Economic view

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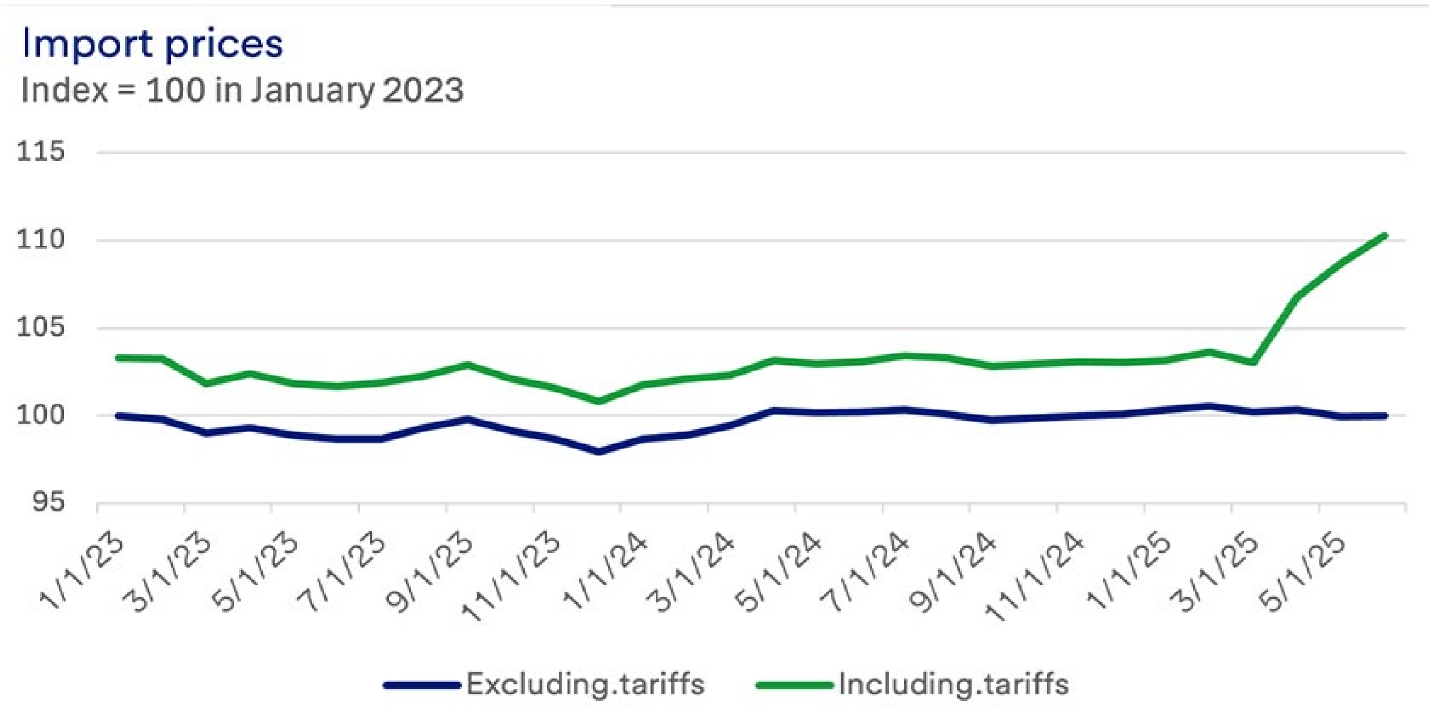
From the desk of Chief Economist Beth Ann Bovino

Who is picking up the tab?

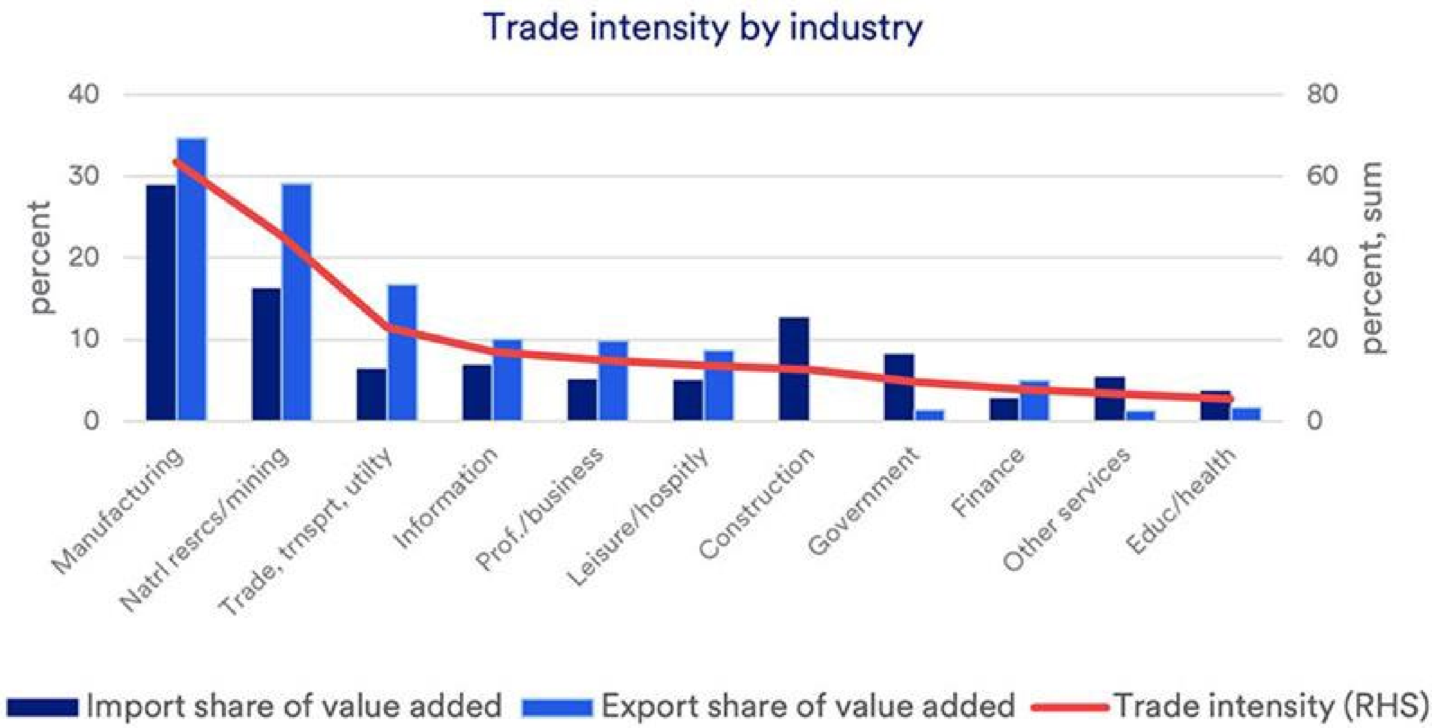
As the tariff pause nears its end, who will cover the tab of higher tariffs? We expect the effective tariff rate to settle at around 16% when all is said and done, over six times its pre-election 2.5% rate. The White House insists that the rest of the world will carry the load by cutting their prices to keep foreign customers. But, so far, the data points in the opposite direction. Americans are picking up the bill.

As in the past, most foreign businesses appear to be layering a U.S. tariff cost on top of their price. Import prices, including tariffs, surged since March. If foreign businesses were absorbing these tariffs, import prices before tariffs would have declined to protect market share. But import prices excluding tariffs haven't moved much – and certainly not enough to capture the size of tariffs captured since President Trump started the tariff wars. While some foreign suppliers may be covering the cost, most of the load has been left to the American private sector.

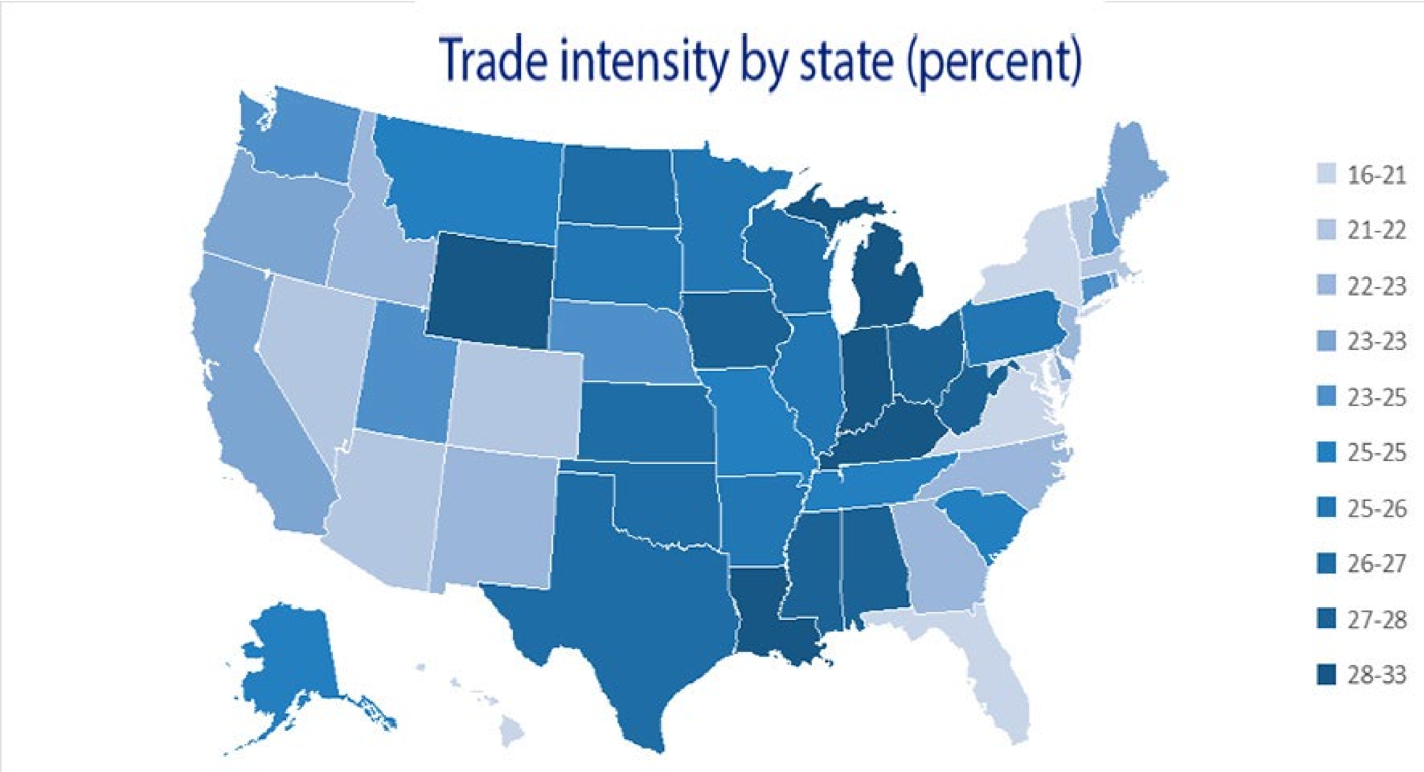


So far, American firms have been covering the tab. The core Producer Prices Index fell from 3.2% to 2.7% in June, but that was largely driven by a large drop in the services component. Finished goods, less food and energy – which is impacted by tariffs – have already climbed from 2.3% in March to 2.7% in June, as they eat costs to hold onto customers. By allowing some compression in margins, they keep their customers, with the expectations that this pain-point will be short. They also seemed to have used inventories bought before tariffs, but eventually these inventories will need to be restocked at a higher price.

Using data from the four largest retailers in the U.S. from February through July, research showed that the price of imported goods has risen sharply (“). While domestic goods have also increased, it was “more gradual and steadier,” and likely due to the reliance of U.S.-made products relying on imported components that are subject to new tariffs.



By industry, according to a paper by the Chicago Fed, manufacturers are the most exposed to the trade dispute, with a trade intensity of 63.6%, followed by natural resources & mining at 45.4% (“” June, 2025). Manufacturing’s top billing help explain why they are depressed, with the recent ISM and S&P Global PMI U.S. manufacturing surveys in contraction territory. Excluding construction, the service sectors all have much lower trade intensities. The authors found that states in the middle of the country trade the most because their industries are concentrated in manufacturing and/or natural resources and mining, and they expect those states to feel the largest impact from the trade war.



Eventually consumers will be stuck with the tab.

As has happened in the past (including the trade dispute with China under the first Trump administration), we expect a complete pass-through of tariffs as the costs of tariffs are eventually transferred to consumers in the form of higher prices over time.

It may have just started. Procter & Gamble announced that the tariff policy is causing it to push through price hikes to shoppers to protect its profit margins. And June consumer inflation data may have been the first month with signs of tariff pass-through, with prices of goods directly exposed to tariffs – such as household furnishings, appliances, clothing, electronics and furniture – showing larger increases than not. However, the weak July job gains with sharp downward revisions in prior months, together with other signs that the private sector spending and investment has slowed, leaves the Fed in a bind.

Tension between the two mandates – stable prices and maximum employment – has increased. Still, signs of tariff-driven inflation will make it difficult for the Fed to cut in September, especially since the unemployment rate remains low. But the dual dissents at the July FOMC meeting highlight the internal (and external) pressure for easing, with the disappointing July jobs report (in part driven by DOGE layoffs and tighter immigration), challenges the Fed's decision to stick to their 'wait-and-see' approach.

Still, the Fed may point to their playbook, that when the two mandates are in tension, the Fed targets the one farther away from their target. Given inflation is much further away from its 2.0% target than the unemployment rate, the Fed may still be able to wait another month before they cut rates. But external pressure after the weak jobs report could very well force their hand.

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