

Tariffs in limbo: courts, deals, and the road ahead

Bottom line: The situation with tariffs is rapidly evolving and the headlines have caused significant moves in financial markets. From being unilateral initially, tariffs have moved to become tit-for-tat between trading partners. The trade war has also quickly become a legal battle for the US administration. Pause in tariffs, to touting of initial deals, and now the court ruling to eliminate levies in 10 days, to an appeals court staying the order in favour of the administration have all left markets confused. What's next?

- ▶ **We think we are not out of tariff woods yet.**
- ▶ **Legal headwinds add to the uncertainty.**
- ▶ **While it is difficult to game out the end state, we still ...**
- ▶ **... see average effective tariff rate in the 15%-20% range.**

Court battles on tariffs...

- ▷ On May 28, the US Court of International Trade (USCIT) ruled that tariffs imposed under the International Emergency Economic Powers Act (IEEPA) exceeded its authority. The three-judge panel unanimously ordered the administration to remove the tariffs within 10 days.
 - Most tariffs on Liberation Day (April 2), including the 10% universal, country-specific reciprocal, and fentanyl-based tariffs on Canada, China, and Mexico, fall under the court ruling.
 - The unaffected tariffs include Section 301 tariffs on China from Trump's first term, extended by Biden, and Section 232 global tariffs on aluminium, autos, auto parts, and steel.
 - Considering existing exemptions and the recent reduction of China tariffs, implementing this ruling would lower the average effective tariff from about c14% to 5-6%, and China tariff rates from around 40% to 10-11%.
- ▷ However, upon appealing, the United States Court of Appeals for Federal Circuit in Washington said it was pausing the lower court's ruling to consider the Government's appeal and ordered the plaintiffs in the cases to respond by June 5 and the administration by June 9.

...add to uncertainty...

- ▷ The numerous incomplete bilateral trade deals, Section 232 investigations, and the upcoming USMCA review already made the future of tariffs uncertain. The court order has further complicated matters, potentially delaying these ongoing trade deals. Add to this the recent exchange between US and China about breaching the agreements, and Trump's recent proposals to double the steel and aluminum tariffs, things are far from clear.
- ▷ Here it is worth noting that despite any legal headwinds to the implementation of tariffs, Trump administration can still pursue the agenda under various provisions other than IEEPA. The involvement of the Supreme court adds significance to this matter but also delays the steady state. Here, we list a few options acknowledging that it is difficult to determine which of them the administration would use:
 - Section 301 permits tariffs if a trading partner gains an "unfair advantage." However, it requires a lengthy investigation to identify and measure this advantage for specific items. Tariff rates must match the quantified harm and be periodically reviewed. During Trade War 1.0, the investigation on China lasted over six months.
 - Section 232 protects US industries by imposing tariffs when imports threaten national security. Currently, it includes 25% tariffs on steel, aluminum, and autos, with ongoing investigations on pharmaceuticals, semiconductors, copper, and lumber. These global tariffs require thorough investigation and justification, though specific countries may receive exemptions.
 - Section 122 allows the president to impose tariffs up to 15% for 150 days on all countries to address balance of payments issues or prevent dollar depreciation. Congressional approval is required after 150 days.
 - Section 201 tariffs protect domestic industries from injury due to increased imports, without needing a national security justification. Each industry must undergo investigations to identify

Kishore Muktinutalapati

Head - Investment Strategy

Tel: +971 (0)2 812 6457

kishore.muktinutalapati@adcb.com

Prerana Seth, CFA

Fixed Income Strategist

Tel: +971 (0)2 812 6449

prerana.seth@adcb.com

Mohammed Al Hemeiri

Senior Analyst

Tel: +971 (0)2 812 6450

mohammed.alhemeiri@adcb.com

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specific items and justify harm before imposing tariffs, which last four to eight years. In 2018, such tariffs were placed on solar cells to support US manufacturers and extended by the Biden administration until 2026.

- Section 338 allows tariffs if a trading partner discriminates against US commercial interests by imposing unreasonable taxes, tariffs, regulations, or restrictions on US products. These actions must be targeted and not be universally applied. The tariff ceiling is 50%, with no time limit, and an investigation is required to justify the tariff.

...but we think path for tariff rates is still higher; we estimate effective tariff in 15%-20% range.

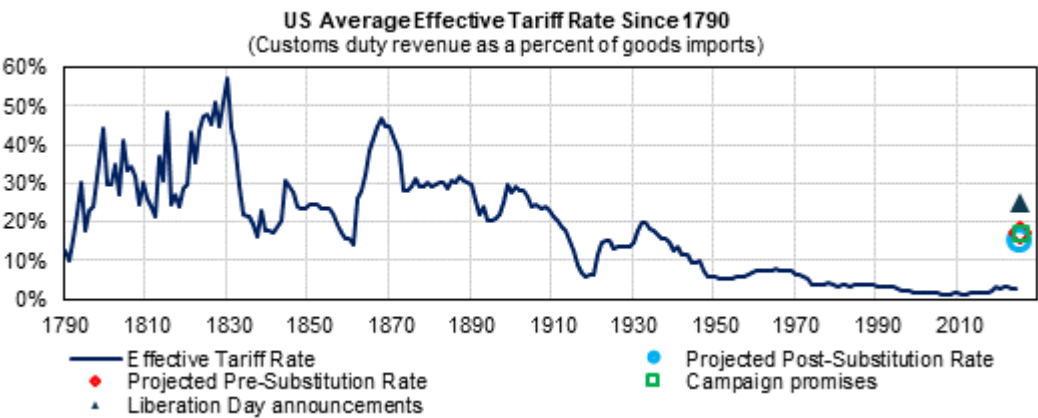
In our view, tariffs are key portion of the Trump 2.0, and the administration will use one of the available options outside the IEEPA to pursue their agenda should courts rule against the current procedure. While the other options are more time consuming, they also allow President Trump to be more hawkish. We had previously estimated that the effective tariff rate will be around 15%-20% in its steady state ([Deal or No Deal: Navigating the US-China Trade Maze, May 13 2025](#)) and that we continue to monitor tariff developments using our five-category framework discussed in our note [From a jump to a stump: Trump's tariff announcements, April 10 2025](#). We still see the path for the average effective tariff rate to be in the 15%-20% range in its steady state. Exhibit 1 shows our "dirty" calculation methodology accounting for substitution effects (using the methodology adopted by The Budget Lab at Yale) and exhibit 2 puts the current tariff rates in the context of long-term history.

Exhibit 1: A brief calculation detailing our assumptions and the average effective tariff rate

	Import Share			Average Effective Tariff	
	Effective Tariff	Pre-Substitution	Post-Substitution	Pre-Substitution	Post-Substitution
China	40%	14%	6%	6	2
Canada	20%	13%	15%	3	3
Mexico	15%	15%	17%	2	3
Rest of World	12%	58%	62%	7	7
Total		100%	100%	17	15

Source: The Budget Lab at Yale, and ADCB Asset Management

Exhibit 2: We expect the average tariff rate to rise to 15%-20%



Source: The Budget Lab at Yale, and ADCB Asset Management

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