Waiting for Tariff Inflation…

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In Samuel Becket's renowned play, Vladimir and Estragon wait for Godot, who never arrives. Seems a bit like waiting for the inflation impact of recent tariff increases. But is it?

On April 2, "liberation day," the Trump Administration announced a baseline 10% tariff on most imported goods and additional "reciprocal" tariffs, quickly delayed until August, on select countries. This was on top of new tariffs on vehicles, parts, steel, aluminum, and other select commodities. I estimate that by June these initiatives increased the import-weighted average of tariff rates on all goods imports - call it the "statutory" tariff rate - by 17.5 percentage points, to 20%. At May's volume of imports, that implies an increase in the "run rate" of customs duties of nearly $600 billion at an annual rate, a staggering rise. If passed fully forward, it would lift the aggregate price level by roughly 1.7%. Yet so far, despite economists' warnings, any impact on inflation has been difficult to discern. Why?

One reason is that imports temporarily surged early this year as importers rushed to beat the anticipated increase in tariffs (Chart 1). Until the resulting excess stocks are worked down, merchants can postpone selling goods subject to the new higher tariffs, delaying price pressures arising from the recent increases. But is there even more to it than that?

So far, we can rule out the tariffs being absorbed by foreign suppliers. Chart 2 shows the price of imported goods through June, both before tariffs (as reported by the Bureau of Labor Statistics) and including customs duties collected by the US government. Since March the price of imports, including tariffs, has jumped sharply with no discernible offsetting decline in the price before tariffs. So, there's little indication here that foreign suppliers have trimmed margins to protect market share. Note, however, that since March the increase in price including tariffs is "only" 7%, far short of the 17.5% percentage point rise in the statutory tariff rate. Why?

Chart 3 compares my statutory tariff rate to the effective tariff rate defined as the ratio of payments received by the US government to total goods imports. The statutory rate jumped from 2.3% in January to above 25% in April and May, when the tariff rate against China was temporarily set at 145%, but in June slipped to 20%. Meanwhile, the effective rate has risen only the 7 percentage points reflected in the price of imports gross of tariffs. Again, why?

Chart 4 compares the calculated statutory tariff liability to customs duties received by the US government as percentages not of total imports, but of "dutiable" imports, i.e., only those imports

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that have been released from customs when they become subject to tariffs. By May the statutory tariff rate on dutiable imports jumped to 20%, but customs duties have lagged behind for at least two reasons. First, payments are not due until 15 days after the liability is assessed. As tariff liabilities increase, this delay can push some payments into the following month, slowing the rise in payments until customs duties reach a steady run rate. Second, given the uncertain legality of the tariffs, importers, perhaps hopeful the tariffs will be rescinded, may be delaying payments with reduced fear of enforcement penalties.

But the lag in payments is not nearly enough to explain the slow rise in the effective tariff rate on all imports. The difference is explained by the ability of importers to delay the release of imports from customs by storing merchandise in bonded warehouses for up to five years. As evidence of this phenomenon, Chart 5 depicts the share of imports recorded as dutiable. Before the new tariffs this share hovered near 30%. However, with the notable carve out for USMCA-compliant imports, the new tariffs apply to nearly all imported goods, not just those that previously were dutiable. I estimate that roughly 85% of goods imports are now potentially subject to tariffs, yet the actual share has risen only to 44%. The difference may be hiding temporarily in bonded warehouses.

It's likely that importers and other wholesalers are, for now, absorbing some of the increase in tariffs. But unless policy changes, there seems little doubt where this is headed. The effective tariff rate will double towards the statutory 20% rate as the share of dutiable imports rises towards 85%, implying that considerably more inflation pressure will metastasize in domestic supply chains. Furthermore, the area between the two curves in Chart 3 represents an as-of-yet unmaterialized cost that eventually will start moving forward towards final demanders. And none of this reflects the steep reciprocal tariffs that (might) go into effect in just a few weeks.

Despite the lags, evidence that the new tariffs are pushing through to price inflation is gradually emerging. For example, Chart 6 shows the 3-month change (at annualized rates) of producer prices for private capital goods and consumer durable goods, two categories of commodities with high concentrations of imports. In the 3 months since liberation day, both have moved up to exceed 4%. But with so much of the eventual costs still unrealized, it is too early to assume there's little more tariff-related inflation risk to come – or to base monetary policy on that assumption - because in my epilogue to Becket's play, Godot arrives pretty soon.

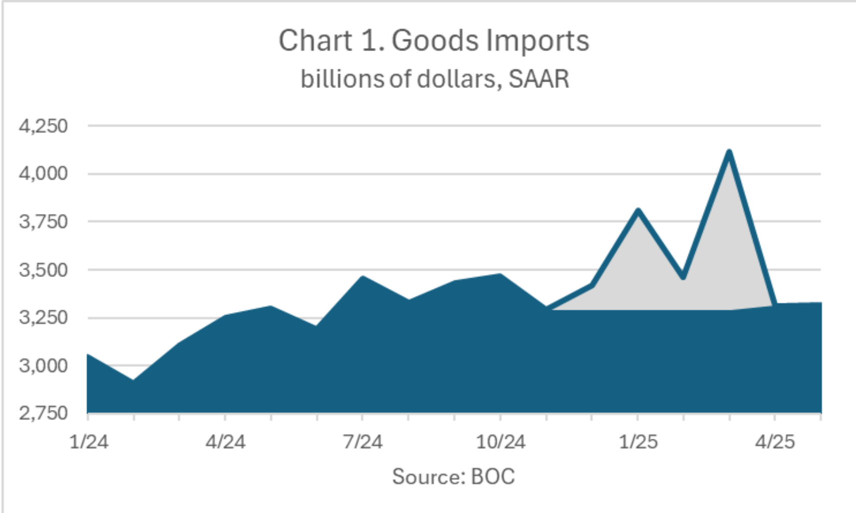
Chart 1. Goods Imports
billions of dollars, SAAR
4,250
4,000
3,750
3,500
3,250
3,000
2,750
1/24
4/24
7/24
10/24
1/25
4/25
Source: BOC

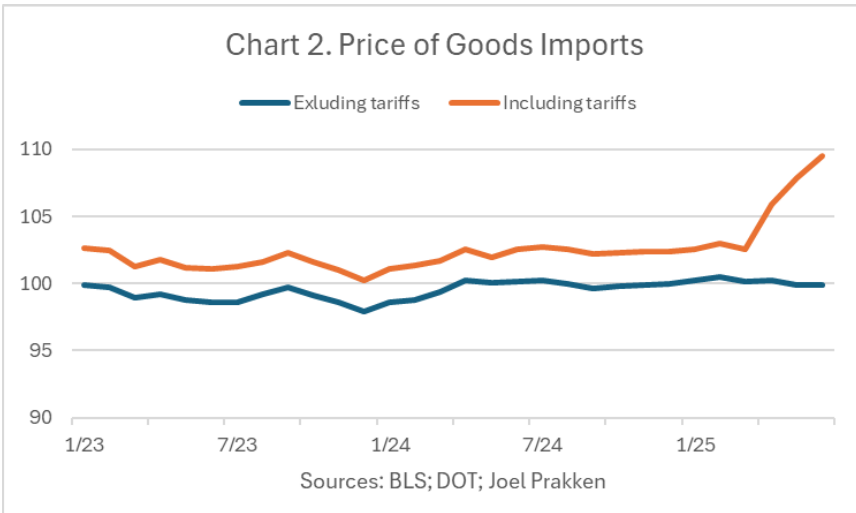
Chart 2. Price of Goods Imports
Exluding tariffs
Including tariffs
110
105
100
95
90
1/23
7/23
1/24
7/24
1/25
Sources: BLS; DOT; Joel Prakken

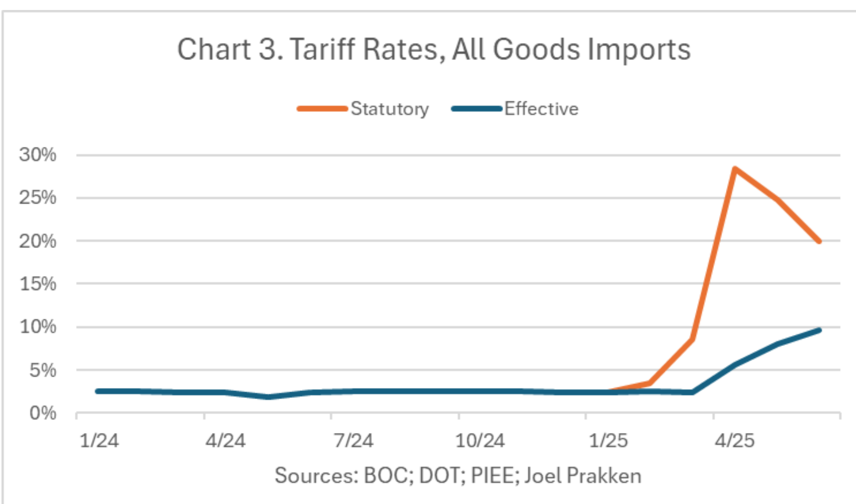
Chart 3. Tariff Rates, All Goods Imports
Statutory
Effective
30%
25%
20%
15%
10%
5%
0%
1/24
4/24
7/24
10/24
1/25
4/25
Sources: BOC; DOT; PIEE; Joel Prakken

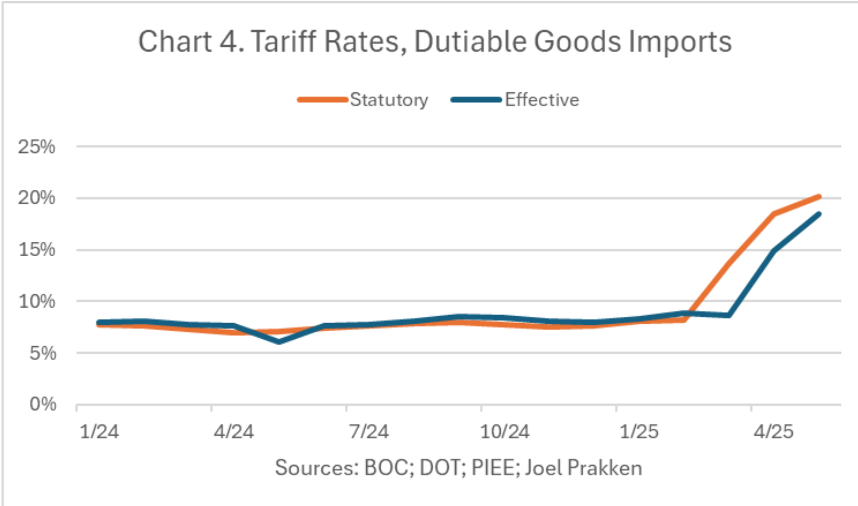
Chart 4. Tariff Rates, Dutiable Goods Imports
Statutory
Effective
25%
20%
15%
10%
5%
0%
1/24
4/24
7/24
10/24
1/25
4/25
Sources: BOC; DOT; PIEE; Joel Prakken

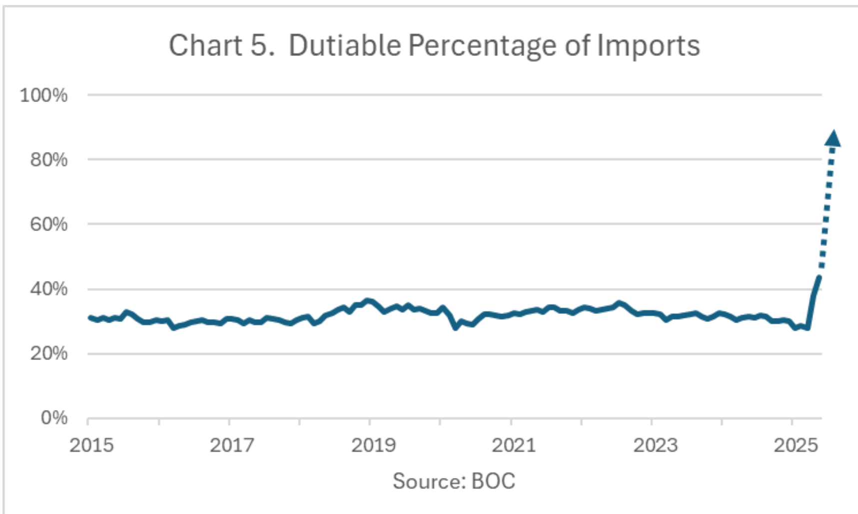
Chart 5. Dutiable Percentage of Imports
100%
80%
60%
40%
20%
0%
2015
2017
2019
2021
2023
2025
Source: BOC

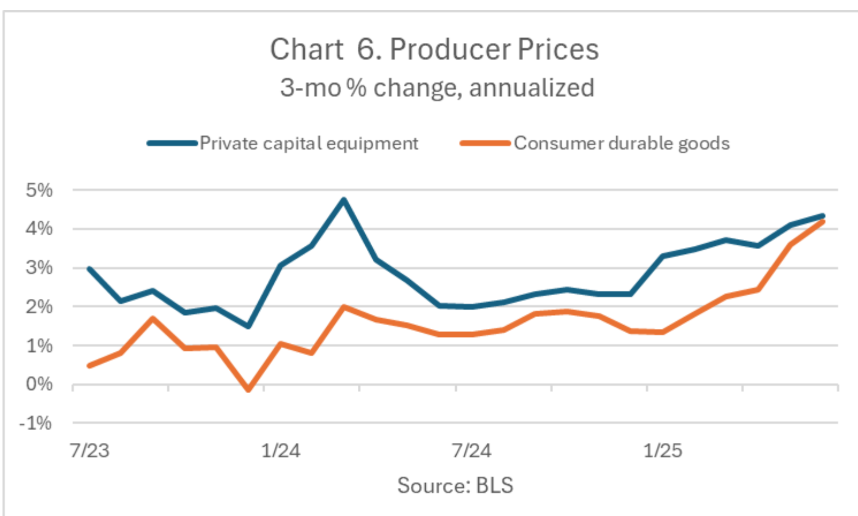
Chart 6. Producer Prices
3-mo % change, annualized
Private capital equipment
Consumer durable goods
5%
4%
3%
2%
1%
0%
-1%
7/23
1/24
7/24
1/25
Source: BLS