

SPECIAL ISSUE ARTICLE

How the US Reciprocal Tariff Plan May Save the Global Trading System

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(Received 30 May 2025; revised 30 May 2025; accepted 30 May 2025)

Abstract

The US plan to impose reciprocal tariffs is a game changer. If you ask *The Economist*, Trump's tariffs 'really mean chaos for global trade'. If managed well, the opposite could be true: it could be the largest round of trade negotiations since the creation of the World Trade Organization (WTO) and a much-needed rebalancing of global trade relations to catch up with fundamental changes that occurred, but remained unaddressed, for close to a quarter century.

Keywords: WTO; reciprocal tariffs; most-favoured nation; tariff renegotiations; balance of concessions; reform of the trading system; tariff as interface

1. The US Reciprocal Tariff Plan

Before April 2025, Trump tariffs targeted specific countries (e.g. China) or products (e.g. steel and aluminium). These tariffs were enacted to protect an industry at home, or as leverage to change something abroad. They were temporary, ad hoc.

Tariffs under the US reciprocal tariff plan (announced on 2 April 2025¹), on the other hand, hit all trading partners and all products with only limited exceptions: a base rate of 10% for everyone (on top of pre-existing rates) increased country-by-country depending on the bilateral trade balance. Deals will likely be struck to lower the initial rate. However, it remains to be seen whether President Trump will be willing to bargain also about the 10% base rate.

Because US tariffs are expected to be used as a much-needed source of revenue (allowing for internal corporate and income tax cuts), US reciprocal tariffs (or at least some of them) are likely here to stay. They were enacted both as a leverage to strike deals and as a source of revenue and an incentive to bring production back to the US.

As initially announced on 13 February 2025,² it seemed that the US reciprocal tariff would vary, not only country-by-country but also product-by-product and be based on whatever tariff or non-tariff barriers or distortions the exporting country has in place against the US. The US tariff on, for example, cars would no longer be 2.5% for everyone (except countries with whom the US has a free

¹'Regulating Imports with a Reciprocal Tariff to Rectify Trade Practices that Contribute to Large and Persistent Annual United States Goods Trade Deficits', Executive Order, 2 April 2025.

²'Reciprocal Trade and Tariffs', The White House, 13 February 2025.

trade agreement). Instead, the US car tariff would mirror whatever tariff a trading partner imposes on US cars. Today that means 10% for European cars, 15% for Chinese cars, and 75% for Indian cars.

This did not materialize. Nor did the US administration calculate the reciprocal tariff based on any aggregate level of protection or trade distortion in place in the exporting country. Instead, US reciprocal tariffs were calculated with reference to what the US sees as a proxy or consequence of the lack of reciprocity in current US trade relations, namely: bilateral (goods) trade deficits. As a result, the US reciprocal tariffs vary from 10% (e.g., for the UK, with whom the US has a goods trade surplus) to 50% (for Lesotho, which sells textiles and diamonds to the US but hardly buys anything from the US).

2. The Rationale behind US Reciprocal Tariffs

The US explains its reciprocal tariffs with reference to a lack of reciprocity in current US trade relations. Essentially, the US has among the lowest simple average MFN tariff rates in the world (3.3%), whereas many other countries have significantly higher rates (the EU: 5%; China: 7.5%; India: 17%). More importantly, other countries maintain relatively high non-tariff barriers and other economic policies, including currency policies and policies that suppress domestic wages and consumption and thereby demand for US exports. In addition, many countries (in particular, China) provide subsidies and create other distortions (such as structural overcapacity) which artificially increase the competitiveness of their goods in global markets and thereby inflate US imports.

Although large and persistent, overall increases in trade deficits (the US overall trade in goods deficit increased from 158 billion US\$ in 1995, when the WTO entered into force, to 1.2 trillion US\$ in 2024) are caused by many factors (including low saving rates in the US), the US administration is convinced that lack of reciprocity in trade relations is one causal factor. Similarly, even though trade deficits can be tackled in several ways (e.g. by reducing government spending or weakening the US\$), the US administration is determined that rebalancing trade relations is one way to reduce the US trade deficit.³

On 2 April 2025, President Trump declared 'large and persistent annual US goods trade deficits' to be a national emergency and invoked executive powers under the International Emergency Economic Powers Act (IEEPA) to impose, without Congressional approval, the reciprocal tariffs.

However, on 9 April 2025, for all countries except China, these tariffs were suspended for 90 days on the ground that 'more than 75 ... foreign trading partners ... have approached the United States to address the lack of trade reciprocity in our economic relationships and our resulting national and economic security concerns. This is a significant step by these countries toward remedying non-reciprocal trade arrangements and aligning sufficiently with the United States on economic and national security matters.'⁴

At the time of writing (late May 2025), foreign delegations are frantically flying in and out of Washington DC to negotiate with US authorities. The US reached (preliminary) trade deals with the UK⁵ and China⁶. In both deals, the 10% base rate of the US reciprocal tariff was maintained. The current 90-day deadline to reach more deals ends on 8 July 2025.

3. The WTO, Reciprocity and US Unilateralism

Variable tariff rates, depending on origin, for one and the same product fly in the face of a key principle of the global trading system that has been in place for close to 80 years: the so-called

³See US Census Bureau data, www.census.gov/foreign-trade/balance/c0004.html.

⁴'Modifying Reciprocal Tariff Rates to Reflect Trading Partner Retaliation and Alignment', Executive Order, 9 April 2025.

⁵'Trump, Starmer Hail Limited US-UK Trade Deal, but 10% Duties Remain', Reuters, 9 May 2025.

⁶'US and China Agree to Drastically Rollback Tariffs in Major Trade Breakthrough', CNN, 12 May 2025.

non-discrimination or Most-Favored Nation (MFN) rule. In defense, the US is invoking the WTO's national security exception. If prior WTO dispute rulings on this exception are of any guidance, it is unlikely that the US defense would succeed⁷.

Chaos for global trade, and the end of the WTO? Perhaps, but it does not have to end this way.

It is not just President Trump who seeks reciprocity. When it was created in the mid 1990s, the WTO itself was fundamentally built on reciprocal balance of trade concessions. It was only when all WTO members considered the exchange of trade concessions (including non-tariff concessions such as protecting intellectual property rights and special considerations for developing countries) to be sufficiently reciprocal that MFN obligations kicked in.

MFN does not operate in a vacuum. It is pre-conditioned on reaching a state of rough equivalence in trade concessions, understanding the different economic status of various countries. However, once this reciprocity is seriously out of kilter, applying MFN no longer makes sense. Though trade concessions were considered to be on balance 'reciprocal' in 1994, the world has dramatically changed, first and foremost as a result of the rise of China based on a radically different model than the market-based model that was expected when China joined the WTO in 2001. Yet, no update or re-adjustment to this balance has happened since.

The problem is that for the last quarter century (ever since China was admitted to the WTO and the so-called Doha Round negotiations were kicked-off, in 2001) the WTO has been hopelessly blocked from reaching a new consensus on even small items, much less a fundamental rebalancing of the terms of trade.

In the face of this deadlock, and after trying for decades, the US has taken matters into its own hands, using unilateral pressure and tariffs rather than consensus building and cooperation. It is not the first time this has happened. Similarly, frustrated with lack of progress in GATT negotiations in the 1980s, the US used unilateral sanctions and regional trade agreements (especially NAFTA) to pressure trading partners (particularly the EU and Japan) to agree to trade deals in Geneva. The result of this first period of US 'aggressive unilateralism'⁸ was the creation of the WTO in 1994.

4. Things to Watch If and When the US Strikes Reciprocal Trade Deals

At the time of writing, hurried, bilateral trade negotiations between the US and other countries threatened by US reciprocal tariffs seem far removed from ordinary trade negotiations which normally take years to conclude. Most observers also fear that such deals would undermine rather than restore the global trading system.

How could such negotiations be stepping stones toward a global rebalancing?

Firstly, at this stage, the US seems to prefer to negotiate bilaterally, in order to exert as much pressure as possible and keep the upper hand. That said, other countries may want to team up to negotiate (and, where needed, retaliate) collectively (e.g. under the umbrella of ASEAN or the CPTPP). Coalitions of the willing could also be formed to tackle collectively certain systemic issues that go beyond bilateral tariffs (e.g. trade relations with China). Even if, at first, purely bilateral deals are struck, such deals could subsequently be expanded to create regional, sectorial, or issue-specific plurilateral agreements or 'clubs'⁹. In short, anything that could elevate bilateral agreements to bigger

⁷ See Panel Report, *Russia – Measures Concerning Traffic in Transit*, WT/DS512/R, adopted on 26 April 2019. See also Panel Report, *US – Certain Measures on Steel and Aluminium Products*, WT/DS544/R, circulated on 9 December 2022 (under appeal).

⁸ J. Bhagwati and H. Patrick (1990) *Aggressive Unilateralism: America's 301 Trade Policy and the World Trading System*, University of Michigan Press.

⁹ A case in point may be an emerging steel arrangement or 'steel club' whereby a group of like-minded countries agree on certain common principles (be they related to national security, tackling Chinese overcapacity, or carbon emissions) and on that basis liberalize steel trade between them. Countries outside of the club remain subject to higher trade restrictions. See 'General Terms for the US–UK Economic Prosperity Deal', The White House, 8 May 2025 under which the US would drop its 25% national security duty on steel and aluminum subject to the UK meeting certain 'US requirements on the security of

groups or clubs could not only speed-up dealmaking in view of US-imposed deadlines, it could also facilitate tackling cross-cutting, collective problems, avoid circumvention and trade diversion, and ensure more efficient implementation.

Secondly, as much as countries may give tariff and other trade concessions to the US in order to avoid the US reciprocal tariff, the question arises whether these concessions will be extended also to other WTO members on an MFN-basis. Unlike the US, the EU and many other countries remain deeply committed to the WTO. So technically, if the EU reduces its car tariff from 10% to 2.5% or even 0%, it should grant this benefit not just to US cars but also to cars from all WTO members, including, for example, Chinese cars. For the EU and most other countries willing to lower their tariffs, this creates a serious free-rider problem. China, in the case at hand, would benefit without giving anything in return. One way out is to conclude a deal with the US that would qualify as a free trade agreement (FTA) under GATT Article XXIV. However, this requires, amongst other things, liberalizing ‘substantially all trade’ between the parties, on a reciprocal basis, something that may be hard to achieve (even if a long implementation period of, say, 10 years were chosen). The pressure to comply with MFN and/or WTO FTA conditions¹⁰ may force countries to sit around the table more collectively in order to tackle the free-riding problem head-on. Would China, in the example used above, be willing to give something to the EU in return for the EU extending certain concessions on an MFN basis? Any incentive pushing countries to discuss matters more collectively, beyond their trade relation with the US, could be a stepping stone to a rebalancing of the broader trade system.

5. GATT Article XXVIII as a Mechanism to Bring Reciprocal Tariffs and Reciprocal Tariff Deals Back under the WTO Umbrella

A lot of uncertainty remains as to whether the US will be able to strike meaningful bilateral deals and, if so, whether (i) any of these deals will trigger more collective agreements or (ii) broader concessions beyond US trade. Equally unclear is whether there will be a role for the WTO in cases where deals are struck and have ripple effects beyond US trade. The US may decide to leave the WTO, and an alternative structure may be created or emerge organically. The WTO could also survive, with or without US withdrawal, and fallback on more technical, committee work (focusing on exchange of information and best practices) rather than attempt to address the big questions of the day, which have become highly political and for which the WTO may simply not be equipped (if only because of its consensus principle).

That said, there is one mechanism that already exists and that may be a workable tool to house some of the rebalancing within the architecture of the WTO, and without the need for a consensus of all WTO members.

The good news for the WTO is, indeed, that a procedure already exists that permits a single country to trigger a re-negotiation of current tariff levels. It is Article XXVIII of the GATT, pursuant to which any WTO member can unilaterally change its tariff commitments, subject to negotiating compensation with those countries that are most affected by the tariff change (in effect, countries representing 10% or more of imports). Although the US has not triggered Article XXVIII, that is exactly what it is doing in practice: telling other nations that it wants to pull back US tariff commitments and replace them with a new balance of concessions: namely, a base reciprocal tariff of 10% (on top of pre-existing US tariff rates), plus variable additional rates depending on the bilateral trade balance.

Pursuant to Article XXVIII, the US should first negotiate ‘compensation’ with its trading partners. This offers an opportunity to incorporate into the WTO any of the bilateral deals the US may strike

the supply chains of steel and aluminum products intended for export to the United States and on the nature of ownership of relevant production facilities.’

¹⁰See ‘UK Accused of Undermining WTO Rules with US Trade Deal’, Politico, 22 May 2025.

before 8 July. In addition, even if no deals were struck with certain countries, Article XXVIII allows the US to raise unilaterally its tariffs anyhow, after which substantially affected countries (representing more than 10% of imports under an affected tariff heading) can retaliate by suspending substantially equivalent concessions initially negotiated with the US.

Although the US is not likely to be willing to offer any 'compensation' in return for its reciprocal tariff – in its view, this tariff merely compensates for trade barriers and distortions already in place in other countries – the Article XXVIII process offers a way to incorporate bilateral deals, the US may make, into the WTO structure. Similarly, although the US is not willing to suffer retaliation by other countries in response to its reciprocal tariff, the right to retaliate set out in Article XXVIII (without having to go through a prior WTO dispute process) provides an incentive for the US to make a deal while avoiding an escalating trade war, as Article XXVIII caps this right to retaliate at an amount equivalent to the original tariff modification.

Instead of purely bilateral discussions with, and retaliation (or retaliation threats) against the US, the EU and other major trading nations should coordinate a broad-based Article XXVIII re-negotiation process. The domino effect of this process (with each change in tariff or retaliation in response, other countries are drawn into the negotiation round) would de facto force all major trading nations to sit around the table and agree on a new balance of trade concessions. And even if they do not agree, other countries can change their tariffs unilaterally subject only to capped retaliation by substantially affected trading partners. If managed properly, this could, in effect, turn into the biggest tariff negotiation round since the creation of the WTO, with the potential to create a fairer and more enduring result.

6. Tariffs as a 'Price' or 'Interface' to Offset Domestic Divergencies and Distortions that Are Here to Stay

The above-described tariff negotiations, be they conducted purely bilaterally in Washington DC or housed under Article XXVIII, will likely differ from those in the past in one key aspect: tariffs could not only go down (as is the case in standard FTA negotiations), they could also go up.

The difficulty for the WTO is that it was created on the assumption that economic models (even that of China) would converge around the Washington Consensus, including its principle of reducing trade restrictions, privatizing state-owned enterprises, and abolishing barriers that restrict competition or foreign direct investment. Under this model, tariffs should only go one way: down.

We are no longer living in such a world. The reality today is that the political and economic organization of states varies dramatically and that many, or most, of these differences are here to stay.

To enable trade between such differently regulated states, interface mechanisms are needed. One such interface is to put a price on the major differences. Think of the competitiveness impact of certain forms of state intervention or regulation, or the lack thereof, including major differences in social or environmental regulation, competition policy, or even free speech. These are all sensitive topics that a world trade organization should not attempt to iron out. What it could do instead is bring countries around a table to discuss what it would take to have a roughly balanced trade regime (starting with reciprocal tariff levels) that takes these major differences into account.

This 'tariffication' of the cross-border spillovers of major divergencies cannot and should not be calculated to precision. Political agreement on an overall, reciprocal balance would suffice. Defusing major divergencies between the US and China, the EU and the US, the EU, the US and India, and others, by putting a 'tariff price' on them would also take the sting out of national security exceptions and even trade remedies, which are now being used (often unsuccessfully) to address problems that go beyond what these safety-valve instruments were designed for.

7. How to Make a New Balance of Tariff Concessions MFN-Proof?

A key challenge of reciprocal tariffs or tariffs that ‘price’ distortions in place in specific trading partners, is whether this can be done on an MFN-basis – that is, in a non-discriminatory way.

One approach to marry MFN with reciprocal tariffs is the option under GATT Article II:1(b) to make tariff concessions conditional on certain requirements (‘subject to the terms, conditions, or qualifications set forth in [a WTO member’s] Schedule’). In practical terms, the US could keep its current tariff bindings in place but condition them on the absence of certain trade barriers or distortions in the exporting country. Even if this would mean that US tariffs on, say, China are higher than those on the EU, this difference would not be discriminatory if it can be justified with reference to objective conditions set out in the US schedule (for example, structural overcapacity induced by the government in place in China, but absent in the EU).

8. Conclusion

The above-described re-set or de facto new ‘round’ of tariff negotiations would take some time. The US has set a deadline for bilateral deals of 90 days, expiring on 8 July 2025. If no deal is struck, the US threatens to unilaterally impose its country-specific reciprocal tariff. Similarly, under WTO rules, a deadline of 6 months could be set and even if a specific country objects, the process cannot be blocked by any WTO member. Indeed, when Article XXVIII negotiations over a tariff line fail, the country proposing the change can implement it unilaterally. In response, the major exporters of the product concerned can withdraw equivalent concessions initially negotiated with the country modifying its tariff. Agreement or no agreement, reciprocity is the rule. The US may, at first, prefer to re-set reciprocity through bilateral negotiations. With time, it may realize, however, that the WTO is ultimately built on the same reciprocity principle and that working within the WTO structure would enhance the value of bilateral deals by multilateralizing and stabilizing them under one roof.

The WTO leadership has a key role to play. The Director-General of the WTO should immediately start consultations with WTO members to mobilize the energies of members with a view to address, in an orderly fashion, a number of imbalances that have triggered the radical reactions of the US administration. The EU faces major challenges similar to those that motivated the US to push for a new reciprocity approach. Those imbalances need to be urgently tackled after close to a quarter century of immobilism. It should be agreed that discussions and negotiations amongst members should be finalized within the limited horizon of six months. If no agreement is reached, individual WTO members can unilaterally modify their tariffs in line with GATT Article XXVIII.

There are several other very important issues that WTO members need to address, including trade and inclusiveness, the rise of industrial policies and subsidies, and improving the deliberative function of the WTO. It would be impossible to practically deal with them during such a short period of time. Yet, a revitalized WTO, following a positive outcome on reciprocal tariffs, would create the conditions for better international cooperation on these matters too.

If this could materialize, instead of chaos for global trade and the death knell of the WTO, Trump’s reciprocal tariff plan could be a boost for WTO reform and the creation of a new, fairer balance in global trade.