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US Announces Widespread Reciprocal Tariffs; Potential Impact on India Likely to be Moderate

- On April 2, US President Trump unveiled a reciprocal tariff plan, imposing a 10% baseline tariff on imports from all countries starting April 5, with higher tariffs on around 60 countries effective from April 9. Certain products, including pharmaceuticals and energy, are exempted from the new tariffs.
- India faces a 26% reciprocal tariff, significantly higher than the existing tariff differential with the US.
- While the US is India's second-largest trading partner, accounting for around 18.2% of India's total exports, Indian goods exports to the US represent only 2.1% of GDP, limiting the potential impact on India's economy.
- The direct impact of the reciprocal tariffs on India is estimated to be moderate, around 22bps of GDP, given that India's economy is primarily domestically oriented.
- Indirectly, US tariffs could lead to a global economic slowdown, which, in turn, could potentially impact India's GDP by an additional 21-32 bps.
- Sectors with higher exposure to the US market, such as electronics, textiles, precious stones, chemicals, and machinery, are likely to be most affected, while pharmaceuticals and energy-related exports will fare better due to exemptions.
- Higher US tariffs on Asian peers like Vietnam and China could create opportunities for Indian exports, particularly textiles and electronics, due to the favourable tariff differential.
- India is also actively negotiating a bilateral trade agreement with the US, expected to be concluded by Fall 2025, which could help mitigate the long-term impact of the tariffs.
- The RBI is expected to reduce the policy repo rate by 25bps in its April meeting to support economic growth, with inflation concerns likely taking a back seat.

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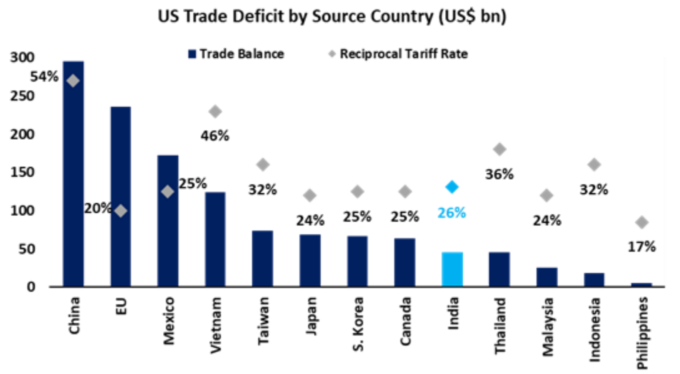
US President Donald Trump Unveils Reciprocal Tariff Plan; Escalates Global Trade Tensions

On April 2, US President Donald Trump unveiled a reciprocal tariff plan aimed at addressing its trade imbalances. Under this plan, the US will impose a baseline tariff of 10% on imports from all countries, effective from April 5. Additionally, higher reciprocal tariffs will be levied on around 60 countries and regions—including major economies like China, the European Union, and India—effective April 9. Further, certain key imports, including copper, pharmaceuticals, semiconductors, lumber, certain critical minerals, and energy products, have been exempted from these tariffs. Additionally, previously announced sector-specific tariffs on steel, aluminium and auto are likely to remain unaffected by the new reciprocal tariffs.

US Announces Widespread Reciprocal Tariffs



Source: BEA, White House. Note: China's tariff is calculated with the latest announcement and previously announced rate. Similarly, Canada and Mexico tariff rates are based on previous announcements.

According to the US Trade Representative (USTR), reciprocal tariffs are designed to balance bilateral trade deficits by calculating the necessary tariff rates to equalize trade flows between the US and its trading partners. This approach assumes that persistent trade imbalances are driven by both tariff and non-tariff barriers that impede balanced trade. Bloomberg estimates suggest that the effective US tariff rate could rise to approximately 23% in 2025, up from about 2.5% last year, because of the announced tariffs.

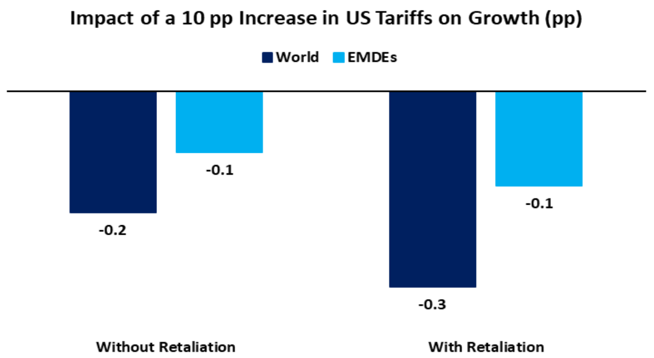
Trump's plan marks an unprecedented escalation in the global trade war, with several countries considering retaliatory measures. This raises the risk of stagflation in the near term for the US economy and a potential sharp slowdown in global economic activity, which could influence central bank policy responses. Additionally, heightened risk aversion is expected to persist in near-term, leading to increased markets and currencies volatility.

Potential Implications for India are Likely to be Moderate, given the Primarily Domestic Orientation of the Economy

The US has imposed a 26% reciprocal tariff on India, effective from April 9. This is much higher than the tariff differentiation of ~6.5 percentage points (as per WITS latest available data) between two countries, due to the methodology used by the US administration. Nonetheless, the reciprocal tariff imposed on India is much lower than that on several of its Asian peers, which could provide opportunities for Indian exports in the future. Moreover, India (along with Japan) enjoys a favourable relationship with the Trump Administration, which could help expedite less severe trade terms in the months ahead.

We estimate that the direct impact of the announced tariffs on India's GDP is around 22 bps of nominal GDP, excluding any indirect effects from tariffs on other countries or potential retaliatory measures. Also, this estimate is computed excluding the exempted sectors (accounting for ~18.7% of India's exports to the US). India's relatively low reliance on external trade helps mitigate the significant impact. While the US is India's second-largest trading partner—accounting for ~18.2% of India's exports (in CY2024)—India's goods exports to the US represent only ~2.1% of India's GDP.

US Tariffs to Weigh on Global Growth



Source: World Bank, January 2025 Report. Note: Impact on annual growth in 2025 relative to the baseline in the case of a 10-percentage-point increase in US tariffs, with and without global retaliation. EMDE refers to Emerging Markets and Developing Economies.

There will also be indirect impact via spillover from a likely global economic slowdown. Given the dynamic nature of the developments, it is unclear how long the announced tariffs will remain in place, which countries will be affected, or how US trading partners might respond or retaliate. Also, the situation is highly dynamic and unprecedented, global economy will be in uncharted territory. To give a sense of the possible impact on the global economy and its spillover to India, we refer to World Bank's simulations and the RBI's sensitivity estimates. According to a World Bank's simulation, a 10-percentage-point increase in US tariffs on all trading partners in 2025—without retaliatory measures—would reduce global growth by 0.2 percentage points relative to the baseline (projected at 2.7% YoY in 2025). If proportional retaliatory tariffs are imposed, the negative effects on global growth would increase to 0.3 percentage points relative to the baseline. To estimate the impact of announced higher tariffs, we have assumed nearly doubling of World Bank's stimulated estimates, acknowledging the implications could be non-linear. Considering these global effects, the indirect impact of the global slowdown on India's economy is estimated at around 21-32 bps of nominal GDP, depending on whether retaliatory measures are not taken or are taken by other countries, respectively. Therefore, the total potential impact on India—combining both direct and indirect effects—is likely to range from 43bps to 54bps of nominal GDP.

Certain sectors in India that have higher exposure to US trade are likely to be most affected by the reciprocal tariffs, including electronics, textiles, precious stones, chemicals, and machinery. In contrast, energy-related exports and pharmaceuticals are expected to fare better due to their exemption from the new tariffs. It remains unclear whether these exemptions will stay in place or whether sectoral tariffs will be imposed in the future. The IT sector could also face pressure from the US and global slowdown.

India's Select Sectors are Relatively More Vulnerable to Tariffs Given Higher Exposure to the US

Commodities	India's Exports to US (US$ Bn)	Share of Commodity Exports to US in India's Total Exports of Commodity	Share of Each Commodity in India's Total Exports to the US
All commodities	**80.8**	**18.2%**	**100.0%**
Non-POL	**76.4**	**20.6%**	**94.6%**
A. Agricultural & allied products	**5.4**	**10.7%**	**6.7%**
B. Ores & minerals	**0.1**	**1.5%**	**0.1%**
C. Manufactured goods (Out of which):	**70.1**	**22.7%**	**86.7%**
a. Leather & leather manufactures	1.0	21.5%	1.2%
b. Chemicals & related products :	14.0	22.4%	17.3%
(of which) Drugs, pharmaceuticals & fine chemicals	9.6	32.8%	11.8%
c. Engineering goods (Out of which):	17.2	15.5%	21.3%
(of which) Iron and steel	0.5	4.8%	0.6%
(of which) Ferrous and non-ferrous metals	4.4	19.6%	5.5%
d. Electronic goods (Out of which)	11.8	32.2%	14.7%
(of which) Motor vehicle/cars	0.0	0.3%	0.0%
(of which) Auto components/parts	1.9	23.0%	2.3%
e. Textiles (excluding readymade garments)	5.0	26.1%	6.2%
f. Readymade garments	5.2	33.0%	6.4%
g. Other manufactured goods	15.8	26.9%	19.6%
D. Other commodities	**0.9**	**13.0%**	**1.1%**
Commodities excluded from tariff*	**15.14**	**53.4%**	**18.7%**

Source: CMIE. Based on CY2024 numbers. Note: * include Petroleum, Pharma, Copper, Gold, Silver bullion, Semiconductors, Lumber articles, etc.

Ongoing India-US Negotiations Keep Possibility of Potential for a Trade Deal Alive

India is actively negotiating with the US to finalize a Bilateral Trade Agreement, which is expected to be concluded by Fall 2025. Media reports suggest that India is open to reducing tariffs on over half of US imports worth $23 billion as part of the first phase of the deal. Notably, a significant portion of India's imports (by value) from the US are subject to low or no tariffs—83% faced tariffs between 0% and 10%, and 3% were duty-free. Around 10% of imports were subject to tariffs ranging from 10% to 20%, while only about 3.7% faced tariffs exceeding 20%. This suggests that most of India's imports from the US face relatively low duties, with only a small share subject to higher tariffs. This increases the likelihood of striking a deal with the US in the coming months, which could lead to a reduction or lifting of the reciprocal tariffs imposed on India, limiting the long-term trade impact.

Moreover, the higher tariffs imposed on Asian peers such as Vietnam (46%), Taiwan (32%), China (34%+20%, announced previously), and Bangladesh (37%), could present opportunities for certain India's exports, such as textiles and electronics, as the tariff differential may work in India's favour. However, it remains to be seen how these countries respond to new tariffs and how soon they could reach a deal with the US.

Implications for the Policy Outlook: RBI to Cut Repo Rate in April Meeting

We anticipate that the RBI will reduce the policy repo rate by 25 basis points in its April meeting, as economic growth concerns are likely to outweigh inflation risks. Inflation has fallen below 4% (3.6% in February) and is likely to remain contained in the near future. The RBI is also expected to continue supporting systemic liquidity conditions to facilitate the transmission of policy rate cuts.

The US tariffs will weigh on India's economic growth both directly and indirectly, particularly through the channel of slower global growth. The impact on India's inflation will depend on several factors, including retaliatory tariffs on US imports, pass-through effects from any sustained rupee depreciation to CPI inflation, and potentially lower commodity prices resulting from a global economic slowdown. We believe that economic growth concerns will likely outweigh inflation risks, given the dominance of food items in India's CPI inflation basket and the expected limited pass-through from the exchange rate depreciation amidst sluggish demand conditions. Barring any sustained currency pressures, global growth slowdown and likely lower commodity prices should provide room for RBI to support economic growth. Moreover, India's retaliatory measures are likely to be selective rather than broad-based, implying less probability of tariff-induced inflationary pressures.

Market Reaction (3rd April): The Nifty 50 Index fell by 0.35%, a relatively modest decline compared to other Asian markets, reflecting the relatively lower tariffs imposed on India and the exemption for pharmaceutical exports. The rupee appreciated by 0.08% to 85.44 against the US dollar. The benchmark 10-year G-Sec yield remained steady at around 6.50%.

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