



Insight

Understanding Tariffs and GDP Growth

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Executive Summary

- Treasury Secretary Bessent has stated that every \$300 billion collected in tariff revenue would contribute 1 percentage point to gross domestic product (GDP) growth.
- The Trump Administration argues its tariffs are necessary to reduce U.S. imports, which it views as negatively impacting GDP growth.
- While the impact of tariffs on growth is difficult to estimate, as is always the case with taxes, Secretary Bessent's claim is mistaken because reductions in imports simultaneously lead to reductions in household spending and business investment; this insight walks through the relationship between tariffs and economic growth.

Introduction

Treasury Secretary Bessent has stated that every \$300 billion collected in tariff revenue contributes 1 percentage point to gross domestic product (GDP) growth. The Trump Administration argues its tariffs are necessary to reduce U.S. imports, which it views negatively impacting GDP growth. While the impact of tariffs on growth is difficult to estimate, as is always the case with taxes, Secretary Bessent's [claim](#) is mistaken because reductions in imports simultaneously lead to reductions in household spending and business investment.

This insight discusses the way in which GDP is calculated, as well as the impact tariffs might have on each of the components that make up GDP, in order to get a better understanding of the relationship between tariffs and economic growth.

What Is Gross Domestic Product?

Secretary Bessent's claim that U.S. tariffs boost economic growth misrepresents how a tariff interacts with the fundamental components that constitute GDP. To see this, let's review how GDP is calculated.

Gross domestic product is a [measure](#) of the total economic output of a country and is used to keep track of the total value of final goods and services produced during a given period. There are a few ways to calculate GDP, the most common being the expenditure approach.

Figure 1: The Expenditure Approach

$$GDP = Consumption + Investment + Government Spending + Exports - Imports$$

In the expenditure approach, GDP is equal to the total value of consumption, investment, government spending, and net exports (exports minus imports). Consumption tracks all private spending by individuals, investment refers to all capital expenditures by businesses, government spending includes all government payments, and net exports factors in the amount of domestic output exported versus foreign output imported. The net exports term is equivalent to the U.S. trade deficit, with imports being subtracted - not because they detract from GDP, but because doing so prevents a "doubling counting" effect. More on this later.

GDP can increase due to either an increase in prices or an increase in the quantity of goods and services produced. Higher prices result in higher GDP, but this is due to inflationary pressures rather than more goods and services in the economy. Real GDP growth is the result of [higher productivity](#) among workers that occurs through technological innovation. This allows for more output within the economy using the same number of inputs.

What Is a Trade Deficit?

A trade deficit - displayed in Figure 1 - occurs when a country imports more than it exports. Contrary to what the expenditure approach might imply, a trade deficit does not reduce GDP.

Imports are subtracted from the equation to prevent overcounting GDP since these goods and services are tracked in each of the other GDP categories. For example, if someone buys an imported banana in a grocery store, that purchase contributes to domestic consumption. Consumption increases GDP; however, the banana was not produced domestically so its import value does not count toward U.S. GDP and is therefore subtracted, resulting in a net-neutral impact to GDP. The same principle holds if a government purchases foreign

products or if a business imports machinery.

It is worth noting that these imports increase the [utility](#) (e.g. benefits or satisfaction) of U.S. consumers. Businesses also benefit from importing cost-effective or specialized inputs as it allows them to provide more value to consumers and produce more final products within the United States. In both cases, U.S. consumers and businesses are making an independent decision to purchase a good. This is very different from how the Trump Administration has characterized imports, [stating](#) they are equivalent to the United States as a whole subsidizing other countries. Trade is a two-sided transaction where both parties willingly accept a transaction because it is mutually beneficial.

Why Do Tariffs Not Raise GDP?

In Q1 2025, U.S. GDP was just over \$30 trillion, meaning Bessent's \$300-billion tariff revenue estimate is equivalent to about 1 percent of GDP. So far so good. The claim then assumes that \$300 billion in tariff revenue would result in a \$300 billion reduction in U.S. imports, boosting GDP by 1 percent. While tariff cost [estimates assume](#) imports fall, \$1 raised in import taxes does not represent a \$1 drop in import value. Consumers will shift their demand decisions based on higher prices but will continue to purchase imported products with the additional tax. The lack of the one-to-one correlation between tariffs and imports is highlighted by the Penn Wharton Budget Model, which [assumes](#) tariffs will generate \$419 billion in revenue in 2025 while reducing imports by \$319 billion.

Another issue with Bessent's remarks is that it views imports in isolation and does not consider consumption or investment. Recall that imported goods count toward consumption, meaning a reduction in imports is an equivalent reduction in consumption. Tariffs [reduce consumer demand](#) by raising prices for goods while also reducing take-home income for U.S. households, thereby degrading the consumption category. Tariffs also reduce domestic investment as companies pay the additional cost and have less available cash to spend on other economic activities. Higher input costs alongside foreign retaliation may also reduce domestic production, resulting in fewer exports. Though tariffs will increase government revenue and allow for more government spending, it is important to note that this revenue is collected from private individuals and firms, limiting their spending and investments.

While tariffs alone are not a secret path to boosting GDP, tariffs used as a blunt instrument could increase GDP. For instance, threatening high tariffs on other countries will likely result in companies investing in the United States or ramping up domestic production for the U.S. market. This would increase the investment category and increase GDP, all else being equal. Unfortunately for the Trump trade team, this does not factor in foreign retaliation and requires long-term tariff policy to remain in place, otherwise firms would not

make large-scale investments. With long-term tariffs come long-term tariff costs, which -as outlined above - have negative effects that reduce consumption and domestic investment.