Opening Statement – Joint Committee on Finance, Public Expenditure, Public Service Reform and Digitalisation and Taoiseach

'Impact of Tariffs on the Irish Economy and Related Policy Discussion'

Dr Tom McDonnell,

Co-director, Nevin Economic Research Institute, TUREC Network

16/07/2025

1. Introduction

First of all I would like to thank the Cathaoirleach, and members and staff of the Committee for the invitation to appear before you.

My name is Tom McDonnell. I am Co-director of the Nevin Economic Research Institute (NERI) and I am grateful for the opportunity to present our views on tariffs.

While the final landing point for the US tariffs is uncertain, the minimum we can expect is 10% on most goods, and there is a significant possibility of larger rates potentially varying by sector and potentially including services depending on how the EU responds to the US provocations.

2. Domestic US motivations and expectations

In attempting to understand how events might play out, we first need to understand the motivations of the US administration.

In essence, alongside its value as a bargaining tool and lever for political pressure the administration's four arguments justifying tariffs are[1]:

[1] A 5th justification for tariffs, albeit not relevant in the US context, relates to development economics. Tariffs can be used to support catch-up industrialisation and to facilitate learning, imitation and improvement. They

1. That tariffs will lower import prices (before tariffs are counted) thereby shifting costs onto foreign producers, and improving the US terms-of-trade in a welfare improving way for the US
2. That tariffs will lead to a relocation of manufacturing production to the US which will boost domestic employment including the *quality* of domestic employment
3. That tariff revenues will allow the US administration to reduce taxes in other areas, for example taxes on income or taxes on corporate profits
4. That tariff revenues will reduce trade deficits with foreign countries which is something they perceive as a security issue.

Tariffs are not an inherently leftwing or rightwing policy and are supported by many progressives in the US. Whether a tariff (or industrial subsidy) is progressive or not depends on the role it plays in the overall development strategy and they can legitimately be used to counterbalance imperfect competition or where a country has lost ground in global competition (see Footnote 1).

3. Likely impacts on the US and trading partners

However, as it happens, the likely impacts are very different from those anticipated by the US administration. Economic theory suggests that import tariffs have a number of economic transmissions (see Table 1 in the Appendix for descriptions) and that the outcomes will include weaker domestic and trade partner GDP, potential improvements to the trade balance conditional on exchange rate movements, and ultimately weaker average productivity as

were very successfully used by the so-called East Asian Tiger economies as part of their development strategies in the 20th century. Development economists are often in favour of temporary and selective tariffs in sectors they want to build or make competitive although only for a specific time period.

market share shifts away from the most productive exporting firms to less productive domestic firms.

In addition, empirical studies consistently reveal negative impacts from tariffs. Based on the literature the outcomes we can expect are:

A. **Prices will increase in the US.** For example, research finds that the 2018 US tariffs lead to a near complete pass-through to import prices. In other words, the tax incidence was absorbed by US retailers and US consumers rather than by foreign importers cutting their prices.
B. **Economic output and productivity will fall on both sides.** This is due to resource misallocation and to reduced competition and innovation in the tariff imposing country, and due to falling demand in the country facing the tariff. Real exchange appreciation is *generally* expected to occur in the tariff imposing country which would then strain its export sectors.[2] The expectation is that certain sectors would benefit but that overall welfare would decline.
C. **Unemployment and inequality will rise** in the tariff imposing country due to the introduction of a regressive tax on imported goods and the decline in real incomes and aggregate demand. Unemployment will also rise in the countries facing the tariff due to the reduction in external demand.
D. **Global value chains will fragment and supply costs will be disrupted as will trade flows.** This will erode efficiencies and competitiveness and ultimately productivity. Exports and imports will both shrink.

[2] However, it is important to note that this effect has not manifested thus far with the dollar depreciating this year against a basket of major currencies. There was a sell-off in US financial assets in April along with a decline in investor sentiment towards the US. The weakening dollar adds to inflationary pressures but does make US goods cheaper and exports more competitive.

E. The uncertain nature of the tariffs i.e. permanent or temporary or subject to negotiation will lead to **a slowdown in business investment** which will reduce employment in the short-run and productivity in the long-run.

A further issue to consider is the extent of diverted exports from tariff-hit countries. For example, diverted goods from China risk flooding the EU market. Overall, protectionism is expected to distort production and resource allocation, to erode competitiveness, and ultimately generate welfare losses on both sides. These effects are magnified if the affected countries retaliate.

Research from the TUREC network[3] (IMK Germany), of which the NERI is a member, used the NiGEM model to estimate impacts on the US of various tariff scenarios. The results showed higher inflation, declining domestic demand and falling imports and exports with harmful effects dominating overall in the US, and to a lesser extent in trade partners. Reciprocal tariffs will have analogous impacts on the country or bloc imposing tariffs with actual results depending on the extent and nature of the trade relationship.

We can think of tariffs as imposing 4 shocks to the US and other economies. The 1st shock is the direct impact of the tariffs themselves including distortions to existing supply chains, shifts in demand, and lower average productivity and job losses over the medium-term. The 2nd tariff shock is the inflation effect specifically the higher prices which research indicates will ultimately be borne by consumers in the tariff imposing countries and which reduces their purchasing power. The higher inflation is also expected to cause a monetary policy reaction, leading to higher interest rates and to negative GDP and employment effects.

[3] Presented by Theobald at TUREC Conference (Vienna, June 2025)

The 3rd and 4th shocks are linked to uncertainty and loss of confidence. The erratic, inconsistent and unreliable behaviour of the current US administration is causing significant economic uncertainty. A mix of increased uncertainty and higher expected inflation are combining to increase the term premium on US treasury bonds as well as the cost of corporate credit.[4] The IMF estimates that uncertainty shocks could double the negative effect of direct tariff rate shocks, with investment plans in abeyance until the period of uncertainty ends.

A loss of confidence can have a number of impacts. Most obvious are an increase in precautionary saving and a decline in household consumption and business investment. Confidence effects are non-linear and come with tipping points. A full blown trade war could precipitate an abrupt loss of confidence in the US, and a recession, which in turn would further damage exports to that country particularly for non-necessities and substitutable goods.

4. Impact on Ireland

Ireland is one of the most highly globalised economies in the world. It has significant two way linkages with the US economy and is itself the most exposed economy to tariffs within the EU relative to its size. The US maintains a large trade deficit in goods with Ireland (the 4th largest in the world). The €72 billion in goods exports to the US last year (see Table 2 in Appendix for a breakdown) was the 2nd largest in the EU and four times that of Spain.[5] Ireland's exposure to the US was illustrated by the surge in exports and in GDP in advance and in expectation of the US tariff announcements.

---

[4] NIGEM research (reported by Theobald, TUREC Conference) suggests a 100 basis point increase in the cost of government borrowing will reduce GDP by circa 0.45% relative to baseline and a 100 basis point increase in the cost of corporate credit will reduce GDP by circa 0.5% relative to baseline.

[5] German goods exports were €161.2 billion, Irish goods exports were €72.1 billion and Italian goods exports were €64.8billion.

The US is the top export destination for the EU (20.6%)[6] with goods exports making up 61% of the total[7] and with a goods export surplus of €198 billion in 2024. Germany, Italy and Ireland have a combined share of 55% of Member State (MS) goods exports to the US explaining their relatively dovish stances in the trade negotiations. However, much of the Irish exports are actually US multinationals operating out of Ireland and re-exporting goods to the US. The exports are highly concentrated with €58 billion in pharmaceuticals and chemicals. The US makes up 53.7% of extra EU exports, which is more than double the percentage for any other EU country.

The proposed tariff increases[8] and potential reciprocal escalation are therefore a potentially game changing threat to the Irish economic model. Tariffs reduce trade and disproportionately affect small open economies (SOEs). Uncertainty around the timing, scale and extent of tariffs will likely slow investment location decisions until such time as there is greater policy clarity.

The large trade surplus in the pharmaceutical sector makes it a particular target for the Trump administration. While it is possible that jobs could be moved to the US in order to circumvent tariffs, the practicalities of this are not particularly feasible in the short-term. Relocating pharmaceutical plants to the US could take 5 to 10 years, and hopefully the tariffs will be long gone by then. It is a highly specialised sector with complex supply chains that needs a skilled workforce. More realistic is the loss of future foreign direct investment (FDI) and slower employment growth. In addition, multinationals may choose to shift intra-company payments to reduce their tariff exposure. This would reduce corporate profits in Ireland. Overall, pharmaceutical companies may

[6] Galgoczi (2025, TUREC Conference, Vienna)
[7] Of this, Machinery & Equipment makes up 38.8% and Chemicals 32.1%
[8] Future corporation tax changes in the US and/or the collapse of the OECD BEPS process represent further potential challenges to the Irish economic model.

shift some production to the US over the medium-term in order to serve that market, but uncertainty over whether tariffs will outlast the Trump presidency might induce companies to reasonably take a wait and see approach.

The actual sectoral impacts of the tariffs will depend on the characteristics of the good in question. Inelastic essential goods with limited substitutes such as many pharmaceutical goods and medical instruments are unlikely to see much reduction in export volume in the short-run, whereas elastic non-essential goods with easy substitutes such as dairy (butter), beef[9] and alcohol are likely to see much more significant reductions in their export volumes and in the prices that producers can obtain. Short-run job losses are therefore more likely in food and drink than in pharmaceuticals, and indeed this is where we expect job losses to occur.

Escalation of a trade war would further expose the Irish economy. For example, a different tariff than obtains for Northern Ireland or Scotland would create a competitive disadvantage for whisky produced in the Republic of Ireland. Escalation of protectionism to include pharmaceuticals or services would particularly hit Irish growth prospects and the future trajectory of the public finances.

Tariffs, whether unilateral 10%, reciprocal, or escalatory, will lead to higher levels of inflation, possibly inducing central banks to slow (or reverse) interest rate cuts. In addition, they will lead to reduced scope for multinationals to make profits, and might ultimately lead to slower rates of FDI and lower employment levels as well as lower corporation tax and income tax revenues. One silver lining would be higher tax receipts from the tariffs themselves.

[9] The agri-food sector exports about €2 billion in goods to the US.

The Cathaoirleach and members will of course be aware of the research done earlier this year by the ESRI[10] showing projected declines relative to a no tariff baseline for GDP and modified domestic demand, and declines for employment and for consumption, alongside increases in prices and in government debt. After four years a permanent 10% reciprocal tariff reduces employment by 1.9%, modified domestic demand by 1.3% and consumption by 2.4% while prices rise 0.2% and government debt rises by 0.9%.[11] While these effects are significant (circa 50,000 less net new jobs) it is also worth emphasising that the projections are for slower growth in output and employment but not necessarily for an actual recession.

Similarly, analysis earlier this year from the Aston school (Du and Shepotylo, 2025)[12] based on a global and reciprocal 25% tariff found there would be significant declines in welfare in Ireland. Finally, Galgoczi (TUREC conference) estimates that a 20% tariff on EU goods exports would put 720,000 EU jobs at risk with the overwhelming majority in manufacturing.

5. Policy response

A standard analysis from a trade economist would suggest the Irish government and the EU should seek to de-escalate the situation as much as possible and to seek to prevent the extension of tariffs to services including indirectly via the anti-coercion instrument. There are differential impacts across the EU – both sectoral and regional – and Ireland is very much exposed.

---

[10] Egan, P. and Roche, F. (2025) The impact of de-globalisation and protectionism on a small open economy.
[11] All estimates are relative to a no tariff baseline
[12] Du, J. and Shepotylo, O. (2025) Tariffs and triumph: The UK's edge in a fractured world.

In contrast, a behavioural economist or game theorist might suggest going toe-to-toe with the Trump administration in the short-run, in order to get a better deal in the longer-term. The EU has clout due to its market size but also dependence on the US which puts it in a weaker position than China. A 'TACO' strategy that assumes Trump will always back down is understandable, but also obviously very risky, and it could induce a global recession.

Were this to happen, and were it deemed to be temporary, than an EU wide response to preserve productive capacity akin to a scaled down Covid response (e.g. SURE or an expanded EGF) would be appropriate. Ideally, such a response would be sector specific and, if done, ought to be tied to social conditionality. It will be important to broaden sectoral dialogues and build sectoral taskforces for the affected sectors. In addition, monetary and fiscal policy would need to be proactive and supportive. However, such a response can only be a holding position.

What governments should not do, is use a crisis to rush towards a 'competitiveness' agenda that undermines workers rights. Such an approach is a developmental dead end. The NERI has been working on an alternative policy suite or 'New Economic Model' which we would be happy to discuss with the Committee either now or at a later date.

In short, reciprocal tariffs will further damage the EU and Irish economies but there may nevertheless be strategic advantages to responding in-kind. If retaliation is the decision then my personal view is that a general approach is preferable to a targeted one.

Ultimately, any deal with this administration is unlikely to be superior to that offered to the UK, which was a blanket 10% tariff on goods imports. Crucially, any deal should not be an excuse to reduce standards whether labour, environmental or otherwise.

There is a possibility of the US Congress re-exerting control of trade policy in 2027. It is important therefore that the EU signal its willingness for an in-kind de-escalation if and when the opportunity presents.

In addition, we should acknowledge that China's vertical industrial policy has proven more successful than the EU's horizontal industrial policy in recent years and that therefore a reassessment of strategy is required. The EU should also seek to align with countries in the Global South to develop a new trade policy framework.

The Irish economy has been heavily reliant on US capital compared to other high income European SOEs, and heavily reliant on US multinationals for employment and corporation tax receipts. The sustainability of this growth model is clearly in question. Going forward we need to spread our international economic relationships to a number of countries – investment, trade, supply chains – and reduce our reliance on US capital and markets – much the same way we reduced our reliance on UK markets and capital.

Indeed, the NERI's view is that the Irish economic model is going to need to evolve and be reformed if it is to be fit for purpose to endure the profound challenges it faces in the next generation.

I am happy to take any questions.

Appendix

Table 1: Economic transmissions of import tariffs (illustrative causal chains)

Causal Chains	→	→	→	→	→
Import tariffs (1)	Higher domestic import prices	Higher domestic consumer prices	Higher domestic policy interest rates	Lower domestic GDP	
Import tariffs (2)	Higher domestic import prices	Higher domestic consumer prices	Higher domestic policy interest rates	Stronger domestic currency	Weaker domestic trade balance
Import tariffs (3)	Higher domestic import prices	Lower domestic import volumes	Higher domestic GDP		
Import tariffs (4)	Higher domestic import prices	Lower domestic import volumes	Stronger domestic trade balance		
Import tariffs (5)	Higher domestic import prices	Lower domestic import volumes	Lower trade partner export volumes	Lower trade partner GDP	
Import tariffs (6)	Higher domestic import prices	Lower domestic import volumes	Lower trade partner export volumes	Weaker trade partner trade balance	
Import tariffs (7)	Higher trade partner export price	Lower trade partner export volumes	Lower trade partner GDP		
Import tariffs (8)	Higher trade partner export price	Lower trade partner export volumes	Weaker trade partner trade balance		

Notes: (1) Some of the effects are functionally equivalent (e.g. 5/7 and 6/8) but shown separately for clarity. (2) An important additional effect is falling average productivity with less productive domestic suppliers gaining market share. Trade partners also experience falling productivity as the share of exports in the economy declines and their economies pivot more towards the domestic market.

Table 2: Top 10 merchandise exports to the US

Commodity group	€, billions (US share of total)
Medicinal and pharmaceutical products	44.382 (44.4%)
Organic chemicals	9.405 (11.6%)
Professional, scientific and controlling apparatus	4.297 (40.4%)
Essential oils, perfume materials, toilet preparations etc	3.923 (33.8%)
Miscellaneous manufactured articles n.e.s.	3.115 (31.3%)
Electrical machinery, appliances etc	1.348 (11.3%)
Other transport equipment	1.086 (16.3%)
Beverages	0.904 (39.2%)
General industrial machinery and parts n.e.s.	0.623 (25.3%)
Dairy products and birds' eggs	0.613 (14.3%)