

Trumping Trade: USA Tariff Shocks and India's Policy Response

Rupali Rajvanshi¹

Assistant Professor

K. D. G. D. College

University of Lucknow, Lucknow (India)

Email: rupalirajvanshi@gmail.com

ORCID: 0009-0000-6950-343X ¹

Vivek Rajvanshi²

Professor

Indian Institute of Management Calcutta

Kolkata (India)

Email: vivekr@iimcal.ac.in

ORCID: 0000-0003-0610-4428 ²

ABSTRACT

Tariffs, a part of International Economics, play a vital role in global trade. The recent imposition of additional tariffs in August 2025 has sparked debate over whether tariffs are instruments of overall economic welfare or political tools that may disrupt international trade. In this study, we examine the economic impact of high tariffs, focusing on their effect on the Indian economy. Further, we analyse the Government of India's policy intent for its export-oriented sectors. Our study demonstrates that the Indian government leveraged this challenging situation into an opportunity by exploring new markets and promoting manufacturing.

Keywords: Economic Tariffs, Sanctions, Oil Imports, Economic Policy, International Trade

1. Introduction

The recent imposition of high tariffs by the USA on several countries worldwide has sparked debate over whether tariffs are economic or political tools (Hannon, 2024; FT Editorial, 2025). In the Indian-USA context, tariff policy has always been a topic of news and is subject to change from one regime to another. Recently, in 2025, a novel "reciprocal" tariff regime has emerged, in which tariffs are calibrated based on the partner's applied tariff structure, trade deficit, and broader geopolitical alignment with import values, reflecting this dual economic and strategic rationale (Kurtkoti, 2025).

Tariffs are taxes or duties imposed on goods and services imported from abroad. They are instruments of trade policy designed to regulate international trade flows, generate fiscal revenue, and protect domestic industries. Higher tariffs, as a price-distorting mechanism, encourage consumers to purchase domestic goods over foreign goods, potentially stimulating domestic production (Salvatore, 2020). Therefore, all countries continue to negotiate tariffs in their favour to bolster their economies (Handley & Limao, 2017). However, appropriate tariffs and overprotection of economies create deadweight losses by reducing overall economic welfare and can generate uncertainty for businesses and governments (Fajgelbaum et al., 2020).

Sometimes, countries impose Retaliatory Tariffs as a political tool to distort or maintain international relationships and bargaining power (Grossman & Helpman, 1992; Fetzer & Schwarz, 2021; Bown, 2021).

India's response to the USA's reciprocal tariffs is well-balanced, maintaining calibrated reciprocity, strategic diplomacy, and trade diversification, consistent with its policy of preserving export competitiveness and national

¹ Corresponding Author

interests (Ayyub, 2023; TOI, 2025; Reuters, 2025). Uncertainty in tariffs creates challenges for Indian businesses in making investment decisions and long-term planning, prompting firms to either delay investments or switch to alternative markets or products with lower risk, while the government takes steps to support the economy against these costs.

This study analyses the economic rationale behind the USA tariff imposition, underscores the implications of high tariffs for India, examines India's policy response, and highlights its contribution as an early, detailed discussion of reciprocal tariffs.

In the subsequent sections, we provide the objectives of the study, scope and methodology, results and discussions on (1) the economic rationale behind tariffs, (2) Impact of U.S. Tariffs and Russia Sanctions on India's Trade, Strategic Response (3) Tariffs, Sanctions and Oil Trade (4) India's Response to the New Tariff Regime (5) Negotiations and Talks with the USA over Tariffs. Further, we provide the limitations and research gap for future studies, and in the final section, we conclude the paper.

2. Objectives

The present study aims to examine the economic and trade implications of the tariff shocks imposed by the United States during the Trump administration and to analyze their impact on India's external trade performance and domestic economic stability.

Specifically, the study seeks to evaluate the sector-wise effects of increased US tariffs on Indian exports. Further, we assess the extent of trade diversion and investigate the macroeconomic consequences for India, including trade balance and exchange rate dynamics. We also critically analyze India's policy responses, both short-term corrective measures and long-term strategic trade adjustment, to understand how effectively India adapted to the changing global trade environment. The study also intends to draw broader implications for emerging economies facing protectionist trade regimes and shifting geopolitical trade alignments.

3. Scope and Methodology

This study examines trade disruptions caused by the United States' tariff measures during the Trump administration. It focuses on their impact on India's merchandise trade and overall policy response. The analysis covers key affected sectors, including steel, aluminium, textiles, pharmaceuticals, and selected manufactured goods. The study situates these developments within the broader context of global protectionism and changing trade alignments.

The paper adopts a mixed analytical approach. It relies on secondary data obtained from sources such as the WTO, UN Comtrade, the World Bank, the Reserve Bank of India, and the Ministry of Commerce and Industry. Trend analysis and sector-wise export performance evaluation are conducted to assess the magnitude of the impact. We analyse the trade to identify expected shifts in trade patterns. Notifications/News available in the public domain are also examined to understand India's response strategy.

4. Result and Discussion

4.1 Economic Rationale Behind Tariffs

Tariff imposition makes the terms of international trade favourable for a country which imposes them. The imposition of a tariff raises the price of imported goods by the amount of the duty, making them less competitive. Rational consumers seek to maximise their utility and start to prefer buying indigenous items. The Indigenous industry finds this opportunity productive and profitable, and it increases its output. Consequently, the demand for imported goods tends to decline over time.

The other economic theory behind tariff imposition is the need to correct the balance of payments. Tariff duties increase the price of goods. This encourages consumers to purchase indigenous goods, thereby reducing imports, which is a significant step towards correcting the balance of payments.

Tariff imposition provides protection to the domestic industry. In the infant stage, it is the government that upholds the industry to flourish. President Trump's policy signals a clear priority to safeguard vital industries and economic

stability. The United States adopted a strategic trade policy to boost domestic manufacturing. In this practice, import duties are barriers in the chosen sectors to promote domestic champions.

The primary objective of USA policymakers is to shield American producers and manufacturers from foreign competition. Using tariffs as an instrument, employment generation and industrial capacity building are being undertaken.

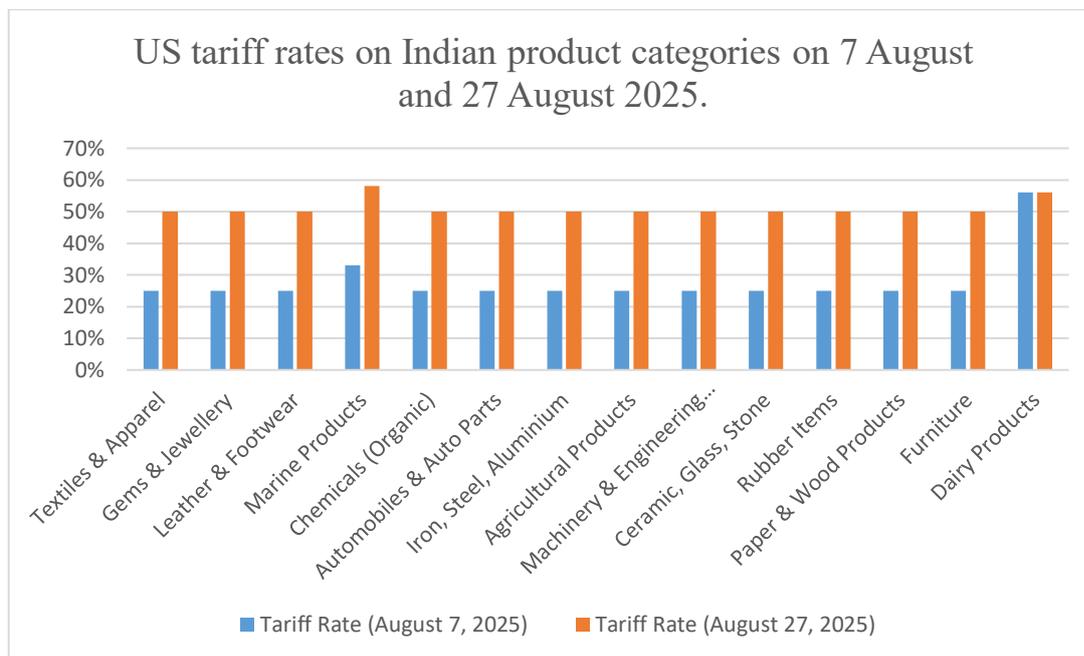


Figure 1: USA tariff rates on Indian product categories on 7 August and 27 August 2025.

Source: Authors' Estimates.

Figure 1 provides details of the tariffs imposed by the USA on India over a short period. The figure shows a significant jump in US government-imposed tariffs in August 2025 across most categories, except Energy and Pharmaceuticals. The tariff rate had reached 50% or more in most cases, compared to the 25% imposed earlier. Doubling the tariff rate clearly suggests that the tariff imposition is not the result of a desire to protect USA markets, but rather may be driven by some political motivation.

Higher tariff impositions are not solely governed by economic perspective, but also by political incentives, lobbying pressures, and strategic bargaining objectives. It is a politically driven tool in the current geopolitical context to exert pressure and strengthen its bargaining position. United States tariff actions against India were expected to interfere with India's trade, energy, and foreign policy alignments, particularly regarding its economic engagement with Russia and China (Sahai, 2025). The United States administration argued in support of tariff policy, citing national security concerns. Tariffs on steel and aluminium under Section 232 of the U.S. Trade Expansion Act of 1962 (19 U.S.C. § 1862) were stated to be necessary because the items were deemed to threaten national security.

4.2 Impact of U.S. Tariffs and Russia Sanctions on India's Trade, Strategic Response

President Trump argues that tariffs are necessary to prevent a global economic depression, justifying the invocation of presidential emergency powers and the imposition of tariffs (Aydogan, 2025). US courts have ruled that these tariffs exceeded the president's authority, creating uncertainty among businesses and countries (The Washington Post, 2025).

Table 1: Timeline of USA tariffs on Indian goods

Date	Event	Tariff Announcement
April 2, 2025	Announcement of reciprocal tariffs	The USA announced a 26% tariff on Indian goods, later adjusted to 25%.
April 5, 2025	Baseline tariff effective	A 10% baseline tariff on all imports, including India, was implemented.
April 9, 2025	Delay of nation-specific tariffs	The 16% nation-specific tariff for India was delayed for 90 days until July 9.
July 8, 2025	Extension of delay	The delay period for nation-specific tariffs has been extended to August 1.
July 30, 2025	Announcement of 25% tariff plus penalty	The USA announced a 25% tariff on Indian goods, effective August 7, and an unspecified penalty on Russian oil purchases.
August 1, 2025	The initial 25% tariff is effective	A 25% tariff (10% baseline + 15% reciprocal) applied to Indian goods.
August 7, 2025	Executive order for 25% tariff	The White House issued an executive order confirming a 25% tariff on Indian goods, effective immediately, with exemptions for pharmaceuticals, electronics, and energy.
August 27, 2025	An additional 25% tariff is effective	An additional 25% tariff was implemented, bringing the total to 50% for most Indian goods (except exempted sectors).
October 5, 2025	Grace period for in-transit goods	Goods loaded onto ships before August 7 and arriving before October 5 are subject to the earlier 25% tariff rate, rather than the 50% rate that applies to most Indian goods.

Source: Authors Estimates.

In August 2025, the United States imposed 50% ad valorem duties on Indian goods, including a 25% penalty on purchases of Russian oil, by invoking the 1977 International Emergency Economic Powers Act (Thorne, 2025). This tariff escalation has widened India's trade deficit, as the associated increase in trade barriers has dampened export performance. The resulting drop in exports has had a particularly pronounced effect on labour-intensive sectors such as textiles, gems and jewellery, engineering goods, and chemicals, which have borne the heaviest losses (ANI, 2025). Tariffs are a blunt and costly policy instrument: their adverse effects are of particular concern. Not only do consumers face higher prices, but tariffs also generate allocative inefficiencies and heighten the risk of trade conflicts. Moreover, these efficiency losses extend beyond the consumer, affecting producers, employment, and overall welfare.

In addition to the direct trade effects of U.S. tariffs on Indian exports, sanctions-related financial frictions further constrain India's engagement with Russian energy. Another important concern is transaction settlement. Following the imposition of sanctions, many Russian banks were cut off from the SWIFT international payment system, making it difficult to settle transactions in U.S. dollars. A common response to this problem has been to route payments through third countries, such as the UAE, which increases the complexity and opacity of the payment system (Verma & Browning, 2023). Furthermore, Indian companies face significant difficulties in handling Russian cargo due to insurance and shipping issues, as these transactions are perceived as highly risky because of concerns about inadvertently violating sanctions (Verma, 2024).

4.3 Tariffs, Sanctions and Oil Trade

As the United States imposes sanctions on Russia, India has purchased Russian crude oil at a significant discount, thereby reducing its import bill (Sahai, 2025). India's strategic approach to energy procurement demonstrates that it has created a notable cost advantage in the global energy market. In this complex geopolitical context, India has positioned itself strategically, transforming sanctions-induced market disruptions into substantial economic gains while formally maintaining compliance with international frameworks.

Indian exporters are also seeking to capitalise on the opportunities created by the withdrawal of Western firms from the Russian market, particularly in pharmaceuticals, engineering goods, and consumer supplies (Jayaprakash, 2024). However, they have thus far failed to fully fill the gap left by these firms, indicating constraints in supply capacity, market access, or risk tolerance.

4.4 India's Response to the New Tariff Regime

India has pursued a policy of strategic diplomacy calibrated toward reciprocity and trade diversification, with the main objective of preserving national policy autonomy. Diplomatic negotiations were the Government of India's initial response, aimed at maintaining its role as a strategic partner in the global trading system. India presents itself as ready to export its products and strengthen global partnerships, while consistently seeking to protect the interests of vulnerable sectors during negotiations (Sahai, 2025).

Subsequently, India was compelled to adopt retaliatory tariff measures. The diversification strategy is expected to expand markets for Indian products in other countries and foster new trade relationships worldwide (Aditya, 2025). In parallel, the government has launched several schemes, including Make in India and the Production-Linked Incentive (PLI) programme, to promote self-reliance across sectors and reduce external dependence. Together, these measures constitute a mix of short-term and long-term strategies to mitigate the challenges posed by tariffs and sanctions.

In the short term, the Government of India aims to minimise trade disruption caused by high tariffs, especially in labour-intensive export sectors such as gems and jewellery, precious stones, and textiles. Negotiations and strategic discussions are ongoing to address these concerns. At the same time, India is exploring new avenues for expanding its trade relations. For agricultural products, for example, negotiations with New Zealand have advanced to a fourth round, and significant progress has been reported (PIB, 2025). Alternative markets in the European Union, Asian economies, and the Middle East are emerging as important destinations for Indian exports (Tylson, 2025; Choubey, 2025). The government is also considering offering export incentives, such as tax relief, low-cost logistics, and targeted subsidies, to support export-oriented sectors.

Over the long term, a balanced structural strategy is required that aligns the pursuit of national interests with the principles of multilateral trade. A recalibrated policy framework offers a path to strengthening self-reliance and enhancing global competitiveness. This requires building technological capacity, promoting low-cost and efficient production, and consolidating a strong industrial base to reduce import dependence. It also entails improving workforce quality through upskilling, amending rules and regulations to reduce frictions, and ensuring efficient governance to facilitate economic activity. A robust institutional framework can enhance stability, transparency, and investor confidence, thereby supporting sustainable growth in an uncertain global trade environment.

4.5 Negotiations and Talks with the USA over Tariffs

Many rounds of talks between the two countries have been progressing well, and both sides are negotiating a comprehensive agreement that adheres to World Trade Organisation (WTO) norms (The Federal, 2025). It is widely expected that the two parties are close to a fair-trade deal, with convergence achieved on most outstanding issues. The Government of India has stated that it seeks a fair, equitable, and balanced trade agreement with the United States and will not compromise on the interests of farmers, fishermen, and the dairy sector (Indo-Asian News Service, 2025).

The primary objective of the higher tariffs imposed on India has been to curb its purchases of Russian oil, and these measures have had a significant impact on purchasing patterns (Jones & MacRae, 2025). Indian refiners have reportedly scaled back purchases of Russian crude oil, and major refiners are hesitating to place new orders.

This pattern suggests that Western sanctions and associated tariff measures have substantially constrained Indian oil buyers' ability to purchase Russian oil. As part of the ongoing negotiations, India has also pledged to increase its crude oil purchases from the United States (Singh, 2025).

5. Limitations and Research Gaps

Though this study is comprehensive and covers the subject, it still has some limitations. First, it relies predominantly on secondary data sources and publicly available reports. Second, the analysis is largely descriptive and trend-based, without employing advanced econometric or counterfactual modelling techniques to isolate the causal impact of U.S. tariff shocks from other concurrent macroeconomic factors such as global demand fluctuations, exchange rate volatility, or post-pandemic recovery effects due to the unavailability of more granular data.

Additionally, the rapidly evolving geopolitical environment and ongoing negotiations between India and the United States imply that the findings reflect a specific time frame and may not capture long-term structural adjustments or future policy reversals.

6. Conclusion

This study examines the impact of the new tariffs imposed by the USA on India and their impact on the Indian economy. In August 2025, the USA doubled the tariffs on Indian goods in several sectors, imposing an additional 25% tariff as a penalty for buying oil from Russia under the 1977 International Emergency Economic Powers Act. India's response to the USA tariffs has been balanced, and the country is attempting to resolve this conflict through diplomatic dialogue. Several rounds of talks between these two countries have progressed well. Indian refiners have reduced their purchases of Russian oil. India is also seeking new markets to expand its exports and reduce its dependence on the USA. India is also focusing on the 'Made in India' campaign and Production-Linked Incentive Schemes to provide support to Indian manufacturers, enabling them to compete with their international counterparts.

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