Economic Impacts of Trade Policy Uncertainty in the U.S.-China Trade War

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Abstract

This study examines the economic consequences of the U.S.-China trade conflict, highlighting trade policy uncertainty (TPU) as a primary driver of disruption — more so than the tariffs themselves. The Trump administration's erratic and contradictory policy actions have fostered a climate of sustained unpredictability, destabilizing conventional expectations in global trade. This uncertainty has significantly dampened business investment, constrained labor market activity, weakened consumer sentiment, and hindered innovation in both the United States and China. It has also induced structural shifts in global supply chains and altered cross-border capital flows. These effects have extended beyond the bilateral conflict, amplifying global economic vulnerabilities and exposing institutional weaknesses in trade governance. The findings underscore TPU as a persistent and independent force shaping macroeconomic outcomes, with broad implications for corporate strategy and international policy design.

Keywords: Trade Policy Uncertainty, U.S.-China Trade War, Investment, Labor Market, Consumer Confidence, Global Economy.

I. Introduction

The U.S.-China trade conflict under the new Trump administration marked a

sharp break from past trade strategies. Rather than relying solely on traditional tariff measures, the administration has introduced an unstable and unpredictable approach that significantly increased trade policy uncertainty (TPU). This uncertainty has become a key factor shaping global economic behavior, often more impactful than the tariffs themselves.

Figure 1 illustrates the TPU Index on a monthly basis from 2015 to April 2025. The index remained relatively stable with occasional spikes during events such as the U.S.-China trade tensions in 2018–2019. However, a dramatic surge occurred starting in late 2024, reaching a record high of 1,151.36 in April 2025. This sharp rise suggests a significant increase in uncertainty surrounding global trade policies, possibly triggered by major geopolitical or economic disruptions. The figure highlights the growing volatility in the global trade environment and signals a pressing need for further empirical analysis to understand its causes and consequences.

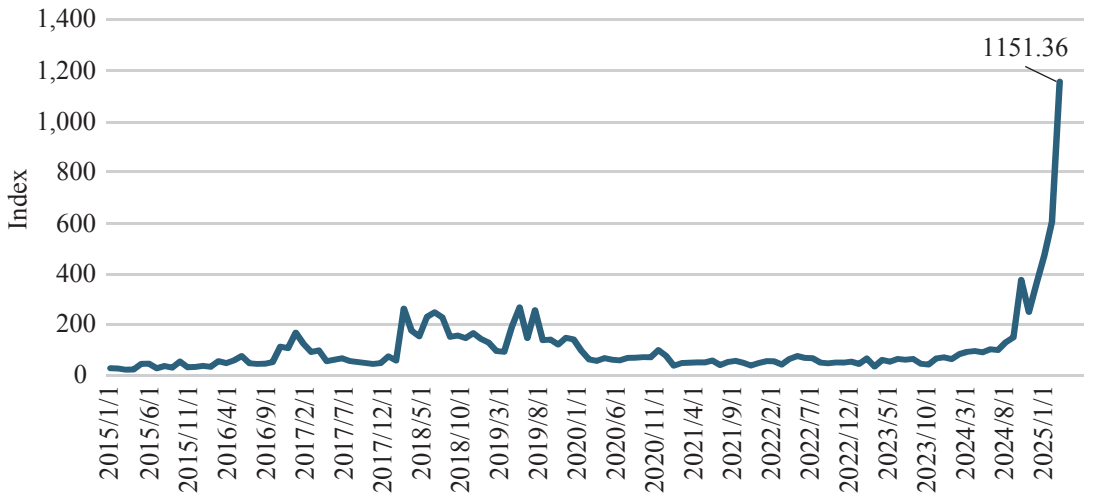

Figure 1 Trade Policy Uncertainty Indicators

Source: Compiled by authors. Data from Economic Policy Uncertainty, "Trade Policy Uncertainty Index," May 25, 2025 accessed, *Economic Policy Uncertainty*, <https://www.policyuncertainty.com/trade_cimpr.html>.

The tariff policies implemented between 2018 and 2020 produced their most severe economic effects not through the magnitude of tariff rates themselves, but through the channel of heightened TPU. The economic disruptions stemming from this uncertainty have proven both deeper and more persistent than those caused by direct price effects. Firms and markets found themselves reacting not only to enacted policies but also to the specter of future actions — creating a form of "policy overhang" that fundamentally impaired long-term planning and risk assessment.

The idea that TPU functions as a distinct economic force is supported by a growing body of research. Studies have shown that uncertainty affects investment, employment, innovation, and financial stability.[1] The trade war created prolonged uncertainty that disrupted supply chains, slowed investment, and reshaped expectations in ways that conventional tariff analysis cannot fully explain.

This study argues that TPU is not a side effect of trade disputes, but a core element of economic change in the post-2018 world. It explores how the Trump administration's strategy has caused lasting shifts in economic behavior in both the U.S. and China, and across global markets, by making unpredictability a central feature of international trade. This trade conflict represents more than a disagreement over trade balances. It signals a deeper shift — toward an economic environment where policy unpredictability is a key driver of decision-making, with long-term consequences for the global economy.

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1. Nicholas Bloom, "The impact of uncertainty shocks," *Econometrica*, Vol. 77, No. 3, May 2009, pp. 623-685, *WILEY*, <https://doi.org/10.3982/ECTA6248>; Kyle Handley & Nuno Limão, (2017). "Policy uncertainty, trade, and welfare: Theory and evidence for China and the United States," *American Economic Review*, Vol. 107, No. 9, September 2017, pp. 2731-2783, *American Economic Association*, <https://doi.org/10.1257/aer.20141419>; Lubos Pástor & Pietro Veronesi (2012). "Uncertainty about government policy and stock prices," *The Journal of Finance*, Vol. 67, Issue 4, August 2012, pp.1219-1264, *WILEY*, <https://doi.org/10.1111/j.1540-6261.2012.01746.x>; Fang Zheng, Xue Chen, & Yun Sun, "The Influence of Trade Policy Uncertainty on Corporate Innovation Strategies," *Finance Research Letters*, Vol. 75, April 2025, *Science Direct*, <https://doi.org/10.1016/j.frl.2025.106922>.

The paper is structured as follows. First, the study examines how TPU has affected investment, labor, and consumer behavior in the U.S. in Section 2. Next, it further looks at how China adjusted its economic strategies under sustained uncertainty in Section 3. Section 4 analyzes global spillover effects and risk transmission. The final section summarizes the findings and considers how future trade policies might be managed under continued uncertainty.

II. Impact of the U.S.-China Tariff War on the U.S. Economy

The economic consequences of the U.S.-China tariff war were felt far beyond the immediate effect of higher costs for imports. It was not the tariffs that made the headlines but the unpredictability of trade policy: the frequent reversals, the muddled rules, and the arbitrary escalations did deeper, lasting harm. This distress eroded the U.S. economy's underpinnings, warping investment patterns, labor markets, and consumer confidence.

1. Investment Paralysis Driven by Uncertainty Expectations

TPU has increased uncertainty and made it more difficult for firms to forecast future operating conditions. Firms postponed or canceled investment plans due to worries about input costs, export access, and demand prospects. Instead of making long-term commitments, firms tend to wait for signals to become clearer.

If so, policy uncertainty will have reduced U.S. investment by some 4.4 percent by 2025, according to the Penn Wharton Budget Model.[2] The capital stock could decline by 0.6% by 2030 and by nearly 10% by 2054 if such trends continue. These are not mere temporary slowdowns; there are deeper structural hesitations that change the way in which firms assess long-term risk and opportunity.

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2. Felix Reichling, "The Economic Effects of President Trump's Tariffs," April 10, 2025, *Budget Model*, <https://budgetmodel.wharton.upenn.edu/issues/2025/4/10/economic-effects-of-president-trumps-tariffs>.

This is consistent with another broad-based measure of the economy, the U.S. Conference Board's Leading Economic Index (LEI). Figure 2 shows the development of the leading (blue line), coincident (red line), and lagging (yellow line) indicators (June 2020 to January 2025). Although all three measures developed similarly immediately after the recession caused by the COVID-19 pandemic, there was a marked divergence from mid-2022. The forward-looking index, which is a barometer of future economic activity, has been on a downward trajectory since 2022, indicating a loss of momentum in economic growth and increased uncertainty. The coincident index, which measures the current state of the economy, is also on the moderate rise side. The lagging index, which tends to trail economic activity, is currently high and stable, with none of the indicators in this category flashing a warning sign of a possible coming slowdown. This degree of increasing divergence is probably further evidence of the effect that increased trade policy uncertainty (as indicated in Figure 1) is having on forward-looking expectations, despite a current- and past-economic-conditions environment that is quite a bit less fragile than such a large spread would imply. The uncoupling of these indices suggests the importance of reconsidering conventional wisdom during periods of high policy uncertainty.

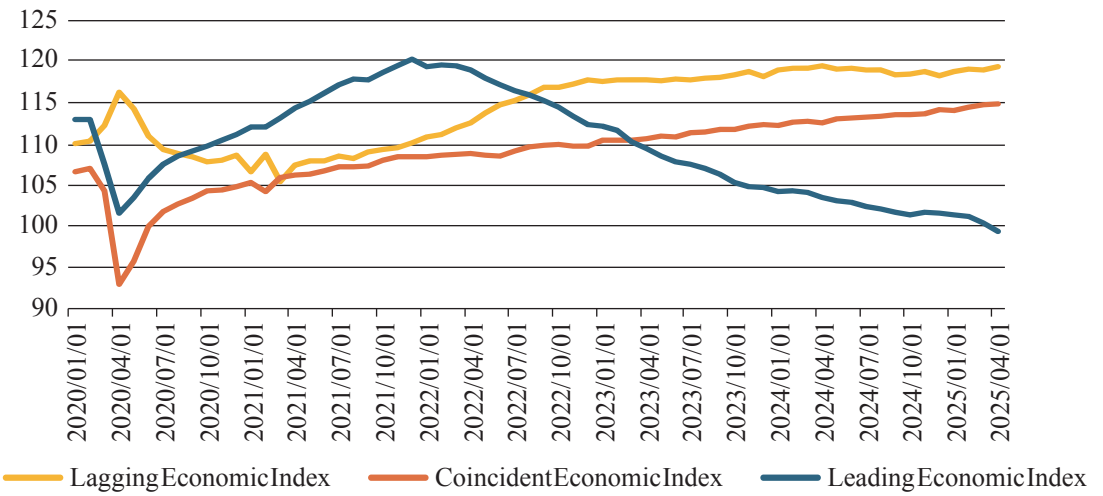

Figure 2. Divergence of U.S. Economic Indicators Amid Trade Policy Uncertainty (2020–2025)

Source: Compiled by authors. Data from "CEIC Data Global," May 25, 2025 accessed, *CEIC*, <https://www.ceicdata.com>.

2. Labor Market Frictions and Hiring Caution

Figure 3, mapping the U.S. labor market using Job Openings and Labor Turnover Survey (JOLTS) data from mid-2020 through early 2025, shows U.S. labor market dynamics. The blue line represents overall job openings, which shot up in 2021 but quickly plummeted after early 2022, receding by about 33 percent by 2025. By contrast, the red line which describes recruitment activity has been much more stable over that time.

This divergence suggests that even as firms pared back on new job listings — most likely in response to heightened economic and trade policy uncertainty — they kept current staff levels in place. The numbers indicate that companies became increasingly wary about prospects for growth, scaling back their plans for expansion as opposed to implementing widespread layoffs. This contrast is consistent with a labor market that is averse to risk, as opposed to becoming tighter, which would serve to maintain the uncertainty faced by the broader economy at this time.

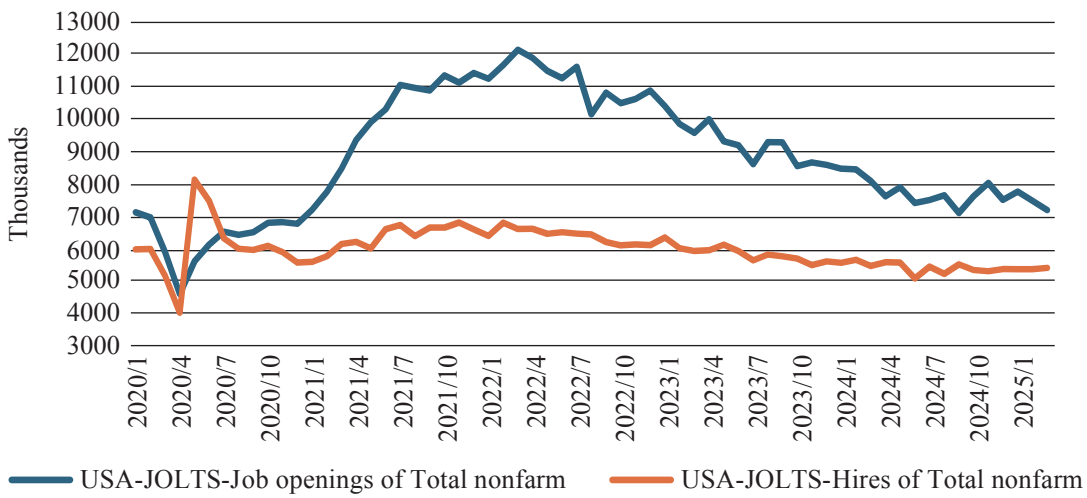

Figure 3. Job Openings and Labor Turnover Survey (JOLTS)

Source: Compiled by authors. Data from U.S. Bureau of Labor Statistics, "Job Openings and Labor Turnover Survey," *U.S. Bureau of Labor Statistics*, May 25, 2025 accessed, <https://data.bls.gov/PDQWeb/jt>.

This hiring freeze is also consistent with TPU literature finding that firms avoid irreversible decisions (like hiring) when policy signal is ambiguous. Even businesses making money played it safe, refusing to commit to jobs until the policy landscape was steadier. Exact numbers vary, but studies find that tariffs have led to substantial direct job loss in the United States, but the slacker labor market effects, like delaying hiring, slowing promotions, and moderating wage gains, will have so far been likely to weigh more. Policy-risk-induced uncertainty raises economic uncertainty by causing firms to delay investment and hiring decisions, and investment is projected to fall by 4.4% by 2025.

3. Consumer Sentiment and Demand Compression

Consumer behavior was no less affected by uncertainty. As investment decelerated and hiring plans were put on ice, households grew more cautious. Despite relatively healthy employment and income figures, people spent less and saved more — a reflection of increasing anxiety about the future.

The Yale Budget Lab calculates that tariff-induced price hikes, on average, cost a family more than US$2,300 a year. Across major categories of goods, prices went up: clothing (6 to 10 percent), electronics (8 to 15 percent), and vehicles (12 to 19 percent). These frictions eroded real income and ate into discretionary consumption.

Figure 4 shows the trajectories of the two most important indicators of U.S. consumer confidence to early 2025: the University of Michigan's Consumer Sentiment Index (red line) and the Conference Board's Consumer Confidence Index (blue line). Both indices display a strong decline at the start of the COVID-19 pandemic in 2020, followed by a partial recovery. But since 2021, both indices have trended consistently downward with measures falling noticeably through 2024 and continuing in the first half of 2025. This sustained erosion in consumer confidence indicates that households have become significantly more conditional in their expectations for the economy and the explanation would seem to be a deterioration in various determinants of a household's economic expectations, such as inflation, increasing TPU (illustrated in Figure 1) and weakening forward-looking economic indicators. The data signal

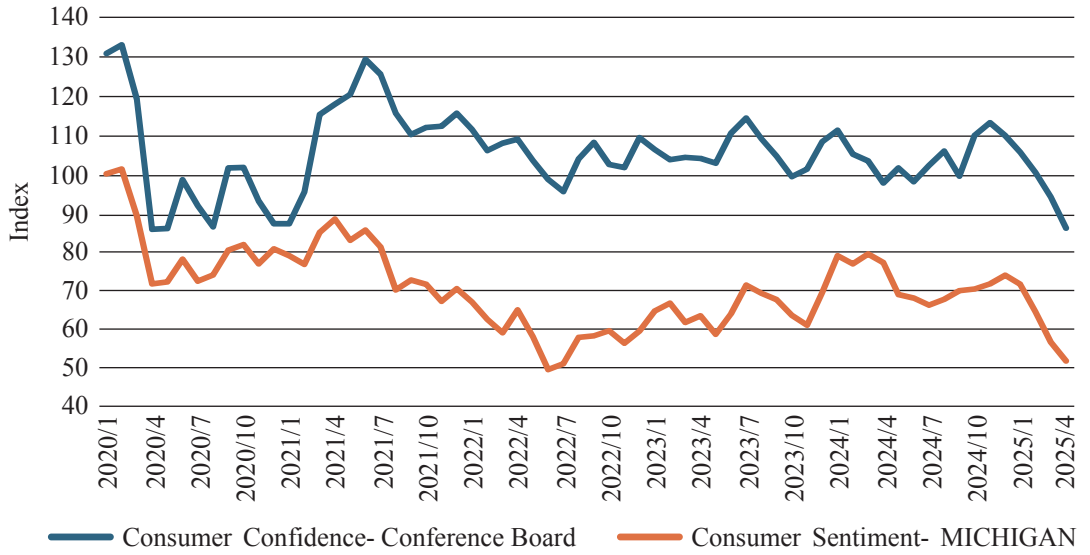

Figure 4. The University of Michigan's Consumer Sentiment Index and the Conference Board's Consumer Confidence Index

Source: Compiled by authors. Data from CEIC Data Global; the University of Michigan's Surveys of Consumers: "United States Michigan Consumer Sentiment," May 25, 2025 accessed, *University of Michigan*, <https://www.sca.isr.umich.edu/tables.html>.

waning consumer sentiment that could drag on spending and overall economic growth going forward.

This space that is created by the distance between the present economic circumstances and those in the future is the psychological aspect of TPU. Households not only responded to current costs — they changed behavior out of fears of future shocks. That prompted even more saving and less spending, particularly on durable goods, which further reduced demand.

This type of feedback loop, with uncertainty leading to caution, leading to depressed demand, and ultimately feeding back into business hesitancy, can be self-reinforcing. It takes more than stimulus to break such a cycle: It requires credible and stable policy frameworks to rebuild confidence.

4. Structural Constraints on Growth Recovery

Taken together, the impacts on investment, employment, and spending have left lasting impediments to regaining economic health. And while some of the trade tensions had diminished, the uncertainty they sowed weighed on growth. The U.S. GDP growth is projected to slow from 2.8% in 2024 to 1.8% in 2025 and uncertainties of trade policy and the continuous increase in tariffs are said to be the primary drivers, citing TPU as one of the main causes. What makes this decline so striking is that other fundamentals — such as low unemployment and stable inflation — signal that conditions are ripe for growth.

But the tools that are available to policymakers, like looser money and more fiscal stimulus, have relatively little effect in this context. When businesses and households lack confidence in the policy environment, they behave very gingerly, no matter how strong the short-term conditions seem to be. This is a more fundamental shift. TPU has spawned what some economists call "regime uncertainty" — a condition where the economic rules of the game are considered unreliable. In this environment, when risk and return are so far from traditional models, long-term decision making is fraught.

The real long-term cost is not just slower growth, but the loss of dynamism. No investment, no innovation. Wage gains slow down without job creation. With no confident consumers, demand craters. All of this is combining to diminish the competitive standing of the United States long after the trade war ends.

III. China's Economic Response to Trade Policy Uncertainty: From Shock to Structural Realignment

The U.S. tariffs aimed to reduce China's trade surplus, but their most significant impact came through uncertainty. Constant shifts in U.S. policy — tariff hikes, reversals, and vague rhetoric — left Chinese firms and policymakers unsure about the future. This environment of TPU disrupted planning, slowed reforms, and forced China to rethink its economic model.

1. Growth Deceleration through the Lens of TPU

China's economic growth forecasts have been repeatedly revised downward, not only due to declining exports but also because firms have become increasingly reluctant to invest amid fears of further sanctions or restrictions. Unlike regular trade shocks that fade with time, TPU has lasting effects. Even after some tariffs were removed, confidence did not return quickly. Restoring it requires more than economic incentives — it requires credible policy signals, both domestically and internationally.

Heightened U.S. trade policy uncertainty has negatively impacted China's output, consumption, and investment in the short run.[3] While Goldman Sachs[4] has warned

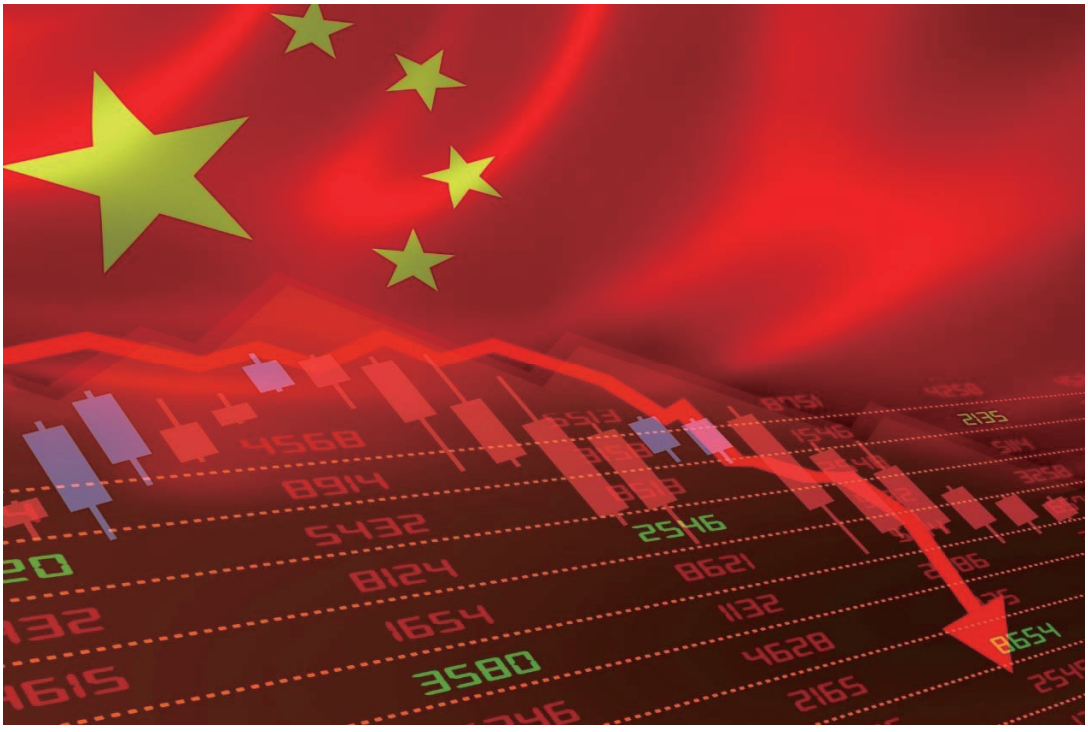

Figure 5. China's Economic Growth Dragged Down by TPU

Source: Depositphotos.

3. World Bank Group, *Global Economic Prospects* (Washington, DC: World Bank, 2025), pp. 55-57.
4. Goldman Sachs Asset Management, "Market Pulse," April 2025, *Goldman Sachs Asset Management*, <https://am.gs.com/cms-assets/gsam-app/documents/insights/en/2025/market-pulse-us_0425.pdf>.

that persistent trade tensions could significantly reduce China's growth — with earlier analyses suggesting potential losses of up to 2 percentage points under extreme scenarios — their most recent forecasts for 2025 project GDP growth between 4.6% and 4.8%, reflecting both ongoing uncertainty and recent policy responses.

2. Supply Chain Realignment and Strategic Vulnerability

TPU pushed many multinationals to diversify away from China. "China+1" strategies — adding production in Vietnam, Mexico, or India — became standard risk management. But while this shift reduces exposure to China-specific risks, it also introduces new ones. These alternative hubs often lack China's infrastructure, skilled labor, and scale. Worse, they may also become targets in future disputes.

This shift is costly and complex. China's manufacturing strength did not emerge overnight: it was built over decades through specialization, supplier coordination, and deep institutional support. Relocating production erodes these accumulated advantages and rebuilding them elsewhere will take years.

For China, this means more than just lost output. As foreign firms leave, so do opportunities for knowledge transfer and technological learning. Without tight integration into global value chains, China risks sliding back toward lower-value-added production.

3. Investment and Innovation Retrenchment Under Policy Volatility

TPU has led both domestic and foreign investors in China to take a more conservative stance. Exporters face unclear rules and market access barriers, while domestic firms contend with demand uncertainty and employment instability. This has led to shorter investment horizons and weaker capital spending.

In 2024, manufacturing investment grew only 2.6%, the slowest pace in over a decade, despite government incentives. This was not due to a lack of funds but to doubts about future returns. JPMorgan, meanwhile, has noted that even partial tariff

rollbacks do not restore momentum, as lingering uncertainty continues to weigh on business expectations and investment plans.[5]

Raising average tariffs from 20% to 40% could cut Chinese exports to the U.S. by 14% and reduce GDP by about 2 percentage points. But these estimates may still understate the impact, as they don't fully capture how uncertainty depresses innovation and delays investment.[6] Even with policy support, households saved more and spent less, dragging down GDP by an estimated 0.4 percentage points.

Perhaps the biggest risk lies in innovation. Ongoing trade tension, combined with restrictions on tech collaboration, has made R&D investments far riskier. A-share listed firms showed clear drops in both spending and output for innovation, especially among exporters. These trends threaten China's goals under initiatives like "Made in China 2025" (MIC25), which depend on stable conditions for long-term tech development. If TPU persists, it could shift China away from innovation-driven growth and back toward older, low-productivity models.

Table 1 summarizes the severity of TPU's impact across key economic dimensions, revealing a broad-based strain on China's development trajectory. These quantified effects provide a foundation for the analysis in Section III, which explores how such disruptions have evolved into a deeper structural challenge. From export losses and labor dislocation to declining investment and innovation setbacks, each domain reflects the cascading consequences of sustained trade policy uncertainty. The following section examines these pressures in detail, tracing China's economic response from initial shocks toward longer-term strategic realignment.

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5. J.P. Morgan Asset Management, "China 2025: Trade War 2.0.," December 30, 2024, *J.P. Morgan Asset Management*, <https://am.jpmorgan.com/us/en/asset-management/institutional/insights/portfolio-insights/fixed-income/fixed-income-perspectives/china-2025-trade-war-2-0/>.
6. A. Garcia Herrero, Jianwei Xu, & Jeremy, J., "How will US' additional tariffs impact the Chinese economy," April 2, 2025, *Natixis CIB Research*, <https://www.research.natixis.com/Site/en/publication/IsoDoX-ScCo6Ik2vcuyNmw%3D%3D>.

Table 1. Economic Impact Severity of TPU Across China's Core Domains

Impact Domain	Severity	Explanation
Export Sector	Very High	U.S. tariffs rising from 20% to 40% may reduce exports to the U.S. by 14-18%, equivalent to a 1.9-2.5 percentage points GDP loss.
Labor Market	High	Export shock (12-17% decline) could reduce manufacturing employment by 6.4-9.1%, or put 6-9 million jobs at risk.
Domestic Consumption	Medium	A 1% drop in wages leads to a 0.7% fall in spending, reducing GDP by about 0.4 percentage points.
Fixed Investment	Medium-High	Falling confidence causes a 0.2 percentage point reduction in Fixed Asset Investment (FAI) contribution to GDP growth.
Technological Upgrading	High	U.S. controls on critical tech impair core components of MIC25; limited return on massive subsidies.
Financial and Policy Tools	Medium	China's monetary easing, cutting rates and reserve requirements, added about RMB 1 trillion to the economy, but it only offsets around 30% of the GDP loss caused by tariffs.

Data sources: Complied from Jinyue Dong, Betty Huang, & Le Xia, "China Economic Outlook," March 2025, *BBVA Research*, <https://www.bbvaresearch.com/en/publicaciones/china-economic-outlook-march-2025/>; A. Garcia Herrero, Jianwei Xu, & Jeremy, J., "How will US' additional tariffs impact the Chinese economy"; A. Garcia Herrero, Jianwei Xu, "How is China reacting to Trump's trade war?" May 9 2025, *Natixis CIB Research*, <https://www.research.natixis.com/Site/en/publication/4DfErFy8KcZwuJb7kHA-gQ%3D%3D>.

IV. Global Economic Spillovers and Systemic Risk Channels

What began as a bilateral trade dispute between the U.S. and China has evolved into a structural source of global economic instability. While tariffs triggered the initial shock, it is the persistence of TPU that has amplified disruptions, altering how economies function and how markets price risk. The ripple effects have spread widely, straining global cooperation and increasing vulnerability across regions.

1. Global Growth Slowdown and Widening Vulnerability

TPU has led to a synchronized global growth slowdown — not just by reducing trade volumes, but by influencing how businesses and consumers respond to future uncertainty. Investment delays, weaker consumption, and declining policy effectiveness have all become more visible.

Global growth is projected to slow to 2.3% in 2025 amid rising trade tensions and uncertainty, with developing economies especially vulnerable to external shocks, capital flight, and reduced demand from key partners.[7] These factors compound existing challenges like high debt and limited fiscal space, creating a "perfect storm" that risks reversing development progress.[8]

This broader deceleration reflects a set of reinforcing mechanisms: trade-driven demand shocks, suspended infrastructure and FDI projects, and reduced cross-border technology flows. Even as headline tensions ease, the underlying hesitation remains, hindering recovery in many parts of the world.

In emerging markets like Brazil, South Africa, and Mexico, TPU has led to capital outflows, falling exports, and growing fiscal strain. These economies must now manage both domestic policy uncertainty and a less predictable global environment, often without sufficient buffers.

2. Supply Chain Fragility in Asia and the Regional Spillover Effect

Asia's role as a central manufacturing and supply chain hub makes the region particularly sensitive to disruptions tied to TPU. The heavy dependence on Chinese intermediate goods has turned a localized shock into a region-wide coordination challenge.

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7. UNCTAD "Trade and Development Foresights 2025: Under pressure-Uncertainty reshapes global economic prospects," 2025, *United Nations*, <https://aduananews.com/wp-content/uploads/2025/04/gdsinf2025d1_en.pdf>.
8. UNCTAD "World Economy Is on a Recessionary Trajectory, Driven by Trade Tensions and Uncertainty," 2025, *The United Nations Correspondent*, <https://theunitednationscorrespondent.com/world-economy-is-on-a-recessionary-trajectory-driven-by-trade-tensions-and-uncertainty-unctad/>.

Huang and Xia's Input-output analysis highlights this exposure.[9] Vietnam relies on China for 23% of its intermediate goods, Cambodia for 38% of electronics inputs, and Laos for 35% of computing components. Any production volatility in China ripples through these networks, causing delays, cost overruns, and inefficiencies. In parallel, several Asian economies attempting to replace Chinese suppliers in U.S. markets now face their own tariffs. This "dual exposure" leaves them vulnerable from both supply and demand ends — undermining the region's hard-won integration gains.

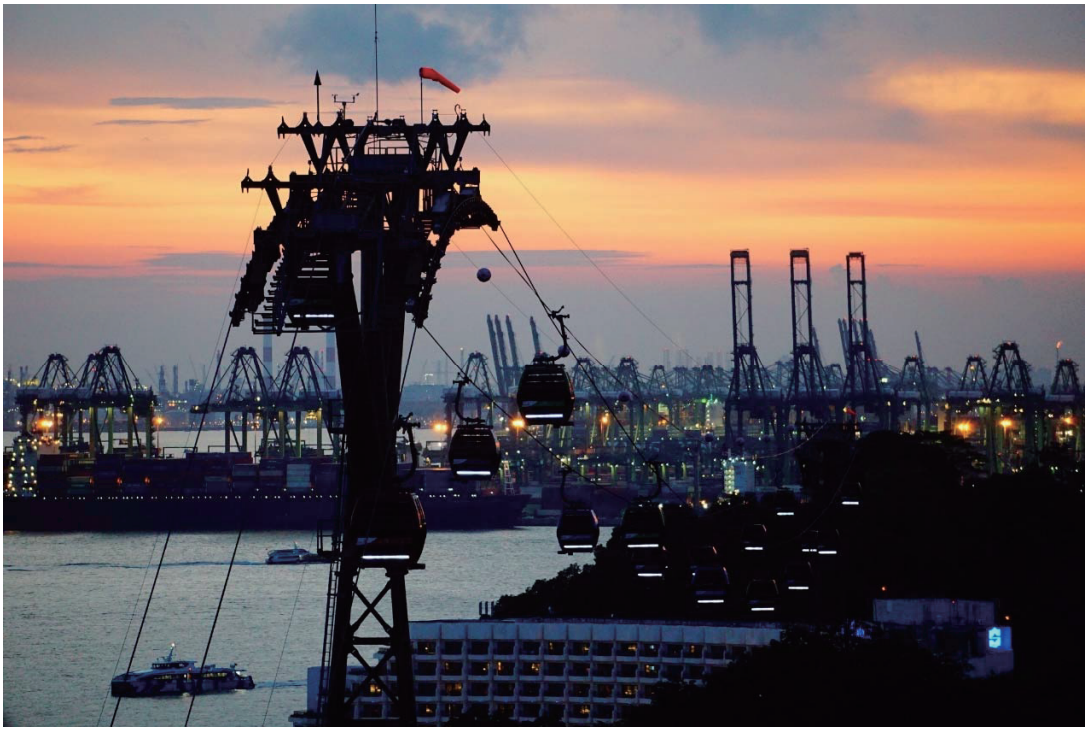

Figure 6. Supply Chain Fragility in Asia

Source: Depositphotos.

9. Betty Huang & Le Xia, "An Input-Output Table Analysis on U.S.'s 'reciprocal' Tariffs on Asian countries," May 6, 2025, *BBVA Research*, <https://www.bbvaresearch.com/wp-content/uploads/2025/05/An-input-output-table-analysis-on-US-reciprocal-tariffs-impact-on-Asian-countries.pdf>.

In worst-case scenarios, highly exposed economies such as Vietnam and Cambodia could face significant GDP losses—some simulation studies suggest up to 10% — under prolonged TPU, as global trade tensions erode exports and investment.[10] While these figures are derived from extreme scenario modeling and may not represent the official projections of major international institutions, they highlight the acute risks faced by smaller, export-dependent economies.

Even larger, more integrated economies like Malaysia and South Korea are affected through their participation in higher-tier supply chains. Declining external demand and shifting trade regimes amplify risks, as noted in recent regional outlooks.[11] Deep regional interdependence, once considered a strength, has thus become a structural risk amid unstable trade policies, heightening vulnerabilities across the region.

3. Repricing Investment Risk and Strategic Recalibration

The global investment environment has shifted in response to TPU. As unpredictability becomes the norm, businesses are rethinking how and where they allocate capital. Long-term, globally integrated projects are increasingly seen as vulnerable.

Rather than isolated shocks, tariff decisions are now viewed as tools of broader geopolitical strategy. This perception disrupts standard investment planning. Oxford Economics notes that forward-looking corporate strategies have become more

10. Betty Huang & Le Xia, "An Input-Output Table Analysis on U.S.'s 'reciprocal' Tariffs on Asian countries."

11. IMF, "Regional Economic Outlook: Asia and Pacific," May 2025, *IMF*, <https://www.imf.org/en/Publications/REO>; ASEAN+3 Macroeconomic Research Office, "ASEAN+3 Regional Economic Outlook," April 15, 2025, *AMRO*, <https://amro-asia.org/asean3-regional-economic-outlook-areo/>.

defensive, favoring optionality over long-term commitments.[12]

This caution is visible in sectors such as automotive, electronics, and energy — industries that depend on global supply chains and stable regulations. Even firms not directly affected by tariffs face indirect hits, as clients scale back operations and delay expansion.

According to Fitch Ratings,[13] the investment slowdown caused by uncertainty may have broader economic consequences than tariffs themselves. Risk aversion has constrained productivity growth, job creation, and technological upgrading across a wide set of countries and industries.

Figure 7. The Global Investment Environment Has Shifted in Response to TPU

Source: Depositphotos.

12. Oxford Economics, "The US-China tariff deal signifies a major de-escalation," May13, 2025, *Oxford Economics*, <https://www.oxfordeconomics.com/resource/us-china-tariff-deal-signifies-a-major-de-escalation/>.

13. Fitch Ratings, "US-China tariff de-escalation does not signal trade normalization," May 13, 2025, *Fitch Ratings*, <https://www.fitchratings.com/research/sovereigns/us-china-tariff-de-escalation-does-not-signal-trade-normalisation-13-05-2025>.

4. Financial Volatility and Confidence Erosion

TPU has not only reshaped real economic behavior but also become a driver of global financial volatility. Market responses to vague policy signals or threats of new tariffs now trigger rapid changes in currency, equity, and commodity markets — often disproportionate to the actual economic content of those signals. BBVA Research finds that persistent TPU leads to correlated swings across emerging market currencies, stock indices, and commodity prices. These responses often reflect fear of future disruptions more than present conditions.

The effect extends to household behavior. Uncertainty erodes consumer confidence even in countries not directly involved in the dispute. Surveys show rising precautionary savings, falling durable goods purchases, and a general pullback in consumption, especially when monetary and fiscal policy tools appear less effective in offsetting risk perceptions.

The overlap between trade tension, national security concerns, and energy policy has created complex risk clusters. In this environment, traditional financial models struggle to price assets, assess exposure, or guide investor decisions. As strategic competition spreads across sectors, markets face persistent ambiguity.

5. Toward a More Uncertain Global Order

The long-lasting presence of TPU has set in motion structural changes in the global economy. While temporary easing of tariffs, such as limited U.S.-China deals, may offer the persistent presence of TPU has triggered structural shifts in the global economy. Temporary tariff relief may offer short-term stability, but it does not undo the institutional erosion caused by inconsistent and unpredictable trade policy. The once-predictable, rules-based global trading system has given way to a more fragmented framework characterized by retaliation, *ad hoc* agreements, and shifting alliances. In response, firms are adjusting through diversified sourcing strategies, enhanced risk management, and shorter investment horizons. Governments, in turn, are increasingly prioritizing regional partnerships and domestic market development to reduce external vulnerability.

Restoring credibility in trade policy — regardless of tariff rates — could yield greater economic benefits than marginal changes in duties.[14] The core constraint is trust: without it, even open markets and policy incentives are insufficient to stimulate long-term investment or deeper integration. This poses a fundamental challenge for global economic governance. If TPU becomes a lasting feature of international commerce, institutional frameworks must adapt accordingly. This requires investment in transparency, contingency planning, and mechanisms capable of withstanding political volatility.

V. Conclusion and Policy Implications

This paper has found that the U.S.-China trade conflict was not a mere shock but a structural break. It wasn't the tariffs *per se* that defined this period, but rather their broader, longer-lasting, and more widely felt twin in the form of trade-policy uncertainty. Unlike previous trade disputes, in which there was a clear policy shift followed by an adjustment period, this episode has left firms and governments in a phase of extended uncertainty.

TPU is no longer a sidekick in the global economy; it is also transforming how firms invest, hires, and innovate. Its impact is evident along several dimensions: investment is falling, labor market mismatches are worsening, R&D activity is compressing, and confidence in policy's ability to deliver is evaporating.

Elsewhere, in the United States, uncertainty has depressed private capital formation and tempered productivity growth. Projections from the Penn Wharton Budget Model estimate that investment could decline by 4.4 percent by 2025, with long-term capital stock losses nearing 10 percent by 2054 if uncertainty continues. The upshot for China is a change of its development strategy, declining from global to regional to national — and the enormous efficiency and long-term costs of the downsizing effort.

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14. United Nations Conference on Trade and Development, *World investment report 2024: Investment facilitation and digital government* (New York: UN, 2024), *UNCTAD*, <https://unctad.org/system/files/official-document/wir2024_en.pdf>.

There are big spillovers around the world. TPU has degraded supply chains, weakened investor sentiment, increased financial instability, and propagated uncertainty into the households and firms of many countries beyond the two main actors of the conflict. Emerging markets, notably in Asia, have been worst hit because they are deeply enmeshed in China's manufacturing networks and thus also have significant exposure to U.S. market access.

With TPU's sweeping — and enduring — impact, we cannot rely on *ad hoc* policy fixes. What is required is a broader architecture — one that deals with the institutional roots of uncertainty and supports stability mechanisms.

Strengthening Trade Institutions: Governments need to make trade and trade institutions more transparent and accountable, for example through reform of the World Trade Organization (WTO), dispute resolution, and domestic parliamentary oversight. Early warning systems and independent monitors can sound alarms when policy shifts risk becoming destabilizing.

Figure 8. Interdependence Must be Based upon Strong Institutions and Rules

Source: Depositphotos.

Supporting Corporate Adaptation: Companies need to implement flexible strategies such as diversified supply chains and scenario planning. Public support, for example, in the form of taxes, infrastructure and policy risk insurance, can also ensure that business remains competitive.

Supporting for Vulnerable Sectors and Innovation: Sectors like manufacturing and R&D require targeted financial support and protective measures to manage the volatility. Public R&D investment and international collaboration are essential to the continued flow of innovation.

Embedding TPU in Macroeconomic Policy: TPU should be considered a key macroeconomic risk. Policy-makers will need to factor it into their forecasting models, stress tests and policy communications to hold credibility.

Regional Cooperation and Risk-Sharing: Countries should be coordinating on customs duties, investment insurance, and infrastructure to shield against shocks. TPU should be covered in trade agreements, and development banks should offer bridging capital in cases of disruption.

The challenge in dealing with TPU is not to decline uncertainty, but rather to create systems that are robust in the face of it — transparent, responsive, and credible. Absent that, the strategic deployment of uncertainty will challenge the global economic order. It's clear what we should have learned from the trade tensions of the last several years: Interdependence must be based upon strong institutions and rules rather than simply on open markets.