



When will tariffs boost US inflation?

Despite massive tariff increases, the US inflation rate has fallen. Will the feared inflation-boosting effect fail to materialize, or will it only come later? The answer to this question is likely to have a decisive impact on the Federal Reserve's policy and, consequently, on developments on the global financial markets.

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Tariffs are rising, but inflation is falling...

Between February and April, US President Trump ordered numerous and, in some cases, drastic tariff increases. Although many of these tariff increases were suspended on April 9 and replaced by a 10% tariff for the time being, the threat of further tariff increases remains.[1] According to calculations by the Yale Budget Lab, the average tariff rate has risen to around 15.8%, which would be a good 13 percentage points higher than the average for 2024. Since around one-tenth of demand in the US is met by imports, the higher tariffs were expected to increase consumer prices by an estimated 1.3%.

However, inflation in the US has not picked up recently, but has actually tended to decline. Excluding volatile energy and food prices, the consumer price index rose by only 1.8% in the three months to May (seasonally-adjusted annualized rate; see title chart). In 2024, this rate was still 3.2%.

... and the Fed is coming under pressure

Despite weaker inflation, the Federal Reserve has not yet lowered its key interest rate, but is keeping the fed funds target range at 4.25%-4.50%, a relatively high level by international standards. Fed Chairman Jerome Powell has justified the Fed's restraint primarily by pointing out that the tariffs would only have a delayed impact on consumer prices. Furthermore, it is not yet clear how high the tariffs will ultimately be. The Fed is therefore waiting until the fog clears. However, the Fed is coming under increasing pressure. President Trump is calling for drastic interest rate cuts and considers Powell's refusal to be "un-American," and the longer the effects of the tariffs remain unrecognizable, the greater the pressure is likely to become.

The distribution chain of tariff increases

In fact, to quote Jerome Powell, it "takes some time for tariffs to work their way through the chain of distribution to the end consumer." First, the importer pays the tariffs. Wholesalers may also be involved before the goods are available for sale in retail stores. The chain is even longer if the imported goods are an input or intermediate product for the US manufacturing sector. In this case, there are even more intermediate steps to be taken before the end product is offered for sale. Every participant in the entire distribution chain strives to pass on the increased purchase prices resulting from customs duties to their customers. Whether this is completely successful depends on the respective market position, the strength of demand, and the availability of alternatives.

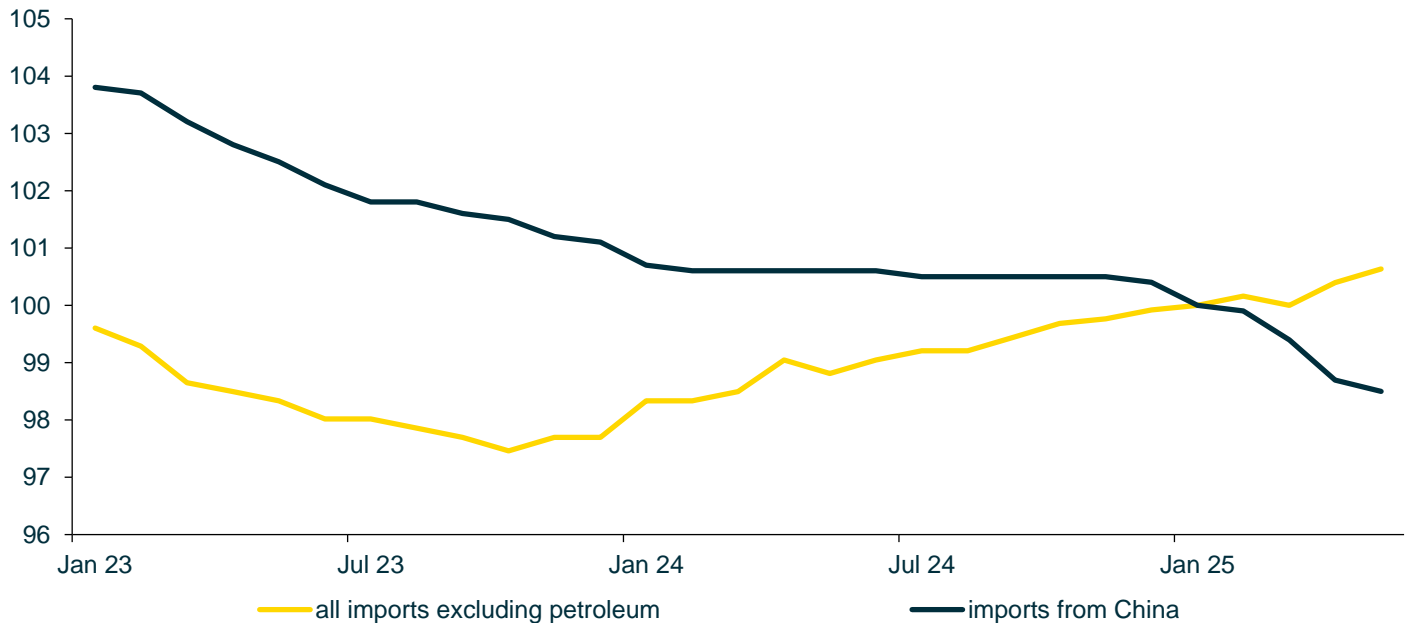
China pays only a very small portion of the bill...

The latest figures on US import prices show that the tariffs have so far been largely paid by American importers. It is important to note that tariffs are **not** included in these indices. If foreigners were to bear the tariffs, US import prices would have to fall significantly in order for prices for US importers to remain the same, taking into account the tariff surcharge.

However, the data suggests the opposite. Import prices for all goods except oil have been rising slightly since the end of 2024. This trend continued in April and May despite the higher tariffs (Chart 1). The effect is most noticeable in imports from China. After a period of unchanged prices, these have recently become slightly cheaper. However, the 2% decline in prices since the end of 2024 does not come close to offsetting the 30% additional tariff on most goods. Calculated on the basis of all imports, this obviously plays an even smaller role. [2]

**Chart 1 - Tariffs did not really have a big impact on import prices**

import prices, index January 2025 =100



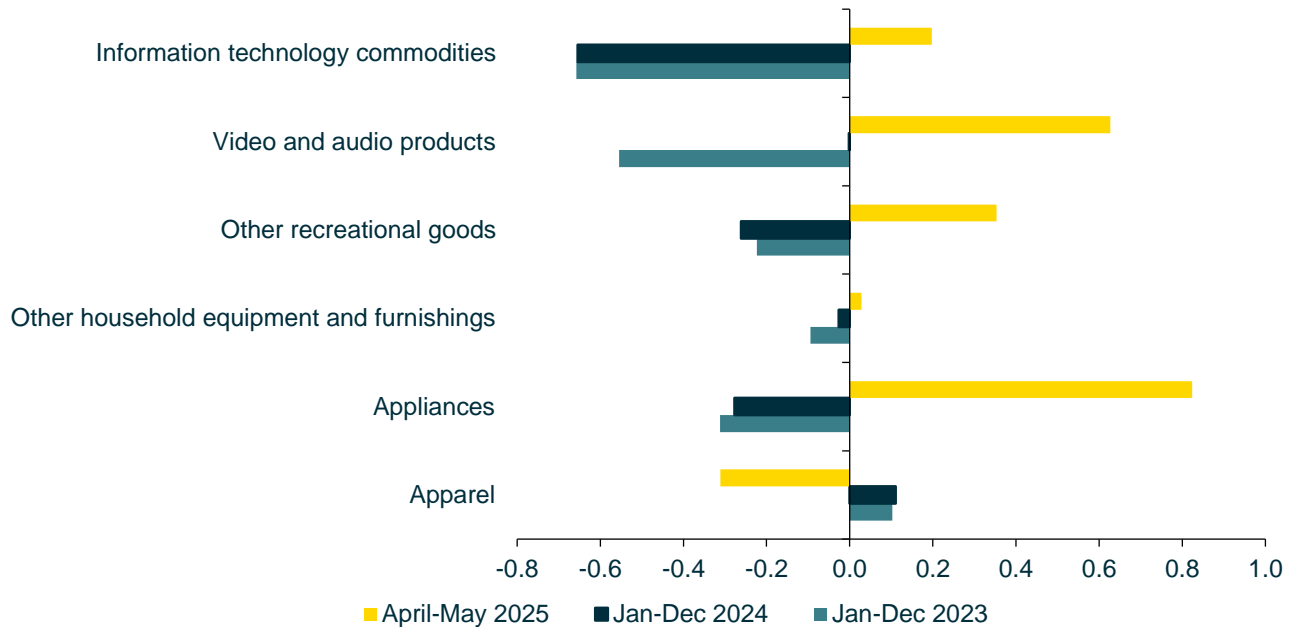
Source: BLS, S&P Global, Commerzbank Research

... and only some of this has been passed on to consumers

As a result, the tariffs have primarily been paid by Americans. Some of this has already been passed on to consumers. Although price pressure has eased in recent months as measured by the core consumer price index, there are clear signs that tariffs are beginning to have an impact on consumer prices. This is suggested by price developments in product groups that are typically imported, especially from China. Household appliances, for example, rose by an average of 0.8% in April and May compared with the previous month, whereas in 2023 and 2024 they had fallen by around 0.3% per month (Chart 2). IT goods saw a monthly price decline of 0.7% in 2023/24, most recently rising by 0.2%. Only clothing does not fit the picture. Here, prices fell in the last two months after rising slightly in 2023 and 2024. Overall, however, the effects on consumer prices are still very limited and nowhere near as large as would be expected given the massive tariff increases.



Chart 2 - Some goods that are typically being imported have indeed become more expensive after tariffs were introduced
consumer prices for selected categories of goods, average month-on-month change in %



Source: BLS, S&P Global, Commerzbank Research

So far, US companies have borne the brunt of the burden...

This means that US companies have borne the brunt of the tariffs so far. Their reluctance to pass on the burden to their customers is likely due primarily to the high level of uncertainty surrounding future tariff policy. Because the Trump administration has repeatedly introduced tariffs and then suspended them, at least in part, many companies are probably waiting to see which tariff rates will ultimately remain in place.

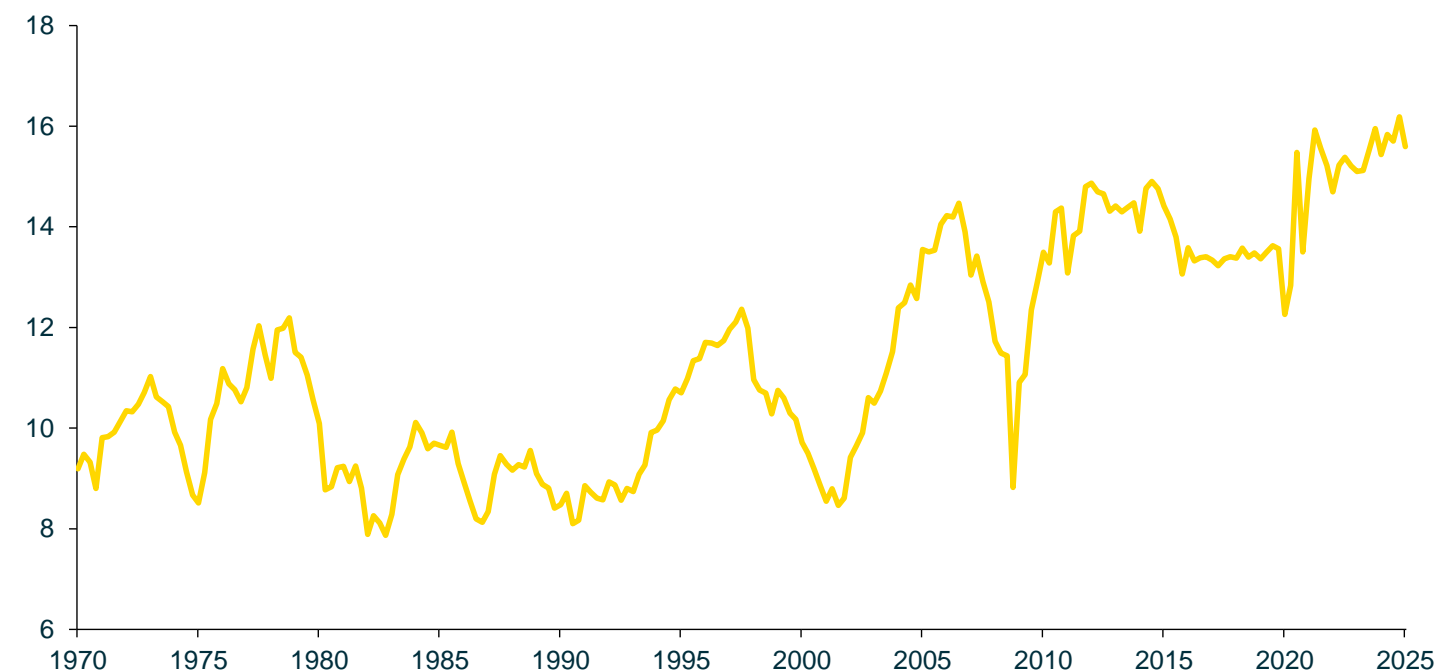
Many companies can afford to adopt this wait-and-see approach in the short term because they significantly increased their inventories before the tariffs came into effect. In addition, profit margins are close to historic highs (Chart 3). Both factors make it easier for them to avoid passing on the full cost of the tariffs immediately.

Waiting is also advisable due to political pressure. Large companies in the spotlight are likely to fear the president's wrath if they raise prices significantly. The press reported that Trump made it clear to auto industry executives that he would disapprove of such behavior, causing managers to worry that penalties could be imposed in such a case. Under these circumstances, it might be a better strategy not to be the first or second in the industry to raise prices, but to wait for a less conspicuous moment.



Chart 3 - Profit margins near record high

corporate profits with inventory valuation and capital consumption adjustments according to national income and product accounts, in % of national income



Source: BEA, S&P Global, Commerzbank Research

All these factors are delaying the impact of the tariffs on prices, but are unlikely to prevent it in the long term. We continue to assume that the average tariff rate will be at least 15 percentage points higher in the longer term than before Trump took office. Since imports account for roughly 10% of final demand, this corresponds to a potential price increase of 1.5%. It seems realistic that consumers will ultimately have to shoulder most of this, especially as other measures taken by the Trump administration are also likely to push up prices, such as reducing the number of available workers through stricter deportation policies. This means that there are still significant inflation risks.

Fed taking its time with interest rate cuts, yields higher in the medium term

This also explains why the Federal Reserve is taking more time with interest rate cuts than some expect and is refusing to bow to Trump's demands for a drastic reduction in key interest rates. We still expect interest rates to be cut only in September, followed by cautious and slow cuts of 25 basis points every three months. The effects of the tariffs are likely to become more apparent in the second half of the year, and the bond market is therefore likely to place greater emphasis on inflation risks again. US Treasury yields are therefore likely to rise in the medium term.

[1] Calculating the effective customs duty rate as the ratio of customs payments received to nominal imports, the figures currently available indicate a rate of 7%. This is also significantly higher than last year's 2.5%. However, there appear to be delays in data collection and the receipt of customs payments, meaning that this calculation underestimates the customs duty rate that will ultimately be payable. ([back to text](#))

[2] The rise in import prices could be at least partly attributable to the fact that the dollar has depreciated by 8% in trade-weighted terms since the beginning of February, when the US government announced the first tariff increases. However, since most US imports are invoiced in dollars, the effect of exchange rate changes on import prices is likely to be very limited, at least in the short to medium term. This is also supported by the fact that import prices had risen in the previous months, even though the dollar had strengthened significantly. ([back to text](#))



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