concluded a deal, which soon became obsolete and was followed by new US trade measures and subsequent retaliation by China. The latest meeting between US President Trump and China's leader, Xi, held in late October in South Korea, led to a new truce, which appears to be holding for now. On the European side, the president of the European Commission, Ursula von der Leyen, signed a framework agreement on behalf of the EU with the US president in late July 2025 during their meeting in Scotland. The agreement does not focus solely on trade and should be considered in the broader context of a rapidly evolving, multi-polar world.

A tariff war as never seen before

In April 2025, the US president announced 'Liberation Day', which led to a broad range of tariff increases for its trading partners, which remain in place today. Their levels keep fluctuating, even after the conclusion of bilateral deals, as the US president frequently changes his mind on which tariffs to apply to which countries. The process of determining appropriate levels is not rocket science, but it is often opaque. Except China, which faces significantly higher tariffs, for most countries, they broadly range between 10% and 40%, mainly depending on the trade deficit. The American tariffs are legally based on the 'national security argument' in Section 232 of the US Trade and Expansion Act of 1962, as well as on Section 301 (Title III of the Trade Act of 1974), "Relief from Unfair Trade Practices". The tariffs are both broad and sector-specific. While their main goal is to correct the bilateral trade deficit with each trading partner, the tariffs equally pursue non-trade-related goals. In the case of China, one of the initial arguments by the US to apply tariffs was to counter Chinese exports of fentanyl to the US, which is responsible for killing tens of thousands of US citizens every year. These were referred to as the 'Fentanyl tariff' and were initially set at a level of 20%, but were subsequently reduced to 10% following the understanding reached between President Trump and President Xi in South Korea on 29 October 2025. India was charged with an additional 25% tariff on many products, as a consequence of India's continued purchase of Russian oil. In the case of Canada, an additional 10% punitive tariff was imposed on Canadian goods following the Ontario government's controversial TV ad, which featured remarks by former President Ronald Reagan against tariffs.

The evolution of US tariffs applied against China, and the Chinese retaliatory tariffs against the US, is more complex, with their levels fluctuating and frequently changing in response to the outcomes of bilateral negotiations and agreements reached between the US and China. According to a detailed tracking of the tariff history by Chad Bown from the Peterson Institute for International Economics since the trade war was launched under Trump's first administration until today, the tariffs against China reached a peak of nearly 150% this summer. Since then, they have frequently changed, and the rates 'stabilised' at 57.6% of US tariffs against China and 32.6% tariffs applied by China against the US. Most developing countries, as well as some of the least developed, face tariffs between 15% and 30%. This compares with an average most favoured nation (MFN) import duty of around 3.5% in most developed countries and a 6.5% import duty applied by China towards its trading partners and the US, before the trade war. As explained further below, the MFN rate is the WTO's legally binding commitment for its members. Hence, the actual tariff rates far exceed the average legally binding ones.

Developed countries have negotiated different deals: the UK negotiated a relatively good deal with a 10% tariff; Switzerland was initially hit with one of the highest tariffs at 39%, but in mid-November it managed to bring these down to 15%. In addition, Switzerland will reduce import duties on US goods, and Swiss companies have committed to investing $200 billion in the US by 2028. The EU concluded a tariff rate of 15%, as discussed further below. While the US maintains its policy of duty-free treatment of products originating from Mexico and Canada under the US-Mexico-Canada Agreement (USMCA), which secures free trade among the three partners, the US applies 25% import duties on goods that do not originate under USMCA. Examples are certain imported and mostly foreign-made vehicles, auto parts and components, steel and aluminium products imported from third countries and not subject to exemptions, semiconductors, pharmaceuticals, and some consumer goods. Also, it has become apparent that the level of the tariff rates was not only determined by the bilateral trade deficit, but to a large extent by the negotiating techniques and skills of the leaders and the president's own judgement. This demonstrates, to some extent, the arbitrary nature of the tariff levels.

The EU-US 'trade agreement'

European Commission President Ursula von der Leyen signed the so-called US-EU 'trade' agreement in Scotland in late July 2025, referred to as the US-EU Framework on an Agreement on Reciprocal, Fair, and Balanced Trade ('Framework Agreement'). The White House issued details on its contents on 21 August 2025. Under the terms of the Framework Agreement, the US tariffs applied against the EU are set at the higher of either the US MFN tariff rate or 15%, comprised of the MFN tariff and a reciprocal tariff on goods originating from the EU. The EU, on its part, intends to eliminate tariffs on all US industrial goods and provide preferential market access for a wide range of seafood and agricultural products. The effect and impact of the tariffs will differ for each sector, with the European automobile industry being one of the most affected sectors.

In addition to tariffs, the Framework Agreement covers a range of other areas, including energy supplies, that is, buying US liquified gas, oil and nuclear energy estimated at $750 billion; FDI 'commitments' into the US of around $600 billion; procurement of military defence; non-tariff barriers; agriculture; environment (Carbon Border Adjustment Mechanism); critical minerals; intellectual property rights; and electronic commerce. Hence, the agreement is not exclusively a trade agreement but encompasses many areas that extend well beyond trade.

Looking more carefully at the so-called 'Trade' Framework Agreement, the language used in the agreement is often non-binding and at times weak. Additionally, it refers in many places to further work that needs to be undertaken, indicating that it is a work in progress. On tariffs, the agreement states that the EU 'intends' to scrap all tariffs on US industrial goods. A key question is whether the EU will apply the MFN principle, thus extending that advantage to all of the EU's trading partners. The word 'intends' is mentioned in many places, including about the EU's intention to procure US liquefied natural gas, oil and nuclear energy products to the amount of $750 billion. The same applies to the purchase of $40 billion worth of US AI chips for its computing centres, and again, the same applies to a $600 billion investment by EU companies across strategic sectors in the US through 2028. These investments are private sector investments, and hence, cannot be enforced by governments. It is said that these investments are the outcome of consultations with European business leaders and were largely planned in advance.

While the agreement implies significant economic costs – mainly on the European side – on the upside, the agreement certainly creates a more stable and predictable environment in relations between the two biggest trading partners than would be the case without the agreement and guarantees continued market access to both sides of the Atlantic. The agreement will be up for review and refinement as time passes.

While the agreement has led to critical reactions, observations and questions about its contents and the rationale for giving in to US demands, especially from members states that are likely to be the most impacted, including France and Germany, for now the agreement offers stability and predictability in its relations with the US and provides a basis for continued discussions and negotiations. One often-heard, and probably most important, explanation for this deal is the broader EU consideration of maintaining good relations with the US as an ally in the West at a critical juncture in the war between Russia and Ukraine. Moreover, the US is a key trade partner with a significant market, and maintaining close transatlantic economic and trade ties is of mutual economic interest. Harmonious relations between the US and the EU are of the essence, and that is, for now, achieved through the Framework Agreement, despite its shortcomings.

That being said, given the uncertainties in transatlantic trade relations and the costs associated with the implementation of the agreement, the EU should pursue its efforts to expand and diversify its trade relations with other trade partners on all continents, including with Canada, Japan, India, South Korea and countries in Latin America. Efforts to that effect are underway, and in September of this year, the European Commission formally submitted the final text of the EU-Mercosur partnership agreement to the European Council for ratification by its member states.

Bilateralism puts multilateralism at risk and nationalism drives fragmentation

Geopolitical tensions, the tariff and trade wars, and the significant number of bilateral deals they led to put multilateralism at risk. Already, the WTO multilateral trading system has been significantly weakened over the past decades, as its rules have not kept pace with the developments in international trade and are outdated in many instances. Trade patterns have changed drastically following a period of globalisation and with the introduction and rapid evolution of new technologies. The trade rules designed at the time of the Bretton Woods conference shortly after World War II are largely obsolete. Even the WTO, created in 1995 and meant to address the challenges emerging from globalisation, is no longer offering the panoply of rules required in today's trading environment. The new rules meant to take into account the new patterns of trade following the dynamics of globalisation are no longer adequate. Most importantly, the bilateral deals undermine the fundamental principle of the MFN, which requires each WTO member to apply the same tariff to all its trading partners multilaterally. Even though, according to the WTO, most world trade is still conducted under MFN, this principle is now being eroded. The MFN concept ensures equal treatment between WTO members, securing transparency, stability and predictability. To the extent that tariffs negotiated and contained in bilateral trade agreements exceed the tariff bindings, they are in breach of the MFN principle. It is also noted that tariffs are typically reduced in 'rounds' of multilateral trade negotiations, rather than increased. Exceptionally, they can be increased, which implies a complex and onerous process, involving lengthy negotiations with the main trading partners and providing 'compensation'. These rules are ignored under the newly negotiated bilateral deals, and no compensation in the sense of Art. XXVIII of the General Agreement on Tariffs and Trade (GATT) is discussed. Under the relevant GATT provision, compensation should be offered to any trading partner that is affected by the change in tariff. It is deemed to be covered under bilateral deals, disregarding the rights of third parties.

The sky-high tariffs the world has witnessed have not only not been seen in over 100 years, but they are also in direct violation of the MFN principle. Substituting MFN tariffs with bilaterally agreed duties puts the multilateral trading system at risk. Equally, the ongoing tariff war and proliferation of unilateral economic security policies have eroded trust in global trade and significantly undermined the rules-based framework established under the WTO. The multilateral trading system risks becoming increasingly irrelevant if it cannot restore order. Restoring trust in trade does not happen overnight and requires cooperation and coherence. This will take time.

From an economic angle, and more globally, the significant increase in tariffs also poses a risk for the world economy, triggering inflation, and hence, price increases for consumer goods. Reports by the WTO, International Monetary Fund and OECD underscore that the protectionist measures and policies are already undermining economic growth. The escalation of trade conflicts and a rise of tariffs to peak levels never seen before, followed by tit-for-tat policies, worsens economic prospects, hence the urgency to contain and defuse trade conflicts. The price increases (inflation) that have occurred have most recently led to the US president reducing them on essential consumer goods.

The new, unpredictable and often uncertain policy directions directly affect business and investment decisions. As part of US policies, both American and foreign companies are strongly encouraged to increase their investments and relocate their economic activities to the US, regardless of the efficiency principle. The results are that global value chains (GVCs) are shortened by relocating production nearer to the consumer, a trend often associated with the process of 'de-globalisation' or 're-globalisation'. While it is generally recognised that globalisation has generated economic welfare benefits to society, it is also true that globalisation has not come to the benefit of all, thus leading to a considerable setback. For a better understanding, globalisation mainly consisted of the free flows of trade and investment across the globe, with companies allocating parts of the production processes where the most economic efficiency gains could be obtained. Through the GVCs, many countries became part of the production process, based on the notion of comparative advantage and leading to the final product. While the efficiency gains obtained in the course of production generated economic benefits for producers and consumers around the globe alike, it also implied delocalisation of production across borders. It is often argued that this led to the loss of jobs domestically and caused the trade deficits. This, in turn, led to governments introducing nationalistic policies aimed at protecting domestic markets, securing national welfare and protecting jobs based on national security considerations. A host of protectionist measures and policies were introduced to that effect, including tariffs, and as shown earlier, many of which are spinning out of control and applied with a total disregard for the rules of the WTO.

From a trade policy perspective, the world has thus entered a period of chaos and uncertainty, which, in turn, affects productive investment and disrupts GVCs. A process of decoupling – de-globalisation – has led to economic fragmentation, a re-orientation of trade and the forming of new alliances along geographic lines. According to UNCTAD reports, it has also led to a significant decline in FDI, as companies are holding back on their long-term commitments. Trade uncertainty affects business decisions, which are based on a long-term vision and require a stable, secure and predictable environment.

That being said, it is also argued that the deep specialisation and breaking up of production processes have shown their weaknesses and vulnerability. While trade integration and specialisation increase economic efficiency, at the same time, they increase the risk factor inherent to a high interdependency between nations. As ‘a chain is as strong as its weakest link’, the longer the chain, the higher the vulnerability. Both the risks and vulnerabilities were further exposed during and after the Covid-19 pandemic and increased following the geopolitical trade wars. This would then argue in favour of shorter supply lines again.

A revival of industrial policies drives competition in high tech and AI

A major factor changing the economic and trade landscape is the significant and unprecedented rise in technologies, accompanied by a rapid increase in AI. As a result, international competition in trade of goods has fundamentally changed, creating new challenges and opportunities for both production and trade. Access to those technologies is of critical importance in determining comparative advantages and efficiency, and hence, is at the centre of current trade wars between leading trading nations. The production processes require raw material inputs, such as rare earth elements and various minerals, which are predominantly found in certain countries. China holds a near-monopoly position in the inputs that are essential for the high-tech industry. Given the strategic importance of technology in creating a competitive edge, the US, China and Europe are all competing for a dominant position in the high-tech industry.

Limitations in access to critical minerals through import and/or export bans affect supply lines and the very existence of the industries that depend on these inputs. It has been at the centre of the trade war between the US and China, with measures and retaliatory actions taken on both sides of the Pacific. The US measures have direct extra-territorial implications and apply to industries in Europe alike, as European industries were also prohibited from selling technology and chips to China.

This explains why governments increasingly pursue nationalistic policies paired with pro-active industrial policies in support of potential winners. Governments support their industries in various ways, mostly through subsidies. These can be found in different forms on all continents. Governments' industrial policies specifically target high-technology sectors to generate value addition and create a competitive edge. Government support programmes include R&D funding and subsidies to build productive supply capacity. Such programmes are found in the US, China and Europe alike and involve billions of dollars. Subsidies, by definition, distort competitive conditions, thus adding to trade tensions.

The ways forward: Diversification, coherence and cooperation

This leads to the question of how trade should be conducted in an increasingly fragmented and polarised trading environment, taking into account both national security and national and global economic interests. What trade policies offer the most appropriate response to the new economic realities, and what WTO reforms can fix the system, make it relevant again, and contribute to sustainable and equitable development? How can a framework be designed that preserves openness while minimising vulnerabilities? Last, but not least, what role is there for the EU to play? It is time for bold actions, taking into account the new economic realities.

The high trade interdependencies have increased the vulnerabilities of the GVCs and triggered fragmentation in trade and new patterns of trade along geopolitical lines. The rules of the WTO have not kept up to date with the rapidly evolving realities in trade and the emergence of new technologies, which in many cases have made the trade rules irrelevant. Bilateral approaches and regionalism are increasingly becoming the alternative to multilateralism, addressing trade concerns where multilateral trade rules are lacking. Pro-active industrial policies are increasingly pursued by governments, including by providing subsidies in critical sectors of the economy, especially in the high-tech, AI and IT sectors, and significantly distort competitive conditions. A lack of diversification and overreliance on single sectors has proven problematic for many countries. Governments employ various forms of direct and indirect state intervention, indicating a system of friction.

There is an urgent need to return to a more stable, predictable and inclusive trading environment. This requires proactive leadership and a vision for the future. Theoretical and ideological approaches have not been productive. While recognising that the US, for now, is no longer as actively engaged in the multilateral trading system as it was before, there is a need for leadership, which should not be limited to the main players, that is, the EU, US (albeit unlikely) and China, including the middle grounders and especially the emerging economies.

Achieving more inclusive, resilient and sustainable outcomes requires intensified global cooperation and coherence in economic policies at the global level. This includes coherent and sustainable industrial policies, avoiding subsidy wars and creating new economic opportunities for developing countries in support of their fuller integration into the trading system. Inclusiveness also means a deeper involvement of Africa in trade, which should benefit from trade and investment, especially in the critical mineral sector, and bring them into the GVC.

The business community and civil society have a crucial role to play in rebuilding trust in trade. Business needs to be made more fully aware of the risks, build resilience of GVCs, diversify and innovate. Productive ecosystems need to be built around security concerns in addressing trade and investment policies. Approaches to national security need to be comprehensive and coherent. Vulnerabilities due to dependencies on critical inputs, which are essential for maintaining competitive conditions, including rare earths, need to be mitigated by revisiting GVCs through innovation and diversification.

To conclude, the world needs more cooperation, not less, as all policies are increasingly interconnected and cannot be solved by one country alone. Coherent policies require governments to communicate and collectively address concerns, rather than attempting to address them individually, as this would only exacerbate fragmentation and trade tensions. The EU, through the Commission and its member states, can and should play a leading role in support of a strong and open multilateral trading system, especially with the upcoming 14th WTO Ministerial Conference to be held in March 2026, and when France will host and lead the G7 in 2026.