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US Tariff Policy Harms America's Auto Industry

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One would not think that physics and international trade intersect but they do. Newton's Third Law of Motion is a prime example when applied to the automotive provisions of the USMCA (United States-Mexico-Canada Agreement), one of the largest free trade areas in the world.

Sir Isaac posits that for every action (in this case trade liberalization) there is an equal and opposite reaction (negative economic impacts).

U.S.-Mexico trade negotiations are confronting new challenges as disagreements, all surrounding tariffs on cars, steel and aluminum are impeding initiatives to reach an agreement ahead of the review of the United States-Mexico-Canada Agreement.

According to an October 16 *Wall Street Journal* report, there has been a slowdown in negotiations, courtesy of opposition from U.S. Commerce Secretary Howard Lutnick to significantly reducing tariffs on Mexican vehicles and metals.

The two countries had reportedly been moving toward an agreement that would ease certain U.S. tariffs in exchange for concessions from Mexico. However, disagreements over the proposed reductions have slowed considerably.

Assessing the USMCA benefits for the U.S. auto sector, the positive features of the $280 billion North American auto industry are substantial. The main benefit is preferential market access. Another benefit is regional sourcing incentives whereby the principal regional value-content requirement (75%) encourages purchases from North American suppliers. Still another USMCA asset is support for higher wage production. Labor-value-content requirements of 50-45% tied to an average wage of at least $16 an hour for qualifying activities, encourages USMCA partner production and research. Finally, regional materials demand is another benefit. Most notably at least 70% of a producer's steel and aluminum purchases by value must originate in North America.

Be that as it may, current tariffs harm U.S. automakers in several important ways. First, it taxes their own Mexican production. An American brand receives no exemption simply because its headquarters are in the United States. The U.S. importer pays the duty and must absorb it, negotiate cost reductions, or pass some of it to buyers. To illustrate, note a $40,000 vehicle assembled in Michigan containing $8,000 of Mexican components. A tariff on those components raises the manufacturer's input cost even though final assembly occurs in the U.S. and employs America workers.

Second, the tariffs compress margins or force auto companies to raise prices. Absorbing the tariff reduces earnings, and passing it through raises purchase prices or lease payments potentially reducing sales. Lower-priced models have less room to absorb several thousand dollars of additional cost. In short, it can raise the cost of U.S. assembly. (One should note, too, that American factories using nonqualifying covered Mexican parts face additional costs).

If tariffs reduce Mexican vehicle production, American companies supplying those factories can lose orders. The $35.8 billion in U.S. parts exports to Mexico shows why a tariff aimed at Mexican assembly can also affect American manufacturing It forces expensive production changes. Moving a model requires tooling, supplier capacity, plant preparation, and validation. Automakers can increase U.S. production over time, but the tariff bill arrives before that adjustment is complete.

The financial burden is already visible. GM reported approximately $3.1 billion of tariff impact in 2025. According to the Center for Automotive Research, a 25% tariff on vehicles and parts imposes $107.8 billion in additional costs on U.S. automakers. Said another way, a simple 25% tariff on a $25,000 vehicle could represent as much as $6,250 in additional cost before exemptions/mitigation.

General Motors, Ford, Stellantis, Tesla, and many foreign-branded manufacturers operate within deeply integrated North American production networks. Because vehicles and components can cross borders multiple times, an unrelieved 25% tariff can create a cascading cost effect rather than a one-time, easily contained charge. U.S. parts manufacturers can lose export business when Mexican assembly plants reduce output, even when they do not import finished automobiles themselves.

Presently, US-Mexico trade relations are at a hiatus. The United States declined to extend the USMCA, the NAFTA replacement, for 16 years during the joint review in July due to growing trade deficits and a push for stricter trade terms.

This impasse leaves automakers with 4 choices: absorb the tariff and absorb a lower margin; raise the vehicle's price and risk losing sales; replace the Mexico supplier, potentially at a higher underlying cost; or invest in new U.S. capacity, requiring capital and several years of adjustment.

In a 2016 episode of the TV series *Shooter*, Bob Lee Swagger rigs an explosive round that Lon loads into his rifle, which detonates in his face when fired. That is a metaphor for U.S. trade policy towards Mexico and many of our other trading partners.

With the exception of national security, tariffs are unjustified, irrational and self-defeating impediments to global commerce. US-North American auto trade is a vivid and costly reminder.

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