WORKING PAPER

The German Economy in Trump’s Trade War

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Abstract

At the start of Trump's second term as US President, Germany and the EU are facing a number of new challenges, from punitive tariffs to increased defense spending. These new challenges have precipitated several questions. Namely, what impact will Trump's trade policy have on the German economy, and how will Berlin deal with trade policy challenges together with Brussels in the coming years? This article will try to find answers to these questions.

1. Introduction

Germany and Europe are facing a new set of challenges as Donald Trump begins his second term as US president. In addition to curtailing US support for Ukraine and calling for a sharp increase in European defense spending, the relaunch of the Trump administration's trade war—which first began with higher US tariffs on products from Canada, Mexico, and China—is likely to have an impact on the European and German economies through export restrictions and import tariffs. Although they have since been paused, on April 2, Trump announced new US tariffs for trading partners worldwide that sent European markets spiraling downward—referred to as a "day of liberation" for the US[1] (see timetable in the appendix).

The European Union, along with China, is one of the United States' most important trading partners. The total trade deficit between the US and the European Union in 2024 was USD 247 billion. The US has the highest trade deficit among three-member states, at USD 88 billion with Germany, closely followed by Ireland at USD 87 billion, and Italy at USD 46 billion in the same year.[2] The trade deficit of

[1] Rob Wile, "Trump's tariff 'Liberation Day' is a little over a week away, but the details are still a mystery," NBC News, March 24, 2025, https://www.nbcnews.com/business/economy/trump-tariffs-april-2-liberation-day-what-to-expect-rcna197822.
[2] ITC Trade Map, https://www.trademap.org/Index.aspx.

Germany, Ireland, and Italy together accounts for almost 90 percent of the trade deficit between the United States and the European Union.

Trump's latest threats to impose wide-ranging tariffs on imports from every country are a radical departure from free world trade—the new punitive levies have shaken the global economy that was built by Washington with Europe's support in the aftermath of World War II. Germany, by far the US's most important European trading partner, will likely be hit hardest by the tariffs of any European state. This article, therefore, takes an in-depth look at German sectors that are particularly vulnerable to Trump's tariffs, the state of the German economy, and how Germany as a whole will be affected by the Trump's administration oncoming trade war.

2. Trump's Action: Import Tariff on Cars

Following the tariffs on steel and aluminum, President Donald Trump announced additional tariffs of 25 percent on all car imports, including engines, gearboxes, transmission parts, and electrical components, all of which are important for car production. With this move, he is thus exacerbating a trade dispute with the European Union/Germany.

The German automotive industry has been present and successful in the US for decades. The US levies only a 2.5 percent tariff on cars from the EU, while the EU levies a 10 percent tariff on US car imports.[3] The tenfold increase in tariffs on passenger cars is a severe setback for the German automotive industry, as the US is the most important buyer of passenger car exports from Germany.[4] Total trade in automotive goods between Germany and the US amounted to EUR 44.7 billion in 2024. German exports reached a total value of EUR 36.8 billion, while imports amounted to EUR 7.9 billion. The total export value of the German automotive industry in 2024 was EUR 280 billion, of which 13.1 percent went to the US.[5]

The German automotive industry employs approximately 138,000 people in the US. Of these, 48,000 work for car manufacturers and another 90,000 for German

[3] Thomas Puls, "Die Automobilindustrie im Jahr 2024," IW Koeln Report 38/2024, Köln, September 22, 2024, https://www.iwkoeln.de/fileadmin/user_upload/Studien/Report/PDF/2024/IW-Report_2024-Automobilindustrie.pdf.

[4] "US tariffs on German cars threaten industry profits and trade ties," MSN, https://www.msn.com/en-us/autos/electric-cars/us-tariffs-on-german-cars-threaten-industry-profits-and-trade-ties/ar-AA1BMSdw?ocid=BingNewsSerp.

[5] Ibid.

suppliers.[6] The US is an important part of the German automotive industry's production network, and it is from here that the global market is served. In 2024, German manufacturers produced more than 844,000 vehicles in the US, about half of which were exported worldwide.[7]

3. How Can the German Economy Mitigate Auto Import Tariffs?

The first option to mitigate the effects of the tariffs is negotiations between Brussels and Washington. Brussels would be open to negotiations with Donald Trump without conditions, and it is still hoping to find a negotiated solution. So far, however, Trump has reacted to the proposal from Brussels as was expected of him: "… They want to negotiate a deal. That's possible if we can get something for the deal," said Trump. "… We can do something if we can get something in return."[8]

The second option is to relocate the production of some sectors that are heavily affected by import duties to the United States. As Trump said, "If you build your car in the USA, there will be no tariffs."[9] If the German car manufacturers could produce the exported quantity of cars in the US, German car manufacturers, who previously produced the majority of their cars in Germany or Mexico, can now relocate their production to the US to compensate for the loss of profits caused by the import duties. In this context, not only car manufacturers in the domestic market are affected, but also their partners in Mexico. Around 1,900 German companies are located in Mexico, producing and exporting goods to the US market, which will also be affected by the trade war.

However, in the case of relocating car production from Germany to the US, this would have an important effect on the German economy. First, the relocation of car production from Germany to the US will undoubtedly lead to high unemployment in the car industry, a significant reduction in car production, and a decline in Germany's growth rate in the short run. This disturbing development is

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[6] Simon Schütz, "VDA statement regarding planned US tariffs on imported cars," VDA, Berlin, March 27, 2025, https://www.vda.de/en/press/press-releases/2025/250327_VDA_statement_regarding_planned_punitive_tariffs_on_imported_cars.

[7] Ibid.

[8] Wenn wir etwas dafür bekommen" – Trump zeigt sich offen für „Deals" über Zölle, MSN. https://www.msn.com/de-de/finanzen/top-stories/wenn-wir-etwas-daf%C3%BCr-bekommen-trump-zeigt-sich-offen-f%C3%BCr-deals-%C3%BCber-z%C3%B6lle/ar-AA1BSycH

[9] Rob Vile, "Trump to impose 25% tariff on all imported vehicles and foreign-made auto parts," NBC News, March 26, 2025, https://www.nbcnews.com/business/autos/trump-auto-tariffs-which-companies-how-much-when-what-to-know-rcna198223.

all the more serious when one considers that around 70% of jobs in the automotive industry in Germany depend on exports. This is a very big problem with major unpredictable consequences for the German economy.[10]

The third option is to search for alternative export markets to ensure the survival of the automotive industry. Under this strategy, car manufacturers must discover new markets and expand their current market share in the global economy. In the past, China was one such potential market for German car companies. While the Chinese car market grew by around 3 percent in the first nine months of 2024, deliveries by all three German companies fell by an average of 12 percent.[11] China now produces 60 percent of the world's electric cars—many of them its own brands—and 80 percent of the batteries that power them.[12] Today, however, China is emerging as a new power in the automobile industry. Their share of the Chinese car market will rise from just 5.4 percent in 2020 to 32 percent in 2023, and it will reach 39 percent of cars sold from January to September 2024—and domestic carmakers are meeting the bulk of this demand.[13] China is revolutionizing car production, which has put the mighty German car manufacturers under intense pressure and fierce competition. In other words, the German car industry is caught between two fronts: being severely challenged from American import tariffs and Chinese competition.[14]

4. What Does Trump Expect from the Trade War?

On the one hand, Trump has said that this "day of liberation" is one of the most important days in the history of the US. He hopes to boost his popularity with the American people, claiming that "The golden age of the USA is returning." As a first step, Trump's trade policy aims to reduce the enormous public deficits, including foreign and domestic debts. He is particularly targeting countries with

[10] "VDA President Müller calls for comprehensive economic reforms," VDA Berlin, January 21, 2025, https://www.vda.de/en/press/press-releases/2025/250121_PM_Jahrespressekonferenz_2025_EN.
[11] Alexander Brown and Andreas Mischer, "German Carmakers Are Placing a Risky Bet on China," The Diplomat, December 9,2024, https://thediplomat.com/2024/12/german-carmakers-are-placing-a-risky-bet-on-china/.
[12] Ibid.
[13] Ibid.
[14] John Sudworth, "Why Trump is hitting China on trade - and what might happen next," BBC, April 9, 2025, https://www.bbc.com/news/articles/c9qwwe9rdwlo.

high trade surpluses with the US. He has described these countries as the “worst offenders” in the trade war. [15]

President Trump is known as an advocate of protectionism. He favors protecting the domestic economy, even at the expense of other countries, and discriminating against foreign competitors in the domestic market to allow US companies to compete better. This sort of protectionism is referred as a “beggar my neighbor” policy.

This argument assumes that countries that lose export sales and production will not retaliate and that foreign governments will remain silent and take no countermeasures. Retaliation in the form of protectionist measures directed against US exports would mean that neither country would achieve production or employment gains and both countries would lose effectiveness.

However, contrary to Trump’s strategy, in addition to the European Union, Canada, Mexico, and China, have announced countermeasures and “counter-tariffs” on imports from the US. It can be assumed that neighboring countries will continue to react strongly to the restrictions imposed on them. It is argued that protectionism is a desirable way of increasing output and employment in the domestic market, because of the multiplier effect of reduced imports. However, as Australian Prime Minister Anthony Albanese pointed out, “tariffs and escalating trade tensions are a form of economic self-harm and a recipe for lower growth and higher inflation. The costs will be paid by households.”[16]

After fierce opposition inside and outside America against his trade policy, Trump needed a temporary break from the trade war. Following the April 2 announcement, stocks in the US, Europe, and Asia fell sharply, reflecting concerns that the tariffs will slow economic growth and fuel inflation, initially leading to a global recession. According to Trump, more than 75 countries have reached out to US officials to discuss and negotiate following the imposition of his global “reciprocal tariffs,” which he suspended for 90 days.

Recently, something unexpected has happened. The Trump administration has temporarily exempted smartphones, computers, and some other electronic devices from the "reciprocal" tariffs, which include a 125 percent duty on imports

[15] Natalie Sherman, “Trump to charge high tariffs on 'worst offenders' globally,” BBC, April 3, 2025,. https://www.bbc.com/news/articles/cm257z1y2q9o.

[16] “As Trump dashes its hopes for tariff relief, Australia rejects retaliation,” *South China Morning Post*, March 12, 2025, https://www.scmp.com/news/asia/australasia/article/3302022/trump-dashes-its-hopes-tariff-relief-australia-rejects-retaliation.

from China. This is a clear indication that Trump could easily change his mind about implementing tariffs if he were to be convinced at the right time and under the right conditions. On the other hand, Trump understands that tariffs as an instrument in domestic and foreign policy. Washington is using the tariffs to put pressure on other countries facing trade surpluses to gain advantages in political, economic, and security negotiations and to achieve results favoring Washington.

5. An Overview of German Economy in 2025

The trade relations between the US and the EU and Germany are likely to continue to decline, and dramatic changes could be on the horizon, particularly with regard to further trade tariffs. The extent of the damage caused by a trade war will, of course, depend on the current economic stability and adjustment capacity of the German economy. In light of these tariffs and their effects on the European economy, the following questions arise: where does the German economy stand today? What impacts will Trump's trade policy have on the German economy? How will Germany deal with these trade policy challenges in the coming years? It will therefore be worth looking at the forecasts of the leading international research institutes for the German economy in 2025.

German Economy in Recession

A pessimistic scenario for the German economy in 2025 has been developed by the Kiel Institute for the World Economy (IfW).[17] According to the IfW report, the German economy is stuck in a state of recession. It appears that the economic situation is not going to improve much. There is little prospect of an improvement in economic activity in the short term, as there are increasing signs that economic weakness is structural rather than temporary.[18]

If US President Donald Trump follows through on his protectionist trade policies, as assumed in this forecast and has indeed already done, German exports will continue to be under pressure. This is because economic activity is weighed down by high uncertainty and weak external demand. The expected US tariffs and the worsening crisis in German industry are the main reasons for the downward revision of economic growth rates. GDP is expected to contract by 0.2 percent this

[17] "Kiel Institute winter forecast: German economy likely to stagnate in 2025," IfW Kiel, December 12, 2024, https://www.ifw-kiel.de/publications/news/kiel-institute-winter-forecast-german-economy-likely-to-stagnate-in-2025/.
[18] Ibid

year. Meanwhile, the OECD estimates the same growth rate for Germany in 2025.[19] Exports will be on a gradual recovery path as demand from the main trading partners picks up.

6. Impacts of the Trade War on the German Economy

Calculations by the Institute der deutschen Wirtschaft (IW) show the extent to which Trump's punitive tariffs could have a negative impact on the German economy as a whole. Economists estimate the damage over the four-year term of office at between EUR 130 billion and EUR 180 billion, depending on the scenario. That would be equivalent to four percent of Germany's total economic output (considering a 10-percent to 20-percent tariff on imports from Europe to the United States).[20] The IFO Institute for Economic Research in Munich estimates that German exports to the US could fall by around 15 percent as a result of the tariffs.[21]

The first negative effects of the trade war can be seen in the stock and currency markets. New US punitive tariffs are dampening the atmosphere on the stock markets in Europe and the US, including heavy losses in technology stocks Investors' concerns about an escalation of the trade dispute between the EU and the US have led to a rapid rise in the price of gold and pushed the euro to its lowest level since November 2022.[22]

The decline in America's importance as a direct export market for Germany gives rise to the following new challenges and proposed solutions. First, German policymakers need to rebalance their own economy. They need to put greater weight on domestic demand and reduce dependence on exports for growth.

Second, as stated by Bundesbank President Joachim Nagel at the presentation of the Bundesbank's new forecast for Germany, "The German economy is struggling

[19] "OECD Interim Economic Outlook," OECD, March 17, 2025, https://www.oecd.org/en/publications/oecd-economic-outlook-interim-report-march-2025_89af4857-en.html.
[20] "'Ökonomisch schwierigster Moment,'" Tagesschau, November 6, 2024, https://www.tagesschau.de/wirtschaft/weltwirtschaft/trump-us-wahl-folgen-deutschland-protektionismus-100.html.
[21] Doloresz Katanich, "Germany versus the 'Tariff' Man: How Trump could make it lose out," Euro news, November 14, 2024, https://www.euronews.com/business/2024/11/14/germany-is-facing-the-tariff-man-how-europes-biggest-economy-could-lose-out-under-trump-pl.
[22] "Handelskrieg in vollem Gange – Börsen sacken ab, Gold im Aufwind," TGR, April 3, 2025, https://www.rainews.it/tgr/tagesschau/articoli/2025/04/handelskrieg-in-vollem-gange--borsen-sacken-ab-gold-im-aufwind-12a0ee72-c810-47b3-8b36-cdd5a808a5dd.html.

not only with persistent economic headwinds but also with structural problems."[23] Therefore, the German government must pay more attention to structural reforms in order to overcome the weaknesses of the German economy, such as low industrial dynamism, low innovation, low investment, and low productivity growth, and to restore the country's stability and competitiveness in international markets.

In the same context, Mario Draghi, former President of the European Central Bank, presented his report on the future of European competitiveness to the European Parliament on September 17, 2024.[24] In this report, Draghi clearly sets out Europe's economic and institutional weaknesses and makes recommendations on how Europe can finance and coordinate its policies in order to avoid falling behind on the world stage. Overall, he assesses that Europe's economic future is in serious danger. To overcome this danger, Draghi calls for major reforms and a reorientation of EU policies. The aim is to keep up with Chinese and American companies in global competition.

After Germany's general election on February 23, 2025, the first task of the newly elected German government has prepared for a major shift in the economy. This renewed focus on the economy comes at a time of heightened trade tensions and growing uncertainty about the global economy. In order to give the German economy new impetus and make it more self-sufficient, the new Federal Government has presented a comprehensive growth initiative so that Germany can overcome the two-year recession and increase its competitiveness and prosperity.

The OECD has also recommended the same approaches:[25]

(1) The new political measures focus on the following areas: Financing the EUR 500-billion program for infrastructure and climate protection, the easing of the debt brake for defense, and tax reform as tax relief for citizens and companies by improving financing options, especially for young, dynamic companies. The main aim is to stimulate private consumption and investment—domestic demand—with

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[23] "Forecast for Germany: significantly gloomier growth outlook," Deutsche Bundes Bank, December 13, 2024, https://www.bundesbank.de/en/tasks/topics/forecast-for-germany-significantly-gloomier-growth-outlook-947724.
[24] "The Draghi report on EU competitiveness," European Commission, https://commission.europa.eu/topics/eu-competitiveness/draghi-report_en.
[25] "OECD Economic Outlook, Germany," OECD, December 4, 2024, https://www.oecd.org/en/publications/oecd-economic-outlook-volume-2024-issue-2_d8814e8b-en/full-report/germany_0686f49c.html#indicator-d1e6629-b07c47d29f.

the help of a demand-oriented Keynesian approach in the years 2025–2026 in order to overcome the recession.[26]

(2) More investment to support growth and promote the green and digital transitions. Particular attention will be paid to structural reforms and promoting the innovation economy through research activities.

(3) Investment agreements, in cooperation with Brussels—for example with India, Australia, and several Southeast Asian countries, as well as deeper trade relations with African countries—seem more important than ever due to the current US tariff policy. The Germans hope this will help to free Germany from American dominance and make it more independent.[27]

7. Conclusion

There are currently two political options for the EU/Germany on the agenda. Brussels should start negotiations with Washington to reach an acceptable and efficient tariff for both sides. The EU/Germany still hopes to find a negotiated solution with the US. As the President of the European Commission Ursula von Leyen has emphasized, "At the same time, it must also be clear: Europe did not start this confrontation. We do not necessarily want to retaliate, but we have a strong plan to retaliate if necessary."[28] In other words, Brussels will have to prepare a "strong plan for retaliation" against Trump's tariffs.[29] Olaf Scholz stated that Europe was "focusing on cooperation, not confrontation" and asserted that "Europe will respond to the US decision with unity, strength and in an appropriate manner."[30]

Past events show that there is a great deal of mistrust toward Trump in Berlin and Brussels. For example, former German Chancellor Angela Merkel emphasized in her memoirs that "With Trump, there would be no joint work for a networked world.

[26] Ibid.

[27] Tim Ross and Nette Nöstlinger, "Germany's Merz vows 'independence' from Trump's America, warning NATO may soon be dead," Politico, February 23, 2025, https://www.politico.eu/article/friedrich-merz-germany-election-united-states-donald-trump-nato/

[28] Tim Haines, "European Commission President: 'We Are Open To Negotiations' On Tariffs, 'Europe Holds A Lot Of Cards'," Real Clear Politics, April 1, 2025, https://www.realclearpolitics.com/video/2025/04/01/european_commission_president_we_are_open_to_negotiation_with_us_on_tariffs.html.

[29] Ibid.

[30] "Die gesamte Weltwirtschaft wird leiden": Scholz wirft Trump „Anschlag" auf die Handelsordnung vor," Tagesspiegel, April 3, 2025, https://www.tagesspiegel.de/politik/die-gesamte-weltwirtschaft-wird-leiden-scholz-wirft-trump-anschlag-auf-die-handelsordnung-vor-13479082.html.

He judged everything from the perspective of the property entrepreneur he had been before politics. He did not believe that cooperation could promote prosperity for all."[31] Therefore, any negotiations will likely involve a sort of give and take approach.

The second option would be close cooperation and the immediate start of trade negotiations between China and Indo-Pacific economies and EU/Germany: it seems necessary for the two economic giants to work together during the trade war triggered by Trump and create a counter-bloc and a free trade order against the American tariff offensive. This would strengthen trade relations through regional trade between the European Single Market and the Regional Comprehensive Economic Partnership (RCEP). The intensifying of regional transactions will reduce dependence on the US as much as possible.

However, even if the higher US tariffs hurt the Chinese export economy by making Chinese goods more expensive and therefore less competitive in the US market, Europeans need to be aware that China is the world's largest manufacturing country, producing far more than its population consumes domestically (over capacity). Therefore, export prices can be kept lower than in the international markets (damping prices). Instead, China will try to expand its market share, particularly in Europe and the Indo-Pacific region. China's potential export offensive to Europe would also challenge the German economy and significantly increase competitive pressure on Europeans and Germany.

If Washington is not ready to accept international cooperation to stop its trade war, we will enter a new phase in trade relations. The US will be largely isolated from the global market, and its role will be significantly reduced. The world economy will be divided into two parts: the US and its close allies, on the one hand, and the rest of the world economy, on the other.

The trade war between the United States and European Union/Germany and the conflict between China and the United States will put significant pressure not only on Germany but also on the 27-member states of the EU, which have different national economic and security interests with Washington and Beijing. If they are divided and pursue their own national interests and take sides, the European Union

[31] Angela Merkel, *Freiheit* (Kiepenheuer & Witsch, 2024), 630–31.

will be an absolute loser. In the worst-case scenario, Trump could use “the law of the stronger” rather than “the rule of law” to put pressure on divided Europeans and win them over to his side in order to mobilize Washington’s economic and security policy against the “greatest threat, China.”

Nevertheless, not matter the outcome of the trade war, it is time for the European Union and Germany to realize its ambitions and strengthen its role in transatlantic and Indo-Pacific relations. Only a united and independent Europe and Germany together—strong economically, politically, and in terms of security—can create a balance of power between the United States and China in the global economy.

APPENDIX

Trump’s Import Tariffs Announcements[32]

February 1: The president announces a 25% tax on Canadian and Mexican exports to the US—and an additional 10% on China
February 3: Mexico and Canada reach a deal to pause US tariffs for one month
February 10: Trump announces a 25% import tax on all steel and aluminum entering the US
March 4: The White House increases the tariff for Chinese imports to 20%
March 5: Trump temporarily exempts carmakers from the 25% tax imposed on Canada and Mexico
March 7: Trump expands the range of goods exempted from the Canada and Mexico tariffs
March 12: The 25% steel and aluminum tariffs take effect
March 26: The White House announces 25% duties on cars that will apply from April 2 and on car parts at a later date but before May 3
April 2: Trump says the US will impose “reciprocal tariffs” of up to 50% on certain countries and 10% on imports from all other countries
April 5: The 10% tariffs take effect

[32] Jennifer Clarke, “What are tariffs and why is Trump using them?” BBC, April 14, 2025, https://www.bbc.com/news/articles/cn93e12rypgo.

April 9: Tariffs on roughly 60 countries—described by the US president as the "worst offenders"—are introduced. Trump later announces a 90-day pause, during which the 10% "baseline" rate will be paid, excluding China, for which an 125% tariff is applied

April 10: China's retaliatory 84% levy on US goods takes effect. The White House says tariffs on China would reach 145% for some products due to a previous 20% levy for those producing the drug fentanyl

April 11: China sets tariffs on US imports at 125% from April 12. It says it will not respond to any further US tariffs, saying they will become a "joke."

There are a number of exemptions to the tariffs announced.

For example, goods in small parcels sent from China that are worth less than USD 800 (GBP 624) are not included until May 2. These will have a duty rate of 90% or USD 75 per item—increasing to USD 150 per item after June 1.

The "baseline" 10% rate does not apply to Canada and Mexico. There have been a number of exemptions and delays since Trump announced they would face tariffs of 25% on most goods and 10% on Canadian energy.